Wealth Effected How?

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

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With the arrival of September, the moment of Fed tapering (or not) is upon us. While I still expect the FOMC will taper from its current $85 billion pace in monthly asset purchases, I also expect it will announce the taper with dovish language underscoring how rates will remain historically low. The Fed won't begin tapering without making sure the markets feel comfortable that it stands ready to support risk assets again if necessary. The bigger question to be answered in the months ahead is how will tapering impact the "wealth effect" observed among U.S. consumers, who tend to spend more disposable income when their investments and home values are rising. For the last few years, the FOMC's actions have succeeded in creating a strong tailwind in asset prices (both stocks and bonds) and home values. When tapering is implemented, will we see the wealth effect tailwind start to diminish?

September 2013

Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
1 **China PMI (August)**	2 **Labor Day (U.S. Trading Holiday)** **European PMIs**	3 10:00 AM: **U.S. ISM Manufacturing**	4 2:00 PM: **Fed Beige Book**	5 **Bank of Japan Meeting**	6 8:30 AM: **U.S. Labor Report**	7 **China Trade Balance**
8	9 **U.S. Senate and House Return**	10 **China Retail Sales and Industrial Production**	11	12 8:30 AM: **U.S. Initial Jobless Claims**	13 8:30 AM: **U.S. Retail Sales**	14
15	16 8:30 AM: **U.S. Empire State Manufacturing Survey**	17	18 2:00 PM: **FOMC Statement and Economic Projections** 2:30 PM: **FOMC Press Conference**	19 10:00 AM: **U.S. Existing Home Sales**	20	21
22 **Germany's Federal Election**	23	24 9:00 AM: **U.S. S&P Case-Shiller HPI**	25 10:00 AM: **U.S. New Home Sales**	26	27	28
29	30 **China PMI (September)**					

Times shown are Eastern Time.

September indicators / events of note:	You should be watching:
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.	The emerging markets continue to struggle year to date. However, I still believe this is a cyclical trend within a larger secular bull trend. For the remainder of 2013, I do not expect emerging markets to overtake any of the currently favorable overweight areas of investment opportunity, such as small caps. When stabilization eventually returns to the emerging markets, it will start with China. Last month's reported China PMI for July was 50.3, up slightly from June's 50.1. China PMI has not had a print above 51 since April 2012. Plain and simple, the August PMI will tell us if China is starting to lay the foundation for stability in the emerging markets.
European PMIs Each country's PMI is a key measure of the state of its manufacturing sector. An index value above 50 indicates growth, below 50 contraction.	As I wrote in my blog "Europe: One Year Later," Europe has become investable once again. U.S. investors will return from the Labor Day holiday to get a look at Europe's manufacturing data for August. The U.K. has been posting strong PMI figures, achieving a 54.6 last month compared with 47.9 in February. Also last month, German PMI rose to 52, and even France edged closer to surpassing 50, with a reading of 49.7. Overall eurozone PMI was 51.3 last month. Keep in mind, eurozone PMI was at 44.0 just over a year ago, in July 2012, when eurozone bond yields were spiking.
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.	ISM Manufacturing came in at a very healthy 55.4 last month, with significant improvement in the new orders-to-inventory ratio as well. While the figures reported in August point to a modest rebound and stabilization in manufacturing, investors should be prepared for this month's ISM reading to not be as strong. In fact, we could see some moderation, possibly two full percentage points less, in the August data reported in the September report. Even if the reading does slip to 53.5 as expected, that would still be much better than the 49.0 for May that was reported in June, and would suggest that the second quarter impact of the sequester has been digested by the market.
Fed Beige Book FOMC commentary on current conditions in each of the Federal Reserve's 12 districts is released two weeks prior to the next FOMC meeting.	The Beige Book released on September 4 will give us a sense of the agenda for the September 17-18 FOMC meeting, which is when the Fed is expected to start tapering its monthly asset purchases.
Bank of Japan Meeting The Bank of Japan (BOJ) holds its monthly monetary policy meeting on September 5.	At its August meeting, the BOJ kept its policy in place and its economic assessment unchanged. The yen is in a position to depreciate further, and I expect to see Japan continue in its commitment to more of the same, extremely accommodative monetary policy. Also worth following in Japan this month is BOJ Governor Kuroda's speech at the National Securities Industry Convention in Tokyo on September 19.

