

The Empire manufacturing survey bounced to a 7-month high of 9.53 in December. The Philly Fed survey bounced to an 8-month high of 10.3 in December. Both suggest that the US economy is weathering the ongoing European crisis relatively well.

The US current account deficit narrowed from \$124.7 billion to \$110.3 billion in the September quarter. In terms of investment flows there was a huge swing in foreigners' net transactions in US Treasuries, with a total of \$123.8 billion of inflows as the European debt crisis intensified. Interestingly TIC data also revealed that net foreign purchases of US securities were just \$4.8 billion in October. US jobless claims fell by 19,000 to 366,000 in the last week - 3½ year low.

European shares rose in thin volume on Thursday after a Spanish bond auction produced good demand. Spanish Treasury sold €2.5 billion of 5yr bonds at a yield of 4.02pct compared with 5.28pct on the December 1. The FTSEurofirst index rose 1 while the UK FTSE rose 0.6pct and the German Dax rose 1.0pct.

US shares recorded healthy gains on Thursday following the upbeat US manufacturing and employment data. However a warning from the head of the IMF that the world economic outlook was "quite gloomy" and will require action by all countries to head of a global recession capped gains. With an hour of trade, the Dow Jones was up 59 points or 0.5pct. The S&P 500 rose 0.5pct, and the Nasdaq was higher by 4 points or 0.2pct.

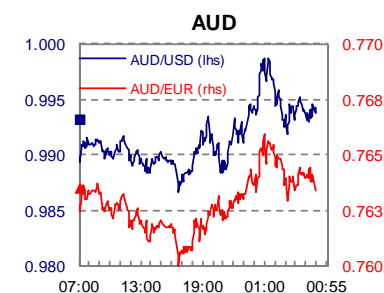
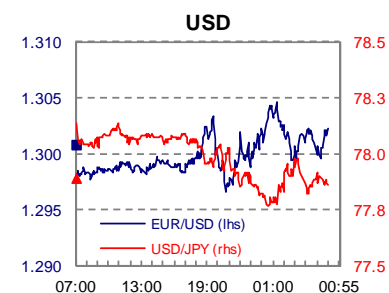
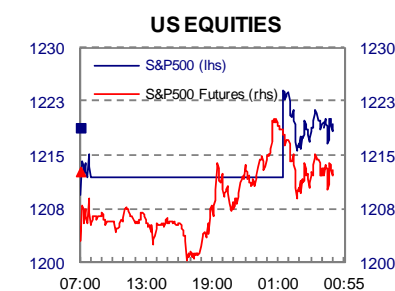
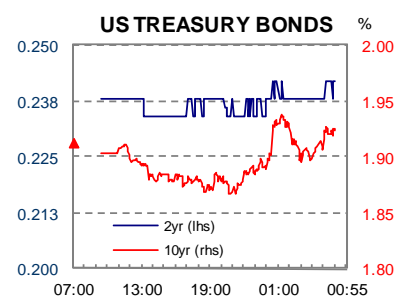
US long-dated treasuries were little changed on Thursday. The employment and manufacturing data suggested that the US economy was gathering momentum however this was offset gains the European debt backdrop. US 2yr yields were flat at 0.24pct and US 10yr yields were flat 1.91pct.

The Euro recorded a modest rebound against the greenback in overnight trade. The Euro rose from lows near US\$1.2965 to around US\$1.3045 and was near US\$1.3015 in late US trade. The Aussie dollar rose from lows around US98.60c to US99.85c, and was near US99.20c in late US trade. And the Japanese yen held between 77.70 yen per US dollar and JPY78.10, and was near JPY77.90 in late US trade.

World crude oil prices continued its recent slide on Thursday in a volatile trading session. As concerns about the slowdown in Europe overshadowed the upbeat US economic data. Nymex crude oil fell by US\$1.08 to US\$93.87 a barrel and London Brent crude rose US17c to US\$105.19 a barrel.

Base metal prices were mostly stronger on the London Metals Exchange on Thursday. Metals rose between 0.1-.2.9pct with the exception of Lead and Zinc. Similarly the gold price fell for a third straight session following the lower oil price. Comex February gold price lost S\$9.70 an ounce or 0.6pct to US\$1,577.20.

Ahead: In Australia, no economic data is release. In the US, consumer price data is released.



