WEEKLY ECONOMIC COMMENTARY

Week beginning 23rd November 2015

ECONOMIC DATA ROUNDUP

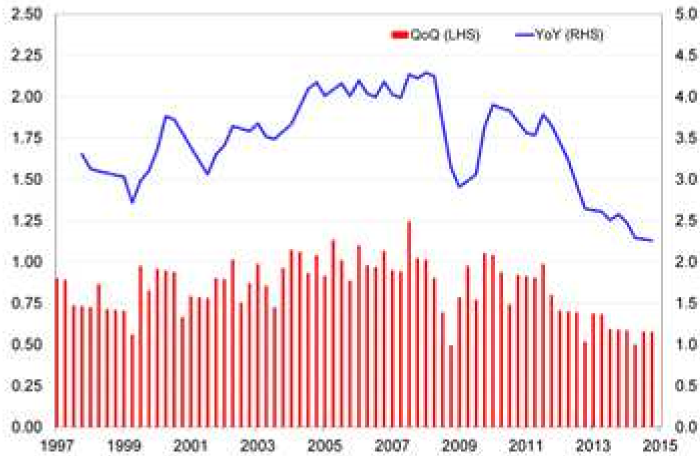
DATA RELEASED LAST WEEK

Economic Data	Period	Actual	Previous
New Motor Vehicle Sales	October	-3.6%	+5.5%
Wage Price Index	Sept Quarter	+0.6%	+0.6%

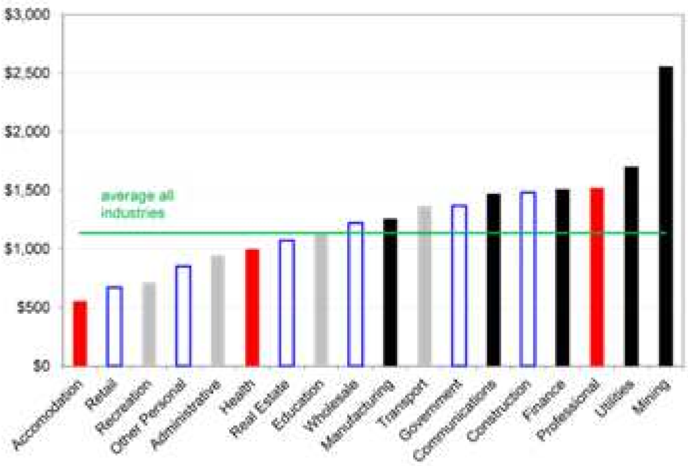
New motor vehicle sales fell 3.6% in October to be up 4.2% over the year. Sales of ‘passenger and other vehicles’ decreased by 0.1% and 0.5% respectively while sales of ‘sports utility vehicles’ increased by 1.5%. Seven of the eight states and territories experienced an increase in sales this month with the Australian Capital Territory recording the largest percentage increase (+1.6%), followed by South Australia (+0.7%) and New South Wales (+0.6%), while the Northern Territory was the only state to record a decrease in sales (-1.4%).

The **Wage Price Index** was up 0.6% in the September quarter to be up just 2.3% annually, the weakest year-on-year rise over the history of the index (back to late 1990’s). The bulk of the labour market comes from the private sector where wages growth was steady at 0.5% in the quarter and +2.1% annually, also a fresh record low. Relatively low paid industries such as ‘accommodation and food services’, ‘other services’, ‘arts and recreation services’ and ‘health care and social assistance’ all saw increases in wages of more than 1% over the quarter. On the other hand, the weakest outturn was for mining, with a rise of just 0.4% in the quarter.

Wage Price Index



Average weekly earnings by industry



The minutes of the November Reserve Bank Board meeting were released last week but gave no additional insight into their decision to leave the cash rate unchanged in November. The minutes repeat comments made earlier in the Governor’s statement and the Statement on Monetary Policy that low inflation provides scope to ease policy further if needed, but that “prospects for an improvement in economic conditions had firmed a little over recent months.”

Since the November Board meeting, the October employment data was stronger than expected but the global backdrop remains uncertain, including soft data out of China, Japan falling back into recession, the terrorist attacks in Paris, mixed data out of the US and continued weak commodity prices. While the risk to rates remains on the downside given the recent low inflation data and the rise in bank lending rates, the hurdle for a further RBA rate cut remains high.

In other news, the Westpac-Melbourne Institute Leading Index, which indicates the likely pace of economic activity three to nine months into the future, lifted to negative 0.08% in October, up from negative 0.3% in September. Westpac claim the Australian economy is set for a marked improvement next year, thanks to a lift in household spending and net exports.

