

Australia and New Zealand - Weekly Prospects

Summary

- The week ahead in **Australia** is quiet, with just the 4Q dwelling starts data due for release on Wednesday. The highlight of the week, therefore, will be the release Tuesday of the minutes from the RBA's March Board meeting, at which officials chose to deliver another rate hike. The tone will be upbeat, as before. One point of particular interest will be any discussion on consumers, and how they are coping with the rate hikes already delivered. Uncertainty over this seemed to be the main reason the RBA paused in February. The details of last week's employment report for February were firm, even though the jobless rate ticked up a notch; the economy held on to the stellar job gains of recent months and hours worked soared 2.4% over the month. The report confirmed that further official rate rises are ahead, although we continue to believe the RBA will wait until early May before hiking again.
- **RBNZ** Governor Alan Bollard said in the statement accompanying last week's 'no change' decision that higher bank funding costs are doing some of the heavy lifting on the policy front. This comment, though, failed to alter our forecast that the RBNZ will deliver the first rate hike in July. Bollard highlighted recently that the official cash rate (OCR) was not lowered in 25bp hops so, when the recovery appears sustainable, there could be some "meaty chunks" on the upside. Those "meaty chunks" will not match the 100bp or 150bp moves we saw on the way down, but 50bp moves are likely given the amount of policy stimulus that needs to be removed; we forecast 50bp hikes in July and September. The OCR currently is at a record low of 2.5%.
- Last year's biggest macroeconomic surprise came from the household sector, which delivered the decisive spark lifting the **global economy** out of recession. The consumer's rapid swing from deep contraction to above-trend spending gains directly boosted growth while also prompting large changes in financial markets and business decisions. Indeed, global manufacturers have been playing catch-up, adjusting levels of production to better-than-expected news on final demand. This development has sustained a double-digit pace of global industrial activity gains for more than six months now. To be sure, the lift by consumers was supported by substantial fiscal stimulus that is now fading. However, there are strong reasons to believe that the global consumer will continue to provide surprisingly solid support for growth this year, even as fiscal supports fade from the scene.
- **China's** inflation rate was higher than expected at 2.7% oya in February. The reading raises the question of whether the economy might be overheating and elicit a strong policy response. Although a more broad-based tightening in policy does appear imminent, the chances that Chinese authorities will take forceful action to slow the economy appear low. For one thing, the pickup in inflation in China largely is limited to food, whereas non-food inflation is barely above zero. In addition, while there were signs of a healthy rebalancing in January/February activity data—with exports accelerating alongside a moderation in investment—there also were hints that GDP growth might be softer than expected this quarter. In particular, sequential gains in both IP and retail sales are relatively sluggish in the quarter-to-date when compared with our forecast for growth in GDP (9.8%q/q saar).

This week's highlight

The RBA Board minutes Tuesday should include colour on Board members' deliberations on the strength of the household sector. Conspicuously, there was no comment on consumers in the policy statement two weeks ago.

March 15, 2010

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Data and event previews - Australia and New Zealand

Date	Time ^(a)	Data/event	Forecast		Previous
			JPMorgan	Consensus ^(b)	
Monday, March 15	11.30am	Aust. lending finance (%m/m, Jan.)	na	na	-4.7
Tuesday, March 16	11.30am	RBA Board minutes (Mar.)	na	na	na
Wednesday, March 17	10.30am	Aust. Westpac Leading Index (%m/m, Jan.)	na	na	0.5
Wednesday, March 17	11.30am	Aust. dwelling starts (%q/q, 4Q)	5.0	na	9.4
Wednesday, March 17	12.00pm	RBA Assistant Governor Debelle panel discussion	na	na	na
Thursday, March 18	11.00am	Westpac-ACCI survey of industrial trends (1Q)	na	na	na
Thursday, March 18	1.00pm	NZ ANZ-RM consumer confidence (%m/m, Mar.)	na	na	-5.9
Friday, March 19	8.45am	NZ visitor arrivals (%m/m, Feb.)	-4.0	na	-2.4
Friday, March 19	1.00pm	NZ credit card spending (%m/m, Feb.)	0.4	na	1.5

(a) Australian Eastern Standard Time.

(b) Consensus based on Bloomberg survey.

Australia

RBA Board minutes (Mar.) - The Board minutes will discuss in detail the Reserve Bank's decision two weeks ago to hike the cash rate a further 25bp. In particular, we will be looking for any comments on the consumer, who failed to crack a mention in the statement at the time of the rate hike announcement. Prior to the March rate hike, the RBA Board appeared reluctant to hike again owing to the significant amount of uncertainty about how households were coping with the tightening already delivered.

Dwelling starts (%q/q, 4Q) - Dwelling starts probably rose a further 5% in 4Q. Building approvals were up 13% over the quarter, as continued house price appreciation increased the expected returns to housing investment. A prolonged rise in new home construction would be a welcome development given Australia's substantial housing shortage. In a speech last week, RBA Assistant Governor Lowe remarked that the undersupply of housing cannot be blamed on underinvestment per se. Rather, investment has been increasingly directed toward renovation activity rather than the production of new stock. This provides another perspective through which Australia's high house prices 'make sense'—resources have been dedicated to improving quality rather than quantity. This fact does little to put policymakers at ease, however. Higher prices transfer wealth to property holders at the expense of prospective buyers, and increasing inequality can only complicate monetary policy deliberations by increasing the political and welfare-related difficulties of 'one size fits all' policy.

RBA Assistant Governor Debelle participates in panel discussion - The Assistant Governor (Financial Markets) is a panel discussant at the Mortgage and Finance Association of Australia's Industry Leaders Luncheon in Melbourne. The discussion will focus on current complexities and trends in the housing market. A Q&A session will follow.

Data previews - contd.

New Zealand

NZ visitor arrivals (%m/m, Feb.) - Short-term visitor arrivals to New Zealand probably fell another 4% m/m in February. Arrivals from Australia probably will be solid, thanks to the effective promotion of New Zealand as a destination for Australian travellers, but will not be enough to offset declines in tourist visits from elsewhere.

NZ credit card spending (%m/m, Feb.) - Credit card spending jumped 1.5% m/m in January, but will likely pull back in February to be up 0.4%. Households are becoming increasingly cautious, mainly owing to growing expectations that the recovery in the labour market will be slow. Business confidence may be rising, but business lending remains weak, implying that investment will be subdued this year; this has weighed on the employment outlook.

Australia

- **Home loans plunged, but consumer confidence stayed high**
- **Aussie labour market took a breather in February**
- **RBA board minutes the focus this week**

Of the mixed bag of economic data released in Australia last week, the employment numbers were the highlight. Although employment was flat in February and the jobless rate ticked up a little, the RBA will be wary of the clear tightening in the labour market over the last six months. Also, the rapid swelling of the investment pipeline will boost employment, so conditions will become increasingly tight. Wage increases triggered by emerging skill shortages will place upward pressure on inflation, reaffirming our view that the cash rate has further to rise in 2010.

RBA minutes to explain March hike

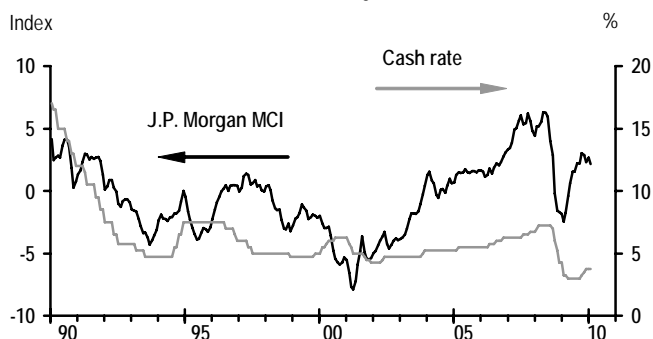
On Tuesday, the Reserve Bank will release the minutes of the March Board meeting, at which members raised the cash rate another quarter-point to 4%, the fourth hike since October. The minutes will expand on the upbeat commentary that accompanied the decision two weeks ago. It will be interesting to see if there is an explicit mention of the Aussie consumer, which was strangely absent at the time of the rate hike announcement. We had expected an “unchanged” outcome back in March, mainly owing to perceived uncertainty about how consumers were coping with the tightening already delivered. In February, it seemed that officials left the cash rate unchanged because evidence on how the economy (and, in particular, the household sector) was handling the earlier rate hikes was “mixed.”

