WEEKLY ECONOMIC COMMENTARY

Week beginning 21st September 2015

ECONOMIC DATA ROUNDUP

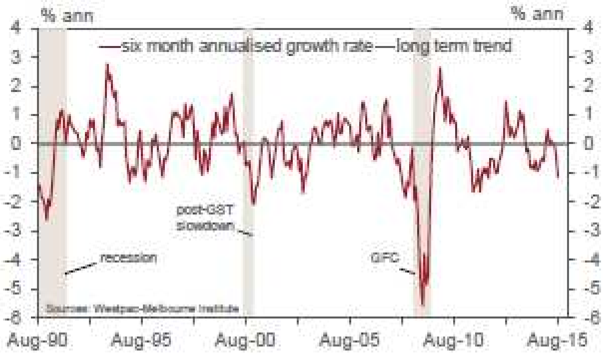
DATA RELEASED LAST WEEK

Economic Data	Period	Actual	Previous
Motor Vehicle Sales	August	-1.6%	-1.3%

New motor vehicle sales declined 1.6% in August representing the second consecutive monthly fall. At this time last year, sales were 2.1% higher. Passenger and other vehicles decreased by 0.3% and 0.7% respectively while sales for sports utility vehicles increased by 0.5%.

In other data released last week, the **Westpac-Melbourne Institute Leading Index**, which indicates the likely pace of economic activity three to nine months into the future, decreased to -1.14% in August from -0.40% in July (refer chart at right). The Leading Index gives insight into the likely momentum in the economy through the second half of 2015 and beyond, and the latest weak number points to a likely "below trend" start to next year.

Westpac/MI Leading Index



The September **Reserve Bank Board minutes** were released last week, but offered little new information for the market. The RBA highlighted the volatility in global share markets over August, with reactions to concerns over China's slowing growth and the devaluation of the Yuan seen as the main drivers of the volatility. Despite some improvement in the US and European growth numbers, the events in financial markets were shaped as increasing the "downside risks" to the world growth outlook. Given that growth remains soft and economic data patchy, economists continue to expect the cash rate to remain on hold, although recent developments suggest that the risks have further tilted towards lower rates.

The headlines were devoted to the **Liberal Party leadership** vote last week where Malcolm Turnbull defeated the incumbent Tony Abbott 54 votes to 44 to become Australia's 29th Prime Minister. The change should be positive for the market, with Mr Turnbull's former career as a successful investment banker and corporate lawyer viewed positively by investors. None of Australia's recent Prime Ministers (Tony Abbott, Julia Gillard or Kevin Rudd) had experience with financial markets.

Turnbull has now announced his new Cabinet will feature a new Treasurer in Scott Morrison. This change is likely to be taken positively as the market had lost faith in Joe Hockey following poorly received budgets and a perceived inability to "read" the economy.

The change of leadership should be positive for both business and consumer sentiment which have been adversely affected recently by the lack of economic and fiscal policy direction. Turnbull will also engage in informed economic debate rather than catchphrases to address previously forgotten inquiries into areas that could increase economic growth, productivity and supply side reform.

It's not all plain sailing though as Mr Turnbull has inherited a slowing economy and he will need to start showing economic leadership quickly. That said, it is highly unlikely that economists or analysts have changed their forecasts for GDP growth this year, the official cash rate, or the Australian dollar on account of these political developments.

A continuation of the Abbott Government might have led to an early election but the change in Prime Minister is more likely to see the current government serving the full term, which expires on 11 November 2016.

Data over the next week

Economic Data	Date	Period	Forecast	Previous
House Price Index	22 Sept	June Quarter	+2.3%	+1.6%
DEER Internet Vacancies Index	23 Sept	August	n/a	+0.1%

ECONOMIC COMMENTARY

LAST WEEK

The release of the minutes from the Reserve Bank's September meeting were overshadowed by events in Canberra last week, with Australia's 29th Prime Minister, Malcolm Turnbull sworn in at Government House. Events out of Asia dominated the RBA minutes, including a detailed course of events in the Chinese equity and currency markets and the subsequent interventions elsewhere in Asia. The RBA Governor Steven's testimony to the House of Representatives Economics Committee on Friday did not contain any new variation to recent RBA forecasts. Comments on the economy were mixed, with good and bad elements – a CAPEX decline and falling investment lending growth (a sign that APRA policies were working?) were specifically mentioned. Local financial markets were a little confused, with share markets taking cues from the softer Chinese data and the Australian dollar stabilising after its recent drop.

Offshore, the focus was on the US Federal Reserve meeting and the interest rate decision. The time arrived (Friday morning our time) but the Fed just couldn't bring itself to raise US rates for the first time in almost a decade. They cited continued uncertainty and recent volatility in global markets (China) as the reason for the delay but added that this was a postponement of a rate hike, not a cancellation and they were still on track to raise rates "at some point this year". Markets reacted as expected with equities and bond yields rallying while the US dollar was lower.

By the close of trading on Friday, the 90-day bank bill was trading unchanged over the week at 2.18% while in the long term maturities, 3 and 10 year bond yields closed at 1.94% and 2.78% respectively, from 1.89% and 2.74% a week earlier.

