

- ❖ The US Federal Reserve appears to be moving closer to tapering, minutes of its policy committee meeting on October 29-30 suggested.
- ❖ The central bank said that it might reduce its USD85 billion in monthly bond purchases “in coming months” if economic data were consistent with its view of an improving labour market. Committee members also discussed extensively on ways to reduce asset purchases without triggering a rise in interest rates. These included ways to enhance forward guidance including cutting the interest paid to banks on excess reserves and lowering the unemployment threshold on when to consider raising interest rates.
- ❖ Policymakers will hold their next meeting on December 17-18, but most market participants expect no change in policy until the March gathering as the Janet Yellen will assume the Fed chairmanship in February 2014. The US central bank is not expected to raise interest rates until mid-2015 at the earliest.
- ❖ Across the Atlantic, the European Central Bank has cut interest rates to a new record low of 0.25% in early November, but inflation in the Eurozone is still well below the central banks’ target. It seems, therefore, that the ECB has also been discussing strategies to signal its intention of keeping interest rates at low levels for a sustained period. There has been rumours that the ECB is considering making banks pay to deposit cash with it overnight, that is, negative interest rates. While there does not seem to be much support for such a move, ECB President Mario Draghi said in early November that the central bank was in fact “technically ready” for negative rates, if warranted by the economy.

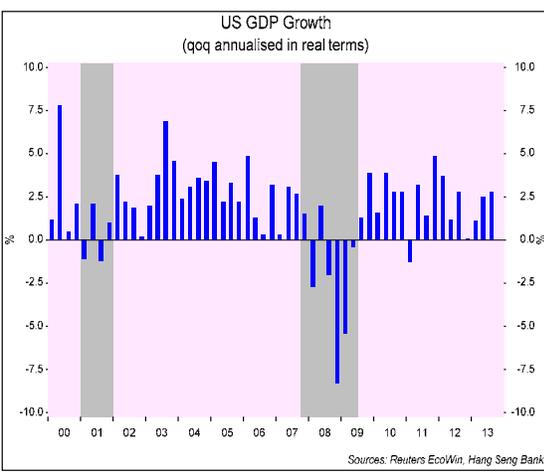
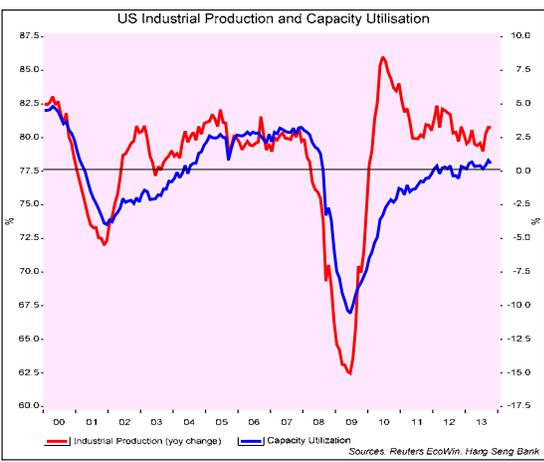
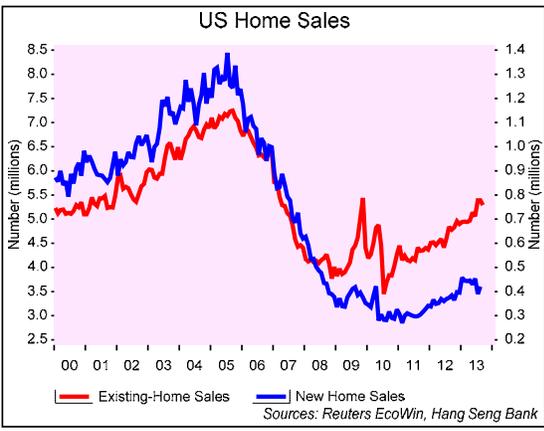
	2013Q2	2013Q3	2013Q4F	2014Q1F	2014Q2F
US Fed Funds Target Rate	0 - 0.25	0 - 0.25	0 - 0.25	0 - 0.25	0 - 0.25
Japanese Target Rate	0 - 0.10	0 - 0.10	0 - 0.10	0 - 0.10	0 - 0.10
Euro Refinancing Rate	0.50	0.50	0.25	0.25	0.25
British Repo Rate	0.50	0.50	0.50	0.50	0.50
Australian Cash Rate	3.00	2.75	2.50	2.50	2.50
Canadian Bank Rate	1.00	1.00	1.00	1.00	1.00
China One-year Lending Rate	6.00	6.00	6.00	6.00	6.00

