

Australian & Global Economic Overview



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International Backdrop



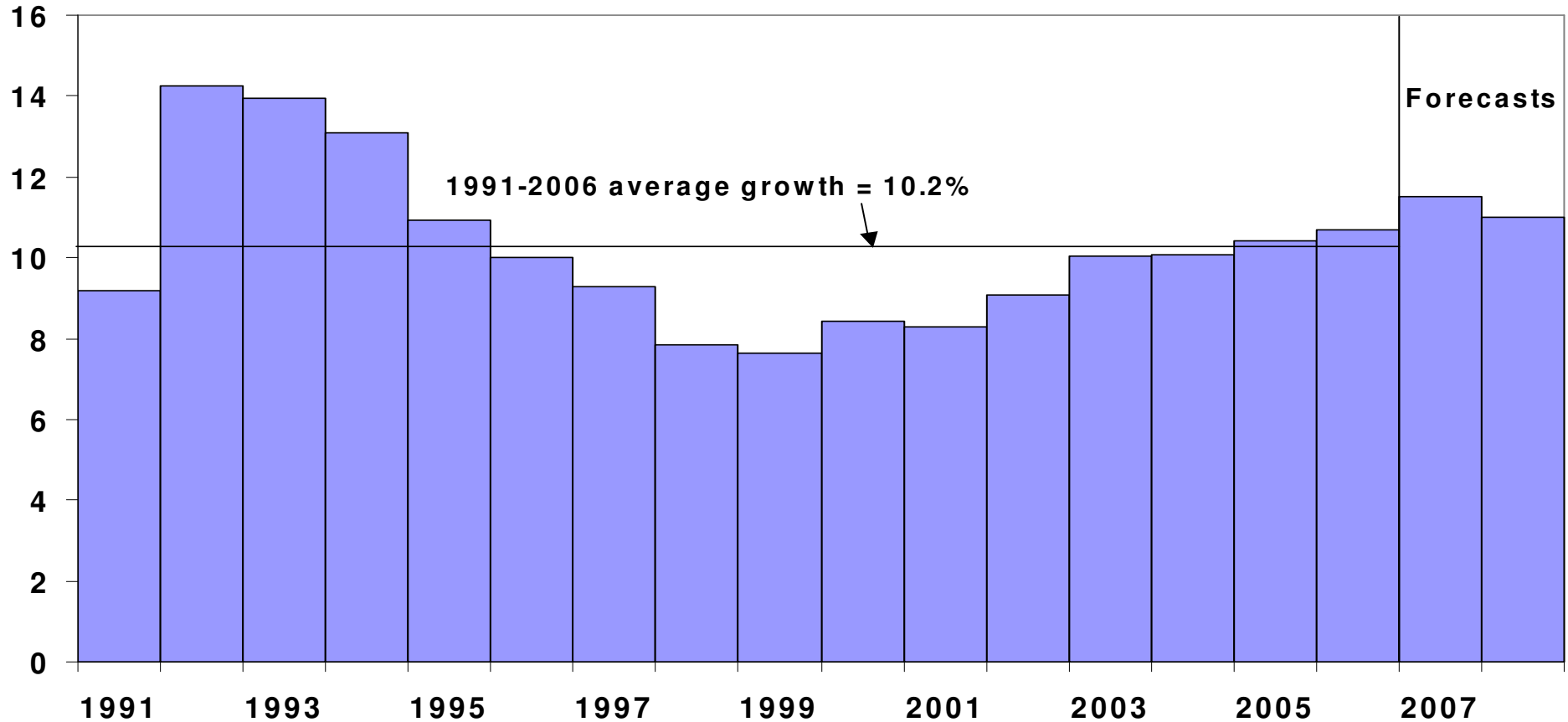
Global Economy - Key Themes

Another Solid Year for Global Growth.... But to Slow

- Global Growth Solid, but to Slow to around Trend
- US Growth - Set to Slow (Downside Risks!)
- Japan - Slowdown has Arrived
- Euro-Zone - Moderating Growth from Stronger Base
- China & India - Expected to Remain Strong

