

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



Monday, January 21st
Front Page Headline, Globe and Mail – “Protests Become Standard Fare During Spain’s Recession.”

Monday, January 21st

Martin Luther King Jr. Holiday in the United States

Spanish workers are increasingly walking off the job to protest wage reductions and privatizations by the government as it tackles a steep public deficit. Judges, garbage collectors, doctors and bus drivers are among those involved in a wave of disruptive strikes and demonstrations, as workers lose patience with the centre-right government’s spending cuts after four years of economic crisis. Francisco Garcia, a hospital cleaner and union leader complained: ‘The government has put the country on the path to ruin. They are taking away all of our benefits and our purchasing power.’ Mr. Garcia and his co-workers went on strike for 17 days this month to protest two months of not being paid by the Valencia regional government. The strike – which led to reports of unsanitary conditions – was just one of many recent walkouts. **See also, Longwave Analytics Economic Outlook for 2013: Europe, January 18, 2013.** www.longwavegroup.com/economic-predictions



Protestors in Madrid shout slogans objecting to higher court fees.

Source: Associated Foreign Press

- Statistics Canada reports the nation's wholesale sales rose by 0.7% in November to \$49.6 billion (CAD), led by higher sales volumes in the computer and communications equipment and supplies industry. Ontario wholesalers reported a 2.1% increase – the largest since July 2011 – while Manitoba and Alberta also posted gains.
- German Chancellor Angela Merkel's bid for a third term in office suffered a blow yesterday when left-leaning opposition parties defeated a coalition of her Christian Democrats and pro-business Free Democrats with a razor thin one-seat majority in a closely-watched election in the state of Lower Saxony. The narrow defeat for Ms. Merkel's centre-right coalition parties reveals how difficult it may be for her coalition to stay in power after the general election in September.
- Front Page Headline, Financial Times – **“President Obama Defends Role of Strong Government.** In his Inaugural Washington speech, U.S. President Barack Obama mounted a vigorous defense of interventionist government and the role of a social safety net in an uplifting and uncompromising address to the nation, which marked the formal commencement of his second term as America's head of state. Delivered from the steps of the Capitol building to a crowd that filled the Washington Mall, President Obama's speech struck the optimistic notes and oratorical highs which are his trademark. Moreover, he acknowledged the coalition which returned him to the White House, with nods to equality for women and gays, a path to citizenship for illegal immigrants and the necessity for the state to play a role in combating poverty. The President stated: ‘Preserving our individual freedoms ultimately, requires collective action.’”



U.S. President Obama delivers inaugural speech. Source: Washington Post

- Front Page Headline, Financial Times – **“America's Debt Dilemma: A Looming Crisis.** As the Obama administration begins its second term this week, in the first of a series, the Financial Times explores the real fiscal choice for the United States: not the short-term frenzy of cliffs, debt ceilings, (fiscal) deficits and sequesters, but how or whether, to pay for an older population. The answer will decide the very nature of the

U.S. economy in the 21st. century. Down one path, the retirement contract is untouched, however, tax levels must increase by 30% or more; the U.S. would resemble a mature European economy. Down the other (path), taxes remain low, but barring a revolution in healthcare costs, provision for at least some retirees – current or future, rich or poor – must be slashed. The question is whether a small federal government can endure with an aging population, which helps to explain why the political battle is so extraordinarily vicious. The choice is not between a little more tax on the rich, or a nasty squeeze on the education budget. Rather, it is about what kind of country America will become. For President Barack Obama and the Democrats, it is clear there should be a balance of tax increases and spending cuts: ‘The alternative is for us to proceed and cut commitments which we've made on things like Medicare, Medicaid or Social Security and for us to fundamentally change commitments which we've made to ensure that seniors don't go into poverty' ... It is in the 2020s when the big spending will commence. The baby boomers, then into their 70s, will start getting sick; the Social Security retirement age will stabilize at 67 in 2022 and the Congressional Budget Office is unwilling to assume that certain controls on medical costs will remain for more than a decade. The revenue and spending paths will become irreconcilable and the debt (level) will quickly mount. Plans which do tackle the long-term, such as the Simpson-Bowles proposal which emerged from the President's deficit commission, all mix three elements: spending cuts, tax increases plus efforts to extract more out of Medicare. The trick is to find a balance.”