Data over the next week

Economic Data	Date	Period	Forecast	Previous
DEER Internet Vacancies Index	25 Nov	October	n/a	+1.8%
Construction Work Done	25 Nov	Sept Quarter	-2.0%	+1.6%
Private Sector Capital Expenditure (CAPEX)	26 Nov	Sept Quarter	-2.9%	-4.0%

ECONOMIC COMMENTARY

LAST WEEK

Market reaction to last week's terror attacks in Paris have been consistent with recent history. Tragically, too many of these events have taken place in recent years, and as such, the market reaction has become less pronounced. Following an initial flight to safety last Monday, markets have remained reasonably calm with minimal response and, barring any extended impact on confidence or a slowdown in growth, the impact is likely to be only temporary. The resultant flight to quality knee-jerk buying of government bonds and US dollar was short-lived and markets returned to a form of normality by mid-week.

Offshore, the minutes of the US Federal Reserve November meeting were released last week and noted "most members felt it could well be appropriate to hike rates at the next meeting" which increased the probability of a US rate lift off on 16 December higher. Sentiment was helped by the Fed adding that the pace of any eventual rate hikes would be "very gradual" which was well received by markets.

The minutes of the November board meeting revealed that the RBA remains optimistic about the outlook for the economy but has left the door open to cut interest rates further if economic growth slows. Markets focused on the slight improvement in economic conditions, unwinding future expectations of rate cuts here in Australia.

By the close of trading on Friday, the 90-day bank bill was trading at 2.25% from 2.24% a week earlier while in the long term maturities, 3 and 10 year bond yields closed at 2.14% and 2.91% respectively, from 2.15% and 2.96% a week earlier.

CURRENCY

Despite the flight to US dollars early in the week, the Australian dollar has remained resilient, holding up on the cross rates despite a firmer US dollar and softer commodity prices. Our currency surprisingly found support after the release of the RBA board minutes although they contained nothing new relative to the post-meeting RBA statement or the following Statement on Monetary policy. It appears there is a lot of negative news already factored into the Australian dollar so any further sell-off is limited. The currency traded in a range between USD0.71 and USD0.72 for most of the week.

By the close on Friday, the Australian dollar was trading at USD0.7202 compared to USD0.7123 a week earlier.

EQUITIES

Immediate reaction to the terrorist attacks in Paris saw global equity markets sell off last Monday as investors switched to the safe haven of government bonds. The reaction saw the index fall below the psychological 5,000 level on the open last Monday but the sell-off was short-lived as confidence returned and share markets bounced. Commodities remained soft with copper down 2.6% last week to a six-year low, oil down below $40 per barrel and iron ore down 4% to $45 (a fresh multi-month low) as traders continued to fret about Chinese demand. Despite the dismal performance of commodities last week, the prospect of higher US rates buoyed investor sentiment, which pushed our share market over 4% higher since closing a fraction above 5,000 points on Monday.

By the close on Friday the S&P/ASX200 Index was trading at 5,256.1 compared to 5,051.3 a week earlier.

THIS WEEK

Data this week see the release of the first partial indicators that feed into the upcoming September quarter economic growth (GDP) data. Unfortunately both construction work done and private capital expenditure are going to print a negative number for the quarter with an expected slowdown in engineering and non-residential building work done driving the results.

INTEREST RATE VIEW

In a speech over the weekend, European central bank president Mario Draghi said that the ECB would do what it takes to raise inflation, setting the scene for the announcement of more quantitative easing in Europe in early December. This is in contrast to the US where there is a 70% probability of a rate hike in December. Locally, our market is unwinding the probability of future rate cuts with less than a 10% probability of a cut in December and a terminal (low) cash rate of 1.85% by June 2016.

Economic Data	12 months ago	6 months ago	3 months ago	1 month ago	Now
Official Cash Rate	2.50	2.00	2.00	2.00	2.00
90 day Bank Bill	2.74	2.13	2.14	2.16	2.25
180 day Bank Bill	2.82	2.25	2.24	2.23	2.36
1 year swap	2.71	2.10	2.04	1.96	2.15
3 year swap	2.81	2.27	2.16	2.03	2.25
5 year swap	3.15	2.67	2.52	2.40	2.60
10 year swap	3.67	3.21	3.02	2.91	3.07
AUD/USD	0.8624	0.7924	0.7307	0.7207	0.7202
S&P/ASX200 Index	5,304.3	5,664.7	5,214.6	5,263.8	5,256.1

