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The Morning Briefing

North American Edition
Friday, August 17, 2012
6:30 am (EDT), 11:30 am (BST)
Allen Sinai, Chief Global Economist

GLOBE AT A GLANCE – Chang Liu, London/Pierre Ellis, New York

Equities: Europe Higher, Asia Mixed. Japanese equity markets closed higher. Other major Asian markets were mixed, however. European bourses rose through morning trade, boosted by hopes that policymakers will take steps to contain the region's debt problems.

Bonds: Europe Mixed, Japan Lower. JGB prices fell across nearly all maturities, with the yield curve steepening on the medium to long-term end. European bond prices saw continued divergences, however, with Bunds lower, but peripheral markets mostly higher, led by Spain.

Currencies: Weaker Yen. The dollar rose slightly against the yen through both the Asian and morning European sessions, trading higher to near ¥/$ 79.47. Against the euro, the US currency seesawed through both sessions, moving marginally lower to around $/€ 1.237.

Eurozone: Exports Pick Up. Seasonally adjusted trade data showed a larger and higher-than-expected surplus of € 10.5 bln in June.

Taiwan: Mixed Messages in GDP Confirmed. Updated national accounts data still showed GDP contracting in Q2, but with the fall revised slightly downwards to -0.18% Y/Y.

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

Treasuries fell a bit further Thursday, with the two-year yield rising a basis point, to 0.29%, and the ten-year yield up two, to 1.84%. Prices opened little changed, after recovering from some overnight weakness, and firmed in early trading, only to fall back after mid-morning and spend the afternoon in the mildly negative territory where they closed. Data of the day were mixed, and probably neutral on net, and there were no clear market themes noted.

On the data front, July **housing starts** were at the mildly soft end of expectations, falling 1.1% (Consensus: -0.4%; Decision Economics: -1.3%) from a prior-month level revised down by 0.8%. But, the numbers were highly disappointing on the single-family side, with that total dropping 6.5%, after a 4.7% gain last month.

The suggestion is that builders are considerably less optimistic in their hard decisions than they seem to be in the NAHB sales-activity surveys—particularly in July, when the headline NAHB index jumped 6 points. Of course, some volatility is the norm in starts—but there is clearly still serious shakiness in conviction about the outlook being demonstrated here.

The issue is the extent to which that ground-level indication represents the state of general business willingness-to-commit. There has been little sign of any strength of that type anywhere else lately—so the data yesterday reinforced the picture of semi-paralysis already in place.

Builder confidence may grow in coming weeks—with the August NAHB showing a further gain—but, then, mortgage rates may be rising too.

The starts disappointment does not rise to the level that would restart momentum for a quick QE3—the economy is not pushed closer to the brink of the abyss—but FOMC doves have never stopped arguing for more MBS-driven action, and will do so a bit more loudly now.

Weekly **initial claims**, meanwhile, rose an in line 2,000 (Consensus: +3,000; Decision Economics: -1,000) from a prior-week level revised up by 3,000. The new number covered the fourth of five weeks in payroll August, and, at 366,000, put the month-to-date average figure at 364,000—down 12,000 from the payroll-July average.

That month-to-month decline in layoffs is clear enough to allow August payroll employment growth to firm up a bit—assuming that outright new hiring did not slow down by more than layoffs.

As it happens, however, outright new hiring seemed to be a bit on the strong side in July—the payroll gain was big in relation to the decline in layoffs—and there is some question whether enthusiasm to hire might have settled back a bit this month. Notably, the motion in continuing claims is adverse in August so far.

Odds are, payroll estimates keying off these numbers will stick close to the July result, for now.

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Lastly yesterday, the headline August **Philadelphia Fed index** met expectations, improving to -7.1, from -12.9 in July (Consensus: -5.0; Decision Economics: -8.6). Details of the report paint a picture of steady-state decline—but, unlike the Empire State Survey numbers, do not show new deterioration.

Notably, the new orders index showed easing decline, rising to -5.5 from -6.9, while the employment index was virtually steady, at -8.6 versus -8.4, and the workweek index nudged less-worseward, at -14.6 versus -17.3. Obviously, these are still sickly numbers, but a bit less so than in July, and much less so than in June, when the orders index was at -18.8.

The national picture probably remains of stagnant manufacturing activity—pressured by export weakness and lack of domestic demand-side confidence. But, that is different from a picture of worsening decline, and incipient recession.

The latter scenario would probably be necessary to motivate the FOMC consensus to take the big step of a new QE3 right now. But doves, harping on the issue of missed employment goals, may win the debate down the line.

DAILY CALENDAR

Of the reports today, the University of Michigan Consumer Sentiment index has the far greater potential to surprise, and to cause a market reaction should it do so. Almost any new information on consumer behavior is apt to be seized upon nowadays, since consumer spending growth is absolutely critical in the economic outlook, and the sentiment surveys, for better or for worse, are prone to occasional sharp volatility.

