Australia and New Zealand - Weekly Prospects

Summary

- The 100bp rate cut delivered by the RBA last week was twice market expectations and signalled that officials want to stay well ahead of developments in financial markets and the real economy. The rate cut was all about getting mortgage rates down. We expect another 50bp cut in early November, and a cash rate of 4.5% by mid-2009. The Government announced over the weekend that it will guarantee deposits at banks, building societies and credit unions, and wholesale term funding issued by banks and other deposit taking institutions. The Government also will double the public funds committed to purchasing RMBS to A$8 billion. We have lowered the forecast for growth in **Australia's economy** for 2009 to just 1.8% (from 2.5%); we now expect virtually no growth in household spending in 2009. The risks are to the downside.

- The **RBNZ** surprisingly left the official cash rate (OCR) unchanged last week even though other central banks across the globe were easing policy. Following news of coordinated rate action among central banks, we thought the RBNZ might deliver an inter-meeting rate cut, especially given that the economy (already in recession) is battling more headwinds than most. Retail sales data today unexpectedly rose 0.4%m/m in August, but there is pain for households ahead. The household sector remains under significant pressure from still-high interest rates, alongside elevated food and energy prices, and the rapidly deteriorating housing market.

- The **global financial crisis** has risen to a fever pitch. Despite a coordinated easing in global monetary policy, unsecured funding markets are experiencing intensified stress. US commercial paper outstanding contracted and interbank lending rates rose further across the board. The 3-mth USD LIBOR/OIS spread widened out to a record 364bp. Emerging market corporate financing is now under significant pressure, with our index of EM corporate overseas borrowing rates up more than 300bp in less than four weeks. Adding significant insult to the injury already being inflicted on credit markets, global equities fell about 20% last week and are down over 40% for the year.

- The outlook for the **emerging economies** is dimming rapidly. The continued slide in the G3 economies is taking an increasing toll on EM exports and industrial production. In addition, the associated collapse in investor risk appetite has produced a sharp decline in the prices of EM financial assets and a drying up of dollar funding, which is feeding back negatively on domestic demand. In response, we have made a succession of forecast downgrades that put EM growth at 4% over the four quarters ending 2Q09—2% points below our estimate of trend.

- We still expect a large fiscal stimulus from **China** in the form of tax cuts and spending on infrastructure, as well as monetary policy easing via cuts in interest rates and the RRR. Additional and more widespread easing also is on the way in the rest of EM Asia, where recent data are menacingly bad. Bellwether Taiwan's exports collapsed in September.

This week's highlight

With the data schedule in Australia and New Zealand quiet, the highlight will be developments offshore; in particular, the coordinated steps the G7 and G20 leaders resolve to take to address the global financial crisis.

Contents

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Data and event previews - Australia and New Zealand

Date [(a)]	Data/event	Forecast		*Previous*	Comment
		JPMorgan	Consensus		
Monday, 13 October (11.30am)	**Aust. ANZ job advertisements (Sep, %m/m)**	**-3.0**	na	***-4.9***	Job ads plunged nearly 5% in August and probably will be lower again in September. Employers clearly now are more cautious about hiring. We expect job growth of only 0-5,000 persons per month from here, and an unemployment rate with a 6% "handle" in late 2009.
Tuesday, 14 October (11.30am)	**Aust. NAB business confidence (Sept., %m/m)**	**-13**	na	*-7*	Business confidence will sink in the NAB business survey, given what is happening in global financial markets. Confidence already was under pressure despite lower official interest rates, but any relief provided by the RBA's rate cut (and the prospect of more to come) probably will be swamped by pessimism about global financial instability and the prospect of much lower economic growth, both globally and in Australia.
Wednesday, 15 October (10.30am)	**Aust. Westpac leading index (Aug., %m/m)**	**na**	na	*0.2*	na
Thursday, 16 October (10.30am)	**NZ PMI (Sept., index)**	**na**	na	*45.7*	na

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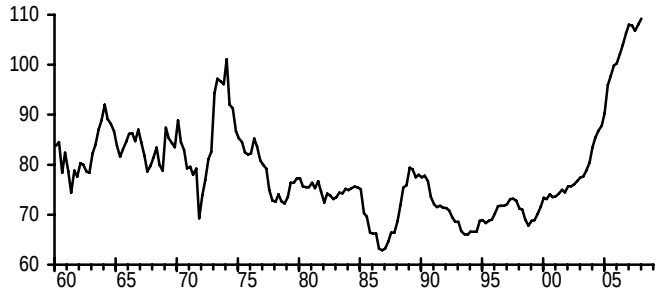
Feature charts

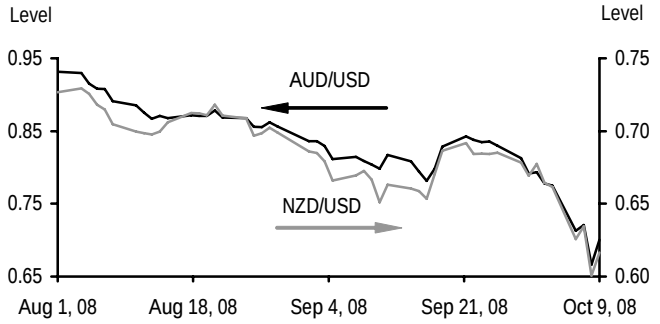
Australia: terms of trade

2004-05=100, sa



Until last week, RBA officials regularly highlighted the importance of the booming terms of trade as a powerful source of support for national income and spending power. The deteriorating outlook for the global economy means, however, that global demand will moderate; we now forecast a global recession. This suggests that commodity prices will ease, and the terms of trade will decline next year. Indeed, the long terms of trade boom is over.

Antipodean currencies have fallen significantly



Since the start of August, the AUD and NZD have shed 28% and 17%, respectively, against the US dollar. The sharp decline in the Antipodean currencies has emerged alongside a significant deterioration in global sentiment and falling commodity prices. The currencies' favourable yield advantage also is narrowing as the RBA and RBNZ cut interest rates more aggressively than other central banks.

New Zealand: RBNZ official cash rate

%

The RBA's surprisingly large 100bp cut to the cash rate target last week prompted us to adjust our Kiwi rate outlook. The unexpectedly assertive easing by the RBA greased the wheels for equally aggressive action by the RBNZ. We now forecast a 100bp cut in the OCR by the RBNZ on October 23 in place of the 50bp cut we had expected previously. By mid-2009, the OCR should have fallen to 5.0%, from 7.5% today.

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Economic Research note

Lower growth in Antipodean economies as exports suffer

- **Downgrades to global growth forecasts point to weaker growth in Australia and New Zealand**
- **The Shaky Isles already are in recession, but Australia's growth outlook is slightly firmer**
- **RBA and the RBNZ will continue to ease policy; monetary conditions still are too tight**

The recent downgrades to JPMorgan's GDP growth forecasts to include a global recession mean that growth in Australia and New Zealand also will be weaker. The Antipodean economies are small, open, exporting economies that cannot sail in calm waters as the global economy battles a worsening storm. Export volumes from both Australia and New Zealand inevitably will be softer than previously forecast. Similarly, high commodity prices, which previously were the bright spot in the Antipodean economies, probably cannot be sustained. Also, there will be negative passthrough effects from weaker external demand to softer growth in domestic demand, mainly via downward revisions to capital spending plans and slower job growth.

Lower GDP growth; more rate cuts

Consequently, we trimmed the GDP growth forecasts for Australia and New Zealand. We now expect a more severe slowdown in New Zealand's GDP in 2008 and growth of just 1.0% in 2009, down from 1.6% previously. Similarly, we now expect GDP growth of just 1.8% for Australia in 2009 (previously 2.6%). Growth in 2008 now probably will be 2.5%, down from 2.7% previously. Weaker GDP growth means a slightly better inflation profile, which should enable the RBA and RBNZ to ease policy more aggressively than previously forecast.

Reflecting Australia's weaker economic growth profile and the slightly more benign inflation outlook, accumulating downside risks, and the turmoil in global financial markets, the RBA last week stunned markets by delivering a surprise 100bp cut to the cash rate target. This was the biggest single official rate cut since 1992. We believe, though, that there will be another 50bp rate cut on November 4 and a further 100bp of easing by mid-2009. The risks to the cash rate forecast are to the downside. The unexpectedly assertive easing by the RBA greases the wheels for equally aggressive action by the RBNZ. We now forecast a 100bp cut in the OCR by the RBNZ on October 23 in place of the 50bp cut we had expected previously.

JPMorgan forecast changes
Annual % change

	Australia		New Zealand	
	2008	2009	2008	2009
GDP				
Previous	2.7	2.6	0.6	1.6
New	2.5	1.8	0.5	1.0
Inflation				
Previous	4.5	3.3	4.9	3.9
New	4.4	3.0	4.3	2.6
Cash rate (end period)				
Previous	6.5	6.0	6.75	6.0
New	5.25	4.5	6.0	4.75

Source: JPMorgan

Aussie and Kiwi GDP growth expected to slow sharply

Four changes to Australia's GDP forecast

We have made four main revisions to Australia's 2009 growth outlook. First, we have substantially downgraded expected growth for consumer spending. Previously, we had expected real household spending to grow 1.8% in 2009. Now, we expect spending to barely grow at all. The downgrade reflects consumer confidence's plunge (the index dived 11% this week), the impact of tighter credit (even for creditworthy borrowers), and more significantly, a weaker outlook for employment growth. The latter partly reflects downward revisions to firms' capital spending plans.

