TCorp Local Government Services

Economic Commentary – September 2015

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The Month in Review

Economic and Market Trends

The outlook for the Chinese economy remains uncertain. While retail sales growth improved in August, industrial production and fixed-asset investment remains lacklustre and failed to meet economist expectations. Some analysts believe activity was held back by a decision by authorities to shut down factory production in Beijing in order to improve air quality ahead of a national celebration. Moreover, there has been incremental improvement in the housing sector which suggests that some pick-up in activity remains plausible. That said, if this doesn't become apparent in the next couple of months, then the Chinese authorities will be forced to abandon their 7% growth goal for 2015.

In the US, the key question is whether weakness in the rest of the world - and volatility in financial markets - has the capacity to undermine domestic activity, and force it to delay a tightening in monetary policy. Certainly, most signs continue to suggest that the US economy remains healthy. For example, the unemployment rate fell to 5.1% in August, which is the lowest level since April 2008.

The fall in equity markets in August does appear to have dented consumer confidence in the US. As recently as June, the University of Michigan consumer sentiment index stood at 96.1, but had fallen to 85.7 by September. Alert to the risk that this could be reflected in weaker spending in coming months, the market was placing a fairly low 30% chance that the US Federal Reserve would raise its key policy interest rate at its September policy meeting. In the end, the US Fed conceded that it was too soon for it to start raising its key policy rate, citing increased volatility in global financial markets as the key reason for the delay.

As in the US, financial market volatility appears to have taken a toll on Australian business and consumer confidence, with both measures dropping in the past month. But while firms are more uncertain about the future, they also reported stronger actual trading conditions in August. This seems to reflect the impact of the weaker A$ boosting the competitiveness of exporters and import-competing firms, alongside the stronger housing market. The recent change of Australia's Prime Minister to Malcom Turnbull seems to have boosted more frequent measures of sentiment, although the question remains as to whether this will be sustained.

The labour market is also consistent with steady - rather than deteriorating – economic growth. The unemployment rate declined to 6.2% (from 6.3%) in August, with a moderate growth in jobs. NSW continues to record the lowest unemployment in Australia, at 6%. NSW has also been responsible for more than half of the jobs growth in Australia over the past year.

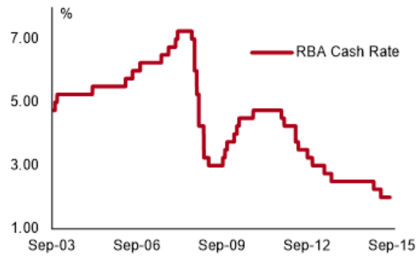
For these reasons, most analysts and policymakers downplayed the importance of the June quarter GDP data which – at face value – did suggest that there had been a sharp moderation of growth in Q2. The GDP data suggested the economy grew by just 0.2% in the June quarter, down from 0.9% in the previous three months.

The sell-off in global equity markets that was ignited in August continued through September. Most of the major developed world equity markets were down between 2 and 5%. Negative anecdotes around the global automotive industry dampened market sentiment further, while a sharp decline in the share price of a global resources company put into question the outlook for commodity prices and demand. Global bond yields declined in the month, despite the impending normalisation of monetary policy in the US.

