

## Finance ministers approve €78 billion Portugal bailout.

**Net capital inflow to the US** was US\$116 billion in March, up from US\$95.6 billion in February and US\$38.7 billion in January. Chinese holdings of treasuries eased from \$1.1541 trillion to US\$1.1449 trillion. The National Association of Home Builders index was unchanged at +16 in May. And the Empire State manufacturing index hit a 5-month low of 11.88 in May, down from 21.88 in April.

**Eurozone finance ministers** have approved a 78 billion euro bailout for Portugal. Two-thirds of the funds will come from EU facilities and the remainder from the IMF.

**European shares fell** again on Monday with banks leading the declines on concern about the region's debt crisis. The FTSEurofirst index fell by 0.2pct with the German Dax lower by 0.2pct and the US FTSE was down by 2.2pts or less than 0.1pct.

**US sharemarkets** fell again on Monday as more signs of a faltering economy caused investors to book profits on recent gains. Technology stocks - the best performers over 2011 - were hardest hit by profit-taking. And shares in Lowe's - the second largest home improvement chain - lost 3.6pct after reporting weaker-than-expected earnings. The Dow Jones lost 47pts or 0.4pct with the S&P 500 lower by 0.6pct and the Nasdaq lost 46pts or 1.6pct.

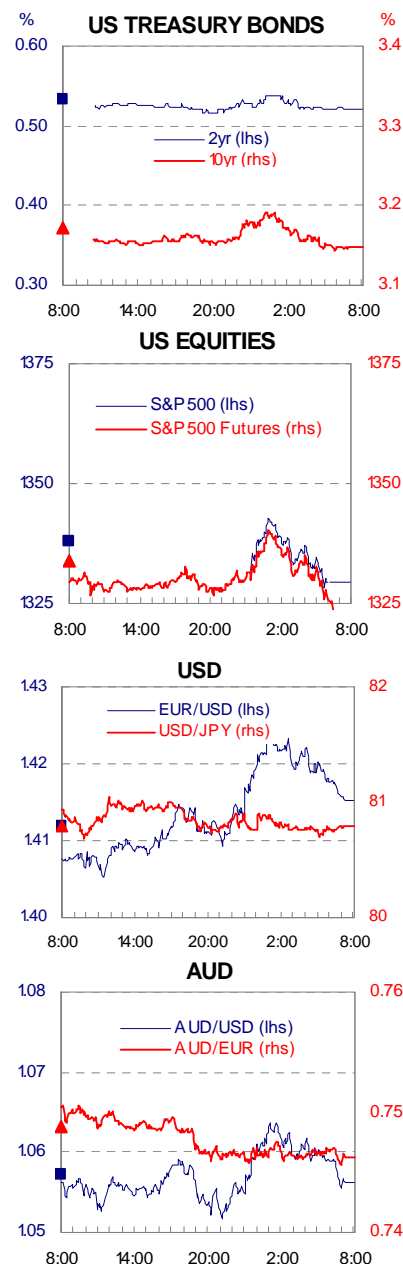
**US treasuries** rose again on Monday (yields lower) as investors shrugged off news that the US Government had hit its debt limit of US\$1.294 trillion. Investors believe that lawmakers will agree to lift the debt limit before a default is triggered in August. A weaker sharemarket also buoyed demand for treasuries on Monday. US 2yr yields fell by 2pts to 0.53pct and US 10yr yields fell by 4pts to 3.15pct.

**The US dollar** gave back some of its recent gains against major currencies in European and US trade on Monday. The Euro rose from lows near US\$1.4090 to US\$1.4240, before ending US trade near US\$1.4170. The Aussie dollar rose from lows near US105.15c to US106.40c before ending US trade near US105.75c. And the Japanese yen lifted from 81.00 yen per US dollar to JPY80.75, ending US trade near its strongest levels.

**US and European crude oil** prices fell on Friday as investors fretted about a slowdown in the US economy. The Nymex crude oil contract fell by US\$2.28 or 2.3pct to US\$97.37 a barrel and London Brent crude fell by US\$1.10 to US\$112.73 a barrel. US gasoline futures also fell by 4.7pct.

