

Australia and New Zealand - Weekly Prospects

Summary

- The **RBA** pulled the interest rate trigger again last week. Clearly, the apparent uncertainty from February over how households were coping with earlier rate hikes has passed. The tone of the statement was upbeat, as you would expect, but did not signal there was additional urgency about policymakers' desire to return the policy stance to "normal". Another hike in April is possible if the domestic data-flow is firm and there is calm offshore. We suspect, though, that the next move will come in May. The intervening period will give Board members a window to assess how other uncertainties, like the sovereign issues in Europe, are evolving. Following last week's GDP data, which showed the economy growing at a decent clip in 4Q, this week should see a 10,000 gain in employment (but a small rise in the jobless rate) and a 3% rise in home loans. Consumer confidence, though, probably dropped for the second straight month after the RBA's rate hike. Tomorrow's ANZ job ads report will be a handy guide on upcoming employment prints.
- In **New Zealand**, the highlight will be the RBNZ official cash rate (OCR) announcement Thursday, even though Governor Bollard is unlikely to deliver many surprises. We suspect the statement accompanying what will be a 'no change' decision will be similar to that delivered six weeks ago, but more downbeat on the domestic economy given the slew of weak data released recently. Our forecast remains that the first OCR hike will be delivered in July (+50bp)—the consensus is clustered around the June decision, with a 25bp hike. Before kicking off the next tightening cycle, Governor Bollard wants hard evidence that the recovery underway has legs. He probably will sit on the policy sidelines until after the 1Q GDP report is released in late-June.
- As the **global economy** moves through the first quarter of 2010, GDP growth appears to be downshifting. However, through this downshift there is also evidence that the anticipated broadening in the base of economic growth is taking hold. It may take some time for this dynamic to be reflected in stronger activity readings—particularly as the negative impact of inclement winter weather has yet to fully reverberate through January and February releases. However, just as spring follows winter, the motion of the global economy is now firmly directed toward delivering self-sustaining growth. We are confident there will be strong and synchronized global growth in the spring.
- **Chinese inflation** is being pushed higher by food prices. It is expected to rise to 2.1% oya in February in this week's report, and move gradually toward an expected peak of 3.9% sometime this summer. However, the PBOC is not able to raise rates yet as it needs hard evidence of rising inflation to win over the more dovish voices in the Beijing policymaking structure. As such, the focus of the PBOC will remain on liquidity and credit management. Another near term RRR hike is likely to continue the process of withdrawing excess liquidity. Signs that inflation is set to move above the 3% target level will likely pave the way for an initial 27bp hike in April followed by two more hikes later this year, which would bring the real deposit rate into positive territory. With exports expected to track a solid recovery this year, imported inflation emerging as a concern, and political pressure easing somewhat, we expect CNY/USD to resume a gradual appreciation path in late 2Q.

This week's highlight

The Aussie employment print Thursday, which should show that monthly job growth moderated in February to 10,000 (consensus +15,000). We expect a small rise in the jobless rate to 5.4%.

March 8, 2010

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Data and event previews - Australia and New Zealand

Date	Time ^(a)	Data/event	Forecast		Previous
			JPMorgan	Consensus ^(b)	
Tuesday, March 9	8.45am	NZ card spending (%m/m, Feb.)	0.5	na	0.5
Tuesday, March 9	11.30am	NAB business confidence (Index, Feb.)	15	na	15
Tuesday, March 9	11.30am	ANZ job advertisements (%m/m, Feb.)	na	na	-8.1
Wednesday, March 10	8.45am	NZ terms of trade (%q/q, 4Q)	0.6	na	-1.3
Wednesday, March 10	9.00am	RBA Assistant Governor Lowe's speech	na	na	na
Wednesday, March 10	10.30am	Westpac-MI consumer confidence (%m/m, Mar.)	-3.5	na	-2.6
Wednesday, March 10	11.30am	Aust. housing finance (%m/m, Jan.)	3.0	2.0	-5.5
Thursday, March 11	7.00am	RBNZ official cash rate announcement (%)	2.50	2.50	2.50
Thursday, March 11	8.30am	NZ business PMI (Index, Feb.)	na	na	52.0
Thursday, March 11	8.45am	NZ food prices (%m/m, Feb.)	na	na	2.1
Thursday, March 11	11.00am	Aust. consumer inflation expectation (% , Mar.)	na	na	3.2
Thursday, March 11	11.30am	Aust. employment change (000s., Feb.)	10	15	52.7
Thursday, March 11	11.30am	Aust. unemployment rate (% , Feb.)	5.4	5.3	5.3
Thursday, March 11	11.30am	Aust. participation rate (% , Feb.)	65.3	65.3	65.3
Thursday, March 11	11.30am	RBA Bulletin (Mar.)	na	na	na
Friday, March 12	8.00am	REINZ house sales (% oya, Feb.)	na	na	-1.1
Friday, March 12	8.00am	REINZ house prices (%m/m, Feb.)	0	na	-1.6
Friday, March 12	8.45am	NZ retail sales (%m/m, Jan.)	0.2	na	0.0
Friday, March 12	8.45am	NZ retail sales ex-auto (%m/m, Jan.)	0.2	na	-1.8

(a) Australian Eastern Standard Time.

(b) Consensus based on Bloomberg survey.

Data previews - contd.

Australia

NAB business confidence (Index, Feb.) - Business confidence is at an elevated level after rebounding in January, and will probably have remained there in February. The RBA's surprise decision to leave the cash rate unchanged last month will have offset the growing uncertainties that emerged on the global front.

ANZ job advertisements (%m/m, Feb.) - The sharp drop (-8%) in job ads in January, the largest monthly fall since February 2009, took job ads back down to very depressed levels. Ads remain nearly 60% below the most recent peak and only 8% off the low from July 2009. On this evidence, there is likely to be a moderation in employment gains, at least in the near term. This falls in line with our view that many employers will rebuild workers' hours, which were cut significantly over the last 12 months, before hiring new staff.

RBA Assistant Governor Lowe's speech - The Assistant Governor (Economic) is speaking at the Urban Development Institute of Australia's National Congress in Sydney on "Future Directions in Finance". Given the audience, Dr. Lowe hopefully also will touch on how developments in the housing market may influence RBA policy. Unfortunately, there is no Q&A session scheduled following the speech.

Westpac-MI consumer confidence (%m/m, Mar.) - Consumer confidence probably fell further in March (-3.5% m/m), but will remain at an elevated level of 113. The number of optimists continues to outnumber pessimists, as they have done since mid-2009. The fall in confidence in March will owe much to the RBA's decision to hike the cash rate a further 25bp last week. Expectations of further rate hikes will continue to weigh on sentiment near-term.

Housing finance (%m/m, Jan.) - We expect a rebound in the number of home loans issued in January, after the exceptionally weak end to last year. Our forecast is for a 3% m/m rise, although home loan demand will likely ease throughout 1H10. Many first home buyers (FHBs) will withdraw from the market, owing to the end of the expanded FHBs' grant on December 31, the introduction of price caps on the original FHBs' grant this year, rising interest rates and lousy affordability. The effectiveness of the Government's expanded FHBs' grant will be judged as much on its aftermath as its operational period—the test will be whether the momentum gained in 2009 can attract investors to replace FHBs.

Employment change (000s, Feb.) - Leading indicators of employment suggest that the astonishing gains in employment in recent months will ease. The economy has added a whopping 195,000 jobs since last September; 52,700 of these jobs were added in January. Our forecast is for "just" 10,000 jobs to have been added to the economy last month. One concern for RBA officials anxious about the economy's lack of spare capacity will be the size of the monthly employment gains, which in recent months have been at levels similar to those recorded during the last resources boom. The participation rate likely remained steady in February at 65.3%, but the unemployment rate will rise a notch to 5.4%. We suspect the unemployment rate probably peaked at 5.8%, topping out just 1.9%-pts above the low touched in February 2008.

RBA Bulletin (Mar.) - While discussing prudential issues in Parliament some weeks ago, RBA Governor Stevens indicated that the March Bulletin would feature an update on developments in bank funding costs. The discussion will shed light on how the Bank views the return to 'average' lending rates, relative to the adjustment in the cash rate that has already been made. This issue is of central importance to understanding how far the cash rate is from a neutral or restrictive setting.

New Zealand

NZ card spending (%m/m, Feb.) - Weak labour market conditions should have underpinned credit card usage in February. We expect a rise of 0.5% m/m, the same rate as in January. High unemployment and household debt levels will, however, keep consumers cautious about spending, so many will be reluctant to acquire excessive amounts of credit card debt.

NZ terms of trade (%q/q, 4Q) - After declining for six straight quarters, the terms of trade probably increased in 4Q, owing to strong export prices and a drop in import prices over the quarter. The terms of trade probably rose 0.6%q/q from the four year low touched in 3Q.

RBNZ official cash rate (%q/q, 4Q) - The RBNZ will leave the cash rate at a record low 2.5% and reiterate that, providing the economy continues to recover in line with the Bank's forecasts, policy stimulus will begin to be removed "around the middle of 2010." Don't expect too many surprises, however. The statement will likely be similar to that delivered six weeks ago, although probably will be more downbeat on the domestic outlook following the slew of weak data since the start of the year, on top of recent global jitters. The RBNZ will sit on the policy sidelined until July.

REINZ house prices (%m/m, Feb.) - We expect that house prices in New Zealand would have remained steady in February, with REINZ to report that the national median residential house price remained at NZ\$350,000. The median house price was up 7.7% oya in January, but was NZ\$10,000 lower than in December 2009.

NZ retail sales (%m/m, Jan.) - Expect only a modest rise in retail sales in January. Sales will have been buoyed by still-low interest rates and solid net permanent migration flows, but the weakness in the labour market will have dragged on spending at the start of the year, as will softer growth in house prices and equity price declines. The labour market will be slow to recover in 2010 given that the weakness in business lending suggests investment will remain soft, which will weigh on employment.

