Monday November 11th, 2013

LONGWAVE group

UNDERSTANDING THE LONGWAVE ECONOMIC AND FINANCIAL CYCLE

THAT WAS THE WEEK THAT WAS

Monday, November 11th

Front Page Headline, Bloomberg News – "Fitch Downgrades Chicago's Credit Rating. Fitch Ratings downgrades the City of Chicago's credit rating on $8 billion (U.S.) of general obligation bonds to 'A' (Low) from 'AA' (Low), citing unfunded public sector pen-

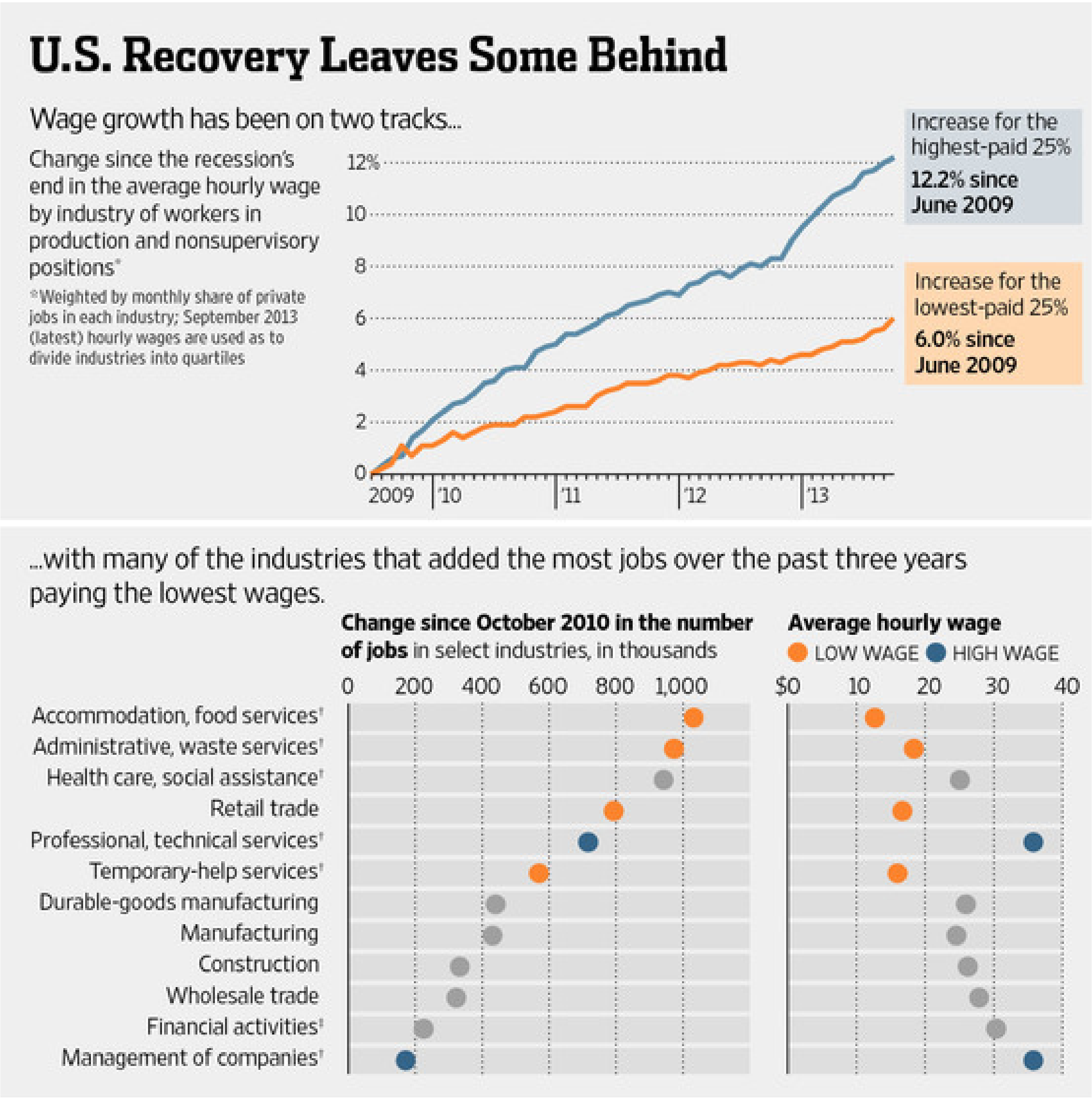
MONDAY, NOVEMBER 11TH
Remembrance Day Holiday in Canada / Veterans' Day in USA