Nonetheless, the process of monetary policy normalization has much further to run; we continue to forecast a cash rate of 5% by year end, with the next 25bp move to be delivered in May. That said, a run of unexpectedly firm data could see the RBA deliver a back-to-back hike in April. Indeed, every Board meeting from here is “live.”

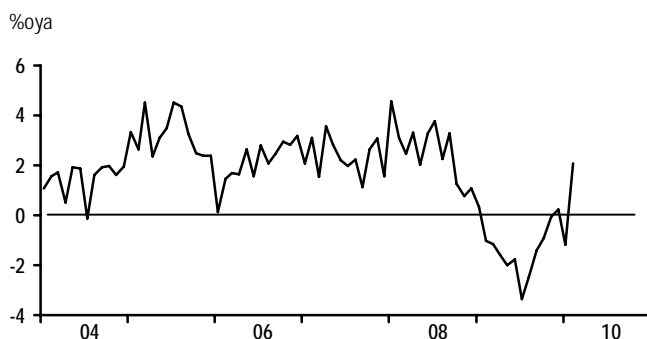
Workers' hours spiked in February

Employment gains in February moderated sharply, as expected. The economy added just 400 jobs last month (J.P. Morgan: 10,000; consensus: 15,000), significantly less than the 56,500 jobs added in January. The 11,400 full-time jobs added were offset by an 11,000 decline in part-time jobs. The moderation in employment growth was partly payback for several months of astonishing gains and following the

Australia: RBA cash rate and monetary conditions



Australia: aggregate hours worked



release of patchy leading indicators of employment. The ANZ job advertisements series, for example, plunged 8.1% m/m in January.

The jobless rate rose from 5.2% to 5.3% and probably will remain sticky around current levels near-term as workers' hours, which were cut significantly in 2009, are reinstated. Hours spiked 2.4% m/m in February, easily reversing the declines recorded in the previous two months. Firms will rebuild reduced hours of existing staff before hiring new workers, meaning the shift from part-time to full-time work will continue. The unemployment rate, though, probably already has peaked at 5.8%, having topped-out less than 2%-pts above the trough reached in February 2008; this is a stark contrast to the sharp rises recorded elsewhere. Indeed, the Aussie labour market has proved resilient, with 198,000 jobs having been added since September last year.

RBA officials will be feeling anxious about the labour market outlook. The swelling investment pipeline and strong demand for Australia's key commodity exports means that significant employment gains are likely to be recorded in the resource-rich states in the latter six months of the year. In the heart of the mining boom in Western Australia, for ex-

ample, the unemployment rate has dropped to just 5.0%, and thanks to another 4,400 jobs being added in February, employment is now at a nine-month high.

Housing finance falling off a cliff

The total number of home loan commitments issued in Australia nose-dived 7.9% m/m in January (J.P. Morgan: +3.0%; consensus: +2.0%), having already plummeted 14% between September and December 2009. We had forecast a minor rebound in January, given the collapse in demand for loans that accompanied the phasing down of the expanded First Home Buyers' (FHBs') grant and the RBA's three consecutive 25bp rate hikes in 4Q09. The early message from last week's data is that the hangover from the Government's intervention may be more significant, and depress activity for longer than many anticipated.

The proportion of commitments logged by FHBs continued to fall to 20.5% and is now approaching historical norms after reaching an all-time high of 28.5% in May last year. Fixed rate loans fell for the seventh straight month and now account for just 2.5% of the total. While the official cash rate is expected to rise further, pricing for fixed rate loans will remain prohibitive relative to variable rate loans for some time yet.

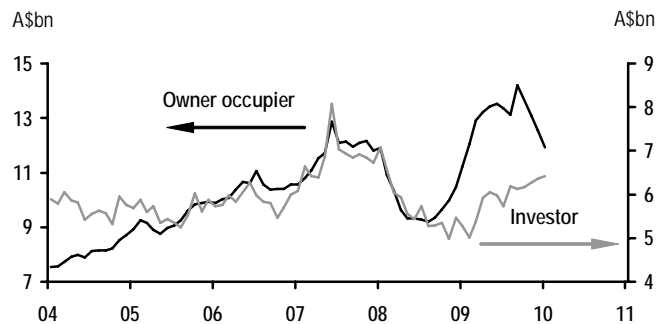
The value of home loans issued fell 5% m/m in January. Both the number of loans and the average loan commitment of FHBs fell over the month, which would have depressed the outcome. On the other hand, average loan sizes for non-FHBs continue to rise, though demand is tracking at a lower volume than in December. Loans for investment purposes pushed up 0.9% over the month, with investors accounting for 30% of all loans issued in value terms.

Given that the expanded grant ended on December 31, price caps on the original grant became effective on January 1, and with mortgage rates poised to rise further, loan demand will face significant headwinds in 2010. With building approvals starting 2010 on a soft note, the last domino to fall is house prices. Our forecast is for the rapid pace of house price appreciation to moderate. The undersupply of housing will continue to support house prices, albeit in a fairly undesirable fashion.

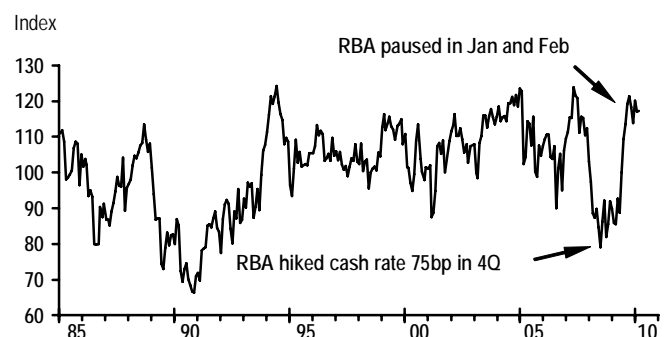
Consumer confidence still elevated

Consumer confidence in Australia, as measured by the

Australia: housing finance



Australia: Westpac-Melbourne Institute consumer confidence index



Westpac-Melbourne Institute (WMI), unexpectedly improved in March, albeit by a mere 0.2% m/m. We had anticipated a fall in confidence owing to the RBA's decision to hike the cash rate a further 25bp two weeks ago. Despite the official cash rate increase and expectations of further rate increases down the track, consumer sentiment toward family finances one year ago and one year ahead posted the largest increases, rising 1.4% m/m and 5.5%, respectively.

As highlighted by the WMI, mortgage rates have yet to reach the point where increases are having a major impact on confidence. This is partly because the majority of mortgage holders maintained their monthly repayments over the course of the RBA's easing cycle. As highlighted by the WMI, in the last cycle, when the average standard variable mortgage rate reached 7.25% (compared to around 6.9% today), households became much more sensitive to rate hikes. With standard variable mortgage rates approaching these levels, consumer sensitivity to rate hikes will soon increase. Thus, we expect to see significant monthly drops in confidence going forward—when the RBA lifted the cash rate 175bp to 7.25% between 2006 and 2008, the average fall in the index after each 25bp rate hike was 8.5%.

Data releases and forecasts

Week of March 15 - 19

Wed Mar 17 10:30am	WMI leading index sa				
	%m/m	Oct	Nov	Dec	Jan
		0.5	1.0	0.5	—

Wed Mar 17 11:30am	Dwelling starts sa				
	(%q/q)	1Q09	2Q09	3Q09	4Q09
		-1.2	-1.9	<u>9.4</u>	<u>5.0</u>

Dwelling starts probably rose a further 5% in the December quarter. Building approvals were up 13% in 4Q, as continued house price appreciation increased the expected returns to housing investment.

Review of past week's data

ANZ job advertisements

		Dec	Jan	Feb	
	%m/m, sa	6.0	-8.1	<u>-3.0</u>	19.1

NAB monthly business survey

% balance, sa		Dec	Jan	Feb	
Business confidence		8	15	<u>15</u>	19

WMI consumer confidence survey

100=neutral, sa		Jan	Feb	Mar	
%m/m		5.5	-2.6	<u>-3.5</u>	0.2

Housing finance approvals: owner occupiers

Number of loans, sa		Nov	Dec	Jan	
%m/m		-6.1	-6.2	-5.5	-5.1
%oya		13.4	13.3	0.4	0.2
				<u>3.0</u>	-7.9
				-1.4	-12.0

Labour force

		Dec	Jan	Feb	
Unemployment rate (% , sa)		5.5	5.3	5.2	5.4
Employed (000 m/m, sa)		37.5	37.4	52.7	56.5
Participation rate (% , sa)		65.3	65.3	65.3	65.2

New Zealand

- **RBNZ left rates unchanged and maintained rhetoric**
- **Underlying retail sales very weak**
- **Terms of trade jumped in 4Q**

The statement that accompanied the RBNZ's decision to leave the official cash rate at a record low last week was slightly more dovish than that delivered six weeks ago. We anticipated this, however, given global jitters and a string of weak domestic data. It appears Governor Bollard wants hard evidence that the recovery underway is sustainable. With that in mind, we continue to believe the Governor will sit on the sidelines until after the late-June release of the 1Q GDP report, before delivering the first hike in July.

