# Ai GROUP ECONOMICS WEEKLY

## Week in Review: 21 March – 25 March 2011

- Preliminary **ABS Merchandise Imports** data revealed that that imports increased by a seasonally adjusted 6% in February 2011 on a balance of payments basis. Imports of intermediate and capital goods rose by 12% and 2% respectively, while imports of consumption goods were largely unchanged.

- The Reserve Bank of Australia's March 2011 **Financial Stability Review (FSR)** reported on the current state of the financial system, noting that confidence in the banking systems of major countries had generally improved since the time of the previous Review in September 2010. Nevertheless, it was reported that banks globally faced a number of challenges arising from the high level of non-performing asset ratios in many banking systems; the continued dislocations in property markets and; the likelihood of a slow and patchy recovery in some major economies. This was expected to weigh on banks' asset quality and profitability. With respect to Australia's banking system, the FSR reported that it had continued to outperform many other countries consistent with the relative strength of the domestic economy in recent years. Deposits had continued to outpace growth in credit (reducing their reliance on short-term wholesale debt) and profitability had recovered to near pre-crisis levels for the largest banks. In addition, recent adverse weather events were not expected to have a major negative effect on bank's asset quality. However, it was noted that non-performing asset levels remained higher than a few years ago despite slight signs of improvement in non-performing business loans. The FSR also pointed to the challenges facing Australia's financial institutions in adapting to a post crisis environment where growth opportunities will be more limited, particularly given the more cautious approach that was being exhibited by consumers and businesses to borrowing.

## How this affects you

Last week's data pointed to restraint by businesses in their investment expenditure in early 2011 despite the influence of a strong Australian dollar which is acting to lower the cost of imports. Spending on telecommunications equipment and industrial transport imports were both pared back (original terms) in February while expenditure on imports of industrial machinery and equipment increased by just 1.4% (or $17 million) following a 10.0% decline in January. This suggests a degree of caution by businesses, and indicates that many may still be holding back on any discernable increase in their capital base until signs emerge of a broader lift in economic growth. This is also consistent with recently released RBA credit data revealing a fall in business credit in January. Moreover, the increase in imports of intermediate and other merchandise imports was mainly driven by fuels and lubricants with a number of the other capital input categories either declining or showing subdued growth. On-going caution by consumers was also suggested by the relatively flat level of imports of consumption goods in February, an outcome which is consistent with the recent slowing in domestic demand and weak retail volumes. On the positive side, the strong increase in Australia's terms of trade (the ratio of export prices to import prices) is boosting national income and is expected to be supportive of stronger consumer and business spending through the full course of 2011. This is despite the anticipated short term dampening impact on the Australian economy from recent severe weather events and the negative ramifications of the earthquake in Japan on growth prospects.

## Latest data*

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|---|---|
| **Official cash rate** | 4.75 per cent - |
| **AUD/USD exchange rate** | $1.0259 ▲ |
| **Oil price** | **USD 104.84 per bbl** ▲ |
| **Annual growth in GDP** | 2.7 per cent - |
| **Unemployment rate (%)** | 5.0 per cent - |
| **Annual growth in headline CPI** | 2.8 per cent - |
| **Copper price** | AUD 9469.73 ▼ |
| **Australian PMI (February)** | **51.1 -** |
| **Australian PSI (February)** | **48.7 -** |
| **Australian PCI (February)** | **44.6 -** |

## Week in Preview: 28 March – 1 April 2011

- On Wednesday, the ABS will release estimates of **Job Vacancies** in February 2011 for the private and public sectors.
- The ABS data will be supplemented with the release by the Department of Education, Employment and Workplace Relations on Wednesday of the **Skilled Vacancy Report** for March 2011.
- The HIA - Jeld-Wen **New Home Sales** report for March 2011 will also be published on Wednesday.
- On Thursday, the ABS will release data on **Retail Trade** and **Building Approvals** for February 2011.
- Data for February on total credit provided to the private sector by financial intermediaries will also be made available on Thursday with the release of the latest RBA **Financial Aggregates** publication.
- Ai Group will release its Australian Performance of Manufacturing Index **(Australian PMI®)** for March 2011 on 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.