

UNDERSTANDING THE LONGWAVE ECONOMIC AND FINANCIAL CYCLE
THAT WAS THE WEEK THAT WAS



Monday, November 14th

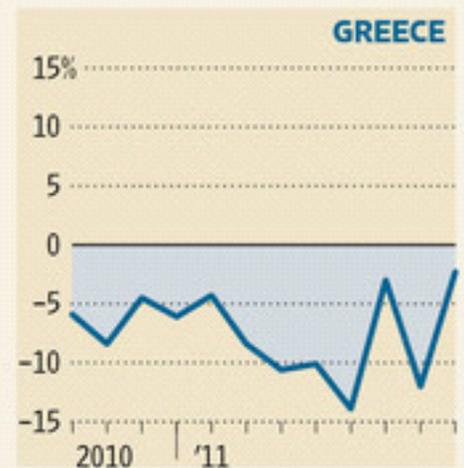
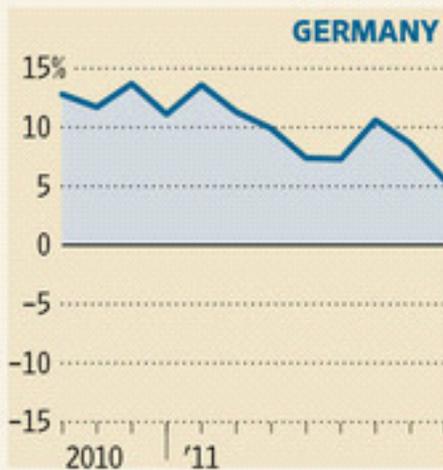
The Cabinet Office reports Japan's gross domestic product (GDP) grew at a 6% annual rate in the 3rd. quarter ended September 30th., the fastest pace in 18 months, citing a recovery from the earthquake and tsunami by companies such as Toyota Motor Corp.

MONDAY, NOVEMBER 14TH

- Front Page Headline, Bloomberg News – “Italy Auctions 5-Year Bonds as Yield Surges. The Italian Treasury issues 5 billion euros (\$4 billion U.S.) of 5-year bonds at a 6.29% yield basis – the highest yield level since June 1997 – and significantly higher than the 5.32% yield basis of the previous auction on October 13th. Yesterday, Mario Monti accepted a mandate to form a new government from Italy’s President Giorgio Napolitano; succeeding Silvio Berlusconi, who resigned as Prime Minister on November 12th., after defections eroded his parliamentary majority. Mr. Monti, an economist and former advisor to Goldman Sachs Group, faces a national debt of 1.9 trillion euros and about 200 billion in bond maturities requiring refinancing next year: ‘Italy must heal its finances and resume economic growth because today’s leaders owe it to future generations.’ At present day levels (or higher) across Italy’s yield curve and given the domestic austerity measures the Italian government must implement, it will prove a daunting – if not impossible – task not only to refinance, but also to service the new debt.
- Front Page Headline, Bloomberg News – “Boeing Wins Record Civilian Jet Order. Emirates Airlines signs a \$26 billion (U.S.) agreement with Boeing Co. to purchase fifty 777-300ER wide-body jets with an option for an additional twenty. Emirates currently operates a fleet of 90 of the 777s, the world’s largest.”
- The Paris-based Organization for Economic Cooperation and Development (OECD) reports its composite leading indicator (CLI) for members declined for the seventh consecutive month to a reading of 100.4 in September, following a level of 100.9 in August and represents the lowest reading since December 2009. In a statement, the OECD commented: “Compared to last month’s assessment, the CLIs point more strongly to a slowdown in all major economies.” The OECD CLIs are designed to anticipate turning points in economic activity relative to trend, which tends to precede turning points in economic activity by about six months.
- Following the U.S. State Department’s announcement of at least a one-year delay for a decision on the Keystone XL oil pipeline, Canadian Prime Minister Stephen Harper informs reporters at a press briefing during the Asia Pacific Economic Conference (APEC) in Hawaii: “This does underscore the necessity of Canada making sure that we’re able to access Asian markets for our energy products and that will be an important priority of this government” in the future ... “We’re formally expressing our willingness to participate in APEC’s Trans-Pacific Partnership (TPP) free-trade talks” which would link countries around the Pacific Rim; including the United States, Japan, Australia, New Zealand, Chile and Vietnam. Better late than never, Mr. Prime Minister.

