Global Markets Research

Economics: Daily Alert

10 June 2011

- US claims for unemployment insurance (jobless claims) rose by 1,000 to 427,000 in the latest week. Economists were looking for a result near 415,000. But the US trade deficit narrowed from $46.82bn to $43.68bn in April, far better than expectations of a $48.8bn deficit. Exports rose 1.3pct with imports down 0.4pct. And US household wealth rose by $943bn in the March quarter with debt falling at a 2pct annual rate.

- The European Central Bank left official rates at 1.25pct and Bank of England left rates at 0.5pct.

- European shares rose for the first time in seven days on Thursday with resources stocks in demand. The FTSEurofirst index rose by 0.9pct, the German Dax gained 1.4pct, and the UK FTSE rose by 0.8pct. In London trade, shares in both Rio Tinto and BHP Billiton rose by 1.3pct.

- US sharemarkets rose for the first time in seven days on Thursday but ended trade off their highs. Shares in Exxon Mobil rose 0.5pct after saying that it bought privately held natural gas company Phillips Resources and related company TWP Inc for $1.69 billion last week. The Dow Jones lifted by 75pts or 0.6pct after being up 135pts at one stage. The S&P 500 index was higher by 0.7pct and the Nasdaq gained 9.5pts or 0.4pct.

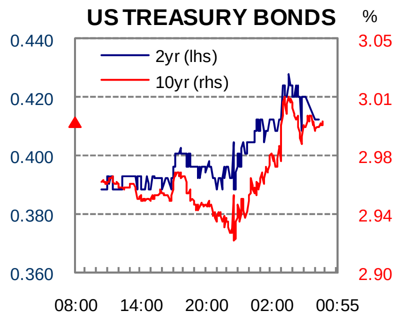
- US treasury prices fell on Thursday (yields higher) as investors switched affections from safe-haven government bonds to equities and commodities. Weak demand for an auction of $13 billion of 30-year bonds put further downward pressure on prices. US 2yr yields rose 3pts to 0.416pct and US 10yr yields rose 5pts to 2.99pct.

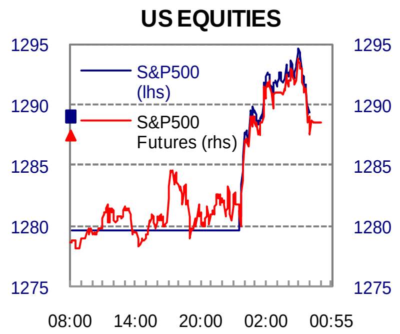
- The US dollar was stronger against the Euro and Japanese yen on Thursday but weaker against commodity currencies as metal and oil prices rose. The Euro fell from highs near US$1.4645 to US$1.4480, before ending US trade near US$1.4510. But the Aussie dollar rose from lows near US105.65c to near US106.50c before ending US trade near US106.25c. And the Japanese yen eased from 79.95 yen per US dollar to JPY80.40, ending US trade near JPY80.30.

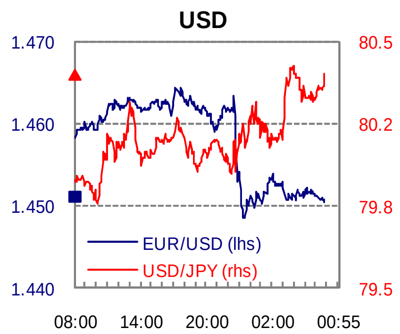
- Crude oil prices rose again on Thursday as investors embraced commodities despite a modestly firmer greenback. The decision on Wednesday by OPEC oil producers to leave output targets unchanged further supported prices. The Nymex crude oil contract rose by US$1.19 or 1.2pct to US$101.93 a barrel. And London Brent crude rose by US$1.72 to a five-week high of US$119.57 a barrel.

