Economics & Markets Research

Emerging Asia Economics Monthly – September 2009

1 September 2009

Global Markets – Asia Team:

EconsAndResearchAsia@anz.com

Paul Gruenwald
Chief Economist, Asia
+65 6216 1814
Paul.Gruenwald@anz.com

Tamara Henderson
Director, FX and Rates Strategy
+65 6216 1845
Tamara.Henderson@anz.com

Yeo Han Sia
Associate Director,
FX and Rates Strategy
+65 6216 1968
HanSia.Yeo@anz.com

Franklin Poon
Economist, North East Asia
+852 3929 5340
Franklin.Poon@anz.com

Chang Wei Liang
Analyst, Economic Research
+65 6216 1918
Weiliang.Chang@anz.com

Research Interns:

Zhou Hao

Raj Gopalakrishnan

Ray Lam

Jaimin Shah

Eesh Mengi

Yansen Poaler

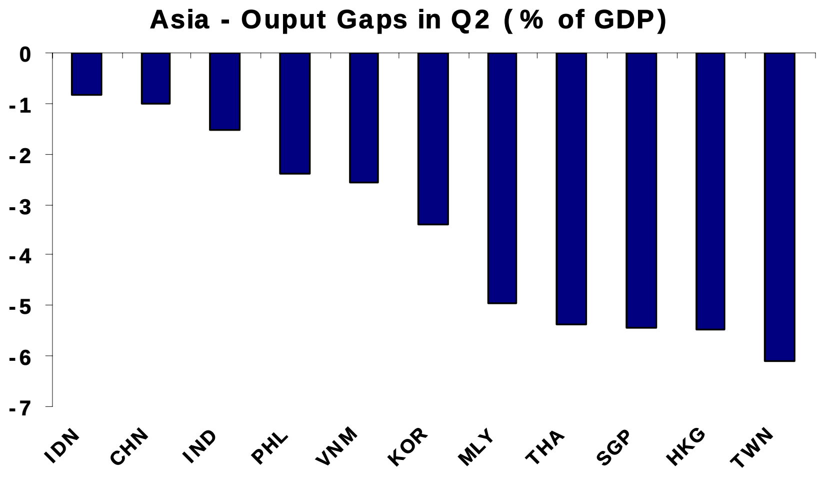
Our Vision:

For Economics & Markets Research to be the most respected, sought-after and commercially valued source of economics and markets research and information on Australia, New Zealand, the Pacific and Asia.

Highlights

- Q2 growth surprised on the upside. For the Newly Industrialised Economies the main drivers were net exports and consumption. The main growth driver for the ASEAN group was investment.
- China's strong momentum has carried into Q3, and the authorities are trying to cool the rate of credit expansion. This is a mid-course adjustment and not a reversal—the stimulus plan will continue.
- We remain wary of labelling the recent rebound a "recovery" given ongoing weak discretionary consumption out of the US and Europe.
- The broad downtrend in USD-AXJ (Asia excluding Japan) is expected to remain intact into 2010, with risk appetite sustained by further progress away from the cyclical low. Near-term, however, portfolio rebalancing may present headwinds for AXJ currencies.
- The bias for rates remains neutral-to-higher. Markets know that it is only a matter of time before central banks initiate the tightening cycle; however, output gaps remain sufficiently wide to dissipate inflationary pressures—allowing central banks to stand pat.

Chart of the Month:



Sources: ANZ Economics, CEIC

Table of Contents

Feature Article: Can Vietnam Replicate China's Recovery? 2
FX and Rates Strategy Overview: Time for Rebalancing........... 5
FX and Policy Rate Forecasts 6
FX Cross Rate Forecasts 7
Long-Term Foreign Currency Government Bond Ratings 8
Sovereign CDS Spreads 8
Country Updates & FX and Rates Strategy.................................. 9

Feature Article: Can Vietnam Replicate China's Recovery?

China's rapid turnaround has been impressive, and reflects in large part the command nature of its economy. In emerging Asia, Vietnam's economic structure most closely resembles that of China, suggesting that Vietnam may rebound similarly. However, while the Vietnamese economy is recovering, we think a repeat of China's experience is unlikely. First and foremost, Vietnam has a weaker balance of payments than China and must rely on foreign financing (FDI and portfolio flows), which have been subdued, to sustain high growth. Additional constraints are the public sector balance sheet and the strength of the policy apparatus. Vietnam will recover and may outperform some of the region, but it will not be able to replicate China's turnaround.

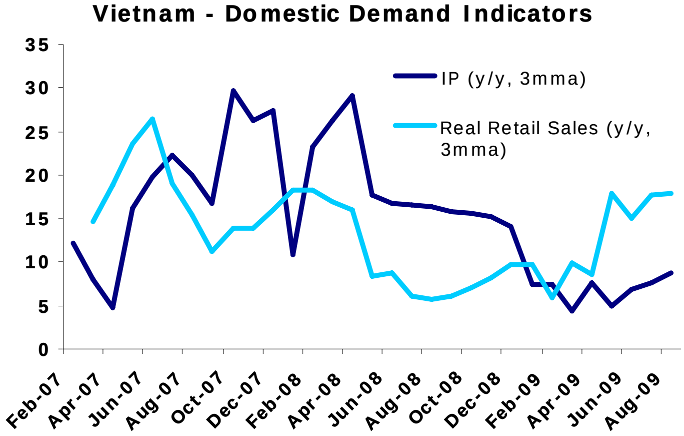
Command-style economies are well suited for implementing effective short-term stimulus plans, as attested by China's recent turnaround. The current global recession reflects a shortfall in aggregate demand as both consumers and firms are unwilling or unable to spend. With a command-style economy, state-controlled banks can essentially be ordered to lend and state-owned enterprises ordered to produce, thus helping to overcome the demand shortfall. Since its stimulus plan was announced in November 2008, China's recovery has surprised most observers as growth rose from about zero (q/q, sa) in Q4 2008 to over 15% in Q2 2009.

Vietnam announced its fiscal stimulus plan in January 2009 (see table). The objective was to revive the economy by promoting consumption and investment, including tax cuts and interest rate assistance for business, infrastructure, housing, schools and hospitals. On the monetary policy side, the plan featured a 4 ppt interest rate subsidy for lending activity in the targeted sectors. The subsidy is to be paid by the State Bank of Vietnam. On the fiscal side, the plan featured a reduction in the corporate income tax as well as temporary VAT refunds and tax deferments. The cost of the stimulus plan this year is estimated at US$6bn (VND100tn), or 6.8% of GDP.

Vietnam – Key Stimulus Measures	
Fiscal Policy	30% corporate income tax payable deduction enacted.
	An extension of 9 months for the submission of 2009 taxes payable.
	A temporary refund of 90% of the value added tax for exported goods in advance of "justifiable payment documents."
Monetary/ Financial Policy	Between Oct 2008 and Jan 2009, the SBV cut its benchmark interest rate six times from 14.00% to 7.00%.
	The reserve requirement was lowered by 1 percentage point for VND and 2 percentage points for foreign currencies.
	The trading band for USD/VND was widened in Nov 2008 from ±2% to ±3%, and again to ±5% in March 2009.
	A 4ppt interest rate subsidy will be paid on loans with a maximum duration of 8 months disbursed from Feb 1, 2009 to Dec 31, 2009.
Social Policy	An unemployment insurance scheme was launched on Jan 1, 2009.
	Interest-free loans were provided to enterprises for paying salaries, social insurance and unemployment subsidies.

Source: Various Vietnamese government agency websites.

Growth in Vietnam has picked up after reaching a decade low in Q1. GDP growth fell to 3.1% (y/y) in Q1 as exports dropped off sharply and the pace of domestic activity, mainly industrial production, slowed markedly. This slowdown reflected both the effects of tightening measures taken in Q3 of 2008 in response to Vietnam's "mini-balance of payments crisis" as well as the deepening of the global financial crisis late in the year. As the stimulus plan took hold, growth rebounded to 4.5% (y/y) in Q2. As in China's national accounts, which are also reported on a production basis, the turnaround was led by the secondary or industrial sector. Moreover, the most recent domestic activity indicators continue to improve. August industrial production growth reached 10.6% (y/y), double the rate of increase earlier in the year. Real retail sales (covering purchases by households and firms) continued to strengthen as well and are now growing at over 20%. As we have seen elsewhere in Asia, the recent pick-up in activity has been domestic-led.



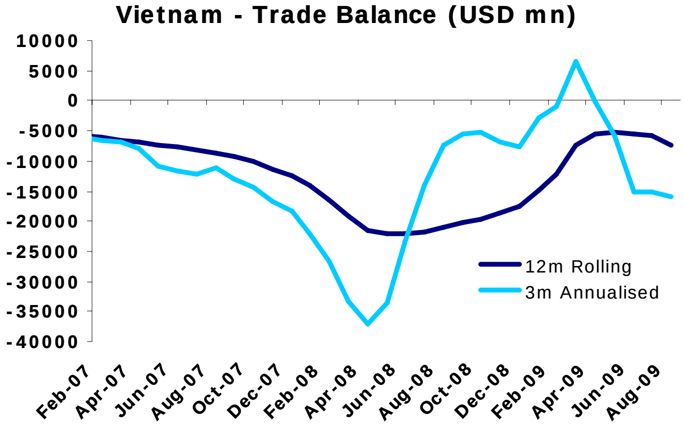
Source: Bloomberg, ANZ Economics.

Inflation has revived owing to base effects and demand pressures. While year-on-year inflation has fallen from a peak of 27.9% in September 2008 to 2.0% in August, price pressures have begun to rise. Indeed, the decline in the year-on-year rate has almost certainly ended since the large monthly spikes in the middle of 2008 have fallen out of the data. On a shorter-term basis consumer prices have been rising at 1¼% to 1½% on a rolling 3-month basis (or 5% to 6% on an annual basis) for the past few months. While we estimate Vietnam still has an output gap of around -2½%, modest price pressures are likely to continue going forward. As inflation rises, real interest rates will fall, adding further stimulus to demand, including imports.

Meanwhile, the external sector remains a drag on growth. Like elsewhere in Asia, exports have declined sharply since late last year. While the worst has past, shipments as of August are falling by 18.9% (y/y). Rice, clothing and electronic components have outperformed. On the other hand import growth turned positive in August for the first time in ten months, rising 5.1% (y/y). Electrical components and medicaments outperformed whilst steel and petroleum imports remained weak.

A sizeable monthly trade deficit has re-emerged. From a surplus in the first quarter of this year, the trade balance has deteriorated sharply as imports have begun to recover while exports have remained weak. August's trade deficit was $1¾bn, the highest since May 2008. Moreover, both our in-house momentum measure as well as the 12-month rolling trade deficit are now deteriorating, although we are still far from the imbalances in the second quarter of 2008.[1] Over the past month, pressures on the currency have re-emerged, with the VND 12M NDF trading at almost 19,500 per USD, some 10% weaker than spot. In contrast, China's trade and current account balances remain in solid surplus, although both have narrowed since the onset of the crisis as exports there remain subdued, and pressure on the currency remains on the strong side.

[1]We would caution against putting too much weight on Vietnam's official trade numbers, which are compiled on a year-to-date basis (as are other economic data). For example, based on this measure the trade deficit through August was widely reported in the press to have fallen by two-thirds relative to last year. Using a year-on-year measure gives the opposite result.



Source: Bloomberg, ANZ Economics.

As the trade balance has deteriorated, external financing has ebbed. This is a worrisome combination. For Vietnam, the main financing items for the current account are FDI and portfolio flows. (The authorities have been sparing in their use of foreign reserves.) Weak economic performance in source markets as well as investors' inability to hedge longer-term VND exposure have led to a decline in FDI *disbursements* by 22.5% through July to $4.6bn; *pledges* of FDI this year to date have fallen by over 80% to $10.1bn. Reflecting heightened global risk aversion, equity flows have also slowed sharply and are running at one-fourth of 2008 levels through end-July (US$114mn net). The combined reduction of these two potentially large inflows implies that Vietnam's ability to run a trade deficit is limited. This, in turn, is likely to constrain the growth rate of the economy.

Vietnam - Summary Balance of Payments
(as a % of GDP)

	2005	2006	2007	2008
Current Account	-1.1	-0.3	-9.8	-10.3
Trade Balance	-4.6	-4.6	-14.6	-13.7
Other	3.5	4.3	4.8	3.4
Financial Account	5.9	5.1	24.6	10.2
Net FDI	3.6	3.8	9.3	8.7
Net Loans	1.7	1.6	2.8	1.0
Net Portfolio/ST capital	0.6	-0.5	12.5	0.6

Sources: IMF, ANZ Economics.

Additional constraints to a stimulus-led recovery are the public sector balance sheet and the policy apparatus. Vietnam's public debt to GDP ratio at end-2008 was 38% of GDP (China's was 17% of GDP). Although this level is moderate for an emerging market economy, there is a risk that this year's deficit could surprise on the upside.[2] Moreover, if the global downturn persists, more stimulus spending may be required and the public debt to GDP could conceivably rise above 50% of GDP, a level at which sustainability concerns might begin to be raised. We would also note that the policy apparatus in Vietnam is less developed and predictable than in China, which has potential effects on investor confidence as well as the efficiency of the stimulus plan.

All told, Vietnam should be able to outperform some of emerging Asia given its command structure, but not recover at the pace we have seen in China. The main constraint is external, and with balance of payments financing likely to be less forthcoming than in recent years, imports and growth will necessarily be constrained. The fiscal situation and the policy apparatus may constrain growth as well. As in China, the downside risk for Vietnam is efficiency. Since resource allocation will likely not be fully market based, a rise in both non-performing loans and unproductive capacity are medium-term concerns.

Paul Gruenwald and Raj Gopalakrishnan

[2] For example, the World Bank projects a fiscal deficit this year for Vietnam at 12% of GDP.

FX and Rates Strategy Overview:
Time for Rebalancing

Market Outlook

A 22% slide in Chinese equities in August has trimmed the Shanghai composite index's gains to "only" 47% year-to-date (ytd). The trigger was further steps taken by Chinese authorities to discourage the build-up of asset bubbles. The measures—including the curbing of investment in sectors facing overcapacity and closer scrutiny of bank lending—are a long-term positive for Chinese economic growth prospects, but markets have used the initiatives as an excuse to book a nice run of profits.

Profit-taking in other parts of AXJ (Asia excluding Japan) is likely as the recent realignment in the Shanghai composite makes the 73% ytd gains on the Jakarta composite index and on the Ho Chi Minh index appear out of sync. Meanwhile, in anticipation of a US growth spurt, portfolio tilts toward US equities are increasingly likely. The ytd gain in US equities has been much more benign and P/E ratios tend to be lower. As many real money accounts conduct quarterly rebalancing exercises, a slight upward bias in USD-AXJ is expected to persist during the month of September. A pullback in risk appetite would also be supportive of this tactical long USD-AXJ view.

More broadly, however, we maintain our outlook for the downtrend in USD-AXJ to remain intact into 2010. Risk appetite should remain sustained as the global economy makes further progress away from the cyclical low, and once global demand starts to recover in a meaningful way, AXJ's larger exposure to trade shocks suggests that AXJ currencies stand to benefit the most within emerging markets.

FX Strategy

The Indonesian rupiah (IDR) has out-performed within AXJ this year, gaining roughly 9% against the USD thus far. IDR out-performance has had three components: 1/ a correction from unfair punishment last year (when Indonesia's relatively strong fundamentals were ignored), 2/ the removal of political uncertainty with the re-election in July of a market-friendly incumbent President Yudhoyono, and 3/ attractive yields.

Going forward, however, the IDR faces headwinds: more near-term from an over-extended stock market, and further down the road from building inflation momentum. As such, we continue to favour the Korean won (KRW) into 2010, expecting the KRW to be a primary beneficiary as global demand improves. The Korean economy is more sensitive to foreign demand conditions and Korean exports are much more competitive owing to the collapse of the KRW during the meltdown in global financial markets last year. On a strategic basis we suggest:

- ***AXJ corporates* with USD payables**: Increase IDR hedge ratios and reduce KRW hedge ratios.
- ***Real money funds with dedicated AXJ allocations:*** Under-weight IDR and over-weight KRW.
- ***Leveraged funds:*** Sell USD-KRW and buy USD-IDR forward outright.

Rates Strategy

The bias for rates remains neutral-to-higher. AXJ central banks have all concluded their easing cycles, now all in "wait-and-see" mode for a clear signal to reign in ultra-loose monetary conditions. However, clarity is not expected anytime soon as the prerequisite normalisation in global demand conditions and closing of output gaps remains some way off. Still, markets know that it is only a matter of time before central banks raise policy rates.

We favour curve flatteners as a means of waiting out the official turn in the interest rate cycle. Flatteners reduce interest rate risk via the shortening of duration and have the added benefit of positive carry. AXJ yields likely to face greater upward pressure more quickly are those in the countries with the stronger growth momentum and weaker inflation fighting records (i.e. India, Indonesia and Vietnam).

- ***Real money funds with dedicated AXJ allocations:*** Underweight INR and VND government bonds. Cut overweight IDR bond allocations to neutral.

- ***Leveraged funds:*** Opt for payers on the INR, IDR and VND interest rate swap curves.

