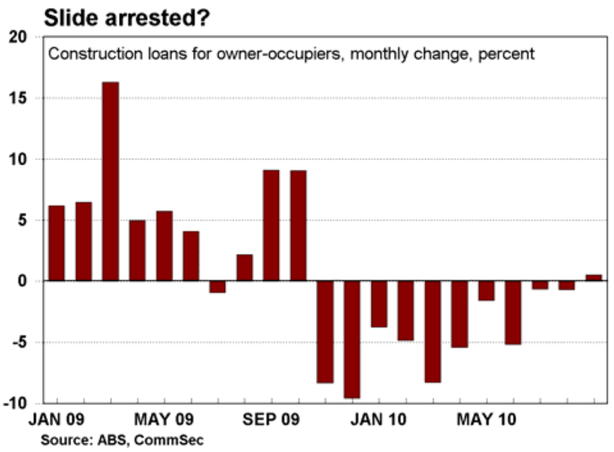
Confidence falls to five month low on rate hike

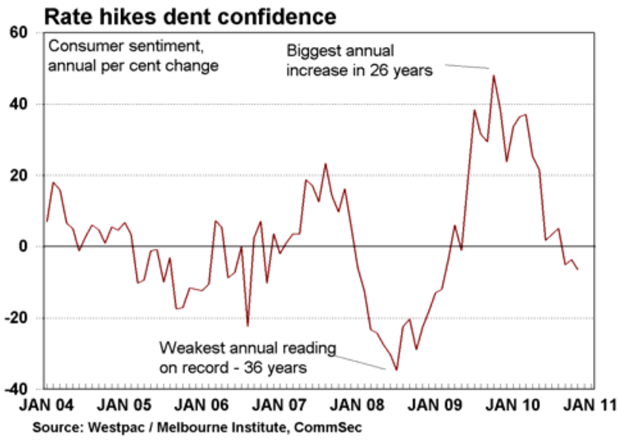
Housing finance; Consumer sentiment

- **As expected, the Westpac/Melbourne Institute index of consumer confidence fell in the latest month in response to the latest interest rate hike. The index fell by 5.4 per cent to a five-month low of 110.7 in November.**
- **Home lending recorded a modest rise in September. The number of new home loans to owner-occupiers rose for the third consecutive month, rising by 1.3 per cent in September. In annual terms housing finance commitments are still down 24.6 per cent on a year ago.**
- **Construction of dwellings rose for the first time in 11 months, up by 0.5 per cent in September. The value of investment loans rose by 1.0 per cent in September. The average home loan across Australia stood at $285,100 up 5.8 per cent on a year ago.**

What does it all mean?

- The big picture story for the Australian economy remains good, but it seems that the latest rate hike has taken its toll on confidence levels. Confidence levels are at the weakest levels in five months, and blame can be squarely based on the latest rate hike. In fact the latest result could have been even bleaker if not for the recent rally in equity markets and the Aussie dollar holding at 28 year highs – no doubt two factors that helped temper the slide in sentiment.
- Aussie consumers are holding on to their conservative attitudes and the latest rate hike is unlikely to help improve activity levels. Interest rates need to remain on hold for a an extended period before consumers are tempted to part with their cash. The recent fall in confidence will only make the trading environment more difficult for retailers. Retail discounting is likely to be a theme in coming months to generate interest. No doubt the strength of the Australian dollar will help alleviate the margin pressure being felt by retailers
- The Reserve Bank can certainly rest easy over coming months. The higher interest rates have certainly taking its toll on new housing activity. And the latest pickup in new commitments is hardly a drop in the ocean, given the magnitude of the slide. Housing finance is only showing early signs of stemming the slide, with commitments modestly improving from nine year lows in the past couple of months. In annual terms commitments are still down

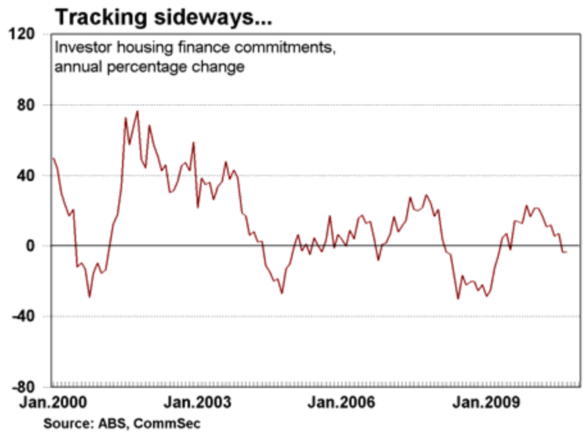




Savanth Sebastian – Economist (Author)
(612) 8223 7130 (work)

25 per cent on a year ago. The weakness in dwelling activity will no doubt result in more subdued economic growth in the near term.

- It is still early signs but the pickup in construction loans after 10 straight months of weakness is encouraging, and will be closely watched to gauge if activity is finally bottoming out. However the recent rate hike and the healthy growth in house prices over the past year, are likely to ensure potential home buyers remain circumspect.
- The slowdown in dwelling activity is certainly being felt across the states. Queensland has seen the number of new loans slump by almost 32 per cent on a year ago. Similarly NSW, Western Australia, and South Australia have seen new loans slide by around 30 per cent. The only state that seems to be holding up relatively well given the conditions has been Victoria.



