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

Equities: Major markets generally firmer Wednesday. Japanese equity markets closed lower, dragged down by the shipping sector. However, most other Asian markets were up, save for China. European bourses were volatile and directionless in the morning session, but settled into a strong rising trend late in the day, never looking back. U.S. stocks strengthened too, in early activity, but later fell into considerable volatility—though closing not far from the daily highs.

Bonds: Japan higher Wednesday, Europe and U.S. lower. JGBs were broadly higher. However, European benchmarks fell across the curve. Treasuries weakened with Europe early on, but recovered some of the ground later, after a successful ten-year auction.

Currencies: Mixed dollar Wednesday. The dollar rose strongly against the yen in Asian and European hours, but gave back some of the gain in U.S. trade, closing near ¥90.50. Against the euro, the US currency strengthened in late Asian hours but much more than reversed the advance later, closing near \$1.3660.

Germany: Exports slump back. The seasonally adjusted trade surplus almost halved in January, a result of a further 6.0% M/M gain in imports, which was this time accompanied by a slump of 6.3% in exports, the first fall since August.

France: Production bounces back very clearly. Overshooting expectations clearly, manufacturing output rose by 0.8% M/M in January.

Italy: Industrial production recovers clearly. Very much exceeding expectations, industrial output

jumped 2.6% M/M in January, an upside surprise accentuated by an upward revision to the December outcome.

United Kingdom: Manufacturing suffers marked setback. Surprising to the downside, and showing broad-based weakness, January manufacturing output slumped 0.9% in M/M terms.

Sweden: Output bounces back. Surprising on the upside, industrial production rose by 1.6% M/M in January.

Norway: More mixed inflation readings. Headline CPI inflation in February rose clearly and again by more than generally expected, rising from 2.5% Y/Y to an eight-month high of 3.0%.

Hungary: Continued recession confirmed. Final national accounts data showed GDP falling by an unrevised 0.4% Q/Q on a seasonally adjusted basis in Q4, having dropped 1.2% in Q3.

Japan: Orders slip back. Very much matching expectations this time around, core machinery orders (excluding shipping and utilities) fell by 3.7% M/M in January.

China: Export growth up. Trade data for February showed exports growing by 45.7% Y/Y, a much more marked gain than in January, when exports were up 21.0%.

Thailand: Policy on hold, but hike drawing closer. As expected, the Bank of Thailand kept its benchmark interest rate on hold for a seventh straight meeting in March, leaving the 1-day repurchase rate at 1.25%.

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

Treasuries fell back Wednesday, more than offsetting the small Tuesday gains, with the two-year yield rising a bit more than three basis points and the ten-year yield up two. Most of the net decline was suffered overnight, with morning trade extending the move, but an afternoon rally restoring prices to the opening levels. The catalyst for the partial recovery was a solid ten-year auction result, while the extent of the gain was seen limited by healthy respect for the uncertainties the thirty-year sale today. There were no important economic indicators or comments from Fed officials.

DAILY CALENDAR

Due today are the January trade balance and the weekly unemployment insurance report, both at 8:30 EST/13:30 GMT, and a speech from New York Fed President Dudley, at 14:00 EST/19:00 GMT.

The **international trade** figures will be watched both for a first reading on whether export and import developments will help or hurt GDP growth in the new quarter and for an update on the longer-term evolution of the deficit, which has been clouded greatly by currency and relative-growth developments.

Is generally expected to hold relatively steady (Consensus: widen \$0.8 billion, to \$41.0 billion; Decision Economics: shrink \$1.5 billion, to \$38.7 billion). Any result in the forecast range would leave the January level worse than the \$36.6 billion average in the fourth quarter, starting the new quarter off with at least a mild presumption that the trade sector will not be a positive factor in GDP growth—and a strongish presumption, if the deficit is at or beyond the wide end of the range.

Only a quite surprising contraction in the deficit would immediately raise hopes that trade will contribute to growth in the quarter. However, thinking about the impacts of anything other than an extreme deficit move, in either direction, will remain cautious until estimates can be made of the real-value export and import changes implied by the nominal results. Price movements are varying widely across product types, and translations from nominal to real can be heavily affected by the composition of the export and import totals.