Financial/Economic Data

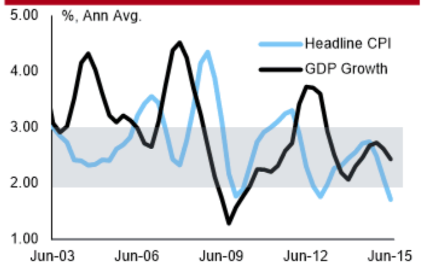
September 2015

RBA Cash Rate

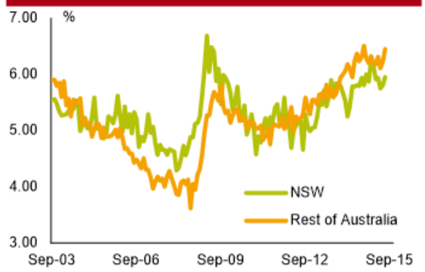


Australia Dollar

Australian Economy



Unemployment Rate



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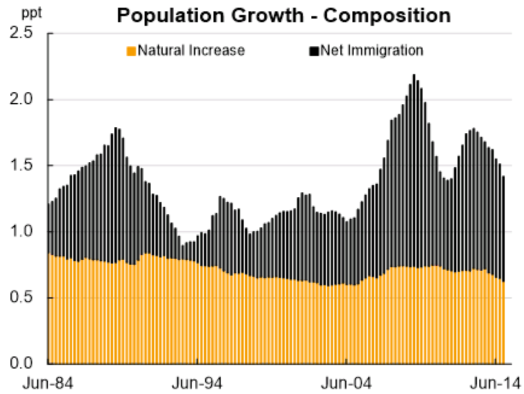
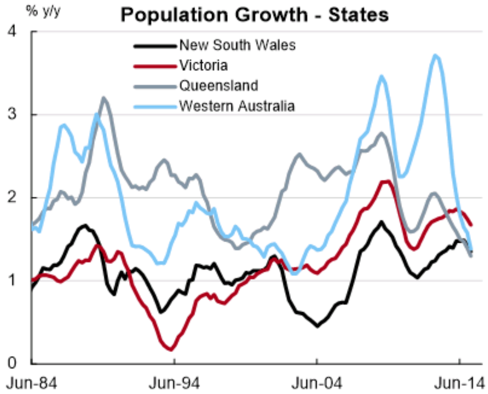
The State of NSW

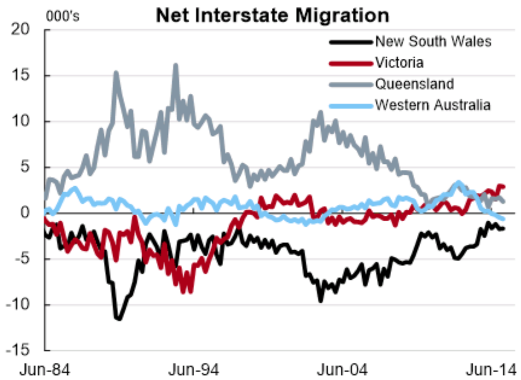
Where are the people going?

Population shifts have important implications for economy activity. Population growth can dictate the amount of infrastructure spending required, the scope of public services provided and the amount of tax revenue that governments collect. There are two sources of population growth - the natural increase and net migration. The natural increase – the netting of births and deaths – is the stable contributor to population growth. Net migration, however, is much less predictable and more cyclical. Economists believe that protracted periods of economic uncertainty (i.e. rising unemployment) and worsening affordability (i.e. rising house prices) tend to dampen sources of population growth. And both factors may have contributed to the recent slowing in population growth in Australia.





The top-left chart shows that population growth in Australia has slowed from 1.8% y/y to 1.4% y/y. Furthermore, the chart shows that while the natural increase in the population has eased, most of the deceleration in population growth has been driven by net migration. Those people who migrate to Australia tend to do so for job opportunities. As migrants enter the labour force, the potential growth rate for the economy also increases. However, this works both ways. And this is why slower population growth could prove challenging for the economic outlook more broadly. The RBA now expects population growth to average 1.50% over the next few years rather than the 1.75% it previously assumed.



Market Movements and Economic Data

Financial Data	30 Sep	Monthly change	
Cash Rate	2.00%	0.00	–
Corporate Bond Yield*	3.63%	-0.04	▼
Term Deposit**	2.20%	0.00	–
ASX200	5022	-3.6%	▼
S&P500	1920	-2.6%	▼
AUD/USD	0.702	-0.010	▼
Economic Data* **	**30 Sep**	**Quarterly change**	
Headline CPI	1.5%	0.2%	▲
Trimmed Mean CPI	2.2%	-0.1%	▼
GDP Growth	2.0%	-0.5%	▼
House Prices	10.5%	3.0%	▲
Unemployment Rate	6.2%	0.2%	▲

*A-rated 5-year rate, source: RBA **Average 90-day rate of the five largest banks for $10,000, source: RBA ***National data, y/y, source: ABS, RBA

While population growth has slowed in all States, there has also been a convergence of growth rates. WA and Queensland have seen the most slowing, consistent with the sharp fall in mining investment. But while population growth in NSW and Victoria has decelerated, the pace remains at historically high levels. This reflects the economic outperformance of NSW and Victoria. The net interstate migration data show the increasing preference for households to live in NSW and Victoria (bottom-left chart). Most economists expect these population trends to continue, although they also highlight that deteriorating housing affordability in NSW and Victoria is a risk which could result in households turning their attention to the more affordable States.