Monday March 5th, 2012

LONGWAVE group

UNDERSTANDING THE LONGWAVE ECONOMIC AND FINANCIAL CYCLE

THAT WAS THE WEEK THAT WAS

Monday, March 5th

Front Page Headline, Globe and Mail – "China Lowers GDP Growth Target. In a two-hour address to the opening session of the National People's Congress, Chinese Premier Wen Jiabio asserts: "We are keenly aware that China still faces many difficulties and

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challenges in economic and social development. Internationally, the road to global economic recovery will be tortuous, the global financial crisis is still evolving, and some countries will find it hard to ease the sovereign debt crisis anytime soon. Domestically, it has become more urgent, but also more difficult to solve institutional and structural problems and alleviate the problem of unbalanced, uncoordinated and unsustainable development … Since growth stability remains Beijing's top priority; policymakers will keep inflation to 4% and set a new GDP target of 7.5%."

- The Commerce Department reports U.S. factory orders declined by 1% in January, following an upwardly revised increase of 1.4% in December. Separately, the Tempe, Arizona-based Institute for Supply Management's non-manufacturing index rose to a reading of 57.3 in February from a level of 56.8 in January, citing a service industry expansion at the fastest pace in a year.

- Front Page Headline, Financial Times – "Police and Protestors Clash in Moscow. Police and demonstrators clashed and hundreds of arrests were made in central Moscow during protests against widespread fraud in Sunday's election of Vladimir Putin to a third term as Russia's President. Police noted the protest which began peacefully, numbered 14,000 while organizers claimed 20,000.

Photo Source: Getty / Financial Times

- Front Page Headline, Daily Telegraph U.K. – "Dutch Freedom Party Advocates Euro Exit as 2.4 Trillion Euro Bill Looms. The Dutch Freedom Party calls for a return to the Guilder, becoming the first political movement in the euro zone with a large popular base to opt for withdrawal from the euro currency. Geert Wilders, the leader of the right wing populist party with one sixth of the seats in the Dutch Parliament, declared: 'The euro is not in the interests of the Dutch people. We want to be master of our own house and our own country, so we say yes to the guilder. Bring it on.' Mr. Wilders made his decision after receiving a report by London-based Lombard Street Research, concluding that the Netherlands is badly handicapped by EU membership and it could cost the European Monetary Union's creditor core more than 2.4 trillion euros to hold the EMU together over the next four years. 'If the politicians in The Hague disagree with our report, let them show the guts to hold a referendum. Let the people decide.' The study's co-author Charles Dumas, predicted: 'The euro zone cannot survive in its current form. The longer Europe's politicians dither, the more costly it will become. The euro can only survive if it becomes a fiscal transfer union with national sovereign debt subsumed in euro zone bonds … The report concludes that 'EMU membership locks the Netherlands into a system in which cost competitiveness is matched by massive structural overvaluation of costs in Med-Europe, resulting in costs that will suck cash out of the core euro zone.

Dutch Freedom Party Leader Geert Wilders
Source: EPA / Daily Telegraph U.K.

- Front Page Headline, Daily Telegraph U.K. – "Spain's Sovereign Thunderclap and the End of Merkel's Europe. International Business Editor, Ambrose-Evans Pritchard writes: 'The Spanish rebellion has begun, sooner and more dramatically than I expected. As many readers will already have seen, Premier Mariano Rajoy has refused point blank to comply with the austerity demands of the European Commission and the European Council (hijacked by Merkozy). Taking what he called a 'sovereign decision,' he simply announced that he intends to ignore the EU deficit target of 4.4% of GDP for this year, setting his own target of 5.8% instead (down from 8.5% in 2011). In the twenty years or so that I have been following EU affairs closely, I cannot remember such a bold and open act of defiance by any state. Usually, such matters are fudged. Countries stretch the line, but do not actually cross it … Premier Rajoy is surely right to seize the initiative. Spain's economy will contract by 1.7% this year under its modified plans and unemployment will reach 24% (or 29% under the 1990s method of counting). To compound this with manic fiscal tightening – and no offsetting devaluation – is intellectually indefensible. There comes a point when a democracy can no longer sacrifice its citizens to please reactionary ideologues determined to impose 1930s scorched earth policies. What is striking is the wave of support for Mr. Rajoy from the Spanish commentaries. This one from Pablo Sebastian left me speechless: 'Spain isn't any old country that will allow itself to be humiliated by the German Chancellor. The behavior of the European Commission towards Spain over recent days has been infamous and exceeds their treaty powers … these eurocrats think they are the owners and masters of the Iberian Peninsula. Other nations in the EU along with Spain are sick and tired of Chancellor Merkel's meddling and Germany's usurpation – with the help of Sarkozy's France and their pretended 'executive presidency' that does not in fact exist in EU treaties. Rajoy must not retreat one inch. The stakes are high and the country is in no mood to suffer humiliations from a Chancellor who is amassing all the savings of Europe and won't listen to anybody, as if she were the absolute ruler of the Union. Merkel and the Commission should think hard before putting their hand into the sovereignty of this country – or any other – because it will be burned.' This then is the fermenting mood in the fiercely proud and ancient nation of Spain in year three of depression, probably the worst depression the country has seen since the 1640's – or have I missed a worse one? As for the fiscal compact, it is rendered a dead letter by Spanish actions. If the text were enforced, the consequences would be ruinous. It enshrines Hooverism in EU law, and imposes contractible policies without the consent of future parliaments – including any future Bundestag. Indeed, it probably violates the German constitution. But it won't be enforced in any meaningful sense because the political realities of the EU are already intruding and will intrude further. A President Francois Hollande of France will rip it up. The Latin Bloc is awakening."

