

Market carnage. US & EU shares, yields & oil down.

US consumer prices rose by a surprising 0.5pct in July. To be up 3.6%pa largely due to the sharp rebound in gasoline prices. The core CPI rose by a more sedate 0.2pct in July and 1.8% pa. US initial jobless claims nudged higher to 408k last week.

The Philadelphia Fed survey of manufacturing collapsed in August, plunging by 33.9 points to -30.7. The result marked the weakest reading since early 2009. The sub components were all lower. US existing home sales fell by 3.5pct in July.

European shares recorded their biggest daily fall in over 2½ years on Thursday. Doubts about the global recovery and sovereign debt issues continued to dominate price action. Concerns about bank funding also gained traction after an unidentified euro zone bank borrowed \$500 million in one-week dollars from the ECB. The Euro banking sector falling by 6.7pct. The STOXX 600 basic resources index lost 6.9pct. The FTSEurofirst index fell by 4.8pct and the German Dax was down by 5.8pct while the UK FTSE fell by 4.5pct.

US sharemarkets fell sharply on Thursday. Weak economic data added to earlier fears about another recession. A Wall Street Journal report cited that the Federal Reserve was taking a closer look at the US units of Europe's biggest banks, concerned that the European debt crisis could spill into the US banking system. A weaker-than-expected earnings result from Hewlett Packard weighed on technology stocks. The Dow Jones lost 419pts or 3.7pct while the S&P 500 fell 4.5pct and the Nasdaq gave back 131pts or 5.2pct.

US long-term treasuries rose again on Thursday (yields lower) as fears about global growth drove demand for safe-haven treasuries. US 2yr yields were flat at 0.194pct while US 10yr yields fell by 9pts to 2.07pct.

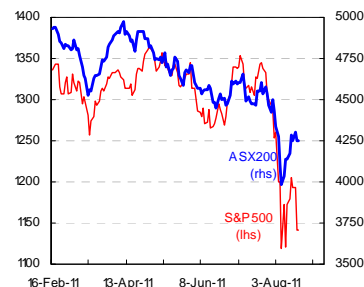
Major currencies fell against the greenback over the European and US sessions. The Euro fell from US\$1.4450 to US\$1.4275, ending the US session at US\$1.4330. The Aussie dollar fell from US105.05c to US103.55c, ending US trade near US104.00c. And the Japanese yen lifted from 76.70 yen per US dollar to JPY76.45, ending US trade near JPY76.55.

Global crude oil prices fell sharply on Thursday. Investors sold off commodities and equities on heightened fears about global economic growth. Nymex crude oil fell by US\$5.20 or 5.9pct to US\$82.38 a barrel and London Brent crude fell by US\$3.61 to US\$106.99 a barrel.

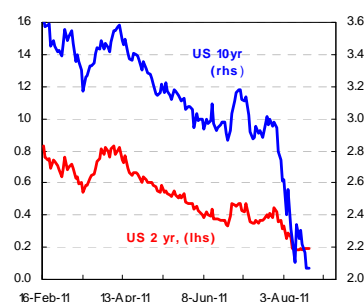
Base metal prices were lower on the London Metal Exchange on Thursday following the slide in the oil price. The stronger US dollar added to the weakness in base metals. And the gold price edged up to fresh record highs with Comex December gold up by US\$28.20 an ounce to a record US\$1,822.

Ahead: In Australia, no economic data is expected. Earnings are expected from QBE, Fortescue metals, Santos and Billabong. In the US, no data is released.

