Economics

News, analysis and commentary

Existing Home Sales; Canada Budget; Banxico Chief
By Ben Baris and Geoff King

What to Watch: Economists surveyed by Bloomberg forecast U.S. existing home sales declined by 2.5 percent in February from a month earlier to a 5.55 million seasonally adjusted annualized rate, 10 a.m. This follows a 3.3 percent rise to a 5.69 million rate in January. Canadian Finance Minister Bill Morneau presents the country’s budget to the House of Commons, the second of Prime Minister Justin Trudeau’s term. Canada is one of 10 countries with triple-A grades from the three leading debt rating companies. Morneau told reporters the budget he’s presenting will maintain fiscal responsibility.

Economics: The Mexico Banking Association’s convention in Acapulco will feature speeches by Mexico Central Bank Governor Agustin Carstens at 8:40 p.m. and Finance Minister Jose Antonio Meade at 9 p.m. This year’s conference topic is the world’s economic dilemma: liberalism versus populism.

Government: U.S. Secretary of State Rex Tillerson hosts foreign ministers and leaders of the 68-nation Global Coalition fighting the Islamic State, in Washington. As IS loses ground in its former strongholds in Iraq and Syria, the summit will focus on military needs, financing goals and the humanitarian crisis.

Companies: The U.S. EIA releases its weekly crude oil inventory report. Follow the TOPLive blog for real-time coverage on the Bloomberg terminal at 10:30 a.m.

Markets: Equities tumbled across the globe after the S&P 500 Index fell the most since Donald Trump’s election, as stocks joined an unwinding of reflation trades amid uncertainty over prospects for the U.S. president’s policies. The yen rose a seventh day as investors sought safety.

Home Resales Expected to Drop in February

— Carl Riccadonna and Yelena Shulyatyeva, Bloomberg Intelligence economists

Commentary in This Issue

In a mere four months economic conditions in Canada have progressed from relatively lackluster to almost stellar: Richard Yamarone.

The Fed remains confident that it is not behind the curve in tightening monetary policy: Bloomberg Intelligence economists.

Mexico is the most attractive emerging market for investors, based on a range of metrics analyzed by Bloomberg, while India is the worst: Masaki Kondo and Yumi Teso.

Trump Watch

President Donald Trump’s pick as his top trade negotiator, Robert Lighthizer, said the U.S. plans to forge stronger ties with Taiwan, a move that could raise tensions with China.

2.75-3.25 Percent

Global growth in 2017, according to Pimco, up from a forecast of 2.5 percent to 3 percent in December. The euro area, the U.K. and EM will all grow faster than the firm expected in December, according to its latest cyclical outlook report. (Link to terminal)

Tweet of the Day

I’m watching European banks to see if bail-in works in Italy. Doubt it. TLAC = bail in = fantasy #AskNeel twitter.com/WiiJameb6/sta…

Details

Live chart on the Bloomberg terminal.
Canada

Sales Need to Be Sustained to Avert Deja Vu of 2016

By Richard Yamarone, Bloomberg Intelligence economist

In a mere four months economic conditions in Canada have progressed from a relatively lackluster state of affairs to a vibrant, almost stellar pace of activity.

Unlike the U.S., where the majority of the post-election gains have been in the sentiment indicators, Canada is experiencing solid and relatively broad-based increases in its most critical indicators. Unfortunately we've seen this movie before, only to see the economy tank and teeter on the brink of recession. There are a number of risks looming which could potentially derail these gains.

Advances in Canadian economic indicators have been exceeding the Street's expectations. The Citi Economic Surprise Index currently resides at 94, its highest reading since July 21, 2010 (95.4). This supports a possible upward revision to aggregate demand estimates in the first quarter.

Sales started the year on an extremely favorable note, with better-than-expected gains in retail, wholesale and manufacturing activity. If these gains are sustained, a much larger increase in first-quarter GDP would be in order. Currently the consensus estimate is 2.2 percent.

Manufacturing sales in January climbed 0.6 percent, exceeding consensus, which called for a 0.3 percent decline. Meanwhile, wholesale trade surged 3.3 percent, blowing out the expectations of a mild 0.5 percent gain, and total sales on the retail level advanced 2.2 percent in January — the strongest monthly increase since March 2010 (2.6 percent) — bettering the expected 1.5 percent gain.

