Australia and New Zealand - Weekly Prospects

Summary

- There were two main surprises in the data released in **Australia** last week. First, the consumer confidence index showed an alarming slump in February, even though the survey was conducted after the RBA's decision to cut the cash rate 100bp and the government's huge fiscal stimulus announcement. Second, employment rose in January, albeit mildly—the forecast was for a large decline. The 0.3% point rise in the unemployment rate, though, was in line with our expectation. This week, RBA communications are the main focus. The minutes from the RBA's February Board meeting are released Tuesday, and probably will explain in detail the reasons behind the decision to cut the cash rate so aggressively - the profound weakness offshore will be the main focus. Also, the RBA Governor testifies to Parliament on Friday - this should be the highlight of the week.

- In **New Zealand**, retail sales values slumped in December, driven by a fall in automotive fuel retailing. Consumers have become increasingly reluctant to spend amid widespread recession fears, still-elevated market interest rates, falling asset prices, and heightened anxiety about job security. Retail sales volumes fell more than expected, with the weaker than expected result prompting a further downgrade to our 4Q GDP growth forecast from -0.5%q/q to a deeper contraction of 0.7%; this will mark four straight quarters of falling GDP. We expect household spending will fall 0.5% this year, with only the forthcoming tax cuts in April and lower interest rates preventing an even larger decline than currently forecast.

- In tracking the path of the **global credit crisis** since August 2007, it is important to distinguish between bank and nonbank activity. A concentration of the credit tightening over the first year of the credit crisis resulted from the seizing up of securitized sources of funding that had grown dramatically over the previous two decades. Banks, for their part, tightened credit standards, but continued to increase lending. As a result, banks served as an important stabilizer over the first year of the crisis, moderating the drag on overall activity. The role of banks in the crisis is now changing. The onset of a severe recession is weakening bank balance sheets and prompting a further tightening in credit conditions. In addition, it has become unusually difficult for banks to raise private capital, increasing institutional caution. As a result, bank lending has flattened, a pattern seen regularly following the onset of past economic downturns.

- **Global consumer spending** appears to have increased in January, building on a tentative firming that took hold into year end. Spending was supported by the purchasing power lift from lower energy and food prices, which offset the drags from falling net worth and decelerating labour income. The back to back gains in global vehicle sales in December and January are the most broad-based sign of improvement. These gains followed a 20% decline over the previous five months. To this, add the strong advance in January US retail sales and the apparently solid gains in the UK and China. All told, we estimate that our index of global retail sales rose 0.5%m/m in January, its second increase in the past three months.

This week's highlight

RBA Governor Glenn Stevens will deliver his six-monthly testimony to Federal Parliament's House of Representatives Standing Committee on Economics on Friday.

Contents

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Data and event previews - Australia and New Zealand

Date [a]	Data/event	Forecast			Comment
		JPMorgan	Consensus	***Previous***	**Comment**
Monday, February 16 (3:30pm)	**Speech by RBA's Chris Ryan**	**na**	na	*na*	Chris Ryan, Head of International Department at the RBA, will deliver a speech on Recent Conditions in the Australian Foreign Exchange Market.
Tuesday, February 17 (11:30am)	**RBA Board minutes (Feb.)**	**na**	na	*na*	The minutes from the RBA's February Board meeting will explain in detail the reasons behind the decision to cut the cash rate by another 100bp earlier this month. The minutes probably will indicate that the RBA remains focused primarily on conditions in the global economy, which have deteriorated substantially.
Wednesday, February 18 (9:20am)	**Speech by RBA Assistant Gov. (Economic) Malcolm Edey**	**na**	na	*na*	The RBA's Malcolm Edey, Assistant Governor (Economic), will deliver a speech to the CEDA Economic and Political Overview 2009 in Sydney.
Wednesday, February 18 (10:30am)	**Westpac leading index (%m/m, Dec.)**	**na**	na	*-1.0*	The leading index has been indicating that growth in the economy has slowed abruptly. This month's index is likely to follow the same path.
Wednesday, February 18 (11:30am)	**Aust. retail sales ex. inflation (%q/q, 4Q)**	**1.1**	1.0	*0.1*	Retail sales volumes should surge 1.1%q/q in 4Q08, marking the largest rise in 2008. The increase in sales volumes will be owing to significant discounting among retailers, alongside significant cuts to the cash rate, falling petrol prices and the one off bonus payments delivered in December to low- and middle-income earners.
Thursday, February 19 (11:30am)	**Aust. new motor vehicle sales (%m/m, Jan.)**	**-2.5**	na	*1.8*	Vehicle sales bounced in December, but probably will have fallen back in January. The euphoria associated with December's fiscal boost probably will have faded.
Friday, February 20 (9:00am)	**RBA Gov. Stevens' semi-annual Parliamentary testimony**	**na**	na	*na*	RBA Governor Stevens will deliver his six-monthly testimony to Federal Parliament's House of Representatives Standing Committee on Economics. The Governor will deliver a prepared statement that probably will echo the balanced tone of the February policy announcement and take questions from Members of Parliament. The hearing will last for about three hours.

(a) Australian Eastern Standard Time.

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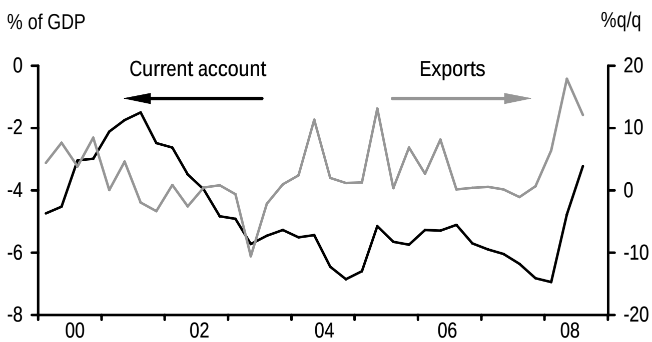
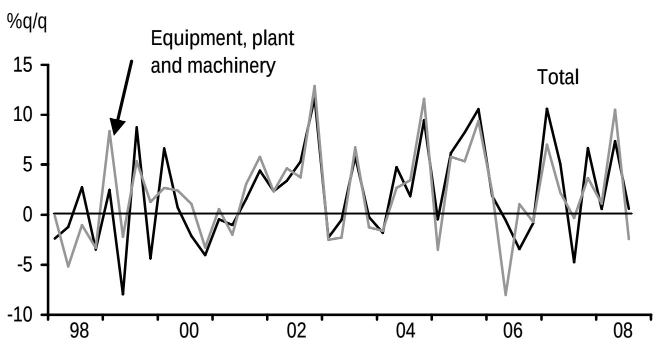
Feature charts

Australia: current account balance and exports



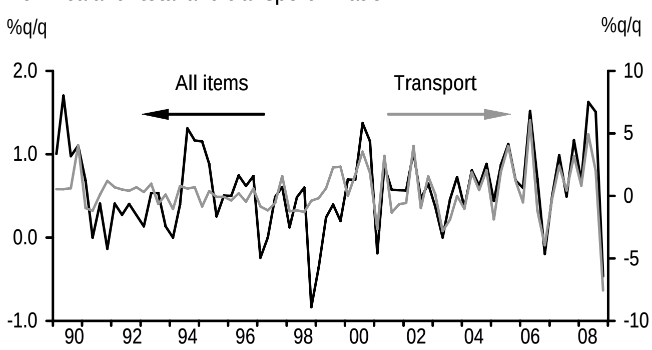
Australian exports, particularly commodities, improved markedly in the current account data over 2008, mainly thanks to higher prices, rather than volumes. This year, however, falling commodity prices and lagging demand from Australia's major trading partners will likely see a reversal of such fortunes. Deteriorating conditions offshore were the major factor driving our recent growth downgrade for the Australian economy.

Australia: private capital expenditure



The recent business sentiment and consumer confidence data have shown a significant downturn. This will lead to further drops in investment as firms scale back all aspects of operations in a bid to cut costs. Business investment will probably fall 7.4% this year, after a rise of 11.4% in 2008. The associated cuts to new capital projects, and to output from the producers of plant and machinery themselves, represent another section of the labour market that will be hit hard in 2009.

New Zealand: total and transport inflation



Inflation pressures have eased in New Zealand, predominantly due to the precipitous fall in petrol prices (reflected here in transport costs). The relief from supply-side concerns, and poor retail trade figues, increase the likelihood of further assertive rate cuts from the RBNZ. Following the massive 150bp cut in January, we forecast a further 125bp reduction during this easing cycle, yielding a terminal rate of 2.25%.

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Research note

Recession fears drive increase in Aussie household saving

- **Australia's household saving rising as economy falls into recession**
- **Massive wealth destruction in household sector has sparked more precautionary saving**
- **Reduction in credit availability will force many to save to purchase big-ticket items**

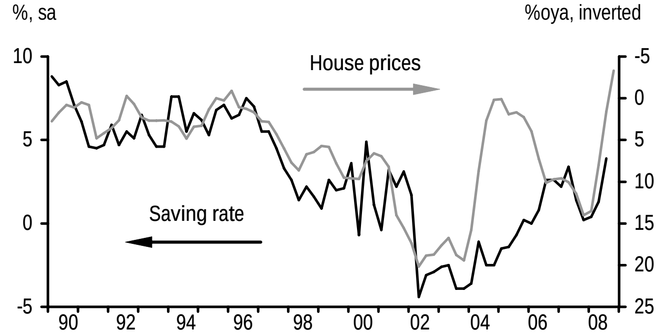
Australia is in the midst of its first recession since the early 1990s. The recession started in 4Q08 and probably will intensify in 1Q09. The collapse in consumer confidence resulting from widespread fears over job losses and growing uncertainty surrounding the outlook for the global economy is driving a rise in household saving. The household saving rate already has started to increase after two decades of decline, rising from nearly zero at the end of 2007 to 3.9% in 3Q08, the highest level since 2000, but a stark contrast to the 10% levels observed in the 1980s. We expect the household savings rate to rise rapidly this year, possibly beyond earlier peaks.

