J.P.Morgan

Australia and New Zealand - Weekly Prospects

Summary

- And the winner is ….. nobody! With three quarters of the vote counted, voters in Saturday's Federal election look to have delivered the first hung Parliament in **Australia** since 1940. Neither of the two major parties has won the "magic number" of 76 seats needed to form a majority government. A handful of independents and one Green MP, therefore, will play the roles of "king-makers" in determining which of the major parties will be asked to form a government. With the "horse-trading" only just having started between the independents and the major parties, it could be weeks before we know whether the Labor government has been "re-elected", or whether the Opposition will be able to form a government. The latter looks more likely. A hung Parliament is the worst possible outcome for financial markets, with the uncertainty (and even the possibility of a fresh election) persisting for weeks. The last Government formed in Australia after a hung Parliament lasted just over a year.
- In **New Zealand**, RBNZ Governor Bollard delivered a speech last week that will likely be the first of many aimed at talking down inflation expectations. The Governor warned against households and businesses increasing margins and wages in response to the forthcoming GST hike. He stressed that doing so would worsen inflation, via building inflation expectations, forcing the RBNZ's policy tightening hand more than otherwise would be the case. Indeed, a rise in already-elevated inflation expectations has the potential to have a lasting impact on reported inflation. This week, the 3Q inflation expectations survey is released. We think that expectations will be higher over both the one- and two-year horizons, having spiked to 2.9%oya and 2.8%, respectively, in 2Q, at the top of the RBNZ'S target range.
- Three months ago, our **global** economic forecast called for a moderate slowing in 2H growth as global manufacturing activity came off the boil. The forecast has since undergone a series of revisions that reflects accumulating evidence that the downshift has broader sources. There has been a widespread softening in consumer spending gains. In addition, our global PMI surveys have failed to show the lift in service industries expected to offset the slowing in manufacturing. Notably, there have been growth disappointments in each of the three largest economies in the world. In China this disappointment has been modest; in the US and Japan, growth momentum has turned decisively. The significant downward revision taken to these two countries lowers our forecast of 2H10 global GDP gains to a sub-trend pace.
- A key issue is whether sub-par growth will create a **negative feedback loop**—in the US and across the globe. Thus far, the deterioration in financial markets and private sector sentiment has been modest and the risk that downward momentum feeds on itself and produces a global recession seems small. However, the odds have risen for the US, where we now place the likelihood of a new phase of economic contraction at close to 30%. Our assessment that a US double-dip remains unlikely rests on the observation that cyclically sensitive components of demand that tend to drive the economy into contraction sit at levels consistent with depressed behaviour and are not likely to break sharply lower. We see the risk of a significant credit shock as similarly low due to the financial deleveraging that has already taken place.

This week's highlight

Given Australia's election non-result, the highlight will be the horse-trading between the major parties and the independents to see which party can form a government. We probably will not get a resolution this week.

August 23, 2010

Contents

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Data and event previews - Australia and New Zealand

Date	Time [a]	Data/event	Forecast: JPMorgan	Forecast: Consensus [b]	*Previous*
Tuesday, August 24	1.00pm	RBNZ 2yr inflation expectation (%, 3Q)	**3.0**	na	*2.8*
Wednesday, August 25	11.30am	Aust. construction work done (%q/q, 2Q)	**3.0**	3.0	*1.9*
Thursday, August 26	10.00am	Aust. Conference Board Leading Index (%m/m, Jun.)	**na**	na	*0.3*
Thursday, August 26	11.30am	Aust. private capital expenditure (%q/q, 2Q)	**1.5**	2.3	*-0.2*

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

Australia

Construction work done (%q/q, 2Q) - We expect the composition of construction to have continued shifting from public works toward private activity in 2Q. Indeed, our GDP forecasts assume that the fading profile of public spending is filled in as private capex, in particular, gathers momentum. Construction work done probably rose 3%q/q (5.7%oya), with public sector building downshifting in growth terms, as the government's intervention in the education sector fades, but with private residential building and engineering work rising in its place. Private residential completions have been soft for some time, owing to the lag that developed between building approvals and dwelling starts in 2009. This gap closed significantly in 4Q09, meaning we should be seeing the benefits of earlier robust improvements in housing market activity in coming quarters. The uncertainty surrounding the resources tax likely weighed on sentiment in that sector in 2Q, but probably was insufficient to turn up in softer construction *completions* within the quarter.

Private capital expenditure (%q/q, 2Q) - The June quarter business investment survey should confirm that firms' capital spending plans remain largely intact, after much to-ing and fro-ing over the proposed mining tax. Initially, the RSPT generated harsh opposition from mining companies, with many announcing intentions to scale back investment plans, while others put projects on hold or "under review." The Mineral Resource Rent Tax (the watered down, post "negotiation" version of the tax, announced in July) brought a quick about-face, and many projects were put back online. While the tax issue was not resolved within 2Q, the miners' threats largely related to commitments still in the planning stage, and so should not have affected the actual spend in the June quarter. We, therefore, expect capital spending will have risen 1.5%q/q in 2Q, having unexpectedly declined in the previous three months. Managers, despite being a little more downbeat than three months ago, will still plan to lift spending in the year ended June 2011. Indeed, firms probably will *boost* investment spending by 9% in the year ended June 2011; previously, the expectation was for a 14% rise. The first estimate of firms' spending plans for 2011/12 also will be released, and should show that firms intend to boost spending by 18%.

New Zealand

RBNZ 2yr inflation expectation (%, 3Q) - We expect that inflation expectations would have risen in 3Q, given a series of one-off policy changes coming into effect in 2H10. In the current quarter, changes to the ETS (July 1) have pushed prices of fuel and electricity higher. A rise in accident compensation levies for motor vehicles and a rise in insurance premia owing to changes to the taxation of insurance companies also has added upward pressure on prices. Then in 4Q, the government will increase the GST to 15% from 12.5% (October 1). Thus, we expect that two-year inflation expectations would have risen to 3% in 3Q, to the very top end of the RBNZ's target range.

Research note

Riding the lifts and lulls of Australia's fiscal stimulus

- **Stimulus hangover does not seem significant in broad consumer spending patterns or investment**
- **But spending on household goods appears to have been dragged forward, and now is tepid**
- **Impact of stimulus on home loans is more subtle due to simultaneity of monetary policy cycle and the grant**

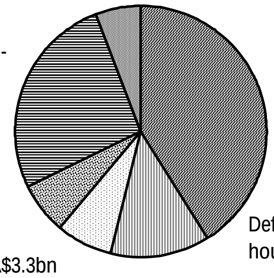
The financial crisis that began in 2H08 empowered policymakers globally to pursue coordinated, aggressive fiscal and monetary loosening. In Australia, the fiscal mechanism swung into action across a broad range of sectors. We have noted previously the influence of the federal government's public works programs in the education sector—the largest single component of the stimulus package (pie chart)—on the GDP growth profile (see "Australia's stimulus: political headaches, fiscal hangovers," *GDW*, February 5, 2010).

Here, we look at individual sectors that have been touched by other stimulus policies: retail sales (through the government's cash handouts), investment (through the investment allowance), and housing finance (through the expanded first-home buyers' grant). The aim is to determine whether activity simply has been shifted forward, or whether there is a lingering net positive for the economy. Our conclusion is that retail sales have benefited from the stimulus packages, due to positive feedback from income and sentiment, while sales of household goods (i.e., "one-off" big-ticket purchases) have suffered, due to negative feedback from heavy discounting post stimulus. Investment has been well-supported by the programs, while the effect on (total) housing finance commitments is obscured in the data by simultaneity with the monetary policy cycle.

Success turns on both peaks and troughs

The purpose of expansionary fiscal policy is to smooth out downshifts in the business cycle that would otherwise be too damaging to productive capacity and welfare. One way to measure the success of such programs is to ask how actual outcomes compare with what would have been expected in the absence of stimulus support. The latter, being a counterfactual, is unobservable, meaning any related conjecture cannot be scientifically tested, and should be interpreted with caution. However, we can use the data to construct useful reference points for how events unfolded. Here, we undertake such an exercise for retail sales, also

Selected Federal fiscal stimulus programs: October 2008 onward



Generating baseline estimates

Achieving an estimate for the baseline scenario (or counterfactual) in each sector is a three-step process:

First, we estimate a model to explain changes in the relevant variable (e.g., retail sales growth) as a function of several economic variables of interest. The model is estimated over a timeframe that leads up to—but does not include—the launch of the stimulus measures (in our case, we use 1Q97 to 2Q08). This establishes a historical framework that is free of any disturbance from the interaction of the variables of interest with the stimulus itself.

Second, we use the estimated relationship, along with the inputs we have in hand, to generate an out-of-sample prediction of the dependent variable over the crisis/stimulus period and beyond (in our case, from 3Q08 to 2Q10). Working with the historical data in this fashion is known as "ex post forecasting," and allows us to use a richer set of explanatory variables than we could if we were attempting to predict the value of some variable in the future. For example, food sales are an important component of retail sales, and should not be overly stimulus-sensitive. Using food sales in constructing our model then allows us to obtain a more rigourous baseline estimator of retail sales, while still leaving "room" for the stimulus to generate a departure from the prediction of the model.

Third, we use the projections from the model (e.g., retail sales growth) to dynamically forecast its level (e.g., quarterly retail sales), given the previous period's outcome. The specifications for each model have minor variations depending on the sector, though all include lags of the dependent variable as well as the following core variables: inflation, employment/unemployment, profits from the NAB business survey, consumer confidence, the RBA cash rate, and equity prices. If the models are well specified, the difference between the model and the actual outcomes will reflect the role of the stimulus programs.

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sales of household goods in particular, plant and machinery investment, and home loans, where the impact of the various stimulus measures should be apparent (see box on previous page for method).

The ghost of stimulus past

Government spending obviously boosts activity in the near term, but the real question is, What does the trade-off look like over time? Gauging the performance of sectors relative to an ex.-stimulus hypothetical series gives a sense of how the immediate gains of government spending are offset by the payback that follows. A common argument against fiscal intervention is that programs that induce investment, and similarly, spending on bigger-ticket consumer items, necessarily depress future activity by simply substituting finite demand over time. In this sense, testing the effectiveness of stimulus programs would be a fairly uninteresting exercise, in that the positives and negatives should approximately balance over a long enough timeline.

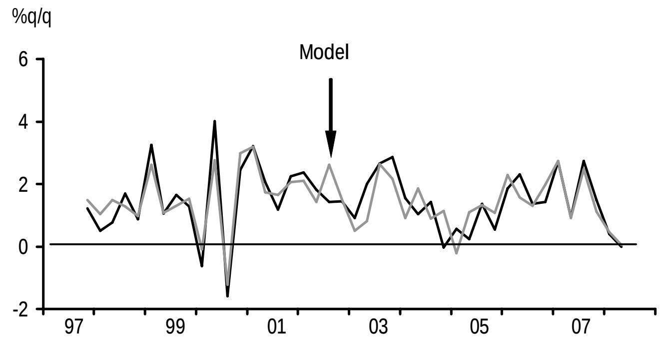
But there also is an important feedback loop in play: fiscal intervention in one sector can spill over to the wider economy, raising income and sentiment, and infecting results in the next period beyond what would be predicted by the model framework. The feedback from the stimulus, and the conditions that necessitated it, to actual outcomes is arguably the most important driver of whether the lifts and lulls balance, and is the major swing factor in our tracking exercise. We show here that this feedback can be broadly classed as positive or negative in our consumer spending and investment exercises, but there are complicating factors for home loans.

Retail sales boosted by cash handouts...

