J.P.Morgan

Economic Research
April 30, 2010

Global Data Watch

- **Economic recovery gaining power even as mounting fiscal stress raises anxiety in developed world**
- **Multi-year package for Greece will relieve pressure but still leave on table worries about solvency and contagion**
- **Asian growth continues to surprise on the upside, compelling another forecast upgrade in Japan**
- **Brazil's COPOM kicks off its tightening cycle with a 75bp hike; others reluctant to follow**

Strong growth, slow and painful healing

Even as the global recovery gains breadth and momentum, European fiscal developments are a reminder that the process of healing from the severe global recession will be a slow and painful one. Initial soundings on 1Q GDP from the US and Emerging Asia haave been strong, consistent with our view that global GDP rose at a near 4% annualized pace in 1Q10. Given the impressive advance in the higher-frequency indicators, the economy may do even better in the current quarter. The available business surveys rose impressively in April and stand far above their 1Q averages, a finding that should be confirmed by our global PMI next week. Notably, the surprises are coming from across the globe and include both manufacturing and services, and small as well as large businesses. Consumer confidence also is up, reflecting the improving labor market, as seen in this week's reports from Japan, Germany, and Brazil. In the same vein, US private payrolls are forecast to increase for the fourth straight month by 85,000 in next week's report. Against this backdrop, we have begun raising forecasts after an extended period in which our global forecast was stable, and are highlighting upside risk in other places where we have yet to change numbers. This week we boosted our 2010 GDP forecast for Japan for the second time in a month, from 2.4% to 3.2% (4Q/4Q).

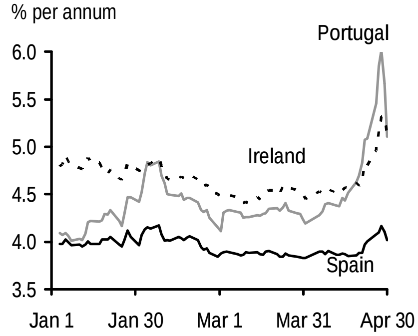
Although economic activity is accelerating, the damage done to public finances is creating market anxieties in parts of the developed world. These tensions are focused inside the Euro area, where a handful of countries have developed very high deficits and debt burdens, led by Greece. Although financial support for Greece is on the way, the question of its ultimate solvency remains. Moreover, market pressures recently have broadened to other Euro area economies with burdensome deficits, including Portugal and Spain, threatening to broaden the crisis.

Business and consumer surveys

	1Q10	Apr 10
Manufacturing		
US avg regional Fed surveys	52.8	56.7
Euro area PMI	54.4	57.5
Japan PMI	52.5	53.5
Nonmanufacturing		
US NAHB survey	15.7	19.0
US Richmond Fed services PMI	-8.0	9.0
Euro area services PMI	52.8	55.5
Japan Shoko-Chukin	42.0	45.7
Consumer confidence		
US avg of Mich and Conf Bd	62.8	65.1
EU survey	-16.8	-15.0

10-year bond yields

% per annum



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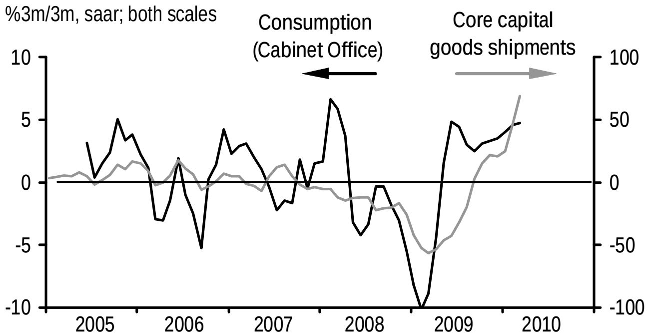
Japan domestic demand indicators



With high deficits and rising debt set to persist across much of the developed world, the potential for additional flare-ups will remain. The immediate concern is whether the high levels of European sovereign debt that sit on bank balance sheets will impair the flow of credit in the region. Nonetheless, it is important not to lose sight of the forces of containment. Recent experience has shown that, up to a point, stronger entities are willing to support their weaker brethren in order to limit systemic risk. This is most recently on display in Europe, where the establishment of a template for action within the Euro area means that officials will be better prepared to respond should the crisis widen to other, bigger countries.

More fundamentally, the global economy is in transition to a strong, self-sustaining expansion. This will allow governments to begin withdrawing support—both stimulus and the automatic stabilizers—while at the same time bolstering revenues. Thus, our forecast foresees a substantial improvement in underlying budget positions in 2011 and 2012. In addition, one benefit of the low level of activity is that it is delivering a striking decline in G-3 core inflation. This means that global monetary policy can remain highly accommodative for a more extended period, reinforcing the upswing in economic growth. To this point, this week the FOMC reaffirmed its low-for-long guidance, while the BoJ signaled additional unconventional easing is on the way even as it upgraded its economic forecast. While we are mindful of the risk of a more negative outcome, we maintain our forecast that the global economy will deliver broadly based, above-trend growth through at least next year.

European stress test

Although the spotlight in the Euro area is being focused squarely on sovereign credit concerns in Southern Europe, sentiment indicators for the region as a whole have been picking up as a less-noted, but still-impressive, cyclical upswing is gaining momentum. Given recent signs of a material positive shift in household and business behavior, the tepid recovery is now showing signs of accelerating to an above-trend pace of 3%q/q saar in the current quarter. Indeed, if not for the intensification of sovereign credit stresses this year, our outlook would be more upbeat.

In the event, however, the fiscal stresses have dominated the scene. This clearly poses a risk to the cyclical growth story. The risk is not concerned with the potential for additional large-scale fiscal tightening in Greece, Portugal, Spain, and Ireland. The much larger economies of the region are still easing policy this year on net. Instead, the main risk flowing from the sovereign stress is that European banks will curtail credit to each other and to private borrowers in a way similar to the post-Lehman bankruptcy fallout. Financial market indicators give little indication this is happening yet. However, these are contemporaneous indicators and, given the importance of sentiment at times like this, it is hard to have a high level of conviction about how the situation will unfold.

The details of a multi-year financial support package for Greece appear forthcoming within the next few days. This will effectively enable the Greek government to stay away from the capital markets for three years or so. This is certainly a necessary condition to ease the financial market stress, in Greece and elsewhere. That said, we recognize this may not be sufficient. Concerns about Greek solvency are likely to persist, and it is apparent that the other sovereigns in the spotlight all have huge fiscal adjustments ahead.

CEEMEA policymakers wary

As is the case elsewhere, economic fundamentals have improved across the CEEMEA region in recent months. However, concerns about potential spillover from the Southern European fiscal turmoil is likely to keep policymakers reluctant to begin policy normalization any time soon.

The CBRT is to be the first central bank in the region to reflect this concern. Despite a faster-than-expected recovery in domestic demand and a worsening in inflation dynamics, the CBRT clearly stated its intention to keep rates unchanged until the last quarter of the year. Renewed uncertainty about the Euro area recovery was the main reason behind this decision. Given the CBRT's strong determination to leave rates unchanged in the short term, we have pushed back the start of the hiking cycle to September.

Central Europe's central banks have also turned more dovish in recent months, although largely in response to the rise in their currencies. Our base case remains that the NBP and CNB will start raising interest rates in the fourth quarter of

Latin American real GDP

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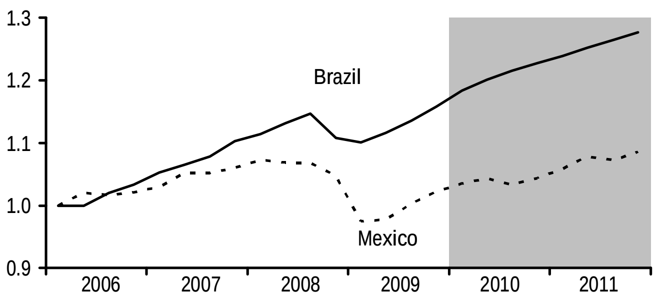

this year on the back of rising inflation and stronger growth. Yet, weaker Euro area demand than we currently anticipate would likely delay the start of hiking cycles until 2011.

Asian growth pressuring policymakers

Strong data reports in EM Asia continue to reinforce the view among regional policymakers that a gradual tightening is appropriate. Once China begins its rate hike cycle and allows its currency to appreciate—events we expect during the current quarter—that will strengthen the resolve of others in Asia to do the same. But even before those initial moves in China, recent data releases are pushing policymakers in individual countries to reach the same conclusion.

In Korea, growth continues to run past official forecasts. The Bank of Korea revised up its 2010 GDP forecast two weeks ago, but this week's 1Q GDP report and March data reports suggest upside risk to this view. We maintain that the BoK's first rate hike will happen in 3Q as asset price inflation—a key concern for policymakers—has settled in recent months, but a move could come as early as July. With the unemployment rate still quite elevated, we expect the CBC in Taiwan to stay on hold until September. However, with inflation expected to pick up and the potential impact of easy monetary conditions on asset markets and financial stability, a rate hike as early as June is possible. Following its recent shift to a tightening stance, the Monetary Authority of Singapore was again upbeat on growth prospects for 2010 at this week's biannual macroeconomic review, a view underscored by the strong 1Q labor report.

The strong growth in EM Asia has been a key driver of Australian growth and this is leading the RBA to tighten policy faster than any other G-20 central bank. If the RBA hikes next week as expected, it will mark the sixth 25bp hike in the last seven meetings. This week's material upside surprises on consumer and producer prices—on both the headline and core measures—strengthen the case for another hike.

COPOM and Banxico on separate tracks

Similar to Asia, their relative insulation from foreign sovereign credit woes means that Latin American policymakers are in a position to focus on domestic fundamentals as they consider their options. This week Brazil initiated its tightening cycle with a 75bp rate hike. The large size of the hike suggests that whatever factors had influenced the central bank to stay on hold in prior months amid visibly increasing inflation risks have now been left behind. Against a backdrop of real GDP growth projected at 7%, a historically low unemployment rate, and robust credit growth, the lingering fiscal and quasi-fiscal stimulus will place the full burden of containing inflation squarely on monetary authorities.

In contrast to Brazil, Banxico could be on hold somewhat longer than previously expected. Although GDP is expanding at a robust pace, the level of activity remains depressed, and the recent rise in inflation is being viewed as a one-off jump related to tax increases. This message was underscored by this week's inflation report from the central bank, which indicated no second-round impacts of tax hikes on inflation and continued to deliver a generally dovish tone. While we expect two 25bp rate hikes this year starting in October, the risk is for no move at all this year.

Likely UK coalition gov't to face challenges

As the UK faces its largest fiscal adjustment in a generation, next week's election appears likely to deliver a coalition government between center right (Conservatives) and center left (Liberal Democrats). Such a political outcome is undeniably less stable than a single party majority, but is unlikely to prevent the UK from presenting more detail on its fiscal consolidation program and accelerating its implementation. After a structural tightening of 1% of GDP this fiscal year, the departing Labour administration had planned a 2% cut for next year. We have anticipated this rising to a 3% tightening for 2011-12, perhaps with some of that increment pulled into 2010.

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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			
	2009	2010	2011	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11	1Q10	2Q10	4Q10	2Q11
The Americas														
United States	-2.4	3.5	3.1	5.6	3.2 ↑	4.0	4.0	3.5	2.5	2.5	2.4	2.2	1.2	1.1
Canada	-2.6	3.4 ↑	3.3	5.0	5.8 ↑	2.7 ↓	3.3	4.0	4.0	2.3	1.6 ↓	1.3 ↓	1.8 ↓	2.1
Latin America	-2.9	4.9	3.8	7.2	5.2	4.6	2.6	4.5	4.0	4.9	5.8	6.3	7.0	6.9
Argentina	-2.0	4.5	3.0	7.9	8.0	8.0	3.0	3.0	2.0	3.0	7.5	8.0	10.0	10.0
Brazil	-0.2	7.0	4.0	8.4	8.7	6.3	4.8	4.0	3.8	4.2	4.8	4.9	5.0	4.5
Chile	-1.5	5.5	5.5	5.9	-6.0	8.0	22.0	18.0	-2.0	-6.0	0.2	3.3	4.1	3.8
Colombia	0.4	3.0	4.1	4.7	2.7	2.8	2.9	3.1	4.5	4.8	2.0	2.1	3.7	2.9
Ecuador	0.4	2.0	3.0	1.3	2.0	3.5	4.0	4.5	3.0	2.5	4.1	3.9	4.7	4.4
Mexico	-6.5	4.5	3.5	8.4	5.0	3.2	-3.8	4.2	5.7	7.9	4.6	4.4	5.1	4.5
Peru	0.9	6.0	6.0	11.5	4.1	4.3	4.6	5.0	6.3	7.2	0.6	1.0	2.0	2.2
Venezuela	-3.3	-1.5	2.5	-4.6	-4.0	-2.0	12.5	1.5	1.5	1.5	27.6	31.8	33.7	39.3
Asia/Pacific														
Japan	-5.2	3.2 ↑	2.2 ↑	3.8	5.0 ↑	2.5 ↑	2.7 ↑	2.7 ↑	2.2 ↑	2.0 ↑	-1.2 ↑	-1.4 ↑	-0.7 ↑	0.1
Australia	1.3	3.1	3.6	3.7	3.0	3.3	3.8	3.9	3.1	4.2	2.5	2.5	2.6	3.0
New Zealand	-1.6	2.8	2.5	3.3	3.2	3.2	3.7	2.9	1.3	2.3	2.2	2.3	2.5	2.8
Asia ex Japan	4.6	8.6 ↑	7.2	7.6	10.4 ↑	7.1	6.4	6.8	7.2	7.4	3.8	4.4	3.8	3.2
China	8.7	10.8	9.4	10.8	13.1	9.4	9.3	9.0	9.1	9.5	2.2	3.2	3.1	2.4
Hong Kong	-2.7	5.3	4.2	9.5	4.5	4.3	4.0	3.8	4.2	4.3	1.1	2.4	2.3	1.9
India	7.2	8.0	8.3	-2.0	10.4	8.1	7.0	8.7	7.9	7.8	12.7	11.9	6.2	5.5
Indonesia	4.5	6.2	5.8	9.6	6.0	6.0	4.0	5.0	6.5	6.5	4.4	5.3	6.3	4.9
Korea	0.2	5.8 ↑	4.1	0.7	7.5 ↑	4.0 ↓	4.5 ↑	3.8 ↑	4.0	4.0	2.7	2.8	3.4	3.6
Malaysia	-1.7	7.7	4.8	15.4	5.0	4.0	5.0	5.0	4.9	4.9	0.8	1.7	2.4	2.4
Philippines	0.9	4.5	4.3	3.5	6.0	5.0	3.5	4.0	4.5	4.5	4.3	5.0	5.2	4.9
Singapore	-2.0	9.0	4.0	-2.8	32.1	5.3	-9.6	4.9	6.6	6.6	0.9	3.4	4.7	3.7
Taiwan	-1.9	8.2	4.8	18.0	5.7	3.6	3.8	4.0	5.0	5.3	-0.3	0.9	2.0	1.8
Thailand	-2.3	7.3	6.6	15.3	5.7	5.3	3.6	3.6	8.0	8.0	4.0	5.5	4.4	3.0
Africa/Middle East														
Israel	0.7	3.0	4.5	4.8	3.5	3.5	3.0	3.0	4.0	5.0	3.5	2.7	2.7	3.1
South Africa	-1.8	3.0	3.5	3.2	3.9	4.2	4.0	4.0	3.6	2.8	5.6	4.6	5.4	5.7
Europe														
Euro area	-4.0	1.5	2.1	0.2	1.5	3.0	2.3	2.0	2.0	2.0	1.1	1.2	1.1	0.8
Germany	-4.9	1.7	2.1	0.0	1.0	3.0	2.0	2.0	2.0	2.0	0.9	0.9	1.3	1.3
France	-2.2	2.0	2.2	2.4	1.5	3.0	2.0	2.5	2.0	2.0	1.4	1.4	0.9	0.9
Italy	-5.1	0.9	1.7	-1.3	1.0	2.5	1.5	2.0	1.5	1.5	1.3	1.1	1.1	1.1
Norway	-1.4	2.1	2.8	1.3	2.0	3.0	3.0	3.0	2.8	2.8	3.1	3.2	1.7	0.7
Sweden	-4.7	1.3	3.1	-2.2	2.2	3.5	3.5	3.0	3.0	3.0	1.2	1.6	1.2	1.9
Switzerland	-1.5	2.5	2.8	3.0	2.5	2.8	3.0	3.0	2.8	2.8	1.1	1.0	0.9	0.8
United Kingdom	-4.9	1.4	3.2	1.8	0.8	3.0	3.0	3.5	3.0	3.0	3.3	2.9	1.9	1.5
Emerging Europe	-5.0	4.1	4.7	5.0	1.8	4.5	3.9	3.8	4.1	4.4	6.2	5.8	5.9	5.4
Bulgaria	-5.0	-1.5	4.5	…	…	…	…	…	…	…	…	…	…	…
Czech Republic	-4.2	2.0	4.0	3.0	2.5	2.5	2.0	2.0	3.5	4.5	0.6	1.2	2.8	2.8
Hungary	-6.3	0.5	4.0	-1.7	1.5	2.5	2.0	2.0	4.0	4.0	6.1	4.8	3.7	2.8
Poland	1.8	3.2	4.2	5.3	3.0	4.0	2.7	3.0	3.0	4.0	3.0	2.0	2.6	2.8
Romania	-7.1	1.5	4.0	…	…	…	…	…	…	…	4.9	4.5	4.5	4.5
Russia	-7.9	5.5	5.0	8.1	1.0	6.0	5.5	5.0	5.0	5.0	7.3	6.5	7.2	7.0
Turkey	-4.7	5.1	5.5	…	…	…	…	…	…	…	9.3	10.3	8.5	6.6
Global	-2.5	3.5 ↑	3.4 ↑	4.0	3.8 ↑	3.9 ↑	3.5 ↑	3.5 ↑	3.1	3.1	2.2	2.1	1.8	1.7
Developed markets	-3.4	2.7 ↑	2.7 ↑	3.2	2.9 ↑	3.3	3.2 ↑	2.9	2.4 ↑	2.3	1.5	1.4 ↑	1.0	1.0
Emerging markets	1.0	6.7	5.8	6.9	7.4 ↑	5.9	5.0 ↑	5.6	5.8	6.2	4.8	5.0	4.9	4.4
Memo:														
Global — PPP weighted	-0.8	4.8	4.4	4.9	5.3	4.8	4.4	4.5	4.2	4.2	3.1	3.2	2.8	2.6

Note: For some emerging economies, 2009-2011 quarterly forecasts are not available and/or seasonally adjusted GDP data are estimated by J.P. Morgan.
Bold denotes changes from last edition of *Global Data Watch*, with arrows showing the direction of changes. Underline indicates beginning of J.P. Morgan forecasts.

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G-3 economic outlook detail

Percent change over previous period; seasonally adjusted annual rate unless noted

				2009	2010				2011		
	2009	2010	2011	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q
United States											
Real GDP	-2.4	3.5	3.1	5.6	3.2	4.0	4.0	3.5	2.5	2.5	3.0
Private consumption	-0.6	2.7	2.6	1.6	3.6	3.3	3.0	3.0	2.5	2.0	2.5
Equipment investment	-16.6	11.0	9.5	19.0	13.4	12.0	12.0	10.0	9.0	8.0	8.0
Non-residential construction	-19.8	-12.6	1.5	-18.1	-14.0	-8.0	-3.0	-3.0	0.0	7.0	9.0
Residential construction	-20.5	1.3	15.7	3.7	-10.9	5.0	10.0	15.0	15.0	20.0	20.0
Inventory change ($ bn saar)	-108.3	46.3	49.2	-19.7	31.1	44.2	56.4	53.6	45.5	47.2	50.3
Government spending	1.8	0.4	-0.1	-1.3	-1.8	0.5	1.1	1.4	-0.8	-1.0	-1.0
Exports of goods and services	-9.6	12.2	9.8	22.8	5.8	14.0	12.0	11.0	9.0	9.0	8.0
Imports of goods and services	-13.9	9.6	7.5	15.8	8.9	8.0	8.0	8.0	7.0	8.0	7.0
Domestic final sales contribution	-2.8	2.2	2.9	1.5	2.3	3.1	3.3	3.4	2.6	2.5	2.9
Inventories contribution	-0.6	1.2	0.0	3.8	1.6	0.4	0.4	-0.1	-0.3	0.0	0.1
Net trade contribution	1.0	0.1	0.2	0.3	-0.6	0.5	0.3	0.2	0.1	0.0	0.0
Consumer prices (%oya)	-0.3	1.8	1.2	1.5	2.4	2.2	1.5	1.2	1.1	1.1	1.2
Excluding food and energy (%oya)	1.7	0.8	0.6	1.7	1.3	0.9	0.6	0.3	0.4	0.4	0.6
Federal budget balance (% of GDP, FY)	-9.9	-9.4	-7.8								
Personal saving rate (%)	4.2	3.1	3.4	3.9	3.1	3.0	3.0	3.2	3.2	3.3	3.4
Unemployment rate (%)	9.3	9.5	9.1	10.0	9.7	9.4	9.5	9.4	9.3	9.1	9.0
Industrial production, manufacturing	-11.3	4.9	3.9	5.6	6.6	5.0	5.0	4.0	3.0	3.0	4.5
Euro area											
Real GDP	-4.0	1.5	2.1	0.2	1.5	3.0	2.3	2.0	2.0	2.0	2.0
Private consumption	-1.0	0.0	1.3	-0.2	-1.0	1.0	1.0	1.0	1.5	1.5	1.5
Capital investment	-10.8	-1.1	3.8	-5.2	-1.0	2.0	3.0	4.0	4.0	4.0	4.0
Government consumption	2.3	0.8	1.0	-0.4	0.0	1.0	1.0	1.0	1.0	1.0	1.0
Exports of goods and services	-12.8	8.3	8.1	7.6	9.0	10.0	8.0	8.0	8.0	8.0	8.0
Imports of goods and services	-11.4	5.7	7.7	5.1	5.0	7.5	6.5	7.5	8.0	8.0	8.0
Domestic final sales contribution	-2.5	0.0	1.7	-1.3	-0.8	1.2	1.4	1.6	1.9	1.9	1.9
Inventories contribution	-0.8	0.5	0.1	0.4	0.6	0.7	0.1	0.1	0.0	0.0	0.0
Net trade contribution	-0.8	1.1	0.3	1.0	1.7	1.1	0.7	0.4	0.2	0.2	0.2
Consumer prices (HICP, %oya)	0.3	1.2	0.9	0.4	1.1	1.2	1.2	1.1	0.9	0.8	0.9
ex unprocessed food and energy	1.3	0.9	0.6	1.0	1.0	1.0	0.8	0.7	0.5	0.6	0.7
General govt. budget balance (% of GDP, FY)	-6.1	-6.7	-5.5								
Unemployment rate (%)	9.4	9.9	9.5	9.9	10.0	10.0	9.8	9.7	9.6	9.5	9.4
Industrial production	-14.7	3.1	3.2	8.2	2.0	4.0	3.5	3.5	3.0	3.0	3.0
Japan											
Real GDP	-5.2	3.2	2.2	3.8	5.0	2.5	2.7	2.7	2.2	2.0	1.5
Private consumption	-1.1	2.8	1.7	2.8	3.5	2.0	2.3	2.5	1.2	1.8	1.0
Business investment	-19.3	3.1	6.0	3.8	8.0	8.0	8.0	6.0	6.0	5.0	5.0
Residential construction	-13.9	0.7	9.7	-12.5	20.0	18.0	15.0	10.0	10.0	8.0	5.0
Public investment	6.6	-4.5	-11.6	-5.0	15.0	-25.0	-15.0	-10.0	-8.0	-10.0	-12.0
Government consumption	1.6	1.1	0.9	2.5	0.5	1.5	0.5	1.0	1.2	0.5	0.5
Exports of goods and services	-24.2	18.9	8.7	21.7	16.0	12.0	11.0	10.0	8.0	6.0	8.0
Imports of goods and services	-17.1	7.8	7.9	5.1	8.0	8.0	9.0	9.0	8.0	6.0	7.0
Domestic final sales contribution	-3.5	2.1	1.8	2.1	4.1	1.8	2.2	2.3	1.7	1.7	1.1
Inventories contribution	0.2	-0.5	0.0	-0.6	-0.5	-0.2	-0.2	-0.2	0.1	0.0	-0.1
Net trade contribution	-2.0	1.7	0.5	2.2	1.3	0.9	0.7	0.5	0.4	0.3	0.5
Consumer prices (%oya)	-1.4	-1.1	-0.1	-2.0	-1.2	-1.4	-1.3	-0.7	-0.5	0.1	0.2
General govt. net lending (% of GDP, CY)	-6.8	-7.5	-8.8								
Unemployment rate (%)	5.1	4.8	4.5	5.2	4.9	4.8	4.8	4.7	4.6	4.6	4.5
Industrial production	-21.8	21.6	10.0	25.9	29.4	15.0	12.0	12.0	8.0	8.0	10.0
Memo: Global industrial production	-11.0	7.6	5.3	10.2	8.2	6.8	6.1	5.4	4.5	4.8	5.6
%oya				-2.8	7.4	8.7	7.8	6.6	5.7	5.2	5.1

Note: More forecast details for the G-3 and other countries can be found on J.P. Morgan's Morgan Markets client web site.

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Central Bank Watch

	Official interest rate	Current	Change from Aug '07 (bp)	Last change	Next meeting	Forecast next change	Jun 10	Sep 10	Dec 10	Mar 11	Jun 11
Global	GDP-weighted average	1.31	-336				1.36	1.45	1.54	1.68	2.01
excluding US	GDP-weighted average	1.86	-249				1.94	2.07	2.20	2.41	2.72
Developed	GDP-weighted average	0.51	-360				0.52	0.56	0.60	0.72	1.07
Emerging	GDP-weighted average	4.49	-238				4.68	5.01	5.28	5.50	5.77
Latin America	GDP-weighted average	6.01	-292				6.32	6.88	7.57	7.75	8.25
CEEMEA	GDP-weighted average	4.16	-270				4.17	4.41	4.51	4.70	5.14
EM Asia	GDP-weighted average	4.04	-205				4.26	4.54	4.72	4.97	5.09
The Americas	GDP-weighted average	0.78	-481				0.83	0.92	1.03	1.09	1.48
United States	Federal funds rate	0.125	-512.5	16 Dec 08 (-87.5bp)	23 Jun 10	2Q 11 (+25bp)	0.125	0.125	0.125	0.125	0.50
Canada	Overnight funding rate	0.25	-400	21 Apr 09 (-25bp)	2 Jun 10	2 Jun 10 (+25bp)	0.50	1.00	1.50	2.00	2.50
Brazil	SELIC overnight rate	**9.50**	-250	**28 Apr 10 (+75bp)**	9 Jun 10	**9 Jun 10 (+75bp)**	**10.25**	**11.50**	**12.50**	**12.50**	**12.50**
Mexico	Repo rate	4.50	-270	17 Jul 09 (-25bp)	21 May 10	Oct 10 (+25bp)	4.50	4.50	5.00	5.00	5.75
Chile	Discount rate	0.50	-450	9 Jul 09 (-25bp)	13 May 10	Jun 10 (+25bp)	0.75	1.50	2.25	3.75	5.00
Colombia	Repo rate	3.50	-550	23 Nov 09 (-50bp)	27 May 10	1Q 11 (+50bp)	3.50	3.50	3.50	4.50	5.50
Peru	Reference rate	1.25	-325	6 Aug 09 (-75bp)	<u>6 May 10</u>	10 Jun 10 (+25bp)	1.50	2.25	3.00	3.75	4.50
Europe/Africa	GDP-weighted average	1.28	-324				1.29	1.33	1.39	1.63	2.08
Euro area	Refi rate	1.00	-300	7 May 09 (-25bp)	<u>6 May 10</u>	1Q 11 (+25bp)	1.00	1.00	1.00	1.25	1.75
United Kingdom	Repo rate	0.50	-500	5 Mar 09 (-50bp)	10 May 10	Nov 10 (+25bp)	0.50	0.50	0.75	1.00	1.25
Sweden	Repo rate	0.25	-325	2 Jul 09 (-25bp)	Jul 10	1Q 11 (+25bp)	0.25	0.25	0.25	0.50	0.75
Norway	Deposit rate	1.75	-275	16 Dec 09 (+25bp)	<u>5 May 10</u>	5 May 10 (+25bp)	2.00	2.25	2.50	2.75	3.25
Czech Republic	2-week repo rate	1.00	-175	16 Dec 09 (-25bp)	<u>6 May 10</u>	**4Q 10 (+25bp)**	1.00	1.00	1.25	1.75	2.25
Hungary	2-week deposit rate	**5.25**	-250	**26 Apr 10 (-25bp)**	31 May 10	**3Q 10 (-25bp)**	5.25	5.00	5.00	5.00	5.00
Israel	Base rate	1.50	-250	28 Mar 10 (+25bp)	24 May 10	**24 May 10 (+25bp)**	2.00	2.25	2.75	3.25	3.75
Poland	7-day intervention rate	3.50	-100	24 Jun 09 (-25bp)	25 May 10	4Q 10 (+25bp)	3.50	3.50	3.75	4.00	4.50
Romania	Base rate	6.50	-50	29 Mar 10 (-50bp)	<u>4 May 10</u>	4 May 10 (-50bp)	5.75	5.50	5.50	6.00	6.50
Russia	1-week deposit rate	**3.25**	25	**29 Apr 10 (-25bp)**	May 10	**May 10 (-25bp)**	3.00	3.00	3.00	3.00	3.50
South Africa	Repo rate	6.50	-300	25 Mar 10 (-50bp)	13 May 10	1Q 11 (+50bp)	6.50	6.50	6.50	7.00	8.00
Switzerland	3-month Swiss Libor	0.25	-225	12 Mar 09 (-25bp)	Jun 10	Sep 10 (+25bp)	0.25	0.50	0.75	1.00	1.25
Turkey	Overnight borrowing rate	6.50	-1100	19 Nov 09 (-25bp)	17 Jun 10	17 Jun 10 (+50bp)	7.00	8.50	8.50	8.50	8.50
Asia/Pacific	GDP-weighted average	2.14	-130				2.25	2.41	2.51	2.65	2.72
Australia	Cash rate	4.25	-200	6 Apr 10 (+25bp)	<u>4 May 10</u>	4 May 10 (+25bp)	4.50	5.00	5.25	5.50	5.75
New Zealand	Cash rate	2.50	-550	30 Apr 09 (-50bp)	10 Jun 10	29 Jul 10 (+25bp)	2.50	3.00	3.50	4.00	4.25
Japan	Overnight call rate	0.10	-43	19 Dec 08 (-20bp)	20 May 10	4Q 11 (+15bp)	0.10	0.10	0.10	0.10	0.10
Hong Kong	Discount window base	0.50	-625	17 Dec 08 (-100bp)	24 Jun 10	2Q 11 (+25bp)	0.50	0.50	0.50	0.50	1.00
China	1-year working capital	5.31	-126	22 Dec 08 (-27bp)	2Q 10	2Q 10 (+27bp)	5.58	5.85	6.12	6.39	6.39
Korea	Base rate	2.00	-250	12 Feb 09 (-50bp)	11 May 10	3Q 10 (+25bp)	2.00	2.25	2.50	2.75	3.00
Indonesia	BI rate	6.50	-200	5 Aug 09 (-25bp)	<u>5 May 10</u>	4Q 11 (-25bp)	6.50	6.50	6.50	6.50	6.50
India	Repo rate	5.00	-275	19 Mar 10 (+25bp)	27 Jul 10	20 Apr 10 (+50bp)	5.50	6.00	6.00	6.50	6.75
Malaysia	Overnight policy rate	2.25	-125	4 Mar 10 (+25bp)	13 May 10	13 May 10 (+25bp)	2.50	3.00	3.00	3.00	3.00
Philippines	Reverse repo rate	4.00	-350	9 Jul 09 (-25bp)	3 Jun 10	Jun 10 (+25bp)	4.25	4.75	5.00	5.00	5.00
Thailand	1-day repo rate	1.25	-200	8 Apr 09 (-25bp)	2 Jun 10	2 Jun 10 (+25bp)	1.50	1.75	1.75	1.75	1.75
Taiwan	Official discount rate	1.25	-188	18 Feb 09 (-25bp)	2Q 10	3Q 10 (+25bp)	1.25	1.50	1.75	2.00	2.25

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

The J.P. Morgan View: Markets

Contagion checkpoint

- **Asset allocation:** Overall long equities and high-yield, underweighting the hot spots in the world—China, Europe, banks.
- **Economics:** Global growth forecast raised, breaking out of the range.
- **Fixed income:** EU/IMF support should bolster short-dated Greek bonds, but long-dated spreads will remain wide until the budget deficit falls. Position for wider Euro area money market spreads. Turn neutral on Brazil.
- **Equities:** Sovereign stress and regulations raise downside risks for banks. US Senate bill will likely have dramatic impact on FI business for IBs.
- **Credit:** Remain underweight European versus US corporates.
- **FX:** Stay short the euro.
- **Commodities:** Oil forecast raised from $90 to $93 in 4Q.

This was a volatile week that nudged riskier assets down, in particular bank stocks and bonds. Our view remains that the threats from the European sovereign credit crisis, EM policy tightening, and regulatory overkill are trumped by the power of the business cycle, the zero return on cash, and soaring corporate profits. We stay long equities and higher-yielding credit, recognizing the risk of a moderate, short-term correction.

Our economic forecasts are breaking out. Our economists have maintained a 2010 world growth forecast in a 3.3%-3.4% range since September, with the consensus gradually catching up. This week, we raised Japan and Korea each by 1/2%-pt, pushing **our world 2010 forecast to 3.5%**—maybe not a huge gain, but still meaningful and indicative of continued positive momentum in growth perceptions. Even more important is that the recovery is getting a better footing with both consumer and corporate demand rising across regions and sectors, raising our confidence that the recovery is sustainable.

Our belief that the business cycle will conquer its multiple threats needs to be monitored closely for signs that any of these brush fires is breaking out into a wildfire. This is the **contagion question**. We see little so far from the onset of policy tightening in emerging economies. Brazil, India, and China are tightening, leading us to underweight Brazil and China within EM. EM local bond markets did not follow the rally in DM bonds, but have still outperformed significantly this year. The rising risk of regulatory overkill on banks has hurt bank stocks and bonds, but has had little impact on the rest of the market.

The **potential contagion from the Greek debt crisis** needs closer monitoring if only because it could become another Lehman. By itself, Greece's economy and bond market are too small for any restructuring to have a global impact. But that could have been said of Lehman and subprime also. What made Lehman a global disaster was contagion. We see current contagion risk on four levels: the economy, credit losses, other government bond markets, and the interbank market.

Economic contagion could come through the impact on fiscal policy in other European countries and on private sector spending. Fiscal policy is massively tightening in Greece, as well as in Portugal, Ireland, and Spain. But the overall fiscal stance of the Euro area remains expansionary, due to Germany. A move to further tightening by Spain, Portugal, and Ireland would only move the overall fiscal stance of the Euro area to neutral. Recent economic data and surveys for the region are also showing that private sector demand is picking up, not falling off.

Contagion from credit losses on higher-yielding EMU bonds could induce a fire sale of other credits and counterparty problems. The good news here is that the €47 billion YTD loss on government bonds from Greece, Spain, and Portugal has been neatly offset by a €52 billion gain on other EMU government bonds. Clearly, not all bondholders are fully diversified across these bonds.

The so far successful assault on weak governments could embolden market participants to go after larger prey. And indeed, **US and UK** 10-year benchmarks have moved to above Libor this year, despite an improved outlook for deficits. Here the good news is that these swap spreads stopped widening against governments over the past two weeks. We are long USTs versus 10-year swaps.

The fourth form of contagion impacts the **interbank market**, which is where the Lehman default did the most damage. Overnight volumes in the unsecured interbank market are little changed over the past week. Beyond overnight, volumes have fallen but from low levels, as this market never fully recovered after Lehman. Big Spanish and Portuguese banks still have access to the interbank market, but at a higher price. The repo market for Spanish, Portuguese, and Irish bonds is thinning as everyone wants to short them and few want to be on the other side. The ECB has surely learned from the Lehman debacle and will do all it can to avoid a money market crisis. See this week's *Flows & Liquidity* for more details.

Fixed income

The Euro area debt crisis worsened markedly again this week after S&P cut Greece's rating by three notches to BB+, and downgraded Spain and Portugal as well. Greek two-year yields surged to over 18% by Wednesday, but have retraced sharply since then, on increased confidence that a three-year support package for Greece will be announced within days.

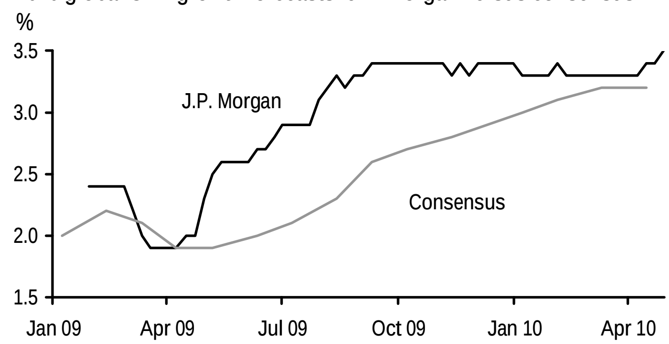
This package will remove near-term liquidity risks and should prompt a rally in short-dated Greek bonds. But concerns over solvency are likely to persist for some time, and the prospects for longer-term Greek bonds (and indeed those of Portugal and Ireland) depend on the market's confidence that these governments can implement a difficult fiscal adjustment. Spreads are thus likely to remain high until budget deficits fall significantly. With Greece soon to receive EU/IMF funding, the market's focus is likely to switch to Ireland's and Portugal's debt issuance over the coming months, with Portugal in particular having €20 billion of debt maturing over the rest of the year.

Portuguese and Irish spreads also widened sharply this week, but there is little sign that investors are questioning the creditworthiness of major economy government bonds. The spread of G-7 10-year government yields to swap rates has been little changed over the past month, and core bond markets rallied strongly this week as Greece's troubles escalated. Concerns over banks' exposure to high-deficit Euro area countries led to a small rise in interbank borrowing rates. We recommend positioning for Euro area interbank rates to increase further relative to expected policy rates, as the low level of spreads makes the return on spread wideners highly asymmetric.

Equities

Global equities finished the week 2% lower as rating downgrades of Euro area sovereigns raised fears of contagion. Despite this week's loss, global equities are down by only 3% from their April 15 peak, as impressive 1Q earnings cushioned equity markets from sovereign stress. **Equities are seen as more remote to sovereign problems** as they represent a liability for the corporate sector, which, in contrast to the government sector, is going from strength to strength.

2010 global GDP growth forecasts: J.P. Morgan versus consensus



The sector more susceptible to sovereign stress is banking. Banks normally hold around 10% of their assets in government bonds. Bank funding costs typically rise in tandem with sovereign funding costs, on the perception that domestic banks cannot be less risky than the sovereign. In addition, banks are covered by government guarantees, which are worth less in an environment of sovereign stress. Indeed, banks have recently underperformed, especially in Europe, which is the epicenter of the sovereign stress. We see further downside from here. Our European bank analysts estimate that every 10bp increase in funding costs reduces earnings by 1.7% (see *Greek Sovereign Risk—Potential implications for European Banks*, Francesca Tondi, Carla Antunes Da Silva, Paul Formanko et al., April 30).

The other headwind for banks is regulation. The financial reform bill in the US Senate is fueling uncertainty in investment banks (IB). The bill will likely have a material impact on fixed income business and in particular credit and rate derivatives. IB ROEs will likely decline to 12%, which is a lot lower than current IB ROE targets of 20%. As a result, CEOs would be under pressure to cut compensation ratios from an average 44% to 35% in 2011 (see *Dodd/Lincoln Bill Analysis: implications for the future structure of the IB industry*, Kian Abouhossein, April 29).

Credit

The series of rating downgrades of southern European sovereigns shocked markets earlier this week, pushing spreads wider across credit markets. Contagion risk is highest in Financials, leading them to underperform Industrial bonds, which continue to benefit from strong corporate earnings and strong economic data. The Greek crisis is unlikely to be resolved near term even when the bailout funds are deployed, as Greece has to convince markets it can tackle the fiscal deficit problem. This will continue to put stress on the Euro area region, offsetting better economic data. We stay underweight European credit versus US credit in CDS indices.

In the **US**, the debate on financial reform is also creating uncertainty, as rating agencies threaten to downgrade banks in anticipation of lower profitability and less government support for the sector. These risks are keeping us tactically short in US HG credit near term. However, medium term, strong corporate earnings and strengthening fundamentals should support HG spreads. Our strategists estimate net issuance of credit products at $300 billion in 2011 and $400 billion in 2012. This is only a quarter of the pace seen during the credit boom of 2006/07. We believe this limited credit supply will cause spreads to tighten across all credit products medium term (*Credit Market Outlook & Strategy*, April 30).

Foreign exchange

Since the EU/IMF announced their (now trivial-sounding) €45 billion assistance package three weeks ago, we have avoided the temptation to trade sovereign risk through EUR/USD. Shorts are too large to give the currency much downward momentum (as evidenced by the euro's falling beta with respect to sovereign spreads), but policy is too unpredictable to bet on a sustained euro recovery. Selling the euro crosses remains the lower-drama means of exploiting Greece's main macroeconomic legacy to the region: **a lower rate environment for longer and thus a good environment for funding out of euros**. Stay short EUR/CAD, EUR/IDR, and EUR/INR. Also stay short EUR/CHF as a bet on unsustainable SNB intervention when growth and inflation are rising. We also increase yen shorts, adding long KRW/JPY to long CAD/JPY given that the possibility of a strong payrolls report next Friday should lift US yields and weaken the yen.

UK elections will be held Thursday but the outcome may not be known until midday Friday, given a tight race and the number of constituencies that are not counting votes overnight. One outcome is sterling-positive (outright Tory victory) and two are sterling-negative (Labour victory and hung parliament), but even sterling strength has limits given the growth consequences of tighter fiscal policy post-election. The UK appears to face a muddle-through year given its fiscal position, not a near-crisis event such as Greece experienced. In cash markets, we are flat but are biased to sell: EUR/GBP has declined alongside a collapse in Euro-UK rate expectations, but that move in rates markets looks suspect in view of the fiscal tightening that awaits the next government.

Commodities

Commodities are close to flat this week with precious metals once again outperforming, while base metals lost nearly 4%. WTI is now up this week recovering all the losses seen until Wednesday. **We keep our positive outlook and raise our crude oil price forecast.** We believe that WTI should average $93 in 4Q, a $3 increase relative to our previous forecast.

We continue to see signs that the demand for oil is improving. At the same time, we expect that OPEC members will be sluggish in adjusting their production, allowing prices to move higher. OPEC has started to once again focus on inventory levels rather than prices. This sends a strong message that OPEC wants a tighter market. We increased our long position in crude oil last week when prices went below $82.50, and will maintain this position a while longer. On the spread side, we believe that Brent will continue to trade at a premium to WTI, as the pressure on the WTI front contract will persist due to regional oversupply. WTI will need to trade at least $2 lower than Brent to incentivize a move out of the region.