sions as a major issue. Chicago, a city of about 2.7 million residents, is projecting a budget deficit of as much as $1 billion (U.S.) in fiscal 2015, unless the Illinois legislature restructures the public pension system, which is a state creation. Unsurprisingly, Illinois lawmakers adjourned their fall session yesterday without taking any action."

- Front Page Headline, Wall Street Journal – "Major U.S. Cities Still Not Recovered from Financial Crisis. In a new study, the Pew Charitable Trusts – an Iowa-based non-profit research firm reports: 'Beyond the shaky revenue picture, some cities' long-term obligations threaten their near-term and long-term finances. The annual cost of retirement benefits continues to rise, particularly in cities severely underfunded retiree pension and health care obligations."

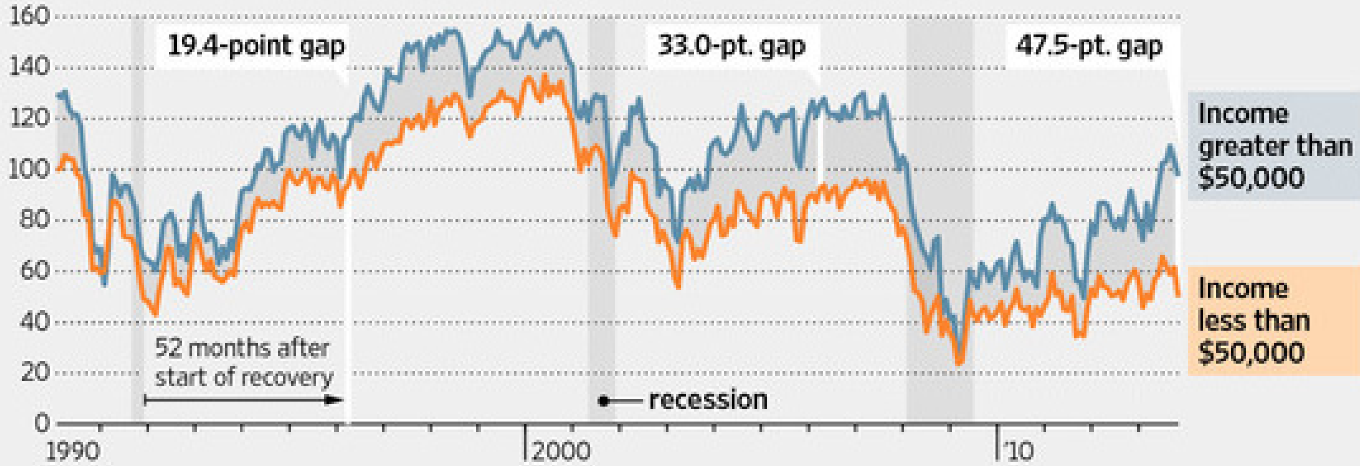
- Front Page Headline, Wall Street Journal – "U.S. Job Gap Widens in Uneven Economic Recovery. America's employment recovery is proceeding on two separate tracks in a pattern that is persisting far longer than after past economic rebounds and lately has been growing worse. Despite three years of steady job gains and four years of economic growth, many Americans have yet to experience much that could be described as a financial recovery. In the aftermath of a recession, that sort of employment pattern isn't unusual, but it usually eases as economic growth improves. For example, youth unemployment nearly always improves after recessions more slowly than that of prime age workers, those between 25 and 54. Following the 2001 recession, it took six months for the gap between the youth and prime age unemployment rates to return to its long run average. After the early 1990s recession, it took 30 months.

