J.P.Morgan

Australia and New Zealand - Weekly Prospects

Summary

- Last week, the **RBA** signaled it had tacked away from the previous commentary hinting that a rate cut was more likely than a hike. Indeed, one message from Governor Stevens' speech was that the Bank will not wait for the jobless rate to peak before tightening—this will be an important break from convention. Today, the RBA will leave the cash rate steady, but the tone of the language will be upbeat, more in line with the Governor's speech last week than the last policy announcement. Also, the statement will remove the implied easing bias by erasing the earlier reference to "scope for further easing." On Friday, the RBA's quarterly statement will include upward revisions to the official growth and inflation forecasts, which will confirm the RBA has moved to a neutral policy bias. This week also brings key economic data—the July labour force survey should deliver a jobless rate with a 6%-handle for the first time since 2003, thanks to a 25,000 drop in employment. The June retail outcome today, though, probably will print a solid monthly gain; the quarterly data should show volumes bouncing 1.7%q/q; this will make a significant positive contribution to 2Q GDP growth.
- In **New Zealand**, RBNZ Governor Alan Bollard remained dovish in the statement accompanying the OCR announcement last week, in which rates were kept on hold. While the market expected such rhetoric, officials surprised by strongly voicing concern about continued NZD strength and the impact the currency may have on a prospective export-led recovery. The RBNZ explicitly said that if financial conditions fail to ease, the RBNZ would "reassess policy settings." Economic data this week should confirm that labour markets continue to deteriorate, with unemployment rising sharply in 2Q.
- Economic developments this year provide a case study in the dynamism of the **global business cycle**. Even as the global economy was in the midst of a severe and synchronized downturn at the start of the year, a foundation for a quick recovery was being laid. The central pillar was policy medication that proved sufficient to contain the crisis in funding markets, moderating a significant drag on the economy. This medication was also important in calming downside tail-risk fears. As such, it combined with other supports—fiscal stimulus and a drop in inflation—to stem the slide in consumer spending. The resilience of consumer demand during 1H09 was a major surprise to firms and it allowed them to make dramatic and rapid adjustment to their inventories and production costs.
- At this stage, however, the central element of our forecast is that the **global recovery** will have "legs"—with above-trend growth sustained for a number of quarters. To track this view, we need to look beyond coincident growth indicators and gauge whether a positive feedback loop is established. This loop entails positive reverberations from the rebound in growth—to labour income, financial conditions, and confidence—which promotes stronger spending by households and business. The power of this dynamic coming out of a deep downturn should not be underestimated.

This week's highlight

The RBA's quarterly statement Friday. The statement will include upwardly revised growth and inflation forecasts. The changes will further strengthen the argument that the next move in the cash rate will be a hike.

Aug 4, 2009

Contents

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Data and event previews - Australia and New Zealand

			Forecast		
Date	**Time** [(a)]	**Data/event**	**JPMorgan**	Consensus [(b)]	***Previous***
Tuesday, August 4	11.30am	Aust. house price index (%q/q, 2Q)	**1.0**	1.9	*-2.2*
Tuesday, August 4	11.30am	Aust. retail sales (%m/m, Jun.)	**0.9**	0.5	*1.0*
Tuesday, August 4	1.00pm	NZ ANZ commodity price index (%m/m, Jul.)	**na**	na	*0.2*
Tuesday, August 4	2.30pm	RBA cash rate announcement (%)	**3.00**	3.00	*3.00*
Wednesday, August 5	9.30am	AiG performance of services index (Index, Jul.)	**na**	na	*50.2*
Wednesday, August 5	11.30am	Aust. trade balance (A$mn, Jun.)	**-750**	-800	*-556*
Thursday, August 6	8.45am	NZ employment (%q/q, 2Q)	**-0.4**	-0.5	*-1.1*
Thursday, August 6	11.30am	Aust. employment (ch. 000s, Jul.)	**-25**	-18	*-21.4*
Friday, August 7	9.30am	AiG performance of construction index (Index, Jul.)	**na**	na	*42.6*
Friday, August 7	11.30am	RBA's quarterly Statement on Monetary Policy	**na**	na	*na*

(a) Australian Eastern Standard Time.
(b) Consensus based on Bloomberg survey.

Australia

Aust. house price index (%q/q, 2Q) - House prices probably rose 1.0%q/q in 2Q, though differing rates of population growth and affordability will mean that the price falls will not be uniform across the nation. Solid demand from first home buyers will have prevented a fall in house prices in 2Q; this burgeoning demand has kept house prices at the lower end of the house price spectrum particularly well supported.

Aust. retail sales (%m/m, Jun.) - We expect another spike in retail sales—consumer confidence surged in June, equity prices were up, and so was AUD, all factors which probably helped prolong the cashed-up consumer spending binge. Also, some of May's fiscal boost in the form of cash payments would have leaked into June. The quarterly retail volume numbers are important for our 2Q GDP forecast, and will show a big rise.

RBA cash rate announcement (%) - The RBA will leave the cash rate steady, but the tone of the language will be upbeat, more in line with the Governor's speech last week than the last policy announcement. Also, the statement will remove the implied easing bias by erasing the earlier reference to "scope for further easing". The RBA's quarterly statement Friday will see upward revisions to the official growth and inflation forecasts, which will confirm the RBA has moved to a neutral policy bias.

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Data and event previews - contd.

Aust. trade balance (A$mn, Jun.) - Imports will hold steady in June, but exports will fall, mainly owing to declining prices for Australia's key commodity exports. The trade deficit will worsen slightly to A$750 million.

Aust. employment (ch. 000s, Jul.) - The Aussie labour force survey should show a 25,000 drop in employment for July, following a 21,400 fall in June. With the participation rate remaining elevated at 65.3%, the unemployment rate should print at 6.2%, up 0.4% from the previous month. We continue to argue that the participation rate will be slow to decline in this recession, the main reason being that older workers will stay in the work force for longer in order to resurrect their retirement funds.

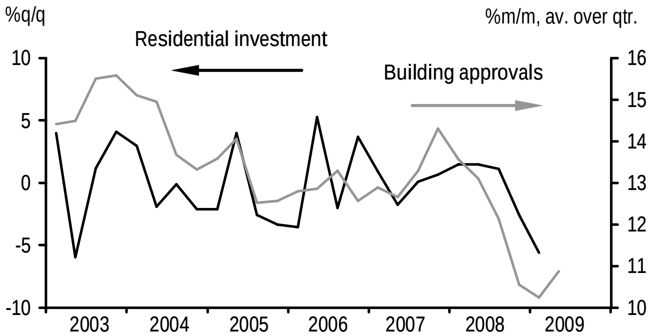
RBA's quarterly Statement on Monetary Policy - The quarterly statement will bring key changes to the official forecasts. The fact that Australia's economy avoided technical recession in 1Q (the last SoMP forecast recession), means that the quarterly statement will include an upgrade to the GDP forecast. We also expect an upward revision to the core inflation forecast of around 1%.

New Zealand

NZ employment (%q/q, 2Q) - Employment in New Zealand probably fell 0.4%q/q in 2Q, after falling 1.1% in 1Q. The unemployment rate should have risen significantly to 5.5% from 5.0%, marking the sixth straight quarterly rise, and labour force participation will remain at an elevated 68.3%. More indicative of the weakness in the labour market, though, will be the anticipated elevated level of underemployed workers. Of the 473,500 people employed part-time in 1Q, 21.1% wanted to work more hours, up from 19.3% in the previous quarter.

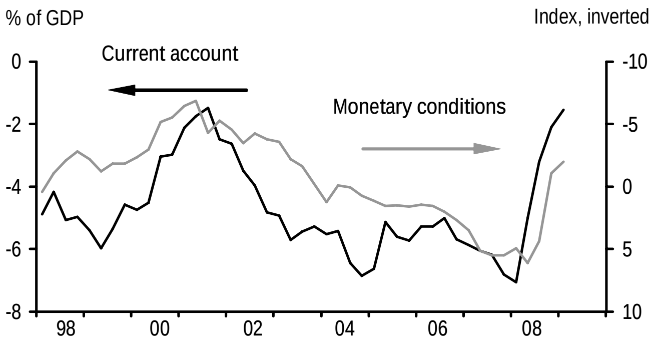
Feature charts

Australia: private residential investment and building approvals



RBA Governor Stevens has expressed concern that the Australian housing market—buoyant since the expansion of the FHB's grant—could see price rises without an expansion in housing supply. Residential investment has struggled to rise in the past year due to difficulties for buyers obtaining finance and exuberant state-level taxing. With immigration at record levels, greater housing supply is needed sooner rather than later. The rise in building approvals in 2Q suggests this is on track.

Australia: current account balance and J.P. Morgan MCI



Australia's current account deficit has become less burdensome over the last couple of years due to the terms of trade boom. However, for the majority of the decade, strong global growth, rising domestic interest rates and, consequently, AUD appreciation led to increasingly deep deficits. While interest rates now are very low by historical standards, they currently are among the highest in the developed world. A continued rally in AUD could see the current account worsen again.

New Zealand: house prices and GDP growth

The majority of Kiwi households' wealth is held in property. It is no surprise then, that oscillations in the housing market have a significant bearing on real demand through wealth effects. The New Zealand economy has been in recession for five straight quarters, with house prices declining over the same period. As falling mortgage rates bolster home loan demand, house price falls have moderated. GDP growth too appears to have reached a bottom—we expect the recession to end in 4Q09.

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Australia

- **RBA signals no more rate cuts**
- **Employment likely fell 25,000 in July**
- **Credit growth remains soft**

The economic focus in Australia last week was on central bank commentary. The RBA Governor essentially reaffirmed our assessment that the Bank's easing cycle is over, and that the official cash rate will rise before the unemployment rate peaks.

RBA signals that next move is a hike

Reserve Bank Governor Glenn Stevens' speech to the Australian Business Economists' lunch last week signalled that the RBA is changing tack. The biggest takeaway was that the Governor did not rule out raising the cash rate while the jobless rate is climbing. There is a perception in markets, supported by history, that the RBA will not tighten policy as unemployment rises. The unusual nature of this easing cycle, however, in that the policy stimulus was delivered early and in spades, means that the tightening cycle also will be unusual—the established rules no longer apply.