TUESDAY, MARCH 6TH

- In a new report, the Institute of International Finance (IIF), a banking trade group, warns: "A disorderly default by Greece would likely force Italy and Spain to seek aid to prevent being engulfed by the debt crisis and would cause more than 1 trillion euros ($1.36 trillion U.S.) in damage to the euro zone." The IIF helped negotiate a voluntary Greek debt exchange involving bondholders taking a 53.5% loss on their principal, then exchanging their current bond holdings for new bonds with longer maturities and lower coupons; enabling Greece to cut more than 100 billion euros from its debt load. According to the IIF, "Failure to complete the debt exchange (by Thursday of this week), could endanger the country's second bailout leaving the potential for a hard default. The European Central Bank (ECB) would likely suffer major losses, putting the ECB's Greek exposure at 177 billion euros, while Ireland and Portugal would likely need further assistance. A default would also likely trigger at least 160 billion euros in recapitalization costs."

- The Brazilian national statistics agency reports the nation's gross domestic product (GDP) grew by 2.7% for the full year of 2011, following a 7.5% GDP expansion in 2010. John Welch, chief strategist for CIBC World Markets in New York, commented: "Brazil is losing international competitiveness. Brazilian officials are blaming all their problems on the high level of the real, but have ignored structural reforms."

- Front Page Headline, Globe and Mail - "Stocks Slide on Fears of Greek Default, Slower Growth in China. Stock markets fall sharply; handing equity investors their worst day in months on renewed fears of a disorderly default in Greece and concerns that China's slowdown would impede global economic growth. On Wall Street, the Dow Jones Industrial Average (DJIA) fell 203.66 points to 12,759.15 at the close. On Bay Street, Toronto's S&P/TSX composite index tumbled 225.31 points to 12,298.63."

Greek protestors burn a German flag while trying to enter parliament in Athens February 7th. Source: Daily Telegraph U.K.

- Front Page Headline, New York Times – "Stanford Convicted: $7 Billion (U.S.) Ponzi Scheme. A federal jury convicts Allan Stanford, a Texas financier, on 13 of 14 counts of fraud, in connection with a worldwide scheme that lasted more than two decades and involved more than $7 billion (U.S.) in investments. The jury's decision followed a six-week trial and came 3 years after Mr. Stanford was accused of defrauding nearly 30,000 investors in 113 countries in a Ponzi scheme involving $7 billion (U.S.) in fraudulent high interest certificates of deposit at the Stanford International Bank , which was based on the Caribbean island of Antigua. Mr. Stanford now faces a possible life sentence."

- Front Page Headline, National Post – "Raymond James Adds Banking. Raymond James Bank, a wholly owned subsidiary of Florida based Raymond James Financial has completed the acquisition of the local assets of Allied Irish Banks PLC's Canadian Operations. The U.S. bank, founded in 1984, made the acquisition through its Canadian subsidiary, Raymond James Finance Co. of Canada. The transaction was announced last June and has spent the past 8 months navigating through the U.S. regulatory process."

WEDNESDAY, MARCH 7TH

- Automatic Data Processing (ADP) reports U.S. private sector payrolls increased by 216,000 in February, led by hirings in the service sector and small businesses, following an upwardly revised gain of 173,000 in January, previously estimated as 170,000. Joel Prakken, Chairman of Macroeconomic Advisors (which produces the report for ADP) commented: "Payroll conditions continue to improve at a moderate pace and are consistent with other indicators suggesting some firming of the labor market."

- The Economy Ministry in Berlin reports German factory orders (seasonally and inflation adjusted) declined by 2.7% in January, following a 1.7% gain in December, citing a drop in export demand for machinery and equipment

- Statistics Canada reports the value of domestic building permits declined by 12.3% in January, following December's 10.5% gain, which had taken building permits to a seasonally adjusted 4 ½ year high point

- The Bank of Nova Scotia reports net income for the fiscal quarter ended January 31st. rose by 15% to $1.44 billion (CAD) from $1.25 billion (CAD) in the same period a year ago. Total revenue increased by 11% to $4.72 billion (CAD), with acquisitions accounting for more than half the increase, enabling the bank to raise its annual dividend by 3 cents per share to 55 cents per share. In a research note, John Aitken, an analyst at Barclay's Capital commented: "We believe that the significant operating leverage BNS generated in the first fiscal quarter is a positive step and could represent a turnaround on Scotiabank's relative expense growth."

