JPMorgan

Australia and New Zealand - Weekly Prospects

Summary

- Once again we have arrived at the quarterly fork in the road that is the **Australian** inflation data, and the 'will they, won't they' debate on the likely RBA response. A 0.7%q/q print on the core trimmed mean and weighted median statistical measures on Wednesday (which, for the first time, will be released simultaneously with the headline data) should be enough to keep the RBA sidelined next month. Headline inflation will be boosted to 0.9%q/q (from just 0.1% in Q1) by rising fuel and food prices, and higher rents and house purchase costs. The offset should come from lower import prices. It would take a core print of at least 0.8% to bring an August rate hike into play. Today's PPI data will be a tasty apertizer—the PPI has as good as nailed the CPI result for the last four quarters.
- Inflation remained at the centre of the economic radar in **New Zealand** last week. Although headline CPI came in above expectations in 2Q, markets centered their attention on the reading for nontradables inflation, which printed at an unexpectedly high 4.1%oya in the June quarter. After considering the inflation report, in addition to other key economic data that has printed on the firmer side, the forecast now anticipates that the RBNZ will raise the official cash rate by 25 basis points to a fresh record high of 8.25% on Thursday. Moreover, there is a growing risk of a second tightening in September.
- Recent financial market developments underscore the risk that an unexpected, sharp tightening in financial conditions has the potential to slow the **global economy** in coming months. Barring such a tightening, activity data are sending mostly positive signals about global growth prospects. The jury is still out on the strength of the US economy after what is expected to have been a solid second quarter. We remain comfortable with the view that, with the housing market downturn losing force and gasoline prices moving lower, the **US economy** will generate growth of 3% or better in coming quarters. Looking beyond the United States, the latest business surveys and the hard activity data from **Europe** and **Asia** point to continued above-trend growth. Likewise, rising commodity prices continue to support growth in the commodity-exporting emerging economies.
- The latest data from **China** deliver a strong message about its own and global growth. The 2Q quarterly advance in real GDP, estimated to be 15.9% (q/q, saar), was the strongest since the early 1990s, with the exception of the 3Q03 increase that followed the SARS crisis. China's growth is multifaceted, featuring huge increases in retail sales, fixed-asset investment, and exports. Moreover, the strength of the June activity indicators suggests that the economy has carried strong momentum into the current quarter.

This week's highlight(s)

Actually, there are two. First, the Aussie CPI data Wednesday, which will all but determine the outcome of the August RBA meeting. Second, the RBNZ decision Thursday - in a change of forecast, we now look for a 25bp tightening.

Contents

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Economic Research note

RBNZ expected to hike cash rate to 8.25% this week

- **The RBNZ is likely to consider July an opportune time to hike the OCR to a fresh record-high 8.25%**
- **Surging dairy prices, a relentless housing market, and fiscal largesse argue for further tightening**
- **Last week's final piece of the RBNZ policy puzzle—nontradables[1] inflation—was too strong to dismiss**

The RBNZ's war on inflation is not over, and another OCR tightening now appears warranted. In a change of forecast, JPMorgan expects the RBNZ to raise the OCR 25bp to a record high 8.25% on Thursday. Previously, we suggested that there was a 30% probability of a July rate hike, although we now see a 65% chance, given that the four criteria we believed had to be satisfied ahead of the July policy decision for the RBNZ to tighten have been met, if not surpassed.

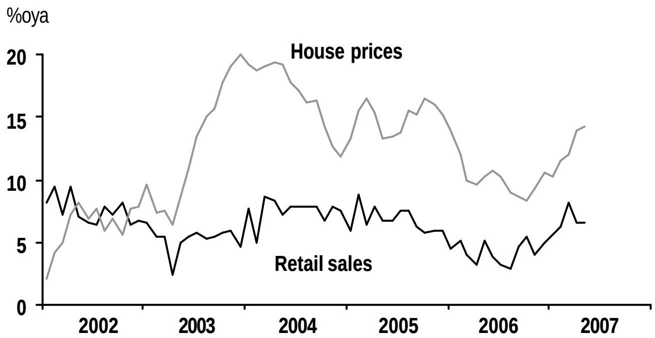
Hitherto, RBNZ officials' resolve to pull the housing market into line, frustrations over expansionary fiscal policy, and concerns about the pass-through effects from surging dairy prices, have fueled the central bank's willingness to tighten policy. Already, the RBNZ has raised the OCR three times this year in order to encourage a lower inflation trajectory, and hawkish public commentary indicates that officials have sufficient determination to go further. The June Monetary Policy Statement (MPS) stated, "a sustained period of slower growth in domestic activity will be required to alleviate inflation pressures," with Governor Bollard adding, "the risks to domestic activity appear to remain on the upside."

Key criteria surpassed for RBNZ rate hike

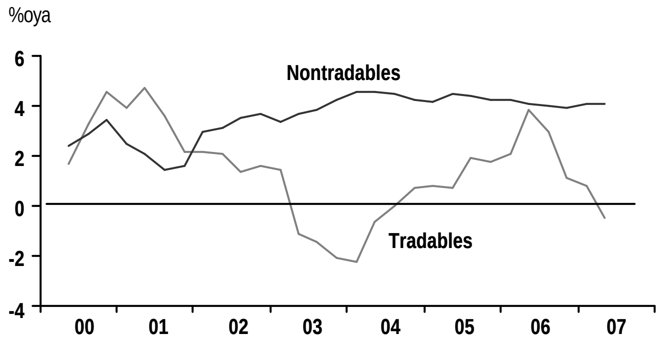
In our last RBNZ research note (see "RBNZ puts heat on inflation with scorched earth policy" *GDW*, Jun 29), we outlined four key criteria that would need to be satisfied in order for the RBNZ to tighten. Three of the four rate hike criteria—still elevated business confidence, stubbornly buoyant retail spending, and rising house prices—argue for another rate hike but, on their own, are not sufficient to push the RBNZ across the line. However, the most important of the four criteria for a tightening—still-elevated nontradables inflation—was satisfied last week, when the annual rate printed at an unexpectedly high 4.1%oya; it has now remained around the 4% level for the past four years.

1. Nontradables are goods and services that do not face foreign competition.

Retail sales and house prices



CPI: tradables and nontradables



The four data criteria we set, in order of importance, are:

- **Nontradables inflation.** Again printing above expectations, nontradables inflation was 1.1%q/q in 2Q, and remained above the psychological 4% level in annual terms. Despite the fact that much of the momentum in 2Q inflation was driven by a jump in gasoline prices (up 8%q/q) and a surge in electricity costs (up 3%), the chunky quarterly outcome and unsatisfactorily high annual growth rate give the hawks within the RBNZ more than enough to squawk about. The likely second-round impacts of rising gasoline, electricity, and food prices mean that the RBNZ possibly has more work to do, even though previous tightening is still be working its way through the economy.
- **NZIER Quarterly Survey of Business Opinion.** Falling in line with expectations, general business confidence dropped to -37 in 2Q, down from -15 in 1Q. The growing pessimism recorded in the survey was "widespread," according to the NZIER. All key indicators of capacity usage and inflation (utilization rates, pricing, cost intentions, and difficulty finding labor) fell over the quarter and point to lower inflation pressure in the pipeline. That said, the levels of the key indicators remain uncomfortably high, and continue to point to the need for vigilance on the inflation outlook. Consumer confidence also fell, but the massive dairy

income payout and a stable labor market are putting a cushion under consumption growth.

- **House prices.** Home construction and sales activity are showing signs of buckling, yet house prices remain elevated. According to the June REINZ report, the median house price fell to NZ$347,500 from NZ$350,000. Although this contrasted with the Quotable Value series, which reported that house prices rose 12.2%oya calculated over the three months to June, up from 11.1% previously. Both reports showed a reduction in trading activity, and suggested that the soaring housing market has hit an air pocket. The RBNZ, however, which focuses primarily on the QV house price series, will want to make sure the reduction in activity is not just related to cold weather, and is in fact a turn in the market.
- **Retail sales.** Retail spending unexpectedly bounced back in May, rising a healthy 1.2%m/m after falling 1.2% in April. Core retailing, which excludes vehicle-related industries, posted a chunky 0.8%m/m gain. The message from the retail data was mixed, though, as the major gains in retailing from food, furniture, and vehicle sales were partially offset by sharp falls in department store and clothing retailing. That said, the report showed that sales have returned to the March level, which was when the RBNZ was particularly concerned about persistently strong consumption growth.

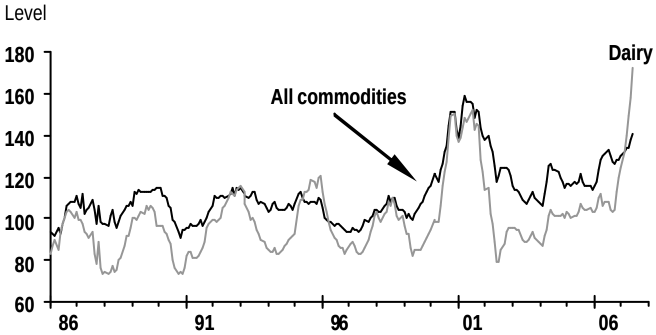
The cracks beneath the surface in some of the data (i.e., falling housing activity rather than prices) will not be enough to offset central bank concerns over still-elevated nontradables inflation. Indeed, the accumulation of solid (albeit softening) economic indicators, and the RBNZ's inability to drag nontradables inflation below 4%oya, make it difficult for Governor Bollard to dismiss the need for a further 25bp rate hike this week.