RBNZ on hold, statement more dovish

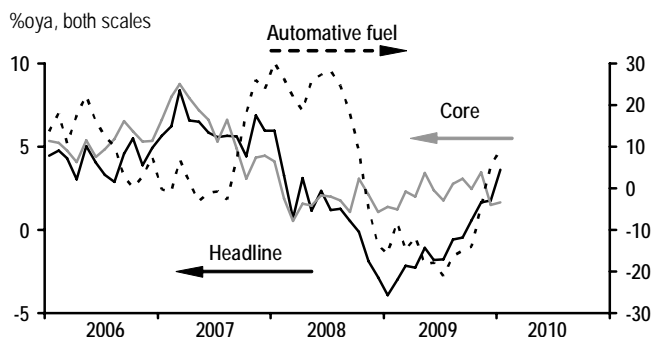
The RBNZ left the official cash rate (OCR) at a record low 2.5% last week, as expected. Although the statement was slightly more dovish than the previous edition, Governor Bollard reiterated that the policy stimulus may be removed "around the middle of 2010," providing the economy continues to recover in line with the Bank's forecasts. This appears to be the case, with the Governor stating that the "economy is recovering broadly as expected and growth is predicted to pickup further through 2010."

Unlike in the previous statement in January, the RBNZ highlighted that higher bank funding costs are doing some of the heavy lifting on the policy front. In the MPS, the Bank noted that the marginal cost of funds is around 150bp above the OCR. This, though, has not changed our view that the RBNZ will kick off the next tightening cycle in July with a 50bp hike. Bollard has said previously 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. Those "meaty chunks" will not, however, match the 100bp or 150bp moves we saw on the way down given that elevated bank funding costs are reducing the extent of future increases in the OCR.

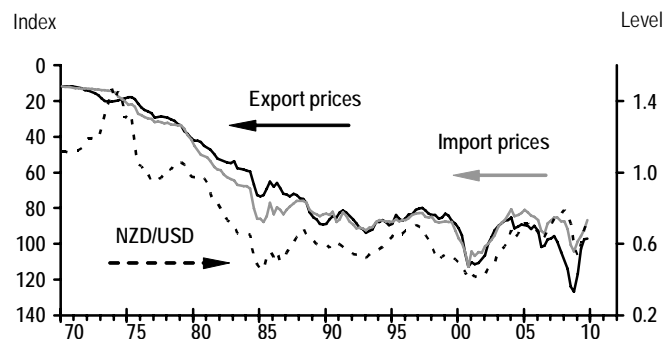
We still expect a 50bp hike to kickoff the next tightening cycle in July. Bollard appears to want hard evidence that the recovery is sustainable so the RBNZ probably will sit on the policy sidelines until after the late-June release of the 1Q GDP report. The RBNZ expects quarterly GDP growth of 0.9% in 1Q10, compared to our forecast of 0.8%.

On the domestic front, Dr. Bollard highlighted that consumer confidence and household spending have improved,

New Zealand: retail sales



New Zealand: export and import prices



but business spending and credit growth remain subdued. Indeed, in over-year-ago terms, growth in business lending is negative and lending to the agricultural sector has slipped back into single digit territory. On the household side, consumer lending has fallen for 11 straight months and housing credit growth has remained stable with a 3%-handle despite the spike in housing activity toward the end of 2009. On the latter, the RBNZ made a point of highlighting the fact that house sales remain subdued, which will ease the RBNZ's concerns about the potential reemergence of debt-fueled housing excesses. The pickup in house prices toward the end of 2009 was remarkably strong, but gains since then have tapered off. In the Monetary Policy Statement that accompanied the announcement, the RBNZ highlighted that potential changes to the taxation of property may also weigh on house prices in the medium-term.

Risks around the global outlook have increased, according to Bollard, but trading partner growth has recovered "a little faster than expected," with activity strongest in China, Australia, and emerging Asia. The statement was a little more dovish with respect to growth in other trading partners, though, which the RBNZ says is "more muted."

The RBNZ remains comfortable with the inflation outlook, with annual CPI inflation set to track within the Bank's 1%-3% target range in the medium-term. There may be some upward pressure on headline inflation in the short-term, however, owing to the implementation of the amended Emissions Trading Scheme and increases in accident compensation charges. The RBNZ appears willing to look through these temporary factors. We believe, though, that inflationary pressures will become a growing concern in the latter months of the year, as domestic prices rise and excess capacity continues to diminish.

Underlying retail sales weak

Retail sales values spiked in New Zealand in January, but the headline masks a relatively weak picture of consumer spending. Sales were up 0.8% m/m (J.P. Morgan: 0.2%, consensus: 0.5%), after falling 0.4% in December, with the upside surprise driven by the vehicle-related industries, owing to continual gains in petrol prices. More importantly, core sales were up just 0.3% m/m (J.P. Morgan: 0.2%, consensus: 0.7%), after tumbling 2.0% in the previous month, which was the largest fall on record. Low interest rates and solid net permanent migration flows probably prevented an even weaker reading on the core measure.

The weakness in core retailing reaffirms our view that any recovery in consumer spending this year will be relatively benign. With housing market activity moderating and labour market conditions weak, households will remain cautious. Add to this the recent rises in petrol prices and the expected increase to the GST to 15% in October, and the retail environment won't be a favourable one.

Terms of trade spiked in 4Q

After declining for six straight quarters, New Zealand's terms of trade jumped 5.7% q/q in 4Q (J.P. Morgan: 0.6%), marking the largest rise since 1Q76. The terms of trade shot well beyond our forecast, owing to a sharper than expected drop in import prices (-5.8%). Export prices also fell, but only modestly (-0.3%).

It was also reported that export volumes tanked 1.2% q/q in 4Q, marking the first fall since 3Q08, and import volumes

rose 1.6%. Net exports will, therefore, subtract significantly from 4Q GDP growth. As a result, we have trimmed our preliminary GDP growth forecast to 0.6% q/q, having also taken into account other data released last week on construction and manufacturing—both look set to provide a positive contribution to GDP growth. Manufacturing sales volumes rose 3.1% in 4Q and a rise in home construction led to a 0.7% increase in building work put in place.

Data releases and forecasts

Week of March 15 - 19

	Nov	Dec	Jan	Feb
Visitor arrivals				
Fri Mar 19 10:45am nsa				
Total (%m/m)	-4.7	8.0	-2.4	<u>-4.0</u>
Net permanent immigration				
Fri Mar 19 10:45am nsa				
Monthly (000s)	2.5	1.4	2.5	—
12 month sum (000s)	20.0	21.3	22.6	—
Credit card spending				
Fri Mar 19 3:00pm % change				
%oya	1.6	1.9	2.6	<u>0.4</u>

Review of past week's data

	2Q09	3Q09	4Q09	
Terms of trade				
(%q/q)	-9.4	-1.3	-1.6	<u>0.6</u> 5.7

Business PMI

	Dec	Jan	Feb
Index, sa	53.0	52.0 52.1	— 53.3
(%oya)	25.4	23.0	— 35.5

RBNZ cash rate announcement

No change delivered. See main text.