**Base metal prices** were again mixed on the London Metal Exchange on Monday. Copper rose 0.5pct and zinc was largely unchanged but other metals fell 0.2-2.1pct with tin faring worst. And the gold price fell again on Monday, with Comex gold futures down by US\$3.00 an ounce to US\$1,490.60.

**Ahead:** In Australia, minutes of the last Reserve Bank Board meeting are released. Lending finance data is released. In the US, data on housing starts and industrial production are released.



Indicative market rate at 7am Source: Bloomberg

| Currencies |              | 10 Yr Bond Yields (%) |            | Commodities    |              |          | Equities      |  |  |
|------------|--------------|-----------------------|------------|----------------|--------------|----------|---------------|--|--|
| AUD/USD    | 1.0563 -0.2% | Australia             | 5.33 -0.02 | CRB Index      | 336.78 -0.5% | Dow      | 12548.4 -0.4% |  |  |
| NZD/USD    | 0.7807 -0.9% | NZ                    | 5.20 -0.03 | S&P GS Index   | 680.32 0.0%  | S&P 500  | 1329.5 -0.6%  |  |  |
| EUR/USD    | 1.4157 0.3%  | US                    | 3.15 -0.02 | Aluminium \$/t | 2560.8 -1.1% | NASDAQ   | 2782.3 -1.6%  |  |  |
| USD/JPY    | 80.78 -0.1%  | AU less US            | 2.19       | Copper \$/t    | 8816 0.5%    | FTSE     | 5923.7 0.0%   |  |  |
| GBP/USD    | 1.6192 0.1%  | NZ less US            | 2.05       | Lead \$/t      | 2284.3 -0.7% | Shanghai | 2849.1 -0.8%  |  |  |
| USD/CHF    | 0.8844 -0.9% | AUD Swap Rates (%)    |            | Nickel \$/t    | 24356 -0.2%  | H.Seng   | 22960.6 -1.4% |  |  |
| AUD/NZD    | 1.3530 0.7%  | 3mth                  | 4.97 -0.09 | Zinc \$/t      | 2135 0.0%    | Nikkei   | 9558.3 -0.9%  |  |  |
| AUD/JPY    | 85.33 -0.3%  | 3yr                   | 5.32 -0.03 | Gold \$/o      | 1490.3 -0.3% | ASX200   | 4650.0 -1.3%  |  |  |
| AUD/EUR    | 0.7462 -0.5% | 5yr                   | 5.62 -0.02 | WTI Oil \$/b   | 97.37 -2.3%  | NZSX50   | 3543.9 0.2%   |  |  |



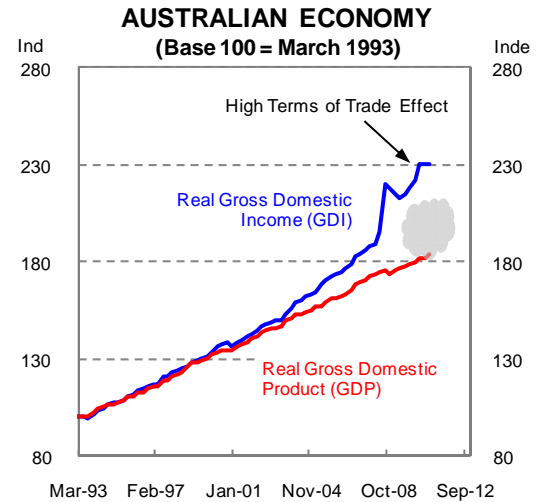
**Economics: Preview**

**AUSTRALIA & NEW ZEALAND**

**Tuesday 17 May**

**AU RBA Board Minutes, May**

As expected the RBA kept the cash rate at 4.75% at its May policy meeting. In the statement accompanying the May meeting the RBA board appeared to be readying market participants for the possibility of a near-term rate hike. Notably the RBA indicated that the terms of trade will reach “higher levels than assumed” recently, the decline in underlying inflation has “run its course”, and headline inflation will now be “close to target”. The RBA Statement on Monetary Policy (SMP), released a few days later, reaffirmed these views. In the SMP the RBA lifted its inflation and terms of trade forecasts. Despite this updated outlook, we are sticking with our August rate hike call, but the risks of an earlier hike are in play. The May RBA meeting minutes are likely to reaffirm the RBA’s tightening bias.

