Investor Signposts: Week Beginning March 29 2009

Upcoming economic and financial market events

Australia		
March 31	Private sector credit (February)	*Consumers and businesses are reluctant to take on debt*
April 1	Retail trade (February)	*A 1.2pct fall is expected – only the second fall in eight months*
April 1	Building approvals (February)	*We tip a 3pct rise on the back of firmer housing loan figures*
April 2	International trade (February)	*A surplus of $1.5 billion is expected*
Overseas		
April 1	US ISM manufacturing (March)	*The current index of 35.8 is well below the 50 break-even line*
April 3	US ISM services (March)	*A modest increase from 40.2 to 42.0 is expected*
April 3	US Non-farm payrolls (March)	*Economists tip a decline in jobs of 600-700,000*

The big picture

- More buoyant conditions are returning to housing markets across Australia, in fact creating what some are calling mini-booms in some regions. Given the weakness in housing markets in other countries, the situation in Australia appears odd. But simply, it all gets to demand and supply.
- In terms of housing demand, affordability has greatly improved, assisted by generational-low interest rates, flat house prices and the first home buyers grant. As a result, demand for home loans is skyrocketing, leading to processing backlogs at major banks. Tight rental markets are also continuing to push rents up 10-15 per cent per annum across the country, causing tenants to turn their attention to property ownership.
- APRA are closely watching the stellar levels of lending that are occurring to ensure that Australia doesn't repeat the mistakes of the US. Reserve Bank's Head of Economic Analysis Anthony Richards says that there is little risk that current low interest rates will lead to a jump in bad loans. But clearly vigilance by all concerned is required.
- On the supply side, Australia continues to under-build. Population is growing at the fastest rate in 40 years but construction is failing to keep pace. The Reserve Bank believes that an additional 40,000 dwellings are required to get the rental market closer to balance. The National Housing Supply Council says that the shortfall is around 85,000 properties. The true figure is probably somewhere between the two estimates, but it is certainly high compared with the current annual commencements of around 140,000 dwellings.
- While first home buyers, and some investors, are active in the market, the difficult part is supply. In terms of established dwellings, home owners are choosing to stay put, constraining the amount of stock on the market and pushing prices higher. And the first home builders are finding it hard to get land close to city centres. The Reserve Bank has commented on the lack of land available, noting that it is keeping the cost of housing high and constraining affordability.
- At present, analysts have to rely on anecdotal evidence and some limited statistics to gauge market trends. For instance weekly data on auction clearance rates are available, but of course most sales in the current market are by way of private treaty. Still, auction clearance rates hit 73 per cent in both Sydney and Melbourne in the latest week, well up on levels near 50 per cent a year ago.
- The only real factor holding back housing demand is job security. However if the recent signs of stabilisation continue on global sharemarkets, leading to stronger consumer and business confidence, greater numbers of budding home buyers will move into the market to compete for the relative small number of listings.
- The last thing either the Reserve Bank, or for that matter first home buyers, want to see is a new surge in home prices. Interest rate increases are certainly not on the horizon, so it may require tighter lending criteria by banks to keep demand and supply for homes in reasonable balance.

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The week ahead

- There is a spattering of economic data over the coming week, but it is still more likely that global, rather than domestic influences, will determine if the Reserve Bank returns to the rate cutting arena In April.
- On Tuesday, private sector credit (lending) figures for February will be released with retail trade, the Performance of Manufacturing index and building approvals data issued on Wednesday. International trade is released on Thursday with the Performance of Services index on Friday.
- A modest 0.4 per cent increase in private sector credit growth is expected in February with the main area of lending growth being owner-occupier housing. Credit growth can be expected to gradually strengthen over 2009 as consumers and businesses become more confident about borrowing.
- Aussie consumers probably retreated from the shopping malls in February after putting government stimulus payments to work over December and January. We expect retail spending fell by 1.2 per cent in February – only the second fall in eight months.
- Solid increases in new loans for dwelling construction in December and January are yet to be reflected in dwelling approvals. However we expect some catch-up with approvals tipped to have risen by 3 per cent in February.
- Meanwhile another trade surplus is expected in February with a modest rise in exports outpacing a flat result on imports. The expected trade surplus of $1.5 billion would be the seventh straight month the trade accounts have been in the black – the best result for almost eight years.
- In the US, its that time of the month again – the time when the monthly employment, or non-farm payrolls, figures dominates the radar screen. Most economists expect Friday's figures to show that payrolls contracted by 600-700,000 in March, broadly similar to the dreadful results recorded over January and February. The unemployment rate is expected to edge up from 8.1 per cent to 8.4 per cent – getting closer to what is expected to be the peak level of around 9 per cent.
- The only good news is that recent signs of improvement in housing and investment figures may mean that we are getting close to the peak in job losses.
- Also on the agenda over the week is consumer confidence and a home price index on Tuesday with the ISM manufacturing index, construction spending, ADP employment survey and car sales to be released on Wednesday. Data on factory orders is released on Thursday with the ISM services index on Friday.

Sharemarket

- Was March 9 the low-point for the current bear market? That's the question on everyone's lips. While investors are wary of false bottoms, at least this time there has been a run of more favourable economic data in the US. And there is greater intent as well as actions to stabilise the banking system. It is clear that the banking system must be stabilised first before there is any hope of sustainable recovery in the sharemarket or the economy.
- Since the low on March 9, the US Dow Jones has lifted by 21 per cent with the ASX 200 up 16 per cent, Japanese Nikkei up 23 per cent and German Dax up 19 per cent. The UK FTSE has dragged the chain, up just 13 per cent.

Interest rates

- Businesses aren't keen to lock in their funding unless they are confident rates have hit bottom. But the hard part is being able to pick the low point in practice. And the key question is whether businesses have again missed the boat. In early February, three-year swap rates hit record lows of 3.38 per cent. They bounced higher from there only to return to lows of 3.40 per cent on March 9. But in the period since they have bounced higher again and by a significant margin, lifting to 3.80 per cent. Concern about the global investor appetite for government securities together with the decision of the Australian Government to guarantee semi-government debt have both led longer-term yields higher. The other complication is that equities are back in vogue on a renewed bout of optimism.
- It's not just businesses that need to carefully assess the interest rate picture. Home loan borrowers must now assess whether the Reserve Bank will cut rates again if global optimism takes over. Fixed rate home loans aren't in vogue at present, but that could all change if there is a growing perception that the Reserve Bank has retired to the interest rate sidelines for good.

Currencies & commodities

- Investors are scouring for evidence that the worst is over. Equity markets have certainly rallied since early March and currency and commodity markets haven't been far behind. The CRB commodity futures index hit a 6½ year low of 200.34 on March 2 and in the period since has rallied 14 per cent. And the barometer of global sentiment – the Aussie dollar – has risen just under 12 per cent since the low of US62.88c set on March 2.
- Certainly not everything is pointing the way of recovery. The Baltic Dry sea freight index hit five month highs on March 10 and has since lost 24 per cent. Still it had rallied 246 per cent from the December lows, so the recent fall may just be consolidation after a sharp run up.

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