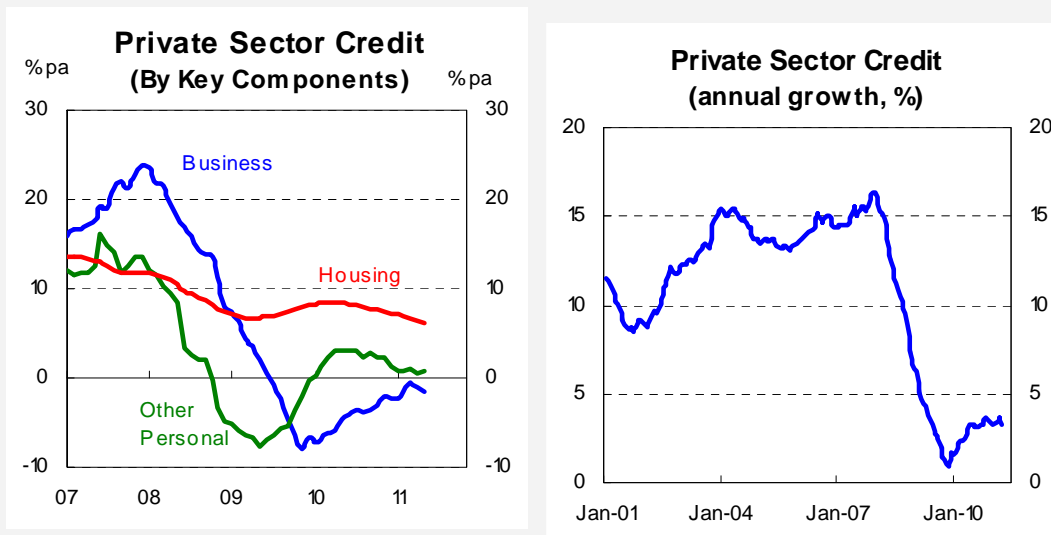


DATA SNAPSHOT

Private Sector Credit: In different gears?

Thursday, 30 June 2011

- Today's data presents conundrum – business credit rose by a paltry 0.1%, following a surprising 0.5% contraction in April. This is despite strong growth in capex spending. While resource companies likely able to fund projects internally due to large amounts of cash obtained from existing operations, the pullback might reflect businesses outside mining are delaying or shelving investment plans. We expect business credit to eventually pick up in line with the deepening capex upswing.
- Private sector credit rose by 0.3% in May. On a year-on-year basis, private sector credit rose by 3.1%, the weakest annual growth in a year.
- Credit to households remains weak, reflecting unwillingness for households to take on debt. Housing credit grew by 0.5% in May and rose by 6.2% over the year to May. This was the weakest annual rate since the data becomes available in 1976. Other personal credit was also subdued and was flat in May.
- These areas of weakness in the domestic economy along with heightened global growth concerns point to little urgency for the RBA to move soon. However, with the economy facing capacity constraints, the risk of inflationary pressures building still remains. We believe that an August rate rise is still a possibility, however we believe that it will be conditional on a high outcome for 2Q underlying inflation. A more likely outcome would be a rate rise in October or November.



Credit to the private sector rose by 0.3% in May, which was broadly inline with expectations for a 0.4% rise. On a year-on-year basis, private sector credit rose by 3.1%, the weakest annual growth in a year.

Business credit rose by a paltry 0.1%, following a surprising 0.5% contraction in April. The current softness is a little surprising as weak business credit is usually accompanied by weak business investment.

Credit to the business sector was on a path to recovery the beginning of this year, but has since pulled back over Q2. This is despite a large amount of investment in the pipeline according to the capex survey and construction engineering data. With resource companies

likely able to fund projects internally due to large amounts of cash obtained from existing operations, the pullback may be an early sign that businesses outside mining are delaying or shelving investment plans.

Housing credit grew by 0.5% in April, slightly up from 0.4% rises recorded in March and April, but still showing weak growth. Over the year to May, housing credit weakened further rising by 6.2%, the weakest annual rate since the data becomes available in 1976. Credit to both owner-occupied and investor housing remain soft. Owner-occupier housing rose by 0.5% while investor housing credit grew by 0.4% in May.

Other personal credit, which includes purchases on credit cards and personal loans, was also subdued. This segment posted a flat outcome for May and follows a 0.3% fall in April.

The weakness in household credit reflects the caution by households, and is consistent with consumer sentiment surveys. According to the Westpac consumer sentiment survey, there is a very high proportion of respondents nominating paying off debt or the home mortgage as the wisest place for savings. This suggests consumers remain unwilling to take on more debt.

Reserve Bank Outlook:

The RBA has welcomed the caution by households on their borrowing as it makes room for the expansionary effect of the resource boom on the economy. In addition, today's data might potentially reflect businesses outside mining are delaying or shelving investment plans. These areas of weakness in the domestic economy along with heightened global growth concerns point to little urgency for the RBA to move soon. However, we expect business credit to eventually pick up in line with the deepening capex upswing.

In addition, with the economy facing capacity constraints, the risk of inflationary pressures building still remains. We believe that an August rate rise is still a possibility, however we believe that it will be conditional on a high outcome for 2Q underlying inflation, which will be released 27 July. A more likely outcome would be a rate rise in October or November when the deepening upswing in investment in mining should spread to other sectors of the economy and the boost from rebuilding after the floods and cyclone will get underway.

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