WEEKLY ECONOMIC COMMENTARY

Week beginning 9th December 2013

ECONOMIC DATA ROUNDUP

DATA RELEASED LAST WEEK

Economic Data	Period	Actual	Previous
Building Approvals	October	-1.8%	+14.4%
Balance of Payments	Sept Quarter	-$12.7bn	-$9.4bn
Retail Sales	October	+0.5%	+0.8%
GDP	Sept Quarter	+0.6%	+0.7%
International Trade Balance	October	-$529m	-$284m

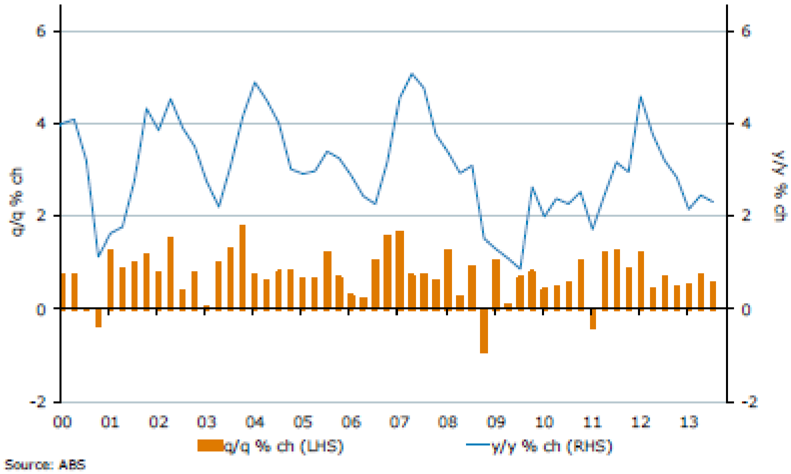
Residential **building approvals** declined by 1.8% in October but followed a large spike in September which was revised up to 16.9%, to be up 23.1% annually. The last two months' approvals combined were the highest for any two-month period since 1994. The weakness this month was concentrated in multi-dwellings (i.e. "private sector dwellings excluding houses") which fell 2.7% following an upwardly revised rise of 37.4% in September. Private sector houses fell by 0.3% following a 1.3% rise in September.

The **Balance of Payments** printed a slightly larger current account deficit than expected at $12.7bn in the September quarter (or 3.3% of GDP). The trade balance narrowed marginally to -$2.6bn in the quarter from -$2.7bn previously. The result was driven by a small rise in exports (+0.3%) and a fall in goods import volumes (-3.3%), although a sharp rise in import prices partly mitigated the weakness in import volumes.

Retail sales were stronger than expected rising 0.5% in October to be up 3.6% annually. The Australian Bureau of Statistics has flagged it made some significant changes to the composition of the retail sales data this month so comparisons are not available. The data is consistent with a general improvement in consumer confidence and retail sector anecdotes that suggest retail sales activity is improving.

Gross Domestic Product (GDP) was slightly lower than expected for the September quarter, rising 0.6% to bring annual growth to +2.3%. The expenditure measure of GDP rose 0.6% (+2.2% annually) which was weaker than expected (largely due to a smaller than expected rise in business investment). The income measure rose 0.6% (+2.5% annually) also weaker than expected while the production measure of GDP was up 0.5% (+2.3% annually). Out of the 19 broad industry sectors, 10 reported positive growth while 9 were negative in the quarter. The strongest growth industries include arts and recreation services (+3.5%), other services (+3.3%), mining (+2.7%), transport, postal and warehousing (+1.4%), public administration and safety (+1.2%), and construction (+1.1%). The sectors reporting negative growth were wholesale trade (-2.9%), and agriculture, forestry and fishing (-2.2%).

GDP Growth



The **Trade Balance** for October posted a deficit of $529m. Exports fell 0.1%, with iron ore exports down, but this was partially offset by a 7.4% rise in coal exports. Imports rose 0.8% driven by a 9.1% rise in fuels and lubricants imports.

