



Hadrian Brief

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Growth and Inflation

The global economy is expanding at a slow rate with the U.S. showing relative strength to Europe and Asia. The OECD's recent outlook sums up the growth backdrop. 2012 growth was projected at 2.0% in the U.S. up from 1.7% in 2011, while growth in Europe was forecast to rise 0.2% in 2012 compared to 1.6% in 2011. China and India were expected to expand at 8.5% and 7.2% respectively in 2012 down from 9.3% and 7.7% in 2011. Europe continues to suffer fall out from the sovereign debt crisis and austerity measures, while India and China are facing the lagged effect of macro tightening measures. The U.S. economy is benefiting from easy monetary and loose fiscal policy along with a restructured corporate sector.

Inflationary pressures are declining. Headline inflation numbers have dropped sharply in China and India over the past month, while inflation measures in Europe and the U.S. are contained. Core inflation is rising 2.2% in the U.S. and 1.6% in the EZ. Commodity prices are moderating. The UN's food index was flat month on month in November, but is down 10% from its February peak. At the same time, OPEC appears ready to keep oil supplies ample and cap energy prices. Aggregate demand has weakened globally, and is limiting pricing power. The major deflationary threat remains a buckling Chinese real estate market. The China Index Academy indicated that home prices fell for a third straight month in November with prices in Shanghai down 40% from their mid 2009 peak. There are also reports that Beijing has a two year supply of homes to be sold.

Money Markets

Treasury prices are expected to trade reactionary to sovereign credit risk in Europe and global economic trends. The Fed's twist continues to pressure yields at the long end of the curve and offset heavy issuance by the Treasury. U.S. economic growth is firming as rail traffic is strong and initial unemployment

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claims have been consistently below 400,000 in recent weeks. The market appears skeptical of domestic growth trends, and it may take strong holiday sales to generate selling. After a robust start, holiday spending has been in a lull. Internationally, manufacturing PMI readings below 50 in the Eurozone and China and a contraction in Indian industrial production are providing support. The trade does not seem to believe that the U.S. economy can see run away growth without the rest of the World showing economic strength. Valuation remains poor given the 10 year treasury yield is below the year over year core inflation rate. However, the Fed's twist is sucking up new issuance and capping yields. Treasuries have persistently shown poor valuation compared to corporate debt and equities. Statements by the head of the IMF saying the global economy could face a 1930's style scenario are helping to provide price support and causing investors to look the other way on valuation.

Foreign Exchange

The FX market will be a function of dollar demand at year end and relative growth differential. Basis swaps continue to show European institutions short dollars. The ECB is working to provide liquidity, but banks need dollars and there is a reluctance to lend to EZ banks in light of the sovereign debt crisis. The FX market will be sensitive to the need for dollars in the New Year, when funding pressures could relax and central bank actions could have a greater impact. Furthermore, U.S. economic data has been strong to expectations in recent weeks and U.S. economy is outperforming Asia and Europe on a relative basis. Growth and inflation trends are reducing the ability of the Fed to undertake additional measures of stimulus, while the ECB and Asian central banks are in position to provide policy accommodation.

The **euro** remains pressured by the lack of resolution to the sovereign debt crisis, signs of recession, and the likelihood of additional monetary ease by the ECB. There are two

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potential positives for the euro. First, the recent decline in 2 year yields in Italy, Spain, and Belgium suggests that the ECB may be successful in providing stability via its 3 year loan program. Second, the euro is against the January 2011 low at 1.2867 and subject to technical support. The **sterling** will be pressured by signs of weak consumer spending, a slowdown in the manufacturing activity, and sluggish job creation. There could also be some pressure on the sterling if inflation starts to fall as expected in 2012. However, turbulence in the EZ will provide support as investors look for alternatives to the euro and the U.S. dollar. The **Swiss franc** will be pressured by the SNB's desire to cap gains. At its last meeting, the SNB said it was ready to take additional measures to weaken the franc if needed. The SNB appears worried about deflation and slow growth in the wake of the euro crisis. As a result, it is willing to fight capital inflows related to safe haven and euro alternative. The **Canadian dollar** has been pressured by weaker commodity prices and the general U.S. dollar rally. The economy continues to move forward, but a weaker labor market and a softer tone in recent export and manufacturing sales data has undercut support for the currency. The Canadian dollar remains supported by diversification flows. The **Australian dollar** will be sensitive to Asian growth, commodity prices, and the outlook for monetary ease. The real estate slowdown in China and contraction in India's industrial output have cooled the growth picture of Asia and seem to be spilling into the Australian economy. Labor and export data have shown weakness. The RBA is likely to continue on its path toward rate cuts given low inflation expectations and soft growth. The **yen** remains range bound against the U.S. dollar. The currency seems capped by the threat of intervention or BOJ policy to stem yen gains. The economy is not showing a powerful recovery post the earthquake, and the yen's strength is a drag on growth. However, the low rate structure in the OECD and turbulence in Europe are providing support. Capital flow data has shown a pick up in foreign bond

buying by Japanese investors in recent weeks, but the magnitude of gain is not dramatic. Technical traders will be watching the recent EUR/JPY low of 100.76. This level could provide the foundation for a pivotal move.

