

The Week Ahead

- Fears for the global economy remain intense, with policy leaders warning the world remained in a “danger zone”.
- The Fed’s announcement of “Operation Twist” failed to buoy market sentiment.
- After a week of communication overload from the RBA the central bank communications focus shifts to the US, with several Fed speakers, including Fed Chairman Ben Bernanke, speaking.

Deep concerns for the health of the global economy continue to affect markets. World finance ministers and officials of the IMF and World Bank are meeting in Washington for the IMF’s annual meetings. World Bank President Robert Zoellick and IMF Managing Director Christine Lagarde have both urged action by advanced and emerging economies to head off a world-wide downturn.

Markets were unimpressed this week by the announcement of ‘Operation Twist’ by the Federal Reserve. The announcement of a US\$400bn shift in the duration of the Fed’s Treasury holdings did not buoy equity markets. Downgraded forecasts from the IMF added to the gloom, although the new numbers represented more a catchup to more frequently revised private sector forecasts, rather than adding any significant new information about the outlook. The IMF’s title for the updated outlook was “*Slowing Growth, Rising Risks*” which summarises the general tone very succinctly. Our International Economist, Martin McMahon reviews the IMF’s revised forecasts from page thirteen.

Meanwhile, in Australia – now home to Euromoney magazine’s ‘Finance Minister of the Year’ – a relatively quiet data week was dominated by central bank communications. The RBA minutes on Tuesday highlighted the RBA Board’s concerns surrounding the extreme uncertainty in global markets. RBA Deputy Governor Ric Battellino addressed the Euromoney Forum in New York this week, and highlighted how Australia’s economy is no longer subject to the same strong links to US economic performance as it was from the 1970s to early 1990s. Assistant Governor Philip Lowe detailed some of the changing patterns of household saving and spending in Australia, concluding that the shift away from expenditures on goods has resulted in the retail trade data being an unreliable indicator of the pulse of household behaviour. The RBA released its bi-annual financial stability review this morning, finding that the Australian banking system remains in a relatively strong condition and is considerably better placed to cope with periods of market strain than it was before the GFC.

In light of the heightening risks of a major financial shock our Chief Economist, Michael Blythe, has taken a look at Australia’s defences and our ability to withstand another shock. His analysis can be found on page two.

Next week the key data releases are private sector credit growth, population growth and the QII financial accounts. We are expecting credit to grow modestly in August, though there are downside risks – particularly on business and other personal credit – to growth from the recent uncertainty in markets and its affect on confidence.

Across the Tasman, trade and building permits figures for August are released. This week saw the release of QII GDP figures, which were weaker than expected. Our New Zealand Economist, Chris Tennent-Brown, reviews the NZ GDP release from page sixteen.

Internationally, the major US data releases next week include durable goods orders, the Case-Shiller home price index, new home sales and consumer confidence. The week ends with the latest update on QII US GDP. However, before the week is over there are no less than 9 speeches by various US Federal Reserve system figures, including Fed Chairman Ben Bernanke who is speaking in Cleveland, Ohio on Wednesday night. Wednesday also includes speeches by the Swiss National Bank’s Thomas Jordan and the ECB’s Yves Mersch.

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Australian Economic Perspective

Manning the barricades – how good are Australia’s defences?

- We dodged the recession bullet a few years ago through a combination of good policy and good luck.
- The good policy framework is still there. But it may prove less effective. And some of the luck has run out.
- We still expect Australia to outperform in the face of another financial shock. But it may be more of a struggle.

Our economic reputation was forged in the post Lehman’s environment when we dodged the global recession bullet. Australia is still outperforming the major economies. Many of these are yet to regain pre-Lehman’s levels of output. Financial issues and growth concerns in the North Atlantic economies are lifting again. And the debate about our economic resilience has resurfaced.

We don’t believe that a replay of 2008-09 is underway. But it is worthwhile examining Australia’s defences and our ability to withstand another global financial shock.

We pulled through last time with a combination of good policy and good luck. The good policy reflects the intellectual and policy reform effort of the 1980s and 1990s. The luck was just that – luck.

The good policy framework is still there. But it may prove less effective against any future shock. And some of the luck has run out. We would still expect Australia to outperform other countries in the face of another financial shock. But it may be more of a struggle.

There is little doubt that the RBA would cut rates again if required. More importantly, lower interest rates would work. The mere sniff of the possibility of an interest rate cut in recent weeks has been enough to shift the interest-rate sensitive parts of household sentiment. But fiscal responses could be less aggressive than last time. And household appetite to spend any fiscal largesse may prove more muted as well.

The bigger issue may be the AUD. Global “shocks” typically go hand in hand with a (much) lower AUD. But the recent experience with the Aussie is a bit different. The Aussie’s trajectory after recent shocks is much more resilient. So there is a risk that the currency may not play its usual buffering role and worse economic outcomes could result.

Luck comes in many forms. And a combination of factors helped protect the Australian economy during the 2008-09 financial crisis. Some of these factors are still at work. Others are not. And some new ones are in play.

The support from strong population growth has gone. And the ability to export our problems to the rest of the world is less. But the emergence of Asia continues. And reconstruction activity post the Queensland floods is now underway. Queensland coal exports will recover. The potential impact of the coal story is very large. A return to end 2010 export levels will add ¾ppts to GDP growth in H1 2011. This boost will be a significant offset to whatever drag may eventuate from current uncertainties and risks.

How the confidence issue played out last time was one of the more unusual pieces of luck. The near panic at the time fed a huge lift in job security concerns. Government forecasts suggesting a doubling of the unemployment rate added to these fears. Unemployment rose. But it wasn’t the catastrophe that many feared. The gap between fear and reality was an important support under consumer confidence. Job security fears are now lifting again. Watching the gap between perception and reality will be important when assessing the downside risks to the Australian outlook.



Can we dodge the bullet again?

The Australian economic story was an easy one to “sell” over the past few years. Our reputation was forged in the post Lehman’s environment when we dodged the global recession bullet.

Debate about our economic resilience has resurfaced.

Australia is still outperforming the major economies. Many of these are yet to regain pre-Lehman’s levels of output. Financial issues and growth concerns in the North Atlantic economies are lifting again. And the debate about our economic resilience has resurfaced.

We don’t believe that a replay of 2008-09 is underway. But it is worthwhile examining Australia’s defences and our ability to withstand another global financial shock.

Good policy and good luck saved us last time.

We pulled through last time with a combination of good policy and good luck. The good policy reflects the intellectual and policy reform effort of the 1980s and 1990s. The luck was just that – luck.

We still expect Australia to outperform.

The good policy framework is still there. But it may prove less effective against any future shock. And some of the luck has run out. We would still expect Australia to outperform other countries in the face of another financial shock. But it may be more of a struggle.

Recent research by the International Monetary Fund (IMF) and the Institute for management Development (IMD) nicely captures our relative position.

The IMF has modelled the impact on the rest of the world of Euro area turbulence that severely disrupts global financial markets. Their work shows that emerging Asia is the *region* least affected under such a scenario. And Australia is the *country* least affected.

The IMD has a long-running project tracking world competitiveness. Their 2011 survey puts Australia in the number two slot in terms of economic resilience and ability to withstand external shocks.

Good policy

Australia’s policy response post Lehman’s was world’s best practice.

Australia’s effective policy response to the post Lehman’s environment was world’s best practice. Policy makers stuck to the script set out by the experts for dealing with a financial crisis and recession. We ticked all the policy boxes outlined in Table 1.

The policy decision to “go hard, go early, go households” paid off in 2008-09. Cash handouts supported consumer spending. Low interest rates and the 1st home-owners boost supported housing activity. Tax incentives supported business capex.

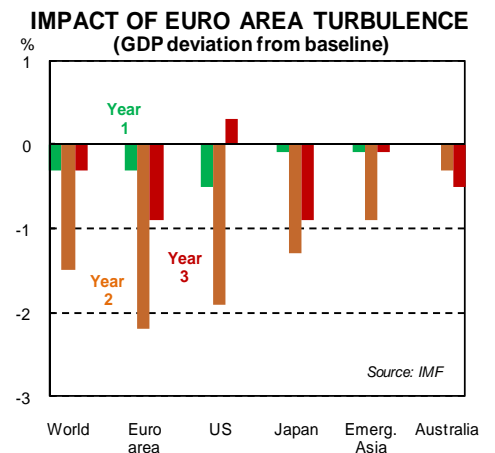
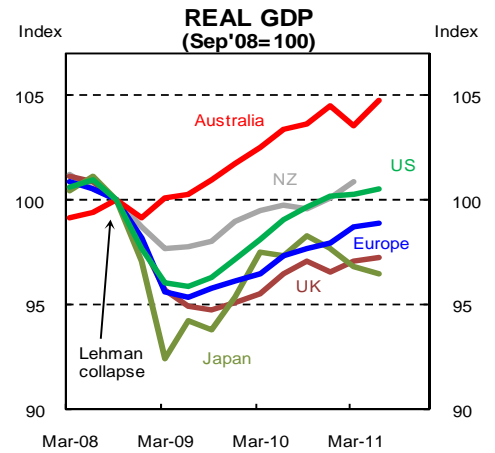
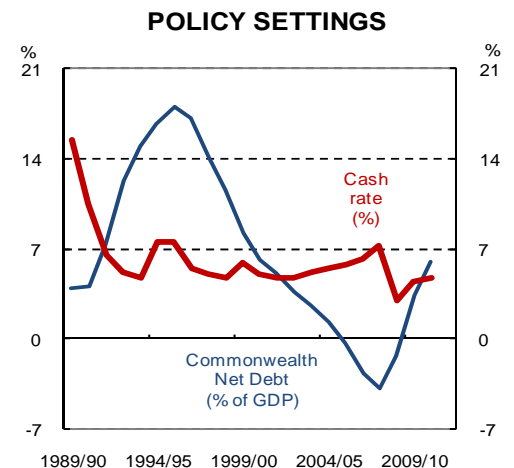


Table 1: Optimal Policy Rules for a Financial Crisis & Recession

- Aggressive monetary response - rate cuts, quantitative measures if needed
- Aggressive fiscal response – fiscal policy more effective in a financial crisis
- Short-term stimulus measures to follow the 3 T’s (timely, targeted & temporary)
- Long-run policy measures to target the 3 P’s (population, participation & productivity)
- Debt sustainability to be preserved – fiscal policy becomes less effective as debt rises
- Exit strategy for the withdrawal of policy stimulus





And by sticking to the final part of the policy prescription – the exit strategy – we have put ourselves in a good position to deal with any new threats. Interest rates have been normalised and the fiscal balance is on track to return to surplus in 2012/13. That exit strategy is in fact a contributor to the loss of economic momentum in 2011.

GFC Mk II would see rates slashed again...

There is little doubt that the RBA would cut rates again if required. More importantly, lower interest rates would work. The mere sniff of the possibility of an interest rate cut in recent weeks has been enough to shift the interest-rate sensitive parts of household sentiment. The proportion of households who think now is a good time to buy a dwelling, for example; has moved decisively higher.

... but any fiscal response may be more muted.

But fiscal responses could be less aggressive than last time. Issues crimping the appetite for fiscal expansion include:

- the political credibility invested in the idea of a Budget surplus by 2012/13;
- the difficulties with some of the stimulus measures used last time; and
- the difficult legislative environment.

On the other side of the equation, household appetite to spend any fiscal largesse may prove more muted as well. The saving ratio is much higher than it was pre Lehman's. And the CBA's *survey of consumer perceptions* indicates a preference for using any additional cash for saving or paying off debt. Balance sheet repair does, of course improve the ability of the economy to withstand shocks.

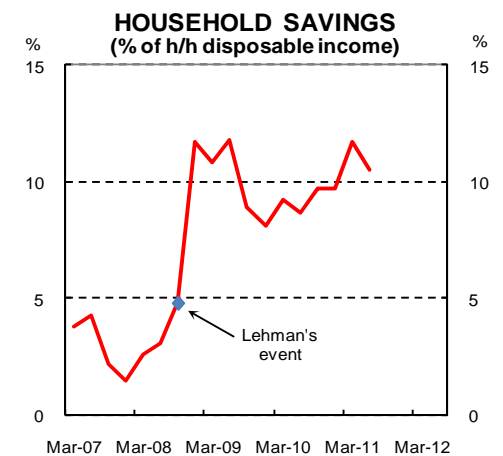
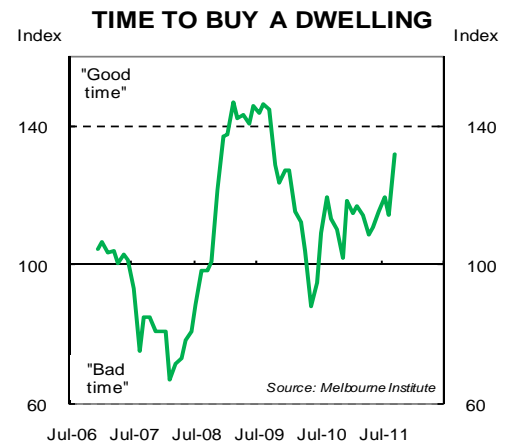
Good policy also meant that our financial system was better placed to take the strain when the financial crisis hit peak intensity. And good policy meant that the Aussie dollar was available as a buffer against the global "shock".

