AFP EconWatch

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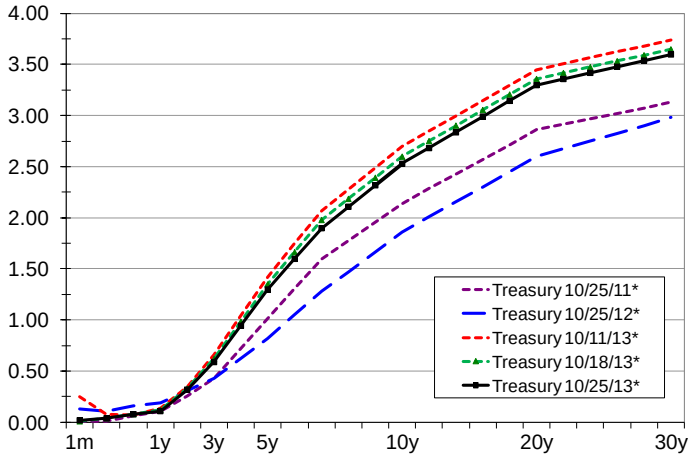
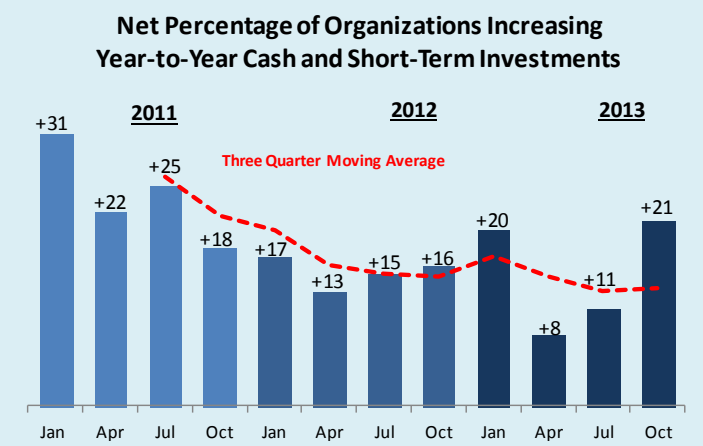
Weekly Economic Newsletter for Treasury and Finance *October 28, 2013*

The Big Picture: Yield Curve & AFP Corporate Cash Indicators™



U.S. Treasury Yield Curve—Source: U.S. Department of the Treasury



AFP Corporate Cash Indicators™—Source: Association for Financial Professionals

Measure	Numerical Trend	Current Trend	Analysis
Employment September 2013 *Source: Bureau of Labor Statistics*	*Non-Farm Payrolls* *Change from Previous Month* *Seasonally Adjusted* *Thousands* Sep 13: +148 Aug 13: +193 Sep 12: +138	↑	In addition to September's gain, the BLS added 21,000 workers to its estimate for August (to a 190,000 gain) but lowered its count for July by 15,000 jobs (to an 89,000 increase). Non-farm payrolls totaled a seasonally adjusted 136.290 million jobs, up 2.225 million from a year earlier but below the 138.056 million count from when payrolls peaked in January 2008. The private sector added 126,000 jobs, split by 100,000 in the service sector and 26,000 in the goods producing side of the economy. Based on a separate household survey, the unemployment rate slipped 1/10th of point to 7.2% (its lowest since November 2008).
Durable Goods September 2013 *Source: Census Bureau*	*Percentage Change from Previous Month* *Seasonally Adjusted* Sep 13: +3.7% Aug 13: +0.2% Sep 12: +9.8%	↑	The biggest single-month increase in new orders for durable goods in 3 months (totaling $233.4 billion during September) largely reflected a 57.5% surge in orders for civilian aircraft. Net of the 12.3% increase in new orders for transportation goods, durable goods orders declined 0.1%. Shipments totaled $231.8 billion, up 0.2% from August. Unfilled orders grew for the 7th time in 8 months (+0.8%) while inventories expanded for the 5th time in 6 months (+0.9%).