Hopes for a longer-term trend improvement in the deficit have been cooled a bit by uncertainties about growth abroad and about the fact that the weakening of the dollar has not been as broad based as once thought likely—and, not incidentally by the explosion of the fiscal deficit, which has offset much, if not all, of what might have been the brute force impact of a big domestic savings increase in cutting imports relative to exports.

Now, there is at least some chance that the trade deficit could stop shrinking on a trend basis, or start widening. A single month of data brings little real guidance on the long-run trend—but explosively worse, or better, numbers could jolt thinking for a while.

The **initial claims** figure today will cover the third of four weeks in payroll March—bringing the amount of water that has passed under the bridge to the point that the character of the full month can be pretty well assessed. Results in the first two weeks pointed to a month-on-month rise in average claims about as severe as the 20,000 increase seen in February compared to January—confirming, and extending, the adverse move that suddenly occurred then.

The number today can still bend the monthly average considerably, and the direction of movement will hint at the underlying trend. Forecasts point to a decline in claims that would cut the month-on-month rise by about 10,000 (Consensus and Decision Economics: -9,000 to 460,000), moderating the deterioration enough to suggest that the situation is not necessarily worsening.

An in-line result would also be the second meaningful decline in a row (following on -29,000 last time), hinting that the extremely high reading in the first week of the survey month (+22,000 to 496,000) was an aberration—and that further declines may come.

Dudley, who votes at all FOMC meetings, speaks in London at the annual dinner of the U.K. Society of Business Economists.

Dudley is a stalwart of the dovish group that seems to be dominating policy now, and to that degree might be a bellwether of adjustments to come. He is also a career business economist himself, and often tends to speak about Fed policy and policy mechanics in a more concrete manner than many of his colleagues—so that important smoke signals could appear in just such a setting as the pro-to-pro talk today.

However, the proximity of the next FOMC meeting would make any clear pronouncements very unseemly—and, odds are, he would save them for a domestic audience anyway.

WESTERN EUROPE – Andrew Wroblewski, London

EUROZONE

GERMANY – Exports slump back. Undershooting expectations very markedly, the (unadjusted) trade surplus was €8.0 bln in January, albeit still up from €7.1 bln in the same month of 2009, but down clearly on the December surplus of €13.4 bln. On a seasonally adjusted basis, the trade surplus was down clearly too, almost halving at €18.7 bln, compared to that in December. The latter development was as a result of a further 6.0% M/M gain in imports, which was this time accompanied by a slump of 6.3% in exports, the first fall since August. *Most likely poor weather was responsible for the drop in exports.*

Meanwhile, the (unadjusted) January current account surplus improved to €3.6 bln in January from €3.2 bln in the same month of 2006.

Consumer price inflation broadly lower. Final data for February CPI inflation eased back 0.2 percentage points to 0.6% Y/Y rate in February, a result revised up 0.2 percentage points from the preliminary estimate, largely a result of a recalculation of vehicle insurance fees by the various laender. In M/M terms there was a rise of 0.4%, largely a result of a recovery in vacation costs and some rise in food and clothing offset partly by lower fuel prices. These M/M swings are also likely to be behind the softer Y/Y reading. The EU-harmonized version fell similarly, albeit dropping 0.3 percentage points to 0.5% Y/Y.

Underscoring the extent to which these data are indicative of softer underlying price pressures, Bundesbank computed data showed the ex-energy measure edged down 0.2 percentage points to a fresh cycle-low of 0.6% Y/Y – while (ex-rent) services inflation actually decreased more markedly to a new low also of 0.6%.

FRANCE – Production bounces back very clearly. Overshooting expectations clearly, manufacturing output rose by 0.8% M/M in January, an upside surprise hardly tempered by a paring back of the December reading to -0.9%.

The latest recovery in a series still displaying clear month-to-month volatility was far from broad-based, owing much to a bounce back in vehicle and general transport production. Overall production, meanwhile, jumped by 1.6% in January, the more sizeable recovery a reflection of a further surge in energy production. Nevertheless, the overall Y/Y rate of change (at 3.5%) turned positive for the first time in 21 months.