Tamara Henderson

Foreign Exchange and Policy Rate Forecasts

		Current	Sep 09	Dec 09	Mar 10	Jun 10	Sep 10	Dec 10
China	USD/CNY, eop	6.832	6.83	6.83	6.83	6.83	6.82	6.80
	AUD/CNY, eop	5.701	5.20	5.00	5.10	5.20	5.30	5.40
	PBoC base lending rate	5.31	5.31	5.31	5.31	5.31	5.58	5.85
Hong Kong	USD/HKD, eop	7.750	7.750	7.750	7.750	7.760	7.770	7.800
	AUD/HKD, eop	6.475	6.4	6.2	6.2	6.4	6.5	6.7
	HKMA discount rate	0.50	0.50	0.50	0.50	0.50	0.75	1.00
India	USD/INR, eop	48.73	48.5	48.0	47.0	47.5	47.0	47.0
	AUD/INR, eop	41.08	39.8	38.4	37.6	39.4	39.5	40.4
	RBI repo rate	4.75	4.75	4.75	4.75	5.00	5.25	5.50
Indonesia	USD/IDR, eop	10,060	10,250	9,750	9,500	9,625	9,250	9,000
	AUD/IDR, eop	8,399	8,400	7,800	7,600	8,000	7,800	7,700
	BI rate	6.50	6.50	6.50	6.50	6.75	7.00	7.00
Malaysia	USD/MYR, eop	3.52	3.55	3.50	3.48	3.45	3.40	3.40
	AUD/MYR, eop	2.97	2.91	2.80	2.78	2.86	2.86	2.92
	BNM overnight rate	2.00	2.00	2.00	2.00	2.00	2.25	2.25
Philippines	USD/PHP, eop	48.80	49.0	48.0	48.0	47.0	47.0	46.0
	AUD/PHP, eop	41.12	40.2	38.4	38.4	39.0	39.5	39.6
	BSP reverse repo rate	4.00	4.00	4.00	4.00	4.00	4.25	4.25
Singapore	USD/SGD, eop	1.439	1.47	1.46	1.45	1.44	1.44	1.43
	AUD/SGD, eop	1.213	1.21	1.17	1.16	1.20	1.21	1.23
	3M SGD SIBOR	0.68	0.69	0.69	0.85	1.00	1.30	1.50
S Korea	USD/KRW, eop	1248	1260	1125	1175	1150	1100	1050
	AUD/KRW, eop	1044	1030	900	940	950	920	900
	BoK overnight call rate	2.00	2.00	2.00	2.00	2.00	2.25	2.50
Taiwan	USD/TWD, eop	32.92	33.1	32.5	32.0	31.5	31.0	30.3
	AUD/TWD, eop	27.55	27.1	26.0	25.6	26.1	26.0	26.1
	CBC discount rate	1.25	1.25	1.25	1.25	1.25	1.50	1.75
Thailand	USD/THB, eop	34.01	34.0	34.0	34.0	34.0	33.5	33.5
	AUD/THB, eop	28.67	27.9	27.2	27.2	28.2	28.1	28.8
	BoT repo rate	1.25	1.25	1.25	1.25	1.25	1.50	1.50
Vietnam	USD/VND, eop	17,820	17,800	18,500	18,500	18,500	18,500	19,300
	AUD/VND, eop	14,913	14,600	14,800	14,800	15,400	15,500	16,600
	SBV base lending rate	7.00	7.00	7.00	7.00	7.00	7.50	8.00

Foreign Exchange Cross-Rate Forecasts

	Current Spot	ANZ Forecast					Implied Spot from 12M Fwd or NDF	Implied 12M % Change	
		Sep-09	Dec-09	Mar-10	Jun-10	Sep-10		ANZ	Forwards
CNY-HKD	1.13	1.13	1.13	1.13	1.14	1.14	1.14	1%	0%
CNY-INR	7.13	7.10	7.03	6.88	6.95	6.90	7.14	-3%	0%
CNY-IDR	1,470	1,500	1,430	1,390	1,410	1,360	1,470	-7%	0%
CNY-MYR	0.515	0.520	0.512	0.510	0.505	0.499	0.513	-3%	-1%
CNY-PHP	7.14	7.17	7.03	7.03	6.88	6.90	7.12	-3%	0%
CNY-SGD	0.211	0.215	0.214	0.212	0.211	0.211	0.211	0%	0%
CNY-KRW	183	184	165	172	168	161	182	-12%	0%
CNY-TWD	4.82	4.85	4.76	4.69	4.61	4.55	4.79	-6%	0%
CNY-THB	4.98	4.98	4.98	4.98	4.98	4.92	4.97	-1%	0%
HKD-INR	6.29	6.26	6.19	6.06	6.12	6.05	6.28	-4%	0%
HKD-IDR	1,300	1,320	1,260	1,230	1,240	1,190	1,300	-8%	0%
HKD-MYR	0.454	0.458	0.452	0.449	0.445	0.438	0.451	-4%	-1%
HKD-PHP	6.30	6.32	6.19	6.19	6.06	6.05	6.26	-4%	-1%
HKD-SGD	0.186	0.190	0.188	0.187	0.186	0.185	0.186	0%	0%
HKD-KRW	161	163	145	152	148	142	160	-12%	0%
HKD-TWD	4.25	4.27	4.19	4.13	4.06	3.99	4.22	-6%	-1%
HKD-THB	4.39	4.39	4.39	4.39	4.38	4.31	4.37	-2%	0%
INR-IDR	206	211	203	202	203	197	207	-5%	0%
INR-MYR	0.072	0.073	0.073	0.074	0.073	0.072	0.072	0%	-1%
INR-PHP	1.00	1.01	1.00	1.02	0.99	1.00	1.00	0%	0%
INR-SGD	0.030	0.030	0.030	0.031	0.030	0.031	0.030	4%	0%
INR-KRW	25.6	26.0	23.4	25.0	24.2	23.4	25.6	-9%	0%
INR-TWD	0.676	0.682	0.677	0.681	0.663	0.660	0.672	-2%	-1%
INR-THB	0.698	0.701	0.708	0.723	0.716	0.713	0.696	2%	0%
IDR-MYR	0.00035	0.00035	0.00036	0.00037	0.00036	0.00037	0.00035	5%	-1%
IDR-PHP	0.00485	0.00478	0.00492	0.00505	0.00488	0.00508	0.00483	5%	-1%
IDR-SGD	0.00014	0.00014	0.00015	0.00015	0.00015	0.00016	0.00014	9%	0%
IDR-KRW	0.124	0.123	0.115	0.124	0.119	0.119	0.124	-4%	0%
IDR-TWD	0.00327	0.00323	0.00333	0.00337	0.00327	0.00335	0.00325	2%	-1%
IDR-THB	0.00338	0.00332	0.00349	0.00358	0.00353	0.00362	0.00337	7%	0%
MYR-PHP	13.9	13.8	13.7	13.8	13.6	13.8	13.9	0%	0%
MYR-SGD	0.409	0.414	0.417	0.417	0.417	0.424	0.412	4%	1%
MYR-KRW	355	355	321	338	333	324	356	-9%	0%
MYR-TWD	9.35	9.32	9.29	9.20	9.13	9.12	9.35	-2%	0%
MYR-THB	9.66	9.58	9.71	9.77	9.86	9.85	9.69	2%	0%
PHP-SGD	0.029	0.030	0.030	0.030	0.031	0.031	0.030	4%	1%
PHP-KRW	25.6	25.7	23.4	24.5	24.5	23.4	25.6	-9%	0%
PHP-TWD	0.675	0.676	0.677	0.667	0.670	0.660	0.674	-2%	0%
PHP-THB	0.697	0.694	0.708	0.708	0.723	0.713	0.698	2%	0%
SGD-KRW	868	857	771	810	799	764	864	-12%	0%
SGD-TWD	22.9	22.5	22.3	22.1	21.9	21.5	22.7	-6%	-1%
SGD-THB	23.6	23.1	23.3	23.4	23.6	23.3	23.5	-2%	0%
KRW-TWD	0.026	0.026	0.029	0.027	0.027	0.028	0.026	7%	0%
KRW-THB	0.027	0.027	0.030	0.029	0.030	0.030	0.027	12%	0%
TWD-THB	1.03	1.03	1.05	1.06	1.08	1.08	1.04	5%	0%

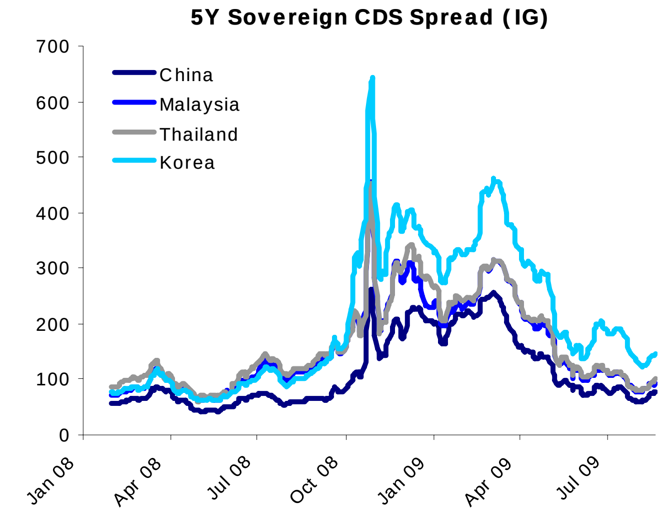
Long-Term Foreign Currency Government Bond Ratings

	Moody's	S&P	Fitch
Investment Grade			
China	A1	A+	A+
Hong Kong	Aa2	AA+	AA
India	Baa2	BBB-	BBB-
Korea	A2	A	A+
Malaysia	A3	A-	A-
Singapore	Aaa	AAA	AAA
Taiwan	Aa3	AA-	A+
Thailand	Baa1	BBB+	BBB
Sub-Investment Grade			
Cambodia	B1	B+	NR
Indonesia	Ba3	BB-	BB
Philippines	Ba3	BB-	BB
Vietnam	Ba3	BB	BB-

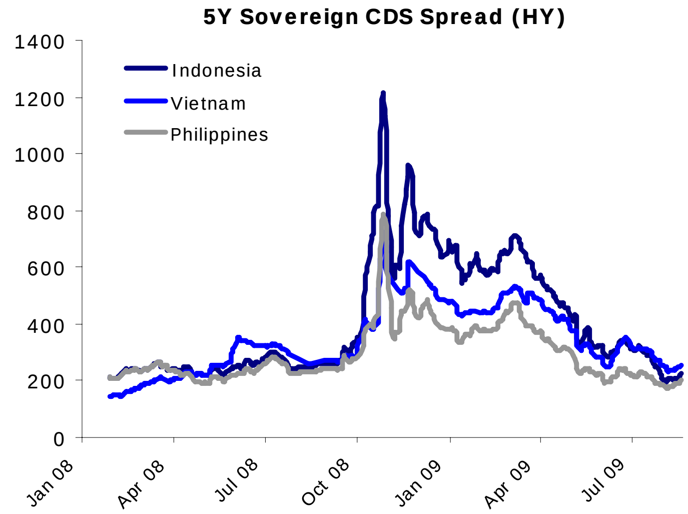
** denotes an upgrade; # denotes a downgrade over previous month*

Source: Bloomberg

Sovereign CDS Spreads

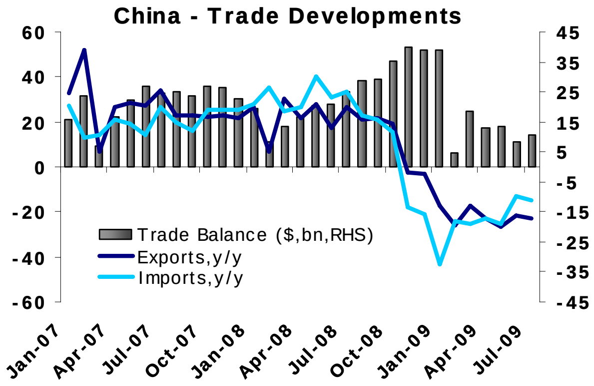


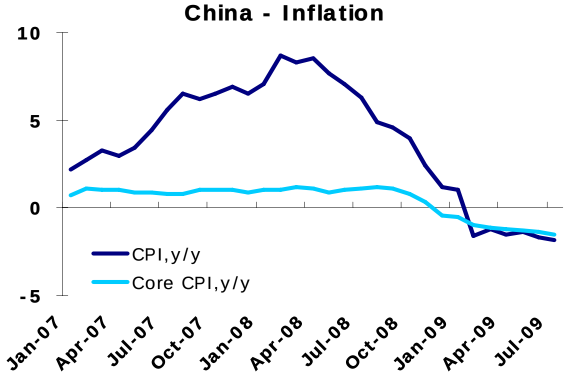
Source: Bloomberg

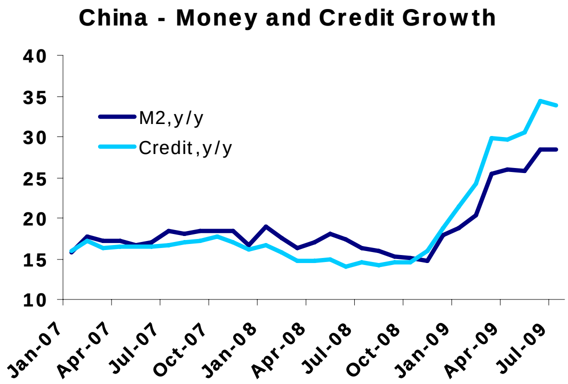


Source: Bloomberg

Country Update: China







The pace of domestic activity remains robust. However, trade remains weak although momentum appears to have improved. We expect the authorities to continue to implement their stimulus plan albeit with some mid-course adjustments. We see no major policy changes in the near term.

- Retail sales rose 15.2% (y/y) in Jul, slightly better than the 15.0% growth in Jun. Sales in wholesale and retail, hotel and catering, and other industries increased by 15.2%, 16.8% and 2.6%, respectively. Industrial production continued its uptrend, gaining 10.8% in Jul compared with a 10.7% rise in Jun.
- Exports fell by 23.0% (y/y) in Jul, worse than the 21.4% fall in Jun, although shipments rose 10.4% (m/m). Imports also declined faster despite the stimulus plan, falling 14.9% (y/y) in Jul as against -13.2% in Jun. However, imports in Jul increased 8.7% (m/m). Part of the drop in imports is due to lower prices for commodities. The trade surplus rose to $10.6bn in Jul from $8.3bn in Jun.
- The CPI declined for the sixth month in a row in Jul, falling 1.8% (y/y) after a 1.7% drop in Jun. That said, inflation momentum seems to have turned positive. The Producer Price Index was down by 8.2% (y/y) in Jul as against a 7.8% dip in Jun.
- New Yuan-denominated loans slowed sharply to CNY356bn in Jul, the smallest increase in nine months; Jun's pace was CNY1530bn. The central bank said it would use market tools to check lending growth during the second half of 2009 to reduce the risk of asset bubbles. Total new loans for Jan-Jul stood at CNY7.7tn, far exceeding the initial CNY5.0tn target for all of 2009.
- China's official PMI was 53.3 in Jul, up fractionally from Jun, marking the fifth consecutive reading above 50, indicating an expansion. CLSA's PMI rose to a one-year high of 52.8 in Jul from 51.8 in Jun, the fourth consecutive month above 50. The output growth and new orders components were at 14-month highs.
- We project growth of 8.1% in 2009 with some upside risk as the stimulus plan runs ahead of schedule. On policy, we expect the authorities to continue the accommodative overall policy stance, adopting mid-course adjustments—not drastic changes—as required.

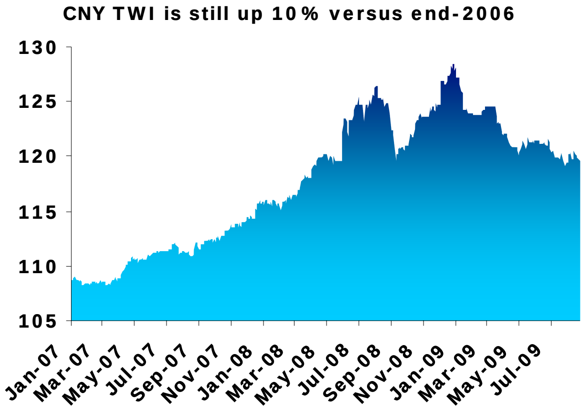
Paul Gruenwald

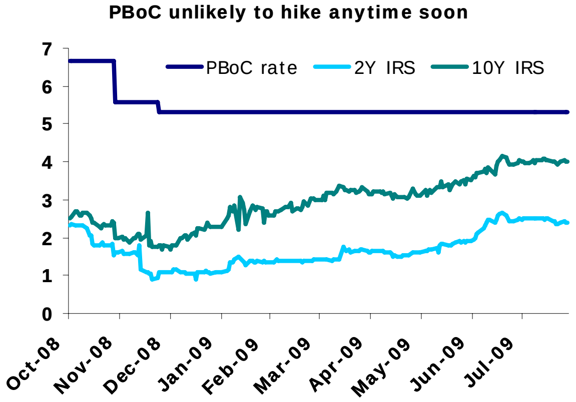
Economic Data – China

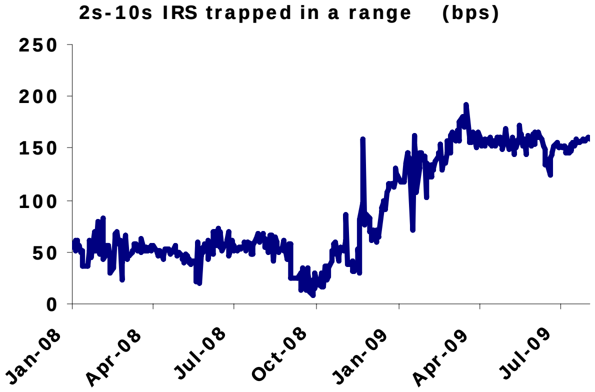
Monthly data	**Dec-08**	**Jan-09**	**Feb-09**	**Mar-09**	**Apr-09**	**May-09**	**Jun-09**	**Jul-09**
Industrial Production, % y/y	5.7	0.0	N/A	8.3	7.3	8.9	10.7	10.8
Retail Sales, % y/y	19.0	18.5	11.6	14.7	14.8	15.2	15.0	15.2
Consumer Price Index, % y/y	1.2	1.0	-1.6	-1.2	-1.5	-1.4	-1.7	-1.8
Exports, % y/y	-2.8	-17.5	-25.7	-17.1	-22.6	-26.3	-21.4	-22.9
Imports, % y/y	-21.3	-43.1	-23.8	-24.9	-22.8	-24.8	-13.0	-14.9
Trade Balance, US$ bn	39.0	39.1	4.8	18.6	13.1	13.4	8.3	10.6
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Real GDP, % y/y	13.0	12.0	10.6	10.1	9.0	6.8	6.1	7.9
-Primary Sector ytd	4.3	3.7	2.8	3.5	4.5	5.5	3.5	3.8
-Secondary sector ytd	14.8	14.7	11.5	11.3	10.6	9.3	5.3	6.6
-Tertiary sector ytd	14.0	13.8	10.9	10.7	10.5	9.5	7.4	8.3
Nominal GDP, RMB tn	17.4	25.7	6.3	13.5	20.8	30.1	6.6	14.0
Foreign Exchange Reserves, US$ bn	1,433.6	1,528.2	1,682.2	1,808.8	1,905.6	1,946.0	1,953.7	2,131.6
Current Account, US$ bn (semi-annual)	N/A	371.8	N/A	191.7	N/A	426.1	N/A	130.0
Capital Account, US$ bn (semi-annual)	N/A	3.1	N/A	1.7	N/A	3.1	N/A	1.3

Sources: CEIC

China: FX and Rates Strategy







The authorities are expected to keep USD-CNY stable well into 2010, awaiting the return of discretionary demand in the US and Europe. Meanwhile, recent steps by the PBOC to reign in liquidity are seen more as a means of supporting growth (by averting an asset bubble) than as a sign of imminent rate hikes.

FX

USD-CNY remains rock steady and is expected to remain so well into 2010, in line with our outlook for a protracted period of sub-par growth in the developed economies. Economic growth has clearly bottomed in China, but exports have yet to show any sign of a recovery, still down 23% (y/y) in Jul. Meanwhile, on a trade-weighted basis the sharp appreciation experienced during the meltdown in global financial markets at the end of last year has now unwound, such that Chinese exporters are no longer at a significant disadvantage.

In the offshore market, the discount in USD-CNY NDFs has narrowed in tandem with the sharp 22% slide in Chinese equities in Aug. The trigger for the sell-off was further measures taken by Chinese authorities to discourage the build-up of asset bubbles. Such measures are actually a positive for China's long-term growth prospects, so the USD-CNY NDF discount is expected to revert wider once real money accounts complete their rebalancing exercises at the end of this quarter.

Rates

Local rates have failed to reap much benefit from the sharp sell-off in Chinese equities during Aug, as the market remains concerned that recent "fine-tuning" actions by the authorities to avert an asset bubble will translate into outright rate hikes, sooner rather than later.

Although we expect market rates to maintain an upward bias into 2010 in anticipation of the turn in the official interest rate cycle, no PBOC rate hikes are expected until the second half of next year. Comments by the authorities continue to suggest that there is no intention of reigning in accommodative fiscal and monetary policies anytime soon. Indeed, clarity about the timing and scope of recovery in discretionary demand in the US and Europe is still some way off.