Australia

- **RBA continued to normalise rate settings**
- **Aussie economy expanded a solid 0.9%q/q in 4Q**
- **Job growth will have slowed to 10,000 a month**

By hiking another 25bp last Tuesday, the RBA took another step toward a more normal cash rate and signaled that the process of policy normalization has much further to run. There is little doubt that Australia's cash rate is too low, particularly following data last week showing the economy expanded at a solid 0.9%q/q clip in 4Q09. The week ahead will provide further evidence that the economy is holding up relatively well, with consumer and business confidence to remain elevated and employment gains to have continued in February, albeit at a more moderate pace.

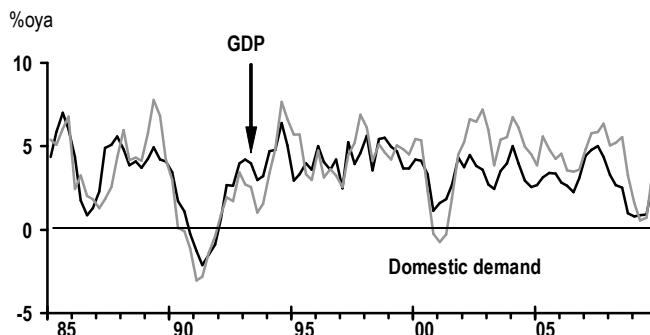
Upbeat RBA raised cash rate again

The RBA last week lifted the cash rate a further 25bp to 4%, the fourth hike since last October and a resumption of the tightening cycle that unexpectedly stalled in February. We had forecast another "unchanged" outcome last week on the basis that, arguably, there is more uncertainty over the outlook now than there was four weeks ago, particularly offshore. It seems, though, that Board members this time were willing to take a leap of faith on Australia's economy being sufficiently resilient to withstand another small hop towards a normal policy stance and that the "tail risks" overseas are not immediately threatening.

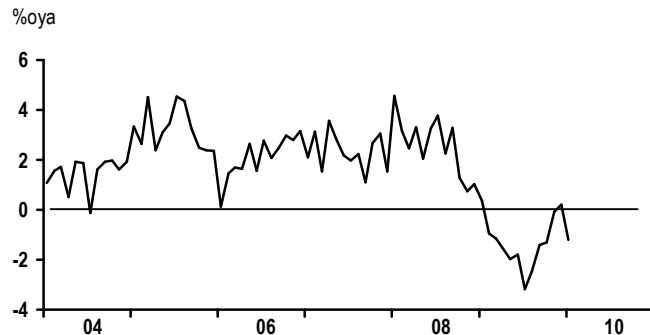
Last week's commentary was a virtual echo of the tone of last month's equally optimistic "hike-like" statement, which included everything but the announcement of a higher cash rate. The comments on Australia are a little more upbeat than they were last month—particularly in regard to the investment pipeline and house prices—but the sentiment on the world economy is a little more downbeat. On balance, then, the tone is about the same as before. The statement described the global recovery as "hesitant" and, for the first time in nearly a year, there was no explicit mention of China, Australia's single largest export partner.

We look for the next hike in the cash rate to come in May, with officials using the intervening two-month period to gauge how quickly the lingering clouds of doubt are clearing. Any convincing evidence that the clouds have darkened, or that it has started to rain, will see the RBA's pause last even longer. Alternatively, a run of unexpectedly firm data could see the RBA deliver a back-to-back hike in April. With officials clearly believing that their policy stance remains easy, every meeting from here is live.

Australia: GDP and domestic demand



Australia: aggregate hours worked



Aussie economy expanded solidly in 4Q

Australia's economy advanced at a healthy clip in 4Q. Real GDP expanded 0.9%q/q (J.P. Morgan: 1.1%; consensus: 0.9%), three times the rate of growth in 3Q. The robust rate of expansion far exceeded official expectations when the emergency interest rate settings were put in place, explaining why the RBA was the first G-20 central bank to tighten monetary policy. With net exports a drag on GDP growth again, all of the growth in the economy came from domestic sources. Indeed, domestic final demand soared 2%q/q, the fastest rate of growth since 1Q07. The impressive performance of the domestic economy occurred despite the RBA pulling the interest rate trigger in each month of 4Q09. The RBA, of course, last week raised the cash rate another quarter point to 4%.

Private investment led the way in 4Q. The majority of this new spending is destined for the booming mining sector. Generous government stimulus programs also played a key role in the acceleration in GDP growth, as did underlying private demand. Household spending rose 0.7%q/q, and dwelling investment rose 1.1%. Net exports shaved 1.3%-pt from GDP growth, while inventories made a modest 0.1% positive contribution.

Economy probably added “just” 10K jobs

Leading indicators, including the ANZ job advertisements series and employment component of the NAB business survey, suggest that the astonishing gains in employment in Australia in recent months eased in February. The economy has added a whopping 195,000 jobs since last September, 52,700 of these jobs were added in January, but our forecast is for “just” 10,000 jobs to have been added to the economy last month. Further, given the significant fall in workers’ hours in 2009, we believe that employers will reinstate workers’ hours before hiring new staff, which should keep a lid on employment gains in the near term.

With the participation rate likely having remained steady at 65.3%, the unemployment rate will rise a notch to 5.4%. We suspect that the unemployment rate probably already has peaked at 5.8%, topping out just 1.9%-pts above the trough touched in February 2008, a stark contrast to the sharp rises recorded elsewhere across the globe. The concern for the RBA will be the size of the monthly employment gains, which in recent months have been at levels similar to those recorded in the last resources boom.

Loans to bounce, but trend weakening

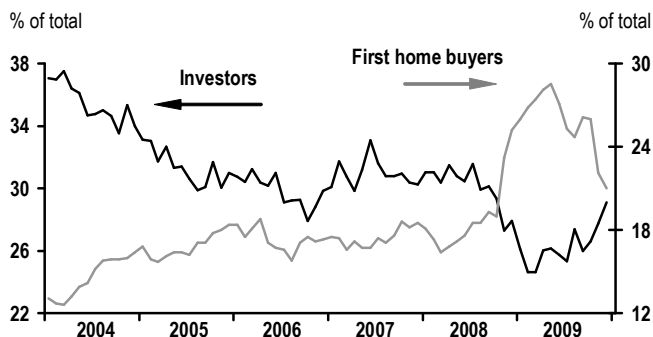
New home loan commitments probably rose 3% m/m in January. Indeed, some payback is due for the massive 5.5% and 6.1% slumps in December and November respectively. Currently, the flow of new loans is 14% weaker than that in September, which represented the last month of the fully expanded First Home Buyers’ (FHBs’) grant. The likely bounce in January notwithstanding, the trend in housing finance will, therefore, continue to weaken. Building approvals activity has softened (data this week showed approvals slumped 7% m/m in January), and monthly house price appreciation appears to be easing.

The withdrawal of FHBs, as evidenced by their falling representation as a percentage of total loans (21% as of December), likely continued in January. The first half of 2010 will represent something of a crucible for the housing market, as interest rates rise, price caps are applied to the vanilla FHBs’ grant, and sell-side activity rebounds due to higher prices. It is hard to envisage a substantial loosening of the market, however, given low unemployment and persistent undersupply of available housing.

Confidence slipping further post rate hike

Consumer confidence, as measured by the Westpac-Melbourne Institute (WMI), probably fell further in March.

Australia: housing finance



Australia: retail sales and consumer confidence



We suspect that the WMI slipped 3.5% m/m, following a 2.6% drop in February, owing mainly to the RBA’s decision to hike the cash rate last week. In response to the rate hike, the largest falls in confidence will likely be recorded in sentiment toward family finances.

Of those surveyed in February, 93% expected the cash rate to rise over the next 12 months, with over 60% expecting the increase to be more than 1%; this will weigh on sentiment near-term. In 2H10, however, the anticipated investment boom has positive implications for the employment outlook and, therefore, for wages and spending, which will underpin sentiment down the track.

Discretionary spending strong in Australia

Retail sales values unexpectedly spiked 1.2% m/m in January (J.P. Morgan: flat; consensus: +0.5%), the second fastest monthly growth rate since March 2009. The remarkably strong retail result stemmed largely from a bounce in discretionary spending (+0.7% m/m), with department store sales the main driver, rising 7.2%.

The surge in spending came despite the three straight quarter-point rate hikes delivered by the RBA in 4Q and the decision by most of the commercial banks to out-hike the

RBA. However, the recent strength in consumer spending should soon start to ease. Anecdotal evidence suggests that consumers are taking a more conservative approach to spending, mainly owing to expectations of further rate hikes.

Data releases and forecasts

Week of March 8 - 12

ANZ job advertisements		Nov	Dec	Jan	Feb
Tue Mar 9 11:30am	sa				
	%m/m	5.2	6.0	-8.1	<u>-3.0</u>

Job ads likely slipped again in February, after posting the largest fall since February 2009 in the previous month. Our view is that employers will reinstate worker hours (which were cut significantly over the last 12 months) before hiring new staff.

NAB monthly business survey		Nov	Dec	Jan	Feb
Tue Mar 9 11:30am	% balance, sa				
	Business confidence	19	8	15	<u>15</u>

After rebounding in January, business confidence will remain steady at an elevated level in February. The RBA's surprise decision to leave the cash rate unchanged will offset the growing uncertainties that emerged on the global front.

WMI consumer confidence survey		Dec	Jan	Feb	Mar
Wed Mar 10 10:30am	100=neutral, sa				
	%m/m	-3.8	5.5	-2.6	<u>-3.5</u>

Housing finance approvals: owner occupiers		Oct	Nov	Dec	Jan
Wed Mar 10 11:30am	Number of loans, sa				
	%m/m	-2.9	-6.1	-5.5	<u>3.0</u>
	%oya	24.7	13.4	0.4	<u>-1.4</u>

Labor force		Nov	Dec	Jan	Feb
Thu Mar 11 11:30am	sa				
	Unemployment rate (%)	5.6	5.5	5.3	<u>5.4</u>
	Employed (000 m/m)	33.1	37.5	52.7	<u>10.0</u>
	Participation rate (%)	65.2	65.3	65.3	<u>65.3</u>

Review of past week's data

Inventories

	2Q09	3Q09	4Q09		
%q/q sa	-3.1	-1.9	0.8	0.1	<u>-0.5</u> 0.2
%oya sa	-3.0	-1.4	-3.4	-3.7	<u>-2.7</u> -2.6

Company operating profits (business indicators)

Nominal, gross operating, sa	2Q09	3Q09	4Q09		
%q/q	-7.0	-6.9	-2.4	-1.4	<u>3.0</u> 2.2
%oya	-12.6	-19.6	-19.7	<u>-13.7</u> -11.2	

Current account balance

	2Q09	3Q09	4Q09		
Current account (A\$ bn sa)	-13.1	-16.2	-14.7	<u>-16.9</u> -17.5	
As a % of GDP	-4.2	-5.2	-4.7	<u>-5.4</u>	

As a percentage of GDP the CAD widened further in 4Q to 5.4%. The CAD will continue to expand given that business investment is set to surge in 2H10, and mining investment will rise further as a share of GDP.