Second, we trimmed our expectation for firms' investment plans, reflecting the likelihood that funding such projects has become significantly more difficult and increased pessimism about the global economic outlook. The latter weighs heavily on mining investment, in particular. In the latest official capital spending intentions survey, firms expected to boost capex by 33% in the year ended June 2009. In the wake of recent troubling developments in financial markets and offshore economies, this expectation now looks wildly optimistic.

Third, weaker global economic growth means that growth in Australia's export volumes in 2009 probably will be just 2.8%

vs. 4.6% previously. This expected growth rate compares very unfavorably with export volume growth at the end of the last sustained boom in mining investment in the early 1980s.

Our fourth adjustment to the forecast profile is a positive offset. We have upgraded the forecast for growth in public spending in 2009, reflecting in part the Federal government's recent announcement of a likely acceleration in infrastructure spending. Similarly, key state governments are in a position to spend the windfall revenue collected on the back of soaring commodity prices to improve sagging public services and infrastructure. We now expect growth in real public spending in 2009 of 6.0%, nearly double our previous forecast.

It follows that lower GDP growth this year and next will improve Australia's inflation profile. Indeed, while announcing last week's aggressive cut to the cash rate, the RBA admitted that the increased downside risks to growth mean there is a greater chance of inflation returning to target earlier than the 2010 time frame suggested in the official forecasts. Inflation will remain elevated in the near term. However, by cutting the cash rate a total of 125bp in the last five weeks even as inflation accelerates, RBA officials appear to have pushed anxiety about inflation to the back burner as they focus on the intensifying financial instability and downside risks to growth.

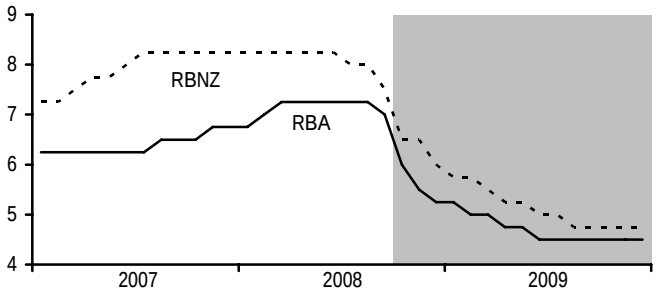
Prolonged recession expected in NZ

Similarly, the outlook for the New Zealand economy has deteriorated significantly. Two quarters of declining GDP in 1H08 mean the economy already has endured a technical recession. We now forecast another three quarters of falling GDP. The anticipated weakening in global demand now will be a larger drag on exports and investment than previously forecast. We have downgraded our forecasts for export growth to just 0.2% in 2008 and -0.2% in 2009, and expect fixed investment to grow just 0.7% this year and 0.3% next year. These forecast changes are occurring in an economy in which we already anticipate weak consumption, owing mainly to very tight financial conditions.

Firms facing high input costs have for some time been unable to pass on these higher costs to customers, owing to weakness in consumer purchasing power. Corporate profitability has dwindled amid soaring gasoline prices and tighter credit conditions, and will continue to do so. This means that firms will become increasingly reluctant to hire workers, leading to a

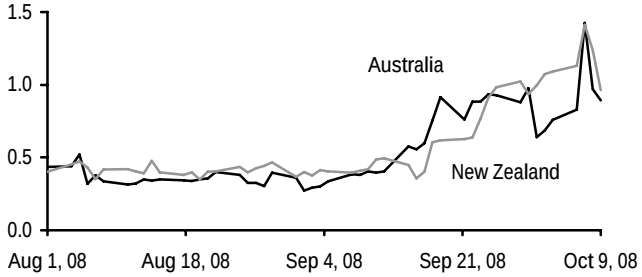
RBA and RBNZ to ease policy aggressively

Official cash rate, %



Wholesale market funding costs still elevated

3-mth loan rate and OIS rate spread



rise in the unemployment rate from 3.9% currently to 6.7% by the end of next year. Previously, we saw unemployment reaching 4.6% in 2009. Moreover, wage growth will slow as firms become less willing to pay more for workers amid softer labor markets.

The loosening labour market will add further to consumers' woes. The household sector remains under significant pressure from still-high interest rates, elevated food and energy prices, and the rapidly deteriorating housing market. We maintain our view that consumer spending—expected to be flat in 2008 and grow 0.7% in 2009—will show some improvement next year as the RBNZ lowers the OCR significantly. We acknowledge, though, that if credit conditions tighten further, households already neck-deep in debt will come under additional pressure, exacerbating the extent of the slowdown.

The onset of financial market instability and accumulating downside risks to global economic growth point to even more significant policy easing from the RBNZ. Our forecast calls for an OCR of 6.0% by year end and 4.75% by end-2009.

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Australia

- **RBA unexpectedly slashed cash rate 100bp to 6%**
- **Aussie employment growth slowed**
- **Demand for home loans remained weak**

We believed that the RBA was certain to cut the cash rate last week, but the 100bp move delivered on Tuesday was twice market expectations. RBA officials cited rising global financial market instability, the growing downside risks to the terms of trade, and the high debt-servicing burden on households and corporates as the main reasons for the surprisingly large move. Our forecast now calls for a cash rate of 5% by mid-2009.

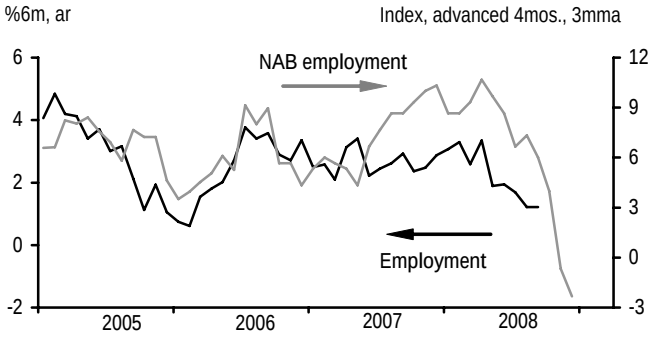
RBA slashed cash rate target 100bp

The RBA stunned markets last week by announcing a 100bp reduction in the cash rate target to 6%; this is the second official rate cut in as many months, but the first triple-digit cut since 1992. The main reason for the aggressive rate cut was to ensure that market interest rates—the only ones that matter for the real economy—fell substantially. The major Aussie banks responded shortly after the RBA announcement by cutting their variable mortgage rates (which account for over 80% of all outstanding loans) 75-80bp.

The RBA's commentary made clear that this assertive rate cut does *not* set a pattern for future decisions, and described the unexpected move as "unusual." In the wake of last week's move, our revised forecast calls for *at least* another 50bp of rate cuts by the end of this year, with the pace of the decline highly dependent on developments in financial markets and the evolution of the macroeconomic outlook.

Rather than refer to material downgrades to RBA officials' expectations for the real economy (the RBA's commentary indicated that the economy is tracking broadly as forecast), the RBA highlighted the sharp deterioration in global financial market conditions, particularly the dislocation in interbank markets, heightened instability in other markets, and weaker share markets as the main justification for the outsized cut. Obviously, this, and elevated bank funding costs, which make it uneconomic for the commercial banks to pass on the cut in full to the official cash rate, are the main sources of concern for RBA officials. Inflation, previously the RBA's prime source of anxiety, was taken off the back burner and hidden in a cupboard. RBA officials did highlight, though, the likelihood of an acceleration in inflation to "around 5%" in 3Q.

Australia: NAB survey and employment growth



Although officials believe that Australia's growth trajectory is little different from that envisioned in August, the statement made clear that the downside risks to economic growth have become much more acute. In particular, weaker activity in the global economy points to a decline in the terms of trade, with some major export prices already falling. Previously, RBA officials believed that the soaring terms of trade was a powerful source of support for the economy.

Another key source of downside risk is tighter credit conditions, even for "creditworthy borrowers." The abrupt change to the risk profile for growth implies, according to the RBA, that inflation now may be more likely to decline over the medium term, although it will stay above target for some time yet. Indeed, the plunge in AUD—down some US$0.20 in the past ten days alone—worsens an inflation outlook that, in our forecasts, has headline CPI approaching twice the midpoint of the RBA's 2-3%oya inflation target in 3Q. Inflation, though, no longer is the name of the game.

That said, weaker growth means inflation probably will return to target earlier than the mid-2010 timing forecast by the RBA in its August statement; this offers greater scope for the RBA to ease policy assertively, should this prove necessary in coming months.

Aussie job growth fell below 2%oya

Job growth moderated as expected in September. The economy added 2,200 jobs (JPMorgan and consensus 0K), compared to 10,000 in the previous month. The number of full-time jobs fell 15,400 and part-time jobs rose 17,700. More importantly, the rate of job growth slowed to 1.9%oya, falling below 2.0% for the first time since June 2006. This helped push the unemployment rate up to 4.3% from 4.1% in August, which was the lowest jobless rate since February.

