Australia and New Zealand - Weekly Prospects

Summary

- In a quiet week for data in **Australia**, the onset of the global financial market turmoil intensified the downside risks to the domestic growth outlook. This means that, in a change of forecast, we now expect the RBA to cut the cash rate 25bp on October 7. Previously, we had expected the RBA to wait until December before cutting the cash rate again. Auto sales fell for the second straight month as discretionary spending continued to contract. The Aussie data flow resumes in earnest this week, though, with data on credit, retail sales, building approvals, and the trade balance scheduled for release.
- The highlight of the Antipodean economic calendar last week was **New Zealand's** gloomy 2Q GDP data. The Shaky Isles look even more shaky than before because it now is official; the economy entered recession last quarter. In fact, GDP contracted 0.2%q/q after a similar contraction in 1Q. The downgrade to the global economic outlook owing to the latest round of financial instability means the RBNZ now probably will cut the OCR 50bp in October, instead of the 25bp we forecast previously.
- As the US slips toward contraction the specter of a **global recession** looms larger. Certainly the economic news from Western Europe points in that direction. The sharp declines in Euro area business surveys in recent months challenge our forecast that the economy will stagnate rather than contract in coming quarters. The September composite PMI dipped to its lowest level since late 2001. Moreover, a number of other important surveys have moved into territory similar to the start of the deep early 1990s downturn.
- Another key issue is what happens in **Japan**. The economy contracted last quarter, but the recent indicators have shown tentative signs of stability, consistent with our view that the recession will be shallow, as the terms of trade improve with the recent fall in commodity prices. Much will depend on the trajectory of exports. But the pace of corporate adjustment and its feedback on domestic demand are also key, as elsewhere. This week's October Tankan and September Shoko Chukin surveys will shed light on corporate activity.
- Whether the **global economy** slides into recession is likely to be determined by the fate of the emerging market economies. Consistent with revisions to the US, we have significantly lowered our EM growth forecast for the coming quarters. However, the projection of a growth bottom at around 4.5% would represent a far better performance for the group than was recorded during the last US recession. Important support should come from China, where falling inflation and a prompt shift toward policy stimulus is expected to help sustain domestic demand. Demand remains strong among some of the major commodity exporters as well.

This week's highlight

The Aussie retail sales data, even though Budget cuts slashed the size of the sample, creating additional volatility in the series. Sales were strong in July, but probably rose just 0.2%m/m in August.

Contents

JPMorgan Australia Ltd., Sydney
www.morganmarkets.com

Stephen Walters
(61-2) 9220-1599
stephen.b.walters@jpmorgan.com

Helen Kevans
(61-2) 9220-3250
helen.e.kevans@jpmorgan.com

JPMorgan Chase Bank, Sydney
Stephen Walters (61-2) 9220-1599
stephen.b.walters@jpmorgan.com
Helen Kevans (61-2) 9220-3250
helen.e.kevans@jpmorgan.com

Data and event previews - Australia and New Zealand

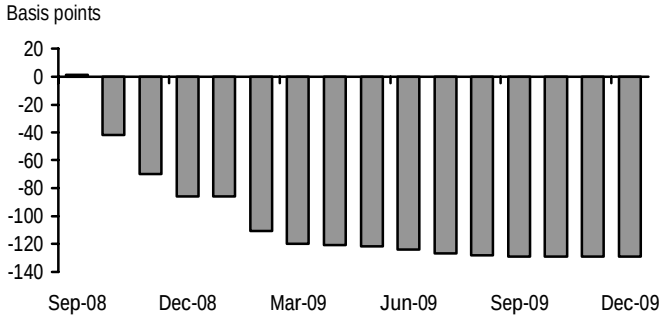
Date [(a)]	Data/event	Forecast		*Previous*	Comment
		JPMorgan	Consensus		
Tuesday, 30 September (7.45am)	**NZ building consents (%m/m, Aug)**	**na**	na	*3.5*	na
Tuesday, 30 September (11.30am)	**Aust. private sector credit (Aug., %m/m)**	**0.3**	0.5	*0.5*	Credit likely expanded just 0.3%m/m in August. There almost certainly was another contraction in credit for personal and other purposes, and business credit probably grew just 0.3%m/m as confidence among managers plunged. Housing credit outstanding, though, probably grew 0.5%m/m, the same as in July, helped along by speculation that RBA rate cuts were on the way. This will be the weakest rate of expansion in total credit since 1993, and will leave annual growth at just 10.1%oya.
Tuesday, 30 September (11.30am)	**Aust. retail sales (Aug., %m/m)**	**0.2**	0.2	*1.4*	Unfortunately, the ABS has dramatically reduced the sample size for this data, owing to cuts in the May Budget, so random volatility in this data has increased. Sales were unexpectedly firm in July (helped by holiday configurations, spending on electronics ahead of the Olympic Games, cold weather, and the introduction of new products), but the anecdotes for sales in August are gloomy. Indeed, none of the factors supporting sales in July were present in August, except for a lingering "Olympic effect." The flipside is that there was widespread speculation that the RBA was edging closer to cutting the cash rate, news that triggered a big rise in consumer confidence during the month. This may provide some support for spending. Also, petrol prices fell in the month, which would free up income for spending elsewhere.
Tuesday, 30 September (11.30am)	**Aust. building approvals (Aug., %m/m)**	**1.5**	-1.0	*-2.3*	Building approvals likely rebounded in August, but this follows a large fall in July. The volatility in the series makes month to month interpretations more difficult than before.
Tuesday, 30 September (1.00pm)	**NZ NBNZ business confidence (Sep, % balance)**	**na**	na	*-20.5*	Confidence rebounded strongly in August following the RBNZ's rate cut in July, although there remained more pessimists than optimists. Confidence probably rose again in September, albeit modestly, given that the RBNZ surprised most by cutting the cash rate by twice market expectations for a 25bp move. Business managers probably still are downbeat about the domestic economic outlook, but the drop in interest rates should have provided some relief.
Thursday, 2 October (11.30am)	**Aust. trade balance (Aug., $ mil)**	**-250**	-200	*-717*	Imports dropped 3%m/m in August. Exports also probably were lower, but a 1% fall in export values still should be enough to drag the trade deficit down to just A$250 million.
Thursday, 2 October (12.00pm)	**NZ ANZ commodity price index (Sep, %m/m)**	**na**	na	*-3.3*	na

(a) Australian Eastern Standard Time.

JPMorgan Chase Bank, Sydney
Stephen Walters (61-2) 9220-1599
stephen.b.walters@jpmorgan.com
Helen Kevans (61-2) 9220-3250
helen.e.kevans@jpmorgan.com

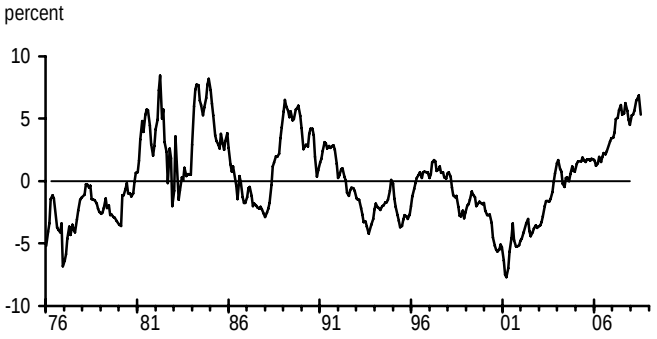
Feature charts

RBA official rate cut expectations



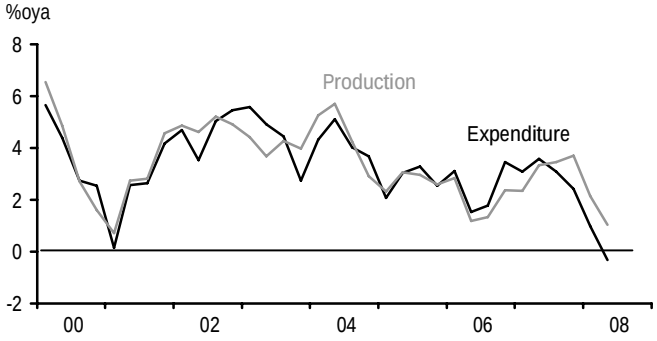
In the wake of recent global financial market instability, we now expect the RBA to lower the cash rate 25bp next week. Previously, we expected the next rate cut in December. The futures market strip now prices 86bp of rate cuts by the end of 2008. We forecast another 100bp of easing from here, but by June 2009.

JPM monetary conditions index - Australia



The RBA cut the cash rate in September and the AUD has fallen sharply since mid-July, yet monetary conditions remain tight. This no longer is appropriate. The weakness in global economic momentum means inflation probably will return to target faster, which means there is more scope for the RBA to accelerate the move to a less restrictive policy stance.

New Zealand - expenditure and production GDP



New Zealand's economy officially slipped into recession in 2Q. The headline production-based GDP data showed a 0.2%q/q contraction. The expenditure based GDP data showed a larger contraction (-0.3%oya). The interest rate sensitive sectors of the economy - consumers and housing were weakest.

JPMorgan Australia Ltd., Sydney
Stephen Walters (61-2) 9220-1599
stephen.b.walters@jpmorgan.com
Helen Kevans (61-2) 9220-3250
helen.e.kevans@jpmorgan.com

Australia

- **RBA now likely to cut the cash rate on October 7**
- **Retail sales and credit growth likely to be weak**
- **Behaviour of commercial banks the key to future official rate moves**

In a quiet week for data in Australia, the onset of the global financial market turmoil intensified the downside risks to the domestic growth outlook. This means that, in a change of forecast, we now expect the RBA to cut the cash rate 25bp on October 7. Previously, we had expected the RBA to wait until December before cutting the cash rate again. The Aussie data flow resumes in earnest this week, with data on credit, retail sales, building approvals, and trade scheduled for release.

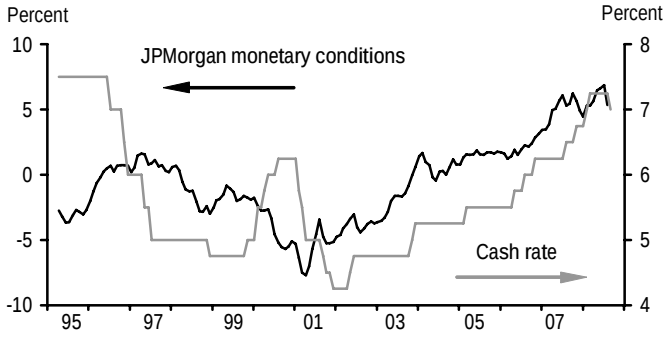
RBA now likely to cut cash rate in October

For some time, we have argued that the macroeconomic case for an RBA rate cut in October was not compelling. Inflation, for example, almost certainly will accelerate in 3Q, firms have substantially upgraded their business investment plans, demand for home loans stabilized in July, the jobless rate fell sharply in August, retail sales unexpectedly boomed in July, and both business and consumer confidence rebounded following the RBA's rate cut in September, the first since December 2001. Also, the plunge in AUD since mid-July has done some of the heavy lifting for the RBA by easing monetary conditions.

