

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



Monday, September 2nd
• Front Page Headline, Wall Street Journal – “Chinese House Prices Outpace Construction.”

Monday, September 2nd

Labour Day Holiday in Canada and the United States

The China Real Estate Index System (CREIS) reports house prices nationwide climbed by 8.6% on a year-over-year basis in August. This maintains the momentum of rising house prices which commenced late in 2012, as Beijing began relaxing controls on the property market in order to boost economic growth. While CREIS reported house prices are up by 22.5% in Beijing and by 22.4% in Guangzhou—on a year-over-year basis—other cities are experiencing more modest increases, with prices in Shanghai up by 7.7%.”

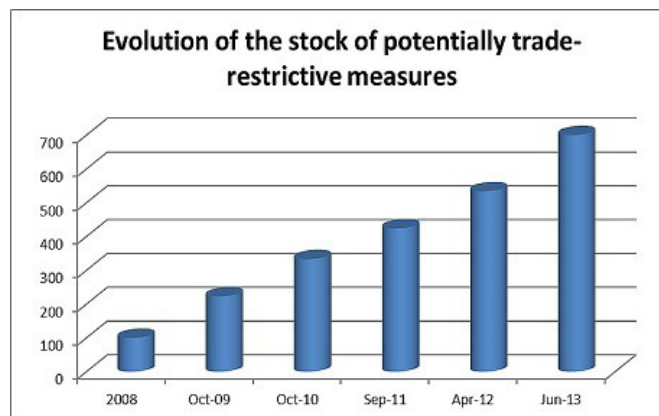


- In the United Kingdom, the purchasing managers' index for the manufacturing industry—compiled by data from Markit Economics and the Chartered Institute of Purchasing and Supply (CIPS)—rose to a reading of 57.2 in August from a level of 54.8 in July, to attain its highest level since February 2011.

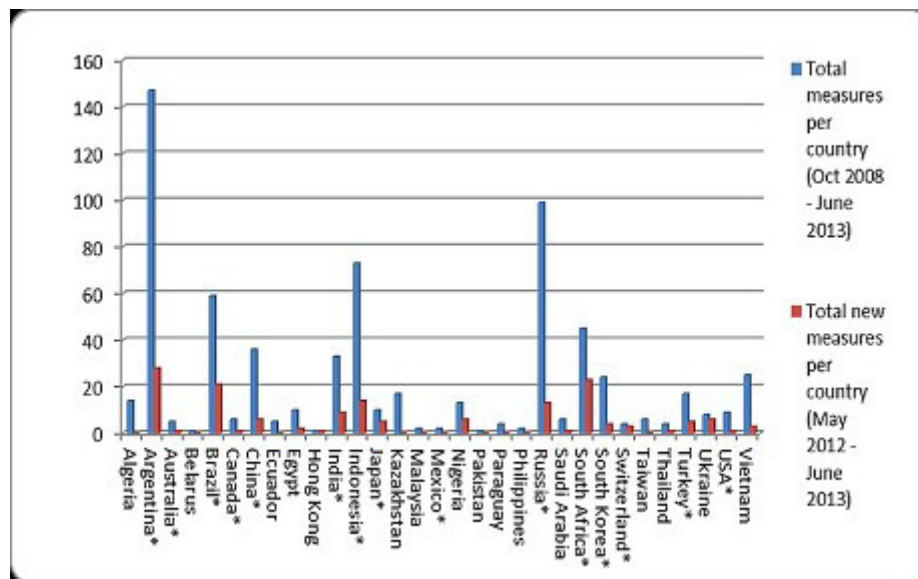
- Markit Economics reports the 17-nation euro zone purchasing managers' index for the manufacturing sector rose to a reading of 51.4 in August, following a level of 50.3 in July. While factory activity growth resumed in Spain following more than two years of decline, Italy, Ireland, Austria, Germany and the Netherlands also experienced some growth.



