

Weekly Market & Economic Update – week ending 13 August 2010



by Dr Shane Oliver, Head of Investment Strategy & Chief Economist

Data/Event	Units*	Movement		Trend
		LATEST	PREVIOUS	
US – Retail sales, July	mom	0.4%	-0.5%	↔
Australia – Westpac/Melbourne Institute consumer sentiment survey	-	+5.4%	+11.1%	↑
China – Consumer price index (CPI or inflation), July	yoy	+3.3%	+2.9%	↔
Australia – Unemployment rate, July	mom	5.3%	5.1%	↓
US - Consumer price index, July	mom	0.3%	-0.1%	↔

Financial markets

Indicator	Friday, 13 August 2010	Friday, 6 August 2010	Weekly change	13 August 2009	12-month change
S&P/ASX 200 Index	4,460	4,566	-2.3%	4,436	+0.5%
S&P/ASX 200 Property Trusts	859	870	-1.3%	820	+4.8%
US S&P 500	1,079	1,122	-3.8%	1,013	+6.6%
Dow Jones Eurostoxx	258	265	-2.7%	250	+3.0%
UK FTSE 100	5,275	5,332	-1.1%	4,756	+10.9%
Japan TOPIX	831	861	-3.5%	968	-14.2%
CITIC/S&P 300 China A	2,414	2,449	-1.4%	2,848	-15.2%
MSCI (ex-Aust/in LC)	795	820	-3.0%	760	+4.7%
Aust 90-day bank bill yield	4.75%	4.75%	0 bps	3.28%	+147 bps
Aust 10-year bond yield	4.99%	5.09%	-10 bps	5.64%	-65 bps
US 10-year bond yield	2.67%	2.82%	-15 bps	3.60%	-93 bps
Oil – West Texas Crude	US\$75.39	US\$80.70	-6.6%	US\$70.52	+6.9%
A\$ in US cents	US\$0.8934	US\$0.9187	-2.8%	US\$0.8419	+6.1%
TWI	69.8	70.4	-0.9%	66.4	+5.1%

Major upcoming global economic releases and events

Date	Data/Event	Units*	Previous	Market Forecast
15 August	Japan – Gross domestic product, June	qoq	-5.0%	-2.3%
17 August	US – Producer price index, July	mom	-0.5%	+0.2%
17 August	China – Conference Board leading index, June	index	145.8	n/a
17 August	US – Housing starts, July	mom	-5.0%	n/a
19 August	Australia – Average weekly wages, May	mom	+1.1%	+1.2%

*Month-on-month (mom); quarter-on-quarter (qoq); year-on-year (yoy); seasonally adjusted annual rate (saar)

Headline developments of the past week

- The past week has been tough for shares, commodities and the Australian dollar (A\$) as investors succumbed to a new bout of worries about a double dip back into global recession in response to weak economic data and disappointment that the US Federal Reserve downgraded its assessment of the US economic outlook but didn't embark on a new round of quantitative monetary easing.

Major global economic releases and implications

- US economic data was generally poor with a blowout in the trade deficit in June and weak data for construction and inventories pointing to a downwards revision to June quarter GDP growth from 2.4% annualised to just 1.25%. Small business confidence also fell, retail sales were weaker than expected and unemployment claims rose. On a positive note, mortgage applications rose for the fourth week in a row and consumer sentiment rose slightly. Core inflation remained benign in July at 0.9% year on year leaving plenty of scope for further easing.
- The eurozone economy rose strongly in the June quarter, with Germany being the main driver, on the back of a surge in global demand over the last year. However, fiscal tightening and slower global growth will likely lead to a slowdown in growth in the year ahead.
- The Bank of Japan left interest rates on hold, but with no measures to stop the rise in the yen. Economic data was soft with falls in bank lending and consumer confidence and soft machinery orders.
- July economic data confirmed that China's economy is slowing, but there is no sign of the hard landing feared by many but nor is there any sign of policy easing. So far the Chinese slowdown is gradual and consistent with a soft landing in the economy, i.e. growth settling down to around 9% per annum. We remain of the view that Chinese tightening measures will start to be eased in the next few months. However, with no sign of any easing as yet, investors are understandably nervous.

Australian economic releases and implications

- Australian economic data was mixed. While data for housing finance, business conditions and business confidence all weakened, consumer confidence rose solidly and job ads rose again in July. Labour market data also presented a mixed picture in July with a decline in full-time jobs and a rise in unemployment but the overall picture is still one of labour market strength as total employment rose solidly and unemployment only rose because of rising labour force participation.
- While it's very early days in the June reporting season, so far the results have been lacklustre. Although there were some good results from companies such as Coca-Cola and Qantas in the last week, the proportion of companies surprising on the upside so far is 37%, which is down from 49% in the February reporting season, and there has been a preponderance of negative or cautious outlook statements consistent with increased uncertainty regarding the economic outlook.

Major market moves

- Despite a solid start to the week, shares ended down sharply on the back of renewed worries about a double dip in the US and a hard landing in China, and the US Federal Reserve's less than inspiring move towards more quantitative easing.
- The return of investor risk aversion saw commodity prices, except gold, and the Australian dollar fall but government bonds benefited from the flight to safety and fears about the economic outlook.

What to watch in the week ahead?

- In the US, producer price inflation in July is likely to remain benign and housing data will be watched closely for signs of stabilisation after the slump following the ending of the first time home buyer tax credit in April.
- In Australia, the minutes from the Reserve Bank of Australia's (RBA) last meeting and a speech by Governor Stevens are likely to confirm that while the RBA still retains a bias to raise interest rates further it doesn't feel compelled to act on it now.
- The Australian June half-year profit reporting season will speed up with 50 major companies due to report. Investors are likely to focus on company outlook statements as they have been relatively downbeat so far, feeding into downwards revisions to earnings growth expectations for 2010-11. It is looking increasingly likely that we have seen the peak in positive earnings revisions.

Outlook for markets

- With the good news from the US profit reporting season behind us, worries about a double dip back into global recession now escalating again and policy makers in the US and China unlikely to respond immediately, shares are now at a high risk of having another leg down, particularly as we head into the normally weak months of September and October. However, beyond the likelihood of another round of near-term share market weakness we remain of the view that a global double dip recession will be avoided and with shares very good value, monetary conditions set to remain favourable and China likely to start relaxing its tightening measures sometime in the next few months, shares are likely to stage a decent rally in the December quarter and then through 2011.
- The A\$ is likely to remain volatile in the short term, particularly with double dip fears persisting and the next interest rate hike in Australia being pushed out, but should rise on a six to 12 month horizon as it becomes clear that the global recovery is continuing (albeit very gradually in developed countries), commodity prices are remaining strong and Australian interest rates are remaining well above global rates.
- Double dip and deflation worries will keep bond yields low in the short term, but medium-term returns are likely to be poor, reflecting low yields and excessive public debt levels in many developed countries.

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