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The Morning Briefing

North American Edition
Monday, March 11, 2013
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GLOBE AT A GLANCE – Andrew Wroblewski, London/Pierre Ellis, New York

Equities: Asia Mixed, Europe Down. Asian markets saw mixed readings, but with clear gains in Japan helped by the weaker yen and ignoring the array of mixed Chinese economic updates. European stock prices, however, fell clearly, as profit-taking was evident in the morning session.

Bonds: Japan Lower, Europe Mixed. JGB prices were lower across the whole yield curve, save for the very short-end. In contrast, most Eurozone bond prices were largely higher, at least for high quality markets, with some peripheral markets instead seeing pockets of selling after the Italian debt downgrade.

Currencies: Little Changed. There was little clear movement in the FX markets at the beginning of the week. The yen sidelined today, moving around just above the ¥/$ 96.00 mark against the dollar. Meanwhile, the dollar was little-changed against the euro, moving around the $/€ 1.300 mark.

Germany: Exports Recover. The January (unadjusted) trade surplus widened to € 13.7 bln from € 13.2 bln in the same month of last year.

France: Even More Volatility in Production. Surprising to the downside this time around, manufacturing output sank 1.4% in M/M terms in January.

Japan: Orders Correct Back Sharply. Surprising to the downside for the first time in four months, core machinery orders (excluding shipping and utilities) dropped afresh in January and clearly so.

China: Inflation Bounces. Coming in above most expectations, consumer price inflation rose by 1.2 percentage points to 3.2% Y/Y in February.

China: Output Growth Slower, but Investment Growth Picks Up. Coming in below expectations, data for January-February showed industrial production growth slowing to 9.9% Y/Y.

China: Lending Growth Slows. Surprising to the downside, data for February showed new yuan loans falling to 620.0 bln from 710.7 bln in the same period of 2012.

U.S. ECONOMIC AND CREDIT MARKET OUTLOOK – Pierre Ellis, New York

Long Treasuries were hit again Friday, with the ten-year yield rising five basis points, to 2.04%, while the two-year yield held steady, at 0.25%. Prices were very modestly lower overnight, but dropped on the release of much-stronger-than-expected February **employment data** and seesawed back up only about halfway by the close. Dip buying was reported, but caution prevailed ahead of the round of coupon auctions next week.

February **payroll employment** jumped a more-than-expected 236,000 (Consensus: +160,000; Decision Economics: +180,000) from a January level which revisions to increases in January (+119,000, from +157,000) and December (+219,000, from +196,000) caused to be revised lower by 15,000.

Even allowing for the possibility that February was a catch-up for the newly softer January result, by averaging the two increases, the latest two months came in at 178,000 each--faster than the original +157,000 January number, and faster than the consensus February forecast.

February private-sector employment, meanwhile, rose a relatively massive 246,000, from a January level which revisions lowered only by a net 4,000.

In another important indication of strengthening labor demand, the **average workweek** unexpectedly lengthened by 0.1 hour (Consensus and Decision Economics: unched), from an unrevised 34.4 hours in January. Despite the big employment increase, workweeks were still stretched.

Employment gains were broad based—though the reviving construction and manufacturing sectors are showing a notable firming in average monthly increases lately. February also saw a very big pickup in professional and business services employment (+73,000)—fitting almost too perfectly the expected cautious-first-steps-in-expansion model of using outside services to start.

Implied income gains are very firm, but not explosive, with average hourly earnings rising an in-line 0.2%. Combined with the employment and workweek increases, that should put wage and salary income up about 0.6%--apart from whatever paybacks may still occur for the tax-avoiding pulling forward of bonuses in December last year.

Household-survey results were strong too, with the **unemployment rate** unexpectedly dropping 0.2 point (Consensus: Unch; Decision Economics: -0.1 point), to 7.7%, on a relatively strong combination of a 170,000 rise in employment and a 130,000 drop in the labor force. That, of course, would represent progress from the Fed's perspective--but the reaction will be cautious, given the recent volatility in the numbers.