RBNZ's assertive reaction function

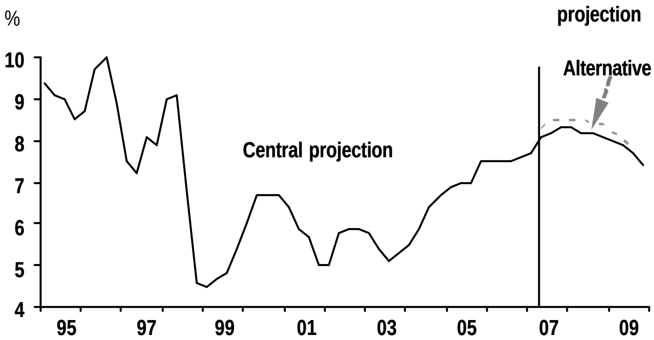
Previously, JPMorgan believed that the RBNZ had time on its hands to assess the full impact of this year's three OCR rate hikes in March, April, and June. The RBNZ's assertiveness in responding to upside surprises on key economic data, though, has intensified this year, owing to frustrations among officials over their inability to drag inflation lower and the housing market back into line. RBNZ officials seemingly have become more comfortable with the risk of possibly overtightening in an effort to end a tightening cycle that already has spanned four years—the RBNZ started tightening policy in January 2004, and has since raised the cash rate 12 times.

The expected 13th tightening this week will extend the Land of the Long Dark Cloud's interest rate advantage over rates on other major currencies. New Zealand already has one of the highest cash rates in the developed world, and a further tightening will only increase the high yielding allure of the Kiwi dollar. At nearly US$0.80, however, NZD will continue to dent the competitiveness of the nation's exporters, those outside the dairy industry that is.

ANZ commodity price index - in NZD



RBNZ MPS: 90 day interest rate track



Beyond July, risk of another hike

The RBNZ's hawkish June MPS hinted that further tightening may be required. With this in mind, and, even after assuming that the RBNZ will tighten now, there is a growing risk of another tightening in September. Further tightening depends on whether the key data-points mentioned above show decisive signs of turning in the third quarter.

The RBNZ's scenario analysis for short-term market interest rates in the latest MPS showed a higher "alternative scenario" that predicted a 90-day interest rate track peaking at 8.5% in 4Q, well above the 8.3% in the central projection. The central bank's alternative scenario was based on an economy that is "more stretched," in which "world dairy prices prove to be higher for longer" than the central projection. These factors appear to be playing out, with 1Q GDP coming in ahead of RBNZ expectations (at 1.0%q/q versus a 0.8% forecast), capacity utilization levels remaining elevated, nontradables inflation still holding at uncomfortably high levels, and dairy prices continuing to soar.

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Australia

- **This week's Aussie 2Q CPI data the clear highlight**
- **Core inflation to print at 0.7%q/q - not enough to trigger an August RBA move**
- **Monday's PPI a handy guide on pipeline price pressure**

The scarcity of top-tier economic data in Australia last week left market pundits to focus their attention on the upcoming release of 2Q CPI data (due July 25). Although annual headline inflation likely will print below the RBA's 2- 3% target range, the central bank board will retain a firm tightening bias, owing to emerging medium-term price pressures. JPMorgan believes that it would take a significant upside surprise on 2Q *core* inflation to trigger an August tightening. The forecast is for a 0.7%q/q rise, a material uptick from the 0.5% increases in the last two quarters, but not enough to prompt the RBA to pull the trigger.

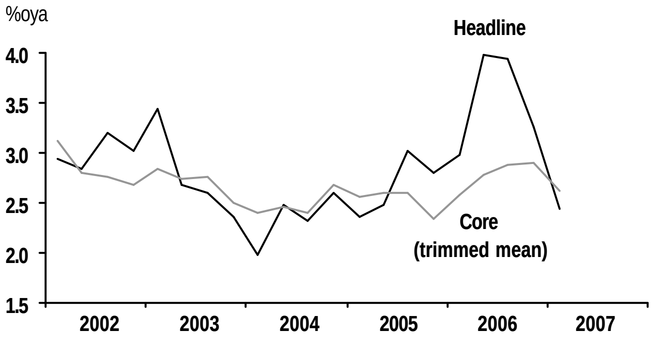
Preview: CPI to print below target range

The clear highlights this week will be Australia's 2Q producer and consumer inflation reports. On Monday, producer prices likely will show a 0.6%q/q rise, following the flat outcome in 1Q. Flat or falling import prices for key commodities owing to rising AUD will be insufficient to offset rising prices for the majority of industry's other inputs.

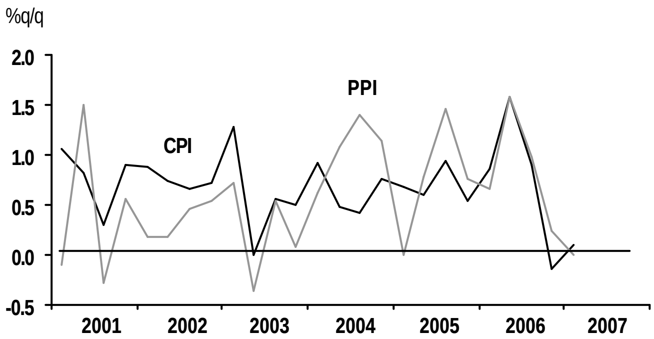
Wednesday's consumer price data, though, will all but determine whether the RBA stays on hold in early August, as forecast, or raises the cash rate for the ninth time in this extended tightening cycle. An upside surprise could convince the RBA that another tightening is warranted. At this stage, though, and ahead of the PPI data Monday, the forecasted 0.9%q/q jump in the headline CPI would represent a significant bounce from the benign 0.1% outcome in the first quarter, but would not be enough to trigger a rate rise.

Also, the high year-ago base stemming from a spike in petrol and banana prices back then means that the 2Q07 year-on-year rate of inflation will have plunged below the RBA's 2-3% target range. A low oya inflation outcome would make a rate hike in August very awkward for the RBA to explain, particularly with the federal election, in which interest rates will be a key point of policy differentiation, due within months. The RBA has never raised the cash rate in the months leading up

Australia: headline and core CPI



Australia: CPI and PPI



to an election, even though it has reiterated that it will tighten policy if necessary at any stage in the political cycle.

The forecast assumes that the main core inflation measures also stepped up in 2Q, to 0.7%q/q from the 0.5% prints of the previous two quarters, but this also will be insufficient evidence to warrant a rate hike. Moreover, with four-quarter growth in the core outcome down into the lower half of the RBA's target range, near-term policy action will remain unlikely. An outcome of 0.8%q/q on the trimmed mean or weighted median measures next week would make an August rate hike more likely, but a core outcome of 0.6% would confirm that the RBA will be sidelined until 2008. Assuming a 0.7%q/q outcome this week, our forecast is that the RBA will wait until next February, well after the federal election, before raising the cash rate again.

Gasoline price rises the main driver in 2Q

The main drivers of the expected acceleration in headline inflation in 2Q will have been gasoline prices (up 7.0%q/q); food, including fresh fruit and vegetables (up 5.0%), meat, dairy,

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and grains (up 2.0%), owing to the impact of the drought; rents (up 1.5%), which are rising at the fastest pace in 15 years; house purchase costs (up 2.0%); and electricity and gas prices (up 5.0% and 3.5%, respectively). Higher private health insurance premiums probably raised the hospital and medical services component 1.5%q/q.

Partly offsetting these price rises will have been lower prices for clothing, electronic equipment, and automobiles, owing mainly to high AUD, which last week reached a fresh 18-year high. Although last week's report of a 0.1%q/q rise in nationwide import prices came in above expectations, the wide gap between price pressure generated domestically and those generated by movements in the exchange rate remains at the core of the inflation outlook.

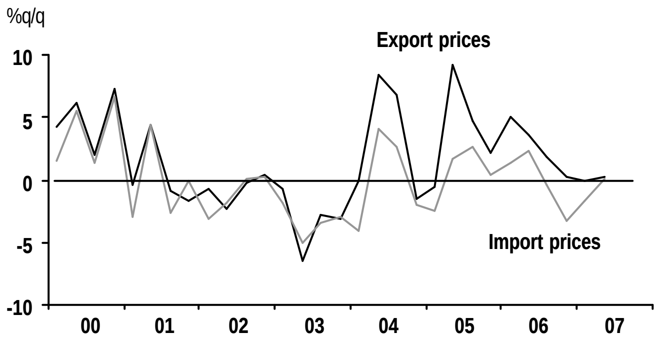
Core CPI revisions for the first time

One risk for the monetary policy outlook is the new phenomenon of possible revisions to the history of the critical statistical measures of core inflation—the trimmed mean and weighted median. Previously, these measures were calculated and released by the RBA 30 minutes after the release by the Australian Bureau of Statistics (ABS) of the headline inflation data. The fact that RBA officials did not have access to the CPI data prior to release by the statistics bureau meant there never were revisions to the back history of the statistical measures of core inflation in subsequent releases.

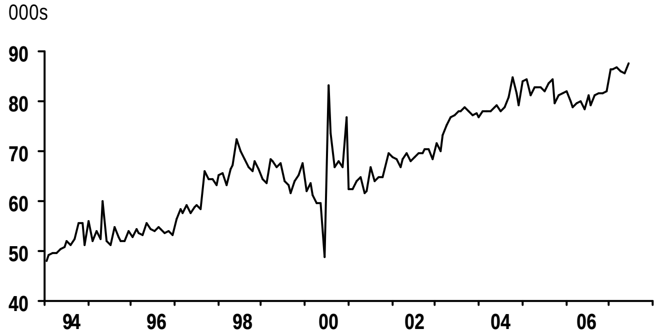
An agreement between the ABS and the RBA, however, means that the ABS now will calculate the statistical core measures, and with greater precision than was employed by RBA officials. The ABS will, for the first time, use concurrent seasonal adjustment factors for the 20 items of the CPI that exhibit seasonal patterns. This change means that, for the first time, there is a reasonable chance of revisions to previously published data. Also, in another change, the ABS will release the statistical measures previously released by the RBA, at the same time as the headline CPI data.

An upward revision to the already released 1Q statistical measures of core inflation could indicate a previously undisclosed pattern of gradually accelerating core inflation. If after the unexpectedly low 0.5%q/q print in 4Q06, core inflation in 1Q07 were revised higher from 0.5% to 0.6% before the expected 0.7% reading in 2Q07, a rate hike in August would be more likely. Alternatively, a downward revision to history would lower the accepted profile of core inflation, and lessen the urgency for a policy response, even if the 2Q outcome is unexpectedly high.