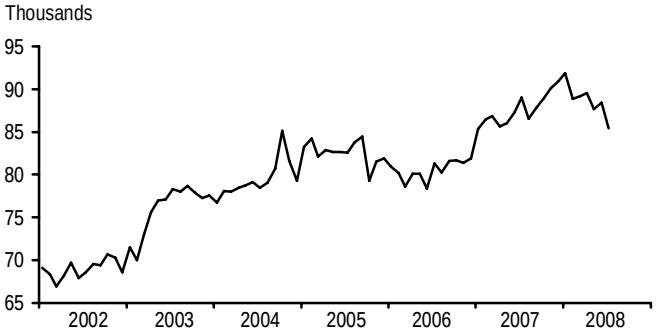
Similarly, the most recent RBA commentary has indicated that officials still believe that there are "opposing forces" at work in the economy; so the case for further rate cuts was not "open and shut." On the one hand, RBA officials believed the booming terms of trade was a powerful source of support for national income. On the other hand, the pace of growth in domestic demand had slowed, which meant inflation probably will track back towards the RBA's target range "over time."

Our prior view was that the RBA could wait until December before easing policy again. But things have changed rapidly in recent weeks, so much so that we now believe that the RBA will cut the cash rate 25bp on October 7. RBA officials will, however, have to tolerate an elevated CPI on October 25, which will likely print almost double the midpoint of its 2-3% target range in the near term. This will be just after they eased policy to mitigate the downside risks to growth that the events of recent weeks have intensified. This will not sit easily with some RBA officials.

Australia: cash rate and monetary conditions



Australia: auto sales



Downside risks to growth have grown

In the current environment of heightened uncertainty, however, and with monetary conditions still very tight, easing too early is a mistake RBA officials now seem more willing to risk, rather than waiting too long before easing again and risking an even more abrupt slowdown in the economy than currently forecast. The RBA macroeconomic forecasts released in August—well before the onset of the latest financial market instability—showed nonfarm GDP growth of just 1.5% in the year to December 2008. Given what has happened since, the risks to this forecast must be skewed to the downside, which means the RBA probably have to be more nimble than before.

On balance, it now looks more likely than not that the RBA will lower the cash rate next week. In addition, it also now seems likely that the RBA will cut the cash rate a third time before year end, probably in December, when the dust of the financial market turmoil may have settled. We now look for a total of another 100bp of easing by June 2009 (compared to 75bp previously), but the rate cuts will be "front-loaded."

Aussie vehicle sales dropped again

Australian auto sales unexpectedly rose in June (up 0.7%m/m)

JPMorgan Australia Ltd., Sydney
Stephen Walters (61-2) 9220-1599
stephen.b.walters@jpmorgan.com
Helen Kevans (61-2) 9220-3250
helen.e.kevans@jpmorgan.com

as some buyers rushed to buy vehicles ahead of the July 1 increase in the luxury car tax. The tax change only this week passed through the upper house of Federal Parliament to become law, but car buyers moved early. Indeed, car sales in July dropped sharply, as the new tax rate kicked in. Sales dropped in August too (down 3.5%) in another sign that discretionary household spending has weakened significantly, albeit this time mainly in response to a punitive tax change.

This week: Aussie data flow resumes

This week brings important economic data releases that may influence how aggressively the RBA cuts the cash rate on October 7. The most important data release is the August retail sales report. Unfortunately, the ABS has dramatically reduced the sample size for this data so random volatility in this data has increased. Sales were unexpectedly firm in July (helped by holiday configurations, spending on electronics ahead of the Olympic Games, and cold weather), but the anecdotes for sales in August are gloomy. Indeed, none of the factors supporting sales in July were present in August, except for a lingering "Olympic effect." The flipside is that there was widespread speculation that the RBA was edging closer to cutting the cash rate, news that triggered a big rise in consumer confidence during the month. This may provide some support for spending. Also, petrol prices fell in the month, which would free up income for spending elsewhere. We forecast a weak 0.2%m/m rise in sales.

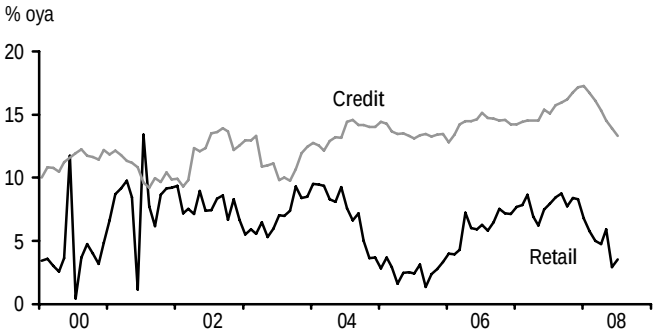
The RBA's credit aggregates for August will also be released. Credit likely expanded just 0.3%m/m. There almost certainly was another contraction in credit for personal and other purposes, and business credit probably grew just 0.3% as confidence among managers plunged. Housing credit outstanding, though, probably grew 0.5%m/m, the same as in July, helped along by speculation that RBA rate cuts were on the way. This will be the weakest rate of expansion in total credit since 1993, and will leave annual growth at just 10.1%oya.

Data releases and forecasts

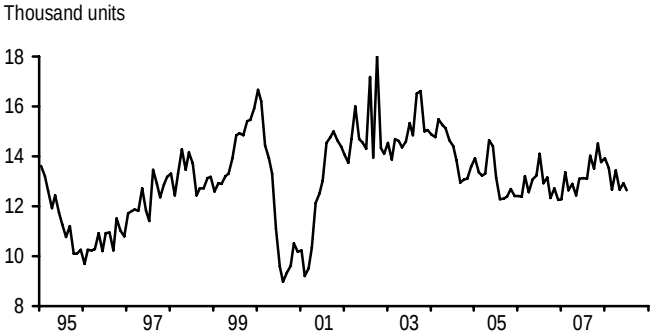
Week of September 29 - October 3

Tue Sep 30 11:30am	Private-sector credit Seasonally adjusted	May	Jun	Jul	Aug
	(%m/m)	0.5	0.4	0.5	0.3
	(%oya)	13.3	11.8	11.2	10.1

Australia: retail sales and credit growth



Australia: building approvals - total



Tue Sep 30 11:30am	Retail trade Seasonally adjusted	May	Jun	Jul	Aug
	(%m/m)	0.7	-0.9	1.4	0.2
	(%oya)	5.9	2.9	3.5	3.0

Tue Sep 30 11:30am	Building approvals Seasonally adjusted	May	Jun	Jul	Aug
	(%m/m)	-5.8	2.2	-2.3	1.5
	(%oya)	1.8	-1.2	-3.7	-2.1

Thu Oct 2 11:30am	Trade balance Seasonally adjusted	May	Jun	Jul	Aug
	Trade balance (A$ mn)	-280	351	-717	-250
	Exports (A$ bn)	22.6	23.1	22.9	22.7
	Imports (A$ bn)	22.8	22.7	23.6	22.9

Review of past week's data

Sales of new motor vehicles

Units, seasonally adjusted

	Jun		Jul		Aug	
(%m/m)	~~0.8~~	*0.7*	~~-3.4~~	*-4.0*	__	*-3.5*
(%oya)	~~1.3~~	*0.9*	~~-4.1~~	*-4.5*	__	*-7.2*

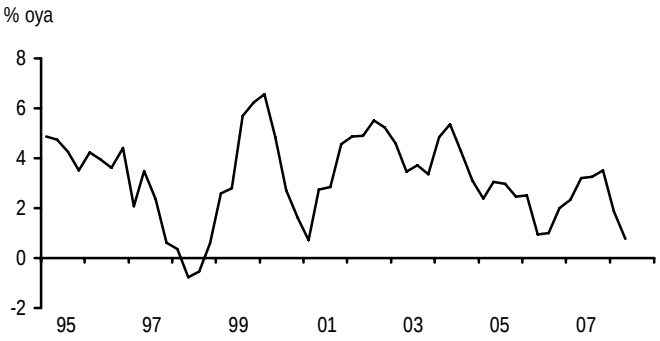
JPMorgan Australia Ltd., Sydney
Stephen Walters (61-2) 9220-1599
stephen.b.walters@jpmorgan.com
Helen Kevans (61-2) 9220-3250
helen.e.kevans@jpmorgan.com

New Zealand

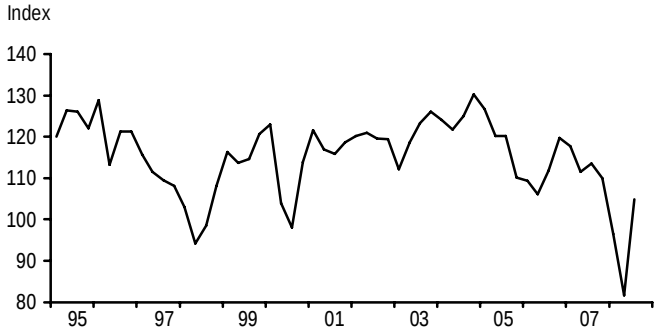
- **It's official: New Zealand entered recession in 2Q**
- **RBNZ now likely to cut 50bp in October**
- **Business confidence the highlight this week**

The highlight of the Antipodean economic calendar last week was New Zealand's gloomy 2Q GDP data. The Shaky Isles look even more shaky than before because it now is official; the economy entered recession last quarter. In fact, GDP contracted 0.2%q/q in 2Q, after a similar contraction in 1Q. The downgrade to the global economic outlook owing to the latest round of financial instability means the RBNZ now probably will cut the official cash rate 50bp in October, instead of the 25bp we forecast previously.

New Zealand: GDP growth



New Zealand: consumer confidence



NZ economy drops into recession

While the more timely monthly economic data left little doubt that the economy was on its knees, the GDP data for 2Q confirmed that New Zealand experienced a technical recession over the first half of 2008. GDP contracted 0.2%q/q in 2Q, after a 0.3%q/q contraction in 1Q. This is the sharpest rate of contraction since 4Q 2005. As expected, the interest rate-sensitive sectors suffered most, with consumer spending and home construction falling in the quarter. We expect another small contraction in GDP in 3Q, and a stagnant 4Q.

