

# Christmas Arrived Early in 2013

Key economic indicators and capital market events for December 2013 by Joe Terranova, Chief Market Strategist



Christmas arrived early for investors this year. The first quarter shift in Japanese monetary policy was a powerful tailwind, helping the equity market overcome the fiscal cliff, sequester, and Cyprus banking crisis that followed. The S&P 500® Index has steadily climbed, exhibiting technically pristine bullish performance, with five modest corrections, none greater than 8%. This December is free of the worries of a year ago, which should motivate money managers to enjoy what they couldn't last year – holiday downtime in an excellent global market for risk assets. In keeping with this spirit, our calendar is fairly light, absent of European data, as the relevant action there occurred in November when the ECB lowered interest rates, and Q3 corporate earnings are behind us. Ahead of the FOMC December 17-18 meeting, we do want to watch for any better-than-expected or acceleration in U.S. data that would suggest an earlier “taper” start date than the current March 2014 consensus. Globally, we should also pay attention to China's data. Finally, thanks to everyone who utilizes the monthly capital markets calendar. I hope you find value in its content. I wish a happy and healthy holiday season to all.

## December 2013

Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
1	2 10:00 AM: U.S. ISM Manufacturing	3	4 8:30 AM: U.S. New Home Sales (Sept./Oct.) 2:00 PM: Fed Beige Book	5	6 8:30 AM: U.S. Labor Report	7
8	9 Market Reaction to China Key Data	10 7:30 AM: U.S. NFIB Small Business Optimism Index	11	12 8:30 AM: U.S. Retail Sales	13 S&P 500 Quarterly Review	14
15	16	17 8:30 AM: U.S. CPI	18 2:00 PM: FOMC Statement and Economic Projections 2:30 PM: FOMC Press Conference	19	20 S&P 500 Quarterly Rebalance	21
22	23	24	25 Christmas Holiday – Markets Closed	26 Holiday Sales First Glance	27	28
29	30	31 China Manufacturing PMI				

Times shown are Eastern Time.

## December indicators / events of note:

### U.S. ISM Manufacturing

Issued by the Institute of Supply Management, this report provides an influential monthly measure of the health of U.S. manufacturing based on an in-depth survey of 300 manufacturing firms. An index value of 50 is the dividing line between an expanding or slowing economy. Data released is for the previous month.

## You should be watching:

For much of late 2012 and into early 2013, the services side of the economy has led the U.S. recovery. Lately we are seeing evidence of a dramatic snapback on the manufactured goods side. The ISM report is incredibly important to that narrative and to what the Federal Reserve may do relative to tapering. From July through October, ISM stayed above 55, which is the first time we've had four consecutive months of readings over 55 since the first four months of 2011. This follows lower ISM readings from April through June, providing the ultimate evidence that the second quarter sequester spending cuts were a one-time fiscal drag.

> October	56.4	> June	50.9
> September	56.2	> May	49.0
> August	55.7	> April	50.7
> July	55.4		

### U.S. New Home Sales

Issued monthly by the U.S. Census Bureau, U.S. Commerce, and U.S. Housing Departments, this report reveals the number of newly constructed homes with a committed sale.

On December 4, we'll get home sales data for October as well as September, which was delayed due to the government shutdown. While 30-year mortgage rates have risen, there is evidence to suggest that the rise in rates – which I would characterize as a return to normalization for the five-year period – should not impede the housing recovery. I'm still focused on the incredibly low inventory level, and the number of foreclosure homes which have fallen from 4.3 million in 2012 to 900,000 in 2013.

### Fed Beige Book

The Beige Book provides FOMC commentary on the current economic conditions in each of the Federal Reserve's 12 districts and is released two weeks prior to the next FOMC meeting, scheduled for December 17-18.

The Beige Book will set the agenda for the December FOMC meeting and is still relevant to the "will they or won't they" Fed taper conversation. While consensus is for tapering to be delayed until the FOMC's March 2014 meeting, better-than-expected data could force it to move sooner.

### U.S. Labor Report

Private payroll data is part of the Labor Department's monthly U.S. Employment Situation report. This data gives the true employment story, is the best gauge of the economy's direction, and has the power to move markets.