Building approvals

	Nov	Dec	Jan		
%m/m sa	10.4 8.5	2.2 5.2	-2.0 -7.0		
%oya sa	40.5 39.3	53.3 54.8	55.4 47.6		

Residential building approvals plummeted in January, owing to a 29% slump in "other" (i.e., higher density) dwellings.

Retail trade

	Nov	Dec	Jan		
%m/m sa	1.5	-0.7 -0.9	0.0 1.2		
%oya sa	7.1	7.2	2.1	2.0	<u>1.8</u> 3.0

RBA cash rate announcement

25bp rate hike. See main text.

Real GDP

Chain volume, sa	2Q09	3Q09	4Q09		
%oya	0.6	0.7	0.2	0.3	<u>1.1</u> 0.9
%q/q	0.4	0.9	0.5	0.9	<u>2.6</u> 2.7

Trade balance

	Nov	Dec	Jan		
Trade balance (A\$ mn, sa)	-1728	-1720	-2251	-2174	<u>-1500</u> -1176

New Zealand

- **RBNZ to reinforce steady cash rate until midyear**
- **Delay will bring need for larger rate hikes**
- **Retail sales will have risen modestly in January**

In New Zealand, the economic data flow has slowed to a trickle in recent weeks. The RBNZ decision Thursday is the highlight, but should fail to deliver a surprise. Governor Bollard will likely leave the official cash rate (OCR) unchanged and reiterate that policy stimulus may be removed “around the middle of 2010.” Given the string of weak domestic indicators released in recent months, there is little urgency to kickoff the next tightening cycle. Retail sales numbers this week will likely show that consumer spending remains subdued.

RBNZ will remain on hold until July

The RBNZ will leave the OCR at a record low 2.5% Thursday and reiterate that—providing the economy continues to recover in line with the Bank’s forecasts—policy stimulus may be removed “around the middle of 2010.” The OCR statement will likely mirror that delivered six weeks ago, although, if anything, the RBNZ may be a little more downbeat on the domestic economy. Recent data on the housing market, employment, and retail sales have painted a gloomy picture of the domestic economy.

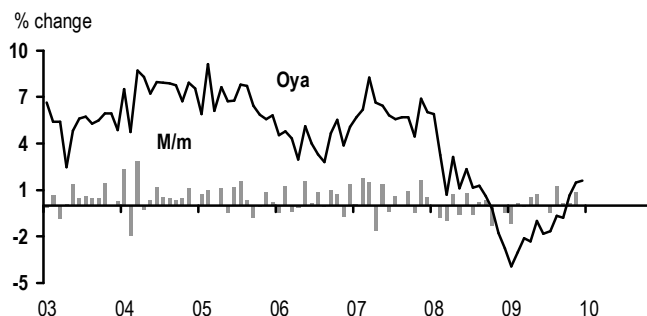
Given the persistent stream of weak data and Governor Bollard’s desire for hard economic evidence that the recovery is sustainable, it is likely the RBNZ will remain sidelined near term. As noted in detail in our recent note titled “RBNZ probably will hold to hinted midyear tightening” (*GDW*, February 19, 2010), we expect that the RBNZ will kick off the next tightening cycle in July with a 50bp hike. Bollard himself has said that the OCR didn’t come down in 25bp hops, so when he is confident the recovery is sustainable, there could be some “meaty chunks” on the upside.

We maintain our forecast that the OCR will rise to 4% by year-end and increase steadily throughout 2011. The medium-term inflation outlook will become a growing concern. Domestic prices are rising, excess capacity is diminishing, and on our forecasts, headline inflation will be back at the top end of the RBNZ’s target range within the foreseeable future.

Kiwi consumer spending still subdued

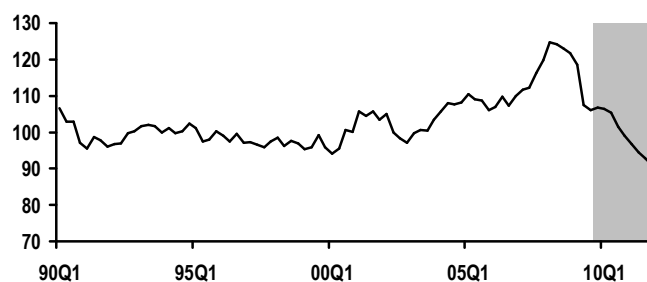
Retail sales probably rose 0.2% m/m in January, buoyed by

New Zealand: retail trade



New Zealand: terms of trade

1985=100, sa



still-low interest rates and solid net permanent migration inflows, which recently hit a five-year high. The rise we forecast is slightly less than the 0.5% m/m increase in electronic card transactions recorded in the January month, which were lifted by a strong result in the fuel component. The pickup in consumer spending, after a flat retail sales result in December, will be underwhelming and will likely remain that way during 2010. The relatively benign recovery we forecast in consumer spending owes mainly to the slow improvement we expect in the labour market. Business lending remains soft, suggesting that business investment also will remain subdued; this will weigh on employment.

Data releases and forecasts

Week of March 8 - 12

Wed Mar 10 10:45am	Terms of trade sa	1Q09	2Q09	3Q09	4Q09
	(%q/q)	-2.7	-9.4	-1.3	<u>0.6</u>

After declining for six straight quarters, the terms of trade probably increased in 4Q, owing to strong export prices and a drop in import prices over the quarter. The terms of trade probably rose 0.6% q/q from the four-year low touched in 3Q.

Thu Mar 11 10:30am	Business PMI sa				
		Nov	Dec	Jan	Feb
	Index	51.9	53.0	52.0	—
	(%oya)	48.3	25.4	23.0	—
Thu Mar 11 9.00am	RBNZ cash rate announcement				
	No change expected. See main text.				
Fri Mar 12 10:45am	Retail trade sa				
		Oct	Nov	Dec	Jan
	%m/m	0.1	0.8	0.0	<u>0.2</u>
	%oya	0.6	1.6	2.2	<u>3.4</u>

Review of past week's data

Net permanent immigration

	Nov	Dec	Jan	
Monthly (000s, nsa)	2.5	1.4	—	2.5
12 month sum (000s, nsa)	20.0	21.3	—	22.6

ANZ commodity price series

nsa		Dec	Jan	Feb	
Index - world prices (%m/m)	2.6	0.4	—	3.8	
Index - NZD (%m/m)	4.3	-1.2	—	7.9	

Global Essay

- **The transition to self-sustaining growth is well under way**
- **As inflation slides in the developed world, food prices are pushing EM inflation higher**
- **EM policymakers continue to display growth oriented bias**
- **BoJ to discuss further actions to fight deflation this week**

There will be growth in the spring

As the global economy moves through the first quarter of 2010, GDP growth appears to be downshifting. However, through this downshift there is also evidence that the anticipated broadening in the base of economic growth is taking hold. It may take some time for this dynamic to be reflected in stronger activity readings—particularly as the negative impact of inclement winter weather has yet to fully reverberate through January and February releases. However, just as spring follows winter, the motion of the global economy is now firmly directed toward delivering self-sustaining growth. We are confident there will be strong and synchronized global growth in the spring.

While it is impossible to tease out the magnitude of weather effects in the February US employment report, it is encouraging to see that recent positive trends remained in place despite the large impact of storms that fell in the sample week. Bad weather did depress the workweek, but a move toward labour income gains continues as does the recovery in hiring in manufacturing and business services. The unemployment rate also held on to the decline recorded in the previous month despite a second consecutive rise in the participation rate. A meaningful turn toward private hiring is imminent.

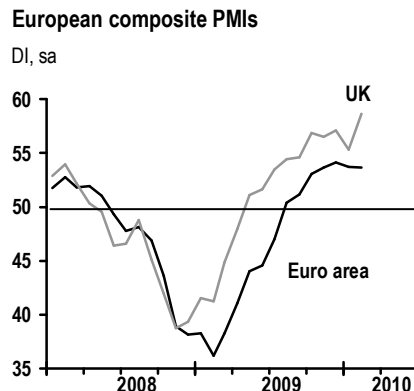
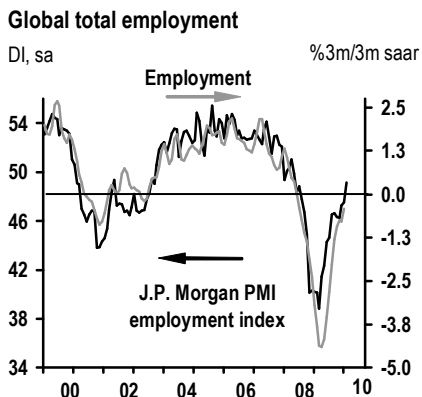
Equally important is the positive news from our February

global PMI survey. The global all-industry PMI employment index rose almost 2pts last month—returning to a level consistent with job growth for the first time since July 2008. Much of this gain came from an improvement in the service sector, which has been lagging the recovery thus far. Geographically, the Euro area continues to be the laggard, and there are legitimate concerns that the fallout from the Greek crisis will continue to slow the region’s overall recovery. Thus far, the spillover to sentiment in other countries looks modest. More encouraging has been the recent news from the UK and Japan. The UK PMI output reading now stands well above its post-1996 average, and survey readings on the labour market continue to improve. In Japan, the two major consumption indicators for January moved in opposite directions. But key surveys are moving higher, and the 4Q09 MoF corporate survey shows that corporate profits are recovering at a rapid pace. It may be too early to draw a strong link, but the recent rise in vacancies and employment suggests that the profit turn may be setting the stage for a recovery in job growth.