Ten-year Government bond yields

	Current	Jun 10	Sep 10	Dec 10	Mar 11
United States	3.67	4.10	4.25	4.50	4.70
Euro area	3.02	3.30	3.45	3.60	3.90
United Kingdom	3.85	4.40	4.55	4.65	4.80
Japan	1.28	1.40	1.50	1.55	1.55
GBI-EM	6.80			7.70	

Credit markets

	Current	YTD Return
US high grade (bp over UST)	131	3.9%
Euro high grade (bp over Euro gov)	150	2.0%
USD high yield (bp vs. UST)	584	7.0%
Euro high yield (bp over Euro gov)	586	9.2%
EMBIG (bp vs. UST)	268	4.9%
EM Corporates (bp vs. UST)	303	5.7%

Foreign exchange

	Current	Jun 10	Sep 10	Dec 10	Mar 11
EUR/USD	1.33	1.30	1.35	1.35	1.30
USD/JPY	94.1	87	90	93	96
GBP/USD	1.53	1.43	1.50	1.52	1.48

Commodities - quarterly average

	Current	10Q2	10Q3	10Q4	11Q4
WTI ($/bbl)	86	86	94	93	90
Gold ($/oz)	1180	1400	1300	1200	1225
Copper($/m ton)	7319	8000	6800	6250	6500
Corn ($/Bu)	3.73	4.05	3.95	3.90	4.00

Source: J.P. Morgan, Bloomberg, Datastream

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1. Research notes listed have been published in the *GDW; Special Reports* and *Global Issues* are stand-alone features, but may also have appeared in some form in *GDW*.

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Economic Research Note

US: keep an eye on the average workweek

- **Small moves in the length of the average workweek can mean big moves in household income**
- **With caution still prevalent, this margin may be business' preferred means to increase labor usage**
- **A normalization in the workweek would add about 1.5% to labor income**

Ask an economist what number he or she is forecasting for the next jobs report and you are unlikely to get for an answer something like "33.9 hours." The number most questioners would expect relates to the change in nonfarm employment, or perhaps the unemployment rate. This expectation is understandable and well-justified. However, in cyclical turning points, the length of the average workweek can be a critical determinant of the growth of labor income of the household sector. That, in turn, is crucial in assessing the sustainability of any rebound in consumer spending.

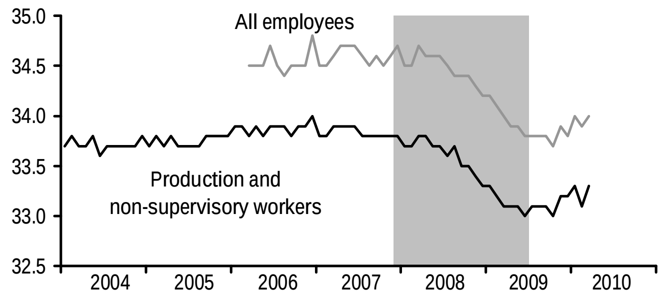
This sustainability has been called into question by the long-delayed and extremely sluggish pace of job creation. Of course, for the household sector as a whole, spending power increases not only when the number of jobs increases, but also when the pay of the existing jobs increases, or when the number of hours worked of existing jobs increases. While the first two of these factors have been anemic, the third factor, the average workweek, has increased enough in recent months to provide a significant lift to labor incomes.

Because of the large size of the workforce, even small increases in the average workweek can be important for incomes. For instance, an increase in the average workweek of 0.1 hour—or 6 minutes—provides the same lift to income as would a 380,000 increase in the number of jobs. Because such apparently small increases in the workweek have such a meaningful impact on incomes, this indicator will continue to be a key gauge of whether the labor market is supplying the household sector with the means to continue the recent path of solid spending gains.

The workweek may be particularly important in this cycle: the record-high share of persons working part-time for economic reasons is testimony to the degree to which firms placed full-time workers on part-time schedules in order to trim labor costs. As we discuss below, reversing this trend may be the path of least resistance for firms as they look to

Average workweek

Hours, sa, private nonfarm



Sources of labor income growth

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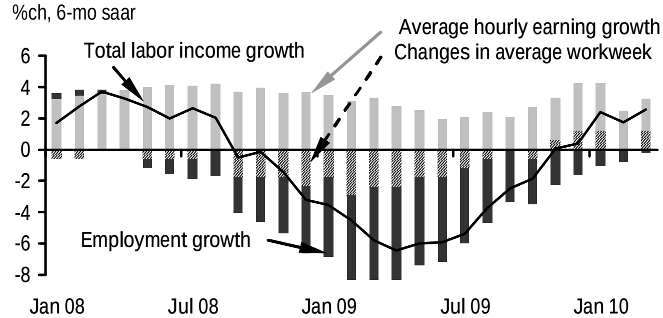


increase the overall number of hours worked, and so the focus on total employment may miss an important margin along which firms are reacting to the recovery.

Where next for the workweek

Before turning to the outlook for the workweek, a note should be made about the data. Historically, the length of the average workweek had only been measured for production and non-supervisory workers in the private nonfarm sector—workers who account for about 80% of the employment in the private nonfarm sector. Recently, the BLS has also begun publishing the workweek for all workers in the private nonfarm sector, including supervisors and other white collar workers. Because this latter series only goes back to 2006, in order to draw historical inferences, it is better to look at the production and nonsupervisory worker series. (This probably doesn't have much impact on the long-term picture: in the productivity report, the BLS reports a long history of the workweek for all workers in the nonfarm business sector, and it generally tracks the series for production and nonsupervisory workers quite closely.)

Both measures of the workweek are up 0.3 hour from their lows reached last year. As alluded to earlier, in terms of total hours worked, this is equivalent to the private sector adding over a million new jobs. Of course, the private sector is still quite far from adding a million jobs. The preference among business to increase the amount of labor used by bringing part-time workers up to full-time status rather than increasing overall headcount is probably a symptom of some lingering caution on the part of managers toward the durability of the recovery.

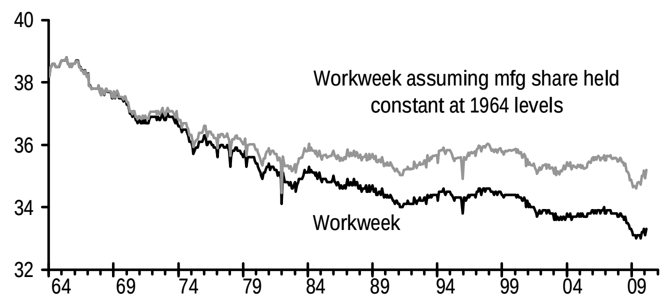
If the pattern of the past two cycles is any indication, it seems likely that this caution will melt away only slowly, and so further increases in the workweek may well remain the preferred means by which business increases its use of labor inputs. Another factor that has sometimes been mentioned as an incentive for business to increase labor usage through increasing average hours worked rather than headcount is the prospect of additional employer cost mandates, particularly relating to health care. This story has some merit: as the fixed cost per employee increases due to requirements to fund health insurance, firms will find it more efficient to employ fewer workers but work them more intensively. While the story is consistent, it is also hard to prove or disprove. Moreover, the mandate in the recently passed health care legislation that would fine employers for each employee that is on government-funded health care does not go into effect until 2014, a horizon far enough away that it may limit the degree to which it is affecting current headcount versus workweek decisions.

Trend and cycle

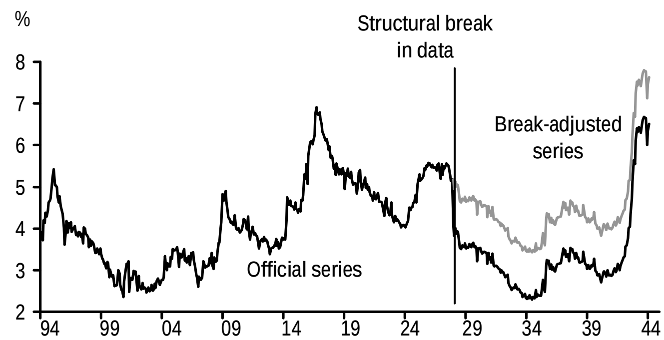
There has been a persistent downtrend in the average workweek, a fact that complicates the question of to what level the workweek will return when it returns to normal. To answer this question, it is helpful to understand the forces that have pushed the workweek down over time. There are two related compositional forces that have probably played a big role in the trend decline in the workweek. First, the manufacturing workweek is longer than the non-manufacturing workweek. As the manufacturing share of employment has declined, the average workweek has correspondingly gone down. This accounts for about one-third of the decline in the workweek since the data began in 1964. Second, the average male workweek is longer than the average female workweek by about five or six hours. (Some caution is warranted here: the data on the workweek by gender is from the household survey, and there are reasons to believe that the data quality is low for the household survey measure of the workweek.) As the female share of the workforce has increased, this has lowered the average workweek by about three-quarters of an hour.

Effect of declining manufacturing on average workweek

Hours, sa, private nonfarm production and non-supervisory workers



Working part-time for economic reasons as a share of employment



In thinking about where the workweek “should” go when it returns to normal, it is useful to note that over the past 30 years, when the compositional effect of declining manufacturing is removed, the average workweek is virtually trendless, with the remaining variation mostly cyclical. Given the relatively decent prospects for manufacturing currently, we don’t think the trend should be a big influence, and so we think that as the recovery continues, the workweek should return to near where it was before the recession: around 33.8 hours for the production worker series (compared to 33.3 hours currently) and 34.6 hours for the all-employees series (compared to 34.0 hours now).

A recovery to a more normal workweek would mean an increase in hours worked of between 1.5% and 1.8%, depending on which measure you use. In terms of labor income, that is equivalent to about 2.1 million new full-time jobs. In most recessions, the workweek recouped much of its loss within 18 months after the trough of the cycle. The decline in the workweek was particularly severe this time, so it may take longer to climb out of the hole, but it is foreseeable that the workweek could normalize over the next year, particularly since the workweek has already retraced about one-third of the decline experienced during the recession.

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Economic Research Note

Cyclical lift arrives in the Euro area—better late than never

- **Surveys moving up strongly through the spring**
- **Improvement evident everywhere except Greece**
- **Sovereign stress a big downside risk**

Although the Euro area recession ended last summer, the region has not yet experienced any cyclical lift, in the sense that the output lost in the recession is being recovered. GDP gains since last summer have averaged close to 1%, slightly below our estimate of potential (see the special report "The long slide in Euro area growth potential is likely to continue," March 25, 2010).

But, the situation looks to be changing dramatically as we go through the spring. Business surveys suggest that GDP growth is accelerating and that from the second quarter onward it will run at a well-above-potential pace. Our view is that this move reflects more than the impact of transitory forces, such as the inventory cycle. If this judgement is right, it will come as a pleasant surprise to both the ECB and the consensus.

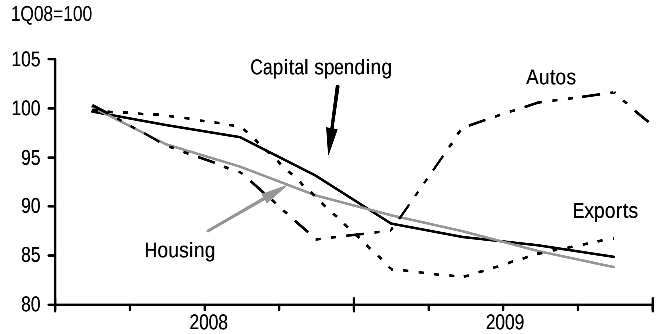
Clearly, the sovereign stress in the region has the ability to derail the cyclical upswing. For now, our judgement is that the cyclical forces will dominate. But, this may require more decisive policy action than appears to be on the table at the moment.

The case for cyclical lift

Since the recession ended last summer, our forecast for Euro area growth has sought to calibrate the interaction of two huge forces at work. On the one hand, the depth of the recession and the extensive policy support looked to be creating the conditions for a strong cyclical upswing, as exports, durables spending, and inventories bounced from very depressed levels. On the other hand, the huge secular headwinds—a more cautious attitude toward debt accumulation, deleveraging by banks, fiscal tightening, and sliding growth potential—looked likely to dampen the growth dynamic for an extended period.

Our growth forecast has combined these cyclical and secular forces by looking for an upswing that would be robust relative to the consensus, but muted relative to the depth of the recession and the degree of policy support. Our judgement has been that the secular headwinds would not pre-

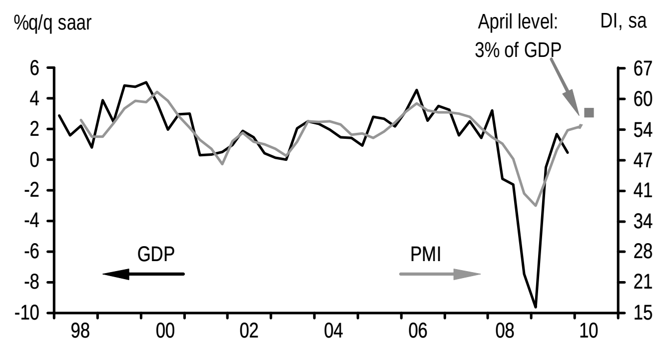
Euro area: spending on durables and exports



Growth in the 2000s business cycle (4Q00 to 2Q07)

	Average of business cycle	Latest reading
GDP %q/q, saar	1.9	0.2
Manufacturing output %q/q, saar	1.8	7.3
Manufacturing PMI index	53.2	61.3
Service PMI index	53.8	55.5
Composite PMI index	53.6	57.3
IFO overall index	95.6	101.6
IFO current conditions index	94.7	99.3
IFO expectations index	96.7	104.0
Consumer confidence % bal	-11.1	-15.0
Consumer major purchases % bal	-17.2	-21.4
Composite PMI employment index	50.2	49.6

Euro area GDP and the composite PMI output



German export expectations and export orders

vent a robust cyclical upswing, but they would limit its strength relative to what would otherwise have occurred.

In the event, our expectations over the past nine months have been disappointed. Although the industrial sector has lifted strongly—since last summer industrial production has grown at an average annualized pace of over 6%—the gain in GDP has been subdued. Our current expectation of a 1.5% annualized gain in GDP in the first quarter would put the average growth rate in the first nine months of the recovery at 1.1%.

The arrival of cyclical lift

It is not entirely clear why the upswing has been so subdued so far. Global trade and spending on autos have bounced strongly. Admittedly, the sovereign stress is a headwind that we did not anticipate last summer, but that has only really been a factor since the end of last year.

In any event, things look to be changing as we go through the spring. Business surveys have moved up dramatically: over the past two months, the composite PMI has risen 3.7pts (a 1.7 standard deviation move) and the German IFO survey has risen 6.3pts (a 3.0 standard deviation move). To the extent that we can tell what is happening on the expenditure side, it looks like the uplift is being driven by exports and corporate spending. Household spending looks to be lagging, but consumer sentiment has improved and the composite PMI employment index is close to the average of the last business cycle, during which employment growth averaged 1.1% ar and consumption growth averaged 1.6% ar.

The downside risks

All other factors held constant, the momentum in the business surveys might suggest upside risk to our forecast that GDP growth will average 2.3% ar over the coming year. However, the intensification of the sovereign stress in the region is clearly a major downside risk to the cyclical growth dynamic. In addition to the direct effects of fiscal tightening and lower asset prices on Greek growth, there are two major channels of contagion. First, the increased spreads in other sovereign debt markets could add pressure for further fiscal tightening. The degrees of fiscal tightening in Spain, Portugal, and Ireland this year, as outlined in the respective stability programs, are modest relative to what Greece is doing. But, this could change. Indeed, the Portuguese government has announced already that it will tighten more. And second, the decline in bond prices is putting pressure on bank capital positions around the region, which could influence credit availability.

German capital goods orders

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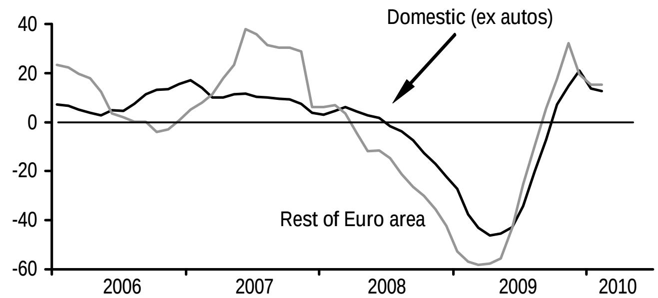
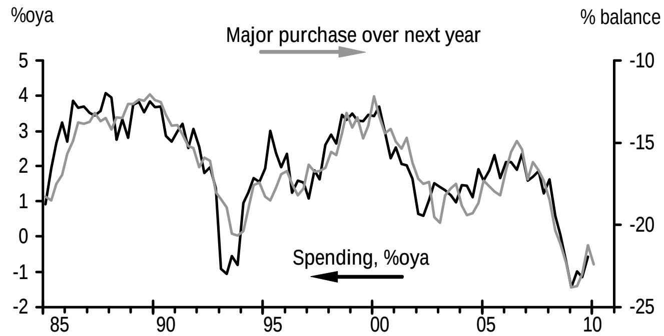


Euro area consumer spending and confidence



Fiscal thrust across Euro area

%-pt change in cyclically adjusted primary positions
A positive is a move to tightening

	2010	2011	2012
Germany	-2.6	0.3	1.5
France	-0.1	2.0	1.0
Italy	0.1	0.8	1.0
Spain	2.3	2.3	1.9
Netherlands	-1.4	0.9	0.5
Belgium	1.3	0.5	0.8
Portugal	1.1	2.2	2.0
Greece	7.0	3.4	2.5
Ireland	1.0	1.0	2.3
Finland	-1.5	0.6	0.1
Austria	-1.1	0.5	0.7
Euro area	-0.3	1.2	1.3

For now, we are sticking to the view that the cyclical lift coming from the shift away from retrenchment toward expansion will dominate the deleveraging, fiscal, and structural drags. The areawide lift in the survey data is evident everywhere except in Greece, which suggests that the contagion has not yet reached a level sufficient to impact growth either in Spain, Portugal, and Ireland or in the rest of the region. But, a further buildup in stress without a corresponding policy response could mean that the long-awaited cyclical uplift turns out to be short-lived.

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Economic Research Note

Japan: BoJ to ease more even as economy improves

- **BoJ eases policy even when the economy is recovering to promote exit from deflation**
- **The main channel for boosting the economy is through a weaker yen**
- **BoJ to announce in June a new measure to promote bank lending, along with government's growth strategy**

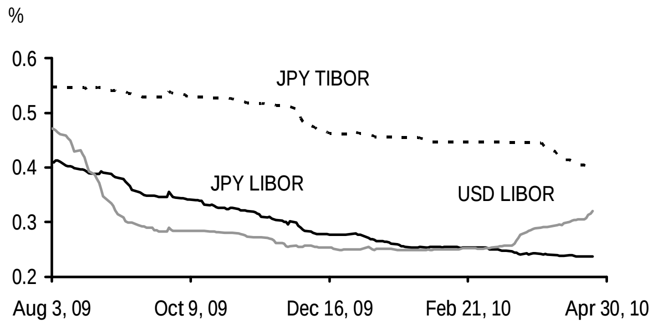
The BoJ eased monetary policy further in March by increasing the amount of liquidity provided through its fixed-rate operations to ¥20 trillion from ¥10 trillion, "to prompt a fall in the interbank term rates and, accordingly, bank lending rates." Since then, three-month yen LIBOR has fallen further, albeit only modestly. However, three-month yen TIBOR, which is used as a benchmark for bank lending rates, has fallen by even more. In summer 2009, the spread between three-month yen TIBOR and LIBOR was 15bp, but widened to more than 20bp in March 2010, as banks did not want to lower TIBOR, which would squeeze profit margins. But after the BoJ's decision to increase the amount of its fixed-rate operation, TIBOR has fallen, with the spread narrowing to 8bp in April.

BoJ's new response function

The BoJ today surprised market participants by announcing that it would adopt new measures "to support private financial institutions in terms of fund provisioning with a view to strengthening the foundation of economic growth." While the details of the new measures were not released, the important aspect of both the March and the April decisions is that the BoJ eased policy even as it upgraded its assessment of the economy and prices. Previously, the BoJ had eased policy only when its assessment of current conditions and/or outlook had been revised down. Consequently, it would seem that the BoJ's policy response function has changed.

Today's BoJ policy statement confirmed the board members' consensus that "Japan's economy faces the critical challenge of overcoming deflation and returning to a sustainable growth path with price stability." This is a relatively clear message from the BoJ that, even though the economic recovery has been stronger than expected, the bank now appears to want to accelerate the pace of the recovery in an attempt to end deflation sooner.

Three-month rates



BoJ's GDP forecast

%y/y	BoJ		J.P. Morgan
	April report	*Old*	
FY2010	1.8	*1.3*	3.0
FY2011	2.0	*2.1*	2.1

BoJ's core CPI forecast

%y/y	BoJ		J.P. Morgan
	April report	*Old*	
FY2010	-0.5	*-0.5*	-1.0
FY2011	0.1	*-0.2*	0.0

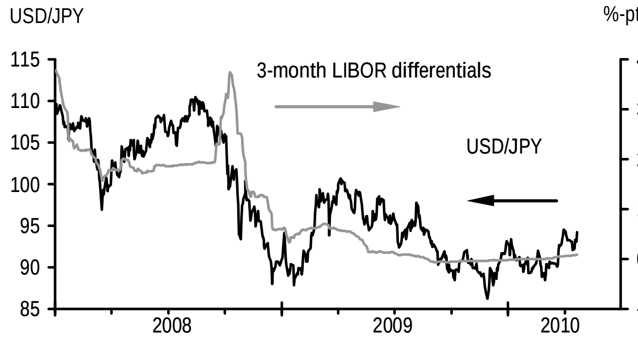
The BoJ's Semiannual Outlook Report, published today, indicated that the median of board members' FY2010 GDP forecast was revised up to 1.8%y/y from 1.3%. In addition, the BoJ now foresees that core CPI deflation will end in FY2011, forecasting 0.1%, up from the previous -0.2%. However, it is still far below the midpoint (1.0%) of the BoJ's de facto inflation target—a "positive range of 2% or lower."

Transmission mechanism

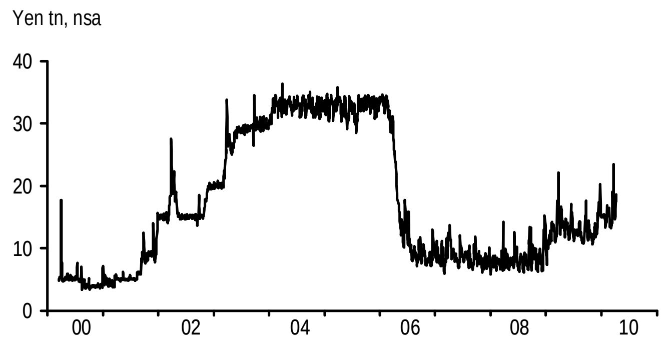
The BoJ's introduction and subsequent increase in the amount of the fixed-rate operation has been intended to lower interbank term interest rates and thereby bank lending rates. However, three-month LIBOR and TIBOR have each fallen just 6bp over the past five months. Consequently, the corresponding impact on bank lending has been extremely limited, especially as the demand for bank loans has been falling. Corporate profits have boosted liquidity even as capex has only begun a gradual recovery. In addition, as bank lending rates in February were, on average, 1.28% for all domestic banks, there is only limited room for any further decline, especially if mean credit risks are taken into account. As an alternative transmission channel, the BoJ is considering weakening the yen through further easing. Further monetary easing in Japan stands in sharp contrast to policy in other major central banks that are beginning to plan exit strategies from their exceptionally accommodative stances. Indeed, the recent movement of dollar/yen can be mostly explained by the short-term interest rate differentials between the US and Japan. The BoJ's accommodative policy appears to have more impact on the yen exchange rate, as the three-month dollar LIBOR started to rise in March. To be sure, increasing the short-term rate differential to one percentage point would have only a limited impact on dollar/yen, but if yen stays around 90-95, this would still be beneficial for exporters, whose assumed dollar/yen rate for FY2010 is around 90.

Meanwhile, according to the BoJ, the role of the size of the central bank's balance sheet is limited in terms of stimulating the economy and eliminating deflation, although the BoJ's current account balance, just like banks' reserves, has risen gradually (second chart). Governor Shirakawa reiterated in a speech that comparing the size of the balance sheet of central banks is not useful to measure the aggressiveness of monetary easing. The BoJ learned from quantitative easing during the period between 2003 and 2006 that an increase in banks' excess reserves did not prompt banks to increase risk assets on their balance sheets. While the size of the BoJ's balance sheet is 25.8% of GDP, larger than the Fed's 16.0% and the BoE's 16.7%, the growth rate of the BoJ's balance sheet is far slower than the Fed's or the BoE's, mainly because, according to the BoJ, the financial crisis was much less problematic in Japan than in the US and the UK.

USD/JPY and short-term rate differentials



BoJ current account balances



What's next?

While it remains to be seen what the new measure to encourage increased bank lending will look like, Shirakawa stated that the BoJ would like to help banks extend loans to those areas in which growth can be expected, such as R&D, environment, and energy-related businesses. Meanwhile, Shirakawa played down the role of the fixed-rate operation as a measure to stimulate the economy. As the markets rely more on the fixed-rate operations and less on ordinary operations, banks find it difficult to manage their liquidity positions flexibly. In addition, narrowing profit margins for bank lending and money market operations discourage financial intermediaries from performing their function and ultimately will result in a much smaller number of financial intermediaries.

The BoJ does not seem to be keen to expand the role of fixed-rate operations further, but, instead, appears to have shifted gears into a type of credit easing that will facilitate lending to corporates. While it appears odd that the BoJ unexpectedly referred to credit easing today, Shirakawa admitted that liquidity is not the constraint facing bank lending, but that the new measure should promote increased demand for loans. As for a timetable, the staff report is expected to be submitted to the Board in June, when the government will announce the details of its growth strategy and medium-term fiscal outlook.

In all, while we believe that the BoJ will ease policy further through this new initiative directed as easing credit, we no longer expect the BoJ to ease policy by extending the maturity or increasing the amount of the existing fixed-rate operations. Instead, we expect the BoJ's new initiative to be announced in June with its objective being to promote economic growth. From a political perspective, the BoJ will unlikely face severe pressure from the government up to the June board meeting. However, ahead of the summer election, some DPJ members may put pressure on the government to urge the BoJ to take more radical measures to end deflation. Some radical members, not only in the DPJ but also in the opposition parties, are arguing for amendment of the BoJ Law to reduce the BoJ's independence. The BoJ's new response function needs to be interpreted against this background of persistently growing political pressure, spreading to a large number of politicians.

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Economic Research Note

UK: the election and beyond

- **Conservative minority dependent on Lib Dem support looks likely (given agreement on electoral reform)**
- **Both parties have an incentive to make coalition work**

Next week's election looks likely to deliver a hung parliament.[1] The defining event of the election campaign thus far has been a surge in support for the Liberal Democrats (Lib Dems), typically the "third party" in UK politics. At the time of this writing, opinion polls are placing support for the Conservatives in the 33%-36% range, with the Lib Dems at 28%-31%, and Labour at 25%-30%. It remains to be seen whether the final televised leaders' debate (April 29), and Gordon Brown's "bigot" gaffe, will meaningfully impact party support,[2] and whether the rise in Lib Dem support will be sustained on election day (May 6) itself. Translating the polls into seats in Parliament is more uncertain than usual given that there have been relatively large shifts in support for each of the three main parties compared to the last election, while the regional wrinkles of the recent rise in Lib Dem support have not been well documented.

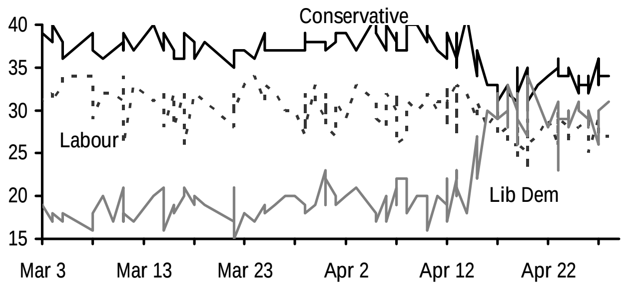
Getting to a new government

Given the possibility of a late swing in support, sampling error in the polls, and luck in the regional breakdown, an absolute majority for the Conservatives cannot be entirely ruled out. If they fall only just short of an absolute majority (polling just over 300 seats but short of 320) they may attempt to govern on the basis of support from Irish, Scottish, and Welsh nationalist parties. While such an arrangement would avoid having to negotiate with the Lib Dems, it would likely generate only a very slim majority. If electoral fortune were to swing otherwise, it is possible that Labour could emerge as the party with the single highest number of seats in Parliament despite coming third in terms of its percentage share of the vote. But the polls suggest the most likely outturn is that the Conservatives emerge as the single largest party with around 290 seats in the 650-seat Parliament, followed by Labour with around 250 and the Liberal Democrats around 85 seats.

Such an outturn would put the Lib Dems in the position of kingmakers. With the Conservatives having the highest vote share and highest number of seats, the Lib Dems have said they would negotiate with them first about forming a government. As we have written before, the Conservative move toward the political middle ground, and shared rec-

Opinion poll support for the three main parties

% of vote for England and Wales



ognition that spending cuts will have to do the bulk of the work in cutting the deficit, creates scope for the parties to cooperate.[3] The main stumbling block, however, is that the increase in Lib Dem support during the campaign has led the party to be more assertive in demands for electoral reform. A system that generates more alignment between share of the vote and seats in Parliament would likely damage Conservative electoral prospects in the future, making Labour-Lib Dem coalition governments more likely. At this stage, it is not clear how these differences could be bridged. But the Conservative negotiating position is weak: in the event that they are not able to reach an agreement with the Lib Dems, then the Lib Dems will begin to negotiate forming a government with Labour.

Lib Dem leader Nick Clegg has stated that he would not support Gordon Brown remaining as Prime Minister if Labour were to come third in the share of the vote. We doubt a change of Labour leadership would be a particular sticking point in the discussions unless Clegg were to push to be Prime Minister himself. It is also more likely that a Labour-Lib Dem agreement would be formalized by the Lib Dems taking senior cabinet positions. A Conservative-Lib Dem coalition would be more likely to proceed on a "confidence and supply" basis, where the Lib Dems do not take cabinet positions but support an initial vote of confidence in a Conservative government and then consider supporting pieces of legislation on a case-by-case basis.

Negotiations between the parties on forming a new government will take place amid pressure to reach agreement as soon as possible. Parliament is scheduled to reconvene on May 19, and the Queen's Speech laying out the legislative program of the new government is on May 25.

1. For more detail on the UK electoral system see "UK Politics: an election year primer," *Global Data Watch*, January 8, 2010.
2. See http://news.bbc.co.uk/1/hi/uk_politics/election_2010/8649853.stm. Polling by YouGov the day after "Bigotgate" does not suggest a big impact on Labour party support.
3. See "UK: A hung parliament can deliver (if it gets a chance)," *Global Data Watch*, March 12, 2010.

Can Cameron-Clegg coalition govern?

There is understandable nervousness over whether a Conservative-Lib Dem government would be effective or have any durability. Coalition government of any kind is not the norm in the UK, and this particular arrangement would seek to bridge widely divergent views on a number of issues. Both parties, however, would have a significant self-interest in making such an arrangement work at the outset.

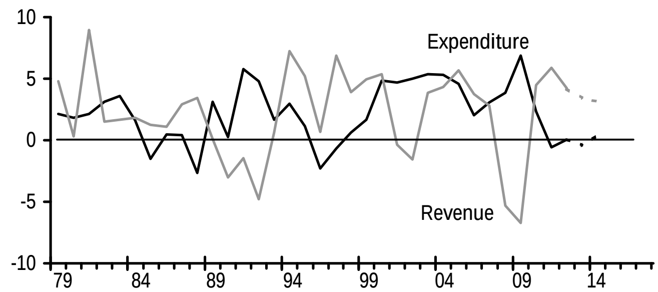
The incumbent prime minister does not have the right to call new elections directly; he or she can only request that the sovereign do so. It is ambiguous whether the sovereign would grant that request early in the term of a new Parliament if a viable government could be formed by other groups (such as the Lib Dems supporting Labour). Even assuming opinion polls were to move in the Conservatives' favor, it is not clear that a quick return to the polls is an option, giving the Conservatives an incentive to make coalition work. The Lib Dems, on the other hand, have the opportunity to demonstrate that their participation in government, for the first time in a generation, is a stabilizing rather than destabilizing force. They also have an incentive to ensure that the new Parliament lasts long enough for a referendum on electoral reform to take place.

On the substance of policy issues, however, there are areas where the stated aims of Conservative and Lib Dem policy are almost diametrically opposed. The Lib Dems are in favor of Euro entry in principle, while the Conservatives have stated they would never give up the pound. The Lib Dem manifesto proposes large-scale changes that would make the tax system more explicitly redistributive, including an annual "mansions tax" on properties valued at over £2 million. Conservative manifesto pledges to raise the threshold for inheritance tax to £2 million cut in the other direction. Certainly, any viable Conservative- Lib Dem administration will require the larger partner to reach back to pre-Thatcherite notions of "one nation" Conservatism. But on a number of issues the parties' policies are more closely aligned: both would seek to reverse some of the centralization of expenditure control and limits to civil liberties that have occurred under Labour. And in the economic space, both have argued that the budget deficit needs to be reduced faster than Labour has planned, and that the fiscal process needs institutional change to enhance its credibility.

As the Institute for Fiscal Studies has pointed out, the more than 11% of GDP budget deficit has cast a shadow over the election, but none of the political parties have offered much detail as to how they would deal with it. Much has been made of Conservative plans to reduce spending by £6 billion this fiscal year in order to prevent increases in social contributions next year, but at 0.4% of GDP that change is relatively small. The Lib Dems have outlined plans for £15 billion of savings in addition to those planned by Labour, £10 billion of which would be used to cut the deficit. They have argued that deficit-cutting measures should depend on economic conditions, and their "working assumption" is that the recovery would be strong enough for these to begin in 2011. However, Labour's current set of plans already embodies a 1% of GDP structural tightening this year, and the Lib Dems have not argued against that. These differences in the timing of fiscal consolidation do not appear particularly material. Indeed, both parties have suggested the overall fiscal envelope should be set with reference to external input: the Conservatives through the creation of an "Office for Budgetary Responsibility," the Lib Dems via a "Council for Financial Stability." Negotiations on specific expenditure-reducing and revenue-raising measures will inevitably be difficult, but Lib Dem involvement may offer a broader base of public support.

Labour's current tax and spending plans

%oya, real, dotted lines denote forecasts



Labour-Lib Dem may worry markets more

Should the Conservatives and Lib Dems be unable to resolve their differences and form a government, then a Labour-Lib Dem coalition would ensue. This arrangement would give less priority to clarifying the fiscal outlook soon after the election (Labour plans simply to conduct a Comprehensive Spending Review in the summer). The debt rating agencies are looking at minimum for more detail on the coming fiscal consolidation (Moody's), and also for an acceleration in the pace from current plans (Fitch, S&P). A Labour-Lib Dem coalition would arguably be stabler over time, and our expectation is that it would deliver fiscal change. But it is more likely in this case that pressure from financial markets to detail the fiscal outlook would play a role in the near term.

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Economic Research note

Turkey: strong tourism performance to persist

- **Diversification of export markets and success in tourism should limit the widening in CAD**
- **Turkey has managed to increase its share of global tourism despite the recession in source markets**
- **Turkey needs to invest to exploit its potential fully**

Turkey's current account deficit contracted dramatically to US$14.0 billion (2.3% of GDP) in 2009 from US$41.5 billion (5.7% of GDP) in 2008. Four factors were mainly responsible for this contraction: 1) a sharp weakening in domestic demand, 2) lower energy prices, 3) diversification of export markets, and 4) strength in tourism performance. However, with the recovery of domestic demand and higher energy prices pushing imports up, the current account deficit started widening once again in the last months of 2009. While the first two factors have lost their significance, the other two will continue to support Turkey's external balance, and help to keep the current account deficit comfortably below the 5% of GDP mark in the coming years. We see the deficit widening to US$28.8 billion (3.9% of GDP) in 2010 and to US$37.1 billion (4.2% of GDP) in 2011.

Turkish exporters have proven skillful at diversifying their export base. The economic slowdowns in the EU and in Russia have been a drag on Turkey's export prospects, but the impact has been mitigated by Turkey's ability to diversify its export portfolio. EU countries remain Turkey's main trading partners, but since end-2007, their share has declined sharply to 46% from 56%. In contrast, the export share of Middle Eastern countries rose to 19% from 14%, and that of African countries rose to 10% from 5.5%. Although less important, Turkey's exports to non-EU Europe and Asia also performed better during this period. This diversification of export markets is likely to continue.

Higher share in global tourism

Tourism revenues have recently been increasing their share in Turkey's total exports of goods and services, rising to 15% in the past 15 months from 12% (first chart). As exports of goods pick up, we expect this ratio to remain stable in the coming months. Given the deep recession in many of the major source markets, Turkey's superior performance in tourism deserves special attention. According to data from the World Tourism Organization, the total number of tourists declined 4.3% in 2009. In contrast, there was a 3.3% increase in the number of tourist arrivals in Turkey in 2009. In fact, Turkey was the only G-20 country securing a rise in tourist arrivals. As a result, Turkey's share in global tourism rose to 3.6% from 3.4%. Importantly, this success was achieved when Turkey's top three source markets—Germany, Russia, and the UK—were in deep recession. Despite the recession at home, 12% more UK citizens and 1.6% more German citizens visited Turkey in 2009. Importantly, similar to the case with exports, Turkey managed to diversify its source markets for tourism. The number of tourists coming from Iran and Bulgaria rose 22% and 12%, respectively. As a result, these countries are among Turkey's top 10 source markets. This trend is likely to continue as Turkey improves its relations with its neighbors.

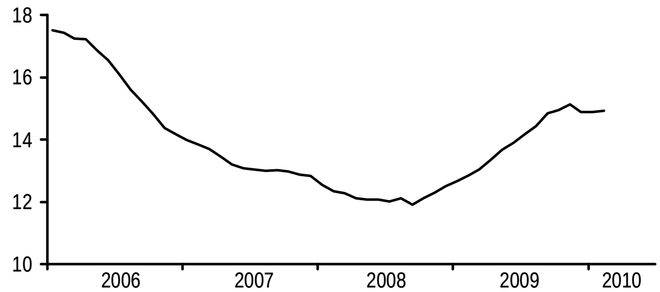
Current account balance

% of GDP

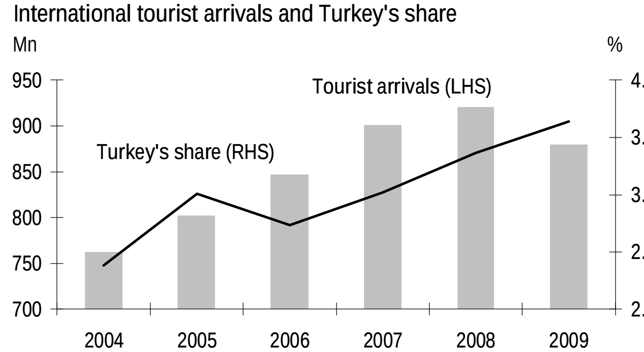
	2008	2009	2010	2011
Current account balance	-5.7	-2.3	-3.9	-4.2
Trade balance	-7.3	-4.1	-5.8	-6.1
Exports	19.3	17.9	16.8	16.9
Imports	26.6	22.0	22.6	23.0
Services balance	2.4	2.6	2.7	2.5
o/w tourism income	3.0	3.5	3.4	3.5
Income balance	-1.1	-1.3	-1.1	-1.1
Transfers	0.3	0.4	0.3	0.2
Net errors and omissions	0.7	1.4	0.7	0.0

Tourism revenues

% of exports of goods and services



International tourist arrivals and Turkey's share



The decline in global tourism revenues was even more pronounced because the declining number of tourists also began to prefer less expensive destinations and shorter holidays, and spent less money while on holiday. Turkey benefited from being a relatively cheap destination and did not feel the impact of the other two factors. In particular, tourists, on average, spent 10.6 days in Turkey in 2009. This was marginally higher than the 2008 level of 10.5 days. Similarly, spending per tourist rose sharply to US$714 at the end of the year from US$615 at the beginning of the 2009 tourism season.

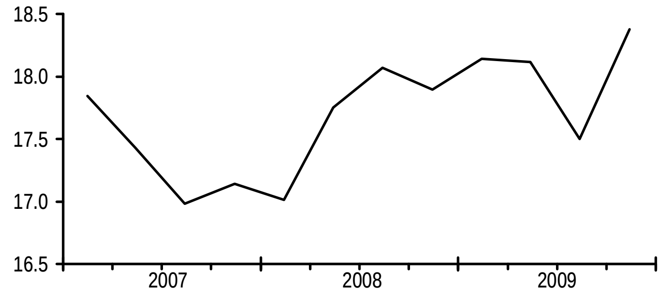
Turkey's success can at least partly be attributed to the increasing share of package tours. A package tour is a tour arranged by a travel agent in which transportation, lodging, and food are all provided at one price. The main advantage of buying a package tour is that the purchaser knows with a reasonable degree of certainty what the total cost of the holiday will be. This is especially advantageous when people face uncertainties about future income flows. Package tours comprised 17% of Turkey's total tourism income in 2007, and rose to 18.5% in 2009 (first chart). Given the continued problems in source markets, we expect this ratio to continue rising this year.

Exploiting the potential

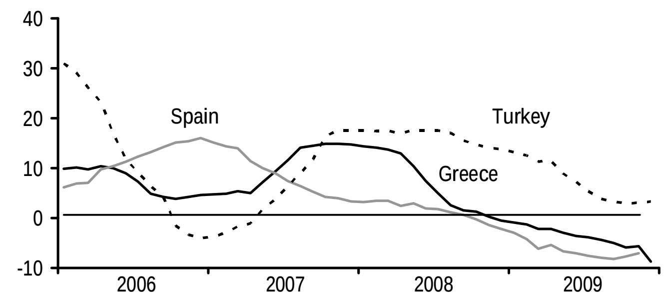
Turkey has shown its competitive power in the past few years, but more needs to be done in order to exploit the country's huge potential. In recent years, Turkey has been consistently performing better than Greece and Spain, its two competitors in the Mediterranean region. The number of tourists visiting Greece and Spain fell 8.7% and 7.0%, respectively, in 2009. In contrast, Turkey secured a 3.3% increase in 2009 and 11% in the first quarter of 2010. Whether this outperformance could be sustained depends critically on Turkey's competitiveness. It is, however, quite difficult to gauge the competitiveness of the services sector.

The only existing comprehensive indices on travel and tourism are the competitiveness indices developed by the World Economic Forum. Countries are ranked according to a number of factors influencing the country's general tourist competitiveness such as natural and cultural resources, transport infrastructure, health and hygiene, safety and security, and prices. These individual rankings are then combined into a general competitiveness ranking. Rankings are shown on an ordinal scale, thus providing information on the relative positioning of countries, but not on the magnitude of the differences between countries. According to the 2009 results, Turkey is ranked 54th among 133 countries in terms of general competitive power in tourism. This is significantly below Spain (ranked 6th) and Greece (ranked 24th) (see table). The results support the conclusion that Turkey has high potential, but needs to improve its infrastructure. For instance, Turkey ranks 17th in terms of cultural resources and 23rd in terms of natural resources. However, the country ranks 100th in safety and security, 84th in environmental sustainability, and 77th in human resources, showing the need for further investment. In fact, tourism is likely be a major target for FDI inflows and will also be a generator of new employment in the coming years. Finally, there is need for diversification of tourism products. The country has already proven itself in coastal tourism but needs to continue to develop alternatives such as winter, eco-, or cultural tourism.