Data over the next week

Economic Data	Date	Period	Forecast	Previous
ANZ Job Ads	9 Dec	November	n/a	-0.1%
Housing Finance	10 Dec	October	+0.5%	+4.4%
NAB Business Confidence	10 Dec	November	n/a	+5.0
Westpac Consumer Confidence	11 Dec	December	n/a	+1.9%
Employment	12 Dec	November	+12,000	+1,100
Unemployment	12 Dec	November	5.8%	5.7%

ECONOMIC COMMENTARY

LAST WEEK

As was widely expected, the Reserve Bank of Australia again left the official cash rate unchanged after their monthly Board meeting last week, with only minor changes to their post-meeting statement. Monetary policy bias remains unchanged and retains an easing bias, but only slightly, with comments that the Australian Dollar remains “uncomfortably high” despite the Australian Dollar falling around 3 to 4 cents since the November Board meeting

Speculation over the proposed timing of the winding back of the US Federal Reserve’s asset purchase program continued to drive market direction last week, with stronger than expected US economic data fuelling expectations for an earlier start to “tapering”.

The moves in offshore markets impacted our market which saw yields push higher while equities and the currency fell.

By the close of trading on Friday, the 90-day bank bill was trading at 2.60% compared to 2.61% a week earlier. At the long end, 3 and 10 year bond yields closed higher at 3.14% and 4.44% from 3.06% and 4.23% a week earlier.

CURRENCY

The Australian Dollar sold off last week and is trading near a three-month low after some positive US economic data fuelled speculation that the US Federal Reserve may begin tapering their stimulus package as early as this month, sending the US Dollar higher against the cross rates. Investors also reacted to the lower than expected third quarter GDP data pushing back forecasts of the first RBA rate hike next year, which also hurt the currency.

By the close on Friday, the AUD was trading at USD0.9047 having briefly traded below USD0.90 last Wednesday, compared to USD0.9096 a week earlier.

EQUITIES

A negative lead from Wall Street (on good US data and associated tapering fears) and weak local economic data releases saw our share market close lower last week despite higher commodity prices, which supported our miners. The index was weighed down by a weak financial sector as well as a warning of a first-half loss of up to $300m and flagging 1,000 job cuts from Qantas.

By the close on Friday the S&P/ASX200 Index was trading at 5,186.0 compared to 5,320.1 a week earlier.

THIS WEEK

The last major economic data announcements for the year will be released this week. Releases include the latest monthly jobs numbers, with November ANZ Job Ads out on Monday and the ABS employment data out on Thursday. Despite a small increase in the number employed, the unemployment rate is expected to tick up to 5.8%.

We also get the next month of sentiment data this week where analysts are expecting to see some weakness in business confidence following the large bounce in the months around the Federal election.

