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The Morning Briefing

North American Edition
Tuesday, August 7, 2012
6:30 am (EDT), 11:30 am (BST)
Allen Sinai, Chief Global Economist

GLOBE AT A GLANCE – Andrew Wroblewski, London/Pierre Ellis, New York

Equities: Asia Mixed, Europe Little Changed. Asian markets largely saw further gains, responding to an easing in global concerns. European markets edging down in the morning session despite initial modest mark-ups.

Bonds: Largely Down. JGBs were lower, as the yield curve steepened. European bonds were also largely down, save for some of the minor peripheral markets.

Currencies: Little Changed. The yen eased back a little against the dollar mainly in the European session, moving to the ¥/$ 78.30 mark. Meanwhile, the euro moved sideways around the $/€ 1.2400 level.

Germany: Orders Drop Resumes. Coming in clearly below expectations this time around, manufacturing orders fell afresh in June, down 1.7% M/M.

Italy: Continued Recession But No Deeper? Q2 GDP decreased by 0.7% Q/Q according to preliminary data, very much as expected and accentuating the 0.8% drop of the previous quarter.

United Kingdom: Manufacturing Succumbs? Surprising to the upside, June manufacturing output still slumped 2.9% M/M, more than unwinding the bounce of 1.2% seen in the previous month.

Taiwan: Fall Further and Faster. Exports fell by 11.6% Y/Y in July, a fifth consecutive drop, also being the steepest in that sequence.

Australia: Policy Held, No Hint of Further Action? As was universally expected, the Reserve Bank of Australia decided to keep the Cash Rate unchanged at 3.50% at its meeting in August.

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

Treasuries finished little changed Monday, with the two-year yield essentially unchanged, at 0.24% and the ten-year yield up a small fraction of a basis point, to 1.57%. The market was volatile in a narrow upside range for almost the entire day, bubbling up repeatedly in overnight trading, but opening New York flat, and then running up to a noontime high, only to fall back quickly in midafternoon and finish near flat. No strong themes were noted, though the looming refunding auctions were a dampening factor. There were no important economic data releases, and early-morning comments from Chairman Bernanke cause no ripples.

DAILY CALENDAR

Like yesterday, **Chairman Bernanke's** appearance should be the main item on a day of a relatively quiet schedule. However, as was the case yesterday, the circumstances of the speech seem to limit the potential for any revelations of market interest. In what the Fed is billing as "A Teacher Town Hall Meeting," the Chairman will talk to a group of "educators of economics, personal finance, and related disciplines" in Washington, with the speech videocast simultaneously to similar gatherings at Fed offices around the country.

The focus of Bernanke's talk will be the "need for personal financial education in the wake of the recent financial crisis," a subject on which he and other Fed officials have spoken many times by now—so big surprises are unlikely. Notably, however, he will entertain questions from the audience—and some attendees might just ask considerably more sophisticated ones than many Senators and Representatives do at the Humphrey Hawkins sessions. Between the FOMC meeting, the employment report, and the GDP numbers, there is a lot of fodder for discussion.

Weekly store sales reports will cover the first of four weeks in retail August, the leading edge of the full-blown back-to-school shopping season—and there will be intense interest in the degree of willingness to spend that families are exhibiting, particularly at mid- and lower-bracket chains.

Though is very early to get a sense of the full month, first-week reports do create impressions that only very significant surprises later can fully erase. In any case, the two store survey groups settle on their full-month forecasts today—giving a numerical first-impression of the month.

Consumer credit figures will probably get relatively little attention, unless the figure is well outside the relatively high forecasts range (Consensus: +$11.0 billion; Decision Economics: +$8.5 billion). The numbers are hard to interpret, with, for instance, big increases sometimes read as indicating that consumers are spending with healthy enthusiasm and sometimes as evidence that consumers are strapped, and living off "plastic."

The Schedule:

Weekly store sales reports from ICSC/Goldman Sachs and Redbook Research, at 7:45 EDT/11:45 GMT and 8:55 EDT/12:55 GMT respectively, an appearance by Chairman Bernanke, at 12:30 EDT/16:30 GMT, and June Consumer Credit data, at 15:00 EDT/20:00 GMT.

DE Forecasts:

Consumer Installment Credit (Change in amount outstanding) (June): +$8.5 billion.

