

## Global Data Watch

- Continued signs of slowing global growth momentum led by US and China
- Rising claims, soft consumers increase risk of subpar US growth
- The Fed acts and BoJ talks but uncertainty about monetary tools runs high

### Quantitative teasing

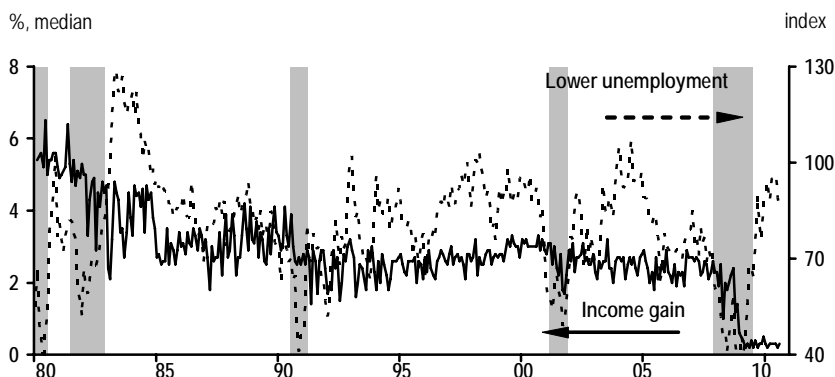
At the start of last quarter, financial stress arose from the combination of sovereign credit concerns and weak economic performance in Europe, placing the region on the brink of an existential crisis. Since that time the tables have turned dramatically. This is partly because European policymakers effectively stemmed a brewing funding crisis for its banks and sovereigns. However, there has also been a dramatic swing in relative growth momentum. This week's releases underscore this shift as the Euro area economy recorded a 3.9% (q/q saar) GDP gain in 2Q10—fueled by a German bounce (9%) that represents the country's strongest quarterly performance since reunification. This outcome stands in striking contrast to last quarter's China downshift (7.2%) and US data pointing to 2Q growth at less than a 1.5% pace.

These outcomes do not accurately reflect relative positions one year into the global expansion. China is in the midst of an inventory correction that appears close to ending. The US was weighed down last quarter by a surge in import volumes that produced a net trade drag on growth amounting to three percentage points. In contrast, trade and inventories likely added significantly to Euro area growth. This gap in trade and inventory contributions will unwind as it likely reflects the Euro area's position as a laggard in the global expansion.

With Europe likely set to follow the lead set by the US and China, the more important news is the moderation continuing into the current quarter in both countries. In China, growth appears to be tracking our forecast of a roughly 8% gain; this quarter's growth will come on the back of a rising trade surplus due to weak import growth. Looking at the domestic economy, there is further moderation in the pace of investment spending and industrial production growth. In the US, the hard data flow for July points to sluggish growth (tracking modestly lower than our forecast of 2.5%) weighed down by soft consumer spending.

Growth momentum waxes and wanes through an expansion, and an important element of the recent global growth slowdown is a normal early cycle dynamic whereby an acceleration phase in the global manufacturing sector ends. How-

### US consumer expectations (University of Michigan)



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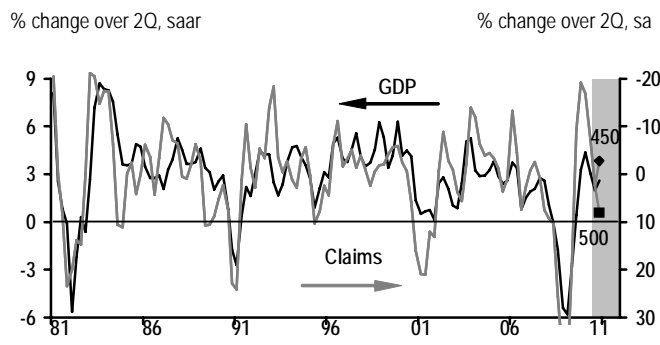
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## Real GDP and initial jobless claims



Note: Chart displays outcomes for initial jobless claims at 450,000 and 500,000 in 4Q10

ever, the latest news also raises questions about the strength of behavioral pillars supporting the expansion. Across most of the world, there is little reason to be concerned about these fundamental supports. Unfortunately, the behavioral foundations supporting the US expansion feel more fragile at this stage than we had anticipated.

- Initial jobless claims have been remarkably stable this year, hugging close to 360,000 each month. However, the latest two readings have exceeded 380,000. Two weeks do not make a trend, but a continued upward drift would push claims toward levels that would raise the specter of a double-dip recession. Even at the current four-week average of 473,000, claims are pointing to growth with minimal job gains, a message suggesting that the forward motion of business behavior toward expansion may be weakening.
- Retail spending trends are notoriously volatile, and the recent soft patch in US retail sales has come on the heels of strength earlier this year. However, underneath the surface there is a sense of structural pessimism emerging in consumer confidence surveys even as expectations for growth and credit conditions improve. Household surveys suggest a high level of uncertainty about the future along with depressed expectations regarding income prospects.
- The transmission of accommodative monetary policy is expected to be facing the headwinds of cautious consumer and business behavior. But recent market movements point to a significant slide in inflation expectations—a development that could further hamper effective transmission.

It is against this backdrop that the Fed's decision to maintain the size of securities on its balance sheet should be seen. The FOMC statement reflects increased concern

about the outlook and its desire to ease financial conditions. In addition, the Fed wants to bolster confidence by displaying that there are tools that can be calibrated to a changing assessment of risks. In the event, the Fed succeeded in pushing market interest rates lower this week. But the 19bp fall in 10-year bond yields gives the committee cold comfort. Much of the decline reflects weaker economic news and lower inflation expectations. This point was reinforced by a fall in equity markets and widening in credit spreads. As a result, uncertainties about the effectiveness of unconventional tools to offset economic weakness and disinflation remain quite high.

## Euro area's fleeting growth bounce

After a sluggish start to the recovery, the Euro area economy has picked up significant momentum led by a turbocharged German bounce last quarter. However, the rest of the core experienced solid gains in output. Excluding Greece the periphery held up surprisingly well, with GDP gains of close to 1% ar in Spain and Portugal. Greece is being weighed down heavily by fiscal consolidation, and the economy contracted by almost 6% ar.

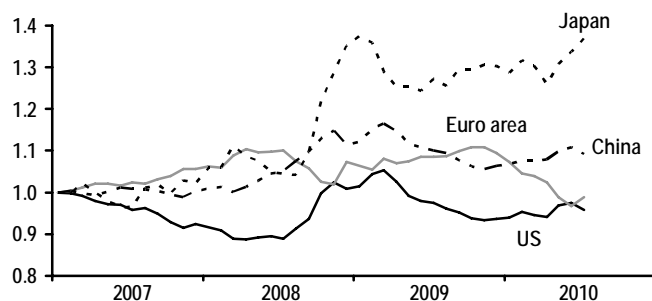
At this stage, there is very little information on the composition of regional growth. The German statistics office said that a weather-related rebound in construction and net trade were important contributors to growth. In France, where expenditure data are available, there was a modest gain in household consumption, a solid gain in business fixed investment, and an inventory contribution of 2.7%-pts ar.

Euro area growth likely is downshifting this quarter, as parts of the 2Q gain clearly were transitory—including the jump in construction in Germany and what was likely a broad-based inventory contribution across the region. Moreover, global growth is slowing and the fiscal and banking adjustments are intensifying in the periphery. That said, at this juncture the risks appear tilted to the upside of our 2% growth forecast as July surveys showed that the economy's underlying momentum was maintained early in the third quarter.

As growth moderates in the coming months attention is likely to focus again on the issue of debt sustainability in the periphery. So far, the news is encouraging. Fiscal performance is on or ahead of schedule, and implied official 2H GDP growth forecasts are realistic. However, Greece faces an added challenge in that the slide in the economy is raising the chances of a move into deflation. Although this would help improve Greece's competitiveness, it would add to the challenge of achieving debt sustainability.

**Nominal broad trade-weighted exchange rates**

Jan 07=1.0

**China looks toward an 8% landing**

China's July activity indicators hinted that the economy is growing at about an 8% annualized pace this quarter. Although current performance varies across sectors consumer spending remains robust. The slowdown in fixed investment and inventory accumulation continue but appear to be close to ending. Meanwhile, net trade is poised to contribute to growth. Having dipped to near zero earlier this year, the trade surplus has soared into midyear and is likely to be double the 2Q average in the current quarter. Exports have slipped in recent months, but imports are falling faster, mostly due to the inventory adjustment.

Inflation popped back above 3% oya last month, but it likely is near the peak and remains just 1.3% excluding food. With domestic and global growth having slowed, policy is likely to turn somewhat more growth-friendly in coming months.

**Japan officials voice concern about yen**

Japan's economy has downshifted along with China's. This will be verified in next week's GDP report, which is expected to show the economy rose 2.3% annualized last quarter, down from 5.0% in 1Q. The growth moderation is most striking in manufacturing and export volume, each of which declined in June. Against this backdrop, Japanese officials (the MoF and BoJ) this week voiced concern about the rapid appreciation of the yen. Currency appreciation is unwelcome in most economies and it is not surprising that Japanese officials spoke out, with the yen TWI having increased about 12% in the past three months. The recent gain builds on very large increases in the past few years. Although officials clearly are reluctant to formally intervene in the FX market, they are likely to step up their verbal intervention in the face of continued yen appreciation.

**Global slowing reinforcing RBA caution**

Officials at Australia's Reserve Bank received more mixed signals on the economy this week. Employment rose

strongly again in July and consumer confidence has rebounded. Demand for home loans, though, sank, as did a major business confidence reading. While the signals on the domestic economy are mixed, the message from offshore is clearer: momentum has been lost, including in China, the largest single destination for Australia's exports. The RBA will remain inactive on policy while the offshore uncertainty persists, and as officials await clarity on the strength of the domestic economy. That said, the forecast remains that the RBA will resume tightening in November, with further rate hikes likely in 2011. The economy still is expected to grow at a better than 3.5% pace in 2H. With little spare capacity, this will exacerbate RBA concerns about the inflation outlook.

**Turkey backs away from fiscal rule**

This week Turkey's government announced it will delay the implementation of its "fiscal rule" reform, designed to enforce cuts in the budget deficit and public debt. Rigorous application of the rule was expected to facilitate Turkey's upgrade to investment grade status and enhance the attractiveness of Turkish financial assets. The decision raises concerns the government will deliver a sharp rise in spending in the run-up to next year's parliamentary elections, contravening existing budget targets. This likely would exacerbate the rise in the current account deficit and leave the country more vulnerable to the whims of external financing. Market reaction so far has been muted, reflecting the government's strong fiscal performance to date. However, uncertainty regarding the future of the fiscal rule could begin to hurt the markets if/when public spending increases and/or global risk appetite deteriorates more sharply.

**Food inflation set to rise in Latin America**

Global inflation has been moving downward as oil-price base effects diminish. The effect may prove short-lived in Latin America, however, where food comprises a large share of the consumer basket. The severe drought in Russia combined with a poor outlook for EU crops has pushed global wheat prices up 50% from end-June levels. There has been contagion to other agricultural prices and the aggregate J.P. Morgan agricultural price index is about 13% higher since end-June. Our commodity strategists expect wheat prices to remain elevated near term, so this will boost food inflation across Latin America in coming months. With the Latin economies expected to post continued, solid growth in 2H, the expected rise in headline inflation will sustain the drive to normalize policy interest rates across the region.

Editor

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## 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	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11	3Q11	1Q10	2Q10	4Q10	2Q11
<b>The Americas</b>														
United States	-2.6	3.0	2.7	3.7	2.4	<u>2.5</u>	3.0	2.5	2.5	3.0	2.4	1.8	<b>1.0 ↑</b>	<b>1.3 ↑</b>
Canada	-2.5	3.4	2.7	6.1	<u>2.6</u>	3.2	3.2	2.7	2.0	2.4	1.6	1.4	1.7	1.9
Latin America	-2.9	5.4	3.8	4.2	<u>4.0</u>	3.3	4.0	4.2	5.2	2.0	6.0	6.5	7.0	6.9
Argentina	-2.0	8.5	4.5	12.5	<u>13.0</u>	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	<u>2.6</u>	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	<u>4.8</u>	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	<u>3.5</u>	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	-1.4	<u>3.2</u>	-1.8	4.2	5.7	7.9	-2.3	4.8	4.4	5.1	4.5
Peru	0.9	7.3	6.0	7.3	<u>9.5</u>	4.0	4.5	6.0	6.7	7.2	0.7	1.2	2.6	2.2
Venezuela	-3.3	-4.0	1.0	-5.6	<u>-5.0</u>	5.0	1.0	1.0	1.0	1.5	27.4	32.1	32.1	32.1
<b>Asia/Pacific</b>														
Japan	-5.3	3.3	1.8	5.0	<u>2.3</u>	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	<u>1.9</u>	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	<u>3.5</u>	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	6.9	10.7	<u>6.7 ↑</u>	<b>5.8 ↑</b>	6.5	<b>7.2 ↓</b>	7.1	7.1	4.3	4.5	4.4	<b>4.0 ↓</b>
China	9.1	10.0	8.8	10.8	7.2	<u>8.2</u>	8.6	9.5	9.1	8.7	2.2	2.9	2.8	2.7
Hong Kong	-2.8	6.8	<b>4.3 ↑</b>	8.7	<b>5.7 ↑</b>	<u>4.0</u>	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	<u>8.1</u>	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	<u>4.5</u>	5.0	5.3	5.2	5.0	3.7	4.4	5.8	5.5
Korea	0.2	6.1	4.0	8.8	6.0	<u>2.5</u>	3.8	4.0	4.0	4.5	2.7	2.6	3.2	3.5
Malaysia	-1.7	7.2	4.6	5.0	<u>5.0</u>	4.0	4.0	4.9	4.9	4.5	1.3	1.6	2.4	2.4
Philippines	1.1	6.8	4.3	12.9	<u>3.6</u>	4.9	4.0	4.5	4.5	4.5	4.3	4.2	5.2	4.9
Singapore	-1.3	<b>15.5 ↑</b>	<b>4.5 ↓</b>	<b>45.7 ↓</b>	<b>24.0 ↑</b>	<b>-8.5 ↑</b>	0.0	<b>6.1 ↓</b>	6.6	<b>8.2 ↓</b>	0.9	<b>3.1 ↓</b>	<b>3.0 ↓</b>	<b>1.7 ↓</b>
Taiwan	-1.9	8.8	4.2	11.3	<u>2.0</u>	3.0	3.5	4.2	4.6	5.5	1.3	1.1	2.0	1.8
Thailand	-2.2	8.5	5.0	16.0	<u>-2.0</u>	2.8	2.8	6.0	5.5	4.0	3.7	5.5	4.4	3.0
<b>Africa/Middle East</b>														
Israel	0.7	3.0	4.5	3.3	<u>3.5</u>	3.0	3.0	4.0	5.0	5.5	3.5	3.0	3.0	3.2
South Africa	-1.8	3.0	3.5	4.6	<u>3.9</u>	2.8	3.4	3.7	3.1	3.6	5.7	4.5	4.7	4.9
<b>Europe</b>														
Euro area	-4.1	<b>1.5 ↑</b>	<b>1.5 ↑</b>	0.8	<b>3.9 ↑</b>	<u>2.0</u>	1.0	1.0	1.0	1.8	1.1	1.5	1.5	0.9
Germany	<b>-4.7 ↑</b>	<b>3.3 ↑</b>	<b>2.4 ↑</b>	<b>1.9 ↑</b>	<b>9.0 ↑</b>	<u>3.0</u>	2.0	2.0	1.5	2.0	0.8	1.0	1.2	0.9
France	-2.5	1.6	1.4	<b>0.7 ↑</b>	2.5	<u>2.0</u>	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	<u>2.0</u>	1.0	1.0	1.0	1.5	1.3	1.6	1.5	1.1
Norway	-1.5	1.6	2.4	0.6	<u>2.0</u>	3.0	2.8	2.0	2.0	2.5	2.9	2.5	1.3	1.0
Sweden	-5.1	3.8	2.7	6.2	4.7	<u>3.5</u>	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	<u>2.8</u>	2.5	2.3	2.3	2.5	2.8	1.1	1.1	0.9	0.6
United Kingdom	-4.9	1.6	2.6	1.3	4.5	<u>2.5</u>	2.5	2.0	2.5	3.0	3.3	3.5	2.5	1.7
Emerging Europe	-4.9	3.9	4.3	<b>2.6 ↑</b>	<b>4.0 ↓</b>	3.1	3.3	3.6	4.0	4.1	6.1	<b>5.4 ↓</b>	5.7	5.6
Bulgaria	-5.0	-0.5	4.0	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	-4.1	2.0	3.2	2.0	<b>3.2 ↑</b>	<u>2.5</u>	2.3	2.5	3.0	5.0	0.7	<b>1.2 ↓</b>	2.8	2.7
Hungary	-6.3	1.0	3.0	<b>2.4 ↓</b>	<b>0.0 ↓</b>	<u>2.0</u>	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	<u>4.0</u>	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	<b>3.4 ↑</b>	<b>5.9 ↓</b>	<u>4.0</u>	4.5	5.0	5.0	4.5	7.2	5.9	6.6	7.0
Turkey	-4.7	5.9	5.0	...	...	...	...	...	...	...	9.3	9.3	7.5	6.7
<b>Global</b>	-2.6	3.4	2.9	3.9	<b>3.5 ↑</b>	2.8	2.8	2.7	2.8	3.0	2.2	2.2	1.9	1.9
Developed markets	-3.5	2.5	2.2	2.9	<b>3.0 ↑</b>	2.3	2.2	1.9	2.0	2.5	1.5	1.4	<b>1.1 ↑</b>	<b>1.1 ↑</b>
Emerging markets	1.1	<b>6.9 ↑</b>	5.6	<b>7.5 ↑</b>	<b>5.5 ↓</b>	4.6	5.2	<b>5.7 ↓</b>	6.0	<b>5.2 ↓</b>	5.1	5.1	5.2	4.9
<b>Memo:</b>														
Global — PPP weighted	-0.8	4.6	4.0	5.2	4.3	3.7	3.9	3.9	4.0	4.1	3.3	3.3	3.1	<b>3.0 ↑</b>

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.

## G-3 economic outlook detail

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

				2010				2011			
	2009	2010	2011	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
United States											
Real GDP	-2.6	3.0	2.7	3.7	2.4	2.5	3.0	2.5	2.5	3.0	4.0
Private consumption	-1.2	1.5	2.2	1.9	1.6	1.5	2.8	2.1	2.0	2.5	3.0
Equipment investment	-15.3	15.1	10.6	20.4	21.9	17.0	10.0	9.0	8.0	8.0	10.0
Non-residential construction	-20.4	-13.4	2.2	-17.8	5.2	-4.0	-3.0	0.0	7.0	9.0	10.0
Residential construction	-22.9	-0.7	11.5	-12.3	27.8	-15.0	5.0	15.0	20.0	20.0	20.0
Inventory change (\$ bn saar)	-113.1	63.6	63.3	44.1	75.7	69.4	65.2	60.5	63.5	62.6	66.5
Government spending	1.6	0.9	0.0	-1.6	4.4	1.2	0.6	-0.8	-1.0	-1.0	0.4
Exports of goods and services	-9.5	12.1	8.3	11.4	10.4	8.0	8.0	8.0	9.0	8.0	8.0
Imports of goods and services	-13.8	11.2	6.7	11.2	28.8	2.0	5.0	5.0	8.0	6.0	6.0
Domestic final sales contribution	-3.1	1.8	2.7	1.4	4.1	2.0	2.8	2.4	2.5	2.9	3.7
Inventories contribution	-0.6	1.4	0.0	2.6	1.1	-0.2	-0.2	-0.2	0.1	0.0	0.1
Net trade contribution	1.0	-0.2	0.1	-0.3	-2.8	0.7	0.3	0.3	0.0	0.2	0.2
Consumer prices (%oya)	-0.3	1.6	1.1	2.4	1.8	1.2	1.0	0.9	1.3	1.2	1.1
Excluding food and energy (%oya)	1.7	1.0	0.7	1.3	1.0	0.9	0.7	0.8	0.7	0.6	0.7
Federal budget balance (% of GDP, FY)	-10.0	-9.6	-7.9								
Personal saving rate (%)	5.9	6.2	6.5	5.5	6.2	6.5	6.5	6.4	6.5	6.6	6.7
Unemployment rate (%)	9.3	9.6	9.3	9.7	9.7	9.6	9.6	9.5	9.4	9.2	9.0
Industrial production, manufacturing	-11.1	5.6	4.3	6.1	7.9	3.5	4.0	4.0	4.0	4.5	5.0
Euro area											
Real GDP	-4.1	1.5	1.5	0.8	3.9	2.0	1.0	1.0	1.0	1.8	2.0
Private consumption	-1.2	-0.1	0.6	-0.4	-0.5	0.3	0.5	0.5	0.8	1.0	1.5
Capital investment	-10.8	-1.2	3.3	-4.8	7.0	3.0	3.0	3.0	3.0	3.0	3.5
Government consumption	2.7	0.9	-0.1	0.8	1.0	1.0	0.0	-0.5	-0.5	-0.5	-0.5
Exports of goods and services	-13.2	8.8	8.5	8.8	12.0	10.0	9.0	8.0	8.0	7.0	7.0
Imports of goods and services	-11.9	8.3	6.7	16.1	9.0	5.0	7.0	7.0	7.3	6.0	6.0
Domestic final sales contribution	-2.5	-0.1	0.9	-1.0	1.3	0.9	0.9	0.8	0.9	1.1	1.4
Inventories contribution	-0.8	1.3	-0.3	4.5	1.4	-1.0	-0.8	-0.3	-0.3	0.2	0.0
Net trade contribution	-0.8	0.3	0.8	-2.6	1.2	2.1	0.9	0.5	0.4	0.5	0.6
Consumer prices (HICP, %oya)	0.3	1.4	1.0	1.1	1.5	1.6	1.5	1.3	0.9	0.9	1.0
ex unprocessed food and energy	1.3	0.8	0.7	0.9	0.8	0.7	0.7	0.6	0.6	0.7	0.8
General govt. budget balance (% of GDP, FY)	-6.3	-6.7	-5.5								
Unemployment rate (%)	9.4	10.0	9.6	9.9	10.0	10.0	9.9	9.8	9.7	9.5	9.3
Industrial production	-14.9	7.0	3.6	10.2	10.4	3.5	3.5	3.0	3.0	3.0	3.0
Japan											
Real GDP	-5.3	3.3	1.8	5.0	2.3	1.8	1.6	1.5	2.2	1.8	2.0
Private consumption	-1.0	1.9	1.2	1.7	0.0	2.0	1.6	0.5	1.8	0.8	1.5
Business investment	-19.3	2.3	6.0	2.6	8.0	8.0	6.0	6.0	5.0	5.0	5.0
Residential construction	-13.9	-7.7	2.8	1.8	5.0	-5.0	0.0	5.0	5.0	5.0	5.0
Public investment	8.0	-6.8	-11.0	-1.8	-25.0	-10.0	-10.0	-8.0	-10.0	-12.0	-12.0
Government consumption	1.5	1.4	0.9	1.7	1.5	1.0	0.8	0.8	0.8	1.0	1.0
Exports of goods and services	-24.1	25.3	6.5	30.6	30.0	3.0	3.0	4.5	6.0	8.0	10.0
Imports of goods and services	-16.8	9.4	5.7	9.3	20.0	4.0	4.0	4.0	5.0	7.0	7.0
Domestic final sales contribution	-3.5	1.2	1.3	1.6	0.4	1.9	1.5	1.1	1.6	1.0	1.5
Inventories contribution	0.2	-0.2	0.0	0.3	-0.2	-0.1	0.0	0.1	0.1	0.2	-0.3
Net trade contribution	-2.0	2.3	0.4	3.0	2.2	0.1	0.1	0.3	0.4	0.5	0.8
Consumer prices (%oya)	-1.4	-1.0	-0.1	-1.2	-0.9	-1.1	-0.7	-0.5	0.1	0.2	-0.1
General govt. net lending (% of GDP, CY)	-7.2	-7.6	-8.4								
Unemployment rate (%)	5.1	4.9	4.5	4.9	5.2	4.9	4.7	4.6	4.6	4.5	4.4
Industrial production	-21.8	17.8	4.0	30.9	5.8	1.0	3.0	3.0	5.0	7.0	7.0
Memo: Global industrial production											
%oya	-11.0	8.7	4.7	11.4	8.5	3.9	4.1	4.1	4.8	5.2	5.5
				9.1	10.6	8.4	6.8	5.1	4.2	4.6	4.9

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



## Central Bank Watch

	Official interest rate	Change from		Last change	Next meeting	Forecast next change	Forecast				
		Current	Aug '07 (bp)				Sep 10	Dec 10	Mar 11	Jun 11	Sep 11
Global	GDP-weighted average	1.37	-329				1.39	1.44	1.49	1.57	1.62
excluding US	GDP-weighted average	1.96	-240				1.99	2.06	2.13	2.25	2.33
Developed	GDP-weighted average	0.54	-357				0.55	0.57	0.60	0.64	0.67
Emerging	GDP-weighted average	4.70	-216				4.75	4.89	5.04	5.28	5.43
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				4.09	4.11	4.13	4.37	4.86
EM Asia	GDP-weighted average	4.23	-187				4.29	4.50	4.59	4.74	4.78
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	<b>On hold</b>	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)	<u>20 Aug 10</u>	4Q 11 (+25bp)	4.50	4.50	4.50	4.50	4.50
Colombia	Repo rate	3.00	-600	30 Apr 10 (-50bp)	<u>20 Aug 10</u>	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	1.30	1.31	1.39	1.51
Euro area	Refi rate	1.00	-300	7 May 09 (-25bp)	2 Sep 10	<b>On hold</b>	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	4Q 11 (+50bp)	6.50	6.50	6.50	6.50	6.50
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	-	<u>19 Aug 10</u>	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	2.45	2.53	2.57
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	<b>On hold</b>	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	<b>On hold</b>	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	<b>On hold</b>	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	1.625	1.750	1.875	1.875

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

## The J.P. Morgan View: Markets

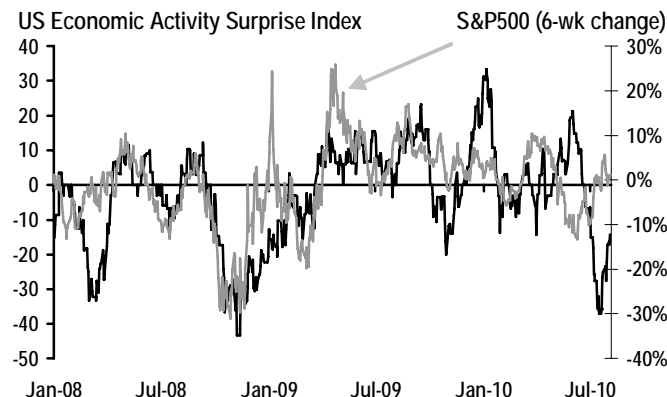
# Ranging risk markets favor income, yield, and spreads

- **Economics** — Weak US retail sales and claims raise downside risks.
- **Asset allocation** — Risk markets have been in a range for almost a year. This will make investors favor income, yield, and spreads over capital gains.
- **Fixed income** — Stay long and in flatteners. MBS now offers good value.
- **Equities** — Downshift in global manufacturing and the search for yield are negative for Industrials and Cyclical sectors more broadly.
- **Credit** — Record US\$22 billion issuance in US HY this week. Stay long given strong demand and strong corporate fundamentals.
- **FX** — JPY forecast to rally to all-time low of 79 versus USD by year-end.
- **Commodities** — Stay underweight in Oil and Base Metals, and overweight Agriculture.

**And there we go again!** A few weaker US economic data prints overwhelmed better news elsewhere and drove risky markets down again, and government bond markets up. The **disappointing economic data** are coming largely from the US, with Europe still surprising on the upside, and Asia moderating in line with our lowered forecasts. Adding it all up, this ought to be a clean neutral, if it were not that US economic data tend to lead the world, while European data tend to lag.

Two US data points stand out—a **fall in core retail sales, and higher unemployment claims**. Core retail sales are flat over the past three months, likely in response to weaker jobs growth. And that is where claims are raising warning flags. Claims are a momentum indicator, and their recent rise suggests the expansion is weakening. Our principal concern is whether businesses are reversing course and turning more defensive, which would pose a fundamental threat to the recovery. Although the relationship between job growth and claims is not tight, our model suggests that employment will stall if claims persist at the current level.

**Are we on the slippery slope toward a double dip?** Our economists have been arguing against a renewed contrac-



tion in the world economy, but accept that growth rates themselves are dipping down again. The issue is by how much. Slower growth comes from the aging inventory cycle in manufacturing and dramatic fiscal tightening in developed markets, not sufficiently offset by an expansion in private demand. The forecast remains for moderation in growth, rather than a dramatic fall, but the recent US data prints are now creating a downside risk bias on forecasts.

Equities, commodities, and credit have now been effectively in a range for almost a year. Without much upside on the economy, investor interest is likely to focus even more than before on the income component of returns instead of on capital gains. This greatly **favors longer-duration bonds, carry trades, and spread product in fixed income, and high dividends, preferreds, and utilities within equities**. It favors most EM asset classes over DM, except equities, where dividend yields are similar to DM.

Moderating growth, but no new recession, and recent range trading in risk markets favor fixed income over equity risk. But surely this flies in the face of the **record-high risk premia that equities offer** over anything in the bond world. US equities now trade at only 12 times the top-down 2011 EPS consensus forecast of US\$88—a real yield over 8%—while 10-year TIPS real yields stand at 1% (and the 5-year at zero). So how can one favor credit over equity risk, as we do?

There is no denying that equity risk premia versus bonds are at historic highs. Most of this is due to record-low bond yields, in turn brought on by record-easy monetary policy. High risk premia on equity are relevant to investors, but likely only for those with truly long-term investment horizons—five to 10 years out—as these risk premia mean-revert at a glacial pace. For the majority of market participants, who need to deliver in one to two quarters, we need to see evidence that investors are reacting to these high equity risk premia. That is, **we need to see the flows**. Our weekly *Flows & Liquidity* provides detailed updates on this. In short, mutual

fund investors heavily favor bonds, and corporates are not rushing out to exploit the equity/bond pricing gap. Global equity buybacks have risen to US\$8 billion per week so far this year from US\$2 billion in 2009. But this is half of the US\$16 billion per week seen in 2007. And M&A is tracking a US\$2 trillion annualized pace so far this year, up 10% from 2009 but half of the pace seen in 2007.

## Fixed income

Central banks signaled that tightening is further away than ever, pushing bonds higher. The Fed's move to reinvest prepayments on its mortgage portfolio in the Treasury market—to the tune of around US\$250 billion over the next year—maintains the very easy stance of monetary policy. Further easing is clearly possible if US data continue to disappoint. Meanwhile, the Bank of England reduced its growth forecast, and continues to expect inflation to fall below target from its current elevated level. **The theme of central banks on perma-hold is strengthening, and augurs even lower yields and flatter curves.**

**Euro area peripherals** underperformed the core, and have now reversed half of July's spread tightening. Ireland led the way, sparked by a greater focus on its troubled banking sector and impending issuance next week. Peripheral government debt will remain vulnerable until budget deficits, and so heavy issuance needs, moderate. It is, however, underpinned both by strong support from the core—the ECB reportedly bought Irish debt this week—and by investor demand for carry as yields on the safest assets become ever less appealing. We stay long the periphery.

US mortgage spreads have been pushed sharply wider by a spate of rumors that the US government will introduce new measures to facilitate mortgage refinancing, perhaps as soon as next week. Refinancing has been subdued despite the low level of bond yields, partly because borrowers have been hampered by low incomes and credit scores. **We think that a government-induced refinancing wave is unlikely, and that MBS offers value at these levels** (see M. Jozoff, Agency MBS, *US FIMS*).

## Equities

Weak US economic data continue to weigh on equities, preventing them from breaking out of their three-month range. The weakness can be seen in our **US Economic Activity Surprise Index** (top chart). The EASI dipped to a low of -37 in mid-July, a level last seen in the months after the Lehman bankruptcy. Despite some improvement over the past few weeks, at -20 the EASI remains very negative by historical standards. The EASI will likely need to turn

positive again for equities to break out of their range. This should allow investors to start focusing on equity valuations, which have become even more compelling following the 2Q reporting season and the recent rally in bonds. But admittedly it will take time for this value to be unleashed, especially as flows continue to favor bonds over equities (see *Flows & Liquidity*, July 30).

**Our strategy focuses on Overweighting EM equities and Underweighting Industrials.** Flows are clearly favoring EM. Flows into EM equity funds totaled US\$20 billion over the past three months. In contrast, DM equity funds saw outflows of US\$40 billion over the same period. Our EM versus DM equity allocation model also favors an EM overweight, as both two-month return momentum and relative IP growth (i.e., the difference between the oya rates in EM IP versus DM IP) are supportive. See *The EM vs. Developed Markets equity allocation*, Koo and Panigirtzoglou, Apr 2009. The trade also benefits from increased deflation concerns in DM. Deflation was disastrous for Japanese equities. Increasing worries that Europe and the US are headed the same way can induce further equity flight into EM.

Industrials are trading at close to recent highs versus the rest of the equity market. The downshift in the global manufacturing sector raises downside risks for industrial and cyclical sectors more generally. This downshift is expected to last for six to 12 months. See *Gravity bites: The global manufacturing downshift has begun*, B. Kasman, July 29. **The search for yield is another headwind for cyclical sectors** as it favors Telecoms and Utilities, which offer dividend yields of 5% and 4%, respectively, well above the average 1.7% dividend yield of cyclical sectors.

## Credit

Credit markets sold off this week due to a string of weak economic data. HY bonds were hit the hardest, on the back of **record issuance**. Despite HY spreads widening this week, investors continue to buy into HY bond funds, a sign of the strong demand of the asset class. The market readily absorbed the mammoth supply of US\$22 billion this week, which is the highest on record and more than four times the year-to-date issuance pace. We continue to favor longs in HY although summer volatility could keep spreads volatile. In the environment of low rates and strong corporate fundamentals, HY will rally into year-end as investors seek better returns.

In addition to HY, EM credits are also attracting ample investor attention. Spreads of **high-grade EM dollar corporate bonds** are significantly higher than US HG bonds, despite better growth prospects in EM compared to the US.



Even if EM and US corporate spreads tighten by the same magnitude, returns would be higher by holding EM corporates due to carry, making it ideal for investors seeking yield. The cumulative inflow into EM fixed income year to date has already surpassed the peak annual inflow into EM, and our strategists see continuing inflow into EM bonds for the rest of the year.

Within US HG, we recommend **overweighting Metal and Mining bonds**, which we upgraded from neutral this week. The Metal and Mining sector is currently trading 24bp wider than the overall HG index and valuation is attractive. Credit metrics are expected to continue improving as current expectations for 3Q results are considerably better than a year ago.

## Foreign exchange

For the past two weeks we have positioned for selective USD weakness—versus JPY given the Fed outlook and versus EUR and CHF given a brief data decoupling between the US and Europe. The yen story has much further to run given the indefinite flow imbalance created by a Japanese trade surplus and declining US yields. **A new all-time low looks likely, so we place the base at 79 by year-end.** Commodity FX forecasts are also lowered to reflect weaker global growth into year-end.

**The long EUR/USD trade is not working.** We expected the strength of European data to allow the euro to rally even in the face of a weak stock market, and particularly given the Fed's easier policy stance. We've been wrong, either because we have mismeasured the extent of euro short covering or because sovereign stress is re-emerging as stocks fall. Take losses on that trade, and profits on long EUR/NZD. The overall portfolio remains defensive: long CHF vs. USD and EUR, and long JPY vs. USD and NZD.

At current levels, the most compelling **vol hedges for deflation** are through commodity currencies and Scandis (liquidity permitting) given how low vol premia have fallen. Commodity and Scandinavian currencies have proven to be by far the best vol hedges in stress episodes historically given the spike in vols that usually accompanies a spot sell-off. These currencies are also prone to sharp squeezes in rallies that keep realized vols firm and make long vol positions less painful to carry. Most of these currencies also have flat-to-inverted vol term structures in the 1-year to 3-year sector as well as steep skews, both of which serve to mitigate the bleed on options with the passage of time. We recommend adding to commodity/USD and commodity/EUR vol spreads.

## Ten-year Government bond yields

	Current	Sep 10	Dec 10	Mar 11	Jun 11
United States***	2.69	3.10	3.10	3.25	3.50
Euro area	2.39	2.30	2.45	2.60	2.75
United Kingdom	3.12	3.25	3.50	3.70	3.85
Japan	0.98	1.30	1.40	1.50	1.55
GBI-EM	6.53			7.90	

## Credit markets

	Current	YTD Return
US high grade (bp over UST)	163	8.9%
Euro high grade (bp over Euro gov)	175	4.8%
USD high yield (bp vs. UST)	696	8.2%
Euro high yield (bp over Euro gov)	690	7.7%
EMBIG (bp vs. UST)	302	11.8%
EM Corporates (bp vs. UST)	347	10.6%

## Foreign exchange

	Current	Sep 10	Dec 10	Mar 11	Jun 11
EUR/USD	1.28	1.25	1.25	1.25	1.25
USD/JPY	86.2	80	79	81	83
GBP/USD	1.56	1.47	1.44	1.42	1.42

## Commodities - quarterly average

	Current	10Q3	10Q4	11Q1	11Q2
WTI (\$/bbl)	75	77	75	75	77
Gold (\$/oz)	1214	1250	1275	1250	1250
Copper(\$/m ton)	7230	6500	6750	6750	7000
Corn (\$/Bu)	4.26	3.90	3.80	4.00	4.20

Source: J.P. Morgan, Bloomberg, Datastream

\*\*\* Under review

## Commodities

Commodities sold off heavily this week, especially oil. We remain **underweight crude oil and industrial metals** due to weakening global growth. Poor US economic data are keeping us cautious on the oil outlook as we see downside risk to the demand forecasts. Moreover, the supply dynamics also seem unattractive as non-OPEC production rises and alternative fuels compete for market shares. These are likely to keep oil prices under pressure. The risk of underweighting oil is a hurricane disrupting oil supply. However, we recommend taking any price spikes to add risk on short oil positions.

The rally in agriculture continued this week and we remain overweight. In addition to the Russian droughts and export bans, the flooding in China is now threatening food supply, especially for grains. The flooding has affected agricultural production, destroying crops and interrupting transportation. Coupled with upside risks in demand forecasts, we stay long agriculture.

## Selected recent research<sup>1</sup> from J.P. Morgan Economics

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

## Economic Research Note

# US: The Fed exits the exit

- Fed asset purchases have served varying roles over the course of the last three years
- The goal of purchasing longer-term Treasuries is to keep long-term rates lower than otherwise
- The ability of these purchases to stimulate the economy is limited

The Federal Reserve's conception of how its balance sheet can be used as a policy tool has evolved over the past three years. The recent decision to reinvest all prepaying and maturing securities on its balance sheet is a reflection of the latest thinking on how the balance sheet can help promote economic recovery. Even though the Treasury market is well-functioning, purchases of longer-term Treasury securities should push down rates at that tenor, and—assuming credit spreads are about unchanged—thereby lower interest rates for private sector borrowers.

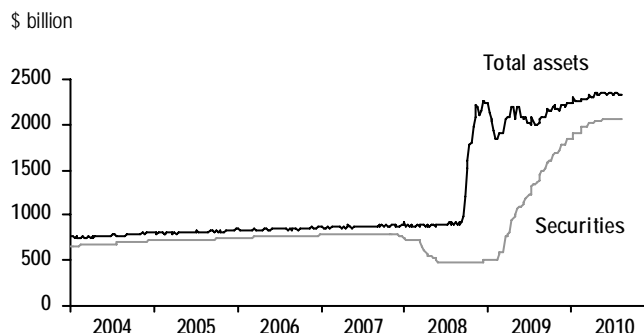
Given this goal, last Tuesday's FOMC decision could be judged a success: longer-term rates did decline following the announcement. To be sure, higher equity prices and a weaker dollar did not follow, so some of the transmission channels probably weren't as strong as one would hope for. Indeed, for all of what remains in the Fed arsenal, the textbook effects should come through their influence on the yield curve. An indirect effect—generally too ethereal to find its way into the textbooks—is their impact on confidence and risk-taking behavior.

## An August surprise

The August 10 FOMC statement landed with a thud: the markets and the media generally responded unfavorably to the latest policy directive. Some of that sentiment was a response to the quite dour outlook for economic growth—surprisingly dour given the relatively reassuring pronouncements of Fed officials in the weeks leading up to the meeting. To be fair to the Fed, early-week accusations of the Fed panicking turned to late-week observations that the economy is tanking, so some of that “panic” looks more justified after seeing the jobless claims and retail sales numbers. Whether in a democratic society a central bank should deliver to the public an outlook for the economy that is more upbeat than its internal forecast is a separate matter that we don't consider here.

This week wasn't the first time that the markets and the Fed misunderstood each other, nor will it likely be the last.

Federal Reserve balance sheet



What is more important is that the public and markets gain understanding of what the Fed is attempting to accomplish with its balance sheet policy. Because the way the Fed has used its balance sheet has evolved over the past three years, so too have the speeches and testimonies of Fed officials describing the intent of the Fed's policies.