The key to an upward revision to first-quarter growth will be predicated on the sustainability of sales momentum. The increases in the sales measures this year are very similar to those in the January 2016 kickoff, when they posted impressive gains in retail (2.1 percent), wholesale (0.9 percent) and manufacturing sales (2.1 percent). But they soon petered out, and the economy floundered.

After registering an impressive 0.5 percent increase in January 2016, real GDP eventually sputtered with back-to-back declines of 0.2 percent in February and March and a flat performance in April.

The Alberta wildfires in May upended the economy with a 0.6 percent slump — the steepest since the throes of the Great Recession in March 2009 (minus 0.8 percent) — and the economy had struggled for the remainder of the year.

The root cause of the February-April 2016 slump was tumbling energy prices, particularly sub-$30 West Texas Intermediate crude oil. Current expectations do not project a return to those levels, but oil prices have fallen below the psychological $50-barrel level, matching a near four-month low. While this may not be the catalyst for cooler sales trends, it certainly won't be a positive contributor.

Other, and perhaps greater, risks to sustainable sales gains are the uncertainties surrounding tax and trade policy with the U.S. Canadians have been assured that the still unknown trade policy will only be "tweaked" from the present NAFTA agreement, while the potential for a border adjustment tax continues to loom in the markets. The imposition of a border tax would be economically-compromising for both countries, particularly imperiling Canada's trade and manufacturing activity.

So, before any upgrades to the Canadian economy are made based on the better-than-expected economic reports, it would be wise to see some clarity in those looming risks of policies, energy trends and the sustainability of gains in sales.
Emerging Markets

Trump-Bashed Mexico Most Attractive Emerging Market, India Worst

By Masaki Kondo and Yumi Teso

Mexico is the most attractive emerging market for investors, based on a range of metrics analyzed by Bloomberg including growth, yields and equity valuations. India is the worst.

The central American nation saw its currency slide and bond yields surge as President Donald Trump was elected in November after lambasting the country for stealing U.S. jobs. Even after an initial selloff subsided, Mexico’s 10-year bond yield is still more than a percentage point above where it was before the election. The peso’s real-effective exchange rate is close to a 21-year low, boosting the earnings outlook for exporters.

“Both Mexico’s currency and bonds have been sold too much,” said Akira Takei, who helps oversees the equivalent of $440 billion as a fund manager at Asset Management One Co. in Tokyo. He said expectations the dollar will weaken have convinced him to hold a higher proportion of pesos and Mexican government bonds in his portfolio than recommended by the benchmarks he follows.

India is the least attractive developing nation for investors due to its relatively expensive stocks, bonds and currency. India’s NSE Nifty 50 Index rose to a record and the Sensex climbed to a two-year high last week as the electoral victory of Prime Minister Narendra Modi’s party in the nation’s biggest state sparked optimism he will accelerate reforms including the introduction of a goods and services tax.

The new tax “is a great thing in the medium term, but there will be some disruption to consumption in the months following its introduction,” said Vaninder Singh, an economist at NatWest Markets in Singapore.

Singh agrees India appears unattractive for investors at the moment. “You will have to see a correction in the equity markets, and as a consequence the Indian rupee as well.”

— With assistance from Hannah Dormido

Looking for Value

Source: Bloomberg

<table>
<thead>
<tr>
<th>Metrics</th>
<th>Mexico</th>
<th>Turkey</th>
<th>Chile</th>
<th>Hungary</th>
<th>S. Africa</th>
<th>Brazil</th>
<th>Russia</th>
<th>China</th>
<th>India</th>
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<tbody>
<tr>
<td>GDP</td>
<td>-0.72</td>
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<td>0.47</td>
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<td>Current Account</td>
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<td>0.09</td>
<td>0.94</td>
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<td>-0.36</td>
<td>-0.14</td>
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<td>Yield</td>
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<td>-0.6</td>
<td>1.03</td>
<td>-0.94</td>
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<td>0.04</td>
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<td>REER</td>
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<td>0.35</td>
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<td>-0.11</td>
<td>-1.11</td>
<td>-0.78</td>
<td>1.56</td>
<td>-0.44</td>
</tr>
<tr>
<td>Total</td>
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<td>2.15</td>
<td>1.04</td>
<td>0.57</td>
<td>0.52</td>
<td>-0.38</td>
<td>-0.8</td>
<td>-3.78</td>
<td>-4.56</td>
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Bloomberg’s analysis covers nine of the 10 countries making up JPMorgan Chase & Co.’s Emerging Market Currency Index. Singapore is excluded as it is considered to be a developed nation. The attractiveness of each country is computed for the following criteria, with forecasts compiled from Bloomberg surveys of analysts and economists: Forecast growth in gross domestic product for 2017; Forecast current-account balance for 2017 relative to GDP; Price-earnings ratio for the key stock index; Ten-year bond yield; Real-effective exchange rate based on data from Bank for International Settlements; Implied foreign-exchange volatility; Sovereign credit rating.