Package tour income
% of total



Number of tourists
%oya



Measures of competitiveness
Rank in 133 countries

	Greece	Spain	Turkey
Competitiveness index	24	6	56
Environmental sustainability	67	36	84
Safety and security	73	102	100
Health and hygiene	39	1	63
Air transport infrastructure	40	34	55
Ground transport infrastructure	47	30	54
Tourism infrastructure	4	7	64
Price competitiveness	83	63	57
Human resources	82	52	77
Affinity for travel and tourism	16	53	42
Natural resources	23	7	23
Cultural resources	9	2	17

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Economic Research note

Thailand: tracking the impact of politics on the economy

- **Sentiment indicators have taken a dip following recent political uncertainty**
- **Comparison with the political uncertainty in 2006 provides a useful baseline**
- **A quick resolution would imply a limited hit to headline growth even as underlying composition shifts**

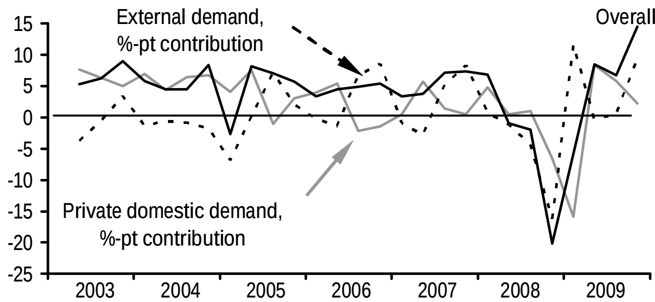
The recent data flow out of Thailand has been uniformly strong, with both external and domestic demand recovering robustly. Of note, domestic investment recovered solidly in 2H09 and this strength continued into 1Q10. However, the recent political uncertainty could throw a spanner into the wheels of domestic activity. If the current situation is resolved as rapidly as the 2006 crisis, then the implications to the economy should be limited. The key risk to this otherwise benign view is that the likelihood of a violent showdown is not negligible. Indeed, if this were to be followed by a political impasse wherein economic policy remains unclear, this would also affect growth more than in the 2006 episode.

In the past few years, domestic demand in Thailand has been a contributor to sequential growth, with the exception of three recent episodes: the recent crisis in 2008/09, the political crisis in 2006, and the hike in domestic energy prices in mid-2005 (first chart). To frame the likely impact of recent political events on growth, it is worthwhile analyzing the impact of the 2006 political crisis on Thailand's economy (see grey box). In comparing the 2006 political crisis with the current crisis, it should be remembered that following the 2006 crisis, normalcy was restored relatively quickly and, even though political fissures remained, they did not manifest in a disruption of day-to-day economic activity. The uncertainty lasted for around two quarters from April to October 2006, with an interim government established by October following the September coup.

With this chronology in mind, the 2006 crisis did not lead to a material decline in headline GDP growth, as a boost from net exports offset the slowdown in domestic demand. If a similar dynamic were to transpire in 2010, this would suggest that the extant headline forecast can remain unchanged even as the underlying composition of demand shifts. Indeed, our forecast assumes GDP growth for the rest of 2010 averaging 4.2%q/q saar, which is below the 4.6%q/q saar average in 2006 and well below the average growth rate of 5.3% during the previous upturn. Moreover, unlike the 2006

Contribution to real GDP growth

%q/q, saar



Summary of the 2006 political crisis

Political opposition to then-Prime Minister Thaksin began to build among the Bangkok political elite in 3Q05. The noise was turned up in January 2006 after Thaksin's family sold its remaining stake in Shinawatra Corporation amid accusations of an inappropriate exemption from paying taxes on gains from the sale. The ensuing political crisis was marked by mass demonstrations in Bangkok and eventually led to a set of elections in April, which resulted in a landslide victory for Thaksin's political party. However, due to other considerations, Thaksin resigned as Prime Minister, leaving a political vacuum. The army then launched a coup in September 2006 to resolve the political impasse. Following the coup, sentiment took a turn for the worse, which led to a contraction in private domestic demand in 2H06. Of note, even during the buildup to the coup, domestic demand had held up reasonably well, growing 5.2%q/q saar in 1Q06 and 7.2%q/q saar in 2Q06.

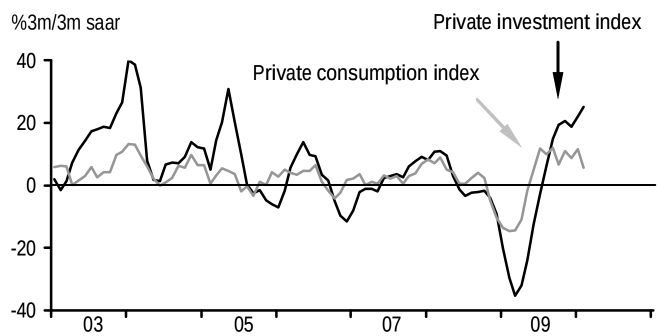
Contribution to real GDP

%q/q, saar for headline and %-pt contribution to growth for components

	1Q06	2Q06	3Q06	4Q06	1Q07	2Q07
GDP (1+2+3)	3.4	4.5	4.9	5.4	3.4	3.8
1. Priv. dom. demand	3.9	5.4	-2.1	-1.4	0.5	5.7
Consumption	2.6	2.1	0.2	0.3	1.2	1.1
Capital formation	1.3	3.3	-2.3	-1.7	-0.7	4.6
2. Govt. cons.	-0.4	0.4	0.3	-1.7	3.8	0.9
3. Net exports	-0.2	-1.3	6.7	8.5	-0.9	-2.8

Private investment and consumption indices

%3m/3m saar



crisis, which occurred three years into the global recovery, the recent upturn remains fairly nascent and has solid momentum behind it. This also suggests that domestic demand might not be marked down as much as it was in 2006 unless the political crisis worsens significantly.

The 2006 crisis and its impact

The political crisis in 2006 was characterized by mass protests in Bangkok in 1Q06 followed by a snap election in 2Q06 and finally a coup in 3Q06, which then saw the appointment of an interim government in 4Q06. Of note, despite the increase in political uncertainty, domestic demand grew relatively strongly, adding 3.9%-pts and 4.5%-pts to sequential growth in 1Q06 and 2Q06, respectively. It was only in 3Q06 that domestic demand began to falter, reflected in a drop in private investment, which continued to soften into 4Q06. Of note, while consumption also softened, the amplitude of the swings was noticeably smaller relative to investment (second chart previous page).

In terms of the shock, private domestic demand fell 0.7%q/q sa in 3Q06 and another 0.5%q/q sa in 4Q06. With domestic demand accounting for around 76% of GDP, the estimated hit to overall GDP was in the range of 0.3%-0.5%-pt per quarter, which was more than offset by the increase in net exports. What is also interesting is that the unrest was generally localized in Bangkok—had it spread beyond the city, the hit to activity would likely have been larger. Another aspect of the 2006 crisis is that policy uncertainty lasted for a relatively short time, between April and September. The policy uncertainty likely hindered investment plans; this was also reflected in the decline in government consumption, which should otherwise have provided a counter-cyclical boost. The fiscal stimulus materialized only in 1Q07 after politics had calmed and an interim government was established, but, more importantly, private sector activity rebounded relatively quickly thereafter, suggesting resilience to the disruption.

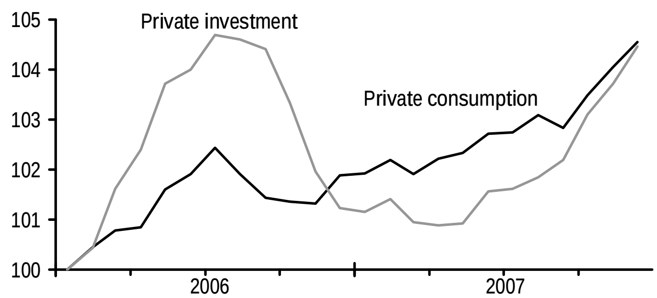
A closer look at the impact points

In this context, consumption recovered as early as 4Q06 while investment only recovered two quarters later in 2Q07 (first chart). The high-frequency private domestic demand data provide sufficient granularity to determine which sectors were most affected by the coup.

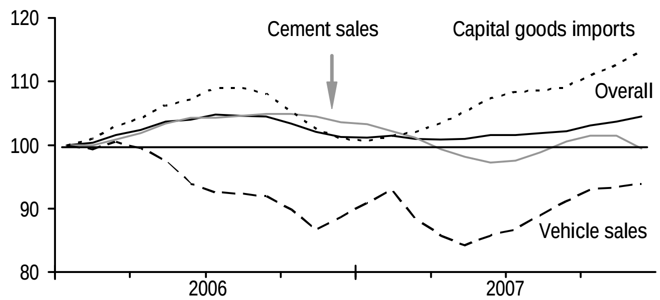
In terms of the investment downturn, all sectors were affected, with particularly large declines in vehicle sales and cement demand. Although imports of capital goods also declined, they recovered in 1Q07 ahead of the recovery in either vehicle or cement demand (second chart). By contrast, while consumption also softened, the declines were more modest and the recovery more rapid, reflected in the relatively quick recovery in real VAT receipts and increase in consumer goods imports (third chart). However, car sales continued to languish through 1Q07 and staged a tentative recovery in 2Q07. The upshot is that discretionary expenditure will likely be most affected by political uncertainty even as demand for basic consumption items remains fairly resilient.

In terms of the data flow, the high-frequency private domestic demand indicators, released at the end of each month with a one-month lag, should be watched to determine the impact of recent events.

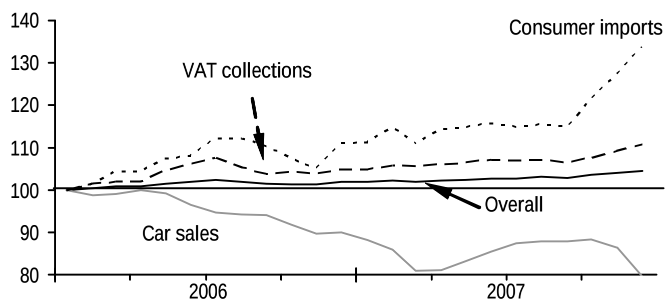
Private investment and consumption indices
Index, Jan 2006=100, 3mma, sa



Private investment index
Index, Jan 2006=100, 3mma, sa, real terms



Private consumption index
Index, Jan 2006=100, 3mma, sa, real terms



United States

- **Real GDP up 3.2% saar in 1Q10**
- **Forecast looks for a turn to 4.0% growth this quarter and next despite less help from inventories**
- **Upcoming April ISM, auto sales, and labor market reports are expected to confirm stronger growth**

The first estimate of 1Q10 real GDP shows that the economy advanced 3.2% at an annual rate. Real consumer spending (3.6% saar) and business spending on equipment and software (13.4%) posted solid gains, while housing and nonresidential construction continued to decline at a double-digit pace and real state and local spending (-3.8%) contracted for the third consecutive quarter. Real inventories increased ($31.1 billion) for the first build since early 2008.

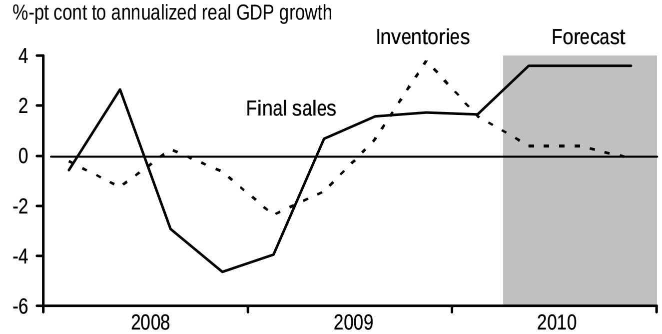
The forecast looks for an acceleration in real GDP growth to a 4.0% pace both this quarter and next quarter, despite a sharply reduced contribution to growth from inventories. Importantly, a wide range of economic reports indicate that the economy strengthened toward the end of last quarter and into April, in line with the forecast. This view will be tested next week with the first batch of comprehensive economic data for April. Both ISM surveys reached their highest levels of the expansion to date in March, and the forecasts look for further gains in April to 61.0 for the manufacturing survey and to 57.0 for the nonmanufacturing survey. April auto sales are expected to edge up to 11.9 million saar, well above the 11.0 million average sales pace in the first quarter. And the labor market report is expected to show a further acceleration in private sector payrolls, to an increase of 85,000 in April from an average 49,000 in the first quarter.

The advance GDP report confirms that solid growth is being accompanied by a slowdown in core inflation. The core PCE price index slowed to only 0.6% saar in 1Q10 (a new quarterly low for this series dating back to 1959) and to 1.4%oya. The market-based PCE price index, a measure that excludes imputed prices including the price of free financial services (such as use of ATM machines) slowed to only 0.3% saar and 1.2%oya. The overall GDP price index rose 0.9% saar and 0.4%oya.

One influence that has been contributing to low core inflation is last year's dramatic 4.7% decline in unit labor cost (4Q/4Q). With payrolls and the workweek now expanding, productivity is bound to slow and unit labor cost will not remain in a free fall. But data in hand point to a 1.4% saar decline in unit labor cost in 1Q10, and the forecast expects modest declines on average for all of 2010—a force for

Contribution to real GDP growth: final sales and inventories

%-pt cont to annualized real GDP growth



ISM manufacturing survey with April forecast

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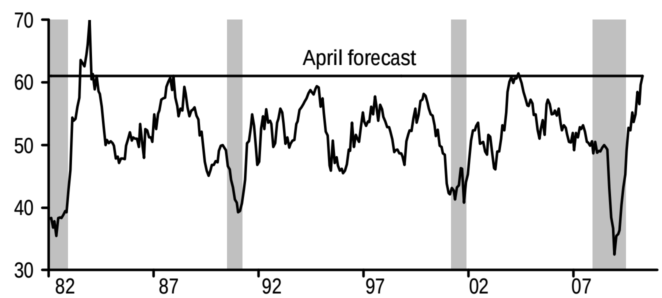


Employment cost index, private-sector

%ch saar

continued low core inflation. To be sure, the private sector ECI did increase 0.6% saqr in 1Q10, a larger increase than the recent trend. But the acceleration appears mainly to reflect nonrecurring company contributions to beef up defined-contribution benefit plans rather than ongoing cost pressures. The ECI measure of wages and salaries slowed to 1.4% saar and is running only 1.5%oya.

Another quarter of GDP growth

The new information in the GDP report does not change the forecast of 4.0% growth this quarter, but the composition has been changed slightly to a bit more final sales growth and a bit less of a contribution from inventories.

Real consumer spending rose at a 3.6% pace last quarter despite a slight decline in spending on motor vehicles and parts. Anecdotal April reports point to levels of both auto sales and core retail sales that are well above their 1Q10 averages. Consequently, the forecast for 2Q10 real consumer spending is being lifted to 3.3% saar (from 2.8%).

Real business spending on equipment and software posted a double-digit gain for the second quarter in a row. And strong March reports on production of business equipment and core capital goods orders point to another strong gain this quarter. (The forecast is for 12.0% saar this quarter, only slightly slower growth than in 1Q10.)

Net exports subtracted 0.6%-pt from annualized growth in the first quarter as real exports slowed more than imports, to growth of 5.8% in 1Q10 from growth averaging roughly 20% in the prior two quarters. The forecast looks for a return to double-digit export growth and a contribution from net exports this quarter, based partly on March ISM survey readings that show new export orders in manufacturing (61.5) and nonmanufacturing (57.5) that were new highs for the expansion and well above their 1Q10 averages.

Housing contracted at a 10.9% pace in 1Q10, but housing starts have increased in the three months through March, and housing looks poised for a modest gain this quarter.

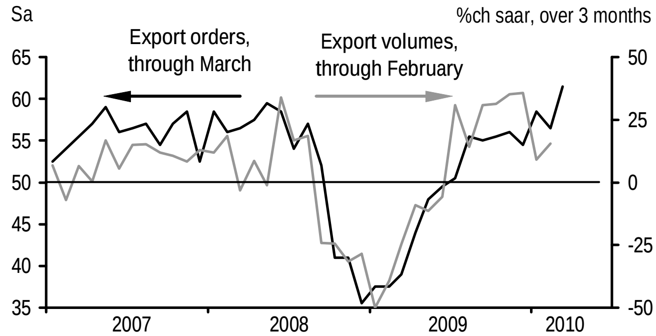
The March ISM nonmanufacturing survey and payroll reports confirm a broadening in growth, but there are still lagging sectors. Investment in nonresidential structures posted a fifth consecutive quarter of double-digit declines in 1Q10 and is expected to continue to contract through the end of the year. Total government spending is likely to remain weak, as state and local governments especially remain under intense financial pressure. And with inventories now growing at a decent pace, the contribution to annualized growth from the turn in the inventory cycle is apt to slow to less than 0.5%-pt over the next few quarters from an average 2.0%-pt in the first three quarters of the expansion.

Manufacturing gaining strength into 2Q

The release of next week's key April reports including the ISM business surveys and the labor market report will be important in conditioning views of activity early in 2Q10. And the early April business surveys point to continued strength.

The bulk of the April surveys in hand is Fed regional manufacturing surveys. And these have generally gotten stronger. In addition, today's Chicago PMI (which is not a Fed survey) increased 5.0pts to 63.8, with good gains in the measure of both new orders (65.2) and employment (57.2).

ISM manufacturing export orders and export volumes



Fed regional manufacturing surveys, derived composite

Sa

	Jan	Feb	Mar	Apr
New York	53.5	52.3	57.1	59.6
Philadelphia	52.5	55.1	52.8	53.4
Dallas	51.8	48.5	52.2	55.0
Richmond	50.8	50.9	53.0	61.0
Kansas City	52.5	53.7	54.7	54.7

Note: The derived composite is calculated from components using ISM weights.

All in all, it appears that the ISM manufacturing survey for April (Monday) should rise at least modestly from the elevated 59.6 reading in March, and the forecast looks for an increase to 61.0. Note that this would put the ISM manufacturing index at an extremely high level. There have only been two episodes of a reading as high as 61.0 in the past 25 years, in 2H87 and 1H04.

The only regional Fed survey that bears on nonmanufacturing activity is the Richmond Fed service firm survey. The Richmond Fed and ISM nonmanufacturing surveys have tended to trend together over time, but the Richmond Fed services survey has been much weaker over the past year. In April, the Richmond survey jumped from 0 to 9, the highest reading since June 2007; along with stronger consumer and housing indicators lately, this is a good reason to expect an increase in the ISM nonmanufacturing survey (Wednesday).

Data releases and forecasts

Week of May 3 - 7

Mon
May 3
8:30am

Personal income

%m/m sa, unless noted

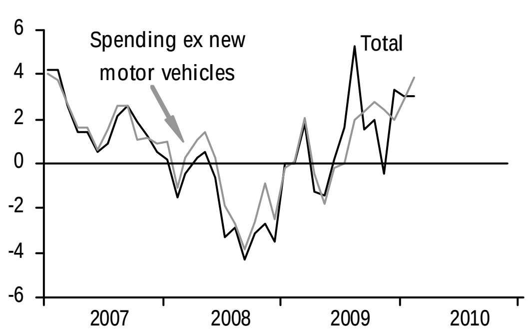
	Dec	Jan	Feb	Mar
Personal income	0.4	0.3	0.0	0.5
Wages & salaries	0.0	0.4	0.0	0.4
Consumption	0.4	0.4	0.3	0.5
Real consumption	0.2	0.2	0.3	0.4
PCE price index	0.2	0.2	0.0	0.1
Core	0.11	-0.01	0.03	0.08
Mkt-based core	0.1	0.0	0.1	
Core (%oya)	1.6	1.5	1.3	1.3
Mkt-based core (%oya)	1.6	1.4	1.2	
Saving rate	4.0	3.4	3.1	2.9

A bounceback in hours worked in March after a storm-depressed February should support a 0.6% increase in wages and salaries. We look for overall personal income to increase 0.5%, less than the rise in wages and salaries as softness in personal income receipts on assets and proprietors' income holds back some of the gain. We expect nominal disposable income to increase 0.5%; a level shift up in taxes in January depressed disposable income for the quarter, but BEA's assumption for taxes for months other than January tend to be modest. Real disposable income is expected to increase 0.4%, as we think the headline PCE price index will rise 0.1%. Following the very soft core CPI and trend-like medical care prices in the PPI, we expect the core PCE price index will increase 0.08%, keeping the over-year-ago core PCE deflator running at 1.3%.

Nominal consumer spending is expected to increase 0.5%, supported by the 14.5% increase in light vehicle sales as well as the solid 0.4% increase in sales in the retail control category. Outlays on utilities probably fell in March as the weather turned milder. There will likely be upward revisions to February real consumer spending as well.

Real consumption spending

%ch over 3 months, saar



Mon
May 3
10:00am

ISM manufacturing survey

Sa

	Jan	Feb	Mar	Apr
Overall index	58.4	56.5	59.6	61.0
Production	66.2	58.4	61.1	
New orders	65.9	59.5	61.5	
Inventories	46.5	47.3	55.3	
Employment	53.3	56.1	55.1	
Supplier deliveries	60.1	61.1	64.9	
Export orders	58.5	56.5	61.5	
Imports	56.5	56.0	57.0	
Prices	70.0	67.0	75.0	

The ISM manufacturing survey is forecast to edge slightly higher to 61.0 in April.

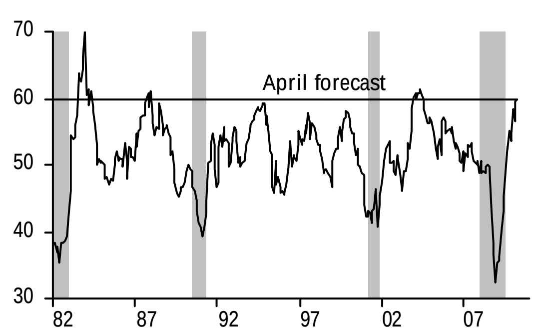
The index rose 3.1pts to 59.6 in March, the highest reading since July 2004, and this turned out to be a reliable indicator of other upbeat March activity readings for the manufacturing sector. Manufacturing IP rose 0.9% in March, and core durable goods orders rose 3.0%.

The Fed's regional manufacturing surveys for April have posted improvements from their March levels and point to another rise in the ISM national measure for this month. A reading of 61.0 would be considered very strong. The ISM has only reached 61 during two periods in the past 25 years, in the fall of 1987 and the spring of 2004.

The risks to the forecast of an increase in the ISM reading would likely come from the inventories component. The 55.3 reading for inventories is the highest reading for this component since 1984, while growth of real manufacturing inventories in March appears to be roughly in line, or weaker than, the average during recoveries over the past 20 years.

ISM manufacturing survey

Sa



Mon
May 3
10:00am

Construction spending

%m/m sa

	Dec	Jan	Feb	Mar
Nominal	-3.4	-1.4	-1.3	-0.7
Private	-3.6	-1.7	-1.2	-0.8
Residential	-4.2	1.0	-2.1	0.0
Nonresidential	-3.0	-3.8	-0.4	-1.5
Public	-3.2	-0.8	-1.7	-1.5

Construction spending has declined in 10 of the past 12 months and is forecast to decline another 0.7% in March.

However, the forecast decline in construction activity in March is more moderate than the decline on average over the past several months. One reason for the relative improvement is the recent increase in housing starts, up 1.6% in March and 9.3% (not annualized) in the first three months of the year.

Both private nonresidential construction and public construction activity are expected to continue to decline in March. But the declines are forecast not to be as great as the average over the past several months. March construction activity may be benefiting, at least slightly, from the improvement in the overall economy. And, to the extent that February activity was depressed some by the blizzards, there may be some bounceback in March. Payroll detail is not a very reliable guide to construction spending. But employment in nonresidential construction and nonresidential specialty trades shifted from a decline of 38,000 in February to an increase of 18,000 in March.

Mon
May 3

Motor vehicle sales

Mn saar

	Jan	Feb	Mar	Apr
Light trucks and autos	10.8	10.3	11.8	11.9
Imports	2.6	2.5	2.8	
Domestics	8.1	7.9	9.0	
Autos	3.8	3.7	4.3	
Light trucks	4.3	4.1	4.7	

Guidance from the automakers suggests that unit auto sales edged up to a pace of 11.9 million units in April.

The forecast, if realized, would leave the current quarter starting with a significant improvement from the average 11.0 million selling pace in 1Q10 and an average 10.8 million selling pace in 4Q09. March sales were also on the high side of the 1Q10 quarterly average, but blizzards in February and problems at Toyota had depressed sales that month and pushed sales into March. Although auto sales have improved, they are still very low relative to the 16.6 million sales pace that prevailed from 2002-2007.

The University Michigan consumer survey includes a question on buying conditions for automobiles. Responses to this question have not been a close correlate of auto sales. But it is still worth noting that responses to this question have improved over the past few months, with substantially fewer respondents saying that buying conditions are unfavorable because of bad times.

Tue
May 4
10:00am

Pending home sales

sa, unless noted

	Dec	Jan	Feb	Mar
Total (mn, ar)	97.8	90.2	97.6	100.5
%ch m/m	0.8	-7.8	8.2	3.0
%oya (nsa)	9.2	8.6	17.3	18.3

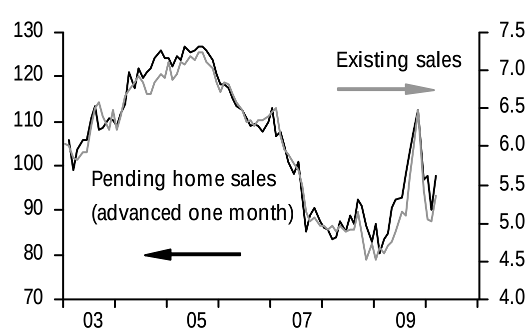
The forecast looks for another 3.0% increase in pending home sales in March.

Pending home sales are based on a sample of home sales contracts and are a reasonably reliable indicator of existing home sale closings over the following few months. The increase in pending home sales in February and forecast rise in March reflect a response to the second homebuyer tax credit. This tax credit likely helped motivate the 6.8% increase in existing home sales in March and is expected to lead to at least some further increase in April.

The expected level of March pending home sales would be 10.6% below the October level, a level that reflected a peak response to the first homebuyer tax credit. This is consistent with the view that the second tax incentive will prove less effective in boosting sales than the first tax credit.

Until 2007, pending home sales moved closely with mortgage purchase applications. But the relationship has broken down since. Consequently, the 8.8% increase in mortgage purchase applications in March should not be considered a useful guide to March pending home sales.

Pending home sales, existing home sales



Tue
May 4
10:00am

Factory goods report

%m/m sa,unless noted

	Dec	Jan	Feb	Mar
New orders	1.5	2.5	0.6	0.2
Shipments	1.8	0.7	-0.1	1.4
Inventories	-0.2	0.3	0.5	0.4
Inventory/sales ratio	1.29	1.29	1.29	1.28

Already-released data show a 1.3% decline in March orders at manufacturers of durable goods, pulled down by a plunge in aircraft orders in what was otherwise a solid report. We expect that rising prices of petroleum and related chemical prices will support a 1.5% increase in shipments at manufacturers of nondurable goods. (For manufacturers of nondurable goods, orders are assumed to equal shipments.) We look for another modest increase in factory inventories, but given the strength expected in shipments, we think the inventory-sales ratio should tick down.

Wed
May 5
8:15am

ADP employment

Change from month ago, sa

	Dec	Jan	Feb	Mar
ADP	-149	-82	-24	
BLS private payroll	-83	16	8	

The ADP survey undershot BLS private payrolls by 146,000 in March. It is not clear whether this undershoot relates to the fact that employees probably did not come off and then back on to the ADP service because of a temporary weather distortion like the one experienced in February, or whether this is just another large miss for this survey.

Wed
May 5
10:00am

ISM nonmanufacturing survey

Sa

	Jan	Feb	Mar	Apr
Nonmfg. index (NMI)	50.5	53.0	55.4	57.0
Business activity	52.2	54.8	60.0	
New orders	54.7	55.0	62.3	
Employment	44.6	48.6	49.8	
Prices	61.2	60.4	62.9	

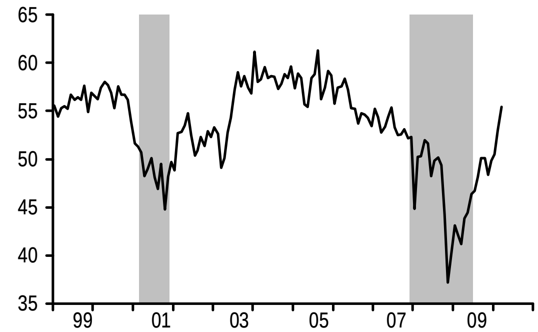
The ISM nonmanufacturing survey has increased in each of the past four months and a further 1.6pt increase to 57.0 is forecast for April.

The recent improvement reflects the substantial broadening of the economic expansion, a trend that is also reflected in the payroll diffusion index. Indeed, the reading on new orders for nonmanufacturing in March (62.3) is higher than for manufacturing (61.5).

There is good reason to think that the nonmanufacturing survey should continue to improve. The trend in housing activity, both starts and home sales, has been increasing lately. Both auto and nonauto retail sales increased in March and are forecast to increase again in April. Finally, the one regional nonmanufacturing survey from the Richmond Fed did show significant improvement in April.

ISM nonmanufacturing index

Sa



Thu
May 6
8:30am

Jobless claims

000s sa

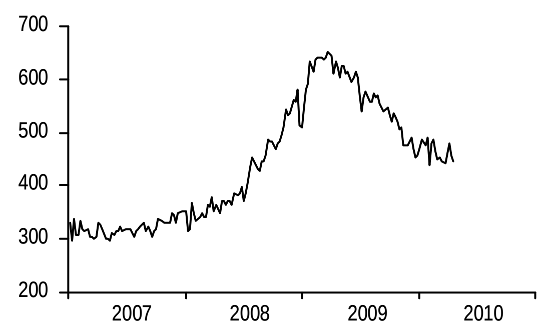
	New claims (wr.) Wkly	New claims (wr.) 4-wk avg	Continuing claims Wkly	Continuing claims 4-wk avg	Insured Jobless,%
Feb 20	486	474	4712	4787	3.6
Feb 27	466	468	4694	4762	3.6
Mar 6	451	471	4694	4724	3.6
Mar 13[1]	454	464	4668	4692	3.6
Mar 20	445	454	4681	4684	3.6
Mar 27	442	448	4562	4651	3.5
Apr 3	463	451	4686	4649	3.7
Apr 10	480	458	4663	4648	3.6
Apr 17[1]	459	461	4645	4639	3.6
Apr 24	448	463			
May 1	440	457			

1. Payroll survey week

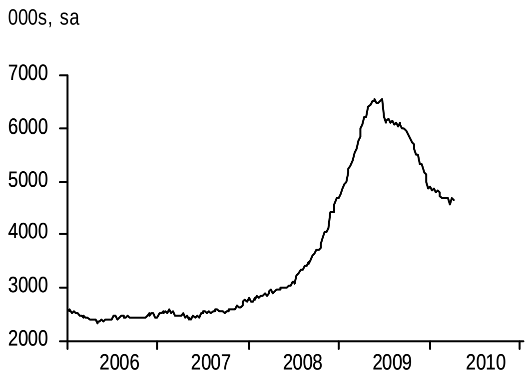
Initial claims fell another 11,000 in the latest survey and have retraced most of their worrying move up from earlier in April. That said, claims have not reached a new low and the pace of improvement in the first four months of this year has slowed compared to the second half of last year. We expect claims for the week ending May 1 to move closer to the low of 439,000 reached in the week ending February 6.

Initial jobless claims

000s, sa



Continuing jobless claims (first 26 weeks of UI)



Thu
May 6
8:30am

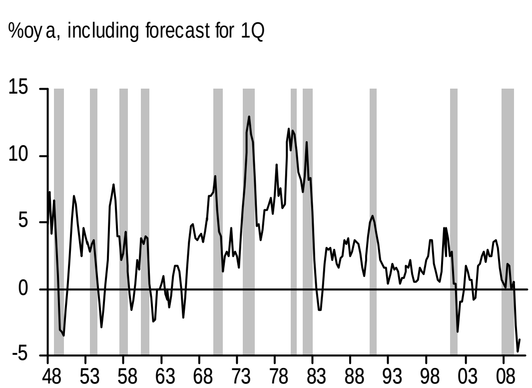
Productivity and costs

Nonfarm business sector, %q/q saar, unless noted

	2Q09	3Q09	4Q09	Prel 1Q10
Productivity	7.6	7.8	6.9	3.1
%oya	2.9	4.6	5.8	6.4
Output	-1.1	2.2	7.6	4.4
%oya	-5.4	-3.9	-0.2	3.2
Hourly compensation	7.7	-0.4	0.6	1.8
%oya	3.4	1.8	0.8	2.4
Unit labor costs	0.1	-7.6	-5.9	-1.4
%oya	0.5	-2.7	-4.7	-3.8
Hours	-8.1	-5.3	0.6	1.2
%oya	-8.1	-8.2	-5.7	-2.9

After a scorching three-quarter run, nonfarm productivity looks set to cool to a slower, but still quite strong, 3.1% rate of growth in 1Q, which would leave the over-year-ago rate at 6.4%, one of the top few performances since records began in 1947. One factor supporting productivity growth last quarter was the extremely weak hours for the self-employed. While hours worked by wage and salary workers increased at a 1.8% rate, our calculation of seasonally adjusted hours worked by the self-employed showed a contraction at a 4.8% annual rate. Compensation growth picked up last quarter, but even so, unit labor costs likely declined for the third consecutive quarter.

Nonfarm business unit labor cost



Fri
May 7
8:30am

Labor market report

Sa

	Jan	Feb	Mar	Apr
Payroll employment				
ch, m/m, 000s	14	-14	162	145
Private payrolls	16	8	123	85
Goods-producing	-30	-47	41	0
Construction	-60	-59	15	-15
Manufacturing	22	6	17	15
Service-providing	44	33	121	145
Private service-providing	46	55	82	85
Wholesale trade	-8	4	9	
Retail trade	49	8	15	
Professional services	23	40	11	
Temporary help	49	37	40	
Education/health	20	27	45	
Leisure and hospitality	12	16	22	
Government	-2	-22	39	60
Average weekly hours	34.0	33.9	34.0	34.1
Index, hrs worked (%m/m)	0.7	-0.3	0.4	0.4
Hourly earnings (%m/m)	0.3	0.2	-0.1	0.1
%oya	2.0	2.0	1.8	1.7
Unemployment rate (%)	9.7	9.7	9.7	9.8

Private payrolls increased 123,000 in March, though some of that probably reflected a rebound from storm-depressed levels in February. We're looking for an 85,000 increase in private payrolls in April and are expecting another relatively strong month for manufacturing payrolls. Seasonally mild weather should limit the damage to construction employment. Within private services, industry reports point to continued gains in temp help employment, and we expect retailers to also lead in employment gains. Outside the private sector, we think ex-Census government will shed another 20,000 positions, while Census will add 80,000 jobs. The Census plan had looked for a little over 100,000 new positions between the end of March and the end of April. We're a little below that as the hiring likely ramped up throughout the month, one person can hold more than one position, and the mail-in rate on Census forms was higher than anticipated, reducing the need for door-to-door enumerators.

We look for the unemployment rate to be unchanged, though there is a risk it could round up to 9.8%. Last month the unemployment rate barely rounded down to 9.7%, and we think many Census workers are likely new entrants or reentrants. Average hourly earnings fell 0.1% last month, though we think the weakness was exaggerated by the swings in the workweek associated with the snowstorms. That said, the trend has been soft, and we only anticipate a 0.1% increase. The average workweek has recovered from the dip in February but not moved higher. We expect the April workweek will increase another 0.1 hour.

Review of past week's data

S&P/Case-Shiller home price index (Apr 27)

%oya, unless noted

	Dec	Jan		Feb	
20-city composite	-3.1	-0.7		~~1.2~~	0.6
%m/m, sa	0.3	0.3		~~0.2~~	-0.1
10-city composite	-2.4	~~0.0~~	-0.1		1.4

The S&P/Case-Shiller 20-city house price index for February declined 0.1% on a seasonally adjusted basis and was up 0.6%oya. The C-S house price index had been running stronger than other house price measures including the FHFA and Loan Performance indices lately, and the decline (following a string of eight consecutive monthly increases on an adjusted basis) brings Case-Shiller more in line with these other measures. Although there are questions about the reliability of seasonal adjustment factors that have been raised by Case-Shiller, the fundamental news here is that prices are running slightly above year-ago levels, marking a shift to stabilization. One theme of the city detail is the fairly large increase in house prices in California over the past several months.

Consumer confidence (Apr 27)

Sa

	Feb	Mar		Apr	
Conference Bd index	46.4	~~52.5~~	52.3	~~53.0~~	57.9
Present situation	21.7	~~26.0~~	25.2		28.6
Jobs plentiful	4.0	~~4.4~~	4.0		4.8
Jobs hard to get	47.3	~~45.8~~	46.3		45.0
Plentiful less hard to get	-43.3	~~-41.4~~	-42.3		-40.2
Expectations	62.9	~~70.2~~	70.4		77.4

The Conference Board's measure of consumer confidence increased from 52.3 in March to 57.9 in April, and this measure is now at the high end of its fairly depressed range over the past year. In April, the assessment of current conditions increased 3.4pts and expectations rebounded another 7.2pts from the recent low in February. The labor market measure (percent jobs plentiful less jobs hard to get) improved 2.1 points to -40.2.

Employment cost index (Apr 30)

	3Q09		4Q09		1Q10	
Total (%q/q sa)	0.4		~~0.5~~	0.4	~~0.4~~	0.6
Wages and salaries	0.4		0.5		~~0.5~~	0.4
Benefits	~~0.4~~	0.3	0.5		~~0.3~~	1.1
Total (%oya nsa)	1.5		1.5		~~1.5~~	1.7
Wages and salaries	1.5		1.5		~~1.7~~	1.5
Benefits	1.6		1.5		~~1.5~~	2.2

The employment cost index rose 0.6% (1.7%oya) in 1Q10. Wages and salaries were up only 0.4% on the quarter, but private sector benefits costs rose 1.4%, well above the recent trend. Labor productivity is expected to slow to about 2.0% in 1Q10 and to about 2.0% for this year as a whole. With productivity running higher than the ECI, unit labor cost should continue to decline—consistent with our forecast of very low core inflation.

Gross domestic product (Apr 30)

%ch, q/q saar, unless noted

	3Q09	4Q09		Adv 1Q10	
Real GDP	2.2	5.6		~~3.0~~	3.2
Final sales	1.5	1.7		1.6	
Domestic final sales	2.3	1.4		~~2.0~~	2.2
Consumption	2.8	1.6		~~3.1~~	3.6
Equip. and software	1.5	19.0		~~9.0~~	13.4
Nonres. structures	-18.4	~~-18.0~~	-18.1	~~-18.0~~	-14.0
Residential investment	18.9	3.7		~~-10.0~~	-10.9
Government	2.7	-1.3		~~0.4~~	-1.8
Net exports (%-pt contr.)	-0.8	0.3		~~-0.4~~	-0.6
Inventories (%-pt contr.)	0.7	3.8		~~1.4~~	1.6
Core PCE price index	1.2	1.8		~~0.5~~	0.6
%oya	1.3	1.5		1.4	
GDP chain price index	0.4	0.5		~~0.5~~	0.9
%oya	0.6	0.7		~~0.3~~	0.4

Real GDP increased at a 3.2% annual rate in the first quarter. Although this was a slowdown from the inventory-led 5.6% rate in 4Q, the 1.6% rate of increase in real final sales was very close to the pace seen in the prior two quarters. The 1.6%-pt contribution to growth from inventories was a little stronger than we assumed, so the mix of growth going forward is a touch weaker. That said, the main message from this report is that private final demand is picking up and the recovery is further establishing its footing.

Within private final demand, consumption growth was perhaps the most impressive, as real consumer spending increased at a 3.6% annual rate, and the level of real spending surpassed its pre-recession highs. Real disposable income was flat on the quarter.

Real outlays for capital equipment and software increased robustly for the second straight quarter, expanding at a 13.4% annual rate. Nonresidential structures declined at a 14.0% rate, a slight moderation in the decline from earlier quarters, and residential investment contracted at a 10.9% rate, as storms depressed activity in this increasingly minuscule part of the economy.

A big 3.8% decline in the state and local government spending pulled down overall government spending at a 1.8% rate. The GDP deflator increased at a 0.9% annual rate, which, by recent standards, is relatively firm.

Consumer sentiment (Apr 30)

	Mar	Pre Apr	Fin Apr	
Univ. of Mich. Index (nsa)	73.6	69.5	~~71.0~~	72.2
Current conditions	82.4	80.7		81.0
Expectations	67.9	62.3		66.5
Inflation expectations				
Short term	2.7	2.9		2.9
Long term	2.7	2.7		2.7
Home buying conditions	156.0	151.0		154.0

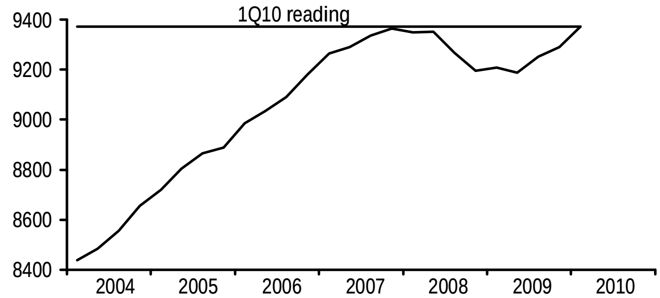
US focus: recovery in consumer spending

- Real consumer spending increased 3.6% at an annual rate in 1Q10, the third consecutive quarterly increase. Real spending has now reached a level slightly above the prior 4Q07 cyclical peak.

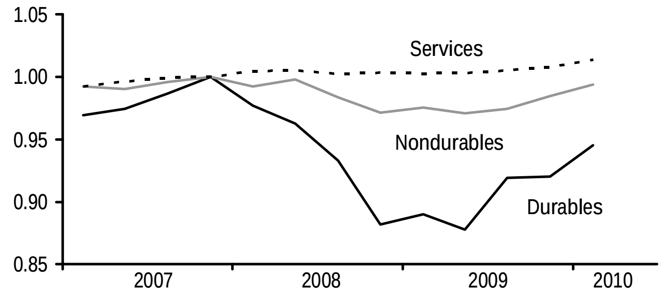
- The full recovery in real consumer spending largely reflects continued gains in traditionally non-cyclical categories, especially spending on housing, utilities, medical care, and groceries. In addition, real spending on what are called durable recreational goods in the NIPA accounts, including video and audio equipment and home computers, has grown rapidly over the past year.

- Many highly cyclical spending components are still depressed relative to their prior peaks. Real spending on motor vehicles and parts is more than 20% below its pre-recession norm. And spending on cyclical services components—including transportation, restaurants and hotels, and recreation—is still well below pre-recession levels.