One thing that has remained constant is that the liability side of the balance sheet has not been the operative element in the Fed's attempts to shore up the economy or the financial system. The creation of a liability—reserves—has been a by-product of the Fed's purchases of assets. This is in contrast to early manifestations of Japanese QE. The idea, frequently encountered in discussions in the popular media, that the Fed is trying to “flood the economy with cash,” or similarly phrased balderdash, has absolutely no relation to Fed policymaking. Increasing reserves to increase bank lending has not been a goal of the central bank. While this fallacy will not die, the Fed is well aware that it is shortages of bank capital and creditworthy borrowers that are constraining bank lending, not a shortage of reserves.

## The aim of asset purchases

The goal of Fed balance sheet policy has been on the asset side of its balance sheet, to influence the prices of the assets it purchases. During the early period of Fed asset purchases, the assets were mostly illiquid mortgage-related assets. Assets that are illiquid command a lower price and hence will have a higher yield. By providing a bid for these assets, the Fed brought liquidity back into the market. This was called “credit easing” by Chairman Bernanke, to emphasize that the lower mortgage rates that ensued would ease credit conditions for private borrowers.

In some ways this credit-easing period of Fed balance sheet operations is similar to the most traditional role of central banks: lender of last resort. The lender of last resort function presumes that there will be periods when market li-

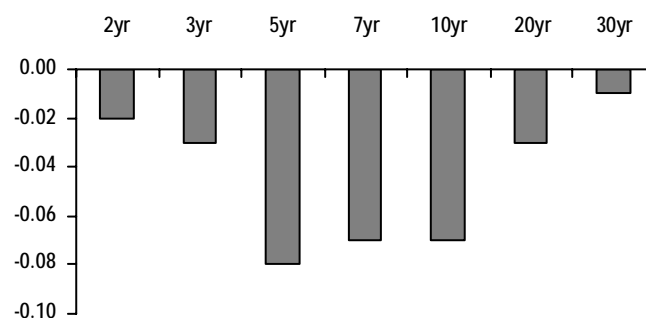
quidity freezes up for perfectly solvent assets. When that happens, the central bank steps in to lend against those temporarily illiquid assets. While the lender of last resort lends, obviously, rather than buys, both operations seek to prevent temporary illiquidity from causing credit conditions to tighten for final borrowers.

When the Fed first conducted large-scale purchases of Treasury securities in March 2009 it was arguable that a similar mechanism was in play: the Treasury market was not functioning perfectly and taking liquidity premia out of Treasury prices would lower rates in that market, which would presumably also affect rates in spread markets that fed through to final borrowers. Even then, that argument was a bit of a stretch, as the Treasury liquidity premium was not huge. Instead, what was likely the most important factor then, and is certainly an even more important factor now, is the portfolio balance effect.

To understand this effect, first imagine investors are indifferent as to whether they bear risk or not. In that case, the rate of interest they would demand for lending for, say, 10 years, would be no different than the rate they would expect to get lending overnight and rolling that loan over every night for 10 years. This way of imagining that longer-term interest rates are set is referred to the Pure Expectations Hypothesis (PEH) of long rates. Of course, investors aren't indifferent to risk, and usually demand extra compensation for bearing the risk of locking their funds up for 10 years. This extra compensation is referred to as term premium. (In principle this could be negative, though in practice it is almost always positive).

Breaking longer-term rates apart into the expected short-rate component and the term premium component, we would expect the short-rate component to respond to expectations for the economy and how the Fed sets overnight rates in response, not to Fed purchases of longer-term securities. However, it is possible term premium is directly affected by Fed asset purchases. Investors earn term premium to hold duration risk; if there is less duration supply—i.e., long-term securities—and the same duration demand, the price will go up and yields will go down: this is the portfolio balance effect. This is the means by which Fed balance sheet policy seeks to affect the economy: by purchasing longer-term Treasury securities, lowering longer-term Treasury rates. These lower rates should affect private borrowing costs, increase assets prices such as equities, and lower the foreign currency value of the dollar.

Change in Treasury yields on day of Aug 10 FOMC announcement



Like most propositions in economics, the portfolio balance effect is not universally accepted. Empirically, however, Fed actions over the past few years suggest it is important. For example, after the March 2009 asset purchase announcement, 10-year Treasury yields fell 47 basis points. The contention that this was a portfolio balance effect rather than shifting expectations of short rates rests on the fact that 2-year yields—presumably a good proxy for short rate expectations—fell by far less, 22 basis points.

Just because it has been important in the past does not mean the portfolio balance effect will be equally important in the future. Indeed, there are many good reasons for thinking that there are diminishing marginal returns to asset purchases: each additional billion in asset purchases probably results in less of a reduction in longer-term rates. This consideration implies the Fed will not embark on another round of large-scale asset purchases unless the scale is very large indeed. Even if it does decide to unleash another massive round of buying—an outcome not in our forecast but certainly feasible if the outlook deteriorates further—the likely impact on already-depressed long-term rates would alone not be enough to kick-start the economy.

The above discussion suggests another means of stimulating the economy: lowering expectations of the path of short rates. This can be done by promising to keep short rates low for a long time, or even by reducing the already low level of short rates by reducing the interest on the excess reserve rate. In either case, the effect on interest rates, and hence on the economy, is probably fairly minor, given that expectations for the first rate hike are generally already pretty distant. Even if the Fed pulls out everything in its arsenal, there is no guarantee that will pull the economy out of the doldrums.



## Economic Research Note

# UK inflation: Sticky, but set to slide faster than the MPC thinks

- Inflation has been both high and sticky despite significant spare capacity
- The MPC and many other forecasters now expect above-target inflation to persist until 2012
- Our forecast sees a gradual slide to just below the target by next spring

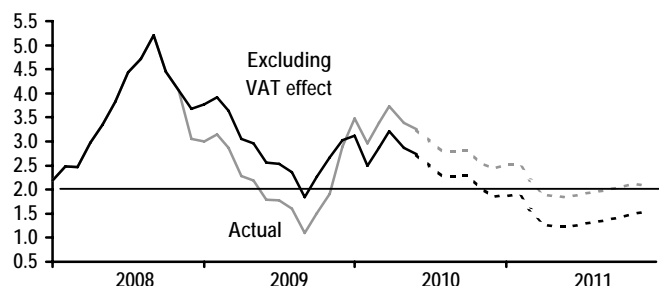
A string of upside surprises has left CPI inflation running well above the MPC's 2% target, and looking pretty sticky. This week saw the MPC revise its inflation forecast to show inflation running well above target until early 2012. Inflation is not expected to stay so high after such a deep recession. Before rewriting the textbooks for the UK, however, there are several factors that point to a slide in inflation over the next year. These are:

- **Smaller import price gains should help core goods prices to weaken.** The weaker currency appears to have had a major influence on goods inflation in the UK. Since the currency has stabilized, import price gains have moderated. This points to a softer trajectory for core goods inflation from here, with other factors including slack and slower ULCs helping to generate small price declines later this year.
- **Energy price inflation will continue to slow, provided oil prices remain under \$90 a barrel.** The rise in oil prices through to April pushed up both petrol prices and inflation. Although oil prices have risen recently, they are still below prior levels, and petrol prices have been falling. This will pull energy inflation lower over the next six months. A rise in oil to \$90 would likely prevent this.
- **Spare capacity should soften services inflation modestly.** Spare capacity has a larger influence on service sector pricing, and has already helped to pull down inflation within the sector. This process will likely continue. But with slack already being absorbed, the size of the downward pull from this source has been reduced.

One factor likely to offset some of these downward pressures is food prices. Commodity prices have been rising briskly, and the recent surge in wheat prices is expected to reinforce this trend in the near term. Based upon a basket of commodity prices, we estimate that food price inflation will accelerate above 4% in the coming months, before

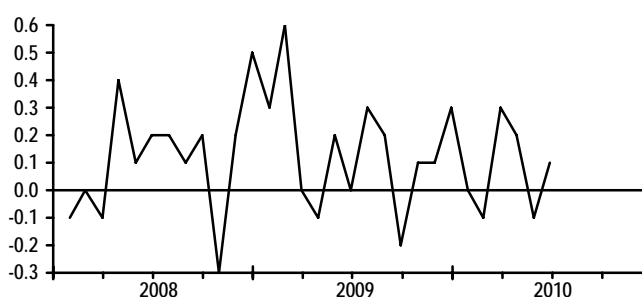
## Headline CPI inflation

%oya, VAT effects estimated by J.P.Morgan



## The balance of inflation surprises

%pt. difference between actual versus consensus forecast for %oya CPI



## J.P.Morgan CPI inflation forecast

%oya	2009			2010				2011		
	1H	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q
Headline %oya:	2.5	1.5	2.1	3.3	3.5	2.9	2.6	2.4	1.9	1.9
Core inflation	1.6	1.8	2.2	3.0	3.0	2.6	2.2	2.2	1.8	1.7
Goods	-1.6	0.3	1.9	2.8	2.2	1.1	0.6	0.9	0.3	0.2
Services	3.8	2.8	2.4	3.1	3.6	3.6	3.3	3.2	2.8	2.7
Contributions to headline CPI %oya										
Food, drink, tob.	1.2	0.5	0.4	0.4	0.5	0.6	0.6	0.4	0.4	0.4
Utility bills	0.7	0.1	-0.3	-0.3	-0.2	-0.2	-0.1	0.0	0.1	0.1
Petrol prices	-0.6	-0.5	0.3	0.8	0.8	0.5	0.4	0.3	0.0	0.1
Core inflation:	1.2	1.3	1.6	2.3	2.3	1.9	1.7	1.7	1.3	1.3
Goods	-0.5	0.1	0.6	0.9	0.7	0.4	0.2	0.3	0.1	0.1
Services	1.7	1.2	1.1	1.4	1.6	1.6	1.5	1.4	1.3	1.2

slowing to 3% next year. These assumptions are all conditional on the currency remaining within a broadly stable range.<sup>1</sup> They imply that CPI inflation (both headline and core) will slow gradually this year, falling back to the 2% target in 2Q11, but hovering around this level until year-end 2011. These estimates include the boost from higher VAT, which is set to rise for a second consecutive year to 20% next January. We estimate that this will add around 0.5% to inflation until the end of 2011. During the remainder of this note, we consider each element of our inflation forecast in more detail.

1. As a rough guide, we have estimated in the past that a further 10% drop in the currency would add 1%-pt to the CPI price level over the following two years.



## Goods price inflation to slide lower

Core consumer goods prices are typically hard to forecast in the UK. The fact that these goods are traded brings into play a number of international factors that must be considered when gauging pricing behavior within the sector. This means that the currency and foreign goods prices can be just as important as domestic factors, such as home-produced goods prices, wages, and slack. To complicate matters further, there appears to have been significant substitution toward foreign-produced goods during the past decade.

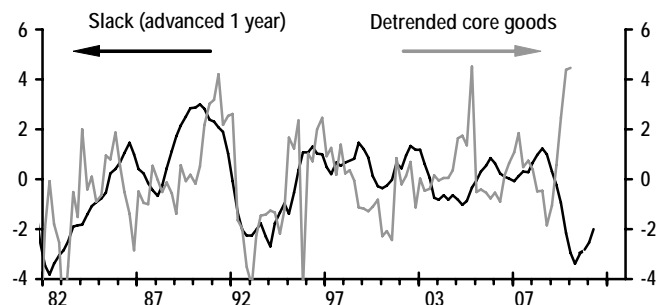
In research we published earlier this year,<sup>2</sup> we modeled CPI core goods inflation using three key inputs: Unit Wage Costs (UWCs), economic slack, and a price proxy for retailers' product costs. The latter was a weighted average of domestically produced and imported core goods prices. We took a best guess at how the rate of substitution had evolved over time, and used this to determine the relative weight used in our product costs proxy. The result of our analysis suggested that, due to imported goods accounting for an increasingly high proportion of retail goods, import prices were a far more important driver of consumer goods price pressures than (domestic) producer prices. The former is also the most significant driver of the near-term outlook for core goods prices in our model.

We estimated that the large drop in the currency in 2008 (and surge in import prices) served to push core consumer goods prices up 2.5% in 2009. With the currency having now stabilized, import inflation has moderated over the past year. And as the third chart to the right shows, this points to a slowing in CPI core goods inflation in the second half of the year. This factor, together with spare capacity and softer UWC growth, leads our model to project falling consumer goods prices this year—with some stabilization in 2011. The model is of course subject to forecast error, and core goods inflation has been somewhat higher than expected recently. However, recent pricing behavior has remained within one standard error of the model's central forecast for inflation, and does not look unusual. We expect a 0.5%oya drop in core goods prices by year-end (excluding VAT effects). This assumes outturns continue to run on the high side of the model's projection.

The drop in oil prices since April has also been lowering petrol prices. With utility bills already down from year-ago levels, the lower level of petrol prices will roughly halve energy inflation by year-end from its current rate of almost 6%. Though oil prices have ticked higher of late, it would take a move up in prices to \$90 a barrel to stop energy inflation from slowing (assuming a stable currency).

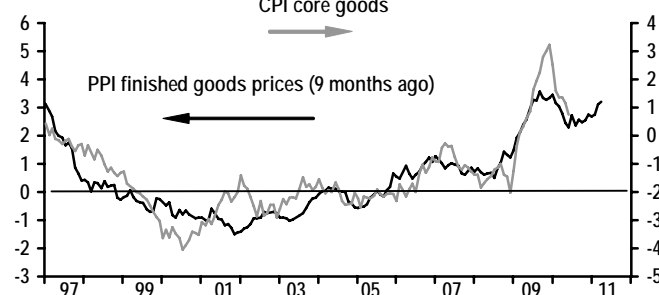
### Core goods prices versus slack

% of potential GDP      %oya, consumption deflator, detrended, excludes VAT



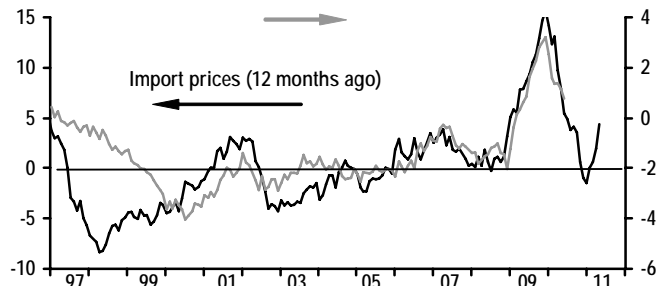
### Finished goods PPI prices versus core CPI goods prices

%oya      %oya, excl. VAT estimate



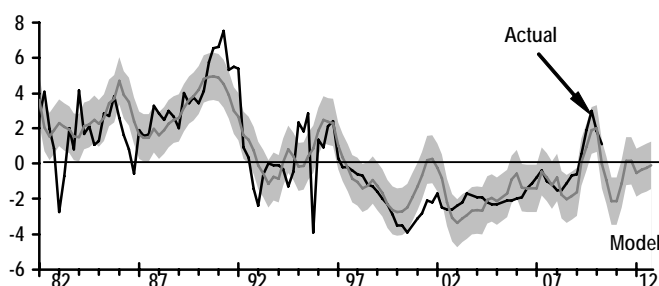
### Core imported versus core CPI goods prices

%oya      %oya, excl. VAT estimate



### Core goods model

%oya, excludes estimate of VAT effect



## Slack should soften services inflation

On our estimates, spare capacity began to build as the economy entered recession in 2Q08. We have found that the degree of slack in the economy is a key driver of services inflation, with a lag of around one year. And sure enough, the widening in spare capacity began to pull services inflation down at the start of 2009. As the recession intensified, our calculations suggest that output was then pushed down to a level around 3.5% lower than potential at the start of last year. This widening in spare capacity shaved a total of 2%-pts off of services inflation from its peak.

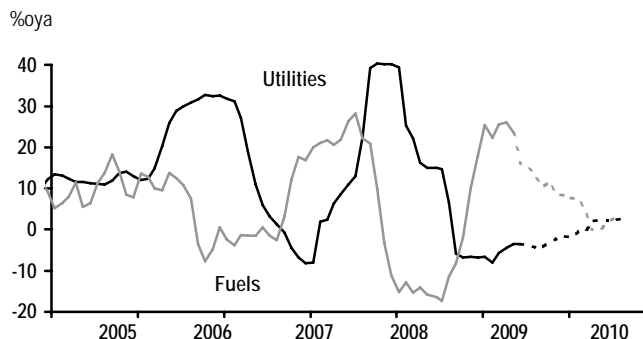
Indeed, this process does not yet look complete. Services inflation has tended to run a little higher than our model (based solely on slack) had suggested. But this behavior does not yet look unusual relative to history. There appears some scope for services inflation to slow from its 2Q10 pace of 3.1% (again excluding VAT). We have assumed a further gradual slowing of 0.5%-1.0%-pts over the next year. This is a similar (but much less extreme) situation to the one seen in the early 1990s recession. Back then, inflation moved clearly outside of the model's range. It did return to the central projection, but not for some time.

One striking development during the recovery has been the faster-than-expected decline in spare capacity. After hitting a trough of 3.5% last April, we estimate that the level of slack has now already fallen back to around 2%. So rather than slow further from here, there is a risk that services inflation simply stabilizes, naturally coming back into line with the lower level of slack in a year's time. Either way, if slack continues to shrink as seen recently, this suggests that service inflation could be rising by the end of 2011.

## Effect of surging food commodity prices

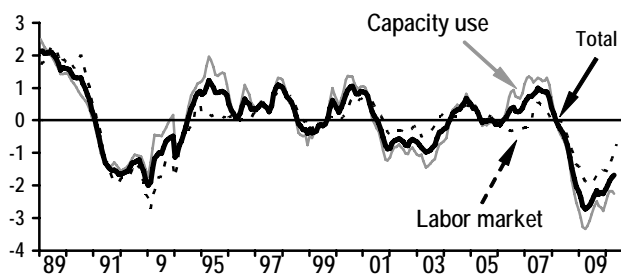
The discussion so far about goods and services has highlighted reasons for expecting inflation to slow over the next six months or so. The behavior of food, alcohol, and tobacco pricing, on the other hand, will likely provide some offset. This partly reflects the period of falling food prices last summer, which is likely to push inflation rates higher this year. But there has also been a notable shift in the price of some food commodities such as wheat and corn. Gauging the effect of these changes is not easy. Food retailers may have contracts that fix the price of imported foods, and cost pressures may be absorbed in profit margins. Bearing these difficulties in mind, we have attempted to quantify the effect of changes in commodity prices on CPI food inflation. We have used the global food commodity price index published by the Food and Agriculture Organization

## Energy price inflation in the CPI



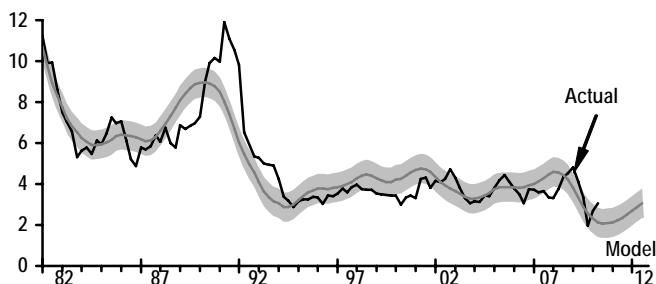
## Components of our composite slack measure

Std devs from mean, negative indicates output is running below normal



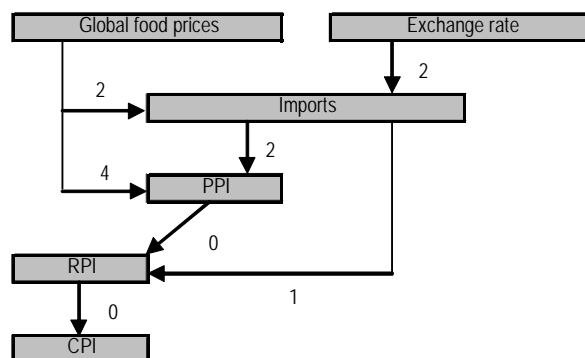
## Services inflation model

%oya, excludes estimate of VAT effect



## Linkages identified in our model of food price inflation

Lags (in months) shown next to arrows



(FAO). Changes in global food prices may impact UK consumer prices either directly (via import price changes) or indirectly (via domestically produced goods price changes). Including currency changes, we have developed a network of equations that estimate the timing and pass-through of changes in global food prices to the CPI (diagram, previous page, and first table, opposite). This suggests that a 10%-pt increase in food commodity prices boosts CPI food prices by slightly more than 1%—but with large errors.

Where food commodity price inflation will run over the coming year is very uncertain. We have made the baseline assumption that global prices expand at a 10%-15% annualized pace. This would be significantly higher than the 3% historical average recorded since the early 1990s, but not as extreme as the 40%-50% pace of increase seen during 2008. On our estimates, this would double CPI food inflation to a 4% pace by the end of this year, before prompting a slowing to a 3% average next year. There are also more specific questions about the effects that individual global commodity price changes will have on the CPI. Once again, there are significant uncertainties with any of these calculations. But to help answer these questions, we have estimated the impact that price changes in a selection of 12 commodities have on the FAO aggregate price index (table). These elasticities were then applied (in the same way as changes in the aggregate FAO index were before) to estimate the impact on CPI inflation. Given the large errors around these estimates, they should only be used as an indicative guide. These estimates suggest that a sustained 50% increase in the global price of wheat may raise CPI food inflation by 0.5%-pt.

## A soft landing after a deep recession

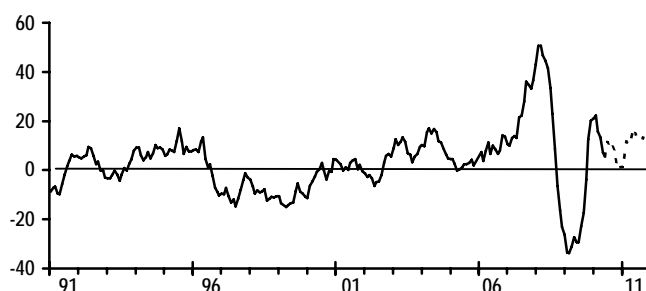
Putting the components of the forecast together, and assuming a 0.5% wedge created by VAT changes, inflation looks set to slide back to target by 2Q11 (see table, first page, for component contributions). Some of the immediate concerns about high inflation should therefore fade. The MPC has struggled to calibrate the impact of various shocks to inflation over recent years, and has been puzzled as to why spare capacity has not had a bigger impact. Our analysis suggests that recent inflation performance can be explained within the usual bounds of error of our models, which suggest inflation should slide from here. Although the balance of inflation surprises may shift in the coming months, our forecast implies only a modest inflation undershoot next year relative to the 2% target. And with slack already being absorbed, inflation is likely to begin rising again by late 2011. The impact of VAT hikes fading from the oya rate, in early 2012, may mask this to some degree.

## Modeling food inflation

%								
Model	Parameters						R <sup>2</sup>	S.E.
	Explanatory variables (%oya)							
	Cons.	RPI	PPI	Imports	E.R.	Global food		
CPI	-0.08	1.11	-	-	-	-	0.98	0.44
RPI	0.79	-	0.56	0.07	-	-	0.65	1.51
PPI	1.12	-	-	0.26	-	0.12	0.80	1.37
Imports	1.70	-	-	-	-0.57	0.22	0.78	2.86

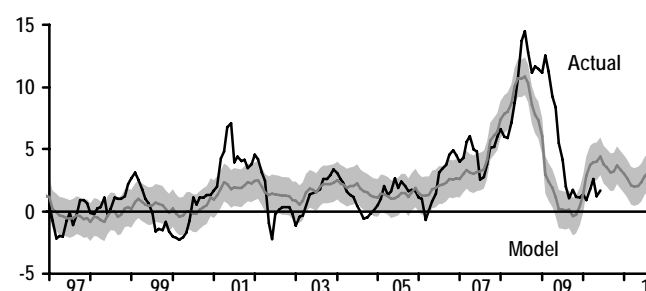
## FAO food price index

%ch over 12 months



## CPI food prices

%oya



## Estimated effects of commodity price changes on inflation

% each case assumes a 10% increase in the corresponding commodity price

	Effect on commodity basket	Effect on food CPI
Barley	0.64	0.08
Bananas	0.06	0.01
Beef	0.84	0.10
Corn	0.60	0.07
Lamb	0.72	0.09
Groundnuts	0.89	0.11
Olive oil	0.38	0.05
Rapeseed oil	0.50	0.06
Rice	0.35	0.04
Suger	1.01	0.13
Soybean	0.34	0.04
Wheat	0.89	0.11

The effect on the food commodity basket is estimated from a regression of FAO food commodity price changes against the joint list of the 14 commodities shown in the table. The FAO includes more commodities than are listed above, but this simple model can explain around 70% of the fluctuations in the FAO index. The effect on the CPI is derived using the system of food price equations shown in the table and diagram above.

But the lower currency, VAT hikes, and a damaged supply side are key reasons why the recession and early part of the recovery will see a relatively limited slowdown in inflation.

## Economic Research Note

# Australia's federal election still too close to call

- The August 21 election will be tight; current polling suggests government will be reelected, but only just
- Little policy differentiation between the major parties, except on the proposed mining tax
- Both sides committed to delivering budget surplus by 2012-13 and curbing immigration

Australians go to the polls on August 21 to elect a federal government for the next three years. Newly installed Prime Minister Julia Gillard, whose supporters deposed former PM Kevin Rudd in late June, opportunistically called an early election, hoping voters would react favorably to the change from the unpopular Rudd. Opinion polls suggested initially that the tactic had worked, but more recent polling shows the opposition party closing the gap on the government. In fact, the latest published polls indicate that the election will end in a photo finish, with the outcome ultimately decided in two dozen or so key marginal seats.

On a two-party preferred basis (that is, after distribution of second and subsequent preferences of minor parties to Labor and the Coalition), 52% of voters favor the Labor government, leaving 48% for the Coalition. If replicated on polling day, the government probably would be reelected with a reduced majority of seats in the Lower House of Parliament, where government is decided. In the 2007 election, Labor won with 53% of the vote. Respondents to opinion polls are fickle, though, with the opposite results recorded in an identical poll a week earlier. Bookmakers, who arguably have a better track record of predicting election results than the pollsters, still favor the government being reelected, and by some distance. Indeed, the betting odds favoring the government shortened this week.

## States of play

In the 2007 election, Labor won 83 of the 150 seats in the Lower House. Population redistributions, though, have notionally given Labor an extra five seats with sitting Coalition members. The Coalition now (notionally) has 59 seats, and there are three independents, each of whom is likely to be reelected. The redistribution favoring the government means the Coalition now needs to win 14 seats to seize government with the help of independents, which would require a national swing away from Labor of 2.4%.

## Australia's Parliament: state of the houses

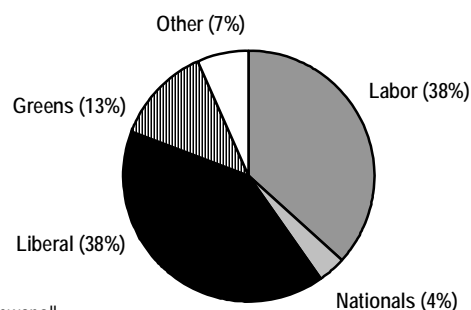
Number of seats (after latest redistributions)

	Lower House	Upper House
Liberal (Coalition)	50	32
Country Liberal (Coalition)	-	1
National (Coalition)	9	4
Labor	88	32
Green	-	5
Family First	-	1
Independent	3	1
Total seats	150	76

Source: Australian Electoral Commission, Parliament

## Voting intentions: all parties

Percent



Source: Newspoll

There are vast differences in voters' preferences across the six states. The government is particularly vulnerable in the mining states, Western Australia (WA) and Queensland, where Labor could lose up to 12 seats. Hostility to Labor's proposed mining tax is most acute in WA, while former PM Rudd, whose brutal political assassination bred resentment, hails from Queensland, where there is a clutch of marginal seats. The toxically unpopular state Labor government in New South Wales is a drag on Labor's vote there, but Prime Minister Gillard is popular in South Australia, where she lived as a child, and in Victoria, where she now resides. Labor probably will retain all its seats in Tasmania.

The tight polling hints that the election could deliver a hung Parliament, but this is unlikely; the last time this happened in Australia was 1940. A hung Parliament would necessitate the formation of coalitions, the most likely being an alliance between the right-of-center independents and the Coalition. Labor would struggle to gain the lasting support of the independents, and the Greens probably would not have sufficient Lower House seats to be influential.

## The role of the Greens

High voter dissatisfaction with the major parties means that there will be a high minor party vote. Voter preference for the Greens, in particular, is at a record high, but history



suggests this will cool by election day. The Greens, the largest minnow, will play a key role in the outcome of the election. Some 80% of second preferences of Green voters flowed to Labor at the last election. Essentially, the Greens drained votes from Labor, but returned them via preferences. How preferences flow at this election will be crucial. Voters can control where their preferences go, but a deal between the Greens and Labor could encourage another high flow of preferences to Labor. This could, for the first time, see a Green member elected to the Lower House.

The growing influence of the Greens, though, will be most evident in the Upper House, where they already have five Senators. Polling suggests the number of Green members in the Senate could swell to as many as 10; they almost certainly will hold the balance of power. A reelected Labor government could find support from the Greens on key policies, including a more onerous mining tax, which the Greens favored in its original form. The Greens would be more hostile to a Coalition agenda, should the opposition win the election. This would result in a Coalition government facing trouble implementing its legislative agenda, even with a clear mandate from voters. The incentive then, should the Coalition win the election, would be to rush through legislation before the new Senate sits from mid-2011.

## Coalition easily leading in “spendathon”

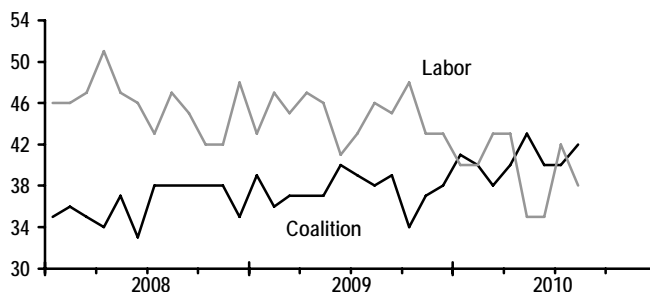
As is usual during an election campaign, both parties have announced a considerable number of new spending initiatives. The Coalition, with spending on promises already worth more than A\$20 billion, has by some distance “out-spent” the government’s promised A\$5 billion. Both parties have pledged to match new spending with savings elsewhere, so that the impact on the Budget is minimal. Predictably, health and education, both of which are potential election-swinging issues, have received most attention.

The election, though, probably will be decided on voters’ preferences on four policy issues: the economy (including Labor’s patchy track record), climate change, immigration, and the mining tax. On the economy, the parties essentially have the same policies—returning the Budget to surplus by 2012-13, providing offsetting savings for new spending measures to maintain budget discipline, and maintaining the independence of the RBA. The direction of interest rates unexpectedly has been a “sleeper” issue in the campaign, following the RBA Board’s decision to leave the cash rate steady earlier this month. A rate hike would have damaged Labor’s chances, but the government dodged that bullet.

There is broad consensus across the major parties on immigration policy: both parties pledge to lower the annual in-

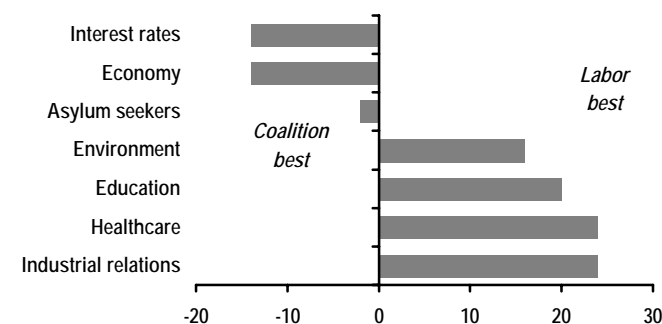
## Voting intentions: major parties

Percent



Source: Newspoll

## Voters' perceptions, preferred party by issue, net %



Source: AC Nielsen

take, and both are determined to slash illegal entries. The business community is appalled at the thought of lower skilled immigration, but, for now, populism rules. On other key policy issues, though, there is differentiation. Tony Abbott, the leader of the Coalition, has pledged to abolish even the recalibrated mining tax. Labor pledges to push ahead with the reworked 30% tax on the “super” profits of mining companies from mid-2012; Labor’s original proposal was for a 40% tax.

On climate change, PM Gillard has delayed the start of an emissions trading scheme (ETS) until at least 2012. Abbott opposes an ETS and previously has dismissed arguments that humans contribute to global warming. Both parties’ indecision over how to tackle climate change explains the high implied vote for the Greens. Abbott also has pledged to cancel the government’s planned rollout of the A\$35 billion National Broadband Network.

## Election is anyone’s to lose

With the election on a knife edge, the outcome could depend on which leader avoids mistakes in the final week of campaigning. Thus far, Abbott has averted disaster by presenting himself as a “small target,” while Gillard has avoided land mines such as former PM Rudd’s potentially destructive appearance on the campaign trail.



## United States

- **Latest reports on jobless claims, retail sales, and mortgage applications point to slow GDP growth**
- **Risks to the 2.5% GDP forecast for 3Q10 are on the low side; first Fed rate hike not expected until 2Q12**
- **Upcoming reports on jobless claims and August business surveys will help clarify the extent of weakness**

The latest round of reports on growth continue to come in on the low side of expectations. The combination of rising initial jobless claims and soft consumer spending poses downside risks to the forecast of 2.5% real GDP growth this quarter, and the government's estimate of growth last quarter is likely to be revised down to 1.3% (from the first estimate of 2.4%).

In response to the combination of disappointing growth and low core inflation, the forecast for the first Fed tightening has been pushed out even further to 2Q12 (from 4Q11).

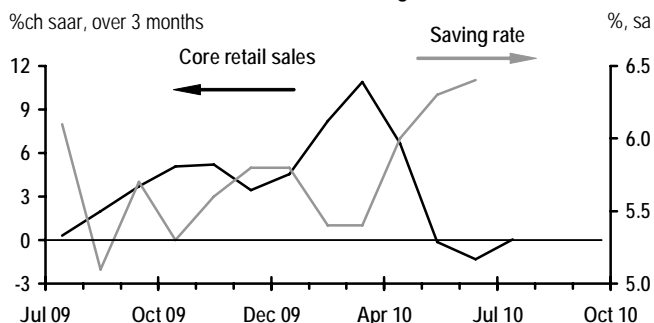
**Jobless claims are up:** Initial jobless claims have been remarkably stable most of the year, averaging within 10,000 of 458,000 for every month since February. But the two latest readings have each exceeded 480,000 and the four-week average is up to 473,500, its highest level since the week of February 20. While two weeks do not make a trend, the latest reports hint that the August labor market report could be even weaker than the past few.

**Consumer spending is tracking low:** Core retail sales rose 0.4% in July on the back of higher unit auto sales and higher gasoline prices. But core retail sales declined 0.1% in July and the trend in core retail sales has slowed dramatically since March. Early in the third quarter, real consumer spending growth is tracking only 1.2% saar, well below the prior forecast of 2.4% growth for the quarter.

**Mortgage purchase applications are not responding to lower mortgage rates:** One way in which an economy going through a soft patch can right itself is through financial market stabilizers. The latest flurry of soft data has brought long-term interest rates down, with 30-year mortgage rates more than 50 basis points below their 1H10 average. But mortgage applications for home purchase have not responded and remain mired near lows reached immediately after the expiration of the home buyer tax credits.

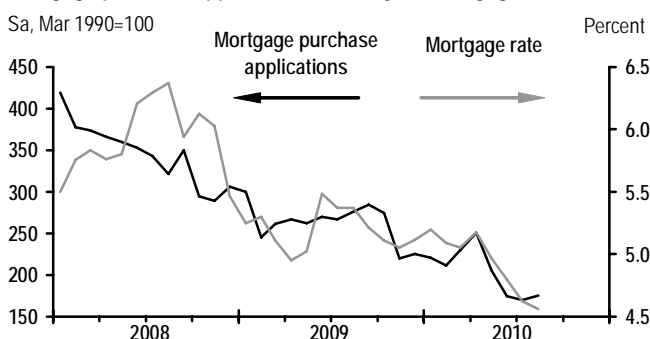
**2Q GDP growth will be revised down:** June inventories were weaker than assumed by BEA in the first estimate of 2Q10 real GDP growth, and the June foreign trade gap was

### Core retail sales and the household saving rate



Note: Retail sales plotted through July, saving rate through June.

### Mortgage purchase applications and 30-year mortgage rate



Note: Chart shows monthly averages and the latest observations.

much wider. These releases account for the expected large, downward revision to 2Q10 real GDP growth.

Upcoming reports, including another week of jobless claims, early August manufacturing surveys from the New York Fed (Monday) and the Philadelphia Fed (Thursday), and the August Homebuilders survey (Monday), will provide additional timely information about the pace of expansion this quarter.

## Spending remains sluggish in July

Both the 0.4% increase in July retail sales and the composition of growth were largely as expected. Sales at auto dealers rose 1.6% samr, in line with the reported rise in unit new cars and light trucks; sales at gasoline stations rose 2.3% reflecting higher fuel prices; and core retail sales (ex. autos, gasoline, and building materials) edged down 0.1% in line with anecdotal reports of sluggish chain store sales.

Core retail sales accelerated through the first quarters of the expansion and were up 10.9% saar in the three months through March. They have slowed dramatically since, and were unchanged in the three months through July.

Although total retail sales rose 0.4% in July, the CPI rose 0.3%, and it appears that total real consumer spending (including services) was probably unchanged on the month. The reinstatement of extended unemployment benefits should give a small lift to consumer spending in August. But, the forecast for real consumer spending this quarter is being lowered to 1.5% (from 2.4%).

The forecast for overall real GDP growth is being held at 2.5%, with an upward revision to the forecast contribution from inventories offsetting the downward revision to consumer spending. Since the pace of inventory accumulation in 2Q10 is apt to be revised sharply lower, it now seems likely that inventories will be about neutral for growth this quarter rather than the 0.9% drag that was in the forecast.

### Core CPI up 0.13% in June, 0.9%oya

The July CPI rose 0.3%, mainly due to the 4.6% rise in the price of gasoline. But the core CPI maintained its recent trend with a 0.1% increase and held at 0.9%oya. To be sure, the core CPI was up 0.13% to two digits, and the latest wiggle in core inflation has been up for both core goods and core services, leaving the core CPI up 1.7% saar over the past three months.

The forecast views the recent, slightly higher readings for the core CPI as a wiggle up (similar to those that occurred in mid-2008 and 2Q09), rather than a reversal of the slowing trend. Most features of the economy argue for lower inflation, including the abundant slack and the sluggish pace of consumer spending.

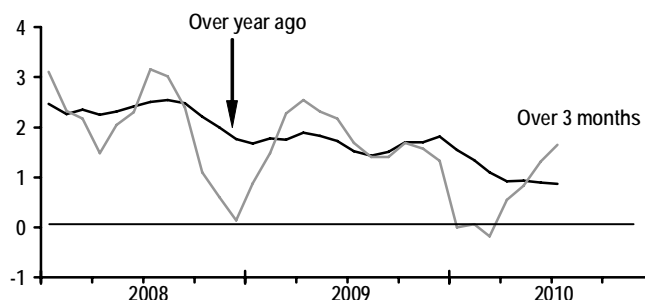
In addition, import prices are slowing and are also having a damping effect on US inflation. Nonfuel import prices declined in July for the second month in a row and have slowed to -1.0% saar over the past three months. Much of the overall slowing in the past few months reflects recent weakness in the price of industrial materials. But the price of nonauto consumer goods also declined in both June and July and is down 1.1% nsaar over the past three months.

### Import surge looks to be short-lived

The foreign trade deficit widened to -\$49.9 billion in June from -\$42.0 billion in May despite a monthly decline in the value of oil imports. Merchandise import volumes surged 4.8% in June following a 2.9% increase the month before and are up 27.6% saar in the three months through June. In contrast, merchandise export volumes declined 1.6% samr in June and are down 5.8% saar in the three months through June.

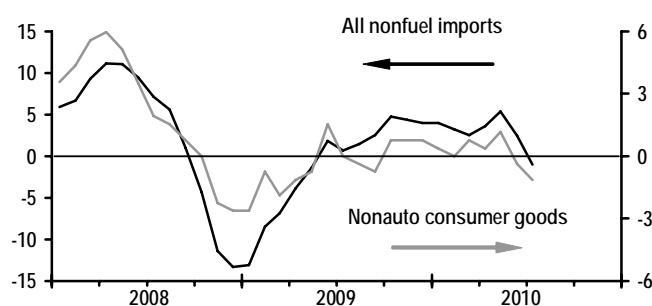
#### Core CPI

%ch saar



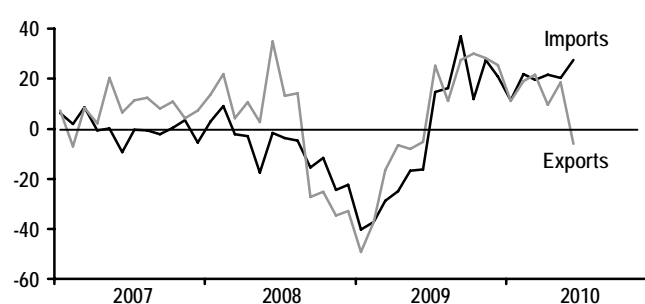
#### Import prices

%ch saar over 3 months, both scales



#### Merchandise import and export volumes

%ch saar, over 3 months



Foreign trade reports are sometimes choppy, and the extreme contrast between import and export performance lately seems like an outlier. Strong import growth is unlikely to be sustained against a backdrop of slower US consumer spending and moderating IP growth. Similarly, the decline in export volumes over the past three months does not seem to fit with either estimates of foreign growth or the results of business surveys. The ISM manufacturing survey, for example, posted readings for export orders of 56.0 in June and 56.5 in July, consistent with healthy gains rather than outright declines. The huge drag on real GDP growth from net exports in 2Q10 will likely be followed by much weaker import growth, stronger export growth, and a positive contribution from net exports this quarter.

