



09

St. George Bank
**STATE OF THE REGION
SUMMIT**

Economic Trends

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Australian Economic Outlook: Potholes, Cracks & Crevasses?

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2 June, 2009

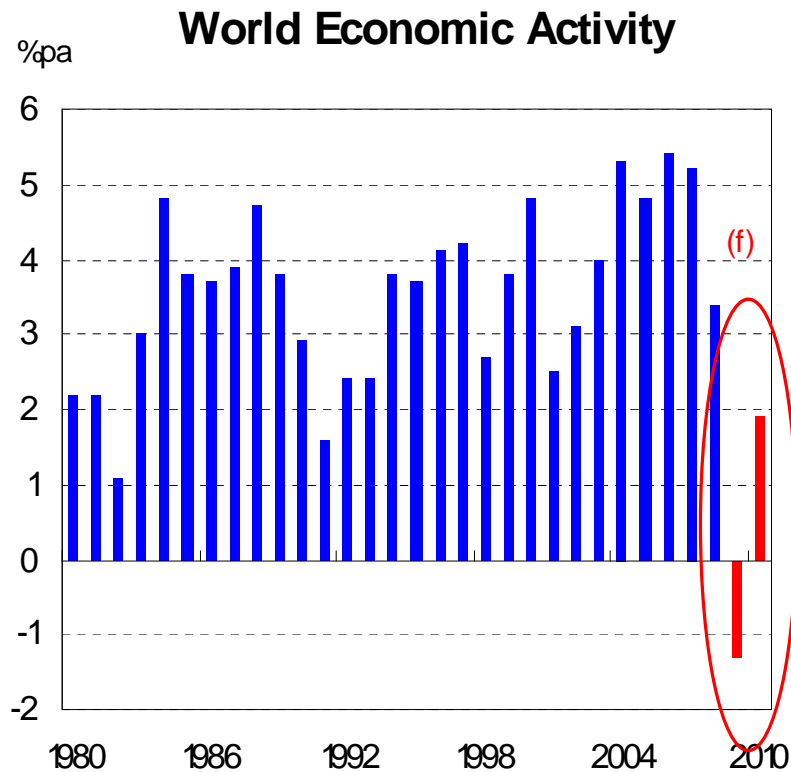
Institutional & Financial Markets



Road Map

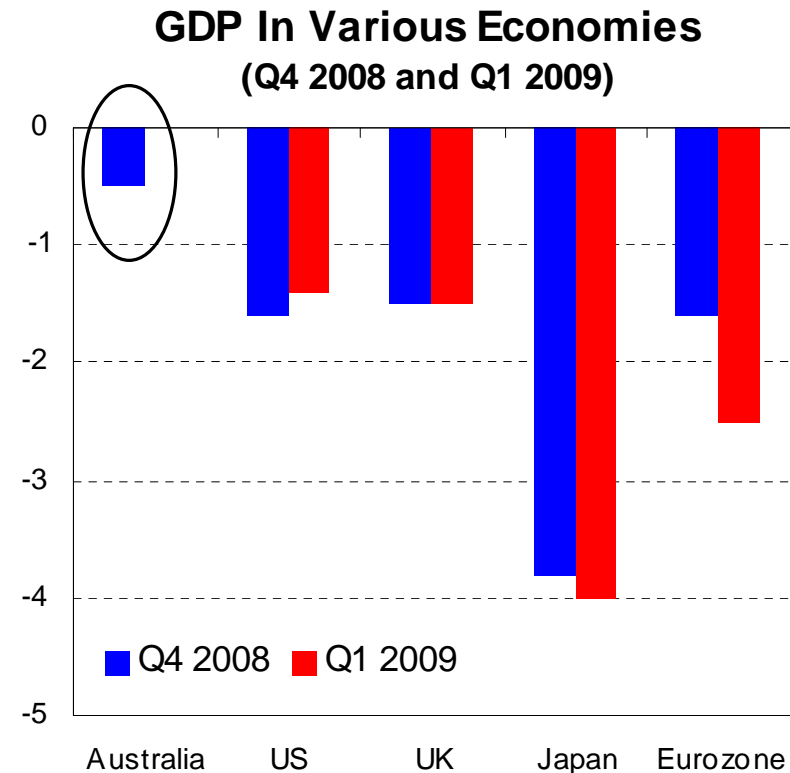
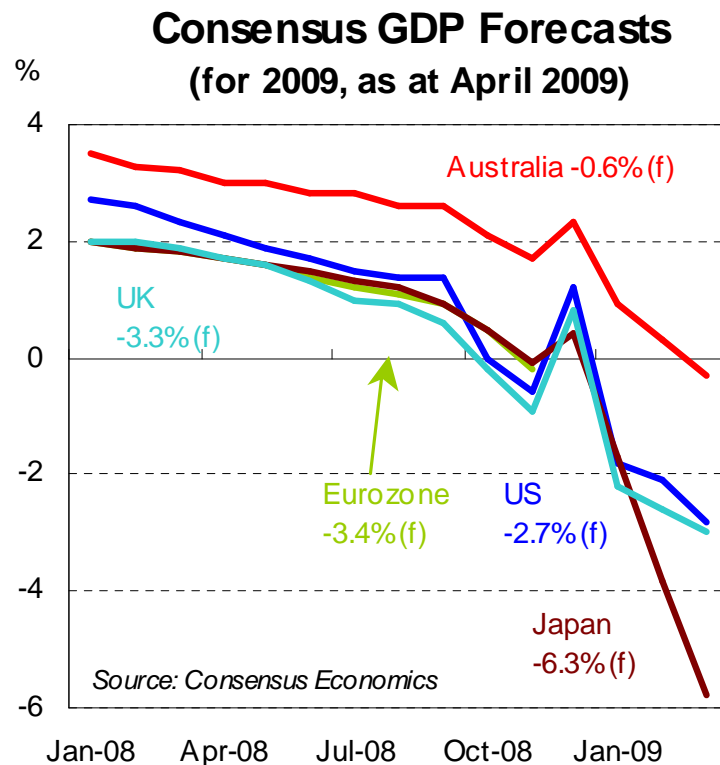
- **World economic outlook**
- **Domestic economic conditions**
- **Interest rate outlook**
- **Credit market developments**
- **Aussie dollar outlook**
- **Questions & answers session**

The World Economy Shifts Into Reverse Gear



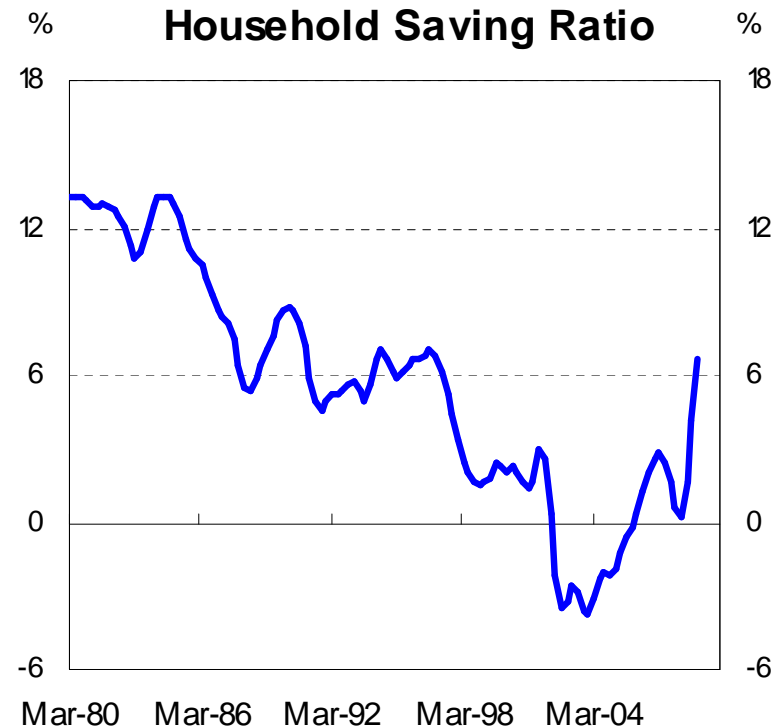
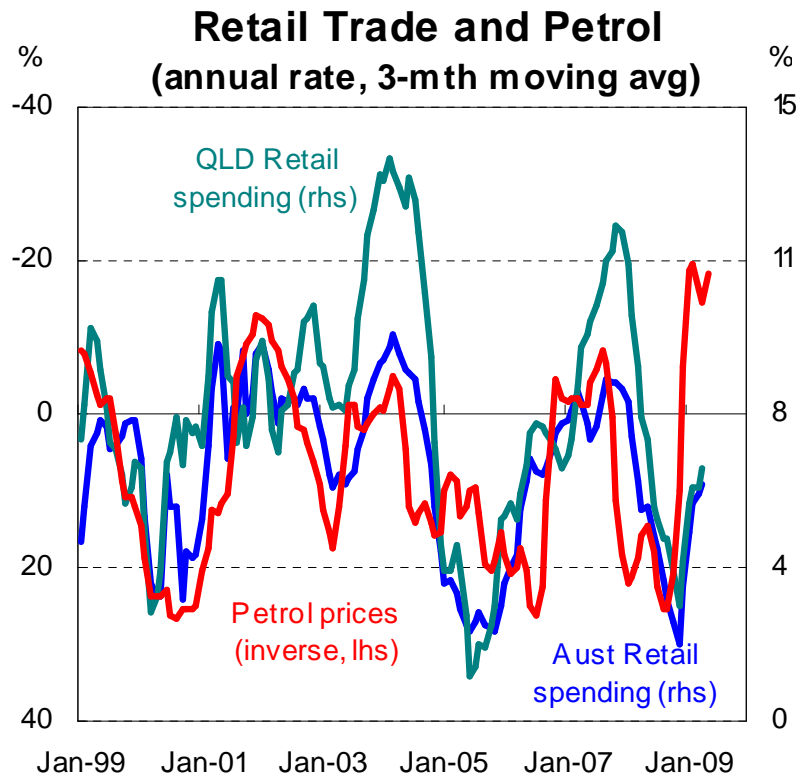
- The world economy is expected to contract this year by more than 1%, down from near 5% in 2007 and just over 3% in 2008.
- It will be the weakest downturn since at least WWII.
- Downturns caused by financial crises tend to be deeper and longer.