WESTERN EUROPE – Andrew Wroblewski, London

EUROZONE

GERMANY – Orders Drop Resumes. Coming in clearly below expectations this time around, manufacturing orders fell afresh in June, albeit with the 1.7% M/M drop more than unwinding the (upwardly revised) 0.7% rise seen in May. Notably, the breakdown showed this resumed drop both on the export and domestic side and dominated by a slump back in intermediate good orders.

These orders numbers continues to be prone to marked volatility, albeit with no special additional distortion this month coming from swings in bulk order items. If anything a slightly softer tone is discernible as orders fell a little in Q/Q terms through Q2. As a result, these numbers do not fully echo the much more sobering message in downbeat surveys.

ITALY – Continued Recession But No Deeper? Q2 GDP decreased by 0.7% Q/Q according to preliminary data, very much as expected and accentuating the 0.8% drop of the previous quarter but in line with the Q4 fall. As a result, Y/Y growth turned even more negative, losing 1.1 percentage points to -2.5%, the softest reading since edn-2009. No break-down was provided, although official statisticians did acknowledge that the GDP drop came mainly from softness on the industrial side, with services stable.

Industrial Production Drops Afresh. Surprising a little to the downside, June industrial production dropped afresh, with the 1.4% seasonally adjusted M/M fall more than offsetting the 1.0% May bounce. Notably that May rise remains only the second positive reading this year and certainly does not disguise a clear worsening trend in terms of output levels. Also of note, this fresh fall in June was relatively broad based, the main exception being a further recovery on the energy side. Regardless, Y/Y work-day adjusted growth turned much more negative at -8.2%.

The data very clearly still suggest a further, clear hole emerged into Q2 regarding economic activity, albeit perhaps not quite as large as that seen in the two previous quarters.

NETHERLANDS – Production Drops Even Further. Coming in a weaker than expected yet again, June industrial output dropped 0.6% M/M, twice the fall of the previous month and the third successive fall. As a result, Y/Y growth moved back to the negative and clearly so (at -2.45%).

OTHER WESTERN EUROPE

UNITED KINGDOM – Manufacturing Succumbs? Surprising to the upside, June manufacturing output still slumped 2.9% M/M, more than unwinding the little-revised bounce of 1.2% seen in the previous month, the latter being only the second rise so far this year. Y/Y growth was much more negative at -4.3%. The June slump was largely broad-based however. Indeed, despite cool and wet weather during the month, energy/utility production was clearly down afresh. As a result, overall industrial production dropped 2.5%% in M/M terms.

How Clear is the Underlying Weakness

Clearly, the swings in the overall production data of late reflect not only the impact of swings in the weather, but also (more recently) the impact of the Royal Jubilee celebration which meant that June had one fewer working day, a contrast to the backdrop seen in May data.

All of which will make the interpretation of the key manufacturing backdrop all the harder to discern, albeit it clear that a much weaker undertone is being highlighted by factory sector surveys, albeit with different sourced versions of the later pointing to different scales of downside risks.

Less Weak Q2 GDP?

Regardless, the production data are less weak than envisaged in the Q2 GDP report, enough to mean that a circa-0.1 percentage point upward revision may be in the offing. Indeed, the upward revision may be more sizeable if June construction data (due Friday) also prove to be less weak than envisaged in the national account numbers.

DE View: While a less sizeable drop in Q2 GDP than the existing 0.7% Q/Q plunge may emerge when revised data arrive on August 24, a further hole will surely still be evident. However, given the array of distortion and revisions the numbers may not affect BoE thinking duly as the Inflation Report due tomorrow may highlight. Even so, the BoE is likely to scale back its GDP projection for this year to around zero.

Sluggish Sales. According to the British Retail Consortium (BRC), like-for-like nominal Y/Y store sales growth slowed clearly in July, with the growth rate sliding 1.3 percentage point to just 0.1%. Overall (or total) sales growth slowed similarly, but to 2.0%.

As the BRC itself stresses, a three-month average better reflects underlying trends given the gamut of distortions that have dogged recent data, these now including the boost to sales last month from somewhat better weather. These continue show that sales have been largely flat of late. Even so, it is also worth noting that as the BRC sales data are in nominal terms, they imply that real sales have continued to fall clearly.