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The unemployment rate will trend higher as economic growth moderates. Leading indicators of job growth have recently weakened—the ANZ job ads series, for example, recorded its largest fall in seven years in August. Jobs already are being shed in consumer-related industries, such as the retail sector, but with the global outlook deteriorating rapidly and credit market conditions remaining stressed, businesses in other sectors probably will soon scale back their hiring intentions and even report job cuts. Employment growth will moderate in industries focused externally, like mining, as global demand eases. In our forecasts, job growth will average between 0 and 5,000 per month over the next year, and the unemployment rate will rise swiftly toward 6% throughout 2009.

Home loans fall for seventh straight month

The number of home loans in Australia issued in August fell 2.2%m/m (JPMorgan -0.5%, consensus -1.0%), marking the seventh straight monthly decline. Demand for housing finance has pulled back considerably this year in the wake of the four interest rate hikes delivered by the RBA between August 2007 and March 2008; these rate hikes were topped up by disproportionate increases in domestic banks' standard variable loan rates.

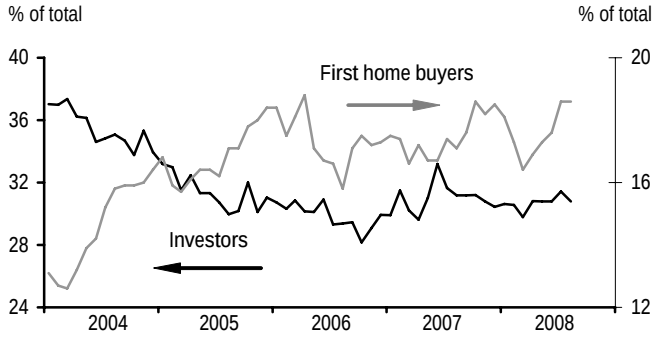
The number of first home buyers in the market remained steady in August, after jumping a full percentage point in the previous month. Since midyear, first home buyers have accounted for 18.6% of all loans, helped by the July 1 introduction of the Government's First Home Saver Accounts scheme. The scheme offers deposit saving support for first home buyers who are battling against record low levels of housing affordability. Investors, meanwhile, continued to account for around a third of the home loan market.

Amid growing speculation that the RBA would soon start cutting interest rates, the number of fixed rate loans as a percentage of all dwellings financed dropped to 4.6% in August from 8.8% in July, a stark contrast with the near 24% levels recorded earlier this year. Demand for fixed rate loans should fall further amid expectations the RBA will cut the cash rate significantly in coming months.

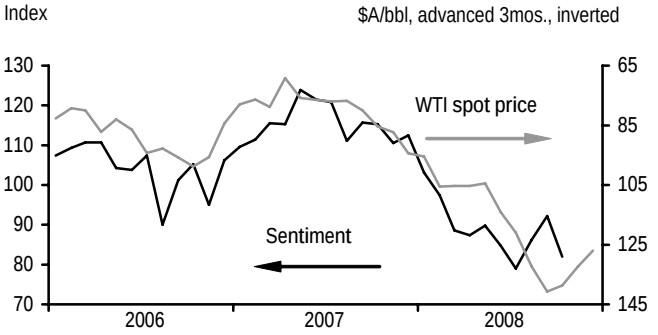
Consumer confidence slumped

Consumer confidence dropped 11%m/m in October (JPMorgan -5%), after surging 7% in September. While there was widespread speculation prior to the consumer sentiment survey's collection that the RBA would cut the cash rate as much as 50bp at its October meeting, at the same time there was an equal amount of speculation that domestic commercial banks would not pass on the cut in full to the official rate. Financial market volatility also was elevated, and the global economic outlook was deteriorating rapidly.

Australia: housing finance



Australia: consumer sentiment and crude oil price



The consumer sentiment index fell from 92.2 to 82.0, well below the level of 100 at which the number of optimists equals pessimists. Sentiment fell in all of the five major categories of the index, led by sentiment toward the economy one year ahead (-20.2%). According to the Westpac-Melbourne Institute, 32% of respondents said that petrol prices were having a major dampening effect on their spending. Over the month, petrol prices were largely steady—the 12% drop in oil prices in USD terms was offset by the sharp decline in AUD. The Aussie currency has shed 24% vis-à-vis USD since the start of August.

We expect that consumer sentiment in the final months of the year will be bolstered by the RBA's aggressive policy easing. Indeed, the next consumer sentiment survey will reflect the reaction to the RBA's 100bp rate cut last week.

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Data releases and forecasts

Week of October 13 - 17

Mon Oct 13 11:30am — **ANZ job advertisements**
Seasonally adjusted

	Jun	Jul	Aug	Sep
(%m/m)	-3.0	-0.3	-4.9	__

Tue Oct 14 11:30am — **NAB monthly business survey**
% balance, seasonally adjusted

	Jun	Jul	Aug	Sep
Business confidence	-9	-9	-7	__

Wed Oct 15 10:30am — **WMI leading index**
Seasonally adjusted

	May	Jun	Jul	Aug
(%m/m)	0.0	0.1	0.2	__

Review of past week's data

WMI consumer sentiment index

100=neutral, seasonally adjusted

	Aug		Sep		Oct	
(%m/m)	9.1		7.0		~~-5.0~~	*-11.0*

Housing finance approvals: owner occupiers

Number of loans, seasonally adjusted

	Jun		Jul		Aug	
(%m/m)	~~-3.7~~	*-3.2*	~~-0.2~~	*-0.9*	~~-0.5~~	*-2.2*
(%oya)	~~-24.7~~	*-24.6*	~~-21.4~~	*-21.8*	~~-25.2~~	*-25.0*

Labor force

Seasonally adjusted

	Jul		Aug		Sep	
Unemployment rate (%)	4.3		4.1		*4.3*	
Employed (000 m/m)	~~19~~	*17*	~~15~~	*10*	~~0~~	*2*
Participation rate (%)	65.3		~~65.2~~	*65.1*	~~65.2~~	*65.1*

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New Zealand

- **RBNZ expected to cut OCR 100bp this month**
- **Consumer spending will remain weak**
- **New liquidity measures announced**

The RBNZ surprisingly left the official cash rate (OCR) unchanged last week, even though other central banks across the globe were easing monetary policy. Following news of coordinated rate action among central banks, we thought the RBNZ might deliver an intermeeting rate cut, especially given that the economy (already in recession) is battling more headwinds than most.

Kiwi consumer spending rose in August

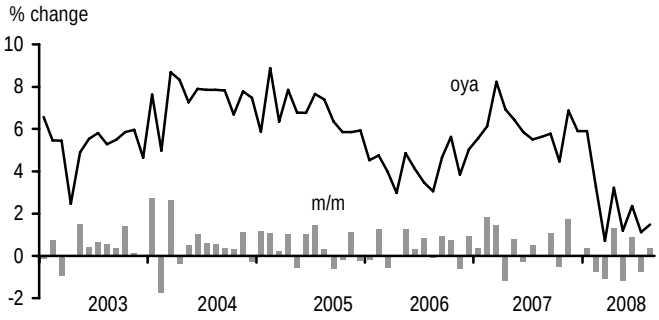
Data this morning, the value of New Zealand's retail sales grew a stronger than expected 0.4%m/m in August (JPMorgan -0.2%, consensus +0.3%), after falling a revised 0.7% in July (previously -0.8%). The strength in consumer spending followed the RBNZ's decision to cut the OCR 25bp in July from a record high 8.25%.

Sales rose in 15 of the 24 retail categories in August. The largest rises were recorded in sales of footwear (+4.6%), sales at bars and clubs (+3.8%), and sales at department stores (+2.5%). The largest falls were recorded in personal and goods hiring (-4.2%) and fuel retailing (-3.3%) as petrol prices at the retail level remained relatively high.

The household sector continues to face significant headwinds. Interest rates at 7.5% remain high (even after the RBNZ's 50bp cut in the OCR in September), petrol prices only recently started to fall, consumer confidence has stabilized but remains fragile, the labour market is softening, and house prices are still falling. That said, looking further down the track and into 2009, consumers should benefit from the personal income tax cuts delivered from October 1 and falling interest rates.

We believe that the RBNZ will cut the OCR aggressively, including a 100bp rate cut next week. Our forecast calls for an OCR of 6.0% by year end and 4.75% by mid-2009. The problematic global economic and financial market outlook, sagging domestic house prices, the falling terms of trade, and the improving prospect that inflation will return to the RBNZ's 1-3% target range over time provides ample scope for the RBNZ to ease policy assertively.

New Zealand: retail trade



RBNZ announced more liquidity measures

RBNZ Governor Alan Bollard announced this week that the New Zealand financial system currently "is working satisfactorily," adding that it has held up relatively well "in the face of the volatility and disruptions" occurring across the globe.

Over the past year, the Bank has announced a number of new measures to maintain liquidity in the financial market, and this week announced that it would temporarily broaden its security program. The RBNZ said in a statement that it would "if required, be prepared to lend on the basis of fully-secured Residential Mortgage-Backed Securities (RMBSs), prior to those securities achieving formal ratings."