Australia: export and import prices



Australia: vehicle sales



Still, in the absence of material revisions to the back data, the forecast 0.7%q/q print for the trimmed mean and the weighted median in 2Q would be insufficient to trigger an August rate rise. It would leave core inflation running at 2.4%oya, in the lower half of the RBA's target range.

RBA's Stevens comfortable with high AUD

RBA Governor Glenn Stevens last week made one of his rare ventures into the public domain to deliver a speech commemorating the tenth anniversary of the Asian financial crisis. The Governor revealed useful insights into the causes, impacts, and lessons associated with the crisis but, not surprisingly, made no reference to the domestic policy outlook.

In the question and answer session after the speech, however, Stevens made observations on elevated AUD and the local impact of the subprime mortgage problems in the US. On the exchange rate, the Governor made clear his lack of surprise

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at AUD strength in light of the relative prices of exports and imports, noting that Australia's terms of trade in the last four years have risen 40% to a 50-year high. On credit risk, the Governor suggested that many central bankers would welcome a return to more realistic pricing of risk. He also wondered whether officials from local government authorities, many of whom are loaded up with sophisticated financial products backed by corporate debt, know the precise nature of the instruments they hold and the amount of risk involved.

Economic growth to continue apace

Solid economic growth over the next three to nine months will also keep upward pressure on inflation and interest rates. The Westpac-Melbourne Institute last week reported a 0.5-point rise (+0.2%) in its leading index of economic activity, which took the growth rate to 6.1% on an over-year-ago basis, well above the long-term trend of 4.4%. With economic growth already running above potential, the widening gap between the actual and potential growth rates will continue putting upward pressure on inflation, adding further reason for the RBA to maintain a firm tightening bias.

The rise in the leading index was largely attributed to the stock market gains enjoyed during May, with the All Ordinaries Index component contributing 0.9% point (compared to 0.8pt in the previous month) to the annualized growth rate. Real money supply, productivity, and real corporate gross operating surpluses also made positive contributions to the leading index—1.9, 1.5, and 2.0 percentage points, respectively—although these were less or the same as their contributions in April. Deducting from the leading index were dwelling approvals (-0.4pt), manufacturing material prices (-0.3pt) and overtime worked (-0.1pt).

Australia:
Data releases and forecasts

Week of July 23 - 27

Mon
Jul 23
11:30am

Producer price index
Not seasonally adjusted

	3Q06	4Q06	1Q07	2Q07
(%q/q)	1.0	0.2	0.0	0.6
(%oya)	4.0	3.5	2.8	1.8

Wed
Jul 25
11:30am

Consumer price index
Not seasonally adjusted

	3Q06	4Q06	1Q07	2Q07
Headline				
(%q/q)	0.9	-0.1	0.1	0.9
(%oya)	3.9	3.3	2.4	1.7
Core (trimmed mean)				
(%q/q)	0.7	0.5	0.5	0.7
(%oya)	2.9	2.9	2.6	2.5

Review of past week's data

WMI leading index
Seasonally adjusted

	Mar	Apr	May
(%m/m)	0.1	~~0.7~~ *0.6*	__ *0.2*

Sales of new motor vehicles
Units, seasonally adjusted

	Apr	May	Jun
(%m/m)	-1.4	-0.4	__ *2.2*
(%oya)	7.7	6.7	__ *11.3*

Import price index
Not seasonally adjusted

	4Q06	1Q07	2Q07
(%q/q)	-3.2	-1.7	__ *0.1*
(%oya)	0.0	-3.0	__ *-5.1*

Export price index
Not seasonally adjusted

	4Q06	1Q07	2Q07
(%q/q)	0.2	0.0	__ *0.3*
(%oya)	11.1	5.8	__ *2.4*

Export prices were up 0.3%q/q in 2Q, buoyed by higher prices of crude materials (+5.3%) and manufactured goods (+6.1%), while prices fell in all other components of the export price index. Import prices rose 0.1%q/q on the back of a 12.8% surge in import prices of mineral fuels. However, all other components of the import price index fell in response to the near 5% appreciation of AUD.

New Zealand

- **Nontradables inflation in NZ remains elevated**
- **RBNZ now seen lifting interest rates this week**
- **Net-permanent migration points to cooling demand**

Inflation remained at the core of the economic radar in New Zealand last week. Although headline CPI came in above expectations in 2Q, markets centered their attention on the reading of nontradables inflation, which printed at an unexpectedly high 4.1%oya in the June quarter. In consideration of the inflation report, in addition to a myriad of other key economic factors, JPMorgan now anticipates that the RBNZ will raise the official cash rate by 25 basis points to a fresh record high of 8.25% on Thursday.

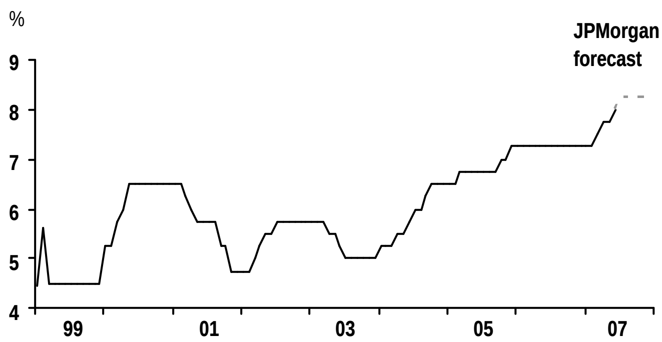
Preview: RBNZ to hike rates to a record

With data last week showing nontradables inflation still running above the psychological 4%oya level, a July tightening in New Zealand now appears warranted. In a change of forecast, therefore, JPMorgan expects the RBNZ to raise the official cash rate by 25bp on Thursday, taking the key rate to a record high of 8.25%. In this week's research note titled "RBNZ now expected to hike cash rate to 8.25% this week", we outline four key criteria that have supported another tightening. Three of the four rate hike criteria—still elevated business confidence, stubbornly buoyant retail spending, and rising house prices—argue for another rate hike but, on their own, are not sufficient to push the RBNZ across the line.

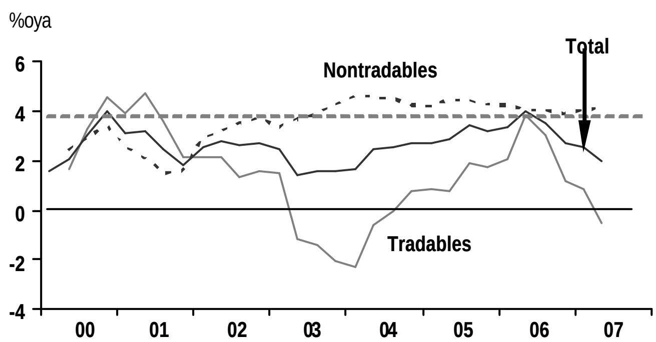
The most important of the four data points, however, came to hand last week—nontradables inflation. Nontradables inflation printed above expectations in 2Q, logging an annual growth rate of 4.1%. Although much of the momentum in inflation was driven by a jump in gasoline prices and a surge in electricity costs, the persistently high reading surely will unnerve the RBNZ. Moreover, the likely second-round impacts of rising gasoline, electricity, and food prices suggest that nontradeables inflation will remain elevated near-term.

The RBNZ has raised the OCR three times this year in an effort to create a lower inflation trajectory, and hawkish public commentary indicates that officials have sufficient

RBNZ official cash rate



New Zealand: consumer price index



determination to go further. Frustrations among central bank officials over their inability to drag inflation lower mean that another rate hike beyond July cannot be ruled out. That said, tightening beyond July will remain highly dependent data developments over the quarter.

Nontradeables inflation still elevated

Inflation pressures in continued to build in 2Q, with headline inflation posting a larger than expected gain of 1.0%q/q (JPMorgan and consensus 0.7%), or 2.0%oya. The faster than expected growth in CPI was fuelled by a 2.4%q/q rise in the transport-related group, driven by a 8.0%q/q spike in petrol prices. If gasoline prices had remained flat, headline CPI would have risen just 0.6%q/q.

More concerning for the interest rate outlook, however, was the 1.1%q/q gain in nontradables inflation—nontradables being those goods and services that do not face foreign competition. Nontradables inflation was again driven by prices emanating out of the housing market, with prices of housing and household utilities rising 2.6%q/q. A 3.0%q/q surge in electricity prices, and a 1.6% rise in the purchase of new housing, also contributed to the overall spike in prices in the housing group.

Net-Permanent Migration trends lower

Annual growth in net-permanent migration fell to a 14-month low in June, suggesting demand for housing and broader consumption will ease. According to Statistics New Zealand, in seasonally adjusted terms, net permanent and long-term migration was 10,100 in the June 2007 year, down from the net gain of 10,700 in the June 2006 year. Annual net PLT migration has eased since reaching 14,800 in the November 2006 year. The June 2007 year's figure is close to the annual average of 12,200 recorded for the December years 1990–2006. There is a strong relationship between annual net PLT, house prices and consumption growth (chart). Last Friday's data suggests some downside to 3Q data.

New Zealand:
Data releases and forecasts

Week of July 23 - 27

Thu
Jul 26
9:00am

RBNZ cash rate announcement

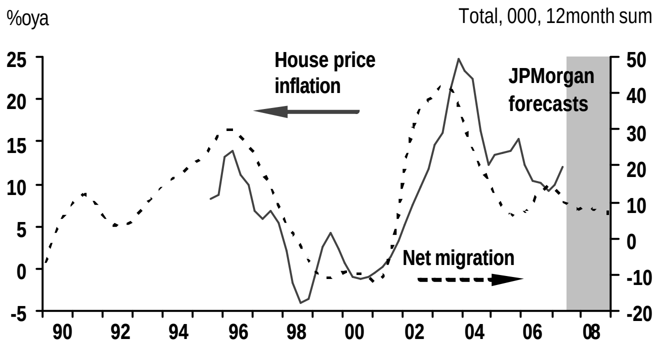
The RBNZ is expected to hike the OCR to 8.25%.

