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Australia and New Zealand - Weekly Prospects

Summary

- There was little economic data released in **Australia** last week, although the RBA monetary policy minutes from the May board meeting provided market pundits with plenty to chew on. It now seems more likely that the rapidly rising terms of trade and recently delivered income tax cuts may prevent the further significant easing in domestic demand that RBA officials expect to help curb inflation. This raises the risk that the RBA may yet have to raise the cash rate again. Other data showed an improvement in consumer confidence in May following the Federal Budget. This week, credit growth should have slowed in April and capital spending intentions probably will be scaled back slightly owing mainly to credit market problems and diminished confidence in the resilience of the global economy.

- In **New Zealand,** the calendar was also light on key data last week; the Federal Budget was the highlight. The unexpectedly large income tax cuts and increased government spending will likely prevent the RBNZ from easing monetary policy in coming months. Today, data showed the trade balance in deficit in April for the second straight month as imports were bolstered by one-off items. Later in the week, data should show business confidence remained subdued in May.

- The latest indicators, on balance, reinforce our "less growth, less fear" outlook theme. A broad-based slowing in **global growth** appears to be taking hold following a surprisingly resilient growth outcome during 1Q08. The growth of global manufacturing output is stalling as we move toward midyear. US and Japanese output is now contracting while EM production gains are downshifting. Meanwhile, May business surveys reinforce the view that the Euro area economy is moving into a phase of sub-par growth, even as a pronounced rotation in growth is under way toward Germany. At the same time, the broadening out of the growth slowdown is not producing intensified weakness in the US. The message from high-frequency indicators is that the US economy continues to limp slowly forward as business cutbacks remain mild, and as financial stress gradually abates. Combined with the beneficial effects of the tax rebate checks now in the pipeline, the risk of a protracted recession has declined.

- As the risk of a slide in the **US economy** declines, inflation is becoming a more pressing concern for much of the globe. Global consumer prices rose 4% in the 12 months through April, the most rapid rate of increase since 1999. Emerging market inflation has moved up far more dramatically—by more than three percentage points since early 2007, to 7.6%oya. While there are good reasons to look at the spike in headline inflation as a relative price movement reflecting food and energy price gains, there are increasing signs also of passthrough from rising commodity costs to other prices.

This week's highlight

The Aussie capex survey on Thursday. Firms probably wil trim their previously upbeat business investment plans (up 25% for 2008-09), owing to increased anxiety about the outlook for the global economy and funding difficulties.

Contents

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Data and event previews - Australia and New Zealand

Date [(a)]	Data/event	Forecast			Comment
		JPMorgan	Consensus	*Previous*	
Tuesday, 27 May (11:00am)	**NBNZ business confidence (May, % balance)**	**-56.0**	na	*-54.8*	Kiwi business confidence probably will worsen in May, with 56% of respondents likely to expect business conditions to deteriorate over the coming year. Corporate profitability continues to dwindle amid soaring petrol prices and tighter credit conditions.
Tuesday, 27 May (12:00pm)	**RBNZ inflation expectations (2Q, %q/q)**	**na**	na	*2.7*	na
Wednesday, 28 May (10:30am)	**Aust. WMI leading index (Mar, %m/m)**	**na**	na	*0.0*	na
Wednesday, 28 May (11:00am)	**Aust. DEWR skilled vacancy index (May, %m/m)**	**na**	na	*-0.8*	na
Wednesday, 28 May (11:30am)	**Aust. construction work done (1Q, %q/q)**	**na**	2.3	*-1.0*	na
Thursday, 29 May (11:30am)	**Aust. private new capital expenditure (1Q, %q/q)**	**2.5**	3.0	*5.1*	Investment spending probably rose modestly in 1Q. Firms likely will trim their investment plans slightly, however, owing to renewed doubts about global growth and funding difficulties. We look for a A$86 billion print for spending intentions for 2007-08, and a A$79.75 billion estimate for 2008-09, which will signal an 18% rise over 2007-08.
Friday, 30 May (08:45am)	**NZ building consents (Apr, %m/m)**	**na**	na	*-9.1*	na
Friday, 30 May (11:30am)	**Aust. private sector credit (Apr, %m/m)**	**0.7**	0.8	*0.8*	Growth in credit probably slowed further in April, following the RBA's rate hikes in February and March and the commercial bank's rate hikes independent of the cash rate. Personal credit probably contracted again, with growth in housing credit slowing to 0.7% and business credit rising 0.9%.

(a) Australian Eastern Standard Time.

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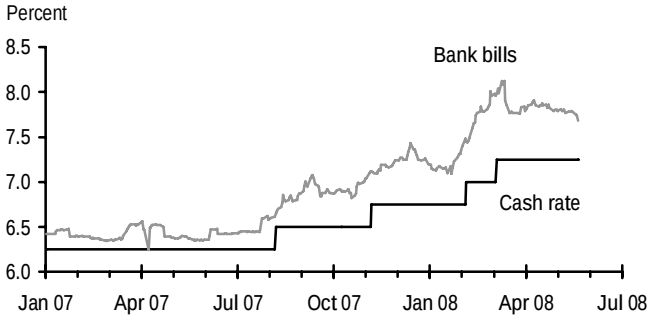
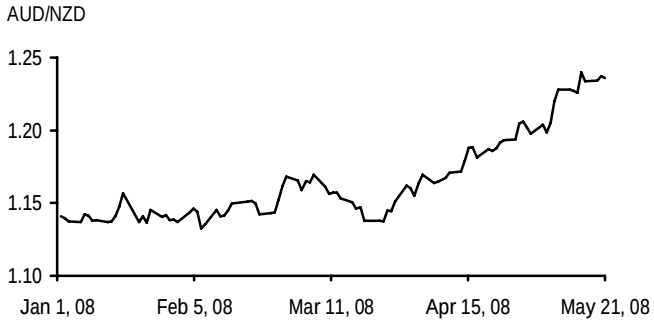
Feature charts

Australia: cash rate target and 90-day bank bill rate



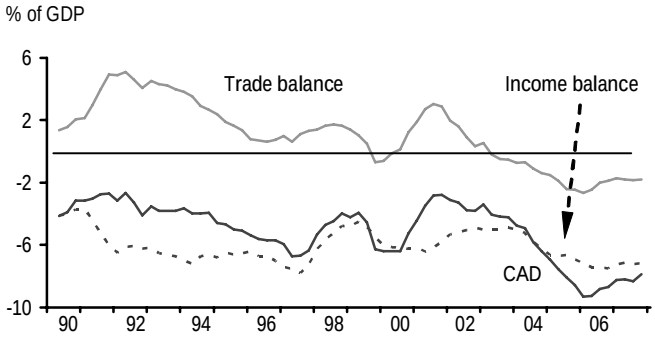
Funding pressures in Australia appear to have eased further, with the 90-day bank bill rate still converging towards the RBA's cash rate target. In fact, the 90-day bank bill rate has dropped to the lowest level since February. The 40-odd basis point spread over cash, though, remains more than double the spread seen before the credit crunch began last year.

Australia dollar retains support against NZD



The Australian dollar has appreciated 8% against NZD this year. The RBA's back-to-back hikes to interest rates in February and March and recent, growing speculation that further tightening may be warranted have helped push the aussie above NZ$1.24. The high-yielding Australian unit ventured above 96 US cents this week, and is up 10% against the greenback this year.

New Zealand: current account



A key risk to New Zealand's economic outlook is the burgeoning current account gap. The current account deficit represented 7.9% of GDP in 4Q. Any worsening of the fiscal position, coupled with increased risk aversion and growing speculation that the RBNZ will soon cut interest rates, could send the Kiwi dollar into a tailspin. This would add upside risk to inflation which, according to our forecast, will remain above the RBNZ's 1-3% target range in 2008 and 2009.

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Economic Research note

Aussie Budget not as inflation-fighting as government claims

- **Australia's new Treasurer sold his first Budget as a key tool in the fight against inflation**
- **While it is disinflationary in the medium term, policy changes will add to inflation in the near term**
- **The Budget slugged high income earners to fund tax cuts for low and middle income earners**

Australian Treasurer Wayne Swan recently delivered his maiden Budget, the first by a Labor government for 13 years. When a Labor treasurer last delivered a Budget, Ben Crenshaw won the Masters and Pete Sampras beat Boris Becker in the final at Wimbledon. The Budget delivered broadly what was expected, a mammoth surplus, the biggest for nearly a decade as a share of GDP, thanks to the mining boom and the associated boost to company tax receipts.

The Budget delivered the promised personal income tax cuts for low and middle income earners, means testing of middle class welfare, and new spending on health, education, water, and infrastructure. This is aimed at improving productivity and the country's creaky infrastructure. The government announced targeted cuts to spending, which became unnecessarily bloated under the previous Coalition government. The Treasurer hinted pre-Budget that there would be few surprises and he delivered. If there were rabbits to be released, Swan kept them in his hat. Treasurers normally hold back some good news to generate favourable post-Budget press coverage, but not this time.

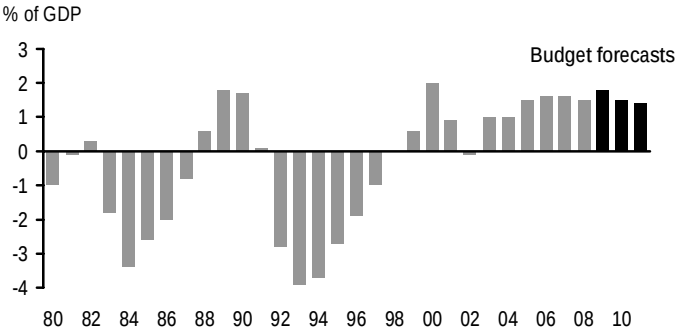
The government's failure to cut more deeply into bloated spending and defer the tax cuts, however, leaves open the possibility that the RBA may yet pull the trigger again and raise the cash rate. If necessary, RBA officials will finish the job the government has left half-completed. Indeed, the Budget anticipates a contraction in the budget surplus in the three years to 2011-12, meaning that the government intends to loosen fiscal policy slightly, relative to 2008-09.

Budget sold as an "inflation-fighter"

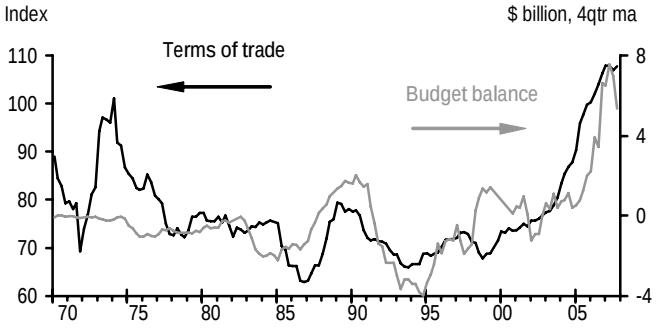
This budget had three primary objectives beneath the oft-repeated, overarching aim of using fiscal policy to quell domestic inflation pressure:

- To deliver on Labor's election promises, including the personal tax relief and targeted spending in key, politically sensitive portfolios like health and education;

Commonwealth budget position



Terms of trade and budget balance



- To reward Labor's treasured "working families," who delivered last November's Federal election victory; and
- To establish Labor's credentials as prudent managers of the economy. Traditionally, economic management has been the badge worn by the Coalition, not by Labor.