Data releases and forecasts

Week of October 13 - 17

		Jun	Jul	Aug	Sep
Mon Oct 13	QVNZ house prices %, median				
	(%oya)	0.1	-2.2	-4.5	__
Mon Oct 13 10:45am	Retail trade Seasonally adjusted	May	Jun	Jul	Aug
	(%m/m)	-1.3	1.0	-0.8	*0.4*
	(%oya)	1.1	2.4	1.1	*1.5*
Thu Oct 16 12:00pm	Business PMI Seasonally adjusted	Jun	Jul	Aug	Sep
	Index	45.2	48.7	45.7	__
	(%oya)	-12.8	-10.7	-18.9	__

Review of past week's data

NZIER QSBO
% balance of respondents

	1Q08	2Q08	3Q08	
Headline index	-64.0	-64.0	__	*-19.0*

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Global Essay

- **Intensification of global financial crisis elicits powerful policy response**
- **The dilemma: severe damage is being done while policy is being decided and implemented and before its benefits arrive**
- **EM growth outlook is turning darker**
- **EM policymakers shifting to easing bias, led by aggressive action in China**

Time (the revelator)

The global financial crisis rose to a fever pitch last week. Despite a coordinated easing in global monetary policy, unsecured funding markets are experiencing intensified stress. US commercial paper outstanding contracted and interbank lending rates rose further across the board. The 3-month USD LIBOR/OIS spread widened out to a record 364bp. Emerging market corporate financing is now under significant pressure, with our index of EM corporate overseas borrowing rates (CEMBI) up more than 300bp in less than four weeks. Adding significant insult to the injury already being inflicted on credit markets, global equities fell about 20% this week and are now down over 40% for the year.

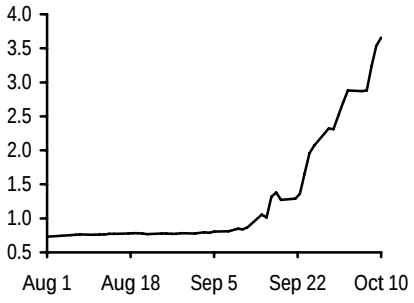
We continue to mark down growth forecasts as tighter credit conditions and greater wealth destruction will magnify drags on a global economy that already entered recession last quarter. The US economy is expected to contract at a 2% annualized pace over the next two quarters, a profile that should push global GDP growth into negative territory over this period. If realized, this would represent the first episode of two-quarter contraction in global GDP since 1982. Our modal forecasts, however, have limited value in an environment where the ultimate damage caused by financial market stress is difficult to gauge. Embedded in our view is an assumption that financial market stress will linger despite a material improvement in credit markets by year end.

Chaotic global financial markets call for a coherent global policy response and the actions taken over recent weeks suggest that this is now taking shape. In particular, there are three steps that are expected to take effect across a wide range of countries.

- **A zero real policy rate.** Last week's coordinated easing pushed US policy rates decisively into negative territory (adjusted for core inflation). However, the more important action on rates this week came from Europe, where to date there has been no regional ease. Over the coming months, policy rates in Europe should move sharply lower toward an ultimate resting point of about 2%. Combined with substantial ease in the EM and a further move by the Fed, this means that real global policy rates should fall below the lows of 2003-04 and could move into negative territory for the first time since the 1970s.
- **Big fat central bank balance sheets.** Through the first year of the financial crisis, central banks lent funds and government securities collateralized by illiquid bank assets but these actions were limited by a desire to control monetary base growth. Recent actions—including the Fed's decision to pay interest on excess reserves, the ECB's move to a fixed rate tender, and the Riksbank's issuance of interest bearing certificates—reflect a broad-based agreement that the scale of liquidity operations needs to be ramped up. The balance sheets of the Fed and the BoE are already close to doubling in size in recent weeks. The ECB balance sheet has expanded 20% over the past month and should expand considerably further in the coming weeks. Recent initiatives bursting balance sheets, including the Fed's CP program and dollar swap arrangements for foreign central banks, are geared to provide lender-of-last-resort facilities for stressed money markets not normally subject to central bank operations.

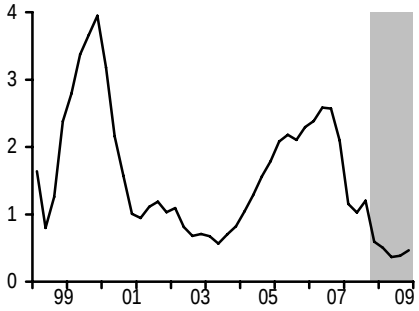
Three-month USD Libor/OIS spread

Percent per annum



Global real policy rate

Percent; deflated using %oya in core CPI



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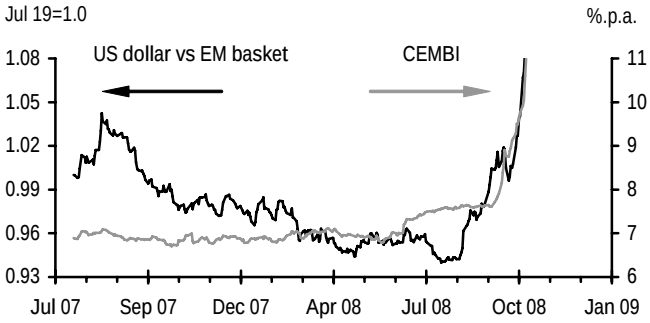
USD vs EM Fx basket and EM external corporate borrowing rate



- **Public sector funds to support banks.** Although central banks can inject enormous liquidity into the financial system, they cannot force banks to lend when the perception of counterparty risk is high. To address these concerns, the Bank of England unveiled initiatives last week that both guarantee bank liabilities and make public equity financing available to banks. Some form of these initiatives—which put taxpayers at risk—will likely emerge across a wide range of countries. The US TARP, which initially was focused on asset purchases, also appears to be shifting toward equity injections.

The immediate issue is not about the efficacy of these initiatives. Instead, it is whether these actions will be implemented quickly enough to prevent severe damage to financial markets and the global macroeconomy. Many of the recently announced policy initiatives will not be implemented for a number of weeks. And the easing now expected from central banks will likely be delivered only over months.

EM outlook dimming rapidly

The outlook for the emerging economies is dimming rapidly. The continued slide in the G3 economies is taking an increasing toll on EM exports and industrial production. In addition, the associated collapse in investor risk appetite has produced a sharp decline in the prices of EM financial assets and a drying up of dollar funding, which is feeding back negatively on domestic demand. In response, we have made a succession of forecast downgrades that put EM growth at 4% over the four quarters ending 2Q09—2% points below our estimate of trend.

In past crises, public sector debt dynamics were key to determining the relative vulnerability of EM countries. This time the focus has shifted to corporate sector debt servicing and refinancing needs, and the way that rapid asset price movements are compounding the problem. Banking system weakness also is an issue in some cases. During 2007 alone, a record $464bn of EM bank syndicated loans to corporates, $150 bn of Eurobonds, and $210bn of equity issued by EM companies came to market. Given the fears about the ability of EM corporates to roll over $309bn of syndicated loan and corporate bonds through 2009, the high-yield subsegment of the CEMBI dropped 18.2% in September. This was the worst-performing credit asset class globally, in what was one of the worst months for credit markets ever seen.

Weakness in the corporate market is particularly pronounced in Russia, Mexico, Brazil, Korea, China, Kazakhstan, and Dubai. The precise origins of the selloff in each market vary: in Brazil, it was concerns with respect to losses on fx derivatives; in Russia, a disorderly unwind of leveraged equity positions and rising capital flight; in China, the ongoing downturn in the domestic real estate markets; in Kazakhstan, continued concerns about the health of the banking sector; in Dubai, concerns over an overheated real estate market; and in Korea, mounting concerns about short-term fx funding needs. However, two common themes stand out: the extent of the dependence of each market and sector on continued access to credit (frequently external credit), and the potential damage emanating from recent sharp falls in EM currencies and commodity prices.

China leads EM Asian policy easing

Policymakers throughout the EM have shifted rapidly, from a pattern of widespread monetary tightening to going on hold or even easing. Ironically, this transition has been led by China, which remains the fastest-growing economy in the world, and whose markets have been relatively insulated from the global financial crisis. The PBoC kicked off the easing process in mid-September with a surprise rate cut. The central bank eased again last week, lowering its benchmark lending and deposit rates 27bp, cutting the reserve requirement ratio 50bp, and suspending the 5% tax on deposit interest income. Other EM Asian central banks quickly followed with various easing moves of their own, including Taiwan, Korea, Hong Kong, India, and Singapore.