- Front Page Headline, Globe and Mail – “Italy’s UniCredit to Seek \$10 billion (U.S.), Cut 5,000 Jobs. UniCredit’s Chief Executive Officer Federico Ghizzoni announces a \$10 billion (U.S.) rights issue and 5,000 job layoffs, as it retrenches to its core operations. The retrenchment process will include an exit from its London-based equity sales and trading business.”
- Eurostat reports industrial production in the euro zone declined by 2% in September from August, the steepest slide since February 2009. On a year-over-year basis, industrial output rose by only 2.2%, the weakest gain in nearly two years. Ben May, an economist at Capital Economics commented: “The euro zone will soon fall back into a fairly deep recession.”
- Front Page Headline, Financial Times – “Spanish Bond Yields Rise Sharply. Spain’s 10-year bond yield increases by 26 basis points to 6.11%, pushing the yield spread over comparable German bunds to 433 basis points (1% is equal to 100 basis points). Bond traders reported there was little investor interest to purchase Spanish or Italian bonds amid a lot of sell orders, particularly from euro zone banks. However, the European Central Bank (ECB) was buying in small size. Elisabeth Afseth, fixed income strategist at Evolution Securities commented: “The bond market is very nervous with both Spain and Italy suffering a rise in yields. The Italian bond auction was the likely trigger.”

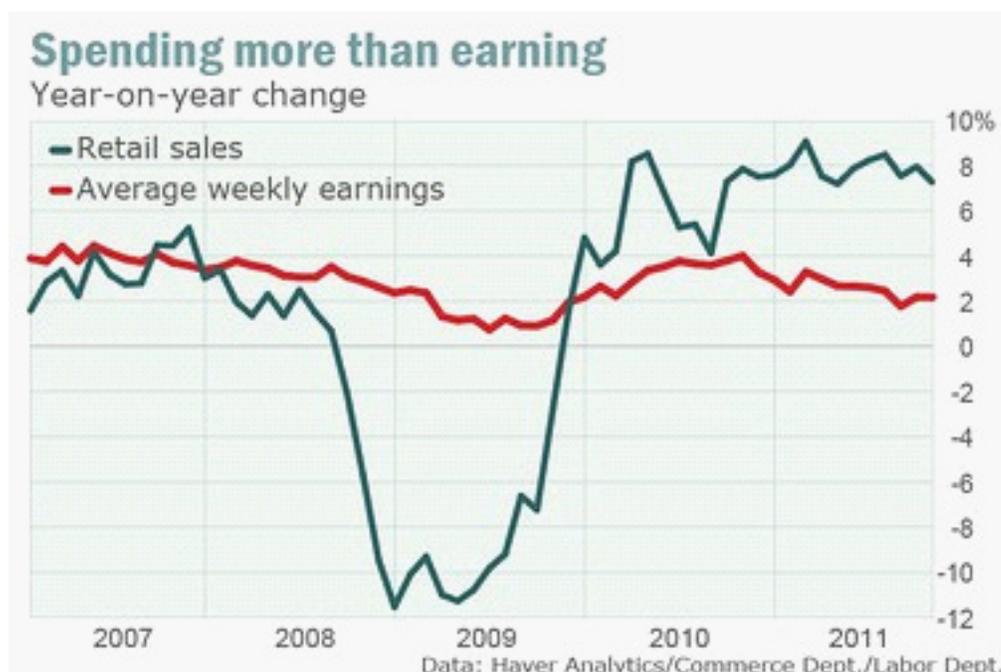
Losing Steam | Change from a year earlier in industrial production