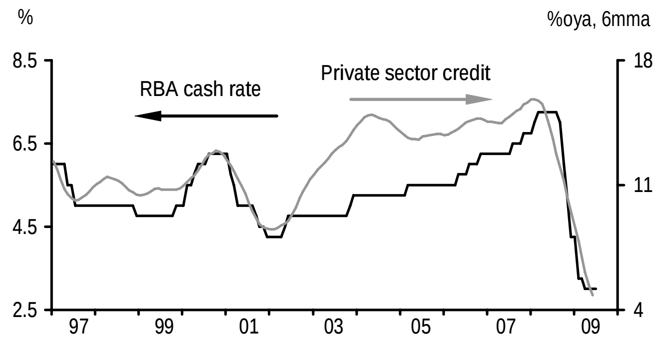
Stevens' comments on the domestic economic challenges were little changed from the Board minutes of two weeks ago, except that he made clear it now is easier to see upside risks as well as downside. In particular, his comments focused on the importance of productivity gains, and that economic conditions are firmer than had looked likely earlier this year. Also, employment has held up, so the rise in the jobless rate has been unexpectedly mild. One challenge, though, is that the dwindling business investment pipeline means that productivity growth will slow. The shrinking pipeline makes it more likely that firms will start to trim workers, not just hours. The Governor made clear that inflation will continue to fall.

More broadly, he alluded to the complexity of one problem in the global financial sector: while some institutions are too big to fail, they also are too big to save. Moreover, last week's sticky core inflation print was not really a surprise. Finally, he pointed to the vague concept of a neutral cash rate, hinting that the nature of neutral has changed because banks now are more inclined to adjust rates independently of the RBA.

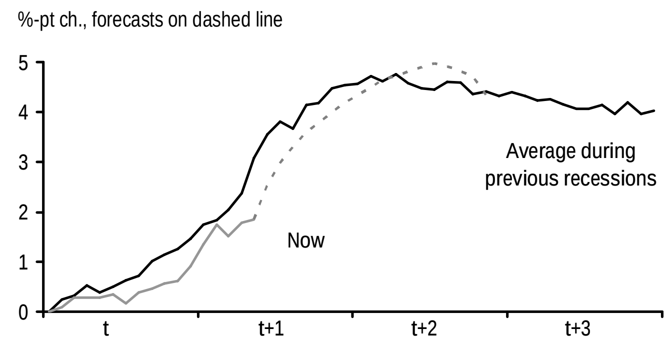
RBA to stand pat, but push forecasts up

The RBA today will leave the cash rate steady at 3% for the fourth straight month. The Statement on Monetary Policy Friday, however, will bring key changes to the official fore-

Australia: RBA cash rate and credit growth



Australia: unemployment t years from trough



casts. The fact that Australia's economy avoided technical recession in 1Q (the last SoMP forecast recession), means that the quarterly statement almost certainly will include an upgrade to the GDP forecast. This will make it even more clear that the easing cycle is well and truly over, and that the RBA has turned its attention to the nature and timing of the exit strategy. A material upward revision to the inflation forecast is also expected.

Our forecast is that the RBA will hike by mid-2010 at the latest, even as unemployment is climbing towards 9%. The substantial policy accommodation provided by the generational-low cash rate, coupled with the largest fiscal stimulus since the early 1970s, should be sufficient triggers for the RBA to take a leap of faith and tighten preemptively, provided they are confident that the jobless rate is close to peaking.

6%-handle likely on Aussie jobless rate

The Aussie labour force survey should show a 25,000 drop in employment for July, following a 21,400 fall in June. With the participation rate remaining elevated at 65.3%, the unemployment rate should print at 6.2%, up 0.4% from the previous month. We continue to argue that the participation rate will be slow to decline in this recession, the main reason being that older workers will stay in the work force for

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longer in order to resurrect their retirement funds.

Though we have yet to see the falls in employment we had anticipated earlier this year, there was a sharp fall in the number of hours worked during 1H09, as firms took advantage of the previous government's unprecedented industrial flexibility, much of which ceased on June 30. This allowed firms to curb labour costs while retaining skilled workers. The plunge in hours worked since December is equivalent to the loss of 90,000 full-time jobs, on top of the 40,000 positions the official data show have been trimmed. Eventually, though, firms will shed workers while also trimming hours, as was the case in earlier recessions.

Consumers still splurging

We expect that retail sales values in Australia grew 0.9%m/m in June, nearly matching the solid 1.0% expansion in May. Consumer confidence surged in June, equity prices were up, so was AUD, all factors which probably helped prolong the cashed-up consumer spending binge, which initially owed to the generous government cash handouts. Treasury forecasts, though, that most of the impact of the fiscal stimulus packages is felt in the first six months after they are paid out, before gradually dissipating; thus, retailers are justifiably concerned about the consumer spending outlook. Indeed, the real test of the consumer will be in 2H when the impact of the fiscal stimulus abates.

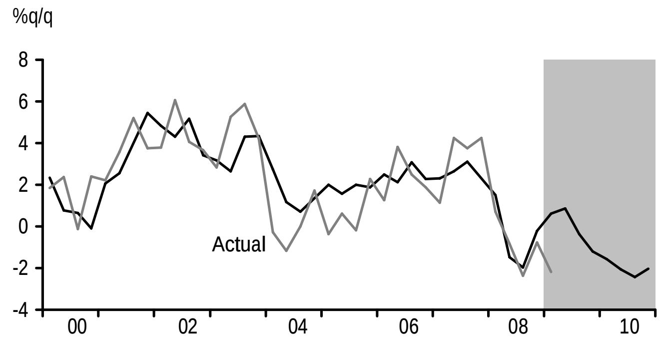
The quarterly retail volume numbers this week are important for our 2Q GDP forecast, with retail sales accounting for a quarter of GDP. In 2Q, we forecast retail volumes to rose 1.7%q/q, the largest rise in nearly two years, again thanks to the fiscal stimulus.

House prices still high . . . for now

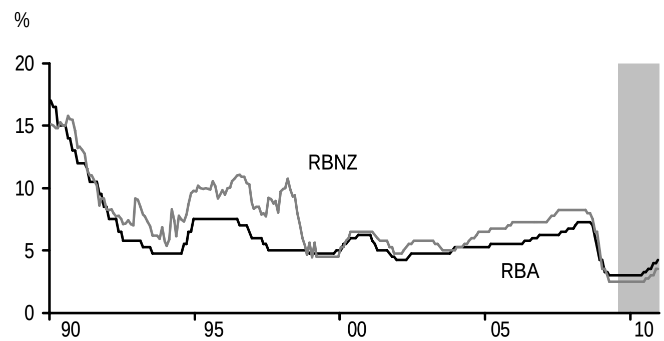
Australian house prices probably rose 1.0%q/q in 2Q, after falling 2.2% in 1Q, which was the fourth straight quarterly decline. Differing rates of population growth and affordability will mean that the price falls will not be uniform across the nation. Solid demand from first home buyers will have prevented a fall in house prices in 2Q; this burgeoning demand has kept house prices at the lower end of the house price spectrum particularly well supported.

Our forecast calls for house prices to fall 15% from peak to trough. The most economically significant variable in our house price model is unemployment. The model estimates that a 1%-point rise in the jobless rate depresses house prices 1.25%-points. Projections for unemployment, therefore, have a significant bearing on our house price forecasts; we see the jobless rate peaking at 9% in 2010.

Australia: house prices, model vs actual



Australia and New Zealand: cash rates



Credit aggregates grew again

The RBA's measure of private credit grew 0.1%m/m in June, the same rate as in each month since February, barring May. Then, credit outstanding contracted 0.1%. Before May, only once since 1992 had the amount of credit outstanding contracted. Interestingly, for two straight quarters now, the rate of credit growth has fallen below GDP growth, an event that tends to happen only during recession. Personal and business lending continued to fall. Personal loans were down 0.3%m/m, and business lending fell 0.5%. The RBA attributed the significant decline in business lending since November last year to falls in foreign currency denominated lending, owing in part to strengthening AUD. Higher bank lending rates, tighter lending standards, and firms' trimming of capital spending plans, also helps explain the persistent weakness in business loans.

Loans for housing picked up in June, as expected in the wake of the government's decision in May to extend the first home buyers' grant until year-end (from its previous July 31 expiry). This was confirmed in the credit numbers which showed the rise in housing credit over June was mainly due to growth in lending to owner-occupiers, not investors. The expanded grant, though, will be phased

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down gradually during 2H09, meaning that loan growth for housing may moderate from the current rate of 0.6%m/m.

RBA Governor Glenn Stevens last week warned of a credit fuelled property bubble, saying that the challenge ahead was “how to ensure that the ready availability and low cost of housing finance is translated into more dwellings, not just higher prices.” The Governor believes that the current environment offers good opportunities to increase “dwelling stock without a major run-up in prices” and help Australia overcome its chronic shortage of housing supply.

Data releases and forecasts

Week of August 3 - 7

Mon
Aug 3
11:30am

ANZ job advertisements
Seasonally adjusted

	Apr	May	Jun	Jul
(%m/m)	-7.5	-0.2	-6.7	__

Mon
Aug 3
11:30am

Retail trade
Seasonally adjusted

	Mar	Apr	May	Jun
(%m/m)	2.2	0.3	1.0	0.9
(%oya)	6.3	6.8	7.1	9.2

Tue
Aug 4
11:30am

House price index: eight capital cities
Weighted average

	3Q08	4Q08	1Q09	2Q09
(%q/q)	-2.6	-1.2	-2.2	1.0
(%oya)	1.4	-3.9	-6.7	-5.0

Tue
Aug 4
02:30pm

RBA cash rate announcement

No change expected.

Wed
Aug 5
11:30am

Trade balance
Seasonally adjusted

	Mar	Apr	May	Jun
Trade balance (A$ mn)	2000	-282	-556	-750

Imports will hold steady, but exports will fall, mainly owing to declining prices of key commodity exports.