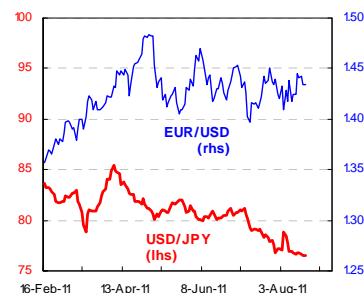
S&P 500 & ASX200



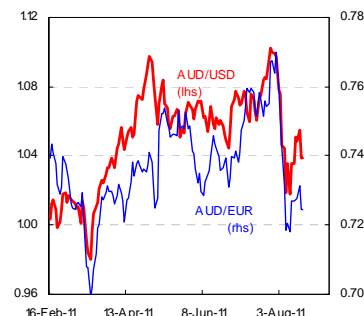
US BOND YIELDS



USD/JPY & EUR/USD



AUD/USD & AUD/EUR



Currencies			10 Yr Bond Yields (%)			Commodities			Equities		
AUD/USD	1.0390	-1.5%	Australia	3.88	-0.18	CRB Index	326.42	-2.3%	Dow	10,991	-3.7%
NZD/USD	0.8214	-1.9%	NZ	4.48	0.00	GS Index	#N/A	N/A	S&P 500	1,141	-4.5%
EUR/USD	1.4338	-0.6%	US	2.06	-0.10	Aluminium \$/t	2303	-2.37%	NASDAQ	2,380	-5.2%
USD/JPY	76.54	-0.1%	AU less US	1.82		Copper \$/t	8751	-2.16%	FTSE	5,092	-4.5%
GBP/USD	1.6521	-0.1%	NZ less US	2.42		Lead \$/t	2308	-2.67%	Shanghai	2,559	-1.6%
USD/CHF	0.7938	0.5%	AUD Swap Rates (%)			Nickel \$/t	21260	-2.96%	H.Seng	20,016	-1.3%
AUD/NZD	1.2647	0.4%	3mth	4.82	-0.06	Zinc \$/t	2152	-1.66%	Nikkei	8,944	-1.3%
AUD/JPY	79.53	-1.6%	3yr	4.13	-0.16	Gold \$/o	1824.7	1.9%	ASX200	4,251	-1.2%
AUD/EUR	0.7246	-0.9%	5yr	4.57	-0.14	WTI Oil \$/b	82.38	-5.9%	NZSX50	3,286	-0.1%

Source: Bloomberg 7.00AEST

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Economics: Preview

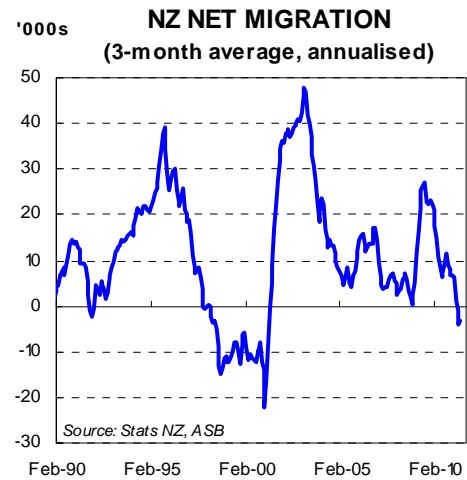
AUSTRALIA & NEW ZEALAND

Friday 19 August

NZ International Travel and Migration - July

Net Migration (prev: -340), Visitor Arrivals (prev: -5.1% mom)

The permanent outflow of New Zealanders following the February quake continued in June, with migration data recording a net departure of 340 people. This follows net outflows recorded in March, April and May as well. The number of New Zealanders leaving permanently (particularly to Australia) had been high prior to the February earthquake, reflecting the challenging NZ economic environment and the attraction of the strong Australian labour market. The earthquakes have added further momentum to this trend. We expect that net outflows may continue over the coming months, particularly following the large aftershocks in June, which is likely to add to the frustrations of many residents. Visitor arrivals dropped sharply in June, largely due to disruption caused by the volcanic ash cloud. In particular, tourists from Australia declined by 11% from May, as the grounding of flights meant that many trips were cancelled. We expect a recovery in overall short-term visitor arrivals over the coming months.

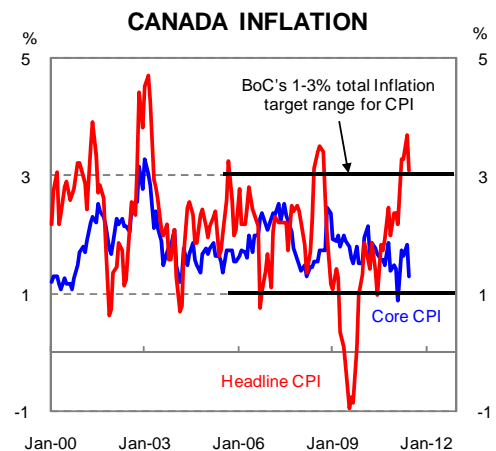


INTERNATIONAL

Friday 19 August

CA CPI, July, m/y%ch, (-0.7/3.1 prev)

Canadian consumer prices fell 0.7% in June, bringing annual inflation down to 3.1% from 3.7% in May. On an annual basis, Canadian CPI was at its highest level in May since September 2008. High headline CPI has been driven by higher energy and food prices. Falling fuel costs helped lower the CPI in June: gasoline prices fell 3.7% in the month. In addition, a 3.1% drop in passenger vehicle prices, due to discounts from some manufacturers made a significant contribution to June's drop. The Bank of Canada (BoC) has expected headline inflation to exceed the top of its inflation target band, but expects the breach to be transitory. In addition to higher food and fuel prices, provisional sales tax increases have also boosted Canadian inflation. The BoC expects these factors to ease in the second half of 2011. Core inflation remains relatively benign. Core CPI, which excludes eight volatile items moderated in June, falling 0.6% in the month. As a result, annual core inflation fell from 1.8% in May to 1.3% in June. The strength of the CAD and the spare capacity in the domestic economy continues to anchor underlying inflation





