New York • London • Boston
DECISION ECONOMICS, INC.
Information for Decisions™
New York: 212 884 9440
London: 011 44 20 7959 3045
Boston: 617 994 0500

The Morning Briefing

Friday, May 17, 2013
06:30 EDT; 11:30 BST
Allen Sinai, Chief Global Economist

FRIDAY BRIEFING POINTS – Andrew Wroblewski, London/Pierre Ellis, New York/Francisco Larios, Miami

United States: Is Sentiment Stable? The May **University of Michigan Consumer Sentiment** report seems likely to be the item of the day, given the market hunger for any clear indication of improvement or deterioration, and the **leading indicators** will be looked at, on the off chance that a recession signal might be developing.

Canada: April **CPI** is likely to continue its persistently soft trend and expectation is that inflation will be slower than the 1% Y/Y mark it hit in March mainly due to lower gasoline prices.

Mexico: Real GDP probably slowed during the first quarter (DE: 2% Y/Y). This is fundamentally the result of two factors: slower exports of manufactured goods and the impact of diminishing worker remittances from the U.S. on consumption.

U.S. DATA AND EVENTS OUTLOOK – Pierre Ellis, New York

Scheduled today are the first look at the May University of Michigan Consumer Sentiment Survey, at 9:55 EDT/13:55 GMT, the April leading indicators, at 10:00 EDT/14:00 GMT, and a speech by Minneapolis Fed President Kocherlakota, at 13:45 EDT/17:45 GMT. On Saturday, Chairman Bernanke will be giving a commencement address, at 11:00 EDT/15:00 GMT.

The **Consumer Sentiment** report seems likely to be the item of the day, given the market hunger for any clear indication of improvement or deterioration, and even the **leading indicators** will be looked at, on the off chance that a recession signal might be developing.

Kocherlakota, though not currently voting on the FOMC, is well within the Committee dovish consensus group—so his thinking on the "tapering" issue will amount to another reading on where the center of gravity is there. **Bernanke**, of course, is always a focus of attention.

Forecasts for the headline **University of Michigan Consumer Sentiment Index** point to a partial rebound from the 2.2-point decline suffered last month (Consensus: +1.5 points; Decision Economics: +1.1 points).

That sort of result would reinforce the picture of a resilient, but still slow-growing, economy painted by the April employment and retail sales results. The March weakness in those reports is now seen not to have been the beginning of a serious slowdown, but just a bump.

At the same time, the April recoveries gave no indication of a acceleration in underlying growth—they were rebounds to the same mildly growing trend that was in place before. And, even that recovery has been made to look precarious by the soft manufacturing reports and the so-so housing and initial claims results this week.

The Consumer Sentiment index actually peaked in March, with the decline coming only in April; the May forecasts would restore it just to the February level. Of course, given market uncertainty about the outlook, a surprise sharp move in either direction could cause a reaction.

The **index of leading indicators**, meanwhile, is expected to show a modest increase (Consensus and Decision Economics: +0.2%), following on the 0.1% decline last month—the first in over six months.

Usually, forecasts are not too wide of the mark—but the recent numbers are so small that revisions, or minor forecast errors, might easily produce the traditional recession signal of two monthly declines in a row.

Of course, two small declines would give a less clear-cut signal than two bigger declines—if only because the small declines are more likely to be revised away—but, markets are sensitive to any hints of direction now.

Kocherlakota will be at the Chicago Booth Business School Annual Management Conference, participating in a panel discussion of "The Future of Financial Regulation and Monetary Policy. Appearing with him will be Sweden Riksbank Governor, and Basel Committee Chairman Stefan Ingves, and former Fed Governor Randal Krozner.

Bernanke will be speaking at the Bard College commencement, in Great Barrington, Massachusetts. The working title of the Address is "Economic Prospects for the Long Run," a not-inappropriate topic for discussion with newly educated young people, entering the workforce.

Presumably, one focus of the talk will be the long-run outlook for potential growth—where the amount and quality of human capital are usually thought to be critical factors. A more immediate, and relatively mundane, question—but one with monetary policy implications—would be where the level of potential output is at present.

DE Forecasts:

University of Michigan Index of Consumer Sentiment (May): + 1.1 points, to 77.5.

Index of Leading Economic Indicators (April): +0.2%.

WESTERN HEMISPHERE ANALYSIS

UNITED STATES – Pierre Ellis, New York

Weak real-side indications. Real economy numbers came in on the soft side yesterday, with weekly **initial claims** rising more than expected, April **housing starts** falling even harder than looked for, and the May **Philadelphia Fed Survey** showing unexpected further erosion. But, indications on the general trend of the economy are limited. Clearly there is no acceleration being shown, but the downside movements are contained within recent ranges.

Initial claims jumped a more-than-expected 32,000 (Consensus and Decision Economics: +7,000), from a prior-week level revised up by 5,000. No special factors were cited. The new level is 360,000.

But, the latest jump followed a net decline of 27,000 over the preceding three weeks, and probably reflected some seasonal maladjustment over the full period. Smoothing that out, the four-week moving average increased by just 1,000, to 339,000.

The new number covered the fourth of five weeks in payroll-May, and the month-to-date average rate of layoffs is still down a very significant 23,000 from the payroll April average.

The figure next week will tell how much more smoothing out might be necessary—but a very high number would be necessary to erase the picture of a meaningful decline in layoffs in payroll May from payroll April. Payroll forecasts will be a bit more cautious now—but will still look for some improvement from last month.