- Front Page Headline, National Post – "Canadian Bank Mortgage Rate Dichotomy. On the same day, the Royal Bank of Canada raises its 4-year fixed mortgage rate by 40 basis points to 3.39%, while the Bank of Montreal lowers its 5-year fixed mortgage rate by 50 basis points to 2.99%. In an interview, Royal Bank spokesman Matt Gierasimczuk related: 'Our long-term funding costs have increased considerably due to global economic concerns and while we have refrained from passing along rate changes to our clients, it is now necessary for us to increase our 4-year mortgage rate.' Concurrently, Frank Techar, manager of BMO's domestic retail bank explained: 'We believe this will allow our customers to borrow smartly. This mortgage rate is consistent with the debate around the need to reduce consumer debt levels."

- In the latest semi-annual list compiled by Global Finance Magazine, six Canadian banks rank among the world's top 25 most creditworthy financial institutions: Royal Bank of Canada (10th.); Toronto-Dominion Bank (11th.); Bank of Nova Scotia (14th.); Caisse Centrale Desjardins (18th.); Bank of Montreal (23rd.) and CIBC (25th.).

THURSDAY, MARCH 8TH

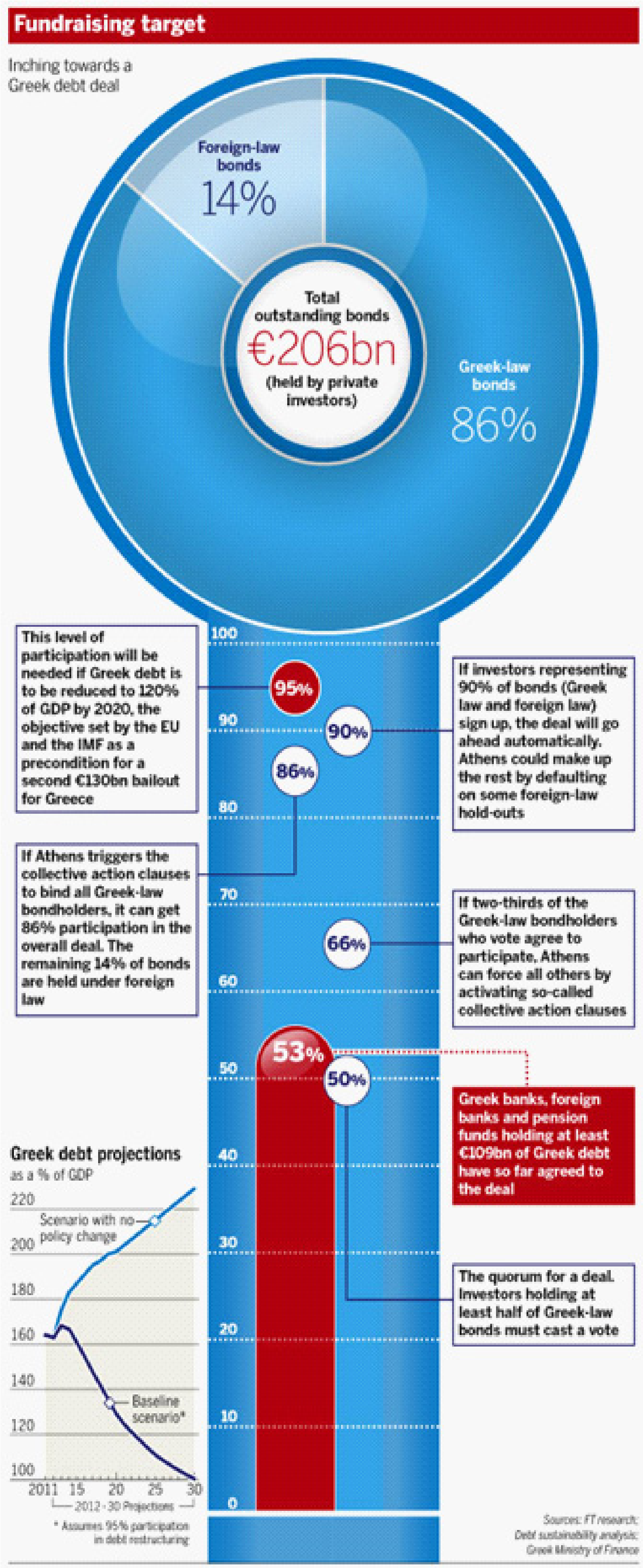
- Statistics Canada reports the nation's new home price index rose slightly by 0.1% in January, citing price increases of 0.3% in both metropolitan areas of Calgary and Vancouver over December; while prices in metro Toronto remained relatively flat

- The Labor Department reports U.S. initial claims for state unemployment benefits increased by 8,000 to 362,000 in the week ended March 3rd. while continuing claims rose by 10,000 to a seasonally adjusted 3.42 million in the week ended February 25th. Separately, according to consultants Challenger, Gray and Christmas, the number of U.S. corporate planned layoffs declined slightly to 51,728 in February, down 3.3% from the 53,486 announced in January. Job losses were up 2% compared with the same period a year ago, when 50,702 job layoffs were announced. The greatest losses were in the transport and consumer products sectors. CEO John Challenger commented: "Being heavy users of fuel, both sectors are feeling the impact, not only of rising fuel prices, but also, from their dependency on consumers who are being forced to spend more on gas."