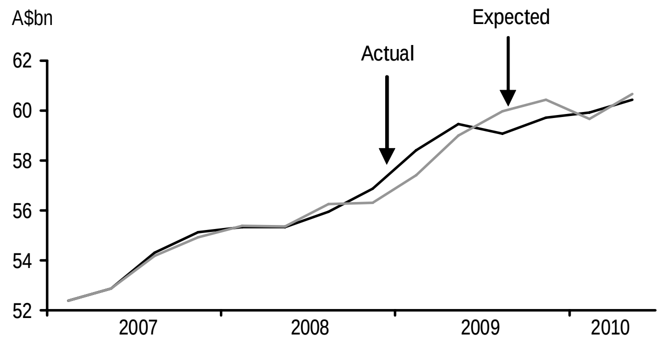
In October 2008, the government launched the A$10.4 billion "Economic Security Strategy," which included cash payments to low- and middle-income families and retirees, in December of that year. In February 2009, the expansion into the A$42 billion "Nation Building and Jobs Plan" included another round of cash payments to eligible families, singles, students, and farmers. In total, A$12.2 billion was allocated in cash handouts between 4Q08 and 2Q09.

The first chart above shows the ex post forecasting framework for growth in quarterly retail sales values. In the second chart, the implied growth rates derived from applying this framework to the data are overlaid to produce the "expected" (or baseline) retail sales numbers. Note that the actual values begin to depart from the model estimates in 4Q08, as the first round of stimulus payments were delivered. The total estimated lift from this period (i.e., until sales began to undershoot the baseline) is A$1.7 billion.

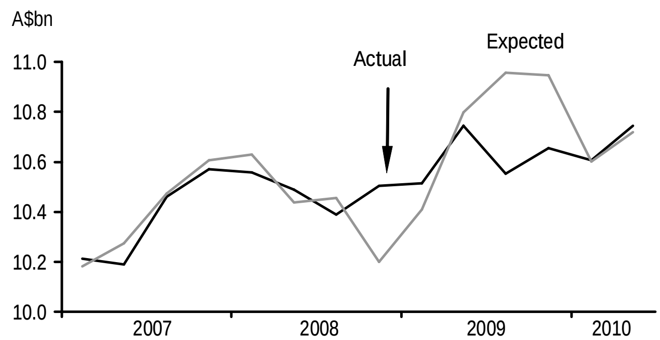
Quarterly retail sales: actual and model



Quarterly retail sales: actual and model counterfactual



Quarterly household goods sales: actual and model counterfactual



Summing the subsequent undershoots from 3Q09 onward, we estimate the lull from the earlier drag-forward of sales to be A$1.3 billion. Given the performance so far in 2010, sales appear to have returned to levels implied by the model growth rates, yielding a total net gain of A$0.4 billion.

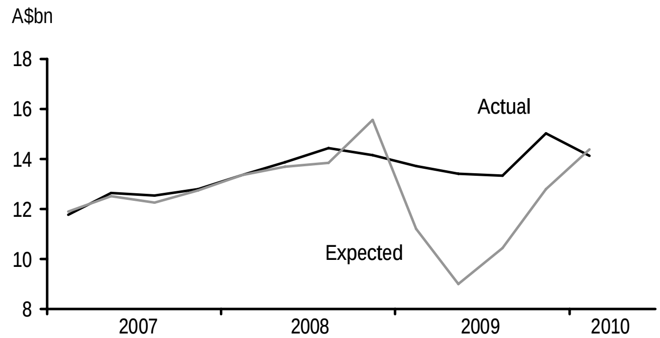
The fact that the over- and undershoot are not symmetric reflects the influence of other factors that the model parameters miss. While we should not invest too much faith in a counterfactual analysis, one possible explanation is that positive feedback effects have yielded some of the residual A$0.4 billion: the boost to sentiment and income from the initial splurge has allowed the economy to negotiate the period in which output would have been lost due to heightened risk aversion and consumer caution.

...but bigger-ticket items suffering payback

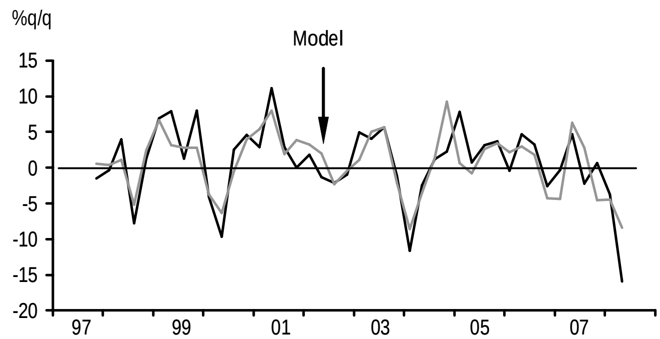
As noted earlier, the retail sales model includes food sales, since we are attempting to pick up the impact of the stimulus on the more discretionary aspects of retail spending. We also have pursued this approach more directly by modeling the performance of a particular subset of discretionary sales—those of household goods. The outcomes here are less positive. We estimate the lift to household goods sales to be A$0.3 billion, whereas the post-stimulus drag is A$0.7 billion, a net loss of A$0.4 billion.

The negative feedback is intuitive here given that household good purchases, typically capturing the bigger-ticket items, are more likely to be "one-offs" than are the other areas of discretionary spending, like sales at cafes and restaurants. As firms endure lighter volumes in the wake of the stimulus, many respond by discounting heavily in order to move unwanted inventory. The negative feedback then results in a price drag, which is added to the volume drag. It appears, based on our experiment, that this negative feedback has outweighed the positive effects on income and sentiment that have supported spending more broadly.

Plant and machinery investment: actual and model counterfactual



Housing finance: actual and model



Capex and the investment allowance

In December 2008, the government introduced a tax deduction of 10% for capital investment on asset purchases over A$10,000. The allowance originally applied to assets purchased up until end FY2008-09, and in use before end-FY2009-10. In February 2009, the deduction was raised to 30%, and the program was broadened to cover small business purchases of over A$1,000. In its final incarnation, announced in May 2009, the tax deduction was raised to 50% for small business purchases undertaken up to December 2009. Deductions of 30% and 10% applied to other businesses for purchases (again, in excess of A$10,000) in the first and second half of 2009, respectively.

Actual investment initially (i.e., in 4Q08) undershot the model's prediction. This is not surprising given that the majority of the program's heft only came into play in mid-2009 and, more importantly, that investment is a very forward-looking decision, which would not otherwise be captured contemporaneously in the data. As such, the RBA's aggressive interest rate cuts in 4Q08 (which are implicit in the baseline projection), while promoting investment, probably were insufficient to outweigh concerns of global financial meltdown that were at the forefront of managers' decision-making at the time. Moving into 2009, the economic data turned sour, with unemployment rising and business survey results turning south, and the baseline prediction deteriorated markedly. Actual investment, on the other hand, managed to tread water, supported by the allowance, and, of course, strong commodity demand from the Asian region, which meant cancellation of mining projects was relatively limited. From mid-2009, firms' sentiment (and the data more broadly) turned for the better, as it became clear a severe downturn would be averted. This has returned the baseline to near the current levels of actual investment.

Taking into account the entirety of this profile, the role of the allowance appears to have been to lower the effective cost of investment, so that firms could more modestly trim capex plans while they waited to see whether the global downturn spilled into the Australian economy. In the event, there was little fallout. The lack of a deep, crisis-induced dip means that there was no bounceback, though the capex outlook remains robust given the number of mining projects likely coming on line in the years ahead. Hence, the allowance seems to have left a net positive impact on the economy, although the importance of shifting expectations to investment, which the data miss, likely overstates the impact as gauged against the baseline scenario.

Home loans and the expanded grant

In October 2008, the government announced the First Home Owners' Boost: an expansion of the existing grant for first home purchasers from the original level of A$7,000 to A$14,000 for purchase of existing housing, and to A$21,000 for the purchase of newly constructed dwellings. The grant originally was active until June 30, 2009, but was extended until September 30, 2009, with a scaled-down version (A$10,500 and A$14,000 for existing and new dwellings, respectively) in play in 4Q09. Thereafter, the grant fell back to its original level of A$7,000, with new price caps applied.

On face value, it appears the grant has had little positive impact on total demand for home loans, since the actual series sits below the baseline and both have a similar shape (first chart). However, the conclusions for housing finance are more subtle than suggested by the counterfactual. We show that while there are factors complicating the analysis of housing finance in the aggregate, we can tease out the impact of the expanded grant on loans for new dwellings.

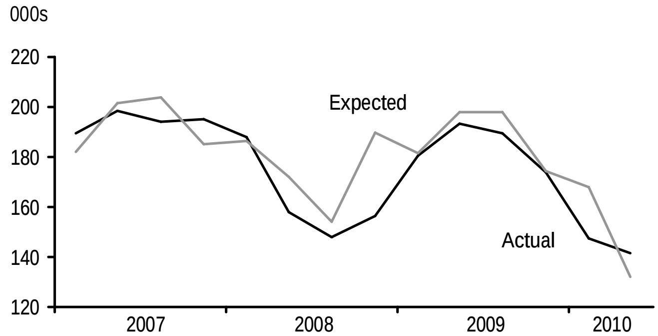
Expectations and rate hikes cloud picture

The fact that the housing finance model overshoots (second chart, previous page) leading into the crisis is instructive. The sharp deterioration in housing finance in *early* 2008 suggests that households became uncertain about the outlook for house prices and the economy, and began withdrawing from the market leading into the crisis. Since the grant came online after households' uncertainty had escalated (arguably, as a direct response to it), but before that uncertainty got a chance to manifest itself in the broader economic data, we have an artificially inflated baseline, which will understate the role of the grant in stimulating loan demand. This helps explain why, despite intuition to the contrary, loans underperformed the baseline series.

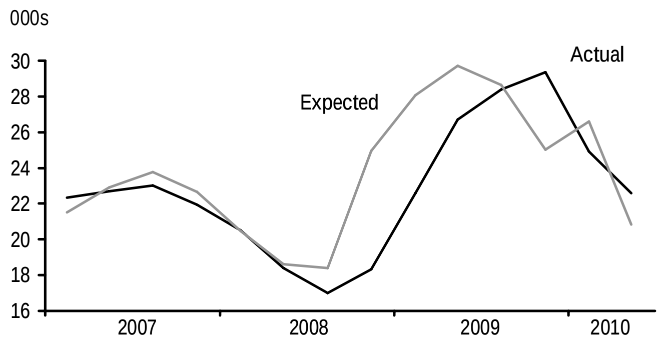
The similarity in the shapes of the baseline and actual series is also important. It reflects the fact that the cycles of the grant and monetary policy were tightly correlated over the stimulus period: interest rates were falling until 2Q09, which is when the grant was supposed to end. Thereafter, rising interest rates were in the cards, and the majority of grant-sensitive buyers had already purchased, depressing loan demand. This correlation means the baseline, which captures only the interest rate effect, can mimic the shape of the actual series, which captures both rates and the grant.

These complications make it difficult to confirm our a priori expectation that the grant promoted total demand for housing finance. We therefore re-estimated the housing finance model, replacing the dependent variable with housing finance for new dwellings only (which is more tightly bound to first-home buyers and more heavily incentivized in the grant). The results confirm our suspicion: early on, the simultaneity of rate hikes and the grant cloud the picture, but eventually home loans begin to outperform the baseline, as rate hikes and the extension of the grant push in opposite directions in 2H09, teasing out the impact of the grant.

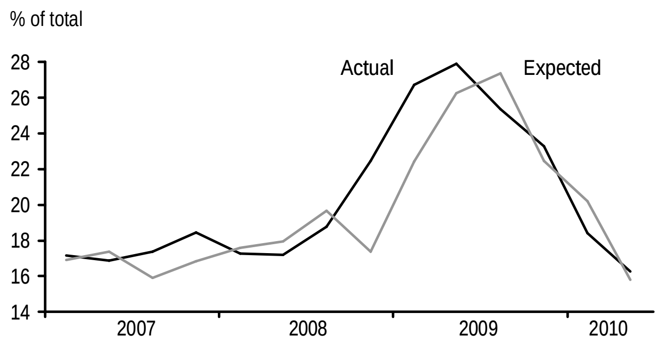
Housing finance: actual and model counterfactual



Housing finance for new dwellings: actual and model counterfactual



FHBs' share of housing finance: actual and model counterfactual



The evidence suggests that the grant stimulated demand for loans for new dwelling investment, though it remains difficult to quantify the extent of the support for total loans. Of course, in terms of the composition of buyers, the grant had powerful effects. Replicating the exercise once more with the share of loans taken by FHBs as the dependent variable, we see a significant drag forward under the grant, with each series reaching similar peaks, but FHB representation being uniformly higher (by up to 5%-pts) in 1H09 in the actual series, at the expense of investors and refinancers. We discussed this dynamic, its unwinding, and the legacy issues that presents in "First-home buyers casting a long shadow over Aussie data," *GDW*, July 30, 2010.