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International Trade August 2013 *Source: Bureau of Economic Analysis/Census Bureau*	*Percentage Change from a Year Earlier Seasonally Adjusted* Aug 13: -$38.8 Jul 13: -$38.6 Aug 12: -$44.0	↓	Both export and import activity was essentially unchanged from July. Exports totaled $189.2 billion (+3.9% vs. a year earlier) while imports summed to $228.0 billion (+0.9% vs. August 2012). The goods deficit widened by $0.1 billion to -$58.2 billion while the services surplus contracted by $0.1 billion to +$19.4 billion. The "real" trade deficit, based on 2009 chained dollars, remained at -$47.3 billion (5.8% below year ago levels).
Existing Home Sales September 2013 *Source: National Association of Realtors*	*Seasonally Adjusted Annualized Rate Millions* Sep 13: 5.29 Aug 13: 5.39 Sep 12: 4.78	↑	Sales of previously owned homes were up 10.7% from a year earlier. Sales fell on a month-to-month basis in 3 of 4 Census regions, including a 5.3% drop in the Midwest, a 2.8% decline in the Northeast and a 1.6% slip in the South. Sales of previously owned homes inched up 1.6% in the West. Inventories of unsold homes totaled 2.21 million units at the end of September, flat vs. August and up 1.8% from a year earlier.
Construction Spending August 2013 *Source: Census Bureau*	*Percentage Change from Previous Month Seasonally Adjusted Annualized Rate* Aug 13: +0.6% Jul 13: +1.4% Aug 12: -0.3%	↑	The SAAR value of construction put into place during August was $915.052 billion, up 7.1% from a year earlier. Private sector construction spending was at $636.1 billion, a 0.7% increase from July and 11.5% above the August 2012 pace. Spending on residential construction was up 1.2% during the month while the gain on the non-residential side was a paltry 0.1%. Spending on public construction was at $274.5 billion, up 0.4% for the month but 1.8% under year ago levels.
Job Openings and Labor Turnover August 2013 *Source: Bureau of Labor Statistics*	*Job Openings Seasonally Adjusted Thousands* Aug 13: 3,883 Jul 13: 3,808 Aug 12: 3,632	↑	The private sector had 3.520 million job openings at the end of August, +3.5% vs. July and +9.2% vs. August 2012. 4.488 million people were hired during August (essentially unchanged from July and +1.9% vs. August 2012) while 4.376 million people left their jobs (+2.4% vs. July 2013 and +0.8% vs. August 2012). Voluntary quits totaled 2.364 million (+10.5% vs. August 2012) while the number of layoffs was 1.648 million (-11.4% vs. August 2012).
Import/Export Prices September 2013 *Source: Bureau of Labor Statistics*	*Import Prices Percentage Change from Previous Month* Sep 13: +0.2% Aug 13: +0.2% Sep 12: +1.0%	↑	The price of imported fuel increased 0.6% with imported petroleum prices growing 0.8%. Net of fuel of fuel, import prices inched up 0.1% (with non-fuel industrial supplies & materials being the largest positive contributors). Import prices have fallen 1.0% over the past year with a 12-month comparable of -1.2% net of imported fuel. Export prices grew for the 1st time since May (+0.3%) but were off 1.6% over the past year.
University of Michigan Surveys of Consumers October 2013 *Source: University of Michigan*	*Diffusion Index 1966 Q1=100 Seasonally Adjusted* Oct 13: 73.2 Sep 13: 77.5 Oct 12: 0	↓	The headline index was off 2.0 points from the preliminary October reading released 2 weeks earlier and was the 3rd straight monthly decline (losing 11.9 points over the span). Sentiment for current and expected conditions both deteriorated: the index for the former lost 2.7 points to 89.9 while the latter lost 5.3 points to 62.5. Inflation expectations moderated to 3.0% for the next year.

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Economic Commentary edited by Kevin Roth

Eroding business confidence resulting from political uncertainty in Washington and uneven economic growth resulted in many U.S. businesses to build out cash reserves during the third quarter. The quarter-to-quarter and year-to-year indices from the AFP Corporate Cash Indicators™ hit multi-year highs, according to the report released today. The quarter-over-quarter index increased seven points to +19 (its highest reading since January 2012) while the year-over-year indicator jumped ten points to +21 (its highest reading since July 2011). Companies' decisions to grow/shrink the size of their cash and short-term investment portfolios reflect their business outlook and direction—organizations that are confident in their future prospects are more likely to deploy current cash holdings, including increased capital expenditure spending, hiring and merger & acquisition activity. Conversely, larger cash holdings can be linked to concerns about the future.