Source: Eurostat

TUESDAY, NOVEMBER 15TH

- Front Page Headline, Bloomberg News – “Italian 10-Year Yield Breaches 7%; French Yield Reaches 3.67%. The yield on Italian 10-year bonds climbs by 26 basis points to 7.07%; while the yield spread on 10-year French bonds rose to 190 basis points over comparable German bunds. Elwin de Groot, a senior market economist at Rabobank Nederland in Utrecht commented: ‘Investors have no confidence that the euro zone can solve its debt problems. They will look for the safest place where they can store their money, which is in Germany. Every place else is suffering.’”
- The Federal Reserve Bank of New York reports its Empire State manufacturing index rose to a reading of 0.6% in November – following a level of minus 8.5 in October – the first positive reading since May, citing an improvement in the level of shipments and an expanding employee work week. The index measures manufacturing activity in New York State, northern New Jersey and southern Connecticut.
- The Canadian Real Estate Association (CREA) reports home sales in Ontario were stronger than anticipated during the 3rd. quarter, resulting in a slightly higher outlook for CREA’s 2011 and 2012 national forecasts. The industry association is now projecting sales this year will increase by 1.4%, but expects there will be slightly fewer units sold next year.
- Front Page Headline, Globe and Mail – “Two Nebraska Senators now Back Keystone Pipeline. Two Nebraska Senators, Ben Nelson (D-Neb.) and Mike Johanns (R-Neb.) issue statements endorsing the Keystone XL oil pipeline, now that TransCanada Pipeline has agreed to reroute it through Nebraska. Senator Nelson affirmed: “This is a win for Nebraskans. The pipeline will be moved out of environmentally sensitive areas of Nebraska with TransCanada proposing a new route. The pipeline will be built, bringing jobs to Nebraska.” Senator Johanns conjoined: “It appears that common sense has prevailed. I’m optimistic this could be a pathway to responsible completion of the pipeline, so we can begin transporting more energy from a friendly ally and decrease our dependence upon countries which may not share our values.”
- The Commerce Department reports U.S. retail sales rose by a seasonally adjusted 0.5% in October, following an increase of 1.1% in September, citing an increase in online sales with retailers such as Amazon and Best Buy
- Statistics Canada reports the nation’s manufacturing sales increased by 2.6% to \$49.2 billion (CAD) in September – the third consecutive monthly increase – citing, higher sales in the petroleum, coal products and transportation equipment industries.



Keystone's developments



Oil sands ■
Nintey-seven per cent of Canada's 175-billion-barrel oil reserve is contained in Alberta's oil sands.

Hardisty terminals
Hardisty is the Athabasca Oil Sands' transportation and storage hub. Its three storage tanks have a combined capacity of one million barrels.

The Ogallala Aquifer ■
Much of the opposition to Keystone XL has focused on the massive Ogallala Aquifer, which in Nebraska provides 78 per cent of water used by residents and industry and 83 per cent of water used for irrigation.

- PROJECT PHASES**
- *Keystone Pipeline*
 - ① **Hardisty to Steele City Wood River & Patoka**
In service: 2010
Length: 2,981 km
Diameter: 762 mm
Pump stations: 39
Capacity: 435,000 bpd
 - ② **Steele City to Cushing**
In service: February, 2011
Length: 480 km
Diameter: 912 mm
Pump stations: 11
Capacity: Increased Keystone to 591,000 bpd
 - *Proposed Keystone XL Pipeline*
 - ③ **Cushing to Houston & Port Arthur**
In service: 2013 target
Length: 700 km
Diameter: 912 mm
Pump stations: 26
Capacity: Would increase Keystone to 1.3 million bpd
 - ④ **Hardisty to Steele City**
In service: 2013 target
Length: 1,897 km
Diameter: 912 mm
Pump stations: 26
Capacity: Would increase Keystone to 1.3 million bpd

Cushing, Okla.
North America's key trading hub for oil and the price settlement point for West Texas Intermediate on the New York Mercantile Exchange.

Focus groups said they found images that ranged from sexy to spooky in the drafts of Canada's new polymer banknotes they examined. Here's a sampling of what they saw.

Back of the \$50 bill:

1. Some participants thought the Inuktitut writing near the top of the new \$50 polymer bill was a secret code. The writing translates to the word "Arctic."
2. Several focus groups said they saw faces in a series of small windows at the front of the icebreaker's bow, and one respondent suggested they looked like skulls and crossbones.
3. The shape of Newfoundland and Labrador, which appears on the back of the new \$50 bill, behind the CCGS Amundsen, was initially mistaken by some respondents for a bird, a war plane, or Pinocchio.