Food for further inflation rises across EM

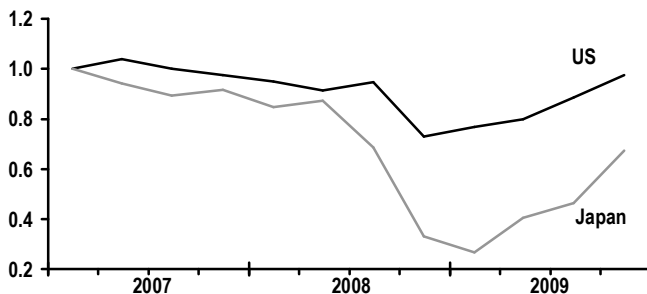
We have been highlighting a prospective marked decline in inflation in the developed economies. Core inflation already is in a steady slide, reflecting unprecedented resource slack and a lack of corporate pricing power. The fall in core inflation is about to be reinforced by a rollback in energy and food inflation, as the very large, positive base effects from these key commodity prices run off.

Inflation dynamics are very different in the emerging economies. For one thing, core inflation does not appear to be under much downward pressure. This is because the EM economies came into the recession in a overheated condition—meaning resource utilization was quite high—and because they have rebounded so strongly over the past year.



Corporate profits

Index, 1Q07=1.0; 4Q09 is forecast for US



In addition, movements in agricultural commodity prices affect consumer prices more strongly and slowly in emerging economies. The weight of food in the overall emerging market consumer baskets is 50% higher than in the developed economies and has a heavier concentration of unprocessed items. Also the passthrough to consumer prices occurs more slowly in EM with passthrough dragging out a full six months. The upshot of this dynamic is that the 2H09 rise in agricultural commodity prices will push EM inflation higher into midyear. EM headline inflation is thus likely to continue climbing for some time, even as the inflation decline in the developed world becomes well established.

One place where this dilemma already has flared up is Turkey, where adverse weather has produced a surge in local food prices that is proving to be a major threat for the inflation-targeting regime. Although core inflation remains stable at around 4% oya, headline inflation rose to 10.1% in February compared with the CBRT's target of 6.5%. With inflation expected to remain elevated, the CBRT will have a tough balancing act between its desire to support growth and the need to anchor inflation expectations. A shift in rhetoric at this week's policy meeting now appears likely.

China inflation rise to spark rate moves

Chinese inflation is also being pushed higher by food prices. It is expected to rise to 2.1% oya in February in this week's report, and move gradually toward an expected peak of 3.9% sometime this summer. However, the PBOC is not able to raise rates yet as it needs hard evidence of rising inflation to win over the more dovish voices in the Beijing policymaking structure. As such, the focus of the PBOC will remain on liquidity and credit management. Another near term RRR hike is likely to continue the process of withdrawing excess liquidity. Signs that inflation is set to move above the 3% target level will likely pave the way for an initial 27bp hike in April followed by two more hikes later this year, which would bring the real deposit rate into positive territory. With exports expected to track a solid recovery this year, imported inflation emerging as a concern, and political pressure easing some-

what, we expect CNY/USD to resume a gradual appreciation path in late 2Q.

The growth-friendly tilt of Chinese policy was reinforced last week as Premier Wen delivered the annual government work report at the National People's Congress (NPC). The report stresses a desire for relatively rapid economic growth, balanced by the need to manage inflation expectations and asset price inflation, while also continuing the gradual process of economic restructuring. Note that we believe GDP will overshoot the government's 8% growth target this year—expanding 10%. That said, the combined January-February data releases in the spotlight this week should show growth momentum easing due to the colder-than-usual weather and recent curbs on credit expansion.

Latin CBs fight FX appreciation first

There are also inflation pressures building across Latin America. While the recent resumption of FX appreciation in the region—on the back of a strong growth recovery, supportive commodity prices, and solid FDI and portfolio inflows—could provide relief, central banks are actually moving to offset this appreciation through reserve accumulation. With currency values already elevated, central banks' primary focus at present is to try to limit the loss of competitiveness of their manufacturing sectors.

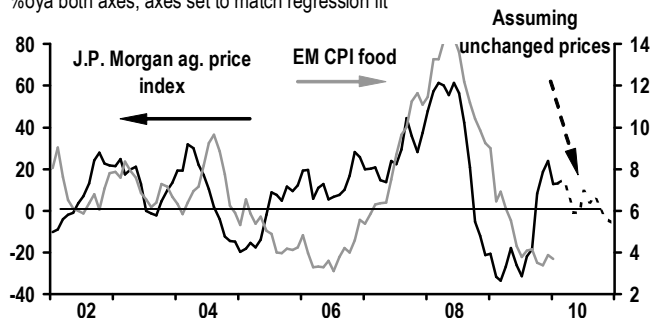
Last week, Colombia announced it would start accumulating reserves at a pace of \$20 million per day. This comes two weeks after Mexico also announced plans to accumulate reserves through a monthly auction of \$600 million in US dollar put options. Central banks in Brazil and Peru maintain their policies of discretionary FX intervention and have bought \$2.3 billion and \$1.6 billion, respectively, so far this year. Although Chile's central bank currently does not have a program to accumulate reserves, we believe that some measure may be announced in the near future since the government will probably repatriate more US dollars held in the offshore copper fund in order to finance the reconstruction efforts following last week's earthquake. The challenge to contain appreciation will intensify as central banks in the region embark on policy rate hikes well before the Fed or ECB, a development that would lend further support to currencies.

The Greek chorus gives limited support

Greece's announcement of a further 2% of GDP of deficit-cutting measures was met with a chorus of approval from European officials and the ECB. Greek officials have said they want to see specific and detailed measures from the EU in return. But it appears likely that European support at this stage will extend no further than an implicit willingness to backstop Greece's ability to finance itself. The hope among

Agricultural commodity prices and EM CPI food prices

%oya both axes; axes set to match regression fit



Euro area nations is that the improvement in market conditions suggested by Greece's sale of EUR5 billion of debt last week will continue, and the promise of European support will not need to be called upon. Last week's deficit-reducing measures have already been passed into legislation, but the vagaries of the data-reporting process mean that an assessment of Greece's progress in reducing the fiscal deficit will take months rather than weeks to make.

A range of signals from developed CBs

In the developed world, central bank meetings last week and next highlight the wide range of policy motion across the group.

- Last week the RBA raised rates another 25bp to 4%, a move we suspected would be delayed until April. Officials had paused in February, and subsequent economic reports had been somewhat mixed. That said, RBA officials have made clear that the policy stance is overly accommodative, so last week's move was not a big surprise. Our best judgment is that the next quarter point move will be delivered in May, although a run of unexpectedly firm data could prompt the RBA to deliver a back-to-back hike in April.
- The Bank of Canada left rates on hold at 0.25% last week and reaffirmed its intention to remain on hold through midyear. However, the Bank offered subtle hints of a policy shift thereafter, consistent with our view that the Bank will begin raising rates in July. In particular, the accompanying statement highlighted that both growth and inflation are higher than anticipated, replacing standard commentary from previous statements that had emphasized downside inflation risk and a willingness to consider unconventional easing.
- Similar to the BoC, the Swiss National Bank is likely to use this week's meeting to change rhetoric in a way that signals rate hikes can be expected after midyear. Last week's GDP report showed that the Swiss economy accelerating quickly, boosted by a healthy combination of net exports and domestic demand, following a fairly shallow recession. With the SNB already uneasy about keeping rates near zero for too long, we look for a first hike in 3Q10.
- With inflation well below target and the economy still struggling, the ECB is a long way from raising interest rates. Nonetheless, officials continue to gradually withdraw emergency liquidity measures put in place during the financial crisis. As in December, last week's announcement advanced the process a little more quickly than anticipated, shifting the three-month liquidity provision to a bidding mechanism rather than unlimited availability at the policy rate.
- When the BoJ meets next week, the issue on the table will be how to combat deflation. Although the economy has performed reasonably well over the past few quarters, GDP growth is expected to moderate as a loss of fiscal stimulus damps the growth of consumer spending and public works. With financial conditions having tightened somewhat year to date, it would not be surprising if officials discussed additional QE measures that could be rolled out in the next few months if needed.

JPMorgan View - Global Markets

Uncertainty is receding— add to risky assets

- **Asset allocation:** Confidence in the sustainability of the rally is growing as major threats from jobs and policies are receding. We have moved from small to normal overweights of risky assets.
- **Economics:** No change in forecasts of recovery, but increased confidence as the risks to sustainability are gradually receding.
- **Fixed income:** Close shorts in US 2s, but stay short in the UK. Buy Greek government debt.
- **Equities:** Stay long, focused on small caps and cyclical sectors. We are reluctant to overweight EM equities despite their higher beta.
- **Credit:** Investors are becoming more bullish US HG spreads but have yet to adjust their positions. Stay long USHG.
- **FX:** Take profit on long USD positions against EUR, GBP, and commodity currencies.
- **Commodities:** Stay long commodities, favouring base and precious metals near term.

Better economic data and receding risks contributed to strong rallies in equities, credit, and commodities, and a backup in bonds. The US dollar was flat.

Our analysis continues to focus on two separate drivers of markets—**expected growth of economies and earnings, and the uncertainty around these growth rates**. The first force—which we called the **recovery rate**—is largely spent. Our economists' forecast for global growth in 2010 has been at the same 3.3%-3.4% level for six months now, and the consensus has almost fully caught up with them. The second driver—receding fears and uncertainties—is the more important driver of markets now. And it is here that we've gotten really good news over the past two weeks.

The twin threats to our positive views have come from two risk areas—premature policy tightening and unfinished delevering. The last few weeks have provided a number of signals that major central banks recognize economic vulnerabilities and falling core inflation and will thus stay on hold. A gradual clean-up of emergency policy measures is, and should be, providing confidence in the sustainability of growth, rather than increasing worries. China is the most

important test case. We expect a soft landing, but understand market worries and thus are underweight China and flat EM equities. Concerns about a generalized and economy-killing fiscal tightening enforced by bond vigilantes are also receding, as Greece takes its tough medicine.

