Australia and New Zealand - Weekly Prospects

Summary

- The economic data flow picked up in **Australia** last week and confirmed that domestic activity weakened further in late 2008. In November, the trend in retail sales moderated, the trade surplus narrowed significantly, and building approvals slumped. The highlight this week will be the December employment report. Leading indicators of employment, such as the ANZ job advertisements series and the employment component of the NAB survey, recently have collapsed, indicating that labour market conditions are finally starting to loosen. We expect another massive contraction in employment (-20,000) in December and another rise in the unemployment rate (to 4.5%).

- In **New Zealand,** ahead of a quiet week on the economic front, trade data last week showed a sharp narrowing of the trade deficit. The global downturn and falling commodity prices weighed on exports, and imports plunged, reflecting the significant slowdown in domestic demand. In our forecasts, net exports will remain a drag on economic growth in 2009; we call for GDP growth of just 0.2% this year.

- In the midst of a deep and synchronized **global economic downturn**, two elements in the recent data flow stand out. First, the US labour market is shedding jobs at an alarming rate. Private-sector employment fell at a 5.5% annual pace during the last three months of 2008, a pace last exceeded during an earlier credit crunch in the spring of 1980. The sharp slide in US employment contrasts markedly with labour-market performance elsewhere, where there is little evidence of significant cutbacks to date. Although the relative weakness of the US labour market is striking, the relative weakness in Asian industry also stands out. Asian industrial production is estimated to have declined at a 32% pace last quarter, roughly double the rate of decline in the Americas and Europe.

- **Global inflation** is plunging in response to the deep economic downturn and the associated collapse in commodity prices. Last week's reports registered sharp declines in December inflation across a range of countries in Europe and Asia. This week US CPI is expected to post a -0.3%oya reading—the first negative oya reading since 1955. Globally, inflation is expected to have eased to about 2%oya last month, down from a peak of 5.2% last July. We look for a decline toward zero by midyear.

- This week, it's the **ECB's** turn and we expect it to ease 50bp, bringing policy rates down to 2%. Activity data have continued to come in on the weak side in the Euro area, making it clear that the economy contracted more in the final quarter of last year than we were previously assuming. Instead of the 3.5% annualized drop in GDP that we were anticipating, we now think that the Euro area economy contracted 4% annualized, with a particularly sharp 5% decline in Germany. Meanwhile, inflation is now below the ECB's definition of price stability, with a decisive move down to 1.6% in December.

This week's highlight

The Aussie employment report on Thursday. We expect the unemployment rate to rise another notch to 4.5% and a massive 20,000 jobs to be shed in December.

Contents

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Data and event previews - Australia and New Zealand

Date [(a)]	Data/event	Forecast			Comment
		JPMorgan	Consensus	***Previous***	
Monday, 12 January (11.30am)	**Aust. ANZ job ads (%m/m, Dec.)**	**na**	na	*-8.6*	The ANZ job ads series recently have collapsed. Further deterioration in line with the broader decline in labour market conditions is expected.
Tuesday, 13 January (8.00am)	**NZIER business opinion survey (Index, 4Q)**	**na**	na	*-19.0*	na
Wednesday, 14 January (8:45am)	**NZ building permits (%m/m, Nov.)**	**na**	na	*-21.9*	na
Wednesday, 14 January (11.30am)	**Aust. home loans (%m/m, Nov.)**	**1.5**	1.0	*1.3*	After rising 1.3%m/m in October, marking the first rise since January, we expect that the number of home loans issued in November increased 1.5%, owing to falling mortgage rates. Mortgage rates fell in the final months of 2008 as the RBA embarked on the most aggressive pace of monetary policy easing since the early 1990s, delivering 300bp of cuts to the official cash rate between September and December.
Thursday, 15 January (11.30am)	**Aust. employment change (000s, Nov.)**	**-20.0**	-20.0	*-15.6*	The economy probably shed 20,000 jobs in December. We expect the jobless rate to tick up to 4.5% in December after recently drifting up from the 33-year low of 3.9% reached back in February. We expect employment to fall 1% during the recession, and for Australia's jobless rate to soar to 9% by the end of 2010.

(a) Australian Eastern Standard Time.

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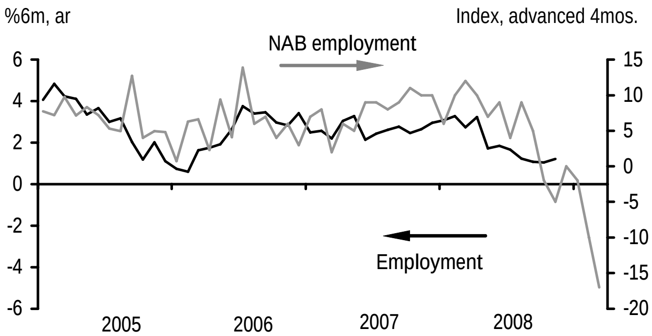
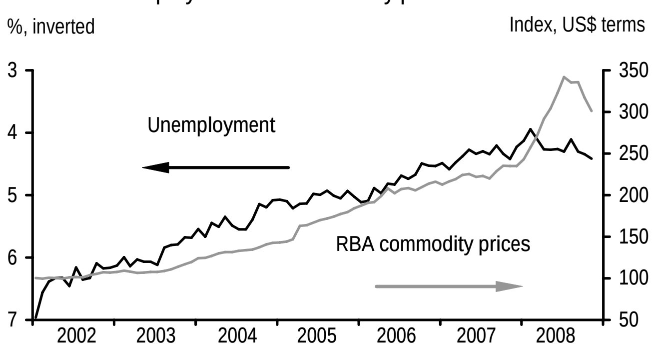
Feature charts

Australia: NAB survey and employment growth



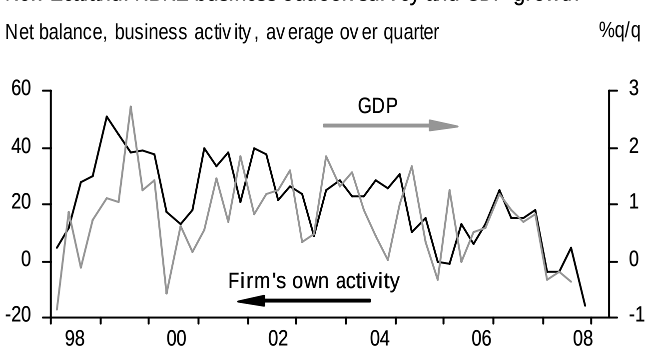
Leading indicators of employment in Australia, such as the employment component of the NAB Business Survey, recently have collapsed. The employment report this Thursday should show that another 20,000 jobs were shed in December. We expect that labour market conditions will continue to deteriorate rapidly, helping to push the unemployment rate to nearly 9% by the end of next year, from just 4.4% currently.

Australia: unemployment and commodity prices



Our call for a 9% jobless rate within two years is supported by the avalanche of job losses announced recently, including many in the mining sector, which led the charge during the long employment boom. The continued collapse of commodity prices resulting, in part, from the downturn in the global economy will damage corporate profits in the mining sector; thus, mining companies probably will report even further, significant job losses in coming months.

New Zealand: NBNZ business outlook survey and GDP growth



With little on the economic front in NZ recently, our forecast remains that the economy will grow just 0.2% in 2009. Household spending, in particular, will be a large drag on growth. The rise in unemployment probably is the biggest headwind facing consumers. Business confidence has tumbled owing to falling corporate profitability (thanks to tighter credit conditions) and, as a result, firms have become more reluctant to hire workers. We expect that the unemployment rate will rise from the current five-year high of 4.2% to 6.7% by year end.

Economic Research note

New Zealand will struggle to emerge from recession in 2009

- **New Zealand's recession will extend over five quarters, but it will be shallow**
- **Private consumption and exports will remain particularly weak in 2009**
- **GDP growth should rebound to 2.4% in 2010**

The New Zealand economy already was in a homegrown recession before the recent international troubles unfolded. So the outlook for 2009 is even worse. Weaker export demand (owing to the worsening outlook for New Zealand's key trading partners), lower commodity prices, negative wealth effects from falling asset prices, and weaker consumer and business sentiment mean that the economy will be running on empty for some time.

The Kiwi economy already has strung together three straight quarters of falling GDP, and will probably contract in 4Q08 and will in 1Q09 too. Our forecast calls for GDP growth of just 0.2% in 2009, compared to a sluggish 0.4% in 2008. Such subdued rates of growth point to a deterioration in the government's fiscal position as tax revenues inevitably dry up.

Private consumption will remain subdued

Private consumption, accounting for nearly two thirds of the economy, should grow just 0.1% in 2009, the same rate as in the previous year. Consumers have become increasingly reluctant to spend as confidence has deteriorated sharply amid widespread recession fears, increased financial market volatility, and falling asset prices. Excessive leverage in the household sector in an environment of declining house prices—which fell 4%oya in November, marking the eighth straight monthly decline, and should fall another 10% in 2009—has been a major drag on consumption. These negative factors have outweighed the positive influences of lower petrol prices, falling interest rates, and tax cuts delivered from October 1. Another round of tax cuts is due in April 2009.

There is downside risk to our private consumption forecast given that dairy cooperative Fonterra—which accounts for 35% of global dairy output and has a major impact on income in New Zealand—recently announced that falling commodity prices and fluctuations in the local currency have put downside pressure on its payout forecast for the period ending May 31, 2009. The payout decision will be announced January 27.

New Zealand: GDP growth forecasts

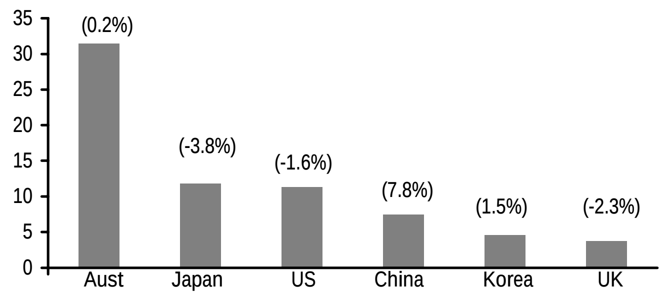
	2008	2009	2010
Household spending	0.0	0.1	1.8
Government spending	4.1	7.4	-0.5
Fixed investment	-3.8	-5.2	6.5
Change in inventories[1]	2.2	-0.5	-0.4
Exports	-1.0	-3.1	3.2
Imports	3.4	-4.2	1.9
GDP	0.4	0.2	2.4

Source: JPMorgan

1. Contribution to growth

Weak trading partner growth will weigh on exports

% of exports, 2009 GDP growth forecasts in brackets



Already, in November, the company cut the payout forecast to NZ$6/kg of milk solids from NZ$6.60. We estimate that the November payout reduction will remove around NZ$1bn from the economy.

Job insecurity a big issue in 2009

Probably the biggest cloud hanging over household spending in 2009, though, is the likely rise in unemployment and consumers' increased anxiety about job security. Corporate profitability has dwindled amid tighter credit conditions, making firms more reluctant to hire workers. Business confidence slumped to a record low in December, according to the NBNZ business survey, and firms' own expectations collapsed—a net 22% of managers expected conditions in their own business to deteriorate in the year ahead.

The jobless rate already is at a five-year high of 4.2% and will trend higher in 2009. In our forecast, the unemployment rate will rise to 6.7% by year end. In December, NZ Treasury forecast that 68,000 workers would lose their jobs in the next 15 months, but this number could rise to as high as 87,000 if economic conditions worsen. The rise in unemployment and the expected moderation in wage growth will hurt local retailers.

Exports and investment to remain weak

Given our forecasts of global recession, exporters will face significantly weaker external demand. Even though the end of the drought should boost agricultural activity, exports probably will fall 3% in 2009, owing to much weaker growth in the country's key trading partners. Annual GDP growth in Australia of just 0.2% in 2009 will be a major headwind.

Business investment also will remain weak. Investment volumes recently have sunk, signalling that the downturn has widened from households to businesses. Reflecting the significant downturn in the housing market, residential investment slumped in 2008, and ongoing financial market uncertainty simultaneously deterred business investment. The drag on growth from these components will gradually ease in the latter half of 2009 as interest rates fall and financial market volatility declines.

Falling OCR should soften the blow

Households' disposable incomes have been strangled by tighter and more expensive credit conditions resulting from the global credit crunch, but should benefit from rapidly falling interest rates. The prolonged recession, coupled with the rising prospect that inflation will fall to within the RBNZ's target range in coming quarters, point to further assertive policy easing in coming months. The RBNZ cut the OCR from 8.25% in early 2008 to 5% in December.

Headline inflation surged 5.1%oya in 3Q to more than double the midpoint of the RBNZ's 1-3% target range, but should fall below target in 2009. The RBNZ expects annual CPI inflation to trough around 1.5% in 3Q09, compared to our forecast of a trough of 0.8% in 4Q09.