The expenditure-based GDP data was even weaker than the headline production-based decline. Expenditure-based GDP dropped 0.5%q/q, after a 0.6% drop in 1Q. An important contributor to the weakness in 2Q was consumer spending, which sank 0.2% across the quarter. Home construction plunged 8.2%. Business investment, though, surprised with a 6.1% expansion, and government spending rose 0.5%. Exports fell 0.2% (the second straight contraction, albeit a big improvement from the plunge in 1Q), and imports bounced 3.3%. Expenditure-based GDP growth over the year sank to -0.3%oya, from a revised 1.0% in the year to 1Q.

On the production side of the accounts, the biggest fall was in construction, which dropped 3.8%q/q. Output from the retail and accommodation sector dropped 1.9%, electricity and gas output fell 1.6%, and wholesale trade fell 1.2%. Farm output fell 0.6%. The biggest rise in output in the June quarter was in manufacturing (up 1.4%), followed by transport (up 1.2%) and government "output". Production-based GDP rose 1.0%oya.

The RBNZ cut the official cash rate an unexpectedly assertive 50bp earlier this month. While another rate cut on October 23 is a certainty, the onset of financial market instability and accumulating downside risks to global economic growth mean the RBNZ now probably will ease by another 50bp (previously we expected a 25bp rate cut). Indeed, since the RBNZ's 50bp cut on September 11, the global economic outlook has become significantly darker, and conditions in financial markets have substantially worsened. Only if economic and financial conditions had improved would the RBNZ be inclined to slow the pace of monetary easing. We expect a further rate cut in early December, and a cash rate of 6% by mid-2009.

More contemporary data last week showed the economy in a better light. The Westpac-McDermott Miller consumer confidence index, for example, rebounded strongly in the September quarter from a 17-year low, as households reacted with relief to the RBNZ's 50bp rate cut earlier this month. The index unexpectedly shot above the breakeven point where optimists outnumber pessimists to 104.8, the highest reading since last December.

Data releases and forecasts

Week of September 29 - October 3

Tue
Sep 30
10:45am

Building consents

Not seasonally adjusted

	May	Jun	Jul	Aug
(%m/m)	-30.3	-17.6	3.5	__
(%oya)	-28.8	-47.1	-34.7	__

Tue
Sep 30
3:00pm

NBNZ business confidence

	Jun	Jul	Aug	Sep
% balance of respondents	-38.7	-43.2	-20.5	__

Confidence rebounded strongly in August following the RBNZ's rate cut in July, although there remained more pessimists than optimists. Confidence probably rose again in September, albeit modestly, given that the RBNZ surprised most by cutting the cash rate by twice market expectations for a 25bp move. Business managers probably still are downbeat about the domestic economic outlook, but the drop in interest rates should have provided some relief.

Thu
Oct 2
3.00pm

ANZ commodity price series

Not seasonally adjusted

	Jun	Jul	Aug	Sep
Index - world prices (%m/m)	0.0	1.8	-3.3	__
Index - NZD (%m/m)	2.1	2.8	2.0	__

Review of past week's data

Real GDP

Seasonally adjusted, production-based

	4Q07		1Q08		2Q08	
(%oya)	~~3.5~~	*3.7*	~~1.9~~	*2.2*	~~0.8~~	*1.0*
(%q/q)	~~0.8~~	*0.9*	-0.3		~~-0.3~~	*-0.2*

JPMorgan Chase Bank, New York
Bruce Kasman (1-212) 834-5515
bruce.c.kasman@jpmorgan.com
David Hensley (1-212) 834-5516
david.hensley@jpmorgan.com

Global Essay

- **US forecast revised to include a US recession**
- **With slowdown broadening and deepening elsewhere, risk of a global downturn has risen significantly**
- **Deeper global slowdown will create slack and ease underlying inflation pressure**
- **Policy support will become more widespread, with the Fed now forecast to ease in December**

The sound of the other shoe dropping

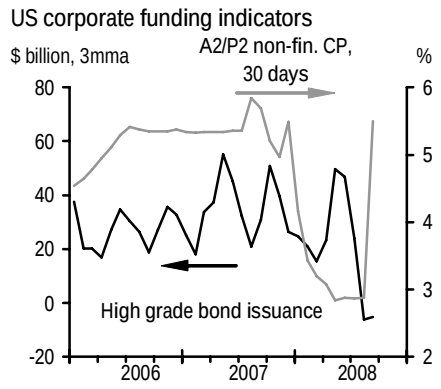
As we go to press the fate of the US Treasury's TARP proposal remains uncertain. Unfortunately, we are more certain that the US economy will face increasing difficulties in the quarters ahead as drags on growth intensify. Last week we revised our forecast to incorporate a US slide into recession over the coming two quarters.

Our earlier expectation that the economy could skirt recession was premised on the judgment that US firms—with a healthy financial position and lean inventories—would not intensify cutbacks in hiring and spending in the face of a contraction in consumption during 2H08. This US view was already being challenged by recent labour market indicators pointing to increased job shedding and deteriorating hiring intentions. The latest wave of financial market stress appears to be creating problems for corporate funding, adding a negative shock to an already fragile environment. Little commercial paper is being issued at maturities of more than a few days, and credit spreads on both high-yield and high-grade corporate bonds have reached new highs for the cycle. Investor caution has also been associated with stalled net high-grade bond issuance. How long corporate funding is impaired will depend on policy action. Regardless, this financial shock is already significant enough to inflict damage. We look for US businesses to pull back in the coming two quarters, with investment spending expected to reverse course and contract at an 8% annualized pace. We also expect payroll losses to average 150,000 per month over this period, double the pace thus far this year.

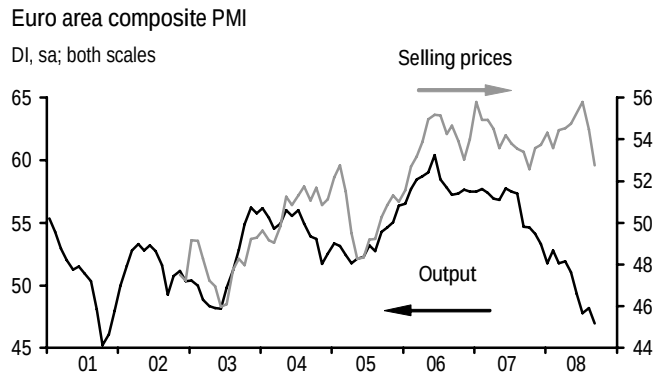
As the US slips toward contraction the specter of a global recession looms larger. Certainly the economic news from Western Europe points in that direction. The sharp declines in Euro area business surveys in recent months challenge our forecast that the economy will stagnate rather than contract in coming quarters. The September composite PMI dipped to its lowest level since late 2001. Moreover, a number of other important surveys have moved into territory similar to the start of the deep early 1990s downturn.

Another key issue is what happens in Japan. The economy contracted last quarter, but the recent indicators have shown tentative signs of stability, consistent with our view that the recession will be shallow, as the terms of trade improve with the recent fall in commodity prices. Much will depend on the trajectory of exports. But the pace of corporate adjustment and its feedback on domestic demand are also key, as elsewhere. This week's October Tankan and September Shoko Chukin surveys will shed light on corporate activity.

Whether the global economy slides into recession is likely to be determined by the fate of the emerging market economies. Consistent with revisions to the US, we have significantly lowered our EM growth forecast for the coming quarters. However, the projection of a growth bottom at around 4.5% would represent a far better performance for the group than was recorded during the last US recession. Important support



JPMorgan Chase Bank, New York
Bruce Kasman (1-212) 834-5515
bruce.c.kasman@jpmorgan.com
David Hensley (1-212) 834-5516
david.hensley@jpmorgan.com



should come from China, where falling inflation and a prompt shift toward policy stimulus is expected to help sustain domestic demand. Demand remains strong among some of the major commodity exporters, as well.

Developed economies to free up slack

One silver lining in this otherwise dark cloud is that the inflation outlook is improving. Headline inflation already is turning downward in response to the sharp correction in global commodity prices. But the more abiding issue for the inflation outlook is the level of resource utilization. Global resource utilization climbed to a multi-decade high during the 2000s expansion. This contributed to a gradual acceleration in unit labour costs and core prices. Indeed, core inflation—excluding all food and energy prices—climbed to 2.3%oya in August, almost one percentage point higher than the low reached in early 2004.

With the JPMorgan forecast now anticipating a sustained period of below-trend global growth, this will generate a significant amount of resource slack. Our measure of aggregate resource utilization, which combines movements in the rates of unemployment and capacity utilization, is forecast to decline from almost two standard deviations above normal in late 2007, when growth first dipped below trend, to just a half point above average by the end of 2009. Utilization is expected to fall even farther in the developed economies. This should go a long way toward alleviating underlying inflation pressures in the major economies, especially the US, where the unemployment rate is expected to reach 7%. By comparison, the growth undershoot in the emerging economies is expected to be more modest, and thus free up less slack. This will keep medium-term inflation objectives at risk.

Door opening to more policy ease

With inflation headed lower, the combination of an elevated threat of global recession and intensified financial market stress should have an important impact on monetary policy. The Fed's resolve to separate its policy setting and liquidity management tools will be reinforced by the passage of TARP. However, the recognition that firms are pulling back and the economy is contracting will likely produce an ease. We now expect the Federal Reserve to lower its policy rate to 1.5% and view the December meeting as the most likely time for action.

The ECB also is expected to respond to weak growth and the prospects for a move earlier than our current expectations (end of 1Q09) are increasing. But, this week's press conference is likely to signal only a modest shift in stance. President Trichet will likely acknowledge significant downside risks to the growth forecast published barely a month ago, but also stress upside inflation risks, as survey measures of prices remain elevated, wage demands are high, and inflation expectations in the bond market on a forward basis have not fallen back in recent weeks, even as oil prices have receded. Action is likely to be forthcoming even sooner elsewhere in the developed world. Officials in Australia and NZ are expected to lower rates next month. And the BoE is on tap to begin easing in November.