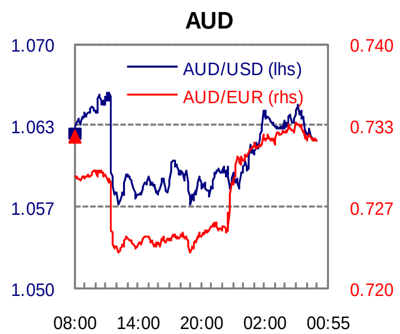
- Base metal prices were again mixed on the London Metal Exchange on Thursday as a firmer greenback balanced the more confident tone of global investors. Nickel rose 2.2pct with lead up 1.2pct but aluminium and zinc lost 0.3pct. And the gold price rose modestly in line with other commodities on Thursday with Comex gold futures up by US$4.00 an ounce to US$1,542.70.

- ***Ahead:*** In Australia, no major economic data is scheduled. In the US, import and export prices are released. In China, trade data is released.









Currencies			10 Yr Bond Yields (%)			Commodities			Equities		
AUD/USD	1.0627	*0.0%*	Australia	5.12	*0.02*	CRB Index	350.84	*0.7%*	Dow	12,124	*0.6%*
NZD/USD	0.8248	*1.2%*	NZ	5.10	*-0.02*	GS Index			S&P 500	1,289	*0.7%*
EUR/USD	1.4510	*-0.5%*	US	3.00	*0.06*	Aluminium $/t	2635	-0.34%	NASDAQ	2,685	*0.4%*
USD/JPY	80.36	*0.6%*	*AU less US*	2.12		Copper $/t	9040	0.28%	FTSE	5,856	*0.8%*
GBP/USD	1.6366	*-0.2%*	*NZ less US*	2.11		Lead $/t	2604	1.16%	Shanghai	2,703	*-1.7%*
USD/CHF	0.8414	*0.6%*	**AUD Swap Rates (%)**			Nickel $/t	23175	2.16%	H.Seng	22,610	*-0.2%*
AUD/NZD	1.2883	*-1.1%*	3mth	5.02	*0.01*	Zinc $/t	2265	-0.28%	Nikkei	9,467	*0.2%*
AUD/JPY	85.40	*0.6%*	3yr	5.16	*-0.03*	Gold $/o	1544.1	*0.4%*	ASX200	4,550	*0.3%*
AUD/EUR	0.7324	*0.5%*	5yr	5.46	*-0.02*	WTI Oil $/b	101.93	*1.2%*	NZSX50	3,489	*-1.0%*

Indicative market rate at 7am Source: Bloomberg

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Economics: Preview

AUSTRALIA & NEW ZEALAND

- No major economic data is released in Australia or New Zealand.

INTERNATIONAL

Friday 10 June

CH Trade Balance, May, USD bn, (11.4 prev)

China's trade balance continued to rebound in April, rising to a surplus of US$11.4bn. In the year to April, China's exports rose 29.9%, while imports increased 21.8% (YoY). The continued rebound in the trade balance further illustrates that the trade deficit seen in February is highly attributable to the Lunar New Year.

Looking ahead, the global economic outlook remains firm. The OECD recently reaffirmed its 4.2% global growth forecast for 2011. Despite this robust level of growth we expect China's trade surpluses to remain small by past standards. As China's economy continues to rebalance and domestic consumption lifts, demand for imports should trend higher.

Friday 10 June

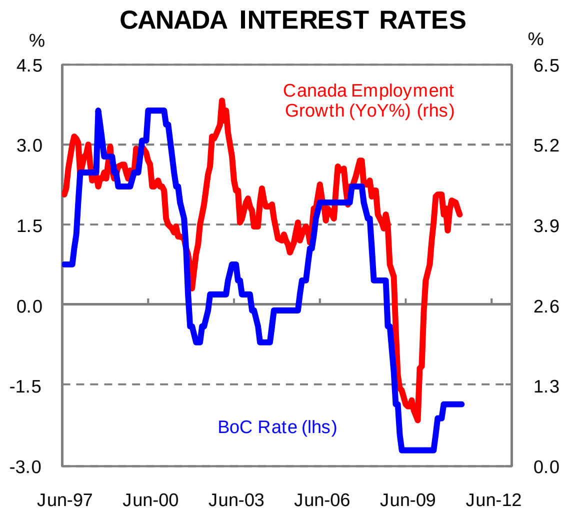
CA Net Change In Employment, May, '000, (58.3prev)

CA Participation Rate, May, %, (67.0 prev)

CA Unemployment Rate, May, %, (7.6 prev)

Employment in Canada rebounded in April, rising by 58,300 in the month, almost three times market expectations. The rise in April was led by part-time employment, which was up 41,100. In total, Canada's labour market has added 182,000 jobs since October 2010.