Currencies			10 Yr Bond Yields (%)			Commodities			Equities		
AUD/USD	0.9932	0.1%	Australia	3.29	-0.06	CRB Index	294.45	-0.3%	Dow	11,895	0.6%
NZD/USD	0.7543	0.3%	NZ	3.75	-0.13				S&P 500	1,219	0.6%
EUR/USD	1.3008	0.1%	US	1.91	0.01	Aluminium \$/t	1973	0.80%	NASDAQ	2,547	0.3%
USD/JPY	77.89	-0.2%	AU less US	1.38		Copper \$/t	7192	0.08%	FTSE	5,401	0.6%
GBP/USD	1.5494	0.2%	NZ less US	1.84		Lead \$/t	1961	-1.08%	Shanghai	2,181	-2.1%
USD/CHF	0.9411	-1.1%	AUD Swap Rates (%)			Nickel \$/t	17906	2.89%	H.Seng	18,027	-1.8%
AUD/NZD	1.3168	-0.2%	3mth	4.55	0.04	Zinc \$/t	1848	-0.20%	Nikkei	8,377	-1.7%
AUD/JPY	77.36	-0.1%	3yr	3.76	-0.08	Gold \$/o	1571	-1.1%	ASX200	4,140	-1.2%
AUD/EUR	0.7635	0.0%	5yr	4.19	-0.08	WTI Oil \$/b	94.24	-0.7%	NZSX50	3,263	-0.6%

Source: Bloomberg 7.00AEST



Economics: Preview

AUSTRALIA & NEW ZEALAND

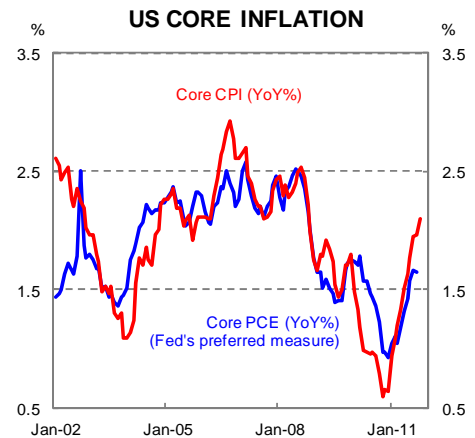
- No major economic data is released in Australia or New Zealand.

INTERNATIONAL

Friday 16 December

US CPI, Nov, m/y%ch, (-0.1/3.5 prev)

Headline CPI inflation has started to ease as retail petrol prices have fallen. We estimate retail petrol prices eased by about 7% in November. Core CPI inflation may also start to ease in coming months. An important foundation of the Fed's policy stance is core inflation will moderate further and remain at or below their 1.7-2.0%pa 'comfort zone'. A vindication of the Fed's inflation forecast will leave the door open to further policy easing if the economic outlook deteriorates significantly further.



SHORT-TERM TECHNICAL CURRENCY MARKET OUTLOOK

The **USD** should continue to experience appreciation over the coming sessions. Expect the currency pairs to move toward: **EUR/USD** 1.2870; **AUD/USD** .9665; **NZD/USD** .7370; **EUR/YEN** 100.75; **AUD/YEN** 76.60; **USD/YEN** 78.00.

Prepared by CBA's FX Sales Desk Strategist



Economics: Review

Australia and New Zealand

- The Business NZ Manufacturing PMI fell to 45.7 over November, and is at the lowest level since June 2009. The manufacturing PMI has fallen sharply over recent months, and points to a sharp contraction in manufacturing production over QIV.

US & CANADA

- Somewhat unexpectedly US industrial production declined in November. The 0.2% monthly dip was the first decline in seven months. Factory production, which accounts for close to 75% of total production also recorded its first falls since April in November. However, much of the decline was in motor vehicles and parts, and likely due to parts shortages as a result of disruption caused by Thailand's floods. Capacity utilisation levels also declined in November, falling to 77.8%. Over the past 20 years the average level of capacity utilisation has been 79.5%.
- The Empire manufacturing survey bounced to a seven-month high of 9.53 in December, while the Philly Fed survey lifted to an eight-month high of 10.3 in December. A lift in the measures of new orders and employment were the general drivers of the improving regional surveys.
- US initial jobless claims dropped to the lowest level since May 2008, which is an encouraging sign the labour market recovery may be continuing to gain traction. Initial jobless claims declined to 366,000 in the week ending 10 December.
- The US current account deficit slipped to US\$110.3bn in QIII, down from US\$124.7bn recorded in QII. The fall was largely the result of a smaller goods and services balance.
- In terms of investment flows there was a huge swing in foreigners' net transactions in US Treasuries. A US\$59.3bn outflow recorded in QII reversed into a US\$123.8bn inflow in Q3. This was largely the result of the recent intensification of the European debt crisis.
- Interestingly TIC data for October revealed that net foreign purchases of US securities declined to just US\$4.8bn in October, as net purchases of Treasury bonds and notes plunged from US\$84.4bn to US\$7.6bn.

FOMC view

Given the loss of momentum in the US economy, we expect the Fed to initiate more policy easing in 2012. Policy easing is first likely to take the form of enhanced guidance.