Our fears of further **delevering** have been focused not on banks or consumers but on **corporates**, given their piling up of cash. Year-end jobs data had raised the risk that a wait-and-see attitude by companies uncertain about final demand could become self-fulfilling and drag the world economy down again.

And it is here—on the jobs front—that we are getting welcome relief. Our global PMI released this week suggests that global job growth has returned. Numerous countries already are reporting job gains, and the US may well have joined that camp if not for the impact of the snowstorms.

Our reading is that **risks are receding, from high, to not so high anymore, and are low compared to what is priced into asset markets**. Our monthly *GMOS* has a more in-depth analysis of the comparison of risk premia with uncertainty, which we summarize here. We measure the price of risk in the US as the slope of the risk-return trade-off line across major assets (second chart). We measure risk or uncertainty as the dispersion of US economic growth forecasts for the coming four quarters. Risk and risk premia have each fallen but remain above normal. However, risk has declined significantly more than what is priced into the market.

The combination of this quantitative valuation of risk premia and our more heuristic analysis of risk keeps us into risky assets. In order of importance, we like **most equities (small caps and cyclicals), then higher-yielding credits, followed by commodities (base metals), and rounded off with a small long in US HG**. This strategy is not mega bearish bonds, where we trade tactically from the short side.

Fixed income

Bonds fell slightly last week, on stronger activity data and increased confidence that Greece will be able to fund its fiscal deficit. The lack of major surprises from central banks has been another contributor to diminishing market uncertainty. Last week, the ECB announced that it would make its liquidity provision slightly less generous, in keeping with our expectation that G-4 central banks will unwind their extraordinary stimulus very gradually. Those central banks that are tightening, such as the RBA last week, are doing so in response to strengthening economies, a benign outcome.

We maintain a medium-term bearish view, as demand for bonds should fall much more than supply this year, largely due to the end of QE. But we have been playing shorts tactically, to benefit from the lack of clear direction in bond markets, and **close our US short duration position** in response to last week's sell-off. However, we stay underweight in the UK, where many shorts have been covered over the past few weeks, leaving positions more conducive to higher yields.

Greece took two significant steps toward bolstering market confidence this week, announcing further fiscal consolidation measures and issuing a 10-year bond. Greek debt is likely to remain volatile, not least because of the difficulty in implementing austerity measures. But spreads of close to 400bp provide ample compensation, and we go long Greece. Ireland provides a less volatile way to position for intra-EMU convergence—we stay long.

Equities

Equities were up 3%. **Flows have turned more supportive**, driven by a rise in share buyback and M&A activity as well as retail buying. Retail investors bought equity funds for a third straight week following six straight weeks of outflows.

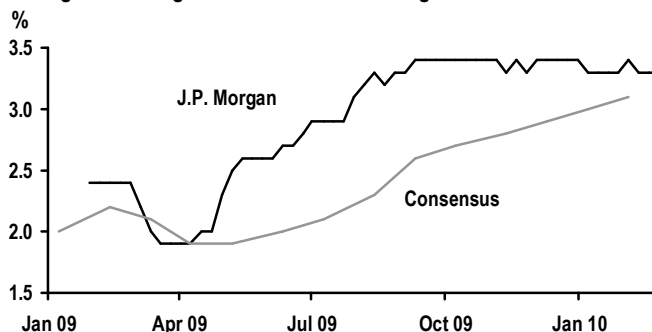
We maintain a **positive view on equity markets**. Our positive stance is best captured by overweighting cyclical sectors and small caps. **We are reluctant to overweight EM equities despite their higher beta**. The growth outperformance of EM versus Developed Market (DM) economies, as proxied by the difference between EM and DM IP oya growth, is set to narrow dramatically from a record high of 18.5% in December 2009 to 2.6% in December 2010, based on our economists' forecasts. This makes it more likely that EM equities will underperform DM equities this year.

A simple regression model of the relative performance of MSCI EM versus MSCI World on world equities (MSCI World) and on the difference between EM versus DM IP growth versus its historical mean produced a high 60% R² based on annual total return data since 1992:

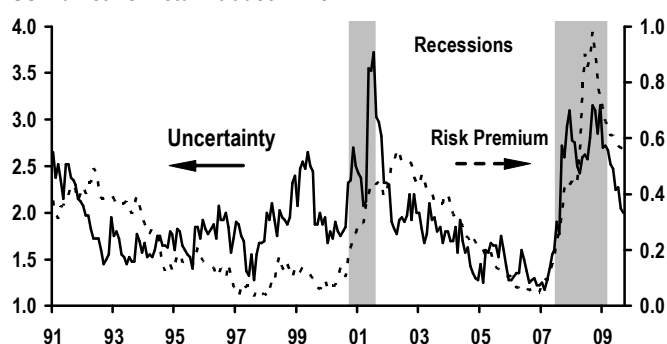
$$MSCIEM - MSCIWorld = 0.15 \times MSCIWorld + 4.7 \times (EMIP oya - DMIP oya - 4.7\%)$$

Plugging in our 2.6% projection for the gap between EM and DM IP growth for 2010, which is below its historical 4.7% mean, and assuming a 15% return for world equities, points to MSCI EM underperforming MSCI World by close

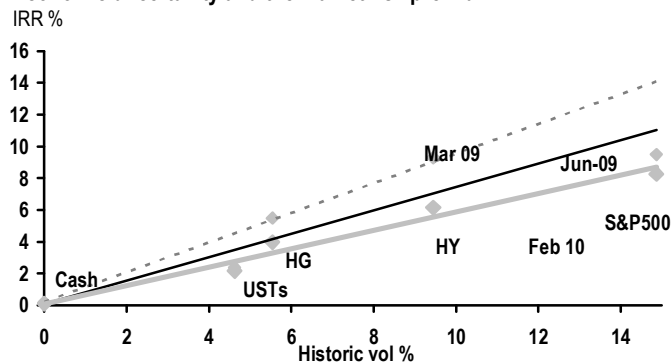
2010 global GDP growth forecasts: J.P. Morgan versus consensus



US market risk-return tradeoff line



Economic uncertainty and the market risk premium



to 7.5%-pts this year. Already this year EM equities have fallen by 2%-pts more than DM equities; the model suggests a further 5.5%-pt underperformance.

Credit

Credit markets rallied across the board last week. We see the spread tightening trend restarting once again and stay overweight credit, especially higher-yielding debt such as high yield, super-senior CMBS, and EM corporates.

Our **US HG credit survey** shows that investors are more bullish HG spreads compared to a month ago, with a net

50% of investors seeing spreads tighter over the next month versus only 22% in February. But investors have yet to re-balance their holdings, as only 10% of investors are currently overweight versus the recent peak of 23%. Hence, demand for US HG in the coming month should be strong, as investors move their positions in line with their more bullish views. Credit fundamentals are also steadily improving with US nonfinancials continuing to increase cash holdings and reduce leverage (debt/EBITDA) in 4Q, while profit margins improved. Stay long US HG credit.

We are also **long in US high yield** as fundamentals are supportive and spreads are expected to tighten another 150bp by year-end. The upswing of the upgrade-to-downgrade ratio of HY bonds, a sign of credit quality that correlates well with spread performance, is improving. The default rate for HY bonds has also fallen from 8.1% in January to 7.4% in February, a strong decline of 0.7%. This is expected to fall toward our year-end target of 2%.

In the past two weeks, high yield mutual funds have started to see inflows once again. As discussed in our latest *GMOS* publication, mutual fund flows provide a useful signal to trade US corporate credit. The recent inflows to HY funds suggest overweighting both US HG and HY credit. A simple strategy that goes long corporate credit when the cumulative two-week HY fund flow is positive has a good information ratio of 0.8 (see Credit section of the *GMOS*, March 3).

Foreign exchange

The year 2010 has been one of unusually broad **dollar** strength, but two months into that move, this rally looks set to end, giving way to a **range**. The issues that drove dollar strength in 1Q—global slowdown, sovereign risk, China tightening—have not been resolved. But progress on some has been substantial (Greece), and the technical backdrop has turned dramatically (with USD positions now very long) such that the dollar is unlikely to make new highs trade-weighted or pairwise this spring. Accordingly, we **close USD longs versus commodity currencies, euro, and sterling**. We now have no directional USD risk. Focus instead on the cross rates, where the relative growth story is more compelling. Within the commodity bloc, stay long CAD versus AUD and NZD, and add a long versus GBP. Within Europe, stay short GBP versus EUR and CHF.

Ten-year Government bond yields

	Current	Mar 10	Jun 10	Sep 10	Dec 10
United States	3.68	3.90	4.10	4.25	4.50
Euro area	3.16	3.15	3.30	3.45	3.60
United Kingdom	4.06	4.25	4.40	4.45	4.55
Japan	1.31	1.30	1.40	1.50	1.55
GBI-EM	7.15				7.90

Credit markets

	Current	YTD Return
US high grade (bp over UST)	162	2.4%
Euro high grade (bp over Euro gov)	153	1.9%
USD high yield (bp vs. UST)	666	2.5%
Euro high yield (bp over Euro gov)	680	4.5%
EMBIG (bp vs. UST)	288	2.5%
EM Corporates (bp vs. UST)	342	3.1%

Foreign exchange

	Current	Mar 10	Jun 10	Sep 10	Dec 10
EUR/USD	1.36	1.45	1.48	1.45	1.40
USD/JPY	90.3	85	82	85	89
GBP/USD	1.51	1.54	1.59	1.58	1.56

Commodities - quarterly average

	Current	10Q1	10Q2	10Q3	10Q4
WTI (\$/bbl)	82	77	82	85	90
Gold (\$/oz)	1132	1250	1400	1300	1200
Copper(\$/m ton)	7366	7350	8000	6800	6250
Corn (\$/Bu)	3.76	3.85	4.05	3.95	3.90

Source: J.P. Morgan, Bloomberg, Datastream

Commodities

On a medium-term basis, we are also bullish crude oil and recommend buying more on dips. **Crude oil** has traded in a tight range between \$77 and \$82 in the past two weeks, as the market remains torn between falling floating storage and lower demand as refineries move into seasonal maintenance. We also see weaker Chinese refinery demand whenever prices move above \$80 due to government-mandated refinery margin policy.

