

Review of the week ending 27 January 2011

Inflation result seen as allowing the RBA to cut interest rates in February. Fed indicates low rates out to end 2014

Economic data

In Australia, the December quarter CPI was unchanged for a 3.1% increase over the year. The RBA trimmed mean measure increased by 0.6% for a 2.6% increase over the year. The result is seen as allowing the RBA to cut the cash rate target at its next Board meeting on February 7.

In the US, the Federal Reserve indicated that its Federal Funds target will remain at 0-0.25% until the end of 2014. Activity data has generally been a little firmer than expected, although December quarter GDP grew by less than anticipated at 2.8%.

Rates

Australian bond yields traded higher in yield after the CPI but finished the week firmer reflecting lower US bond yields. US bond yields fell on the Federal Reserve's decision to keep the Federal Funds rate at its current level until the end of 2014 and a somewhat disappointing Q4 GDP report.

Over the week, Australian two-year yields rose 0.01% to 3.28%, while 10-year yields fell 0.01% to close at 3.81%.

Domestic bond yields are likely to open slightly lower on Monday in the wake of lower US yields in Friday's session.

US 10-year notes fell 0.13% to close at 1.89% while 2-year yields fell 0.03% to finish at 0.21%.

Credit

Credit spreads narrowed somewhat with the Australian iTraxx index closed narrower at 156 basis points.

Westpac joined other major banks in issuing a covered bond.

Other Markets

The oil price rose 1.1% to US\$99.60 per barrel. Gold rose 4.3% to US\$1,739 per oz. Commodity prices rose 1.4% to 497 as measured by the CRB commodity price index.

In FX markets, the US dollar was weaker against major currencies. The EUR/USD rose 2.2% to close at 1.322 while the GBP/USD rose 1.0% to close at 1.573. The AUD increased 1.7% to \$US1.066.

US equity markets were range bound with the S&P 500 increasing 0.1% to 1,316. The FTSE increased 0.1% to 5,733 while the ASX200 increased 1.1% to finish at 4,288.

The week ahead

The main domestic focus will be on the release of the NAB business conditions and confidence data for December. December private sector credit data will also be of some significance. Data on house prices and activity, manufacturing and services activity and trade will also be released.

Chinese manufacturing data will also be of some interest to Australian markets.

A busy data week in the US with the release of December personal income and expenditure data, the December consumption deflator, January ISM manufacturing and services data, Q4 labour cost and productivity data and January labour market data, including the ADP survey and non-farm payrolls.

The Market Data Dashboard on the next page provides an overview of changes in key market rates and prices over the week and the month. Particular focus is given to fixed income markets, but there is also some currency, commodity and equity market data. The dashboard provides start and end values for each period as well as "sparkline" charts which provide an indication of the path of changes over the period.

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BlackRock Australia Fixed Income