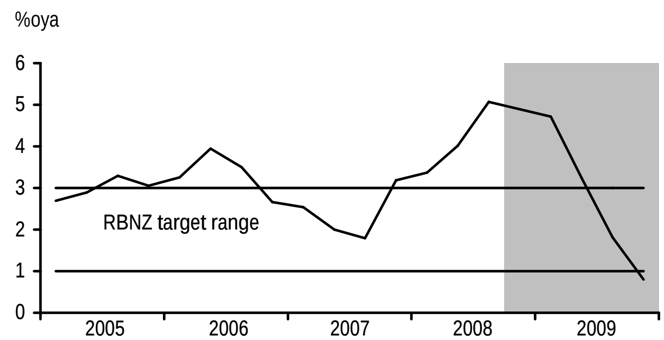
Official anxiety about elevated inflation in the near term, however, means that inflation is not yet on the backburner. RBNZ Governor Alan Bollard in December signalled that inflation remains a key policy consideration, even though the economy is in recession. He noted that inflationary pressures need to be reduced significantly to provide scope for further policy easing and suggested that various sectors of the economy should respond to reduced demand by lowering prices. We maintain our forecast for a terminal policy interest rate of 3.25% in the third quarter of 2009.

New government focused on economy

The forthcoming fiscal stimulus is one key factor preventing even larger official interest rate cuts. The government plans to inject about NZ$7bn, or 4% of GDP, into the economy over the

Official cash rate to fall quickly

Inflation back below target by end 2009



next two years. The newly elected National Party-led government, which took the helm in November, has announced "the economy" as its number one priority. It plans to increase the Budget deficit significantly to more than 3% of GDP by the year ended June 2011, as it funds significant personal income tax relief and accelerates public infrastructure spending. Increased welfare payments (owing to rising unemployment) also will help push the Budget into significant deficit.

The government estimates that public debt will jump to 33% of GDP by 2012-13 (from 17% currently), a level beyond what it considers prudent; this will necessitate a significant boost in bond issuance.

Economic outlook for 2010 a little brighter

Firmer global growth and significant policy easing should help the economy rebound from this prolonged recession. Monetary policy now is accommodative and the planned fiscal easing generally is more expansionary than that elsewhere. The rebound also will be fuelled by stronger private consumption, buoyed by lower interest rates and personal income tax cuts, and positive export growth on the back of firmer global demand.

Australia

- **Building approvals slumped in November**
- **Employment forecast to contract again**
- **Home loan demand likely supported by rate cuts**

The economic data flow picked up in Australia last week and confirmed that domestic activity weakened further in late 2008. In November, the trend in retail sales moderated, the trade surplus narrowed significantly, and building approvals slumped. The highlight this week will be the December employment report, which should indicate another massive contraction in employment and another rise in the unemployment rate.

Aussie employment likely contracted

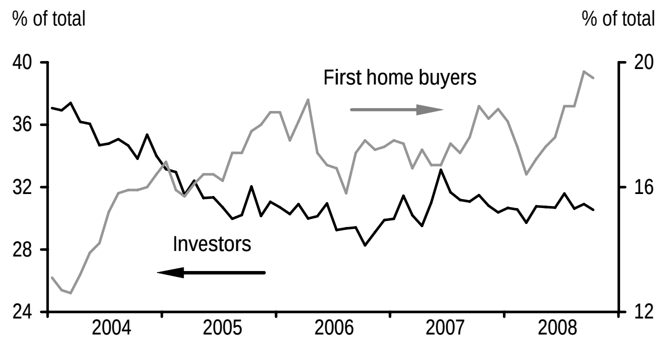
Leading indicators of employment in Australia, such as the ANZ job advertisement series and the employment component of the NAB Business Survey, recently have collapsed, signalling that labour market conditions have started to deteriorate. The employment report this Thursday should show that the economy shed another 20,000 jobs in December, following a 15,600 fall in the previous month.

Given last year's government budget cuts for the Bureau of Statistics, which triggered a dramatic reduction in the sample size for the Labour Force Survey, we believe that the jobless rate probably provides the best reading on underlying labour market trends, rather than the full-time/part-time employment breakdown. We expect the jobless rate to tick up to 4.5% in December from 4.4% in the previous month, after recently drifting up from the 33-year low of 3.9% reached back in February.

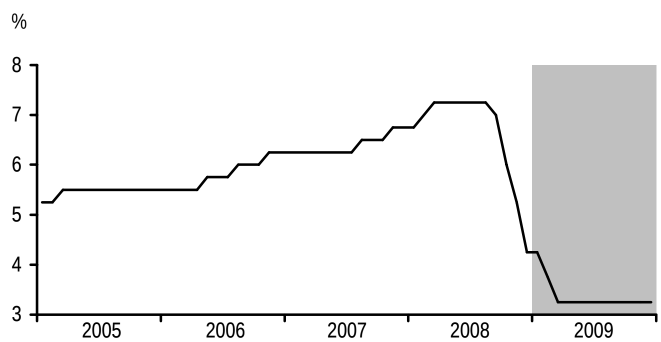
We expect employment to *fall* 1% during the recession, which we estimate started during 4Q08 (we believe that real GDP will fall in 1Q09 too), and for Australia's jobless rate to soar to 9% by the end of 2010—double the current rate. This will be a more benign outcome than during Australia's last two recessions in the early 1980s and early 1990s. Back then, the jobless rate reached double figures and stayed there for extended periods.

Our call for a 9% jobless rate within two years is supported by the avalanche of job losses announced recently, including many in the mining sector, which led the charge during the long employment boom. Our assumed 1% fall in employment during this recession compares with 3% declines in each of the last two recessions.

Australia: housing finance



Australia: RBA cash target rate



We suspect, though, that labour force participation will be slower to decline this time around, which will inflate the unemployment rate. This is because of highly skilled migration flows, older workers staying in the work force longer to compensate for the fact that their retirement nest-egg has dwindled (thanks mainly to falling equity prices), and second income earners from many households seeking work to make fraying financial ends meet.

Home loans probably buoyed by rate cuts

After rising 1.3%m/m in October, marking the first rise since January, we expect that the number of home loans issued in November increased 1.5%, owing to a significant fall in variable mortgage rates. Mortgage rates fell in the final months of 2008 as the RBA embarked on the most aggressive pace of monetary policy easing since the early 1990s, delivering 300bp of cuts to the official cash rate between September and December.

That said, an even larger rise in home loans in November will be prevented by the fall in confidence resulting from deteriorating economic conditions, which drove potential home buyers to boost precautionary savings. The massive wealth de-

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struction occurring in the highly leveraged Aussie household sector also has encouraged many of those who have loans to pay down debt, which will weigh on new demand for housing credit.

Demand for fixed interest rate loans probably remained weak in November in the wake of the RBA's rate cut and as expectations of further policy easing continued to increase. Fixed rate loans accounted for just 3% of all loans issued in October, compared to 22% at the start of 2008.

Demand for home loans from first home buyers should have risen, helped by the July 1 introduction of the "First Home Saver Accounts" scheme and the doubling of the first home buyers grant in October to A$14,000. First home buyers accounted for 19.5% of all loans in October, a number that we expect increased in November. The prospect of further interest rate cuts, coupled with falling house prices, will also have been attractive to potential first home buyers.

We maintain our forecast that the RBA will cut the cash rate 50bp to 3.75% in early February, with a terminal cash rate of 3.5% in March. RBA officials seem to be aiming for a policy stance that leans to the easy side of neutral as quickly as possible.

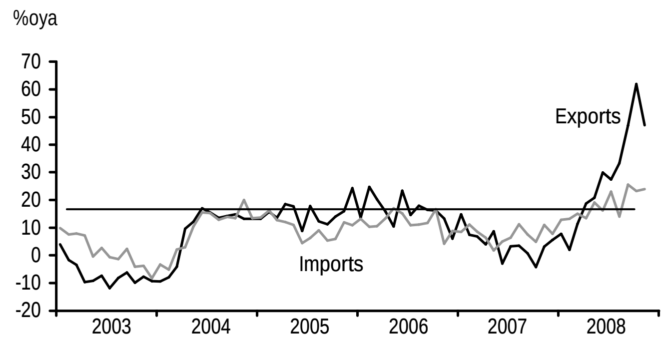
Aussie retail sales rose in November

The value of Australia's retail sales increased unexpectedly in November, rising 0.4%m/m (JPMorgan -0.3%m/m, consensus -0.4%m/m), after spiking 1.0% in October. We suspect that sales volumes were boosted in November by the aggressive discounting seen among retailers, coupled with lower interest rates and falling petrol prices.

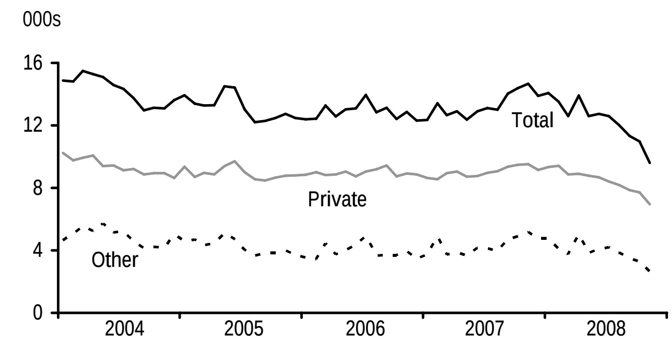
It is difficult to read too much into the seasonally adjusted retail sales data in November, however. The ABS reinstated the full survey sample size (back to 2,700 from only 900 in October) in November and, as a result, the change in the seasonally adjusted data is of limited use in the November month. The trend series was in line with expectations, however, rising 0.1%m/m, after October's 0.2% increase.

The major driver of the rise in retail sales in November was the food component, which accounts for a quarter of total retail sales. Reflecting still-elevated food prices, the value of food sales was up 1.8%m/m, but ex-food sales were down 0.5%. The largest drag on retail sales in November was "other" re-

Australia: export and import growth



Australia: building approvals



tailing—including newspaper and stationary sales, recreational goods retailing, and sales of pharmaceuticals, among other items—which slumped 6.5%m/m, after a strong bounce in the previous month.

Households are facing considerable headwinds. The labour market has started to loosen, credit availability has fallen, and precautionary saving has risen amid difficult financial conditions. Of these factors, the largest drag on consumption in the foreseeable future probably will be the deterioration in labour market conditions. As mentioned previously, we expect the unemployment rate to nearly double by the end of 2010.

In the very near term, though, December sales should remain strong, owing mainly to the one-off bonus payments delivered by the government to low- and middle-income earners on December 8, combined with the significant policy easing from the RBA.

Trade surplus narrowed on fewer exports

Australia's trade balance narrowed more than expected in November, falling to A$1.45bn (JPMorgan A$2.0bn, consensus A$2.1bn), after blowing out to A$2.96bn in October. The Oc-

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tober surplus was the highest on record.

The fall in the surplus was mainly owing to a 4%m/m slump in exports. Nonfarm shipments fell nearly 5%m/m in November, thanks to a 13% decline in the metal ores and minerals component. This was a surprise given that in recent months still-elevated prices for coal and iron ore have buoyed the value of exports. Farm exports also fell, slipping 1% over the month. On the other side of the trade ledger, imports rose 2%m/m in November, falling much in line with expectations following the release of preliminary estimates from the Bureau of Statistics.

The downturn in global demand will weigh on export volumes, although exporters should, to some extent, benefit from falling AUD, which shed 20% vis-à-vis the US dollar in 2008. Export volumes are expected to weaken significantly in coming quarters, given that we believe the global economy already is in recession. Net exports probably will remain a drag on economic growth in 2009.

Building approvals slumped in November

Building approvals in Australia slumped 12.8% in November (JPMorgan -2.0%, consensus 1.5%), more than four times the 3.1% decline recorded in October. The November fall marked the fifth straight monthly decline and the largest fall in the series since late 2002.

The downtrend in the number of building approvals will likely continue amid low confidence, elevated construction and material costs, excessive red tape in the building sector, and persistent funding pressures that continue to deter new developments. So, while the series remains highly volatile, the near-term outlook for the building sector remains bleak. On the upside, past and future cuts to the official interest rate should provide an offset.

