

Weekly Market & Economic Update – week ending 12 June 2009



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Economic data and events

Data/Event	Units*	Movement		Trend
		LATEST	PREVIOUS	
Australia – National Australia Bank (NAB) business confidence, May	-	-2	-14	↑
Australia – Investor housing finance, April	mom	+0.9%	+4.7%	↑
Australia – Unemployment rate, May	-	5.7%	5.5% (revised from 5.4%)	↑
US – Trade balance, April	US\$ billion	-29.2	-28.5 (revised from -28.7)	↔
US – Retail sales, May	mom	+0.5%	-0.2% (revised from -0.4%)	↑

Financial markets

Indicator	Friday, 12 June 2009	Friday, 5 June 2009	Weekly change	12 June 2008	12-month change
S&P/ASX 200 Accumulation Index	27,728	26,852	+3.3%	34,521	-19.7%
S&P/ASX 200 Property Trusts	777	756	+2.8%	1,529	-49.2%
US S&P 500	946	939	+0.7%	1,340	-29.4%
Dow Jones Eurostoxx	233	229	+1.7%	342	-31.9%
UK FTSE 100	4,442	4,405	+0.8%	5,791	-23.3%
Japan TOPIX	951	927	+2.6%	1,363	-30.2%
CITIC/S&P 300 China A	2,421	2453	-1.3%	2,539	-4.6%
MSCI (ex-Aust/in LC)	721	714	+1.0%	1,018	-29.2%
Aust 90-day bank bill yield	3.32	3.24	+8 bps	7.88	-456 bps
Aust 10-year bond yield	5.55	5.62	-7 bps	6.73	-118 bps
US 10-year bond yield	3.79	3.87	-8 bps	4.21	-42 bps
Oil – West Texas Crude	US\$72.04	US\$68.09	+5.8%	US\$136.74	-47.3%
A\$ in US cents	US\$0.8079	US\$0.7891	+2.4%	US\$0.9371	-13.8%
TWI	65.1	64.1	+1.6%	72.0	-9.6%

Major upcoming global economic releases and events

Date	Data/Event	Units*	Previous	Market Forecast
16 June	US – Producer price index (PPI), May	mom	+0.3%	+0.6%
16 June	US – Housing starts, May	mom	flat	480,000
17 June	Australia – Dwelling commencements, March quarter	qoq	-9.9%	-3.0%
18 June	Australia – Customs imports, May	mom	-2.0%	na
19 June	US – Leading index, May	mom	+1.0%	+0.9%

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

Headline developments of the past week

- The backup in bond yields globally, and worries this may derail the economic recovery is a growing concern. This is understandable given the global recovery is still very fragile and is yet to commence. The US and Australian fixed rate mortgage rates have already been pushed higher as a result and one major Australian bank has raised its variable mortgage rate, albeit marginally. The more likely scenario is that falling inflation and the realisation that monetary policy is not about to be tightened will likely see bond yields settle down again over the next few months.
- The World Health Organisation declared swine flu to be a pandemic as a result of its global spread. It is important to note that though there are now over 28,000 cases world wide and over 1300 in Australia, the death rate has remained low outside of Mexico (with just 36 deaths out of 22,533 cases outside of Mexico so far, or around 0.16%), which is more akin to regular flu.

Major global economic releases and implications

- While economic data from the US was mixed, there were more positives than negatives. On the negative side, mortgage refinancing applications fell reflecting the back up in mortgage rates. May retail sales data was mixed, showing only a modest improvement in underlying terms but being revised up for April. Against this, the Federal Reserve's Beige Book of anecdotal evidence noted that the downtrend in economic activity was beginning to moderate in several districts. A survey of small businesses reported a further rise in confidence. Consumer confidence rose further and initial unemployment claims fell further.
- In Japan the fall in machinery orders was disappointing however, the improvement in business and consumer confidence as well as signs of improvement in exports were encouraging. Bankruptcies fell during the month.
- Chinese economic data for May continued to paint a clear picture of a strong domestically driven recovery. Exports remained weak, but appear to be stabilising. Industrial production came in stronger than expected and both retail sales and fixed asset investment were robust. Loan growth also remained strong.

Australian economic releases and implications

- More 'green shoots' appeared across the Australian economic landscape over the last week. Business confidence rose and consumer confidence had its strongest gain in 22 years. Housing finance for owner occupiers rose for the seventh month in a row which is pointing to a housing recovery from later this year. Labour markets were better than expected in May. Unemployment rose back to 5.7% and only 1,700 jobs were lost in May. Business conditions slipped according to the National Australia Bank's survey and the ANZ job ads survey had its smallest fall in 13 months.
- The improvement now becoming evident in indicators such as housing finance, building approvals, business and consumer confidence suggest that the unemployment rate may peak earlier and below the

Government's forecast of an 8.5% rate in June 2011. Further interest rate cuts are likely as unemployment rises, inflation falls and possibly as the Reserve Bank of Australia (RBA) seeks to stop other banks from raising their mortgage rates. The proliferation of better than expected economic data suggests that the risk that we have seen the low point for interest rates has increased.

Major market moves

- Share markets outside Europe pushed higher over the last week on continuing signs of economic recovery. The Australian share market broke decisively through the 4000 level, helped by more indications that the Australian downturn will be mild and that a sustained recovery will commence later this year.
- After rising further earlier on, bond yields settled down later in the week helped by a successful US bond auction
- Most commodity prices (including the oil price) continued to rise with copper breaking out to an 8-month high as Chinese copper imports rose to a record high. The Australian dollar (A\$) rose, helped by rising commodity prices and expectations that Australian interest rates will remain above those in other countries.

What to watch in the week ahead?

- Some business surveys will be released in the US along with a survey of home builders. Data for housing starts, industrial production and inflation will also be released.
- In Australia, the RBA minutes from its last Board meeting are likely to simply reinforce the impression that while interest rates may still fall they are on hold for now given the turn for the better in economic data and the fact that rates have already been eased substantially.

Outlook for markets

- Shares are expected to continue gaining ground, albeit with bumps along the way. Shares are still very attractive compared to low yielding cash and bonds. Most investors are still underweight shares and a further improvement in economic data is likely as we head towards an economic recovery from later this year. Our view remains that shares have embarked on a cyclical recovery that has further to run.
- Bond yields are likely to fall back in the short term as inflation continues to fall and it becomes obvious that central banks are not going to be raising interest rates any time soon. However, the medium-term return potential from bonds is very poor.
- The broad trend in the A\$ is likely to remain up on the back of strengthening commodity prices and a resurgence in carry trades. The A\$ is likely to rise to around US\$0.85 by year-end.
- The broad trend in commodity prices is likely to remain up on the back of a falling US dollar, recovering growth - particularly in China, and constrained supply.

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