The Budget achieved these objectives, but the key question of whether the Budget is successful in capping inflation pressure remains unresolved. Granting massive personal tax relief behind a veneer of spending austerity is a risky strategy, particularly with the Reserve Bank forecasting that inflation will stay above target for the next two years. The Treasurer has admitted that the budget is "mildly disinflationary," which sits uncomfortably with the government's earlier declaration of war on inflation.

Robin Hood hits high-earners

The Treasurer unabashedly robbed from the "rich"—those earning above A$150,000 per year—to give to the "poor" in this Budget. The winners are lower income earners and Labor's ubiquitous "working families"—those on average incomes, for example, received personal income tax relief worth A$50 per month. Others received beneficial changes to the Medicare public health arrangements, which now exclude many households from having to pay the tax surcharge, mea-

sures to improve housing affordability, and increased spending on public education and health.

The clear losers are higher income earners, who forfeit much of their current welfare payments via new means tests, had their income tax cuts promised by the previous Coalition government deferred, and have to pay more for their luxury cars. The rise in the luxury car tax from 25% to 33% means car prices will rise from 1 July, while the changes to the health care arrangements will cause thousands of people to bail out of private health insurance. Industry estimates suggest a likely exodus of up to one million health fund members. These two measures combined could add 0.3% points to inflation in 2008. In the medium term, however, the extra spending on infrastructure should help to alleviate bottlenecks, and some of the public spending cuts will quell growth in domestic demand. This should help to cap the upside for inflation, which already is certain to track well above the RBA's target zone this year.

Surplus now a massive 1.8% of GDP

Swan produced a mammoth surplus of A$21.7 billion (1.8% of GDP), slightly above market expectations. Fortunately for the Treasurer, a surge in company tax receipts on the back of the terms of trade boom helped close the gap left by the tax cuts. The increase in the Budget surplus relative to the 2007-08 outturn of A$16.8 billion (1.5% of GDP) means the Budget is contractionary, as it should be if the government is serious about confronting Australia's chronic inflation problem. In fact, the 1.8% of GDP surplus is the largest since 1999-00, so the government is doing some hard yards in attempting to slow economic growth and cap the upside for inflation.

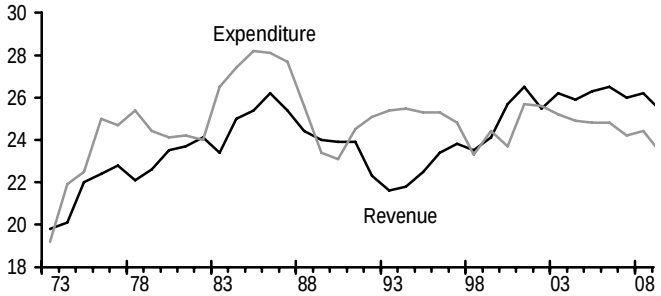
That said, the Budget could, and should, have been more contractionary. Deferring the tax cuts, for example, or legislating for them to be paid into pension funds, could have pushed the Budget surplus closer to A$30 billion. This would have helped take even more of the froth out of discretionary parts of the economy and put downward pressure on inflation. Instead, for political reasons—it would have been political suicide for the government to cancel the tax cuts—the government pulled its best punch.

Slowing economy a difficult backdrop

With growth in the domestic economy slowing, growth in some of the world's largest economies weakening, energy prices at record highs, interest rates having risen sharply, and inflation soaring, the economic backdrop to this budget was the most difficult for some time. Indeed, the Treasurer faced

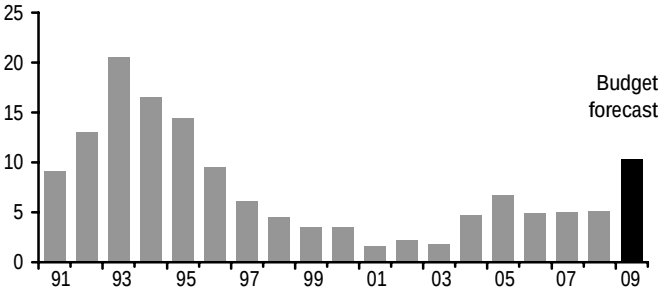
Government revenue and expenditure

% of GDP



Gross federal government bond issuance

A$ billion, year ended June



the difficult task of appearing to take the worsening inflation problem seriously, while supporting "working families," many of whom are suffering from soaring food and petrol prices, and high interest rates.

The Treasury expects economic growth of 2.75% in 2008-09, down from the 3.5% forecast before the election, and inflation averaging 4.0% in 2008-09, well above the RBA's 2-3% target range. The Treasury's longer term inflation forecasts are below the RBA's; the government could not deliver a so-called inflation-fighting Budget while simultaneously forecasting inflation well above target for an extended period. The inflation forecasts look optimistic given the high base from 1Q and the likelihood that food and energy prices will remain elevated for an extended period.

Bond issuance to rise to A$10.3 billion

The Budget announced that bond issuance would be A$5.3 billion in 2008-09, although the government subsequently announced additional issuance of up to $25 billion over five years, including an extra $5 billion in 2008-09. This will be sufficient to ensure the proper functioning of the bond and futures markets. Bond issuance has been averaging A$5 billion per year since 2003.

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Economic Research note

Dark clouds forming over New Zealand's economy

- **RBNZ to embark on monetary easing cycle in 4Q**
- **Growth will slow as inflation remains above target**
- **GDP growth to slump to 1.4% in 2008 before recovering in 2009**

Economic momentum in New Zealand will slow significantly in 2008, owing mainly to weaker private consumption growth and a contraction in residential construction. Our forecast calls for GDP growth to dive from 3.1% in 2007 to a subpar 1.4% in 2008, with a contraction in economic growth anticipated for 2Q. The RBNZ probably will delay easing monetary policy until October; RBNZ officials will be searching for evidence of whether the recent weakness in employment and consumer spending will be sustained.

Upside pressure on inflation persists

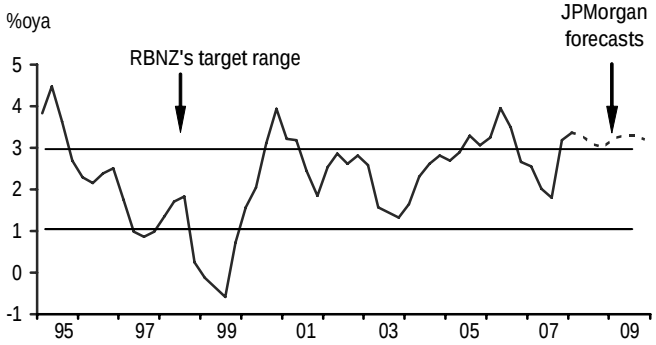
Also, upside inflation risks will prevent an interest rate cut before 4Q. Headline inflation rose to 3.4%oya in 1Q, hovering above the RBNZ's 1-3% target range for the second straight quarter. More importantly, nontradables inflation—generated domestically and not influenced by exchange rate fluctuations—held at 3.5%, even though domestic demand recently has slowed significantly.

There still appear to be price pressures building in the pipeline. Producer prices spiked in 1Q amid soaring crude oil costs, rising dairy prices, and increased demand for electricity. Prices paid by power companies surged 42%q/q as low hydro lake levels owing to the drought bolstered wholesale electricity costs. Both nontradable and producer price inflation will have to moderate before the RBNZ considers embarking on an easing cycle.

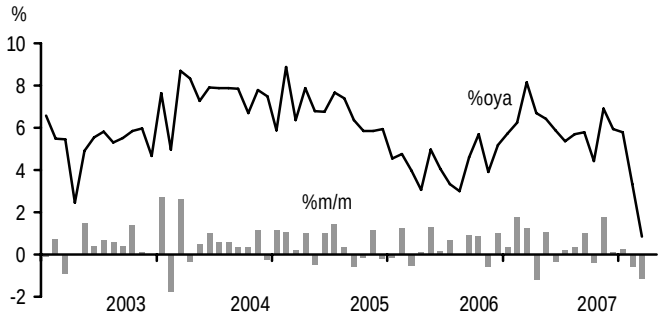
First cut to OCR in October

The RBNZ has left the official cash rate (OCR) at a record high of 8.25% since July 2007. According to our forecast, the RBNZ will cut the key rate 25bp in October, and again in December and 1Q next year. Our previous forecast that a rate cut would be delayed until 2009 was based mainly on the assumption that inflation would track above the RBNZ's target range for an extended period. But, signs that the economy will slow to a standstill midyear mean that the RBNZ now will be more inclined to tolerate what will be uncomfortably high CPI readings in coming quarters.

CPI growth to remain elevated



Downside risks for retail sales



Also, the government's decision to delay the introduction of the emissions trading scheme (ETS) will take some upside pressure off inflation. The government recently announced that the introduction of the ETS would be postponed for two years, protecting consumers against higher costs for gasoline and fuel until 2011. Estimates suggest that the ETS would add up to 8 cents a litre to the price of petrol and fuel, which already are elevated and eating away at household budgets.

Private consumption growth tanking

The recent change in our rate call emerged amid a slew of weak economic data. In particular, labour market statistics indicated that labour market conditions loosened in 1Q, with employment contracting and wage growth easing unexpectedly. Being lagging indicators, these developments provided reason for concern about the health of the economy, especially since business confidence has recently plunged. Corporate profitability has dwindled amid soaring petrol prices and tighter credit conditions, meaning that firms will become increasingly reluctant to hire workers, sending the jobless rate higher throughout 2008.

Household consumption will be dampened further throughout 2008. Consumer spending already is suffering, with retail sales volumes unexpectedly slumping 1.2%q/q in 1Q—the biggest quarterly drop since March 1997—under the weight of record

high interest rates, rising energy costs, a rapidly deteriorating housing market, and drought conditions in key dairy producing regions. There is additional downside risk now that a number of domestic banks have begun passing on higher funding costs resulting from credit market tightening. Domestic lending rates have increased even though the OCR has remained unchanged since July.

That said, the forecast 50bp cut to the OCR in 4Q, and the personal income tax relief recently announced in the May 22 Budget should cushion the downside for private consumption. The income tax cuts delivered by Finance Minister Michael Cullen last week were larger than expected, and will total NZ$10.6 billion over the next four years. Any further deterioration in the nation's fiscal position, however, may lead to credit rating downgrades, and significant tax cuts and increased spending run the risk that the RBNZ will not be able to start lowering interest rates this year.