- Front Page Headline, Daily Telegraph U.K. – **“Europe Fears Uncontrolled Protectionism As Emerging Markets Reject Free Trade.** In a new study of world trade, the European Commission (EC) reports the initiative by several states to unravel the World Trade Organization structure is alarming: ‘Such practices should be strongly condemned, since their potential proliferation could risk and even nullify the entire global agreement of rules governing trade, thereby opening the door to blatant and uncontrolled protectionism.’ The EC study cited 154 new trade tariffs and restrictive trade measures which have been adopted within the past year, while virtually none has been abolished. This violates a promise by the G20 bloc of leading economies to dismantle trade barriers before they become embedded in the global system. European Union (EU) trade commissioner Karel de Gucht observed: ‘It is a striking phenomenon. More than ever, looming protectionism is now a significant threat to global economic growth. It is high time for the G20 pledge to be enforced in full.’ The EC has catalogued several abuses noting Argentina, Brazil, India, Russia, Indonesia and South Africa as top offenders over the past year. (See U.K. Telegraph charts below and on following page).”



Countries are using every trick to keep goods and services imports down, going far beyond tariffs and fees. These include licensing barriers, technical regulations, procurement rules and internal stimulus measures which distort competition. The EC study notes many forms of protectionism are difficult to police: 'These measures are often applied without a pre-warning for businesses. Whole consignments of goods become blocked in customs entry points and warehouses. Perishable products can often completely lose their market value in the process.'



Neil Shearing, an analyst with Capital Economics, commented: 'The G20 is unlikely to make any breakthrough on world trade. While the bloc controls 85% of global gross domestic product (GDP), it is a dysfunctional club; with no permanent staff and deeply conflicting views.'

Tuesday, September 3rd

- The Tempe, Arizona-based Institute for Supply Management reports its U.S. manufacturing index rose to a reading of 55.7 in August—the highest since June 2011—from a level of 55.4 in July, citing higher demand for automobiles, furniture, appliances and building materials.
- The Commerce Department reports U.S. construction spending rose by 0.6% in July to a \$900.8 billion (U.S.) annual rate, the highest since June 2009.
- Front Page Headline, New York Times – **“Federal Budget Battles Keep U.S. Agencies Guessing.** The collision if the \$1 trillion (U.S.) in federal budget cuts—known as sequestration—and the breakdown of the traditional budgeting process is creating anxieties, not only in Washington, but also, for a vast web of agencies that are dependent upon federal financing. Many offices are uncertain about how much money—if any—they will receive for fiscal 2014 which begins on October 1st. Among others, the budget woes are afflicting state governments, native American tribes, military contractors and cancer research laboratories. Budget experts note that the short-term funding concerns are also hampering long-term plans and making government officials reluctant to either commit to big projects, or hire needed employees. In an interview, Dr. Francis Collins, the Director of the National Institute of Health, cited 2013 as the darkest year ever for his agency, whose budget is at its lowest inflation-adjusted appropriations level in more than a decade. Dr. Collins noted: 'The stopgap measures which have kept the federal government operating have further hobbled the agency. Continuing resolutions discourage people from trying something new and bold.'