Housing starts, meanwhile, fell a big 16.5% (Consensus: -6.1%; Decision Economics: +3.8%), but the majority of the drop was in multi-family starts, which plunged 38.9%, from the very high end of the recent range to the very low end—not hugely unusual volatility for that sector.

Single family starts, meanwhile dipped 2.1%, to a level well within the six-month range.

Fed officials will leap to no conclusions on these numbers, with doves content with their steady-easing stance, and hawks seeing no reason to believe the economy is falling off its recovery track—or that inflation will not be a danger within the policy-relevant future.

The **Philadelphia Fed Survey** mirrored the disappointing Empire State Survey results, sagging on a broad front.

As always, the issue is whether the weakening in the Middle-Atlantic region reflects a national trend, or local problems--ut the upside for national-level performance is clearly a bitmore limited than before.

The headline Philadelphia Fed index dropped 6.5 points (Consensus: +0.8 point; Decision Economics: +0.2 point) to -5.2. The decline in that standalone index was more than matched by a 6.9-point drop, to -7.9, in the critical new orders index—an absolutely unwelcome indication of weakness on the demand side.

Despite a drastic reversal in shipments, with that index dropping 17.6 points to -8.5, the backlog continued to fall, with the index off 0.6 point to -9.3. And, there was no indication of confidence about the outlook in employment behavior, with that index slipping a further 1.9 points, to -8.7, after dropping 9.5 points last month.

To all appearances, Philadelphia manufacturing is in a slow-motion sinkhole, with the important indexes now all in a moderate-decline range. A quick revival is not impossible—but local players apparently have little confidence that it will happen soon.

On the inflation front, the April **Consumer Price Index** was also softer than expected, with the core, ex-food-and-energy index, rising just 0.1% (Consensus and Decision Economics: +0.2%).

That result is not striking in itself, but it does intensify the picture of trend disinflation, with the year-on-year increase slipping to 1.7%, from 1.9% in March—and from 2.3% back in April 2012.

The suggestion is that the core-PCE price index trend monitored by the Fed will slow further notch as well. That index was up just 1.1% year-on-year in March, down from +1.3% in February and from 2.0% in March 2012. Conceivably, there could be a sub-1% reading in April.

Even FOMC doves have expressed the view that the core-PCE slowdown is temporary, and not yet meriting a policy adjustment. But their patience may be tested in coming months. On the core-CPI basis, there must be increases of at least 0.2% in May and June in order to prevent further erosion in the year-on-year rate.

WESTERN EUROPE – Andrew Wroblewski, London

EUROZONE – Construction Output Fall Continues. Construction output dropped 1.7% M/M in March, very much accentuating the falls of the four previous months (a cumulative 5.0%). The additional fall came in both civil engineering and building and resulted in the Y/Y terms swinging back to the negative, at -7.9%).

DE View: *The cold weather has clearly been aggravating the adverse economic backdrop in hurting construction, the 3.0% Q/Q drop in Q1 largely accounting for the 0.2% Q/Q GDP fall in the Eurozone.*

Car Sales Far Less Weak. Car registrations fell by 1.7% Y/Y in April, a far less steep fall than the drop in the previous month. The data showed continued weakness on a geographical basis, but with the reading for Germany having turned positive. *The early Easter may have been responsible for the accentuated drop in March and then the less-weak April reading.*

Notably, seasonally adjusted numbers (computed by the ECB) showed a further M/M rise in April, actually the third in succession, albeit still not enough to offset the slump seen in January.

JAPAN – Andrew Wroblewski, London

Orders Jump Even More Sharply. Surprising to the upside once again, core machinery orders (excluding shipping and utilities) jumped even more clearly in March, with the 14.2% M/M increase very much accentuating the downwardly-revised 4.2% bounce as well as being the largest rise in a decade.

This latest result suggests M/M volatility is less evident with five increases in the last six months of data. As a result, it is surprising that the Government failed to upgrade its assessment, instead still saying orders are showing a modest pick.

ASIA PACIFIC ANALYSIS – Chang Liu, London

CHINA – Leading Index Bounces. The April Conference Board-compiled leading index rose afresh and by 1.5% in M/M terms, more than reversing the 0.6% decline in the previous month and a twenty-third increase in the past 24 months. The coincident index, meanwhile, saw a 0.2% increase in April, adding to the 0.3% gain in March and hitting a new cycle-high.

Notably, four of the six components contributed positively to the headline index in April, with real estate and credit expansion being the main drivers behind the latest bounce. However, commenting on these results, a Conference Board economist noted that while these (volatile) factors may boost growth in the short-term, overcapacity in the industrial sector remains a drag on the economy going forward.

SINGAPORE – Exports Rise Further. Surprising to the downside, seasonally adjusted non-oil exports still rose by 1.1% M/M in April, albeit slowing clearly from the 8.0% jump seen in the preceding month. In Y/Y terms, meanwhile, non-oil exports saw a less steep drop of 1.0% in April following the 4.8% drop in the previous month. The breakdown revealed the latest outcome to be the result of a less steep fall for electronics exports (-9.0% from -17.9%) coming alongside a pick up in non-electronic export growth (3.3% from 2.3%).

Meanwhile, total exports bounced 1.6% Y/Y after a 7.6% drop in March, while imports rose 2.5% following a 13.4% decline in the previous month.

Notably, data from the first few months of the year will have been distorted by the timing of the Lunar New Year holidays (which fell in January last year but were in February this year) and have been very volatile. As a result, it is notable that export growth has averaged 1.2% M/M through the first four months of the year.