CURRENCY

Although drifting higher over the course of last week, the Australian dollar has seen wild action in the wake of the decision from the US Federal Reserve to keep rates at record lows. The initial reaction pushed the local unit as high as USD0.7277 (a three-week high) before gains were reversed as investors concluded the outcome of the Fed meeting was not far removed from what was expected. Traders were also concerned that the accompanying statement from the Fed only added to the uncertainty, which hurt growth-oriented currencies such as the Australian dollar.

By the close on Friday the Australian dollar was trading at USD0.7223 compared to USD0.7056 a week earlier.

EQUITIES

Global equity markets started the week with a positive but tentative tone, with investors reluctant to take on large positions ahead of the Fed meeting later in the week. Despite some falls on Chinese equity markets early last week, our local share market etched out some small gains early in the week.

The decision by the US Fed to delay raising interest rates only temporarily boosted equity markets and our market lost ground last Friday to close on a weak note. The reaction probably reflected the signal that a rate rise was still likely to occur later this year or investors were spooked by the lift in global growth concerns by the US Fed.

By the close on Friday the S&P/ASX200 Index had, trading at 5,170.5 compared to 5,071.1 a week earlier.

THIS WEEK

Another quiet week ahead for economic data releases, with June quarter established house prices the only significant release this week. The data should post another solid increase as the quarter pre-dates the imposition of higher interest rates for investor loans by the major banks, which occurred towards the end of July.

INTEREST RATE VIEW

The RBA retains in a "neutral" stance (rates on hold for some time), meaning that the next move in rates could go either way, however if rates were to move in the next six months, it would be most likely be down (hence the easing bias currently priced into financial futures markets). It appears that the official cash rate is likely to remain at 2% for some time, although the risk remains to the downside in the event of any unexpected market shocks, also noting that it will be "quite some time" before the RBA thinks about interest rates going up.

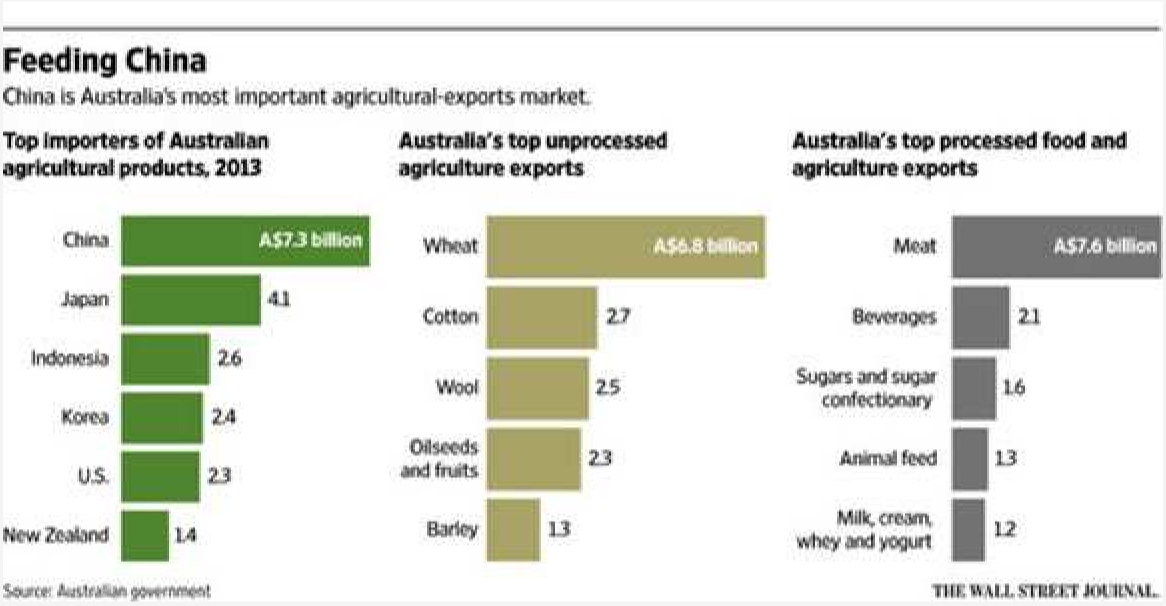
Economic Data	12 months ago	6 months ago	3 months ago	1 month ago	Now
Official Cash Rate	2.50	2.25	2.00	2.00	2.00
90 day Bank Bill	2.65	2.28	2.14	2.14	2.18
180 day Bank Bill	2.72	2.33	2.25	2.24	2.26
1 year swap	2.71	2.09	2.06	2.04	2.06
3 year swap	3.07	2.10	2.20	2.16	2.14
5 year swap	3.50	2.39	2.65	2.52	2.53
10 year swap	4.05	2.79	3.27	3.02	3.08
AUD/USD	0.8956	0.7678	0.7761	0.7304	0.7223
S&P/ASX200 Index	5,433.1	5,975.5	5,597.0	5,288.6	5,170.5

CHART OF THE WEEK

This week's chart shows the significance of the Chinese market to Australian agricultural exports.

Chinese consumers perceive food produced in Australia's to be three times as safe as food grown in China, and 50% healthier than food grown in the U.S., Brazil or France.

As a result, the demand - from consumers who can afford quality products, such as China's growing middle class - for Australian food is growing.



Source: http://goo.gl/Z175YI

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