But financial professionals may be sensing the economic lull *could* be short-lived as the pace of cash accumulation is expected to slow during the final three months of 2013. The forward-looking indicator measuring expectations in the change of cash holdings during the current quarter dropped from a reading of +14 in the July 2013 report to +6. One explanation for the forward-looking indicator's lower reading is that companies are deciding to sit on their recently inflated cash balances until policymakers in Washington reach a long-term agreement on fiscal issues. Read the full report on the October 2013 AFP Corporate Cash Indicators™ in back of this edition of *AFP EconWatch*.

Last week featured a series of economic data releases that had been previously postpone because of the partial federal government shutdown.

A report from the Bureau of Economic Analysis and Census Bureau indicates that trade activity was steady during August. The "nominal" trade deficit was at a seasonally adjusted -$38.6 billion during August, up by a mere $161 million from July and significantly smaller than the -$44.0 deficit of August 2012. Also barely budging from the July levels were exports ($189.2 billion, +3.9 percent from August 2012) and imports ($228.0 billion, +0.9 percent from August 2012), along with minor month-to-month changes in trade balances for both goods (-$58.2 billion) and services (+$19.4 billion). The largest trade deficits in goods were with China (-$29.9 billion), European Union (-$9.8 billion), OPEC (-$7.3 billion) and Japan (-$6.4 billion).

U.S. payrolls expanded for a 36th straight month during September and the unemployment rate declined to its lowest reading in nearly five years, but the Bureau of Labor Statistics employment report left many wanting more. Employers added 148,000 non-farm jobs during the month, down from a 193,000 job gain in August and below most forecasts. The private sector was responsible for 126,000 of the new jobs, with the biggest payroll gains experienced in transportation/warehousing (+23,400), retail (+20,800), temporary help services (+20,200) and construction (+20,000). The public sector added 22,000 workers, almost entirely in state and local education. The average number of weekly hours worked was 34.5

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hours (unchanged from September 2012) while average weekly earnings have grown 2.1 percent over the past year to $831.11.

The household survey from the same report places the unemployment rate at 7.2 percent, off 6/10ths of a point from a year earlier and its lowest reading since November 2008. The labor force expanded by 73,000 workers (its first increase in three months) but the labor force participation rate remained at 63.2 percent, its lowest reading since the summer of 1978. A few other tidbits from the household survey:

- 7.926 million people had a part-time job but were seeking a full-time opportunity, essentially unchanged from August but down from 8.607 million a year earlier.
- The typical unemployed person has been jobless for 16.3 weeks, off 1/10th of a week from August and down from 18.7 weeks in September 2012.
- The broadest measure of labor underutilization, the U-6 series, dropped 1/10th of a point to 13.6 percent, down 1/10th of a point from August and a full percentage point a year earlier. This was the lowest reading for the U-6 series since December 2008.

There were a seasonally adjusted 350,000 first-time claims made for unemployment insurance benefits during the week ending October 19. While this was down 12,000 claims from the week before, the Department of Labor jobless count remained bloated because of the partial federal government shutdown (e.g., furloughed private-sector government contractors, etc.). The resulting four-week moving average of 348,250 was up 10,750 from the week before and was roughly 20,000 above recent readings, but below the 369,000 moving average of a year earlier. The headline jobless count does not include layoffs of federal employees caused by the government shutdown. The Department of Labor reported that there were 44,132 first-time claims made by federal employees during the week ending October 12, up dramatically from the 1,991 count of the same week a year earlier.

Perhaps to the shock of no one, the partial federal government shutdown and the debt ceiling crisis did little to boost consumer confidence this month. The Index of Consumer Sentiment reading from the University of Michigan Surveys of Consumers lost 4.3 points during October to a seasonally adjusted 73.2 (1966 Q1 = 100). This reading was down a full two points from the preliminary October reading released a few weeks earlier. Consumers were less positive about both current and future conditions, but the expectations index took the bigger hit during month as it lost 5.3 points to 62.5 (its lowest reading since November 2011). The present conditions index shed 2.7 points to 89.9, matching its reading from April. The press release noted the highest percentage of survey respondents in "more than a half-century history of the surveys" had "negatively mentioned the federal government" when asked about the state of the economy.