The result for each is shown as a Z-score, which measures the relationship of the individual value to the mean. The scores are computed based on the five-year average between one country’s variable and the mean of the nine emerging markets.

The results for stock price-earnings ratios, real effective exchange rate and foreign-exchange volatility are reversed as higher figures mean they are less attractive for investors.

GDP growth measures the potential for asset returns, while the current-account balance indicates the risk of a currency crisis. Equities, government bonds and currencies represent major investment classes.

Implied volatility gauges risks to carry trade. The credit rating is a proxy of the riskiness of government bonds and currencies. Ratings are based on Moody’s Investors Service, and the alphabetical symbols are converted into numbers, with Aaa given a value of 20 and C representing zero.
Fed's 2017 Rate-Hike Schedule Faces Headwinds

By Carl Riccadonna and Yelena Shulyatyeva, Bloomberg Intelligence economists

The gradualist Fed remains confident that it is not behind the curve in proceeding toward a less-accommodative stance — and this confidence is shared by a substantial number of meeting participants, as reflected in the relatively tight clustering in the dot plot. The pace of future tightening will likely be influenced by the economy’s response to higher rates, the post-election surge in sentiment and the arrival of full employment. The FOMC’s median interest-rate forecast implies two more hikes in 2017.

Following a 25-basis-point fed funds rate increase in March, BI Economics projects the remaining hikes to occur in June and December. The composition of the most recent dot plot signals that there is a strong coalition of doves and moderates that favors this interest-rate trajectory.

The timing and pace of rate hikes in 2017 will depend on how the economy performs near full employment. Rate policy will be particularly sensitive to the relationship between intensifying labor scarcity, mounting wage pressures and accelerating growth.

Ultimately, these factors will drive inflation higher. The BI Fed Spectrometer aims to classify each FOMC governor or regional reserve bank president along a spectrum of minus 2 (dovish) to 2 (hawkish) based on his or her policy inclination.

The average voting member rating in 2017 is minus 0.6 versus 0.7 for non-voters, signaling a dove-hawk divide between voters and non-voters. Ratings suggest the prospect for dissents is low, as there are only two moderate hawks who are voters; the rest are doves or moderates. Governors rarely dissent.

A primary objective of the Trump administration is to lift growth through fiscal stimulus, thereby leaving monetary policy makers to ponder whether they need to institute offsetting actions to prevent the economy from overheating.

In Chair Yellen’s press conference following the March FOMC meeting, she noted that the Fed would not need to intervene in certain circumstances, for example if well-designed infrastructure investment boosted the natural growth rate, or “speed limit”, of the economy.

While some policy makers incorporated a lift from fiscal policy into their forecasts, several others refrained from doing so until greater detail is known regarding the composition and timing of stimulus. As a result, the trajectory of Fed policy could be significantly reconfigured in the medium term.

President Donald Trump could meaningfully alter the composition of the Federal Reserve Board of Governors in the coming year. This will have implications for the Fed’s approach to monetary policy and financial industry regulation. The president appoints members of the board who are confirmed by the Senate and serve for 14 years.

In addition, with Janet Yellen’s term as chair ending on Feb. 3, 2018 and Stanley Fischer’s term as vice chairman expiring on June 12, 2018, President Trump will also select the new chair and vice chair. These appointments are also subject to Senate confirmation.

The Federal Reserve Bank of Atlanta recently announced Raphael Bostic of the University of Southern California will become the president and chief executive officer of the bank effective June 5. The appointment follows President Dennis Lockhart’s retirement in February. Bostic will participate in the June FOMC meeting as a non-voting policy maker and will rotate in as a voter 2018.