Retail trade

	Nov	Dec	Jan
%m/m	0.8 0.9	0.0 -0.4	<u>0.2</u> 0.8
%oya	1.6	1.7	2.2 1.8 <u>3.4</u> 3.6

Global Essay

- **Global consumption on track for solid gains even as fiscal supports fade**
- **China's rising inflation and slowing growth news likely to be tempered when March data are released**
- **Japan's growth news is positive, but deflation is intensifying**
- **This week: A quiet Fed, more QE from the BoJ, and a 50bp hike from COPOM**

Spend and delever

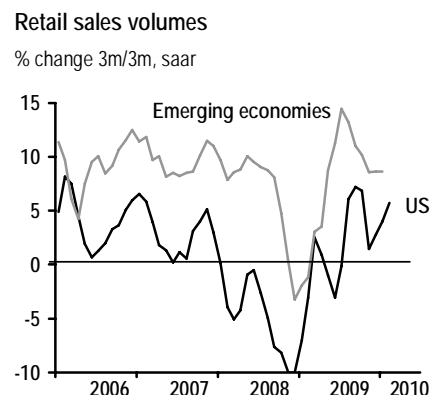
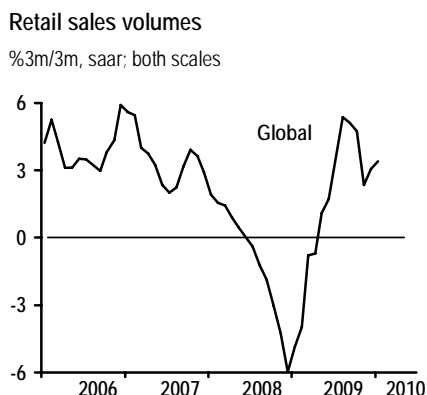
Last year's biggest macroeconomic surprise came from the household sector, which delivered the decisive spark lifting the global economy out of recession. The consumer's rapid swing from deep contraction to above-trend spending gains directly boosted growth while also prompting large changes in financial markets and business decisions. Indeed, global manufacturers have been playing catch-up, adjusting levels of production to better-than-expected news on final demand. This development has sustained a double-digit pace of global industrial activity gains for more than six months now. To be sure, the lift by consumers was supported by substantial fiscal stimulus that is now fading. However, there are strong reasons to believe that the global consumer will continue to provide surprisingly solid support for growth this year, even as fiscal supports fade from the scene.

- **Labour markets are turning.** Outside of periods of major financial and policy shocks, labour market developments are the key factor determining the pace of household spending. It appears that labour income is again growing in the developed world, and we expect material job gains in the coming months. The establishment of a positive employment trend will outweigh the drags in train from fading fiscal stimulus.

- **Shifting centers of gravity.** Bolstered by China and India, labour income and employment is already growing at a solid pace across emerging economies. This development takes on increasing significance in the aftermath of a decade in which EM consumers have sharply increased their share of the global consumption pie. The EM consumer now accounts for more than one-third of global spending (up from 23% at the start of the last global expansion). Thus, the relative health of EM households, along with continued purchasing power gains from rising currencies, should provide important support for global demand. Our aggregate emerging market retail sales volume index grew at a robust 9% pace last year. Although some rotation is in train as China cools and other countries gather steam, increases at this pace look likely to be sustained.

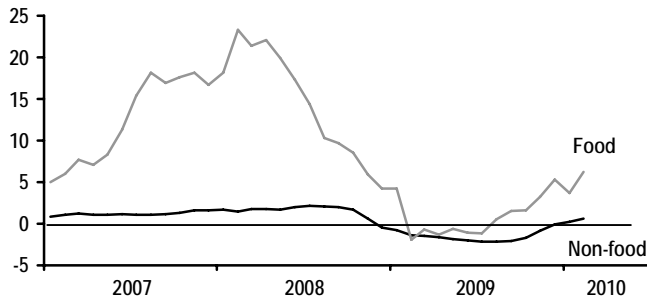
- **US households spend and delever.** Discussion of the outlook for US consumers often focuses on the dynamics of household debt and the need for further balance sheet adjustment. However, US household debt is predominantly mortgage obligations. As such, the recent declining trend of household debt will continue in the coming quarters as a result of a large foreclosure pipeline and the low turnover in the housing market, which will keep amortization exceeding net originations of mortgages. In an environment in which home prices and credit conditions stabilize, spending will likely grow alongside delevering, propelled by rising labour income and consumer confidence.

Our forecast for 2.7% US consumption growth this year incorporates lift that is tempered by drags related to credit availability that keeps the saving rate on a modest upward trajectory. Last week's February retail sales report leaves real consumer spending tracking nearly 3.5% this quarter, an impressive outcome given drags expected from last month's storms. It is premature to extrapolate the latest



China consumer prices

% ch over 12 months



good news, but we recognize that the risks to our 2010 consumption forecast are skewed to the upside given the depth of the downturn in discretionary spending and prospective improvement in labour markets.

Japan: expected slowing not yet visible

Japan is also producing surprisingly strong consumption growth alongside a general trend of positive news. With a 1% m/m increase in the January consumption index, 1Q10 consumption growth will exceed our modest estimate of 0.5% annualized. In addition, the Economy Watchers survey continued to gain ground, similar to the already-released Shoko Chukin survey, which suggests that the hit to business sentiment from the sharp tightening in financial conditions in late 2009 has dissipated. Finally, the revision to the 4Q GDP report was encouraging, as the solid growth of final sales—including the modest rise in capex—was left unchanged, while the inventory contribution was marked down to negative territory. In all, the risks to our 1Q GDP growth forecast (1.8% q/q saar) have shifted to the upside.

Despite this growth picture, the rate of core price inflation has intensified to exceed -1% oya, due to the economy's large output gap. Alarmed by this development, the government has put increased pressure on the Bank of Japan to implement new policy measures. Odds are that the BoJ will announce new QE measures at this week's policy meeting, although any changes are likely to be modest. The BoJ's most likely step is to expand the fund-supply operation it adopted in December, either by raising the amount from 10 trillion yen or extending the duration of loans beyond three months. The BoJ also could adjust its policy statement to include a commitment to maintain its easy monetary policy for an extended period, similar to the Fed. The BoJ is not likely to announce an increase in its purchases of government bonds this week.

China: look to March data for guidance

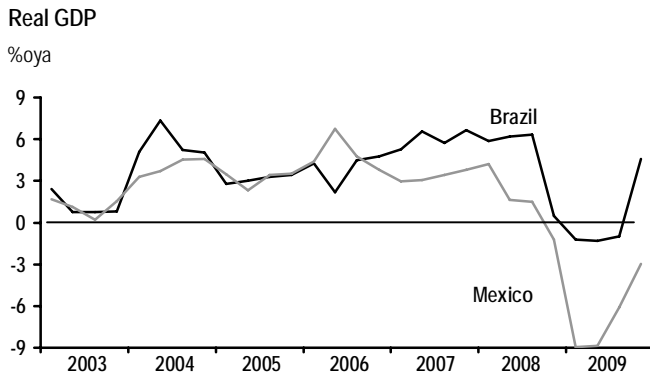
China's inflation rate was higher than expected at 2.7% oya in February. The reading raises the question of whether the economy might be overheating and elicit a strong policy response. Although a more broad-based tightening in policy does appear imminent, the chances that Chinese authorities will take forceful action to slow the economy appear low. For one thing, the pickup in inflation in China largely is limited to food, whereas non-food inflation is barely above zero. In addition, while there were signs of a healthy rebalancing in January/February activity data—with exports accelerating alongside a moderation in investment—there also were hints that GDP growth might be softer than expected this quarter. In particular, sequential gains in both IP and retail sales are relatively sluggish in the quarter-to-date when compared with our forecast for growth in GDP (9.8% q/q saar). That said, interpretation of the data is clouded by multiple factors, including the Lunar New Year holiday, unusually harsh winter weather, and previous policy tightening.

In sum, March data will be critical to determining the path of both inflation and growth, and thus policy. We think headline inflation will increase more gradually from here and peak near 4% as food inflation levels off. Likewise, we look for large monthly gains in March IP and retail sales to leave our GDP forecast on track. If events play to this script, policymakers appear set to enact additional, modest tightening measures in the next few months. Another hike in banks' RRR could come at any time, followed by an initial interest rate hike in mid-April (after receipt of March data), and a rise in CNY/USD by June.

Greek progress report to be endorsed

The Greek government has responded aggressively to pressure for fiscal consolidation. To follow up the fiscal tightening of 5%-pts of GDP announced in the stability program published in January, 2%-pts of tightening were added last week to compensate for the optimistic growth projections contained in the original program. In whole, Greece is committed to a degree of fiscal tightening that no other Euro area country has ever achieved. The largest tightening seen to date was in Belgium in 1982, when the fiscal drag was 5.3%-pts of GDP.

Considerable risks surround the ability of the Greek government to implement these measures, a fact underlined last week by a fresh wave of protests in Athens. With this in mind, it is encouraging that many of the proposals have already been enacted. According to a treasury newsletter



published last week, roughly half of the proposed tightening measures have been passed into law. Consequently, the Greek progress report to be reviewed by the EU Council of finance ministers next Tuesday (March 16) will likely be enthusiastically endorsed. This endorsement will open the door for Greece to receive financial assistance if necessary.