China's actions demonstrate that its officials are determined to try to maintain "steady and relative fast growth" above 9%. Signs of slowdown are evident in the data: China's real activity indicators, including industrial production, electricity pro-

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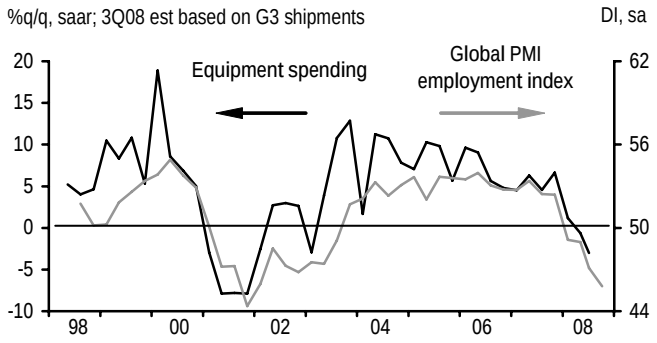
Global business equipment spending and employment



duction, manufacturing PMIs and real export volume have been easing in recent months. In addition, housing-related investment has started to decelerate with the consolidation in the property market.

We continue to expect a large fiscal stimulus from China in the form of tax cuts and spending on infrastructure, as well as monetary policy easing via cuts in interest rates and the reserve requirement ratio. Additional and more widespread easing also is on the way in the rest of EM Asia, where recent data are menacingly bad. Bellwether Taiwan's exports collapsed in September. And Singapore's GDP contracted for a second straight quarter in 3Q, highlighting the significant passthrough of slowing global demand on EM Asia.

Japan takes baby steps on policy support

The Bank of Japan did not participate in last Wednesday's global rate cuts. With hindsight, this outcome was signaled by Tuesday's policy meeting and press conference, which reaffirmed that officials still hope to ride out the recession with rates on hold at 0.5%, in a period when we foresee a continued decline in GDP through at least early 2009. That said, the BoJ has become more aggressive in its injections of liquidity into the yen money market and is considering paying interest on bank reserves, as the Fed is doing. The government is making progress on its fiscal plan. The supplementary budget, which includes the stimulus package proposed last month, passed the Lower house with the approval of the opposition DPJ. That implies that the package will pass in the near future in the Upper House as well. However, its size (spending at 0.3% of GDP) is too small to have much impact on the economy. Prime Minister Aso may push for an additional plan that would include an income tax cut. However, it is not clear how the DPJ would respond as it continues to push for an early election.

Business retrenchment intensified in 3Q

Japanese machinery orders continued to plunge in August. This is a warning that Japanese businesses have stepped up the pace of cost-cutting. The message extends beyond Japan's shores, however. Orders and shipments for capital goods are contracting across the G3. These data closely track movements in global business equipment spending. Indicators are pointing to a similar weakening in global labor markets. Job growth is slowing and the rate of unemployment is moving up.

In whole, the data clearly are signaling that global businesses curbed spending in the latest quarter, even in advance of the intensification of the financial crisis in September. This turn toward business retrenchment, which is reinforcing the slowdown in global consumer spending and housing, played a key role in pushing the global economy into recession last quarter. The pace of business retrenchment is likely to accelerate further in response to the intensification of the global financial crisis. The sharp downtrend in JPMorgan's global PMI employment index, and the continued climb in US initial jobless claims into October, certainly points in this direction.

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JPMorgan View - Global Markets

Stampede

- Investors moved into panic mode last week. Aggressive global policy easing and an avalanche of gigantic support measures did not stop the panic that is feeding on itself. Even rational investors could not afford to stand in front of a stampede. The selloff in US equities sets a **new historic record for weekly falls,** going back to 1927, including the crashes of October 1929 and of October 1987. October is a dangerous month, indeed.

- There was no clear trigger or rational explanation for the crash in equities last week. Economic activity data did not provide solace to us, but they were close to consensus forecasts. If we had known in advance of the coordinated central bank rate cuts and the flood of government support measures, then we would have turned positive on equities. Hence, one needs to point to **self-fulfilling panic and capitulation** to explain last week's move.

- **Liquidity** in markets, which is at the core of the crisis, **has not improved** this week and remains **at record lows**. Credit issuance remains a pittance, although the equity market is open to banks, at a price. Government bond trading has receded to a few benchmark issues. Counterparty risk has pushed trading activity almost completely from OTC to the exchanges. On the positive side, US investors are no longer exiting prime money market funds, which had earlier been forced to sell their CP holdings. **Central banks** are now throwing in their weight, and balance sheet, to fund the banks and, thus taking the place of the money market. The US government (Treasury, Fed, GSE) are now gearing up to replace the credit function of the banks, if they cannot revive credit creation.

- **What can and will reverse the crash** in risky markets? Much of what we hoped for in terms of rate cuts, capital injections, public guarantees, and liquidity injections to support the banking sector have happened already—fast and in size. Investors are policy-fatigued and need to see results, in implementation and impact, before buying again. This will take time—weeks for implementation, and several quarters on economic results. Hence, we must rely on time as the main support for markets.

- Portfolio management and **strategy** may seem pointless during a stampede and record low liquidity in markets, but we do not want to give up. Our long duration positions and steepeners in government bonds are working well and we stay with them. The same goes for our long in JPY. We similarly stay underweight credit. In equities, we have largely country and sector positions (such as long large banks). All these are recession trades and this week's events keep us in these positions.

10-yr Government bond yields

	Current	Dec 08	Mar 09	Jun 09	Sep 09
United States	3.83	3.40	3.45	3.45	3.55
Euro area	3.99	3.70	3.55	3.50	3.50
United Kingdom	4.47	3.70	3.40	3.50	3.60
Japan	1.54	1.60	1.60	1.80	2.00

Equities

	Current	YTD Return (local currency)
S&P	852	-37.0%
Topix	841	-37.5%
FTSE 100	3932	-30.9%
MSCI Eurozone	131	-39.6%
MSCI Europe	882	-35.9%

Credit markets

	Current	YTD Return
US high grade (bp over UST)	511	-9.5%
US high grade (bp over swaps)	357	
Euro HG Ind (bp over swaps)	194	-2.2%
USD high yield (bp vs. UST)	1265	-17.1%
EMBIG (bp vs. UST)	620	-12.6%

Foreign exchange

	Current	Dec 08	Mar 09	Jun 09	Sep 09
EUR/USD	1.38	1.42	1.40	1.38	1.36
USD/JPY	105.4	102	101	105	108
GBP/USD	1.77	1.78	1.75	1.75	1.74

Commodities

		Quarterly Average			
	Current	Dec 08	Mar 09	Jun 09	Sep 09
WTI ($/bbl)	79	101	94	96	102
Gold ($/oz)	843	825	875	865	850
Copper($/m ton)	5375	7500	7800	7500	6500
Corn ($/Bu)	4.08	6.30	6.50	6.80	6.60

Source: J.P. Morgan, Bloomberg, Datastream

Fixed income

- As an asset class, global government bonds are down on the week, as the long end sold off in fear of the likely avalanche coming to fund support programs for the financial sector. The short end of curves in major markets, in contrast, rallied strongly on coordinated rate cuts.

- **Overall liquidity is very poor,** creating massive dislocations. Long-only bond managers who do not require funding thus will find a treasure drove of opportunities. Others should stick with longs at the short end and with steepeners. The best, if not the only, liquidity is in exchange traded options and futures, as counterparty risk considerations have ravaged OTC liquidity.

- **Interbank unsecured markets** remain frozen, with very little

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activity beyond overnight between the banks and their wholesale clients. EONIA vols have come down significantly over the past week as many banks are using the ECB standing facilities to limit credit risks. Repo markets are more active but activity is concentrated to government only collateral.

Equities

- Equity markets crashed last week by more than 20%. Unprecedented daily volatility has pushed the VIX index to a record high of 75%, an indication of how extreme investors' pessimism and fear have become. Equity markets are now down more than 40% from last year's peaks. There were only two recessions over the past 60 years that saw larger peak-to-trough falls—1973 and 2001. The last resulted from a valuation bubble. The former was a deep global recession that saw a 46% peak-to-trough move in the S&P500, matching the current bear market. This suggests **a deep recession is priced in.**

- We have been reluctant to join the bear market, expecting that unprecedented policy action combined with extreme investor pessimism and positions should have favored a rebound. To our and many investors surprise, policy response failed to provide the trigger, in turn inducing even more capitulation.

- **We retain an overall defensive sector stance** taking comfort that our model portfolio of recommendations is performing well, even as our outright long on US banks suffered this week. We admit that the extremity of investors positions is not enough to trigger a rebound or even limit downside. The risk has risen that sentiment and positions will become even more extreme. We look for signs that policy actions are starting to have an impact on funding markets before switching to a positive view.

- We continue to **underweight sectors and regions more exposed to the severe downturn in the global manufacturing and commodity cycle**; i.e. Industrials, Materials and Energy. We overweight Financials in both developed markets and EM, focusing on the largest banks. Within countries, we stay overweight China vs Brazil on China's policy flexibility, and Mexico vs Russia and Taiwan vs Korea, as the latter offer economic reform and counter-cyclical fiscal policy.

Credit

- We remain **cautious in credit.** We underweight European HG credit, and favour senior bank debt over subordinated Tier 1. We continue to trade up the quality curve within HY bonds and underweight consumer ABS.

- **Issuance remains very light** in US HG credit and nonexistent outside US HG. Our trading desks continue to see selling of cash bonds, largely by hedge funds, but some small buying interest is emerging from real money investors, which find themselves increasingly underweight given their continued reluctance to buy.