Chinese Economic Growth

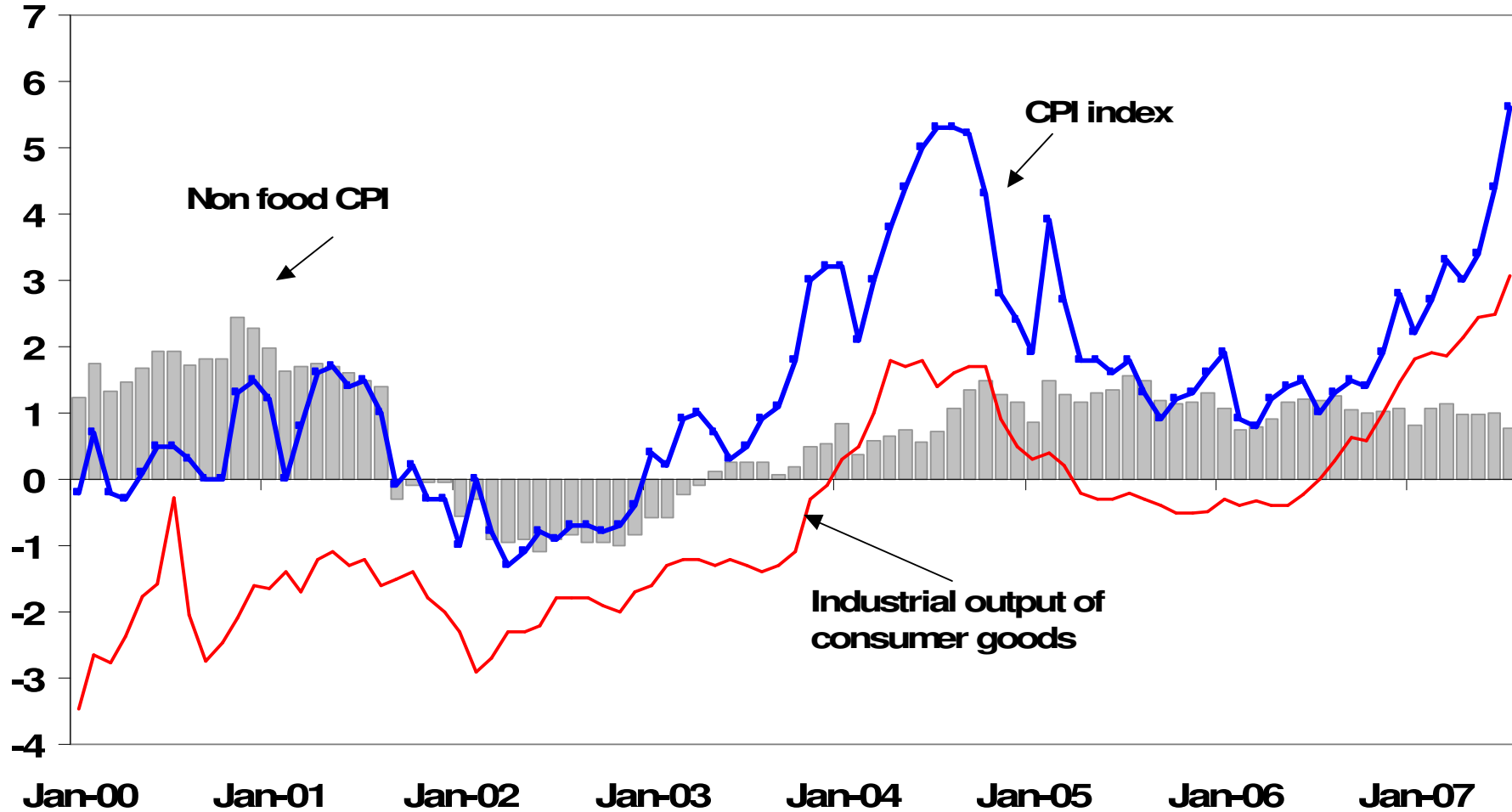
Economic growth in China



- Tighter policy (& slower global growth) may start to slow the economy a touch in 2008
 - But, given momentum (plus Olympics), hard to see slowing