We would need to see 250,000 or more jobs added to both the headline and private payroll numbers in order for the Fed to initiate tapering at the December FOMC meeting. The Street's expectations are nowhere near those figures. In fact, consensus estimates are for the November labor report to come in much weaker than October's report. The Street estimates adding 160,000 jobs to the headline number versus last month's 204,000, and for private payrolls to pick up 170,000 jobs over last month's 212,000. Expectations are for the unemployment rate to drop back down from 7.3% to 7.2%. In order for the December labor report to equal a taper, it would need to deliver a big surprise, which seems unlikely given expectations and the potential for negative revisions to the very weak October report.

## December indicators / events of note:

### Market Reaction to Key China Data (Released In the Prior Weekend)

China releases key data the weekend of December 7-8, including CPI, PPI, and trade balance reports.

## You should be watching:

The rise in value of China's currency, the yuan, has been incredibly important in helping global risk assets appreciate. With U.S. Treasury yields beginning to rise, how do the Chinese as owners of Treasuries feel about owning them? Will the People's Bank of China (PBOC) begin to look at trade balance figures and consider a return to the policies of the mid-2000s when their efforts were on keeping the yuan weak? That would be somewhat problematic. China exports and imports are still not exhibiting the year-on-year double-digit growth we witnessed years ago. Last month, China reported a \$31.1 billion trade surplus, with imports up 7.6% and exports up 5.6%. We need to watch China's economic data to gauge what its central bank's intentions will be in 2014 toward its currency, as that will be most impactful for global risk assets.

### U.S. NFIB Small Business Optimism Index

This index offers insight on the health of the small business sector and is based on a survey conducted by the National Federation of Independent Business (NFIB) of its members. Results are for the previous month.

I like to monitor the NFIB Small Business Optimism Index, particularly now that global expectations are for growth to accelerate, since there is historically a high degree of correlation between this index and the equity market. From May through September, we had five consecutive months of very strong readings above 93.5. However, the index fell from 93.9 in September to 91.6 in October, and we're looking to see if the slowdown was just a transitory effect of the October government shutdown. To this point, the numbers have been solid and nowhere near the mid-to-low 80s figures indicative of a lack of optimism – and I would argue pessimism – for risk assets.

### U.S. Retail Sales

Retail sales data are released monthly by the U.S. Department of Commerce, providing total sales receipts for durable and nondurable goods. Consumer spending accounts for two-thirds of GDP and is therefore a key element in economic growth. Each report is based on the previous month's data.

Even though we'll get more relevant retail figures after Christmas, the retail sales report for November will tell us what the effect of the October government shutdown was heading into Black Friday. To this point, consumer spending continues to climb with unabashed resiliency. During the recent earnings season, consumer discretionary exhibited the strongest earnings growth of any sector due to pure sales growth, and is evidence of a favorable environment for the retail space going into the holiday spending season.

### S&P 500 Quarterly Review and Rebalance

Standard & Poor's conducts its quarterly review and rebalance of the constituents in the S&P 500 Index on December 13 and December 20, respectively.

This is of interest for the trading activity that occurs related to any constituent changes in the S&P 500 Index. Last quarter, Delta was added to the S&P 500 last quarter. I suspect we will see more airlines added to the S&P 500 as the recovery continues to take hold.

## December indicators / events of note:

### U.S. Consumer Pricing Index (CPI)

The Consumer Price Index measures the price of goods and services paid by consumers and is therefore considered to be a key indicator of inflation.

### FOMC Statement, Economic Projections, and Press Conference

Following its December 17-18 monetary policy meeting, the Federal Open Market Committee (FOMC) releases its statement and quarterly economic projections, and Chairman Bernanke gives his final press briefing.

### Holiday Sales First Glance

Early holiday spending data starts to be released in reports from private agencies such as MasterCard Advisors SpendingPulse and the International Council of Shopping Centers.

### China PMI

China PMI (purchasing managers' index) provides a monthly gauge of China's manufacturing sector which, when combined with the monthly U.S. ISM Manufacturing Index value, gives a clear picture of global manufacturing health. A PMI value above 50 indicates growth, below 50 contraction.

