

Weekly Market & Economic Update – week ending 18 June 2010



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Data/Event	Units*	Movement		Trend
		LATEST	PREVIOUS	
Australia – Westpac leading index, April	index	flat	+0.9%	↑
US – Housing starts, May	-	593,000	672,000	↔
US – Producer price index (PPI), May	mom	-0.3%	-0.1%	↔
Japan – Tertiary industry activity index, April	index	+1.4%	+1.2%	↑
US – Consumer price index (CPI), May	mom	-0.2%	-0.1%	↔

Financial markets

Indicator	Friday, 18 June 2010	Friday, 11 June 2010	Weekly change	18 June 2009	12-month change
S&P/ASX 200 Index	4,552	4,506	+1.0%	3,892	+17.0%
S&P/ASX 200 Property Trusts	886	882	+0.5%	742	+19.4%
US S&P 500	1,118	1,092	+2.3%	918	+21.7%
Dow Jones Eurostoxx	262	253	+3.5%	223	+17.7%
UK FTSE 100	5,251	5,164	+1.7%	4,281	+22.7%
Japan TOPIX	885	866	+2.1%	911	-2.9%
CITIC/S&P 300 China A	2,336	2,336	flat	2,540	-8.0%
MSCI (ex-Aust/in LC)	818	800	+2.3%	692	+18.3%
Aust 90-day bank bill yield	4.92	4.95	-3 bps	3.28	+164 bps
Aust 10-year bond yield	5.43	5.40	+3 bps	5.58	-15 bps
US 10-year bond yield	3.22	3.23	-1 bp	3.83	-61 bps
Oil – West Texas Crude	US\$77.18	US\$73.78	+4.6%	US\$71.37	+8.1%
A\$ in US cents	US\$0.8794	US\$0.8503	+3.4%	US\$0.7995	+10.0%
TWI	67.5	67.5	flat	63.5	+6.3%

Major upcoming global economic releases and events

Date	Data/Event	Units*	Previous	Market Forecast
21 June	Australia – New motor vehicle sales, May	mom	+8.4%	n/a
22 June	Hong Kong – Consumer price index (CPI), May	yoy	+2.4%	n/a
22 June	US – Existing home sales, May	millions	5.77	6.20
23 June	US – New home sales, May	-	504,000	470,000
24 June	US – Durable goods orders, May	mom	+2.9%	-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

- China's central bank has announced that that their currency is moving from a US dollar (US\$) currency peg to a more flexible basket currency basis. This decision to allow greater currency flexibility will probably see a gradual and modest appreciation of China's currency. Whilst this may make Chinese industry less competitive, this should be considered a broadly positive move by signalling a commitment to rebalance China's economy to be less reliant on exports, an additional means to help control inflation, and less risk of trade tensions with America or Europe.
- Tensions in the euro-zone sovereign bond market eased somewhat, with Spain successfully selling bonds. The European Union also agreed to release the results of its bank stress tests, which should help improve transparency regarding the risks to the European banking system.
- Both Korea and Indonesia announced measures to reduce the volatility of capital inflows and encourage longer term foreign investment. Such moves obviously reflect concerns about hot money inflows at a time when interest rates in the US and elsewhere are likely to remain very low. They are unlikely to prevent longer term appreciation in Asian currencies though.

Major global economic releases and implications

- US economic data was pretty mixed, consistent with continued growth of around 2.5-3.0%. Housing starts, permits to build new homes and a survey of home builders' conditions all fell in the wake of the expiry of the first home buyer tax credit and weekly unemployment claims rose. Against this, industrial production, surveys of manufacturing conditions in New York and Philadelphia all remained strong, and the Conference Board's leading indicator rose in May. Inflation remained benign, with deflation now becoming more of a risk than inflation. While housing activity clearly appears to have fallen sharply after the ending of the first home buyer tax credit in April, it still seems to be tracing out a broad bottom after the 2006 to 2009 collapse. Nevertheless, the ongoing softness in the housing sector and continuing low inflation suggest that the US Federal Reserve (Fed) will keep interest rates near zero into next year.
- European data provided nothing new. Euro-zone industrial production rose in April but employment was flat in the March quarter. Inflation measures in Europe and the UK were softer than expected, with core inflation in the euro-zone at 0.8% over the year to May.
- Japanese data was positive, with increases in industrial production, Tokyo condominium sales, machine tool orders and a tertiary industry index. The Bank of Japan left interest rates on hold but announced a new loan scheme to commercial banks which may be a response to rising political pressure to toughen up on deflation.

Australian economic releases and implications

- It was a quiet week for Australian economic data. Dwelling starts were up 4.3% in the March quarter and the Westpac leading index for April was unchanged from the previous month, though well up on its long term trend in annualised terms. Meanwhile, the minutes from the RBA's last meeting reinforced the view that interest rates may remain on hold for a while yet due to the renewed uncertainty regarding the global economic outlook on the back of European debt problems. June quarter inflation data will now be the Bank's focus.

Major market moves

- It was a good week for share markets, helped by successful bond auctions in Europe and positive corporate news. Improving investor confidence saw the euro and the A\$ rise, while oil and gold prices were also higher.

What to watch in the week ahead?

- In the US, data for homes sales are likely to show sharp falls, reflecting the ending of the first home buyers tax credit, but durable goods orders for May, which provide a good guide to business investment. are likely to remain strong. The Fed is expected to leave interest rates on hold near zero and, given the sub-par nature of the recovery, continuing softness in the housing sector and uncertainty about the impact of the problems in Europe, is also expected to reiterate that rates will remain low for an extended period. Euro-zone manufacturing conditions indexes, along with the German IFO business conditions index for June, are worth keeping an eye on in terms of gauging the impact of the European debt crisis on business activity.

Outlook for markets

- The recovery in share markets from their April/May correction is likely to continue, as is the global economic recovery. Shares remain very oversold and are still cheap. Investor sentiment toward shares remains negative, which is positive from a contrarian perspective. The recent outbreak of uncertainty will help ensure that global monetary conditions remain easy and Chinese tightening is now on hold, with the prospect of some easing in property tightening measures in the months ahead. As such, our view remains that the cyclical recovery in shares that commenced in March last year is still on track. That said, volatility will remain a key feature going forward.
- The A\$ is likely to regain strength as Australian interest rates remain well above global rates and as commodity prices resume their upswing.
- Low yields are pointing to poor medium term returns from government bonds, particularly as worries about excessive public debt impact and as the latest bout of investor risk aversion abates.

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