Rising joblessness pushing up savings

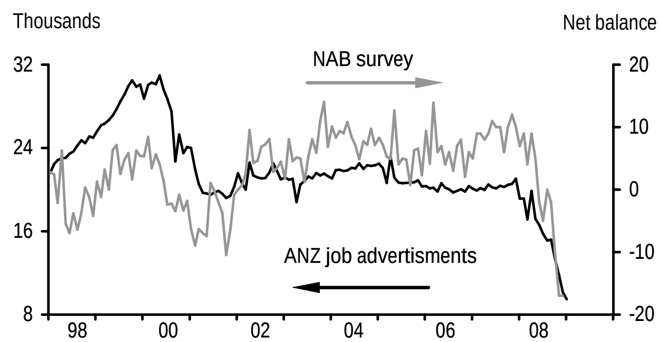
Lower asset prices, rising unemployment, and reduced credit availability are pushing the saving rate higher.

- **Falling asset prices.** Household wealth has declined over the past year as asset prices tumbled. House prices, for example, were down 3.3% in 2008 (the first fall since 1996) and the equity market shed over 40%. The massive wealth destruction (that is still occurring) in the highly leveraged household sector prodded fearful consumers into more conservative spending behavior.
- **Rising unemployment.** Increased anxiety about job security is also pushing up the household saving rate. Business confidence has fallen to a record low, and firms have started to reassess their capital spending plans and trim their work forces amid challenging economic conditions. Employment growth eased to just 0.9%oya in January, the slowest rate since early 2004. The jobless rate shot up to 4.8% from 4.5%, nearly a full percentage point higher than the 33-year low of 3.9% recorded in February 2008. At the same time, more people entered (or stayed in) the workforce to try and make financial ends meet, with the labour force participation rate rising another notch to 65.1% in January from 65.0%.

Household saving rate and house prices



Leading indicators of employment have collapsed



The fear of becoming unemployed is growing as the labor market continues to deteriorate. The Melbourne Institute found that the number of households citing the main reason to save for the proverbial rainy day as "becoming sick or being unemployed" rose to 48.1% in 4Q, up 8%-points from 3Q; this figure will rise further given the deep labor market adjustment we forecast. Based on our estimates, employment will fall 1% in this recession and the jobless rate will rise to 9% by the end of 2010, just shy of the double-digit rates recorded in previous recessions.

- **Reduction in credit availability.** The extended decline in the saving rate in recent decades can be explained, to a large extent, by the steady rise in credit made available to households following financial market deregulation in the 1980s.

  The extent to which households smooth their spending over time depends on their ability to borrow and save. The reduction in credit availability underway as banks trim their balance sheets, and the related tightening of credit standards owing to rising loan losses, should lead to a rise in the level of saving, as households seek alternative means to smooth consumption.

Changing attitudes toward money

Households' attitudes toward saving, spending, and taking on new debt already have changed as a result of new-found conservatism. The significant rise in the household saving rate in the first nine months of 2008 was accompanied by a 23% spike in bank deposits. More recently, demand for debt has slumped, with private sector credit outstanding falling 0.3% in December, the first monthly fall since 1992.

Rising conservatism has meant that the Government's attempt to get consumers spending with the A$10.4 billion stimulus package implemented in December failed to have the desired effect (i.e. not immediately reflected in increased consumption). The majority of low- and middle-income households that received the one-off payments paid off debt or boosted savings. The latest Fujitsu mortgage stress survey found that 18% repaid debt and 43% saved the extra cash. Also, the Australian National Retailers Association reported that nearly 75% of mortgage holders have been paying off their mortgages faster, rather than reducing monthly repayments. The remaining quarter cut repayments, although half of them said they were using the money to pay off other debts. With economic anxiety even higher now, a larger share of the new A$12.7 billion in one-off cash payments, passed by Parliament this week, to be delivered in March will be saved.

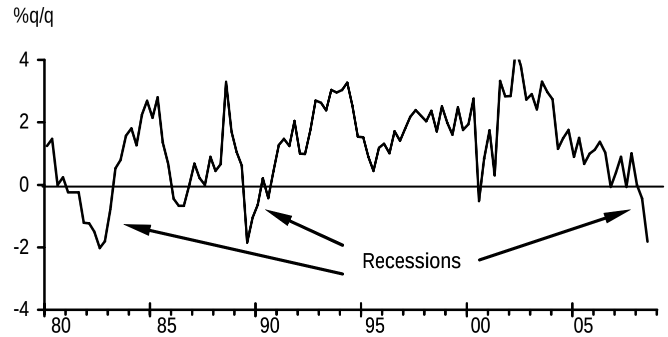
This change in behaviour means that a long period of deleveraging lies ahead for the highly indebted household sector—the debt to income ratio of just under 160% is among the highest in the developed world, up from "just" 84% a decade ago. The extent of this deleveraging will be a key determinant of the depth and duration of this recession. We expect household consumption, which accounts for 55% of the economy, to contract 0.4% in 2009. Our working assumption is that households will reduce debt in an orderly fashion. More severe deleveraging and a sharper rise in the savings rate, however, would trigger an even sharper correction.

Interest rates and the falling terms of trade

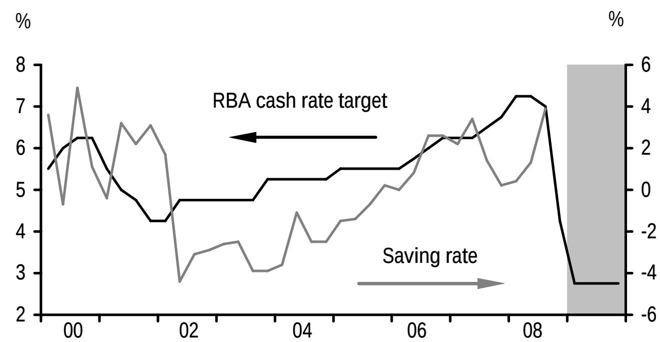
The contraction under way in major industrial economies is reversing Australia's previously booming terms of trade. This fall in the terms of trade should cap the rise in the household saving rate. We expect that export volumes will fall and commodity prices for iron ore and coal, Australia's two largest export commodities, will be significantly lower in 2009. This will remove a key source of stimulus to national income.

Rapid income growth driven by the soaring terms of trade, up 70% since the early 1990s, was one of the factors that helped pull the household saving ratio out of negative territory in

Household debt to disposable income ratio



Lower interest rates to curb rise in saving rate



2005. The government used rising company tax receipts to fund generous personal tax relief, fuelling an extended consumer spending splurge. However, the rise in spending did not keep up with the surge in incomes, resulting in an increase in the share of income saved. It follows that the weakening terms of trade will work in reverse and thereby cap the upside for household saving.

The fall in real returns on savings also will limit the rise in the household saving rate. The RBA has delivered a mammoth 400bp of policy easing since September, the most aggressive series of official rate cuts since the 1990-91 recession. The Federal government's decision to guarantee bank deposits means many consumers have shifted out of risker investments to have the peace of mind of Government backing, but low returns means the incentive to save has been reduced.

Further policy easing, in our view, will be limited, however. The 2.75% official cash rate we expect following the RBA's March Board meeting is our forecast for the trough in the current easing cycle. That said, further deterioration of economic conditions offshore, particularly in the nation's major trading partners, and the significant rise we forecast in the jobless rate point to downside risk to our terminal cash rate forecast.

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Australia

- **Aussie jobless rate jumped to 4.8% in January**
- **Consumer confidence fell despite policy stimulus**
- **RBA communications in focus this week**

There were two surprises in the economic data released in Australia last week. First, the consumer confidence numbers showed a decline in February, even though the survey was conducted last week following the RBA's decision to cut the official cash rate another 100bp and the government's announcement of a huge stimulus package. Second, employment rose in January, albeit mildly—the forecast was for a large decline.

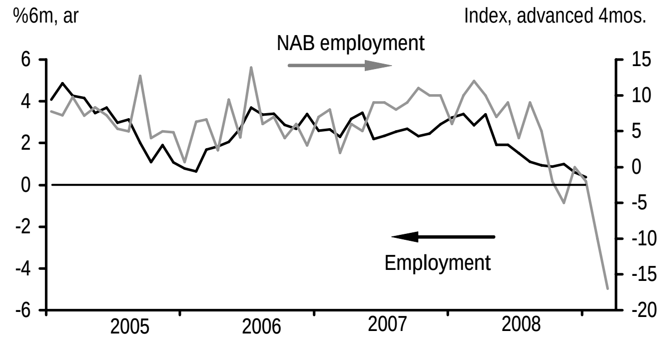
RBA communications in focus

The minutes from the RBA's February Board meeting will be released Tuesday, and will explain in detail the reasons behind the decision to cut the cash rate by another 100bp earlier this month. The minutes probably will indicate that the RBA remains focused primarily on conditions in the global economy, which have deteriorated substantially. The minutes will confirm that RBA officials cut the cash rate aggressively for the fourth month in five (there was no scheduled Board meeting in January) because of growing concerns that the world economy was at greater risk of slipping into recession. That said, the minutes probably will reiterate that economic conditions in Australia have been affected less than in other advanced economies.