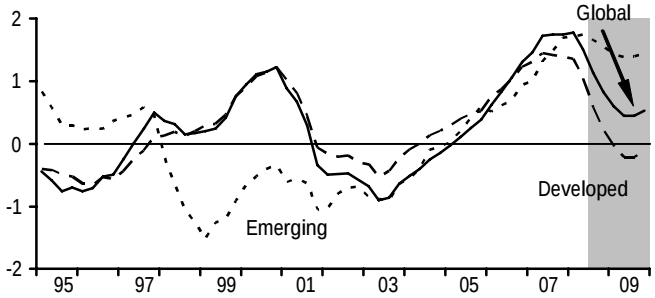
In the emerging world, central banks are gradually going on hold as the risks between inflation and growth are perceived to be more balanced. However, a few central banks have already begun easing. China recently kicked off the process with an unexpected cut in the benchmark lending rate and in banks' required reserve ratio. This move was expected to encourage other Asian banks to follow its lead, albeit with a delay. Taiwan—one of the high-beta EM economies that is most closely tied to the global cycle—surprised markets by cutting rates last week, ending a rate hike cycle that began in 3Q04. Governor Perng stated after the quarterly monetary policy meeting that "the decision was made as inflationary pressure fell and there is rising downside risk to economic growth.'' Perng's view is gradually being adopted by policymakers around EM Asia who, as a group, have traditionally shown a growth bias.

However, the policy frameworks used by the region's central banks will constrain the speed at which this ease is delivered. In particular, countries that adopted inflation targeting frame-

JPMorgan Chase Bank, New York
Bruce Kasman (1-212) 834-5515
bruce.c.kasman@jpmorgan.com
David Hensley (1-212) 834-5516
david.hensley@jpmorgan.com

Resource utilization

Std. dev from 1990-2007 avg.; composite of unemp. and cap. util. rates



works after the Asian financial crisis (Korea, Indonesia, the Philippines, and Thailand) so far have shown little inclination to cut rates, because inflation, though declining, remains well above target. For these central banks, we envisage the easing cycle to start in 1H09. Another laggard is India, where the RBI still seems likely to deliver one more repo rate hike at the October policy meeting, although we now expect rate cuts starting in April 2009. In contrast, Singapore is likely to ease policy next month by guiding its trade-weighted exchange rate lower.

Latin economies join global slowdown

In contrast to Asia, central banks in big Latin economies are still focused on inflation risk. This includes Mexico, which is relatively open and the Latin economy most closely integrated with the US. This structure is now costing Mexico in the form of much weaker exports and industrial production. Mexican firms also have been cutting costs in a bid to boost their competitiveness, leading to a decline in real wages and increased joblessness, which has damped consumption. In response to these factors, the growth forecast has been cut to just 1.6% for both 2008 and 2009. Despite this subpar forecast, we do not look for Banxico to ease policy until late next year because of the central bank's strong commitment to its inflation objective. Indeed, both headline and core inflation are expected to end the year above 5%oya, compared with Banxico's ceiling of 4%. The beginning of the wage negotiation season also is keeping Banxico on hold.

Compared with Mexico, Brazil's economy is much less open and has enjoyed a robust domestic demand engine. Nonetheless, the combination of sustained monetary tightening, tighter domestic financial conditions, and slowing exports is expected to take a toll on growth. Last week we trimmed our 2009 GDP growth forecast to 3.2%—2% points below the expected 2008 pace. Although consumer price inflation is still contained—indeed, Brazil is of the few EM countries where inflation is inside the Bank's target range—the central bank is taking no chances. We look for the COPOM to continue tightening policy on the back of high resource utilization rates and double-digit wage settlements.

JPMorgan Securities Ltd., London
Jan Loeys (44-20) 7325-5473
jan.loeys@jpmorgan.com
John Normand (44-20) 7325-5222
john.normand@jpmorgan.com

JPMorgan View - Global Markets

Wake me up when September ends

- The blizzard of momentous events in markets is leaving investors **stunned**, and has pushed them further in **capital preservation** mode, even if it is not clear what is safe nowadays. Trading volumes are collapsing. The crisis in confidence is proving contagious and has become a run on the financial system that requires equally powerful counteraction by governments.

- The continued rapid slide in economic activity data and the worsening financial crisis are again **pushing down growth expectations** and raising hopes for rate cuts. We have lowered our US growth forecasts again and now accept that the **"old" world of the US, Europe and Japan is most likely in recession.** Our hopes are for a shallow and short recession, but risk is biased towards a longer and more global recession, drawing in EM.

- Our recent switch to a **tactical long on risky assets** did not work in equities or credit, and only worked in mortgages and asset-backed securities, as they at least are the direct target of government buying. A successful passage of the Paulson plan should support riskier assets. However, we repeat that if a rally takes place, it is unlikely to be long-lasting in a worsening recession environment. Recessions do have bear-market rallies that can be violent, but they do not last. Only the prospect of a longer-lasting shift to stronger growth in economies and earnings brings a sustained rally. This is quite some time away from now. The current environment requires tactical trading on risky assets, from an underweight basis, and strategic long positions in government bonds.

Fixed income

- Government bonds rallied across much of the world on weaker US data and doubts on the Paulson plan. A renewed flight to quality made governments outperform other debt markets. A congressional passage of the TARP should reverse some of last week's move. In particular, it should push swap spreads lower again, and government bond yields higher. However, beyond this reversal, the reality of a G10 recession and **the prospect of monetary rate cuts in Europe and the US should push government yields and swap rates down again and should steepen curves.** Japanese bonds should follow the rest of the world, but without a steepening in the curve as the prospect of BoJ easing remains dim.

- A passage of the Paulson plan introduces the world's newest sovereign wealth fund, one that is not really intent on a high return (though it would like to), but one that is intent on pushing asset prices and market liquidity up. The **strategy thus here remains one of buying what the US Treasury buys** and selling what it sells (issues). ABS and MBS prices are already picking up on this, but have further to go. Stay long.

10-yr Government bond yields

	Current	Dec 08	Mar 09	Jun 09	Sep 09
United States	3.81	3.65	3.70	3.70	3.75
Euro area	4.15	4.05	4.00	3.95	3.90
United Kingdom	4.53	4.30	4.30	4.20	4.20
Japan	1.45	1.60	1.60	1.80	2.00

Equities

	Current	YTD Return (local currency)
S&P	1200	-16.3%
Topix	1148	-20.3%
FTSE 100	5088	-16.8%
MSCI Eurozone	176	-25.2%
MSCI Europe	1172	-21.4%

Credit markets

	Current	Dec 08
US high grade (bp over UST)	408	230
US high grade (bp over swaps)	269	171
Euro HG Ind (bp over swaps)	128	116
USD high yield (bp vs. UST)	924	800
EMBIG (bp vs. UST)	405	325

Foreign exchange

	Current	Dec 08	Mar 09	Jun 09	Sep 09
EUR/USD	1.46	1.42	1.40	1.38	1.36
USD/JPY	106	108	110	112	114
GBP/USD	1.84	1.78	1.75	1.75	1.74

Commodities

		Quarterly Average			
	Current	Dec 08	Mar 09	Jun 09	Sep 09
Gold ($/oz)	884	825	875	865	850
Copper($/m ton)	6962	7500	7800	7500	6500
Corn ($/Bu)	5.46	6.30	6.50	6.80	6.60

Source: JPMorgan, Bloomberg, Datastream

Equities

- We moved to a tactical long and reversed several of our defensive trades recently on the view that the recent global policy response, especially the Paulson plan, significantly reduces tail risk. This, coupled with extreme investor pessimism, made it likely that a market rebound will take place in the near term.

- This anticipated rebound failed to materialize last week on concerns not only regarding the approval and the final form of TARP, but also its impact. We continue to believe that the TARP bill will be ultimately passed early this week, supporting equity markets, but admit that **it will take time to restore market confidence** given how fearful people are of

JPMorgan Securities Ltd., London
Jan Loeys (44-20) 7325-5473
jan.loeys@jpmorgan.com
John Normand (44-20) 7325-5222
john.normand@jpmorgan.com

financial failures.

- If the bill is passed and has a positive impact on equity markets, we will look at taking profits soon. Trading and liquidity conditions have worsened materially and investors have shortened their investment horizons. The deterioration in economic data, which is forcing us to lower our already weak growth forecasts, clouds the earnings outlook, even as we still expect that the global economy will escape a deep recession. It is thus likely that a potential market rally will be more muted this time relative to the one in March.

- Investor pessimism has also reached extreme levels in **Emerging Markets.** Recent fund manager surveys show that investors have moved to their largest underweight position in EM equities since 2001. This, along with better valuations in both EM equities and currencies, a stabilization in commodity prices, and our expectation that EM policy response will be more pronounced that the market currently anticipates, especially in China, led us to move to an outright long in EM equities last week. We focus on the under-owned domestic names, especially financials. Across countries we overweight China, underweight Russia, but move Brazil to neutral on an improved macro outlook. We also overweight Mexico and Taiwan, which offer economic reform and counter-cyclical fiscal policy, and overweight Turkey and domestic South Africa to position for an improved inflationary and monetary outlook into 2009 (see *Key Trades and Risks: Emerging Markets Equity Strategy*).

Credit

- Credit spreads widened in tandem with other risky markets. As with equities, we turned more positive last week focusing on **ABS, ABX and nonagency MBS and CMBS**. We stay long in these credits and see significant upside, especially in ABS/ABX, if the Paulson plan is passed.

- **Issuance** has slowed and has not returned after the usual summer slowdown, a reflection of how weak demand is. Cash balances have likely increased among credit investors, after an unprecedented four months of negative net issuance, but so has the issuance backlog. The modest amount of new bond supply is coming at significant concessions to secondary market levels, putting pressure in HG bond spreads. We are thus **more cautious in HG** credit and expect cash bond spreads to widen and underperform CDS as funding conditions remain tight.

Foreign exchange

- **How should one position around TARP?** Medium term or not at all. Last Friday we assumed the Treasury's proposal would win congressional approval, if only for lack of a credible alternative. Stabilizing financials in turn would cap volatility, halt the deleveraging process and sponsor a gradual recovery in carry as counterparty risk receded. None of this would be a straight-line process, but the direction of the risky markets would at least be clearer, which in turn argued for closing yen longs and buying the odd oversold currency (GBP, NOK) which had been overturned by last week's spike in volatility. We were too hopeful in expecting congressional signoff on TARP, but gains on the sterling baskets offset small losses on NOK.

- Despite grandstanding within the Beltway, we maintain that the TARP will pass in a form with sizable balance sheet commitment, but the associated implementation risks are sufficient reason to **avoid moving back into carry now**. At the same time, shorting the higher-yielders also looks like a bad bet, as a number of position metrics suggest that there is very little risk to sell, at least in G-10 currencies. IMMs, for example, show near record longs in JPY and record shorts in AUD. Japanese margin positions have been scaled back meaningfully since July, from NZ$31bn to NZ$13bn, and from A$15bn to A$8bn. Currency manager positions also look quite flat on carry, as evidenced by a change in their beta from positive to zero over the past 2 months.

