

Ai GROUP ECONOMICS WEEKLY

Week in Review: 11 July – 15 July 2011

- **ABS Housing Finance** data showed that finance for owner occupied housing rose by 4.4% in May. This was the second consecutive month of growth in housing finance, with this two-month upturn reversing the majority of the decline recorded during the first three months of the year. Finance for the construction of dwellings (a lead indicator of dwelling approvals) rose by 6.4%, with solid increases also recorded in finance for the purchase of new dwellings (+4.6%) and the purchase of established dwellings (+4.1%). Despite these growth outcomes, the level of housing finance remains close to an 11-year low, consistent with a number of indicators which continue to point to subdued conditions in the housing sector.
- The **National Australia Bank Monthly Business Survey** showed that activity in the domestic economy improved slightly in June, although overall conditions remained subdued and business confidence deteriorated sharply. The overall business conditions index (a composite index of trading performance, profitability and employment) increased by 2 points to a +2.0 point index level, partly unwinding the previous month's decline. The loss of economic momentum over the first half of the year weighed on business confidence levels with the index falling by 6 points to a reading of zero index points, significantly below the average of the series (of +7.0). Confidence deteriorated across a majority of industries with the exception of mining, where confidence improved, and wholesale, where it was unchanged.
- The **Westpac-Melbourne Institute Consumer Sentiment Index** fell by 8.3% to 92.8 in July, the lowest level for the Index since May 2009. The component of the Index measuring views on the outlook for economic conditions over the next 12 months fell by 13.5% while the Index tracking the 5 year outlook was down by 10.2%. Households' assessments of their own financial position also declined with the index tracking "finances compared to a year ago" down by 2% and "finances over the next 12 months" down by 4%. One factor that was supportive of consumer sentiment was confidence in housing which picked up by 3.3%, most likely reflecting modest recent falls in house prices improving affordability. The decline in consumer confidence reflects a combination of concerns, including the European financial crisis; the ongoing impact of interest rate rises between October 2009 and November 2010; and uncertainty about introduction of a price on carbon. (The consumer sentiment survey was closed for responses the day before the government's announcement on the details of the decision to price carbon and provide an associated compensation package).
- ABS data on **Lending Finance** showed that total finance commitments (which include housing, personal, commercial and lease finance) increased by 6.1% (seasonally adjusted) in May. The strongest growth was registered in the value of commercial finance commitments (+8.7%) followed by personal finance commitments (+ 3.8) and housing finance for owner occupation (+2.2%). In contrast, the value of lease finance commitments fell by 5.7%.
- The **Housing Industry Association (HIA)-RP Data Residential Land Report** reported a fall in land sales for a sixth consecutive quarter in March 2011, signaling the prospect of weakening levels of residential construction through to at least the December quarter this year. The report found that the volume of land sales fell to a record low in early 2011 with sales down by 6% over the March quarter 2011 to be 43% lower when compared to the March 2010 quarter.

How this affects you

The strengthening in the demand for commercial finance is an early signal that businesses may be starting to expand their capital base, consistent with the upturn in investment that is projected over the next 12-18 months. However, investment outside of mining still remains subdued while the recent fall in building approvals points to on-going weakness in private sector construction investment. It is also clear that consumers remain cautious in their intentions, despite incomes growth and a robust jobs market. The degree of conservatism among consumers was underlined in the Westpac Melbourne Institute Index of Consumer Sentiment which revealed that households' assessments of their own finances is now comparable with the 2008/09 period which corresponded with the worst months of the Global Financial Crisis. The subdued state of industry conditions outside of the resources sector was highlighted in the findings of the NAB Business Conditions survey which revealed that mining continued to report solid conditions in June, while the retail sector deteriorated sharply to concerning levels, and weakness persisted in the manufacturing, construction and wholesale sectors. Business confidence levels also fell across the majority of the non-resource sectors with the most marked declines reported in construction, followed by finance/business & property services, retail and recreation & personal services. These findings are consistent with Ai Group's Performance of Manufacturing Index (**Australian PMI®**), Performance of Services Index (**Australian PSI®**) and Performance of Construction Index (**Australian PCI®**), which reveal continued tough conditions in manufacturing and on-going declines in construction and service sector activity. This indicates that large parts of the Australian economy are continuing to struggle under the weight of high dollar, continued cautiousness of households and the lingering effects of the January floods.

Latest data*

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| Official cash rate | 4.75 per cent - |
| AUD/USD exchange rate | \$1.0640 ▼ |
| Oil price | USD 97.22 per bbl ▲ |
| Annual growth in GDP | 1.0 per cent - |
| Unemployment rate (%) | 4.9 per cent - |
| Annual growth in headline CPI | 3.3 per cent - |
| Copper price | AUD 9028.20 ▼ |
| Australian PMI (June) | 52.9 - |
| Australian PSI (June) | 48.5 - |
| Australian PCI (June) | 35.8 - |

Week in Preview: 18 April – 21 April 2011

- ABS **Sales of New Motor Vehicles** data for June 2011 will be released on Monday.
- The minutes of the July **Reserve Bank of Australia Monetary Policy Briefing** of the RBA Board will be released on Tuesday.
- On Tuesday, the ABS will also publish its latest **International Merchandise Imports** data for Australia. This will provide data on total imports and commodity aggregates for June 2011.
- The **Westpac – Melbourne Institute Leading Index** for May 2011 (which indicates the likely pace of economic activity three to nine months into the future) will be released on Wednesday.
- Also on Wednesday, the ABS will release data on the value of non-residential **Building Activity** for the March quarter 2011, including detailed estimates of work done, commencements and work yet to be done.
- On Friday, the ABS will release its **International Trade Price Indexes** publication for June 2011.

* Arrows represent directional movement relative to previous week's issue. For further assistance from Ai Group's Economics & Research Unit or for any suggestions for economic information you would like to be included in the report, please email economics@aigroup.asn.au.