Thu
Aug 6
11:30am

Labour force
Seasonally adjusted

	Apr	May	Jun	Jul
Unemployment rate (%)	5.5	5.7	5.8	6.2
Employed (000 m/m)	26	-8.5	-21.4	-25
Participation rate (%)	65.4	65.4	65.3	65.3

Review of past week’s data

Building approvals
Seasonally adjusted

	Apr		May		Jun	
(%m/m)	~~4.1~~	*3.1*	~~-12.5~~	*-11.0*	~~3.0~~	*9.3*
(%oya)	~~-15.4~~	*-15.3*	~~-22.4~~	*-21.3*	~~-21.2~~	*-14.3*

Private-sector credit
Seasonally adjusted

	Apr		May		Jun	
(%m/m)	0.1		-0.1		~~0.0~~	*0.1*
(%oya)	4.5		~~3.9~~	*3.8*	~~3.3~~	*3.4*

New Zealand

- **RBNZ on hold until mid-2010**
- **RBNZ concerned about NZD strength**
- **Unemployment to have jumped higher in 2Q**

RBNZ on hold, anxious about strong NZD

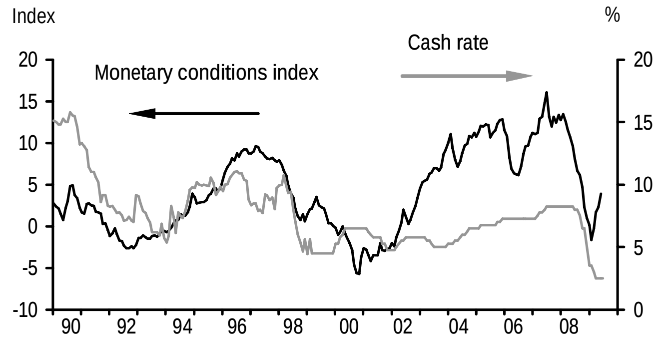
The RBNZ left the official cash rate (OCR) unchanged at 2.5%, but the accompanying commentary undoubtedly was more dovish. Governor Bollard reiterated that the OCR would remain "at or below" current levels until the end of 2010, but the language surrounding his anxiety about continued NZD strength was firmer than that used previously.

The RBNZ expects a recovery in New Zealand starting toward year end, but the return to growth will be "patchy." The main risk is elevated NZD. Governor Bollard again flagged continued NZD strength as a key risk to the economic outlook. Not only is high NZD hampering a prospective export-led recovery that could emerge in sync with a global demand pickup, but it is also contributing to tighter domestic monetary conditions. Unlike in previous statements, the RBNZ explicitly said that if financial conditions fail to ease, the RBNZ would "reassess policy settings."

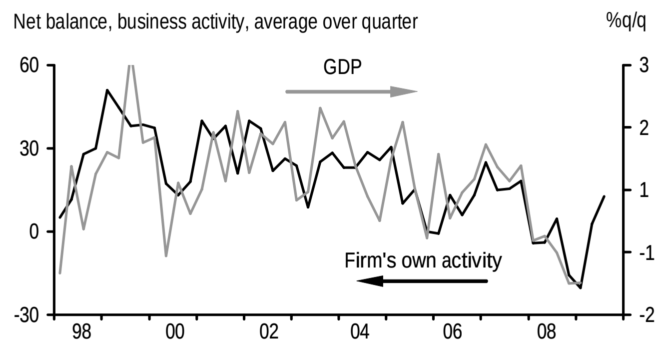
The statement accompanying the decision failed to bring up many positive factors. There was no mention, for example, of stabilization offshore or "upside opportunities for activity" as there was accompanying the last OCR announcement six weeks ago. Then, the RBNZ acknowledged "a potential rebound in household spending and residential investment as a result of the rise in net immigration and the pickup in the housing market." The central bank is becoming more concerned that consumers may revert to their old "borrow to spend" habits. Recent RBNZ comments have highlighted the need for a shift away from debt-driven consumption to boost growth; this is a key argument for interest rates not to go any lower.

There is more scope for further policy easing—financial conditions remain tight, the terms of trade are falling, and inflation pressures have eased—but the aggressive pace at which the RBNZ cut the cash rate in this easing cycle means that the RBNZ Governor probably will be wary of leaving the cash rate too low for too long. It will, in our view, take a material deterioration in the global outlook to trigger a further reduction in the cash rate. We believe the RBNZ's job in this rate cutting cycle is finished. Our forecast calls for rate hikes from 3Q10.

New Zealand: RBNZ official cash rate and J.P. Morgan MCI



New Zealand: NBNZ business outlook survey and GDP growth



NZ businesses becoming more upbeat

The NBNZ business confidence survey improved again in July, with a net 18.7% of respondents now expecting business conditions to improve (up from 5.5%). This is encouraging, as the end to New Zealand's prolonged recession is within reach, and firmer confidence is key to the prospective recovery. Firms' own activity expectations rose to +12.6 from +8.3, signalling that any contraction in 3Q GDP will be mild; the economy should finally start to expand in 4Q. Our forecast is for the economy to contract just 0.1%q/q in 3Q, marking the seventh straight quarterly GDP contraction, before an expected expansion of 0.6% in 4Q.

NZ labour market softening

Employment in New Zealand probably fell 0.4%q/q in 2Q, after falling 1.1% in 1Q. The unemployment rate should have risen significantly to 5.5% from 5.0%, marking the sixth straight quarterly rise, and labour force participation will remain at an elevated 68.3%. More indicative of the weakness in the labour market, though, will be the anticipated elevated level of underemployed workers. Of the 473,500 people employed part-time in 1Q, 21.1% wanted to work more hours, up from 19.3% in the previous quarter.

Data this morning showed that private sector labour costs (as measured by the LCI) rose just 0.3%q/q in 2Q (J.P. Morgan 0.6%, consensus 0.5%), below all market economists' forecasts. The 2Q result marked the slowest quarterly wage growth since early 2000. From a year ago, wage inflation eased to the slowest pace in eight years, rising just 2.6%oya. All sector wage growth slowed to 0.3%q/q, or 2.9% from the previous year. Indeed, following the weakness in the LCI today, there is upside risk to our unemployment rate forecast of 5.5% in 2Q.

Soft wage growth and rising job insecurity, with the unemployment rate expected to rise for at least the next 12 months, means that private consumption will remain weak in the foreseeable future. In our forecasts, household spending will fall by 1.6% this year, but if labour market indicators deteriorate faster than expected, the risks to our private consumption growth forecast will be skewed to the downside.

Data releases and forecasts

Week of August 3 - 7

Tue Aug 4 3.00pm — **ANZ commodity price series**
Not seasonally adjusted

	Apr	May	Jun	Jul
Index - world prices (%m/m)	2.6	2.8	0.2	__
Index - NZD (%m/m)	-2.7	-1.4	-5.0	—

Tue Aug 4 10:45am — **Labour cost index and average hourly earnings**
Private sector, ordinary time, sa

	3Q08	4Q08	1Q09	2Q09
(%q/q)	1.1	0.7	0.6	0.3

Thu Aug 6 10:45am — **Labour force survey**
Seasonally adjusted

	3Q08	4Q08	1Q09	2Q09
Unemployment rate (%)	4.3	4.7	5.0	5.5
Employment (000, q/q)	4	13	-24	-8.7
Participation rate (%)	68.6	69.1	68.4	68.3

Review of past week's data

Trade balance
Not seasonally adjusted

	Apr		May		Jun	
Trade balance (NZ$ mn)	~~319~~	*342*	~~858~~	*907*	~~350~~	*-417*

Building consents
Not seasonally adjusted

	Apr	May	Jun	
(%m/m)	-7.5	22.7	__	*-11.1*
(%oya)	-57.5	-25.1	__	*-20.3*

NBNZ business confidence

	May	Jun	Jul	
% balance of respondents	-1.9	5.5	~~8.0~~	*18.7*

RBNZ cash rate announcement

No change in rates.

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Global Essay

- **Current-quarter GDP growth rates revised up for the US (3.0%), Euro area (2.5%), Japan (3.5%), and Brazil (5.5%)**
- **A positive feedback loop is developing between growth and financial-market conditions**
- **UK's MPC to hold firm this week, counseling patience in assessing the full impact of its QE policies**
- **Return of risk appetite green-lights CEE central banks to refocus efforts from fx stabilization to credit creation**

Loops and legs

Economic developments this year provide a case study in the dynamism of the global business cycle. Even as the global economy was in the midst of a severe and synchronized downturn at the start of the year, a foundation for a quick recovery was being laid. The central pillar was policy medication that proved sufficient to contain the crisis in funding markets, moderating a significant drag on the economy. This medication was also important in calming downside tail-risk fears. As such, it combined with other supports—fiscal stimulus and a drop in inflation—to stem the slide in consumer spending. The resilience of consumer demand during 1H09 was a major surprise to firms and it allowed them to make dramatic and rapid adjustment to their inventories and production costs. Starting in Asia last quarter, and spilling towards North America and Western Europe this quarter, growth is rebounding as firms calibrate the pace of adjustment and begin to upgrade expectations about the future.

Recent data releases bolster our confidence that this dynamic will deliver above-trend growth across the globe this quarter. Consistent with this view, our July global manufacturing PMI index rose to its highest level since the start of 2008 on Monday, hitting the breakeven 50 level. What's more, signs that capital goods shipments are stabilizing suggest that the impetus for a recovery in production includes improved capital spending trends, alongside a moderation in the global inventory correction.

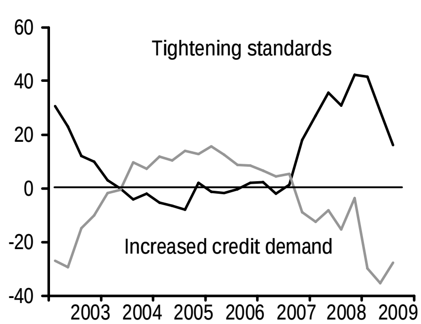
At this stage, however, the central element of our forecast is that the global recovery will have "legs"—with above-trend growth sustained for a number of quarters. To track this view, we need to look beyond coincident growth indicators and gauge whether a positive feedback loop is established. This loop entails positive reverberations from the rebound in growth—to labour income, financial conditions, and confidence—which promotes stronger spending by households and business. The power of this dynamic coming out of a deep downturn should not be underestimated. In the ashes of severe recessions in 1974-75 and 1981-82, the developed world was able to generate 5% GDP growth during the first four quarters of expansion. Our current forecast of 2.6% developed world growth for the coming four quarters reflects expectations that this feedback loop will emerge, but be tempered by drags from ongoing adjustments in credit markets and balance sheets.