Equities

The U.S. equity market will be sensitive to the outlook for profit growth in the face of relatively cheap valuation and moves by corporations to unlock value. Although the U.S. economy has shown positive momentum and the upward slope to the Empire and Philly surveys argue for flat to higher stock prices, weak growth overseas and the sovereign debt crisis are weighing on the profit outlook. The S&P 500 is expected to earn \$103/share over the next 12 months. The market looks attractive at 11.8 times forward earnings in a world where cash yields nothing and the 10 year treasury yield is below 2.00%. However, EPS estimates have been easing lower. Corporations have provided a mixed picture on the profit outlook. On the bullish front, FedEx provided firm guidance and suggested solid economic activity. Adobe, Aetna, Broadcom, United Technology, and Coca Cola Enterprises have provided a friendly profit picture. However, Intel, Texas Instruments, Accenture, Pentair, Nordson, Research in Motion, and Schwab have recently lowered guidance. Inexpensive valuation and measures to boost shareholder value are highlighted by ConocoPhillips and Pfizer adding to their \$10 bln repurchase plans. The market has also seen a number of aggressive dividend hikes. Discover Card (+66%), Disney (+50%), and Waddell & Reed (+20%) provide examples. Covidien and Sunoco have recently announced spin offs. These events will entice investors to remain invested.

Commodities

Commodity prices will be sensitive to the trajectory of economic growth, the strength of the dollar, and investment flows. The downshift in global growth and a strong dollar

have pressured the CRB by prompting fund selling into year end. As a result, the total return for CRB in 2011 was off 11% through mid December and commodities were badly lagging the return on the S&P 500 and 10+ year treasuries which were down 1.4% and up 33.2% respectively. Looking at individual markets:

The **oil** market will be trying to digest the implications of the OPEC meeting, while it keeps an eye on geopolitics and the pace of global growth. OPEC agreed to a production ceiling of 30 mbd which is near current output, but up from the prior 24.8 mbd quota. On one hand, the upward ceiling is seen as cutting down on the potential for cheating and is aimed at providing group cohesion. On the other hand, some will see the higher ceiling as a reason to boost production. The compliance track record of OPEC has been weak in recent years. Current supply and demand trends are mixed. U.S. oil stocks are falling consistent with the normal seasonal pattern. There was a 22.6 day supply of crude in storage compared to a 23.8 day supply a year ago. However, gasoline inventories have surged in recent weeks and are up more than the normal pattern. There was a 25.3 day supply of gasoline compared to 23.7 last year. Gasoline demand is down 4.5% y/y over the past 4-weeks and has been persistently weak, creating a bearish dynamic for the oil market. Distillate inventories have recovered in recent weeks after a sharp decline. The distillate market is more supportive to the price of crude oil than the gasoline market. The days supply is 37.3 compared to 43.3 last year. Demand has weakened on the back of mild weather. Distillate demand is up 1.8% y/y over the past 4-weeks and has slowed from a mid single digit growth rate in late October early November. In China, oil demand rebounded in November to 9.5 mbd – the second highest level of demand on record. Record refinery runs were noted, and the country moved to reduce a diesel shortage. The IEA is projecting Chinese demand to average 10.0 mbd in 2012. However, underlying economic growth has

slowed, which may dampen oil demand once diesel inventories normalize. Likewise, India's demand growth could slow as its economy struggles and the rupee has plunged. Geopolitically speaking, Iran has threatened to close the Strait of Hormuz and tensions are high given the recent downing of a U.S. drone over Iranian airspace. These factors could cause a risk premium to surface from time to time.

Natural gas prices will be sensitive to weather and the pace of withdrawal. A mild December has left the market in oversupply. As of the week ending December 9th, there was 3,729 Bcf in storage. Storage levels were 4.3% ahead of last year and 10.3% above the 5-year average. As of December 16th, NOAA's 8 to 14 day forecast projected above normal temperatures across the upper Midwest and into the East Coast. Below normal temps were expected in the deep south from New Mexico to Florida. The pattern of weather argues for soft heating needs and temps need to chill to improve the price outlook. Heating degree days for the U.S. were 39 below last year as of the week ending December 8th. Below the surface, there were a number of major pipeline outages. El Paso's Ruby Pipeline, the Millennium Pipeline, and the Bison Pipeline were experienced disruption, and may have weighed on spot prices, temporarily. In its weekly report, the DOE noted that gross natural gas production was up 6.9% y/y in the week ending December 14th, while consumption was off 7.7% y/y led by a 12.5% decline in residential and commercial usage.

