

# Australia and New Zealand - Weekly Prospects

## Summary

- Last week's minutes from the **RBA's** August Board meeting reaffirmed our expectation that the RBA will cut the cash rate on 2 September. RBA officials now place significantly more emphasis on the downside risks to growth than the upside risks to inflation. By presenting an unexpectedly nuanced assessment of the growth and inflation dynamics, however, the minutes indicate that there remains "considerable uncertainty" about the outlook and that there are "powerful forces pulling in opposite directions." Indeed, an extended period of official rate cuts is not a "done deal". Data this week probably will show that demand for credit remained subdued in July, but that firms boosted their business investment spending in 2Q, after an unexpected contraction in 1Q. The investment spending pipeline should remain impressive.
- In **New Zealand**, the 2Q PPI print indicated that pipeline price pressures remain significant; this increases the risk that RBNZ officials may rethink the length and depth of the easing cycle on which it recently embarked. Our forecast calls for a gradual and steady decline in the OCR to 6.25% by mid-2009. Inflationary pressures remain at large, however, and data this week should show that inflation expectations, measured by the RBNZ, remained elevated in 3Q, with business managers expecting inflation to be at the top end of the RBNZ's 1-3% oya target range in two years' time.
- **Global growth** turned sharply weaker around midyear and there are good reasons to expect growth to remain subpar for some time. There is significant pressure on European and Asian firms to cut back in response to a profit margin squeeze and an unwanted rise in inventories during 1H08. What's more, there is little in the way of global policy stimulus to cushion the blow. Tight credit conditions are offsetting the beneficial effects of the past year's 200bp drop in global real policy rates. Fiscal policy remains modestly accommodative, largely driven by EM governments. But the principal policy dynamic currently at work is the fading of the benefits from US tax rebate checks at a time when incomes are being compressed by high inflation. This week's July personal income report should show a second straight fall in real consumption, pointing to the first quarterly contraction by US consumers since 1991.
- **UK GDP growth** stalled in 2Q, but what's alarming is the message on demand growth. Private consumption, and business and other investment each fell, and the 3.5% annualized rate of decline in domestic demand matched lows not seen since the depths of the early 1990s recession. Although some of the weakness in 2Q consumption was payback for 1Q strength, the trajectory of retail sales into 3Q and the forthcoming increases in energy bills point to continued consumption weakness. Households may come under added pressure from a weaker labour market, as recent indicators suggest that the corporate adjustment is spreading from capex to employment. While the magnitude and longevity of the spike in CPI inflation remain a concern for the MPC, the severity of the downturn in demand reinforces the case for a rate cut this November.

## This week's highlight

The Aussie business investment survey on Thursday. Spending probably rebounded in 2Q, but the most important part of the survey is firms' expectations of future spending. This survey is likely to see plans scaled back a little, owing to fragile confidence.

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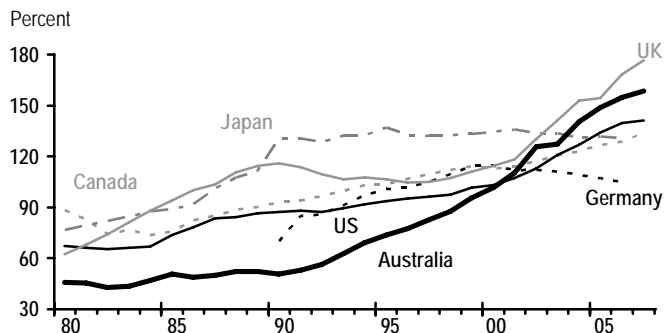
## Data and event previews - Australia and New Zealand

Date <sup>(a)</sup>	Data/event	Forecast			Comment
		JPMorgan	Consensus	Previous	
Tuesday, 26 August (8.45am)	<b>NZ trade balance (NZ\$ mil, Jul.)</b>	<b>-425.0</b>	-538.0	-223.0	The trade deficit should have widened in July, marking the fifth straight monthly deficit. Export growth should benefit from weaker NZD and higher dairy and oil exports; the latter reflecting increased production from the Tui oil field and elevated prices of dairy products and crude oil. Import growth should have slowed from a year ago on the back of weaker domestic demand.
Tuesday, 26 August (3.00pm)	<b>RBNZ inflation expectations (%q/q, Q3)</b>	na	na	2.9	Inflation expectations should remain elevated in 3Q at the top end of the RBNZ's 1-3% target range. In 2Q, the RBNZ's survey of 80 business managers showed that inflation is expected to average 2.9% in two years' time. On our and the RBNZ's forecast, inflation has yet to peak. The RBNZ expects inflation to peak at 5% oya in 3Q, but we expect it to peak at 5.2% in 4Q given the recent surge in producer prices and the sharp decline in NZD.
Wednesday, 27 August (11.30am)	<b>Aust. construction work done (%q/q, Q2)</b>	2.2	1.5	2.3	Construction work done probably expanded by 2.2%q/q in the June quarter, after a similar-sized rise in Q1. The resulting positive contribution to GDP growth will help offset the hole left by consumer spending.
Thursday, 28 August (11.30am)	<b>Aust. private business investment survey (%q/q, Q2)</b>	<b>4.0</b>	2.0	-2.5	Private investment spending probably rebounded 4%q/q in Q2, despite higher funding costs, lower confidence and increased doubts about the resilience of the global economy. More importantly, there will be an update of firms' investment spending plans for the year ended June 2009. In the last survey in May, managers estimated that they would boost capex by 24% in the current fiscal year, down only slightly from the 25% rise expected in the previous survey. To maintain this impressive growth rate, the third spending estimate for 2008-09 needs to print at A\$94 bn. The final estimate for 2007-08 probably will come in at A\$86.3 bn. The latest Access Economics survey of the investment plans shows a pipeline of spending worth more than A\$600 bn - the pipeline has expanded by 19% over the past year.
Thursday, 28 August (3.00pm)	<b>NBNZ business confidence (% , Aug.)</b>	<b>-40.0</b>	na	-43.2	The NBNZ business confidence survey likely improved slightly in August in the wake of the RBNZ's rate cut. Watch out for the reading of firms' own activity expectations, which dropped sharply in July to -8.2 from -4.0 in June and pointed to a contraction in GDP growth in 2Q. Corporate profitability continues to suffer amid high interest rates and tighter credit conditions, but rate cuts should help support economic growth in late 2008, helping to pull the struggling economy out of recession.
Friday, 29 August (8.45am)	<b>NZ building consents (%m/m, Jul.)</b>	na	na	na	na
Friday, 29 August (11.30am)	<b>Aust. private sector credit (%m/m, Jul.)</b>	<b>0.4</b>	0.5	0.4	Credit growth has dropped sharply since the RBA's rate hikes earlier this year. Credit likely expanded just 0.4% m/m in July, only one third the growth rate of the last quarter of 2007. Personal credit probably contracted again, and housing and business credit likely rose 0.5% m/m and 0.4%, respectively. The annual growth rate in total credit probably dropped to 11% - the weakest growth rate since 2002.

(a) Australian Eastern Standard Time.

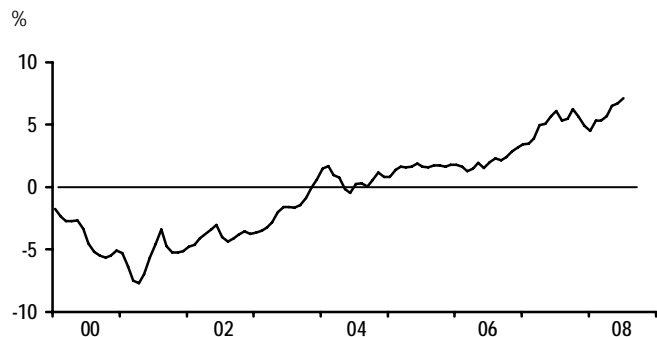
## Feature charts

Household debt to disposable income ratio



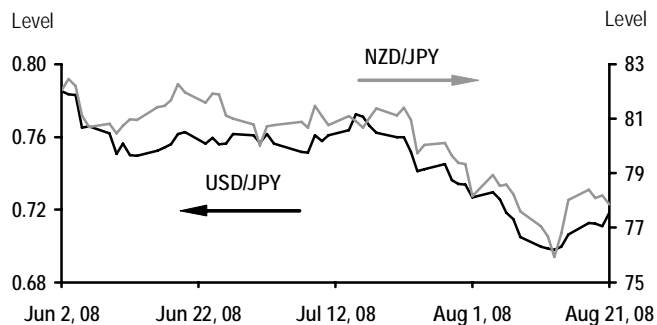
Australian consumers' ratio of debt to disposable income has soared to 160% since the mid-1990s, but still trails the 177% in the UK (according to the OECD). The US also has seen a big rise to 140%. House prices in the UK and the US are tumbling. Australian house prices also are likely to decline, but to a much lesser extent than in the US and the UK. This is partly because Australia does not have an overhang of unsold homes. Also, there is indirect support for the housing market from Australia's mining boom and rising skilled migration.

Australia: JPM monetary conditions index



Monetary conditions in Australia are the tightest since 1991, as measured by the JPMorgan MCI, although should loosen in coming months. Our forecast calls for the RBA to cut interest rates twice this year, with the first cut coming in September. The domestic banks probably will pass on the official rate cuts. NAB and ANZ, two of the "Big Four" banks, have promised to deliver borrowers the full benefit of the official rate cut anticipated in September.

NZD heading south



The Kiwi dollar has shed 8.5% against the US dollar since the start of June and 5% against the yen. The kiwi will continue to trend south as the RBNZ cuts interest rates and the economy battles through recession. Our forecast calls for the RBNZ to cut interest rates by another 75bp this year and for the economy to record two negative quarters of growth in 2Q and 3Q, after the 0.3%q/q contraction in GDP logged in the first three months of the year.

## Economic Research note

### RBNZ easing will prevent prolonged recession

- **Shallow economic recession forecast in 2008**
- **RBNZ to cut cash rate another 75bp this year**
- **Inflation to peak at 5.2%oya in 4Q**

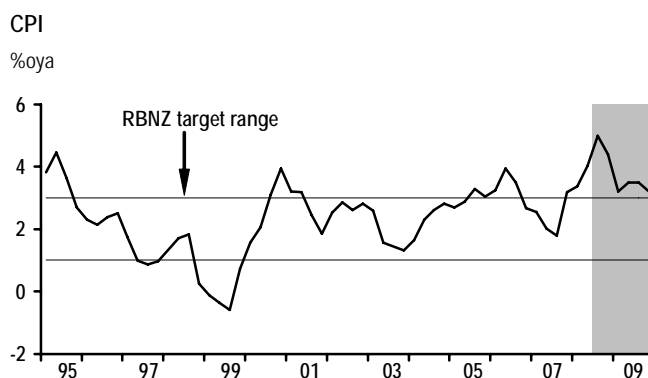
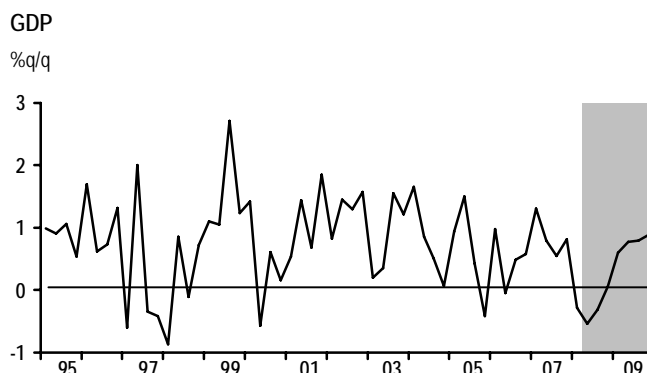
RBNZ Governor Alan Bollard signaled in June that softer economic growth and the prospect of easing medium-term inflation were paving the way for the official cash rate (OCR) to fall. In July, amid signs of further deterioration in the New Zealand economy, the RBNZ embarked on what we believe will be an extended easing cycle. It cut the OCR 25bp to 8.0%, the first rate cut in five years.