The financial system is, if anything, stronger than it was a few years ago. Capital ratios are higher, lending standards are tighter and funding composition has improved.

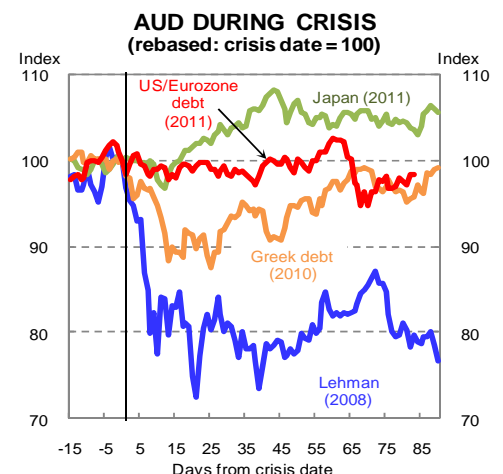
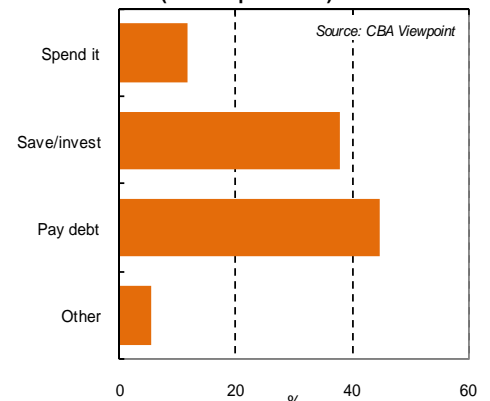
There is a risk that the Aussie fails to play its usual buffering role.

The bigger issue may be the AUD. The Aussie is widely seen as a barometer of global growth expectations and risk appetite. So global "shocks" typically go hand in hand with a (much) lower AUD. This drop typically keeps Australian exports attractive even in a contracting global market. It supports local currency incomes even when world prices fall. And it eases domestic financial conditions.

But the recent experience with the Aussie is a bit different. As the facing chart shows, the trajectory traced out after recent shocks is much more resilient. The AUD dipped when the Greek debt crisis first emerged in 2010, for



WHAT TO DO WITH AN UNEXPECTED \$5K (% of respondents)





example, but soon returned to pre-crisis levels. So there is a risk that the Aussie may not play its usual buffering role and worse economic outcomes could result.

This possibility is yet to be tested, of course, by a full-blown crisis.

Flexible labour markets helped.

The cumulative impact of the economic reform effort, including to the labour market, was to improve flexibility. This flexibility arguably produced better labour market outcomes during the GFC period than would have occurred otherwise. The bulk of the adjustment was to hours worked rather than the headcount.

Background conditions at the time accentuated the flexibility between employers and employees. We were close to full employment so employers were encouraged to hoard labour. In turn, intense job security fears encouraged employees to accept changed working arrangements.

Good luck

Luck comes in many forms.

Luck comes in many forms. And a combination of factors helped protect the Australian economy during the 2008-09 financial crisis. Some of these factors are still at work. Others are not. And some new ones are in play.

Business and consumer confidence collapsed everywhere post Lehman's. Businesses responded by curtailing capex. Consumers cut spending on durables. But much of this spending from an Australian context is on imported items. In a sense we were able to push part of our adjustment burden on to the economies that produced those imports. So the impact on Australian production (or GDP) was more muted.

Our ability to "export" part of the problem is less.

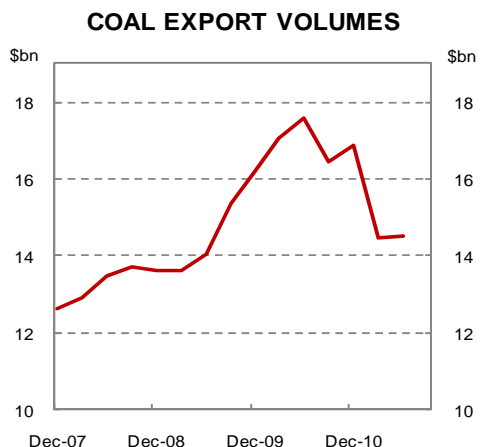
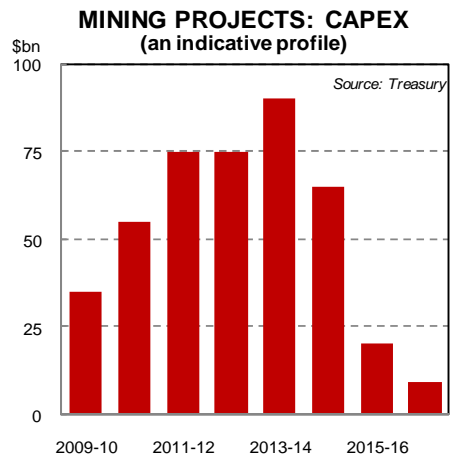
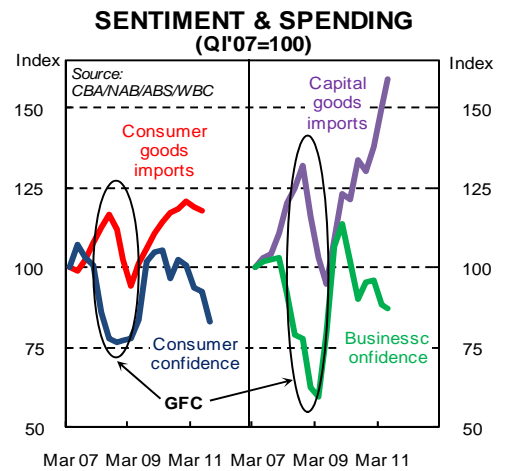
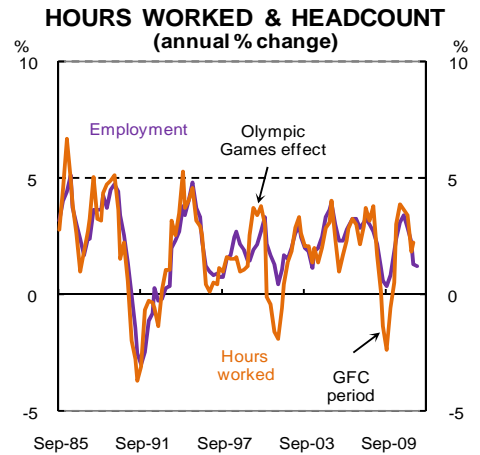
Lower consumer confidence could restrain consumer goods imports again. But the nature of the capex boom means capital goods imports are unlikely to respond. The mining projects underlying the capex boom will roll on whatever the global backdrop. Those same projects will also support domestic activity. On some indicative figuring, the peak impact from current projects won't be felt until 2013/14.

A weather-driven boost to the rural sector is unlikely...

A bit of rain at the right time in the right places boosted grain production in 2008/09. And higher rural production contributed 0.3ppts to GDP growth in that year. Floods earlier in 2011 filled water storages and restored soil moisture in many areas. But much of the boost to rural production occurred in 2010/11. The potential for a significant addition to activity in the period ahead is smaller as a result.

...but a weather-influenced boost to coal exports is.

There will be some positive weather-related impacts in 2011/12. The bulk of reconstruction





activity post the Queensland floods will occur during H1 2011. And Queensland coal exports will recover. The potential impact of the coal story is very large. A return to end 2010 export levels will add ¼ppts to GDP growth in H1 2011. This boost will be a significant offset to whatever drag may eventuate from current uncertainties and risks.

A domestic dynamic is sustaining Asian strength, supporting Australian trade and commodity prices.

Global financial turmoil since 2007 coincided with a period where a domestic dynamic took hold in many Asian economies. Regional growth is now much less dependent on strong export markets. The Asian region will be the stronger part of the global economy in the period ahead whatever the outcome elsewhere. A very high proportion of Australia's exports to the region are tied in with that domestic story. Some 80% of our exports to China, for example, remain in China. So we will continue to benefit from our exposure to the stronger and more durable part of the Asian growth story.

The prop from strong population growth is weaker.

The population growth rate was accelerating in the period around the Lehman's debacle. So demographic forces supported housing demand at a critical point. Strong population growth also supported demand across the economy more broadly.

Population growth is, however, now slowing quickly. There is still an excess demographic demand for housing that will limit downside risks in that sector. But the stimulus from population growth is weaker.

But slower growth in the working-age population will help keep unemployment low.

There is another side to the population story. The slowing reflects less migration. As a result, growth in the working-age population has slowed dramatically as a result. Fewer new jobs are required each month to absorb new entrants into the labour force and keep unemployment constant. The critical jobs number has dropped from 19k per month in mid 2010 to 10k now. So a weaker economy may do less damage to unemployment and confidence than feared.

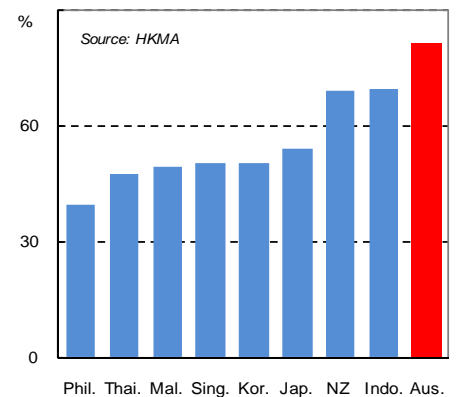
How the confidence issue played out last time was one of the more unusual pieces of luck. The near panic at the time fed a huge lift in job security concerns. These concerns reached record highs on some measures. Government forecasts suggesting a doubling of the unemployment rate from 4% in 2008 to more than 8% by 2010 added to these fears.

The gap between labour-market perception and reality will be important.

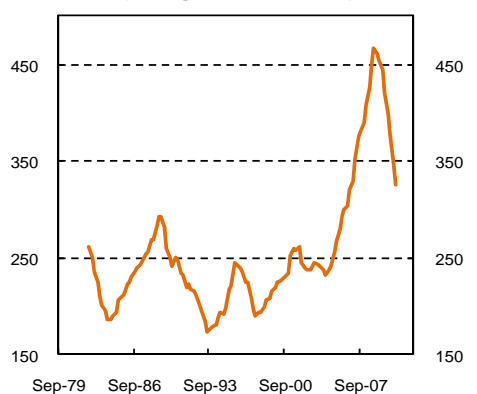
The reality, though, was that the unemployment rate rose by about 1½% to peak at less than 6%. Unemployment rose. But it wasn't the catastrophe that many feared. The gap between fear and reality was an important support under consumer confidence.

Job security fears are now lifting again.

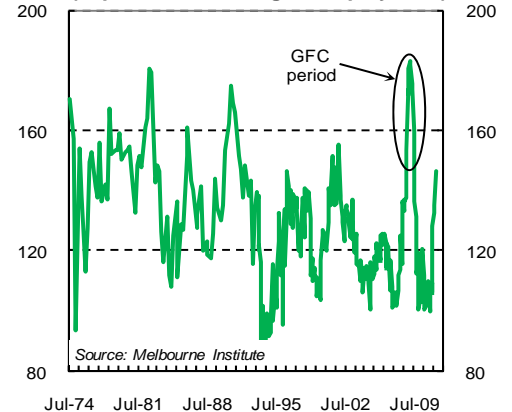
CHINA & EXPORTS
(% of a country's exports that remain in China)



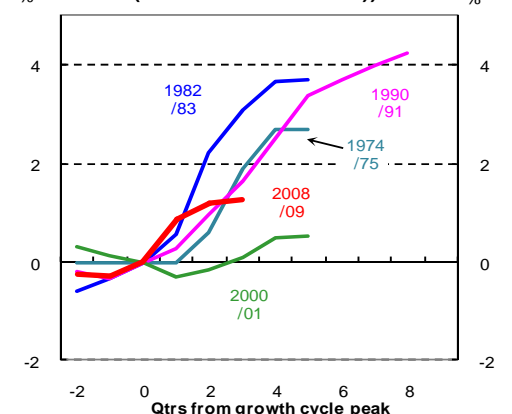
POPULATION
(rolling annual increase)



JOB SECURITY CONCERNS
(expectations of rising unemployment)



RECESSIONS & UNEMPLOYMENT
(cumulative % increase)





Watching the gap between perception and reality will be important when assessing the downside risks to the Australian outlook.

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Australian Economic Perspective

Labour Market Heat Maps – regional & industry jobs growth

- Labour market outcomes are a key barometer of the health of the economy, and of regions and industries therein.
- Divergences in industry and regional economic outcomes are apparent from labour market data.
- We have applied the “Heat Map” concept to the labour market data to illustrate the “patchwork” nature of the economy.

Labour market outcomes are one measure of the health of the economy. However, like any measure there are drawbacks. Employment outcomes tend to lag economic activity by around 6-9 months, and are subject to swings in business sentiment. Our analysis suggests that one such sentiment shift is apparent from recent outcomes. The recent GDP figures highlight that the economy is actually stronger than commonly thought. Firms have been increasing output, but employment growth has been exceptionally weak. Just 10.1k jobs have been created since January 2011, and the unemployment rate has risen from 4.9% to 5.3%.