Fri
Jul 27
10:45pm

Trade balance
Not seasonally adjusted

	Mar	Apr	May	Jun
Exports ($NZ mn)	3321	3196	3352	__
Imports ($NZ mn)	3257	3385	3343	__
Trade balance ($NZ mn)	65	-189	9	__

New Zealand: house price inflation and net permanent migration



Review of past week's data

Consumer price index
Not seasonally adjusted

	4Q06	1Q07	2Q07	
Headline (%q/q)	-0.2	0.5	~~0.7~~	*1.0*
Headline (%oya)	2.7	2.5	~~1.7~~	*2.0*
Nontradables (%q/q)	0.8	1.2	~~0.8~~	*1.1*
Non-tradable (%oya)	3.8	4.1	~~3.9~~	*4.1*

Credit card spending
Seasonally adjusted

	Apr		May		Jun	
(%oya)	~~7.8~~	*8.0*	~~5.8~~	*5.7*	___	*9.1*

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Global essay

- **China's booming growth signals strong internal and external demand**
- **Futures market points to lower US (and global) gasoline prices**
- **Data, rather than election outcome, are key to August BoJ decision**
- **Strong activity data are putting pressure on BoE and RBNZ**

China's boom reflects domestic and global strength

Last week's financial market developments underscore the risk that an unexpected, sharp tightening in financial conditions has the potential to slow the global economy in coming months. Barring such a tightening, activity data are sending mostly positive signals about global growth prospects. The jury is still out on the strength of the US economy after what is expected to have been a solid second quarter. We remain comfortable with the view that, with the housing market downturn losing force and gasoline prices moving lower, the US economy will generate growth of 3% or better in coming quarters. Looking beyond the United States, the latest business surveys and the hard activity data from Europe and Asia point to continued above-trend growth. Likewise, rising commodity prices continue to support growth in the commodity-exporting emerging economies.

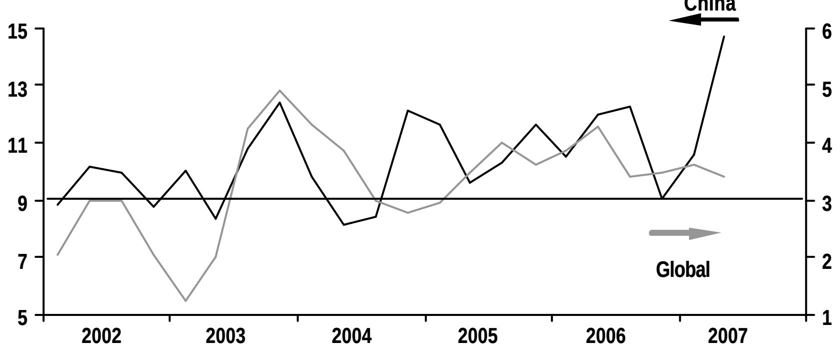
The latest data from China deliver a strong message about its own and global growth. The 2Q quarterly advance in real GDP, estimated to be 15.9% (q/q, saar), was the strongest since the early 1990s, with the exception of the 3Q03 increase that followed the SARS crisis. China's growth is multifaceted, featuring huge increases in retail sales, fixed-asset investment, and exports. Moreover, the strength of the June activity indicators suggests that the economy has carried strong momentum into the current quarter.

China's big gains in domestic demand are an important source of demand for its trading partners. Capital goods producers in EM Asia, Japan, Germany, and the United States are benefiting from the rapid pace of investment spending. At the same time, the strength of China's exports and industrial production serve as a window on global final demand and the unfolding acceleration in global industry. On this score, we estimate that China's manufacturing output advanced 29%q/q, saar in 2Q, the fastest pace of the 2000s expansion.

Consumer price inflation has risen in China alongside the faster pace of economic growth, reaching 4.4%oya in June. This development, combined with the booming pace of first-half growth, ensures that authorities will continue to adjust policy accordingly. In addition to today's interest rate increase, policymakers are likely to rely on higher bank reserve requirements, increased bank "window guidance," and tighter administrative controls on lending. These moves, combined with additional currency appreciation, are expected to deliver more moderate second-half growth, mainly through a reduced rate of investment spending. In this vein, it is important to realize that the authorities are not uncomfortable with rapid growth *per se*, particularly as the recent jump in inflation can be attributed primarily to a food price runup, with the core rate remaining below 1%oya.

Real GDP

% ch over 2 qts, saar; both scales



Contributions to US retail gasoline price

	Aug 06	Jan 07	May 07	Jul 07	Sep 07	Dec 07
Oil price ($/bbl)	73	54	63	76	76	75
($/gal)	*1.75*	*1.29*	*1.51*	*1.81*	*1.80*	*1.78*
Crack spread ($/bbl)	11	7	33	16	10	9
($/gal)	*0.27*	*0.16*	*0.79*	*0.38*	*0.24*	*0.23*
Retail markup ($/bbl)	41	36	39	38	32	32
($/gal)	*0.98*	*0.85*	*0.93*	*0.90*	*0.75*	*0.76*
Retail price ($/gal)	*3.00*	*2.29*	*3.23*	*3.09*	*2.79*	*2.77*

Note: Actual values are monthly averages. The oil price and crack spread projections are based on futures market prices as of Jul 17, 2007. The retail markup projections are generated from an ARMA(1,1) model with a linear trend estimated from Jan 90 to Jan 07. There are exactly 42 gal/bbl.

The door is open to lower gasoline prices

Since May, the WTI spot price for oil has climbed about $13/bbl, and yet this has coincided with a fall in the average price of US retail gasoline from $3.23/gal to $3.09/gal. This seeming disconnection reflects a significant fall in margins along the supply chain. In particular, the spread between the price of oil and wholesale gasoline (i.e., the crack spread)—which surged to a record high in the period from January to May—has plunged in the last two months by $17/bbl ($0.41/gal) and the retail markup has fallen $1/bbl ($0.03/gal). To a lesser degree, crack spreads and retail prices have fallen in Canada and Europe, as well. These developments are consistent with our previous analysis that gasoline prices will shift from being a headwind to a tailwind for consumer spending in 2H07 ("Consumers will be supported by lower gas prices in 2H07, *GDW*, Jun 22).

In the accompanying table, we provide a roadmap for gasoline prices based on information from the futures market. The market is anticipating a significant further decline in the crack spread, to $10/bbl in September and $9/bbl in December. This is expected to happen alongside a stable crude oil price. To complete the model, we project the retail markup to edge down in the coming months (no futures market exists). Based on these inputs, the retail price of gasoline would fall roughly $0.32/gal to $2.77/gal by December. Our energy analysts are more bearish on oil prices, looking for them to fall to $60/bbl by year's end, much as they did last year. In this case, the gasoline price would fall by a much greater 22% to $2.41/gal.

Data, not election, hold key to BoJ decision

Japan's Upper House election is less than a week away, with 122 seats in the balance. In the lead-up to the July 29 vote, opinion polls show that support for the LDP is falling, while that for the DPJ is rising. If the LDP wins fewer than 44 seats, there is a significant chance that Prime Minister Abe will resign. Whatever the outcome, we do not believe that the election will have a big impact on the BoJ's August rate decision. The key issue for the BoJ is whether it is still comfortable with its forecast for above-trend growth and a gradual rise in inflation.

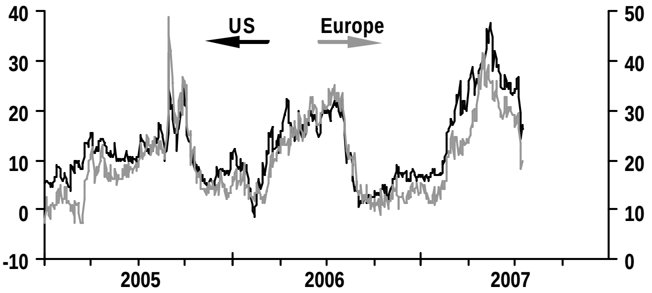
Between now and the August 23 policy meeting, the industrial production report for June is likely to be the most important economic indicator release. In particular, policymakers are looking for signs that manufacturing activity is turning the corner after back-to-back declines in 1Q and 2Q. The BoJ also will be keen to see the 2Q GDP report. Governor Fukui already has stated that policymakers expect that growth downshifted last quarter. But an extremely weak outcome, especially if produced by an unexpected shortfall in domestic demand, might stay the BoJ's hand. In this regard, this week's report that department store sales were robust in June suggests that consumer spending ended the quarter on a strong note.

Screws tightening on Bank of England

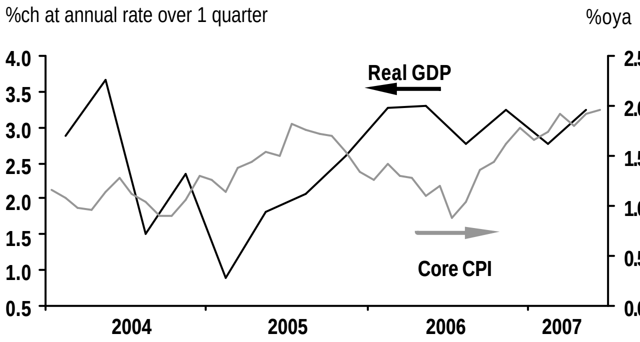
Rapid growth and accelerating prices are leaving little wiggle room for the BoE. GDP in the UK strengthened 0.8%q/q (sa) in 2Q, its sixth straight quarter of above-trend growth. Excluding the energy and government sector, core output growth has been running at roughly a 4% annualized pace. At the same time, headline inflation is easing back toward the 2%oya target more slowly than the BoE expected, while the core rate, which excludes energy, food, alcohol, and tobacco, reached a decade high of 2% in June. In all, it is becoming increasingly clear that meeting the inflation target will require a meaningful slowing in growth. We maintain that the BoE will raise the

Crack spreads

$/bbl, both scales



Real GDP and core CPI, UK



base rate to 6% in September, and stress that an August hike is not out of the question.