The powerful improvement in global financial market conditions over the past month confirms that a key element of this positive feedback loop is now materializing. If we are right, labour market indicators will also gradually become part of this dynamic. For next week, we expect US payroll declines to moderate to 275,000 in July. Over the coming months, a move toward stabilization in jobs and hours should become evident in the US as well as in other large economies.

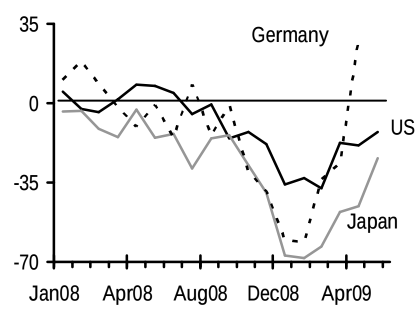
The rising tide hits Europe and LatAm

The key factor making this global recession the worst in generations is that the shocks were global. By the middle of last year, the first phase of the financial crisis, the resulting slide in household wealth, and a surge in commodity prices had already pushed developed economies down a path to

Bank loan officer survey, G4
% balance



Capital goods shipments
%3m, saar (US and Japan through Jun 09)



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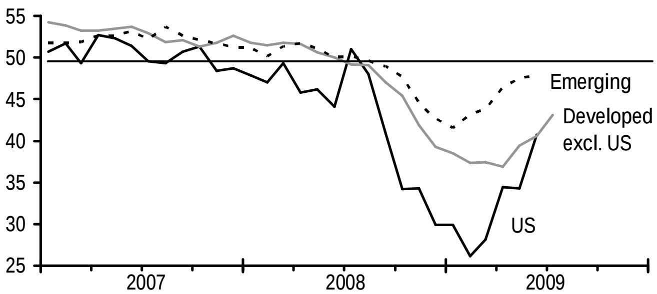
Manufacturing employment PMI employment

DI, sa



recession. Against this backdrop, the sharp intensification of the credit crisis in 4Q08 acted as an accelerant, amplifying the drags already in train and spreading the pain to the emerging economies.

With shocks abating and being offset by unprecedented monetary and fiscal policy support, it is only natural to now expect the recovery to be global. To be sure, Asia is leading the recovery, but all signs are now pointing to a strong and synchronized bounce in economic activity in the current quarter. In addition to a small upward revision to our 3Q09 US growth outlook, we made a number of larger revisions last week to our already above-consensus forecast, highlighting the breadth of the rebound under way.

- In **Asia,** industrial production in the region surged 40% annualized in 2Q09, leading to robust gains in GDP. Most encouraging is that the pace of growth has shown little sign of letting up, pointing to another huge gain in 3Q09. Industrial production in Japan continued to expand rapidly in June. Combining the strong trajectory with the survey forecasts for continued strong growth in July and August, factory output looks likely to post another huge gain this quarter, leading us to revise up our projection for 3Q09 GDP growth from 2.5%%q/q, saar to 3.5%. The manufacturing boom also continued in Korea, where IP surged in June, putting upside risk to our 3Q09 outlook.
- Given the depth of the **Euro area** recession—a 5.8% peak to trough decline in the level of GDP—there are strong forces at work that will deliver growth that is both much stronger than many anticipate (including the ECB) but still fairly modest given how far activity has fallen over the past year. The Euro area recession looks to have ended in the past few weeks, and we now expect GDP growth to average 2.5-3.0%ar between 3Q09 and 1Q10, a 0.75%-point upward revision. Our revised call for above-trend growth in the coming quarters reflects a sharp swing in corporate spending behavior, as the aggressive cutback in capital outlays and the pace of inventory destocking both ease considerably. In addition, net trade is projected to move from being a huge drag to relatively neutral on growth, as exports pick up smartly in response to the rise in global trade, as evidenced already in Asia. Elsewhere in Europe, we are also revising up our Scandinavian projection 1% point annualized in the coming three quarters.
- In **Latin America**, we follow up our recent upward revision to our outlook for Mexico with a large upward revision to GDP growth in Brazil in 2009 and 2010. This week's June IP report will likely confirm that manufacturing activity leaped 15% (q/q,saar) in 2Q09 and is set to expand at a robust pace in 3Q09. Combined with the solid gains in service sector activity, GDP likely grew at 7.0% pace last quarter. Robust consumer spending has been a key driver of the Brazilian resurgence, reflecting resilient labour markets, a recovery in the credit markets, and strong policy stimulus. At the same time, rates of resource utilization will remain depressed, keeping the COPOM on hold through next year.

The BoE sees QE as a friend with benefits

The prospects for a quick return to above-trend growth is forcing central banks to consider how to manage their highly accommodative policy stances. No major central bank is expected to tighten policy this year. Indeed, few are expected to move in advance of a sustained decline in unemployment rates. However, there are some central banks expected to adjust policy early next year—notably the BoE and RBA. Their actions and comments in coming months will provide a valuable guide to timing adjustments ahead.

With its quarterly forecasts in hand, the Bank of England will announce whether to extend QE beyond £125bn next Thursday. We expect the MPC to stay on hold. With policy rates effectively at zero, and QE amounting to 9% of GDP having been announced, the BoE is counseling patience as it anticipates the stimulative effect of its policies to build over time. We maintain that the MPC's view will ultimately be validated. However, this will require considerable change in both financial conditions and the data flow in the coming months. The recovery in output growth already implied by the PMI should gain traction in the official activity data, and headline inflation should rise to 3% in January. Meanwhile, money and credit growth is expected to pick up modestly. While this provides a recipe for an early rate adjustment, the Inflation Report due on August 12 will suggest that, in the MPC's view, the increase in policy rates to nearly 2.5% by the end of 2010 currently discounted by markets is excessive, and would generate a marked undershoot of the inflation target.

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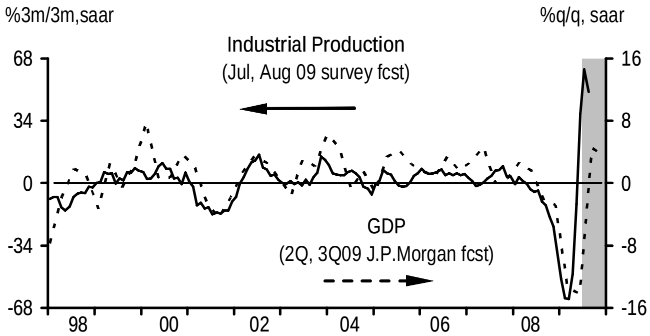
Industrial production and real GDP, Japan



CEEMEA takes an opportunity to ease

While the easing cycle across most of the world is over, the recovery in global risk appetite has created a window of opportunity for many CEEMEA central banks to reduce policy rates. In Turkey, the central bank has already cut rates 850bp since last October and the policy rate currently stands at 8.25%, a historic low. The dovish tone evident in the latest quarterly inflation report showed that the CBRT is concerned about the widening output gap while encouraged by lack of inflation pressures. We now expect the CBRT to cut 125bp by October. In Hungary, with rapidly falling external deficits trimming fx tail risks and economic activity contracting sharply, central banks are now focusing on reviving credit growth. The NBH delivered a surprisingly large 100bp rate cut last week, reversing last autumn's 300bp rate hike to stabilize the currency and is expected to ease another 200bp by early next year. In Romania, we also expect another 200bp of easing.

The central banks of Poland and the Czech Republic are expected to cut once more but are nearing the end of their easing cycles. We expect the CNB to start reversing rate cuts in early 2010, when the economy is expected to rebound and negative real rates may no longer be appropriate. While the National Bank of Poland is likely to take longer before raising rates, we see little scope for further rate cuts beyond this autumn.

India's central bank to stay low for long

In its July quarterly policy review last week, the Reserve Bank of India (RBI) kept policy rates unchanged and assured markets of continued easy liquidity conditions until there are definite and robust signs of recovery or rising inflationary expectations. With resource utilization likely to remain depressed even as economic growth picks up, we do not expect policy rates to be hiked before the second half of 2010. At the same time, the central bank warned that a normalization should be expected without indicating timing. Supply-side inflation pressures, particularly for food prices, have firmed, and there are fears that these could be amplified by the unseasonally dry weather. While this could fuel inflation pressure, at present this has a low probability, given overcapacity in several industries.

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JPMorgan View - Global Markets

Carry joins the recovery trade family

- **Portfolio strategy:** economic uncertainty and market volatility are falling in tandem. This suggests mixing the recovery trade with positive carry positions in bonds, commodities, and fx.
- **Economics:** we raise 3Q DM and world growth above trend.
- **Fixed income:** stay focused on front-end carry.
- **Equities:** earnings expectations are rising in line with prices, preventing overvaluation.
- **Credit:** keep overweight in US HG and overweight banks vs industrials.
- **Fx:** stay short the dollar, focusing on NOK and HUF as the long legs.
- **Alternatives:** Stay short oil on contango, high inventories.

Equities and credit rallied again last week with the economic recovery wave, reaching new cycle highs. We remain long both. US economic data were a bit mixed this week, but globally we are still seeing activity data coming in stronger than hoped for. This week alone, this led our **economists to raise growth forecasts again for almost all developed markets**. We now project a 3.0% growth pace for both the US and the Euro area for 3Q and 3.5% for Japan. UK raised 4Q to 2.5%. Each is way above consensus. We retain a 9.3% 2H growth pace for China, and raise the full-year growth path for Brazil.

Positions and value—always threats to any major rally—do not yet scare us. Earnings expectations are rising along with equity prices and multiples are only in the mid-teens. The 4-month old rally in the equity markets must have created quite a number of tactical longs, but surveys and numerous client discussions still suggest that there remain more end investors with defensive portfolio allocations.