Residential construction another key drag

The worst declines in employment in the March quarter were in industries related to the housing sector, conditions which have deteriorated sharply in recent months. House prices fell 1.2% in April, the medium number of days to sell a home rose from 40 to 44, and house sales are now down more than 45%oya—the lowest since 1991.

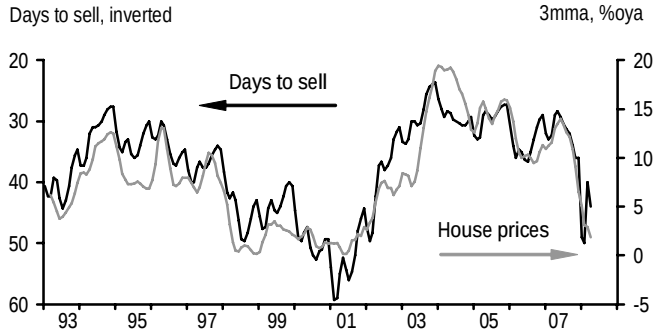
The house price boom in recent years has been fuelled by excessive household borrowing, with many households clearly taking on too much debt. Household debt as a percentage of nominal disposable income rose to 164% in the December quarter. Confidence in New Zealand's housing market now is at its lowest in 12 years, heightening the risk that house prices will fall more than the 5% we and the RNBZ forecast for 2008.

Recession should be avoided

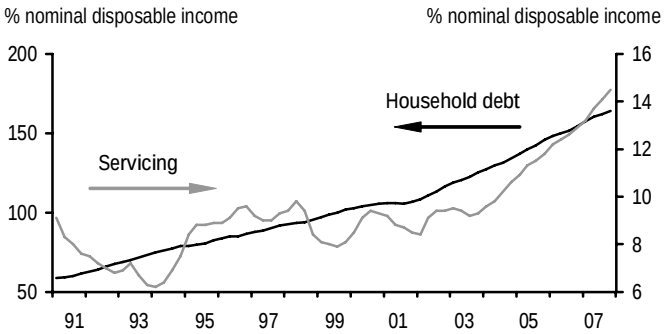
A recession in 2008 should be avoided, but the risks are skewed to the downside. Weaker NZD will help boost exports, which account for a significant 30% of the economy. Our forecast calls for the NZD—which recently sank to a four-month low—to be at $0.78 by year end, bearing in mind that NZD will retain upside support from higher commodity prices.

But the impact of the drought on exports will remain a drag. The dairy industry, the nation's largest exporter, has announced that it faces a NZ$500 million cut to its export income from production losses because of the drought. Furthermore, an unexpectedly sharp slowdown in global demand remains a key risk to the predicted export-led growth rotation away from

Housing market deteriorating rapidly



Household claims and debt servicing rising



households in 2008; this may develop if the credit crisis triggers a deeper global slowdown.

The RBNZ has acknowledged that if credit conditions tighten significantly, the economic slowdown will be exacerbated, putting additional financial pressure on households already knee-deep in debt. The RBNZ recently announced, new liquidity measures, similar to those adopted by other central banks, aimed at ensuring sufficient liquidity in the banking system in the event of further global financial market volatility.

One other area for concern is the burgeoning current account gap. Any further deterioration of the current account deficit (now 8% of GDP), coupled with increased risk aversion and growing speculation that the RBNZ will soon start cutting interest rates, could send the NZD into a tailspin, adding upside risk to inflation.

Indeed, downside risks to growth have grown in recent months, but building inflation pressures mean that the OCR will remain at its current level until later in the year. Increased government spending on health, education and infrastructure, and the deliverance of personal income tax cuts should limit the extent of the economic slowdown, however, meaning that a recession should be avoided.

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Australia

- **RBA minutes indicate retention of tightening bias**
- **Aussie consumer sentiment improved in May**
- **Business investment survey the highlight in a quiet week**

There was little economic data in Australia last week, although the RBA monetary policy minutes provided market pundits with plenty to chew on. It now seems more likely that the rapidly rising terms of trade and recently delivered income tax cuts may prevent the further significant easing in domestic demand that RBA officials expect to help curb inflation. Other data showed an improvement in consumer confidence in May following the recent Federal Budget. In the week ahead, credit growth should have slowed in April and capital spending intentions probably will be scaled back slightly owing mainly to credit market problems and diminished confidence in the resilience of the global economy.

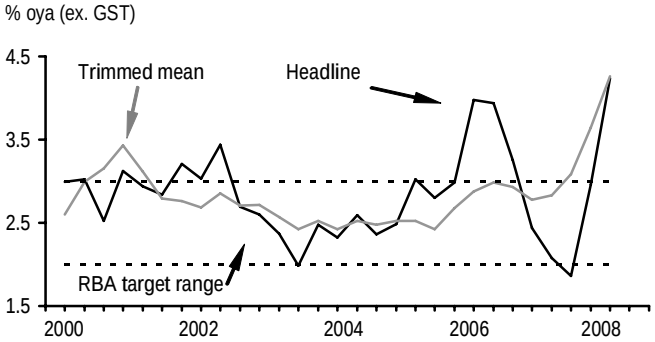
RBA leaves door open to tightening

The RBA last Tuesday released the minutes of the monetary policy meeting on May 6, when the Board decided to leave the cash rate steady at 7.25% for the second straight month. This decision was despite the 1Q CPI release in late April showing headline and core inflation at 4.2% and 4.0%, respectively, putting both measures well above the RBA's 2-3% target range. The fact that the RBA looked through such elevated inflation readings and concentrated instead on evidence of weakening domestic growth and tighter credit conditions was an important break from convention. Previously, any rise in core inflation, let alone an alarming spike, would have triggered a rate hike shortly after.

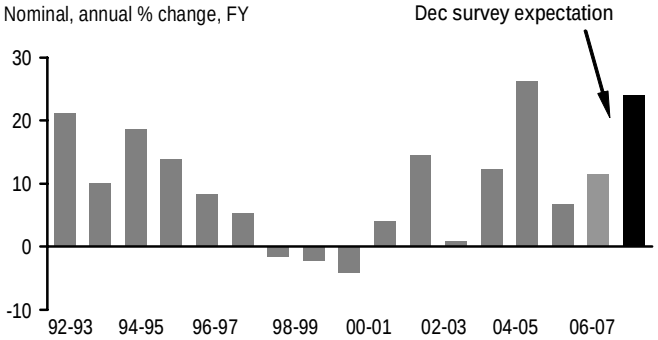
The RBA is on hold given heightened uncertainty, but the dominant risk is that the RBA may need to raise the cash rate again. Indeed, the minutes showed that Board members questioned in May whether policy was "sufficiently restrictive" to secure low inflation, and spent considerable time discussing the case for a further rise in the cash rate. It seems that the merits of rate cuts were not discussed. The considerable uncertainty over the policy outlook, though, means officials believe they need more time to assess the likely trajectories of growth and inflation.

Board members noted that inflation had spiked up to uncomfortably high levels and was likely to stay elevated for an extended period. Members took account of the fact that some of the recent rise in inflation stemmed from offshore influences, like high energy prices. Furthermore, high AUD had helped to cap the upside for some prices. That said, members also noted

Australia: headline and core CPI



Australia: business investment



that inflation pressures were broadly based, and that elevated inflation readings may become entrenched in expectations for prices and wages.

On the real economy, Board members noted the weakness in retail spending, low consumer and business confidence, and softening demand for home loans, which partly are responses to the tightening in credit conditions. On the flipside, however, the Board minutes reveal that a considerable amount of time was spent discussing the benefits of the high and rising terms of trade, which RBA officials believe will be an important source of support for domestic income. The RBA's working assumption is that the terms of trade will rise 20% in 2008—our more upbeat, although still conservative, forecast is for a 28% rise. Also, employment growth remains robust.

The minutes were consistent with recent RBA commentary suggesting that officials are prepared to tolerate elevated inflation, given the unusually heightened level of uncertainty about the outlook for the domestic and offshore economies, and the improved, but still problematic, conditions in global credit markets. The RBA forecasts core inflation above the 2-3% target range until 2010. The fact that policy was unchanged in early May indicates that officials believe the recent deterioration in the indicators of domestic demand is material, and will likely be sustained.

That said, the RBA also seems content to tolerate weaker domestic demand in order for inflation to begin its long journey back to the RBA's comfort zone. Indeed, the RBA's public commentary has indicated that officials want to see a "significant" slowing in domestic demand in order for inflation to return to the target band. It would be counterintuitive for Board members to cut interest rates to cushion the downside for the economy when a sustained slowdown in demand is the Board's primary objective in curbing inflation. Rate cuts any time soon, therefore, are very unlikely.

Indeed, on balance, the RBA is on hold while officials navigate between weakening domestic demand and elevated inflation. The income tax cuts recently delivered in the Budget, though, and the soaring terms of trade, could trigger a rebound in domestic demand growth in the second half of this year. This would mean that inflation's journey back to the target range would last longer than expected and could be enough to trigger further policy tightening.

Capital spending intentions likely to fall

The first-quarter Australian business investment survey is released on Thursday. In the last survey, firms anticipated a 25% rise in business investment spending in the year ended June 2009. This represented a significant upgrade on spending plans from the previous survey. The upgrade was triggered by soaring commodity prices and optimism that growth in the global economy was not as soggy as some suggested.

Firms probably will downgrade their investment plans in this week's survey. There has been an accumulation of evidence suggesting that growth in the global economy is likely to be weaker than previously thought. This is despite further evidence that growth in China—a major market for Australian commodity exporters—was holding up. Also, the tightening in credit markets probably means some firms are finding it more difficult to raise financing, which means firms may postpone some of their investment plans.

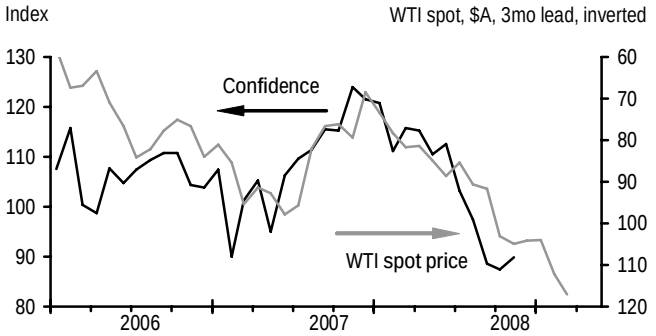
Credit growth to remain subdued

The RBA's private sector credit aggregates likely grew 0.7%m/m in April, slowing from 0.8% in March. The annual rate of credit growth will ease from 14.9% to 14.4%, slowing in response to the four RBA policy tightenings since August, and the disproportionate rises in domestic banks' variable mortgage rates.

Borrowing by businesses will have remained subdued in April, growing 0.9%m/m, the same rate as in the previous month. This lending was likely, however, used to fund investment in additional capacity, particularly in the mining sector. Housing and personal credit will have remained subdued, given the significant tightening in credit conditions. Household credit will have grown just 0.7%m/m in April, slowing from 0.8% to mark the slowest rate of growth since August 2007. Personal credit growth probably contracted 0.1%m/m, after falling 0.2% in March.