Australian Economy – Still Ahead of the Pack



- **Australia is sharing in the pain of the world economic downturn.**
- **But growth prospects are still more favourable in Australia than in other major economies around the world.**

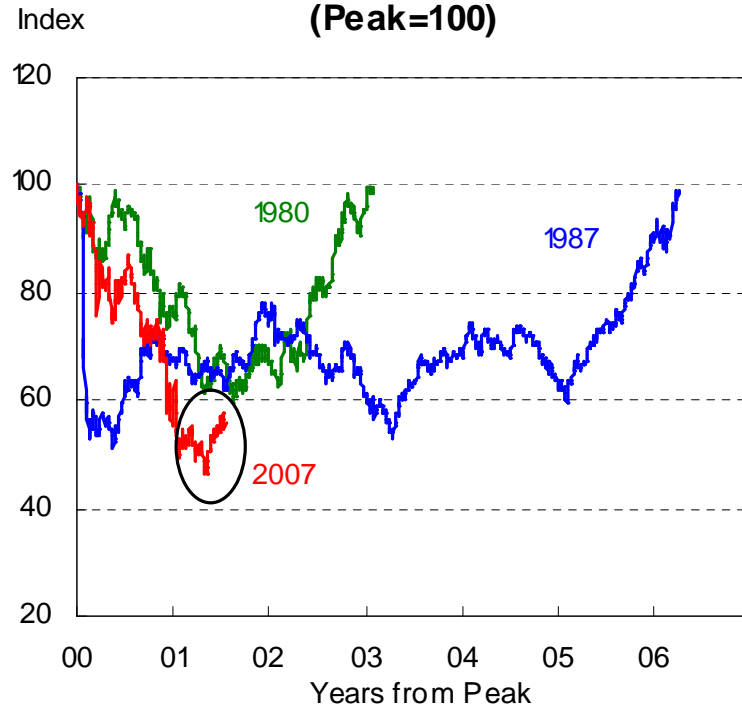
Consumer Spending Puts in a Sluggish Performance



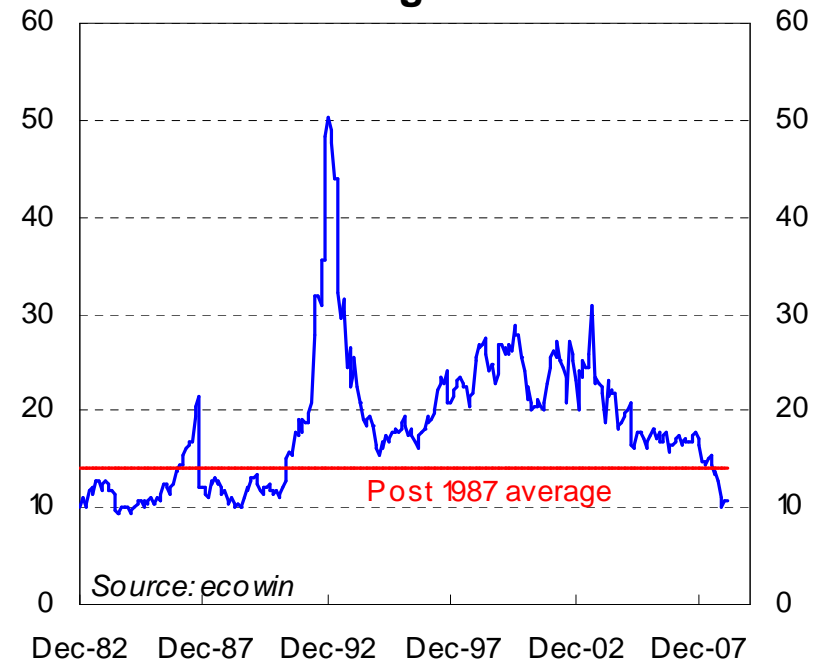
- **Retail spending has been subdued, as consumers' purse strings have tightened and net wealth has declined.**
- **Consumers remain cautious amid the ongoing turmoil in the global economy. But some of the negative forces are receding.**

Share Market – Changing Lanes?

Largest Falls in Australian Equities
(Peak=100)

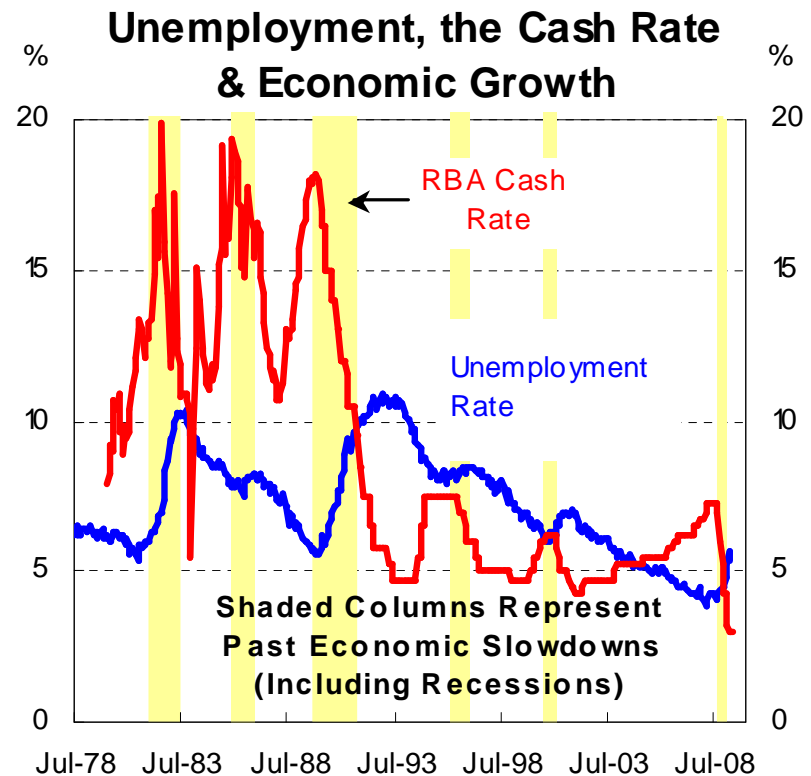
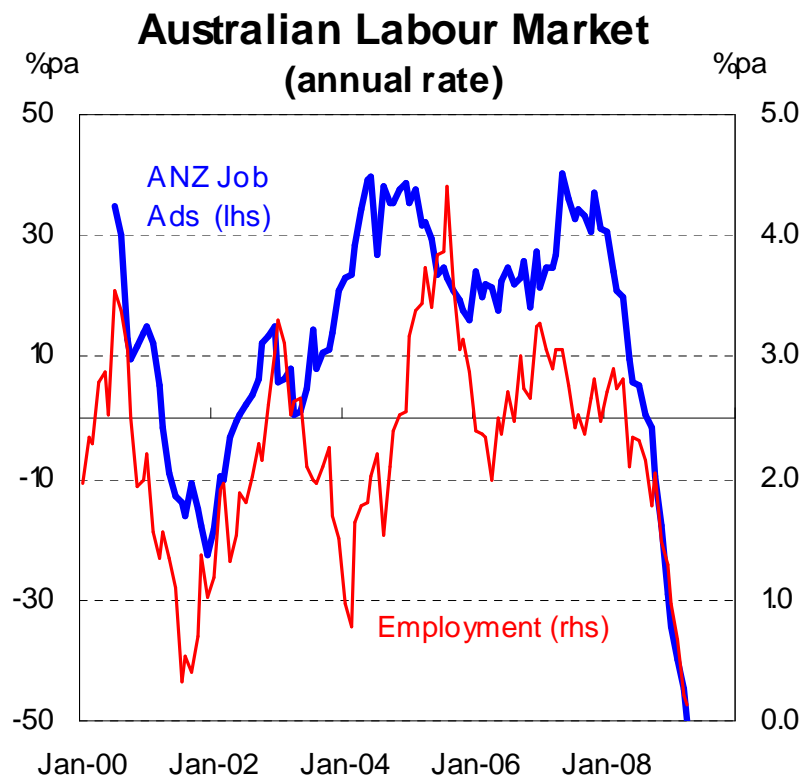