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Australia

- **Federal election delivered a hung Parliament**
- **RBA comfortable sitting on policy sidelines for now**
- **Step up in wage growth postponed a quarter**

With three quarters of the vote counted, voters in Saturday's Federal election look likely to have delivered the first hung Parliament in **Australia** since 1940. Neither of the two major parties has won the "magic number" of 76 seats needed to form a majority government. A handful of independents and one Green MP, therefore, will play the roles of "king-makers" in determining which of the major parties will be asked to form a government.

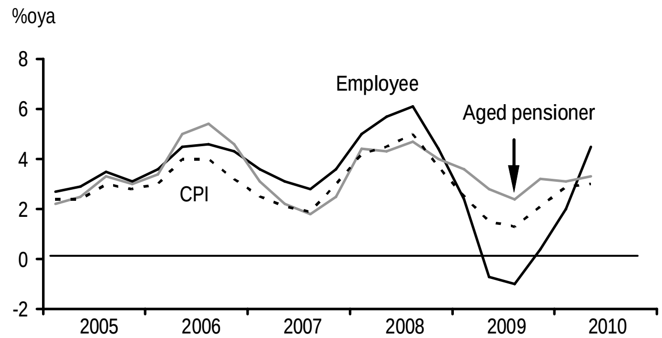
With the "horse-trading" only just having started between the independents and the major parties, it will be some days before we know whether the Labor government has been "re-elected", or whether the Opposition will be able to form a government. The Coalition easily won the highest share of the popular vote, and looks likely to win the most seats in the Lower House. The Coalition, therefore, is slightly better-placed to form a government, although many votes are yet to be counted.

No ammo given RBA's policy inaction

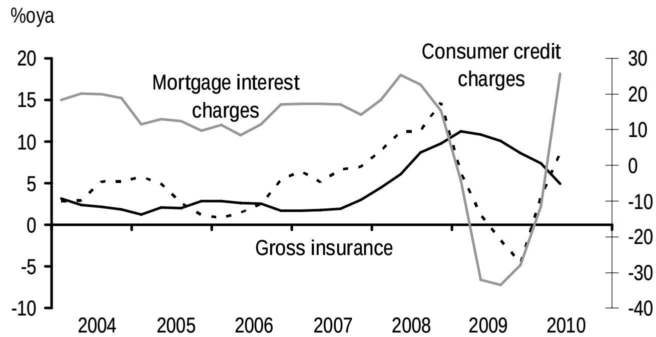
Had the RBA delivered an August rate hike, the Opposition would have used the argument that the government's poor management of the economy had pushed prices up, forcing the RBA's hand. During the last election campaign in 2007, the RBA's decision to hike the cash rate crippled the government, assisting in the termination of the former PM John Howard's long-running reign. Current Prime Minister Julia Gillard was fortunate to avoid the same scenario, particularly given that the "cost of living" already is a hot topic, with electricity prices, for example, having risen considerably.

Indeed, official ABS data confirmed last week that living costs have risen sharply, at least for some households. The ABS' living cost index for the June quarter showed that the households most squeezed are those with regular incomes (chart). The index measures price changes in items according to the spending patterns of different household types. For "employee households," the living cost index increased 4.5%oya in 2Q (well above official headline inflation of 3.0%). The substantial rise in living costs for this group since mid-2009 has coincided with the rise in mortgage interest charges (first chart next page) resulting from the RBA's current tightening cycle, which got under way in October last year. The divergence between the living cost index for employee households and the CPI numbers can be largely explained by the fact that the CPI calculation excludes mortgage repayments. Indeed, changing mortgage payments are much more important to households with employees than to older households. For the latter group, living costs increased in 2Q, but in line with the official inflation rate. The living cost index for aged pensioners rose 3.3%oya, and by 3.0% for self-funded retirees.

Australia: ABS' living costs indexes (by household type) vs CPI



Australia: ABS' living costs indexes (by employee household)



RBA comfortable with current settings

Mortgage holders can breathe a sigh of relief, however, with the RBA likely to keep the powder dry for the time being. The minutes from the RBA's August Board meeting released last week showed that officials remain upbeat, but comfortable to sit on the policy sidelines for now. The tone of the commentary was similar to that delivered in the statement two weeks ago. Board members balanced the strength of domestic economic conditions against the impact of some signs of weakness offshore, leaving the view fundamentally unchanged. The RBA deemed that the current level of the cash rate remained "appropriate," particularly given the significant degree of market volatility.

The decision to leave the cash rate unchanged in August, for the third straight month, had been widely anticipated, particularly given that the 2Q CPI print had shown a further decline in underlying inflation. The RBA highlighted in the August Board minutes that headline inflation in 2Q had been bolstered by the effects of the increase in the tobacco excise, and that underlying inflation had fallen below the top end of the RBA's 2%-3% target range for the first time in three years. While these results had been consistent with the Bank's own forecasts, they did provide the RBA with further scope to pause for a little while longer.

Tightening cycle not yet over, however

RBA officials expressed in the Board minutes their desire for "further information." This probably includes more information on the global economy, in light of heightened concerns about the prospects of a double-dip recession, and more information on domestic inflation. Indeed, the RBA probably will remain on the policy sidelines until after the late-October release of 3Q CPI data, which should prove that 2Q was, in fact, the low point in the inflation cycle. Our base case is for the next rate hike to be delivered in November, with the tightening cycle to continue well into 2011. The soaring terms of trade, the narrowing of the output gap, the tight labour market, and building wage pressure will halt the downward descent of core inflation and result in a lofty base for 2011, when capacity constraints really start to bite.

Mixed signals from employment data

One issue for the RBA is that the employment data are suggesting that the economy is growing above trend, while the GDP data suggest the economy is growing at trend. This conundrum played out in 2006, with the employment data giving a truer read on the pulse of growth momentum. This likely will not be far from policymakers' minds, and means that any fall in the unemployment rate below 5% could have important consequences for policy. The current unemployment rate is 5.3%, having touched 5.1% in June.

Given the significant tightening of the labour market since the middle of last year, the RBA already is concerned about building wage pressures. Since mid-2009, the economy has added some 330,000 jobs and the jobless rate has dropped 0.5%-point. But, while a tight labour market can generally be expected to generate faster wage growth, the labour price data last week showed that wages have thus far remained subdued. Annual wage growth was steady at 3% in 2Q, having held at this level or below for three straight quarters.

That said, wage growth is poised to accelerate. The unemployment rate topped out at a much lower level than we

Australia: labor price index and unemployment

(and the RBA) forecast, mainly owing to the fact that, during the downturn, employers cut workers' hours, rather than shedding jobs. Despite the fact that employment gains slowed in July (to a still-solid +23,000), and that we expect job creation to be more subdued going forward relative to 1H10, the absence of a significant hangover in the labour market after robust gains in the previous cycle suggests that supply-side pressures are looming. Further, even without these pressures, wage growth in 3Q will increase, with Fair Work Australia recently announcing a A$26-a-week increase in the minimum wage, effective from July 1.

Existing wage pressures are stemming from the expected suspects (first chart). The largest movement in the June quarter was recorded in resource-dependent Western Australia, where wages grew 1.0%q/q, having been at just 0.6% in 2Q09. The largest movement by industry was in mining, where wages were up 1.4%, nearly three times the growth rate of just 0.5% in 3Q09. This provides more evidence that supply-side constraints already are biting early on in the next upswing of the mining boom, which will cause further capacity constraints to emerge in the labour market.

Mining boom underpinning capex

The June quarter business investment survey this week should confirm that firms' capital spending plans remain largely intact. This will be despite the uncertainty around the Resource Super Profits Tax (RSPT) announced in May. The RSPT on mining companies had generated harsh opposition from resources giants. Following the announcement, some of the world's largest commodity extractors lined up to condemn the idea. Some even announced intentions to scale back investment in Australia, while others put projects on hold or under review. The controversial RSPT was, however, diluted in early July following negotiations with the mining industry. It was replaced with the Minerals Resource Rent Tax (MRRT). The new MRRT prompted

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many in the industry to put back on the agenda the projects that supposedly had been shelved.

In the June quarter, capital spending will have risen 1.5%q/q on our forecasts, having unexpectedly declined in the previous three months. Managers, despite being a little more downbeat than three months ago, will still plan to lift spending in the year ended June 2011. Indeed, firms probably will *boost* investment spending by 9% in the year ended June 2011; previously, the expectation was for a 14% rise. The first estimate of firms' spending plans for 2011/12 also will be released, and should show that firms intend to boost spending by 18%.

Data releases and forecasts

Week of August 23 - 27

Mon
Aug 30
11:30am

Private new capital expenditure
Seasonally adjusted

	3Q09	4Q09	1Q10	2Q10
%q/q	-4.4	6.1	-0.2	1.5
%oya	1.0	-2.8	1.0	2.8

See main text.

Wed
Aug 26
11:30am

Construction work done
Seasonally adjusted

	3Q09	4Q09	1Q10	2Q10
%q/q	0.9	-0.2	1.9	3.0
%oya	5.0	0.7	5.6	5.7

The composition of construction should have continued to shift from public works toward private sector activity in 2Q. Construction work finished probably rose 3%q/q (5.7%oya), with public sector building downshifting in growth terms, as the government's intervention in the education sector fades, but with private residential building and engineering work rising in its place. Private residential completions have been soft for some time, owing to the lag that developed between building approvals and dwelling starts in 2009. This gap closed significantly in 4Q09, meaning that we should be seeing the benefits of earlier robust improvements in housing market activity in coming quarters.

Review of past week's data

Sales of new motor vehicles
Units, sa

	May		Jun		Jul	
%m/m	~~-3.9~~	*-4.2*	~~-1.2~~	*-1.4*	~~2.0~~	*-2.6*
%oya	~~16.5~~	*16.6*	~~8.2~~	*7.8*	~~18.4~~	*11.6*

Car sales unexpectedly fell in July, thanks to a drop in passenger vehicles (-4.3%) and other vehicles (-4.2%), while SUV sales were up (+3.2%). We thought headline sales volumes would have been bolstered by discounting going into the new financial year. There had been anecdotes that many cars ordered under the government's investment allowance last year were delayed in delivery. Sales are counted at the time of delivery, so this phenomenon would result in a spike in sales even after the expiry of the government program. With six months having passed, however, this effect should be well and truly fading.

WMI leading index

	Apr		May		Jun	
%m/m,sa	~~0.0~~	*0.1*	~~0.2~~	*0.3*	—	*0.0*

Labour price index

	4Q09	1Q10	2Q10	
%q/q,sa	0.6	0.9	~~1.0~~	*0.8*
%oya,sa	2.9	3.0	~~3.2~~	*3.0*

The labour price index grew 3.0%oya, the same rate as the previous quarter. Private sector wage growth accelerated to 2.8%oya (from 2.6%), while public sector wage growth slowed to 4.0% (from 4.2%).