The main fear that is keeping many investors at bay is not so much about the next three to four months. Most accept that massive monetary and fiscal stimulus measures will produce positive prints for world GDP this quarter and next. But it is what happens afterwards—in **2010**—that is keeping a lot of money in cash. It is close to a majority view that consumers and banks will remain in deleveraging mode through next year, as increased saving and capital raising

10-yr Government bond yields

	Current	Sep 09	Dec 09	Mar 10	Jun 10
United States	3.51	3.25	3.00	3.25	3.50
Euro area	3.30	3.30	3.40	3.50	3.60
United Kingdom	3.80	4.10	4.25	4.50	4.55
Japan	1.42	1.50	1.45	1.40	1.30
Foreign exchange					
	Current	Sep 09	Dec 09	Mar 10	Jun 10
EUR/USD	1.43	1.43	1.50	1.47	1.45
USD/JPY	94.7	94	96	100	103
GBP/USD	1.67	1.74	1.85	1.77	1.73
Commodities - quarterly average					
	Current	3Q09	4Q09	1Q10	2Q10
WTI ($/bbl)	68	60	65	65	65
Gold ($/oz)	956	950	975	-	
Copper($/m ton)	5605	5300	5600	-	
Corn ($/Bu)	3.45	3.50	3.65	4.00	4.15

Source: J.P. Morgan, Bloomberg, Datastream.

so far are not enough to repair consumer balance sheets, or cover future bank losses.

We accept that the phantom of the crisis will remain with us for some time and depress long-term growth (see Kasman et al, *Bouncing toward Malaise*, May 7). But this bearish thinking downplays the likelihood that policy stimulus will first produce a robust cyclical swing over the next year and a half. As our Chief Western European Economist David Mackie argues frequently, "Even structurally challenged economies can experience strong cyclical swings." Based on our forecasts, the global cyclical rebound will become more real than the uncertain fears about the longer term. We expect that the concreteness of the rebound will produce a slow, but steady drip of investors reducing the defensiveness of their portfolios. **A rally based on reduced fear is more solid than one based on any exuberance,** which remains far away, with the possible exception of domestic Chinese equities.

Beyond equities and credit, **bonds, currencies, and commodities** similarly still dance to the recovery tune, but are increasingly affected by another force that tends to emerge as economic recoveries settle in: the **carry trade**. Reduced uncertainty and downside risk about the near-term economic outlook have already reduced market volatility. The low-for-long assurances of central banks and improved control they appear to have over money market conditions also help to lower uncertainty. We see this carry trade, or searching for yield, clearly in the bond markets, which were able to rally last week, despite strong US supply and a rally in equities. We continue to like earning carry at the shorter

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ends of the US and Euro bond curves.

Fixed income

Government bonds rallied last week, despite the continued uptrend in equities. The massive tightening in credit spreads is inducing a bid for government paper as that tightening renders government bond carry trades increasingly attractive relative to credit carry trades. While this dynamic could push government yields lower still, we remain wary of heavy upcoming supply, and thus remain **neutral at the longer end of curves.**

Instead, **we remain long at the short end of curves (ex UK)** on a view that low capacity utilization rates, and hence low near-term inflation, will allow the Fed, ECB, and BoJ to keep policy rates low for long. The exception is in the UK, where inflation pressures will likely force policy rates higher in early 2010. **German Bunds outperformed US Treasuries** last week by 7bp, bringing ytd outperformance to 100bp. Expect this trend to continue as issuance needs in the US remain gargantuan, while 3Q net issuance in Germany should be negative. **Stay long Bunds vs. 10-year USTs**.

Equities

Stocks continued to gain, having broken their ranges already two weeks ago. The ytd return prints are starting to look impressive, and are putting pressure on those investors who have so far sat out the rally. **Fear of missing out on this rally** is now joining continued upside surprises on earnings and economic data as the drivers of the rally in 2H.

US 2Q earnings continue to come in stronger than analysts had predicted. With almost two thirds of the S&P500 having reported, 75% of companies are beating earnings estimates, and only 16% are missing. On average, 2Q EPS is so far coming in 17% above expectation, a meaningful beat. The bottom up estimate for 2Q EPS, filled in with recent announcements, has moved from $13.85 to $15.26. Full year 2009 bottom up earnings forecasts are now just under $60, making the almost 1,000 level of the index an acceptable 16.5 multiple.

On the downside, US earnings surprises are still coming mostly from **cost control,** with overall top-line revenues coming in close to market expectations. We elect to interpret this positively, as an indication that cost cutting is nearly its end, positioning future earnings growth with a good starting point. We continue to expect that S&P500 EPS will next year return to near its long-term trend.

We remain overweight small caps in the US, which so far have merely kept pace with large caps. Small cap indices contain many regional banks, and have been the favourite shorts for bears. We do see financials generally outperforming and thus add this to the higher beta and more cyclical nature of the Russell 2000 to stay overweight.

Credit

We remain **overweight US HG** despite the powerful rally, as spreads remain wide by historical standards. The reduced spread does make the market a bit less attractive, but the other drivers of the rally in credit—steady flows from cash to bonds and improving credit quality—remain in place. In addition, the effect of reduced spread is offset by a dramatic drop in net new issuance. We stay with our forecast, which is coming through in July already, that net new issuance of corporate bonds in the world will fall to near zero in 2H. Also, the improvement in credit metrics, mostly from cost savings in 2Q, is likely to continue in 3Q as revenues increase alongside an overall economic rebound.

Within HG, we recommend **overweighting Banks vs Industrials** as spreads are higher on bank paper of the same rating class. Although some investors are restricted by concentration limits, reducing their ability to buy more financials, the relative cheapness of bank paper will not persist, in our view, as other investors will jump in.

Alternatives

Near term, we prefer to stay **short oil** to benefit from contango and high stocks. We may have to wait until 2011 to see oil inventories return to normal levels. Gold will likely stay range bound. We see less upside now as the safe haven demand is weakening. Inflation fears remain the key support for gold, as consumer interest is weak at current levels. The medium-term outlook remains bullish for commodities. We are **long base metals**, as restocking activity is spreading to the western world.

Hedge funds will likely finish another month in positive territory, as daily indices show gains. **Convertible arb** and **relative value** continue to outperform. These styles remain our preferred ones, but the upside is now more limited as most of the excessive premia seen earlier this year have by now dissipated. On the positive side, convertible bond supply will likely stay strong. On the regulatory front, it is now clear that the European directive will suffer significant changes to address some of the polemic points, such as the potential barriers on non-European funds.

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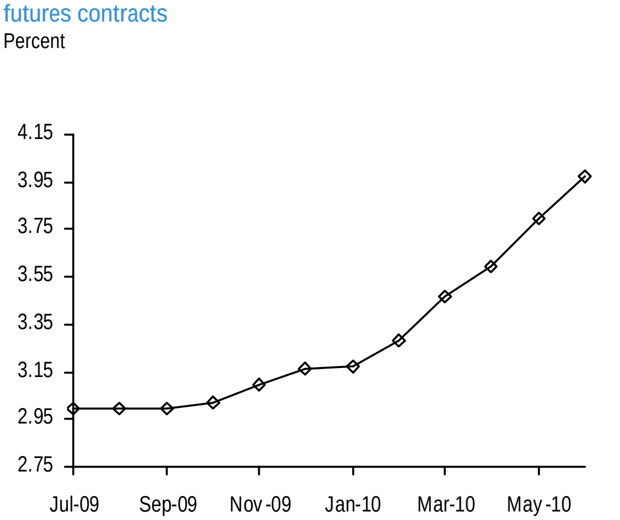
Markets - Australia and New Zealand

Below is a summary of *The Antipodean Strategist*, published weekly. The full version can be found on Morgan Markets.

Australia and New Zealand

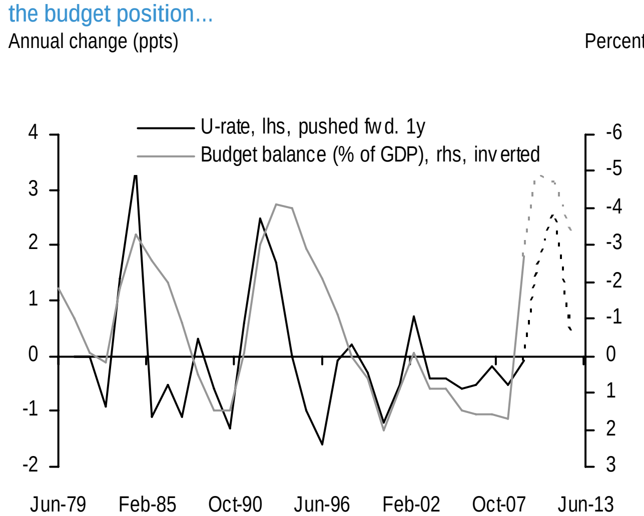
- The RBA Governor delivered a reasonably upbeat assessment of economic conditions last week. In a macroeconomic sense, the main challenge for the RBA at present is whether or not the current setting of policy is appropriate in order to sustain economic growth that is consistent with the inflation target in the medium term.
- And if, as the Governor suggested, the current downturn is not one of the worst post-WWII, then it doesn't really make sense to have mortgage rates at generational lows. While removal of the government guarantee for bank funding could help resolve this anomaly, there is a strong probability the burden of policy adjustment may fall squarely on the RBA's shoulders.
- From here, we think trading strategies are highly dependent on the timing of the tightening cycle. For investors who believe that the RBA could deliver a rate hike by year end, we favour flatter front end spreads (2y1y vs. 1y or bills vs. 3-years) and a narrower 3s10s bond/swap box spread. Investors who believe that the RBA will bide its time should buy the very front end (Dec-09 IBs, Jun-10 bills) and/or remain outright short in the 3-year sector.
- One implication of a stronger economic environment is that the Government's budget position should improve. This has important implications for bond supply projections. We estimate that bonds on issue as at mid-2013 could be $125bn (almost a full $100bn below our estimate based on current J.P. Morgan forecasts).
- This has significance for the bond market; at the very minimum some of the supply premium should be taken out of current market pricing. Cash bonds should not be trading as cheap to the bond futures as they are at present. Swap spreads may not narrow as much as expected, but we still expect 10-year spreads to narrow more than 3-year spreads.
- One of the most striking aspects of the last week was the divergence in monetary policy outlooks from the antipodean central banks. The RBA were noticeably more upbeat than the RBNZ; indeed, the RBNZ issued one of the more dovish statements that we have seen in sometime. Concern about the level of the NZD was the driving force behind the RBNZ's assessment—they explicitly noted that the strong currency was threatening the sustainability of future growth and brought with it "*additional economic risks*". Moreover, they noted that "*…The forecast recovery is based on a further easing in financial conditions. If this easing does not occur, the forecast recovery could be put at risk. In these circumstances we would reassess policy settings.*"

Cash rate expectations in Australia, using 30-day interbank cash futures contracts



Source: J.P. Morgan and Bloomberg

Movements in the unemployment rate are an important influence on the budget position...