Front of the \$100 bill:

4. Focus groups thought that former prime minister Robert Borden looked either cross-eyed or that his eyes were looking in different directions in the draft of the \$100 bills they examined.
5. Almost all of the groups agreed the see-through window on both of the new polymer bills looked like the silhouette of a woman's body.
6. All of the groups said they saw religious iconography on the face of the Peace Tower clock in the bottom right corner of the \$100 bill, and some said it looked like the Star of David.
7. Some respondents felt that Mr. Borden's moustache was poorly groomed. Some of the former prime minister's whiskers fall well below his upper lip in the Bank of Canada's final version of the \$100 polymer bill.



Back of the \$100 bill:

8. One focus group in Vancouver thought the double-helix DNA strand on the new \$100 bill looked like sex beads, while others saw the Big Dipper.
9. Some groups compared the bills to "Monopoly money," noting the polymer they're made out of felt less real than paper money.



- Front Page Headline, Globe and Mail – “Bank of Canada Introduces New Polymer Bills into Circulation. The Bank of Canada places new polymer (plastic) \$50 and \$100 dollar bills into circulation to replace the paper-style money used since the early 1800s. The new banknotes will be almost impossible to counterfeit.
- According to a new Bank of America / Merrill Lynch survey, 53% of U.S. fund managers polled in November believe the United States will suffer another sovereign debt rating downgrade by 2013, while 36% believe it could occur as soon as next year. Moreover, the majority of fund managers still see the probability of a global recession materializing within the next 12 months. Separately, the overwhelming majority of European fund managers polled expect the euro zone to fall into recession soon, with 72% believing it is likely to happen within the next 12 months. This represents a significant increase from the 37% forecasting a recession in October.

WEDNESDAY, NOVEMBER 16TH

- The Federal Reserve reports U.S. industrial production – the output of the nation’s factories, mines and utilities – rose by 0.7% in October, following a revised decline of 0.1% in September previously reported as a gain of 0.2%. Capacity utilization – a gauge of slack in the economy – rose to 77.8% in October from 77.3% in September, its highest level since July 2008.
- The Labor Department reports the U.S. consumer price index (CPI) declined by 0.1% in October, following a 0.3% rise in September. The core rate (excluding food and fuel) rose by 0.1% in October, matching September as the smallest monthly increase this year.
- Front Page Headline, Globe and Mail – “Britain’s Jobless Rate Hits 17-Year High. The Office for National Statistics reports the number of people without a job on the wide ILO measure grew by 129,000 in the three months ended September 30th. to 2.622 million – the highest level since the 3rd. quarter of 1994 – as the number of unemployed young people exceeded a record one million. The coalition government’s room for manoeuver is limited by its pledge to erase the nation’s huge budget deficit through a tough austerity plan, which includes curtailing an estimated 400,000 public sector jobs. Separately, in a press conference, Bank of England Governor Mervyn King stated: ‘The immediate impact of the decline in (confidence) sentiment is that the growth outlook for the world economy has worsened since August. That is also true here in the United Kingdom, where (economic) activity could be broadly flat until the middle of next year.’
- Eurostat reports euro zone consumer prices rose by 0.3% in October – holding the annual rate steady at 3% – citing higher fuel costs. Excluding energy, consumer inflation in the euro zone was 2% in October on a year-over-year basis.
- Front Page Headline, Globe and Mail – “Moody’s Downgrades 10 German Banks. Nearly all of Germany’s public sector Landesbanks are downgraded by Moody’s Investors Service, citing: ‘Future government (or systemic) support for German public sector banks has become less certain, partly owing to the new bank resolution regime which enables the government to impose losses on creditors outside of liquidation.’ Several of the Landesbanks – a network of state-controlled lenders – that mainly offer commercial banking services to Germany’s small and mid-sized companies, were forced to accept state aid during the 2008 financial crisis.
- Front Page Headline, New York Times – “Citi to Shed 3,000 Jobs; BNP Paribas Plans to Cut About 1,400. Citigroup plans to eliminate about 3,000 jobs, or 1% of its global work force, with approximately one third coming from its securities and banking unit. Separately, BNP Paribas announces plans to cut about 1,400 jobs: including 400 jobs in France and the remaining layoffs occurring at the bank’s international operations.”
- Front Page Headline, National Post – “Fitch Warns of Further Contagion Risks to U.S. Banks. In a report entitled U.S. Banks – European Exposure, Fitch Ratings warns: ‘We believe that unless the euro zone debt crisis is resolved in a timely and orderly manner, the broad credit outlook for the U.S. banking industry could worsen. Direct exposures appear manageable in the context of banks’ capital positions and diverse earnings streams. Recently, public disclosure of direct exposures has generally improved; however, it varies from bank to bank.’ Fitch’s warning follows a week that has witnessed ‘core’ euro zone sovereign bond yields increase sharply. France, Austria and the Netherlands all incurred higher bond yields this week, as the fixed income markets began pricing in the threat of a possible euro zone dissolution.”