S&P/ASX 200 Index Price-Earnings Ratio



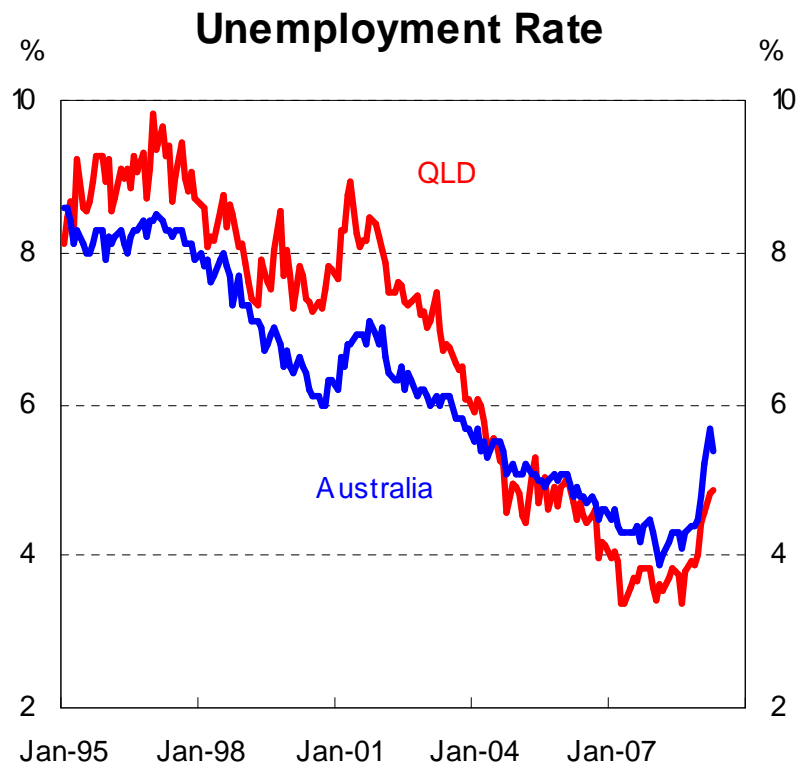
- The share market is approaching the bottoms of historical recessions.
- The price-earnings (P/E) valuation measure is also well below the post-1987 average.

The Danger That Lies Ahead

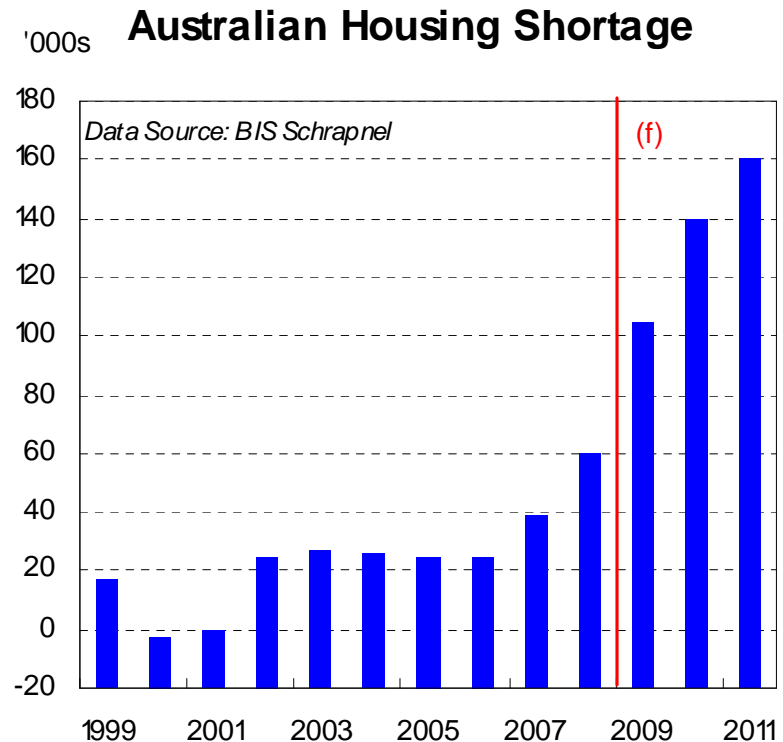
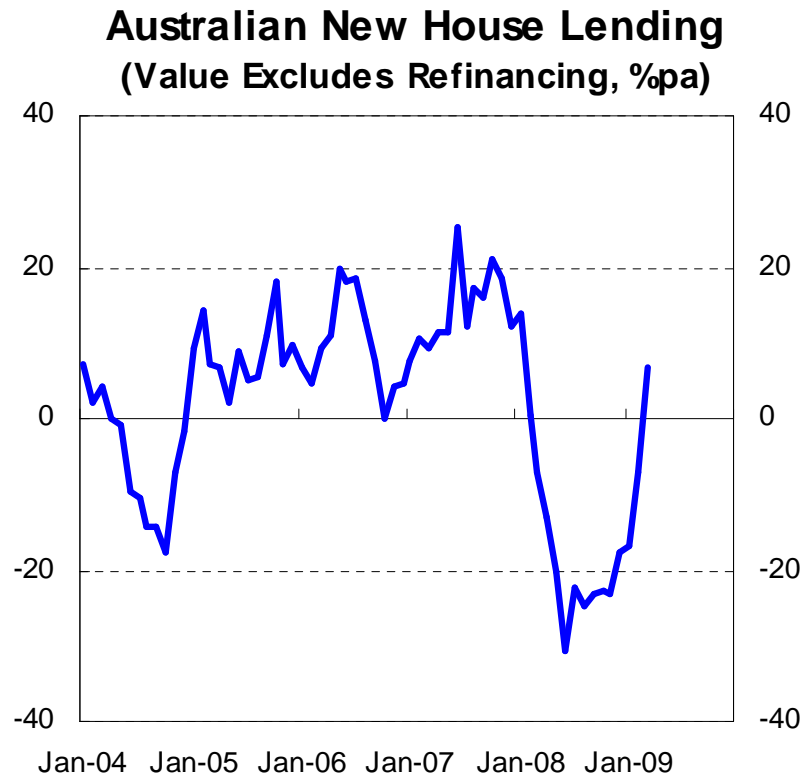


- **The peak in the unemployment rate will occur around the middle of next year. We expect the peak to be between 8 & 9% (from 5.4% now).**
- **The rising unemployment rate will keep caution among consumers intact.**