Another BLS report released last week finds import prices had increased for a second consecutive month during September. But even though they have risen 0.2 percent in each of the last two months, import prices remained 1.0

percent below year ago levels. The main contributor to September's hike was imported petroleum, the price of which grew 0.8 percent during the month. Net of petroleum, import prices were unchanged during the month (net of all fuel, which also includes natural gas, import prices grew 0.1 percent). Export prices grew for only the second time since February with a 0.3 percent increase, with positive contributions coming from agricultural exports, non-agricultural industrial supplies/materials and capital goods. Export prices were down 1.6 percent from a year earlier.

Orders for Boeing aircraft led to the biggest one-month increase in new orders for durable goods in three months during September. The Census Bureau reported on Friday that durable goods orders totaled a sesaonally adjusted $233.4 billion during the month, up 3.7 percent from August and 7.4 percent from a year earlier. But after controlling for the 12.3 percent jump in new orders for transportation goods (itself reflecting a 57.5 percent surge in civilian aircraft orders—vehicle orders dropped 0.3 percent), durable goods orders slipped 0.1 percent during the month. Sizable one-month percentage gains in orders also occurred with primary metals (+2.7 percent) and computer/electronic products (+0.6 percent) but machinery (-1.8 pecent) and fabricated metals (-0.9 percent) were drags on manufacturing.

There also were two reports released on October manufacturing activity from regional Federal Reserve banks.

- Manufacturing activity was stuck in neutral in the area served by the Federal Reserve Bank of Richmond. The headline composite diffusion index from the Fifth District Survey of Manufacturing Activity inched up by a point to a seasonally adjusted reading of +1, just above the neutral reading of 0. The bright spots in the report were an 18 point surge in the shipment index to +17 and a ten point gain in employment (to +4). But other indices pulled back, including new orders (down five points to 0) and unfilled orders (down eight points to -15).
- The Federal Reserve Bank of Kansas City noted that manufacturing activity in their district had "improved moderately." The composite index from the Tenth District Manufacturing Survey added four points to a seasonally adjusted +6. The production index jumped ten points to +14, but new orders index lost five points (to +3) and the employment index shed two points (to -2).

The Census Bureau reports construction spending grew at its slowest rate during August, with a 0.6 percent gain. But the seasonally adjusted annualized value of construction put into place during the month— $909.4 billion—was up a healthy 7.1 percent from a year earlier, with much of the gain coming from the housing sector. Private residential construction spending was up 1.2 percent during the month, including a 1.6 percent increase in spending on new single-family homes. Private residential construction spending has grown 11.5 percent over the past year, including a 28.2 percent increase in new single-family home construction expenditures. Non-residential private sector construction spending eked out a 0.1 percent increase (+4.3 percent from August 2012) while public sector construction spending grew 0.4 percent during the month but was off 1.8 percent over the past year.

Despite of rising home prices and interest rates, sales of previously owned homes remained near post-recession highs during September. The National Association of Realtors reported that existing home sales were at a 5.29 million unit

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seasonally adjusted annualized rate, down 1.9 percent from August but up 10.9 percent from that of September 2012. Sales declined in three of four Census regions during the month (the West was the exception with a 1.6 percent gain), but improved on a year-to-year basis in all four regions (with gains spanning from +7.8 percent in the West to +15.0 percent in the Northeast).

Inventories of unsold homes remained tight with a 5.0 month supply available at the end of September. As a result, the median sales price in September—$199,200—was up 11.7 percent from a year earlier. NAR's press release noted that homebuyer affordability dropped to a five-year low, thanks to the big jump in home prices and the recent rise in interest rates. Further, the trade group indicated that sales activity *may* have been hurt by the recent government shutdown.

Another measure of home prices released last week showed general strength, but suggests the increases may be slowing. The Home Price Index from the Federal Housing Finance Agency, which measures prices of previously owned homes purchased with a conforming mortgage, grew a seasonally adjusted 0.3 percent during August (its smallest increase in nearly a year) and was 8.5 percent above year ago levels. The index was up in seven of nine Census regions, with the biggest one month increases in the Mountain (+1.3 percent), West North Central (+1.2 percent) and Pacific (+0.8 percent) regions.

Bankruptcy activity continued to slow from recession highs, with the Administrative Office of the U.S. Courts reporting the number of filings falling for a third consecutive year. The 1.108 million bankruptcy filings during FY2013 was down 12.1 percent from the previous year and well below 1.596 million seen during the tail end of the recession in FY2010. During the 12-month period through September 30, there were 34,892 business filings and 1.073 million non-business filings. The same measures for FY2012 were 42,008 and 1.219 million, respectively.