Debate continues within the BoE over whether the 200bp rise in the base rate since the fall of 2003, combined with the 5% appreciation of the trade-weighted exchange rate over the last year, is sufficient to generate the necessary slowing in activity. In addition, the puzzling weakness in employment growth in recent months and the potential for a sharp downshift in consumer spending is of some concern. However, signs that households are reining in spending in response to weak income gains and higher rates are at best tentative. Our forecast anticipates a gradual easing in consumption growth to a 2% pace over time, but evidence of that slowing is likely to take time to accumulate and the BoE is not likely to wait until such evidence shows through.

New Zealand rate hike sooner, not later

The noninflationary limits of growth are also being tested in New Zealand, where buoyant asset prices, upbeat business confidence, and robust consumer spending are reflecting an economy that is expanding at an above trend-pace. This was evident in the details of last week's inflation reading. Although headline inflation eased to 2%oya in 2Q, prices for nontradables rose at an unexpectedly high rate of 4.1%oya and have now been rising around 4% per annum over the past four years.

In response, JPMorgan now expects the RBNZ to raise the OCR 25bp to a record-high 8.25% on Thursday. Four key data reports have been released since the June policy meeting, and collectively, they have remained elevated enough to push the central bank into tightening policy again. Three of the four reports—rising house prices, elevated business confidence, and stubbornly strong retail spending—argue for another rate hike, but on their own are still not sufficient. However, the recent inflation report is likely force the Reserve Bank's hand.

Brazil eases again but with less conviction

In Brazil, monetary policy continues to ease, although strong growth amid tightening resource utilization is tempering the process. The COPOM cut the Selic rate 50bp this week as expected. However, whereas last month's 50bp cut came against two dissenting votes (out of seven) calling for a more modest 25bp cut, last week's action garnered three such dissents. The policy statement this time indicated that the positive inflation outlook justified the easing, but that future monetary policy actions will be more data-dependent.

The COPOM's statement, combined with the closer vote margin, is consistent with our view that the pace of policy easing will slow in September. Output appears to be expanding at an above-trend pace and inflation expectations have begun to shift up. Indeed, surprisingly strong economic activity figures in 2Q are prompting an upward revision to our full-year 2007 GDP growth forecast, tentatively to around 5%oya, from our current estimate of 4.4%.

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JPMorgan View - Markets

A traffic jam in credit

- **Cross-markets:** Fallout from credit on equities and EM to be limited by strong growth and earnings.

A tale of two worlds. But can it last?

- **The bond world remains in the midst of a flight to quality,** but this has been **largely ignored by equity, currency, and emerging markets**. Outside of the bond world, investors see the turmoil in corporate credit largely as a welcome correction to more rational pricing rather than a deterioration in economic or corporate fundamentals. As such, this is healthy. Within bond markets, the turmoil is closer at hand and thus more real. Our view is that over coming weeks, headline news from US subprime and the traffic jam in leveraged credit will **continue to push up credit spreads and drive government bond yields down.** This will likely have some negative impact on equities, but the damage should be limited by still positive news from 2Q earnings.

- Beyond the turmoil in credit markets, the fundamentals of strong economic growth and corporate earnings, combined with subdued inflation, are keeping us **positive on global equities and emerging markets over coming months. Credit** spreads should eventually recover some of their losses, but not all, as investors are unwilling to accept the loose conditions that prevailed until a month ago. Into late summer, bond yields will likely rise again as credit markets settle down and central banks repeat their concerns about inflation.

Fixed income

- **Bonds rallied strongly,** especially in North America and Europe, on continued negative headline news from US subprime as well as signs of a liquidity jam in leveraged loans and bonds. The significant widening of swap and corporate spreads shows that there is a large **flight to quality** element to the recent rally.

- **This flight to quality rally in bonds is not over.** Near term, it will likely be further rating actions on leveraged products and hedge-fund failures that create more fireworks. And medium term, there will be further rises in delinquencies on subprime mortgages. But at some point—our guess is within the month—investors will find bonds expensive relative to the message from hawkish central banks and robust economic activity data. Bond yields will then likely rebound. We continue to see **higher bond yields in 2-3 months time, even as we are long duration over coming weeks.**

Government bond yields

		Current	Sep 07	Dec 07	Mar 08	Jun 08
United States	2-yr	4.76	5.15	5.60	5.75	5.65
	10-yr	4.95	5.25	5.65	5.75	5.60
Euro area	2-yr	4.41	4.55	4.60	4.50	4.30
	10-yr	4.44	4.60	4.65	4.60	4.40
United Kingdom	2-yr	5.65	5.90	5.95	5.90	5.80
	10-yr	5.32	5.65	5.70	5.70	5.65
Japan	2-yr	1.03	1.10	1.20	1.50	1.40
	10-yr	1.89	2.10	2.10	2.30	2.30
Canada	10-yr	4.55	4.75	5.05	5.05	5.05
Australia	10-yr	6.15	6.50	6.85	6.90	6.70
Korea	5-yr	5.47	5.40	5.50	5.60	5.50
Mexico	10-yr	7.75	7.60	7.60	7.70	7.70
Singapore	10-yr	2.97	3.50	3.75	3.90	4.00
South Africa	10-yr	8.49	8.15	8.50	8.45	8.45
Sweden	10-yr	4.38	4.50	4.55	4.50	4.30

Equities

	Current	Ytd return (local currency)
S&P	1534	10.1%
Topix	1776	5.3%
FTSE 100	6585	7.7%
MSCI Eurozone	256	12.5%
MSCI Europe	1629	10.4%
DAX	7875	19.7%
CAC	5957	10.9%

Sector allocation for equities

	Deviation	Recommendation[1]
Energy	3.2%	Overweight
Materials	-1.5%	Underweight
Industrials	0.8%	Neutral
Consumer discretionary	-3.2%	Underweight
Consumer staples	3.9%	Overweight
Healthcare	2.7%	Overweight
Financials	-3.6%	Underweight
Information technology	-2.3%	Underweight
Telecommunications	2.3%	Overweight
Utilities	-2.4%	Underweight

1. Recommendations reflect current stance, which can change over the year.

Regional allocation for equities

	Deviation	Recommendation
North America	2.0%	Neutral
United Kingdom	-3.0%	Underweight
Eurozone	-2.1%	Underweight
Rest of Europe	-0.4%	Neutral
Japan	3.8%	Overweight
Asia ex Japan	-0.3%	Neutral

Source: JPMorgan.

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- **EM local bonds** have been most insulated from the turmoil in riskier markets. They gained in recent weeks, because both their currencies and core bond markets rallied. We stay long both outright and against core markets at present, but recognize that we will need to become more cautious into the fall, as EM central banks are slowly starting to hike rates to assure that their strong growth does not become inflationary.

Equities

- Equities succumbed to profit-taking last week as continued weakness in credit markets and expectations of a slowing in LBO activity weighed on the market, despite an unexpectedly good 2Q US earnings season. A repricing of high-yield credit means that private equity financing is becoming more expensive and more difficult to complete. This will likely **slow LBO activity**, removing some support for equity markets. But strategic M&A, as well as recapitalizations and other forms of shareholder-enhancing transactions, will likely stay strong.

- Accommodative monetary conditions, rising currencies, and high commodity prices are supportive of **EM equity markets**, especially domestic demand-oriented sectors. A booming China is leading the surge in EM growth and we stay long there despite the 50% gain in Chinese equities ytd. We overweight Singapore, China, Thailand, the Philippines, and Brazil; and underweight Hong Kong, South Korea, India, Hungary, and Czech Republic.

Credit

- **Credit spreads underwent further weakness**, with CDS hitting fresh wide levels, on news of large hedge fund losses and continued worries about the US housing and subprime markets and the supply overhang in US high yield. These issues are unlikely to be resolved soon; we thus expect volatility to stay high for at least a few weeks.

- We expect further deterioration in **US subprime** well into 2008. Problems to date have been related largely to poor underwriting or weak housing prices. But later this year, resets of subprime mortgages will likely lead to further weakness.

- **US high yield** spreads are likely to remain volatile in coming weeks. But over the next several months, with fundamentals still healthy but a sizable supply backlog capping meaningful upside, we see high yield spreads consolidating in a 300-350bp range.

- The market-directionality of correlation has reversed its typical pattern, where correlation used to fall with significant spread widening. The recent correction saw a **rise in correlation** as credit investors are more comfortable taking default risk in place of market risk in the current environment. Demand for mezzanine risk, a traditional source of the "structured bid," should rebound once spreads stabilize, reversing the rise in correlation.

Credit markets

	Current	Dec 07
US high grade (bp over swaps)	40	35-40
Euro HG industrials (bp over swaps)	35	35-40
USD high yield (bp vs. UST)	346	325
EMBIG (bp vs. UST)	190	150

Commodities

		Quarterly average			
	Current	07Q3	07Q4	08Q1	08Q2
WTI oil $/bbl	75.9	67.0	60.0	56.0	52.0
Gold ($/oz)	684	660	675	700	715

Foreign exchange

	Current	Sep 07	Dec 07	Mar 08	Jul 08
EUR/USD	1.38	1.35	1.36	1.33	1.31
USD/JPY	121	123	125	126	125
GBP/USD	2.06	2.01	2.03	2.02	1.98

- **EM external debt** spreads widened 15bp on the week, dampened by corporate credit markets. Our latest client survey showed **that investors scaled back risk** in external debt, leaving their overall exposure close to neutral. Ytd inflows into EM debt stand at $17bn and are now tracking our $25bn forecast for the year. We stay medium-term positive and overweight selected markets that also benefit from high commodity prices: i.e., Brazil, Russia, and Venezuela.

Foreign exchange

- Fed Chairman Bernanke's semiannual testimony confirmed our view that the Fed is going to remain on hold until at least late this year. This outcome is supportive for risky assets and thus carry trades. We remain **short the yen** versus USD, AUD, NOK, and GBP.

- Similarly, **high-yielding emerging market** currencies have benefited from Bernanke's testimony. We continue to **hold exposures outside Asia** where central bank intervention tends to be less aggressive (long BRL, TRY, and HUF).

