Let the Search for Growth Begin

Key economic indicators and capital market events for January 2014 by Joe Terranova, Chief Market Strategist

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From September 1, 2011 through March 31, 2013, the optimal investment strategy was "the search for yield." During those six quarters, the 10-year U.S. Treasury yield averaged 2.86%, creating clear justification for such a strategy. Now, with the yield on the 10-year approaching 3%, the focus must shift toward the search for growth. That growth will need to come in multiple forms: an acceleration of U.S. growth, continued recovering growth in Europe and China, and a transition for S&P 500® corporations to achieving strong sales growth. Over the last few years, the month of January has been a tone and trend setter for the balance of the year that followed. That is why I encourage investors to closely monitor the flows of capital to select asset classes over the next few weeks to potentially gain similar insight on what may be ahead for 2014.

January 2014

Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
			1 **China Mfg. PMI (Dec.)** **Latvia Adopts the Euro** **Russia Assumes G8 Presidency**	2 **European PMI Mfg.** 10:00 AM: **U.S. ISM Mfg.**	3	4
5	6 10:00 AM: **U.S. ISM Non-Mfg.**	7	8 **China Trade Balance & CPI**	9 **BOE & ECB Meetings**	10 8:30 AM: **U.S. Labor Report**	11
12	13	14 8:30 AM: **U.S. Retail Sales** **JPM Kicks Off Q4 Earnings*** **China Q4 GDP**	15 2:00 PM: **Fed Beige Book**	16 8:30 AM: **U.S. CPI**	17	18
19	20 **U.S. Holiday Markets Closed**	21 **Q4 SPX Earnings Intensify – 75 reports this week (estimate)**	22	23	24	25
26 **BOJ December Minutes**	27 **Q4 SPX Earnings Halfway – 118 reports this week (estimate)**	28 **U.S. State of the Union Address**	29 2:00 PM: **FOMC Meeting Concludes**	30	31 **China Mfg. PMI (Jan.)**	

*Times shown are Eastern Time. *Expected earnings release date; may be subject to change.*

January indicators / events of note:	You should be watching:
China Mfg. 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.	Over the last 12 months, China PMI has averaged 50.7. A 12-month high of 51.4 was established with the October report, which was matched in November. Preliminary readings during December point toward a potential moderation in China PMI, however, I caution investors not to pay too much attention to it unless there is a significant contraction in the reading, back below 50. Any potential moderation we see may be a short-term reaction to the structural domestic reform policies recently announced by the Communist Party of China (CPC).
Latvia Adopts the Euro Latvia becomes the eighteenth European nation to adopt the euro as its new currency, replacing the lats.	Isn't it interesting that a few years ago, everyone expected the 17-member euro to break apart, and here we are now, adding an eighteenth member. Latvia adopting the euro is indicative of the recovery going on in Europe. Very few projected that in January 2014 the number of euro members would go up from 17, not down.
Russia Assumes G8 Presidency Russia is president of the Group of Eight (G8) in 2014 under the rotating annual presidency, which includes hosting the annual summit this summer. The G8 represent eight of the world's largest national economies.	Russia is in a unique position with three consecutive global leadership roles over a three-year period. Following up to its 2013 presidency of the G20, Russia will host the Sochi Winter Olympics and assume the G8 presidency in 2014, and will chair the BRIC group in 2015. As a result of being elevated to a grander global stage and having the opportunity to put forth policies, Russia hopes to follow the path of the U.K., the 2013 G8 presidential nation, which has been enjoying strong economic growth.
European PMI Mfg. A country's PMI (purchasing managers' index) is a key measure of the state of that country's manufacturing sector. An index value above 50 indicates growth, below 50 contraction.	The recovery in European manufacturing continues, with many countries reporting PMI readings above 50. Last month, the overall eurozone recovered to a 52.7. Leading the way was the U.K. with a 58.4 and Germany with a 54.2, both multi-year highs. Switzerland, a country I don't usually write about, had a 56.5 (compared to 48.3 in March 2013). Even Italy came in over 50, with a 51.4. France continues to struggle, with a 47.0. For the most part, last month's European PMI readings were the highest they've been since the May 2011 onset of the sovereign debt crisis. From August 2011 to June 2013, there wasn't a European PMI reading above 49.0. I would expect the positive momentum in manufacturing to continue. As I wrote in my Q1 2014 playbook, I favor German, U.K., and Swiss assets for the quarter based on the strength in manufacturing seen in these countries.
U.S. ISM Manufacturing Index The ISM Manufacturing Index is 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.	We're at an inflection point, where the goods side of the economy (measured by the ISM Manufacturing Index) is starting to catch up to the services side (measured by the ISM Non-Manufacturing Index)—something we haven't seen in several years. Last month's ISM Manufacturing was 57.3. That was the fifth consecutive month where this index came in above 55 (July 55.4, August 55.7, September 56.2, October 56.4, and November 57.3), much stronger than the prior quarter (June 50.9, May 49.0, and April 50.7). The transition is upon us where goods manufacturing is accelerating once again, rising up to meet services, which has been very strong.