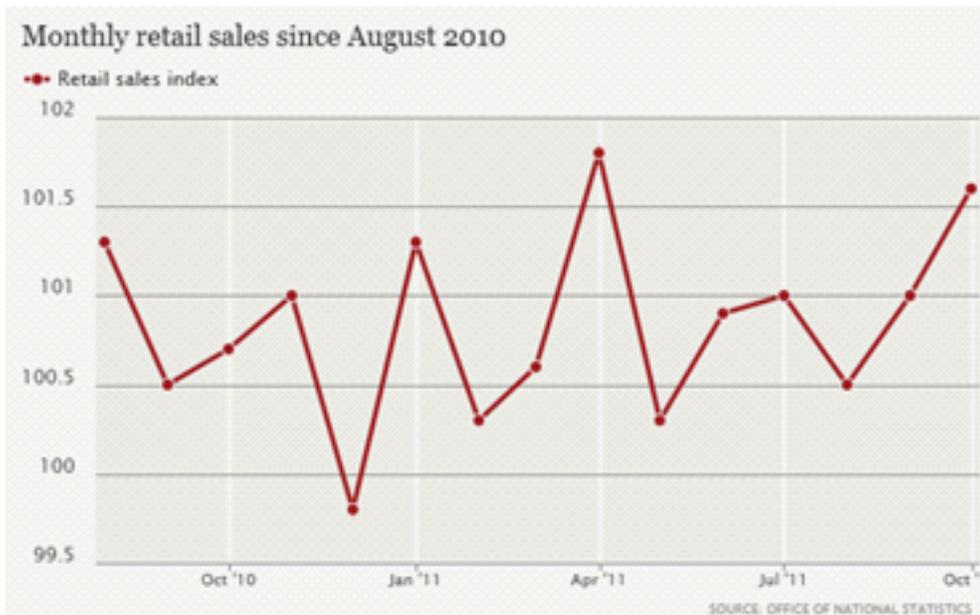
THURSDAY, NOVEMBER 17TH

- The Commerce Department reports U.S. housing starts declined by 0.3% to an annual pace of 628,000 units in October from a downwardly revised pace of 630,000 units in September. Separately, building permits increased at an annualized rate of 10.9%.