- Beyond TARP, the prospect of **a synchronized G-3 recession suggests a range on EUR/USD**, owing to offsets from a an equally-bleak outlook in the US and Europe. Expect a 1.40 - 1.48 range in 4Q. We recommend buying a range binary to profit from this consolidation.

Commodities

- We now forecast that **oil prices will pivot around $100** for the rest of this year, weakening into the first half of 2009, before year-end tightening emerges. The supply and demand balance has the potential to be the weakest since 2002, with weather and more aggressive cuts from OPEC being the main upside risk. Prices may have to push below $90 to prompt aggressive OPEC tightening. Downside risks to global growth should keep **base metals under pressure**, even though prices are close to marginal costs. We maintain a neutral to bearish outlook in precious metals as the passage of TARP will likely reduce risk aversion.

JPMorgan Australia Ltd., Sydney
Sally Auld (61-2) 9220-7816
sally.m.auld@jpmorgan.com

Markets - Australia and New Zealand

Australia

- **The RBA announced new liquidity management initiatives and a USD10b swap line with the Fed designed to ease USD funding pressures in the Asian time zone.**
- **We now expect the RBA to cut by 25bps in October, with a further 25bps cut in December. We now expect the cash rate to reach 6.0% by mid-2009.**
- **We continue to recommend defensive fixed income strategies. Position for a steeper 3s10s yield curve and retain long positions in the very front of the yield curve.**

It is clear that downside risks are mounting for the domestic economy. We think the distribution of risks have now shifted enough to prompt the RBA into near term easing. We expect a 25bp rate cut at the RBA's next meeting in October, and a further 25bp in December. We have also revised down our terminal funds rate for the cycle, and expect the RBA cash rate to trough at 6.0% mid next year.

There are a number of issues confronting the RBA at present. The first is a deteriorating global economy. While our economists are not particularly optimistic on the fate of the G3+ economies, they believe that global recession will be averted largely thanks to strength in emerging markets. But this leaves the global economy (and Australia) very exposed to a weaker than expected outcome in the developing economies. Signs of considerable capital outflow from EM regions in recent months may portend a significant tightening of financial conditions, and potentially, a much slower growth outlook.

For an economy which has leveraged itself to the commodity prices boom and growth in developing economies, there are some worrying signs. That said, it is possible that the A$25bn of mining capex might not go ahead thanks to the credit crisis and falling commodity prices. While this is probably not considered large relative to projects already in the pipeline, it underscores how quickly the underlying environment can change; this should be of genuine concern to policymakers.

Tighter monetary policy over the last 5 years has eventually driven a sharp slowdown in household sector activity, leaving the growth outlook quite dependent on the fortunes of the mining sector. A strong mining sector and sluggish household sector growth is probably equivalent to GDP growth of 2-2.5%. But a negative shock to the commodity cycle would mean GDP growth closer to flat for Australia. And don't forget how dependent Australia's fiscal position has been on the profits of mining companies in recent years.

Chart 1: 3-month BBSW/3-month OIS spread, daily data
Percentage Points

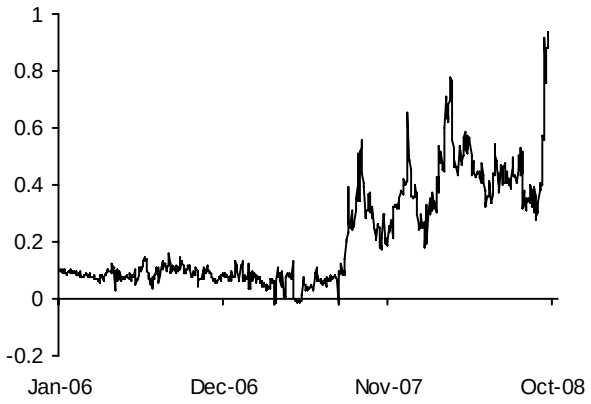
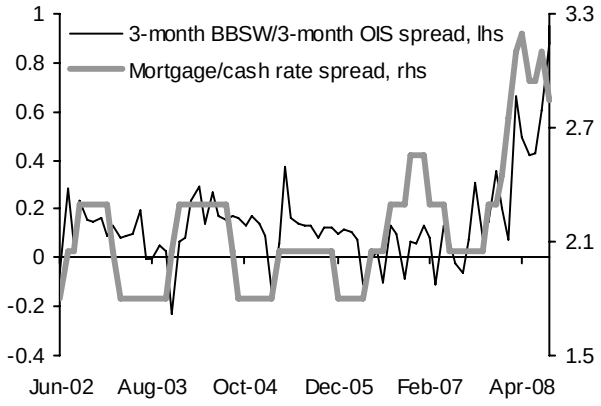


Chart 2: Spread between variable mortgage rate and the RBA cash rate and the 3-month BBSW/3-month OIS spread, monthly data
Percentage Points Percentage Points



The second issue concerns bank funding costs. The variable mortgage rate is the main channel though which monetary policy decisions impact the household sector. But the sharp rise in 3-mth BBSW/3-month OIS spreads (chart 1) have raised the spectre that the domestic banks may not pass on any (or all) of the RBA's easing next month. This means that the RBA may need to cut the cash rate by more than anticipated in order to achieve the desired fall in variable mortgage rates. Chart 2 shows the broad directional relationship between the 3-mth BBSW/3-month OIS spread and the spread between the variable mortgage rate and the RBA cash rate. It illustrates the strong directional relationship between these two variables.

While this may argue for at least 50-75bps of easing by year end, it doesn't necessarily argue for a 50bp rate cut in Octo-

Chart 3: Exchange Settlement Accounts at the RBA, daily data
AUD $m

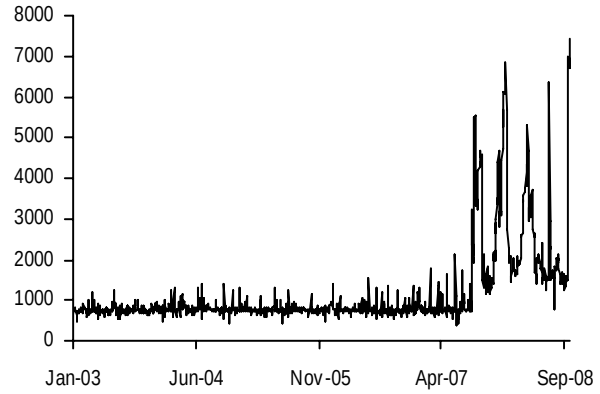
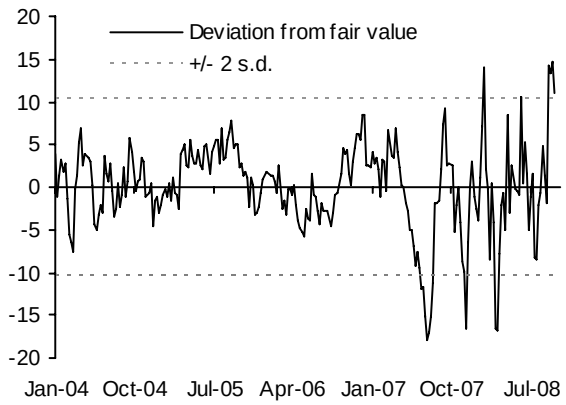


Chart 4: AUS 10-year swap/efp – deviation from fair value
Basis Points



ber. The RBA's preferred strategy may be to cut by 25bp in October, wait for the banks' responses, and then assess whether a further 25bp rate cut is required to effect the desired decline in variable mortgage rates. This implies that to a certain extent, the RBA's policy path may be highly dependent on bank funding costs and the banks' desire to adjust lending margins. But with little relief in libor rates in sight, the risks are biased towards more easing than less in coming months.

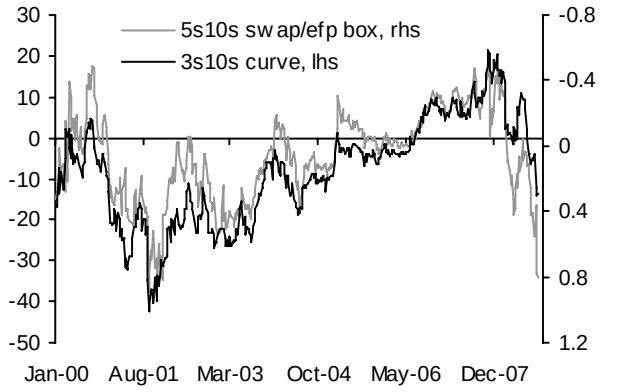
All of this suggests to us that the correct strategies for the local market remain long front end positions and curve steepening positions. The downside risks to growth and continued elevation of bank funding costs imply that the RBA may be forced to cut rates aggressively in coming months. And if the emerging markets growth story takes a leg down, then the risks are clearly biased towards considerably looser monetary policy in Australia next year.

RBA conducts first USD repo

Last week, the RBA conducted its first USD repo operation. While this facility has been in operation for a number of months in other jurisdictions, the RBA announced this initiative just a few days ago. The aim of the USD repo operation is to ease USD funding pressures in the Asian time zone.

The auction was for USD10b, with a minimum bid rate of 2.35% (USD 1-mth OIS + 50bps). All $10b was taken, at a weighted average rate of 3.165% (81.5bps above the min bid rate) and a bid/cover ratio of 1.3. The results suggest robust demand for the facility (although we note that the bid/cover ratio for the Fed's last TAF auction was 1.7). We would expect more of

Chart 5: 3s10s curve and 5s10s swap/efp box spread
Basis Points Percentage Points



these auctions to be announced, given that there seems to be little relief in sight in libor markets.

The other initiative announced by the RBA was a term deposit facility. The RBA will accept term deposits from any organisation with access to the exchange settlement accounts and/or ADIs. The deposits will occur via auction – the first one is for 14 days starting on 29 Sept. This initiative is essentially to help out with the RBA's liquidity management purposes – it is just a way in which the RBA can drain liquidity from the market when so desired and is simply the equivalent

of issuing a liability. It should give depositors the opportunity to earn more than they would if their cash was parked in the exchange settlement account (which offer cash less 25bps). And in doing so, it should reduce the huge ES balances (a reflection of excess liquidity) which have been a feature over the last little while (chart 3). We would view this initiative as one designed more to help the RBA with its liquidity operations and balance sheet management (ie increase control of liquidity), rather than anything reflective of risk aversion or funding pressures. We do not think this intitiative has any immediate implications for the monetary policy outlook.

