

DAILY GLOBAL COMMENTARY

Northern Trust  
Global Economic Research  
50 South LaSalle  
Chicago, Illinois 60603  
northerntrust.com

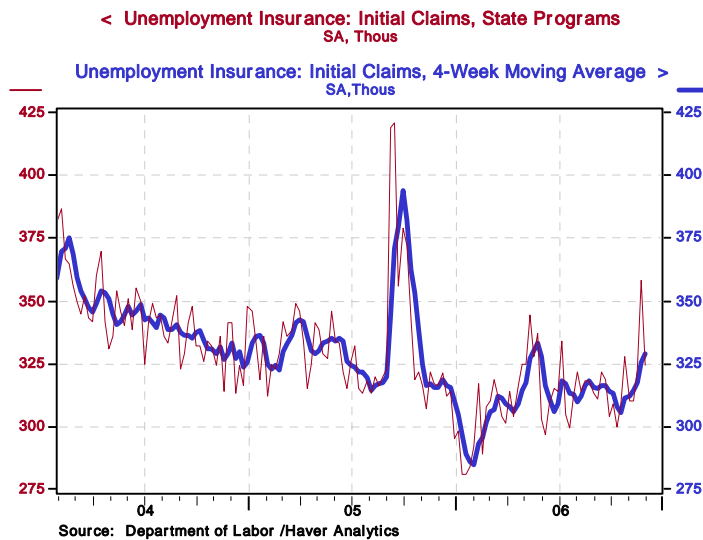
Asha Bangalore  
agb3@ntrs.com

**Hiring Remains Sluggish, Additional Information Will be Available Soon**

December 7, 2006

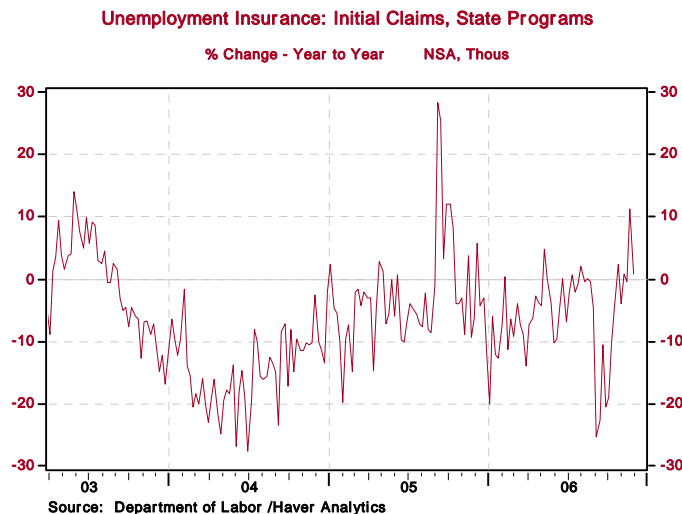
Initial jobless claims dropped 34,000 to 324,000 during the week ended December 2 after a sharp gain of 35,000 in the prior week. Although the two weekly changes in initial claims leave the level nearly unchanged compared with the reading of the week ended November 18, the underlying trend remains sluggish. The 4-week moving average at 329,000 has steadily climbed from a low of 306,000 during the week ended October 21 (see chart 1).

Chart 1



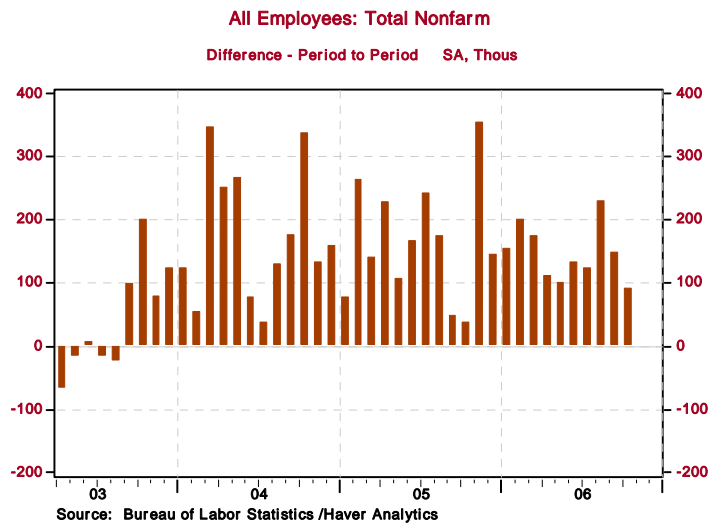
Moreover, the year-to-year change in initial jobless claims has held positive for four out of the last six weeks (see chart 2). Continuing claims, which lag initial claims by one week, rose 57,000 to 2.524 million and the insured unemployment rate held steady at 1.9%.