The Fed, having been burned by early-year false dawns a number of times now, will not leap to conclusions about all this. But, any pressure for a stepped-up rate of easing is quashed, at least for a while.

It would make sense for the economy to be reassembling itself now—political uncertainty has been resolved to a certain extent, excesses have been purged, natural healing has taken place, and monetary policy has been extremely accommodative for a very long time.

A risk which the Fed will not be ignoring is that strengthening activity will kick bank lending into overdrive, given the huge volume of excess reserves—accelerating bank balance sheet and money supply growth. But that process would take months to become fully evident.

DAILY CALENDAR

There are no important economic indicators or events formally scheduled today.

CANADA – Thomas Lee, New York

(Friday) Housing starts maintain sub-200,000 level. Housing starts jumped in February to a seasonally adjusted annual rate of 180,700 in February from 159,000 in January (Consensus: +175,000; Decision Economics: +170,000). Thus marks three consecutive months in which housing starts have been below the 200,000 threshold which is a positive sign for policymakers as they attempt to mitigate the overheating housing market. On a trend basis, as calculated by the Canada Mortgage and Housing Corporation, February's result brings the six-month moving average (SAAR) to 195,000. Urban area housing starts advanced 18.4% from the month prior driven by an increase in its multi-family sub category which advanced 27.7%. The two readings mark their first positive advancement since August 2012. Lastly, single family starts nudged upward 6.1% while rural starts decreased 14.9%.

(Friday) Manufacturing employment "lone industry to post a notable decline" Employment results in February surprised to the upside with a 50,700 gain from a 21,900 loss in the previous month (Consensus: +8,000; Decision Economics: unch). The gain in employment was led by the service producing sector, which has been recent trend, as service employment edged higher 59,000. Goods producing sector, on the other hand, declined 8,600 with the manufacturing sector losing 25,600 jobs from the month prior. Gains were seen in both full (+33,600) and part (+17,200) time jobs. The unemployment rate, despite the employment gains, remained at 7.0% as more people participated in the labor force. Regionally, gains were seen in Ontario and British Columbia while Manitoba saw a decline. *While the job report on the whole is fairly positive, the lack of encouraging readings from the manufacturing sector does raise some eyebrows. Nonetheless, Canada's employment environment seems to be in healthy form.*

(Friday) Q4 labor productivity increases after two quarters of consecutive decline. Labor productivity edged higher 0.1% in Q4 2012 (Consensus: unch; Decision Economics: +0.3%). Business output and hours worked remained at almost the same level as the previous quarter. Labor costs per unit of output in the business sector rose 0.6%, a slower pace than in the three previous quarters.

WESTERN EUROPE – Andrew Wroblewski, London

EUROZONE

GERMANY – Exports Recover. The January (unadjusted) trade surplus widened to € 13.7 bln from € 13.2 bln in the same month of last year, and was up even more clearly from the € 12.1 bln December reading. In seasonally adjusted terms, however, the trade surplus was down at € 15.7 bln in January, as more marked rise in exports (of 1.4% M/M) came alongside a sharp bounce-back in imports (of 3.3%).

The cumulative trade surplus for last year stood at € 166.9 bln, 13.4% up on 2011.

FRANCE – Even More Volatility in Production. Surprising to the downside this time around, manufacturing output sank 1.4% in M/M terms in January, albeit only after an upwardly revised 1.3% gain in the previous month, all part of comprehensive revisions that have only served to accentuate what was already a very volatile pattern to recent data. Overall industrial production, however, also saw a clear fall back, but of 1.2% following a 0.9% rise in December.

Notably, the latest outcome left January industrial production 0.7% below the Q4 average, further hinting that official data in recent months may be belatedly echoing more long-standing business survey data.

ITALY – Continued and Deeper Recession. Q4 GDP decreased by 0.9% Q/Q, a far more marked drop than the 0.2% drop of the previous quarter, albeit unrevised from the preliminary reading. As a result, Y/Y growth was not that much more negative, dropping to -2.7%, still the softest reading since end-2009.

