

Economic and Market Overview – September 2013

National Data and Impact of International Factors

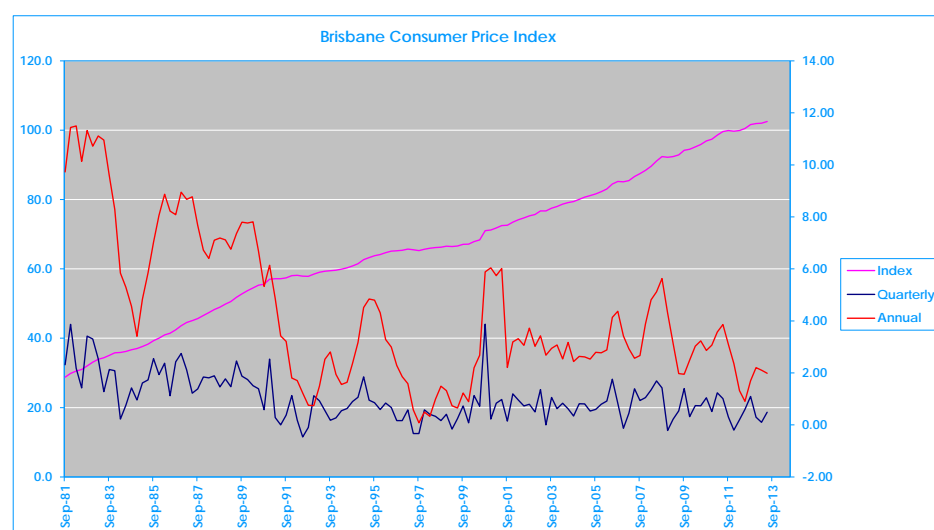
Consumer
Price Index
June Qtr 2013

The Australian Bureau of Statistics states:

- The most significant price rises this quarter were for medical and hospital services (+3.4%), tobacco (+3.0%), new dwelling purchase by owner-occupiers (+0.9%), furniture (+4.8%) and rents (+1.1%).
- The most significant offsetting price falls this quarter were for domestic holiday travel and accommodation (-4.0%) and automotive fuel (-3.1%).

Queensland Treasury and Trade Overview of the June Qtr 2013 states:

- Brisbane's headline consumer price index (CPI) increased 0.5% in June quarter 2013, to be 2.0% higher over the year. In annual terms, Brisbane recorded the second-lowest increase while Darwin recorded the largest increase for all capital cities in Australia.
- For Brisbane, the Housing group made the largest contribution to inflation in June quarter 2013 (0.23 of a percentage point). Within the Housing category, New Dwelling purchase by owner-occupiers increased 1.8% in the quarter.
- For Brisbane, the Transport group recorded the largest detraction from inflation in June quarter 2013 (-0.14 of a percentage point). Within the Transport category, automotive fuel decreased by 3.0% in the quarter.



Source : Chesterton Research

The following commentary is extracted from the Reserve Bank of Australia in its August statement on monetary policy and minutes of the 3rd September 2013 meeting of the board. It is supplemented with Chesterton research as identified.

Economic
Activity

- The outlook for the global economy is a little softer than at the time of the *May Statement*. World GDP growth is expected to remain close to average over the rest of this year, but with annual average growth of around 3 per cent for 2013 reflecting weaker growth around the turn of the year. Growth is then expected to pick up, to be slightly above average in 2014.
- Growth of Australia's major trading partners in the June quarter was around its average of the past decade and recent indicators suggested that this pace of growth had continued. The Chinese economy was growing at the pace evident since the start of the year,

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Economic Activity (Cont'd)

- There had been a modest rise in global commodity prices since the previous Board meeting. Spot prices for iron ore had increased, consistent with further growth in Chinese steel production. Crude oil and base metals also rising over the past month (August, 2013).
- Prospective changes in the stance of US monetary policy remained the main focus of financial markets over the past month (August, 2013). Members observed that while the Federal Reserve was not expected to increase its policy rate until 2015, markets anticipated the fed could commence 'tapering' its asset purchases at its September meeting.
- The depreciation of the exchange rate will be helpful in rebalancing growth given the transition that the Australian economy is facing. Business investment as a share of GDP has risen to record high levels, with mining investment rising substantially on the back of very high levels of the terms of trade. Though they remain high, the terms of trade have declined over the past two years.
- For June Quarter; Household consumption growth appeared to have been below the average of recent years, while business investment overall looked to have increased and exports growth remained relatively strong.
- The available indicators suggested that growth of household consumption in the June quarter had been below average. Retail sales had been little changed since March and retail sales growth had been only modest in recent months. In contrast, measures of consumer sentiment had moved higher and were a little above long-run average levels.
- Conditions in the housing sector show continued improvement in response to lower interest rates
- Exports also grew in the June quarter with strong growth in resources. The depreciation of the Australian dollar is also expected, over time, to help export volumes more broadly.
- On the domestic front, there are risks to both the downside and upside for economic activity and inflation. In particular, there remains considerable uncertainty about the process of economic growth rebalancing away from mining investment towards other sources of domestic demand and to exports.