Notes: End of period figures; F denotes forecast
Sources: Central Bank Data, Bloomberg L.P., Reuters, Hang Seng Bank



US Economy

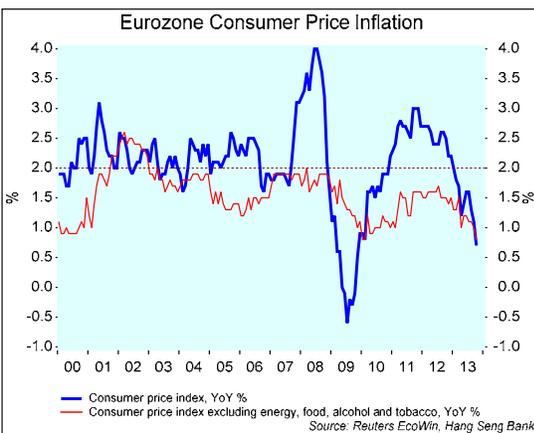
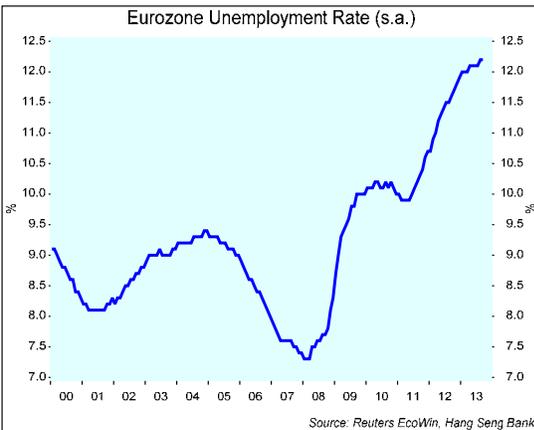
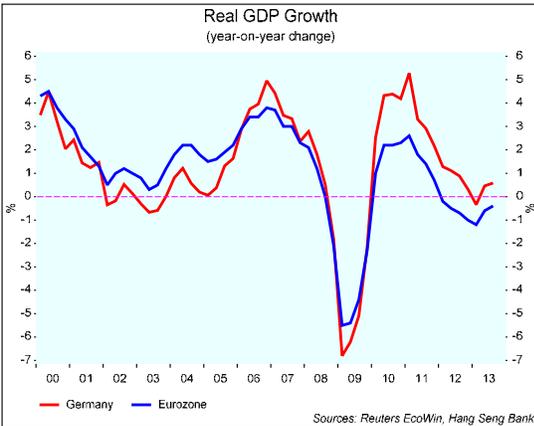
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- ❖ The US economy shows obvious signs of slowing in the final quarter as the housing recovery loses momentum. The partial government shutdown in October also played a role as it undermined consumer and investor sentiment to some extent.
- ❖ Transactions in the housing market, the main engine for growth in recent quarters, have been falling as higher prices and mortgage rates curbed demand. The number of Americans signed contracts to buy previously-owned homes fell for a fourth consecutive month in September, to its lowest level this year. This so-called pending home sales index is a leading indicator as it tracks purchase contracts. At the same time, confidence among homebuilders, as reflected by the National Association of Home Builders/Wells Fargo builder index, also remained at a four-month low of 54 in November.
- ❖ The outlook is, however, not all negative as the job market is holding up relatively well. US employers added 204,000 workers in October and the number for September was revised upwards. If job growth persists at the current pace of about 200,000 a month, the unemployment rate would continue to decline and the number of jobs could return to pre-crisis levels in about a year's time.
- ❖ Factory production also picked up mildly in October, rising 0.3% compared with the previous month. The increase mainly reflected more output of furniture, metal and electronics.
- ❖ US consumers did not seem to be affected by the partial government shutdown. Retail sales rose 0.4% in October, the most in three months, as consumers snapped up big-ticket items such as cars and furniture, clothing and electronic products. Retail sales excluding cars, gasoline and building materials, the so-called core retail sales, increased 0.5%, after advancing 0.3% in September.
- ❖ US inflation remained tame, with the consumer price index falling 0.1% in October, after rising 0.2% in the previous month. In the 12 months through October, the CPI increased only 1%, the smallest gain since October 2009.