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New Zealand

- **RBNZ concerned about inflation expectations**
- **Double whammy of GST hike and ETS in 2H10**
- **Escalating expectations would force more rate hikes**

RBNZ worried about inflation expectations

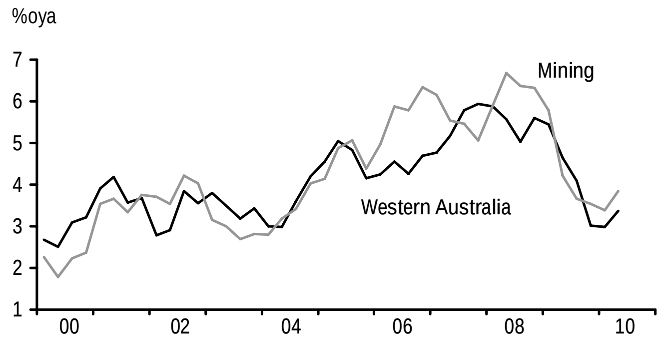
RBNZ Governor Alan Bollard delivered a speech last week entitled "Keeping inflation anchored during economic recovery." The Governor discussed the forthcoming hike to the goods and services tax (GST), and its possible implications for monetary policy.

While headline inflation has been well-behaved, it is set to rise significantly, owing to the introduction of a series of one-off policy changes. In the current quarter, changes to the ETS (effective July 1) have pushed prices of fuel and electricity higher. A rise in accident compensation levies for motor vehicles and a rise in insurance premia owing to changes to the taxation of insurance companies also have added upward pressure on prices. In 4Q, the government will increase the GST to 15% from 12.5% (effective October 1), which will add around 2%-pts to headline CPI. On our forecasts, having printed at 1.8%oya in 2Q (below the middle of the RBNZ's 1%-3% target range), headline inflation will rise as high as 5.6% next year.

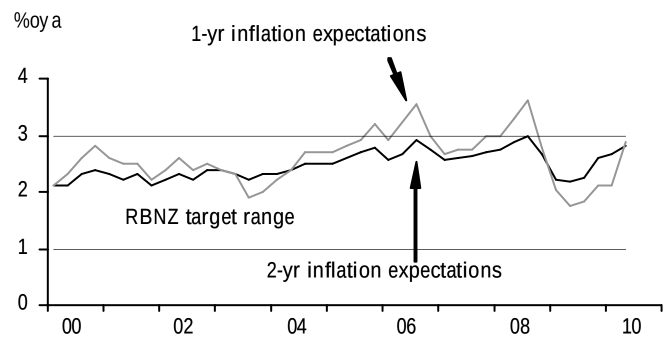
Indeed, the key challenge for the RBNZ will be to prevent elevated inflation spilling over to changes in price- and wage-setting behaviour. Bollard warned that if households and businesses increase margins and wages in response to the GST hike, they will worsen inflation, via higher inflation expectations. As a result, we expect a series of similar speeches from the RBNZ Governor in coming months attempting to ensure that inflation expectations remain anchored. A rise in already-elevated inflation expectations has the potential to have a lasting impact on reported inflation. In 2Q, the RBNZ's measure of inflation expectations was higher over both the one- and two-year horizons, spiking to 2.9% and 2.8%, respectively. The next survey of inflation expectations will be released tomorrow, and should show two-year inflation expectations rising to 3.0%oya.

The Governor believes that the "inflationary effects [of the one-off policy changes] should be largely out of the system by later next year." On our forecasts, however, headline inflation will still be hovering above the RBNZ's target rate in 4Q11. In the case that expectations rise significantly, the RBNZ would be forced to respond by tightening policy more than would have otherwise been the case. Even in the absence of a significant rise in inflation expectations, our forecast remains for another two rates hikes this year, with the most likely month for a pause being October.

Australia: labor price index



Inflation expectations already near top end of RBNZ's target



Data releases and forecasts

Week of August 23 - 27

No releases this week.

Review of past week's data

Producer price index

	4Q09	1Q10	2Q10	
Inputs (%q/q,nsa)	0.4	1.3	~~-0.1~~	*1.4*
Outputs (%q/q,nsa)	-0.1	1.8	~~-0.2~~	*1.1*

With pipeline pressures remaining strong, the risks are skewed toward even higher inflation prints that we currently forecast. Input prices, or changes in the costs involved in production, were up 1.4% in 2Q, while prices received by producers, or output prices, were up 1.1%.

Visitor arrivals

	May		Jun		Jul	
Total (%m/m,nsa)	~~1.1~~	*1.2*	~~0.3~~	*0.7*	__	*1.4*

Net permanent immigration

	May	Jun	Jul	
Monthly (000s, nsa)	0.3	-0.7	__	*1.4*
12 month sum (000s, nsa)	18.0	16.5	__	*15.2*

Credit card spending

	May	Jun		Jul	
%oya	3.4	~~4.5~~	*4.4*	__	*2.7*

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Global Essay

- **Weaker data, led by jump in claims, trigger US forecast downgrade**
- **Fed, BoE now expected to renew government bond-buying programs**
- **US, European core price disinflation to continue amid subpar growth**

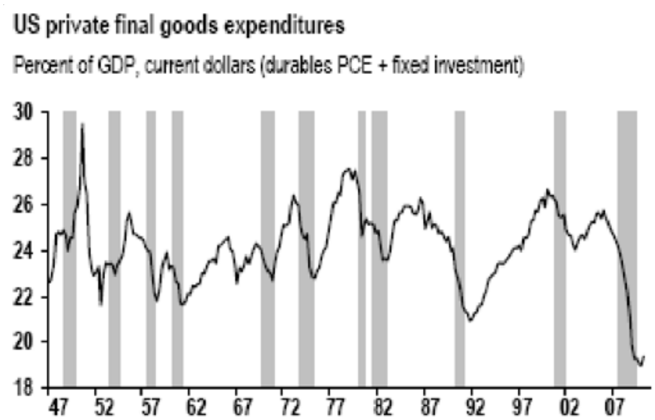
When the facts change

Three months ago, our global economic forecast called for a moderate slowing in second-half growth as global manufacturing activity came off the boil. The forecast has since undergone a series of revisions that reflects accumulating evidence that the downshift has broader sources. There has been a widespread softening in consumer spending gains. In addition, our global PMI surveys have failed to show the lift in service industries expected to offset the slowing in manufacturing. Notably, there have been growth disappointments in each of the three largest economies in the world. In China this disappointment has been modest; in the US and Japan, growth momentum has turned decisively. The significant downward revision taken to these two countries this month lowers our forecast of 2H10 global GDP gains to a sub-trend pace.

Although we already had trimmed our expectations for US GDP growth in 2H10 in response to signs of softening around midyear, the forecast had maintained a contour of forward motion in the expansion. Despite disappointments in hiring and spending, the shift in household and business behaviour away from retrenchment was expected to remain in place—proving sufficient to generate solid labour income gains and keep the unemployment rate on a modest downward trajectory.

Coming together with continued softness in July economic indicators, the sharp rise in initial jobless claims this month challenges this thesis. Taken at face value, a 500,000 level of claims is consistent with a stall in growth and a contraction in private sector jobs. More fundamentally, it suggests that the shift in business behaviour away from retrenchment may have stopped in its tracks. We recognize that three weeks of rising claims does not constitute a trend. But the movement has been sharp enough and sustained enough to warrant a further change in our economic forecast. We now anticipate GDP growth of 1.5%q/q saar this quarter (previously 2.5%). We are lowering next quarter's growth projection to 2% (previously 3%). It is still likely that the composition of growth will rotate from goods- to service-producing industries, a development that will moderate the impact of lower growth on job creation.

But the current forecast still implies very little gain in private sector employment and a rise in the unemployment rate toward 10% by year-end. A key issue is whether subpar growth will now create a negative feedback loop—both in the US and across the globe. Thus far, the deterioration in financial markets and private sector sentiment has been modest and the risk that downward momentum feeds on itself and produces a global recession seems small. However, the odds have risen for the US, where we now place the likelihood of a new phase of economic contraction at close to 30%. Our assessment that a US double-dip remains unlikely rests on the observation that cyclically sensitive components of demand that tend to drive the economy into contraction—construction, inventories, consumer durables, equipment spending—sit at levels consistent with depressed behaviour and are not likely to break sharply lower. We see the risk of a significant credit shock as simi-



larly low due to the financial deleveraging that has already taken place.

Of greater concern is the possibility of a prolonged soft patch. A sustained period of growth at 2% or less would create very worrisome medium-term dynamics in labour markets, public finances, and inflation. The risk of deflation would rise, partly due to increased downward pressure on inflation expectations. The movement downward in medium-term inflation expectations has gathered pace this month and already raises concerns that the Fed may be losing its reflationary credibility. Although our baseline forecast sees drags gradually fading as the economy continues to grow and as temporary drags from the downshift in manufacturing and fiscal tightening fade, the risk of a prolonged soft patch now looks like a reasonable alternative scenario.

Given the loss of momentum in the recovery, the odds favour further Fed action to expand the balance sheet. This most likely will entail a resumption of purchases of longer-dated Treasuries. We are now thinking through the likely size and timing of those purchases. Chairman Bernanke's Jackson Hole speech may give some clue to how close the committee is to taking additional steps to support the recovery.

Japan's economy hit a wall in 2Q

Japan's 2Q GDP report was much weaker than expected, with output rising just 0.4% annualized. Although net trade made another large positive contribution to growth, there was minimal growth in the core domestic demand components of consumption and capex. Moreover, growth in back quarters was marked down, putting the year-ago GDP gain at a moderate 1.9%, or 0.2% in nominal terms. The report suggests that the expiration of the government's "ecopoints" program may be exerting a larger drag on durables consumption than anticipated. In addition, businesses are not raising capex as aggressively as expected, despite abundant cash on hand. One caution is that the pronounced weakness in 2Q did not register in the monthly business surveys, which normally give good guidance to the economy's underlying momentum. Even so, the risks to our 2H growth forecast (1.7% saar) lie to the downside, with the export sector poised for a sharp slowdown in response to slowing external growth and the stronger currency.

These developments have prompted discussions among policymakers about how to support the economy. The government is considering another fiscal package, although it is likely to be very limited in scope, amounting to less than 0.5% of GDP. In addition, Prime Minister Kan is expected to meet BoJ Governor Shirakawa early this week to discuss the economy. However, the indications are that the BoJ retains a relatively optimistic outlook and is not prepared to undertake significant new easing measures.

G-4 banks slowly easing loan standards

Bank lending attitudes slowly are becoming more supportive of growth. The latest senior loan officer surveys show that a small majority of banks in the G-4 relaxed terms and standards on new loans in 3Q for the third consecutive quarter. This represents a major departure from the past several years, when banks relentlessly tightened standards. History shows that surveys of bank lending standards correlate well with actual spending. Thus, if credit conditions continue to ease, this would bode well for the economic recovery. The rally in credit markets also is supporting demand, both directly and through its feedback on bank behaviour. Indeed, in last week's Fed survey, respondents cited competition from other banks and non-bank sources as the prime reason why they were easing standards. Despite these developments, the stock of bank loans has yet to recover. Although private spending is rising, the associated new borrowing likely does not yet match the flow of amortization banks receive on existing loans. Alternative sources of financing, along with bank writedowns, also are playing a role. All that said, bank loans recently have shown signs of stabilization and will turn upward with a continued recovery in spending.

Euro area core inflation still in downtrend

We have long anticipated a significant decline in Euro area core inflation across the periphery; indeed, the sharp

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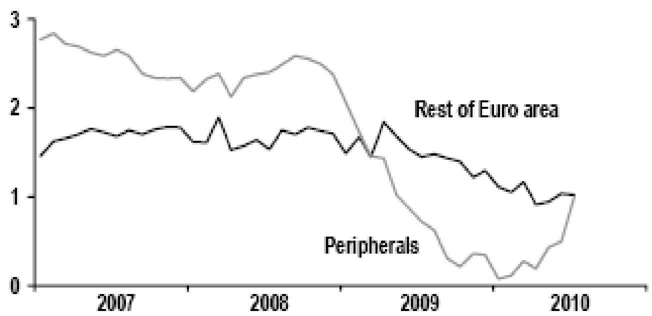
Euro area core inflation

%oya, HICP ex. food, energy, alcohol, and tobacco



increases in core inflation in Greece, Spain, Ireland, and Portugal since the start of the year have added 0.16%-points to areawide core inflation. Excluding fiscal effects, Euro area core inflation is likely to slide further, although the downward momentum is likely to moderate as the output gap stabilizes and as core inflation moves closer to zero.