INTEREST RATE VIEW

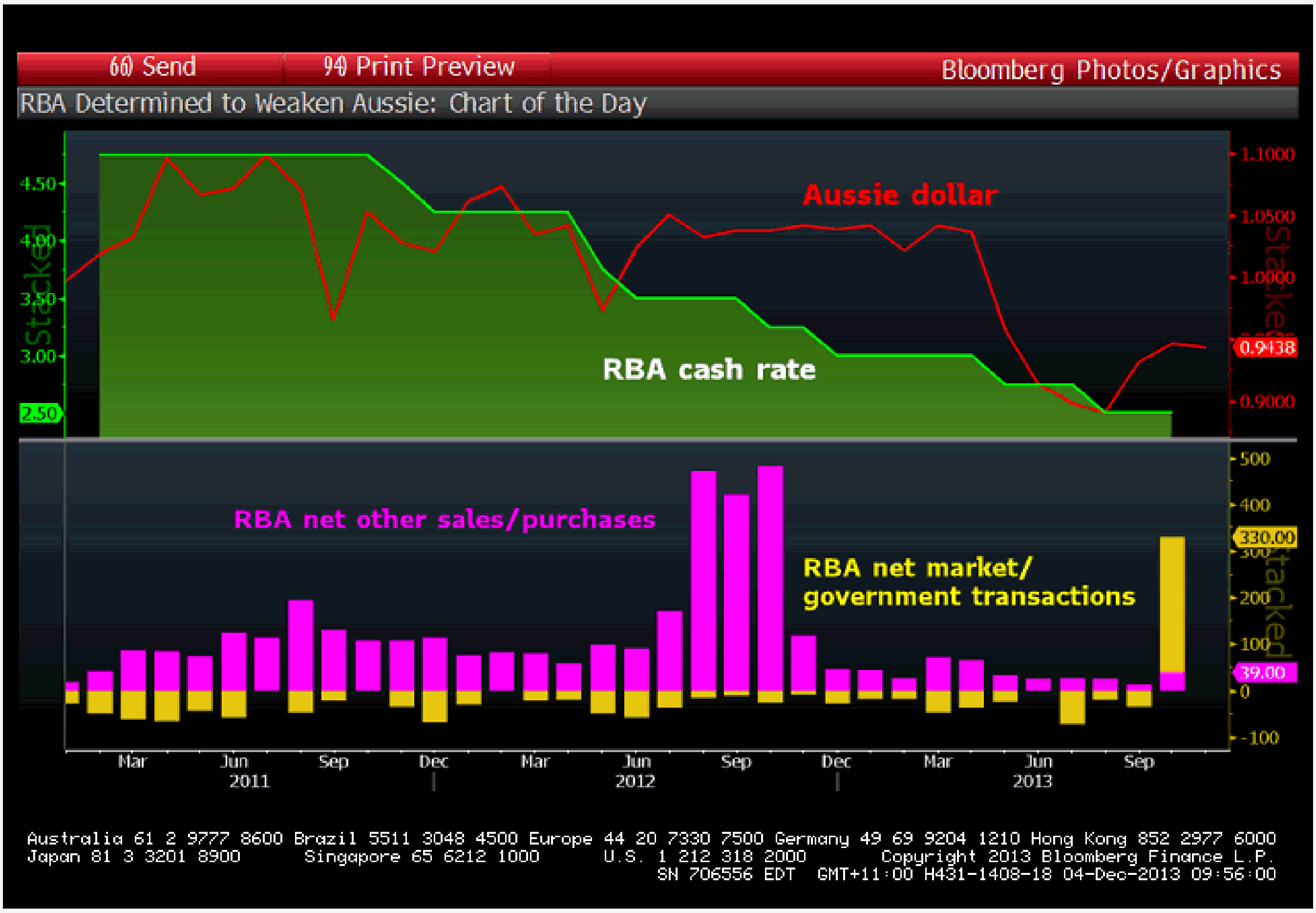
Rates are on hold for now, at least until early February when the Reserve Bank Board next meets, but an easing bias remains, albeit very slightly. All the talk at the moment is whether the US Federal Reserve will begin its tapering of the bond buying program at its next meeting which is scheduled for 17th and 18th December.

Markets retain a 20% probability of a rate cut early next year but currently have an 80% chance of a rate hike by the end of 2014.

Economic Data	12 months ago	6 months ago	3 months ago	1 month ago	Now
Official Cash Rate	3.00	2.75	2.50	2.50	2.50
90 day Bank Bill	3.11	2.80	2.59	2.58	2.60
180 day Bank Bill	3.08	2.74	2.61	2.61	2.62
1 year swap	3.02	2.73	2.75	2.76	2.74
3 year swap	3.16	2.96	3.45	3.35	3.38
5 year swap	3.44	3.37	4.04	3.89	3.99
10 year swap	3.87	4.01	4.79	4.64	4.86
AUD/USD	1.0477	0.9495	0.9140	0.9467	0.9047
S&P/ASX200 Index	4,551.8	4,737.7	5,145.0	5,400.7	5,186.0

CHART OF THE WEEK

(Source – Bloomberg, 3rd December by Kevin Buckland and Hiroko Komiya): The Reserve Bank of Australia is putting its money where Governor Glenn Stevens' mouth has been, backing his call that the "uncomfortably high" Aussie will weaken. History shows it's not wise to bet against it. The chart below shows the Australian dollar heading for its steepest annual decline since 2008 after the central bank cut benchmark borrowing costs to a record.