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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.	Clearly, Wall Street is anticipating an incredibly important jobs report in September. Last month's report was a disappointment, rooted in a headline figure that only added 162,000 new jobs to the economy, with private payrolls increasing just 161,000. I expect marginally better figures for August that might be enough to confirm my expectation for tapering to start in late September. Consensus estimates call for both headline and private payrolls to gain 165,000 to 175,000 jobs, and for the unemployment rate to remain unchanged at 7.4%.
China Economic Data > **Trade Balance** – China's monthly trade report provides important import, export, and interest rate data on its economy. > **Retail Sales** – The monthly retail sales report tracks total receipts at stores that sell durable and nondurable goods across China. > **Industrial Production** – This monthly indicator measures changes in output for the industrial sector of China's economy, including manufacturing, mining, and utilities.	Last month, China reported an overall trade surplus of $17.82 billion, which is favorable for further yuan appreciation. Exports were up 5.1%, and imports rose 10.9%, year on year. While these are certainly nowhere near the robust figures of a few years ago, they were an improvement over what was reported for June. Again, as is the case with China PMI, investors should look for any indication of a stabilization trend in China, such as double-digit growth continuing for imports, and exports moving back toward double digits. China's retail sales and industrial production data also showed slightly better stability last month. Retail sales were up 12.8% for July, and we are expecting unchanged or slightly better growth in August. Last month, industrial production rose 9.4%, and we're looking for a print that is either unchanged or slightly higher in August, possibly back above 10%.
U.S. Senate and House Return from Summer Recess On Monday, September 9, U.S. policymakers get back to work on Capitol Hill.	With Washington back in session, the contentious argument about raising the debt ceiling resumes and will intensify in October. Some of the discussion will center on who will be the next Fed chairman. Janet Yellen, the Fed's current vice chair, is clearly favored by Wall Street, while economist Lawrence Summers is viewed in a negative light and as more of a political choice. Based on the reaction of the equity market in August to Mr. Summers' candidacy, the Street doesn't appear to like that prospect. I expect asset prices will continue to be highly sensitive to media coverage of this topic in the days ahead. The one potentially favorable concession the Republican-controlled House could get from the Obama administration is a lower corporate tax rate. For now, changes to investor portfolios are not warranted in connection with the renewal of the debt ceiling debate this fall.