Queensland Data Snapshot

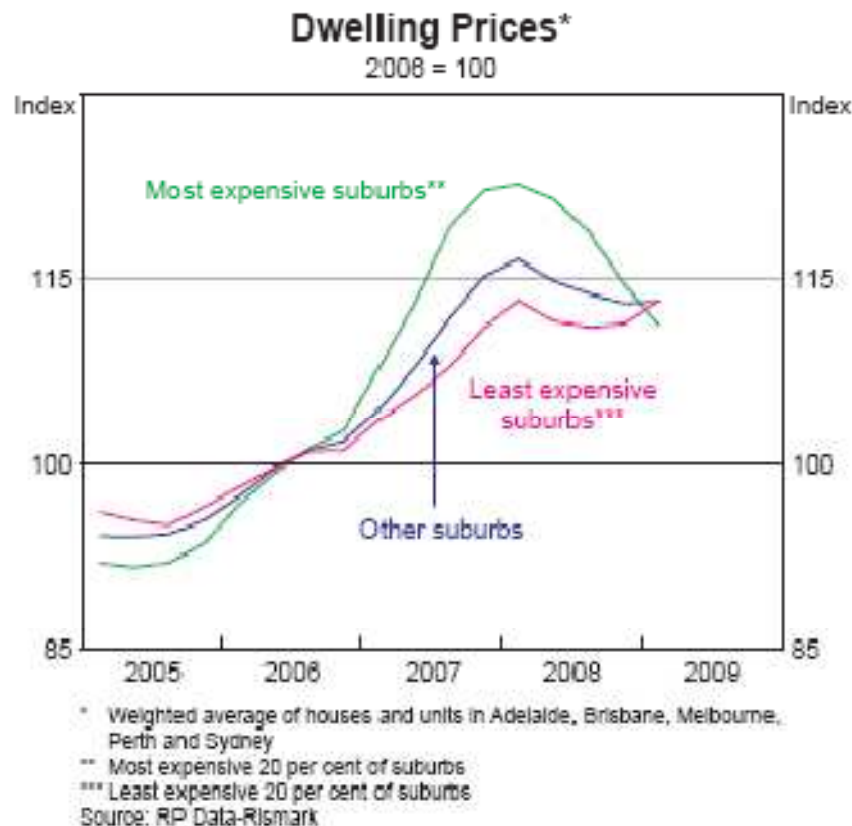


Housing – Keep Your Eyes on the Road



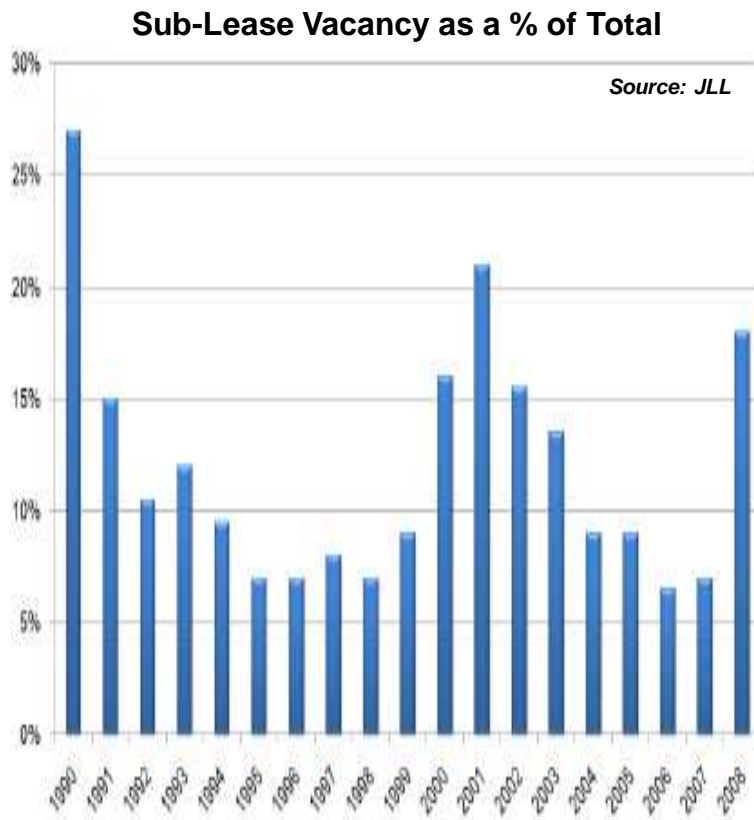
- On one hand: housing grants, rate cuts, demographics. On the other: rising unemployment, uncertainty about the economic outlook and tighter lending criteria.
- Key signpost: pent-up demand exists in Australia.

Housing the Hybrid Car



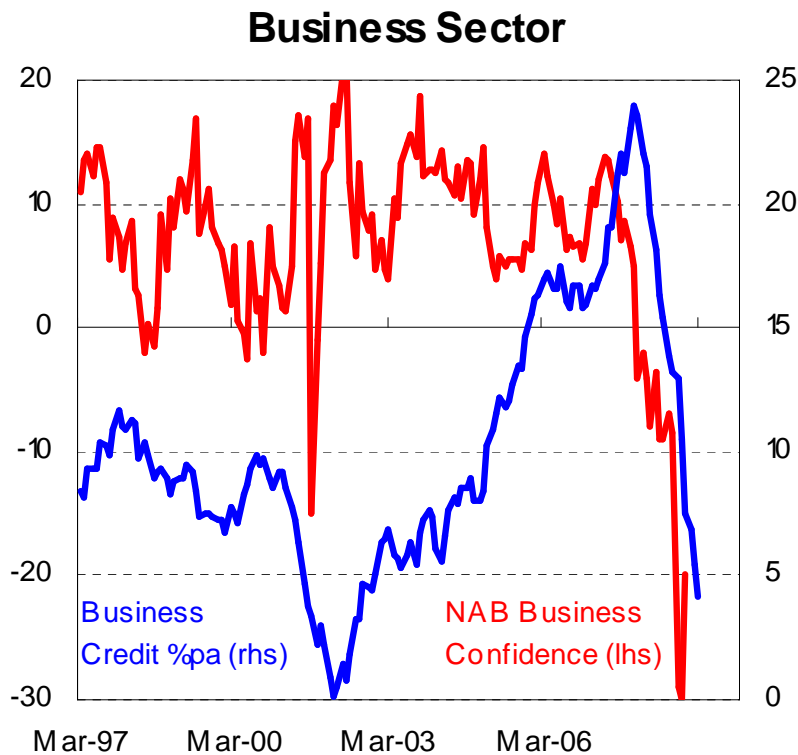
- Recovery in housing has started.
- But 'upgrader demand' still relatively sluggish.
- The strong lift in first-home buyer demand needs to filter through to upgrader demand for a more sustained & broader recovery.

Commercial Construction Slows Sharply



- A more pronounced downturn in the non-residential building sector is being witnessed. Falls sharper for large-scale projects.
- Partly reflects restricted access to external financing.
- Commercial sector also closely tied to the state of the labour market.

