Business Insights

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THE STATE OF THE ECONOMY

Overall the Australian economy appears to be growing steadily although interest rate sensitive sectors such as retail and housing are battling. Retail sales, excluding cars, are still soft and building approvals are still dropping. Commodity prices continue to rise but concerns persist about the global economy, specifically the European economies and the strength of the Chinese economy.

These global concerns led to the Reserve Bank not increasing interest rates this month. Whilst further interest rate rises are still being predicted given the inflationary pressures in the Australian economy, a number of economists are now of the opinion that interest rates will remain on hold for at least the next quarter and some are predicting that they may in fact decline, given the soft nature of retail and housing.

With the continued growth in employment, economists are predicting a better second six months. The key to resuscitating the economy is to get consumers and businesses spending big again. The IMF forecasts that the Australian economy will grow by 3% in 2010 and 3.5% in 2011. Whilst the property market is not expected to do much in the next 6 – 12 months, economists are predicting a 27% increase in share values over today's prices by June next year.

This week's issue highlights the key features in the economy with a focus on housing and investment.

AUSTRIALIAN ECONOMY

Retail Outlook

Wesfarmers (owners of Bunnings, Coles, Target and Kmart) managing director Richard Goyder is of the opinion that consumers are cautious but they "haven't gone into hiding". "Retail conditions are OK but not good. Our expectation is that they [conditions] will stay like they are probably through to the end of the calendar year," he said.

Retail sales rose a modest 0.2% in May. Consumers continue to shy away from discretionary spending on household goods and retailers in NSW and Victoria were the only states to increase their turnover. JP Morgan Chase economist Ben Jarman said the May retail sales were "a fairly good result", given consumer confidence tanked, equity markets and the currency fell and extremely wet weather reduced foot traffic.

John Kehoe, *The Australian Financial Review* – 2 July.

Urbis are of the opinion that retail sales will improve. But while the retail market is expected to mend, it is doubtful it will return to pre-GFC boom conditions. "Growth conditions will improve in Australia in the second half of the year, but retailers should not expect an immediate return to the boom conditions that prevailed pre-2008 when it was not uncommon for annual growth to exceed 7%," Urbis state in their "Retailer Perspectives" report.

Lisa Carapiet, *The Australian Financial Review* – 9 July.

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Employment surge stokes inflation fears

The Australian dollar surged and the sharemarket rose on the news that full time jobs posted their 10th consecutive rise. The labour force figures published this week indicate the economy is rapidly approaching full employment, raising concerns about workers and unions pushing for excessive wage increases.

The Australian Financial Review – 9 July.

(Editor: As employment surges, the prospects for retail and housing improve, but this needs to be assessed against increasing inflation which will result in higher interest rates.).

Paul Syvert does not believe that reducing our jobless queue will be fast. He cites data that shows that both average hours worked and under-employment are still worse than before the world economy fell off a cliff. He believes that there is a lot of spare capacity in the workforce and that hours of work can be increased without the need to increase employment – based on the fact that hours worked are still lower than pre-GFC levels.

Paul Syvert, *The Courier Mail* – 9 July.

In Brisbane, youth unemployment remains stubbornly high in the outer suburbs.

John McCarthy, *The Courier Mail* – 9 July.

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HOUSING

House prices unlikely to plummet

Macquarie Bank has dismissed analyst's predictions of a plunge in house prices over the next 12 months but still expects them to soften. According to Macquarie, a combination of rapid population growth, strong labour market conditions and sustainable debt suggests the Australian housing market is built on solid foundations.

Macquarie's residential market prognosis, contained in its September quarter general economic outlook, said rising interest rates would soften the market over the next year but would not trigger a dramatic price correction.

Maurice Dunlevy, *The Weekend Australian* – 10-11 July

(Editor: The median house price in Brisbane has increased by 10.3% in the year to March, after dropping by 6.4% in the previous year. In March 08 the median price was $442,081, in March 09, $413,906 and in March 10, $456,687. Based on these numbers, in real terms, the property price has not done much since March 08.).

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Building approvals down

Building approvals have fallen 17% over the past two months and are at their lowest monthly level since October 2009. Housing Industry Association chief economist Harley Dale said that higher interest rates, together with obstinately large supply side constraints, were weighing down the new home building industry.

"The hikes in interest rates that we have already experienced are clearly biting, exacerbating ongoing difficulties with land supply, credit availability, and a range of other obstacles preventing a sustainable boost to Australia's new housing supply."

John Kehoe, *The Australian Financial Review* – 2 July

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Rents take breather after steady growth

Despite the widely held view that there are not enough homes, rents around the country are not going up. Figures by RP Data show that in the three months to June, rents for units rose only 1.4%, and there was no increase at all for houses.

Research analyst Cameron Kusher put the phenomenon down to last year's low interest rates and first home0buyer incentives, which spurred people to buy their own homes and took pressure off rental accommodation.

Chris Martin, senior policy officer at the tenants Union of NSW, said rents were unlikely to rise much further. He said more than a quarter of the rental market was in housing stress, defined as paying more than 30% of income as rent. That will put a brake on rent for a while as people will choose cramped conditions over spending more.

Ben Hurley, *The Australian Financial Review* – 8 July

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INVESTMENT

Cash is king for investors

The world is drowning in cash.

Global sharemarkets may have ended the week with a bounce but investors the globe over are still hoarding hard currency like there is no tomorrow. Macquarie's senior economist, Brian Redican, said the flight to cash was a natural reaction by investors seeking a safe heaven, particularly as markets around the world remained ultra-volatile.

Scott Murdoch, *The Weekend Australian* – 10-11 July

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Sharemarket still characterised by volatility....but with good prospects

Doubts about Europe, China and the global economy in general has resulted in the locak sharemarket losing 14% in value since hitting a high on April 15, 2010.

Economists continue to predict more volatility in the next six months. However, most economists are predicting a rally from early next year and are predicting an average increase of 27.8% in sharemarket values in the financial year 2011. For gutsy investors willing to take a risk, this may potentially be much better returns than property in the short term with the option of buying shares now and delaying property being an investment strategy that you should discuss with your financial advisor.

The Australian sharemarket is today 36% below its peak on November 1, 2007.

Editor. Information sourced from *The Australian Financial Review* Market Wrap – 2 July

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TAX

Fudging your revenue? Think again, says ATO

If you run a small business and you're not recording the revenue you should, the Australian Taxation Office has you in its sights. The consequences of under-reporting revenue can be severe. Expect jail time and a criminal record, and the tax office forever on your back. "We will crack down on businesses using cash transactions to hide income and evade tax, using benchmarks for more than 100 industries," said Tax Commissioner, Michael D'Ascenzo.

Alexander Cain, *The Age* – 9 July

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