The RBNZ appears prepared to lower its policy rate significantly, although at a steady pace so as to not destabilize the economy or financial markets. It has acknowledged that there is ample scope for a projected easing in interest rates, given that real interest rates in New Zealand are among the highest in the developed world. We expect another three 25bp cuts this year—in September, October, and December (there is no scheduled policy meeting in November) and further rate cuts in 2009. We forecast the OCR at 6.25% by mid-2009, but how quickly the RBNZ lowers the cash rate will depend on how the economy responds to policy changes. The desire to avoid an inflationary plunge in NZD minimizes the chance of a 50bp cut.

#### Recession to be shallow and short-lived

Economic momentum in New Zealand has stalled. Retail spending is at its weakest since 1991, consumer confidence is at a 17-year low, business confidence has collapsed, and house sales have plummeted to near 16-year lows. Elevated export prices, however, and the government's expansionary fiscal policy, have prevented a sharper downturn.

The economy contracted 0.3%q/q in 1Q. We expect another two quarters of GDP contraction in 2Q and 3Q, and for the economy to stagnate in the final quarter of the year. The last time the Kiwi economy endured successive quarters of negative growth was at the end of 1997 and in early 1998; this was a relatively mild recession. The recession we forecast in 2008 also should be shallow and short-lived. Our forecast calls for GDP growth to recover to 1.5% in 2009 thanks mainly to the forthcoming personal income tax cuts, lower interest rates, increased govern-



ment spending, less drag from the housing market, and the anticipated positive impact on exports from weaker NZD, which has come under significant selling pressure in recent weeks.

#### Inflation to get worse before improving

Inflation pressures remain widespread, however. Headline inflation accelerated to an 18-year high of 4%oya in 2Q, well above the RBNZ's 1-3% target range, owing to surging gasoline and food prices. More importantly, nontradable inflation—generated domestically and not influenced by the exchange rate—remained uncomfortably high at 3.4%oya; this remains a key point of focus for RBNZ officials.

The risk is that with nontradable inflation persistently high, despite the significant easing in domestic demand, wage and price setting behaviour could change—already elevated inflation expectations are trending higher. The potential for second- and third-round inflation effects to develop is a primary concern for the RBNZ. That said, RBNZ Governor Bollard believes that the bank's current policy of inflation targeting is anchoring inflation expectations and allowing room to accommodate short-term inflation shocks. Monetary policy, he says, should be flexible to deal with unavoidable price shocks, while ensuring that inflation returns to target in the medium term—

monetary policy should be “firm enough to ensure that generalized second- round inflation effects do not take hold.” This argues against more aggressive rate cuts.

The RBNZ forecasts inflation to peak at 5% oya in 3Q before returning to target over the medium term; that is, as long as “commodity prices stop rising, inflation expectations remain anchored, and weakening economic activity contributes to an easing in nontradable inflation.” Our forecast calls for headline CPI to peak in 4Q at a slightly higher 5.2% oya, with upside risks owing to the recent decline in NZD. The significant price pressures in the pipeline—producer input and output prices spiked 5.6%q/q and 3.5%, respectively, in 2Q—places additional upside risks on our forecast. That said, RBNZ officials will look through elevated inflation readings in coming quarters. The focus for RBNZ officials remains the near-term growth outlook and the medium-term inflation outlook.

### Business sentiment still very weak

Employees’ ability to demand higher wages in response to high inflation, however, should be limited. Corporate profitability has dwindled amid soaring petrol prices and tighter credit conditions, meaning that firms will probably shed employees to cut costs as economic momentum slows and become less willing to pay more for existing workers.

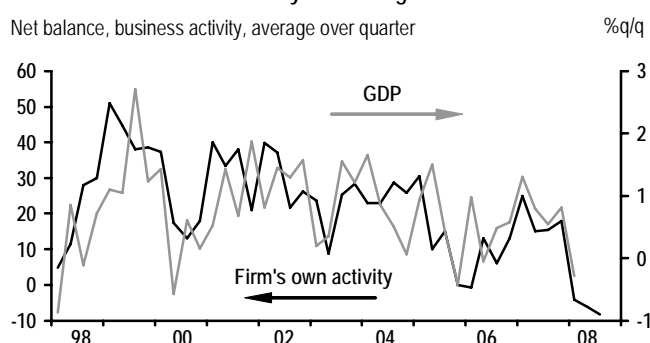
The NBNZ July business confidence survey showed that 43.2% of respondents expect business conditions to deteriorate in the year ahead. Had it not been for heightened speculation of an imminent rate cut, business confidence would likely have fallen further. More worrisome was the sharp drop in firms’ own activity expectations from -4.0 to -8.2; this signals a deeper contraction in economic growth in 2Q. Only 16 negative readings in firms’ own activity expectations have occurred in the last 20 years. The NBNZ says that five of these “were right at the start of the survey in 1988, as the 1987 crash washed through.”

### Some relief for struggling consumers

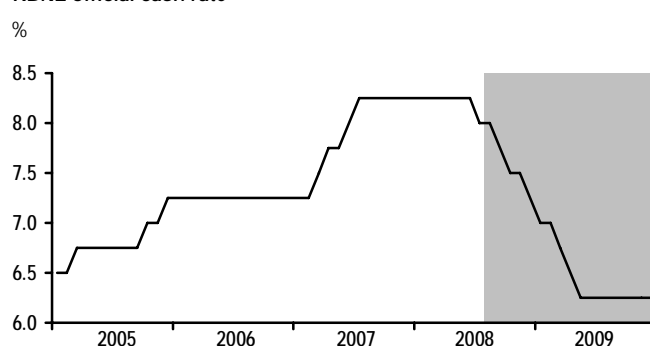
The household sector also is under intense pressure. High interest rates, elevated food and energy prices, and the negative wealth effects from the crumbling housing market have created significant headwinds for consumers. These headwinds have dramatically squeezed consumer spending. In real terms, retail sales sank 1.5%q/q in 2Q, the largest fall on record and the first time since June 1998 that volumes have fallen in two straight quarters—in 1Q volumes fell 1.2%.

While the near-term outlook for retailers is bleak, some improvement in sales can be expected toward year end. Along with lower interest rates, the consumer sector should benefit from

NBNZ business outlook survey and GDP growth



RBNZ official cash rate



additional government spending, lower petrol prices, and the income tax relief delivered starting October 1. Furthermore, the domestic banks already are passing on the OCR cuts to borrowers, mainly via lowering two-year fixed mortgage rates. Fixed rate loans account for 88% of total loans in New Zealand. Mortgage rates probably will edge lower as the RBNZ’s easing cycle continues.

### NZD still a key concern for RBNZ

A key risk to the interest rate outlook is a sharp fall in NZD. Expectations of an extended easing cycle, coupled with the rapid deterioration of the economy, have driven a sharp fall in the NZ dollar in recent weeks. NZD has shed 7% against the US dollar since mid year. If NZD falls even more sharply, the inflation profile will deteriorate, leading the RBNZ to refrain from cutting interest rates as steadily and for a long as currently forecast.

Recent NZD weakness is also reflecting broad USD strength and growing speculation that the RBA, Australia’s central bank, will begin easing policy next month. Like the RBNZ, the RBA has the luxury of high interest rates as a starting point. With that in mind, the downside for NZD should be limited—NZD should retain some interest rate-derived support in that the OCR will remain high even after the 75bp in rate cuts we forecast this year.



## Australia

- **RBA minutes point to September rate cut**
- **Business investment to rebound in June quarter**
- **Credit growth to remain subdued at 0.4%/m/m**

The minutes from the RBA's August Board meeting provided no revelations and reaffirmed our expectation that the RBA will cut official interest rates in September. RBA officials now place significantly more emphasis on the downside risks to growth than on the upside risks to inflation. Data this week probably will show that demand for credit remained subdued in July and that firms boosted their business investment spending in 2Q, after an unexpected contraction in 1Q. The investment spending pipeline should remain impressive.

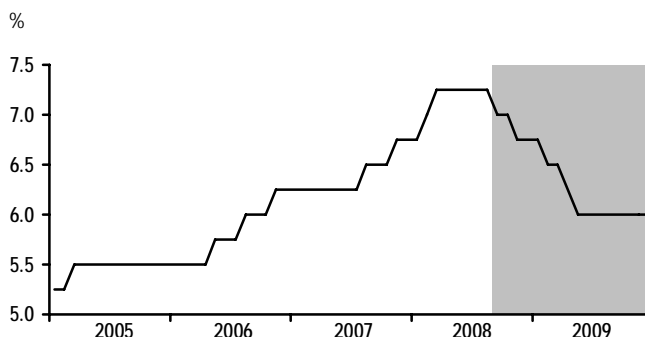
### RBA minutes point to September rate cut

The minutes of the RBA's August Board meeting, after which officials signaled clearly that an easing cycle was about to begin, were more equivocal than many expected. A 25bp rate cut on September 2 remains more likely than not but, by presenting an unexpectedly nuanced assessment of the growth and inflation dynamics, Tuesday's minutes indicate that there remains "considerable uncertainty" about the outlook and that there are "powerful forces pulling in opposite directions." We continue to look for the first 25bp rate cut early next month, but these minutes hint that this is far from a "done deal." Also, the minutes indicate that the 50bp rate cut talked about in some circles is very unlikely.

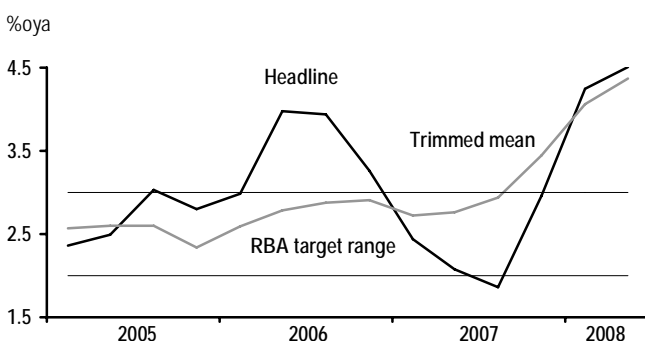
The RBA is balancing two key policy considerations—elevated inflation and weak domestic growth, owing mainly to tight financial conditions. Also, there is uncertainty about how the opposing forces at work in the economy will play out. The more nuanced nature of Board members' discussions back in early August, relative to the clear message sent in the statement on the day of the Board meeting, cautions against the market getting too far ahead of itself and pricing in more assertive easing into 2009. We still forecast further easing by mid-2009, but the dominant risk appears to be that the RBA will move less aggressively than we anticipate. Either way, the persistence of elevated inflation means that the policy rate will likely be on the tight side of neutral even when the easing cycle ends.