## You should be watching:

St. Louis Fed President James Bullard has been a strong advocate for paying attention to inflation. Over the last couple of months, overall CPI inflation has been trending down, falling to a very uncomfortable level of 0.9% in October from 2% in July, on a year-on-year basis. Because the pure CPI readings are so low, I don't foresee an inflationary environment. A significant contributor to CPI is much lower commodity costs, and we're not seeing evidence of wage inflation. I view the readings as trough-type figures, and I expect inflation to push back to a more normalized level in 2014, which should alleviate some of the current concerns FOMC members may have about deflation.

The economic data leading up to the FOMC meeting will have to be incredibly strong to motivate the Fed to taper this month. This will be Chairman Bernanke's final opportunity to address the business media at the quarterly FOMC press conference. I expect much of his remarks will be reflective, as reporters will be interested in his thoughts on these last historic five years.

The holiday season is important to retail companies, which get an estimated 25%-35% of their overall revenue from holiday sales. In 2011, Macy's generated 60% of its revenue from holiday sales. This year's holiday season is setting up to be much different from last year, which was negatively impacted by the fiscal cliff conversation and the aftereffects of Hurricane Sandy and the Sandy Hook tragedy. Last year, sales in the two months before Christmas were up only 0.7% over the prior year, according to MasterCard Advisors SpendingPulse. Even though this year's holiday season is technically shorter because of the late Thanksgiving, I'm expecting a surprise to the upside for sales.

China's manufacturing sector continues to recover, producing strong readings for the last five months:

> October	51.4	> July	50.3
> September	51.1	> June	50.1
> August	51.0		

Plain and simple, this evidence suggests the contraction in China's economic growth has troughed, which is good news.



**JOSEPH M. TERRANOVA**, *Chief Market Strategist, Virtus Investment Partners*

Joe Terranova is chief market strategist for Virtus Investment Partners, a position he was elevated to in 2009, after having started with the company as chief alternatives strategist. In his current role, Mr. Terranova works with Virtus' regional sales teams and the financial advisors who sell the company's investment products, providing insight into the domestic and global investing landscape and has represented Virtus as a keynote speaker for several financial institutions. He is a member of the Virtus Investment Oversight Committee.

Prior to joining Virtus in 2008, Mr. Terranova spent 18 years at MBF Clearing Corp., rising to the position of director of trading for the company and its subsidiaries. In this capacity, he managed more than 300 traders and support staff for MBF, one of the New York Mercantile Exchange's largest firms. His work was highlighted as the feature story in the June 2004 issue of *Futures* magazine.

Mr. Terranova is perhaps best known for his risk management skills, honed while overseeing MBF's proprietary trading operations during some of the most calamitous times for the U.S. markets, including the first Gulf War, the 1998 Asian Crisis, 9/11, and the collapse of Amaranth Advisors. In 2003, he was one of the first Wall Street professionals to make an early call for higher energy, natural resources, and commodity prices. In June 2008, he cautioned investors to move to the sidelines in commodities and, in March 2009, he encouraged investors to ignore the global "embracement of pessimism" and overweight equities. Before joining MBF, Mr. Terranova held positions at both Swiss Banking Corp. and JP Morgan Securities.

Mr. Terranova has been an ensemble member of the CNBC *Fast Money* franchise since 2008. He also frequently contributes exclusively to CNBC's other business programs. He is the author of *"Buy High, Sell Higher"* (Business Plus, 2012), a book about the "new rules" of investing based on his years as a professional trader.

Mr. Terranova is strongly committed to charitable causes benefiting children. He founded and funds the 501(c) South Nassau Rock organization, which provides specialized athletic experiences for children, and works with Nassau County to sponsor the improvement of baseball and outdoor ice rink facilities. In 2007, he established "Bossy's Bunch," a program that rewards academic excellence among elementary school students, with New York Islanders Hall of Fame hockey player Mike Bossy. In 2013, he expanded his charity work with the Islanders, creating and sponsoring the "Courier of Courage" program, which acknowledges children who have overcome hardships, disabilities, or illness.

Mr. Terranova earned a bachelor's degree in finance from the Peter J. Tobin College of Business at St. John's University in New York.

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