
GLOBE AT A GLANCE – Andrew Wroblewski, London / Pierre Ellis, New York

Equities: Japan mixed, Europe higher. Japanese equity markets were mixed with the Nikkei index higher and the Topix index marginally lower. Other Asian markets were, however, mainly down, dragged lower by financial and mining shares. In contrast, European bourses fell shortly after opening but rose through morning trade more than recouping the ground lost initially.

Bonds: Japan higher, Europe mixed. Japanese government bonds rose across the curve. In contrast, European benchmark bonds were mixed with short-term maturities lower and long-term bonds higher.

Currencies: Stronger yen. The dollar fell against the yen throughout Asian and European hours, trading down below ¥/\$ 97.9. Against the euro, the US currency, saw little net change in Asian hours having seen a short-lived rise in early European trade fell back, it traded above \$/€1.29.

United Kingdom: Downside risks still underscored? The minutes from the April 8-9 BoE MPC meeting showed the committee to have been unanimous in regard to keeping Bank Rate at 0.5%.

United Kingdom: Labor market unraveling less rapidly? Claimant count unemployment increased

sizably again last month but less appreciably than in February.

United Kingdom: Record borrowing. Public sector finance data saw yet another worse-than-expected outcome last month, with net borrowing (PSNB) of £ 19.09 bln, the highest ever outcome.

United Kingdom: Less robust monetary data? The BoE said that March M4 growth was unchanged in M/M terms and down one percentage point (to 17.6%) on a Y/Y basis

Japan: Exports edge higher. The seasonally adjusted trade balance deteriorated slightly, staying in deficit, widening to -¥ 97.1 bln last month, albeit with exports showing a modest rise of 2.2%, the first increase since May last year.

Malaysia: Consumer prices fall. On the back of a larger-than-expected 0.2% M/M drop in the CPI, consumer price inflation fell from 3.7% Y/Y in February to 3.5% last month, an 11-month low.

Australia: Downward surprise to inflation. Undershooting expectations consumer price inflation fell from 3.7% Y/Y to 2.5% in Q1, a 1½-year low and right in the middle of the central bank's target-range (2-3%).

U.S. ECONOMIC AND CREDIT MARKET OUTLOOK – Pierre Ellis, New York

Treasuries gave back some ground Tuesday, with the two-year yield rising about two and a half basis points and the ten-year yield up six. The market strengthened modestly overnight, and more firmly in early trading, but sold off steeply at mid-morning—coincident with a strong rally in stocks touched off by Treasury Secretary Geithner's comment that "Currently, the vast majority of banks have more capital than they need to be considered well capitalized by their regulators." Stocks preserved, and built upon the early gains, over the rest of the day.

Economic data were limited to modestly downbeat weekly **chain store sales** reports. This was the second of four retail-April weeks, and commentary took a cooler tone, though neither survey group saw reason to shave its full-month comparable stores forecast.

The first week of the retail month put the pre-Easter week in comparison with more-normal weeks, both immediately prior and year-ago, and results for the second week were fully expected to pale in

comparison—if only because Easter Sunday itself represented a lost business day.

As it happened, sales were soft even relative to the adjusted expectations—putting, according to Redbook, "many retailers off plan for the week." That group saw unfavorable weather as a partial explanation, but ICSC/Goldman noted a potentially more ominous fading at "discounters and specialty stores, such as books and jewelry."

The loss of a Sunday may have hit particularly hard at such stores—so no message is being read of a new turn to extreme spending conservatism. Still, the hint of mild revival in consumer discretionary spending read in the pre-Easter results is now threatened a bit—and evidence of renewed enthusiasm in coming weeks will be imperative to sustain that particular "green shoot."

DAILY CALENDAR

There are no important economic indicators or appearances by Fed official formally scheduled today.

CANADA – Andrew Husby, New York

(Thursday) Rate hits lower bound. Surprising many, the Bank of Canada cut its overnight rate by 25 bp to 0.25% (Consensus: hold; DE: cut 25 bp). Conditional on the outlook for inflation, the BoC committed to holding the overnight rate at the current level (the effective lower bound) until the end of the second quarter of 2010.

While there has been speculation on the specific form that possible credit or quantitative easing would take, the statement only indicated that “the Bank retains considerable flexibility in the conduct of monetary policy at low interest rates,” but put off any further discussion, instead noting that the framework would be “outlined” in the *Monetary Policy Report Update* to be released on Thursday.

With respect to growth, the bank indicated that the “global recession has intensified and become more synchronous,” while the range of monetary and fiscal policy responses to stabilize the global financial system “have taken longer than expected to enact.” Because of this and deteriorating credit conditions, the statement noted that Canada’s downturn will be “deeper than anticipated,” contracting by 3.0% in 2009. A gradual recovery is projected to begin in the fourth quarter, with 2.5% growth expected for 2010, and 4.7% growth for 2011.