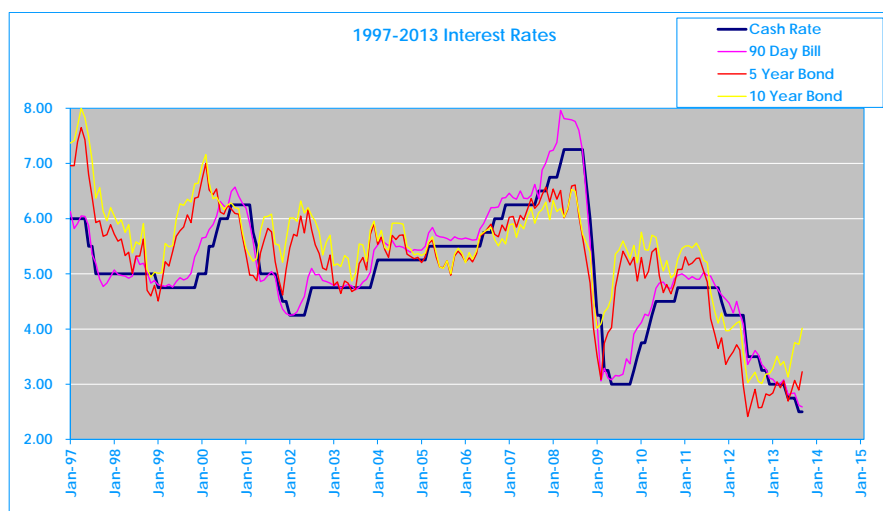
Interest Rates

- The Reserve Bank Board maintained the target cash rate at 2.50 per cent at its September meeting. Rates on overnight indexed swaps (OIS) currently imply an expectation that the cash rate will be lowered to 2.25 per cent early in 2014.
- Rates on bank bills and certificates of deposit (CDs) are lower than at the time of the previous *Statement*, with the yield on 3-month bills reaching a historical low of 2.59 per cent in early August. The spread between 3-month bills and OIS rates has remained broadly stable at around 15 basis points in recent months.
- In contrast, yields on long-term Commonwealth Government securities (CGS) have increased significantly since the previous *Statement*, reflecting the rise in bond yields observed globally.
- In more volatile trading conditions, 10 year CGS yields briefly reached an 18-month high of 4.04 per cent in late June as speculation grew that the US Federal Reserve may taper its asset purchase program earlier than anticipated.
- With the 10-year CGS yield 60 basis points above its levels of three months ago and the prices of shorter term CGS supported by expectations of further monetary policy easing, the spread between 3-year and 10-year CGS is now around 120 basis points, its widest level in around four years.

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Interest Rates (Cont'd)



Interest Rates	31 Aug 12	31 Jul 13	31 Aug 13	12 mth change	One month change
Cash Rate	3.50%	2.75%	2.50%	(1.00%)	(0.25%)
90 day Bill	3.58%	2.68%	2.60%	(0.98%)	(0.08%)
5 year Bond	2.61%	2.92%	3.09%	0.48%	0.17%
10 Year Bond	3.04%	3.74%	3.90%	0.86%	0.16%
Spread 90 day to 10 year	0.54%	(1.06%)	(1.30%)	(1.84%)	(0.23%)
Spread 5 year to 10 year	(0.44%)	(0.82%)	(0.81%)	(0.38%)	0.01%

Source : Chesterton Research

International Equity Markets

- Equity prices in major markets have fluctuated significantly since the previous *Statement*, falling by around 8½ per cent in late May and June before almost fully recouping this, to be back around their highest level since 2008.

