J.P.Morgan

Global Data Watch

- **A surprising Fed raises the role of discretion in forward guidance**
- **PMIs are stronger than our forecast, adding focus on September flash**
- **EM problems persist but Fed relieves pressure for monetary tightening**

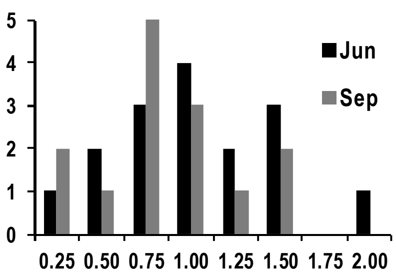
Discretion is the better part of guidance

The response to this week's FOMC decision brings to mind an old joke highlighting the power of Fedspeak: "This morning's market dive on the outbreak of nuclear war was reversed by hints of Fed easing." This week's market reversal came as the FOMC altered expectations that they themselves promoted starting in May. They stepped back from a widely expected September tapering move and downplayed the increased role of the unemployment rate in their forward guidance. On the unemployment rate, Chairman Bernanke jettisoned a June signal that the Fed would complete its purchase program about the time the unemployment rate reached 7%. He also diminished the unemployment rate's role as a guide to timing the first rate hike, arguing that "in making its assessment, the Committee would also take into account additional measures of labor market conditions, such as job gains. Thus, the first increases in short-term rates might not occur until the unemployment rate is *considerably* below 6-1/2 percent" [emphasis ours].

While recognizing the uncertainty created by a committee that has significantly surprised the market at its last two meetings in which economic projections were updated, we take two messages from this week's FOMC meeting:

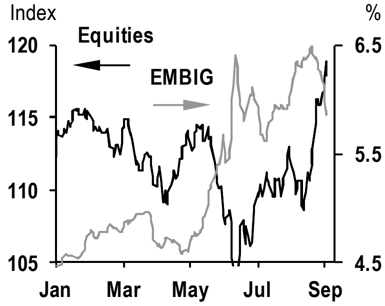
- **The Fed strengthens its growth bias.** Whereas Fed officials have generally brushed off concerns about higher interest rates this summer, rising rates loomed large in the FOMC's newfound skittishness about the health of the recovery. They also expressed concern about the upcoming fiscal debates. If we are right that downside growth risks do not materialize—the economy is expected to pick up steam into year-end—it is reasonable to continue to expect the Fed's purchase plan to be completed by mid-2014. But more than the short delay in tapering, the message of a heightened sensitivity to growth risks should have a lasting impact on the distribution of possible policy actions in the quarters ahead.

FOMC appropriate rate of policy, end-15
Number, excl forecasts above 2%



Source: J.P. Morgan, FRB

EM equities and USD sovereign rates
Index %



Source: J.P. Morgan

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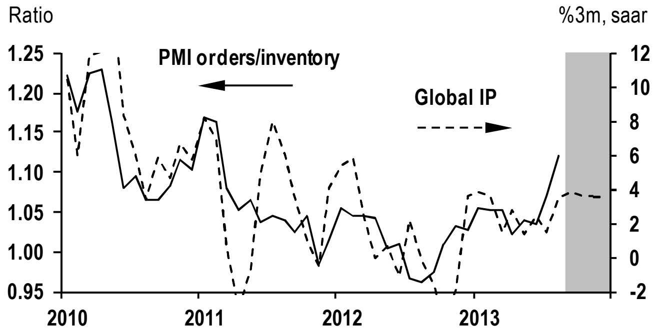
Global manufacturing



Source: J.P. Morgan

- **Less rule-based, more discretionary forward guidance.** The Fed has moved down the path of quantitative state-contingent forward guidance over the past year—providing an indication of how economic variables will guide the path of policy. The goal in this effort is to reduce uncertainty by creating a credible and direct feedback loop between the evolution of the economy and the expected path of policy. There is, however, a tension between the clarity provided by simple rules and the need for the Fed to maintain discretion. If anything, this tension has been heightened by the Fed's reliance on the unemployment rate—the rapid decline of which has opened up a lively debate about its value as a measure of slack and the economy's capacity to grow. This week's press conference saw the Fed rebalance its forward guidance in the direction of greater emphasis on discretion—reflecting its open-mindedness about measures of economic slack.

Both of these developments should be positive for risky assets. However, this week's events also highlight the work-in-progress nature of the Fed's forward guidance framework, which will soon be led by a new chair. We are also aware of the inherent time inconsistency problem in forward guidance. The nature of this increase in uncertainty could have negative consequences down the road.

EM CBs gain breathing space from the Fed

A Fed that has a stronger growth bias than previously thought is supportive for growth everywhere, including in the EM, where financial markets have bounced and currencies have lifted or at least stabilized of late. However, it is important to not overestimate the impact of this week's news. The EM accounts for nearly all the downward revisions to our global growth outlook since the start of this year. This disappointment largely reflects the unwinding of the domestic credit cycle that kicked into high gear following the global financial crisis as well as a growing concern over depressed corporate profit margins in the face of weak pricing power and strong wage growth. Consequently, we believe a delayed Fed tapering buys time for EM policymakers, but does not change the nature of the adjustments that lie ahead.

This is particularly true in those economies with inflation pressures from past currency declines and rising inflation expectations. Indeed, this week, India's and South Africa's central banks delivered more hawkish-than-expected outcomes in meetings that followed the FOMC. With the Indian rupee 10% stronger over the last three weeks, the RBI began unwinding the emergency measures by reducing the upper end of the policy corridor as we had anticipated. However, the central bank surprised everyone by hiking its policy rate, emphasizing that it is still focused on price stability, and signaled that further hikes would be forthcoming. The SARB remained on hold but struck a hawkish tone due to a further deterioration in the inflation outlook. Despite a softening in the economy and the relief rally following the Fed, we maintain our call for a hike by mid-2014. In Turkey, the CBRT meeting delivered few surprises (it was prior to the Wednesday Fed meeting). The bank has been leaning toward the dovish side, but this week's statement underlined its determination to tighten policy further unless inflation returned to its medium-term target.

Elsewhere, the recent improvement in currencies is being used to slow the pace of tightening. In Brazil, we believe the current relief trims the risk for more policy rate tightening than the 75bp of additional hikes that we are forecasting. Similarly, Bank Indonesia's need to hike aggressively to defend its currency has been tempered with the latest strength in the rupiah and we now expect a slower pace of rate hikes in the coming months.

In Mexico, the statement accompanying Banxico's surprising 25bp cut in early September was already quite dovish, raising the probability of an additional rate cut in October. With the Fed failing to taper and the consequent MXN appreciation, we believe a window has opened for an additional 25bp rate cut. We also see increased odds of further action in Chile, where we are already expecting a 25bp cut next month.

Flash PMIs: stable would be very good

Our global PMIs rose impressively in August, signaling upside risk to our growth forecast. In particular, the manufacturing PMI orders/inventory ratio vaulted to a level consistent with robust global IP gains of 6% annualized. The available August IP reports suggest acceleration is already underway. Global IP appears on track for a 0.4%m/m gain last month, lifting the 3-month rate to 3.5% annualized, in line with the pace of GDP growth we expect in the coming quarters.

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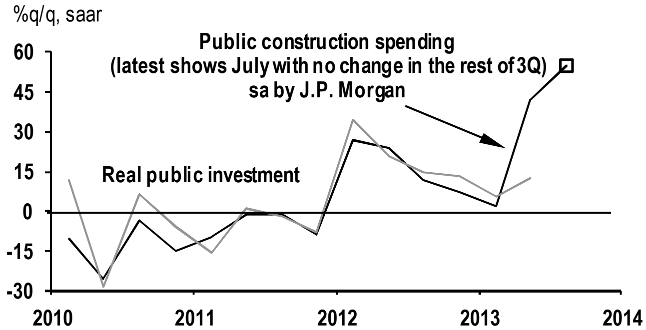
Public investment, Japan



Source: MLIT, Cabinet Office, J.P. Morgan

The key question is whether global IP growth will stabilize now, or accelerate further, in line with the orders/inventory ratio. Next week's flash September PMIs from the US, the Euro area, and China, which together account for nearly 60% of global manufacturing output, will give guidance on this question. If our forecast for trend GDP growth is correct, the flash PMIs should soon deliver a meaningful decline in the global orders/inventory ratio. A stabilization or rise in this ratio would increase the odds that IP growth is poised to materially overshoot our forecast.

Japan to take on further insurance

The trajectory of GDP in Japan is looking even more impressive. In the near term, economic activity looks to be expanding somewhat more strongly than projected this quarter. Public construction spending was reported to have shot up even further in July and now stands an impressive 55% annualized above its 2Q level. Also encouraging this week was a reported 6.4% jump in real exports last month that more than offset July's surprising 4.9% decline.

Discussions are heating up regarding the stimulative measures needed to cushion a consumption tax rate hike in April 2014. We assume a package with ¥3 trillion but the latest estimates are now ranging from ¥5-10 trillion (or 1% to 2% of GDP), including an earlier end of a corporate surcharge to help pay for Tohoku rebuilding and new auto incentives. Assuming some of this is offset elsewhere in the budget and only about ¥4 trillion ends up as new stimulus, this would offset over half of the nearly 2%-pt drag from the consumption tax hike and scheduled social insurance premium hike (worth ¥9 trillion, combined). Abe is expected to announce his intentions to move forward with the consumption tax in early October, at which point he could unveil the stimulus package alongside his longer-term growth strategy.

Germany votes, Europe waits

The results of the German Federal Election will likely be clear before European markets open on Monday morning. Chancellor Merkel's CDU is almost certain to be the largest party represented, but a range of coalition options are possible and the parties will spend a significant period of time—potentially several weeks—debating the composition of a new government. If the current coalition of the CDU/CSU-FDP is returned, this process will focus on the distribution of ministerial responsibilities and should be completed relatively quickly. If the Chancellor is forced to enter a Grand Coalition with the center-left SPD, we expect a more prolonged period of uncertainty. The Bundestag itself needs to meet within 30 days (by October 22), but it is possible that a full coalition agreement may not be implemented by that time.

Antipodean divergences

As growth outcomes between Australia and New Zealand diverge, so do their central bank reactions. With growth soft, unemployment rising, and inflation tamed, this week's spike in AUD to a three-month high increases our conviction that the RBA will trim the cash rate in November. By contrast, economic activity in New Zealand is accelerating and the jobless rate continues to fall. Whereas a senior RBA official this week called claims of froth in the Australian housing market "alarmist," the RBNZ is increasing its macro-prudential measures to contain the credit excesses seen in housing. The RBNZ's restrictions on high LTV lending, which start next month, are likely to have a more profound interaction with the policy rate than we had anticipated, so we have pushed out the likely timing of the first rate hike to 2Q14, from 4Q13.

Iranian president sends positive signals

The prospects for constructive negotiations over Iran's nuclear program appear to be increasing. President Obama and President Rouhani recently exchanged private letters that opened the door to direct talks. Rouhani has made numerous gestures of goodwill ahead of this address to the UN General Assembly on September 24, which is expected to mark a clear shift from his predecessor. In an op-ed letter to the *Washington Post*, he reiterated promises to "engage in constructive interaction with the world." The presidents may meet on the sidelines of the UN Assembly. This would be the first such meeting since 1977 and would mark an important confidence-building measure. Importantly, press reports have indicated that President Rouhani may be willing to shut down the Fordow nuclear site in exchange for an easing of international sanctions.

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Global economic outlook summary

	Real GDP			Real GDP							Consumer prices				
	% over a year ago			% over previous period, saar							% over a year ago				
	2012	2013	2014	4Q12	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	4Q12	2Q13	4Q13	2Q14	4Q14
The Americas															
United States	2.8	1.6	2.5	0.1	1.1	2.5	2.0	2.5	2.3	2.5	1.9	1.4	1.5↓	2.0↓	1.7
Canada	1.7	1.7	2.2	0.9	2.2	1.7	2.5	2.1	1.9	2.2	0.9	0.8	1.6	1.8	2.0
Latin America	2.6	2.6↑	3.0	3.8	1.9	4.7↑	0.7↓	1.7	4.2	3.2	4.7	5.2	4.7	4.6	4.8
Argentina	1.9	5.3	1.5	6.0	6.3	14.2	4.1	-9.6	11.0	0.0	10.6	10.0	11.0	11.0	11.0
Brazil	0.9	2.3	2.3	3.1	2.6	6.0	-2.0	1.5	2.9	3.4	5.6	6.6	6.0	5.7	5.8
Chile	5.6	3.8	4.0	8.2	3.2	1.9	3.0	3.0	6.0	2.7	2.2	1.3	2.2	3.8	3.9
Colombia	4.2↑	3.8↑	4.5	6.9↓	1.2↓	8.9↑	2.0↓	4.5	4.5	4.7	2.8	2.1↓	2.9	3.0	2.9
Ecuador	5.1	3.0	4.0	4.8	0.8	3.0	3.5	4.0	4.0	4.0	4.6	2.9	2.2	2.0	3.2
Mexico	3.8	1.8	4.0	3.0	0.1	-2.9	3.4	4.5	4.0	3.6	4.1	4.5	3.4	3.1	3.7
Peru	6.3	5.5	6.0	2.4	5.5	7.5	5.5	6.0	6.5	6.0	2.9	2.5	2.6	2.5	2.5
Uruguay	3.9	3.5	4.0	-1.9↓	7.2↑	9.5↑	7.0	6.0	4.0	3.0	8.5	8.1↓	7.7	7.1	6.6
Venezuela	5.6	0.0	3.0	3.5	-5.1	6.4	1.5↓	2.5	3.0	3.0	18.7	33.0	44.7	40.8	30.7
Asia/Pacific	4.8	4.5	4.5	5.5	4.2	4.8↓	4.5	5.2	5.1	2.7	2.2	2.2	3.0	3.8↓	3.5↓
Japan	2.0	1.9	1.6	1.1	4.1	3.8	2.3	3.8	4.0	-4.5	-0.2	-0.3	1.0	3.2	2.9
Australia	3.7	2.4	2.7	2.7	2.2	2.4	1.9	1.7	2.7	3.4	2.2	2.4	2.3	2.5	2.0
New Zealand	2.7	2.6↑	2.8	6.6↑	1.6↑	0.7↓	3.6↑	3.0↓	3.5	1.6	0.9	0.7↓	1.7↓	2.3↓	2.2↓
Asia ex Japan	6.2	6.0	6.0	7.8	4.6	5.7	5.9	6.3	6.0	5.9	3.4	3.3	4.0↓	4.3↓	3.9
China	7.7	7.6	7.2	9.3	6.2	6.7	7.8	7.8	7.0	7.0	2.1	2.4	3.0	3.6	3.2
Hong Kong	1.5	3.1	3.3	5.7	0.8	3.2	3.8	4.0	2.0	3.5	3.8	4.0	3.7	3.7	3.2
India	5.0	4.1	5.0	5.5	5.1	3.1	3.0	4.5	5.5	4.8	10.1	9.1	9.5	8.5	8.5
Indonesia	6.2	5.5	4.9	6.5	5.8	5.6	4.0	4.5	5.0	5.0	4.4	5.6	9.3↓	7.5↓	4.6↑
Korea	2.0	2.7	3.7	1.1	3.4	4.5	3.8	4.0	4.0	3.5	1.7	1.1	1.4	2.9	2.9
Malaysia	5.6	3.3	5.7	16.6	-13.0	7.1	5.5	5.5	5.5	6.0	1.3	1.8	2.7↑	2.3↑	1.5
Philippines	6.8	7.1	5.6	7.8	9.6	5.7	4.9	5.7	5.7	5.7	3.0	2.7	3.2	3.7	3.2
Singapore	1.3	3.4	3.8	3.3	1.7	15.5	-0.8	4.5	3.4	3.4	4.0	1.6	2.1	3.4	2.6
Taiwan	1.3	2.1	3.4	7.1	-2.5	2.3	2.8	3.5	3.4	3.7	1.8	0.8	1.3	2.2	2.2
Thailand	6.5	2.6	3.0	11.4	-6.5	-1.4	2.6	3.5	3.8	4.0	3.2	2.3	1.9	2.2	2.8
Africa/Middle East															
Israel	3.3	3.6	3.5	3.0↓	2.6↓	4.9↓	3.6	3.6	3.2	3.6	1.6	1.2	2.2	1.9	2.2
South Africa	2.5	2.1	3.3	2.1	0.9	3.0	2.6	3.2↑	3.6↑	3.3 ↓	5.6	5.7	5.5↓	6.0	5.9↓
Europe	0.1	0.3	1.8	-1.3	-0.2	1.4	1.4	1.5	1.8	1.8	3.0	2.4	2.2	2.2	1.9
Euro area	-0.6	-0.3	1.3	-1.9	-0.6	1.2	0.5	1.0	1.5	1.5	2.3	1.4	1.4↑	1.6↑	1.1
Germany	0.9	0.5	1.9	-1.8	0.0	2.9	1.0	2.0	2.0	2.0	2.0	1.5	1.8↑	1.9↑	1.7
France	0.0	0.2	1.1	-0.7	-0.6	1.9	0.5	0.5	1.0	1.5	1.7	0.9	1.2↑	1.6↑	1.1
Italy	-2.4	-1.7	1.1	-3.7	-2.4	-1.2	0.5	1.0	2.0	1.5	2.6	1.3	1.5	1.5	1.0
Spain	-1.6	-1.4	0.7	-3.0	-1.5	-0.4	0.0	0.0	1.0	1.0	3.2	1.8	0.9↑	1.0↑	0.3
United Kingdom	0.2	1.5	3.1	-0.9	1.1	2.9	3.5	3.5	3.0	2.5	2.7	2.7	2.5	2.4	2.2
Emerging Europe	2.3	1.8	2.7	0.9	0.5	1.3	3.6	2.1↑	2.1	2.5 ↑	5.7	5.6	4.9	4.5↓	4.4↓
Bulgaria	0.8	1.2	1.7	...	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	-1.2	-0.9	1.8	-1.4	-5.1	2.5	2.6	2.0	1.4	1.8	2.8	1.5	1.3	0.9	2.1
Hungary	-1.7	0.5	1.8↑	-2.1	2.3	0.3	1.5	2.5↑	2.0↑	2.0 ↑	5.4	1.8	1.3↓	2.0↓	2.7↓
Poland	1.9	1.4↑	2.8↑	0.4	0.8	1.6	3.5↑	2.5	2.5	2.5	2.9	0.5	1.3↓	2.1↓	1.9
Romania	0.7	2.6	2.3	4.1	1.5	2.2	5.3	2.4	1.6	1.2	4.8	5.3	2.5	1.9	3.7
Russia	3.4	1.6	2.5	1.2	0.9	1.0	3.7↓	2.0↑	2.2	2.7	6.5	7.2	5.7↑	4.9↓	4.7↓
Turkey	2.2	3.5	3.8	...	...	...	...	...	...	...	6.8	7.0	7.8	7.0	6.2
Global	2.5	2.3	3.0↑	1.8	1.9	3.1	2.6	3.0	3.2	2.4	2.5	2.3	2.5	2.9	2.6
Developed markets	1.4	1.1	2.0	-0.3	1.1	2.2	1.7	2.2	2.3	1.2	1.7	1.2	1.5	2.0↓	1.8
Emerging markets	4.6	4.4	4.7	5.7↓	3.3	4.8↑	4.2↓	4.5	4.9	4.7	4.1	4.1	4.3↓	4.4↓	4.2
Memo:															
Global — PPP weighted	3.1	2.8	3.4	2.7	2.2	3.4	3.0↓	3.4	3.7	3.0	3.0	2.7	2.9↓	3.2↓	3.0

Note: For some emerging economies, 2013-2014 quarterly forecasts are not available and/or seasonally adjusted GDP data are estimated by J.P. Morgan.
Bold denotes changes from last edition of *Global Data Watch*, with arrows showing the direction of changes. Underline indicates beginning of J.P. Morgan forecasts. Unless noted, concurrent nominal GDP weights calculated with current FX rates are used in computing our global and regional aggregates. Latin America CPI aggregate now includes only those countries where central banks actively target inflation (excluding Argentina, Ecuador and Venezuela).

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G-3 economic outlook detail

					2012	2013				2014		
	2011	2012	2013	2014	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q
United States												
Real GDP	1.8	2.8	1.6	2.5	0.1	1.1	2.5	2.0	2.5	2.3	2.5	3.0
Private consumption	2.5	2.2	1.9	2.1	1.7	2.3	1.8	1.4	2.2	2.0	2.2	2.7
Equipment investment	12.7	7.6	3.5	6.0	8.9	1.6	2.9	5.8	6.0	6.0	6.0	7.0
Non-residential construction	2.1	12.7	0.9	6.0	17.5	-25.7	16.2	6.5	9.0	9.0	9.0	10.0
Intellectual property products	4.4	3.4	3.2	9.2	5.7	3.8	-0.9	5.0	4.0	3.5	4.0	4.0
Residential construction	0.5	12.9	13.5	15.1	19.8	12.5	12.9	9.6	16.0	15.0	15.0	18.0
Inventory change ($ bn saar)	33.6	57.6	51.9	33.3	7.3	42.2	62.6	58.1	44.9	31.3	32.7	34.5
Government spending	-3.2	-1.0	-2.2	-1.0	-6.5	-4.2	-0.9	-0.3	-1.7	-1.2	-0.7	-0.6
Exports of goods and services	7.1	3.5	2.6	5.8	1.1	-1.3	8.6	4.4	5.8	5.5	6.0	6.0
Imports of goods and services	4.9	2.2	1.4	4.2	-3.1	0.6	7.0	2.2	2.0	3.0	6.0	6.5
Domestic final sales contribution	1.9	2.4	1.5	2.4	1.5	0.5	1.9	1.9	2.4	2.3	2.6	3.1
Inventories contribution	-0.2	0.2	0.0	-0.1	-2.0	0.9	0.6	-0.1	-0.4	-0.4	0.0	0.0
Net trade contribution	0.2	0.2	0.2	0.2	0.7	-0.3	0.0	0.3	0.5	0.3	-0.1	-0.1
Consumer prices (%oya)	3.1	2.1	1.5	1.7	1.9	1.7	1.4	1.6	1.5	1.5	2.0	1.7
Excluding food and energy (%oya)	1.7	2.1	1.8	1.6	1.9	1.9	1.7	1.7	1.7	1.6	1.6	1.6
Federal budget balance (% of GDP, FY)	-8.3	-6.7	-3.9	-3.3								
Personal saving rate (%)	5.7	5.6	4.5	4.8	6.6	4.1	4.5	4.7	4.7	4.7	4.8	4.8
Unemployment rate (%)	8.9	8.1	7.5	7.0	7.8	7.7	7.6	7.4	7.2	7.1	7.0	6.9
Industrial production, manufacturing	3.4	3.9	2.3	2.5	2.4	4.9	-0.4	3.0	4.0	2.0	2.0	3.0
Euro area												
Real GDP	1.6	-0.6	-0.3	1.3	-1.9	-0.6	1.2	0.5	1.0	1.5	1.5	1.5
Private consumption	0.3	-1.4	-0.6	0.8	-1.8	-0.8	0.7	0.0	0.5	1.0	1.0	1.3
Capital investment	1.7	-3.7	-3.6	1.3	-4.8	-8.5	1.0	-1.0	1.0	2.0	2.0	1.5
Government consumption	-0.1	-0.6	0.2	0.7	0.4	0.0	1.7	0.0	0.5	0.5	1.0	1.0
Exports of goods and services	6.5	2.7	1.1	4.2	-2.2	-4.0	6.8	4.0	4.0	4.0	4.0	4.0
Imports of goods and services	4.5	-1.0	0.0	3.9	-3.5	-4.2	5.5	3.5	3.5	4.0	4.0	4.0
Domestic final sales contribution	0.5	-1.6	-0.9	0.8	-1.8	-2.1	0.9	-0.2	0.6	1.0	1.1	1.2
Inventories contribution	0.2	-0.5	0.1	0.1	-0.6	1.5	-0.5	0.3	0.0	0.3	0.2	0.1
Net trade contribution	0.9	1.6	0.5	0.3	0.5	-0.1	0.8	0.4	0.4	0.2	0.2	0.2
Consumer prices (HICP, %oya)	2.7	2.5	1.5	1.3	2.3	1.9	1.4	1.4	1.4	1.3	1.6	1.3
ex unprocessed food and energy	1.7	1.8	1.3	1.1	1.6	1.5	1.3	1.3	1.3	1.2	1.3	1.1
General govt. budget balance (% of GDP, FY)	-4.2	-3.7	-2.8	-2.1								
Unemployment rate (%)	10.2	11.4	12.2	12.3	11.8	12.0	12.1	12.2	12.3	12.3	12.3	12.3
Industrial production	3.2	-2.3	-0.3	2.7	-7.5	0.9	4.8	0.5	2.5	3.0	3.0	3.0
Japan												
Real GDP	-0.6	2.0	1.9	1.6	1.1	4.1	3.8	2.3	3.8	4.0	-4.5	1.2
Private consumption	0.5	2.4	1.9	1.0	2.0	3.4	3.0	0.5	4.2	5.5	-8.5	1.0
Business investment	3.3	1.8	-0.7	4.8	-4.8	-0.1	5.1	7.0	5.0	5.0	3.5	4.2
Residential construction	5.5	3.0	7.8	2.0	15.1	7.7	-1.0	10.0	12.0	8.0	-10.0	-8.0
Public investment	-7.0	12.5	12.5	2.8	13.5	5.8	12.7	20.0	10.0	0.0	-10.0	0.0
Government consumption	1.4	2.4	1.6	1.5	2.5	0.2	3.0	1.5	1.5	1.5	1.2	1.0
Exports of goods and services	-0.4	-0.1	2.1	5.0	-10.2	16.8	12.4	0.5	6.0	5.5	4.7	4.5
Imports of goods and services	5.9	5.5	2.3	5.4	-7.8	4.1	6.2	7.0	8.0	9.0	-2.0	4.3
Domestic final sales contribution	0.8	2.7	2.1	1.6	1.5	2.5	2.9	3.4	4.2	4.5	-5.6	1.2
Inventories contribution	-0.5	0.0	-0.2	-0.1	0.1	-0.3	-0.2	-0.2	-0.2	-0.1	0.0	-0.1
Net trade contribution	-0.8	-0.8	0.0	0.0	-0.5	1.8	1.0	-0.9	-0.2	-0.4	1.0	0.1
Consumer prices (%oya)	-0.3	0.0	0.2	2.5	-0.2	-0.6	-0.3	0.7	1.0	1.0	3.2	2.9
General govt. net lending (% of GDP, CY)	-9.7	-10.0	-9.9	-8.4								
Unemployment rate (%)	4.6	4.4	4.1	3.9	4.2	4.2	4.0	4.0	4.0	4.0	3.9	3.9
Industrial production	-2.6	0.2	-0.6	4.2	-7.0	2.3	6.2	6.5	8.0	7.0	-8.0	7.5
Memo: Global industrial production	3.9	0.8	1.9	3.8	0.3	2.8	2.9	3.8	4.7	3.9	2.5	4.4
%oya					8.2	0.3	1.5	2.4	3.5	3.8	3.7	3.8

Note: More forecast details for the G-3 and other countries can be found on J.P. Morgan's Morgan Markets client web site

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Global Central Bank Watch

	Official rate	Current rate (%pa)	Change since (bp) 05-07 avg	Trough[1]	Jul 11	Last change	Next mtg	Forecast next change	Forecast (%pa) Sep 13	Dec 13	Mar 14	Jun 14
Global		2.13	-224	29	-62				2.20	2.23	2.23	2.23
excluding US		2.78	-153	30	-70				2.88	2.92	2.91	2.92
Developed		0.40	-309	0	-41				0.40	0.39	0.39	0.39
Emerging		5.35	-168	47	-91				5.58	5.69	5.67	5.69
Latin America		6.79	-398	91	-224				6.73	7.12	7.10	7.10
EMEA EM		3.51	-295	0	-81				4.64	4.60	4.36	4.41
EM Asia		5.48	-31	100	-54				5.51	5.56	5.61	5.63
The Americas		1.59	-373	42	-45				1.57	1.65	1.65	1.65
United States	Fed funds	0.125	-438	0	0	16 Dec 08 (-87.5bp)	30 Oct 13	On hold	0.125	0.125	0.125	0.125
Canada	O/N rate	1.00	-273	75	0	8 Sep 10 (+25bp)	23 Oct 13	4Q 14 (+25bp)	1.00	1.00	1.00	1.00
Brazil	SELIC O/N	9.00	-625	175	-350	28 Aug 13 (+50bp)	9 Oct 13	9 Oct 13 (+50bp)	9.00	9.75	9.75	9.75
Mexico	Repo rate	3.75	-412	0	-75	6 Sep 13 (-25bp)	25 Oct 13	25 Oct 13 (-25bp)	3.50	3.50	3.50	3.50
Chile	Disc rate	5.00	31	450	-25	12 Jan 12 (-25bp)	17 Oct 13	17 Oct 13 (-25bp)	5.00	4.50	4.25	4.25
Colombia	Repo rate	3.25	-406	25	-125	22 Mar 13 (-50bp)	27 Sep 13	Jul 14 (+25bp)	3.25	3.25	3.25	3.25
Peru	Reference	4.25	19	300	0	12 May 11 (+25bp)	10 Oct 13	On hold	4.25	4.25	4.25	4.25
Europe/Africa		1.16	-270	0	-80				1.40	1.39	1.34	1.35
Euro area	Refi rate	0.50	-248	0	-100	2 May 13 (-25bp)	2 Oct 13	On hold	0.50	0.50	0.50	0.50
United Kingdom	Bank rate	0.50	-444	0	0	5 Mar 09 (-50bp)	10 Oct 13	On hold	0.50	0.50	0.50	0.50
Czech Republic	2-wk repo	0.05	-235	0	-70	1 Nov 12 (-20bp)	26 Sep 13	On hold	0.05	0.05	0.05	0.05
Hungary	2-wk dep	3.80	-333	0	-220	27 Aug 13 (-20bp)	24 Sep 13	24 Sep 13 (-20bp)	3.60	3.20	3.00	3.00
Israel	Base rate	1.25	-300	75	-200	27 May 13 (-25bp)	23 Sep 13	On hold	1.25	1.25	1.25	1.25
Poland	7-day interv	2.50	-202	0	-200	3 Jul 13 (-25bp)	2 Oct 13	4Q 14 (+25bp)	2.50	2.50	2.50	2.50
Romania	Base rate	4.50	-369	0	-175	5 Aug 13 (-50bp)	30 Sep 13	30 Sep 13 (-50bp)	4.00	3.75	3.50	3.50
Russia	Repo rate	5.50	N/A	N/A	N/A	13 Sep 12 (+25bp)	Oct 13	Nov 13 (-25bp)	5.50	5.25	4.75	4.75
South Africa	Repo rate	5.00	-329	0	-50	19 Jul 12 (-50bp)	21 Nov 13	May 14 (+50bp)	5.00	5.00	5.00	5.50
Turkey	Effctve rate	6.52	-941	177	27	N/A[2]	23 Oct 13	N/A	6.50	7.00	7.00	7.00
Asia/Pacific		3.65	-2	75	-47				3.66	3.67	3.71	3.72
Australia	Cash rate	2.50	-344	0	-225	6 Aug 13 (-25bp)	1 Oct 13	Nov 13 (-25bp)	2.50	2.25	2.25	2.25
New Zealand	Cash rate	2.50	-488	0	0	10 Mar 11 (-50bp)	30 Oct 13	2Q 14 (+25bp)	2.50	2.50	2.50	2.75
Japan	O/N call rate[3]	0.05	-17	0	0	5 Oct 10 (-5bp)	4 Oct 13	On hold	0.05	0.05	0.05	0.05
Hong Kong	Disc. wndw	0.50	-548	0	0	17 Dec 08 (-100bp)	31 Oct 13	On hold	0.50	0.50	0.50	0.50
China	1-yr working	6.00	-14	69	-56	7 Jul 12 (-31bp)	-	On hold	6.00	6.00	6.00	6.00
Korea	Base rate	2.50	-165	50	-75	9 May 13 (-25bp)	10 Oct 13	4Q 14 (+25bp)	2.50	2.50	2.50	2.50
Indonesia	BI rate	7.25	-262	150	50	12 Sep 13 (+25bp)	8 Oct 13	4Q 13 (+25bp)	7.25	7.50	7.75	8.00
India	Repo rate	7.50	63	275	-50	20 Sep 13 (+25bp)	29 Oct 13	4Q 13 (+25bp)	7.50	7.75	8.00	8.00
Malaysia	O/N rate	3.00	-24	100	0	5 May 11 (+25bp)	7 Nov 13	On hold	3.00	3.00	3.00	3.00
Philippines	Rev repo	3.50	-356	0	-100	25 Oct 12 (-25bp)	24 Oct 13	On hold	3.50	3.50	3.50	3.50
Thailand	1-day repo	2.50	-133	125	-75	29 May 13 (-25bp)	16 Oct 13	On hold	2.50	2.50	2.50	2.50
Taiwan	Official disc.	1.875	-71	62.5	0	30 Jun 11 (+12.5bp)	26 Sep 13	4Q 14 (+12.5bp)	1.875	1.875	1.875	1.875

1 Refers to trough end-quarter rate from 2009-present ² Effective rate can be adjusted on daily basis 3 BoJ targets ¥50-60tn/year expansion in monetary base
Bold denotes move since last GDW and forecast changes. Underline denotes policy meeting during upcoming week. Aggregates are GDP-weighted averages.

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Nowcast global growth: All quiet on the 3Q front

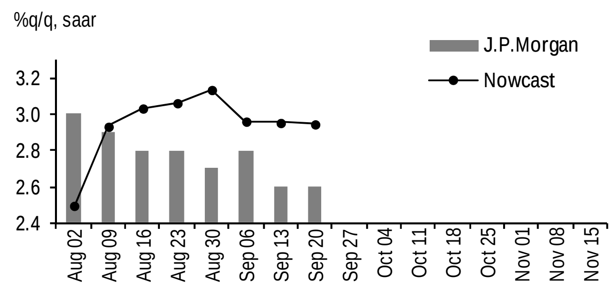
- This week brought a handful of relatively small revisions to our set of country-level current quarter forecasts, aggregating to an unchanged global projection of 2.6%. The national revisions of the largest magnitude—up in New Zealand and down in Colombia—came in response to surprising 2Q growth figures released this week. Apart from those, we modestly lifted our sights on current quarter growth in Poland while making small mark-downs to our Russia and Venezuela calls.
- For a second straight week, our global nowcaster was effectively unchanged. However, in rounded terms, the model projection nudged down to 2.9%, a low since August 9. With the nowcaster and global forecast printing close to their week-ago levels, the nowcaster continues to point to some upside risk to the official J.P. Morgan bottom-up global growth call in 3Q.
- This was a slow week for nowcast input data releases, with only small fine-tunings made to monthly figures already in hand. The largest changes in terms of magnitude (but not necessarily impact on the nowcaster output) came to our global auto sales calculations. Delayed by their summer holiday, Eurostat released auto registrations data for July and August this week. While the August level of sales was in line with our estimate, the monthly profile was a bit different. As a result we now calculate global auto sales to have grown 0.8%-pts slower in July than our previous figure, while bumping August growth 0.3%-pts higher. Also of note this week were the slightly weaker-than-expected global IP reports, with output now having risen 1.4%ar in the three months through July, from 1.5%.
- Next week marks the start of the busier portion of the nowcast data release calendar. On Monday we will receive the flash September manufacturing PMIs from the US, Euro area, and China, allowing us to project the global index for the month. This will provide our first signal of how global activity closed out the quarter. The surging orders-to-finished goods inventory ratio through August suggests further output gains are likely to be accrued in September.
- Today we update our global manufacturing nowcaster, which estimates the pace of output growth based on the common impulse in the price moves of oil, industrial metals, and agricultural commodities. The model projection has drifted higher since the middle of the year but remains depressed, currently pointing to very sluggish global manufacturing output growth. This stands in stark contrast with the manufacturing output PMI and the hard activity data. However, the nowcaster has consistently underpredicted IP since the start of the year, and thus the improvement over recent weeks could be seen (assuming the error persists) as consistent in the pickup presaged in the other indicators.

Global real GDP
%q/q, saar (Current forecast shaded)

	2Q13	3Q13		
		Current	Last week	4 weeks ago
J.P. Morgan	3.0	2.6	2.6	2.8
Nowcaster (DFM-Eco)	2.9	2.9	3.0	3.1
Global PMI model	2.3	3.2	3.2	2.8

Source: J.P. Morgan

Nowcasting global real GDP by forecast date, 3Q2013



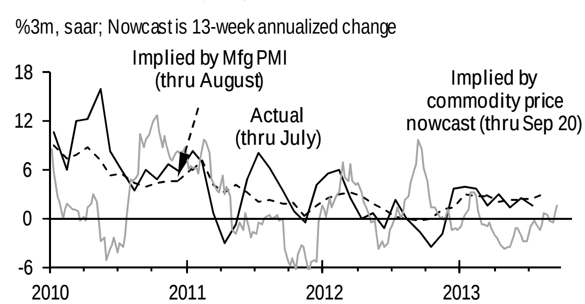
Source: J.P.Morgan

J.P. Morgan global aggregates
Quarters are %3m/3m,saar (PMIs avg level); Months are %m/m (PMIs level)

	2Q13	3Q13	Jun 13	Jul 13	Aug 13	Sep 13
PMI, mfg	51.3	52.1	51.4	51.5	52.3	52.4
PMI, serv	52.2	55.6	51.1	54.9	56.1	55.9
IP	2.2	2.6	0.4	0.1	0.4	0.3
Retail sales	4.6	4.0	0.1	0.4	0.3	0.3
Auto sales	9.7	-1.7	-0.9	0.2	-0.1	0.5
Cap. Orders	13.6	-2.8	-1.5	-2.1	1.7	0.0
Nowcast	2.9	2.9	2.6	2.9	3.3	3.2

Note. Shaded values show forecasts computed by the Kalman filter estimates from the dynamic factor model. Underlined values are our estimates based on available data and our judgment. Source: J.P. Morgan, Markit, and national statistical agencies.

Global manufacturing output



Source: J.P.Morgan

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1. Research notes listed have been published in *GDW; Special Reports* and *Global Issues* are stand-alone features, but may also have appeared in some form in *GDW.*

The J.P. Morgan View: Markets

Policy risk up. Economic risk down.

- **Asset allocation:** We go back long credit and EM as the Fed refocuses on the economy and away from perceived unemployment rate targeting.
- **Economics:** The FOMC's surprise non-taper raises policy uncertainty, but puts broad economic data back in charge of policy, reducing the risk of policy errors and economic uncertainty. We now see a Dec-to-June taper, but this all depends on better data. Manufacturing continues to gain.
- **Fixed income:** Cut duration shorts, but do not go long as US rates will eventually still go higher than even the Fed forecasts. Bearish curve trades.
- **Equities:** Upgrade EM equities to overweight.
- **Credit:** Close UW US vs. EU HG and go long US HY and EMBIG.
- **FX:** Dollar heading down again, on taper push back.
- **Commodities:** Buy gold on higher inflation risk after Fed's volte-face.

The FOMC shocked markets by deciding not to slow its large-scale asset purchase program, after all the signals it had sent out in previous months that it would do so. Investors are now all trying to rethink what this means for markets and policy, with many dismayed by the increased uncertainty about Fed policy. Our take is that **policy uncertainty has indeed increased**, but towards a more flexible and rational approach that improves the Fed's ability to support the economy. In our mind, **higher policy uncertainty has brought us lower economic uncertainty**. We thus add exposure to assets that should benefit from reduced economic uncertainty, such as equities, EM and corporate credit, away from assets that are more sensitive to policy uncertainty, such as nominal bonds.

Mr. Bernanke stated the FOMC decided to delay tapering as it wants to see more economic data, given the downside risks created by higher mortgage rates and the evolving US fiscal debate. In his press conference, he clearly downgraded the increasingly dominant role that the unemployment rate had taken in determining the end of QE purchases and the start of rate hikes. All this makes sense to us, but does appear a reversal from the steady march towards rate guidance and targets/triggers for the unemployment rate. We have commented that this approach had reached declining returns in that ever more guidance requires ever more discussion on what the Fed would and would not do under what circumstances up to three years out. Talk about future options becomes priced in immediately and the focus on the wide range of future options increases uncertainty and thus risk premia.

In one dramatic move, **Mr. Bernanke has reversed this steady march to a rule-based policy and has brought discretion and flexibility back**. The Fed may argue it never really gave up discretion, but we think the market nevertheless saw increased rigidity and thus a greater risk of policy errors. By bringing back discretion, the economy broadly, rather than just unemployment, has retaken precedence. This has reduced economic uncertainty. To use popular terms, the Bernanke Put and asset reflation are back, while the end-of-easy money trade needs to await better economic data.

Markets are still trying to decide what to make of the Fed's volte-face, with many participants first covering positions and even reversing them. Over time, we expect that the market will come to the view that the Fed made the right decision, pulling itself out of the rate guidance corner it had painted itself into. We ourselves had underestimated the ability of the FOMC to reverse course so fast and thus need to pare back the end-of-easy-money trades we had recommended. These positions involved underweighting EM assets and being neutral on credit, despite attractive spreads, as we thought both asset classes vulnerable to the tightening of US monetary policy that had started late May.

Our view is not that this eventual tightening will not happen: we are not changing the likely end to QE3 (mid next year) and only that tapering starts later (December). The second quarter of 2015 remains the likely first rate hike and we continue to think that rates will be higher in 2016 than the Fed's own forecast, keeping us bearish on duration. But, in our view, the perceived return of "the data" and policy flexibility greatly reduces the risk of unintended monetary tightening and policy errors and increases confidence that the Fed, joined by other major central banks, will "do what it takes" to support growth. We thus like a broader set of risk assets that depend on economic confidence, and remain wary of nominal risk premia (term) that are vulnerable to policy uncertainty and inflation. That means, we retain bearish bond views, even as we cut short duration position in the current position reversal environment.

Hence, we go back into credit and EM, two assets classes that were hurt by the perceived risk of premature monetary tightening. We add longs in HY, EM FX, EM external debt, and EM equities. We move our long equities to fixed income asset allocation back to full strength.

Fixed income

Global fixed income rallied strongly, but not dramatically, on the FOMC's decision not to start slowing its large-scale asset purchase program. Rate investors remain dismayed, though, about the Fed's communication chaos and are not eager to go long duration.

We are staying with **bearish bond yield forecasts** on a view that the outlook for Fed rates has not changed and that the return of the Bernanke put, via higher risk asset prices, will be bullish for the economy and thus will eventually require higher short rates than are currently priced in and forecast by the FOMC itself. The Washington gridlock around the budget and the debt ceiling has a very ambiguous impact on bond yields, but its uncertainty will likely keep rate investors from going long carry. We stay bearish duration and overweight the EMU periphery.

EM local bonds have been caught in the turmoil around the Fed and the end of easy money. They rallied strongly with over 1% capital gains in local terms since the FOMC, on our GBI-EM index, greatly outperforming developed market bonds. We cut much of our underweights in local EM bonds (see Joyce Chang and Luis Oganes, *Keep calm and carry on: Upgrading EMBIG to OW and removing the EM FX hedge*, Sep 19).

Equities

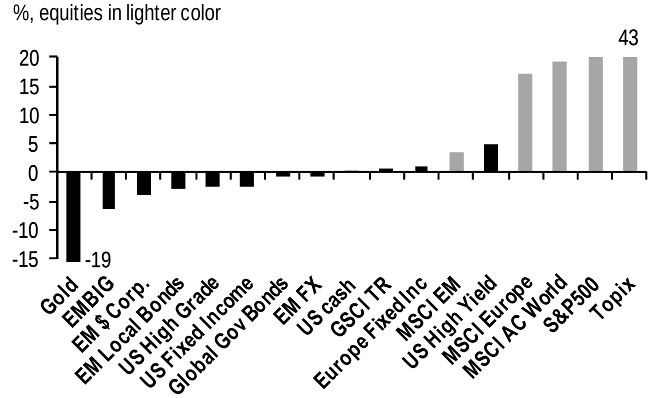
Equities rose sharply following this week's unexpected FOMC decision. The Fed is providing insurance against downside risks to the US economy, supporting growth assets such as equities.

The assets that suffered the most previously due to tapering expectations, e.g., EM assets, are now rebounding forcefully. We cut our underweight in EM equities at the beginning of the month. **We now move EM equities to overweight** as flows into EM bonds and equities are rising. The first leg of these inflows is driven by fast money, but we expect real money investors to follow as the majority of real investors are tactically underweight or lagging their benchmarks.

We open a long in MSCI EM$ vs. MSCI World$ in our long/short portfolio. In our long only portfolio, we focus our overweights in Europe and EM equities at the expense of US and Japanese equities. The flow support is stronger for the former as shown in our weekly publication, *Flows & Liquidity*. US debt ceiling risks are a potential headwind for US equities. Japanese equities are lacking policy impetus right now.

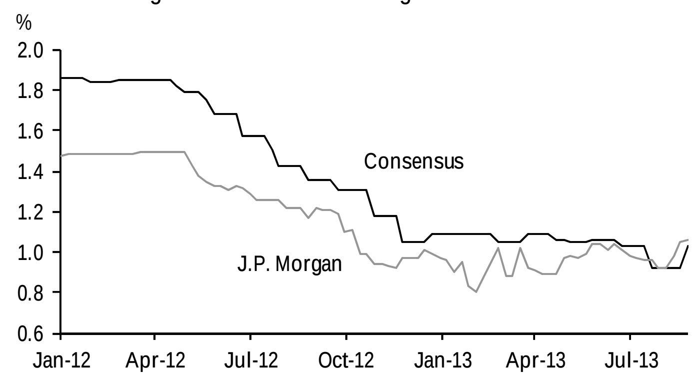
Our main sectoral view, to **overweight Cyclical vs. Defensive** sectors, is working. While the Fed's non-taper is somewhat helping certain Defensive sectors that had previously suffered from tapering expectations, we believe that the rebound in global manufacturing currently underway will allow Cyclical sectors to continue to outperform.

YTD returns through: 19-Sep
%, equities in lighter color



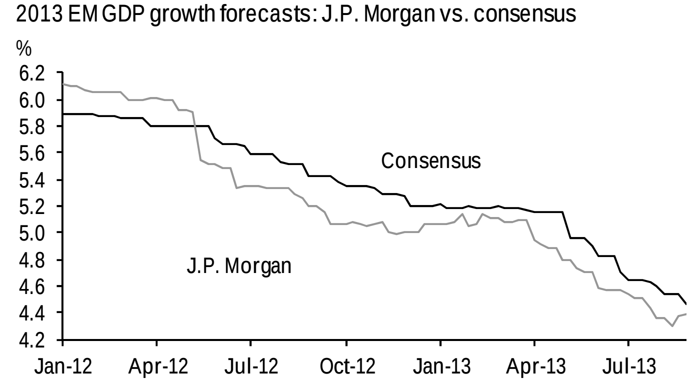
Source: Consensus Economics and J.P. Morgan

2013 DM GDP growth forecasts: J.P. Morgan vs. consensus
%



Source: Consensus Economics and J.P. Morgan

2013 EM GDP growth forecasts: J.P. Morgan vs. consensus
%



Source: Consensus economics and J.P. Morgan

We updated this week our quarterly publication "***Trade opportunities for long term investors***", Sep 19. In the equity space, we launched a long-term equity position in India, Indonesia and the Philippines vs. China, Korea and Taiwan. Currency strength is a drag for Chinese, Korean and Taiwanese equities. Coupled with differences in demographic trends, financial leverage risks and potential growth, we believe this is currently a good entry point to overweight India, Indonesia and the Philippines.