In the UK, a combination of impact from a weaker currency and an increase in indirect tax has kept core inflation running above the 2% target since December, exacerbating the concerns raised by persistently high headline inflation. Our analysis suggests that a fading currency impact and continued weak economic growth should now be damping core inflation, and last week's July reading was a major step in that direction. We look for inflation to be close to the MPC's 2% target by 2Q11, which is more quickly than the MPC expects. With our forecast now calling for growth to fall below trend toward year's end, we think the MPC will opt to restart its program of gilt purchases, beginning with a £25 billion installment in November.

SARB to ease on subpar growth outlook

While economic activity in CE-3 is helped by strong growth in Germany, momentum has been lost in other parts of the CEEMEA region, notably Russia and South Africa. In Russia, activity has been hit hard by an extreme heat wave and associated drought and wildfires in July and August. Although 4Q growth is likely to be stronger, paying back much of the weather-related downshift in 3Q, there are downside risks to our 5% growth forecast for 2010.

In South Africa, this week's 2Q10 GDP report is likely to confirm that the recovery lost steam faster than expected. Although growth is expected at 3.2%q/q saar, it likely would have been closer to 2% if not for the boost from the World Cup. We have trimmed our growth outlook to near 3% in coming quarters, or about 0.7%-point below trend, reflecting sluggish domestic demand, and pressure on net exports from slowing global growth and the much stronger currency. Recent SARB rhetoric suggests less tolerance for currency strength, while some politicians have raised the possibility of introducing a tax on inflows to stem FX appreciation (which we doubt will pass). With the strong rand and wide output gap set to contain inflationary pressures, the door is open for the SARB to cut rates by 50bp at the September 9 policy meeting and possibly once more thereafter.

Latins resisting global slowdown

Amid the latest wave of soft data releases and forecast revisions, Latin America stands apart. Despite the deteriorating external backdrop, regional activity indicators continue to surprise on the upside, prompting us to hold the line on our near-term growth forecasts. Last week's reports delivered signs of widespread momentum across the region, including Mexico, Argentina, Colombia, Chile, and Peru. Data also show the economy accelerating in Brazil after a subpar 2Q performance. The resilience of Latin growth flows from the strong recovery in domestic demand across the region, whereas the contribution from net trade already is negative. To be sure, a continued deceleration in global activity eventually will hit Latin America, although the main fallout will likely occur in 2011. Mexico is particularly vulnerable given its close economic links with the US. In the meantime, the region's faster growth rate and rising interest rate differential (as policy rate normalization proceeds) are attracting capital inflows that support growth. This is driving FX appreciation, prompting many central banks to step up intervention.

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JPMorgan View - Global Markets

No bubble in bonds

- **Economics**—Global growth through mid-2011 lowered to trend level of 2.6%.
- **Asset allocation**—Long duration. Overweight credit versus equities and both versus commodities. Remain overweight EM assets.
- **Fixed income**—Fed and Bank of England to add to QE this year, further bullish flattening curves.
- **Equities**—Equities can withstand a short-lived soft patch, but not a prolonged one.
- **Credit**—European spreads likely to stay volatile within a wide range.
- **FX**—Expect short-term unwind of carry trades.
- **Commodities**—Stay underweight oil and industrial metals.

Another set of weak data from the US and Japan is forcing us **to lower global growth forecasts** again, this time to only 2.6% for the coming four quarters, down from the 3.5% over the past year. Our initial assumption that we are not on the slippery slope toward a double dip is being challenged. We are clearly getting a dip in growth rates. The economic drivers we see are not yet telling us that we will get a dip in economic activity—a recession—although we do now gauge the risk of a US recession over the next year at 30%.

The implications for markets all depend on whether this is it, or whether growth prospects continue to fall. If the cause of the weakening were a natural pause in growth or a one-off shock that is now fading, then we would have little to worry about. But this may not be the case anymore. Part of the slowing we just can't explain, which is worrisome. And part is simply unfinished delevering by US consumers, with little clarity on when this process will be complete. The increased caution by US companies is more puzzling, as their balance sheets are in good condition. Maybe they are just anticipating weak demand. And one can't blame credit-constrained small companies relative to large ones with easy access to the bond markets for the weakening, either, as both are doing little hiring. There are a lot of maybes here that create uncertainty.

The downside risks to growth are compounded by the realization that **policy makers are running out of ammunition**. With bond yields near historic lows, more QE buying of government bonds will not accomplish much. And fiscal easing is unlikely with most major governments heading the other way. At some point, policy makers will be tempted to abandon caution, moving QE to a new level, or cutting taxes again, but this is likely more a risk for next year.

Lower growth poses a clear danger for risky assets. Most at risk are commodities, followed by equities, with **credit least affected.** Commodities are most at risk as they offer no yield, are more sensitive to the industrial cycle, and are a clear short for those starting to position for deflation. Stay negative here. Equities require growth more than does credit, which just needs downside protection. As long as we see only slower growth without recession, then **credit risk is a better place than equities**. And that indeed remains our investment strategy.

Is this just a US problem, and a US underweight, or are **all US problems global ones?** Two years ago, we thought US consumer delevering was a US shock with modest implications for the rest of the world, and implying simply underweighting US assets. But then Lehman made this a truly global crisis, with economies in Europe, Japan, and many EM countries contracting even more than the US. Here we are again at the same point, and again treating this as a US shock. Maybe we never learn, and a 2008-type crisis is truly unpredictable, but this time around, we feel good in saying we are seeing a US slowing that requires underweighting its assets.

There are two possible **US underweights—one within DM, versus Europe and Japan, and one versus EM**. We strongly prefer underweighting US assets against EM ones, as EM does not have the delevering, deflation, and demographic problems of the older economies. We could see some short-term position- squaring on EM, after recent massive inflows, but the outlook for EM overweights remains positive through year-end. **Overweight EM** equities, credit, bonds, and currencies. The case for Europe and Japan against US assets is much less clear, as Japan has weakened a lot also in 2Q, and we figure Europe risks following the US in 2H.

Are bonds in a bubble? A good question, with global bond yields at historic lows and equity risk premia at historic highs, and after the equity and credit bubbles we saw already in the past decade. **We do not think so.** Historically, three conditions signal the presence of a bubble: excessive optimism, leverage, and huge misvaluation against fundamentals. These conditions are not clearly in place.

Long duration positions are subdued, despite massive

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Japanese buying. Bond yields have been falling for 20 years and have been below average for at least 10. Most important, the fundamentals against which to value bond are not clear. If growth and inflation return to normal, then bonds are massively overvalued. But there is a serious risk now that we have entered a decade of low growth, with deflation around the corner. We thus remain long fixed income.

Fixed income

Further weakness in US data pushed bond yields still lower across the board. We stay long in both DM and EM. **We now expect both the Fed and the Bank of England to extend their QE later this year.** Both are very likely to focus any purchases on medium- to longer-dated government bonds, thus bolstering the bullish flattening trend.

Japanese buying of foreign bonds has surged since June, reaching $25 billion last week, and $163 billion over the past three months (see Friday's *Flows and Liquidity*). This is likely driven in large part by the very low level of JGB yields—now below 1% for the first time since 2003. But it may also be because the domestic experience of deflation makes Japanese investors attribute a greater likelihood to deflation abroad. We expect Japanese yields to stay low, suggesting that Japanese bond buying should stay strong.

EM local bonds continue to keep pace with core markets, and have now gained almost 8% on the year. **The seemingly secular support of steady inflows from abroad is being augmented by the cyclical boost of easier monetary policy.** For one, we now expect the central bank to ease next month in South Africa, which remains our favoured long in CEEMEA.

Equities

Weak US economic data continue to weigh on equity markets. But the damage has been rather contained so far. **Equities remain in the middle of their three-month range and volatility has barely risen over the past two weeks.** Both the VIX and VStoxx indices remain well below their May peak.

Why are equities not selling off more significantly? What matters for equities is earnings and not GDP growth. US GDP growth projections are being cut, but earnings projections have been little affected so far. Investors and analysts are hoping that, to the extent the soft patch in US GDP growth lasts for only a few quarters and does not spill over to the rest of the world, US companies will be able to protect their revenues and profits. Indeed, this is what happened during 2Q, when US companies were able to deliver strong top line and EPS growth even as US GDP grew at only a 1% pace.

It is a prolonged soft patch that poses the greater threat for corporate earnings and equity markets as it raises the specter of deflation and profit margin contraction. Why is deflation bad for corporate profitability? When nominal interest rates are bounded at zero, a fall in expected inflation causes a rise in real interest rates and the cost of capital, hurting corporate profitability. In addition, nominal wage rigidities mean that deflation reduces output prices by more than input prices putting pressure on corporate profitability. Indeed, the Japanese experience of the 1990s provides an example of the erosion in corporate margins under a deflationary environment.

While a prolonged soft patch is not our baseline case, the risk of this happening has risen in recent weeks. This makes us focus recommendations on relative rather than outright equity trades. **Across regions, we avoid the US and Japan**, where most of the economic weakness is currently being felt. Indeed, EM equities resumed their outperformance this month. **Across sectors we avoid Industrials and other Cyclicals sectors** as they are being hurt by the downturn in manufacturing and their low dividend yields relative to Defensive sectors.

Credit

We believe **US credit is likely to underperform that of EM** near term. Although our base case remains no US recession, recent data weakness creates more uncertainty and increases downside risk. In contrast, emerging economies continue to see strong growth. EM corporate bonds are also more attractive to investors as their yields are higher than those of similar US high-grade bonds. Overweight EM dollar-denominated bonds (CEMBI) versus similarly rated US HG bonds.

HY bonds should continued to benefit from the search for yield. Within HY, we **favour higher-quality bonds**, as they are more protected if the US economy slows even more than our lowered forecast. They are also more likely to benefit from crossover investor flow given their lower probability of default.

A tug of war between investors expecting a double-dip

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scenario and those seeing a sustained slow growth environment is likely to keep **European HG spreads volatile within a wide range**. Thus, we keep directional risk low and position on relative value trades instead. Our strong conviction trade in Europe continue to be OW distressed lower Tier II versus senior bank debt.

Hybrid capital has been gathering media attention as the Basel Committee released a consultation paper on the loss absorbency of regulatory capital. Under the proposal, bond holders could incur principal losses, even without default, when the government decides a firm has reached a "point of non-viability." Future issuance of Tier II will likely suffer most as the required risk premia would have to increase substantially to reflect the higher likelihood of losses. Thus issuers are likely to prefer Tier I hybrids (see *Muddying the Waters*, Henriques, August 19). This proposal will not affect existing hybrid bonds, and we continue to find selected lower Tier II bonds attractive.

Foreign exchange

Our running theme for the past month has been that the dollar's broad sell-off in July would narrow in August as earnings season excitement gave way to dismal US data. We expected the dollar to gain versus the commodity currencies/high-yielders but weaken versus the yen and euro, particularly as the Fed reinstituted QE. Most currencies are moving as expected except the euro, which is weakening more on declining stock markets and recurring sovereign stress than it is benefiting from Fed actions. The original scenario looked like one of this year's typical corrections, but now that jobless claims are signaling a material downshift in US growth, the odds favour a further rise in volatility and a **more substantial carry unwind**. Indeed, every 1% downgrade in US growth tends to be worth about 3% on the trade-weighted dollar.

The only comfort comes from positions, which generally are much smaller than in May. Still, carry unwinds have become such familiar events over the past two years that they have established a pattern: they move exposures from long to almost flat and take currencies from expensive to cheap. Given that positions are half of May's levels and valuations are fair, the maximum downside on the commodity currencies and high-yielders is probably 5%. Funding currencies will continue to benefit, so we stay short NZD/JPY and EUR/CHF, and add a long in CHF/NOK. USD/JPY is not a carry trade but nonetheless should move lower if cross-yen falls. Stay short.

