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

Wednesday, February 19, 2014
6:00 EST; 11:00 GMT
Allen Sinai, Chief Global Economist

WEDNESDAY BRIEFING POINTS – Andrew Wroblewski, London/Andrew Husby, New York/Francisco Larios, Miami

Poland: Industrial production slows. Production is expected to have slowed in the first month of 2014 with DE and Consensus forecasting a deceleration to 5% Y/Y and 3.5% Y/Y from 6.6% recorded in the prior month. Industrial production growth was largely positive for 2013.

United States: FOMC Minutes. Investors will attempt to glean the underlying FOMC balance of opinion within today's Minutes to the January 28-29 meeting, while housing starts and producer prices round out the hard data, likely weather impacted on the former.

U.S. DATA AND EVENTS OUTLOOK – Andrew Husby, New York

Today brings January housing starts and producer prices at 8:30 EST/13:30 GMT, and the Minutes to the January 28-29 FOMC meeting, at 14:00 EST/19:00 GMT.

DE Forecasts:

Housing Starts (January): -4.9% to 0.950 million.

Building Permits (January): -0.6% to 0.980 million.

Producer Prices (January): +0.2%.

Likely Little New Within FOMC Minutes

Fed observers will likely see little major in terms of news within the FOMC minutes, as the January 28-29 meeting occurred before the disappointing January labor market report, and because Fed Chair Yellen provided more color during her testimony before Congress last week. That testimony suggested the "notable change" in the outlook sufficient to pause the current tapering path is likely not close to being met, even taking into account the jobs surprise. Other disappointing data flow looks increasingly weather-impacted, a fact which – along with prior inventory build – lends credibility to the view that investors should for now treat Q1 as a temporary soft patch. Unless things go very wrong, the tapering path should be viewed as tough to shake.

Still, the sizeable dovish contingent will remain vigilant on incoming data, particularly inflation figures. It will be important to watch whether concerns seem to be broadening among not only the doves, but hawks as well, the latter receptive to soft-inflation concerns. Any broadening in the scope of inflation-related language would be telling, with "many" participants already having expressed concern about the deceleration in consumer prices in the Minutes to the December meeting. Slipping further behind on the inflation component of the Fed's mandate will cause more discomfort the longer it persists.

Weather-Impacted Housing Data?

Elsewhere, January **housing starts** are set to be weather-impacted, with a greater decline in new construction (**DE and Consensus: -4.9% to 0.950 million**) than **permits** (**Consensus: -1.6% to 0.975 million; DE: -0.6%**), as intentions remain stable. Geographic results will be important here as Western states generally experienced warmer-than-expected temperatures while the North Central, Northeast, and Southeast all saw negative anomalies.

Broad-based declines would more-credibly hint at something other than weather, i.e. general or more-prolonged hesitation in building activity after the late-summer 2013 lull. Still, November and December data (2m average) showed a marked 15% jump in single-family starts after flat-to-negative results from April through October. Consolidation of those levels will boost notions of a new uptrend in 2014, but seasonal factors play a significant role in the winter months. A reason to remain positive on housing market conditions ahead is that the disappointing February NAHB housing market survey of builders was clearly weather-impacted, hitting supply chains and buyer traffic, not the outlook for fundamental demand.

WESTERN EUROPE – Andrew Wroblewski, London

EUROZONE – Construction Output Bounces Back. Construction output rose 0.8% M/M in December, ending a run of three successive drops. Notably, this recovery came on both the building side and civil engineering sides, tempering the overall Y/Y drop to -0.2%.

OTHER WESTERN EUROPE

UNITED KINGDOM – BoE Disregarding Jobless Drop. Surprising few, the minutes to the February 5-6 BoE MPC meeting showed the committee still unanimous in its decision to keep the asset purchase program target unchanged and not to alter policy in the near-term. Notably, and unlike last August when guidance was introduced, there was no formal vote on the updated forward guidance framework that was detailed by the BoE last week. In this regard, Governor Carney said at the press conference last week that there had been strong support on the MPC for the new framework, but the BoE refused to confirm or deny whether there was a vote on it and the minutes show one was not held.

DE View: The question therefore is whether the whole MPC is as fully behind the updated forward guidance as the Governor hinted at! Regardless, there is no sign that any MPC member is uncomfortable with the policy stance of keeping conventional policy on hold for some to ti9me to come.

Jobless Drop Less Clear! Providing a less positive outcome for once, the latest labor market report was not a strong as previous data had suggested. While claimant count unemployment fell further in January, the last two falls were not nearly as marked as in data prior to December. Even so, this measure of joblessness dropped 27 600, still enough to pare the jobless rate on this basis from 3.7% to a fresh low of 3.6%.

Jobless Rate Consolidates

Moreover, a less corroborative backdrop was evident in the alternatively-sourced and broader ILO measure of unemployment, these being for the three months to December. This saw a further fall in joblessness, but with the latest jobless rate (at 7.2%) actually 0.1 percentage point above that estimated in the previous set of data, albeit with single month figure for December staying at 7.2%.