In response to rising sovereign credit concerns across the Euro area, some are now suggesting a European Monetary Fund (EMF) that would supplant the need for any distasteful future IMF involvement. A German proposal along these lines is to increase the penalties for failing to abide by the fiscal criteria of the stability pact and to create a mechanism for temporary, conditional intra-regional financial support if necessary. It remains to be seen whether the rest of the region signs on to the German proposal, and it is unclear whether an EMF would need a formal treaty revision. In any event, it would be a long-term project, and would not be available to help in the near term.

Mexico-Brazil policy divergence widens

Monetary authorities will meet in Brazil and in Mexico this week, but the similarities end there. In Brazil, growth and inflation indicators suggest that the tightening cycle is already overdue, with rising utilization rates and increasing inflation expectations raising the likelihood that inflation will soon exceed the central bank's target. Last week's 4Q09

GDP and January's retail sales reinforced this perception that Brazil is now booming. Consequently, we expect Brazil's COPOM will begin its tightening cycle with a 50bp hike at this week's meeting.

In sharp contrast to Brazil, economic activity in Mexico remains well off its prior peak and, although recently enacted tax measures are temporarily lifting consumer price inflation, underlying price pressures are to the downside. Recent wage negotiations have generated modest increases while inflation expectations have been well anchored. These factors combined with dovish comments from central bank officials, have led us to push back our forecast for Banxico's first rate hike from June to October.

The current divergence is rooted in the different reactions of each country to the financial crisis. While Brazil was able to ease rates by 500bp and implemented a large fiscal stimulus package to stimulate consumption, Mexico pushed down its monetary policy rate less and actually tightened its fiscal stance. Moreover, Mexico's tight trade linkages with the US and Brazil's greater linkages to EM Asia have amplified the growth differences.

Russia: CBR still in rate cutting mode

Russia's policymakers are fearful that a strengthening currency in response to the expanding commodity sector will damage the competitiveness of the manufacturing sector. However, the near-term threat of import substitution will stay modest as long as domestic demand is likely to remain soft. In fact, we maintain that the current account surplus will reach close to 5% of GDP this year. At the same time, with economic activity still well off its prior peak and capital inflows adding further upward pressure to the ruble, core inflation is likely to continue moving down. Consequently, we expect the CBR to proceed with monetary easing in the coming months, with a 25bp cut sometime this month and another 50bp in 2Q10.

JPMorgan View - Global Markets

Upside risk to 1Q growth

- **Asset allocation** — No change to our long in risky assets.
- **Economics** — Upside risks to 1Q growth from surprises in US retail sales, EU IP and Japanese consumption, offsetting softer Chinese data.
- **Fixed Income** — Stay short in the UK. Position for a steeper Euro area money market curve.
- **Equities** — Small caps reached their highest level relative to large caps since mid 2006. Stay overweight. Within EM, underweight China as hard landing remains a non-negligible risk.
- **Credit** — Stay overweight credit.
- **FX** — The euro's risk premium appears excessive, and its reduction could push EUR/USD to 1.42 and EUR/JPY to 130 in the near term.
- **Commodities** — Stay long commodities on strong manufacturing growth.
- Another week of strong equity and credit markets, and softer bond markets. **The dollar was weaker, possibly re-establishing its negative relation to risky markets, while commodities were basically flat.**

Our strategy remains to be long equities, credit, and commodities, and to trade bond markets from the short side. In equities, we focus on higher beta sectors—cyclicals and small caps—but are neutral on EM. In credit, given how much HG spreads have come in, we are up-in-yield, and down-in-quality. The bond strategy is not really bearish given central banks on hold and falling core inflation, but we are opportunistically short to exploit a worsening supply-demand balance.

Our overweight in risky assets is primarily a **macro-value strategy**, based on a judgement that risk premia in the market are high and attractive relative to gradually fading macro risks in the world. We are getting further support for this view. The quantitative measure we introduced last week—the dispersion of US growth forecasts—tightened again in the March survey, showing gradually falling uncertainty on the macro economic outlook (bottom chart on the next page). Monetary policy makers around the world continue to signal they are in no hurry to tighten given the continued fragility of the recovery and low core inflation readings.

A value strategy only works if investors act upon it. That is, we need to see **flow support**. Here too, recent indicators are

positive. Retail investors are again putting money in equity and HY funds, while companies are also buying stocks, as evidenced by an acceleration in M&A activity and equity buybacks. We recognize that regulations are pushing UK and US pension funds away from equities towards long-dated bonds, but expect that the much higher yield/IRR on equities will induce the average investor to rely on equities rather than bonds to fund its future spending needs.

The China question. A major focus of market concern remains whether Chinese policy makers will be able to control their red-hot economy. Last week's softer activity data and higher inflation readings added fuel to these worries. Weather effects and the lunar new year, as well as the narrowness of the CPI inflation rise—largely food—create enough data uncertainty to make us stay with our more sanguine forecasts. But on the margin, they do create downside risks to our 1Q Chinese GDP projection. We currently handle this risk via an underweight of Chinese equities and a neutral on EM versus DM equities, but do not consider the risk big enough to take profit on our overall long in risky assets.

We have been arguing that the **recovery trade**, or the steady upgrading of growth forecasts, is a force that is largely spent. And indeed, our 2010 global growth forecasts have been in a range for over six months now. But the recovery trade is not completely spent. The consensus forecast for global growth is still catching up with ours, narrowing the gap to 0.1% in the last reading. In addition, last week's activity data for the G3—retail sales in the US, IP in Europe, and consumption in Japan—were quite strong and of a much greater magnitude than the downside in China. This creates an **overall upside risk bias to our 1Q global GDP forecasts**.

Fixed income

Bonds fell a little last week as a mixed bag of data surprised to the upside on balance. But the most striking feature of major government bond markets this year continues to be a **lack of volatility**. Bund yields, for example, have remained within a 30bp range since September, a level of stability not seen since the early 1990s.

We remain **medium-term bearish on duration**, on the expectation that supply will outstrip demand this year. The postponement last week of liquidity regulations which would have prompted banks to buy gilts worsened the supply-demand imbalance in the UK, where we stay short. But we are tactically neutral on other core markets, awaiting more attractive levels to go short.

Overnight euro rates remain far below the ECB's official policy rate, reflecting the abundant liquidity supplied by the ECB. However, the EONIA curve implies that overnight rates will move steadily higher, by some 30bp, over the next six months. We expect that the ECB's commitment to provide as much liquidity as banks request until October will limit the increase in overnight rates, and so recommend long positions in September 2010 EONIA. Money market steepeners provide another way of expressing this view, but with greater protection against a change in monetary policy expectations.

Equities

Equities have risen in four of the past five weeks and **have recaptured 90% of the loss incurred between mid Jan and mid Feb**. Better than expected economic data continue to bolster equity investors' sentiment, a trend that is likely to continue given the upside risks we see for G3 economic growth in 1Q.

Flows are also supportive. Retail investors have been buying equities for four straight weeks. M&A activity rose to a US\$200 billion per month pace in March versus US\$140bn per month during Jan/Feb. Share buyback activity has also accelerated over the past weeks to an US\$11 billion per week pace versus US\$5 billion per week in 4Q09 and US\$1.6 billion per week between 1Q-3Q09. The acceleration in share buybacks and M&A activity is supportive of equity markets and suggests that **corporates are turning more expansionary**. See *Flows & Liquidity* for more details.

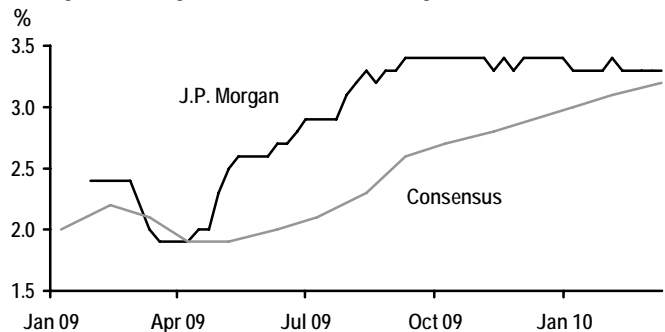
We stay long equities focusing on cyclical sectors and **small caps**. The relative return index of MSCI World\$ small caps index versus MSCI World\$ reached the **highest level since mid 2006**. We stay overweight in small versus large caps as both return momentum and the rebound in M&A activity favour the former.