Australia: private sector credit aggregates

Australia: consumer sentiment and gasoline prices



Consumers more upbeat after Budget

Consumer confidence in May increased for the first time this year, rising 2.7%m/m (JPMorgan +3.0%) after falling 1.3% in April. The Westpac-Melbourne Institute's consumer sentiment index rose to 89.8 from 87.4, but is still down 26% from the May 2007 peak.

The index reading remains well below 100, meaning the majority of those surveyed are pessimistic, owing to myriad factors: 12-year high interest rates, ongoing global growth concerns, financial market volatility, and rising petrol prices, to name a few. Also, the decision among several domestic banks to raise their standard variable loan rates by more than, and outside of, the recent rises in the official cash rate continues to weigh heavily on sentiment.

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The improvement in sentiment emerged in the wake of the RBA's decision to leave interest rates steady earlier in the month and the recent Federal Budget. The improvement in confidence stemmed primarily from low and middle income earners, who benefited the most from the personal income tax cuts delivered in the Budget. Sentiment improved 12.3% among those households with a combined annual income of between A$40,000 and A$60,000.

Sentiment toward household finances continued to deteriorate, however, probably owing to growing speculation that the RBA may need to hike interest rates again this year. The two components of the confidence index to fall were related to family finances, with sentiment toward family finances a year ago and a year ahead falling 2.8% and 10.9%, respectively. Confidence improved in all other components of the index.

Data releases and forecasts

Week of May 26 - 30

Wed May 28 11:30am — **Construction work done**
Seasonally adjusted

	2Q07	3Q07	4Q07	1Q08
(%q/q)	-1.9	3.5	-2.0	__
(%oya)	2.9	9.5	2.9	__

Wed May 28 10:30am — **WMI leading index**
Seasonally adjusted

	Dec	Jan	Feb	Mar
(%m/m)	-0.2	-0.1	0.0	__

Thu May 29 11:30am — **Private new capital expenditure**
Seasonally adjusted

	2Q07	3Q07	4Q07	1Q08
(%q/q)	7.0	-6.2	5.1	2.5
(%oya)	11.9	9.0	15.3	8.1

Investment spending probably rose modestly in 1Q. Firms likely will trim their investment plans slightly, however, owing to renewed doubts about global growth and funding difficulties. We look for a A$86 billion print for spending intentions for 2007-08, and a A$79.75 billion estimate for 2008-09, which will signal an 18% rise over 2007-08.

Fri May 30 11:30am — **Private-sector credit**
Seasonally adjusted

	Nov	Dec	Jan	Feb
(%m/m)	1.0	0.6	0.8	0.7
(%oya)	16.2	15.4	14.9	14.4

Review of past week's data

WMI consumer sentiment index
100=neutral, seasonally adjusted

	Mar		Apr		May	
(%m/m)	-9.0		-1.4		~~3.0~~	*2.7*

Sales of new motor vehicles
Units, seasonally adjusted

	Feb		Mar		Apr	
(%m/m)	~~-2.4~~	*-2.5*	~~1.0~~	*0.7*	__	*-0.8*
(%oya)	3.0		~~3.7~~	*3.5*	__	*3.5*

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New Zealand

- **NZ Budget reduces chance of RBNZ rate cut this year**
- **Trade accounts to remain in deficit in April**
- **Business confidence to stay weak**

In New Zealand, the calendar was also light on key data last week; the Federal Budget was the highlight. The unexpectedly large income tax cuts and increased government spending will likely prevent the RBNZ from easing monetary policy in coming months. In the week ahead, data should show that business confidence remained weak in May.

NZ Budget may delay rate cut

New Zealand's Finance Minister Michael Cullen delivered his ninth Budget last week. According to the Minister, the Budget focused on providing a "fair deal" for all New Zealanders and planning for a strong and sustainable future. The Budget centered on five key areas: responding to families needing relief from price pressures; a fair, longer term tax program; maintaining social services; sensible fiscal management; and an integrated program to build a stronger, sustainable economy.

GDP growth will slow to 1.5% in the year to March 2009, according to government forecasts; this compares to JPMorgan's GDP growth forecast of 1.4% in the 2008 calendar year. The government also forecasts that inflation will moderate over the next three years, falling back within the RBNZ's 1-3% target range in 2009-10. We currently forecast inflation at 3.2% in 2008 and 2009.

The income tax relief was the focus of the Budget. Tax cuts will total NZ$10.6 billion over four years, and were made mainly via adjustments to income tax thresholds, although the lower tax rate was reduced. As of October, the bottom tax rate will fall from 15.0% to 12.5%. The changes to the tax thresholds over coming years mean that a worker earning NZ$50,000 a year will receive an extra NZ$16 a week from October 1 this year, an extra $22 from April 1, 2010, and an extra $32 from April 1, 2011.

The significant loosening of fiscal policy via unexpectedly large income tax relief delivered in the Budget, and the significant boost to government spending, leaves little scope for the RBNZ to cut interest rates in coming months. Futures market pricing had implied rate cuts could come as early as next month, but this now looks less likely. Expectations of a near-term boost to disposable income should boost household confidence, but the rising cost of staples, such as food and energy, will mean that the RBNZ nevertheless will offer some interest rate relief later this year.

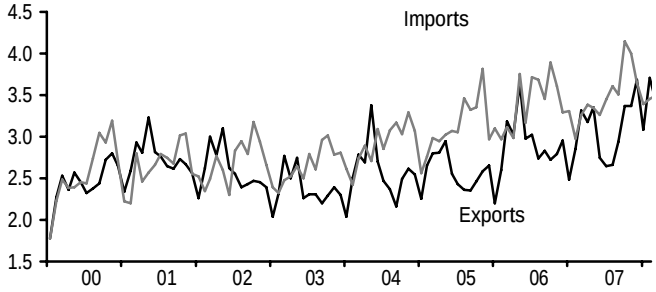
NZ Budget economic forecasts

	2008-09	2009-10	2010-11
Economic growth	1.6	2.9	3.2
Unemployment	3.7	4.4	4.5
Inflation	3.2	2.8	2.8
Current account (% of GDP)	-7.2	-7.2	-7.1
Private consumption	1.9	1.9	1.6
Exports	-0.9	4.0	4.4
Imports	0.9	1.3	1
90-day bank bill	8.5	7.9	7.9
TWI	68.6	63.1	59.1

Source: NZ Treasury

New Zealand: exports and imports

NZ$ billion, nsa



Our forecast calls for the RBNZ to cut the OCR 25bp in October and another 25bp in December, taking the key rate to 7.75% by year end. The risk, though, in the wake of this week's Budget, is that the RBNZ leaves the OCR at 8.25% until early 2009.

NZ trade balance remained in deficit

Data this morning showed that New Zealand's trade deficit widened to NZ$334 million in April (JPMorgan and consensus -NZ$150 million), marking the second straight monthly deficit. In March, a deficit of NZ$44 million was recorded (revised from –NZ$50 million), following a surplus of NZ$244 million in February.

In the 12 months to April, the deficit shrank to NZ$4.65 billion (JPMorgan -NZ$4.68 billion, consensus -NZ$4.42 billion) from a deficit of NZ$4.53 billion in the year to March. From a year ago, exports surged 19.7% to a record high, mainly owing to oil-related commodities, which have irregular monthly trade patterns. Crude oil exports were up NZ$265 million in April.

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Shipments of milk powder, butter and cheese were also up strongly, rising NZ$131 million. On the other side of the trade ledger, imports spiked 22%oya in April, a rise also attributed to oil-related commodities, including two large items—an oil platform and an oil production vessel—totaling NZ$477 million.

Kiwi business confidence still weak

NBNZ business confidence should have worsened in May. We forecast that the headline index will have dropped to -56.0 from -54.8 in April, suggesting that a net 56% of respondents expected business conditions to deteriorate over the coming year. Business confidence has deteriorated significantly in recent months as corporate profitability has dwindled amid soaring petrol prices and tighter credit conditions. The fact that most survey respondents still expect sales to fall over the next year has reaffirmed that momentum in the Kiwi economy is stalling.

Data releases and forecasts

Week of May 26 - 30

Mon May 26 10:45am — **Trade balance**
Not seasonally adjusted

	Jan	Feb	Mar	Apr
Exports ($NZ mn)	3082	3704	3439	3360
Imports ($NZ mn)	3395	3455	3489	3510
Trade balance ($NZ mn)	-313	249	-50	-150

Tue May 27 3:00pm — **RBNZ inflation expectations**
Not seasonally adjusted

	3Q07	4Q07	1Q08	2Q08
(%q/q)	2.6	2.7	2.7	__

Tue May 27 3:00pm — **NBNZ business confidence**

	Feb	Mar	Apr	May
% balance of respondents	-43.9	-57.9	-54.8	-56.0

Fri May 30 10:45am — **Building consents**
Not seasonally adjusted

	Jan	Feb	Mar	Apr
(%m/m)	0.3	7.5	-16.4	__
(%oya)	-7.3	-10.4	-30.9	__

Review of past week's data

Visitor arrivals
Not seasonally adjusted

	Feb		Mar		Apr	
Total (%m/m)	~~5.4~~	*5.3*	~~-0.3~~	*-0.5*	__	*-11.8*

Net permanent immigration

	Feb	Mar	Apr	
Monthly (000s)	2.0	-1.0	__	*-1.3*
12 month sum (000s)	4.6	4.7	__	*4.7*

Credit card spending
Seasonally adjusted

	Feb		Mar		Apr	
(%oya)	~~8.0~~	*8.1*	~~3.5~~	*3.3*	__	*8.3*

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Global essay

- **As global slowdown takes hold, rising inflation pressures trigger more central bank rhetoric than action for now**
- **Core inflation has surged in EM, while pipeline pressures are mounting in developed markets**
- **As EM Asian fiscal positions deteriorate under weight of surging fuel subsidies, retail price hikes become necessary**
- **Weakening data point to a potential contraction of 2Q**

Talk loudly and carry a little stick

Central banks are used to making difficult choices as they weigh the impact of their actions on growth, inflation, and financial stability. However, the choices they face today—with inflation pressures intensifying against a backdrop of fragile financial conditions and slowing global growth—present a unique challenge. The risk that subpar growth interacts negatively with credit market stress warrants the accommodative monetary policy stance currently in place in the global economy. However, inflation is moving sharply higher as commodity prices surge and global resource utilization remains elevated. The most likely response to these developments is for central banks to talk tough but act soft on inflation in the coming months. In doing so, they will reaffirm their bias toward growth and a belief that the underlying pressures pushing inflation higher will likely prove temporary. If our view is right, this behaviour will set the stage for a growth rebound and a more serious inflation threat next year. Accordingly, this year's tough talk will be followed by tough action in 2009.