Data releases and forecasts

Week of January 5 - 9

Mon Jan 12 11:30am — ANZ job advertisements
Seasonally adjusted

	Sep	Oct	Nov	Dec
(%m/m)	-1.4	-5.9	-8.6	—

Wed Jan 14 11:30am — Housing finance approvals: owner occupiers
Number of loans, seasonally adjusted

	Aug	Sep	Oct	Nov
(%m/m)	-1.8	-2.4	1.3	1.5
(%oya)	-25.4	-26.5	-24.2	-25.0

Thu Jan 15 11:30am — Labor force
Seasonally adjusted

	Sep	Oct	Nov	Dec
Unemployment rate (%)	4.3	4.3	4.4	4.5
Employed (000 m/m)	-6	37	-16	-20

Review of past three weeks' data

Retail trade
Seasonally adjusted

	Sep		Oct		Nov	
(%m/m)	~~-1.0~~	*-1.6*	~~0.7~~	*1.0*	~~-0.3~~	*0.4*
(%oya)	~~1.7~~	*1.4*	2.2		~~1.3~~	*2.0*

Building approvals
Seasonally adjusted

	Sep		Oct		Nov	
(%m/m)	~~-5.9~~	*-5.8*	~~-5.4~~	*-3.1*	~~-2.0~~	*-12.8*
(%oya)	~~-19.4~~	*-19.2*	~~-26.1~~	*-23.6*	~~-28.1~~	*-34.7*

Trade balance
Seasonally adjusted

	Sep		Oct		Nov	
Trade balance (A$ mn)	~~1255~~	*1111*	~~2952~~	*2960*	~~2000~~	*1448*

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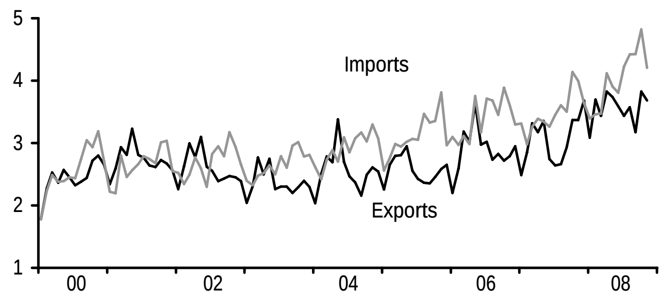
New Zealand

- **Trade deficit narrowed as exports slowed**
- **Net exports to remain drag on economic growth**
- **RBNZ to continue cutting OCR**

In New Zealand, ahead of a quiet week on the economic front, trade data last week showed a sharp narrowing of the trade deficit. The global downturn and falling commodity prices weighed on exports, and imports plunged, reflecting the significant slowdown in domestic demand. In our forecasts, net exports will remain a drag on economic growth in 2009; we call for GDP growth of just 0.2% this year.

New Zealand: exports and imports

NZ$ billion, nsa



NZ trade gap narrowed in November

New Zealand's trade deficit narrowed to NZ$520mn in November (JPMorgan -NZ$750mn, consensus -NZ$775mn), from a deficit of NZ$996mn in October. The annual trade gap fell to -NZ$5.16bn, from -NZ$5.27bn, which had been the widest gap recorded this year.

Significantly softer global demand and falling commodity prices weighed on exports, which grew 9.4%oya in November, compared to 13.6% in the previous month. That said, still-elevated dairy prices buoyed outbound shipments, with the largest contribution to the rise in exports coming from milk powder/butter/cheese, which rose 10.3%oya. Interestingly, exports to Australia, New Zealand's largest export destination, exceeded NZ$10bn for the first time.

On the other side of the trade ledger, reflecting the significant slowdown in domestic demand and falling oil prices, demand for imports moderated sharply, growing just 5.2%oya in November, after a stellar 16.4% rise in the previous month. The intermediate goods category recorded the largest increase, rising 31.4%oya, while the largest decrease was recorded in imports of vehicles, parts, and accessories, which were down 39%.

Net exports to subtract from GDP growth

Net exports will remain a drag on economic growth in 2009. Weak global demand and falling commodity prices will mean that export growth will moderate, even though the end of the drought should fuel further agricultural activity and NZD depreciation will boost exporters' competitiveness. NZD fell 5.5% in trade-weighted terms in November, the ninth straight monthly decline.

Demand for imports will remain subdued as domestic demand flags amid deteriorating housing and labour market conditions, although aggressive monetary policy easing should cushion the blow. Our forecast calls for the RBNZ to cut the OCR 50bp at the end of January, with a terminal cash rate of 3.25% by July.

Data releases and forecasts

Week of January 5 - 9

Tue Jan 13 10:00am	NZIER QSBO % balance of respondents	1Q08	2Q08	3Q08	4Q08
	Headline index	-64.0	-64.0	-19.0	__
Wed Jan 14 10:45am	Building consents Not seasonally adjusted	Aug	Sep	Oct	Nov
	(%m/m)	-7.5	23.1	-28.3	__
	(%oya)	-47.0	-17.8	-43.8	__
Fri Jan 16	QVNZ house prices %, median	Sep	Oct	Nov	Dec
	(%oya)	-5.8	-6.8	-6.8	__

Review of past three weeks' data

Trade balance

Not seasonally adjusted

	Sep		Oct		Nov	
Trade balance (NZ$ mn)	~~-1260~~	*-1253*	~~-942~~	*-996*	~~-750~~	*-520*

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Global Essay

- **Business sector adjustments are intensifying across the globe**
- **Continued downward revisions push EM GDP growth into negative territory**
- **US consumption is stabilizing despite collapse in employment**
- **This week: US CPI to post first oya negative reading since 1955**
- **ECB to ease 50bp on its way to a 1% policy rate**

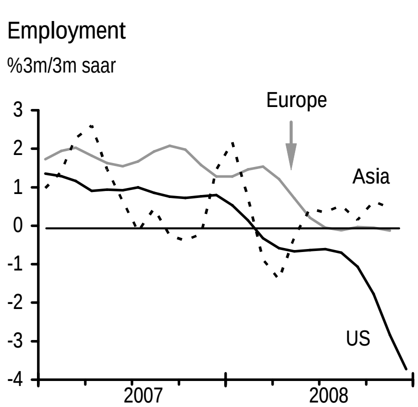
This wheel's on fire

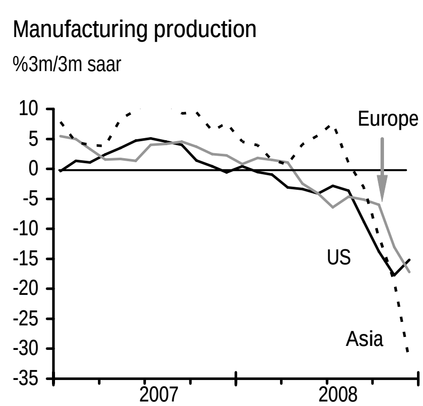
In the midst of a deep and synchronized global economic downturn, two elements in the recent data flow stand out. First, the US labour market is shedding jobs at an alarming rate. Private-sector employment fell at a 5.5% annual pace during the last three months of 2008, a pace last exceeded during an earlier credit crunch in the spring of 1980. The sharp slide in US employment contrasts markedly with labour-market performance elsewhere, where there is little evidence of significant cutbacks to date. Although the relative weakness of the US labour market is striking, the relative weakness in Asian industry also stands out. Asian industrial production is estimated to have declined at a 32% pace last quarter, roughly double the rate of decline in the Americas and Europe.

We have been expecting this pattern of activity to emerge around year end. The two negative shocks that hit the global economy during 2008—rising energy prices and tightening credit conditions—lowered demand across the globe. However, US domestic demand was hit hardest with consumption diving during the summer and early fall as the impact of these drags were magnified by a collapse in wealth and confidence. It is thus no surprise that US firms have responded aggressively. At the same time, global demand for autos and other consumer durables—which were sensitive to both credit and energy shocks—found a significant source in Asian industry. Combined with a trade financing squeeze during September and October, industrial activity has collapsed in countries important in the production chain for autos and high-tech.

There are, however, other dynamics at work that are important for the path ahead. Asian producers appear to have been slow to respond to gathering clouds in the global business cycle through 2008; their recent behavior likely marks the start of an overdue correction in levels of employment, inventories, and capital spending. It is troubling that there is little evidence of progress thus far, as regional employment and manufacturing inventories rose last quarter despite the sharp falloff in production. With pricing power also waning, margins are being squeezed; it looks like this adjustment will remain intense through the early months of this year.

In the US, the aggressive actions by firms likely maintained productivity levels and prevented a buildup in finished goods inventories last quarter. Both finished goods inventories and final sales look to have fallen during the quarter with the inventory/sales ratio moving higher. These developments send a mixed message about the future. With labor market adjustments producing a sharp compression in nominal incomes, there is reason to be concerned that the feedback loop from business retrenchment to household demand will be powerful and extend the downturn. However, there is reason to hope that important supports now being put in place—from lower





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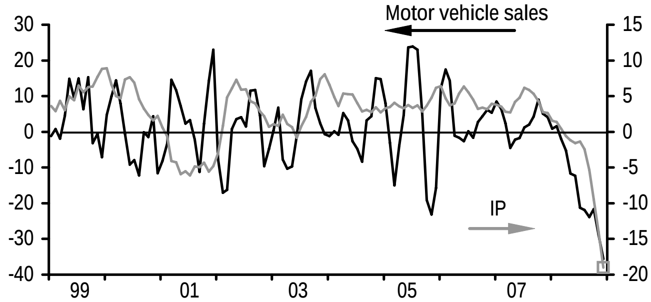
Global unit motor vehicle sales and industrial production

%3m/3m, saar both scales; Dec08 IP fcst boxed



energy prices, lower mortgage rates, and fiscal stimulus—can cushion household demand, paving the way for US business to complete its adjustment during 1H09 without further amplifying the recession. In this regard, US real consumption looks to have stabilized in November and December, a point likely to be supported by this week's retail sales report. The key test for the economy has still to come as we watch how households respond to continuing adjustments by firms.

Global inflation going to zero

Global inflation is plunging in response to the deep economic downturn and the associated collapse in commodity prices. Last week's reports registered sharp declines in December inflation across a range of countries in Europe and Asia. This week US CPI is expected to post a -0.3%oya reading—the first negative oya reading since 1955. Globally, inflation is expected to have eased to about 2%oya last month, down from a peak of 5.2% last July. We look for a continued decline toward zero by midyear.

The slide in inflation is working to cushion growth through several channels. With global consumer prices falling outright on a monthly basis, this has provided a powerful boost to household purchasing power. Indeed, this boost probably is reflected in the widespread gains in retail sales volume in November, and the stabilization of global automobile sales in December. In addition, with headline inflation already dropping below central bank targets and resource utilization set to fall considerably further in 2009, monetary policymakers are moving aggressively to lower rates. Global real rates have now fallen below zero, as widespread easing in the developed economies is being reinforced by more reticent central banks in the EM. Last week's moves in the UK, Korea, Indonesia, and Chile maintained the global easing process.

ECB to respond to deepening gloom

This week, it's the ECB's turn and we expect it to ease 50bp, bringing policy rates down to 2%. Activity data have continued to come in on the weak side in the Euro area, making it clear that the economy contracted more in the final quarter of last year than we were previously assuming. Instead of the 3.5% annualized drop in GDP that we were anticipating, we now think that the Euro area economy contracted 4% annualized, with a particularly sharp 5% decline in Germany. Meanwhile, inflation is now below the ECB's definition of price stability, with a decisive move down to 1.6% in December.

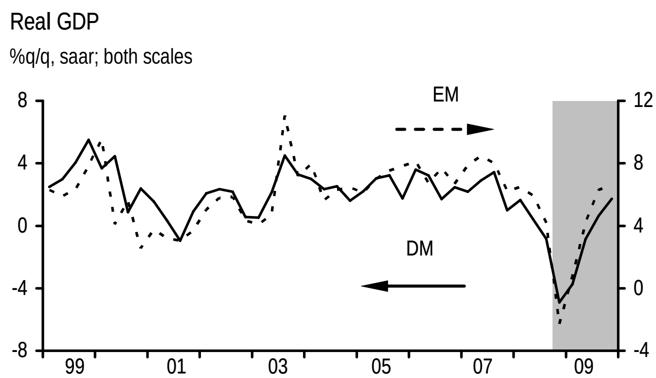
Back in early December, the ECB staff forecast suggested a growth trajectory that comprised a GDP contraction of around 1.5% in the fourth quarter of last year, and one of around 1% in the first quarter of this year. It also suggested that CPI inflation would end last year at around 2%, and would average 1.4% this year. The data in recent weeks suggests that the macro landscape is falling well short of these projections. Our latest estimates suggest that the contraction in GDP in the six-month period from last autumn to this spring will be about three times as intense as the ECB anticipated in its last forecast.

With both growth and inflation currently undershooting the ECB forecast published in early December, the case for a further easing this week is strong. It is possible, that the ECB may pause, given that the policy rate has been cut 175bp in three months, and that the February meeting is only three weeks later. If it does, this would not affect our view of a terminal rate of 1% later in the spring.

EM showing its unit beta stripes

Although the most strikingly negative data have come out of EM Asia, incoming reports from CEEMEA and Latin America show that virtually the entire EM group was engulfed in recession at year end. Indeed, there is every indication that economic activity in the EM has fallen in lockstep with the developed economies, consistent with the unit beta relationship we identified in previous research. Indeed, once the unfolding revision process at JPMorgan runs its course, this is likely to culminate in back to back declines in EM GDP in 4Q08 and 1Q09—something that did not happen during the long-running EM financial crisis a decade ago.