- **Redemptions from loan funds** are accelerating causing lots of forced selling across the loan market. This triggers margin calls, leading to even more forced selling. If loans sell off, it makes HY bonds look rich, so it too needs to sell off. Loan funds were marketed as low-vol, safe investments. And history prior to last summer supported this description. The past 18 months blew this expectation out of the water and investors are starting to abandon the asset class.

Foreign exchange

- Global deleveraging accelerated last week, despite the first coordinated central bank cuts since September 11, taking down all high-yield currencies and pushing USD/JPY below 100 for the first time since March. Ten weeks into the sharpest carry unwind on record, losses on the high-yielders are a staggering 10-30% since August, a performance as pitiful as that of equity and commodity markets, which are normally two to three times more volatile than fx.

- Owning the **yen** remains our highest-conviction view. Global interest rates will continue to fall and yield spreads with Japan will narrow. On our latest forecast, the average spread between G-7 and yen rates will fall to its lowest level in the last 30 years. A global recession and the reduction in global interest rates to Japanese-style levels should continue to exert upward pressure on the yen. We recommend holding the bulk of the position vs USD and EUR, although we recognize the risk that policymakers deliver some sort of surprise next week. For this reason we book the not unsubstantial profits on the short AUD/JPY leg of our long yen basket.

Alternatives

- **Precious metals** rallied strongly on FTQ and should continue to gain. Gold is up more than 5%. All other sectors took a beating, with energy and industrial metals down over 10%. **WTI** is now around $80—close to our forecast for early next year. The deepening global recession creates clear downside risks on oil. **Base metals** similarly went down badly this week on the global recession. Demand for industrial metals has collapsed, and supply is supported by lower currencies in producing countries. We are bearish.

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Global Economic Outlook Summary

	Real GDP			Real GDP							Consumer prices			
	% over a year ago			% over previous period, saar							% over a year ago			
	2007	2008	2009	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	2Q08	4Q08	2Q09	4Q09
The Americas														
United States	2.0	1.5 ↑	-0.2 ↓	0.9	2.8	0.0 ↑	-2.0 ↓	-2.0 ↓	0.0 ↓	2.5	4.3	3.7 ↓	1.6 ↓	1.2 ↓
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	3.8 ↓	1.8 ↓	1.6 ↑	4.7 ↓	2.2 ↓	1.8 ↓	0.3 ↓	1.7 ↓	3.1 ↓	7.5	8.0	7.5	6.5
Argentina	8.7	6.5	1.0 ↓	2.4	8.7	4.5	2.0 ↓	0.5 ↓	-3.9 ↓	1.5 ↓	9.1	8.8	8.6	9.8
Brazil	5.4	5.1 ↓	2.8 ↓	3.4	6.5	3.4	3.1	2.0	3.7 ↓	3.4 ↑	5.6	6.2	6.3	5.1
Chile	5.1	4.0	2.5 ↓	6.8	7.4	0.0 ↓	2.0 ↑	2.5 ↓	2.5 ↓	2.5 ↓	8.9	9.0 ↑	7.6 ↑	4.7 ↑
Colombia	7.7	3.5 ↓	3.0 ↓	-0.8	2.6	4.0 ↓	2.8 ↓	1.8 ↓	2.5 ↓	4.0 ↓	6.4	7.1	5.5	5.0
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	1.4 ↓	0.3 ↓	-0.5	0.6	-0.5 ↓	-1.0 ↓	-1.2 ↓	1.0 ↓	3.0 ↓	4.9	5.3	4.5	3.7
Peru	8.9	9.2	5.3 ↓	7.5	10.1	6.9 ↑	4.9 ↓	2.8	5.5 ↓	6.0	5.5	6.1	4.5	3.5
Venezuela	8.4	5.0	2.5 ↓	-1.6 ↑	11.8 ↓	5.0	9.0 ↓	-5.0 ↓	0.5 ↓	3.5	31.0	33.9	33.6	31.2
Asia/Pacific														
Japan	2.0	0.4	-0.4	2.8	-3.0	-0.7	-1.0	-0.5	0.0	0.8	1.4	1.9	1.3	1.0
Australia	4.2	2.8 ↑	1.8 ↓	2.7	1.1	3.5 ↑	2.7 ↓	0.2 ↓	2.3 ↑	1.6 ↓	4.5	4.6	3.0 ↓	2.4 ↓
New Zealand	3.2	0.5 ↓	1.0 ↓	-1.2	-0.6	-1.8 ↓	-0.8 ↓	-0.5 ↓	3.0 ↓	4.7 ↑	4.0	4.9 ↓	3.2 ↓	0.8 ↓
Asia ex. Japan	8.8	7.1	6.5	8.6	6.6	5.2 ↓	5.4 ↓	5.6 ↑	6.9	8.0 ↓	7.0	5.5 ↓	3.5 ↓	3.8 ↓
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	7.3 ↓	9.8	5.9	6.9 ↓	5.7 ↓	5.5 ↑	6.5 ↓	7.9 ↓	7.8	8.9	6.3	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	4.3	3.5	3.3	3.4	1.5	3.0	3.3	4.0	5.0	4.8	5.0	3.3	3.0
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	2.0 ↓	1.0 ↓	15.7	-6.0	-6.3 ↓	-2.8 ↓	-1.2 ↑	7.0 ↑	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	5.0 ↑	6.0 ↑	7.5	4.9 ↓	1.1 ↓	3.3 ↓
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	12.4 ↓	8.3 ↑	6.8 ↑
Europe														
Euro area	2.6	1.0	0.0 ↑	2.7	-0.7 ↑	-1.0	-1.0	0.0	0.5	1.0	3.6	3.2	2.3	1.9
Germany	2.6	1.4	-0.1	5.2	-2.0	-0.8	-0.8	0.0	0.5	1.0	3.0	2.7	1.9	1.3
France	2.1	0.9	0.3	1.7	-1.3	-0.5	0.0	0.5	0.5	1.0	3.7	3.0	1.8	1.6
Italy	1.4	-0.2	-0.3	2.0	-1.1	-1.5	-1.0	0.0	0.0	0.5	3.8	3.6	2.6	2.0
Norway	6.3	2.6	0.3	-0.2	3.9	0.5	-0.5	-0.5	0.0	1.0	3.2	3.8	3.2	1.4
Sweden	2.9	1.0	0.2	0.5	-0.1	1.0	-0.5	-0.5	0.5	1.0	3.8	3.7	2.6	1.6
Switzerland	3.3	1.9	0.7	1.1	1.5	0.5	-0.5	0.5	1.0	1.5	2.7	2.2	1.1	1.1
United Kingdom	3.0	1.0	-0.6	1.1	0.0	-1.0	-1.5	-1.5	0.0	1.0	3.4	4.8	3.3	2.0
Emerging Europe	6.5	5.6 ↓	3.1 ↓	6.4	6.4	4.4 ↓	3.4 ↓	1.2 ↓	3.1 ↓	4.2 ↓	10.2	9.5 ↑	8.2 ↑	7.2
Bulgaria	6.2	5.9 ↑	3.5 ↓	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	6.6	4.3 ↓	1.5 ↓	3.8	3.6	4.5 ↑	3.0 ↓	0.0 ↓	0.0 ↓	0.5 ↓	6.8	5.2 ↓	1.4 ↓	1.8 ↓
Hungary	1.3	1.8 ↓	1.0 ↓	2.2	2.3	1.8 ↓	1.3 ↓	0.5 ↓	1.0 ↓	1.5 ↓	6.8	5.3 ↓	4.0 ↓	3.5 ↓
Poland	6.6	5.0 ↓	3.5 ↓	5.7	6.1	3.0 ↓	2.5 ↓	3.0 ↑	3.6	4.0	4.3	3.8 ↓	3.5 ↓	2.9 ↓
Slovak Republic	10.4	6.5	1.5 ↓	8.7	5.3	3.0	-5.0	3.5 ↓	3.3 ↓	3.0 ↓	4.5	4.1	3.2	3.4 ↓
Romania	6.0	8.5	2.5 ↓	...	...	...	...	...	...	...	8.6	6.6 ↑	7.5 ↑	6.5 ↑
Russia	8.1	7.4	4.0 ↓	7.2	7.3	5.5	4.7 ↓	0.5 ↓	4.0 ↓	6.0	14.8	14.2 ↑	12.8 ↑	11.2 ↑
Turkey	4.6	3.8	2.6 ↓	...	...	...	...	...	...	...	10.3	10.0	8.5	7.2
Global	3.4	2.1	0.9 ↓	2.7 ↑	1.7	0.6 ↑	-0.2 ↓	0.0 ↓	1.3 ↓	2.6	4.4	4.1 ↓	2.7 ↓	2.2 ↓
Developed markets	2.4	1.1	-0.1 ↓	1.7	0.6 ↑	-0.4 ↑	-1.3 ↓	-0.9 ↓	0.3 ↓	1.7	3.5	3.3 ↓	1.9 ↓	1.5 ↓
Emerging markets	7.5	6.0	4.6 ↓	6.4 ↑	6.0 ↓	4.2 ↓	4.1 ↓	3.5 ↓	4.9 ↓	6.1 ↓	7.8	7.0 ↓	5.4	5.2