Indices	31 Aug 12	31 Jul 13	31 Aug 13	12 mth change	One month change
All Ordinaries	4,339.00	5,035.70	5,125.30	18.12%	1.78%
Property Trusts	914.40	1,021.40	1,008.80	10.32%	(1.23%)
Nikkei	8,839.91	13,668.32	13,388.86	51.46%	(2.04%)
Hang Seng	19,482.57	21,883.66	21,731.37	11.54%	(0.70%)
Dow Jones	13,090.84	15,499.55	14,810.31	13.13%	(4.45%)
Nasdaq	3,066.96	3,626.37	3,589.87	17.05%	(1.01%)
FTSE	5,711.50	6,621.10	6,412.90	12.28%	(3.14%)

Source : Chesterton Research

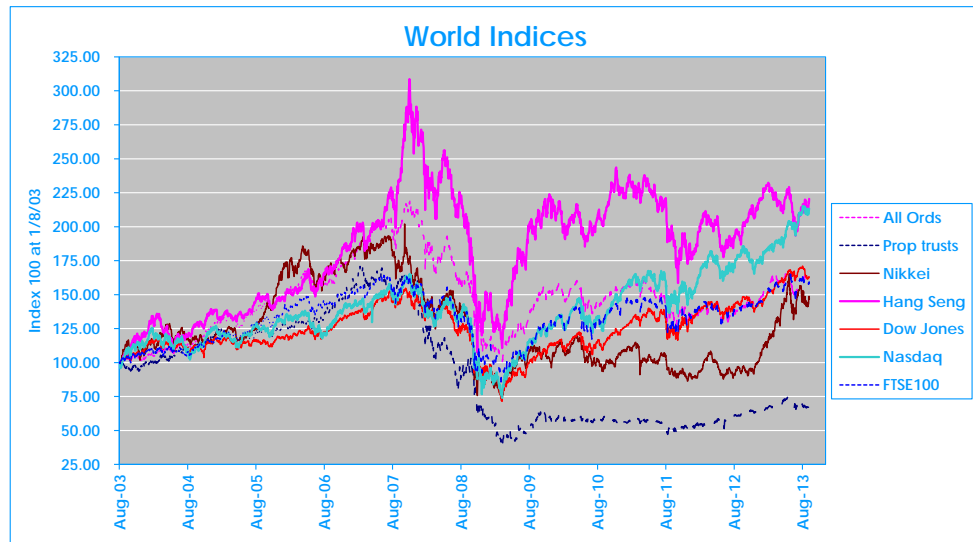
- Equity prices have been most resilient in the United States, with the S&P 500 surpassing its previous historical peak as economic data improved and the outlook for corporate profits strengthened.
- Japanese share prices fell by 20 per cent from late May to early June, following the 80 per cent run-up in equity prices from November 2012. Measures of volatility in Japanese share prices also increased significantly during this time.
- European equities have been little changed since the previous *Statement*, weighed down by continued weak economic data and ongoing concerns about peripheral euro area economies. Expansion in the euro area noted in the RBA September minutes, looks hopeful for future growth.

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International Equity Markets (Cont'd)

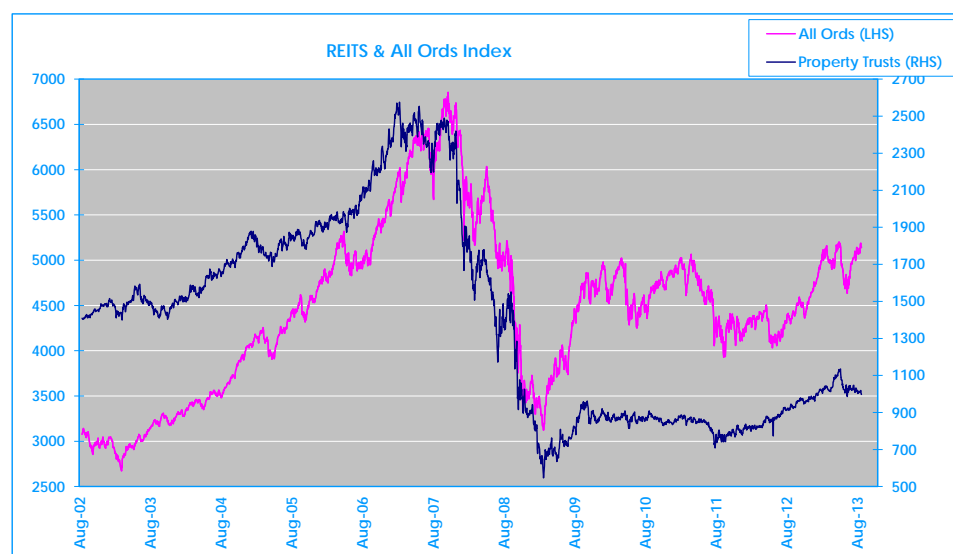
- The falls in share prices have been particularly sharp for Brazil, where economic growth appears to have softened, and China, where weaker-than-expected data and concerns about the PBC's initial reluctance to alleviate the liquidity shortage in interbank markets weighed on investor sentiment. Concerns about the outlook for Chinese growth also weighed on Asian markets more broadly.