The past week provided further confirmation that the



CEEMEA region is in recession. Available data show that regional manufacturing output was on track for a 20%-plus (%q/q, saar) decline in 4Q08. One common theme was the effect that the collapse in global auto sales has had on key producing countries including Russia, Turkey, the Czech Republic, and Poland. As data disappoint, we continue to mark down forecasts. Last week we lowered our 2009 growth projection for South Africa an additional 0.5% point to just 0.4%y/y. Likewise, Turkey's GDP growth forecast was cut from 2.2% to 1.7% for 2008 and from 0.5% to -0.8% for 2009. Additional revisions to other countries in the region are likely in coming days. With growth and inflation sliding, more policy ease is on the way. We now expect the CBRT to cut its key policy rate 100bp to 14% in next week's meeting, with rates on their way to 12.5% by April.

The gas conflict between Russia and Ukraine has added an additional downside growth risk in the region, although both sides have now agreed to allow international observers to monitor gas transit, which should help restore gas supplies to Europe shortly. The countries that appear to have been most affected are Bulgaria, Hungary, Slovakia, and the Balkans. Some countries in the region have already announced gas supply restrictions to large industrial producers. Key car manufacturers in Hungary and Slovakia, for example, have announced cuts in production, citing gas shortages, although weaker demand is also to blame.

In addition to CEEMEA, data releases from Latin America over the past two weeks confirmed a severe deceleration of economic activity in the last quarter of 2008. While weak activity numbers have been commonplace in Colombia and Mexico since the middle of last year, Brazil and Chile have delivered significant negative surprises of late. In Brazil, last week's data confirmed that auto sales and production, as well as overall IP, are falling sharply. In response, we revised down our GDP growth forecasts to an even sharper slowdown of -4.4%q/q, saar in 4Q08 (from -3.8%) and -2.2%q/q, saar in 1Q09 (from +0.4%). In Chile, the drop in November IP coincided with another negative print in the monthly economic activity indicator (IMACEC), prompting a revision of GDP growth projections to -4.0%q/q, saar in 4Q08 (from 2.0% previously) and -3.0% in 1Q09 (from 2.5% before). Thus, Brazil and Chile have joined Argentina and Mexico among the Latin American countries falling into outright recession at the end of last year

Amid weaker activity data, inflation is finally becoming a second-order consideration for Latin central banks—as in the rest of the world. Whether actual inflation prints already show moderation, the policy bias is turning decisively in favor of supporting growth, and central banks seem willing to frontload cuts as they embark on easing cycles. After Colombia's unexpectedly large 50bp cut in December, Chile surprised markets with a 100bp cut last week. We now expect Mexico and Brazil to kick off their easing cycles with a cut of 50bp in Mexico on January 16 and 75bp in Brazil on January 21. Peru, which stood pat last week, is now expected to cut 25bp in February. During the first half of the year, cumulative easing is expected to reach 250bp in Brazil and Chile, 200bp in Colombia and Mexico, and 100bp in Peru. As elsewhere, these moves are being complemented with fiscal support to try to contain the downturn.

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JPMorgan View - Global Markets

The third derivative

Amid the awful news on the world economy, there is one glimmer of hope. The **third derivative of GDP and earnings forecasts is positive**. The consensus expects both GDP and corporate earnings to contract, and every few weeks these expectations keep being lowered. Both the 1st and 2nd derivative thus remain negative. But the pace of the forecast revisions itself is becoming less negative, producing a positive 3rd derivative. If this sounds like grasping at straws, it is. A slowing in the pace of downward revisions in forecasts is a necessary condition for recovery trades, but it is far from sufficient. However, waiting for upward forecast revisions will likely get us into risky assets well after the rally. Hence, we look instead for a flattening of growth expectations—no further falls. We are not there yet, and thus stay broadly in recession trades.

At the start of this year, we **concentrate recession exposures in bonds, commodities, and currencies**. This means we stay squarely long duration, pushing more and more into local EM bonds where central banks are now playing catch-up with those in developed markets. In commodities, we are outright short base metals. In credit and equities, we have tactically covered our bearish positions, recognizing that value-oriented investors are now making some of their long-delayed allocations. In credit, we position long in US spread products, effectively coinvesting with the Fed/Treasury complex.

Beyond the issue of how long and deep the recession will be, there are two other debates raging among market participants: How will the market absorb the almost $2 trillion in government bond issuance this year? And which risky asset class—credit or equities—is the best recovery trade? On issuance, we have a minority view that it will be absorbed at falling yields by heavy buying by commercial and central banks. On the equity vs credit horse race, there is a lively debate among clients, and within this Bank, on who will win the race. In the last two months of last year, equities were clearly beating credit as the latter was held down by hedge fund deleveraging. In the first full week of this year, though, credit is winning hands down, as value-flows are favouring it, while equities are getting hurt by the start of the earnings season.

Fixed income

The front end continued to rally on expectations that central banks will remain aggressive in supporting growth. 10yr rates sold off early in the week on supply concerns, but recovered Friday as falling equity markets and weak jobs data reinforced the reality of the global economic recession. **We stay bullish duration near term, on weak economic data and quantitative easing**.

10-yr Government bond yields

	Current	Mar 09	Jun 09	Sep 09	Dec 09
United States	2.38	2.40	2.00	1.75	1.65
Euro area	3.01	2.70	2.60	2.65	2.70
United Kingdom	3.13	3.05	3.00	3.00	3.05
Japan	1.27	1.25	1.35	1.55	1.55

Foreign exchange

	Current	Mar 09	Jun 09	Sep 09	Dec 09
EUR/USD	1.35	1.28	1.30	1.35	1.37
USD/JPY	90.3	88	85	85	90
GBP/USD	1.52	1.36	1.41	1.48	1.52

Commodities

		Quarterly Average			
	Current	09Q1	09Q2	09Q3	09Q4
WTI ($/bbl)	40	38	40	45	50
Gold ($/oz)	860	750	800	825	825
Copper($/m ton)	3162	3000	3000	3250	3300
Corn ($/Bu)	4.12	4.45	5.30	5.15	5.00

Source: J.P. Morgan, Bloomberg, Datastream

The **main risk** in being long duration is that an avalanche of **government bond issuance** will overwhelm an investor community already overweight in bonds. In our forecasts, net issuance in our Global GBI universe (think G10) will be $1.9tr in 2009, double the pace of last year. Massive as this supply pressure is, the market should be able to absorb it, at least until the middle of this year. We expect issuance to be met by strong demand from EM central banks that are loath to let their currencies appreciate, DM central banks that expand their holdings with an objective to lower bond yields, and commercial banks that find a shrinking credit demand from the private sector.

Having reached our target levels, we **take profits on EU and UK steepeners.** We reintroduce a **2s10s flattener in the US.** As policy rates have reached cycle lows, further rallies will likely turn into bullish flattening. **We remain overweight the new market for FDIC guaranteed bank debt, Agency debt**, as well as MBS, although the latter has come close to our spread targets. We believe these trades will be supported by heavy government bond issuance, buying by the Fed and the Treasury, reduced bank funding costs, and a gradual fall in volatility that will raise demand for carry.

Equities

Last week, equity markets gave back the previous week's gains on worries about the 4Q reporting season. Our expectation is for the operating S&P500 EPS to post a reading of $13.40 for 4Q, which is below both the bottom-up consensus of $16 and the top-down consensus of $17. Thus we are likely to face a **4Q earnings disappointment** in coming weeks that could bring an early end to the current bear market rally, despite the improvement in flows.

Cyclical stocks continued to outperform last week even as equity markets declined. The relative performance of cyclical vs noncyclical sectors correlates well with the global PMI index, which we view is near the low for this recession and is likely to turn upward by March. Thus, we are biased towards further outperformance in coming months.

Our economic forecasts look for a rotation in activity data from consumers to producers. We thus favor **an overweight in US discretionary vs industrials. Materials** continued to outperform Energy this week. We stay with this trade as the large gap in the relative valuation between Energy and Material stocks remains. Within EM, although we remain more positive in Asia medium term, the trade is less attractive near term given the higher beta of EM Asia to the global IP cycle thus we prefer staying out for now.

Credit

The **momentum in flows** has improved significantly over the past few weeks. **Primary issuance has been very strong** over the past week in both the US and Europe even after excluding government guaranteed bank paper, a reflection of how much demand has improved. Low government bond yields are inducing demand for government-guaranteed bank bonds from agency and government funds. This removes a significant amount of bank bond supply from traditional HG investors and thus is supportive of **bank credit** which we remain overweight. The **improvement in sentiment** has been also reflected in last week's US HG credit client survey. Two thirds of respondents—mostly real money—expect tighter spreads over the next month, which is the highest level since the survey began in 2001. Moreover, 50% of respondents expect their assets dedicated to HG bonds to increase in this quarter vs the previous quarter.

In the US, we turn more positive by **adding risk to our ABS overweight and upgrading CMBS to overweight.** We are less positive in Europe. With the default cycle yet to begin in Europe, a lack of direct government buying (e.g., CP), lower policy support, and lower buying interest reported by our European trading desks, we remain cautious and keep a **small underweight in European HG credit**. In HY, we see more upside in high quality HY bonds and loans.

Foreign exchange

Although a zero-rate world draws closer with every central bank meeting, several vexing questions remain unanswered. These include: Who next joins the Fed and Bank of Japan at zero? How aggressive will quantitative easing be? And, how will governments attract financing while paying pittance yields? Given present policies, we still expect the dollar and sterling to prove the weakest currencies in 2009. But in such a fluid policy environment, we have high conviction only on short-term views and will switch allegiances as and when policymakers change the rules of engagement. The main risk is a continuation of the equity market recovery which began November 21 and has been proceeding in fits and starts since. But given the lack of policy impact from stimulus measures until 2Q/3Q, we are comfortable fading these risky market moves, reentering short USD/JPY and AUD/JPY positions. We are already short CHF/JPY. We also **begin to reintroduce relative value trades** (NOK/SEK). RV may seem foolhardy in a market undergoing structural change, but given that positions are now much cleaner, rates/fx betas are reasserting themselves. This is an encouraging sign for RV.

Alternatives

We expect HF performance to remain modest in 1Q, owing to continued redemptions, but improving later this year to deliver 5-8% in 2009. Weak demand is still the main medium-term driver for **oil**, despite the political tension in the Middle East. The Brent curve remains very steep and we recommend flatteners. While we are overall negative on industrial metals, **copper** remains the most vulnerable as inventories keep rising, prices are comfortably above marginal cost, and supportive Chinese buying should be mostly temporary. **Agricultural** commodities remain our favourite sector since demand is less sensitive to overall economic conditions. We are long agriculture vs industrial metals, and short copper, in particular.

Markets - Australia and New Zealand

Australia

- **Since the December RBA Board meeting, the data flow have been mixed for the RBA. While some of the local real time data have been more optimistic in recent weeks, offshore data have continued to remain very weak (although we note that some of the offshore data may be starting to show tentative signs of stabilization, albeit at extremely low levels).**
- **For the RBA, a key assessment in coming months will be whether this pick up in activity indicators represents a meaningful and sustained change in economic momentum, or whether it is merely a blip in an otherwise downward trend.**
- **In Australia, bond yields are now around 20bps off recent lows. If this is the start of a genuine mid-easing cycle sell-off, then yields can move at least another 50bps higher. Accordingly, we favour tactical shorts in the Australian bond market at present.**
- **In this environment, trades with a bearish bias should perform well. Paid positions in AUD 3m1y swap offer modestly attractive rollup to spot, and received swap/efp positions should perform. NZD rates also look ready for some under-performance relative to AUD rates.**
- **Strategically, we would use any sell-off as an opportunity to re-establish longs. We would target a move to 96.00-96.25 in 3-years in the first instance before looking to buy the market. We still believe that risks are biased towards lower yields in 2009 as the macroeconomic environment remains sluggish amidst continued household deleveraging.**
- **The yield curve is proving difficult to pick at present. For the near term, we favour a range of 60-85bps within a broader flattening trend. We will be wrong on this view if the RBA needs to be more aggressive than currently priced by the market and the cash rate troughs later in 2009.**

A mixed bag for the RBA…

The first Tuesday of January passed without any announcement from the RBA. But there should be some interesting discussion at February's meeting. On the one hand, global economic data has continued to print on the soft side of expectations. The outlook for Japanese GDP is now considerably weaker in the wake of some extremely weak industrial numbers released just before Christmas. Our economists now expect GDP to fall by a 7% quarterly annualised rate in both Q4 08 and Q1 09. This has prompted reasonable downward revisions to the global growth outlook (given Japan's importance to global growth); we now expect global growth to contract 4.1% (saar) in Q4 2008 and 2.6% (saar) in Q1 2009 (see chart 1). This downgrade is also significant for Australia, given Japan's status as one our largest trading partners. We now expect Australian GDP growth of just 0.2% this year.