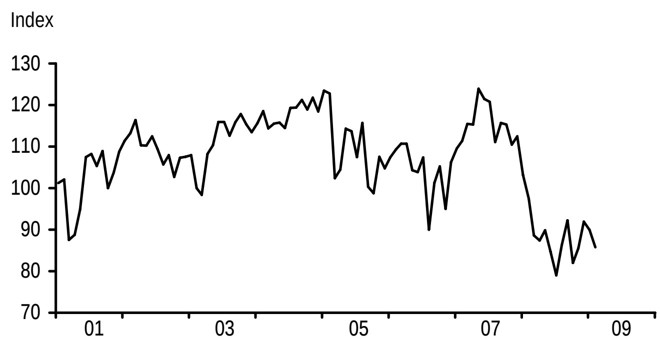
It will be interesting to see the extent to which the announcement of the government's fiscal stimulus package played a role in the policy decision. In the statement accompanying the decision to slash the cash rate two weeks ago, the RBA said that the decision took account of the loosening in fiscal policy the had occured earlier that day. The Government's fiscal package passed through the upper house of Parliament on Friday. Only after the provision of an additional A$900 million for water provision in the parched Murray Darling Basin was the package passed.

Also, Glenn Stevens, the RBA Governor, will deliver his six-monthly testimony to Federal Parliament's House of Representatives Standing Committee on Economics in Canberra on Friday. The Governor will deliver a prepared statement that probably will echo the balanced tone of the minutes from the January Board meeting. He also will take questions from Members of Parliament. This week also sees a speech by Malcolm Edey, the RBA's Assistant Governor (Economic).

Australia: NAB survey and employment growth



Australia: Westpac-Melbourne Consumer Sentiment Index



Real retail sales probably surged in 4Q

Retail sales volumes should surge 1.1%q/q in 4Q08, following a mild 0.1% rise in 3Q, marking the largest rise last year. The increase in sales volumes will be owing to significant discounting among retailers, alongside significant cuts to the cash rate, falling petrol prices and, in the final weeks of the year, the one-off bonus payments delivered to low- and middle-income earners on December 8.

Real consumer spending will be weak in 2009, however. Households are facing considerable headwinds given the massive wealth destruction that has occurred in the highly leveraged household sector. The largest drag on consumption, however, probably will be the deterioration in labor market conditions and rising unemployment.

Unemployment rate highest since 2006

Australia's labour force report showed an unexpected rise in employment of 1,200 in January (J.P.Morgan -25,000, consensus -18,000), following no change in December. Employment growth slowed to 0.9%oya, the slowest rate since early 2004, and down sharply from the 3.0% growth rate recorded last

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February. Reversing last month's changes, the number of part-time jobs fell 32,600, and a striking 33,700 full time jobs were added. It's very hard to believe in the current economic climate that so many full-time jobs were added. Indeed, industry anecdotes indicate that many firms shed full-time workers last month.

The jobless rate provides the best reading on underlying labor market trends, rather than the full-time/part-time employment breakdown, which remains extremely volatile. The jobless rate shot up to 4.8% in January from 4.5% (J.P.Morgan 4.8%, consensus 4.5%), nearly a full percentage point higher than the 33-year low of 3.9% recorded in February 2008, and the highest rate since June 2006.

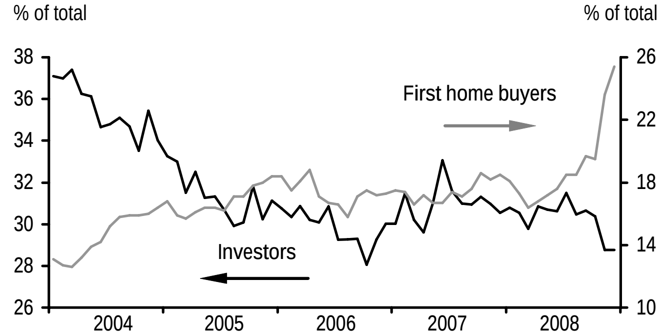
The jobless rate ventured higher even though employment rose because labour force participation increased, indicating that more people are entering (or staying in) the work force to try and make financial ends meet. The labour force participation rate increased another notch to 65.1% from 65.0% in December. In this recession (we expect contractions in GDP growth in 4Q08 and 1Q09 and growth of -0.5% in CY09), we suspect that labour force participation will be slower to decline, which will inflate the jobless rate. This is mainly because of elevated skilled migration flows and older workers staying in the work force longer than they had planned to compensate for the fact that their retirement nest-egg has dwindled.

In our forecasts, the jobless rate will soar to 9% by the end of 2010—a more benign outcome than during the last two recessions in the early 1980s and early 1990s, when the jobless rate ventured into double digit territory. This call is supported by the avalanche of anecdotal job losses announced recently and leading indicators of employment, such as the ANZ job advertisement series, which have collapsed. We forecast that labour market conditions will deteriorate significantly, resulting in employment falling 1% during the current recession.

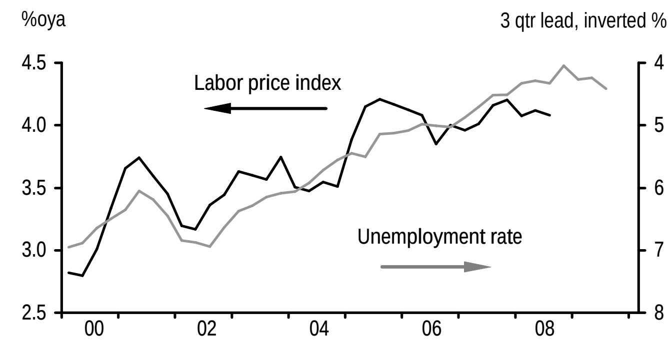
Consumer confidence fell unexpectedly

The Westpac-Melbourne Institute consumer confidence index slumped 4.6%m/m in February, after a 2.2% fall in January. The decline was unexpected, as the survey was conducted after another significant cut to the official cash rate and the government's announcement of another round of cash handouts for workers, parents, farmers, carers and students. The number of pessimists continued to outweigh the number of optimists, with the index falling to 85.8 in February from 89.9, re-

Australia: housing finance



Australia: labor price index and unemployment



maining below the neutral level of 100 for the twelfth straight month.

In the absence of the significant monetary and fiscal policy stimulus recently announced, consumer confidence would have spiralled further south in February. The Australian government last Tuesday announced another significant fiscal stimulus package which included a big rise in spending on infrastructure and more cash payments to low and middle income earners. On the same day, the RBA slashed the cash rate another 100bp to 3.25%, taking the cumulative rate cuts since September to 400bp, the most aggressive easing since the 1990-91 recession.

Business conditions at recession levels

Business confidence also is at extremely low levels. The NAB business survey showed that business confidence hit a fresh record low (-32) in January. Most of the 400 companies, though, responded to the survey before the fiscal stimulus package and the RBA rate cut were announced early last week. The largest falls in sentiment were recorded in profitability, exports, and forward orders. NAB's quarterly survey

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showed that business confidence dropped 24 points to -31, the lowest reading since the series began in 1989, just ahead of the early 1990s recession.

First home buyers dominating market

The number of home loans issued in December surged 6.4%m/m (J.P.Morgan 4.5%, consensus 3.5%), after rising 1.3% in November, owing to the significant RBA policy easing, the resulting drop in mortgage rates, and a rise in first home buyer demand.

The main driver of the rise in housing finance was in the number of loans issued for the purchase of new dwellings. We suspect that this stemmed from the tripling of the first home buyers grant in October to A$21,000 for those purchasing newly constructed homes. Aside from the boost to the first home buyers grant, the prospect of further interest rate cuts, coupled with falling house prices, would also have been attractive to first home buyers, who accounted for 25% of loans in December, the highest level since 2001. Expectations of further rate cuts dampened demand for fixed interest rate loans. Fixed rate loans accounted for just 1.9% of all loans issued in December, down from 2.5% in November and a stark contrast to the 24% at the start of 2008 (when the RBA was still hiking interest rates).

With the RBA nearing the end of this current easing cycle (our forecast calls for another 50bp cut to the cash rate in March to 2.75%, which we think will be the terminal cash rate in this cycle), the fall in confidence resulting from deteriorating economic conditions will curb demand for home loans. The massive wealth destruction under way in the highly leveraged household sector (the debt to income ratio is 156%), a reduction in credit availability, and rising unemployment are already weighing on confidence.