The data imply that cold weather had some impact, but possibly acting as a boost in January given the further surge in energy production. Regardless, overall production in January was up some 1.7% above the Q4 average, the later quarter having endured only a meager 0.2% Q/Q gain.

ITALY – Industrial production recovers clearly. Very much exceeding expectations, industrial output jumped 2.6% M/M in January, an upside surprise accentuated by an upward revision to the December outcome, which now shows a more modest drop of 0.2% occurred in that month. Overall, the data suggest the first clear gain in output since the huge and offsetting swings in August and September last year, with the breakdown showing yet another rise in consumer goods output. Moreover, the latest work-day adjusted Y/Y growth rate turned fractionally positive at 0.1%.

The January production data from much of the Eurozone have come in higher than expected, suggesting a firmer start to the current quarter than widely envisaged and certainly better than that seen at the start of Q4, thereby boding better for current quarter growth. It does seem to be the case that poor weather has had an effect but for most of Europe it seems the cold snap has more clearly weighed on Q4 activity than that for the current quarter with the exception of Germany where the slump in exports (see above) almost certainly was a reflection of weather induced problems.

None of which means to imply that the Eurozone is actually on a firmer overall footing, merely that there may have been an over-reaction to recent weak data. What is clear is that the globally sensitive Eurozone factory sector is showing some clearer response to the improvement in world trade, albeit with the still strong euro having some adverse effect on overall activity in boosting imports.

Back in recession. Q4 GDP dropped 0.3% Q/Q according to final data, unwinding some of the 0.5% Q3 rise, the latter having ended the five-quarter long slump. The data were revised down from the preliminary figures, now meaning that Y/Y growth was negative to the tune of 3.0%.

The previously unavailable break-down showed broad based weakness behind the fresh Q/Q slump, with only a boost from inventories preventing a more sizeable drop.

OTHER WESTERN EUROPE

UNITED KINGDOM – Manufacturing suffers marked setback. Surprising to the downside, and showing broad-based weakness, January manufacturing output slumped 0.9% in M/M terms, exactly unwinding the positive surprise seen in December. Very likely, and an assertion supported by the findings of the statisticians compiling the data, the January drop was probably a result of cold weather, albeit with it likely too that the slump was a pay-back for the strength in December as production had been brought forward ahead of the rise in VAT at the beginning of the year.

Regardless, a sturdier tone was evident in the three-month rate of growth (favored by statisticians) which actually improved to 1.0%, the best such reading in three years, albeit one whose strength will fade markedly unless data in coming months make up for the January slump. The Y/Y growth rate was also less weak, at 0.2%, it was actually the first positive reading in 21 months. Meanwhile, total industrial output fell by 0.4% M/M, the less negative outcome supported by a further rise in utility and oil production, developments also consistent with cold weather affecting the January numbers.

Comment: *These are obviously disappointing results and a contrast to the upbeat messages from various business surveys. Admittedly, too much emphasis should not be placed on the weakness in any one month especially given the clear weather impact (which was almost certainly responsible for the January plummet in exports), but this also means that less faith should be placed on the December strength. A clearer picture will hopefully come with more data. However, at this juncture, the risk remains that the UK economy will suffer a fresh contraction in the current quarter (Q1 GDP due late April), a development that will potentially be crucial for both the general election outcome (assuming it takes place in May) as well as for the ability of whoever wins to bite the fiscal bullet and make deeper budget cut measures soon after.*

For the BoE, the weakness in the economy will be doubly worrying. Not only is there the possibility that more downside risks to activity may be materializing but also there is the concern within parts of the MPC that stalled output may mean that capacity which is being currently suspended on a temporary basis may be scrapped permanently, thereby meaning that any given degree of economic weakness triggers far less of an output gap than otherwise.

SWEDEN – Output bounces back. Surprising on the upside, industrial production rose by 1.6% M/M in January, a result however, that merely unwound part of the sizeable 1.9% drop now estimated for December in data that underwent sizeable (downward) revisions largely due to new seasonal adjustments. Nevertheless, the Y/Y rate was far less negative while the January level of output was above that of the Q4 average, hinting that the current quarter is less likely to repeat the 1% Q/Q slump in production that so markedly helped undermine last quarter GDP.