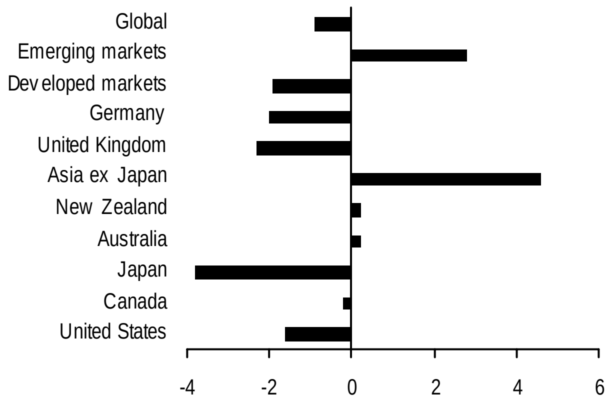
Locally, anecdotes from retailers suggest that December was a much better month for household spending. Industry data suggest that car sales rose by almost 7% in December. Just before Christmas, retailer Harvey Norman reported some like-for-like sales data, which suggest that momentum in retail sales picked up appreciably over December (see chart 2). These data imply that the policy stimulus (a combination of rate cuts and government handouts) is having some impact, at least in the short term. Although retail sales ex food fell 0.5% in November, the risk is that some of the activity data could print a bit better in coming weeks. Indeed, some of the early surveys of the manufacturing and services industries have shown slightly better readings for December; while the actual levels remain at depressed levels, it is important to acknowledge that the outright levels are not falling further.

The building approvals data for November were genuinely weak – apartment approvals, which are the notoriously volatile part of these data, fell 20% – but "core" approvals, ie, private sector houses, were off 10% in the month. This is an extremely sharp fall and does not bode well for economic activity given that approvals are a good leading indicator of employment and residential investment.

These data highlight how hard it will be to get a good read on the economy in the first few months of this year – some of the data will continue to print very weak, but others (such as consumer confidence and retail spending) will probably show some signs of life. It will make the very front end of the curve difficult to trade, and explains why the market has largely hedged its bets between a 50bp and 100bp cut next month.

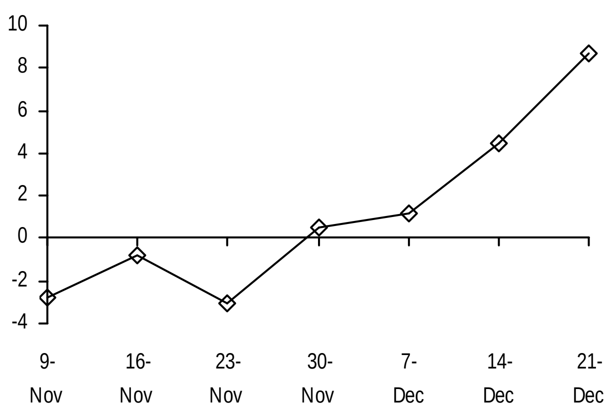
For the RBA, a key assessment in coming months will be whether this pick up in retail activity represents a meaningful and sustained change in retail spending as we head into 2009,

Chart 1: J.P. Morgan's growth forecasts for 2009
Annual average percent



Source: J.P. Morgan

Chart 2: Harvey Norman like-for-like sales* showing signs of better momentum in December
Percent



or whether it is merely a blip in an otherwise downward trend. For fixed income markets, we suspect a better tone to the activity data could well add to bearish sentiment. Essentially, the RBA will need to make an assessment about whether the stance of policy looks appropriate given the outlook for growth and inflation. The December Board minutes suggest that the RBA was comfortable with the setting of policy. Since this meeting, the incoming data has been mixed. The global data remains weak but real time Australian data has been more positive. Our economists expect the trough in the cash rate to be reached in March, with a terminal rate of 3.5% for the cycle. Risks to this view are biased to the downside.

Is this the mid-cycle sell off?

The new year has not been a positive one so far for the Australian bond market. This is consistent with price action globally; 2009 appears to have brought a considerable change in sentiment toward government bonds. In December, investors were happy to continue buying government bonds, with risk aversion, very soft data and the prospect of quantitative easing all supportive for fixed income markets. But 2009 has brought with it concerns that global government bond markets look expensive, an uncomfortable outlook given the prospect of considerably higher bond supply in many markets. Already, 3-year and 10-year yields are around 20bps off cyclical lows. The yield curve, consistent with price action in other markets, has bearishly steepened over the past week.

For a little while we have suggested that the local market has looked ready for an easing cycle sell off. As we have noted before, this has been a feature of previous easing cycles, usually spurred by a "mini pause" from the central bank. If the RBA entertains the idea of waiting another month or two before easing again or if we are close to the end of the easing cycle, then the front end of the Australian yield curve could move considerably higher in yield in coming weeks. We suspect the current weakness in the bond market could well turn out to be the mid cycle sell-off we have been waiting for.

Tactically, we therefore favour playing the market from the short side, and target a move to 96.00-96.25 in 3-years. This would represent a correction of around 60-80bps from the high seen in mid December – a mild mid cycle sell-off by historical standards (see chart 3), but consistent with the bottom of the bullish channel in place for much of the last 7 months (chart 4). Our sense of positioning at present suggests that the short base remains modest, with most of the selling of late reportedly driven by offshore investors. So perhaps the risk lies towards a sell off that is greater in magnitude than we currently expect.

In this environment, trades with a bearish bias should perform well. We like outright short positions; paid positions in AUD 3m1y swap offer modestly attractive rollup to spot. We also favour received swap/efp positions. NZD rates also look ready for some underperformance relative to AUD rates.

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Strategically, we would look upon any sell-off as a good opportunity to re-establish longs. We suspect that macro-economic environment will remain sluggish at best in 2009; on our forecasts, global growth is expected to contract by 0.9% this year. With the unemployment rate expected to rise appreciably in coming months, asset prices will remain subdued. Consumption may look slightly better in 2009, but once again, any prospect of meaningful growth in household expenditure will be capped by a rising unemployment rate and ongoing balance sheet deleveraging. And investment growth looks set to take a significant step down in 2009 in light of the correction in commodity prices.

The yield curve – where to next?

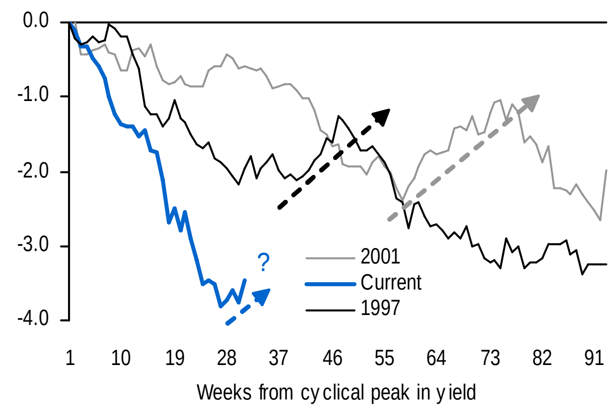
The AUD 3s10s bond curve is now 36bps off its peak, and remains in a broader flattening trend for the time being (chart 5). But movements in the yield curve of late have perplexed a number of investors. We don't disagree – the dynamics of yield curves are difficult to disentangle at the moment. In the US, the curve is simply a directional play. With the front end of the curve tied to a 0% to 0.25% range for the Fed Funds rate for the foreseeable future, movements in the 10-year sector will be the prime determinant of curve direction. We suspect steepening will ultimately be limited by the potential for the Fed to purchase longer dated USTs.

- The monetary policy cycle. Interestingly, movements in the yield curve are consistent with our house view on the RBA cash rate. Our economists are expecting the cash rate to trough in March. This is consistent with historical experience – the yield curve tends to peak 3-4 months ahead of the trough in the cash rate. We also note that a cash rate of 2.75% or 3% by Q1 would also be consistent with a curve peak in November 2008.

- Offshore influences. As **chart 6** illustrates, the dominant trend of late in offshore markets has been for yield curves to steepen. It is this dynamic which is largely responsible for the recent steepening of the Australian yield curve. But as we note above, we ultimately think any such effect will be limited by the potential for the Fed to purchase longer dated USTs.

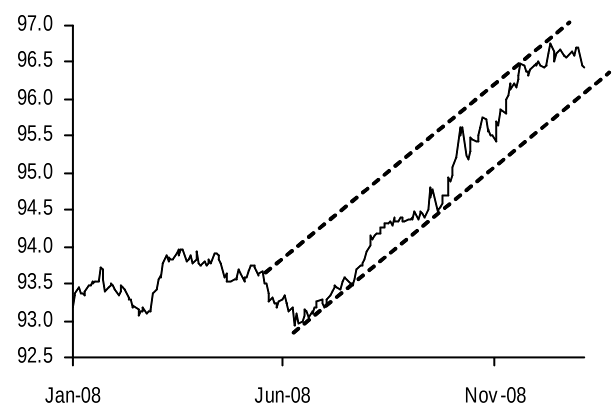
- Supply and inflation. The prospect of greater supply of ACGBs and globally generated inflation *could* work to steepen the curve (although we note that the sharp rise in JGB supply did not lead to a structurally steeper curve in Japan). Typically, the inflation risk premium is greatest at the long end of the curve.

Chart 3: Mid-cycle sell offs are usually a feature of easing cycles
Percentage Points, weekly data



Source: J.P. Morgan and Bloomberg

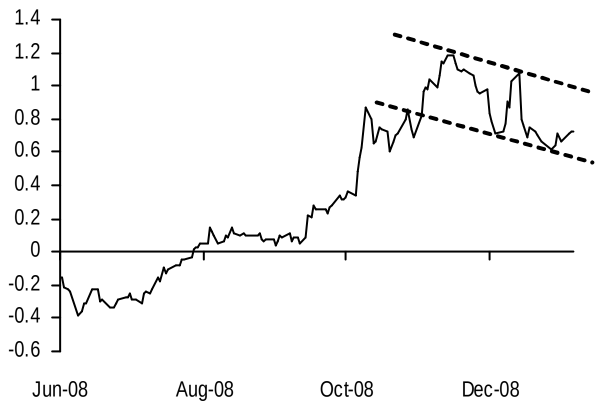
Chart 4: 3-year bond futures are currently mid range; look for a retracement to the 96.00 level
Price



Source: J.P. Morgan and Bloomberg

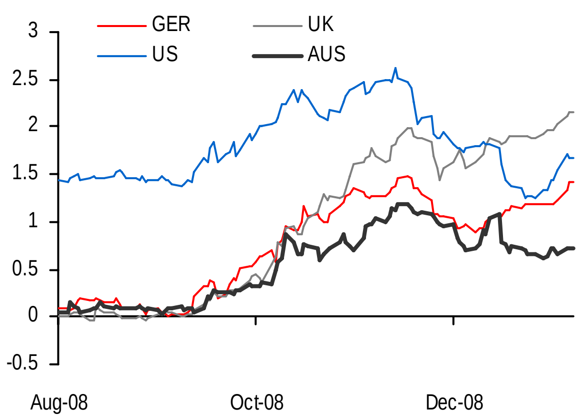
Ultimately, forecasting yield curves in 2009 will require an ability to distinguish between the influence of cyclical and structural factors. In Australia, the influence of structural factors should be limited to the extent that they will be mostly preva-

Chart 5: The AUD 3s10s curve
Percentage Points, daily data, basis futures



Source: J.P. Morgan and Bloomberg

Chart 6: Government bond yield curves (AUD is 3s10s, all others 2s10s)
Percentage Points, daily data



Source: J.P. Morgan and Bloomberg

lent in offshore markets (that is, those markets where quantitative easing is in play). Accordingly, cyclical factors are probably the best guide to local curve dynamics. **At the moment, we would be happy to characterize the 3s10s curve as range bound within a flattening trend, with a range of 60-85bps for the time being.** This view is consistent with the cash rate reaching a trough in late Q1 or early Q2. We will be wrong on this view if the cash rate troughs later in 2009, and the RBA needs to be more aggressive than currently priced by the market.

New Zealand

- **As expected, the RBNZ delivered a 150bps rate cut in early December. But more weak data suggests that the RBNZ's job is not yet done. We expect more rate cuts from the central bank in the new year.**
- **We think that one of the more obvious mis-pricings in the New Zealand fixed income market relates to the NZD 2s10s spot swap curve. All of our models continue to point to the fact that the curve is too flat, given economic fundamentals.**

The data flow in New Zealand has been largely minimal over the past couple of weeks, but unlike Australia, the local data has shown little sign of improvement. **Chart 1** illustrates household credit fell for the first time in November since the series began. Credit card spending in November was also softer than expected, falling 2.3% in the month. The WBC McDermott-Miller measure of consumer confidence reached a new cycle low in Q4, with the jobs plentiful index falling from +25% in Q3 to -26% in Q4.

