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Investment Strategy & Economics

Weekly Market & Economic Update – week ending 4 June 2010

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Data/Event	Units*	Movement		Trend
		LATEST	PREVIOUS	
Australia – Current account, March quarter	A$ billion	-16.6	-17.5	⇓
Australia – Reserve Bank of Australia (RBA) cash rate decision, June	-	4.50%	4.50%	⇔
US – Institute for Supply Management (ISM) manufacturing index, May	index	59.7	60.4	⇔
China – Manufacturing purchasing managers index (PMI), May	index	53.9	55.7	⇔
US – Non-farm payroll employment, May	-	431,000	290,000	⇑

Financial markets

Indicator	Friday, 4 June 2010	Friday, 28 May 2010	Weekly change	4 June 2009	12-month change
S&P/ASX 200 Index	4,449	4,458	-0.2%	3,935	+13.1%
S&P/ASX 200 Property Trusts	877	863	+1.6%	783	+12.0%
US S&P 500	1,065	1,089	-2.2%	943	+12.9%
Dow Jones Eurostoxx	246	250	-1.6%	231	+6.5%
UK FTSE 100	5,126	5,188	-1.2%	4,387	+16.8%
Japan TOPIX	890	879	1.3%	911	-2.3%
CITIC/S&P 300 China A	2,324	2,411	-3.6%	2,458	-5.5%
MSCI (ex-Aust/in LC)	787	798	-1.4%	708	+11.2%
Aust 90-day bank bill yield	4.83	4.88	-5 bps	3.27	+156 bps
Aust 10-year bond yield	5.28	5.35	-7 bps	5.51	-23 bps
US 10-year bond yield	3.20	3.29	-9 bps	3.71	-51 bps
Oil – West Texas Crude	US$71.51	US$73.97	-3.3%	US$68.81	+3.9%
A$ in US cents	US$0.8203	US$0.8438	-2.8%	US$0.8015	+2.3%
TWI	67.4	67.8	-0.6%	63.8	+5.6%

Major upcoming global economic releases and events

Date	Data/Event	Units*	Previous	Market Forecast
10 June	Australia – unemployment rate, May	-	5.4%	5.4%
9 June	Australia – Westpac consumer confidence, June	-	-7%	-
10 June	US – Trade balance, April	US$ million	-40,423	-41,000
11 June	China – Consumer price index (CPI), May	index	4.4	-
11 June	US – retail sales, May	mom	0.4%	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

- While the situation in Europe remains tenuous with new concerns about Hungary's finances, there are several reasons why the European debt crisis is unlikely to knock the world economy into a double-dip recession: Spain, Portugal and Greece are only 16% of euro-zone economic activity, the fall in the euro will provide a boost to European economic activity, Europe would only contribute 0.3% to world growth this year anyway, and the US recovery is looking increasingly self-sustaining with the labour market picking up and growth in Asia continuing to surprise.
- As expected the RBA left interest rates at 4.5%. We see the uncertainty about global growth and signs of softness in domestic housing and consumption resulting in rates remaining on hold at least out to August.

Major global economic releases and implications

- US economic data was mixed with the ISM business conditions indexes remaining at high levels, factory orders exceeding expectations, construction spending rising strongly in April, vehicle sales up in May, layoffs remaining well below year ago levels and pending home sales surging in April. However, a sharp fall in mortgage applications over the last month suggests that the housing sector has weakened after the expiration of the first home buyers' tax credit, and growth in private sector employment was weak in June suggesting that the recovery still remains fragile.
- European economic data was generally soft with measures of industrial and consumer confidence dipping a notch in May, retail sales falling in April and euro-zone unemployment rising to 10.1%.
- Chinese manufacturing and services conditions surveys recorded a dip in May and input prices fell sharply confirming that the Chinese economy is cooling down from the unsustainable growth of 11.9% for the year to March.

Australian economic releases and implications

- The pace of GDP growth in Australia slowed in the March quarter but it is likely to pick up in the June quarter with solid retail sales growth in March and April pointing to a pick up in consumer spending, the lagged rise in building approvals likely to flow through to stronger housing construction and business investment remaining on track.

Major market moves

- Shares started weak, had a strong bounce on the back of solid US economic data and then fell sharply in response to weaker than expected US employment growth and worries about Hungary.
- Australian shares were hampered by earnings downgrades, worries about reduced Chinese commodity demand and ongoing worries about the impact of the Resources Super Profits Tax.
- Commodity prices fell on concerns about Chinese demand, the fragility of the US recovery and the rise of the US$.

What to watch in the week ahead?

- Chinese economic data for May will likely be the key focus with inflation likely to increase to 3% year on year (from 2.8% in April) and data for new loans, industrial production, investment and property prices are likely to show the economy cooling down adding to expectations that China will soon ease up on its tightening measures.
- The focus in the US will be May retail sales which should fall slightly after several months of gains.
- In Australia, May data should show a modest 10,000 extra jobs and the unemployment rate falling back to 5.3%. Consumer and business confidence readings from Westpac and National Australia Bank are likely to show modest falls with renewed worries about the economic outlook.

Outlook for markets

- While share markets remain twitchy it's likely that the bulk of the correction is behind us. Shares are very oversold and cheap. Investor sentiment towards shares has fallen so far that it's now positive from a contrarian perspective. The global recovery should remain on track providing a further boost to profits. 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 an easing in property tightening measures in the months ahead. Our view remains that the cyclical recovery in shares that commenced in March last year is still on track, but markets are likely to remain very choppy.
- The Australian dollar should regain strength over the next few months as Australian interest rates remain well above global rates and as commodity prices resume their upswing. By contrast, after a likely bounce from oversold conditions the euro is likely to continue to struggle on the back of relatively weak growth prospects in the euro-zone.
- Gold is likely to remain a long-term beneficiary of the uncertainty about major currencies.
- While government bonds have had a good run over the last few weeks on the back of safe haven buying, their low yields are pointing to poor returns over the medium term. As higher global interest rates are priced in and given the large supply of government bonds, investors will demand a higher risk premium to invest in them.

Further information
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AMP Capital's Client Service Team on 1300 139 267
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