The bottom panel shows the RBA sold a net $330 million of its currency in the open market in October as it rebounded. That was the most aggressive selling since a net $1.4 billion in transactions over the three months to October 2012, when policy makers also deemed the Aussie to be "on the high side." "They took a decision to maintain their exposure in foreign currency, effectively ensuring they keep their short position in Aussie," said Sean Keane, at Triple T Consulting. "It amounts to the RBA putting its money where its mouth is, and they're probably the most successful central bank in the world in terms of managing their foreign currency exposure."

Policy makers held the benchmark interest rate unchanged today for a fourth month and reiterated a lower Aussie would help the economy as a mining investment boom winds down. Stevens said in a speech last month "the Australian dollar is currently above levels we would expect to see in the medium term." The Aussie will fall to 89 US cents by end-2014, the median forecast of analysts surveyed by Bloomberg shows.

It was buying around 90.86 US cents in Sydney. The Aussie averaged $1.04 while the Reserve Bank was selling it between August to October 2012, as it spent a record 10 months above parity, before slumping to a three-year low of 88.48 U.S. cents in August of this year.

The central bank bought large quantities of Australian dollars during the financial crisis that started in 2008 as the currency nose-dived to 60 U.S. cents - trades that were ultimately "very profitable," according to Assistant Governor Guy Debelle.

Australia Set for Third-Largest Wheat Crop Boosting Supplies

December 3 (Bloomberg by Phoebe Sedgman) -- Australia increased its wheat crop estimate to the third-biggest on record as the harvest in the west of the country offsets frost damage in the east, adding to global production that's already at an all-time high.

Farmers may reap 26.2 million metric tons from 24.5 million tons estimated in September and 22.5 million tons a year earlier, the Australian Bureau of Agricultural and Resource Economics and Sciences said in a report today. Growers in Western Australia, the largest producing state, will gather 9.6 million tons from 7.3 million tons seen in September, it said. The country is the world's third-largest shipper.

Wheat tumbled 15% this year as corn slumped 39% and soybeans lost 6% on expectations global output of the crops will reach records. Increasing global supplies will pressure crop prices through year-end, according to HSBC Holdings Plc. Lower prices may cut the world's food-import bill by 3.2% to $1.15 trillion this year, according to the United Nations' Food & Agriculture Organization.

"The South Australian and Western Australian crops are beautiful," said Michael Pitts, a commodity sales director at National Australia Bank Ltd. in Sydney. Production of lower protein, softer varieties of wheat will increase and "Australia will be selling that pretty aggressively to Asia and the Middle East," he said by phone today.

Wheat for March delivery added 0.2 percent to $6.63 a bushel on the Chicago Board of Trade at 5:32 p.m. in Singapore today. New South Wales milling wheat futures for January delivery gained as much as 1 percent to A$298 ($270) a ton as ABARES reduced its production estimate for the state.

Frost Damage

Global wheat production will increase 7.8% to 706.4 million tons as output in Canada climbs 22% and Russia's harvest surges 37%, the US Department of Agriculture estimates. The ABARES estimate compares with 25.5 million tons forecast by the USDA last month.

"Generally favorable conditions and timely rainfall during spring increased prospective yields, particularly in southern and central Western Australia," said Canberra-based ABARES. Crops in southern Queensland and northern New South Wales were hurt by frost in August, while some in New South Wales suffered "significant" frost damage in October, it said.

New South Wales, set to be the second-biggest producer, will harvest 6.7 million tons from 7.2 million tons estimated in September. ABARES lowered its estimate for area planted to wheat in Australia to 13.5 million hectares (33.4 million acres) from 13.7 million hectares seen in September.

Canola production may reach 3.4 million tons from 3.3 million tons predicted in September, it said. Barley output may total 8.6 million tons from an estimate of 7.7 million tons, while cotton production may be 975,000 tons from 990,000 tons seen in September.

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