Tamara Henderson

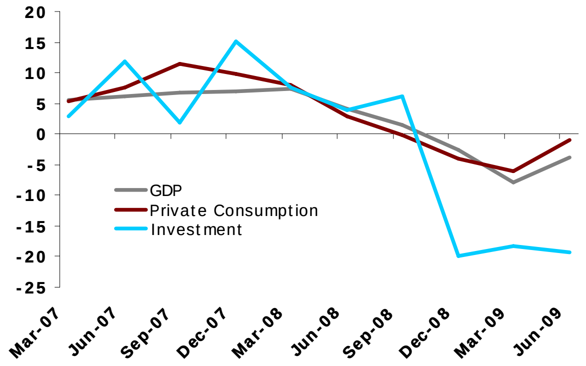
Market Forecasts – China (eop)

FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-CNY	6.832	0.1%	6.83	6.83	6.83	6.83	6.82	6.80
AUD-CNY	5.701	18.9%	5.20	5.00	5.10	5.20	5.30	5.40
NZD-CNY	4.680	18.5%	4.00	3.80	3.70	3.70	3.70	3.80
JPY-CNY	0.073	-3.4%	0.070	0.068	0.065	0.063	0.062	0.061
EUR-CNY	9.763	2.4%	9.22	8.88	8.88	8.95	9.00	8.98
Rates	**Current**	**Ytd**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
PBOC's 1-year base lending rate	5.31	0	5.31	5.31	5.31	5.31	5.58	5.85
3-month SHIBOR	1.73	-5	1.8	2.1	2.3	2.5	3.0	3.5
2-year IRS (onshore vs 7-day repo fix)	2.40	133	2.6	2.9	3.1	3.3	3.8	4.3
10-year IRS	3.99	220	4.1	4.2	4.3	4.4	4.7	4.9

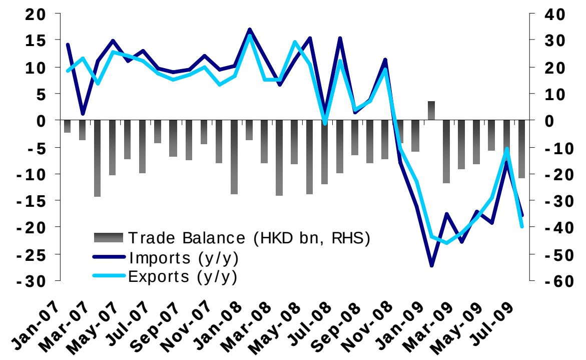
Sources: Bloomberg, ANZ

Country Update: Hong Kong

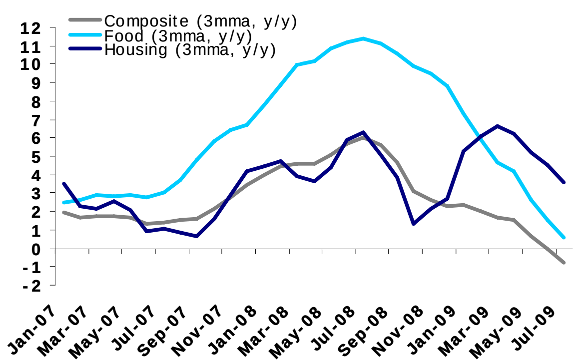
Hong Kong - GDP composition (y/y)



Hong Kong - External Trade



Hong Kong - CPI



The economic contraction ended in Q2, with growth supported by improved consumer sentiment and increased government spending. However, we remain wary about the outlook, as external demand is forecast to remain fragile. Our 2010 growth forecast remains unchanged at 3.3%.

- GDP fell by 3.8% (y/y) in Q2. On a q/q (sa) basis, however, GDP grew by 3.3%, reversing the contraction in the preceding four quarters. Growth was supported by private consumption and government spending, while the external sector stabilised. Companies remained cautious with their investment plans in Q2.
- Growth in retail sales improved to -4.8% (y/y) in Jun from May's -6.2%. Volume growth also rose to -4.2% from -6.4% as sentiment improved somewhat.
- Exports declined by 19.9% (y/y) in Jul, compared with Jun's -5.4%, ending four months of narrowing contraction. Jul's export weakness was partly due to a high base, but it also suggested an uneven export recovery path ahead. Imports dropped by 17.8% (y/y), from Jun's -7.9%. A trade deficit of HK$21.7bn was recorded, compared with Jun's HK$16.5bn.
- The composite CPI dropped by 1.5% (y/y) in Jul, the second consecutive decline. Netting out the effects of the government's one-off measures, consumer prices declined by 0.3% in Jul, from Jun's 0.4% increase, mainly due to the larger decrease in food prices and the smaller increase in private housing rentals.
- Property prices continued to rise in Aug. Mortgage rates remain lower than rental yields, and capital inflows have remained strong. The jobless rate stayed unchanged at 5.4% in Jul.
- The PMI increased for the eighth straight month to reach 49.9 in Jul, from 47.1 in Jun, close to the neutral level of 50, consistent with the end of the economic contraction.
- Hong Kong and Guangdong signed eight cooperation agreements to promote economic development. The pacts cover various aspects, including Hong Kong-Shenzhen services and financial sector cooperation.
- On the back of the stronger than expected Q2 GDP data, we have revised upward our 2009 forecast to -3.5% from -3.9%. At the same time, our 2010 forecast remains unchanged at 3.3%, highlighting downside risks from the external sector.

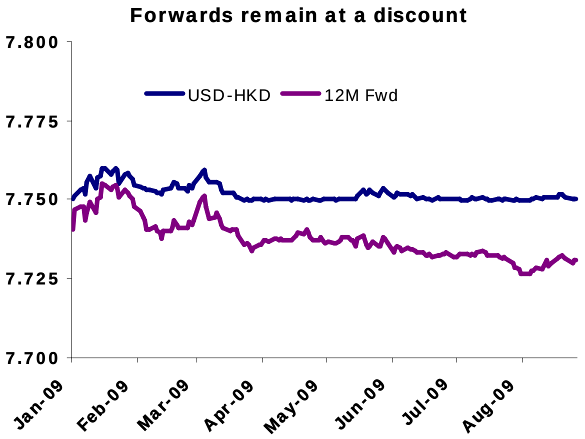
Franklin Poon

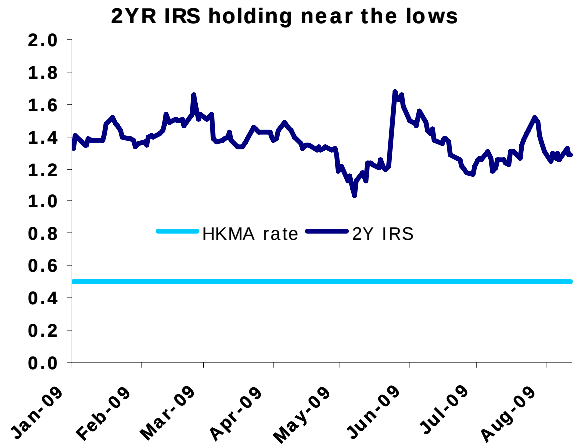
Economic Data – Hong Kong

Monthly data	Dec-08	Jan-09	Feb-09	Mar-09	Apr-09	May-	Jun-09	Jul-09
Retail Sales, % y/y	1.1	7.3	-12.7	-7.8	-4.3	-6.2	-4.8	N/A
Composite Consumer Price Index sa, % y/y	2.1	2.7	1.1	1.2	0.6	0.1	-0.8	-1.4
Exports, % y/y	-11.4	-21.8	-23.0	-21.1	-18.2	-14.5	-5.4	-19.9
Imports, % y/y	-16.2	-27.1	-17.5	-22.7	-17.0	-19.2	-7.9	-17.8
Trade Balance, US$ bn	-1.5	0.9	-3.0	-2.3	-2.1	-1.4	-2.1	-2.8
Foreign Exchange Reserves, US$ bn	178.1	174.4	171.7	181.7	185.9	196.2	205.7	N/A
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Industrial Production, % y/y	-2.1	-0.3	-4.5	-4.2	-7.0	-10.6	-10.1	N/A
Real GDP, % y/y	6.8	6.9	7.3	4.1	1.5	-2.6	-7.8	-3.8
-Private consumption	11.4	9.7	8.0	3.0	-0.2	-4.1	-6.0	-1.0
-Government consumption	2.4	3.3	0.6	3.1	1.6	1.8	1.4	1.6
-Gross fixed capital formation	-1.1	8.0	9.9	5.1	2.9	-17.8	-13.7	-14.0
Nominal GDP, HKD bn	415.5	448.0	410.0	401.4	430.2	435.3	379.6	392.7
Current Account, US$ bn	7.8	6.1	6.5	4.1	9.6	10.4	5.5	N/A
Capital & Financial Account, US$ bn	-9.6	-8.3	-4.3	-2.6	-11.9	-8.9	-3.9	N/A

Sources: CEIC

Hong Kong: FX and Rates Strategy





Amid an upcoming change in leadership at the HKMA, market participants continue to speculate about an adjustment in the currency regime. In our view, no adjustment in the HKD peg is likely in the foreseeable future. USD-HKD should remain on the strong side of the convertibility zone until the US signals an end to its policy of quantitative easing—more likely in 2010 than 2009.

FX

USD-HKD continues to trade on the strong side of the convertibility zone, supported by fund inflows. The upcoming change in leadership at the helm of the HKMA (effective 1 October) continues to fuel speculation of an adjustment in Hong Kong's currency regime—despite clear indications by the authorities supporting the status quo. Chief Executive Joseph Yam's successor, Norman Chan, has said that the HKD-USD peg will be maintained, while the use of the renminbi would be expanded.

We believe that an adjustment in the currency peg is highly unlikely as long as: 1/ global financial markets remain fragile and global growth remains sub-par, and 2/ Hong Kong's trade and financial links remain dominated by the West. As such, no adjustment in the USD-HKD peg is expected in the foreseeable future, and USD-HKD should remain on the strong-side of the convertibility zone into next year.

Rates

HKD rates remain range-bound as the latest FOMC statement on 12 Aug supported the status quo of an exceptionally low federal funds rate for an extended period. Meanwhile, US economic data have continued to exceed market expectations, even suggesting a possible turn in the housing market. Favourable base effects on headline inflation rates will soon start to unwind and the impact of government stimulus measures should be working more fully through the economy. All in all, this suggests a pickup in volatility in US and HK rates as markets attempt to time the withdrawal of ultra-loose monetary policy. We favour HKD flatteners during the waiting period as this is a means of hedging interest rate risk while earning positive carry.

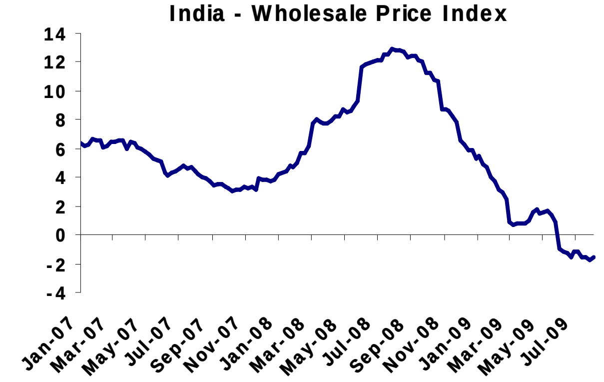
Tamara Henderson

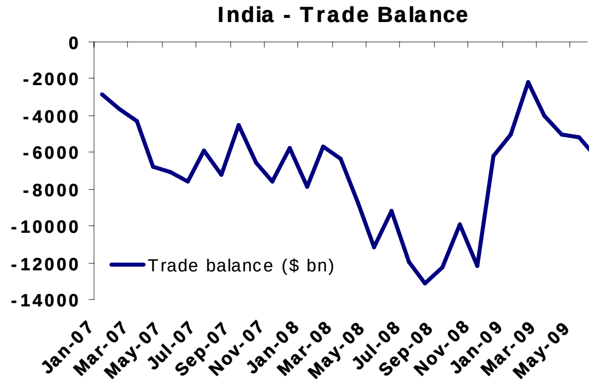
Market Forecasts – Hong Kong (eop)

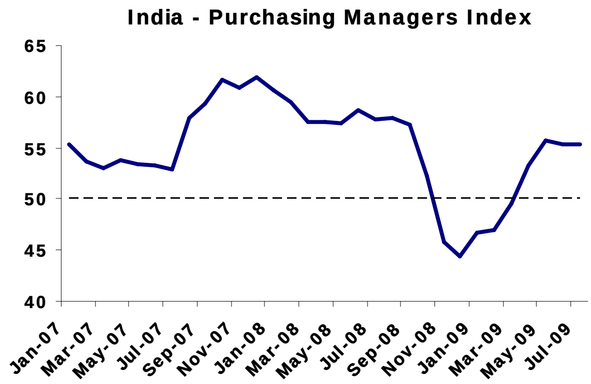
FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-HKD	7.750	0.0%	7.750	7.750	7.750	7.760	7.770	7.800
AUD-HKD	6.475	18.9%	6.4	6.2	6.2	6.4	6.5	6.7
NZD-HKD	5.313	18.3%	5.1	5.0	4.6	4.6	4.7	4.8
JPY-HKD	0.082	-3.5%	0.079	0.078	0.074	0.072	0.071	0.070
EUR-HKD	11.083	2.3%	11.0	10.7	10.7	10.9	10.9	11.1
Rates	**Current**	**Ytd (bps)**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
HKMA's discount rate	0.50	0	0.50	0.50	0.50	0.50	0.75	1.00
3-month HIBOR	0.21	-74	0.4	0.6	0.7	0.8	1.3	2.1
2-year IRS (onshore versus 3M)	1.29	-21	1.4	1.6	1.7	2.0	2.5	3.2
10-year IRS	3.27	134	3.5	3.7	4.0	4.2	4.4	4.7

Sources: ANZ, Bloomberg

Country Update: India







The pace of recovery surprised on the upside in Q2 on a strong turnaround in domestic demand, but a rainfall deficit could weigh on growth in H2. Inflation readings look set to rise in the coming months on higher farm prices and fading base effects.

- GDP expanded by 6.1% (y/y) in Q2, accelerating for the first time since 2007. In seasonally adjusted q/q terms, output rose by 1.8%, the fastest pace in 3 quarters. The growth contribution was broadly stable across sectors, with higher manufacturing growth offsetting a slowdown in social and community services.
- Passenger vehicle sales jumped 29.2% (y/y) in Jul after an 8.3% rise in Jun, supported by the launch of new models and easier retail financing conditions. Commercial vehicle sales ended their 11-month contraction to rise 9.5%.
- Exports showed few signs of a turnaround, declining for the ninth consecutive month at -27.7% (y/y) in Jun. Imports rose from the record low of -39.2% in May to -29.3%. The improvement was partly due to higher oil prices. The monthly trade deficit widened to $6.2bn from $5.2bn in May.
- The WPI continued to post declines into Aug, but the food articles index climbed 10.5% (y/y) in the week ending 8 Aug as weak monsoons hampered farm output. Fading base effects could accentuate the rise in headline WPI in Q4. Meanwhile, other measures of consumer prices rose further. CPI for industrial workers rose to 9.3% in Jun from 8.6% in May; rural workers experienced price increases of 12.7% in Jul, the highest in a decade.
- Industrial production surprised at 7.8% (y/y) in Jun, well above market expectations of 3.8%. The manufacturing PMI also indicated sustained output expansion with a reading of 55.3 in Jul, unchanged from Jun. The new orders index rose to a nine-month high of 59.8.
- While the pace of recovery in Q2 was faster than expected, the weak monsoon rainfall could worsen the fiscal deficit and slow growth momentum in H2. More than a quarter of India's 604 districts could experience a drought and the sowing of crops is down 20% (y/y). However, we believe the economy should outperform RBI's forecast of "6% with upward bias" in FY09/10, notwithstanding the growing downside risks to agriculture output.

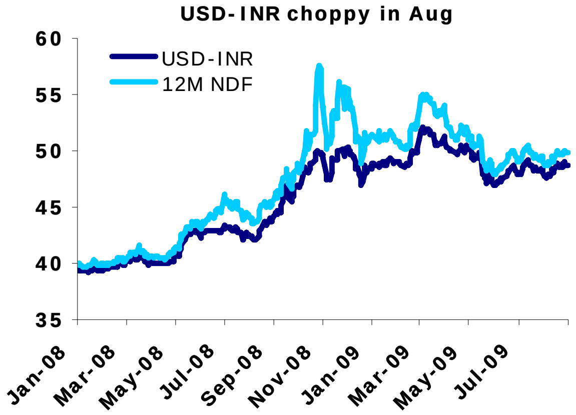
Yeo Han Sia

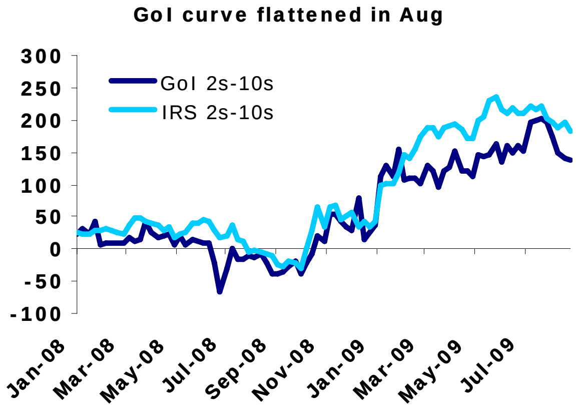
Economic Data – India

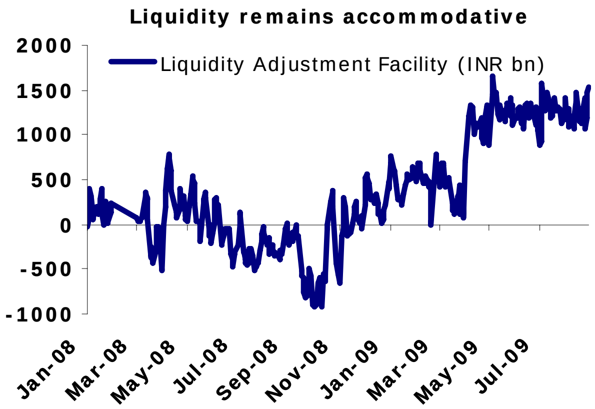
Monthly data	**Dec-08**	**Jan-09**	**Feb-09**	**Mar-09**	**Apr-09**	**May-**	**Jun-09**	**Jul-09**
Industrial Production, % y/y	-0.2	1.0	0.2	0.3	1.2	2.2	7.8	N/A
Passenger Vehicle Sales, % y/y	-13.9	-6.9	15.0	-1.2	4.4	-0.8	8.3	29.2
Wholesale Price Index, % y/y	5.9	4.5	3.1	0.8	1.7	0.9	-1.6	-1.6
Exports, % y/y	-13.2	-16.8	-21.7	-33.3	-33.2	-29.2	-27.7	N/A
Imports, % y/y	-8.4	-19.2	-23.3	-34.0	-36.6	-39.2	-29.3	N/A
Trade Balance, US$ bn	-5.7	-6.1	-4.9	-4.0	-5.0	-5.2	-6.2	N/A
Foreign Exchange Reserves, US$ bn	246.6	238.9	238.7	241.4	241.5	251.5	254.1	251.5
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Real GDP, % y/y	9.0	9.3	8.6	7.8	7.7	5.8	5.8	6.1
-Agriculture	3.9	8.1	2.2	3.0	2.7	-0.8	2.7	2.4
-Industry	9.8	9.0	6.5	6.4	6.5	2.0	1.2	3.4
-Services	10.3	10.3	11.8	10.2	9.8	10.2	8.6	8.1
Nominal GDP, INR tn	9.9	11.5	11.9	11.6	11.8	13.1	12.9	N/A
Current Account, US$ bn	-4.3	-4.5	-1.5	-9.0	-12.5	-13.0	4.7	N/A
Capital Account, US$ bn	33.2	31.0	26.0	11.1	7.6	-4.3	-5.3	N/A

Sources: CEIC

India: FX and Rates Strategy







The 200-day MA continues to cap USD-INR gains, but the pair could breach this topside resistance on signs of fatigue in AXJ equity markets. Rate hike expectations are on the rise, but curve flattening in Aug appears overdone.