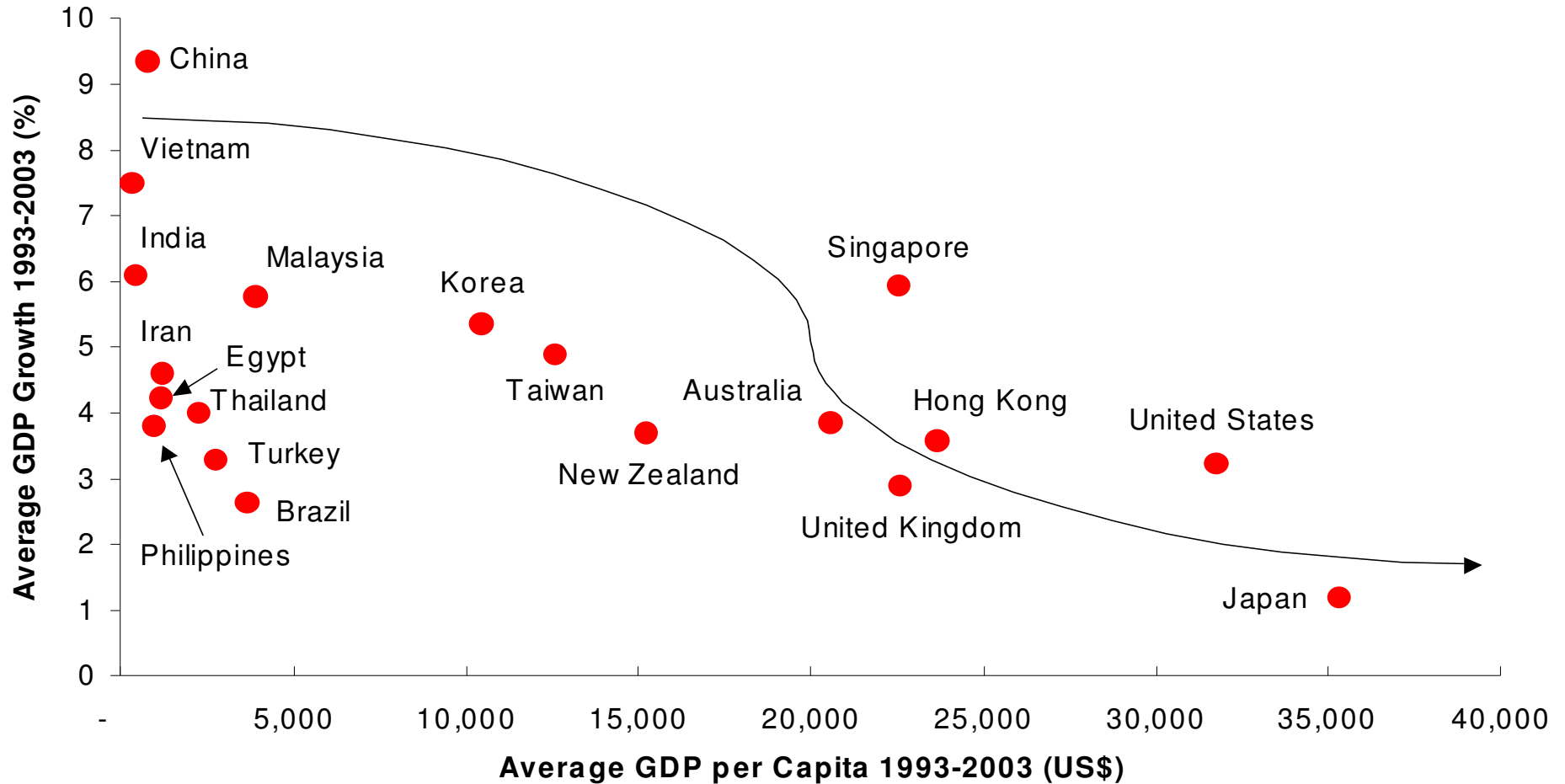
Chinese Inflation % yoy

Consumer price inflation



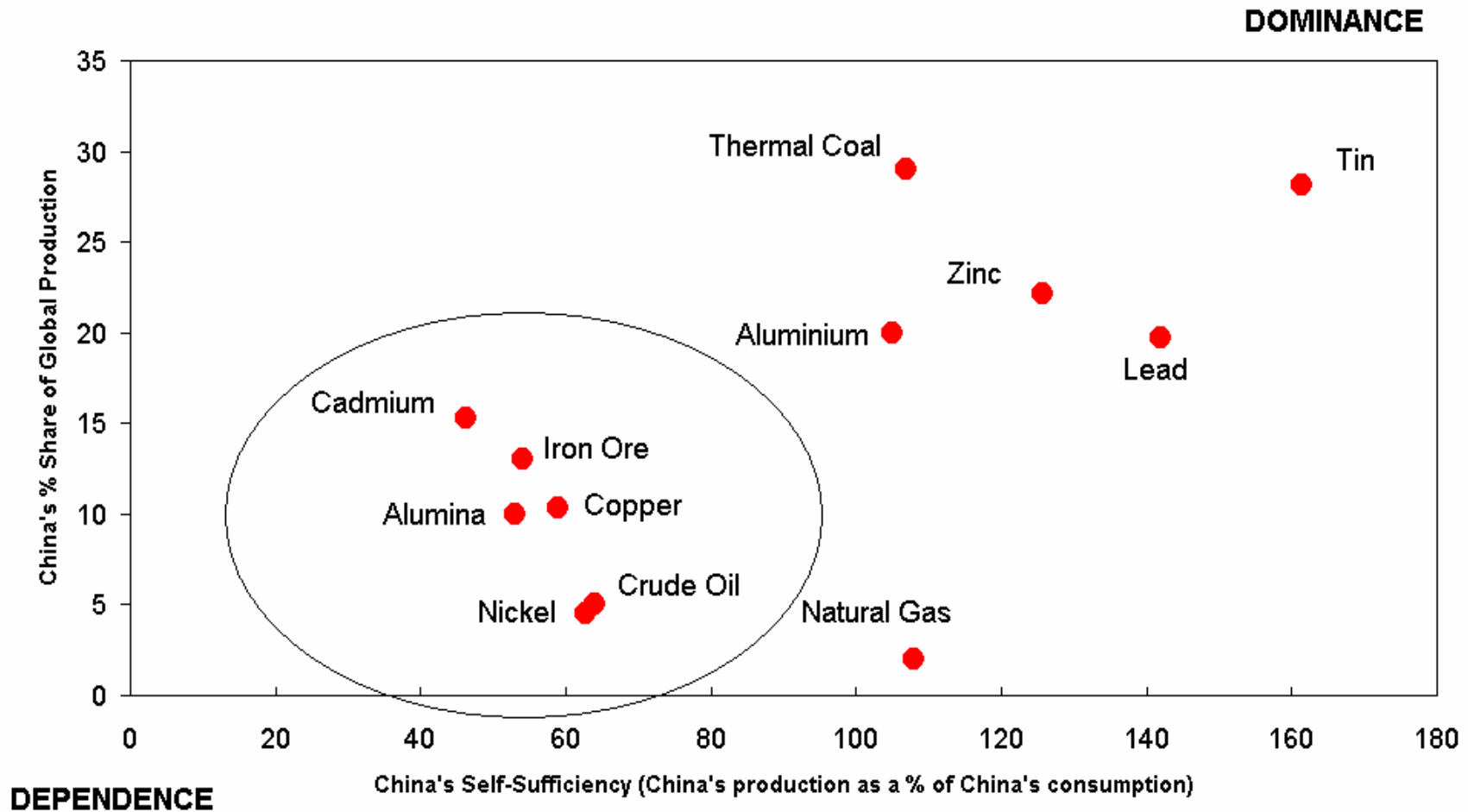
Long-term Growth Prospects of Trading Partners

