

Morning Call

Friday, 3 September 2010

Latest Market Headlines

US payrolls seen falling, private hiring tepid

US employment likely fell for a third straight month in August as more temporary Census jobs ended and cautious businesses scaled back hiring, an outcome that could pressure the Federal Reserve to prop up growth. Median market forecasts are for a net fall in employment of 100,000 after a drop of 131,000 in July. Private payrolls, a better barometer of the labour market's underlying health, are seen rising only 41,000, well below the 71,000 jobs added in July. Against the backdrop of weak data such as housing, larger than expected job losses last month could heighten fears the US economy is sliding back into recession and push the Federal Reserve closer to launching a fresh round of government bond buying. A downbeat report would also further dim the chances of Democrats holding their majorities in the US Senate and House of Representatives in mid-term elections in November.

The bar is set fairly low for today's jobs report, but if we get a much larger decline than market projections, with weakness particularly evident in private employment, then that would raise the odds of a double-dip recession.

Japan capex slows, Q2 GDP seen revised up

Japanese companies cut capital spending in April-June by a less than expected 1.7% from the same period last year, pointing to an upward revision of an anaemic preliminary reading for second-quarter GDP growth. But the strong yen and slowing exports to major destinations such as the United States and China may hurt business sentiment and corporate willingness to spend, boding ill for the economic outlook. The 1.7% fall in capital spending for April-June was slower than the median market forecast of a 6.5% decrease and an 11.5% drop in the first quarter.

The better showing in capital spending reflected improving corporate profits, a trend that is likely to continue for now. But given that some signs of a slowdown in the economy are emerging, there is a risk that the appetite for corporate capital spending may be curbed.

The Fundamentals: The Economist's View

US Treasuries

US Treasuries were mostly steady in Asian trade on Friday, with the focus on whether the August payrolls figures will provide a catalyst for a further rebound in the benchmark 10-year yield from last week's 19-month low. ***Another factor to watch is whether Japanese investors trim their holdings of foreign bonds including Treasuries ahead of the close of Japan's fiscal half-year at the end of September. Data released in recent days showed that Japanese investors applied the brakes on their foreign bond buying last week, with net buying dropping to 70.8bn yen (\$840.1m), the smallest weekly amount since early May. Their net purchases since early April total roughly \$177bn.***

Eurozone Bonds

German government bonds were steady at Friday's open with markets cautious ahead of the US jobs data. The risk is that a slightly weaker number will lead to a sell-off. It could be sell on a weak number, sell on a strong number. We think it would have to be a seriously weak number to get bond prices pushing higher again. However, we don't necessarily see the current back-up in yields as the end of the bond bull market. ***We acknowledge that fundamental valuations are looking stretched, but we still see good reasons why yields can stay lower for longer and expect the 10-year Bund yield to hold within the 2.00% to 2.50% range for the time being.***

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UK Gilts

After disappointing data on the manufacturing sector this week, the focus this morning turns to the services sector, with the release of the August PMI. The market is looking for a marginal fall in the index to 52.9 from 53.1 in July, but the risks are tilted to the downside. However, the reading is likely to remain well above the 'neutral' 50 level. **Overall, the latest PMI surveys are not expected to impact on the Bank of England meeting next week, where no change in monetary policy is anticipated. That said, a fall in the services PMI this morning should be negative for sterling but positive for Gilts.**

Other Bonds

New data released yesterday showed that the Swiss economy powered ahead in the second quarter as companies' investment spending fuelled growth as exports and consumer spending were steady. Switzerland's GDP grew by 0.9% from the previous quarter in real terms, almost matching the 1.0% growth from the first three months of the year. The Swiss economy has weathered the crisis better than many of its European neighbours thanks to its resilient consumers and the Swiss National Bank (SNB) forecasts growth of around 2.0% for this year. However, recent surveys have indicated that the recovery is set to slow in the coming months as the cooling of the US economy and the strong Swiss franc are taking its toll. Still, the Swiss economy is performing very well, arguing for a tightening of monetary policy by the SNB sooner rather than later. **We don't expect a move this month, but if the economy holds up between now and year-end, then a rate hike at the December quarterly policy meeting cannot be ruled out, pushing short-dated bond yields higher and lending further support to the Swiss franc.**

Key Economic Indicators / Events of the Day

Time (BST)	Country	Release	Period	Bloxham	Median	Last
8.00	Europe	ECB Executive Board member Jose Manuel Gonzalez-Paramo and Norges Bank Deputy Governor Jan Qvigstad participate in panel discussion at the Money, Macro and Finance Conference at the Cyprus University of Technology, in Limassol, Cyprus				
8.00	Eurozone	ECB Governing Council member Ewald Nowotny participates in a panel discussion at the European Forum Alpbach 2010, in Alpbach, Austria				
9.00	Eurozone	Services PMI	Aug Final	55.6	55.6	55.6
9.00	Eurozone	Composite PMI	Aug Final	56.1	56.1	56.1
9.30	UK	Services PMI	August	52.5	52.9	53.1
10.00	Eurozone	Retail Sales	July	-0.2%	+0.2%	Flat
12.00	EU	EU Economic and Monetary Affairs Commissioner Olli Rehn holds a news conference, in Helsinki				
13.30	US	Non-Farm Payrolls	August	-98,000	-100,000	-131,000
13.30	US	Unemployment Rate	August	9.5%	9.6%	9.5%
13.30	US	Average Earnings	August	+0.1%	+0.1%	+0.2%
15.00	US	Services PMI	August	53.0	53.5	54.3
15.00	US	Federal Reserve Bank of Atlanta President Dennis Lockhart speaks on the economy at an event hosted by East Tennessee State University, in Johnson City, Tennessee				
15.30	US	ECRI Leading Indicator	w/e Aug 27	121.5	121.2	120.9

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Today's Debt Auctions /Buybacks/ Announcements

UK sells T-bills.