As for inflation, the Bank expects core inflation to fall through 2009, and then return gradually to the 2% target in the third quarter of 2011. Overall inflation is expected to reach a low of -0.8% y/y in the third quarter of this year, and then return to the target, also in the third quarter of 2011.

While the overnight rate is expected to remain at 0.25% for at least one year, the Bank indicated that, conditional on the inflation outlook, it would continue to provide guidance on the duration of its maintaining the lower bound, in each future rate announcement.

WESTERN EUROPE – Andrew Wroblewski, London

EUROZONE – Rising debt and deficits. The average Eurozone government budget deficit rose to 2.5% of GDP in 2008, up from 1.3% in 2007). Partly as a result, the debt ratio rose 1.7 percentage points to a decade-high 70.0%.

ECB – Averse to buying bonds. In a keynote interview, ECB Council member Weber stressed that while he would not rule out anything, he would prefer any non-standard measures the central bank introduces to be directed through the banking system, as this remains the channel through which the Euro-system does most of its financing. Indeed, he suggested that he would regard the purchase of government bonds as being undesirable, not so much because it would cause a potential conflict between fiscal and monetary policy, but because it would suggest that the banking system has failed. Instead he implied that the ECB has to give a clear signal that banks’ financing costs and conditions are going to remain as they are for some time and give

refinancing security for a longer time than is currently the case, stressing that the power of these two measures should not be underestimated as, currently, there is some hesitancy in the banking system, due to banks not entering into longer term refinancing because they expect central banks borrowing costs to come down or borrowing horizons to be prolonged.

NETHERLANDS – Less depressed confidence reading. Consumer confidence increased six points to -28 this month recovering from the five-year low set in March. The recovery (to a four-month high) was concentrated in of the perceived economic climate.

BELGIUM (Tuesday) – Consumer sentiment less gloomy. The Belgian National Bank consumer confidence index increased two points to -22 in April, thereby moving a little further away from the 15-year low of -25 seen December. The breakdown showed that the worries about the current economic situation eased clearly.

OTHER WESTERN EUROPE

UNITED KINGDOM – Downside risks still underscored? The minutes from the April 8-9 BoE MPC meeting showed the committee to have been unanimous in regard to keeping Bank Rate at 0.5%. It was also unanimous about continuing with the program of £ 75 bln worth of asset purchases by the creation of central bank reserves that was started in March and that this would take a further two months to complete. As before, it underlined that the scale and timing of purchases should be reviewed at each MPC meeting and there was seemingly no discussion about possibly having to purchase more paper (ultimately) and/or change the maturities which were being bought.

The minutes acknowledged some brighter signs were emerging in real activity. But they stressed it was too soon to be sure that these improvements would continue, as many of the indicators were both volatile and vulnerable to further shocks. Indeed, with a sharp rise in unemployment occurring, this might prompt further falls in confidence and adjustments to household spending. As a result, the MPC still judged that the risks to the domestic economy remained weighted to the downside (a view that the latest set of more downbeat BoE Agents survey numbers would fully support).

The Committee also discussed the unexpectedly higher CPI inflation figures (for February), reiterating that the resilience in the data was very much due to sterling weakness. However, rather than making any fresh conclusions about the inflation outlook there and then, the MPC decided to leave any reassessment to the May Inflation Report.

Comment: *There may very well have to be a clearer discussion about the inflation outlook at the next meeting, but even if the CPI profile is raised somewhat it is unlikely to alter the BoE’s overall thinking which clearly lies with the downside risks to the economy. However, while playing down the less downbeat signs*

that were evident at the time of the meeting this month, the MPC may be more willing to embrace these signs in May as they seem to be largely continuing, eg the smaller than expected fall in unemployment in the latest set of jobs data as well as the small recovery in world trade data provided by the Dutch Bureau for Economic Policy Analysis (numbers which the MPC have started to focus on).

But clearly, the next MPC meeting will be assessing the asset purchase plan. The fact that government bond yields are now largely higher than before the announcement of the program may make the MPC uneasy. In particular, the BoE may be wary about the manner in which the markets may behave once the £ 75 bln plan has been completed, ie making the BoE ponder whether further purchases should be made. However, the BoE may very well start to believe that it is the economic backdrop (less downbeat activity signs and less risk of genuine deflation) that is pushing up yields, aware too that it will have to wean the gilt market off its asset purchase plan at some time.

Crucially though, the decision about going beyond £ 75 bln or not (NB: the BoE has a remit to purchase up to £ 150 bln) will depend on what is happening to money supply, as this is the main barometer the BoE has stressed for assessing the plan's success. In this regard, the surprise softness in M4 growth in March (ie the first month of the asset purchase plan) is notable, albeit with it unclear how much is due to fluctuations in other financial corporations holding of money rather than the underlying pace. A break-down of the data (due on May 1) may help resolve the issue, but the BoE will surely want more than one month's set of money data before making any fresh judgment.