The break-down released for the first time with this update again showed fairly broad-based weakness, at least domestically, but with inventories by far and away the main cause.

OTHER WESTERN EUROPE

NORWAY – Softer Inflation Backdrop. Surprising few, February CPI inflation still fell by 0.3 percentage point to 1.0% Y/Y, a five-month low on the back of lower clothing and energy price inflation. On a M/M basis, prices bounced by 0.7%. Meanwhile, the core rate, CPI-ATE (excluding taxes and electricity) fell back slightly to 1.1% Y/Y from 1.2% in January.

Notably, the new data leaves inflation around the Norges Bank projections made back in October last year.

SWITZERLAND – Retail Sales Strength Less marked. Real retail sales, adjusted for working days, rose by 1.9% Y/Y in January, down clearly from the very upbeat December rise of 4.7%. A softer back-drop was also seen in the seasonally adjusted M/M data, where sales decreased 0.5%, the first fall in the last three months of data. Meanwhile, Y/Y growth in nominal working-day adjusted sales slowed as well, but to 0.6%, albeit leaving the implied sales deflator slightly less negative at -1.6% Y/Y.

CENTRAL EUROPE, RUSSIA AND TURKEY – Chang Liu, London

CZECH REPUBLIC – Recession Continues. Final seasonally adjusted real GDP data for Q4 showed the economy contracting by 1.7% Y/Y, unrevised from the preliminary estimate and still a steeper decline than the 1.5% fall seen in the previous quarter; now the largest drop since 2009. In Q/Q terms, however, GDP fell an unrevised 0.2%, a less steep decline than the 0.4% drop seen in Q3 but still extending the recession to a fourth quarter, now the longest recession in 15 years.

The expenditure side breakdown actually revealed the latest outcome to be a reflection of a steeper fall in household consumption (-4.1% Y/Y from -3.9%) and capital expenditures (-5.0% from -

3.0%), but being contrasted by a bounce in government spending to 0.8% from -0.4% in Q3. Elsewhere, and on a more upbeat note, net trade also provided a boost to growth in the quarter, with the rise in exports (1.4%) outpacing that in imports (1.2%).

Inflation Falls Further. Undershooting expectations once again, consumer price inflation fell by 0.2 percentage point to 1.7% Y/Y in February, a fourth straight decline and now a fresh cycle-low. On a M/M basis, meanwhile, prices actually rose by 0.1%. The Y/Y breakdown showed the latest outcome to be a reflection of falls in price pressures for food (5.0% from 5.7%), alcohol & tobacco (3.6% from 3.9%) and health (3.3% from 3.4%).

Notably, these latest figures came in below the Czech National Bank's inflation forecast (made in February and by 0.3 percentage point).

HUNGARY – Less Steep Fall in Exports. Trade data for January showed exports falling by 2.4% Y/Y, a much less steep fall than the 14.3% slump in the previous month. Imports, meanwhile, also turned much less negative, but to -0.8% Y/Y following a 13.0% drop in December. As a result, the January trade surplus narrowed to HUF 97.2 bln from HUF 109.3 bln in the same month of 2012.

JAPAN – Andrew Wroblewski, London

Orders Correct back Sharply. Surprising to the downside for the first time in four months, core machinery orders (excluding shipping and utilities) dropped afresh in January and clearly so, with the 13.1% M/M slump also enigma the first fall in four months

This latest result suggests fresh M/M volatility is returning. Even so, the Government maintained its assessment, still saying orders are showing modest pick, albeit acknowledging the January fall.

Stronger Monetary Data. Coming in higher than expected yet again, February M2 money supply growth picked up 0.2 percentage point to 2.9% Y/Y, albeit still the highest since last March. Moreover, growth in the broader M3 measure picked up to 2.4% Y/Y from 2.3%.

