Investment Strategy & Economics

Weekly Market & Economic Update – week ending 25 June 2010

by Bob Cunneen, Senior Economist

Data/Event	Units*	Movement		Trend
		LATEST	PREVIOUS	
Australia – New motor vehicle sales, May	mom	-3.2%	+9.0% revised	⇑
Hong Kong – Consumer price index (CPI), May	yoy	+2.5%	+2.4%	⇑
US – Existing home sales, May	millions	5.66	5.77	⇑
US – New home sales, May	-	300,000	504,000	⇓
US – Durable goods orders, May	mom	-1.1%	+3.0% revised	⇑

Financial markets

Indicator	Friday, 25 June 2010	Friday, 18 June 2010	Weekly change	25 June 2009	12-month change
S&P/ASX 200 Index	4,413	4,552	-3.1%	3,856	+14.4%
S&P/ASX 200 Property Trusts	857	886	-3.3%	747.5	+14.6%
US S&P 500	1,077	1,118	-3.6%	920.3	+17.0%
Dow Jones Eurostoxx	252	262	-3.8%	222	+13.5%
UK FTSE 100	5,047	5,251	-3.9%	4,253	+18.7%
Japan TOPIX	867	885	-2.0%	920	-5.8%
CITIC/S&P 300 China A	2,310	2,336	-1.1%	2,586	-10.7%
MSCI (ex-Aust/in LC)	791	818	-3.3%	688	+15.0%
Aust 90-day bank bill yield	4.96	4.92	+4 bps	3.24	+172 bps
Aust 10-year bond yield	5.25	5.43	-18 bps	5.57	-32 bps
US 10-year bond yield	3.11	3.22	-11 bp	3.54	-43 bps
Oil – West Texas Crude	US$78.61	US$77.18	+1.9%	US$69.63	+12.9%
A$ in US cents	US$0.8729	US$0.8794	-0.7%	US$0.8029	+8.7%
TWI	68.5	67.5	+1.5%	64.1	+6.9%

Major upcoming global economic releases and events

Date	Data/Event	Units*	Previous	Market Forecast
29 June	US – Consumer confidence, June	yoy	15.5%	n/a
1 July	China – PMI Manufacturing, June	Index	53.9	53.2
1 July	US – Construction expenditure, May	mom	+2.7%	-0.8%
1 July	Australia – Retail sales, May	mom	+1.8%	n/a
2 July	US – Unemployment rate, June	-	9.7%	9.8%

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

Headline developments of the past week

- Australia has a new Prime Minister in Ms Julia Gillard. While this has no major immediate implications for Australia's economic policy, one key issue where there is likely to be a change is the Resource Super Profits Tax (RSPT). Under the previous Rudd Government, this RSPT involved a proposed 40% tax to be applied to the mining sector's profits from July 2012. Prime Minister Gillard has announced that the government will enter negotiations with the mining sector, which has apposed the tax, over the coming months. This suggests changes will be made to the proposed RSPT.
- The US Federal Reserve (Fed) kept official interest rates on hold at 0% to 0.25% and maintained its pledge to keep rates at a record low for an 'extended period'. The European sovereign debt crisis is perceived as tightening global financial conditions and is less supportive of US economic growth. While the US labour market is gradually improving, the Fed conceded that consumers are constrained by high unemployment and tight credit. As a result, the Fed is likely to keep interest rates on hold for a considerable time, perhaps even into next year given America's subdued economic recovery.
- Britain's new coalition government has announced a significant austerity budget plan to ensure that Britain maintains its AAA credit rating. Essentially, this emergency budget aims to reduce the UK's budget deficit from -11% of UK gross domestic product (GDP) this year to a modest surplus of 0.3% of GDP in 2014-15. This budget balancing act is primarily through spending cuts, namely a two-year wage freeze for public sector workers. There are also some notable tax-raising measures. Britain's consumption tax will rise 2.5% (to 20%) from 2011 onwards and there is also a levy on banks' balance sheets. However, Britain's gross domestic product (GDP) growth forecasts have been revised down by 0.3% for 2011 (to 2.3%) to reflect the negative impact of these austerity measures.

Major global economic releases and implications

- US economic data was generally softer. Existing and new homes sales fell in May, though both were adversely affected by the ending of the first home buyer tax credit. A regional manufacturing survey showed a modest pullback in activity and mortgage applications continued to fall. However, rising durable goods orders in May and lower jobless claims in June, signalled that the US recovery is sustainable.
- Economic data in Europe remains consistent with a subdued recovery. Consumer confidence rose modestly, an index of European manufacturing activity edged lower and Germany's key IFO business conditions index posted its highest reading since May 2008. These are actually positive signs that Europe's sovereign debt crisis is yet to have a material impact on business activity in the region.
- Chinese officials announced that they were removing export tax rebates on some steel and metal products. In Japan, industry activity jumped in April after March's slide and department store sales fell in May.

Australian economic releases and implications

- New motor vehicle sales fell 3.2% in May but this follows a sharp 9% rise in April, and the Australian Bureau of Agricultural and Resource Economics raised the forecast for 2011 export earnings by 8.3% on the back of increased contract prices for iron ore and coking coal. Exports are expected to be worth around A$202.5 billion in the year to June 2011, a significant surge on the expected 2010 result of A$164.1 billion.

Major market moves

- Global shares fell over the week amid softer US economic data, proposed American banking regulation and concerns over Europe's financial stability. While new US banking legislation is yet to be resolved between the alternative US Senate and Representatives' proposals, US bank shares have drifted lower on concerns that tighter proprietary trading restrictions will restrain profits. Australian shares ended the week lower on the back of softer commodity prices and a poor lead from global share markets.
- Commodity prices edged slightly higher and gold prices hit record highs. The Australian dollar (A$) fell against its US counterpart amid speculation that Europe's debt crisis will dampen global economic growth.

What to watch in the week ahead?

- It's a busy calendar in terms of US economic data, with June's labour market data (particularly the monthly payrolls change and unemployment rate), the Institute for Supply Management's manufacturing survey and the Conference Board's latest consumer confidence figures due to be released.
- In Australia, the focus will be on May's retail sales and building approvals data. The market will be looking at just how well the consumer and building construction sectors are doing after the sequence of interest rate rises since October 2009.

Outlook for markets

- Prospects for the global economy are still generally promising. However, the current doubts over America's recovery and bank regulation, European government debt and China's monetary policy intentions have served to constrain global shares. Shares are still cheap and sentiment is negative, suggesting that once these doubts dissipate, global shares should deliver strong positive returns.
- 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.

Further information
If you would like to know more about how AMP Capital can help you, please contact one of the following:
Financial Planners
AMP Capital's Client Service Team on 1300 139 267
Personal Investors
Adviser or Financial Planner
Wholesale Investors
AMP Capital's Client Service Team on 1800 658 404
or visit **www.ampcapital.com.au**