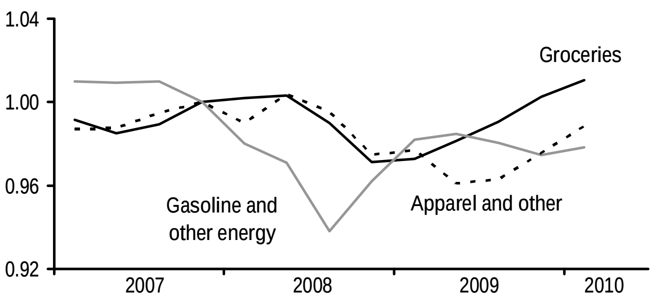
Real consumer spending
$ 2005 bn



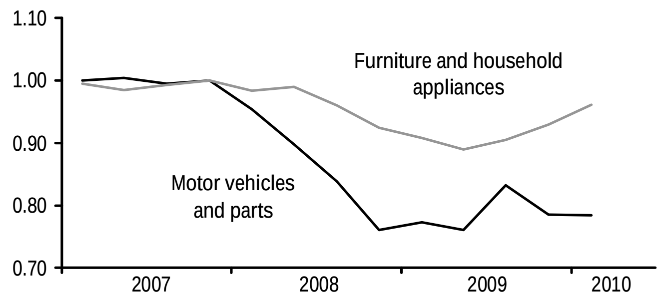
Real consumer spending
Index, prior 4Q07 peak = 1.00



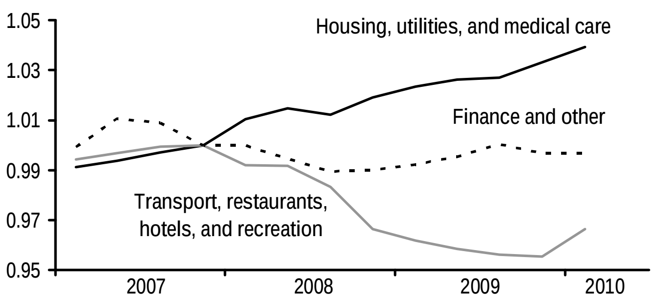
Real nondurables spending
Index, prior 4Q07 peak = 1.00



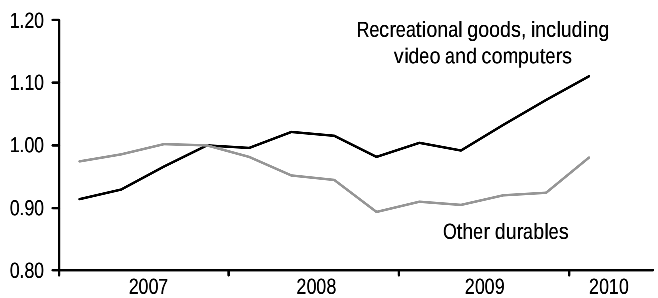
Real durables spending, motor vehicles and household durables
Index, prior 4Q07 peak = 1.00



Real services spending
Index, prior 4Q07 peak =1.00



Real durables spending, recreational goods and others
Index, prior peak 4Q07 = 1.00



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Euro area

- **Fiscal stresses intensify again**
- **Economic data continue to signal faster growth**
- **Spillover to economic data beyond Greece remains small, although contagion risks remain**

This week saw the sovereign stresses in the region intensify even further, with increasing pressure from markets spreading beyond Greece. But, at the same time, the economic data continued to surprise on the upside, suggesting that the region is finally experiencing the strong cyclical lift that we have been expecting since the middle of last year (see the research note, "Cyclical lift arrives in the Euro area—better late than never," in this *GDW*). It remains unclear which of these opposing forces will gain the upper hand, given the huge uncertainty. But, for now, we are sticking with our central view that the cyclical lift will dominate and produce solid growth in the Euro area overall in the coming quarters.

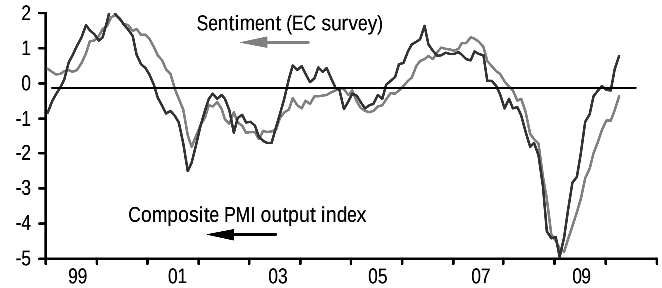
Over the coming few days, we will see the details of the multi-year financial support package for Greece. The aim will be to allow Greece to stay away from the capital markets through end-2012. Policymakers are hoping that the resolution of the uncertainty around this package will both calm markets in Greece and limit contagion pressure. If this does not happen, further financial support might be needed. In addition, the ECB could step up its support by either re-establishing the provision of liquidity over longer horizons or initiating outright purchases. The key problem with the former is how much help it would provide, even if the tenders were extended to beyond 12 months. The key problem with the latter is how the ECB feels about the Lisbon Treaty's prohibition on the direct monetary financing of fiscal deficits. In our view, outright purchases in the secondary market are not precluded by the Treaty, but the ECB may not agree. In addition, it is possible the ECB may need to loosen the collateral regime further. In any event, we do not expect any dramatic announcements at next week's ECB meeting.

Little sign of economic spillover yet

While economic sentiment nudged lower in Greece, from an already very depressed level, there continues to be little evidence of negative spillover effects to the other countries that are also facing fiscal stress in the region. Instead, sentiment in April continued to trend higher in Italy, Spain, and Portugal, suggesting that the cyclical improvement in the data remains relatively broad-based across countries. In addition, there were some positives in the details of the

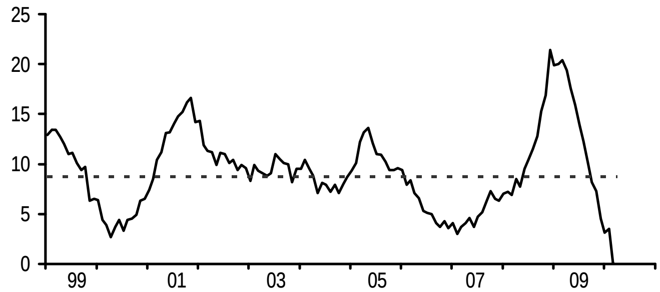
Euro area PMI and economic sentiment

Standard deviations from average over 2000 to 2007 period



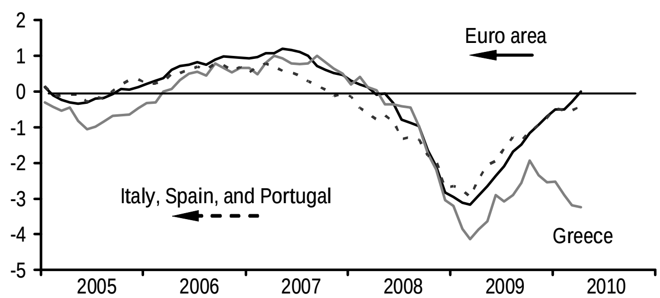
Euro area sentiment survey: level of inventory in manufacturing

% balance, sa, dotted line shows average over 1999 to 2007 period



Euro area economic sentiment

Standard deviations from long-run mean



Greek sentiment survey—consumer confidence fell again, but there were encouraging increases in manufacturing, services, and retail sector confidence. Of course, the events of the past two weeks will not have been captured by the April surveys. But, it is encouraging that sentiment has improved at least until early April in countries that also face the prospect of large fiscal adjustments ahead.

German labor market impresses

Our view is that the Euro area labor market will stabilize earlier than is widely expected. The improvement continues

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to be most striking in Germany, where unemployment fell by over 100,000 over the past two months alone. In addition, the gradual increase in vacancies over the past six months suggests not only that firms are able to retain the labor they hoarded during the recession, but also that there is increasing demand for labor in parts of the economy. This is due not only to increases in public sector employment, but also to increases in part-time work and renewed hiring by temporary help agencies. Even though the latter two generate less household income than full-time employment, they do illustrate the success of past reforms at increasing the flexibility of the German labor market and should therefore be seen as positives.

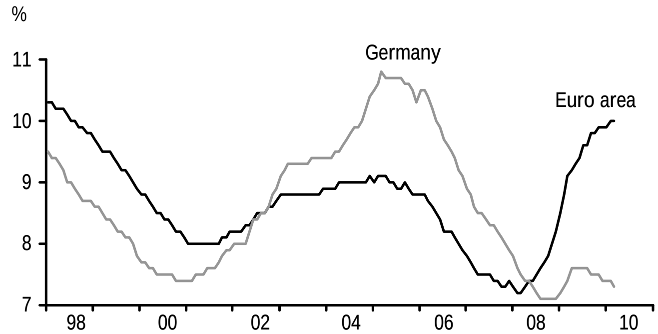
Outside of Germany, this week's labor market reports were more mixed. The Euro area unemployment rate remained unchanged at 10.0% in March, but the number of unemployed rose a bit more than we had expected. The latter reflected stickiness in a number of countries, where unemployment is still rising, albeit at low rates. Nevertheless, it was encouraging that households' unemployment expectations fell in April after recent wobbles, most impressively in Germany. And looking ahead, we still expect the large improvements in the employment indices of key business surveys to translate into a shift to more stable employment levels.

A steady flow of credit

The main positive in this week's bank lending report was the flow of actual bank loans. Loans to households continued to expand at a 3% annualized pace, while corporate loans are contracting more slowly than a few months ago. The strong growth of bank deposits held by firms (7%oya) suggests that cash generation has improved considerably. This reduces their need for bank loans as a source of finance for increases in capital spending. Overall, the actual lending data continue to send a positive message about both the demand and availability of bank lending.

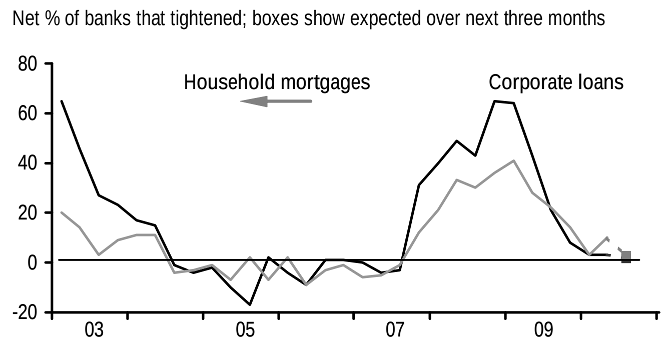
This was also the message of the ECB's April Bank Lending Survey, which showed only a small further tightening of lending criteria. However, the survey also suggested that banks remain relatively cautious, with banks citing ongoing concerns about the economic outlook and the creditworthiness of firms and households, rather than funding and balance sheet pressures, as the main reasons for this caution. Looking ahead, the recent improvements in key business surveys and the labor market data could ease these concerns further. But, equally, there remains the risk that the sovereign stress and drops in prices of government bonds create renewed pressure on bank balance sheets.

Unemployment rate

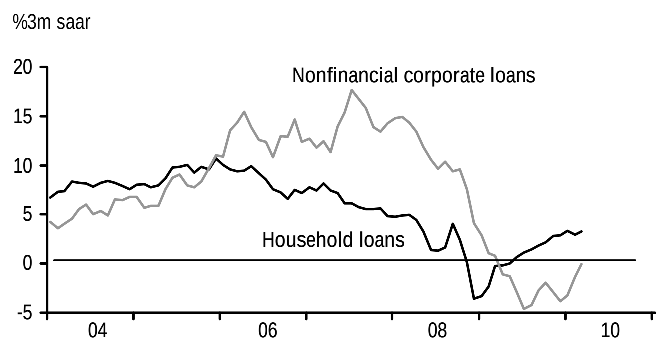


Euro area unemployment expectation and actual unemployment

Euro area bank lending standards



Euro area bank lending



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Data releases and forecasts

Week of May 3 - 7

Output and surveys

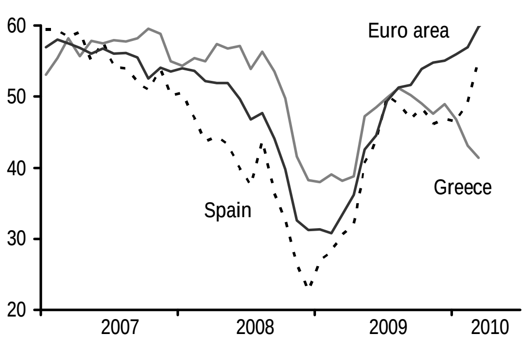
Purchasing managers index final (manufacturing)
Index, sa

		Jan	Feb	Mar	Apr
Mon	Euro area				
May 3	Overall region	52.4	54.2	56.6	57.5
10:00am					
9:55am	Germany	53.7	57.2	60.2	61.3
9:50am	France	55.4	54.9	56.5	56.7
9:45am	Italy	51.7	51.6	53.7	54.5
9:15am	Spain	45.3	49.1	51.8	52.5

The strong increases reported in the April flash release for the Euro area overall, Germany, and France imply that most of the rest of the region must have also increased solidly (by around 1pt on average). This implies that we could see further improvements in countries such as Spain, Italy, and Ireland. In these economies, the level of the manufacturing PMI was still below the Euro area average in March, but very large increases of 9pts in February and March saw the PMI in Spain and Ireland close the gap to the Euro area overall. Recently, only Greece has fallen back into contractionary territory. Given the risk of contagion from the fiscal troubles in Greece, it will be important to see how the country breakdown fares in the final April PMI release.

In terms of the region overall, the final release should confirm that the expansion in industry stepped up again in April, with the output index at over 61, the new orders to inventory ratio still supportive of strong output gains in the coming months, and the employment index signalling that job cutting in industry has almost come to an end.

PMI manufacturing - output index
DI, sa



Purchasing managers index final (services)
Index, sa

		Jan	Feb	Mar	Apr
Wed	Euro area				
May 5	Overall region	52.5	51.8	54.1	55.5
10:00am					
9:55am	Germany	52.2	51.9	54.9	55.0
9:50am	France	56.3	54.6	53.8	57.8
9:45am	Italy	50.9	50.8	55.3	55.5
9:15am	Spain	48.8	47.1	51.3	52.5

The service PMI finally rose above its pre-recession average in the April flash report, pointing to a broadening of the recovery. Outside of Germany and France, the service PMI must have increased by almost 1pt in April, after the huge 4pt gain in March (which was broad-based across Italy, Spain, and Ireland). Note that Greece does not have a service PMI.

Purchasing managers index final (composite)
Index, sa

		Jan	Feb	Mar	Apr
Wed	Euro area				
May 5	Overall region	53.7	53.7	55.9	57.3
10:00am					
9:55am	Germany	54.6	55.7	58.7	59.1
9:50am	France	58.0	55.6	55.8	58.4
9:45am	Italy	52.1	51.9	55.6	56.0
9:15am	Spain	48.2	47.7	52.3	53.5

The flash PMI for April suggested that the region has stepped up to a 3% annualized pace of GDP growth. As discussed above, improvements were spread across the region. We expect the new country details to show further increases of the PMI in Italy, Spain, and Ireland.

Industrial production

		Dec	Jan	Feb	Mar
Fri	Germany				
May 7	Production sector (%m/m sa)	-0.9	0.1	0.0	2.0
12:00pm	%oya sa	-5.0	2.1	5.4	6.8
	Prod sec ex constr (%m/m sa)	-0.8	1.1	-0.1	1.2
	%oya sa	-5.2	2.9	6.5	7.7
	Industry (%m/m sa)	-1.2	0.6	0.1	__
	%oya sa	-5.9	2.7	6.4	__

German industrial production likely rose 2%m/m or so in March after being flat over the prior couple of months. In our view, output ex construction rose 1.2%m/m, a move that seems consistent with the PMI output reading of 64.2 in March and with the rise in orders in earlier months. Meanwhile, we expect construction output to have shot up 15%m/m in March after a massive weather-related drop of 14.2% in January and only a modest gain of 1% in February.

If our forecast is realized, IP will still only be up 1.5% ar or so in 1Q. This is due to the very weak level of construction activity at the start of the quarter (construction output is likely to be down about 35% ar in 1Q as a whole). Excluding construction, IP is likely to be up around 4.5% ar. The rise in manufacturing orders at the start of this year, and the likely rebound in construction activity through the spring, should set German IP up for a strong gain in 2Q.

Manufacturing orders
Index, sa

		Dec	Jan	Feb	Mar
Thu	Germany				
May 6	Volumes, sa				
12:00pm	Total (%m/m)	-2.4	5.1	0.0	2.5
	%oya	7.1	20.5	24.5	22.7
	Domestic (%m/m)	-2.1	6.7	-1.9	__
	%oya	5.4	14.0	18.7	__
	Foreign (%m/m)	-2.5	3.7	1.8	__
	%oya	8.6	27.0	30.1	__

German industrial orders likely rose 2.5%m/m in March after being flat in the previous month. The gain seems consistent with the strong manufacturing PMI new orders reading in March (65.2), which also looks high when juxtaposed with the inventory reading (49.8). If our forecast is realized, German orders will be up around 24% ar in 1Q, showing a clear reacceleration from 4Q (when they rose 3.5% ar) and paving the way for significant gains in IP through the spring.

Demand and labor markets

Retail sales
Total sales, volumes

		Dec	Jan	Feb	Mar
Wed	Euro area				
May 5	%m/m sa	0.8	-0.2	-0.6	0.5
11:00am	%oya, working-day adj.	-0.2	-0.6	-1.1	__
Tue	Germany				
May 4	Sales ex autos and petroleum, volumes				
8:00am	%m/m sa	1.1	-1.3	1.1	0.2
	%oya sa	-1.5	-1.6	-0.3	__

Through the considerable noise, both German and Euro area retail spending have been broadly flat recently, after having fallen sharply from mid-2008 until early 2009. The forecasts we have penciled in for March are still in line with this stable trend. In terms of 1Q10 overall, they would put retail spending flat in Germany and slightly down in the Euro area overall. Given that car registrations in 1Q10 were below the 4Q09 average in both Germany and the Euro area overall, total consumer spending is likely to have declined at the start of the year. But surprisingly, Euro area car registrations have picked up in February and March, pointing to a slightly better trajectory for 2Q10.

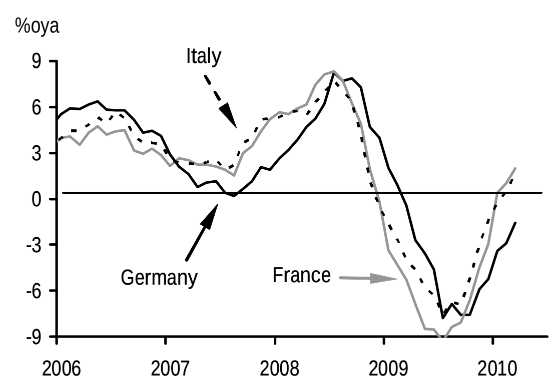
Inflation

Producer prices

		Dec	Jan	Feb	Mar
Tue	Euro area				
May 4	%m/m nsa	0.1	0.7	0.1	0.6
11:00am	%oya nsa	-2.9	-1.1	-0.5	0.8

Producer prices in the Euro area likely moved towards a positive inflation rate in March, thanks to a significant acceleration in intermediate goods producer prices, as well as sequential increases in both food and energy components.

PPI across the Euro area



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Review of past week's data

Output and surveys

European Commission survey

% balance of responses, sa

	4Q09	1Q10		2Q10	
Euro area					
Level of capacity utilization	71.0	~~72.0~~	72.3	~~74.0~~	75.5
	Feb	Mar		Apr	
Euro area					
Industrial confidence	-13	-10		~~-8~~	-7
Recent production trend	-5	0		__	8
Production expectations	7	9		__	9
Export order books	-42	~~-37~~	-36	__	-32
Stocks of finished products	4	0		__	-1
Selling-price expectations	-4	~~-1~~	-2	__	5
Construction confidence	-29	-25		__	-25
Retail confidence	-9	-6		__	-1
Service confidence	1	1		__	5
Consumer confidence (final)	-17	-17		-15	

Economic sentiment rose more than expected in April, driven by large gains across all sectors. This contrasts with the concern that fiscal pressures could spread beyond Greece and weigh on areawide activity, although the very recent events will not have been captured by the April survey.

The sector details were very firm. Industry is seeing rapid growth of output and orders, while firms' assessment of their inventory level fell to another record low. Similarly, current and expected demand were boosted sharply in both services and retail. In the latter, intentions of placing orders continued to rise, while the volume of stock remained low. Employment expectations improved in all sectors, again pointing to increasing stability in labor markets in the region. Finally, despite the rise, capacity utilization in manufacturing is still far below the long-run average of 81.5 and points to weak inflation developments. But, capacity utilization has already regained more of the cumulative decline seen in the recession than has output itself, suggesting that capacity scrapping is also acting to normalize utilization rates in addition to the recovery in output.

The improvement in consumer confidence is a new cycle high and encouraging in light of the risk that fiscal stresses and uncertainties could have weighed more on sentiment. The details showed that there was a huge 10pt improvement in the index for expected unemployment (a large part of which came from a huge 20pt improvement in Germany). Also, the index for expected major purchases, which correlates most closely with actual spending, improved 2pts.

By country, economic sentiment fell marginally to 69.1 in Greece, with little sign of negative spillover effects to Portugal, Spain, or Italy. Also, the Greek details showed another sizable decline in consumer confidence, but encouraging increases in manufacturing, services, and retail.

National business surveys

	Feb	Mar		Apr	
Italy (ISAE survey)					
2000=100, sa					
Producer confidence	84.0	~~84.1~~	84.4	__	85.5

Demand and labor markets

Unemployment

Seasonally adjusted

	Jan		Feb		Mar	
Euro area						
Harmonized measure (Eurostat)						
Unemployment rate (%)	9.9		10.0		10.0	
	Feb		Mar		Apr	
Germany						
Registered (ch m/m, 000s sa)	~~-1~~	-10	~~-31~~	-42	~~-10~~	-68
(000s nsa)	3643		3568		__	3406
Unempl. rate (% sa)	8.1		8.0		~~8.0~~	7.8

Employment

	Jan		Feb		Mar	
Germany						
change m/m, 000s, sa	~~4~~	-18	~~7~~	-1	5	10

The Euro area unemployment rate was unchanged at 10.0%, as expected. But, the monthly change was slightly to the high side of our expectation. Unemployment increased by 101,000 in March, which implies an average monthly increase of 87,000 in 1Q10, after just 47,000 in 4Q09. Outside of Germany (where unemployment fell), the report showed signs of some stickiness in the last few months, with unemployment nudging higher at low but steady rates in a number of countries.

The German labor market data continued to come in firmer than expected in April. Apart from better-than-expected unemployment data, vacancies continued their recent upward trend as well, rising by another 8,000 (all non-subsidized). Finally, the employment gains in April reflect a shift to part-time and public sector employment (incl. in health and education), but recent business surveys suggest that job losses in manufacturing are also ending and that the private service sector could already be creating some jobs. Therefore, the data point to a broad-based improvement in the German labor market.

Looking ahead, it will still be important for the economic recovery to generate enough labor demand for the sharp reduction in hours worked during the recession to be reabsorbed. For now, these cuts in hours appear sustainable and the recent extension of the government's short-time work subsidy scheme should further support this. In any case, new applications for the scheme fell again, suggesting that other sources of labor market flexibility are acting strongly to protect jobs.

Inflation

Consumer prices

	Feb	Mar	Apr	
Euro area (flash)				
HICP (%oya nsa)	0.9	1.4	~~1.6~~	*1.5*
Germany (prelim)				
%m/m nsa	0.4	0.5	~~0.2~~	*-0.1*
%oya	0.6	1.1	~~1.3~~	*1.0*
HICP (%oya)	0.5	1.2	~~1.4~~	*1.0*
Baden Wuerttemberg (%oya)	0.3	1.3	~~1.5~~	*1.1*
Bavaria (%oya)	0.4	1.1	~~1.2~~	*0.9*
Brandenburg (%oya)	0.3	0.8	~~1.0~~	*0.7*
Hesse (%oya)	0.3	0.8	~~1.0~~	*0.8*
North-Rhine West (%oya)	0.6	1.2	~~1.3~~	*0.8*
Saxony (%oya)	0.5	1.3	~~1.4~~	*1.1*
Italy (prelim)				
%m/m nsa	0.1	0.3	~~0.2~~	*0.4*
%oya nsa	1.2	1.4	~~1.4~~	*1.5*
HICP (%oya nsa)	1.1	1.4	~~1.5~~	*1.6*
Spain (flash)				
HICP (%oya nsa)	0.9	1.5	*1.6*	
Belgium CPI				
%m/m nsa	0.4	0.4	~~0.4~~	*0.3*
%oya nsa	0.7	1.7	*1.8*	

The downside surprise in Euro area flash inflation in April was due to the low inflation number printed in Germany. The details from the national inflation measures sent a mixed message: inflation for hotels and restaurant and leisure was down sharply in Germany, only marginally down in Belgium, and up again in Italy. It appears very unlikely that the disruption in air transport due to volcanic ash had any measurable effect on tourism-related inflation. We expect to see a part of the decline to reverse in May. The other components of core inflation appear to have declined very slightly, in line with expectations. Through the noise, core inflation appears to be declining in line with expectations.

Energy inflation increased in line with expectations in Italy and Belgium, although it remained relatively softer in Germany. Food inflation was on the rise everywhere. We expect to see monthly gains in fresh food inflation in April

The downward surprise in the preliminary German inflation report in April was concentrated in two components: package holidays and hotels and restaurants. Prices of package holidays fell in April to -9.2%oya, after +2.4%oya in March. Despite the small weight (2.5% of the basket), the magnitude of the downward surprise in this component was enough to pull the headline inflation rate down by 0.16%-pt in April.

Hotel and restaurant inflation declined as well from 2.1%oya in March to 1.0%oya in April. The sharp movement in prices is not in line with the seasonal dynamic for services connected to tourism. We expect a correction in May, but the recent volatility in the series makes it very difficult to separate noise from signal. Core inflation in the rest of the basket appears not to have moved much in April.

Meanwhile, energy inflation was below the expectations derived from gasoline prices at the pump, while food inflation kept rising in April. In particular, fresh food prices moved up significantly in sequential terms.

Producer prices

	Jan		Feb		Mar	
France						
%m/m nsa	~~0.6~~	*0.7*	~~0.2~~	*0.1*	__	*0.7*
%oya nsa	~~0.3~~	*0.4*	1.0		__	*2.0*
Italy						
(%m/m nsa)	0.6		~~0.2~~	*0.3*	__	*0.5*
(%oya nsa)	-0.3		~~0.4~~	*0.5*	__	*1.7*

Import prices

	Jan	Feb	Mar	
Germany				
%m/m nsa	1.7	1.0	~~0.8~~	*1.7*
%oya nsa	1.4	2.6	~~4.0~~	*5.0*

Import prices in Germany rose acrosss all components in March. Not only was import energy inflation up 5.4%m/m, but also inflation for core goods was up 1.1%m/m in March. The sharp increases were concentrated in durable consumer goods, as well as food.

Financial activity and public finance

Money and credit data

	Jan		Feb		Mar	
Euro area						
M3 (%m/m sa)	~~-0.2~~	*-0.3*	0.0		~~0.0~~	*0.1*
M3 (%oya)	0.1		~~-0.4~~	*-0.3*	~~-0.2~~	*-0.1*
M3 (%oya 3mma)	~~-0.2~~	*-0.1*	-0.2		~~-0.2~~	*-0.1*
Private loans (%oya)	-0.6		-0.4		___	*-0.2*

Euro area money and credit growth remained weak in March. But, as in recent months, the details show further positive trends for the Euro area overall. First, household loans are continuing to grow at a 3% annualized pace, while corporate loans are falling less quickly than a few months ago. This still argues against the existence of severe credit constraints in the region overall, as was also suggested by the ECB Bank Lending Survey. Second, while M3 remains weak (-0.1%oya in March), the sector breakdown shows nonfinancial corporates accumulating liquid bank deposits at an increasing pace. The 7%oya increase in March contrasts with one year earlier when corporates were forced to dip into their liquidity buffers due to revenue and cost pressures. Finally, in aggregate, the banking system is no longer reducing the size of its balance sheet and even appears to be increasing it again.

Japan

- **We revised up our CY2010 GDP growth forecast to 3.2%oya from 2.6%**
- **1Q IP gained faster than in 4Q09, but likely to slow in 2Q; nonmanufacturing sentiment continues to improve**
- **Consumption was solid in March; deflation pressure appears to be easing**
- **BoJ revised up its outlook, but will introduce new initiative to strengthen foundations for growth**

We have revised up our real GDP growth forecast, not only for 1Q (data released on May 20), but also for the whole of 2010. We now expect real GDP to increase 5.0%q/q saar in 1Q, instead of our previous forecast of 3.5%, and for growth to be 0.5%-pt higher than we had previously penciled in for the next five quarters (table). Our motivation for the upward revision for near-term growth reflects the better-than-expected outcomes for key monthly indicators; our modifications for coming quarters are based on our judgment that the economy is establishing a firm foundation for a faster recovery, mainly in consumption, capex, and housing investment.

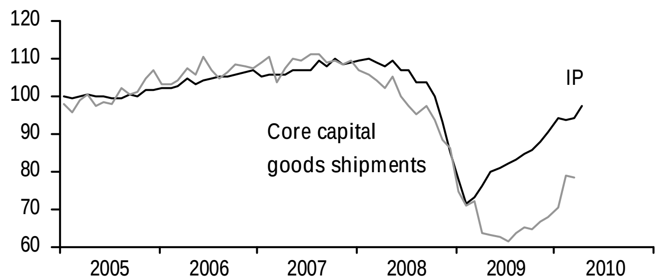
The BoJ also used April's Outlook Report to revise up its FY2010 GDP growth forecast, to 1.8%oya from 1.3%oya. Board members remain more cautious over Japan's growth prospects than we do, however the BoJ's key forecast change in the report was the upward revision of core CPI for FY2011; it now anticipates 0.1%oya inflation, instead of the previous 0.2% deflation. This decision can be attributed to both the smaller output gap and the expected rise in commodity prices—note that Japan's core CPI includes food (excluding fresh food) and energy.

The BoJ revealed its thinking behind the upward revision to the outlook in a statement following the board meeting: "Members shared the view that it was necessary for the Bank to make new efforts to contribute to strengthening the foundations for economic growth." Governor Shirakawa, Chairman of the Board, said he "instructed staff to examine possible ways to support private financial institutions in terms of fund provisioning." In a press conference after the meeting, Governor Shirakawa's tone was a little more ambiguous; however, he hinted that the new initiatives are not meant to add liquidity to financial markets. As we interpret the situation, a simple expansion or extension of the fixed-rate operation (currently with a three-month maturity, capped at a maximum level of ¥20 trillion) is no longer the next likely course of action, as we had expected.

Real GDP forecast
%ch, saar

		1Q10	2Q10	3Q10	4Q10	CY10	CY11	FY10	FY11
J.P. Morgan	New	5.0	2.5	2.5	2.7	3.2	2.2	3.0	2.1
	Old	3.5	2.0	2.0	2.2	2.6	1.9	2.4	2.0
BoJ April Outlook report								1.8	2.0

IP and core capital goods shipments
Index , 2005=100, latest points for IP are manufacturers' projection for Apr and May



The new initiative was not a surprise. We believe the Bank wants to show a cooperative stance to support the government's efforts to foster growth and to escape from deflation, while avoiding taking more radical measures—including an aggressive purchase of JGBs. (For more discussion of BoJ policy, see the research note, "Japan: BoJ to ease more even as economy improves," in this *GDW*.)

Another encouraging IP report and business survey

Industrial production rose 0.3% in March after a 0.6% fall in February, leaving the 1Q average up 29.4% annualized above 4Q last year. While the IP gain on a m/m basis has slowed, the quarterly gain in 1Q was faster than 4Q09 (+25.9%) and exceeded that registered in 2Q last year (+28.9%), which was the highest since 4Q59. Moreover, the softer-than-expected March gain accompanied a significant upward revision in manufacturers' projections for April (rising to 3.7% from 0.6%). The April PMI manufacturing rate was also encouraging, rising to the level seen at the end of last year (53.5) from an average of 52.5 in 1Q.

To be sure, the pace of gain in 2Q IP will likely be slower than previous quarters, as we see the strong rebounding phase drawing to a close. In fact, the inventory index rose in 1Q, the first rise since 4Q08. However, the pace of IP gain is expected to remain around 15% annualized, which is stronger than we had expected (10%). We expect IP to continue to increase at a solid pace. Meanwhile, it should be noted that core capital goods shipments—the best coincident indi-

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cator to track GDP-based capex—edged down 0.5%m/m sa in March, but the jump in February pushed 1Q up 68.7%q/q saar, the largest gain on record since 2Q78.

The Shoko Chukin small firm sentiment index surprised on the upside, rising in April for the fourth consecutive month, on top of a marked jump in the previous month. The current index level stands at 46.8, which is 3.7pts higher than its 1Q average and the highest since November 2007. The result suggests that the momentum in the economy has strengthened at the start of this quarter.

Impressive improvement was seen in the nonmanufacturing DI (45.7 from the 1Q average of 41.9), which is an input to our real GDP growth model along with industrial production. Truck transport and retail trade were the principal drivers of April's improvement. Our model estimates that the real growth rate is 4.5%q/q saar for 1Q and 3.2% for 2Q (assuming that 2Q IP and sentiment estimates are actually reflected in output).

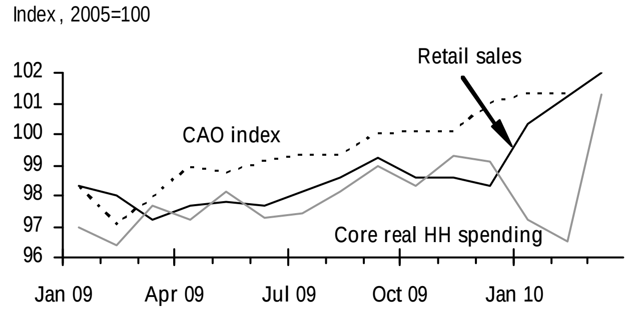
Consumption was strong in March

The wide divergence between two major monthly indicators for private consumption (retail sales versus household spending) in the previous two months was closed by the record 5.0%m/m sa jump in the core household (HH) spending index in March. While average HH spending in 1Q fell 2.3%q/q saar, the March jump decisively supported our view that consumption was solid, particularly at the end of the last quarter. We accept that both readings are not necessarily good indicators for tracking GDP-based consumption, and will have to wait for the cabinet office's composite index of private consumption data (probably due on May 10) for more accurate information. However, in our view it is quite likely that private consumption accelerated in March.

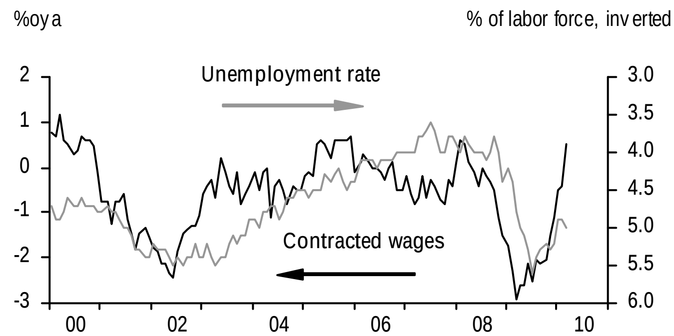
Another positive for consumption was the first oya gain (+0.5%oya) in monthly contracted wages in March since July 2008. The increase in overtime payments (11.7%oya after February's 8.1%) was noteworthy, but the sharp moderation of decline in the core scheduled payments to -0.2% from -1.0% was the main contributor to the improvement. With the rise in employment demonstrated in the labor force survey, the wage data confirm that the oya fall of labor income (compensation of employees) ended in March.

Looking ahead, we think the rate of increase in labor income will be modest given firms' perception of excess labor and cautious outlook. Indeed, the unemployment rate edged up in March to 5.0% from 4.9% in February. However, the ratio of job offers to applicants—a more stable monthly indicator for the labor market—continued to rise, suggesting that employment conditions are improving, albeit gradually. While some moderation in consumption is likely in April as payback for the strong rise in March and unusually cold weather in the month, we expect it to maintain its robust upward trend, thanks to the improving labor market and rise in disposable incomes.

Consumption-related data



Wages and unemployment rate



Deflation pressure easing

The focus for the CPI print this week was the April Tokyo preliminary report, where the pace of the oya decline in the core core CPI accelerated by just 0.2%-pt to -1.4%oya. The acceleration was smaller than the impact from the elimination of high school tuition fees (-0.4%-pt), which started this month. This outcome supported our view that the underlying trend of CPI deflation is now easing gradually.

By our estimate, the elimination of high school tuition should subtract 0.5%-pt from the oya change in the nationwide core CPI through FY2010, which is exactly the same as the BoJ's estimate. The Bank's board forecasts core CPI deflation at 0.5%oya for FY2010, excluding the tuition fee effects, which is also close to our call of -0.6%, and less than that last year (-1.6%).

Data releases and forecasts

Week of May 3 - 7

Thu
May 6
8:15am

Services/composite PMIs

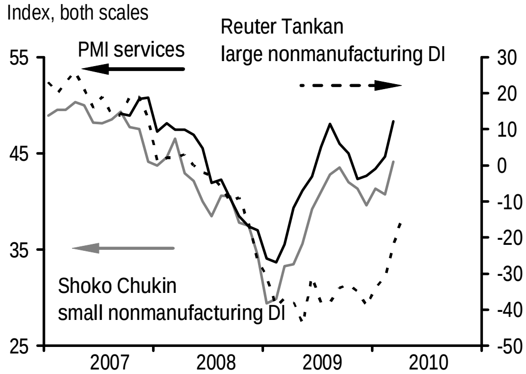
DI

	Jan	Feb	Mar	Apr
Services (business activity)	43.4	44.6	48.3	___
Composite (output)	46.8	47.4	50.3	___

The report will reiterate the message sent by the nonmanufacturing DIs in the surveys that the large-manufacturing-led recovery is now spreading to the nonmanufacturing sector.

Nonmanufacturing DIs in monthly survey reports

Index, both scales



Thu
May 6
2:00pm

Auto registrations

%oya, unless noted

	Jan	Feb	Mar	Apr
Total	36.8	35.1	37.2	35.0
mn units saar	3.51	3.30	3.21	3.46
J.P. Morgan-adjusted (incl. light vehicles)				
mn units saar	4.27	4.08	3.95	___

It appears that the momentum in auto consumption, triggered by government measures to promote sales of environmentally friendly cars and which had been driving overall consumption, began to moderate at the turn of the year. Note, though, that some of the recent softness may reflect consumers waiting for cuts in the auto weight tax (which is paid at registration or via compulsory inspections) that took effect on April 1.

Review of past week's data

Corporate service prices (Apr 26)

%oya

	Jan	Feb	Mar
Overall	-1.2	~~-1.3~~ *-1.2*	~~-1.5~~ *-1.1*
Ex international transport	-1.7	~~-1.7~~ *-1.6*	___ *-1.3*

After excluding international transportation, some components of which are affected by global demand and yen FX rates, the CSPI for March posted the smallest oya decline since June last year.

Looking at the details, price declines have been broad-based across components; however, prices of miscellaneous services rose oya for the first time in eight months, albeit a slight 0.1%, reflecting oya rises in chartered accounting services and civil engineering/architectural services and the reduced decline in lodging. Meanwhile, rental and leasing (-4.7%oya after -1.9% in February) and advertising (- 2.8%oya after -2.6%) show intensified weakness in March.

Given the correlation between the core CSPI (the CSPI ex. international transportation) and the CPI services, we expect the oya decline in the latter to moderate in coming months.

Shoko Chukin small firm survey (Apr 27)

Diffusion index

	Feb	Mar	Apr
Sentiment index	42.3	45.8	~~44.0~~ *46.8*
Manufacturers	44.2	47.9	___ *48.1*
Nonmanufacturers	40.7	44.1	___ *45.7*
Sales (%oya)	1.4	~~0.3~~ *3.4*	___ *5.1*
Profit margins	-16.3	-10.3	___ *-10.1*
Financing conditions	-8.5	-5.1	___ *-2.4*
Inventory	-15.7	-13.2	___ *-11.5*
Capacity	-24.0	-20.8	___ *-19.4*
Employment	-13.2	-10.5	___ *-11.5*
Input prices	1.9	3.5	___ *9.3*
Output prices	-11.4	-9.8	___ *-6.9*

The headline index rose in April for the fourth consecutive month, even after the jump in March. It now stands at a level 3.7pts higher than its 1Q average and the highest level since November 2007. The result suggests that the momentum in the economy has strengthened at the start of this quarter.

In April, the manufacturing DI rose only slightly by 0.2pt. However, there is reason to think that this underestimates the latest state of that sector. In the last recovery phase, 2002-07, the manufacturing and the nonmanufacturing DIs fell in each April, with only one exception for each. Indeed, after our seasonal adjustment, the manufacturing DI rose a substantial 1.7pts last month, on top of the 0.1pt rise in the previous month (the pace of improvement in small manufacturers' sentiment accelerated in April, rather than in March, in our seasonally adjusted series). By sector, sentiment among machinery producers, especially auto makers, softened, but it appears that this was payback for outsize improvement in the previous months.

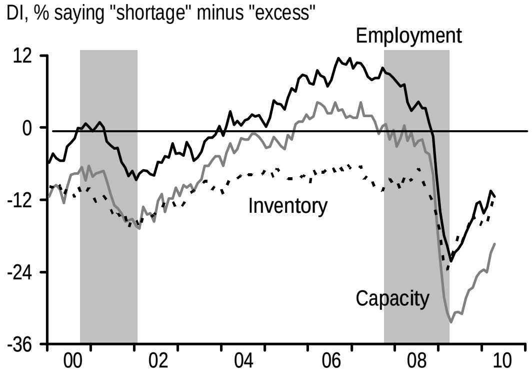
Meanwhile, the nonmanufacturing DI, which is an input in our real GDP growth model along with actual industrial production, posted a stronger 1.6pt rise, with the major contributors being truck transport and retail trade. Outside of the sentiment DIs, each of the inventory, capacity, and employment DIs for small firms suggests that firms' perceptions of excess inventories/capacity/employment have been fading.

Looking ahead to May, the level of the nonmanufacturing DI is predicted to remain virtually unchanged at a two-year high (the nonmanufacturing outlook DI marked 45.6). The optimism of restaurants/hotels was boosted for the month by the Golden Week Holidays, but truck transport firms expected some payback from the April strength, while sentiment among retail trading firms was generally stable.

Although small manufacturers are generally expecting a deterioration in business conditions (the manufacturing outlook DI marked 45.4), the expected levels of their May sentiment index are still firm, in comparison with past readings in this cycle. Note, also, that those prospects may prove to be too cautious in the May report, as was the case in April (in the March report, small manufacturing firms predicted their sentiment DI to decline to 44.7 in April).

Details of Shoko Chukin small firm survey

DI, % saying "shortage" minus "excess"



Commercial sales (Apr 28)

%oya, unless noted

	Jan	Feb	Mar
Commercial sales	-3.8	-0.9	___ *2.0*
Wholesale sales	-6.1	-2.7	___ *1.1*
Total retail sales	2.3	4.2	~~3.2~~ *4.7*
%m/m sa	2.0	0.9	~~1.0~~ *0.8*

Retail sales, in value terms, remained strong in March, posting the third consecutive m/m rise. Indeed, for all of 1Q, sales rose 11.3%q/q saar, the largest q/q gain since the current series started in 2000. Even though this series is not a good indicator for tracking private consumption in GDP, the result supports our view that consumer spending has maintained the solid momentum prevailing since spring last year (the average growth of real GDP consumption in the last three quarters of 2009 was 3.3% at an annual rate), at least through the end of the last quarter.

By category, sales at household appliance retailers increased at a much faster 6.9%m/m sa than the 3.4% in February and 3.6% in January, though the acceleration probably included demand boosted by the extension of the "eco-point" system from April 1 (the extended "eco-point" system excludes several items that had been included in the original program). Sales at apparel retailers also showed a further solid gain (up 0.9% for the fifth consecutive m/m rise), probably reflecting in part a continued boost from favorable weather.

For April, some payback in household appliances is likely, and it is possible that the unusually cold weather weighed on sales of seasonal clothing. However, we believe the underlying trend of consumption continues to pick up, amid gradually improving labor income (the product of average wages and the number employed).