Ten-year Government bond yields

	Current	Sep 10	Dec 10	Mar 11	Jun 11
United States	2.57	2.65	2.50	2.50	2.50
Euro area	2.27	2.25	2.25	2.30	2.45
United Kingdom	2.98	2.90	3.00	3.20	3.35
Japan	0.93	0.85	0.80	0.80	0.90
GBI-EM	6.41			7.90	

Credit markets

	Current	YTD Return
US high grade (bp over UST)	164	10.1%
Euro high grade (bp over Euro gov)	173	5.4%
USD high yield (bp vs. UST)	698	8.6%
Euro high yield (bp over Euro gov)	679	8.6%
EMBIG (bp vs. UST)	302	13.5%
EM Corporates (bp vs. UST)	344	12.0%

Foreign exchange

	Current	Sep 10	Dec 10	Mar 11	Jun 11
EUR/USD	1.27	1.25	1.25	1.25	1.25
USD/JPY	85.7	80	79	81	83
GBP/USD	1.55	1.47	1.44	1.42	1.42

Commodities - quarterly average

	Current	10Q3	10Q4	11Q1	11Q2
WTI ($/bbl)	73	77	75	75	77
Gold ($/oz)	1227	1250	1275	1250	1250
Copper($/m ton)	7286	6500	6750	6750	7000
Corn ($/Bu)	4.34	3.90	3.80	4.00	4.20

Source: J.P. Morgan, Bloomberg, Datastream

around 1.25. Further QE is euro-positive, but recurring sovereign stress and lower equity markets this fall are obvious positives. And since EUR/USD moves intra-week are more random than in other pairs, owning funding currencies is the better strategy in this environment. Take profits on short USD/CHF, as the randomness of EUR/USD renders USD/CHF inferior to EUR/CHF as risky markets fall.

Commodities

As US and global growth loses momentum, we continue to see downside risk in the demand forecasts for **oil and industrial metals and stay underweight.** For agriculture, our overweight position has performed very well over the past weeks. Given the recent strong rally, we see little upside in the near term and agriculture prices are likely rangebound into mid-September. However, strong fundamentals for corn are likely to push agriculture prices higher into year-end.

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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	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11	3Q11	1Q10	2Q10	4Q10	2Q11
The Americas														
United States	-2.6	**2.8** ↓	**2.4** ↓	3.7	2.4	**1.5** ↓	**2.0** ↓	2.5	2.5	3.0	2.4	1.8	**0.9** ↓	**1.2** ↓
Canada	-2.5	3.4	2.7	6.1	2.6	3.2	3.2	2.7	2.0	2.4	1.6	1.4	1.7	1.9
Latin America	-2.9	**5.5** ↑	3.8	**4.1** ↓	**9.0** ↑	**2.6** ↓	**3.1** ↓	**3.2** ↓	**5.7** ↑	**2.8** ↑	6.0	**6.2** ↓	7.0	**7.1** ↑
Argentina	-2.0	8.5	4.5	12.5	13.0	4.0	4.0	2.0	4.0	8.0	9.0	9.0	10.0	11.0
Brazil	-0.2	7.5	4.0	11.4	2.6	6.2	3.3	3.8	4.2	4.1	4.9	5.1	5.3	5.4
Colombia	0.8	4.5	4.1	5.3	4.8	3.7	4.0	4.0	4.1	5.0	2.0	2.1	2.8	3.3
Ecuador	0.4	2.0	3.0	1.3	3.5	4.0	4.5	3.0	2.5	2.5	4.0	3.3	3.9	4.1
Mexico	-6.5	4.5	3.5	**-2.5** ↓	**13.5** ↑	**-3.6** ↓	**3.1** ↓	**2.9** ↓	**9.2** ↑	**-0.1** ↑	4.8	**4.0** ↓	5.1	4.5
Peru	0.9	**8.2** ↑	6.0	**8.0** ↑	**12.7** ↑	**4.8** ↑	**3.5** ↓	**5.8** ↓	6.7	7.2	0.7	1.2	2.6	2.2
Venezuela	-3.3	**-2.2** ↑	1.0	**-2.0** ↑	**5.2** ↑	**3.0** ↓	**-5.0** ↓	**2.0** ↑	1.0	1.5	27.4	**31.9** ↓	**31.6** ↓	**34.7** ↑
Asia/Pacific														
Japan	**-5.2** ↑	**2.7** ↓	**1.7** ↓	**4.4** ↓	**0.4** ↓	1.8	1.6	1.5	2.2	1.8	-1.2	-0.9	-0.7	0.1
Australia	1.3	2.7	3.2	2.0	1.9	3.3	3.8	2.7	3.2	4.0	2.9	3.5	3.8	4.1
New Zealand	-1.7	2.5	2.7	2.3	3.5	2.3	1.9	2.7	3.4	3.2	2.0	1.8	4.9	5.6
Asia ex Japan	4.8	8.6	**6.8** ↓	**10.6** ↓	**7.1** ↑	**5.3** ↓	**6.2** ↓	**7.0** ↓	**7.0** ↓	**7.2** ↑	4.3	**4.4** ↓	**4.2** ↓	**3.9** ↓
China	9.1	**9.8** ↓	**8.6** ↓	10.8	7.2	**7.5** ↓	**8.1** ↓	**9.1** ↓	**8.9** ↓	**9.1** ↑	2.2	2.9	2.8	2.7
Hong Kong	-2.8	**6.6** ↓	**4.1** ↓	8.7	5.7	4.0	3.8	4.2	4.3	4.7	1.9	2.6	2.5	2.2
India	7.4	8.3	8.5	9.2	8.1	8.0	8.9	8.0	8.5	8.6	15.3	13.6	11.8	10.1
Indonesia	4.5	6.0	5.4	3.0	7.5	4.5	5.0	5.3	5.2	5.0	3.7	4.4	**6.8** ↑	**6.6** ↑
Korea	0.2	6.1	4.0	8.8	6.0	2.5	3.8	4.0	4.0	4.5	2.7	2.6	3.2	3.5
Malaysia	**-1.2** ↑	7.2	4.6	**4.8** ↓	**7.2** ↑	**3.0** ↓	**3.5** ↓	4.9	4.9	4.5	1.3	1.6	**1.1** ↓	**1.3** ↓
Philippines	1.1	6.8	4.3	12.9	3.6	4.9	4.0	4.5	4.5	4.5	4.3	4.2	**1.8** ↓	**1.5** ↓
Singapore	-1.3	15.5	4.5	45.7	24.0	-8.5	0.0	6.1	6.6	8.2	0.9	3.1	3.0	**1.4** ↓
Taiwan	-1.9	**9.9** ↑	**4.1** ↓	**10.9** ↓	**7.2** ↑	**1.5** ↓	**2.3** ↓	4.2	4.6	5.5	1.3	1.1	2.0	1.8
Thailand	-2.2	8.5	5.0	16.0	-2.0	2.8	2.8	6.0	5.5	4.0	3.7	**3.2** ↓	**1.1** ↓	**1.5** ↓
Africa/Middle East														
Israel	**0.8** ↑	**3.5** ↑	4.5	**3.6** ↑	**4.7** ↑	3.0	3.0	4.0	5.0	5.5	3.5	**2.8** ↓	**2.6** ↓	**3.0** ↓
South Africa	-1.8	**2.9** ↓	**3.1** ↓	4.6	**3.2** ↓	**3.1** ↑	**3.2** ↓	**3.1** ↓	3.1	**3.4** ↓	5.7	4.5	4.7	4.9
Europe														
Euro area	-4.1	1.5	1.5	0.8	3.9	2.0	1.0	1.0	1.0	1.8	1.1	1.5	1.5	0.9
Germany	-4.7	3.3	2.4	1.9	9.0	3.0	2.0	2.0	1.5	2.0	0.8	1.0	1.2	0.9
France	-2.5	1.6	1.4	0.7	2.5	2.0	1.5	1.0	1.0	1.5	1.5	1.8	1.3	0.6
Italy	-5.1	1.1	1.3	1.6	1.5	2.0	1.0	1.0	1.0	1.5	1.3	1.6	1.5	1.1
Norway	**-1.2** ↑	**1.5** ↓	**2.3** ↓	**0.7** ↑	**1.9** ↓	3.0	2.8	2.0	2.0	2.5	2.9	**2.6** ↑	**1.4** ↑	1.0
Sweden	-5.1	3.8	2.7	6.2	4.7	3.5	2.8	2.3	2.3	2.8	1.0	1.0	2.3	2.4
Switzerland	-1.5	2.3	2.5	1.6	2.8	2.5	2.3	2.3	2.5	2.8	1.1	1.1	0.9	0.6
United Kingdom	-4.9	1.6	**2.2** ↓	1.3	4.5	2.5	**1.5** ↓	**1.0** ↓	2.5	3.0	3.3	3.5	**2.6** ↑	**1.9** ↑
Emerging Europe	-4.9	3.9	4.3	2.6	4.0	**2.9** ↓	**4.1** ↑	**3.5** ↓	4.0	**4.3** ↑	6.1	5.4	**5.9** ↑	**6.0** ↑
Bulgaria	-5.0	-0.5	4.0	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	-4.1	2.0	3.2	2.0	3.2	2.5	2.3	2.5	3.0	5.0	0.7	1.2	2.8	2.7
Hungary	-6.3	1.0	3.0	2.4	0.0	2.0	2.0	2.0	3.0	3.5	6.0	5.4	4.6	3.7
Poland	1.8	3.5	3.8	2.0	4.0	3.5	3.5	3.0	3.5	4.0	3.0	2.3	2.6	2.6
Romania	-7.1	-2.0	1.5	...	...	...	...	...	...	...	4.6	4.4	8.0	7.2
Russia	-7.9	5.0	5.0	3.4	5.9	**3.5** ↓	**6.0** ↑	**4.8** ↓	5.0	**5.0** ↑	7.2	5.9	**7.2** ↑	**8.0** ↑
Turkey	-4.7	5.9	5.0	...	...	...	...	...	...	...	9.3	9.3	7.5	6.7
Global	-2.6	**3.3** ↓	**2.8** ↓	**3.8** ↓	**3.6** ↑	**2.4** ↓	**2.4** ↓	**2.5** ↓	2.8	**3.1** ↑	2.2	**2.1** ↓	1.9	1.9
Developed markets	-3.5	**2.3** ↓	**2.0** ↓	**2.8** ↓	**2.7** ↓	**1.9** ↓	**1.7** ↓	**1.8** ↓	2.0	2.5	1.5	1.4	1.1	1.1
Emerging markets	1.1	6.9	**5.5** ↓	7.5	**7.0** ↑	**4.2** ↓	**5.0** ↓	**5.4** ↓	**6.1** ↑	**5.6** ↑	5.1	**4.9** ↓	**5.1** ↓	4.9
Memo:														
Global — PPP weighted	-0.8	**4.5** ↓	**3.9** ↓	**5.1** ↓	**4.6** ↑	**3.3** ↓	**3.5** ↓	**3.7** ↓	4.0	**4.2** ↑	3.3	**3.2** ↓	3.1	3.0

Note: For some emerging economies, 2010-2011 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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Global Central Bank Watch