This time it has been 52 months and the gap has hardly narrowed. For those with decent jobs, wages are rising, albeit slowly and job security is the strongest it has been since prior to the recession. Many families have paid down debts and are seeing the value of assets – from homes to stocks – rebound strongly. However, many others – the young, the less educated and particularly the unemployed – are experiencing hardly any financial recovery at all. Hiring remains weak and the jobs which are available are disproportionately low-paying and often only part-time. Wage growth is nearly nonexistent, partly because with so many workers still looking for jobs, people have little bargaining power. Harry Holzer, a professor of public policy at Georgetown University who has studied low-wage jobs, concludes: 'It's not only more difficult to get a job, but also more difficult to land a good job. Today, companies are more willing to create jobs if they're low-paying, carry minimal benefits and require a minor security commitment."


U.S. Recovery Leaves Some Behind
Wage growth has been on two tracks...
Change since the recession's end in the average hourly wage by industry of workers in production and nonsupervisory positions*
*Weighted by monthly share of private jobs in each industry; September 2013 (latest) hourly wages are used as to divide industries into quartiles
12%
10
8
6
4
2
0
2009
'10
'11
'12
'13
Increase for the highest-paid 25%
12.2% since June 2009
Increase for the lowest-paid 25%
6.0% since June 2009
...with many of the industries that added the most jobs over the past three years paying the lowest wages.
Change since October 2010 in the number of jobs in select industries, in thousands
0
200
400
600
800
1,000
Average hourly wage
LOW WAGE
HIGH WAGE
$0
10
20
30
40
Accommodation, food services†
Administrative, waste services†
Health care, social assistance†
Retail trade
Professional, technical services†
Temporary-help services†
Durable-goods manufacturing
Manufacturing
Construction
Wholesale trade
Financial activities†
Management of companies†

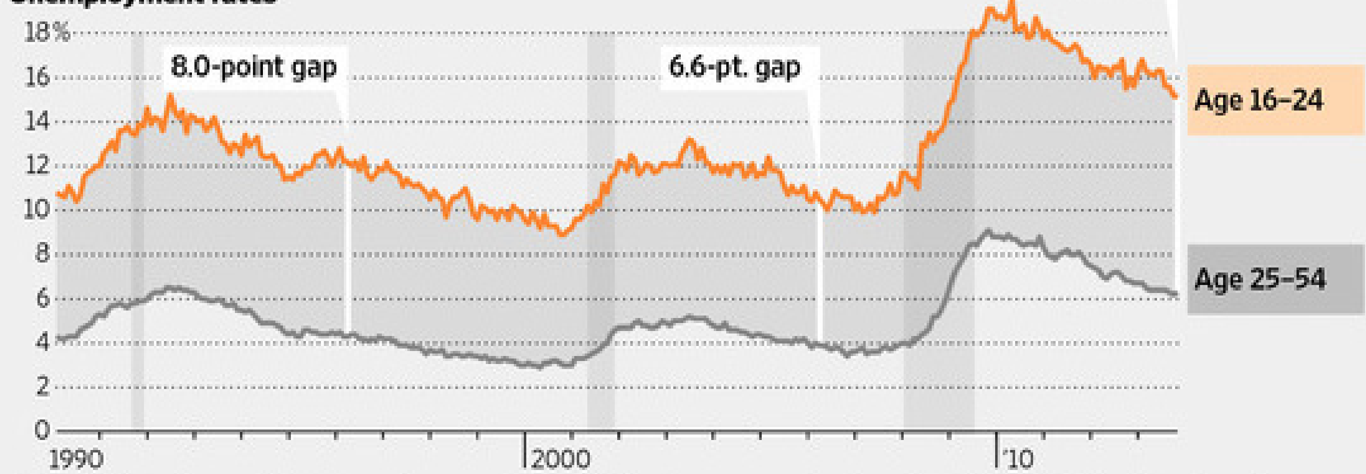
There's also a widening confidence gap between higher- and lower-income households...

Indexes of consumer confidence, and the gap at this point in each recovery



...and stubbornly high joblessness, especially among the young.

Unemployment rates



†Wage data flagged are as of September; other wage data as of October; temporary services is a subset of administrative and waste services.
‡Finance, insurance and real estate Note: Data are seasonally adjusted.