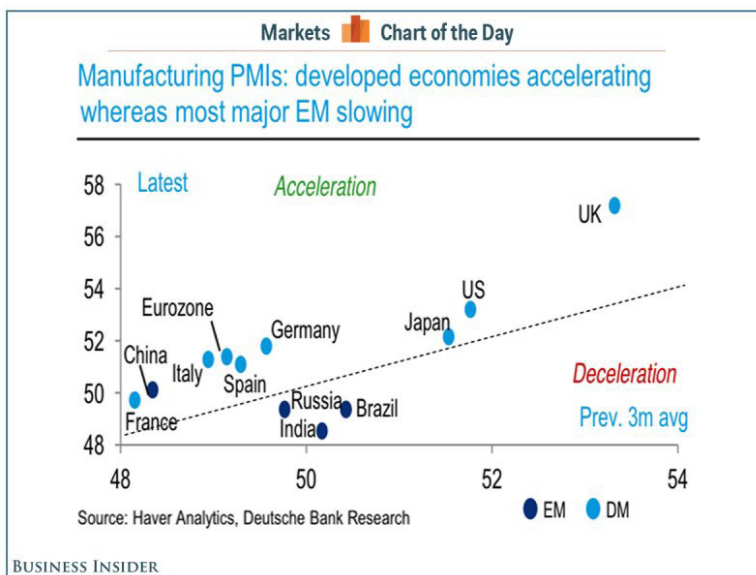
One is supposed to tread water and science is very badly served by that message.’ A number of U.S. budget issues have lingered unresolved during Congress’ long summer recess. Earlier this year, the House and Senate passed spending bills for fiscal 2014 that differed by about \$90 billion (U.S.), but never settled on a final figure. With lawmakers returning to Washington next week, Congress is expected to pass another stopgap bill—known as a continuing resolution—financing the federal government for a few more months, but it is unclear whether such funding will remain at current levels or decline. If the Republicans and the Democrats, who control the House and Senate, respectively, fail to reach a budget agreement this month, many areas of the federal government could close down on October 1st.”



Dr. Francis Collins with U.S. President Barack Obama

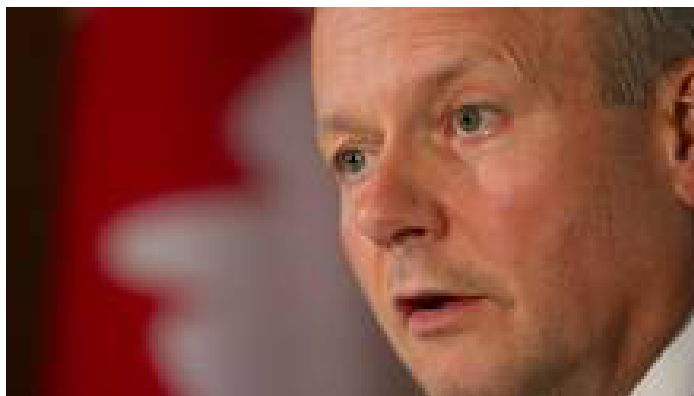
Source: Agence France Press – Getty Images

- Front Page Headline, Mish’s Global Economic Trend Analysis – **“India in Serious Trouble.** Last Thursday, India’s trade minister, Anand Sharma, suggested the Reserve Bank of India (RBI) should consider the possibility of monetizing gold holdings; in the latest proposal aimed at combatting a gaping current account deficit which has hammered the rupee. While the RBI holds 557.7 tonnes of gold in its own reserves, India has the world’s third largest current account deficit which is approaching \$90 billion (U.S.). In comments published in The Hindu newspaper last week, David Gornall, chairman of the London Bullion Market Association, stated India could raise \$23 billion (U.S.) by swapping gold for a payable currency over a period of its choice, while remaining the long-term holder of the gold. I am not certain which is the more ridiculous: proposing the sale of gold outright, or proposing India could obtain \$23 billion (U.S.) in free money by swapping gold while retaining ownership.”
- Front Page Headline, Business Insider – **“The State of the World Economy.** Deutsche Bank has just published a chart showing how countries have been performing recently, according to their newly released August purchasing managers’ index reports. Any country plotted above the dotted line is improving at an accelerating pace. Outlined below are four key points from the Deutsche Bank chart:
 1. Positive momentum with data on an improving trajectory across key economic regions, excepting emerging markets.
 2. Emerging markets: Data weakness due to country-specific structural challenges and liquidity concerns driven by U.S. Federal Reserve QE tapering speculation.
 3. Euro zone: Positive 2nd. quarter economic growth marking an end to the longest recession in the region’s history.
 4. China: Economic slowdown fears reduced on improving recent data.