Tuesday, January 22nd

- The ZEW Center for Economic Research in Mannheim reports its index of analyst and investor expectations – which aims to predict German economic developments six months in advance – rose to a reading of 31.5 in January from a level of 6.9 in December. Jens Kramer, an economist at Nord LandesBank in Hanover commented: ‘The higher reading gives reason for optimism. We should see a considerable economic improvement toward mid-year with stronger momentum. The worst in the (economic) crisis seems to be behind us.’
- In its annual study of global employment trends, the Geneva-based United Nations agency International Labour Organization reports: “Global unemployment grew by another 4 million people over the course of 2012, amid weaker economic activity and lingering uncertainty about hiring. In the fifth year after the outbreak of the global financial crisis, global (economic) growth has decelerated and unemployment has begun to increase again. The length and depth of the labour market crisis is worsening labour market mismatch, contributing to extended spells of unemployment.

Jobs in exporting countries are particularly vulnerable, as international trade weakened in some areas of the world. Accordingly, new jobs which become available often require competency levels which the unemployed do not possess. These skills mismatches will make the labour market slower to respond if economic activity improved, unless more policies to promote skills training are introduced ... We expect the global unemployment rate will increase again this year and next, with the number of unemployed people reaching 210.6 million over the next five years. The economic slowdown has dramatically diminished the labour market prospects for young people as well, since many experience long-term unemployment right from the beginning of their labour market entry; a situation which was never observed during previous (economic) cyclical downturns."

- Statistics Canada reports the nation's retail sales rose by a modest 0.2% to \$39.4 billion (CAD) in November – the fifth consecutive monthly gain – citing higher sales at automotive and parts dealers, as well as electronics and appliance stores
- The National Association of Realtors reports U.S. existing home sales declined by 1% to a seasonally adjusted annual pace of 4.94 million units in December
- Front Page Headline, Globe and Mail – **“Nebraska Approves New Route of Keystone XL Oil Pipeline.** Nebraska Governor Dave Heineman announces his state has approved the revised route for the Keystone Oil Pipeline that would transport Canadian oil sands crude oil to refineries in Texas, paving the way for the Obama administration to grant approval for the project. Trans Canada Corp., the Canadian company building the pipeline to transport 830,000 barrels of crude oil per day, had submitted a new route after environmentalists complained that the initial route would cross ecologically sensitive regions in Nebraska.”



File photo of Nebraska Governor Heineman

Source: Reuters

the European Union; in a surprise move that threatens to inhibit trade and cast a new shadow over the troubled bloc. Mr. Cameron plans to say that if elected in 2015, a Conservative Government would renegotiate the U.K.'s relationship with the EU and then hold a referendum on the new settlement during the first half of its 5-year parliamentary term. Such a referendum would mark the first time in recent years that an EU member has offered its citizens such a vote ... While many people remain focused on the risk of Greece leaving the euro zone, the promise of a referendum by Mr. Cameron would raise the prospect of an exit by a far more essential member; one of the bloc's biggest economies and its most important London financial center. The move is a risky gambit by Mr. Cameron, who has found himself in a tight spot on the issue of Europe. Repeatedly, Mr. Cameron has said that he believes it is in Britain's best interest to remain part of the EU. However, some members of his own party – who think too much power is ceded to Brussels – have aggressively pressed him to significantly reduce the U.K.'s ties to the bloc, or exit all together ... Mr. Cameron is gambling that, by offering the vote, he can appease both the anti-Europe wing of the Conservative Party and simultaneously, keep Britain in the EU under new and better terms. Mr. Cameron is due to say: 'I want the European Union to be a success and I want a relationship between Britain and the EU that keeps us in it.' His pledge is also dependent upon the U.K. being able to negotiate a treaty with the other members of the EU, which will number 28 with Croatia's planned accession in July.”