Sources: Labor Department (job and wage data); RBC Capital Markets (confidence)

Ben Casselman (analysis of wage growth by quartiles) and Pat Minczeski/The Wall Street Journal

TUESDAY, NOVEMBER 12TH

- The Office for National Statistics reports the U.K. inflation rate rose by 2.2% in October on a year-over-year basis, down from a 2.7% annualized rate in September. Rob Carnell, an economist at ING Bank NV in London, commented: "The inflation figures are helpful, but they're not by any stretch suggesting that we need to embark upon another round of monetary policy easing. The inflation picture is much worse in the U.K. than it is in Europe. Today's inflation report may be just a flash in the pan."

- At an Edmonton, Alberta press conference, Canada's Finance Minister Jim Flaherty informed reporters that the federal government will post a surplus of $3.7 billion (CAD) in the fiscal year ending March 31, 2016: "While slower economic growth will reduce the government's projected revenue by $10.4 billion (CAD) over the next five years, it now plans to spend $14.4 billion (CAD) less over the same period than earlier forecast. Freezing government operating budgets from April 1st.will save a further $5.2 billion (CAD) over five years. My preference is to reduce public debt, because I just don't believe in public debt."

Bank of Canada Governor Stephen Poloz (L) and Cdn. Finance Minister Jim Flaherty. Source: Bloomberg

- Front Page Headline, Globe and Mail – "Despite Stimulus Measures, Global Economy Faces Risk of Deflation. Inflation is retreating across the developed world, increasing the possibility that an extraordinary era of monetary policy will be extended as central banks struggle to attain their inflation targets. A report from the Office for National Statistics (see above) revealed that consumer prices in Britain rose by 2.2% in October from a year earlier, a sharp deceleration from the September rate of 2.7%. Swedish prices actually contracted in October from September, dropping the annual rate as measured by the central bank's preferred price gauge to 0.6% from 0.9%. These figures were the most recent reminder that global economic growth continues to disappoint. Unemployment is elevated and industrial capacity remains idle. Those conditions introduce slack into an economy and put downward pressure on prices. Weaker inflation raises the threat of price contractions, which if they were to persist, could have a corrosive effect on any economy so afflicted … Last week the European Central Bank (ECB) cut its benchmark lending rate to a record low 0.25% after inflation in the euro zone declined to 0.7%; far from the ECB's price stability target of about 2%. In Japan, inflation is at zero and in the United States, inflation is stagnant at a rate of about 1%."

WEDNESDAY, NOVEMBER 13TH

- Eurostat reports euro zone factory output declined by 0.5% in September, citing production dropped in every sector but energy, signaling the region's economic recovery remains fragile at best. Output of durable consumer goods, such as cars and electronics, was down by 2.6% on the month, while in the highly volatile energy sector, output rose by 1.3%. Production in Europe's two biggest economies, Germany and France, declined in September, while Italy returned to economic growth following two months of consecutive declines and Spain's output expanded for a third month in a row. Peter Vanden Houte, an economist at ING, commented: "We don't think that today's reports cast doubt over the economic recovery in Europe, but it certainly shows that (GDP) growth remains stuck in first gear. The weakness of the (economic) upturn means that not much is needed to arrest it."

- Front Page Headline, New York Times – "German Economic Policy Beset by Domestic Criticism. Not only is criticism coming from European Union (EU) officials in Brussels, warning that Germany's huge trade surplus is threatening the competitiveness of the rest of the bloc, but also, from the German Council of Economic Experts; a panel of leading economists who advise the government. In its annual report on the domestic economy, the council noted: 'Germany has failed to follow the advice it has given to other countries, putting its own future (economic) growth in jeopardy as the population ages and the percentage of retired people increases. Political leaders should invest more in education and continue to deregulate the labour market, by reducing restrictions on temporary labour. Forward-looking economic policy is necessary to strengthen Germany's economic growth and to ensure the viability of public finances and the social security systems. The German government should not give the impression that it expects – or even demands – painful adjustment processes from other countries, but shies away from unpopular measures for Germany."