Chart 2



The November employment report, to be published on December 8, will refute or reinforce the current perception of a very sluggish demand for labor. The unemployment rate is expected to edge higher to 4.5% in November vs. a 4.4% reading in October. An increase of 110,000 in payroll employment is expected compared with a gain of 92,000 in October. Market expectations are similar to our forecast.

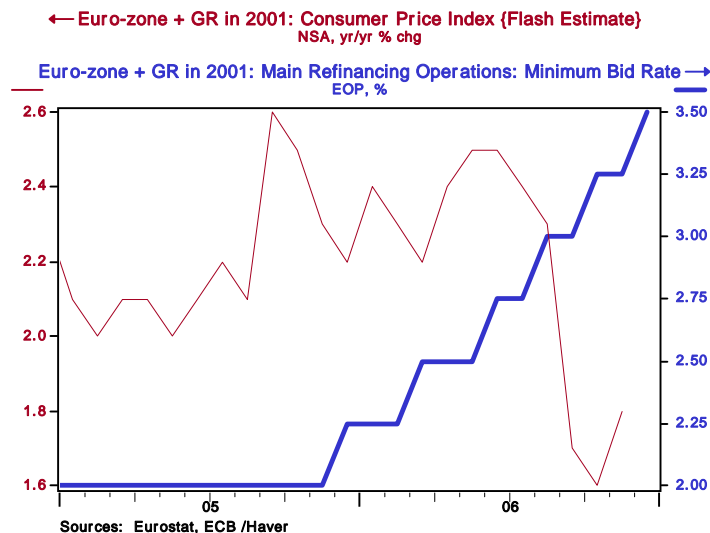
Chart 3



Victoria Marklew  
[vem1@ntrs.com](mailto:vem1@ntrs.com)

### ECB: Today's 25bp Hike Unlikely To Be The Last, But The End Is In Sight

As usual, the most interesting part of this morning's policy meeting at the European Central Bank (ECB) was not what happened – another 25bp increase in the refi rate, as expected, taking it to 3.50% – but what was said. Between the accompanying statement from the Governing Council and the subsequent press briefing from Governor Trichet, it is obvious that the overall stance remains hawkish, but also that the end of the tightening cycle is approaching.



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The still-hawkish-stance was revealed by the use of such phrases as “our policy continues to be accommodative,” “money and credit growth [are] strong and liquidity in the euro area [is] ample,” the Council “will monitor very closely all developments,” and “looking ahead, acting in a firm and timely manner to ensure price stability in the medium term is warranted.”

That Trichet and company are becoming less hawkish was revealed by the absence of a key sentence from past monetary policy statements: “If the ECB’s economic assumptions were confirmed, the central bank would continue to withdraw monetary accommodation from the economy.” And, Trichet was adamant in his refusal to comment on what the Council anticipates doing in February.

As we noted last week (Daily Global Commentary, [November 30: “Euro-zone Data Point to Healthy Economy and Higher Rates in 2007”](#)), recent credit, money supply, and inflation expectations data indicate at least one more rate hike in Q1 – if not February 8, then March 8. Whether there will be a final hike in Q2 will depend on how the Euro-zone economy develops over the next three months. Trichet pointed out today that although the Euro-zone economy is expected to grow “at solid rates around potential” next year, the risk forecast has now shifted from “balanced” to “on the downside.”

For the remainder of this month, Euro-zone dates to watch include our two favorite leading indicators, the German Ifo on the 19<sup>th</sup> and the Belgian business indicator on the 20<sup>th</sup>, and Euro-zone money supply and credit data on the 29<sup>th</sup>.