The headline **Consumer Sentiment Index** is seen changing very little (Consensus: -0.3 point, to 72.0; Decision Economics: +0.7 point), an outcome that would represent the second month of rough stability, following on a relatively sharp (6.1-point) decline in June.

While the fact of sentiment stabilization in itself would be noteworthy, and reassuring in suggesting that no new shock to spending is looming, the market reaction would probably be minimal. A notably stronger-than-expected result, on the other hand, would add to the very solid July retail sales results in hinting that very easy Fed policy is finally promoting stronger demand-side growth—a signal that markets would respond to.

Of course, a much weaker-than-expected result would push in the other direction, suggesting that the retail sales result was a fluke, and unsustainable.

The **leading indicators**, meanwhile, are watched more on a developing-trend basis, do not tend to surprise very significantly, and today are expected to show mild movement (Consensus: +0.2%; Decision Economics: +0.3%) in line with the mildly choppy sideways-motion pattern of recent months.

The Schedule:

The preliminary August reading of the University of Michigan Consumer Sentiment Survey, at 9:55 EDT/13:55 GMT, and the July leading indicators, at 10:00 EDT/14:00 GMT.

DE Forecasts:

University of Michigan Consumer Sentiment Index (August): +0.7-point, to 73.0.

Leading Indicators (July): +0.3%.

CANADA – Melissa Pumphrey, New York

(Thursday) Shipments and inventories slide on oil. Canadian manufacturing shipments declined 0.4% m/m (Consensus: +0.3%; Decision Economics: +0.6%) in June to C$48.9 billion from a May total which was revised upwards by four tenths. Petroleum and coal products posted a -10.6% m/m drop as crude oil prices eased over the month. Ex-petroleum and coal products, shipments advanced 1.1% m/m mainly on transportation equipment (+1.7% m/m), machinery (+5.2% m/m), and food (+0.8% m/m). Inventories slipped by 1.7% m/m (Decision Economics: -0.8%) to C$64.8 billion as crude oil stockpiles shrank. Oil refineries had increased petroleum stockpiles in May on temporary shutdowns. The inventory-to-sales ratio declined two hundredths to 1.32. New orders gained 1.7% (Decision Economics: -0.4%).

WESTERN EUROPE – Chang Liu, London

EUROZONE – Exports Pick Up. Seasonally adjusted trade data showed a larger and higher-than-expected surplus of € 10.5 bln in June, up from the May upwardly revised € 6.8 bln outcome as a 2.4% M/M rise in exports came alongside a flat backdrop in imports.

The (unadjusted) June trade balance, meanwhile, showed a surplus of € 14.9 bln, a clear improvement from the modest € 0.2 bln surplus seen in the same month of2011. This was a reflection of a 12% increase in exports and a 2% rise in imports.

GERMANY – Pipeline Prices Fall Further. Undershooting expectations, July producer prices were flat in M/M terms following two successive falls including the 0.4% drop in the previous month. The latest fall came in spite of an increase in energy prices, with the ex-energy gauge actually seeing a fall of 0.2% in the month. The overall Y/Y rate, meanwhile, dropped 0.7 percentage point to 0.9 %, still the lowest since May 2010.

ASIA – Chang Liu, London

SINGAPORE – Mixed Messages in Exports. Surprising to the upside this time around, seasonally adjusted non-oil exports still fell by 3.6% M/M in July, albeit still only partly unwinding the 6.7% jump in the previous month and extending the volatility in the series. In Y/Y terms, meanwhile, non-oil exports slowed to 5.8% in July, accentuating the 6.6% gain in June. The breakdown revealed the latest moderation to be the result of slower growth in non-electronics exports growth (7.9% Y/Y from 9.2%), while electronics growth actually picked up to 2.0% from 1.6%.

Meanwhile, total exports actually rose by 0.3% Y/Y after a 0.5% decline in June, while import growth slowed slightly to 6.0% from 6.1%.

TAIWAN – Mixed Messages in GDP Confirmed. Updated national accounts data still showed GDP contracting in Q2, but with the fall revised slightly downwards to -0.18% Y/Y from an initial estimate of -0.16%. This revision still left a swing into contraction territory from the Q1 gain of 0.40%, the first decline since 2009. On a seasonally adjusted Q/Q basis, however, GDP actually saw a 0.85% gain (revised up from a 0.78% rise), accentuating the 0.38% rise in the previous quarter and now a five-quarter high.

The expenditure breakdown (all purely in Y/Y terms) showed slower growth in both private consumption (0.76% from 1.44%) and government spending (2.41% from 2.74%). Capex growth, however, actually turned less negative at -5.24% from the 10.24% slump in Q1. Elsewhere, and on a more upbeat note, net trade provided a slight boost to growth, with the drop in exports (2.00%) being outpaced by that in imports (3.70%).

On the output side, the data showed the mixed messages in the secondary sector as improvements in manufacturing were undermined by deterioration in utilities and construction, while the tertiary sector saw a moderate improvement.

Notably, following today's report, the Government revised down its GDP forecast for 2012 to 1.66% from 2.08% previously, while inflation is now projected to be around 1.93% this year from 1.90% previously.