Data releases and forecasts

Week of February 16 - 20

Wed Feb 18 10:30am	**WMI leading index** Seasonally adjusted	Sep	Oct	Nov	Dec
	(%m/m)	-1.6	-0.2	-1.0	__
Wed Feb 18 11:30am	**Retail trade, quarterly** Seasonally adjusted	1Q08	2Q08	3Q08	4Q08
	(%q/q)	-0.1	-0.2	0.1	1.1
	(%oya)	4.0	2.3	0.8	0.9
Thu Feb 19 11:30am	**Sales of new motor vehicles** Units, seasonally adjusted	Oct	Nov	Dec	Jan
	(%m/m)	-0.3	-5.2	1.8	__
	(%oya)	-10.4	-17.7	-15.7	__

Review of past week's data

ANZ job advertisements
Seasonally adjusted

	Nov		Dec		Jan	
(%m/m)	-8.6		-9.7		__	*-6.3*

NAB monthly business survey
% balance, seasonally adjusted

	Nov		Dec		Jan	
Business confidence	-30		-20		~~-14~~	*-32*

WMI consumer sentiment index
100=neutral, seasonally adjusted

	Dec		Jan		Feb	
(%m/m)	7.6		-2.3		~~12.0~~	*-4.6*

Housing finance approvals: owner occupiers
Number of loans, seasonally adjusted

	Oct		Nov		Dec	
(%m/m)	~~1.4~~	*1.9*	~~1.3~~	*1.8*	~~4.5~~	*6.4*
(%oya)	~~-24.1~~	*-23.5*	~~-24.9~~	*-23.9*	~~-21.0~~	*-18.6*

Labor force
Seasonally adjusted

	Nov		Dec		Jan	
Unemployment rate (%)	~~4.4~~	*4.5*	4.5		*4.8*	
Employed (000 m/m)	~~-16~~	*-17*	~~-1~~	*0*	~~-25~~	*1*
Participation rate (%)	65.1		65.0		~~65.0~~	*65.1*

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New Zealand

- **Retail sales slumped in December**
- **RBNZ to cut rates further**
- **GDP growth forecast downgraded again**

In New Zealand, data last week showed that retail sales values slumped in December, driven by a fall in automotive fuel retailing. The sharper than expected fall in quarterly retail sales volumes prompted another downgrade to our 4Q GDP growth forecast.

NZ retail sales slumped in December

Retail sales values fell more than expected in December, declining 1.0%m/m (J.P.Morgan -0.2%, consensus -0.7%), after rising a revised 0.2% in November (previously zero). Rising unemployment and recession fears spooked consumer spending, even though confidence probably got some lift from lower interest rates, a small rise in equity prices, and falling petrol prices.

The decline in retail sales in the month of December was driven by a fall in automotive fuel retailing (-8.4%m/m), owing to lower gasoline prices. The next largest decrease was for sales at supermarkets and grocery stores (-1.1%). The retail sales trend continued to decline (-0.2%), as it has done since January last year, marking the most prolonged period of decline on record.

Another downgrade to NZ GDP forecast

Retail sales volumes in 4Q were down 0.6%q/q, much worse than the 0.2% decline we had forecast. The biggest contributor to the fall in sales volumes was motor vehicle retailing (-4.9%q/q). The weaker than expected result prompted a further downgrade to our 4Q GDP growth forecast from -0.5%q/q to a deeper contraction of 0.7%; this will mark four straight quarters of falling GDP.

Consumers have become increasingly reluctant to spend amid widespread recession fears, still-elevated market interest rates, falling asset prices, and heightened anxiety about job security. We expected household spending will fall 0.5% this year, with only the forthcoming tax cuts in April and lower interest rates preventing an even larger decline than currently forecast. We forecast that the RBNZ will cut the OCR another 75bp in March to 2.75%, and a terminal cash rate of 2.25% to be reached by April.

Review of past week's data

QVNZ house prices
%, median

	Nov	Dec	Jan
(%oya)	-6.8	-7.4	__ *-8.3*

Business PMI
Seasonally adjusted

	Nov	Dec	Jan
Index	~~35.4~~ *35.2*	42.5	__ *42.0*
(%oya)	~~-37.1~~ *-37.9*	~~-20.4~~ *-20.1*	__ *-20.4*

Retail trade
Seasonally adjusted

	Oct	Nov	Dec
(%m/m)	~~-1.3~~ *-1.2*	~~0.0~~ *0.2*	~~-0.2~~ *-1.0*
(%oya)	-0.2	~~-1.7~~ *-1.6*	~~-2.0~~ *-2.7*

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Global Essay

- **Fed steps up efforts to revive nonbank lending**
- **Other central banks prepare to join Fed in quantitative easing**
- **Euro area GDP swoons, led by Germany**
- **Surge in bank lending is latest sign of economic upswing in China**

Good bank, bad bank

In tracking the path of the global credit crisis since August 2007, it is important to distinguish between bank and nonbank activity. A concentration of the credit tightening over the first year of the credit crisis resulted from the seizing up of securitized sources of funding that had grown dramatically over the previous two decades. Banks, for their part, tightened credit standards, but continued to increase lending—largely as existing lines of credit were drawn and banks were able to count on the Fed and the FHLB for reliable low-cost funds. As a result, banks served as an important stabilizer over the first year of the crisis, moderating the drag on overall activity. The role of banks in the crisis is now changing. The onset of a severe recession is weakening bank balance sheets and prompting a further tightening in credit conditions. In addition, it has become unusually difficult for banks to raise private capital, increasing institutional caution. As a result, bank lending has flattened, a pattern seen regularly following the onset of past economic downturns.

It is against this backdrop that last week's policy announcements should be assessed. Treasury Secretary Geithner's financial plan was received with justifiable disappointment, as it lacked details on how he will stress test banks and move forward with his "bad bank"—the Public-Private Investment Fund. Without losing sight of the importance of this initiative, it is unlikely that bank lending will accelerate anytime soon. Of greater near-term importance is the direction the Federal Reserve is taking. Last week, the Fed announced a significant expansion of its "good bank" facilities to support new nonbank lending. It is already engaged in the commercial paper market and is purchasing GSE debt and agency MBS. This week it announced that its TALF program could expand to $1 trillion as it injects liquidity directly into a wide range of securitized lending markets. With the banking sector adjustment likely to linger even under the best laid plans, the success of these new nonbank flows will be central to promoting economic recovery in the coming quarters.

In some areas, progress is evident. Indeed, the Fed's balance sheet has contracted by over $400 billion in recent weeks as an improvement in corporate funding markets has reduced the call on its CP and fx swap facilities. This reduction is likely to be a pause that refreshes, as the Fed's purchases of mortgage-backed securities grow and its TALF facility likely significantly adds to the monetary base in the coming months.

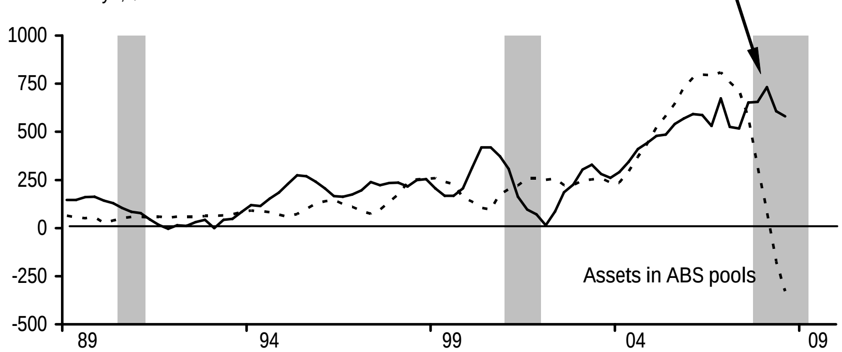
Credit easing is catching on

A number of other central banks have moved policy rates close to zero and are also considering using their balance sheets to directly support credit markets. The BoJ has purchased equities and is helping finance CP issuance. At next week's meeting there will be further discussion of a proposal for the BoJ to purchase corporate bonds.

In Europe, we now expect the BoE (March) and Riksbank (April) to take rates to 0.25% and to follow this by expanding its monetary base to purchase assets. UK purchases will likely be restricted to gilts and high-grade corporate debt at the start

US: credit extended by banks and ABS issuers

Difference oya, $bn



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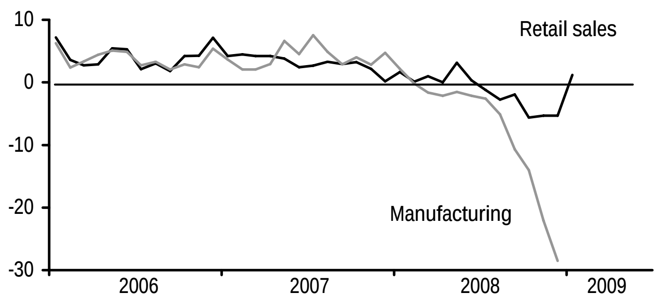
Global retail sales volume and manufacturing
%3m, saar; both scales; ret sales w/ Jan est



and geared to complement the BoE's existing Asset Purchase Facility funded by government borrowing. At this stage, the size and scope of operations of European central banks looks likely to remain modest in relation to the Federal Reserve's, which may ultimately triple its balance sheet from its level at the start of the crisis.

Consumer spending firms . . . for now

Global consumer spending appears to have increased in January, building on a tentative firming that took hold into year end. Spending was supported by the purchasing power lift from lower energy and food prices, which offset the drags from falling net worth and decelerating labor income. The back to back gains in global vehicle sales in December and January are the most broad-based sign of improvement. These gains followed a 20% decline over the previous five months. To this, add the strong advance in January US retail sales and the apparently solid gains in the UK and China. All told, we estimate that our index of global retail sales rose 0.5%m/m in January, its second increase in the past three months.

This firming in retail sales took place against the backdrop of a 3.6% average monthly decline in global manufacturing in November and December. Our global PMI points to continued deep losses in output in the current quarter. This week's January IP report from the US (-2.3%m/m) should reinforce this view. The upshot of these developments is that progress toward eliminating unwanted inventory is now being made. The adjustment is moving ahead rapidly in the US auto industry—albeit on the back of an estimated annualized decline in production tracking more than 70% this quarter. Likewise, the various PMI measures of manufacturers' finished goods inventories have fallen sharply in recent months, even as the indexes for new orders have moved up.

The question is whether this favourable dynamic will be sustained. While the drags on consumer spending remain intense, the temporary slide into deflation that bolstered household purchasing power in late 2008 and early 2009 is fading. The key will be whether expected support from healthier credit markets and monetary and fiscal policy will be strong enough in the near term to prevent a renewed bout of consumer weakness.