Income & Real GDP Growth: Averages 1993-2003

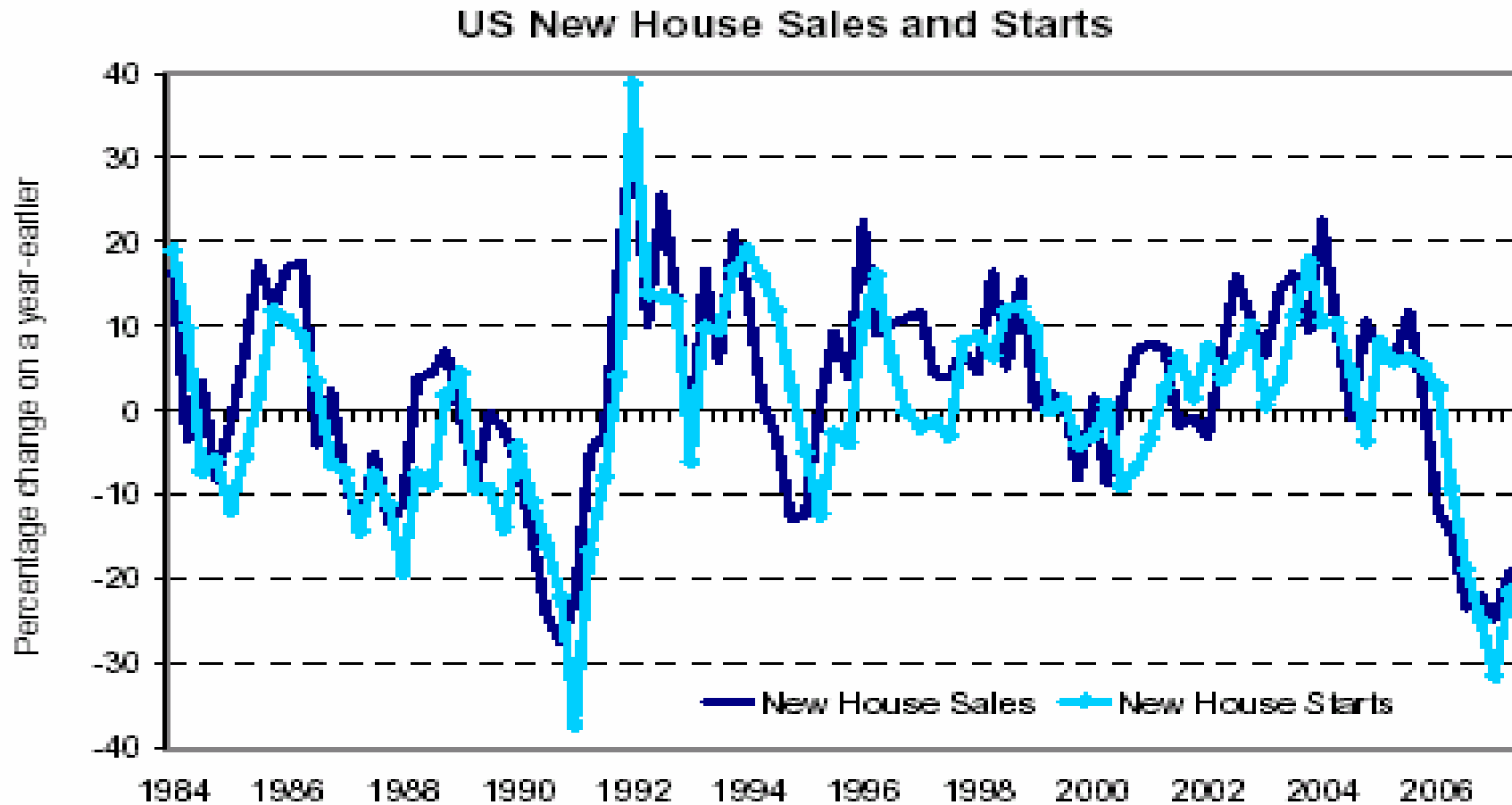


China & Commodity Markets

China's Influence in Selected Commodity Markets

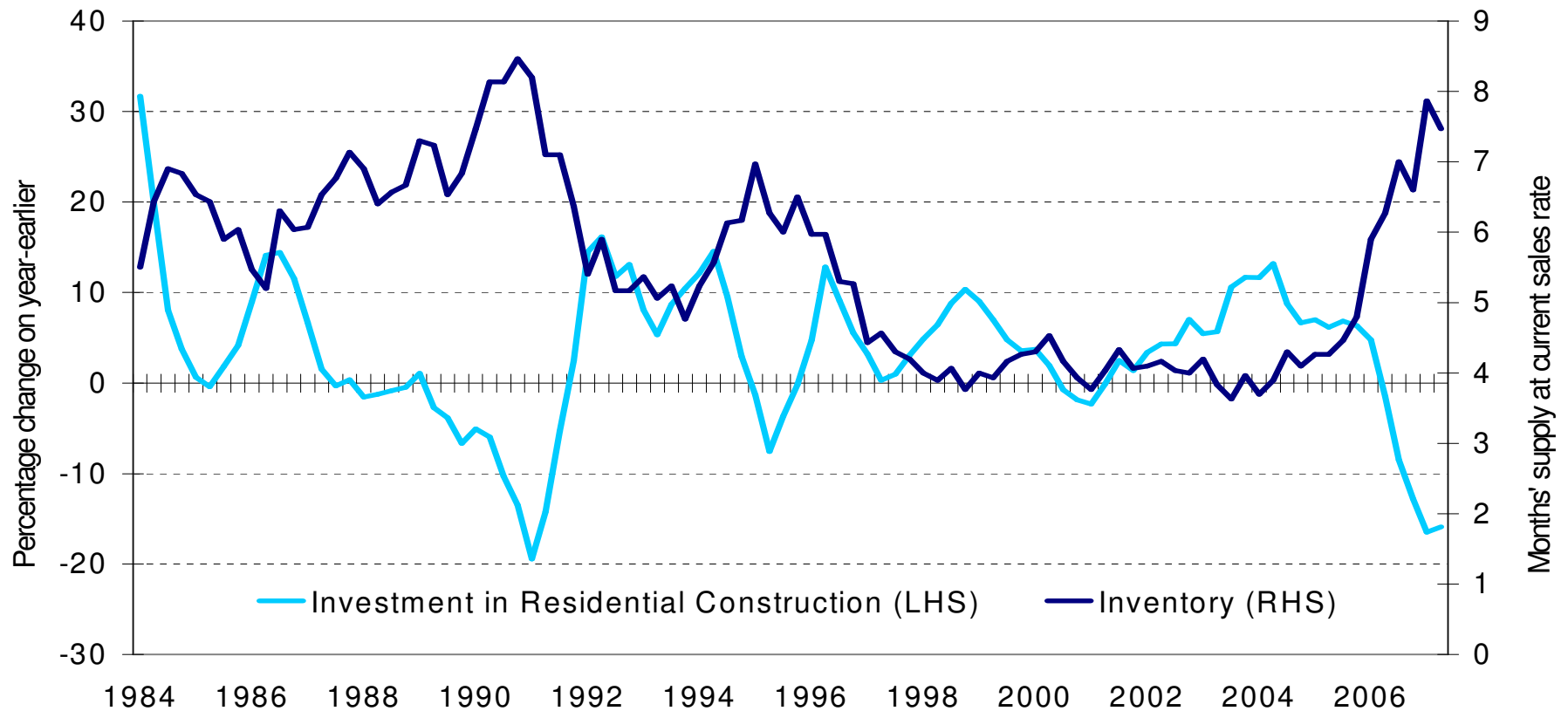


US housing construction – an increasing drag on GDP growth in the second half of 2007



Fundamental Overbuilding of US Housing

New Housing Inventory and Residential Fixed Investment



Dwelling construction down by 20% over the past year. Started in the Sept 2006 accounts. Worth best part of 1% off growth.