NORWAY – Manufacturing Rises Further. Manufacturing production saw a 0.8% M/M rise in June, therefore accentuating the 1.2% April and 0.6% May bounces. While the numbers still seem consistent with a volatile pattern, a better underlying tone may be emerging, something possibly evident in the much more positive Y/Y rate of 4.3%.

Regardless, there may be risks given the clear weakening in the latest manufacturing survey data.

Meanwhile, overall industrial production increased 0.6% in M/M terms in June, seeing a widely based bounce save for utilities.

SWITZERLAND – Inflation Less Negative. As widely expected, July consumer price inflation was somewhat less negative at -0.7% Y/Y, a tenth successive negative reading but 0.4 percentage point up from a June reading which had been the lowest in almost three years. In M/M terms, prices dropped 0.5% reflecting the impact of lower clothing and fuel costs. Meanwhile, core inflation measures were also less negative, with the ex-food, energy and fuel figure up 0.2 percentage point at -1.0% Y/Y while the measure that also excludes administered price products rose similarly but to -1.4%.

The headline inflation outcome in the first month of Q3 is softer than that predicted by the SNB in its June assessment.

Stable Unemployment. Very much as expected, the seasonally adjusted jobless rate was 2.9% in June, remaining unchanged for a third successive month. The unadjusted rate was unchanged but at 2.7%.

CENTRAL EUROPE, RUSSIA AND TURKEY – Andrew Wroblewski, London

HUNGARY – Output Drops Back. June seasonally adjusted preliminary industrial production dropped 2.2% M/M, partly unwinding the 3.5% bounce in the previous month and extending the volatility in the series. Meanwhile, in unadjusted Y/Y terms, output growth slowed to 0.6%.

ASIA – Andrew Wroblewski, London

TAIWAN – Exports Fall Further and Faster. Exports fell by 11.6% Y/Y in July, a fifth consecutive drop, also being the steepest in that sequence, including the 3.2% June fall. Imports, meanwhile, dropped less sharply, sliding 3.2% following a 8.4% slump in the previous month. As a result, the trade surplus more than halved to $ 0.90 bln last month from $ 3.37 bln in July 2011. Meanwhile, on a geographical basis, exports weakness became more acute in terms of sales to Europe, the USA and China.

OCEANIA – Andrew Wroblewski, London

AUSTRALIA – Policy Held, No Hint of Further Action? As was universally expected, the Reserve Bank of Australia (RBA) decided to keep the Cash Rate unchanged at 3.50% at its meeting in August. This matches the decision of last month, both these following a 25 bp and 50 bp rate cut in June and May respectively.

Little Change in Thinking

Otherwise, the statement by Governor Stevens showed no notable changes. Instead, it seems clear that the while the RBA recognizes the likely impact of the strong A$, it still wising to assess the impact of the easing in policy it has put in place since the end of last year which has brought effective interest rates to a little below their medium-term averages.

Some Signs Stimulus Has Worked?

Indeed, if anything, the statement even suggests that tentative evidence hints that a positive impact from the lowering in rates is already discernible, pointing specifically to recent strong business credit growth alongside a firming in dwelling prices. In addition, there is a slightly less pessimistic, assessment of the global economy, with the RBA no longer suggesting that growth in the key area of China is slowing any further, leaving the pace of global growth at around par. Understandably, Europe remained the key area of risk.

In terms of the domestic economy, the RBA was more even more concise this month, suggesting that most indicators point to trend-type growth. Understandably, the RBA assessment of the outlook for inflation was unchanged: it is expected to be consistent with the target over the next one to two years, albeit stressing that maintaining low inflation over the longer term will, however, require growth in domestic costs to continue their recent moderation as the effects of the earlier exchange rate appreciation wane.

DE View: Extended Policy Pause. *A clearer picture of RBA thinking will come with the quarterly Statement on Monetary Policy due this Friday, where little change is envisaged in terms of the outlook for inflation: the Q2 CPI reading released recently was very much in line with RBA thinking. However, based on the clearly solid domestic backdrop and outlook, the overall rhetoric from the RBA is of extended policy pause, unless any of clear global risks materialize meaningfully.*

NEW ZEALAND – Labor cost growth slows. According to the Quarterly Labor Cost Index, Q2 labor costs rose by 0.5% Q/Q for ordinary-time wage rates, matching the gain seen in Q1 both readings down from the final quarter of last year. Y/Y wage cost growth, meanwhile, was unchanged at 2.0% for a third straight quarter.