## Data releases and forecasts

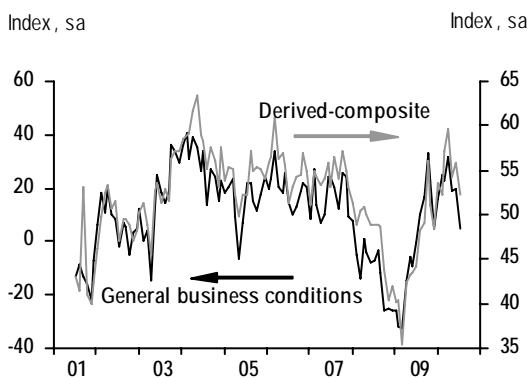
Week of August 16 - 20

Mon	Empire State survey				
Aug 16	Diffusion indices, sa				
8:30am		May	Jun	Jul	Aug
	General bus. conditions	19.1	19.6	5.1	<u>8.0</u>
	New orders	14.3	17.5	10.1	
	Shipments	11.3	19.7	6.3	
	Unfilled orders	-7.9	-1.2	-15.9	
	Prices paid	44.7	27.2	25.4	
	Prices received	5.3	4.9	-1.6	
	Composite	54.3	55.8	52.3	

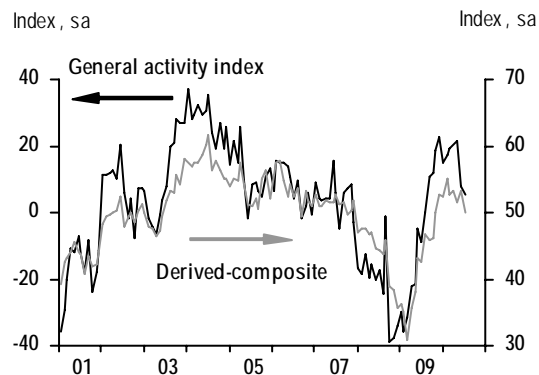
Thu	Philadelphia Fed survey				
Aug 19	Diffusion indices, sa				
10:00am		May	Jun	Jul	Aug
	General bus. conditions	21.4	8.0	5.1	<u>7.0</u>
	New orders	6.1	9.0	-4.3	
	Shipments	15.8	14.2	4.0	
	Inventories	-7.9	4.6	4.5	
	Prices paid	35.5	10.0	13.1	
	Prices received	3.5	-6.5	-8.4	
	Composite	51.6	53.3	50.0	

The Empire State and Philadelphia Fed surveys have both shown significant slowing in manufacturing activity recently. The Empire State survey fell 14.5 points in July and the Philadelphia Fed survey fell 13.4 points in June; both surveys sit at 5.1 as of July. We expect to see slight rebounds in these surveys since they declined more than the other regional surveys in July, but we do not anticipate any major improvements in the August data. We look for the Empire State survey to increase 2.9 points to 8.0 and the Philadelphia Fed survey to increase 1.9 points to 7.0.

## Empire State survey and derived-composite



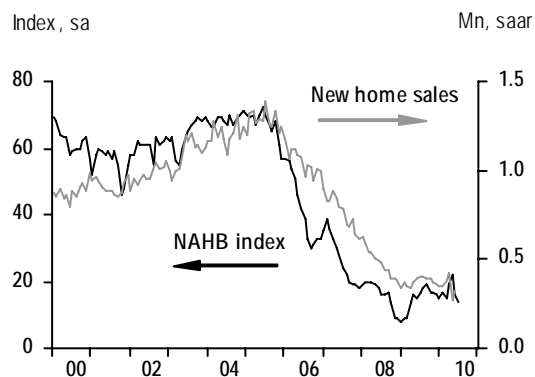
## Philly Fed general business activity and derived-composite



Mon	Homebuilders survey				
Aug 16	Sa				
10:00am		May	Jun	Jul	Aug
	Housing market	22	16	14	<u>15</u>
	Present sales	23	17	15	
	Prospective buyer traffic	16	13	10	

We expect the NAHB survey to increase 1 point in April to 15. The index should remain near the low levels we have seen since it dropped off after the expiration of the home buyer tax credit. The volume of mortgage applications has been low since the credit ended although data for the first week of August show a slight increase in applications. The early August data on mortgage rates show that rates have continued to decline since April.

## NAHB index and new home sales



Tue  
Aug 17  
8:30am

**Producer price index**  
%/m sa, unless noted

	Apr	May	Jun	Jul
Finished goods	-0.1	-0.3	-0.5	<u>0.1</u>
%oya nsa	5.5	5.3	2.8	<u>4.1</u>
Core	0.2	0.2	0.1	<u>0.2</u>
%oya nsa	1.0	1.3	1.1	<u>1.4</u>
Energy	-0.8	-1.5	-0.5	<u>-0.9</u>
Cars	0.6	0.2	-0.5	<u>0.2</u>
Trucks	-0.2	0.8	-1.0	<u>0.6</u>
Core intermed.	1.1	0.3	-0.4	<u>-0.2</u>
Core crude	4.0	-1.6	-4.8	

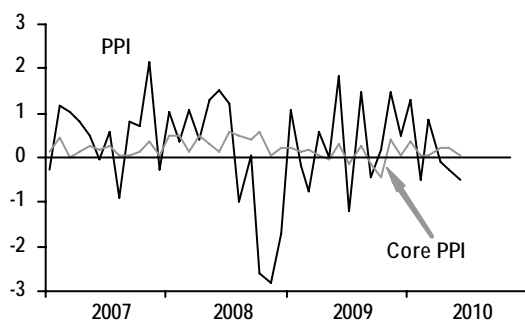
We expect the headline PPI for finished goods to edge up 0.1% in July after decreasing the prior three months. We anticipate that the core PPI measure, which has been rising steadily since November 2009, should increase another 0.2% in July.

Within the core measure, we expect prices of cars to increase 0.2% and trucks to increase 0.6%; both of these measures were down last month and tend to be volatile. Excluding light vehicles, we expect the core PPI to increase 0.1%, which is slightly softer than the trend we have seen since March 2010.

Outside of the core measure, we expect falling energy prices to continue to weigh on the headline measure. Industry data suggest that energy prices will be down 0.9% in July, which is in line with the weakness seen in recent months. We expect food prices to increase 0.8% in July after being down in the prior three months. The Department of Agriculture reported that prices received by farmers for farm products increased 3.6% in July.

**Producer price index for finished goods**

%/m



Tue  
Aug 17  
8:30am

**Housing starts**  
Mn units, saar

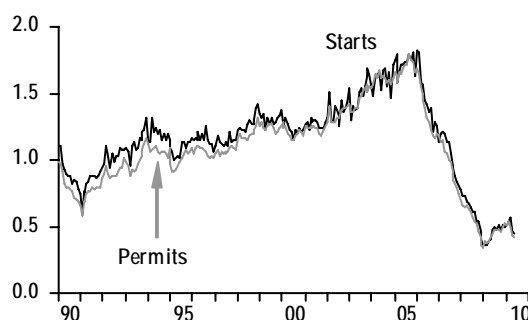
	Apr	May	Jun	Jul
Starts	0.68	0.58	0.55	<u>0.54</u>
Single-family starts	0.56	0.46	0.45	<u>0.44</u>
Multifamily starts	0.12	0.12	0.10	<u>0.10</u>
Permits	0.61	0.57	0.58	<u>0.57</u>

We expect total housing starts to continue to decline in July with the third straight monthly decline in single-family starts. The steep dropoff in single-family starts following the end of the home buyer tax credit moderated in June, but since permits are running below starts, we look for an additional 4% decline in single-family starts in July. This would keep single-family starts at a very depressed level, but still above the levels seen between November 2008 and May 2009. We expect multifamily starts to bounce back 10% after dropping 21.5% in June.

Single-family permits have declined since April and we anticipate a further decline of 1.3% in July. There were strong increases in multifamily permits in the past two months and we look for permits to come down 5.0% in July.

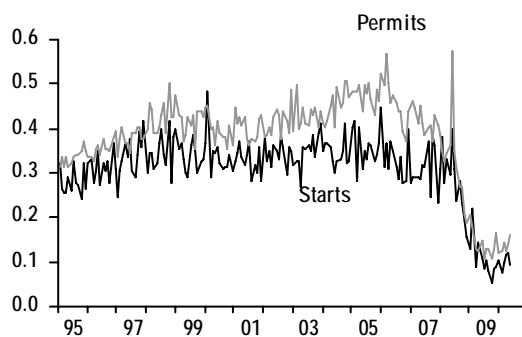
**Single-family starts and permits**

Millions, saar



**Multifamily starts and permits**

Millions, saar



Tue  
Aug 17  
9:15am

**Industrial production**  
%/m sa, unless noted

	Apr	May	Jun	Jul
Industrial production	0.3	1.3	0.1	<u>1.1</u>
Manufacturing	0.8	1.0	-0.4	<u>1.0</u>
Motor vehicles and parts	-1.2	5.6	-1.9	<u>8.3</u>
High-tech	1.5	1.4	1.2	
Mfg ex motor vehicles	0.9	0.8	-0.3	<u>0.7</u>
Business equipment	1.8	1.4	0.9	
Capacity utilization (% sa)	73.1	74.1	74.1	<u>75.0</u>
Manufacturing	70.9	71.7	71.4	<u>72.2</u>

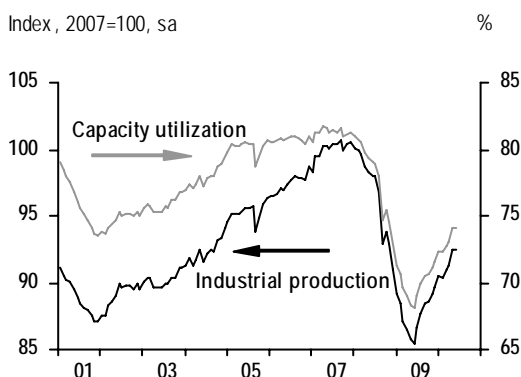
We expect industrial production to increase 1.1% in July after increasing 0.1% in June. The details of the June IP report were soft, but a 2.7% increase in utilities production boosted the headline number. In July, we expect utilities production to continue to surge (+2.5%) as temperatures continued to be hotter than normal, but we expect a much more well-rounded IP report in July than in June.

In July, hours worked in the manufacturing sector increased and we look for overall manufacturing production to increase 1.0%. We also saw very strong data on production of autos for July and we forecast an 8.3% increase in the production of motor vehicles and parts.

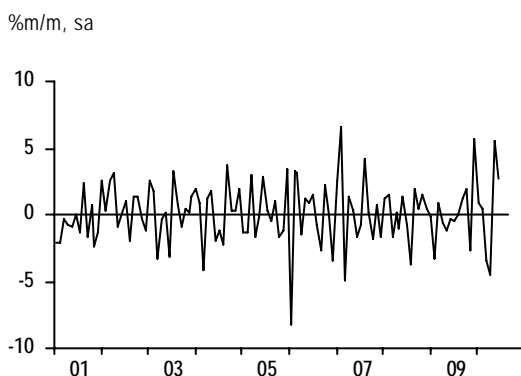
We anticipate mining production increasing 0.5% in July after rising 0.4% in June. There was an increase in hours worked of mining workers in July as well as a growing number of active rigs and increased crude oil field production.

The forecast increase in industrial production should lead to capacity utilization increasing 0.9%-pts to 75.0% in July.

#### Industrial production and capacity utilization



#### Industrial production - utilities



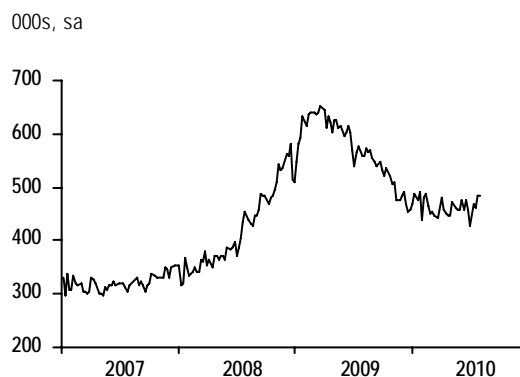
Thu Aug 19 8:30am	Jobless claims		000s, sa				Insured Jobless,%
	<u>New claims (wr.)</u>		<u>Continuing claims</u>				
	Wkly	4-wk avg	Wkly	4-wk avg			
	Jun 5	459	464	4593	4608	3.6	
	Jun 12 <sup>1</sup>	476	464	4573	4593	3.6	
	Jun 19	459	463	4637	4573	3.6	
	Jun 26	475	467	4434	4559	3.5	
	Jul 3	458	467	4710	4589	3.7	
	Jul 10	427	455	4484	4566	3.5	
	Jul 17 <sup>1</sup>	468	457	4568	4549	3.6	
	Jul 24	460	453	4570	4583	3.6	
	Jul 31	482	459	4452	4519	3.5	
	Aug 7	484	474				
	Aug 14 <sup>1</sup>	475	475				

1. Payroll survey week

Initial jobless claims for the week ending August 7 increased 2,000 to 484,000. This is the highest level of initial claims since the week ending February 20 and the second consecutive week in which claims have been above the level seen throughout most of the year. The data on continuing claims have been volatile recently within a range; continuing claims now sit toward the low end of this range after declining 118,000 to 4,452,000 for the week ending July 31. The four-week moving average for continuing claims remains stable at 4,519,000. The insured unemployment rate for the same week edged down from 3.6% to 3.5%. The number of Emergency Unemployment Compensation claimants has increased in the two weeks since the program was reinstated; the number of claimants for the week ending July 24 increased 1.2 million to 4.5 million. Note that EUC has not affected the continuing claims data since they are reported separately.

We expect initial claims to remain high but to drop a bit in the week ending August 14, with claims declining 9,000 to 475,000.

#### Initial jobless claims





## Review of past week's data

### Productivity and costs (Aug 10)

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

	4Q09	1Q10	Prel 2Q10		
Productivity	-6.3	6.0	-2.8	3.9	<del>-0.7</del> -0.9
%oya	-5.6	6.2	-6.1	6.3	<del>-4.0</del> 3.9
Output	-7.0	6.7	-4.0	5.0	2.6
%oya	-0.3	0.3	-3.0	3.2	3.9
Hourly compensation	-1.9	1.5	-1.5	0.0	<del>-0.3</del> -0.7
%oya	-0.2	2.5	-1.6	3.5	<del>-0.6</del> 1.0
Unit labor costs	-7.0	-4.2	-1.3	-3.7	<del>-0.4</del> 0.2
%oya	-5.1	-3.5	-4.2	-2.7	<del>-3.2</del> -2.8
Hours	0.7		1.1		<del>-3.4</del> 3.6
%oya	-5.6	-3.0	-2.9	<del>-0.1</del> 0.0	

Nonfarm business productivity growth declined 0.9% saar in the preliminary 2Q10 report, marking the end of a period of strong growth. In the prior five quarters, productivity had increased by an average of 5.7% saar. The decline in 2Q came as the amount of hours worked surged 3.6% saar—the largest increase in more than four years—while nonfarm business output grew at a slower pace (+2.6% saar) than in 1Q (+5.0% saar). Even though compensation per hour fell 0.7% saar, unit labor costs increased 0.2% saar in 2Q, reflecting the decline in productivity; unit labor costs had decreased in the prior three quarters as strong productivity growth outpaced increases in hourly compensation.

Manufacturing productivity continued to grow in 2Q, up 4.5% saar. This growth is in line with the long-term trend for the data after manufacturing productivity looked exceptionally strong in the second half of 2009.

The 1Q10 productivity data were revised up 1.1%-pts to 3.9% saar to match an upward revision to output. The change in unit labor costs were revised down about 2.5%-pts to -3.7%. For 2009, productivity growth was revised down slightly while the decline in unit labor costs was less than previously reported. Productivity growth was revised down and unit labor costs were revised up for 2008 and 2007, though the revisions to 2008 were more significant than those for 2007.

### International trade (Aug 11)

\$ bn, samr

	Apr	May	Jun		
Balance (BOP basis)	-40.3	-42.3	-42.0	<del>-40.5</del>	-49.9
Services	12.2	-12.2	12.4	<del>-12.4</del>	12.1
Merchandise	-52.5	-54.5	-54.3	<del>-53.0</del>	-62.0
Exports (%m/m)	-0.7	-2.4	2.5	<del>-1.0</del>	-1.3
Imports (%m/m)	-0.4	-2.9	2.8	<del>-0.5</del>	3.0

The trade balance widened out to \$49.9 billion in June from \$42.0 billion in May, as imports leaped 3.0% while exports slid 1.3%. The decline in exports was not particularly striking, as it followed a 2.5% increase in May. It was rather the increase in imports, which followed a 2.8% increase in May, that was more eye-catching. The surge in imports was even stronger in real terms: up 4.8% in June after a 2.9% increase in May, the strongest two-month run on record. This strength in real imports was mostly in consumer goods,

which are up 15.6% over the last two months. Given this end-use product, it is not surprising to see Chinese imports still running strong, up 37% over a year ago. This lift to imports may represent the last push of Chinese exporters ahead of the July 15 expiration of their VAT rebate.

### Import prices (Aug 12)

%m/m nsa, unless noted

	May	Jun	Jul		
Import prices	-0.5	-0.8	-1.3		0.2
%oya	-8.7	8.5	-4.5	4.2	<del>-5.4</del> 4.9
Ex fuel import prices	0.5	-0.6	-0.5	<del>-0.0</del>	-0.3
%oya	3.6	-2.8	2.9	<del>-3.0</del>	2.8

Import prices increased 0.2% in July and are now up 4.9% oya. The headline reading was boosted by a 2.0% increase in petroleum prices. This contrasts the prior two months in which declining petroleum prices pulled down the headline import price index. Excluding fuels, however, import prices looked soft. Nonpetroleum import prices declined 0.2% and nonfuel import prices fell 0.3% in July and are only up 3.1% oya and 2.8% oya, respectively.

Import prices of capital goods were driven down by lower prices for computers, peripherals, and semiconductors and fell 0.1% for the second straight month in July. Consumer goods decreased 0.2% in July as prices for home entertainment equipment fell. Prices of nonpetroleum industrial supplies fell 0.7% on top of a 1.4% decline in June as a result of declining prices for unfinished metals and building materials. Auto prices and food prices bounced back in July—both increased 0.4% after declining in June.

The export price index also fell 0.2% in July after dropping 0.8% in June on declines in the prices of fuels, chemicals, and steelmaking materials.

### Retail sales (Aug 13)

%m/m sa

	May	Jun	Jul		
Total	-1.1	-1.0	-0.5	-0.3	<del>-0.5</del> 0.4
Ex autos	-1.2	-1.3	-0.1		0.2
Ex autos and gas	-1.0	-1.1	-0.1	0.2	-0.1
Building materials	-9.0	-8.9	-1.0	-0.8	<del>-1.5</del> -0.3
Control group <sup>1</sup>	-0.5		-0.1	0.0	<del>-0.3</del> 0.2
Ex gasoline	-0.2		-0.2	0.3	<del>-0.0</del> -0.1

1. Control group is total less automotive dealers and building materials.

Retail sales rose 0.4% in July, thanks to an already-reported increase in auto sales and a bump-up in gas station sales on the back of higher fuel prices. Excluding autos and gas, however, retail sales fell 0.1%. More generally, after starting the year off pretty well, ever since April retail sales have generally been a disappointment. The core retail sales measure, which excludes autos, gas, and building materials sales, was down 0.1% last month and is unchanged over the prior three months. Given the soft trajectory in retail sales, real consumer spending in the third quarter is tracking about a 1-1/4% annual rate of increase, a modest slowing from the already-soft 1.6% second quarter pace. The sluggish growth

in retail spending is the unavoidable outcome of a labor market that is barely producing jobs. The soft trend in income growth may have been further restrained last month by the temporary delay in payments of emergency unemployment benefits, though some of this drag was offset by lump sum payment of delayed checks toward the end of the month. Regardless, a more durable rebound in consumer spending will not be forthcoming until the long-awaited recovery in the labor market materializes.

Most categories of retailers saw declines last month. The three exceptions were online retailers, bars and restaurants, and the ever-popular miscellaneous category. Clothing stores, grocery stores, and furniture stores each saw declines for the fourth straight month. Even the relatively strong electronics store segment could not manage to eke out a gain last month. Sales at building material stores continue to let out air after getting lifted earlier in the Spring by the cash-for-appliances program. While normally ignored for purposes of assessing real consumption, sales at building materials stores are now used to estimate housing improvements in the national income accounts, and this indicator suggests a setback for residential investment in the third quarter.

### CPI (Aug 13)

%m/m sa, unless noted

	May	Jun	Jul	
Total	-0.2	-0.1	<del>-0.4</del>	0.3
%oya nsa	2.0	1.1	<del>-1.4</del>	1.2
Core	0.12	0.16	<del>-0.14</del>	0.13
%oya nsa	0.9	0.9	<del>-1.0</del>	0.9
Core services	0.1	0.1		0.1
Core goods	0.1	0.2		0.2
Food	0.0	0.0	<del>-0.3</del>	-0.1
Energy	-2.9	-2.9	2.6	
Housing	0.0	-0.1		0.1
Owners' eq. rent	0.03	0.08	<del>-0.05</del>	0.06
Rent	0.01	0.07	<del>-0.05</del>	0.07
Lodging away from home	2.5	1.3	<del>-0.4</del>	0.2
Apparel	0.2	0.8	<del>-0.4</del>	0.6
New vehicles	0.1	0.1	0.1	
Used vehicles	0.6	0.9	<del>-0.0</del>	0.8
Airfares	1.9	-0.6	<del>-0.0</del>	-1.2
Communication	-0.2	-0.2	<del>-0.1</del>	0.1
Medical care	0.1	0.3	<del>-0.4</del>	-0.1

The CPI for July increased 0.3% boosted by a 2.6% increase in energy prices. In the prior three months, declining energy prices had pulled the headline CPI measure down. Excluding food and energy, the core CPI measure increased 0.13% in July. This increase continues the firming in core CPI seen over the last three months after the core measure started the year extremely soft. Even with this most recent increase, the core CPI is only up 0.9%oya and running 1.1% saar over the past six months.

The 2.6% increase in energy prices for July contrasts the average monthly decline of 2.4% seen between April and June. In July, gasoline prices increased 4.6% and energy services were up 0.8%. Fuel oil prices declined for the third straight month in July, though, dropping an additional 1.6%.

The food index has been very soft in recent months with food prices declining 0.1% in July due to declines in prices of fruits and vegetables.

Within the core measure, core goods increased 0.2% in July. This was a result of the second straight strong month for apparel prices (+0.6%) as well as increases in the prices of new vehicles (+0.1%) and used vehicles (+0.8%). The CPI for tobacco products increased 1.6% in July as several states introduced new or increased taxes on cigarettes. Core services were up a modest 0.1% in July. Shelter prices increased 0.1% for the third straight month. Transportation services held basically flat for the second consecutive month. Consumer prices for medical care services actually declined for the first time since 2005, falling 0.03% in July. This was largely a result of a 0.6% decline in the CPI for hospital services.

### Consumer sentiment(Aug 13)

Michigan preliminary

	Jun	Jul	Aug	
Univ. of Mich. Index (nsa)	76.0	67.8	<del>69.0</del>	69.6
Current conditions	85.6	76.5		78.3
Expectations	69.8	62.3		64.1
Inflation expectations				
Short term	2.8	2.7		2.8
Long term	2.8	2.9		2.7
Home buying conditions	154.0	152.0		153.0

The University of Michigan index on consumer sentiment increased from 67.8 in July to 69.6 in the preliminary August survey. Even with this slight improvement, sentiment remains low after dropping off significantly in July. The gains in sentiment were shared about equally between the measures of current conditions (+1.8 points to 78.3) and expectations (+1.8 points to 64.1).

The components of the index showed mixed results. The measures of buying conditions for houses and vehicles both edged up slightly in August. Expectations regarding personal finances decreased for the second straight month, down 4 more points in August after dropping 7 in July. Expectations on changes in unemployment similarly declined another 3 points in August after falling 7 in July. Expectations on future business conditions brightened in the August survey; expectations for the next 12 months increased from 66 to 69 and expectations for the next five years increased from 73 to 82 in August, making up most of the decline from July.

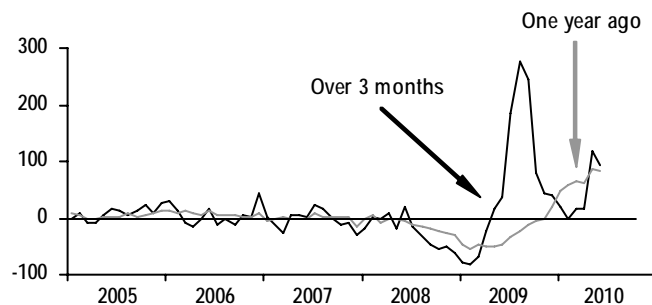
Inflation expectations for one year ahead ticked up from 2.7% to 2.8% in August. Inflation expectations looking forward five years moved down from 2.9% to 2.7%; this is on the low side of the expected levels we have seen throughout the year.

## US focus: import surge

- The US trade deficit widened to \$49.9 billion in June, which is the largest deficit since October 2008. This widening occurred even as import prices of petroleum declined significantly in May and June.
- Changes in import and export volumes had been tracking each other for some time before starting to diverge in April. Since then, import growth has remained solid while export growth appears to be moderating.
- There was a surge in imports from China in May and June as Chinese exporters rushed out goods prior to the July 15 expiration of the VAT rebate. Imports from other countries increased as well.
- Growth in auto import volumes has been very strong in recent months by historical standards, though not nearly as strong as in the middle of 2009.
- Import volumes of capital goods (ex. autos) have grown since the middle of 2009 and have been soaring lately.
- Import volumes of industrial supplies and materials have slowed in the last few months after being very strong earlier in the year.

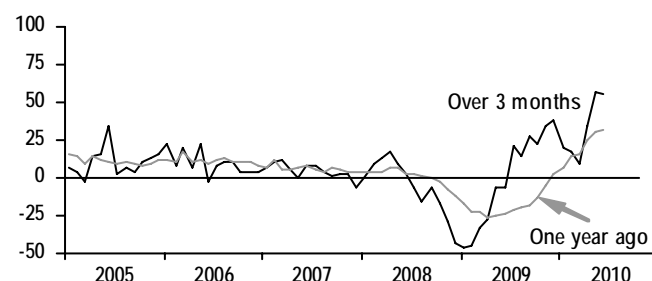
### Import volumes of autos

%ch, saar



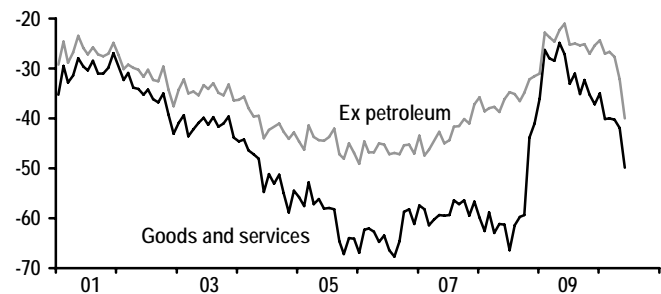
### Import volumes of capital goods excluding autos

%ch, saar



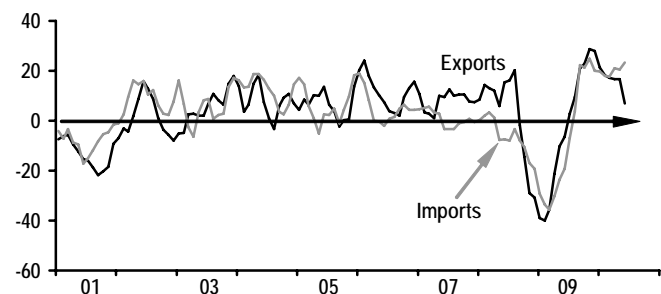
### US trade balance

\$bn, samr



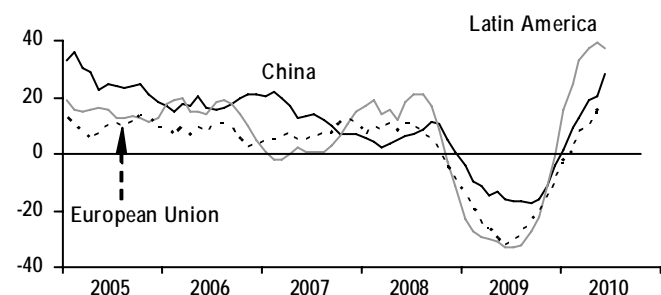
### Import and export volumes

%3m/3m, saar



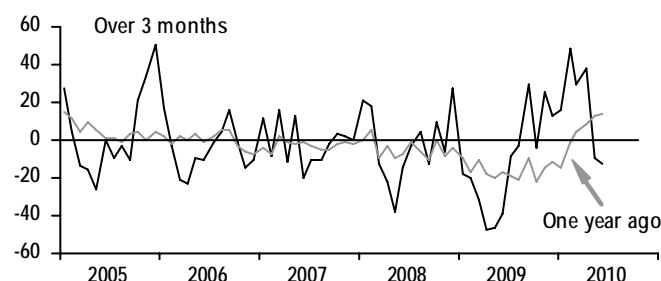
### Nominal imports by market

%ch 3m/12m, nsa



### Import volumes of industrial supplies and materials

%ch, saar



## Euro Area

- Cyclical lift finally arrives in the Euro area
- Germany led the way with a record 9%q/q saar GDP gain in 2Q10 ; rest of region also grew at firm pace
- Greek GDP declines but fiscal objective remains on track for this year

After a disappointingly sluggish start to the recovery, the Euro area finally delivered the long-awaited growth bounce, posting a 3.9% annualized GDP gain. A turbo-charged and weather-assisted German economy posted its largest-ever GDP increase of 9% annualized, which means that two thirds of the output decline seen during the recession has now been recovered. In comparison, the rest of the core countries grew at a solid, albeit less spectacular, pace. And the periphery excluding Greece held up surprisingly well, with GDP gains of close to 1% in Spain and Portugal. No second-quarter GDP data are yet available for Ireland.

It is not entirely clear what this very strong report means for growth in the current quarter and beyond. The business surveys suggest that most of the underlying growth momentum in the region carried over into early 3Q. The PMI suggests a 2.8% annualized pace of growth at the start of 3Q, which is above our forecast of a 2% gain. But, there are two big uncertainties. First is the extent to which global growth slows and the global IP cycle moderates; second is the extent to which there is payback in construction. There is currently great uncertainty about the global backdrop. Regarding construction payback, so far this appears very limited given that the huge contribution it made in Germany in 2Q reflects catch-up after a weather-affected first quarter. Overall, we are not inclined to make any changes to our current-quarter GDP estimate due to these uncertainties. But, the risks appear to be skewed to the upside.

### Greek GDP falls, but it wasn't all bad

The only Euro area country to post a decline in GDP was Greece (the Irish figure will not be available for a while). The 5.8% annual decline in 2Q means that the official government/IMF/EC adjustment program assumption of a 4% GDP contraction this year now requires GDP to fall at just over a 6% annualized pace in 2H10. The risk to this is probably skewed slightly to the downside given that the fiscal tightening has not yet been fully felt and that the bank funding stress can still lead to even tighter credit conditions later this year.

But, while real GDP is contracting, the government debt dynamics depend much more on the evolution of nominal

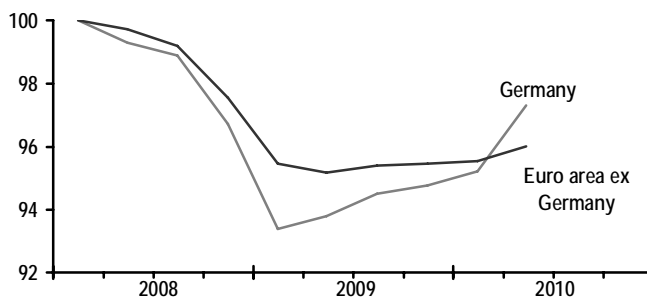
### Euro area GDP growth

%q/q saar, annualized rates are partly approximated for Spain, Austria, Belgium

	2Q09	3Q09	4Q09	1Q10	2Q10
Euro area	-0.3	1.6	0.5	0.8	3.9
Germany	1.8	3.0	1.2	1.9	9.0
France	0.6	1.1	2.3	0.7	2.5
Italy	-1.1	1.7	-0.4	1.6	1.5
Spain	-3.8	-1.1	-0.6	0.3	0.8
Netherlands	-4.7	2.3	2.4	2.0	3.6
Belgium	0.6	4.2	1.8	0.0	2.8
Austria	-3.2	2.4	1.6	0.0	3.6
Portugal	2.9	0.7	-0.5	4.3	1.1
Greece	-1.2	-1.9	-3.1	-3.9	-5.8
Ireland	-1.3	-0.8	-10.2	11.1	-

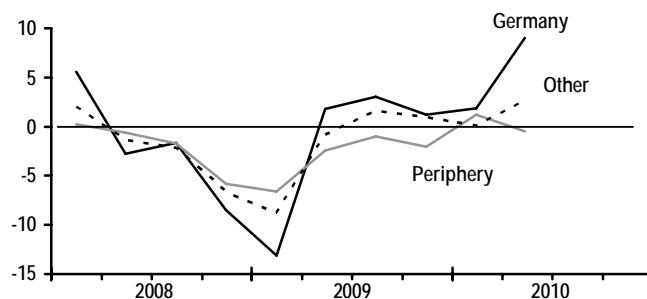
### Level of real GDP

1H08=100



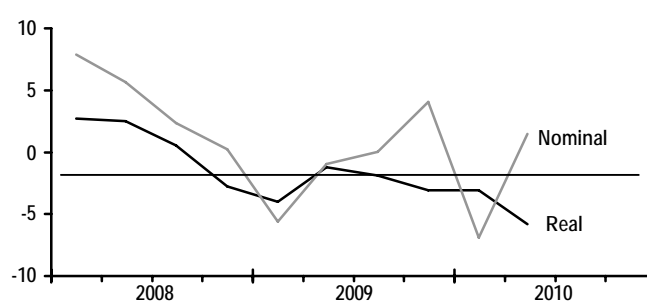
### Euro area GDP growth

%q/q saar



### Greek GDP

%q/q saar



GDP. The report delivered an upside surprise on this. Nominal GDP increased 1.5% ar in 2Q. The official adjustment program assumes a 2.8% ar decline in nominal GDP this year, and the data so far are pointing to a better outcome. The better trajectory for nominal GDP, and the monthly data on central government borrowing through July, implies that this year's fiscal objective, a deficit of 8.1% of GDP, stands a good chance of being met.

## German exports still surging ahead

Separate from the 2Q GDP report, Eurostat published June trade figures. Exports rose 5.2% m/m in June, capping a very strong second quarter, which saw a huge 28% ar gain. The recovery of German exports remains most impressive, having almost regained the pre-recession level in June and having increased by a record amount in 2Q. Therefore, despite some weather-related transport disruptions in January (severe snow) and April (volcanic ash cloud) the trend has remained firmly upward. The recovery in the rest of the region is progressing at a more moderate pace, but through the noise the trend is also pointing upward in most countries.

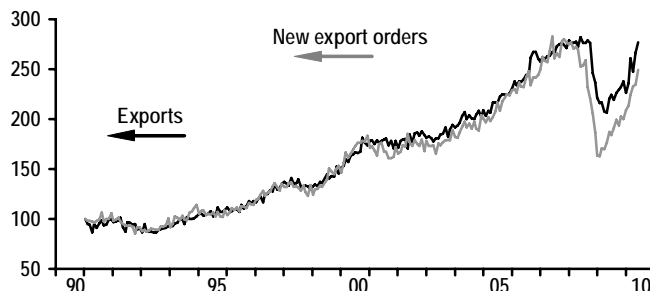
## No severe credit tightening in Spain

The steep decline in Spanish government bond yields over the past month indicates much lower financial market pressure. But, it is important to assess the damage done by the intense pressure in May and June, especially for Spanish banks. In this context, the Bank of Spain released national results from the ECB Bank Lending Survey this week. The results were not too bad. Out of a (representative) sample of 10 Spanish banks, only one tightened its lending standards for mortgages and consumer credit and three tightened their lending standards for corporate loans. Overall, the move was larger for corporates, but, in all cases, the tightening was "somewhat" rather than "considerable." And the main motivating factor was the increased funding pressure (which will have lessened now), rather than the economic outlook and concerns about the creditworthiness of firms and households. Overall, the results were encouraging about credit supply and banks also reported some increases in credit demand, at least by households.

The Spanish results left the picture in the Euro area periphery looking quite mixed. While all Portuguese banks in the sample tightened their lending criteria in the three months to June, there was no tightening in Ireland and, in Greece, it could not have been very severe, according to this survey. As one of the transmission channels of the sovereign stress to the real economy, the news on credit conditions has been good so far. But, it is far too soon to give the all clear, given that the sovereign crisis is far from over.

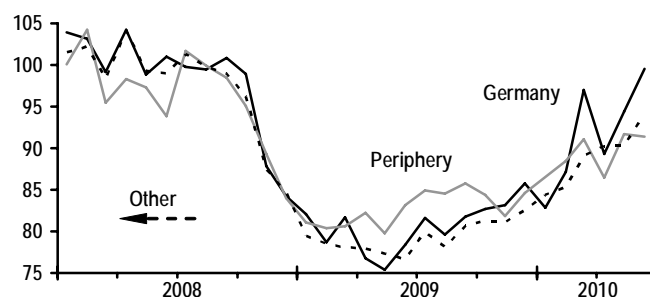
## German exports and new manufacturing export orders

Index, January 1991=100



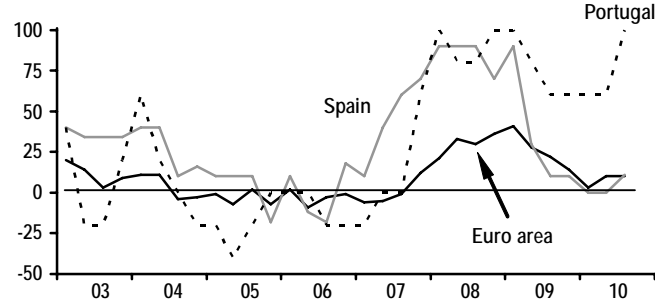
## Euro area exports

3Q08=100, "Periphery" refers to Greece, Portugal, Spain, and Ireland



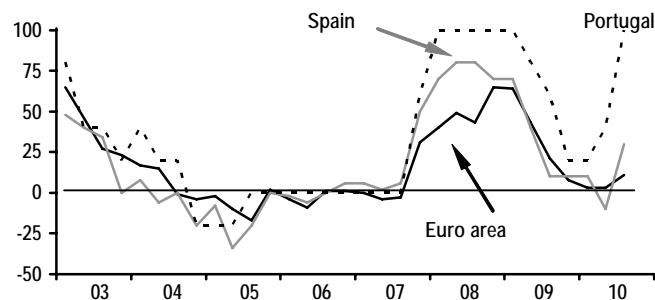
## Bank lending standards for household mortgages

Net percentage, positive indicates tightening



## Bank lending standards for nonfinancial corporate loans

Net percentage, positive indicates tightening





## Data releases and forecasts

Week of August 16 - 20

### Inflation

#### Consumer prices

		Apr	May	Jun	Jul
Mon	Euro area (final)				
Aug 16	HICP (%m/m nsa)	0.5	0.1	0.0	<u>-0.4</u>
11:00am	HICP (%oya nsa)	1.5	1.6	1.4	<u>1.7</u>
	HICP (%oya core-XX) <sup>1</sup>	0.8	0.9	0.9	<u>0.9</u>
	HICP (%oya core-XX) <sup>2</sup>	0.8	0.8	0.9	<u>0.9</u>
	HICP (%m/m ex tobacco)	0.4	0.1	0.0	<u>-0.4</u>

1. Excluding unprocessed food and energy.

2. Excluding food, alcohol, tobacco, and energy.

Euro area inflation is expected to have increased in July thanks to a rise in the yearly rate of inflation for energy and food. Indeed two thirds of the rise in headline is expected to have been caused by the fading base effect in energy inflation, as a consequence of last year's significant declines in oil prices. The rest of the increase in headline inflation is due to food prices, which have not so far declined as much as the seasonal average would have suggested. Core inflation is expected to have remained stable overall in July, with a small decline in certain core goods, such as clothing and furniture. The information available so far suggests that inflation may have increased slightly in certain sectors connected with tourism, although there was no clear pattern across the region.