Commodities

- We look for **WTI prices to stay supported in 3Q**, owing to geopolitical risk and seasonal demand, before moderating in 4Q. The **softer USD allowed gold and silver to rise sharply**. We remain bulls for precious metals short and long term and bulls for base in the short term. Gold is expected to trade towards the $700-715/oz level by mid-2008.

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AUD and NZD Commentary

- **Interesting differences in policymaker comfort with AUD versus NZD in recent days**
- **History suggests NZD may not benefit that much even if RBNZ hikes rates again in coming week**
- **Technicals: Vulnerable to a short term pullback, but interim trends continue to point higher**

Strategy comments

- Broad US dollar weakness was the main factor lifting both AUD and NZD in the latest week: AUD/USD and NZD/USD rose 1.3% and 1.4%, respectively. That said, even with some late-week subprime jitters, an interest in carry trades lingered: AUD and NZD still posted trade-weighted gains during the week of 0.7% and 0.8%, respectively.
- Separately, last week brought sharp contrast in policymaker comfort levels regarding Antipodean currencies, suggesting that NZD outperformance may not last. In Australia, central bank Governor Stevens suggested that AUD strength largely reflected terms of trade trends, and that AUD levels are "unsurprising." Contrast that with not only actual RBNZ intervention to sell NZD in recent weeks, but also on Wednesday, reported comments from New Zealand Finance Minister Cullen that the government does not rule out preventing further rate hikes. In a New Zealand Herald interview, Cullen said that a little-known section of the Reserve Bank Act, known as "section 12", would allow the government to order the RBNZ to make interest rate decisions not just based on traditional inflation measures but also on other measures such as FX levels. While Cullen himself suggested such a step was not imminent, the verbal "warning shot" suggested greater discomfort in New Zealand with both yields and the Kiwi.
- Antipodean focus in the week ahead is squarely on the RBNZ meeting. Following strong business confidence, retail spending, house price and critically, non-tradeable inflation data, JPMorgan changed its forecast from steady to higher rates on July 26. In a world where investors are extremely focused on yield, a G-10 currency likely to offer policy rates at 8.25% would seem an easy buy. And indeed, we see NZD holding relatively firm against most peers (especially low-yielding JPY) for the next few months at least. However, looking more immediately around recent RBNZ hikes, NZD has not actually fared that well. Indeed, looking at the last 10 rate hikes, NZD has consistently softened, albeit very modestly, in the two trading weeks following a hike (by an average 0.5%). We expect this pattern to reflect a few things: first, the fact that speculative investors likely took some tactical profits on long NZD positions following these meetings; second, the fact that New Zealand policymakers often verbally intervened to stem NZD strength following recent rate hikes.

Technical analysis

- AUD/USD and NZD/USD hit new cyclical highs last week, as the bullish action stays intact. The trends still seem resilient and while there is potential for a near term pullback in both, we still see little evidence of a sustained reversal.
- The rally in NZD/USD has turned into more of a grind to new highs, suggesting the upside momentum is waning. However, with key supports intact new highs are likely beyond any near term pullback. Support starts at 0.7940 and then 0.7880, while the 0.7715-00 area will now act as a short term floor. Deeper targets enters at 0.8000/30 and then the 0.8100 zone.
- We see a similar setup for AUD/USD going into next week, as near term pullbacks should find support in the 0.8755/30 area before releasing higher. Targets start at 0.8865/75 and then 0.8900/20. The 0.8640/00 zone should act as a short-term floor.

AUD/USD - Daily technical chart

Source: CQG, Inc. © 2007 All rights reserved worldwide. www.cqg.com Fri Jul 20 2007 16:26:12

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Global Economic Outlook Summary

	Real GDP % over a year ago			Real GDP % over previous period, saar							Consumer prices % over a year ago			
	2006	2007	2008	4Q06	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	1Q07	2Q07	4Q07	2Q08
The Americas														
United States	3.3	2.3	2.8	2.5	0.7	3.5	3.0	3.5	3.0	2.5	2.4	**2.7**	**3.4**	**2.3**
Canada	2.8	2.6	2.6	1.5	3.7	3.0	3.0	2.8	2.5	2.3	1.8	**2.2**	**3.1**	**2.0**
Latin America	5.3	4.5	4.7	4.2	2.9	**4.9**	5.1	5.2	4.5	4.7	5.0	**5.0**	**5.1**	5.7
Argentina	8.5	8.0	6.0	6.8	3.9	10.8	8.2	8.2	5.3	4.1	9.5	8.8	8.1	9.4
Brazil	3.7	4.4	4.5	4.3	3.1	3.8	4.2	4.8	4.1	5.5	3.0	3.2	3.6	3.5
Chile	4.0	6.0	5.0	7.9	9.5	5.5	4.0	4.0	5.5	5.5	2.7	2.6	3.6	3.1
Colombia	6.8	6.8	5.5	2.0	10.3	6.9	5.0	5.0	5.5	5.5	5.2	6.3	5.7	4.7
Ecuador	4.1	3.0	2.0	1.0	2.5	5.0	6.5	5.0	1.5	0.0	2.1	1.6	2.1	3.4
Mexico	4.8	2.8	4.5	1.5	0.6	**4.1**	4.9	4.9	4.9	4.5	4.1	**4.0**	**4.0**	**4.1**
Peru	7.8	7.0	6.0	10.6	3.5	4.0	8.0	5.0	4.5	5.5	0.4	0.7	2.1	2.1
Venezuela	10.3	7.0	3.5	11.5	3.3	5.0	6.0	6.5	2.5	2.0	19.1	19.5	19.1	27.3
Asia/Pacific														
Japan	2.2	2.8	2.4	5.4	3.3	1.7	3.0	2.8	2.5	2.3	-0.1	0.0	0.1	0.4
Australia	2.7	4.1	3.4	4.3	6.6	2.8	3.7	3.8	4.5	2.8	2.4	1.6	3.3	3.7
New Zealand	1.5	2.7	2.3	3.3	4.2	2.0	2.3	2.1	2.3	3.2	2.5	1.7	1.9	2.4
Asia ex. Japan	8.4	**8.1**	**7.7**	**6.2**	**9.2**	**10.1**	**6.9**	**5.9**	**8.8**	**8.3**	3.2	**3.4**	**3.3**	3.4
China	11.1	**11.3**	**10.5**	**7.6**	**13.6**	**15.7**	**8.2**	**6.1**	**13.0**	**12.6**	2.7	**3.6**	**2.9**	**2.9**
Hong Kong	6.9	5.3	4.6	6.1	2.0	4.5	7.5	5.5	4.5	3.8	1.7	1.4	2.4	3.3
India	9.4	8.0	7.5	7.4	11.4	6.6	7.4	7.0	8.7	7.0	7.0	6.0	5.1	5.4
Indonesia	5.4	6.2	6.0	4.2	7.1	6.0	5.5	5.5	6.0	5.0	6.4	6.2	6.8	6.8
Korea	5.0	4.4	4.8	3.8	3.6	5.5	4.2	5.0	4.5	5.0	2.0	2.3	2.9	3.2
Malaysia	5.9	5.8	5.6	3.8	5.4	6.6	6.0	6.0	5.3	5.3	2.6	1.8	2.2	2.2
Philippines	5.4	6.7	5.9	3.4	10.2	6.5	6.6	6.5	6.0	5.0	2.9	3.3	3.7	3.7
Singapore	7.9	**7.5**	**5.2**	7.9	7.6	**12.8**	**5.0**	**5.0**	**4.3**	**4.5**	0.5	**0.9**	**2.0**	**1.3**
Taiwan	4.7	4.5	4.6	4.8	0.4	5.8	6.3	5.7	4.0	3.8	1.0	0.2	2.2	2.3
Thailand	5.0	4.2	5.1	2.5	4.9	4.5	5.6	5.5	5.5	5.5	2.5	2.0	2.4	2.4
Africa														
South Africa	5.0	4.8	4.9	5.6	4.7	4.5	4.4	4.2	4.9	5.8	5.9	6.8	5.9	4.8
Europe														
Euro area	2.9	2.9	2.1	3.6	2.9	2.4	3.0	2.5	1.8	1.8	1.9	1.9	2.3	2.0
Germany	3.0	3.0	2.2	4.0	2.1	2.5	3.0	2.8	1.8	1.8	1.9	1.6	1.7	1.2
France	2.2	2.0	2.1	1.6	2.2	2.2	2.6	2.3	2.0	2.0	1.3	1.3	2.0	1.7
Italy	1.9	2.1	1.7	4.7	1.1	1.5	2.0	1.8	1.6	1.6	2.0	1.9	2.0	1.9
Norway	4.6	4.5	3.1	4.1	5.7	3.0	3.5	3.5	3.0	3.0	1.0	**0.3**	**0.4**	2.4
Sweden	4.5	**3.2**	**3.0**	3.6	2.6	**2.8**	4.0	3.5	3.0	2.5	1.9	**1.8**	**2.8**	**2.6**
Switzerland	2.7	2.4	1.9	2.0	3.2	2.5	2.3	2.0	1.8	1.8	0.0	0.5	1.1	1.0
United Kingdom	2.8	2.9	2.6	3.3	2.8	3.0	2.8	2.8	2.7	2.5	2.9	2.5	2.1	2.1
Emerging Europe[1]	6.3	**6.3**	**6.1**	10.7	4.9	5.7	6.0	8.0	4.3	7.4	6.5	6.5	5.9	5.3
Bulgaria	6.1	6.4	4.7	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	6.4	5.8	5.5	6.1	6.1	5.0	5.0	5.0	5.5	6.0	1.5	2.3	3.4	3.2
Hungary	3.9	2.8	3.3	2.8	2.4	2.5	3.5	3.5	3.2	3.0	8.5	8.5	5.3	3.4
Poland	6.1	6.5	6.0	7.0	7.0	5.0	5.5	5.8	6.3	6.3	2.0	2.4	2.7	2.5
Slovak Republic	8.3	9.0	7.5	9.2	9.1	8.0	7.5	7.5	7.5	7.5	2.8	2.4	2.6	2.4
Romania	7.7	6.5	6.0	...	...	...	...	...	...	...	3.8	5.7	5.2	5.0
Russia	6.7	**7.2**	**6.8**	14.6	3.7	6.0	5.0	12.0	2.0	8.0	7.9	7.8	7.7	7.3
Turkey	6.1	5.0	6.0	...	...	...	...	...	...	...	10.3	9.6	7.3	5.7
Global	3.8	**3.5**	3.3	4.0	3.1	**3.9**	**3.7**	**3.7**	**3.4**	**3.3**	2.3	2.4	**2.8**	**2.4**
Developed markets	3.0	2.7	2.5	3.3	2.2	2.8	3.0	3.0	2.5	2.3	1.8	1.9	**2.4**	**1.9**
Emerging markets	6.9	**6.6**	**6.4**	**6.4**	**6.8**	**8.0**	**6.3**	**6.1**	**6.9**	**7.2**	4.3	4.4	**4.3**	4.3

Note: For some emerging economies, 2006-2008 quarterly forecasts are not available and/or seasonally adjusted GDP data are estimated by JPMorgan.
Bold denotes changes from last edition of *Global Data Watch*, with arrows showing the direction of changes.