The Bank of Canada sees business investment increasing in 2011. Business investment is likely to be the main driver of Canada's growth in 2011. As a result the recent improvement in private sector employment looks set to continue over 2011. Consequently, Canada's unemployment rate should move lower from its current 7.6% level in the coming months. At 7.6%, Canada's economy has substantial excess capacity. During the economic expansion of 2006-2008, Canada's unemployment rate averaged 6.2%.

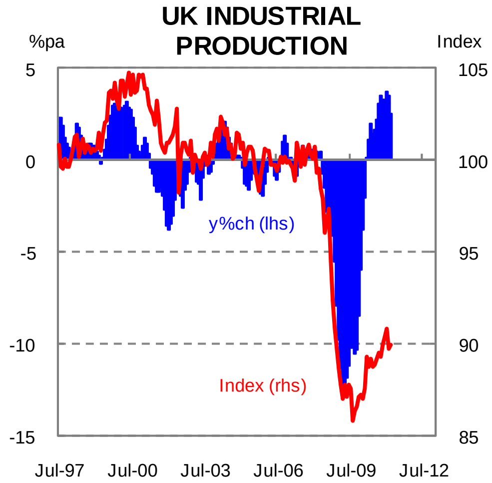


Friday 10 June

UK industrial production, Apr, m/y%ch, (0.2/0.7 prev)

UK industrial production increased by only 0.2% in March, up 0.7% from a year earlier. This was the slowest annual pace of growth since the rebound in production began in March 2010. It appears that UK industrial production is once again moderating. However the recent deceleration is in stark contrast to the period between January 2008 and August 2009, when production declined 14%.

While the UK economic "slowdown" in QIV was thought to have been largely weather affected, the QI GDP data did not show any significant signs of health in UK domestic demand. In addition recent UK manufacturing PMI data has decelerated, signalling additional softness in UK production may eventuate. That being said, the relative GBP weakness and improving trading partner growth bodes well for UK exports and hence export related manufacturing.



Economics: Review

AUSTRALIA & NEW ZEALAND

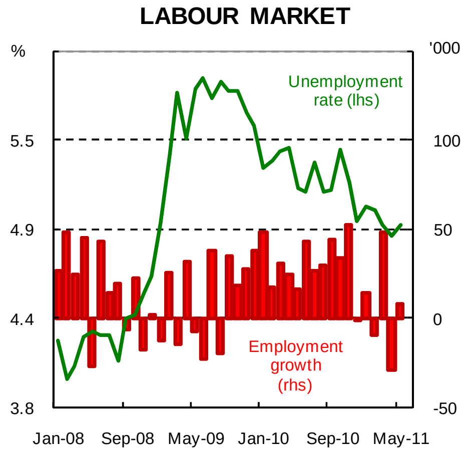
Australia

AU Labour Force, May

- **Employment, '000, 7.8 (-29.4 prev)**
- **Participation rate, %, 65.6 (65.6 prev)**
- **Unemployment rate, %, 4.9 (4.9 prev)**

The ABS estimates that total employment rose by a much weaker than expected 7.8k in May. The composition of the jobs change showed another large fall in full-time jobs (-22.0k) outweighed by a large rise in part-time jobs (+39.8k). Hours worked rose 0.4%.

Jobs growth was strongest in New South Wales (+25.6k) and Victoria (+12.9k). WA's job surge continued, with a 6.6k lift in May. Queensland's robust post-flood momentum suffered a hit in May, with 4.8k jobs lost.



The unemployment rate was unchanged at 4.9% (slight increase from 4.859% to 4.927%). The participation rate remained at 65.6%. The underlying population dynamics in the labour market remain unchanged, and are a continuing source of concern. The supply of workers into the labour force means that the hurdle rate to put downward pressure on the unemployment rate remains low at 12k. Jobs growth over the past 6 months has averaged 5.0k, well down from the 38k monthly average in the prior 6 months. But the unemployment rate has remained stable, for now, courtesy of a 0.4%pt fall in the participation rate over that period. The employment to population ratio has fallen slightly, but remains at near its early-2008 record high. It is still in the zone that previously saw a strong lift in underlying inflation.