The RBA believes that the weakness in the domestic economy will persist. A second 25bp ease, therefore, could come as early as October, but this will depend on the health of the data flow and the behaviour of the Aussie banks. The

Australia: RBA cash target rate



Australia: headline and core CPI



flow of the economic data should show that the economic activity has softened but, already, consumer confidence has rebounded and anecdotes from retailers indicate that July's retail sales were decent, helped along by healthy sales of flat screen TVs ahead of the Olympic games. The uncertainty about the outlook, though, means the RBA will likely move in measured steps, with each step highly dependent on developments along the way.

That said, the minutes again indicate that RBA officials now place more weight on the evidence of weakness in the domestic economy than on elevated inflation. Indeed, the official RBA forecasts in last week's quarterly statement now show inflation peaking at 5% late this year—double the midpoint of the RBA's 2-3% target range and up from the previous forecasts. Yet, officials have indicated that the case for the RBA to move to a less restrictive policy stance has strengthened. Officials seem to be creating some "wriggle room" to focus on growth rather than inflation by emphasizing that the RBA targets inflation "on average over the cycle," and that inflation will return to target "over time."

Unsurprisingly, the tone of the minutes followed closely the tone of the RBA's recent commentary. The RBA believes that

there are signs of a loss of momentum in the domestic economy with the labour market softening (despite a bounce in employment in July), demand for credit slowing, and consumer and business confidence weakening. On the flipside, though, the terms of trade remains an important source of support for the economy. Also, consumers just received another round of generous personal income tax cuts. These factors, and the persistence of elevated inflation, argue against a precipitous drop in the cash rate. In particular, officials raised the risk of high inflation being reflected in wage growth, although wage demands thus far have been contained.

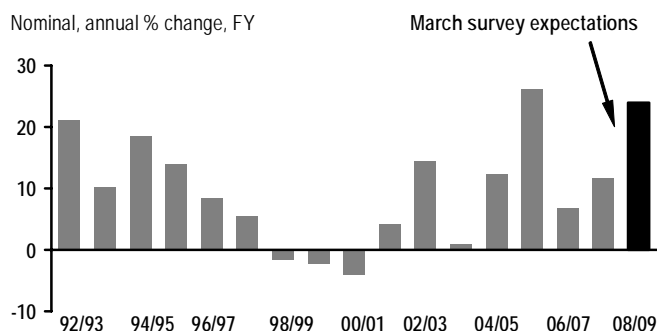
It now looks more likely than not that the Aussie banks will pass on the RBA's first 25bp rate cut in full. The political pressure on banks has stepped up a notch, but the decision to pass on the rate cuts will have more to do with the competitive tension in the home mortgage market than the threat of retribution. The demise of some nonbank mortgage providers means that the competition in the home loan market is not as intense as before, but the market remains competitive. Indeed, there is a possibility now that one of the big banks will lower its mortgage rates more than 25bp after the RBA's first rate cut, which is sure to prompt a response from other banks.

## 2Q business investment likely rebounded

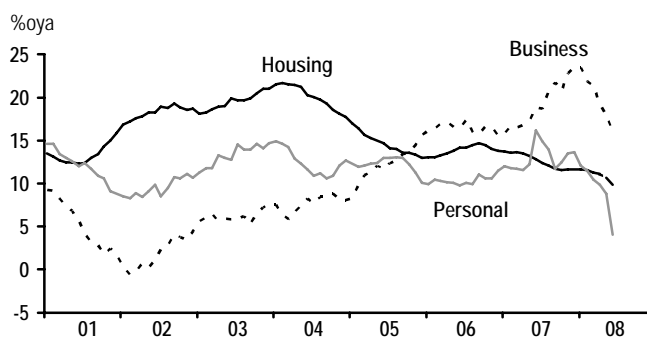
Firms probably boosted their business investment spending 4.0%q/q in 2Q, after spending unexpectedly dropped 2.5% in 1Q. Spending in mining and infrastructure likely dominated the rise in the March quarter as firms otherwise focused on the domestic economy probably trimmed spending. High interest rates and energy prices, in particular, weighed on business sentiment in the quarter, as did the cascading bad news on the global financial system. The rebound in spending in 2Q partly was payback for the weak first quarter, but also reflected the ongoing capacity expansion in export industries.

More importantly, however, firms probably maintained their investment spending plans for the year ended June 2009. In the last survey released back in May, managers estimated that they would boost capex 24% in the current fiscal year, down only slightly from the 25% rise expected in the previous survey. To maintain this impressive growth rate, the third spending estimate for 2008-09 needs to print at A\$94 billion. The final estimate for 2007-08 probably will come in at A\$86.3 billion. The latest Access Economics survey of investment plans shows a pipeline of spending worth more than A\$600 billion—the pipeline has expanded 19% over the past year.

### Australia: business investment



### Australia: private sector credit aggregates



## Credit growth likely remained weak in July

Credit outstanding to the private sector should have grown a mild 0.4% m/m in July, the same as in the previous month, remaining subdued amid still-tight monetary conditions. Annual growth in credit probably fell to 11% oya, significantly lower than the 16% rate at the start of the year. High interest rates and low consumer confidence, which has dived to recession-like levels, are major drags on housing and personal credit growth, while businesses also are pulling back on borrowing, presumably as some firms postpone investment plans. Housing, personal, and businesses credit should have remained subdued in July, growing 0.5% m/m, -0.1% m/m and 0.4%, respectively.

## Data releases and forecasts

Week of Aug 25 - 29

Wed	Construction work done			
Aug 27	Seasonally adjusted			
11:30am	3Q07	4Q07	1Q08	2Q08
(%q/q)	3.5	-0.8	2.3	<u>2.2</u>
(%oya)	9.2	3.7	3.3	<u>7.4</u>

Thu **Private new capital expenditure**

Aug 28 Seasonally adjusted

11:30am

	3Q07	4Q07	1Q08	2Q08
(%q/q)	-6.3	7.3	-2.5	<u>4.0</u>
(%oya)	9.1	17.6	4.6	<u>2.0</u>

The forward looking expectations for business investment are the most important parts of the capex survey. In the last survey released back in May, managers estimated that they would boost capex 24% in the current fiscal year, down only slightly from the 25% rise expected in the previous survey. To maintain this impressive growth rate, the third spending estimate for 2008-09 needs to print at A\$94 billion. The final estimate for 2007-08 needs to come in at A\$86.3 billion.

Fri **Private-sector credit**

Aug 29 Seasonally adjusted

11:30am

	Apr	May	Jun	Jul
(%m/m)	0.4	0.5	0.4	<u>0.4</u>
(%oya)	14.1	13.3	11.7	<u>11.0</u>

**Review of past week's data**

**WMI leading index**

Seasonally adjusted

	Apr	May	Jun
(%m/m)	0.4	0.0	— 0.1

**Sales of new motor vehicles**

Units, seasonally adjusted

	May	Jun	Jul
(%m/m)	<del>-1.5</del> -2.7	<del>1.0</del> 0.8	— -3.4
(%oya)	<del>2.4</del> 1.9	<del>1.4</del> 1.3	— -4.1



## New Zealand

- **Business confidence likely to remain weak in August**
- **Pipeline price pressures were significant in 2Q**
- **Inflation expectations should remain high**

In New Zealand, the 2Q PPI print indicated that pipeline price pressures remain significant; this increases the risk that RBNZ officials may rethink the length and depth of the easing cycle on which it recently embarked. Our forecast calls for a gradual and steady decline in the OCR to 6.25% by mid-2009. This week should show that inflation expectations, measured by the RBNZ, remained elevated in 3Q, with business managers expecting inflation at the top end of the RBNZ's 1-3% oya target range in two years' time.

### NZ pipeline price pressures intensified

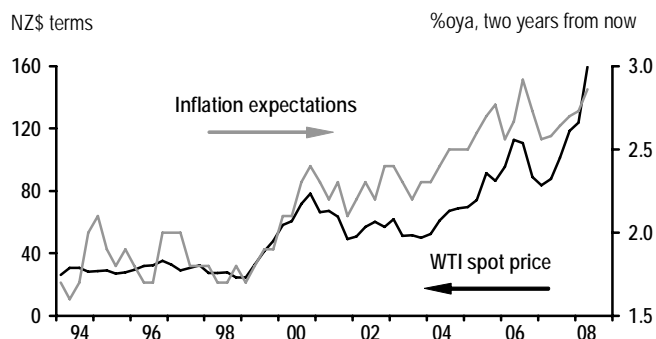
Pipeline price pressures continued to build in New Zealand in 2Q. Producer input prices surged 5.6%q/q, more than double the 2.3%q/q spike recorded in the March quarter and the largest rise since 1980. Output prices also grew at a much faster rate than expected, rising 3.5%q/q, the largest rise since 1985, and up from a 1.8% rise previously. The significantly faster rate of growth in input prices over output prices confirms that producers are still finding it difficult to pass rising costs on to consumers, leaving profit margins squeezed. This is not surprising given the sharp slowdown in domestic demand in recent months.

The main driver in the rise in output prices was the electricity generation and supply component, up 30.9%q/q—the largest rise since the series began; this was owing to lower lake levels in the hydro-generation sector, according to the stats agency. The surge in input prices also was driven by the electricity generation and supply index, up 50.8%q/q. Again, lower lake levels owing to the drought, were blamed for the rise in costs for electricity generation. Higher electricity generation costs have led to increases in spot prices in the wholesale electricity market, which have pushed producer prices higher.

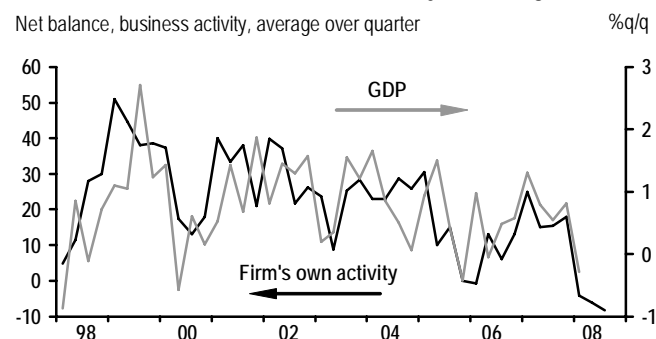
### RBNZ inflation expectations still high

In the September quarter, inflation expectations, as measured by the RBNZ, should remain elevated. In the June quarter, the RBNZ's survey of 80 business managers showed that inflation is expected to average 2.9% in two years' time, compared to 2.7% in the 1Q survey, remaining at the top end of the central bank's target range.