FX

USD-INR rose from a two-month low on improved risk aversion in Aug, but gains were again capped by the 200-day MA near the 49.10 level. Growth concerns continue to mount on the persistent monsoon rainfall deficit, but the faster than expected pace of output recovery in Q2 mitigates some of the downside risk. That said, market expectations on FY09/10 GDP growth could still be pared substantially if widespread drought hits India. Near-term, USD-INR is at risk of breaching topside resistance on signs of fatigue in the AXJ equity markets. Over the medium-term, we remain bullish on the INR with the domestic demand driven economy showing increasing signs of a recovery. The signing of the India-ASEAN free trade agreement in Aug (effective 2010) should also improve India's trade performance as tariff reductions are phased in over coming years.

Rates

We see growing risks of an RBI rate hike before Q2 2010. The widely-watched WPI is in negative territory at the moment, but other CPI measures remain stubbornly high and are on the rise again. Market rate hike expectations have also risen in the past month, generating bear-flattening in the G-Sec curve. While part of the sharp rise in front-end yields was related to the launch of the government's new Cash Management Bills, we continue to expect strategic flattening trades to gain favour as the year progresses. From a tactical perspective, however, the 70bps of flattening over the past month appears overdone when viewed against modest up-ticks in the OIS curve and the RBI's recent policy signals.

Earlier plans to restructure subsidy programmes could be sidelined with food and global oil prices firming. Price interventions could slow the rise in headline inflation, but a severe drought would stretch the FY09/10 budget further. While officials have in the past month emphasised repeatedly that the FY09/10 deficit target will be met, the balance of risks is tilting towards a larger financing gap on higher subsidy bills on food, employment and farm debt waivers.

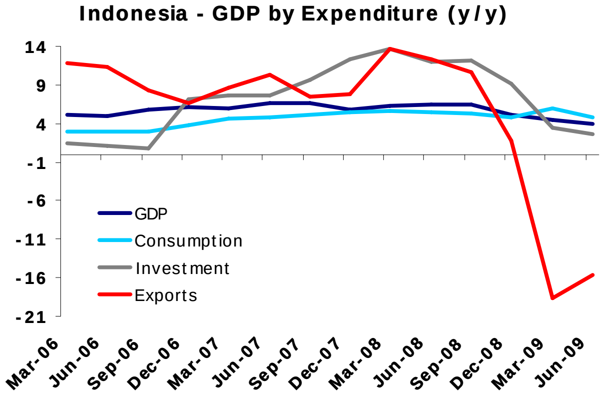
Yeo Han Sia

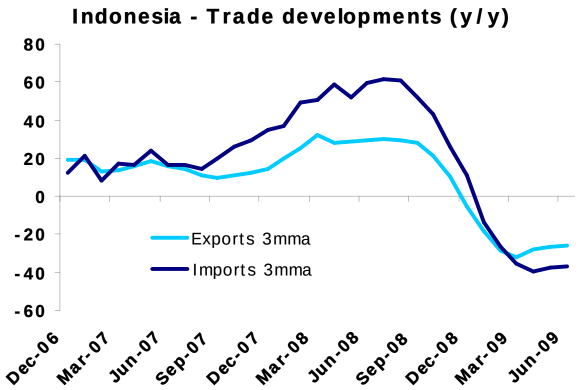
Market Forecasts – India (eop)

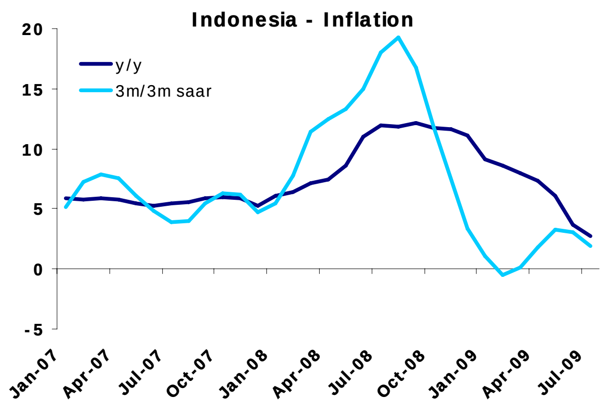
FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-INR	48.73	-0.2%	48.5	48.0	47.0	47.5	47.0	47.0
AUD-INR	41.08	20.1%	39.8	38.4	37.6	39.4	39.5	40.4
NZD-INR	33.39	18.4%	32.0	30.7	27.7	28.0	28.2	29.1
JPY-INR	0.52	-3.3%	0.495	0.480	0.448	0.440	0.427	0.420
EUR-INR	69.91	2.8%	68.9	66.2	64.9	66.5	65.8	66.7
Rates	**Current**	**Ytd (bps)**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
RBI's repo rate	4.75	-175	4.75	4.75	4.75	5.00	5.25	5.50
3-month MIBOR	4.51	-438	4.6	4.6	4.7	5.0	5.3	5.6
2-year IRS (versus NSE MIBOR)	5.29	85	5.1	5.1	5.3	5.6	6.1	6.4
10-year IRS	7.13	231	7.1	7.1	7.2	7.4	7.7	7.9

Sources: Bloomberg, ANZ

Country Update: Indonesia







Q2 GDP growth was above market expectations. Consumption growth eased but this was offset by an improvement in net exports and investment. Inflation remains low, but momentum has picked up. The re-election of President Yudhoyono will likely support consumer and business sentiment going forward, and we expect the economy to register growth of 4.6% this year.

- GDP grew by 4.0% (y/y) in Q2, down from 4.4% in Q1. The contributions to growth from domestic demand and net exports were about even, with consumption growth easing to 4.8% while net exports rose 21.5% due to lower imports. Investment remains weak but has reversed Q1's decline, growing 1.3% (q/q saar).
- Domestic demand remains buoyant. Retail sales grew for the fourth straight month, increasing 2.8% (y/y) in Jun compared with 4.8% in May. The consumer confidence index rose to 115.4 in Jul 2009, its highest level since Dec 2004.
- Motorcycle and auto sales in Jul also improved, rising 12.3% (m/m) and 5.9%, respectively, compared with 6.0% and 10.5% in Jun.
- Exports fell by 27.2% (y/y) in Jun, against a 28.7% decline in May, as trade in industrial and agricultural sectors remained muted. Imports improved to -32.7% in Jun, compared with -34.5% in May, resulting in a trade surplus of $1.4bn in Jun.
- Inflation eased further to 2.7% in Jul from 3.7% a month earlier; however, momentum has turned up.
- Manufacturing production was up by 2.1% (q/q) in Q2 2009, reversing two quarters of negative growth. This was largely due to the increased production of textiles, metals and minerals, and motor vehicles and parts.
- Cement consumption increased by a modest 2.2% (m/m) in Jul 2009, supported by infrastructure and construction activity related to the government's stimulus package.
- Bank Indonesia lowered its benchmark rate by 25bps to 6.5% and signalled that it is now at the end of the easing cycle. It also signalled a shift in focus toward the management of inflation expectations.

Chang Weir Lang

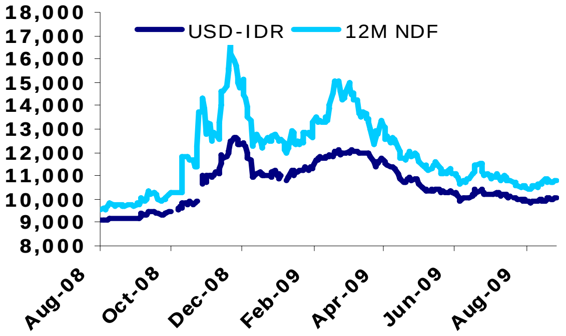
Economic Data – Indonesia

Monthly data	Dec-08	Jan-09	Feb-09	Mar-09	Apr-09	May-	Jun-09	Jul-09
Industrial Production, % y/y	-1.9	-1.7	0.9	1.4	1.1	-0.1	0.2	N/A
Retail Sales Index, % y/y	-5.0	2.9	-8.2	5.9	4.2	4.8	2.8	N/A
Consumer Price Index, % y/y	11.1	9.2	8.6	7.9	6.0	4.6	3.7	2.7
Exports, % y/y	-18.7	-35.0	-32.3	-28.3	-22.6	-28.7	-27.2	N/A
Imports, % y/y	-8.0	-27.9	-40.1	-33.7	-41.6	-34.5	-32.7	N/A
Trade Balance, US$ bn	2.6	1.9	2.4	3.3	3.0	3.0	2.9	N/A
Foreign Exchange Reserves, US$ bn	49.2	48.3	47.9	52.2	54.0	55.2	54.9	54.8
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Real GDP, % y/y	6.6	5.8	6.2	6.4	6.4	5.2	4.4	4.0
-Private consumption	5.1	5.5	5.7	5.5	5.3	4.8	6.0	4.8
-Government consumption	6.5	2.0	3.6	5.3	14.1	16.4	19.2	17.0
-Gross fixed capital expenditure	9.7	12.4	13.7	12.0	12.2	9.1	3.4	2.7
Nominal GDP, IDR tn	1,030.8	1,034.9	1,117.6	1,229.6	1,332.5	1,274.3	1,301.8	1,365.5
Current Account, US$ bn	2.2	3.4	2.8	-1.0	-0.9	-0.7	2.9	3.1
Capital & Financial Account, US$ bn	-0.9	0.7	-1.4	2.5	0.9	-3.3	1.8	-2.4

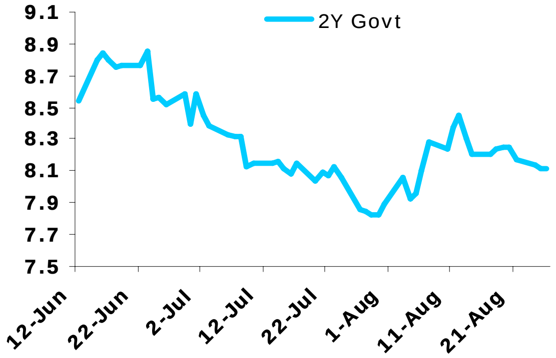
Sources: CEIC

Indonesia: FX and Rates Strategy

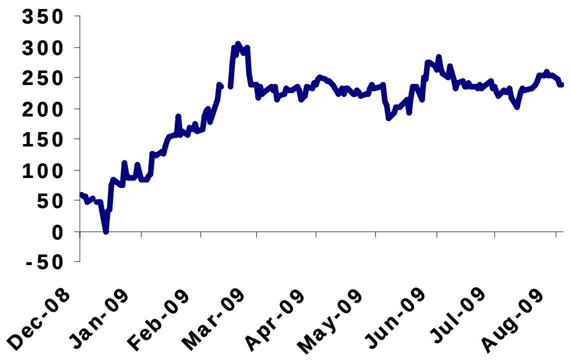
USD-IDR downmove has stalled



Yields have troughed



2s-10s GOV steepening has stalled



The IDR is starting to face headwinds, having shed 1.5% against the USD in Aug. Although sustained risk appetite should maintain the broad downtrend in USD-IDR into year-end, scope for further out-performance within AXJ appears limited.

FX

The IDR has been an out-performer within AXJ this year, rallying 9% against the USD compared with the (un-weighted) average gain of 0.4% for AXJ as a whole. The IDR has been supported by: 1/ a correction from unfair punishment last year (when Indonesia's relatively strong fundamentals were ignored), 2/ the removal of political uncertainty with the re-election in July of a market-friendly incumbent President Yudhoyono, and 3/ attractive yields.

Going forward, the IDR should continue to benefit on an outright basis from sustained risk appetite and attractive yields. In relative terms, however, the IDR faces headwinds: more near-term from an over-extended stock market, and further down the road from inflation. After the 22% correction in Chinese equities during Aug, year-to-date gains of 73% on the Jakarta stock exchange look quite over-extended. Meanwhile, inflation momentum has reversed and is set to pickup further, even before highly favourable y/y base effects have unwound.

Rates

In line with market expectations, Bank Indonesia (BI) delivered one last rate cut of 25bps and signalled the end of its easing cycle at its meeting on 5 Aug. Although official rate hikes are some way off and Indonesia's high yields will remain appealing to investors seeking to enhance returns, favourable inflation momentum has already reversed on a m/m basis. In response, BI has already signalled a shift in focus toward the management of inflation expectations, reflecting Indonesia's smaller output gap and suggesting that the central bank seeks to improve its inflation-fighting record. For now, a shift to neutral from over-weight in IDR bond allocations appears sufficient.

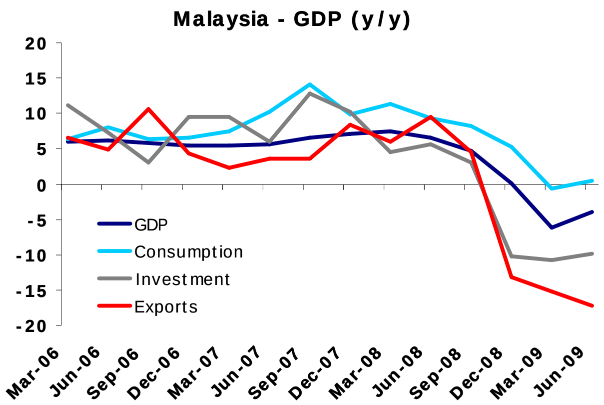
Tamara Henderson

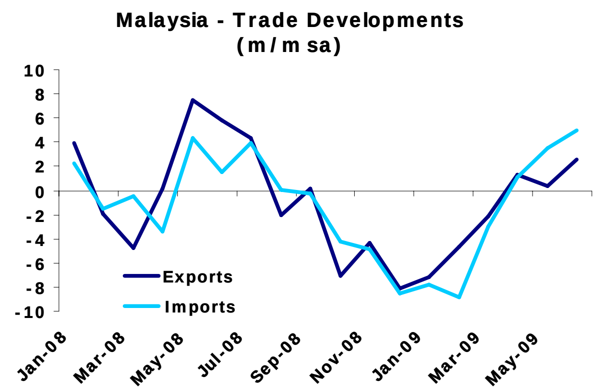
Market Forecasts – Indonesia (eop)

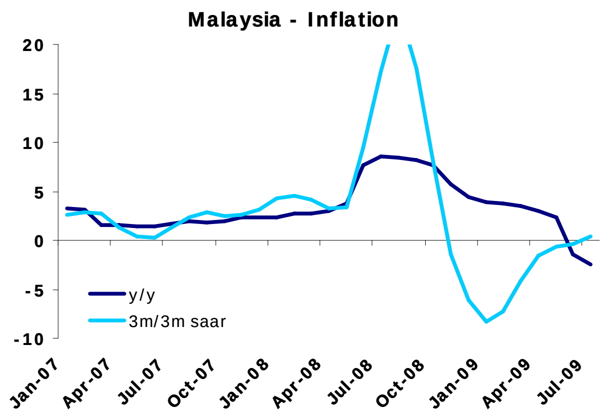
FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-IDR	10,060	-9.5%	10,250	9,750	9,500	9,625	9,250	9,000
AUD-IDR	8,399	5.5%	8,400	7,800	7,600	8,000	7,800	7,700
NZD-IDR	6,889	5.0%	6,800	6,200	5,600	5,700	5,600	5,600
JPY-IDR	107	-14.3%	100	100	90	90	80	80
EUR-IDR	14,378	-9.2%	14,600	13,500	13,100	13,500	13,000	12,800
Rates	**Current**	**Ytd (bps)**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
BI's bank rate	6.50	-275	6.50	6.50	6.50	6.75	7.00	7.00
3-month JIBOR	7.01	-512	7.1	7.0	6.9	7.2	7.4	7.7
2-year IDR bond yield	8.12	-330	8.1	8.0	7.9	8.1	8.4	8.6
10-year IDR bond yield	10.51	-138	11.2	10.8	10.5	10.6	10.7	10.8

Sources: Bloomberg, ANZ

Country Update: Malaysia







Malaysia's Q2 GDP growth surprised on the upside, boosted by higher consumption and investment. However, the picture is not all rosy with net exports remaining tepid, reflecting weak demand for electronics, the country's major export product. Inflation momentum seems to be turning but should remain subdued given a still sizeable output gap.

- Q2 GDP growth improved to -3.9% (y/y) in Q2 from -6.3% in Q1. Consumption showed notable improvement, growing 0.5% in Q2 from -0.7% in Q1. Investment also stabilised, with the y/y decline narrowing to -9.8% in Q2 from -10.8% previously.
- Consumption indicators show signs of stabilisation. Retail sales growth declined to 2.8% (y/y) in Q2 from -7.8% in the previous quarter. However, the q/q sequential decline has reversed, with sales rising by 1.0% on a q/q sa basis.
- Industrial production plunged 9.6% (y/y) in Jun, driven by declines in manufacturing and mining activities. However, this represented a seasonally-adjusted m/m increase of 1.2%, indicating firming activity. Manufacturing output also posted an increase of 1.6% (m/m sa) from May.
- Manufacturing sales fell by 25.5% (y/y) in Jun, marginally better than the 25.9% drop in May. This was primarily led by cutbacks in the iron/steel sector and plastics manufacturing.
- Exports remain weak but the pace of decline has slowed considerably. We estimate that Q2 exports fell by a marginal 0.8% (q/q saar), compared with -11.5% in Q1. Imports rebounded strongly in Q2, rising by 35.3% (q/q, saar) with capital equipment such as machinery and transport accounting for more than half of all imports. Net exports were little changed, falling just -0.7% (y/y).
- Consumer prices fell by 2.4% (y/y) in Jul, a second straight month of deflation. This reflected base effects from lower petrol and diesel prices. However, inflation momentum was positive, with prices rising 1.1% (m/m, sa).
- Bank Negara Malaysia kept its overnight rate unchanged at 2.00%, in line with market expectations. The central bank said that there had been signs of improvement in the global economic picture and believes that the current monetary policy stance is appropriate and would support economic activity.