- The Labor Department reports U.S. initial claims for state unemployment benefits declined by 5,000 to 388,000 in the week ended November 12th., while continuing claims declined by 57,000 to 3.61 million in the week ended November 5th. The number of people who have exhausted their traditional benefits but are now receiving emergency or extended benefits from federal programs fell by about 70,400 to 3.46 million in the week ended October 29th.
- Front Page Headline, Bloomberg News – “Spanish Bond Yields Rise to Euro-Era Record. Spain auctions 3.56 billion euros (\$4.8 billion U.S.) of 10-year bonds maturing in January 2022 at an average yield of 6.975%, up 154 basis points from the previous 10-year auction only a month ago (100 basis points is equivalent to 1%). Laurence Boone, chief economist at Bank of America / Merrill Lynch in London commented: ‘Tensions are increasing on Spain for sure even as interest rate levels remain sustainable for the moment. This is not necessarily due (only) to Spain itself, rather more to the lack of a (debt) solution at the euro zone level.’
- The Office for National Statistics reports U.K retail sales rose by 0.6% in October compared with September, citing pre-Christmas discounts and strong food sales
- Front Page Headline, Bloomberg News – “Congressional Debt Panel Members Harden Positions as November 23rd. Deadline Nears. Super Committee Co-Chairman Jeb Hensarling (R-Tx.) tells reporters his party won’t go beyond its offer to increase tax revenue by \$300 billion (U.S.) to cut the debt, until Democrats offer a plan to address the long-term growth in federal spending on entitlement programs such as Medicare: ‘I’m not moving (from) this particular offer. I’m still waiting for Democrats to actually solve the problem of entitlements. Should that come, I would be more than willing to negotiate.’ Super Committee Co-Chairwoman Patty Murray (D-Wa.) informed reporters: “Members of my party are not going to accept a (deficit reduction) plan which gives a tax break to the wealthiest Americans and balances all of this incredible challenge we have on the backs of middle-class Americans.’ Both parties must agree on a proposal to enable a committee vote by its November 23rd. deadline. By the year end, failure to enact a plan which would cut \$1.2 trillion (U.S.) from the deficit over the next decade, would force that amount in automatic spending cuts commencing in 2013. Democrats oppose reductions in entitlement programs such as Medicare – as sought by Republicans – unless Republicans agree to larger increases in tax revenue. As was the case during last summer’s statutory debt ceiling debate, political gridlock remains very much alive in Washington, as the national debt breaches the \$15 trillion (U.S.) mark.

Housing Starts (Monthly Index Level)
Through October 2011, Seasonally-Adjusted (SGS, Census)





FRIDAY, NOVEMBER 18TH

- Front Page Headline, New York Times – “ECB President Rejects Calls to Rescue Euro Zone. In his first speech as President of the European Central Bank, Mario Draghi complains to the Frankfurt European Banking Congress that Europe’s political leaders have been too slow to carry out their own plans to address the euro zone debt crisis. Despite heightened calls for ECB intervention, Mr. Draghi implicitly rejected calls for the central bank to use its enormous resources to halt the rising borrowing costs for Spain and Italy which threaten their solvency and by extension, the European and global economies. Mr. Draghi asserted: “The ECB will not deviate from its focus on price stability because other measures could undercut the bank’s credibility. Gaining credibility is a long and laborious process. However, losing credibility can happen quickly and history shows that regaining it has huge economic and social costs. Where is the implementation of long standing decisions made at numerous summit meetings? We should not be waiting any longer.”
- Front Page Headline, New York Times – “Detroit to Lay Off 9% of its Public Work Force. Detroit’s Mayor Dave Bing announces the jobs of 1,000 City employees – about 9% of its municipal work force – will be eliminated early in 2012. Mayor Bing stated the layoffs are intended to save the City \$14 million (U.S.) by June 2012 – at which time the City will have a \$45 million (U.S.) deficit – and will be coupled with pay cuts and higher health care contributions from those workers remaining employed; a corporate tax rate increase; pay concessions from contractors hired by the City and an immediate hiring freeze for civil service jobs. In a statement, Mayor Bing summarized: “Job layoffs will be strategic. We will limit the impact on residents, protecting core services like police and fire protection as much as we can. Our fiscal crisis will require everyone to share in the sacrifice. We need support from our residents to help push our unions, businesses, vendors and elected officials to enact the common sense changes which we need.”
- Front Page Headline, Daily Telegraph U.K. – “Spain – The Fifth Victim to Fall in Europe’s Arc of Depression. As union leader Javier Dos described it, the EU-imposed austerity plans of the incoming Partido Popular “are nothing more than the continuation of policies leading Europe toward disaster.” The new government of Mariano Rajoy has precious few policy levers at its disposal and cannot alone do anything at this late stage to prevent a death spiral within the straitjacket of the European Monetary Union. The immediate destiny of his country lies entirely in the hands of Germany, the ‘AAA’ rated creditor core, the EU authorities and the European Central Bank: the nexus of policy-making power that together dictates whether Spain will be thrown a lifeline or be pushed further into depression and social catastrophe. What can the quiet Galatian do to stop Spain’s 22.6% unemployment rate – or 46% for youth – from ratcheting higher this winter as the combined effects of fiscal austerity and a credit crunch together do their worst? How can he stop real M1 deposits from contracting at a 5% rate?”

