Out of the Ordinary®

Investec
Group Economics

Week ahead: SA's data releases will be under heightened scrutiny as the global outlook fails to improve

22nd June 2012

Key data releases in the week ahead

- **SA:** **PPI, Money Supply, PSCE, Trade Balance, Leading Indicator**
- **US:** **GDP, Home sales, Durables, Jobless Claims, Confidence Indicators**
- **Euro zone:** **M3, CPI, Confidence Indicators,**

Figure 1: South Africa Monetary Policy Committee (MPC) meeting dates for 2012

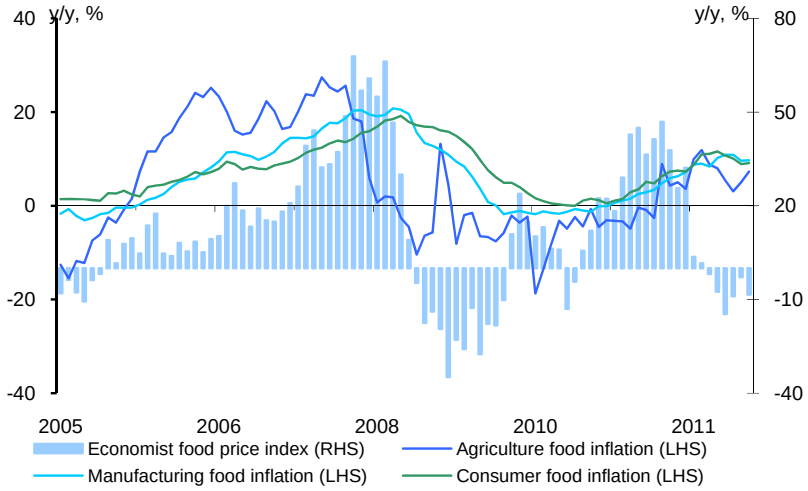
July	17-19	Flat
September	18-20	Flat
November	20-22	Flat

Source: SA Reserve Bank

South Africa

The Federal Reserve Bank's decision to continue Operation Twist until the end of the year is the latest in a long list of support measures aimed at keeping financial market conditions accommodative in order to prevent a marked global economic downturn (recession). The extension of "operation twist" (due to expire this month) means the Fed will purchase an additional $267 billion US treasuries with maturities ranging from six to thirty years. This will not increase liquidity, as the Fed will sell short dated bonds (three years or less) to fund the purchases, and once again QE3 has been avoided. The Fed´s balance sheet does not expand under "operation twist" (i.e. liquidity will not be pumped into the system) so emerging market currencies should not see the same harmful appreciation experienced under quantitative easing. It is hoped that low long-term interest rates (aimed at stimulating asset backed finance) will see the US avoid recession. The global outlook remains bleak on Europe's continuing sovereign debt crisis, the US's looming fiscal cliff (pre-programmed tax hikes and fiscal spending cuts which would cause the world's largest economy to contract by up to 4.0% in H1.2012) and poor US jobs and consumer spending data. While initial market disappointment ensued at lack of further quantitative easing (the rand weakened), the Fed's subsequent comment that it is "prepared to take further action" was taken to mean that there is still a possibility of QE3. We believe the Fed will not embark on QE3 unless growth stalls (and likely recession ensues). However, with strains remaining in euro bond markets (Spanish bond yields are at record highs since the advent of the euro) and little progress toward resolution of the crisis (and not merely stopgaps) QE3 cannot be ruled out. In this global environment SA's publication of its most recent economic readings will be scrutinized for any signs of slowing economic growth. Neither SA's employment nor household balance sheets have made up the losses experienced in the last recession and another recession would likely have a more detrimental impact than 2009's on these sectors. The FRA curve is now factoring in an increased chance of a 50bp cut in interest rates (almost 70% chance). We believe it is becoming a close call. PPI inflation is expected lower on moderating commodity prices while the money supply and credit figures are not expected to record a marked rise in growth rates.

Figure 2: Food inflation



Sources: Stats SA, I-Net

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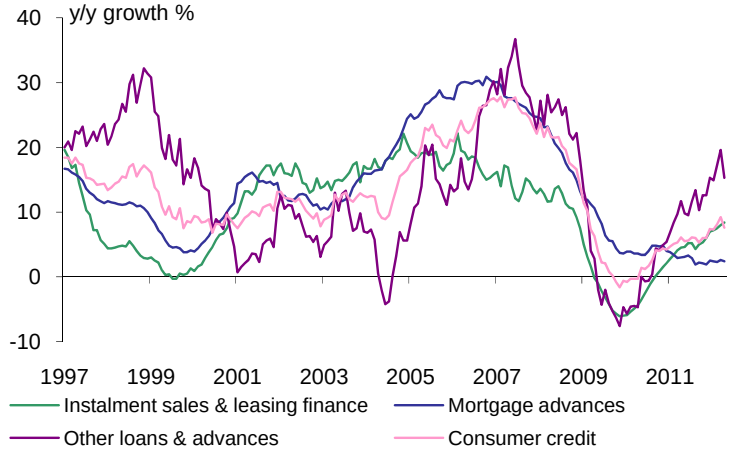
http://www.investec.co.za/research-and-insights/economic-research.html

