

January 2010

## Economic snapshot

### Key points

The highlights for January are: a breather on cash rate momentum: a return to Canberra and the debate on climate change and aging of the Australian population: confirmation that the German economy shrank by 5% in 2009 (c/f +8.7% for China): tensions building in the Eurozone on the possibility that Greece could default on its debt obligations, and the UK finally crawls out of recession (just) in the final Q of 2009.

### Statistics, statistics and more statistics



Building approvals; new car sales; job ads (Dec); personal finance commitments; unemployment; house prices; retail sales; trade



Construction activity; home loans; job ads (Jan); new home sales.

### Australia

- Last week the RBA outsmarted most economists as the day began with a 70% probability that they would increase rates by a further 25bps - whereas they announced no change in lieu of increased market competition amongst lenders. Most likely this is simply a month deferment of the inevitable and many believe it wise to budget for a full 1% rise over the next 12 months. Even the Treasurer got in early and warned banks about gouging on the back of the (would be) interest rate rise.
- The Central Banks demurring can be sourced from the Governor's accompanying statement which, while providing a bullish perspective on the local economy, stated "inflation has, as expected, declined in underlying terms from its peak in 2008, helped by the fall in commodity prices at the end of 2008, a noticeable slowing in private sector labour costs during 2009, the recent rise in the exchange rate and, a period of slower growth in demand.....inflation is expected to be consistent with the target in 2010".
- One major debate galvanizing the nation in the last six months has been around climate change and how best to tackle global warming. This is an issue that will receive a lot of attention during this sitting of Parliament and may endure post the 2010 election. However, a second debate - and one that is similarly resonating in every Western democracy - relates to an aging population. This is not new and there have been many studies and dire predictions leading up to the current focus by the Treasurer and the PM.
- The implications of an aging population are severe as the social fabric is burdened by a population that requires mounting support to maintain a reasonable level of wellbeing. To be over simplistic, popular rhetoric states that the younger, healthier and working (productive) members of the community will have to increasingly forgo Government services and pay higher taxes to maintain the unproductive (and growing) rump of the community. If true, Government deficits, higher taxes and reduced services will characterise the Australian economic and political landscape over the next 40 years and possibly beyond.
- The irony is that the boomers are the ones that invented middle class welfare, have lived well from Government largesse and are now leaving the implications for the less fortunate to clean up. There are many counter arguments to this, not least of which is the quality of life enjoyed now by all Australians is the result of the investment and sacrifices of those now entering their senior years. As the piper gets paid though the prognosis is not good and Australia will have to embrace substantial productivity increases (through public/private investment/education/broad-based skilling) and probably a lift in the SGL to 12% (interim) and eventually to 15% (and maybe beyond). Meanwhile infrastructure investment isn't enjoying the best of times with the private sector concerned by tax issues and poor yields and risk return premiums.
- There's also been significant conjecture about the heat of the Chinese economy and the potential for a bust that could replicate the crisis the Japanese economy endured (and never recovered from) in the early 1990's. The argument is simple and revolves around an asset price bubble (particularly housing) which is pricked by assertive monetary policy (self inflicted as the Central Bank moves to stymie runaway inflation). The fear in (and outside) China is that the wound will be self inflicted and reverberate around the world (particularly in Australia). Beyond the concerns of the mounting US Government deficit on world financial order, this is one issue that could be a significant threat to the increasing prosperity of Australia.

### Rest of World



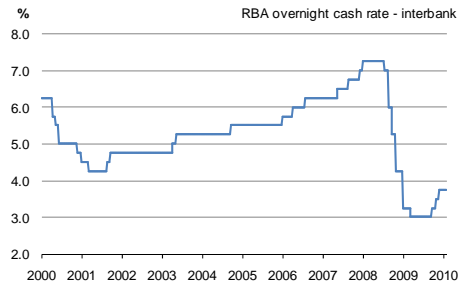
- GDP in the world's third-largest economy (China) rebounded to double-digit growth in the 4Q09 at 10.7%. China's authorities are tightening bank lending and increasing borrowing costs to keep a lid on price pressures. A recent poll in China found that 80% of respondents associated "happiness" with "owning their own home". Property prices in China's 70 major cities rose at the fastest pace in 16 months in November 2009, raising the spectre of an asset bubble.
- The UK crawled out of recession in the final quarter of 2009, recording a meagre 0.1%. This was tepid to say the least, but heralded the end of the longest recession in recorded UK financial history.
- The US economy grew by 4% over the last six months of 2009 but recorded a budget deficit of US\$1.3T (or 9.2% of GDP). The deficit forecast for 2010 is forecast to rise to a massive US\$1.56Trillion.