New Zealand: RBNZ inflation expectations and crude oil price



New Zealand: NBNZ business outlook survey and GDP growth



Still-elevated inflation expectations are not surprising given that inflation has yet to peak, according to our and the RBNZ's forecasts. The RBNZ expects inflation to peak at 5% oya in 3Q. Given the recent surge in producer prices and the sharp decline in the NZ dollar, however, our forecast calls for headline CPI to peak at 5.2% oya in 4Q and to remain above target until the end of 2009.

### Kiwi business confidence still weak

The NBNZ business confidence survey likely improved slightly in August to -40 from -43.2 in July. The headline index will suggest that a net 40% of respondents expect business conditions to deteriorate over the coming year. The improvement will come in the wake of the RBNZ's rate cut. The RBNZ cut the OCR 25bp in July from a record high 8.25%.

More important to watch will be the reading of firms' own activity expectations, which dropped sharply in July to -8.2 from -4.0 in June; this points to a contraction in GDP growth in 2Q (chart). Only 16 negative readings in firms' own activity expectations have been recorded over the last 20 years. Corporate profitability continues to suffer amid high interest rates and tighter credit conditions, weighing on firms' own activity

expectations. Monetary easing should help support economic growth in late 2008, helping to pull the struggling economy out of recession. Our forecast calls for the RBNZ to cut interest rates another 75bp this year in September, October, and December, and further rate cuts are expected next year, taking the key rate 6.25% by mid-2009.

## NZ trade deficit likely widened in July

The trade deficit should have widened to NZ\$425 million in July from NZ\$223 million in June, the fifth straight monthly deficit. Export growth should have remained supported by the weaker NZD and higher dairy and oil exports; the latter reflecting increased production from the Tui oil field (which began in July) as well as the elevated prices of dairy products and crude oil. On the other side of the ledger, import growth should have slowed from a year ago on the back of weaker domestic demand, although it likely retained upside support from imports of petroleum and products, which again were buoyed by elevated crude prices.

## Data releases and forecasts

### Week of Aug 25 - 29

Tue Aug 26 10:45am	Trade balance	Apr	May	Jun	Jul
	Not seasonally adjusted				
	Trade balance (\$NZ mn)	-288	-168	-223	<u>-425</u>
	Exports (NZ\$ mn)	3831	3742	3585	<u>3550</u>
	Imports (NZ\$ mn)	4119	3910	3808	<u>3975</u>

Tue Aug 27 3:00pm	RBNZ inflation expectations	4Q07	1Q08	2Q08	3Q08
	Not seasonally adjusted				
	(%q/q)	2.7	2.7	2.9	—

Wed Aug 27 3:00pm	NBNZ business confidence	May	Jun	Jul	Aug
	% balance of respondents	-49.7	-38.7	-43.2	<u>-40.0</u>

Fri Aug 29 10:45am	Building consents	Apr	May	Jun	Jul
	Not seasonally adjusted				
	(%m/m)	51.4	-30.3	-17.6	—
	(%oya)	33.2	-28.8	-47.1	—

## Review of past week's data

Producer price index	4Q07	1Q08	2Q08	3Q08
nsa				
(%q/q)	<del>1.5</del>	1.2	<del>1.8</del>	1.9
(%oya)	<del>4.0</del>	3.8	6.1	<del>6.3</del>

Visitor arrivals	May	Jun	Jul	Aug
Not seasonally adjusted				
Total (%m/m)	9.1	-1.4	—	2.1

Net permanent immigration	May	Jun	Jul	Aug
Not seasonally adjusted				
Monthly (000s)	-1.3	-0.6	—	0.7
12 month sum (000s)	4.9	4.7	—	5.2

Credit card spending	May	Jun	Jul	Aug
Seasonally adjusted				
(%m/m)	<del>-1.2</del>	-0.9	<del>-0.7</del>	-0.4
(%oya)	5.9	<del>3.3</del>	3.4	—

## Global Essay

- **Significant and broad-based downward pressure on global growth**
- **Key test is whether support from lean US nonfinancial firms and EM demand will limit downward momentum**
- **The major energy price drag on global consumption should turn to support in 4Q08**
- **Asian tech activity is poised for a significant correction**

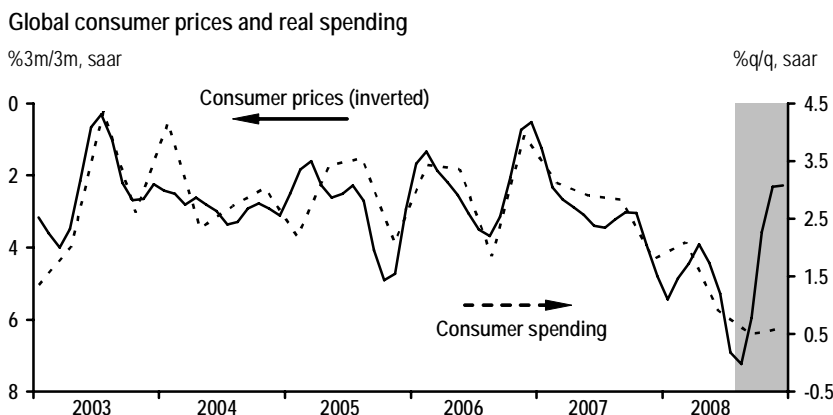
### It's testing time again

Global growth turned sharply weaker around midyear and there are good reasons to expect growth to remain subpar for some time to come. There is significant pressure on European and Asian firms to cut back in response to a profit margin squeeze and an unwanted rise in inventories during 1H08. What's more, there is little in the way of global policy stimulus to cushion the blow. Tightening credit conditions are offsetting the beneficial effects of the past year's 200bp drop in global real policy rates. Fiscal policy remains modestly accommodative, largely driven by EM governments. But the principal policy dynamic currently at work is the fading of the benefits from US tax rebate checks at a time when incomes continue to be compressed by high inflation. This week's July personal income report is likely to show a second consecutive fall in real consumption, setting the stage for the first quarterly contraction by US consumers since 1991.

Having made substantial downward revisions to the outlook in recent weeks, we now anticipate global growth averaging about 1.5% (q/q, saar) through early next year—not far above the 1% threshold that has typically represented the dividing line between recession and expansion. Concern that the glo-

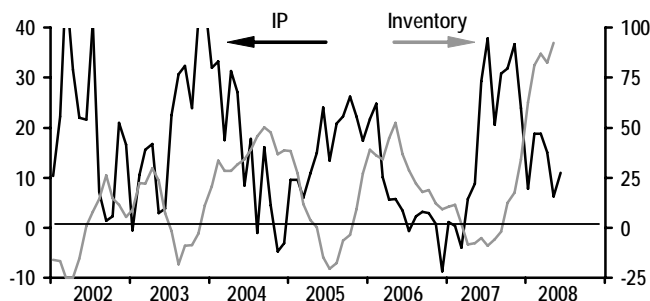
bal economy could disappoint further and enter an outright recession remains uncomfortably high. In the coming weeks, we will enter a testing mode, watching the data to gauge how the elements central to our view—a global economy that skirts recession and begins to recover early next year—are tracking.

- **The US rotates toward stagnation.** As the US economy moves through the summer, consumption is contracting and export gains look set to moderate. GDP growth is expected to slow—from an estimated 1H08 pace of 1.7% to 0.8% in 2H08. If we are right, firms will not intensify spending and hiring cutbacks. Along with a significant boost to 2H08 growth as a period of aggressive destocking ends, this behaviour is expected to prevent the economy from contracting. In tracking this view, high-frequency indicators from the manufacturing sector, business surveys, and labor markets should point to weakness but not drop to their levels in either of the past two recessions.
- **Asian production falls while domestic demand rises.** Emerging Asian industry (ex China) will likely contract in the face of weak G-3 demand, rising labour costs, and a significant inventory correction in high-tech sectors. However, regional domestic demand is expected to prove resilient in the face of this adjustment, led by sustained strong growth from China and supportive policies elsewhere. Overall, Chinese growth should remain above 8% annualized, providing a solid base for sustained growth elsewhere in the region.
- **Oil has taken and will now give.** Sharp movements in global inflation have aligned closely with consumption spending in the past, and we are now moving through the most dramatic up and down move in inflation during this expansion.



### EM Asia tech IP and inventory

%6m, saar, both scales



A key factor behind the slowdown in global growth this year was the spike in oil prices. This sharply squeezed purchasing power—slowing growth of consumption spending to a tepid 1% pace in the middle quarters of the year. Now, global inflation is expected to slide from a 6% pace in 3Q08 (q/q, saar) to a 2% pace in the fourth quarter.

The most significant risk is that we are underestimating downward growth momentum and the feedback loop between elevated US financial market stress and the real economy. However, the risk profile will change materially if the US and global expansion can be sustained in the coming months—notably because the beneficial effects of moderating inflation could provide a more significant global lift than we currently forecast.

### Global high-tech downshifting rapidly

Shifts in global demand growth are almost always quickly transmitted to the industrial sector. Developments in 2008 have played to script. As global growth slid below trend over the course of 1H08, growth in the industrial sector gradually came to a halt; output then posted back to back monthly declines in May and June. The lion's share of the July IP data will arrive in the next two weeks. These data are likely to confirm that global output remains in a modest contraction phase of about 1% at an annual rate. The global business surveys are pointing in this direction. Our global manufacturing PMI edged down another half point to 49 in July, while the early August surveys from the Euro area and regional Fed banks point to a similar reading in August.

The industry slowdown is broadly based, although with important variations by region and sector. Output is falling in the developed world, including each of the G-3 economies.

Production also has downshifted in the EM. China's growth has held up better, but IP growth in the EM excluding China slowed to just 2.3% in June on a 3m/3m annualized basis. Across the EM, Asia (with and without China) and Europe have fared better than Latin America, where output is falling.

The coming months should bring a further moderation in EM IP growth as weakness in the developed world continues to feed through to the EM group with the customary lag. EM domestic demand growth also is moderating. In particular, activity in EM Europe is likely to be hit by the full brunt of the growth slowdown in Western Europe. A slowdown in oil-rich Russia, which has served as an engine of domestic demand for others in the region, also will play a role.

In EM Asia the main concern is the unfolding slowdown in global high-tech activity. Global tech output remained resilient in early 2008, continuing to grow at a double-digit pace even as other aspects of industry were slowing. This subsequently gave way to a sharp deceleration, however, as global capex and consumer spending lost momentum in 2Q.

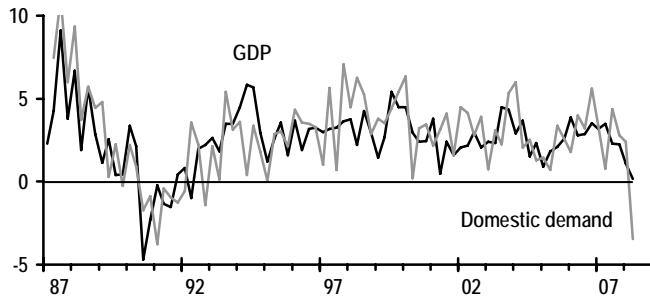
Asian tech output has moderated too, but it has not kept pace with the drop in demand, resulting in stockbuilding in Taiwan and especially Korea (and also Japan). Continued weak global demand, combined with a regional buildup of inventory, points to a further downturn in regional tech activity. This week's July IP releases in Korea, Taiwan, and Japan will be scrutinized for signs of this adjustment.