#### Producer prices

		Apr	May	Jun	Jul
Thu	Germany				
Aug 19	%m/m nsa	0.8	0.3	0.6	<u>0.3</u>
8:00am	%m/m sa	0.7	0.1	0.5	—
	%oya nsa	0.6	0.9	1.7	<u>3.5</u>

## Review of past week's data

### Output and surveys

#### Real GDP

	4Q09	1Q10	2Q10	
Euro area (flash estimate)				
%q/q sa	0.1	0.2	<u>0.7</u>	1.0
%q/q saar	0.5	0.8	<u>3.0</u>	3.9
%oya	-2.1	0.6	<u>1.5</u>	1.7
Germany (flash estimate)				
%q/q sa	0.2	0.3	0.2	0.5
%q/q saar	0.7	1.2	0.6	1.9
%oya	-2.2	-2.0	1.5	2.0
France (preliminary)				
%q/q sa	0.6	0.4	0.2	0.6
%q/q saar	2.3	0.5	0.7	2.5
%oya	-0.5	1.2	1.6	1.7
GDP components (%q/q saar)				
Private consumption	3.9	0.4	0.2	—
Government consumption	2.5	2.4	0.3	—
Fixed investment	-4.3	-4.2	-3.7	—

Exports	3.0	2.9	17.7	17.8	—	11.4
Imports	11.7	11.4	0.6	7.6	—	17.8
Contributions to GDP growth (%q/q saar)						
Domestic final sales	2.1		-0.6		—	1.9
Inventories	2.8	2.7	0.8	-1.0	—	2.7
Net trade	-2.5	-2.4	2.0	2.3	—	-2.0
Spain (flash estimate)						
%q/q sa	-0.1		0.1		0.3	0.2
%q/q saar	-0.6		0.3		1.2	0.7
%oya	-3.1		-1.3		0.1	-0.2

After a disappointingly sluggish start to the recovery, the Euro area economy finally delivered the long-awaited growth bounce. The report was clearly strong and shows a broad-based improvement in 2Q. And the July business surveys suggest that most of this carried over into early 3Q. Our forecast is that Euro area GDP will grow 2%q/q saar in 3Q, while the July PMI suggests a stronger 2.8%q/q saar pace at the start of the quarter. But, there are two uncertainties: the extent to which global demand slows and the extent to which weather-assisted construction boosted 2Q GDP (for which there could be partial payback in 3Q). Overall, we remain comfortable with our GDP forecast for 3Q at this stage.

German GDP surged 9% at an annual rate (2.2%q/q). This was the largest quarterly gain ever recorded since reunification, albeit with significant assistance from the weather. German GDP is still reported to have declined 6.6% peak-to-trough during the recession, but almost two thirds of this has now been recovered. Investment (including the weather-related rebound in construction) and net trade made the main contributions, but consumer spending also rose. The final German GDP report for 2Q later this month will reveal the split between construction and the underlying improvement in the rest of the economy, which is evident from other data (incl. consumer indicators) and the business surveys.

Outside of Germany, where weather effects played much less of a role in 2Q, GDP reports were less spectacular, but still very firm. This points to some improvement in domestic demand. French GDP rose in line with our expectations—all GDP components increased, including business investment for the first time in the recovery. While Spanish GDP was a touch softer than expected, Dutch and Austrian GDP increased around 3.6%q/q saar. In most of the periphery, growth was still positive in 2Q, although the second half of the year will almost surely be harder.

#### Industrial production

	Apr	May	Jun	
Euro area				
%m/m sa	0.8	1.0	1.1	-0.2
%oya	9.6	9.5	9.7	8.3
France				
Ind production (%m/m sa)	-0.5	-0.4	1.7	1.9
%oya sa	0.1	7.8	0.2	8.5
Manuf prod (%m/m sa)	0.3	0.6	0.5	0.6
%oya sa	0.8	8.6	7.5	7.8

IP in the Euro area is up around 10% ar in 2Q as a whole, a rate of increase similar to that in the previous quarter and pointing to strong industrial output growth at midyear.

In the details, intermediate goods output fell a little (-0.6% m/m), and capital goods output growth slowed to 0.2% m/m, but these soft readings came after very large in-

creases in earlier months. Meanwhile, consumer goods output fell 0.2% m/m, confirming that the recovery across this type of goods is proving slower following a more moderate decline during the recession.

Across countries, German and French output fell by 0.5% m/m and 1.6%, respectively, following strong gains in May. Italian output continued to gain, by 0.6% m/m. Spanish output fell for the second consecutive month (-0.3% m/m), while Greek and Portuguese output fell 0.7% m/m and 0.5% respectively, following gains in May. Irish output, on the other hand, gained 1.3% m/m, building on the gain seen in the prior month. Broadly speaking, IP growth in 2Q looks to have held up well across the region, with the clear exception of Greece, which saw the second quarterly decline of around 10% ar. Irish IP also fell in 2Q (by around 12% ar), but this came after a massive surge in 1Q.

## External trade and payments

### Foreign trade

	Apr	May	Jun		
<b>Euro area</b>					
€ bn sa					
Trade balance	0.1	0.0	-3.0	-2.7	— -1.6
Trade balance—year earlier	1.3	1.0	2.2	2.1	2.1 2.0
Exports	121.6	122.1	123.6	124.3	— 130.8
%m/m sa	-3.1	2.9	1.6	1.8	— 5.2
Imports	121.4	122.1	126.5	127.0	— 132.4
%m/m sa	-3.0	-2.8	4.2	4.0	— 4.3
<b>Germany</b>					
€ bn, values, sa					
Trade balance	12.8	13.2	10.6	—	12.3
Trade balance—year earlier	9.4	9.6	10.3	10.4	11.6
Exports	74.0	74.7	80.8	80.5	— 83.6
%m/m	-6.3	-5.1	9.2	7.9	-1.0 3.8
Imports	61.2	61.5	70.3	69.9	— 71.2
%m/m	-7.2	-6.1	14.8	13.7	— 1.9

German exports surged in June, for a record 44% annualized in 2Q10, and have now recovered almost 95% of the massive peak-to-trough decline. Following the 26% collapse of the level of exports during the recession, the German trade recovery has been remarkable. German exports have been affected by two weather-related setbacks this year, which caused transport disruptions in January (severe snow) and April (volcanic ash cloud). But, through this noise, the trend has been firmly up and consistent with the still very upbeat business surveys through to July (IFO, PMI). Therefore, exports are still set for further increases, although the pace will surely slow. In terms of net trade in 2Q10, this is now tracking a slightly larger-than-expected 3% q/q saar contribution to GDP. In real terms, both exports (34% q/q saar) and imports (30% q/q saar) rose strongly in 2Q10.

## Inflation

### Consumer prices

	May	Jun	Jul	
<b>Euro area</b>				
HICP (%oya nsa)	1.6	1.4	1.7	
<b>Germany (final)</b>				
%m/m nsa	0.1	0.1	0.2	0.3
%m/m sa	-0.1	0.0	—	0.1
%oya nsa	1.2	0.9	1.1	1.2
HICP (%oya)	1.2	0.8	1.2	
<b>France</b>				
%m/m nsa	0.1	0.0	-0.4	-0.3
Index ex tobacco nsa	120.04	120.02	119.56	119.68
%oya nsa	1.6	1.5	1.6	1.7
HICP (%oya)	1.9	1.7	1.8	1.9
<b>Italy (final)</b>				
%m/m nsa	0.1	0.0	0.4	
%oya nsa	1.4	1.3	1.7	
HICP (%oya nsa)	1.6	1.5	1.8	
<b>Spain (final)</b>				
%m/m nsa	0.2	0.2	-0.5	-0.4
%oya nsa	1.8	1.5	1.9	
HICP (%oya nsa)	1.8	1.5	1.9	

The final CPI details for Germany confirmed our first impression of a relatively small decline in core inflation, from 0.7% oya in June to 0.6% oya in July. While inflation in core goods components such as clothing, furniture, and cars declined in July, service inflation components appear to have remained stable overall in the month.

Headline inflation moved up in July owing to the base effect in the energy component and more strengthening of fresh food prices. Indeed, energy prices declined 0.9% on a monthly basis, but the yearly rate moved up, thanks to the very large decline in oil prices last year. Food inflation accelerated sharply, failing to show the usual seasonal pattern of fresh food price declines.

The details on French inflation showed that the upward surprise was due to core inflation being more resilient than expected: the declines in seasonal prices in clothing and shoes were smaller than last year, pushing the inflation rate for services up slightly in July. Service inflation remained unchanged in the month. Overall core CPI inflation rose one tenth to 1.0% oya in July.

Inflation in the volatile components of food and energy was largely in line with our expectations. Energy inflation was up in yearly terms, thanks to a base effect, due to last year's significant decline in oil prices. Food prices accelerated slightly, with a monthly decline that was a bit smaller than the seasonal average.

## Japan

- **BoJ stayed on hold as expected, but both BoJ and MoF voiced concern about rapid yen appreciation**
- **Business and consumer sentiment holding up well; temporary factors appear to be providing support**
- **Machinery orders rebounded in June to some extent, but domestic demand is sluggish**

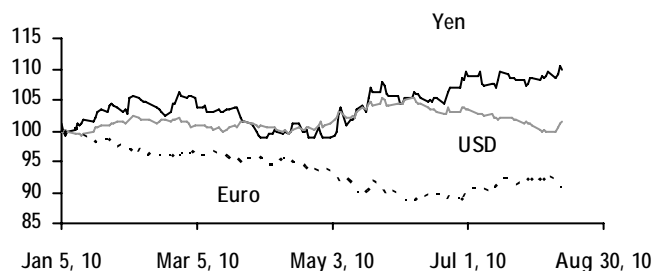
As expected, the BoJ remained on hold at its policy meeting this week. The statement was effectively a copy and paste from July, reiterating both the upside risks to the economic outlook—higher-than-expected growth in emerging economies—and the downside risk—financial market movement, including the effects of the European sovereign crisis and the financial climate. Governor Shirakawa said in his press conference that yen appreciation represents a headwind to growth in exports, profits, and sentiment, and that it needs to be monitored closely. However, he also noted that the effects of monetary easing are taking hold, with some decline in long-term interest rates and rise in profits. The BoJ believes that the economy is currently in line with its target and incorporates the cautious outlook for recovery in both the US and Europe.

The BoJ's policy stance and risk assessment differ from that of the US Fed, highlighted by the FOMC's decision to reinvest principal payments from its holdings of MBS and agency debt into Treasury securities, and a measurable downshift in the Fed's economic outlook. With slightly weaker data readings in the US and China, the perception remains that Japan's authorities are reluctant to act, prompting typical risk-averse reactions from the market: the yen hit a 15-year high against USD at 84; long-term (10-year) JGB yields slid below 1.0%, and equity prices slumped to a new low for the year on Thursday morning.

On back of the market reaction, the MoF held an emergency press conference while the BoJ posted the governor's statement voicing concerns about rapid yen appreciation on its website. The market reacted favorably to the move as the yen depreciated to a level of 86. In our view, however, the main hurdles (JPY-selling intervention and the BoJ's additional easing) still look high. With regard to intervention, our FX strategists emphasize that the G-7 countries' consistent criticism of currency manipulation and huge unrealized losses in Japan's FX reserves should preempt any aggressive market intervention by the government. As for the BoJ's approach to easing, comments from the executive director that "the BoJ's assessment of its policy stance has not changed from two days

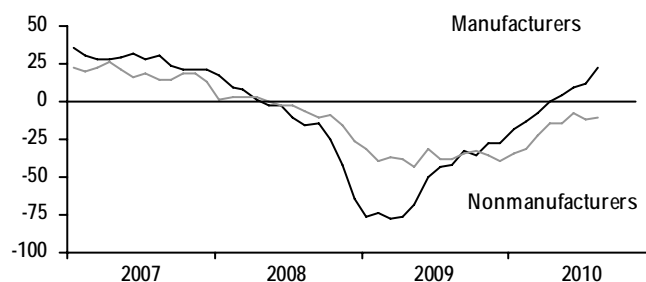
Nominal effective exchange rate

Jan 4, 2010=100



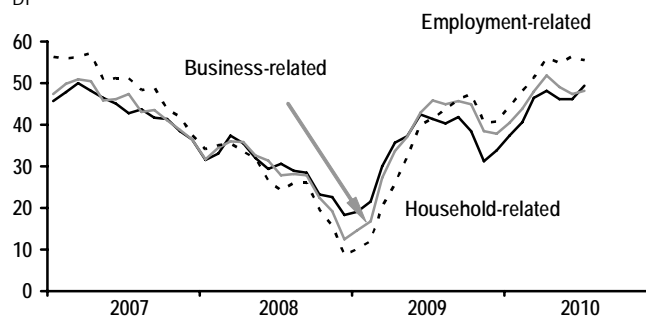
Reuters Tankan business confidence

Index



Economy Watchers survey—business sentiment

DI



ago when the monetary policy meeting was held" underscore the feeling that the Bank has no intention of acting soon. Note, too, that the DPJ's leadership election (i.e., the selection of the Prime Minister) takes place next month, and this likely makes it difficult for the government to make any radical moves before then.

## Current sentiment remains strong, but the outlook has turned cautious

The manufacturing DI in the Reuters Tankan large firms survey jumped unexpectedly in August. It recorded the largest m/m rise in 14 months (10 points) and reached its highest level since November 2007 (22) against expecta-

tions that a strong yen dampened corporate sentiment. However, such a leap likely includes temporary factors, as it probably reflected the sharp rise in the auto sector (marking 38 after 7 in July), which is now experiencing the “front-loading” of purchases of environmentally friendly cars ahead of the reduction in government support, and in the food sector (marking 44 after 25 previously), which is benefiting significantly from the recent extreme heat. Indeed, the outlook DI, which represents respondents’ prospects for the conditions three months ahead, looks for a calming down, to 15.

The headline current conditions DI in July’s Economy Watchers survey—which focuses on small businesses that are particularly sensitive to the economic cycle—recovered all of the loss of the previous two months. The result confirms the view that the decline in sentiment during the past two months of 2Q was largely the result of temporary factors such as foot-and-mouth disease and bad weather. Looking at the details, while the household and the business DIs each recovered solidly, the employment DI stayed well above neutral despite a modest fall in July. Consumer sentiment in July dipped to 43.3 from 43.5, but is still above May’s level, providing evidence that consumers are not necessarily upbeat, but are not yet feeling the downturn.

As for conditions two to three months ahead as detailed in the Economy Watchers survey, there are fears of a triple-whammy of lingering hot conditions hindering autumn sales, payback for the front-loading of green car purchases, and the negative impact of a stronger yen on Japanese exports.

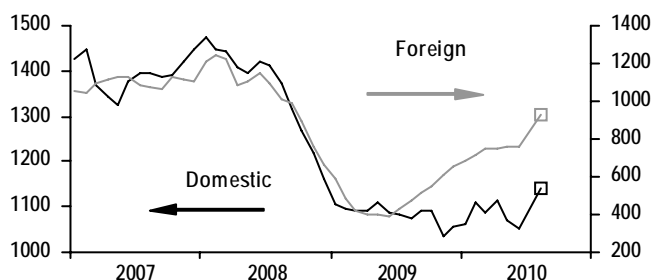
### Machinery orders picked up in June, but domestic demand remains sluggish

Core domestic machinery orders rose only 1.6% m/m sa in June, after a steep fall of 9.1% in May. In 2Q as a whole, the pace of rise in core orders slowed significantly, to 1.4% q/q saar from 12.2% in 1Q. The ESRI’s outlook suggests that the modest uptrend in core orders will be extended to this quarter, with the expectation of a further rise of 3.2%. This trajectory is slightly below our forecast, but we still think that capex is on a gradual uptrend.

Meanwhile, foreign orders have been holding up well in the latter part of 2Q, marking a 2.7% m/m sa gain and finishing 2Q at 9.9% q/q saar, even after the double-digit rise of the previous three quarters. Furthermore, the survey projections look for a reacceleration to 123.1% q/q saar in 3Q orders, suggesting that demand from Asian countries remains robust—a significant portion of this can be probably attributed to Japanese companies in the region.

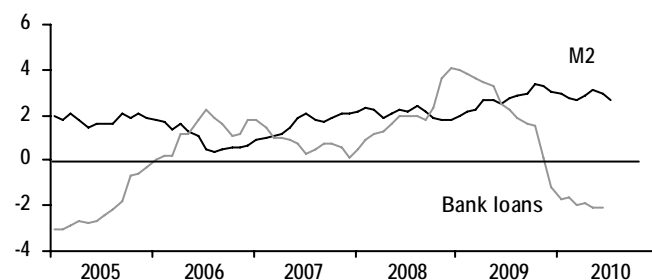
### Machinery orders

Yen bn 3mma for both scales, boxes are projection for 3Q10



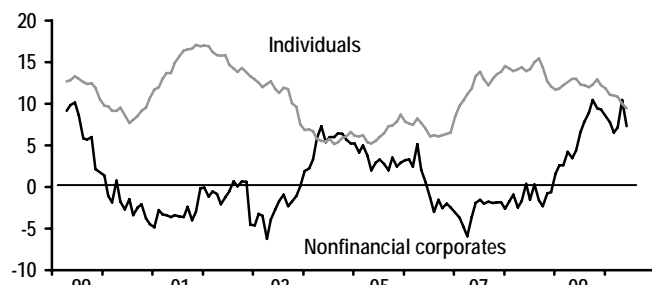
### M2 and bank loans

% oya



### Bank deposits

Yen tn, difference from a year ago, through June



### Money stock keeps rising, but loans fall

The basic contour of the flow of funds remains unchanged. M2, the broad measure of money supply, continued to rise, at almost 3% oya (2.7% in July and 2.9% in June), while bank loans maintained their downward trend, falling at close to 2.0%. A key feature of the recent flow of funds has been the rise in corporate deposits alongside the fall in bank loans. Corporate profits have recovered sharply, but firms are cautious about exercising new capital expenditure (and hiring) given the negative prospects for the economy. To be sure, they are increasing investment overseas, particularly in Asia, but confidence to spend within Japan appears thin.

## Data releases and forecasts

Week of August 16 - 20

Mon Aug 16 8:50am	<b>GDP—first estimates</b> %q/q saar	3Q09	4Q09	1Q10	2Q10
	Real GDP	0.4	4.6	5.0	<u>2.3</u>
	Private consumption	2.6	2.9	1.7	<u>0.0</u>
	Residential investment	-26.0	-10.2	1.8	<u>5.0</u>
	Business investment	-8.1	4.7	2.6	<u>8.0</u>
	Public consumption	0.3	2.7	1.7	<u>1.5</u>
	Public investment	-3.3	-3.6	-1.8	<u>-25.0</u>
	Exports	39.2	25.2	30.6	<u>30.0</u>
	Imports	24.9	4.1	9.3	<u>20.0</u>
	%-pt contribution to q/q saar GDP growth				
	Net exports	2.1	2.7	3.0	<u>2.2</u>
	Inventories	-0.3	-0.5	0.3	<u>-0.3</u>
	GDP deflator (%oya)	-0.7	-2.8	-2.8	<u>-1.7</u>

Although strength in the first two months of 2Q resulted in further robust gains in exports despite growing signs of a slowdown in the economy, the contribution from net exports was likely depressed by the sharp spike in imports. In addition, the CAO private consumption index suggests that consumption finished the quarter on a soft note, probably reflecting the temporary hit from adverse weather. Consequently, we expect real GDP growth to have slowed meaningfully from the solid pace seen in the previous two quarters.

Mon Aug 16 8:50am	<b>Index of tertiary sector activity</b> % change	Mar	Apr	May	Jun
	%m/m sa	-2.6	2.4	-0.9	<u>-0.5</u>
	%oya	1.8	1.8	1.1	<u>0.3</u>

The tertiary sector activity index is anticipated to have declined further in June. Softness in the CAO private consumption index in the month, which we expect to reverse in coming months, reflects the overall dull tone in consumer-oriented businesses. Moreover, data indicate a substantial m/m fall in the activity index of securities businesses.

Tue Aug 17 2:00pm	<b>Construction spending</b> % change	Mar	Apr	May	Jun
	Public	5.9	-17.4	-2.1	—
	%m/m sa, by J.P. Morgan	-9.6	-17.9	17.9	—
	Private	-20.2	-19.3	-12.4	—
	Residential	-17.1	-14.4	-11.3	—
	Nonresidential	-23.0	-24.2	-13.4	—
	Building and structures	-29.0	-26.2	-21.3	—
	Civil engineering	-16.0	-21.5	-2.6	—

Thu Aug 19 1:30pm	<b>Index of all sector activity</b> %m/m sa	Mar	Apr	May	Jun
	All sectors	-0.6	1.9	0.2	<u>-0.3</u>
	Tertiary sector	-2.6	2.4	-0.9	<u>-0.5</u>
	Industrial production	1.2	1.3	0.1	-1.1
	Construction	-4.0	-4.4	8.9	—
	Public sector	0.0	-0.8	0.9	—

Thu Aug 19 2:30pm	<b>Nationwide department store sales</b> %oya, unless noted	Apr	May	Jun	Jul
	Overall	-5.8	-3.9	-7.4	<u>-6.0</u>
	%m/m sa, by J.P. Morgan	-0.6	-0.1	-1.1	<u>-1.8</u>
	Same store	-3.7	-2.1	-6.0	—

Sales reports from major stores suggest that a loss of upward momentum emerged around the turn of the year and became more evident in July. The recovery in sales of luxury goods continues to stagnate, although there was some good news in positive apparel sales.

## Review of past week's data

### Money stock and bank lending (Aug 9)

%m/m sa, incl. agricultural worker households	May	Jun	Jul
M2	3.1	2.9	<u>3.0</u> 2.7
L	<u>1.8</u> 1.9	<u>1.6</u> 1.5	<u>1.6</u> 1.3
Bank lending	-2.1	-2.1	<u>-2.0</u> -1.9
Adjusted for special items	-1.9	-1.9	<u>-1.8</u> -1.7

Reports reiterate that abundant liquidity in the corporate sector has been depressing demand for bank loans, and also that a broadening gap between growth in deposit assets and lending is encouraging banks to buy JGBs.

### Balance of payments (Aug 9)

¥ bn sa, unless noted	Apr	May	Jun
Current account	1380	905	<u>1045</u> 1362
Trade balance	771	376	<u>442</u> 634
Services	-220	-115	<u>-150</u> -100
Income	953	729	<u>850</u> 918
Current transfers	-124	-85	<u>-95</u> -91
Current account (nsa)	1242	1205	<u>1155</u> 1047

Aside from monthly volatility, the three-month moving average of the surplus charted down for a third month in a row, albeit modestly. The latest fall reflects the smaller trade surplus and the continued slide in the income account surplus.

Moving forward, we expect the overall surplus to remain relatively low for some time, as the trade surplus continues to be depressed due to moderating exports (mainly the result of the slowdown in Asian economies) while the income account surplus remains soft amid low interest rates in global markets.



## Economy Watchers survey (Aug 9)

DI

	May	Jun	Jul
Current conditions	47.7	47.5	<del>48.0</del> 49.8
Households	46.2	46.2	<del>46.2</del> 49.4
Business	49.1	47.3	<del>48.2</del>
Employment	54.8	56.3	<del>55.5</del>

See main essay.

## Machinery orders (Aug 11)

%m/m sa

	Apr	May	Jun
Domestic private sector, ex for ships and from utilities	4.0	-9.1	<del>4.0</del> 1.6
Manufacturing	-5.5	-13.5	<del>9.9</del>
Core nonmanufacturing	5.3	-6.0	<del>-3.9</del>
Foreign	-3.7	2.7	<del>2.4</del>

In June, orders in the manufacturing sector recovered part of the decline of the previous two months, with chemicals (coming off a 70.8% m/m jump after four consecutive monthly falls through May) being the major contributor. In addition, 3m/3m sequential rises in orders from industrial machinery and from auto/auto parts producers continued, but at a more moderate pace.

Meanwhile, orders from the nonmanufacturing sector fell for the second month in a row. However, the ex. mobile phone measure rebounded sharply, at 6.7% m/m sa after a sizable 17.2% loss the previous month, suggesting that June's weakness does not necessarily reflect broader weakness in capital investment (most mobile phones are likely for consumer use).

## Corporate goods prices index (Aug 11)

%oya

	May	Jun	Jul
Domestic CGPI	<del>0.5</del> 0.4	<del>0.5</del> 0.4	<del>0.1</del> -0.1
Export prices	-1.4	-3.6	<del>-4.2</del>
Import prices	<del>14.0</del> 14.4	<del>8.0</del> 8.6	<del>4.4</del>

The oya change in the CGPI moved into negative territory, after posting rises in May and June. The key driver of weakness in July came from energy, where price rises had been behind the uptrend seen in previous months. That said, the slowdown in the fall in the CGPI ex. energy and electric/gas utilities appears to be stalling (on our rough calculation, it dipped 0.8% oya in July vs. -0.8% in June, -0.9% in the 2Q average, and -2.1% in the 1Q average).

By end use, while the consumer durables CGPI fell m/m for the tenth straight month, the capital goods CGPI remained at the same level as in the previous three months. The continuing large divergence between the two reiterates that firms' pricing power related to consumer goods has been especially constrained. Indeed, this also supports our view that CPI deflation is moderating only gradually.

## Industrial production—final (Aug 12)

%m/m sa

	Apr	May	Jun
Production	1.3	0.1	<del>-1.5</del> -1.1
Shipments	1.4	-1.7	<del>-0.2</del> 0.2
Inventories	0.6	2.0	<del>0.7</del>
Inventory/shipments ratio	1.2	4.8	<del>-1.4</del> -1.7
Operating ratio	0.0	0.8	<del>-2.1</del>
Production capacity (%oya)	1.8	1.9	<del>3.1</del>

## Consumer sentiment (Aug 12)

Diffusion index, nsa

	May	Jun	Jul
Consumer sentiment	42.8	43.5	<del>44.0</del> 43.3
Standard of living	43.0	43.6	<del>43.2</del>
Income growth	41.1	41.6	<del>41.5</del>
Labor market conditions	40.1	41.4	<del>41.8</del>
Durable goods purchases <sup>1</sup>	46.9	47.2	<del>46.7</del>

1. The DI asks whether a respondent thinks that now is a good time to purchase durable goods.

The consumer sentiment index for July fell m/m after consecutive rises since the start of this year. That said, the July level of the index, 43.3, was only 0.2-pt lower than the cyclical high marked in June. The result suggests that consumer sentiment remains relatively buoyant despite the recent financial market turmoil and the exclusion of several items from the "eco-point" system.

Based on movements in the CAO private consumption index, we expect flat q/q growth in GDP consumption in the past quarter. However, the household DI in the Economy Watchers survey climbed in July, with respondents citing strong sales of household appliances and beverages amid the extreme heat and "front-loading" of purchases of eco-friendly cars ahead of the reduction of government support scheduled for end-September. This report provided further proof that 3Q consumption will likely revert to solid growth, as demonstrated by the temporary boost in the Economy Watchers survey.

## Reuters Tankan survey (Aug 13)

DI, % saying "good" minus "bad"

	Jun	Jul	Aug
Manufacturing	9	12	<del>22</del>
Nonmanufacturing	-8	-12	<del>-10</del>

The August jump in the manufacturing DI was driven by the auto sector (marking 38 after 7 in July), which is now experiencing "front-loading" of purchases of environmentally friendly cars ahead of the reduction of government support, and the food sector (marking 44 after 25), which is benefiting from the recent extreme heat. Indeed, the outlook DI for three months ahead expects the reading to cool to 15. The nonmanufacturing DI recovered part of the fall of the previous month, and is predicted to continue improving modestly within a sector indicating "bad" conditions.

Overall, the report repeated the message from earlier survey reports that the Japanese economy has been holding up despite slowing external demand and the recent yen appreciation. However, the increasingly uncertain global economy could weigh on the confidence of Japanese companies.

## Canada

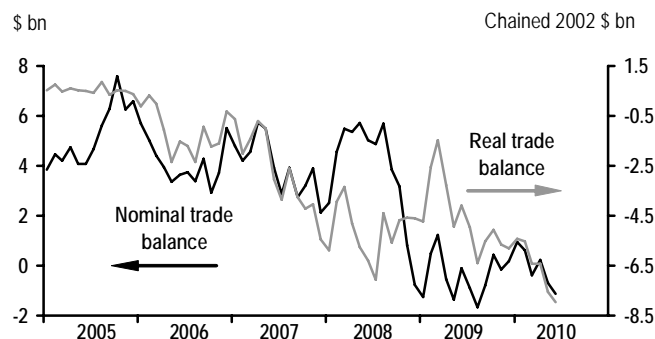
- **Trade deficit widens to 1.1 billion in June, pointing to a significant drag from net exports on 2Q GDP**
- **Housing continues to disappoint**
- **Upcoming data will help us refine our forecast for 2Q GDP, currently at 2.6%q/q saar**

The economy continued to show signs of slowing this week, but with some bright spots. Both the nominal and the real trade deficits widened in June, and that points to a significant drag on 2Q GDP from net exports. July housing starts declined for the third month in a row. For the first month of 3Q, starts were down 23% ar from the 2Q average, after quarterly increases of 21% ar in 2Q and 37% ar in 1Q. July single-family construction is off almost 30% from its recovery peak, and July existing home sales (to be released early next week) are not expected to recover much from their June collapse. The strong improvement in sales at the beginning of the recovery and through the early part of this year is being reflected in strengthening home prices. The New Housing Price index has been climbing steadily since late last year and was up almost 3% oya in 2Q. New vehicle sales were up 2.5% in June, with higher truck sales the main contributor to the increase.

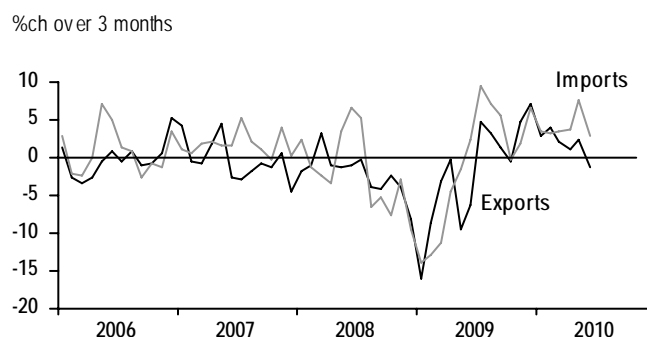
The Canadian nominal trade deficit widened to C\$1.1 billion in June from a downwardly revised -C\$695 million in May (originally reported as a C\$503 million deficit). Both merchandise exports and imports were down. Nominal exports fell 2.5% m/m and nominal imports fell 1.2% m/m. The export sectors were mixed, but two thirds of the decline was accounted for by a 7.1% decrease in industrial goods and materials. Energy (-5.5%) and automotive (-4.6%) products were also large contributors to the decrease (but the fall in auto product exports followed a 21.9% surge in May). Real exports (chain weighted) were down 2.1% m/m. Moderate gains in the imported durables categories could not offset the 19.3% decrease in energy products. Imports excluding energy grew 0.9%. Real imports (chain weighted) were down 0.6% m/m.

With real imports falling less than real exports, the real trade deficit deteriorated further in June —to C\$8.0 billion from a downwardly revised C\$7.6 billion in May. The real deficit has now widened for five of the last six months. A growing trade gap could have a negative effect on economic growth in 2H10. However, a positive for business investment has been the uninterrupted increase in imports of machinery and equipment since February (Canadian businesses import more than 70% of their machinery and

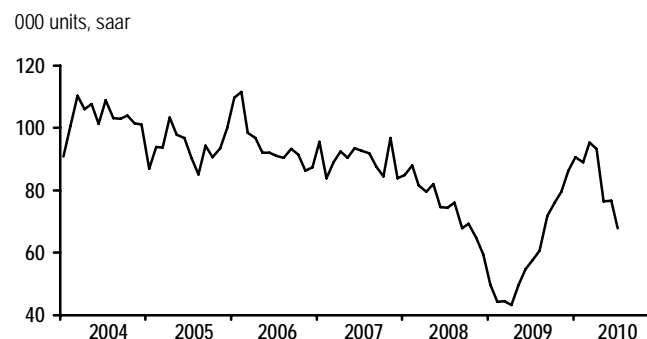
Merchandise trade balance



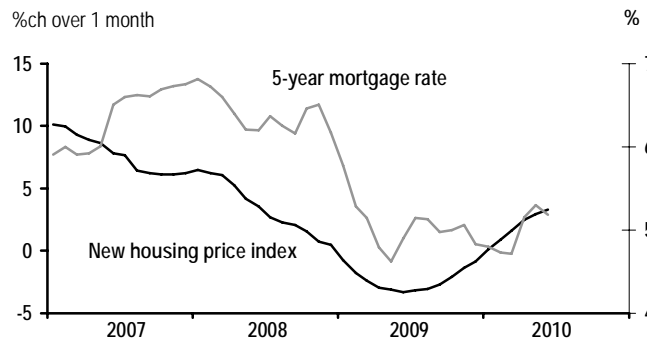
Real merchandise trade



Single-family housing starts



Home prices and mortgage rate



equipment purchases). This points to strong performance for capex in 2Q to offset some the drag from net exports.

The slowdown in the pace of housing construction has been dramatic in recent months. Starts were down 1.6% in July and are now down 8% from their April post-recession peak. An 11% decrease in single-family starts and a plunge in the small rural category in July was only partially offset by a 13% increase in the volatile multi-family category. Residential investment looks to be a much smaller boost to overall GDP growth in 2H10 after accounting for a large positive contribution over the last three quarters. New home prices were up again in June, increasing 0.1%/m. However mortgage rates have been edging up since April. Rising prices and mortgage rates are no doubt tempering demand for new housing. The expected moderation in 2H10 should be seen as a natural cooling off in sector that became red hot immediately after the start of the recovery in an environment of near-record-low interest rates.

New vehicle sales were up 2.5% in June led by a 3.2% increase in sales of trucks. Truck sales have surpassed passenger car sales for each of the past seven months, the longest period in the history of the series dating back to 1946. Although demand there is likely to slow, it points to another plus for business investment in 2Q.

### Data releases and forecasts

#### Tue Aug 17 8:30am Manufacturing report

%m/m sa, unless noted

	Mar	Apr	May	Jun
Sales	1.4	0.4	0.4	<u>0.1</u>
New orders	-1.1	0.6	2.5	<u>-1.3</u>
Unfilled orders	-0.5	-0.4	1.3	<u>0.1</u>
Inventories	-0.9	0.1	-0.7	<u>-0.5</u>
Inventory-shipments ratio	1.32	1.32	1.30	<u>1.30</u>

Manufacturing sales are likely to moderate in June on the back of lower durable goods production. The volatile aircraft category is expected to be down sharply after two months of marked increase. An increase in non-durables should provide the offset as petroleum and coal sales are expected to be up.

#### Thu Aug 19 8:30am Wholesale sales

Sa

	Mar	Apr	May	Jun
Total,%m/m	1.1	-0.2	-0.1	<u>0.2</u>
%oya	9.8	9.9	9.5	<u>8.3</u>

Wholesale sales probably rebounded in June, but should maintain growth along the lines of the recent moderate growth in manufacturing.

#### Thu Aug 19 8:30am Leading indicators

%m/m

	Apr	May	Jun	Jul
Smoothed	1.1	1.1	1.0	
Unsmoothed	2.5	0.7	-0.6	

#### Fri Aug 20 7:00am Consumer price index

%m/m nsa, unless noted

	Apr	May	Jun	Jul
Total CPI	0.3	0.3	-0.1	<u>0.1</u>
%oya	1.8	1.4	1.0	<u>1.4</u>
CPI BOC core	0.3	0.3	-0.1	<u>0.1</u>
%oya	1.9	1.8	1.7	<u>1.8</u>
Ex food & energy	0.4	0.3	-0.1	<u>0.1</u>
%oya	1.2	1.0	0.9	<u>1.2</u>
Ex food, energy, tax (%oya)	1.2	1.1	1.0	

We expect a 0.1%/m increase in the headline CPI and the core in July. The energy category is expected to be down due to a historical trend for natural gas prices to be down sharply in July. The other categories should remain tame except for clothing and footwear, which is set for a rebound after two months of sharp decreases.

### Review of past week's data

#### Housing starts (Aug 10)

	May	Jun	Jul
Total (000)	195.3	197.9	189.3
%m/m	-5.1	-3.8	-3.1
%oya	-53.1	55.1	-32.0

#### New house prices (Aug 10)

Nsa

	Apr	May	Jun
Total,%m/m	0.3	0.3	<u>0.2</u>
%oya	2.5	2.9	3.3

#### International trade (Aug 11)

Sa

	Apr	May	Jun
Balance (C\$ bn)	-0.33	0.22	-0.50
Exports (%m/m)	-1.3	-0.6	-5.2
Imports (%m/m)	-1.4	-2.5	-5.7
Balance (Chn. 2002 C\$ bn)	-6.98	-6.43	-7.42

#### New motor vehicle sales (Aug 13)

Sa

	Apr	May	Jun
Total (mn units, ar)	1.514	1.521	1.518
%m/m	-4.1	-3.9	0.2
%oya	-5.1	5.6	-4.3

## Mexico

- **Inflation reached an inflection point**
- **Domestic demand starts to pick up**
- **GDP to post the strongest growth of 2010**
- **Banxico to reiterate that there will be no rate cuts**

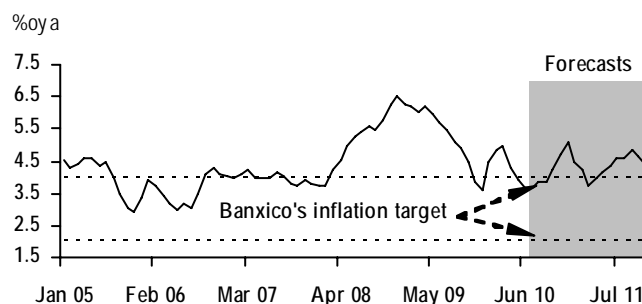
Banco de México released the inflation figure for the month of July this week; 12-month inflation came in at 3.6%, the same level observed in June. Annual inflation has been falling sharply over the last four months after reaching 4.97% in March (on the back of the new taxes implemented early in the year). Even though inflation has surprised to the downside, we believe it is highly likely that consumer price growth will trend upward in 2H10 (first chart). We base this forecast on four main points: (1) the removal of the electricity tariff discounts; (2) the agricultural price reversal, particularly in tomatoes; (3) the higher wheat, corn, and rice prices that could boost prices of bread, cereal, and tortillas; and (4) the price increases that we usually observe during the winter holiday season, which we expect to be higher as the economy is at a recovery stage of the business cycle.

### Investment and sales signal that the rebound in domestic demand has begun

We believe that domestic demand has now started to gain momentum. INEGI released the gross fixed investment (GFI) report for the month of May, which came in at 6.2%oya, far above market expectations for a rise of 3.8%, but closer to our own forecast of 5.9%. GFI has grown 11.2%oya year-to-date, mainly led by acquisition of imported machinery and equipment, while investment declined 13.7%oya during the same period in 2009. Construction appears to be the only sector that has not yet caught up with the global rebound, having increased by a mere 0.9%oya during the first five months of the year. However, we highlight that this is the third positive yearly growth rate in a row—using revised figures—after 14 negative prints in the past 16 months (second chart).

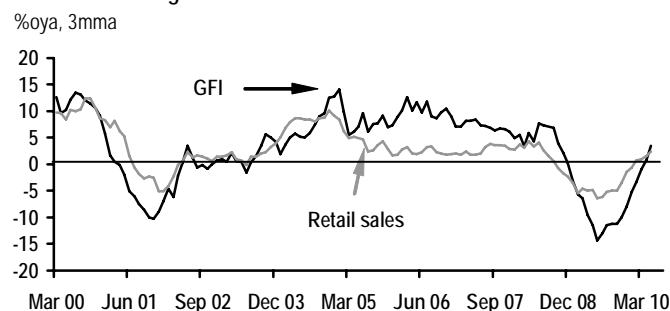
Supermarket sales—published by ANTAD during the week—also support our view, rising by 1.1% in July with respect to July 2009 (in real terms). This is the timeliest piece of data we have about consumer demand, and—along the same lines as GFI's behavior—it is showing that domestic demand has now started to gain momentum. We believe that it will continue trending upward in 2H10 as several investment projects, particularly in the auto industry, continue to provide a more promising GFI scenario for

CPI headline inflation and forecasts



Source: J.P. Morgan and Banco de México

Retail sales and gross fixed investment



Source: INEGI

### GDP

%oya	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10
GDP	-7.9	-10.0	-6.1	-2.3	4.3	7.5
Agriculture	0.1	3.4	1.3	2.1	-1.5	6.4
Industrial	-9.6	-11.1	-6.3	-1.9	5.4	7.8
Manufacturing	-13.5	-16.1	-9.4	-1.4	9.9	13.4
Nonmanufacturing	-4.3	-4.2	-2.1	-2.7	-0.1	1.0
Services	-7.3	-10.2	-6.2	-2.9	3.8	7.6

Source: INEGI and J.P. Morgan

2010, and the significant improvement in employment conditions is now helping to boost private consumption.

### GDP probably grew 7.5%oya in 2Q10

Next week INEGI will release Mexico's GDP for the second quarter of 2010 (Friday). In our view, the country's GDP posted a year-over-year growth rate of 7.5%, the strongest growth rate of the year (14%q/q saar). We believe this number will strongly benefit from the positive base effects from last year's large decline of 10%. However, the Mexican economy has experienced an important structural change in its manufacturing sector, particularly in the auto industry: Automakers around the world have reallocated part of their production to Mexico, mainly due to the real depreciation of the peso vis-à-vis the US dollar and other currencies, as well as the country's strategic geographic location and still relatively high transport costs. In fact, we

already know that industrial production—which accounts for about 30% of the country's GDP—rose by 7.8%oya in 2Q10. Furthermore, we forecast the services sector grew 7.6%, also boosted by considerable positive base effects engendered by last year's activity freeze decreed by the government in response to the influenza A (H1N1) outbreak. Last, but not least, we expect agricultural production to have advanced by 6.4% in 2Q (table). All in all, we remain confident with our 4.5% GDP growth forecast for 2010. In this context, even though growth in manufacturing production is now losing momentum, domestic demand is starting to pick up, following our three-phase recovery scenario in which we first saw an important rebound in manufacturing activity, which boosted job creation, and, about two quarters later, is starting to have positive effects on domestic demand.