Chang Wei Liang

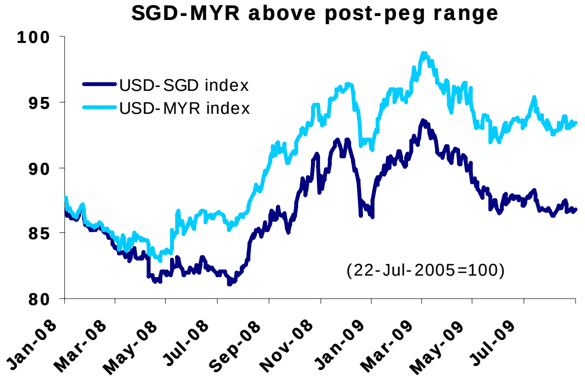
Economic Data – Malaysia

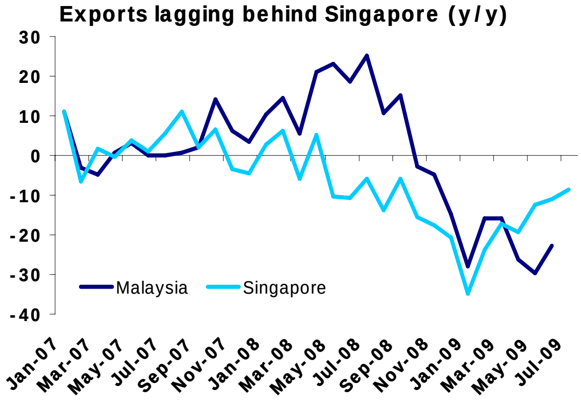
Monthly data	Dec-08	Jan-09	Feb-09	Mar-09	Apr-09	May-	Jun-09	Jul-09
Industrial Production, % y/y	-15.9	-17.9	-12.5	-12.6	-11.7	-11.4	-9.6	N/A
Manufacturing Sales, % y/y	2.1	-1.9	-21.0	-25.6	-26.3	-25.9	-25.5	-27.8
Consumer Price Index, % y/y	4.4	3.9	3.7	3.5	3.0	2.4	-1.4	-2.4
Exports, % y/y	-14.9	-27.8	-16.0	-15.7	-26.3	-29.7	-22.6	N/A
Imports, % y/y	-22.8	-30.4	-27.6	-29.0	-22.4	-27.8	-20.8	N/A
Trade Balance, USD bn	3.3	2.2	3.3	3.4	2.1	2.9	2.6	N/A
Foreign Exchange Reserves, US$ bn	85.7	85.9	85.3	82.4	81.9	82.2	85.3	84.4
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Retail Sales, % y/y	39.7	35.7	19.8	23.8	25.4	16.5	7.8	2.8
Real GDP, % y/y	6.5	7.2	7.4	6.6	4.8	0.1	-6.3	-3.9
-Private consumption	14.2	9.9	11.3	9.4	8.2	5.3	-0.7	0.5
-Government consumption	6.0	4.0	14.1	10.3	6.4	12.7	2.1	1.0
-Gross fixed capital formation	12.7	10.2	4.6	5.6	3.1	-10.2	-10.8	-9.8
Nominal GDP, MYR bn	165.4	176.2	175.5	188.5	197.6	177.0	155.3	161.3
Current Account, US$ bn	8.6	8.0	7.2	11.7	11.2	8.6	8.6	N/A
Capital & Financial Account, US$ bn	-9.0	-5.2	8.6	-3.4	-18.0	-20.8	-8.2	N/A

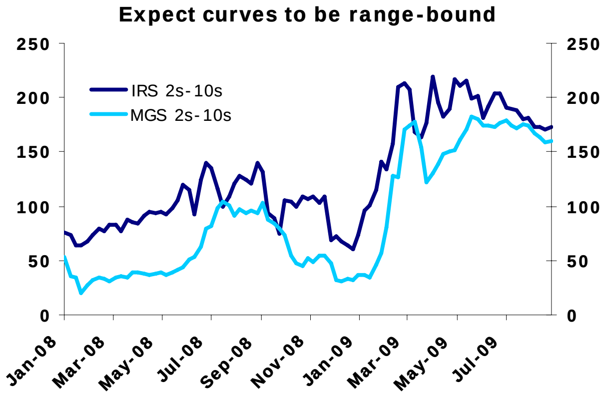
Sources: CEIC

Malaysia: FX and Rates Strategy

The stronger than expected recovery in Q2 has pared risk of further MYR weakness, but the underperforming external sector weighs on near-term prospects. Focus will shift to the 2010 budget in the coming weeks; aggressive fiscal consolidation could spark a knee-jerk bull-flattening of the MGS curve.







FX

USD-MYR traded in a narrow range of 3.48 to 3.55 in Aug, and is now at the midpoint near the 3.52 level. The MYR is the second worst performing AXJ currency in 2009 so far, and we see limited scope for USD-MYR to rise further from here. Q2 GDP surprised on the upside at 4.8% q/q, narrowing Malaysia's growth underperformance with other AXJ economies. The decline in private consumption eased sharply, with consumer sentiment surveys indicating a recovery into H2. The accelerated implementation of fiscal stimulus measures in Q2 should also contribute to the rebound in domestic demand. As a major natural resource producer in the region, the stabilisation in global commodity prices should ease the growth drag from the mining sector. However, the weak external sector continues to weigh on MYR's near-term prospects given uncertainty over the sustainability of a domestic demand-driven recovery. The relative out-performance in Singapore's exports could sustain SGD-MYR above the post-peg trading range of 2.20-2.40 in the coming months.

Rates

BNM's Aug policy statement was noticeably more upbeat on the economic outlook, though the overall assessment on growth prospects in H2 and 2010 remained unchanged. Governor Zeti indicated after the Q2 GDP release that the official GDP forecast of a 4 to 5% contraction will be revised in view of recent improvements, but we expect the revision to be largely 'technical' in nature. That said, more stable economic conditions have reduced the need for another fiscal stimulus package, limiting the prospects for MGS curve-steepening. Indeed, Second Finance Minister Ahmad Husni announced that the 23 Oct budget will cut operating expenditures by 15%, with plans to introduce means testing on fuel subsidies to lower the subsidy bill. While aggressive fiscal consolidation in 2010 could trigger a knee-jerk bull-flattening of the MGS curve, we expect the 2s-10s spread to remain largely range-bound until clearer signs of improvement in external demand emerge.

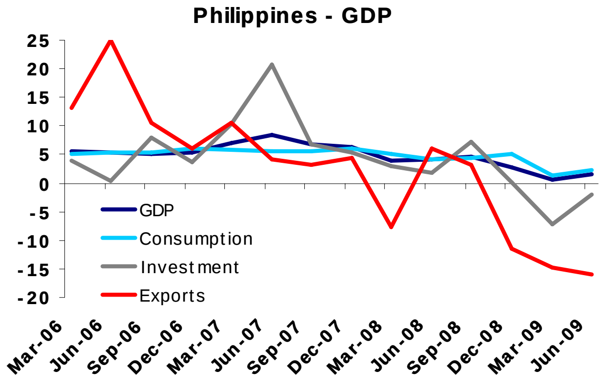
Yeo Han Sia

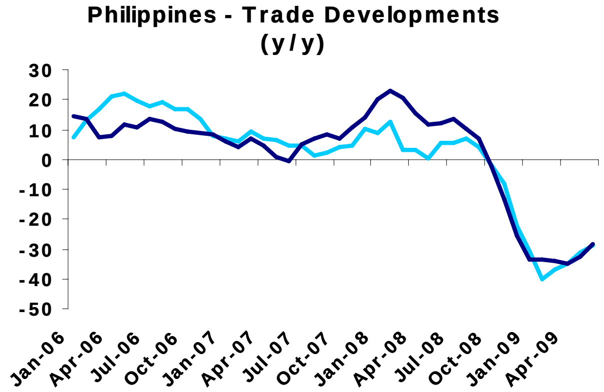
Market Forecasts – Malaysia (eop)

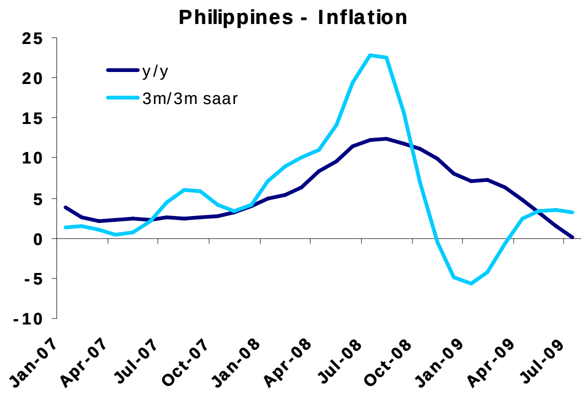
FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-MYR	3.52	1.6%	3.55	3.50	3.48	3.45	3.40	3.40
AUD-MYR	2.97	22.3%	2.91	2.80	2.78	2.86	2.86	2.92
NZD-MYR	2.41	20.5%	2.34	2.24	2.05	2.04	2.04	2.11
JPY-MYR	3.75	-10.5%	3.62	3.50	3.31	3.19	3.09	3.04
EUR-MYR	5.05	4.7%	5.04	4.83	4.80	4.83	4.76	4.83
Rates	**Current**	**Ytd (bps)**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
BNM's overnight policy rate	2.00	-125	2.00	2.00	2.00	2.00	2.25	2.25
3-month KLIBOR	2.14	-123	2.1	2.1	2.1	2.1	2.3	2.3
2-year IRS (versus 3M KLIBOR)	2.76	-6	2.7	2.7	2.8	2.8	3.0	3.1
10-year IRS	4.47	97	4.5	4.5	4.6	4.6	4.7	4.8

Sources: Bloomberg, ANZ

Country Update: Philippines







Q2 GDP growth beat market expectations largely due to buoyant domestic demand, which boosted consumption and investment. Net exports were weaker due to increasing imports, but trade activity has recovered from its nadir in Q1. Inflation remains low but momentum appears to be turning positive.

- GDP grew 1.5% (y/y) in Q2, up from 0.6% in Q1. Consumption rose 2.3% from 1.3% in the previous quarter, reflecting improved sentiment with the worst of the economic crisis now past. Investment also improved significantly, with the decline narrowing to -1.9% in Q2 from -7.2% in Q1. In fact, foreign direct investment grew strongly in the first five months of the year, rising 86.0% from the same period a year ago.
- Overseas remittances reached a record $1.5bn in Jun, growing by 3.3% (y/y). Remittance flows amounted to $8.5bn during H1 2009, a gain of 2.9% over the same period last year. Improving global economic conditions and new employment arrangements with other countries should be supportive for remittances growth in 2009.
- Bank lending continued to be strong, growing by 11.1% (y/y) in Jun, compared with a 10.2% increase in May. Major contributors were the loans to the agriculture and real estate sectors which grew by 38.7% and 27.6%, respectively.
- Exports staged a strong rebound, increasing by 27.2% (q/q saar) in Q2. However, shipments still remain below their Q3 2008 level. Imports also grew strongly on a quarterly basis, resulting in a smaller contraction of 2.7% (y/y) in Q2 compared to -20.6% in Q1.
- Inflation eased to 0.2% (y/y) in Jul, down from 1.5% a month earlier, but momentum appears to be rising.
- The government reported a larger than expected monthly budget deficit of PHP34.6bn in Jul on account of increased government spending and faltering tax revenues. We estimate that the 2009 deficit will widen beyond the PHP250bn target set by the government.
- The BSP kept the benchmark overnight borrowing rate unchanged at a record low of 4.00%, ending its eight-month easing campaign. The bank announced that it will keep rates steady until next year as it expects inflation to remain within its target range.

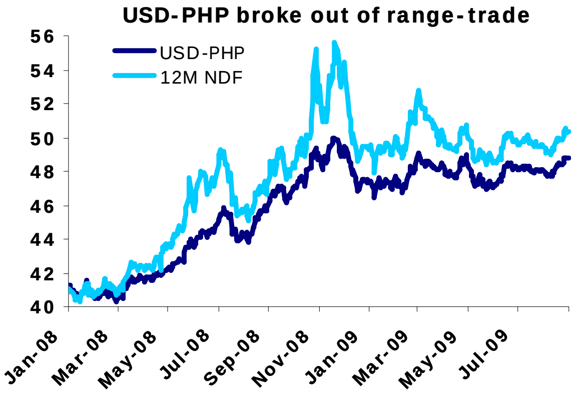
Chang Wei Liang

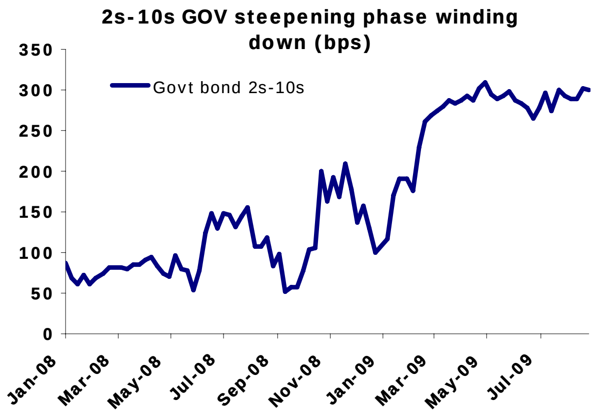
Economic Data – Philippines

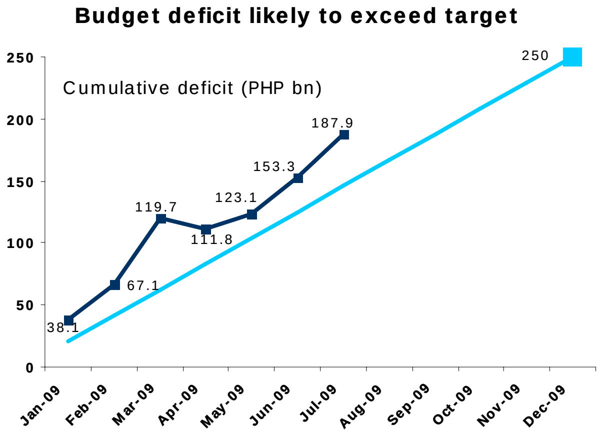
Monthly data	**Dec-08**	**Jan-09**	**Feb-09**	**Mar-09**	**Apr-09**	**May-**	**Jun-09**	**Jul-09**
Manufacturing Production Value-add, % y/y	-10.2	-24.5	-20.7	-11.9	-17.5	-13.0	N/A	N/A
Passenger Car Sales, % y/y	-19.5	13.9	1.0	0.2	-5.7	3.1	-0.4	-7.0
Consumer Price Index, % y/y	8.0	7.1	7.3	6.4	4.8	3.3	1.5	0.2
Exports, % y/y	-40.3	-40.6	-39.0	-30.8	-35.2	-26.9	-26.9	N/A
Imports, % y/y	-34.0	-34.5	-31.9	-36.2	-37.4	-24.3	-24.3	N/A
Trade Balance, US$ bn	-0.6	-0.8	-0.6	-0.4	-0.2	-0.5	-0.5	N/A
Foreign Exchange Reserves, US$ bn	32.6	34.1	33.6	33.9	34.3	34.1	39.6	N/A
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Real GDP, % y/y	6.8	6.3	3.9	4.2	4.6	2.9	0.6	1.5
-Private consumption	5.7	6.2	5.1	4.1	4.4	5.0	1.3	2.3
-Government consumption	-2.6	8.0	-0.3	0.0	11.8	2.6	4.5	9.1
-Gross fixed capital formation	6.8	5.3	3.0	1.7	7.1	0.1	-7.2	-1.9
Nominal GDP, peso bn	1,610.7	1,895.7	1,660.3	1,833.9	1,853.4	2,075.5	1,738.8	1,869.9
Current Account, US$ bn	1.3	2.0	1.3	0.9	-0.3	2.3	2.2	N/A
Capital & Financial Account, US$ bn	3.1	-0.1	0.5	0.4	0.4	-3.3	-0.8	N/A

Sources: CEIC

Philippines: FX and Rates Strategy







Improving economic indicators should limit USD-PHP gains to the Mar high of 49.20 after the pair broke out of its range-trade in Aug. The BSP signalled a neutral stance in Aug, but strong Q2 GDP data appear to have shifted its policy bias toward tightening.

FX

USD-PHP broke out of its range-trade in mid-Aug, breaching trend line resistance to gain 1.6% during the month. Year-to-date, the PHP tops the list of the worst performing AXJ currencies, having lost 3% against the USD in the first eight months of the year. However, with economic indicators showing signs of improvement, any short-term pull back in USD-PHP is likely to be limited to the Mar high of 49.20. Remittance inflows have stabilised in the 3 to 4% (y/y) range in H1, reaching a record high of $1.5bn in Jun and beating market expectations for a contraction this year. GDP growth also surprised at 2.4% q/q in Q2, with private consumption rebounding to 1.8% from -2.6% in Q1. Notwithstanding the recovery in domestic demand, an underperforming external sector continues to be a drag, limiting the scope for PHP gains in the coming months.

Rates

The BSP left its policy rate unchanged at 4.00% on 20 Aug and signalled a neutral policy stance. The risk between growth and inflation is now seen as "fairly balanced"; the BSP also pledged to leave the policy rate unchanged for "as long as necessary." While this is broadly in line with our view of steady interest rates into H1 2010, the surprisingly strong Q2 GDP print on 27 Aug appears to have shifted the BSP's stance slightly in favour of tightening. Deputy Governor Guinigundo said that the strong Q2 data vindicated the BSP's stand pat stance in Aug, from which "a possible shift in monetary policy may be decided." As such, we see increasing risk of a rate hike as soon as Q2. While the GOV curve remains range-bound, we favour strategic flattening trades in anticipation of higher headline inflation from fading base effects and rising inflation momentum into year-end.

Meanwhile, monthly budget numbers continue to disappoint. The cumulative deficit rose to PHP188bn in Jul, on track to breach the full year target of PHP250bn as early as Sep. The decision to restart plans to issue retail Treasury bonds (RTB) also hints at increasing funding pressure. After shelving plans to reissue RTBs in Jul, the government is now in talks with banks to tap retail savings to fund the deficit.

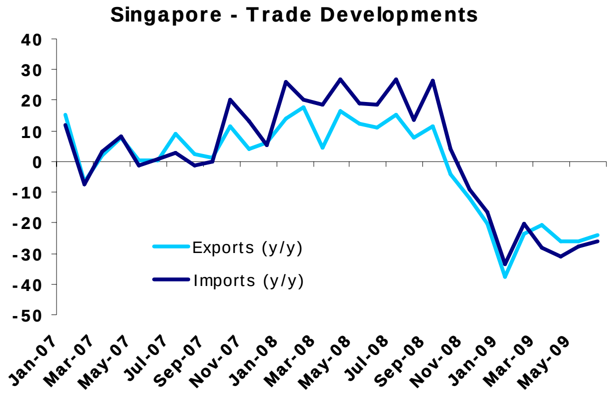
Yeo Han Sia

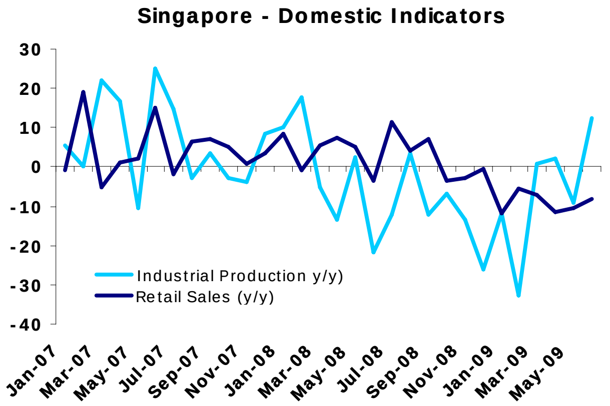
Market Forecasts – Philippines (eop)

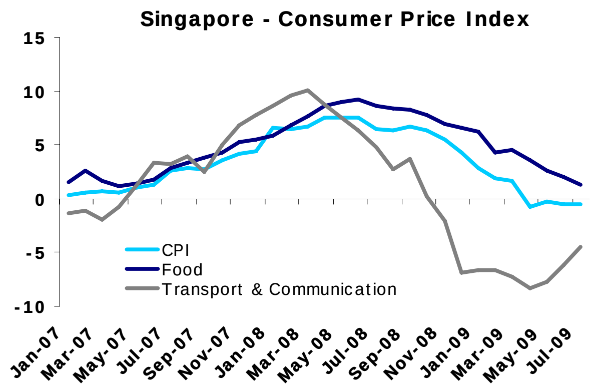
FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-PHP	48.80	2.7%	49.0	48.0	48.0	47.0	47.0	46.0
AUD-PHP	41.12	23.5%	40.2	38.4	38.4	39.0	39.5	39.6
NZD-PHP	33.40	21.7%	32.3	30.7	28.3	27.7	28.2	28.5
JPY-PHP	0.52	-0.5%	0.500	0.480	0.457	0.435	0.427	0.411
EUR-PHP	69.99	5.7%	69.6	66.2	66.2	65.8	65.8	65.3
Rates	**Current**	**Ytd (bps)**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
BSP's overnight reverse repo rate	4.00	-150	4.00	4.00	4.00	4.00	4.25	4.25
3-month PHIBOR	4.19	-106	4.2	4.2	4.2	4.3	4.5	4.5
2-year IRS (versus 3M IB ref rate)	4.71	64	4.5	4.7	4.8	5.0	5.3	5.4
10-year IRS	6.03	-7	6.0	6.1	6.1	6.3	6.4	6.5

Sources: Bloomberg, ANZ

Country Update: Singapore







Singapore's economy is showing signs of recovery and the record fiscal stimulus will likely not have to be extended. Non-oil domestic exports fell the least in ten months. Industrial production unexpectedly rebounded on pharmaceutical gains. Inflation declined in Jul, matching Jun's retreat on lower housing and transport costs. The decline in retail sales eased, boosted by a month-long island-wide sale.