Source: J.P. Morgan, Commonwealth Budget Papers and ABS

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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	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	1Q09	2Q09	4Q09	4Q10
The Americas														
United States	0.4 ↓	-2.6 ↓	2.9 ↑	-5.4 ↑	-6.4 ↓	-1.0	3.0 ↑	2.0	3.0	4.0	-0.2	-0.9	1.1	0.7
Canada	0.4	-2.3	2.4 ↑	-3.7	-5.4	-3.5 ↓	2.0 ↑	2.0	3.0	3.0	1.2	0.0	1.2	2.3
Latin America	3.8	-3.1 ↑	4.1 ↑	-8.9	-10.1	-0.1 ↑	8.0 ↑	3.4 ↑	4.3 ↑	4.4 ↑	7.5	6.8	5.7 ↓	6.5
Argentina	6.8	-3.0	2.0	-2.0	0.2	-6.0	0.0	-4.0	6.0	6.0	6.6	7.0	6.0	10.2
Brazil	5.1	-0.4 ↑	4.5 ↑	-13.8	-3.3	7.0 ↑	5.5 ↑	4.0 ↑	4.0 ↑	5.0 ↑	5.8	5.2	4.3	4.5
Chile	3.2	-1.5	3.2	-7.9	-2.5	0.0	3.0	4.0	4.0	3.5	5.6	2.0	-0.5 ↓	3.2
Colombia	2.5	-0.5	3.0	-5.9	0.9	0.0	0.8	2.1	3.5	4.3	6.6	4.6	4.1	4.5
Ecuador	6.5	-2.0	0.5	-1.0	-6.3	-4.0	-4.0	0.0	1.5	2.5	7.9	5.5	4.8	4.1
Mexico	1.3	-6.5	5.0	-9.8	-21.5	-4.0	15.5	5.0	5.0	4.0	6.2	6.0	4.2	3.4
Peru	9.8	1.7	5.4	-1.2	-6.2	-0.5	13.0	9.0	3.0	4.1	5.6	3.5	1.5	2.0
Venezuela	4.8	-2.5	1.5	1.4	-9.3	-4.0	-2.0	0.0	2.0	3.5	29.5	28.4	31.5	37.4
Asia/Pacific														
Japan	-0.7	-5.4 ↑	2.5 ↑	-13.5	-14.2	4.5	3.5 ↑	3.5	3.0	-0.5	-0.1	-1.0 ↓	-1.3	-0.8
Australia	2.3	0.3	1.7	-2.2	1.5	2.0	-2.2	1.2	2.9	1.6	2.5	1.4	1.5	2.8
New Zealand	0.2	-2.2	2.3	-3.9	-3.9	-1.2	-0.4	2.5	3.4	2.7	3.0	1.5	1.1	2.3
Asia ex. Japan	5.8	3.8	6.8	-5.2	2.7	11.0 ↓	7.4	6.6	6.4	7.0	2.6	1.2	2.0	3.0
China	9.0	8.4	9.0	1.9	8.3	14.9	9.5	9.0	8.7	8.7	-0.6	-1.5	1.7	1.9
Hong Kong	2.4	-4.0	4.8	-7.4	-16.1	6.8	6.6	5.0	4.5	4.3	1.7	-0.1	-0.9	3.0
India	6.1	6.2	7.2	2.3	6.4	3.9	6.5	7.5	8.0	9.4	9.4	7.5	4.2	4.6
Indonesia	6.1	3.5	4.5	1.5	4.8	3.0	3.0	2.0	5.0	6.0	8.6	5.6	3.5	6.2
Korea	2.2	-1.1	3.9	-18.8	0.5	9.7	4.0	3.5	3.5	3.5	3.9	2.8	2.6	3.5
Malaysia	4.6	-3.0	4.4	-10.1	-15.1	10.0	6.1	4.5	1.6	4.9	3.7	1.5	0.3	2.4
Philippines	3.8	1.3	5.0	1.1	-8.9	8.0	6.0	6.0	5.0	4.0	6.9	4.7	3.0	3.7
Singapore	1.1	-2.8	4.9	-16.4	-14.6	20.4	7.8	2.0	0.4	4.1	2.1	-0.4	-0.7	3.6
Taiwan	0.1	-3.8	5.0	-23.8	-3.4	12.8	8.0	5.0	4.3	3.5	0.0	-0.6	0.3	2.1
Thailand	2.6	-3.1 ↓	6.1	-22.1	-7.3	10.0 ↓	7.8	4.9	3.2	8.2	-0.2	-2.8 ↓	0.5	2.4
Africa														
South Africa	3.1	-2.0	2.5	-1.8	-6.4	-2.9	1.0	2.2	3.6	4.1	8.4	7.8	6.2	4.2
Europe														
Euro area	0.6	-4.4 ↑	2.1 ↑	-6.9	-9.7	-4.0	2.5 ↑	2.5 ↑	3.0 ↑	2.0	1.0	0.2	0.6	1.1
Germany	1.0	-5.9 ↓	2.8 ↑	-8.6	-14.4	-4.0 ↓	3.5 ↑	4.0 ↑	4.0 ↑	2.0	0.8	0.1	0.3	0.3
France	0.3	-2.4 ↑	2.3 ↑	-5.7	-4.8	-2.0 ↑	2.5 ↑	2.5 ↑	3.0 ↑	2.5 ↑	0.7	-0.1	0.6	0.7
Italy	-1.0	-5.3 ↑	1.3 ↑	-8.3	-10.1	-4.0 ↑	1.0	1.0 ↓	2.0	2.0 ↑	1.4	1.0	1.0	1.0
Norway	2.5	-1.1 ↑	2.5 ↑	-3.0	-3.9	-1.0	2.5 ↑	3.0 ↑	3.0 ↑	2.5	2.4	3.1 ↑	1.4 ↑	0.4
Sweden	-0.4	-4.3 ↑	3.1 ↑	-18.4 ↑	-3.5 ↑	-0.1 ↑	3.0 ↑	4.0 ↑	4.0 ↑	2.5	0.8	-0.4	0.1 ↑	0.1
Switzerland	1.6	-1.4	1.9	-2.2	-3.2	-2.0	1.8	2.3	2.5	2.0	0.0	-0.6	0.1	0.4
United Kingdom	0.7	-4.4 ↑	1.9 ↑	-7.0	-9.3	-3.2	1.0	2.5 ↑	2.0	2.5	3.0	2.1	1.5	2.1
Emerging Europe	4.1	-5.2 ↑	3.0 ↑	-7.7	-17.1	-1.2 ↑	3.5 ↑	3.9 ↑	3.0 ↑	2.9	8.7	7.6 ↓	7.0	6.0 ↑
Bulgaria	6.1	-5.0	-1.5	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	3.0	-3.0	2.0	-6.8	-12.9	-1.0	2.5	3.0	1.5	2.5	2.1	1.5	1.3	3.6
Hungary	0.6	-6.0	-0.5	-7.2	-9.6	-4.5	-3.2	-1.0	0.0	1.0	3.0	3.7	7.2	2.4
Poland	4.9	0.0 ↑	2.2 ↑	0.0	1.6	-3.0 ↑	0.5 ↑	1.0 ↑	3.5 ↑	3.0	3.3	3.7 ↓	3.0	2.4 ↑
Romania	7.1	-4.0	1.5	...	...	...	...	...	...	...	6.8	6.3	7.0	6.5
Russia	5.6	-8.5	4.5	-11.6	-30.3	0.0	6.5	6.5	4.0	3.5	13.9	12.5	11.0	9.2
Turkey	1.1	-4.7	3.0	...	...	...	...	...	...	...	8.4	5.7	5.0	4.9
Global	1.3 ↓	-2.8 ↓	3.1 ↑	-7.0 ↑	-7.5 ↓	0.3	3.5 ↑	3.0 ↑	3.4 ↑	3.2 ↑	1.4	0.6	1.3	1.5
Developed markets	0.4 ↓	-3.6 ↓	2.5 ↑	-7.2 ↑	-8.5 ↓	-1.2	2.6 ↑	2.4 ↑	2.9 ↑	2.5	0.5	-0.3	0.6	0.8
Emerging markets	4.9	0.4	5.4 ↑	-6.4	-3.5	6.1 ↑	6.9 ↑	5.3 ↑	5.4 ↑	5.7 ↑	5.0	3.8	3.9	4.4