We took profit on our long position in 2014 FTSE dividend futures as the strength of the pound is eroding bottom-up dividend estimates. We remain OW European vs. US equities, Peripheral equities vs. DAX, and Cyclical vs. Defensive sectors.

We kept our equity risk premia monetization trades despite a sharp shrinkage of the yield gap between equities and bonds. Our S&P500 Equity Risk Premium estimate declined by 210bp since June 2012 as a result of the rally in equities and the rise in real bond yields. But at 4.9%, the S&P500 Equity Risk Premium remains two percentage points above its historical average. Stay long high dividend yield US Equity ETFs vs. 10y USTs.

Credit

Credit spreads came in sharply across the board following the Fed's no tapering announcement. The unemployment rate has been downgraded to only one of many pieces of economic data the Fed will use to assess when to finally bring an end to their very accommodative policies. This reduces the risk of further premature tightening in financial conditions simply because the unemployment rate is falling even if growth expectations remain subdued. This is positive for corporate cash flows and reduces economic uncertainty, and is thus positive for credit markets.

Corporate supply is now likely to pick up and stay elevated into year-end but we expect the last few months of QE trade to unwind to halt and to some extent reverse. Thus spreads should tighten into year-end with the credits most hit by expectations of tapering, tightening most. W**e close the UW of US vs. EU HG and we go outright long US HY. We also switch our OW EMBIG vs. CEMBI into an outright long in EMBIG**.

Foreign exchange

With Fed tapering pushed back until late 2013/early 2014, the trade-weighted USD is now expected to decline modestly into year-end. The trade weighted USD is currently close to fair value, so valuations should keep it range bound. However, on a more micro level, many EM pairs and commodity currencies screen cheap on short-term fair value models, while shorts in commodity currencies are well above what is normal when the global economy is delivering near-trend growth. This risk premium/extreme positioning could only be justified if US rates were moving higher imminently, a force much diminished, and there is no longer an argument for USD strength into year-end. Within the G10, USD is expected to weaken the most against CAD and NOK, but strengthen versus the Antipodeans and EUR. USD should be weaker against almost all EM Asia FX (notably INR and KRW), but strengthen versus EMEA EM (primarily a function of the drift lower in EUR/USD) although ZAR is a notable exception. In Latam, USD should be weaker only versus MXN, but stronger against the rest.

The 2014 targets are more debatable since tapering has been delayed rather than cancelled. Some of the impediments to tapering—government shutdown/debt ceiling debates—are temporary, and US Treasuries are still rich on most valuation measures (so a 3% US 10-yr can be reached easily on the right data triggers). The problem with reflexively translating this forecast for higher US rates into broader USD strength is that by the time US rates do move higher, more non-US economies could be lifting too. And since simultaneous regional upswings and rate rises tend to be USD negative (because the US is still a zero cash rate currency with a current account deficit) the list of currencies against which the dollar can rally next year is small. The weakest currencies should be TRY, IDR, AUD and MYR, and the strongest are CAD, MXN and NOK.

Commodities

Commodities are mixed this week, with energy down 2% while both base and precious metals rallied some 3.5%. Oil prices have given back some of their recent gains as a significant amount of Libyan oil production has come back online. In spite of this, supply in the oil market remains relatively tight as there are still production problems elsewhere. The Brent futures curve remains steeply downward sloping and still implies a 12% a year return from buying the front future and rolling into the second each month. **We expect spot prices to stabilize from here and we stay overweight energy via the GSCI energy index.**

This week's surprise by the Fed in not tapering their asset purchases led to a 5% rally in precious metals. In our view, the main driver of gold's performance over the past five years has been QE. Following the 2008 crisis, the unprecedented expansion of central bank balance sheets led to fears of inflation further down the road and resulted in very strong demand for gold, a large amount of which came via ETFs. As QE continued and inflation expectations remained subdued, this demand for an inflation hedge subsided, ETF positions were unwound and gold prices fell. Along with precious metals rallying, inflation breakevens widened following the Fed announcement, another indication that uncertainty around future inflation may pick up as a result of the Fed's volte-face on tapering. Additionally, positions are much cleaner now, following the unwinding of ETF positions, and physical demand from retail buyers in Asia has been very strong. **We open a long position in gold.**

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Forecasts & Strategy

Interest rates		Current	Dec-13	Mar-14	Jun-14	Sep-14
United States	Fed funds rate	0.125	0.125	0.125	0.125	0.125
	10-year yields	2.72	3.00	3.20	3.50	3.75
Euro area	Refi rate	0.50	0.50	0.50	0.50	0.50
	10-year yields	1.94	2.10	2.20	2.30	2.50
United Kingdom	Repo rate	0.50	0.50	0.50	0.50	0.50
	10-year yields	2.92	3.00	3.15	3.30	3.50
Japan	Overnight call rate	0.05	0.05	0.05	0.05	0.05
	10-year yields	0.69	0.80	0.85	0.90	0.90
Emerging markets	GBI-EM - Yield	6.41		0.00		
Credit markets						
US high grade (bp over UST)		162	145			
Euro high grade (bp over Euro gov)		142	110			
USD high yield (bp vs. UST)		481	450			
Euro high yield (bp over Euro gov)		475	400			
EMBIG (bp vs. UST)		326	325			
EM Corporates (bp vs. UST)		369	375			
Foreign exchange						
EUR/USD		1.35	1.33	1.33	1.32	1.32
USD/JPY		99	100	102	102	103
GBP/USD		1.60	1.60	1.63	1.61	1.61
AUD/USD		0.94	0.9	0.89	0.88	0.87
USD/BRL		2.21	2.35	2.40	2.45	2.45
USD/CNY		6.12	6.1	6.08	6.05	6.03
USD/KRW		1077	1060	1055	1050	1050
USD/TRY		1.98	2	2.05	2.1	2.15

Commodities	Current		14Q1	14Q2	14Q3
Brent ($/bbl)	109	117	117	113	118
Gold ($/oz)	1328	1325	1375	1400	1430
Copper ($/metric ton)	7321	7900	7600	7500	7700

YTD equity sector performance*	US		Europe		Japan		EM$	
Energy	16.5%	OW	6.3%	OW	9.9%	UW	-8.1%	N
Materials	12.6%	OW	0.2%	N	39.9%	UW	-17.2%	UW
Industrials	22.5%	OW	19.0%	UW	37.5%	OW	-3.9%	OW
Discretionary	27.5%	OW	22.6%	OW	49.6%	OW	2.7%	N
Staples	17.0%	UW	11.3%	N	39.3%	OW	-2.6%	UW
Healthcare	29.2%	OW	18.9%	OW	28.6%	UW	4.1%	N
Financials	24.0%	OW	19.1%	OW	51.6%	OW	-4.6%	N
Information Tech.	13.3%	OW	21.0%	OW	28.7%	UW	6.0%	OW
Telecommunications	7.2%	N	23.8%	UW	68.7%	OW	-1.9%	UW
Utilities	7.9%	UW	10.2%	UW	43.5%	UW	-8.5%	N
Overall	19.2%		15.7%		39.8%		-3.9%	

*Levels/returns as of Sep 19, 2013
Source: J.P. Morgan

Investment themes and impacts

Growth rotations
Europe and Japan show positive growth momentum: OW in equities. OW EMU periphery. EM remains negative, but should stabilize.

Manufacturing rebound
OW Cyclicals and base metals. Industrial EMs outperform importing EM's.

End of easy money : DOWNGRADED
Unwinding of search-for-yield assets. Short bond duration. Credit spreads have difficulty tightening. UW EM in FI and FX.

Cycle at mid-age
Bonds in bear market; credit spread tightening over. Equities outperform. Growth should accelerate. Confidence should improve.

Value
Only ERP is above historic mean, while others are near or below their means.

Momentum
Long equities and commodities; short bonds; UW EM; neutral credit.

Source: J.P. Morgan, *GMOS*, Sep 4, 2013

Tactical overview

	Direction	Country	Sector
Asset allocation	Long real risk premia vs. nominal	EU, EM	OW Equities, Comm's vs FI and cash
Equities	Bullish	EU, EM	Cyclicals
Bonds	Bearish		UW Belly in US. OW periphery.
Credit	Long	OW HY	FINs; BBB's vs. A's
FX		Short $	
Comd's	Long on industrial rebound		Long energy. & metals. Corn vs. soybeans.

Source: J.P. Morgan

Economic Research Note

The macro consequences of the AQR and stress test

- **Euro area banks to undergo a balance sheet assessment next year ahead of the launch of the banking union**
- **Pressure on banks to provision more and raise capital**
- **AQR and stress test likely to keep borrowing rates for households and corporates elevated**
- **Capital backstop unlikely to prevent this**

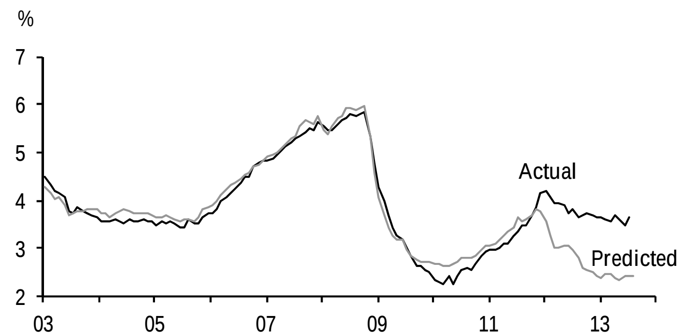
Ahead of the launch of the banking union in the autumn of 2014, Euro area banks will undergo an assessment of their balance sheets next spring. This assessment has two parts: an asset quality review (AQR) and a stress test. There are concerns that these exercises will do damage to the real economy in the short term, even though they are well intentioned for the long term.

These macro concerns are focused on whether there will be a well-defined backstop for potential capital needs. But, this focus misses an important point. The AQR could do damage to the real economy regardless of the existence of a capital backstop. The AQR will put pressure on banks' provisioning for non-performing loans. In the first instance, this is a shock to a bank's income. The AQR could contribute to persistently elevated borrowing costs for households and non-financial corporates, until the additional provisioning process is complete. The pressure for more capital could well come from the stress test. Nevertheless, the stress test could have an impact on borrowing costs similar to the AQR's given that banks will have an opportunity to meet additional capital needs on their own before resorting to public sector resources available in the backstop.

The nature of the exercises

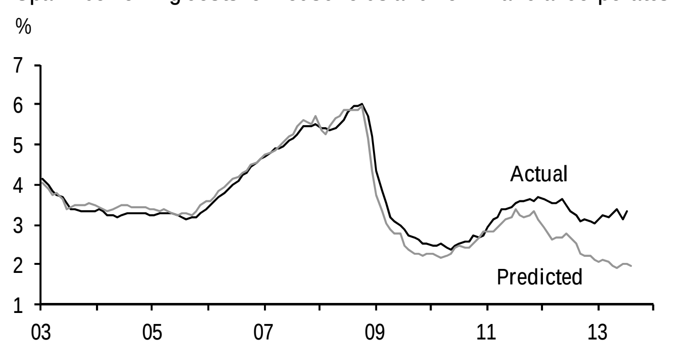
The AQR is an exercise in harmonizing definitions of forbearance and non-performing exposures (see "The Tip Of The Iceberg," Axel Finsterbusch, Roberto Henriques, and Alan Bowe, Europe Credit Research, July 24, 2013). To the extent that banks have to recognize additional non-performing loans, they will have to provision more. In the first instance, provisioning is a charge on a bank's income. Of course it also gets reflected on a bank's balance sheet. We argued earlier this year that the increased pressure to provision more in Italy and Spain over the past two years is a key reason why lending rates to households and non-financial corporates have remained elevated even as funding costs have fallen. Banks have sought to offset the shock to their income from increased provisioning by widening their margins and limiting the

Italy: borrowing rates for households and non-financial corporates



Source: Reuters, ECB and J.P. Morgan

Spain: borrowing costs for households and non-financial corporates



Source: Reuters, ECB and J.P. Morgan

Euro area growth framework

%q/q saar	2012	2013E	2014E	Change 2012/11	Change 2013E/12	Change 2014E/13E
Growth potential	1.3	1.3	1.3	0.0	0.0	0.0
Monetary policy	1.6	1.6	1.6	0.4	0.0	0.0
Fiscal policy	-1.7	-0.9	-0.7	-0.7	0.8	0.2
Exchange rate	0.4	-0.6	0.0	0.4	-1.0	0.6
Global growth	-0.2	-0.1	0.0	-0.1	0.1	0.1
Terms of trade	-0.2	0.4	0.5	0.1	0.6	0.1
Inventory	-0.4	0.3	0.2	-0.1	0.7	-0.3
Residual	-1.8	-1.5	-1.4	-1.7	0.2	0.1
Actual GDP	-1.0	0.5	1.5	-1.7	1.5	1.0

Source: J.P Morgan, Eurostat, and European Commission

availability of credit. The existence of a capital backstop does not help to ease these pressures unless provisioning is so great that income becomes very negative.

The stress test is different. This will identify capital shortfalls related to hypothetical shocks to bank balance sheets. The existence of a capital backstop is clearly important to this exercise. Nevertheless, the stress test could also deliver a shock to the real economy even with the existence of a capital backstop. In the first instance, banks will seek to meet increased capital needs themselves, through capital raising, cutting dividends, or selling assets. As they do this, they tend to maintain higher borrowing rates for households and non-financial corporates and tighter lending standards. So the stress test could also act as a drag on the macro economy for a while, even with a well-defined capital backstop in place.

Of course, banks may seek to provision more ahead of the AQR, to limit both the impact of the AQR itself and the subsequent stress test. Depending on the magnitude of this effect, it could adversely impact borrowing costs and bank lending standards ahead of the balance sheet assessment next year.

The macroeconomic impact

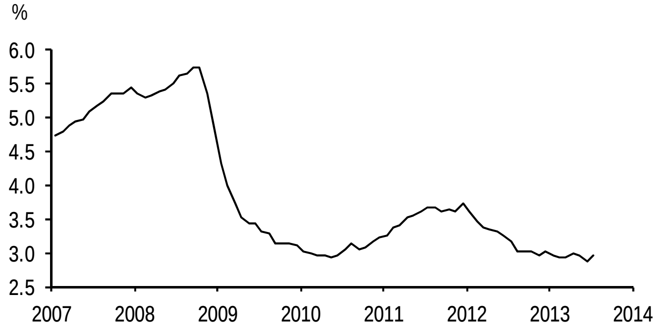
How does all this feed into our macro outlook? We can illustrate this by considering a framework that we use to describe the headwinds and tailwinds affecting the Euro area economy. We do this in the table on the previous page.

We begin with the region's growth potential; this is the pace of growth that the region would experience in the absence of any headwinds or tailwinds. We then identify six forces acting on growth momentum where we have some ability to identify their contributions (monetary policy, fiscal policy, the exchange rate, the global backdrop, the terms of trade, and the inventory cycle). In the past, this has left a residual that measures the gap between all the forces that have been identified and the actual GDP outcomes. For the past few years, we have interpreted this residual as being related to financial stress in the region. In order to use this table as a forecasting framework, a judgment has to made about how this residual will evolve.

The table makes it immediately clear why the region returned to recession in late 2011. There were sizable additional headwinds from fiscal policy and financial stress (as identified in the residual). Indeed, the table suggests that the increase in financial stress was more important in driving the region back into recession than the increase in fiscal tightening. The exit from recession can be explained in this framework by the fading of the fiscal headwind, the support from the terms of trade (from lower commodity prices), and the ending of the corporate inventory drawdown. Importantly, the exit from recession does not rely on a huge decline in the headwind from financial stress. This judgment makes sense. Even though stress in wholesale financial markets has declined dramatically in the past year, the improvement at the retail level has been much more modest.

Looking ahead to next year, we can consider what is needed to ensure that growth moves in line with the average 1.5% annualized rate in our forecast. Some of the supports this year will be less evident next year: the fiscal headwind looks likely to fade a bit more next year but not as much as it did this year; the terms of trade will still be a support next year but broadly

Borrowing rates for households and non-financial corporates



Source: ECB and J.P. Morgan

Bank lending standards for households and NFCs

Source: ECB and J.P. Morgan

of the same magnitude as this year; and the inventory cycle is not expected to be making much of a contribution to growth. But, on the other hand, the exchange rate drag is expected to end. As the table makes clear, to fully meet our growth expectation for next year, the headwind from financial stress (the residual) needs to ease a bit more, but not by much. Essentially, our forecast assumes that the healing of the transmission mechanism is a very slow process. Importantly, we are assuming that the approaching AQR and stress test do not add more of a headwind. If they do, then growth will not improve next year in the way that we currently expect.

We can track this process by monitoring the ECB data on borrowing rates for households and non-financial corporates, published on a monthly basis, and the ECB bank lending survey, published on a quarterly basis. The pace of healing of the transmission mechanism will be evident in how quickly borrowing rates fall and lending standards ease. One way of interpreting our growth forecast is that we are not expecting much movement in either direction. But, if borrowing rates fall and bank lending standards ease, upside risks around our central projection would emerge. On the other hand, if borrowing rates rise and bank lending standards tighten, then downside risks around our central projection would emerge.

Economic Research Note

ECB: the 2014 problem

- **ECB's rate guidance is still under pressure**
- **Hugely different ECB reaction functions are being estimated, with some predicting a rate hike by mid-2014**
- **This highlights need for greater clarity from the ECB**

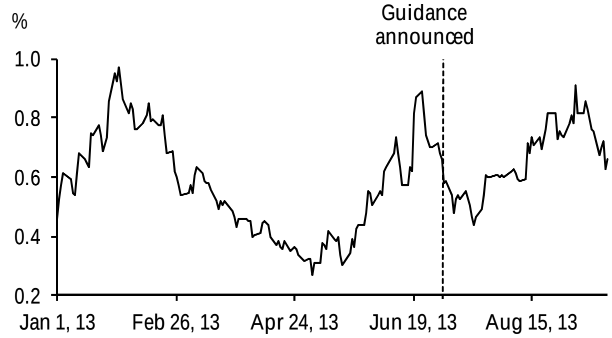
Even by its own admission, the ECB's forward guidance has only been a partial success so far. Market rate expectations have mostly been above the level in early July when the guidance was first announced. And the moderation in forward interest rates observed over the past two weeks is arguably due to more mixed growth news, which should prove temporary, to expectations of a new liquidity injection by the ECB, and to the Fed's decision to not taper its asset purchases, rather than due to the ECB's guidance. Although ECB Governing Council members are speaking a lot about forward guidance, they are not providing the clarity that is needed to improve its efficacy, i.e., they are not clarifying that a return to growth will not alter the inflation outlook for a long time. The reason for more clarity can be illustrated in new research by former ECB policymakers, which suggests that the central bank should start raising interest rates by May 2014. While there are some conceptual issues with this research, it illustrates the key issues that the ECB should be addressing.

Mind the gap

In a recent research note ("ECB forward guidance: more clarity needed," *GDW*, August 30, 2013), we argued that the ECB needs to address two issues if it is to make its guidance more credible. First, it must be clearer about its reaction function and explain that its behavior and the inflation process are driven by slower-moving level variables (e.g., the output gap and unemployment), rather than by growth momentum. And, second, it must clarify how it sees these slower-moving level variables evolving as the economy recovers.

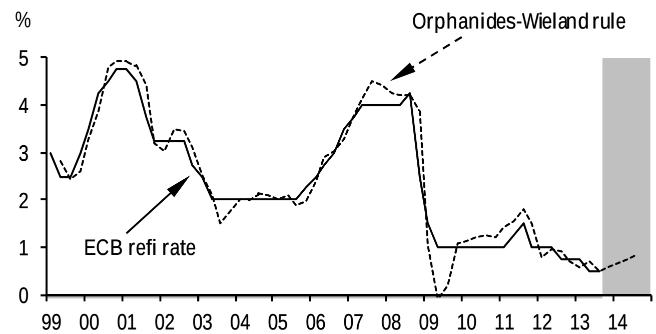
The importance of clarifying this can be illustrated with a recent article published on Vox.[1] This article is based on earlier work by Athanasios Orphanides, who was Governor at the Central Bank of Cyprus and an ECB Governing Council member until mid-2012, and by Volker Wieland, who is a German economist.[2] Wieland has held research and advisory positions at the ECB and is currently one of the German

One-month Eonia rate in October 2015



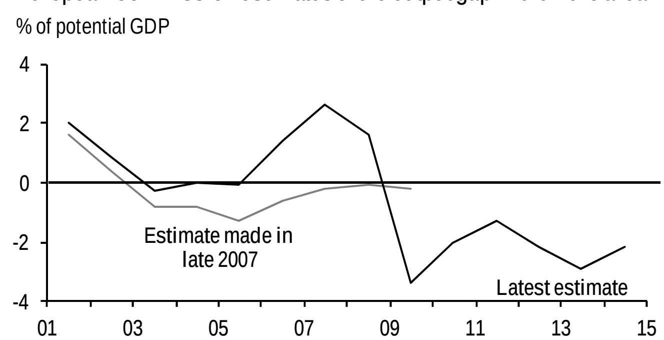
Source: J.P.Morgan

Orphanides-Wieland interest rate rule for the ECB



Source: ECB, J.P.Morgan

European Commission estimates of the output gap in the Euro area



Source: European Commission

government's "Five Wise Men" (i.e., members of the German Economic Council).

In the Vox article, Wieland and his co-author use the Orphanides-Wieland interest rate rule for the ECB. This rule says that the ECB should consider raising its main refinancing rate if inflation is above the target and/or GDP is growing faster than potential GDP. The rule gives both inputs equal weight. Specifically, it is written as:

$$\Delta Refi = 0.5 * (Inflation\ gap) + 0.5 * (Growth\ gap)$$

Two related issues are noteworthy. First, by focusing on the growth gap, the rule says that the ECB should respond to changes in the output gap, rather than to the level of the output

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[1] Bletzinger and Wieland (2013), "Low for how long? Estimating the ECB's "extended period of time,"" available at http://www.voxeu.org/article/low-how-long-estimating-ecb-s-extended-period-time.

[2] Orphanides and Wieland (2013), "Complexity and Monetary Policy," *International Journal of Central Banking*, Vol.9, pp.167-203.

gap (as in the normal Taylor rule). Orphanides and Wieland motivated this by pointing out that the output gap is very hard to measure in real time and that it gets revised substantially, so that a rule based on the change in the gap would be more robust than a rule based on the level. However, the uncertainty around estimates of the output gap relate to a significant degree to uncertainty about estimates of growth potential. This uncertainty is particularly large at present. The European Commission estimates that growth potential has slowed substantially since the start of the crisis, but this judgment could yet be revised. And it is also uncertain to what extent growth potential will recover as the economy expands.

Second, the left-hand side of the interest rate rule has the change of the main refinancing rate. It means that the rule does not actually recommend the level at which the policy interest rate should be set, only whether the rate should be changed from whatever level it happened to be at in the prior quarter. Even if this is sensible in light of the uncertainty in measuring the output gap, it is problematic empirically. In particular, the authors claim that the rule explains the ECB's past behavior well, but this is true only because of the implicit use of a lagged dependent variable (i.e., the actual refi rate during the last quarter), which always brings the model back on track (second chart on first page). Dynamic forecasts show that the model can get seriously off track in terms of the rate level (first chart on this page).

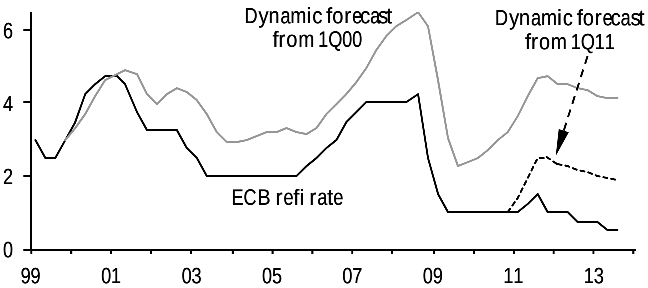
ECB to hike by May 2014?

In the Vox article, the rule is also projected forward. The authors use one-year-ahead inflation and GDP growth projections from the ECB's Survey of Professional Forecasters and compare these to an inflation target of 1.75%[3] and the European Commission's estimate of potential GDP growth. With these inputs, the interest rate rule says that the ECB should begin to raise the main refi rate by May 2014 at the latest. This is mainly because the assumption of very weak potential growth (of just below 0.5%oya) creates significant upward pressure on interest rates. This offsets the downward pressure that comes from inflation running below the target next year. It is striking that the authors reject using the level of the output gap in their interest rate rule, but then passively accept the European Commission's very weak estimate of growth potential, which is a big part of the output gap uncertainty.

Raising rates by the middle of next year is clearly not what ECB president Draghi has in mind. Given the level of forward interest rates in markets in recent weeks, we think Draghi is implicitly referring to an "extended period" that exceeds two years when he describes market pricing as "unwarranted."

Dynamic forecasts using the Orphanides-Wieland rule

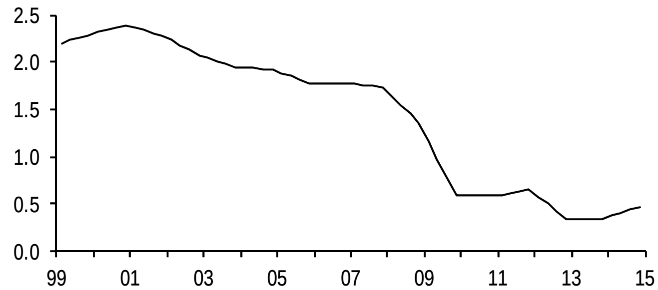
%, dynamic forecast uses model predicted refi rate as starting point for next quarter



Source: ECB, J.P.Morgan

European Commission estimate of Euro area growth potential

%oya, linear interpolation between annual estimates



Source: European Commission, J.P.Morgan

To give credible forward guidance, we believe the ECB needs to clarify that its reaction function is based on the level of the output gap, rather than its change. Our own modeling of the ECB's reaction function suggests that the ECB does in fact respond to the level of slack, and to core inflation. And, in this way, it is possible to very closely explain the level at which the ECB has set its policy interest rate in the past. This can be done without having to resort to a lagged dependent variable. And it can be done by using a measure of slack that is not prone to revision, namely the European Commission's measure of capacity utilization in manufacturing.

The ECB does mention such level variables as justifying its forward guidance. For example, at the last ECB meeting, Draghi said that "several other governors observed that the recovery was still 'too green'...: slack is still wide, weak credit, weak monetary aggregates, inflation is subdued in the medium-term, unemployment is still high." But, even this dovish camp on the Governing Council mixes level variables with variables that relate more to growth momentum. And, in our view, it is important for the ECB to not only clarify this but to also explain how slack is likely to evolve as the economy recovers. This is because, even in our own reaction function, rate hikes are predicted for next year if very depressed assumptions are made about growth potential.

3 They actually estimate a band using an inflation target of 1.5%oya for the lower end of the band and an inflation target of 2.0%oya for the upper end of the band.

Economic Research Note

Turkey: pricing rather than funding risk

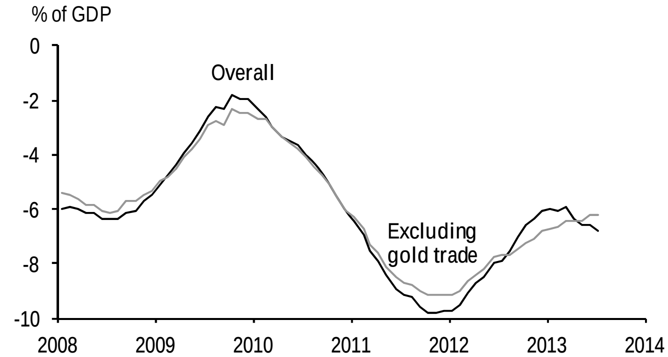
- **Turkey's external financing needs stay high despite improved price competitiveness**
- **Turkey is likely to cover its financing requirements albeit at a higher price**
- **The low level of reserves prevents the CBRT from direct interventions in a sustained way**

Turkish financial assets and especially the lira have been under pressure for some time. Despite the sharp price adjustment seen so far, we see potential for more weakness. Idiosyncratic risks such as the increase in political turbulence and the complicated and unorthodox policy mix of the CBRT were some of the factors hurting the investor appetite for Turkey. However, the real cause of concern has been Turkey's high external deficit and its dependence on capital inflows. True, the sharp lira weakness has improved the country's price competitiveness, and higher bank lending rates should lead to weaker domestic demand and hence lower imports. However, Turkey's current account deficit will still likely be in the range of 6.5%-7.0% of GDP and the economy will remain vulnerable to shifts in global risk appetite. Turkish banks and corporates have never faced any major difficulty in rolling over their debt obligations since fiscal performance remains strong and sovereign debt is quite small. Hence, Turkey has a pricing rather than a funding problem, in our view. Barring a deep and prolonged EM sell-off in global markets, Turkey will be able to finance its external deficit comfortably albeit at a higher cost.

Turkey's 12-month trailing current account deficit widened to 6.8% of GDP from 6.0% in the first eight months of the year. However, this widening was purely due to the deterioration in gold trade. The foreign trade data have been distorted by this anomalous gold export trend. Turkey's gold exports to Iran increased significantly in 2012 as Iranians invested more in gold and gold was used as a medium of payment in trade with Iran. This rise in gold exports led to a fall in gold inventories. This year, however, due to tighter international scrutiny, gold exports to Iran came down sharply. Turkish companies presumably used the recent fall in gold prices as an opportunity to replenish their inventories. Turkey's headline exports rose only 1.3%oya, ytd and imports rose 7.7 over the same period. Excluding gold trade, however, the 7.3%oya, ytd growth in exports compared favorably with the 3.8% increase in imports.

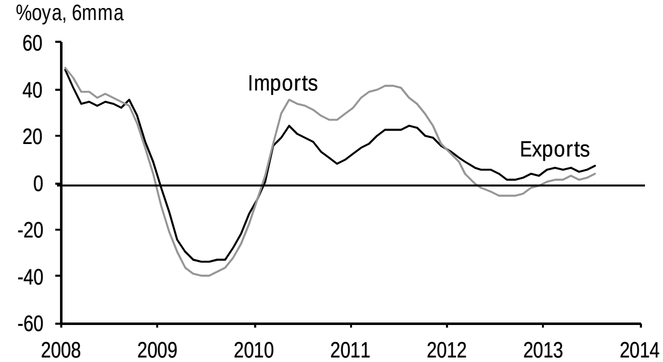
In fact, exports have been growing faster than imports since the beginning of 2012, and we expect this trend to continue as

12-month trailing CAD



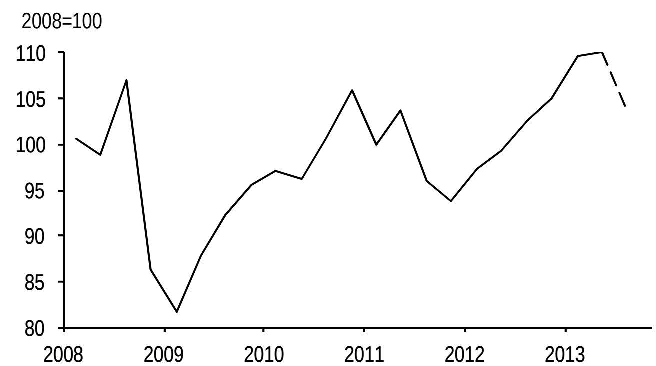
Source: CBRT

Export and import growth



Source: Turkstat

US$-based labor cost index



Source: Turkstat

high bank lending rates and weaker domestic sentiment translate into weaker domestic demand as the currency weakness improves Turkey's price competitiveness. Turkey's labor costs have been rising rapidly for the last two years. Following the sharp lira weakening, however, the labor cost index likely fell to where it was two to three years ago. Also the economic recovery in Europe should support export performance (Europe is still Turkey's main export market). Finally, strong tourism data suggest that the impact of street protests on tourist arrivals has been quite modest. In short, we the risks to our full-year CAD forecast of US$57.7 billion (6.9% of GDP) are skewed to the downside.

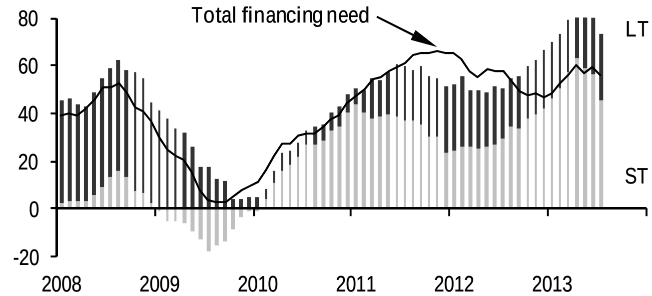
However, Turkey's external borrowing needs will still be quite high. Furthermore, FDI inflows have been weak and the country has become increasingly dependent on short-term inflows in financing this deficit. From 2008-2010, long-term capital inflows (FDI, long-term net credit by banking and real sectors, and bonds issued by banks and the Treasury) were the main financing tools while short-term flows (portfolio flows, short-term net credit by banking, and real sectors and bank deposits) were either small or negative (first chart). This trend has reversed since then. In fact, approximately two-thirds of capital inflows during that time have been short term. Turkey needs to attract FDI in order to make its external financing more sustainable and to continue creating jobs as domestic savings remain low. However, the political and policy uncertainty at home and the volatility in global markets do not provide many reasons to be optimistic on this front.

Another key issue surrounding LT capital flows is the ease with which Turkish businesses find new LT credit from abroad. It is encouraging to see that banks and corporates have faced no difficulty in rolling over their debt obligations in recent years (second chart). Even after the Lehman crisis, the rollover ratio of corporates did not fall below 70%. The strength of the Turkish banking system and close relations with European banks have been instrumental in the success of the Turkish banks in finding financing even in times of weak global sentiment. As for corporates, the ease with which the Turkish corporate sector continues borrowing from abroad supports the view that a significant number of these loans are cash-collateralized and thus could be rolled over easily even in adverse market conditions. The rollover ratio of long-term borrowing was 170% for corporates and 377% for banks in July. This implies that there is again no problem with LT borrowing. Banks also attracted US$11 billion in the form of deposits in the first eight months of the year. This trend will likely continue following the recent rise in bank deposit rates.

Continued portfolio outflows constitute a key challenge for Turkey, in our view. Since end-May, Turkey saw outflows of US$2.2 billion and US$3.3 billion from equity and bond markets, respectively. As a result, the share of foreign investors in the Turkish bond market declined to 25% from above 28% during this period. Foreign participation was already quite low and has fallen even further in the last three months. However, there is potential for further outflows given that foreign investors still have a total of US$50 billion invested in the Turkish bond market. In order to avoid any further portfolio outflows and to encourage inflows, Turkey needs to pay higher yields and make sure the currency is more stable.

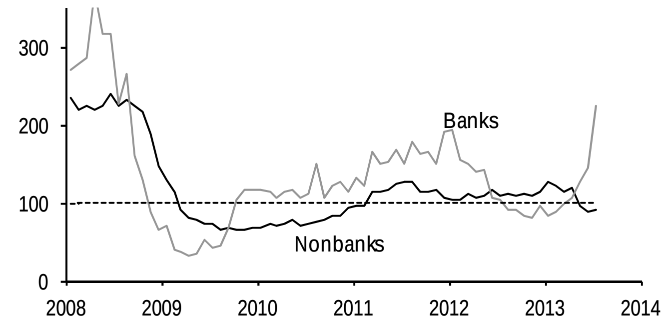
Finally, the low level of the CBRT's FX reserves is seen as a major weakness of the Turkish economy. The CBRT's net FX reserves stand at US$47 billion, which is indeed extremely low.

Sources of external financing
US$ billion, 12-month cumulative



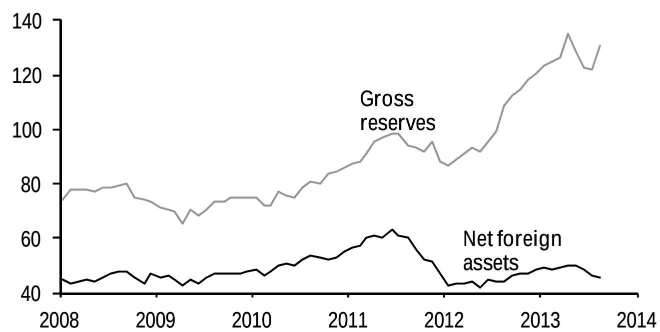
Source: CBRT

Rollover ratio of banks and nonbanks
%, 6mma



Source: CBRT

CBRT's gross reserves and net foreign assets
US$ bn



Source: CBRT

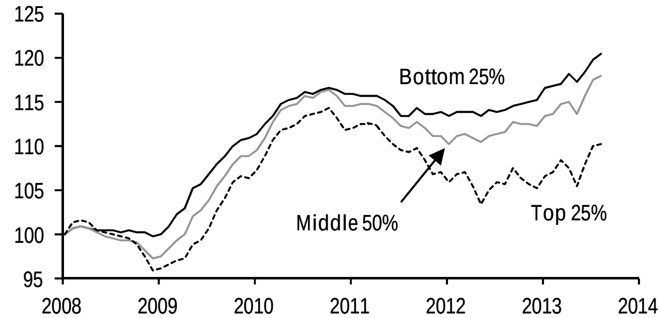
This is the reason why the CBRT cannot support the lira through direct FX interventions in a sustained way. However, the Bank's gross reserves are at a somewhat more respectable level of US$130 billion. The FX required reserves and the FX reserves held in relation to the reserve option mechanism (ROM) constitute the bulk of the difference between gross and net reserves. Banks could easily use the ROM facility less and use the excess FX in covering their financing needs. Similarly, the CBRT could cut the RRR on FX liabilities or the ROCs to provide liquidity to the banking system. Thus, the FX liquidity that can be used to cover external needs is higher than what net reserves suggest. This supports our view that the rollover risks are contained while pricing risks remain high in Turkey.

Aussie first home buyers absent in housing upswing

- **Dwelling prices have trended higher this year, up 3.6% since January**
- **First home buyer activity has ebbed further, slipping to just 14.7% of total loans**
- **First home buyers are at risk of being priced out of the market as investor activity surges**
- **Affordability is now becoming an issue for the most price-sensitive home buyers**

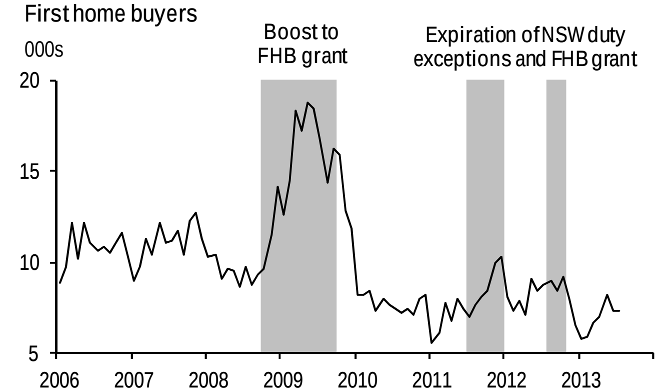
Australia's residential housing market has been one of the better-performing sectors of the economy in 2013, benefiting from the significant easing already delivered by the RBA in the current cycle. Dwelling prices, in particular, have been impressive this year, with broad-based gains across all price brackets (first chart). This uptick in prices has largely been underpinned by surging investor activity, as falling interest rates improve loan serviceability and cause yields in cash-like asset classes to fall. In contrast, there has been a significant pullback in the proportion of first home buyers (FHBs) entering the housing market, with new loans currently held by this buyer group accounting for just 14.7% of the total and tracking close to multi-decade lows. With FHBs already under-represented in the housing market, it appears these buyers are now at risk of being increasingly priced out as investors drive prices higher.

Dwelling price brackets
Index, 2008 = 100



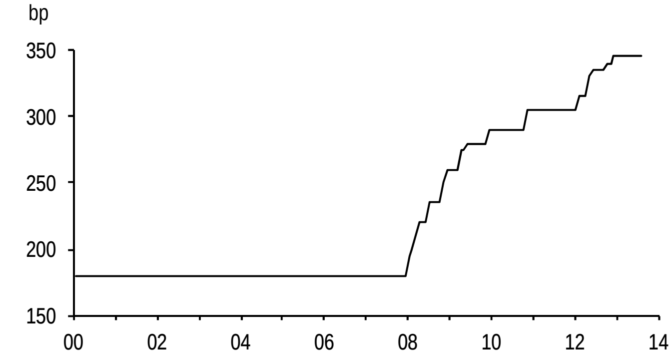
Source: RP Data

First home buyers
000s



Source: ABS, NSW government

Spread between cash rate and the average standard variable rate
bp



Source: ABS

Where are the first home buyers?

The RBA has eased policy by 225bp since November 2011, trimming the cash rate to a post-independence low of 2.5%. This appears to have been insufficient to lure FHBs back to the housing market, however, with the proportion of new loans drawn by this group falling substantially throughout the easing cycle. In December 2011, FHBs comprised roughly 21% of new loan commitments; however, since then, these buyers have pulled back and now account for a lowly 14.7% of the total. The initial decline, commencing in 2012, was triggered by the expiration of various state-level housing stimulus programs that eliminated expensive transfer taxes and provided generous grants for FHBs.[1] Admittedly, the magnitude of this slump was accentuated by a run-up in activity prior to expiration as buyers pulled forward purchases to capitalize on these offers. Even so, the volume of new loans to FHBs has since fallen well below the decade average, suggesting that these declines are more than just an activity hangover phenomenon. There are still government-funded stimulus programs on offer, though most of these are geared toward the purchase and construction of new dwellings in a bid to revive activity across the struggling construction sector.

In addition, we expect that the widening spread between the official cash rate and the standard variable rate may have had a more significant impact on FHBs than was felt by other

[1] In New South Wales, the First Home Plus Scheme was replaced by the First Home – New Home Scheme on 1 January 2012, which abolished stamp duty exemptions for FHBs purchasing established dwellings. The AUD$7,000 FHB grant for established dwellings also expired on 30 September 2012, while grants for new homes and vacant land were lifted to AUD$15,000. Similar stimulus programs funded by the Queensland State Government also expired in October 2012.

buyer groups. This spread was remarkably stable prior to 2008, with fluctuations in the cash rate simultaneously filtering through to borrowing rates (third chart previous page). This spread has blown out over the past five years, however, as lenders became more reluctant to pass through rate cuts as margins came under pressure. We speculate that the decoupling that has occurred between these rates has had a greater impact on FHBs, who are typically more income-constrained and sensitive to interest rate fluctuations than other owner-occupiers or investors.

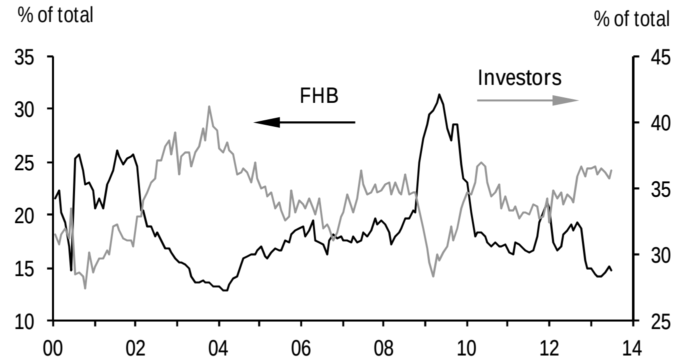
A lesser issue, though still important for FHBs, is that banks have become increasingly cautious in their lending behavior since 2008, highlighted by sharp declines in low doc lending growth. Although this doesn't suggest that banks are unwilling to lend to first home buyers, it does imply that requirements around loan serviceability have become increasingly stringent. Given the backdrop of rising unemployment, soft economic activity and tepid wage growth, it appears the next obstacle for first home buyers is price-related, as affordability metrics become increasingly unfavorable for this price- and interest-rate-sensitive group.

Affordability becoming an issue

As we have previously pointed out (see "Aussie housing and the real economy: surge or diverge," *GDW*, September 6), the recent pickup across the housing sector has been underpinned by investors rotating their portfolios toward the housing sector. Considering that first home buyers are typically highly sensitive to price changes (first chart), the current investor-led price surge is likely creating affordability issues. This scenario is not uncommon, with these buyer groups historically maintaining an inverse relationship, the residual being other owner-occupiers. Intuitively, such a correlation makes sense, with investor participation conditional on the ability of these properties to be rented out, the burden of which usually falls on potential first home buyers.

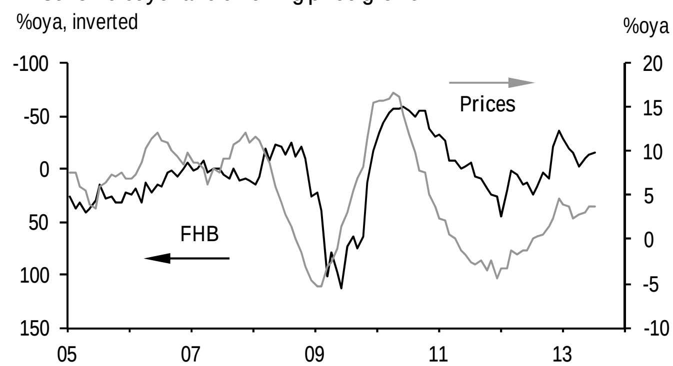
As shown in the second chart, there is a clear negative relationship between first home buyer activity and house price growth, with price increases (decreases) typically resulting in a lagged decline (increase) in the run rate of FHB activity. This was particularly pronounced in late 2008, when the sharp downturn in housing prices (coupled with a falling cash rate and stimulus payments) was followed by a subsequent surge in FHB activity, as both outright affordability and loan serviceability improved. The following rebound in prices was, unsurprisingly, accompanied by a decline in activity, presumably as FHBs were increasingly priced out of the market. Although there are obviously other factors influencing activity, including heightened economic uncertainty, the introduction (and elimination) of government stimulus programs, and a wider cash rate to standard variable rate (SVR) spread, the inverse relationship between these variables has remained, supporting the theory that rising prices are likely to be a major obstacle for first home buyers over the coming quarters.

First home buyer and investor activity



Source: ABS

First home buyer and dwelling price growth



Source: ABS

External price pressures

In 2009, as a response to the global financial crisis, the Rudd government relaxed the regulations governing foreign ownership of residential property. In particular, these rule changes allowed offshore investors to buy established dwellings (of any value) with no formal approval required from the Foreign Investment Review Board (FIRB). Following speculation that offshore activity was driving up prices, the regulations were tightened in April 2010, the most significant step seeing temporary visa holders once again required to seek approval from the FIRB when purchasing Australian residential property. Despite this more rigorous approval process, the number of temporary visa holders purchasing domestic property has surged post-2009, with the FIRB approving 9,768 applications in FY2012, well above the pre-crisis average of 3,741. While, admittedly, these numbers are small in comparison to total housing turnover, this still suggests offshore demand may be bidding prices higher.