The second consecutive "weak" jobs outcome makes it harder to dismiss recent labour market movements as statistical noise. Jobs growth has slowed. It needed to. With a rapid fall in the supply of workers, a moderation in demand was necessary to prevent a wage breakout and a major risk to inflation. Labour supply has been further weakened by a slip in the participation rate.

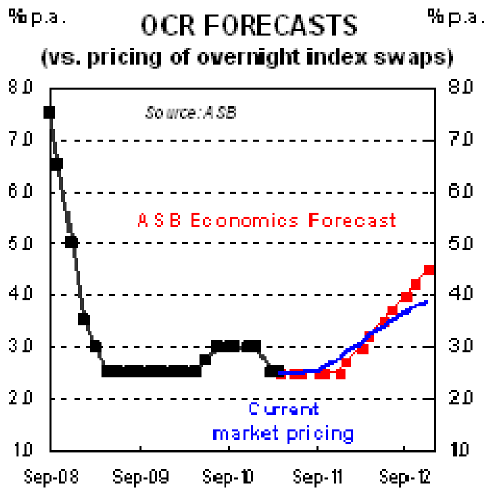
But how long will weakness in labour demand persist? Post-disaster construction activity and the impacts of "Mining Boom Mark II" are yet to make their full weight felt on the economy. The withdrawal of post-GFC fiscal stimulus is weighing on activity at present, particularly in the non-residential construction sector. The demand outlook for the economy, and the labour market, remains very strong. But concerns about labour supply remain.

The labour market is already at near full-employment levels. Labour supply concerns are localised to specific industries at present. But the weak growth in working age population could pose a challenge to the anticipated upswing. The employment to population ratio is already near levels which resulted in a significant upswing in underlying inflation. Migration flows are the swing variable affecting working age population growth. A meaningful increase in working age population will be needed to reduce the likelihood of inflationary surge in wage growth as the labour market tightens further.

New Zealand

NZ RBNZ OCR, %, June, 2.5 (2.5 prev)

The OCR remained on hold at 2.5%, as widely expected. But the RBNZ's perceived risks to its previous outlook have shifted. The RBNZ has become more comfortable that the wider economy is starting to pick up but less comfortable about the inflation outlook. Both of these factors raise the risk of an earlier tightening than we have previously thought. We have shifted our view of the first tightening to January, from March. We still view December through March as the more likely window.



The RBNZ's outlook for the economy has improved since the March Monetary Policy Statement, noting that the "*negative confidence effect of the earthquake on economic activity throughout the rest of the country has been limited.*" The RBNZ notes firms expect to increase hiring and capital investment. The RBNZ expect that the caution shown by households will continue, and household expenditure is only forecast to grow modestly. High household debt is expected to continue to constrain retail spending. These expectations are similar to our own forecasts.

The RBNZ forecasts reconstruction in Canterbury to "*add about 2 percentage points to GDP growth over 2012, and boost the level of activity for several years thereafter*". The pick up in construction activity forecast by the RBNZ is stronger than our own. Nonetheless, we think the inflationary impact of our more conservative (but still high) level of construction over the coming years will be greater than the RBNZ's forecasts suggest.

While the RBNZ acknowledges the recent jump in medium-term inflation expectations, it continues to expect annual CPI inflation will track around the midpoint of the target band of 2% "*over the latter part of the projection*". This expectation is based on the optimistic assumption that medium-term inflation expectations will start to trend down from current high levels of 3% over the coming year. Nonetheless, recent strong inflation indicators are starting to cause the RBNZ some discomfort. In a box highlighting the effects of *reconstruction in the Canterbury region, the RBNZ notes its expectation "generalised* pressure on prices will persist for several years". In particular, construction costs, rents and insurance premiums are highlighted as areas the RBNZ expects to see this upward pressure come through. We see upside risk to the RBNZ's inflation forecast given the extent of rebuilding required, with construction cost inflation expected to receive a strong boost later in 2012 as a result.