We expect crude prices to rise over the course of the year, moving to \$90 by 4Q. Near term, crude is more likely to range trade, tightening only later in 2Q. We also expect the curve to turn backwardated in coming months. There is an agreement in the market that both crude and distillate floating inventories are in a declining trend, but the curve is surprisingly flat given the likely offshore inventories still to be offloaded.

Global Economic Outlook Summary

	Real GDP			Real GDP							Consumer prices			
	% over a year ago			% over previous period, saar							% over a year ago			
	2009	2010	2011	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	4Q09	2Q10	4Q10	2Q11
The Americas														
United States	-2.4	3.4 ↓	3.1	2.2	5.9	2.5 ↓	4.0	4.0	3.5	2.5	1.5	2.2	1.1	0.9
Canada	-2.6 ↓	3.1 ↑	3.4	0.9 ↑	5.0 ↑	4.5	2.5	3.5	4.0	4.0	0.8	1.4	1.7	1.9
Latin America	-3.0	4.6	3.8 ↑	5.8 ↑	6.4 ↓	4.1 ↓	4.7 ↑	4.4 ↑	3.4 ↑	3.0 ↓	5.3	6.7	7.5	7.0 ↑
Argentina	-4.0	4.5	3.0	0.2	1.0	8.0	8.0	3.0	3.0	2.0	7.1	8.0	10.0	10.0
Brazil	0.1	6.2	4.0	5.1	7.7	6.3	5.0	5.1	4.0	3.8	4.2	4.5	4.7	4.7
Chile	-1.7	5.5 ↑	5.5 ↑	4.6	8.0	-6.0 ↓	8.0 ↑	22.0 ↑	18.0 ↑	-2.0 ↓	-3.0	3.3 ↑	4.1 ↑	3.8 ↑
Colombia	0.3	3.0	4.1	0.9	3.7	3.0	3.5	3.7	4.0	4.2	2.4	2.1	3.7	2.9
Ecuador	-1.0	2.0	3.0	1.1	-2.0	2.0	3.5	4.0	4.5	3.0	3.9	4.2	4.5	3.8
Mexico	-6.5	4.5	3.5	10.4	8.4	4.1	4.9	0.5	1.4	3.0	4.0	4.4	5.1	4.5
Peru	0.9 ↓	5.5	6.0	10.0 ↑	11.5 ↓	3.0	3.5	4.0	5.0	6.0	0.4	1.0	2.0	2.2
Venezuela	-3.3 ↓	-1.5	2.5	-7.4 ↑	-4.6 ↓	-4.0	-3.0 ↑	15.0	1.0	1.5	28.1	41.4	43.2	39.1
Asia/Pacific														
Japan	-5.1	2.3	1.9	0.0	4.6	1.8	1.5	2.0	2.2	1.8	-2.0	-1.9	-1.2	-0.1
Australia	1.3 ↑	3.1 ↑	3.6 ↑	1.1 ↑	3.7 ↑	3.0 ↓	3.3 ↓	3.8 ↓	3.9	3.1	2.1 ↓	2.5 ↓	2.6	3.0
New Zealand	-1.6	2.5	3.2	0.8	2.2	3.6	3.0	2.9	2.6	2.9	2.0	1.8	1.8	2.3
Asia ex Japan	4.6 ↑	7.9 ↑	7.2	10.7 ↑	7.2 ↓	7.3 ↓	7.1	7.1	6.8	7.0	2.9 ↑	4.4 ↓	3.8	3.2
China	8.6	10.0	9.4	10.3	10.0	9.8	9.4	9.5	9.0	9.1	0.7	3.2	3.1	2.4
Hong Kong	-2.7	5.3	4.2	1.6	9.5	4.5	4.3	4.0	3.8	4.2	1.3	2.4	2.3	1.9
India	7.2 ↑	8.0 ↑	8.3	15.0 ↑	-2.0 ↓	10.4	8.1	7.0	8.7	7.9	13.3 ↑	11.9	6.2	5.5
Indonesia	4.5	5.5	6.6	5.8	9.6	6.0	4.0	8.5	5.0	6.0	2.6	5.3	6.3	4.9
Korea	0.2	5.3	4.1	13.6	0.7	3.6	4.2	4.2	3.5	4.0	2.4	3.1	3.6	3.4
Malaysia	-1.7	6.8 ↑	4.8 ↓	10.4	15.4	1.2 ↓	4.9 ↓	4.9 ↓	4.9 ↓	4.9	-0.2	1.7	2.4	2.4
Philippines	0.9	4.5	4.3	3.1	3.5	6.0	5.0	3.5	4.0	4.5	3.0	5.0 ↑	5.2 ↑	4.9
Singapore	-2.0	6.8	4.8	11.5	-2.8	11.2	7.0	4.9	4.9	4.1	-0.3	2.0 ↓	2.6 ↓	2.1
Taiwan	-1.9	7.0	4.8	10.2	18.0	1.2	3.5	3.8	4.0	5.0	-1.3	0.9	2.0	1.8
Thailand	-2.3	6.5	4.0	6.9	15.3	2.8	5.3	3.6	3.6	4.1	1.9	5.5	4.4	3.0
Africa/Middle East														
Israel	0.5	3.0	4.5	3.0	4.4	3.0	3.5	3.5	4.0	4.0	3.6	3.2	3.0	3.1
South Africa	-1.8	3.0	3.5	0.9	3.2	4.4	4.3	4.3	4.9	3.6	6.0	4.3	5.3	5.8
Europe														
Euro area	-4.0	1.6	2.1	1.7	0.5 ↑	1.5	3.0	2.3	2.0	2.0	0.4	1.3	1.3	0.8
Germany	-4.9	1.7	2.1	2.9	0.0	1.0	3.0	2.0	2.0	2.0	0.3	0.9	1.3	1.3
France	-2.2	2.0	2.2	0.7	2.4	1.5	3.0	2.0	2.5	2.0	0.4	1.4	0.9	0.9
Italy	-4.9	1.1	1.7	2.4	-0.8	1.0	2.5	1.5	2.0	1.5	0.7	1.1	1.1	1.1
Norway	-1.4	2.3	2.8	1.4	1.3	3.0	3.0	3.0	3.0	2.8	1.4	1.9	1.2	1.2
Sweden	-4.7 ↓	1.6 ↓	3.0	-0.4 ↓	-2.2 ↓	3.5	3.5	3.0	3.0	3.0	-0.4	1.1	0.9	1.8
Switzerland	-1.5	2.5 ↑	2.8	2.0 ↑	3.0 ↑	2.5	2.8	3.0	3.0	2.8	-0.2 ↓	0.8 ↓	0.7	0.8
United Kingdom	-5.0	1.2	3.1	-1.2	1.1	1.2	2.5	2.8	3.5	2.8	2.1	2.2	1.4	1.9
Emerging Europe	-5.1	3.9	4.7	4.4 ↑	5.6 ↑	3.7	3.6	3.3	3.9	4.4	6.2	5.6	5.5	4.9
Bulgaria	-5.1	-1.5	4.5	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	-4.3	2.0	4.0	3.3	-2.4	2.0	3.0	2.5	2.5	3.5	0.4	1.3	3.0	3.0
Hungary	-6.3	0.5	4.0	-4.7	-1.6	1.5	2.5	2.0	2.0	4.0	5.2	4.3	3.0	2.8
Poland	1.7	3.2	4.2	2.4 ↑	4.9 ↑	3.0	4.0	3.0	3.0	4.0	3.3	2.0	2.5	2.5
Romania	-7.1 ↑	1.5	4.0	...	...	...	...	...	...	...	4.6	4.5	5.3	4.5
Russia	-7.9	5.5	5.0	7.9	10.5	5.0	4.0	4.0	5.0	5.0	9.2	6.7	7.2	6.9
Turkey	-5.3	4.3	5.5	...	...	...	...	...	...	...	5.7	9.2	6.6	4.6
Global	-2.5	3.3	3.3	2.8 ↑	4.2	2.9 ↓	3.7	3.6	3.4	3.0	1.3	2.1	1.7	1.6
Developed markets	-3.4	2.5 ↓	2.6	1.4	3.6 ↑	2.1 ↓	3.1	3.0 ↓	2.9	2.3	0.6	1.3	0.9	0.9
Emerging markets	0.9	6.3 ↑	5.8	8.1 ↑	6.6 ↓	5.8 ↓	5.8 ↑	5.7 ↑	5.4 ↑	5.4 ↓	4.0 ↑	5.1	4.9	4.3
Memo:														
Global — PPP weighted	-0.8	4.5	4.4	4.4	4.8	3.8	4.4	4.3	4.1	3.8	2.4	3.2	2.8	2.5