This is a reassuring development for the Riksbank who will be debating the impact of those very disappointing Q4 GDP results which implied the economy unexpectedly returned to recession in the second half of last year. The extent of the weakness in those Q3 and Q4 GDP numbers were not fully in accordance with monthly data through the last half of 2009, hence providing statisticians with the motivation for the marked revisions to these production numbers.

All of which will leave policy makers, such as the Riksbank, with clear headaches as they try and adjust/decide policy on the basis of data prone not only to such large-scale revisions but also to actual calculation error (NB Statistics Sweden said it will be revising what were very upbeat January retail sales result reported late last month after finding a mistake in the data).

NORWAY – More mixed inflation readings. Headline CPI inflation in February rose clearly and again by more than generally expected, rising from 2.5% Y/Y to an eight-month high of 3.0%. This latest jump takes the headline rate clearly above Norges Bank target of 2.5%, having been very much below only as recently as October (0.6%). Prices surged by 1.3% M/M last month, led very much by an even steeper rise in electricity costs and airfares. The jump in the headline Y/Y rate was electricity related too, with a clear dampening effect coming from a swing down in clothing costs. As a result, the officially recorded core rate (CPI-ATE, which excludes taxes and electricity) fell clearly (ie 0.4 percentage points) to a two-year low of 1.9% Y/Y.

The Norges Bank focuses more on a different version of core inflation, placing more emphasis on a measure which removes only ‘underlying swings’ in energy costs (called CPIXE) and which it computes itself but publishes later on the day of release of the CPI numbers. This figure (2.4% Y/Y) in January very much tracks swings in CPI-ATE and is probably now in line with existing Norges Bank projections, which envisage that the rate will fall back more clearly (ie to 1½% through the first half of this year.)

The CPI data will have little impact on Norges Bank thinking, with the weak GDP data having a more measurable bearing. The Board meets next on March 24 having implied an evens chance that there will then be a further rate hike delivered. That probability of such a move may have fallen somewhat, although worries about house price may still mean a further hike is pushed though. If so, however, in an attempt to temper the impact on the strong krone (a very sensitive issue domestically), the Norges Bank may pare back its expectations for future hiking in revised projections it will deliver with its updated Monetary Policy Report.

CENTRAL EUROPE, RUSSIA AND TURKEY – Samuel Sidenbladh, London

CZECH REPUBLIC – Current account improves. Balance of payments data for December showed the current account in deficit to the tune of CZK 16.79 bln, an improvement on the CZK 19.27 bln shortfall in the same month of 2008. The narrowing of the deficit was due to a much wider goods surplus more than offsetting a narrower services surplus and a wider income deficit.

HUNGARY – Continued recession confirmed. Final national accounts data showed GDP falling by an unrevised 0.4% Q/Q on a seasonally adjusted basis in Q4, having dropped 1.2% in Q3. The Q4 drop was the seventh in as many quarters, but the smallest since Q2 2008, although still leaving the economy in recession. On an unadjusted Y/Y basis, the economy shrank by 4.0%, the smallest drop in four quarters, but, nonetheless, a fifth straight decline and with the working-day adjusted drop even marginally steeper (at 4.1%).

The expenditure breakdown showed continued weakness in private sector demand last quarter, with household consumption falling by 5.7% Y/Y, although with this drop being less acute than in Q3 (-8.8%), subtracting some 3.6 percentage points from GDP. Fixed capital formation was also falling in Q4, plunging 8.1% Y/Y, with the drop being steeper than in the preceding quarter (6.8%). In contrast, government spending rose very clearly, jumping 4.9%, thereby tempering the weakness elsewhere to the tune of 0.5 percentage points. Exports, meanwhile, rose by 3.1% Q/Q the first gain in over a year, meaning that net trade actually made a positive contribution to headline growth.

Although the recovery in exports will be welcome, providing as it does some support for the economy over and above that the Government is trying to provide through very modest fiscal initiatives, the latter hampered by the need to reduce the structural budget deficit. However, as the Q4 data showed, private domestic demand is still waning,

although the Statistical Office said it expected a turnaround soon. Despite this expected improvement, the Government and central bank is still expecting the economy to contract in 2010 (by 0.2%), although it should be noted that the Q4 GDP reading was less downbeat than the central bank's latest (February) forecast of -5.3%.