Bank of Canada view

Softness in the US economy is likely to affect the Canadian economy given the strong trade ties. We expect the BoC to remain on hold until early 2013 before it embarks on a slow and steady removal of policy accommodation

EUROZONE & UK

- Eurozone flash PMIs for December beat expectations. Despite the modest increase, the PMIs remain in contractionary territory. Interestingly service sector PMIs generally outperformed their manufacturing counterparts. In Germany the services PMI lifted to 52.7, but the Eurozone aggregate remains relatively weak at 48.3. The composite aggregate reading for the Eurozone rose modestly, heading up to 47.9, from 47.0. Nonetheless, the aggregate reading is still indicative of a GDP contraction in the coming quarters.
- Eurozone CPI inflation held stable at 3.0% (YoY) in November for the 3rd month running. On a monthly basis headline CPI rose by just 0.1%. The core measure of inflation also remained stable, rising by 1.6% (YoY) in November.
- Spain sold €6.03bn worth of bonds compared with a maximum target of €3.5bn in what could be labelled as a successful auction. The 5-year maturity bonds were sold at a yield of 4.02%, which was down from 5.276% attained only a few weeks' ago. Ten-year bonds were sold at 5.54%, with a bid to cover ratio of 2.16. Overall the Spanish bond market rallied strongly overnight with yields now back under 5% out to 7 years.
- UK retail sales excluding auto fuel fell by 0.7% (MoM) in November, taking the annual rate of growth down to just 0.5%. The decline in November exceeded market expectations and was the largest month fall since May 2011. The falls in retail sales came about even though UK retailers continue to offer large discounts. Concerns about the Eurozone debt crisis, coupled with the fact that UK wages growth is struggling to keep pace with elevated inflation are no doubt



weighing on UK household consumption patterns.

- In December the Confederation of British Industry index of factory orders declined to -23, its lowest level since October 2010. The unfolding crisis in the Eurozone, the UK's largest trading partner, continues to undermine export orders. The measure of export orders fell to -32, its lowest level since January 2010.

SWITZERLAND

- The Swiss National Bank (SNB) left its EUR/CHF 1.2000 floor and other monetary policy measures unchanged at its final quarterly policy meeting of the year. But SNB President Hildebrand made it clear that the SNB stands ready to take further action if needed to stem the threat of deflation. The SNB continues to forecast a drop of 0.3% in consumer prices in 2012. The SNB continues to express its view that the CHF should continue to weaken over time. The SNB reiterated its stance that the EUR/CHF floor will continue to be defended with "*utmost determination*".

European Markets

- The day started with EUR/CHF under pressure as the SNB left its EUR/CHF 1.20 floor unchanged. A decent set of European economic surveys coupled with another positive Spanish bond auction fuelled a decent day for investors in peripheral European bond markets. Spanish yields declined by another 20-45bps along maturities 2s-10s. These moves were mirrored in the BTP market. The US economic news flow in the afternoon kept up the modestly positive tone, as business surveys touched multi-month peaks. Equities generally had a modestly positive day, in Europe closing roughly 1% higher.

Bank of England view

Ongoing deterioration in the UK economy has resulted in the BoE undertaking another round of asset purchases, lifting it to GBP275bn. With the risks to the UK economy skewed to the downside, we now expect the BoE to raise the asset purchase target up to the £350-400bn area in 2012.

ECB view

The recent deterioration in Eurozone economic indicators has resulted in the ECB continuing to reduce its refi rate. We expect the ECB to cut rates again in early 2012.

CHINA & JAPAN

- The Tankan large manufacturing index declined more than expected to -4 in QIV. The results indicate that Japan's largest manufacturers have become more pessimistic about the economic outlook. The outlook survey for large manufacturers declined to its lowest level since QI 2010. The pessimism in the manufacturing sector has been driven by the uncertainty and developing financial stresses in the Eurozone. Interestingly the index for non-manufacturing exceeded expectations, rising from 1 to 4, its highest level since QII 2008.

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.



Calendar - Australasia, Japan and China

Date	Time		Econ	Event	Period	Unit	Last	Forecast	
	AEST							Market	CBA
Fri 16 Dec	11:30	AU		RBA foreign exchange transaction	Nov	\$mn	401.0	~	~

Calendar – North America & Europe

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

Date	UK		Econ	Event	Period	Unit	Last	Forecast	
	Time							Market	CBA
Fri 16 Dec	08:00	IT		Draghi, King, Bini Smaghi, Visco, Regling at Rome Conference					
	10:00	EC		Euro-Zone labour costs	QIII	y%ch	3.6	~	~
	10:00	EC		Euro-Zone trade balance	Oct	€bn	2.1	~	~
	13:30	CA		International securities transaction	Oct	\$bn	7.4	~	~
	13:30	US		CPI	Nov	m%ch	-0.1	0.1	~
						y%ch	3.5	3.5	~
	17:00	US		Fed's Fisher speaks on economy in Austin, Texas					



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