But existing workers have been doing additional hours. Hours worked have increased by 2.6% since January. As a result, average weekly hours worked have risen from 31.9 to 32.7. Increasing the average work week by 0.1 hours is equivalent to around 25k additional jobs. Concerns about the outlook have seen employers freeze hiring, and work existing staff with greater intensity.

Increases in hours, and also jobs, are not evenly spread across the economy. Our labour market “Heat Maps” illustrate the industries and regions where jobs growth has been strongest over the year to August 2011. The “Heat Maps” break down the labour market into individual regions (capital city vs rest of state) and industries, and group these according to their proportional share of total employment. These “Heat Maps” illustrate where jobs growth is strongest, and which industries or regions are struggling. They illustrate the “patchwork” effects occurring across the economy.

The “patchwork” is broadly similar to the themes we have been highlighting across the economy. Employment in mining and construction has been very strong, as resources and infrastructure construction activity accelerates. Retail sector employment growth moderated, but remains solid. The shift in consumer spending towards discretionary services has seen sectors such as accommodation and food services, and recreation and arts growing jobs at a rapid pace.

Non-mining tradeable sectors (agriculture and manufacturing) have experienced significant job losses. Manufacturing in particular lost 30.7k jobs over the three months to August 2011. But the picture is far from uniform across the manufacturing sector. Around ¼ of the manufacturing sector (those subcomponents linked to mining and infrastructure construction in particular) experienced strong jobs growth over the year to August.

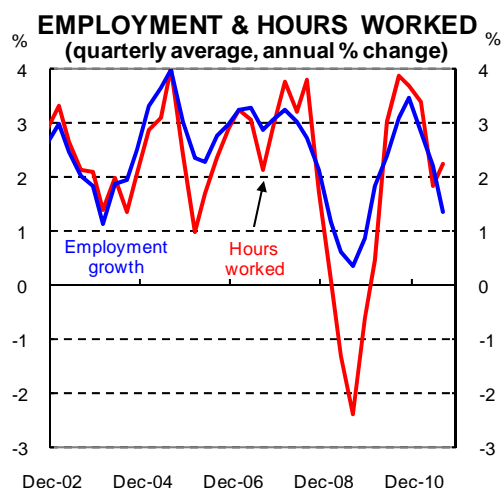
Significant divergences across the regions remain a feature of the labour market landscape. Jobs growth in the capital cities continues to lag regional employment growth outcomes. There is a link here to the industry composition of jobs growth. There are no major minerals or energy projects built in the suburbs of Sydney or Melbourne. Even though many of the major resource projects may be utilising employees from outside the project’s home region, there are still likely to be significant spillovers for local economies hosting mining, energy and major infrastructure projects.

Jobs growth has been exceptionally weak over the last 6 months.

The pace of jobs growth slowed to a halt since the beginning of 2011. Since January there have been only 10.1k jobs created, an average of just 1.4k per month. Jobs growth had been the extreme opposite over 2010. The annual pace of jobs growth has slowed to 1.3%.

But employers have increased workers hours to deliver higher production.

However the details of the labour market point to underlying strength in labour demand. And an air of caution by employers. Recent uncertainty over the past few months may have led employers to put a freeze on hiring new workers. But it hasn’t been able to put a freeze on demand for labour, which has instead been met by an increase in hours worked. Whilst employment has risen by only 0.1% since January, hours worked have climbed 2.6%.





We estimate that average weekly hours have risen from 31.9 to 32.7 from January to August. Increasing the average work week by 0.1 hours is equivalent to around 25k additional jobs.

The current dynamics mean labour market headlines may mislead.

So the headline indicators – including the rise in the unemployment rate from 4.9% to 5.3% – are potentially misrepresenting the signal the labour market is presenting on the economy.

To gain a broader sense of which parts of the economy are holding up better we have broken down the jobs data into industry and regional outcomes to illustrate the ‘patchwork’ of outcomes across the economy.

Employment in tradeable sectors falling significantly.

The updated industry heat maps indicate a continuation of the trends evident over the May 2011 quarter. Employment growth in the tradeable sectors (i.e. those impacted by the high Australian dollar) has fallen significantly over the past year. Employment in domestically influenced (or non-tradeable) sectors remains solid. Weakness in manufacturing and agricultural employment was the major driver.

Employment in the retail sector has moderated, but remains solid. Retail employment rose by 16.8k over the year to August 2011, and should be supported by the sector’s record profits.

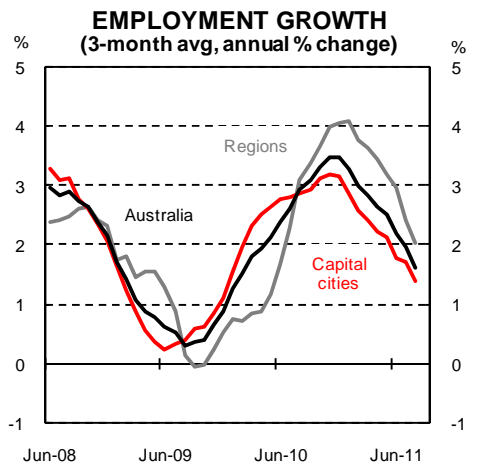
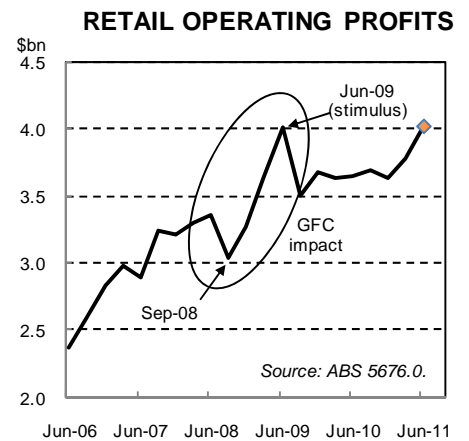
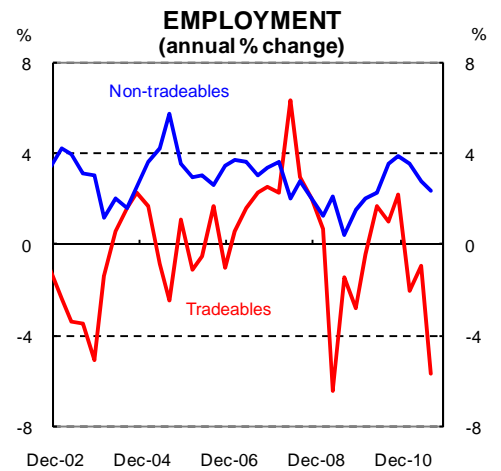
Regional jobs growth remains stronger than capital cities.

With the exception of NSW, regional employment growth continues to outpace capital city growth. Over the three months to August 2011 regional employment growth was 2.0%, compared to 1.4% for capital cities.

How to read the Heat Maps

The labour market is broken down into its individual categories (industries, or region). The size of each box corresponds to the share of the labour market attributable to each category. The label inside each square details the category (industry, region), its share of employment, and growth over the year.

The colours indicate the strength of growth, moving from red (where jobs growth is weak), blue (around trend) or dark green (strong).



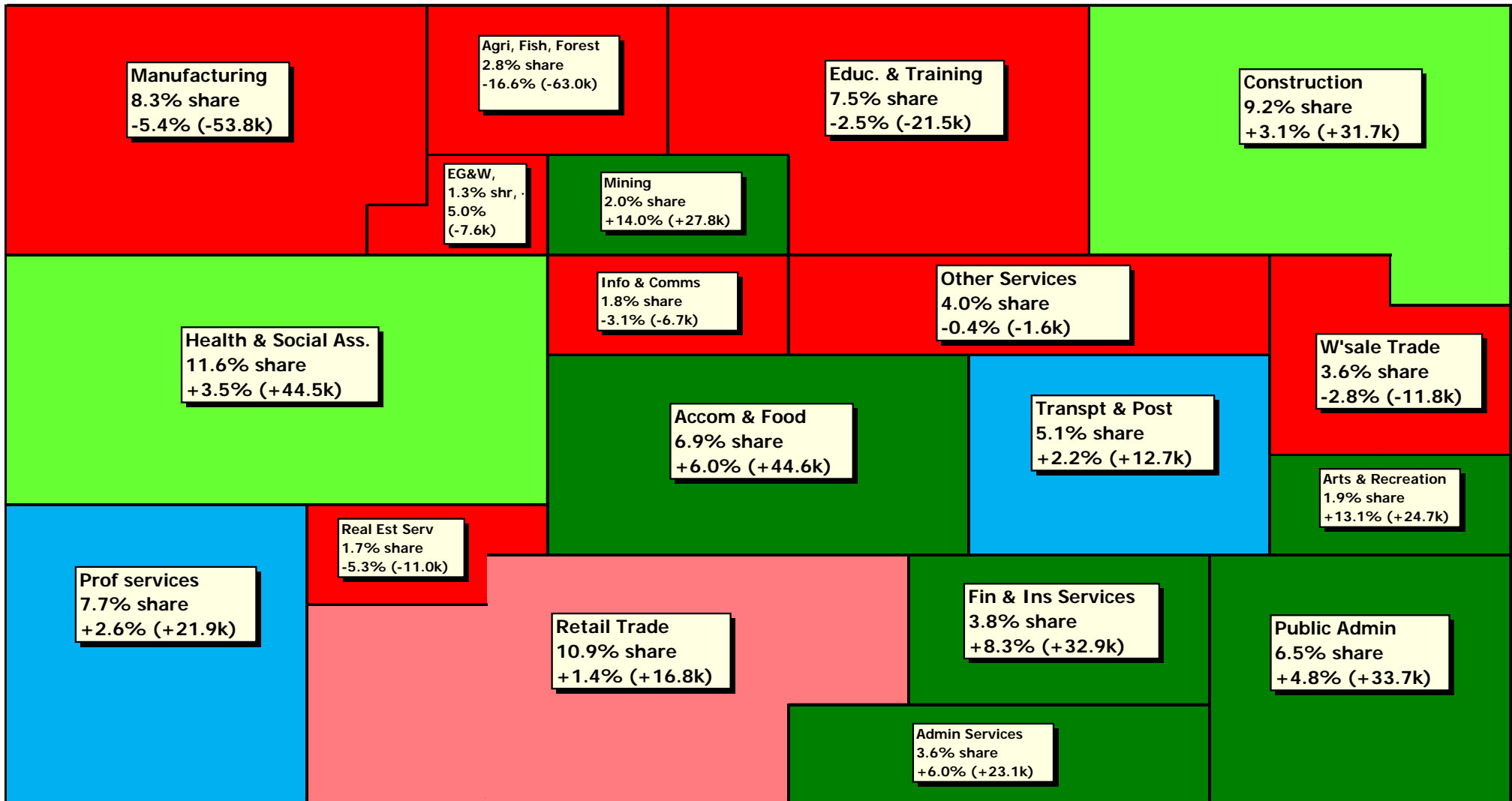
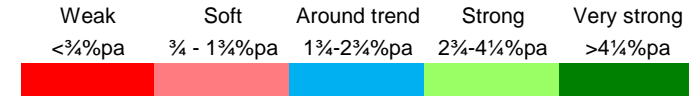


Industry employment heat map – annual jobs growth

Colours below correspond to annual % change, August 2011, using original data.