Wednesday, September 4th

- The Commerce Department reports America’s trade deficit widened by 13.3% to \$39.1 billion (U.S.) in July from a revised \$34.5 billion (U.S.) in June—previously reported as \$34.2 billion (U.S.)—citing higher imports of crude oil and record imports of automobiles. Joshua Dennerlein, an economist at Bank of America in New York, noted: “Looking ahead, imports are probably going to grow at a faster pace than exports, reflecting an increase in domestic demand.”
- Statistics Canada reports the nation’s merchandise trade deficit more than doubled to \$931 million (CAD) in July from \$460 million (CAD) in June, citing a 0.6% increase in imports and a decline in exports by a similar percentage. Among the higher volume of imports were industrial chemicals, metal ores and non-metallic mineral products, plastic and rubber products.
- Front Page Headline, Globe and Mail – **“Bank of Canada Leaves Bank Rate Unchanged at 1%.** In a statement following the central bank’s monthly Monetary Policy Committee meeting in Ottawa, Bank of Canada Governor Stephen Poloz reported that the Bank Rate would remain unchanged at 1% since: ‘uncertain global economic conditions appear to be delaying the anticipated rotation of demand in Canada towards exports and investment.’ In a research note to clients, Bank of Montreal chief economist Douglas Porter stated: ‘The bottom line is that we are still looking at a very long period of inactivity by the Bank of Canada and (we) may well be talking about four years of unchanged (administered interest) rates a year from now.’”



Bank of Canada Governor Stephen Poloz.

Source: Globe and Mail

- Ford Motor Co. of Canada reports it retained the top spot for Canadian vehicle sales in August with a 7% gain on a year-over-year basis to 199,156 cars, trucks and utility vehicles in the first eight months of the year; up from 195,582 in the same period of 2012. Meanwhile, Chrysler Canada reported passenger car sales increased by 20% on a year-over-year basis in August, with calendar year-to-date sales totaling 36,761.
- Front Page Headline, Financial Times – **“EU Drafts Law to Regulate Shadow Banking.** At a Brussels press conference, Michel Barnier—the European Union Commissioner for Internal Market and Services—announces regulations for euro zone money market funds which force big corporations to stockpile liquid assets and when offering a guaranteed stock price to investors, build capital buffers to avert investor panic runs. In reference to constant net asset value funds—which typically offer investors a stable one dollar or one euro redemption price, Mr. Barnier elaborated: ‘We believe this is something that is important for our economy. I prioritized security and safety rather than legislate a formal and brutal ban against them.’ An outright ban would hit Ireland and Luxembourg registered funds managing some 480 billion euros and force them to move to variable share prices. Such a move was recommended last year by central bankers and regulators on the European Systemic Risk Board, which monitors financial risk across the bloc. When a prominent U.S. fund ‘broke the buck’ during the financial crisis in 2008, it was followed by a wave of withdrawals across the industry and heavy government intervention to restore confidence.”