- Q2 GDP rose by an annualised 20.7% (q/q), after shrinking by a revised 12.2% in the first quarter as manufacturing and services improved. The economy is showing signs of recovery after contracting by 6.5% (y/y) in the first half of 2009. PM Lee announced that the record S$20bn fiscal stimulus spending unveiled in Jan will not have to be extended.
- Retail sales fell 8.2% (y/y) in Jun after sliding by a revised 10.4% in May, as an annual island-wide sale boosted spending. Department store sales rose 3.5%.
- Singapore's non-oil domestic exports dropped 8.5% (y/y) in Jul, contracting by a revised 11.1% in Jun. The official forecast for exports in 2009 has been revised to a range of -10% to -12%, from the previous estimate of -13%. Electronic shipments dropped by 14.5% while non-electronics shipments (which include petrochemicals and pharmaceuticals) fell 4.8%.
- Industrial production unexpectedly rebounded by 12.4% (y/y) in Jul as pharmaceuticals output surged by 139.2%. Excluding biomedical manufacturing, production contracted 7.4% in Jul, after shrinking by a revised 13.8% in Jun.
- Inflation in Jul was -0.5% (y/y), matching Jun's retreat, amid lower housing and transport costs. Food prices rose by 1.3% while transport and communication costs fell 3%. Housing costs declined by 1.3%.
- The central bank will review its policy as scheduled in Oct and has revised the official inflation estimate for 2009 to a range of 0.5% to -0.5% from an earlier estimate for a decline of 1%.
- In Aug 2009, the STI index declined by 2% on profit-taking and expectations of weak corporate earnings.

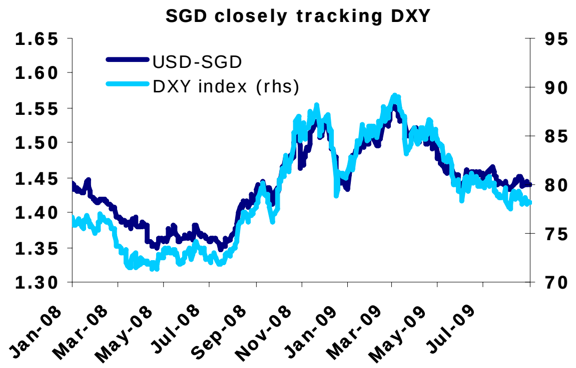
Ivy Tan

Economic Data – Singapore

Monthly data	**Dec-08**	**Jan-09**	**Feb-09**	**Mar-09**	**Apr-09**	**May-**	**Jun-09**	**Jul-09**
Industrial Production, % y/y	-13.4	-26.2	-11.8	-32.7	0.7	2.2	-9.0	12.4
Retail Sales, % y/y	-0.6	-11.8	-5.5	-7.0	-11.5	-10.4	-8.2	N/A
Consumer Price Index, % y/y	4.3	2.9	1.9	1.6	-0.7	-0.3	-0.5	-0.5
Domestic Exports (Non-oil), % y/y	-20.8	-34.9	-23.8	-17.3	-19.2	-12.6	-11.1	-8.5
Imports (Non-oil), % y/y	-14.0	-29.1	-17.3	-25.4	-26.6	-20.0	-18.6	-18.7
Trade Balance, US$ bn	0.7	0.5	0.8	2.7	2.4	1.6	1.6	2.6
Foreign Exchange Reserves, US$ bn	168.9	169.2	166.0	164.9	166.6	169.3	172.1	172.2
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Real GDP, % y/y	9.5	5.5	6.7	2.5	0.0	-4.2	-9.5	-3.5
-Private consumption	6.3	5.8	4.1	4.4	2.7	-1.2	-4.2	-3.7
-Government consumption	-0.6	9.5	10.4	9.0	9.9	2.7	-1.7	6.3
-Gross fixed capital formation	15.4	17.0	30.5	25.0	14.9	-9.9	-15.1	-7.2
Nominal GDP sa, SGD bn	64.2	66.5	66.0	64.3	64.5	62.8	59.7	62.3
Current Account, US$ bn	11.5	6.3	8.1	6.7	7.7	4.5	4.1	4.9
Capital & Financial Account, US$ bn	-8.0	0.7	2.0	-3.8	-8.6	-1.1	-7.8	-4.1

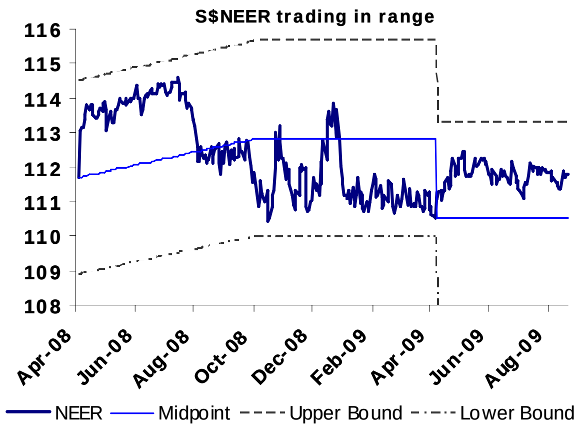
Sources: CEIC

Singapore: FX and Rates Strategy

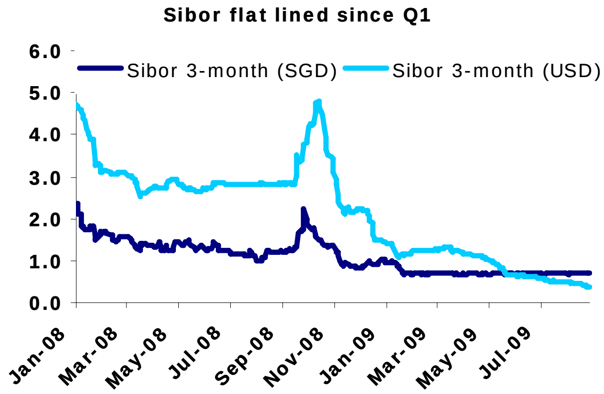


Recent economic data point to a recovery, but the authorities' policy focus will likely remain centred on growth in H2. We see the MAS holding its S$NEER policy bias unchanged in Oct, but growing evidence of speculative activity in the housing market could prompt the central bank to withdraw liquidity support earlier.

FX



Economic data released in Aug indicate a recovery is now underway. Final Q2 GDP showed that the economy rebounded more than expected at an annualised pace of 20.7% (q/q), beating the market consensus of a slight downgrade to 19.2%. Unemployment unexpectedly stabilised at 3.3% in Q2, though in part due to lower labour force participation. Retail sales, exports and industrial production were also stronger than expected. The rebound in asset prices was also evident in the property market, with private housing transactions hitting a record high in Jul and the authorities warning of "signs of speculation." However, the growing signs of a recovery did not alter policymakers' views on the economy. The government warned of more job losses in H2, describing the pace of recovery to be "neither quick nor strong." The MAS also reaffirmed its neutral policy stance after the release of the Q2 economic report. Market participants broadly concurred with the authorities' assessment, with the S$NEER trading in the familiar 0.5-1.5% range. USD-SGD mirrored the moves in the DXY, holding in the 1.4310 to 1.4530 range. We continue to expect the zero S$NEER appreciation bias to be maintained into 2010.



Rates

Inter-bank rates continue to hold in the 0.65-0.70% range on comfortable liquidity conditions and slowing credit demand. Sibor rates are expected to harden in 2010, but the timing will largely depend on the Fed. However, we see a risk of the MAS withdrawing liquidity support before the Fed does. The trigger is likely to come from growing evidence of speculative activity in the property market. Meanwhile, front-end IRS yields remain capped by benign inflation expectations and historically low Sibor rates.

Yeo Han Sia

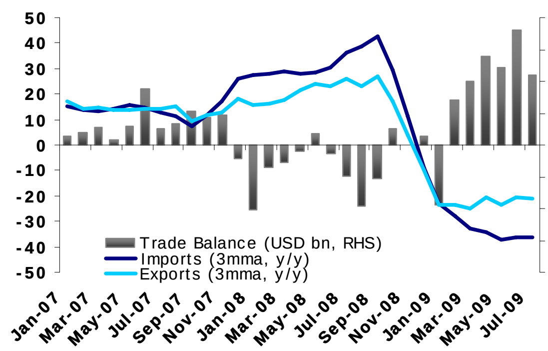
Market Forecasts – Singapore (eop)

FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-SGD	1.439	0.6%	1.47	1.46	1.45	1.44	1.44	1.43
AUD-SGD	1.213	20.7%	1.21	1.17	1.16	1.20	1.21	1.23
NZD-SGD	0.986	19.0%	0.97	0.93	0.86	0.85	0.86	0.89
JPY-SGD	1.532	-2.8%	1.50	1.46	1.38	1.33	1.31	1.28
EUR-SGD	2.064	3.3%	2.09	2.01	2.00	2.02	2.02	2.03
Rates	**Current**	**Ytd (bps)**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
3-month SIBOR	0.68	-27	0.69	0.69	0.85	1.00	1.30	1.50
2-year IRS (onshore versus 6M SOR)	1.65	9	1.7	1.8	1.9	2.1	2.2	2.4
10-year IRS	2.94	67	2.9	2.9	2.9	3.0	3.0	3.2

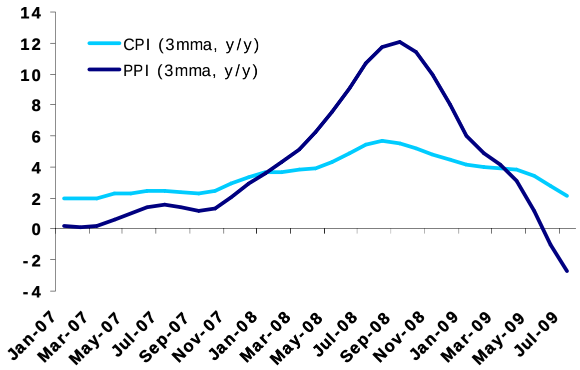
Sources: Bloomberg, ANZ

Country Update: South Korea

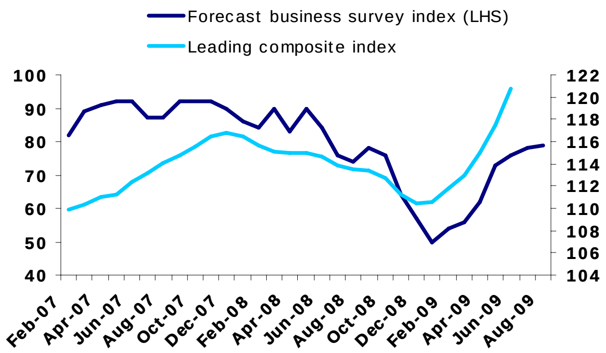
Korea - External Trade



Korea - Prices



Korea - Leading indicators



While domestic demand continues to recover as shown by the improving department store sales and rising consumer and business confidence, the external sector remains the laggard with shipments still falling by more than 20% in Jul. We maintain our growth forecast at 3.3% for 2010, highlighting the downside risks given the uncertain global economic outlook.

- Department store sales rose for the fifth straight month in Jul, gaining 4.0% (y/y), compared with Jun's 3.6%. Discount store sales, however, dropped by 6.0% in Jul against Jun's -1.4%.
- Exports fell by 20.1% (y/y) in Jul, the ninth consecutive decline, and compared with the 12.4% decline in Jun. Exports to China dropped the least, by 15.7% in the first 20 days of the month, compared with -26.5% for the US and -32.6% for Japan. Imports dropped by 35.8% in Jul, compared with Jun's -32.9%. The trade surplus stood at $5.1bn in Jul against $7.3bn in Jun.
- The CPI rose by 1.6% (y/y) in Jul, slower than the 2.0% increase in Jun. Core CPI inflation also fell to 3.2% in Jul from 3.5% in Jun. PPI inflation remained negative in Jul, the third month in a row, at -3.8%.
- The leading composite index rose 2.8% (m/m, sa) in Jun, after May's 2.2% rise, the sixth consecutive monthly increase. The forecast manufacturing business survey index for Sep rose to 93 from Aug's 80, now only 7 points below the 100 neutral level.
- Consumer confidence rose to 114 in Aug from 109 in Jul, the fourth consecutive month above the neutral level of 100 and the strongest since Q3 2007.
- The BoK kept the base rate unchanged at 2.00% for the sixth consecutive month, and will likely maintain its accommodative policy stance. The central bank remains concerned about the likelihood of a delay in the recovery of major advanced economies, and the heightened credit risks from the expansion in mortgage loans.
- We maintain our 2010 growth forecast at 3.3%, highlighting the downside risks given the uncertain global economic outlook.

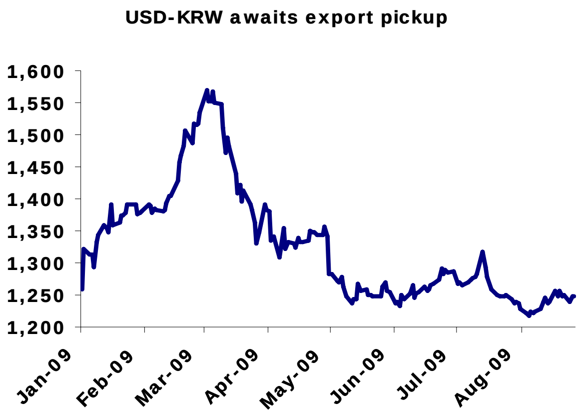
Franklin Poon

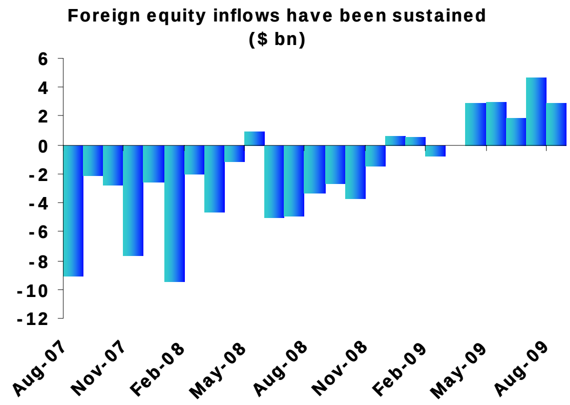
Economic Data – South Korea

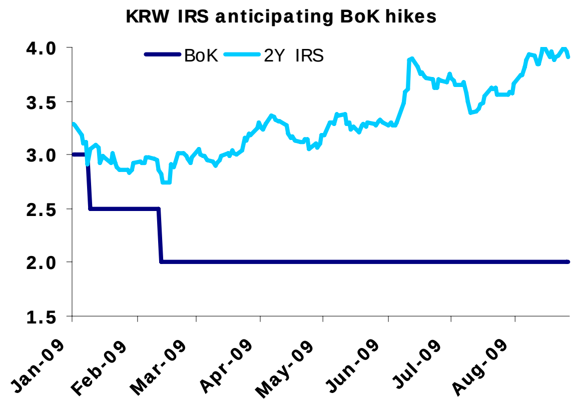
Monthly data	**Dec-08**	**Jan-09**	**Feb-09**	**Mar-09**	**Apr-09**	**May-**	**Jun-09**	**Jul-09**
Industrial Production, % y/y	-18.7	-25.5	-10.0	-10.5	-8.2	-9.0	-1.2	0.7
Retail Sales, % y/y	-1.2	-1.2	-3.9	-2.3	-1.4	1.8	6.6	N/A
Consumer Price Index, % y/y	4.1	3.7	4.1	3.9	3.6	2.7	2.0	1.6
Exports, % y/y	-17.9	-34.5	-18.5	-22.5	-19.9	-28.6	-12.5	-20.1
Imports, % y/y	-21.6	-31.4	-30.8	-35.7	-35.4	-40.0	-32.9	-35.8
Trade Balance, USD bn	0.5	-3.8	2.8	4.0	5.6	4.9	7.3	5.1
Foreign Exchange Reserves, US$ bn	201.0	201.6	201.8	206.4	212.5	226.5	231.2	238.8
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Real GDP, % y/y	4.9	5.7	5.5	4.3	3.1	-3.4	-4.2	-2.5
-Private consumption	5.4	4.7	4.0	2.3	1.4	-3.7	-4.4	-1.1
-Government consumption	4.8	4.7	3.6	4.0	4.5	4.7	7.3	7.0
-Gross fixed capital formation	1.5	3.1	-0.5	0.6	1.8	-7.3	-8.1	-4.0
Nominal GDP, KRW tn	246.7	263.1	240.8	260.7	261.5	260.9	236.9	N/A
Current Account, US$ bn	2.0	-0.8	-0.1	1.8	-1.3	0.9	6.6	5.4
Capital & Financial Account, US$ bn	-3.9	0.3	0.4	-3.6	-4.4	-4.8	-2.7	-0.4

Sources: CEIC

South Korea: FX and Rates Strategy







KRW remains trapped in the May range, still showing no inclination to challenge 1,200—a level that has held since last October. While a break below 1,200 is expected before year-end, portfolio tilts toward US equities may present a headwind over the near-term.

FX

USD-KRW remains trapped in a 17-week trading range, showing no inclination yet to challenge the 1,200 level. This despite sustained risk appetite from better-than-expected Q2 corporate earnings and GDP prints globally. Korean equities rallied 2% in Aug (in sharp contrast with the 22% sell-off in Chinese equities), but USD-KRW continues to shrug off strong foreign equity inflows. The BoK may be at work capping KRW gains, but we also suspect that there is a degree of equity portfolio rebalancing taking place, tilting toward US equities in anticipation of a US growth spurt. Within AXJ, Korea has attracted the lion's share of foreign equity inflows for the past seven weeks running. Aug inflows amounted to $3.0bn, bringing the total net foreign equity inflow to $15.3bn year-to-date versus an outflow of nearly $37bn in 2008. Meanwhile, FDI into Korea surged by 62% in Q2.

We continue to favour the KRW into 2010, expecting the KRW to be a primary beneficiary as global demand improves. The Korean economy is more sensitive to foreign demand conditions and Korean exports are much more competitive owing to the collapse of the KRW during the meltdown in global financial markets last year. Also, a landmark free trade agreement with the EU could take effect as early as H1 2010.

Rates

Korean local rates are expected to maintain a neutral-to higher bias, anticipating the BoK's eventual unwinding of monetary policy stimulus. We still think that rate hikes are a long way off, however, as any recovery in H2 would be very weak without the normalisation of discretionary demand in the US and Europe. This means Korea's negative output gap should remain wide enough to dissipate inflation pressures from domestic demand well into 2010. During the prolonged wait for BoK rate hikes, we favour curve flatteners which allow investors to earn positive carry while trimming interest rate risk.

