Investment Strategy & Economics

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Weekly Market & Economic Update – week ending 12 March 2010

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Data/Event	Units*	Movement		Trend
		LATEST	PREVIOUS	
Australia – Consumer sentiment, March	yoy	+37.1%	+36.4%	⇑
Australia – Unemployment rate, February	-	5.3%	5.3%	⇓
US – Trade balance, January	US$ billion	-37.3	-40.2	⇔
US – Retail sales, February	mom	+0.3%	+0.5%	⇑
US – Business inventories, January	mom	flat	-0.2%	⇑

Financial markets

Indicator	Friday, 12 March 2010	Friday, 5 March 2010	Weekly change	12 March 2009	12-month change
S&P/ASX 200 Index	4,818	4,767	+1.1	3,236	+48.9
S&P/ASX 200 Property Trusts	867	887	-2.3	611	+41.9
US S&P 500	1,150	1,139	+1.0	751	+53.1
Dow Jones Eurostoxx	273	271	+0.7	182	+50.0
UK FTSE 100	5,626	5,600	+0.5	3,712	+51.6
Japan TOPIX	936	911	+2.7	701	+33.5
CITIC/S&P 300 China A	2,713	2,736	-0.8	1,858	+46.0
MSCI (ex-Aust/in LC)	851	842	+1.1	555	+53.3
Aust 90-day bank bill yield	4.47	4.21	+26 bps	3.11	+136 bps
Aust 10-year bond yield	5.64	5.47	+17 bps	4.26	+138 bps
US 10-year bond yield	3.70	3.68	+2 bps	2.85	+85 bps
Oil – West Texas Crude	US$81.24	US$81.50	-0.3	US$47.03	+72.7
A$ in US cents	US$0.9180	US$0.9076	+1.1	US$0.6561	+39.9
TWI	71.3	70.2	+1.6	54.9	+29.9

Major upcoming global economic releases and events

Date	Data/Event	Units*	Previous	Market Forecast
15 March	US – Industrial production, February	mom	+1.0%	-0.1%
17 March	Australia – Dwelling starts, December quarter	qoq	+8.9%	n/a
17 March	Australia – Westpac leading index, January	mom	+0.5%	n/a
18 March	US – Consumer price index (CPI), February	mom	+0.2%	+0.1%
18 March	US – Leading indicators, February	mom	+0.3%	+0.2%

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

Headline developments of the past week

- Chinese economic data for February remained robust pointing to more tightening measures in China in the months ahead. However, it would be wrong to get too concerned about Chinese tightening. First, it is worth stressing that much of the rise in Chinese inflation is being driven by higher food prices. Also, momentum in industrial production and fixed asset investment is likely to cool a bit going forward anyway as the easy gains following the recovery of the last year are behind us. Further, despite foreign skepticism, China has proven to be quite adept at successfully managing its economy in recent years. Finally, by starting the tightening process preemptively, i.e. before inflation has gotten out of hand, China has likely headed off the need for aggressive tightening down the track. We remain of the view that Chinese tightening won't become overly aggressive and that gross domestic product growth (GDP) growth will settle down around 10% per annum rather than collapse as some seem to fear.

Major global economic releases and implications

- US economic data was mixed. Positively, retail sales rose more than expected in February, weekly mortgage applications rose strongly, wholesale inventories fell as sales continued to exceed production, and the trade deficit was narrower than expected in January. However, small business optimism fell, and an early reading of March consumer sentiment dropped. Weekly unemployment claims fell but by less than expected.
- European industrial production surged in January by much more than expected.
- Japanese economic data again showed that the recovery is slowly taking a firmer hold. Machine tool orders rose strongly in February, machine orders appear to be bottoming, a business survey rose in February, and a leading indicator rose. Meanwhile, Taiwanese export data and Malaysian and Indian industrial production data are continuing to point to a strong economic recovery in Asia.

Australian economic releases and implications

- Australian economic data remained robust and consistent with a continuation of the economic recovery. Business conditions and confidence both rose in February according to the National Australia Bank's business survey and consumer sentiment remained high in March despite the latest interest rate hike. While employment was essentially flat in February this masked more gains in full time employment and a strong rise in hours worked, and a sharp increase in job ads points to solid employment growth ahead. The only fly in the ointment was housing finance which fell for the fourth month in a row on the back of interest rate hikes and the ending of the first home owners boost.

Major market moves

- Share markets rose as the focus on Greece's sovereign debt problems receded and confidence in the global economic recovery continued to improve. US shares are now challenging their recent recovery highs in January with other share markets, including Australia's, following along behind. From their lows in February, Australian shares are up 7%, Asian ex Japan shares are up 8%, and US shares are up 9%.
- The improvement in investor confidence has also flowed through to the Australian dollar (A$) which also benefitted from strong local economic data.

What to watch in the week ahead?

- In the US, the Federal Reserve's (Fed) interest rate setting meeting will be watched closely to see whether it softens its assessment that economic conditions will likely justify keeping rates low for an "extended period". The Fed is unlikely to make a change this time around, but a change in the wording to give it more flexibility is expected once employment starts to grow again.
- In Australia, interest rates will remain a focus with a speech by the Reserve Bank of Australia's (RBA) Malcolm Edey and the release of the minutes from the last rate setting meeting.

Outlook for markets

- From a six to 12 month perspective, we expect the rising trend in shares to remain in place. While worries about monetary tightening and sovereign debt will cause occasional bouts of volatility, further gains in shares are likely to be underpinned by the continuing recovery in corporate profits, still low global interest rates, strong growth in the emerging world and the fact that there is still a lot of cash sitting on the sidelines. Our year-end target for the Australian All Ords and ASX 200 indices remains 5600.
- The ride for commodity prices and the A$ will likely remain bumpy, but further gains are still expected this year as global economic growth will remain commodity intensive. With commodity prices likely to remain strong and the spread between Australian and US interest rates likely to widen further, it is only a matter of time before the A$ breaches parity against the US dollar.
- Government bond yields are likely to be pushed higher over the year ahead as monetary tightening starts to be factored in, the supply of government bonds increases, and private sector credit demand picks up. Bond risk premiums are also likely to rise on the back of very high public debt levels in the US, Europe and Japan.

Further information
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