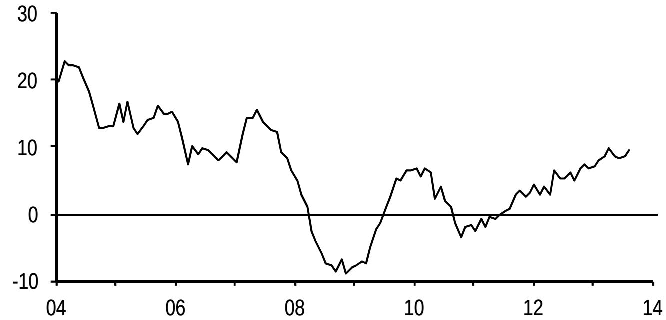
Economic Research Note

Adjusting for interplay between the RBNZ's policy tools

- **RBNZ announced LVR restrictions on new mortgage lending in August**
- **Governor Wheeler expects the measures to provide "greater flexibility" on rates, with a 30bp impact on the OCR path flagged in the September MPS**
- **This is a greater overlap between the policy settings than we had assumed, so we push out the timing of the first rate hike to 2Q14**

REINZ house price index

%oya



Source: RBNZ.

Our forecasts for above-trend growth in 2013-14 in New Zealand are tracking. The data are showing domestic demand strength to be broad-based, with only short-term supply-side drags in the agriculture sector holding back GDP growth in 2Q. Greater uncertainty surrounds the mapping between the real economy and the monetary policy response, however. The RBNZ's most recent foray into macroprudential policy, the announcement of loan to value ratio (LVR) "speed limits" in August, reflects officials' frequently stated concern with high-LVR mortgage lending this year. However, we have been surprised by the extent to which the effects of this decision are assumed to spill over into monetary policy space. Here we review our monetary policy outlook for that reason.

Fundamental concerns

The RBNZ has been busy on the macroprudential front this year. The flurry of activity reflected the fact that, even before examining the case for deployment, there were several wrinkles in the institutional framework that needed to be ironed out. The banks were briefed on how such interventions would work in practice; definitions, such as what legally constitutes an act of "lending," were tightened; and an MoU enshrining the RBNZ's powers in this space was signed. Throughout the process, the concerns of the RBNZ's Financial Stability Department regarding the skew of residential mortgage lending to high LVR (>80%) borrowers, on an already "over-valued" housing stock, became increasingly clear. When it came to deployment, the first step was to boost capital adequacy in terms of buffers held against such lending. But the discussion evolved around midyear toward directly restricting high-LVR lending.

A question of semantics

While the macroprudential agenda was advancing, the mantra from RBNZ officials was that these tools were complements to, not substitutes for, conventional monetary policy. Assistant Governor McDermott's speech in March noted that such measures "will generally support and complement our efforts to stabilize inflation with conventional monetary policy," and Deputy Governor Grant Spencer in April stated that macroprudential policy "is not seen as a replacement for monetary policy." So officials may not have felt comfortable raising interest rates to target housing, given the low level of inflation, but our reading was that deploying macroprudential policy would not be assumed to explicitly take pressure off monetary policy, in terms of the broader price stability objective. In the same way that wanting a left shoe makes one no less likely, and probably more likely, to want a right shoe, if the two policy tools are complements, we assumed that deployment of macroprudential tools would not depress the OCR path materially.

There were also fundamental reasons to think that the two policy arms could be deployed independently. The focus in the first half of the year was on raising the level of regulatory capital required to be held against high-LVR lending, and RBNZ policy documents noted at the time that capital adequacy measures were usually met by the banks raising that capital, rather than shrinking their balance sheets. Credit supply effects should therefore be minimal. As the discussion evolved toward LVR restrictions, the focus was on the composition, rather than the quantum, of credit growth, which remained low. It seemed that the parameters on LVR restrictions would be set with an eye to only crimping the undesirable activity, and so affect the composition of credit growth, without necessarily hitting aggregate credit supply (for example, the restrictions, and the banks' pricing decisions that followed, might see more loans written at lower LVRs).

More interplay, and a messier message

Recent developments show our prior interpretation to be incorrect. RBNZ Governor Wheeler stated upon the announcement of LVR restrictions that this would "provide the Bank with greater flexibility in considering the timing and magnitude of any future increases in the OCR." Also in last week's September Monetary Policy Statement (MPS), it is stated that LVR restrictions are assumed to take 30bp off the bank bill rate projections (and implicitly the OCR path). So while the case for macroprudential policy may well have been made on its own merits, and not couched as a decision relative to the alternative of a rate hike, ultimately, deployment is being assumed to have material monetary policy-like effects.

The conceptual muddiness around complements and substitutes also guided expectations around how burdensome the parameters on LVR restrictions would be, and in the event, these came out more hawkish than we expected. From October 1, new residential mortgage loans with LVRs above 80% will be restricted to 10% of new lending, having previously run at 30% (normal is around 20%). A sharper reduction increases the likelihood of broader credit supply adjustment, and therefore has monetary policy-like effects. The assumption in the MPS is that there will be a transmission to credit, house prices, and consumption growth, which is equivalent to a 30bp increase in the OCR. Whether or not the 30bp calibration is correct will have a bearing on policy later, but for now, the impact is to delay the start of the hiking cycle.

Recalibrating policy for 2014

Having previously expected the RBNZ to first raise the OCR in December this year, we now push this out to 2Q14. The LVR restrictions commence on October 1, with a phase-in period of six months. There is clear evidence that banks are managing to the new requirements already, though, given they have a significant backlog of non-compliant pre-approvals under the old regime that will need to be offset over the phase-in period. Mortgage rates are beginning to split along the 80% LVR boundary, too, with lenders requiring premia of 20-50bp for high LVR loans. Also the 20-30bp rise in new customer mortgage rates on fixed loans over the last couple of months is moderating loan growth further, removing the urgency for a complementary near-term OCR hike.

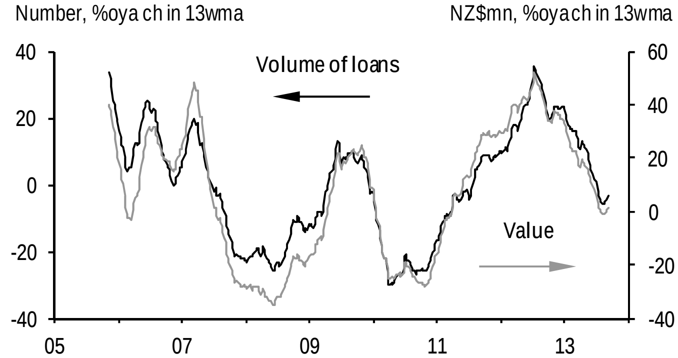
Further, it seems that RBNZ officials will allow time to accumulate evidence on the effect of LVR limits. Governor Wheeler stated at the MPS briefing that the Bank will provide an assessment of how LVR restrictions are working at the Financial Stability Review (FSR), and we expect OCR hikes to be on the backburner until officials are close to declaring their judgment on that. The next FSR is in November, which clearly is too soon, with the next review after that being on May 14. By that time, the impact of LVR restrictions on credit supply should be known, and the case for a broader tightening of monetary conditions on the basis of domestic demand activity and inflation risks should be clear.

Moving parts to the RBNZ's forecasts

Our prior forecast was for 50bp of tightening through to 4Q14. Delayed lift-off doesn't change this dramatically, since the LVR limit parameters ultimately have turned out to be more burdensome than we expected. We therefore add only an extra 25bp of tightening, taking the total to 75bp through to 4Q14, from 50bp previously.

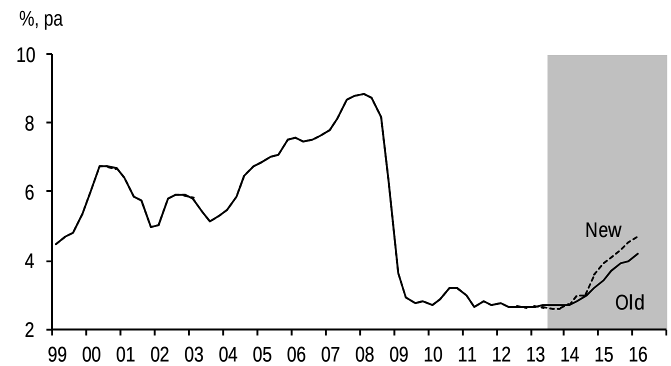
Benchmarking this against the RBNZ's guidance is messy. Even with the depressing effect of LVR limits, the bank bill projections were steepened in the last MPS, implying 100bp of hikes to 4Q14, still more than we are forecasting. The LVR limit effect presumably was marked near term, but intuitively that shock to the OCR level should last as long as the limits are in place. The uplift in the bank bill path therefore incorporates even stronger positive underlying forces. The growth forecasts didn't change, so the major catalyst seems to be the downgrade of the TWI forecasts, which now sit around 4% below spot. In our view, high LVR lending has not been a major driver of domestic demand. Debt servicing costs are low, deleveraging headwinds are fading, and growth is well-supported by earthquake reconstruction. With LVR limits assumed to influence both the amount and the timing of rate hikes, the Bank has doubled-down on its view that this tool can have monetary policy-like effects on consumption. We do not have a strong view on whether the 30bp estimate is right, but note that if the RBNZ does get caught behind the curve, there are upside risks to its currency forecasts, which would moderate the pressure on its bank bill projections.

New Zealand: weekly new mortgage lending



Source: RBNZ

RBNZ 90-day bill forecasts (Sep vs Jun MPS)



Source: RBNZ

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Economic Research Note

Emerging Asia riding on the coattails of China's tourists

- **China's rising discretionary incomes and relaxation of travel regulations leading to rise in outbound tourism…**
- **…Leading to solid increase in China's tourism-related service outflows and inflows for destination countries**
- **Main beneficiaries so far have been Hong Kong, Korea, Taiwan, and Thailand**

China's domestic demand is generally linked to the rest of the world through two major channels. The best recognized in the past decade has been China's demand for goods, especially commodity imports, which is closely tied to its fixed investment cycle. Another increasingly important channel is the spending of Chinese tourists abroad, which reflects the general rise in Chinese consumers' spending power. Looking ahead, while China's commodity demand growth will likely moderate in the medium term (see "China's commodity demand tracks the economic cycle," *GDW*, September 6), the second channel of Chinese tourists' spending abroad will likely have significantly room to grow.

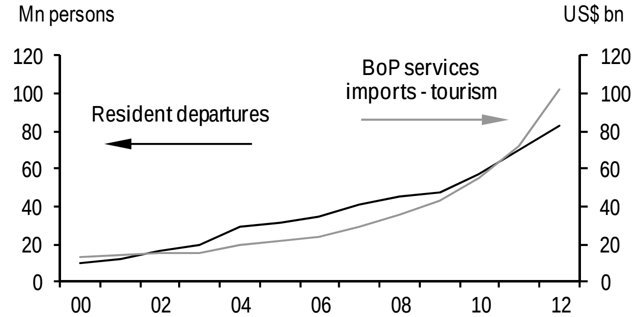
Already, there has been a clear acceleration in Chinese tourist arrivals across the region, with Hong Kong, Korea, Taiwan, and Thailand seeing especially explosive growth in the past three years. Mainland tourists now account for around a third of total tourists in these countries from less than 15% in 2010. These improving flows are also reflected in a rise in tourism receipts in the balance of payments. Domestic employment, incomes, and consumption should also see a lift in beneficiary countries, but this development is beyond the scope of this note. Indeed, this impact is captured in the relatively high output multiplier of 1.6 in Singapore's hospitality industry, based on the 2007 input/output tables.

Sharp rise in China's tourism spending

An increasing number of Chinese tourists have been going abroad in recent years. For the decade ending 2009, resident departures abroad expanded at a steady annual pace of 17.8%. The pace of growth picked up after 2009, rising at an average 20.4% annual pace by 2012, as many countries relaxed travel requirements for Chinese tourists after the financial crisis and the steady appreciation of the renminbi helped to strengthen Chinese tourists' spending power.

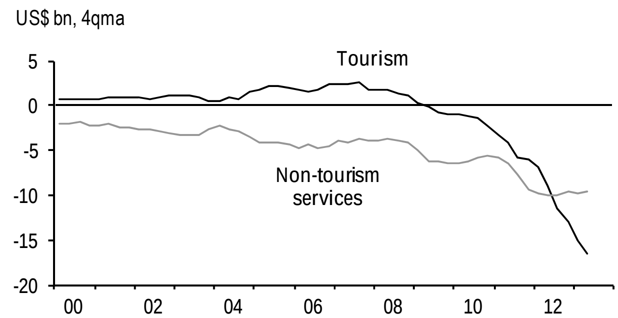
Not surprisingly, China's spending on tourism services abroad from the balance of payments account accelerated to a remarkable 32.4% annual rate in the last three years,

China: resident departures and BoP tourism services imports



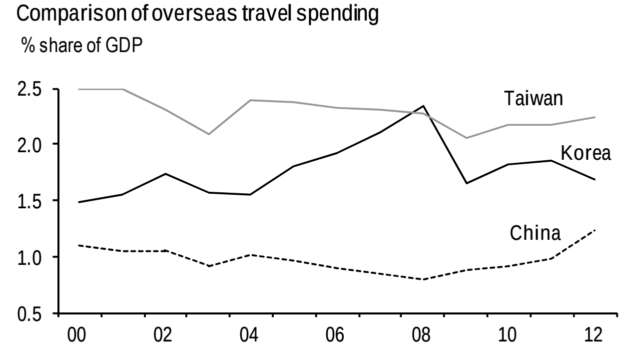
Source: China NBS and SAFE

China current account service balance breakdown



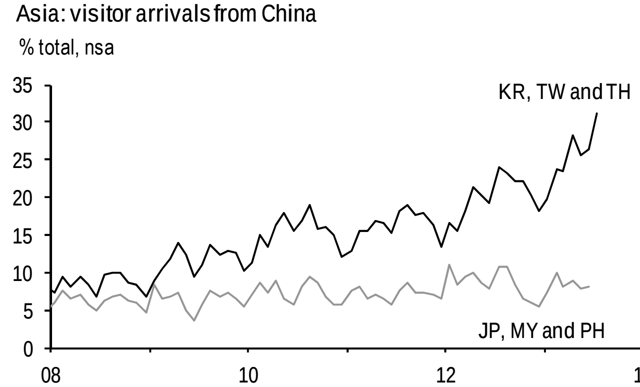
Source: NBS

Comparison of overseas travel spending



Source: China NBS, SAFE, BoK, and Taiwan DGBAS

Asia: visitor arrivals from China



Source: CEIC and J.P.Morgan

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compared to 14.9% growth during the decade prior to the financial crisis (first chart). From a macro perspective, this increase in Chinese tourists' overseas spending has had a notable impact on China's current account. While the current account surplus narrowed significantly from US$420.6 billion in 2008 to US$193.1 billion in 2012, the goods surplus narrowed only moderately (with a decline of US$39.1 billion, or 10.8%, during the same period), while the service account deficit expanded more than sixfold (by US$77.9 billion), led by the tourism sector (which turned from a modest surplus to a notable deficit). Such sharp expansion of the tourism deficit in turn reflects the increasing ability and willingness to spend by Chinese consumers, as well as the gradual rise in the importance of the tertiary/service industries in the Chinese economy (the share of tertiary industry in overall GDP rose from 40.9% in 2006 to 44.6% in 2012). While overseas tourism spending has risen steadily as a share of China's GDP in recent years, there will likely be further scope to expand judging from its regional peers (third chart previous page).

In the near term, however, the introduction on October 1of a new travel law in China that forbids travel agencies from arranging shopping trips could slow tourism departures in the near term and also raise travel costs. This should have limited impact over the medium term as Chinese incomes rise.

Some winning more than others

Hong Kong experienced a tourism surge from the mainland starting in 2003, with gradual opening for mainland individual visitors. Aside from Hong Kong, since 2009 the region has generally seen an increase in tourist arrivals from China. Korea, Taiwan, and Thailand have seen an especially strong rise in the share of tourist arrivals from China in the past three years, which also coincides with a relaxation of travel restrictions (fourth chart previous page and table). While the other countries in the region have also seen a strong rise in Chinese arrivals, the pace has been less dramatic (first chart). The one country that actually has seen a reduction in the share of arrivals from China is Japan, with the share declining to 10.8% in 1H13 from a peak of 18.2% in 1H12, likely due to rising diplomatic tensions.

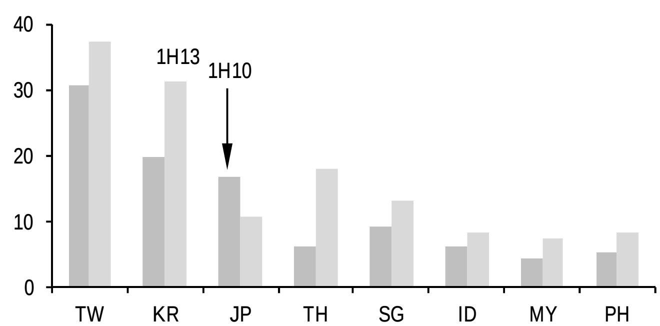
One impact from rising tourism arrivals has been the rise in tourism receipts in the balance of payments. This is most apparent in Thailand, where tourism receipts surged to US$11.8 billion in 1Q13 from US$6.0 billion in 1Q10 (fourth chart). While arrivals have also risen in Korea and Taiwan, outbound tourism has masked the impact of inbound tourism receipts in the BoP. Nonetheless, the rise in tourist arrivals has helped reduce the services deficit in both of these countries. Tourism has also exerted a positive impact on overall output, as reflected in the relatively high output multiplier; in the case of Singapore we estimate an output multiplier of 1.58 for unit demand for hotel and restaurant services based on the 2007 I/O data.

Asia: tourist arrivals
Mn, nsa

	1H10	2H10	1H11	2H11	1H12	2H12	1H13	Chg[1]
Hong Kong	16.9	19.2	19.3	22.6	22.3	26.3	25.4	15.6
China	10.5	12.2	12.7	15.4	15.6	19.3	18.8	23.3
Non-China	6.4	7.0	6.6	7.2	6.7	7.0	6.6	0.6
Thailand	7.6	8.4	9.8	9.5	10.6	11.7	12.7	18.9
China	0.5	0.7	0.9	0.8	1.2	1.6	2.3	67.1
Non-China	7.1	7.7	8.9	8.6	9.5	10.1	10.5	14.2
Malaysia	11.9	12.7	11.4	13.4	11.6	13.4	12.6	2.3
China	0.5	0.6	0.6	0.7	0.8	0.8	0.9	19.3
Non-China	11.4	12.1	10.8	12.7	10.9	12.6	11.6	1.4
Singapore[2]	5.5	6.1	6.4	6.8	7.1	7.3	7.6	11.4
China	0.6	0.6	0.8	0.8	1.0	1.0	n/a	28.9
Non-China	5.0	5.5	5.6	6.0	6.1	6.4	n/a	9.3
Korea	4.2	4.6	4.3	5.5	5.3	5.8	5.5	11.0
China	0.8	1.1	0.9	1.3	1.2	1.6	1.7	27.4
Non-China	3.3	3.6	3.4	4.2	4.1	4.2	3.8	6.3
Japan	4.2	4.4	2.8	3.4	4.0	4.3	5.0	7.4
China	0.7	0.7	0.5	0.6	0.7	0.7	0.5	-0.3
Non-China	3.5	3.7	2.4	2.8	3.3	3.6	4.4	9.2
Indonesia[2]	3.4	3.6	3.6	4.1	3.9	4.2	4.2	7.1
China	0.2	0.2	0.3	0.3	0.3	0.3	n/a	16.3
Non-China	3.1	3.4	3.3	3.7	3.6	3.8	n/a	6.5
Taiwan	2.7	2.8	2.9	3.2	3.6	3.7	3.8	13.1
China	0.8	0.8	0.8	1.0	1.3	1.3	1.4	24.5
Non-China	1.9	2.0	2.0	2.3	2.3	2.4	2.4	8.4
Philippines	1.7	1.8	1.9	2.0	2.1	2.1	2.4	10.4
China	0.1	0.1	0.1	0.1	0.2	0.1	0.2	21.3
Non-China	1.6	1.7	1.8	1.9	2.0	2.0	2.2	9.8

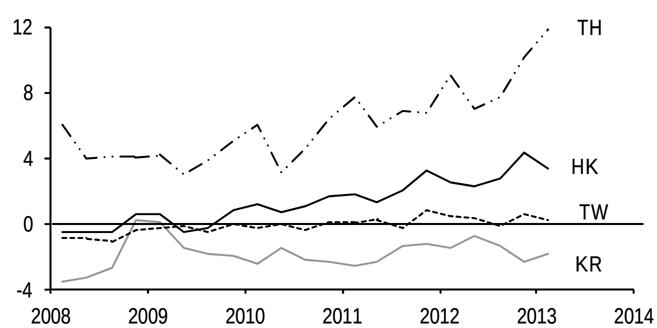
1. Average annual growth rate, 1H13 from 1H10
2. 2H12 from 2H10; Source: CEIC and J.P. Morgan

Asia: China tourist arrivals
% total, ID & SG, 2H12 and 2H09



Source: CEIC and J.P. Morgan

EM Asia: tourism receipts
US$bn, net, nsa



Source: CEIC and J.P. Morgan

Economic Research Note

What lies beneath Thailand's current account deficit?

- **Flip from years of sizable surpluses reflects protracted deterioration in trade balance**
- **Weak exports part of the story, but demand for fuel and gold pushing up imports**
- **Moderation in other CA outflows owes to a surge in regional tourist arrivals**

The lingering dip into deficit has been an unusual feature of Thailand's recent current account data, with the headline balance printing in the red in five of the first seven months of the year. Behind this flip from several years of sizable surpluses, two opposing forces have been at work: a collapse in the trade surplus to almost flat levels, and a notable improvement in the invisibles balance (first chart and table).

Sluggish external demand has been partly responsible for Thailand's narrowing trade surplus. In large part, weak export growth reflects muted demand from China and the G-3, amid signs of structural headwinds facing the Thai electronics sector. But while exports continue to look soft, demand for certain imports—particularly oil and gold—remains sticky, even as domestic activity has slowed through the year. Strength in these imports has widened the oil, gas, and gold deficits considerably; the trade balance outside of these commodities has held up better (second chart).

While the persistent narrowing in the trade surplus is weighing on the current account balance, the deterioration is being offset in part by a rapid improvement in the invisibles balance. Here, a surge in tourist arrivals is pushing the balance of trade in services into surplus for the first time in years.

Soft exports are not the whole story

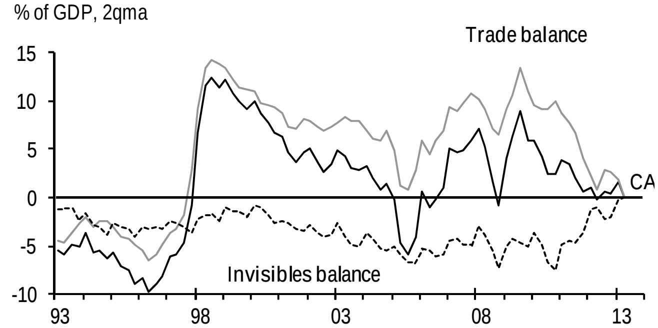
The deterioration in Thailand's trade surplus was triggered by a collapse in exports during the 2011 flooding and persisted amid a subsequent surge in capital goods imports during the post-flood rebuild. However, the prolonged deterioration through 2013 has been striking, reflecting a combination of weak exports and sticky imports. This strength in imports has been largely concentrated in two areas: demand for oil and demand for gold. While the trade balance outside of these commodities has improved on the margin through 2013, both the gold balance and the oil and gas balance have widened notably over the past year or so, largely on account of the persistent rise in imports (second and third charts).

Thailand: current account balance
% of GDP, selected years

	1996	2007	2012	1H13	Chg.[1]
Current account balance	-8.1	6.3	0.1	-1.9	-8.2
Trade balance	-5.2	10.8	1.7	-0.4	-11.1
Exports	30.1	61.1	61.7	56.0	-5.1
Imports	35.3	50.4	60.1	56.4	6.0
Oil balance	-3.0	-7.4	-8.6	-9.2	-1.8
Gold balance	-0.2	0.0	-1.6	-4.3	-4.3
Invisibles balance	-2.9	-4.4	-1.6	-1.5	2.8
Tourism-related	2.7	4.7	7.5	..	2.9
Others	-5.6	-9.1	-9.1	..	0.0

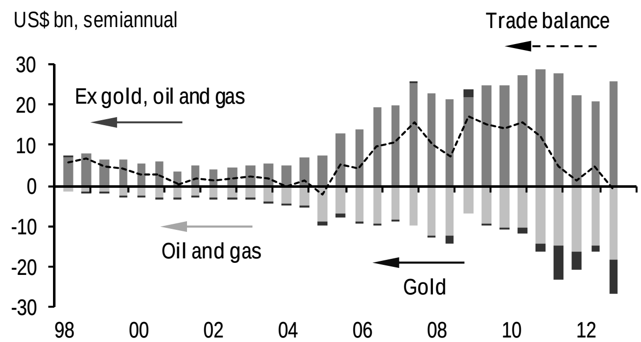
1. %-pt. change, latest since 2007. Oil balance includes gas imports.
Source: Bank of Thailand, IMF, J.P. Morgan

Thailand: current account balance
% of GDP, 2qma



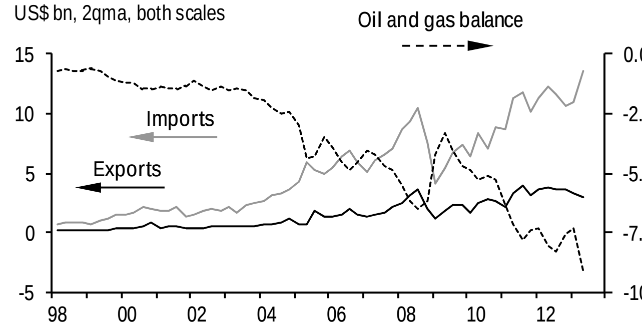
Source: Bank of Thailand, IMF, J.P. Morgan

Thailand: composition of trade balance
US$ bn, semiannual



Source: Bank of Thailand, J.P. Morgan

Thailand: oil and gas trade
US$ bn, 2qma, both scales



Source: Bank of Thailand, J.P. Morgan

The usual suspects: oil and gold imports

Trade in crude oil accounts for the bulk of the deficit in the oil and gas balance. Here, the widening deficit has largely reflected fluctuations in oil prices; volumes of crude imports have been more stable. In contrast, import volumes of fuel excluding crude oil have been strikingly strong. Demand for refined fuel products—including LPG and other petroleum products—surged through 2012 and into 2013, feeding a substantial volumetric increase in these fuel imports. This rise in fuel demand, along with movements in oil prices, saw the oil and gas deficit reach around US$10 billion in 2Q, almost equal to the entire non-commodity trade surplus.

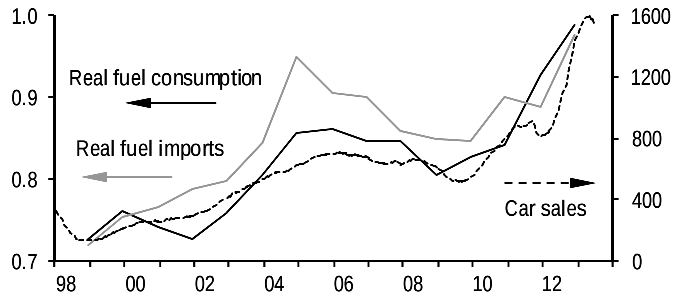
The stickiness of real fuel imports—despite the recent moderation in the domestic economy—is interesting. One factor behind the rise in demand is likely the increase in the stock of cars and other vehicles on Thailand's roads—largely a product of last year's first-car rebate scheme, which led to soaring auto sales (first chart and see: "Thailand: Autos slowing but domestic demand not stalling," *GDW*, March 27). Demand for LPG, for example, has shifted firmly toward the auto sector. Auto-related demand accounted for 22% of all LPG consumption in the year through July, an 8%-pt increase over the share in 2012.

Aside from a rise in fuel demand, imports of gold have also increased rapidly, but the large swings from month to month are more difficult to square. Historically, volumes of gold imports have remained fairly stable, but the surge in nominal imports through 2013 was not due to price movements. One observation here is that the decline in the gold balance has moved in step with larger outflows from the errors and omissions component in the balance of payments (second chart).

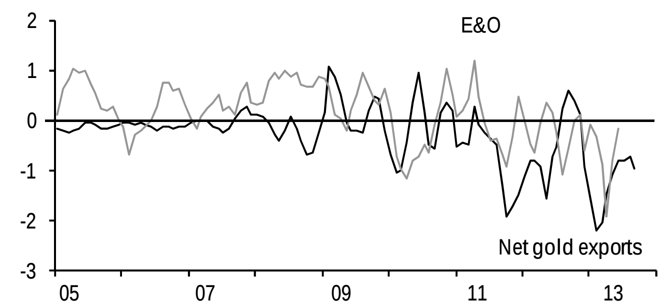
Tourist surge benefits other CA flows

In the absence of a pickup in exports, elevated demand for gold and fuel could continue to depress the trade balance. (The expectation that several domestic refineries will wind down output toward 2015 could also add to the oil import bill, further weighing on the oil and gas balance). On the flip side, a reduction in other outflows on the CA should work to offset the narrowing trade surplus. Net outflows from the invisibles have shrunk considerably over the past year or so, largely as a result of a surge in tourist arrivals.

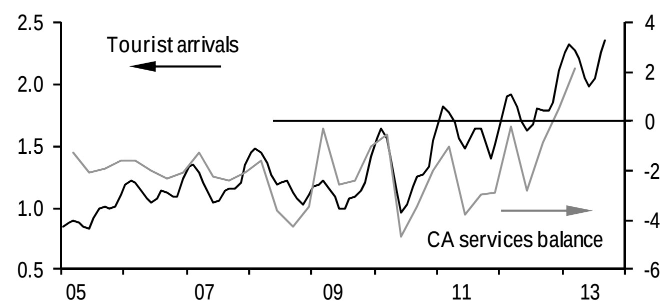
The rise in visitor arrivals has pushed the balance of trade in services into surplus for the first time in years, mostly due to a rapid increase in Asian tourists (third chart). Mainland Chinese arrivals have been particularly strong, up almost five-fold since end-2011 and reaching around half a million per month in August, or 20% of all visitors—an important factor behind the rapid increase in tourism receipts (fourth chart). For more detail see the research note "Emerging Asia riding on the coattails of China's tourists" in this *GDW*.



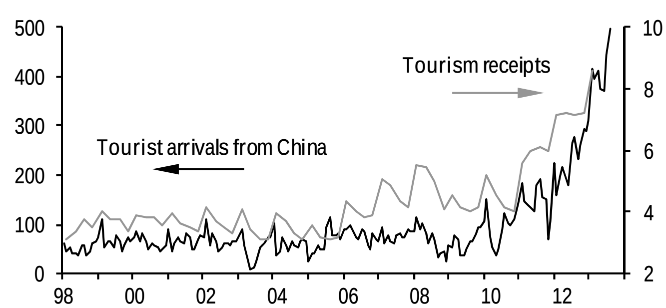
Source: Thailand Energy Policy and Planning Office, Bank of Thailand, J.P. Morgan



Source: Bank of Thailand, J. P. Morgan



Source: Bank of Thailand, J.P. Morgan



Source: Bank of Thailand, J.P. Morgan

Economic Research Note

Singapore: another uneventful MAS meeting expected

- **Singapore's growth outlook has become more constructive and downside risks have dissipated**
- **Inflation has moderated but a tight labor market leaves risks, particularly for core inflation, biased upward**
- **MAS most likely to maintain monetary policy settings, though there is a small chance of modest tightening**

Singapore's outlook was uncertain early this year as the global economy began 2013 facing several headwinds (including US fiscal drag and slower Chinese growth). But, the global economy has weathered these challenges and Singapore's economy has actually performed well, growing modestly in 1Q and then surging 15.5% (annualized) in 2Q. Growth has moderated recently and DM and EM economies still face challenges but Singapore's growth outlook has become more positive while downside risks have dissipated over the year.

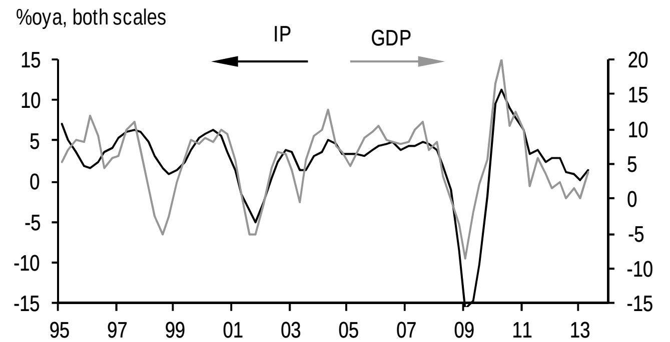
At the same time, inflation has eased. Most of the slowdown has been due to housing and certificate of entitlement (COE) costs, but core inflation (ex. accommodation and private transport) has also eased. However, the labor market, which historically has driven core price pressures, remains tight (COE prices have started to rise again, too). Thus, we expect CPI and core inflation to drift higher, though neither measure is likely to reach the uncomfortably high growth rates of 2011 and 2012.

Given the improved growth outlook and expectation for price pressures to firm, the MAS has no room to ease next month. On the other hand, the global recovery remains fragile and numerous risks remain, so the MAS does not have much room to tighten policy, either. Thus, we expect that the MAS will stay on hold next month with a hawkish bias warning that it will be on guard against price pressures that could arise from a tight labor market and an improved growth outlook.

Traditional external linkages mostly intact

The link between global demand and growth in Singapore is straightforward: strong global demand leads to stronger exports and fixed investment. More investment translates to more jobs and higher income growth, which supports consumption, and leads to price pressures. This framework has not changed in recent years despite stronger domestic demand and weaker external demand. In fact, simple regression analysis shows that many of the correlations between these links have increased in the period since the 2008-09 global crisis.

Global IP and Singapore real GDP

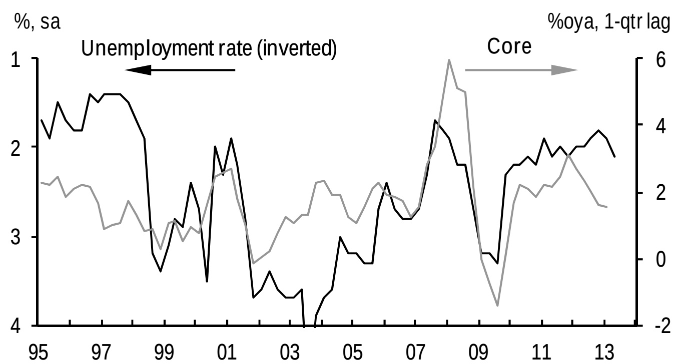


Source: Department of Statistics; J.P. Morgan

Singapore: real GDP and unemployment rate

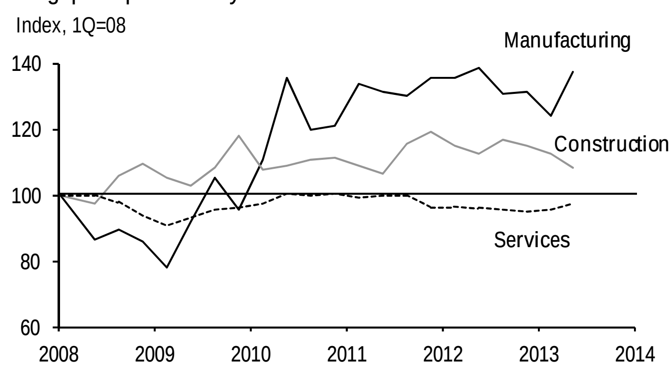
Source: Department of Statistics and Ministry of Manpower

Singapore: unemployment rate and CPI inflation



Source: Ministry of Manpower; MAS

Singapore: productivity



Source: J. P. Morgan

One recent wrinkle in the framework, however, is that the link between growth and employment has weakened. This has happened for a few reasons. First, immigration has tightened due to the government's economic restructuring plan. This has kept the unemployment rate low despite slower economic growth in 2011 and 2012 by restricting labor supply (second chart, previous page). Second, a strong credit cycle and large public sector infrastructure pipeline have supported domestic demand. Since construction and services are more labor-intensive and less productive than manufacturing, hiring in these sectors has been resilient to slower growth (manufacturing in contrast has shed jobs on net since 2007). Thus, until construction or service sector productivity rises, or until economic growth slows more sharply, labor market conditions will likely remain tight.

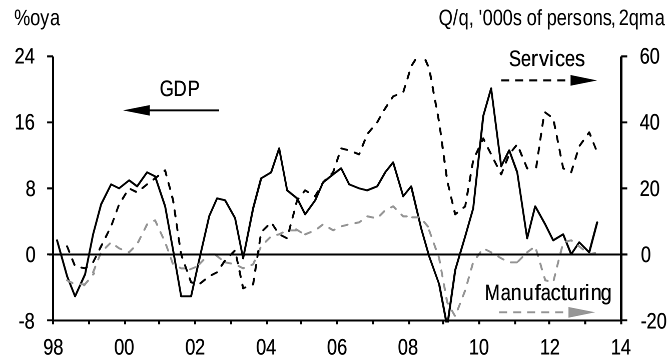
Inflation has eased for the wrong reasons

Since hitting a 2013 high of 4.9%oya in February, CPI inflation slowed to 1.9% as of July. Core inflation eased as well, albeit more gradually, to 1.6% from 1.9% in July. This year, we forecast CPI and core inflation to average 2.6% and 1.7%, respectively, well below their 2012 averages of 4.6% and 2.5%. Nevertheless, the MAS is not taking comfort in the lower CPI inflation rate, for a few reasons. First, accommodation and transport (which includes COEs), which monetary policy has little effect on, have accounted for 2.7%-pts of the 3.0%-pt decline in CPI inflation since February. Core inflation, which excludes most of those categories, has slowed only 0.3%-pt over the same period. Second, while inflation rates are not likely to print anywhere near their 2011 and 2012 rates, price pressures will likely gain traction later this year from tight labor market conditions and perhaps from less benign import prices (COE prices have also started to rise again, which will contribute to higher CPI inflation). Thus, while the MAS is unlikely to be alarmed by the inflation outlook, we expect CPI inflation will print in the 2%-3% range during the remainder of 2013 from the 1.5%-2% range in the last four months, while core inflation should creep toward 2.0%oya by year-end from 1.6% in July.

Another uneventful MAS meeting

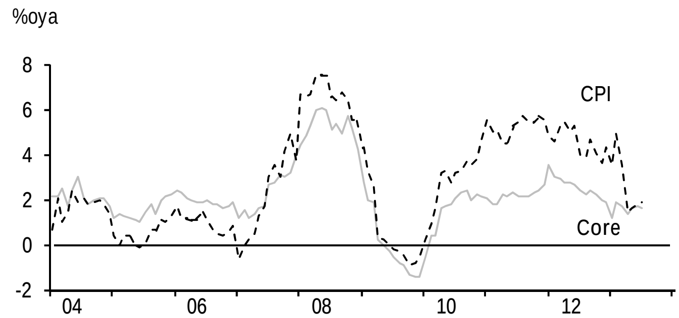
Between October 2004 and April 2007, the MAS did not change its monetary stance once. Then, between October 2007 and April 2012, the MAS changed its stance at almost every meeting, and it often adjusted more than one setting of its band, basket, crawl (BBC) regime. We have now likely shifted back to a policy environment similar to the 2004-2007 period when changes to the currency band will be less frequent. We expect the MAS to maintain its stance next month for the third straight meeting, and we put only a 10%-15% probability on the risk of a surprise tightening, which would most likely come from an upward shift in the slope.

Singapore: GDP and change in employment



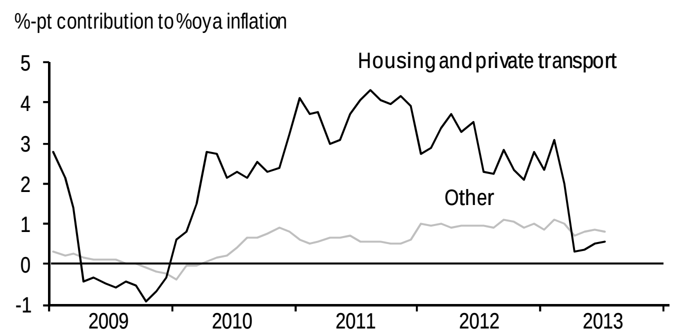
Source: Department of Statistics and Ministry of Manpower

Singapore: CPI inflation



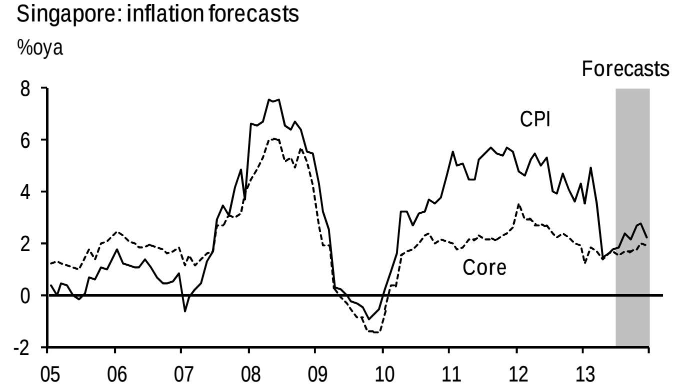
Source: Department of Statistics

Singapore: contributions to inflation



Source: Department of Statistics

Singapore: inflation forecasts



Source: Department of Statistics; J.P. Morgan

United States

- **FOMC decides not to taper, and its fed funds forecast at year-end 2016 is centered on an unexpectedly low 2.0%**
- **Taper expected in December but depends on greater confidence in Fed forecast of stronger growth ahead**
- **Manufacturing indicators turn more positive, housing data are very mixed, inflation is still well below target**

The FOMC statement and forecasts and Chairman Bernanke's commentary in the post-meeting press conference show more concern about risks to growth and greater willingness to support the economy than previously appreciated. The Fed decided to leave its $85 billion per month asset purchase program intact. The median of the participants' forecasts look for the fed funds rate to end 2016 at only 2.0%, even though the FOMC central tendency forecasts show the unemployment rate approaching mainstream estimates of NAIRU and inflation approaching the Fed's 2.0% target at that time.

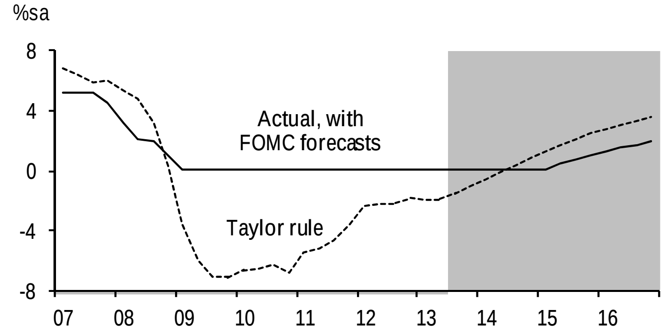
In the press conference, Chairman Bernanke mentioned three reasons for delaying tapering. The first was a desire to see more data before being confident in the Fed's forecast of stronger growth ahead. Data in hand suggest that both payroll employment and real GDP are slowing this quarter. The second reason was to have more time to assess the impact of financial tightening, including higher mortgage rates, on the economy. The third was to wait for more clarity on fiscal policy including the debate about raising the debt ceiling.

The economic data are unlikely to give the Fed materially greater confidence in the economic outlook as soon as the October 29-30 meeting. Assuming the economy delivers to our forecast of stronger job growth and economic growth through the rest of the year, we think that the Fed will start to taper asset purchases in December.

This past week's calendar provided timely information about the manufacturing and housing industries. The 0.7% samr increase in factory output in August and the improvement in the first Fed factory surveys for September indicate that manufacturing activity is accelerating. The latest housing indicators are mixed, with the September Homebuilders survey and August existing home sales at their peaks for the expansion, August housing starts and permits holding in their relatively narrow range over the past several months, and the 6-months' expectations component of the NAR realtor survey turning down noticeably in August.

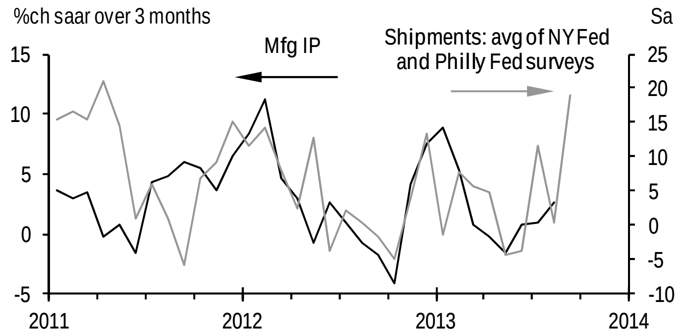
The upcoming calendar includes the third report on 2Q13 GDP and results are expected to show 2.9% saar growth (up from 2.5%) with the revision concentrated in domestic final

FOMC central forecast of fed funds rate and Taylor rule forecast



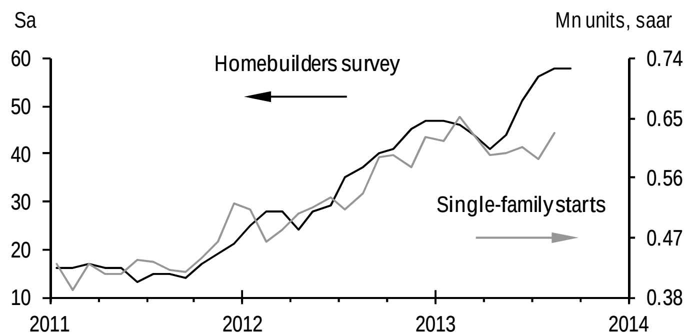
Source: Federal Reserve, J.P. Morgan

Manufacturing IP and NY Fed/Philly Fed measure of factory shipments



Source: Federal Reserve Board, NY Fed, Philadelphia Fed

Homebuilders survey and single-family housing starts



Source: NAHB, Census

sales. Other economic releases including the September flash PMI (Monday), August new home sales (Wednesday), and August consumer spending (Friday) will also influence views on economic performance.

Manufacturing looking a lot better

The ISM and PMI manufacturing surveys have been pointing to an upturn in factory output since July. The first hard evidence of the rebound came in the August IP report. While the 0.7% samr increase in August factory output was every bit as strong as expected based on the factory detail of the payroll report and on auto production schedules, the strength was partly offset by a downward revision to the previously released July figure to -0.4% (from -0.1%). This July-August pattern partly reflects a sharp drop in auto production in July followed by a rebound in August. Factory output ex. motor vehicles increased 0.4% in August following a 0.1% decline in July.

Factory output, whether measured in total or ex. motor vehicles, has accelerated from outright declines in the 3 months through May to moderate gains of 2.6% saar (all manufacturing) or 2.3% (mfg. ex. autos and parts) in the 3 months through August. The various September manufacturing surveys will condition views on the near-term outlook. The evidence from the first two September regional manufacturing surveys, from the New York and Philadelphia regions, suggests that activity is continuing to accelerate in September.