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U.S. ISM Non-Manufacturing Index The ISM Non-Manufacturing Index is based on surveys of nearly 400 firms from 60 sectors across the U.S., including agriculture, mining, construction, transportation, communications, wholesale trade, and retail trade. The index provides the economic backdrop for the various markets, and consists of data on business activity, new orders, employment, and supplier deliveries.	As discussed in the ISM Manufacturing commentary, the services side of the U.S. economy was very strong for much of 2013. In fact, ISM Non-Manufacturing for August hit 58.6, a six-year high. We've recently seen a little moderation in services—55.4 in October and 53.9 in November. I'm not suggesting that the ISM Non-Manufacturing Index has to fall back below 50 because the ISM Manufacturing Index is accelerating again. Rather, manufacturing is experiencing the momentum recovery that the non-manufacturing sector witnessed in 2013. Going into 2014, both goods and services are producing strong numbers above 53, and that's an overall positive for the direction of the economy.
China Trade Balance & CPI > **China Trade Balance Report** – Provides important import, export, and interest rate data on the Chinese economy. > **China Consumer Price Index** – Measures changes in the prices of China's consumer goods and services, and is therefore a key indicator of inflation.	China is interesting to watch, especially as it skates towards the New Year, however, its trade balance report is not likely to be as meaningful or impactful as it once was. China trade balance came in last month at a $33.8 billion surplus. This lends itself to continued yuan appreciation, which is good. Last month, exports rose 12.7% and imports were up 5.3% year on year—also positive. In addition, China CPI rose 3% year on year last month, which is okay. The fact is, Chinese economic numbers are not likely to have a dramatic impact on risk assets right now. Wall Street understands that China is undertaking, as was announced in November at the Third Plenary Session of the CPC Central Committee, a number of economic reforms geared toward achieving open and competitive markets. In the near term, this may limit China's growth acceleration, but these reforms are much needed and will lead to favorable conditions longer term. I would never take China data off the calendar but its relevancy compared to prior years has changed for the time being.
BOE & ECB Meetings Both the Bank of England (BOE) and European Central Bank (ECB) release monetary policy announcements on January 9 following their first meetings of the new year.	The BOE is more of a focus right now than the ECB. If we are going to see a monetary policy adjustment similar to the Fed's asset tapering, it will come from the BOE. However, we need to watch how both central banks talk about their currencies. The ECB recently cut interest rates to 0.25%, and I don't see much change there. Following the ECB meeting, I expect President Draghi will talk to trying to keep the euro—which is back up to 1.37—below 1.40. It's more important to get a sense of when the BOE will begin pulling back on its easy monetary policy efforts. Currently, its target interest rate is 0.50%, and its asset purchase program is at 375 billion pounds. I expect the BOE will try to keep the pound below 1.65.

Return to Page 1

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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.	Last month, headline payrolls added 203,000 jobs, private payrolls rose 196,000, and the unemployment rate fell to 7%. Private payrolls will be important in the December report. Expectations are for private payrolls to add 190,000 to 210,000, the headline number to gain 190,000 to 200,000, and the rate to remain unchanged. I'd also start looking at average hourly earnings, which in the last report were up 2% year on year and 0.2% month on month. I want to see if there is wage growth. Also last month, the labor force participation rate came in at 63%, the underemployment rate was 13.2%, and the average weekly hours worked was 34.5. I don't expect the December report to be much different from the November report.
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.	We had a very strong back-to-school season last quarter, but it looks like we'll see a moderation in earnings for the fourth quarter, based on the extensive amount of deep discounting done during the holiday season. I think the bar has been lowered enough for retail sales expectations; however, we don't want to see an abysmal reading this month. We've now gone eight consecutive months without a negative month-on-month change in retail sales—and 17 consecutive months with only one month-on-month negative reading (-0.3% in March 2013).
JPM Kicks Off Q4 Earnings* J.P. Morgan (JPM) is expected to release earnings on Tuesday, January 14.	Even though earnings season officially starts on Thursday, January 9, it doesn't really get underway until the week of January 14, when the financials sector starts reporting. The Street has very robust expectations for earnings in the upcoming quarter on a bottom-up basis, and it's possible we could hit double digits. Financials and consumer discretionary may both weaken a tad, however, technology, materials, and industrials should experience significant growth acceleration on a bottom-up basis from the prior quarter. Sales growth should uptick marginally. Over the last five quarters, profit margins have risen 75 basis points, close to 9%, to fuel the multiple expansion we've seen. If that's to stay consistent in 2014, we will need to see sales growth uptick more substantially.
China Q4 GDP China's gross domestic product (GDP) growth rate provides an aggregated measure of changes in the value of goods and services produced by the world's second largest economy.	China has had six consecutive quarters of GDP between 7.4% and 7.9%. In the third quarter, China GDP grew 7.8%, and we are expecting similar growth for the fourth quarter. The question is, by the second half of 2014, will we see a return to 8% growth in China GDP? Certainly, China's implementation of new structural and social reforms will intensify in the middle of 2014, and the globe views these reforms as long needed and favorable over the long term. However, I don't think China's economic environment will be good enough for its GDP to come in at 8% soon. For added perspective, the last time China GDP was above 8% was the first quarter of 2012, and it hasn't been above 10% since the second quarter of 2010.