Sub Prime Defaults

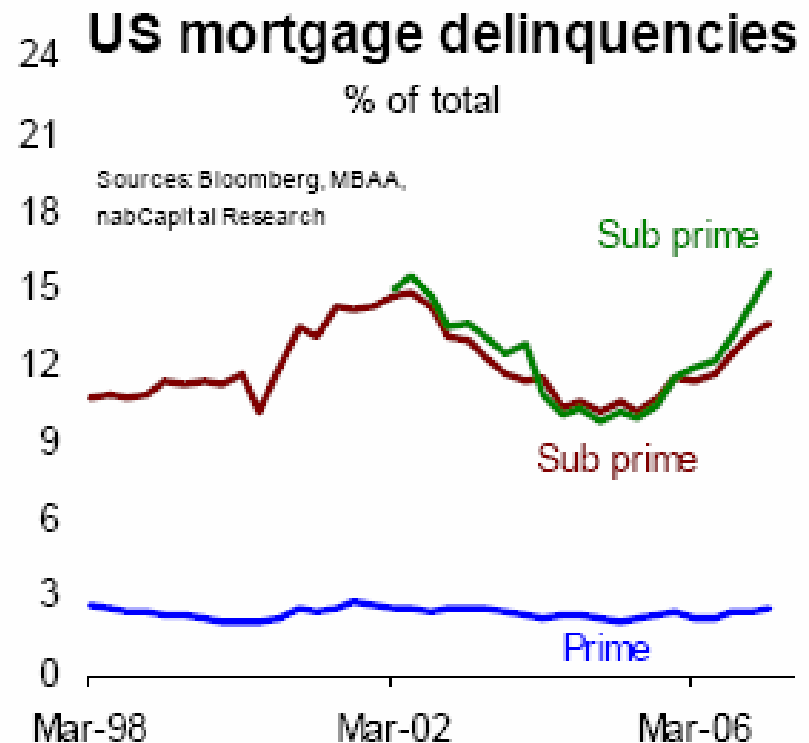
➤ Sub prime defaults.....

- A big market around 15 % of the total US mortgage market
- Current estimates as much as 20% in arrears (Country wide the largest lender in US said its sub prime is now 25% impaired)

➤ Key driver is adjustable rate mortgages (ARM's).....

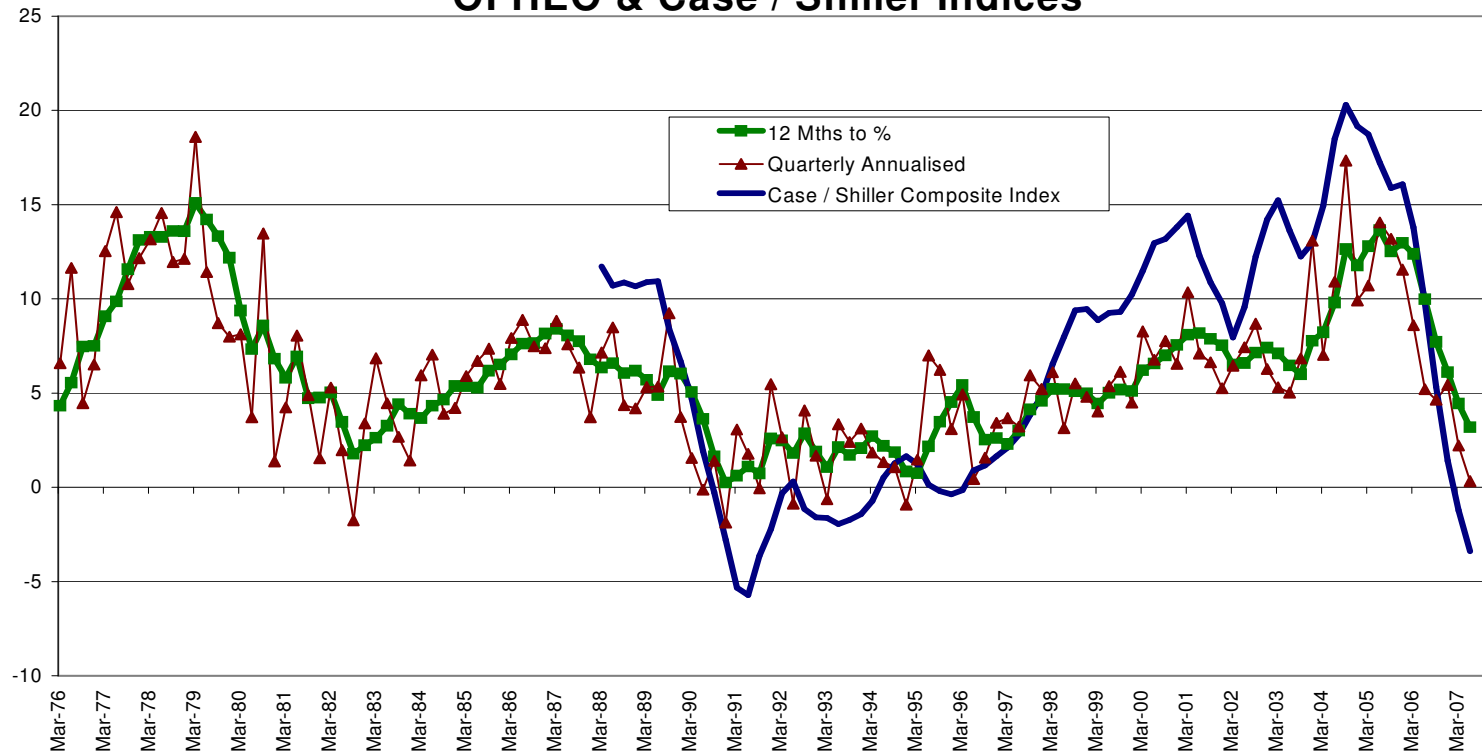
ie. deep discount for a couple of years now rolling off to full fixed loans (rates up from say 3% or lower to 6 1/2 - 7%)