Labor market unraveling less rapidly? Claimant count unemployment increased sizably again last month but less appreciably than in February when it rose by the fastest pace on record. Indeed, and in contrast to February, joblessness jumped by far less than was generally expected, rising 73 700, after a downwardly revised preceding-month increase of 136 600. This latest jump still caused the unemployment rate on this basis to rise another 0.2 percentage points to 4.5% (the highest since 1998), while the (broader) ILO measure of the unemployment increased similarly, albeit to 6.7%, having been pushed up by a further 177 000 leap in actual joblessness, above previous reports.

Not surprisingly, there were continued signs of a clearly softer labor market dynamics in the details of the figures, including (this time around) a sharp fall in hours worked. Very notably, redundancies rose once again, and to a new high, although the scale of the pick-up was less marked than in the previous month. More fundamentally, employment fell further with the Y/Y rate of change deteriorating to -0.8%. Meanwhile, on a more perturbing note, vacancies tumbled once more, although the unadjusted data gave some better signs. Of some note, activity (participation) rates remained unchanged, thereby retaining the increase seen in previous months.

Earnings growth turns more negative. Average earnings growth fell markedly and (once again) by much than expected, dropping to a record-low of 0.1% Y/Y in the three months to February (from 1.7%) and with the actual single month Y/Y figure for February plunging to -2.1%, also an unprecedented result, largely reflecting a further swing in private (services) sector bonuses. In contrast, ex-bonus earnings figures were down only slightly, inching down to 3.2%, albeit still a 12-year low. Manufacturing unit wage costs, meanwhile, increased further (to 10.0%) in the latest data.

Comment: Yet again, these are troubling labor market numbers, despite the less sizable fall in claimant count joblessness. Indeed, while this development is encouraging (especially the fact that there were more outflows from the claimant count total), the alternative measure of unemployment (from the labor force survey) showed a steeper rise than in previous months. In addition, the clear (albeit bonus induced) weakness in earnings will only accentuate the damage to spending power both from fragile confidence but also from the what is now an employment backdrop that is clearly eroding.

Admittedly, there is some solace in the fact that unemployment is a lagging indicator, but even in that regard the immediate omens are very negative: the latest BoE Agents survey shows an even bleaker labor market profile. Perhaps the main encouragement is that the rise in joblessness is as much a result of people (re)entering the labor market given the rise in participation rates seen of late. The question is what is driving this development, most likely income strains rather than confidence about job prospects.

Record borrowing. Public sector finance data saw yet another worse-than-expected outcome last month, with net borrowing (PSNB) of £ 19.09 bln, the highest ever outcome. As a result, in fiscal year that ended last month, borrowing was a record-high .19% of GDP, despite downward revisions to previous months. This was £ 53.3 bln up on the previous FY and £ 12.4 bln higher than estimated by the Treasury in the December Pre-Budget Report. The data reflected somewhat slower receipt growth (at -3.5%, down even more clearly in Y/Y terms and still far from purely being a reflection of the VAT cut, as both the growth rates in income and corporation tax were negative). There was some slight slowing in spending growth, to 5.3%.

As in previous months, the year-on-year deterioration was broad-based, but still clearest in the current (as opposed to the capital) budget. The data showed that as a percentage of GDP, net government debt was 50.9% (up from 42.9% over the year), albeit with over eight percentage points of this due to financial sector interventions.

Less robust monetary data? The BoE said that March M4 growth was unchanged in M/M terms and down one percentage point (to 17.6%) on a Y/Y basis, albeit down from the February cycle-high. Meanwhile, underlying M4 lending rose by £ 29.4 bln, pushing Y/Y

growth on this basis up by 0.2 percentage point to 15.5%.

These data are clearly providing a misleading picture of underlying monetary trends, with the headline numbers undermined by repo activity but boosted by financial company deposits.

JAPAN – Andrew Wroblewski, London

Exports edge higher. The headline (unadjusted) trade balance deteriorated from ¥ 1096 bln in March 2008 to ¥ 11.0 bln last month, albeit with the outcome actually being a better-than-expected result for the second successive month. Moreover, the data showed a less steep slump in exports, which fell by 45.6% Y/Y in March compared to the record slump of 49.4% seen in February (NB: the slump in imports eased even more clearly to -36.7% Y/Y. Meanwhile, in seasonally adjusted terms, the trade balance deteriorated slightly, staying in deficit, widening to -¥ 97.1 bln last month from a gap of ¥ 71.7 bln in February, albeit with exports showing a modest rise of 2.2%, the first increase since May last year.