Gold prices have been pressured by liquidation linked to a strong dollar and fund positioning at year end, but data on positioning suggests the market remains very long. Recent CFTC data showed managed money reducing the net long by slightly more than 15,000 contracts, but this category of traders was still a net long of approximately 135,000 contracts. Gold ETF holdings are off their high, but still very elevated at 75 mln ounces. Outside of positioning, the Indian rupee has fallen sharply

in recent weeks, and may be undercutting demand from a large user group. Likewise, the global slowdown may be rationing demand in the emerging world and Europe. Gold will remain supported by uncertainty over the fate of the euro and lack of confidence in the U.S. political system. Real interest rates remain low to negative in the OECD and major central banks are cutting rates and expanding monetary policy. Signs of falling inflation in both the developed and emerging world could reduce gold's luster, presenting a downside risk.

Copper prices will be sensitive to the direction of global growth, especially the trend in the Chinese real estate market, which shows signs of faltering. The leading index of copper activity was down 0.8% y/y in October and has been pointing to slower usage into the first half of 2012. LME copper stocks are trending lower and suggest tightening supplies at 381,250 mts. Inventories in Shanghai have rebounded in recent weeks, but do not suggest abundance at 79,570 mts. Production disruptions due to strike activity have pressured inventory levels. In the short run, the market remains supported by constrained supplies, but high prices are leading to expansion bigger picture. Codelco is set to double output at its Antonio operation in Northern Chile to 60,000 mts a year. Copper miner Xstrata indicated that weak output at Chile's Escondida mine and the strike at Freeport -McMoRan would cause the market to be in deficit this year. However, Freeport appears to have ended the strike at its Indonesia operation. Wages are expected to rise 24% in the first year of the contract and 13% in the second year. The strike led the company to cut its Q4 sales forecast to 800 mln lbs of copper down from a mid October estimate of 915 mln pounds. Output should improve in the coming months, and the trade will be looking to see if inventory levels reverse higher.

Corn and Soybean prices will sensitive to South American production and the pace of export sales. Weather patterns are projected

to be dry in Argentina, but provide adequate soil moisture in Brazil. The risks to the Argentina's crop may provide price support given the large sell off in recent weeks. The market does not appear comfortable with South American growing conditions which may allow for a risk premium. On the demand front, U.S. export sales are lackluster. Corn and soybean export sales are down 41.4% y/y and 21.2% y/y over the past 4-weeks. Total commitments as a percent of total exports are tracking firm for corn at 57% compared to the 5-year average of 52%, but weak for soybeans at 62% compared to the 5-year average of 68%. The outlook for Chinese demand is mixed, and not likely to stoke speculative buying interest. China's corn output was revised higher by the National and Grain & Oils Information Center. The Center is projecting a record 191.8 mmts harvest. The forecast compares to a November estimate of 184.5 mmts. This could cut down on corn demand relative to expectations. However, the Center is projecting corn imports of 4 mmts in 2012, which is above the USDA's projection for 3 mmts. Lastly, the Center is projecting a reduction in Chinese soybean imports. Imports are projected at 5.0 mmts in January compared to 5.4 mmts in December and 5.7 mmts in November.

Wheat prices will be sensitive to the price of corn and soybeans, crop conditions in the Ukraine and U.S. Plains, and the pace of export sales. The area of plantings in the Ukraine is down 22% from a year ago hurt by dry weather. As a result, output from this region is likely to fall sharply. In contrast, weather patterns are expected to bring meaningful participation in Texas, Oklahoma and Kansas. The rains should bolster the outlook for winter wheat production. Export sales are weak and a drag on the market. Over the past 4 weeks, U.S. export sales are down 40.7% y/y. Total commitments as a percent of total exports is 71% compared to the 5-year average of 77%.

Cotton prices will be sensitive to export sales, international developments, and holiday apparel sales. The global crop appears ample. The USDA revised up its outlook for 2011/2012 ending stocks to 57.67 bales from 54.96 bales in November. China's imports were revised down and its ending stock revised up 2.0 mln bales to 15.55 mln bales. India and Brazil were also expected to see their ending stocks lift. The Pakistan Cotton Ginners' Association indicated that output may be 12.7 mln bales up from the government's estimate of 12.2 mln bales in October. The UDSDA has Pakistan's production at 10 mln bales. After bouncing sharply in October and early November, export sales have slumped in recent weeks. Chinese restocking seems to be exhausted. U.S. cotton export sales are down 39.9% y/y over the past 4 weeks. U.S. apparel sales in the holiday and profit numbers from Nike may influence pricing in the coming weeks by providing a picture of demand.