Concern that it will spread to prime market. Have seen cocktails of prime / sub prime.



House Prices and their Impact on Consumer Spending

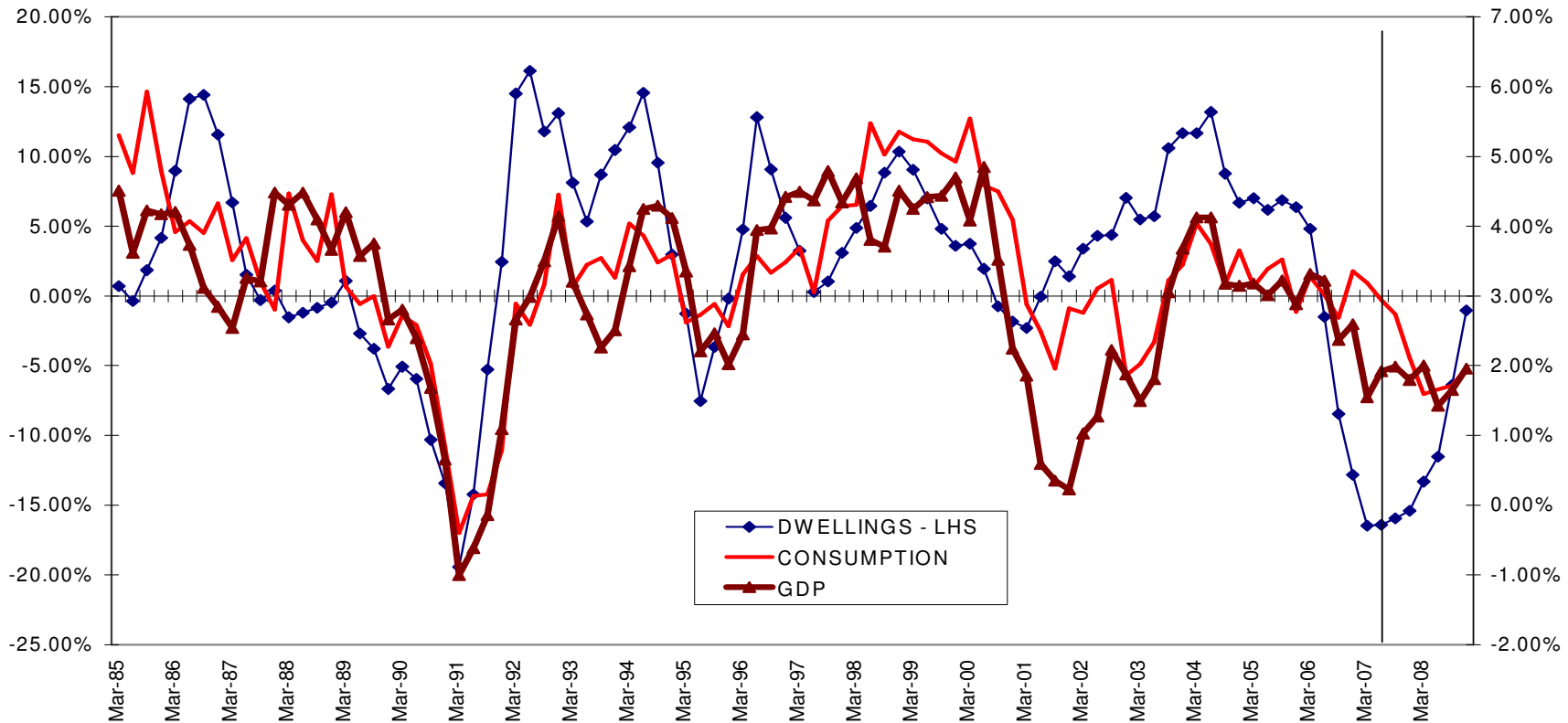
USA House Price - Quarterly & 12 Mth to %
OFHEO & Case / Shiller Indices



- House prices have gone from 15% growth last yr (fastest rate since 1979) to 0 or lower.
 - Our Assumption: House Prices slow to -2 to 5%;
- Note: a 10% slower rate of growth in house prices lowers growth in consumption by 1%.

Where do we think the US is heading?