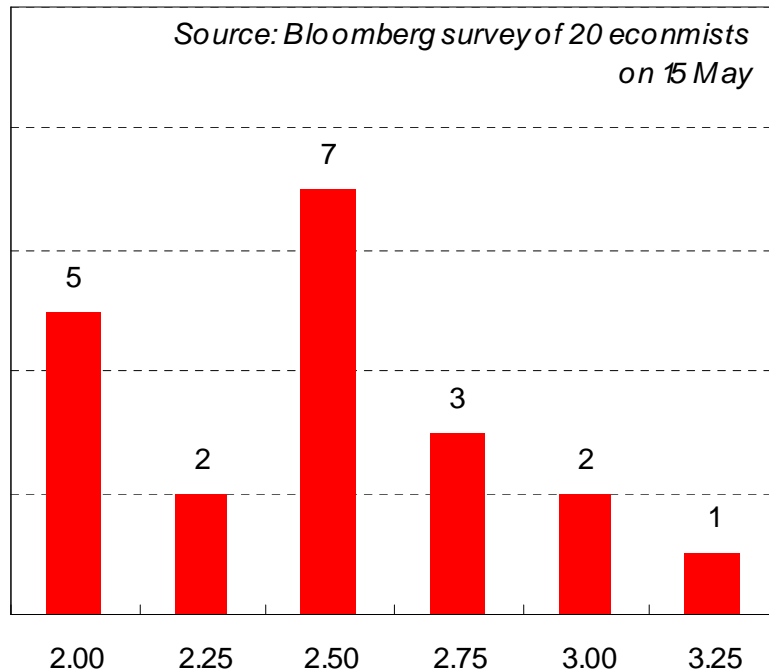
Business – Slow Sign Ahead



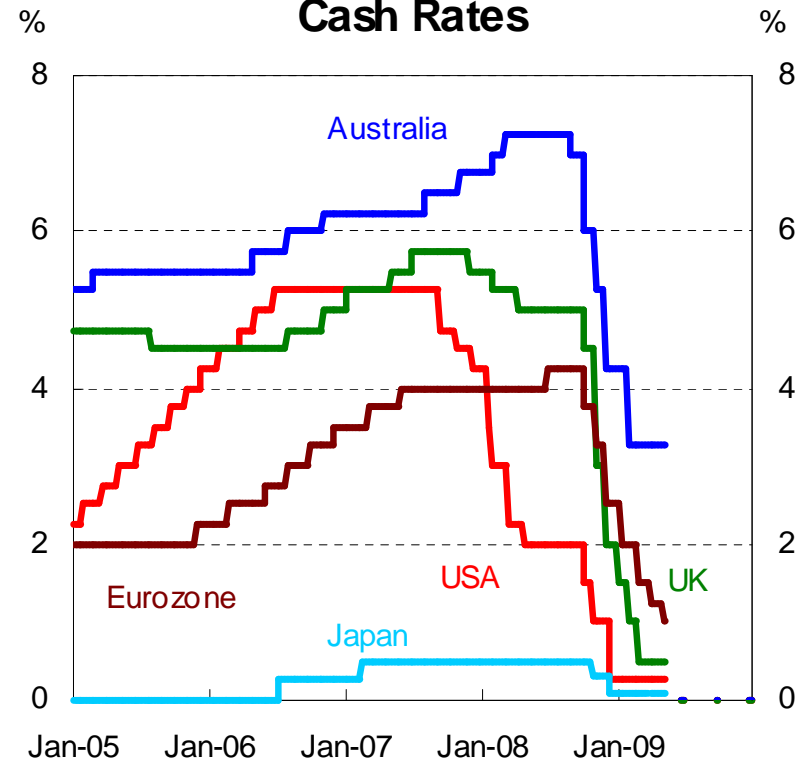
- **Work in the pipeline means business investment has not yet collapsed.**
- **Government injection will assist business investment.**
- **But business investment plans for this financial year and next being scaled back, so business spending set to slow more markedly.**

Interest Rates – The Race to Zero?

**Cash Rate Expectations
(by end Dec 2009)**

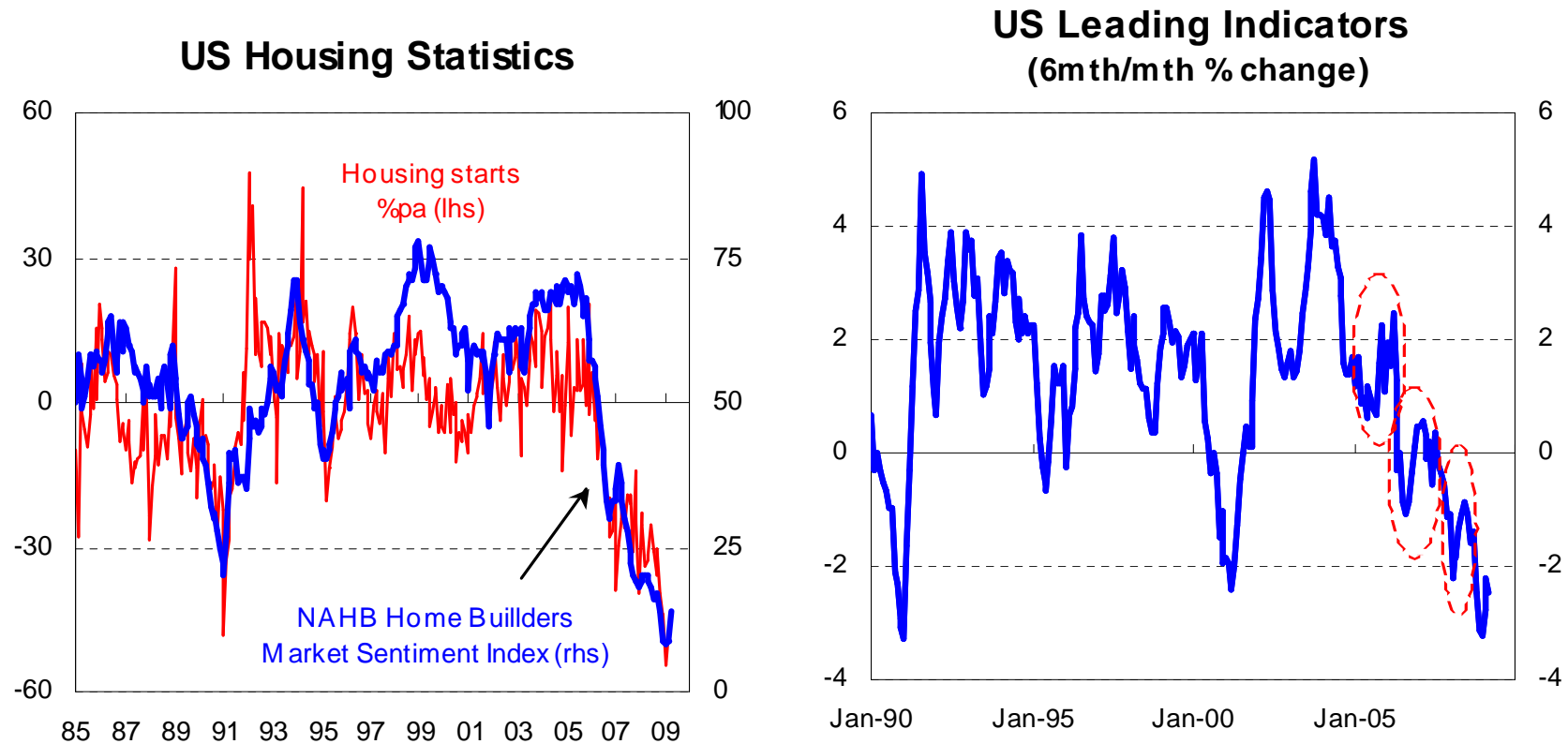


Cash Rates



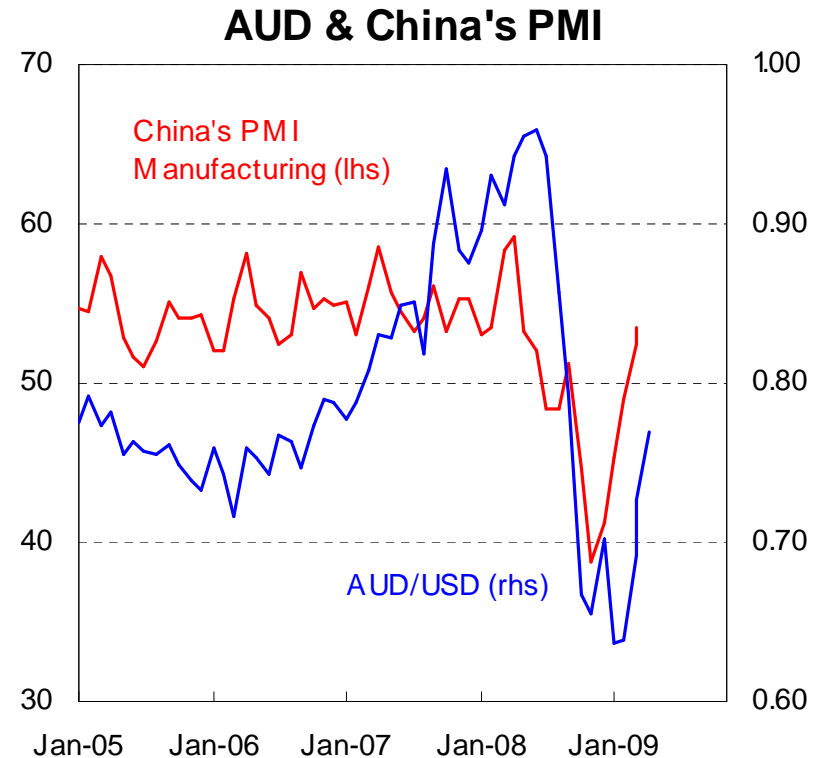
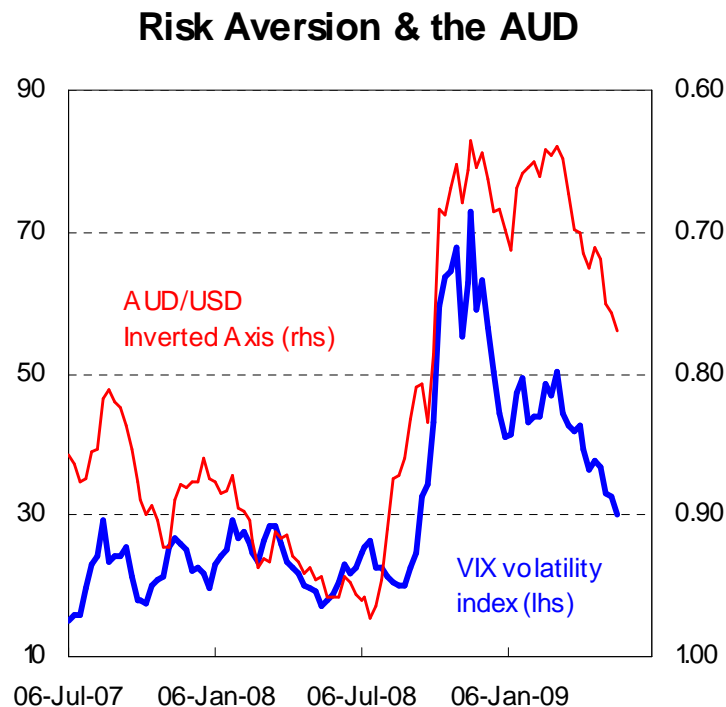
- **St George expects the cash rate to fall to a low of 2.50% by the end of this year. But the possibility of no further rate cuts is ‘alive’.**
- **Credit-market and world economic developments will be important in determining the low point for the cash rate.**

US – A Dim Light at the End of the Tunnel?