Employment CAGR - 10 years to August 2011: +2.3%

Legend



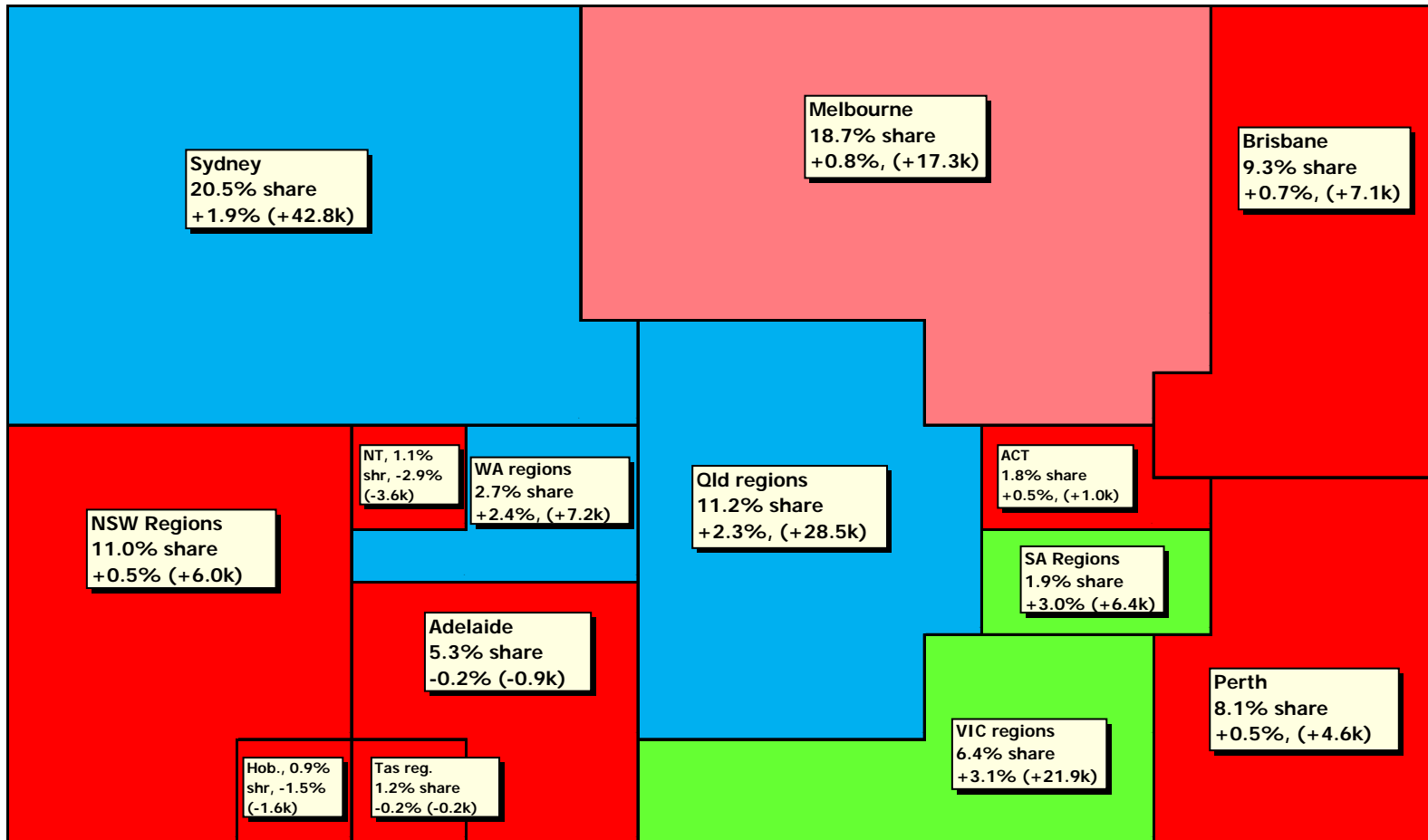
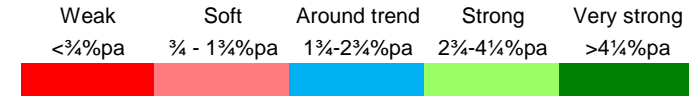


Regional employment heat map – annual jobs growth

Colours below correspond to annual % change, August 2011, using original data.

Employment CAGR - 10 years to August 2011: +2.3%

Legend





Employment by Industry

The industry employment outcomes broadly match the themes we have been highlighting across the economy.

Mining and construction were strong, as were discretionary services.

Manufacturing outcomes were again mixed.

Mining and construction employment is very strong, along with a host of service sectors. Growth in retail employment is solid, whilst non-retail consumer discretionary sectors (such as accommodation and food services, and arts and recreation) are expanding jobs at a rapid pace. Health and social assistance continues to grow strongly, though education slipped surprisingly.

Manufacturing employment was down considerably, with 30.7k jobs lost over the three months to August 2011. Manufacturing employment levels are 5.4% lower than a year ago. But the picture is not uniform across the manufacturing industry. Around ¼ of the manufacturing sector (by employment) registered strong jobs growth over the year to August. In particular, this included sectors linked to the mining boom and infrastructure spending. However, these gains were outweighed by the large declines the remaining ¾ of the manufacturing sector. Job losses were concentrated, with 4 sub-sectors accounting for more than 2/3 of the declines. Machinery & Equipment manufacturing (-12.4k), Textile, Leather, Clothing and Footwear Manufacturing (-10.9k), Pulp, Paper & Converted Paper Product Manufacturing (-7.5k) and Printing (-22.6k) accounted for the lion's share of manufacturing job losses.

Manufacturing employment	% share of	Change	y%ch
<i>Year to August 2011</i>	manuf jobs	'000	
<u>Manufacturing sectors growing jobs</u>			
Petroleum and Coal Product Manufacturing	1.2	4.7	70.7
Beverage and Tobacco Product Manufacturing	3.2	7.4	32.8
Primary Metal and Metal Product Manufacturing	10.0	9.8	11.6
Furniture and Other Manufacturing	6.5	2.8	4.8
Non-Metallic Mineral Product Manufacturing	4.0	1.4	3.8
Growth total	24.8	26.0	12.5
<u>Manufacturing sectors losing jobs</u>			
Basic Chemical and Chemical Product Manufacturing	4.2	-0.1	-0.3
Fabricated Metal Product Manufacturing	5.8	-1.8	-3.2
Polymer Product and Rubber Product Manufacturing	3.3	-1.2	-3.5
Food Product Manufacturing	20.7	-8.4	-4.1
Transport Equipment Manufacturing	8.5	-5.3	-6.2
Wood Product Manufacturing	3.8	-3.0	-7.8
Manufacturing, nfd	7.6	-6.7	-8.4
Machinery and Equipment Manufacturing	11.6	-12.4	-10.1
Textile, Leather, Clothing and Footwear Manufacturing	4.0	-10.9	-22.4
Pulp, Paper and Converted Paper Product Manufacturing	1.5	-7.5	-34.2
Printing (including the Reproduction of Recorded Media)	4.0	-22.6	-37.2
Loss total	75.2	-79.8	-10.1
<u>Manufacturing overall</u>	100	-53.8	-5.4
<i>Source: ABS Cat. No. 6291.0</i>			

Employment by region

Regional jobs growth continues to outpace capital city growth.

The trend identified in the last employment by region report has continued through to August 2011. Capital city jobs markets, in the main, have not been achieving the same pace of jobs growth as the regions. Sydney is the exception. Employment growth in Sydney has risen by 1.9% over the year to August, whereas growth in the rest of New South Wales was only 1.4%. The largest discrepancy was in Victoria, where regional employment growth is booming (+4.3%), outpacing the healthy growth outcome in Melbourne.

As we have highlighted before, the employment opportunities from the mining boom are concentrated in regional areas. Employment spillovers to local economies may be significant for regions hosting mining and energy projects, even though many much of the project workforce may reside in a different region entirely.



International Economic Perspective

“Slowing Growth, Rising Risks” – the IMF lowers its global growth forecasts in 2011 and 2012, but only a touch.

- The IMF lowered its global growth forecasts to 4.0% in both 2011 and 2012. Previous numbers had been 4.3% and 4.5% respectively.
- The main driver of the downward revisions was weaker expansion in the industrialised economies. Emerging market growth is expected to remain brisk.
- Forecast US economic growth for 2011 was lowered to 1.5% from 2.5%, for 2012 to 1.8% from 2.7%. For the Eurozone GDP growth is expected to edge lower to 1.6% in 2011 and followed by just 1.1% in 2012.

The IMF’s new forecasts

The IMF this week published its latest World Economic Outlook and associated global economic forecasts. The title of the document summarizes the general message fairly succinctly, “*Slowing Growth, Rising Risks.*”

As was widely expected the IMF lowered its GDP growth forecasts for the global economy, both for this year and next. The IMF now expects global economic expansion of 4.0% in both 2011 and 2012. Previous numbers had been 4.3% and 4.5% respectively. On the face of it these are hardly dramatic downward revisions. GDP growth of 4% is not bad by the standards of the past 30 years, just not bumper. It certainly does not indicate any sort of “double-dip.”

In terms of the composition of this growth, the pattern remains familiar, with the BRICs and emerging markets generally leading the way. The advanced economies remain the laggards.

Indeed, it is downward revisions to advanced nation growth in both 2011 and 2012 that accounts for much of the reduction in the global numbers. In the opinion of the IMF, the advanced economies will expand by just 1.6% this year and 1.9% in 2012. These forecasts have been revised down from 2.2% and 2.6% back in the summer.

Emerging markets on the other hand are expected to grow 6.4% and 6.1% in 2011 and 2012. China should post numbers of 9.5% and 9.0% compared to the US’s 1.5% and 1.8% and the Eurozone’s 1.6% and 1.1%.

The concerns for the IMF

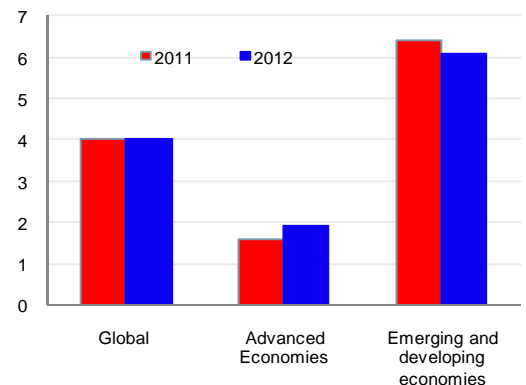
Naturally there are plenty of qualifications and risks highlighted around the central case forecast numbers. These are familiar and have appeared in plenty of official policy-maker speeches and documents of late.

In the words of the IMF, “*global activity has weakened and become more uneven, confidence has fallen sharply recently, and downside risks are growing.*” Risks are now clearly to the downside with potentially “*severe*” repercussions if Europe fails to contain the ongoing debt crisis. The economic recovery has become “*much more uncertain.*”

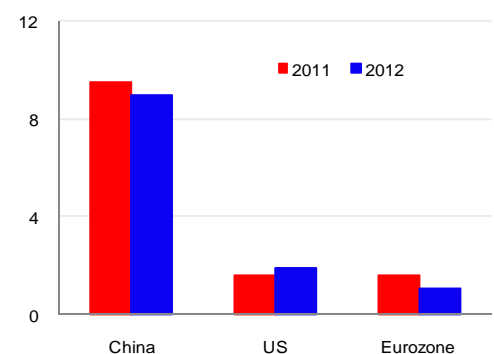
On the European debt crisis, “*leaders must stand by their commitments and do whatever it takes to preserve trust in national policies and the euro.*” The IMF’s forecasts are based on the assumption that European policymakers *do* implement the measures agreed at the July summit and that volatility in financial markets *does not* worsen.



IMF GDP GROWTH FORECASTS



IMF GDP GROWTH FORECASTS





The risks to the IMF's view

Generally speaking there is little particularly contentious in the new set of numbers. It would have been more of a surprise had there not be downward revisions to the advanced country growth forecasts. Key from here is to what extent any of the downside risks to the growth outlook materialise.

In terms of the disappointing state of the global recovery, the obvious culprits are highlighted. Some moderation in global growth was to be expected anyway given the turn in the inventory cycle and ongoing fiscal consolidation in large parts of the industrialised world.

The added headwinds from soaring oil prices due to Middle East tensions and disruptions due to the Japanese earthquake and Tsunami were plausible drivers of additional economic weakness in recent quarters. These have all been well documented and fortunately, the latter at least, are temporary factors which are already in the process of reversing.

The more interesting question marks relate to the longer run dynamics at work and the ongoing rebalancing required, both in many major domestic economies and also the global economy more generally. It is here where there are more worrying question marks about progress, and from where the potential need for additional policy response emerges.

The need for fiscal consolidation in large parts of the industrialised world requires that private sector demand takes on the baton of growth in coming years. Alternatively put growth must rebalance away from the domestic public sector. Effectively this boils down to the household sector and business sector contributing more to economic expansion.

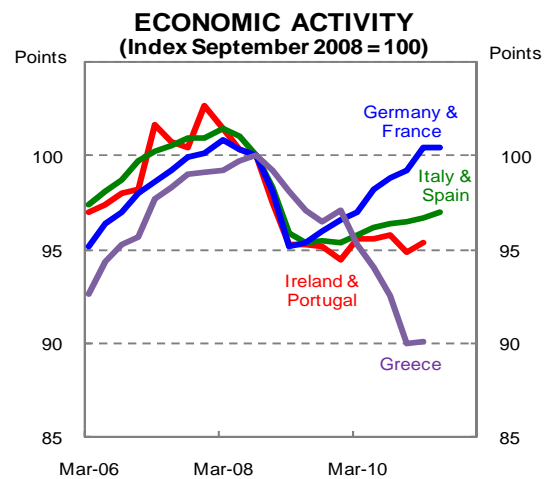
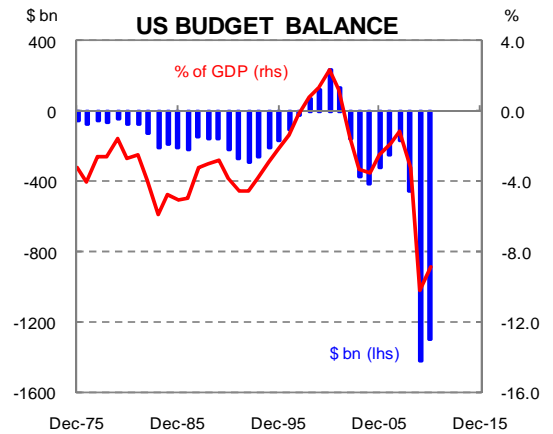
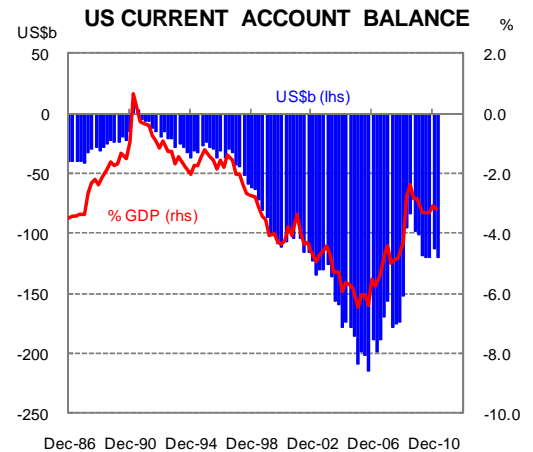
Unfortunately, this is not really happening as yet, particularly on the household side given subdued real income growth, ongoing balance sheet repair and tight bank lending given problems in various domestic banking sectors.