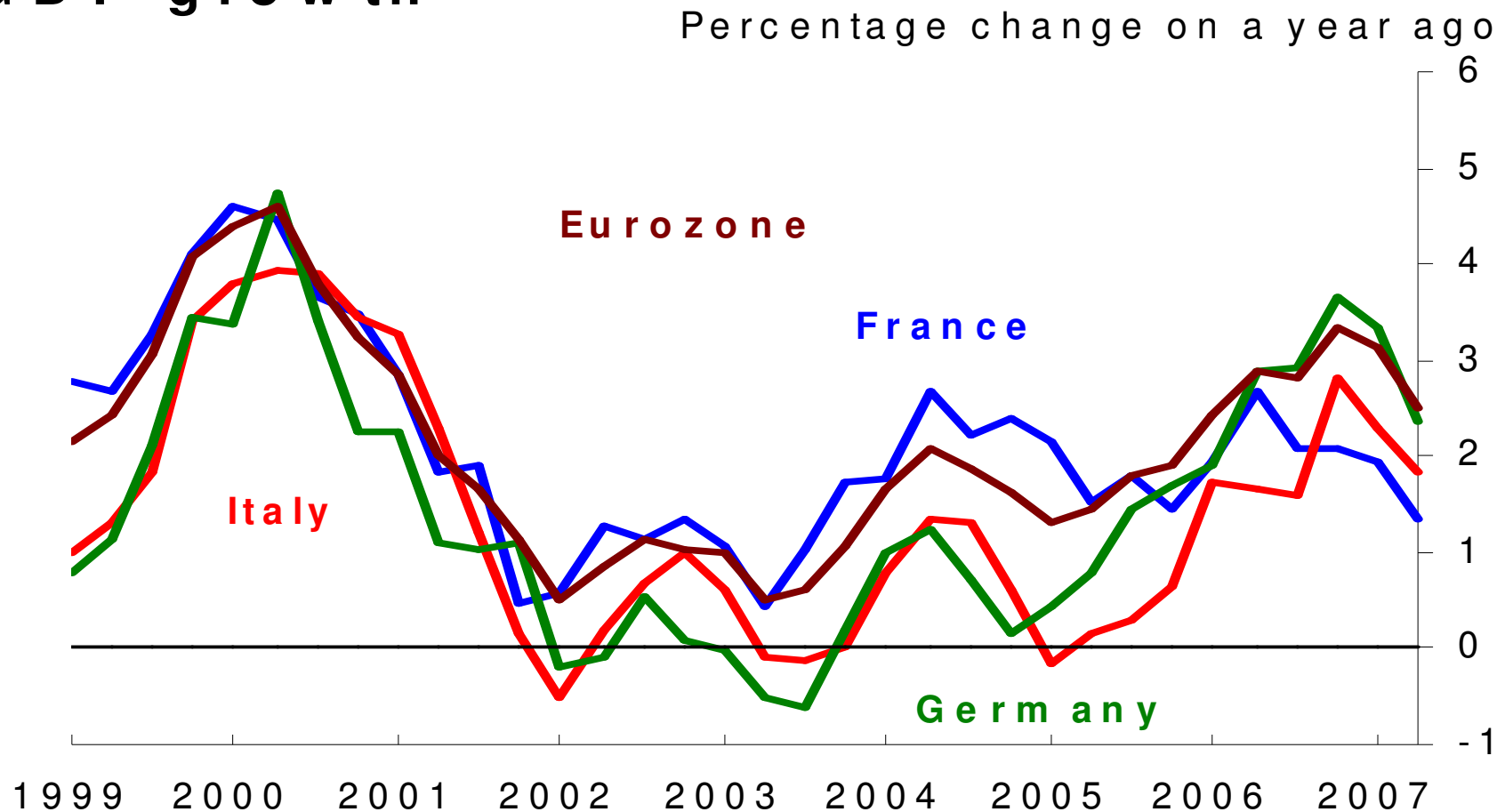
DRIVERS OF US ACTIVITY - Consumption Dwellings and GDP
12 Mths to %



Drawing all together we now only expect growth of around 1 ¾ % over the next 18 months - i.e. growth recession. Liquidity crunch not helping but not the main dynamic.

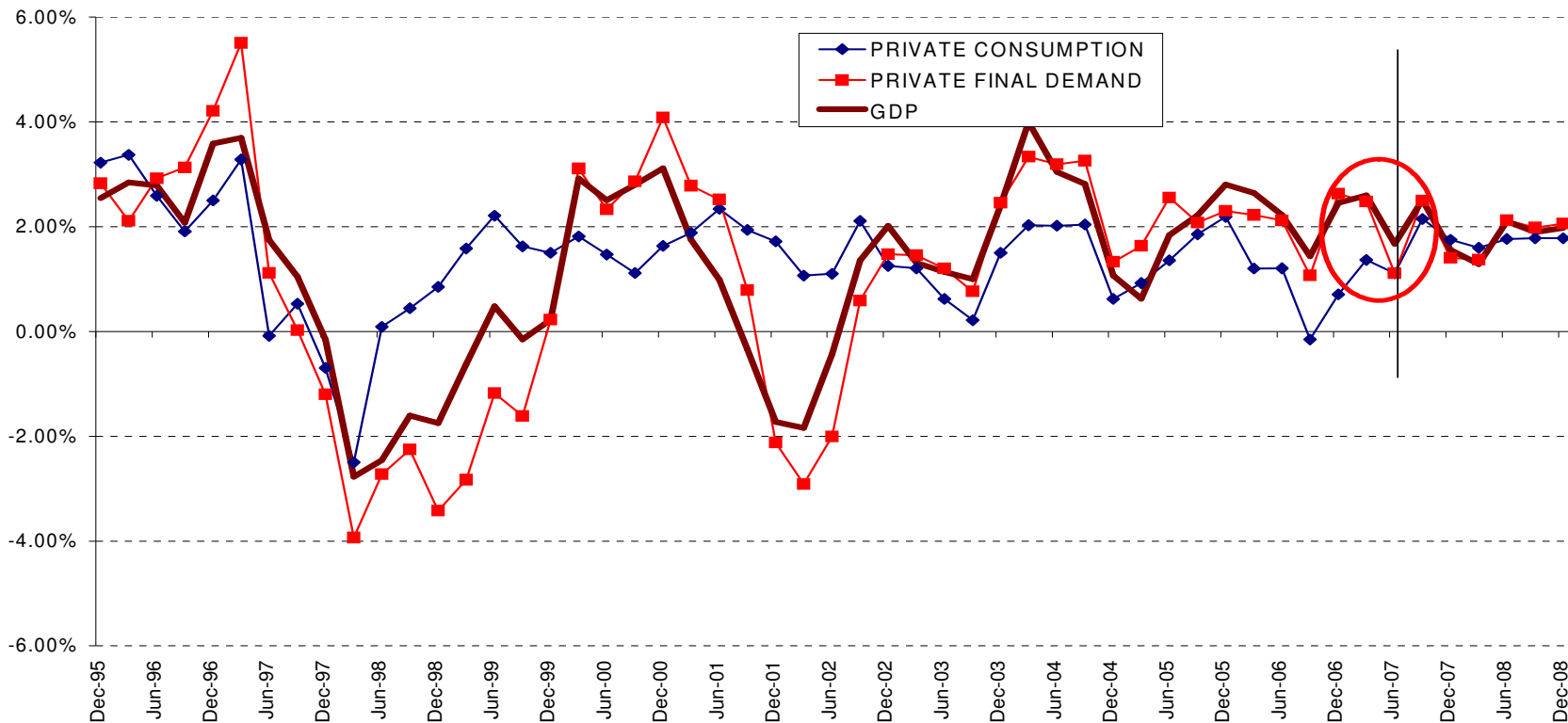
Signs of Slowing in Europe – Albeit from Reasonable levels

