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FROM THE EDITOR – the state of the economy

The past month has seen both very good news and some indications of disturbing news that could still have a negative impact on the economic conditions going forward.

Clearly, the most upbeat economic news has been the fact that Australia has avoided a technical recession and grew by 0.6% in the last quarter coupled with the continued strong rebound in business and consumer confidence. Economists are treating the increases in confidence with trepidation - the economy is still probably facing a period of sluggish economic growth with the result that the high levels of confidence is unlikely to be maintained.

David Bassanese, *Australian Financial Review* economist, is of the opinion that both consumers and companies have expressed a loud sigh of relief that a wrenching downturn has most likely been avoided, but perhaps do not fully appreciate the hard slog ahead.

Some economists are of the view that we are going through a period of 'premature optimism'.

Latest unemployment figures, whilst static at 5.8%, mask the loss of 30,000 jobs last month and it is being held down by surging underemployment – the proportion of employees who want more work has climbed to a record high of 7.5% - and is also growing by the number of job seekers becoming discouraged and dropping out of the hunt for work. Economists predict that unemployment will rise to 6.75%.

There has also been some cooling in housing demand and retail sales, which were both expected as the effects of the stimulus wear off. Retail spending fell for the second consecutive month in July, while demand for home loans eased for the first time in 10 months.

Australia's terms of trade – what we export versus what we import – has deteriorated markedly in the June quarter posing a major risk to the economy.

After last week's surprise rise in economic growth for the June quarter, economists were predicting between 2 – 3 interest rate hikes between now and December. But, with economic figures no longer lining up, economists are now predicting a small interest rate hike in December.

Quote of the week:

"From a labour market perspective, the recession has a long way to go. Everyone can be

optimistic about gross domestic product (GDP) and the stockmarket but things will continue to get worse in the job market.” Bob Gregory, Australian National University economist.

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AUSTRALIAN ECONOMY

Consumers upbeat but spend less

Shoppers are winding down their spending despite consumer confidence hitting its highest level in more than two years, in a sign that the effect of federal government handouts on household demand is fading.

The Westpac-Melbourne Institute consumer sentiment index jumped by 5.2% this month to reach 119.3 points, its highest mark since July 2007.

Despite the high confidence, shop turnover fell 1% in July. Retailers across the country have indicated that July’s weakening sales have continued into August. Prominent retailer Bob Swyers commented: “We got a kick along from the cash handouts but now people are saying they don’t have money to spend.”

Adrian Rollins, *The Australian Financial Review* – 10 September

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Short term concern for retail

The outlook is bright for Australian retailers but they may have to wait more than a year to realise the benefits.

Access Economics state that the next 18 months are still expected to be tough for the retail sector. Whilst the retail sector has performed well to date, Access are of the opinion that it will get harder for Australian families to sustain this spending effort from here on in.

The cash handouts are beginning to fade, interest rates are more likely to rise, and the labour market is still set to weaken. This will place a damper on current confidence.

Stefanie Balogh, *The Courier Mail* – 9 September

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Six-year high for business confidence

Business confidence has surged to a 6 year high as evidence that the nation has dodged a deep downturn buoys the mood of employers.

However, the brighter outlook is yet to translate into activity and companies are proving reluctant to place orders or dust off expansion plans, in a sign that many are cautious about the strength and duration of the recovery.

Adrian Rollins, *The Australian Financial Review* – 11 September.

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Optimism ‘premature’ beware coming crunch

Australia’s economy faces another downturn before staging a strong recovery in 2011, a leading analyst predicted this week.

Forecasting firm BIS Shrapnel said Federal Government stimulus spending had created ‘premature optimism’ about the economy, which would head south again because of a credit crunch through next year.

Funds availability to finance investment will be a key issue going forward.

Anthony Marx, *The Courier Mail* – 9 September

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Poor terms of trade

Australia’s terms of trade – what we export versus what we import – has deteriorated markedly in the June quarter – largely due to lower commodity prices and increased imports driven by consumer

demand for electronic products.

The poor terms of trade can derail Australia's economic recovery.

Paul Syvert, *The Courier Mail* – 2 September

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Interest rate increase – when?

The first batch of local economic data leading into the next Reserve Bank board meeting has presented relatively mixed news on the economy. On balance, however, the simmering chance of an October rate increase has weakened, though a rate rise by December still seems quite possible.

David Bassanese, *The Australian Financial Review* – 11 September.

ANZ chief executive Mike Smith has issued a stern warning to fellow bankers considering raising interest rates, saying it would be 'crazy' to move too soon and risk Australia's economic recovery.

Pia Akerman, *The Australian* – 3 September

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EMPLOYMENT

Job losses cloud rosy picture

Employers are holding onto staff but continue to cut work hours as they draw on the benefits of the federal government's cash splash and hopes of a recovery to limit lay-offs.

The national jobless rate was steady at 5.8% last month and has barely budged for five months, but it is being held down by surging underemployment – the proportion of employees who want more work has climbed to a record high of 7.5% - and is also growing by the number of job seekers becoming discouraged and dropping out of the hunt for work.

The economy shed more than 30,000 jobs last month.

Prime Minister Kevin Rudd was downbeat about the labour market warning of more pain ahead for job seekers and workers.

Adrian Rollins, *The Australian Financial Review* – 11 September.

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Growing line of long term unemployed

The number of unemployed whose search for work has stretched out for more than a year has begun to creep up as the labour market slips back into patterns set in previous downturns.

Emma Connors, *The Australian Financial Review* – 11 September.

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Jobless rate tipped to peak 6.75%

Gloomy government predictions for unemployment to peak at 8.5% in 2010/11 are unlikely to materialise after a recent stampede of positive economic indicators, economists say.

A median forecast of five economists surveyed by AAP was for unemployment to peak at 6.75% by 2010 following better-than-expected employment, consumer confidence and gross domestic product figures released in September.

AAP – 11 September.

Job vacancies rose for the first time in almost 18 months – according to ANZ Bank. But demand for workers remains weak job advertisements down almost 48% from last year.

Adrian Rollins, *The Australian Financial Review* – 8 September.

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PERSONAL FINANCE

Stocks defy September hoodoo

The sharemarket defied weaker than expected jobs data to soar to an 11 months high as investors ploughed into equities after latching onto a strong lead from Wall Street.

Argo Investments portfolio manager Christopher Hall said the strong gains are being questioned by investment managers, who were worried stock valuations were becoming stretched without further evidence of earnings growth.

Justin Bailey, *The Australian Financial Review* –11 September.

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One-third of nation at risk of loan default – Kuraby in risk category

One-third of the country – including battlers’ suburbs and some of the wealthiest urban areas – has entered the danger zone for financial distress, despite signs that economic conditions are improving.

Queensland suburbs at risk:

- Acacia Ridge (ranked 5)
- Boonah (ranked 6)
- Lawnton (ranked 7)
- Greenslopes (ranked 13)
- Kuraby (ranked 14)

Adele Ferguson, *The Australian* –7 September.

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