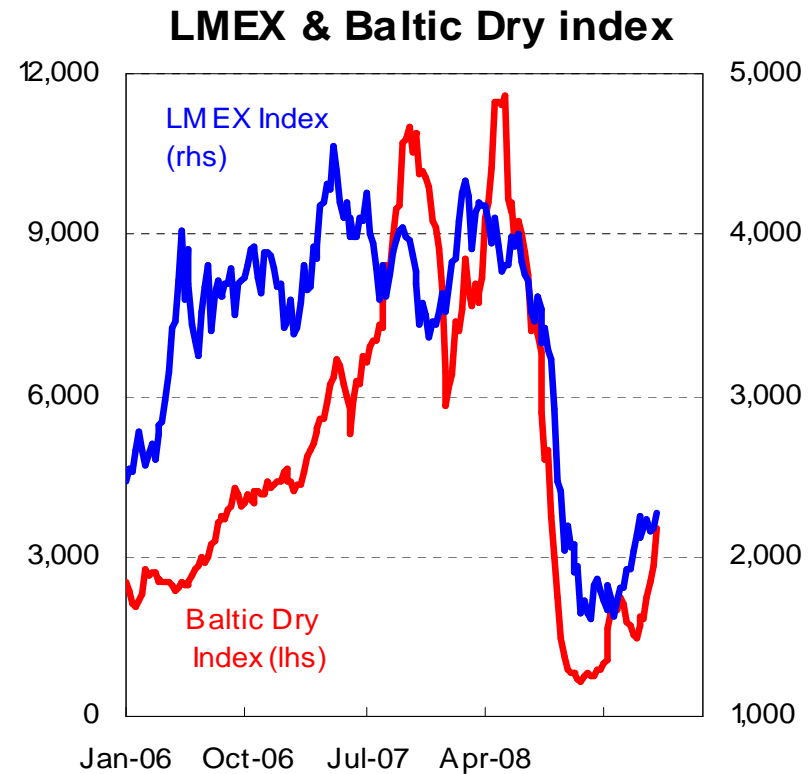
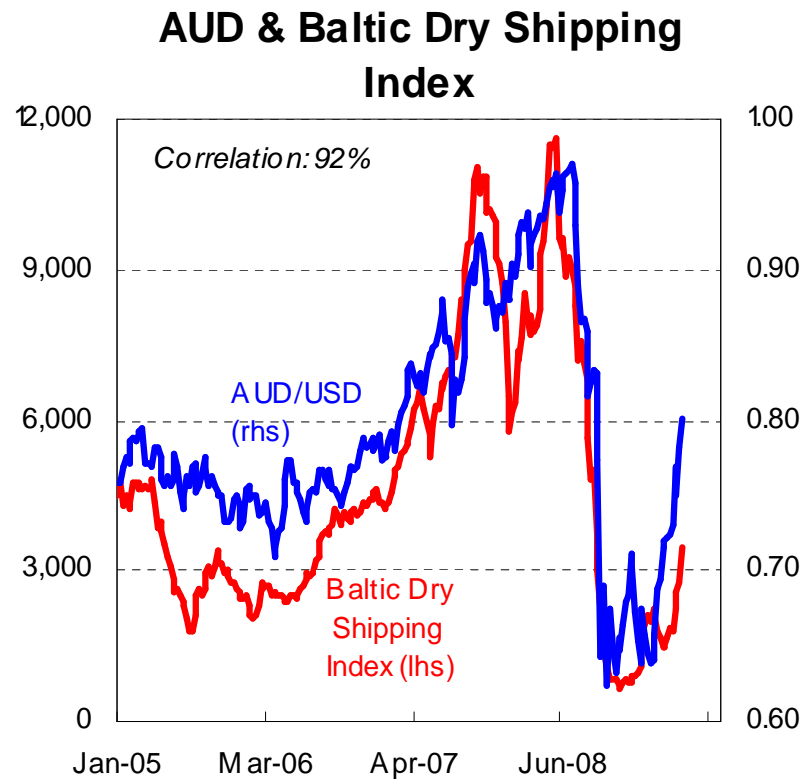
- **The downturn may no longer be intensifying in the US. But the US economy is still set for a (fat) U-shaped recovery not a V-shaped one.**
- **US unemployment rate sits at 8.9%, up from a low of 4.4% in March 2007. Expected to avg 9.10% this year and 9.60% next year.**

The AUD's Dashboard



- **Interest-rate differentials are not the strong force in determining currency direction as they once were.**
- **Investors appetite towards risk is a dominant driver of the AUD.**

Signposts from Commodities

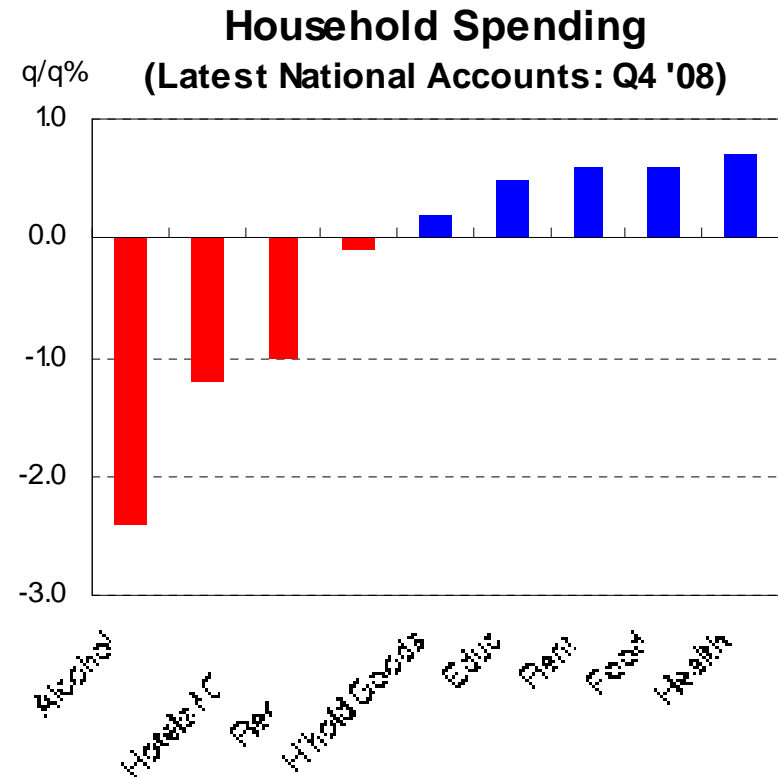
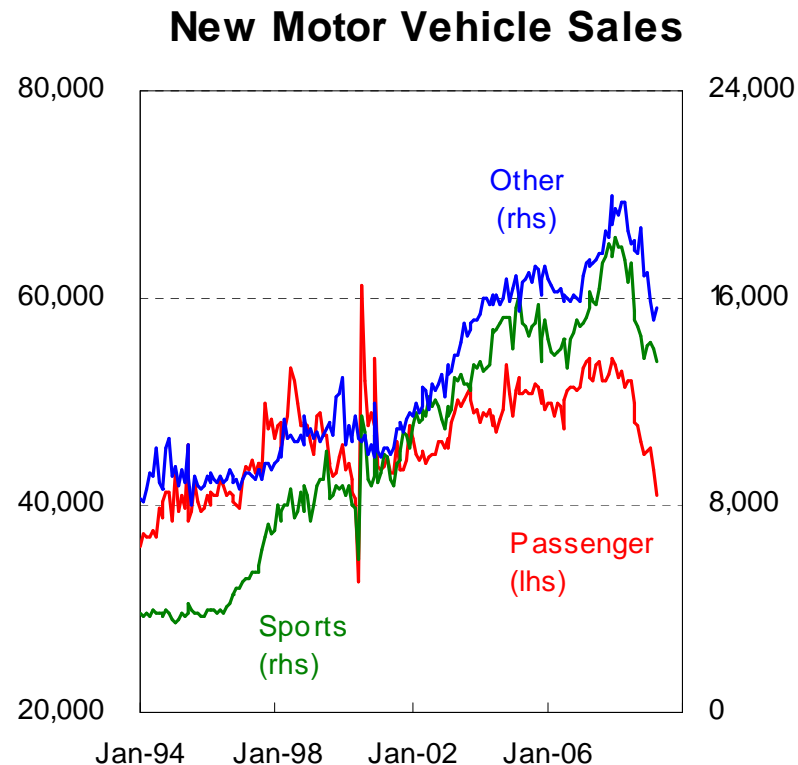


- But Baltic Dry Index suggests the AUD may have overshot.