## Banxico on hold

Also next week, Banco de México will hold its monetary policy meeting on Friday, in which market consensus expects the central bank to keep the reference rate on hold at 4.5%, shifting the market's focus to the post-meeting communiqué. In our view, board members might be more cautious with respect to: (1) the inflation outlook ahead, particularly given the large price increases that we have observed in wheat, corn, and rice, and (2) the speed at which the output gap will probably close—it could be sooner than expected. Nevertheless, we believe any mention of these two issues will be directed toward explaining why there is a very low possibility of a rate cut. All in all, we believe that the final message will be a confirmation that the monetary authority will remain on hold for a long period of time as medium-term inflation expectations remain well-anchored.

## Data releases and forecasts

### Week of August 16 - 20

Tue Aug 17 9:00am	<b>Central bank foreign reserves</b>				
	US\$ bn	Jul 23	Jul 30	Aug 6	Aug 13
	Gross international reserves	103.4	104.9	105.6	—
Thu Aug 19 2:30pm	<b>Banamex CPI inflation expectations survey</b>				
	%oya, except policy rate: %p.a., median value	Jul 6	Jul 20	Aug 5	Aug 19
	End-2010	4.66	4.70	4.60	—
	Core	4.16	4.10	4.06	—
	End-2011	3.83	3.83	3.83	—
	One year forward	4.30	4.14	4.34	—
	Banxico policy rate				
	End-2010	4.50	4.50	4.50	—
	End-2011	5.50	5.50	5.50	—

Fri Aug 20 9:00am	<b>Indicator of overall economic activity (IGAE)</b>				
		Mar	Apr	May	Jun
	%oya	7.0	7.4	8.8	<u>7.4</u>
	%m/m sa	1.2	1.0	0.2	<u>0.1</u>

Fri Aug 20 9:00am	<b>Real GDP</b>				
	%oya, unless noted				
		3Q09	4Q09	1Q10	2Q10
	Total	-6.1	-2.3	4.3	<u>7.5</u>
	%q/q saar	10.1	7.9	-1.4	<u>14.0</u>
	Agriculture	1.3	2.1	-1.5	<u>6.4</u>
	Industry	-6.3	-1.9	5.4	<u>7.8</u>
	Services	-6.2	-2.9	3.8	<u>7.6</u>

## Review of past week's data

### Consumer prices (Aug 9)

	Jun 2H	Jul 1H	Jul 2H	
%2w/2w	0.03	0.15	<u>0.19</u>	0.11
Core	0.14	0.13	<u>0.07</u>	-0.02
%oya	3.67	3.61	<u>3.74</u>	3.66
Core	3.95	3.87	<u>3.81</u>	3.72
	May	Jun	Jul	
All items (%m/m nsa)	-0.63	-0.03	<u>0.26</u>	0.22
%oya	3.92	3.69	<u>3.68</u>	3.64
Core (%m/m nsa)	0.24	0.13	<u>0.24</u>	0.20
%oya	4.10	3.94	<u>3.84</u>	3.79

### Fixed investment (Aug 10)

%oya nsa				
	Mar	Apr	May	
Total	3.2	0.5	<u>5.9</u>	6.2
Machinery and equipment	1.7	2.0	<u>4.4</u>	13.9
Construction	4.0	-0.3	<u>2.5</u>	2.6

### Nominal wage settlements (Aug 10)

% per annum, one year ahead				
	May	Jun	Jul	
Nominal increase	4.8	4.6	<u>4.7</u>	4.8
Real terms <sup>1</sup>	0.9	0.9	—	1.1

1. Using 12-month average CPI inflation.

### Automobile production and sales (Aug 10)

%oya				
	May	Jun	Jul	
Production	65.3	102.0	<u>51.5</u>	65.4
Export	73.9	109.1	<u>51.2</u>	57.9
Domestic sales	15.3	7.0	<u>8.1</u>	9.8

### Industrial production (Aug 11)

	Apr	May	Jun	
%oya nsa	6.4	8.4	<u>9.5</u>	8.4
Manufacturing	11.4	14.2	<u>15.8</u>	15.2
%m/m sa	0.1	0.5	<u>0.3</u>	-0.4
Manufacturing	-0.5	1.5	<u>0.2</u>	-0.1

### ANTAD same-store sales (Aug 12)

%oya, real terms				
	May	Jun	Jul	
Total	2.2	0.6	<u>2.1</u>	1.1



## Brazil

- **June retail sales confirm 2Q10 final demand was in much better shape than IP**
- **Even so, a significant slowdown was recorded in 2Q10**
- **But momentum and fundamentals favor a 3Q10 recovery**

While recognizing that 2Q10 supply-side indicators were softer than we thought initially, we have been calling this weakness temporary due to the strength of domestic demand. This week's June retail sales report confirmed this assumption, printing at an above-consensus 1.0% m/m sa, following May's 1% expansion. Although this sequential expansion did not counterbalance the huge plunge in April (exacerbated by a faulty seasonal adjustment—see below), and the 2Q10 collapse in the retail sales growth rate, the upward trajectory in the final weeks of last quarter signals a significant recovery is in the making for 3Q10.

Against this backdrop of retail sales expanding sequentially through 2Q10, and IP falling, the BCB released its proxy for the monthly GDP (the so-called IBC-Br), showing a flat path for the past quarter (first chart). According to the BCB proxy, Brazil's GDP slowed to 5.4% q/q saar in 2Q10, from 10.1% in 1Q10, which is a more moderate reading than our own forecast of a deceleration to 2.6% from the official 1Q10 print of 11.4%. However, the initial sectoral indicators for the beginning of this quarter show that after a stagnant 2Q, the economy will return to more robust growth rates through the second half of the year, fueled by real income, credit conditions, and high consumer and business confidence.

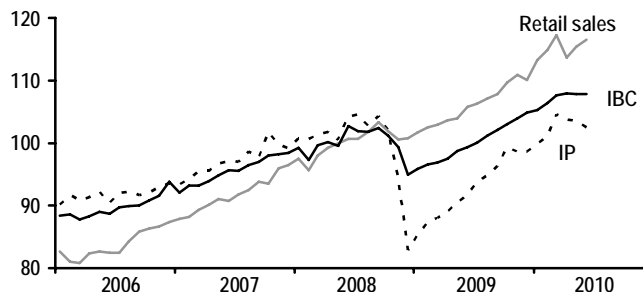
### 2Q10 retail sales slowed, but June surprised on the upside

The narrow retail sales volume index (which excludes vehicle and building materials) increased 1.0% m/m sa (11.3% oya), above consensus and J.P. Morgan forecasts of 0.5%, following May's 1.5% expansion. The breakdown by sector (see table) showed that most subgroups posted sequential expansion in June. The broad retail sales figure (which includes vehicles and building materials) remained flat in May, hurt by still-poor vehicle sales and a slide in building materials sales.

Despite the better reading in June, the narrow retail sales index slowed sharply in 2Q as a whole, although we still believe this was exacerbated by seasonal factors. Allowing for the June reading, 2Q retail sales (narrow index) revealed no growth at all after the 19% q/q saar jump in 1Q10

### Economic activity indicators: IBC-Br, retail sales and IP

Index 2008=100, sa

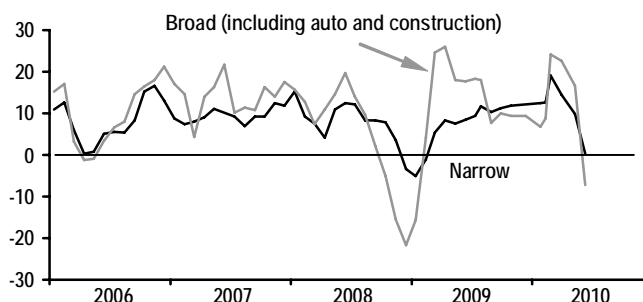


### Retail sales volume: breakdown by sectors

	%m/m, sa		%oya, nsa	
	May 10	Jun 10	May 10	Jun 10
<b>Narrow retail</b>	<b>1.5</b>	<b>1.0</b>	<b>10.2</b>	<b>11.3</b>
1. Fuel	1.7	-1.2	6.0	5.6
2. Food, beverages, and supermkts	1.1	1.5	8.2	11.9
3. Apparel	-3.8	1.0	11.9	4.3
4. Furniture and home appliances	-0.3	0.6	19.6	17.0
5. Pharmaceuticals	0.8	-0.9	12.1	10.3
6. Computers, office supplies	0.7	5.4	28.9	23.2
7. Stationers, books	1.7	-2.3	9.7	4.7
8. Others	-1.8	5.2	2.9	9.4
<b>Broad retail (1 to 10)</b>	<b>-0.1</b>	<b>0.0</b>	<b>9.6</b>	<b>3.4</b>
9. Vehicles, parts	0.0	-0.6	6.7	-9.5
10. Construction material	2.4	-3.1	20.2	12.2

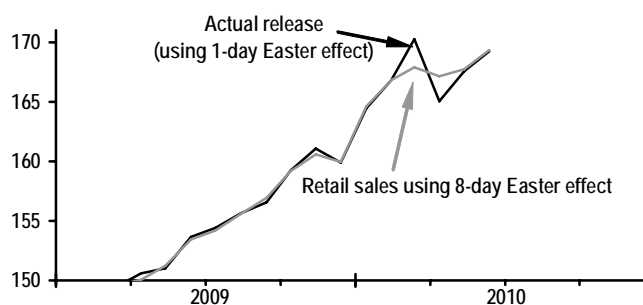
### Retail sales: sharp 2Q10 slowdown, despite good June performance

% 3m/3m saar



### Seasonal parameters exaggerated the volatility in retail sales

index; sa



(second chart). The spike in March, followed by the drop in April's retail sales, created a large negative carryover effect for 2Q sales.

We have been highlighting that the March and April figures were distorted by difficulties in the seasonal adjustment for the Easter holiday. In fact, Easter took place at the very beginning of April this year (April 4), and the IBGE (Brazilian statistical institute) registers the holiday's impact on the economy, both the narrow and broad indices, as starting one day before the break. Simply by rerunning the seasonal adjustment including an eight-day Easter effect (i.e., the impact beginning eight days prior to the holiday) instead of a one-day Easter effect, the change in the seasonally adjusted series is quite substantial (third chart, previous page), with a much softer March expansion and a relatively flat April performance. With only this change, seasonally adjusted 2Q10 growth would be 4%q/q saar instead of zero—reinforcing our view that 2Q was stronger than it appeared in the official data. Of course, even excluding this distortion, growth in 2Q slowed. Our assessment is that this was largely the result of the end of some fiscal incentives (which boosted durable goods sales in 1Q and caused a payback in 2Q); interruptions related to the Brazil football matches in the World Cup likely weighed against the performance of some sectors in June, also damaging 2Q10 results (probably more than offsetting the boost the event provided to sales of televisions).

## Fundamentals remain supportive, and should boost sales once again in 2H10

We have highlighted that credit expansion accelerated in 2Q when compared to the 1Q performance. Additionally, consumer confidence is already well above the previous peaks reached in 1H08, and improved further still in 2Q10 (compared to 1Q10). Finally, the unemployment rate remains at historical lows and the expansion of real labor income maintained the strong pace registered in 1Q, growing 8%q/q saar. Therefore, the sharp 2Q10 retail sales slowdown was at odds with the performance of its key drivers (credit, income, and confidence), and we anticipate 3Q figures showing a recovery; note that the May and June readings already left a sizable positive carryover (4.7%q/q saar) for 3Q10 narrow retail sales. Additionally, the July performance of auto sales was quite positive (close to 10%), suggesting that the outlook for broad retail sales is also much more favorable.

## Data releases and forecasts

Week of August 16 - 20

Tue Aug 17 6:00am	General prices (IGP-10) %/m m nsa			
	May	Jun	Jul	Aug
Overall	1.1	1.3	0.1	<u>0.6</u>
%oya	4.0	5.4	5.8	<u>7.1</u>
Wholesale prices	1.3	1.7	0.0	<u>1.0</u>
Consumer prices	0.6	0.0	-0.2	<u>-0.3</u>
Construction prices	0.8	2.0	0.7	<u>0.3</u>

Fri Aug 20 7:00am	Consumer prices (IPCA-15) %/m m nsa, % weights in parentheses			
	May	Jun	Jul	Aug
Total (100)	0.6	0.2	-0.1	<u>0.06</u>
%oya	5.3	5.0	4.7	<u>4.56</u>
%ytd	3.2	3.4	3.3	<u>3.32</u>
Ex volatile	0.6	0.5	0.2	<u>0.3</u>
Trimmed mean	0.6	0.5	0.3	<u>0.3</u>
By major component				
Food (20.5)	1.0	-0.4	-0.8	<u>-0.8</u>
Transport (20.7)	0.3	-0.1	-0.4	<u>0.1</u>
Housing (13.6)	0.7	0.6	0.5	<u>0.4</u>

## Formal job creation (CAGED)

Aug 16 - 20	Apr	May	Jun	Jul
Monthly creation (000)	305.0	298.0	212.9	<u>na</u>
12-month sum	1908.9	2075.4	2168.9	<u>na</u>

## Review of past week's data

Retail sales	Apr	May	Jun
%m/m sa	-3.1	1.4	<del>0.5</del> 1.0
%oya nsa	9.2	10.2	<del>10.3</del> 11.3

## Argentina

- **Kirchner's positive image continues to strengthen**
- **2011 presidential elections remain a wide-open contest**
- **Opposition getting bills only halfway through Congress**

In July the image of the Kirchner administration continued to strengthen in lockstep with the economic recovery. According to the latest public opinion poll by Poliarquia, the percentage of respondents with a positive image of President Cristina Kirchner rose to 37% in July from 33% in June (first chart). This is a big recovery from the trough of 21% at the end of last year and lifts the Kirchners' hope of remaining in power after the October 2011 election. The improvement in Nestor Kirchner's image lags that of his wife but has also risen significantly, to 34% (from the low 20s).

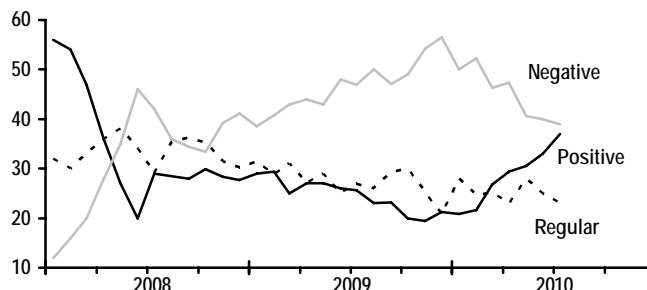
President Kirchner is reaping a significant political dividend from the economic recovery (forecast at 8.5%) and a broadening of social transfer programs. If Poliarquia is right, these factors are prevailing in the public opinion over negative developments like continued high inflation (second chart), less improvement in labor market conditions than the business cycle would normally dictate (third chart), and a multitude of corruption accusations against the government.

Conventional wisdom states that after the Kirchners' two terms in office, a fragmented but growing majority of anti-Kirchner voters will likely deny them a re-election bid if the vote goes to a second round (required when the candidate with the most votes does not achieve 40% with a 10%-point lead over the runner-up). That view was supported by the Kirchners' defeat in the key Buenos Aires district in the 2009 legislative election and the couple's highly negative image. Yet today's trend in the president's image suggests that elections—while still a long way away—might be a closer call than expected.

Potential opposition candidates (see table) have not helped to reduce electoral uncertainty. The Coalicion Civica suffers internal squabbles, legal challenges constrain leaders of the PRO party, and dissident Peronist leaders suffer a highly negative image (Duhalde) or remain evasive about their intentions to compete (Reutemann). In Congress, opposition parties have sought to nurture a unified front to limit the executive's use of discretionary power, challenge its policies, and inspire confidence in a future anti-Kirchner alliance's capacity to govern. But while many initiatives have been approved by one of the two chambers, the opposition is failing to get laws out the door. This week's Senate approval of a bill to reform INDEC (the statistics institute with which the Kirchners intervened in 2007) might be an exception.

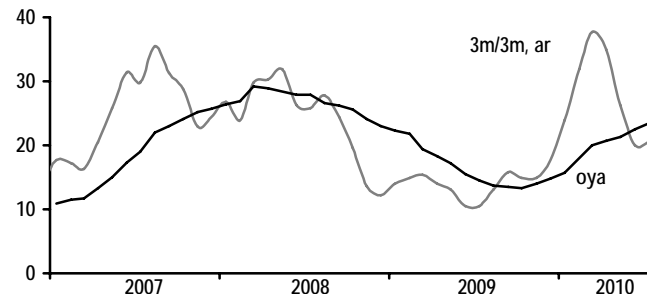
### President Cristina Kirchner's image

% of polled, source: Poliarquia



### CPI estimate (BA City)

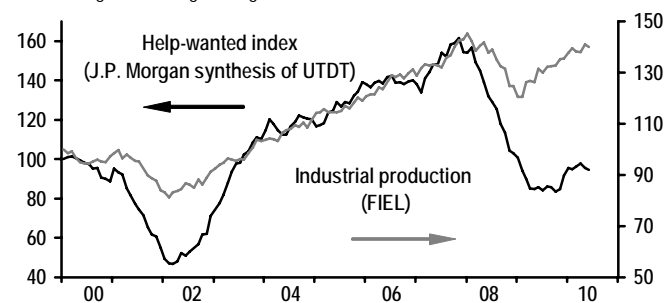
% oya



### Industrial production and help-wanted index

Level, weighted average of regional indices

Level, sa



### Political leaders' image

% of polled, July 2010, source: Poliarquia

	P - N	Positive	Regular	Negative	N/A
Pro-Kirchner Peronist (center left)					
N. Kirchner	-9	34	22	43	1
D. Scioli	12	37	33	25	5
J. Urtubey	4	7	10	4	80
Dissident Peronist (center right)					
C. Reutemann	11	31	36	20	14
E. Duhalde	-12	26	32	38	4
F. Sola	7	29	37	22	12
PRO (center right)					
M. Macri	7	35	32	28	5
F. De Narvaez	10	35	29	25	11
ARI / Radical Party (center left)					
R. Alfonsin	28	43	28	15	13
E. Carrio	-8	27	35	34	5
J. Cobos	10	36	30	25	9

## Argentina:

### Data releases and forecasts

Week of August 16 - 20

Fri Aug 13	Consumer prices	Apr	May	Jun	Jul
	Consumer prices (%m/m)	0.8	0.7	0.7	—
	%oya	10.2	10.7	11.0	—
	Wholesale prices (%m/m)	1.0	1.0	0.9	—
	%oya	14.5	15.2	15.2	—
Thu Aug 19	Consumer confidence	May	Jun	Jul	Aug
	Consumer prices (%m/m)	48.61	47.63	48.17	—
Fri Aug 20	Industrial production	Apr	May	Jun	Jul
	%oya nsa	10.2	10.2	9.80	—
Fri Aug 20	Economic activity	Mar	Apr	May	Jun
	%oya nsa	8.10	9.70	12.40	—

### Review of past week's data

No data released.

## Colombia:

### Data releases and forecasts

Week of August 16 - 20

Wed Aug 18	Industrial production	Mar	Apr	May	Jun
	%oya	6.54	7.56	7.53	—
Wed Aug 18	Real retail sales	Mar	Apr	May	Jun
	%oya	9.47	7.95	13.10	—
Fri Aug 20	BanRep monetary policy meeting				
	%p.a.	May	Jun	Jul	Aug
	Repo rate	3.0	3.0	3.0	<u>3.0</u>

### Review of past week's data

No data released.

## Ecuador:

### Data releases and forecasts

Week of August 16 - 20

No data releases expected.

### Review of past week's data

No data released.

## Peru:

### Data releases and forecasts

Week of August 16 - 20

Mon Aug 16	Real GDP	Mar	Apr	May	Jun
	%oya nsa	8.76	9.26	9.19	—
	%m/m nsa	7.22	4.35	5.23	—

### Review of past week's data

No data released.

## Venezuela:

### Data releases and forecasts

Week of August 16 - 20

Week of Aug 16 - 20	Real GDP	3Q09	4Q09	1Q10	2Q10
	%oya nsa	-4.61	-5.80	-5.76	<u>-5.7</u>
	%q/q saar	-6.78	-5.30	-5.57	<u>-5.0</u>

### Review of past week's data

No data released.

## United Kingdom

- **Data continue to suggest slowing growth into summer**
- **Strong gain in household-survey measure of employment comes as more timely indicators soften**
- **MPC keeps door open to more QE**

This was another week of mixed signals, which are consistent with some slowing in growth at midyear, but do little to shed light on the extent or longevity of that slowing. The recent softer tone to indicators close to the consumption decision continued with a weak RICS survey and a slowing in the BRC measure of retail sales for July. The labor market data report a broadening improvement through to June, but the claimant count measure of unemployment warns that momentum was being lost in July. Indeed, as we expected, the majority on the MPC remain open-minded on where policy is headed next, and continue to regard high inflation outturns as temporary while risks to growth remain.

### Labor market: better and worse at once

As the claimant count measure of unemployment has registered declines through the first half of 2010, we have argued that the declines were large enough to suggest that other data sources would start to report significant gains in employment. The data, based on a survey of households through to May, had shown unemployment falling and employment rising, but with the latter driven entirely by self- and part-time employment. The data through to June delivered more strength, with one of the largest quarterly gains in employment on this measure since 1989. Moreover, a decent portion of that job growth (just over 40% of it) came in the form of full-time employees.

It remains the case that a shift toward part-time working is playing an important role in keeping people out of unemployment. Of course, the 74,000 gain in full-time employees over 2Q pales into near insignificance compared to the 945,000 jobs lost during the recession. But many commentators have been skeptical that the labor market would report any meaningful growth in full-time employment as output began to recover; the 2Q data suggest otherwise.

The June data also demonstrate that, relative to the potential swings in the private sector, the likely loss of jobs in the public sector this year is small. The change in government and the emergency budget have created the misleading impression of an abrupt swing toward a large-scale loss of public sector jobs. However, according to the projections from the Office for Budget Responsibility, general

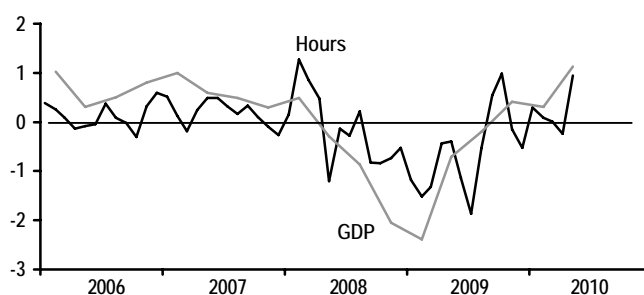
### Household survey-based employment

% 3m/3m sa



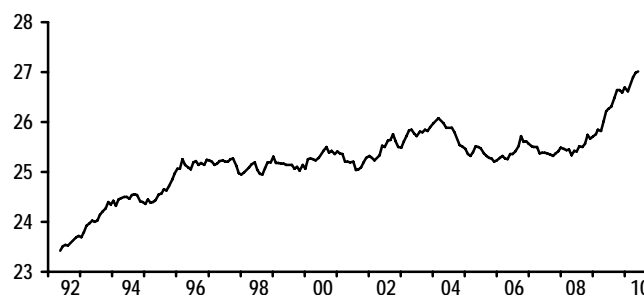
### Total hours worked versus real GDP

% 3m/3m sa



### Part-time employment

% share in total employment



government employment will fall by less than 10,000 (0.1%) comparing March 2011 with March 2010. The loss of jobs then steps up to a further 60,000 in the following year, and 80,000 the year after. To put these numbers in context, the 184,000 gain in employment in the three months to June is hence larger than the cumulative loss of public sector jobs forecast for the coming three years. In the near term, it is restraint in terms of public sector pay, rather than the large-scale loss of jobs, that serves to limit growth in the public sector wage bill.

The balance between public sector wage gains and job losses is forecast to change over the later years of this Par-



liament. As wage growth picks up to around 3%, but growth in the total wage bill is limited, the loss of public sector jobs is forecast to average near 160,00 a year over 2013-16. But the decline in public sector employment is forecast to be more back-loaded than many realize, and is likely to be overwhelmed by the swings taking place in the private sector over the coming couple of years.

The bad news is that, even as the data through to June have begun to deliver solid labor market performance, more timely indicators have turned weaker. The claimant count measure of unemployment fell by only 3,800 in July. Aside from a snow-disrupted January, that is the smallest such decline since October. The data on vacancies also softened a little in July, while business survey readings on employment have also turned weaker over the past couple of months. None of these movements is large enough to be definitive at this stage. But although the labor market may have performed better than many expected through to midyear, signs are accumulating that outperformance may prove short-lived.

## 2Q construction surge confirmed

A surge in construction output was the key driver of the upside surprise in 2Q GDP. The full data for the quarter have seen the gain in construction output revised higher to 8.6%q/q sa, the largest since 1963. The gain was broad-based across sectors, with private housing work rising 22%q/q. Although weather may have disrupted output in 1Q, the strength of the 2Q data cannot be explained solely by that. After such a large gain in 2Q, and with the government canceling some spending on public infrastructure, it would be foolhardy to expect another large gain in the next quarter. But the level of construction work as a whole remains down 8.6% from its pre-recession peak, and beyond the possibility of some mild payback in the 3Q GDP number, we see little reason to expect construction output to emerge as a big drag on GDP in the next handful of quarters.

## MPC remains inclined to ease

The August inflation report played largely to the script we described last week, with the MPC keen to downplay the significance of recent inflation surprises as a barometer of the medium-term trend, and retaining a willingness to move policy in either direction as the data flow evolves. The fact that the report suggests inflation is "a little more likely to be below the target than above it during the second half of the forecast period" suggests that the majority on the MPC remains more inclined to extend QE in the near term than begin tightening. Next week's minutes will reveal whether any of the MPC were already voting for additional QE; our

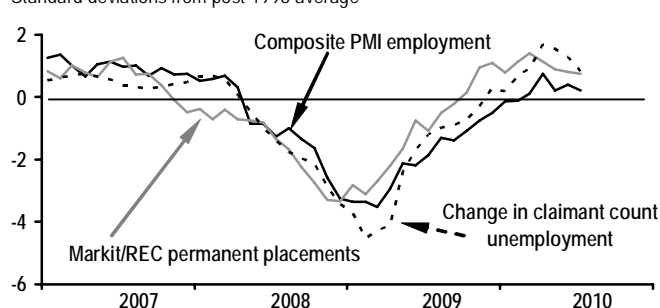
## OBR forecast for general government employment

Data are for March of each year

	2010	2011	2012	2013	2014	2015	2016
Level (mn)	5.54	5.53	5.47	5.39	5.23	5.04	4.92
% change		-0.1	-1.2	-1.3	-3.0	-3.7	-2.4

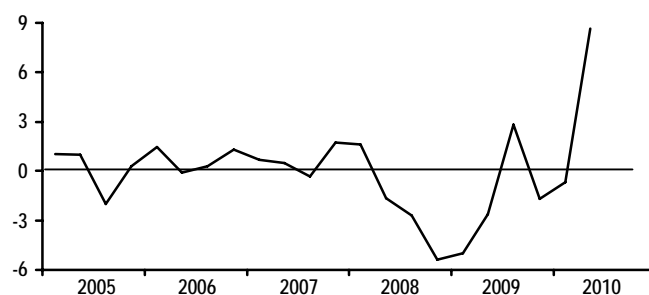
## Timely labor market indicators

Standard deviations from post-1998 average



## Construction output

% q/q sa, volume



best guess is that the vote remained at 8-1 with Sentence dissenting for a hike in rates.

Although the MPC's forecast for GDP growth was downgraded, the move down was less than we had thought. The MPC's central forecast for growth at a near-3% pace through 2011-12 remains relatively upbeat compared to consensus and other official forecasts. The near-term inflation forecast was upgraded as expected given the coming increase in VAT, and does not show inflation slipping back below the 2% target until early 2012. Our analysis suggests that this forecast is too high, with inflation likely to fall below target in 2Q11 assuming sterling and global commodity prices are stable (see the research note "UK inflation: Sticky, but set to slide faster than the MPC thinks" in this week's *GDW*). The forecast continues to anticipate that policy remains on hold until rates begin to rise in May of next year.

## Data releases and forecasts

Week of August 16 - 20

Tue Aug 17 9:30am	Retail prices %oya	Apr	May	Jun	Jul
	CPI	3.7	3.4	3.2	<u>3.0</u>
	Core CPI <sup>1</sup>	3.1	2.9	3.1	<u>2.8</u>
	RPI (1987=100)	222.8	223.6	224.1	<u>223.6</u>
	RPI	5.3	5.1	5.0	<u>4.8</u>
	RPIX	5.4	5.1	5.0	<u>4.8</u>

1. CPI ex food, energy, alcohol, and tobacco.

Core goods prices rose significantly in July last year. Our view has been that a fading impact from currency weakness would slow gains in core goods prices this year. So far, the news on this front has been mixed, but if we are right, a slowing in core goods inflation—together with softer energy and services inflation—will bring core inflation down to 2.8%. Risks here appear to the upside. However, we have penciled in a strong monthly gain for food, alcohol, and tobacco prices. This would follow two weaker readings, and the risks here appear to the downside. Overall, this implies balanced risks on the forecast for headline inflation. If the CPI slows to 3.0%, Mervyn King will avoid having to write another open letter to the Chancellor. He will have to write such a letter if CPI prints at 3.1%oya or above.

Wed  
Aug 18  
9:30am

### BoE's minutes of Aug MPC meeting

An 8-1 vote for unchanged rates is expected, with Sentence retaining his dissent for a hike in rates. A vote for an extension of QE from Miles or Posen is possible, but we doubt they have seen enough weakness in the data to persuade them as yet.

Thu  
Aug 19  
9:30am

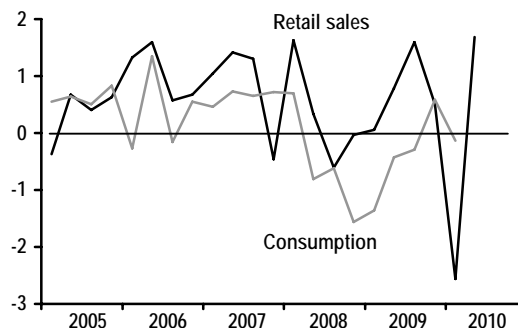
### Retail sales

Volumes, seasonally adjusted	Apr	May	Jun	Jul
Including auto fuel (%m/m)	-0.2	0.8	0.7	<u>0.3</u>
Ex auto fuel (%m/m)	-0.3	0.7	1.1	<u>0.2</u>
Ex auto fuel (%oya)	1.6	2.9	3.1	<u>1.8</u>
Ex auto fuel (% 3m/3m saar)	-0.7	1.8	5.4	<u>5.8</u>

The retail sales data enter 3Q with decent momentum after solid gains in May and June. Indications for July are mixed: the CBI retail survey was strong, but the BRC reading softened in the month. The forecast for a modest gain in ex auto fuel sales would leave the retail sales data looking strong relative to other indicators close to the consumption decisions (such as confidence and mortgage approvals). As always, we would caution that the retail sales data are not a very reliable window on broader trends in consumer spending.

### Retail sales versus private consumption growth

% q/q sa, volumes



Thu  
Aug 19  
9:30am

### Provisional estimates of M4 money and credit

Seasonally adjusted

	Apr	May	Jun	Jul
M4 (%m/m)	0.1	-0.1	0.0	—
M4 (%oya)	3.2	2.7	3.0	—
M4 lending (%m/m) <sup>1</sup>	-0.5	-0.5	0.0	—
M4 lending (%oya) <sup>1</sup>	2.6	1.2	1.3	—

1. Excludes the effect of securitization.

Thu  
Aug 19  
9:30am

### Public sector finances

£ bn, nsa

	Apr	May	Jun	Jul
PSNCR	6.5	14.1	20.9	—
PSNB	8.7	17.0	14.5	<u>7.5</u>
Balance on current budget	-7.0	-14.9	-12.6	<u>-5.2</u>
Net debt to GDP (%)	62.0	62.6	63.9	—

July is an important month for tax revenues, which usually results in a lower borrowing requirement. However, for the past year or more, revenue-intensive months have surprised with larger borrowing requirements. We have taken this into account, and expect a £7.5 billion borrowing requirement. More recently, the trend in public sector finances has stopped deteriorating. Even with our forecast for July, borrowing would be on track to come in slightly below the OBR's £149 billion projection for 2010-11.

Thu  
Aug 19  
11:00am

### CBI industrial trends

% balance

	May	Jun	Jul	Aug
Total order book	-18	-23	-16	<u>-16</u>
Output expectations	17	15	6	<u>4</u>
Output prices	14	9	5	—

The manufacturing side of the survey data has held up well to date, and the CBI survey has never quite delivered the degree of strength seen in the PMI or official output data. Those two observations suggest this first look at manufacturing activity for August should not see a sharp weakening.

## Review of past week's data

### RICS housing market survey

%bal sa

	May	Jun	Jul
Prices in past 3 months	21.5 21.4	9.5 8.3	8.0 -8.4
Stocks of homes on books	61.7 61.9	66.7 66.4	— 69.1
Sales in past 3 months	16.5	16.7	— 16.6
Sales to stocks ratio (%)	26.8 26.7	25.0 25.1	— 24.0
New buyer inquiries	8.4	5.1 -5.7	— -9.9

The July RICS survey extended the weakening trend of recent months with the reported prices balance falling into negative territory for the first time since July 2009. The recent pattern of depressed sales but an increasing flow of property coming on to the market for sale has continued. RICS have suggested that the step up in the flow of property may reflect vendors testing the market given that the new government has abolished the need for them to provide home information packs. However, there appears little imminent prospect of a step up in demand, with the new buyer enquiries reading falling further below zero. Averaging across the lender's indices, the 3m/3m rate of change of house prices remains positive, but the RICS survey continues to flag downside risks to our view that house prices will run flat in nominal terms into early 2012.

### BRC retail sales monitor

	May	Jun	Jul
Like-for-like sales (%oya)	0.8	1.2	— 0.5
Total (%oya)	3.0	3.4	— 2.6

Both the indicators of BRC retail sales are down by more than half a point on June, and are at the bottom of the range seen over the past nine months or so once the effects of shifting seasonality and the weather are stripped out. Base effects for the oya comparison in the month were mildly negative, but the strength in the CBI retail reading for the month has not been replicated here.

### Trade balance

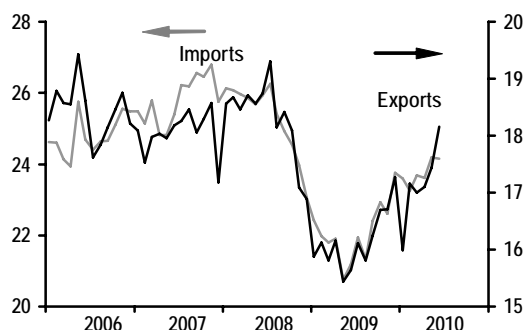
£ bn, seasonally adjusted

	Apr	May	Jun
Trade balance (goods)	-7.4	-8.1 -8.0	— -7.4
Trade balance (services)	3.9 4.1	4.2	— 4.1
Total trade balance	-3.5 -3.4	-3.8	— -3.3

The June trade report showed a solid performance for exports in the month capping what was a solid performance across 2Q as a whole, suggesting a small positive contribution to GDP growth from net trade for the first time in four quarters. The bad news is that some of the strength in exports in 2Q reflects a bounce after a weather-impacted 1Q, and that there is still little sign of the drop in the currency being translated into lower foreign currency prices. Moreover, although growth in imports was relatively soft in 2Q, the trend remains for it to broadly keep pace with exports.

### UK goods exports and imports volumes

£bn samr, excluding MTIC fraud



### DCLG monthly house price data

	Apr	May	Jun
All dwellings (%oya nsa)	10.1 9.8	11.0 10.6	— 9.9

### Nationwide consumer confidence index

	May	Jun	Jul
Index, sa	66	63	60 66

### Labor market statistics

	May	Jun	Jul
Claimant count (000s ch m/m sa)	-31.1	-20.8 -15.9	-18 -3.8
Claimant count rate (%sa)	4.6	4.5	4.4 4.5
Average weekly earnings (3mma % oya sa)	Apr	May	Jun
Headline	4.1	2.8 2.7	1.2 1.3
Ex bonuses	1.9	1.8	2.0 1.6
Private sector ex bonuses	1.2	1.1	0.9 1.0
Three months to:	Dec	Mar	Jun
Labor force survey (all percentage rates)			
Activity rate	63.2	63.1	— 63.2
Employment rate	58.0	58.0	— 58.3
Unemployment rate	7.8	8.0	7.8

See main text.

### BoE quarterly inflation report

See main text.

### Construction output

All work, volume sa

	4Q09	1Q09	2Q10
%q/q	-1.5 -1.7	-1.1 -0.7	— 8.6
%oya	-6.4 -6.5	-1.9 -2.2	— 9.1

See main text.

## Sweden and Norway

- **Norges Bank stays put and delivers neutral rhetoric**
- **Conflicting signals on 2Q GDP in Norway**
- **Core inflation to slow further in Sweden and Norway**

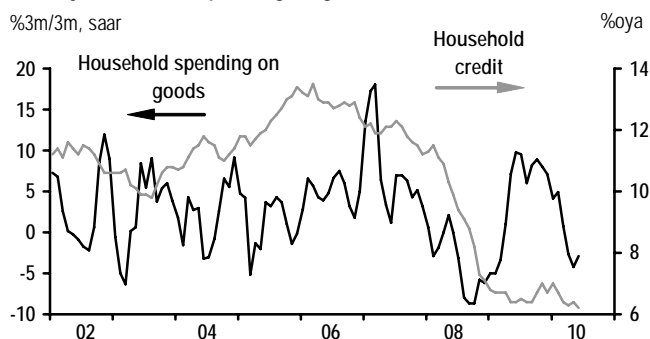
The Norges Bank this week kept the policy rate at 2%, as widely expected, and delivered a neutral statement. The Bank assessed that growth and inflation have been largely in line with its forecast. It also noted that global growth has been a little stronger than expected and that European sovereign market stress has been receding, but that the outlook for the US economy has become more uncertain.

More generally, the Bank commented that, although Norwegian household debt growth slowed recently, a gradual rise in the policy rate ahead is warranted to prevent financial imbalances from building. Still, the Bank seems in no rush to move, mentioning that the policy rate will likely lie in the interval of 1.5%-2.5% (midpoint: 2%) in the period until the publication of its next monetary policy report in late October. Implicitly, the Bank seems to have endorsed the policy rate projections it presented in June, which involved a gradual rise in the policy rate from December this year or early next year. With European growth slowing into year-end, and with core inflation continuing to slide in Norway, we think that the Bank will not move until 2Q next year.

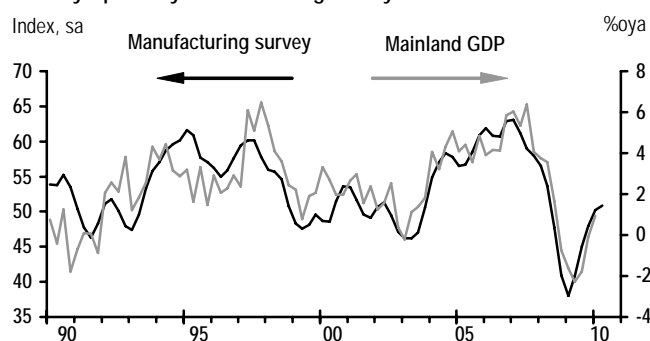
### Uncertainty around Norway's 2Q GDP

We and the Norges Bank expect mainland (non-oil and gas) GDP—released next week—to have grown 2% ar in 2Q. Our confidence in the forecast, however, is low given the difficulty in tracking Norwegian GDP on a high-frequency basis and given conflicting signals from available activity indicators. The Norges Bank's regional network report (its quarterly company survey) points to output growth of around 2% ar. At the same time, manufacturing activity rose a solid 4.3% ar in 2Q, and Statistics Norway's manufacturing business survey—which we use as a proxy for growth in the non-oil economy—was at a level consistent with our GDP forecast. Available expenditure indicators, on the other hand, have been disappointing. The index of household goods' consumption fell 3% ar in the quarter, and trade figures suggest that trade was a drag on mainland GDP. That leaves government spending, fixed investment, and stockbuilding doing the bulk of the lifting. We expect mainland investment to rebound following a sharp fall in 1Q, and we expect inventories to provide a big boost to growth. We should point out that our confidence in the forecast is not very high.

### Norway: household spending on goods and household credit

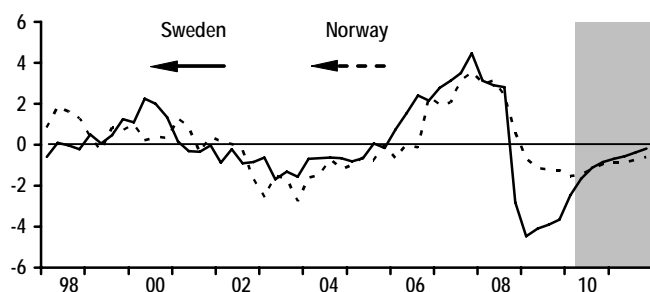


### Norway: quarterly manufacturing survey and mainland GDP



### Output gap

% deviation of GDP from potential (J.P. Morgan estimates)



### Core inflation to slide further below target

This week's releases showed CPIF ex. energy inflation in Sweden falling, to 1.5%oya from 1.8%oya, while CPI-ATE inflation in Norway stabilized at 1.3%oya in July. Swedish growth has been very strong in recent quarters, but the low level of activity means that the output gap will take time to close. In Norway, the output gap was smaller to start with, but the recovery has been sluggish so far. The still-low level of resource utilization in Sweden and Norway suggests that core inflation will drop further, to close to 1%oya by year-end in our forecast.

The next Sweden and Norway data watch will be published on August 27.