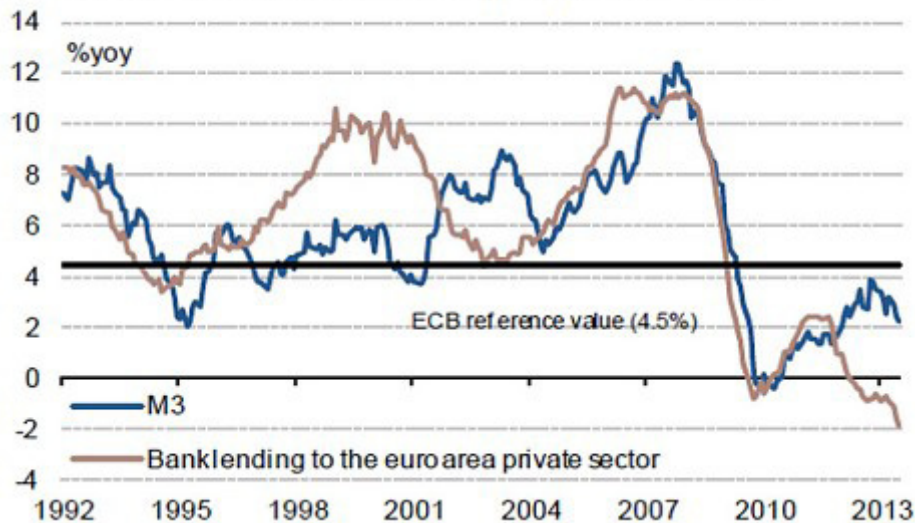
EU Commissioner Michel Barnier

Source: European Press Association

- Front Page Headline, Daily Telegraph U.K. – **“U.S. Government’s \$5 billion Lawsuit Is Revenge for AAA Rating Downgrade: S&P.** The U.S. Department of Justice (DOJ) is suing Standard and Poors—America’s largest credit rating agency—for allegedly misleading banks about the (inherent) risk of certain (mortgage-backed) debt securities in the period leading to the 2008 financial crisis, in order to boost the fees it could claim. While other major credit ratings agencies also afforded the so called collateralized debt obligations (CDO) high ratings at the time, S&P is the only one being taken to court by the DOJ. Yesterday, the credit ratings agency accused the DOJ of pursuing an ‘impermissibly selective, punitive and meritless lawsuit in retaliation’ for its decision to exercise ‘free speech rights with respect to the creditworthiness of the United States of America.’ S&P controversially downgraded America’s AAA (sovereign debt) credit rating to AA (High) in 2011. The case continues.”
- Front Page Headline, Daily Telegraph U.K. – **“Multiple Shocks Threaten Europe’s Sickly and Deformed Economic Recovery.** In an op-ed, International Business Editor Ambrose Evans-Pritchard asserts: ‘Europe has not recovered economically. It has begun to stabilize, but only just, amid mass unemployment and debt trajectories still spiraling out of control in Italy, Portugal, Spain and once again in Greece. The complacency of those dictating the euro zone’s policies—though not its victims—is breathtaking. Simon Tilford, at the Centre for European Reform, cites: ‘It seems that Europe has become anesthetized to bad news. The reality is that the Spanish and Italian economies will contract by a further 2% in 2013. Greece is on course to contract by an additional 5% to 7% and Portugal by 3% to 4%. Far from being on the mend, the economic crisis across the south is deepening. Real interest rates are increasing from already high levels. The elephant in the room is the increase in the debts of Portugal and Spain by 15 percentage points of gross domestic product (GDP) over the last year, by 18 percentage points in Ireland and by 24 percentage points in Greece. Italy’s ratio rose by 7 percentage points to 130% of GDP, already at or near the point of no return.’

An end to the (economic) slump—hardly assured—is not enough to reverse a compound interest trap across the euro zone as debt loads rise faster than nominal GDP, or enough to render Italy and Spain vulnerable within the European Monetary Union (EMU)—such is the denominator effect.

Euro area M3 and bank lending to private sector



Source: U.K. Telegraph

This is the fruit of naked austerity, conducted without offsetting monetary stimulus. Debt (to GDP) ratios are rising even faster. The hair shirt strategy has been self-defeating even on its own terms. The debt spiral cannot be checked until the euro zone embarks upon full-blown reflation, yet EMU creditors shun such a course. Moreover, euro zone states have yet to discover a leader of stature, willing to forge a debtors' cartel and bargain from strength. Rather, they allow themselves to be picked off one by one."

