Ai GROUP ECONOMICS WEEKLY

Week in Review: 14 – 17 June 2011

- ABS data on **Lending Finance** showed that total finance commitments (which include housing, personal, commercial and lease finance) declined by 3.8% (seasonally adjusted) in April. The commercial sector, which is the major driver of overall credit, contracted by 8.8% to be at its lowest level in the past seven months while personal finance commitments rose by just 0.4% in the month consistent with on-going consumer caution and the reluctance by consumers to take on debt. In contrast, the value of owner-occupied housing finance increased by a solid 6.3% in April, suggesting that housing conditions are starting to improve from the weather induced weakness of the first quarter of the year.

- The **National Australia Bank Monthly Business Survey** showed that business conditions deteriorated further in May. The overall business conditions index (a composite index of trading performance, profitability and employment) fell by 4.0 points to a +1.0 point index level, only slightly above the weak levels recorded in February immediately following the floods. The decline in business conditions reflected broad-based falls in trading conditions, employment and profitability. The survey also revealed that business confidence declined in May (despite remaining in positive territory) with the manufacturing reporting the weakest confidence levels of all industries, indicating that the high Australian dollar is continuing to weigh on sentiment.

- The **Westpac-Melbourne Institute Consumer Sentiment Index** declined by 2.6% to 101.2 in June, the lowest reading since June 2009. Consumers' concerns about their own financial position were reflected in fall of 2% in the component of the Index measuring "family finances compared to a year ago" and a fall of 2.1% in the Index tracking views on "whether now is a good time to buy more household items". Consumer caution also dominated savings decisions in the survey with a significant shift in preferences towards low risk investments. Additionally, respondents expressed less confidence about prospects for the economy with assessments of "economic conditions over the next 12 months" and; "economic conditions over the next 5 years" falling by 6.2% and 3.7% respectively.

- ABS preliminary estimates of **Dwelling Unit Commencements** showed that the total number of dwelling units commenced rose by a seasonally adjusted 3.1% in the March quarter (following a fall of 4.0% in the December quarter 2010) to be 12.9% down on an annual basis. Commencements of new private sector other residential buildings (largely comprising apartments) increased by 14.7% in the March quarter while new private sector house commencements (comprising almost 60% of total commencements) fell by 1.9%. On a state basis, growth in the quarter was driven by a strong rise of 12.8% in Queensland followed by New South Wales (+7.7%) and Victoria (+1.8%). Falls were registered in Tasmania (-9.3%), Western Australia (-4.5%) and South Australia (-2.9%).

- ABS data compiled in conjunction with the Federal Chamber of Automotive Industries showed that **New Motor Vehicle Sales** declined by a seasonally adjusted 7.6% in May, the largest monthly decline since January 2001. This fall reflected a combination of weak consumer spending and supply issues due to production disruptions in Japan. For the year, new motor vehicle sales were down by 14.5%. During May sales of passenger vehicles, sports utility and other vehicles decreased by 7.5%, 10.6% and 4.5% respectively. Declines were registered in all eight states and territories during May with Victoria recording the largest percentage decrease of 12.3%, followed by the Australian Capital Territory (8.5%) and Queensland (7.3%).

How this affects you

The contraction in commercial finance is a likely reflection of weak demand for lending from small and medium businesses which are typically more reliant on bank lending to fund expenditure (as distinct from internal cash flows/equity. It is also a further indication that the trading environment encountered by large parts of the economy is not yet supportive of a rise in capital investment to boost capacity, with many businesses outside of mining continuing to struggle under the weight of the strong Australian dollar. In addition, consumers remain cautious in their intentions, despite incomes growth and a robust jobs market. The degree of conservatism among consumers was underlined by the subdued growth in personal finance commitments in April, whilst the Westpac Melbourne Institute Index of Consumer Sentiment revealed continued caution with respect to households' financial decisions and a less optimistic view on both the medium and longer term prospects for the economy. The subdued state of industry conditions outside of mining was highlighted in the findings of the NAB Business Conditions survey which revealed that the retail, manufacturing, wholesale and construction sectors exhibited particular weakness in May in stark contrast to the on-going strength in mining, which surged higher in the month. Profitability also deteriorated in the majority of non-resource sectors according to the NAB survey, with the most marked declines recorded in wholesale and construction. This is consistent with Ai Group's performance indices which revealed continued declines in manufacturing, services and construction sector activity during May. It is also a strong indication that factors including the sustained high dollar, higher interest rates, and skill shortages, together with cautious consumer and investor spending, are dampening conditions in these sectors with implications for the growth of the broader economy.

Latest data*

Official cash rate	**4.75 per cent -**
AUD/USD exchange rate	**$1.0626 ▲**
Oil price	**USD 93.00 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 8565.31 ▲**
Australian PMI (May)	**47.7 -**
Australian PSI (May)	**49.9 -**
Australian PCI (May)	**39.6 -**

Week in Preview: 20 June– 24 June 2011

- The minutes of the June 2011 **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 May 2011.

- The **Westpac – Melbourne Institute Leading Index** for April 2011 (which indicates the likely pace of economic activity three to nine months into the future) will be released on Wednesday.

- Speech by **Philip Lowe, Reserve Bank of Australia, Assistant Governor** (Economic), to the BankSA Trends Business Luncheon, InterContinental Hotel, Adelaide, 11.30 am Friday.

* 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.