Cattle supplies are poised to expand into February, and will cause the market to focus on demand. The December Cattle on Feed report showed numbers up 4% y/y and highlighted the potential for supply to pick up near term. Placements rose 4% y/y, while marketings were flat compared to 2010. Domestic demand should ease post New Years, but the trade sector has been hot and price supportive. Beef exports in October were up 10.7% y/y, while imports fell 4.4% y/y. In the last week, export sales data showed beef shipments up 6.7% y/y. Packer margins are reportedly in the red and will slow cattle purchases. Retail beef prices averaged \$4.50/lb in November up 9.7% from last year. High prices could lead to substitution to pork and chicken. Cattle feeders look current and are not under pressure to be aggressive sellers. Slaughter was 642,000 head in the last week down 2.7% y/y, while dressed weights were 3 lbs above a year ago.

Hog prices will be driven by demand. The export market is strong and should offset the reduction in ham demand post Thanksgiving and Christmas. Pork exports in October rose

42% y/y. China, South Korea, and Japan have been strong buyers. At the same time pork imports were down 11% y/y in October pressured by a reduction in Canadian imports. The trade surplus in pork has contributed to record high retail pork prices. The USDA retail pork price in November was \$3.51/lb and could generate some substitution into chicken. By contrast, broiler prices were \$1.79/lb and down slightly from last year. Hog producers look current and the trend in supply seems consistent with the hogs and pigs report. In the last week, hot slaughter totaled 2.333 mln head down 0.5% y/y. Hog carcass weights are up about 1 lb from last year. Slaughter levels should pick up mildly compared to last year in Q1 2012.

The supply/demand balance for **coffee** appears price positive, but bullish supply factors could be undercut by concerns over the pace of global growth. The ICO indicated that global production would be 128.6 mln bags in the 2011/2012 crop year. Output is expected to be down from 133.1 mln bags in 2010/2011 due to poor growing conditions and damaged crops in exporting nations. The ICO cut its outlook for Columbia's crop 0.7 mln bags to 8.5 mln bags. Asian output was projected to fall 4.6% to 35.8 mln bags despite higher production in Indonesia. The caution toward output was echoed by Volcafe, which is projecting the 2012/2013 Brazilian coffee crop to be 55.7 mln bags compared to 57.6 mln bags in a similar two year crop cycle in 2010/2011. Flowering failed to lead to strong cherries and will cut into production. The possible short fall was confirmed by the Brazilian Growers Cooperative which said output in 2012/2013 would be 4.7% below the prior high yielding season in 2010/2011. Researcher Safras & Mercado is projecting Brazil's crop at 52.2 to 55.0 mln bags. Volcafe also believes the Columbian coffee crop may struggle to reach 7 mln bags. On the demand front, the ICO believes consumption is strong. Usage was estimated at 135.0 mln bags for 2010/2011 up from 131.9 mln bags the year prior. However, weak economic growth risks

dampening usage. The recent sell off in Green Mountain Coffee has coincided with concerns over slower demand for its coffee product.

Despite supply being revised down in a few regions, the supply/demand balance has loosened for **sugar**. Researcher Kingsman is projecting a 9.7 mmts surplus in the new crop year up 15% from the projection in October. Additional supply from Brazil and China was behind the forecast. China's production is expected at 12.57 mmts up from 12.0 mmts, while Brazil was projected to produce 32.77 mmts up from 31.19 mmts. Supportive to ample supply, Unica indicated that sugar cane output would be above 490 mmts and ahead of

the November estimate of 488.5 mmts. Planted area in 2012 is expected to rise 4.5%. Sugar production in the EU is expected to be a record in 2011/2012 up 15% to 18.25 mmts (FranceAgriMer). However, conditions in Russia could be marginally supportive. The Institute of Agricultural Market Studies indicated that lack of processing and storage capacity could delay the harvest and cut yield. As a result, output from beets could be below the Institute's 2011/2012 production estimate of 4.5 to 5.2 mmts. Like Russia, Australia is reducing its output forecast by 7.1% to 3.9 mmts due to lower yields and reduced plantings.