- Front Page Headline, Financial Times – "Japan Posts Record Current Account Deficit. The Japanese Finance Ministry reports a record 437 billion yen current account deficit in January – the biggest monthly shortfall since comparable records began in 1985 – defying the most pessimistic expectations for the world's third-largest economy. In the wake of a trade deficit for the calendar year 2011 – a first for Japan over more than two decades – fears are intensifying that Japan is rapidly moving towards a lasting current account deficit. This could lead to reliance upon foreigners to purchase government bonds, ultimately forcing up bond yields and possibly threatening a fiscal crisis. January's shortfall fuelled those fears, as rising imports met an 8.5% year-over-year decline in exports, caused partly by the early timing of Chinese New Year. Such deficits are a relatively new phenomenon for Japan. For the past few decades, the country has consistently exported more than it imported, while earning more income on its overseas investments than it paid to foreigners in interest and dividends."

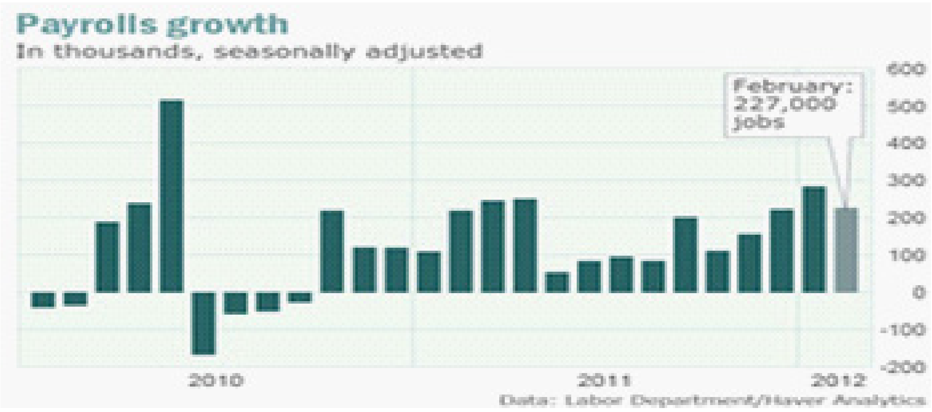
- Front Page Headline, Daily Telegraph U.K. – "Legal Deception in Greece May Doom Portugal. At the start of the (sovereign debt crisis), European Union leaders declared it unthinkable that any euro zone state should require debt relief, let alone default. Each pledge was breached and the haircut imposed on banks, insurers and pension funds ratcheted up to 75%. In a comment to the Telegraph, Marc Ostwald at Monument Securities stated: 'The rule of law has been treated with contempt. This will lead to litigation for the next ten years. It has become a massive impediment for long-term investors and people will now be very wary about Portugal.' In February, the European Central Bank (ECB) exercised its droit du seigneur, exempting itself from losses on Greek bonds. The instant effect was to concentrate more losses on other bondholders. Marchel Alexandrivich at Jefferies Fixed Income asserted: 'It does not matter how often the European Union authorities repeat that Greece is a 'one-off' case, nobody in the (bond) market believes them.' This might not matter too much if Greece were really a 'one-off' case but the bond market is afraid that Portugal will dive into the same downward (financial) spiral when austerity (measures) begin to take effect."

- Front Page Headline, MarketWatch News – "Greek Bond Exchange Successfully Concluded. Private-sector bondholders owning 85% of Greece's outstanding sovereign debt – well above the government's minimum threshold – have consented to participate in the bond exchange, enabling Greece to force any public-sector bondholders regulated under Greek law to comply with the majority. The success of the bond exchange will reduce Greece's debt burden in excess of 100 billion euros and remove one of the few remaining obstacles preventing its creditors from completing a bailout initiative worth 130 billion euros. Jane Foley, senior currency strategist at Rabobank International in London commented: 'The (bond exchange) deal … is just one more hurdle in a crisis that is still very likely to bring further bad news in the coming months.' Eric Wand, an interest rate strategist at Lloyds TSB in London, elaborated: 'Overall, a successful debt exchange … should be taken (by investors) as a knee-jerk positive for risk markets as uncertainty is removed. However, the immediate positive reaction will be overshadowed very soon with concerns over the macro environment and the effectiveness of (European Union) firewalls to save the next (euro zone country) in line.'


Fundraising target
Inching towards a Greek debt deal
Foreign-law bonds
14%
Total outstanding bonds
€206bn
(held by private investors)
Greek-law bonds
86%
100
90
80
70
60
50
40
30
20
10
0
95%
90%
86%
66%
53%
50%
This level of participation will be needed if Greek debt is to be reduced to 120% of GDP by 2020, the objective set by the EU and the IMF as a precondition for a second €130bn bailout for Greece
If Athens triggers the collective action clauses to bind all Greek-law bondholders, it can get 86% participation in the overall deal. The remaining 14% of bonds are held under foreign law
If investors representing 90% of bonds (Greek law and foreign law) sign up, the deal will go ahead automatically. Athens could make up the rest by defaulting on some foreign-law hold-outs
If two-thirds of the Greek-law bondholders who vote agree to participate, Athens can force all others by activating so-called collective action clauses
Greek banks, foreign banks and pension funds holding at least €109bn of Greek debt have so far agreed to the deal
The quorum for a deal. Investors holding at least half of Greek-law bonds must cast a vote
Greek debt projections
as a % of GDP
220
200
180
160
140
120
100
Scenario with no-policy change
Baseline scenario*
2011 15 20 25 30
2012 - 30 Projections
* Assumes 95% participation in debt restructuring
Sources: FT research; Debt sustainability analysis; Greek Ministry of Finance