Thursday, September 5th

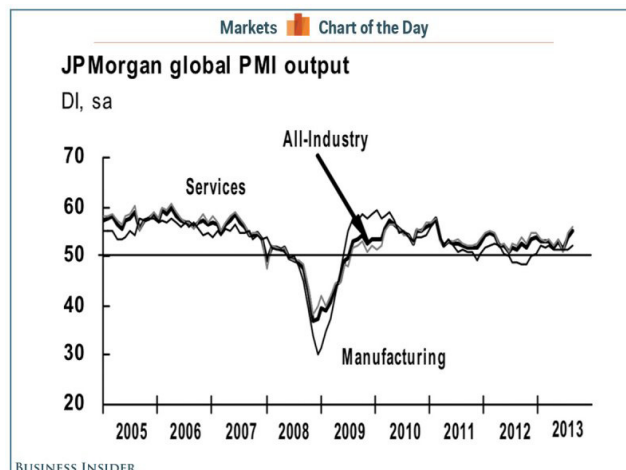
- The Labor Department reports U.S. claims for state unemployment benefits declined by 9,000 to 323,000 in the week ending August 31st. from a revised level of 332,000 reported the previous week; while continuing claims declined by 43,000 to 2.95 million in the week ended August 24th. The number of Americans who have exhausted their traditional benefits and are now receiving emergency or extended benefits under state or federal programs declined by 17,000 to 1.49 million in the week ended August 17th.
- The Roseland, New Jersey-based ADP Research Institute reports U.S. corporations added 176,000 workers to their payrolls in August, following a revised gain of 198,000 in July. In round numbers, ADP noted that workers were added in several industries including construction 4,000, manufacturing 5,000, trade/transportation 40,000, finance 1,000 and professional services 50,000.
- The U.S. Federal Reserve's 'Beige Book'—a survey of economic conditions in its 12 districts from early July through late August, released yesterday in Washington—indicates the U.S. economy expanded at a modest to moderate pace during the period, citing higher consumer demand for automobiles and housing related goods, such as furnishings and home improvement items. However, several regions reported that consumers remain cautious and 'highly price-sensitive.'

- Front Page Headline, New York Times – **“At the Core of a Debate about Food Stamps / On the Edge of Poverty.** Officially called the Supplemental Nutrition Assistance Program, or SNAP, food stamps have long been a cornerstone of the American federal safety net. On a monthly basis, benefits—adjusted for income—are loaded onto a government-issued debit card. Recipients divulge that the money typically lasts a little more than two weeks. When Congress returns to Washington next week, the diets of nearly 49 million Americans (a total as at December 31/12) will be involved in a debate over the reduction of the federal deficit. Republicans, alarmed by a rising enrollment in SNAP, are seeking to revamp and scale back the program. Democrats are resisting any cuts. Irrespective of whatever Congress decides, food stamp benefits will be reduced in November, when a provision in the 2009 stimulus bill expires. Yet as lawmakers cast the food stamp battle in terms of spending, nonpartisan budget analysts and hunger relief advocates warn of a spike in food insecurity among Americans (such as those living in Dyersburg, Tenn.) who look like they are healthy, but live on the edge of poverty, skipping meals and rationing food. Surrounded by corn and soybean farms—including one owned by Tennessee Republican Congressman Stephen Fincher—Dyersburg (about 75 miles north of Memphis) provides an eye opening view into Washington’s food stamp debate. Representative Fincher, who was elected in 2010 on a Tea Party wave and who collected nearly \$3.5 million (U.S.) in farm subsidies from the federal government from 1999 to 2012, recently voted for a farm bill that omitted food stamps, citing: ‘The one who is unwilling to work shall not eat.’ **Wake up call for Representative Fincher: Do enjoy your next meal as you continue to bask in woeful ignorance.”**