### UK alarm bells are ringing

UK GDP growth stalled in 2Q, but what's alarming is the message on demand growth alongside the revised data. Private consumption, and business and other investment each fell, and the 3.5% annualized rate of decline in domestic demand matched lows not seen since the depths of the early 1990s recession.

Although some of the weakness in 2Q consumption was payback for 1Q strength, the trajectory of retail sales into 3Q and the forthcoming increases in energy bills point to continued consumption weakness. Households may come under added pressure from a weaker labour market, as recent indicators suggest that the corporate adjustment is spreading from capex to employment. While the magnitude and longevity of the spike in CPI inflation remain a concern for the MPC, the severity of the downturn in demand reinforces the case for a rate

UK real GDP and domestic final demand  
%q/q, saar



cut this November.

### CEEMEA growth also shifting down

This week brought further evidence of a downshift in manufacturing growth in Central and Eastern Europe. July IP releases for Poland and Russia both came in below expectations as the global slowdown and rising costs weighed on production. In Poland, we have removed the final 25bp rate hike from our forecast (previously expected in September) after the MPC minutes revealed a clear shift in focus from upside inflation risks to growth concerns. The high correlation between IP

releases in the region bodes negatively for Czech and Hungarian IP data out over the next two weeks.

For Russia, we have downgraded our economic growth outlook roughly half a percentage point for both 2008 and 2009 (to 7.4% y/y and 6.5%, respectively) following a significant slowdown in IP and investment activity. We also expect consumption growth to cool down amid higher interest rates and a slowdown of real income growth. At the same time, the global slowdown and fall in commodity prices make it more probable that Russia will experience a negative terms-of-trade shock next year. Weaker Russian demand will have a knock-on effect for the rest of Europe via trade linkages.

Increasing headwinds are likely to intensify the slowdown in South Africa too. We now expect the SARB to cut rates a cumulative 200bp in 2009, rather than the 150bp anticipated earlier. At face value, last week's GDP report for 2Q08 pointed to a strong performance, yet softer global commodity prices and subpar growth in key trading partners will worsen the drag from net imports on growth well into 2009. We have marked down our 2009 GDP growth forecast to 2.7% y/y (from 3.2%) despite the eventual positive impetus from additional monetary easing.



## JPMorgan View - Global Markets

### In the eye of the storm

- Financial markets are largely unchanged on the week, with the exception of credit spreads that continue to widen. Day-to-day volatility remains high. This is more a reflection of poor August liquidity than of significant opinion changes among investors.
- Market participants admit to high uncertainty and confusion, but the majority subscribe to, and are largely positioned for, the view that we are in the midst of a global economic slowdown/recession. Our own forecasts show a slowing in growth in developed economies similar in depth to, though shorter in length than, the ones of the early 1990s and early this decade. These periods of economic “slump” did not see outright contractions of activity—unlike in the early 1980s—but were bad enough to cause bear markets in riskier assets.
- The main issue vexing market participants now is where we are in the global slump and when one should sell bonds and reenter risky markets. By historical standards and economic logic, equity and credit markets should rebound once uncertainty starts receding. That is typically not until the later stages of the slump. We find it too dangerous to re-enter risky markets now, as there remain significant uncertainty and downside risks around economic forecasts, focused around the question of whether corporates will move from caution to outright fear, and will consequently slash spending. If they do, then we are only at the start of a severe economic correction. We continue to monitor closely signals on corporate spending on capital and people.
- The second quarter of this year saw a significant shift in economic weakness from North America to Europe and Japan. This was the basis of so-called growth-rotation trades, where investors switched recession trades (long duration and steepeners, plus short equity, credit, and the currency) from the US and Europe. These trades have become consensus positions at a time when economic data will likely start showing a return of weakness to the US as the impact of monetary, fiscal, and trade stimulus loses some of its steam. We thus see the US joining Europe and Japan in stagnation, if not under-performing them. We therefore advise taking profit on these growth rotation trades, in particular long USD, long Bunds/USTs, and overweight US equities.

#### Fixed income

- Bonds rallied earlier last week, but then sold off today on bearish comments out of Jackson Hole. We remain long du-

#### 10-yr government bond yields

%oya	Current	Sep 08	Dec 08	Mar 09	Jun 09
United States	3.87	3.85	4.05	4.30	4.30
Euro area	4.22	4.10	3.90	3.80	3.80
United Kingdom	4.58	4.40	4.20	4.20	4.20
Japan	1.47	1.50	1.60	1.60	1.80

#### Equities

	Current	YTD return (local currency)
S&P	1292	-11.8%
Topix	1216	-16.2%
FTSE 100	5482	-14.2%
MSCI Eurozone	180	-23.4%
MSCI Europe	1204	-19.4%

#### Credit markets

	Current	Dec 08
US high grade (bp over UST)	290	230
US high grade (bp over swaps)	194	168
Euro HG corp (bp over swaps)	90	65
USD high yield (bp vs. UST)	801	800
EMBIG (bp vs. UST)	321	250

#### Foreign exchange

	Current	Sep 08	Dec 08	Mar 09	Jun 09
EUR/USD	1.48	1.47	1.47	1.45	1.42
USD/JPY	110	108	110	112	115
GBP/USD	1.85	1.84	1.84	1.81	1.80

#### Commodities

	Current	Quarterly average	
		Sep 08	Dec 08
Gold (\$/oz)	826	915	900
Copper(\$/m ton)	7973	8800	8000
Corn (\$/Bu)	6.12	6.15	6.30

Source: JPMorgan, Bloomberg, Datastream.

ration, largely in 2s and 5s, across global markets, as risk is biased to central banks having to ease more, or hike less, than is currently priced in. We are less positive on the longer end of the curve, especially in the US where supply pressures from federal and local governments as well as Agencies remain intense. We accordingly stay in steepeners in the US (5s10s).

- In line with our fear that the growth rotation trade (from US to Europe) is near an end, it makes sense to take profit on the long European duration against the US. Long duration positions are at extremes in Europe but very light in the US.
- Spreads over government paper have come in slightly in a number of markets but remain near historical wides. Funding problems for banks have not gone away and investors remain wary about the outlook for the Agencies. We are more optimistic, if only because the government has few options



left but to support the Agencies outright. We therefore stay medium-term positive and overweight on MBS and agency debt even as we accept that spreads will stay volatile in coming weeks.

## Equities

- Global equities are in the middle of the range they have traced over the past month. On the negative side, the economic and financial news is depressing and is likely to remain so for the next few months. On the positive side, many investors have seen this economic slump coming and have been already positioned for it for some time. World equities (MSCI World free) are 20% off their peak (Oct 07) and could be said to have paid a recession penalty already. This does not mean that equities can't go lower (remember that the last recession saw a 50% drop in stock prices). But, together with the ubiquity of underweight positions, this does suggest that we are not far from the cycle low.
- Timing the bottom in equities will depend on when investors feel that the light at the end of the tunnel is in sight. Our fear is that with economic news deteriorating in coming months—as weakness widens again to the US and then EM exporters—the lows so far may not be the cycle lows. There remain significant downside risks over the next 1-2 mths. We don't advise being outright short—as the end-of-recession rally will be swift and violent—but at the same time advise waiting 1-2 mths before going long. Technically, October, right before the US elections, beckons as a good time to go long again.
- EM stocks have significantly underperformed this month as investors are convinced that the global economic slump will soon bring down the emerging economies. We see slowing in EM, especially in manufacturing and among exporters. But at the same time, we see strong evidence that domestic growth, especially in Asia, will keep supporting EM growth and prevent the severe slump that investors are gearing up for. We thus stay overweight EM, focused on Asia, and domestic companies rather than exporters, and commodity producers. Within EM, we are overweight China and Mexico.

## Credit

- Credit is the poor cousin among the riskier markets, with spreads at new highs in a number of sectors. This is because the current crisis is at its core a credit crisis and its resolution requires an avalanche of debt refinancing that investors are having trouble absorbing. From a medium-term point of value, high-grade spreads fully price in a recession. But high-yield spreads are not fully there yet as default rates remain benign.

- We see few catalysts to push spreads tighter in coming weeks and stay bearish in credit overall. Given that investors appear slightly overweight currently, HG is susceptible to forthcoming heavy supply, while HY faces the headwind of fast-rising downgrade and default rates.

## Foreign exchange

- While holding to a bullish dollar view medium term, we have progressively reduced our dollar longs in the past two weeks, aware that USD was becoming stretched relative to cyclical drivers, proxied by the decoupling from interest rate differentials. That said, we did retain a core long position, primarily versus AUD, on the basis that speculative USD positions did not appear unduly stretched. There was also the potential for medium-term players (corporates, real-money) to hedge more aggressively against a trend reversal in the dollar. Because of this we gave back a part, but fortunately only a very small part, of our accumulated long dollar profits as the greenback succumbed to profit-taking last week.
- The risk over coming weeks is for further consolidation or modest retracement in the dollar and we therefore close our remaining G-10 dollar long versus AUD. The reasons: 1) speculative positions have become more stretched—IMM USD longs were up 40% in the past week to \$13.4bn, the most since end-2005; 2) European data are no longer undershooting expectations aggressively, and the prior collapse in European data vis-à-vis the US was probably the key driver of the sharp slide in EUR/USD. 3) US financial concerns are once again in focus as uncertainty over the GSEs persists and the broker-dealer earnings season in mid-September approaches; 4) USD's interest rate support is ebbing as 2-yr Treasury yields hit their lowest level since May and spreads versus G-10 widen anew.
- In all, the dollar has lost much of its fundamental momentum for now. We are likely to want to buy a dollar dip but it will need to be deeper than we have so far seen. After all, the dollar remains expensive relative to rate spreads. For now, the sideline is the best place to be as the dollar retreats into a choppy consolidation phase.

## Commodities

- We still see base metals trading down in the short term, waiting for more detailed information on how China's economy evolves into 4Q. But downside support is solid in nickel, lead, and zinc due to near-market marginal production costs. Gold has modest upside risk, toward \$850-\$870/oz, supported by physical buying, but this is likely to cap this year.