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Market Data Dashboard

| | | | Week | | | | | | | Month | | | | | | |
|---------------------|---------------------|------------------------|--------|-----------|----------|-------|--------|--------|-------|--------|--------|--------|-------|--------|--------|-------|
| | | | 20-Jan | 27-Jan | Move | % | Min | Max | Range | 28-Dec | 27-Jan | Move | % | Min | Max | Range |
| | | | Rates | Australia | RBA Cash | 4.25 | 4.25 | 0.00 | | 4.25 | 4.25 | 0.00 | 4.25 | 4.25 | 0.00 | |
| 12m Implied Cash* | 3.24 | 3.33 | | | 0.09 | | 3.24 | 3.33 | 0.09 | 3.22 | 3.33 | 0.11 | | 3.15 | 3.33 | 0.18 |
| 30 day BBSW | 4.41 | 4.36 | | | (0.05) | | 4.36 | 4.41 | 0.05 | 4.45 | 4.36 | (0.09) | | 4.36 | 4.50 | 0.14 |
| 90 day BBSW | 4.38 | 4.36 | | | (0.02) | | 4.35 | 4.38 | 0.03 | 4.50 | 4.36 | (0.14) | | 4.35 | 4.50 | 0.15 |
| 2Y Govt Bond | 3.27 | 3.28 | | | 0.01 | | 3.27 | 3.41 | 0.14 | 3.35 | 3.28 | (0.07) | | 3.13 | 3.41 | 0.28 |
| 10Y Govt Bond | 3.82 | 3.81 | | | (0.01) | | 3.81 | 3.99 | 0.18 | 3.77 | 3.81 | 0.04 | | 3.67 | 3.99 | 0.32 |
| 3-10 Fut. Curve | 65.0 | 62.5 | | | -2.5 | | 62.5 | 69.5 | 7.0 | 67.0 | 62.5 | -4.5 | | 62.5 | 69.5 | 7.0 |
| Aug-2020 Real Yield | 1.10 | 1.11 | | | 0.01 | | 1.10 | 1.24 | 0.14 | 1.21 | 1.11 | (0.10) | | 0.98 | 1.24 | 0.26 |
| US | Fed Funds Target | 0.25 | | 0.25 | 0.00 | | 0.25 | 0.25 | 0.00 | 0.25 | 0.25 | 0.00 | | 0.25 | 0.25 | 0.00 |
| | 12m Implied Target* | 0.30 | | 0.28 | (0.02) | | 0.27 | 0.39 | 0.12 | 0.34 | 0.28 | (0.06) | | 0.23 | 0.39 | 0.16 |
| | 2Y Treasury | 0.24 | | 0.21 | (0.03) | | 0.21 | 0.24 | 0.03 | 0.27 | 0.21 | (0.06) | | 0.21 | 0.27 | 0.06 |
| | 10Y Treasury | 2.02 | | 1.89 | (0.13) | | 1.89 | 2.06 | 0.17 | 1.92 | 1.89 | (0.03) | | 1.86 | 2.06 | 0.20 |
| | 2-10 Curve | 178 | | 168 | (10) | | 168 | 183 | 15 | 165 | 168 | 3 | | 163 | 183 | 19 |
| | 10Y Real Yield | (0.02) | | (0.22) | (0.20) | | (0.22) | (0.01) | 0.21 | (0.12) | (0.22) | (0.10) | | (0.23) | (0.01) | 0.22 |
| Aus/US | 2Y Spread | 303 | | 307 | 4 | | 306 | 319 | 13 | 309 | 307 | (2) | | 292 | 314 | 22 |
| | 10Y Spread | 180 | 192 | 12 | | 192 | 201 | 9 | 185 | 192 | 7 | | 181 | 193 | 12 | |
| UK | BoE Bank Rate | 0.50 | 0.50 | 0.00 | | 0.50 | 0.50 | 0.00 | 0.50 | 0.50 | 0.00 | | 0.50 | 0.50 | 0.00 | |
| Euro | ECB Refi Rate | 1.00 | 1.00 | 0.00 | | 1.00 | 1.00 | 0.00 | 1.00 | 1.00 | 0.00 | | 1.00 | 1.00 | 0.00 | |
| Credit | Australia | Aus iTraxx | 169 | 156 | (13) | | 156 | 169 | 13 | 183 | 156 | (27) | | 156 | 185 | 29 |
| | | AA 5Y vs Bond | 192 | 198 | 6 | | 191 | 200 | (10) | 179 | 198 | 19 | | 179 | 200 | (22) |
| | | BBB 5Y vs Bond | 360 | 376 | 17 | | 360 | 376 | (17) | 351 | 376 | 26 | | 340 | 376 | (36) |
| | US | CDX Inv. Grade | 108 | 101 | (7) | | 101 | 108 | 7 | 121 | 101 | (20) | | 101 | 122 | 21 |
| | | CDX High Yield | 602 | 562 | (40) | | 561 | 602 | 41 | 682 | 562 | (120) | | 561 | 689 | 127 |
| | Euro | Euro iTraxx | 154 | 141 | (13) | | 141 | 154 | 13 | 174 | 141 | (33) | | 141 | 180 | 39 |
| Currencies | AUD/USD | 1.048 | 1.066 | 0.017 | 1.7% | 1.048 | 1.066 | 0.017 | 1.009 | 1.066 | 0.056 | 5.6% | 1.009 | 1.066 | 0.056 | |
| | EUR/USD | 1.293 | 1.322 | 0.029 | 2.2% | 1.293 | 1.322 | 0.029 | 1.294 | 1.322 | 0.028 | 2.2% | 1.267 | 1.322 | 0.055 | |
| | GBP/USD | 1.558 | 1.573 | 0.015 | 1.0% | 1.557 | 1.573 | 0.016 | 1.546 | 1.573 | 0.027 | 1.7% | 1.532 | 1.573 | 0.041 | |
| | USD/JPY | 77.0 | 76.7 | -0.3 | -0.4% | 76.7 | 77.8 | 1.1 | 77.9 | 76.7 | -1.2 | -1.6% | 76.7 | 77.9 | 1.2 | |
| | AUD/JPY | 80.7 | 81.7 | 1.0 | 1.2% | 80.7 | 82.4 | 1.7 | 78.7 | 81.7 | 3.1 | 3.9% | 78.4 | 82.4 | 4.0 | |
| Comds | Oil | WTI Crude | 98.5 | 99.6 | 1.1 | 1.1% | 98.5 | 99.7 | 1.2 | 99.4 | 99.6 | 0.2 | 0.2% | 98.5 | 103.2 | 4.8 |
| | Gold | US\$ | 1,667 | 1,739 | 72 | 4.3% | 1,665 | 1,739 | 74 | 1,557 | 1,739 | 182 | 11.7% | 1,546 | 1,739 | 193 |
| | All | CRB Index | 490 | 497 | 7 | 1.4% | 490 | 497 | 7 | 480 | 497 | 17 | 3.5% | 480 | 497 | 17 |
| Equities | Australia | ASX200 Price Index | 4,240 | 4,288 | 49 | 1.1% | 4,224 | 4,288 | 64 | 4,089 | 4,288 | 200 | 4.9% | 4,057 | 4,288 | 232 |
| | US | S&P500 Price Index | 1,315 | 1,316 | 1 | 0.1% | 1,315 | 1,326 | 11 | 1,250 | 1,316 | 67 | 5.3% | 1,250 | 1,326 | 76 |
| | Japan | Nikkei 225 Price Index | 8,766 | 8,841 | 75 | 0.9% | 8,766 | 8,884 | 118 | 8,424 | 8,841 | 418 | 5.0% | 8,378 | 8,884 | 505 |
| | UK | FTSE 100 Price Index | 5,729 | 5,733 | 5 | 0.1% | 5,723 | 5,795 | 72 | 5,507 | 5,733 | 226 | 4.1% | 5,507 | 5,795 | 288 |

*CSFB

Australia Fixed Income