Prime Minister Cameron leaves 10 Downing Street on Tuesday.

Source: European Pressphoto Agency

- Front Page Headline, Wall Street Journal – **“U.K. Plans to Offer Vote on EU Role.** U.K. Prime Minister David Cameron will propose offering the British people a vote on whether the country should remain a member of
- Front Page Headline, Globe and Mail – **“EU Group Obtains Approval for Financial Transaction Tax.** A group of eleven European Union countries, including Austria, Belgium, Estonia, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia and Spain – the

Netherlands may also participate – have obtained approval from the European Commission (EC) – the EU’s executive branch – to introduce a tax on financial transactions. The tax is designed to help pay for the rescue of Europe’s banks; as well as discourage risky trading. It would apply to anyone in the eleven countries who makes a bond, share or derivatives trade. At a press conference following a meeting of the bloc’s 27 finance ministers, EU Tax Commissioner Algirdas Semeta stated: ‘The Financial Transaction Tax decision marks a major milestone for EU tax policies. While I have no immediate estimate of how much revenue the tax would generate, the EC had previously estimated that such a tax across the 27-nation bloc could yield 57 billion euros (\$76 billion U.S.) a year.’ While the EC had hoped that the tax would be adopted by the entire EU membership, several countries including Britain – home to the EU’s biggest financial hub – refused to endorse the measure amid concerns over its economic impact. The eleven countries involved now are expected to begin working out detailed proposals.”

- Front Page Headline, Financial Times – **“President Obama Agrees to Short Term Debt Limit Extension.** The White House announces it would not oppose a proposal by Republicans to extend the U.S. statutory debt limit until May 19th. paving the way for a temporary pause in the debt ceiling stalemate. White House Press Secretary Jay Carney noted: ‘The threat of default alone was already causing harm to the economy and concern to business. Certainly, we welcome what appears to be a decision by many Republicans not to pursue that strategy.’”
- Front Page Headline, Business Insider – **“Disturbing Abuses of Monetary Policy Evident: Weidmann.** Speaking at a reception at the Frankfurt stock exchange’s operator, Deutsche Boerse, German Bundesbank President Jens Weidmann warned: ‘We are witnessing disturbing abuses in Japan and Hungary, where the new government is interfering massively in the affairs of the central bank, calling forcefully for a more aggressive monetary policy. An unintended consequence of governments dictating monetary policy could be a much stronger politicization of exchange rates. To date, the international monetary system has weathered the (sovereign debt) crisis and avoided a devaluation race, which I very much hope will remain the case.’ **See also, Longwave Analytics Economic Outlook for 2013: Japan, January 18, 2013.** <http://www.longwavegroup.com/economic-predictions>
- Front Page Headline, Financial Post – **“Perfect Storm Hits Alberta Oil Revenues.** In an address to the Calgary Chamber of Commerce yesterday, Alberta Finance Minister Doug Horner warned: ‘The province is facing a perfect storm because Canadian oil marketed in the U.S. is selling at a deep discount, world markets seem increasingly out of reach and resource revenues have plummeted. No storm is good and this one is going to be severe. The gravity of the problem just registered

in the past few months when Alberta, the federal government and the oil industry realized the magnitude of the North American oil glut. Our biggest problem is that Alberta is landlocked. In fact, of the world’s major oil-producing jurisdictions, Alberta is the only one with no direct access to the ocean. Until we solve this problem – and that means all of Canada must work together – the differential will remain large. Of course, it’s significantly affecting Alberta’s bottom line to the tune of billions of dollars.’ Indeed, Alberta’s bitumen is getting \$30 (U.S.) a barrel less than oil from Mexico and Texas, plus lighter crude varieties are getting \$50 (U.S.) less than oil from the Middle East. Almost a third of the province’s revenue is derived from oil and gas revenues. At present, while the provincial government is not planning any tax or royalty increases and is not yet ruling out a balanced budget; it is, however, warning that its March 7th. budget for the fiscal year ending in March 2014 will be making a big course correction from big spending to big belt tightening. **At Longwave Analytics, we would remind our readers that the Canadian Federal Government allowed the Province of Alberta to default on its debt obligations during the Great Depression in 1936.**