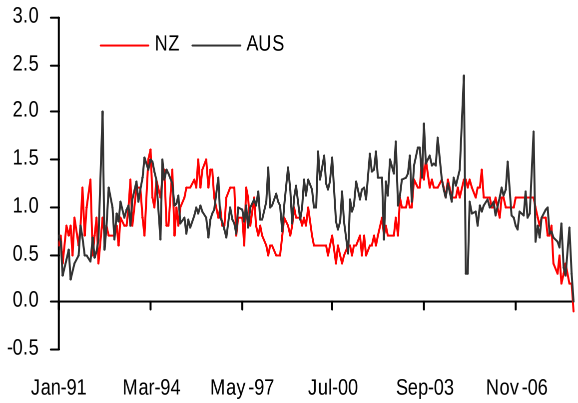
The combination of more weak domestic data and ongoing distress in global economic data means that there is still plenty of scope for the policy rate to fall further in New Zealand. Our economists expect a 50bp cut to the cash rate later this month; risks are likely biased towards a 75bp cut. A 75bp cut would leave the NZ policy rate on par with the policy rate in Australia. Interestingly, our global PMI suggests that the RBNZ still has plenty of scope to ease rates further (see **chart 2**).This is in contrast to Australia, where the current setting of policy looks broadly appropriate when we use the J.P. Morgan's global PMI as a benchmark.

All our models continue to point towards the risk of further steepening in the NZD 2s10s swap curve. The J.P. Morgan global PMI is telling a similar story (see **chart 3**). Accordingly, for investors who still like exposure to 'recession' or long duration trades, we think 2s10s steepeners in NZD swaps are the best way to express this view. Having said that, the main risk to this view is largely centred around the RBNZ's inflation targeting mandate. Just last month, Governor Bollard expressed concern about the domestic inflation outlook. If the RBNZ do not lower the OCR as much as we anticipate, then the curve will struggle to steepen much further from here.

Trade Updates

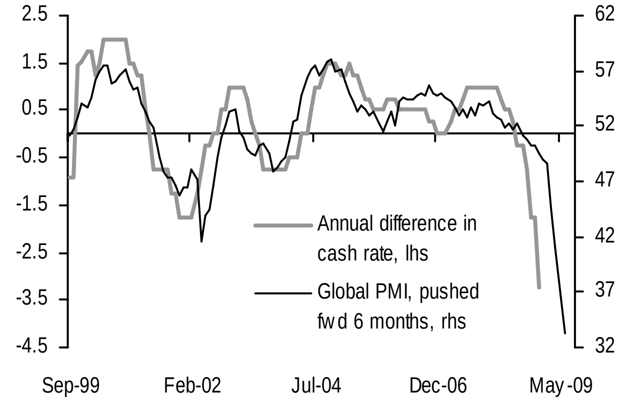
- **Received positions in 5-year swap/efp vs 10-year swap/efp.** We entered the trade at a spread of -57bps, and it has moved 1bp in our favour. We recommend continuing to hold the trade in anticipation of further out-performance by the 5y/efp spread.
- **Received positions in AUD 1y1y swap vs NZD 1y1y swap.** We entered this trade at a spread of 50bps and the trade has moved against us so far (to be at 41bps). We placed a stop at 35bps.
- **Paid positions in AUD 3m1y swap.** The market has rallied since we entered this trade earlier in the week, with the 3m1y swap rate close to our stop level of 3.14%. We recommend leaving the position to run.

Chart 1: Household credit growth registered its first ever monthly decline in New Zealand in November
Percent, month-on-month, household + personal



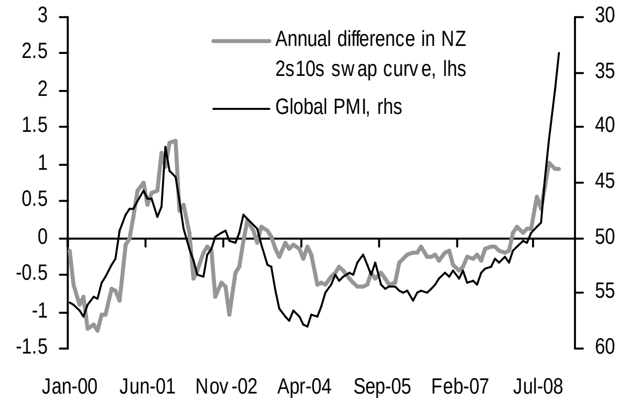
Source: J.P. Morgan, RBA and RBNZ

Chart 2: The RBNZ clearly has more work to do, according to J.P. Morgan's global PMI
Percentage Points Index



Source: J.P. Morgan and RBNZ

Chart 3: NZD 2s10s curve looks to have scope to steepen further
Percentage Points Index



Source: J.P. Morgan and Bloomberg

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AUD and NZD Commentary

- **Beyond the noise of earnings season, the story for 1Q is still about an indefinite recession and a zero-interest rate environment. Stay defensive, expecting a weaker USD vs JPY but a range-bound EUR/USD. Go short AUD/JPY.**

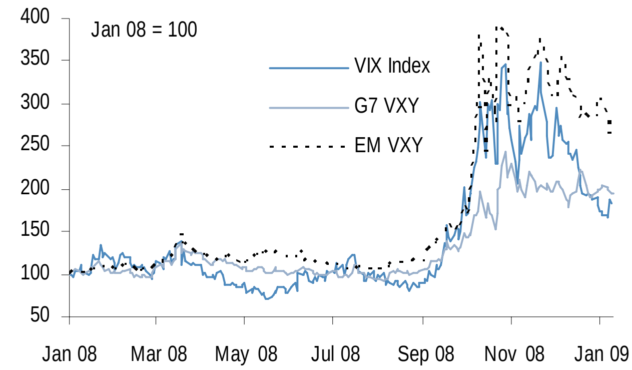
- **Technicals: Broad ranges continue, as both AUD/USD and NZD/USD approach critical resistance levels**

- Financial markets are moving in uncomfortable fits and starts, but through the intra-week gyrations, a trend is emerging. Since Nov. 20—the day the President-elect Obama nominated his Treasury Secretary – risky markets have edged meaningfully higher. The S&P has rallied 19%, high-grade credit spreads have narrowed 60bp, and equity and rate vol have collapsed. Forex markets are tracking those moves, albeit haltingly, with high-yield currencies roughly 1.5% - 2.5% higher and G-10 implied vol two points lower.
- We look for opportunities to fade the rally in markets; we view the greatest obstacle to sustained momentum in the risky markets is policy impact. As massive as US monetary stimulus has been and fiscal policy will be, we believe they are unlikely to impact activity data until the second half of 2009. In the interim, it seems heroic to bet on the length of this recession, even if most investors agree that Q1/Q2 2009 is a write-off. We suspect that any Dec/Jan glow around risky markets will fade once a US fiscal package is detailed and the reality of a multi-month implementation lag sets in. The Fed will likely precede with its quantitative easing program while the BoE contemplates its, which should renew the downward pressure on both currencies.
- From an FX perspective, we recommend staying in defensive trades, primarily short USD/JPY. We also expect the commodity currencies to give back some of their recent gains, and we recommend going short AUD/JPY, the G-10 currency cross most closely tied to risk aversion/appetite.
- The week ahead is dominated by the ECB rates decision. Against the backdrop of sharply deteriorating macro conditions and receding inflation expectations, we look for a 50bps rate cut and a downbeat tone to the press conference, a fact which should weigh on EUR. With global demand and cross-border capital flows collapsing, trade data from UK, Euro area and US as well as US TIC flow data will be keenly anticipated. A surprise in the Australian employment report should trigger a knee-jerk reaction in AUD.

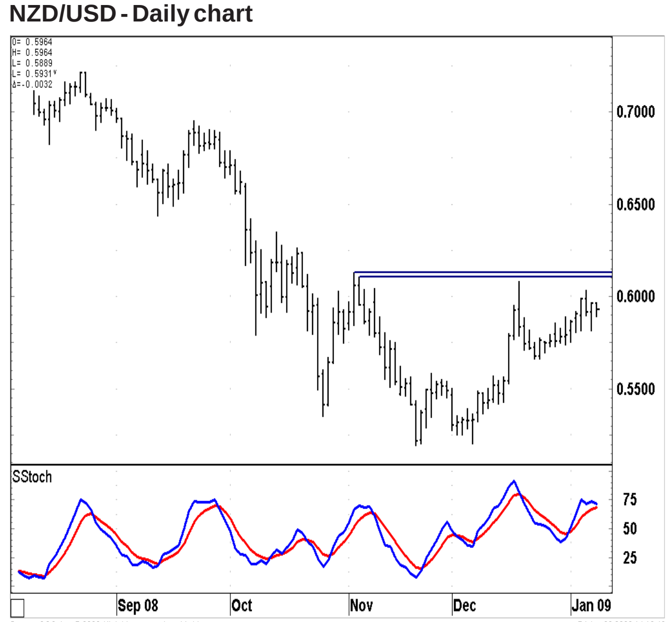
Technical analysis

- The broad ranges for NZD/USD and AUD/USD continue to develop. However, we see an important juncture for both as the advances from the late-2008 lows are now testing critical levels, which should define whether the ranges persist, or a bullish breakout is underway. For AUD/USD the key levels to watch start at the 0.7240/.7350 zone, which includes the October highs. Breaks would at least a short term base breakout and deeper retracement initially to the 0.75 area, if not a sustained recovery to the 0.77/.78 zone, which represents the breakdown zone from early-Oct. Importantly, near term dips will now find support at 0.6950 and 0.6850, which should maintain the more immediate upside bias.
- NZD/USD maintains the two-sided bias after approaching the critical 0.6080/.6130 resistance zone, which includes the late-October high, as well as the Nov/Dec peaks. This area will remain the key upside pivot with breaks confirming a deeper retracement into the 0.6350/0.6440 zone. The 0.5815/00 area will now act as initial support, while the 0.5660 level should hold to maintain the short term bullish framework and an upside resolution to this range.

Chart 1: Equity market volatility has fallen more than FX volatility
EASI indices for US, Euro area and UK



NZD/USD - Daily chart



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Global Economic Outlook Summary