We stay neutral in EM versus DM. Within EM we continue to underweight China against OECD exporters such as Taiwan and Mexico. **The underperformance of Chinese equities is likely to continue** due to policy risks and poor relative earnings revisions. China delivered last week a package of January/February data that hinted at an unpleasant combination of moderating growth and rising inflation, a reminder that a **hard landing remains a non-negligible risk**.

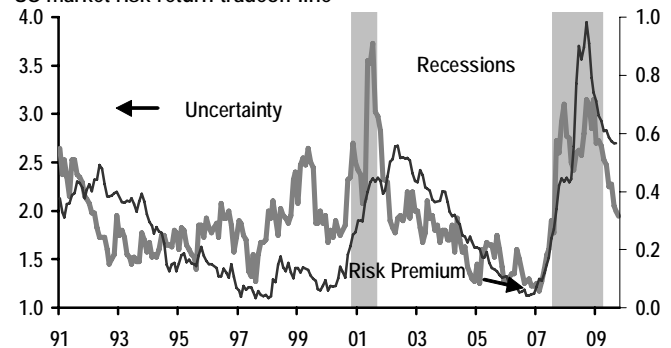
Credit

Credit markets continued to rally last week, with HY spreads

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



US market risk-return tradeoff line



tightening by 16bp. We stay overweight in credit as uncertainty is receding, investor demand is strong and fundamentals are improving steadily. Keep overweights in both HG and HY corporate credit, EM corporates, ABS and super senior CMBS. **Focus on lower-quality sectors to pick up extra yield**.

EM corporate credit (CEMBI) is benefiting from rising demand by crossover investors and a collapse in the default rate which should fall sharply to only 1.8% this year, close to the 2% rate we project for US HY corporate bonds.

CEMBI is attractive versus HY on a total return basis, as we expect BBB-rated EM corporates to generate a similar total return to B-rated US HY corporate bonds this year.

With investment grade EM sovereign spreads well below those of developed countries in many cases, we stay neutral EMBIG. Instead, **we focus on relative value within EMBIG** and rotate exposure to high yielders such as high-beta countries and uncorrelated frontier markets. Although developed market sovereign risk is unlikely to spread to EM sovereigns or EM corporates, we continue to underweight EM European sovereigns given their very low yields. Over-

all, EM sovereign debt remains well supported by upside surprises to growth, front-loaded issuance, and strong inflows, which we believe will reach a record US\$40-45bn in 2010.

The **ABS** portion of the US TALF program ended two weeks ago. Overall, the program was successful in revitalizing the non-mortgage ABS market. In our view, the end of TALF poses little threat to the ABS market as benchmark issuers have been able to access the market without TALF since mid-2009 and off-the-run issuers can afford to wait as TALF financing has already fulfilled near term funding needs. Stay overweight ABS as strong demand is expected to continue from real money managers, given the scarcity of high-quality credit.

Foreign Exchange

The dollar is completing its worst week since early January, a period which parallels March in that equities, credit and commodities are higher while the dollar declines. One week is hardly conclusive, but it is still highly suggestive. For all the predictions that Europe's sovereign debt crisis would doom the euro even if Greece stabilized, market dynamics have not changed much. Global growth and higher equities still bring a weaker dollar, even versus the euro.

Last week we argued that the dollar's 1Q rally was nearing an end since the three systemic threats which drove the currency higher this year — a global slowdown, sovereign risk, and China tightening — were dissipating. So far this scenario is tracking, but the broad dollar move is not the interesting story. **More unusual is the apparent risk premium which the euro still carries:** EUR/USD and EUR/JPY trade 4-5% cheap to what the recovery in underlying markets would predict, probably reflecting residual scepticism that sovereign risk is contained. This premium is excessive, and its removal can push EUR/USD to 1.42 and EUR/JPY to 130 short-term. Buy the euro and the Swiss franc, which tends to move with the euro, versus the dollar, or leverage the sovereign premium by owning CHF/JPY.

Commodities

Commodities finished the week nearly flat, after recovering on Friday on a surge in US retail sales and above-consensus Euro area IP growth. We remain overall bullish commodities on strong manufacturing growth. Energy was the only sector with positive performance with WTI rising to

Ten-year Government bond yields

	Current	Mar 10	Jun 10	Sep 10	Dec 10
United States	3.70	3.90	4.10	4.25	4.50
Euro area	3.17	3.15	3.30	3.45	3.60
United Kingdom	4.10	4.25	4.40	4.45	4.50
Japan	1.34	1.30	1.40	1.50	1.55
GBI-EM	7.13				7.70

Credit markets

	Current	YTD Return
US high grade (bp over UST)	158	2.0%
Euro high grade (bp over Euro gov)	147	1.9%
USD high yield (bp vs. UST)	637	3.6%
Euro high yield (bp over Euro gov)	644	5.8%
EMBIG (bp vs. UST)	271	3.6%
EM Corporates (bp vs. UST)	313	4.1%

Foreign exchange

	Current	Mar 10	Jun 10	Sep 10	Dec 10
EUR/USD	1.38	1.45	1.48	1.45	1.40
USD/JPY	90.5	85	82	85	89
GBP/USD	1.52	1.54	1.59	1.58	1.56

Commodities - quarterly average

	Current	10Q1	10Q2	10Q3	10Q4
WTI (\$/bbl)	81	77	82	85	90
Gold (\$/oz)	1102	1250	1400	1300	1200
Copper(\$/m ton)	7431	7350	8000	6800	6250
Corn (\$/Bu)	3.64	3.85	4.05	3.95	3.90

Source: J.P. Morgan, Bloomberg, Datastream

close at \$82.50. Besides the strong retail and IP releases, crude prices were also supported by better inventory numbers and improved demand forecasts by the IEA and EIA. We remain medium-term bullish crude oil, but there are downside risks near term as we enter a period where refinery maintenance is likely to intensify.

Agricultural products had large losses almost across the board, averaging a decline of 3% last week. This sector is the worst performer this year, with losses near 13%. Raw sugar, the worst performing soft commodity, continues its negative run, declining more than 10% since last Friday. Raw sugar is now below \$20, much lower than its February peak of more than \$28 on concerns that production is increasing substantially this year. We closed our long position in agriculture earlier this year but continue to look for relative value opportunities in the sector. We stay long white sugar premium over raw sugar, favouring white sugar Oct 10 versus raw sugar Jul 10 to account for processing time. White sugar Oct 10 was down only 7% last week.

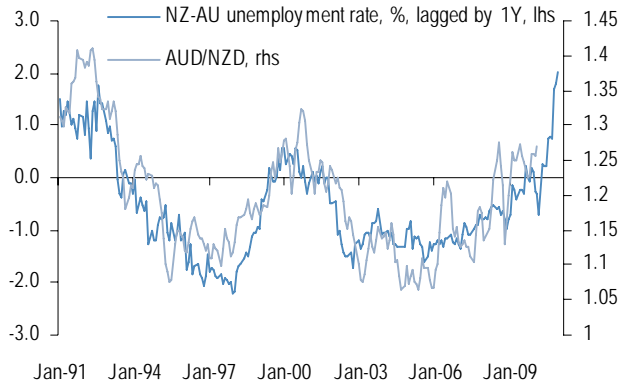
AUD and NZD Commentary

- **The RBNZ meeting last week very much reinforced our short NZD view: add to short NZD positions via AUD/NZD in cash and options.**
- **AUD/USD is vulnerable to a near term pullback, but short term upside bias intact. NZD/USD maintains the short term range. AUD/NZD still in position for additional upside.**
- Labour market tightness driven by a commodity based investment boom will keep the RBA ahead of the curve in terms of rate hikes and we expect the RBA to continue to reaffirm its status as the central bank moving most aggressively toward policy normalization. Look for AUD to outperform against the majors and commodity FX both in coming months.
- In contrast, NZD continues to under-perform following dovish commentary from the RBNZ on Wednesday. In the statement following the decision to keep rates on hold, Bollard stated he expects the RBNZ to begin raising rates in Q3 as before, but also downgraded the assessment of the economy. Given the less robust economic release since the RBNZ last released a policy statement in January, it was not surprising that their assessment of the economy was less bullish this time around. However, the central bank is keeping with its key wording that it anticipates the removal of monetary stimulus from around the middle of 2010. Taken together, the changes in the most recent statement are a negative for NZD and should help AUD/NZD to continue to push higher.
- Another easy way to summarize the case for AUD to continue to make gains against NZD is the divergence that has opened up between the unemployment rate in the two countries. The chart compares the two series (which are 70% correlated since 1990), with the unemployment rate lagged one-year to emphasis how AUD/NZD has followed rather than led economic fundamentals. AUD/NZD remains on course for a move to 1.35 in coming months.
- Buy AUD/NZD in cash and options (call with rko). Buy a 3-month 1.3150 AUD call/NZD put, RKO 1.3650. Cost 30bp. (Bought intra-week on March 11). Buy AUD/NZD at 1.3090 with a stop at 1.2845.