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Global Central Bank Watch

	Official interest rate	Current	Change from Jun 04 (bp)	Last change	Forecast next change	Sep 07	Dec 07	Mar 08	Jun 08	Dec 08
Global	GDP-weighted average	4.75	222			4.90	5.05	5.31	5.30	5.33
excluding US	GDP-weighted average	4.51	126			4.69	4.78	4.93	4.91	4.96
Developed	GDP-weighted average	4.13	262			4.28	4.46	4.80	4.80	4.84
Emerging	GDP-weighted average	7.43	28			7.46	7.44	7.40	7.31	7.30
The Americas	GDP-weighted average	5.51	354			5.61	5.80	6.22	6.21	6.21
United States	Federal funds rate	5.25	425	29 Jun 06 (+25bp)	11 Dec 07 (+25bp)	5.25	5.50	6.00	6.00	6.00
Canada	Overnight funding rate	4.50	250	10 July 07 (+25bp)	5 Sep 07 (+25bp)	4.75	4.75	5.25	5.25	5.25
Brazil	SELIC overnight rate	**11.50**	-450	**18 July 07 (-50bp)**	**5 Sep 07 (-50bp)**	11.25	10.75	10.25	10.00	10.00
Mexico	Repo rate	7.25	75	27 Apr 07 (+25bp)	21 Sep 07 (+25bp)	7.50	7.50	7.50	7.50	7.50
Chile	Discount rate	5.25	350	12 July 07 (+25bp)	9 Aug 07 (+25bp)	5.50	5.75	5.75	5.75	5.75
Colombia	Repo rate	9.00	225	15 Jun 07 (+25bp)	27 Jul 07 (+25bp)	9.50	9.50	9.50	9.50	9.00
Peru	Reference rate	4.75	225	5 July 07 (+25bp)	1Q 08 (+25bp)	4.75	4.75	5.00	5.00	5.00
Europe/Africa	GDP-weighted average	4.83	165			5.08	5.25	5.42	5.39	5.39
Euro area	Refi rate	4.00	200	6 June 07 (+25bp)	6 Sep 07 (+25bp)	4.25	4.50	4.75	4.75	4.75
United Kingdom	Repo rate	5.75	125	5 July 07 (+25bp)	6 Sep 07 (+25bp)	6.00	6.00	6.00	6.00	6.00
Sweden	Repo rate	3.50	150	20 Jun 07 (+25bp)	7 Sep 07 (+25bp)	3.75	4.00	4.25	4.25	4.25
Norway	Deposit rate	4.50	275	27 Jun 07 (+25bp)	15 Aug 07 (+25bp)	5.00	5.25	5.50	5.75	5.75
Czech Republic	2-week repo rate	2.75	50	31 May 07 (+25bp)	26 July 07 (+25bp)	3.25	3.50	3.75	4.00	4.50
Hungary	2-week deposit rate	7.75	-375	25 June 07 (-25bp)	27 Aug 07 (-25bp)	7.50	7.00	6.50	6.50	6.50
Poland	7-day intervention rate	4.50	-75	27 Jun 07 (+25bp)	**29 Aug 07 (+25bp)**	4.75	5.00	5.25	5.50	6.00
Russia	Refinancing rate	10.00	-300	19 Jun 07 (-50bp)	1Q 08 (-50bp)	10.00	10.00	10.00	9.50	9.50
Slovak Republic	2-week repo rate	4.25	-75	27 Apr 07 (-25bp)	18 Dec 07 (+25bp)	4.25	4.50	4.50	4.50	4.50
South Africa	Repo rate	9.50	150	7 Jun 07 (+50bp)	16 Aug 07 (+50bp)	10.00	10.00	10.00	10.00	10.00
Switzerland	3-month Swiss Libor	2.50	200	14 Jun 07 (+25bp)	13 Sep 07 (+25bp)	2.75	3.00	3.00	3.00	3.00
Turkey	Overnight borrowing rate	17.50	-450	20 Jul 06 (+25bp)	16 Oct 07 (-25bp)	17.50	16.75	16.00	15.25	14.25
Asia/Pacific	GDP-weighted average	3.47	101			3.59	3.62	3.77	3.77	3.90
Australia	Cash rate	6.25	100	8 Nov 06 (+25bp)	5 Feb 08 (+25bp)	6.25	6.25	6.50	6.75	6.75
New Zealand	Cash rate	8.00	225	7 Jun 07 (+25bp)	**26 July 07 (+25bp)**	**8.25**	**8.25**	**8.25**	**8.25**	**8.25**
Japan	Overnight call rate	0.50	50	21 Feb 07 (+25bp)	23 Aug 07 (+25bp)	0.75	0.75	1.00	1.00	1.25
Hong Kong	Discount window base	6.75	425	30 Jun 06 (+25bp)	12 Dec 07 (+25bp)	6.75	7.00	7.50	7.50	7.50
China	1-year working capital	**6.84**	153	**20 July 07 (+27bp)**	**on hold**	6.84	6.84	6.84	6.84	6.84
Korea	Overnight call rate	4.75	100	12 Jul 07 (+25bp)	4Q 07 (+25bp)	4.75	5.00	5.00	5.00	5.00
Indonesia	BI rate	8.25	91	5 July 07 (-25bp)	7 Aug 07 (-25bp)	8.00	8.00	8.00	7.75	8.00
India	Repo rate	7.75	175	30 Mar 07 (+25bp)	on hold	7.75	7.75	7.75	7.75	7.75
Malaysia	Overnight policy rate	3.50	80	26 Apr 06 (+25bp)	on hold	3.50	3.50	3.50	3.50	3.50
Philippines	Reverse repo rate	6.00	-75	12 Jul 07 (-150bp)	on hold	6.00	6.00	6.00	6.00	6.00
Thailand	1-day repo rate	**3.25**	200	**18 July 07 (-25bp)**	29 Aug 07 (-25bp)	**3.00**	3.00	3.00	3.00	3.00
Taiwan	Official discount rate	3.125	175	21 Jun 07 (+25bp)	late Sep 07 (+12.5bp)	3.25	3.375	3.50	3.50	3.50

Bold denotes move this week and forecast changes

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Forecasts - Australia and New Zealand

Australia: economic projections *percentage change over previous period, seasonally adjusted annual rates, un*

				2006			2007				2008			
	2006	2007	2008	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Chain volume GDP	2.7	4.1	3.4	2.5	1.9	4.3	6.6	2.8	3.7	3.8	4.5	2.8	2.3	2.7
Private consumption	3.1	3.7	2.3	2.8	2.9	5.0	6.0	2.0	1.6	2.0	2.4	2.4	2.8	2.8
Construction investment	5.1	9.8	4.5	17.4	-4.5	7.4	25.7	3.8	8.5	3.2	4.3	4.4	3.0	6.4
Equipment investment	6.2	5.3	0.8	-8.7	-8.6	-2.9	24.9	4.3	6.4	4.3	0.0	0.0	-4.1	-8.1
Public investment	12.5	-5.5	5.2	2.9	22.4	53.3	-52.3	7.2	6.1	4.2	4.6	5.2	5.4	5.8
Government consumption	4.0	2.3	1.9	8.4	7.2	-4.4	3.3	2.8	2.4	2.0	2.0	1.6	1.6	1.6
Exports of goods & services	3.4	6.5	8.7	8.3	0.8	3.9	5.8	10.0	10.4	8.2	12.6	6.1	4.1	8.2
Imports of goods & services	7.6	9.0	3.7	11.8	-2.2	28.7	9.0	5.1	2.0	3.0	4.1	4.1	3.2	6.1
Contributions to GDP growth:														
Domestic final sales	4.3	4.3	2.7	5.9	1.4	6.8	5.4	2.8	3.5	2.5	2.6	2.6	2.3	2.5
Inventories	-0.6	0.6	0.0	-2.2	-0.1	2.7	2.1	-0.6	-1.2	0.4	0.4	0.0	0.0	0.0
Net trade	-1.0	-0.8	0.8	-1.0	0.6	-5.0	-1.0	0.6	1.4	0.8	1.4	0.2	0.0	0.2
GDP deflator (%oya)	4.7	3.6	2.5	4.6	5.1	4.5	4.8	4.0	3.0	2.6	2.5	2.5	2.5	2.5
Consumer prices (%oya)	3.5	2.2	3.2	4.0	3.9	3.3	2.4	1.7	2.0	3.2	3.7	3.3	3.0	2.6
Producer prices (%oya)	7.9	1.4	2.7	9.9	7.9	6.1	2.8	1.8	0.1	2.0	2.9	2.9	2.7	2.5
Trade balance (A$ bil, sa)	-13.3	-14.7	-14.2	-3.5	-2.0	-4.1	-4.1	-3.6	-3.4	-3.7	-3.1	-3.4	-3.8	-3.9
Current account (A$ bil, sa)	-54.9	-62.8	-65.2	-13.4	-12.8	-15.5	-15.4	-15.4	-15.4	-16.7	-15.6	-16.4	-16.8	-16.4
as % of GDP	-5.5	-5.8	-5.7	-5.4	-5.1	-6.0	-5.8	-5.7	-5.6	-6.0	-5.6	-5.7	-5.8	-5.6
3m eurodeposit rate (%)*	6.0	6.4	6.75	5.8	6.2	6.2	6.4	6.3	6.5	6.5	6.7	6.8	6.8	6.8
10-year bond yield (%)*	5.6	6.4	6.71	5.6	5.7	5.7	5.9	6.2	6.5	6.9	6.8	6.6	6.7	6.8
US$/A$*	0.75	0.81	0.77	0.74	0.77	0.77	0.80	0.83	0.82	0.80	0.80	0.78	0.76	0.74
Commonwealth budget (FY, A$ bil)	15.8	13.6	8.5											
as % of GDP	1.6	1.3	0.7											
Unemployment rate	4.9	4.6	5.2	5.0	4.8	4.6	4.6	4.2	4.6	4.8	5.0	5.1	5.3	5.5
Industrial production	-0.6	0.9	0.0	0.2	7.3	8.3	-2.1	-2.0	-4.0	-1.0	1.0	3.0	4.0	0.0

