CONCERNS EXPRESSED OVER THE SIZE OF UK PUBLIC BORROWING
During the week, the International Monetary Fund warned that Britain’s public finances were deteriorating at the fastest pace in the Group of 20 countries. According to one estimate, in the two years 2009-10 and 2010-11 the government will have to raise £350bn. As a share of national income, public borrowing is expected to rise from 2.6% in 2007-08 to 12.6% in 2009-10 as tax revenues plummet. For his part, Governor of the Bank of England Mervyn King warned that the government could not afford a second fiscal stimulus in next month’s Budget. Concerns over the size of UK public spending were echoed by the European Commission which gave Britain until 2013-14 to bring the budget deficit back below 3% of national income. Meanwhile, data showed that in the three months to the end of February, public money funded almost half of new home building. Separately, a rise in the CPI from 3% in January to 3.2% in the year to February forced Governor Mervyn King to write to Chancellor Alistair Darling to explain why prices were still rising more than 1% above the Bank’s 2% target. Mr King explained that the rise in inflation reflected retailers’ decisions to pass on consumer the effect of higher import prices (a result of Sterling’s depreciation relative to the Dollar and the Euro since the summer of 2007). Meanwhile, official figures showed that retail sales volumes fell by 1.9% on the month in February, a much sharper decline than had been expected. Compared to the same month last year, sales grew by 0.4%, the lowest pace since 1995 and much lower than the 3.8% growth rate in January. The CBI employers’ group distributive trades’ survey showed that in the early weeks of March retailers reported further falls in sales and said they did not expect any improvement next month. The dismal retail statistics bring to an end a run of data that has shown sales holding up relatively well over Christmas amid heavy discounting.

GERMAN ECONOMIC DATA MIXED
The outlook for the German economy was downgraded this week. Germany’s government, which previously predicted that Europe’s largest economy would contract this year by more than 2.25%, is expected to release a fresh forecast showing that the economy will shrink by up to 4.5%. Commerzbank said that it expects demand for German exports to collapse and the German lender revised its outlook for the country’s economy to a 7% decline, double its previously-forecast decline. Two economic institutes also revised their forecasts. Meanwhile, the Ifo institute reported that its German business climate index dropped to 82.1 in March, the lowest since the survey began in 1991. On a positive note, a component that measures expectations about prospects for the next six months rose for a third consecutive month. Germany’s GfK research institute said that its consumer confidence index, which has held steady in recent months, fell in April. In France, the Insee statistics office reported that French consumer confidence was stable in March, albeit at a low level. Separate figures showed that manufacturers’ confidence held at the lowest level since data began in June 1962. The number of unemployed in France rose 3.5% month-on-month in February. Meanwhile, an Italian business-confidence index declined more than had been expected to 59.8 in March, the lowest since the series started in 1986. In Ireland, 4Q08 GDP contracted by 7.5% from the same period a year ago. Several European central banks announced monetary easing during the week. In Norway, the Krone fell against the Euro after the central bank, the Norges Bank cut the nation’s benchmark deposit rate by 0.5% to 2% and predicted that additional rate cuts were imminent. Poland’s central bank, the Narodowy Bank Polski cut its benchmark rate to a record low of 3.75%. Meanwhile, the Czech Koruna depreciated against the Dollar when the country’s government collapsed after losing a vote of confidence over its handling of the economic crisis. A 101-96 vote marked the end of the coalition government of Mirek Topolanek, the centre-right Prime Minister. In other news, an International Monetary Fund-led financing package of €20bn ($27.1bn) was offered to Romania to help steer the country through the economic crisis. International financial institutions will extend to Serbia around €3bn in standby credit for just over two years. The €3bn package replaces a more modest $520m on standby loan that the IMF agreed to in January.

US REVISES FINANCIAL RESCUE PROGRAMME
This week saw the US Treasury announce the latest steps in its financial rescue programme to help spur US growth. It said that it will finance as much as $1 trillion in purchases of distressed assets. The Treasury’s Public-Private Investment Program will use $75 billion to $100 billion from the $700 billion Troubled Asset Relief Program enacted last year, giving the government “purchasing power” of $500 billion. The Treasury said the program may double “over time.” In a separate statement, US Treasury secretary Tim Geithner set out plans for more stringent scrutiny of the financial services sector, capturing hedge funds and derivatives in a new regulatory regime and demanding institutions build up a bigger layer of capital. The S&P 500 Index jumped 7.1%, its steepest gain since October. Prices of Treasury 10-year notes fell, driving yields higher as the US government prepared to sell $98 billion of two, five and seven-year notes. Meanwhile, updated Commerce Department data showed that US GDP contracted at an annualised rate of 6.3% in the fourth quarter of last year, 0.1% worse than last month’s estimate. The revision was due to a draw-down of inventories and a slowing of construction and exported services. A weakened US economy pulled corporate profits down by 16.5%, or $250.3bn, in the fourth quarter of 2008 from the third quarter, the biggest drop since 1953. By contrast, durable-goods orders in February increased by 3.4%. The increase in demand for longer-lasting products was the biggest gain in more than a year and the first in seven months.