Technical analysis

- AUD/USD maintains the short term rally phase as the persistent rally from the Feb. low continues to develop. For this week, we see an important test as the key .9200 resistance zone is now in focus amid a short term overbought setup. Importantly, this area which includes the breakdown area from Jan. will define whether an extension into the .9330 Jan. high, if not higher is underway. Again, this advance has reasserted the broad range view below the 4Q highs, but the medium term bias has improved to sug-

AUD/NZD has plenty of scope to rally to reflect the historic divergence in unemployment rates (one specific illustration of the marked difference in the output gap between Australia and NZ).



Source: J.P. Morgan

gest new highs are likely. For the near term picture, dips should find support at .9055 and then .8975 while the .8800 area should maintain the short term upside bias.

- The price action for NZD/USD has shifted into a well-defined range above the February lows but the rally has so far been capped at the key initial resistance levels. As such, a break above the .7100/.7155 area is necessary to argue for a deeper retracement of the decline from the January high. Until then, the NZD underperformance bias is likely to remain intact. In that regard, the breakout in AUD/NZD through the important 1.29/1.30 medium term range highs is likely to extend. Moreover, the EUR/NZD is attempting to base in the 1.92/1.90 support zone, while NZD/CAD stays vulnerable to new lows.

AUD/NZD - Daily chart



Source: CQG, Inc. © 2010 All rights reserved worldwide. www.cqg.com

Fri Mar 12 2010 17:34:39

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	<u>2.5</u>	4.0	4.0	3.5	2.5	1.5	2.2	1.1	0.9
Canada	-2.6	3.2 ↑	3.4	0.9	5.0	<u>4.5</u>	3.0 ↑	3.5	4.0	4.0	0.8	1.4	1.9 ↑	2.1 ↑
Latin America	-3.1 ↓	4.6	3.8	6.4 ↑	<u>6.6</u> ↑	4.1	4.8 ↑	4.3 ↓	3.5 ↑	3.0	5.3	6.3 ↓	7.0 ↓	6.9 ↓
Argentina	-4.0	4.5	3.0	0.2	<u>1.0</u>	8.0	8.0	3.0	3.0	2.0	7.1	8.0	10.0	10.0
Brazil	-0.2 ↓	6.2	4.0	7.0 ↑	<u>8.4</u> ↑	<u>6.3</u>	5.0	5.1	4.0	3.8	4.2	4.9 ↑	5.0 ↑	4.5 ↓
Chile	-1.7	5.5	5.5	4.6	<u>8.0</u>	-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	<u>3.7</u>	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	<u>-2.0</u>	2.0	3.5	4.0	4.5	3.0	3.9	3.9 ↓	4.7 ↑	4.4 ↑
Mexico	-6.5	4.5	3.5	10.4	8.4	<u>4.1</u>	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	<u>3.0</u>	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	<u>-4.0</u>	-2.0 ↑	12.5 ↓	1.5 ↑	1.5	28.1	31.8 ↓	33.7 ↓	39.3 ↑
Asia/Pacific														
Japan	-5.2 ↓	2.1 ↓	1.9	-0.6 ↓	3.8 ↓	<u>1.8</u>	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	<u>3.0</u>	3.3	3.8	3.9	3.1	2.1	2.5	2.6	3.0
New Zealand	-1.5 ↑	2.9 ↑	2.8 ↓	0.8	<u>3.3</u> ↑	4.1 ↑	2.9 ↓	3.5 ↑	1.5 ↓	2.8 ↓	2.0	2.3 ↑	2.5 ↑	2.8 ↑
Asia ex Japan	4.6	7.9	7.2	10.7	7.2	<u>7.3</u>	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	<u>9.8</u>	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	<u>4.5</u>	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	<u>10.4</u>	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	<u>6.0</u>	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	<u>3.6</u>	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	<u>1.2</u>	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	<u>6.0</u>	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	<u>11.2</u>	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	<u>1.2</u>	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	<u>2.8</u>	5.3	3.6	3.6	4.1	1.9	5.5	4.4	3.0
Africa/Middle East														
Israel	0.7 ↑	3.0	4.5	3.6 ↑	4.9 ↑	<u>3.0</u>	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	<u>4.4</u>	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	<u>1.5</u>	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	<u>1.0</u>	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	<u>1.5</u>	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	<u>1.0</u>	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	<u>3.0</u>	3.0	3.0	3.0	2.8	1.4	2.8 ↑	1.7 ↑	0.9 ↓
Sweden	-4.7	1.6	3.0	-0.4	-2.2	<u>3.5</u>	3.5	3.0	3.0	3.0	-0.4	1.5 ↑	1.1 ↑	1.9 ↑
Switzerland	-1.5	2.5	2.8	2.0	3.0	<u>2.5</u>	2.8	3.0	3.0	2.8	-0.2	0.9 ↑	0.8 ↑	0.7 ↓
United Kingdom	-5.0	1.2	3.1	-1.2	1.1	<u>1.2</u>	2.5	2.8	3.5	2.8	2.1	2.6 ↑	1.9 ↑	1.9
Emerging Europe	-5.1	3.9	4.7	4.3 ↓	<u>6.1</u> ↑	3.7	3.6	3.2 ↓	3.9	4.1 ↓	6.2	5.7 ↑	5.7 ↑	5.2 ↑
Bulgaria	-5.0 ↑	-1.5	4.5	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	-4.2 ↑	2.0	4.0	2.3 ↓	3.0 ↑	<u>2.0</u>	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	-1.7 ↓	<u>1.5</u>	2.5	2.0	2.0	4.0	5.2	4.8 ↑	3.7 ↑	2.8
Poland	1.7	3.2	4.2	2.4	4.9	<u>3.0</u>	4.0	2.7 ↓	3.0	3.0 ↓	3.3	2.0	2.6 ↑	2.8 ↑
Romania	-7.1	1.5	4.0	...	...	...	...	...	...	...	4.6	4.5	5.3	4.5
Russia	-7.9	5.5	5.0	7.9	<u>10.5</u>	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	9.6 ↑	7.5 ↑	5.8 ↑
Global	-2.5	3.3	3.3	2.7 ↓	<u>4.1</u> ↓	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	1.3 ↓	<u>3.4</u> ↓	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	8.2 ↑	<u>6.8</u> ↑	5.8	5.8	5.6 ↓	5.4	5.4	4.0	5.0 ↓	4.9	4.4 ↑
Memo:														
Global — PPP weighted	-0.9	4.4	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	1.34	1.42	1.51	1.96
excluding US	GDP-weighted average	1.85	-251				1.85	1.91	2.03	2.16	2.65
Developed	GDP-weighted average	0.51	-361				0.51	0.51	0.54	0.59	1.04
Emerging	GDP-weighted average	4.46	-241				4.47	4.65	4.91	5.17	5.65
Latin America	GDP-weighted average	5.72	-321				5.91	6.31	6.73	7.21	7.82
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	0.81	0.89	0.98	1.39
United States	Federal funds rate	0.125	-512.5	16 Dec 08 (-87.5bp)	<u>16 Mar 10</u>	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)	<u>17 Mar 10</u>	17 Mar 10 (+50bp)	9.25	10.25	11.25	11.75	11.75
Mexico	Repo rate	4.50	-270	17 Jul 09 (-25bp)	<u>19 Mar 10</u>	Oct 10 (+25bp)	4.50	4.50	4.50	5.00	5.75
Chile	Discount rate	0.50	-450	9 Jul 09 (-25bp)	<u>18 Mar 10</u>	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)	8 Apr 10	10 Jun 10 (+25bp)	1.25	1.50	2.25	3.00	4.50
Europe/Africa	GDP-weighted average	1.31	-321				1.30	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	5 May 10 (+25bp)	1.75	2.00	2.25	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)	29 Mar 10	29 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	26 Apr 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	Sep 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)	Jun 10	Sep 10 (+25bp)	0.25	0.25	0.50	0.75	1.25
Turkey	Overnight borrowing rate	6.50	-1100	19 Nov 09 (-25bp)	<u>18 Mar 10</u>	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)	29 Apr 10	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)	<u>17 Mar 10</u>	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)	<u>17 Mar 10</u>	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)	8 Apr 10	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)	22 Apr 10	Jun 10 (+25bp)	4.00	4.25	4.75	5.00	5.00
Thailand	1-day repo rate	1.25	-200	8 Apr 09 (-25bp)	21 Apr 10	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	-23.4	-23.3	-0.9	-4.3	-5.7	-6.0	-6.0	-5.9	-5.6	-5.6	-5.7	-5.5	-6.6
Current account (A\$ bil, sa)	-67.0	-72.1	-74.6	-13.1	-14.7	-17.5	-18.0	-18.1	-18.1	-17.9	-18.1	-18.4	-18.3	-19.9
as % of GDP	-6.2	-5.4	-5.3	-4.2	-4.7	-5.4	-5.5	-5.5	-5.4	-5.3	-5.3	-5.3	-5.2	-5.6
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	0.95	0.82	0.88	0.91	0.94	1.00	0.99	0.98	0.96	0.95	0.94	0.93
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)	-1.5	2.9	2.8	0.9	0.8	3.3	4.1	2.9	3.5	1.5	2.8	4.3	2.2	2.3
Private consumption	-0.7	2.3	1.2	1.5	3.0	4.1	2.8	1.1	0.5	1.0	1.0	1.5	2.0	1.5
Fixed Investment	-12.9	-1.1	4.5	-2.8	-6.0	-7.7	-2.0	5.4	4.6	5.7	2.2	4.1	6.0	7.4
Residential construction	-20.4	-3.3	4.5	-8.7	-18.6	-6.0	-2.0	4.0	3.2	6.0	3.2	4.8	6.0	4.0
Other fixed investment	-11.4	-0.7	4.5	-1.6	-3	-8.0	-2.0	5.6	4.8	5.6	2.0	4.0	6.0	8.0
Inventory change (NZ\$ bil, saar)	-2.6	-0.5	0.2	-1.0	-0.7	-0.6	-0.4	-0.3	0.1	0.1	0.0	0.1	0.1	0.1
Government spending	0.9	0.1	0.7	-5.8	1.5	-2.0	0.8	1.0	1.6	0.8	0.4	0.8	0.0	0.2
Exports of goods & services	0.8	6.7	9.2	20.0	0.1	8.0	8.0	6.0	5.0	5.0	12.0	12.0	12.0	8.0
Imports of goods & services	-16.5	5.5	7.9	-9.3	2.7	4.0	7.0	9.0	10.0	7.0	5.0	8.0	12.0	9.0
Contributions to GDP growth:														
Domestic final sales	-5.2	0.9	1.8	0.8	-1.6	0.2	1.3	2.0	1.5	2.0	1.1	1.9	2.6	2.6
Inventories	-3.0	1.6	0.6	-8.6	3.2	1.8	2.4	1.8	3.6	0.1	-0.6	1.0	-0.5	0.0
Net trade	6.6	0.4	0.4	9.4	-0.8	1.3	0.3	-0.9	-1.6	-0.7	2.2	1.3	0.1	-0.3
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	2.5	3.0	2.3	5.3	-0.7	2.2	2.7	2.1	2.9	3.3	2.9	3.2	3.6
%oya	2.1	2.2	3.0	1.9	1.7	2.0	2.2	2.3	1.6	2.5	2.7	2.8	3.1	3.2
Trade balance (NZ\$ bil, sa)	2.2	-3.5	-6.1	0.8	0.7	-0.2	-0.5	-0.6	-1.0	-1.3	-1.3	-1.4	-1.6	-1.8
Current account (NZ\$ bil, sa)	-3.6	-10.9	-14.3	-0.4	0.3	-1.4	-1.2	-1.7	-2.7	-3.2	-3.3	-5.2	-3.4	-3.0
as % of GDP	-2.0	-5.7	-7.2	-0.9	0.8	-3.1	-3.7	-5.7	-6.7	-6.8	-7.0	-6.1	-7.2	-8.4
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	4.4	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	6.3
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	6.2	7.0	6.0	6.0	6.5	7.3	7.3	7.1	6.9	6.6	6.4	6.2	6.0	5.5