Germany sings the blues

As the fourth-quarter GDP reports roll in, they reinforce the message of how universal the downshift in activity was into year end. The initial report of a 3.8% contraction in US GDP is likely to be marked up to over 5%, based on subsequently released source data. We estimate that today's reports will show that Japanese GDP contracted at a 9% pace. Last week's flash report showed that the Euro area economy contracted at a 6% annualized pace in 4Q08.

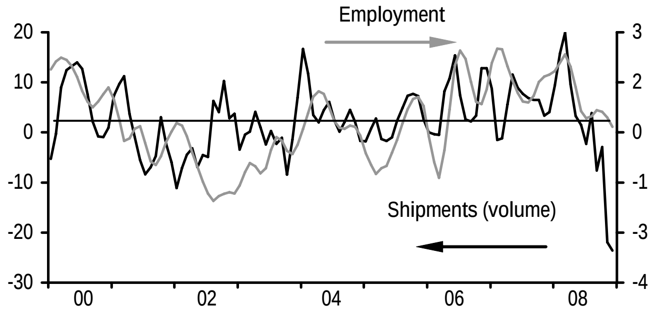
What is as striking as the size of the Euro area contraction is the relative performance within the major economies. Last summer, the consensus was that the fundamental vulnerabilities of overleverage and low saving were greater elsewhere across the Euro area (e.g., Spain) compared with Germany, and thus the region would see a tiering of macro performance, with Germany outperforming. In fact, precisely the opposite has occurred. In the fourth quarter, Germany contracted at an 8.2% annual rate, well above the pace in the Euro area as a whole and over twice that of Spain.

Some of the weakness in Germany is easy to understand. As one of the world's largest producers and exporters of durable goods, Germany was hard hit by the global impact of tighter credit availability from last autumn, which depressed both demand for durable goods and trade flows. German corporates apparently responded to these developments with an unusually quick and severe retrenchment. Domestic capital goods shipments fell at a 24% annual rate in the fourth quarter. It also may turn out that they sharply curtailed the growth of inventory.

Last week we revised down our Euro area forecast to incorporate a 5% contraction in GDP relative to 4Q08. Although the Euro area PMI stabilized in January, it was below the 4Q aver-

German domestic capital goods shipments and employment

%3m/3m, saar; both scales



age. German manufacturing orders, particularly for capital goods, were collapsing at year end. And if European corporates behave holistically, then employment is set to adjust dramatically in the coming months. Meanwhile, one of the key drivers of the downturn in the fourth quarter—the lack of credit availability for households and small businesses—will remain a major headwind, judging by the latest ECB bank lending survey.

Getting EM Asia lending flowing again: China takes the lead

Economic activity, especially in tech manufacturing, has been crashing in EM Asia. Liquidity and credit market conditions in the region have also deteriorated, though not nearly to the same extreme degree. Credit growth is softening, most notably in Singapore, Hong Kong, and also in Korea, where the BoK last week cut the base rate 50bp and said it “will do what is needed to improve liquidity conditions.” Recently even in India and Indonesia, where credit expansion had been resilient, loan growth is slowing.

Against this regional trend in lending growth, the recent revival in China is notable. Chinese authorities have focused on easing overall monetary conditions to support economic growth, and data last week showed January monetary aggregates and loan growth spiking for the second month, with new loans in January amounting to one third of total new loans created during full-year 2008. While the January new loan figure was magnified by surging short-term bill financing, a significant part of the new loans was channelled to public sector infrastructure projects under the government’s fiscal stimulus package, hinting at a further increase in public fixed-investment growth.

It will take time to see if this increase in lending translates into real activity. Key January data for China, including IP, fixed investment, and retail sales, will only be released together with the February numbers, a concession to the noise created in the data by the lunar new year holiday. While PMIs in China and Singapore stabilized, and this week’s report on Taiwan exports actually showed them moving up on the month, there were at least as many negative surprises in the January data released across EM Asia.

A busy period ahead in India

The focus in India next week will be on the interim budget (to fund the government over April-June before the newly elected government takes office and tables the full-year budget) which is scheduled to be presented to Parliament on Monday. Typically, interim budgets do not contain major policy shifts. However, given weak economic conditions, the government could break tradition and front-load expanded outlays for existing programs and cut taxes (mostly indirect) to support some of the worst hit sectors, such as exports and automobiles. The government is also likely to enhance spending on infrastructure projects and provide incentives to ease the import of capital goods.

However, given India’s unpleasant experience with large fiscal deficits and already high public debt, the space for additional stimulus appears limited. The sharp decline in December IP and a likely substantial contraction in external trade in January could prompt the RBI to resume monetary easing early. The easing cycle was put on hold in the January policy meeting after aggressive loosening in the previous quarter. In particular, we expect policy rates to be cut 100-150bp, in phases, by the scheduled April policy meeting. Elections are likely to be announced soon and further fiscal support will have to await the formation of the new government in June, leaving monetary policy virtually the only policy tool until then.

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JPMorgan View - Global Markets

Keep your eye on consumers

- **Portfolio strategy:** Policy confusion has drawn attention away from better economic data flow. We see near-term upside on riskier assets.
- **Fixed Income:** Low for long keeps us long duration.
- **Equities**: Cyclicals are beating noncyclicals despite the slide in indices; cover EM underweight.
- **Credit:** HG spreads keep coming in, whatever equities or economic data do, as HG is seen as least unattractive asset and most stable class.
- **Fx**: Currencies likely in a range; buy range accruals.
- **Alternatives**: HF's made 0.5% in January, beating a typical bond-equity portfolio by 5%; inflows into Gold ETFs remain strong; gold to up further near term.

10-yr Government bond yields

	Current	Mar 09	Jun 09	Sep 09	Dec 09
United States	2.89	2.40	2.00	1.75	1.65
Euro area	3.10	2.90	2.80	2.75	2.70
United Kingdom	3.55	3.20	3.20	3.25	3.30
Japan	1.25	1.25	1.10	1.20	1.40

Foreign exchange

	Current	Mar 09	Jun 09	Sep 09	Dec 09
EUR/USD	1.29	1.28	1.30	1.35	1.37
USD/JPY	91.9	88	85	85	90
GBP/USD	1.44	1.33	1.33	1.42	1.51

Commodities

		Quarterly Average			
	Current	09Q1	09Q2	09Q3	09Q4
WTI ($/bbl)	38	38	40	45	50
Gold ($/oz)	942	850	825	825	825
Copper($/m ton)	3378	3000	3000	3250	3400
Corn ($/Bu)	3.63	4.20	5.00	4.90	4.70

Source: J.P. Morgan, Bloomberg, Datastream

A hint at some form of stabilization is the early message we are getting from economic activity data for January, especially from orders, inventories, and retail spending. But equity markets are not paying much attention, both because previous "early shoots" came to nothing, and because new US policy initiatives were less than convincing.

Our bias is **to think more positively over the coming month about riskier assets**, as recent economic data allow us to trim marginally the risk on the doomsday scenario of a mini-depression. That is not to say data are surprising on the upside, or that a return to growth is imminent. US data are merely in line with our baseline forecast, which incorporates an end to recession by midyear. We advise **paying more attention on the interaction between the consumer and the producer in coming weeks than on the Washington theater.**

Markets had high hopes for a resolution of uncertainty on the new US administration's plan to get US credit flowing again. The complexity of the issues and the large amounts involved clearly required more time. We again like to think in positive terms here, and with patience, continuing to overweight senior bank debt. The near-term outlook on bank stocks is more uncertain though.

High-quality fixed income spread product remains investors' favorite asset class this year. We see steady inflows, both by retail and institutional buyers. This is not because investors expect to make a ton of money on this asset class. The attraction is, instead, that investors see a modest return with little downside, and one that should not be massively affected by the state of the world economy. A continued recession will widen spreads, but on top of a lower government yield. A recovery produces tighter spreads on top of higher government yields. The outright yield on HG corporates remains little changed.

Fixed income

Our **Global Government Bond Index is up 1% last week**, with gains at both the long and short end of developed market curves. Geithner's proposal did not bode well for equities, but was a positive for bonds, as it did not imply the even more massive issuance than some had feared.

We remain **long duration**, with a preference for the **short end of the curve**, where supply is less of a concern, and performance has been more consistent. The BoE last week suggested it may move towards quantitative easing, and the 2-year yield rallied 39bp to 1.3%. We now forecast that the BoE will cut rates to 0.25% at the Mar 5 meeting, and expect that rate to hold until at least the end of 2010. We also lower our target low for the ECB refi rate, from 1% to 0.5%, beginning in Dec 09.

Intra EMU spreads widened significantly as poor economic data and a report from Moody's reignited concerns on sover-

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eigns' public finances. Greek 10-year spreads to Bunds widened 39bp, undoing slightly more than half the tightening we saw over the past two weeks. We maintain our intra EMU convergence trades, however, seeing a high probability of intra EMU sovereign bailouts, should the need ever arise. We are thus still long Greek and Spain 10-year vs Bunds.

Our **shorts in Euro area inflation breakevens** were again profitable. With the report showing German and French 4Q GDP contracting at an annualized 8.4% and 4.6% rate, and capacity utilization at extreme lows, we believe risks to inflation are clearly on the downside and thus remain short Euro area breakevens.

Equities

Equity markets are down several percentage points this week, as the hoped-for full details on TARP II were not delivered. Confusion about what is causing the delay and about how the new US administration will bring about new credit flows pushed risk premia in equity markets, and in particular in financials. We advise patience and to focus on recent activity data that are raising the chances that consumer spending is stabilizing and that producers will soon have to start rebuilding their inventories.