Industrial production—preliminary (Apr 30)

%m/m sa

	Jan	Feb	Mar
Production	4.3	-0.6	~~1.0~~ *0.3*
Shipments	4.5	-0.2	___ *1.6*
Inventories	1.1	1.6	___ *-1.6*
Inventory/shipment ratio	-1.8	0.3	___ *-5.2*

The March rebound in industrial production was weaker than our own and market consensus expectations. However, 1Q finished up 29.4%q/q saar, the fastest pace of growth since 4Q59 (during this recovery phase, it grew at +25.9% in 4Q09, +22.8% in 3Q09, and +28.9% in 2Q09).

Looking ahead, manufacturers' output predictions included in this report were relatively strong. April's forecasts were revised up significantly, to +3.7%m/m sa from +0.6% in the previous report, though the first print of May's estimates looks for a marginal payback of -0.3%. This suggests that the expected slowdown in industrial output in 2Q may be more modest than we had anticipated.

Also in the report, core capital goods shipments, a key monthly capex indicator, ended last quarter with the record q/q rise, while inventories in the industrial sector increased q/q for the first time in five quarters.

Purchasing Managers Survey (manufacturing) (Apr 30)

DI

	Feb	Mar	Apr
Overall index	52.5	52.4	~~52.5~~ *53.5*

The headline index in the manufacturing PMI report gained a little more than 1pt in April, after stabilizing in 1Q at levels a little lower than the 4Q average. This points to a further solid rise in manufacturing output in April, which agrees with the survey predictions included in the March IP report.

Also worth noting is that new orders for the month recovered most of the loss in the previous three months, with new export orders jumping to the highest level since October 2001. Furthermore, the employment index rose above the neutral 50 level for the first time since July 2008.

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Consumer prices (Apr 30)

%oya

	Feb	Mar	Apr
Tokyo			
Overall	-1.8	~~-1.8~~ *-1.7*	~~-2.1~~ *-1.5*
Core (ex fresh food)	-1.8	-1.8	~~-2.2~~ *-1.9*
Ex food and energy	-1.3	-1.2	~~-1.1~~ *-1.4*
Nationwide			
Overall	-1.1	~~-1.2~~ *-1.1*	
Core (ex fresh food)	-1.2	-1.2	
Ex food and energy	-1.1	~~-1.0~~ *-1.1*	

The oya decline in the nationwide core CPI for March was the same as in February and a bit slower than in January and December last year (-1.3%). After excluding all food and energy prices, the latter of which explain most of the 1.2%-pt pickup from the fastest pace of decline in August last year, the CPI has shown similar declines (it fell 1.2%oya in January and December).

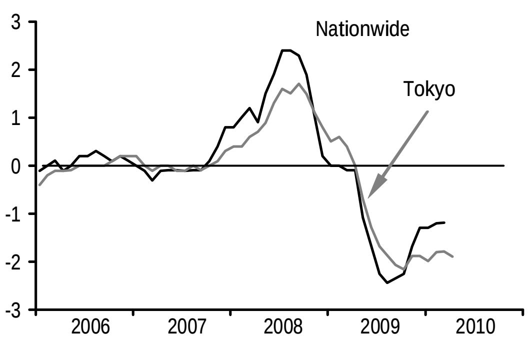
More focus should be paid to the preliminary April Tokyo report, which showed the pace of the oya decline in the core CPI accelerating a modest 0.1%-pt, compared to a month earlier. This actually reflected a pickup in prices other than high school tuition. The elimination of tuition, which started this month as a part of the government fiscal package, subtracted 0.37%-pt from the oya change in core prices.

The elimination of high school tuition will have an even larger impact on the nationwide measure, because of a higher weighting. On our estimate, that component will subtract 0.5%-pt from the oya change in the nationwide core CPI, and thus the deflation on a nationwide basis will likely intensify, at least temporarily, in April.

That said, the reports suggest that the underlying trend of CPI deflation is now easing at a very gradual pace. This is also consistent with a widely held view that the output gap (which is estimated to have been the largest in 1Q09) affects the core core CPI with a four-quarter lag.

Core CPI

%oya, 2005-based



Labor force survey (Apr 30)

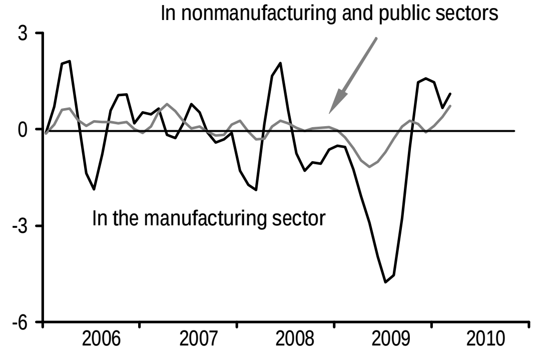
	Jan	Feb	Mar
Unemployment rate (% sa)	4.9	4.9	~~4.9~~ *5.0*
Labor force (%m/m sa)	0.7	-0.4	___ *0.1*
Total employment (%m/m sa)	0.9	-0.4	___ *-0.1*
Unemployed (%m/m sa)	-4.7	-2.1	___ *3.1*
Job offers ratio (sa)	0.46	0.47	~~0.48~~ *0.49*

The unemployment rate rose 0.1%-pt in March, but from a rate that was 0.7%-pt lower than the cycle peak last July. The details in the March report were better than the headline figure, with the number employed at firms recovering almost all of the previous month's loss (although it was offset by a fall in the number of self-employed and an increase in labor-force participation), and the job offers ratio rising for the third consecutive month.

The result is still consistent with gradually improving labor-market conditions, which has been reflected in labor-market DIs in the survey reports. Rising new job offers (the 5.6%m/m sa jump in March marked a seventh consecutive rise) suggest the labor-market recovery will continue in coming months.

Employment by sector

%3m/3m, sa by J.P. Morgan



Household survey of expenditures (Apr 30)

%m/m sa, incl. agricultural worker households

	Jan	Feb	Mar
All households			
Real spending	-1.3	-1.6	~~2.0~~ *5.9*
%oya	1.7	-0.5	~~1.4~~ *4.4*
Core	-1.9	-0.7	___ *5.0*
%oya	0.4	0.1	___ *3.2*
Worker households			
Real disposable income	3.4	-0.1	___ *-1.1*
Propensity to spend ratio (%)	73.5	72.2	___ *78.1*

Core real household spending, which excludes several volatile components and is the measure the government uses as an input to GDP consumption, exhibited an unprecedented jump in March. This helped to narrow a significant gap between the performance of the two major monthly consumption indicators (this measure and nominal retail sales in the commercial sales report) that had emerged over the first two months of 1Q.

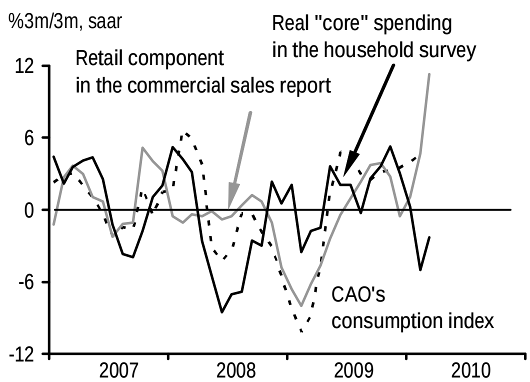
Indeed, the CAO's private consumption index, which combines demand- and supply-side statistics, has been tracking solid consumption growth in 1Q, consistent with likely gradual improvement in aggregate labor income and the recovery in consumer sentiment. We have been placing more confidence in the strength of the retail sales data.

Employers' survey (Apr 30)

%oya

	Jan	Feb	Mar
Total earnings per employee	-0.2	-0.7	___ *0.8*
Contracted wages	-0.5	-0.4	~~-0.2~~ *0.5*
Scheduled payments	-0.8	-1.0	___ *-0.2*
Overtime payments	2.4	8.1	___ *11.7*
Special payments	8.4	-26.1	___ *11.2*
Total hours worked/employee	0.4	0.6	___ *3.2*
Regular employment	-0.2	0.2	___ *0.2*
Full-time workers	-0.8	-0.9	___ *0.1*
Part-time workers	1.4	3.0	___ *0.4*

Monthly consumption indicators



With the rapid rise in overtime payments, which is consistent with recovering industrial production, average contracted wages rose in over-year-ago terms for the first time since July 2008. Meanwhile, regular employment, in this survey measure, rose oya for the second consecutive month, reiterating the message from the labor force survey that employment is now recovering gradually.

The report was encouraging and suggested that a gradual improvement in labor income (the product of average wages and the number employed) is supporting, and will likely continue to support, consumer spending.

Housing starts (Apr 30)

%oya, unless noted

	Jan	Feb	Mar
Housing units %oya	-8.1	-9.3	~~-5.0~~ *-2.4*
%m/m sa	5.4	-7.9	~~4.8~~ *7.5*
Mn units saar	0.86	0.79	~~0.83~~ *0.85*

Housing starts rebounded more strongly than expected in March, after having been unexpectedly weak in February (when they registered their first monthly drop since August last year). As a result, unit starts gained 25.2%q/q saar in all of 1Q, even after the robust 51.6%q/q rise in 4Q. The result eased concerns over the sustainability of the recovery in housing construction activity.

For residential investment in the national accounts, recorded in put-in-place terms, our forecast for a 20.0%q/q saar rise after four consecutive double-digit annualized declines is supported by the six-month moving average of starts measured in floor space.

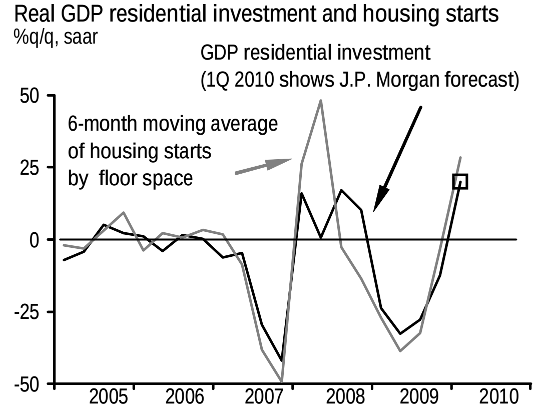
Looking ahead, we expect housing investment growth to continue in 2Q, though slower pace, against a backdrop of improving household sentiment.

Construction orders (Apr 30)

%oya

	Jan	Feb	Mar
Total	15.7	-20.3	___ *42.3*
Domestic, private sector	9.5	-20.2	___ *75.3*
Domestic, public sector	13.7	-12.8	___ *-14.3*

Real GDP residential investment and housing starts



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Canada

- **GDP posts sixth consecutive monthly increase in February**
- **We raised our 1Q GDP forecast to 5.8%q/q saar from 4.5%**
- **BoC Governor Carney attempts to increase Bank's maneuverability, but June 1 rate hike still likely**

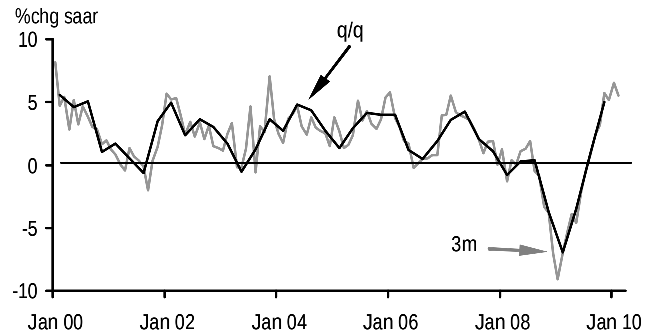
February GDP and comments before parliament by Bank of Canada Governor Carney were the highlights of a rather light week. GDP increased 0.3%m/m, its sixth consecutive monthly increase, pulling the oya rate up to 1.8%. The increases in January and February point to a faster pace of growth in 1Q than we had envisaged. So, we are upping our forecast to 5.8%q/q ar from 4.5%. The BoC, in its April Monetary Policy Report published on April 22, coincidently raised its 1Q GDP expectation to 5.8%q/q ar.

Carney, in two separate appearances before parliament, appeared to carve out a little more wiggle room for the Bank's next interest rate decision. At the April 20 rate announcement, the Bank had removed its conditional rate commitment (which was set to expire at the end of June), leading the market (and us) to expect rate normalization to begin with a 25bp increase in the overnight rate on June 1.

Carney expanded on the language in the rate announcement, saying that the removal of the commitment "represents a tightening of policy" but that "nothing is pre-ordained." The market initially removed a bit of the tightening it had priced in, but the 3-month OIS rate moved to new highs after Friday's monthly GDP report. To be sure, the Bank has not yet decided whether to hike in June, and there are key data reports ahead that could influence that decision. So, the BoC likely wanted to keep its June options wide open. Nonetheless, the Bank would not have removed its rate commitment just two months before its expiry unless it thought that it would need to hike rates before the commitment had expired. We still look for a 25bp increase in June and another 100bp over the rest of 2010.

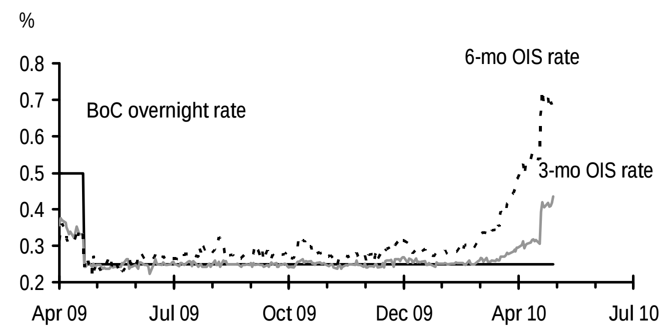
In the details of the February GDP report, goods-producing industries increased 0.7%, largely on the strength of manufacturing (+1.2%) which accounted for nearly half of the monthly increase in overall GDP. Mining, excluding oil and gas extraction, jumped 7.6% in February. Construction slowed in February, rising just 0.1% after a 2.0% jump in January. Still, it is on track to make another significant contribution to overall GDP in 1Q.

Monthly and quarterly real GDP

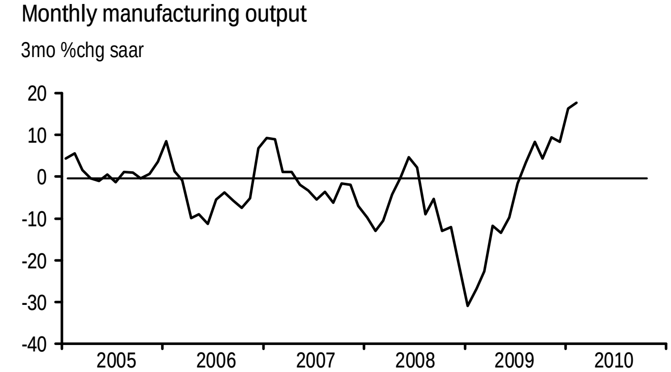


Monthly real GDP

BoC overnight rate and OIS rates



Monthly manufacturing output



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Services output edged up only 0.1%, mostly reflecting a 1.4% drop in wholesale trade. Retail trade posted another solid increase, rising 0.6% on top of a 1.1% jump in January. The rises in January and February put retail sales up 6.4% ar from the 4Q average, pointing to another solid contribution by consumption to overall GDP in 1Q. Services also were boosted by the Winter Olympics in Vancouver. Output of arts, entertainment, and recreation surged 6.1%m/m (not annualized), its largest monthly increase since 1998. However, this category accounts for only 1.3% of total service production and 1% of total GDP. So this category added a modest 0.06%-pt to overall GDP growth in February.

Monthly GDP is constructed from the output side, while economists mostly look at GDP from the expenditure side. Monthly data to date offer some hints as to how expenditure in 1Q is progressing. Consumer demand is still a key component of the rebound—though it is moderating. Real retail sales in January/February are up 2.5% ar from the 4Q average, slower than the 3.7%q/q ar increase in 4Q, but still likely to make a solid contribution to overall 1Q growth. Housing continues to be an important contributor though it too is slowing. Housing starts rose 11%q/q (not annualized) in 1Q after a 15%q/q jump in 4Q. Net exports are on track to contribute in 1Q for the second consecutive quarter. The monthly average real trade deficit narrowed by C$300 million in January/February from the 4Q average, about the same amount of narrowing that occurred in 4Q. So, it would seem that net exports are on track to add around 1.5%-pt in 1Q as they did in 4Q. Capex has posted a marginal gain in the first two months of 1Q (real imports of machinery and equipment in January/February are up 2.0% ar from their 4Q average, but this stands in sharp contrast to the 6.0%q/q ar decline posted in 4Q). Monthly data on inventories are comparatively scarce, but what we have points to around unchanged so far in 1Q compared with a C$4.3 billion decline in 4Q.

Data releases and forecasts

Thu
May 6
8:30am

Building permits
Sa

	Dec	Jan	Feb	Mar
Total,%m/m	-2.7	-4.7	-0.5	1.9
%oya	30.9	32.9	56.7	26.4

Building permits are expected to rebound in March after four straight months of decline. Total residential permits should rise in March after an outsize decline in multi-family permits caused a dip in residential permits in February. Single unit permits have been trending up since last spring.

Thu
May 6
10:00am

Ivey PMI

	Jan	Feb	Mar	Apr
Sentiment index[1] (sa)	54.2	49.2	53.7	53.6
Purchasing index (nsa)	50.8	51.9	57.8	52.8
Prices index (nsa)	67.8	55.9	61.5	

1. Calculated and seasonally adjusted by J.P. Morgan.

Fri
May 7
7:00am

Labor force survey
Sa

	Jan	Feb	Mar	Apr
Employment (mn)	16.92	16.95	16.96	16.98
ch, m/m, 000s	43.0	20.9	17.9	20.0
%m/m	0.3	0.1	0.1	0.1
%oya	-0.1	0.5	0.9	0.8
Labor force (mn)	18.46	18.46	18.48	18.50
%m/m	0.1	0.0	0.1	0.1
%oya	0.9	0.8	0.9	0.8
Unemployment rate (%)	8.3	8.2	8.2	8.1
Avg hrly earnings (%oya)	2.2	2.5	2.5	2.3
Hours worked (%m/m)	0.2	0.2	-0.4	0.2

The uptrend in employment is expected to continue into April. Increases have been steady since January; the average monthly increase in employment in 1Q was 27,300. The unemployment rate is expected to decrease to 8.1%.

Review of past week's data

Monthly GDP (Apr 30)
Sa

	Dec		Jan		Feb	
Total, %m/m	~~0.5~~	*0.4*	0.6		~~0.2~~	*0.3*
%oya	0.0		1.3		~~1.7~~	*1.8*

Industrial PPI (Apr 30)
%m/m nsa, unless noted

	Jan		Feb		Mar	
Total	0.4		~~0.0~~	*0.1*	~~-0.5~~	*-0.4*
%oya	-0.2		~~-0.6~~	*-0.5*	~~-1.4~~	*-1.3*
Ex energy	~~-0.1~~	*0.0*	~~-0.2~~	*0.3*	~~-0.7~~	*-0.6*
%oya	-2.7		~~-2.9~~	*-2.8*	~~-3.9~~	*-3.8*

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Mexico

- **Banxico reinforced its dovish stance**
- **The central bank revised up its 2010 GDP forecast but left inflation projections unchanged**
- **The FEC did not modify the dollar put options mechanism**

Last Wednesday Banxico published its Quarterly Inflation Report (QIR). In it, the Mexican monetary authority left its projected inflation ranges unchanged (table), and revised its GDP forecast range for 2010 upward to 4%-5%, from 3.2%-4.2%, as we had anticipated. Moreover, at the press conference that followed, Governor Carstens said that the pickup in inflation is temporary, as it has been boosted mainly by "one-off" price increases, while medium- and long-term inflation expectations remain well-anchored. Furthermore, he said that the central bank has not observed any contamination from higher taxes and administered price increases to inflation, implying that the Bank does not see any demand-side inflationary pressures.

Governor Carstens mentioned that the economic recovery has been driven mainly by external demand, and that domestic demand, particularly private consumption and GFI, needs to strengthen further as it is still below 2008 levels (charts). He added that, even though the output gap has been closing, the economy will remain below potential in upcoming quarters. Banxico's board noted that its current projected inflation ranges are subject to the following risks: (1) upside risk if there is an abrupt peso depreciation due to quick outflows from episodes of higher risk aversion; (2) downside risk if Mexico's economic recovery is less vigorous; and (3) on both sides, reflecting the highly volatile prices of fresh fruits and vegetables.

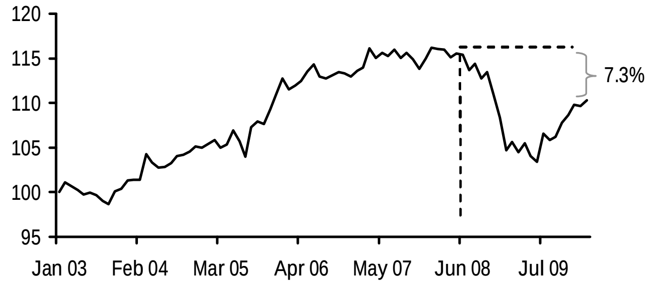
In sum, our perception is that Banxico does not see any second-round effects in inflation, domestic demand remains weak, wage negotiations have been moderate, and medium- and long-term inflation expectations remain well-anchored. As a result, even though we continue calling for two 25bp rate hikes, one in October and one in November—along the same lines as the market consensus—we believe that the probability of the Bank leaving monetary policy on hold for the remainder of this year has increased.

The FEC auctioned US$ 600 mn worth of USD Put/MXN Call options

On April 30, the Foreign Exchange Committee (FEC)—formed by members of the central bank and the Ministry of Finance—sold US$ 600 million of USD put/MXN call options to Mexican financial institutions. This mechanism is exactly the same as the one used back in the 1996-2001 period to accumulate reserves. The owners of the options have the right to sell US dollars to the central bank (in exchange for pesos) at the previous day's "fixing" rate, whenever this rate is below or at the 20-day moving average.

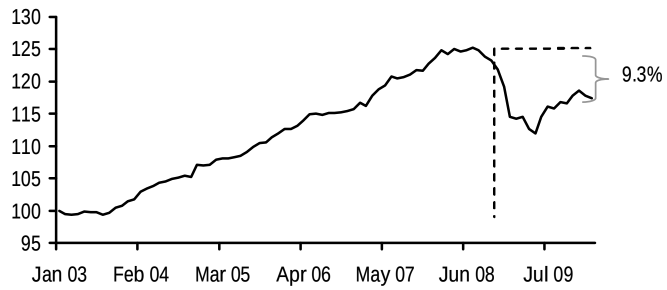
We had anticipated that the FEC could decide either to implement another intra-month US$ 600 million USD put/MXN call auction if 80% or more of the amount auctioned is exercised before the first half of the month or to auction a larger amount. In our view, the FEC's balance of pay-

Industrial production[1]
Index (2003=100), sa



Source: INEGI 1. From INEGI's monthly GDP proxy *IGAE*

Services sector activity[1]
Index (2003=100), sa



Source: INEGI 1. From INEGI's monthly GDP proxy *IGAE*

Banxico's current inflation projection intervals[1]
%oya

	Banxico	J.P. Morgan forecast[1]
1Q10	4.25 - 4.75	4.75
2Q10	4.50 - 5.00	4.39
3Q10	4.75 - 5.25	4.55
4Q10	4.75 - 5.25	5.08
1Q11	4.50 - 5.00	4.67
2Q11	3.50 - 4.00	4.04
3Q11	3.25 - 3.75	4.20
4Q11	2.75 - 3.25	4.20

Source: Banco de México
1. 12-month inflation quarterly average.

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ments estimates might include the large amounts of portfolio capital that has flowed into Mexico's financial markets over the past few weeks, as well as the inflows that could transpire if Mexico's local bonds are included in Citigroup's World Government Bond Index (WGBI). However, the FEC left the options mechanism unchanged. In this context, we acknowledge that the recent episode of high volatility—mainly due to the Euro area sovereign crisis—might have tilted the FEC's decision in favor of leaving the mechanism unchanged. We think the FEC will extend this mechanism in the near term as otherwise, in our view, they would be losing a good opportunity to "capture" portfolio inflows that could be used in the event of an abrupt reversal.

Data releases and forecasts

Week of May 3 - 7

Mon May 3 9:00am

Banxico expectations survey
%oya, average value

	Jan	Feb	Mar	Apr
Inflation				
End-2010	4.93	5.21	5.28	___
Four years forward	3.67	3.69	3.69	___
Real GDP				
2010	3.3	3.9	4.1	___
2011	3.5	3.7	3.6	___
USD/MXN				
2010	12.97	13.04	12.70	___
2011	13.31	13.24	12.93	___

Mon May 3 12:00pm

***IMEF* PMI survey**[1]
Index

	Jan	Feb	Mar	Apr
Manufacturing	52.2	52.2	55.2	54.5
Nonmanufacturing	52.0	53.7	55.1	55.0

1. Using the same methodology as the US ISM survey.

Tue May 4 2:30pm

Consumer confidence, INEGI-Banxico
Jan 2003 = 100

	Jan	Feb	Mar	Apr
Composite	82.1	80.6	81.8	82.1

Tue May 4 9:00am

Central bank foreign reserves
US$ bn

	Apr 9	Apr 16	Apr 23	Apr 30
Gross international reserves	96.2	97.4	97.3	___

Tue May 4 2:30pm

Banamex CPI inflation expectations survey
%oya, except policy rate: %p.a., median value

	Mar 22	Apr 7	Apr 17	May 4
End-2010	5.22	5.25	5.22	___
Core	4.62	4.60	4.60	___
End-2011	3.84	3.81	3.83	___
One year forward	3.98	3.89	3.86	___
Banxico policy rate (YE10)	5.00	5.00	5.00	___

Fri May 7 9:00am

Consumer prices

	Mar 1H	Mar 2H	Apr 1H	Apr 2H
%2w/2w	0.46	0.16	-0.31	0.05
Core	0.18	0.19	-0.03	0.15
%oya	5.06	4.88	4.41	4.37
Core	4.45	4.35	4.13	4.16

	Jan	Feb	Mar	Apr
All items (%m/m nsa)	1.09	0.58	0.71	-0.20
%oya	4.46	4.83	4.97	4.39
Core (%m/m nsa)	0.66	0.40	0.36	0.14
%oya	4.70	4.60	4.40	4.15

Review of past week's data

Central bank foreign reserves (Apr 27)
US$ bn

	Apr 9	Apr 16	Apr 23	
Gross international reserves	96.2	97.4	___	*97.3*

Indicator of overall economic activity *(IGAE)* (Apr 27)

	Dec	Jan		Feb	
%oya	0.5	2.4		~~3.9~~	*3.4*
%m/m sa	0.1	~~-0.8~~	*-1.0*	~~0.8~~	*0.5*

Family remittances (Apr 28)

	Jan	Feb	Mar	
Total (US$ bn)	1.3	1.6	~~1.7~~	*1.9*
%oya	-15.8	-14.1	~~-19.2~~	*-7.3*

Commercial bank credit supply (Apr 30)
%oya, real terms

	Jan	Feb	Mar	
Credit to private sector	-6.0	-6.3	___	*-5.1*
Consumption	-20.3	-18.5	___	*-18.1*
Housing	10.7	10.3	___	*9.1*
Corporate	-4.2	-5.7	___	*-3.6*

Public sector indicators (Apr 30)
Mex$ bn

	Jan	Feb	Mar
Overall balance	6.4	16.5	___
Ytd	6.4	22.9	___
Primary balance	25.4	24.2	___

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Brazil

- **COPOM starts with 75bp, trying to catch up with the March decision to remain on hold**
- **Unemployment rate is well below Brazil's NAIRU**
- **Credit to households is booming**

With several activity and inflation indicators clearly showing that a monetary tightening was overdue, the COPOM this week finally kicked off a rate-hiking cycle, lifting the policy rate 75bp (to 9.50%). This move was broadly priced in by the market, even though a large share of analysts (including ourselves) still looked for a 50bp hike due to recent official communications that suggested a more moderate start. Although it is the first rate hike of the cycle, the statement highlighted that the decision is part of an ongoing adjustment process of monetary conditions, which had started with the normalization of 70% of the reserve requirements eased during the crisis. The mention of an adjustment in "monetary conditions" instead of a rate hike is not usual in COPOM statements, and we will have to wait for next week's minutes to pinpoint whether this reference is a signal that the monetary policy tightening ahead will continue to use both instruments, or was used just to highlight that the tightening had already started, which is the most likely interpretation, in our view.

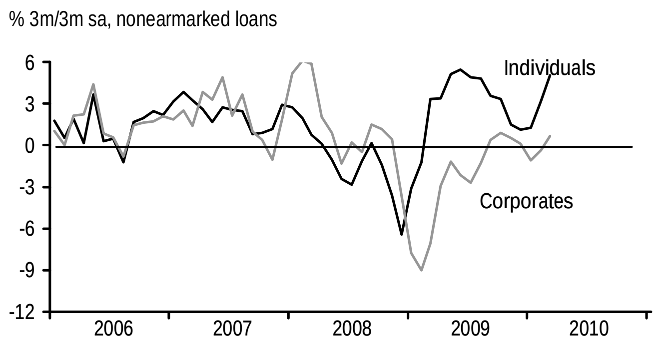
We now expect 375bp for the total cycle

Including this week's increase, we now expect a total of 375bp of monetary tightening to be implemented by year-end. Note we were already expecting two hikes of 75bp in June and July and three hikes of 50bp between September and December—so we are essentially just incorporating the larger-than-expected rate hike this week. We see growing evidence that the Brazilian economy is close to overheating (see below), and therefore the bias is for even stronger monetary tightening (that may well be complemented by higher reserve requirements). But the key risk to be monitored still is the continued fiscal and (mainly) quasi-fiscal stimulus that may eventually increase the burden of monetary policy (see "Brazil: fiscal policy challenging interest rate convergence," *GDW*, October 23, 2009). Indeed, more recently, despite the expected end of tax incentives for vehicle sales, the government has extended tax incentives to the construction sector, allowed the Sovereign Wealth Fund to help capitalize Banco do Brazil, confirmed an additional R$80 billion capitalization of BNDES, and is likely to allow the Congress to increase pensions more than budgeted, clearly not helping to tame the above-potential expansion of domestic demand.

Unemployment rate reached a new low in March

Surging job growth and labor income in 1Q10

New loans to corporates and individuals



Booming demand supported by labor income and credit

The aggressive expansion of domestic absorption is the main pillar of our above-consensus 2010 GDP growth projection of 7.0%, and this week's economic releases were highly supportive of our optimistic view on household demand expansion. The March reports for the labor market and bank credit showed that both labor income and new loans will continue to support booming final demand.

- **Tight labor market underpins inflation concern.** The March labor report showed the unemployment rate at 7.6% nsa with the seasonally adjusted figure decreasing to 6.9%, from 7.1% in February, to reach a new historical low. Note that the current unemployment rate is well below the NAIRU (non-accelerating inflation rate of unemployment) range estimated by the BCB of 7.5%-8.5% before the 2008 crisis. Total employment growth in 1Q10 reached 1.8%q/q sa, which is the highest pace of expansion for a single quarter over the last few years. This upsurge in employment is supporting the lift in total real labor income (2.2% in 1Q10q/q sa). With investment poised to expand firmly in coming months, quasi-fiscal expansion still in place, and credit expansion still showing strong momentum, employment should continue to perform well. This, along with unemployment already below NAIRU (and mounting evidence of labor shortages in some sectors) and higher past inflation (an important variable in wage settings), should prompt further wage gains in the 2H10 wage negotiations—suggesting that despite the ongoing monetary tightening, inflation concerns will remain in place for some time.

- **Household credit is booming.** The March bank credit report reinforces the message sent by the labor report that the expansion of household demand is very well underpinned. The pace of new loan growth to individuals is accelerating, rates are declining, maturities are increasing, and delinquency rates are collapsing. The details of the report show that the origination of new loans for households expanded 1.7%m/m sa from 2.8% in February, delinquency rates for individuals are much lower than a year ago (7.0% versus 8.4% a year ago), and credit standards are the best ever for households to get a loan.

Data releases and forecasts

Week of May 3 - 7

Mon May 3 9:00am — Merchandise trade balance

US$ bn

	Jan	Feb	Mar	Apr
Trade balance	-0.2	0.4	0.7	1.2
Year to date	-0.2	0.2	0.9	2.0
Last 12 months	25.7	24.3	23.3	20.7

Tue May 4 7:00am — Industrial production

	Dec	Jan	Feb	Mar
%m/m sa	0.1	1.3	1.6	2.6
%oya nsa	19.0	16.0	18.4	19.7

Thu May 6 8:30am — Vehicles production (Anfavea)

	Jan	Feb	Mar	Apr
Output (000 units)	246.3	249.8	330.1	na
%oya nsa	33.2	22.1	20.3	na

Thu May 6 6:00am — General prices (IGP-DI)

%m/m nsa

	Jan	Feb	Mar	Apr
Overall	1.0	1.1	0.6	0.7
%oya	-0.5	0.8	2.3	3.0
Wholesale prices	1.0	1.4	0.5	0.7
Consumer prices	1.3	0.7	0.9	0.7
Construction prices	0.7	0.4	0.8	1.0

Fri May 7 7:00 am — Consumer prices (IPCA)

%m/m nsa, % weights in parentheses

	Jan	Feb	Mar	Apr
Total (100)	0.8	0.8	0.5	0.60
%oya	4.6	4.8	5.2	5.29
%ytd	0.8	1.5	2.0	2.67
Ex volatile	0.6	0.7	0.4	0.44
Trimmed mean	0.5	0.4	0.5	0.48
By major component				
Food (20.5)	1.1	1.0	1.6	1.53
Transport (20.7)	1.5	0.8	-0.5	-0.24
Housing (13.6)	0.3	0.3	0.3	0.08

Review of past week's data

National unemployment

% of labor force, new methodology

	Jan	Feb	Mar
Open rate, nsa (30 days)	7.2	7.4	*7.6*

General prices (IGP-M)

%m/m nsa

	Feb	Mar	Apr
Overall	1.2	0.9	~~0.7~~ *0.8*
%oya	0.2	1.9	~~2.8~~ *2.9*
Wholesale prices	1.4	1.0	~~0.5~~ *0.7*
Consumer prices	0.9	0.8	~~0.8~~ *0.7*
Construction costs	0.4	0.5	~~1.0~~ *1.1*

Public sector borrowing requirement

Minus denotes surplus

	Jan	Feb	Mar
R$ bn			
Primary	16.1	0.9	~~2.7~~ *-0.2*
Primary, ytd	16.1	17.0	~~19.8~~ *16.8*
12-month sum, as % of GDP			
Primary	-2.3	-2.2	~~-2.0~~ *-1.9*
Interest payments	5.3	5.4	*5.3*
Nominal	3.0	3.2	~~3.3~~ *3.4*
Net debt, % of GDP	41.2	42.1	~~42.6~~ *42.4*

Chile

- **Consumer and business moods diverge after quake**
- **Consumers' worry deviates from misery index**
- **BCCh ready to pull the trigger on rate hikes soon**

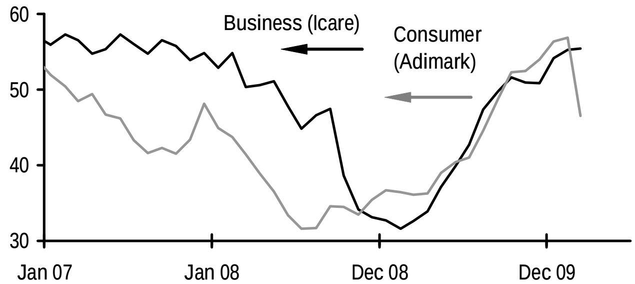
Following the February earthquake, measured confidence in Chile has diverged: business sentiment (ICARE) rose in March by 0.4pt to 57.0 and consumer sentiment (Adimark) fell by 10.4pts to 46.5 (first chart). This week's data flow highlighted the significant contrasts in fundamentals affecting these sectors.

Paradoxically, the fundamentals that normally drive sentiment among households appear to have deteriorated the least (second chart). The February-March reading on the unemployment rate (based on a new survey) was 9.0%—down 0.1%-pt versus the prior three-month period—and March CPI inflation (subject to measurement distortions) had printed well below expectations. All in all, confidence has dropped more than the misery index (constructed with unemployment and inflation data) would anticipate. While consumers may be more downbeat due to the personal and physical damage suffered, macro fundamentals also explain the weakening in sentiment: The new unemployment survey now provides monthly estimates of joblessness in addition to the standard three-month moving average measure. And on a monthly basis, unemployment was adversely affected by the earthquake—it rose 0.4%-pt m/m in March.

Meanwhile, sharper-than-anticipated output disruptions have not affected sentiment among business managers (third chart). Interestingly, this was the case in the manufacturing sector and not just within the construction and the mining sectors. The latter two benefit from reconstruction plans and higher commodity prices, respectively. In contrast, industrial sector sentiment for March (57.9) reached a new record high for the series even as it was reported that March industrial production sank 17.4%oya in the aftermath of the earthquake. In fact, the gap between industrial sector confidence and output is the largest on record (see chart) and suggests that IP should rebound to a +8.0% pace once operations normalize. The new government's sympathy for preserving a competitive exchange rate should continue to support confidence in the industrial sector, although some slippage in the index should be expected next month given increased policy discussion of potential tax increases to corporates. Looking ahead, with domestic and external demand rising rapidly, we maintain our 5.5% real GDP forecast for 2010—that implies a sharp rebound in 2H10.

Chile - business and consumer confidence

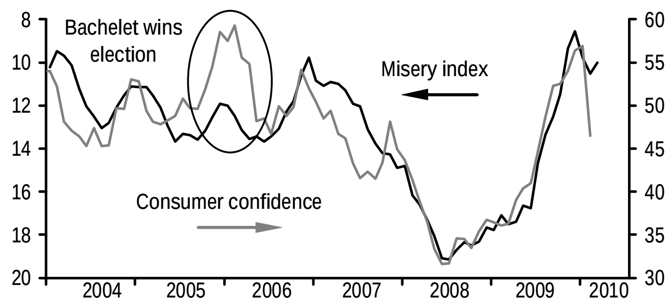
index, min=0; max=100



Chile - consumer confidence (Adimark) and misery index (JPMorgan)

Sum of adj U-rate and core CPI, inverted scale

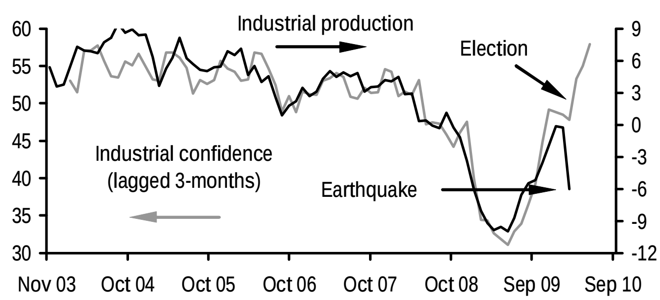
Index, min=0, max=100



Chile - industrial confidence (Icare) and industrial production (INE)

Index, min=0; max=100

%oya, 3-mma



In this environment, the central bank (BCCh) is preparing the market for the initiation of its normalization process for the policy rate (currently 0.5%). The J.P. Morgan forecast calls for a first rate hike in June and for the rate to reach 2.25% by December and 5.00% by June 2011. The April monetary policy minutes raise some risk that the first hike could be carried out in May. In favor of an earlier move is the argument that the economy was already growing above potential prior to the earthquake (and the fact that BCCh's hawkish view has already been sufficiently telegraphed). In contrast, the earthquake distortions to the data (and the concerns that risk of delay are smaller than risk of hiking too early) favor waiting until June for more reliable statistics.

Argentina:

Data releases and forecasts

Week of May 3 - 7

Fri Apr 30 — Construction activity

	Dec	Jan	Feb	Mar
%oya	2.6	2.2	5.2	___

Week of May 3 - 7 — Government tax revenue

	Jan	Feb	Mar	Apr
ARS bn	29.03	27.40	28.51	___

Review of past week's data

Trade balance

	Jan	Feb	Mar
US$ bn	1.22	0.60	___ *0.31*

Industrial production

	Jan	Feb	Mar
%oya nsa	5.2	11.0	___ *10.6*

Chile:

Data releases and forecasts

Week of May 3 - 7

Fri Apr 30 — Unemployment rate

	Dec	Jan	Feb	Mar
% of labor force	8.6	8.7	8.5	___

Wed May 5 — Economic activity

	Dec	Jan	Feb	Mar
%oya	3.69	4.22	2.67	___

Fri May 7 — Inflation

	Jan	Feb	Mar	Apr
Consumer prices (%m/m)	0.50	0.30	0.10	___
%oya	-1.30	0.30	0.30	___

Fri May 7 — Trade balance

	Jan	Feb	Mar	Apr
US$ bn	2.07	1.33	1.36	___

Review of past week's data

Industrial production

	Jan	Feb	Mar
%oya nsa	-1.10	0.50	___ *-17.4*

Colombia:

Data releases and forecasts

Week of May 3 - 7

Tue May 4 — Consumer prices

	Jan	Feb	Mar	Apr
Consumer prices (%m/m)	0.69	0.83	0.25	0.30
%oya	2.10	2.09	1.84	___
Wholesale prices (%m/m)	1.22	0.86	0.58	___
%oya	0.48	-0.44	-0.17	___

Review of past week's data

BanRep monetary policy meeting

	Feb	Mar	Apr
Repo rate %p.a.	3.5	3.5	3.5

Ecuador:

Data releases and forecasts

Week of May 3 - 7

Thu May 6 — Inflation

	Jan	Feb	Mar	Apr
Consumer prices (%m/m)	0.83	0.34	0.16	___
%oya	4.44	4.31	3.35	___

Review of past week's data

No data released.

Peru:

Data releases and forecasts

Week of May 3 - 7

Sat May 1 — Inflation

	Jan	Feb	Mar	Apr
Consumer prices (%m/m)	0.30	0.32	0.28	0.11
%oya	0.44	0.84	0.76	0.85
Wholesale prices (%m/m)	0.82	0.07	0.26	___
%oya	-2.81	-1.22	-0.47	___

Thu May 6 — BCRP monetary policy meeting

%p.a.

	Feb	Mar	Apr	May
Reference rate	1.25	1.25	1.25	1.25

Review of past week's data

No data released.

Venezuela:

Data releases and forecasts

Week of May 3 - 7

No data releases expected.

Review of past week's data

No data released.

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United Kingdom

- **Polls point to hung parliament at next week's election**
- **Bank credit remains weak, but house prices and retail spending continue to rise**
- **A closer look at measures of UK public debt**

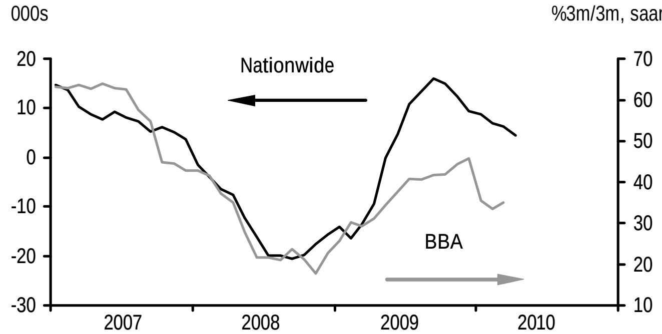
With only a week to go until the general election, media reports are keenly focused on which party is gaining the most political ground. There is more uncertainty over this election than any in recent memory. The polls point to a hung parliament, with no party winning an overall majority. It appears that the Conservative party may take the largest number of seats, and begin negotiating with the Liberal Democrats. In a research note in this week's *GDW*, we explore whether an agreement can be formed between these two parties.