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U.S. Initial Jobless Claims The U.S. Labor Department issues a weekly report on the number of individuals filing for first-time unemployment benefits. An increasing (decreasing) trend suggests a deteriorating (improving) labor market.	As I recently discussed in my blog "Dual Mandate: Labor and Inflation," weekly initial jobless claims reports continue to provide evidence directly related to one of the Fed's key mandates, the reduction of unemployment. Initial jobless claims have been trending lower, hitting their lowest levels in August since October 2007. The September 12 jobless claims report is particularly important as it gives the FOMC one last look at employment figures before its September meeting. Although the monthly U.S. labor report has been erratic in providing consistent evidence of progress in the employment picture, the initial jobless claims reports have clearly shown a well-defined trajectory of improvement over the last 12 months.
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.	What did consumers do during their back-to-school shopping season in the first few weeks of August? This month's retail sales report will tell us whether consumers are feeling wealthier from rising asset prices and home values and therefore spending more. Last month retail sales were up 0.4%. Expectations are for August retail sales to have modestly risen. Using history as a guide, we will want to see some acceleration in retail sales figures now through December. There has not been a negative U.S. retail sales report for the month of August since 2008.
U.S. Empire State Manufacturing Survey This monthly indicator provides useful intelligence on regional manufacturing conditions within the New York Federal Reserve district and is a useful indicator of national manufacturing trends.	U.S. manufacturing has continued to stabilize and strengthen. The FOMC gets its last piece of manufacturing data to consider ahead of its September meeting with this regional manufacturing report from New York's tri-state area. Since recording a -1.43 print in May, this index has produced strong readings for the last few months: 7.84 in June, 9.46 in July, and 8.24 in August.
FOMC Statement, Press Conference, and Economic Projections Following its September 17-18 monetary policy meeting, the Federal Open Market Committee (FOMC) releases its statement and quarterly economic projections, and Chairman Bernanke hosts a press briefing.	I continue to expect the FOMC will start the tapering process at its September meeting, reducing its monthly asset purchases from $85 billion to somewhere between $60 and $75 billion. The potential also exists at this meeting for the Fed to lower its outcome-based guidance for the unemployment rate to 6% from 6.5%. In my view, the investment community has spent too much time concerned with the start of tapering when the end is what matters most. Including the September meeting, there are only two FOMC meetings left in 2013 (October 29-30 and December 17-18) and seven meetings before the Street expects the tapering to be completed, at the meeting scheduled for June 17-18, 2014.

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U.S. Housing Indicators > **Existing Home Sales** – This monthly report from the National Association of Realtors provides sales-closing data on previously constructed homes, condos, and co-ops. > **S&P Case-Shiller Home Price Index (HPI)** – This index, released on a two-month lag, tracks changes in the value of residential real estate in 20 metropolitan regions across the U.S. > **New Home Sales** – Issued monthly by the U.S. Census Bureau, U.S. Commerce and Housing Departments, this report reveals the number of newly constructed homes with a committed sale.	Whatever the Fed's announcement is on September 18, we'll want to measure its impact on housing, which is a key piece of the wealth effect, as I discussed in my opening comments. On a day-to-day basis, we can measure the impact on asset prices, the other wealth effect component, by looking at the movement of the stock and bond markets. However, our access to housing data is more limited. At the end of September, we'll get our first look at how housing is being impacted by interest rates moving toward 3%. Last month existing home sales were up 6.5%, month on month, to 5.39 million, the highest reading since November 2009. Also last month, the S&P Case-Shiller Index reported that home prices had risen over 12% year to date. Some of the greatest home price appreciation has been in the so-called "sand states" of California, Arizona, and Nevada, the same states where home prices contracted significantly during the 2008 crisis. Will perceived higher home values translate into increased consumer spending? Housing data will also be important for telegraphing the pace of Fed tapering. Once the Fed starts tapering, I don't expect it to reverse course, however, it could extend the length of the taper runway if the housing market starts to slow. For July, new home sales were down 13.4% month on month, to 394,000, the lowest figure in seven months. From January through June, monthly new home sales stayed above 439,000. That was the first chink we've seen in the housing market's armor. How will rising rates impact home sales going forward?
Germany's Federal Election Germans head to the polls on September 22 to elect a new parliament for the eurozone's largest member state.	Europe's economic improvement increases the chances that Chancellor Angela Merkel will be reelected to a third term and her Christian Democratic Union Party will retain control of the German government. Merkel is running against the finance minister from her first term, Peer Steinbruck, head of the Social Democratic Party. Similar to what happened in President Obama's reelection campaign, Chancellor Merkel's greatest opponents are German economic indicators and the fate of the eurocurrency over last 12 months. With both the economy and currency working in her favor, it would be very surprising if she lost the election.

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Joe Terranova is chief market strategist for Virtus Investment Partners. He was elevated to that position in June 2009, having started with the company in the role of 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.

In 2007, Mr. Terranova and Hockey Hall of Fame player Mike Bossy established "Bossy's Bunch," a program that rewards excellence in the classroom for elementary school students.

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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