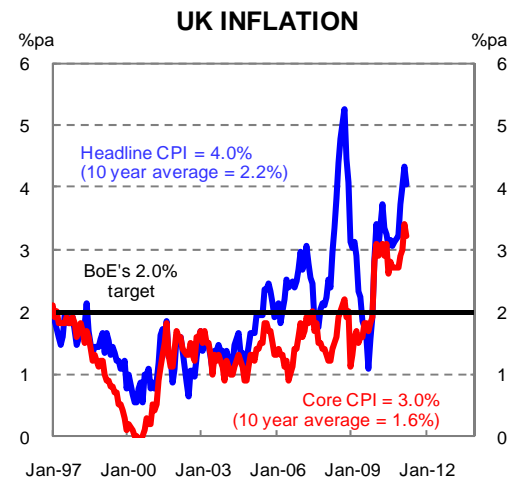


**INTERNATIONAL**

**Tuesday 17 May**

**UK CPI, Apr, m/y%ch, (0.3/4.0 prev)**

UK CPI unexpectedly slowed in March, coming in at 4.0% (YoY). Despite the slowdown, UK CPI is still double the Bank of England’s (BoE) 2% target. The deceleration in March was largely a function of a 1.4% (MoM) fall in the Food and Non Alcohol component. The slowdown in March is unlikely to be the start of a trend. The recent lift in commodity prices, coupled with the higher UK sales tax and relative GBP weakness continues to impact prices in the UK economy.

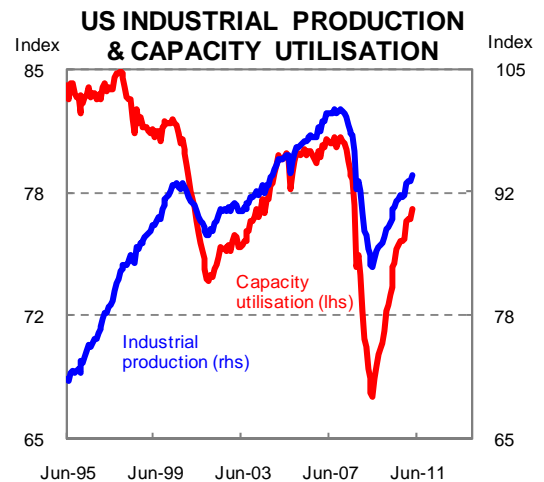


The BoE, in its May *Inflation Report*, indicated that “there is a good chance that inflation will reach 5% later this year”. Significantly, the *Inflation Report* also illustrated that the BoE is now of the opinion that UK inflation may stay above its 2% target until 2013. In an effort to quell the development of second round price effects, we believe the BoE will tighten policy in the coming months, even though recent UK economic data has been soft.

**US Industrial Production, Apr, m%ch, (0.8 prev)**

**US Capacity Utilisation, Apr, %, (77.4 prev)**

US industrial production outperformed expectations in March, rising 0.8% in the month. Manufacturing, which accounts for 75% of production, rose 0.7% in the month. Manufacturing growth looks set to be a driver of the US economic expansion in 2011. Manufacturers continue to benefit from rising business investment, a relatively weak USD and trading partner economic growth.



Capacity utilisation was 77.4% in March, its highest level since August 2008. Capacity utilisation has now increased by 10.1ppts from its June 2009 lows. Further capacity utilisation growth is important. The relative excess capacity in plant usage over recent years has been one of the outlets through which US inflationary pressures have been contained.

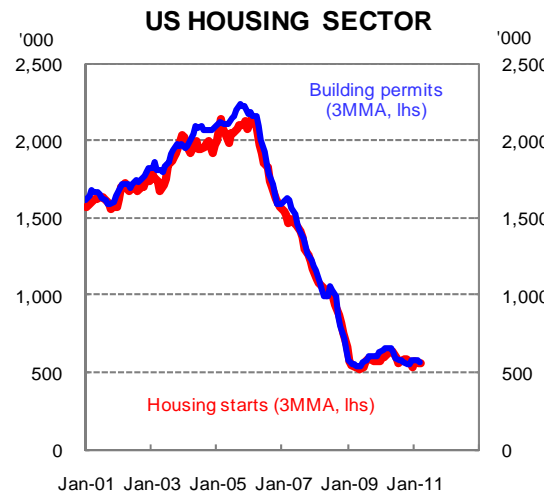


**US Building Permits, Apr, '000, (585 prev)**

**US Housing Starts, Apr, '000, (549 prev)**

In March, US building permits, a sign of future housing starts, surged 11.2%, rising to a 585,000 annual pace. The lift in March was driven by a relatively strong 7.7% rise in single family homes, and a 5.8% increase in multi-family dwellings. Despite the monthly gain, building permits remain well off the average 1.9mn annual pace witness between 2004 and 2007.