Wrapping up this week's data

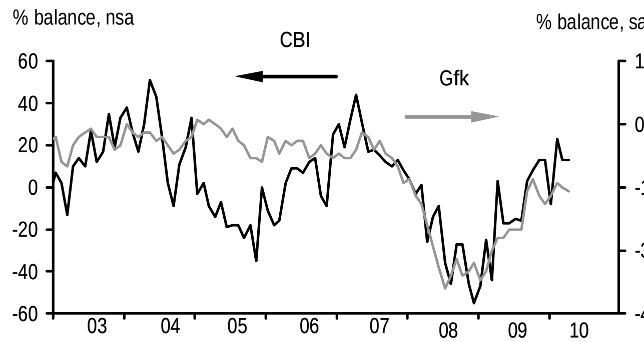
Elsewhere, in a quiet week for data, the British Bankers Association (BBA) survey showed that bank credit flows remain weak. Nonetheless, house prices are still rising faster than expected, and there were further signs from the CBI that household spending growth accelerated into this quarter:

- **The BBA reported a more modest gain in mortgage approvals than expected in March.** Approvals remain very low at 34,900, relative to both the 60,000 long-run average of the BBA and the 40,000-45,000 average of 4Q last year. The main reason for the dip this year is the expiry of the stamp duty holiday in January. We continue to look for a pickup in approvals from April onward. The March Budget announced a new two-year stamp duty holiday for first-time buyers on properties of up to £250,000, effective from March 25. And the BoE lenders survey in 1Q indicated that banks expected to ease mortgage credit availability in 2Q, and were expecting a rise in demand. Despite tight credit, the Nationwide reported a 1%m/m gain in house prices in April. The trend remains toward smaller gains in prices, but the slowdown is occurring less quickly than we thought.
- **The corporate part of the BBA survey showed bank net lending to nonfinancial firms falling £3 billion in March.** Lending has been falling at an average pace of £1.7 billion over the previous six months. Given the usual range of fluctuation around this average, the March data suggest there has been no shift in the trend. But it remains the case that banks are scaling back loans to firms. Part of this weakness in lending may reflect weak demand, especially from the larger firms able to tap capital markets.

BBA mortgage approvals versus Nationwide house prices



CBI retail sales volume versus Gfk consumer confidence



The BoE's 1Q lending survey showed that lenders anticipated both an easing in credit availability in 2Q and a pickup in demand. This may point to slower declines in the flow of net lending to firms in the coming months.

- **The CBI survey flags an acceleration in spending growth in 2Q, to a near average pace.** The volume of sales reading in the CBI retail survey in April remained at +13. Relative to the +9 average last quarter, the survey indicates that we should expect some lift in spending growth in 2Q—after disruption caused by the snowstorms at the start of the year. The expectations reading of the April survey was reported even higher at +17—not far short of its average. This points toward a healthy pace of growth in retail spending in 2Q. Though measures of credit conditions have been slow to improve, the dominant driver of the shift away from retrenchment in household spending over the past six months appears to be the sharp rise in consumer confidence—which is up significantly from the lows of early last year. Despite a second consecutive drop in Gfk NOP consumer confidence in April, the survey remains in line with its recent average. We look for household spending growth to continue to firm later in the year. This assumes that the recent declines in confidence do not persist into 3Q.

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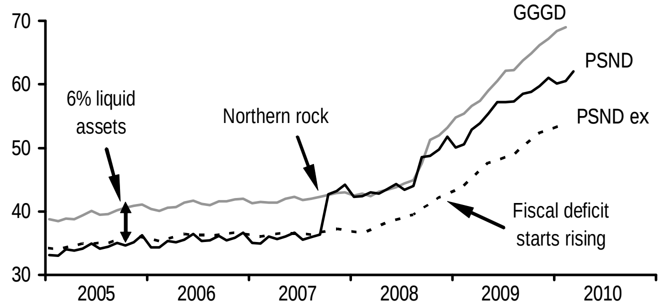
Understanding measures of public debt

In the current environment of heightened sovereign stress, scrutiny of fiscal data has increased. In the UK, the fiscal deficit is in double digits (as a percent of GDP) and government debt is rising. To complicate matters, there are a number of different definitions of borrowing and debt, which can create confusion. Here we try to offer some clarification on these measures. As the largest differences occur between measures of debt, as opposed to borrowing, we focus on the former here.

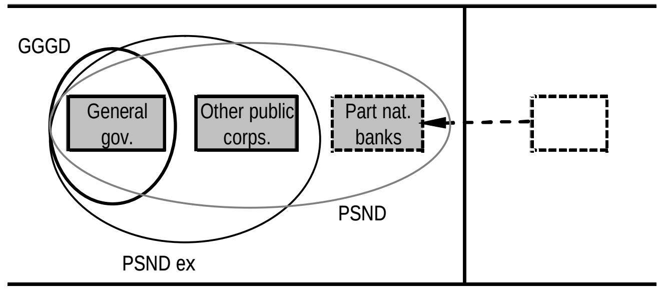
- **Public Sector Net Debt (PSND).** This is the most commonly cited measure of debt in the UK. It takes the consolidated liabilities of the entire public sector, and nets out only liquid assets. These assets include official reserves, deposits, and other short-term instruments. They accounted for less than 6% of GDP prior to the crisis, and are now at 7%-10%. In late 2007, the government nationalized the UK banks Northern Rock and Bradford and Bingley. The balance sheets of these banks were pulled within the broad boundary of the public sector (see diagram). However, as most of the assets of these banks were not liquid, this had the effect of pushing PSND significantly higher (by 6%-7% of GDP). Then, in late 2008, the government helped recapitalize the UK banks RBS, HBOS, and Lloyds and became a significant shareholder in these institutions. As a result, the ONS reclassified them as part of the public sector. At some point over the summer, the ONS will incorporate this reclassification into its debt statistics. As with Northern Rock, the huge debt of these banks, relative to their liquid assets, will push PSND significantly higher. The ONS estimates that this change could leave PSND running at 170% of GDP.
- **Public Sector Net Debt excluding financial interventions (PSND ex).** This measure takes the PSND metric and makes assumptions designed to remove the temporary effect of financial interventions by the government. This is done by assuming that fully or partly nationalized banks will end up back in the private sector. Although these banks now fall within the public sector in the eyes of the ONS, they fall outside of the boundary used to calculate the PSND ex measure of debt (see diagram). Northern Rock and Bradford and Bingley are two examples and explain most of the gap between PSND and PSND ex that is shown at present. When the ONS includes the other part-nationalized banks in PSND in the summer, this gap will grow much larger, from around 7% of GDP shown now, to possibly over 110%. The PSND ex will be unaffected by this specific change. However, it does not exclude all effects from the government's financial interventions. For example, when the government recapitalized the banks, it effectively borrowed and then passed capital "outside" of the PSND ex boundary, thereby pushing up the measure of PSND ex debt. Conversely, the bank recapitalization process had no impact on the PSND measure—under this boundary the flow of capital amounted to a sectoral redistribution.
- **General Government Gross Debt (GGGD).** This is a European Union standard that is used in accordance with the Excessive Deficit Procedure of the Maastricht treaty. Similar to the PSND ex measure, the nationalized banks fall outside of the GGGD boundary. But there are two differences between these measures. First, GGGD is

Public sector debt

% of GDP



ONS assumptions regarding financial interventions



Measures of UK public debt

£ bn or % of GDP, as stated

	Latest	Estimate after ONS changes
Net debt:		
£ bn	890	2390
% of GDP	62.0	169.1
Net debt, excluding financial sector interventions:		
£ bn	772	unch.
% of GDP	53.8	unch.
General government gross debt:		
£ bn	978	unch.
% of GDP	68.4	unch.

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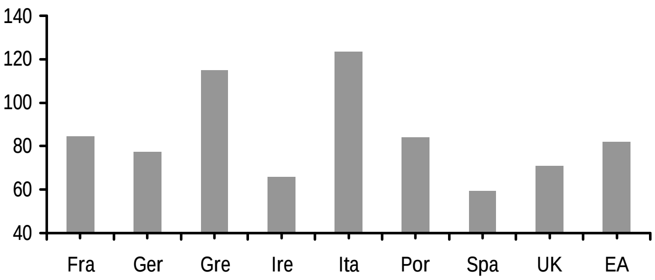
purely a gross concept, and so not even liquid assets are netted out from this measure of debt. Second, it refers just to the debt of the general government, instead of other public corporations. However, the latter of these two differences is usually relatively small. As with PSND ex, GGGD also includes general government borrowing associated with financial interventions.

What measure should be used? This depends on the question being posed. The PSND measure does not give a fair reflection of the UK's debt position at this point in time, for two reasons. First, it excludes large chunks of the assets from nationalized banks' balance sheets. Second, many of these effects will be temporary as the government's involvement in them is wound down over time. The PSND ex and GGGD measures avoid these issues as they exclude the balance sheets of the nationalized banks. However, one may argue that they also ignore some potentially significant future losses and contingent liabilities.

Future government liabilities

With regard to the financial crisis, the government had initially made the cautious assumption that these "net fiscal costs" would total 3.5% of GDP. But since then, financial markets have improved, and the equity prices of nationalized banks have risen from the very weak levels they were purchased at. The government in the 2010 Budget therefore slashed its estimate of the net fiscal cost of its interventions to 0.4% of GDP—immaterial relative to the outstanding public debt burden on any measure.

General government gross financial liabilities
% of GDP, OECD, 2009



When it comes to contingent liabilities, the more substantive issue is the demographic changes that will occur over the coming decades. An aging population will push up the cost of health care and state pensions, which the government will have to fund. This will partly be done through raising taxes and lowering government payouts where possible—e.g., raising the pension age or reducing entitlements. But some of these costs will be met from higher borrowing and could push up public debt significantly. Estimating these costs is very difficult due to the many uncertainties inherent in these calculations. In its Long Term Financing Report in 2006, the Treasury estimated that age-related spending in the UK would rise from the 20.8% of GDP in 2005-06 to 26% over the next 50 years. This is not a problem specific to the UK. And in terms of starting points before these age issues begin to bite, the UK's debt position may come as a surprise. At the end of 2009, the GGGD measure of debt in the UK was lower than the Euro area average, and even that of Germany and France.

Data releases and forecasts

Week of May 3 - 7

During the week

Halifax house price index
Seasonally adjusted

	Jan	Feb	Mar	Apr
%m/m	0.4	-1.6	1.1	<u>0.5</u>
%oya	3.4	4.1	6.9	<u>9.6</u>
%3m/3m saar	13.6	7.2	2.5	<u>-0.9</u>

The house price data have been more volatile of late, and this week's 1%m/m gain in Nationwide house prices was a surprise. We would continue to focus attention on the 3m/3m saar. Through the volatility in recent data releases, this measure, based upon the average of the Halifax and Nationwide measures, has continued to slow. We have penciled in another sequential gain of 0.5% for the Halifax in April. This would leave the 3m/3m saar of the Halifax showing a 0.9% drop. Though this is unlikely to be sustained, we remain of the view that the underlying trend remains toward softer house price gains this year.

Tue May 4 9:30am

PMI survey, manufacturing
% balance, sa

	Jan	Feb	Mar	Apr
Overall index	56.6	56.5	57.2	<u>57.7</u>

The survey is already very elevated, with the output reading at its second highest level on record. The CBI survey for April showed an impressive gain. We look for the output reading of the PMI to hold its ground for the same month—remaining around the 62 mark—with a broader improvement in the rest of the survey lifting the overall index around half a percentage point. This would leave the PMI pointing to manufacturing growth in the region of 5% ar. Our 2Q forecast for manufacturing is a touch softer at 4%.

Tue May 4 9:30am

Money supply [1]
Seasonally adjusted

	Dec	Jan	Feb	Mar
M4 ex IOFCs (%m/m)	-0.5	-0.1	0.3	__
M4 ex IOFCs (%3m/3m ar)	-1.6	0.6	-1.0	__
M4 (%m/m)	-1.0	0.3	0.2	<u>0.1</u>
M4 (%oya)	6.7	5.0	3.9	<u>3.5</u>

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M4 lending (%m/m)[2]	0.0	0.6	-0.1	0.4
M4 lending (%oya)[2]	4.7	5.1	3.8	3.3

1. Forecast taken from provisional release.
2. Excludes the effect of securitization.

The release of provisional M4 money and credit showed small gains in March. This release will reveal the sectoral detail of these gains. Recently, the money holdings of households and PNFCs have shown healthy growth firming, despite weak flows of bank credit—particularly to the corporate sector.

Tue
May 4
9:30am

Net lending to individuals (BoE release)

£ bn, average

	Dec	Jan	Feb	Mar
Consumer credit (ch, m/m)	0.3	0.5	0.5	0.5
Secured lending (ch, m/m)	1.2	1.5	1.6	1.5
Mortgage approvals (000s sa)	59.3	56.8	47.1	48.5

The BBA hinted at just a small gain in mortgage approvals in March. We continue to look for a gradual drift higher in the months ahead.

Wed
May 5
12:01am

Nationwide consumer confidence index

Sa

	Jan	Feb	Mar	Apr
Index	76	81	72	72

Though its broad trend has been stable, the Gfk consumer confidence survey surprised with another decline in April. We would have assumed the same in the Nationwide, but March showed a particularly large decline—and so we look for this reading to stabilize in April.

Wed
May 5
9:30am

PMI survey, construction

% balance, sa

	Jan	Feb	Mar	Apr
Overall index	48.6	48.5	53.1	__

Thu
May 6
12:01am

Markit report on jobs

% balance, sa

	Jan	Feb	Mar	Apr
Permanent placements	60.5	63.2	65.2	__
Permanent salaries	53.0	54.1	53.6	__
Availability of permanent staff	53.9	52.6	53.1	__

Thu
May 6
9:30am

PMI survey, services

% balance, sa

	Jan	Feb	Mar	Apr
Overall business activity	54.5	58.4	56.5	57.5

The business activity reading of the survey has shown greater volatility so far this year. But the March reading left the survey broadly in line with its recent average. We are expecting an acceleration in service sector growth in 2Q, and so we look for a gain of around a point in the services PMI. However, even at its current level, the survey points toward growth in the sector that is a percentage point or so stronger than our 3%q/q saar forecast for 2Q.

Fri
May 7
9:00am

New car registrations

%3m/12m nsa

	Jan	Feb	Mar	Apr
Total	41.5	32.7	27.3	__
Private (ex business and fleet)	93.6	72.8	37.8	__

Fri
May 7
9:30am

Producer prices

Nsa

	Jan	Feb	Mar	Apr
Input prices (%m/m nsa)	1.4	0.6	3.6	1.0
%oya nsa	7.7	7.5	10.1	13.2
Output prices (%m/m nsa)	0.4	0.3	0.9	0.3
%oya nsa	3.8	4.2	5.0	4.6
Core output prices[1] (%m/m nsa)	0.4	0.4	0.7	0.3
%oya nsa	2.6	3.0	3.6	3.5

1. PPI output ex food, beverages, tobacco, and petroleum products.

Core output prices have continued to show firm gains this year. However, the particularly strong rise in March was helped along by a surge in scrap metal prices, which may be unwound in April. We therefore look for a softer increase in core output prices of 0.3%m/m. Sterling oil prices rose in April and should push input prices up again. We have assumed a 0.3% gain in headline output prices, but the rise in energy could push these prices up by 0.4%.

Review of past week's data

BBA lending

	Jan	Feb	Mar
Secured lending (ch £bn, sa)	~~2.6~~ *2.5*	~~2.8~~ *2.7*	~~2.6~~ *2.4*
Loan approvals (000s sa)[1]	~~35.2~~ *35.4*	~~35.3~~ *33.4*	~~38.0~~ *34.9*

1. For house purchase.

See main text.

CBI survey of distributive trades

% balance

	Feb	Mar	Apr
Volume of retailer sales	23	13	~~14~~ *13*

See main text.

Nationwide house price index

	Feb	Mar	Apr
%m/m sa	~~-0.8~~ *-1.0*	~~0.7~~ *1.0*	~~0.4~~ *1.0*
%oya sa	9.3	9.1	~~9.6~~ *10.6*
%3m/3m saar	~~7.2~~ *6.9*	~~6.7~~ *6.3*	~~4.0~~ *4.4*

We have been expecting slower price gains this year, and the rise in the Nationwide in April is a surprise. However, since monthly price changes have been very volatile recently, we continue to focus attention on the 3m/3m saar. Through the recent volatility, this measure slowed a further 2%-pts to 4.3% in April, and is down from a 16% peak in September of last year.

Gfk consumer confidence

	Feb	Mar	Apr
% balance, sa	-14	-15	~~-14~~ *-16*

See main text.

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Russia

- **Economy waking up from winter sleep**
- **CBR cuts 25bp, as expected**

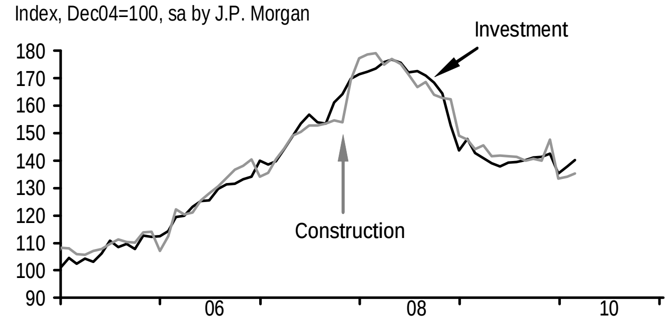
Most indicators of economic activity showed improvement in March. Both capital investment and construction rose from February; however, the growth was not impressive given the deep winter declines due mostly to cold weather. Investment increased 1.8%m/m sa (+0.7%oya, the first positive over-year-ago reading since October 2008), while construction rose 0.9%m/m sa in March (seasonally adjusted by J.P. Morgan). Transport turnover increased 1.1%m/m sa (12.4%oya), but compared to 4Q09, transport turnover in 1Q10 was still down about 0.6% sa (not annualized) on our estimates. The weakness in investment, construction, and associated activities at the start of the year was likely the prime reason for relatively weak expected 1Q10 GDP growth (J.P. Morgan forecast: 1%q/q saar, or 6.3%oya; consensus: 4.6%oya).

In consumption, visible improvement has continued in nonfood sales (+1.3%m/m sa), as firming consumer confidence and the end of consumer credit declines are lifting durable sales. The “cash-for-clunkers” scheme and growing car sales (included in retail sales in Russia) have further strengthened this trend. Retail food added about 0.3%m/m sa in March. However, consumption of services shrank about 0.5%m/m sa. In addition, after employing the data from the SME survey, Rosstat revised up its estimate of retail sales for 2009 to -4.9%y/y from -5.5%y/y. Consumer retrenchment last year thus appears to have been less dramatic than thought. A lighter fall in final sales amid very deep declines in domestic output last year means that companies cut inventories perhaps even more aggressively than currently estimated (destocking explained 6.4%-pts of the 7.9% GDP collapse in 2009). This adds to hopes that production will continue to recover gradually through 2010 as firms end destocking (unless growing demand is satisfied by imports).

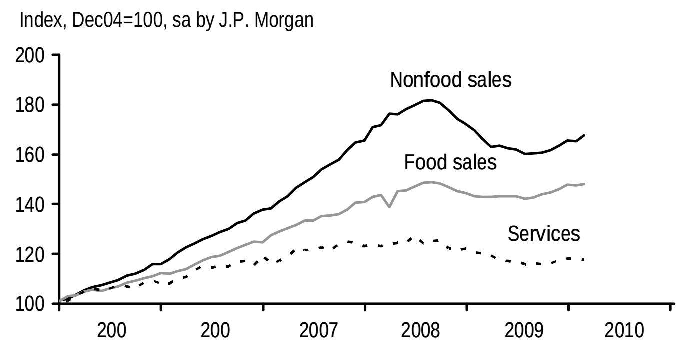
On the negative side, unemployment quashed part of the strong February gain, staying unchanged at 8.6% nsa or increasing around 0.2%-pt in seasonally adjusted terms (after falling 0.7%-pt in February). We are not inclined to read too much into this slight setback. The falling trend for unemployment seems to have been robust from mid-2009 (third chart).

Despite improving demand dynamics, tentative signs of recovery in credit activity, and less dovish CBR rhetoric in recent weeks, the central bank cut its key operational rates, the deposit and the repo rate, by 25bp last week. The cut was in line with both our expectations and those of many in the market (though some expected no cut). Some analysts appeared to have been influenced by less dovish comments by CBR officials and the Minister of Finance. In our view, the change in rhetoric was to signal the approaching end of monetary policy easing , now apparent in the CBR statement, which changed notably compared to the March release. The assessment of domestic demand growth has improved, though the recovery is still considered unstable.

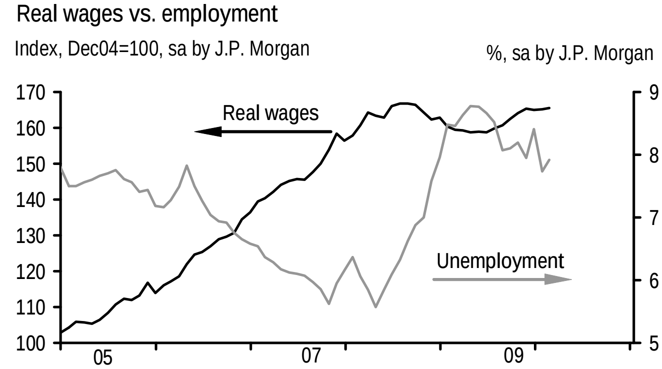
Capital investment vs. construction



Real retail sales and consumption of services



Real wages vs. employment



The Russia data watch is published biweekly, next on May 14.

The risk of short-term capital inflows attracted by a high carry was dropped from the statement. Inflation dynamics are still considered favorable, but the notion of “no preconditions for faster price growth this year” was changed to the statement that over-year-ago inflation may increase in 2H10, though partly on base effects. As a result, further rate changes would demand a more detailed analysis of inflation trends, according to the CBR.

Given the change in rhetoric, further rate cuts will likely be delivered only if the recovery remains sluggish, credit activity weak, and inflation expectations low in the coming months. We have been expecting rate cuts in 2Q10 to be the last in this cycle, so the CBR signal is broadly in line with our expectations. We maintain that the CBR will cut key operational rates by an additional 25bp by the end of the second quarter, but acknowledge that the risks to our call are now probably skewed to the downside (no cut).

Data releases and forecasts

Weeks of May 3 - 14

Consumer prices

	Jan	Feb	Mar	Apr
%m/m nsa	1.6	0.9	0.6	0.4
%oya	8.0	7.2	6.5	6.2

Federal budget

RUB bn, cash flows

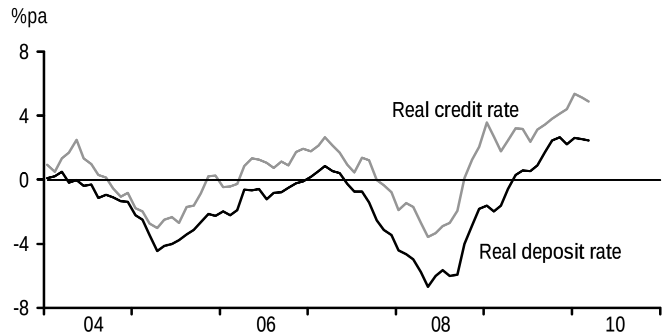
	Jan	Feb	Mar	Apr
Balance	87	-257	-138	-140
% of GDP	3.0	-7.9	-3.9	-3.8
Revenue	738	571	645	660
Tax revenue	576	537	626	630
% of GDP	19.7	16.5	17.8	17.2
Expenditure	651	827	783	800
Noninterest	634	809	748	770

Merchandise trade

US$ mn, nsa

	Dec	Jan	Feb	Mar
Trade balance	12.6	16.5	15.2	14.7
Exports	34.2	27.9	30.6	33.2
%oya	19.7	55.5	64.7	60.0
Imports	21.6	11.3	15.4	18.6
%oya	-9.8	7.6	14.8	28.0

Real interest rates: retail deposits and company loans (CPI-deflated)



Review of past two weeks’ data

Real economy indicators

Real terms, %oya

	Jan	Feb	Mar	
Construction	-10.7	-9.8	~~-8.0~~	*-5.1*
Agriculture	3.2	3.3	~~3.0~~	*4.1*
Transportation	12.2	9.8	~~7.5~~	*12.4*
Retail sales	0.0	0.9	~~2.5~~	*2.9*
Fixed investment	-8.7	-7.4	~~-6.0~~	*0.7*
Income per capita	15.5	5.0	~~0.0~~	*4.2*
Average monthly wage due	1.2	2.5	~~3.3~~	*3.4*

Industrial producer prices

	Jan	Feb	Mar	
%m/m nsa	-1.0	2.3	~~0.6~~	*1.8*
%oya	33.1	22.9	~~20.1~~	*19.2*

Broad money supply

	Jan	Feb	Mar	
Broad money, M2	15331	15566	~~16138~~	*15997*
%m/m nsa	-2.3	1.5	~~3.7~~	*2.8*
%oya	27.9	29.5	~~33.2~~	*32.1*
Cash in circulation	3873	3950	~~4120~~	*3986*
%m/m nsa	-4.1	2.0	~~4.3~~	*0.9*
%oya	16.9	19.6	~~25.7~~	*21.6*
Bank deposits	11458	11616	~~12018~~	*12010*
%m/m nsa	-1.7	1.4	~~3.5~~	*3.4*
%oya	32.0	33.2	~~36.1~~	*36.0*

International reserves

US$ bn, eop

	Jan	Feb	Mar 26	
Gross international reserves	435.8	436.3	___	*444.0*
Gold	22.3	23.0	___	

Market indicators

End of period

	Feb	Mar	Apr 29
USD/RUB (official CBR)	29.95	29.50	29.29
RTS index (US$ terms)	1411	1573	1589

Turkey

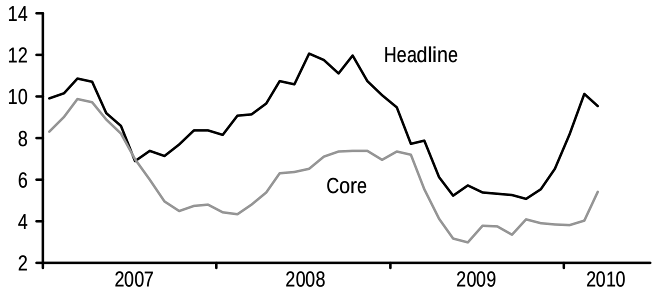
- **The CBRT revised up its inflation forecasts, but is determined to remain on hold until 4Q**
- **We expect the CBRT to hike rates by 200bp this year and 100bp in 2011**
- **Ongoing problems in the Euro area are the main risk**

The CBRT revised up its inflation forecasts substantially, and more importantly the Bank explicitly stated in its quarterly inflation report that the policy rate would remain unchanged until the last quarter of the year. Given the CBRT's strong determination to keep rates unchanged in the short term, we have revised our monetary policy and inflation forecasts. We still expect a total of 200bp of hikes in 2010, but we have pushed back the start of the hiking cycle to September from June. Including the technical rate adjustment (whereby the 1-week repo rate becomes the policy rate), we expect four 50bp hikes in the last four months of the year and thus see the policy rate at 8.5% by year-end. Given the general elections in July 2011 (which could be brought forward to May) and the appointment of the CBRT governor in April 2011, we think that the CBRT will be inclined to remain on hold in the first half of 2011. However, in light of worsening inflation prospects, we expect it to deliver two 50bp hikes in 2H and see the policy rate at 9.50% at end-2011. We are keeping our end-2010 CPI inflation forecast unchanged at 8.1%Dec/Dec, but we are revising our end-2011 forecast up to 6.8% from 6.5%. We see inflation falling to 5.0% by end-2012.

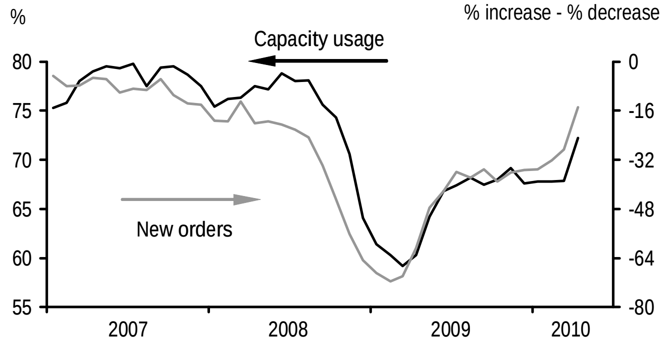
The inflation report shows the CBRT's continued belief that total demand conditions are supporting the disinflation process. The CBRT notes that although the recovery across emerging economies seems to be stronger, ongoing problems across developed economies—with their prominent role in global trade—still create downside risks for emerging economies. Moreover, constraints related to external finance could delay the recovery in many emerging economies. According to the inflation report, "assuming that the liquidity measures are normalized gradually over the short term and that policy rates are kept constant at current levels for some time followed by limited increases starting in the last quarter of 2010, with policy rates staying at single digits throughout the three-year forecast horizon," the Bank sees inflation at 8.4%Dec/Dec at end-2010 and at 5.4% at end-2011. In line with our forecast, the CBRT expects inflation to fall to 5.0% by end-2012. Interestingly, the new forecast for end-2010 is just below 8.5%, i.e., the upper band of the inflation target, and the new forecast for end-2011 is just below the official target of 5.5%. The 2010 forecast seems reasonable, but the 2011 forecast is overly optimistic, in our view.

Headline and core CPI

%oya



Capacity usage in manufacturing and orders received



We think the later-than-expected rate hikes, and the worsening in inflation expectations that will likely follow, increase the inflation risks. Yearly headline inflation stands at 9.6%, but is expected to reach 11% within two months. Yearly core inflation jumped to 5.4% in March from 4.1% in February, showing that inflation pressures have become more broad-based. However, we are still comfortable with our end-2010 inflation forecast mainly because of our expectation that some legislative changes (e.g., lifting the ban on meat imports and streamlining the wholesale fruit and vegetable markets) should offset the inflation pressures. In 2011, however, wage pressures are likely to push inflation higher. Following the increase in official inflation forecasts and given the looming general election, we believe public sector wage increases could reach 10% next year.

External factors constitute the main risk to our inflation and monetary policy calls. In particular, problems in Euro area countries will likely hit the growth prospects in the region. If these problems increase in severity and if global risk appetite weakens significantly, the resulting worsening in Turkey's growth prospects could urge the CBRT to delay the hiking cycle.

The Turkey data watch is published biweekly, next on May 14.

Data releases and forecasts

Weeks of May 3 - 14

Mon
May 3
10:00am

Inflation

%

	Jan	Feb	Mar	Apr
Consumer prices				
%oya	8.2	10.1	9.6	10.3
%m/m	1.9	1.5	0.6	0.7
Producer prices				
%oya	6.3	6.8	8.6	9.3
%m/m	0.6	1.7	1.9	1.3
Core CPI (I)				
%oya	3.8	4.1	5.4	6.0
%m/m	-0.5	-0.5	0.6	1.5

Inflation pressures are on the rise as economic activity picks up and inflation expectations worsen. While a seasonal rise in clothing prices should be the main contributor to headline inflation, price pressures will likely be present in most of the subcategories. The expected rise in core inflation could lead to further worsening in expectations.

Mon
May 10
10:00am

Industrial production

%oya

	Dec	Jan	Feb	Mar
Total	23.5	12.3	18.0	16.1
Manufacturing	28.1	14.5	20.4	18.0
Mining	15.0	0.5	12.2	9.4
Energy and utilities	10.9	3.2	5.0	5.5

Although the gradual recovery in domestic and external demand along with some inventory building is likely helping, the main factor behind elevated yearly growth should be the extremely weak base. Turkey is likely to exhibit double-digit GDP growth in the first quarter of the year.

Tue
May 11
10:00am

Balance of payments

US$ bn

	Dec	Jan	Feb	Mar
Current account	-3.2	-3.0	-2.6	-4.1
Trade balance	-3.4	-2.7	-2.2	-3.8
Exports, fob	10.7	8.3	8.9	10.6
Imports, fob	14.2	11.0	11.1	14.4
Net invisibles and transfers	0.2	0.3	-0.4	-0.3
Capital account	2.4	1.8	0.4	2.5
Overall balance	1.3	0.7	1.7	0.5

The current account deficit likely widened on the back of stronger imports in March. The 12-month trailing CAD likely widened to US$21.7 billion (3.3% of GDP) in March from US$18.8 billion (2.9% of GDP) in February. The widening in the 12-month trailing deficit might look alarming at first glance, but it is mainly due to a very weak base, and the pace of widening will likely come down within a few months. Financing should not be a problem, as portfolio inflows pick up and the Treasury manages to borrow from abroad comfortably.

Central government budget

TRY bn, current prices

	Jan	Feb	Mar	Apr
Expenditures	22.6	22.3	23.4	25.3
Interest	6.0	4.6	4.3	5.8
Noninterest	16.6	17.7	19.1	18.5
Revenues	19.5	20.0	17.5	20.0
Taxes	17.3	16.1	14.5	17.0
Primary balance	3.0	2.3	-1.6	1.5
Budget balance	-3.1	-2.3	-5.9	-4.3

Fiscal performance likely continued improving in April on the back of a cyclical improvement in tax collection and some discipline on the spending side.

Review of past two weeks' data

Capacity utilization

%

	Feb	Mar	Apr
Total manufacturing	67.8	67.9	~~68.3~~ *72.2*
Durables	65.5	64.1	~~65.5~~ *67.5*
Nondurables	69.6	69.9	~~70.5~~ *72.1*

In April, manufacturing capacity usage reached its highest level since October 2008. Furthermore, the m/m increase was the sharpest increase seen in the past six years. Importantly, the recovery was quite uniform across sectors with each sector reporting an increase.

Foreign trade

US$ bn, except as noted

	Jan	Feb	Mar
Trade balance	-3.7	-3.4	~~-4.4~~ *-5.0*
Exports, fob	7.9	8.3	~~9.8~~ 10.0
%oya	-0.2	2.3	~~20.1~~ *22.4*
Imports, CIF	11.5	11.8	~~14.2~~ *15.0*
%oya	24.2	29.8	~~34.9~~ *42.7*

The sharp rise in imports (especially in consumer good imports) showed that the recovery in domestic demand is gaining pace. The recovery in exports should lag behind given the gradual recovery in many of the export markets, particularly the Euro area.

Central government debt

US$ bn

	Jan	Feb	Mar
Domestic debt stock	226.5	221.0	~~223.2~~ *223.9*
Market	185.1	180.8	~~182.5~~ 183.0
Public sector	41.4	40.2	~~40.7~~ 40.9
External debt stock	75.7	73.7	~~74.0~~ *74.3*
Loans	33.1	32.7	~~32.5~~ *32.4*
Bonds	42.6	41.0	~~41.5~~ 41.9
Total debt stock	302.2	294.7	~~297.2~~ *298.2*

Although central government debt remained flat in TRY terms, in USD terms there was an increase due to the lira's appreciation against the dollar. As the government makes further fiscal adjustments, we expect an improvement in debt dynamics in the second half of the year.

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Australia and New Zealand

- **High 1Q CPI bolsters case for RBA hike next week**
- **Retail sales probably subdued in March**
- **RBNZ on hold, but guidance changed**

This week's 1Q Aussie inflation report delivered modest upside surprises on the main measures, thereby boosting the case for another RBA rate hike on Tuesday. Indeed, the annual rate of core inflation is at the top of the RBA's target range. There remains, though, considerable uncertainty around the outcome of next week's meeting, particularly given the troubling events unfolding in the Euro area. We still call for a 25bp hike next week, which will be the sixth in the past seven meetings, but the decision is a close one.

The RBNZ this week left the cash rate steady, but indicated that policy stimulus will be removed "over the coming months." This was a subtle, but important shift away from previous guidance, which had locked the bank into a "mid-year" hike. We continue to call for the first hike in July.

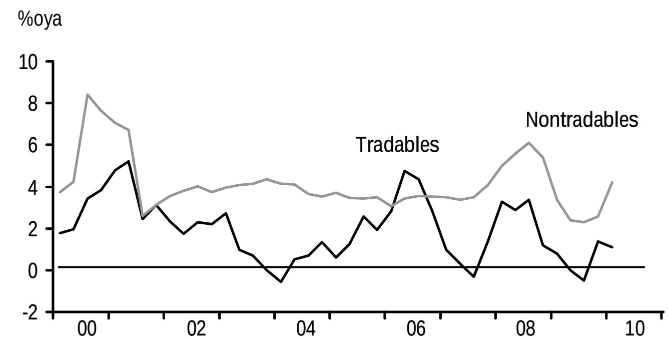
RBA to hike and lift inflation forecast

The RBA Board meets Tuesday; we expect a 25bp hike, a view we have held for some time. This week's upside surprise on all three measures of the CPI—headline and the two main core measures—bolstered the case for a rise, as did recent news that contract prices for coal and iron ore, Australia's two largest export commodities, rose 60% and 100%, respectively, from April 1. Recent data prints on the domestic economy have been mixed, but commentary from RBA officials has indicated that further rate hikes are very likely. The debate now is over the timing of the moves, which remains difficult to predict from month to month.

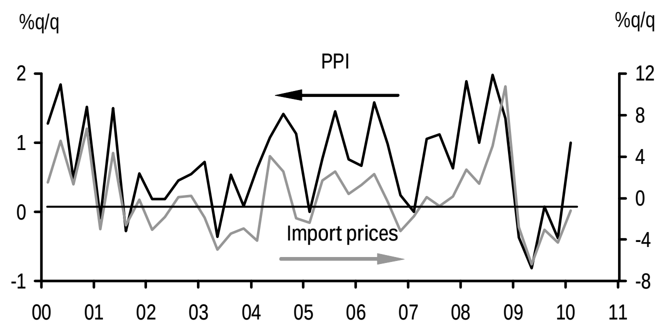
Indeed, next week's decision remains a close call. What seems an open and shut case for a rate hike is complicated by recent events in Europe, which may prompt Board members to tread carefully. If so, assuming events offshore do not escalate, skipping a rate increase next week merely would delay the move until June. The cash rate is below average and is too low for an economy growing at trend, particularly with the income side of the economy about to enjoy a sustained boost from the soaring terms of trade.

On Friday, the RBA releases the Statement on Monetary Policy (SoMP), which we believe will include upgrades to the official GDP growth and inflation forecasts. This week's elevated inflation prints for 1Q imply that the current published official inflation forecasts are too low.

Australia: tradables and nontradables inflation



Australia: PPI and import prices



Price pressures resurfacing in Australia

The general message from this week's relatively high prints on PPI and CPI is that upstream price pressures have arrived and are feeding through to the consumer more quickly than expected after a moderate, but brief downturn. The 1Q headline CPI measure printed slightly above expectations at 0.9%q/q nsa (J.P. Morgan and consensus: 0.8%), having briefly dipped to a soft 0.5%q/q in the December quarter. The annual rate of headline inflation rose for the second quarter in a row, up to 2.9%oya (from 2.1%), with year-ago base effects (in particular the outright decline in headline CPI in 4Q08) continuing to fade out. The core inflation prints averaged 0.8% in 1Q (trimmed mean 0.8%, weighted median 0.8%), again slightly above our forecast. The annual average rate of change on the core measures dipped slightly to 3.1%oya, but remained above the RBA's 2%-3% target range for the eleventh straight quarter.

The "usual suspects" were all influential in the upward move in the CPI, with a 4.2%q/q rise in the price of automotive fuel, a 10.3% rise in the price of vegetables (and a 1.1% rise in the broader food group), and a 2.0% rise in financial and insurance services over the quarter. However, there was significant "event-related" repricing in several other components as well. Education costs rose 5.6% over the quarter owing to the start of the new school year, and health costs rose 4.7%, thanks to a cyclical reduction in the proportion of individuals eligible for the Pharmaceutical Benefit Scheme. Finally, electricity prices rose 5.9% due to tariff increases in Melbourne, and severe-weather-induced peak-period pricing in Adelaide.

Nontradables inflation, which reflects domestic inflation pressures and is unaffected by the currency, printed at 1.5%q/q, and jumped to 4.2%oya in 1Q from 2.6%oya in 4Q. In contrast, tradables inflation continues to be depressed by the strengthening of the currency over the past year, and is now hovering around 1.1%oya. Given the core and nontradables inflation prints, the medium-term inflation outlook presents challenges. On our forecasts, core inflation will remain elevated near 3% this year. The narrowing of the output gap, combined with the recent turnaround in the labor market (the unemployment rate has peaked at a remarkably low 5.8%) will halt the downward descent of core inflation in 2010, and result in a lofty base for 2011, when capacity constraints will really start to bite.

Aussie retail sales probably soft in March

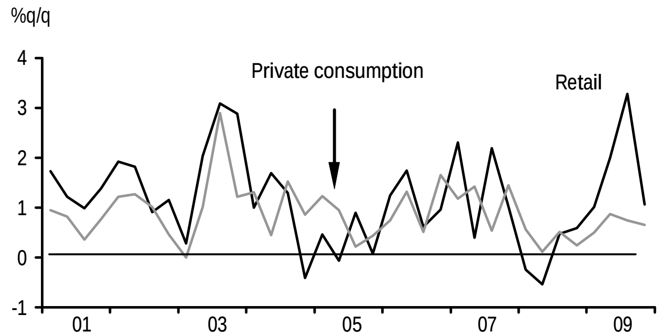
The March retail sales report on Thursday should show that sales remained sluggish. The RBA hiked the cash rate early in March, which will be a drag on spending, and anecdotes from retailers show that sales were soft. Consumer confidence is high, but there appears to have been some price discounting during the month. This was prompted partly by an elevated AUD, but, in some cases, by a desire to boost turnover. We expect only a 0.2%m/m gain in sales, after the 1.4% plunge in February. Sales over the quarter probably will have been close to flat in volume terms.

The winding down and expiration of the expanded First Home Buyers' (FHBs') grant has noticeably depressed home loan demand and building approvals, but has left dwelling prices and broader market sentiment surprisingly untouched. On the evidence accumulated so far in 2010, last year's stimulus-induced buy-in is depressing the current volume of housing purchasers and investors, but the remaining individuals' willingness to pay is well-supported due to a healthy labor market and the momentum garnered in prices over 2009. As such, we expect that the softness in building approvals data continued in March, with the number of approvals down 1%m/m. House price appreciation, on the other hand, will have slowed only mildly, to 3.5%q/q in 1Q10 from the gangbuster 5%-plus growth rate in 4Q09.

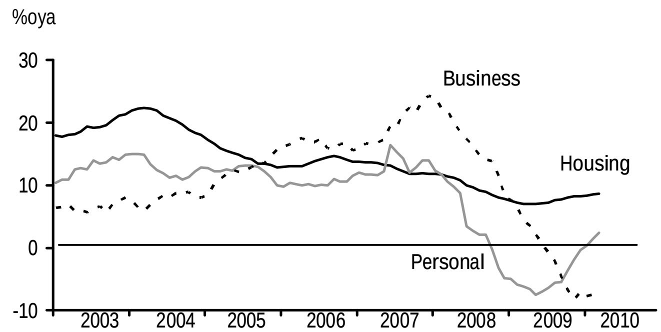
Business credit finally expands

This week's credit and lending aggregates showed a continued improvement in credit growth over the first quarter of the year. Credit growth increased in March to 0.5%m/m, owing partly to the expansion of business credit. Housing credit again was the fastest-growing pool, though we expect some deceleration in the months to come, owing to the winding back of the government's expanded First Home Buyers' grant. Personal credit rose a further 0.5%, and has been increasing at a healthy clip since July 2009.