In terms of external rebalancing, there has also been lack of progress which is unhelpful to growth in the advanced economies. A pick-up in external demand would help to offset softer domestic demand in economies such as the US. Unfortunately, this is not materialising, with emerging economies still running large current account surpluses.

Finally, of course, there has been a sharp increase in fiscal and financial uncertainty in recent months. Worries over fiscal sustainability have been simmering away for a while with respect to smaller peripheral European economies. Now investor concern has spilled over to larger sovereigns as well. Fears over sovereigns have spilled over into fears over banks holding the bonds of these sovereigns. The main risk has been that subdued growth and weak fiscal and financial fundamentals fuel each other negatively, increasing the risks of general instability.

In the view of the IMF strong policy action is necessary. Fiscal consolidation must progress, but not too fast to kill off growth or too slow to lack credibility. Financial measures are required to make banks stronger, probably in the form of additional capital buffers from either public or private sectors. Finally, external rebalancing must progress in Asia so that foreign demand contributes more to growth in the advanced economies.

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International Economic Perspective

Bank of England Monetary Policy Update

- September MPC minutes opened the door wide to imminent QE2 in the UK.
- There was no change in the voting pattern this time out, but most of the committee see an expansion of QE as “increasingly probable.”
- While various policy measures were discussed, it was decided that asset purchases would be the preferable option.
- Ongoing deterioration in the UK economic numbers since the September meeting suggests that it is now a case of “when” not “if” the MPC announces additional QE.
- We now expect the MPC to embark on another round of QE in Q4, announcing a GBP50b. expansion of its asset purchase program by November the latest, but quite possibly already at its October 6th meeting.

September MPC minutes

The minutes of the September Bank of England (BoE) Monetary Policy Committee (MPC) meeting contained no changes to the voting pattern of the 9-member committee. But the discussion signalled a significant change in stance and opened the door wide to additional QE.

Most members of the committee believed that it was “increasingly probable that further asset purchases to loosen monetary conditions would become warranted at some point”. It was already a “finely balanced decision whether to embark on further easing” in September.

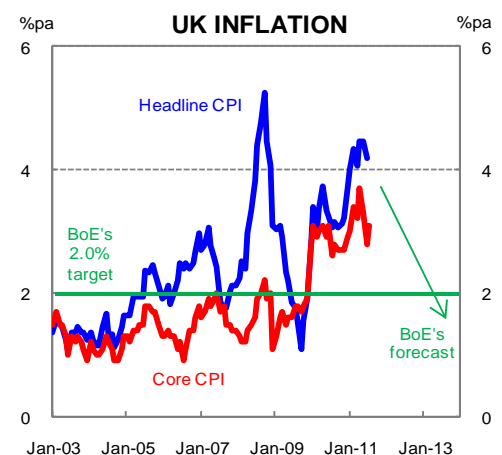
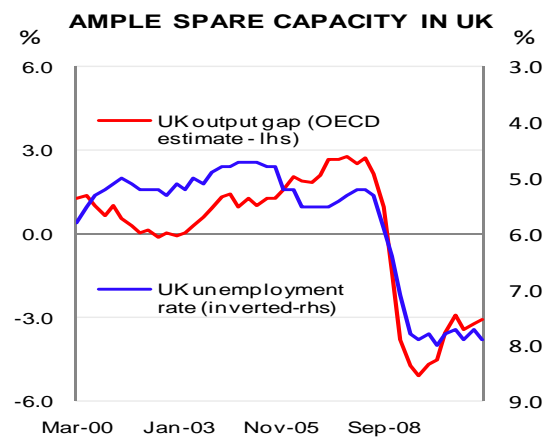
According to most members of the MPC, the recent stresses in the financial markets and economic weakness had “significantly strengthened the case for an immediate resumption of asset purchases.”

Given that economic data have continued to deteriorate since the September MPC meeting, it now appears to be more a case of “when” not “if” the MPC announces further monetary policy ease.

The minutes made it clear that additional asset purchases are the MPC’s favoured option. Various other policy measures were discussed including changing the maturity of the assets in the current £200bn portfolio and explicit guidance on the future path of bank rate. In the view of the MPC none of the other options “appeared to be preferable to a policy of further asset purchases.”

Our new ECB expectations

We have adjusted our BoE policy call and now expect the MPC to announce another round of asset purchases in QIV. We expect the MPC to announce at least a £50bn expansion of the BoE’s asset purchase program in QIV, possibly as early as the 6 October meeting. If not October, the November meeting is a strong possibility. The BoE’s next full quarterly forecasting round is released in November. We are also pushing back our call for the next BoE bank rate hike from QIII 2012 into QI 2013.



Central Bank	Current	End Period					
		Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12
Bank of England (BoE)	0.50	0.50	0.50	0.50	0.50	0.50	0.50
	<i>Old</i>	0.50	0.50	0.50	0.50	0.75	1.00



New Zealand Economic Perspective

NZ QII GDP: Speed bump won't slow NZ economy for long

- QII GDP grows just 0.1%, following a sturdy 0.9% increase in QI.
- Result highlights pockets of weakness remain, underlying momentum slower than initially thought.
- Softer GDP growth reduces urgency for OCR increases, allowing RBNZ to assess offshore developments

QII GDP expanded 0.1%...

QII GDP expanded just 0.1%, in line with our forecast, although weaker than the market expectation of +0.5%. The softer growth follows the previous quarter's 0.9% increase (upwardly revised from 0.8%). Averaging through the volatility, the economy recorded respectable growth of around 0.5% per quarter. This is still a robust performance, given the disruption caused by earthquakes in February and June. Nonetheless, the pace of growth has disappointed, appearing slightly less impressive than initially thought, just a few weeks ago.

...the pace of growth disappoints.

Strong contribution from house sales pick-up.

Driving a large contribution to QII growth was a pickup in house sales activity which underpinned strong growth in real estate and business services. Growth in finance and insurance, although relatively subdued, was also slightly stronger than we expected.

Retail lift added to the momentum.

The buoyant lift in retail activity over QII also added to momentum. Over the first half the year, growth in retail volumes has been surprisingly robust, with strength relatively broad based across regions. Nonetheless, there was likely an element of earthquake damage replacement contributing to QII's retail strength. Over the coming quarters, the hospitality industry will benefit from a huge lift in activity due to the influx of overseas visitors arriving for the Rugby World Cup tournament.

Good grass growth helped dairy.

Good grass growing conditions helped extend the dairy season over QII, propelling agricultural growth by 4.3%. This strength largely reflects a stronger than usual performance at the end of season (typically a low production period).

Weak primary activity elsewhere.

However, activity in the remaining primary industries was weak, with declines in fishing and mining output, along with stalled growth in forestry activity.

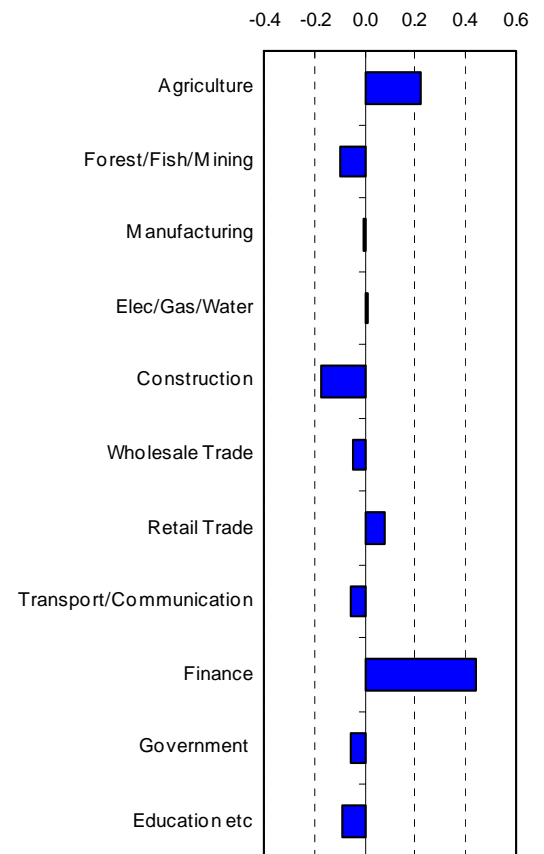
Construction and wholesale trade weak.

Much of the weakness in GDP was centred in construction and wholesale trade activity, as already foreshadowed in data released earlier in the month. Construction contracted 4.3%, with the weakness led by a sharp decline in residential construction. We continue to expect residential construction will stabilise over the rest of 2011, before lifting strongly over 2012 and 2013 on earthquake reconstruction activity.

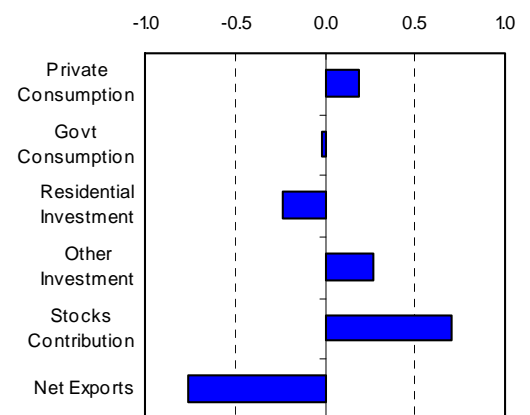
Core manufacturing growth slowed.

Core manufacturing growth slowed over QII, following robust growth over the previous 2

Q2 2011 PRODUCTION GDP
 (pp contribution to quarterly % change)



Q2 2011 EXPENDITURE GDP
 (pp contribution to quarterly % change)





Communication weak.

quarters. The outlook for manufacturing remains relatively upbeat, and we expect to see continued, albeit more modest, growth over the coming year.

Communications remained an area of weakness, falling 1.6% due to declines in telecommunication activity and postal services. This has been an area of chronic weakness over recent years. Measurement issues with telecommunication and internet usage may be underestimating activity. Meanwhile, postal activity appears to be suffering from a long-run trend decline.

Business investment increased.

Business investment increased 1.3% in QII. As expected, there were sharp declines in the lumpy transport component. However, this was offset by strength in other areas. Other Construction picked up 7.7%, following on from the previous quarter's 3% increase. This is likely to be related to earthquake repairs on infrastructure. Encouragingly, there was also a 4.7% increase in plant and machinery equipment investment. Business confidence surveys have shown an improvement in sentiment in recent months. Firms' investment intentions point to a continued recovery in business investment over the coming year, as businesses become more confident about the recovery in demand ahead and look to expand operations.

Exports slightly weaker than expected.

Exports were slightly weaker than expected, largely due to a sharper than expected decline in exports of services which fell 5.8%. This was largely due to a decline in visitor numbers as a result of the February earthquake and June's ash cloud travel disruption. Over the second half of the year, we expect exports of services to be a key driver of growth, with increased visitor numbers due to the Rugby World Cup.

Rugby World Cup to boost QIII.

Looking ahead, over the second half of 2011 Rugby World Cup related activity will underpin GDP growth. Moving onto 2012, we expect the recovery in underlying demand to become more apparent. Earthquake reconstruction activity should also add to activity from the second half of 2012.

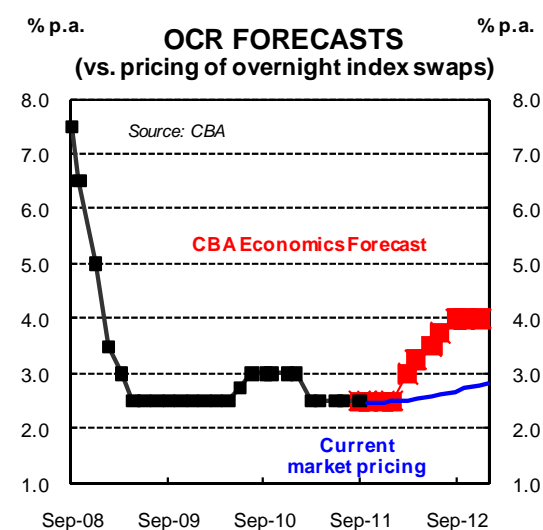
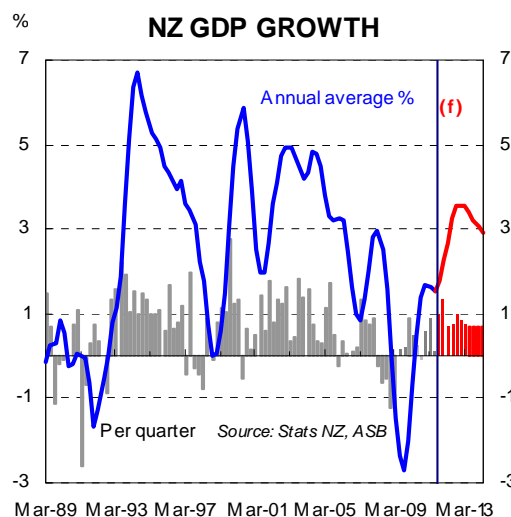
No urgency for RBNZ.