Historically building permits have turned into housing starts in the space of a few months. Based on the March rise in building permits, it appears likely that April housing starts may rise from the March 549,000 annual pace. Although housing starts have undergone some recent volatility, they appear to have stabilised, averaging an annual rate of 578,000 since bottoming in April 2009. However given the continuing weakness in US home prices, a substantial lift in construction appears unlikely in the near to medium-term.



**Economics: Review**

**Australia and New Zealand**

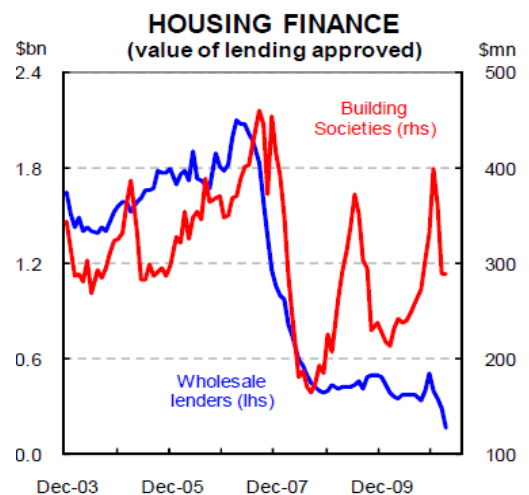
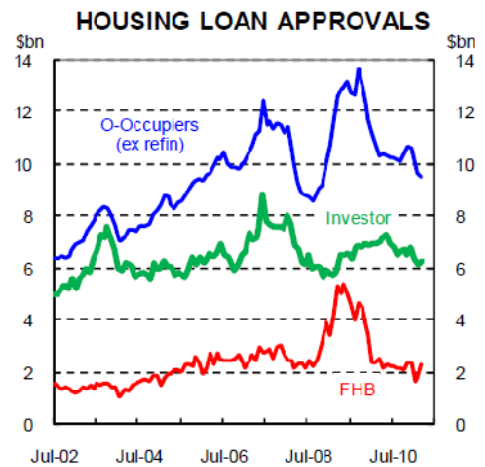
The **Business NZ Performance of Services Index** showed mixed results over April. The overall index improved on a seasonally-adjusted basis, lifting 1.5 points to 52.6. However, most of the improvement appears to have been driven by the service industry recovering in the South Island, following a severe contraction following the February earthquake. Meanwhile, the services outlook in the North Island deteriorated slightly.

**Housing Finance Approvals – March 2011**

- The number of loan approvals to owner occupiers fell by 1.5% in March, to the lowest since February 2001.
- The value of loan approvals to owner occupiers fell 1.1% in March, to the lowest level since November 2008.
- The value of loans to investors rose 2.1% to \$6.28bn, but remains 10.6% lower than a year ago.
- The value of all construction related loans stood out, rising 9.3% in March.
- First Home Buyer numbers look to be stabilising, rising to 8,089 in March, 7.1% lower than a year ago.

The surprise 1.5% fall in the number of owner-occupied loans disappointed market expectations which were centered on a 2.0% rebound (CBA(f) +3.0%). The value of owner-occupier loan approvals fell by slightly less (-1.1%) in March. But a 2.1% increase in investor lending saw the value of total loan approvals fall just 0.1% in March.

The volume of housing transactions slowed over the first few months of 2011. Housing sales transactions have declined, and thus so to have loan approvals. The background conditions suggest that the weakness is unlikely to be a permanent affair. First home buyer activity looks to be stabilising. The labour market has performed strongly (abstracting from monthly volatility) and the business investment surge is expected to intensify in 2011/12 further boosting labour demand. Strong jobs growth is being complimented by a return to strong growth in wages. Household incomes are rising, strongly. At some point the strengthening in household incomes and balance sheets (through higher savings) will see housing activity normalise.