### **Bank of England Stands Pat But Policy Outlook For 2007 Remains Uncertain**

As expected, the Bank of England’s Monetary Committee (MPC) left the repo rate at 5.0% today. With sterling in the ascendant and the manufacturing sector apparently starting to suffer, many analysts assume that rates have hit their peak for this cycle. We continue to feel that although another rate hike in Q1 2007 is not a sure bet, nor can it be ruled out. The outlook remains uncertain.

The details of today’s policy debate will be revealed when the minutes are published on December 20<sup>th</sup>. It will be interesting to see what the members made of the past week’s data, which were decidedly mixed. The housing market and services sector continue to accelerate, but manufacturing activity unexpectedly stalled.

According to today’s report from the Halifax, annual house price inflation hit a 20-month high in November, with prices rising 1.7% on the month and 9.6% on the year, versus 1.8% and 8.6%, respectively, in October. Last week, the Nationwide building society reported a 1.4% monthly jump in prices in November, taking the annual rate to 9.6%, the highest since February 2005.

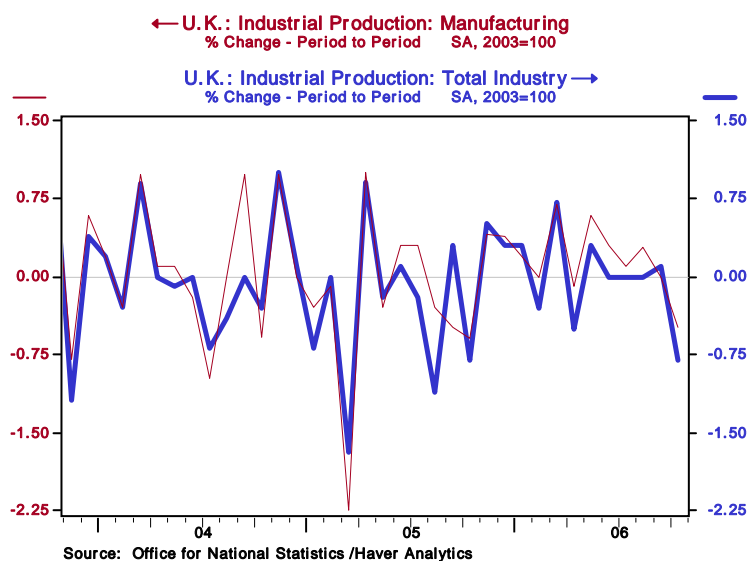
According to Tuesday’s CIPS/RBS Services PMI, the service sector – which accounts for about three-quarters of the total UK economy – grew at its fastest pace in nearly three years in October. The index rose from 59.3 in October to 59.8 in November, the highest reading since January 2004 and one of the strongest in the survey’s 10-year history. The “prices charged” index eased for the

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third straight month, 52.9 in November versus 53.0 in October, but companies took on more workers than at any time in the past eight years. That suggests that the labor market may be on the verge of another round of tightening, which would put upward pressure on wages. As we've noted often recently, the MPC is concerned about the January pay round. If wages start to rise, they will be more inclined to tighten further.

In contrast, yesterday's industrial sector data showed output slipped in October for the first time in over a year, down 0.8% on the month, while manufacturing dipped 0.4%, its biggest contraction in a year. Unusually mild weather may have played a role, but last week's CIPS/RBS Manufacturing Purchasing Managers' Index for November also fell, coming in at 52.6 versus a (downwardly-revised) 53.5 in October, to record the lowest reading since March. In particular, orders slowed, suggesting that the rising pound may be starting to dent export orders.



Chancellor Brown's pre-budget statement yesterday was upbeat about the state of the economy – raising this year's growth forecast to 2.75%, keeping next year's forecast at 3.00%, and nudging up the trend rate of growth from 2.50% to 2.75%. The growth outlook for this year looks about right, as does the new trend assessment, but cheerfully expecting 3.00% real GDP growth in 2007 looks overly optimistic – but then, Brown's a politician looking to take over as PM in the first half of next year, so he could hardly be expected to be anything but upbeat.

In terms of this month's data, key numbers to watch will be November inflation on the 12<sup>th</sup>, October unemployment and average earnings on the 13<sup>th</sup>, and November retail sales on the 14<sup>th</sup>.

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