As a result, we see **a decent chance of an upmove in equity indices in coming weeks,** and recommend overweighting sectors that should benefit from better economic activity data. This involves largely an overweight of cyclical sectors: materials, IT, discretionary and industrials. cyclicals have continued to outperform in global portfolios in recent weeks, despite the down move in overall indices.

Despite the dismal start of the year for global equities and commodities, **emerging equity markets** are flat so far this year in local terms, and only down a few percentage points in USD terms, denying their past sensitivities to these two drivers. Two weeks ago, we went underweight EM to express our worries about equities and commodities. This has not worked. Signs of stabilization in Chinese activity data and strong stimulus measures are reducing the main concern that investors had for the asset class. And flows into EM equities have improved recently. Cover the EM underweight.

Credit

Stock markets did not like the lack of detail in the TARP II announcement, but **senior bank bonds** saw no major problem, and spreads continued to tighten. We **stay overweight in both US and Europe**. Subordinated and Tier 1 debt also came in, but we prefer to underweight them as they are at risk of further downgrades and extension risk is increasing.

Credit technicals remained strong last week with strong demand, credit fund flows and decent primary issuance of $14bn in the US. We see further support to US high grade credit spreads as average monthly redemptions for 2009 are estimated at $55bn. Adding about $20bn from coupons means that bond managers have approximately $75bn to reinvest per month. Moreover, new government guaranteed bank bonds are being bought up by Agency funds rather than HG funds, leaving more capital for investment in HG Industrial bonds.

Stay long US ABS as the Term Asset-Backed Securities Loan Facility (TALF) will stimulate further investor demand, especially with the recent announcement that TALF will be increased up to $1tr. Our overweight in high quality **US ABS** student loans and autos continues to perform well and we recommend adding exposure in BBB credit card ABS with yields over 20%.

Alternatives

Commodities are down 6% last week, as both energy and base metals underperformed owing to increased inventories. The rally in **base metals** was short-lived as we had originally expected, but the market continues to react strongly to any glimmer of hope in China. We remain bearish copper in a 3-6 month horizon, but these positive price spikes are likely to remain frequent. **Gold** continues to be supported by massive ETF inflows. Demand from investors is compensating for soft demand from traditional buyers. We expect to see new highs near term testing $980-990 due to favorable technicals.

Hedge funds returns were marginally positive in January (0.5% average), but hedge funds outperformed a bond-equity portfolio with similar volatility by 5%. This modestly positive return was actually very positive news for hedge funds and should support a slowdown in redemptions in coming quarters. January redemption estimates are in line with our net outflows forecast of $200bn in 1H.

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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			
	2008	2009	2010	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	4Q08	2Q09	4Q09	4Q10
The Americas														
United States	1.3	-1.8	2.5	-0.5	-3.8	-5.5	-0.5	1.5	2.5	2.5	1.5	-0.9	0.5	0.7
Canada	0.6	-1.7	2.6	1.3	-3.5	-5.0	-2.0	2.0	2.5	3.0	1.9	0.3	1.6	2.0
Latin America	4.1	-0.6 ↓	3.0 ↓	4.2	-4.7	-3.8 ↓	-0.5	2.9 ↑	3.3 ↑	3.7	8.2	7.7	6.7	6.0
Argentina	6.2	-1.5	2.0	5.4	-5.0	-6.0	-4.0	4.0	0.0	6.0	7.8	7.0	7.5	10.2
Brazil	5.7	0.8	3.0	7.4	-6.0	-2.2	2.5	4.0	3.5	2.5	5.9	5.0	4.5	4.5
Chile	3.7	0.0	4.0	-0.2	-4.0	-3.0	0.0	4.0	6.0	4.0	8.6	5.0	3.0	3.2
Colombia	3.1	0.5	3.0	2.9	-1.0	-0.5	0.5	1.0	1.0	3.5	7.8	5.9	5.5	4.5
Ecuador	6.9	0.0	3.0	4.8	-0.5	-3.5	-3.5	2.0	2.5	3.5	9.3	6.0	5.3	4.0
Mexico	1.5	-2.3 ↓	3.0 ↓	2.6	-6.2	-6.2 ↓	-2.0	2.0 ↑	4.1 ↑	4.1	6.2	5.6	3.8	3.4
Peru	9.1	4.0	5.5	6.7	0.0	2.9	4.2	5.5	5.3	5.4	6.7	4.7	3.0	2.0
Venezuela	4.9	0.0	2.5	-1.0	4.2	-2.0	-5.0	0.0	1.0	2.5	33.4	41.1	41.5	29.6
Asia/Pacific														
Japan	-0.4	-5.7	2.2	-1.8	-9.0	-12.0	-2.5	-1.0	2.0	3.5	1.0	-0.7	-1.2	-0.3
Australia	2.2	-0.5	1.5	0.3	-0.9	-3.4	1.4	1.3	0.8	0.8	3.7	1.8	1.9	2.1
New Zealand	0.4	-0.7	1.4	-1.5	-2.0	-1.1	-0.7	1.5	1.6	0.9	3.4	0.4	-0.4	2.7
Asia ex. Japan	6.0	3.3 ↓	6.6	3.6	-4.8 ↓	1.3	6.7	8.6	9.0	6.0	4.5	1.0 ↓	1.5	2.8
China	9.0	7.2	8.5	5.5	1.5	5.1	10.0	11.7	12.6	7.0	2.5	-0.7	1.2	2.1
Hong Kong	2.9	-2.5	3.8	-2.0	-5.5	-6.5	0.5	3.0	5.0	4.0	2.3	-0.7	-0.5	1.4
India	6.2	5.5	7.7	8.7	0.3	0.1	4.8	8.9	10.9	9.1	9.1	3.2	1.3	4.1
Indonesia	6.0	4.2	5.0	6.4	3.0	3.0	4.0	5.0	5.0	5.0	11.5	6.1	3.5	4.9
Korea	2.5	-2.5	4.1	2.1	-20.8	-3.0	5.9	6.5	4.5	4.0	4.5	2.2	2.5	3.4
Malaysia	5.1	1.3	4.6	3.1	-5.1	-1.0	4.9	5.7	6.6	2.8	5.9	3.9	1.2	1.6
Philippines	4.6	3.0	4.0	4.8	4.1	1.5	2.0	2.0	3.0	4.5	9.7	4.7	3.0	3.7
Singapore	1.1	-4.0	4.7	-6.8	-17.2	-5.9	7.0	4.9	4.9	4.1	5.4	2.1	1.0	3.5
Taiwan	0.9 ↓	-3.4 ↓	4.8	-8.7	-17.0 ↓	-2.5	3.0	5.8	6.3	4.2	1.8	-0.6 ↓	0.5 ↑	2.1 ↓
Thailand	3.4	-0.7	4.3	2.2	-14.4	0.0	4.1	6.1	4.1	3.2	2.2	-1.6	3.5	2.2
Africa														
South Africa	3.1	0.4	2.4	0.2	-0.7	-0.8	-0.1	1.9	3.3	3.1	11.1	6.5	5.0	4.3
Europe														
Euro area	0.7 ↓	-2.8 ↓	0.8	-0.7	-5.9 ↓	-5.0 ↓	-2.0 ↓	0.0	1.0	1.0	2.3	0.2 ↓	0.5 ↓	1.0 ↓
Germany	1.0 ↓	-3.1 ↓	0.8	-2.2 ↓	-8.2 ↓	-4.0	-1.0	0.0	1.0	1.0	1.7	0.1	0.3	0.9
France	0.7	-1.8 ↑	0.8	0.4 ↓	-4.6 ↑	-3.0	-1.0	0.0	1.0	1.0	2.0	-0.1	0.6	1.1
Italy	-0.9 ↓	-2.9 ↓	0.8	-2.2 ↓	-7.1 ↓	-4.0	-1.0	0.0	1.0	1.0	2.9	1.1	1.2	1.7
Norway	2.2	-1.3	1.0	1.0	-3.0	-3.0	-1.5	0.0	1.0	1.0	3.6	1.6	0.4	1.7
Sweden	0.2 ↓	-2.8 ↓	0.9	-0.4	-7.0 ↓	-5.0 ↓	-1.0	0.0	1.0	1.0	2.4	-0.6	-0.5	1.0
Switzerland	1.7	-2.0	1.1	0.1	-4.0	-5.0	-1.0	0.5	1.0	1.2	1.6	-0.6 ↓	0.3 ↓	0.3 ↓
United Kingdom	0.7	-2.9	1.0	-2.6	-5.9	-5.0	-1.5	0.0	1.0	1.0	3.9	0.7	0.2	2.3
Emerging Europe	4.3 ↓	-1.9 ↓	2.2	4.9 ↓	-8.3 ↓	-5.2 ↓	-1.7	0.2 ↑	1.2 ↑	2.6	9.5	7.0 ↑	6.5	5.4
Bulgaria	5.2	-1.5	2.0	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	3.5	-2.0	-0.5	3.8	-2.4 ↑	-7.0 ↓	-2.5	-2.0 ↑	-1.0 ↑	-0.5 ↓	4.7	0.5 ↑	1.3 ↑	3.0 ↑
Hungary	0.6 ↓	-3.2	0.2	-2.0 ↓	-3.9 ↑	-4.5	-3.5	-3.0	-2.0	1.0	4.3	1.8	2.4	2.5
Poland	4.9	0.0	1.8	4.9	-3.0	-2.5	-0.5	0.0	1.0	2.0	3.8	2.1	1.9	2.5
Romania	8.0	-3.0	1.0	...	...	...	...	...	...	...	6.8	6.0	8.0	5.0
Russia	5.6 ↓	-3.0 ↓	3.4	6.3	-13.5 ↓	-6.5 ↓	-1.5	2.0	3.0	4.0	13.8	11.7 ↑	10.4	8.1
Turkey	1.7	-0.8	2.0	...	...	...	...	...	...	...	10.9	6.9	6.1	5.0
Global	1.7	-1.9 ↓	2.4	0.1	-5.3 ↓	-5.1 ↓	-0.3 ↓	1.6	2.7	2.6	2.8	0.5 ↓	1.0	1.5 ↓
Developed markets	0.8	-2.8 ↓	1.8	-0.8	-5.3 ↓	-6.2 ↓	-1.3 ↓	0.5	1.8	2.0	1.9	-0.3	0.3	0.8 ↓
Emerging markets	5.1 ↓	1.4 ↓	4.9	3.9	-5.1 ↓	-1.0 ↓	3.6	5.8 ↑	6.4 ↑	4.9	6.4	3.8	3.7	4.1