Wednesday, January 23rd

- Front Page Headline, Washington Post – **“U.S. House of Representatives Votes to Suspend Debt Limit.** By a vote of 285 to 144, the U.S. House of Representatives votes to suspend the nation’s statutory debt limit (currently \$16.4 trillion U.S.) thereby, allowing the federal government to borrow as needed to meet spending obligations through May 18th. In addition, the GOP’s measure would impose a new requirement on Congress, a key to gaining support from a broad range of their own members. Both chambers of Congress must adopt a budget by April 15th. as required by law, or have their congressional remuneration withheld until the commencement of the new Congress in 2015.”



House Speaker John Boehner addresses reporters. Source: Getty Images

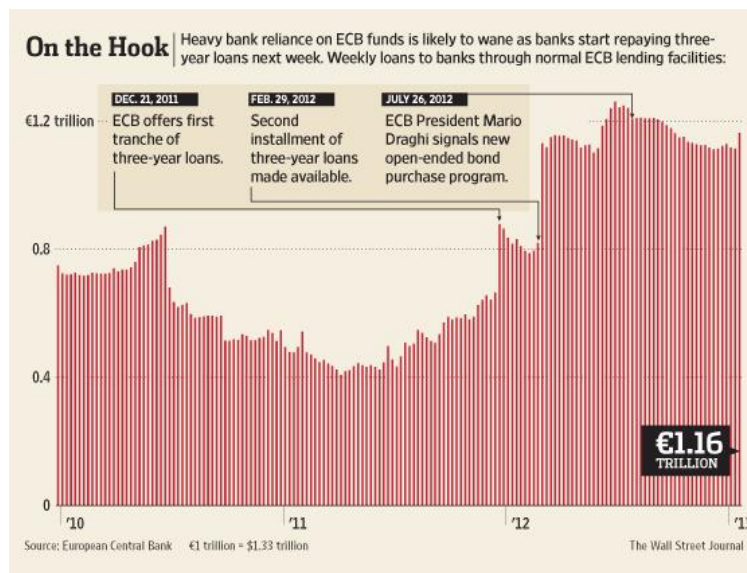
- The Office for National Statistics reports U.K. unemployment claims declined by 12,100 to 1.56 million in December – the lowest level since June 2011 – while the nation’s unemployment rate, as measured by the International Labour Organization, declined slightly to 7.7% in the quarter ended November 2012
- Front Page Headline, Business Insider – **“Five Major Global Risks Which Davos Elites Should Fear.** Business, government and entertainment elites are meeting this week at the World Economic Forum in Davos, Switzerland. In a new report entitled The Vulnerability of Elites: Geopolitical Risk in 2013, the Eurasia Group highlights five such risks to political and financial elites. ‘The vulnerability of elites cuts across emerging markets and advanced economies, democracies and authoritarian states, public and private institutions and a wide array of issues. This is the challenge: as their legitimacy becomes suspect, political actors struggle to react to instability, crises and opportunities in the most effective manner.’
 1. Sino-Japanese relations could worsen over the Senkaku-Diaoyu Islands and could (adversely) impact Japan’s economy and place pressure on the U.S. for support.
 2. The violence in Syria is expected to continue and this could further destabilize the region and provide fertile ground for Al Qaeda to re-emerge.
 3. Diplomacy could fail and the Iran-Israel-U.S. nuclear standoff could intensify, raising concerns of (military) strikes on Iran.
 4. As the U.S. withdraws its troops, Afghanistan risks a resurgence of the Taliban.
 5. Reliance upon the European Central Bank (ECB) for (financial) assistance could backfire and voters could turn to euro-skeptic (political) parties. The inability of European governments to respond to the euro zone’s sovereign debt crisis has left the ECB as ‘the only effective actor. Central banks are neither democratically legitimized, nor democratic’ and while countries like Spain are looking for ECB (financial) assistance, countries like Germany are concerned about the expanding role of the ECB. Moreover, governments in Germany, Austria, the Netherlands and Finland are finding it more difficult to convince their parliaments to bailout countries like Italy and Spain. This risks causing voters to turn to ‘euro-skeptic or nationalist parties, such as the True Finns in Finland or Austria’s Freedom Party.” **See also, Longwave Analytics Economic Outlook for 2013: Europe.** www.longwavgroup.com/economic-predictions
- In its Monthly Policy Report, the Bank of Canada left its Bank Rate unchanged at 1% and highlighted “a more muted inflation outlook and the beginning of a more constructive evolution of imbalances in the household sector. Therefore, the timing of any withdrawal of stimulus from the economy is less imminent than previously anticipated.”
- Front Page Headline, Financial Times – **“Pentagon Faces a Rebel Yell over Pensions.** Along the Florida coast, there is a sense of foreboding among American military retirees about what the country’s fiscal problems might mean for their finances, but at the Fleet Landing retirement community in Jacksonville, that resentment is focused squarely on the Pentagon. Founded by officers from the nearby Mayport Naval Station and only a few blocks from the beach, Fleet Landing houses a large number of retired veterans who have watched with increasing anxiety as the Pentagon has warned about runaway military entitlement spending ... For Chuck Hagel, the controversial nominee to be the next secretary of defence, getting confirmed by the Senate will be only the first stage in a series of bruising political battles in the years ahead. As President Barack Obama begins his second term in office, the U.S. federal budget remains in crisis. Efforts to rebalance finances could have a profound effect on the defence budget. The Pentagon has already agreed to take \$485 billion (U.S.) from its planned spending over the next decade and more cuts could be in the pipe line; especially if Congress cannot strike a long-term budget agreement. Of all the politically difficult budget issues which Mr. Hagel will face, few are more charged than the question of military entitlements which have risen sharply over the last decade. A 2012 report by the Center for Strategic and Budgetary Assessments concluded that at current rates, ‘military personnel costs will consume the entire defence budget by 2039.’ Robert Gates, President Obama’s first defence secretary once warned that these expenses were ‘eating us alive.’ Lawrence Korb, a former assistant secretary of defence during Ronald Reagan’s administration, has commented: ‘It is a perfect storm of rising pensions, salaries and health care costs. At some point we will be faced with making choices between new weapon systems or entitlements.’”