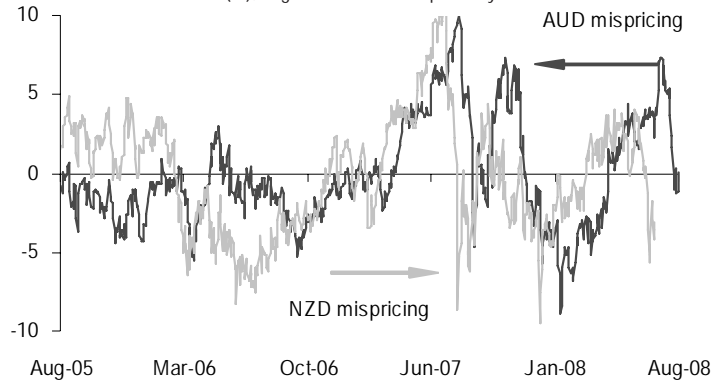
## AUD and NZD Commentary

- **The dollar pause is likely to continue as financial market concerns in the US keep US yields low; take profits in short AUD/USD. Hold short AUD/NZD which still looks too high relative to interest rate differentials**
- **Technical: Short term corrections continue above the August lows for both AUD/USD and NZD/USD**
- The recent USD rally has stalled as concerns about the health of the US financial system continue. US financial stocks ended the week lower whilst Freddie Mac and Fannie Mae share prices continued to slide. The US release schedule was light but there was further evidence of the weak state of housing. Yield spreads consequently moved against USD. JPY was the main beneficiary of equity market weakness despite another downgrade in the economic assessment by the BoJ. Sentiment towards GBP remained bearish though retail sales printed strongly. The rebound in commodities lent support to AUD and NZD, the latter performing strongly as yield spreads moved in its favour.
- Our medium-term view towards USD remains unchanged and we continue to look for steady appreciation over the coming year as the rotation in growth sees the Fed begin to normalise rates whilst other major central banks ease. Over the near-term, however, we see some potential hurdles for USD which suggest that a period of consolidation is likely. In last week's FX Markets Weekly, we took profits on our long USD position versus EUR based on the misalignment of the currency pair relative to yield spreads. Rate spreads moved further against USD over the past week, with the US giving up nearly 15bps versus its G7 counterparts. The catalyst for falling yields has been ongoing concerns over the health of the US financial. As a result of recent developments, we have now moved to neutral USD exposure.
- We still see downside risks to commodity currencies as the market evaluated the depth of the economic woes in NZ and Australia and the extent to which the respective central banks will need to ease rates. However, AUD/USD is now fair relative to rates and NZD/USD is too low relative to rate differentials. We are now neutral on the AUD and NZD relative to USD but likely holding short AUD/NZD.

### Technical analysis

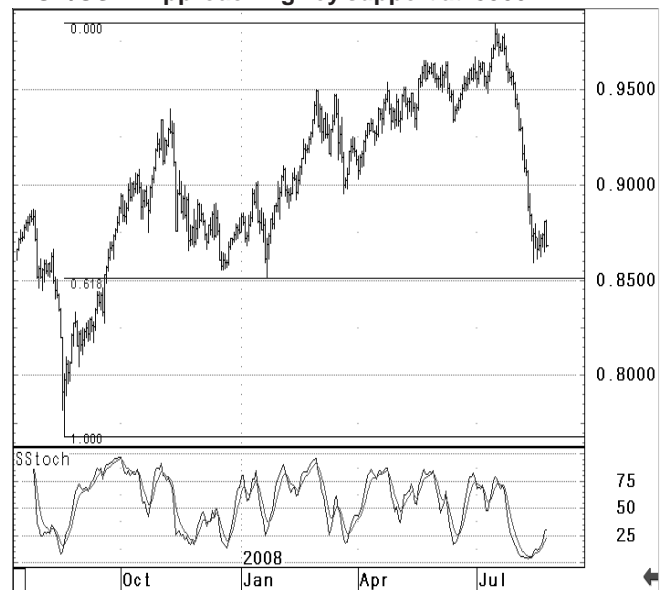
- The short term corrective phase continues to develop for both AUD/USD and NZD/USD following the reversal from the August lows. This is in line with the bounce in gold, crude, and other commodities. For AUD, the bounce from the 0.8600 support area is likely to continue to for the short term,

**AUD/USD now fair given rate differentials; NZD/USD too low**  
 Residual, or "mispricing," of AUD/USD and NZD/USD relative to 3-mon, 1-yr forward rate differentials (%); regression over the past 3 years



- but the corrective action has so far failed to suggest a base is in place. There is still risk of additional short term weakness that can allow for a closer test of key support in the 0.8500. This area represents the January '08 low and the 61.8% retracement from the August '07 low and where prices are more vulnerable to a deeper retracement of the decline from the July peak. Resistance starts at .8815 and .8950.
- NZD/USD maintains the short term corrective phase after effectively holding key support at the .6820 trendline from the 2001 cycle low. Still For the short term picture, the action should maintain a two-sided bias above this key support area. Resistance enters at .7220 and .7335 levels, which will maintain the short term downside bias. Breaks of the .6820 low would target deeper in the 0.6700/0.6640 zone, which includes the August '07 low and where prices are likely to sustain a deeper correction of this fall from the year's high.

### AUD/USD - Approaching key support at .8500



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Fri Aug 22 2008 11:40:04

## 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	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	2Q08	4Q08	2Q09	4Q09
<b>The Americas</b>														
United States	2.0	1.5	2.0	0.9	1.9	0.5	1.0	2.0	3.0	3.0	4.3	4.8	3.2	1.9
Canada	2.7	1.1	2.4	-0.3	0.8	1.5	2.3	2.5	2.8	3.0	1.9	2.4	1.7	1.9
Latin America	5.3	3.8 ↓	3.6	1.6	3.2 ↓	3.4 ↑	4.0 ↓	3.2	3.8	3.7 ↑	7.5	8.2	7.6	6.5
Argentina	8.7	6.5	3.0	2.6	6.1	6.1	6.1	2.0	1.6	0.0	9.1	9.1	8.9	9.8
Brazil	5.4	4.4	3.8	2.9	3.0	4.0	4.0	3.8	3.5	3.4	5.6	6.6	6.6	5.0
Chile	5.1	3.5	3.5	5.8	9.5 ↑	-2.0 ↓	0.0 ↓	4.0	5.0 ↑	3.0 ↑	8.9	8.4	6.8	4.5
Colombia	8.2	3.7 ↓	3.6 ↓	-3.7	3.8 ↓	5.8 ↑	6.2 ↑	1.2 ↓	2.1	2.9	6.4	6.9	4.5	4.0
Ecuador	2.0	2.5	2.5	2.0	1.5	1.0	1.0	2.5	3.5	4.0	9.1	9.8	5.3	4.5
Mexico	3.2	2.4	3.5	2.1	1.0	2.0	3.0	4.1	4.1	4.5	4.9	5.6	5.0	3.9
Peru	9.0	8.5	6.1	7.5	11.2	3.0	2.3	2.6	13.5	9.0	5.5	4.8	3.5	3.1
Venezuela	8.4	3.5	3.5	-12.5	4.5	7.5	10.0	-2.5	2.5	3.5	31.0	33.6	32.5	30.5
<b>Asia/Pacific</b>														
Japan	2.0	0.7	0.6	3.2	-2.4	-0.5	0.2	0.7	1.2	1.7	1.4	2.0	1.6	1.0
Australia	4.3	2.8	2.6	2.5	1.3	2.6	3.2	3.2	2.0	2.4	4.5 ↑	4.6 ↑	3.2 ↓	3.0 ↓
New Zealand	3.1	0.8	1.8	-1.1	-0.2	-0.1	0.3	2.2	3.6	2.5	3.3	3.9	4.0	3.4
Asia ex. Japan	8.8	7.2	7.2	8.5	6.2 ↓	5.7 ↓	6.3	7.2	7.6	7.8	7.0	6.3	4.5	4.6
China	11.9	10.1	9.6	11.7	11.5	8.7	9.0	9.5	10.0	10.0	7.8	5.3	4.5	5.1
Hong Kong	6.4	4.0	4.5	8.2	-5.5	0.8	5.2	5.5	6.0	6.5	5.7	3.1	2.4	3.6
India	9.0	7.0	7.5	8.8	4.8	6.6	6.3	7.5	7.0	7.8	7.8	8.9	5.8	5.7
Indonesia	6.3	5.6	4.7	6.0	5.4	5.0	4.5	4.5	5.0	5.0	10.1	14.2	8.3	6.8
Korea	5.0	4.4	4.8	3.3	3.4	3.0	4.0	5.0	6.0	5.5	4.8	5.0	3.4	3.1
Malaysia	6.3	4.7	4.5	6.4	2.4	-1.2	0.8	6.6	7.0	7.4	4.9	7.1	4.9	2.3
Philippines	7.2	3.2	4.3	4.3	2.0	1.0	2.0	5.0	5.5	6.0	9.7	8.0	4.3	3.7
Singapore	7.7	4.0	4.3	15.7	-6.0	6.6	4.1	4.5	4.5	5.3	7.5	4.7	1.2	2.8
Taiwan	5.7	3.9 ↓	4.4 ↓	3.0	1.3 ↓	2.5 ↓	3.8	4.8	5.2	5.5	4.2	2.1	2.8	2.4
Thailand	4.8	4.2	4.6	5.6	1.0	0.0	1.0	2.0	3.0	5.0	7.5	11.3	6.5	5.0
<b>Africa</b>														
South Africa	5.1	3.3 ↑	2.7 ↓	2.1	4.9 ↑	0.9 ↓	-0.4 ↓	2.2 ↓	3.5 ↑	5.6 ↑	11.6	13.6 ↑	8.7 ↑	6.6 ↑
<b>Europe</b>														
Euro area	2.7	1.2	0.4	2.9	-0.8	-0.5	0.0	0.5	0.7	1.5	3.6	3.5	2.7	2.0
Germany	2.6	1.6	0.7	5.2	-2.0	0.5	0.5	0.8	1.0	1.5	3.0	2.7	1.9	1.7
France	2.1	1.0	0.7	1.6	-1.2	0.0	0.5	0.8	1.0	1.5	3.7	3.5	2.1	1.8
Italy	1.4	-0.1	0.1	2.0	-1.1	-1.0	-0.5	0.5	0.5	1.0	3.8	3.6	2.8	2.3
Norway	6.3	2.8 ↓	1.7 ↓	-0.2 ↓	3.9 ↑	1.5	1.2 ↓	1.5 ↓	1.5 ↓	2.0 ↓	3.2	4.2	4.2	2.2
Sweden	2.9	1.1 ↓	1.2 ↓	0.6	-0.1	1.2 ↓	0.8 ↓	0.8 ↓	1.5	2.0	3.9	4.4	3.3	2.2
Switzerland	3.1	2.0	1.0	1.3	1.0	0.5	0.5	1.0	1.5	1.5	2.7	2.7	1.7	1.1
United Kingdom	3.1	1.1	0.4	1.1	0.8	-1.0	-1.0	0.5	1.0	2.0	3.4	4.9	3.4	2.1
Emerging Europe	6.5	5.7 ↓	5.3 ↓	3.2	7.0 ↓	2.7 ↓	9.9	1.2	6.1 ↓	2.9 ↓	10.3	9.3	7.8	7.2 ↓
Bulgaria	6.2	5.2	5.5	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	6.6	4.8	3.5	3.6	3.6	5.0	4.5	2.5	2.0	3.0	6.8	5.9	2.8	3.0
Hungary	1.3	2.2 ↑	2.8	1.3	2.0	2.5	2.5	2.2	2.2	3.0	6.8	5.7	4.4 ↑	3.8 ↓
Poland	6.6	5.3 ↓	4.8	5.7	4.8	4.0	3.2	2.8	3.5	4.5	4.3	4.0 ↓	3.8 ↓	3.2 ↓
Slovak Republic	10.4	7.5	5.5	8.7	5.3	10.5	12.0	-5.0	6.0	8.5	4.5	4.3	3.2	3.8
Romania	6.0	7.0	4.0	...	...	...	...	...	...	...	8.7	6.4	5.8	5.5
Russia	8.1	7.4 ↓	6.5 ↓	0.9	10.1 ↓	1.0 ↓	16.0	0.0	9.0 ↓	1.5 ↓	14.8	13.2	11.3 ↓	11.0
Turkey	4.5	3.8	5.2	...	...	...	...	...	...	...	10.5	10.3	8.6	7.2
<b>Global</b>	3.5	2.3	2.2	2.6	1.4	1.0	1.7	2.1	2.8	3.0	4.4	4.6	3.4	2.6
Developed markets	2.4	1.3	1.2	1.8	0.3	0.0	0.5	1.3	1.8	2.2	3.5	3.9	2.8	1.8
Emerging markets	7.5	6.0 ↓	5.9	5.7	5.6 ↓	4.5 ↓	6.2 ↓	5.0	6.3 ↓	5.9	7.8	7.4	5.9	5.5