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Global Central Bank Watch

	Official interest rate	Current	Change from Aug '07 (bp)	Last change	Next meeting	Forecast next change	Sep 09	Dec 09	Mar 10	Jun 10	Dec 10
Global	GDP-weighted average	1.35	-336				1.32	1.32	1.33	1.36	1.44
excluding US	GDP-weighted average	1.93	-251				1.89	1.88	1.90	1.94	2.06
Developed	GDP-weighted average	0.48	-366				0.48	0.48	0.50	0.52	0.57
Emerging	GDP-weighted average	4.80	-220				4.67	4.63	4.65	4.68	4.89
Latin America	GDP-weighted average	5.81	-300				5.79	5.79	5.79	5.82	5.96
CEEMEA	GDP-weighted average	5.88	-113				5.32	5.17	5.25	5.36	5.48
EM Asia	GDP-weighted average	4.01	-231				4.00	4.00	4.00	4.00	4.27
The Americas	GDP-weighted average	0.76	-483				0.76	0.76	0.76	0.76	0.77
United States	Federal funds rate	0.125	-512.5	16 Dec 08 (-87.5bp)	12 Aug 09	on hold	0.125	0.125	0.125	0.125	0.125
Canada	Overnight funding rate	0.25	-425	21 Apr 09 (-25bp)	10 Sep 09	on hold	0.25	0.25	0.25	0.25	0.25
Brazil	SELIC overnight rate	8.75	-275	22 Jul 09 (-50bp)	2 Sep 09	on hold	8.75	8.75	8.75	8.75	8.75
Mexico	Repo rate	4.50	-275	17 Jul 09 (-25bp)	21 Aug 09	on hold	4.50	4.50	4.50	4.50	4.50
Chile	Discount rate	0.50	-500	9 Jul 09 (-25bp)	13 Aug 09	on hold	0.50	0.50	0.50	1.00	3.50
Colombia	Repo rate	4.50	-475	19 Jun 09 (-50bp)	28 Aug 09	on hold	4.50	4.50	4.50	4.50	4.50
Peru	Reference rate	2.00	-275	9 Jul 09 (-100bp)	6 Aug 09	6 Aug 09 (-50bp)	1.50	1.50	1.50	1.50	1.50
Europe/Africa	GDP-weighted average	1.49	-310				1.42	1.41	1.45	1.50	1.59
Euro area	Refi rate	1.00	-300	7 May 09 (-25bp)	6 Aug 09	on hold	1.00	1.00	1.00	1.00	1.00
United Kingdom	Repo rate	0.50	-525	5 Mar 09 (-50bp)	6 Aug 09	1Q 10 (+25bp)	0.50	0.50	0.75	1.00	1.50
Sweden	Repo rate	0.25	-325	2 Jul 09 (-25bp)	3 Sep 09	on hold	0.25	0.25	0.25	0.25	0.25
Norway	Deposit rate	1.25	-350	17 Jun 09 (-25bp)	12 Aug 09	on hold	1.25	1.25	1.25	1.25	1.25
Czech Republic	2-week repo rate	1.50	-175	7 May 09 (-25bp)	6 Aug 09	6 Aug 09 (-25bp)	1.25	1.25	1.75	2.50	3.50
Hungary	2-week deposit rate	8.50	75	**27 Jul 09 (-100bp)**	24 Aug 09	**24 Aug 09 (-50bp)**	7.50	7.00	6.50	6.50	6.50
Israel	Base rate	0.50	-350	23 Mar 09 (-25bp)	27 Aug 09	4Q 09 (+50bp)	0.50	1.00	2.00	3.00	4.00
Poland	7-day intervention rate	3.50	-125	24 Jun 09 (-25bp)	27 Aug 09	30 Sep 09 (-25bp)	3.25	3.25	3.25	3.25	3.25
Romania	Base rate	9.00	200	30 Jun 09 (-50bp)	4 Aug 09	4 Aug 09 (-50bp)	8.00	8.00	8.00	7.50	7.00
Russia	1-week deposit rate	6.75	350	4 Jun 09 (-50bp)	3Q 09	3Q 09 (-50bp)	6.25	5.75	5.75	5.75	5.75
South Africa	Repo rate	7.50	-250	28 May 09 (-100bp)	13 Aug 09	on hold	7.50	7.50	7.50	7.50	7.50
Switzerland	3-month Swiss Libor	0.25	-225	12 Mar 09 (-25bp)	17 Sep 09	on hold	0.25	0.25	0.25	0.25	0.25
Turkey	Overnight borrowing rate	8.25	-925	16 Jul 09 (-50bp)	18 Aug 09	**18 Aug 09 (-50bp)**	7.00	7.00	7.00	7.00	7.00
Asia/Pacific	GDP-weighted average	2.05	-149				2.05	2.05	2.05	2.06	2.25
Australia	Cash rate	3.00	-350	7 Apr 09 (-25bp)	4 Aug 09	1 Jun 10 (+25bp)	3.00	3.00	3.00	3.25	4.25
New Zealand	Cash rate	2.50	-575	30 Apr 09 (-50bp)	10 Sep 09	8 Jul 10 (+25bp)	2.50	2.50	2.50	2.50	3.50
Japan	Overnight call rate	0.10	-40	19 Dec 08 (-20bp)	11 Aug 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)	13 Aug 09	on hold	0.50	0.50	0.50	0.50	0.50
China	1-year working capital	5.31	-171	22 Dec 08 (-27bp)	2Q 09	4Q 10 (+27bp)	5.31	5.31	5.31	5.31	5.58
Korea	Base rate	2.00	-300	12 Feb 09 (-50bp)	11 Aug 09	on hold	2.00	2.00	2.00	2.00	2.50
Indonesia	BI rate	6.75	-150	3 Jul 09 (-25bp)	5 Aug 09	**5 Aug 09 (-25bp)**	6.50	6.50	6.50	6.50	6.50
India	Repo rate	4.75	-300	21 Apr 09 (-25bp)	27 Oct 09	**3Q 10 (+25bp)**	4.75	4.75	4.75	4.75	5.25
Malaysia	Overnight policy rate	2.00	-150	24 Feb 09 (-50bp)	25 Aug 09	on hold	2.00	2.00	2.00	2.00	2.00
Philippines	Reverse repo rate	4.00	-200	9 Jul 09 (-25bp)	20 Aug 09	on hold	4.00	4.00	4.00	4.00	4.00
Thailand	1-day repo rate	1.25	-200	8 Apr 09 (-25bp)	26 Aug 09	on hold	1.25	1.25	1.25	1.25	1.25
Taiwan	Official discount rate	1.25	-188	18 Feb 09 (-25bp)	3Q 09	on hold	1.25	1.25	1.25	1.25	1.25

Bold denotes move since last GDW and forecast changes. Underline denotes policy meeting during upcoming week.

Economic forecasts - Australia

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	0.3	1.7	1.4	0.9	-2.2	1.5	2.0	-2.2	1.2	2.9	1.6	2.9	3.6
Private consumption	2.2	0.5	0.6	-0.5	0.3	1.2	2.3	0.0	-2.4	-0.8	1.2	1.6	2.4	2.0
Construction investment	5.2	-3.2	2.6	1.7	6.5	-0.5	-11.5	-6.0	0.0	3.0	3.3	2.0	4.9	9.8
Equipment investment	15.7	-15.9	-9.7	36.8	1.4	-1.7	-33.1	-28.2	-19.3	-4.1	-10.0	-12.0	0.0	8.6
Public investment	12.0	-0.8	9.6	3.7	18.9	-11.1	-9.5	2.4	5.4	7.1	9.7	11.9	14.4	15.3
Government consumption	3.7	1.4	4.2	5.3	2.3	1.0	1.4	0.1	0.5	3.7	5.6	6.0	5.0	4.7
Exports of goods & services	3.9	-2.5	0.3	10.5	-3.4	-3.3	11.1	-16.8	-7.8	-3.9	2.0	6.1	8.2	10.4
Imports of goods & services	10.3	-11.3	0.5	15.7	2.6	-27.0	-25.2	4.1	-2.0	-7.8	-3.9	4.1	8.2	21.6
Contributions to GDP growth:														
Domestic final sales	4.4	-1.7	1.6	4.9	2.5	-3.6	-7.1	2.5	-2.5	0.7	1.9	2.0	3.8	4.8
Inventories	-0.6	-0.2	0.1	-1.9	-0.2	-5.4	0.1	4.2	1.5	-0.4	-0.3	-0.7	-0.7	1.1
Net trade	-1.5	2.2	0.0	-1.5	-1.4	7.1	9.0	-4.6	-1.2	0.9	1.2	0.3	-0.1	-2.2
GDP deflator (%oya)	6.7	2.0	1.8	6.7	8.5	7.5	5.1	2.5	0.3	0.3	1.8	1.7	1.7	2.0
Consumer prices (%oya)	4.4	1.5	2.4	4.5	5.0	3.7	2.5	1.4	0.7	1.5	2.1	2.3	2.6	2.8
Producer prices (%oya)	8.3	-3.5	0.7	8.7	10.9	6.7	-1.0	-4.4	-5.4	-2.8	1.1	0.5	0.4	1.0
Trade balance (A$ bil, sa)	-4.2	-13.3	-25.2	-2.1	1.4	4.4	4.6	-4.6	-6.3	-7.1	-7.3	-6.2	-5.9	-5.8
Current account (A$ bil, sa)	-67.0	-59.6	-74.2	-14.8	-9.7	-6.4	-4.6	-16.8	-18.7	-19.6	-19.8	-19.2	-17.9	-17.3
as % of GDP	-6.2	-4.9	-5.9	-5.0	-3.2	-2.1	-1.5	-5.5	-6.2	-6.4	-6.4	-6.2	-5.7	-5.4
3m eurodeposit rate (%)*	6.0	3.6	4.9	7.8	7.0	4.1	3.1	3.2	4.1	4.0	4.6	4.7	5.0	5.1
10-year bond yield (%)*	5.6	5.1	5.7	6.5	5.4	4.0	4.4	5.4	5.4	5.4	5.8	5.6	5.7	5.7
US$/A$*	0.75	0.77	0.86	0.74	0.77	0.65	0.68	0.75	0.82	0.83	0.84	0.85	0.86	0.87
Commonwealth budget (FY, A$ bil)	13.5	-35.0	-68.0											
as % of GDP	1.1	-2.9	-5.4											
Unemployment rate	4.2	6.4	8.7	4.2	4.3	4.5	5.3	5.7	6.9	7.7	8.3	8.7	8.9	9.0
Industrial production	2.0	-7.4	3.5	-0.1	-4.9	-17.3	-12.7	-2.0	1.0	3.0	6.0	4.0	2.0	0.0

*All financial variables are period averages

Australia - summary of main macro views

- Australia is in **recession** even though we avoided back-to-back falls in GDP—GDP probably will fall in 3Q in the absence of new fiscal stimulus, and as other support (i.e. the investment allowance) is wound back.
- We expect a **sustained fall in business investment**, particularly mining, which will force down employment.
- With **labour force participation falling** only slowly, the jobless rate will soar to 9% by end-2010. The sustained fall in hours worked is a leading indicator of firms trimming employment.
- On **housing**, the expanded first home owners' grant has sucked forward buyers from 2010. The mini-boom will end in tears in 2010 as the jobless rate rises and house prices fall.
- The still **fragile consumer** is yet to be fully tested—households have been on financial "life support" from the RBA and the government's fiscal support.
- **Export volumes** have held up owing mainly to firm demand from Asia, but the terms of trade is tumbling.
- The **RBA** is comfortably on hold, but the next move in the official cash rate will be up in the middle of 2010, even though the jobless rate will not yet have peaked.
- Having front-loaded the **policy support**, the government is unlikely to deliver more significant fiscal stimulus.