Euro Zone Economy

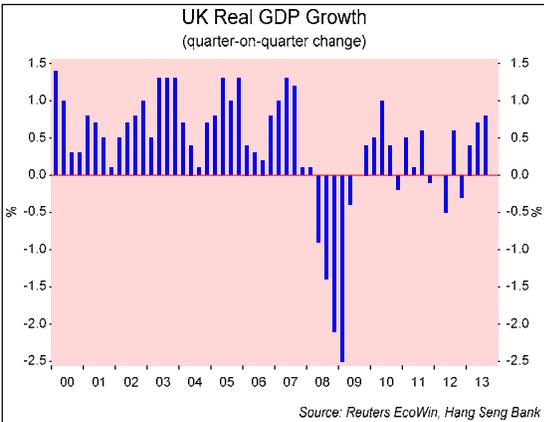
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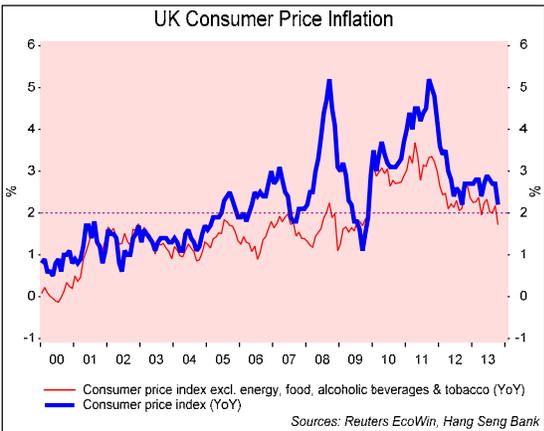
- ❖ The Eurozone's economy continued to expand in the third quarter after emerging from an 18-month recession, the longest since its creation in 1999, in the three months to June, in line with recent data showing growing confidence among businesses and consumers and continued expansion in manufacturing activity.
- ❖ The rate of growth, however, was only 0.1%, down from 0.3% in the second quarter and falling short of earlier expectations that the 17-country region's economic recovery should gather pace in the second half of the year. In particular, the currency bloc's second and third largest economies, France and Italy, both shrank in the three-month period, although two bailout countries, Portugal and Spain, saw growth again.
- ❖ Eurozone unemployment rate stayed at a record high of 12.2% in September, highlighting the fact that the recovery has yet to feed through to the real economy. In Spain and Greece, more than one in four is out of work. Heightened concerns about jobs and income should therefore continue to weigh on consumer spending and economic growth for some time.
- ❖ Slowing inflation provides further evidence that the underlying economy remains weak. Consumer price annual inflation fell to 0.7% in October, the lowest since November 2009. Stripping out volatile energy, food, alcohol and tobacco prices, core inflation also dropped, from 1.0% to 0.8%. Both measures undershot the European Central Bank's target of "close to, but below, 2%" by a wide margin.
- ❖ Highly indebted countries such as Greece and Ireland are experiencing price declines, going through the process of price adjustments to regain economic competitiveness. This suggests that in these countries, and hence for the whole eurozone, inflation is likely to remain low going forward. In response to such fears of a protracted period of disinflation, the ECB lowered its main policy rate from 0.50% to 0.25% after its November meeting. Mario Draghi, its chief, said that the ECB could do more if inflation falls further.