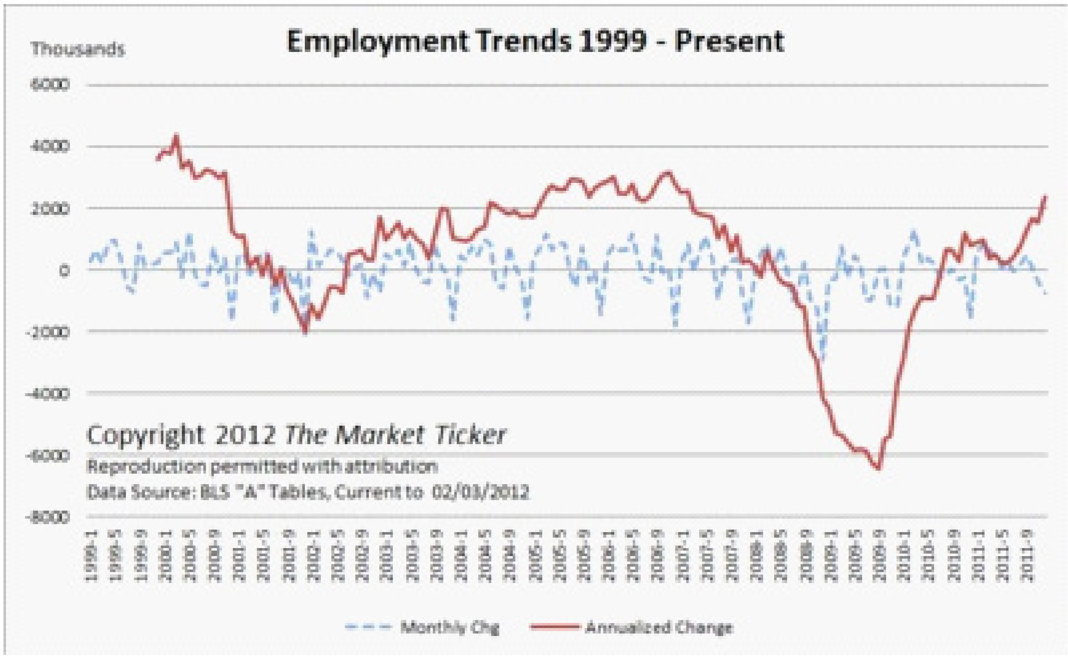
FRIDAY, MARCH 9TH

- The U.S. Bureau of Labor Statistics reports the nation's non-farm payrolls increased by 227,000 in February while the unemployment rate remained unchanged at 8.3%.