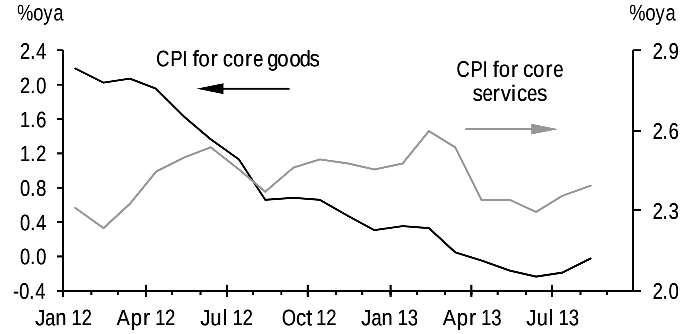
The average of the two derived composites of the NY and Philly surveys (calculated from components using ISM weights) increased 3.9pts to 53.7, its highest level in more than two years. The measure of shipments in both surveys increased sharply: up 15.0pts to 16.4 in New York, up 21.2pts to 21.2 in Philadelphia. New orders rose in both surveys as well, although by much more in the Philadelphia Fed region than in New York. The forecast looks for the flash PMI for September (out Monday), a more representative national survey, to increase from 53.1 in August to 54.0, which would be the highest reading for the PMI since March.

Housing data turn stronger, and weaker

Different housing indicators continue to tell very different stories about how the housing market has responded to higher mortgage rates. The National Homebuilders Survey remains the strongest of the housing indicators, posting strong gains in July and August and then holding its August level in September. The component measuring the assessment of current sales had hit new highs for the expansion in July and August and was unchanged in September. This contrasts with the Census estimate of new home sales showing a 13.4% samr plunge in the latest July reading. The measure of prospective buyer traffic continued to increase through September, sharply at odds with concerns that higher mortgage rates might be discouraging potential homebuyers.

While the Homebuilders Survey is appreciably higher than its 1H13 average, single-family housing starts and permits are not. There were good gains in the latest August readings for both single-family housing starts, up 7.0% samr, and permits, up 3.0%. August levels were not much above their 1H13 averages, and trends for both single-family starts and permits have flattened out over the past several months. While single-family activity has flattened out lately, the trends in multifamily starts and permits have declined from early year peaks and the July-August average for both is about 6% (not annualized) below their 1H13 averages.

CPI: core goods and core services



Source: BLS

Although new home sales had dropped sharply in July, existing home sales continued to climb through the latest August reading, up 1.7% samr to a pace of 5.48 million. This leaves existing homes sales for the quarter to date running 41.3% saar above the 2Q13 average, presumably reflecting a rush to buy before mortgage rates rose even further. Commentary from the NAR suggests that home sales in future months will be uneven, reflecting the effects of higher mortgage rates and low inventories. The August Realtors survey shows a slight increase in the monthly assessment of current conditions, but the six-month outlook has been declining since June.

Reports on August new home sales (Wednesday) and August pending existing home sales (Thursday) will provide new information about the housing market. New home sales are expected to rise 6.6% samr, reversing nearly half the July decline. Pending home sales are forecast to be unchanged.

Core inflation still well below target

The rate of increase in the core PPI has been slowing, and nonfuel import prices have declined over the past year. This deceleration has passed through into slower increases in the CPI for core consumer goods. This pattern continued in August. The CPI for August rose just 0.1% samr and the core CPI was also up 0.1% (or 0.13% to two digits). Core goods prices were unchanged and have progressively slowed from 2.1%oya in January 2012 to readings slightly below year-ago levels for the past five months. The rate of increase in core services prices has been much more stable. These increased 0.2% in August and are running 2.4%oya, close to their average pace through 2012-2013.

The Fed’s preferred measures of inflation are the PCE price measures rather than the CPI. Based on detail of the August CPI and PPI releases, the PCE price index for August is expected to rise 0.1% samr and 1.1%oya. The core PCE price index is forecast to rise 0.07% samr in August. This result would leave the core PCE price index up 1.2%oya and up 1.5% saar over the past three months. In short, inflation continues to run well below the Fed's 2.0% target.

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Data releases and forecasts

Mon
Sep 23
8:58am

Markit manufacturing PMI (flash)

Index, sa

	Jun	Jul	Aug	Sep
Composite[1]	51.9	53.7	53.1	54.0
New orders (30%)	53.4	55.5	55.7	
Output (25%)	53.5	54.8	52.5	
Employment (20%)	49.9	53.0	53.1	
Sup. del. (15%, inv.)	50.6	47.4	46.2	
Stks of purch (10%)	50.6	48.7	46.2	
New export orders	46.3	52.5	52.0	
Backlogs of work	51.3	52.6	49.6	
Output prices	51.6	50.8	51.1	
Input prices	54.1	57.8	56.2	
Stocks of finished goods	51.4	47.6	45.5	
Quantity of purchases	53.4	54.4	53.9	
ISM-weighted composite[2]	51.4	52.9	52.2	

1. Weights in parentheses
2. Attributes ISM-composite weights (equal weights) to corresponding PMI

We forecast that the Markit manufacturing PMI's headline increased 0.9pt to 54.0 in the flash September report. Although the survey's headline cooled a bit in August, its forward-looking gap between orders and inventories improved and pointed to additional activity in the manufacturing sector ahead. Several other manufacturing indicators have also been upbeat lately, including a substantial improvement in the September Philadelphia Fed survey.

Tue
Sep 24
9:00am

S&P/Case-Shiller home price index

%oya, unless noted

	Apr	May	Jun	Jul
20-city composite	12.1	12.2	12.1	12.7
%m/m, sa	1.7	1.0	0.9	0.9
10-city composite	11.5	11.8	11.9	

Tue
Sep 24
9:00am

FHFA home price indexes

purchase-only

	Apr	May	Jun	Jul
%oya	7.3	7.6	7.8	8.6
%m/m (sa)	0.5	0.8	0.6	0.9

We believe both the Case-Shiller 20-city composite index and the FHFA house price index increased 0.9% samr in July. These forecasted increases should bring the Case-Shiller index up 12.7%oya in July and the FHFA index up 8.5%oya in the month. Most house price measures have been rising for more than a year while the housing market has been recovering, and we believe house prices will continue to appreciate. We had seen some signs that the pace of price increases started to moderate over the few months leading up to June (and we expect additional moderation eventually), but the July data already reported in the CoreLogic house price index point to another solid increase in house prices during the month. The CoreLogic, Case-Shiller, and FHFA house price indexes generally move in a similar manner, although there are some differences in terms of sampling, timing, and index construction between the various measures.

Tue
Sep 24
10:00am

Consumer confidence

Sa

	Jun	Jul	Aug	Sep
Conference Bd index	82.1	81.0	81.5	79.5
Present situation	68.7	73.6	70.7	
Jobs plentiful	11.3	12.3	11.4	
Jobs hard to get	37.1	35.2	33.0	
Labor mkt diff	-25.8	-22.9	-21.6	
Expectations	91.1	86.0	88.7	

We forecast that the Conference Board consumer confidence index declined 2.0pts to 79.5 in September. The index peaked at 82.1 in June before slipping to 81.0 in July and then most recently edging up to 81.5 in August. Meanwhile, several other consumer sentiment barometers have also cooled recently from their respective expansionary peaks. We expect some additional weakening in the Conference Board measure in September based on the decline already reported in the preliminary University of Michigan consumer sentiment index for the month. The Conference Board and University of Michigan indexes typically have similar trends even though the monthly changes do not always match up.

Wed
Sep 25
8:30am

Durable goods

%m/m, sa

	May	Jun	Jul	Aug
New orders	5.5	3.9	-7.4	-0.3
Ex transportation	1.3	0.1	-0.8	0.5
Nondef cap. gds ex air	2.1	1.1	-4.0	1.5
Shipments	1.3	-0.1	-0.3	0.7
Nondef cap. gds ex air	2.0	-1.0	-1.7	1.6
Inventories	-0.1	0.1	0.3	

We estimate that new orders for durable goods slipped 0.3% in August while related shipments increased 0.7%. The data on durable goods have looked soft lately even though the national manufacturing surveys have been upbeat. Excluding the volatile transportation components, durable goods orders increased only 2.3% saar over the three months through July while the durable goods shipments declined 0.7% saar. And for the important core capital goods components, orders declined 3.5% saar over the same three months while shipments declined 2.5% saar. Separate manufacturing IP data had also looked soft through July, but then improved nicely in August, and we expect similar improvement in the August durable goods report. Specifically, we forecast a 1.5% increase in core capital goods orders and a 1.6% increase in core capital goods shipments for the month. Even with these increases, the trends in the data (as measured on a 3-month basis) should still look soft after the recent declines in the monthly data.

Away from the core capital goods data, industry data point to another large decline in civilian aircraft orders in August as well as a more modest decline in aircraft shipments during the month, which should weigh on the figures reported for total orders and shipments. On the

Sources: ADP/Moody's Analytics, BEA, BLS, Census Bureau, Conference Board, Federal Reserve Board, ISM, J.P. Morgan, NAHB, NAR, NFIB, NY Fed, Markit, Philadelphia Fed, Standard & Poor's, University of Michigan, US Treasury

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positive side, data already reported on IP point to an increase in orders and shipments of motor vehicles and parts, which should provide some offset to the declines in the aircraft data.

Wed
Sep 25
10:00am

New home sales

	May	Jun	Jul	Aug
Total (000s,saar)	439	455	394	420
%m/m	-1.6	3.6	-13.4	6.6
%oya nsa	17.1	26.5	6.1	12.3
Months' supply	4.5	4.3	5.2	
Median price (%oya)	9.8	11.1	8.3	

We believe new single-family home sales increased 6.6% to 420,000 saar in August. New home sales tumbled 13.4% in July, which was likely at least partially a response to the recent increase in mortgage rates. While various other housing indicators have also weakened since rates increased, the data related to new home sales have been mixed lately. Homebuilder sentiment regarding home sales continued to trend higher despite the increase in mortgage rates, while mortgage purchase application volumes have moved lower over the past few months. The University of Michigan survey data on homebuying conditions dropped off in August but then undid some of the August decline in the preliminary September report. With this mixed tone of the data in mind as well as our belief that the housing recovery will likely continue, we look for about half the July decline in new home sales to be undone in the August report.

Thu
Sep 26
8:30am

Jobless claims

Thousands, sa

	New claims (wr.)		Continuing claims		Insured
	Wkly	4-wk avg	Wkly	4-wk avg	Jobless,%
Jul 13[1]	336	347	3003	3027	2.3
Jul 20	345	346	2951	3026	2.3
Jul 27	328	342	3023	3025	2.3
Aug 3	335	336	2970	2987	2.3
Aug 10	322	333	3003	2987	2.3
Aug 17[1]	337	331	2994	2998	2.3
Aug 24	332	332	2944	2978	2.3
Aug 31	323	329	2815	2939	2.2
Sep 7	294	322	2787	2885	2.1
Sep 14[1]	309	315			
Sep 21	330	314			

1. Payroll survey week

We forecast that initial jobless claims increased 21,000 to 330,000 during the week ending September 21. The levels of claims reported for the weeks ending September 7 (294,000) and September 14 (309,000) were the two lowest figures of the expansion to date, but the Department of Labor noted that these low levels of claims were related to reported issues caused by computer upgrades in two states (believed to be California and Nevada). With the disruptions caused by these upgrades expected to ease and some potential payback for any claims that were unable to be filed or processed, we look for a jump up in claims in the upcoming report. While there is a considerable amount of uncertainty regarding the impact of the recent claims distortion, it appears that the underlying trend in the data (away from the distortion) has continued to improve at least to some degree lately.

Thu
Sep 26
8:30am

Gross domestic product

%ch, q/q, saar, unless noted

	1Q13	Adv 2Q13	Sec 2Q13	Thi 2Q13
Real GDP	1.1	1.7	2.5	2.9
Final sales	0.2	1.3	1.9	2.3
Domestic final sales	0.5	2.0	1.9	2.4
Consumption	2.3	1.8	1.8	2.2
Equipment	1.6	4.0	2.9	3.1
Intellectual property	3.8	3.9	-0.9	-0.9
Nonres. structures	-25.7	6.8	16.2	17.8
Residential investment	12.5	13.4	12.9	14.1
Government	-4.2	-0.4	-0.9	-0.4
Net exports (pct.pt.contr.)	-0.3	-0.8	0.0	-0.1
Inventories (pct.pt.contr.)	0.9	0.4	0.6	0.6
Core PCE price index	1.4	0.8	0.8	
(%oya)	1.5	1.2	1.2	
GDP chain price index	1.3	0.7	0.8	
(%oya)	1.6	1.4	1.4	
Adj. corporate profits	-1.3		3.9	
(%oya)	2.1		5.0	

We believe 2Q real GDP growth will be revised up from 2.5% to 2.9% between the BEA's second and third reports on growth for the quarter. The 2Q Quarterly Services Survey pointed to stronger consumption growth during the quarter than the BEA had previously estimated, and we believe real consumption growth will be revised up from 1.8% to 2.2% (also incorporating a slight upward revision to goods consumption based on separate retail sales data). Away from the Quarterly Services Survey, most of the recent economic indicators have been slightly stronger than, but fairly close to, the figures used by the BEA in its second report on GDP. We look for pretty modest upward revisions to equipment spending (from 2.9% to 3.1%), nonresidential structures investment (from 16.2% to 17.8%), residential investment (from 12.9% to 14.1%), and government spending (from -0.9% to -0.4%). We also anticipate slight downward revisions to net exports (from -$422.0 billion to -$426.8 billion) and the change in inventories (from $62.6 billion to $61.9 billion) reported for the second quarter.

Thu
Sep 26
10:00am

Pending home sales

sa, unless noted

	May	Jun	Jul	Aug
Total (mn, ar)	111.3	110.9	109.5	109.5
%ch m/m	5.8	-0.4	-1.3	0.0
%oya (nsa)	11.2	9.1	8.6	7.5

Sources: ADP/Moody's Analytics, BEA, BLS, Census Bureau, Conference Board, Federal Reserve Board, ISM, J.P. Morgan, NAHB, NAR, NFIB, NY Fed, Markit, Philadelphia Fed, Standard & Poor's, University of Michigan, US Treasury

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We forecast that the pending home sale index was unchanged in August. Pending home sales—which are counted when contracts are signed—declined in June (-0.4%) and July (-1.3%,) which was likely a response to the recent increase in mortgage rates. A number of other housing indicators have also weakened lately following the rise in rates, but there continue to be some upbeat housing indicators as well; with these mixed signals, we do not see a clear reason for a change in the pending home sales index.

Fri
Sep 27
8:30am

Personal income

%m/m, sa, unless noted

	May	Jun	Jul	Aug
Personal income	0.3	0.3	0.1	0.4
Wages & salaries	0.2	0.4	-0.3	0.3
Consumption	0.2	0.6	0.1	0.2
Real consumption	0.1	0.2	0.0	0.1
PCE price index	0.1	0.4	0.1	0.1
Core	0.11	0.23	0.08	0.07
Mkt-Based Core	0.1	0.2	0.1	
Core (%oya)	1.2	1.2	1.2	1.2
Mkt-Based Core (%oya)	1.1	1.1	1.2	
Saving rate	4.6	4.4	4.4	4.5

We believe real consumption increased 0.1% in August while nominal spending increased 0.2%. Data already released on auto sales point to solid pickup in motor vehicles and parts consumption during the month, but separate data from the August retail sales report point to pretty modest gains in spending on several other goods categories. We also anticipate a decline in utilities consumption in August, which should be a drag on the overall spending numbers based on related production data from the August IP report.

We estimate that nominal income increased 0.4% in August with a similar-sized increase in disposable income during the month as well. With persistent labor market slack in recent years, income gains have been pretty soft. The July report was especially soft regarding wages and salaries (-0.3%) which was due in part to government furloughs associated with sequestration, though private sector wages declined during the month as well. Data from the August employment report point to a bounce back in private sector wages during the month, and we expect a more trend-like soft reading for government wages (meaning not much additional drag from furloughs) resulting in overall wages and salaries increasing 0.3% in August. The August data for the other main components related to income should be close to the recently reported trends.

For the main price indexes, data from the August CPI and PPI point to a 0.1% increase in the August PCE deflator (+1.1% oya) and a 0.07% increase in the core PCE deflator during the month (+1.2% oya). These expected increases would keep headline inflation as well as the core index—the Fed's preferred measure of underlying inflation—trending below the Fed's 2% target.

Sources: ADP/Moody's Analytics, BEA, BLS, Census Bureau, Conference Board, Federal Reserve Board, ISM, J.P. Morgan, NAHB, NAR, NFIB, NY Fed, Markit, Philadelphia Fed, Standard & Poor's, University of Michigan, US Treasury

Fri
Sep 27
9:55am

Consumer sentiment

	Jul	Aug	Pre Sep	Fin Sep
Univ. of Mich. Index (nsa)	85.1	82.1	76.8	78.0
Current conditions	98.6	95.2	91.8	
Expectations	76.5	73.7	67.2	
Inflation expectations				
Short term	3.1	3.0	3.2	
Long term	2.8	2.9	3.0	
Home buying conditions	167	155	159	

We look for the University of Michigan consumer sentiment index to be revised up from 76.8 to 78.0 between the preliminary and final September reports, which would still represent a decline in sentiment relative to the figure reported for August (82.1). Like the Michigan survey, several other sentiment measures have weakened in recent months from their recently reported expansionary peaks. But upward revisions between the preliminary and final monthly surveys have been common over the past few years, and the daily Rasmussen Consumer Index and weekly Bloomberg Consumer Comfort Index also point to modest improvement in sentiment since earlier in the month.

Review of past week's data

Industrial production (Sep 16)

%m/m, sa, unless noted

	Jun		Jul		Aug	
Industrial production	~~0.2~~	*0.1*	0.0		~~0.6~~	*0.4*
Manufacturing	~~0.2~~	*0.3*	~~0.1~~	*-0.4*	*0.7*	
Motor vehicles & parts	1.2		~~1.7~~	*-4.5*	~~4.1~~	*5.2*
High-tech	~~0.2~~	*-0.1*	~~1.0~~	*1.3*		*1.7*
Mfg ex motor vehicles	~~0.1~~	*0.3*	~~0.0~~	*-0.1*	~~0.5~~	*0.4*
Business equipment	~~0.4~~	*0.7*	~~0.0~~	*-0.9*		*0.9*
Capacity utilization	~~77.7~~	*77.8*	77.6		~~78.0~~	*77.8*
Manufacturing	~~75.9~~	*76.1*	~~75.8~~	*75.7*	~~76.2~~	*76.1*

Overall industrial production increased 0.4% in August with a 0.7% increase in manufacturing production during the month. The solid August manufacturing data came after a weak few months (including a downward revision to July). And with separate national manufacturing survey data pointing to continued growth in production ahead, we believe the increase in August IP likely marks the start of an improving trend in manufacturing output.

In some of the details of the IP report, motor vehicle and parts production popped up 5.2% in August, more than undoing the 4.5% drop reported for July. Away from the auto sector, manufacturing IP rose 0.4% in August, which was the largest monthly gain since February, and production increased in most of the main underlying industry groups during the month. Away from manufacturing, mining production increased 0.3% in August for its sixth consecutive monthly gain. And utilities production continued to drop off in August, falling 1.5% during the month and 18% saar over the most recent five months—this plunge in utilities production came after a surge earlier this year.

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Empire State survey (Sep 16)

Diffusion indices, sa

	Jul	Aug	Sep	
General bus. conditions	9.5	8.2	~~10.0~~	*6.3*
New orders	3.8	0.3		*2.4*
Shipments	9.0	1.5		*16.4*
Unfilled orders	-8.7	-6.0		*-6.4*
Prices paid	17.4	20.5		*21.5*
Prices received	1.1	3.6		*8.6*
Composite	51.3	50.8		*52.4*

The Empire State survey's headline—reflecting general business conditions—cooled off a bit in September while the underlying details were mixed, but generally somewhat more upbeat. Its headline slipped from 8.2 in August to 6.3 in September while its ISM-weighted composite increased from 50.8 to 52.4, reaching its highest level since February. The survey's shipments index jumped up 15.0 points to 16.4 in September while the new orders index inched up 2.1 points to a still-modest 2.4. The inventories index increased 5.8 points to 2.2, its first reading above zero since May 2012. And rounding out the components related to the ISM composite, the delivery times index declined 3.1 points to -4.3 while the employment measure slipped 3.3 points to 7.5. The Empire State survey is the first regional survey to be reported each month, so it is timely, but it is not one of the more reliable manufacturing indicators.

CPI (Sep 17)

%m/m, sa, unless noted

	Jun	Jul	Aug	
Total	0.5	0.2	*0.1*	
%oya (nsa)	1.8	2.0	*1.5*	
Core	0.16	0.15	~~0.16~~	*0.13*
%oya (nsa)	1.6	1.7	*1.8*	
Core services	0.2	0.2		*0.2*
Core goods	0.2	0.0		
Food	0.2	0.1	~~0.0~~	*0.1*
Energy	3.4	0.2	~~-0.1~~	*-0.3*
Housing	0.2	0.0		*0.1*
Owners' eq. rent	0.19	0.15	~~0.18~~	*0.25*
Rent	0.21	0.24	~~0.22~~	*0.37*
Lodging away from home	-0.8	0.2	~~-0.2~~	*-0.7*
Apparel	0.9	0.6	~~-0.4~~	*0.1*
New vehicles	0.3	0.1	~~-0.1~~	*0.0*
Used vehicles	-0.4	-0.4	*-0.1*	
Airfares	-1.7	-1.3	~~-0.4~~	*-3.1*
Communication	-0.1	-0.2	~~-0.2~~	*0.0*
Medical care	0.4	0.2	~~-0.3~~	*0.6*

The consumer price index ticked up 0.1% in August, in line with our expectations, on mild increases in core and food prices and a small decline in energy prices. The trend in headline prices has been subdued over the past year, with the index up 1.5%oya. Core prices, which exclude food and energy, moved up 0.13%, the softest core print since April. Core prices are now up 1.8% over the prior year. The medium-term outlook for core inflation should continue to be benign, with no pressure from either imported inflation or wages. Falling prices for education (-0.1%m/m), airfares (-3.1%), and lodging away from home (-0.7%) contributed to the weak core outcome in August. These declines were offset in part by acceleration in rents (owners' equivalent rent +0.25%m/m; tenants' rent +0.37%) and medical care prices (+0.6%). Energy prices dipped 0.3% in August on falling prices for gasoline and utility gas service. Food prices edged up 0.1%, staying within the tight 0.0% to 0.2% range that such prices have kept to for much of the past year.

Turning to details of core prices, the drop in education prices was the largest in the history of the series, which dates back to 1993. The drop was largely due to a tumble in college tuition, which tends to be volatile in August and September and generally stable the remainder of the year. The decline in airfares was the largest single-month drop since November 2008, and airfares are down 22%saar over the past three months. Vehicle prices were tame in August, with used vehicle prices sliding 0.1% and new vehicle prices unchanged. Apparel prices ticked up 0.1%, a slowdown from increases of 0.9% and 0.6% in June and July, respectively. However, a few key components of core prices heated up in August. The increase in owners' equivalent rent was a step up from the 0.15% rise in July, and the jump in tenants' rent was the largest increase since June 2008. Similarly, the jump in medical care prices was the largest since July 2007. Medical care services prices in the CPI and PCE have diverged in recent months, up 2.4%saar for the six months through July in the CPI and up 0.7%saar over the same period in the PCE. This divergence likely continued in August given the strong CPI outcome and weakness in August PPI medical services prices (the PPI prices are inputs to the PCE medical services index).

Details from the August CPI and PPI releases signal a 0.1% rise in the August PCE deflator (1.1%oya) and a 0.07% increase in the core PCE deflator (1.22%oya).

Homebuilders survey (Sep 17)

Sa

	Jul	Aug		Sep	
Housing market	56	~~59~~	*58*	~~59~~	*58*
Present sales	59	62			*62*
Prospective buyer traffic	45	~~45~~	*46*		*47*

The NAHB housing market index was unchanged at 58 in September from an August figure that was revised down by 1 point. The recent resilience in the NAHB data is a welcome contrast from the many separate housing indicators that have weakened since interest rates started to rise in May. Despite the recent increase in rates, the overall NAHB index has not declined since April and the 58 reported for the most recent two months was the highest figure reported since November 2005. We remain optimistic that the housing recovery will continue going forward, acknowledging that the 3Q data have been soft for the most part, likely in response to the change in mortgage rates.

Within the details of the NAHB survey, the present sales measure held at its expansionary peak of 62 in September. The sales expectations index slipped from 68 in August (its expansionary peak so far) to 65 in September while the prospective buyers traffic index ticked up from 46 to 47, reaching its new high for the expansion. All four of the regional indexes increased in September to their respective expansionary

Sources: ADP/Moody's Analytics, BEA, BLS, Census Bureau, Conference Board, Federal Reserve Board, ISM, J.P. Morgan, NAHB, NAR, NFIB, NY Fed, Markit, Philadelphia Fed, Standard & Poor's, University of Michigan, US Treasury

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highs signaling that the recent improvement in the housing market has been broad-based across regions (these monthly regional measures are really three-month averages).

Housing starts (Sep 18)

Million units, saar

	Jun		Jul		Aug	
Starts	~~0.85~~	*0.84*	~~0.90~~	*0.88*	~~0.90~~	*0.89*
Single-family starts	0.60		0.59		~~0.60~~	*0.63*
Multifamily starts	~~0.24~~	*0.23*	0.30		~~0.30~~	*0.26*
Permits	0.92		0.95		~~0.96~~	*0.92*

The starts and permits data came in weaker than anticipated in August, with starts edging up 0.9% to 891,000 saar and permits declining 3.8% to 918,000 saar (as well as modest downward revisions to starts in June and July). But the disappointing figures reported for August were due to the declines in the volatile multifamily data, and the single-family data—which are more important and less choppy—improved in August and were stronger than anticipated. Overall, the starts and permits report was consistent with our view that the housing recovery will continue going forward, although growth in residential investment likely slowed somewhat between the second and third quarters.

Within the details of the report, single-family permits—an important forward-looking indicator—increased 3.0% to 627,000 saar in August; this increase more than reversed the 2.6% decline reported for July and brought the level of permits up to a new high for the expansion (which is still quite low by historical standards). Meanwhile, single-family starts jumped up 7.0% to 628,000 saar in August. Although the August starts data remained below the peak for the expansion reported for February (652,000), the current gap between starts and permits points to additional growth in starts to come.

There were large drops in multifamily starts (-11.1% to 263,000 saar) and permits (-15.7% to 291,000 saar) in August after even larger increases reported for July. Through the monthly volatility, the trends in the multifamily data have weakened in recent months and multifamily starts and permits were each down slightly more than 30% saar over the six months through August.

Philadelphia Fed survey (Sep 19)

Diffusion indices, sa

	Jul	Aug	Sep	
General bus. conditions	19.8	9.3	~~11.0~~	*22.3*
New orders	10.2	5.3		*21.2*
Shipments	14.3	-0.9		*21.2*
Inventories	-21.6	-11.3		*-1.8*
Prices paid	21.5	17.3		*25.3*
Prices received	7.0	9.9		*12.7*
Composite	51.1	48.8		*55.0*

The Philadelphia Fed survey's headline popped up 13.0 points to 22.3 in September while its ISM-weighted composite surged 6.2 points to 55.0. The Philadelphia Fed survey is generally one of the more reliable regional manufacturing indicators regarding the national activity measures, and while we had been expecting activity in the manufacturing sector to pick up, the improvement in the September Philadelphia Fed survey surpassed our expectations.

The details of the report were upbeat across the board. There were large increases in the important new orders index (+15.9 points to 21.2) and as well as the shipments measure (+22.1 points to 21.2). There were also more modest, but still solid, increases in the measures of employment (+6.8 points to 10.3) and delivery times (+7.8 points to -1.2). Rounding out the components related to the ISM composite, the inventories index increased 9.5 points to -1.8, keeping a healthy forward-looking gap between the orders and inventories measures.

Most other details of the report also looked good away from the ISM composite's components. The workweek measure jumped 14.8 points to 12.2 and the general expectations measure soared 19.3 points to 58.2, its highest level since 2003.

Existing home sales (Sep 19)

	Jun	Jul		Aug	
Total (mn, saar)	5.06	5.39		~~5.25~~	*5.48*
%m/m	-1.6	6.5		~~-2.6~~	*1.7*
%oya nsa	8.0	20.7		~~8.5~~	*10.5*
Months' supply (nsa)	5.1	~~5.1~~	*5.0*		*4.9*
Single-family	5.2	~~5.0~~	*4.9*		*5.0*
Median price (%oya)	13.3	~~13.7~~	*13.1*		*14.7*

The August existing home sales report signaled continued improvement in the housing market. We should note that the existing home sales data lag most other housing indicators, and a lot of the housing data have turned softer over the past few months since mortgage rates increased. In today's report, existing home sales increased 1.7% to 5.48mn saar in August, reaching a new high for the expansion. Other related indicators (including pending home sales and mortgage purchase applications) point to a decline in existing home sales sometime in the near term. While we anticipate some slowing in the housing recovery between the second and third quarters, we are optimistic that the housing recovery will continue.

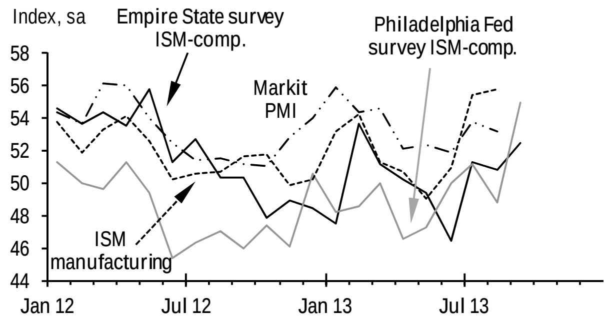
In other details of the report, the median existing home sale price increased 14.7% oya in August; although this is not a very reliable home price measure, because it does not control for change in the sale mix, other more reliable measures also show a solid pace of house price appreciation lately. Prices are likely benefitting from a reduced share of distressed sales in the market, which declined from 22% to 12% over the 12 months through August. Limited available inventory is also likely to keep upward pressure on prices and spur new home construction.

Sources: ADP/Moody's Analytics, BEA, BLS, Census Bureau, Conference Board, Federal Reserve Board, ISM, J.P. Morgan, NAHB, NAR, NFIB, NY Fed, Markit, Philadelphia Fed, Standard & Poor's, University of Michigan, US Treasury

Focus: manufacturing perks up

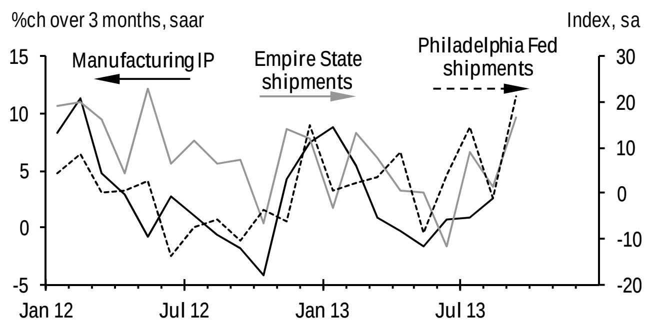
- The most recent round of manufacturing indicators supported our view that the manufacturing is gaining some momentum after a soft patch earlier in the year. Manufacturing industrial production popped up 0.7% in August after declining 0.4% in July, and before the August increase, it was up only slightly over the six months through July (+0.3% saar). Much of the July-August swing in production was due to the auto sector, but a similar trend in the data showed up when excluding motor vehicles and parts. Away from motor vehicles and parts, manufacturing IP also increased only 0.3% saar over the six months through July before increasing 0.4% samr in August.
- Most details in the September Empire State and Philadelphia Fed manufacturing surveys point to continued growth in the manufacturing sector. Although the headline for the Empire State survey (reflecting general business conditions) slipped from 8.2 to 6.3 in September, its ISM-weighted composite rose from 50.8 and 52.4 and included increases in its new orders and shipments measures. The Philadelphia Fed survey was even more upbeat in September—its headline jumped from 9.3 to 22.3 and its ISM-weighted composite surged from 48.8 to 55.0 including large gains in orders and shipments.
- The flash PMI for September released on September 23 will be the first look at manufacturing activity at the national level during the month. Of the Empire State, Philadelphia Fed, ISM survey, and PMI, the PMI has typically been the most reliable survey regarding some of the hard manufacturing data. The table on the right shows regression results testing how the survey data predict manufacturing IP, core capital goods shipments, core capital goods orders, and manufacturing payrolls since the start of 2012 (using corresponding survey data on shipments/production/output, new orders, and employment). Manufacturing IP and core capital goods shipments are typically most accurately predicted by the PMI data, followed by the Empire State data, the Philadelphia Fed data, and lastly the ISM data. Core capital goods orders are also best predicted by the PMI data, with the other survey data having basically no predictive power. The PMI also has the most predictive strength for the change in manufacturing payrolls, trailed by the Philadelphia Fed survey, the Empire State survey, and then the ISM.
- The results of these regressions generally weakened extending the sample back to 2010, but the PMI is still typically the most reliable indicator over this extended time frame.
- In addition to the available survey data, auto production schedules (not shown) also point to increases in manufacturing ahead. Schedules from IHS show auto production in creasing about 10% saar in 3Q while schedules from Wards (which we believe to be less reliable) show a more modest, but decent 4% increase during the quarter.

Manufacturing survey composite measures



Source: NY Fed, Philadelphia Fed, ISM, Markit

Manufacturing production and regional survey shipments measures



Source: Federal Reserve Board, NY Fed, Philadelphia Fed

Manufacturing survey regression results (sample starting 2012)

	coef.	t-stat	r-squared
Manufacturing industrial production (%3m saar)			
Empire State	0.19	2.01	0.18
Philadelphia	0.20	1.79	0.15
ISM	0.20	0.84	0.04
PMI	1.15	2.88	0.33
Core capital goods shipments (%3m saar)			
Empire State	0.33	2.26	0.23
Philadelphia	0.31	1.78	0.16
ISM	0.34	0.84	0.04
PMI	1.98	3.61	0.43
Core capital goods orders (%3m saar)			
Empire State	0.01	0.02	0.00
Philadelphia	0.10	0.17	0.00
ISM	0.43	0.37	0.01
PMI	3.39	1.83	0.17
Manufacturing payrolls (m/m, 000s)			
Empire State	0.41	0.98	0.05
Philadelphia	1.19	2.04	0.19
ISM	2.60	1.48	0.11
PMI	5.21	2.26	0.22

Source: J.P. Morgan

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Euro area

- **Next week's flash PMI an important test of the recovery; we expect a 0.5pt increase to 52.0**
- **We push back our expectation of a two-year LTRO from December to 1Q14**
- **While IP was weak in July, consumer spending indicators are holding up well so far in 3Q13**

Next week's flash PMI will give an important update on the momentum in the Euro area economy. The PMI increased strongly through to August, but the July IP reports have been weak across the region, raising some concern. We think that any IP-related disappointment will be confined to 3Q13 and should be viewed in conjunction with the upside GDP surprise in 2Q13. But, it will nevertheless be important that the PMI reinforces the sense of an underlying uptrend in the economy. We expect an increase of 0.5pt to 52.0 in next week's report for September, which would provide this trend.

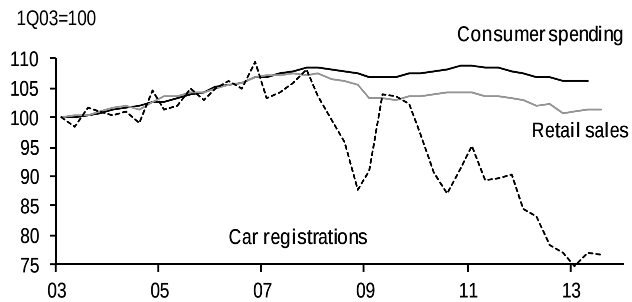
In terms of ECB policy, the Fed's decision to not taper its asset purchases has taken a bit of pressure off the ECB to reinforce its own guidance in the near term by narrowing its interest rate corridor or by injecting more liquidity. Hence, we have pushed back our call for a two-year LTRO from December to 1Q14. While the Fed's decision has led to a stronger euro exchange rate, we think the net effect on financial conditions has been positive. This will allow the ECB to wait a bit longer. One risk is that recent LTRO repayments have been surprisingly rapid, which could put upward pressure on Eonia rates and prompt an earlier intervention by the ECB.

Consumer spending is holding up

While the IP data were weak in July, the news about consumer spending has been good. Retail sales data for July have been available for a while, but the German data have been revised up this week. The decline reported in Germany is still big, with July down 4% annualized on the 2Q13 average, but that is nevertheless better than the 6.4% ar decline that was initially reported. The revised German data have not yet been incorporated into the Euro area series, but the effect is that Euro area retail sales should track a small increase in 3Q13 of around 0.5% annualized (compared to flat before).

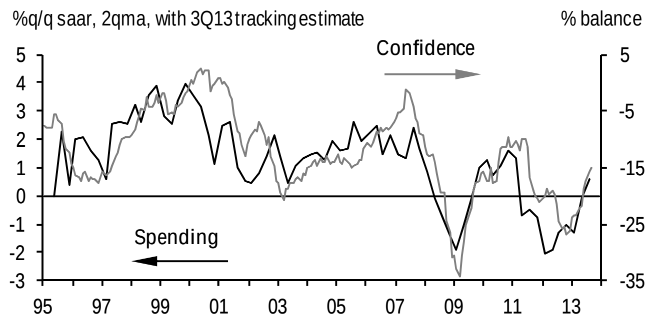
In addition, new data on car registrations and consumer confidence have been positive this week. Car registrations fell 1.2%m/m in July and rose 0.8%m/m in August, according to the ECB's seasonally and calendar adjusted data, with the July/August level down just 1% annualized relative to the 2Q13 average. This comes after a 12%q/q saar increase in 2Q13. Hence, since the start of the year, car registrations have recovered slightly, even if the recent trend has flattened again. In contrast, consumer confidence is recovering more clearly, rather than just stabilizing. In the flash report for September, confidence rose 0.7pt to -14.9, which is now very close to the long-run average.

Level of Euro area consumer spending



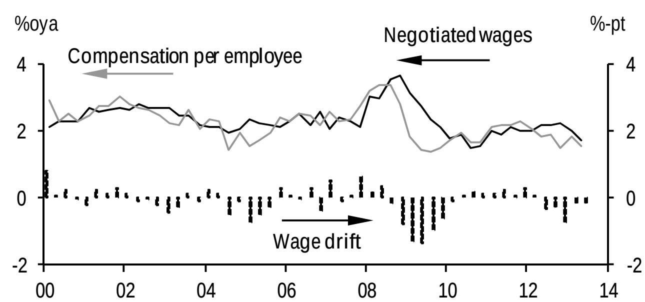
Source: Eurostat, ECB, J.P.Morgan

Euro area consumer confidence and spending



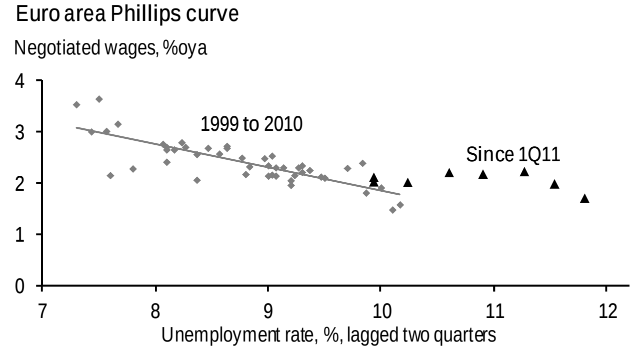
Source: European Commission, Eurostat, J.P.Morgan

Euro area wages and wage drift



Source: ECB, Eurostat, J.P.Morgan

Euro area Phillips curve



Source: ECB, J.P.Morgan

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Overall, our tracking tool for consumer spending suggests that spending could post another increase in 3Q13, after having already grown 0.7%q/q saar in 2Q13. Taking into account the recent tracking errors, an increase of 0.5%q/q saar looks plausible. This would be a bit better than expected.

Labor costs softened in 2Q13

Data on labor costs are now available for 2Q13. Negotiated wage growth softened from 2.0%oya in 1Q13 to 1.7%oya in 2Q13. By country, this slowing was broadly based. In Germany, negotiated wage growth slowed from 2.9%oya to 2.2%oya, although this mostly reflected the timing of new deals, so a pickup is likely again in 2H13. In France, the slowing has been much more modest, and in Italy, wage growth has been quite stable at 1.4%oya. In Spain, a more pronounced deceleration has taken place, with negotiated wages growing at only a 0.6%oya pace now, compared to 1.7%oya last year.

These trends are also reflected in the data on compensation per employee, which measure effective wages (i.e., they take into account the wage drift associated with changes in hours worked per employee, overtime payments, bonus payments, etc.). These effective wages are stagnating in Spain, growing relatively modestly in Italy and more rapidly in France. Since effective wages are rising in Germany, Spain and to a lesser extent Italy are still making a relative adjustment in their labor costs, while this is still not the case in France.

Overall, there seems to be considerable stickiness in wage setting, considering that the Euro area unemployment rate averaged 12.1% in 2Q13. Hence, there still seems to be a break in the historical Phillips curve relationship. This could just reflect lags that are longer than usual, in which case the recent slowing in wage growth may have a bit further to go. But, it could also simply point to nominal rigidities or a structural deterioration in the labor market (with a higher natural rate of unemployment). The measure of effective wages from the national accounts sends a similar message. Compensation of employees has slowed somewhat, but was still up 1.5%oya in 2Q13 on a per employee basis. This implies that wage drift is only slightly negative at present in the Euro area.

What does this mean for the inflation outlook? Unit labor costs grew 1.6%oya last year, and this slowed to 1.0%oya in 2Q13, mainly because the economy returned to growth (which led to an increase in labor productivity). However, firms used this deceleration in unit labor costs to increase their profit margins. In fact, the net effect has been to push up the GDP deflator, which is a broad measure of the prices of domestically produced goods. The GDP deflator rose solidly in 2Q13 (2.1%q/q saar and 1.8%oya). In effect, the slower growth of labor costs was more than offset by a jump in unit profits (5.9%q/q saar and 2.3%oya). Unit labor costs and unit profits often move in opposite directions and limit the overall cyclicality of the GDP deflator.

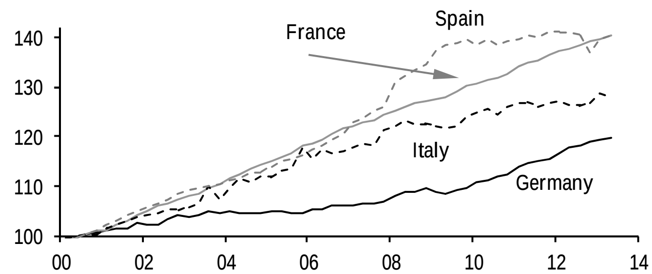
Of course, consumer prices have been growing more slowly, but according to the national accounts this owes much to falls in import prices. To the extent that this relates to slower energy price inflation and to the stronger currency, it could prove temporary. In terms of our forecasts for consumer prices, we expect Euro area HICP inflation to remain low in the coming quarters, but we do not expect a significant deceleration of core inflation. The stickiness in prices that is seen at the level of the GDP deflator and the underlying pricing behavior that is driving it are important in limiting the disinflationary pressures.

Negotiated wages in the Euro area
%oya

	00-08	09-10	2011	2012	1Q13	2Q13
Euro area	2.5	2.1	2.0	2.2	2.0	1.7
Germany	1.8	1.9	1.8	2.6	2.9	2.2
France	2.5	2.0	2.2	2.1	1.9	1.8
Italy	4.1	2.6	1.7	1.5	1.4	1.4
Spain	3.1	2.0	2.8	1.7	0.5	0.6
Netherlands	2.6	2.0	1.1	1.4	1.5	1.3
Belgium	2.7	1.6	2.7	3.0	2.4	2.0
Austria	2.4	2.5	2.0	3.3	2.9	2.6
Portugal	2.8	2.4	1.7	1.1	0.7	-

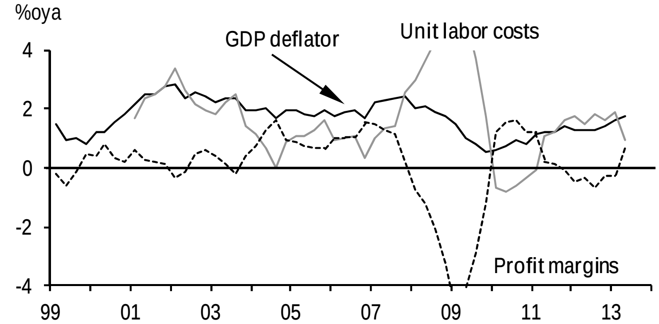
Source: ECB, national sources, J.P. Morgan

Compensation per employee
2000 = 100



Source: ECB, J.P.Morgan

Euro area unit labor costs and profit margins
%oya



Source: Eurostat, ECB, J.P. Morgan

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Data releases and forecasts

Week of September 16 – 20

Output and surveys

Purchasing managers index flash (manufacturing)

		Jun	Jul	Aug	Sep
Mon	Euro area				
Sep 23	Overall region	48.8	50.3	51.4	52.0
10:00am					
9:30am	Germany	48.6	50.7	51.8	
9:00am	France	48.4	49.7	49.7	

Purchasing managers index flash (services)

		Jun	Jul	Aug	Sep
Mon	Euro area				
Sep 23	Overall region	48.3	49.8	50.7	51.5
10:00am					
9:30am	Germany	50.4	51.3	52.8	
9:00am	France	47.2	48.6	48.9	

Purchasing managers index flash (composite)

		Jun	Jul	Aug	Sep
Mon	Euro area				
Sep 23	Overall region	48.7	50.5	51.5	52.0
10:00am					
9:30am	Germany	50.4	52.1	53.5	
9:00am	France	47.4	49.1	48.8	

We expect the Euro area composite PMI to improve further to 52.0 in September, reflecting the fading headwinds. In August, the PMI details were positive. In manufacturing, orders had increased strongly while the inventory indices fell overall, creating some upward pressure on the output index for September. And, by country, the PMI increases have been broadly based. There is some risk of payback in the periphery, given that the jump in August was large and the level is elevated. But, the French PMI may provide an offset as it had unexpectedly declined in August, with the level still low. Finally, Germany may improve a bit further. In terms of our Euro area forecast, the PMI needs to improve further to become consistent with a 1.5%q/q saar pace of growth next year. But, for 2H13, it is already close to the required level.

European Commission survey

		Jun	Jul	Aug	Sep
Fri	Euro area				
Sep 27	% balance of responses, sa				
11:00am	Industrial confidence	-11	-11	-8	
	Economic confidence	91.3	92.5	95.2	
	Recent production trend	-11	-8	-4	
	Production expectations	1	2	5	
	Export order books	-24	-24	-21	
	Stocks of finished products	6	6	4	
	Selling-price expectations	-3	-1	-1	
	Construction confidence	-32	-33	-34	
	Retail confidence	-15	-14	-11	
	Service confidence	-9.6	-7.8	-5.3	
	Consumer confidence	-18.8	-17.4	-15.6	

We expect Euro area economic sentiment to improve further in September, matching the gain we expect for the PMI. This would confirm the return to growth that reflects the fading of key headwinds in the region. The country details will also be important. In recent months, the improvements have been broadly based in the region, with the periphery also improving strongly.