ASIA – Chang Liu, London

CHINA – Inflation Bounces. Coming in above most expectations, consumer price inflation rose by 1.2 percentage points to 3.2% Y/Y in February, more than reversing the 0.5 point fall seen in the previous month and a 10-month high. In M/M terms, prices rose by 1.1%. The Y/Y breakdown, meanwhile, showed clear rises in price pressures for food (6.0% from 2.9%) and recreation (2.0% from 0.5%), but being tempered by a fall in clothing inflation (2.1% from 2.5%). As a result, non-food inflation saw a much less marked increase to 1.9% Y/Y from 1.6% in January, albeit still to a new cycle-high.

Elsewhere, producer price deflation was stable at -1.6% in Y/Y terms from January, still a twelfth straight negative reading and coming on the back of stable deflation in producer goods prices alongside unchanged price pressures for consumer goods.

Notably, data for the first two months of the year were likely distorted by the timing of the Chinese New Year holidays (which fell in January last year but are in February this year). As a result, comparing the average of the January and February data to the same period in 2012 shows inflation actually falling clearly to 2.6% from 3.9%.

Output Growth Slower, but Investment Growth Picks Up. Coming in below expectations, data for January-February showed industrial production growth slowing to 9.9% Y/Y from 10.3% in December, ending a run of four straight increases. The latest outcome was a reflection of moderation across most components, led by utilities (4.7% from 6.5%) and electrical equipment (9.8% from 10.7%), but being tempered by a clear improvement in automobiles (11.2% from 6.6%).

Fixed-asset investment growth, meanwhile, actually rose to 21.2% Y/Y in January-February from 20.6% in the previous month, a new cycle-high. The breakdown showed the latest outcome to be a reflection of faster investment growth for the primary (37.4% from 32.2%) and tertiary (25.0% from 20.6%) sectors, but being undermined by a fall in secondary industry growth (15.6% from 20.2%). Elsewhere, and notably, railway transportation investment rose 5.2% over the past two months, accentuating the 2.4% gain seen in December and in even clearer contrast to the mid-40% slumps seen through much of last year, also being only the third rise following a run of fifteen consecutive negative readings.

It is notable that the clear improvement seen in railway transportation investment is likely to be a sign of clear fiscal stimulus measures undertaken by the Government in recent months.

Lending Growth Slows. Surprising to the downside, data for February showed new yuan loans falling to 620.0 bln from 710.7 bln in the same period of 2012. Yuan loans growth, meanwhile, fell by 0.4 percentage point to 15.0% Y/Y, exactly reversing the gain in January and back to a joint cycle-low. Total lending was 69.28 trn yuan in February, up from the 68.55 trn outcome in the preceding month, while yuan deposits growth fell to 14.6% Y/Y from 16.0% in January.

Elsewhere, money supply growth fell for the broader measures of M2 (15.2% from 15.9%) and M1 (9.5% from 15.3%), but with M0 growth surging to 17.2% in February from, 4.4%.

Once again, these figures will have been affected by base effects relating to the timing of the Chinese New Year holidays.

Retail Sales Growth Falls. Retail sales data for January-February showed sales growth falling to 12.3% Y/Y from 15.2% in December, ending a run of five successive increases and now the lowest for the January-February period since 2004. The latest outcome reflected slower sales across most components, led by food (12.1% from 18.3%), automobiles (6.9% from 9.0%) and petroleum (11.2% from 19.0%), but being tempered by a clear improvement in household electronics (16.7% from 9.7%).

It is important to remember that these figures are in nominal terms, thus the recent pick up in inflation implies that real retail sales growth may have seen an even more marked moderation.

MALAYSIA – Output Growth Picks Up. Surprising to the downside again, January industrial production growth still rose to 4.6% Y/Y from 3.5% in the previous month. The breakdown showed the latest outcome to be the result of faster growth across all three sectors of manufacturing (4.9% from 4.3%), mining (2.4% from 0.9%) and electricity (9.8% from 5.6%).

Exports Bounce. Coming in above expectations, exports rose by 3.5% Y/Y in January following a 5.8% slump in the previous month. Imports, meanwhile, surged 16.0% Y/Y following a 6.5% drop in December. As a result, the trade surplus narrowed clearly to 3.27 bln ringgit from a gap of 8.75 bln ringgit in the same month of 2012.