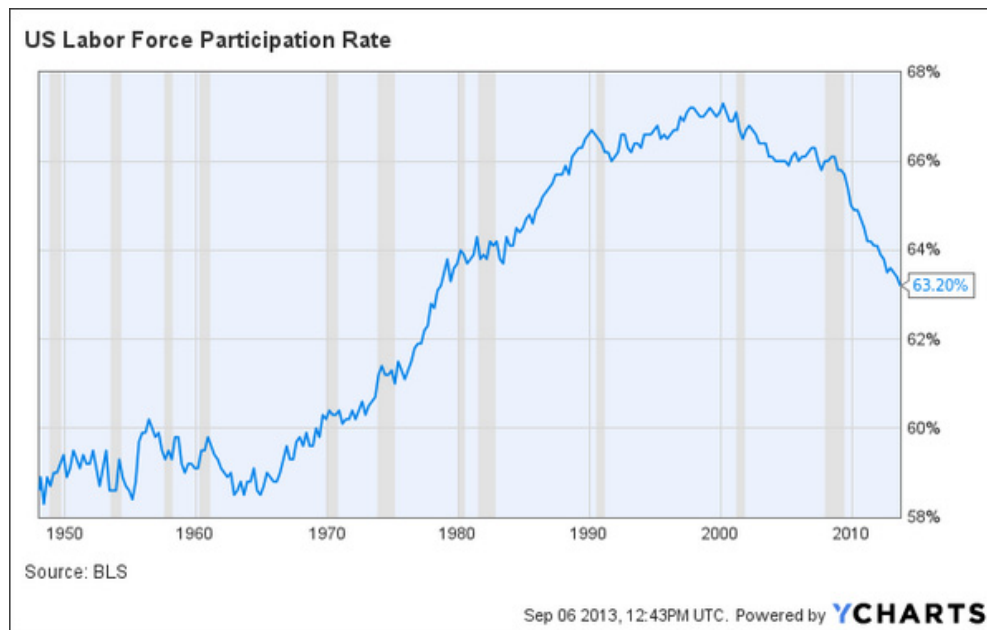
Rep. Stephen Fincher’s home near Dyersburg, Tennessee. Source: New York Times

- At his monthly news conference, European Central Bank (ECB) President Mario Draghi issued a sober assessment of the euro zone economy acknowledging: “I can’t share the (market’s) enthusiasm about budding economic growth in the euro zone. Not only am I very, very cautious about the prospects for economic growth, but also, we are certainly alert to the geopolitical risks which may emanate from the Syrian situation.’ Therefore, the ECB announced it was leaving its benchmark lending rate at a record low 0.5%.



Friday, September 6th

- The Labor Department reports U.S. non-farm payrolls rose by 169,000 in August, following downwardly revised gains of 140,000 in July and 104,000 in June, while the official unemployment rate declined from 7.4% to 7.3%—the lowest since December 2008—on a seasonally adjusted basis. Cary Leahey, an analyst at Decision Economics in New York, commented: ‘Even the Federal Reserve would conclude that the employment trend is moderating and for that reason alone, the Federal Open Market Committee (FOMC) will have second thoughts about tapering (U.S. Treasury purchases this month).’ Also reported was a decline in the U.S. labor force participation rate to 63.2%, the lowest level since 1978.



Shaded areas indicate recessions.

Source: Bureau of Labor Statistics

- Statistics Canada reports the Canadian economy created 59,200 jobs in August fuelled by a surge in part-time positions, concentrated mostly in Ontario and Alberta. The nation’s official unemployment rate declined slightly to 7.1%.
- The Office for National Statistics (ONS) reports the U.K. trade deficit for manufactured products was 9.9 billion pounds (\$15.45 billion U.S.) in July, considerably wider than June’s deficit of 8.2 billion pounds and the biggest trade gap in nine months. Driving the widening deficit was lower exports of goods to countries outside of the European Union (EU), which declined by 15.8%—or 2.2 billion pounds—to 11.8 billion pounds; the biggest percentage drop since January 2009. The ONS also released industrial production data, which revealed overall U.K. factory output was flat in July compared with June and was 1.6% lower on a year-over-basis.

	CLOSING LEVELS FOR FRIDAY, September 6th	WEEKLY CHANGE
Dow Jones Industrial Average	14,922.50	+ 112.19 points
Spot Gold Bullion	\$1,386.50 (U.S.)	– \$6.11 per oz.
S&P / TSX Composite	12,820.92	+ 167.02 points
10 - Year U.S. Treasury Yield	2.94%	+ 11 basis points
Canadian Dollar	95.95 cents (U.S.)	+ 1.14 cents
U.S. Dollar Index Future	82.15	– 0.15 cent
WTI Crude Oil (October)	\$110.53 (U.S.)	+ \$3.55 per barrel

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