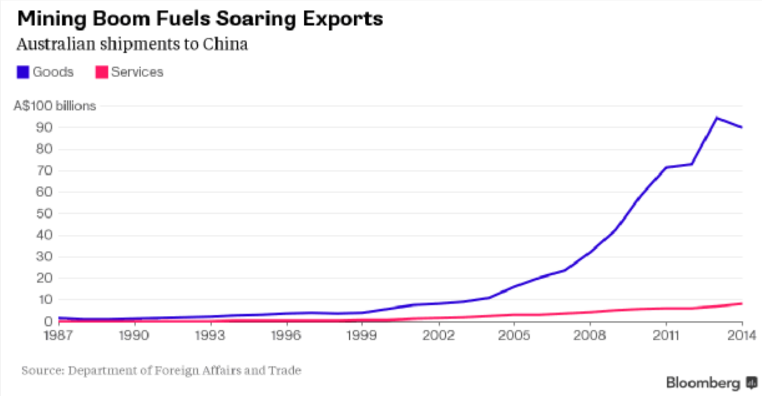
CHART OF THE WEEK

Australia's Exports to China Seen Doubling as Middle Class Grows

Source: Bloomberg - By Iain McDonald 20 October 2015 - China's shift toward consumption could see Australia's exports to the world's second-largest economy double by 2030, even as growth in key commodity sales stalls.

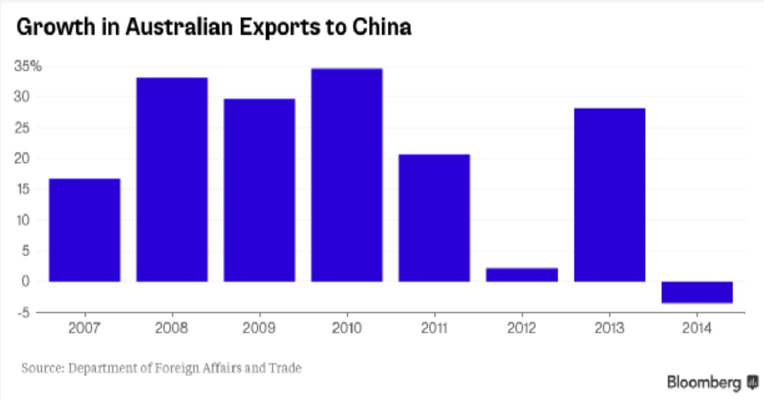
Services and agriculture exports to China will grow 10% annually, while coal and iron ore exports stagnate, according to economists at Australia & New Zealand Banking Group Ltd.

"In particular, the tourism and education sectors can expect strong growth as more Chinese citizens travel to Australia for leisure and study," the ANZ economists said. "As a result of emerging opportunities like these, we project that Australia’s exports to China will almost double by 2030 but the transition could be a bumpy one."



Forecasts like these will be welcome news for Australians, who are wondering where the next wave of economic growth will come from after prices for the country's biggest commodity exports tumbled.

Australia rode a mining investment boom for a decade, driven largely by China's fast growing demand for raw materials. But as construction in China slows, so does that demand, causing the value of goods and services exports to China to fall in 2014 for the first time in 16 years.



ANZ says a further 300 million new middle-class consumers will emerge in China's urban areas by 2030 and spending by the middle class should more than double, lifting consumption as a proportion of the economy's annual output to nearly 50% from 38% last year.

Consumption contributed nearly 60% of China's growth in the first nine months of the year, according to data released on Monday 19th October showing the country's economy grew 6.9% in the third quarter from a year earlier.

Growth in the value of Chinese visits to Australia will grow more strongly in the next few years with the tripling of airline capacity between the two countries, ANZ says.

"While Australia’s commodities will still be needed for China’s growing housing, infrastructure and energy markets, Australia needs to adapt to China’s new growth model by moving towards service exports, as well as opportunities in agriculture and manufacturing," ANZ Chief Economist Warren Hogan said.

Still, Australia's efforts to boost such exports to China haven't always run smoothly.

Insurance Australia Group, one of the country's largest insurers, said last week that it had abandoned plans to boost its business in China. “After completing significant work on assessing the opportunities available, IAG has determined not to pursue further investment in China,” Chief Executive Officer Mike Wilkins said, without giving any further reason for the decision.

Questions have also been raised as to Australia's ability to continue attracting more Chinese visitors as much of the country's tourist infrastructure is tired and outdated.

As ANZ says, China's swing toward more consumption presents some challenges as well as opportunities.

About Rural Bank and Rural Finance

Rural Bank has been a wholly-owned subsidiary of Bendigo and Adelaide Bank Limited since 2010 and is the only Australian-owned and operated dedicated agribusiness bank in the country.

From 1 July 2014, Victorian agribusiness lender, Rural Finance joined Rural Bank as a division of Bendigo and Adelaide Bank Limited. As a specialist rural lender, Rural Finance has been fostering the sustainable economic growth of rural and regional Victoria for more than 65 years.

Together, Rural Bank and Rural Finance are supporting farmers and farming communities by providing them with specialist financial tools, industry insights and investment into the future of the Australian agribusiness sector.

Rural Bank's specialist farm finance tools are available nationally via a network of banking partners, including Bendigo Bank and Community Bank® branches and Elders Rural Services. Additionally, Rural Finance has a network of offices across regional Victoria.

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