Continuing this less-strong theme, actual employment numbers rose, but a slower pace than of late, as did hours worked. But there were more solid signs regarding (rising) vacancies, while the rate of redundancies was down clearly yet again.

Labor Costs Still Weak

Despite the still very solid nature to this report, this relative strength in employment is still seemingly coming at a price. Average earnings (at 1.1%) continued to run at a pace still well below CPI inflation, meaning a continued squeeze on spending power, this possibly a cause of the softer consumer spending signals that have appeared of late.

Less Weak Productivity

The combination of rising hours and employment mean that productivity may have remained weak last quarter, albeit these latest data actually hinting that an additional drop may not now be on the cards, ie there should not be a repeat of the fall seen in Q3.

DE View: Little should be read into the fresh rise in the ILO jobless rate, especially as the data is so volatile and also is a poor indicator of slack in the labor market, considerations that the BoE has only belatedly recognized. However, the data do chime with the DE view that the UK economy has stopped accelerating and may not be able to match the close to 1% Q/Q rises in GDP that the BoE expects in the first two quarters of this year.

JAPAN – Andrew Wroblewski, London

Output Slips. The all industries index decreased 0.1% M/M in December, unwinding a little of the 0.4% November bounce, thereby maintaining the volatility seen of late. Regardless, the Y/Y rate picked up to 2.2%.

ASIA-PACIFIC ANALYSIS – Chang Liu, London

CHINA – Weaker Business Confidence. According to Market News International, the February business confidence index dropped further and by two points to 50.2, hitting a 5-year low but still an eighteenth consecutive above-50 reading and implying continuing expansion in the sector. The breakdown reflected slower growth in both new orders and production. Elsewhere, the three-month outlook also fell, but to 50.6 from 50.6, the weakest outcome on record.

MALAYSIA – Inflation Rises. Consumer price inflation rose by 0.2 percentage point to 3.4% Y/Y in January, hitting a fresh cycle-high. In M/M terms, prices rose 0.6% on the back of an increase in food and utilities prices. The Y/Y breakdown, meanwhile, revealed the latest outcome to be a reflection of rises in price pressures for utilities (3.2% from 2.4%) and restaurants (4.2% from 3.3%).

It is also notable that the elevated headline reading is still being boosted by the alcohol and tobacco component (rising 14.1% Y/Y), where prices rose sharply in October last year likely as a result of an (off-budget) increase in tobacco excise duties starting 30 September. Looking forward, inflation is likely to remain elevated due to the implementation of a minimum wage and cash transfers to low-income earners, as well as upward pressures stemming from a still-weak currency.

AUSTRALIA – Wage Growth Slows to Fresh Record-low. According to the Australian Bureau of Statistics, wages rose by 0.7% Q/Q in seasonally adjusted terms in Q4, picking up slightly from 0.5% in the previous quarter, albeit still the joint second-lowest outcome in the cycle. This reflected faster wage growth in both the private and public sectors. However, on a Y/Y basis, wage pressures eased a notch further to 2.6% in Q4 from 2.7%, hitting the lowest since records began in September 1997.

These results should be welcomed by the RBA, which switched to a neutral policy stance earlier this month but emphasized that the inflation outlook was uncertain as upside risks stemming from the recently weaker AUD was expected to be somewhat offset by downward pressures engendered by subdued wage inflation. Going forward, with the unemployment rate yet to reach its cycle-peak, wage pressures are likely to remain fairly contained at least for the coming year.

Leading Index Rises Further. The December Conference Board-compiled leading index rose further and by 0.8% M/M, accentuating the 0.2% gain seen in the previous month, a fourth successive rise. The coincident index, meanwhile, also rose further but by 0.1% to 127.7, hitting a new cycle-high.

Leading Index Falls Afresh. The leading index compiled by Westpac fell by 0.2% in M/M in January following a 0.1% rise in the previous month. The annualized growth rate, as a result, slowed to 0.46% from 1.09% in December.

Notably this is only the fourth release of the "new" leading index figures which no longer seems to contain information on trend growth or a coincidence counterpart. However, the new measure is released a month earlier (the previous index figures due this month would have been for December). In interpreting these results, the compilers highlighted that the index was designed to reflect endogenous growth trends in the economy and could not capture effects of exogenous shocks (such as the recent mining boom). As a result, while the index continues to point to above-trend growth in the economy, Westpac are officially projecting below trend growth of around 2.6% this year as mining investment unwinds.

SOUTH AFRICA – Chang Liu, London

Inflation Rises Further. Surprising to the downside once again, January consumer price inflation picked up to 5.8% Y/Y from 5.4% in December, helped by food and energy prices. Meanwhile, on an M/M basis, prices rose by 0.7%.

It is worth noting that the headline rate is within the South African Reserve Bank (SARB)'s target range for the sixth time in eight months. However, renewed weakness in the rand has caused the SARB to clearly revise up its inflation projections at its latest meeting (at the end of January) where it also implemented a 50 bp rate hike. Going forward, while inflation is likely to breach the ceiling of the Bank's target range once again in coming months, the Bank should not be overly worried as long as no fresh external shocks occur.