The Week in Corporate Finance edited by Brian Kalish

So we have re-opened the federal government and increased the debt ceiling until early 2014. The market's reaction to this short-term reprieve has been decidedly positive, with the stock market rallying on the news. Interest rates have dropped as the prospect of the Fed taking their collective foot off the stimulus accelerator has lessened. Instead of the Fed easing back on their stimulus as early as this past September, many market watchers think we will witness the Fed buying fewer Treasuries and agency MBS in the latter part of the first quarter 2014.

Over the past three weeks, the U.S. Treasury 2-year note yield was down 3bps to 30bps (indicating the Fed will not raise interest rates until early 2015); the 5-year note yield was down 12bps to 1.27 percent: the 10-year note yield was down 13bps to 2.50 percent (after being as low as 2.47 percent); and the 30-year bond yield was down 13bps to 3.59 percent. Mortgage rates have also dropped over the past few weeks. The average 30-year fixed-rate mortgage fell to a four-month low of 4.13 percent and the average 15-year fixed-rate mortgage dropped to 3.24 percent.

With interest rates dropping, the attractiveness of the U.S. dollar has diminished. The U.S. dollar fell to a two-year low of $1.3832 versus the Euro, and near its 52-low versus Sterling at 1.6168.

Stocks benefitted from the perceived continuation of cheap money from the Fed as the S&P 500 reached a new all-time high of 1,559.33, the NASDAQ touched a new 13-year high of 3.961.10 and the Dow closed near its all-time high at 15,537.21.

Oil prices continued their recent slide, falling to a low of $95.95/barrel. As recently as August 28th, oil was at its 52-week high of $109.70. US crude inventories have grown to 379.8 million barrels, while production has grown to 7.9 million barrels/day; the most since March 1989 (think "She Drives Me Crazy" by the Fine Young Cannibals).

The corporate debt issuance market had a bit of a rebound this week after all the government shutdown-related challenges of the past few weeks, raising over $35 billion. Bristol-Myers came to market with a three-tranche offering comprised of $500 million each of 5-year, 10-year, and 30-year securities.

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This week we have both the second-to-last scheduled FOMC meeting of 2013 and the AFP Annual Conference in Las Vegas. At Conference, watch for the release of the updated Cost of Capital survey.

Viva Las Vegas!

What to watch over the next week:

Monday, October 28, 2013

- AFP Corporate Cash Indicators™ (October 2013)
- Pending Home Sales (September 2013)

Tuesday, October 29, 2013

- Producer Price Index (September 2013)
- Retail Sales (September 2013)
- The Conference Board Consumer Confidence (October 2013)
- S&P/Case-Shiller Home Price Index (August 2013)

Wednesday, October 30, 2013

- FOMC Meeting
- Consumer Price Index (September 2013)

Thursday, October 31, 2013

- Jobless Claims (week ending October 26, 2013)
- Agricultural Prices (October 2013)

Friday, November 1, 2013

- Vehicle Sales (October 2013)
- ISM Report on Business—Manufacturing (October 2013)

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AFP EconWatch—Weekly Economic Newsletter by:
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AFP® CORPORATE CASH INDICATORS™

Association for Financial Professionals®

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October 2013 Survey Results

Confidence among U.S. businesses further softened during the third quarter, impacted by both uneven economic growth and political uncertainty in Washington surrounding the Federal budget and debt limit. According to the October 2013 AFP Corporate Cash Indicators, the pace of corporate cash accumulation increased during the third quarter of 2013. The quarter-over-quarter index increased to +19, its highest reading since January 2012. The year-over-year indicator jumped 10 points to +21. But financial professionals may be sensing the economic lull may be short-lived as the pace of cash accumulation is expected to slow during the final three months of 2013. The forward-looking indicator measuring expectations in the change of cash holdings during the current quarter dropped from a reading of +14 in the July 2013 report to +6. The indicator for short-term investment aggressiveness increased by a point to a reading of +2, indicating that companies were marginally more aggressive in how they managed their cash during the third quarter.

Over the past quarter, did your organization's cash and short-term investment holdings increase, decrease or remain the same?

