

Weekly Market & Economic Update – week ending 19 February 2010



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Data/Event	Units*	Movement		Trend
		LATEST	PREVIOUS	
US – Housing starts, January	-	591,000	575,000 (revised from 557,000)	↔
US – Industrial production, January	mom	+0.9%	+0.7% (revised from +0.6%)	↑
Australia – National Australia Bank (NAB) business confidence, December quarter	index	+18	+16	↔
US – Producer price index (PPI), January	mom	+1.4%	+0.2%	↑

Financial markets

Indicator	Friday, 19 February 2010	Friday, 12 February 2010	Weekly change	19 February 2009	12-month change
S&P/ASX 200 Index	4,827	4,562	+5.8%	3,449	+40.0%
S&P/ASX 200 Property Trusts	881	866	+1.7%	662	+33.1%
US S&P 500	1,117	1,076	+3.8%	779	+43.4%
Dow Jones Eurostoxx	269	252	+6.7%	197	+36.5%
UK FTSE 100	5,335	5,143	+3.7%	4,018	+32.8%
Japan TOPIX	956	892	+7.2%	752	+27.1%
CITIC/S&P 300 China A	2,859	2,728	+4.8%	1,930	+48.1%
MSCI (ex-Aust/in LC)	841	796	+5.7%	600	+40.2%
Aust 90-day bank bill yield	4.19	4.21	-2 bps	3.08	+111 bps
Aust 10-year bond yield	5.53	5.50	+3 bps	4.22	+131 bps
US 10-year bond yield	3.60	3.69	-9 bps	2.84	+76 bps
Oil – West Texas Crude	US\$75.78	US\$74.13	+2.2%	US\$39.48	+91.9%
A\$ in US cents	US\$0.9009	US\$0.8877	+1.5%	US\$0.6433	+40.0%
TWI	70.8	69.3	+2.2%	54.1	+30.9%

Major upcoming global economic releases and events

Date	Data/Event	Units*	Previous	Market Forecast
22 February	Australia – New motor-vehicle sales, January	mom	+3.3%	n/a
24 February	US – Consumer confidence, February	index	55.9	56.0
25 February	US – New home sales, January	-	342,000	350,000
25 February	US – Real capital expenditure, December quarter	qoq	-3.9%	+1.0%
26 February	US – Durable goods orders, January	mom	+0.3%	+1.5%

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

Headline developments of the past week

- The US Federal Reserve (Fed) continued to unwind its liquidity support for financial markets by increasing its discount rate from 0.5% to 0.75%. This move was foreshadowed by the Fed a week ago and does not signal a change in monetary policy. Bank access to emergency Fed loans via the 'discount window' has collapsed, so the increase in the discount rate will have virtually no impact on bank borrowing costs. Although the Fed's unwinding of liquidity support is consistent with an eventual increase in the Federal Funds rate, this is still likely to be many months away. The Fed has repeatedly implied that economic conditions are likely to justify an exceptionally low Federal Funds rate for an extended period. Finally, it should be noted that although we are moving into a rising interest rate environment, this is generally a good thing because it is a sign economic conditions are improving. In contrast, the falling interest rate environment in the US from August 2007 was in reaction to terrible economic and financial news and was not a good time for shares.
- There was an avalanche of commentary from the Reserve Bank of Australia (RBA) over the week, with the minutes from the last board meeting and speeches from RBA officials Debelle and Lowe and Governor Stevens. The overriding message is that further interest rate rises are likely, but given lingering uncertainties, including sovereign debt levels and credit conditions, the process will be gradual.

Major global economic releases and implications

- US data releases were mostly encouraging. Recent surveys of manufacturing conditions in the New York and Philadelphia regions rose strongly. Industrial production also rose, as did housing starts and home builders conditions. The US leading index pushed higher in January and mortgage delinquencies edged down in the December quarter 2009. However, bad weather pushed down new mortgage applications and weekly retail sales data, and pushed up jobless claims. Snowstorms are likely to depress many economic releases for February, ahead of a rebound in March. In addition, inflation remains benign, suggesting monetary tightening in the US is still likely to be a long time away.
- Japanese economic data was surprisingly upbeat with a stronger-than-expected 1.1% rise in December quarter 2009 gross domestic product (GDP).

Australian economic releases and implications

- Australian economic data was mixed. The NAB business survey conditions slowed in January, but confidence rose, consistent with continued economic recovery. Skilled vacancies rose solidly in February,

reversing a fall in January and suggesting that the improvement in the labour market is continuing.

- We are now just over 50% of the way through the December half 2009 profit reporting season in Australia. Despite a few disappointments, the general impression remains strong. Of the major companies to have reported so far, 56% have seen their results beat expectations, compared to a long-term norm of 47%. Also, dividends have been increasing again and 60% of companies have seen their earnings rise over the year to the December half 2009. Outlook statements have generally been positive, consistent with a continuing recovery. Overall, the results so far provide confidence that profits will grow 20% or so over the year ahead.

Major market moves

- Global share markets rose on supportive economic data and profit results, and as sovereign debt fears abated somewhat. Australian shares were pushed higher over the week by the global rebound, higher commodity prices and good earnings results.
- Along with shares, higher commodity prices also helped the Australian dollar (A\$) and reinforced expectations for more interest rate hikes in Australia.

What to watch in the week ahead?

- In the US, data for house prices, home sales, consumer confidence and durable goods orders will be the focus.
- In Australia, business investment and construction activity data will be studied closely, given this feeds into the December quarter 2009 GDP result. Wages growth, car sales and private credit data will also be released.

Outlook for markets

- This year will remain a bumpy one for shares, with some countries starting to unwind their stimulus measures, increased interest rates and worries about high sovereign debt likely to be a recurring theme. However, the trend is likely to remain up, underpinned by improving profits, solid growth in emerging countries (including China) and the likelihood that interest rates will remain at relatively low levels.
- Monetary tightening will also ensure a bumpy ride for commodity prices and the A\$. However, further gains in the A\$ are still likely this year because global economic growth should remain commodity intensive. The spread between Australian and US interest rates is more likely to widen than narrow over the next six months.
- Government bond yields are likely to push higher over the year ahead once monetary tightening starts to be factored in, the supply of government bonds increases and private sector credit demand picks up. Corporate debt is far more attractive with yields of 7.5% or more.

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