Bostic serves as a Freddie Mac board member and previously worked at the Department of Housing and Urban Development. His housing-market expertise would be extremely timely. Previously, Elizabeth Duke, a Fed Board of Governors member from 2008-2013, was known as a housing-market expert on the FOMC.
Data & Events

Pillar of Trump Rally Cracks as Banks Sink Most Since Brexit

The start of spring greeted stock-market investors with something they haven’t seen since fall. The S&P 500 Index capped its first decline of 1 percent since October amid a rout in financial shares that have been the biggest beneficiary of Donald Trump’s election. Banks plunged around 2.9 percent — the most since the Brexit vote in June — trimming a rally that had reached 22 percent through March 20 and was double the S&P 500’s gain since the vote. While blame for the selloff spread from profit-taking to a renewed drop in Treasury yields and a warning from Morgan Stanley on weakness in fixed income, looming above the rout were Trump and concern that his pro-growth agenda may not be the slam-dunk investors had bet on.

— Oliver Renick

Source: Bloomberg. Surveys updated at 5:05 a.m. in New York.

Full story with live chart on the Bloomberg terminal.

Calendar

<table>
<thead>
<tr>
<th>TIME</th>
<th>COUNTRY</th>
<th>EVENT</th>
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<tr>
<td>7:00</td>
<td>U.S.</td>
<td>MBA Mortgage Applications</td>
<td>—</td>
<td>3.10%</td>
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<td>7:30</td>
<td>Chile</td>
<td>Central Bank’s Traders Survey</td>
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<tr>
<td>8:00</td>
<td>Brazil</td>
<td>IBGE Inflation IPCA-15 MoM</td>
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<tr>
<td>8:00</td>
<td>Brazil</td>
<td>IBGE Inflation IPCA-15 YoY</td>
<td>4.73%</td>
<td>5.02%</td>
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<tr>
<td>9:00</td>
<td>U.S.</td>
<td>FHFA House Price Index MoM</td>
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<tr>
<td>10:00</td>
<td>U.S.</td>
<td>Existing Home Sales</td>
<td>5.55m</td>
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<td>10:00</td>
<td>U.S.</td>
<td>Existing Home Sales MoM</td>
<td>-2.50%</td>
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<td>11:00</td>
<td>Mexico</td>
<td>International Reserves Weekly</td>
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<td>11:30</td>
<td>Brazil</td>
<td>Currency Flows Weekly</td>
<td>—</td>
<td>—</td>
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<tr>
<td>16:00</td>
<td>New Zealand</td>
<td>RBNZ Official Cash Rate</td>
<td>1.75%</td>
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<td>TBD</td>
<td>Canada</td>
<td>Finance Minister Bill Morneau Introduces Federal Budget</td>
<td>—</td>
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</table>

Source: Bloomberg. Surveys updated at 5:05 a.m. in New York.

Click on the highlighted releases to see the full range of economists’ forecasts on the terminal.

Overnight

Europe

- Sweden’s Riksbank says policy in 2016 has had the intended effect. Inflation has risen closer to the target, long-term inflation expectations are back around 2 percent and the Swedish economy has developed well, the central bank said in a statement on account of monetary policy in 2016. The central bank added “the upturn in inflation was still fairly fragile and there were moreover risks linked to international developments”

Asia

- Japan’s exports rose for a third consecutive month in February as strengthening global demand continued to help the nation’s moderate economic recovery. The increase was the biggest in two years, reflecting the timing of Lunar New Year holidays in Asia. Exports rose 11.3 percent from a year earlier, beating a Bloomberg survey median estimate for 10.1 percent, according to government data. Imports increased 1.2 percent, slightly below the 1.3 percent estimate. The trade surplus for February was 813.4 billion yen ($7.29 billion), compared with an estimate of 807.2 billion yen. Lunar New Year holidays fell mostly in January this year and February last year, crimping the export result for January and boosting the performance in February.

- China’s central bank injected funds via open-market operations for a third day after the benchmark money rate climbed to the highest level since April 2015 and some smaller lenders were said to fail to make debt payments in the interbank market. The People’s Bank of China pumped in a net 40 billion yuan ($5.8 billion) today, taking net injections so far this week to 110 billion yuan.