	Official interest rate	Current	Change from Aug '07 (bp)	Last change	Next meeting	Forecast next change	Sep 10	Dec 10	Mar 11	Jun 11	Sep 11
Global	GDP-weighted average	1.37	-329				1.39	1.43	1.48	1.57	1.62
excluding US	GDP-weighted average	1.96	-240				1.98	2.05	2.12	2.25	2.32
Developed	GDP-weighted average	0.54	-357				0.55	0.57	0.60	0.64	0.67
Emerging	GDP-weighted average	4.70	-216				4.74	4.87	5.01	5.25	5.40
Latin America	GDP-weighted average	6.60	-233				6.65	6.73	7.15	7.64	7.71
CEEMEA	GDP-weighted average	4.07	-279				4.04	4.06	4.08	4.32	4.80
EM Asia	GDP-weighted average	4.23	-187				4.29	4.49	4.57	4.71	4.76
The Americas	GDP-weighted average	0.88	-471				0.90	0.94	1.02	1.11	1.11
United States	Federal funds rate	0.125	-512.5	16 Dec 08 (-87.5bp)	21 Sep 10	On hold	0.125	0.125	0.125	0.125	0.125
Canada	Overnight funding rate	0.75	-350	20 Jul 10 (+25bp)	8 Sep 10	8 Sep 10 (+25bp)	1.00	1.50	2.00	2.50	2.50
Brazil	SELIC overnight rate	10.75	-125	21 Jul 10 (+50bp)	1 Sep 10	Jan 11 (+25bp)	10.75	10.75	11.50	12.50	12.50
Mexico	Repo rate	4.50	-270	17 Jul 09 (-25bp)	24 Sep 10	**On hold**	4.50	4.50	4.50	4.50	4.50
Colombia	Repo rate	3.00	-600	30 Apr 10 (-50bp)	24 Sep 10	1Q 11 (+50bp)	3.00	3.00	4.00	5.00	5.50
Peru	Reference rate	2.50	-200	5 Aug 10 (+50bp)	9 Sep 10	9 Sep 10 (+50bp)	3.00	4.00	4.50	4.50	4.50
Europe/Africa	GDP-weighted average	1.28	-324				1.29	1.29	1.30	1.39	1.50
Euro area	Refi rate	1.00	-300	7 May 09 (-25bp)	2 Sep 10	On hold	1.00	1.00	1.00	1.00	1.00
United Kingdom	Repo rate	0.50	-500	5 Mar 09 (-50bp)	9 Sep 10	May 11 (+25bp)	0.50	0.50	0.50	0.75	1.00
Sweden	Repo rate	0.50	-300	1 Jul 10 (+25bp)	2 Sep 10	2 Sep 10 (+25bp)	0.75	0.75	0.75	1.00	1.25
Norway	Deposit rate	2.00	-250	5 May 10 (+25bp)	22 Sep 10	2Q 11 (+25bp)	2.00	2.00	2.00	2.25	2.50
Czech Republic	2-week repo rate	0.75	-200	6 May 10 (-25bp)	23 Sep 10	2Q 11 (+25bp)	0.75	0.75	0.75	1.00	1.25
Hungary	2-week deposit rate	5.25	-250	26 Apr 10 (-25bp)	23 Aug 10	3Q 11 (+25bp)	5.25	5.25	5.25	5.25	5.50
Israel	Base rate	1.75	-225	26 Jul 10 (+25bp)	23 Aug 10	27 Sep 10 (+25bp)	2.00	2.25	2.50	2.75	3.25
Poland	7-day intervention rate	3.50	-100	24 Jun 09 (-25bp)	24 Aug 10	2Q 11 (+25bp)	3.50	3.50	3.50	3.75	4.00
Romania	Base rate	6.25	-75	4 May 10 (-25bp)	29 Sep 10	3Q 11 (+25bp)	6.25	6.25	6.25	6.25	6.50
Russia	1-week deposit rate	2.75	-25	31 May 10 (-50bp)	Aug 10	2Q 11 (+25bp)	2.75	2.75	2.75	3.25	3.75
South Africa	Repo rate	6.50	-300	25 Mar 10 (-50bp)	9 Sep 10	**9 Sep 10 (-50bp)**	6.00	6.00	6.00	6.00	6.00
Switzerland	3-month Swiss Libor	0.25	-225	12 Mar 09 (-25bp)	16 Sep 10	16 Dec 10 (+25bp)	0.25	0.50	0.75	1.00	1.25
Turkey	1-week repo rate	7.00	-1050	-	16 Sep 10	Jul 11 (+50bp)	7.00	7.00	7.00	7.00	8.25
Asia/Pacific	GDP-weighted average	2.24	-120				2.27	2.38	2.44	2.52	2.56
Australia	Cash rate	4.50	-175	4 May 10 (+25bp)	7 Sep 10	Nov 10 (+25bp)	4.50	4.75	5.00	5.25	5.50
New Zealand	Cash rate	3.00	-500	29 Jul 10 (+25bp)	15 Sep 10	15 Sep 10 (+25bp)	3.25	3.50	4.00	4.25	4.50
Japan	Overnight call rate	0.10	-43	19 Dec 08 (-20bp)	6 Sep 10	On hold	0.10	0.10	0.10	0.10	0.10
Hong Kong	Discount window base	0.50	-625	17 Dec 08 (-100bp)	22 Sep 10	On hold	0.50	0.50	0.50	0.50	0.50
China	1-year working capital	5.31	-126	22 Dec 08 (-27bp)	3Q 10	4Q 10 (+27bp)	5.31	5.58	5.58	5.85	5.85
Korea	Base rate	2.25	-225	9 Jul 10 (+25bp)	8 Sep 10	4Q 10 (+25bp)	2.25	2.50	2.75	2.75	2.75
Indonesia	BI rate	6.50	-200	5 Aug 09 (-25bp)	3 Sep 10	2Q 11 (+25bp)	6.50	6.50	6.50	6.75	6.75
India	Repo rate	5.75	-200	27 Jul 10 (+25bp)	16 Sep 10	16 Sep 10 (+25bp)	6.00	6.25	6.50	6.50	6.75
Malaysia	Overnight policy rate	2.75	-75	8 Jul 10 (+25bp)	2 Sep 10	On hold	2.75	2.75	2.75	2.75	2.75
Philippines	Reverse repo rate	4.00	-350	9 Jul 09 (-25bp)	26 Aug 10	1Q 11 (+25bp)	4.00	4.00	4.25	4.75	5.00
Thailand	1-day repo rate	1.50	-175	14 Jul 10 (+25bp)	25 Aug 10	25 Aug 10 (+25bp)	1.75	2.00	2.00	2.00	2.00
Taiwan	Official discount rate	1.375	-175	24 Jun 10 (+12.5bp)	3Q 10	3Q 10 (+12.5bp)	1.500	1.500	1.500	1.500	1.625

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

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Economic forecasts - Australia

Australia: economic projections *percentage change over previous period, seasonally adjusted annual rates, un*

				2009			2010				2011			
	2009	2010	2011	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Chain volume GDP	1.3	2.7	3.2	3.4	1.1	4.5	2.0	1.9	3.3	3.8	2.7	3.2	4.0	2.8
Private consumption	1.6	2.0	2.0	5.1	1.3	3.6	2.3	0.8	0.4	1.6	2.8	2.4	2.4	2.0
Construction investment	-0.5	1.5	6.0	-2.8	2.6	1.1	-3.3	4.7	6.2	6.4	5.5	5.0	7.9	7.8
Equipment investment	-3.4	6.9	9.5	0.1	-13.1	46.8	-20.9	27.3	12.9	17.5	5.1	3.4	6.4	8.6
Public investment	4.9	32.1	9.3	13.5	43.6	49.7	55.4	14.2	10.0	10.6	6.8	11.2	6.8	9.6
Government consumption	2.8	3.6	1.7	3.4	5.4	7.5	3.3	0.1	3.9	0.2	0.1	3.7	3.7	0.4
Exports of goods & services	1.4	1.7	2.7	8.4	-6.5	8.3	-2.0	3.2	2.4	2.8	2.0	2.8	3.2	4.1
Imports of goods & services	-7.8	10.9	4.1	3.5	18.0	36.6	7.3	0.0	3.2	3.2	4.1	6.1	3.2	8.2
Contributions to GDP growth:														
Inventories	-0.5	-0.9	-0.6	0.9	2.9	0.7	0.7	-8.1	0.0	-0.1	-0.2	0.1	-0.2	-0.1
Net trade	2.0	-1.9	-0.4	0.9	-4.6	-5.0	-2.0	0.6	-0.2	-0.2	-0.5	-0.8	-0.1	-1.0
GDP deflator (%oya)	0.2	3.1	2.4	0.1	-2.1	-1.5	1.4	4.1	3.7	3.2	2.2	2.4	2.5	2.5
Consumer prices (%oya)	1.8	3.1	3.6	1.5	1.3	2.1	2.9	3.1	3.0	3.3	3.5	3.8	3.6	3.4
Producer prices (%oya)	-5.4	1.6	3.5	-6.4	-7.2	-6.8	-0.2	1.4	1.1	4.0	2.5	3.5	4.0	4.0
Trade balance (A$ bil, sa)	-6.8	-18.7	-21.4	-0.9	-4.1	-5.0	-4.0	-4.7	-5.0	-5.0	-5.1	-5.2	-5.1	-6.0
Current account (A$ bil, sa)	-51.4	-35.7	-28.8	-12.7	-13.8	-18.5	-16.6	-7.6	-4.9	-6.7	-7.1	-7.0	-7.0	-7.7
as % of GDP	-4.1	-2.7	-2.0	-4.1	-4.4	-5.8	-5.1	-2.3	-1.5	-2.0	-2.1	-2.0	-2.0	-2.2
3m eurodeposit rate (%)*	6.0	4.7	5.6	3.5	3.4	4.1	4.3	4.8	4.8	5.1	5.4	5.6	5.6	5.7
10-year bond yield (%)*	5.6	5.7	6.3	5.5	5.1	5.8	5.6	5.5	5.9	6.1	6.2	6.3	6.4	6.4
US$/A$*	0.75	0.88	0.90	0.82	0.88	0.91	0.94	0.84	0.88	0.86	0.88	0.92	0.90	0.89
Commonwealth budget (FY, A$ bil)	-27.0	-51.0	-32.0											
as % of GDP	-2.1	-3.8	-2.3											
Unemployment rate	5.6	5.3	4.8	5.7	5.8	5.6	5.3	5.3	5.3	5.2	5.0	4.9	4.7	4.3
Industrial production	-7.9	3.3	1.5	4.8	-4.2	22.1	0.2	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** emerged from the global downturn largely unscathed. That said, we recently lowered expected GDP growth following our colleagues' growth downgrades for the US and China.
- **Business investment** probably will rise close to 10% in 2010-11, with mining leading the way, particularly with the mining tax roadblock being "dismantled". There will be a bigger rise in 2011-12.
- 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.
- **Consumer confidence** deteriorated sharply earlier this year as mortgage rates rose, but the index rebounded in July, and rose again in August. Optimists easily outnumber pessimists.
- **Export volumes** have held up owing mainly to firm demand from China, and the terms of trade has bounced thanks mainly to higher bulk commodity prices.
- The **RBA** hiked the cash rate six times between October and May, but then paused. The Bank will likely remain on the sidelines until November. We expect four further rate hikes throughout 2011.
- **Australian voters** have delivered a hung Parliament, the first since 1940. The Coalition looks likely to win the most seats and, therefore, is best-placed to be asked to form a government.