## Global Central Bank Watch

	Official interest rate	Change from			Forecast		Sep 08	Dec 08	Mar 09	Jun 09	Dec 09
		Current	Aug 07 (bp)	Last change	Next meeting	next change					
Global	GDP-weighted average	3.81	-90				3.83	3.85	3.87	3.93	4.24
excluding US	GDP-weighted average	4.67	20				4.69	4.72	4.63	4.49	4.47
Developed	GDP-weighted average	2.85	-129				2.84	2.82	2.82	2.91	3.29
Emerging	GDP-weighted average	7.72	67				7.82	8.00	8.09	8.09	8.05
Latin America	GDP-weighted average	10.08	127				10.39	10.88	10.86	10.84	10.47
CEEMEA	GDP-weighted average	6.30	121				6.40	6.53	6.61	6.36	6.02
EM Asia	GDP-weighted average	6.70	37				6.73	6.82	6.94	7.08	7.33
The Americas	GDP-weighted average	2.95	-264				2.99	3.04	3.25	3.65	4.49
United States	Federal funds rate	2.00	-325	30 Apr 08 (-25bp)	16 Sep 08	17 Mar 09 (+25bp)	2.00	2.00	2.25	2.75	3.75
Canada	Overnight funding rate	3.00	-150	22 Apr 08 (-50bp)	3 Sep 08	Jul 09 (+25bp)	3.00	3.00	3.00	3.00	3.75
Brazil	SELIC overnight rate	13.00	150	23 Jul 08 (+75bp)	10 Sep 08	10 Sep 08 (+75bp)	13.75	15.00	15.00	15.00	14.25
Mexico	Repo rate	8.25	100	15 Aug 08 (+25bp)	19 Sep 08	on hold	8.25	8.25	8.25	8.25	8.25
Chile	Discount rate	7.75	225	14 Aug 08 (+50bp)	4 Sep 08	4 Sep 08 (+25bp)	8.00	8.00	8.00	7.50	6.50
Colombia	Repo rate	10.00	75	25 Jul 08 (+25bp)	19 Sep 08	1Q 09 (-25bp)	10.00	10.00	9.75	9.75	9.50
Peru	Reference rate	6.25	150	7 Aug 08 (+25bp)	11 Sep 08	4Q 08 (+25bp)	6.25	6.50	6.50	6.50	6.50
Europe/Africa	GDP-weighted average	4.80	20				4.81	4.79	4.59	4.31	4.08
Euro area	Refi rate	4.25	25	3 Jul 08 (+25bp)	4 Sep 08	Mar 09 (-25bp)	4.25	4.25	4.00	3.75	3.50
United Kingdom	Repo rate	5.00	-75	10 Apr 08 (-25bp)	4 Sep 08	Nov 08 (-25bp)	5.00	4.75	4.50	4.00	4.00
Sweden	Repo rate	4.50	100	3 Jul 08 (+25bp)	4 Sep 08	on hold	4.50	4.50	4.50	4.50	4.50
Norway	Deposit rate	5.75	100	25 Jun 08 (+25bp)	24 Sep 08	on hold	5.75	5.75	5.75	5.75	5.75
Czech Republic	2-week repo rate	3.50	25	7 Aug 08 (-25bp)	25 Sep 08	25 Sep 08 (-25bp)	3.25	3.25	3.00	3.00	3.00
Hungary	2-week deposit rate	8.50	75	26 May 08 (+25bp)	<u>25 Aug 08</u>	2Q 09 (-25bp)	8.50	8.50	8.50	8.25	7.75
Poland	7-day intervention rate	6.00	125	25 Jun 08 (+25bp)	<u>27 Aug 08</u>	on hold	<b>6.00</b>	<b>6.00</b>	<b>6.00</b>	5.75	5.25
Romania	Base rate	10.25	325	31 Jul 08 (+25bp)	25 Sep 08	25 Sep 08 (+25bp)	10.50	11.00	11.00	10.50	9.50
Russia	1-week deposit rate	4.25	100	11 Jul 08 (+25bp)	Sep 08	Sep 08 (+25bp)	4.50	4.75	5.00	5.00	5.00
Slovak Republic	2-week repo rate	4.25	0	27 Apr 07 (-25bp)	<u>26 Aug 08</u>	Mar 09 (-25bp)	4.25	4.25	4.00	3.75	3.50
South Africa	Repo rate	12.00	200	12 Jun 08 (+50bp)	9 Oct 08	Apr 09 (-50bp)	12.00	12.00	12.00	11.00	<b>10.00</b>
Switzerland	3-month Swiss Libor	2.75	25	13 Sep 07 (+25bp)	18 Sep 08	on hold	2.75	2.75	2.75	2.75	2.75
Turkey	Overnight borrowing rate	16.75	-75	17 Jul 08 (+50bp)	18 Sep 08	Apr 09 (-25bp)	16.75	16.75	16.75	16.00	14.50
Asia/Pacific	GDP-weighted average	3.75	21				3.75	3.77	3.81	3.84	4.07
Australia	Cash rate	7.25	75	4 Mar 08 (+25bp)	2 Sep 08	Sep 08 (-25bp)	7.00	6.75	6.50	6.00	6.00
New Zealand	Cash rate	8.00	-25	24 Jul 08 (-25bp)	11 Sep 08	10 Sep 08 (-25bp)	7.75	7.25	6.75	<b>6.25</b>	6.00
Japan	Overnight call rate	0.50	0	21 Feb 07 (+25bp)	17 Sep 08	4Q 09 (+25bp)	0.50	0.50	0.50	0.50	0.75
Hong Kong	Discount window base	3.50	-325	1 May 08 (-25bp)	17 Sep 08	18 Mar 09 (+25bp)	3.50	3.50	3.75	4.25	5.25
China	1-year working capital	7.47	45	20 Dec 07 (+18bp)	3Q 08	1Q 09 (+27bp)	7.47	7.47	7.74	8.01	8.46
Korea	Base rate	5.25	25	7 Aug 08 (+25bp)	10 Sep 08	on hold	5.25	5.25	5.25	5.25	5.25
Indonesia	BI rate	9.00	75	5 Aug 08 (+25bp)	4 Sep 08	4 Sep 08 (+25bp)	9.25	9.50	9.50	9.50	9.50
India	Repo rate	9.00	125	29 Jul 08 (+50bp)	24 Oct 08	24 Oct 08 (+50bp)	9.00	9.50	9.50	9.50	9.50
Malaysia	Overnight policy rate	3.50	0	26 Apr 06 (+25bp)	<u>25 Aug 08</u>	on hold	<b>3.50</b>	<b>3.50</b>	<b>3.50</b>	<b>3.50</b>	<b>3.50</b>
Philippines	Reverse repo rate	5.75	-25	17 Jul 08 (+50bp)	<u>28 Aug 08</u>	28 Aug 08 (+25bp)	6.00	6.00	6.00	6.00	6.00
Thailand	1-day repo rate	3.50	25	16 Jul 08 (+25bp)	<u>27 Aug 08</u>	on hold	3.50	3.50	3.50	3.50	3.50
Taiwan	Official discount rate	3.625	50	26 Jun 08 (+12.5bp)	Sep 08	Sep 08 (+12.5bp)	3.75	3.75	3.75	3.75	4.00

**Bold** denotes move this week and forecast changes. Underline denotes policy meeting during upcoming week.

## Forecasts - Australia and New Zealand

Australia: economic projections <i>percentage change over previous period, seasonally adjusted annual rates, ur</i>														
				2007			2008				2009			
	2007	2008	2009	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Chain volume GDP	4.3	2.8	2.6	4.5	4.9	2.7	2.5	1.3	2.6	3.2	3.2	2.0	2.4	2.3
Private consumption	4.6	3.4	1.8	3.3	4.7	6.3	2.8	1.2	2.8	2.0	1.2	1.6	2.0	2.4
Construction investment	9.7	3.6	3.7	4.1	10.0	-5.5	7.9	1.8	6.1	3.0	5.1	2.0	1.9	5.9
Equipment investment	7.7	3.9	3.4	26.7	-11.2	16.1	-6.0	4.3	13.2	4.2	-2.1	4.2	0.0	8.6
Public investment	5.4	11.9	5.8	82.8	-29.8	28.0	25.9	3.5	5.8	5.7	5.8	6.0	6.3	6.7
Government consumption	2.2	4.5	3.4	0.6	5.8	6.5	1.4	6.7	5.4	3.7	3.5	2.2	1.8	2.2
Exports of goods & services	3.2	2.5	4.6	3.5	8.1	-2.8	2.1	2.4	4.1	6.1	4.1	4.1	6.1	4.1
Imports of goods & services	10.6	10.4	4.2	7.4	10.0	14.3	14.6	6.1	8.2	4.1	2.0	4.1	5.1	2.0
Contributions to GDP growth:														
Domestic final sales	5.2	4.2	2.6	6.5	4.1	7.2	5.6	-1.1	4.8	2.9	2.2	2.3	2.1	3.7
Inventories	0.7	0.5	0.2	-1.0	1.4	-0.5	-0.1	3.5	-0.9	0.1	0.6	-0.1	0.4	-1.7
Net trade	-1.7	-2.0	-0.1	-1.0	-0.7	-3.7	-2.9	-1.0	-1.2	0.2	0.3	-0.2	-0.1	0.3
GDP deflator (%oya)	3.8	3.3	2.6	4.1	3.3	3.5	3.5	3.7	3.4	2.8	2.6	2.6	2.6	2.5
Consumer prices (%oya)	2.3	4.3	3.2	2.1	1.9	3.0	4.2	4.3	4.3	4.4	3.6	3.2	3.1	3.0
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)	-20.7	-26.0	-18.1	-4.5	-5.4	-7.0	-8.3	-7.8	-5.3	-4.6	-4.2	-4.2	-4.9	-4.8
Current account (A\$ bil, sa)	-67.0	-72.3	-67.2	-16.0	-16.3	-18.7	-19.5	-19.4	-17.0	-16.5	-16.3	-16.4	-17.2	-17.3
as % of GDP	-6.2	-6.3	-5.5	-6.0	-6.0	-6.7	-6.9	-6.8	-5.9	-5.6	-5.5	-5.4	-5.6	-5.6
3m eurodeposit rate (%)*	6.0	7.6	6.9	5.8	7.1	7.2	7.6	7.8	7.7	7.4	7.2	7.0	6.8	6.6
10-year bond yield (%)*	5.6	6.1	5.8	5.6	5.7	6.4	6.1	6.2	6.2	6.1	6.0	5.9	5.8	5.7
US\$/A\$*	0.75	0.90	0.83	0.74	0.77	0.91	0.91	0.97	0.87	0.84	0.83	0.83	0.83	0.83
Commonwealth budget (FY, A\$ bil)	17.2	16.8	21.7											
as % of GDP	1.6	1.5	1.8											
Unemployment rate	4.4	4.5	5.3	4.3	4.3	4.3	4.0	4.3	4.4	4.7	4.9	5.1	5.3	5.5
Industrial production	3.2	3.3	0.9	3.0	-0.1	5.5	6.7	3.0	0.0	-1.0	3.0	2.5	1.0	0.0