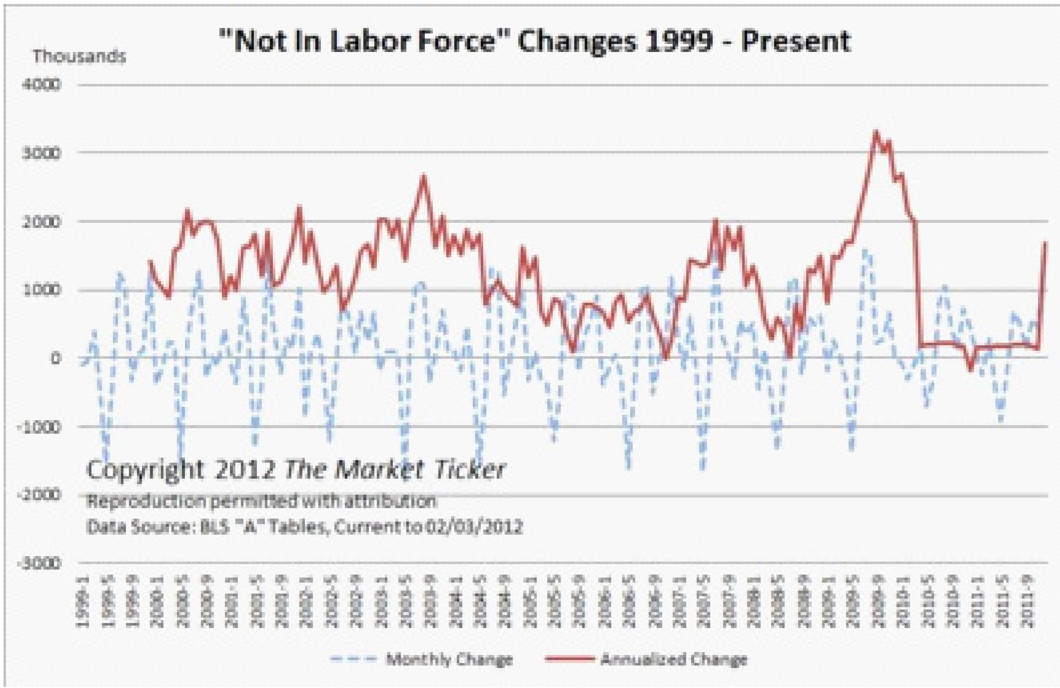


According to The Market Ticker: "This employment report is an intentionally false picture being presented by a government agency. In December, the alleged 200,000 jobs that were gained were a phantom; when one looked inside the household data, we found instead deterioration in both the employment participation rate and a decline in the absolute number of employed persons, while population rose. That is, the actual counts,(as opposed to black-box statements) said that the labor picture deteriorated in December, contrary to the reported numbers. In January, it was worse … far worse.

Let's start with the 'base picture' that is causing the cheering.