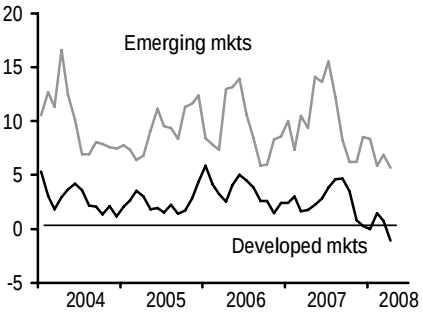
The latest indicators, on balance, reinforce our "less growth, less fear" outlook theme. A broad-based slowing in global growth appears to be taking hold following a surprisingly resilient growth outcome during 1Q08. The growth of global manufacturing output is stalling as we move toward midyear. US and Japanese output is now contracting while emerging market production gains are downshifting. Meanwhile, May business surveys reinforce the view that the Euro area economy is moving into a phase of subpar growth, even as a pronounced rotation in growth is under way toward Germany. At the same time, the broadening out of the growth slowdown is not producing intensified weakness in the United States. The message from high-frequency indicators is that the US economy continues to limp slowly forward as business cutbacks remain mild, and as financial stress gradually abates. Combined with the beneficial effects of the tax rebate checks now in the pipeline, the risk of a protracted recession has declined.

As the risk of a slide in the US economy declines, inflation is becoming a more pressing concern for much of the globe. Global consumer prices rose 4% in the 12 months through April, the most rapid rate of increase since 1999. Emerging market inflation has moved up far more dramatically—by more than three percentage points since early 2007, to 7.6%oya. While there are good reasons to look at the spike in headline inflation as a relative price movement reflecting food and energy price gains, there are increasing signs also of passthrough from rising commodity costs to other prices.

Recognizing that growth is slowing—in part, owing to the purchasing power squeeze from higher food and energy prices—the temptation to maintain a patient policy stance is strong. However, the lesson taught to every central banker is that the best defense against the costs of disinflation is to preemptively nip price pressures in the bud. The rhetoric from central bankers has turned uniformly more hawkish in recent weeks, reflecting this point of view. However, talk is not action and we do not foresee conditions that would produce tightening by major central banks in the coming months.

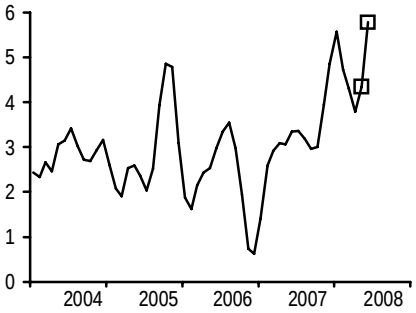
Global industrial production

%3m/3m, saar



Global consumer prices

%3m/3m, saar; fcst for May 08, Jun 08 (boxed)



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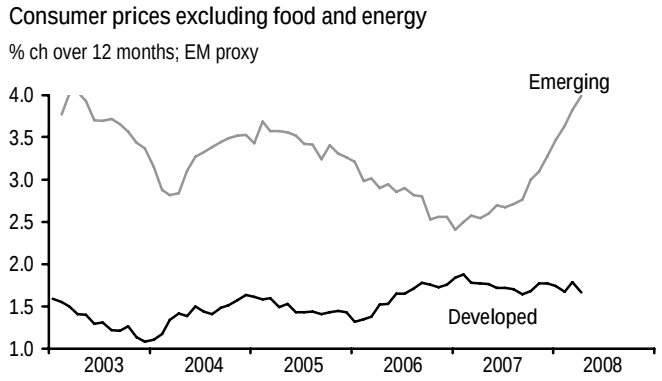

Until the US economy generates solid job growth, the Fed is in no position to begin normalizing rates. At the same time, the growth slowdown in Europe and Japan, along with political considerations in China, makes it unlikely that monetary policy will tighten any time soon. While some emerging market central banks are expected to tighten policy noticeably—Brazil, Russia, South Africa, and Indonesia—our GDP-weighted measure of global monetary policy rates is projected to remain essentially unchanged through year end. With real global policy rates expected to end the year more than a percentage point below neutral levels, the prospects for a recovery in growth in early 2009 should be seen as a mixed blessing. If our view is right, growth will pick up steam with inflation still elevated and global resource utilization rates above their 1990s peaks. This is a recipe for a significant, and potentially destabilizing, adjustment in monetary policy next year.

Global inflation pressures building

As central banks consider their response to recent inflation developments, they are processing a range of information that extends beyond the increases in food and energy prices that, even now, tend to be considered transitory. Indeed, although most central banks target headline inflation, they are less likely to respond to developments in the headline measure if they are not backed up by a corresponding movement in underlying inflation (i.e., excluding food and energy) or wages.

Global inflation excluding all food (including processed) and energy prices has been roughly stable of late, albeit at a fairly high level by the standard of recent years. However, this stability masks an important dichotomy among regions. In particular, core inflation over the past year and a half has surged in the emerging economies, wiping out the disinflation achieved in the earlier years of the expansion. In contrast, there has been a slight easing in the rate of core inflation in the developed economies, focused in the United States.

The story is similar concerning wages. Wage growth has gained speed across the EM, although the extent of this move is hard to quantify given the lack of comprehensive official data. Resource utilization is elevated in the EM group, and economic growth has remained robust, at least through late 2007. Wage pressures are better contained in the developed economies. Wage gains had begun to ramp up in the United States through the middle of last year, but have cooled since then in response to the rise in the unemployment rate. And although wage growth is rising to varying degrees elsewhere in the developed world, the pace has not been alarming.

While core prices and wages appear contained in the developed economies overall, there is an array of other indicators suggesting that the potential for a wage and price acceleration is high, barring a sustained period of below-trend growth. First of all, resource utilization remains elevated in the developed markets, despite some easing in the United States. Producer prices are escalating rapidly, as are import prices, even excluding food and energy. In some cases, these measures are rising at rates not seen in over a decade. Similarly, surveys of manufacturers' pricing intentions point to very widespread increases in the prices of both inputs and finished goods.

In addition to pipeline inflation pressures in the developed markets, inflation expectations have also picked up. In the United States, one-year inflation expectations in the Michigan survey are at the highest level since 1982, and the more telling 5-10 year inflation expectations are now at their highest level since 1996. In the United Kingdom and the Euro area, inflation perceptions are at the top end of the range of the past decade. Financial market indicators of inflation expectations are more mixed. Index-linked markets show 5y/5y forward breakevens moving up over the past year, although the move has been modest except in the United Kingdom, where there has been a much more marked deterioration.

EM Asia trimming energy subsidies

Although the shift toward market liberalization over the past decade has led some countries in EM Asia—such as the Philippines and Thailand—to reduce or entirely remove fuel subsidies, others continue to absorb rising energy costs. For these countries, the recent surge in energy prices is leading to a sharp deterioration in fiscal account positions. At the cur-

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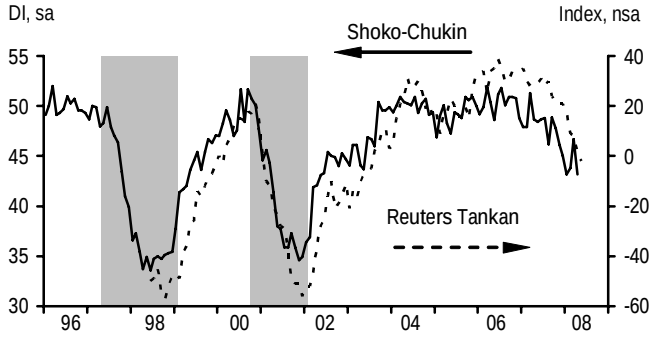
Japan manufacturing business sentiment



rent pace, these subsidy programs are fiscally unsustainable and will, ultimately, force hikes in retail fuel prices. The political, social, and economic fallout from this could be damaging.

In India, the revenue foregone by the state oil companies that sell fuel at subsidized retail prices could reach US$50 billion this year, or 3.8% of GDP. Such a drain on fiscal resources cannot be sustained and so fuel price hikes appear to be in the offing. The day of reckoning already has arrived in Indonesia. Although oil and gas production revenue has risen along with the rise in energy commodity prices, it has not gone up enough to offset the increase in subsidy costs. With a deficit that threatened to widen to 3% of GDP, the government has been forced to raise fuel prices an average of 28.7% (the last major increase was in 2005). Last week's reports indicate that plans also are afoot to cut subsidies in Taiwan and Malaysia.

Japanese economy hitting a wall in 2Q

There has been a striking loss of momentum in Japan's key activity indicators, a trend that continued last week in the form of news of an abrupt, sharp drop in export volume and falling department store sales. This week will bring a more complete look at activity in April. If the figures are close to our expectations, we are likely to revise down our GDP forecast to show a contraction in the current quarter. The BoJ, however, is likely to look past this development following two quarters of above-trend GDP growth. Indeed, veteran data-watchers know that Japan's activity data—and GDP—are subject to big momentum shifts that do not necessarily signal a change in the economy's underlying trajectory. What is more worrisome is the continued slide in the monthly business surveys (e.g., Shoko Chukin, Reuters Tankan), which have anchored our views about underlying growth in the past. The message they are sending now is that growth is turning decidedly weak.

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JPMorgan View - Global Markets

From recession to inflation fear

- Equity and credit markets have given back some of their recent gains, and bonds joined the selloff, as the rising price of oil and higher inflation readings raised **fears of a 1970s style bear market.** Over that decade, real returns were negative on US bonds and cash, and zero on US equities. The root cause of this dismal performance was a spike in oil prices, combined with the economic inefficiencies caused by high and volatile inflation, and procrastination by policymakers in fighting inflation.

- On the surface, the similarities with today are scary. But the differences are strong enough to keep us positive in riskier assets, for the moment. For one, the current rise in commodity prices is due more to a **demand shock**— from strong EM growth—rather than an OPEC-orchestrated supply shock. In addition, we are confident policymakers will move to control inflation before it gets out of hand.

- The global economy is weakening (even as it performs better than consensus expectations), which ought to reduce inflation pressure over the coming year, barring further rises in oil prices. Hence, we perceive a **window of opportunity** for riskier assets between the high recession risks of past quarters and the approaching fight against the global inflation monster. In our forecasts, this fight only becomes serious next year. The chronology of past US business and inflation cycles tells us that equities peak only a few months before the onset of an inflation-fighting induced recession, and not a year or so earlier. We thus stay overweight riskier asset classes, overweight EM equities, and short EM local bonds.