Source: Chesterton Research

Domestic Equity Markets

- Australian equity prices have declined by 4 per cent since the previous Statement, weighed by uncertainty about the outlook for economic growth in China and uncertainty over the path of monetary policy in the US.
- Resources sector share prices fell by 3 per cent since the previous Statement, despite declining almost 14 per cent at one stage.
- In contrast, share prices of energy companies have been broadly unchanged since the previous Statement due to support from higher oil prices.
- Financial sector share prices declined by 5 per cent, largely due to declines in the prices of high-yielding bank stocks.

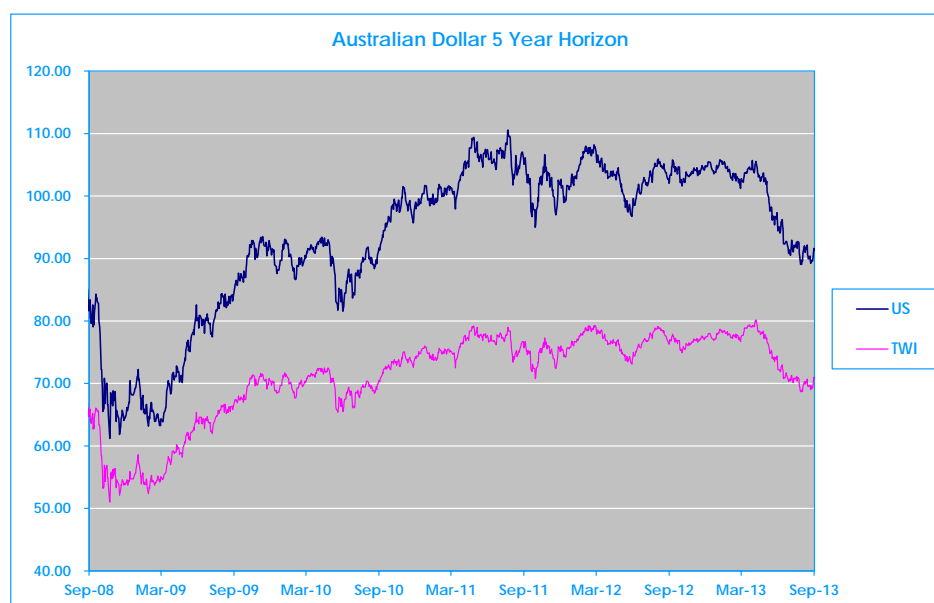


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Australian Dollar

- After briefly reaching its highest level since 1985 on a trade-weighted basis in early April, the Australian dollar has depreciated against most currencies to be around 15 per cent below its April peak.
- In trade-weighted terms, the Australian dollar is now around its lowest level since August 2010, though it remains at a high level by longer-term standards



Economic Outlook

- Growth of Australia's major trading partners in 2013 is expected to be a bit below its decade average of around 4 per cent, before picking up to 4¼ per cent in 2014.
- The exchange rate is assumed to remain at its current level over the forecast period (A\$ at US\$0.90 and the TWI at 69, which is around 10 per cent lower than was assumed in the May Statement).
- The cash rate remained unchanged (September meeting) at 2.50 per cent. This profile is slightly higher than market expectations, which currently imply a further 25 basis point reduction in the cash rate by the end of the year.
- GDP growth is expected to remain a little below trend at close to 2½ per cent through to mid 2014, before picking up to above-trend growth by the end of the forecast horizon.