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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	1.93	-279				1.63	1.39	1.36	1.25	1.34
excluding US	GDP-weighted average	2.77	-169				2.33	1.99	1.94	1.77	1.91
Developed	GDP-weighted average	0.86	-328				0.64	0.48	0.47	0.32	0.36
Emerging	GDP-weighted average	6.15	-85				5.55	5.03	4.89	4.90	5.22
Latin America	GDP-weighted average	9.53	72				8.59	7.74	7.73	7.73	7.88
CEEMEA	GDP-weighted average	7.72	71				7.25	6.74	6.43	6.44	6.30
EM Asia	GDP-weighted average	4.29	-203				3.77	3.36	3.24	3.26	3.81
The Americas	GDP-weighted average	1.22	-438				1.08	0.99	0.99	0.99	1.03
United States	Federal funds rate	0.125	-512.5	16 Dec 08 (-87.5bp)	17 Mar 09	on hold	0.125	0.125	0.125	0.125	0.125
Canada	Overnight funding rate	1.00	-350	20 Jan 09 (-50bp)	3 Mar 09	3 Mar 09 (-50bp)	0.50	0.50	0.50	0.50	1.00
Brazil	SELIC overnight rate	12.75	125	21 Jan 09 (-100bp)	11 Mar 09	11 Mar 09 (-100bp)	11.75	10.50	10.50	10.50	10.50
Mexico	Repo rate	7.75	50	16 Jan 09 (-50bp)	20 Feb 09	20 Feb 09 (-50bp)	6.75	6.25	6.25	6.25	6.25
Chile	Discount rate	4.75	-75	**12 Feb 09 (-250bp)**	12 Mar 09	**12 Mar 09 (-100bp)**	3.75	3.00	3.00	3.00	5.50
Colombia	Repo rate	9.00	-25	30 Jan 09 (-50bp)	27 Feb 09	27 Feb 09 (-50bp)	8.50	7.50	7.50	7.50	7.50
Peru	Reference rate	6.25	150	5 Feb 09 (-25bp)	5 Mar 09	5 Mar 09 (-25bp)	6.00	5.25	5.00	5.00	5.00
Europe/Africa	GDP-weighted average	2.50	-209				2.00	1.58	1.53	1.21	1.19
Euro area	Refi rate	2.00	-200	15 Jan 09 (-50bp)	5 Mar 09	5 Mar 09 (-50bp)	1.50	1.00	1.00	0.50	0.50
United Kingdom	Repo rate	1.00	-475	5 Feb 09 (-50bp)	5 Mar 09	**5 Mar 09 (-75bp)**	0.25	0.25	0.25	0.25	0.25
Sweden	Repo rate	1.00	-250	**11 Feb 08 (-100bp)**	21 Apr 09	**21 Apr 09 (-75bp)**	1.00	0.25	0.25	0.25	0.25
Norway	Deposit rate	2.50	-225	4 Feb 09 (-50bp)	25 Mar 09	6 May 09 (-50bp)	2.50	2.00	1.50	1.50	1.50
Czech Republic	2-week repo rate	1.75	-150	5 Feb 09 (-50bp)	26 Mar 09	**26 Mar 09 (-25bp)**	1.50	1.00	1.00	1.00	2.00
Hungary	2-week deposit rate	9.50	175	19 Jan 09 (-50bp)	23 Feb 09	23 Feb 09 (-50bp)	8.50	7.50	7.00	7.00	7.00
Israel	Base rate	1.00	-300	25 Jan 09 (-75bp)	23 Feb 09	4Q 09 (+50bp)	1.00	1.00	1.00	1.50	3.00
Poland	7-day intervention rate	4.25	-50	27 Jan 09 (-75bp)	25 Feb 09	25 Feb 09 (-75bp)	3.00	2.50	2.50	2.50	2.50
Romania	Base rate	10.00	300	4 Feb 09 (-25bp)	31 Mar 09	31 Mar 09 (-25bp)	9.75	11.00	13.00	14.00	12.00
Russia	1-week deposit rate	8.25	500	**10 Feb 09 (+100bp)**	2Q 09	**3Q 09 (-100bp)**	8.25	8.25	7.25	7.25	6.25
South Africa	Repo rate	10.50	50	5 Feb 09 (-100bp)	16 Apr 09	16 Apr 09 (-100bp)	10.50	8.50	8.00	7.50	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	13.00	-450	15 Jan 09 (-200bp)	19 Feb 09	19 Feb 09 (-50bp)	12.00	11.00	11.00	11.00	11.50
Asia/Pacific	GDP-weighted average	2.20	-134				1.93	1.74	1.69	1.70	2.00
Australia	Cash rate	3.25	-325	3 Feb 09 (-100bp)	3 Mar 09	3 Mar 09 (-50bp)	2.75	2.75	2.75	2.75	3.75
New Zealand	Cash rate	3.50	-475	29 Jan 09 (-150bp)	11 Mar 09	11 Mar 09 (-75bp)	2.75	2.25	2.25	2.25	2.25
Japan	Overnight call rate	0.10	-40	19 Dec 08 (-20bp)	19 Feb 09	on hold	0.10	0.10	0.10	0.10	0.10
Hong Kong	Discount window base	0.50	-625	17 Dec 08 (-100bp)	18 Mar 09	1Q 10 (+25bp)	0.50	0.50	0.50	0.50	0.63
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	2.00	-300	**12 Feb 09 (-50bp)**	11 Mar 09	**11 Mar 09 (-25bp)**	1.75	1.75	1.75	1.75	2.50
Indonesia	BI rate	8.25	0	4 Feb 09 (-50bp)	4 Mar 09	4 Mar 09 (-50bp)	7.75	7.00	7.00	7.25	8.00
India	Repo rate	5.50	-225	2 Jan 09 (-100bp)	21 Apr 09	1Q 09 (-100bp)	4.50	4.00	4.00	4.00	5.00
Malaysia	Overnight policy rate	2.50	-100	21 Jan 09 (-75bp)	24 Feb 09	**29 Apr 09 (-25bp)**	2.50	2.00	2.00	2.00	2.00
Philippines	Reverse repo rate	5.00	-100	29 Jan 09 (-50bp)	5 Mar 09	5 Mar 09 (-50bp)	4.50	4.00	4.00	4.00	4.00
Thailand	1-day repo rate	2.00	-125	14 Jan 09 (-75bp)	25 Feb 09	25 Feb 09 (-50bp)	1.50	1.00	1.00	1.00	1.00
Taiwan	Official discount rate	1.50	-163	7 Jan 09 (-50bp)	1Q 09	1Q 09 (-50bp)	1.00	0.75	0.75	0.75	0.75