THURSDAY, NOVEMBER 14TH

- Front Page Headline, Bloomberg News – "Moody's Downgrades Credit Ratings of Four U.S. Banks. Moody's Investors Service has downgraded the credit ratings on four of the biggest American banks, including Morgan Stanley, Goldman Sachs Group, JP Morgan Chase and Bank of New York Mellon, after concluding that the U.S. government would be less likely to assist them repay creditors during a financial crisis. In a prepared announcement, Robert Young, a managing director at Moody's stated: 'We believe that U.S. bank regulators have made substantive progress in establishing a credible framework to resolve a large, failing bank. Rather than relying upon public funds to bail out one of these institutions, we expect bank holding company creditors will be bailed in and thereby, shoulder much of the burden to help recapitalize a failing bank.' Accordingly, Bank of New York Mellon was cut from A1 to Aa3; Goldman Sachs was lowered to Baa1from A3; JP Morgan Chase was cut to A3 from A2 and Morgan Stanley was downgraded to Baa2 from Baa1."

- The Labor Department reports U.S. initial claims for state unemployment benefits declined by 2,000 to a seasonally adjusted 339,000 in the week ended November 9th. while continuing claims – those drawn by workers for more than a week – was unchanged at 2.874 million in the week ended November 2nd.

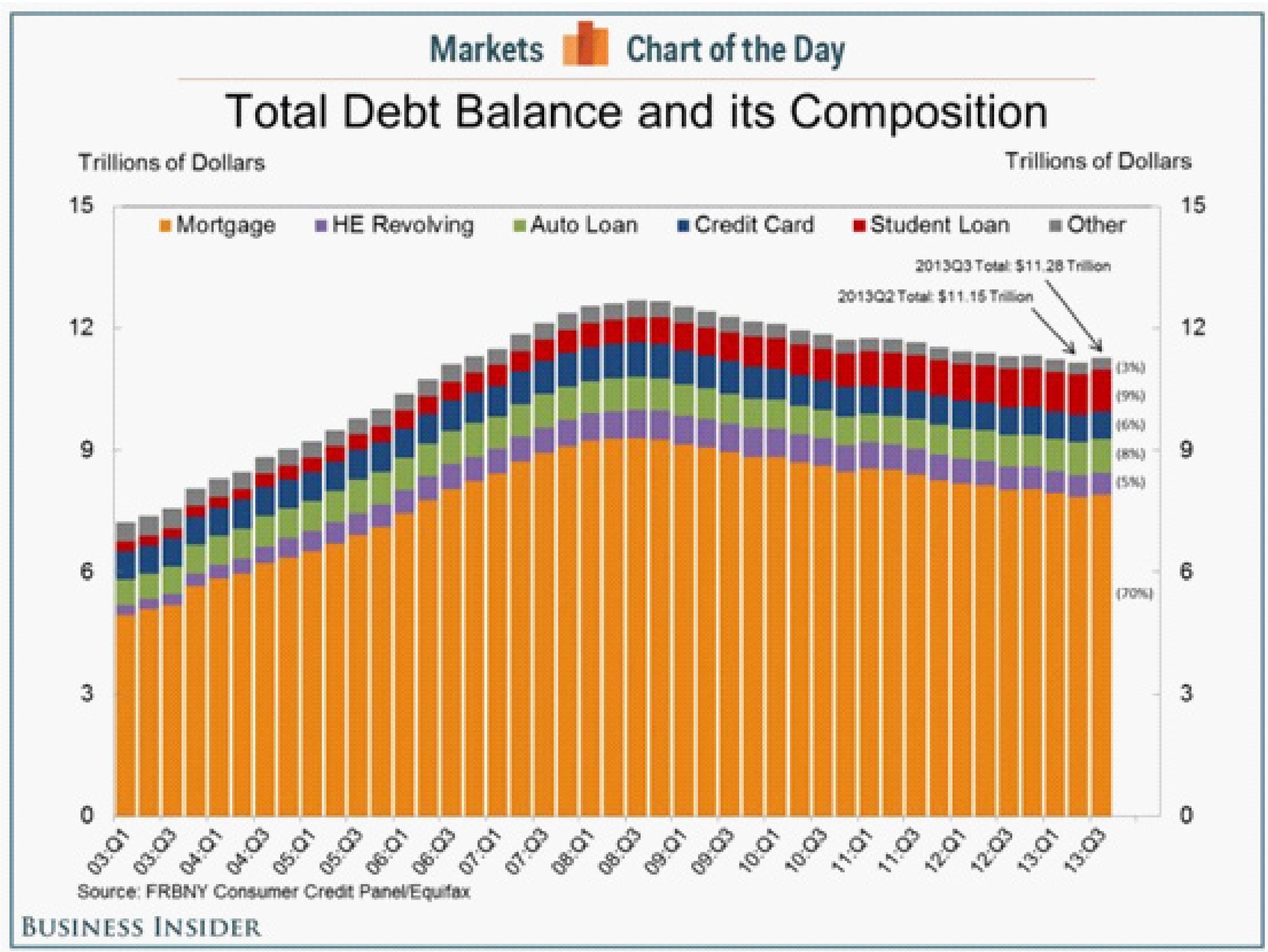
- Front Page Headline, Wall Street Journal – "In testimony at a confirmation hearing before the Senate Banking Committee, Janet Yellen, the White House nominee to become chairperson of the U.S. Federal Reserve in January, stated: 'I would abide by plans to decelerate the Fed's $85 billion (U.S.) monthly quantitative easing program in the coming months if the economy improves (sufficiently). At each Federal Open market Committee (FOMC) meeting, Fed officials are trying to decide whether the moment is right to begin trimming the bond purchases. There is no set time."