Global Central Bank Watch

	Official interest rate	Change from			Forecast						
		Current	Aug '07 (bp)	Last change	Next meeting	next change	Mar 10	Jun 10	Sep 10	Dec 10	Jun 11
Global	GDP-weighted average	1.30	-337				1.30	1.35	1.44	1.51	1.98
excluding US	GDP-weighted average	1.85	-251				1.86	1.92	2.05	2.16	2.68
Developed	GDP-weighted average	0.51	-361				0.51	0.51	0.55	0.59	1.04
Emerging	GDP-weighted average	4.46	-241				4.47	4.67	4.98	5.19	5.74
Latin America	GDP-weighted average	5.72	-321				5.91	6.41	7.05	7.31	8.26
CEEMEA	GDP-weighted average	4.41	-245				4.30	4.16	4.41	4.66	5.19
EM Asia	GDP-weighted average	4.00	-209				4.00	4.22	4.43	4.61	5.01
The Americas	GDP-weighted average	0.75	-484				0.77	0.82	0.93	0.99	1.43
United States	Federal funds rate	0.125	-512.5	16 Dec 08 (-87.5bp)	16 Mar 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)	20 Apr 10	20 Jul 10 (+25bp)	0.25	0.25	0.75	1.25	1.75
Brazil	SELIC overnight rate	8.75	-325	22 Jul 09 (-50bp)	17 Mar 10	17 Mar 10 (+50bp)	9.25	10.25	11.25	11.75	11.75
Mexico	Repo rate	4.50	-270	17 Jul 09 (-25bp)	19 Mar 10	Jun 10 (+25bp)	4.50	4.75	5.25	5.25	6.75
Chile	Discount rate	0.50	-450	9 Jul 09 (-25bp)	18 Mar 10	Nov 10 (+25bp)	0.50	0.50	0.50	1.00	2.50
Colombia	Repo rate	3.50	-550	23 Nov 09 (-50bp)	26 Mar 10	1Q 11 (+50bp)	3.50	3.50	3.50	3.50	5.50
Peru	Reference rate	1.25	-325	6 Aug 09 (-75bp)	<u>11 Mar 10</u>	Jul 10 (+25bp)	1.25	1.25	2.00	2.75	4.25
Europe/Africa	GDP-weighted average	1.31	-321				1.31	1.29	1.33	1.41	2.08
Euro area	Refi rate	1.00	-300	7 May 09 (-25bp)	8 Apr 10	1Q 11 (+25bp)	1.00	1.00	1.00	1.00	1.75
United Kingdom	Repo rate	0.50	-500	5 Mar 09 (-50bp)	8 Apr 10	Nov 10 (+25bp)	0.50	0.50	0.50	0.75	1.25
Sweden	Repo rate	0.25	-325	2 Jul 09 (-25bp)	20 Apr 10	1Q 11 (+25bp)	0.25	0.25	0.25	0.25	0.75
Norway	Deposit rate	1.75	-275	16 Dec 09 (+25bp)	24 Mar 10	24 Mar 10 (+25bp)	2.00	2.25	2.50	2.50	3.25
Czech Republic	2-week repo rate	1.00	-175	16 Dec 09 (-25bp)	25 Mar 10	23 Sep 10 (+25bp)	1.00	1.00	1.25	1.75	2.75
Hungary	2-week deposit rate	5.75	-200	22 Feb 10 (-25bp)	30 Mar 10	30 Mar 10 (-25bp)	5.50	5.50	5.50	5.50	5.50
Israel	Base rate	1.25	-275	28 Dec 09 (+25bp)	28 Mar 10	2Q 10 (+25bp)	1.25	1.75	2.25	2.75	3.75
Poland	7-day intervention rate	3.50	-100	24 Jun 09 (-25bp)	31 Mar 10	3Q 10 (+25bp)	3.50	3.50	3.75	4.00	5.00
Romania	Base rate	7.00	0	3 Feb 10 (-50bp)	29 Mar 10	29 Mar 10 (-25bp)	6.75	6.25	6.00	6.00	7.00
Russia	1-week deposit rate	3.75	75	19 Feb 10 (-25bp)	Mar 10	Mar 10 (-25bp)	3.50	3.00	3.00	3.00	3.50
South Africa	Repo rate	7.00	-250	13 Aug 09 (-50bp)	25 Mar 10	4Q 10 (+50bp)	7.00	7.00	7.00	7.50	8.50
Switzerland	3-month Swiss Libor	0.25	-225	12 Mar 09 (-25bp)	<u>11 Mar 10</u>	Sep 10 (+25bp)	0.25	0.25	0.50	0.75	1.25
Turkey	Overnight borrowing rate	6.50	-1100	19 Nov 09 (-25bp)	18 Mar 10	3Q 10 (+50bp)	6.50	6.50	7.50	8.00	7.50
Asia/Pacific	GDP-weighted average	2.11	-133				2.11	2.22	2.35	2.45	2.67
Australia	Cash rate	4.00	-225	2 Mar 10 (+25bp)	6 Apr 10	4 May 10 (+25bp)	4.00	4.25	4.75	5.00	5.50
New Zealand	Cash rate	2.50	-550	30 Apr 09 (-50bp)	<u>11 Mar 10</u>	29 Jul 10 (+50bp)	2.50	2.50	3.50	4.00	4.75
Japan	Overnight call rate	0.10	-43	19 Dec 08 (-20bp)	17 Mar 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)	17 Mar 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)	1Q 10	2Q 10 (+27bp)	5.31	5.58	5.85	6.12	6.39
Korea	Base rate	2.00	-250	12 Feb 09 (-50bp)	<u>11 Mar 10</u>	3Q 10 (+25bp)	2.00	2.00	2.25	2.50	3.00
Indonesia	BI rate	6.50	-200	5 Aug 09 (-25bp)	6 Apr 10	4Q 11 (-25bp)	6.50	6.50	6.50	6.50	6.50
India	Repo rate	4.75	-300	21 Apr 09 (-25bp)	Apr 10	Apr 10 (+25bp)	4.75	5.25	5.50	5.50	6.50
Malaysia	Overnight policy rate	2.25	-125	4 Mar 10 (+25bp)	13 May 10	13 May 10 (+25bp)	2.25	2.50	2.75	2.75	2.75
Philippines	Reverse repo rate	4.00	-350	9 Jul 09 (-25bp)	<u>11 Mar 10</u>	2Q 10 (+25bp)	4.00	4.25	4.75	5.00	5.00
Thailand	1-day repo rate	1.25	-200	8 Apr 09 (-25bp)	<u>10 Mar 10</u>	2 Jun 10 (+25bp)	1.25	1.50	1.50	1.75	2.25
Taiwan	Official discount rate	1.25	-188	18 Feb 09 (-25bp)	1Q 10	4Q 10 (+12.5bp)	1.25	1.25	1.25	1.375	1.625

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

Economic forecasts - Australia

Australia: economic projections <i>percentage change over previous period, seasonally adjusted annual rates, un</i>														
				2009			2010				2011			
	2009	2010	2011	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Chain volume GDP	1.3	3.1	3.6	2.9	1.1	3.7	3.0	3.3	3.8	3.9	3.1	4.2	4.2	1.8
Private consumption	2.2	1.7	2.1	3.5	3.0	2.6	1.2	0.8	0.4	1.2	3.2	2.8	2.4	2.0
Construction investment	-0.3	2.9	4.6	-2.8	3.4	1.7	3.6	3.4	4.5	3.5	4.3	5.1	6.0	6.2
Equipment investment	-3.4	22.1	9.3	4.3	-11.0	51.2	32.6	22.5	13.0	17.6	5.1	3.4	6.4	8.6
Public investment	3.8	21.3	10.7	18.3	28.3	47.7	17.0	9.5	15.1	11.2	7.4	14.0	7.4	11.8
Government consumption	2.9	3.7	1.7	3.6	5.7	7.2	3.9	0.1	3.9	0.1	0.1	3.8	3.8	0.4
Exports of goods & services	0.5	3.7	4.6	3.3	-9.1	7.0	6.6	4.9	3.2	7.4	4.1	4.1	4.1	4.1
Imports of goods & services	-7.7	11.6	4.1	3.0	18.5	34.6	8.2	4.1	2.0	4.1	4.1	4.1	2.0	12.6
Contributions to GDP growth:														
Inventories	-0.5	-1.9	-0.1	1.1	2.6	0.4	-8.9	-0.2	-0.1	-0.1	-0.2	0.0	-0.3	-0.1
Net trade	1.8	-1.7	0.0	0.1	-5.2	-4.9	-0.5	0.1	0.2	0.5	-0.1	-0.1	0.3	-1.8
GDP deflator (%oya)	0.4	1.8	2.4	0.3	-2.0	-1.4	0.1	2.9	2.4	2.0	2.2	2.4	2.5	2.5
Consumer prices (%oya)	1.8	2.5	2.8	1.5	1.3	2.1	2.5	2.5	2.4	2.6	2.7	3.0	2.8	2.6
Producer prices (%oya)	-5.4	-1.4	3.5	-6.4	-7.2	-6.8	-3.1	-1.6	-1.9	1.0	2.5	3.5	4.0	4.0
Trade balance (A\$ bil, sa)	-6.7	-19.4	-23.4	-0.9	-4.3	-5.7	-5.2	-4.4	-4.9	-4.9	-4.6	-5.8	-6.2	-6.8
Current account (A\$ bil, sa)	-67.0	-70.0	-79.0	-13.1	-14.7	-17.5	-17.6	-16.8	-17.5	-18.0	-18.2	-19.6	-20.2	-21.1
as % of GDP	-6.2	-5.3	-5.6	-4.2	-4.7	-5.4	-5.4	-5.1	-5.3	-5.3	-5.3	-5.6	-5.7	-5.9
3m eurodeposit rate (%)*	6.0	4.9	5.4	3.5	3.4	4.1	4.2	4.8	5.0	5.4	5.4	5.4	5.4	5.4
10-year bond yield (%)*	5.6	5.7	6.0	5.5	5.1	5.8	5.5	5.8	5.8	5.9	5.9	6.0	6.0	6.0
US\$/A\$*	0.75	0.98	0.92	0.82	0.88	0.91	0.94	1.00	0.99	0.98	0.96	0.95	0.90	0.85
Commonwealth budget (FY, A\$ bil)	-27.0	-43.0	-29.0											
as % of GDP	-2.1	-3.2	-2.1											
Unemployment rate	5.6	5.5	5.5	5.7	5.7	5.6	5.4	5.6	5.7	5.7	5.5	5.4	5.4	5.3
Industrial production	-7.8	3.3	1.5	5.2	-5.5	21.8	1.0	0.0	-1.0	-2.0	0.0	1.0	2.0	3.0

*All financial variables are period averages

Australia - summary of main macro views

- The Australian economy powered out of the global downturn largely unscathed. GDP growth was a solid 0.9%q/q in Q4, although the government's stimulus fingerprints were obvious. Growth will soften near-term.
- **Business investment** will be broadly unchanged at elevated levels in the year to June now that firms have upgraded their spending plans. Spending probably will rise close to 20% in 2010-11, with mining leading the way.
- On **housing**, with the expanded first home owners' grant now having expired and price caps on the basic grant in place, house price growth should cool, particularly at the low and middle-end of the price spectrum.
- The **consumer** has remained remarkably resilient in the absence of further fiscal support from the government. Consumer confidence quickly returned to pre-crisis highs, but has fallen in recent months in the wake of the RBA's rate hikes.
- **Export volumes** have held up owing mainly to firm demand from Asia, but the terms of trade has tumbled. This looks set to reverse, though, in 2010 thanks mainly to higher bulk commodity prices.
- The **RBA** was the first central bank in the G20 to tighten monetary policy, with officials anxious about the lack of spare capacity. We expect another 25bp hike in May, and a cash rate of 5% by the end of the year.
- Having front-loaded the **policy support**, the government is winding back the fiscal stimulus. With an election looming, though, the temptation will be to reverse course, particularly if the polls continue to tighten.