10-yr government bond yields

	Current	Jun 08	Sep 08	Dec 08	Mar 09
United States	3.84	4.00	4.05	4.10	4.15
Euro area	4.28	4.25	4.20	4.20	4.25
United Kingdom	4.93	4.70	4.90	4.90	5.00
Japan	1.70	1.30	1.30	1.45	1.60

Equities

	Current	YTD return (local currency)
S&P	1376	-4.3%
Topix	1377	-5.6%
FTSE 100	6087	-2.3%
MSCI Eurozone	214	-9.7%
MSCI Europe	1405	-6.7%

Credit markets

	Current	Jun 08	Dec 08
US high grade (bp over UST)	227	200	
US high grade (bp over swaps)	153	145	
Euro HG corp (bp over swaps)	85		65
USD high yield (bp vs. UST)	657	700	800
EMBIG (bp vs. UST)	280	275	250

Foreign exchange

	Current	Jun 08	Sep 08	Dec 08	Mar 09
EUR/USD	1.58	1.60	1.57	1.53	1.50
USD/JPY	103	100	101	103	105
GBP/USD	1.98	1.95	1.91	1.86	1.85

Commodities

		Quarterly average		
	Current	Jun 08	Sep 08	Dec 08
WTI oil $/bbl	131	105	95	92
Gold ($/oz)	924	920	915	900
Copper($/m ton)	8232	8600	8800	8000
Corn ($/Bu)	6.00	6.05	6.15	6.30

Source: JPMorgan, Bloomberg, Datastream.

Fixed income

- The rally in energy prices continues to push bond yields higher and curves flatter, especially in Europe. The outperformance of USTs vs. Euros in a selloff is atypical and a result of the perceived higher weight on inflation by the ECB and the forced unwinding of longs and steepeners in Europe amid still poor liquidity conditions. The market is pricing good chances of ECB and BoE tightening by the end of the year. We disagree. However, our client surveys are showing that there is still a **strong long base that might be further eroded,** despite the recent position covering. We therefore further reduce exposure to longs and recommend steepeners only at the very front end of the curve. We keep the bulk of the risk in trades that benefit from a normalization of Libor-OIS spreads: outright swap **spread tighteners,** swap spread curve steepeners, and overweight of high yielders vs. low yielders. Libor-OIS spreads are tighter on the week, but we think there is more to go. We also stay overweight **inflation linkers** vs nominals in the US, owing to positive carry, and in Japan, in anticipation of upward surprises in coming inflation readings.

- We introduce **a new strategy for trading the US curve** based on four signals: positions, economic surprises, curve momentum, and monetary policy momentum. Of these four signals, the first three point to US curve flattening (see "Trading the US Curve," Grace Koo and Nikolaos Panigirtzoglou, May 20).

Equities

- We **remain long equities** as the ongoing reversal in growth pessimism should induce more investors to cover their overweights of cash. M&A activity is also supportive. Strategic **M&A** (ex LBOs) has moved up to an $80bn weekly pace vs $50bn per week earlier this year.

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- Inflation fears have risen, putting pressure on equity markets. In our view, inflation is negative for stocks only to the extent that it hurts growth and earnings. This can happen when high inflation interacts with policy mistakes, as it did during the 1970s. We do not see this happening. Cyclically, it happens when tight monetary policy causes a recession. Sustained anti-inflation policies will eventually push the global economy and equities down, but this is a scenario that is 1-2 years away by our reckoning, and thus unlikely to affect equities now. Current high oil prices and their impact on inflation are mostly a reflection of strong EM growth and this keeps us long in equity markets and **overweight in EM.**

- With momentum remaining strong and no sign that demand for commodities is slowing in EM, commodity sectors should continue to outperform in the near term. This is overall positive for EM equities owing to their large exposure to commodity sectors. EM equity fund flows continue to show a **rotation toward commodity markets**, with last week showing the highest weekly inflows for this year into LatAm and EM Europe equity funds. This momentum is inducing us to tweak tactically our recommendations within EM towards oil exporters. We **downgrade China** to neutral and switch into Mexico.

Credit

- Credit spreads widened in CDS, as weaker equity markets induced investors to put on hedges. In cash bonds, in contrast, spreads tightened 10-20bp in HY and were little changed in HG.

- HY credit is supported by continued strong inflows and **stability in the loan market,** with prices stuck at 91 cents for more than a month. The pace of inflows into HY mutual funds has risen to $500mn per week over the past month vs outflows of $50mn per week in 1Q. **HG primary activity** remains very strong at $30bn per week in the US, which threatens to erode the cash balances of credit investors. We do recognize that the technical position of the market has worsened as investors have less cash on hand than two months ago, but **continued strong retail inflows into HG funds** is providing an offset. US retail investors bought HG funds at a $2bn per week pace over the past month, a pace last seen in the second quarter of last year.

- We **stay overweight in credit** on continued strong demand. We specifically favor US HG credit both outright and against US HY and European HG, favour loans vs bonds within HY, and overweight US CMBS, AAA ABS and AAA CLOs. We maintain our maturity steepeners in HG and favour cash bonds vs CDS, as the latter are more susceptible to equity market weakness.

Foreign exchange

- **As summer approaches, we recommend tilting the portfolio toward defensive trades**. The rationale is the odd confluence of central bank inactivity but potentially higher volatility. G-10 rate markets have repriced to imply rates on hold over the next few month. That backdrop normally would imply fewer opportunities to trade the rotation theme (which rests on shifting rate trends) but more opportunities to earn carry (which relies on stable/low volatility).

- The next several weeks argue against such complacency, however, in that the stagflation specter presented by +$130/bbl oil undermines the usual optimism in a period when the Fed is on hold after a major easing cycle. Accordingly, we recommend reopening longs in EUR/USD and selling EUR/CHF to position for weakness in carry trade. We keep a basket of emerging markets currencies (RUB, SGD, BRL), most of which should be less sensitive to volatility due to balance of payments support.

- **As a value trade, we stay long GBP/NZD.** Until last week, sterling and kiwi were the weakest links within G-10. Now, after an upside surprise on UK retail sales and a loosening of fiscal policy in New Zealand, they have both bounced smartly. The rationale for staying long sterling is valuation. Given the move in rate spreads this spring—3-month rates 12-months forward have moved more than 150bp in the UK's favor since March—the cross should be over 2.60.

Commodities

- **Oil** continues to print new all-time highs, bringing ytd gains to +30%. Prices have moved much faster than any verifiable indication of a tightening supply/demand balance, but absent a slowdown in emerging market demand, they will stay high. Upward momentum should slow since the front end of the curve has moved into contango, rendering longs a negative carry position. Base **metals** traded poorly, while precious metals were robust as rampant energy prices underpinned the more inflation-sensitive metals. Copper is now approaching our medium-term buy zone of 7800-8000. We continue to expect precious metals to trade strongly in a weak USD and inflation-sensitive environment, while base metals will show poor internal sector correlation reflecting diverse fundamentals. Copper and zinc offer the best opportunities short term, but aluminum will draw support from high energy prices.

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Global Economic Outlook Summary

	Real GDP			Real GDP							Consumer prices			
	% over a year ago			% over previous period, saar							% over a year ago			
	2007	2008	2009	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	1Q08	2Q08	4Q08	2Q09
The Americas														
United States	2.2	1.4	2.1	0.6	0.6	0.5	1.5	1.0	2.0	3.0	4.2	4.0 ↑	3.9 ↑	2.6 ↑
Canada	2.7	1.0	2.3	0.8	0.0	-0.5	1.5	2.3	2.5	2.8	1.8	1.9	2.4	1.9
Latin America	5.3	4.1	4.0	5.6	2.8	2.9 ↑	3.1 ↓	3.9 ↓	4.4	4.3 ↑	6.3	7.2 ↑	7.0 ↑	6.1 ↑
Argentina	8.7	6.5	3.0	8.0	2.0	8.2	2.8	6.1	2.8	1.6	8.5	9.1	9.1	8.9
Brazil	5.4	4.4	4.0	6.6	2.5	2.5	4.6	4.4	4.1	3.8	4.6	5.4 ↑	5.8 ↑	5.3 ↑
Chile	5.1	3.5	5.0	3.4 ↓	5.8 ↓	5.0 ↑	1.0 ↓	5.0 ↓	5.0	6.0 ↑	8.0	8.0	5.0	3.5
Colombia	7.5	5.0	5.0	6.8	6.0	5.5	5.5	4.5	4.5	5.0	6.1	5.3	5.2	4.4
Ecuador	2.0	2.5	2.5	5.0	2.0	1.5	1.0	1.0	2.5	3.5	5.3	8.3	7.7	4.6
Mexico	3.3	2.6	4.0	3.0	2.0	1.0	2.0	3.0	4.9	4.9	3.9	5.0	4.5	3.0
Peru	9.0	7.7	6.0	10.5	7.9	5.0	3.0	4.5	6.5	7.0	4.7	5.2	4.3	2.8
Venezuela	8.4	6.0	3.5	11.0	3.0	3.5	2.0	3.0	4.0	4.0	26.2	29.3	30.0	30.5
Asia/Pacific														
Japan	2.0	1.6	1.6	2.6	3.3	0.5	1.0	1.5	1.8	1.8	1.0	0.9	1.0	0.9
Australia	3.9	3.1	2.7	2.4	2.4	3.9	2.5	3.4	2.9	1.6	4.2	3.8	3.7	2.7
New Zealand	3.1	1.9	2.3	4.1	2.0	-0.1	0.7	1.7	2.8	3.4	3.4	3.0	2.9	3.2
Asia ex. Japan	8.8	7.4	7.5	6.8	7.4	6.4	7.7	7.4	7.3	7.5	6.2	6.3	4.6	3.9
China	11.9	10.5	9.8	9.2	10.5	10.8	11.7	10.2	9.1	9.1	8.0	6.9	3.7	3.7
Hong Kong	6.4	4.8	5.0	6.6	7.3	-1.0	3.5	3.0	5.5	8.0	4.6	5.4	3.1	2.4
India	8.7	7.0	8.0	4.8	8.2	7.0	7.0	7.4	7.8	8.7	5.8	6.1	6.2	5.2
Indonesia	6.3	5.4	5.2	5.1	5.9	5.0	5.0	5.0	5.0	5.0	7.6	12.4	14.2	8.3
Korea	5.0	4.4	5.0	6.4	2.9	2.7	3.5	4.5	5.5	5.5	3.8	4.1	3.7	3.1
Malaysia	6.3	4.7	5.3	7.4	3.0	1.0	4.0	5.5	6.1	6.1	2.6	3.1	2.2	1.8
Philippines	7.1	4.0	4.5	7.4	3.0	2.0	3.0	4.0	4.0	5.9	5.5	8.5	8.0	4.3
Singapore	7.7	4.5	6.0	-4.8	14.6 ↑	-2.0	5.7	5.7	7.0	7.0	6.6	6.8	4.9	1.9
Taiwan	5.7	3.5	4.5	2.6	0.8	0.2	4.5	4.5	4.8	4.8	3.3	4.0	1.7	2.4
Thailand	4.8	4.6	5.0	7.3	3.0	3.0	5.0	6.0	4.5	4.5	5.0	6.0	5.9	4.5
Africa														
South Africa	5.1	3.4	3.8	5.3	2.7	3.5	1.5	1.2	4.1	5.0	9.9	10.9	9.3	6.2
Europe														
Euro area	2.6	1.8	1.3	1.4	3.0	0.5	1.2	1.2	1.0	1.5	3.4	3.5	3.2	2.3 ↓
Germany	2.6	2.2	1.6	1.1	6.3	-0.8	1.5	1.6	1.8	2.0	3.1	3.0	2.8	1.9
France	2.1	1.8	1.6	1.4	2.6	1.0	1.5	1.4	1.5	1.8	3.3	3.4	2.9	2.1
Italy	1.4 ↓	0.4 ↓	1.0	-1.7 ↓	1.6 ↑	0.5	0.5	0.8	1.0	1.2	3.3	3.7	3.5	2.6 ↓
Norway	6.3 ↑	3.2 ↓	2.4 ↓	4.4 ↑	0.8 ↓	2.5	2.0 ↓	2.2 ↓	2.5 ↓	2.5 ↓	3.5	3.0	2.2	3.2
Sweden	2.8	2.5 ↑	2.3 ↓	3.1	3.2 ↑	1.7	1.5	2.3 ↓	2.5 ↓	2.5 ↓	3.2	3.2	2.5	2.3
Switzerland	3.1	2.3	1.6	4.2	1.8	1.0	1.0	1.3	1.8	2.0	2.5	2.1	1.7	1.3
United Kingdom	3.0	1.7	1.2	2.5	1.6	1.0	0.5	0.5	1.0	2.0	2.4	3.0	4.1	3.0
Emerging Europe[1]	6.5	5.7	5.5	12.9	0.5	6.8	4.2	10.7	1.2	6.3	9.2	9.9	8.4	6.3
Bulgaria	6.2	5.2	5.5	…	…	…	…	…	…	…	…	…	…	…
Czech Republic	6.5	5.0	4.8	7.0	3.6	4.5	3.5	4.5	5.5	5.0	7.4	7.1	5.5	3.0
Hungary	1.3	2.0	2.8	0.5	1.2	3.0	2.8	2.9	2.8	2.8	6.9	6.5	5.3	3.9
Poland	6.5	5.6	5.3	8.2	5.5	4.8	4.0	5.2	5.8	5.5	4.1	4.2	4.1	3.7
Slovak Republic	10.4	7.0	5.5	11.4	5.9	6.0	7.0	7.0	4.0	5.0	4.0	4.3	3.6	4.0
Romania	6.0	5.5	3.5	…	…	…	…	…	…	…	7.9	8.2	6.2	5.5
Russia	8.1	7.1	6.3	19.1	-3.0	9.0	4.0	17.0	-2.5	8.0	12.9	14.4	12.1	10.0
Turkey	4.5	4.4	6.0	…	…	…	…	…	…	…	9.5	10.0	8.3	4.1
Global	3.5	2.6	2.7	2.7	2.5	1.6	2.2	2.4	2.4	3.1	4.0	4.0 ↑	3.7 ↑	2.8
Developed markets	2.4	1.6	1.7	1.4	1.8	0.6	1.3	1.2	1.6	2.2 ↓	3.2	3.2 ↑	3.1 ↑	2.3
Emerging markets	7.4	6.2	6.2	7.5	5.0	5.5	5.8 ↓	7.0	5.4	6.5	6.8	7.2	6.0 ↑	4.9