Thursday, January 24th

- Front Page Headline, Bloomberg News – **“Federal Reserve’s Balance Sheet Balloons to a Record \$3 Trillion (U.S.).** During a press briefing, Fed Chairman Ben Bernanke revealed, as result of the central bank’s ongoing quantitative easing program, the Fed’s total assets rose by \$48 billion (U.S.) in the past week to \$3.01 trillion (U.S.) as of January 23rd. Holdings of U.S. Treasuries increased by \$7.8 billion (U.S.) while the portfolio of mortgage-backed securities rose by \$35.6 billion (U.S.). Fed officials have stated their \$85 billion (U.S.) monthly pace of purchases will continue until the domestic labour market improves substantially.
- Markit Economics reports its preliminary U.S. manufacturing Purchasing Managers’ Index rose to a reading of 56.1 in January, following a level of 54.0 in December. Separately, the Labor Department reports U.S. initial claims for state unemployment benefits declined by 5,000 to a seasonally adjusted 330,000 in the week ended January 19th. while continuing claims fell by 71,000 to 3.157 million in the week ended January 12th. Separately, the Conference Board reported its index of leading economic indicators rose by 0.5% in December, following an upwardly revised similar gain in November.
- Front Page Headline, Wall Street Journal – **“Germany’s Commerzbank Announces a Possible 6,000 Layoffs.** According to an internal memorandum to staff, Commerzbank AG – Germany’s second-largest listed bank – plans to lay off between 4,000 and 6,000 employees by 2016. The cuts, representing up to 12% of the bank’s 49,215 full-time staff will affect all group levels and units within Germany and abroad, although online bank Comdirect AG and Polish unit BRE Bank will be exempted.
- The National Statistics Institute reports Spain’s unemployment rate reached 26% in the 4th quarter of 2012, as the economy shed jobs in both the public and private sectors. The higher unemployment rate illustrates how strongly austerity measures are affecting the economy. Aiming to narrow its budget deficit to 4.5% of gross domestic product (GDP) from about 9% of GDP in 2011, the government has raised income and sales taxes, slowed the growth of pension payments and lowered unemployment benefits. Public agencies have also been discarding workers, cutting back purchases and reducing investment levels.