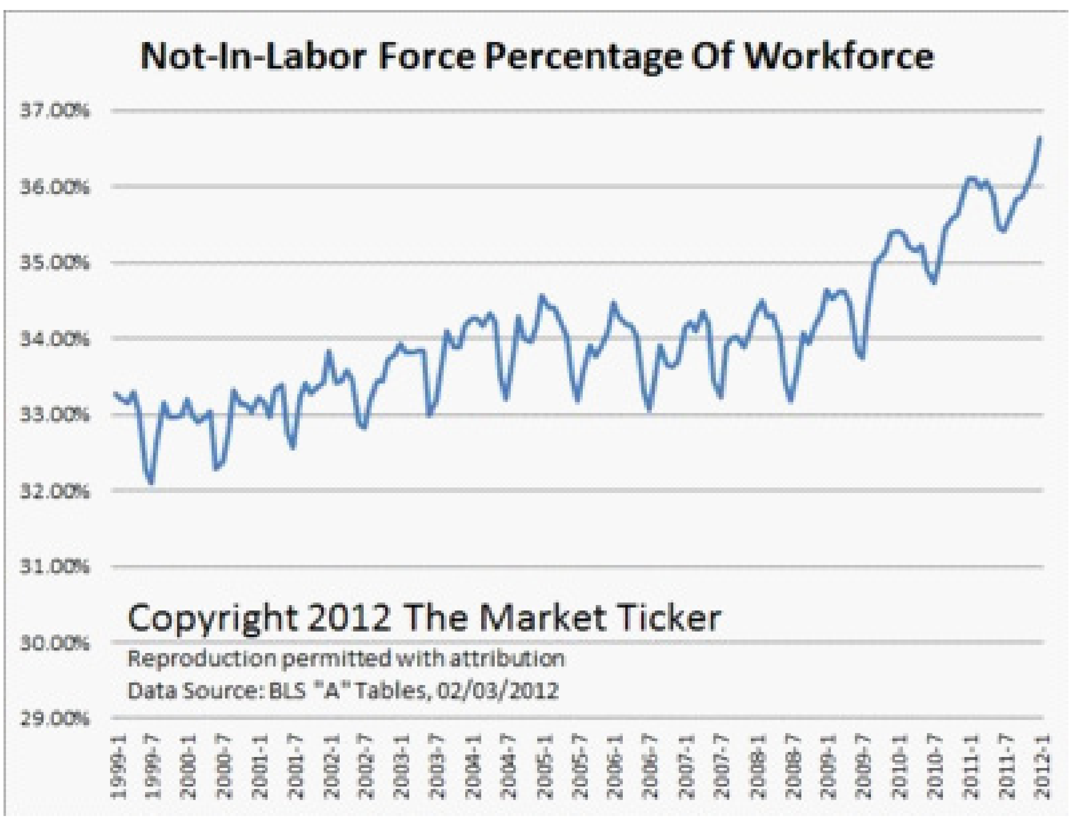


That nice red line looks good, right? Well …

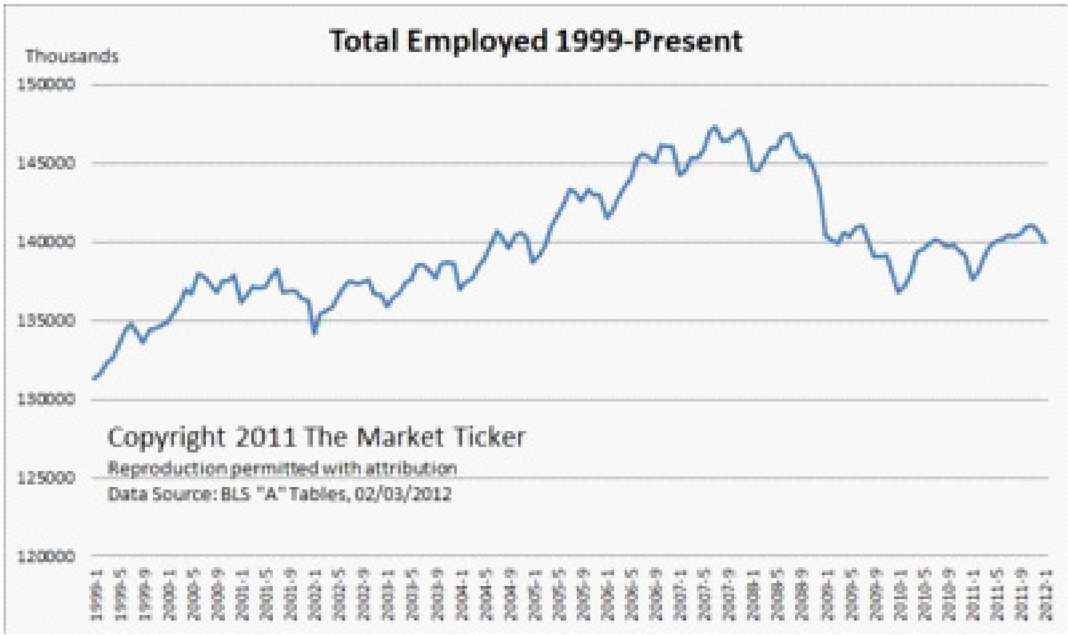


'Not in Labor Force' numbers leaped upward on an annualized basis (seasonally adjusted the 'right way') and what's worse, on a raw basis 1.572 million people exited the labor force in February.

This is reflected in the percentage of those not in the labor force as a percentage of the working-age population, which hit an all-time high going back to the initiation of the data series we've tracked since 1999.

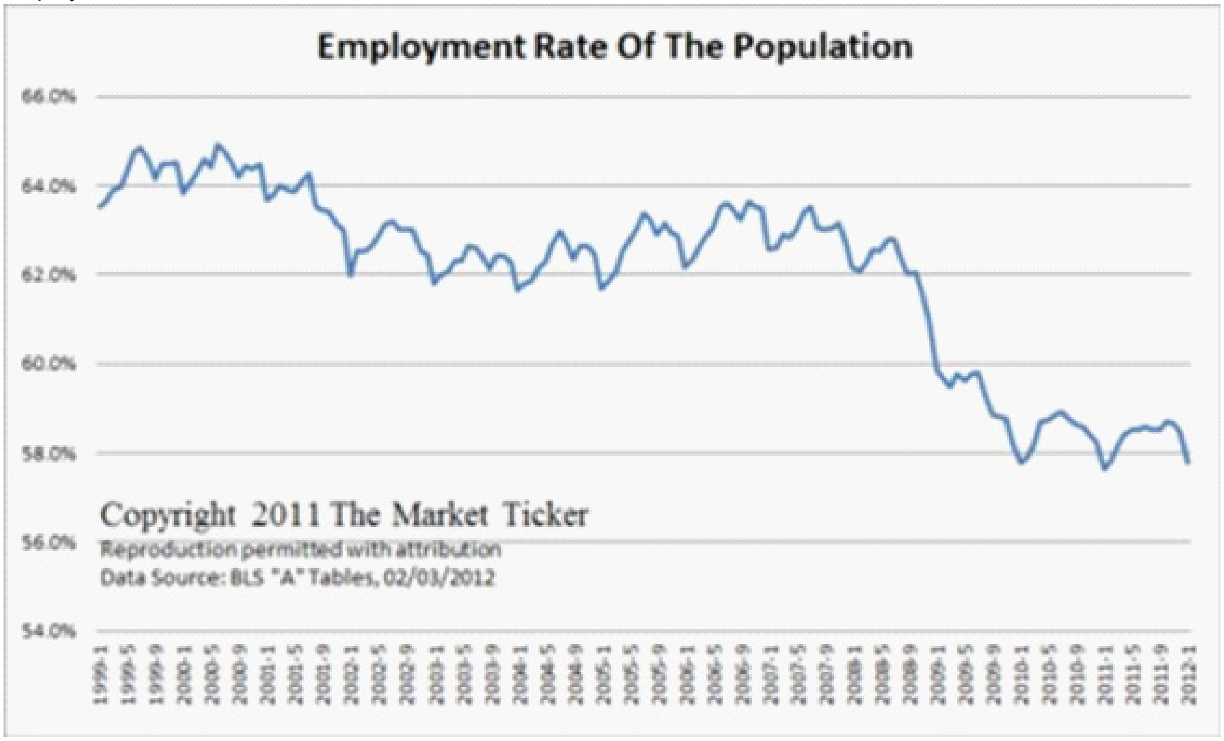


That's 0.6% of the entire labor force that departed the working population in one month, three times the alleged drop in the unemployment rate. This means that internally, the numbers were even worse than they first appeared.



Indeed, the total number of employed persons fell a lot. To put a number on it, the total number of employed persons declined by 737,000 by actual count. The cheerleaders will state that this is a common thing in January and indeed it is. However, the correct adjustment is to look at the population increase and subtract that back off as well. In other words, we take the loss of employment and add the population growth.

As a result, we get a whopping 2.422 million in the wrong direction which was bested only by the minus 2.618 million in January of 2009, through the process of this downturn. In fact, other than January 2009, there has never been a single month in our table, which dates back to 1999, that registered a worse combined number. This performance rates a literal second from utter despair and disaster, and the employment rate shows it.