October 2012	April 2013	July 2013	October 2013
+14	+10	+12	+19

Index: "Increase" percentage minus "decrease" percentage. The higher the index reading, the greater net percentage of organizations that have increased cash and short-term investment holdings over the past quarter.

Over the past year, did your organization's short-term holdings increase, decrease or remain the same?

October 2012	April 2013	July 2013	October 2013
+16	+8	+11	+21

Index: "Increase" percentage minus "decrease" percentage. The higher the index reading, the greater net percentage of organizations that have increased cash and short-term investment holdings over the past year.

During the current quarter, do you expect your organization will increase, decrease or maintain its current cash and short-term investment holdings?

October 2012	April 2013	July 2013	October 2013
+12	-5	+14	+6

Index: "Increase" percentage minus "decrease" percentage. The higher the index reading, the greater net percentage of organizations expected to increase cash and short-term investment holdings during the current quarter.

Over the past quarter, did your organization's investment selection for its cash and short-term investments become more aggressive, more conservative, or remained unchanged?

October 2012	April 2013	July 2013	October 2013
0	+4	+1	+2

Index: "More aggressive" percentage minus "more conservative" percentage. The higher the index reading, the greater net percentage of organizations that have become more aggressive with their investment selection for their cash and short-term investments over the past quarter.

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About the Index Values

Note: Rounding may lead to minor differences in the final index value

- *40 percent of organizations held larger cash and short-term investment balances at the end of Q3 2013 than they did at the end of Q2 2013 while 21 percent had shed cash during the three months. The difference of +19 is up 7 points from the previous quarter's reading and an increase of 5 points from the Q3 2012 survey results.*

- *41 percent of organizations had greater cash and short-term investment balances at the end of Q3 2013 than they had one year earlier, while 19 percent held smaller cash balances relative to a year ago. The difference of +21 is up 10 points from the previous quarter's reading and up 5 points from Q3 2012.*

- *32 percent of organizations anticipate expanding cash and short-term investment balances over the next three months, while 26 percent plan to reduce these balances. The net index reading of +6 is down 8 points from that reported in July and 6 points from the October 2012 survey.*

- *8 percent of organizations were more aggressive with short-term investments in Q3 2013 while 6 percent were more conservative. The difference of +2 is an increase of one point from the prior quarter and up two points from a year ago.*

About the AFP Corporate Cash Indicators™

The AFP Corporate Cash Indicators™ (www.AFPonline.org/CCI), underwritten by State Street Global Advisors, Global Cash, are produced by the Research Department of the Association for Financial Professionals as forward looking measures of corporate cash and short-term investment holdings and of expected business conditions. On the opening days of each quarter, AFP asks select members about the size and make up of their short-term investment holdings. AFP has scheduled the release of the next edition of the AFP Corporate Cash Indicators™ for January 27, 2014.

The survey results are published in the weekly economic newsletter, *AFP EconWatch* (www.AFPonline.org/EconWatch).

For information about publishing the AFP CCI™ on your site, contact pr@afponline.org.

Survey Methodology

The AFP Corporate Cash Indicators™ are derived from a quarterly survey sent to a select group of financial professionals consisting of four questions about how companies manage their cash and short-term investment portfolios. The survey goes to people whose day-to-day job is manage their companies' cash and short-term investment portfolios and are fully aware of their organizations' cash strategies. Companies' decisions to grow/shrink the size of their cash and short-term investment portfolios reflect their business outlook and direction, making these decisions leading indicators of economic activity.

The first 3 questions are:

- *Over the past quarter, did your organization's cash and short-term investment holdings increase, decrease or remain the same?*
- *Over the past year, did your organization's short-term holdings increase, decrease or remain the same?*
- *During the current quarter, do you expect your organization will increase, decrease or maintain its current cash and short-term investment holdings?*

To arrive at the index values for each of the first three questions, subtract the percentage of respondents who report "decrease" from those that report "increase." *(For example, if 40 percent of respondents indicate that their organizations' holdings have increased over the past quarter and 30 percent indicate a decrease, you get an index reading of +10 for the first question).*

The final question asks about strategy:

- *Over the past quarter, did your organization's investment selection for its cash and short-term investments become more aggressive, more conservative, or remained unchanged?*

The index value from this question is the difference of the percentage of respondents who indicated "more aggressive" and those that indicated "more conservative."

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