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Global Central Bank Watch

	Official interest rate	Current	Change from Aug 07 (bp)	Last change	Next meeting	Forecast next change	Dec 08	Mar 09	Jun 09	Sep 09	Dec 09
Global	GDP-weighted average	3.45	-127				3.10	2.91	2.77	2.59	2.57
excluding US	GDP-weighted average	4.37	-10				4.09	3.82	3.61	3.35	3.31
Developed	GDP-weighted average	2.42	-172				1.97	1.78	1.65	1.48	1.48
Emerging	GDP-weighted average	7.61	55				7.64	7.51	7.29	7.09	6.98
Latin America	GDP-weighted average	10.41	160				10.80	10.78	10.67	10.18	9.96
CEEMEA	GDP-weighted average	8.13	87				8.12	8.07	7.64	7.28	7.07
EM Asia	GDP-weighted average	6.38	5				6.29	6.09	5.91	5.87	5.83
The Americas	GDP-weighted average	2.54	-305				2.14	2.14	2.13	2.07	2.05
United States	Federal funds rate	1.50	-375	**8 Oct 08 (-50bp)**	29 Oct 08	**29 Oct 08 (-25bp)**	1.00	1.00	1.00	1.00	1.00
Canada	Overnight funding rate	2.50	-200	**8 Oct 08 (-50bp)**	21 Oct 08	**21 Oct 08 (-25bp)**	2.00	2.00	2.00	2.00	2.00
Brazil	SELIC overnight rate	13.75	225	10 Sep 08 (+75bp)	30 Oct 08	30 Oct 08 (+50bp)	14.75	14.75	14.75	14.50	14.00
Mexico	Repo rate	8.25	100	15 Aug 08 (+25bp)	17 Oct 08	**Jun 09 (-25bp)**	8.25	8.25	8.00	7.25	7.25
Chile	Discount rate	8.25	275	4 Sep 08 (+50bp)	13 Nov 08	**3Q 09 (-25bp)**	8.25	8.25	8.25	7.75	7.50
Colombia	Repo rate	10.00	75	25 Jul 08 (+25bp)	24 Oct 08	1Q 09 (-25bp)	10.00	9.75	9.75	9.50	9.50
Peru	Reference rate	6.50	175	11 Sep 08 (+25bp)	13 Nov 08	**3Q09 (-25bp)**	6.50	6.50	6.50	6.25	6.00
Europe/Africa	GDP-weighted average	4.38	-22				3.89	3.45	3.14	2.71	2.68
Euro area	Refi rate	3.75	-25	**8 Oct 08 (-50bp)**	6 Nov 08	6 Nov 08 (-25bp)	3.25	2.75	2.50	2.00	2.00
United Kingdom	Repo rate	4.50	-125	**8 Oct 08 (-50bp)**	6 Nov 08	9 Oct 08 (-50bp)	3.75	3.25	2.75	2.50	2.50
Sweden	Repo rate	4.25	75	**8 Oct 08 (-50bp)**	23 Oct 08	**17 Dec 08 (-50bp)**	3.75	3.50	3.25	3.00	2.75
Norway	Deposit rate	5.75	100	25 Jun 08 (+25bp)	15 Oct 08	**15 Oct 08 (-50bp)**	4.75	4.50	4.25	4.00	3.75
Czech Republic	2-week repo rate	3.50	25	7 Aug 08 (-25bp)	6 Nov 08	**6 Nov 08 (-50bp)**	3.00	2.50	2.00	2.00	2.00
Hungary	2-week deposit rate	8.50	75	26 May 08 (+25bp)	20 Oct 08	Apr 09 (-25bp)	8.50	8.50	8.25	7.75	7.50
Poland	7-day intervention rate	6.00	125	25 Jun 08 (+25bp)	29 Oct 08	**Jan 09 (-25bp)**	6.00	5.75	5.25	4.75	4.75
Romania	Base rate	10.25	325	31 Jul 08 (+25bp)	30 Oct 08	**30 Oct 08 (+100bp)**	11.25	12.00	12.00	11.00	10.00
Russia	1-week deposit rate	4.25	100	11 Jul 08 (+25bp)	Sep 08	on hold	4.25	4.25	4.25	4.25	4.25
Slovak Republic	2-week repo rate	4.25	0	27 Apr 07 (-25bp)	28 Oct 08	**28 Oct 08 (-50bp)**	3.25	2.75	2.50	2.00	2.00
South Africa	Repo rate	12.00	200	12 Jun 08 (+50bp)	11 Dec 08	Apr 09 (-50bp)	12.00	12.00	11.00	10.50	10.00
Switzerland	3-month Swiss Libor	2.50	0	**8 Oct 08 (-50bp)**	11 Dec 08	11 Dec 08 (-25bp)	2.00	1.50	1.25	1.00	1.00
Turkey	Overnight borrowing rate	16.75	-75	17 Jul 08 (+50bp)	22 Oct 08	**Apr 09 (-50bp)**	16.75	16.75	15.75	15.00	14.50
Asia/Pacific	GDP-weighted average	3.53	-1				3.45	3.34	3.24	3.22	3.20
Australia	Cash rate	6.00	-50	**7 Oct 08 (-100bp)**	4 Nov 08	**4 Nov 08 (-25bp)**	5.50	5.25	5.00	5.00	5.00
New Zealand	Cash rate	7.50	-75	11 Sep 08 (-50bp)	23 Oct 08	**23 Oct 08 (-100bp)**	6.00	5.50	5.00	4.75	4.75
Japan	Overnight call rate	0.50	0	21 Feb 07 (+25bp)	31 Oct 08	on hold	0.50	0.50	0.50	0.50	0.50
Hong Kong	Discount window base	2.00	-475	**9 Oct 08 (-50bp)**	30 Oct 08	**30 Oct 08 (-25bp)**	1.50	1.50	1.50	1.50	1.50
China	1-year working capital	6.93	-9	**8 Oct 08 (-27bp)**	4Q 08	1Q 09 (-27bp)	6.93	6.66	6.39	6.39	6.39
Korea	Base rate	5.00	0	**9 Oct 08 (-25bp)**	6 Nov 08	**Nov 08 (-25bp)**	4.75	4.50	4.50	4.50	4.50
Indonesia	BI rate	9.50	125	**7 Oct 08 (+25bp)**	6 Nov 08	**1Q 09 (-25bp)**	9.50	9.25	9.00	9.00	9.00
India	Repo rate	9.00	125	29 Jul 08 (+50bp)	24 Oct 08	**2Q 09 (-25bp)**	9.00	9.00	8.75	8.50	8.25
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)	20 Nov 08	2Q 09 (-25bp)	6.00	6.00	5.75	5.75	5.75
Thailand	1-day repo rate	3.75	50	27 Aug 08 (+25bp)	3 Dec 08	3 Dec 08 (-25bp)	3.50	3.00	2.75	2.75	2.75
Taiwan	Official discount rate	3.25	13	**9 Oct 08 (-25bp)**	Dec 08	**Dec 08 (-25bp)**	3.00	2.875	2.875	2.875	2.875