On the output side, meanwhile, there was a continued and broad-based, with both primary and secondary sector output falling, and with most tertiary sector components seeing equally downbeat readings.

JAPAN – Andrew Wroblewski, London

Orders slip back. Very much matching expectations this time around, core machinery orders (excluding shipping and utilities) fell by 3.7% M/M in January, thereby unwinding only a little of the 20.1% M/M surge seen in December, the later having more than offset the 11.3% and 4.5% respective drops seen in the two previous months. Admittedly, the latest result merely reinforces the picture of marked M/M volatility seen of late.

Nevertheless, the M/M breakdown showed that the January drop reflected both a setback on the non-manufacturing side but with a further jump on the manufacturing side, while the overall Y/Y figure improved further (to -1.1%). Regardless, the Cabinet Office upgraded its assessment for the first time in four months, now suggesting that the pace of decline is coming to an end.

Modest rise in corporate goods prices. Surprising few, corporate goods prices rose by 0.1% M/M in February, after an unrevised 0.3% reading for the previous month. Consequently, the Y/Y rate was far less negative at -1.5% (up from -2.1%). The data showed that the growth in export prices slowed to 1.2% Y/Y while import price developments increased by 8.0% down from 10.5%.

ASIA – Samuel Sidenbladh & Behrooz Moniri, London

CHINA – Export growth up. Trade data for February showed exports growing by 45.7% Y/Y, a much more marked gain than in January, when exports were up 21.0%. The gain was stronger than expected and was the third in as many months of data. Import growth, meanwhile, nearly halved, falling from 85.5% Y/Y to 44.7%, a three-month low, but a fourth straight gain. As a consequence the trade surplus more than doubled, rising to \$ 7.61 bln from \$ 4.84 bln.

It should be remembered that January/February data are normally influenced by the vagaries of the timing of the Chinese New Year. Indeed, the sharp fall back in imports in February could be explained by the five-day New Year holiday falling that month this year, but in February in 2009. However, this makes the pick-up in export growth last month all the more notable. Underlying the strong data, however, is of course the positive base effects provided by the poor 2009 numbers, although the statistical office was quick to point out that the trade balance were down an average 55% in the first two months of this year in comparison to last. Indeed, the two-month average reveals that imports grew at a much brisker pace than exports (63.6% compared to 31.4%) suggesting that it is still Government-stimulated domestic growth that is the main driver of economic growth.

House price inflation up. Property prices rose by 10.7% Y/Y in February, up from 9.5% in the preceding month and hitting a 23-month high.

PHILIPPINES – Exports rise faster. Coming in above expectations, exports rose by 42.5% Y/Y in January, following a 23.8% in the previous month. The latest reading was the third straight gain and the fastest pace of growth in fourteen years. The Y/Y breakdown showed that the manufacturing sector, accounting for 57% of total exports, rose by 51.2%. Meanwhile, on geographical basis, the exports gain was broad-based.

SOUTH KOREA – Household lending growth slips. Data for February showed growth in household lending falling 0.8 percentage point to 4.5% Y/Y, the lowest reading in over five years and more than canceling out the modest rise seen in January. Admittedly, some of the slowdown will have been due to the timing of the Lunar New Year holiday. Mortgage lending growth slipped as well, falling from 10.0% Y/Y to 8.5%, a 13-month low, but with mortgage lending as a percentage of total household lending unchanged. Lending to companies meanwhile was 513.2 trn won, meaning that growth rose from 2.4% Y/Y to 2.7%, as a less steep fall in large-company lending more than compensated for slowing growth in lending to small/medium enterprises.

Elsewhere, the broadest measure of money supply (LF, formerly called M3) grew by 8.1% Y/Y in January, the same pace as in December, despite M1 growth slowing and a stable M2 reading.

THAILAND – Policy on hold, but hike drawing closer. As expected, the Bank of Thailand kept its benchmark interest rate on hold for a seventh straight meeting in March, leaving the 1-day repurchase rate at 1.25%.