U.S. Federal Reserve Vice Chairwoman Janet Yellen. Source: Associated Press

- Front Page Headline, Financial Times – "Hopes Dashed for Higher Global Economic Growth. Disappointing gross domestic product (GDP) figures in the euro zone and Japan – driven by weak export numbers – have dashed hopes that a global economic recovery would gather pace in the second half of the year. Economic growth faltered in the third quarter, expanding by only 0.1%, following GDP growth of 0.3% in the second quarter. Jonathan Loynes, an economist at Capital Economics observed: 'The near stagnation of the euro zone economy underlines the fragility of the economic recovery and the growing dangers of a damaging bout of deflation in the region.' Meanwhile in Japan, the rate of GDP growth roughly halved to an annualized rate of 1.9% in the 3rd. quarter as weaker (domestic) consumption and exports offset increases in public spending and property investment. Weaker Japanese economic growth than expected, despite a lower yen, added to concerns about the effectiveness of Prime Minister Shinzo Abe's drive to revive the world's third largest economy.

- Front Page Headline, Business Insider – "Chart of the Day: American Household Debt Reaches $11.28 trillion (U.S.). In its latest Quarterly Report on Household Debt and Credit, the Federal Reserve Bank of New York discloses: 'In the 3rd. quarter, American household indebtedness increased to $11.28 trillion (U.S.); 1.1% higher than the previous quarter. Overall consumer debt remains 11% below the peak (level) of $12.68 trillion (U.S.) registered in the 3rd. quarter of 2008.' In a press release, New York Fed economist Donghoon Lee noted: 'In the 3rd. quarter, essentially, we observed an increase of household balances across all types of debt. With non-housing debt consistently increasing and the factors forcing down mortgage balances waning, it appears that U.S. households have reached a turning point in the deleveraging cycle.' Outlined below are several highlights from the New York Fed report in U.S. dollars.

  1. Student loan balances on credit reports rose by $33 billion to 1.03 trillion.
  2. Auto loan balances rose for the 10th. consecutive quarter; up $31 billion to $845 billion
  3. Credit card balances increased by $4 billion to $672 billion
  4. Total mortgage debt increased to $7.9 trillion, up $56 billion
  5. HELOC balances declined by $5 billion to $535 billion
  6. Mortgage originations fell slightly to $549 billion
  7. 168,000 individuals had new foreclosure notations added to their credit reports; 70% below the peak (level) of 566,000 in the 2nd. quarter of 2009