*All financial variables are period averages

New Zealand: economic projections *percentage change over previous period, seasonally adjusted annual rates, unless stated*

				2006			2007				2008			
	2006	2007	2008	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real GDP (1995-96 prices)	1.5	2.7	2.3	1.6	1.0	3.3	4.2	2.0	2.3	2.1	2.3	3.2	1.8	2.0
Private consumption	2.3	4.0	1.2	-0.3	1.6	5.6	8.8	2.1	1.4	1.1	1.1	1.2	1.3	1.2
Fixed Investment	-2.4	4.0	0.4	-19.8	5.1	4.2	17.1	-0.2	0.1	0.4	0.3	0.5	0.6	0.7
Residential construction	-2.7	1.7	0.8	-21.3	16.8	8.2	-1.3	0.0	0.8	1.0	0.7	0.9	0.8	0.9
Other fixed investment	-2.3	4.6	0.2	-19.4	2	3.2	22.6	-0.2	-0.1	0.2	0.2	0.4	0.5	0.6
Inventory change (NZ$ bil, saar)	0.0	-0.1	0.1	-0.1	-0.2	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1
Government spending	4.8	4.2	4.5	7.4	4.0	1.0	3.6	7.4	3.4	5.2	3.5	7.6	1.6	2.8
Exports of goods & services	1.9	4.0	4.4	11.3	11.0	-9.2	8.3	5.0	5.2	4.0	4.4	4.2	4.2	4.0
Imports of goods & services	-2.5	6.5	2.9	-5.0	2.7	6.5	18.4	2.1	2.4	2.6	3.0	3.0	3.6	3.6
Contributions to GDP growth:														
Domestic final sales	0.7	3.9	1.8	-0.8	-0.4	4.5	10.8	1.0	1.6	1.6	1.6	2.6	1.7	1.9
Inventories	-0.8	-0.1	0.2	-2.9	-1.1	4.3	-2.5	0.2	-0.1	0.1	0.4	0.3	0.1	0.1
Net trade	1.6	-1.1	0.3	5.4	2.5	-5.4	-3.7	0.8	0.8	0.3	0.3	0.2	0.0	0.0
GDP deflator (%oya)	2.4	2.8	2.1	2.0	2.7	2.9	3.2	3.2	2.5	2.4	2.1	2.1	2.1	2.1
Consumer prices	3.4	1.9	2.5	6.2	2.8	-0.8	2.0	2.7	1.9	0.8	3.2	4.0	2.6	0.7
%oya	3.4	1.9	2.5	4.0	3.5	2.7	2.5	1.7	1.5	1.9	2.1	2.4	2.6	2.6
Trade balance (NZ$ bil, sa)	-3.2	-4.5	-4.9	-0.7	-0.7	-0.8	-0.9	-1.2	-1.2	-1.2	-1.2	-1.2	-1.2	-1.2
Current account (NZ$ bil, sa)	-14.4	-14.4	-14.3	-3.5	-3.2	-3.6	-3.6	-3.6	-3.6	-3.5	-3.5	-3.6	-3.6	-3.6
as % of GDP	-9.2	-8.7	-8.3	-9.2	-8.1	-9.0	-8.9	-8.8	-8.7	-8.4	-8.3	-8.3	-8.3	-8.2
Yield on 90-day bank bill (%)*	7.5	8.2	8.2	7.5	7.5	7.7	7.8	8.2	8.4	8.3	8.3	8.3	8.3	8.1
10-year bond yield (%)*	5.8	6.3	6.2	5.8	5.8	5.8	6.0	6.4	6.4	6.4	6.5	6.3	6.3	6.2
US$/NZ$*	0.65	0.71	0.65	0.62	0.64	0.67	0.70	0.74	0.73	0.69	0.67	0.65	0.64	0.63
Commonwealth budget (NZ$ bil)	6.5	6.4	5.7											
as % of GDP	4.2	3.9	3.3											
Unemployment rate	3.8	4.0	4.4	3.6	3.8	3.7	3.8	3.9	4.0	4.1	4.2	4.3	4.4	4.5

*All financial variables are period averages

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Australasian economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
23 Jul **Australia:** PPI (11:30am) 2Q 0.6 %q/q	**24 Jul**	**25 Jul** **Australia:** CPI (11:30am) 2Q 0.9 %q/q	**26 Jul**	**27 Jul** **New Zealand:** Trade balance (10:45am) Jun
30 Jul **Australia:** NAB business survey (11:30am) 2Q **New Zealand:** Building permits (10:45am) Jun	**31 Jul** **Australia:** Pvt sector credit (11:30am) Jun Building approvals (11:30am) Jun **New Zealand:** NBNZ Bus. Confidence (15:00) Jul	**1 Aug** **Australia:** Trade balance (11:30am) Jun Retail sales (11:30am) Jun	**2 Aug**	**3 Aug**
6 Aug **Australia:** ANZ job ads (11:30am) Jul **New Zealand:** Labor cost all wages (10:45am) 2Q *Holiday Australia*	**7 Aug**	**8 Aug** **Australia:** RBA Cash target (09:30am) Aug House price index (11:30am) 2Q Housing finance (11:30am) Jun Fx reserves (04:30pm) Jul	**9 Aug** **Australia:** Unemp rate (11:30am) Jul **New Zealand:** Unemployment rate (10:45am) 2Q	**10 Aug**
13 Aug **Australia:** RBA Quarterly monetary policy statement (11:30am)	**14 Aug** **Australia:** NAB business survey (11:30am) Jul **New Zealand:** Retail sales (10:45am) Jun	**15 Aug** **Australia:** Westpac consumer confidence (10:30am) Aug Wage cost index (11:30am) 2Q **New Zealand:** PPI (10:45am) 2Q Retail sales (01:00pm) Jun	**16 Aug** **Australia:** Consumer inflation expectation (10:30am) Aug Avg weekly wages (11:30am) May	**17 Aug**

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Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
23 - 27 July	**23 July**	**24 July**	**25 July**	**26 July**	**27 July**
	Germany • CPI 6 states and prelim (Jul) **Hungary** • NBH meeting	**Euro Area** • Industrial orders (May) • PMI flash (Jul) **Japan** • BoJ bank officers survey (2Q) • Fukui speech **Malaysia** • BNM meeting **Taiwan** • Export orders (Jun) • IP (Jun) **Business surveys** • Belgium (Jul) • Netherlands (Jul)	**Australia** • CPI (2Q) **Japan** • Trade balance (Jun) **Korea** • GDP (2Q) **Poland** • NBP meeting **United States** • Existing homes (Jun) • Fed Beige book **Business surveys** • France (Jul) • Italy (Jul)	**Canada** • Payrolls (May) **Euro Area** • M3 (Jun) **Germany** • IFO bus survey (Jul) **Japan** • CSPI (Jun) **United States** • Durable goods (Jun) • New home sales (Jun) **Central bank meetings** • Czech Rep • New Zealand	**Colombia** • BanRep meeting **Germany** • GFK consumer conf (Aug) **Japan** • Nationwide core CPI (Jun) • Retail sales (Jun) **Mexico** • Banxico meeting **United States** • Consumer sentiment (Jul) • Real GDP (2Q advance)
30 July- 3 Aug	**30 July**	**31 July**	**1 Aug**	**2 Aug**	**3 Aug**
	France • Unemployment (Jun) **Japan** • IP (Jun prelim) **Korea** • IP (Jun)	**Euro Area** • EC bus survey (Jul) • HICP flash (Jul) • Unemployment (Jun) **Japan** • Household spend (Jun) • Jobs and wages (Jun) • PMI mfg (Jul) • Shoko Chukin small bus sentiment (Jul) • Unemployment (Jun) **United States** • Chicago bus sur (Jul) • Construct spending (Jun) • Consumer conf (Jul) • ECI (2Q) • Personal income (Jun) **Central bank meetings** • India, Slovak Rep	**China** • PMI mfg (Jul) **Euro Area** • PMI mfg (Jul) **Korea** • CPI (Jul) **Singapore** • PMI mfg (Jul) **United Kingdom** • Mfg PMI (Jul) **United States** • ISM mfg (Jul) • Light vehicle sales (Jul) • Pending home sales (Jun)	**Euro Area** • ECB meeting **Peru** • BCRP meeting **United Kingdom** • BoE meeting **Sweden** • GDP flash (2Q) **United States** • Factory orders (Jun)	**Canada** • Ivey PMI (Jul) **Euro Area** • PMI services (Jul) • Retail sales (Jun) **United Kingdom** • PMI services (Jul) **United States** • Employment report (Jul) • ISM nonmfg (Jul)