10-year swap/efp spread looks too narrow

On a number of measures, we think 10-yr swap spreads are too narrow. Modelling swap spreads is difficult at the best of times given the array of factors that can influence the market. But our model, which is based on US bond market volatility and the 3-mth/10-yr spread, suggests that 10-yr swap/efp spreads are too narrow (chart 4). When we look at the 5s10s swap/efp box and the 3s10s bond curve, then it is clear that the 10-year swap/efp spread is too narrow (or alternatively, the 3s10s curve is not steep enough).

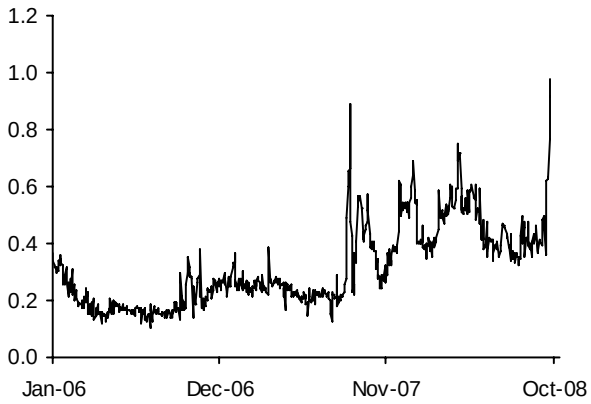
What is driving the mis-pricing in 10-yr swap/efp spreads? There have been a number of flows which have pressured long end swap/efp spreads to narrow. An unwind of swap 2s10s steepeners (driven by a sharp widening of 2-year swap/efp spreads) has been one flow of note. Issuance of more power reverse dual currency structures from Japan has also driven receive-side flows in the 10-year sector.

Once these flows have diminished, we expect payside pressure to emerge in the 10-year sector. Continued volatility and pressure on 3-month rates suggest swap/efp spreads will remain under widening pressure. And if repo markets come under stress, then swap spreads should widen as a matter of course. In the first instance, we target a move back to 90bps, but we would not be surprised to see this spread move back to the top of the recent trading range (100bps) – see chart 6.

Trade recommendations

- Pay AUD 10-yr swap/efp spread. Enter a paid position in the 10-yr swap/efp spread. Target a move to 90bps in the first instance, and with a medium term target of 100bps. Enter half the position (25k DV01) at a spread of 80bps and look to add on any move to the mid to high 70s. Place a stop at 72bps.
- Hold 3s/10s Aussie curve steepener in futures. Expectations of RBA easing should see the curve steepen. We are thus recommending strategic curve steepening positions in AUD. The trade has moved our way, but has further to run. We recommended buying the curve at a spread of 3bps, and have a revised target of +40bps and a revised stop of +10bps. The curve currently is at 31.0bps, for a 28bps gain.

Chart 7: 3-month BBSW/3-month OIS spread, daily data
Percentage Points



New Zealand

- **NZ economy officially in recession. We now expect the RBNZ to cut by 50bps in October and think that the OCR will reach 6% by mid 2009.**
- **Pressure on the 3-mth rate set continues to plague Kiwi fixed income markets. The 3-month BKBM spread to 3-month OIS is now at a record wide.**

Recent weeks have seen considerable stresses in overnight and short term money markets. The USD libor market is one notable example. But it is interesting to observe that the NZ market has not been immune to these stresses. In the last 2 weeks, the 3-mth rate has risen by 45bps, and the 3-mth libor/3-mth OIS spreads is at a record wide (chart 7). In Australia, the rise in the 3-mth rate has been 14bps over this period.

JPMorgan Australia Ltd., Sydney
Sally Auld (61-2) 9220-7816
sally.m.auld@jpmorgan.com

What has driven this dislocation? To a certain extent, the similar dynamics that have pressured short term money markets around the world. But there are also factors specific to the NZ market, namely the 30 September end of financial year for a number of the local banks. We suspect a number of these organisations are long cash into year end, and once Sept 30 passes, we expect pressures on the 3-mth rate set to ease. In our view, we think that the 3-mth rate could fall back around to the 7.8-7.9% level this week. If a fall of this magnitude is not forthcoming, then we would start to worry that elevated 3-month rates were reflective of broader and more fundamental dysfunction in global financial markets.

Trade recommendations

- Hold the 2s10s curve steepener in NZ spot swap. This trade has moved in our favour over the last week, with the 2s10s swap curve now at -17bps (a profit of 7.5bps). We continue to recommend strategic curve steepening positions in New Zealand, but are mindful of stresses in the 3-month rate set. This could pressure front end swap rates higher, and as such, we have moved our stop up to -24.5bps.

JPMorgan Chase Bank, New York
David Hensley (1-212) 834-5516
david.hensley@jpmorgan.com
Carlton Strong (1-212) 834-5612
carlton.m.strong@jpmorgan.com

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
The Americas														
United States	2.0	1.6 ↓	0.6 ↓	0.9	2.8 ↓	0.0 ↓	-0.5 ↓	-0.5 ↓	1.0 ↓	2.5 ↓	4.3	4.3	2.8	1.8 ↓
Canada	2.7	0.7	1.9	-0.8	0.3	0.8	1.5	2.0	2.5	2.8	2.4	3.2	2.0	2.0
Latin America	5.2 ↓	3.9 ↓	2.7 ↓	0.9 ↑	4.9 ↓	2.5 ↓	2.4 ↓	1.2 ↓	3.5 ↑	3.9 ↑	7.5	8.0 ↓	7.5 ↓	6.5 ↓
Argentina	8.7	6.5	3.0	2.4	8.7	4.5 ↓	2.8	2.0 ↓	2.0 ↓	3.6 ↑	9.1	8.8	8.6	9.8
Brazil	5.4	5.2	3.2 ↓	3.4	6.5	3.4 ↑	3.1 ↓	2.0 ↓	4.1 ↑	3.0 ↓	5.6	6.2 ↓	6.3 ↓	5.1 ↑
Chile	5.1	4.0	3.0	6.8	7.4	2.5	-2.0	3.0	3.0	7.0	8.9	8.8	7.3	4.6
Colombia	7.7 ↓	3.7	3.6	-0.8 ↑	2.6 ↓	4.8 ↓	4.3 ↓	2.0 ↑	3.0 ↑	5.0 ↑	6.4	7.0	5.5	4.9
Ecuador	2.0	2.5	2.5	2.0	3.5	4.0	4.0	2.5	2.0	1.5	9.1	9.8	5.9	4.9
Mexico	3.2	1.6 ↓	1.6 ↓	-0.5	0.6	0.0 ↓	0.5 ↓	0.5 ↓	3.0	4.1	4.9	5.3 ↓	4.5 ↓	3.7 ↓
Peru	8.9 ↓	9.2	6.1	7.5	10.1 ↓	6.1	5.1	2.8	10.1	6.0	5.5	6.1	4.5	3.5
Venezuela	8.4	5.0	3.5	-12.5	15.0	5.0	10.0	-2.5	2.5	3.5	31.0	33.9	33.6	31.2
Asia/Pacific														
Japan	2.0	0.5	0.5	2.8	-3.0	-0.5	0.2	0.7	1.2	1.7	1.4	1.8	1.4	1.1
Australia	4.2	2.7	2.6	2.7	1.1	2.6	3.2	3.2	2.0	2.4	4.5	4.6	3.2	3.0
New Zealand	3.2 ↑	0.6 ↑	1.6 ↑	-1.2 ↓	-0.6 ↑	-1.3	0.2	2.4	3.1	3.2	4.0	5.2	4.3	3.0
Asia ex. Japan	8.8	7.1 ↓	6.5 ↓	8.6	6.6	5.7 ↑	5.5 ↓	5.5 ↓	6.9 ↓	8.1 ↑	7.0	5.8 ↑	3.6	3.9 ↓
China	11.9	10.1	9.5	11.7	11.5	8.7	9.0	9.0	9.5	10.4	7.8	4.1	2.4	3.7
Hong Kong	6.4	3.5 ↓	1.8 ↓	8.2	-5.5	0.2 ↓	-1.0 ↓	-0.5 ↓	5.5 ↓	6.5	5.7	2.4 ↓	1.9 ↓	4.1 ↓
India	9.0	7.0	7.5	9.8	5.9	7.0 ↑	5.8 ↓	5.0 ↓	7.2 ↓	8.5 ↑	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	3.7 ↓	3.3	3.4	3.0	3.0 ↓	3.3 ↓	4.0 ↓	5.0 ↓	4.8	5.0	3.4	3.1
Malaysia	6.3	5.1 ↑	3.0 ↓	6.0	3.7	1.2 ↑	0.8	0.8 ↓	4.5 ↓	7.0 ↓	4.9	7.1	4.9	2.3
Philippines	7.2	4.4	4.3	4.2	6.2	2.0	3.0 ↑	4.5 ↓	4.5 ↓	6.0	9.7	8.0	4.3	3.7
Singapore	7.7	3.3 ↓	1.9 ↓	15.7	-6.0	2.0 ↓	0.8 ↓	-3.2 ↓	4.9 ↑	9.1 ↑	7.5	4.7	1.2	2.8
Taiwan	5.7	3.5 ↓	2.7 ↓	3.3	1.3	0.9 ↓	1.2 ↓	1.8 ↓	3.8 ↓	5.5	4.2	2.7 ↑	2.7 ↓	1.6 ↓
Thailand	4.8	4.6 ↑	3.5 ↓	6.0	2.3	1.0 ↑	1.5 ↑	3.0 ↑	4.0 ↑	5.0	7.5	11.3	6.5	5.0
Africa														
South Africa	5.1	3.3	2.5 ↓	2.1	4.9	1.5 ↑	-0.9 ↓	2.7 ↑	3.1 ↓	4.8 ↓	11.6	12.6 ↓	8.0 ↓	6.6
Europe														
Euro area	2.6	1.1	0.4	2.7	-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	1.7 ↑	-1.3 ↓	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	1.2	-0.2	3.9	1.5	0.5	0.5	1.2	1.5	3.2	4.0	3.7	1.8
Sweden	2.9	1.0	0.8	0.5	-0.1	1.0	0.5	0.5	0.8	1.5	3.8	3.7	2.8	2.1
Switzerland	3.3	2.0	1.1	1.1	1.5	0.5	0.5	1.0	1.5	1.5	2.7	2.2	1.1	1.1
United Kingdom	3.1	1.0	0.4	1.1	0.2	-1.0	-1.0	0.5	1.0	2.0	3.4	4.9	3.4	2.1
Emerging Europe	6.5	5.8	4.5 ↓	6.4	6.4	4.7	4.4 ↓	4.0	4.4	4.7	10.2	9.2	7.8	7.2
Bulgaria	6.2	5.2	5.5	…	…	…	…	…	…	…	…	…	…	…
Czech Republic	6.6	4.5	2.5	3.8	3.6	3.5	5.0	0.5	1.0	2.0	6.8	5.3	2.0	2.3
Hungary	1.3	2.2	2.5 ↓	2.2	2.3	2.5	2.0 ↓	2.0 ↓	2.5 ↑	3.0	6.8	5.7	4.4	3.8
Poland	6.6	5.3	4.3	5.7	6.1	4.0	3.5	2.8	3.5	4.5	4.3	3.9	3.8	3.3
Slovak Republic	10.4	7.0	3.5	8.7	5.3	5.0	0.0	5.0	4.0	4.0	4.5	4.1	3.2	3.7
Romania	6.0	8.5	3.5	…	…	…	…	…	…	…	8.6	6.4	5.8	5.5
Russia	8.1	7.4	5.8	7.2	7.3	5.5	5.5	5.5	6.0	6.0	14.8	13.4	11.7	11.1
Turkey	4.6	3.8	4.0	…	…	…	…	…	…	…	10.3	10.0	8.5	7.2
Global	3.5	2.2 ↓	1.6 ↓	2.6	1.7 ↓	0.8 ↓	0.8 ↓	1.1 ↓	2.0 ↓	2.9 ↓	4.4	4.4	3.1 ↓	2.5
Developed markets	2.4	1.2 ↓	0.6 ↓	1.7	0.5 ↓	-0.2 ↓	-0.1 ↓	0.2 ↓	1.0 ↓	2.0 ↓	3.5	3.7	2.5	1.8
Emerging markets	7.5	6.0 ↓	5.2 ↓	6.2	6.1	4.6 ↓	4.4 ↓	4.1 ↓	5.6 ↓	6.4 ↑	7.8	7.1	5.4 ↓	5.2