- Front Page Headline, Armstrong Economics – "Another Municipal Bankruptcy. The City of Desert Hot Springs, California, has announced that, due to burdensome salary and pension costs, it may soon seek court bankruptcy protection since it will likely have exhausted its revenues by March 2014. A bankruptcy filing by Desert Hot Springs, a city of 26,000 about 110 miles east of Los Angeles, would mark the third California city – together with Stockton and San Bernardino – to seek court protection from creditors. The problems in Desert Hot Springs surfaced last week when a new finance director reviewed the city's records and discovered a $3 million (U.S.) shortfall in its (annual) budget of $13.5 million (U.S.). Amy Aguer, the interim finance director, did not possess details about how the shortfall occurred, but commented that it was a result of higher-than-expected salary and pension costs – especially with respect to the police department, plus overly optimistic estimates of revenue. Russell Betts, a city council member, noted: 'It's obvious that we can't continue with salaries and pensions that are in the stratosphere, no matter how much love there exists for our police department."

The City of Desert Hot Springs Police Station.
Source: WordPress

FRIDAY, NOVEMBER 15TH

- Front Page Headline, Wall Street Journal – "JP Morgan Chase Reaches $4.5 billion (U.S.) Settlement with Institutional Investors. Separate and distinct from the bank's talks with the U.S. Justice Department, JP Morgan Chase has agreed to pay $4.5 billion (U.S.) to 21 institutional investors seeking to recover losses from mortgage-backed securities marketed prior to the 2008 financial crisis. The group of institutional investors includes such high profile names as Blackrock Inc. and Pacific Investment Management (Pimco). The new agreement means JP Morgan faces a total bill of nearly $20 billion (U.S.) to settle an array of recent mortgage related lawsuits and investigations. In October, the bank agreed to $5.1 billion (U.S.) in settlements with government owned mortgage finance companies Fannie Mae and Freddie Mac and it currently negotiating a final agreement with the U.S. Justice Department which could surpass another $9 billion (U.S.) in additional new penalties and damages."

- Front Page Headline, Wall Street Journal – "Under New Owners, Heinz to Trim Factories and Jobs. H.J. Heinz Co.'s new owners announced further staff cuts at the storied ketchup maker, stating it would close three factories in North America over the next six to eight months and eliminate 1,350 jobs. The factory closures announced for South Carolina, Idaho and Canada are in addition to 600 corporate layoffs unveiled in August; two months after the Brazilian private equity firm 3G Capital partnered with Warren Buffet's Berkshire Hathaway Inc. to acquire the Pittsburg-based company for $28 billion (U.S.). Heinz announced: 'The latest moves are aimed at consolidating our North American manufacturing facilities to ensure that we are operating as efficiently and effectively as possible to become more competitive in a challenging environment."

- Front Page Headline, New York Times – "Extension of Unemployment Benefits Deemed Unlikely. Unless Congress grants an extension by the end of December, an estimated 1.3 million people will lose access to an emergency program providing them with additional weeks of unemployment benefits. A further 850,000 people could be denied benefits in the first quarter of 2014. Noting the sluggish economic recovery and the continuing high unemployment rate, Congressional Democrats and the White House are pushing once again to extend the period covered by the unemployment insurance program. However, with Congress far from a budget agreement and still struggling to find alternatives to the $1 trillion (U.S.) in long-term spending cuts known as sequestration, lawmakers say the chance of an extension before Congress adjourns in two weeks are slim. As a result, one of the largest stimulus measures passed during the recession is likely to expire and unemployed workers in many states would receive considerable fewer weeks of benefits. In an interview, Gene Sperling, President Obama's top economic advisor, estimated that in total, as many as 4.8 million people could be affected by expiring unemployment benefits through 2014: 'Historically, there has not been a time when the unemployment rate has been this high that benefits have not been extended. Why would Congress not extend now, when we're dealing with nearly unprecedented levels of long-term unemployment following such an historic recession?"