Economics: Review

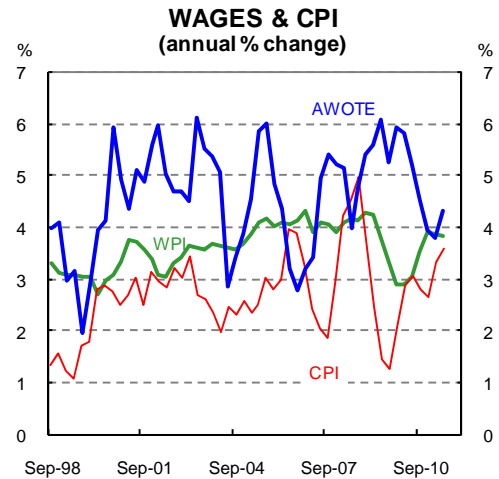
Australia and New Zealand

Yesterday in Australia the AWE data showed a rise of 1.2% to be 4.4% higher over the year. AWE was \$1305.6 per week in May or \$67,891 annually. In comparison, Wednesday's Wages Price Index (WPI) rose by 0.9% in QII to be 3.8% higher than a year ago.

The WPI is the preferred measure of wages trends because it has a much wider coverage and is less volatile. The AWE has some advantages – it gives \$ per week amounts, so it shows absolutes and relativities.

We consider national wages growth to be running at just under 4%pa. Adding jobs growth of 2% pa means that total household income growth is around 6%pa.

The AWE result shows a clear discrepancy between private and public sector wages outcomes in that series. Private sector wages growth was 4.4%pa, while public sector growth was 4.8%pa.



Some of the issues raised in the QII WPI are worth repeating. **Annual wages growth is 3.8% for the WPI and 4.4% for AWE.** But both measures have annual wages growth rising recently. Wages growth, at least for the private sector was considerably weaker following the GFC-induced slowdown in jobs growth and wages demands. While the QII 2011 WPI outcome is below the perceived “threshold” of 4.5%pa which was seen as likely to boost underlying inflation, the AWE result of 4.4% is on the border.

The interesting point is that the 4.5%pa wages “threshold” was against a background of assumed productivity growth of between 1.5% and 2.0%pa. The usual rough figuring has wages less productivity growth giving a good guide to underlying inflation trends. The issue now is that productivity growth is around zero in annual terms. So measures to lift productivity growth, and reduce wages pressures, are required to ensure stable inflation outcomes over the next few years.

In the recent times, the RBA has mentioned that productivity growth has weakened sharply over the past few years compared to earlier periods. And private sector wages and total wages growth have been running in a 3.8%-4% corridor over the past three quarters. With GDP growth expected to rebound to around 4%pa in 2011/12, labour market conditions are likely to tighten further, propelling broad based wages higher.

In our view, this likely scenario will make it very difficult for the RBA to contemplate the rate cut profile the markets are currently anticipating over 2011/12. And it makes us comfortable with our policy call that the next RBA policy move will be to lift rates - unless a profound global meltdown swamps local considerations.

Growth in the WPI has picked up to pre-GFC levels. Given the weak productivity outcomes, solid wage inflation poses a significant risk to the inflation outlook. Unit labour costs rose at an 8.0%pa pace in the QI GDP figures, though some of this deterioration reflected reduced output due to natural disasters. We expect continued strong wages growth in the year ahead as the jobs market tightens further, to levels the RBA would not be comfortable with in terms of the inflation outlook given negligible productivity growth. Growth in average weekly incomes is likely to remain solid as well, supporting household income growth. We see wages and average earnings growth continuing to exceed inflation, resulting in rising real household incomes.

RBNZ view

The RBNZ suggests that current interest rate levels would not be needed much longer. We expect the RBNZ to remove its “insurance cut” in QIV 2011.

RBA view

The QII CPI confirmed the inflation trend has turned up. Rate rises are likely. We expect a rate rise in November. The cash rate is expected to reach 5.75% by 2013.