## Sweden:

### Data releases and forecasts

#### Weeks of August 16 - 27

##### Wed Aug 18 9:30am SCB capacity utilization

	3Q09	4Q09	1Q10	2Q10
Manufacturing (sa)	78.0	80.0	84.9	—

##### Wed Aug 25 9:15am NIER business and consumer surveys

	May	Jun	Jul	Aug
Mfg tendency index, sa	3	10	5	—
Consumer index, nsa	18.8	22.0	23.3	—

##### Thu Aug 26 9:30am Trade balance

	Apr	May	Jun	Jul
Skr bn, nsa				
Exports	92.5	91.5	106.7	—
Imports	86.4	89.4	95.3	—
Trade balance	6.1	2.1	11.4	—

##### Thu Aug 26 9:30am Unemployment: Labor Force Survey (Statistics Sweden)

	Apr	May	Jun	Jul
% of labor force, nsa	9.5	8.8	9.5	—

##### Fri Aug 27 9:30am Retail sales

	Apr	May	Jun	Jul
Volumes				
%m/m sa	0.4	1.3	-0.2	—
%oya wda	-0.9	2.6	2.8	—

### Review of past two weeks' data

#### Purchasing managers survey, manufacturing

% balance, sa	May	Jun	Jul
Overall index	66.0	62.4	— 64.2

#### Unemployment: labor force survey (Statistics Sweden)

	Apr	May	Jun
% of labor force, nsa	9.5	8.8	— 9.5

#### Consumer prices

	May	Jun	Jul
CPI (%oya)	1.2	0.9	— 1.2 1.1
CPIF (%oya)	2.1	1.9	— 1.6 1.7

#### Unemployment: monthly labor market board

	May	Jun	Jul
% of labor force, nsa	4.5	4.8	— 4.8

#### Industrial production

	Apr	May	Jun
Production (%m/m sa)	1.0 1.1	2.3 2.0	— 1.1
Production (%oya nsa)	7.2 7.3	12.4 12.0	— 12.0

## Norway:

### Data releases and forecasts

#### Weeks of August 2 - 13

##### Mon Aug 16 10:00am Trade balance

Nkr bn, excluding erratics, nsa	Apr	May	Jun	Jul
Exports	63.6	61.2	67.2	—
Imports	36.4	34.7	41.8	—
Trade balance	27.2	26.5	25.4	—
Balance ex oil and gas	-11.5	-8.3	-12.0	—

##### Thu Aug 19 10:00am Real GDP

Non-oil	3Q09	4Q09	1Q10	2Q10
Mainland GDP (%q/q sa)	0.3	0.4	0.1	0.5
Mainland GDP (%q/q saar)	1.3	1.6	0.6	2.0

##### Wed Aug 25 10:00am Labor force survey

3mma sa	Mar	Apr	May	Jun
Unemployment rate (%)	3.5	3.6	3.6	—

### Review of past two weeks' data

#### Purchasing managers survey, manufacturing

% balance, sa	May	Jun	Jul
Overall index	50.4	51.2 52.0	— 54.9

#### NEF/EEF house prices

All dwellings, NOK	May	Jun	Jul
%m/m	0.4	-0.4 -0.2	— -1.5
%oya	9.1	8.4 8.3	— 6.6

#### Labor force survey

3mma,sa	Mar	Apr	May
Unemployment rate (%)	3.5	3.7 3.6	— 3.6

#### Industrial production

Manufacturing	Apr	May	Jun
%m/m sa	0.1 0.2	-0.9 -1.3	— 3.3
%oya wda	3.0	2.2 2.4	— 7.2

#### Consumer prices

	May	Jun	Jul
CPI (%oya)	2.5	1.9	— 2.2 1.9
CPI-ATE (%oya)	1.5	1.3	— 1.6 1.3

#### Retail sales

Volumes	Apr	May	Jun
%m/m sa	0.0 0.1	-0.1	— -0.1
%oya sa	1.0	-0.8	— 1.9



## Central Europe: Czech Republic, Hungary, Poland, Romania

- **Poland: “middle of the road” fiscal plan does minimum to keep debt under control ahead of elections**
- **Czech: budget gap target for 2011 set at 4.6% of GDP; reforms to stabilize debt close to 40% of GDP**

Details of the Polish government’s four-year fiscal plan for 2010-13 were released late last Friday after the cabinet approved it earlier in the week. The plan effectively pushes back the deadline for meeting the 3% of GDP Maastricht limit by one year, to 2013—even though Poland is subject to the EU’s excessive deficit procedure, which states that the excessive deficit must be corrected by 2012. There is little in the way of structural/public finance reform in the plan and most of the forecast deficit reduction comes from an increase in the VAT rate, while debt growth will be contained by selling more stakes in state-owned companies. All in all, the fiscal plan appears to do the minimum required to keep public finances under control, while avoiding any cuts in investment or social spending ahead of the 2011 parliamentary elections. Indeed, Prime Minister Tusk aptly called his own program “middle of the road.”

The fiscal plan foresees a reduction in the general government deficit (according to Polish methodology) to PLN45 billion in 2011 from PLN52 billion this year. The increase in the main VAT rate by 1%-point, to 23%, will remain in place for three years and is expected to generate PLN4.9 billion in additional revenue. On the spending side, the plan contains the previously announced cap on discretionary spending. The plan foresees public borrowing staying just below, but dangerously close to, 55% of GDP—the threshold that triggers mandatory fiscal tightening. Net borrowing needs are projected to fall sharply next year, thanks in part to the sale of the government’s stakes in PZU and PKO BP. The government aims to raise around PLN30 billion (2% of GDP) in privatization revenues over the next three years.

Positively, conservative budget planning could yet result in outperformance of the official targets. This year’s state budget deficit is tracking PLN10-15 billion below target thanks to stronger-than-planned growth, and we believe that the 2011 budget due to be submitted to parliament could be about PLN5 billion lower than set out in the fiscal plan. The macro assumptions underlying the four-year plan appear to be on the conservative side of both inflation and GDP growth. Incorporating the impact of the VAT hike from January next year, we estimate that CPI inflation will top 3% oya versus the 2.3% contained in the official plan.

### Poland's four-year fiscal plan

PLN bn, according to Polish methodology

	2010	2011	2012	2013
Central state budget	52.2	45.0	40.0	30.0
General government	80.0	75.8	47.8	23.4
Net borrowing need	82.4	57.5	62.8	38.6
Public debt, % of GDP	54.7	54.4	54.6	53.7
Privatization revenues <sup>1</sup>	25.0	10.0	10.0	10.0
Macro assumptions (%oya)				
Polish real GDP growth	3.0	3.5	4.8	4.1
Euro real GDP area growth	0.9	1.5	2.0	2.0
CPI inflation	2.0	2.3	2.5	2.5

1. Assumes equal distribution of the planned PLN30bn over 2011-13

### Czech: fiscal consolidation in the pipeline

The new government won a confidence vote in Parliament on August 10, as expected. Moreover, the new government presented the first draft of the 2011 budget with a targeted deficit equivalent to 4.6% of GDP, down from 5.3% of GDP targeted for this year. The exact manner by which the deficit reduction will be achieved has yet to be approved, but the intention is to cut public sector operating spending, including the public wage bill, by 10%; to proceed with cuts in social policy spending; and to hike taxes modestly. Naturally, the intended measures are more about keeping the budget gap small than about much-needed long-term structural reform.

Given that the coalition has a large majority in parliament for the first time since the mid-1990s (118 seats out of 200), expectations are high that the government will push through long-delayed reforms, such as pension and healthcare changes. This week, S&P joined Fitch and Moody’s in raising the Czech Republic’s credit rating outlook to positive. The country’s rating, currently A, may be raised if expected reforms are delivered. The path of fiscal consolidation and even willingness to reform will be strongly influenced by the business cycle in Europe. The export-oriented Czech economy has been riding the German recovery so far, but ongoing softening in the recoveries of both the US and Asia are clearly a headwind. However, even in a double-dip scenario, the right-wing government is most likely to keep fiscal accounts under control, in our view. We expect Czech public debt to stabilize at around 40% of GDP over coming years, up from about 30% of GDP during most of the past decade and 35.4% of GDP last year. A stabilization in public debt at relatively low levels, in comparison with regional peers and most of the Euro area countries, should support the Czech Republic’s status as a relative safe haven in the EMEA universe.

The Central Europe data watch is published biweekly, next on August 27.

## Czech Republic:

### Data releases and forecasts

Weeks of August 16 - 27

No major data releases.

### Review of past two weeks' data

#### Monetary policy announcement

The CNB kept its base rate at 0.75% and no MPC member voted for a change in rates. Governor Singer did not sound as dovish as expected, following the recent koruna gains. The FX move has been dramatic over the past two weeks, but the current level is not a serious problem, in his view. We expect the CNB to keep the rate at 0.75% until 2Q11, when a gradual tightening cycle would start. Our target for end-2011 is 1.75%. In the short term, risks to the call are skewed toward a cut in rates if the koruna's rally continues. In the medium term, a revival in core inflation should signal the need to push rates higher, even with likely tightening delivered by FX rises.

#### External trade

CZK bn

	Apr	May	Jun
Trade balance	15.2 14.7	12.3 12.1	13.0 10.4
Ytd	62.4 60.7	74.7 72.8	87.7 83.2
Ytd a year ago	47.8	59.5	79.8
Exports, %oya	13.5 13.4	24.4 24.2	17.7 19.7
Imports, %oya	13.5 13.8	25.9	23.6 28.0

Export-oriented recovery has continued, but the trade surplus has started to narrow as imports bounced at an even stronger pace than exports. A gradual narrowing of the trade surplus is likely to persist in coming months as reviving domestic demand pushes up imports.

#### Industrial output

%oya

	Apr	May	Jun
Production	10.2 10.9	16.9	15.0 9.7

The industrial sector has been performing well, but we expect export-oriented production to moderate due to an anticipated slowdown in the global economy.

#### Consumer prices

%oya

	May	Jun	Jul
%oya	1.2	1.2	1.9
%m/m nsa	0.1	0.0	0.3
Food	-0.3	0.7	3.3
Housing	1.4	1.4	1.9 2.2
Transport	3.8	1.8	1.9 1.5

CPI increased to 1.9%oya in July. We expect headline inflation to continue to drift higher to a range of 2%-3%oya in coming months, driven by the base effect in food and fuel prices and slowly reviving core inflation.

### Balance of payments

CZK bn

	Apr	May	Jun
Current account	12.4	-24.0	-8.0 -15.0
Ytd	28.5	4.5	-3.5 -10.5
Ytd a year ago	28.6	12.9	-5.8
Trade balance	21.2	18.7	19.0 17.4
Services	-2.1	-6.0	-4.0 -8.9
Income	-6.0	-39.5	-25.0 -24.0
Current transfers	-0.6	2.8	2.0 0.4
Financial account	-20.4	36.4	— 28.1
FDI	3.9	7.7	— 6.3
Portfolio investment	32.3	-4.9	— 30.2
Other investments	-57.9	39.7	— -9.1

We expect the current account to widen slightly this year, to close to 2% of GDP from 1.1% of GDP last year, thanks to the bounce in dividend outflows and revival in imports, which until recently lagged the revival in exports.

### Real GDP, preliminary

%oya, unless otherwise stated

	4Q09	1Q10	2Q10
GDP growth	-2.9	1.1	2.2
%q/q saar	2.2	2.0	2.5 3.2

The slight acceleration in the recovery has so far been driven mainly by the export-oriented manufacturing sector in 2Q, but the first signs of a spillover into domestic demand are already visible. Strong industry-driven growth in Germany has been naturally positive and the Czech GDP outlook remains particularly receptive to the performance of Germany's corporate sector. Of course, the anticipated slowdown in global industrial production in 2H10 is an important headwind. However, the ongoing gradual switch from a purely export-driven recovery to growing domestic demand is likely to keep the Czech economy on a gentle upward path over the coming year and half, as long as foreign demand does not weaken abruptly.

## Hungary:

### Data releases and forecasts

Weeks of August 16 - 27

Mon  
Aug 23

#### Monetary policy announcement

The NBH is likely to remain in wait-and-see mode as falling core inflation and weak domestic demand are offset by above-target headline inflation, due to cost-push factors. Given the likely upward revision to staff CPI forecasts, we do not believe that the NBH can afford to resume its easing cycle. We expect the next rate move to be a hike, although not until mid-2011.

Wed  
Aug 25  
9:00am

#### Retail trade

	Mar	Apr	May	Jun
% change				
%oya wda	-4.0	-5.0	-4.7	-5.5
%m/m swda	-0.4	-0.8	-0.5	-0.2

## Review of past two weeks' data

### Industrial output

%oya

	Apr	May	Jun
Production, wda	9.7	9.8	13.7
Production, nsa	9.7	9.6	13.7
%m/m swda	1.2	0.3	5.4

Industrial production maintained positive growth momentum in June. Some payback in the m/m output gain looked inevitable after the May surge, but the annualized IP rate stood at an impressive 17.8% in 2Q, up from 13.5% in 1Q and only marginally lower than the 18.5% gain in the three months to May. Industrial production was driven mostly by export-oriented industries such as vehicles. Domestic sales appear to have reversed their earlier gains, falling back into the red.

### External trade

EUR mn

	Apr	May	Jun
Trade balance	505	429	424
Ytd	1822	2250	2245
Ytd a year ago	978	1402	1729
Exports, %oya	21.4	22.7	22.9
Imports, %oya	21.1	25.2	—

Hungary's June trade surplus was larger than expected. This was the 18th consecutive monthly surplus and took the 12-month trade surplus to new high of 5.1% of GDP. Export growth continued to accelerate, but imports lost some steam. Exports are mainly driven by booming German exports, as a large part of Hungarian exports supply German manufacturing companies. On the bright side, Hungary's external financing needs continue to fall. We now expect the 2010 current account to post a surplus of 0.5% GDP, compared to our earlier forecast of a deficit. This is notwithstanding the likely slowdown in Euro area growth momentum in 2H10.

### Consumer prices

%oya

	May	Jun	Jul
All items (KSH)	5.1	5.3	3.8
%m/m nsa	0.9	0.2	0.1
Food	-1.3	1.1	—
Consumer durables	1.0	0.6	—
Gasoline	27.0	20.4	—
Services	5.7	5.5	—
Core inflation	3.9	3.5	—
%m/m sa	0.1	-0.1	—
Regulated g&s (NBH)	8.6	9.0	—
Market g&s (NBH)	1.8	2.5	—

The over-year-ago CPI rate fell sharply, owing to a base effect from last July's VAT hike. Food prices continued to put upward pressure on inflation following the heavy rains and floods in May and June. At the same time, core inflation extended its downtrend, with the 3m/3m annualized rate falling below 1%. We expect headline CPI inflation to remain broadly unchanged next month, but rising food price inflation to lift the annual headline CPI rate to 4.7% oya by year-end. We see some moderation in 2H11, but cost-push factors should keep the CPI above the 3% target through the year.

### Real GDP, preliminary

%oya, unless otherwise stated

	4Q09	1Q10	2Q10
Real GDP	-4.0	0.1	1.2
%q/q saar	1.0	0.0	2.4

Real GDP growth increased close to expectations in over-year-ago terms, but sequential GDP was flat and the previous two quarters were revised lower. With the exception of a spurt of growth in 1Q, the economy has been effectively stagnating. The detailed GDP release due on September 8 should show that final domestic sales continued to weigh on growth, while net exports and inventories provided a boost. We still look for growth to pick up to an annualized pace of 2% q/q in 2H10, and this would bring full-year growth to around 0.8%-1.0% oya. The absence of any recovery in domestic demand poses downside risk to the forecast.

## Poland:

### Data releases and forecasts

Weeks of August 16 - 27

#### Tue Aug 17 2:00pm Gross wages and employment

	Apr	May	Jun	Jul
Gross wages, nominal	3.2	4.6	3.5	3.0
Real (CPI-adj.)	0.8	2.3	1.2	0.9
Employment, 000s, nsa	5308	5320	5336	5355
Employment, %oya	0.0	0.5	1.1	1.5

Wage growth was probably pulled lower by a negative working-day effect, but employment should have continued to recover both in m/m and oya terms.

#### Wed Aug 18 2:00pm Producer prices

	Apr	May	Jun	Jul
Producer prices	-0.4	1.9	1.9	3.3
%m/m nsa	1.4	2.0	0.8	—

#### Wed Aug 18 2:00pm Industrial output

	Apr	May	Jun	Jul
Industry	9.7	13.5	14.5	12.0
%m/m swda by GUS	-1.8	3.4	1.0	0.5
Manufacturing	11.1	14.5	15.7	—
Construction	-6.2	2.3	9.5	—

Industrial output likely expanded again in July, although at a slower pace than in June. The output component of the July PMI declined 0.7-point, but the level remained in expansion territory.

Fri  
Aug 20  
2:00pm

**Core inflation**  
%oya

	Apr	May	Jun	Jul
CPI—ex food and energy	1.9	1.6	1.5	<u>1.3</u>
CPI—ex administered prices	2.1	1.9	1.9	—
CPI—15% trimmed mean	2.3	2.0	2.2	—
Avg. of four NBP measures	2.1	1.9	1.9	—

Tue  
Aug 24

**Monetary policy announcement**

We expect the NBP to remain on hold. This month's MPC statement might have a more hawkish tone as recent comments suggested that council members are not pleased with the absence of spending cuts in the government's fiscal plan (see main essay). Although headline inflation is set to move higher, core inflation will remain contained and the growth outlook remains uncertain. We do not expect rate hikes until next year.

## Review of past two weeks' data

### Balance of payments

EUR mn

	Apr	May	Jun
Current account balance	-336	<del>-268</del> -889	<del>-900</del> -1004
Ytd (bn)	-1.4	<del>-1.7</del> -2.3	<del>-2.6</del> -3.3
Ytd a year ago (bn)	-0.5	-1.0	-1.2
Trade balance	-262	<del>-455</del> -450	— -287
Exports, %oya	22.9	<del>24.3</del> 24.7	— 28.6
Imports, %oya	23.0	<del>29.6</del> 29.9	— 27.8
Service balance	264	<del>259</del> 250	— 300
Income balance	-881	<del>-955</del> -1571	— -1256
Current transfers	543	<del>883</del> 882	— 239
Fin. + cap. account balance	4143	<del>685</del> 1783	— 1358
FDI, net	430	<del>-370</del> 675	— -535

The current account deficit widened close to our forecast, while the previous month's deficit was revised up significantly. The deficit for the first half of the year tripled from a year earlier, while the 12-month gap rose to 2.1% of GDP. As expected, the current transfers surplus fell sharply owing to smaller EU fund inflows. The income balance was the main source of negative surprise. We expect the current account deficit to widen to 2.5% of GDP by year-end as dividend outflows gather pace and import growth continues to recover. On the financing side, FDI inflows maintained their recent pace. However, a pickup in outflows resulted in a net outflow during the month. Yet, FDI inflows still fully covered the current account deficit in the 12 months to June.

### Consumer prices

%oya

	May	Jun	Jul
All items			
%oya	2.2	2.3	<u>2.1</u> 2.0
%m/m	0.3	0.3	<u>0.1</u> -0.2
Food, %oya	0.6	2.2	— 2.4
Fuel, %oya	16.9	9.8	— 5.8

July CPI inflation eased a little more than forecast. Food and fuel and energy prices together accounted for a third of the inflation decline, largely on base effects, while core inflation accounted for the remainder of the drop in the oya CPI rate.

## Romania:

### Data releases and forecasts

Weeks of August 16 - 27

No major data releases.

### Review of past two weeks' data

#### Monetary policy announcement

The NBR kept its base rate at 6.25%. We continue to think the NBR is done with the easing cycle and expect no change in the next 12 months. While depressed domestic demand and no clear sign of a revival in private credit still call for more monetary easing, the NBR will likely avoid further rate cuts due to the risk of currency depreciation (in case of an adverse development in global markets) and an anticipated surge in headline CPI. Nor do we expect the NBR to increase the rate in the near term, as we share the view that the second-round effects of the VAT hike on inflation will be small, while we do not anticipate a large surge in EUR/RON.

#### Consumer prices

%oya

	May	Jun	Jul
%oya	4.4	4.4	<u>7.4</u> 7.1
%m/m nsa	0.2	0.2	<u>2.8</u> 2.6

Headline inflation jumped to 7.1%oya on the back of the 5%-point VAT hike. The immediate pass-through of the tax hike into inflation was a little weaker than expected. We foresee inflation rising slightly in coming months on delayed pass-through of the VAT hike. However, any sizable second-round inflationary effects are unlikely, in our view, because consumer demand remains depressed and recent austerity measures will not provide support in the close future.

#### Current account balance

EUR bn

	Apr	May	Jun
Current account	-0.6	<del>-0.8</del> -0.3	<u>-0.5</u> 1.2
Ytd	-2.1	<del>-2.9</del> -2.4	<u>-3.4</u> -3.6
Ytd a year ago	-1.4	-1.9	-2.4

The current account (C/A) is deteriorating, principally driven by a drop in labor remittances, while the trade deficit has not yet widened.

#### Real GDP, preliminary

%oya

	4Q09	1Q10	2Q10
%oya	-6.6	-2.6	<u>-0.6</u> -0.5
%q/q saar	-5.9	1.2	<u>2.0</u> 1.2

The contraction of Romanian economy eased further in 2Q, mainly thanks to export-oriented industry. However, ongoing fiscal austerity measures (the VAT hike and public wage cut as of July 1) are likely to prevent the economy from emerging fully from the recession. We expect the Romanian economy to contract 2% this year and rebound only slightly next year.



## Australia and New Zealand

- **RBA minutes to reiterate looming inflation pressure**
- **Aussie job gains slowed in July; jobless rate rose**
- **NZ retail sales unexpectedly bounced in 2Q**

The past week in Australia was chock-full of important economic data, but the messages were mixed. Consumer confidence, for example, boomed in August, but business confidence sank in July. Similarly, employment rose strongly in July, but the June housing finance data showed an unexpectedly sharp decline in demand for new home loans. The unemployment rate climbed, yet there was another healthy rise in the number of job advertisements, which augurs well for employment in the months ahead. The uncertainty probably means that the Reserve Bank will remain sidelined for the time being, while officials also await clarity on the durability of the global cycle.

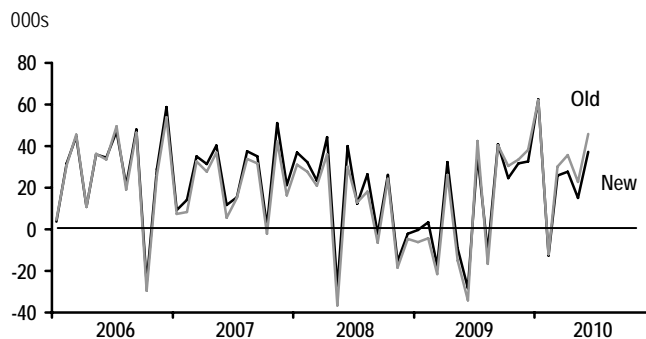
All the while, Australia's federal election campaign meanders toward polling day on August 21. Opinion polls hint that the Labor government will be re-elected with a reduced majority of seats in the Lower House of Parliament, but the opposition party remains competitive. The election probably will be very close, with the outcome determined ultimately by which leader avoids mistakes in the final week of campaigning. There is a small risk of a hung Parliament, which would necessitate prominent roles for the three independents, each of whom is likely to be re-elected. It is likely, though, that one of the major parties will gain a majority in the Lower House, with the Greens the big winners in the Upper House (see the research note "Australia's federal election still too close to call" in this week's *GDW*).

The past week was quiet across the Tasman Sea in New Zealand. The highlights were an unexpectedly large bounce in retail spending in June, and an even stronger rise in volumes terms across the June quarter. There is an element of spending being dragged forward by consumers ahead of the rise in the goods and services tax in October.

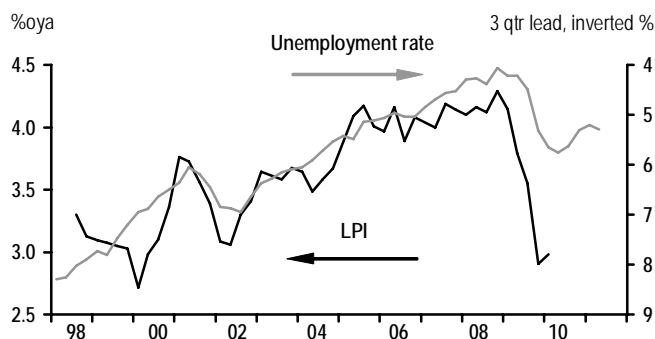
### Australia's jobs numbers slightly softer

This week's Australian labor force numbers for July delivered the slowing in momentum that we believed was in the pipeline, with 23,500 jobs added (J.P. Morgan and consensus: 20,000). The details were less upbeat, with an outright decline in full-time jobs (-4,000) and a rise in the unemployment rate to 5.3% from 5.1%. As hangovers go, though, this was a mild one, and the outlook for job growth remains solid for the rest of the year, given the buoyant ex-

Australia: employment change, new and old ABS estimates



Australia: labor price index and unemployment



port and investment outlook. The simultaneous rise in the unemployment rate represented a turnaround from the trend of recent months, in which a spurt of new additions to the labor force was quickly absorbed into employment. In July, the participation rate rose to 65.5% from 65.3%, representing an additional 48,000 job-seekers, which proved too much for the labor market to digest within the month.

Revisions to the ABS's population parameters mean the recent history of the participation rate also has been lifted uniformly higher. This represents a semi-permanent shock that will limit the downward path of the measured unemployment rate from here. It still is a little unclear whether the implied boost to the unemployment rate going forward represents a slightly looser labor market than previously thought, or redefines the framework for unemployment in general. This means that NAIRU also would be higher, and thus the true level of slack unchanged. Australia's recent experience of surging immigration flows supports the latter conclusion, but ultimately this question will be settled by the wage data.

### Labor prices to show tightening market

We expect the 2Q Labor Price Index, released next week, to show wage growth of 1.0% q/q, indicating that supply-side constraints already are biting, early on in the next up-



swing of the mining boom. The transmission from wage inflation to the goods market is being closely watched by RBA officials, who have cited the recent strength in public sector wage growth as a concern. The elevated reading we are expecting will support our contention that the RBA's tightening cycle has significantly further to run.

## Minutes to show RBA on hold for now

On Tuesday, the Reserve Bank releases the minutes from the early August Board meeting, at which members chose to leave the cash rate steady at 4.5% for the third straight month. The decision seemed pretty straightforward at the time (market economists were unanimous that policy would be unchanged), particularly given that the 2Q CPI result, released the week before the Board meeting, had produced an unexpectedly low print. The fact that core inflation fell back within the RBA's 2%-3% target range for the first time since 2007 gave RBA officials room to breathe. Indeed, having hiked the cash rate target six times since last October, and given the long lags associated with implementing monetary policy, the previous tightening still is washing through the economy. A key theme in the minutes probably will be reference to the stimulatory impact of the terms of trade, which soared 14%q/q in 2Q alone.

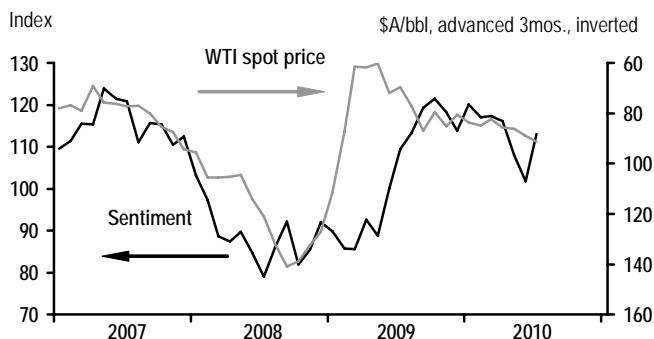
The RBA pushed up slightly the official inflation projections in the quarterly statement released the same week as the Board meeting. Officials now believe that core inflation will be heading back up to 3% by mid-2012. Our forecasts are even less benign, implying that inflation will head back above target during 2011. Indeed, the economy already is operating at close to full employment, a fact supported by yet another healthy gain in employment this week. This means that the policy pause earlier this month probably will not extend into 2011. We expect a further 25bp rate hike in November, followed by four more quarter-point hikes in 2011.

## Consumers refreshed by RBA pauses

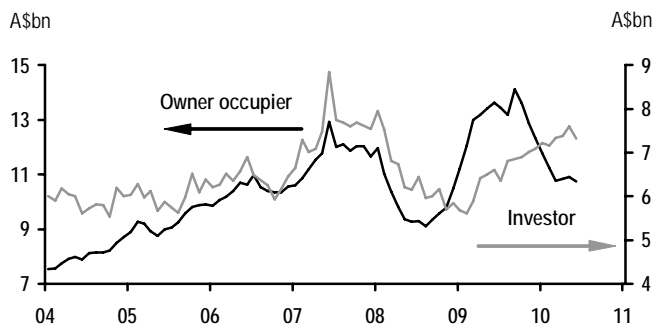
If Australian consumers practice what they preach, we can expect retail sales to gather steam in coming months. The solid 5.4% m/m rise in the Westpac-MI consumer confidence index for August was a particularly firm result given that there was plenty of potential for payback this month, with July's increase of 11.1% marking the largest rise in 13 months. Uncertainty over the outcome of the federal election, for example, could have weighed on sentiment.

Instead, conditions were ripe for consumers in early August: the RBA remained on hold for the third month in a row, AUD strengthened over the month, equities rallied, the release of the June labor market report had shown a fur-

## Australia: consumer sentiment and crude oil price



## Australia: housing finance



ther 46,000 jobs were gained (subsequently revised down), and the resolution of the mining tax impasse likely continued to pay "certainty dividends."

Overwhelmingly, though, the RBA's pause in early August was the most influential factor for this week's strong result. The outlook for consumption therefore hangs on whether, and how quickly, the RBA responds to households' gathering momentum, which can be seen in the details of the confidence report. The proportion of consumers stating that "now is a good time to buy major household items" posted a 3.5% m/m increase, and currently stands at a two-year high. On the other hand, confidence in family finances one year ahead pushed up 6.1% m/m, while the outlook for the economy one year ahead rose 8.6%. Consumers, it seems, plan to boost spending, but the fact that they upgraded their assessment of the economy beyond that for their own finances suggests they remain somewhat wary in anticipation of further monetary tightening.

## Home loans still on the downward trend

The number of home loans issued in Australia fell in June, in an unfortunate, though unsurprising, return to form. Home loan commitments dropped 3.9% m/m (J.P. Morgan and consensus: -2.0%), having risen in May for the first time in eight months. While the withdrawal of grant-sensi-

tive buyers, following the expiration of the expanded First-Home Buyers' (FHBs') grant, likely has run its course, there remain significant drags on loan demand.

FHB representation is still languishing near five-year lows and, while further downside is limited, we do not see a comeback in the pipeline. The absence of stimulus support, and the likelihood of rising interest rates, means the deck is stacked firmly against this sector. With investors currently accounting for 35.3% of total loans issued by value, a recovery in housing finance rests disproportionately on this group taking up the slack from FHBs. However, the softening price trend evidenced in private monthly surveys now is beginning to depress investor participation, too. Admittedly, there is some upside potential coming in the July and August numbers, with the RBA holding fire, though that fact will be counterbalanced by growing uncertainty around financial markets and the global economy, meaning households likely will remain hesitant to borrow.

## Consumer spending to boost NZ GDP

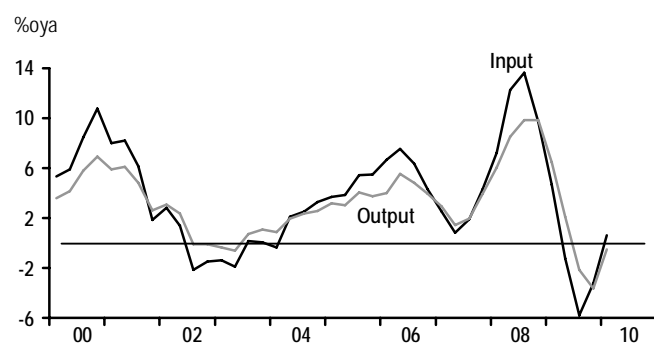
In New Zealand, the June/2Q retail sales reports showed that consumers in New Zealand brought forward demand significantly ahead of the coming Goods and Services Tax (GST) hike in October. Retail sales surged 0.9% over the month (J.P. Morgan: 0.6%; consensus: 0.5%), after rising 0.4% in May. Ex. auto sales were even stronger, rising 1.5% m/m, the largest gain in 13 months. To top it all off, retail volumes boomed, posting a 1.3% q/q gain, which, given the strength of sales values, was only partially explained by firms' discounting of stock. Indeed, in the monthly data, sales were strong in all sectors in which consumption can reasonably be substituted over time, e.g., household equipment, recreational goods, etc., as opposed to fresh produce and sales at cafes and restaurants.

This week's data are very much GDP growth positive, and should result in a significant contribution to 2Q GDP. However, the boost from the looming GST hike is largely synthetic, and obscures the fundamental picture of Kiwi households. Much hangs on how the global economy negotiates the downshift in growth momentum over the remainder of the year. New Zealand's post-GST hangover should arrive in 4Q, at which point the economy could find itself at a particularly difficult juncture. Policymakers have been open in their desire that households realign their spending patterns and consolidate balance sheets, which have historically been too leveraged to housing debt. The concern is that the consumer must take the back seat in driving growth at a time when the risks to trading partner growth, and

New Zealand: consumer confidence and retail sales volumes



New Zealand: PPI



hence the export outlook, appear to be mounting. For the RBNZ, this period is too far down the path to influence immediate policy decisions—we expect two further rate hikes this year, given that the cash rate is still at a highly stimulatory level—but the transition to the new growth model remains far from assured.

## Weak recovery easing supply constraints

Pipeline pressures likely were subdued in New Zealand in 2Q. Producer prices at the final stage of production probably fell 0.2% q/q, with import, gasoline, and consumer price inflation all weaker over the quarter. The benign trajectory of producer prices in New Zealand reflects the slow grind of the recovery so far. The labor market data, for example, have swung wildly, but likely are simply oscillating around mediocre outcomes on a gradually improving trend. Consumption similarly is subdued (some drag-forward pre-GST hike notwithstanding), and households are poised for a period of consolidation after a heady debt-laden few years. Inflation pressures are therefore weak, which should be evidenced in next week's PPI report. The data of course have limited implications for the goods market outlook, given that we already have the 2Q CPI number in hand.

## Australia:

### Data releases and forecasts

Week of August 9 - 13

Mon Aug 16 11:30am	Sales of new motor vehicles Units, sa	Apr	May	Jun	Jul
	%m/m	8.6	-3.9	-1.2	<u>2.0</u>
	%oya	29.2	16.5	8.2	<u>18.4</u>

Industry data suggest sales volumes ticked up over the month, probably buoyed by discounting moving into the new financial year.

Wed Aug 18 10:30am	WMI leading index Sa	Mar	Apr	May	Jun
	%m/m	0.9	0.0	0.2	—

Wed Aug 18 11:30am	Labor price index Sa	3Q09	4Q09	1Q10	2Q10
	%q/q	0.7	0.6	0.9	<u>1.0</u>
	%oya	3.6	2.9	3.0	<u>3.2</u>

### Review of past week's data

#### ANZ job advertisements

	May	Jun	Jul	
%m/m sa	2.7	2.7	2.8	<u>0.8</u> 1.3

#### Housing finance approvals: owner occupiers

Number of loans, seasonally adjusted

	Apr	May	Jun	
%m/m	-1.5	-1.9	1.9	3.0 <u>-2.0</u> -3.9
%oya	-25.0	-26.3	-24.4	-25.0 <u>-26.2</u> -28.6

#### NAB monthly business survey

% balance, sa

	May	Jun	Jul	
Business confidence	5	4	—	2

#### WMI consumer confidence survey

100=neutral, sa

	Jun	Jul	Aug	
%m/m	-5.7	11.1	<u>3.5</u>	5.4

#### Labor force

Sa

	May	Jun	Jul	
Unemployment rate (%)	5.1	5.2	5.1	<u>5.2</u> 5.3
Employed (000 m/m)	23	15	46	37 <u>20</u> 23
Participation rate (%)	65.1	65.2	65.2	65.3 <u>65.2</u> 65.5

## New Zealand:

### Data releases and forecasts

Week of August 9 - 13

Thu Aug 19 8:45am	Producer price index Nsa	3Q09	4Q09	1Q10	2Q10
	Inputs (%q/q)	-1.1	0.4	1.3	<u>-0.1</u>
	Outputs (%q/q)	-1.4	-0.1	1.8	<u>-0.2</u>

Fri Aug 20 10:45am	Visitor arrivals Nsa	Apr	May	Jun	Jul
	Total (%m/m)	-1.6	1.1	0.3	—

Fri Aug 20 10:45am	Net permanent immigration Not seasonally adjusted	Apr	May	Jun	Jul
	Monthly (000s)	-0.6	0.3	-0.7	—
	12-month sum (000s)	20.0	18.0	16.5	—

Fri Aug 20 3:00pm	Credit card spending % change	Apr	May	Jun	Jul
	%oya	0.8	3.4	4.5	—

### Review of past week's data

#### QVNZ house prices

% , median	May	Jun	Jul	
%oya	5.6	5.2	—	4.1

#### Business PMI

	May	Jun	Jul	
Index, sa	54.4	54.3	56.2	55.9 — 49.9
%oya sa	23.5	20.1	—	0.8

#### Retail trade

	Apr	May	Jun	
%m/m sa	-0.3	0.4	<u>0.5</u>	0.9
%oya sa	2.4	2.3	<u>2.8</u>	3.2

#### Retail trade ex. inflation

	4Q09	1Q10	2Q10	
%q/q sa	0.9	0.2	<u>0.2</u>	1.3

## Greater China

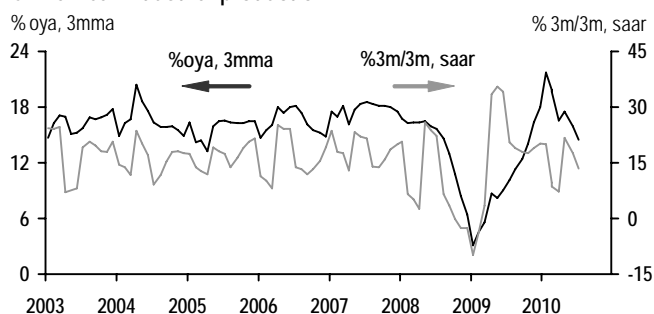
- **China: July macro indicators suggest that the moderation in growth momentum continued**
- **Hong Kong: 2Q GDP rose by 6.5% from the previous year, in line with our expectations**
- **Taiwan: July exports came in better than expected; shipments to developed markets still holding up**

The Chinese economy has shown moderating growth since 2Q, and July's indicators suggest that the steady slowdown in momentum continued through the current quarter. Industrial activity and fixed investment growth eased steadily on the back of monetary normalization and policy curbs targeting the property market and local government investment activities. On the production side, IP rose at 13.4%oya in July (J.P. Morgan: 13.5%; consensus: 13.4%), compared to 13.7%oya growth in June, translating to a modest gain of 0.5% m/m sa—the underlying sequential trend increased 13.4% 3m/3m saar through July.

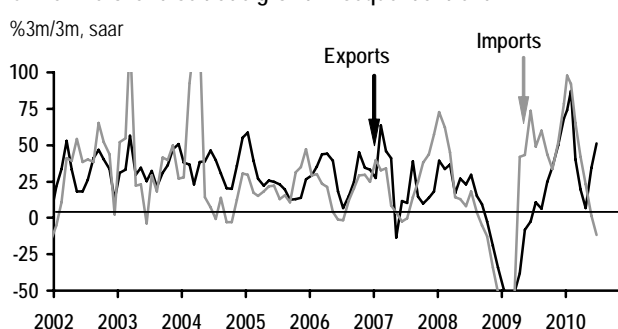
On the demand side, China's July exports were in line with our forecast, rising 38.1%oya, which translates to a modest decline of 1.2% m/m sa after the 1.0% m/m fall in June and the sharp 12.8% m/m spike in May. Looking at the monthly volatility, the underlying sequential trend in exports rose at a solid pace of 50.9% 3m/3m saar in July. Meanwhile, imports came in a touch weaker than expected, rising 22.7%oya in July—this translated to a decrease of 4.7% m/m sa, continuing the 3.9% m/m fall in June, with the sequential trend now down 12.1% 3m/3m saar. The July trade report also highlighted that the pace of broad-based sequential growth in major export product categories, including higher-end tech products as well as lower-end consumer goods, has remained largely intact over recent months. Details in exports by country revealed that the underlying growth trend in shipments to the US continued to outperform (up 95.8% 3m/3m saar by July), followed by Europe and Japan. Meanwhile, export growth to Emerging Asia has generally underperformed in recent months.