Bold denotes move since last GDW and forecast changes. <u>Underline</u> 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	2.2	-0.5	1.5	1.4	0.3	-0.9	-3.4	1.4	1.3	0.8	0.8	2.0	2.5	3.8
Private consumption	2.0	-0.4	1.9	-0.5	0.2	-0.8	-2.8	0.8	1.6	2.4	1.6	2.0	2.0	2.4
Construction investment	3.8	-2.6	-3.5	1.6	2.1	-5.1	-4.8	-1.0	-1.9	-5.0	-6.2	-4.5	-0.4	3.3
Equipment investment	13.7	-12.9	-7.6	39.4	-0.9	-22.7	-29.4	-6.1	-4.1	-8.1	-19.4	-4.1	4.3	4.3
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	19.3
Government consumption	3.9	6.6	4.9	4.3	2.4	5.9	7.8	11.8	4.1	5.2	5.2	5.2	2.2	2.1
Exports of goods & services	4.6	-8.3	-2.2	12.9	0.0	-9.6	-15.1	-13.3	-5.9	0.0	-2.0	-1.2	0.0	2.8
Imports of goods & services	11.7	-4.4	-1.9	14.0	6.5	-7.0	-9.6	-7.8	-4.7	-2.0	-3.9	1.6	1.6	2.0
Contributions to GDP growth:														
Domestic final sales	4.0	0.2	1.6	4.0	1.2	-0.9	-2.9	2.4	1.6	1.5	0.1	2.0	2.8	3.7
Inventories	-0.1	0.0	-0.1	-1.8	0.7	0.3	0.4	-0.2	-0.3	-1.1	0.1	0.6	0.0	0.0
Net trade	-1.7	-0.6	0.0	-0.7	-1.6	-0.3	-0.8	-0.9	0.0	0.5	0.6	-0.6	-0.4	0.1
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)	4.4	1.9	2.0	4.5	5.0	3.7	2.8	1.8	1.1	1.9	2.1	1.9	2.0	2.1
Producer prices (%oya)	8.3	1.6	0.7	8.7	10.9	6.7	4.2	0.6	-0.5	2.3	1.1	0.5	0.4	1.0
Trade balance (A$ bil, sa)	-7.4	-12.6	-15.2	-1.7	1.1	1.1	-0.8	-3.6	-4.4	-3.8	-4.0	-3.7	-3.8	-3.7
Current account (A$ bil, sa)	-67.0	-61.7	-64.2	-14.0	-9.7	-10.7	-12.8	-15.8	-16.7	-16.3	-16.5	-16.7	-15.8	-15.2
as % of GDP	-6.2	-5.1	-5.1	-4.8	-3.2	-3.6	-4.3	-5.2	-5.5	-5.3	-5.3	-5.4	-5.0	-4.7
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	-35.5	-62.0											
as % of GDP	1.1	-2.9	-4.9											
Unemployment rate	4.2	5.8	8.0	4.3	4.2	4.4	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	-1.0	1.4	-0.8	-1.5	-2.6	-1.4	-0.7	1.1	1.9	0.9	2.4	1.3	2.3
Private consumption	0.1	-0.2	2.3	-0.8	-0.6	-0.8	-1.0	-0.1	1.9	2.3	3.0	1.5	3.0	4.0
Fixed Investment	-2.9	-5.4	4.9	7.1	-29.7	-11.1	-1.9	1.4	4.0	7.7	5.7	3.7	4.4	3.5
Residential construction	-16.9	-17.0	3.4	-28.9	-27.6	-40.0	-12.0	0.0	4.0	6.0	4.0	2.0	2.0	3.2
Other fixed investment	0.6	-3.0	5.2	17.1	-30	-4.0	0.0	1.6	4.0	8.0	6.0	4.0	4.8	3.6
Inventory change (NZ$ bil, saar)	1.7	1.2	0.5	0.3	0.6	0.4	0.3	0.3	0.3	0.3	0.2	0.1	0.2	0.1
Government spending	4.1	9.0	-1.1	0.7	4.2	8.1	14.7	10.0	8.0	7.0	-6.4	-3.0	-9.8	-6.8
Exports of goods & services	-1.0	-3.0	3.8	-1.0	-12.0	-5.0	-2.4	-1.5	2.2	3.6	5.0	6.0	2.5	4.5
Imports of goods & services	3.4	-2.4	3.4	16.0	-27.1	-8.0	0.5	5.1	6.2	7.3	2.0	1.0	2.0	1.0
Contributions to GDP growth:														
Domestic final sales	1.3	-0.5	2.1	6.2	-12.1	-2.2	1.2	1.4	2.7	3.6	1.9	1.3	0.9	2.1
Inventories	0.6	-0.4	-0.5	-0.6	2.9	-1.9	-1.7	0.2	0.1	-0.1	-1.8	-0.4	0.4	-0.8
Net trade	-1.6	0.0	-0.1	-6.1	8.6	1.5	-0.9	-2.3	-1.6	-1.6	0.7	1.4	0.0	1.0
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	4.0	-0.4	1.6	6.7	6.2	-1.8	-1.6	-0.8	0.0	0.8	1.6	2.4	3.2	3.7
%oya	4.0	0.3	1.6	4.0	5.1	3.4	2.3	0.4	-1.1	-0.4	0.4	1.2	2.0	2.7
Trade balance (NZ$ bil, sa)	-3.9	-7.6	-13.6	-1.1	-0.9	-1.8	-1.4	-1.3	-2.0	-2.9	-3.5	-3.3	-3.7	-3.2
Current account (NZ$ bil, sa)	-18.0	-19.3	-24.5	-4.7	-4.1	-5.7	-4.1	-5.0	-4.9	-5.3	-6.2	-5.2	-6.6	-6.4
as % of GDP	-10.1	-12.0	-14.0	-10.4	-9.3	-13.1	-11.3	-11.1	-12.0	-13.8	-14.5	-13.9	-14.2	-13.3
Yield on 90-day bank bill (%)*	7.9	3.4	3.5	8.8	8.2	6.0	3.8	3.4	3.2	3.1	3.2	3.4	3.5	3.9
10-year bond yield (%)*	6.0	3.6	4.0	6.5	5.9	5.3	4.1	3.6	3.3	3.3	3.5	3.8	4.0	4.5
US$/NZ$*	0.71	0.68		0.78	0.71	0.58	0.70	0.68	0.67	0.59	0.60	0.62	0.64	0.64
Commonwealth budget (NZ$ bil)	-1.8	-7.2	-8.6											
as % of GDP	-1.0	-4.1	-4.6											
Unemployment rate	4.0	6.1	7.6	3.9	4.2	4.4	5.2	5.7	6.3	7.0	7.3	7.5	7.7	7.7

*All financial variables are period averages

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Australia and New Zealand economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
16 Feb New Zealand : PPI (10:45 am) 4Q 0.3 %q/q	17 Feb	18 Feb Australia : Westpac leading index (10:30 am) Dec Retail sales (11:30 am) 4Q 1.1 %q/q, sa	19 Feb Australia : New motor vehicles sales (11:30 am) Jan	20 Feb
23 Feb New Zealand : Credit card spending (3:00 pm) Jan	24 Feb	25 Feb Australia : Construction work done (11:30 am) 4Q Wage cost index (11:30 am) 4Q New Zealand : RBNZ inflation expectation (10:45 am) 1Q	26 Feb Australia : Private capital expenditure (11:30 am) 4Q New Zealand : Trade balance (10:45 am) Jan NBNZ business conf. (3:00 pm) Feb	27 Feb Australia : Private sector credit (11:30 am) Jan New Zealand : Visitor arrivals (10:45 am) Jan Building permits (10:45 am) Jan
2 Mar Australia : Inventories (11:30 am) 4Q Company profits (11:30 am) 4Q	3 Mar Australia : Retail sales (11:30 am) Jan Current account (11:30 am) 4Q RBA cash target (2:30 pm) Mar	4 Mar Australia : GDP (11:30 am) 4Q New Zealand : ANZ commodity price (3:00 pm) Feb	5 Mar Australia : Building approvals (11:30 am) Jan Trade balance (11:30 am) Jan	6 Mar
9 Mar Australia : ANZ job ads (11:30 am) Feb New Zealand : QV house prices Feb	10 Mar Australia : NAB business confidence (11:30 am) Feb New Zealand: NZIER bus. opinion survey (10:00 am) 1Q	11 Mar Australia : Westpac consumer confidence (10:30 am) Mar Housing finance (11:30 am) Jan New Zealand: Terms of trade (10:45 am) 4Q	12 Mar Australia : Unemployment rate (11:30 am)Feb New Zealand RBNZ official cash rate (9:00 am) Mar	13 Mar New Zealand : Retail sales (10:45 am) Jan

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
16 - 20 February	16 February	17 February	18 February	19 February	20 February
	Euro area • Trichet speech Japan • GDP 1st est (4Q) • IP final (Dec)	Brazil • Retail sales (Dec) Euro area • International trade (Dec) Germany • ZEW business sur (Feb) Japan • Reuters Tankan (Feb) • Tertiary sect activ (Dec) Russia • IP (Jan) United Kingdom • CPI (Jan) United States • NY Fed survey (Feb) • NAHB survey (Feb)	Taiwan • GDP (4Q) United Kingdom • MPC minutes United States • Housing starts (Jan) • Import prices (Jan) • IP (Jan) • FOMC minutes • Bernanke speech	Japan • Dept store sales (Jan) • BoJ meeting Norway • GDP (4Q) Poland • IP (Jan) Sweden • CPI (Jan) Turkey • CBRT meeting United States • Philly Fed survey (Feb) • PPI (Jan)	Canada • CPI (Jan) Euro area • PMI flash (Feb) France • CPI (Jan) • INSEE bus surv (Feb) Japan • All sector activity (Dec) Mexico • Real GDP (4Q) • Banxico meeting United Kingdom • Retail sales (Jan) United States • CPI (Jan)
	23 February	24 February	25 February	26 February	27 February
	Germany • CPI prelim (Feb) Hungary • NBH meeting Israel • BoI meeting	Belgium • BNB business sur (Feb) Euro area • Industrial orders (Dec) Germany • IFO business surv (Feb) Japan • BoJ minutes Malaysia • BNM meeting South Africa • GDP (4Q) Taiwan • Export orders, IP (Jan) United States • CS & FHFA HPI (Dec, 4Q) • Bernanke delivers semiannual policy testimony to Senate	Germany • GDP final (4Q) Italy • ISAE business surv (Feb) Japan • Shoko Chukin (Feb) • Trade balance (Jan) Poland • NBP meeting South Africa • CPI (Jan) Thailand • BoT meeting United Kingdom • GDP (4Q) United States • Existing home sales (Jan)	Euro area • EC business surv (Feb) • M3 (Jan) Germany • Labor mkt report (Feb) United Kingdom • BoE to testify before Parliament on banking crisis	Colombia • BanRep meeting Euro area • HICP final (Jan) • Unemployment (Jan) India • GDP (4Q) Japan • CPI (Jan) • Household spend (Jan) • IP prelim (Jan) • PMI mfg (Feb) • Retail sales (Jan) • Unemployment (Jan) Sweden • GDP (4Q) United States • Chicago PMI (Feb) • Consumer sent (Feb) • Real GDP prelim (4Q)

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