North America

*The **U.S.** economy is expanding at a gradual pace. Unemployment claims argue for improved labor market conditions, while regional purchasing managers' surveys point to expanding growth. Confidence in the growth picture will be shaped by consumer spending during the holiday period. Inflation is benign with lower commodity prices likely to put pressure on headline CPI and force downward convergence to the core rate which is expanding 2.2% y/y. Fed policy is on hold, but officials will be biased toward monetary ease until the unemployment rate moves closer to 7.0%. The **Canadian** economy shows loss of momentum given weaker labor market conditions and slower trade and manufacturing data. However, the longer term trend toward growth has not broken down. Weaker commodity prices and slower growth in Asia and Europe are downside risks. Headline inflation looks to be cresting. The BOC will keep policy steady and delay rate normalization. The BOC is watching the impact of global growth on the economy. Key economic indicators:*

U.S.:

- November Manufacturing ISM rose 1.9 to 52.7 [51.8 forecast]. Detail: 1) New orders rose 4.3 to 56.7. 2) Production rose 6.5 to 56.6. 3) Employment fell 1.7 to 51.8. 4) Prices paid rose 4.0 to 45.0 – below 50 for 4 months.
- November Non-Manufacturing ISM fell 0.9 to 52.0 [53.9 expected]. Details: 1) New orders rose 0.6 to 53.0. 2) Activity rose 2.4 to 56.2. 3) Employment fell 4.4 to 48.9. 4) Prices paid rose 5.4 to 62.5.
- November payrolls rose 120,000 [125,000 forecast]. Revisions added 72,000 jobs in October and September. Detail: 1) Construction fell 12,000. 2) Manufacturing rose 2,000. 3) Retail rose 50,000. 4) Finance rose 8,000 5) Business services rose 33,000 and healthcare jumped 27,000. 6) Government fell 20,000. The diffusion index was 54.7, which is a bit easier to trend.
- November Unemployment Rate fell 0.5% to 8.6% [9.0% forecast]. The participation rate is falling sharply and holding the unemployment rate down. It was 64.0% compared to 64.5% last year.
- November Retail Sales rose 0.2% m/m [0.6% expected]. There is a slowdown from September and October which rose 1.3% and 0.6% respectively. Details: 1) Vehicles rose 0.5%. 2) Furniture rose 0.4%. 3) Electronics rose 2.1% -- strong gains in past 2 month. 4) Building materials fell 0.3%. 5) Gasoline fell 0.1%. 6) Clothing rose 0.5% and general merchandise gained 0.3%. 7) Eating and drinking fell 0.3%.

- November Small Business Confidence rose 1.8 to 92.0 [91.5 expected]. The index is creeping higher. Plans to hire rose 4% to 7%, the capital spending index rose 3% to 24%, but earnings were weaker.
- November CPI was flat [0.1% forecast]. Inflation is up 3.4% y/y and shows signs of cresting. Core inflation rose 0.2% [0.1% expected] and 2.2% y/y. Core inflation is creeping higher. Apparel is strong up 4.8% y/y. Rents are showing limited strength. Transportation costs eased sequentially.

Canada:

- Canada's November Unemployment rate rose 0.1% to 7.4% [7.3% expected]. Employment fell 18,600 [+20,000 expected]. The unemployment rate looks to be making a trough, while job creation has contracted 3 of the past 4 months.
- November Ivey PMI rose 5.5 to 59.9 [55.5 expected]. The index is firm, but employment eased 2.0 to 49.4 and supplier deliveries rose 1.5 to 44.8. Prices were elevated at 68.1.
- November Housing Starts fell 13.3% m/m to 181,000 [200,000 expected] and show signs of weakening.
- October Home Prices rose 2.5% y/y, posting slow and contained growth.
- October Exports fell 3.0% m/m, but rose 12.6% y/y. Imports rose 1.9% m/m and 10.7% y/y. The data is still a positive for growth.
- October Manufacturing Sales fell 0.8% m/m and rose 7.3% y/y. Sales continue to work higher.
- November LEI rose 0.8% m/m and shows continued expansion.

Europe

*The **EZ** economy is contracting. Tighter fiscal policy, lack of confidence in economic policy and monetary union, and a cautious ECB are weighing on activity. Flash PMI numbers did show improved conditions in France and Germany, but not enough to ease recession fears. Inflationary pressures are diminishing. The ECB will be biased toward further monetary accommodation. The **U.K.** economy is sluggish. Consumer spending and the labor market are weak, but housing data from RICS did point to a slight firming in conditions. The manufacturing sector is being hurt by weak growth in the Eurozone and Asia. Inflation remains stubbornly high, but should fall in 2012. The BOE will be biased toward expanding its asset purchase program, but an actual expansion will likely come on a clear decline in the inflation rate in the face of still poor growth. Key economic indicators:*

Eurozone:

- December Flash PMI Composite rose 0.9 to 47.9 [46.5 forecast]. Manufacturing rose 0.5 to 46.9 [46.0 forecast] and Services increased 0.8 to 48.3 [47.0 forecast]. France and Germany saw a bounce in output compared to the rest of the EZ. Composite output has fallen for a fourth straight month despite the rise in the index. Detail: 1) Order backlog fell for a sixth straight month. 2) Manufacturers cut inventory. 3) Hiring rose modestly. 4) Prices charged fell marginally and input costs rose slightly.
- December French Business Confidence fell 1 to 94 [93 expected]. Details: 1) Retail confidence was flat at 93, but hiring deteriorated. 2) Construction confidence was flat at 99. The order book has failed to show material deterioration, but labor demand has weakened in recent months. 3) Service confidence fell 1 to 92 and is continuing its trend lower. Labor force readings eased lower and the outlook deteriorated.
- October German Exports contracted 3.6% m/m [-1.3% forecast], while Imports fell 1.0% [+0.3% expected]. Exports and imports have been flat to lower since the spring and are consistent with weak growth.

- October EZ Retail Sales rose 0.4% m/m [0.1% expected]. Sales were down 0.4% y/y. Consumer spending looks stagnate.
- October Spanish Housing Transactions fell 18% y/y. The contraction is moderating, but home sales are poor and were sequentially weak down 13.1%.
- November Irish Consumer Confidence fell 3.6 to 60.1 and is working sideways at low levels.
- November EZ CPI rose 0.1% m/m and 3.0% y/y [both as expected]. Inflation may be in the early stages of cresting. Core CPI rose 1.6% y/y and shows stable pricing.
- Q3 German Labor Costs fell 0.9% q/q and rose 2.9% y/y. Costs show signs of moderating.

U.K.:

- November Manufacturing PMI rose 0.2 to 47.6 [47.0 expected]. A downtrend remains and it is too early to look for a trough. Detail: 1) Input prices fell for the first time since July 2009. 2) Output prices rose at the slowest rate in 25 months. 3) Employment contracted. 4) The decline in output accelerated. Weak new orders coupled with reluctance to spend weighed on activity.
- November Service PMI rose 0.8 to 52.1 [50.5 expected]. The index has moved sideways since May and shows slow growth. Detail: 1) Employment fell at the quickest pace in 15 month. 2) Higher utility costs raised input prices, but competitive conditions hurt pricing power and caused output prices to be little changed. 3) New orders rose and advertising increased. 4) Public spending cuts and low bank lending hurt growth.
- November BRC Like for Like Sales fell 1.6% y/y [-0.5% forecast], posting its biggest drop since May. Sales have been flat to lower in recent months.
- November BRC Shop Prices rose 2.0% y/y. Inflation is decelerating and the lowest in a year. Food prices rose 4.0% and are easing, while non-food prices rose 0.8%.
- November New Car Registrations fell 4.2% y/y. The uptrend is cresting after about a year of upward growth. Auto demand remains poor.
- November RICS Home Price Balance rose 7% to -17% [-25% forecast]. Pricing is weak overall, but shows signs of firming. The number of homes sold per broker rose to 15.4 from 15.0 and showed an up tick in activity. Stocks of homes on books were up to 73.2 from 71.1. The data seems to suggest marginal improvement in the real estate market.
- November Claimant Count Rate was flat at 5.0% [5.1% expected], and remains elevated.
- November ILO Unemployment Rate was flat at 8.3% [in line]. The rate is in an uptrend.
- October Average Weekly Earnings were up 2.0% y/y on a 3 month basis [as expected]. Wage growth is sluggish.
- November Retail Sales fell 0.4% m/m [-0.3% expected]. Ex-fuel, sales declined 0.7% m/m [-0.4% projected]. Clothing, auto fuel, and non-store retailing showed strength. The level of activity is sluggish. The index was 101.6 compared to 100.9 last year.
- December CBI Total Orders fell 4 to -23 [-20 forecast]. Order growth continues to fall and show weak conditions. Volume of output was flat at -8, but at a depressed level. Average selling price rose 5 to 7 and has firmed in recent months.
- November CPI rose 0.2% m/m [in line]. Inflation is up 4.8% y/y [as expected]. Core inflation rose 3.2% y/y [3.3% forecast]. Core inflation shows early signs of cresting. Details showed strength in clothing, household, and seasonal food. Weakness was present in services and transport.
- November BOE/GfK Inflation index was 4.1% - elevated but cresting.