Fixed investment cooled to 24.9%oya year-to-date in July, which we believe puts growth for the month at 22.3%oya. In the details, real estate investment growth stabilized, rising 37.2%oya ytd in July. But the pace of growth in infrastructure investment, which jumped sharply last year on the back of the government's aggressive fiscal stimulus, has begun to slow. In particular, the pace of railway investment growth declined in recent months, rising 21.5%oya in January-July, compared to the 67.5%oya growth in full-year 2009. Elsewhere, nominal retail sales grew 17.9%oya in

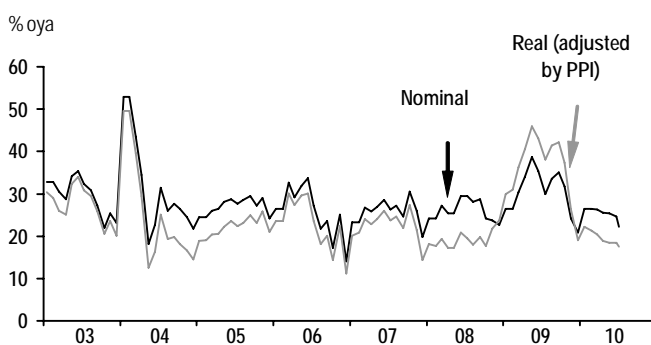
China: real industrial production



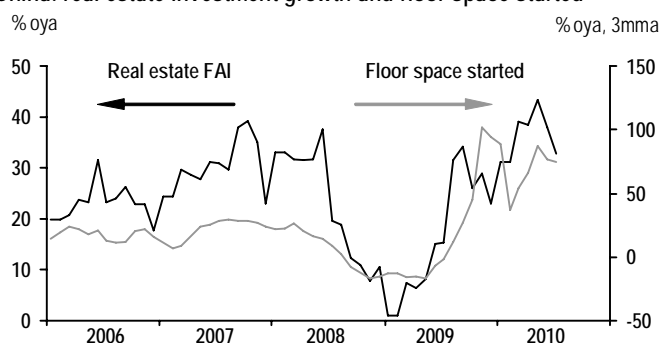
China: merchandise trade growth—sequential trend



China: fixed asset investment



China: real estate investment growth and floor space started



July, compared to 18.3%oya in June. Seasonally adjusted, underlying retail sales picked up to 1.4% m/m sa in July. Upon closer inspection, urban area retail sales increased 18.2%oya in July, while rural area retail sales rose

16.1%oya. The latest data suggest that auto sales growth has moderated markedly, rising 27.6%oya in July, compared to 37.1%oya ytd growth during the January-June period.

July CPI inflation printed at 3.3%oya, translating to a rise of 0.3%m/m sa. Food CPI rose 6.8%oya (up 0.9%m/m sa) in July, reflecting the impact of floods and heavy rain in some parts of the country during the month. Nonfood prices ticked up 1.6%oya, though they remained flat in %m/m sa terms. In addition, PPI advanced 4.8%oya in July, compared to the 6.4%oya rise in June. Seasonally adjusted, PPI fell notably, by 1.2%m/m sa in July, with the sequential trend down to 2.2%3m/3m saar. Among the major PPI categories, PPI for mining rose 15.2%oya in July, and PPI for industrial raw materials was up 8.7%oya. Meanwhile, PPI for consumer goods rose moderately, at 2.1%oya in July.

## Money supply and loan growth eased

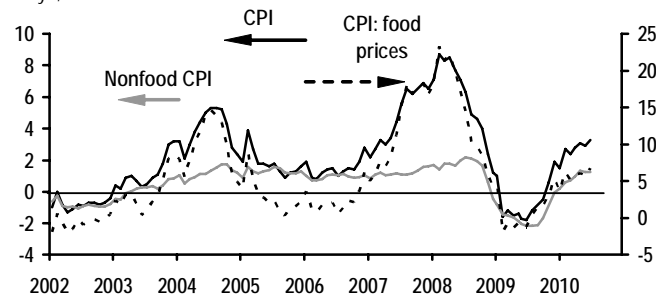
M2 money supply increased 17.6%oya in July, while new loan creation eased modestly to RMB532.8 billion as opposed to RMB603.4 billion in June. Seasonally adjusted, the pace of monthly gain in M2 has slowed substantially, rising 0.4%m/m in July, with the pace of gain in the sequential trend moderating to 13.1%3m/3m saar. New loan creation cooled, too, coming in at RMB532.8 billion in July. Behind the headline numbers, new household loans stood at RMB172.0 billion in July (compared to RMB231.0 billion the previous month), likely held back by slowing mortgage loan growth. Moreover, new medium-to-long-term corporate loans came in at RMB327.4 billion in July (down slightly from RMB335.4 billion in June). In addition, new short-term corporate loans totaled RMB52.7 billion in July compared to RMB152.8 billion in June. Finally, the outstanding level of bill discounting continued to fall, dropping RMB43.6 billion in July.

## Economic and policy outlook

Bearing in mind the continuing impact of monetary policy normalization in China and policy actions targeting the property market and local government investment activities, in conjunction with the outlook for a moderate pace of developed market growth, we expect China's industrial activities to slow in coming months. We estimate real GDP growth coming in at around an 8.2%-8.6%q/q saar pace during 2H10, compared to the strong double-digit pace of increase seen in previous quarters. Indeed, our full-year 2010 GDP growth forecast stands at 10.0%. In our view, risks to the growth outlook for 2H10 come from a weaker-than-expected external demand environment and further inventory correction in China's industrial sector.

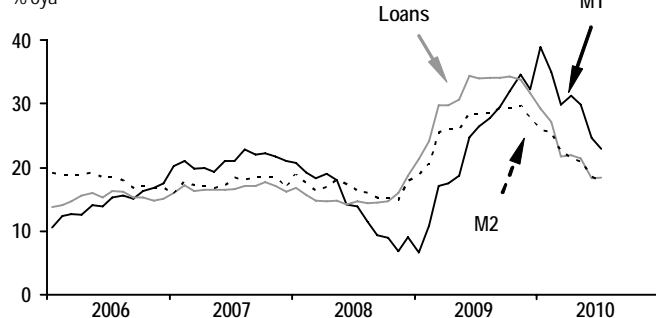
### China: headline CPI, food prices, and nonfood CPI inflation

%oya, both scales



### China: money supply and loan growth

% oya



In terms of policy, we believe the government is keen to set macro policies intended to deliver solid growth. In particular, Chinese policymakers continue to be concerned about the sustainability of the global recovery and the prospects for China's export sector. Overall, moderating growth momentum and signals that input cost pressures have eased in recent months (as demonstrated by the recent fall in PPI) will keep the PBoC on hold until 4Q10, despite the fact that headline CPI inflation has again breached the 3%oya mark. We expect the PBoC to raise the benchmark policy rate once this year, by 27bp in 4Q, when it becomes more confident about the global recovery and in order to calm inflation expectations. At the same time, we believe a major near-term reversal of the sector-specific tightening measures implemented since early this year is unlikely. With regard to currency, our year-end CNY/USD target is 6.6.

## Hong Kong: solid GDP growth in 2Q

Hong Kong's 2Q GDP expanded at a solid pace of 5.7%q/q saar, following a revised gain of 8.7%q/q saar in 4Q09 (previously 10.0%q/q saar). This leaves the rate of over-year-ago real GDP growth at 6.5% (J.P. Morgan: 6.4%; consensus: 6.3%), which is in line with our forecast. In seasonally adjusted terms, private consumption expanded significantly, posting solid growth of 6.1%q/q saar compared to 2.4%q/q saar in 1Q. Export/import sectors moderated



from the strong growth in 1Q, mainly driven by the slow-down in services exports (+3.2%q/q saar in 2Q vs. +29.6%q/q saar in 1Q).

Going forward, our global economic team expects consumer demand to decelerate worldwide, given the recent softening in growth momentum observed in Hong Kong's two major trading partners—the US and mainland China. We believe it is likely that Hong Kong's export sector will continue to see the growth trend slow into 2H10. Though the RMB trade settlement is expected to be beneficial for Hong Kong's financial and trade-related services in the long run, the agreement is likely to have limited impact on existing trade flows or to trigger more service opportunities for commercial banks in the near term given that the size of the RMB deposit base is still low.

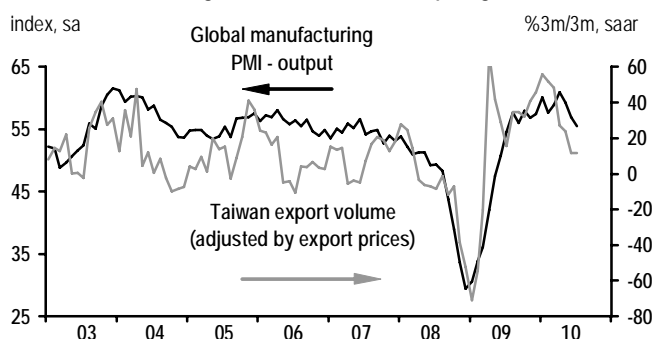
On the domestic front, rising uncertainty over the external environment could affect household sentiment, therefore impacting private consumption. However, tourism inflows have remained strong thanks to the steady influx from mainland China. HKTb expects the positive trend to maintain its steady upward trajectory, and further increase by 20%–25% in 2H10, thereby providing favorable conditions for Hong Kong's retail business in the latter half of this year. In all, given the robust growth momentum in the first half of the year, the government has revised up its 2010 growth forecast to 5%–6% (previously 4%–5%). Our growth forecast stands at 6.8%o/a for 2010.

## Taiwan: July exports beat expectations

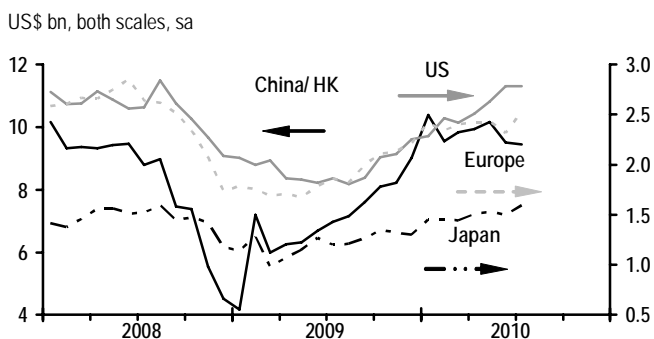
Taiwan's July export growth came in better than expected at 38.5%o/a (J.P. Morgan: 32.5%; consensus: 31.0%). Seasonally adjusted, July exports rose 4.5% m/m following a 6.2% m/m decline in June, with the sequential growth trend stabilizing at 4.6% 3m/3m saar by July, having weakened sharply in recent months from the strong 67.2% 3m/3m saar pace in March. Adjusting for price effects, exports rose in volume terms, up 2.2% m/m sa in July after falling 4.1% m/m sa a month earlier, with the sequential growth trend stabilizing at 11.7% 3m/3m saar. Meanwhile, imports continued their heady pace, up 42.7%o/a in July—this translates to a rise of 2.2% m/m sa in July after a fall of 5.9% m/m sa in June.

Looking at the external environment, our global team has noted that the global manufacturing cycle has been decelerating into midyear following the boom of the past year. The waning contribution to growth from the inventory cycle suggests final demand will be the major determinant of factory output. Overall, J.P. Morgan expects global manufacturing output will decelerate from the strong 10%–12% an-

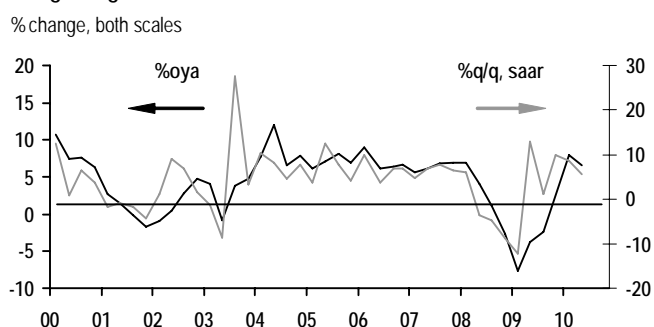
## Global manufacturing PMI and Taiwan real export growth



## Taiwan: exports by destination



## Hong Kong: Real GDP



nualized gains through 1H10 to a still-solid pace of 4%–6% in 2H10. Taiwan's recent trade figures have been consistent with the global theme of a moderating manufacturing cycle. Specifically, Taiwan's July trade report highlighted that shipments to China/Hong Kong seemed to gradually bottom out (edging down 0.7% m/m sa in July after falling notably at 6.5% m/m sa in June), while the sequential trend in shipments to developed markets—including the US (flat in % m/m sa terms in July)—held up rather well, despite growing uncertainty over the global economic outlook.

**China:****Data releases and forecasts**

Week of August 16 - 20

No data released.

**Review of past week's data****Monetary aggregates**

%oya	May	Jun	Jul
M2	21.0	18.5	<u>18.7</u> 17.6
Bank lending	21.5	18.2	— 18.4

**Foreign direct investment**

US\$ bn	May	Jun	Jul
Utilized FDI	8.1	12.5	—
%oya	27.5	39.6	—
%oya ytd	14.3	19.6	—

**Merchandise trade (Aug 11)**

US\$ bn	May	Jun	Jul
Balance	19.5	20.0	<u>22.0</u> 28.7
Exports	131.8	137.4	<u>145.1</u> 145.5
%oya	48.5	43.9	<u>37.7</u> 38.1
Imports	112.2	117.4	<u>123.1</u> 116.8
%oya	48.3	34.1	<u>29.8</u> 22.7

**Consumer prices (Aug 11)**

% change	May	Jun	Jul
%oya	3.1	2.9	<u>3.2</u> 3.3
%m/m sa	0.3	-0.1	<u>0.3</u>

**Producer prices (Aug 11)**

%oya	May	Jun	Jul
Producer (NBS)	7.1	6.4	<u>5.9</u> 4.8
Producer (PBoC)	7.1	6.6	—

**Fixed investment (Aug 11)**

% change	May	Jun	Jul
Fixed investment	25.4	24.6	<u>24.7</u> 22.3
%oya	25.9	25.5	<u>25.4</u> 24.9
%oya, ytd	38.2	38.1	— 37.2
Real estate	38.2	38.1	—
%oya, ytd	24.8	24.9	—
Manufacturing			
%oya, ytd			

**Retail sales (Aug 11)**

% change	May	Jun	Jul
%oya	18.7	18.3	<u>18.1</u> 17.9
%m/m sa	1.7	1.5	<u>1.6</u> 1.4

**Industrial production (Aug 11)**

% change	May	Jun	Jul
%oya	16.5	13.7	<u>13.5</u> 13.4
%m/m sa	0.3	-0.2	<u>0.8</u> 0.5

**Hong Kong:****Data releases and forecasts**

Week of August 16 - 20

Tue Aug 17 4:30pm	Labor market survey	Apr	May	Jun	Jul
	Sa, 3mma				
	Unemployment rate	4.4	4.6	4.6	<u>4.6</u>
	% avg				
	Employed	1.4	-13.7	2.7	<u>5.2</u>
	ch, m/m, 000 persons				
Fri Aug 20 4:30pm	Consumer prices	Apr	May	Jun	Jul
	%change				
	%oya	2.4	2.5	2.8	<u>2.9</u>
	%m/m sa	0.4	-0.2	0.2	<u>0.2</u>

**Review of past week's data****Real GDP (Aug 11)**

	4Q09	1Q10	2Q10
%oya	2.5	8.0	<u>6.4</u> 6.5
%q/q saar	10.0	8.7	<u>4.3</u> 5.7

**Taiwan:****Data releases and forecasts**

Week of August 16 - 20

Thu Aug 19 4:30pm	Real GDP	3Q09	4Q09	1Q10	2Q10
	% change				
	% oya	-1.0	9.2	13.3	<u>10.1</u>
	%q/q saar	11.2	16.7	11.3	<u>2.0</u>
Fri Aug 20 4:00pm	Export orders	Apr	May	Jun	Jul
	% change				
	Oya	35.1	34.0	22.5	<u>22.8</u>
	M/m sa	-1.6	1.4	-2.3	<u>0.3</u>

**Review of past week's data****External trade (Aug 9)**

US\$ bn	May	Jun	Jul
Balance	3.3	1.4	<u>1.2</u> 2.2
Exports	25.5	22.7	<u>22.9</u> 23.9
%oya	57.9	34.1	<u>32.5</u> 38.5

## Korea

- **Bank of Korea stays on hold with hawkish comments**
- **Jobless rate rose further in July, but with improved details**
- **Producer prices rise, but only due to seasonal factors**

The Bank of Korea left the base rate on hold at 2.25% this week after hiking 25bp in July. In the comments, the bank increased its level of caution regarding G-2 risks, albeit only slightly, and continued to emphasize its objective to maintain longer-term price stability. Indeed, the MPC statement adopted a more hawkish tone in its wording on future monetary policy direction, as confirmed by the Governor in his press conference; the change was intended to highlight the importance of price stability amid normalizing growth conditions in the domestic economy. The BoK continues to be wary of new uncertainties arising in global growth conditions. Although the governor said that G-2 risks are still not significant enough to change the BoK's extant forecast for Korea's growth, he admitted that the global environment is still very fluid—we believe this potentially shifts the monetary policy horizon from a medium-term to a near-term focus.

Accordingly, we think the BoK will continue tightening, but at a more gradual pace, with two further 25bp hikes—one in early 4Q10 and one in 1Q11. However, given that the BoK has reiterated its goal of ensuring price stability, while discounting implications of the fact that historically, it has never hiked rates in the month of the Full Moon Festival holiday (which occurs in September this year), we do not rule out the possibility that the next rate hike could come as early as next month. Of course, this will require strong tailwinds in the form of hard data beating expectations in the coming four weeks and the return of global appetite for risk.

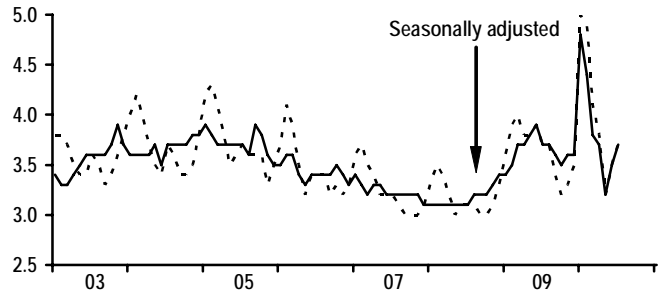
### Employment rebounded in July

The unemployment rate edged up to 3.7% in July from 3.5% the month prior. Seasonally adjusted, the jobless rate moved up for the second straight month after bottoming at 3.2% in May when temporary hires in public sector programs and the election campaign boosted overall job gains.

However, the details of the employment report improved in July, which was in line with our expectation. The rise in July's jobless rate was mainly due to an increase in the labor force that exceeded employment growth. Seasonally adjusted, the labor force grew 158,000 (or 0.64% m/m sa) in the month, its fourth monthly rise in a row and its most

### Unemployment rate

% of total labor force



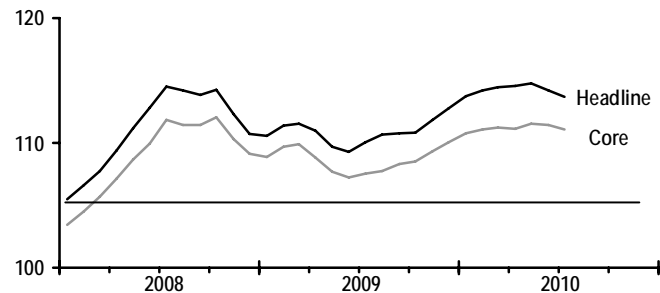
### Labor force and employment

%m/m, sa



### Producer prices: headline vs. core

2005=100, sa by J.P. Morgan



rapid growth pace since June 2009. Employment gains were not quite so robust, coming in at 105,000 (0.44% m/m sa). The gains were seen as payback for the previous month's fall of 76,000 and represented a return to the more moderate pace seen in the April-May period. Looking at the monthly volatility indicators, labor force growth appears to be accelerating while employment gains have moderated since mid-2Q10 (second chart).

### Pipeline price pressure remained subdued

Producer prices rose 0.1% m/m nsa in July, after a decline of 0.3% in June. Both goods and services prices edged up, largely due to seasonal effects. Seasonally adjusted by J.P. Morgan, PPI fell for the second consecutive month, re-

versing the trend of the previous four months, and staying at the same level as in January (third chart). Goods prices fell 0.5% m/m sa in July, about the same pace as in June, with the fall in industrial goods prices more than offsetting the rise in agricultural and non-energy commodity prices. Services prices moved down in July, too, but at a milder pace. We expect PPI to rebound modestly later this year, with some public utility charges scheduled to rise in the August-October period, compounded by the domestic pass-through of KRW weakness in recent months. This should be more apparent in over-year-ago comparisons due to the low base last year. Nevertheless, the continued output gap in developed economies will keep constraining global industrial goods prices, providing a partial offset to domestic price pressures.

## Data releases and forecasts

Week of August 16 - 20

Mon Aug 16 6:00am	Import and export prices				
	%oya	Apr	May	Jun	Jul
	Export prices	-6.7	0.4	1.5	<u>1.2</u>
	Import prices	5.1	11.3	8.0	<u>7.5</u>

On contractual currency terms, both import and export prices should have fallen further in July. However, KRW weakness likely offset this, so the trend should be only partially reflected in local currency terms. Accordingly, import as well as export prices in local currency terms likely edged up on a m/m basis, slowing the pace of deceleration in their over-year-ago comparisons.

Mon	Stage of processing price index				
Aug 15	% change				
6:00am		Mar	Apr	May	Jun
	%oya	4.2	7.4	6.4	5.2

SPPI should have decelerated further, with industrial good prices likely down on a seasonally adjusted basis.

Week of Aug 16	Bankruptcy filings				
	Apr	May	Jun	Jul	
	Bankruptcy filings (No.)	125	120	122	<u>140</u>
	Dishonored bill ratio	0.03	0.03	0.04	<u>0.03</u>

## Review of past week's data

Producer prices (Aug 9)

% change	May	Jun	Jul	
%oya	4.6	4.6	<u>4.3</u>	3.4

Core PPI dipped 0.4% m/m sa in July, following a 0.5% decline in June, but rose 3.3% oya. See main story.

Unemployment rate (Aug 11)

% of total labor force				
	May	Jun	Jul	
Seasonally adjusted	3.2	3.5	<u>3.5</u>	3.7
Not adjusted	3.2	3.5	<u>3.5</u>	3.7

See main story.

Monetary aggregates (Aug 11)

%oya, monthly average				
	Apr	May	Jun	
M2	9.4	9.3	<u>9.4</u>	9.7
Lf	9.0	8.9	<u>9.0</u>	9.3

On a seasonally adjusted trend basis, M2 rose 0.9% m/m sa in June, accelerating from 0.5% in May, on the back of higher interest rates on bank deposits shifting portfolios away from longer-term financial products. LF increased 0.8% m/m sa, up slightly from 0.7% in May. Based on end-of-month data, much of the gain in M2 and LF was concentrated in the earlier part of the month.

Housing prices (Aug 6)

% change from previous week, apartment prices only				
	Week of Jul 19	Jul 26	Aug 2	
	0.0	0.0	—	0.0

## BoK Watch

### • MPC comment slightly more hawkish than in July

Local bond markets had stayed cautious until early this week, with consensus split over the timing of rate hike action (we had consistently called for a combination of no rate action and hawkish comments). Following the BoK's decision on August 12, Korean bond markets rallied, with only a minor correction arising from the Governor's slightly more hawkish tone. Also see first page.

Interest rates

% p.a.	Jul 22	Jul 29	Aug 5	Aug 12
Overnight call	2.27	2.28	2.28	2.27
Three-month CD fixing	2.63	2.63	2.63	2.63
One-year MSB	3.15	3.14	3.20	3.19
Three-year treasury bond 3.82	3.80	3.87	3.76	
Three-year corporate bond 4.76	4.75	4.80	4.70	

Deposit changes at deposit money banks

KRW tn				
	Apr	May	Jun	Jul
Total deposits	9.6	23.4	14.2	7.6
Demand	1.0	1.3	3.6	0.1
Time and savings	8.6	22.0	10.6	7.5

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

- Vietnam's economy rebounded steadily last quarter and growth in 2H10 should continue to be solid
- Inflation is slowing quickly and trade details are more encouraging than the wider headline deficit suggests
- Fitch's rating downgrade was not a surprise and is a lagging indicator; we think the economy is improving

After a surprisingly weak first-quarter GDP print, growth rebounded in 2Q on the back of better manufacturing and construction activity. While most of the region is expected to slow notably in 2H, we expect growth to be more resilient in Vietnam given the country's much lower reliance on global electronics demand and more aggressive policy stance. Thus, though growth will likely moderate from the robust 2Q print, Vietnam's economy should continue to expand at a solid rate in 2H10.

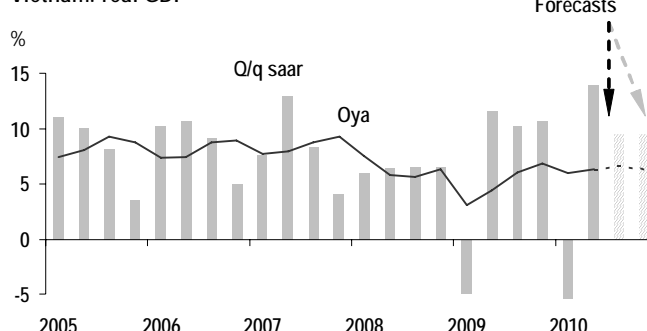
The slowdown in inflation has become more pronounced, and we expect price pressures to continue to ease in coming quarters. This reflects our view that food and commodity prices will remain stable at least into 1H11, allowing %oya inflation to roll off even though credit growth may accelerate and GDP growth should be solid. Despite the improvement in inflation, the trade deficit widened in July after a few subdued months. However, the widening in the deficit reflected volatile gold exports and the oil trade. Excluding these products, the trade deficit peaked several months ago and has since narrowed.

Against this backdrop, Fitch's rating downgrade was not a surprise, and it may be followed by downgrades from other major ratings agencies. Nevertheless, these downgrades are lagging indicators. Though we agree with Fitch's action based on long-term fundamentals, the near-term view is turning more positive. Indeed, neither credit markets nor the offshore currency market suggests any reason for greater concern right now.

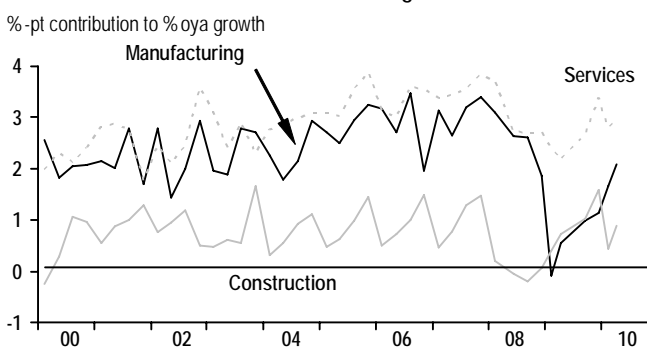
### Economy on a solid footing

Vietnam's GDP jumped 13.9%q/q saar in 2Q10, leaving it up 6.4%oya, or 6.2%oya ytd as the government prefers to report it. The strong sequential rebound came on the back of a soft 1Q print with all major sectors—construction, manufacturing, and services—recovering. Manufacturing (26% of GDP) surged almost 30% annualized while services (42% of GDP) grew about 12%. Construction (8% of

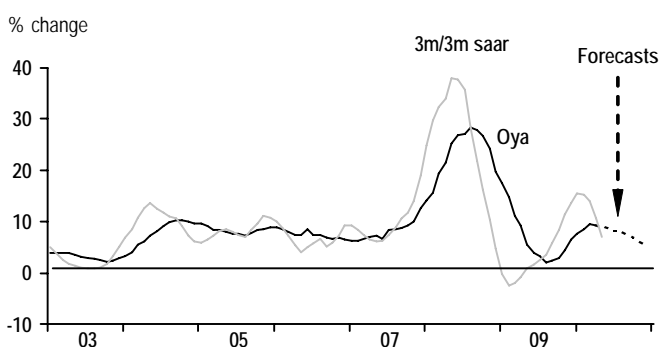
Vietnam: real GDP



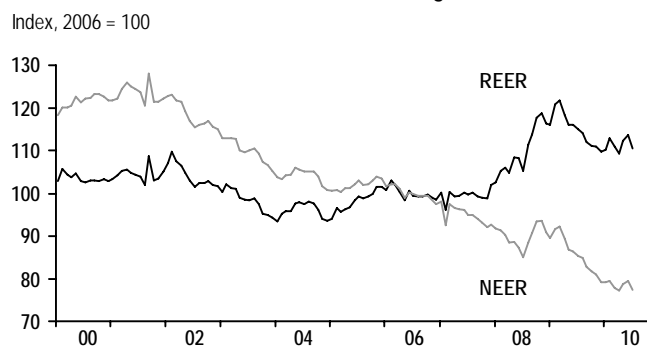
Vietnam: contributions to real economic growth



Vietnam: CPI inflation



Vietnam: real and nominal effective exchange rates





GDP) was also strong, expanding 34%, with only agriculture (17% of GDP) appearing soft. In terms of contributions to %oya growth, services added 2.9%-pts, manufacturing 2.1%-pts, construction 0.9%-pts, and agriculture 0.7%-pts.

The government will likely boost credit growth and keep monetary policy flexible in 2H to try to achieve its 6.5% annual target after realizing only 6.2% in 1H. Such a target assumes above-trend sequential growth in 2H. Consequently, credit growth is likely to pick up after a very weak 1Q and somewhat soft 2Q. Reportedly, credit growth was ahead only 10.5% in 1H compared to a full-year target of 25%. We are forecasting slightly slower GDP growth of 9.5%q/q saar in 2H10. Even this strong rate would leave annual growth at 6.3%, slightly shy of the official target.

### Cyclical indicators improving

Consumer prices rose 8.2%oya in July, marking the fourth month of moderation since the peak at 9.4% in March. Given the large food weighting (40%) in the CPI basket, and the fact that sequential trend inflation has slowed notably and that core inflation (ex. food and energy) has also begun to cool, we expect inflation to continue to ease. By December, we believe inflation could be below 6%oya.

Although the deceleration in inflation has been consistent, improvement in the trade deficit has been choppy. In July, the deficit widened to US\$1.2 billion after two months of sub-US\$1 billion prints. However, much of the movement in the headline trade balance reflects oil exports and imports as well as gold. If these volatile products are excluded, the “core” trade deficit peaked at US\$1.6 billion in May and had nearly halved to US\$0.9 billion in July. Moreover, even when oil and gold trade are included, the 12-month rolling deficit has narrowed about 7% in the past three months.

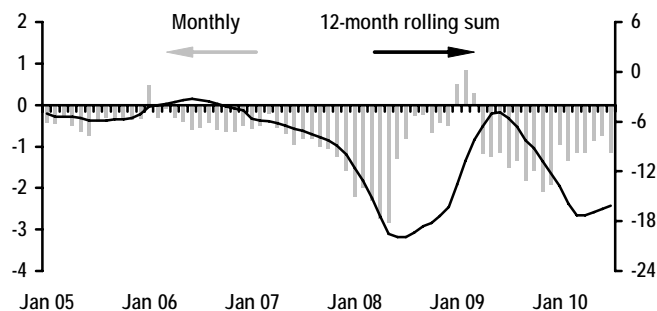
### Fitch downgrade is a lagging indicator

Fitch downgraded Vietnam’s sovereign credit rating to B+ from BB- late last month and changed the outlook to stable from negative. The agency had placed Vietnam on rating watch negative in March.

We agree that Vietnam should be downgraded as it is currently rated alongside much stronger credits such as Indonesia and the Philippines; we have been warning of a downgrade for over a year now. However, the rating change did come at an unusual time since cyclical indicators are improving. Inflation is slowing, FX reserve levels are reportedly rising, and the BoP and exchange rate are stable. Well-behaved inflation remains key to continued macroeconomic stability—high inflation hurts confidence

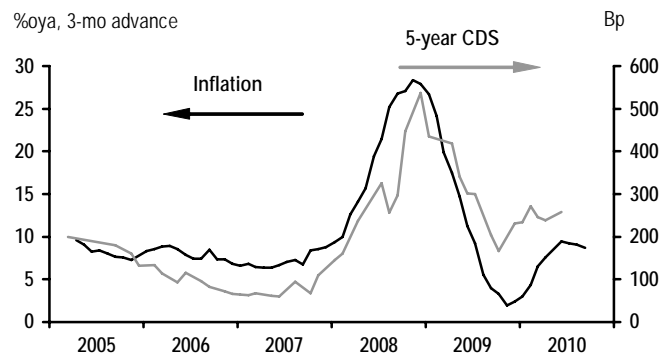
#### Vietnam: trade balance

US\$ bn, both scales



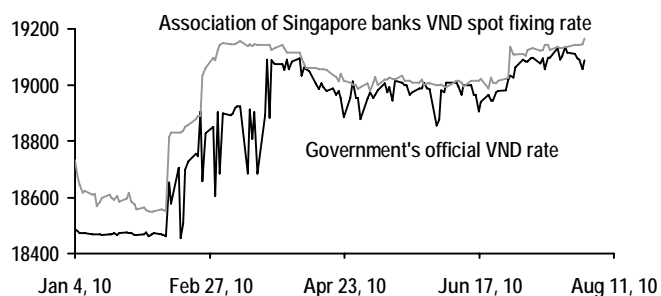
#### Vietnam: CPI inflation and 5-year CDS

%oya, 3-mo advance



#### Vietnam: official versus offshore dong exchange rates

Dong per US\$



in the dong and leads to a large, primarily locally led, capital outflow. In the past, lower inflation has stemmed capital outflow and led to a resumption in inflows. Though not a panacea for all of Vietnam’s challenges, lower inflation should provide the authorities with breathing room to boost growth and to rebuild FX reserve levels. In recent years, inflation has been the macroeconomic indicator most closely correlated with CDS movements. Thus, while we do think further downgrades are likely, markets do not seem concerned with the outlook, and we view any rating changes as overdue lagging indicators rather than new information about the future.

## Indonesia:

### Data releases and forecasts

Week of August 16 - 20

No data releases.

### Review of past week's data

No data released.

## Malaysia:

### Data releases and forecasts

Week of August 16 - 20

Wed Aug 18 5:00pm	<b>Consumer prices</b> Percent change				
		Apr	May	Jun	Jul
	Oya	1.5	1.6	1.7	<u>2.4</u>
	M/m sa	0.1	-0.3	-0.2	<u>0.3</u>

Inflation is expected to have ticked up slightly on account of the recent increase in energy and food prices.

Wed Aug 18 5:00pm	<b>Real GDP</b> Percent				
		3Q09	4Q09	1Q10	2Q10
	Oya	-1.2	4.4	10.1	<u>8.6</u>
	Q/q saar	16.7	8.2	5.0	<u>5.0</u>

Growth is expected to have been modest in 2Q10 with further moderation expected in 2H10.

### Review of past week's data

#### Industrial production (Aug 10)

%oya		Apr	May	Jun	
Total		10.6	12.6	<u>13.4</u>	9.4
%m/m sa		-0.4	1.6	<u>0.2</u>	-1.3

June IP dipped 1.3% m/m sa after a similar-sized gain in the previous month, leaving the headline growth rate lower than expected at 9.4% oya (consensus: 11.8%). In trend sequential terms, IP rose 8.7% 3m/3m saar compared to 20.3% in May. In terms of the subsectors, manufacturing was the largest drag, falling 3.1% m/m sa. Electricity also fell, though more modestly, while mining output was just about flat in June. All three slowed in sequential trend terms with electricity contracting slightly.

## Philippines:

### Data releases and forecasts

Week of August 16 - 20

During the week	<b>Government budget</b> Pesos bn				
		Apr	May	Jun	Jul
	Balance	2.6	-30.5	-34.6	—
	Revenue	124.5	109.7	92.1	—
	Expenditure	121.9	140.2	126.7	—

Mon Aug 16 10:45am	<b>OFW worker remittances</b> Percent change				
		Mar	Apr	May	Jun
	Oya	5.6	5.4	6.5	<u>4.4</u>
	M/m sa	-1.9	1.4	1.6	<u>1.5</u>

We expect remittances to rise modestly due to seasonal inflows to the Philippines related to education expenses around this time of year.

### Review of past week's data

#### Merchandise trade (Aug 10)

\$ bn nsa		Apr	May	Jun	
Exports		3.6	4.2	<u>4.2</u>	
%oya		28.2	37.3	<u>23.7</u>	

Filipino exports rose 2.3% m/m sa in June after a strong gain in May. This left exports stronger than expected at 33.4% oya. Despite the strong monthly and %oya gain, sequential trend export growth moderated to 10.5% 3m/3m saar, which looks likely to be a near-term bottom.

Export performance was mixed in the details. Electronic exports ticked up 3.3% m/m sa and were ahead a stellar 49.1% oya while nonelectronic exports fell 4.3% m/m sa and were up only 12.5% oya. In sequential trend terms, both categories softened, but electronics were still up a solid 37.1% 3m/3m saar while nonelectronics contracted 28.6%.

## Singapore:

### Data releases and forecast

Week of August 16 - 20

Tue Aug 17 1:00pm	<b>Merchandise trade</b> US\$ bn, nsa				
		Apr	May	Jun	Jul
	Trade balance	2.9	3.8	2.5	<u>3.1</u>
	Exports	29.3	27.6	29.3	<u>31.1</u>
	Non-oil domestic (NODX)	10.6	9.7	10.4	<u>11.0</u>
	%m/m sa, \$ terms	3.9	-3.3	3.6	<u>0.7</u>
	%oya, \$ terms	41.5	29.8	33.1	<u>28.0</u>

NODX likely edged up in July after a modest gain in June. However, we expect NODX growth to moderate later this year, in line with softening global demand.

## Review of past week's data

### Real GDP (Aug 10)

	4Q09	1Q10	2Q10
Oya	3.8	15.5 16.9	17.5 18.8
Q/q saar	-1.0	46.0 45.7	10.0 24.0

Singapore's final 2Q GDP print showed the economy surging 24% q/q saar in 2Q, a tad slower than the advance 26% estimate. This left growth up 18.8%. Growth in 2Q was broad-based with domestic demand and net exports contributing. The one area of weakness was transport equipment, a very volatile series, which dragged down fixed investment. In terms of contributions to %oya growth, domestic demand added 8.7%-points while net exports provided 10%-points. Growth was also broad-based across industry, with manufacturing contributing 10.5%-points, services 7.2%-points, and construction 0.5%-point.

MTI did not change its 2010 GDP forecast of 13%-15% following the release, and its statement reiterated that growth is expected to slow sharply in 2H from the blistering 1H rate of 17.9% oya. We also expect much slower growth in 2H and we anticipate the economy will contract on a sequential basis this quarter due to the volatile biomedical cluster (though we currently have the economy skirting a technical recession, which the MTI noted was a possibility). Even with a sharp slowdown expected in 2H, we expect full-year growth to be 15.5% this year before cooling to 4.5% next year.

After the GDP release, MAS Deputy Managing Director Ong Chong Tee made several comments. He noted that wheat prices have not affected the inflation forecast, which remains at 2.5% to 3.5%, and that the employment outlook remains healthy. He also stated that current policy remains appropriate and that the exchange rate is too blunt of a tool to manage property prices. In any case, the MAS does not see any danger of overheating in the property market, though it acknowledges interim pressures on residential property. Finally, Tee noted that capital inflows are not a concern right now and that the MAS is stress-testing Singaporean banks to ensure the safety and soundness of the financial system. These comments, taken with MTI's comments about the 2011 outlook, suggest that the MAS will maintain its modest and gradual appreciation stance in October as the economy is expected to continue expanding. However, we believe a shift to a more aggressive tightening approach is unlikely given the high degree of uncertainty about developed market growth in 2011.

## Retail sales (Aug 13)

### % change

	Apr	May	Jun
Oya	-4.7	-5.7	-3.7 -6.3
M/m sa	-3.6	-1.0	3.0 0.3

June retail sales volumes rose 0.3% m/m sa, leaving the over-year-ago rate down 6.3% oya. On a sequential trend basis, retail sales volumes contracted 27.7% 3m/3m saar following an almost equally weak 26.4% contraction in May. The market follows value rather than volumes, and on this basis retail sales fell 0.7% m/m sa and were down -4.9% oya (consensus: -3.4%).

Due to market rigidities from the COE auction process and the volatile nature of the motor vehicle index, we prefer to look at sales volumes ex autos to get a better sense of underlying consumer spending strength. Excluding autos, retail sales volumes were softer, falling 0.5% m/m sa. On a sequential trend basis, sales ex autos expanded modestly, up 1.5% 3m/3m saar in June compared to 5.1% in May.

Retail sales were weak last quarter even though private consumption grew 8.2% q/q saar in 2Q. In the past, the relationship between retail sales and private consumption has been weak, and especially with the 2Q GDP figure already released earlier this week, we do not expect the soft June retail sales print to elicit much reaction from the market.

## Thailand:

### Data releases and forecasts

Week of August 16 - 20

No data releases.

### Review of past week's data

No data released.

## Vietnam:

### Data releases and forecasts

Week of August 16 - 20

No data releases.

### Review of past week's data

No data released.

## Asia focus: gross portfolio capital inflows

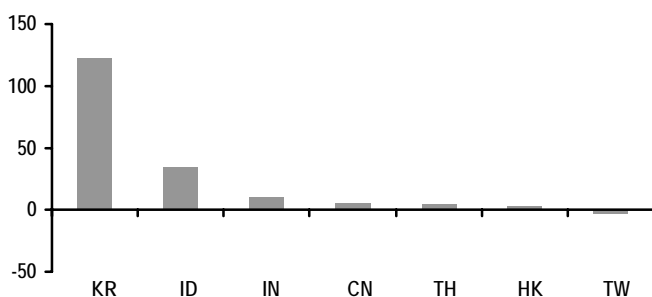
Overall portfolio flows in Emerging Asia have seen a transition in the past couple of decades. Before the Asian financial crisis in 1998, the region had seen net inflows of capital. Following the turmoil, it has experienced net outflows (first chart). There are two sides to this flow. The first is foreign holdings of portfolio assets in the region, reflected as an inflow of foreign capital and an increase on the liability side of a country's balance sheet. The other is domestic outflows, reflected as an increase in asset holdings of domestic investors, but recorded as an outflow in the balance of payments (BoP). Here we highlight the first of these, which focuses on the dynamics of gross foreign inflows.