Tamara Henderson

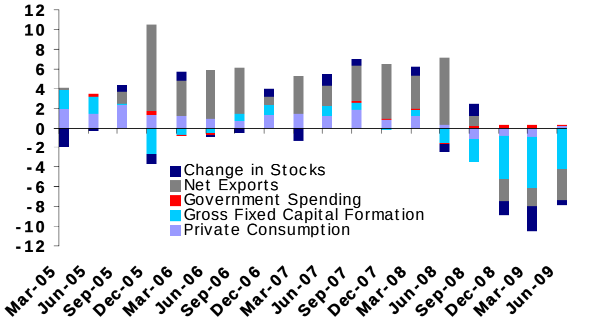
Market Forecasts – South Korea (eop)

FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-KRW	1248	-0.9%	1260	1125	1175	1150	1100	1050
AUD-KRW	1044	17.9%	1030	900	940	950	920	900
NZD-KRW	856	17.3%	830	720	690	680	660	650
JPY-KRW	13.28	-4.3%	12.9	11.3	11.2	10.6	10.0	9.4
EUR-KRW	1786	1.4%	1790	1550	1620	1610	1540	1490
Rates	**Current**	**Ytd (bps)**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
BOK's overnight call rate	2.00	-100	2.00	2.00	2.00	2.00	2.25	2.50
3-month KORIBOR	2.51	-144	2.5	2.6	2.6	2.7	3.0	3.2
2-year IRS (versus 91D KRW CD)	3.91	62	3.8	3.8	3.9	4.0	4.3	4.5
10-year IRS	4.49	92	4.4	4.5	4.6	4.6	4.7	4.8

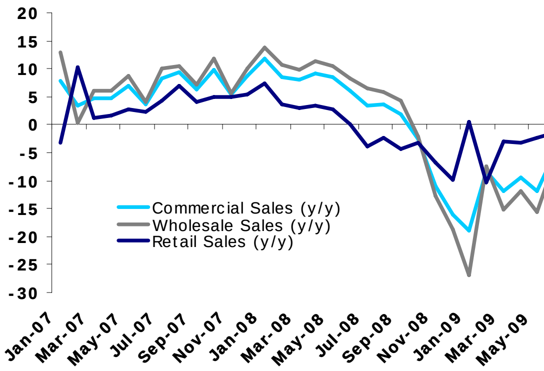
Sources: Bloomberg, ANZ

Country Update: Taiwan

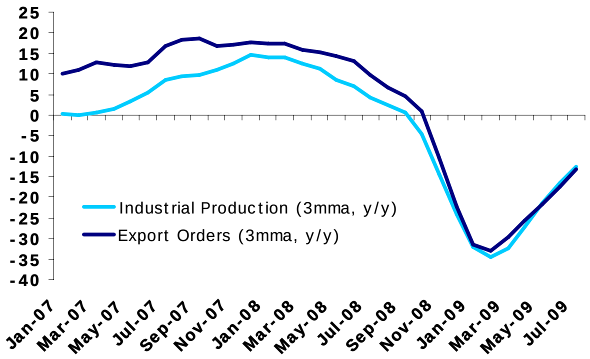
Taiwan - Contribution (ppt) to GDP y/y Growth



Taiwan - Domestic demand



Taiwan - Activity Indicators



Taiwan's economy has begun to turn around. Growth has been partly supported by China's stimulus measures. However, a recovery in Taiwan requires a broad-based rebound in foreign demand. We maintain our 2010 growth forecast at 3.9%.

- GDP grew by 20.7% (q/q, saar) in Q2, a sharp turnaround from Q1's -10.2%, ending the contraction of the previous three quarters. On an annual basis, GDP fell by 7.5%. Growth was supported by steady private consumption and increased government spending, while corporate investment and external demand remained weak.
- Commercial sales declined by 3.1% (y/y) in Jul, up from Jun's -4.5%. Excluding price effects, sales rose by 8.9%.
- Industrial production dropped by 8.1% (y/y) in Jul, the smallest decline in ten months, compared with Jun's -11.4%. Seasonally adjusted, the index rose by 1.2% (m/m). The output of electronics components, supported by China's increased rural consumption of electrical appliances, fell by only 0.8% (y/y).
- Exports fell by 24.4% (y/y) in Jul, against Jun's -30.4%. Shipments to China declined by 21.5%, while those to the US fell by 28.6%. Imports decreased by 34.1%, compared with Jun's -33.5%. The trade surplus rose to $2.0bn from $1.8bn in Jun.
- The CPI dropped by 2.3% (y/y) in Jul, compared with Jun's -2.0%. Excluding food and energy prices, the core index fell by 1%, from Jun's revised -0.8%.
- The composite leading index rose 2.3% (m/m, sa) in Jul, compared with Jun's revised 1.7%, the fifth consecutive monthly rise, signalling a continued improvement in the economic outlook.
- Export orders declined by 8.8% (y/y) in Jul, compared with Jun's -10.9%. Orders from China rose by 2.2%, while those from the US continued to fall, by 12.5%.
- The consumer confidence index rose to 56.2 (still well below the neutral line of 100) in Jul from 51.4 in Jun, the highest reading for the past year.
- The government plans a NT$100bn post-typhoon rehabilitation budget. Assuming spending over 5 years, this would amount to 0.2% of GDP per year.
- With the stronger than expected Q2 data, we have raised our 2009 growth forecast to -4.1%, but have kept our 2010 forecast unchanged at 3.9%. We see typhoon Morakot's growth impact as transitory.

Franklin Poon

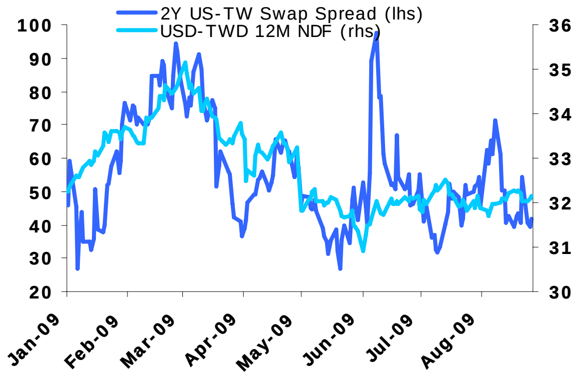
Economic Data – Taiwan

Monthly data	Dec-08	Jan-09	Feb-09	Mar-09	Apr-09	May-	Jun-09	Jul-09
Industrial Production, % y/y	-32.0	-43.3	-27.2	-25.8	-20.0	-18.4	-11.4	-8.1
Retail Trade Index, % y/y	-10.9	-1.0	-9.1	-2.8	-2.8	-2.4	1.2	3.7
Consumer Price Index, % y/y	1.3	1.5	-1.3	-0.1	-0.5	-2.4	-2.0	-2.3
Exports, % y/y	-41.9	-44.1	-28.6	-35.8	-34.3	-31.5	-30.4	-24.4
Imports, % y/y	-44.6	-56.5	-31.6	-49.5	-41.1	-39.1	-33.5	-34.1
Trade Balance, US$ bn	1.8	3.3	1.6	3.4	2.1	3.1	1.8	2.0
Foreign Exchange Reserves, US$ bn	291.7	292.7	294.2	300.1	304.7	312.6	317.6	321.1
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Real GDP, % y/y	7.0	6.4	6.2	4.6	-1.0	-8.6	-10.2	-7.5
-Private consumption	3.1	1.6	2.1	0.5	-2.1	-1.7	-1.6	0.4
-Government consumption	1.7	1.1	1.3	-0.2	1.2	2.2	3.7	1.5
-Gross fixed capital formation	3.8	-0.8	3.7	-8.0	-11.8	-22.6	-33.4	-23.7
Real GNP, % y/y	6.4	6.1	6.8	3.1	-0.5	-8.7	-10.5	-6.5
Nominal GDP, TWD tn	2.8	2.9	2.7	2.6	2.7	2.6	2.5	2.5
Current Account, US$ mn	6,477.0	11,183.	8,520.0	7,042.0	1,865.0	7,467.0	12,674.	9,915.0
Capital Account, US$ mn	-33.0	-18.0	-271.0	-20.0	-32.0	-11.0	-24.0	-17.0

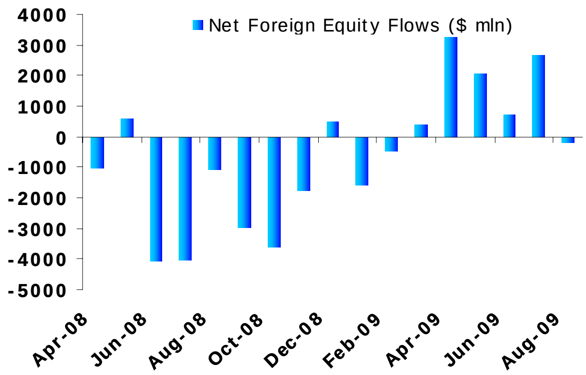
Sources: CEIC

Taiwan: FX and Rates Strategy

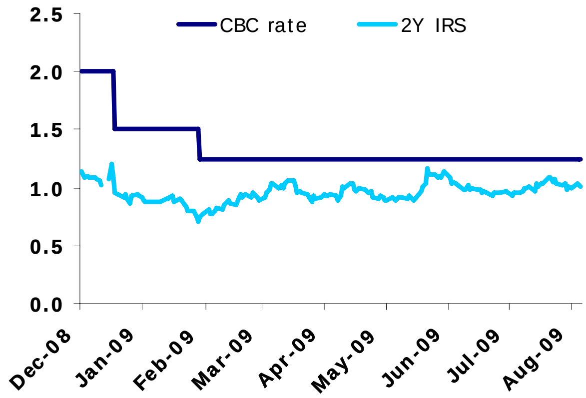
USD-TWD in a holding pattern



Tidal wave of equity inflows has crested



Short-term rates going nowhere



We remain bullish on the TWD on a structural basis, but continue to highlight near-term risks, especially rich equity valuations. The prospect of CBC rate hikes remains well in the future, which should contain the advance in yields.

FX

USD-TWD remains range-bound, largely holding below the 33.0 level. Stronger-than-expected Q2 corporate earnings and Q2 GDP prints globally managed to offset the tendency for summer risk aversion as well as disappointment associated with delays on the investment MOU with Mainland China. Meanwhile, the tidal wave of foreign equity inflows—sparked by the landmark agreement at the end of April allowing Chinese investment in Taiwan—has crested. Net foreign equity inflows amounted to a mere $0.2bn in Aug compared with $2.1bn in Jul.

Over the medium-term, we remain bullish on the TWD, seeing the landmark agreement between Taiwan and Mainland China as a game-changer. Moreover, Taiwan's President Ma said that the recent warming of ties with the Mainland was "just at the beginning," alluding to a fuller agreement that would cut trade restrictions. Top negotiators will meet in Dec to discuss a free trade agreement. Meanwhile, CBC activity to support exporters remains a significant obstacle to significant down-moves in USD-TWD until discretionary demand in the US and Europe recovers. Also, Taiwan stocks appear quite over-stretched, trading at a P/E ratio of 112 compared with an (un-weighted) average of 32 for AXJ and 19 for the S&P500. The sell-off in Mainland equities during Aug has only recently started to dent enthusiasm for Taiwan equities. In a world where the momentum in AXJ equities is fading and the momentum in US equities is starting to build, Taiwan stocks appear particularly vulnerable.

Rates

TWD local rates are expected to exhibit a neutral-to-higher bias, while the curve should remain broadly range-bound over the remainder of H2. Our calculations suggest that Taiwan's output gap is one of the largest in the region. Meanwhile, foreign demand should remain lacklustre for at least another twelve months. A much over-due correction in Taiwan stocks should also help contain the advance in yields this year.

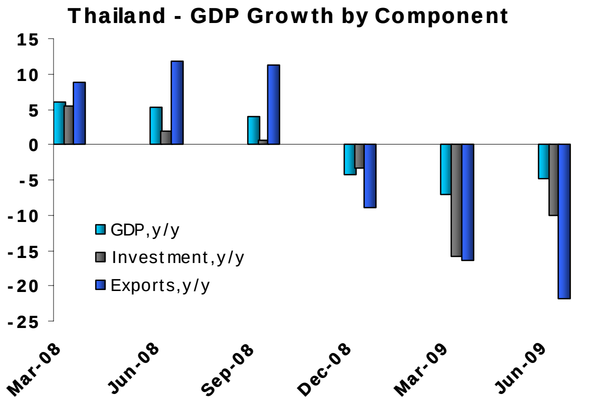
Tamara Henderson

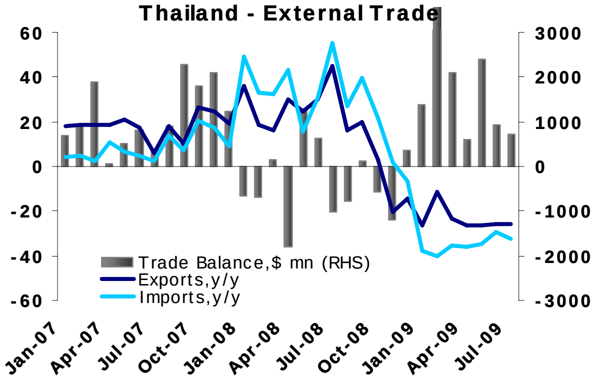
Market Forecasts – Taiwan (eop)

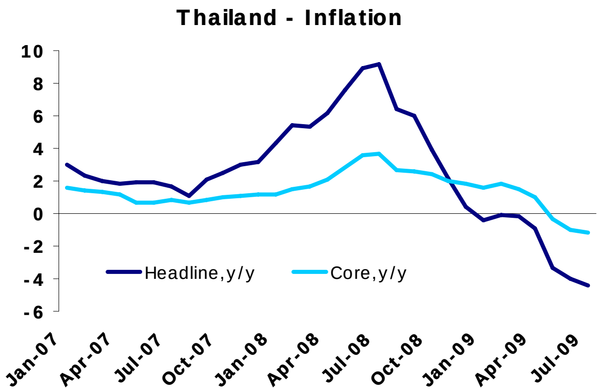
FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-TWD	32.92	0.4%	33.1	32.5	32.0	31.5	31.0	30.3
AUD-TWD	27.55	19.5%	27.1	26.0	25.6	26.1	26.0	26.1
NZD-TWD	22.61	18.9%	21.8	20.8	18.9	18.6	18.6	18.8
JPY-TWD	0.350	-3.4%	0.338	0.325	0.305	0.292	0.282	0.271
EUR-TWD	47.06	2.6%	47.0	44.9	44.2	44.1	43.4	43.0
Rates	**Current**	**Ytd (bps)**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
CBC's discount rate	1.25	-75	1.25	1.25	1.25	1.25	1.50	1.75
3-month CP	0.50	-59	0.5	0.6	0.8	1.1	1.6	2.1
2-year IRS (versus 3M CP)	1.01	-4	1.0	1.1	1.4	1.6	2.1	2.6
10-year IRS	2.04	60	2.1	2.3	2.5	2.6	2.8	3.1

Sources: Bloomberg, ANZ

Country Update: Thailand







The economy contracted by a smaller than expected 4.9% (y/y) in Q2, with exports and investment falling sharply. Economic data continue to show some signs of improvement, but conditions remain weak overall.

- GDP contracted 4.9% (y/y) in Q2, better than expected following a decline of 7.1% in Q1. Seasonally adjusted, the economy expanded by 2.3% in the quarter from -1.9% in Q1. Government consumption rose 5.9% in Q2, driven by the fiscal stimulus package, while exports and investment remained weak, falling 21.8% and 10.1%, respectively.
- Domestic demand remains weak. Car sales fell 3.4% (y/y) in Jul after registering a drop of 13.4% in Jun, the fourteenth consecutive month of decline.
- The consumer confidence index rose for the second straight month from 65.4 in Jun to 66.3 in Jul. The score was still well below the neutral level of 100. Participants remain concerned about political uncertainties, swine flu, and the pace of global recovery.
- The manufacturing production index grew 3.2% (m/m, sa) in Jun, but continued to contract by 7.8% on an annual basis. Industrial capacity utilisation dropped marginally to 60.4 in Jun after recovering to 60.6 in May.
- Exports fell 25.7% (y/y) in Jul, broadly unchanged from Jun's -25.9%. Imports contracted by 32.5% in Jul against a 23.9% decline a month earlier. The trade surplus shrunk to $706mn in Jul from $937mn in Jun.
- Headline inflation fell for the seventh straight month to a record -4.4% (y/y) in Jul from -4.0% in Jun. The sharp decline in consumer prices was mainly due to base effects. Core CPI fell by 1.2% in Jul, below Jun's 1.0%.
- The Thai government approved a THB1.1tn investment plan for the next three years, down from the initial THB1.5tn. The funds are to be used in infrastructure development and social welfare measures.
- Given weak external demand, we see the recovery as being some way off. We expect year-on-year GDP growth to turn positive in Q4; for the whole year, the economy is expected to contract by 3-4%, with the risks on the downside as the political turmoil may intensify in the following months.

Zhou Hao/Yansen Poaler

Economic Data – Thailand

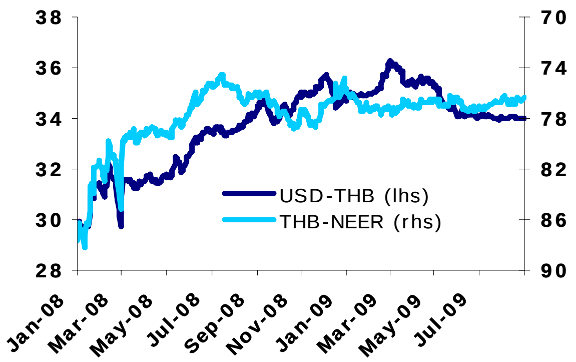
Monthly data	**Dec-08**	**Jan-09**	**Feb-09**	**Mar-09**	**Apr-09**	**May-**	**Jun-09**	**Jul-09**
Industrial Production, % y/y	-18.6	-21.2	-19.9	-14.5	-9.7	-9.8	-7.8	N/A
Retail Sales, % y/y	-2.7	-11.1	-7.7	-11.9	-8.7	-8.5	N/A	N/A
Consumer Price Index, % y/y	0.4	-0.4	-0.1	-0.2	-0.9	-3.3	-4.0	-4.4
Exports, % y/y	-14.6	-26.4	-11.3	-23.1	-26.1	-26.6	-25.9	-25.7
Imports, % y/y	-6.5	-37.6	-40.3	-35.1	-36.3	-34.7	-29.3	-32.5
Trade Balance, US$ bn	0.3	1.4	3.6	2.1	0.6	2.4	0.9	0.7
Foreign Exchange Reserves, USD bn	108.3	107.9	110.4	113.4	114.1	118.5	117.9	120.4
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Real GDP, % y/y	5.1	5.7	6.0	5.3	3.9	-4.2	-7.1	-4.9
-Private consumption	1.9	1.9	2.7	2.5	2.7	2.1	-2.5	-2.3
-Government consumption	8.9	9.0	-0.4	-3.7	-2.9	11.0	3.6	5.9
-Gross fixed capital formation	2.5	3.8	5.4	1.9	0.6	-3.3	-15.8	-10.1
Nominal GDP, THB bn	2,093.7	2,255.7	2,297.1	2,283.1	2,321.4	2,203.3	2,178.2	2,173.6
Current Account, US$ bn	1.7	2.2	1.0	0.7	-0.3	0.1	2.4	0.5
Capital & Financial Account, US$ bn	2.2	1.0	6.6	-4.0	2.5	-1.0	-1.3	N/A

Sources: CEIC

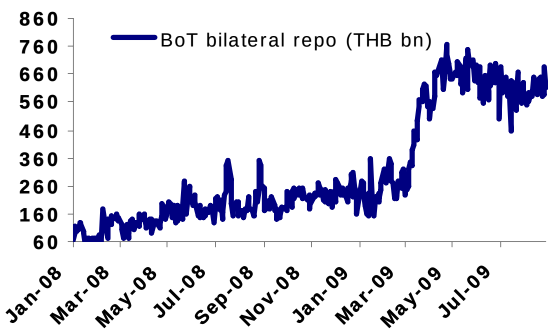
Thailand: FX and Rates Strategy

USD-THB is likely to remain in familiar ranges over the near-term. We expect the recent relaxation of capital outflow restrictions to have limited impact on the baht. The rebound in Q2 growth did not alter the BoT's policy assessment. We continue to expect a rate hike in Q3 2010.