	Real GDP % over a year ago			Real GDP % over previous period, saar							Consumer prices % over a year ago			
	2007	2008	2009	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	3Q08	4Q08	2Q09	4Q09
The Americas														
United States	2.0	1.1	-1.6	-0.5	-6.0	-3.0	-0.5	1.5	2.5	2.5	5.3	1.2 ↓	-1.6 ↓	0.3 ↓
Canada	2.7	0.7	-0.2	1.3	-1.5	-2.0	0.0	2.0	2.5	3.0	3.4	1.7	0.1	1.6
Latin America	5.3	4.1	0.7 ↓	4.4	-2.8 ↓	-1.9 ↓	1.0 ↑	3.8 ↑	4.0 ↑	3.6 ↓	8.2	8.3	7.7 ↓	7.0 ↓
Argentina	8.7	6.5	-1.0	6.6	-2.0	-3.9	-3.9	0.0	-2.0	4.0	8.9	8.1	7.9	9.7
Brazil	5.7	5.7	1.5 ↓	7.4	-4.4 ↓	-2.3 ↓	3.9 ↑	5.8 ↑	5.5 ↑	2.5	6.3	6.3	5.0	4.8
Chile	5.1	3.7 ↓	1.0 ↓	-0.2 ↓	-4.0 ↓	-3.0 ↓	0.0 ↓	12.0 ↑	8.0 ↑	0.0 ↓	9.3	8.6 ↓	5.5 ↓	3.5 ↓
Colombia	7.7	3.2	2.5	2.3	2.0	1.8	2.5	4.0	3.0	3.5	7.7	7.4	5.9	5.5
Ecuador	2.5	7.0	2.0	4.5	-2.5	1.5	2.0	2.5	4.0	3.0	10.0	9.5	4.6	3.8
Mexico	3.2	1.5	-0.6	2.6	-4.0	-2.0	-1.0	2.0	4.1	5.0	5.5	6.0	5.3	3.7
Peru	8.9	9.5	5.3	8.2	4.4	2.8	5.5	6.0	5.5	7.0	6.1	6.3	5.5	4.5
Venezuela	8.4	5.0	1.5	-1.0	4.5	-2.5	2.0	2.0	2.0	2.0	34.7	34.1	42.1	41.8
Asia/Pacific														
Japan	2.4	-0.2	-3.8	-1.8	-7.0	-7.0	-1.5	-0.5	1.5	2.0	2.2	1.1	-0.4	-0.5
Australia	4.0	2.3	0.2	0.3	-0.5	-0.9	0.5	2.0	0.5	0.5	5.0	4.2	2.4	1.9
New Zealand	3.1	0.4	0.2	-1.5	-1.8	-0.9	-0.1	5.5	5.5	1.3	5.1	4.9	3.2	0.8
Asia ex. Japan	8.8	6.3 ↓	4.4 ↓	4.0 ↓	-2.4 ↓	2.5 ↓	7.2 ↑	8.9 ↑	9.1 ↑	6.0 ↓	6.5	5.0	1.8	1.6
China	11.9	9.2	7.8	6.4	1.2	6.1 ↓	10.8 ↑	12.3 ↑	12.8 ↑	7.0 ↓	5.3	3.3	0.5	1.2
Hong Kong	6.4	2.9	-1.3	-2.0	-5.5	-2.5	2.0	3.0	4.0	4.0	4.6	2.2	-0.7	-0.5
India	9.0	6.2	5.5	8.7	0.3	0.1	4.8	8.9	10.9	9.1	9.0	9.1	3.2	1.3
Indonesia	6.4	6.0	4.2	6.4	3.0	3.0	4.0	5.0	5.0	5.0	12.0	12.0	7.2	4.2
Korea	5.0	3.4 ↓	0.5 ↓	2.1 ↓	-11.0 ↓	0.0 ↓	5.9 ↑	7.0 ↑	4.5	4.0	5.5	4.5	3.0	3.2
Malaysia	6.3	5.2 ↓	2.0 ↓	3.1	-2.8 ↓	0.0 ↓	4.9	5.7	6.6	2.8	8.4	7.3	3.9	1.2
Philippines	7.2	4.6	3.5	6.1	0.6	2.0	3.6	4.9	4.5	4.5	12.2	10.7	4.7	3.0
Singapore	7.7	1.3	-2.5	-6.8	-13.3	-5.9	10.4	5.3	5.3	4.1	6.6	6.5	2.1	1.0
Taiwan	5.7	1.3 ↓	-1.9 ↓	-8.7	-10.5 ↓	-1.0 ↓	2.0 ↑	5.5 ↑	5.8	4.2	4.5	1.8 ↓	0.7	-0.3
Thailand	4.9	4.4	2.0	2.2	-0.4	1.2	2.8	4.1	4.1	3.2	7.2	2.2 ↓	-1.6	3.5
Africa														
South Africa	5.1	3.1 ↓	0.4 ↓	0.2	-0.7	-0.8 ↓	-0.1 ↓	1.9 ↓	3.3 ↓	3.1 ↑	13.4	11.6	6.2 ↓	5.0 ↓
Europe														
Euro area	2.6	0.8 ↓	-1.9 ↓	-0.7 ↑	-4.0 ↓	-3.5	-1.0	0.0	1.0	1.0	3.8	2.3 ↓	0.7 ↓	1.1
Germany	2.6	1.1 ↓	-2.3 ↓	-2.1	-5.0 ↓	-3.5	-1.0	0.0	1.0	1.0	3.3	1.9	0.2	0.2
France	2.1	0.7 ↓	-1.5 ↓	0.5 ↓	-4.0 ↓	-2.5	-1.0	0.0	1.0	1.0	3.6	2.2	0.3	0.8
Italy	1.4	-0.6 ↓	-2.3 ↓	-2.1 ↓	-5.0 ↓	-3.5	-1.0	0.0	1.0	1.0	4.1	3.0	1.6	1.5
Norway	6.2	2.2	-1.0	1.0	-2.0	-2.5	-1.5	0.0	1.0	1.0	4.7	3.6	1.6	0.4
Sweden	2.7	0.4 ↓	-1.7 ↓	-0.4	-4.0 ↓	-3.0	-1.0	0.0	1.0	1.0	4.3	2.7	-0.2	-0.4
Switzerland	3.3	1.7 ↓	-1.5 ↓	0.1	-4.0 ↓	-3.0	-1.0 ↓	0.5	1.0 ↓	1.2 ↓	3.0	1.6 ↓	0.0 ↓	0.4
United Kingdom	3.0	0.8	-2.5 ↓	-2.6	-5.0 ↓	-4.0	-1.5	0.0	1.0	1.0	4.8	3.8	0.7	0.2
Emerging Europe	6.4	4.7 ↓	-0.1 ↓	5.2	-1.6	-1.5	-1.6	0.5	1.6	2.8	10.7	9.6	7.6	6.8
Bulgaria	6.2	5.2	1.0	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	6.0	4.0	-1.0	3.8	3.0	-3.1	-2.5	-3.2	-1.5	1.0	6.6	5.2	0.7	1.2
Hungary	1.1	1.1	-3.0	-0.3	-2.5	-3.8	-5.0	-3.0	-1.0	1.5	6.3	4.3	1.9	2.6
Poland	6.7	5.0	1.5	4.9	1.5	1.0	-0.5	1.0	1.5	2.0	4.7	3.8	2.5	2.3
Romania	6.0	8.5	0.5	...	...	...	...	...	...	...	8.1	6.3	5.5	7.0
Russia	8.1	6.4	0.0	6.3	-4.5	-2.0	-1.0	2.0	3.0	4.1	14.9	13.8	11.6	10.4
Turkey	4.6	1.7 ↓	-0.8 ↓	...	...	...	...	...	...	...	11.7	10.9 ↓	9.3	7.5
Global	3.5	1.8	-1.0 ↓	0.2	-4.6 ↓	-2.8 ↓	0.2 ↑	1.8 ↑	2.7	2.5	5.0	2.8 ↓	0.6 ↓	1.2 ↓
Developed markets	2.4	0.8	-2.0 ↓	-0.8 ↑	-5.2 ↓	-3.7	-0.9 ↓	0.6	1.7	1.8	4.2	1.8 ↓	-0.4 ↓	0.5 ↓
Emerging markets	7.5	5.4 ↓	2.6 ↓	4.2	-2.3 ↓	0.8 ↓	4.2 ↑	6.3 ↑	6.6 ↑	4.9 ↓	7.8	6.7 ↓	4.3 ↓	3.9 ↓

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Global Central Bank Watch

	Official interest rate	Current	Change from Aug '07 (bp)	Last change	Next meeting	Forecast next change	Mar 09	Jun 09	Sep 09	Dec 09	Jun 10
Global	GDP-weighted average	2.18	-254				1.72	1.48	1.45	1.45	1.64
excluding US	GDP-weighted average	3.14	-133				2.46	2.12	2.08	2.07	2.17
Developed	GDP-weighted average	1.10	-304				0.69	0.53	0.53	0.53	0.73
Emerging	GDP-weighted average	6.46	-54				5.79	5.27	5.11	5.09	5.23
Latin America	GDP-weighted average	10.32	151				8.91	8.23	8.23	8.23	8.14
CEEMEA	GDP-weighted average	7.91	91				7.77	7.39	6.99	6.86	6.42
EM Asia	GDP-weighted average	4.46	-187				3.87	3.35	3.23	3.25	3.70
The Americas	GDP-weighted average	1.34	-426				1.15	1.07	1.07	1.07	1.39
United States	Federal funds rate	0.125	-512.5	16 Dec 08 (-87.5bp)	28 Jan 09	1Q 10 (+12.5bp)	0.125	0.125	0.125	0.125	0.50
Canada	Overnight funding rate	1.50	-300	9 Dec 08 (-75bp)	20 Jan 09	20 Jan 09 (-50bp)	1.00	1.00	1.00	1.00	1.25
Brazil	SELIC overnight rate	13.75	225	10 Sep 08 (+75bp)	21 Jan 09	**21 Jan 09 (-75bp)**	12.25	11.25	11.25	11.25	11.00
Mexico	Repo rate	8.25	100	15 Aug 08 (+25bp)	16 Jan 09	16 Jan 09 (-50bp)	6.75	6.25	6.25	6.25	6.25
Chile	Discount rate	7.25	175	**8 Jan 09 (-100bp)**	12 Feb 09	**12 Feb 09 (-75bp)**	6.00	5.75	5.75	5.75	5.75
Colombia	Repo rate	9.50	25	19 Dec 08 (-50bp)	30 Jan 09	30 Jan 09 (-50bp)	8.50	8.00	8.00	8.00	8.00
Peru	Reference rate	6.50	175	11 Sep 08 (+25bp)	5 Feb 09	**5 Feb 09 (-25bp)**	6.00	5.50	5.50	5.50	5.50
Europe/Africa	GDP-weighted average	2.96	-163				2.11	1.71	1.66	1.64	1.59
Euro area	Refi rate	2.50	-150	4 Dec 08 (-75bp)	15 Jan 09	15 Jan 09 (-50bp)	1.50	1.00	1.00	1.00	1.00
United Kingdom	Repo rate	1.50	-425	**8 Jan 09 (-50bp)**	5 Feb 09	**5 Feb 09 (-100bp)**	0.50	0.50	0.50	0.50	0.50
Sweden	Repo rate	2.00	-150	4 Dec 08 (-175bp)	11 Feb 09	11 Feb 09 (-50bp)	1.50	1.00	1.00	1.00	1.00
Norway	Deposit rate	3.00	-175	17 Dec 08 (-175bp)	4 Feb 09	4 Feb 09 (-50bp)	2.00	1.50	1.50	1.50	1.50
Czech Republic	2-week repo rate	2.25	-100	17 Dec 08 (-50bp)	5 Feb 09	5 Feb 09 (-50bp)	1.50	1.00	1.00	1.00	2.00
Hungary	2-week deposit rate	10.00	225	22 Dec 08 (-50bp)	19 Jan 09	19 Jan 09 (-50bp)	8.50	7.50	7.00	7.00	7.00
Israel	Base rate	1.75	-225	28 Dec 08 (-75bp)	26 Jan 09	26 Jan 09 (-50bp)	1.00	1.00	1.50	2.00	3.00
Poland	7-day intervention rate	5.00	25	23 Dec 08 (-75bp)	28 Jan 09	28 Jan 09 (-50bp)	4.00	3.50	3.50	3.50	3.50
Romania	Base rate	10.25	325	31 Jul 08 (+25bp)	4 Feb 09	**4 Feb 09 (+50bp)**	11.00	12.00	11.00	10.00	9.00
Russia	1-week deposit rate	6.75	350	28 Nov 08 (+100bp)	1Q 09	1Q 09 (+100bp)	8.75	8.75	7.75	7.75	6.75
South Africa	Repo rate	11.50	150	11 Dec 08 (-50bp)	12 Feb 09	12 Feb 09 (-100bp)	10.50	9.00	8.50	8.00	7.50
Switzerland	3-month Swiss Libor	0.50	-200	11 Dec 08 (-50bp)	13 Mar 08	3Q 10 (+25bp)	0.50	0.50	0.50	0.50	0.50
Turkey	Overnight borrowing rate	15.00	-250	18 Dec 08 (-125bp)	15 Jan 09	**15 Jan 09 (-100bp)**	13.00	12.50	12.50	12.00	11.00
Asia/Pacific	GDP-weighted average	2.35	-120				2.03	1.79	1.74	1.74	2.08
Australia	Cash rate	4.25	-225	2 Dec 08 (-100bp)	2 Feb 09	2 Feb 09 (-50bp)	3.50	3.50	3.50	3.50	4.50
New Zealand	Cash rate	5.00	-325	4 Dec 08 (-150bp)	29 Jan 09	29 Jan 09 (-50bp)	4.00	3.50	3.25	3.25	3.25
Japan	Overnight call rate	0.10	-40	19 Dec 08 (-20bp)	20 Jan 09	1Q 10 (+15bp)	0.10	0.10	0.10	0.10	0.25
Hong Kong	Discount window base	0.50	-625	17 Dec 08 (-100bp)	29 Jan 09	1Q 10 (+25bp)	0.50	0.50	0.50	0.50	1.00
China	1-year working capital	5.31	-171	22 Dec 08 (-27bp)	1Q 09	1Q 09 (-27bp)	4.77	4.23	3.96	3.96	4.50
Korea	Base rate	2.50	-250	**9 Jan 09 (-50bp)**	12 Feb 09	**12 Feb 09 (-25bp)**	2.00	2.00	2.00	2.00	2.50
Indonesia	BI rate	8.75	50	**7 Jan 09 (-50bp)**	4 Feb 09	**1Q 09 (-50bp)**	8.25	7.00	7.00	7.25	8.00
India	Repo rate	5.50	-225	2 Jan 09 (-100bp)	27 Jan 09	**27 Jan 09 (-50bp)**	4.50	3.50	3.50	3.50	3.50
Malaysia	Overnight policy rate	3.25	-25	24 Nov 08 (-25bp)	21 Jan 09	21 Jan 09 (-25bp)	2.75	2.25	2.25	2.25	2.75
Philippines	Reverse repo rate	5.50	-50	18 Dec 08 (-50bp)	29 Jan 09	29 Jan 09 (-25bp)	5.25	5.00	5.00	5.00	5.50
Thailand	1-day repo rate	2.75	-50	3 Dec 08 (-100bp)	14 Jan 09	14 Jan 09 (-50bp)	1.75	1.00	1.00	1.00	1.50
Taiwan	Official discount rate	1.50	-163	**7 Jan 09 (-50bp)**	1Q 09	**1Q 09 (-50bp)**	1.00	0.75	0.75	0.75	1.25