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Economic forecasts - New Zealand

New Zealand: economic projections *percentage change over previous period, seas. 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)	0.2	-2.2	2.3	-0.9	-2.0	-3.9	-3.9	-1.2	-0.4	2.5	3.4	2.7	3.2	3.7
Private consumption	0.1	-1.6	1.7	-0.9	-0.5	-1.0	-5.3	-3.1	2.2	5.2	1.0	0.5	1.2	2.5
Fixed Investment	-3.7	-19.7	-1.1	5.6	-26.2	-22.5	-27.0	-19.7	-10.6	-4.6	2.5	4.6	5.8	7.7
Residential construction	-17.1	-18.2	3.6	-27.2	-25.6	-45.8	-1.2	-8.0	-4.0	2.0	4.8	7.2	10.0	8.0
Other fixed investment	-0.3	-20.1	-2.1	14.7	-26	-16.7	-31.2	-22.0	-12.0	-6.0	2.0	4.0	4.8	7.6
Inventory change (NZ$ bil, saar)	1.4	-0.2	0.4	0.3	0.5	0.2	-0.2	0.0	0.0	0.1	0.1	0.1	0.1	0.1
Government spending	3.9	2.2	1.8	1.6	1.6	6.2	1.4	0.8	1.2	2.0	1.6	2.0	2.8	1.2
Exports of goods & services	-1.5	-3.5	7.2	0.4	-11.5	-11.9	2.3	-1.1	-2.5	5.2	10.0	15.0	7.0	9.0
Imports of goods & services	2.5	-17.0	3.4	13.4	-24.4	-23.6	-30.2	-10.0	-1.0	6.5	4.0	5.0	5.0	8.0
Contributions to GDP growth:														
Domestic final sales	1.3	-6.4	0.8	5.0	-11.0	-6.1	-11.6	-6.3	-0.8	2.6	1.4	-0.4	2.4	3.3
Inventories	0.4	-1.2	0.5	-0.9	2.4	-3.7	-4.8	2.1	0.9	0.4	0.3	0.2	0.2	0.1
Net trade	-1.4	5.4	1.1	-4.8	7.3	6.1	13.7	3.1	-0.5	-0.5	1.7	2.9	0.6	0.3
GDP deflator (%oya)	3.6	3.7	3.0	3.7	2.1	2.5	2.4	3.9	5.4	3.1	2.8	3.0	3.1	3.1
Consumer prices	4.0	1.1	1.7	6.7	6.2	-1.8	1.1	0.7	0.7	2.0	1.3	1.7	2.4	3.8
%oya	4.0	1.4	1.7	4.0	5.1	3.4	3.0	1.5	0.2	1.1	1.2	1.4	1.8	2.3
Trade balance (NZ$ bil, sa)	-2.2	-2.6	1.5	-1.1	-0.8	-0.1	0.9	-0.5	-1.3	-1.7	-1.3	0.1	1.3	1.4
Current account (NZ$ bil, sa)	-16.0	-13.5	-17.4	-4.7	-4.0	-3.7	-4.1	-2.7	-3.1	-3.6	-4.4	-5.2	-4.4	-3.4
as % of GDP	-9.0	-7.6	-7.1	-10.5	-9.1	-8.3	-6.0	-6.8	-8.0	-9.6	-9.5	-7.1	-5.4	-6.5
Yield on 90-day bank bill (%)*	7.9	2.8	3.1	8.8	8.2	6.0	2.8	2.8	2.8	2.8	3.0	3.1	3.1	3.1
10-year bond yield (%)*	6.0	5.0	5.8	6.5	5.9	5.3	4.1	5.4	5.4	5.1	5.5	6.0	6.0	6.0
US$/NZ$*	0.71	0.60	0.66	0.78	0.71	0.58	0.51	0.64	0.62	0.64	0.65	0.66	0.67	0.67
Commonwealth budget (NZ$ bil)	-3.0	-8.9	-9.8											
as % of GDP	-1.7	-4.9	-5.1											
Unemployment rate	4.2	6.1	7.6	4.0	4.3	4.7	5.0	5.8	6.5	7.1	7.5	7.7	7.8	7.5

*All financial variables are period averages

New Zealand - summary of main macro views

- The New Zealand economy was in a homegrown **recession** before the worst of the international troubles unfolded.
- The economy already has contracted for five straight quarters. We forecast another two quarters of negative GDP growth, with mild positive growth forecast for 4Q.
- **Business confidence** recently has improved, though firms' investment will remain a drag on GDP growth; this, of course, has negative implications for the employment outlook.
- The prolonged decline in **private consumption** is set to continue for some time yet. The recession has altered consumer behaviour, leading consumers toward increased saving rather than spending.
- **Increased anxiety about job security** probably is the strongest headwind facing consumers. We expect the unemployment rate to peak close to 8% in 2010.
- The **RBNZ** has delivered 575bp of policy easing since mid-2008. We believe that the OCR, currently at 2.5%, is the terminal cash rate in this cycle, and the RBNZ will begin tightening policy in mid-2010.

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Australia and New Zealand economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
3 Aug Australia: ANZ job ads (11:30 am) Jul Retail sales (11:30am) Jun 0.9 %m/m,sa	4 Aug Australia: House price index (11:30 am) 2Q 1.0 %q/q RBA cash target (2:30 pm) Aug no change expected New Zealand: Private sector labor cost index (10:45 am) 2Q 0.6 %q/q,sa ANZ comm. Price (3:00 pm) Jul	5 Aug Australia: Trade balance (11:30 am) Jun -750 A $mn,sa	6 Aug Australia: Unemployment rate (11:30 am) Jul 6.2 %,sa New Zealand: Unemployment rate (10:45 am) 2Q 5.5 %,sa	7 Aug
10 Aug Australia: Housing finance approvals (11:00 am) Jun New Zealand: QV house prices Jul	11 Aug Australia: NAB bus. Confidence (11:30 am) Jul	12 Aug Australia: Westpac consumer confidence (10:30 am) Aug Labor price index (11:30 am) 2Q	13 Aug Australia: Consumer inflation expectation (11:00 am) Aug New Zealand: Business NZ PMI (10:30am) Jul	14 Aug New Zealand: Retail sales (10:45 am) Jun
17 Aug	18 Aug	19 Aug Australia: Westpac leading index (10:30 am) Jun New Zealand: PPI (10:45 pm) 2Q	20 Aug	21 Aug New Zealand: Visitor arrivals (10:45 am) Jul Credit card spending (3:00 pm) Jul
24 Aug Australia: New motor vehicles sale (11.30 am) Jul	25 Aug	26 Aug	27 Aug Australia: Private capital expenditure (11:30 am) 2Q New Zealand: Trade balance (10:45 am) Jul	28 Aug New Zealand: Building permits (10:45 am) Jul

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Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
3 - 7 August	**3 August**	**4 August**	**5 August**	**6 August**	**7 August**
Brazil • Auto report (Jul) China • Mfg PMI (Jul) Japan • Cabinet Office private consumption index (Jun) Korea • Trade balance (Jul) United Kingdom • Halifax HPI (Jul)	Australia: Retail sales (Jun) Brazil: IP (Jun) Euro area • PMI mfg final (Jul) Germany • Retail sales (Jun) Japan • Auto regs (Jul) • Nominal wages (Jun) Korea • CPI (Jul) Turkey: CPI (Jul) United Kingdom • PMI mfg (Jul) United States • Construct spend (Jun) • ISM mfg, LV sales (Jul)	Australia • RBA meeting Romania • NBR meeting Singapore • PMI mfg (Jul) United States • Pending homes (Jun) • Personal income (Jun)	Euro area • PMI services final (Jul) • Retail sales (Jun) Indonesia • BI meeting Japan • PMI services (Jul) Taiwan • CPI (Jul) United Kingdom • PMI services (Jul) United States • ADP employment (Jul) • Factory orders (Jun) • ISM nonmfg (Jul)	Czech Republic • CNB meeting Euro area • ECB meeting Germany • Mfg orders (Jun) Peru • BCRP meeting United Kingdom • New car regs (Jul) • MPC meeting	Brazil • IPCA (Jul) Canada • Employment (Jul) • Ivey PMI (Jul) Germany • Foreign trade (Jun) • IP (Jun) Mexico • CPI (Jul) Taiwan • Trade balance (Jul) United States • Consumer credit (Jun) • Employment (Jul)
10 - 14 August	**10 August**	**11 August**	**12 August**	**13 August**	**14 August**
China • Money supply (Jul)	China • CPI (Jul) Japan • Econ watcher survey (Jul) • Machinery orders (Jun) Mexico • Auto report (Jul) Norway • CPI (Jul)	China • FAI (Jul) • Trade balance (Jul) Germany • CPI (Jul) Japan • Consumer sent (Jul) • BoJ meeting Korea: BoK meeting Mexico: IP (Jun) South Africa • Mfg production Sweden • CPI (Jul) United States • Prod and costs prelim (2Q) • Wholesale trade (Jun)	China • IP (Jul) • Retail sales (Jul) Euro area • IP (Jun) France: CPI (Jul) Japan • IP final (Jun) Norway • Norges bank meeting South Africa • SARB meeting United Kingdom • Labor mkt report (Jul) United States • International trade (Jun) • FOMC meeting	Brazil • Retail sales (Jun) Chile • BCCh meeting Euro area • GDP flash (2Q) Poland • CPI (Jul) United States • Business inventories (Jul) • Import prices (Jul) • Retail sales (Jul)	Euro area • HICP final (Jul) Japan • Reuters Tankan (Aug) • Tertiary sect activity (Jun) • BoJ minutes United States • Consumer sent (Aug) • CPI (Jul) • IP (Jul)

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