National business surveys

		Jun	Jul	Aug	Sep
Tue	German IFO survey				
Sep 24	2000=100, sa				
10:00am	Business climate	105.9	106.2	107.5	107.7
	Business expectations	102.5	102.4	103.3	104.0
	Current conditions	109.4	110.1	112.0	112.0
Wed	French (INSEE survey - manufacturing)				
Sep 25	Index				
8:45am	Composite index	93	95	98	
	Index of past production	-5	1	5	
	Expected output - personal	-1	2	3	
	Expected output - general	-41.0	-30.1	-18.6	
Fri	Italy (ISAE survey)				
Sep 27	2000=100, sa				
9:30am	Producer confidence	90.6	91.8	92.9	
Tue	Belgium (BNB survey)				
Sep 24	% balance of responses, sa				
3:00pm	Overall	-12.8	-12.0	-8.6	
	Manufacturing	-15.6	-13.8	-9.8	
	Commerce	-18.7	-17.1	-14.1	
	Construction	-8.0	-8.9	-8.6	

The German IFO has been more elevated than the German PMI and may therefore improve by less in September. It is however already at an above-average level and therefore close to the level needed for our growth forecast.

Real GDP

		3Q12	4Q12	1Q13	2Q13
Fri	France				
Sep 27	%q/q sa	0.2	-0.2	-0.2	
7:30am	%q/q saar	0.6	-0.7	-0.6	
	%oya	0.0	-0.3	-0.5	
	GDP components (%q/q saar)				
	Private consumption	0.6	0.3	-0.2	
	Government consumption	1.5	1.6	1.4	
	Fixed investment	-2.2	-3.2	-3.8	
	Exports	0.9	-2.7	-2.1	
	Imports	-0.5	-4.8	0.3	
	Contribution to GDP growth (%q/q saar)				
	Domestic final sales	0.3	0.0	-0.5	
	Inventories	-0.8	-1.3	0.6	
	Net trade	-6.0	0.7	-0.7	

Source: Eurostat, European Commission, ECB, FSO, IFO, INSEE, ISAE, INE, BNB, Markit, and J.P. Morgan

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Demand and labor markets

	Consumer confidence (final)	Jun	Jul	Aug	Sep
Fri	Euro area (European Commission survey)				
Sep 27	% balance of responses				
11:00am	Consumer confidence	-18.8	-17.4	-15.6	-14.9

Euro area consumer confidence likely rose further in September, in line with the flash estimate. This suggests that consumer spending is rising modestly in the region.

Inflation

	Consumer prices	Jun	Jul	Aug	Sep
Fri	Germany (prelim)				
Sep 27	%m/m nsa	0.1	0.5	0.0	0.1
8:00am	%oya	1.8	1.9	1.5	1.5
	HICP (%oya)	1.9	1.9	1.6	1.6
	Baden Wuerttemberg (%oya)	1.7	1.7	1.4	1.3
	Bavaria (%oya)	1.8	1.8	1.4	1.4
	Brandenburg (%oya)	1.7	1.6	1.5	1.5
	Hesse (%oya)	1.6	1.7	1.1	1.2
	North-Rhine West (%oya)	2.1	2.1	1.6	1.6
	Saxony (%oya)	2.0	2.0	1.6	1.6
Fri	Spain (flash)				
Sep 27	HICP (%oya nsa)	2.2	1.9	1.6	0.9
9:00am					
Fri	Belgium CPI				
Sep 27	%m/m nsa	0.2	0.1	-0.1	
11:15am	%oya nsa	1.6	1.5	1.0	

After a substantial fall in August due to a lower level of energy price inflation, headline inflation is likely to remain stable in Germany. But this stability is likely to be short-lived. There is virtually no slack in Germany, as evidenced by the very tight labor market, and core inflation is expected to increase by the end of the year, in our view. A rebound in energy price inflation should also occur if oil prices remain at their current level.

Financial activity and public finance

	Money and credit data	May	Jun	Jul	Aug
Thu	Euro area				
Sep 26	M3 (%m/m sa)	0.3	-0.4	0.5	
10:00am	M3 (%oya)	2.9	2.4	2.2	
	M3 (%oya 3mma)	2.9	2.8	2.5	
	Loans (%oya)[1]	-0.7	-1.0	-1.4	
	Loans (m/m, € bn)[1]	-27.3	-43.7	-37.9	

1. Loans to nonbank private sector, adjusted for securitization

While Euro area M3 has held up relatively well, bank loans were very weak in July. Loans to nonfinancial corporates fell sharply again, while those to households have been stagnating. The ECB continues to view much of this as reflecting weak demand, rather than supply restrictions that it cannot do much about. In terms of the ECB's forward guidance, we expect the money and credit data to remain weak enough not to provide a challenge.

Review of past week's data

Demand and labor markets

Consumer confidence (prelim)

	Jul	Aug	Sep	
Euro area (European Commission survey)				
% balance of responses				
Cons confidence	-17.4	-15.6	~~-15.0~~	*-14.9*

External trade and payments

Foreign trade

	May		Jun		Jul
Euro area					
€ bn, sa					
Trade balance	~~13.8~~	*13.5*	~~14.9~~	*13.5*	*11.1*
year earlier	~~5.6~~	*6.5*	~~8.7~~	*8.0*	*7.1*
Exports	~~155.4~~	*156.4*	~~160.0~~	*158.4*	*155.9*
%m/m sa	~~-2.6~~	*-2.1*	~~3.0~~	*1.3*	*-1.6*
Imports	~~141.6~~	*142.9*	~~145.2~~	*144.9*	*144.8*
%m/m sa	~~-2.1~~	*-1.2*	~~2.5~~	*1.4*	*-0.1*

Inflation

Consumer prices

	Jun	Jul	Aug
Euro area (final)			
HICP (%m/m nsa)	0.1	-0.5	*0.1*
HICP (%oya nsa)	1.6	1.6	*1.3*
HICP (%oya, core-X)[1]	1.3	1.3	*1.3*
HICP (%oya, core-XX)[2]	1.2	1.1	*1.1*
HICP (%m/m, ex tob.)	0.1	-0.6	*0.1*

1. Excluding unprocessed food and energy.
2. Excluding food, alcohol, tobacco, and energy.

The fall in Euro area inflation was confirmed in August. The details did show that a substantial decline in energy price inflation was largely responsible for this. Meanwhile, core inflation remained stable at 1.1%oya, and food price inflation moved down by a few tenths. The picture in the medium term is one in which the level of core inflation is set to decline further, but only by a small amount, in our view. The level of slack in the region is large, as evidenced by the high level of unemployment, which exerts downward pressure on core inflation. On the other hand, nominal rigidities are likely to limit the impact of slack on inflation.

The downward pressure on inflation is also evident when looking at labor cost data. For the Euro area as whole, the pace of the rise in labor costs has declined significantly since 2011. In 2Q13, the rate of increase in labor costs was 0.4%q/q saar, which compares with a rate of increase of 1.6%q/q saar on average in 2012. This decline is important when looking at wages and salaries; these increased only 0.7%q/q saar in 2Q13, while the rate of increase was 1.7%q/q saar on average in 2012.

Source: Eurostat, European Commission, ECB, FSO, IFO, INSEE, ISAE, INE, BNB, Markit, and J.P. Morgan

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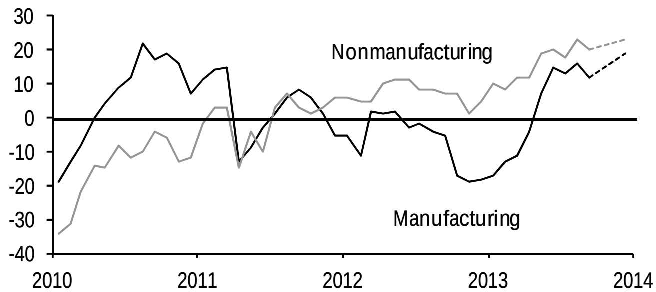
Japan

- **Large firms' sentiment dipped in September, but December outlook anticipates an improvement**
- **Real exports reversed in August, showing an uptrend, although net trade likely will weigh on 3Q GDP growth**
- **Public investment is booming in 3Q**

Reuters Tankan large firms' business conditions

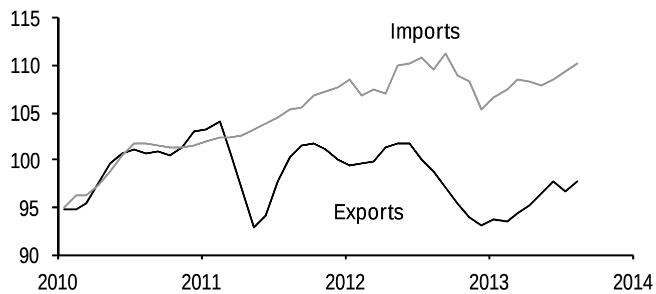
DI, dotted lines show December outlook



Source: Reuters

BoJ real exports and imports

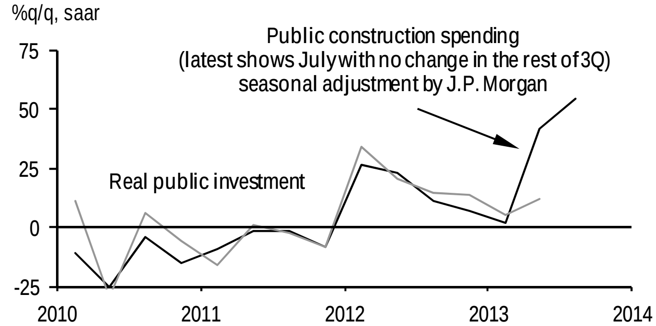
2010=100, sa



Source: BoJ

Public construction spending and real public investment

%q/q, saar



Source: MLIT, Cabinet Office, J.P. Morgan

This summer the Japanese economy appears to have moderated, with exports and private consumption slowing after they boomed in 1H. The latest September large firms' sentiment survey in the monthly Reuters Tankan shows that the current state of business conditions (not the outlook) worsened somewhat in both manufacturing and nonmanufacturing from the recent peak in August, leaving the 3Q averages of both sentiment indices higher than those in 2Q, but showing a smaller increase than in the previous quarter. Real exports jumped 6.4%m/m sa in August, more than reversing the unexpectedly large 4.9% decline in July; however since imports continue to increase steadily, the net trade contribution to 3Q real GDP growth will likely turn into a drag from the boost in 1H. This combination of soft exports and solid imports is one reason why we lowered our 3Q growth forecast to 2.3%q/q saar last week.

However, we are still optimistic on near-term growth. In fact, the December outlook in the Reuters Tankan showed another improvement, suggesting that the positive momentum is intact. The trend in exports, while easing to a 5% annualized gain on a 3m/3m sequential basis in August from 15% in June, remained in positive territory. With the expected firming in the global manufacturing cycle, we think the drag from net trade will be smaller in coming quarters.

At the moment, we think the key driver of growth is probably public and private investment. The former is confirmed by strong public construction spending in July. In our seasonal adjustment, spending continued to increase in July, marking average monthly growth of 5.5%m/m sa since May. The July level of spending was unsustainably high; even assuming no change in August and September, the pace of increase in 3Q (55%q/q saar) would outpace that in 2Q (42%). While it still looks too high relative to the GDP-based public investment, the acceleration from 2Q looks quite likely. Our forecast looks for a 20% gain in GDP-based public investment, but the risk is skewed to the upside.

There is no news on private investment from data this week. Still, the latest developments in financial markets, especially firming equity prices and lower interest rates, should be favorable for business sentiment and capex, although it is difficult to quantify this impact. Moreover, within a couple of weeks (probably on October 1), the prime minister is expected to announce the final decision on implementing the consumption tax rate rise scheduled for April next year, with specific measures to cushion the pain. While the details are still uncertain, it looks quite likely that the measures would include tax breaks for new capex. Capex is likely to continue growing, but the strength of that growth is uncertain. The August IP report (capital goods shipments) and the BoJ quarterly Tankan (capex plan and assessment of own production capacity), which will be released in the first week of October, are worth watching to gauge the strength in capex and the direction of the economy.

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Data releases and forecasts

Week of September 23 – 27

Wed
Sep 25
8:50am

Corporate service prices

%oya

	May	Jun	Jul	Aug
Overall	0.3	0.4	0.4	0.4
Ex international transport	-0.2	-0.1	-0.1	

Wed
Sep 25
2:00pm

Shoko Chukin small firm survey

Diffusion index

	Jun	Jul	Aug	Sep
Sentiment index	49.6	49.4	49.7	49.0
Manufacturing	48.7	48.2	48.4	
Nonmanufacturing	50.4	50.4	50.7	

The latest Reuters Tankan large firm survey suggests that the business conditions worsened temporarily this month, and we expect this survey to follow suit.

Fri
Sep 27
8:30am

Consumer prices

%oya

	Jun	Jun	Aug	Sep
Tokyo				
Overall	0.0	0.4	0.5	0.4
Core (ex fresh food)	0.2	0.3	0.4	0.3
Ex food and energy	-0.4	-0.4	-0.4	-0.3
Nationwide				
Overall	0.2	0.7	0.7	
Core (ex fresh food)	0.4	0.7	0.7	
Ex food and energy	-0.2	-0.1	-0.1	

The previous September report raised the possibility that the underlying trend in consumer prices is gradually exiting deflation at a faster pace we had been thinking.

Review of past week's data

Construction spending (Sep 17)

%oya

	May	Jun	Jul
Public	12.9	19.3	*25.8*
Private	8.9	11.5	*11.5*

Public works contracts

	Jun	Jul	Aug
%oya nsa	21.7	29.4	*7.9*
%m/m sa by J.P. Morgan	-7.5	7.5	*-10.8*
%m/m sa, 6mma	3.0	4.3	*1.8*

Public construction spending in July, after our seasonal adjustment, marked a level 92.7% annualized above the average in 2Q, when it rose 41.9% ar. The 6-month moving average of public works contracts, a forward-looking indicator, has maintained a solid uptrend since earlier this year through the latest August report. The risk to our 3Q GDP public investment forecast, which looks for a further acceleration to +20.0%q/q saar (from +12.7% in 2Q and +5.8% in 1Q) on a boost from the supplementary budget, is now skewed to the upside.

Reuters Tankan survey (Sep 19)

Diffusion index

	Jul	Aug	Sep
Manufacturing	13	16	*12*
Nonmanufacturing	18	23	*20*

Both the large manufacturing and the large nonmanufacturing DIs fell in September, but with expectations for a solid recovery in the coming three months (the manufacturing outlook DI posted 19, while the nonmanufacturing outlook DI marked 23). We think that upward momentum in corporate sentiment has maintained the underlying trend.

Worsening in manufacturing sentiment in September reportedly reflected soft sales overseas; this was offset by a boost to yen-denominated profits from the weak yen, plus the price rises in energy and materials. As for nonmanufacturing, real estate/construction and information/communication remained very good. Retail trading reported a material worsening in business conditions this month, but is expected to recover robustly by the end of this year.

Customs-cleared international trade (Sep 19)

%m/m sa, unless noted

	Jun		Jul		Aug	
Balance (¥ bn sa)	~~-663~~	*-643*	~~-944~~	*-911*	~~-932~~	*-791*
Exports (%m/m sa)	~~0.9~~	*0.8*	~~-1.8~~	*-1.5*	~~0.8~~	*2.2*
Imports (%m/m sa)	-1.5		2.7		~~0.5~~	*0.1*
Balance (¥ bn nsa)	-182		-1028		~~-1252~~	*-960*
BoJ real export index	2.0		-4.9			*6.4*
BoJ real import index	3.1		~~-1.6~~	*-1.7*		*1.3*

The details of the customs trade data on exports, which are in yen-denominated terms, were generally upbeat. Exports to the US increased for the first time in three months (marking +3.0%m/m sa after -4.4% and -4.2%). Exports to Asian countries also showed a solid China-led rebound in the month (marking +2.5%m/m sa after -3.0% and -1.3%). Meanwhile, exports to EU countries, where the recession appears to have just ended, maintained a recovering trend (marking -0.3%m/m sa after +2.5% and +4.5%). For exported goods, the latest rebound was broadly based. For example, auto exports rose 4.1%m/m sa following a total 10.8% drop in the previous three months (see also main essay).

Nationwide department store sales (Sep 20)

	Jun	Jul	Aug	
Overall, %oya	7.0	-2.8	~~2.5~~	*2.3*
%m/m sa by J.P.Morgan	5.4	-11.2	~~5.8~~	*5.6*
Same stores, %oya	7.2	-2.5		

The result was broadly consistent with our view that the weakness in consumption at the start of this quarter was exaggerated due to the early start of summer clearance sales at the end of June (instead of early July) and a drag from bad weather (heavy rains and extremely high temperatures).

Source: Statistics Bureau, BoJ, Shoko Chukin Bank, MLIT, Reuters, MoF, Japan Department Stores Association, East Japan Construction Surety

Canada

- **Key activity data point to solid start to 3Q13**
- **Manufacturers' and wholesale sales pick up in July**
- **Prospect of higher mortgage rates sends existing home sales higher**
- **CPI inflation remains modest**

Key activity data released this week are pointing to a robust start to 3Q13. The activity data in July are looking strong, and a bounce back in July real GDP seems certain after the unusual collapse in June (-0.5%m/m) that was mostly due to temporary factors. The improvement in the manufacturing sector was the highlight this week, kicking off third-quarter output on a high note. Manufacturing shipments rebounded 1.7%m/m in July after a smaller than first reported 0.1%m/m decrease in June. And with inventories gaining 0.4%m/m, the production implications of the report were even more positive. Wholesale sales were also up strongly, rebounding 1.5%m/m following a 3.1% decline in June. With our expected increase in July retail sales (released next week), we anticipate a solid 0.4%m/m pickup in real GDP in July. As expected, the adverse effects of flooding in Alberta and the Quebec construction strike during June faded quickly. At the consumer level, Canadians bought more new cars in July and existing home sales are up over 28% saar in 3Q (as of August). BoC governor Poloz gave a speech this week in which he spoke very optimistically about signs that the Canadian economy will soon be growing at potential, and he anticipates that the two sectors that have been lagging in Canada's recovery thus far—exports and business investment—are about to turn a corner.

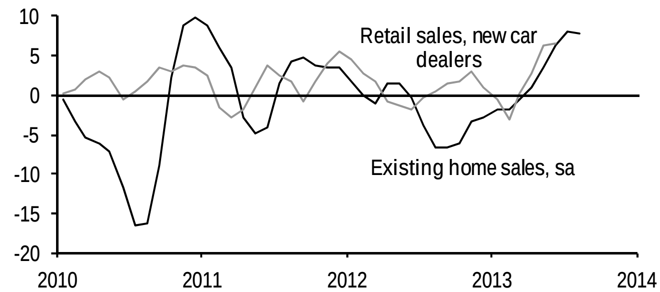
Manufacturers' and wholesale sales higher in July

The July manufacturers' shipments report showed a solid gain, increasing 1.7%m/m. Underlying growth was even stronger than the headline indicated, as a large decrease in aerospace production (which is quite volatile) held down the increase—excluding aerospace, manufacturing shipments were up 3.2%. Almost all of the decrease in aerospace was offset by a 2.4%m/m increase in shipments of motor vehicles and parts—the largest rise since February. Inventories of motor vehicles and parts were also up notably (7.2%m/m).

Rising volumes accounted for most of the increase in July, as real sales were up 1.1%m/m in the month. Higher prices did boost energy sector shipments, however. Manufacturers' orders were down 1.7% in July, but that was due primarily to a decline in orders for aerospace and parts. Behind the weakness in total orders were very impressive gains in orders

Existing home sales and new car sales

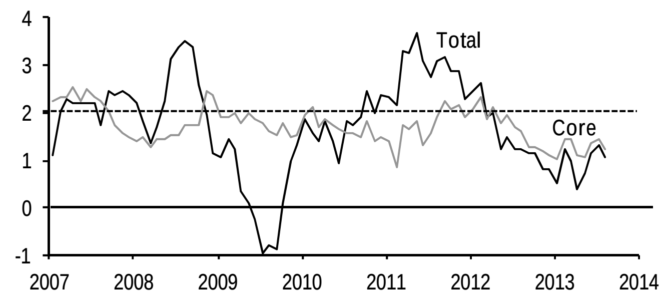
%ch over 3 months in a 3 month moving average



Source:Statistics Canada

Consumer prices

%oya



Source:Statistics Canada

for many durable goods categories like machinery (+22.4%m/m) and motor vehicles and parts (+5.8%m/m). Those solid gains in new orders are likely to provide sustained support to manufacturing production throughout the third quarter.

Wholesale sales were up 1.5% in July following a 3.1%m/m decline in June. Highlighting the report were higher sales of machinery, equipment and supplies, and building materials and supplies. In volume terms, wholesale sales were up 1.4%m/m in July.

With manufacturing and wholesale sales increasing in July, and our expected rebound in July retail sales of 0.6%m/m samr, the key activity data are pointing to a sizable recovery in July real GDP from the June collapse (-0.5%m/m). Monthly output in June was adversely affected by the flooding in southern Alberta and even some parts of Ontario and a province-wide construction strike in Quebec. Service sector output was particularly disrupted, and was down 0.3%m/m in June, the largest decrease since December 2008. Hints of replacement and reconstruction spending seemed apparent in the July activity data.

Existing home and new auto sales pick up

Existing home sales increased 2.8%m/m in August, translating to an 11.5% increase from a year earlier. That over-year-ago gain is tempered by the fact that sales were off sharply last August after tighter mortgage regulations were implemented by the Canadian government in July 2012. The Canadian Real Estate Association noted that the August strength "likely reflects the transient influence of buyers with pre-approved financing making purchases before their lower pre-approved rates expire, particularly in some of Canada's most active and expensive housing markets." Buyers have apparently been rushing in to buy seeing the prospect of higher interest rates on the horizon. The level of sales has now reversed all of its losses of the late 2012 slump and now stands at an almost two-year high. But with the uptrend in mortgage rates, a slowdown in sales is likely ahead.

New motor vehicle sales rebounded 2.0% samr (sa by J.P. Morgan) in July after a 4.2% samr (sa by J.P. Morgan) decrease in June. It's likely that retail sales of autos in June were held down by the flooding and the strike.

Inflation remains modest

Headline CPI was flat m/m nsa in August after a 0.1%m/m increase in July. Compared to a year ago, the headline CPI was up 1.1%oya versus 1.3% in July. Shelter costs were the major factor behind the annual inflation reading as consumers paid more for rent and natural gas. But mortgage costs, also part of shelter costs, were down 3.6%oya. Mortgage costs, which have not seen a positive over-year-ago increase since June 2009, have been restraining inflation throughout the recovery. Gasoline prices, which bounced back in June and July after negative readings in the early spring, were up more moderately in August. On a year-over-year basis, gasoline prices were up 2.2%. The seasonally adjusted headline CPI edged up 0.1%m/m in August, matching the increase in July. Over the six months to August the seasonally adjusted headline is up a very mild 0.33% ar. The BoC core inflation reading remained moderate, increasing 0.2%m/m nsa following no change in July. The rate was down 1.3%oya in August compared with 1.4%oya in July. The BoC core has not been above 1.4%oya since August 2012.

Data releases and forecasts

Week of September 23 – 27

Tue
Sep 24
8:30am

Retail sales
%m/m sa, unless noted

	Apr	May	Jun	Jul
Total	0.2	1.8	-0.6	0.6
%oya	1.7	3.3	3.1	3.0
Ex autos	-0.2	1.1	-0.8	0.3
%oya	0.8	1.5	1.1	0.9
Ex autos & gasoline	0.2	1.1	-1.0	0.2
%oya	1.5	1.9	1.0	0.9
Real retail sales	0.6	1.7	-1.2	0.7
%oya	2.3	3.1	1.9	2.0

Review of past week's data

Manufacturing report (Sep 17)
%m/m sa, unless noted

	May		Jun		Jul	
Sales	~~-0.6~~	*0.9*	~~-0.5~~	*-0.1*	~~-0.7~~	*1.7*
New orders	1.6		~~-2.5~~	*3.2*	~~-1.0~~	*-1.7*
Unfilled orders	~~-0.6~~	*0.5*	~~-2.7~~	*2.8*	~~-1.0~~	*0.4*
Inventories	~~-0.4~~	*-0.3*	~~-0.2~~	*-0.1*	~~-0.5~~	*0.4*
Inventory-shipments ratio	~~1.42~~	*1.41*	~~1.42~~	*1.41*	~~1.42~~	*1.40*

Wholesale sales (Sep 19)
Sa

	May		Jun		Jul	
Total, %m/m	~~-2.2~~	*2.3*	~~-2.8~~	*-3.1*	~~-0.8~~	*1.5*
%oya	~~-0.7~~	*0.8*	~~-1.4~~	*-1.5*	~~0.1~~	*0.6*

Consumer price index (Sep 20)
%m/m nsa, unless noted

	Jun	Jul	Aug	
Total CPI	0.0	0.1	~~0.1~~	*0.0*
%oya	1.2	1.3	~~1.2~~	*1.1*
BoC core CPI	-0.2	0.0	*0.2*	
%oya	1.3	1.4	*1.3*	
Ex food & energy	-0.1	-0.1	*0.0*	
%oya	0.9	1.1	*0.9*	
CPI-XFET (%oya)	0.9	1.1		*0.9*

Source: Statistics Canada

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Mexico

- **Growth disappointment weighed heavily in the policy decision to cut the reference rate to 3.75%**
- **Less concern regarding policy rotation in the US validates the looser approach to monetary policy**
- **We are now expecting an additional 25bp cut at the October 25 meeting**
- **In the meantime, economic activity continues to lack traction, with persistent slack in the labor market**

The minutes of the policy meeting held on September 6 confirmed that the board has become increasingly concerned regarding economic activity, while it continues to be confident that inflation dynamics will remain under control amid a gradual improvement in global economic conditions. The board stated that while economic conditions continue to improve in developed economies, with a special mention to Japan, Europe, and the US, emerging markets continue to lag, reflecting a non-homogeneous recovery in the global economy. Yet the disagreement within the board was related to the monetary policy rotation in the US and the financial stability implications of this change on Mexico's economy.

All members agreed that the US has continued to show improvement in contrast with the deceleration observed in the local economy while a majority of members stressed that economic slack has widened and the deceleration in the second quarter was more pronounced than expected. In fact, most members said that the rate of growth expected for this year will be considerably below the forecasts published in the most recent Quarterly Inflation Report released in the first half of August (back then, the board forecasted growth between 2.0% and 3.0% for 2013).

In terms of inflation, the board was also in agreement, with all members expecting that dynamics in core inflation would continue to be favorable, while the majority of members emphasized downside risk ahead due to economic slack, the lower than previously anticipated inflation impact of structural reforms, and stable inflation expectations.

However, once the board started to analyze the possibility of a rate cut, some opposing views emerged surrounding financial stability concerns from "tapering" risks. The board meeting took place on September 6, two weeks before the all-important FOMC monetary policy decision. As such, "some" board members favored a wait-and-see approach before making a decision to cut rates.

Output gap

% of potential GDP

Source: INEGI and J.P. Morgan

Banxico policy rate forecast

% p.a.

	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14
Previous	3.75	3.75	3.75	3.75	3.75	3.75
New	3.75	3.50	3.50	3.50	3.50	3.50

Source: J.P. Morgan

MXN forecast

EoP versus USD

	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14
Previous	13.10	12.75	12.50	12.25	12.10	11.90
New	12.40	12.60	12.50	12.25	12.10	11.90

Source: J.P. Morgan

Regarding this, one member said that while there were arguments for a rate cut, he preferred to wait before adopting an easier stance on monetary policy. Another member emphasized that "at this moment," moving in the opposite direction to the Fed could prompt capital outflows and further MXN weakness amid a persistent domestic economic deceleration. Yet, a majority of members said that considering the recent market stability, a cut in the Fondeo rate would only have limited impact in the context of increased global turbulence due to the policy rotation in the US.

In all, the split decision within Banxico's board was motivated by the prevailing "tapering" risk at the moment of the policy decision in early September rather than disagreements with respect to economic activity developments or inflation dynamics. Considering that on September 18 the FOMC decided to keep its asset purchase program unchanged, while at the same time downgrading its economic activity path, we believe Banxico will favor the continuation of an easier stance because of the prevailing negative output gap, stable inflation expectations, and the further tightening in monetary conditions derived from a stronger currency and higher mid- and long-term rates.

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Indeed, with financial concerns temporarily out of the picture, we believe Banxico's focus can fully turn to the slack economic conditions that are likely to prevail over the coming quarters. Following the GDP contraction in 2Q, the output gap turned markedly negative, and, according to our growth path, it is likely to remain in negative territory at least through 3Q14 (chart previous page). Banxico—likely placing potential growth slightly above our 3.3% estimate, and having a less upbeat outlook for growth in 2014—definitely shares this view, and most likely sees slack conditions lingering longer than we do (the labor report for August continued to show the stickiness in unemployment, as it increased marginally to 5.2% in August from 5.1% in July).

According to the September 6 statement of the central bank, core inflation—considered by Banxico the best gauge of underlying inflation—will remain subdued ahead "due to the absence of demand side pressure in the next 18 months," providing sufficient room to ease its policy rate by 25bp once again. Furthermore, as mentioned above, with MXN down significantly from the 13.40 high seen this year, and in anticipation of further strengthening in the short term, monetary conditions will become tighter, presenting additional support for a rate cut. Last, the fact that the fiscal reform proposed by the government should have less impact on inflation than anticipated should also make Banxico more comfortable as inflation expectations continue to stabilize.

We are expecting a single 25bp cut in the next meeting, bringing the reference rate to 3.50%, a new historical low. The next monetary policy decision will be announced on October 25. While we believe Banxico will keep the door open for further adjustments in October, the fact that fiscal policy is expected to turn expansionary, coupled with gradually improving data and re-emerging concerns about "tapering" later this year, should keep Banxico from reducing its policy rate by more than 25bp.

Data releases and forecasts

Week of September 23 – 27

Mon Sep 23 9:00am	Retail sales	Apr	May	Jun	Jul
	Retail sales				
	%oya	2.5	0.1	-1.9	0.7
	%m/m sa	-0.8	0.7	0.1	0.2

Tue Sep 24 10:00am	Central bank foreign reserves %m/m sa, unless noted	Aug 30	Sep 6	Sep 13	Sep 20
	Gross reserves	170.7	170.6	170.6	___

Tue Sep 24 9:00am	Consumer prices %oya	Jul 2H	Aug 1H	Aug 2H	Sep 1H
	%2w/2w	-0.02	0.26	0.07	0.23
	Core	-0.04	0.10	0.01	0.22
	%oya	3.42	3.54	3.37	3.35
	Core	2.44	2.38	2.35	2.45

Wed Sep 25 9:00am	Indicator of overall economic activity (IGAE) %oya, unless noted	Apr	May	Jun	Jul
	%oya	3.9	1.1	-0.4	1.1
	%m/m sa	-1.0	0.7	0.0	0.1

Thu Sep 26 9:00am	Trade balance	May	Jun	Jul	Aug
	Balance (US$ mn)	-470	856	-1,437	-1,604
	Exports (US$ bn)	32.8	31.0	32.2	33.6
	%oya	-0.9	2.5	6.3	6.1
	Imports (US$ bn)	33.3	30.2	33.7	35.1
	%oya	1.5	1.7	9.6	7.8

Review of past week's data

Central bank foreign reserves (Sep 18)
US$ bn

	Aug 30	Sep 6	Sep 13	
Gross reserves	170.7	170.6	___	*170.6*

Real GDP by type of expenditure (Sep 19)
%oya, real terms

	4Q12	1Q13	2Q13	
Supply & demand	4.5	0.2	~~2.2~~	*1.8*
Private consumption	5.0	2.5	~~2.4~~	*3.5*
Public consumption	1.3	0.1	~~0.2~~	*0.4*
Fixed investment	4.2	-0.8	~~0.4~~	*0.4*
Exports	3.0	-1.0	~~3.4~~	*2.7*
Imports	8.4	-0.9	~~4.1~~	*2.8*

Labor market report (Sep 20)
% of labor force

	Jun	Jul	Aug	
Unempl. rate	5.0	5.1	~~5.3~~	*5.2*
Sa	5.0	4.9	~~4.9~~	*4.8*

Source: Banxico and INEGI

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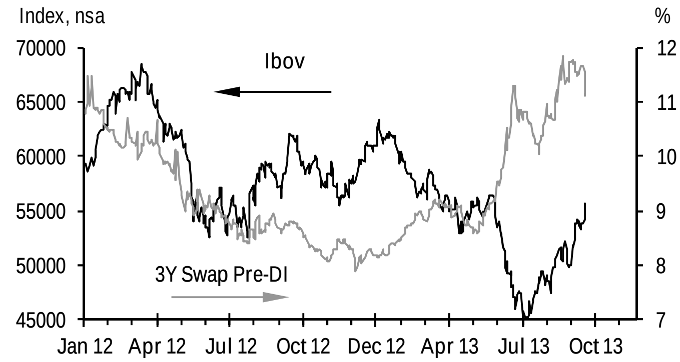
Brazil

- **Meaningful correction in financial assets after the FOMC surprise, but Brazilian authorities keep calm**
- **Continued financial relief could raise upside growth risks, but it is too early to tell, and data flow is choppy**
- **Inflation finally below 6%oya; watch FX movements for signals on inflation ahead**

We have been highlighting that the recent downward revisions in Brazil's GDP growth were a result of negative interactions between financial market jitters and social protests impacting business and consumer sentiment. If the improvement in financial conditions related to this week's no-tapering surprise from the US FOMC persists, it could start to raise upside risks to our current growth projections, especially for the last quarter of this year. But we are keeping the 2.3% forecast for this and next year intact, as more market stabilization is needed and the activity data flow remains too noisy. Indeed, following July's conflicting signals between IP (-2.0%m/m sa) and retail sales (+1.9%), August activity indicators (vehicles production, packaging industry, heavy trucks traffic, and others) are signaling a moderate expansion in manufacturing, but not one robust enough to generate a decisive shift in sentiment. Indeed, this week's preliminary September confidence indicators from FGV and CNI moved in opposite directions, with the former declining to a below-neutral level and the latter improving close to its position prior to the street protests. On the household side, it seems the worst is in the past as well, with the FGV consumer confidence index improving to pre-protests level, and the August CAGED survey pointing to formal job creation rising off the recent lows (May), though not at a pace conducive to a decline in the unemployment rate.

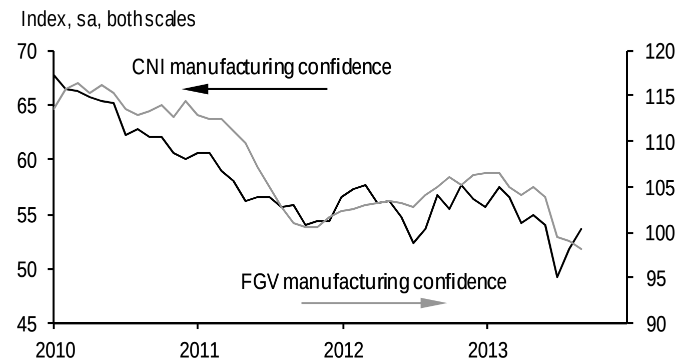
In terms of policy responses to the dovish surprise in the US, it seems authorities will not lower the guard soon. During the pronounced rally in Brazilian financial assets on Wednesday, Governor Tombini of the BCB avoided sending any signal that might interrupt the daily FX interventions on the back of the rally in BRL. Minister of Finance Mantega, however, mentioned that the BCB could well decelerate the daily auctions of FX swaps. In this context, a deceleration in the pace of intervention (while continuing to offer swaps on a daily basis) seems to be the first logical policy response. On the rates side, we think the current relief just trims the risk of the BCB tightening more than we are forecasting, and at this point we don't see it tightening less than the current projection of further hikes of 75bp, lifting the Selic rate to 9.75% by the end of this year. Indeed, Tombini reaffirmed that inflation remains at uncomfortable levels, and that the

Brazil: sell-off in financial assets



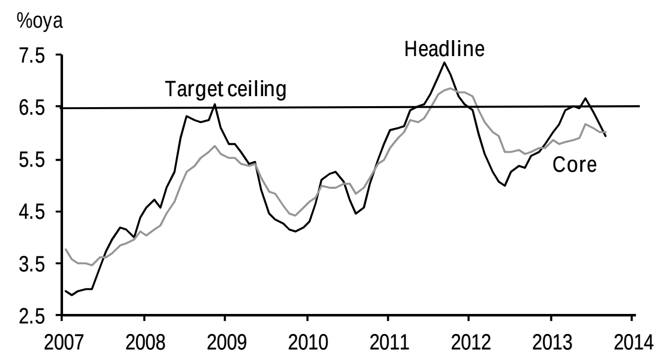
Source: Bloomberg

Brazil: manufacturing confidence



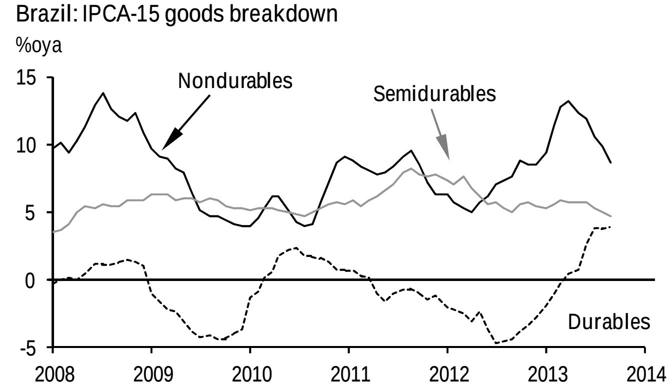
Source: FGV and CNI

Brazil: IPCA-15 headline and core measures



Source: IBGE and J.P. Morgan

Brazil: IPCA-15 goods breakdown



Source: IBGE

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BCB is "especially vigilant" to limit the FX depreciation pass-through to consumer prices.

IPCA-15 prints below 6%oya for the first time this year

This week, the IBGE released the September IPCA-15 (preview of IPCA) at +0.27%m/m—slightly lower than our call of +0.29% and market consensus (0.28%). That result led the over-year-ago reading to 5.93%—the first print below 6% this year—from 6.15% in August. The average of core measures sustained last month's level of 6%oya, after increasing 0.42%m/m in September. At the same time, diffusion of price hikes decreased to 59.5%, from 60.6% in August. Services prices increased 0.62% in the month (8.72%oya, from 8.6% in Aug) due to a 16%m/m increase in airfares, while durable goods prices grew 0.17% (steady at 3.8%oya) and non-durables prices decreased 0.13% (8.6%oya, from 9.8% previously). Market-driven prices continue to rise at a rapid pace (7.5%oya in September), but controlled prices, at 1.2%oya, are helping to bring headline inflation down. We forecast September IPCA at 0.32%m/m.

Even after the announcement of the BCB's USD swap program, we kept our BRL forecast for the end of 3Q13 at 2.45 due to risks from the US monetary policy decision. However, the Federal Reserve surprised with a more dovish-than-expected decision and the risks for a sell-off in BRL in the short term faded. Because of this, we revised our 3Q13 BRL forecast to 2.25. On the one hand, lower BRL reduces inflationary pressures at the end of the year; on the other hand, lower inflationary pressures would open room for the government to finally allow Petrobras to hike gasoline prices next month—we expect a 5% hike, even though the price gap has declined following BRL appreciation in the last few weeks. That said, despite the downward trend since June's IPCA-15 (6.7%oya), this month's IGPs (a mix of wholesale, consumer, and construction sector price indexes) are indicating initial upward inflation pressures from weaker BRL in July and early August. However, we see that this recent upward pressure from higher wholesale prices could be contained by recently improved BRL, and we are revising down the September IPCA to 0.33% because of Friday's print. Taking this into account, we maintain our forecasts for IPCA at 5.9% at the end of this year and at 5.7% in 2014.

Data releases and forecasts

Week of September 23 – 27

	Current account balance	May	Jun	Jul	Aug
Tue Sep 24 9:00am	Current account (CA)	-6.3	-4.0	-9.0	<u>-5.1</u>
	CA, 12-month sum	-72.8	-72.4	-77.7	<u>-79.9</u>
	CA, 12-month sum, %GDP	-3.2	-3.2	-3.4	<u>-3.5</u>
	Foreign direct investment	3.9	7.2	5.2	<u>4.2</u>

	Unemployment rate	May	Jun	Jul	Aug
Thu Sep 26 8:00am	Open rate, nsa (30 days)	5.8	6.0	5.6	<u>5.6</u>

	General prices (IGP-M)	Jun	Jul	Aug	Sep
Fri Sep 27 7:00am	%m/m	0.8	0.3	0.2	<u>1.39</u>
	%oya	6.3	5.2	3.9	<u>4.28</u>

Review of past week's data

General prices (IGP-10)	Jul	Aug	Sep	
%m/m	0.4	0.2	~~0.89~~	*1.05*
%oya	5.6	4.1	~~3.95~~	*4.12*

Consumer prices (IPCA-15)	Jul	Aug	Sep	
%m/m	0.1	*0.2*	~~0.29~~	*0.27*
%oya	6.4	*6.2*	~~5.95~~	*5.93*

Source: IBGE, BCB, FGV, and J.P. Morgan

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Argentina

- **The official peso is weakening at a 35% annualized pace**
- **We forecast a post-election crawl of 45%**
- **Markets are pricing a 60% implied depreciation in 1-yr**

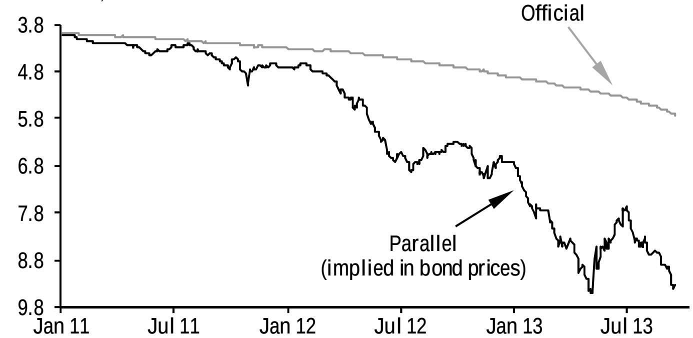
With BCRA reserves still under stress, the government has been accelerating the pace of peso depreciation ahead of the October elections. The depreciation of the official exchange rate has accelerated to a compounded annualized pace of 35% (20day/20 day), up from 17.5% in the first half of the year. NDF markets are pricing in a 60% crawl of the official peso in a one-year horizon, a rate that reflects a visible post-election FX adjustment. The J.P. Morgan forecast also anticipates a pickup in the crawling peg post-October 27 elections—but one that averages 40%-45% on an annualized basis. Thus, the year-end 2013 peso forecast is 6.4 vs. USD. This contrasts with an alternative scenario of a post-election gap devaluation, which we deem to be too politically costly for the administration to embrace.

The pickup in the expected pace of the peso crawl vs. the US dollar is necessary to address Argentina's high inflation and real exchange rate strengthening, particularly because BRL (Brazil is Argentina's main industrial trading partner) has depreciated against the US dollar. Admittedly, recent genuine inflation has risen, but less than was expected. In August, genuine inflation was 1.9%m/m compared to 2.2% in the two previous months. Thus, we scale back our year-end genuine CPI forecast to 26.5%oya, from 31% previously. However, the lack of a credible anti-inflation policy means that if the rate of peso crawl increases (so as to limit international reserve loss), inflation is likely to follow suit with a lag. Ultimately, this will limit the real exchange rate gains of applying this FX strategy.

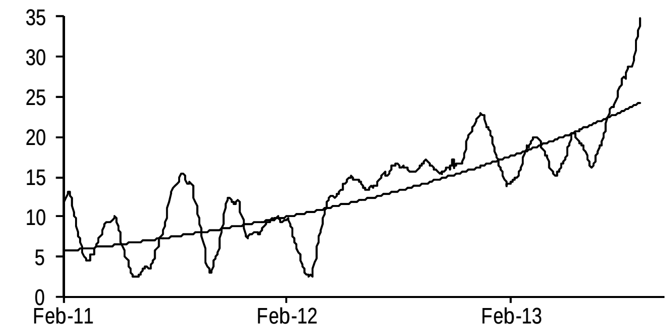
Markets continue to monitor the parallel FX rate as a measure of balance of payment pressures although that market is highly illiquid. The parallel peso currently stands at 9.3. Note that the spread between the official spot and the parallel FX rate (implied in the bond market) has been widening (first chart). A likely value for the parallel FX rate by year-end 2013 would be 10.4. That value would be consistent with our forecast for a 45% annualized crawl for the official peso following elections and standstill assumptions for soybean prices, interest rates, and monetary financing of the deficit (see "Shedding light on Latin America's shadow FX rates," *GDW*, May 24, 2013).

Both the official forecast and the model estimate for the parallel FX rate imply an FX premium of 63% at year-end. This compares with a similar spread currently and in the

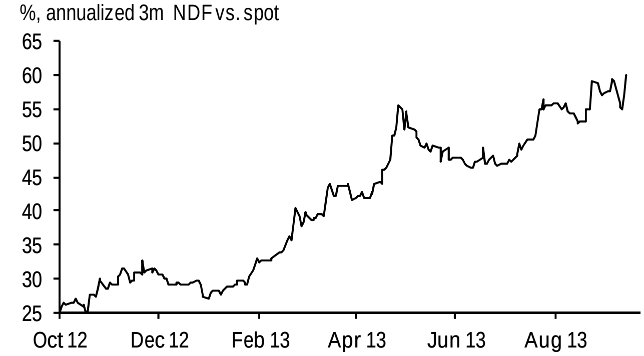
Peso exchange rate
USD/ARS, inverse scale



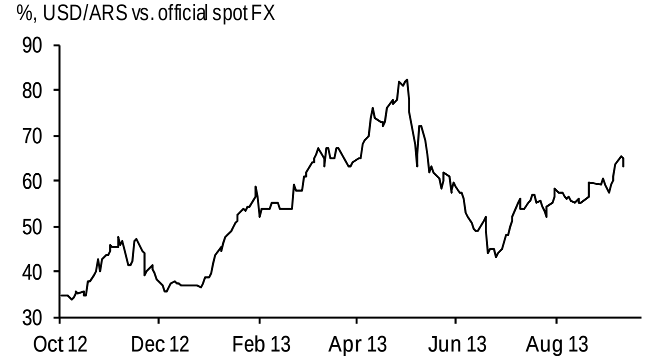
Official peso spot
% 20d/20d, ar



Official peso: 1-year implied depreciation in NDF market
%, annualized 3m NDF vs. spot



Parallel peso premium
%, USD/ARS vs. official spot FX



Source for all charts: J.P. Morgan

middle of the 45%-80% gap that has prevailed during the course of this year. We do not expect the government to formalize a dual FX regime after the election because it would need to sell more reserves than it might feel comfortable doing in response to financial market demand for US dollars.