US & CANADA

United States

- **US core CPI inflation was 1.8% y/y in July** following a 0.2% m/m increase in the index over the month. This was a touch over the consensus expectation. The headline measure surprised positively re-accelerating to 3.6% largely due to the impact of energy prices.
- **The Philadelphia Fed survey of manufacturing collapsed** in August plunging by a whopping 33.9 points to -30.7. While there were clearly downside risks to the August print, the magnitude of the collapse was a shock. The headline index is at its lowest level since Q1 2009 and not far from the post-Lehman's low of -41.2. Unsurprisingly, pretty much all sub-components were weak.
- **US initial jobless claims nudged higher to 408k** in the week to August 13, with the previous week's reading revised up slightly to 399k. The underlying trend remains lower, the 4-week moving average is currently 402,5k, its lowest level since mid-April.
- **US existing home sales dipped to 4.67m** in July and confirm that the US housing market remains in the doldrums.

FOMC view

Given the loss of momentum in the US economy, particularly in the labour market, the first Fed funds hike is not expected until mid 2013 at the earliest.

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

United Kingdom

- **UK retail sales grew by 0.2%** in July, a little below the 0.4% expected. The year on year rate of growth of sales on the High Street dipped back into negative territory, to -0.2% y/y. Clearly there is little to cheer about in these numbers, with the deterioration in the regular run of monthly indicators making the possibility of UK QE2 more likely.

Eurozone

- **Consumer confidence in the Netherlands** plunged unexpectedly in August dropping far more than expected from -12 to -21. (Consensus expectation had been for a fall to -15). The sharp fall does not augur well for consumer confidence readings in other parts of the Eurozone in August. The Netherlands is part of the "healthy" north.

European Markets

- **It was a day of carnage across European equity markets** as bad news continues to come thick and fast. Economic data on the day was abysmal, while reports overnight of disagreement on the FOMC did not help confidence. Reports that Finland had agreed a deal to get collateral in exchange for loans to Greece, is now prompting others including Austria, the Netherlands and Slovakia to follow suit. Fears may also therefore be surfacing that finalisation of the bail-out deal could be delayed. Most European equity indices fell by 5% +, sovereign CDS widened out again and EUR/USD dipped back under 1.43 intraday.

Bank of England view

The MPC continues to stress that the high UK inflation is transitory. Hence, given the subdued outlook for the UK economy, we expect the BoE to remain on hold until QII 2012.

ECB view

Elevated inflation in the Eurozone has led to the ECB re-commencing tightening in an effort to pre-empt the onset of second round inflation effects. With the ECB forecasting 2011 inflation at 2.6%, we expect a further rate hike in QIV.

CHINA & JAPAN



China

- **The People's Bank of China (PBoC) set the USD/CNY midpoint at 6.3942 or 54 points lower, against a mostly flat EUR/USD close overnight.** Also, in the recent trading sessions, the PBoC adopted a strengthening bias with guiding the USD/CNY spot consistently down on an intraday basis. Nevertheless, worsening volatility in the financial markets and tighter USD liquidity lifted offshore forward curves markedly. With risk broadly off, Asian bourses retreated and equity outflow re accelerated to around USD 1bn today. Shanghai composite index ended the session down by 1.61%.
- **China will continue to develop Hong Kong's offshore CNY centre,** said the PBoC Governor Zhou. More specifically, the PBoC will (1) allow both financial and non financial firms to issue CNY denominated debt in Hong Kong with a quota of CNY 50bn in 2011; (2) expand the CNY trade settlement regime to 31 provinces and cities from 20 previously; (3) allow offshore CNY to be invested in domestic stock markets under the existing QFII scheme with an initial quota of CNY 20bn; (4) prioritise Hong Kong in investing in the domestic interbank bond market; and (5) increase the central government's bond issuances to CNY 20bn in 2011. These measures are essentially relaxation of the existing capital account control measures between Hong Kong and the Mainland. As such, the offshore deliverable CNY market is likely to be more closely integrated with its Mainland counterpart and the onshore CNY curve should continue to lead the CNH curve.

Rest of Asia

- **Japan export growth** was weaker than expected in July, down 3.3% on year-ago levels compared to market expectations of a 2.6% decline. Seasonally adjusted, exports lifted 0.8% suggesting the recovery in exports has been sluggish following disruptions caused by the earthquake and nuclear crisis in March. The weaker data also adds to concerns around the export outlook for Japan, given the high level of the yen...