There are few fresh implications from this number for monetary policy. The RBNZ had indicated that data subsequent to the finalising of its MPS forecasts meant the outcome was likely to be lower than its published 0.6% forecast. Moreover, the pivotal influence of global debt issues meant the RBNZ was already unlikely to lift interest rates this year. We see the GDP release as merely reinforcing the apparent lack of urgency the RBNZ has to lift rates.

Given widely-held expectations that GDP will be materially stronger in the second half of 2011, we do not expect the outcome will materially affect the RBNZ's view of NZ's recovery. The RBNZ's growth outlook has swung from being at the optimistic end to (in the September MPS) the conservative end of the range of expectations. Our own forecast for QIII GDP remains the same at 1%, and followed by 1.3% in QIV, boosted by the Rugby World Cup. Beyond that, we would characterise the economic growth as gradual.

We continue to expect that the RBNZ will wait until March 2012 to lift the OCR by 50bp and for the OCR to peak at 4% by end-2012.

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The Week Ahead

Calendar - Australasia, Japan and China

Date	Time			Period	Unit	Last	Forecast	
	AEST	Econ	Event				Market	CBA
Mon 26 Sep	07:45	NZ	Trade balance	Aug	NZD mn	129	-321	~
	07:45	NZ	Exports	Aug	NZD bn	3.72	3.44	~
	07:45	NZ	Imports	Aug	NZD bn	3.59	3.78	~
Tue 27 Sep	~	JN	Small business confidence	Sep	Index	46.4	~	~
	12:00	CH	Industrial profits	Aug	ytd y%ch	28.3	~	~
Wed 28 Sep	11:00	AU	HIA new home sales	Aug	m%ch	-8.0	~	~
Thu 29 Sep	09:50	JN	Retail trade	Aug	m%ch	-0.3	0.2	~
					y%ch	0.6	-0.8	~
Fri 30 Sep	07:45	NZ	Building permits	Aug	m%ch	13.0	-1.5	~
	09:30	JN	Jobless rate	Aug	%	4.7	4.7	
	09:30	JN	National CPI	Aug	y%ch	0.2	0.1	
	09:30	JN	National CPI ex food, energy	Aug	y%ch	-0.5	~	~
	09:50	JN	Industrial Production	Aug P	m%ch	0.4	1.1	~
					y%ch	-3.0	0.3	~
	10:30	AU	RP Data-Rismark house px s.a.	Aug	%	-0.6	~	~
	11:00	NZ	NBNZ business confidence	Sep	Index	34.4	~	~
	11:30	AU	Private sector credit	Aug	m%ch	0.2	~	0.2
					y%ch	2.7	~	2.8
	11.30	AU	ABS Financial accounts	QII	~	~	~	~
	12:00	NZ	Money supply M3	Aug	y%ch	6.3	~	~
	12:30	CH	HSBC manufacturing PMI	Sep	Index	49.9	~	~
	14:00	JN	Vehicle production	Aug	y%ch	-8.9	~	~
	15:00	JN	Construction orders	Aug	y%ch	5.7	~	~
	15:00	JN	Housing starts	Aug	y%ch	21.2	~	~
	Sat 1 Oct	11:00	CH	PMI manufacturing	Sep	Index	50.9	~

Calendar – North America & Europe

Please note all days and times are UK time, not local release day/times

Date	UK			Period	Unit	Last	Forecast	
	Time	Econ	Event				Market	CBA
Mon 26 Sep	09:00	GE	IFO - business climate	Sep	Index	108.7	107.0	~
	10:00	GE	Retail sales	Aug	m%ch	0.3	-0.7	~
	13:30	US	Chicago Fed nat activity index	Aug	Index	-0.06	-0.4	~
	14:30	EC	ECB announces bond purchases					
	14:30	US	Fed's Bullard speaks in New York					
	15:00	US	New home sales	Aug	'000	298	295	~



	15:30	US	Dallas Fed manufacturing activity	Sep	Index	-11.4	-8.0	~
	20:00	US	Fed's Kocherlakota Speaks on Debt Panel in Chicago					
Tue 27 Sep	07:00	GE	GfK consumer confidence survey	Oct	Index	5.2	5.0	~
	07:00	SZ	UBS consumption indicator	Aug	Index	1.3	~	~
	10:05	GE	Import price index	Aug	m%ch	0.8	~	~
	14:00	US	S&P/CS composite-20 city home value	Jul	y%ch	-4.5	-4.4	~
	15:00	US	Consumer confidence	Sep	Index	44.5	46.5	~
	15:00	US	Richmond Fed manufacturing index	Sep	Index	-10.0	-9.0	~
	17:30	US	Fed's Lockhart speaks on economy in Jacksonville, Florida					
Wed 28 Sep	~	UK	BOE publishes statement on financial policy committee meeting					
	~	SZ	SNB's Jordan speaks in Basel					
	~	GE	CPI	Sep	y%ch	2.4	2.4	~
	07:40	US	Fed's Rosengren speaks at Swedbank seminar in Stockholm					
	13:00	LX	ECB's Mersch speaks at Luxembourg two-day event					
	13:30	US	Durable goods orders	Aug	%	4.1	-1.0	~
	13:30	US	Durables ex transportation	Aug	%	0.8	0.2	~
	13:30	US	Cap goods orders nondef ex air	Aug	%	-1.5	~	~
	22:00	US	Fed's Bernanke speaks in Cleveland, Ohio					
Thu 29 Sep	~	GE	German lawmakers vote on European Rescue Fund changes					
	07:50	US	Fed's Rosengren Speaks on Bank Regulation in Stockholm					
	09:30	UK	Net consumer credit	Aug	£bn	0.2	0.2	~
	10:00	EC	Business climate indicator	Sep	Index	0.1	-0.2	~
	13:30	US	Fed's Plosser Speaks on Economy in Radnor, Pennsylvania					
	13:30	US	GDP (annualized)	QII T	q%ch	1.0	1.2	
	13:30	US	Initial jobless and continuing claims	Sep	'000	~	~	~
	15:00	US	Pending home sales	Aug	m%ch	-1.3	-2.1	~
	16:00	US	Kansas City Fed manufacturing activity	Sep	Index	~	~	~
	18:00	US	Fed's Lockhart speaks in Atlanta					
Fri 30 Sep	00:01	UK	GfK consumer confidence survey	Sep	Index	-31.0	-32.0	~
	10:00	EC	CPI estimate	Sep	y%ch	2.5	2.5	~
	10:00	EC	Unemployment rate	Aug	%	10.0	10.0	~
	10:30	SZ	KOF Swiss leading indicator	Sep	Index	1.6	~	~
	13:30	US	Personal income	Aug	%	0.3	0.1	~
	13:30	US	Personal spending	Aug	%	0.8	0.2	~
	13:30	CA	GDP	Jul	y%ch	2.0	2.3	~
	13:30	US	PCE core	Aug	y%ch	1.6	1.7	~
	14:45	US	Chicago purchasing manager	Sep	Index	56.5	56.5	~
	14:55	US	University of Michigan confidence	Sep	Index	57.8	57.8	~
	16:00	US	Fed's Bullard speaks in San Diego					



Calendar – Key Events To Watch

Australia and New Zealand

Monday 26 September

NZ Trade Balance, August, NZD mn, (f) -500 (129 prev)

We expect a trade deficit of \$500 million in August. However, the deficit is seasonal, and on a seasonally-adjusted basis we expect a small trade surplus of around \$70 million. Throughout the second half of the year, agricultural and horticultural commodity exports go into a seasonal decline. Beyond the seasonal effects, we expect to see some decline in dairy exports, largely reflecting lower prices. Log exports may also be constrained, with anecdotes of weak Chinese demand over the middle part of the year.

Meanwhile, imports tend to increase over the second half of the year, so we are expecting to see some pick up in July. Beyond seasonal effects, improved business confidence points to increased investment, so we also expect to see an increase in capital goods imports over the coming months. In addition, continued import of new aircraft over the coming year will continue to add to import volatility (although we have not made any specific allowances for August). Petrol imports were unusually low in July, and we expect some payback in August.

Thursday 29 September

AU Population Growth, QI, q/y%ch, (0.3/1.5 prev)

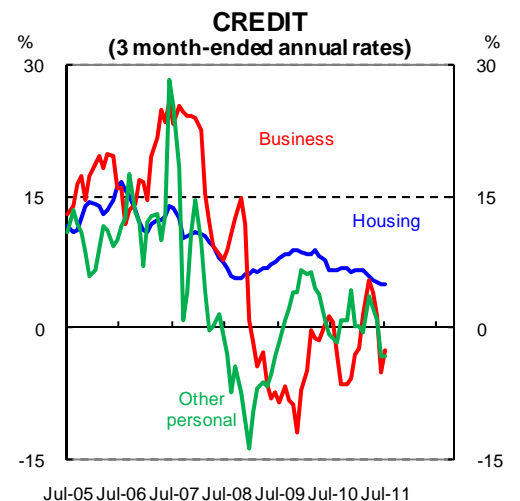
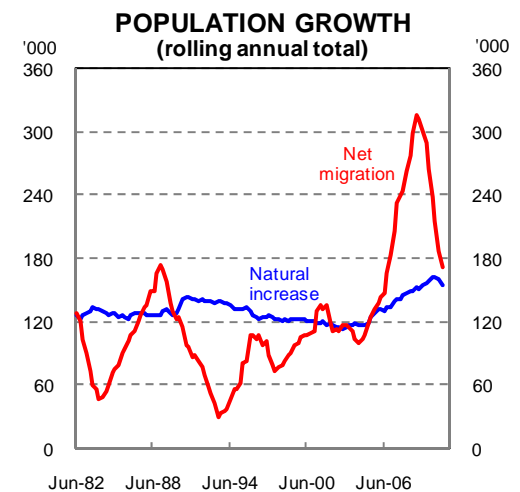
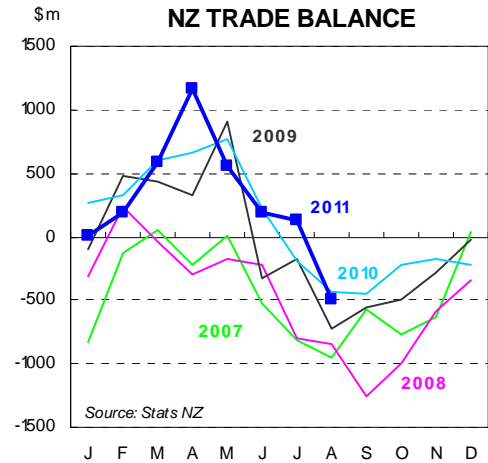
Australia's population growth continued to moderate in QIV 2010, with the population rising by 69.7k to 22.48mn. The annual growth rate in the QIV 2010 was 1.47% (325,500 persons), the lowest annual growth rate since QIV 2005. Population growth in Western Australia defied the trend in QIV, with growth of 2.1%.

Net overseas migration has slowed significantly, driving most of the decline in the population growth rate. The lift in population growth from natural increase has been insufficient to offset the decline. Natural increase has lifted due to a strong rise in births. However population growth from this source is more likely to exacerbate, rather than assist with alleviating, skills shortages and pressure on the labour market. Thankfully, the immigration department is forecasting a lift in net overseas migration over coming years.

Friday 30 September

AU Private Sector Credit, Aug, m/y%ch, (f) 0.2/2.8 (0.2/2.7 prev)

Private sector credit grew in July, lifting by just 0.2%. Positive growth returned due to a flat outcome for business credit in the month. Business credit growth remains negative, though the trend is showing signs of improvement. This trend is likely to be tested in the August data, which is likely to show some early signs of impact from the heightened turmoil in financial markets. Business and other personal credit growth are most likely to be affected. Household credit growth is likely to continue its steady increase, though the pace of growth in in this category has been moderating for some time. Overall, we are expecting another modest growth outcome for August, with a lift of 0.2% in total credit.





Friday 30 September

NZ Building Consents, Aug

- Dwelling Consents, m%ch, (13 prev)
- Non-Residential Consents, annual avg%, (-1 prev)

Residential building consents lifted a robust 13% over July, on the back of both an increased number of apartment consents and recovery in core consent issuance. Excluding the volatile apartment component, consents increased 6.3% over the month – rebounding from the previous month's 4.3% decline. While the level of consents issued remains extremely low, the pick-up in July is an encouraging sign. Over 2011, strong house sales data and anecdotes of tight supply in the rental market suggest demand for new housing construction is starting to increase. We expect to see a continued increase in underlying housing construction activity over the coming year.

There was a surge in the value of non-residential issuance in July, largely reflecting public sector projects. In contrast, consent issuance for retail outlets and office buildings remains fairly subdued, suggesting a degree of caution remains amongst businesses in regards to investment on buildings. Overall, the results point to a soft outlook for private non-residential construction over the coming year.