Figure 3: Components of PSCE

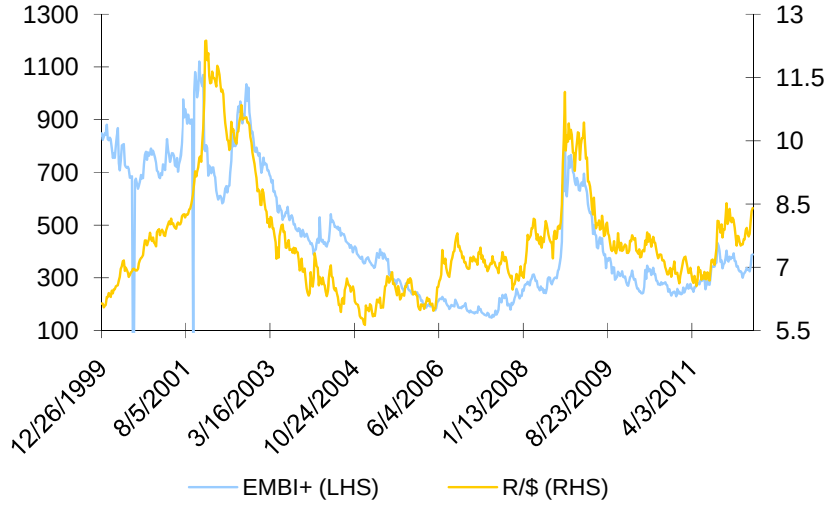


Sources: SARB

International

The week ahead brings the next gathering of Leaders, in the shape of the 28/29 June EU Summit. Markets will look to this with a distant hope that this could deliver some action to calm market strains. As it stands the agenda for that meeting looks unexciting, with 'orientations to boost growth and jobs' the centre. We suspect European leaders will be forced into pressing discussions on how far to budge in negotiations with Greece over relaxing the conditions of its bailout as well as discussions over aid to Spain and perhaps Cyprus too. We noted with curiosity earlier this week the line in June's UK MPC minutes implying that the UK's policy committee considered that the forthcoming Council meeting could 'materially affect the outlook'. We struggle to see this. Whilst we expect the subject of using the Euro area's rescue funds to buy Spanish and Italian bonds will be raised, we are doubtful that Leaders would sign-off on this with Finland vocally in opposition and with Germany stepping back from any discussions. In short, we see no quick turnaround in market strains.

Figure 4: EMBI+ and the rand: risk aversion levels drive rand



Source: I-net Bridge

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Whilst European Leaders are busy discussing their next move, several European sovereigns will be busy with debt issuance; we hope the news flow through next week is helpful for this, but this is far from guaranteed. The schedule includes Italian BOTs, BTPei and medium-long term bonds, Spanish bills, German Bubills, French bills and Belgian bonds. The Euro area data calendar looks quieter - however it is worth highlighting that Germany's flash CPI inflation figures are due on Wednesday. A moderation in the inflation reading, alongside today's drop in Germany's PMI, should help the case for further ECB easing on 5th July.

The run of UK economic releases continues thick and fast next week. The week sees the release of the final Q1.12 GDP estimate, public finances data, GfK consumer confidence, Nationwide house prices, the BoE Financial Stability Report and the BoE's Credit Conditions Survey. Subject to any major shift as a result of the ONS's chain linking revisions which take place alongside this release, we expect GDP to stand unchanged from the second estimate at -0.3% in the quarter. The detailed data that accompanies the release will also be watched closely with this potentially helping to shape the picture of the strength, or not, of recovery momentum going forward. In Q4.11, real net household incomes edged down by 0.2%, with the saving rate easing back to 7.7% (from 7.9%). We would not be surprised to see a similar move this time. Public finances figures for May are set for release early in the week. Our worry is that the weak economic backdrop will have weighed on receipts and added to the challenge of spending cuts. Accordingly we expect to see borrowing (PSNBX) stand £16.3bn in the red, some £1.3bn higher than May 2011.

Across the pond, the final Q1.12 GDP estimate is expected, with the early consensus pointing towards no change to the latest 1.9% (seasonally adjusted annualised rate) estimate. Aside from this, many of the US releases are housing focused with Case-Shiller, new home sales and pending home sales all due. Of late, it has been some of the US housing metrics that have held-up whilst broader US economic data has softened. If the US housing recovery does continue to move up a notch, this would be good news for the US's broader growth prospects; the hope will therefore be that the housing numbers hold firm next week.

Aside from the Euro crisis, another factor weighing on markets has been fears of a slowdown in the Chinese economy ('Chindown'). June's 'flash' HSBC manufacturing PMI added to these woes, with the index recording its 8th consecutive contraction and with the export orders sub-index falling to its lowest level since March 2009. Next week sees the official/NBS June manufacturing PMI published. Although this is subject to the NBS's own adjustment method for seasonal factors, the larger sample makes this worth tracking as another barometer of the Chinese manufacturing economy's health. The May reading stood at 50.4, although the NBS refers to the 50 level as the 'cut off point of economy strength' rather than the 'breakeven point' for growth or contraction.