Data releases and forecasts

Week of September 23 – 27

Mon Sep 23 — Trade balance
US$ bn

	May	Jun	Jul	Aug
Headline balance	1.3	1.2	0.8	__
12-month sum	10.1	10.3	10.0	__
Energy-related	-0.6	-1.1	-1.0	__
12-month sum	-4.4	-4.6	-4.8	__

Mon Sep 23 — Consumer confidence
UTDT

	Jun	Jul	Aug	Sep
Level	44.5	47.5	50.3	__

Tue Sep 24 — Industrial production
Official

	May	Jun	Jun	Aug
%oya	5.2	3.8	2.8	__
%m/m	0.5	-0.1	0.3	__

Fri Sep 27 — Official economic activity (EMAE)
%oya

	Apr	May	Jun	Jul
EMAE	7.0	7.8	6.4	__

Review of past week's data

Real GDP (Official)
%oya

	4Q12	1Q13	2Q13	
Real GDP	2.1	3.0	__	8.3

Current account
US bn

	4Q12	1Q13	2Q13	
CA balance	-0.6	-2.4	__	650

Source: INDEC

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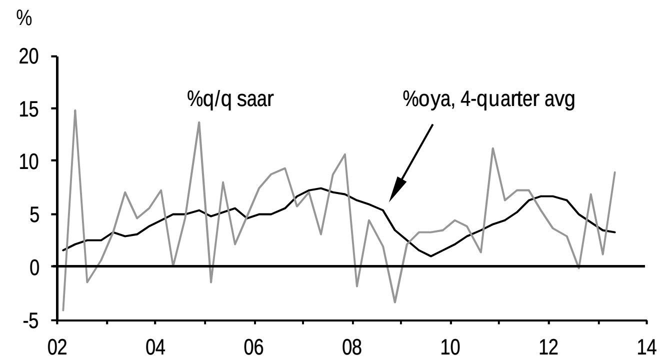
Colombia

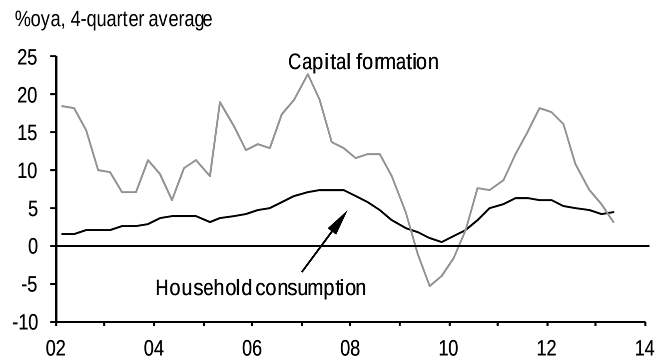
- **2Q GDP growth surprised significantly to the upside: 8.9%q/q saar versus 2.4% expected by J.P. Morgan**
- **3Q may deliver some payback, but BanRep doves' argument for more growth insurance should fall flat**
- **We scrub the 50bp September cut from the forecast, and revert to our original call of 125bp of normalizing hikes in 2H14**
- **We do expect BanRep to extend the dollar purchases, notwithstanding the recent rhetoric to the contrary**

Colombia: GDP growth



Source: DANE

Colombia: household consumption and capital formation



Source: DANE

Second-quarter GDP growth released this week surprised on the upside, printing at 4.2%oya (J.P. Morgan: 2.3%oya; market: 3.3%; BanRep: 3.4%) and delivering an outstanding 8.9%q/q saar sequential rebound (first chart). The less volatile 4-quarter average of year-ago growth decelerated 0.1%-pt to 3.3%, showing that Colombian GDP growth is below potential (estimated to be around 4.5%-5.0%) but at a higher level than we had anticipated. There is lingering uncertainty surrounding growth in Colombia, as 3Q preliminary figures are on the weak side. However, at this point, our expectation for disappointing 2Q growth that we thought would tip the scales in favor of BanRep's doves did not materialize—in fact quite the opposite—and this should preclude the need for the insurance of an additional one-off rate cut this month. We now expect BanRep to keep the policy rate on hold until 2H14, at which point we expect normalization from the current 3.25% to 4.5% by the end of next year. However, on the FX front, the more dovish Fed and the prospects of dollar inflows from Ecopetrol dividends and bond issuance (as well as the government's own global issue this week) should prompt authorities to stay vigilant, despite the recent suggestion from President Santos that BanRep dollar purchases may no longer be necessary. We expect the authorities to extend the program for another three months.

Given this surprisingly strong sequential reading in 2Q (which may have been somewhat exaggerated by the early Easter week in 2013), as well as the recent headwinds (end-August strikes and plummeting consumer confidence), some payback in 3Q is expected. We now expect less pronounced marginal growth during July-September (2.0%q/q saar from 4.5% before). Nonetheless, this should deliver a more robust 4.7%oya print when the data are revealed in mid-December due to a base effect. With growth expected to normalize back to a trend-like 4.5%q/q saar pace in 4Q, full-year 2013 growth should now finish at 3.8% instead of 3.3% as we expected before.

Looking at the demand-side breakdown of GDP, household consumption remained firm, but capital formation decelerated—though less than we had projected. Capital formation was the big surprise compared to our call, printing at 7.7%q/q sa from -1.3% in 1Q. Digging deeper into this number, while agriculture-related investments, machinery, services, and buildings improved on the margin, civil works and transportation decelerated. In all, capital formation performed better than the indicators (such as capital goods imports) had been suggesting. Construction, machinery, and civil works weigh 22%, 32%, and 29% of total capital formation, respectively, and their performance on the less volatile 4-quarter trend remains tepid. Capital formation overall continued to decelerate in this 4-quarter measure, while household consumption accelerated on the margin (second chart). Household consumption increased 2.0%q/q sa after a 0.6% contraction in 1Q, while government consumption increased 2.6%q/q sa after also declining 0.6% in 1Q. The external sector added almost 1.0%-pt to GDP with exports increasing 9.4%q/q sa (from -3.0% in 1Q) and imports increasing 4.6%q/q sa (from -1.6% in 1Q).

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Chile

Data releases and forecasts

Week of September 23 – 27

No data releases during the week.

Review of past week's data

No data released.

Colombia

Data releases and forecasts

Week of September 23 – 27

Mon Sep 23 — Trade balance

	Apr	May	Jun	Jul
US$ bn	-0.2	0.1	0.5	-0.4
US$ bn, 12-month	-1.5	-1.3	-0.9	-0.8

Thu Sep 26 — Current account

	3Q	4Q	1Q	2Q
US$ bn	-3.6	-3.4	-3.0	-3.6
%of GDP, 4-quarter	3.3	3.2	3.6	3.7

Source: DANE and BCB

Review of past week's data

GDP

	4Q	1Q	2Q
%oya nsa	3.3	2.7	~~2.3~~ 4.2
%q/q saar	6.9	1.3	~~2.4~~ 8.9

Industrial production

	May	Jun	Jul
%oya nsa	-2.9	-5.5	~~-4.0~~ *0.2*
%m/m sa	0.1	1.5	~~-0.6~~ *1.6*

Retail sales

	May	Jun	Jul
%oya nsa	5.4	4.4	~~4.0~~ *5.4*
%m/m sa	0.9	-0.6	~~-0.4~~ *1.8*

Source: DANE

Peru

Data releases and forecasts

Week of September 23 – 27

No data releases during the week.

Review of past week's data

GDP

	May	Jun	Jul
%oya nsa	4.8	4.4	~~4.8~~ *4.5*
%m/m sa	0.0	1.4	~~0.3~~ *-1.0*

Unemployment

	Jun	Jul	Aug
%	5.8	6.0	5.6

Source: INEI

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United Kingdom

- **MPC minutes show unanimous vote on QE in September**
- **Inflation continues to fall while core inflation is stable**
- **Retail sales fall in August but the trend remains solid**
- **Next week's services release will shed more light on 3Q GDP**

We had been looking for David Miles to begin voting for more QE in September, after some heavy hints in the last set of minutes. But the speed and breadth of the improvement in the data has left all members in wait-and-see mode. In a recent shift toward increased communication, the minutes of the September meeting provided an updated BoE staff estimate of 3Q GDP, which stands at 0.7%q/q relative to the 0.5% projection in the August Inflation Report. Our current 3Q forecast stands higher than this at 0.8%-0.9%q/q. The minutes note, however, that growth could accelerate to reach this pace in 4Q.

Commentary on the appropriateness of market interest rate expectations was conspicuous by its absence from this set of minutes—unlike in August, when members expressed a range of different views. This is not necessarily a vindication of where markets are priced, but does hint the MPC is becoming less wedded to the mid-2016 message on rates from its August projections. The minutes note there was a range of views on the speed with which slack would be absorbed, and note there had been little news since the last meeting. However, the ILO unemployment rate has fallen since then. We think the MPC will in November revise down its medium-term unemployment rate forecast. But at this stage any revisions are likely to be incremental, with the MPC placing increasing emphasis on the point that 7% is a pre-condition and not a trigger for higher rates.

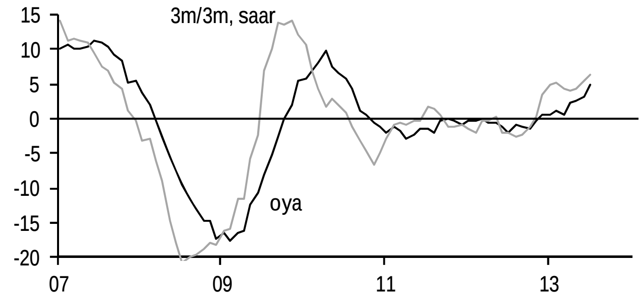
Regarding policy changes, the minutes make clear that no members thought tightening to be appropriate at present. But there is still a range of views about the extent to which further easing might be warranted. For now, though, we think further easing is very unlikely unless the recovery falters.

BoE on regulation and the housing market

Elsewhere in the minutes, the MPC notes that an upswing in housing market activity has the potential to support growth. The committee also noted that a period of rapid expansion in real house prices could become a concern that the FPC and PRA may have to respond to. We had expected the BoE to talk down the prospect of a response to recent housing developments—on the grounds that transactions and mortgage

House prices

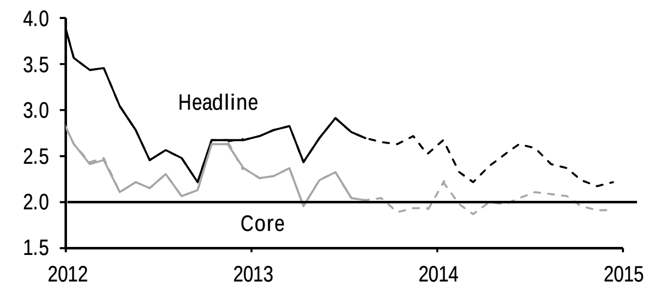
%, average of the Halifax and Nationwide indices



Source: Halifax and Nationwide

CPI inflation

%



Source: ONS

Inflation forecast

%oya

	CPI		RPI		
	Headline	Core	%oya	Index	Wedge
Jun 13	2.9	2.3	3.3	249.7	0.3
Jul 13	2.8	2.0	3.1	249.7	0.4
Aug 13	2.7	2.0	3.3	251.0	0.6
Sep 13	2.7	2.0	3.3	252.3	0.7
Oct 13	2.6	1.9	3.2	253.5	0.6
Nov 13	2.7	1.9	3.5	254.3	0.8
Dec 13	2.5	1.9	3.4	255.2	0.9
Jan 14	2.7	2.2	3.7	254.8	1.0
Feb 14	2.3	2.0	3.3	255.8	1.0
Mar 14	2.2	1.9	3.3	257.0	1.1
Apr 14	2.4	2.0	3.4	257.9	1.0
May 14	2.5	2.0	3.6	258.9	1.1
Jun 14	2.6	2.0	3.8	259.2	1.2
Jul 14	2.6	2.1	3.8	259.2	1.2
Aug 14	2.4	2.1	3.6	260.0	1.2
Sep 14	2.4	2.1	3.6	261.4	1.3
Oct 14	2.2	1.9	3.5	262.4	1.3
Nov 14	2.2	1.9	3.5	263.1	1.3
Dec 14	2.2	1.9	3.4	264.0	1.2
Jan 15	2.2	1.9	3.5	263.6	1.2
Feb 15	2.2	1.9	3.4	264.5	1.2
Mar 15	2.2	1.9	3.3	265.6	1.1
Apr 15	2.3	1.9	3.4	266.7	1.2
May 15	2.3	1.8	3.4	267.7	1.1
Jun 15	2.4	2.1	3.5	268.2	1.0

Source: J.P. Morgan and ONS

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lending remain subdued. Indeed, Deputy Governor Bean has previously dismissed talk of a housing bubble.

It is difficult to see how the FPC would feel that tightening conditions in the mortgage market generally is appropriate at present—particularly given the Help to Buy scheme is trying to do the opposite. And although the FPC can act if it feels prices are rising due to runaway expectations, it is difficult to argue that broader supply and demand fundamentals are not responsible for what we are seeing at present. One area the FPC is likely to explore is buy-to-let lending. Targeted action here could sidestep any conflict with the Help To Buy scheme and credit conditions in the mortgage market more generally, while at the same time helping to address concerns that the current rise in house prices may have a speculative element.

CPI inflation trickles lower, core stable

CPI inflation was in line with expectations in August, with slower energy inflation pulling the headline CPI down from 2.8% to 2.7%oya. Core CPI inflation was stable at 2.0%. If anything, the underlying picture for core inflation continues to look sticky. A drop in clothing and transport services inflation helped to prevent core inflation from rising. More broadly, headline inflation is running below where the MPC had expected.

We continue to assume that gas and electricity prices will rise 5%-6% later this year, pushing sequential inflation back up to 4% in 4Q (excluding the rise in tuition fees and seasonal clothing price changes). Even so, we expect sequential and hence annual food price inflation to soften following the trend lower in agricultural prices—which should help to pull the CPI slightly lower in %oya terms. This is being reinforced by weak core PPI inflation, a renewed drop in oil prices, and a continuation of the recent appreciation in sterling. CPI inflation hence looks likely to average 2.6% in 4Q and undershoot the BoE's 2.9% modal forecast. Stronger growth appears to have taken further easing by the MPC off the table for now. But the failure of underlying inflation pressures to build in response to the recovery this year should help to vindicate the MPC's belief that it can afford to keep policy loose even as growth picks up.

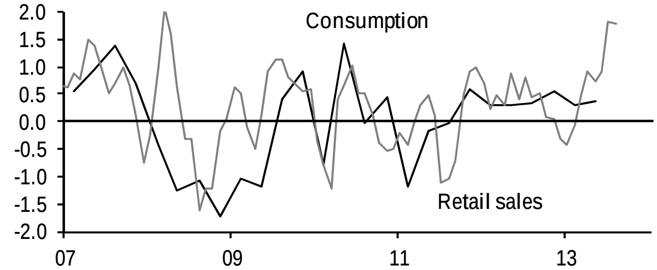
We had expected RPI inflation to accelerate in August despite a falling CPI. The rise turned out to be a touch larger than we expected—with the RPI picking up from 3.1% to 3.3%oya. This pickup is largely related to an unwind in the compression of RPI relative to CPI that we saw during the same period last year. We view today's widening in the wedge as a first step toward a normalization in the gap between RPI and CPI inflation—which is likely to continue this year. We expect the wedge to widen to 0.9%-pt by year-end, and grow larger in 2014 due to the effect that rising house prices are having via measured depreciation costs in the RPI. We see risks around

Inflation
%

	May 13	Jun 13	Jul 13	Aug 13
CPI				
m/m sa	0.0	-0.1	0.4	0.2
3m/3m saar	1.9	0.9	0.6	0.9
oya	2.7	2.9	2.8	2.7
RPI				
Index	250	249.7	249.7	251
m/m nsa	0.2	-0.1	0.0	0.5
oya	3.1	3.3	3.1	3.3
Details (m/m sa)				
Core inflation	0.2	-0.2	0.3	0.0
Goods	0.1	-0.7	0.2	0.0
Services	0.5	0.1	0.0	0.3
Ex. trans. serv.	0.2	0.2	0.2	0.3
Transport services	4.0	-1.1	-1.9	1.5
Food, alc, tobacco	0.0	-0.5	0.9	0.4
Food and non-alc	-0.3	-0.7	0.4	0.8
Alcohol and tobacco	0.6	0.8	0.7	0.7
Energy	-1.9	0.7	1.0	0.4
Gas, electricity	0.1	0.2	0.7	0.6
Petrol and liquid fuel	-3.9	1.3	1.4	0.4
Details (oya)				
Core inflation	2.2	2.3	2.0	2.0
Goods	0.2	0.7	0.3	0.4
Services	3.6	3.3	3.1	3.0
Ex. trans. serv.	3.1	3.1	3.0	3.0
Transport services	9.1	6.0	3.4	2.4
Food, alc, tobacco	5.0	4.6	4.7	4.8
Food and non-alc	4.3	3.8	3.8	4.1
Alcohol and tobacco	6.2	6.4	6.4	6.1
Energy	2.7	4.8	5.5	4.8
Gas, electricity	8.0	8.0	8.1	8.1
Petrol and liquid fuel	-2.7	1.4	2.7	1.3

Source: J.P. Morgan and ONS

Consumption versus retail sales (ex. auto fuel)
%q/q for consumption, %3m/3m, sa for retail sales



Source: ONS

the wedge as to the upside, due to the possibility that the ONS does not make further changes to the measurement of clothing prices (an issue that is still live).

Retail sales show payback in August

The volume of retail sales fell 0.9%m/m sa in August, following July's 1.1%m/m gain. The pattern in spending in these two months has been dominated by sales within food stores, which rose and then fell 2.7%m/m. This may reflect some special factors such as unseasonably good weather in July. The main point is that through this period, the trend in retail sales has been and remains firm. Over the course of this year, the level of spending at food stores has risen 0.8% while spending at nonfood stores is up 2.7%. This momentum is continuing. Despite the decline in August, nonfood stores' sales rose 0.4%m/m. And even assuming a near-flat September outcome, total retail sales appear to be heading for a gain of over 5%q/q saar in 3Q.

Our consumer nowcast—which incorporates a broader range of data relating to consumer spending—has not improved as dramatically as the retail sales data. But the nowcast indicates the underlying trend in consumer spending in 3Q is close to 2%q/q saar. This is consistent with a still-soft expansion in real incomes, and the idea that the acceleration in GDP growth at present is only partly due to the consumer.

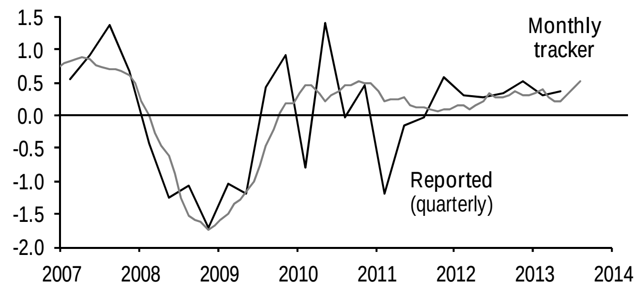
The Fed's non-taper and the MPC

We have long been skeptical of the forward guidance framework and particularly its application in the UK. We note that this week's decision by the Fed helps to highlight the potential difficulties with the framework.

When the Fed began open-ended QE in September last year, the latest available release of the US unemployment rate was 8.1%. As the Fed adopted the forward guidance framework on future rate policy in December, and via subsequent commentary, markets had formed a widely held impression that the course of both asset purchases and rates would be informed by the speed of decline in the unemployment rate. Bernanke himself stated in June that asset purchases were expected to slow to zero as the unemployment rate hit 7%, consistent with consideration of a higher Fed Funds target once the unemployment rate reached 6.5%. Given that framework, the expectation that the decline in the unemployment rate to 7.3% would prompt the Fed to begin to slow its asset purchases was widespread and perfectly reasonable to us. Regardless, the Fed has looked at the broader set of economic conditions existing alongside a meaningful decline in the unemployment rate, and decided that the time to slow asset purchases is not now. While the attempt to summarize the state contingency of policy in the

Consumption: reported versus monthly tracker from nowcast

%q/q, sa, tracking is based on a Dynamic Factor Model with Kalman filter



Source: ONS

path of a single variable (the unemployment rate) may have been appealing to the Fed *ex ante*, it has within a matter of months proven to be problematic.

The mappings between economic variables such as GDP, employment, and unemployment have been much more stable in the US than they have been in the UK through the downturn. So while the unemployment rate has not acted as a great summary statistic for US monetary policy, it is reasonable to think that similar issues are likely to occur in the UK. It should be remembered that this is not just about whether the threshold conditions are ultimately satisfied as policy moves. It also matters whether the interaction between markets, the economy, and the central bank has been helpful in the meantime. For example, it is not clear that recent falls in the unemployment rate in the UK should be invested with a lot of importance about the future path of UK monetary policy. But they certainly helped to underpin the recent steepening in the UK yield curve.

We continue to believe that the Bank of England would have been better advised to lay out rate guidance in the form of a calendar date and explain its thinking about the data as a whole, rather than highlighting a threshold for the unemployment rate. The Fed's actions this week demonstrate that, to some extent, it is moving back toward an assessment of the overall data picture rather than a focus on the unemployment rate. Markets appear to have suspected the same would ultimately be true for the Bank of England from the start. But we anticipate the MPC is still going to have a lot of work to do explaining its way around the movement in the unemployment rate relative to its preferred path for policy through time.

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Data releases and forecasts

Week of September 16 – 20

Tue
Sep 24
9:30am

BBA lending

Sa

	May	Jun	Jul	Aug
Secured lending (ch £ bn, sa)	-0.4	0.0	-0.1	
Loan approvals (000s sa)[1]	36.3	37.3	37.2	

1. For house purchase.

Wed
Sep 25
11:00am

CBI survey of distributive trades

% balance

	Jun	Jul	Aug	Sep
Volume of retailer sales	1	17	27	

Thu
Sep 26
9:30am

Balance of payments (quarterly report)

£ bn, sa

	3Q12	4Q12	1Q13	2Q13
Trade in goods and services	-7.4	-8.5	-5.8	
Income	-2.4	1.0	-2.1	
Current transfers	-5.7	-6.4	-6.2	
Current balance	-15.3	-13.6	-14.5	

Thu
Sep 26
9:30am

Business investment (final)

2000=100, sa

	3Q12	4Q12	1Q13	2Q13
%q/q	3.1	-6.2	-1.2	
%oya	3.3	-1.8	-5.5	

Thu
Sep 26
9:30am

Real GDP (national accounts)

Sa

	4Q12	1Q13	2Q13[1]	2Q13
Total GDP (%q/q sa)	-0.2	0.3	0.7	0.7
%oya sa	0.0	0.3	1.5	
%q/q saar	-0.9	1.1	2.9	
Breakdown (%q/q sa):				
Private consumption	0.5	0.3	0.4	
Public consumption	0.8	0.1	0.9	
Fixed investment	-4.9	0.2	1.7	
Exports	-1.9	-0.1	3.6	
Imports	-1.0	-2.0	2.5	

1. Preliminary outcome

Fri
Sep 27
7:00am

Nationwide house price index

Sa

	Jun	Jul	Aug	Sep
%m/m	0.3	0.9	0.6	
%oya	2.0	3.9	3.5	
%3m/3m saar	2.2	4.0	5.8	

Fri
Sep 27
9:30am

Index of services

Sa

	Apr	May	Jun	Jul
%m/m	0.3	0.2	0.0	0.4
%oya	2.1	1.5	2.8	2.0
%3m/3m saar	3.3	3.1	2.6	2.2

Review of past week's data

Retail prices

%oya

	Jun	Jul	Aug	
CPI	2.9	2.8	2.7	
Core CPI[1]	2.3	2.0	2.0	
RPI (1987=100)	249.7	249.7	~~250.7~~	*251.0*
RPI	3.3	3.1	~~3.2~~	*3.3*
RPIX	3.3	3.2		*3.3*

1. CPI ex food, energy, alcohol, and tobacco.

ONS monthly house price data

Nsa

	May	Jun	Jul	
All dwellings (%oya)	2.9	3.0		*3.3*

Producer prices

Nsa

	Jun	Jul		Aug	
Input prices %m/m	0.2	~~1.1~~	*1.2*		*-0.2*
%oya	4.0	~~5.0~~	*5.1*		*2.8*
Output prices %m/m	0.1	0.2			*0.1*
%oya nsa	2.0	2.1			*1.6*
Core output prices[1] %m/m	-0.1	0.1			*0.0*
%oya	0.9	1.1			*1.0*

1. PPI output ex food, beverages, tobacco, and petroleum products.

BoE's minutes of MPC meeting

See main text.

Retail sales

Volumes, sa

	Jun		Jul		Aug	
Inc auto fuel %m/m	0.2		~~1.1~~	*1.2*		*-0.9*
Ex auto fuel						
(%m/m)	0.2		~~1.1~~	*1.3*		*-1.0*
(%oya)	~~1.8~~	*1.9*	3.2			*2.4*
(%3m/3m saar)	3.7		~~7.2~~	*7.5*		*7.4*

CBI industrial trends

% balance

	Jul	Aug	Sep	
Total order book	-12	0		*9*
Output expectations	15	25		*33*
Output prices	2	0		*3*

Public sector finances

£ bn, nsa

	Jun	Jul	Aug	
PSNCR	-1.4	-21.1		*-3.0*
PSNB	10.1	-1.1		*11.5*
ex. fin. int.	7.9	0.2		*13.2*
Current budget (ex. fin. int.)	-7.2	2.3		*-10.8*
Net debt to GDP (%)	135.0	135.1		*135.6*
ex fin it. (%)	74.8	74.5		*74.6*

Sources: Nationwide, Rightmove, CBI, BBA, RICS, ONS, BoE, and J.P. Morgan

Russia

- **Activity data were mixed in August**
- **GDP is tracking 1.7%oya in 3Q13**
- **Sluggish growth unlikely to unnerve CBR in October**

Retail sales surprised slightly to the downside, slowing from 4.4%oya in July to 4.0% in August (J.P. Morgan: 4.1%; consensus: 4.2%). Seasonally adjusted, sales added 0.1%m/m, a slowdown from 0.6% the prior month. Real food sales continued to rise in August (up 0.3%m/m sa) due to a good harvest and falling prices, while non-food sales declined 0.3% in the month. The weaker retail sales growth was partly compensated by a sudden 1.0%m/m sa jump in consumption of services. Hence, it appears that overall consumption growth has continued through August, even if at a subdued pace.

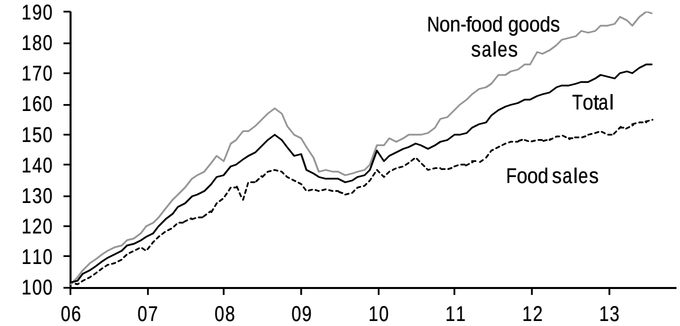
The labor market picture improved a bit in August. Although the unemployment rate remained unchanged at 5.5% sa, it was only due to a rise in the economically active population. Employment added 0.3%m/m sa, by our estimates, while in over-year-ago terms, the contraction in employment slowed to 0.4% from 0.9% the prior month. At the same time, nominal wage growth picked up from 12.6%oya to 13.3% in July, with private sector wage growth bouncing from 5.6%oya to 9.6%, by our estimates. Although this bounce will likely prove temporary and the broader trend for slower wage growth should continue, the labor market outlook looks less weak than the May-June data indicated.

The stagnating trend in investment demand remained intact, despite a continued roller coaster of activity in capital spending and construction—both surprised significantly to the downside in August after a positive surprise in July. In seasonally adjusted terms, capital spending fell 1.2%m/m and construction dropped 2.0% in August. Looking through the volatility, year-to-date capital spending contracted 1.3%oya, and construction fell 0.8%. While favorable base effects may lift over-year-ago prints in the coming months, it seems that the underlying momentum is likely to remain weak, as real interest rates remain high and the growth outlook is poor.

On the supply side, IP came in slightly stronger than expected at 0.1%oya in August (J.P. Morgan: -0.6%; consensus: 0.0%). Seasonally adjusted industrial output added 0.7%m/m, according to Rosstat. We estimate that mining rose 0.8%m/m sa, manufacturing increased 0.5%, and utilities contracted 0.4%. Positively, tentative signs of recovery have begun to appear in capex-related sectors and the automotive industry. Interestingly, capacity utilization seems to have settled at about 75% in recent months, according to the REB survey, some 5%-pts below 2011-12 levels (second chart next page).

Real retail sales

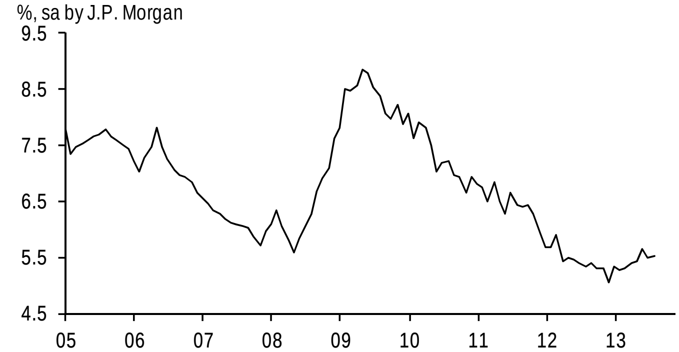
Index, Dec05=100, sa by J.P. Morgan



Source: Rosstat, J.P. Morgan

Unemployment rate

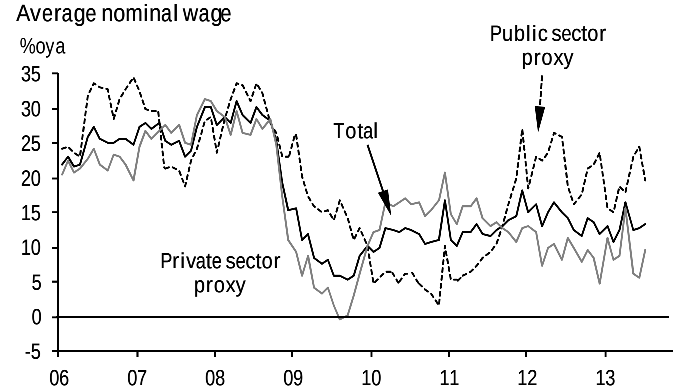
%, sa by J.P. Morgan



Source: Rosstat, J.P. Morgan

Average nominal wage

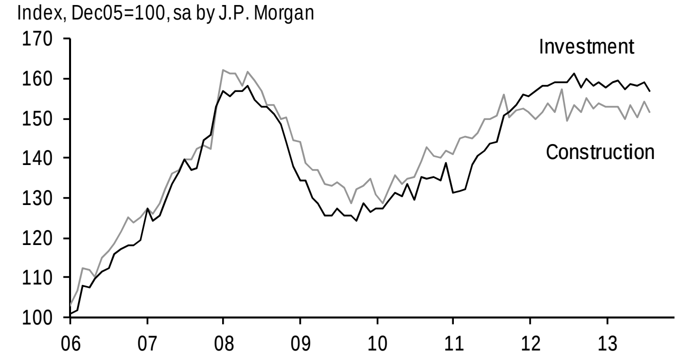
%oya



Source: Rosstat, J.P. Morgan

Capital investment vs. construction

Index, Dec05=100, sa by J.P. Morgan



Source: Rosstat, J.P. Morgan

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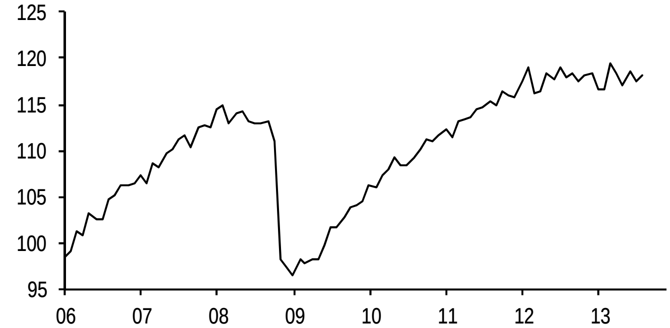
Taken at face value, this implies that Russia's negative output gap may have widened to some 2% of GDP, more than the 0% to 1.0% indicated by filters or labor market indicators.

GDP is tracking a lackluster 1.7%oya in 3Q, but the CBR is unlikely to be too concerned. Although base effects are helping to lift over-year-ago comparisons, underlying growth is likely to remain slightly below potential in 3Q and unlikely to reach the government's 1.8%-2.0% projection for the full year, in our view. We are comfortable with our 1.6% growth forecast in 2013. That said, anemic growth is unlikely to unnerve the CBR at the next meeting, as it is looking to enhance its anti-inflation credentials and has signaled its increased focus on reaching mid-term inflation targets. Unless inflation surprises significantly to the downside in September, the CBR is likely to remain on hold at its next meeting as it signaled in its last policy statement.

Industrial output

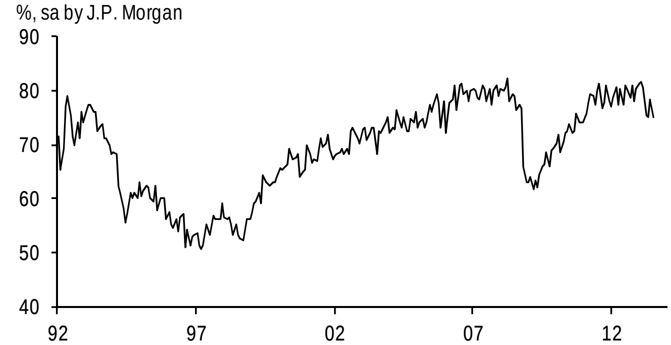
Index, Dec05=100, sa



Source: Rosstat, J.P. Morgan

Capacity utilization in the industrial sector

%, sa by J.P. Morgan



Source: REB, J.P. Morgan

Russia data watch is biweekly, next on October 4.

Data releases and forecasts

Weeks of September 23 – October 4

Consumer prices

	Jun	Jul	Aug	Sep
%m/m nsa	0.4	0.8	0.1	0.2
%oya	6.9	6.5	6.5	6.1

PMI surveys

	Jun	Jul	Aug	Sep
Manufacturing PMI	51.7	49.2	49.4	50.0
Services PMI	48.8	48.7	51.8	52.0

Broad money supply

	May	Jun	Jul	Aug
Broad money, M2	28084	28506	28734	28985
%m/m nsa	0.9	1.5	0.8	0.9
%oya	14.9	15.1	16.5	18.0

Source: Rosstat, Markit, CBR

Industrial producer prices

	Jun	Jul	Aug	
%m/m nsa	0.4	2.0	~~1.9~~	*2.8*
%oya	3.7	6.6	~~3.4~~	*4.6*

State budget

Rubles bn, cash flows

	Jun	Jul	Aug	
Balance	116	-81	~~125~~	*102*
% of GDP	2.1	-1.4	~~2.2~~	*1.8*
Revenue	1141	1072	~~1125~~	*1087*
Expenditure	1025	1153	~~1000~~	*985*

Auto sales

	Jun	Jul	Aug	
Units, 000s	241	235	~~235~~	232
%oya	-11.5	-8.3	~~-9.2~~	-10.5

Source: Rosstat, MinFin, AEB Russia

Review of past two weeks' data

Real economy indicators

Real terms, %oya

	Jun	Jul	Aug	
Construction	-7.9	6.1	~~1.5~~	-4.5
Agriculture	2.1	5.8	~~8.0~~	3.3
Transportation	-0.5	-0.3	~~0.0~~	0.3
Fixed investment	-3.7	2.5	~~0.0~~	-3.9
Retail sales	3.6	4.4	~~4.1~~	4.0
Average monthly wage	5.3	6.4	~~6.0~~	5.9
Unemployment	5.4	5.3	~~5.2~~	5.2
Industrial production	0.1	-0.7	~~-0.6~~	0.1

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Turkey

- **Twelve-month trailing primary surplus reaches a 15-month high of 2.0% of GDP in August**
- **The budget deficit will likely be comfortably below the official target of 2.2% of GDP at year-end**
- **It is a relief to see continued fiscal discipline especially given the external vulnerabilities**

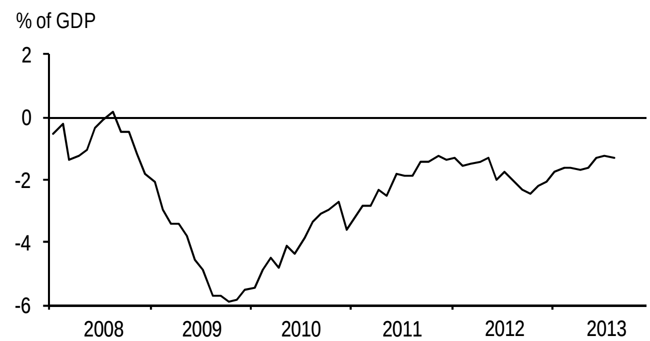
July-August central government budget data released by the Ministry of Finance in Turkey showed continued fiscal discipline over the summer months. It is critical that Turkey avoid the twin deficit problem (running both a large current account and fiscal deficit). While the CAD remains high and thus is a major cause for concern, good fiscal performance has been, and will be, instrumental in supporting investor appetite for Turkish financial assets.

The budget performance in the first eight months of the year supports our long-standing view that the full-year fiscal targets will be overachieved by a significant margin. The performance also shows that the government has ample room to ease fiscal policy in an effort to support growth. Although we expect some fiscal easing in the pre-election period, we think this will not reach a level that could threaten investor sentiment. The AKP government has generally followed fiscally responsible policies in pre-election periods. Given the weakness of the opposition (and thus little need for populist action) we do not see any reason why the performance will be different this time. Finally, the financing requirement of the Treasury is turning out to be lower than originally projected due to continued fiscal discipline. Low borrowing needs, in turn, ease the pressure that could build up on the Treasury given the sharp increase in interest rates.

Turkey ran a primary surplus of TRY38 billion in the first eight months of the year, which is double the full-year target. The 12-month trailing primary surplus reached a 15-month high at 2.0% of GDP while the cash deficit was 1.3% of GDP. The official cash deficit target is 2.2% and the performance so far supports our view that the targets will be overachieved by some margin. In fact, we have recently revised our budget deficit forecast to 1.8% of GDP from 2.0%. Data imply that the risks are for even stronger performance.

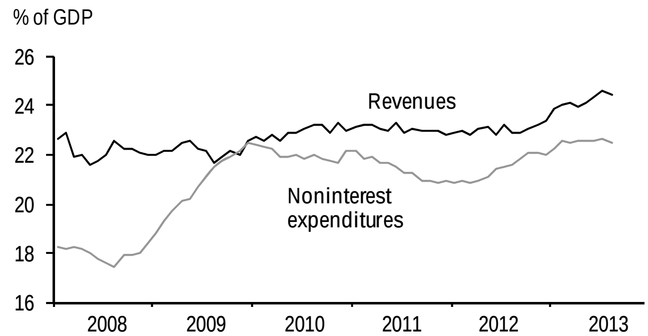
Data show an 18.6%oya increase in tax revenues and a 15.2% increase in non-interest expenditures in the first eight months of the year. The growth in tax revenues was mainly due to stronger indirect tax collection. While corporate tax collection was flat and income tax collection was up 11%, domestic VAT and special consumption taxes were up by 22% and 24%, respectively. Also worth noting was the 30% jump in

Budget balance, 12-month trailing



Source: Ministry of Finance

Central government revenues and expenditures



Source: Ministry of Finance

import tax collection. However, this was at least partly explained by the payment of tax arrears by energy importers.

While tax revenues were up 19%oya, there was also a 15% surge in non-interest expenditures in the first eight months of the year. This clearly shows that the fiscal policy is not contractionary in a significant way. The first eight months saw increases in both social security premiums and in transfer payments to social security institutions. This reflects the improvement in labor market conditions and the increased formalization in the labor market. Personnel expenditures were up 11%oya in the Jan-Aug period, but wage agreements settled with trade unions show that the government remains committed to fiscal discipline. Wages are to be raised by 3% in the first and second halves of next year. This is in line with the inflation target of 5.0%. Importantly, capital expenditures were up 49%oya in the first eight months of the year. This is presumably due to some large public works projects such as the Third Bosphorus Bridge and the Istanbul-Izmir highway. Finally fiscal data also show that Turkey's structural problems such as over-reliance on indirect tax collection and stickiness in personnel spending persist, but these are unlikely to catch market attention.

The Turkey data watch is biweekly, next on October 4.

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J.P.Morgan

Data releases and forecasts

Weeks of September 23 – October 4

Tue
Sep 24
2:30pm

Capacity utilization

%

	Jun	Jul	Aug	Sep
Total manufacturing	75.3	75.5	75.5	75.2
Durables	71.9	72.7	72.5	74.5
Nondurables	72.7	72.9	72.6	72.5

The impact of the recent rise in bank lending rates will be seen in the coming months. Continued export resilience should prevent a sharper fall in capacity usage.

Fri
Sep 27
10:00am

Consumer confidence

	Jun	Jul	Aug	Sep
Consumer confidence	76.2	78.5	77.2	78.0
Financial situation - current	84.1	85.8	85.4	85.2
Financial situation - future	92.4	94.3	93.1	928.0
Economic setting	102.5	104.0	101.7	102.5
Employment	84.1	85.7	86.8	86.5

Consumer confidence likely recovered somewhat due to lira stability. This recovery would have been sharper had there been no rise in bank lending rates.

Mon
Sep 30
10:00am

Foreign trade

US$ bn, except as noted

	May	Jun	Jul	Aug
Trade balance	-9.9	-8.6	-9.8	-8.9
Exports	13.3	12.4	13.1	11.1
%oya	1.4	-6.0	2.2	-13.5
Imports	23.2	21.0	22.9	20.0
%oya	6.7	2.8	10.0	6.2

Exports remain resilient due to continued export penetration to higher-growth markets like Iraq and Libya. Imports are expected to lose momentum as domestic demand slows. Still, the foreign trade deficit remains wide, manifesting Turkey's dependence on continued capital inflows.

Thu
Oct 3
10:00am

Inflation

% change

	Jun	Jul	Aug	Sep
Consumer prices				
%oya	8.3	8.9	8.2	7.4
%m/m	0.8	0.3	-0.1	0.3
Producer prices				
%oya	5.2	6.6	6.4	5.9
%m/m	1.5	1.0	0.0	0.6
Core CPI (I)				
%oya	5.6	6.1	6.4	6.8
%m/m	0.4	0.2	0.0	0.8

Higher food prices have been a major factor behind the recent surge in inflation. Starting in August, we see a weakening in food prices and this along with the seasonal fall in clothing prices should be the main factor behind the low monthly inflation figure. Currency pass-through possibly prevented a sharper fall in prices.

Review of past two weeks' data

Industrial production

%oya

	May	Jun	Jul	
Total	2.0	3.0	~~4.5~~	*5.8*
Manufacturing	2.5	3.9	~~5.8~~	*7.6*
Mining	-6.0	-2.6	~~-2.8~~	*-1.9*
Energy and utilities	1.6	-0.5	~~2.1~~	*-1.6*

The upside surprise in industrial output mainly reflects export strength.

Gross domestic product

%oya, real terms

	4Q12	1Q13	2Q13	
GDP	1.4	2.9	~~3.5~~	*4.4*
Agriculture	3.4	4.3	~~4.2~~	*5.4*
Manufacturing	-0.1	1.6	~~3.8~~	*3.4*
Construction	1.5	5.9	~~7.0~~	*7.6*
Commerce	0.0	2.9	~~3.1~~	*5.0*
Transportation comms.	0.7	2.3	~~2.0~~	*3.3*
Financial services	3.8	6.5	~~7.0~~	*8.5*

While private consumption and public consumption and investment remained strong as expected, the strong inventory buildup was the main factor behind the upside surprise in GDP.

Balance of payments

US$ bn

	May	Jun	Jul	
Current account	-7.5	-4.6	~~-5.4~~	*-5.8*
Trade balance	-8.1	-7.0	-7.9	*-8.1*
Exports	14.4	13.3	~~14.1~~	*14.0*
Imports	22.5	20.3	~~22.0~~	*22.1*
Invisibles and transfers	0.6	2.4	~~2.5~~	*2.3*
Capital account	0.7	3.5	-1.5	
Overall balance	-4.1	-3.3	~~-3.0~~	*-1.7*

The widening in the CAD mainly stemmed from the worsening in the trade balance that followed the plunge in gold exports.

Labor market data

%

	Apr	May	Jun	
Unemployment (%)	9.3	8.8	~~8.6~~	*8.8*
Nonfarm payrolls (%oya)	5.4	4.9	~~5.0~~	*4.9*
Labor participation (%)	51.1	51.6	~~52.2~~	*51.6*

Employment growth remained strong mainly on the back of higher labor force participation rates.

CBRT rate decision

%

	Jul	Aug	Sep
CBRT 1-week repo rate	4.50	4.50	4.50
CBRT ON borrowing rate	3.50	3.50	3.50
CBRT ON lending rate	6.50	7.75	7.75

Governor Basci has stated clearly that the bank will keep its funding rate in the 6.75%-7.75% range until year-end. Thus the decision to keep rates unchanged was no surprise.

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Australia and New Zealand

- **FOMC's policy inaction helped drive AUD to fresh three-month highs**
- **Higher AUD is tightening financial conditions, keeping RBA Board in the game**
- **NZ economy barely grew in 2Q as impact of the drought kicked in**
- **Change of forecast: RBNZ to delay start of the tightening cycle**

The past week was unusually quiet in Australia, with only the release of the latest RBA Board minutes to keep observers interested, alongside the release of the second-tier car sales data. Indeed, the main economic event occurred offshore, with the Fed's decision to defer tapering its bond buying program triggering a spike in AUD to three-month highs. In fact, AUD now has risen 7% against USD since the start of September, and by 4% in trade-weighted terms. This renewed strength is due mainly to a combination of the Fed's unexpected policy inaction, the improved China data, and the end of election uncertainty in Australia, now that the new Abbott government has been sworn in. The week ahead is deathly quiet, with no top-tier economic data to be released, nor public RBA activity.

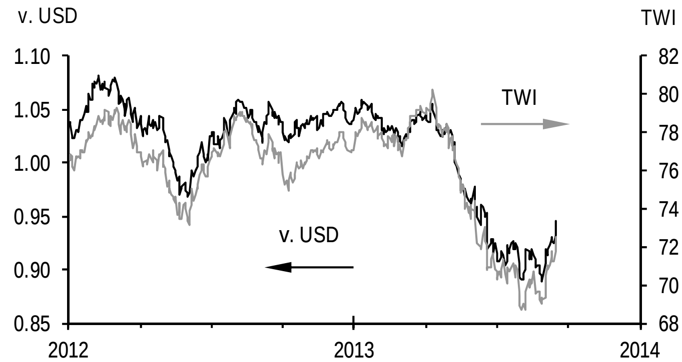
In New Zealand, the belated 2Q GDP result printed smack in line with expectations at 0.2%q/q, the weakest outcome in more than two years, with output growth held back by the fallout from the drought. In a change of forecasts, we have pushed out the likely timing of the first RBNZ rate rise, from 4Q13 to 2Q14, owing mainly to the recent announcement of restrictions on high loan-to-value (LVR) bank lending, which the RBNZ estimates is worth up to 30bp of tightening. Indeed, the greater policy flexibility afforded by the LVR measures means the RBNZ can sit for longer on the low cash rate.

