

JVB Financial Group, LLC

CRONIN'S CORNER MONTHLY

A Perspective on the International Economy

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by Keith Cronin, JVB Senior Vice President of Sovereign Debt Trading

The world's smallest continent is also the world's largest island. The history books remember this country as 'New Holland' as the name was first adapted by Dutch seafarers in the 1600's. At the beginning of the nineteenth century the country was renamed and we know it today as Australia. The southern hemisphere imbues its northern brethren with a sense of mystery, a reversal of nature's paradigm and an impossibility of distance. It was this distance that inspired it as a destination for penal transportation as memorialized by countless ballads over the lamentable purpose of places like 'Botany Bay'. It was perhaps this geographic distance also that helped to keep Australia's global financial and economic influence nestled between the Indian and Pacific oceans. Now however, its eucalyptus of commerce is blooming from the pruned flora of economic weeds.

The Australian economy has, as we have noted previously, been broadly spared the horrors of the global recession of the past year. We have seen global unemployment surge whilst the joblessness rate down under has nudged up a paltry one and a half percent in the past twelve months. Whilst housing prices indiscriminately fell across continents, Australian house prices fell just over one percent year on year in the second quarter of 2009. Technically, Australia avoided a recession as the country only experienced one quarter of economic contraction last year. In the first quarter of this year Oz saw GDP rise by 0.4 percent and by 0.6 percent in the second quarter. It's apparent that Australia is definitely the exception amongst global developed economies. As a testament to this recessionary obtuseness the Central Bank of Australia (CBA) became the first G20 country to implement its policy tightening agenda in October. A quarter point hike to 3.25 percent had a definitive impact on world markets and, suddenly, Australia was dictating the global financial mood. Whilst Australia doesn't have the economic muscle to inflate global economics, the rate hike helped to reassure investors that a global recovery had found a realistically plausible base. Interest rates are now about four percentage points below their peak in early 2008 following another rate increase in November and at this stage it seems that further monetary tightening is imminent. This monetary tightening though is unlikely to reproduce itself in more powerful economies like the US and Europe in the

immediate future as their health remains rather more fragile as 2010 approaches thereby accentuating Australia's rather special position. The country's banking system remained impressively resilient to the global fall out from the credit crisis as the banks had avoided, for the most part, any sub-prime lending. This has no doubt helped the economy navigate the economic cycle but, we feel, an even more powerful variable contributing to Australia's success is its trade relationships with Asia and of course, in particular, China.

Australia is a predominantly commodity exporting driven economy and sells everything from coal and iron to gold and wool across the global matrix of commerce. It seems then almost serendipitous that China's growth has demanded an almost insatiable demand of such products to fuel its relentless march to economic ascendancy. As a result of all of this, China has now become Australia's largest trading partner and the stimulus packages that have been applied to the Chinese economy are being spent in Australia helping push the Aussie Dollar to all time highs. Cementing these countries's future relationship perhaps is the ongoing discussion of a Free Trade Agreement between the two nations. The first round of talks commenced in 2005 and since then banter and bickering across the Indian Ocean have resulted in no resultant accord as of yet. Both parties seem to agree that a high quality trade agreement would benefit both countries and it will certainly help expand the burgeoning trade flows that already exist between the two nations. It is interesting to note, we feel, that the two countries are at different developmental stages across many platforms of their economies. Australia's apparent advantage will serve, we think, to accelerate China's move towards being a Bone Fide 'developed' economy by not only exporting commodities but also knowledge and worker specializations. Some specific points of interest could be the provisions of education perhaps to assist the Chinese further improve their financial services industry, maybe general education initiatives and even much needed input into environmental improvement projects. The breadth of the dynamic is impressive but is it impervious? Well, during the summer when an Australian was arrested for manipulating iron ore prices, a diplomatic row erupted between the two

(Continued on page 2)

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Keith Cronin is Senior Vice President of Sovereign Debt Trading at JVB Financial Group, LLC. Beginning his financial career at Oppenheimer, where he worked with equity-related financial instruments, he has also held positions at Bankers Trust, Republic National Bank and HSBC. Mr. Cronin honed his experience in the FOREX markets working in an Emerging Markets Options group, and has traded an array of international bonds denominated in various currencies, most recently with an emphasis on USD Corporate Bonds. Mr. Cronin has a Masters degree in Economics from University College Cork.



(Continued from page 1)

nations and then when in August the Chinese foreign minister cancelled a trip to Melbourne, it seemed the relationship was on the rocks. However, the Chinese have just recently signed a contract that will have Australia supply them with liquefied natural gas for the next twenty years. Taking all of this into account, the Aussie/Sino relationship seems destined to go all the way to the Altar.

although that will be below the trend line for the past ten or so years add to that increasing domestic consumer confidence a very healthy labor market and of course the Asian variable, and Australia remains a compelling model of economic distinctiveness. Time will continue to reveal as to whether the true wizard of Oz is indeed Chinese. •

Keith Cronin
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The Australian economy can't survive on the Chinese importing frenzy alone and, although a recession was avoided, the country is still obviously vulnerable to broader economic wobbles. However, the economy is forecast to grow by about two percent next year and



Graphic Source: Bloomberg 12/1/09

As demand for commodities has grown and the USD continues to remain under pressure, higher beta units like the Aussie Dollar continue to outperform.

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