Asia

*Asian growth is below trend and momentum is weak. The flash **Chinese** manufacturing PMI stabilized, but remains below 50. Industrial production and the trade sector are seeing reduced activity, while the real estate market looks to be cooling materially. Inflation has peaked and*

should work lower in the coming months. The PBOC will be reducing reserve requirements, and is likely to make a move around the Lunar New Year January 23rd. The government is also likely to under take fiscal measures which aid growth. The **Indian** economy is in a growth recession. Industrial production is contracting and the trade sector has slowed. November auto sales did rise, but the outlook is dim as credit and fuel costs are high. There are reports that mall real estate is in significant oversupply in Bangalore. Inflation has peaked and will fall. The RBI will be cutting rates early in 2012. The **South Korean** economy is on softer footing. Retail sales have slowed, and the labor market has a weak tone. The BOK projected 1% q/q growth in Q4 2011, and is looking for 0.7% q/q and 0.9% q/q in Q1 and Q2 2012 respectively. Inflation is expected to moderate. The BOK is projecting CPI to rise 3.4% in 2012. The BOK will keep policy steady and monitor the spill over effects of weaker growth in Asia and Europe. **Australia's** growth rate has weakened. PMIs are under 50, job creation has sputtered, and retail sales look to have slowed. Weaker commodity prices and slower growth in India and China have reduced the growth picture. Inflation is benign with inflation expectations low. The RBA will continue to cut rates in the coming months. **Japan's** growth rate continues to muddle along. The Tankan survey points to sluggish activity, while a strong yen and weak growth overseas are hurting output. The labor market shows deterioration, but quake reconstruction should be a plus. Deflationary pressures linger. The BOJ will remain biased toward easier policy until the yen weakens, but is likely to be ineffective in generating material growth. Key economic indicators:

Australia:

- November PMI rose 0.4 to 47.8 and has been below 50 five months. It was 47.6 a year ago. Details: 1) Production rose 3.7 to 49.6. 2) New orders rose 1.2 to 48.1. 3) Employment tumbled 6.3 to 45.3. 4) Input prices declined 6.5 to 61.6, while selling prices dropped 3.2 to 44.6 hinting at deflation.
- November Service PMI fell 1.1 to 47.7. It has been below 50 two straight months and was 46.2 last year. Details: 1) Sales rose 0.6 to 48.4. 2) New orders rose 1.0 to 50.4. 3) Employment fell 3.4 to 46.2. 4) Input prices fell 2.9 to 63.5, while output prices fell 6.5 to 44.4.
- October Retail Sales rose 0.2% m/m [0.4% forecast]. Sales are slowly drifting upward. Apparel paced the gain. Department stores and other retailing contracted sequentially.
- October Building Approvals contracted 10.7% m/m [+3.3% forecast]. Housing appears to have weakened significantly in recent months.
- October Number of Home Loans rose 0.7% m/m [flat expected]. Lending activity has been sequentially firm over the past six months.
- November Unemployment Rate rose 0.1% to 5.3% [5.2% forecast]. The trend is creeping higher.
- November Employment contracted 6,300 [+10,000 expected]. Job creation is has been poor since July.
- October Exports fell 0.2% m/m and have declined 4 of the past 5 months. Export growth has been slow since August. Imports rose 2.4% m/m bouncing from weakness in September. Import growth has been sluggish the past 3 months.
- December Westpac Consumer confidence fell 8.3% to 94.7. Confidence fell sharply, and is weak.
- December Consumer Inflation Expectations rose 2.4%. Inflation expectations are at the lower end of the range which has been between about 2.2% and 6.0% over the past 10 years.

China:

- December Flash Manufacturing PMI rose 1.3 to 49.0. Employment and backlog contracted and remain weak. Output and new orders contracted at a slower rate and may show a turn in the downtrend. Output and input prices declined at a marginally slower rate.

- November NBS Non-Manufacturing PMI fell 8.0 to 49.7, showing a material decline. November Markit Non-Manufacturing PMI fell 1.6 to 52.5. It showed no material change in the growth rate. Details: 1) New business slowed. 2) Employment rose at the fastest pace since June. 3) Backlog increased. 4) Input price inflation eased to a 13 month low. 5) Output inflation rose marginally.
- November Industrial Production rose 12.4% y/y [12.6% forecast] and is decelerating. Details: 1) Cement output dipped only slightly on a sequential basis and was up a much slower 11.2% y/y. 2) Electricity output rose sequentially and rose 8.5% y/y – a slower pace. 3) Motor vehicle output contracted 1.3% y/y, but jumped sequentially. 4) Rolled steel output rose 7.8% y/y and is decelerating. The sequential trend is falling.
- November Retail Sales rose 17.3% y/y [16.8% expected]. Detail: 1) Electronic spending rebounded on a year over year basis up 25.0%. 2) Furniture was firm up 34.4%. 3) Construction materials rose 28.4% consistent with trend. Rural spending has slowed sequentially in the past 3 months.
- China Association of Auto Manufacturers said that wholesale deliveries rose 0.3% y/y to 1.34 mlu in November – the slowest pace since May.
- November Exports rose 13.8% y/y [10.9% expected], while Imports rose 22.1% y/y [18.8% expected]. Detail: 1) oil and refined product imports showed significant sequential strength. 2) Iron ore import volume also firmed significantly on a sequential basis. 3) Copper and copper scrap imports surged sequentially as did aluminum and aluminum scrap. None the less, year to date year over year these last items are mostly lower.
- Poly Real Estate indicated that sales declined more than 50% in 13 of 35 cities during November, while Soufun said that housing transactions fell in 27 of 35 cities between December 5th and 11th. Sales plunged more than 60% in Tianjin and Hangzhou.
- November New Yuan Loans were CNY 562 bln [CNY 550 bln forecast]. Lending was CNY 563.97 bln a year ago and CNY 294.76 in November 2009.
- October LEI fell 0.1 to 160.1. The trend is higher with October showing a pause.
- November CPI rose 4.2% y/y [4.5% expected]. Inflation looks to have peaked. Sequentially, CPI contracted 0.2%. Inflation has slowed sharply the past two months. There was across the board moderation, but significant year over year declines in food (8.8% v. 11.9%) and housing (3.0% v. 4.4%).