Friday, January 25th

- Front Page Headline, Wall Street Journal – **“Europe’s Banks to Repay ECB Loans Early.** The European Central Bank reports 278 of Europe’s banks will repay 137 billion euros (\$182.2 billion U.S.) of ECB loans on January 30th. – the first day that the 3-year loans can be repaid – and nearly 2 years before the loans are due. This amount represents about 25% of the 489 billion euros that banks had borrowed from the ECB in December 2011. Europe’s banks borrowed an additional 530 billion euros in a second installment of 3-year loans in February 2012, bringing the total to more than 1 trillion euros.”



- The Commerce Department reports U.S. new home sales declined by 7.3% to an annual pace of 369,000 in December, following an upwardly revised 398,000 in November
- The Office for National Statistics reports the U.K. gross domestic product declined by 0.3% in the 4th. quarter of 2012, citing an unwinding from the Olympic Games and a severe drop in oil and gas output
- Front Page Headline, The Economist – “**Canada’s Housing Market Is World’s Most Overvalued.** According to the Economist’s price-to-rents ratio survey, housing overvaluation in Canada registers a whopping 78%, while at the other end of the scale is Japan with an undervaluation of 37%. The Economist reports: ‘Overvaluation is especially marked in Canada, particularly with respect to rents (78%), but also in relation to income (34%) ... Singapore and Hong Kong also look vulnerable to a correction, given the overvaluation on their price-to-rents ratios.’”

The Economist house-price indicators

	Latest, % change		Under(-)/over(+)	
	on a year	since earlier Q4 2007	valued, against*:	
			Rents	Income†
Hong Kong	21.8	86.8	69	na
Austria	10.1	23.3	-13	na
South Africa	5.0	12.2	-5	10
United States	4.3	-20.5	-7	-20
Switzerland	3.6	21.6	nil	-8
Canada	3.3	20.0	78	34
Singapore	2.8	24.1	57	na
Germany	2.7	8.8	-17	-17
Australia	0.3	10.4	45	23
China	-0.5	16.7	7	-35
Britain	-0.9	-11.2	21	12
France	-1.3	2.7	50	35
Sweden	-2.6	8.1	31	18
Japan	-2.6	-14.2	-37	-36
Italy	-4.0	-11.3	-1	12
Ireland	-5.7	-49.4	-1	-5
Netherlands	-6.8	-13.5	17	33
Spain	-9.3	-24.3	19	21

Sources: BIS; Haver Analytics;
Hong Kong RV; Nationwide;
OECD; Teranet and National Bank;
Thomson Reuters; *The Economist*

*Relative to long-run average
†Disposable income per person

CLOSING LEVELS FOR FRIDAY, January 25th		WEEKLY CHANGE
Dow Jones Industrial Average	13,895.98	+ 246.28 points
Spot Gold Bullion (February)	\$1,656.60 (U.S.)	– \$30.40 per oz.
S&P / TSX Composite	12,816.63	+ 90.94 points
10 - Year U.S. Treasury Yield	1.95%	+ 11 basis points
Canadian Dollar	99.35 (U.S.)	– 1.48 cents
U.S. Dollar Index Future (Spot Price)	79.738 cents	– 0.232 cent
WTI Crude Oil (February)	\$95.88 (U.S.)	– \$0.16 per barrel

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