Australia: private consumption and retail trade volumes



Australia: private sector credit aggregates



The bell-ringer in this report, however, was the return to growth in business credit. Credit conditions have been particularly tight for small to medium-sized businesses since the onset of the financial crisis, and have been slow to recover. This has not hampered the recovery in Australia, since the big end of town has had adequate access to global capital markets. Given that some of the banks have had their fill of mortgage lending during the First Home Buyers' splurge, a rebalancing of the loan book toward business lending should result in a further easing in credit conditions in the future.

RBNZ to start hiking in "coming months"

The RBNZ left the official cash rate (OCR) at a record low 2.5% this week, as expected. While market economists were unanimous in their anticipation that the RBNZ would leave policy on hold, the accompanying statement did offer some new verbiage to mull over. Given the softening on the official data front in recent weeks, in particular, after

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the benign 1Q inflation print (which came in below market expectations at 0.4%q/q), we had expected that the statement would drop the reference to a planned removal of policy stimulus "around the middle of 2010." This was indeed the case: that phrase was jettisoned and replaced by a similarly opaque "in coming months."

While it is tempting to speculate on what this new phrasing means for the timing of the first hike, we are reluctant to claim that the change represents anything substantive. Nonetheless, there are two significant aspects to this change. First, the fact that the language was changed at all does, at least, indicate that officials are less certain of the stability of the domestic recovery than they had envisaged. This, of course, reflects the recent run of softer domestic data. Second, the new language is atemporal, i.e., it can be continuously rolled over from month to month, if the recovery fails to take hold. The fact that the RBNZ is allowing itself the flexibility to defer hiking, we believe, adds a slightly dovish tone compared to the previous statement.

The domestic economy, according to RBNZ Governor Bollard, is, as in previous statements, still "recovering broadly as expected and growth is predicted to pick up further through 2010." Similarly, the tone of the references to specific sectors was broadly unchanged, although the emphasis has shifted slightly to a more export-led recovery.

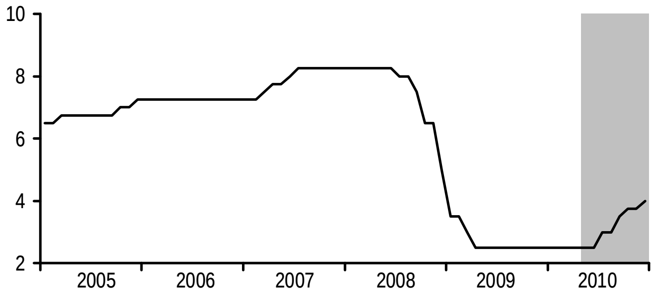
We continue to expect that the RBNZ will begin the normalization of policy with a 25bp hike at the July meeting. But, there have been false starts to the recovery so far, which officials are clearly wary of, and there are other elements doing some heavy lifting for the Bank, including "an increasing wedge between the OCR and lending rates," and a steeper yield curve. These factors, though, are arguments for a more gradual normalization of policy, rather than a substantially delayed start. By July, the RBNZ should have two healthy GDP prints in hand, after the solid 0.8%q/q result in 4Q09 and our forecast for another 0.8% rise in 1Q10. By then, the case for keeping the cash rate at historic lows should have weakened substantially.

NZ unemployment to have peaked in 1Q

The unemployment rate in New Zealand probably remained unchanged at 7.3% in 1Q, which we expect to be the peak in the jobless rate. The details of the employment report should show that the number of employed persons increased in 1Q after four straight quarters of declines: total employment, having contracted 0.1%q/q in the previous three months, should have increased 0.2% in 1Q. The labor force participation rate probably held steady at 68.1%.

New Zealand: RBNZ official cash rate

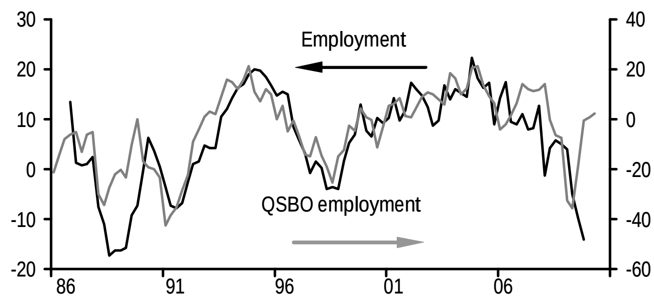
pre-March 1999 = discount rate, percent per annum, eop



New Zealand: employment and QSBO expectations

Quarterly change, 4 qtr mov. avg, thousands

Net balance, 1 qtr lead



We suspect that we have seen the low point in the Kiwi employment cycle, remembering also that employment is a lagging indicator. Any improvement in the labor market going forward will, however, be gradual. The NZIER quarterly surveys have showed that hiring intentions have been marginally positive in recent quarters (+2% in 1Q and +1% in 4Q), but actual hiring is still below long-run averages. With corporate profitability having fallen in 1Q, any significant pickup in new hiring may be delayed. This means that, although the unemployment rate has probably already peaked with excess capacity in the labor market, wage growth will remain subdued this year. We expect data next week to show that growth in private sector labor costs remained subdued in 1Q. The private sector labor cost index, which of the various wage measures receives the most attention from the RBNZ, should have risen 0.3%q/q in 1Q, the same rate as in the previous three months.

Confidence back to previous highs

The headline reading on the NBNZ business confidence index recovered almost all of the previous month's fall in April, rising to 49.5 from 42.5 in March (J.P. Morgan forecast: 44.0). At current levels, the survey indicates that almost 75% of Kiwi firms expect an improvement in general business conditions. We had anticipated a rise in the headline confidence index, owing to fewer global financial jitters over the survey period, although this week's result was

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a significant upside surprise. Clearly, buoyant global growth (particularly demand conditions in the Asian region) is boosting the export outlook for New Zealand firms.

Of more direct significance to the domestic economy's prospects, the all-important firms' own activity outlook index also posted an outsized gain in April, moving up to 43.0 from 38.6. According to the NBNZ, the improvement in confidence over the month was relatively broad-based across sectors.

Australia:

Data releases and forecasts

Week of May 3 - 7

Mon
May 3
11:30am

House price index: eight capital cities

Weighted average

	2Q09	3Q09	4Q09	1Q10
%q/q	4.3	4.4	5.2	3.5
%oya	-0.6	6.6	13.6	18.5

Tue
May 4
2:30pm

RBA cash rate announcement

25bp hike expected.

Wed
May 5
11:30am

Building approvals

sa

	Dec	Jan	Feb	Mar
%m/m	5.1	-5.5	-3.3	-1.0
%oya	55.6	52.7	34.2	23.1

Thu
May 6
11:30am

Retail trade

sa

	Dec	Jan	Feb	Mar
%m/m	-0.8	1.1	-1.4	0.2
%oya	2.0	3.0	3.4	1.1

Retail trade ex inflation

	2Q09	3Q09	4Q09	1Q10
%q/q	1.8	-0.7	1.1	0.1
%oya	4.1	3.2	3.4	2.2

Thu
May 6
11:30am

Trade balance

sa

	Dec	Jan	Feb	Mar
Trade balance (A$ mn)	-2021	-1120	-1924	-1500

Review of past week's data

NAB business confidence

	3Q09	4Q09	1Q10	
% balance, sa	16	18	__	*17*

Producer price index

	3Q09	4Q09	1Q10	
%oya nsa	0.2	-1.5	~~-0.6~~	*-0.1*
%q/q nsa	0.1	-0.4	~~0.6~~	*1.0*

Consumer price index

	3Q09	4Q09	1Q10	
Headline				
%oya nsa	1.3	2.1	~~2.8~~	*2.9*
%q/q nsa	1.0	0.5	~~0.8~~	*0.9*
Core (trimmed mean)				
%oya nsa	3.2	3.2	3.0	
%q/q nsa	0.8	0.6	~~0.7~~	*0.8*

Private sector credit

	Jan	Feb		Mar	
%m/m sa	0.4	0.4		0.5	
%oya sa	1.3	~~1.6~~	*1.7*	~~1.9~~	*2.1*

New Zealand:

Data releases and forecasts

Week of May 3 - 7

Mon
May 3
3.00pm

ANZ commodity price series

nsa

	Jan	Feb	Mar	Apr
Index—world prices (%m/m)	0.4	3.8	1.8	__
Index—NZD (%m/m)	-1.2	7.9	0.4	__

Tue
May 4
10:45am

Labor cost index and average hourly earnings

Private sector, ordinary time, sa

	2Q09	3Q09	4Q09	1Q10
%q/q	0.3	0.4	0.3	0.3

Thu
May 6
10:45am

Labor force survey

sa

	2Q09	3Q09	4Q09	1Q10
Unemployment rate (%)	6.0	6.5	7.3	7.3
Employment (000s, q/q)	-10	-17	-2	4.9
Participation rate (%)	68.4	68.0	68.1	68.1

Review of past week's data

NBNZ business confidence

	Feb	Mar	Apr	
% balance of respondents	50.1	42.5	~~44.0~~	*49.5*

RBNZ cash rate announcement

No change delivered. See main text.

Trade balance

	Jan		Feb		Mar	
Trade balance (NZ$ mn, nsa)	~~263~~	*271*	~~321~~	*335*	~~400~~	*567*

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Greater China

- **China: shift to private sector as essential contributor to growth evident in latest fixed asset investment data**
- **Overall fixed investment growth expected to moderate this year, helping to ease CPI inflation pressure**
- **Hong Kong: further rebound in March trade activity, led by booming regional trade**
- **Taiwan: March leading indicator rose again; global capex upturn to support exports**

One of the major features of China's growth this year is the shift in the primary contributor, with economic activity becoming less dependent on public sector investment and less credit-intensive compared to 2009. We expect the pace of fixed investment growth—the crucial support for headline GDP growth last year—to moderate to 22.5% this year from 31% (see "China: investment to moderate, but still grow at a solid pace," *GDW*, January 29). The latest data on fixed asset investment have been broadly in line with this view.

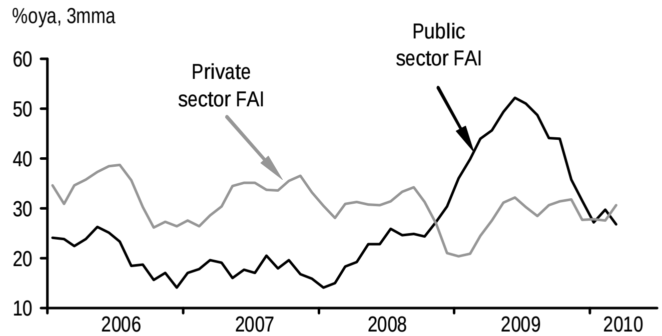
Moderating public investment

The breakdown of recent investment data shows a clear trend of moderation in public investment growth (first chart). The central government has repeatedly reaffirmed that it will maintain its stimulative fiscal policy stance, implying continued fiscal spending to complete ongoing projects. But, given rising concerns about overcapacity, inefficient spending, and local governments' financing conditions, the central government has strengthened its control over the approval of new local government investment projects since late last year. Details on fixed investment by industry show steady moderation in infrastructure-related fixed asset investment (FAI) (table).

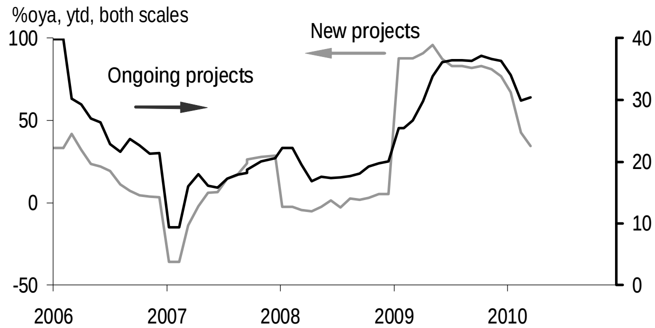
Solid private sector FAI

Meanwhile, private sector FAI, which had underperformed total FAI since late 2008, has been holding up well in recent months. With growing signs of improvement in external demand and export orders, export-related FAI growth—including machinery and electronic equipment and textiles and related industries—has largely held firm. In addition, while real estate FAI growth moderated somewhat in late 2009, the pace of expansion has picked up again (third chart). Given the latest series of notable policy tightening targeting the property sector, however, transaction volume has declined in recent weeks, with prices stabilizing, which would likely cause real estate developers to be more cautious when investing. Meanwhile, as the govern-

China: public and private sector FAI



China: ongoing and new fixed investment projects

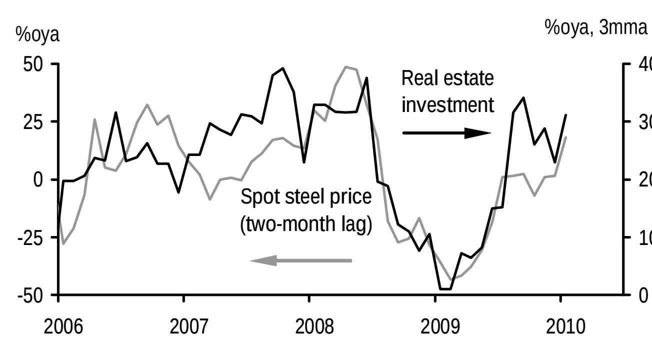


China: nominal fixed asset investment

	2009	1H09	3Q09	4Q09	1Q10
	%share	%oya	%oya	%oya	%oya
Total	100.0	33.6	32.9	26.2	26.4
Primary industry[1]	1.7	68.9	37.4	38.4	9.7
Textile and related	2.0	11.2	15.5	28.3	21.0
Machinery and electronic equipment	7.4	34.4	29.0	35.0	27.9
Metal and commodities	11.5	27.9	17.8	17.7	39.5
Transportation equipment	2.6	36.7	37.5	18.0	17.3
Electricity, gas, and water production[1]	6.9	28.7	25.4	31.3	9.7
Housing	22.2	15.3	33.9	22.0	36.2
Transport infrastructure and construction[1]	13.0	63.4	51.2	36.3	27.0
Water conservation, environment management[1]	9.2	54.5	46.2	34.6	24.5
Healthcare, social security, education, culture[1]	4.2	55.3	55.6	28.6	26.0

1. Sectors targeted for expansion by the government.

China: real estate investment and domestic spot steel price



ment has pledged to increase the supply of low-income housing, total real estate investment will likely rise steadily this year.

Implications for CPI inflation

The moderating pace of investment growth has important implications for inflation. Indeed, looking back to recent cycles, episodes of surging headline CPI were often associated with accelerating FAI growth. As such, the expected moderation in FAI growth this year suggests that demand-pull inflation pressure may not be as severe as some fear, which is an important factor behind our forecast for a moderate 3.2%oya rise in headline CPI for all of 2010. Indeed, it should be noted that the pace of gain in PPI has been easing steadily, to 0.2%m/m sa in March from 0.6%m/m sa in February and 1.8%m/m sa in December 2009. Also, as China's imports of commodities and machinery are closely related to the fixed investment cycle, our FAI outlook suggests the pace of gain in China's imports of raw materials/commodities is likely to ease somewhat in coming quarters.

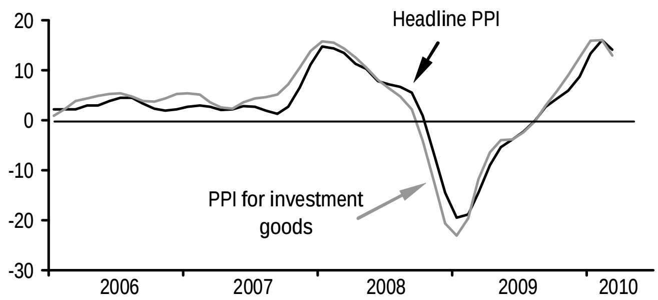
Hong Kong: March rebound in trade

Hong Kong's trade sector expanded significantly in March. The value of total exports rose 32.1%oya, compared to 28.5%oya in February. Seasonally adjusted, this translates into growth of 2.6%m/m sa in March, with sequential trend growth moderating to a still decent 45.0%3m/3m saar. Meanwhile, imports rose 39.8%oya in March, translating into a 3.9%m/m sa gain, with the sequential trend also moderating to 45.5%3m/3m saar through March. The trade deficit widened to HKD38.9 billion last month, compared to HKD19.7 billion in February.

A breakdown by destination suggests strong growth (+44.4%oya) in the value of exports to Asia, specifically exports to Malaysia (+51.4%), India (+50.3%), Thailand (+49.5%), and mainland China (+47.4%). Growth was also evident in exports to some other major destinations such as the US (+4.5%oya), while exports to the UK and Germany posted decreases of 15.6%oya and 8.5%, respectively. Meanwhile, the value of total imports from each of Hong Kong's major suppliers also posted notable increases, in particular from Taiwan (+62.0%oya), Japan (+57.4%), Thailand (+5.2%), Korea (+51.9%), and mainland China (+25.7%). Analysis by sector suggests that there were significant increases in the trade value of most principal commodity divisions, such as electrical machinery, apparatus, and electrical parts.

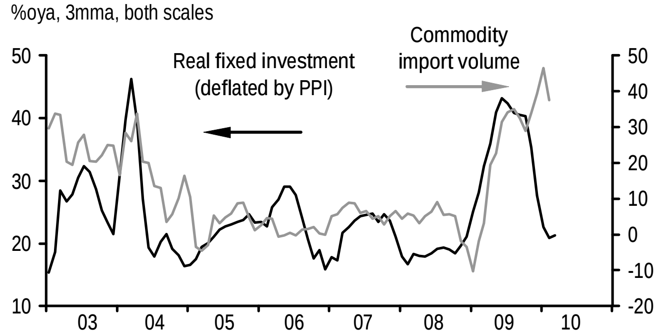
China: headline PPI and PPI for investment goods

%3m/3m, saar



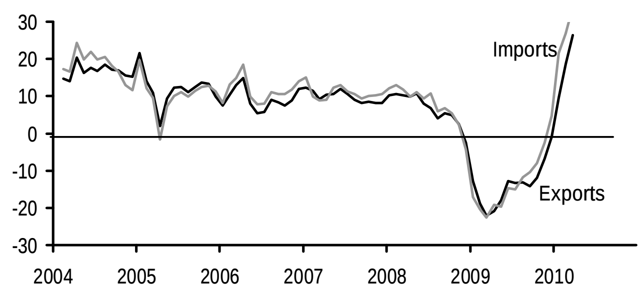
China: fixed investment and commodity imports

%oya, 3mma, both scales



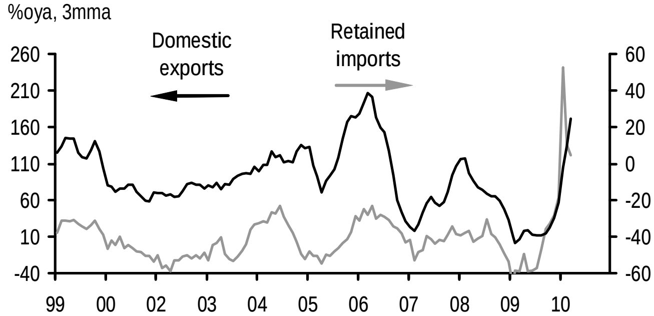
Hong Kong: merchandise trade

%oya, 3mma



Hong Kong: domestic exports and retained imports

%oya, 3mma



Hong Kong's merchandise exports in March have returned to their level prior to the 2008 financial crisis, largely driven by the strong expansion of intra-Asia trade flows. Although the pace of recovery of trade with the US and UK markets remains moderate, we believe that a steady recovery in the global economy will contribute to the regional trading sector, thereby benefiting Hong Kong's merchandise trade further this year.

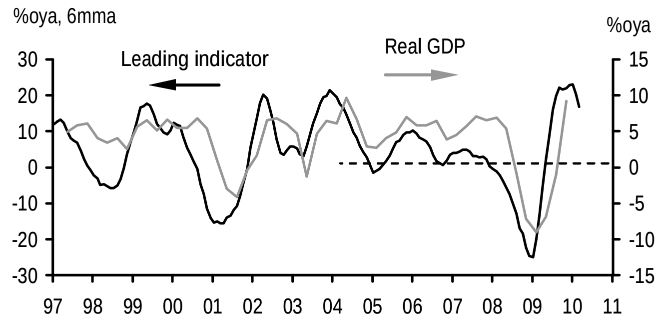
Taiwan: leading indicator rose further

Taiwan's composite index of leading indicators rose in March for the fourteenth consecutive month, up 0.3%m/m sa to reach 109.3, on top of the 0.8%m/m gain in February. The annualized six-month rate of change, which historically has tended to lead real GDP growth by about a quarter (first chart), was 16.9% in March, moderating from 20.3% in February, suggesting that the pace of headline GDP growth in percentage over-year-ago terms likely peaked in 1Q10, in line with our forecasts.

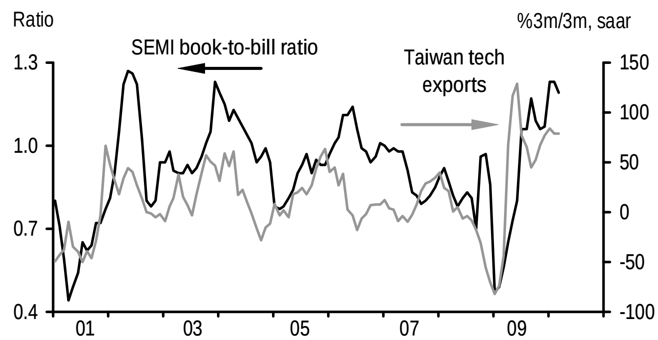
Among the seven major components of the composite index, the series most related to momentum in real economic activity—industry and services average monthly overtime, building permits (measured by floor area), and export orders—continued to register monthly gains in March. Meanwhile, other indicators, largely related to monetary conditions—money supply M1B, the equity price index, and the index of producers' inventory—fell during the month. What is more, the SEMI (Semiconductor Equipment and Materials International) book-to-bill ratio, which tracks global demand for semiconductor manufacturing equipment, edged down modestly in March, but the absolute level remained elevated at 1.19, hovering around its highest point since 2004 (second chart).

Looking ahead, we expect global capital spending to rise at a double-digit pace over the course of 2010—an outcome that could be as strong as any over the past quarter century. Overall, the recovery in business sentiment and earnings currently under way provides a powerful lever for lifting capital spending. These factors should support solid growth in Taiwan's export sector and overall IP in the coming months, though the pace of sequential growth may begin to ease somewhat from the sharp rebound seen in the past 12 months. Our forecast for Taiwan's 2010 real GDP growth stands at 8.2%.

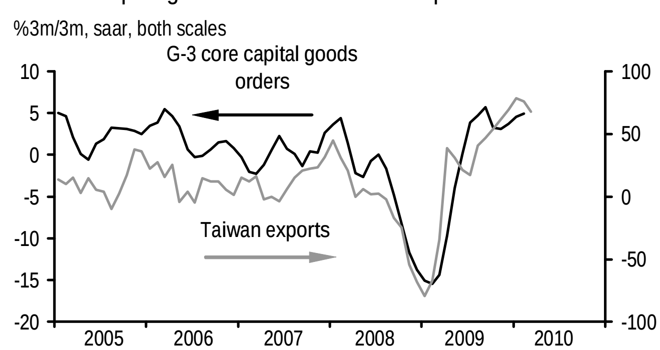
Taiwan: leading indicator and GDP



Taiwan tech exports and SEMI book-to-bill ratio



G-3 core capital goods orders and Taiwan exports



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China:
Data releases and forecasts

Week of May 3 - 7

Sat
May 1
9:00am/
Mon
May 4
10:30am

Manufacturing PMI
Index, sa

	Jan	Feb	Mar	Apr
Overall (Markit)	57.4	55.8	57.0	57.5
Output	60.6	57.8	58.1	__
Overall (NBS)	55.8	52.0	55.1	55.5
Output	60.5	54.3	58.4	__

Manufacturing PMIs likely turned up moderately again in April. The steady upturn in external demand should help support export-related industrial activity in April, while ongoing credit policy to curb excessive lending may have continued to restrain activity in certain domestic sectors.

Review of past week's data

No data released.

Hong Kong:
Data releases and forecasts

Week of May 3 - 7

Mon
May 3
4:30pm

Retail sales volume
% change

	Dec	Jan	Feb	Mar
Oya	11.4	3.2	31.5	29.9
M/m sa	2.3	0.0	9.8	0.4

Retail sales in March are likely to slow from the strong growth experienced during the holiday season, but nevertheless should continue to increase steadily, as the economic recovery gathers momentum and the labor market follows a solid recovery path.

Review of past week's data

Merchandise trade (Apr 27)
HK$ bn

	Jan	Feb	Mar
Balance	-29.5	-19.7	~~-37.1~~ *-38.7*
Exports	222.3	182.5	~~226.0~~ *231.8*
%oya	18.4	28.5	~~28.8~~ *32.1*
Imports	251.8	202.1	~~263.1~~ *270.6*
%oya	39.5	22.4	~~35.9~~ *39.8*

Taiwan:
Data releases and forecasts

Week of May 3 - 7

Wed
May 5
4:00pm

Consumer prices
% change

	Jan	Feb	Mar	Apr
Oya	0.3	2.4	1.3	1.5
M/m sa	0.5	1.2	-0.9	0.2

The March headline CPI likely showed a modest monthly gain, as the Lunar New Year-related seasonal volatility in prices in the previous two months faded.

Fri
May 7
4:00pm

External trade
US$ bn

	Jan	Feb	Mar	Apr
Balance	2.5	0.9	1.5	1.3
Exports	21.7	16.7	23.4	22.4
%oya	75.8	32.6	50.1	50.7
Imports	19.3	15.8	21.9	21.1
%oya	115.4	45.8	80.3	66.2

April's trade report is forecast to show steady gains in exports (at 1.8%m/m sa by our forecast), on the back of steady, broad-based gain in external demand.

Review of past week's data

Composite leading indicator (Apr 27)
% change

	Jan	Feb	Mar
M/m sa	1.9	~~0.6~~ *0.8*	__ 0.3

Korea

- **Real GDP reaccelerated strongly in 1Q10; 2010 growth forecast upgraded**
- **Business sentiment turned less upbeat in April, but still consistent with continued economic expansion**

Real GDP accelerated at a faster rate than we had expected, demonstrating that Korea's economy recorded a solid pace of expansion in 1Q10, after taking a brief breather in the previous quarter. While the upside surprise came at the expense of 2Q, as fiscal spending was front-loaded, it has still prompted us to raise our 2010 full-year GDP forecast to 5.8%y/y from 5.3% previously.

1Q10 real GDP

According to the Bank of Korea's first estimate, real GDP rose 7.5%q/q saar in 1Q10, reaccelerating from a mere 0.7% gain in 4Q09. Manufacturing was the main driver, advancing a solid 15%q/q saar in 1Q, after retreating 6.5% in 4Q09, which itself was a technical payback for the strong gain in the preceding two quarters. Service activity also stayed firm, to rise 6.3% in 1Q, following a 3.7% gain in 4Q09. Agricultural output declined as expected, mainly as a result of unfavorable weather conditions. Expenditure-side details were encouraging, too. To be sure, among domestic final demand, contributions from inventories and government consumption were most notable. However, solid export growth, accompanied by a significantly stronger gain in imports, is further supporting evidence that Korea's recovery is broad-based.

We expect real GDP growth to moderate in 2Q10, but mainly for technical reasons. The inventory cycle should remain supportive, but its contribution is still likely to be less unless restocking broadens to the non-high-tech sector as well in the coming months. Fiscal policy will likely also turn less supportive, after running at a more rapid pace than usual in 1Q. Also, and importantly, the late arrival of spring this year has likely dampened household spending on seasonal products and worked against seasonal labor demand in the construction and agricultural sectors.

Business sentiment down modestly

According to business surveys released this week, growth optimism retreated modestly in recent months. The Federation of Korean Industries (FKI) reported that both the one-month-ahead outlook and current business conditions assessment fell further in April, after seasonal adjustment. The BoK's survey produced similar results. Firms were optimistic about the sales outlook on the back of signs of a global recovery, but still expect a potential loss of competitiveness due to KRW appreciation. Compounded by rising commodity prices, the profitability outlook index fell the most. However, growth continued in the corporate sector, with the composite BSI for investment, inventories, and employment staying nearly flat at levels just above neutral.

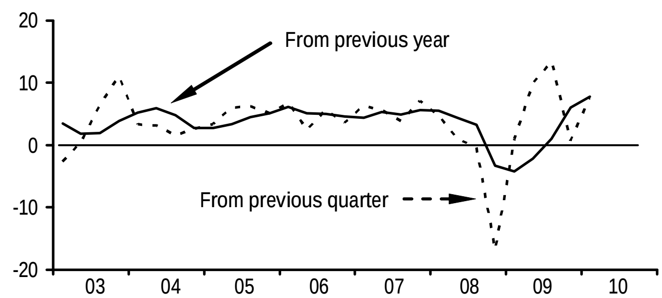
Real GDP

% change at annual rate, BoK 1st estimate for 1Q10

	2008	2009	1Q09	2Q09	3Q09	4Q09	1Q10
%q/q saar							
Real GDP	2.3	0.2	1.0	9.8	13.4	0.7	7.5
Private consumption	1.3	0.2	1.1	14.1	7.1	1.6	2.4
Fixed investment	-1.9	-0.2	1.6	16.7	10.5	6.7	3.5
Construction	-2.8	4.4	25.8	7.2	-2.8	-0.4	3.7
Facilities, equipment	-1.0	-9.1	-35.9	40.9	50.8	22.9	6.3
Intangible assets	2.0	0.5	-9.7	24.0	-4.3	5.4	-23.8
Export of G&S	6.6	-0.8	-12.4	46.5	18.8	-3.9	10.5
Import of G&S	4.4	-8.2	-23.4	40.3	28.7	0.6	18.6
%oya							
Real GDP			-4.3	-2.2	1.0	6.0	7.8
Private consumption			-4.4	-1.0	0.7	5.8	6.2
Fixed investment			-7.4	-2.3	0.4	7.1	10.7
Export of G&S			-10.7	-3.4	1.0	9.8	16.1
Import of G&S			-18.8	-13.3	-7.7	8.7	21.0

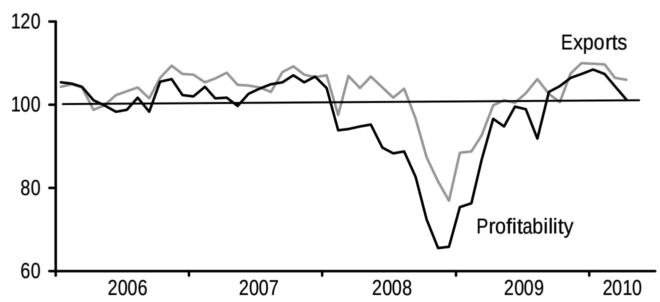
Real GDP

% change, annualized



FKI business survey: 1-month-ahead outlook

100=neutral, sa



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Data releases and forecasts

Week of May 3 - 7

Mon
May 3
10:00am

Customs trade

US$ bn nsa

	Jan	Feb	Mar	Apr
Trade balance	-0.6	2.1	1.8	2.4
Exports	30.8	33.1	37.4	39.9
Imports	31.4	31.0	35.6	37.5

The trade gap is likely to have widened as exports rose more than imports. However, when seasonally adjusted, the increase in imports is anticipated to have been larger than that in exports.

Mon
May 3
8:00am

Consumer prices

% change

	Jan	Feb	Mar	Apr
%oya	3.1	2.7	2.3	2.5
%m/m sa	0.2	0.3	0.0	0.3

Mon
May 3
6:00am

Foreign exchange reserves

US$ bn nsa

	Jan	Feb	Mar	Apr
Total	273.7	270.7	272.3	—

Review of past week's data

FKI business survey (Apr 26)

100 = neutral reading, nsa

	Feb	Mar	Apr	
One-month-ahead outlook	116.2	111.2	~~120.0~~	*113.4*
Current conditions	98.7	113.1	~~112.0~~	*108.9*

Seasonally adjusted, each index fell for the second consecutive month.

Consumer survey (Apr 27)

100 = neutral reading, nsa

	Feb	Mar	Apr	
Index	111	110	~~108~~	*110*

Real GDP 1st estimate (Apr 27)

%q/q saar, unless noted

	3Q09	4Q09	1Q10	
Real GDP	13.4	0.7	~~5.6~~	*7.5*
%oya	1.0	6.0	~~7.4~~	*7.8*

See main story.

Current account (Apr 28)

US$ bn nsa

	Jan	Feb	Mar	
Balance	-0.4	0.2	~~1.2~~	*1.7*

The current account surplus widened in March: a wider merchandise trade surplus offset a wider service deficit.

Industrial production (Apr 30)

% change

	Jan		Feb		Mar	
%oya	~~36.9~~	*37.0*	~~19.1~~	*18.8*	~~21.0~~	*22.1*
%m/m sa	0.0		~~3.6~~	*3.3*	~~0.1~~	*1.6*

The high-tech sector stayed strong, although it grew at a more moderate pace than in February. Excluding the high-tech sector, IP was essentially flat after rising 2.6% in February.

Producer shipments and inventories (Apr 30)

%oya

	Jan		Feb		Mar	
Shipments	~~32.0~~	*32.1*	~~14.3~~	*14.4*	~~16.5~~	*19.1*
Inventories	~~-3.8~~	*-3.6*	~~4.7~~	*4.2*	~~4.0~~	*6.6*

Seasonally adjusted, inventory rose at a moderate rate but was still outpaced by shipments. Thus, the inventory-to-shipments ratio decreased, partially reversing February's increase.

Composite leading indicator (Apr 30)

2005 = 100, sa

	Jan	Feb	Mar	
Index	127.4	127.1	~~127.3~~	*127.2*

Service activity (Apr 30)

% change

	Jan		Feb		Mar	
%oya	~~4.3~~	*4.4*	~~7.1~~	7.3	~~7.3~~	5.2

Service activity fell 0.2%m/m sa, after rising 3.1% in February. Real estate services and leisure industry were down most.

Consumption goods sales (Apr 30)

% change

	Jan		Feb		Mar	
%oya	~~6.8~~	*6.9*	~~12.9~~	*13.1*	~~9.0~~	*9.7*

Consumption goods sales fell 1.3%m/m sa in March, not fully reversing the previous month's gain. Auto sales fell for three straight months, a payback for tax-incentive-driven gains in 2H09. Excluding auto sales, consumption good sales declined only modestly by 0.5%m/m sa, after rising 3.4% in February.

BoK Watch

- **1Q GDP outcome poses upside risk to the BoK's 2010 growth forecast**

The Bank of Korea revised up its 2010 GDP forecast two weeks ago, to 5.2%y/y from 4.6%y/y, but this week's release of 1Q GDP data already poses some upside risks to this forecast. Indeed, the BoK expects real GDP to rise 6.6%oya in 1H10, which is very achievable unless GDP declines in 2Q from 1Q. Accordingly, we expect the BoK to upgrade its growth outlook further at May's MPC meeting, rebalancing its list of concerns.

ASEAN: Indonesia, Malaysia, Philippines, Singapore, Thailand, Vietnam

- **Recent Thai political uncertainty will likely affect demand—sentiment indicators already turning down**
- **High-frequency data through March remain upbeat—though some softening might be expected into 2Q10**
- **BoT normalization postponed indefinitely until the political noise calms**

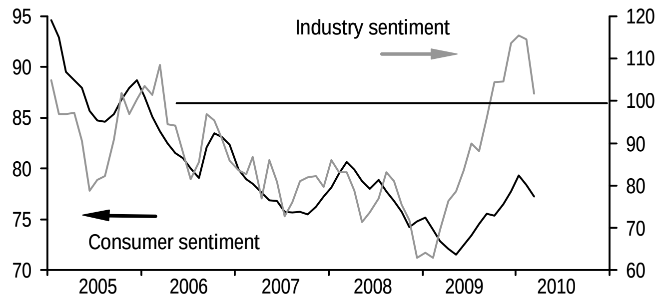
Recent focus in Thailand has shifted well away from the data flow, which had been strong into 1Q10, and on to political developments. The activity data have yet to fully capture the reverberations from the latest bout of violence in April, although the sentiment data had already turned lower after the opposition rally in March and likely fell further in April. So far, the violence has been limited to Bangkok, and while disruptions have been severe in the business district, they have not spread much beyond the city. Thus, while confidence will likely be further affected as unrest continues to dominate the headlines, any actual disruption to economic activity should be smaller. Whether this forecast materializes will likely be reflected in the upcoming April data rather than in the March data released this past week (see the research note "Thailand: tracking the impact of politics on the economy" in this *GDW*).

The March data prints continue to be solid; both external and domestic demand remain strong. However, with the impact of the evolving political uncertainty still unclear, the central bank kept rates on hold on April 21, and the risk, if the uncertainty persists, is that the BoT remains on hold even through the June 5 policy meeting. With policy rates already at historical lows and inflation heading higher, real rates will likely move further into negative territory. That said, continued political uncertainty, with its impact on sentiment, will likely mitigate the potential impact of negative real rates, which would otherwise risk dissaving and encourage risk-seeking.

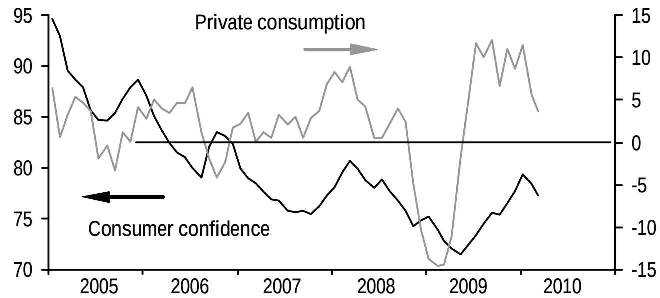
Sentiment takes a dip—watching the data

The recent sentiment indicators from Thailand turned down in March, likely in response to the mass protests in Bangkok. However, political uncertainty took a turn for the worse in April following violent confrontations. This suggests that sentiment likely took another dip in April following the March decline. Thailand currently produces two sets of sentiment data—consumer sentiment and industry sentiment, each based on a balanced score of 100. Consumer sentiment dipped to 77.3 in March from 78.4 in February, while industry sentiment fell to 101.6 in March from 114.5 in the previous month (first chart).

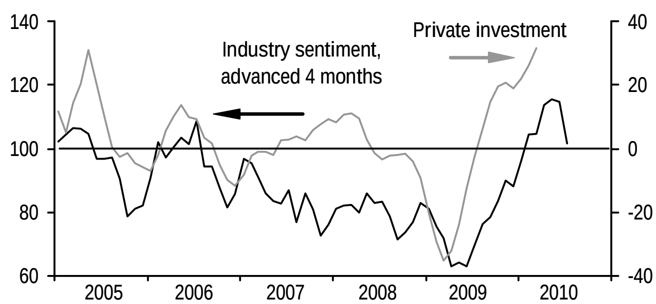
Thailand: consumer and industry sentiment
Balanced score, neutral =100, nsa, both scales



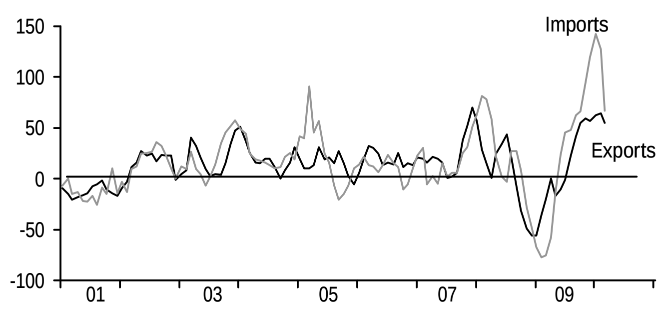
Thailand: consumer confidence and private consumption
Balanced score, neutral =100, nsa
%3m/3m, saar



Thailand: industry sentiment and private investment
Balanced score, neutral =100, nsa
%3m/3m, saar



Thailand: merchandise trade
%3m/3m saar, US$ terms



The correlation between sentiment data and actual activity is mixed. In 2007, private consumption actually accelerated even as consumer sentiment dipped, while in 2H09, the recovery in sentiment lagged the consumption recovery (second chart, previous page). Similarly, prior to 2007, industry sentiment had tracked the inflection points in the investment cycle well, but the correlation has weakened since then (third chart, previous page). Part of the divergence in 2007 stems from the construction of the sentiment index, which is heavily weighted toward industries catering for domestic demand. By contrast, the pickup in investment in 2007 was predominantly driven by export-related industries.

The upshot is that while the sentiment indicators are useful, they may not capture the full breadth of activity. While there will likely be a hit to domestic activity from the unrest, the recent strength in external demand provides some offset.

Recent data have been strong

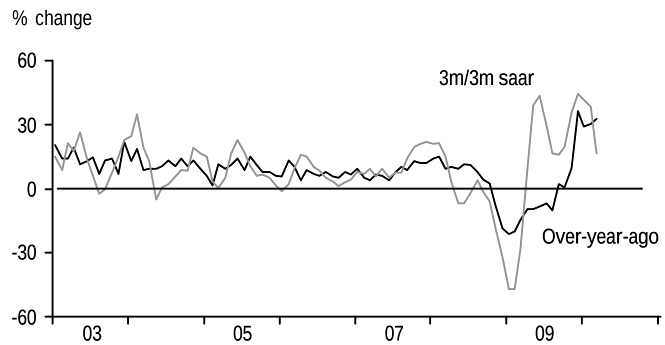
The strong data releases going into 1Q10 have been boosted by external demand in particular. Exports were up a robust 54.5%3m/3m saar in March, demonstrating the continued strength of high-tech products (fourth chart previous page). Imports were up 67.4%3m/3m saar, reflecting an increase in imports of raw materials, which bodes well for investment. Production was up 16.4%3m/3m saar and up 0.7%m/m sa following a 3.3%m/m sa increase in February. A large part of the production upturn reflects the contribution from high-tech products and also from rising agricultural output.

Tourist arrivals, which tend to be sensitive to domestic factors, as was the experience in 2006, roared into 1Q10 with solid momentum (second chart). While arrivals are likely to slow, we are entering the low season (April through June), and thus any slowing should not exact too much of a toll on the tourism industry, which accounts for around 7% of GDP. This of course assumes that the uncertainty is relatively short-lived.

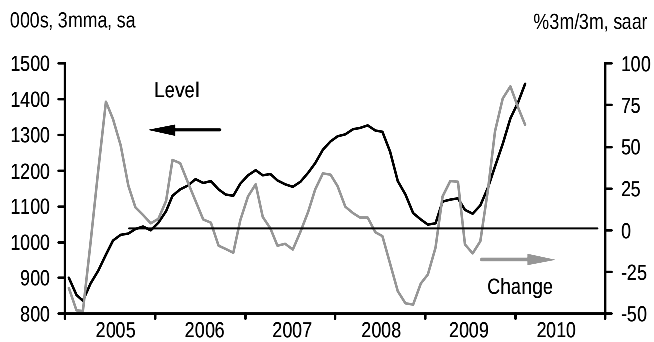
Watching the BoT and deposit behavior

This uncertainty kept the central bank from hiking rates on April 21, and the risk is that further uncertainty may prevent the BoT from hiking rates on June 2 as well. If that happens, the risk is that real rates turn more negative, potentially leading to dissaving among domestic depositors (third chart). A striking observation in the case of Thailand is that in the past few years, interest-bearing deposits have correlated well with real interest rates (fourth chart). However, weak sentiment could keep precautionary savings high. In the event that it does not, the Bank of Thailand could normalize rates even in the face of domestic uncertainty. What this suggests is that the behavior of the domestic deposit base should also be a factor in the central bank's reaction function.