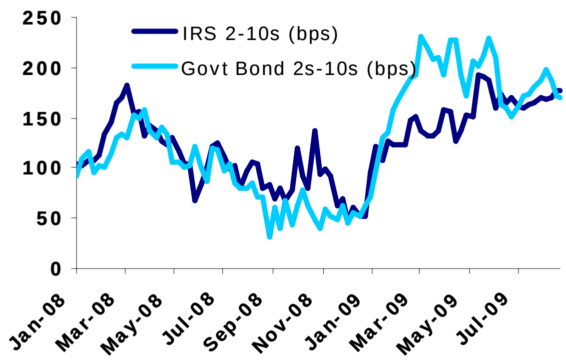
THB and NEER trading in tight range



Interbank liquidity remains high



GOV curve to settle in range-trade



FX

USD-THB extended its holding pattern around the 34.0 level in Aug. The sustained rise in BoT's FX reserves and forward positions indicates an ongoing effort to keep the exchange rate stable. The relaxation of capital outflow measures also hints at the authorities' preference for a weaker baht. Under the new rules announced in early-Aug, large local companies will be allowed to invest directly in foreign securities subject to a $50mn cap. However, the move is not expected to have a significant effect on portfolio outflows. Domestic investors are already allowed to invest in foreign assets through locally registered funds, with only $8.1bn reportedly held in these accounts. USD-THB movements are likely to be confined to a narrow range of 34.0-34.5, but the bias is for a moderately stronger baht into 2010.

Rates

The BoT left the policy rate unchanged at 1.25% on 26 Aug, as was widely expected. While the rebound in Q2 GDP eased tail risk of a 4.5% decline in full year growth, the 2.3% q/q GDP print appears to have done little to alter the BoT's policy stance. The Monetary Policy Committee noted the recent improvement in domestic conditions, but said that a "high degree of uncertainty" over the sustainability of the global recovery continues to pose downside risks to growth. Meanwhile, anti-government protests are regaining pace after a lull, which could threaten the nascent recovery in domestic confidence.

We expect the GOV curve to settle into a range over the near-term. While the risk is for higher fiscal spending in 2009-10, the benign core inflation outlook lends credibility to the BoT's stand pat stance. We continue to expect the BoT to remain on hold until Q3 2010. Retail investors' warm reception to the savings bond issuance in Jul (the next tranche is in early-Sep) and excess banking liquidity conditions should also limit upside risks on bond yields.

Yeo Han Sia

Market Forecasts – Thailand (eop)

FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-THB	34.01	-2.1%	34.0	34.0	34.0	34.0	33.5	33.5
AUD-THB	28.67	17.5%	27.9	27.2	27.2	28.2	28.1	28.8
NZD-THB	23.30	15.8%	22.4	21.8	20.1	20.1	20.1	20.8
JPY-THB	0.35	-3.1%	0.347	0.340	0.324	0.315	0.305	0.299
EUR-THB	47.23	3.0%	48.3	46.9	46.9	47.6	46.9	47.6
Rates	**Current**	**Ytd (bps)**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
BOT's 1-day repo rate	1.25	-150	1.25	1.25	1.25	1.25	1.50	1.50
3-month BIBOR	1.36	-159	1.4	1.4	1.4	1.4	1.7	1.7
2-year IRS (versus 6M THB fix)	2.49	64	2.6	2.6	2.6	2.6	2.9	3.1
10-year IRS	4.27	190	4.4	4.4	4.4	4.4	4.5	4.6

Sources: Bloomberg, ANZ

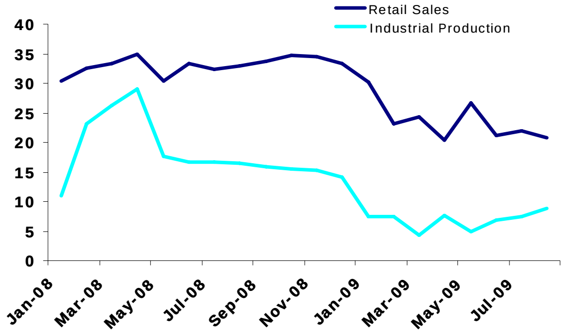
Country Update: Vietnam

The recovery continues to gain traction. The ongoing rebound in activity is being led by domestic demand reflecting stepped-up government spending under the stimulus plan as well as the interest rate subsidy. Like elsewhere in Asia, foreign demand remains depressed. Weak external inflows look likely to constrain growth.

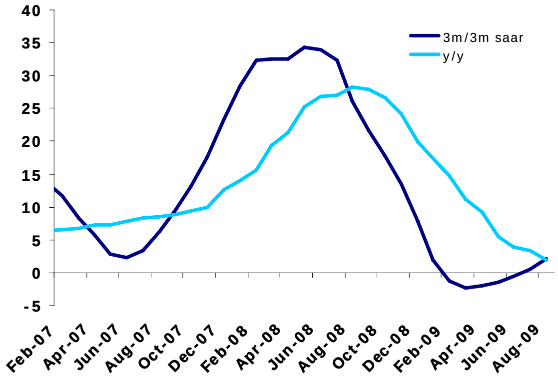
- Retail sales growth is robust and steady. Nominal sales rose 21.2% (y/y) in Aug, unchanged from the pace of Q1. Real sales are rising as inflation falls.
- Industrial production continues to improve. IP in Aug was up 10.6% (y/y) a 3ppt improvement over Jul. This is double the rate of increase registered earlier in the year. The non-state and FDI sectors are driving IP growth.
- Exports remain weak and the trade deficit is widening. Export growth improved somewhat to -18.9% (y/y) in Aug, while import growth was 5.1%, the first positive reading since Oct 2008. The monthly trade deficit rose to $1.7bn and continues to widen.
- Inflation fell again, but momentum has turned. Year-on-year inflation fell to a 7-year low of 2.0%, but trend inflation has bottomed and is now rising.
- As of end-Jul, banks have lent $22bn to businesses as part of the government's loan subsidy plan. Liquidity in the banking system increased by 20.2% as of end-Jul compared with the end of last year. Total deposits and total outstanding loans rose by 2.7% and 2.1% in Jul on a monthly basis.
- Sentiment toward Vietnam continued to improve among both domestic and foreign investors. The Domestic Investor Confidence Index rose to 112.3 in Jul from 111.9 in Jun. The Foreign Investor Confidence Index rose sharply to 137.2 in Jul compared with 101.1 in Jun.
- The State Bank of Vietnam annouced that it will keep its benchmark refinancing rate at 7.00% for a seventh consecutive month. The SBV stance is intended to bolster growth, which it forecasts at 5.0% to 5.2% for 2009.
- The weakening trade balance is a cause for concern and a possible brake on growth. With FDI commitments and disbursements down and portfolio inflows modest, the pace of Vietnam's recovery will potentially be restrained by modest levels of external financing.

Paul Gruenwald

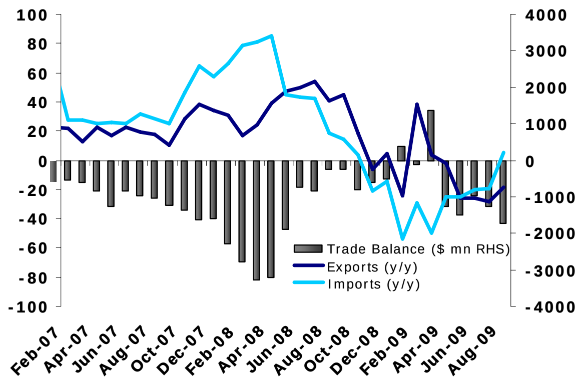
Vietnam - Domestic Demand Indicators (3mma)



Vietnam - Consumer Price Index



Vietnam - Trade Developments

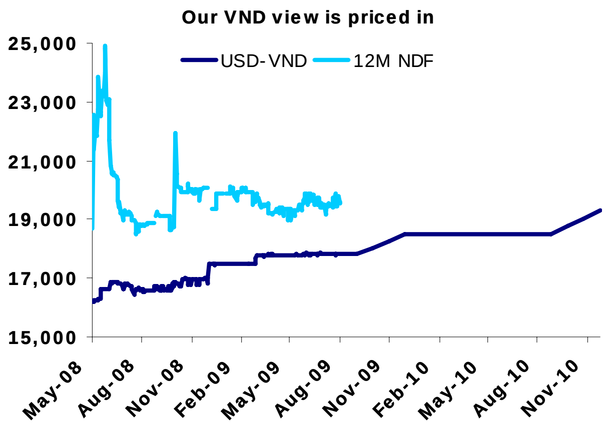


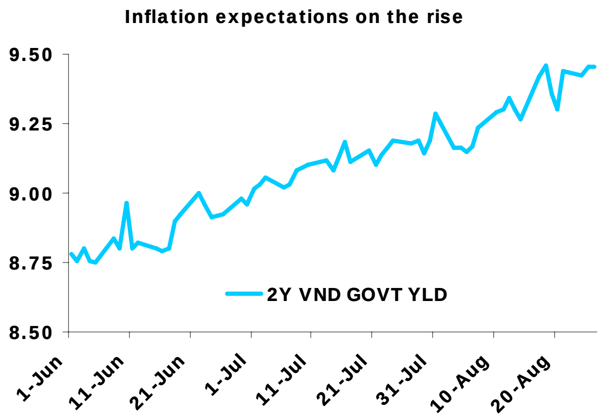
Economic Data – Vietnam

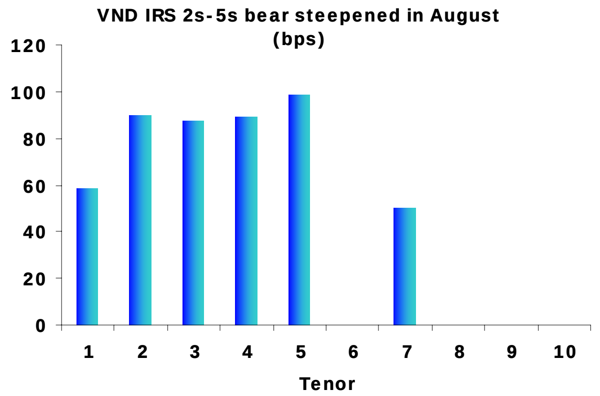
Monthly data	Jan-09	Feb-09	Mar-09	Apr-09	May-	Jun-09	Jul-09	Aug-09
Industrial Production, % y/y	-4.4	14.9	2.4	5.4	6.8	8.2	7.6	10.6
Retail Sales , % y/y	29.7	5.8	37.7	17.7	24.5	21.4	19.9	21.1
Consumer Price Index, % y/y	17.5	14.8	11.2	9.2	5.6	3.9	3.3	2.0
Exports , % y/y	-24.3	38.6	4.0	-2.2	-26.0	-26.1	-28.2	-18.9
Imports , % y/y	-53.8	-29.0	-49.5	-24.7	-24.9	-20.0	-19.3	5.1
Trade Balance, USD bn	0.4	-0.1	1.4	-1.3	-1.5	-1.0	-1.3	-1.7
Quarterly data	**Sep-07**	**Dec-07**	**Mar-08**	**Jun-08**	**Sep-08**	**Dec-08**	**Mar-09**	**Jun-09**
Real GDP, % y/y	8.2	8.4	7.5	6.5	6.5	6.2	3.1	4.5
-Agricultural, forestry, fishery	3.1	3.7	3.2	3.3	3.8	4.1	0.6	1.7
-Industry and construction	10.1	10.2	8.0	7.0	7.0	6.1	1.4	3.0
-Services	8.6	8.9	8.3	7.6	7.2	7.1	5.6	5.7
Nominal GDP, VND tn	293.8	356.5	254.1	371.7	390.8	461.2	311.1	N/A
Foreign Exchange Reserves, USD bn	22.6	23.5	26.4	22.3	23.8	23.9	N/A	N/A

Sources: CEIC

Vietnam: FX and Rates Strategy







Although reluctant thus far, we expect the authorities to sanction further weakening in the dong in support of net exports during the long wait for the normalisation in US and European discretionary demand.

FX

The authorities continue to signal their intention to keep USD-VND stable, with the SBV warning in Aug that a weakening of the dong would have an adverse impact. Indeed, a devaluation without concurrent interest rate hikes would exacerbate domestic inflationary pressures. Without an imminent improvement in global demand conditions, however, Vietnam's external position will quickly deteriorate. The trade deficit continues to widen as imports outpace exports, while FDI and net foreign equity flows remain lacklustre. The government's pro-growth bias ultimately favours a move in the currency at the expense of inflation. Meanwhile, concerns about inflation have already started to weigh on the dong, adding to an already deep-seated preference to hold USD onshore. We expect a 4% devaluation in the VND before year-end, a view which is already priced into the NDF market.

Rates

We expect VND yields to remain in an uptrend and the 1s-5s GOV spread to continue to narrow into 2010. Admittedly, the authorities have taken measures to slow credit growth and the Vietnamese stock market appears ripe for a correction—factors which should be supportive of the market over the nearer-term. Ultimately, however, we expect the management of inflation expectations to become problematic for the central bank, particularly since it has one of the weaker inflation-fighting records within AXJ.

The SBV has promised to keep policy rates unchanged until the end of the year. At the same time, inflation pressures are building and highly favourable base effects from last year's slump in global commodity prices are about to unwind. Meanwhile, the State Treasury continues to struggle to attract bidders for dong-denominated debt, having to issue USD-debt instead.

Tamara Henderson

Market Forecasts – Vietnam (eop)

FX	Current	Ytd (%)	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
USD-VND	17,820	1.9%	17,800	18,500	18,500	18,500	18,500	19,300
AUD-VND	14,913	21.4%	14,600	14,800	14,800	15,400	15,500	16,600
NZD-VND	12,240	20.9%	11,700	11,800	10,900	10,900	11,100	12,000
JPY-VND	189	-1.8%	182	185	176	171	168	172
EUR-VND	25,474	4.3%	25,300	25,500	25,500	25,900	25,900	27,400
Rates	**Current**	**Ytd (bps)**	**Sep-09**	**Dec-09**	**Mar-10**	**Jun-10**	**Sep-10**	**Dec-10**
SBV's base lending rate	7.00	-150	7.00	7.00	7.00	7.00	7.50	8.00
Overnight VNIBOR	7.38	180	7.4	8.4	9.4	10.4	11.4	11.4
1year IRS (versus 3M VNIBOR)	9.60	-88	9.6	10.6	11.6	12.6	13.6	13.6
5-year IRS	10.20	-47	10.2	10.9	11.5	12.2	12.9	12.9
1-5s IRS spread (bps)	60	83	60	27	-7	-40	-73	-73

Sources: Bloomberg, ANZ

Contacts

ANZ Economics & Markets Research

Warren Hogan	Acting Chief Economist	+61 2 9227 1562	Warren.Hogan@anz.com
Fiona Allen	Business Manager	+61 3 9273 6224	Fiona.Allen@anz.com

Australian Economics and Interest Rates Research

Warren Hogan	Head of Australian Economics and Interest Rates Research	+61 2 9227 1562	Warren.Hogan@anz.com
Tony Morriss	Senior Rates Strategist	+61 2 9226 6757	Tony.Morriss@anz.com
Julie Toth	Senior Economist	+61 3 9273 6252	Julie.Toth@anz.com
Riki Polygenis	Economist	+61 3 9273 4060	Riki.Polygenis@anz.com
Dr. Alex Joiner	Economist	+61 3 9273 6123	Alex.Joiner@anz.com
Daniel Bae	Analyst	+61 2 9227 1272	Daniel.Bae@anz.com

Global Markets Credit Research

Jason Hill	Global Markets Credit Analyst	0434 312 356	Jason.Hill@anz.com

Commodity and Industry Research

Mark Pervan	Head of Commodity and Industry Research	+61 3 9273 3716	Mark.Pervan@anz.com
Paul Deane	Rural and Regional Economist	+61 3 9273 6295	Paul.Deane@anz.com
Natalie Robertson	Commodity Research Analyst	+61 3 9273 3415	Natalie.Robertson@anz.com

Property and Financial System Research

Paul Braddick	Head of Property and Financial System Research	+61 3 9273 5987	Paul.Braddick@anz.com
Ange Montalti	Senior Economist	+61 3 9273 6288	Ange.Montalti@anz.com
Dr. Alex Joiner	Economist	+61 3 9273 6123	Alex.Joiner@anz.com
Liam Getreu	Research Assistant		

Foreign Exchange and International Economics Research

Amy Auster	Head of Foreign Exchange and International Economics Research	+61 3 9273 5417	Amy.Auster@anz.com
Katie Dean	Senior Economist	+61 3 9273 1381	Katie.Dean@anz.com
Amber Rabinov	Economist	+61 3 9273 4853	Amber.Rabinov@anz.com

Foreign Exchange and Interest Rates Research (London)

Tim Riddell	Currency and Interest Rate Strategist		Tim.Riddell@anz.com

Asian Economics Research (Singapore)

Paul Gruenwald	Chief Economist, Asia	+65 6216 1814	Paul.Gruenwald@anz.com
Tamara Henderson	Director, FX & Rates Strategy	+65 6216 1845	Tamara.Henderson@anz.com
Yeo Han Sia	Associate Director, FX and Rates Strategy	+65 6216 1968	HanSia.Yeo@anz.com
Franklin Poon	Economist, North East Asia	+852 3929 5340	Franklin.Poon@anz.com
Chang Wei Liang	Analyst, Economic Research	+65 6216 1918	WeiLiang.Chang@anz.com

New Zealand Economics Research (Wellington)

Cameron Bagrie	Chief Economist, New Zealand	+64 4 802 2212	Cameron.Bagrie@anz.com
Khoon Goh	Senior Economist	+64 4 802 2357	Khoon.Goh@anz.com
Philip Borkin	Economist	+64 4 802 2199	Philip.Borkin@anz.com
Steve Edwards	Economist	+64 4 802 2217	Steve.Edwards@anz.com
Kevin Wilson	Rural Economist	+64 4 802 2361	wilsonk1@anz.com

Research and Information Services

Karen Crothers	Head of Research and Information Services	+61 3 9273 6265	Karen.Crothers@anz.com
Marilla Rough	Senior Information Officer	+61 3 9273 6263	Marilla.Rough@anz.com
Manesha Jayasuriya	Publications Coordinator	+61 3 9273 4121	Manesha.Jayasuriya@anz.com

Important Notice

Australia and New Zealand Banking Group Limited is represented in:

AUSTRALIA by:
Australia and New Zealand Banking Group Limited ABN 11005 357 522
10th Floor 100 Queen Street, Melbourne 3000, Australia
Telephone +61 2 9226 6224 Fax +61 2 9227 5711

UNITED KINGDOM by:
Australia and New Zealand Banking Group Limited
ABN 11 005 357 522
40 Bank Street, Canary Wharf, London, E14 5EJ, United Kingdom
Telephone+ 44 20 3229 2121 Fax+44 20 7378 2378

UNITED STATES OF AMERICA by:
ANZ Securities, Inc. (Member of FINRA [www.finra.org] and SEC)
6th Floor 1177 Avenue of the Americas
New York, NY 10036, United States of America
Tel: +1 212 801 9160 Fax: +1 212 801 9163

NEW ZEALAND by:
ANZ National Bank Limited
Level 7, 1-9 Victoria Street, Wellington, New Zealand
Tel: +64 4 802 2000