The Finish Line

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Discretionary Spending Grounds to a Halt



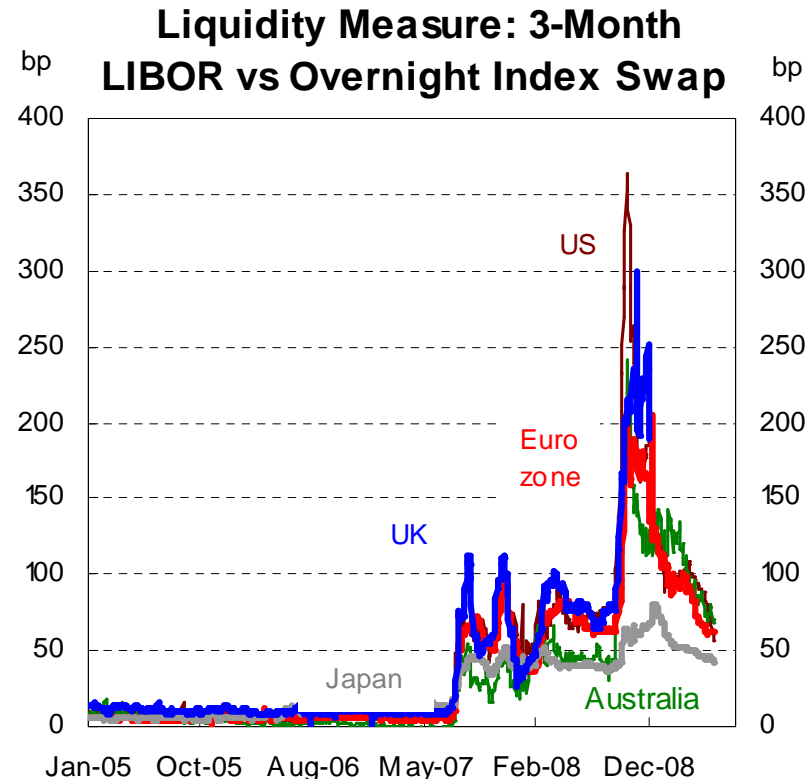
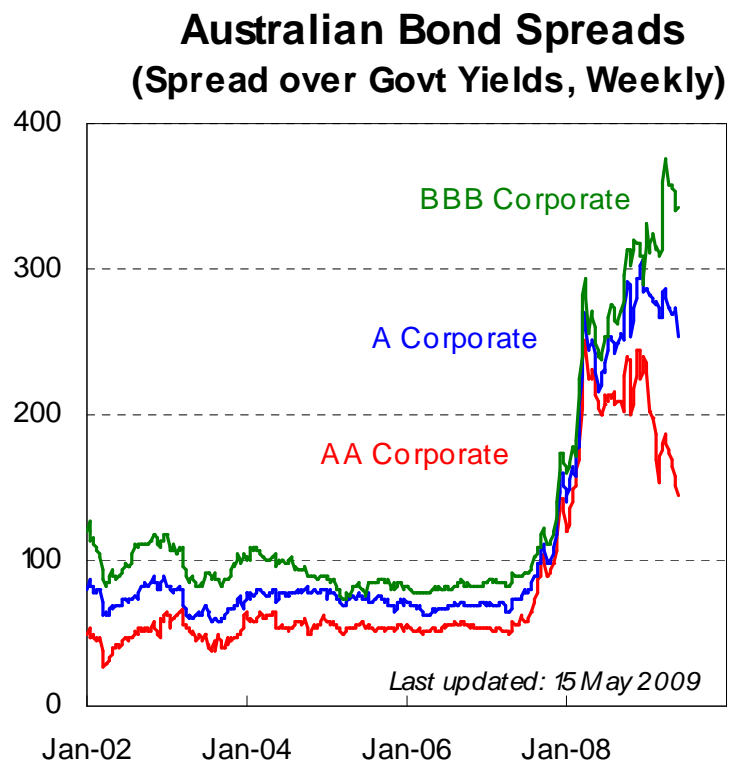
- **Strong areas of retail spending are essential goods like food.**
- **Discretionary spending areas are harder hit as are smaller retailers.**
- **New car sales are down 23% from the peak in November 2007.**

Aussie Swaps Outlook



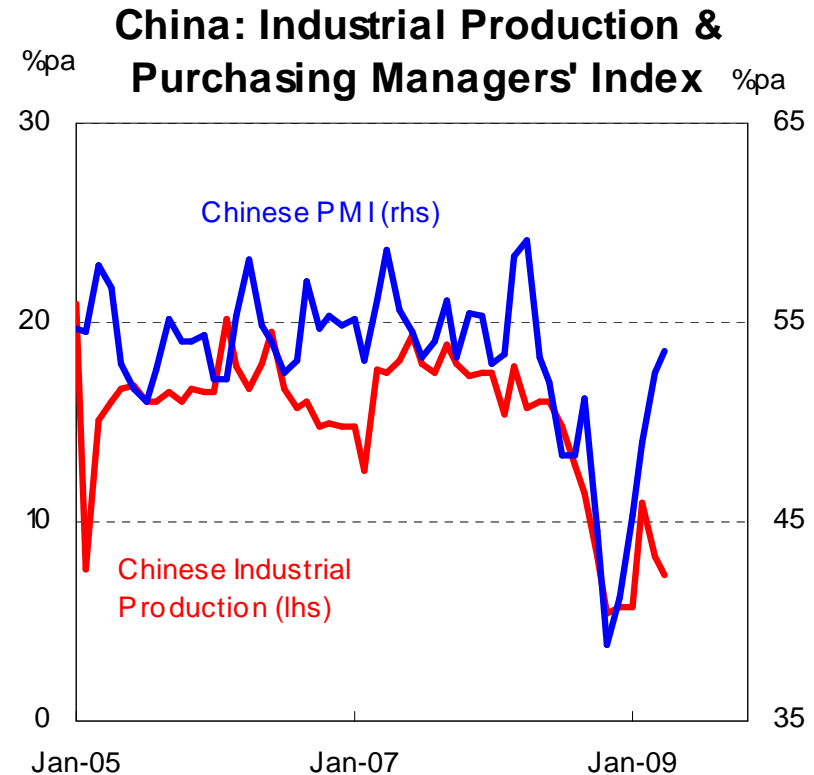
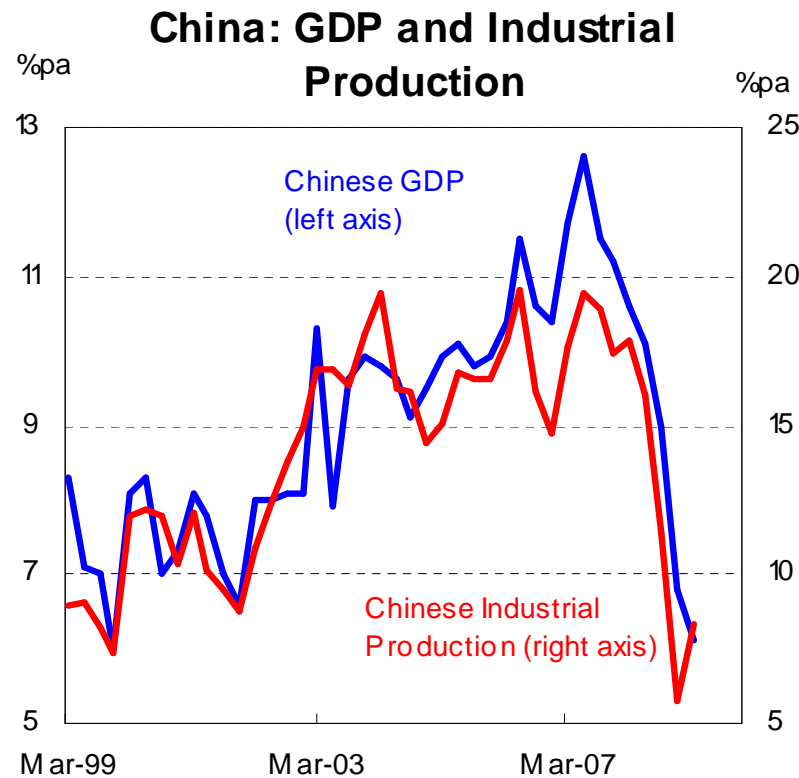
- There's tension between likely negative data outcomes and forward expectations of a recovery over the medium-term. May make it hard to look for significant sustained pullbacks in swap rates.