Economic forecasts - New Zealand

New Zealand: economic projections <i>percentage change over previous period, seas. adjusted annual rates, unless stated</i>														
	2009			2010				2011						
	2009	2010	2011	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real GDP (1995-96 prices)	-1.6	2.5	3.2	0.9	0.8	2.2	3.6	3.0	2.9	2.6	2.9	4.6	3.2	2.6
Private consumption	-0.9	0.8	0.6	1.5	3.0	0.2	0.4	0.8	0.2	0.6	0.7	0.5	0.9	0.6
Fixed Investment	-12.9	-1.6	3.9	-2.8	-6.0	-7.7	-2.0	3.7	3.0	4.3	2.2	4.1	6.0	7.4
Residential construction	-20.4	-3.7	4.3	-8.7	-18.6	-6.0	-2.0	2.0	3.2	6.0	3.2	4.8	6.0	4.0
Other fixed investment	-11.4	-1.3	3.9	-1.6	-3	-8.0	-2.0	4.0	3.0	4.0	2.0	4.0	6.0	8.0
Inventory change (NZ\$ bil, saar)	-2.6	-0.6	0.0	-1.0	-0.7	-0.6	-0.3	-0.2	-0.1	0.1	0.0	0.0	0.0	0.0
Government spending	1.1	0.5	0.6	-5.8	1.5	0.9	0.8	0.8	0.8	0.8	0.4	0.8	0.0	0.2
Exports of goods & services	0.9	8.4	11.0	20.0	0.1	11.0	8.0	10.0	8.0	5.0	12.0	16.0	15.0	10.0
Imports of goods & services	-16.4	5.9	6.8	-9.3	2.7	7.0	8.0	9.0	6.0	7.0	5.0	6.5	12.0	4.0
Contributions to GDP growth:														
Domestic final sales	-5.2	0.2	1.3	0.8	-1.6	-0.8	-0.1	1.4	1.0	1.4	1.0	1.4	2.0	0.4
Inventories	-3.0	1.6	0.4	-8.6	3.2	1.8	3.7	1.2	1.2	1.8	-0.5	-0.1	0.0	0.0
Net trade	6.6	0.8	1.5	9.4	-0.8	1.2	0.0	0.3	0.7	-0.6	2.3	3.2	1.2	2.2
GDP deflator (%oya)	2.1	2.0	2.2	2.0	2.9	0.9	0.7	2.0	2.6	2.8	2.8	2.4	1.9	1.6
Consumer prices	2.1	2.3	2.4	2.3	5.3	-0.7	2.2	2.1	1.9	2.8	2.7	2.6	2.1	1.9
%oya	2.1	2.0	2.4	1.9	1.7	2.0	2.2	2.2	1.4	2.3	2.4	2.5	2.6	2.3
Trade balance (NZ\$ bil, sa)	1.3	-6.3	-8.5	0.8	0.7	-1.1	-1.4	-1.5	-1.7	-1.7	-1.8	-2.0	-2.3	-2.4
Current account (NZ\$ bil, sa)	-3.1	-6.7	-13.7	-0.4	0.3	-0.9	-1.2	-1.2	-2.0	-2.3	-2.7	-5.2	-2.9	-2.9
as % of GDP	-1.7	-4.3	-5.8	-0.9	0.8	-2.0	-2.6	-4.2	-4.9	-5.5	-6.0	-5.8	-5.7	-5.8
Yield on 90-day bank bill (%)*	3.0	3.6	4.5	2.8	2.8	2.8	2.7	3.3	4.0	4.4	4.5	4.5	4.5	4.5
10-year bond yield (%)*	5.5	5.9	6.2	5.7	5.7	5.9	5.7	6.0	6.0	6.1	6.1	6.2	6.2	6.2
US\$/NZ\$*	0.64	0.75	0.70	0.60	0.68	0.73	0.73	0.76	0.75	0.74	0.72	0.70	0.70	0.68
Commonwealth budget (NZ\$ bil)	-4.0	-7.2	-7.1											
as % of GDP	-2.2	-3.8	-3.6											
Unemployment rate	6.1	7.3	6.9	6.0	6.5	7.3	7.2	7.4	7.3	7.2	7.1	7.0	6.9	6.7

*All financial variables are period averages

New Zealand - summary of main macro views

- The **New Zealand economy expanded a mere 0.2%q/q in 3Q**, the same rate as in the previous three months. This marked the second straight quarter of expansion following five quarters of GDP declines.
- **Business confidence** has improved markedly. This mainly owes to continued improvement in economic conditions in Australia and New Zealand's other major trading partners in Asia.
- Even though firms are becoming more upbeat, **investment** will remain a drag on GDP growth this year; this, of course, weigh on the improvement in the labour market.
- The **unemployment** rate probably peaked in 4Q, however. Hiring intentions are picking up, and as employment growth accelerates, wage growth should follow suit.
- **The RBNZ will begin tightening policy in July.** Waiting for hard evidence that the economic recovery underway is sustainable, however, means that the RBNZ will have to tighten more aggressively. The first move will be a 50bp hike.
- **Inflation** fell in the final three months of 2009, with headline CPI slipping 0.2%q/q. Medium term inflation pressures are, however, a concern, given diminishing excess capacity and firms' intentions to raise domestic prices.

Australia and New Zealand economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
8 Mar New Zealand: QVNZ house prices Feb Manufacturing activity (10:45 am) 4Q	9 Mar Australia: NAB bus. Confidence (11: 30 am) Feb <u>15%<i>bal.sa</i></u> ANZ job ads Feb <u>-3.0%<i>m/m.sa</i></u>	10 Mar Australia: Westpac consumer confidence (10: 30 am) Mar <u>-3.5%<i>m/m.sa</i></u> Housing finance approvals Jan <u>3.0%<i>m/m.sa</i></u> New Zealand: Terms of trade index (10:45 am) 4Q <u>0.6%<i>q/q.sa</i></u>	11 Mar Australia: Unemployment rate (11:00 am) Feb <u>5.4%<i>.sa</i></u> New Zealand: Business NZ PMI (10:30 pm) Feb RBNZ official cash rate Mar <u>No change expected</u>	12 Mar New Zealand: Retail sales (10:45 am) Jan <u>0.2%<i>m/m.sa</i></u>
15 Mar	16 Mar	17 Mar Australia: Dwelling starts 4Q Westpac leading index Jan	18 Mar	19 Mar New Zealand: Visitor arrivals (10:45 am) Feb Credit card spending (2:00 pm) Feb
22 Mar Australia: New motor vehicle sales (10: 30 am) Feb	23 Mar	24 Mar	25 Mar New Zealand: GDP (10:45 am) 4Q	26 Mar New Zealand: Trade balance (10:45 am) Feb
29 Mar	30 Mar New Zealand: Building permits (10:45 am) Feb	31 Mar Australia: Building approvals (11:30 am) Feb Retail sales (11:30am) Feb New Zealand: NBNZ business confidence (2: 00 pm) Mar	1 Apr	2 Apr <i>Holiday Australia, New Zealand</i>

Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
8 - 12 March	8 March	9 March	10 March	11 March	12 March
China • M2 (Feb) Japan • Cabinet Office private consumption (Jan)	Germany • IP (Jan) Japan • Econ watcher surv (Feb) Taiwan • Trade balance (Feb) Turkey • IP (Jan)	United Kingdom • Trade balance (Jan) United States • JOLTS (Jan)	China • Trade balance (Feb) Euro area • Trichet speech Germany • CPI final (Feb) • Foreign trade (Jan) Japan • Machinery orders (Jan) Norway • CPI (Feb) Thailand • BoT mtg: No Chg United States • Wholesale trade (Jan)	Brazil • GDP (4Q), Retail (Jan) China: CPI, FAI, IP, Retail France: Employ final (4Q) Japan: GDP 2nd est (4Q) Sweden: CPI (Feb) United States • Flow of funds (4Q) • International trade (Jan) Central bank meetings • Korea: No Chg • New Zealand: No Chg • Peru: No Chg • Philippines: No Chg • Switzerland: No Chg	Canada • Employment (Feb) Euro area • IP (Jan) • Trichet speech Japan • IP final (Jan) Mexico • IP (Jan) United States • Bus inventories (Jan) • Consumer sent (Mar) • Retail sales (Feb)
15 - 19 March	15 March	16 March	17 March	18 March	19 March
	Euro area • Employment (4Q) Poland • CPI (Feb) Russia • IP (Feb) United States • IP (Feb) • NAHB survey (Mar) • NY Fed survey (Mar)	Euro area • HICP final (Feb) Germany • ZEW bus survey (Mar) United States • Housing starts (Feb) • Import prices (Feb) • FOMC mtg: No Chg	Brazil • COPOM mtg: +50bp Euro area • Labor costs (4Q) Japan • BoJ mtg: No Chg United Kingdom • Labor mkt report (Feb) • MPC minutes United States • PPI (Feb)	Chile • BCCh mtg: No Chg Euro area • Foreign trade (Jan) Japan • MoF bus outlook (1Q) • Reuters Tankan (Mar) Turkey • CBRT mtg: No Chg United States • CPI (Feb) • Philly Fed survey (Mar)	Canada • CPI (Feb) Mexico • GDP details (4Q) • Banxico mtg: No Chg Taiwan • Export orders (Feb) United States • Bernanke speech

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