India:

- November Manufacturing PMI fell 1.0 to 51.0 and is in a steady downtrend. Details: 1) New orders expanded, but have slowed. 2) Output growth was weak due to power cuts and a slow rise in new orders. 3) Backlog rose. 4) Employment fell for the fourth straight month. 5) Input costs accelerated substantially. A weak rupee could be at work. 6) Output prices also rose.
- November Service PMI rose 4.1 to 53.1 and has rebounded from two months of contraction. Detail: 1) New business rose at its best pace since August. 2) Backlog was flat. 3) Employment fell for a 4th straight month, but the pace of decline eased. 4) Input prices rose due to higher raw material costs and wages. 5) Output costs rose on pace through.
- October exports rose 10.8% y/y, while imports grew 21.7% y/y. Trade activity has decelerated sharply. The sequential trend in exports has turned noticeably lower and import growth has stalled.
- October Industrial Production plunged 5.1% y/y [-0.7% expected]. Production growth is flirting with the trough made in 2009. Mining and manufacturing output fell 7.2% and 6.0% respectively.
- December 3rd Primary Articles WPI rose 5.48% y/y and is working lower.

Japan:

- November Market PMI fell 1.5 to 49.1 and shows slow growth.
- Q4 Tankan Large Manufacturing index fell 6 to -4 [-2 expected], while Non-Manufacturing rose 3 to 4 [-1 forecast]. The Capex outlook was 1.4% down from 3.0% last quarter [2.5% expected].

Outlooks were cautious with Large Manufacturing at -5 [-3 forecast] and Non-Manufacturing flat [1 expected]. Activity is depressed and well below the expansion levels of the mid 2000's.

- October Household Spending fell 0.4% y/y [-1.5% expected]. Sequentially, spending rose 0.3% and has been firm.
- October Unemployment Rate rose 0.4% to 4.5% [4.2% forecast]. The drop in August and September looked quirky and the rate has mean reverted higher. Average weekly hours did point to economic strength. The labor force expanded, unemployment rose, and employment was flat.
- November Economy Watcher's Survey fell 0.9 to 45.0. The outlook dropped 1.2 to 44.7. Growth looks to have stalled after a post quake bounce.
- November Consumer Confidence fell 0.5 to 38.1 [38.3 expected]. The recent trend is flat.

South Korea:

- November PMI fell 0.9 to 47.1. Activity is on the lower end of the historical range with 2008/2009 the clear low point. Detail: 1) Output fell with a decline in new business. 2) Backlog declined. 3) Employment rose, but the increase was weak to tend. 4) Input inflation is slowing. 5) Output prices declined for the first time in 4 months. The drop was marginal and driven by competition.
- November Exports rose 13.8% y/y [10.4% expected]. Imports rose 11.3% y/y [12.4% expected]. Sequentially, the trend in import and exports points to slowing growth. Year over year rates of gain have also decelerated sharply.
- November Bank Lending was KRW 453 trln. There was little change from October.
- November CPI rose 4.2% y/y [4.4% forecast]. CPI rose 0.1% sequentially [flat forecast]. Core inflation increased 3.5% y/y. Inflation is sticky at relatively high levels.
- November Unemployment Rate was unchanged at 3.1% [3.2% forecast]. Employment looks relatively flat in the past 5 months, while unemployment has dipped marginally. Service industry hiring helped to keep the unemployment rate down.
- November Department and Discount Store Sales each contracted 0.5% y/y. Sales growth at department stores has weakened materially and points to a significant pull back in consumer spending. Discount store sales are soft, but consistent with trend.

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