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Global Central Bank Watch

	Official interest rate	Current	Change from Aug 07 (bp)	Last change	Forecast next change	Jun 08	Sep 08	Dec 08	Mar 09	Jun 09
Global	GDP-weighted average	3.64	-107			3.66	3.70	3.73	3.73	3.91
excluding US	GDP-weighted average	4.43	-3			4.45	4.51	4.55	4.55	4.58
Developed	GDP-weighted average	2.77	-137			2.76	2.76	2.75	2.75	2.99
Emerging	GDP-weighted average	7.22	16			7.34	7.54	7.72	7.70	7.64
The Americas	GDP-weighted average	2.85	-275			2.85	2.89	2.92	2.92	3.33
United States	Federal funds rate	2.00	-325	30 Apr 08 (-25bp)	2Q 09 (+25bp)	2.00	2.00	2.00	2.00	2.50
Canada	Overnight funding rate	3.00	-150	22 Apr 08 (-50bp)	10 Jun 08 (-25bp)	2.75	2.75	2.75	2.75	2.75
Brazil	SELIC overnight rate	11.75	25	16 Apr 08 (+50bp)	4 Jun 08 (+50bp)	12.25	13.25	14.00	14.00	14.00
Mexico	Repo rate	7.50	25	26 Oct 07 (+25bp)	on hold	7.50	7.50	7.50	7.50	7.50
Chile	Discount rate	6.25	75	10 Jan 08 (+25bp)	4 Sep 08 (-25bp)	6.25	6.00	5.75	5.75	5.75
Colombia	Repo rate	9.75	50	22 Feb 08 (+25bp)	1Q 09 (-25bp)	9.75	9.75	9.75	9.50	9.25
Peru	Reference rate	5.50	75	10 Apr 08 (+25bp)	on hold	5.50	5.50	5.50	5.50	5.50
Europe/Africa	GDP-weighted average	4.54	-3			4.58	4.60	4.60	4.61	4.58
Euro area	Refi rate	4.00	0	6 Jun 07 (+25bp)	**on hold**	4.00	4.00	4.00	4.00	4.00
United Kingdom	Repo rate	5.00	-75	10 Apr 08 (-25bp)	on hold	5.00	5.00	5.00	5.00	5.00
Sweden	Repo rate	4.25	75	13 Feb 08 (+25bp)	on hold	4.25	4.25	4.25	4.25	4.25
Norway	Deposit rate	5.50	75	23 Apr 08 (+25bp)	**on hold**	5.50	5.50	5.50	5.50	5.50
Czech Republic	2-week repo rate	3.75	50	7 Feb 08 (+25bp)	1Q 09 (-25bp)	3.75	3.75	3.75	3.50	3.50
Hungary	2-week deposit rate	8.25	50	28 Apr 08 (+25bp)	26 May 08 (+25bp)	8.50	8.50	8.50	8.25	8.00
Poland	7-day intervention rate	5.75	100	26 Mar 08 (+25bp)	**25 Jun 08 (+25bp)**	6.00	6.25	6.25	6.25	6.00
Russia	1-week deposit rate	3.75	50	29 Apr 08 (+25bp)	Jun 08 (+25bp)	4.00	4.25	4.50	4.75	4.75
Slovak Republic	2-week repo rate	4.25	0	27 Apr 07 (-25bp)	3Q 08 (-25bp)	4.25	4.00	4.00	4.00	4.00
South Africa	Repo rate	11.50	150	10 Apr 08 (+50bp)	12 Jun 08 (+50bp)	12.00	12.50	12.50	12.50	12.00
Switzerland	3-month Swiss Libor	2.75	25	13 Sep 07 (+25bp)	Sep 08 (-25bp)	2.75	2.50	2.25	2.25	2.25
Turkey	Overnight borrowing rate	15.75	-175	15 May 08 (+50bp)	16 Jun 08 (+50bp)	16.25	16.75	16.75	16.75	16.00
Asia/Pacific	GDP-weighted average	3.62	7			3.64	3.68	3.75	3.73	3.85
Australia	Cash rate	7.25	75	4 Mar 08 (+25bp)	on hold	7.25	7.25	7.25	7.25	7.25
New Zealand	Cash rate	8.25	0	26 July 07 (+25bp)	23 Oct 08 (-25bp)	8.25	8.25	7.75	7.50	7.50
Japan	Overnight call rate	0.50	0	21 Feb 07 (+25bp)	Jun 09 (+25bp)	0.50	0.50	0.50	0.50	0.75
Hong Kong	Discount window base	3.50	-325	1 May 08 (-25bp)	2Q 09 (+25bp)	3.50	3.50	3.50	3.50	4.00
China	1-year working capital	7.47	45	20 Dec 07 (+18bp)	3Q 08 (+27bp)	7.47	7.74	8.19	8.19	8.19
Korea	Base rate	5.00	0	9 Aug 07 (+25bp)	**Sep 08 (-25bp)**	5.00	4.75	4.50	4.50	4.50
Indonesia	BI rate	8.25	0	6 May 08 (+25bp)	5 Jun 08 (+50bp)	8.75	9.00	9.00	9.00	9.00
India	Repo rate	7.75	0	30 Mar 07 (+25bp)	1Q 09 (-25bp)	7.75	7.75	7.75	7.50	7.25
Malaysia	Overnight policy rate	3.50	0	26 Apr 06 (+25bp)	on hold	3.50	3.50	3.50	3.50	3.50
Philippines	Reverse repo rate	5.00	-100	31 Jan 08 (-25bp)	5 Jun 08 (+25bp)	5.25	5.50	5.50	5.50	5.50
Thailand	1-day repo rate	3.25	0	18 July 07 (-25bp)	**16 Jul 08 (+25bp)**	3.25	3.50	3.75	3.75	3.75
Taiwan	Official discount rate	3.50	38	27 Mar 08 (+12.5bp)	Jun 08 (+12.5bp)	3.625	3.625	3.625	3.625	3.75