Friday 30 September

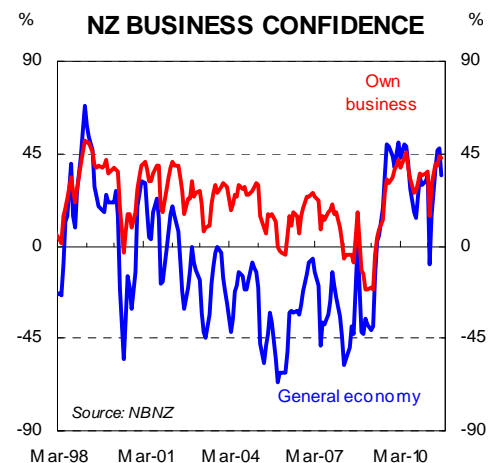
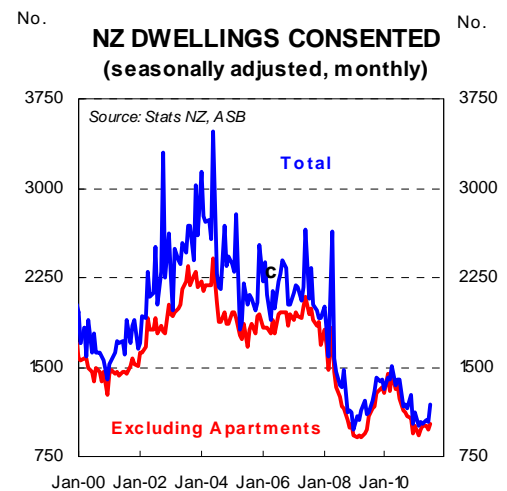
NZ National Bank Business Outlook, Sep, Index

- Headline, (34.4 prev)
- Own Activity, (43.3 prev)

Business confidence dropped in August, reflecting the heightened uncertainty in global financial markets in recent weeks. While the own activity measure held up, there was a weakening across a broad range of activity indicators, including profitability expectations.

In particular, hiring intentions halved although a net 9.1% of businesses still expect to increase staff numbers over the coming months. There was also a softening in investment expectations. It is likely the unrest in global markets have made businesses more cautious in regards to expanding their operations. While we see some potential for further easing in business confidence over the coming months, we expect business confidence will hold up at levels consistent with a gradual recovery in underlying activity.

Inflation indicators generally pointed to an easing in inflation pressures, which should be of some comfort to the RBNZ. There was a drop in pricing intentions and capacity utilisation, suggesting little sign yet of capacity pressures in the NZ economy.





International

Tuesday 27 September

US Consumer Confidence, Sep, Index, (44.5 prev)

US consumer confidence has slumped again following the debt ceiling debacle and the ongoing weakness in the labour market. Low confidence is consistent with weak consumer spending. Consumer spending accounts for about 70% of the US economy. Therefore, we expect the US economy to stay weak in the near term. The low level of confidence makes the US economy exposed to an external shock, such as instability in European banking and sovereign debt markets pushing down equity prices. We also see a risk the US Federal Reserve implements further stimulus before the end of the year following its decision this month to extend the duration of its Treasury holdings. Given the concern markets have about the US economy, another fall in confidence would likely lead to further safe haven flows into USD.

Thursday 29 September

EZ Confidence Indicators, Sep, Index

Aggregate Euro-zone confidence readings across consumer, industrial and service sectors are released for September. The flash consumer confidence reading has already been released and softened more than expected, falling to -18.9 from -16.5. This was the lowest reading since QIII 2009.

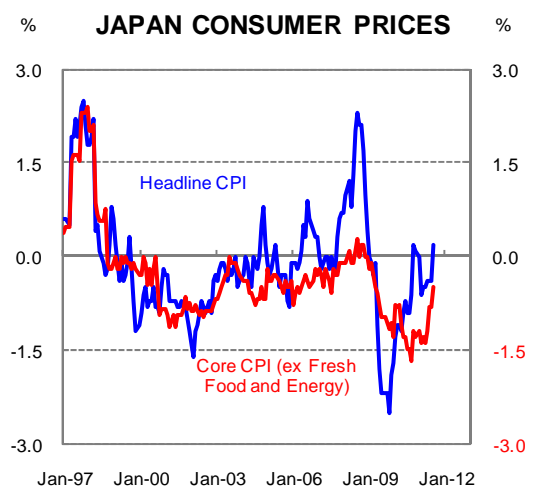
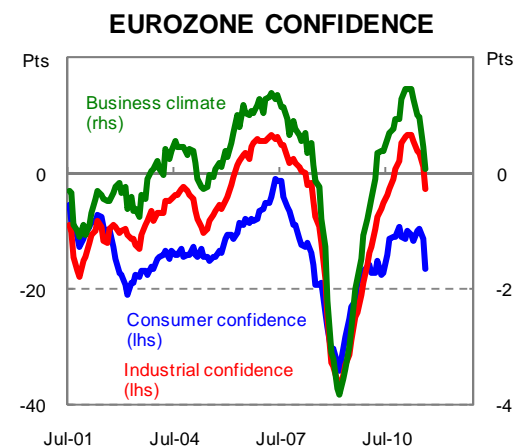
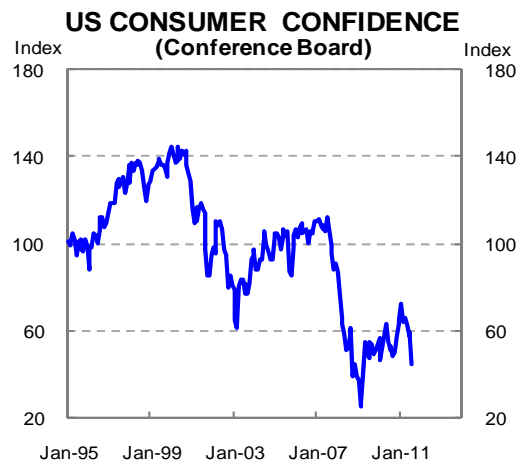
A similar pattern is expected across the other surveys covering general economic confidence, industrial confidence and services confidence. The flash Eurozone PMIs for September showed further declines. The aggregate Eurozone composite PMI dipped under the 50 mark for the first time since July 2009.

Friday 30 September

JP CPI, Aug, y%ch, (0.1 prev)

There is very little evidence supply shortages following the tsunami have raised Japanese consumer prices significantly. Of the ten elements separately identified in Japan's CPI, only one, 'recreation and reading', have prices increased (and only by 0.6% since March). To the extent isolated supply shortages exist, they are unlikely to lead to generalised price pressures that push inflation to high rates (by Japanese standards) for an extended period. The upshot is we see downside risks to the Bank of Japan's (BoJ) inflation forecast for 2012.

In addition, re-basing of the CPI in August lowered the rate of inflation to only 0.1%pa. A similar result is expected in August. The revision lower of Japan's CPI makes the BoJ's job of raising expectations for the CPI from deflation to inflation more difficult.





Friday 30 September

JP Industrial Production, Aug P, y%ch, (-3.0 prev)

Industrial production is recovering from the drop earlier in the year following the Japanese natural disaster, led by greater vehicle production. Industrial production has lifted every month since March's 15.5% (MoM) contraction, but remains down on year-ago levels. In July, industrial production rose 0.4% from a month earlier, to be 3% below year-ago levels. Data is expected to show the recovery continued in August.

Overall, industrial production was significantly down on pre-GFC levels prior to the disaster. The strong JPY is making Japanese products less competitive. Ongoing yen strength, combined with the current global uncertainty will limit the recovery in industrial production.

Friday 30 September

US Personal Income, Spending & Prices, Aug

We see downside risks to personal spending for August because the strong increase in July was 'paid for' by running down savings. Judging by the recent slump in consumer confidence and the weakening labour market, we expect consumers to rebuild savings by reining in spending. In addition, the weak labour market should keep a lid on growth in incomes. The Fed's preferred measure of core inflation is included in this release. US economists expect a small acceleration to 1.7%pa which is at the bottom end of the Fed's implicit inflation target. Inflation is a lagging indicator of the economy. The question for policy makers is whether the recent deceleration in US economic growth pushes inflation back down in 2012. Given the concern markets have about the US economy, surprise fall in core inflation would likely lead to further safe haven flows into USD.

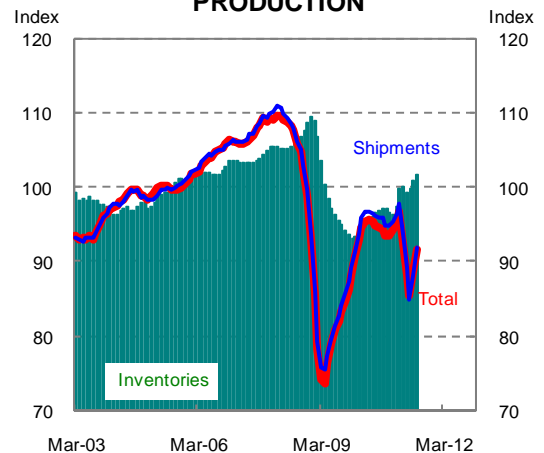
Friday 30 September

CA GDP, July, m%ch, (0.2 prev)

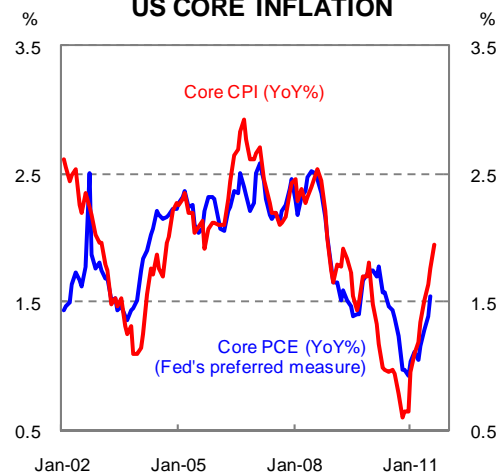
The Canadian economy contracted in QII of 2011, after seven consecutive quarters of expansion. QII GDP dipped 0.1 % (QoQ), or -0.4% at a seasonally adjusted annualised rate. Modest expansion in monthly GDP growth is expected in July.

We see significant downside risks to medium-term Canadian growth. US weakness is likely to weigh on the Canada, via the export sector. Canada sends around 75% of exports to the US, and exports account for 38% of Canadian GDP. In addition to the downside risks to the export sector, there is a risk private consumption, which accounts for 63% of Canadian GDP, continues to grow only modestly in the months ahead.

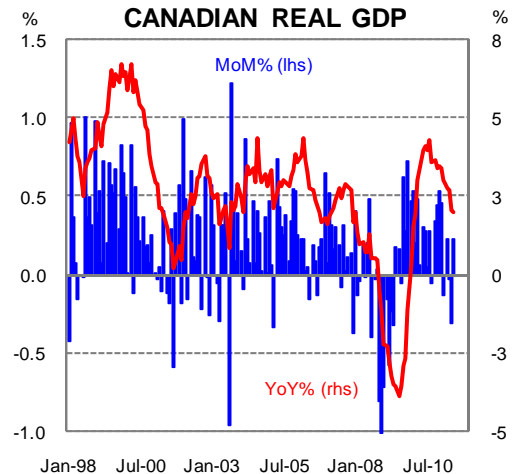
JAPAN INDUSTRIAL PRODUCTION



US CORE INFLATION



CANADIAN REAL GDP

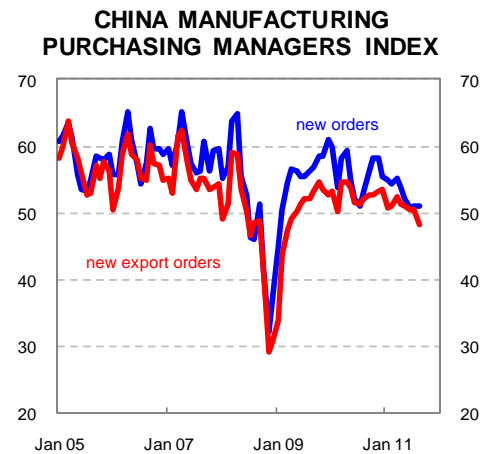




Saturday 1 October

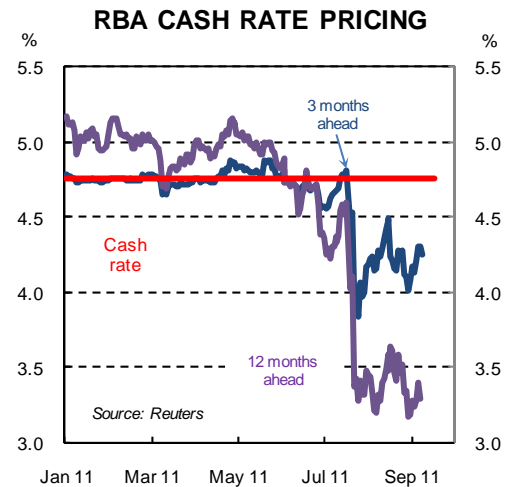
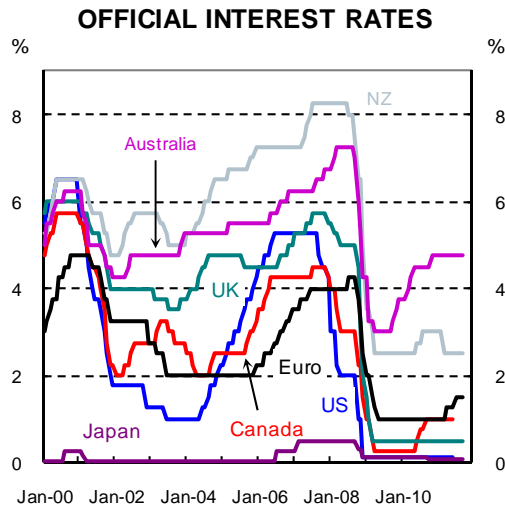
CH PMI Manufacturing, Sep, Index, (50.9 prev)

The August headline purchasing managers index (PMI) was a stronger than expected 50.9, driven mainly by resilient new orders. By contrast, new export orders dipped into contraction territory for the first time since April 2009. Weaker demand from developed economies led the falls. Nevertheless, the overall data suggests a continued stabilization in manufacturing activity. On that note, August industrial production growth, at 13.5% (YoY), was roughly in line with its average pace in the past 12 months. As such, we expect the manufacturing PMI to edge higher to 51.2 in September.