ASIA – Samuel Sidenbladh, London

CHINA – Wholesale prices fall. Mirroring the falls seen in consumer and producer price data, wholesale prices fell by 6.6% Y/Y in March, a fourth straight drop and the largest of the four (February -6.0%). On a M/M basis, however, prices were up 0.2%, boosted mainly by crude oil costs.

MALAYSIA – Consumer prices fall. On the back of a larger-than-expected 0.2% M/M drop in the CPI, consumer price inflation fell from 3.7% Y/Y in February to 3.5% last month, an 11-month low. This drop was driven by weaker food price inflation (8.8% Y/Y vs 9.2%), alongside slightly slower utilities and housing price pressures. Transport prices, meanwhile, fell by 2.1% Y/Y for a third straight month.

The further drop in inflation would allow the central bank (BNM) more room to cut interest rates, especially as inflation may dip into negative territory by the end of the current quarter as the base-effects from high oil and commodity prices in 2008 continue to wash out. However, it should be remembered that unlike most of its neighbors, the BNM did not hike rates in response to the pick-up in inflation associated with the surge in commodity prices in early 2008, meaning that there was less need for rate reductions in the first place and that the cumulative 150 bp cut implemented to date will have had a clear impact. Moreover, with rates at historical lows, the BNM may be wary of further large cuts at its next policy meeting on Wednesday 29, arguing that they will have a more limited impact, and instead opt for other measures to complement the Government's fiscal stimulus packages.

PHILIPPINES – Budget balance deteriorates.

According to the Bureau of the Treasury, March saw a budget deficit of 52.6 bln peso. The largest shortfall in over 15 years and 34.0 bln larger than in the same

month of 2008, as revenues fell and expenditures ballooned.

This left the cumulative deficit for the first three months of 2009 at 199.6 bln peso, more than twice the shortfall seen in the first quarter of last year (51.6 bln peso) and roughly 60% of the way towards the Government's 2009 deficit ceiling of 2009.

TAIWAN – Continued labor market deterioration.

The seasonally adjusted unemployment rate rose to 5.7% in March from 5.6% in the preceding month, with last month's reading the highest in over 13 years. The level of unemployment was up by 51.2% Y/Y to 630 000, the largest gain in a little over seven years. Employment, meanwhile, fell by 1.6% Y/Y, a third straight fall and still the largest since November 2001, while the participation rate was virtually unchanged at 57.8%. *The trend in labor market dynamic is clearly downward, further dampening consumer spending.*

OCEANIA – Samuel Sidenbladh, London

AUSTRALIA – Downward surprise to inflation.

Undershooting expectations consumer price inflation fell from 3.7% Y/Y to 2.5% in Q1, a 1½-year low and right in the middle of the central bank's target-range (2-3%). On a Q/Q basis, prices rose by 0.1%, as falling financial services, recreation, transportation (petrol) and clothing costs partially offset rising prices elsewhere (food, housing, health and education in particular).

The Y/Y breakdown, unsurprisingly, showed the main downward pull having come from the transportation component, which fell by 4.6% (-1.2% in Q4 2008) alongside a slump in financial services prices (-1.7% vs +7.0%) and weaker housing price inflation. Most other components, however, saw price pressures picking up.

The clear fall in headline consumer price inflation last quarter was less evident in the two measures of core inflation the RBA follows most closely, with trimmed mean CPI inflation slipping 0.3 percentage point to 3.9% Y/Y, while the weighted median gauge was down a mere 0.1 percentage point to 4.4%. Indeed, the outcomes were well above market expectations and may cause some food for thought at the next RBA Board meeting on May 5. Regardless, the RBA has signaled that it expects another fall in GDP to have occurred in Q1, meaning that domestic demand pressures are likely to ease further, placing even more pressures on (at least) non-tradables consumer price inflation, which at the moment is the main driver of headline CPI inflation. Indeed, in the minutes to the latest (April 7) policy meeting the RBA Board noted that medium-term inflation was likely to face stronger downward pressures than the Bank had previously expected.

Hence, despite the continued resilience in the headline measures, the RBA is probably still pondering some further rate cuts in the next few months, the core-inflation data will ensure that these are fairly modest in size, with another 25 bp rate cut at the next policy

meeting on May 5 looking likely. The new GDP and inflation forecasts, made available to the RBA Board at that meeting (and then published in the quarterly Monetary Policy Statement two days later) will then be highly influential in deciding policy thereafter.

Skilled vacancies fall further. According to the Department of Employment and Workplace Relations,

skilled vacancies fell by 8.9% M/M in trend terms this month, the eighteenth fall in as many months (-10.9% in February), albeit with the pace of decline having slowed in the last three months. In Y/Y terms, however, the pace of decline picked up from -57.8% to 61.0%.