Bold denotes move since last GDW 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*

				2008			2009				2010			
	2008	2009	2010	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Chain volume GDP	2.3	0.2	1.7	1.4	0.3	-0.5	-0.9	0.5	2.0	0.5	0.5	2.3	3.5	5.0
Private consumption	2.0	-0.1	1.4	-0.5	0.2	-0.8	-1.6	0.8	1.6	1.2	0.8	1.6	2.0	3.2
Construction investment	3.8	-2.0	-2.8	1.6	2.1	-5.1	-3.8	-0.6	-0.6	-4.6	-5.4	-4.2	0.3	4.8
Equipment investment	13.7	-8.3	-7.1	39.4	-0.9	-22.7	-15.6	-2.1	-4.1	-8.1	-19.3	-4.1	4.3	8.6
Public investment	13.3	13.7	13.7	14.3	16.6	16.1	16.2	9.6	10.2	10.8	13.2	15.7	18.1	20.6
Government consumption	3.9	6.6	5.1	4.3	2.4	5.9	7.8	11.8	4.1	5.2	5.2	6.3	2.2	2.1
Exports of goods & services	5.2	-3.8	1.4	12.9	0.0	-0.8	-7.0	-11.5	-3.9	2.8	2.4	3.2	4.9	6.1
Imports of goods & services	12.1	-1.2	-0.2	14.0	6.5	-1.2	-3.9	-6.2	-2.8	-0.8	0.0	1.6	1.6	4.1
Contributions to GDP growth:														
Domestic final sales	4.0	0.8	1.5	4.0	1.2	-0.9	-0.7	2.8	1.8	0.8	-0.3	2.0	3.0	4.8
Inventories	-0.1	-0.2	-0.2	-1.8	0.7	0.3	0.4	-1.4	0.4	-1.1	0.3	0.0	0.0	0.0
Net trade	-1.7	-0.5	0.3	-0.7	-1.6	0.1	-0.5	-0.9	-0.1	0.8	0.5	0.3	0.6	0.3
GDP deflator (%oya)	6.6	3.6	1.8	6.6	8.4	7.4	6.6	4.0	1.9	1.9	1.8	1.7	1.7	2.0
Consumer prices (%oya)	4.5	2.3	2.0	4.5	5.0	4.2	3.3	2.4	1.7	1.9	2.1	1.9	2.0	2.1
Producer prices (%oya)	9.1	4.0	0.7	8.7	10.9	10.0	7.4	3.7	2.6	2.3	1.1	0.5	0.4	1.0
Trade balance (A$ bil, sa)	-5.1	4.4	13.6	-1.7	1.1	3.4	2.7	0.6	0.1	1.0	1.7	2.6	3.9	5.4
Current account (A$ bil, sa)	-67.0	-44.7	-35.4	-14.0	-9.7	-8.5	-9.3	-11.6	-12.2	-11.6	-10.8	-10.4	-8.1	-6.1
as % of GDP	-6.2	-3.6	-2.8	-4.8	-3.2	-2.8	-3.1	-3.8	-4.0	-3.7	-3.5	-3.3	-2.5	-1.9
3m eurodeposit rate (%)*	6.0	5.9	3.7	5.8	7.1	7.2	7.6	6.7	5.9	3.6	3.6	3.7	3.8	3.8
10-year bond yield (%)*	5.6	5.6	4.2	5.6	5.7	6.4	6.1	6.2	5.8	4.4	4.3	4.3	4.2	4.2
US$/A$*	0.75	0.68	0.79	0.74	0.77	0.65	0.60	0.64	0.70	0.76	0.76	0.78	0.80	0.82
Commonwealth budget (FY, A$ bil)	13.5	-14.0	-55.0											
as % of GDP	1.1	-1.1	-4.3											
Unemployment rate	4.3	5.8	8.0	4.3	4.2	4.6	5.1	5.5	6.0	6.4	7.0	7.7	8.3	8.9
Industrial production	3.0	-2.0	3.5	2.6	-4.0	-3.0	-4.0	-2.0	1.0	3.0	6.0	4.0	2.0	0.0

*All financial variables are period averages

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

				2008			2009				2010			
	2008	2009	2010	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real GDP (1995-96 prices)	0.4	0.2	2.4	-0.8	-1.5	-1.8	-0.9	-0.1	5.5	5.5	1.3	0.4	1.9	1.9
Private consumption	0.1	0.1	1.8	-0.8	-0.6	-0.8	0.3	0.2	1.1	2.9	2.2	1.6	1.2	1.3
Fixed Investment	-2.8	-4.9	6.5	7.1	-29.7	-9.3	-1.6	1.4	4.8	6.8	6.3	8.3	8.1	6.0
Residential construction	-16.4	-14.0	6.5	-28.9	-27.6	-32.0	-9.2	0.2	7.0	6.0	8.0	7.9	5.0	6.0
Other fixed investment	0.6	-3.1	6.5	17.1	-30	-4.0	-0.1	1.6	4.4	7.0	6.0	8.4	8.7	6.0
Inventory change (NZ$ bil, saar)	1.7	2.2	2.4	0.3	0.6	0.4	0.4	0.5	0.6	0.7	0.8	0.6	0.5	0.6
Government spending	4.1	6.5	-0.7	0.7	4.2	8.1	10.7	2.5	8.4	3.5	-4.8	-6.9	-0.1	2.1
Exports of goods & services	-1.0	-3.0	3.2	-1.0	-12.0	-5.0	-2.4	-1.5	2.1	2.9	5.5	3.5	2.4	2.1
Imports of goods & services	3.4	-4.2	1.9	16.0	-27.1	-8.0	0.5	0.6	0.6	0.9	2.1	2.7	2.9	3.4
Contributions to GDP growth:														
Domestic final sales	1.4	-0.8	2.0	6.2	-12.1	-1.2	0.0	-0.6	4.5	3.1	-0.5	2.4	3.4	1.9
Inventories	0.6	0.3	0.2	-0.6	2.9	-2.1	0.0	1.2	0.6	1.8	0.9	-2.1	-1.2	0.6
Net trade	-1.6	0.7	0.3	-6.1	8.6	1.5	-0.9	-0.7	0.4	0.5	0.9	0.1	-0.3	-0.6
GDP deflator (%oya)	2.7	1.4	3.0	3.7	1.6	-0.3	-0.6	0.8	2.7	2.7	2.8	3.0	3.1	3.1
Consumer prices	4.3	0.8	1.4	6.7	6.2	4.0	2.0	0.8	0.4	0.0	1.6	2.0	3.2	2.8
%oya	4.3	2.6	1.4	4.0	5.1	4.9	4.7	3.2	1.8	0.8	0.7	1.0	1.7	2.4
Trade balance (NZ$ bil, sa)	-3.8	-7.2	-5.8	-1.1	-0.9	-1.6	-1.7	-1.7	-1.9	-1.9	-1.6	-1.4	-1.3	-1.4
Current account (NZ$ bil, sa)	-17.9	-18.0	-20.8	-4.7	-4.1	-5.6	-2.1	-3.9	-6.6	-5.4	-5.6	-5.4	-4.8	-4.9
as % of GDP	-10.1	-14.1	-10.9	-10.4	-9.3	-12.8	-15.2	-15.1	-14.5	-11.7	-12.1	-11.5	-10.1	-10.1
Yield on 90-day bank bill (%)*	8.5	7.8	5.5	8.8	8.2	8.2	8.0	8.6	8.0	6.6	6.1	5.5	5.3	5.2
10-year bond yield (%)*	6.2	6.0	5.1	6.5	5.9	6.2	6.0	6.4	6.4	5.3	5.2	5.1	5.0	5.2
US$/NZ$*	0.71	0.56		0.78	0.71	0.57	0.51	0.55	0.57	0.61	0.63	0.65	0.67	0.68
Commonwealth budget (NZ$ bil)	-1.8	-7.2	-8.6											
as % of GDP	-1.0	-4.0	-4.5											
Unemployment rate	4.0	5.6	6.4	3.9	4.2	4.4	4.8	5.2	5.8	6.7	6.8	6.4	6.2	6.0

*All financial variables are period averages

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Australia and New Zealand economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
12 Jan Australia : ANZ job ads (11:30 am) Dec	13 Jan New Zealand : NZIER business opinion survey (10:00 am) 4Q	14 Jan Australia Housing finance (11:30am) Nov 1.5 %m/m, sa New Zealand: : Building permits (10:45 am) Nov	15 Jan Australia : Unemployment rate (11:30 am) Dec 4.5 %, sa	16 Jan New Zealand : QV house prices Dec
19 Jan	20 Jan New Zealand : CPI (10:45 am) 4Q	21 Jan Australia : Westpac consumer confidence (10:30 am) Jan New Zealand : Retail sales (10:45 am) Nov	22 Jan Australia : New motor vehicle sales (11:30 am) Dec New Zealand : PMI (10:30am) Dec	23 Jan Australia : Export price index (11:30 am) 4Q Import price index (11:30 am) 4Q
6 Jan New Zealand : Credit card spending (03:00 pm) Dec *Holiday Australia*	27 Jan Australia: NAB bus. confidence (11:30 am) Dec PPI (11:30 am) 4Q	28 Jan Australia : Westpac leading index (10:30 am) Nov CPI (11:30 am) 4Q	29 Jan New Zealand : RBNZ official cash rate (9:00 am) Feb Trade balance (10:45 am) Dec	30 Jan Australia : Pvt. sector credit (11:30 am) Dec Dec New Zealand : Building permits (10:45 am) Dec
Feb Australia : House price index (11:30 am) 4Q	3 Feb Australia : RBA cash target (2:30 pm) Feb Trade balance (11:30 am) Dec	4 Feb Australia : Retail sales (11:30 am) Dec Building approvals (11:30 am) Dec New Zealand: Visitor arrivals (10:45am) Dec ANZ commodity price (03:00pm) Jan	5 Feb New Zealand : Unemployment rate (10:45 am) 4Q	6 Feb *Holiday New Zealand*

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

Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
12 - 16 January	**12 January**	**13 January**	**14 January**	**15 January**	**16 January**
China • Money supply (Dec) • Trade balance (Dec) Japan • Cabinet Office private consumption (Nov)	Canada • BoC business outlook survey (4Q) • BoC loan officer survey (4Q)	Argentina • CPI (Dec) Canada • International trade (Nov) Euro area • Trichet speech Japan • Economy watcher survey (Dec) Sweden • CPI (Dec) United States • International trade (Nov) • Bernanke speech	Euro area • IP (Nov) France • CPI (Dec) Poland • CPI (Dec) Thailand • BoT meeting United States • Beige book • Business inv (Nov) • Import prices (Dec) • Retail sales (Dec)	Euro area • HICP final (Dec) • ECB meeting Japan • Machinery orders (Nov) Turkey • CBRT meeting United States • NY Fed survey (Jan) • Philly Fed survey (Jan) • PPI (Dec)	Euro area • International trade (Nov) Japan • Shirakawa speech Mexico • IP (Nov) • Banxico meeting United States • Consumer sent (Jan) • CPI (Dec) • IP (Dec)
19 - 23 January	**19 January**	**20 January**	**21 January**	**22 January**	**23 January**
China • CPI (Dec) • FAI (Dec) • GDP (4Q) • IP (Dec) • Retail sales (Dec) Japan • Department store sales (Dec)	Hungary • NBH meeting Japan • IP final (Nov)	Canada • BoC meeting Germany • ZEW business surv (Jan) Japan • Consumer sent (Dec) • Tertiary sector activity index (Nov) United Kingdom • CPI (Dec)	Malaysia • BNM meeting United Kingdom • Labor mkt report (Dec) • MPC minutes United States • NAHB survey (Jan)	Euro area • Industrial orders (Nov) Japan • BoJ bank loan officers survey (4Q) • International trade (Dec) • Reuters Tankan (Jan) • BoJ meeting United States • FHFA HPI (Nov) • Housing starts (Dec)	Belgium • BNB business surv (Jan) Canada • CPI (Dec) Euro area • PMI flash (Jan) France • INSEE business surv (Jan) Japan • All sector activity index (Nov) Korea • GDP prelim (4Q) Taiwan • Export orders (Dec) • IP (Dec) United Kingdom • GDP prelim (4Q) • Retail sales (Dec)

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