The accompanying policy statement repeated that the global economic backdrop had improved further since the last (December) policy meeting. However, the BoT continued to caution that risks remained, especially sovereign debt problems and high unemployment, and could hamper the sustainability of the recovery in global growth.

The domestic economy, meanwhile, surprised on the upside last quarter, and with data pointing to the momentum having carried over into Q1 while also becoming more broad-based. Indeed, the BoT noted that private consumption was now close to pre-crisis levels. Moreover, the central bank also highlighted that the downside risks to growth had declined since the last (January) meeting. As for price pressures, the BoT said that CPI inflation had risen clearly in February, mostly due to higher energy and food prices. Meanwhile, core inflation remained low, but in contrast to the January statement, the BoT now more explicitly acknowledged that it would rise in the period ahead as the economy expanded.

All of the above, in the view of the BoT lessened the need for the current exceptionally accommodative monetary policy stance, although the uncertainties surrounding global growth and –what the statement politely referred to as – ‘domestic risk factors that could adversely impact consumer and investor confidence’ (ie renewed political uncertainty) had prevented it from hiking rates.

As the statement made clear, there is now very little standing in the way of the BoT beginning to hike interest rates. Although uncertainty as to the sustainability of global economic growth is a very convenient and diplomatic excuse, it is more likely that it is the continued political upheavals – harking all the way back to the unseating of controversial Prime Minister Thaksin Shinawatra in 2006 – that are the main concern to the central bank. Indeed, the upheavals may come to (another) head this weekend with pro-Thaksin protest.

Should the political turmoil die down after that and the BoT judge the impact on confidence and growth to have been negligible, the central bank may very well start hiking rates at its next policy meeting on April 21, or if not then at the following meeting in June (no May meeting), particularly as a modest hike would still leave policy in accommodative territory. Indeed, at the press conference following the March meeting, Assistant Governor Paiboon Kittisrikangwan said that if there was nothing that would create serious damage to the economy, and the global economy developed in line with BoT forecasts, there was a high probability of the bank adjusting rates to a more normal level in the period ahead.

OCEANIA – Samuel Sidenbladh, London

AUSTRALIA – Home loans fall again. Surprising on the downside once more, total home lending fell by 7.9% M/M in January, a fourth straight and one that was the steepest in that sequence (-5.1%) in December. Moreover the number of loans has now fallen in six out of the last seven months.

This steeper drop was concentrated in new home purchase, which dropped by 13.2% following a 2.2% gain in December, but with construction and existing home purchase lending falling as well, the former at a somewhat slower pace than in the preceding month, though. Total lending ex refinancing, meanwhile, was down 8.2% M/M, having slumped by 5.4% in the preceding month, while the value of loans was down by 3.3%.

Consumer confidence up. According to Westpac, consumer confidence inched up 0.2% M/M this month, only denting the 2.6% drop seen in February, which came on the back of a substantial (5.5%) January jump. The breakdown, meanwhile, was mixed, with confidence regarding family finances improving, but with that for the economy as a whole deterioration. Consumer willingness to purchase durable goods was also down, slipping for a second straight month. However, despite the slip in some indexes in M/M terms, compared to March 2009 all indexes saw substantial (above 20%) gains).

According to Westpac, the survey was conducted during the week that the RBA hiked interest rates. Hence the slight overall improvement in the survey suggests that the central bank’s tightening cycle is still not yet having any significant impact on households. Admittedly, there are signs of some impact from the cumulative 100 bp hikes since October last year, if not in consumer confidence, than at least in the home purchase lending numbers. Indeed the beginning of the sequence of falls in the number of loans coincides with the beginning of the RBA’s hiking cycle last year and with the central bank likely to continue to tighten policy going forward (albeit at a modest pace), a further falls in home lending can be expected.

Little new from the RBA. In a speech in Sydney, Assistant Governor Lowe revealed little new, merely stating that the domestic economy was likely to expand at or above its average pace over the next few years, ie repeating what had already been mentioned in the statement accompanying the March policy decision. Lowe also reiterated that Australia started the current expansion with considerably less spare capacity than thought likely last year, and mentioned the challenge of increasing the supply of housing.