Higher AUD = lower RBA cash rate

Recent AUD strength has important implications for the RBA policy outlook. RBA communications consistently have pointed to officials wanting a lower AUD, which they still describe as high, despite AUD's fall below USD parity this year. We currently characterize the RBA as "reluctant" cutters of the cash rate, on the basis that officials probably would prefer a lower AUD to play a bigger role in easing financial conditions. Inconveniently, however, higher AUD instead is tightening conditions against an economic backdrop of sluggish output growth, rising unemployment, low and fragile confidence, and benign inflation.

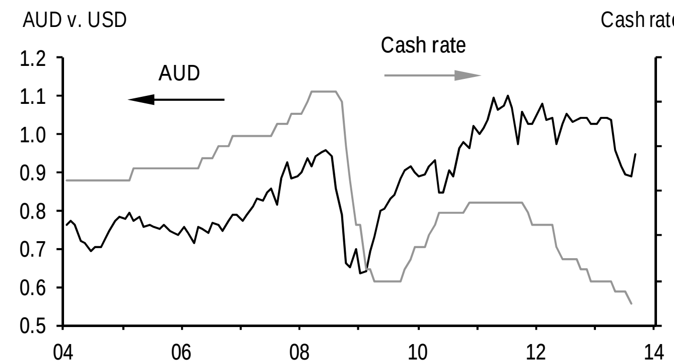
This combination, in our assessment, strengthens the case for the RBA extending the easing cycle; we continue to call for a 25bp rate cut in November. Essentially, the higher AUD climbs, the lower the cash rate needs to be. The RBA already has eased policy a total of 225bp since late 2011, but the impact of the moves thus far has been underwhelming. Business and consumer confidence have lifted, and the leading indicators of housing have improved. Investment outside mining, though, continues to fall, and the influential manufacturing and tourism sectors remain compromised by high AUD and weak demand.

Australian dollar



Source: J.P. Morgan

AUD and RBA cash rate



Source: RBA, J.P. Morgan

Meanwhile, steadily rising unemployment is an impediment to better retail conditions. And, the peak in mining investment, which has been the dominant force driving growth in the economy, is very near. We estimate that the capex peak will pass around the end of this calendar year. The path of least regret for RBA officials in this environment, in our view, would be to deliver further policy support before the onus for driving growth shifts from mining investment to materially weaker alternative sources of growth.

RBA's easing bias opaque, but still there

The minutes to the RBA's September Board meeting, released Tuesday, were consistent with our assessment that the cash rate probably has further to fall. Indeed, the minutes delivered what we had expected in flagging, as they did in August, that "the Bank should again neither close off the possibility of reducing rates further nor signal an imminent intention to reduce them." This was important confirmation that the Board does not want to declare the easing cycle over, and while it stops short of reinstating the "scope to ease further if needed" clause from the policy guidance of a few months back, it is enough for us to think the RBA remains in the easing game.

Reading through the commentary on the domestic economy, it is not surprising to hear the Board unconvinced that it has righted the listing ship. The main protagonists that previously have been identified as needing to lift and offset the drag from mining investment activity are non-mining business investment and dwelling investment; on both these fronts, the discussion in the minutes struggled to get very excited about the progress achieved so far. Non-mining business investment "remained subdued," and while there is a reference to the "apparent reluctance of businesses to take on new risks at present," which some argue may change post election, this remains to be proven.

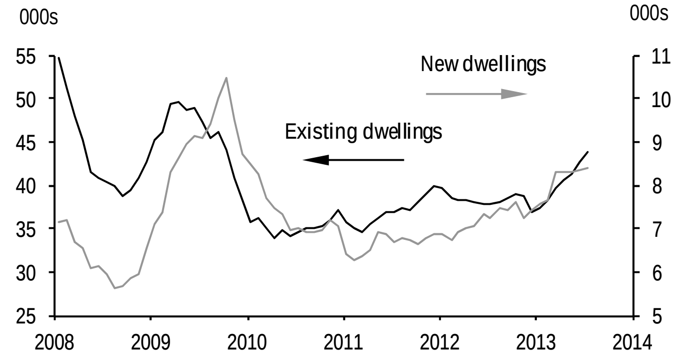
Officials acknowledge better numbers on housing overall, which has "continued to improve," but the pickup in dwelling construction remains "moderate." As in August, officials showed skepticism on the ABS capex intentions survey for mining in particular, which still projects further growth, contrasting that with their assessment that "based on…the Bank's liaison and public statements by mining companies…mining investment was likely to decline noticeably over the next few years." The gap the non-mining economy needs to plug is therefore quite deep.

The notes on the labor market are perhaps the most dovish, in that there is acknowledgment of further slippage, a downplaying of the more constructive parts of the household survey (like the upturn in hours worked, which "tend to be volatile"), and the observation that there is no sense that stabilization is imminent. This is adding further downside to wage growth, and therefore adding to the sense that inflation will remain well-behaved. Similarly, household consumption "had been below average," and "conditions in the domestic business and households sectors had changed little in the past six months."

RBA watching their Antipodean cousins

RBA officials are not totally defeatist, and still are emphasizing monetary policy's long and variable lags—there are several mentions of parts of the economy that are assumed to organically lift over time as a result of prior easing. For those looking for signs of nervousness on housing (the media commentary about booms/bubbles under low rates predictably has stepped up), there isn't much to see, though the two new themes of note introduced this week do touch on those issues.

Australia: volume of home loan commitments for owner occupiers



Source: ABS.

Australia: car sales

Source: ABS

The first was the statement that the Board was briefed on the RBNZ's recent macro-prudential policy decisions. As if anticipating possible misinterpretations of the Board's current thinking on housing market dynamics, this was explicitly mentioned in the context of the Aussie banks' operational exposure to their NZ subsidiaries, rather than being anything that piqued the Board's interest of itself in the policy space.

The second, more interesting, new theme is that RBA staff have identified leveraged investments by households in self-managed superannuation (i.e., pension) funds in housing as an area where "households could be starting to take some risk," which "would be closely monitored." We have been trying to identify channels through which stronger housing turnover could generate broader spillovers to the real economy *without* a meaningful step up in credit growth coming with it, and this is the only escape clause we can identify. Our assessment of this phenomenon is that on the ATO data to June, the numbers are not significant as a proportion of housing turnover, though this bears watching.

NZ economy hit by drought in 2Q

The June quarter Kiwi GDP report printed as we had expected, with the economy expanding a modest 0.2%q/q (J.P. Morgan and consensus: 0.2%q/q). There was a slight upward revision to the prior quarter from 0.3%q/q to 0.4%q/q. Although the gains over the past two quarters have been modest, we view this outcome as fairly encouraging, with most of the weakness attributable to the drought that hit real output in the first half of the year. The good news is that recent reports indicate this drag is fading, with pastoral conditions improving substantially over the past few months, which will likely benefit growth in 2H13.

On the production side, the agriculture sector was, not surprisingly, hard-hit by the drought, highlighted by a 6.4%q/q plunge in agriculture output in 2Q, which stripped 0.3%-pt off of quarterly growth. Waning output in the dairy sector was the main culprit, with this week's decline marking the fourth consecutive quarter that production in the dairy sector has declined. At the same time, there has been a substantial increase in the animal slaughter rate, which raises questions about how quickly production can rebound to pre-drought levels as farmers restock their herds.

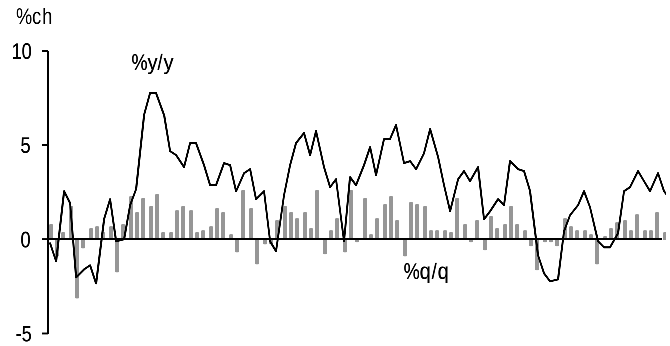
Expenditure on GDP during the quarter was slightly weaker than that of production (the latter being the official measure of GDP), increasing just 0.1%q/q. With agriculture production capacity constrained for much of the second quarter, it should come as little surprise that export volumes were very weak in the three months through June. Specifically, export goods plunged by 8.5%q/q in this week's release, which took a massive 1.8%-pts off of 2Q growth. The pickup in import demand was also unhelpful from a net trade perspective, taking the total drag from the trade sector to -2.2%-pt, though we note that the expenditure-side breakdown typically does not equal the sum of its parts anyway, so this may be overstating the drag.

Clearly with the headline result printing at a small positive, with expenditure GDP up 0.1%q/q, the substantial drag from trade was more than offset by very strong domestic demand, headlined by a 1%-pt boost to growth from final consumption expenditure. Elsewhere, the national accounts were also lifted by an increase in capex (+0.7%-pt) and inventory accumulation (+0.6-pt). With drought effects in dairy likely to fade over the coming quarters, growth in New Zealand is likely to accelerate to levels consistent with the upbeat message we have been getting from business surveys, consumer spending, and housing market data, which all suggest the economy is in full swing.

But NZ exports dodged the drought

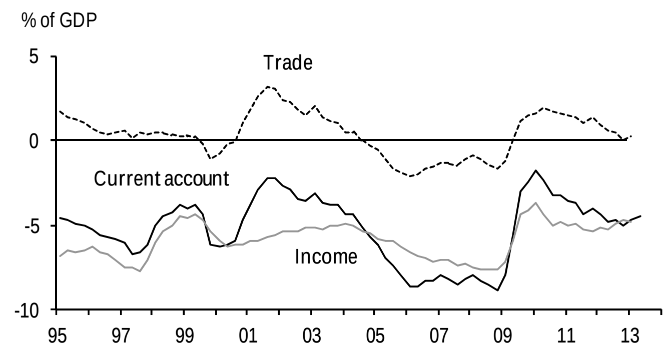
New Zealand's external sector, though, was not as adversely affected by drought conditions in the agriculture sector as we had feared in 2Q. The current account deficit did widen from NZ$0.42 billion to NZ$1.25 billion, but the consensus was looking for a larger slippage to NZ$1.9 billion (J.P. Morgan:

New Zealand: GDP growth



Source: StatsNZ

New Zealand: current account balance



Source: StatsNZ

NZ$1.8 billion). Further, the traded sector normally weakens in the June quarter, as the services balance normalizes after the peak in travel exports in 1Q. The goods trade surplus actually improved over 2Q by close to NZ$300 million, as higher global dairy prices offset weaker real output. The fact that the seasonally adjusted trade balance stayed in positive territory also shows that the external accounts did not suffer too heavily from drought effects. The income account deficit narrowed, too, mostly due to reduced payments on inbound direct equity investments, though income from NZ's foreign investment also picked up (again, mostly on equity investments).

On the capital account side, the focus again is on the balance of earthquake insurance claims on offshore reinsurers. Total claims associated with the earthquake are estimated at NZ$18.7 billion, and as of 2Q, over half of these (NZ$10.5 billion, NZ$1.4 billion in 2Q alone) have been settled. The claims are a capital account asset and so as they are wound down, the overall national investment position deteriorates. However, as we have said previously, this is fairly synthetic as this earthquake reconstruction funding is effectively locked in, meaning that as the claims wind off the investment/savings imbalance will move too, such that the current account should not grind against domestic demand desires.

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J.P.Morgan

Australia
Data releases and forecasts

Week of September 23 – 27

	Job vacancies	3Q12	4Q12	1Q13	2Q13
Thu Sep 26 11:30am	%q/q	-7.0	-10.1	-7.3	-

Review of prior week's forecast

New motor vehicles sales

	Jun	Jul		Aug
%m/m	3.6	~~-3.5~~	*-3.6*	0.8

New Zealand
Data releases and forecasts

Week of September 23 – 27

	International merchandise trade	May	Jun	Jul	Aug
Wed Sep 25 8:45am	NZ$ mn	0.0	0.4	-0.8	-0.4

Review of prior week's forecast

Current account balance

	4Q12	1Q13		2Q13	
NZ$ bn	-3.2	~~-0.6~~	*-0.4*	~~-1.8~~	*-1.3*

Real GDP

	4Q12	1Q13		2Q13
%q/q	1.3	~~0.3~~	*0.4*	*0.2*

Source: StatsNZ, ABS, RBA, J.P. Morgan

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Greater China

- **China: property prices rose further in August, local level fine-tuning of housing policy**
- **Highlights of the Shanghai Free Trade Zone**
- **Hong Kong: unemployment rate stable at 3.3% for three months ending August**

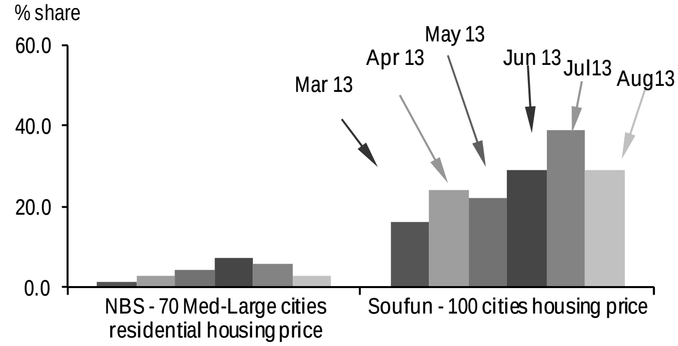
This week the National Bureau of Statistics (NBS) released its 70-city house price index for August. Compared to the previous month, new home prices declined in two cities, stayed flat in two cities, and increased in 66 cities. As such, 94.3% of the cities posted m/m price increases in August. Compared to one year ago, house prices increased in 69 cities in August, the fourth consecutive month that as many cities have featured positive year-ago growth. Wenzhou (in Zhejiang province) was the only city where house prices continued to decline, falling by 2.3%oya. Tier-1 cities continued to lead the house price inflation.

Amid the continuous rise in house prices over the past year, performance across regions and cities has varied considerably. Of the 70 cities surveyed most of the tier-1 cities have registered property price increases at close to a 20% annual rate: Beijing (19.3%oya), Guangzhou (19.0%oya), Shenzhen (18.4%oya), and Shanghai (18.5%oya). However, a large number of tier 2 and tier 3 cities registered less remarkable, single-digit annual price increases. This regional variation may grow, as tier-1 cities still face supply shortages while some small cities are facing oversupply.

Overall, the new administration has made no major public comments on the housing market, unlike in many other sectors. Meanwhile, it appears that the various local governments are in the process of fine-tuning their respective local-level policies (with recent policy easing in Wenzhou and Wuhu on the one hand, and policy tightening in other cities, such as tightening of HPR at Zhengzhou, on the other hand, as well as reports of mortgage tightening in Guangzhou, Beijing, Shenyang, Nanjing, and Shanghai).

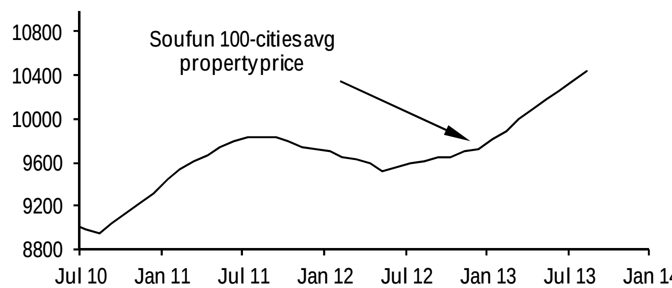
Recently there has been media speculation on the potential implementation of a nationwide real estate tax. According to the reports, a progressive tax would be charged on families with more than two homes in China, with an exemption of 80sqm per person, above which would be subject to progressive tax rates from 1% to 3% of appraised value. This is much higher than in the pilot schemes in Shanghai and Chongqing. In our view, the probability of introducing such a nationwide real estate tax any time soon is very low, but pilot schemes could be extended to a few more cities in the near term.

China cities with %m/m housing price decline
% share



Source: NBS, J.P. Morgan.

China: average housing price
RMB/Sqm



Source: Soufun, J.P. Morgan.

Shanghai Free Trade Zone highlights

China’s (Shanghai) Pilot Free Trade Zone (FTZ), personally endorsed by Premier Li Keqiang, will be officially opened at the end of this month. Although details have not been announced, it has been considered an important step for China to further open its market and a weather vane for the next phase of reforms initiated by the new government.

The market has been focusing largely on financial reform within the Free Trade Zone, e.g., interest rate liberalization. Market watchers are particularly excited about testing the convertibility of renminbi on the capital account on a pilot/experimental basis within the zone. But some market participants have developed the impression that the Free Trade Zone is merely a testing ground for financial reform; In fact, the FTZ pilot program covers trade, investment, finance, and government administration, and the heart of the reform is to redefine the relation between the government and the market. As summarized by Premier Li in the Summer Davos Meeting last week, “the Shanghai Free Trade Zone attempts to explore the negative list approach, and priority will be given to easier investment access and greater openness in the service sector.”

In our view, the markets’ excessive emphasis on financial reforms and unrealistic expectations on their progress is likely to result in confusion and disappointment after a short period of excitement (just as we saw with financial reform in Wenzhou).

What will be included in the FTZ?

The pilot reforms within the Shanghai Free Trade Zone comprise four areas, including trade, investment, finance, and administrative government.

Trade liberalization. To upgrade its trading capabilities—an essential part of a free trade zone—China will tackle two major areas. First is further liberalization of traditional trade businesses to enable the free movement of imports, storage, re-exports, processing, and manufacturing of goods within the zone. This is similar to preferential measures provided by existing bonded zones, but further initiatives may be undertaken to relax customs and tariff regulations. Second is the expansion and strengthening of Shanghai's position in relevant trade sectors. For instance, the Free Trade Zone has proposed to link Waigaoqiao Port, the Yangshan Deep Water Port, and the Pudong International Airport to turn Shanghai into an international shipping center. Moreover, the city is expected to build an international commodity trading platform and warehouses for the delivery of commodity futures and for the smooth transfer of international energy products, industrial raw materials, and agricultural products. If these goals are achieved, it will boost Shanghai's prosperity as a free trade port.

Investment liberalization. Under the so-called negative list approach, all sectors will be opened up, except those specifically excluded by law. This approach represents a partial decentralization of power by the government, as foreign investments within the zone will no longer be under the administrative control of the prevailing Catalogue for Guiding Foreign Investment and restrictions on foreign ownership and scope of business. The current approval system involving relevant government ministries (e.g., the NDRC and MOC) for foreign investments made by Chinese companies may be sidestepped within the zone, and the establishment of foreign investment funds is being encouraged to further facilitate overseas investment.

Financial reform. The lagging development of China's financial sector compared to other existing free trade zones outside China (e.g., Hong Kong) could be a drag on the development of the Shanghai Free Trade Zone. Potential financial reform measures within the zone that are circulating in the market include:

- interest rate liberalization and market-oriented pricing for financial assets;
- the convertibility of renminbi on the capital account on a pilot/experimental basis;
- allowing foreign banks and joint venture banks (which use both domestic private capital and foreign capital) to be established;
- allowing restricted banks to be established;
- allowing foreign-invested credit rating companies to be established;
- allowing some Chinese banks to engage in offshore business;
- encouraging and offering tax incentives for financial lease businesses;
- allowing overseas companies gradually to participate in commodity futures trading, financial lease companies to engage in the commercial factoring business related to their primary business, and overseas futures exchanges to designate or set up warehouses for the delivery of commodities futures;
- a potential 15% corporate tax on project companies engaged in overseas equity investment, in line with the high-tech service sector.

Overall, the financial reform within the zone should remove obstacles that impede the creation of the Free Trade Zone, and will also be a testing ground before China undertakes nationwide financial reform and RMB internationalization. In the long term, the FTZ may be developed into an "offshore" financial sector.

Supporting measures will address legal and administrative issues. We believe the most essential part of the reform within the Free Trade Zone is the change in administrative functions of the government, as the relationship between the government and the market is redefined. For example, the above-mentioned negative-list approach to investment will help China to adhere to the latest standards of international trade, which would enhance investors' confidence; more important, it would represent a fundamental change in China's administrative process. It should result in the market playing a more important role in trade, prevent rent-creating and -seeking activities under the current regime, and reduce monopolization. In terms of legal restraint, the Shanghai Free Trade Zone has been allowed an ad-hoc three-year suspension of implementation of the three laws related to foreign investment ("Law on Wholly Foreign-owned Enterprise," "Law on Chinese-foreign Equity Joint Ventures," and "Law on Chinese-foreign Contractual Joint Ventures") by the National People's Congress in late August.

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What to expect in the near term?

The Free Trade Zone is built by following the guideline of "complete deregulation of first tier, safe and efficient full-control of second tier and free flow of goods within the Zone." "First tier" refers to the relationship between the Free Trade Zone and abroad, whereby goods can exit and enter China free of customs supervision; "second tier" refers to the relationship between the zone and the rest of mainland China, whereby movements of goods shall be subject to applicable taxes and regulation.

The above guidelines are fairly straightforward when applied to physical trade; however, they are less clear when applied in the financial industry. These guidelines are seemingly borrowed directly from the experience of other international free trade zones, but Shanghai's financial reform has significantly lagged that of other free trade zones. The definitions have also given rise to various speculations and uncertainties on the financial reform, such as, should a financial institution have to open a branch or subsidiary in the Free Trade Zone (with area of only 28.78km^2) to benefit from the financial reform? Does complete deregulation of the first tier mean full liberalization of financial operations within the Free Trade Zone? How would authorities maintain full control of the second tier financial flows once the first tier is deregulated?

We believe the government is unlikely to make any aggressive moves in reforming the financial market. Over the near term, financial reform in the FTZ will focus on three aspects. First is to lower the threshold for the establishment of financial institutions (e.g., foreign banks, banking JVs, and financial leasing companies) in the FTZ; second is the potential removal of restrictions on certain offshore financial businesses, which may start from RMB settlement and treasury services for multi-national corporates, and then extend to RMB convertibility and cross-border investment. However, the possibility of a big-bang liberalization of offshore financial businesses is slim. The full liberalization of interest rates (including deposit rates) anticipated by the market is not likely in the short run. Third, channels connecting the FTZ and the rest of the mainland may be made available to enable capital flows to a certain extent (similar to the Renminbi Qualified Foreign Institutional Investors, or RQFII, scheme in the offshore RMB center in Hong Kong). However, the scale will be highly restricted in the near term.

Generally speaking, the development of the Free Trade Zone is likely to be a gradual process; it cannot be built overnight. Details are anticipated in the coming one or two weeks. That, however, is only the beginning, as more specific rules and improvements relating to different areas are expected to phase in over the next one or two years.

Hong Kong: labor force survey

Source: Hong Kong C&SD, J.P. Morgan

Hong Kong: unemployment rate at 3.3%

Hong Kong's average seasonally adjusted unemployment rate stayed at 3.3% for the June-August period, the same as the number for the three months ending July. Seasonally adjusted, the sequential trend in employed persons increased 1.6%3m/3m saar in August (vs. +3.0%3m/3m saar in July).

Overall, the labor market remained resilient through 3Q. In particular, data suggest that labor market demand is stable. Employment has continued to increase at a steady speed since December 2012, compared to generally modest monthly expansion throughout most of 2012. For the near-term outlook, the latest Business Tendency Survey (BTS) suggests that the expectation on business activities remained at a positive level in 3Q, though was slightly lower than in 2Q13. Hiring expectations for 3Q improved notably in sectors like manufacturing, accommodation, and food services. Overall, we expect a modest lift in China, alongside rather solid momentum in the developed countries during 2H13. With this external backdrop, Hong Kong's economic growth is likely to continue its modest pace of expansion in the coming quarters, and the labor market will likely remain largely stable.

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China:
Data releases and forecasts

Week of September 16 – 20

Mon
Sep 23
9:45am

Markit manufacturing PMI (flash)
Index, sa

	Jun	Jul	Aug	Sep
Overall	48.2	47.7	50.1	50.6

Review of past week's data

No data released.

Source: Markit, J.P. Morgan

Hong Kong:
Data releases and forecasts

Week of September 16 – 20

Mon
Sep 23
4:30pm

Consumer prices
% change

	May	Jun	Jul	Aug
%oya	3.9	4.1	6.9	4.3
%m/m sa	0.1	0.4	1.1	-0.7

Thu
Sep 26
4:30pm

Merchandise trade
HK$ bn

	May	Jun	Jul	Aug
Balance	-44.3	-49.7	-37.2	-35.3
Exports	291.5	277.6	305.4	325.5
%oya	-1.0	-0.2	10.6	4.4
Imports	335.8	327.3	342.6	360.7
%oya	1.7	1.4	8.3	3.8

Review of past week's data

Labor market survey (Sep 17)
Sa, 3mma

	Jun	Jul	Aug
Unemployment rate	3.3	3.3	3.3

Source: Hong Kong Census and Statistics Department, J.P. Morgan.

Taiwan:
Data releases and forecasts

Week of September 16 – 20

Mon
Sep 23
8:30am

Labor market survey
%

	May	Jun	Jul	Aug
Unemployment rate, sa	4.19	4.17	4.18	4.18
Unemployment rate, nsa	4.06	4.14	4.25	4.33

Wed
Sep 25
4:00pm

Export orders
% change

	May	Jun	Jul	Aug
%oya	-0.4	-3.5	0.5	0.9
%m/m sa	1.0	-2.2	2.8	1.5

Thu
Sep 26
4:00pm

Industrial production
% change

	May	Jun	Jul	Aug
%oya	-0.3	-0.4	2.1	1.3
%m/m sa	1.4	-1.3	2.7	1.2

Thu
Sep 26
5:00pm

Central bank MPC meeting
%p.a.

	12Q4	13Q1	13Q2	13Q3
Rediscount rate	1.875	1.875	1.875	1.875

Review of past week's data

No data released.

Sources: Central Bank of Taiwan, DGBAS, J.P. Morgan

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South Korea

- **Customs exports to EM Asia rebounded firmly in August, partly inflated by pre-holiday effect**
- **Upstream price pressures on the rise, but contained by the currency move**

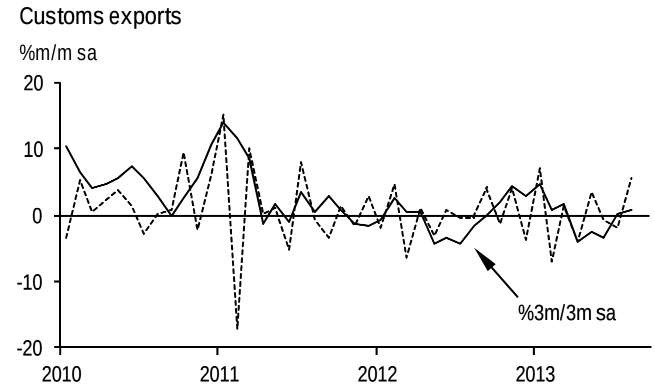
The data calendar was light this week due to the Full Moon Festival holiday from Wednesday to Friday. Since the holiday is occurring earlier than usual and during the workweek, its impact on activity and inflation is expected to be larger than usual. For example, customs exports are expected to decline in September, reversing much of the gain in August that was due to exporters' front-loading shipments ahead of the holiday. There is no official seasonal adjustment process for exports, and the standard method of seasonal adjustment does not fully control for the lunar holiday effect. Industrial production is also expected to soften in September, but the decline should be less noticeable on a seasonally adjusted month-on-month basis since the National Statistics Office tends to remove the holiday effect quite effectively in its official adjusted data series. Finally, the earlier arrival of the holiday likely pressured food prices, with the main harvest of key agricultural products scheduled to come after the holiday, while demand for those products often rises during the holiday week. However, if weather conditions remain favorable after the holiday, food prices should drop in October, making the expected gain in September temporary.

Destination details of August exports

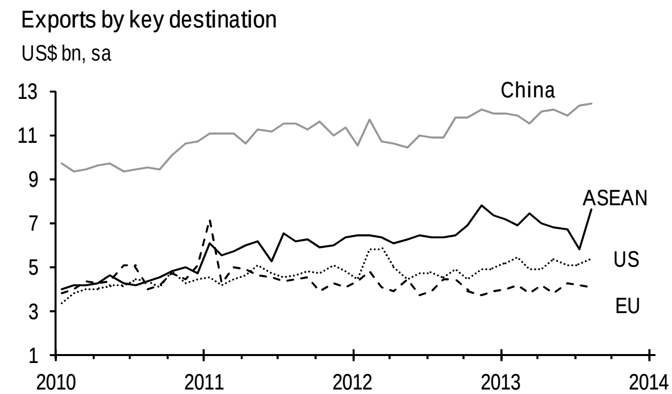
The Ministry of Trade, Industry, and Energy finalized the August trade outcome, confirming that customs exports rose 5.7%m/m sa, far more than reversing the previous two months of declines. Imports were slightly better than in the preliminary report, staying flat in August after having risen 2.6% in June and 0.2% in July. Excluding crude oil (volumes and contract prices for crude oil were down during the month), customs imports rose 2.1% in August after having fallen 0.8% in July. By destination, the export gain was broadly based in August, with shipments to ASEAN surging 30.8% after having declined for seven of the past eight months since December 2012. Much, but not all, of the August gain can be attributed to the pre-holiday effect, suggesting that exports to ASEAN countries are bottoming. Meanwhile, exports to the EU edged down for the second month after the huge gain in June.

Pipeline price pressures only edged up, constrained by currency appreciation

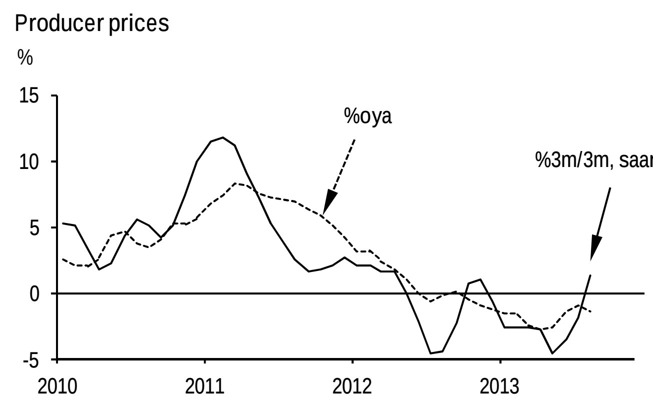
Producer prices rebounded 0.4%m/m sa in August after remaining flat in July, yet the over-year-ago contraction accelerated to 1.3% in August due to base effects. As



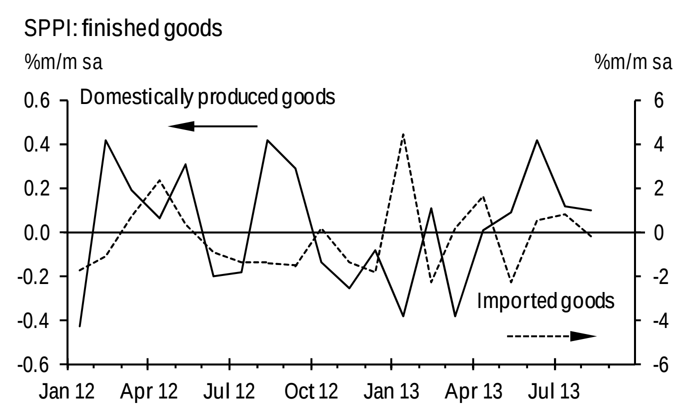
Source: Customs Office and MOTIE



Source: Customs Office and MOTIE



Source: BoK and J.P. Morgan



Source: BoK and J.P. Morgan

expected, the most notable gains were in agricultural and oil products prices, with service prices also adding to price pressures. Excluding food and energy, core PPI prices decelerated 0.2%m/m sa in August after rising 0.4% in June. However, the stage of processing price index inched up, marking the third monthly increase, but at a decelerated pace. Domestically produced good prices rose relatively firmly in August, but imported intermediate and finished goods prices declined modestly in the month, outweighed by the renewed strength of KRW.

Data releases and forecasts

Week of September 23 – 27

Tue
Sep 24
6:00am

Bankruptcy filing
Nsa

	May	Jun	Jul	Aug
Bankruptcy filings	71	58	101	80
Dishonored bill ratio	0.02	0.01	0.02	0.01

Bankruptcy filings likely declined in August, with a calendar effect playing the main role in the volatility of the previous two months.

Thu
Sep 26
6:00am

Consumer survey
100=neutral reading, nsa

	Jun	Jul	Aug	Sep
Index	105.0	105.0	105.0	106.0

Consumer sentiment likely edged up in September, helped by government measures to boost housing purchases and an equity price increase.

Fri
Sep 27
8:00am

Current account
US$ bn nsa

	May	Jun	Jul	Aug
Balance	8.6	7.2	6.7	5.5

While the customs trade surplus widened in August, some of this was related to vessel delivery. Merchandise trade balance seasonally deteriorated, but the deterioration was likely offset by a holiday effect this year.

Review of past week's data

Producer prices (Sep 17)
% change

	Jun	Jul	Aug
%oya	-1.4	-0.9	-1.3

Producer prices rebounded 0.4%m/m sa in August, led by agricultural and oil products prices. Services prices also rose in financial and transportation services. The local equity market rallied in August, so trading commission fees were up, while global oil prices also pushed up transportation fees.

Stage of processing price index (Sep 17)
% change

	Jun	Jul	Aug	
%oya	-2.6	-1.8	~~-2.2~~	*-2.5*

The SPPI declined 0.1%m/m nsa in August, but only for seasonal reasons. Seasonally adjusted, the SPPI edged up 0.1%m/m sa; prices of domestically produced items rose, but were partially offset by a decline in imported goods prices. Among imported goods, intermediate and finished goods prices declined modestly, reflecting the currency move, yet the price hike in global oil prices pushed up raw material prices. Meanwhile, the over-year-ago contraction deepened to 2.5% in August after having slowed for the previous two months.

BoK Watch

The local bond market rallied this week following the global trend ahead of the FOMC meeting. Benchmark 3Y KTB yields closed down 8bp for two days compared to last Friday's closing. Because the local market has been closed since Wednesday, in observation of the full moon holiday, the FOMC decision will be reflected in next week's trading.

Interest rates
% p.a.

	Aug 29	Sept 5	Sept 12	Sept 16
Overnight call	2.50	2.50	2.50	2.50
3-month CD fixing	2.66	2.66	2.66	2.66
1-year MSB	2.67	2.71	2.67	2.66
3-year Treasury bond	2.91	2.99	2.91	2.87
3-year corporate bond (AA-)	3.28	3.37	3.31	3.27

Deposit changes at deposit money banks
KRW tn

	June	July	August	Sept 1-12
Total deposits	14.9	-21.4	13.4	1.4
Demand	5.7	-8.3	3.7	-0.7
Time and savings	9.1	-13.1	9.7	2.1

Source: BoK, Customs Office, MOTIE, NSO, and J.P. Morgan

ASEAN

- **Growth in the Philippines continues to outperform, driven by government spending**
- **BSP to keep policy on hold in 2013—change in SDA investment rules driving money, but not loan growth**
- **Constructive fiscal and political dynamics to elicit additional rating upgrade, perhaps before end of year**

The Philippines' strong growth performance last year is set to be repeated this year. Growth surged 6.8% in 2012 from 3.6% in 2011, and this year we have it forecast at 7.1%, after upside GDP surprises in 1Q and 2Q. A sharp recovery in exports led growth last year, while this year government spending has driven it. Government spending should continue to support growth as activity moderates in 2H from its robust 1H pace.

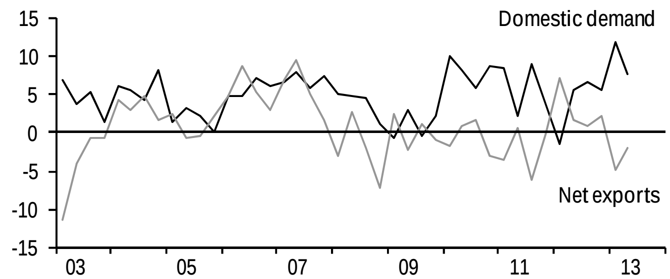
BSP maintained its policy rate at 3.5% last week and kept a neutral tone. We had been expecting another 50bp cut in the special deposit account (SDA) rate this year, but this looks increasingly unlikely, as reserve money and M3 growth have picked up quickly due to BSP's new rules limiting access to SDAs by investment trust funds. While the spike in money growth is probably only temporary (and so far is not transmitting to more general loan growth), BSP will likely be reluctant to lower SDA rates any further. We now expect SDAs to remain at 2.0% into 2014.

The fiscal deficit widened in July, but the government is on pace to meet its 2.0%-of-GDP deficit target this year. Along with strong growth, a 2%-of-GDP deficit will keep debt-to-GDP on a declining path. We forecast debt-to-GDP will fall to 43% of GDP by the end of 2015 from 51.5% at the end of last year. The constructive debt outlook, combined with greater political certainty and a solid BoP position, should lead to more rating upgrades in coming years. In particular, we expect Moody's to upgrade the Philippines to Baa3 this year, leaving the country rated investment grade by all three major agencies.

Growth continues to outperform

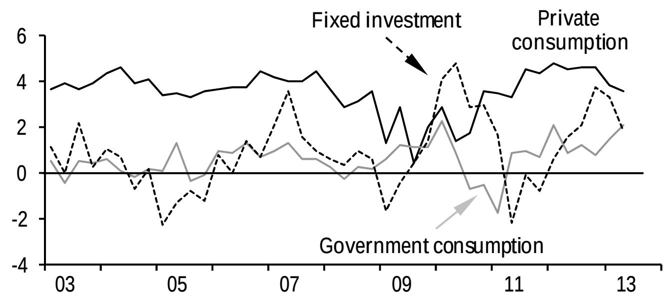
The economy expanded 5.7%q/q saar in 2Q after a 9.6% surge in 1Q. This left growth a bit stronger than expected at 7.5%oya (consensus: 7.2%). Similar to 1Q, domestic demand drove growth, while external demand was a drag. In particular, government spending was strong for a second straight quarter, up 25.0%q/q saar versus 29.9% in 1Q, while private consumption, which accounts for around 70% of GDP, rose 4.7%, about the same pace as in the two previous quarters. Exports shrank again, down 8.7% compared to a 20.3% decline in 1Q, while imports fell by a modest 0.8% in 2Q versus a larger 12.3% fall in 1Q. As a result, the drag from

Philippines: contributions to growth
%-pt contribution to %oya headline growth



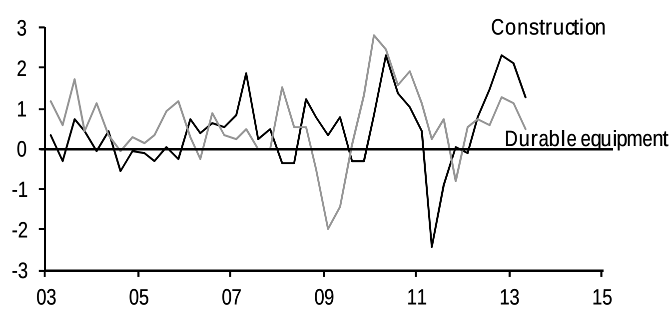
Source: National Statistics and Coordination Board (NSCB)

Philippines: contributions to growth
%-pt contribution to %oya headline growth



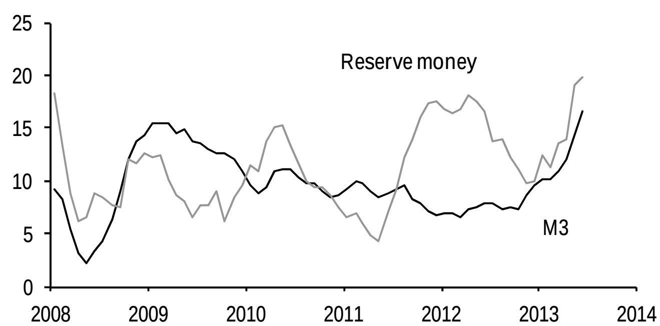
Source: NSCB

Philippines: gross fixed capital formation
%-pt contribution to %oya GDP growth



Source: NSCB

Philippines: monetary aggregates
%oya, 3mma



Source: BSP

net trade in %oya terms moderated to -2.0%-pts from -4.9%-pts in 1Q. The only very large difference from the 1Q report was fixed investment, which after surging 95.8% in 1Q, showed payback in 2Q by shrinking 33.1%. This series tends to be volatile, so we are not reading too much into the choppiness. From the supply side, agriculture output fell, while industry rose 6.0% and services rose 7.3%.

GDP growth in the Philippines has surprised on the upside for most of the last year and a half. In 2012, most of the upside surprise came from net exports, while this year it has come from government spending. The government does not release a breakdown between private and public sector investment, but it does release public spending on infrastructure, which has surged this year. Thus, we suspect that much of the strength in investment is coming from public sector spending. We expect government spending to remain supportive, but it is not likely to remain as strong. Thus, we look for 2H growth to moderate to a 5.3% annualized pace from 7.6% in 1H.

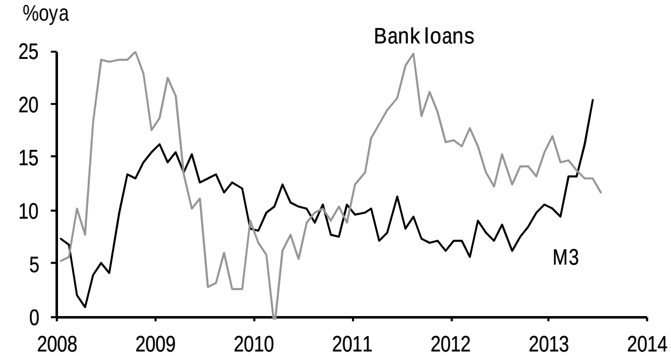
Inflation not likely to follow money growth

BSP announced earlier this year that investment trusts must reduce some of their placements in SDAs (30% by the end of July and the rest by the end of November). As a result, this cash has been pushed into bank accounts, which has led to a surge in reserve money and M3 growth. However, loan growth has continued to slide, as demand for new loans has not changed. Loan growth in the Philippines has lagged the rest of the region in recent years, which has not been due to tight liquidity conditions onshore. BSP noted in its statement last week that the increase in M3 growth is expected to be only temporary. Historically, inflation has been driven by supply-side price pressures in the Philippines. Thus, as long as food and energy prices remain contained, price pressures should, too. In August, inflation rose only 2.1%oya versus BSP's target of 4%+/1%. Unless inflation gets out of hand, we do not expect BSP to change its policy or SDA rates this year, as the economy is enjoying strong growth and tame inflation right now.

Waiting for Moody's

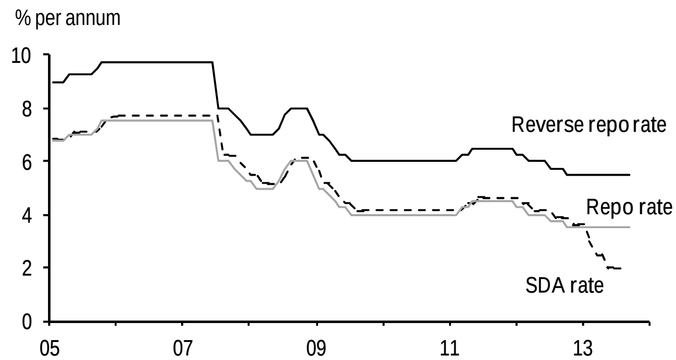
S&P and Fitch upgraded the Philippines to BBB- earlier this year, and Moody's placed the country on review for possible upgrade last July. If Moody's moves, the Philippines would be rated investment grade by all of the major agencies. Philippines local- and foreign-currency bonds already trade at levels consistent with a rating several notches higher, so the impact on government borrowing costs from another upgrade will likely be negligible. Nevertheless, becoming investment grade across the board may boost domestic sentiment and would give the president more political capital to push through economic reforms in coming years.

Philippines: credit and M3



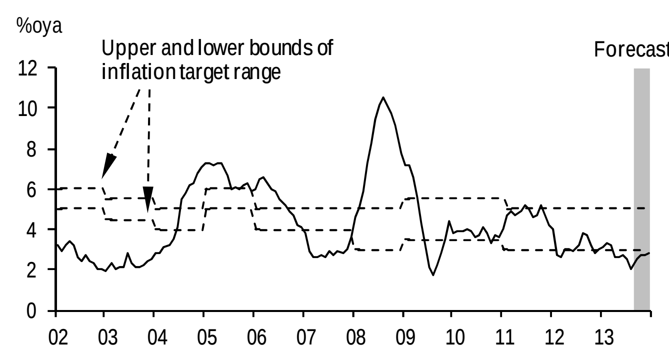
Source: BSP

Philippines: BSP policy rates



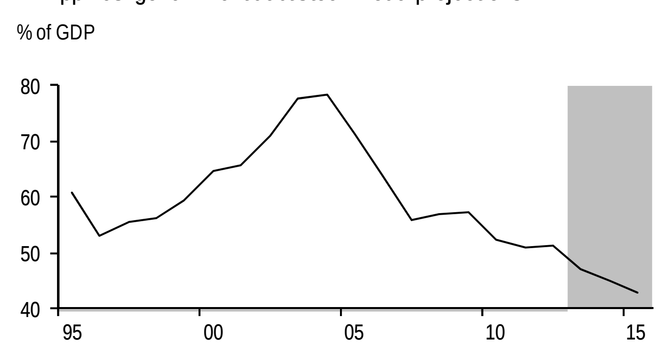
Source: BSP

Philippines: consumer prices



Source: NSO

Philippines: government debt stock model projections



Source: Bureau of Treasury and J.P. Morgan forecasts

ASEAN

Indonesia:

Data releases and forecasts

Week of September 23 – 27

No data releases.

Review of past week's data

No data released.

Malaysia:

Data releases and forecasts

Week of September 23 – 27

No data releases.

Review of past week's data

Consumer prices (Sep 18)
% change

	Jun	Jul	Aug	
All items, %oya	1.8	2.0	~~2.1~~	*1.9*
%m/m sa	0.1	0.2	~~0.2~~	*0.1*

August consumer prices rose 0.1%m/m sa, about the same rate as in the last 12 months. This left inflation up 2.0%3m/3m saar and up 1.9%oya. Excluding the volatiles, core prices (ex. food and energy) were also soft, up 0.1%m/m sa, which left the trend rate up 1.6%3m/3m saar. This left core prices up only 1.2%oya. As has been the case for several months now, most subcategories in the index were subdued, especially following the modest increases seen during Ramadan in July, and were surprisingly soft during August, given the Eid celebrations that follow the fasting month. The modest domestic inflationary pressures are likely also due in part to subdued food pressures globally.

The early September hike in RON95 motor gasoline and diesel prices is expected to add 0.7-0.8%-pt to CPI inflation (assuming a combined 7.4% weight in the CPI basket), which could lift 4Q13 inflation to 2.5-3.0%oya. The price hikes at this point do not change the policy rate outlook, which is expected to remain at 3.00% through 2013—though J.P. Morgan is watchful for further pass-through of the price increases, especially in view of the currently tight margins in certain product categories.