\*All financial variables are period averages

New Zealand: economic projections <i>percentage change over previous period, seasonally adjusted annual rates, unless stated</i>														
				2007			2008				2009			
	2007	2008	2009	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real GDP (1995-96 prices)	3.1	0.3	1.5	3.2	2.2	3.3	-1.1	-2.0	-1.1	0.0	2.4	3.1	3.2	3.6
Private consumption	4.1	-1.1	-0.2	1.7	2.1	2.0	-1.4	-7.5	-0.2	0.0	0.1	0.2	1.1	1.8
Fixed Investment	4.4	-0.7	1.2	0.4	1.6	12.5	-7.6	-5.5	-1.0	0.3	2.0	2.8	3.1	3.9
Residential construction	4.4	-16.9	-1.0	52.6	22.7	-5.5	-52.2	-19.0	0.0	-2.0	0.0	0.8	2.8	3.2
Other fixed investment	4.4	3.4	1.7	-9.4	-3	17.9	8.0	-2.4	-1.2	0.8	2.4	3.2	3.2	4.0
Inventory change (NZ\$ bil, saar)	0.8	0.3	-0.1	0.4	0.3	0.1	0.4	0.1	0.0	-0.1	0.0	0.0	-0.1	-0.1
Government spending	3.9	10.6	7.0	3.8	7.6	0.9	4.7	34.9	14.7	3.9	4.6	4.7	3.3	2.3
Exports of goods & services	3.3	-0.8	-0.5	-4.8	-0.2	19.3	-7.1	-3.5	-7.1	-6.2	2.5	3.2	3.5	4.1
Imports of goods & services	8.6	3.7	-1.1	11.0	3.0	16.2	4.9	-6.2	-0.1	-3.2	-0.5	-0.2	0.2	0.9
Contributions to GDP growth:														
Domestic final sales	4.6	2.3	1.5	4.1	5.0	6.0	-0.2	-0.2	2.6	1.0	0.6	1.7	3.3	2.8
Inventories	0.5	-0.3	-0.3	4.6	-1.5	-2.4	3.3	-3.2	-1.4	-0.2	0.8	0.4	-1.1	-0.1
Net trade	-2.0	-1.7	0.3	-5.4	-1.2	-0.1	-4.2	1.4	-2.3	-0.7	1.0	1.1	1.0	0.9
GDP deflator (%oya)	4.2	4.8	2.8	4.1	3.9	5.6	5.9	5.3	4.9	3.3	2.9	2.8	2.7	2.7
Consumer prices	2.4	4.4	3.8	4.0	2.0	4.8	3.4	4.0	5.1	5.2	5.0	4.3	3.5	3.0
%oya	2.4	4.4	3.8	2.0	1.8	3.2	3.4	3.3	4.1	4.0	4.1	4.0	3.7	3.4
Trade balance (NZ\$ bil, sa)	-2.3	-0.8	0.7	-0.8	-0.7	0.0	-0.2	-0.2	-0.2	-0.2	-0.1	0.1	0.3	0.5
Current account (NZ\$ bil, sa)	-13.8	-13.3	-10.7	-3.6	-3.6	-3.1	-3.5	-3.3	-3.3	-3.2	-2.9	-2.8	-2.6	-2.3
as % of GDP	-8.1	-7.4	-5.7	-8.4	-8.3	-7.0	-7.9	-7.4	-7.2	-7.1	-6.3	-6.1	-5.6	-4.9
Yield on 90-day bank bill (%)*	8.4	8.5	7.7	8.2	8.7	8.8	8.8	8.7	8.5	8.2	8.0	7.8	7.6	7.5
10-year bond yield (%)*	6.3	6.3	5.7	6.4	6.4	6.4	6.4	6.4	6.3	6.2	6.0	5.7	5.5	5.5
US\$/NZ\$*	0.74	0.75	0.68	0.74	0.74	0.76	0.79	0.76	0.74	0.72	0.70	0.68	0.67	0.68
Commonwealth budget (NZ\$ bil)	6.4	5.3	5.0											
as % of GDP	3.7	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

## Australia and New Zealand economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
<b>25 Aug</b>  	<b>26 Aug</b> <b>New Zealand:</b> Trade balance (10:45am) Jul RBNZ inflation expectation (03:00pm) 3Q	<b>27 Aug</b> <b>Australia:</b> Construction work done (11:30am) 2Q  <b>New Zealand:</b> NBNZ business conf. (03:00pm) Aug	<b>28 Aug</b> <b>Australia:</b> Private capital expenditure (11:30am) 2Q  <b>New Zealand:</b> Money supply (03:00pm) Jul	<b>29 Aug</b> <b>Australia:</b> Private sector credit (11:30am) Jul  <b>New Zealand:</b> Building permits (10:45am) Jul
<b>1 Sep</b> <b>Australia:</b> Current account (11:30am) 2Q Company profits (11:30am) 2Q Inventories (11:30am) 2Q	<b>2 Sep</b> <b>Australia:</b> Building approvals (11:30am) Jul RBA cash rate (02:30pm) Sep	<b>3 Sep</b> <b>Australia:</b> GDP (11:30am) 2Q  <b>New Zealand:</b> ANZ commodity price (03:00pm) Aug	<b>4 Sep</b> <b>Australia:</b> Trade balance (11:30am) Jul	<b>5 Sep</b> <b>Australia:</b> Foreign reserves (04:30pm) Aug
<b>8 Sep</b> <b>Australia:</b> ANZ job ads (11:30am) Aug  <b>New Zealand:</b> QV house prices Aug	<b>9 Sep</b> <b>Australia:</b> Housing finance (11:30am) Jul NAB business confidence (11:30am) Aug Retail sales (11:30am) Jul	<b>10 Sep</b> <b>Australia:</b> Westpac consumer confidence (10:30am) Sep  <b>New Zealand:</b> Terms of trade (10:45am) 2Q	<b>11 Sep</b> <b>Australia:</b> Unemployment rate (11:30am) Aug  <b>New Zealand:</b> Cash rate (09:00am) Sep PMI (12:00pm) Aug	<b>12 Sep</b> <b>New Zealand:</b> Retail sales (10:45am) Jul
<b>15 Sep</b> <b>Australia:</b> Dwelling starts (11:30am) 2Q	<b>16 Sep</b>	<b>17 Sep</b> <b>Australia:</b> WMI leading index (10:30am) Jul	<b>18 Sep</b>	<b>19 Sep</b> <b>New Zealand:</b> Visitor arrivals (10:45am) Aug Credit card spending (03:00pm) Aug

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



## Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
25 - 29 August	25 August	26 August	27 August	28 August	29 August
United Kingdom • Nationwide HPI (Aug)	Hungary • NBH meeting  Japan • Shirakawa speech  Malaysia • BNM meeting  Taiwan • Export orders (Jul) • IP (Jul)  United States • Existing home sales (Jul)	Germany • CPI 6 states and prelim (Aug) • GDP (2Q) • IFO business surv (Aug)  Slovak Republic • NBS meeting  United Kingdom • BBA mort lending (Jul)  United States • New home sales (Jul) • OFHEO HPI (Jun, 2Q) • S&P/C-S HPI (Jun, 2Q) • FOMC minutes	Poland • NBP meeting  South Africa • CPI (Jul)  Thailand • BoT meeting  United States • Durable goods (Jul)	Euro area • M3 (Jul)  Germany • Employment (Jul) • Unemployment (Aug)  Philippines • BSP meeting  United States • GDP prelim (2Q)	Canada • GDP (2Q)  Euro area • EC bus survey (Aug) • HICP flash (Aug) • Unemployment (Jul)  Japan • Core CPI, Hh spending, Housing starts, IP prel, retail, unemploy (Jul) • PMI mfg, Shoko Chukin (Aug)  Korea • IP (Jul)  Poland • GDP (2Q)  United States • Chicago Fed survey (Aug) • Consumer sent (Aug) • Personal income (Jul)
1 - 5 September	1 September	2 September	3 September	4 September	5 September
Japan • Cabinet Office private consumption index (Jul)  United Kingdom • Halifax HPI (Aug)	China • PMI mfg (Aug)  Euro area • PMI mfg final (Aug)  Germany • Retail sales (Jul)  Japan • Nominal wages (Jul)  Korea • CPI (Aug) • Trade balance (Aug)  United Kingdom • PMI mfg (Aug)	Australia • RBA meeting  Brazil • IP (Jul)  Japan • Shirakawa speech  Singapore • PMI mfg (Aug)  United States • Construction spending (Jul) • ISM mfg (Aug)	Australia • GDP (2Q)  Canada • BoC meeting  Euro area • GDP prelim (2Q) • PMI services final (Aug) • Retail sales (Jul)  Italy • ISAE business surv (Aug)  United Kingdom • PMI services (Aug)  United States • Beige book • Factory orders (Jul) • Vehicle sales (Aug)	Chile • BCCCh meeting  Euro area • ECB meeting  Germany • Mfg orders (Jul)  Indonesia • BI meeting  United Kingdom • BoE meeting  Sweden • Riksbank meeting  United States • ADP employment (Aug) • ISM nonmfg (Aug) • Productivity, costs (2Q)	Brazil • IPCA (Aug)  Canada • Employment (Aug) • Ivey PMI (Aug)  Germany • IP (Jul)  Japan • MoF corporate surv (2Q)  Russia • CPI (Aug)  Taiwan • CPI (Aug)  United States • Employment report (Aug)

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