- Front Page Headline, Globe and Mail – "Greece Secures Largest Sovereign Debt Overhaul in History. The Greek government announces it has reached its bond exchange target with private sector bondholders of Greek sovereign debt; facilitating a trade for new Greek bonds with lower coupons and longer maturities. The transaction enables Greece to expunge in excess of 100 billion euros ($131 billion U.S.) of its national debt. Bonds totaling 172 billion euros were tendered, bringing the participation rate to 83.5%. That means the minimum threshold was set for Greece to trigger the collective action clauses (CACs) in order to force most of the remaining bondholders into the exchange transaction, raising the participation rate to 95.7%. In a statement Greek Finance Minister Evangelos Venizelos remarked: 'I wish to express my appreciation to all of our creditors who have supported our ambitious program of reform and adjustment and who have shared the sacrifices of the Greek people in this historic endeavour."

- Front Page Headline, Globe and Mail- "Successful Greek Bond Exchange Triggers $3 Billion (U.S.) in Default Swaps: ISDA. The International Swaps and Derivatives Association – the agency which oversees financial derivatives – announces its determinations committee, meeting in London, 'resolved unanimously that a Restructuring Credit Event has occurred with respect to the Hellenic Republic.' This means that holders of credit default swaps (CDS) on Greek bonds will be able to claim insurance payments as a result of Greece's decision to force bondholders subject to Greek law, to participate in the distressed debt exchange. The ISDA noted that overall payouts on CDS linked to Greek bonds will be less than $3.2 billion (U.S.). Once the CACs are triggered, all of the 177 billion euros of sovereign bonds that were issued under Greek (as opposed to foreign) law, will be exchanged for a cash payment and lower-valued bonds. The process will eliminate 53.5% of the face value of the old bonds, equivalent to a net present value loss of more than 70%. As a result, the Greek national debt will decline from 350 billion euros to about 250 billion euros."

- Statistics Canada reports the nation posted a trade surplus of $2.1 billion (CAD) in January, following a $2.86 (CAD) surplus in December, citing a 2.3% decline in exports of industrial goods and materials; as well as precious metals and alloys

- The Commerce Department reports the U.S. trade deficit increased by 4.3% to $52.6 billion (U.S.) in January, following a revised $50.4 billion (U.S.) in December, citing higher imports of machinery and equipment, as well as inventory stockpiling

- Front Page Headline, Globe and Mail – "Russia Beckons for Trade but Canada is Wary of Risks. In a recent interview with the Globe and Mail in Moscow, President Elect Vladimir Putin bemoaned how little trade there is between Canada and Russia, given the two countries' (economic) similarities. Bilateral trade totaled just $2.8 billion (CAD) in 2011, roughly half of what Canada did with Brazil … Investment is also on the light side: Canadian direct investment In Russia totaled less than $600 million (CAD) in 2010, up 12% from 2009 … Russia remains an exceedingly tough place for Canadians to do business – its potential undermined by distance, taxes, corruption, red tape and unpredictable investment rules, particularly in mining. For example, Toronto gold miner Alhambra Resources Ltd. has found success in neighbouring Kazakhstan, but deliberately shuns Russia. Citing high taxes and regulation, Alhambra's chief information officer Ihor Wasylkiw resolved: 'Russia is too difficult. We wouldn't go there. Do you want to invest a billion dollars in a country where they can come to you one morning and say: Good morning, we're taking over your company?' (Just) last month, Barrick Gold Corp. announced it was pulling out of Russia altogether by selling its 20% stake in Highland Gold Mining Ltd. – a move analysts suggested was due to the difficulties of operating there. At Long Wave Analytics, we have well predicted that Western countries will rue the day they allowed Russia to join the World Trade Organization (WTO) last fall. Vladimir the Terrible has just been re-elected President of Russia – most likely for two 6-year terms – under whose direction, the country's financial /economic, or political systems cannot be trusted. To erase any remaining doubts, click the link:
www.economist.com/node/21013016

- The China Customs Bureau reports the country posted a trade deficit of $31.5 billion (U.S.) in February, citing imports rose by 39.6% on a year-over-year basis, following a 15.3% decline in January; while exports increased by 18.4%. Data in the first two months of this year are somewhat distorted by the timing of the week-long Lunar New Year holiday, which occurred in January this year and in February in 2011.

- Default. Fitch Ratings downgrades Greece's sovereign debt credit rating from 'C' to "restricted default" after the country secured a strong majority of private sector creditors to participate in a bond exchange transaction, which will eradicate more than 100 billion euros from Greece's national debt level

LONGWAVE group

CLOSING LEVELS FOR FRIDAY, MARCH 9TH.		WEEKLY CHANGE
Dow Jones Industrial Average	12,922.02	– 55.55 points
Spot Gold Bullion (April)	$1,711.50 (U.S.)	+ $1.70 per oz.
S&P / TSX Composite	12,503.62	– 140.20 points
10-Year U.S. Treasury Yield	2.03%	+ 6 basis points
Canadian Dollar	100.92 cents (U.S.)	– 0.23 cent
U.S. Dollar Index Future	80.064 cents	+ 0.615 cent
WTI Crude Oil (April)	$107.40 (U.S.)	+ $0.70 per barrel