Economic forecasts - New Zealand

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

				2009			2010				2011			
	2009	2010	2011	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real GDP (1995-96 prices)	-1.7	2.9	2.9	0.3	1.2	3.7	2.3	4.4	3.8	2.2	2.3	3.4	3.2	2.2
Private consumption	-0.6	2.6	1.7	1.2	3.8	3.2	0.9	4.3	3.6	0.4	1.0	1.0	2.2	3.5
Fixed Investment	-12.5	0.1	4.1	7.1	-10.4	-7.2	3.3	4.5	4.6	4.1	2.2	4.1	6.0	7.3
Residential construction	-18.5	2.8	4.2	-8.4	-14.7	20.3	2.2	3.2	3.6	4.4	3.2	4.8	6.0	4.0
Other fixed investment	-11.3	-0.4	4.1	10.2	-10	-11.6	3.5	4.8	4.8	4.0	2.0	4.0	6.0	8.0
Inventory change (NZ$ bil, saar)	-1.8	0.7	0.7	-1.1	-0.7	0.2	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.1
Government spending	1.7	3.4	1.9	-3.9	2.6	4.5	6.7	2.4	1.6	2.4	1.6	2.4	2.0	0.4
Exports of goods & services	0.0	5.0	8.0	19.2	0.6	-2.7	5.5	8.0	8.0	8.0	8.0	9.0	7.0	7.0
Imports of goods & services	-15.2	8.9	5.8	-11.2	6.3	25.5	7.4	7.0	7.0	6.0	4.0	5.0	7.0	9.0
Contributions to GDP growth:														
Domestic final sales	-5.0	2.4	2.3	1.4	-1.9	1.1	4.0	4.1	3.5	1.6	1.4	1.9	3.1	3.9
Inventories	-2.6	1.9	0.0	-10.2	5.0	11.6	-0.9	0.2	0.1	0.1	-0.2	0.2	0.2	-0.9
Net trade	5.9	-1.4	0.6	9.9	-1.8	-8.3	-0.8	0.1	0.1	0.5	1.2	1.2	-0.1	-0.8
GDP deflator (%oya)	2.0	2.4	2.2	3.3	2.5	-0.1	1.0	1.9	2.8	3.9	2.8	2.4	1.9	1.6
Consumer prices	2.1	5.0	3.2	2.3	5.3	-0.7	1.5	1.1	5.5	12.1	3.3	1.8	3.9	3.8
%oya	2.1	2.6	4.9	1.9	1.7	2.0	2.0	1.8	1.8	4.9	5.4	5.6	5.2	3.2
Trade balance (NZ$ bil, sa)	2.5	5.7	5.3	0.8	0.7	0.3	0.9	1.6	1.5	1.6	1.5	1.3	1.3	1.2
Current account (NZ$ bil, sa)	-5.5	-5.0	-11.9	-0.4	0.1	-2.9	-1.2	-1.3	-1.0	-0.6	-2.1	-5.2	-3.6	-3.5
as % of GDP	-3.0	-2.6	-6.0	-0.9	0.1	-6.5	-2.8	-2.1	-1.3	-4.4	-7.3	-7.0	-5.4	-4.2
Yield on 90-day bank bill (%)*	3.0	3.2	4.7	2.8	2.8	2.8	2.7	2.9	3.5	3.8	4.3	4.8	4.9	5.0
10-year bond yield (%)*	5.5	5.5	5.0	5.7	5.7	5.9	5.9	5.7	5.3	5.1	5.1	5.1	4.9	4.9
US$/NZ$*	0.64	0.70	0.70	0.60	0.68	0.73	0.71	0.70	0.70	0.67	0.68	0.72	0.71	0.70
Commonwealth budget (NZ$ bil)	-4.0	-7.2	-7.1											
as % of GDP	-2.2	-3.8	-3.6											
Unemployment rate	6.1	6.5	5.8	5.9	6.5	7.1	6.0	6.8	6.7	6.4	6.0	5.9	5.7	5.7

*All financial variables are period averages

New Zealand - summary of main macro views

- The **New Zealand economy** expanded at a healthy clip of 0.6%q/q in 1Q. Economic growth should remain strong in 2Q and 3Q, underpinned by consumer spending, with consumers likely to bring forward spending ahead of the October 1 GST hike.
- That said, households are set to undergo a period of **consolidation**. As a result, private consumption will be sub-trend post GST hike, particularly given higher interest rates and softer house price growth.
- The **unemployment** rate shot up to 6.8% in 2Q from 6.0% in 1Q, and probably will maintain a 6%-handle in the foreseeable future. Actual hiring remains well-below long run averages and, with corporate profitability down, new hiring will likely be postponed.
- The **RBNZ** hiked the OCR 25bp in July. The accompanying commentary suggested that the pace and extent of further tightening will be more moderate than previously forecast. We now expect “only” 50bp of tigthening between now and year end.
- Headline **inflation** continued to hover around the middle of the RBNZ’s 1%-3% target range in the June quarter, although this precedes what we expect will be a series of elevated inflation prints over the coming year.
- Managing **inflation expectations** will be a growing challenge for the RBNZ, given the July 1 introduction of the amended ETS and the GST hike on October 1.

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Non-Japan Asia economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
23 Aug **Singapore:** CPI (1:00 pm) Jul 3.0%oya **Taiwan:** Unemployment rate (4:00pm) Jul 5.2%, sa IP (4:00 pm) Jul 21.9%oya **Thailand:** GDP (9:30 am) 2Q 8.9%oya *Holiday Philippines*	24 Aug **Korea:** External debt (8:00 am) 2Q10 **New Zealand:** RBNZ 2 year inflation expectation 3Q	25 Aug **Australia:** Construction work done (11:30 am) 2Q 3.0%q/q, sa **Korea:** Consumer survey (6:00 am) Aug 111.0 Index, nsa **Philippines:** Imports (9:00 am) Jun 5.1US$ mn **Thailand:** BoT monetary policy meeting (2:30 pm) Aug 25 bp hike	26 Aug **Australia:** Private capital expenditure (11:30 am) 2Q 1.5%q/q, sa **Hong Kong:** Trade balance (4:30 pm) Jul -27.9 HK$bn **Philippines:** GDP (10:00 am) 2Q 6.3%oya BSP Monetary policy meeting (5:00 pm) Aug no change **Singapore:** IP (1:00 pm) Jul 16.2%oya	27 Aug **Korea:** Current account balance (8:00 am) Jul 3.9 US$bn **Taiwan:** Leading index (4:00pm) Jul
During the week: Korea: FKI business survey Aug 111.5 Index, nsa Vietnam: CPI Aug 8.9%oya Trade balance Aug -1.2 US$ bn				
30 Aug **Australia:** Company operating profits (11:30 am) 2Q Inventories (11:30 am) 2Q **New Zealand:** Trade balance (10:45 am) Jul NBNZ business confidence (3:00 pm) Aug *Holiday Philippines*	31 Aug **Australia:** Pvt. Sector credit (11:30 am) Jul Retail sales (11:30 am) Jul Current account balance (11:30 am) 2Q Building approvals (11:30 am) Jul **Hong Kong:** Retail sales (4:30 pm) Jul India: GDP 2Q **Korea:** IP (8:00 am) Jul Leading index (8:00 am) Jul Service sector activity (8:00 am) Jul **New Zealand:** Building permits (10:45 am) Jul **Thailand:** Trade balance (2:30 pm) Jul IP (2:30 pm) Jul PCI (2:30 pm) Jul PII (2:30 pm) Jul *Holiday Malaysia*	1 Sep **Australia:** GDP (11:30 am) 2Q **China:** PMI manufacturing (9:00 am) Aug **India:** PMI manufacturing Aug Trade balance Jul **Indonesia:** Inflation (12:00 pm) Aug Trade balance (12:00 pm) Jul **Korea:** CPI (8:00 am) Aug **New Zealand:** ANZ commodity prices (3:00 pm) Aug **Thailand:** CPI (2:00 pm) Aug	2 Sep **Australia:** Trade balance (11:30 am) Jul **Malaysia:** Trade balance (6:00 pm) Jul BNM monetary policy meeting (6:00 pm) Sep **Singapore:** PMI (9:30 pm) Aug *Holiday Vietnam*	3 Sep **Indonesia:** BI rate announcement (2:00 pm) Sep **Korea:** GDP 2Q
During the week: Korea: Trade balance Aug				
6 Sep **New Zealand:** QV house prices Aug **Taiwan:** CPI (4:00 pm) Aug	7 Sep **Australia:** RBA cash target Sep **Philippines:** CPI (9:00 am) Aug **Taiwan:** Exports (4:00 pm) Aug	8 Sep **Australia:** Housing finance (11:30 am) Jul **New Zealand:** Manufacturing activity (10:45 am) 2Q	9 Sep **Australia:** Unemployment rate (11:30 am) Aug **Korea:** Bank of Korea monetary policy meeting Sep **Malaysia:** IP (5:00 pm) Jul **Philippines:** Exports (9:00 am) Jul *Holiday Indonesia*	10 Sep **China:** Trade balance Aug **India:** IP Jul *Holiday India, Indonesia, Malaysia, Singapore,*
During the week:				
13 Sep **China:** CPI (10:00 am) Aug PPI (10:00 am) Aug FAI (10:00am) Aug Retail sales (10:00 am) Aug IP (10:00 am) Aug **Korea:** Export, Import price index (12:00 pm) Aug *Holiday Indonesia*	14 Sep **Australia:** NAB business confidence (11:30 am) Aug **New Zealand:** Retail sales (10:45 am) Jul **India:** WPI (11:00 pm) Aug	15 Sep **Australia:** Westpac consumer confidence (10:30 am) Sep Dwelling starts (11:30 am) 2Q **Philippines:** Unemployment rate Jul **Korea:** Unemployment rate (8:00 am) Aug	16 Sep **Hong Kong:** Unemployment rate (4:30 pm) Aug **India:** RBI monetary policy meeting Sep **New Zealand:** Business NZ PMI Aug RBNZ official cash rate Aug **Singapore:** Retail sales (1:00 pm) Jul *Holiday Malaysia*	17 Sep **Singapore:** NODX (1:00 pm) Aug
During the week: China: FDI Aug				

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
23 - 27 August	23 August	24 August	25 August	26 August	27 August
	Euro area • PMI flash (Aug) • EC cons conf (Aug) Hungary • NBH mtg: no chg Israel • BoI mtg: no chg Taiwan • IP (Jul)	Belgium • BNB bus conf (Aug) Germany • GDP final (2Q) Poland • NBP mtg: no chg South Africa • GDP (2Q) United States • Existing home sales (Jul) • Richmond Fed surv (Aug)	Germany • IFO bus surv (Aug) Japan • Trade balance (Jul) Thailand • BoT mtg: +25 bps United States • Durable goods (Jul) • New home sales (Jul)	Germany • GFK cons conf (Sep) Italy • ISAE cons conf (Aug) Netherlands • CBS bus conf (Aug) Philippines • BSP mtg: no chg Singapore • IP (Jul) Spain • GDP final (2Q) United States • KC Fed surv (Aug)	Germany • CPI prelim (Aug) Japan • Unemployment rate (Jul) • Core CPI (Jul) United Kingdom • GDP (2Q) United States • GDP revision (2Q) • UMich cons sent (Aug) • Bernanke speech
30 Aug - 3 Sep	30 August	31 August	1 September	2 September	3 September
Germany • Retail sales (Aug) Korea • Trade balance (Aug) Russia • CPI (Aug) • CBR mtg: no chg	Euro area • EC bus conf (Aug) • EC cons conf final (Aug) Poland • GDP (2Q) United States • Personal income (Jul) • Dallas Fed surv (Aug)	Brazil: IP (Jul) Euro area • Unemployment rate (Aug) • HICP flash (Aug) Germany • Labor mkt report (Jul/Aug) India: GDP (2Q) Japan • Mfg PMI (Aug) • IP prelim (Jul) • Shoko-Chukin surv (Aug) Korea: IP (Jul) United States • CB cons conf (Aug) • FOMC minutes (Aug) • Case-Shiller HPI (Jun)	Australia • GDP (2Q) Brazil • COPOM mtg: no chg Japan • Auto regs (Aug) United States • ADP employment (Aug) • ISM mfg (Aug) • Auto sales (Aug) Global mfg PMIs (Aug)	Euro area • GDP revision (2Q) • ECB mtg: no chg Malaysia • BNM mtg: no chg Sweden • Riksbank mtg: +25bps United States • Prod & costs revision (2Q) • Pending home sales (Jul) • Factory orders (Jul)	Brazil • GDP (2Q) Euro area • Retail sales (Jul) Indonesia • BI mtg: no chg Japan • MoF corporate surv (2Q) Korea • GDP (2Q) United States • Employment (Aug) • ISM nonmfg (Aug) Global serv PMIs (Aug)

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