JAPAN’S EXPORTS HALVE AS TRADE SURPLUS DIMINISHES
Deepening recessions in Japan’s key markets were reflected in the trade figures of the world’s second largest economy this week. Exports in February fell 49.4% year-on-year, their worst performance since 1980. Japan recorded a slim trade surplus of ¥82.4bn ($844m), achieved primarily because of a record 43% drop in imports. The fall in imports highlighted the nation’s fast diminishing appetite for raw materials and weakening domestic consumer demand. Prime Minister Taro Aso ordered officials to...
draw up a fiscal stimulus package for enactment early in the fiscal year (which starts in April.) The package is expected to be twice as large as the ¥10 trillion ($104 bn) already pledged. Meanwhile, a joint survey by the Cabinet Office and Finance Ministry showed that sentiment among Japan’s manufacturers fell to minus 66 points this quarter compared with minus 44.5 three months earlier (a negative number means pessimists outnumber optimists.) The drop was the biggest since the report began in 2004. Other statistics showed a softening of commercial land prices in the country’s three biggest metropolitan areas in 2008 – prices declined 6.1% in Tokyo, 5.9% in Nagoya and 3.3% in Osaka. A separate Bank of Japan survey showed that corporate services prices fell 2.6% in February from a year earlier, the fifth consecutive monthly decline.

CHINA CALLS FOR NEW GLOBAL CURRENCY

During the week China’s central bank, the People’s Bank of China proposed replacing the US dollar as the international reserve currency with a new global system controlled by the International Monetary Fund. To replace the current system, central bank Governor Zhou Xiaochuan suggested expanding the role of special drawing rights (SDR), which were introduced by the IMF in 1969. The value of SDRs is based on a basket of four currencies – the US Dollar, Yen, Euro and Sterling – and they are used largely as a unit of account by the IMF and some other international organisations. China’s proposal would expand the basket of currencies forming the basis of SDR valuation to all major economies and set up a settlement system between SDRs and other currencies so they could be used in international trade and financial transactions. Analysts said the proposal was an indication of Beijing’s fears that actions being taken to save the US economy could lead to a devalued Dollar, which may have a negative impact on China. China holds the bulk of its $2,000bn of foreign exchange reserves in Dollars. In a separate statement, Russia’s First Deputy Foreign Minister Andrei Denisov added to calls for currency reform, requesting an international conference at government envoy level to discuss the creation of a new global currency.

CORPORATE NEWS

This week Rio Tinto’s Chief Financial Officer Guy Elliott outlined an alternate strategy to raise capital in the event that Chinalco’s planned $19.5bn investment in the Anglo-Australian miner does not proceed. The executive said that the Anglo-Australian group would consider a rights issue, sale of bonds, additional asset sales and debt rescheduling if the deal with the Chinese aluminium group was not cleared by shareholders or regulators. Rio must repay debts of more than $18bn by the end of 2010, including $8.9bn this October. Chinalco’s investment in Rio includes $12.3bn for minority stakes in a range of Rio’s mining assets and a $7.2bn convertible bond that could boost the Chinese group’s equity stake in the mining group to 18%. Chinalco is also seeking two seats on Rio’s board. The Chinalco deal could provide Rio with better access to China and funding from the Chinese government to develop projects in the country. Separately, Industrial and Commercial Bank of China (ICBC), the world’s largest financial institution by market capitalisation, reported a 35.2% rise in full-year net profit to Rmb111bn ($16.2bn). ICBC secured a promise from Goldman Sachs that the US bank would hold the majority of its stake in the Chinese lender for at least another year. Goldman, which holds 4.9% of the Chinese lender, some on behalf of investors, said that it would sell no more than 20% of that stake before April next year, even though the lock-up for its shares ends in April and October this year.