RBA view

The RBA has raised its inflation and growth outlook despite downward pressure from the high $A. Further rate rises are likely. We expect rates to reach 5.25% by QIV 2011.

RBNZ view

In response to domestic economic weakness and the Christchurch earthquake, the RBNZ delivered a 50bpt rate cut at the 10 March policy meeting. We expect the RBNZ's tightening cycle to resume in QI 2012.

US & CANADA

United States

- Initial jobless claims increased by 1,000 to 427,000 in the week ending 4 June. The previous week's numbers were also revised higher (426,000 vs prev 422,000). Initial jobless claims have now remained above 400,000 for nine consecutive weeks.
- Somewhat unexpectedly the US trade deficit narrowed in April. The trade deficit declined by 6.7% in April to US$43.7bn, its lowest level since December. Exports were 1.3% higher in the month, while imports fell 0.4%. Imports from Japan declined by a substantial US$3bn in April, largely as a result of the recent Japanese natural disasters. Wider US export growth continues to be supported by the relative weakness of the USD. Total exports have risen by 16% since June 2010.
- Wholesale inventories rose 0.8% in April, slightly below market expectations for a 1% rise. The March result was also revised higher to now show a 1.3% increase (prev 1.1%). Sales lifted by 0.3% in April, after rising by a rather robust 3% in March. The April inventory to sales ratio was 1.14 months, slightly above the record low 1.13 months reached

in March. The relative slowdown in demand may see US wholesalers maintain a tight rein on inventories and avoid an unwanted build-up.

- Philadelphia Federal Reserve President Charles Plosser stated that if the US economy "*continues to show weakness*", the timing of the exit from the current emergency stimulus by the Fed may be pushed back. Plosser also indicated that he sees "*inflation risks in the US as being clearly to the upside*", particularly if economic momentum picks up in the coming quarters. Hence according to Plosser, policy makers "*need to do all we can to ensure that the public's expectations of inflation remain stable*".

Canada

- Canada recorded a moderate trade deficit in April, market expectations had been for a C$600mn surplus. Canada's trade gap was C$924mn in April, its widest level in six months. The April trade deficit was a function of a 1.9% drop in exports, while imports dipped by only 0.6% in the month. The drop-off in exports was led by a fall in sales of transport equipment such as aircraft. Furthermore, both Canada's March and February trade balance figures were revised lower. The respective March and February trade surpluses were revised to show deficits. The strong CAD appears to be impacting on Canada's export growth.

Fed view

A debate about ending the QE program is underway. We expect the QE program will end in June and the first Fed Funds hike in QIV 2011.

Bank of Canada view

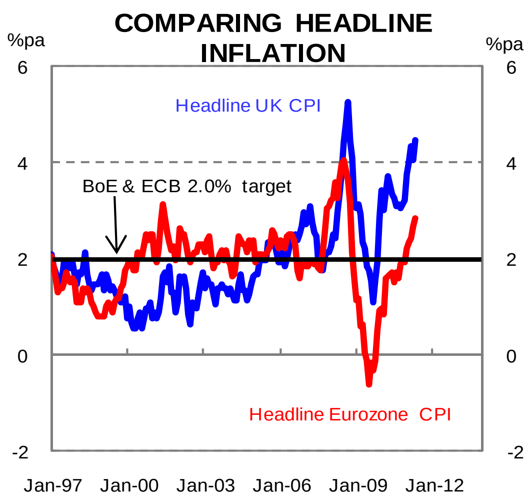
The Canadian economy is recovering, and the BoC has begun to remove stimulus. We expect a slow and steady removal of policy accommodation to ensue.

EUROZONE & UK

Eurozone

EZ ECB Announces Rates, June, %, 1.25 (1.25 prev)

As expected the ECB kept its main refinancing rate at 1.25%. However this pause is unlikely to be maintained for an extended period. ECB President Trichet appeared to signal a July rate hike was a strong possibility. Trichet indicated that the recent data confirmed "*continued upside pressure on inflation*" and as a result "*strong vigilance is warranted*". These views were reinforced by additional Trichet comments stating that "*we are in a mode where there might be in the next meeting an increase of rates, but we are never pre-committed*".