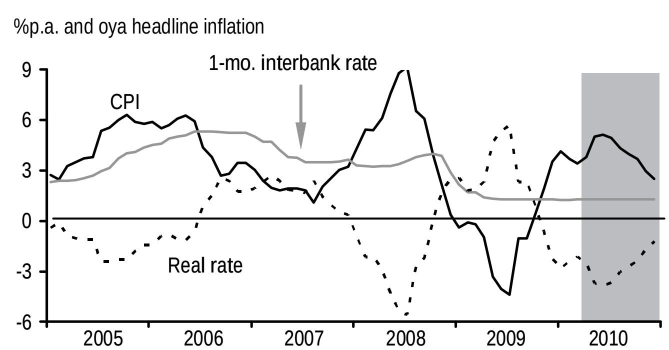
Thailand: manufacturing production



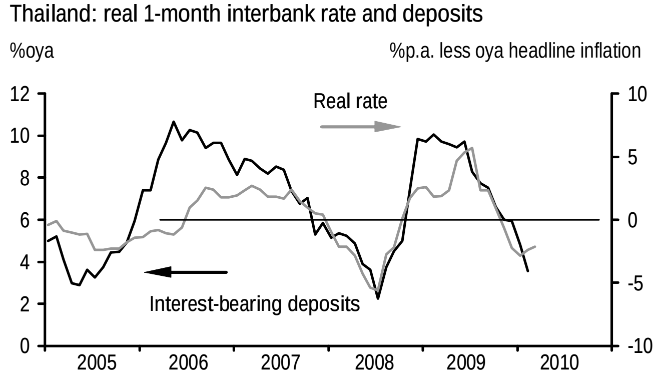
Thailand: tourist arrivals



Thailand: real interest rates



Thailand: real 1-month interbank rate and deposits



Indonesia:

Data releases and forecasts

Week of May 3 - 7

Mon
May 3
2:00pm

Merchandise trade
US$ bn nsa

	Dec	Jan	Feb	Mar
Trade balance	3.0	2.1	1.7	2.4
Exports (%oya)	50.0	59.3	57.1	52.8

The March trade surplus likely rose again—reflecting the strength of commodity exports.

Mon
May 3
2:00pm

Consumer prices
% change

	Jan	Feb	Mar	Apr
Oya	3.7	3.8	3.4	3.5
M/m sa	0.4	0.4	0.2	0.2
Food	4.9	4.8	4.1	—
Nonfood	3.4	3.5	3.2	—

Inflation in April is expected to be benign, reflecting the continuing impact of moderating food prices.

Wed
May 5
1:00pm

BI monetary policy meeting
% p.a.

	Feb	Mar	Apr	May
BI rate	6.50	6.50	6.50	6.50

With inflation expected to be modest through 1H10, there is little need for Bank Indonesia to hike rates.

Review of past week's data

No data released.

Malaysia:

Data releases and forecasts

Week of May 3 - 7

Tue
May 4
6:00pm

Merchandise trade
US$ bn nsa

	Dec	Jan	Feb	Mar
Trade balance	3.5	3.8	3.4	3.9
Exports	16.0	15.5	13.7	17.0
%oya	23.0	44.8	26.1	43.2
Imports	12.4	11.7	10.3	13.0
%oya	27.8	38.5	36.2	54.5

We expect March exports to have come in solidly, thereby helping to boost the overall trade surplus.

Review of past week's data

No data released.

Philippines:

Data releases and forecasts

Week of May 3 - 7

Wed
May 5
9:00am

Consumer prices
%oya

	Jan	Feb	Mar	Apr
All items	4.3	4.2	4.4	4.7
%m/m sa	0.0	0.9	0.3	0.4

Review of past week's data

Government budget (Apr 27)
Bn pesos

	Jan	Feb	Mar
Balance	-37.1	-33.2	*-63.9*
Revenue	92.3	76.7	*96.9*
Expenditure	129.4	109.9	160.7

The deficit in March was twice as large as that in February. The larger monthly deficit was due to a notable rise in non-interest spending, which left the primary balance much wider than in previous months.

The 1Q deficit was worse than the government's target of PHP110.9 billion. Nevertheless, we expect improvement ahead as spending is set to fall due to election-related restrictions on government expenditure and higher revenues from stronger GDP growth and privatization receipts. This should enable the government to meet its year-end target of around PHP295 billion, or about 3.5% of GDP.

Merchandise trade (Apr 27)
US$ bn nsa

	Dec	Jan	Feb
Imports	3.9	3.8	~~3.8~~ *3.9*
%oya	17.9	30.3	~~23.0~~ *27.6*

Imports were flat on the month as weakness in nonelectronics offset a strong gain in electronics imports. Despite the flat monthly gain, %oya import growth remained strong.

Singapore:

Data releases and forecast

Week of May 3 - 7

Tue
May 4
9:30pm

Purchasing managers index
Level

	Jan	Feb	Mar	Apr
PMI	51.4	51.9	51.1	52.0
PMI—electronics	53.8	53.0	53.4	53.5

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Review of past week’s data

Industrial production (Apr 26)

% change

	Jan	Feb	Mar
Oya	39.2	~~19.1~~ *17.9*	~~38.9~~ *43.0*
M/m sa	11.0	~~5.9~~ *5.2*	~~-4.0~~ *-1.5*

IP rose much more strongly than expected at 43.0%oya (consensus: 30.3%). The monthly decline followed an average gain of 10%m/m sa in each of the three preceding months, suggesting that production remains strong despite the modest payback. Sequential trend growth rose 124%3m/3m saar, marking the strongest rate on record since at least the early 1980s.

IP growth should come back to earth, and we should see moderation in the coming months, which could even lead to contraction in manufacturing output given the traditional volatility in Singapore’s industrial data. Nevertheless, production should be strong over the medium term as global demand is forecast to be firm.

Unemployment (Apr 30)

% rate

	3Q09	4Q09	1Q10
Unemployment rate, sa	~~3.4~~ *3.3*	~~2.1~~ *2.3*	~~2.3~~ *2.2*

Singapore saw an employment gain of 34,000 in 1Q10, down slightly from 37,500 in 4Q09. Excluding construction, 1Q10 employment rose 34,800, up from 32,900 in 4Q09. The 1Q10 nonconstruction employment run rate is comparable to the levels seen in 1H06, but still shy of the peak levels seen in 2007, which averaged 49,500 per quarter. The renewed vigor in labor demand, starting in 4Q09, has effectively continued into 1Q10 and, with a strong link between employment/growth and inflation, the recent data flow together with the strong outlook for the economy suggests that inflationary pressures are building.

Thailand:

Data releases and forecasts

Week of May 3 - 7

Mon
May 3
4:00pm

Consumer prices

% change

	Jan	Feb	Mar	Apr
Oya	4.1	3.7	3.4	3.8
M/m sa	0.6	0.7	-0.6	0.2

Although pump prices for energy are up slightly in April, the impact of declining food prices likely kept inflation in check.

Review of past week’s data

Merchandise trade (Apr 30)

US$ bn nsa

	Jan	Feb	Mar
Trade balance	0.6	0.5	~~1.4~~ *1.1*
Exports, %oya	31.3	23.1	~~40.9~~ *40.8*
Imports, %oya	50.0	80.8	~~58.5~~ *62.0*

See main story.

Manufacturing production (Apr 30)

% change

	Jan	Feb	Mar
Oya	29.0	30.3	~~27.7~~ *32.6*
M/m sa	-5.2	3.3	0.7

See main story.

Private consumption index (Apr 30)

% change

	Jan	Feb	Mar
Oya	4.8	9.7	~~6.9~~ *7.4*
M/m sa	-0.5	0.3	~~0.0~~ *0.5*

Private consumption rose 3.7%3m/3m saar, with the wealth effect from higher agricultural prices likely offset by the turn in consumer sentiment, reflected to an extent in the 18%m/m sa decline in car sales in March.

Private investment index (Apr 30)

% change

	Jan	Feb	Mar
Oya	5.9	~~11.4~~ *12.1*	~~14.6~~ *18.2*
M/m sa	2.3	~~1.6~~ *2.2*	~~0.5~~ *3.1*

Private investment experienced a very strong increase, up 31.5%3m/3m saar on account of rising capital goods demand related to the export sector, especially the high-tech sector.

Vietnam:

Data releases and forecasts

Week of May 3 - 7

No data releases.

Review of past week’s data

Merchandise trade

US$ bn nsa

	Feb	Mar	Apr
Trade balance	-1.3	~~-1.4~~ *-1.2*	~~-1.6~~ *-1.3*
Exports, %oya	-25.6	~~-3.0~~ *5.2*	~~26.3~~ *33.2*
Imports, %oya	21.1	~~28.9~~ *33.8*	~~28.7~~ *27.4*

Exports edged up 0.9%m/m sa, leaving them up 33.2%oya. Imports fell 4.1%m/m sa, leaving them up 27.4%oya. In an abrupt shift, export growth has picked up, rising 17.9%3m/3m saar in April, while imports declined 22.8% in April, marking the third consecutive month of decline. Vietnam’s April trade deficit widened to US$1.25 billion from a revised US$1.16 billion in March. The modest widening reflected slightly stronger import growth relative to exports (nsa). The cumulative trade deficit for 2010 now stands at US$4.65 billion, which is notably worse than the US$0.372 billion surplus recorded at the same time in 2009. With the exception of 2008, the deficit is now the widest it has ever been at this point in the year.

Asia focus: little slack left in manufacturing

After sliding throughout 2008 and in early 2009, manufacturing capacity utilization rates in EM Asia have rebounded sharply. Our measure of EM Asia's average utilization rate (which includes Korea, the Philippines, and Thailand—the only nations which supply monthly data) peaked in January 2008 and then tumbled nearly 17% to a record low in January 2009. Over the past year, however, the regional utilization rate rose about 18%, leaving it almost 1.5% below its all-time peak in February 2008. This contrasts sharply with most of the developed world, including Japan, whose rate remains about 15% below its peak.

Though utilization rates have rebounded, some countries have recovered more than others. Korea and the Philippines currently stand at or near record high levels while Malaysia and Thailand are much further from closing their gaps. Malaysia's quarterly capacity utilization data show that the lag in recovery reflects domestic considerations, as capacity usage for domestic-oriented activity is much weaker than for foreign demand. Thailand does not provide such distinction in the data, but the political situation, and clearer industrial production data, suggest a similar dynamic.

Asia: capacity utilization in manufacturing

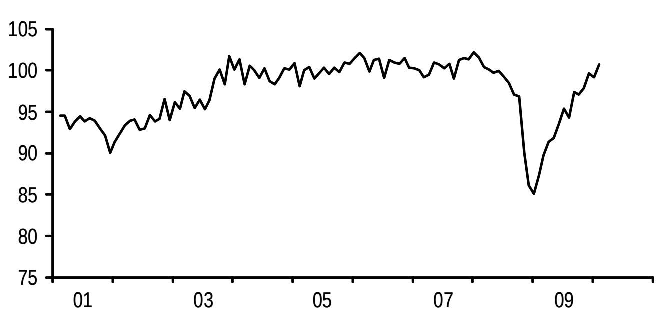
Index, 2005=100 sa, annual and quarterly data period average

	2007	2008	2009	3Q09	4Q09	Jan	Feb
EM Asia avg	100.4	97.7	93.4	95.7	98.2	99.2	100.7
Korea	100.4	96.9	93.0	98.8	98.3	98.9	100.9
Thailand	100.6	94.0	85.4	86.1	93.0	94.6	97.9
Malaysia[1]	75.5	74.7	69.0	71.5	75.1	na	na
Philippines	100.2	102.1	101.8	102.2	103.4	104.1	na
Japan[2]	103.7	99.3	74.0	77.0	81.8	90.1	90.1

1. Data are quarterly and capacity utilization is in % terms.
2. Index 2000=100

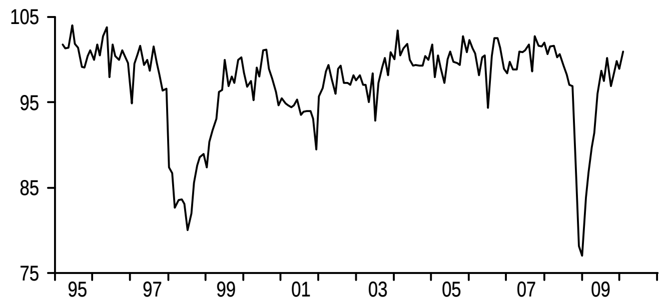
EM Asia: manufacturing capacity rate

2005=100, sa



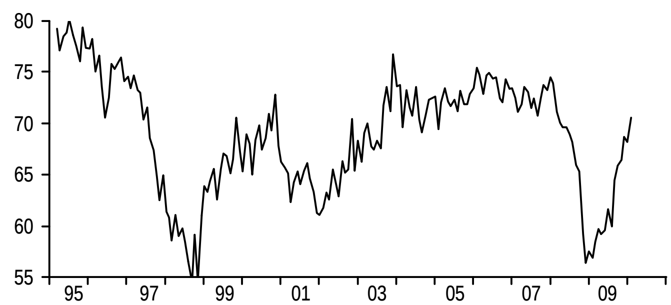
Korea: manufacturing operating ratio

2005=100, sa



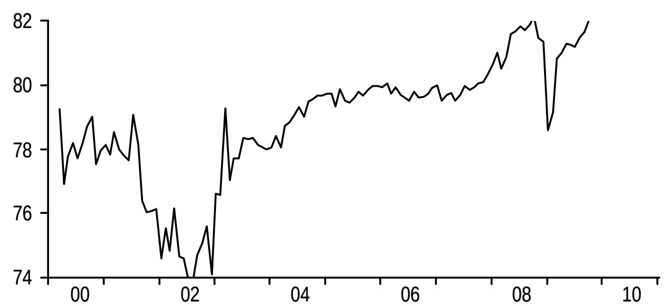
Thailand: manufacturing capacity utilization rate

2005=100, sa



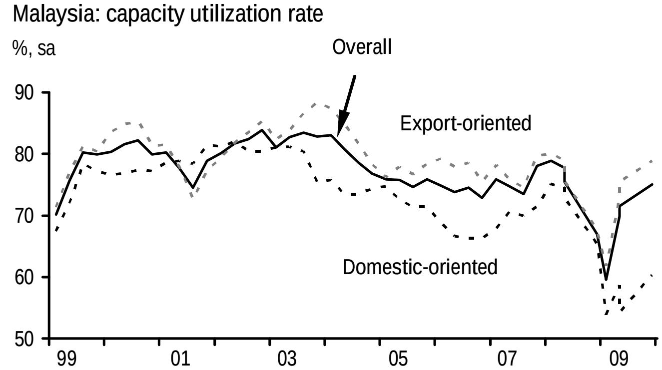
Philippines: manufacturing capacity utilization rate

2005=100, sa



Malaysia: capacity utilization rate

%, sa



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US economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
3 May Personal income (8:30am) Mar 0.5% Real consumption 0.4% Core PCE deflator 0.1% (1.3%oya) ISM manufacturing (10:00am) Apr 61.0 Construction spending (10:00am) Mar -0.7% Light vehicle sales Apr 11.9 mn	4 May Pending home sales (10:00am) Mar 3.0% Factory orders (10:00am) Mar 0.2%	5 May ADP employment (8:15am) Apr ISM nonmanufacturing (10:00am) Apr 57.0 Announce 3-year note $38 bn Announce 10-year note $25 bn Announce 30-year bond $16 bn Boston Fed President Rosengren speaks in Boston (8:30am) and New York (7:00pm) Richmond Fed President Lacker speaks in Richmond (10:10am)	6 May Initial claims (8:30am) w/e prior Sat 440,000 Productivity and costs (8:30am) 1Q preliminary 3.1% (6.4%oya) Unit labor costs -1.4% (-3.8%oya) Chain store sales Apr Chicago Fed President Evans (9:20am, 3:00pm) and Fed Chairman Bernanke (9:30am) speak to Chicago Banking Conf. St Louis Fed President Bullard speaks in St.Louis (9:10am)	7 May Employment (8:30am) Apr 145,000 Unemployment rate 9.7% Average hourly earnings 0.1% Average weekly hours 34.1 Consumer credit (3:00pm) Mar Philadelphia Fed President Plosser speaks in Delaware (12:30pm)
10 May Minneapolis Fed President Kocherlakota speaks in Minneapolis (1:00pm).	11 May NFIB survey (7:30am) Apr Wholesale trade (10:00am) Mar JOLTS (10:00am) Mar Auction 3-year note $38 bn Atlanta Financial Markets Conference with comments by Atlanta Fed President Lockhart (1:15pm) and Philadelphia Fed President Plosser (1:30pm)	12 May International trade (8:30am) Mar Federal budget (2:00pm) Apr Auction 10-year note $25 bn Atlanta Financial Markets Conference with comments by Boston Fed President Rosengren(10:15am) and Atlanta Fed President Lockhart (12:30pm)	13 May Initial claims (8:30am) w/e prior Sat Import prices (8:30am) Apr Auction 30-year bond $16 bn Fed Vice-Chairman Kohn speaks in Ottawa (9:00am). Minneapolis Fed President Kocherlakota speaks in Wisconsin (1:00pm).	14 May Retail sales (8:30am) Apr Industrial production (9:15am) Apr Consumer sentiment (9:55am) May preliminary Business inventories (10:00am) Mar
17 May Empire State survey (8:30am) May TIC data (9:00am) Mar NAHB survey (1:00pm) May	18 May PPI (8:30am) Apr Housing starts (8:30am) Apr	19 May CPI (8:30am) Apr FOMC minutes (economic projections)	20 May Initial claims (8:30am) w/e prior Sat Philly Fed survey (10:00am) May Leading indicators (10:00am) Apr Announce 2-year note $42 bn Announce 5-year note $40 bn Announce 7-year note $31 bn	21 May
24 May Existing home sales (10:00am) Apr	25 May S&P/Case-Shiller HPI (9:00am) Mar, 1Q Consumer confidence (10:00am) May FHFA HPI (10:00am) Mar, 1Q Richmond Fed survey (10:00am) May Auction 2-year note $42 bn Fed Chairman Bernanke (8:30pm) and Philadelphia Fed President Plosser (10:00pm) speak at Bank of Japan Conference	26 May Durable goods (8:30am) Apr New home sales (10:00am) Apr Auction 5-year note $40 bn Chicago Fed President Evans speaks at Bank of Japan Conference (8:00pm)	27 May Initial claims (8:30am) w/e prior Sat Real GDP (8:30am) 1Q second KC Fed survey (10:00am) May Auction 7-year note $31 bn	28 May Personal income (8:30am) Apr Chicago PMI (9:45am) May Consumer sentiment (9:55am) May final

Euro area economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
3 May Euro area: PMI Mfg final (10:00am) Apr 57.5 Index, sa Germany: PMI Mfg final (9:55am) Apr 61.3 Index, sa France: PMI Mfg final (9:50am) Apr 56.7 Index, sa Italy: PMI Mfg (9:45am) Apr 54.5 Index, sa Spain: PMI Mfg (9:15am) Apr 52.5 Index, sa	4 May Euro area: PPI (11:00am) Mar 0.8 %oya Germany: Retail sales (8:00am) Mar 0.2 % m/m, sa	5 May Euro area: PMI services final (10:00am) Apr 55.5 Index, sa PMI composite final (10:00am) Apr 57.3 Index, sa Retail sales (11:00am) Mar 0.5 %m/m,sa Germany: PMI services final (9:55am) Apr 55.0 Index, sa PMI composite final (9:55am) Apr 59.1 Index, sa France: PMI services final (9:50am) Apr 57.8 Index, sa PMI composite final (9:50am) Apr 58.4 Index, sa Italy: PMI services (9:45am) Apr 55.5 Index, sa PMI composite (9:45am) Apr 56.0 Index, sa Spain: PMI services (9:15am) Apr 52.5 Index, sa PMI composite (9:15am) Apr 53.5 Index, sa ECB member Gertrude Tumpel-Gugerell speaks in Madrid , Spain (12:20pm)	6 May Euro area: ECB rate announcement (1:45pm) No change expected ECB press conf. (2:30pm) Germany: Mfg orders (12:00am) Mar 2.5 %m/m,sa External Governing Council Meeting of the ECB in Lisbon, Portugal (9:00am)	7 May Germany: Industrial production (12:00pm) Mar 2.0 %m/m,sa France: Foreign trade (8:45am) Mar Monthly budget situation (8:45am) Mar ECB President Jean-Claude Trichet speaks in Lisbon, Portugal (11:30am CET)
10 May Germany: Foreign trade (8:00am) Mar France: Industrial production (8:45am) Mar Italy: Industrial production (10:00am) Mar	11 May Germany: CPI final (8:00am) Apr Netherlands: CPI (9:30am) Apr	12 May Euro area: GDP flash (11:00am) 1Q Industrial production (11:00am) Mar Germany: GDP flash (8:00am) 1Q France: GDP prelim (8:45am) 1Q CPI (8:45am) Apr Italy: GDP flash (10:00am) 1Q Spain: GDP flash (9:00am) 1Q Netherlands: GDP prelim (9:30am) 1Q	13 May Euro area: ECB monthly bulletin (10:00am) May	14 May Italy: CPI final (10:00am) Apr Spain: CPI final (9:00am) Apr
17 May Netherlands: Industrial production (9:30am) Mar	18 May Euro area: HICP final (11:00am) Apr Foreign trade (11:00am) Mar Germany: ZEW bus. Survey (11:00am) May France: Employment prelim (8:45am) 1Q Italy: Foreign trade (10:00am) Mar	19 May Spain: GDP final (9:00am) 1Q	20 May Euro area: EC cons. Conf. Prelim (4:00pm) May Germany: PPI (8:00am) Apr Italy: Industrial orders (10:00am) Mar Belgium: BNB cons. Conf. (3:00pm) May	21 May Euro area: BoP (10:00am) Mar PMI flash (10:00am) May Mfg, services, composite Germany: GDP final (8:00am) 1Q PMI flash (9:30am) May Mfg, services, composite IFO bus. survey (10:00am) Mar France: PMI flash(9:00am) Apr Mfg, services, composite Netherlands: CBS cons. conf. (9:30am) May
24 May Germany: Import prices (8:00am) Apr	25 May Euro area: Industrial new orders (11:00am) Mar Italy: ISAE cons. conf. (9:30am) May Netherlands: CBS bus. conf. (9:30am) May	26 May Germany: GfK cons. conf. (8:00am) Jun France: INSEE bus. conf. (8:45am) May Consumption of mfg goods (8:45am) Apr Belgium: BNB bus. conf. (3:00pm) May	27 May Germany: CPI 6 states and prelim (8:00am) May France: INSEE cons. conf. (8:45am) May Italy: ISAE bus. conf. (9:30am) May Contractual wages (10:00am)Apr	28 May Spain: HICP flash (9:00am) May Belgium: CPI (11:15am) May

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

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Japan economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
3 May *Holiday:Japan*	4 May *Holiday:Japan*	5 May *Holiday:Japan*	6 May PMI services/ composite (8:15 am) Apr Auto registrations (2:00 pm) Apr <u>35.0%oya</u>	7 May Monetary base (8:50 am) Apr Auction 3-month bill
10 May Minutes of Apr 6-7 BoJ MPM (8:50 am)	11 May Auction 6-month bill Auction 10-year bond	12 May Coincident CI (2:00 pm) Mar Auction 3-month bill	13 May M2 (8:50 am) Apr Current account (8:50 a m) Mar Economy watcher survey (2:00 pm) Apr Auction 40-year bond	14 May
During the week: Cabinet Office private consumption index Mar				
17 May Corporate goods prices (8:50 am) Apr Private machinery orders (8:50 am) Mar Construction spending (2:00 pm) Mar Auction 1-year bill	18 May Reuters Tankan (8:30 am) May Tertiary sector activity index (8:50 am) Mar Consumer sentiment (2:00 pm) Apr Auction 5-year note	19 May IP final (1:30 pm) Mar Auction 3-month bill	20 May GDP 1st est. (08:50am) 1Q BoJ Monetary Policy Meeting Auction 2-month bill Auction 20-year bond	21 May BoJ Monetary Policy Meeting and statement BoJ governor Shirakawa's press conference (3:30 pm)
During the week: Nationwide department store sales Apr				
24 May All sector activity index (1:30 pm) Mar BoJ monthly economic report (2:00 pm)	25 May	26 May Corporate service prices (8:50 am) Apr Shoko Chukin small business sentiment (2:00 pm) May Minutes of Apr 30 BoJ MPM (8:50 am) BoJ governor Shirakawa's opening address at the 2010 international conference held by BoJ Institute for Monetary and Economic Studies of BoJ (9:30am) Auction 3-month bill	27 May Trade balance (8:50 am) Apr Auction 2-year note	28 May Nationwide core CPI (8:30 am) Apr All household spending (8:30 am) Apr Unemployment rate (8:30 am) Apr Job offers to applicants ratio (8:30 am) Apr Total retail sales (8:50 am) Apr

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Canada economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
3 May	4 May	5 May Building permits (8:30am) Mar 1.9% Ivey PMI (10:00am) Apr 52.8 JPM sentiment index (sa) 53.6	6 May BoC deputy Governor Murray speaks in Edmonton (8:05pm)	7 May Employment (7:00am) Apr 20 (0.1%) Unemployment rate 8.1%
10 May Housing starts (8:15am) Apr	11 May	12 May International trade (8:30am) Mar New house price index (8:30am) Mar	13 May	14 May Manufacturing sales (8:30am) Mar New vehicle sales (8:30am) Mar Existing home sales Apr
17 May	18 May	19 May Wholesale sales (8:30am) Mar	20 May Leading indicators (8:30am) Apr	21 May CPI (7:00am) Apr Retail sales (8:30am) Mar
24 May Victoria Day Markets closed	25 May	26 May Payroll employment (8:30am) Mar	27 May	28 May Current account (8:30am) 1Q

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

Latin America economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
3 May Brazil: PMI manufacturing Apr Trade balance Apr US$1.174bn FGV CPI IPC-S May 2 0.72%m/m, nsa Mexico: IMEF survey Apr Manufacturing 54.5 Nonmanufacturing 55.0 Banxico survey Apr	4 May Brazil Fipe CPI Apr 30 0.47%m/m, nsa IP Mar 19.7%oya, nsa Colombia: PPI Apr Mexico: Central bank reserves Consumer confidence Apr 82.1	5 May Brazil: Capacity utilization Mar Chile: Economic activity Mar Colombia: CPI Apr 0.30%m/m, nsa	6 May Brazil: COPOM minutes Auto report (Anfavea) Apr Ecuador: CPI Apr Peru: BCRP meeting May no change	7 May Brazil: IPCA Apr 0.60%m/m, nsa Chile: CPI Apr Trade balance Apr Mexico: CPI Apr -0.20%m/m Core CPI Apr 0.14%m/m
During the week: Argentina: Government tax revenue Apr Auto sales Apr Peru (May 1): CPI Apr 0.11%m/m, nsa WPI Apr				
10 May Brazil: IGP-M 1st rel May Mexico: Formal employment report Mar Peru: Trade balance Mar	11 May Brazil: Fipe CPI May 07 Mexico: Central bank reserves Auto report Apr	12 May Argentina: CPI Apr WPI Apr Brazil: Retail sales Mar Mexico: Wage negotiations Apr Fixed investment Feb IP Mar	13 May Chile: BCCh meeting Colombia: Trade balance Mar	14 May Colombia: BanRep minutes
During the week: Venezuela: CPI Apr				
17 May Argentina: Consumer confidence May Brazil: FGV CPI IPC-S May16 Peru: GDP Mar Unemployment Apr *Holiday: Venezuela*	18 May Brazil: Fipe CPI May15 Chile: GDP 1Q Current account 1Q Mexico: Central bank reserves	19 May Brazil: IGP-M 2nd rel May Colombia: IP Mar Retail sales Mar	20 May Brazil: IPCA 15 May Mexico: IGAE Mar Real GDP 1Q	21 May Argentina: Trade balance Apr IP Apr Economic activity Mar Mexico: Retail sales Mar Banxico meeting *Holiday: Chile*
During the week: Argentina: Budget balance Apr Brazil: CAGED Formal Job Creation Apr Venezuela: GDP 1Q				
24 May Brazil: FGV CPI IPC-S May 23 Mexico: CPI May 1H Core May 1H Trade balance Apr *Holiday: Ecuador*	25 May Brazil: Fipe CPI May 23 Current account Apr FDI Apr Mexico: Central bank reserves CAB 1Q10 Unemployment rate Apr Nominal GDP 1Q10 *Holiday: Argentina*	26 May	27 May Brazil: Unemployment rate Apr Primary budget balance Apr Net Debt % GDP Apr Colombia: BanRep meeting May	28 May Brazil: IGP-M May Chile: IP Apr Peru: GDP 1Q Mexico: Public sector balance Apr

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UK/Scandinavia/Switzerland economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
3 May Sweden: PMI (08:30am) Apr Minutes of Riksbank's April monetary policy meeting (09:30am) Norway: PMI Mfg (09:00am) Apr NEF HPI (11:00am) Apr Switzerland: PMI (09:30am) Apr	4 May United Kingdom: PMI mfg (09:30am) Apr 57.7%bal, sa Net secured lending to individuals (09:30am) Mar 1.5 ch,m/m £ bn Mortgage approvals 48.5 K,,sa M4 & M4 lending final (09:30am) Mar 3.5 %oya Sweden: Riksbank's Deputy Governor Lars E.O. Svensson speaks (08:30am)	5 May United Kingdom: Nationwide cons. Conf. (12:01am) Apr 72 Index, sa PMI construction (09:30am) Apr Norway: AKU unemployment (10:00am) Feb Norges bank rate announcement (02:00pm) 25bp hike expected	6 May United Kingdom: Markit jobs report (12:01am) Apr PMI services (09:30am) Apr 57.5 %bal, sa General Elections 2010 Switzerland: CPI 09:15am) Apr	7 May United Kingdom: New cars regs. (09:00am) Apr PPI (09:30am) Apr Input prices 1.0%m/m, nsa Output prices 0.3 %m/m, nsa Sweden: Industrial production and orders (09:30am) Mar Norway: IP Mfg (10:00am) Mar Government Pension Fund Global Quarterly Report (10:00am) Q1 Switzerland: Unemployment (07:45am) Apr
During the week : United Kingdom: Halifax HPI (08:00am) Apr 0.5 %m/m, sa				
10 May United Kingdom: MPC rate announcement and Asset purchase target (12:00pm) No change expected Norway: CPI (10:00am) Apr PPI (09:30am) Apr	11 May United Kingdom: BRC retail sales (12:01am) Apr RICS HPI (12:01am) Apr Industrial production (09:30am)Mar Sweden: CPI (09:30am) Apr Capacity utilization (09:30am) 1Q AMV unemployment (10:00am) Apr Norway: Financial Stability 2010:01 (02:00pm) Switzerland: Consumer climate (07:45am) 1Q	12 May United Kingdom: Labor mkt report (09:30am) Mar Quoted mortgage int. rates (09:30am) Apr BoE quarterly inflation report (10:30am) Switzerland: Producer & import prices (09:15am) Apr	13 May United Kingdom: Trade balance (09:30am) Mar DCLG HPI (090:30am) Mar	14 May
17 May United Kingdom: Rightmove HPI (12:01am) May Switzerland: SNB's Philipp Hildebrand speaks (06:00pm)	18 May United Kingdom: CPI (09:30am) Apr CBI industrial trends (11:00am)May Norway: Trade balance (10:00am) Apr Norges bank's Governor Svein Gjedrem. Hearing before the Standing Committee on Finance and Economic Affairs of the Storting (11:00am)	19 May United Kingdom: MPC minutes (09:30am) May	20 May United Kingdom: Retail sales (09:30am) Apr Norway: GDP (10:00am) 1Q Switzerland: SNB's Thomas Jordon speaks (04:00pm)	21 May United Kingdom: Business investment prelim (09:30am) 1Q Public sector finance (09:30am)Apr Provisonal estimates of M4 & M4 lending (09:30am) Apr Switzerland: Monthly statistical bulletin (09:00am)
24 May United Kingdom: Business investment prelim (09:30am) 1Q	25 May United Kingdom: GDP Prelim (2nd release) (09:30am) 1Q Index of services (09:30am) Mar BBA lending (09:30am) Apr Sweden: Labor force survey (09:30am) Apr Norway: Sector accounts (10:00am) 1Q Switzerland: UBS cons. Indicator (08:00am) Apr	26 May Sweden: Trade balance (09:30am) Apr	27 May United Kingdom: CBI distributive trades (11:00am) May Sweden: PPI (09:30am) Apr Norway: Labor directorate unemployment (09:00am) May Switzerland: Employment (09:15am) 1Q	28 May United Kingdom: Gfk cons. Conf. (12:01am) May Sweden: GDP (09:30am) 1Q Retail sales (09:30am) Apr Switzerland: Trade balance (8:15am) Apr KOF leading indicator (11:30am) May
During the week : United Kingdom: Nationwide HPI (08:00am) May				

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Emerging Europe/Middle East/Africa economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
3 May Czech Rep: PMI (9:30am) Apr Hungary: PMI (9:00am) Apr Turkey: CPI (10:00am) Apr 0.7%mom PPI (10:00am) Apr 1.3%mom PMI (10:00am) Apr South Africa: Kagiso PMI (11:00am) Apr 60.9 *Holiday: Russia, Poland*	4 May Poland: PMI (9:00am) Apr Finance Ministry CPI forecast 2.2%oya (10:00am) Apr Russia: Manufacturing PMI Apr Romania: Monetary policy announcement -50bp	5 May Romania: Retail sales (10:00am) Mar South Africa: Vehicle sales (11:00am) Apr Russia: CPI Apr 0.4%m/m	6 May Czech Rep: Monetary policy announcement no change Hungary: Industrial output (9:00am) Mar 4.7%oya	7 May Czech Rep: Trade balance (9:00am) Mar CZK 15bn Industrial output (9:00am) Mar 3.0%oya Retail sales (9:00am) Mar 0.0%oya Romania: Industrial output (10:00am) Mar South Africa: Gross reserves (8:00am) Apr US$42.8bn
During the week:				
10 May Czech Rep: CPI (9:00am) Apr 1.1%oya Hungary: Trade balance (9:00am) Mar Israel: Central bank minutes Turkey: Industrial production (10:00am) Mar 16.1%oya *Holiday Russia*	11 May Turkey: Current account (10:00am) Mar -US$4.1bn Hungary: CPI (9:00am) Apr Romania: CPI (9:00am) Apr 4.1%oya	12 May Czech Rep: GDP (9:00am) 1Q 1.7%oya Hungary: GDP (9:00am) 1Q Romania: GDP (9:00am) 1Q -1.5%oya South Africa: Manufacturing output (1:00pm) Mar	13 May South Africa: MPC decision (2:00pm) No change	14 May Czech Rep: Central bank Minutes Israel: CPI (6:00pm) Apr Poland: CPI (2:00pm) Apr
During the week: Russia: GDP 1Q 6.3%oya				
17 May Czech Rep: PPI (9:00am) Apr Current account (10:00am) Mar CZK -1bn Poland: Current account (2:00pm) Mar Romania: Current account Mar Turkey: Unemployment (10:00am) Feb Consumer confidence (10:00am) Apr	18 May Hungary: Average gross wages (9:00am) Mar Turkey: Monetary policy announcement no change Russia: PPI April 1.5%m/m IP April 5.5%oya	19 May Hungary: Central bank minutes Poland: Average gross wages & employment (2:00pm) Apr	20 May Poland: PPI (2:00pm) Apr Industrial output (2:00pm) Apr Core inflation (2:00pm) Apr	21 May Poland: Retail sales (10:00am) Mar
During the week:				
24 May Israel: Monetary policy announcement +25bp Turkey: Capacity utilization (10:00am) May	25 May Hungary: Retail sales (10:00am) Mar Poland: Monetary policy announcement No change South Africa: GDP (11:30am) 1Q	26 May South Africa: CPI (11:30am) Apr	27 May South Africa: PPI (11:30am) Apr	28 May
During the week: Czech Rep: General elections on 28-29 May				

Non-Japan Asia economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
3 May Australia: HPI (11:30 am) 1Q 3.5 %q/q China: PMI manufacturing Apr 57.5 Index, sa Hong Kong: Retail sales (4:30 pm) Mar 29.9 %oya India: Trade balance Mar PMI manufacturing Apr Indonesia: CPI (2:00 pm) Apr 3.5 %oya Trade balance (2:00 pm) Mar 2.4 US$ bn, nsa Korea: CPI (1:30 pm) Apr 2.5 %oya Foreign exchange reserves Apr Trade balance 2.4 US$ bn New Zealand: ANZ commodity price (2:00 pm) Apr Thailand: CPI (2:00 pm) Apr 3.8 %oya *Holiday China, Philippines* *Thailand, Vietnam,*	4 May Australia: RBA cash target (3:30 pm) May 25 bp hike Malaysia: Trade balance (6:00 pm) Mar 3.9 US$ bn New Zealand: Labor cost index 1Q 0.3 %q/q, sa Singapore: PMI (9:30 pm) Apr 52.0 Index	5 May Australia: Building approvals (11:30 am) Mar -1.0 %m/m, sa Indonesia: BI rate announcement (1:00 pm) May no change Philippines: CPI (9:00 am) Apr 4.7 %oya Taiwan: CPI (4: 00 pm) Apr 1.5 %oya *Holiday Korea, Thailand*	6 May Australia: Retail sales (11:30am) Mar 0.2 %m/m, sa Trade balance (11:30am) Mar -1500 A$ mn, sa New Zealand: Unemployment rate (10:45 am) 1Q 7.3 %, sa	7 May Australia: Quarterly monetary policy meet Taiwan: Trade balance (4:00 pm) Mar 1.3 US$ bn
During the week :				
10 May Australia: ANZ job ads (11:30 am) Apr China: Trade balance (12:00 pm) Apr Korea: PPI (12:00 pm) Apr New Zealand: QVNZ house prices Apr *Holiday Philippines*	11 May Australia: NAB bus. Confidence (11: 30 am) Apr China: CPI 10:00 am) Apr PPI(10:00 am) Apr FAI (10:00am) Apr Retail sales (10:00 am) Apr IP (10:00 am) Apr Korea: Money supply (9:00 am)Apr Malaysia: IP (12:00 pm) Mar	12 May Australia: Housing finance approvals (11:30 am) Mar India: IP Mar Korea: BoK monetary policy meeting (10:00 am) May Unemployment rate (9:00am) Apr Philippines: Exports (9:00 am) Mar	13 May Australia: Unemployment rate (11: 30 am) Apr Malaysia: BNM monetary policy meeting (6:00 pm) Apr New Zealand: Business NZ PMI (10:30 pm) Apr *Holiday Indonesia*	14 May Hong Kong: GDP (4:30 pm) 1Q India: WPI Apr Korea: Export price index (10:00 am) Apr Import price index (10:00 am) Apr SPPI Mar New Zealand: Retail sales (10:45 am) Mar Singapore: Retail sales (1:00 pm) Mar
During the week: China: Money supply Apr FDI Apr				
17 May Philippines: OFW remittances (10:45 am) Mar Singapore: NODX (1:00 pm)Apr	18 May Hong Kong: Unemployment rate (4:30 pm) Apr New Zealand: PPI (10:45 am) 1Q Philippines: BOP Apr	19 May Australia: Westpac consumer confidence (10: 30 am) May Malaysia: CPI (5:00 pm) Apr	20 May Hong Kong: CPI (4:30 pm) Apr Taiwan: Export Orders (4:00 pm) Apr	21 May New Zealand: Visitor arrivals (10:45 am) Apr Credit card spending (2:00 pm Apr *Holiday Hong Kong, Korea*
During the week: Indonesia: GDP 1Q Malaysia: GDP 1Q Philippines: Budget balance Apr				
24 May Australia: New motor vehicle sales (10: 30 am) Apr Singapore: CPI (1:00 pm) Apr Taiwan: Unemployment rate (4:00 pm) Apr Taiwan: IP (4:00 pm) Apr Thailand: GDP (9:30 am) 1Q	25 May	26 May Australia: Westpac leading index (10: 30 am) Mar Construction work done (10:30 am) 1Q Private capital expenditure (10:30 am) 1Q Philippines: Imports (9.00 am) Mar Singapore: IP (1:00 pm) Apr Taiwan: Leading index (4:00 pm) Apr	27 May Hong Kong: Trade balance (4:30 pm) Apr Korea: Current account (8:00 am) Apr Philippines: GDP (10:00am) 1Q New Zealand: Trade balance (10:45 am) Apr *Holiday India*	28 May New Zealand: Building permits (10:45 am) Apr Taiwan: GDP (5:00 pm)1Q *Holiday Indonesia, Malaysia,* *Singapore, Thailand*
During the week: Vietnam: CPI May Trade balance May				

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

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Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
3 - 7 May	3 May	4 May	5 May	6 May	7 May
	Brazil • Trade balance (Apr) Germany • Retail sales (Mar) United States • ISM mfg (Apr) • Light vhcl sales (Apr) • Personal income (Mar) PMI: • Czech Republic, Hungary, South Africa, Sweden, Switzerland, Turkey (Apr) PMI mfg: • Brazil, China, Euro area, France, Germany, Italy, India, Norway, Spain (Apr)	Australia • RBA mtg: +25bp Brazil: IP (Mar) Germany: Retail sales (Mar) Poland: PMI (Apr) Romania • BNR mtg: -50bp Russia: PMI mfg (Apr) Singapore: PMI (Apr) UK: PMI mfg (Apr) United States • Pending home sales, Factory orders (Mar)	Euro area • Retail sales (Mar) Indonesia: BI mtg: No chg Norway • IP mfg (Mar) • Norges bnk mtg: +25bp UK: PMI const (Apr) United States • ADP employment, ISM nonmfg (Apr) PMI srv/comp: • Euro area, France, Germany, Italy, Spain (Apr)	Australia • Retail sales (Mar) Czech Republic • CNB mtg: No chg Euro area • ECB mtg: No chg Germany • Mfg orders (Mar) Hungary: IP (Mar) Japan: PMI srv/comp (Apr) Peru: BCRP mtg: No chg United Kingdom • General elections 2010 • PMI services (Apr) United States • Bernanke speech • Productivity and costs (1Q)	Canada • Employment (Apr) Euro area • Trichet speech Germany: IP (Mar) Norway: IP mfg (Mar) Sweden: IP (Mar) Taiwan • Trade balance (Mar) UK: New car regs (Apr) United States • Employment (Apr) • Consumer credit (Mar)
10 - 14 May	10 May	11 May	12 May	13 May	14 May
China • Money supply (Apr) Japan • Cabinet Office private consumption index (Mar)	France • IP (Mar) Germany • Foreign trade (Mar) Italy • IP (Mar) Japan • MPM minutes (Apr) Turkey • IP (Mar) United Kingdom • MPC mtg: No chg	China • CPI, FAI, retail sales, IP (Apr) Germany • CPI final (Apr) United States • JOLTS (Mar)	Brazil: Retail sales (Mar) India: IP (Mar) Korea: BoK mtg: No Chg United Kingdom • Labor mkt rpt (Mar) • BoE qtrly inflation rpt United States • International trade (Mar) • Federal budget (Apr) GDP: • Czech Republic, Euro area, France, Germany, Hungary, Italy, Romania, Spain (1Q)	Chile • BCCh mtg: No chg Japan • Econ Watcher surv (Apr) Malaysia • BNM mtg: +25bp South Africa • MPC mtg: No chg United Kingdom • Trade balance (Mar) United States • Import prices (Apr)	Hong Kong • GDP (1Q) United States • Retail sales (Apr) • IP (Apr) • Consumer sent (May) • Bus inventories (Mar)