Output Growth & Inflation Forecasts						
	Year Ended					
	June 2013	Dec 2013	June 2014	Dec 2014	June 2015	Dec 2015
GDP Growth	2.50%	2.25%	2.50%	2.5 - 3.5%	2.75 - 3.75%	2.75 - 4.25%
Non-farm GDP Growth	2.50%	2.25%	2.50%	2.5 - 3.5%	2.75 - 3.75%	2.75 - 4.25%
CPI Inflation	2.40%	2.00%	2.50%	2 - 3%	2 - 3%	1.75 - 2.75%
Underlying Inflation	2.50%	2.25%	2.25%	2 - 3%	2 - 3%	2 - 3%
	Year Average					
	2012/13	2013	2013/14	2014	2014/15	2015
GDP Growth	2.75%	2.25%	2.50%	2.25 - 3.25%	2.5 - 3.5%	2.75 - 3.75%

Source : Reserve Bank Statement of Monetary Policy August 2013

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- The forecast for consumption spending has been revised lower since the May *Statement*, with the available partial data pointing to near-term weakness.
- Retail sales were unchanged in the June quarter, while consumer sentiment has fallen back towards average levels after rising earlier in the year. The outlook for mining investment has been revised lower reflecting several considerations.
- The outlook for export volumes remains strong with exports expected to make a significant contribution to GDP growth in the coming years.
- The recent depreciation of the exchange rate is unlikely to have affected underlying inflation in the June quarter, but it is expected to exert upward pressure on the prices of tradable items over the next few years.

Queensland Economic Drivers within National Economy

Economic Activity

- Queensland's state final demand (SFD) grew by 0.6% in seasonally adjusted (sa) terms for the second consecutive quarter in June quarter 2013, to be 1.8% higher over the year.

Indicator	% Change		Contribution to SFD	
	Qtr	Annual	Qtr	Annual
Household Consumption	0.50%	2.40%	0.30%	1.20%
Dwelling Investment	0.20%	(7.20%)	0.00%	(0.30%)
Business Investment	(0.50%)	7.00%	(0.10%)	1.30%
Engineering Construction	(4.30%)	1.90%	(0.50%)	0.20%
Non-residential building	9.30%	26.70%	0.20%	0.60%
Public Final Demand	1.30%	(2.80%)	0.30%	(0.60%)
State Final Demand	0.60%	1.80%	0.60%	1.80%
Overseas exports of goods	3.60%	14.70%	na	na
Overseas imports of goods	(3.80%)	(0.80%)	na	na

Seasonally adjusted figures, June Qtr 2013

Sourced from ABS 5206.0 summarised by OESR

- *Household consumption* rose by 0.5% in June quarter 2013 compared to 0.8% in March quarter 2013 and was 2.5% stronger over the year. Expenditure on rent, other dwelling services, furnishing, insurance and vehicles (which all grew over the quarter) were the highest contributors over the quarter.
- Business investment fell 0.5% in June quarter 2013, but was 7.0% higher over the year. Business investment in Queensland in the past two years has been driven by three major CSG-to-LNG projects, which in aggregate have a nominal construction value of over \$60 billion. After reaching a record high in March quarter 2013, new engineering construction fell by 4.3% in the June quarter.
- Overseas exports of goods rose 3.6% in June quarter 2013 in real terms, after falling 3.8% in March quarter 2013. In year average terms, while the real value of exports rose 6.7%, the nominal value fell 15.2%, as lower world prices of key commodities and the strong A\$ weighed on returns to exporters.
- Overseas imports of goods fell 3.8% in June quarter 2013. However, the ABS treatment of LNG imports has somewhat distorted this series in recent years, given that some imports associated with the LNG projects are accounted for at the national level, but have not been assigned at the state and territory levels.

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Queensland Economic Drivers within National Economy (Cont'd)

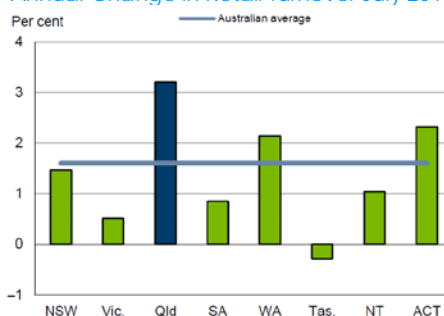
Labour Force

- Trend employment in Queensland rose 0.1% for the third consecutive month in August 2013, to be 0.9% higher over the year. Over the year to August 2013, trend employment grew 22,200 persons, with part-time employment rising 20,700 persons and full-time employment 1,500 persons. Queensland has recorded the strongest trend employment of any state in August.
- With trend labour force also rising 0.1% in the month, Queensland's trend unemployment rate was unchanged at 6.0% in August.
- The trend participation rate in Queensland remained at 65.8% in August 2013, well below its peak of 67.4% recorded in October 2011.
- In more volatile seasonally adjusted (sa) terms, employment in Queensland fell 5,100 persons in August 2013, partially unwinding the very strong 18,500 person rise recorded in July. With sa falling, the sa unemployment rate edged up 0.1 percentage point to 6.0%.
- Nationally, sa employment fell 10,800 persons in August 2013, following a similar decline in July and a much weaker result than market expectations of a 10,000 person rise. The sa unemployment rate rose 0.1 percentage point, from 5.7% to 5.8%, in line with market expectations.