*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.

Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
15 - 19 March	15 March	16 March	17 March	18 March	19 March
	<ul style="list-style-type: none"> Euro area <ul style="list-style-type: none"> • Employment (4Q) Poland <ul style="list-style-type: none"> • CPI (Feb) Russia <ul style="list-style-type: none"> • IP (Feb) United States <ul style="list-style-type: none"> • IP (Feb) • NAHB survey (Mar) • NY Fed survey (Mar) 	<ul style="list-style-type: none"> Euro area <ul style="list-style-type: none"> • HICP final (Feb) Germany <ul style="list-style-type: none"> • ZEW bus survey (Mar) United States <ul style="list-style-type: none"> • Housing starts (Feb) • Import prices (Feb) • FOMC mtg: No Chg 	<ul style="list-style-type: none"> Brazil <ul style="list-style-type: none"> • COPOM mtg: +50bp Euro area <ul style="list-style-type: none"> • Labor costs (4Q) Japan <ul style="list-style-type: none"> • BoJ mtg: No Chg United Kingdom <ul style="list-style-type: none"> • Labor mkt report (Feb) • MPC minutes United States <ul style="list-style-type: none"> • PPI (Feb) 	<ul style="list-style-type: none"> Chile <ul style="list-style-type: none"> • BCCh mtg: No Chg Euro area <ul style="list-style-type: none"> • Foreign trade (Jan) Japan <ul style="list-style-type: none"> • MoF bus outlook (1Q) • Reuters Tankan (Mar) Turkey <ul style="list-style-type: none"> • CBRT mtg: No Chg United States <ul style="list-style-type: none"> • CPI (Feb) • Philly Fed survey (Mar) 	<ul style="list-style-type: none"> Canada <ul style="list-style-type: none"> • CPI (Feb) Euro area <ul style="list-style-type: none"> • Trichet speech Mexico <ul style="list-style-type: none"> • GDP details (4Q) • Banxico mtg: No Chg Taiwan <ul style="list-style-type: none"> • Export orders (Feb) United States <ul style="list-style-type: none"> • Bernanke speech
22 - 26 March	22 March	23 March	24 March	25 March	26 March
		<ul style="list-style-type: none"> Belgium <ul style="list-style-type: none"> • BNB bus survey (Mar) France <ul style="list-style-type: none"> • INSEE bus surv (Mar) Japan <ul style="list-style-type: none"> • Flow of funds (4Q) • MPM minutes South Africa <ul style="list-style-type: none"> • GDP details (4Q) Taiwan <ul style="list-style-type: none"> • IP (Feb) United Kingdom <ul style="list-style-type: none"> • CPI (Feb) United States <ul style="list-style-type: none"> • Existing home sales (Feb) • FHFA HPI (Jan) • Richmond Fed surv (Mar) 	<ul style="list-style-type: none"> Euro area <ul style="list-style-type: none"> • Industrial orders (Jan) • PMI flash (Mar) Germany <ul style="list-style-type: none"> • IFO bus survey (Mar) Japan <ul style="list-style-type: none"> • Trade balance (Feb) Norway <ul style="list-style-type: none"> • Norges Bank mtg: No Chg South Africa <ul style="list-style-type: none"> • CPI (Feb) United States <ul style="list-style-type: none"> • Durable goods (Feb) • New home sales (Feb) 	<ul style="list-style-type: none"> Brazil <ul style="list-style-type: none"> • COPOM minutes Czech Republic <ul style="list-style-type: none"> • CNB mtg: No Chg Euro area <ul style="list-style-type: none"> • M3 (Mar) France <ul style="list-style-type: none"> • Cons of mfg goods (Feb) Italy <ul style="list-style-type: none"> • ISAE bus surv (Mar) South Africa <ul style="list-style-type: none"> • SARB mtg: No Chg Taiwan <ul style="list-style-type: none"> • CBC mtg: No Chg United Kingdom <ul style="list-style-type: none"> • Retail sales (Feb) 	<ul style="list-style-type: none"> Colombia <ul style="list-style-type: none"> • BanRep mtg: No Chg Japan <ul style="list-style-type: none"> • CPI (Feb) United States <ul style="list-style-type: none"> • Consumer sent (Mar) • Real GDP third est (4Q)

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