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

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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	2.5	1.8	3.3	4.3	2.8	2.7	1.1	3.5	2.7	0.2	2.3	1.6	1.3
Private consumption	4.5	2.3	0.6	2.5	4.1	5.7	2.6	-0.6	0.0	0.8	0.4	0.8	1.2	1.2
Construction investment	9.8	2.1	0.1	3.1	10.0	-3.0	9.7	-4.6	-1.9	1.5	0.9	0.0	0.3	1.2
Equipment investment	9.6	14.7	5.7	24.1	-0.6	16.2	-1.3	53.4	13.0	4.2	-2.1	4.2	0.0	8.5
Public investment	5.7	15.1	9.9	72.3	-27.7	30.6	27.5	9.8	11.9	10.7	8.3	9.6	10.1	10.7
Government consumption	2.4	5.3	6.0	1.0	5.5	5.8	2.4	4.8	12.1	8.2	3.5	7.8	1.8	2.2
Exports of goods & services	3.2	5.1	2.8	0.8	8.8	-2.6	7.7	11.1	2.8	2.4	1.6	2.8	2.4	2.0
Imports of goods & services	10.8	11.4	5.0	7.1	11.1	13.4	18.2	9.3	5.1	4.1	7.0	4.1	3.2	2.0
Contributions to GDP growth:														
Domestic final sales	5.3	4.5	2.3	6.8	3.6	6.8	4.8	3.5	3.0	3.1	1.2	2.8	1.6	2.6
Inventories	0.6	-0.1	0.1	-1.9	1.5	-0.2	0.7	-2.2	1.3	0.2	0.4	0.0	0.4	-1.1
Net trade	-1.8	-1.7	-0.7	-1.4	-0.8	-3.5	-2.6	-0.1	-0.7	-0.5	-1.4	-0.5	-0.3	-0.1
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	3.0	2.1	1.9	3.0	4.2	4.5	4.7	4.6	3.9	3.0	2.7	2.4
Producer prices (%oya)	2.3	8.6	1.7	1.5	0.8	3.4	6.9	8.7	9.8	8.9	5.3	1.1	0.7	-0.3
Trade balance (A$ bil, sa)	-20.7	-12.7	-18.3	-4.6	-5.4	-6.9	-8.0	-0.5	-1.4	-2.8	-3.5	-4.1	-5.2	-5.4
Current account (A$ bil, sa)	-67.0	-60.4	-67.4	-16.4	-16.8	-19.0	-19.8	-12.8	-13.1	-14.6	-15.5	-16.3	-17.6	-17.9
as % of GDP	-6.2	-5.1	-5.5	-6.1	-6.1	-6.8	-7.0	-4.4	-4.4	-4.9	-5.1	-5.3	-5.7	-5.7
3m eurodeposit rate (%)*	6.0	7.0	5.5	5.8	7.1	7.2	7.6	7.8	6.7	6.0	5.8	5.5	5.5	5.4
10-year bond yield (%)*	5.6	5.8	4.9	5.6	5.7	6.4	6.1	6.2	5.8	5.0	4.8	4.9	4.9	5.2
US$/A$*	0.75	0.85	0.70	0.74	0.77	0.91	0.91	0.97	0.87	0.64	0.67	0.69	0.71	0.73
Commonwealth budget (FY, A$ bil)	17.2	16.8	8.0											
as % of GDP	1.6	1.4	0.6											
Unemployment rate	4.4	4.3	5.6	4.3	4.3	4.3	4.1	4.3	4.3	4.6	5.1	5.5	5.8	6.1
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)	3.2	0.5	1.0	3.8	2.5	3.6	-1.2	-0.6	-1.8	-0.8	-0.5	3.0	4.7	5.8
Private consumption	4.1	0.1	1.1	1.9	2.2	2.6	-1.7	-1.0	-0.7	-0.5	0.8	2.1	3.8	4.5
Fixed Investment	4.3	2.7	1.1	-0.5	0.8	13.8	-5.6	14.4	-6.0	-1.9	0.9	2.8	3.1	3.9
Residential construction	4.4	-12.1	-2.6	19.6	2.0	-8.9	-19.2	-28.8	-5.8	-2.0	0.0	0.8	2.8	3.2
Other fixed investment	4.3	6.5	1.9	-5.0	1	20.4	-2.1	26.8	-6.0	-1.9	1.1	3.2	3.2	4.0
Inventory change (NZ$ bil, saar)	0.8	0.7	-0.1	0.4	0.3	0.1	0.4	0.4	0.0	-0.1	0.0	0.0	-0.1	-0.1
Government spending	3.3	3.0	3.6	5.2	6.1	1.9	6.3	1.8	-4.3	4.2	5.0	5.1	6.7	4.3
Exports of goods & services	3.2	0.6	-0.8	-3.3	-1.5	19.0	-7.2	-0.9	-0.9	-1.6	-2.2	-0.5	1.5	2.9
Imports of goods & services	8.6	7.7	1.3	10.6	2.9	17.0	5.5	13.7	-1.2	-0.9	0.5	1.1	2.1	3.1
Contributions to GDP growth:														
Domestic final sales	4.8	3.3	2.2	4.5	5.0	6.3	0.0	5.0	2.8	-0.4	-0.4	3.3	6.2	6.3
Inventories	0.5	-0.1	-0.5	4.2	-0.9	-2.1	3.2	-0.2	-4.7	-0.2	0.8	0.4	-1.1	-0.1
Net trade	-2.0	-2.7	-0.7	-4.7	-1.5	-0.4	-4.4	-5.3	0.2	-0.1	-0.9	-0.6	-0.4	-0.3
GDP deflator (%oya)	4.2	3.7	2.5	4.3	3.8	5.6	5.8	3.7	3.5	1.9	1.7	2.8	2.7	2.7
Consumer prices	2.4	4.9	2.6	4.0	2.0	4.8	2.7	6.7	6.1	4.3	1.9	0.8	0.4	0.0
%oya	2.4	4.3	2.6	2.0	1.8	3.2	3.4	4.0	5.1	4.9	4.7	3.2	1.8	0.8
Trade balance (NZ$ bil, sa)	-2.4	-3.5	-2.8	-0.8	-0.7	0.0	-0.2	-1.1	-1.1	-1.1	-1.0	-0.8	-0.6	-0.4
Current account (NZ$ bil, sa)	-14.3	-16.6	-17.2	-3.7	-3.8	-3.2	-3.5	-4.6	-4.1	-4.3	-4.3	-4.4	-4.4	-4.1
as % of GDP	-8.3	-9.2	-9.2	-8.6	-8.8	-7.1	-7.8	-10.3	-9.2	-9.6	-9.4	-9.6	-9.3	-8.6
Yield on 90-day bank bill (%)*	8.4	8.0	5.5	8.2	8.7	8.8	8.8	8.6	8.0	6.6	6.1	5.5	5.3	5.2
10-year bond yield (%)*	6.3	6.1	5.1	6.4	6.4	6.4	6.4	6.4	6.4	5.3	5.2	5.1	5.0	5.2
US$/NZ$*	0.74	0.76	0.68	0.74	0.74	0.76	0.79	0.78	0.67	0.59	0.60	0.62	0.64	0.64
Commonwealth budget (NZ$ bil)	6.4	5.3	5.0											
as % of GDP	3.7	2.9	2.7											
Unemployment rate	3.6	4.0	5.6	3.6	3.5	3.4	3.7	3.9	4.2	4.4	4.8	5.2	5.8	6.7

*All financial variables are period averages

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Australia and New Zealand economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
13 Oct Australia: ANZ job ads (11:30am) Sep New Zealand: Retail sales (10:45am) Aug -0.2 %m/m, sa QV house prices Sep	14 Oct Australia: NAB business confidence (11:30am) Sep	15 Oct Australia: Westpac 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 spdg (03:00pm) Sep	22 Oct Australia: CPI (11:30am) 3Q New Zealand: Visitor arrivals (10:45am) Sep	23 Oct New Zealand: RBNZ official cash rate (09:00am) Oct	24 Oct I
27 Oct	28 Oct	29 Oct	30 Oct New Zealand: Trade balance (10:45am) Sep Building permits (10:45am) Sep NBNZ business conf. (03:00pm) Oct	31 Oct Australia: Pvt sector credit (11:30am) Sep
3 Nov Australia: ANZ comm. price (11:30am) Oct House price index (11:30am) 3Q Retail sales (11:30am) Sep New Zealand: Wage cost index (10:45am) 3Q	4 Nov Australia: RBA cash target (02:30pm) Nov New Zealand: ANZ commodity price (03:00pm) Oct	5 Nov Australia: Building approvals (11:30am) Sep Trade balance (11:30am) Sep	6 Nov Australia: Unemployment rate (11:30am) Oct New Zealand: Unemployment rate (10:45am) 3Q	7 Nov

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

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Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
13 Oct - 17 Oct	13 October	14 October	15 October	16 October	17 October
China • Money supply (Sep) • Trade balance (Sep)		Euro area • IP (Aug) • Trichet speech France • CPI (Sep) Germany • ZEW bus survey (Oct) Japan • Consumer sent (Sep) Poland • CPI (Sep) Russia • IP (Sep) United Kingdom • CPI (Sep)	Euro area • HICP final (Sep) Japan • IP final (Aug) Norway • Norges Bank meeting United Kingdom • Labor mkt report (Sep) United States • Beige book • Bus inventories (Aug) • NY Fed survey (Oct) • PPI (Sep) • Retail sales (Sep) • Bernanke speech	Japan • Reuters Tankan (Oct) United States • CPI (Sep) • IP (Sep) • NAHB survey (Oct) • Philly Fed survey (Oct)	Euro area • Trade balance (Aug) Japan • Dept store sales (Sep) • Tertiary sect activity (Aug) • Shirakawa speech Mexico • IP (Aug) • Banxico meeting Poland • IP (Sep) United States • Consumer sent (Oct) • Housing starts (Sep)
20 Oct - 24 Oct	20 October	21 October	22 October	23 October	24 October
Korea • GDP prelim (3Q)	Hungary • NBH meeting Japan • Shirakawa speech	Canada • BoC meeting China • CPI (Sep) • FAI (Sep) • GDP (3Q) • IP (Sep) • Retail sales (Sep) Japan • BoJ bank loan officers survey (3Q) New Zealand • CPI (3Q)	Australia • CPI (3Q) Japan • All sector act index (Aug) Turkey • CBRT meeting United Kingdom • MPC minutes	Belgium • BNB bus surv (Oct) Euro area • Industrial orders (Aug) France • INSEE bus surv (Oct) Japan • Trade balance (Sep) Mexico: CPI (Oct) Taiwan • Export orders (Sep) • IP (Sep) United Kingdom • BBA lending (Sep) • Retail sales (Sep) United States • OFHEO HPI (Aug) Central bank meetings • New Zealand • Sweden	Colombia • BanRep meeting Euro area • PMI flash (Oct) India • RBI meeting Italy • ISAE bus surv (Oct) Malaysia • BNM meeting United Kingdom • GDP prelim (3Q) United States • Existing home sales (Sep)

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