UK Economy

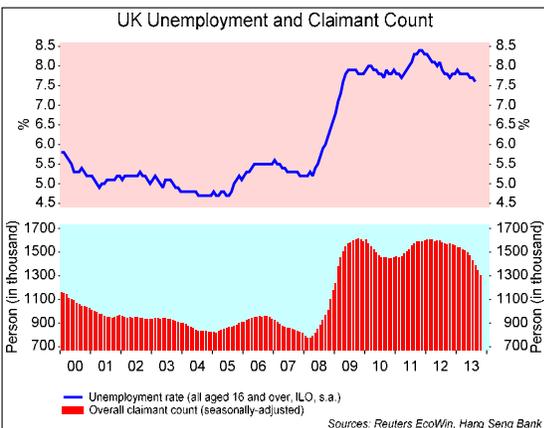
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- ❖ UK gross domestic product expanded 0.8% in the third quarter after a 0.7% rise in the previous three months. The pace of growth was 0.1% above the Bank of England's forecast and also the highest in more than three years. If it continues, the annual growth rate might then rise above 3% next year, close to its average levels over the decade prior to the 2008 global financial crisis.



- ❖ With faster economic growth, the Bank of England acknowledged in its latest inflation report that the recovery had finally taken hold. It now sees the near-term economic outlook a little stronger than in August, expecting the British economy to grow by 2.9% for 2014 and 2.5% for 2015, up from 2.4% for both years previously, and to surpass its pre-crisis peak around the first half of next year.



- ❖ Consumer price inflation fell to 2.2% in October from 2.7% in September as contribution from university tuition fees was smaller than expected. Excluding energy, food, alcohol and tobacco, the underlying inflation was even lower, at 1.7%. The BOE believes that the recent strength of sterling should help keep price pressures contained going forward and inflation will be around 2.2% next year, instead of the earlier estimate of 2.5%.

- ❖ Perhaps more importantly, unemployment will fall at a faster pace with stronger recovery and lower inflation. The Bank of England judges that there is now a "two in five" chance that the jobless rate will reach 7% in the fourth quarter of 2014. Back in August, it thought that unemployment would more likely than not remain above 7% until mid-2016.

- ❖ The BOE offered explicit guidance in August, saying that it would maintain its policy rate at a record low of 0.5% until the unemployment rate falls to the 7% threshold in hope that the commitment would help sustain the economic recovery. Now with its latest forecast, many are speculating that the Bank will raise rates early. The release of the minutes of the Bank's last meeting, however, just showed that officials were in no rush to doing so as they projected inflation to remain close to 2% even they held rates constant throughout the forecast period.



Key Economic Forecast

(Percent)	US			Euro Zone			UK		
	2012	2013F	2014F	2012	2013F	2014F	2012	2013F	2014F
Real GDP	2.8	1.8	2.6	-0.6	-0.5	1.0	0.2	1.3	2.0
CPI Inflation Rate	2.1	1.5	2.0	2.5	1.5	1.6	2.8	2.7	2.3
Unemployment Rate	8.1	7.5	7.0	11.4	12.2	12.2	8.0	7.8	7.6
Official Rate #	0-0.25	0-0.25	0-0.25	0.75	0.50	0.50	0.50	0.50	0.50
10-Year Bond Yield #	1.76	2.90	3.50	1.32	1.90	3.00	1.83	2.80	3.30

Notes: # End-of-period figures; F denotes forecast

US Dollar Exchange Rate

	June 2013	Jul 2013	Aug 2013	Sep 2013	Oct 2013
EUR/USD	1.3010	1.3302	1.3222	1.3527	1.3583
USD/JPY	99.14	97.88	98.18	98.25	98.36
GBP/USD	1.5212	1.5208	1.5504	1.6186	1.6038
AUD/USD	0.9138	0.8982	0.8900	0.9317	0.9458
NZD/USD	0.7740	0.7984	0.7727	0.8299	0.8262
USD/CAD	1.0520	1.0277	1.0537	1.0309	1.0431
USD/CNY(PBOC mid-rate)	6.1787	6.1788	6.1709	6.1480	6.1425

Notes: End-of-period figures

Interest Rate Forecast

	2013Q2	2013Q3	2013Q4F	2014Q1F	2014Q2F
US Fed Funds Target Rate	0 - 0.25	0 - 0.25	0 - 0.25	0 - 0.25	0 - 0.25
Japanese Target Rate	0 - 0.10	0 - 0.10	0 - 0.10	0 - 0.10	0 - 0.10
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