- The longer term fundamental for the property sector are certainly sound. As credit conditions improve investors are likely to looking at property as a more attractive investment vehicle – particularly given that job security is much more certain.

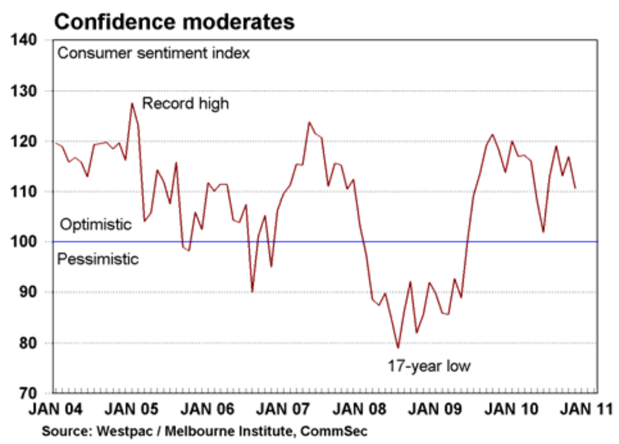
What do the figures show?

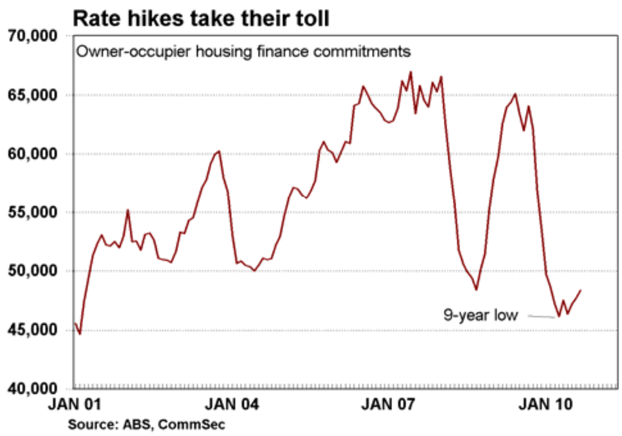
Consumer sentiment

- The **Westpac/Melbourne Institute index of consumer sentiment** fell by 5.4 per cent in November to 110.7 after rising by 3.4 per cent in October. The index is now down 6.4 per cent on a year ago.
- The current conditions index fell by 5.1 per cent, while the expectations index fell by 5.5 per cent.
- Four of the five components of the index fell in November:
  - The estimate of family finances compared with a year ago fell by 10.2 per cent;
  - The estimate of family finances over the next year rose by 0.5 per cent;
  - Economic conditions over the next 12 months was lower by 9.8per cent;
  - The measure of economic conditions over the next five years fell by 6.4 per cent;
  - The measure on whether it was a good time to buy a major household item fell by 1.9 per cent.

Housing Finance

- The *number* of new owner-occupier housing loans for only for the third consecutive month rising by 1.3 per cent in September to 48,333 new commitments.
- After falling for 10 consecutive months, construction loans rose by 0.5 per cent in September. Loans for the purchase of established dwellings (ex refinancing) rose by 1.8 per cent, while loans for the purchase of newly erected dwelling rose by 3.2 per cent. Refinancing commitments were higher by 1.4 per cent.
- Loans rose in most states in September except Queensland (down 0.5 per cent) and Victoria (down 1.4 per cent). Lending rose the most in Western Australia (up 4.9 per cent) followed by Northern Territory (up 2.2 per cent).





- In annual terms housing finance commitments are down 24.6 per cent on a year ago. Across the states new commitments in the Queensland are down 31.7 per cent on a year ago.
- The *value* of new housing commitments (owner occupier and investment) rose by 1.0 per cent in September. Owner-occupier loans rose by 0.6 per cent while investment loans rose by 1.7 per cent.
- **First home buyers** rose from the six year lows of 15.5 per cent to 15.9 per cent of all lending in September – well below the record high of 28.5 per cent set in May 2009. **Fixed rate loans** accounted for 4.4 per cent of all loans, up from 3.4 per cent of loans in August. And the **average home loan** across Australia stood at $285,100, up 5.8 per cent on a year ago.

What is the importance of the economic data?

- **Housing Finance** data is produced monthly by the Bureau of Statistics and shows commitments by lenders, such as banks, to provide finance for housing purposes. The lending figures relate to those looking to buy or build homes to live in as well as those seeking to buy or build homes for investment purposes. Generally people get their finance organised first, so the figures are regarded as a leading indicator on the housing market.

What are the implications for interest rates and investors?

- Day by day, it is looking more likely that the Reserve Bank Board will be sitting on its hands until mid 2011. Interest rates are modestly restrictive and there are good grounds to argue that the move to a tighter monetary policy was a little too quick. The Reserve Bank would be best served by allowing consumers and businesses time to adjust to the recent round of rate hikes.

Savanth Sebastian, Economist, CommSec
Work: (612) 8223 7130;