Retail Trade

- The trend estimate of Queensland's retail turnover remained mostly unchanged in July 2013. Australia's trend turnover decreased by 0.1% during the month.
- The trend value of Queensland's retail turnover decreased from \$4,591.70 million in June 2013 to \$4,589.60 million in July 2013.
- The marginal decrease in Queensland's nominal retail turnover in July 2013 mainly reflected higher spending in cafes, restaurants and takeaway food services and lower spending in Department stores.
- The trend value of Queensland's retail turnover increased by 3.2% over the previous 12 months, from \$4,447.00 million in July 2013.
- Queensland recorded the highest annual growth in retail trade of all states and territories (3.2%). Australian Capital Territory recorded the second-highest increase (2.3%).
- *Cafes, restaurants and takeaway food services* recorded the largest contribution to retail turnover growth in Queensland in the month (0.07 percentage points). *Food retailing* recorded the largest contribution to retail turnover growth in Australia (0.04 percentage points) in July 2013.

Annual Change in Retail Turnover July 2013



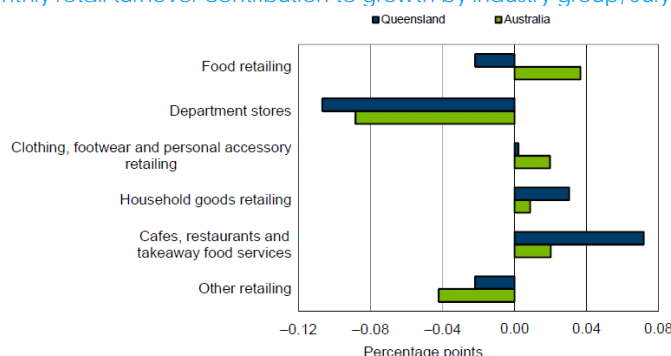
Source: Government Statistician Queensland Treasury & Trade

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Queensland Economic Drivers within National Economy (Cont'd)

Retail Trade
(Cont'd)

Monthly retail turnover contribution to growth by industry group, July 2013



Source: Government Statistician Queensland Treasury & Trade

Building Approvals & Construction

Dwelling approvals

- The trend estimate for total dwelling units approved in Queensland in July 2013 was 2,543, three less approvals than the June 2013 figure. The national trend estimate for total dwelling approvals increased 0.9% during the month.
- The trend estimate for the number of private sector house approvals in Queensland increased 1.8% in July 2013, with a total of 1,538 houses approved. Australia's trend estimate for the number of private sector house approvals was 8,205, an increase of 1.1% from the June 2013 figure.
- In July 2013, trend total dwelling units approved in Queensland accounted for 18.3% of Australia's total dwelling unit approvals. Private sector house approvals in Queensland accounted for 18.7% of Australia's private sector house approvals.
- The trend nominal value of residential building work approved in Queensland decreased 0.5% in July 2013 to a total of \$713.2million. Australia's trend value of residential building work approved increased 0.7% over the month to \$3,998.8 million.
- In annual terms, the trend estimate for total dwelling units approved in Queensland in July 2013 was 8.3% higher than the July 2012 estimate. In comparison, total dwelling units approved in Australia increased 6.7% over the same period.
- Dwelling investment increased by 0.2% in June quarter 2013, but was 7.2% lower over the year. Construction of new dwellings fell by 1.0% in the June quarter to register an annual fall of 2.6%. Alterations and additions increased by 1.8% in the June quarter, but fell by 12.4% over the year.

Non-residential building

- The trend value of non-residential building approved in Queensland in July 2013 was \$506.3 million, a decrease of 3.6% over the month. The value of non-residential buildings approved in Australia in July 2013 was \$2,839.1 million, a decrease of 3.4% over the month.
- *Non-residential building construction* (which includes shops, offices, etc., and is currently 14.0% of total business investment) increased 9.3% in the quarter, to be 26.7% higher than a year ago.