Despite the prospect of a near-term rate hike, longer-term rate rise expectations appear to have been dampened. While the ECB raised its 2011 inflation forecasts to 2.6% (prev 2.3%), it maintained its 2012 forecast (1.7%). With inflation forecast to come back below the ECB's 2% target next year, coupled with the continued uncertainty surrounding the long-term outlook for Eurozone peripheral sovereign debt, market participants appear wary of forecasting a series of ECB rate hikes.

The ECB also increased its 2011 growth forecast to 1.9% (prev 1.7%), but cut back its 2012 growth forecast from 1.8% to 1.7%.

- Reports suggest that the EU and IMF will be required to lend as much as €45bn of additional aid to Greece. According to the reports Greece's 2012-14 financing gap is as wide as €170bn. The reports suggest that this gap will be filled by loans, €57bn of unspent aid from the first bailout package, €30bn in asset sales and approximately €30bn in creditor rollovers.

- French Finance Minister Christine Lagarde stated that the resolution to the Greek deficit issue can not lead to a "credit event". Hence, according to Lagarde, any steps must avoid an involuntary resolution. This is in line with the ECB's view, but in contrast to comments made by German Finance Minister Wolfgang Schaeuable earlier this week. Schaeuable indicated that private bondholders must contribute substantially to the next Greece aid package.

UK

- The UK trade balance narrowed in April. The goods trade gap declined to £7.4bn, 4.1% lower than March. Exports were relatively flat in April, while imports declined by 0.9% (MoM). The fall in imports in April was the third monthly decline in the past four months. The April decline in imports was led by a decline in car and consumer good imports.
- As expected the Bank of England left rates unchanged at 0.5%. Minutes of the meeting, which will be released 22 June, should provide market participants with an insight into the thoughts of the Monetary Policy Committee regarding the outlook for UK monetary policy.

ECB view

Elevated inflation in the Eurozone has led to the ECB commencing tightening in an effort to pre-empt the onset of second round inflation effects. We expect the ECB to raise rates again in QIV 2011.

Bank of England view

While some members of the BoE are concerned about UK inflationary pressures, the majority see downside risks developing in the UK economy. The risk that the BoE remains on hold for an extended period is building.

CHINA & JAPAN

Japan

- The final estimate of QI GDP reaffirmed that Japan has entered into a technical recession. On an annualised basis, the Japanese economy contracted by 3.5% in QI.

China

- No major Chinese economic data was released on Thursday.

Bank of Japan

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.

The Week Ahead

Calendar - Australasia, Japan and China

Date	Time AEST	Econ	Event	Period	Unit	Last	Forecast Market	Forecast CBA
Fri 10 Jun	~	NZ	REINZ housing price index	May	m%ch	1.1	~	~
	08.45	NZ	NZ card spending - total	May	m%ch	1.7	~	~
	09.50	JP	Tertiary industry index	Apr	m%ch	-6.0	~	~
	12.00	CH	Trade balance	May	USD bn	11.4	~	~
	12.00	CH	Exports	May	y%ch	29.9	~	~
	12.00	CH	Imports	May	y%ch	21.8	~	~

Calendar – North America & Europe

Date	Time AEST	Econ	Event	Period	Unit	Last	Forecast Market	Forecast CBA
Fri 10 Jun	~	UK	NIESR GDP estimate	May	%	0.3	~	~
	09.30	UK	Industrial production	Apr	m%ch	0.2	0.0	~
	09.30	UK	Manufacturing production	Apr	m%ch	0.2	0.1	~
	09.30	UK	PPI output nsa	May	m%ch	0.8	0.3	~
	09.30	UK	PPI output core nsa	May	m%ch	0.6	0.4	~
	12.00	CA	Full-time employment change	May	'000	17.2	~	~
	12.00	CA	Net change in employment	May	'000	58.3	25.0	~
	12.00	CA	Part-time employment change	May	'000	41.1	~	~
	12.00	CA	Unemployment rate	May	%	7.6	~	~
	13.30	US	Import price index	May	m%ch	2.2	11.2	~
	19.00	US	Monthly Budget Statement	May	US$bn	~	163.0	~

Unless otherwise noted, all data is sourced from Australian Bureau of Statistics material (www.abs.gov.au).

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