Return to Page 1

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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.	The economic conditions reported in the January Beige Book will set the agenda for the next FOMC meeting and is likely to have some bearing on the pace of tapering of the Fed's monthly asset purchase program.
U.S. Consumer Price 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.	I've elevated CPI on the investor watch list this month, as the one indicator that I believe can give investors the best understanding of the Federal Reserve's current thinking. Right now, CPI has been running 1.2%, a modest uptick from October's very discouraging 1%. Some FOMC members have said they would pause tapering based on CPI, so I want to make sure the January reading doesn't soften. CPI is a guidance metric that's become more in focus than it's been in years and must be watched.
Q4 SPX Earnings Intensify An estimated 75 S&P 500-listed companies are expected to report earnings during the four-day week of January 21.	Q4 earnings intensify during the third week of January, with 75 S&P 500 companies expected to report, including many industrial and technology names. Expectations are for EPS growth to accelerate over the prior quarter.
BOJ December Minutes The Bank of Japan (BOJ) releases minutes from its December 19-20 meeting.	While the rest of the world is looking for growth from Japan, it is the only country where the Street, including myself, expects GDP to contract in 2014. Japan will need to come up with policies to offset the increase in the consumption tax from 5% to 8% that takes place in April 2014. Prime Minister Abe and the very determined BOJ Governor Kuroda will need to take the fight for growth up to another level. We'll probably see Japan introduce some fiscal policies in 2014 that could lower the corporate tax rate, as well as policies focused on increasing nuclear power generation to help offset some of the substantial energy imports just released in Japan's latest trade balance figures. We can also look for the expanded Trans-Pacific Partnership trade pact to be completed. Most important for Japan in 2014 will be keeping the yen as the funding currency for the global carry trade. Japan will be a very integral part of the overall global risk asset story in the first quarter, and January should set the tone.
Q4 SPX Earnings Halfway During the week of January 27, 118 S&P 500 companies are expected to release earnings.	Q4 earnings intensify during the third week of January, with many industrial and technology companies reporting. By the end of that week, we should be halfway through S&P 500 earnings.
U.S. State of the Union Address President Obama gives his annual State of the Union address on January 28.	I expect the looming debt ceiling deadline will be a major topic of the president's State of the Union address. Also, with 2014 being a mid-term election year, I think investors can expect him to use this speech as an opportunity to initiate the campaign season for the Democratic Party.

Return to Page 1

January indicators / events of note:

FOMC Meeting Concludes

Following its January monetary policy meeting—the first under the leadership of Janet Yellen—the Federal Open Market Committee (FOMC) releases its first statement of 2014.

You should be watching:

I expect the first FOMC meeting of 2014 to be more ceremonial in nature and a welcome to Janet Yellen as the new chairperson, succeeding Dr. Bernanke. In order for the Fed to enact substantive further tapering of its monthly asset purchases, we'd need to see a strong acceleration in January's economic figures. The Street expects a $10 billion cut in monthly asset purchases at each of the next seven of the FOMC's meetings, with a $5 billion cut at its final 2014 meeting in December. However, I expect the Fed will need to be more aggressive with its tapering pace and that the program will be completely wound down by the July 30 FOMC meeting.

2014 FOMC Meeting Schedule:

> January 29
> March 19
> April 30
> June 18
> July 30
> September 17
> October 29
> December 17

Return to Page 1

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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