A couple of observations are worth making from the data, which, given the BoP data limitations, do not encompass the whole region. The first is that total regional portfolio inflows have been positive except during 2008. Through 1Q10, total gross inflows were US\$34.5 billion, below the pace seen in 2007. Second, equity inflows tend to dominate. Here, the largest cumulative recipients of equity-related inflows tend to be in North Asia, namely China, Hong Kong, Taiwan, and India. Cumulatively, from 2005 to 1Q10, these four countries saw gross foreign inflows in the region of US\$324 billion (second chart). Only Korea saw outflows of foreign portfolio capital during the same period.

By contrast, bond-related inflows to the region have been lower, but have been somewhat more concentrated. The two major recipients of these flows have been Korea and Indonesia (chart below). Of note, Korea has seen gross cumulative inflows of US\$122.2 billion while Indonesia has seen inflows of US\$34.6 billion from 2005 through 1Q10 into its debt markets against total gross portfolio inflows of US\$41.3 billion over the same period.

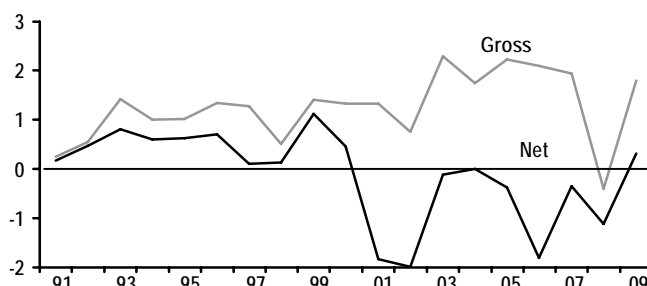
### Emerging Asia: gross debt portfolio inflows

US\$ bn, 2005-1Q10 cumulative, BoP terms



### Emerging Asia: portfolio investment

% of GDP, BoP terms



### Emerging Asia: gross foreign portfolio inflows

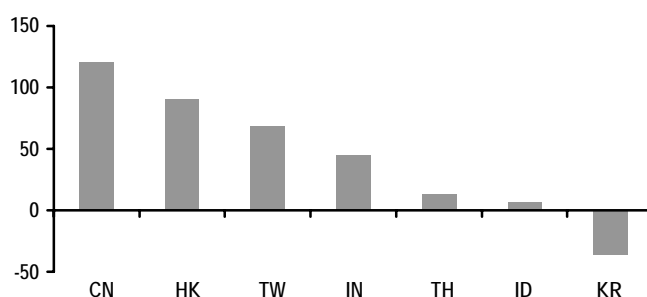
US\$ bn, BoP terms

	2005	2006	2007	2008	2009	1Q10	05-1Q10 <sup>1</sup>
<b>EM Asia</b>	<b>97.4</b>	<b>108.3</b>	<b>163.8</b>	<b>-54.1</b>	<b>135.8</b>	<b>34.5</b>	<b>485.8</b>
Equity	84.0	86.6	64.2	-39.3	97.2	15.9	308.5
Debt	13.5	21.7	99.7	-14.8	38.5	18.6	177.2
<b>China</b>	<b>21.2</b>	<b>42.9</b>	<b>21.0</b>	<b>9.9</b>	<b>28.8</b>	<b>1.6</b>	<b>125.4</b>
Equity	20.3	42.9	18.5	8.7	28.1	1.6	120.1
Debt	0.9	0.0	2.5	1.2	0.6	0.0	5.2
<b>Hong Kong</b>	<b>9.2</b>	<b>15.0</b>	<b>75.1</b>	<b>-12.8</b>	<b>4.9</b>	<b>1.9</b>	<b>93.3</b>
Equity	9.9	14.5	43.6	17.5	4.1	0.8	90.4
Debt	-0.7	0.6	31.4	-30.2	0.8	1.1	2.9
<b>India</b>	<b>9.5</b>	<b>8.8</b>	<b>19.6</b>	<b>-10.1</b>	<b>18.0</b>	<b>9.3</b>	<b>55.1</b>
Equity	10.6	7.9	17.3	-13.0	17.2	4.5	44.6
Debt	-1.1	0.9	2.3	2.9	0.8	4.7	10.5
<b>Indonesia</b>	<b>5.3</b>	<b>6.1</b>	<b>10.0</b>	<b>3.1</b>	<b>10.3</b>	<b>6.6</b>	<b>41.3</b>
Equity	-0.2	1.9	3.6	0.3	0.8	0.4	6.8
Debt	5.4	4.2	6.4	2.7	9.6	6.2	34.6
<b>Korea</b>	<b>14.1</b>	<b>8.1</b>	<b>30.4</b>	<b>-25.9</b>	<b>49.4</b>	<b>10.4</b>	<b>86.4</b>
Equity	3.3	-8.4	-28.7	-33.6	25.7	6.0	-35.8
Debt	10.8	16.4	59.1	7.7	23.7	4.4	122.2
<b>Taiwan</b>	<b>31.0</b>	<b>21.8</b>	<b>4.9</b>	<b>-15.8</b>	<b>21.4</b>	<b>2.6</b>	<b>66.0</b>
Equity	34.8	22.7	5.6	-15.4	19.4	1.7	68.8
Debt	-3.8	-0.8	-0.7	-0.4	1.9	0.9	-2.8
<b>Thailand</b>	<b>7.0</b>	<b>5.7</b>	<b>2.9</b>	<b>-2.5</b>	<b>3.0</b>	<b>2.2</b>	<b>18.3</b>
Equity	5.1	5.2	4.3	-3.8	1.9	0.9	13.6
Debt	1.9	0.5	-1.4	1.3	1.1	1.3	4.7

1. Total over period

### Emerging Asia: gross equity portfolio inflows

US\$ bn, 2005-1Q10 cumulative, BoP terms



## US economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
<b>16 Aug</b>  Empire State survey(8:30am) Aug <u>8.0</u> TIC data (9:00am) Jun NAHB survey (10:00am) Aug <u>15</u>	<b>17 Aug</b>  PPI (8:30am) Jul <u>0.1%</u> Core <u>0.2%</u> Housing starts (8:30am) Jul <u>540,000</u> Permits <u>569,000</u> Industrial production (9:15am) Jul <u>1.1%</u> Manufacturing <u>1.0%</u> Capacity utilization <u>75.0%</u>  Minneapolis Fed president Kocherlakota speaks on FOMC in Michigan (12:30pm)	<b>18 Aug</b>	<b>19 Aug</b>  Initial claims (8:30am) w/e prior Sat <u>475,000</u> Philadelphia Fed survey (10:00am) Aug <u>7.0</u> Leading indicators (10:00am) Jul  Announce 30-year (r) TIPS <u>\$7</u> bn Announce 2-year note <u>\$36</u> bn Announce 5-year note <u>\$34</u> bn Announce 7-year note <u>\$28</u> bn  St. Louis Fed president Bullard speaks on economy in Arkansas (12:30pm) Chicago Fed president Evans speaks to reporters (1:00pm)	<b>20 Aug</b>  Chicago Fed president Evans speaks to reporters (1:00pm)
<b>23 Aug</b>  Auction 30-year (r) TIPS <u>\$7</u> bn	<b>24 Aug</b>  Existing home sales (10:00am) Jul Richmond Fed survey (10:00am) Aug  Auction 2-year note <u>\$36</u> bn  Chicago Fed president Evans speaks in Indianapolis (8:30am)	<b>25 Aug</b>  Durable goods (8:30am) Jul New home sales (10:00am) Jul FHFA HPI (10:00am) Jun, 2Q  Auction 5-year note <u>\$34</u> bn	<b>26 Aug</b>  Initial claims (8:30am) w/e prior Sat KC Fed survey (11:00am) Aug  Auction 7-year note <u>\$28</u> bn	<b>27 Aug</b>  Real GDP (8:30am) 2Q second Consumer sentiment (9:55am) Aug final  Fed Chairman Bernanke speaks at Jackson Hole Conference (10:00am)
<b>30 Aug</b>  Personal income (8:30am) Jul Dallas Fed survey (10:30am) Aug  Announce 10-year (r) TIPS <u>\$10</u> bn  St. Louis Fed president Bullard gives welcoming remarks in St. Louis (1:30pm)	<b>31 Aug</b>  S&P/Case-Shiller HPI (9:00am) Jun, 2Q Chicago PMI (9:45am) Aug Consumer confidence (10:00am) Aug  FOMC minutes	<b>1 Sep</b>  ADP employment (8:15am) Aug ISM manufacturing (10:00am) Aug Construction spending (10:00am) Jul Light vehicle sales Aug	<b>2 Sep</b>  Initial claims (8:30am) w/e prior Sat Productivity and costs (8:30am) 2Q rev Pending home sales (10:00am) Jul Factory orders (10:00am) Jul Chain store sales Aug  Auction 10-year (r) TIPS <u>\$10</u> bn Announce 3-year note <u>\$33</u> bn Announce 10-year note (r) <u>\$21</u> bn Announce 30-year bond (r) <u>\$13</u> bn	<b>3 Sep</b>  Employment (8:30am) Aug ISM nonmanufacturing (10:00am) Aug  Atlanta Fed president Lockhart gives speech on economy in Tennessee (10:00am)
<b>6 Sep</b>  Labor Day Markets Closed	<b>7 Sep</b>  Auction 3-year note <u>\$33</u> bn	<b>8 Sep</b>  JOLTS (10:00am) Jul Beige book (2:00pm) Consumer credit (3:00pm) Jul  Auction 10-year note (r) <u>\$21</u> bn  Minneapolis Fed president Kocherlakota speaks on FOMC in Montana (2:30pm)	<b>9 Sep</b>  Initial claims (8:30am) w/e prior Sat International trade (8:30am) Jul  Auction 30-year bond (r) <u>\$13</u> bn	<b>10 Sep</b>  Wholesale trade (10:00am) Jun



## Euro area economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
<b>16 Aug</b> Euro area: HICP final (11:00am) Jul <u>1.7%oya, nsa</u>	<b>17 Aug</b> Euro area: BoP (10:00am) Jun Germany: ZEW business conf. (11:00am) Aug	<b>18 Aug</b>	<b>19 Aug</b> Germany: PPI (8:00am) Jul <u>3.5%oya, nsa</u> Netherlands: CBS cons. conf. (9:30am) Aug	<b>20 Aug</b> Belgium: BNB cons conf. (3:00pm) Aug
<b>23 Aug</b> Euro area: PMI flash (10:00am) Aug Mfg, services, composite EC cons. conf. prelim (4:00pm) Aug Germany: Import prices (8:00am) Aug PMI flash (9:30am) Aug Mfg, services, composite France: PMI flash (9:00am) Aug Mfg, services, composite	<b>24 Aug</b> Euro area: Industrial new orders (11:00am) Jun Germany: GDP final (8:00am) 2Q Belgium: BNB bus conf. (3:00pm) Aug	<b>25 Aug</b> Germany: IFO bus. survey (10:00am) Aug	<b>26 Aug</b> Euro area: M3 (10:00am) Jul Germany: GfK cons. conf. (8:00am) Sep Italy: ISAE cons. conf. (9:30am) Aug Spain: GDP final (9:00am) 2Q Netherlands: CBS bus. conf. (9:30am) Aug	<b>27 Aug</b> Germany: CPI 6 states and prelim (8:00am) Aug
<b>30 Aug</b> Euro area: EC business conf. (11:00am) Aug EC cons. conf. final (11:00am) Aug Germany: Retail sales (8:00am) Aug Spain: HICP flash (9:00am) Aug Belgium: CPI (11:15am) Aug	<b>31 Aug</b> Euro area: Unemployment rate (11:00am) Aug HICP flash (11:00am) Aug Germany: Employment (9:55am) Jul Unemployment (9:55am) Aug Italy: ISAE bus. conf. (9:30am) Aug CPI Prelim (11:00am) Aug	<b>1 Sep</b> Euro area: PMI Mfg final (10:00am) Aug Germany: PMI Mfg final (9:55am) Aug France: PMI Mfg final (9:50am) Aug Italy: PMI Mfg (9:45am) Aug Contractual wages (10:00am) Aug Spain: PMI Mfg (9:15am) Aug	<b>2 Sep</b> Euro area: GDP prelim (11:00am) 2Q PPI (11:00am) Jul ECB rate announcement (1:45pm) <u>No change expected</u> ECB press conf. (2:30pm) France: ILO unemployment (8:45am) 2Q Italy: PPI (10:00am) Jul	<b>3 Sep</b> Euro area: PMI services & composite final (10:00am) Aug Retail sales (11:00am) Jul Germany: PMI services & composite final (9:55am) Aug France: PMI services & composite final (9:50am) Aug Italy: PMI services & composite (9:45am) Aug Spain: PMI services & composite (9:15am) Aug
<b>6 Sep</b> Euro area: Foreign trade (11:00am) Jul	<b>7 Sep</b> Germany: Mfg orders (12:00pm) Aug	<b>8 Sep</b> Germany: Foreign trade (8:00am) Jul Industrial production (12:00pm) Jul France: Foreign trade (8:45am) Jul Monthly budget situation (8:45am) Jul Belgium: GDP final (3:00pm) 2Q	<b>9 Sep</b> Euro area: ECB monthly bulletin (10:00am) Sep Germany: CPI final (8:00am) Aug France: Industrial production (8:45am) Jul Employment final (8:45am) 2Q Netherlands: CPI (9:30am) Aug Industrial production (9:30am) Jul	<b>10 Sep</b> Italy: Industrial production (10:00am) Jul GDP final (11:00am) 2Q Spain: CPI final (9:00am) Aug

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

## Japan economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
<b>16 Aug</b>  GDP 1st est. (08:50am) 2Q <u>2.3%q/q, saar</u> Tertiary sector activity index (8:50 am) Jun <u>-0.5%m/m, sa</u>	<b>17 Aug</b>  Construction spending (2:00 pm) Jun  Auction 1-year bill	<b>18 Aug</b>  Auction 3-month bill	<b>19 Aug</b>  All sector activity index (1:30 pm) Jun <u>-0.3%m/m, sa</u> Nationwide department store sales (2:30pm) Jul <u>-6.0%oya</u>	<b>20 Aug</b>
<b>23 Aug</b>	<b>24 Aug</b>  Auction 20-year bond	<b>25 Aug</b>  Trade balance (8:50 am) Jul Corporate service prices (8:50 am) Jul  Auction 3-month bill	<b>26 Aug</b>  Auction 2-year note	<b>27 Aug</b>  All household spending (8:30 am) Jul Unemployment rate (8:30 am) Jul Job offers to applicants ratio (8:30 am) Jul Nationwide core CPI (8:30 am) Jul
<b>30 Aug</b>	<b>31 Aug</b>  PMI manufacturing (8:15 am) Aug Total retail sales (8:50 am) Jul IP preliminary (8:50 am) Jul Nominal wages (10:30 am) Jul Shoko Chukin small business sentiment (2:00 pm) Aug Housing starts (2:00 pm) Jul Construction orders (2:00 pm) Jul	<b>1 Sep</b>  Auto registrations (2:00 pm) Aug  Auction 3-month bill Auction 10-year bond	<b>2 Sep</b>  Monetary base (8:50 am) Aug	<b>3 Sep</b>  PMI services/ composite (8:15 am) Aug MoF corporate survey (8:50 am) 2Q
<b>6 Sep</b>  BoJ Monetary Policy Meeting  Auction 6-month bill	<b>7 Sep</b>  Coincident CI (2:00 pm) Jul BoJ Monetary Policy Meeting and statement BoJ governor Shirakawa's press conference (3:30 pm)	<b>8 Sep</b>  Private machinery orders (8:50 am) Jul M2 (8:50 am) Aug Current account (8:50 a m) Jul Economy watcher survey (2:00 pm) Aug BoJ monthly economic report (2:00 pm)  Auction 3-month bill Auction 30-year bond	<b>9 Sep</b>  MoF business outlook survey (8:50 am) 3Q Consumer sentiment (2:00 pm) Aug	<b>10 Sep</b>  GDP 2nd est. (08:50am) 2Q Corporate goods prices (8:50 am) Aug  Minutes of Aug 9-10 BoJ Monetary Policy Meeting (8:50 am)  Auction 5-year note
During the week: Cabinet Office private consumption index Jul				

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

## Canada economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
<b>16 Aug</b> <b>Existing home sales</b> Jul	<b>17 Aug</b> <b>Manufacturing sales (8:30am)</b> Jun <u>0.1%</u>	<b>18 Aug</b>	<b>19 Aug</b> <b>Wholesale sales (8:30am)</b> Jun <u>0.2%</u> <b>Leading indicators (8:30am)</b> Jul	<b>20 Aug</b> <b>CPI (7:00am)</b> Jul <u>0.1% (1.4%oya)</u> Core <u>0.1% (1.8%oya)</u>
<b>23 Aug</b>	<b>24 Aug</b> <b>Retail sales (8:30am)</b> Jun	<b>25 Aug</b> <b>Quarterly corporate profits (8:30am) 2Q</b>	<b>26 Aug</b> <b>Payroll employment (8:30am)</b> Jun	<b>27 Aug</b>
<b>30 Aug</b> <b>IPPI (8:30am)</b> Jul <b>Current account (8:30am)</b> 2Q	<b>31 Aug</b> <b>Quarterly GDP (8:30am)</b> 2Q <b>Monthly GDP (8:30am)</b> Jun	<b>1 Sep</b>	<b>2 Sep</b>	<b>3 Sep</b>
<b>6 Sep</b> <b>Labor Day</b> <b>Markets closed</b>	<b>7 Sep</b>	<b>8 Sep</b> <b>BoC rate announcement (9:00am)</b> <b>Building permits (8:30am)</b> Jul <b>Ivey PMI (10:00am)</b> Aug	<b>9 Sep</b> <b>Housing starts (8:15am)</b> Aug <b>International trade (8:30am)</b> Jul <b>New house price index (8:30am)</b> Jul	<b>10 Sep</b> <b>Employment (7:00am)</b> Aug

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

## Latin America economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
<b>16 Aug</b>  <b>Brazil:</b> FGV CPI IPC-S Aug 15 <u>0.24%/m, nsa</u> <b>Peru:</b> GDP Jun <u>11.3%oya, nsa</u> Unemployment rate Jul <b>Mexico:</b> Consar report Jul  <i>Holiday: Argentina, Colombia</i>	<b>17 Aug</b>  <b>Brazil:</b> Fipe CPI Aug 15 <u>0.20%/m, nsa</u> IGP-10 Aug <u>0.64%/m, nsa</u> <b>Mexico:</b> Central bank reserves	<b>18 Aug</b>  <b>Colombia:</b> IP Jun <u>9.5%oya, sa</u> Retail sales Jun <u>11.3%oya, nsa</u>	<b>19 Aug</b>  <b>Argentina:</b> Consumer confidence Aug <b>Brazil:</b> IGP-M 2nd rel Aug	<b>20 Aug</b>  <b>Argentina:</b> Economic activity Jun IP Jul <b>Brazil:</b> IPCA-15 Aug <u>0.06%/m, nsa</u> <b>Colombia:</b> BanRep meeting Aug <u>no change</u> <b>Mexico:</b> Real GDP 2Q <u>7.5%oya</u> IGAE Jun <u>7.4%oya</u> Banxico meeting Aug <u>no change</u>
<b>During the week:</b> Brazil: CAGED Formal Job Creation Jul Venezuela: GDP 2Q Unemployment rate Jul				
<b>23 Aug</b>  <b>Argentina:</b> Unemployment rate 2Q <b>Brazil:</b> FGV CPI IPC-S Aug 22 Current account Jul FDI Jul <b>Mexico:</b> Retail sales Jun	<b>24 Aug</b>  <b>Argentina:</b> Trade balance Jul <b>Brazil:</b> FGV Consumer Confidence Aug <b>Mexico:</b> CPI Aug 1H Core CPI Aug 1H Trade balance Jul Central bank reserves	<b>25 Aug</b>  <b>Brazil:</b> Fipe CPI Aug 23 Primary budget balance Jul Net debt % GDP Jul <b>Mexico:</b> Nominal GDP 2Q Current account 2Q Unemployment rate Jul	<b>26 Aug</b>  <b>Brazil:</b> Unemployment rate Jul	<b>27 Aug</b>  <b>Peru:</b> GDP 2Q
<b>During the week:</b> Argentina: Budget balance Jul				
<b>30 Aug</b>  <b>Brazil:</b> IGP-M final release Aug <b>Mexico:</b> Budget balance Jul	<b>31 Aug</b>  <b>Argentina:</b> Construction activity Jul <b>Brazil:</b> IP Jul <b>Colombia:</b> Unemployment rate Jul <b>Mexico:</b> Central bank reserves	<b>1 Sep</b>  <b>Brazil:</b> COPOM meeting Sep FGV CPI IPC-S Aug 31 Trade balance Aug <b>Mexico:</b> Banxico expectations survey Family remittances Jul <b>Peru:</b> CPI Aug WPI Aug	<b>2 Sep</b>  <b>Brazil:</b> Fipe CPI Aug 31	<b>3 Sep</b>  <b>Brazil:</b> GDP 2Q <b>Colombia:</b> BanRep minutes PPI Aug <b>Mexico:</b> Consumer confidence Aug IMEF manufacturing survey Aug IMEF nonmanufacturing survey Aug
<b>During the week:</b> Argentina: Government tax revenue Aug: Colombia (Sep 4): CPI Aug				
<b>6 Sep</b>  <b>Brazil:</b> Auto report (Anfavea) Aug <b>Ecuador:</b> CPI Aug	<b>7 Sep</b>  <b>Mexico:</b> Central bank reserves	<b>8 Sep</b>  <b>Brazil:</b> FGV CPI IPC-S Sep 7 <b>Mexico:</b> Formal employment Aug	<b>9 Sep</b>  <b>Brazil:</b> COPOM minutes IPCA Aug Capacity utilization Jul <b>Mexico:</b> CPI Aug Core Aug <b>Peru:</b> BCRP meeting	<b>10 Sep</b>  <b>Brazil:</b> Fipe CPI Sep 7 IGP-DI Aug <b>Colombia:</b> Trade balance Jul <b>Peru:</b> Trade balance Jul
<b>During the week:</b> Venezuela: CPI Aug				

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

## UK/Scandinavia/Switzerland economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
<b>16 Aug</b> Norway: Trade balance (10:00am) Jul	<b>17 Aug</b> United Kingdom: CPI (9:30am) Jul <u>3.0%oya</u> Sweden: House prices (9:30am) Jul	<b>18 Aug</b> United Kingdom: MPC minutes (9:30am) Jul <u>An 8-1 vote expected</u> Sweden: Capacity utilization (9:30am) 2Q	<b>19 Aug</b> United Kingdom: Retail sales (9:30am) Jul <u>0.2 %m/m, sa – ex fuel</u> M4 & M4 lending prelim (9:30am) Jul Public sector finances (9:30am) Jul PSNB <u>£ 7.5 bn, nsa</u> CBI industrial trends (11:00am) Aug <u>-1.6%bal, sa (total orders)</u> Norway: GDP (10:00am) 2Q <u>2.0%q/q, saar</u> Switzerland: Trade balance (8:15am) Jul	<b>20 Aug</b> Sweden: Riksbank's First Deputy Governor Svante Öberg speaks (12:30pm)
<b>23 Aug</b> Norway: Norges Bank's Governor Svein Gjedrem speaks Switzerland: Monthly statistical bulletin (9:00am) Aug	<b>24 Aug</b> United Kingdom: BBA lending (9:30am) Jul	<b>25 Aug</b> Sweden: Business tendency (9:15am) Aug Cons. confidence (9:15am) Aug Norway: AKU unemployment (10:00am) Jun	<b>26 Aug</b> United Kingdom: Business investment prelim (9:30am) 2Q CBI industrial trends (11:00am) Aug Sweden: Trade balance (9:30am) Jul PPI (9:30am) Jul Labor force survey (10:00am) Jul Switzerland: Employment (9:15am) 2Q	<b>27 Aug</b> United Kingdom: GDP prelim (9:30am) 2Q Index of services (9:30am) Jun Sweden: Retail sales (9:30am) Jul Norway: Mfg wage index (10:00am) 2Q Switzerland: KOF leading indicator (11:30am) Aug <u>2.20 Index, sa</u>
During the week : United Kingdom: Nationwide HPI Aug				
<b>30 Aug</b> Sweden: Wage stats (9:30am) Jun Norway: Retail sales (10:00am) Jul Credit indicator (10:00am) Jul	<b>31 Aug</b> United Kingdom: Gfk cons. conf. (12:01am) Aug M4 and M4 lending final (9:30am) Jul Net lending to individuals (9:30am) Jul Switzerland: UBS consumption indicator (8:00am) Jul	<b>1 Sep</b> United Kingdom: PMI Mfg (9:30am) Aug Sweden: PMI (8:30am)Aug Norway: PMI mfg (9:00am) Mfg Switzerland: PMI mfg (9:30am) Aug <u>66.0%bal, sa</u>	<b>2 Sep</b> United Kingdom: PMI construction (9:30am) Aug Sweden: Riksbank's rate announcement (9:30am) <u>25bp hike expected &amp;</u> Monetary Policy Update report Norway: Research conference at Norges Bank (2-3 Sep) Switzerland: GDP (7:45am) 2Q <u>2.7%q/q, saar</u>	<b>3 Sep</b> United Kingdom: PMI services(9:30am) Aug Norway: Labor directorate unemployment (9:00am) Aug Switzerland: CPI (9:15am) Aug <u>0.5%oya, nsa</u>
During the week : United Kingdom: Halifax HPI Aug				
<b>6 Sep</b> United Kingdom: New car regs (9:00am) Aug	<b>7 Sep</b> United Kingdom: BRC retail sales monitor (12:01am) Aug RICS HPI (12:01am) Aug Norway: Gallup cons. conf. (7:00am) 3Q Switzerland: Unemployment (7:45am) Aug	<b>8 Sep</b> United Kingdom: Industrial production (9:30am) Jul Sweden: GDP final (9:30am) 2Q	<b>9 Sep</b> United Kingdom: Trade balance (9:30am) Jul Quoted mortgage interest rates (9:30am) Aug MPC rate announcement (12:00pm) <u>No change expected</u> Sweden: CPI (9:30am) Aug Norway: IP mfg (10:00am) Jul	<b>10 Sep</b> United Kingdom: PPI (9:30am) Aug Sweden: Industrial production & orders (9:30am) Jul AMV unemployment (10:00am) Aug Norway: CPI (10:00am) Aug PPI (10:00am) Aug

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## Emerging Europe/Middle East/Africa economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
<b>16 August</b>  Czech Rep: PPI (9:00am) Jul Turkey: Consumer confidence (10:00am) Jul 86.5 Unemployment (10:00am) May 11.7% Israel: GDP 2Q 3.8%oya, 3%q/q saar	<b>17 August</b>  Poland: Average gross wages 3.0%oya & employment 1.5%oya (2:00pm) Jul Russia: IP Jul 8.2%oya	<b>18 August</b>  Poland: PPI (2:00pm) Jul 3.3%oya Industrial output (2:00pm) Jul 12.0%oya South Africa: Retail sales (11:30am) Jun	<b>19 August</b>  Hungary: Average gross wages (9:00am) Jun 0.5%oya Turkey: Monetary policy announcement no change	<b>20 August</b>  Poland: Core inflation (2:00pm) Jul 1.3%oya
During the week:				
<b>23 August</b>  Hungary: Monetary policy announcement No change Israel: Monetary policy announcement No change	<b>24 August</b>  Poland: Monetary policy announcement No change South Africa: GDP (11:30am) 2Q	<b>25 August</b>  Hungary: Retail sales (10:00am) Jun Turkey: Capacity utilization (4:30pm) Aug South Africa: CPI (11:30am) Jul	<b>26 August</b>  South Africa: PPI (11:30am) Jul	<b>27 August</b>
During the week:				
<b>30 August</b>  Poland: GDP (10:00am) 2Q	<b>31 August</b>  Hungary: PPI (9:00am) Jul Turkey: Foreign trade (10:00am) Jul South Africa: Credit & money (8:00am) Jul Trade balance (2:00pm) Jul	<b>1 September</b>  Czech Rep: PMI (9:30am) Aug Hungary: PMI (9:00am) Aug Poland: PMI (9:00am) Aug Romania: GDP Final (10:00am) 2Q Turkey: PMI (10:00am) Aug Russia: Manufacturing PMI (8:00am) Aug South Africa: Kagiso PMI (11:00am) Aug	<b>2 September</b>  South Africa: Vehicle sales (11:00am) Aug	<b>3 September</b>  Czech Rep: Average wage (9:00am) 2Q Romania: Retail sales (10:00am) Jul Turkey: CPI (10:00am) Aug PPI (10:00am) Aug Russia: Services PMI (8:00am) Aug
During the week:				
<b>6 September</b>  Czech Rep: Trade balance (9:00am) Jul Retail sales (9:00am) Jul Industrial output (9:00am) Jul South Africa: Current account 2Q	<b>7 September</b>  Czech Rep: Current account (10:00am) 2Q Hungary: Trade balance (9:00am) Jul EUR350mn Turkey: Industrial production (10:00am) Jul South Africa: Gross reserves (8:00am) Aug	<b>8 September</b>  Czech Rep: GDP Final (9:00am) 2Q Hungary: GDP Final (9:00am) 2Q Industrial output (9:00am) Jul Central bank minutes (2:00pm) Romania: Industrial output (10:00am) Jul South Africa: Manufacturing output (1:00pm) Jul Israel: Current account 2Q	<b>9 September</b>  Czech Rep: CPI (9:00am) Aug Romania: Trade balance (10:00am) Jul South Africa: Monetary policy announcement	<b>10 September</b>  Hungary: CPI (9:00am) Aug Poland: Current account (2:00pm) Jul EUR-900mn Romania: CPI (10:00am) Aug Current account (10:00am) Jul

## Non-Japan Asia economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
<b>16 Aug</b> <b>Australia:</b> New motor vehicle sales (11:30am) Jul <u>2.0%<i>m/m, sa</i></u> <b>India:</b> WPI (4:30 pm) Jul <b>Korea:</b> Export prices <u>1.2%<i>oya</i></u> Import prices <u>7.5 % <i>oya</i></u> <b>Philippines:</b> OFW remittances Jun <u>4.4%<i>oya</i></u>	<b>17 Aug</b> <b>Hong Kong:</b> Unemployment rate (4:30 pm) Jul <u>4.6%</u> <b>Singapore:</b> NODX (1:00 pm) Jul <u>11.0 US\$bn</u>  <i>Holiday Indonesia</i>	<b>18 Aug</b> <b>Australia:</b> Westpac leading index (10:30 am) Jun Wage cost index (11:30 am) 2Q <u>1.0%<i>q/q, sa</i></u> <b>Malaysia:</b> CPI (4:30 pm) Jul <u>2.4%<i>oya</i></u> GDP (6:00 pm) 2Q <u>8.6%<i>oya</i></u>	<b>19 Aug</b> <b>New Zealand:</b> PPI (10:45 am) 2Q <u>-0.1%<i>q/q, sa</i></u> <b>Philippines:</b> BOP Jul <b>Taiwan:</b> GDP (4:00 pm) 2Q <u>10.1%<i>oya</i></u>	<b>20 Aug</b> <b>Hong Kong:</b> CPI (4:30 pm) Jul <u>2.9%<i>oya</i></u> <b>New Zealand:</b> Visitor arrivals (10:45 am) Jul Credit card spending (3:00pm) Jul <b>Taiwan:</b> Export orders (4:00pm) Jul <u>22.8%<i>oya</i></u>
<b>During the week:</b> Korea: SPPI <u>5.2%<i>oya</i></u> Bankruptcy filings Jul <u>140</u> Philippines: Budget balance Jul				
<b>23 Aug</b> <b>Singapore:</b> CPI (1:00 pm) Jul <b>Taiwan:</b> Unemployment rate (4:00pm) Jul IP (4:00 pm) Jul <b>Thailand:</b> GDP (9:30 am) 2Q <i>Holiday Philippines</i>	<b>24 Aug</b> <b>New Zealand:</b> RBNZ 2 year inflation expectation 3Q	<b>25 Aug</b> <b>Australia:</b> Construction work done (11:30 am) 2Q <b>Philippines:</b> Imports (9:00 am) Jun <b>Thailand:</b> BoT monetary policy meeting (2:30 pm) Aug	<b>26 Aug</b> <b>Hong Kong:</b> Trade balance (4:30 pm) Jul <b>Philippines:</b> GDP (10:00 am) 2Q BSP Monetary policy meeting (5:00 pm) Aug <b>Singapore:</b> IP (1:00 pm) Jul	<b>27 Aug</b> <b>Korea:</b> Current account balance (8:00 am) Jul <b>Taiwan:</b> Leading index (4:00pm) Jul
<b>During the week:</b> Vietnam: CPI Aug Trade balance Aug				
<b>30 Aug</b> <b>Australia:</b> Company operating profits (11:30 am) 2Q Inventories (11:30 am) 2Q <b>New Zealand:</b> Trade balance (10:45 am) Jul NBNZ business confidence (3:00 pm) Aug  <i>Holiday Philippines</i>	<b>31 Aug</b> <b>Australia:</b> 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 <b>Hong Kong:</b> Retail sales (4:30 pm) Jul <b>India:</b> GDP 2Q <b>Korea:</b> IP (8:00 am) Jul Leading index (8:00 am) Jul Service sector activity (8:00 am) Jul <b>New Zealand:</b> Building permits (10:45 am) Jul <b>Thailand:</b> Trade balance (2:30 pm) Jul IP (2:30 pm) Jul PCI (2:30 pm) Jul PII (2:30 pm) Jul <i>Holiday Malaysia</i>	<b>1 Sep</b> <b>Australia:</b> GDP (11:30 am) 2Q <b>China:</b> PMI manufacturing (9:00 am) Aug <b>India:</b> PMI manufacturing Aug Trade balance Jul <b>Indonesia:</b> Inflation (12:00 pm) Aug Trade balance (12:00 pm) Jul <b>Korea:</b> CPI (8:00 am) Aug <b>New Zealand:</b> ANZ commodity prices (3:00 pm) Aug <b>Thailand:</b> CPI (2:00 pm) Aug	<b>2 Sep</b> <b>Australia:</b> Trade balance (11:30 am) Jul <b>Malaysia:</b> Trade balance (6:00 pm) Jul BNM monetary policy meeting (6:00 pm) Sep <b>Singapore:</b> PMI (9:30 pm) Aug  <i>Holiday Vietnam</i>	<b>3 Sep</b> <b>Indonesia:</b> BI rate announcement (2:00 pm) Sep <b>Korea:</b> GDP 2Q
<b>During the week:</b> Korea: Trade balance Aug				
<b>6 Sep</b> <b>New Zealand:</b> QV house prices Aug <b>Taiwan:</b> CPI (4:00 pm) Aug	<b>7 Sep</b> <b>Australia:</b> RBA cash target Sep <b>Philippines:</b> CPI (9:00 am) Aug <b>Taiwan:</b> Exports (4:00 pm) Aug	<b>8 Sep</b> <b>Australia:</b> Housing finance (11:30 am) Jul <b>New Zealand:</b> Manufacturing activity (10:45 am) 2Q	<b>9 Sep</b> <b>Australia:</b> Unemployment rate (11:30 am) Aug <b>Korea:</b> Bank of Korea monetary policy meeting Sep <b>Malaysia:</b> IP (5:00 pm) Jul <b>Philippines:</b> Exports (9:00 am) Jul  <i>Holiday Indonesia</i>	<b>10 Sep</b> <b>China:</b> Trade balance Aug <b>India:</b> IP Jul  <i>Holiday Indonesia, Malaysia, Singapore,</i>
<b>During the week:</b>				

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## Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
16 - 20 August	16 August	17 August	18 August	19 August	20 August
	<p><b>Euro area</b></p> <ul style="list-style-type: none"> <li>HICP final (Jul)</li> </ul> <p><b>India</b></p> <ul style="list-style-type: none"> <li>WPI (Jul)</li> </ul> <p><b>Japan</b></p> <ul style="list-style-type: none"> <li>GDP (2Q)</li> </ul> <p><b>Turkey</b></p> <ul style="list-style-type: none"> <li>Unemployment rate (May)</li> </ul> <p><b>United States</b></p> <ul style="list-style-type: none"> <li>Empire State surv (Aug)</li> <li>NAHB surv (Aug)</li> </ul>	<p><b>Germany</b></p> <ul style="list-style-type: none"> <li>ZEW bus conf (Aug)</li> </ul> <p><b>Russia</b></p> <ul style="list-style-type: none"> <li>IP (Jul)</li> </ul> <p><b>Singapore</b></p> <ul style="list-style-type: none"> <li>Exports (Jul)</li> </ul> <p><b>United Kingdom</b></p> <ul style="list-style-type: none"> <li>CPI (Jul)</li> </ul> <p><b>United States</b></p> <ul style="list-style-type: none"> <li>Housing starts (Jul)</li> <li>IP (Jul)</li> </ul>	<p><b>Poland</b></p> <ul style="list-style-type: none"> <li>IP (Jul)</li> </ul> <p><b>United Kingdom</b></p> <ul style="list-style-type: none"> <li>MPC minutes (Aug)</li> </ul>	<p><b>Netherlands</b></p> <ul style="list-style-type: none"> <li>CBS cons conf (Aug)</li> </ul> <p><b>Norway</b></p> <ul style="list-style-type: none"> <li>GDP (2Q)</li> </ul> <p><b>Taiwan</b></p> <ul style="list-style-type: none"> <li>GDP (2Q)</li> </ul> <p><b>Turkey</b></p> <ul style="list-style-type: none"> <li>CBRT mtg: no chg</li> </ul> <p><b>United Kingdom</b></p> <ul style="list-style-type: none"> <li>Retail sales (Jul)</li> </ul> <p><b>United States</b></p> <ul style="list-style-type: none"> <li>Philly Fed surv (Aug)</li> <li>Leading indicators (Jul)</li> </ul>	<p><b>Argentina</b></p> <ul style="list-style-type: none"> <li>IP (Jul)</li> </ul> <p><b>Belgium</b></p> <ul style="list-style-type: none"> <li>BNB cons conf (Aug)</li> </ul> <p><b>Colombia</b></p> <ul style="list-style-type: none"> <li>BanRep mtg: no chg</li> </ul> <p><b>Mexico</b></p> <ul style="list-style-type: none"> <li>Banxico mtg: no chg</li> </ul> <p><b>Taiwan</b></p> <ul style="list-style-type: none"> <li>Export orders (Jul)</li> </ul>
23 - 27 August	23 August	24 August	25 August	26 August	27 August
	<p><b>Euro area</b></p> <ul style="list-style-type: none"> <li>PMI flash (Aug)</li> <li>EC cons conf (Aug)</li> </ul> <p><b>Hungary</b></p> <ul style="list-style-type: none"> <li>NBH mtg: no chg</li> </ul> <p><b>Israel</b></p> <ul style="list-style-type: none"> <li>Bol mtg: no chg</li> </ul> <p><b>Taiwan</b></p> <ul style="list-style-type: none"> <li>IP (Jul)</li> </ul>	<p><b>Belgium</b></p> <ul style="list-style-type: none"> <li>BNB bus conf (Aug)</li> </ul> <p><b>Germany</b></p> <ul style="list-style-type: none"> <li>GDP final (2Q)</li> </ul> <p><b>United States</b></p> <ul style="list-style-type: none"> <li>Existing home sales (Jul)</li> <li>Richmond Fed surv (Aug)</li> </ul>	<p><b>Germany</b></p> <ul style="list-style-type: none"> <li>IFO bus surv (Aug)</li> </ul> <p><b>Japan</b></p> <ul style="list-style-type: none"> <li>Trade balance (Jul)</li> </ul> <p><b>Thailand</b></p> <ul style="list-style-type: none"> <li>BoT mtg: +25 bps</li> </ul> <p><b>United States</b></p> <ul style="list-style-type: none"> <li>Durable goods (Jul)</li> <li>New home sales (Jul)</li> </ul>	<p><b>Germany</b></p> <ul style="list-style-type: none"> <li>GFK cons conf (Sep)</li> </ul> <p><b>Italy</b></p> <ul style="list-style-type: none"> <li>ISAE cons conf (Aug)</li> </ul> <p><b>Netherlands</b></p> <ul style="list-style-type: none"> <li>CBS bus conf (Aug)</li> </ul> <p><b>Philippines</b></p> <ul style="list-style-type: none"> <li>BSP mtg: no chg</li> </ul> <p><b>Singapore</b></p> <ul style="list-style-type: none"> <li>IP (Jul)</li> </ul> <p><b>Spain</b></p> <ul style="list-style-type: none"> <li>GDP final (2Q)</li> </ul> <p><b>United States</b></p> <ul style="list-style-type: none"> <li>KC Fed surv (Aug)</li> </ul>	<p><b>Germany</b></p> <ul style="list-style-type: none"> <li>CPI prelim (Aug)</li> </ul> <p><b>Japan</b></p> <ul style="list-style-type: none"> <li>Hhold spending (Jul)</li> <li>Unemployment rate (Jul)</li> <li>Core CPI (Jul)</li> </ul> <p><b>United Kingdom</b></p> <ul style="list-style-type: none"> <li>GDP (2Q)</li> </ul> <p><b>United States</b></p> <ul style="list-style-type: none"> <li>GDP revision (2Q)</li> <li>CB cons sent (Aug)</li> <li>Bernanke speech</li> </ul>

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