Philippines:

Data releases and forecasts

Week of September 23 – 27

		Apr	May	Jul	Jul
Wed Sep 25 9:00am	Merchandise trade US$ bn, nsa				
	Imports	5.1	5.3	4.9	5.2
	%oya	7.4	-2.4	-4.8	5.4

		May	Jun	Jul	Aug
During the week	Government budget PHP bn				
	Balance	-13.2	-8.5	-53.2	7.4
	Revenue	154.0	131.1	144.6	157.7
	Expenditure	167.2	139.5	197.8	150.3

Review of past week's data

OFW remittances (Sep 16)
US$ bn nsa

	May	Jun		Jul	
%oya	5.3	5.8		~~8.5~~	*6.6*
%m/m sa	-0.4	~~4.9~~	*4.7*	~~1.5~~	*-2.9*

Overseas foreign worker (OFW) remittances retreated 2.9%m/m sa in July after the 4.7% spurt in June, leaving them up 8.3%3m/3m saar. While their growth trend remains in the single digits, remittances are now growing at their fastest pace of the year. In unadjusted level terms, remittances were US$1.93 billion compared to US$1.92 billion in June, resulting in a 6.6%oya gain.

OFW remittances tend to be choppy, and they have been soft most of this year. Thus, we have been waiting for a strong bounce to come. So far, the June and July numbers hardly constitute a strong bounce, but they are at least lifting remittance levels above their 1H lows. Remittances are now up 4.6%ytd, and we are forecasting 5.0% growth for the entire year. This would still leave remittance growth at its slowest pace since the modest 0.3% contraction in 2001.

From a BoP perspective, the current account remains the main driver of the BoP surplus, even though portfolio inflows have also become an increasingly important flow. We expect steady remittance inflows, along with BPO service exports, to remain the backstop of large current account surpluses, despite the Philippines' persistent trade deficits.

Source: Central Bureau of Statistics, Indonesia; Department of Statistics, Malaysia; National Statistical Coordination Board, National Statistics Office, Philippines; J.P. Morgan forecasts

Singapore:
Data releases and forecasts

Week of September 23 – 27

Mon Sep 23 1:00pm — Consumer prices
% change

	May	Jun	Jul	Aug
All items, %oya	1.6	1.8	1.9	2.4
%m/m sa	0.4	0.5	0.0	0.9

Thu Sep 26 1:00pm — Industrial production
% change

	May	Jun	Jul	Aug
%oya	3.0	-4.2	2.7	6.5
%m/m sa	1.4	-2.0	-1.9	1.8

Review of past week's data

Merchandise trade (Sep 17)
US$ bn nsa

	Jun		Jul		Aug	
Trade balance	~~3.7~~	*3.6*	~~2.8~~	*2.6*	~~4.8~~	*3.2*
Exports	~~33.3~~	*33.2*	~~35.2~~	*35.0*	~~36.0~~	*34.1*
Non-oil domestic	~~11.4~~	*11.3*	~~11.9~~	*11.7*	~~12.1~~	*10.8*
%m/m sa	~~0.5~~	*-0.1*	~~-1.4~~	*-2.3*	~~1.4~~	*-3.8*
%oya US$ terms	~~-7.6~~	*-8.1*	~~-1.3~~	*-2.5*	~~2.8~~	*-8.0*

August non-oil domestic exports (NODX) fell 3.8%m/m sa in US$ terms, leaving them down 12.9%3m/3m saar. Similar to July, the softness was broad-based. As a result, NODX were weaker than expected, at -8.0%oya. The monthly NODX decline in August reflected drops in all of the major components. Electronics fell 3.2%m/m sa, while pharmaceuticals were down 1.7% and "other" exports fell 4.5%. NODX tend to be choppy, so we will not read too much into even two months of soft data, but it is striking that electronics and pharmaceuticals contracted 18.6%3m/3m saar and 82.6% in August (other exports actually rose 27.3% despite the monthly decline).

Following the surge in 2Q manufacturing output (32.1% annualized), some cooling in growth is only to be expected in 3Q. June and July IP figures have shown as much, but NODX growth has been particularly weak, in contrast with the improving export trend across most of the region. This could be due to high inventories, for which we do not have good data—but this may be too simplistic an interpretation (plus, the one inventory datapoint we do have from the PMI does not show high inventories). Perhaps the weak NODX performance reflects problems in data categorization, as the electronics sector, in particular, has undergone a lot of transition in recent years. It is possible that some products are not being accurately included as domestic exports or that the accounting classification for service versus goods exports is becoming blurred. And, of course, the weaker electronics trend in Singapore exports relative to northern neighbors may just reflect a difference in tech product mix between more traditional PC and newer tablet production in each of these countries.

Thailand:
Data releases and forecasts

Week of September 23 – 27

Fri Sep 27 — Manufacturing production
% change

	May	Jun	Jul	Aug
%oya	-7.5	-3.2	-4.5	-1.3
%m/m sa	-0.3	1.5	-2.5	1.8

Review of past week's data

No data released.

Vietnam:
Data releases and forecasts

Week of September 23 – 27

Wed Sep 24 — Consumer prices
% change

	Jun	Jul	Aug	Sep
%oya	6.7	7.3	7.5	6.8
%m/m sa	0.6	0.8	1.0	1.2

Review of past week's data

No data released.

Source: Singapore Department of Statistics; Singapore Economic Development Board; Bank of Thailand; Office of Industrial Economics, Thailand; General Statistics Office, Vietnam; J.P. Morgan forecasts

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India

- **RBI starts normalizing the yield curve by partially rolling back liquidity measures and raising policy rates**
- **We expect liquidity measures to continue to be unwound, but accompanied by another policy hike later this year**
- **WPI inflation breaches 6% in August and momentum rises on food price shocks and currency pass-through**

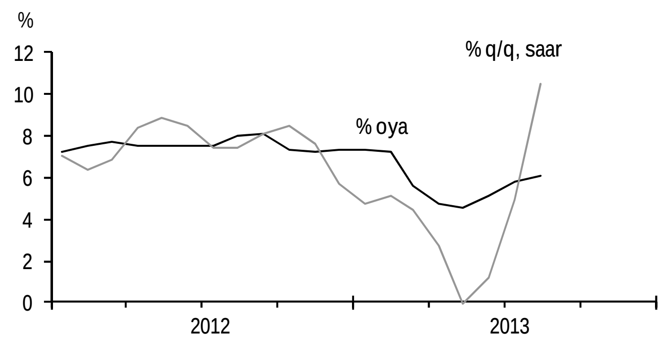
In his maiden policy meeting, India's new RBI governor set out in earnest to try to normalize India's inverted yield curve. With the currency 10% stronger over the last three weeks, the RBI began unwinding emergency measures by reducing the upper end of the rate corridor by 75bp, as we had anticipated. Simultaneously, however, the central bank surprised positively by increasing the key policy rate by 25bp in an important signal that even though its fight against the currency may have become less acute for now, the fight against inflation is ongoing. The RBI also signaled that it will pursue further normalization in the weeks to come, and we expect the emergency measures to gradually be dismantled contingent on the currency stabilizing. It is important, however, that the central bank underscore its commitment to inflation management to keep currency expectations anchored in the absence of the short-term interest rate defense. With meaningful pass-through expected from a weaker currency to domestic prices, we pencil in another policy rate hike in 4Q.

It's equally important, however, that authorities don't leave all the heavy lifting to the central bank. Markets are still awaiting a decisive hike in fuel prices to underscore the government's commitment to its fiscal target for the year. More generally, if the government can reduce the fiscal and current account deficit and the RBI can establish inflation management as its nominal anchor, India might be far better positioned to withstand the impact of any future taper by the Fed than it was earlier this year.

RBI begins to normalize the yield curve

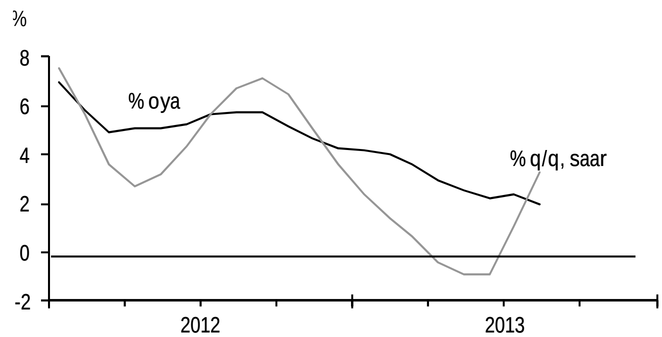
India's central bank partially unwound the emergency tightening measures put in place in July but simultaneously raised policy rates—thereby beginning the process of normalizing the yield curve—to signal that it will continue to fight against rising inflation. The partial unwinding of the liquidity measures was in line with our expectation—a 75bp reduction to 9.5% in the MSF requirement, some relief on banks' daily holding of cash reserve requirements (99% reduced to 95%), and no change in the amount that banks can borrow from the normal policy window (0.5% of their own deposits).

WPI momentum surges again in August



Source: Ministry of Commerce

Core inflation still contained but momentum picks up



Source: Ministry of Commerce

Additionally, however, the RBI raised the policy rate by 25bp to 7.5%—something we and markets had not expected just yet. We had believed that a decisive increase in repo rates would accompany a dismantling of the short-term interest rate defense. However, the central bank should be commended for starting that process, and sending a clear signal that—even after the liquidity measures are unwound—policy rates would have to be higher to combat inflation pressures emanating from the pass-through of the sharp rupee depreciation seen over the last four months.

Expect more steepening

In the press conference that followed, the governor made clear that he intends to bring the repo-MSF gap back down to 100bp. We therefore expect that if the currency continues to be supported, the trade deficit remains relatively contained, and the capital outflows are replaced by inflows under the FCNR/bank borrowing scheme, the RBI will be inclined to continue with the unwinding process even before the review at the end of October. The sequence we envisage is that the MSF rate will first be brought down, in steps, to be 100bp above the repo rate. Once that happens, bank liquidity restrictions will be eased such that the repo becomes the marginal—not inframarginal—cost of funds.

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Similarly, we believe the timing and pace of any future rate hikes will be contingent on the data. The policy statement indicated that the disinflationary forces from a strong harvest and a negative output gap will have to contend with the pass-through of rupee depreciation into domestic prices. Further it made several references to the elevated nature of retail inflation. With retail inflation expected to remain elevated and the pass-through from currency weakness expected to be meaningful, we pencil in another rate hike in 4Q13.

WPI surges again breaching 6%oya

For a third consecutive month, WPI prices surged more than 1% sequentially (m/m, seasonally adjusted) with August inflation printing at 6.1%oya (+1.2%m/m sa) and June inflation revised up from 4.9% to 5.2%. The annualized, quarterly momentum of WPI inflation is now running at 10.5%—similar to the double-digit growth of retail price inflation. The acceleration of the overall index was underpinned by surging food prices, which rose 6%m/m. In particular, vegetable prices jumped 15%m/m—supported, in turn, by a 51% increase in onion prices over the last month. However food prices and consequently headline inflation should moderate as supply and transport bottlenecks ease after unusually strong rains (for this season) in parts of the country and a strong monsoon boosts harvests.

FX depreciation has also contributed significantly over the last three months to rising inflation pressures. Firming global crude prices and a weaker rupee drove up fuel prices 1.3%m/m sa in August—the third straight sequential increase over 1%. On a sequential, annualized basis (3m/3m saar) fuel inflation is now running at 11%—as opposed to contracting at nearly 4% as it did back in May, before the rupee began to weaken. Prices of nonfood primary articles—which are largely imported commodities—surprisingly contracted 0.8% in August, but this appears to be more of a payback following sharp increases the previous three months. On a quarterly, annualized basis (q/q saar) inflation of these commodities is running above 12% due to rupee weakness over the last three months.

Core momentum, while not yet threatening, ticks up again

Core inflation slowed to 1.9%oya in August from 2.4%oya in July largely on base effects, but quarterly momentum has picked up. From April to June—before the impact of the sharp depreciation was felt on the economy—the trend in core inflation was running in negative territory as demand had softened and input price shocks had faded. The dynamic has since shifted. Although August core prices rose just 0.3%m/m sa, this followed a 0.7%m/m sa increase in July. On a quarterly, annualized basis, growth of core inflation has risen to 3.1% from negative territory in June—a swing of 4%-pts in three months.

While the current growth rate may not be uncomfortably high just yet for policymakers, it reveals one of two things—either demand is stronger than reflected by GDP growth, allowing producers to pass on some price increases or, more worryingly, margin compression has been so acute that firms have no option but to pass on some input price increases to output prices, notwithstanding the volume implications. It is perhaps a combination of these phenomena that explains why core CPI inflation is running above 8%. Furthermore, what these dynamics suggest is that further shocks to input prices—through either a weaker rupee or increasing global commodity prices—will continue to manifest themselves in the rising momentum of core inflation.

Data releases and forecasts

Week of September 23 – 27

No data releases.

Review of week's data

Wholesale prices (Sep 16)
% oya

	Jun		Jul	Aug	
Overall	~~4.9~~	*5.2*	5.8	___	*6.1*
Primary	~~8.1~~	*8.8*	9.0	___	*11.7*
Energy group	~~7.1~~	*7.5*	11.3	___	*11.3*
Manu. products	~~2.8~~	*2.9*	2.8	___	*1.9*

RBI monetary policy meeting (Sep 20)
Bp

	Jun	Jul	Sep	
Repo rate	7.50	7.25	7.25	*7.50*

Source: Central Statistical Organization, Government of India; Ministry of Commerce, Government of India; Markit; Reserve Bank of India

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Asia focus: a mixed picture of tech exports

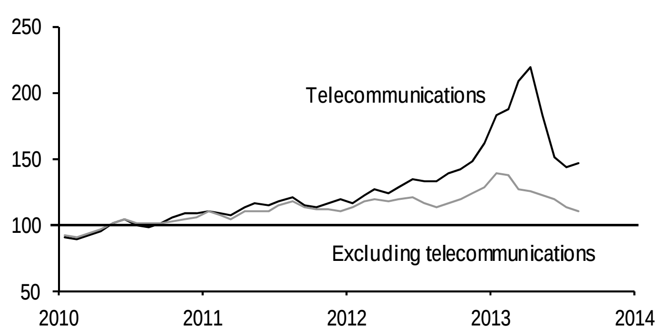
With the global PMI, particularly in the developed markets (DM), recently rising, the forecast assumes that the lift should be reflected in stronger exports in Asia. Here, the tech sector tends to serve as a useful barometer of global activity given its historical sensitivity to the global cycle. For EM Asia, although electronics has declined in the past decade as a share of total exports, it remains important, accounting for between 42% of total exports in Taiwan and 15% in Thailand, with the regional aggregate at 28% in 2012 (first chart).

While the DM manufacturing lift should generally be positive for tech producers in Asia, nuances in the tech cycle suggest that firmer DM demand may not lift all tech boats equally.

Here, there are two points worth making about the tech cycle since 2009 (see "Tech product cycles mixing up EM Asia's cyclical signals," *GDW*, Feb 22). The first is that the demand for electronics has seen a bifurcation between mobile computing devices (MCD) and non-MCD and this is clearly reflected in the US import data, which serve as a useful proxy of DM final demand. Indeed, the traditional non-MCD sector has softened over the course of 2013 even as MCD imports have strengthened, albeit with a good deal of volatility (second chart). The second point is that Asia's tech supply chain appears to be separated between MCD and non-MCD producers, with the North Asian producers of China, Korea, and Taiwan more linked to the MCD cycle while the ASEAN-3 of Malaysia, Singapore, and Thailand appear to be more exposed to the non-MCD cycle, which remained soft in 3Q13 (third and fourth charts). Separately, China's export data have been distorted by invoicing issues in 2012, and this continues to complicate the message from China's tech export data (chart below and see "An alternative picture of China's trade data," *GDW*, June 28).

China: electronics exports

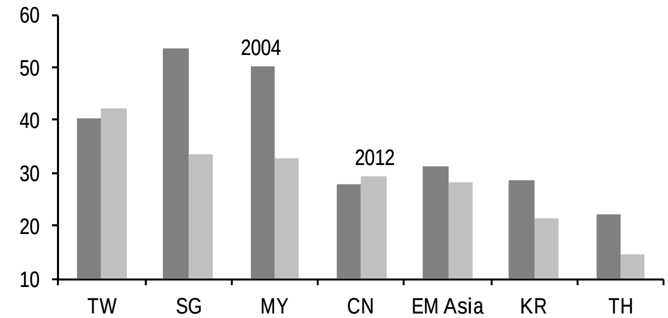
Index, 2010=100, 2mma, sa, US$ terms



Source: CEIC and J.P. Morgan

Emerging Asia: share of electronics in exports

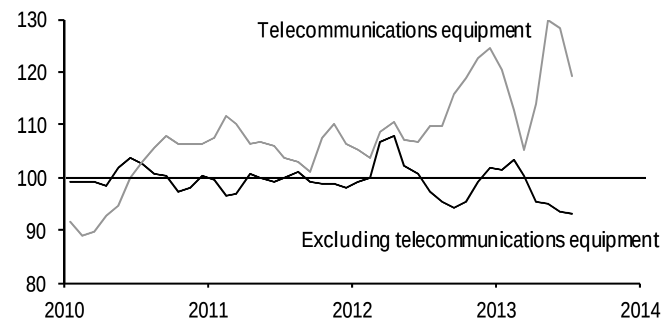
% total exports



Source; CEIC and J.P. Morgan

US: electronics imports

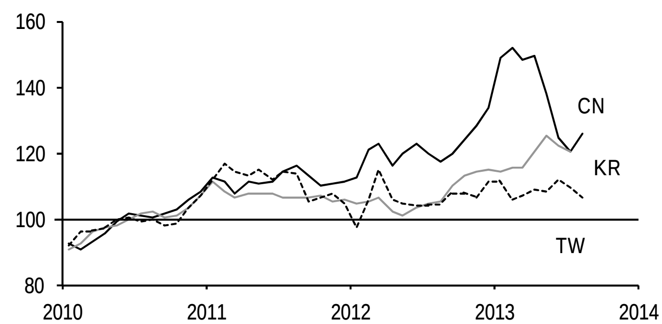
Index, 2010=100, 2mma, sa, US$ terms



Source: CEIC and J.P. Morgan

North Asia: electronics exports

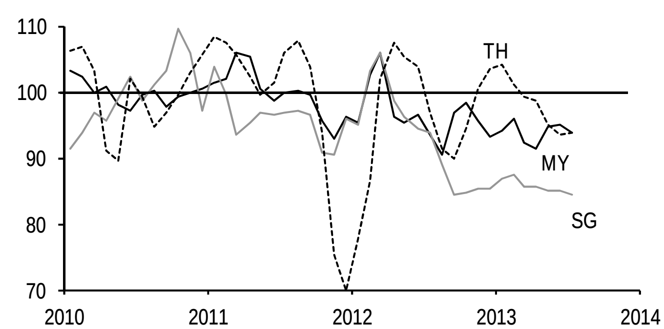
Index, 2010=100, 2mma, sa, US$ terms



Source: CEIC and J.P. Morgan

ASEAN: electronics exports

Index, 2000=100, 2mma, sa, US$ terms



Source: CEIC and J.P. Morgan

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US economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
23 Sep Manufacturing PMI (8:58am) Sep flash 54.0 Atlanta Fed President Lockhart speaks in New York (9:20am) New York Fed President Dudley speaks (9:30am) Dallas Fed President Fisher speaks in Texas (1:30pm)	24 Sep S&P/Case-Shiller HPI (9:00am) Jul 0.9% (12.7%oya) FHFA HPI (9:00am) Jul 0.9% (8.6%oya) Consumer confidence (10:00am) Sep 79.5 Richmond Fed survey (10:00am) Sep Auction 2 year note $33 bn Cleveland Fed President Pianalto speaks in Chicago (9:30am) Kansas City Fed President George gives remarks in Chicago (1:00pm)	25 Sep Durable goods (8:30am) Aug -0.3% Ex transportation 0.5% New home sales (10:00am) Aug 420,000 Financial accounts (12:00pm) 2Q Auction 5 year note $35 bn	26 Sep Initial claims (8:30am) w/e Sep 21 330,000 Real GDP (8:30am) 2Q final 2.9% Pending home sales (10:00am) Aug 0.0% KC Fed survey (11:00am) Sep Auction 7 year note $29 bn Fed Governor Stein speaks on monetary policy in Frankfurt (10:10am) Minneapolis Fed President Kocherlakota speaks in Michigan (12:15pm) Kansas City Fed President George speaks on economy in Denver (9:15pm)	27 Sep Personal income (8:30am) Aug 0.4% Real consumption 0.1% Core PCE deflator 0.07% (1.2%oya) Consumer sentiment (9:55am) Sep final 78.0 Chicago Fed President Evans speaks on economy in Oslo (5:45am and 10:15am) Boston Fed President Rosengren gives remarks in New York (8:30am) New York Fed President Dudley speaks on economy in New York (2:00pm)
30 Sep Chicago PMI (9:45am) Sep Dallas Fed survey (10:30am) Sep	1 Oct Manufacturing PMI (8:58am) Sep final ISM manufacturing (10:00am) Sep Construction spending (10:00am) Aug Light vehicle sales Sep Fed Vice Chair Yellen speaks at Economic Club of New York	2 Oct ADP employment (8:15am) Sep Fed Chairman Bernanke speaks on community banks in St. Louis Boston Fed President Rosengren speaks on economy in Vermont (12:00pm)	3 Oct Initial claims (8:30am) w/e Sep 28 ISM nonmanufacturing (10:00am) Sep Factory orders (10:00am) Aug Chain store sales Sep Announce 3 year note $30 bn Announce 10 year note (r) $21 bn Announce 30 year bond (r) $13 bn San Francisco Fed President Williams speaks in San Diego (11:00am) Dallas Fed President Fisher speaks on economy in Dallas (12:30pm) Fed Governor Powell speaks (1:30pm)	4 Oct Employment (8:30am) Sep New York Fed President Dudley gives remarks in New York (9:15am) Fed Governor Stein speaks at conference in New York (9:30am) Minneapolis Fed President Kocherlakota speaks on monetary policy in Minnesota (1:45pm)
7 Oct Consumer credit (3:00pm) Aug	8 Oct NFIB survey (7:30am) Sep International trade (8:30am) Aug JOLTS (10:00am) Aug Auction 3 year note $30 bn Philadelphia Fed President Plosser (12:30pm)	9 Oct Wholesale trade (10:00am) Aug Auction 10 year note (r) $21 bn FOMC minutes	10 Oct Initial claims (8:30am) w/e Oct 5 Import prices (8:30am) Sep Federal budget (2:00pm) FY13 Auction 30 year bond (r) $13 bn Announce 30 year TIPS (r) $7 bn	11 Oct Retail sales (8:30am) Sep PPI (8:30am) Sep Consumer sentiment (9:55am) Oct preliminary Business inventories (10:00am) Aug
14 Oct Columbus Day, bond market closed	15 Oct Empire State survey (8:30am) Oct	16 Oct CPI (8:30am) Sep TIC data (9:00am) Aug NAHB survey (10:00am) Oct Beige book (2:00pm)	17 Oct Initial claims (8:30am) w/e Oct 12 Housing starts (8:30am) Sep Industrial production (9:15am) Sep Philadelphia Fed survey (10:00am) Oct Auction 30 year TIPS (r) $7 bn Announce 2 year note $33 bn Announce 5 year note $35 bn Announce 7 year note $29 bn Dallas Fed President Fisher speaks to Economic Club of New York (7:45am) Minneapolis Fed President Kocherlakota on monetary policy in Montana (2:45pm)	18 Oct Leading indicators (10:00am) Sep

Times shown are local.

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Euro area economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
23 Sep Euro area: PMI Mfg, services, composite (10:00am) Sep Mfg: 52.0 Index, sa Services: 51.5 Index, sa Composite: 52.0 Index, sa Germany: PMI Mfg, services, composite (9:30am) Sep France: PMI Mfg, services, composite (9:00am) Sep ECB's Draghi speaks to Brussels	24 Sep Germany: IFO bus. survey (10:00am) Sep Bus. climate: 107.7 Index, sa Belgium: BNB bus. conf. (3:00pm) Sep Netherlands: CBS bus. conf. (9:30am) Sep ECB's Constâncio speaks to Madrid ECB's Mersch speaks in Vienna	25 Sep Germany: GfK cons. conf. (8:00am) Oct France: INSEE bus. conf. (8:45am) Sep Italy: ISAE cons. conf. (10:00am) Sep ECB's Asmussen speaks in Frankfurt	26 Sep Euro area: M3 (10:00am) Aug France: INSEE cons. conf. (8:45am) Sep ECB's Asmussen speaks in Berlin ECB's Mersch and Constâncio speak in Frankfurt ECB's Cœuré speaks in New York	27 Sep Euro area: EC bus. conf. (11:00am) Sep EC cons. conf. (11:00am) Sep -14.9% bal Germany: CPI 6 states and prelim (8:00am) Sep 1.5%oya France: Cons. of mfg goods (8:45am) Aug GDP final (8:45am) 2Q Italy: ISAE bus. conf. (10:00am) Sep Spain: CPI prelim (9:00am) Sep 0.7%oya Belgium: CPI (3:00pm) Sep ECB's Draghi speaks in Milan
30 Sep Euro area: HICP flash (11:00am) Sep Germany: Import prices (8.00am) Aug France: PPI (8:45am) Aug Italy: PPI (10:00am) Aug CPI final prelim (11:00am) Sep	1 Oct Euro area: PMI Mfg (10:00am) Sep Unemployment rate (11:00am) Aug Germany: Employment (9:55am) Sep PMI Mfg (9:55am) Sep Unemployment (9:55am) Sep France: PMI Mfg (9:50am) Sep Italy: PMI Mfg (9:45am) Sep Spain: PMI Mfg (9:15am) Sep	2 Oct Euro area: PPI (11:00am) Aug ECB rate announcement (1:45pm) Oct No change expected MFI interest rates for Euro area (10:00am) Aug	3 Oct Euro area: PMI services & composite (10:00am) Sep Retail sales (11:00am) Aug Germany: PMI services & composite (9:55am) Sep France: PMI services & composite (9:50am) Sep Italy: PMI services & composite (9:45am) Sep Spain: PMI services & composite (9:15am) Sep	4 Oct Germany: PPI (8:00am) Aug
7 Oct Spain: CPI final (9:00am) Sep	8 Oct Germany: Foreign trade (8:00am) Aug Mfg orders (12:00pm) Aug France: Foreign trade (8:45am) Aug Monthly budget situation (8:45am) Aug	9 Oct Germany: Industrial production (12:00pm) Aug	10 Oct Euro area: ECB monthly bulletin (10:00am) Oct France: Industrial production (8:45am) Aug Italy: Industrial production (10:00am) Aug Netherlands: CPI (9:30am) Sep	11 Oct Germany: CPI 6 states and prelim (8:00am) Sep CPI final (8:00am) Sep Italy: CPI final (10:00am) Sep Spain: HICP flash (9:00am) Sep
14 Oct Euro area: Industrial production (11:00am) Aug	15 Oct Germany: ZEW bus. survey (11:00am) Oct France: CPI final (8:45am) Sep	16 Oct Euro area: New car regs (8:00am) Aug Foreign trade (11:00am) Aug HICP final (11:00am) Sep Italy: Foreign trade (10:00am) Aug	17 Oct Euro area: Balance of payments (10:00am) Aug	18 Oct Belgium: BNB cons. conf. (3:00pm) Oct Netherlands: CBS cons. conf. (9:30am) Oct

Highlighted data are scheduled for release on or after the date shown. Times shown are local.

Japan economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
23 Sep *Holiday: Japan*	24 Sep	25 Sep Corporate service prices (8:50am) Aug 0.4%oya Shoko Chukin small firm sentiment Sep (2:00pm) 49.0, DI	26 Sep Auction 3-month bill	27 Sep Nationwide CPI (8:30am) Aug 0.7%oya Auction 2-year note
30 Sep PMI manufacturing (8:15am) Sep IP preliminary (8:50am) Aug Total retail sales (8:50am) Aug Housing starts (2:00pm) Aug	1 Oct All household spending (8:30am) Aug Unemployment rate (8:30am) Aug Job offers to applicants ratio (8:30am) Aug BoJ Tankan (8:50am) 3Q Nominal wages (10:30am) Aug Auto registrations (2:00pm) Sep Auction 10-year bond	2 Oct Monetary base (8:50am) Sep	3 Oct PMI services/composite (8:15am) Sep BoJ Monetary Policy Meeting Auction 3-month bill	4 Oct BoJ Monetary Policy Meeting and statement BoJ governor Kuroda's press conference (3:30pm)
7 Oct BoJ monthly economic report (2:00pm)	8 Oct Current account (8:50am) Aug Economy Watchers survey (2:00pm) Sep Auction 6-month bill Auction 10-year bond	9 Oct Minutes of Sep 4-5 BoJ Monetary Policy Meeting (8:50am) BoJ deputy governor Nakaso's address in Shimane prefecture (10:40am) Auction 2-month bill	10 Oct Bank lending (8:50am) Sep Private machinery orders (8:50am) Aug Tertiary sector activity index (8:50am) Aug Consumer sentiment (2:00pm) Sep Auction 3-month bill Auction 30-year bond	11 Oct M2 (8:50am) Sep Corporate goods prices (8:50am) Sep
During the week: CAO private consumption index Aug				
14 Oct *Holiday: Japan*	15 Oct IP final (1:30pm) Aug	16 Oct Auction 1-year note Auction 5-year note	17 Oct Reuters Tankan (8:30am) Oct Construction spending (2:00pm) Aug Auction 3-month bill	18 Oct BoJ deputy governor Iwata's speech at Chuo University (4:30pm)
During the week: Nationwide department store sales Sep				

Highlighted data are scheduled for release on or after the date shown. Times shown are local.

Canada economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
23 Sep	24 Sep Retail sales (8:30am) Jul <u>0.6%</u> Ex auto <u>0.3%</u> BoC Deputy Governor Lawrence Schembri speaks at the CFA Society of Ottawa, Ottawa, ON (12:45pm)	25 Sep	26 Sep CFIB Business Barometer Index (6:00am) Sep	27 Sep Payroll employment (8:30am) Jul
30 Sep Monthly GDP (8:30am) Jul IPPI (8:30am) Aug	1 Oct RBC manufacturing PMI (9:30am) Sep BoC Senior Deputy Governor Tiff Macklem speaks at the Economic Club of Canada, Toronto, ON (12:10am)	2 Oct	3 Oct	4 Oct Ivey PMI (10:00am) Sep
7 Oct Building permits (8:30am) Aug	8 Oct Housing starts (8:15am) Sep International trade (8:30am) Aug	9 Oct	10 Oct New housing price index (8:30am) Aug	11 Oct Labor Force Survey (8:30am) Sep BoC Business Outlook Survey (10:30am) 3Q BoC Senior Loan Officer Survey (10:30am) 3Q
14 Oct *Thanksgiving Day* *Markets closed*	15 Oct New vehicle sales (8:30am) Aug Existing home sales (9:00am) Sep Teranet/National Bank HP Index (9:00am) Aug	16 Oct Manufacturing sales (8:30am) Aug	17 Oct Nonresidential construction (8:30am) 3Q	18 Oct CPI (8:30am) Sep

All existing home sales are tentative. Times shown are local.

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Latin America economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
23 Sep Argentina Trade balance Aug Colombia: Trade balance Jul Mexico: Retail sales Jul 0.7%oya	24 Sep Argentina Industrial production Aug Brazil: Consumer confidence Sep Current account balance Aug BRL -5.1bn FDI Aug BRL 4.2bn Mexico: CPI Sep 1H Headline 0.23%2w/2w Core 0.22%2w/2w Headline 3.35%oya Core 2.45%oya Central bank reserves (prior week)	25 Sep Brazil: Fipe CP Sep 22 0.17%m/m nsa PPI Aug Mexico: Economic activity index Jul 1.1%oya	26 Sep Brazil: Unemployment rate Aug 5.6% Colombia: Current account 2Q13 Mexico: Trade balance Aug -US$1,604	27 Sep Argentina: Economic activity index Jul Brazil: IGP-M Sep 1.39% m/m nsa BCB credit report Aug Central government budget Aug BRL1.0bn Colombia: Central government budget Aug BanRep meeting On hold
During the week: Uruguay: Real GDP 2Q				
30 Sep Argentina: Construction activity Aug Brazil: Primary budget balance Aug Net debt as % of GDP Aug Chile: Manufacturing index Aug Retail sales Aug Unemployment Aug Colombia: Central government budget Aug Unemployment rate Aug Mexico: Banking credit Aug Budget balance Aug	1 Oct Argentina: Govt tax collection Sep Brazil: PMI Manufacturing Sep Trade balance Sep Peru: CPI Aug WPI Aug Mexico: Central bank reserves (prior week) Remittances Aug Manufacturing PMI (IMEF) Sep Services PMI (IMEF) Sep	2 Oct Argentina: Auto report Sep Brazil: Fipe CPI Sep IP Sep Chile: BCCh meeting minutes	3 Oct Brazil: COPOM meeting minutes PMI Services Aug Colombia: CPI Aug Mexico: Consumer confidence Sep Uruguay: CPI Sep Unemployment rate Aug	4 Oct Brazil: IGP-DI Aug IPCA Aug Colombia: PPI Sep
During the week: Brazil: Vehicle sales and production Sep Colombia: Vehicle sales and CPI Sep				
7 Oct Chile: Economic activity index Aug Mexico: Banamex economic survey	8 Oct Brazil: IGP-DI Sep Chile: CPI Sep Mexico: Central bank reserves (prior week) Gross fixed investment Jul	9 Oct Brazil: IPCA Sep COPOM meeting Chile: Trade balance Sep Mexico: CPI Sep	10 Oct Brazil: IGP-M 1st release Oct Mexico: Wage negotiations Sep Peru: BCRP meeting Trade balance Aug	11 Oct Colombia: BanRep minutes Mexico: Industrial production Aug
During the week: Brazil: Vehicle sales and production Sep Colombia: CPI Sep, Consumer Confidence Sep Mexico: Auto report Sep				
14 Oct Brazil: Caged formal job creation Sep Colombia: Vehicle sales Sep Uruguay: Industrial production Aug	15 Oct Argentina: CPI Sep Brazil: Retail sales Aug Tax collections Sep Peru: Economic Activity Index Aug Unemployment rate Sep Mexico: Central bank reserves (prior week)	16 Oct Brazil: IGP-10 Oct Economic Activity Index Aug	17 Oct Brazil: COPOM meeting minutes Chile: BCCh meeting	18 Oct Argentina: Economic activity index Aug Brazil: IGP-M 2nd release Oct IPCA-15 Oct Colombia: IP Aug Retail sales Aug Mexico: Unemployment rate Sep
During the week:				

UK economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
23 Sep BoE's Broadbent speaks in London.	24 Sep BBA Mortgage lending (9:30am) Aug BoE's Miles speaks in Newcastle BoE's Tucker speaks in London	25 Sep CBI distributive trades (11:00am) Sep Financial Policy Committee statement (9:30am)	26 Sep BoP (9:30am) 2Q Business investment final (9:30am) 2Q Real GDP final (9:30am) 2Q 0.7%q/q sa	27 Sep Nationwide HPI (7:00am) Sep Gfk cons. conf. (12:05am) Sep Index of services (9:30am) Jul
30 Sep M4 & M4 lending final (9:30am) Aug Net lending to individuals (9:30am) Aug	1 Oct PMI Mfg (9:30am) Sep	2 Oct BoE housing equity withdrawal (12:01am) 2Q PMI Construction (9:30am) Sep	3 Oct PMI Services (9:30am) Sep	4 Oct New car regs (8:00am) Sep
During the week: Halifax HPI Sep (1-4 Oct)				
7 Oct	8 Oct BCC economic survey (12:01am) 3Q BRC retail sales monitor (12:01am) Sep RICS HPI (12:01am) Sep	9 Oct BoE credit conditions survey (12:01am) 3Q Industrial production (9:30am) Aug Quoted mortgage interest rates (9:30am) Sep Trade balance (9:30am) Aug	10 Oct MPC rate announcement and asset purchase target (12:00pm) Oct No change expected	11 Oct Construction output (9:30am) Aug
14 Oct	15 Oct CPI (9:30am) Sep ONS HPI (9:30am) Aug PPI (9:30am) Sep	16 Oct Labor market report (9:30am) Sep	17 Oct Retail sales (9:30am) Sep	18 Oct

Times shown are local.

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Emerging Europe/Middle East/Africa economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
23 Sep Israel: BoI rate decision (2:00pm) no change	24 Sep Hungary: NBH rate decision (2:00pm) -20bp Poland: Retail sales (10:00am) Aug 2.3%oya Unemployment (10:00am) Aug 13.0% Turkey: Capacity utilization (2:30pm) Sep 75.2% *Holiday: South Africa*	25 Sep South Africa: BER consumer confidence (12:00pm) 3Q	26 Sep Czech Republic: CNB rate decision (1:00pm) no change *Holiday: Israel*	27 Sep Hungary: Current account (8:30am) 2Q €700mn Unemployment (9:00am) Jul
During the week: Russia: Current account final 2Q (27-30 Sep)				
30 Sep Hungary: PPI (9:00am) Jul Poland: Current account (2:00pm) 2Q NBP inflation expectations (2:00pm) Sep Romania: NBR rate decision -50bp Turkey: Foreign trade (10:00am) Aug South Africa: Private sector credit (8:00am) Aug Budget (2:00pm) Aug Trade balance (2:00pm) Aug *Holiday: Czech Republic*	1 Oct Czech Republic: PMI (9:30am) Sep Hungary: PMI (9:00am) Sep Poland: PMI (9:00am) Sep Russia: Manufacturing PMI (11:00am) Sep Turkey: PMI (10:00am) Sep South Africa: Vehicle sales Sep Kagiso PMI (11:00am) Sep	2 Oct Poland: NBP rate decision Romania: Retail sales (10:00am) Aug	3 Oct Turkey: CPI (10:00am) Sep PPI (10:00am) Sep	4 Oct Czech Republic: Retail sales (9:00am) Aug Hungary: Retail sales flash (9:00am) Aug
During the week: Russia: Current account 3Q (1-4 Oct), GDP final 3Q (1-2 Oct), CPI Sep (4-7 Oct)				
7 Oct Czech Republic: Industrial output (9:00am) Aug Trade balance (9:00am) Aug Romania: GDP final (10:00am) 2Q South Africa: Gross reserves (8:00am) Sep	8 Oct Hungary: Industrial output (9:00am) Aug Turkey: Industrial output (10:00am) Aug	9 Oct Czech Republic: CPI (9:00am) Sep Hungary: Trade balance (9:00am) Aug	10 Oct Romania: CPI (10:00am) Sep Industrial output (10:00am) Aug Trade balance (10:00am) Aug South Africa: Manufacturing output (1:00pm) Aug	11 Oct Czech Republic: Current account (10:00am) Aug Hungary: CPI (9:00am) Sep Poland: Current account (2:00pm) Aug Romania: Current account Aug Turkey: Current account (10:00am) Aug Unemployment (10:00am) Jul
During the week: Russia: Foreign trade Aug (9-10 Oct)				
14 Oct Russia: CBR rate decision Oct	15 Oct Czech Republic: PPI (9:00am) Sep Hungary: Industrial output (9:00am) Aug Poland: CPI (2:00pm) Sep Budget balance (3:00pm) Sep Israel: CPI (5:30pm) Sep *Holiday in Turkey*	16 Oct Poland: Average gross wages and Employment (2:00pm) Sep Core inflation (2:00pm) Sep South Africa: Retail sales (1:00pm) Aug Israel: GDP final (12:00pm) 3Q *Holiday in Turkey*	17 Oct Poland: Industrial output (2:00pm) Sep NBP minutes (2:00pm) PPI (2:00pm) Sep *Holiday in Turkey*	18 Oct *Holiday in Turkey*
During the week: Russia: Industrial output Sep (15-16 Oct, PPI Sep (16-17 Oct), Retail sales, Unemployment & Investment Sep (18-21 Oct)				

Times shown are local.

Non-Japan Asia economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
23 Sep China: Flash PMI (9:45am) Sep 50.6 Index, sa Hong Kong: CPI (4:30pm) Aug 4.3%oya Singapore: CPI (1:00pm) Aug 2.4%oya Taiwan: Unemployment rate (8:30am) Aug 4.18%, sa	24 Sep Vietnam: CPI Sep 6.8%oya	25 Sep New Zealand: Trade balance (10:45am) Aug -NZ$440mn Philippines: Imports (9:00am) Jul 5.4%oya Taiwan: Export orders (4:00pm) Aug 0.9%oya	26 Sep Hong Kong: Trade balance (4:30pm) Aug -HK$35.3bn Korea: Consumer survey (6:00am) Sep 106.0, Index Singapore: IP (1:00pm) Aug 6.5%oya Taiwan: IP (4:00pm) Aug 1.3%oya CBC monetary policy meeting (5:00pm) No change	27 Sep Korea: Current account balance (8:00am) Aug US$5.5bn Taiwan: Leading index (4:00pm) Aug Thailand: Mfg. production Aug -1.3%oya
During the week: Philippines: Budget balance Aug (23-26 Sep) PHP7.4bn Vietnam: Trade balance Sep -US$0.8bn; GDP 3Q 5.3%oya (25-27 Sep)				
30 Sep Australia: Pvt. sector credit (11:30am) Aug New Zealand: Building permits (10:45am) Aug NBNZ business confidence (2:00pm) Sep China: PMI mfg. (Markit) (9:45am) Aug Korea: IP (8:00am) Aug Thailand: PCI (2:30pm) Aug PII (2:30pm) Aug Trade balance (2:30pm) Aug	1 Oct Australia: Retail sales (11:30am) Aug RBA official rate announcement (2:30pm) China: PMI mfg. (NBS) (9:00am) Sep Indonesia: CPI (11:00am) Sep Trade balance (11:00am) Aug Korea: CPI (8:00am) Sep Trade balance (9:00am) Sep PMI mfg. (9:01am) Sep Taiwan: PMI mfg. (10:00am) Sep Thailand: CPI Sep *Holiday: China, Hong Kong*	2 Oct Australia: Building approvals (11:30am) Aug Trade balance (11:30am) Aug New Zealand: ANZ commodity price (2:00pm) Sep Singapore: PMI (9:30pm) Sep *Holiday: China, India*	3 Oct Hong Kong: Retail sales (4:30pm) Aug *Holiday: China, Korea*	4 Oct Malaysia: Trade balance (12:00pm) Aug Philippines: CPI (9:00am) Sep *Holiday: China*
During the week:				
7 Oct Taiwan: CPI (8:30am) Sep Trade balance (4:00pm) Sep *Holiday: Australia, China*	8 Oct Australia: ANZ job advertisements (11:30am) Sep Indonesia: BI monetary policy meeting	9 Oct Australia: NAB business confidence (11:30am) Sep Korea: Money supply (12:00pm) Aug *Holiday: Korea*	10 Oct Australia: Unemployment rate (11:30am) Sep New Zealand: Business NZ PMI (10:30am) Sep Korea: BoK monetary policy meeting Malaysia: IP (12:01pm) Aug Philippines: Exports (9:00am) Aug *Holiday: Taiwan*	11 Oct India: IP (5:30pm) Aug Korea: Export price index (6:00am) Sep Import price index (6:00am) Sep
During the week: China: Money supply Sep (10-15 Oct), Trade balance Sep (12 Oct) India: Trade balance Aug (10-15 Oct) Singapore: GDP flash 3Q (8-14 Oct)				
14 Oct China: CPI (9:30am) Sep PPI (9:30am) Sep India: WPI (12:00pm) Sep CPI (5:30pm) Sep Singapore: Retail sales (1:00pm) Aug *Holiday: Hong Kong, Indonesia*	15 Oct Australia: New motor vehicle sales (11:30am) Sep Philippines: OFW remittances Aug *Holiday: Indonesia, Malaysia, Singapore*	16 Oct Korea: Unemployment rate (8:00am) Sep Thailand: BoT monetary policy meeting (2:30pm)	17 Oct Hong Kong: Unemployment rate (4:30pm) Sep Korea: PPI (6:00am) Sep Singapore: NODX (8:30am) Sep	18 Oct China: FAI (10:00am) Sep GDP (10:00am) 3Q IP (10:00am) Sep Retail sales (10:00am) Sep

Times shown are local.

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Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
21 - 27 September	**23 September**	**24 September**	**25 September**	**26 September**	**27 September**
	China • Flash mfg PMI (Sep) **Euro area** • Flash PMI (Sep) • Draghi speech **Israel** • BoI mtg: no chg **United States** • Flash mfg PMI (Sep)	**Germany** • IFO bus survey (Sep) **Hungary** • NBH mtg: -20bp **United States** • C-S HPI (Jul) • CB cons conf (Sep)	**France** • INSEE bus conf (Sep) **Germany** • GfK cons conf (Oct) **Japan** • Shoko Chukin surv (Sep) **Taiwan** • Export orders (Aug) **United States** • Durable goods (Aug) • New home sales (Aug)	**Czech Republic** • CNB mtg: no chg **Euro area** • M3 (Aug) **France** • INSEE cons conf (Sep) **Singapore** • IP (Aug) **Taiwan** • IP (Aug) • CBC mtg: no chg **United Kingdom** • GDP revision (2Q) **United States** • GDP revision (2Q) • Pending home sales (Aug)	**Colombia** • BanRep mtg: no chg **Euro area** • EC cons conf fnl (Sep) • EC bus conf (Sep) • Draghi speech **Germany** • CPI prelim (Sep) **Italy** • ISAE bus conf (Sep) **Japan** • CPI (Aug) **Thailand** • IP (Aug) **United Kingdom** • GfK cons conf (Sep) **United States** • Personal income (Aug) • UMich cons snt fnl (Sep)
28 Sep - 4 Oct	**30 September**	**1 October**	**2 October**	**3 October**	**4 October**
Brazil • Vehicle sales (Sep) **Russia** • CPI (Sep)* * Released Oct 4-7	**China** • Markit mfg PMI final (Sep) **Euro area** • HICP flash (Sep) **Japan** • PMI mfg (Sep) • IP prelim (Aug) • Total retail sales (Aug) **Korea** • IP (Aug) **Romania** • BNR mtg: -50bp	**Australia** • RBA mtg: no chg **China** • NBS mfg PMI (Sep) **Euro area** • PMI mfg (Sep) • Unemployment rate (Aug) **Japan** • Labor mkt report (Aug) • BoJ Tankan (3Q) • Auto regs (Sep) **Korea** • Trade report (Sep) **United States** • ISM mfg (Sep) • Auto sales (Sep) **Global** • PMI mfg (Sep)	**Brazil** • IP (Sep) **Euro area** • ECB mtg: no chg • MFI int rates (Aug) **Poland** • NBP mtg: no chg **United States** • ADP employment (Sep) • Bernanke speech	**Brazil** • COPOM mtg mins (Sep) **Euro area** • PMI srv & all-ind fnl (Sep) • Retail sales (Aug) **Turkey** • CPI (Sep) **United States** • Factory orders (Aug) • ISM nonmfg (Sep) **Global** • PMI srv & all-ind (Sep)	**Brazil** • IPCA (Aug) **Japan** • BoJ MPM: no chg **United Kingdom** • Auto regs (Sep) **United States** • Employment (Sep)