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		Event	Period	Unit	Last	Forecast	
	AEST	Econ					Market	CBA
Mon 15 Aug	08.30	NZ	Performance services index	Jul	Index	54.7	~	~
	09.50	JP	GDP deflator	QII	y%ch	-1.9	-1.7	~
	09.50	JP	Nominal GDP	QII	q%ch	-1.3	-1.4	~
	09.50	JP	GDP annualized	QII	%	-3.5	-2.5	~
	09.50	JP	GDP	QII	q%ch	-0.9	-0.6	~
	11.30	AU	New motor vehicle sales	Jul	m%ch y%ch	1.3 11.0	~ ~	~ ~
Tue 16 Aug	11.00	AU	Reserve Bank's Board August minutes					
	12.00	CH	Conference Board China June Leading Economic Index					
Wed 17 Aug	08.45	NZ	Producer prices- inputs	QII	q%ch	2.2	~	~
	08.45	NZ	Producer prices- outputs	QII	q%ch	1.7	~	~
	10.30	AU	Westpac leading index	Jun	m%ch	-0.1	~	~
	11.00	AU	DEWR internet skilled vacancies	Jul	m%ch	0.0	~	~
	11.30	AU	Wage cost index	Jun	q%ch y%ch	0.8 3.8	~ ~	1.0 4.0
Thu 18 Aug	09.50	JP	Merchandise trade balance total	Jul	¥bn	68.6	~	~
	09.50	JP	Adjusted merchandise trade balance	Jul	¥bn	191.2	~	~
	09.50	JP	Merchandise trade exports	Jul	y%ch	-1.6	~	~
	11.30	AU	Average weekly earnings	May	q%ch y%ch	1.0 3.8	~ ~	0.9 3.9
	15.00	JP	Coincident index CI	Jun	Index	108.6	~	~
	15.00	JP	Leading index CI	Jun	Index	103.2	~	~
Fri 19 Aug	08.45	NZ	Net migration SA	Jul	~	-340.0	~	~
	08.45	NZ	Visitor arrivals	Jul	%	-5.1	~	~
	11.35	CH	MNI August flash business sentiment survey					
	13.00	NZ	Credit card spending	Jul	m%ch y%ch	0.4 4.5	~ ~	~ ~
	14.30	JP	All industry activity index	Jun	m%ch	2.0	~	~



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
Mon 15 Aug	13.30	US	Empire manufacturing	Aug	~	-3.8	~	~
	14.00	US	Total net TIC flows	Jun	\$bn	-67.5	~	~
	15.00	US	NAHB housing market index	Aug	Index	15.0	15.0	~
Tue 16 Aug	07.00	GE	GDP	QII	q%ch	1.5	~	~
	09.30	UK	CPI	Jul	q%ch	-0.1	~	~
					y%ch	4.2	~	~
	09.30	UK	CPI core	Jul	y%ch	2.8	~	~
	10.00	EZ	GDP	QII	q%ch	0.8	~	~
					y%ch	2.5	~	~
	10.00	EZ	Trade balance	Jun	€bn	-0.6	~	~
	13.30	US	Housing starts	Jul	'000	629.0	610	~
	13.30	US	Building permits	Jul	'000	617.0	605.0	~
	14.15	US	Industrial production	Jul	m%ch	0.2	0.5	~
14.15	US	Capacity utilization	Jul	%	76.7	76.9	~	
Wed 17 Aug	09.00	EZ	ECB Euro-Zone current account	Jun	€bn	-5.2	~	~
	09.30	UK	Bank of England minutes	~	~	~	~	~
	09.30	UK	Average weekly earnings	Jun	3m y%ch	2.1	~	~
	10.00	EZ	CPI - core	Jul	y%ch	1.6	~	~
	13.30	US	Producer price index	Jul	m%ch	-0.4	0.1	~
y%ch					7.0	7.0	~	
Thu 18 Aug	09.30	UK	Retail sales w/auto fuel	Jul	m%ch	0.7	~	~
					y%ch	0.4	~	~
	10.00	EZ	Construction output	Jun	m%ch	-1.1	~	~
					y%ch	-1.9	~	~
	13.30	CA	Leading indicators	Jul	m%ch	0.2	~	~
	13.30	CA	Wholesale sales	Jul	m%ch	1.9	~	~
	13.30	US	Consumer price index	Jul	m%ch	-0.2	0.2	~
					y%ch	3.6	3.3	~
	13.30	US	CPI ex food & energy	Jul	y%ch	1.6	1.6	~
	15.00	US	Leading indicators	Jul	m%ch	0.3	0.2	~
15.00	US	Existing home sales	Jul	mn	4.8	5.0	~	
				m%ch	-0.8	3.8	~	
Fri 19 Aug	07.00	GE	Producer prices	Jul	m%ch	0.1	~	~
	12.00	CA	CPI	Jul	m%ch	-0.7	~	~
					y%ch	3.1	~	~
12.00	CA	Bank Canada CPI Core	Jul	y%ch	1.3	~	~	



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