**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 Q1 2012.*

**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.*

**US & CANADA**

**Net capital inflow to the US** was US\$116 billion in March, up from US\$95.6 billion in February and US\$38.7 billion in January. Chinese holdings of treasuries eased from \$1.1541 trillion to US\$1.1449 trillion.

The **National Association of Home Builders index** was unchanged at +16 in May.

The **Empire State manufacturing** index hit a 5-month low of 11.88 in May, down from 21.88 in April.

**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 finance ministers** have approved a 78 billion euro bailout for Portugal. Two-thirds of the funds will come from EU facilities and the remainder from the IMF.

**Eurozone CPI** MoM printed at +0.6% on expectations, following the +1.4% lift in March. EZ Core annual CPI inflation is running at +1.5% (+1.6% expected and 1.3% in the year to March).

**Bank of England view**

*Members of the BoE are becoming more concerned about UK inflationary pressures. But, most members expect significant spare capacity to dull the near-term pressures. We expect the first move in QII 2011.*

**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.*

**CHINA & JAPAN****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       |                         | Econ Event                       | Period          | Unit     | Last   | Forecast |     |
|------------|------------|-------------------------|----------------------------------|-----------------|----------|--------|----------|-----|
|            | AEST       |                         |                                  |                 |          |        | Market   | CBA |
| Tue 17 May | 11.30      | AU                      | Reserve Bank's Board May minutes | May             | ~        | ~      | ~        |     |
| Wed 18 May | 08.45      | NZ                      | Producer prices- inputs          | QI              | q%ch     | 0.9    | ~        | ~   |
|            | 08.45      | NZ                      | Producer prices- outputs         | QI              | q%ch     | 0.2    | ~        | ~   |
|            | 09.50      | JP                      | Tertiary industry index          | Mar             | m%ch     | 0.8    | -5.2     | ~   |
|            | 11.00      | AU                      | Westpac consumer confidence s.a. | May             | index    | 105.3  | ~        | ~   |
|            | 11.00      | AU                      | DEWR skilled vacancies           | May             | m%ch     | 1.7    | ~        | ~   |
|            | 11.30      | AU                      | Wage cost index                  | QI              | q%ch     | 1.0    | 1.1      | 1.1 |
|            |            |                         |                                  |                 | y%ch     | 3.9    | 4.0      | 4.0 |
|            | 14.00      | JP                      | Tokyo condominium sales          | Apr             | y%ch     | 0.0    | ~        | ~   |
| Thu 19 May | ~          | NZ                      | National government budget       |                 |          |        |          |     |
|            | 09.50      | JP                      | Housing loans                    | QI              | y%ch     | 3.2    | ~        | ~   |
|            | 09.50      | JP                      | GDP deflator                     | QI P            | y%ch     | -1.6   | -1.9     | ~   |
|            | 09.50      | JP                      | Nominal GDP                      | QI P            | q%ch     | -0.7   | -0.8     | ~   |
|            | 09.50      | JP                      | GDP annualized                   | QI P            | q%ch ann | -1.3   | -2.0     | ~   |
|            | 09.50      | JP                      | GDP                              | QI P            | q%ch     | -0.3   | -0.5     | ~   |
|            | 11.30      | AU                      | Average weekly wages             | QI              | q%ch     | 1.1    | ~        | 1.1 |
|            |            |                         |                                  |                 | y%ch     | 3.9    | ~        | 3.8 |
|            | 14.30      | JP                      | Capacity utilization             | Mar             | m%ch     | 2.9    | ~        | ~   |
|            | 14.30      | JP                      | Industrial production            | Mar             | m%ch     | -15.3  | ~        | ~   |
|            | 15.30      | JP                      | Nationwide department sales      | Apr             | y%ch     | -14.7  | ~        | ~   |
|            | 15.30      | JP                      | Tokyo department. store sales    | Apr             | y%ch     | -21.5  | ~        | ~   |
|            | Fri 20 May | ~                       | JP                               | BOJ target rate | May      | %      | 0.1      | 0.1 |
| 08.45      |            | NZ                      | Net migration sa                 | Apr             | ~        | -530.0 | ~        | ~   |
| 13.00      |            | NZ                      | Credit card spending sa          | Apr             | m%ch     | -1.6   | ~        | ~   |
|            |            |                         |                                  |                 | y%ch     | 1.5    | ~        | ~   |
| 14.30      |            | JP                      | All industry activity index      | Mar             | m%ch     | 0.7    | -6.0     | ~   |
| 17.00      | JP         | Convenience store sales | Apr                              | y%ch            | 7.7      | ~      | ~        |     |