Headlights on Funding & Liquidity



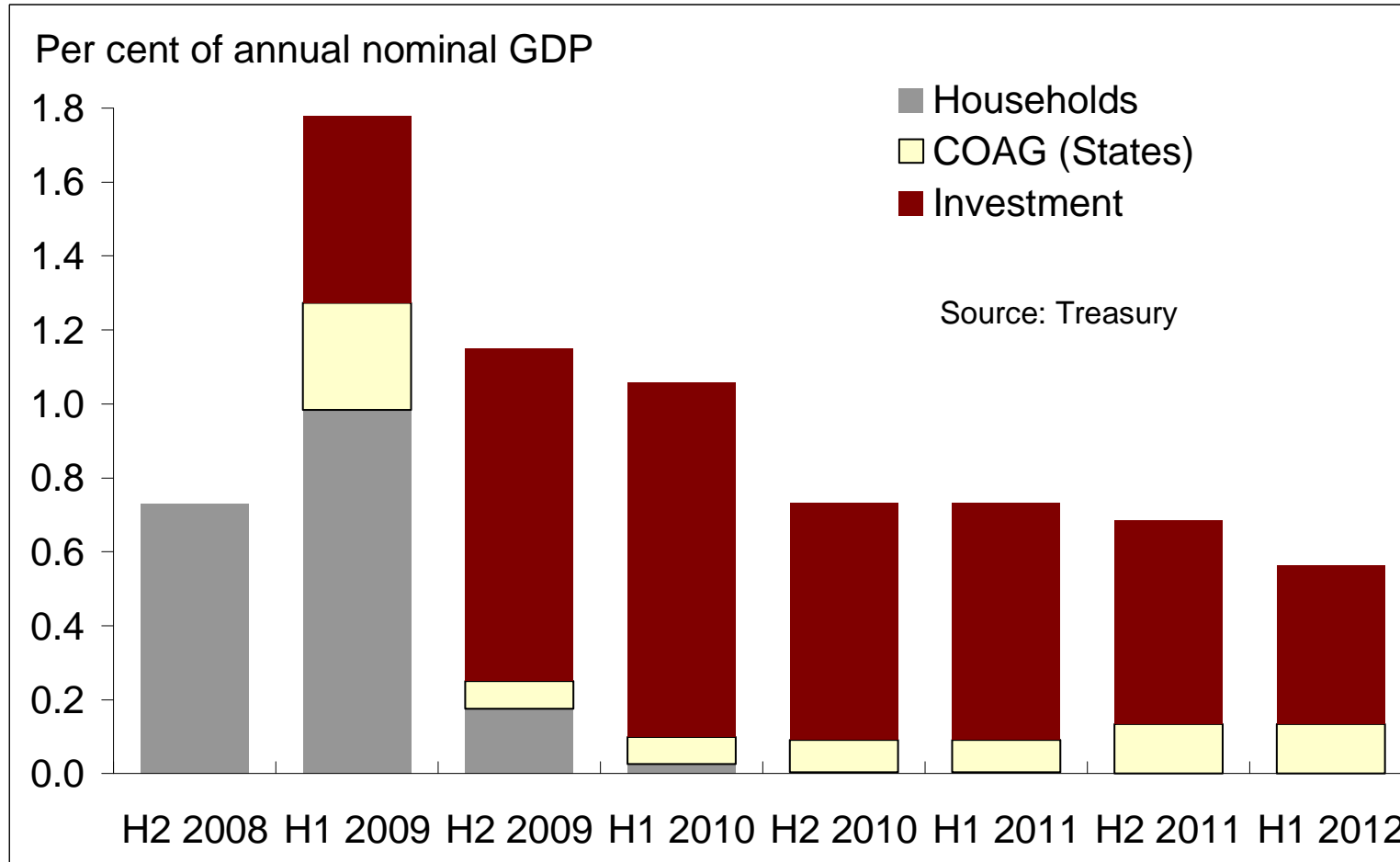
- **Global policy actions to improve conditions in credit markets are having some effect, despite the deterioration in global economic conditions.**
- **There are some mixed signs of improvement in the functioning of credit markets.**

China – Strong as an Ox?

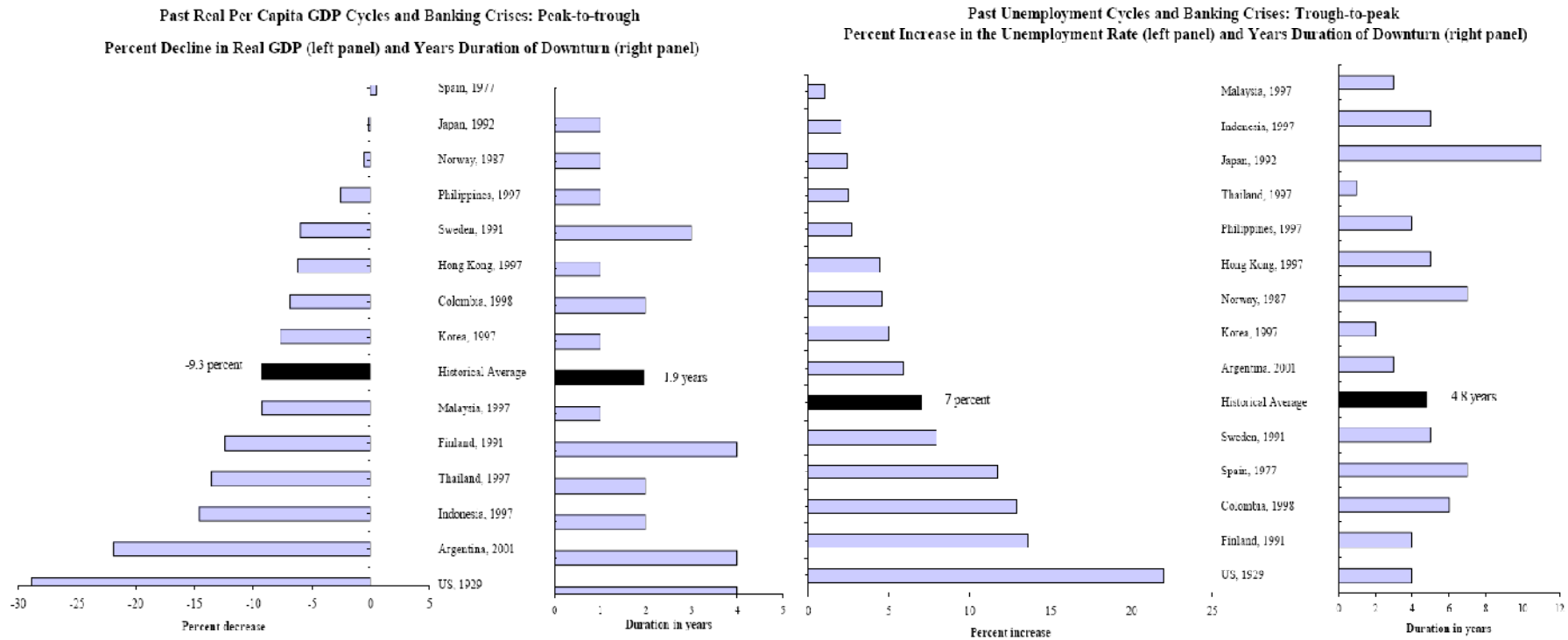


- **China's outlook is important for Australia.**
- **China's Year of the Ox tells us that hard work is required for success.**
- **Chinese GDP slowed to 6.8% in 2008. Slowdown to 6% likely this year.**

Federal Budget



History of Financial Crises & Growth Outcomes



Source: Reinhart & Rogoff (2008), "The Aftermath of Financial Crises"