JPMorgan Chase Bank, New York
David Hensley (1-212) 834-5516
david.hensley@jpmorgan.com
Donald Martis (1-212) 834-5667
donald.j.martis@jpmorgan.com

Global Central Bank Watch

	Official interest rate	Current	Change from Aug 07 (bp)	Last change	Next meeting	Forecast next change	Sep 08	Dec 08	Mar 09	Jun 09	Dec 09
Global	GDP-weighted average	3.81	-90				3.81	3.65	3.55	3.43	3.37
excluding US	GDP-weighted average	4.67	20				4.67	4.67	4.52	4.34	4.25
Developed	GDP-weighted average	2.84	-130				2.84	2.62	2.52	2.40	2.38
Emerging	GDP-weighted average	7.74	68				7.74	7.85	7.73	7.57	7.36
Latin America	GDP-weighted average	10.41	160				10.41	10.86	10.85	10.82	10.47
CEEMEA	GDP-weighted average	8.13	87				8.13	8.13	8.12	7.80	7.35
EM Asia	GDP-weighted average	6.60	28				6.60	6.62	6.43	6.28	6.20
The Americas	GDP-weighted average	2.99	-260				2.99	2.63	2.63	2.62	2.62
United States	Federal funds rate	2.00	-325	30 Apr 08 (-25bp)	29 Oct 08	**16 Dec 08 (-50bp)**	2.00	1.50	1.50	1.50	1.50
Canada	Overnight funding rate	3.00	-150	22 Apr 08 (-50bp)	21 Oct 08	20 Oct 09 (+25bp)	3.00	3.00	3.00	3.00	3.50
Brazil	SELIC overnight rate	13.75	225	10 Sep 08 (+75bp)	30 Oct 08	30 Oct 08 (+50bp)	13.75	14.75	14.75	14.75	14.00
Mexico	Repo rate	8.25	100	15 Aug 08 (+25bp)	18 Oct 08	on hold	8.25	8.25	8.25	8.25	8.25
Chile	Discount rate	8.25	275	4 Sep 08 (+50bp)	9 Oct 08	9 Oct 08 (+50bp)	8.25	9.00	9.00	8.50	7.75
Colombia	Repo rate	10.00	75	25 Jul 08 (+25bp)	24 Oct 08	1Q 09 (-25bp)	10.00	10.00	9.75	9.75	9.50
Peru	Reference rate	6.50	175	11 Sep 08 (+25bp)	9 Oct 08	9 Oct 08 (+25bp)	6.50	7.00	7.00	7.00	7.00
Europe/Africa	GDP-weighted average	4.81	21				4.81	4.77	4.56	4.27	4.05
Euro area	Refi rate	4.25	25	3 Jul 08 (+25bp)	2 Oct 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)	9 Oct 08	6 Nov 08 (-25bp)	5.00	4.75	4.50	4.00	4.00
Sweden	Repo rate	4.75	125	4 Sep 08 (+25bp)	23 Oct 08	11 Feb 09 (-25bp)	4.75	4.75	4.50	4.25	4.00
Norway	Deposit rate	5.75	100	25 Jun 08 (+25bp)	29 Oct 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)	6 Nov 08	**6 Nov 08 (-25bp)**	3.50	3.25	3.00	2.75	2.50
Hungary	2-week deposit rate	8.50	75	26 May 08 (+25bp)	29 Sep 08	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)	29 Oct 08	2Q 09 (-25bp)	6.00	6.00	6.00	5.75	5.25
Romania	Base rate	10.25	325	31 Jul 08 (+25bp)	30 Oct 08	**30 Oct 08 (+25bp)**	10.25	10.50	10.75	11.00	10.50
Russia	1-week deposit rate	4.25	100	11 Jul 08 (+25bp)	Sep 08	3Q 09 (+25bp)	4.25	4.25	4.25	4.25	4.50
Slovak Republic	2-week repo rate	4.25	0	27 Apr 07 (-25bp)	30 Sep 08	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	10.00
Switzerland	3-month Swiss Libor	2.75	25	13 Sep 07 (+25bp)	11 Dec 08	on hold	2.75	2.75	2.75	2.75	2.75
Turkey	Overnight borrowing rate	16.75	-75	17 Jul 08 (+50bp)	23 Oct 08	Apr 09 (-25bp)	16.75	16.75	16.75	16.00	14.50
Asia/Pacific	GDP-weighted average	3.69	15				3.69	3.66	3.56	3.47	3.56
Australia	Cash rate	7.00	50	2 Sep 08 (-25bp)	7 Oct 08	**7 Oct 08 (-25bp)**	7.00	6.50	6.25	6.00	6.00
New Zealand	Cash rate	7.50	-75	11 Sep 08 (-50bp)	23 Oct 08	**23 Oct 08 (-50bp)**	7.50	6.75	6.25	6.00	6.00
Japan	Overnight call rate	0.50	0	21 Feb 07 (+25bp)	6 Oct 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)	30 Oct 08	18 Mar 09 (+25bp)	3.50	3.00	3.00	3.00	3.00
China	1-year working capital	7.20	18	15 Sep 08 (-27bp)	4Q 08	1Q 09 (-27bp)	7.20	7.20	6.93	6.66	6.66
Korea	Base rate	5.25	25	7 Aug 08 (+25bp)	8 Oct 08	**1Q 09 (-25bp)**	5.25	5.25	4.75	4.75	4.75
Indonesia	BI rate	9.25	100	4 Sep 08 (+25bp)	8 Oct 08	8 Oct 08 (+25bp)	9.25	9.50	9.75	9.75	9.75
India	Repo rate	9.00	125	29 Jul 08 (+50bp)	24 Oct 08	24 Oct 08 (+25bp)	9.00	9.25	9.25	9.00	8.50
Malaysia	Overnight policy rate	3.50	0	26 Apr 06 (+25bp)	24 Oct 08	on hold	3.50	3.50	3.50	3.50	3.50
Philippines	Reverse repo rate	6.00	0	28 Aug 08 (+25bp)	9 Oct 08	on hold	6.00	6.00	6.00	6.00	6.00
Thailand	1-day repo rate	3.75	50	27 Aug 08 (+25bp)	8 Oct 08	on hold	3.75	3.75	3.75	3.75	3.75
Taiwan	Official discount rate	3.50	38	**25 Sep 08 (-12.5bp)**	Dec 08	**Dec 08 (-12.5bp)**	3.50	3.375	3.25	3.25	3.25

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

JPMorgan Chase Bank, Sydney
Stephen Walters (61-2) 9220-1599
stephen.b.walters@jpmorgan.com
Helen Kevans (61-2) 9220-3250
helen.e.kevans@jpmorgan.com

Forecasts - Australia and New Zealand

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

				2007			2008				2009			
	2007	2008	2009	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Chain volume GDP	4.2	2.7	2.6	3.3	4.3	2.8	2.7	1.1	2.6	3.2	3.2	2.0	2.4	2.3
Private consumption	4.5	2.7	1.7	2.5	4.1	5.7	2.6	-0.6	2.8	2.0	1.2	1.6	2.0	2.4
Construction investment	9.8	3.2	3.3	3.1	10.0	-3.0	9.7	-4.6	6.1	3.0	5.1	2.0	1.9	5.9
Equipment investment	9.6	14.7	5.8	24.1	-0.6	16.2	-1.3	53.4	13.2	4.2	-2.1	4.2	0.0	8.6
Public investment	5.7	14.0	6.2	72.3	-27.7	30.6	27.5	9.8	5.8	5.7	5.8	6.0	6.3	6.7
Government consumption	2.4	4.2	3.3	1.0	5.5	5.8	2.4	4.8	5.4	3.7	3.5	2.2	1.8	2.2
Exports of goods & services	3.2	5.5	5.1	0.8	8.8	-2.6	7.7	11.1	4.1	6.1	4.1	4.1	6.1	4.1
Imports of goods & services	10.8	11.8	4.4	7.1	11.1	13.4	18.2	9.3	8.2	4.1	2.0	4.1	5.1	2.0
Contributions to GDP growth:														
Domestic final sales	5.3	4.7	2.8	6.8	3.6	6.8	4.8	3.5	4.5	3.0	2.2	2.3	2.1	3.8
Inventories	0.6	-0.3	-0.1	-1.9	1.5	-0.2	0.7	-2.2	-0.6	0.0	0.6	-0.1	0.3	-1.8
Net trade	-1.8	-1.7	-0.1	-1.4	-0.8	-3.5	-2.6	-0.1	-1.2	0.2	0.3	-0.2	0.0	0.3
GDP deflator (%oya)	3.8	5.6	3.2	4.0	3.2	3.5	3.7	6.7	6.3	5.6	5.2	2.6	2.6	2.5
Consumer prices (%oya)	2.3	4.5	3.3	2.1	1.9	3.0	4.2	4.5	4.6	4.6	3.9	3.2	3.1	3.0
Producer prices (%oya)	2.3	8.5	3.4	1.5	0.8	3.4	6.9	8.7	9.8	8.7	6.1	2.5	2.5	2.5
Trade balance (A$ bil, sa)	-20.7	-2.7	15.6	-4.6	-5.4	-6.9	-8.0	-0.5	2.5	3.4	4.0	4.2	3.6	3.8
Current account (A$ bil, sa)	-67.0	-50.4	-33.5	-16.4	-16.8	-19.0	-19.8	-12.8	-9.3	-8.5	-8.0	-8.0	-8.8	-8.7
as % of GDP	-6.2	-4.3	-2.7	-6.1	-6.1	-6.8	-7.0	-4.4	-3.1	-2.8	-2.6	-2.6	-2.8	-2.8
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	1.4	1.7											
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	3.9	0.8	-0.3	1.5	5.6	10.2	1.6	0.0	-1.0	3.0	2.5	1.0	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	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