## Calendar – North America & Europe

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

| Date       | UK    |                      | Event                                 | Period | Unit  | Last  | Forecast |     |
|------------|-------|----------------------|---------------------------------------|--------|-------|-------|----------|-----|
|            | Time  | Econ                 |                                       |        |       |       | Market   | CBA |
| Tue 17 May | 09.30 | UK                   | DCLG UK house prices                  | Mar    | y%ch  | 0.7   | ~        | ~   |
|            | 09.30 | UK                   | CPI                                   | Apr    | m%ch  | 0.3   | ~        | ~   |
|            |       |                      |                                       |        | y%ch  | 4.0   | ~        | ~   |
|            | 09.30 | UK                   | Core CPI                              | Apr    | y%ch  | 3.2   | ~        | ~   |
|            | 09.30 | UK                   | RPI                                   | Apr    | y%ch  | 5.3   | ~        | ~   |
|            | 10.00 | EZ                   | ZEW survey (econ. sentiment)          | May    | Index | 19.7  | ~        | ~   |
|            | 13.30 | US                   | Housing starts                        | Apr    | '000  | 549.0 | 570.0    | ~   |
|            | 13.30 | US                   | Building permits                      | Apr    | m%ch  | 11.2  | 0.9      | ~   |
|            | 14.15 | US                   | Industrial production                 | Apr    | m%ch  | 0.8   | 0.4      | ~   |
| 14.15      | US    | Capacity utilization | Apr                                   | %      | 77.4  | 77.6  | ~        |     |
| Wed 18 May | 09.30 | UK                   | Bank of England minutes               | May    | ~     | ~     | ~        | ~   |
|            | 09.30 | UK                   | Jobless claims change                 | Apr    | '000  | 0.7   | ~        | ~   |
|            | 09.30 | UK                   | ILO unemployment rate (3mths)         | Mar    | %     | 7.8   | ~        | ~   |
|            | 13.30 | CA                   | Leading indicators                    | Apr    | m%ch  | 0.8   | ~        | ~   |
|            | 13.30 | CA                   | Wholesale sales                       | Mar    | m%ch  | -0.6  | ~        | ~   |
|            | 19.00 | US                   | Minutes of FOMC meeting               | Apr    | ~     | ~     | ~        | ~   |
| Thu 19 May | 09.30 | UK                   | Retail sales ex auto fuel             | Apr    | m%ch  | 0.2   | ~        | ~   |
|            | 09.30 | UK                   | Retail sales w/auto fuel              | Apr    | m%ch  | 0.2   | ~        | ~   |
|            | 13.30 | US                   | Initial jobless and continuing claims | May    | ~     | ~     | ~        | ~   |
|            | 15.00 | US                   | Existing home sales                   | Apr    | mn    | 5.1   | 5.2      | ~   |
|            | 15.00 | US                   | Leading indicators                    | Apr    | m%ch  | 0.4   | 0.1      | ~   |
|            | 15.00 | US                   | Philadelphia Fed.                     | May    | Index | 18.5  | 23.0     | ~   |
| Fri 20 May | 09.00 | EZ                   | Current account nsa                   | Mar    | €bn   | -9.5  | ~        | ~   |
|            | 09.00 | EZ                   | ECB EZ current account sa             | Mar    | €bn   | -7.2  | ~        | ~   |
|            | 12.00 | CA                   | Consumer price index                  | Apr    | y%ch  | 3.3   | ~        | ~   |
|            | 12.00 | CA                   | Bank Canada CPI core                  | Apr    | y%ch  | 1.7   | ~        | ~   |
|            | 13.30 | CA                   | Retail sales                          | Mar    | m%ch  | 0.4   | ~        | ~   |
|            | 13.30 | CA                   | Retail sales less autos               | Mar    | m%ch  | 0.7   | ~        | ~   |
|            | 15.00 | EZ                   | Consumer confidence                   | May    | Index | -11.6 | ~        | ~   |



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