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, ur*

				2007			2008				2009			
	2007	2008	2009	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Chain volume GDP	3.9	3.1	2.7	3.5	4.3	2.4	2.4	3.9	2.5	3.4	2.9	1.6	2.5	2.3
Private consumption	4.5	3.5	2.0	2.4	5.3	6.7	2.8	2.4	1.6	2.0	2.4	1.6	2.0	1.6
Construction investment	9.2	1.7	3.7	3.6	2.8	-3.0	1.6	1.8	6.1	3.0	5.1	2.0	1.9	5.9
Equipment investment	7.5	5.8	-1.8	19.6	-9.9	15.9	8.7	8.6	-4.1	0.0	-2.1	-4.1	-8.1	8.7
Public investment	5.1	10.3	6.0	88.3	-6.7	23.8	4.4	5.0	5.2	5.6	6.0	6.4	6.8	7.2
Government consumption	3.0	3.7	2.8	1.4	3.7	7.0	2.9	3.0	2.9	3.0	3.5	2.2	1.8	2.2
Exports of goods & services	3.3	3.8	6.3	3.6	6.1	-2.6	4.1	5.1	7.2	7.8	4.1	6.1	7.2	8.2
Imports of goods & services	10.7	5.1	2.5	5.7	9.4	15.0	2.0	0.0	2.0	3.2	3.2	2.4	1.8	3.2
Contributions to GDP growth:														
Domestic final sales	4.9	3.9	2.3	6.2	3.7	6.7	3.3	3.1	2.3	2.4	2.9	1.6	1.4	3.2
Inventories	0.8	-0.4	-0.3	-2.0	1.5	-0.2	-1.2	-0.2	-0.7	0.2	-0.1	-0.6	0.0	-1.8
Net trade	-1.7	-0.4	0.7	-0.6	-0.9	-3.8	0.3	1.0	0.9	0.8	0.1	0.7	1.0	0.9
GDP deflator (%oya)	3.9	3.1	2.6	4.3	3.4	3.4	3.3	3.4	3.2	2.7	2.6	2.6	2.6	2.5
Consumer prices (%oya)	2.3	3.9	2.7	2.1	1.9	3.0	4.2	3.8	4.0	3.7	3.0	2.7	2.6	2.5
Producer prices (%oya)	2.3	5.7	2.5	1.5	0.8	3.4	6.9	5.0	6.0	5.0	2.5	2.5	2.5	2.5
Trade balance (A$ bil, sa)	-20.9	-25.5	-15.1	-4.4	-5.3	-7.2	-7.2	-6.6	-6.2	-5.5	-5.0	-4.3	-3.1	-2.8
Current account (A$ bil, sa)	-67.0	-79.5	-78.2	-15.8	-16.4	-19.3	-19.8	-20.1	-19.7	-19.9	-20.0	-20.1	-19.6	-18.6
as % of GDP	-6.2	-6.9	-6.4	-5.9	-6.0	-7.0	-7.0	-7.0	-6.8	-6.7	-6.7	-6.7	-6.4	-6.0
3m eurodeposit rate (%)*	6.0	7.3	6.8	5.8	7.1	7.2	7.3	7.3	7.3	7.1	6.9	6.8	6.8	6.7
10-year bond yield (%)*	5.6	6.4	6.3	5.6	5.7	6.4	6.5	6.5	6.5	6.3	6.3	6.3	6.3	6.3
US$/A$*	0.75	0.95	0.84	0.74	0.77	0.91	0.96	0.97	0.95	0.93	0.88	0.85	0.82	0.79
Commonwealth budget (FY, A$ bil)	13.6	15.5	10.0											
as % of GDP	1.3	1.3	0.8											
Unemployment rate	4.4	4.5	5.3	4.3	4.3	4.3	4.1	4.4	4.6	4.9	5.1	5.2	5.3	5.4
Industrial production	3.3	1.9	0.8	1.4	-0.1	5.6	0.0	1.0	3.0	4.0	-1.0	-2.0	-3.0	0.0

*All financial variables are period averages

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

				2007			2008				2009			
	2007	2008	2009	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real GDP (1995-96 prices)	3.1	1.4	2.2	3.6	2.0	4.1	0.1	-0.3	0.7	1.7	2.8	3.4	2.4	3.6
Private consumption	4.3	0.8	1.2	2.2	1.5	2.0	0.5	-0.1	-0.5	0.5	0.7	2.1	2.9	3.3
Fixed Investment	4.5	0.1	0.9	-2.7	1.5	19.4	-6.2	-6.8	-2.7	0.3	2.0	2.8	3.1	3.9
Residential construction	4.3	-9.8	-1.7	13.3	7.7	-6.1	-22.0	-18.0	-6.0	-2.0	0.0	0.8	2.8	3.2
Other fixed investment	4.6	2.6	1.5	-6.4	0	26.9	-2.0	-4.0	-2.0	0.8	2.4	3.2	3.2	4.0
Inventory change (NZ$ bil, saar)	0.8	0.1	-0.1	0.4	0.3	0.0	0.1	0.1	0.0	-0.1	0.0	0.0	-0.1	-0.1
Government spending	4.0	5.5	3.8	4.7	8.5	1.5	6.0	7.0	5.9	4.8	2.4	3.2	2.9	2.5
Exports of goods & services	3.5	4.1	2.8	-3.3	-0.4	23.2	-1.5	1.5	2.5	2.5	2.5	3.1	3.6	3.7
Imports of goods & services	8.8	4.6	1.0	11.0	2.9	18.5	0.6	0.6	0.2	0.5	0.5	1.5	2.2	2.5
Contributions to GDP growth:														
Domestic final sales	4.6	2.3	1.8	4.6	4.7	7.8	-0.3	-0.7	1.4	1.3	1.3	2.6	3.1	3.5
Inventories	0.5	-0.5	-0.1	4.0	-1.5	-3.6	1.1	0.1	-1.4	-0.2	0.8	0.4	-1.0	-0.1
Net trade	-2.0	-0.4	0.5	-4.9	-1.2	0.2	-0.7	0.3	0.7	0.6	0.6	0.4	0.3	0.3
GDP deflator (%oya)	4.0	4.4	2.8	4.0	3.7	5.4	5.3	4.7	4.5	3.0	2.9	2.8	2.7	2.7
Consumer prices	2.4	3.2	3.2	4.0	2.0	4.8	2.7	2.7	3.1	2.9	3.1	3.5	3.4	3.2
%oya	2.4	3.2	3.2	2.0	1.8	3.2	3.4	3.0	3.3	2.9	3.0	3.2	3.2	3.3
Trade balance (NZ$ bil, sa)	-2.3	-0.8	0.8	-0.8	-0.7	0.1	-0.2	-0.2	-0.2	-0.2	-0.1	0.1	0.3	0.5
Current account (NZ$ bil, sa)	-13.8	-10.2	-8.5	-3.5	-3.6	-3.1	-2.6	-2.5	-2.5	-2.6	-2.5	-2.3	-2.0	-1.7
as % of GDP	-8.1	-5.7	-4.5	-8.4	-8.4	-7.0	-5.8	-5.7	-5.5	-5.6	-5.4	-4.9	-4.2	-3.5
Yield on 90-day bank bill (%)*	8.4	8.5	7.8	8.2	8.7	8.8	8.8	8.4	8.4	8.4	8.0	7.9	7.6	7.5
10-year bond yield (%)*	6.3	6.6	7.0	6.4	6.4	6.4	6.4	6.6	6.7	6.8	7.0	7.1	7.0	7.0
US$/NZ$*	0.74	0.80	0.68	0.74	0.74	0.76	0.79	0.83	0.80	0.78	0.72	0.66	0.67	0.68
Commonwealth budget (NZ$ bil)	6.4	5.3	5.0											
as % of GDP	3.8	2.9	2.6											
Unemployment rate	3.6	3.9	4.5	3.6	3.5	3.4	3.6	3.9	4.1	4.2	4.3	4.5	4.6	4.7

*All financial variables are period averages

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Australia and New Zealand economic calendar

26 May New Zealand: Trade balance (10:45am) Apr	27 May New Zealand: RBNZ inflation expectation (02:00pm) 2Q	28 May Australia: Westpac leading index (10:30am) Mar Construction work done (11:30am) 1Q	29 May Australia: Private capital expenditure (11:30am) 1Q New Zealand: NBNZ business conf. (03:00pm) May Money supply (03:00pm) Apr	30 May Australia: Pvt. sector credit (11:30am) Apr New Zealand: Building permits (10:45am) Apr
2 Jun Australia: Inventories (11:30am) 1Q Retail sales (11:30am) Apr Company profits (11:30am) 1Q RBA comm. index (04:30pm) May *Holiday New Zealand*	3 Jun Australia: Current account (11:30am) 1Q Building approvals (11:30am) Apr RBA cash target (02:30pm) Jun	4 Jun Australia: GDP (11:30am) 1Q New Zealand: ANZ commodity price (03:00pm) May	5 Jun Australia: Trade balance (11:30am) Apr New Zealand: RBNZ official cash rate (09:00am) Apr	6 Jun Australia: Foreign reserves (04:30pm) May
9 Jun New Zealand: QV house price May *Holiday Australia*	10 Jun Australia: Housing finance (11:30am) Apr ANZ job ads (11:30am) May NAB business confidence (11:30am) May	11 Jun Australia: Westpac consumer confidence (10:30am) Jun New Zealand: Terms of trade (10:45am) 1Q	12 Jun Australia: Consumer inflation expectation (10:30am) Jun Unemployment rate (11:30am) May New Zealand: PMI (12:00pm) May	13 Jun New Zealand: Retail sales (10:45am) Apr

Highlighted data are scheduled for release on or after the date shown. Times shown are local.

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Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
26 - 30 May	26 May	27 May	28 May	29 May	30 May
	Germany • CPI prelim and 6 states (May) **Hungary** • NBH meeting **Malaysia** • BNM meeting	**Germany** • GDP final (1Q) **Slovak Republic** • NBS meeting **United Kingdom** • BBA mort approvals (Apr) **United States** • New home sales (Apr) • S&P/C-S HPI (Mar, 1Q) **Euro area bus surveys** • France INSEE (May) • Italy ISAE (May) • Netherlands CBS (May)	**Brazil** • IPCA-15 (May) **Japan** • Shoko Chukin (May) • Shirakawa speech **Poland** • NBP meeting **Norway** • Norges Bank meeting **South Africa** • CPI X (Apr) **United States** • Durable goods (Apr)	**Canada** • Payrolls (Mar) **Euro area** • EC bus survey (May) • M3 (Apr) **Germany** • Employment (Apr) • Unemployment (May) **Japan** • Retail sales (Apr) **United Kingdom** • Nationwide HPI (May) **United States** • Real GDP prelim (1Q) • Bernanke speech	**Canada** • Real GDP (1Q) **Euro area** • HICP flash (May) • Unemployment (Apr) **Germany** • Retail sales (Apr) **Japan** • Core CPI (Apr) • Household spend (Apr) • Housing starts (Apr) • IP prelim (Apr) • PMI mfg (May) • Unemployment rate (Apr) **Korea** • IP (Apr) **United States** • Chicago Fed bus survey (May) • Consumer sent (May) • Personal income (Apr)
2 - 6 June	2 June	3 June	4 June	5 June	6 June
Japan • Cabinet Office private consumption index (Apr) **Korea** • GDP (1Q) **United Kingdom** • Halifax HPI (May)	**China** • PMI mfg (May) **Euro area** • PMI mfg final (May) **Japan** • Nominal wages (Apr) **Korea** • CPI (May) • Trade balance (May) **United Kingdom** • PMI mfg (May) **United States** • Construction spend (Apr) • ISM mfg (May)	**Australia** • RBA meeting **Brazil** • IP (Apr) **Euro area** • GDP prelim (1Q) **Singapore** • PMI mfg (May) **United States** • Factory orders (Apr) • Light vehicle sales (May)	**Australia** • GDP (1Q) **Brazil** • COPOM meeting **Euro area** • PMI services final (May) • Retail sales (Apr) **Japan** • MoF corp survey (1Q) **United Kingdom** • PMI services (May) **United States** • ADP employment (May) • ISM nonmfg (May) • Prod and costs revised (1Q)	**Canada** • Ivey PMI (May) **France** • Unemployment (1Q) **Germany** • Mfg orders (Apr) **Taiwan** • CPI (May) **United States** • Flow of funds (1Q) **Central bank meetings** • Euro area • Indonesia • New Zealand • Philippines • United Kingdom	**Germany** • IP (Apr) **Russia** • CPI (May) **United States** • Consumer credit (Apr) • Employment report (May) • Wholesale trade (Apr)

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