JPMorgan Chase Bank, Sydney
Stephen Walters (61-2) 9220-1599
stephen.b.walters@jpmorgan.com
Helen Kevans (61-2) 9220-3250
helen.e.kevans@jpmorgan.com

Australia and New Zealand economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
29 Sep New Zealand: Trade balance (10:45am) Aug	30 Sep Australia: Pvt. sector credit (11:30am) Aug 0.3 %m/m, sa Retail sales (11:30am) Aug 0.2 %m/m, sa Building approvals (11:30am) Aug 1.5 %m/m, sa New Zealand: Building permits (10:45am) Aug NBNZ bus. conf. (03:00pm) Sep	1 Oct	2 Oct Australia: Trade balance (11:30am) Aug -250 A$ mn New Zealand: ANZ commodity price (03:00pm) Sep	3 Oct
6 Oct Australia: ANZ job ads (11:30am) Sep *Holiday Australia*	7 Oct Australia: RBA cash target (02:30pm) Oct	8 Oct Australia: Westpac consumer confidence (10:30am) Oct Housing finance (11:30am) Aug	9 Oct Australia: Unemployment rate (11:30am) Sep	10 Oct
13 Oct New Zealand: Retail sales (10:45am) Aug QV house prices Sep	14 Oct Australia: NAB business confidence (11:30am) Sep New Zealand: NZIER bus. opinion survey (10:00am) 3Q	15 Oct Australia: WMI leading index (10:30am) Aug	16 Oct New Zealand: PMI (12:00pm) Sep	17 Oct
20 Oct Australia: PPI (11:30am) 3Q	21 Oct Australia: New motor vehicles sales (11:30am) Sep New Zealand: CPI (10:45am) 3Q Credit card spending (03:00pm) Sep	22 Oct Australia: CPI (11:30am) 3Q	23 Oct New Zealand: RBNZ official cash rate (09:00am) Oct	24 Oct

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

JPMorgan Chase Bank, New York
Sam Conway (1-212) 834-9123
samuel.e.conway@jpmorgan.com

Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
29 Sep - 3 Oct	29 September	30 September	1 October	2 October	3 October
	Euro area • EC bus surv (Sep) Hungary • NBH meeting Japan • Retail sales (Aug) United Kingdom • M4 lending final (Aug) • Mortgage approvals (Aug) United States • Personal income (Aug)	Euro area • HICP flash (Sep) • Trichet speech Germany • Employment (Aug) • Unemployment (Sep) Japan • Hhold spending (Aug) • Housing starts (Aug) • IP prelim (Aug) • PMI mfg (Sep) • Shoko Chukin (Sep) • Unemployment (Aug) Korea: IP (Aug) United Kingdom • GDP final (2Q) United States • Chicago Fed bus surv (Sep) • S&P C-S HPI (Jul)	China: PMI mfg (Sep) Euro area • PMI mfg final (Sep) • Unemployment (Aug) • Trichet speech Germany • Retail sales (Aug) Japan • BoJ Tankan (3Q) • Nominal wages (Aug) Korea • CPI (Sep) • Trade balance (Sep) United Kingdom • PMI mfg (Sep) United States • ADP employment (Sep) • Construct spend (Aug) • ISM mfg (Sep) • Vehicle sales (Sep)	Brazil • IP (Aug) Euro area • ECB meeting Singpore • PMI (Sep) United Kingdom • BoE credit cond surv (3Q) • Nationwide HPI (Sep) United States • Factory orders (Aug)	Euro area • PMI serv final (Sep) • Retail sales (Aug) Switzerland • CPI (Sep) United Kingom • PMI services (Sep) United States • Employment report (Sep) • ISM nonmfg (Sep)
6 Oct - 10 Oct	6 October	7 October	8 October	9 October	10 October
Japan • Cabinet Office private consumption index (Aug) United Kingdom • Halifax HPI (Sep)	Canada • Ivey PMI (Sep) Taiwan • CPI (sep)	Australia • RBA meeting Germany • Mfg orders (Aug) Indonesia • BI meeting Japan • BoJ meeting Taiwan • Trade balance (Sep) United States • Consumer credit (Aug) • FOMC minutes • Bernanke speech	Brazil • IPCA (Sep) Euro area • GDP final (2Q) Germany • IP (Aug) Japan • Econ watcher surv (Sep) Thailand • BoT meeting South Africa • Mfg production (Aug) United States • Pending home sales (Aug)	Germany • Trade balance (Aug) Japan • Machinery orders (Aug) Mexico • CPI (Sep) Sweden • CPI (Sep) United States • Wholesale trade (Aug) Central bank meetings • Chile • Korea • Peru • Philippines • South Africa • United Kingdom	Canada • Employment (Sep) • Loan Officer Survey • Trade balance (Aug) Japan • BoJ minutes: 16-17 Sep Norway • CPI (Sep) United States • International trade (Aug)

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Economic Research and Global Currency Strategy at JPMorgan

Global Economics

Chief Economist
Bruce Kasman, New York (1-212) 834-5515

Economics: Global

David Hensley (1-212) 834-5516
Joseph Lupton (1-212) 834-5735
Sam Conway (1-212) 834-9123

Data and Forecast Systems

Carlton Strong (1-212) 834-5612
Donald Martis (1-212) 834-5667
Silvana Dimino (1-212) 834-5684

Economics: United States and Canada

United States

Robert Mellman, New York (1-212) 834-5517
Michael Feroli (1-212) 834-5523
Abiel Reinhart (1-212) 834-5614

Economics: Latin America

Brazil

Fabio Hashizume, São Paulo (55-11) 3048-3634
Julio Callegari, São Paulo (55-11) 3048-3369

Colombia, Ecuador, Venezuela, Peru

Luis Oganes, New York (1-212) 834-4326
Andres Ortiz, New York (1-212) 834-7351
Benjamin Ramsey, New York (1-212) 834-4308

Argentina, Chile

Vladimir Werning, New York (1-212) 834-8144
Florencia Vazquez, Buenos Aires (54-11) 4348-3405

Mexico

Alfredo Thorne, Mexico City (525) 540-9558
David Franco, Mexico City (525) 540-9339

Economics: Asia/Pacific

Head of Japan

Masaaki Kanno, Tokyo (81-3) 6736-1166

Japan

Masamichi Adachi, Tokyo (81-3) 6736-1172
Miwako Nakamura, Tokyo (81-3) 6736-1167

Head of Emerging Asia Economic Research

David G. Fernandez, Singapore, (65) 6882-2461

Greater China

Frank Gong, Hong Kong (852) 2800-7006
Grace Ng, Hong Kong (852) 2800-7002
Qian Wang, Hong Kong (852) 2800-7009
Peng Chen, Hong Kong (852) 2800-7005

Korea

Jiwon Lim, Seoul (822) 758-5509

Indonesia, Malaysia, Philippines, Singapore, Thailand

Sin Beng Ong (65) 6882-7143
Matthew Hildebrandt (65) 6882-2253

Australia, New Zealand

Stephen Walters, Sydney (61-2) 9220 -1599
Helen Kevans (61-2) 9220-3250

Economics: Europe/Africa

Head of Western Europe
David Mackie, London (44-20) 7325-5040

United Kingdom, Switzerland

Malcolm Barr, London (44-20) 7777-1080
Allan Monks, London (44-20) 7777-1188

Euro area

Silvia Pepino, London (44-20) 7325-4250
Maryse Pogodzinski, Paris (33-1) 4015-4225
Marta Bastoni, London (44-20) 7325-9114

Scandinavia

Nicola Mai, London (44-20) 7777-3467

Czech Republic, Hungary, Poland, Slovakia

Nora Szentivanyi, London (44-20) 7777-3981
Ryszard Jakubowski, London (44-20) 7777-4504

CEEMEA

Michael Marrese, New York (1-212) 834-4876
Eva Sanchez, New York (1-212) 834-8217

Turkey, Bulgaria, the Baltics

Yarkin Cebeci, Istanbul (90-212) 326-8590

Russia, Ukraine, Bulgaria, Kazakhstan

Nina Chebotareva, Moscow (7-095) 937-7321

Africa

Graham Stock (44-20) 7777-3430

FX Strategy Management

Global Head of Emerging Markets and FX Strategy Research
Joyce Chang (1-212) 834-4203

FX Strategy: United States

Global FX Strategists
Kenneth Landon (1-212) 834-2391
Rebecca Patterson (1-212) 834-4254
Karim Pakravan (1-312) 325-3164

FX Analysts

Holly Huffman (1-212) 834-4953
Arindam Sarndilya (1-212) 834-2304

FX Strategy: Europe

Global FX Strategist
Paul Meggyesi (44-20) 7859-6714

Global FX and Fixed Income Strategist
John Normand (44-20) 7325-5222

Emerging Markets FX Strategist
Nandita Singh (44-20) 7777-3413

FX Analysts
Frida Gjorstrup (44-20) 7777-1503

FX Strategy: Asia

Global FX Strategists
Claudio Piron (65) 6882-2218
Tohru Sasaki (81-3) 5570-7717
Junya Tanase (81-3) 5570-7718

FX Analysts
Yen Ping Ho (65) 6882-2216

FX/Commodities

Technical Strategists
Robin Wilkin (44-20) 7777-1345
Niall O'Connor (1-212) 834-5108

Global Metals Strategist
Jon Bergtheil (44-20) 7325-6433
Michael Jansen (44-20) 7325-5882

Agricultural Commodity Strategist
Lewis Hagedorn (1-312) 325-6409