Monetary Policy



Country	Last Move	Next Meeting and Forecast	CBA View								
Australia (RBA)	25bpt rise to 4.75% on 7 November 2010.	<p>■ 4 October, 2011</p> <table border="1"> <thead> <tr> <th>Sep '11</th> <th>Dec '11</th> <th>Mar '12</th> <th>Jun '12</th> </tr> </thead> <tbody> <tr> <td>4.75%</td> <td>4.75%</td> <td>5.00%</td> <td>5.00%</td> </tr> </tbody> </table>	Sep '11	Dec '11	Mar '12	Jun '12	4.75%	4.75%	5.00%	5.00%	The QII CPI confirmed the inflation trend has turned up. Rate rises are likely. We expect a rate rise in February. The cash rate is expected to reach 5.50% by 2013.
Sep '11	Dec '11	Mar '12	Jun '12								
4.75%	4.75%	5.00%	5.00%								
US (FOMC)	75-100bpt cut to 0-0.25% on 16 December 2008.	<p>■ 2 November, 2011</p> <table border="1"> <thead> <tr> <th>Sep '11</th> <th>Dec '11</th> <th>Mar '12</th> <th>Jun '12</th> </tr> </thead> <tbody> <tr> <td>0-0.25%</td> <td>0-0.25%</td> <td>0-0.25%</td> <td>0-0.25%</td> </tr> </tbody> </table>	Sep '11	Dec '11	Mar '12	Jun '12	0-0.25%	0-0.25%	0-0.25%	0-0.25%	Given the loss of momentum in the US economy, particularly in the labour market, we expect the Fed to maintain the size of its balance sheet until early 2013. The first Fed funds hike is not expected until mid 2013.
Sep '11	Dec '11	Mar '12	Jun '12								
0-0.25%	0-0.25%	0-0.25%	0-0.25%								
Eurozone (ECB)	25bpt rise to 1.50% on 7 July 2011.	<p>■ 6 October, 2011</p> <table border="1"> <thead> <tr> <th>Sep '11</th> <th>Dec '11</th> <th>Mar '12</th> <th>Jun '12</th> </tr> </thead> <tbody> <tr> <td>1.50%</td> <td>1.50%</td> <td>1.50%</td> <td>1.75%</td> </tr> </tbody> </table>	Sep '11	Dec '11	Mar '12	Jun '12	1.50%	1.50%	1.50%	1.75%	The recent deterioration in Eurozone economic indicators suggests that the ECB will pause its process of monetary policy normalisation. We expect the ECB to remain on hold until QII 2012.
Sep '11	Dec '11	Mar '12	Jun '12								
1.50%	1.50%	1.50%	1.75%								
UK (MPC)	50bpt cut to 0.5% on 5 March 2009.	<p>■ 6 October, 2011</p> <table border="1"> <thead> <tr> <th>Sep '11</th> <th>Dec '11</th> <th>Mar '12</th> <th>Jun '12</th> </tr> </thead> <tbody> <tr> <td>0.50%</td> <td>0.50%</td> <td>0.50%</td> <td>0.50%</td> </tr> </tbody> </table>	Sep '11	Dec '11	Mar '12	Jun '12	0.50%	0.50%	0.50%	0.50%	Ongoing deterioration in the UK economy suggests that another round of QE is likely. We expect a GBP50bn expansion of the asset purchase program in QIV 2011, possibly as early as October.
Sep '11	Dec '11	Mar '12	Jun '12								
0.50%	0.50%	0.50%	0.50%								
NZ (RBNZ)	50bpt cut to 2.5% on 10 March.	<p>■ 27 October, 2011</p> <table border="1"> <thead> <tr> <th>Sep '11</th> <th>Dec '11</th> <th>Mar '12</th> <th>Jun '12</th> </tr> </thead> <tbody> <tr> <td>2.50%</td> <td>2.50%</td> <td>3.00%</td> <td>3.50%</td> </tr> </tbody> </table>	Sep '11	Dec '11	Mar '12	Jun '12	2.50%	2.50%	3.00%	3.50%	The escalating debt crisis in Eurozone is dominating the RBNZ's outlook, and we expect the RBNZ will leave the OCR on hold until March next year. We expect a 50bpt OCR increase in March.
Sep '11	Dec '11	Mar '12	Jun '12								
2.50%	2.50%	3.00%	3.50%								
Canada (BoC)	25bpt rise to 1.00% on 8 September 2010.	<p>■ 25 October, 2011</p> <table border="1"> <thead> <tr> <th>Sep '11</th> <th>Dec '11</th> <th>Mar '12</th> <th>Jun '12</th> </tr> </thead> <tbody> <tr> <td>1.00%</td> <td>1.00%</td> <td>1.00%</td> <td>1.25%</td> </tr> </tbody> </table>	Sep '11	Dec '11	Mar '12	Jun '12	1.00%	1.00%	1.00%	1.25%	Softness in the US economy is likely to effect the Canadian economy given the strong trade ties. We expect the BoC to remain on hold until mid 2012 before it embarks on a slow and steady removal of policy accommodation.
Sep '11	Dec '11	Mar '12	Jun '12								
1.00%	1.00%	1.00%	1.25%								
Japan (BoJ)	0-10bpt cut to 0-0.1% on 5 October 2010.	<p>■ 7 October, 2011</p> <table border="1"> <thead> <tr> <th>Sep '11</th> <th>Dec '11</th> <th>Mar '12</th> <th>Jun '12</th> </tr> </thead> <tbody> <tr> <td>0-0.10%</td> <td>0-0.10%</td> <td>0-0.10%</td> <td>0-0.10%</td> </tr> </tbody> </table>	Sep '11	Dec '11	Mar '12	Jun '12	0-0.10%	0-0.10%	0-0.10%	0-0.10%	In response to the recent natural disasters, the Bank of Japan has implemented further quantitative easing measures. Monetary policy in Japan is likely to remain accommodative for some time.
Sep '11	Dec '11	Mar '12	Jun '12								
0-0.10%	0-0.10%	0-0.10%	0-0.10%								



Forecasts - Economic

	Fiscal Years						Calendar Years						
	2007/08 (a)	2008/09 (a)	2009/10 (a)	2010/11 (a)	2011/12 (f)	2012/13 (f)	2006 (a)	2007 (a)	2008 (a)	2009 (a)	2010 (a)	2011 (f)	2012 (f)
Economic Activity													
Private final demand	6.4	0.1	0.8	3.5	4.8	5.2	3.6	7.1	3.1	-0.7	2.2	4.6	5.0
<i>Of which: Household spending</i>	4.7	0.2	2.1	3.3	2.8	3.1	3.4	5.5	1.9	1.0	2.8	3.1	2.9
Dwelling investment	1.2	-1.9	2.1	2.6	2.2	-1.1	-3.0	3.0	2.1	-4.2	4.2	3.3	0.0
Business investment	15.8	1.4	-4.9	6.2	13.4	14.2	8.5	16.1	9.6	-5.4	-0.1	11.6	14.1
Public final demand	4.2	3.6	6.7	4.5	1.5	-0.1	3.7	3.4	6.3	1.8	9.1	1.8	0.5
Domestic final demand	5.9	0.9	2.1	3.8	4.0	4.0	3.7	6.3	3.8	-0.1	3.8	3.9	3.9
Inventories (contrib to GDP)	0.0	-0.4	0.3	0.4	-0.2	0.1	-0.4	0.6	-0.3	-0.4	0.4	0.4	-0.3
GNE	5.9	0.4	2.4	4.1	3.8	4.0	3.2	6.9	3.5	-0.5	4.2	4.2	3.6
Exports	4.0	2.6	5.3	0.2	8.3	7.6	2.2	2.4	4.7	2.6	5.7	-0.1	10.4
Imports	14.6	-3.3	5.1	10.7	9.3	8.6	6.9	12.2	11.5	-9.0	13.7	10.1	8.6
<i>Net exports (contrib to GDP)</i>	-2.1	1.4	0.1	-2.4	-0.4	-0.4	-0.9	-2.0	-1.5	2.7	-1.6	-2.4	0.0
GDP	3.8	1.4	2.3	1.9	3.5	3.7	2.6	4.6	2.6	1.4	2.7	2.0	4.0
Prices & Wages													
CPI	3.4	3.1	2.3	3.1	2.9	3.1	3.5	2.3	4.4	1.8	2.8	3.3	2.9
Underlying CPI	3.7	4.3	3.1	2.4	3.2	3.2	2.8	2.9	4.4	3.7	2.5	2.8	3.2
AWOTE	4.9	5.5	5.6	4.2	4.8	3.9	3.4	4.8	4.8	5.7	4.9	4.5	4.2
WPI	4.1	4.1	3.0	3.8	4.0	3.9	4.1	4.0	4.2	3.6	3.3	3.9	4.0
Real h/hold disposable income	3.0	8.6	0.9	5.2	2.9	2.8	5.6	6.3	4.9	5.8	2.1	4.8	2.4
Labour Market													
Employment	3.0	1.6	1.4	2.9	0.9	1.8	2.6	3.1	2.8	0.7	2.7	1.8	1.2
Unemployment rate	4.2	4.9	5.5	5.1	5.2	5.0	4.8	4.4	4.3	5.6	5.2	5.1	5.2
External Accounts													
Current Account: \$bn	-74.5	-38.5	-53.4	-33.8	-21.6	-23.1	-55.2	-70.3	-55.3	-52.9	-36.0	-29.6	-21.5
% of GDP	-6.3	-3.1	-4.2	-2.4	-1.4	-1.4	-5.3	-6.2	-4.5	-4.2	-2.7	-2.1	-1.4



Forecasts - Financial

End Period	Interest Rates					Exchange Rates				
	Cash Rate	90-day Bank Bill	180-day Bank Bill	3-year Bond	10-year Bond	USD versus AUD	JPY	EUR	GBP	NZD
Dec-07	6.75	7.24	7.36	6.80	6.33	0.88	111.7	1.46	1.98	0.77
Mar-08	7.25	7.86	7.96	6.16	6.05	0.91	99.7	1.58	1.98	0.79
Jun-08	7.25	7.84	7.96	6.72	6.45	0.96	106.2	1.58	1.99	0.76
Sep-08	7.00	7.32	7.04	5.07	5.40	0.79	106.1	1.41	1.78	0.67
Dec-08	4.25	4.15	0.00	3.29	3.99	0.70	90.7	1.40	1.46	0.58
Mar-09	3.25	3.14	3.06	3.37	4.42	0.69	99.0	1.33	1.43	0.56
Jun-09	3.00	3.19	3.31	4.75	5.52	0.81	96.4	1.40	1.65	0.65
Sep-09	3.00	3.38	3.78	5.04	5.36	0.88	89.7	1.46	1.60	0.72
Dec-09	3.75	4.28	4.47	5.06	5.64	0.90	93.0	1.43	1.62	0.72
Mar-10	4.00	4.49	4.76	5.39	5.78	0.92	93.4	1.35	1.52	0.71
Jun-10	4.50	4.92	5.00	4.56	5.09	0.84	88.4	1.22	1.49	0.68
Sep-10	4.50	5.01	5.20	4.82	4.96	0.97	83.5	1.36	1.57	0.73
Dec-10	4.75	5.04	5.23	5.30	5.55	1.02	81.1	1.34	1.56	0.78
Mar-11	4.75	4.93	5.01	5.07	5.49	1.03	83.1	1.42	1.60	0.76
Jun-11	4.75	5.03	5.07	4.78	5.21	1.07	80.6	1.45	1.61	0.83
Sep-11	4.75	4.80	4.70	3.80	4.40	0.98	76.3	1.35	1.54	0.78
Dec-11	4.75	4.90	5.00	4.50	4.70	1.04	77.0	1.39	1.60	0.82
Mar-12	5.00	5.10	5.20	4.65	4.70	1.07	77.0	1.43	1.62	0.83
Jun-12	5.00	5.20	5.30	4.90	4.80	1.08	77.0	1.44	1.64	0.84
Sep-12	5.25	5.40	5.50	5.05	4.90	1.08	78.0	1.44	1.64	0.84
Dec-12	5.25	5.50	5.60	5.15	5.00	1.08	79.0	1.43	1.62	0.84

Forecast

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