- Front Page Headline, Financial Times – "Euro Bank Regulator Attacks Unwieldy Governance. In an interview with the Financial Times, Andrea Enria, chairman of the European Banking Authority (EBA) warned: 'The benefits of crucial bank stress tests to take place over the next year could be impaired, if decision making is not streamlined and nationalist tendencies are not contained. The EBA must move away from consensus-based governance traditions. We need European decision mechanisms rather than always having a committee style decision in a crisis. Committees in a time of crisis don't work because they have conflicts.' The EBA is embarking upon a comprehensive stress test exercise of Europe's top 150 banks in an another attempt by the European authorities to repair battered investor confidence in the sector; following a succession of bank and regulatory failures amid the euro zone debt crisis. In tandem with an 'asset quality review' of euro zone lenders by the European Central Bank (ECB), the exercise is designed to shine unprecedented light on banks' balance sheets. The results, due to be revealed in a year's time, will usher in the creation of the euro zone's banking union, with the ECB becoming the region's chief regulator and a new resolution framework created to wind down failing banks. However, Mr. Enria clearly remains frustrated that the structure of his pan-EU regulator – which depends upon an unwieldy committee of representatives from the EU's 28 member states – will hamper ongoing efforts to maintain a stable and credible financial sector. 'We are given 24 hours to do mediation (in a bank resolution) and we are given a governance (structure) which is impossible. They give us responsibilities, but they put so many national safeguards on every task we need to do, that sometimes I am concerned we will not be able to perform them."

- Front Page Headline, Financial Times – "The Wrong Battle for the Climate. In a Financial Times editorial commentary, the editors conclude that the U.S. should approve the Keystone XL pipeline. The proposed Keystone XL oil pipeline from the Province of Alberta, Canada to the United States has become the Stalingrad of the American environmental movement. Of limited strategic importance in itself, the pipeline has been furiously contested because of its symbolic value to both sides. After more than five years of (debating and negotiating), it is time for the Obama administration to bring the (controversy) to an end. For opponents of Keystone XL, blocking the pipeline curtails the development of Canada's oil sands, which threatens to have a catastrophic effect on global warming. For the oil industry, the pipeline is essential to realizing the full potential of the North American oil boom and safeguarding American energy security.

Neither side's arguments support much scrutiny. The environmentalists are right that extracting heavy oil from the sands creates more greenhouse gas emissions than crude (oil) from some other sources. However, if Keystone XL were blocked, U.S. refineries would use heavy crude oil from other sources that also possess higher emissions. Nor are the project's opponents right that if they block the pipeline, they can prevent oil from the sands from coming onto the market. New investments in train loading facilities and tanker cars will enable increased volumes of heavy oil to be carried by rail. There are also other pipeline proposals, including the plan Energy East route to refineries and export terminals in eastern Canada.

Those plans also expose the hyperbole from the industry about how badly Keystone XL is needed. Other options may be more expensive, but they are perfectively viable. As for energy security, Canada's oil sands have become a sideshow compared to the spectacular developments in U.S. shale production. Keystone XL would carry very little of that new U.S. crude. The above notwithstanding, the pipeline would create tens of thousands of jobs while under construction, ease the paths to U.S. markets for oil from a friendly neighbour and provide a transport route with less risk of serious risks than rail. These benefits set against a marginal long-term difference to U.S. gas emissions mean the Obama administration should approve the project when it decides to make a decision in early 2014. Climate change is a genuine threat and a price on carbon is the right way to address it. Failing that, regulations such as fuel economy standards, the administration's proposed limits from power generation, can play a role. Keystone XL, however, is not the battle to fight." At Longwave Analytics, while Canadians can only apologize on behalf of the Almighty that He deposited vast crude oil resources in the form of oil sands in Alberta, instead of Olympic pool-sized, rock-encased, light sweet crude oil; but it still begs the question to America: Do you want the crude oil or not? Rather, Canada should just expand its export horizons to the Far East and the near east.

CLOSING LEVELS FOR FRIDAY NOVEMBER 15TH.		Weekly Change
Dow Jones Industrial Average	15,961.70	+ 199.92 points
Spot Gold Bullion	$1,287.40 (U.S.)	+ $2.80 per oz.
S&P / TSX Composite	13,482.57	+ 104.24 points
10 – Year U.S. Treasury Yield	2.70%	– 5 basis points
Canadian Dollar	95.72 cents (U.S.)	+ 0.28 cent
U.S.Dollar Index Future	80.810	– 0.396 cent
WTI crude Oil Futures	$93.84 (U.S.)	– $0.76 per barrel

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