- Front Page Headline, Agence France-Presse – “Greece May Lose Billions in Taxes. The European Commission (EC) reports; “Sixty billion euros (\$83 billion U.S.) of unpaid taxes – of which 30 billion euros (\$41.5 billion U.S.) in pending tax cases – are currently outstanding in Greece. An EU official stated: ‘Only half of the legal-in tray is even theoretically collectible and only 11 billion euros is likely ever to be recovered.’ This week, the Greek Finance Ministry reported tax receipts for the first 10 months of 2011 had declined by 4.1% compared to the same period in 2010. Accordingly, the EU executive is assisting Greece in negotiations with Switzerland in a bid to claw back vast amounts of money believed to be hidden in Swiss banks by Greek nationals.”
- The World Gold Council (WGC) reports central banks took advantage of lower gold prices in September by purchasing 148.4 tonnes of gold bullion during the 3rd. quarter, more than double the entire amount of government buying in 2010. Marcus Grubb, WGC Managing Director of Investments, commented: “We are seeing ... unprecedented levels of central bank buying. We do believe this is a long-term trend and not just short-term tactical buying. Some Asian and Latin American nations, which for years have invested their surplus revenues into U.S. Treasuries, are now looking to diversify. The WGC didn’t name the central banks that were doing the buying, although it’s widely known that governments in countries such as China, India, Brazil and Russia are intent upon diversifying their holdings away from U.S. Treasuries. Any pivot in the reserve strategy of countries such as China and India inevitably leads to speculation about the end of the U.S. dollar’s dominant role as the world’s reserve currency.”
- Front Page Headline, National Post – “Run from Debt to Cash Sparks Selling. Concern over widening yield spreads on European sovereign debt hammered investor confidence around the world yesterday, driving stock markets lower and sending a shiver through the financial sector. With euro zone government debt sitting at \$12 trillion (U.S.) and the economy starting to stall, analysts are increasingly pessimistic that struggling members like Greece – which has essentially already been bailed out – and Italy can meet their obligations even if voters there agree to harsh austerity programs that are being rolled out. European banks, which hold the lion’s share of sovereign debt and as a result are sitting in the eye of the storm, hold a whopping \$25 trillion (U.S.) of outstanding loans, including \$5 trillion (U.S.) from foreign creditors. According to the Bank Credit Analyst: “Given the massive amounts of debt involved, even a best case scenario is grim. A synchronized deleveraging of banks and countries would have a huge impact on the global economy if it is enforced aggressively. As much as \$1.2 trillion (U.S.) of debt could be withdrawn from the global economy in 2012, as lenders move to boost capital in a bid to stay solvent, resulting in a 2% drag in global demand.” Alec Levine, an equity derivatives strategist at Newedge Group SA in New York commented: “People are running to cash. The markets, not the policymakers, are controlling events right now and that’s a very dangerous place to be. We’re seeing every type of asset in the world being sold right now except for U.S. Treasuries.”

CLOSING LEVELS FOR FRIDAY, NOVEMBER 18TH.

		WEEKLY CHANGE
Dow Jones Industrial Average	11,796.16	– 357.52 points
Spot Gold Bullion (December)	\$1,725.10 (U.S.)	– \$63.00 per oz.
S&P / TSX Composite	11,892.44	– 384.41 points
10-Year U.S. Treasury Yield	2.01%	– 5 basis points
Canadian Dollar	97.35 cents (U.S.)	– 1.59 cent
U.S. Dollar Index Future (Spot Price)	78.023 cents	+ 1.112 cent
WTI Crude Oil (December)	\$97.67 (U.S.)	– \$1.32 per barrel

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"Those who cannot remember the past are condemned to repeat it." Santayana