### Summary

Australia escaped the global meltdown and the Central Bank hit the running boards hard and early. Unemployment is falling; the RBA is happily asserting its independence and WA is recording the best economic statistics, again. This leads back to the 2 pace economy in West vs. Eastern Australia. For economic thinkers, a fear of the mounting size of US and other public debt remain (too many highly geared public balance sheets) and a possible pricking of an emerging bubble in China. These issues mount up as potential threats to our economic prosperity and near term performance.

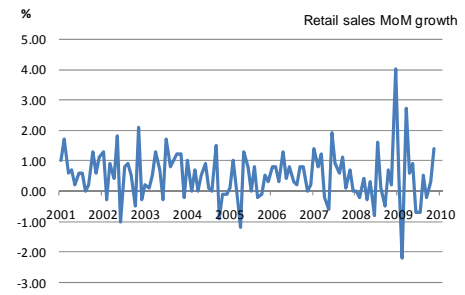
## Big picture indicators

RBA cash



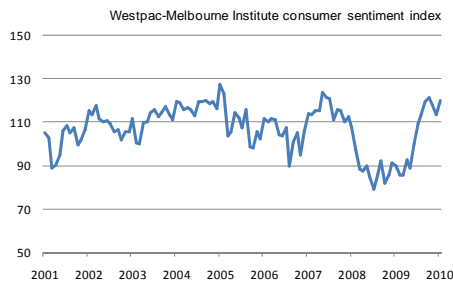
Source: RBA

Retail sales



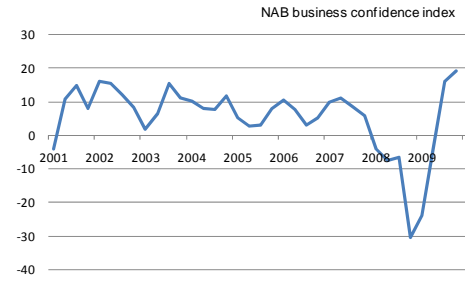
Source: ABS

Consumer sentiment



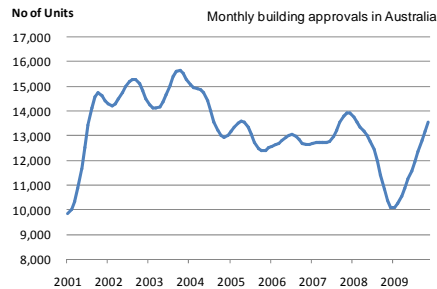
Source: Melbourne Institute

Business sentiment



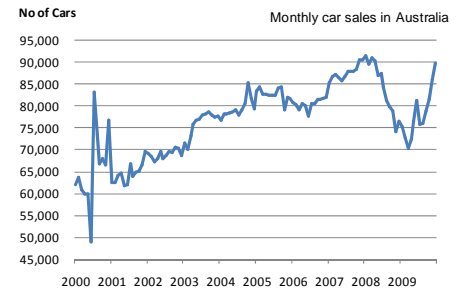
Source: NAB

Building approvals



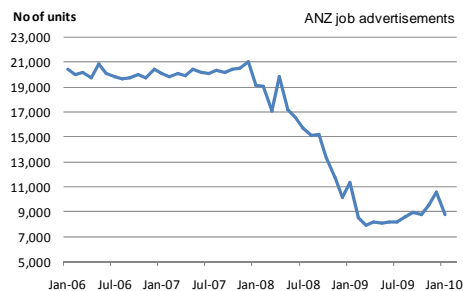
Source: ABS

Car sales



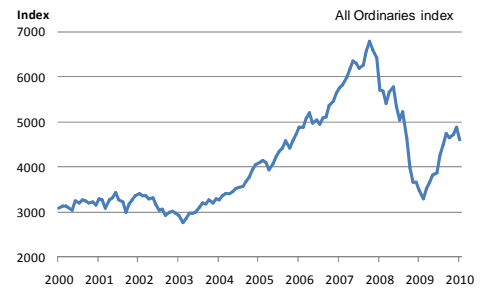
Source: ABS

Job ads



Source: ANZ

ALL ORDS



Source: IRESS

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