International section written in conjunction with Philip Shaw, Victoria Cadman and Ryan Djajasupatra

Outlook

The Federal Reserve Bank's decision to continue "operation twist" until the end of the year (engender low long-term interest rates) is the latest in a long list of global support measures aimed at keeping financial market conditions accommodative, to prevent global recession. The Fed´s balance sheet does not expand under "operation twist" (i.e. liquidity will not be pumped into the system) so emerging market currencies should not see the same harmful appreciation experienced under quantitative easing. The Fed's move is a result of the global outlook remaining bleak on Europe's continuing sovereign debt crisis, the US's looming fiscal cliff (pre-programmed tax hikes and fiscal spending cuts which would cause the world's largest economy to contract by up to 4.0% in H1.2012) and poor US jobs and consumer spending data. While initial market disappointment ensued at lack of further quantitative easing (the rand weakened), the Fed's subsequent comment that it is "prepared to take further action" was taken to mean that there is still a possibility of QE3. We believe the Fed will not embark on QE3 unless growth stalls (and likely recession ensues). However, with strains remaining in euro bond markets (Spanish bond yields are at record highs since the advent of the euro) and little progress toward resolution of the crisis (and not merely stopgaps) QE3 cannot be ruled out.

In this global environment SA's publication of its most recent economic readings will be scrutinized for any signs of slowing economic growth. Neither SA's employment nor household balance sheets have made up the losses experienced in the last recession and another recession would likely have a more detrimental impact than 2009's on these sectors. PPI inflation is expected lower on moderating commodity prices while the money supply and credit figures are not expected to record a marked rise in growth rates.

The FRA curve is now factoring in an increased chance of a 50bp cut in interest rates - we believe it is becoming a close call.

We expect the rand to trade in a range of R8.70/USD – R8.10/USD, R10.80/EUR – R10.20/EUR and R13.40/GBP - R12.80/GBP in the week ahead.

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Figure 5: Economic data releases for the week ahead

Date	Country	Indicator	Month	Forecast	Previous
25/06/12	US	Chicago Fed Nat Activity Index	May		0.11
		New Home Sales	May	0.7% m/m	3.3% m/m
		Dallas Fed Manufacturing Activity	Jun	0.0	-5.1
26/06/12	SA	Leading Indicator	Apr		134.5
	US	S&P/CS 20 City	Apr	0.2% m/m	0.1% m/m
		S&P/CS Composite-20	Apr	-2.1% y/y	-2.6% y/y
		S&P/CashShiller Home Price Ind	Apr		134.1
		Consumer Confidence	Jun	64.0	64.9
		Richmond Fed Manufacturing Index	Jun	5	4
27/06/12	US	MBA Mortgage Applications	Jun		-0.8%
		Durables Goods Orders	May	0.5%	0.0%
		Durables ex Transportation	May	0.7%	-0.9%
		Cap Goods Orders Nondef Ex Air	May		-1.9%
		Cap Gods Ship nondef Ex Air	May		-1.4%
		Pending Home Sales	May	1.5% m/m	-5.5% m/m
28/06/12	SA	PPI	May	0.4% m/m	0.3% m/m
		PPI	May	6.0% y/y	6.6% y/y
	US	GDP	Q1.12	1.9% q/q	1.9% q/q
		Personal Consumption	Q1.12	2.7% q/q	2.7% q/q
		GDP Price Index	Q1.12	1.7%	1.7%
		Core PCE	Q1.12	2.1% q/q	2.1% q/q
		Initial Jobless Claims	Jun 23		387k
		Bloomberg Consumer Comfort	Jun		-37.9
		Kansas City Fed Manufacturing Activity	Jun		9
	Euro-zone	Business Climate Indicator	Jun	-0.81	-0.77
		Consumer Confidence	Jun		-19.6
		Economic Confidence	Jun	90.0	90.6
		Industrial Confidence	Jun	-12.0	-11.3
		Services Confidence	Jun	-6.0	-4.9
29/06/12	SA	Private Sector Credit	May	7.8% y/y	7.3% y/y
		Money Supply	May	6.5% y/y	6.2% y/y
		South Africa Budget	May		-26.4bn
		Trade Balance	May		-R9.9bn
	US	Personal income	May	0.2%	0.2%
		Personal Spending	May	0.1%	0.3%
		PCE Deflator	May	-0.1% m/m	0.0% m/m
		PCE Core	May	0.2% m/m	0.1% m/m
		Chicago Purchasing Manager	Jun	53.0	52.7
		U. of Michigan Confidence	Jun	74.5	74.1
		NAPM-Milwaukee	Jun		57.7
	Euro-Zone	M3 3 mth average	May	2.6%	2.7%
		M3	May	2.2% y/y	2.5% y/y
		CPI Estimate	Jun	2.4% y/y	2.4% y/y

Source: Bloomberg

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