GDP growth



And Japanese growth slowed surprisingly in June qtr.

Consumption & Private Demand - 12 Mths to % Actual & Forecasts



- Driven by lower investment
- Now expect only around 2% from here over the next year.

Global Growth Forecasts

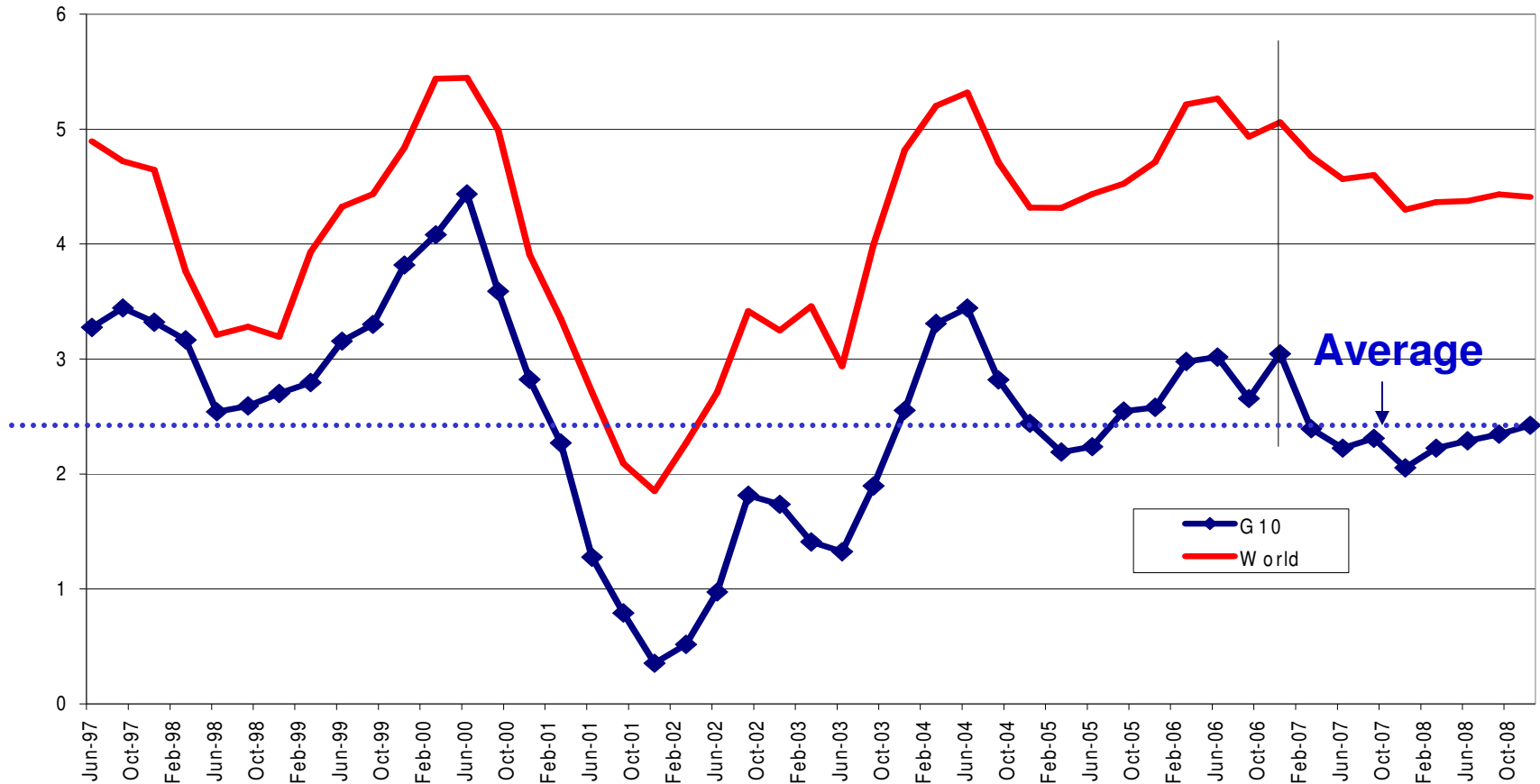
Global GDP Forecasts

December year annual average % change	2004	2005	2006	2007(f)	2008(f)
US	3.9	3.2	3.4	1.8	1.8
Japan	2.7	1.9	2.2	2.0	1.8
UK	3.3	1.9	2.8	2.8	2.0
Eurozone	1.8	1.5	2.9	2.7	2.0
Canada	2.9	2.9	2.7	2.1	2.4
Australia	3.8	2.8	2.7	4.2	3.8
New Zealand	4.4	2.1	1.7	3.0	2.3
China	10.1	9.9	10.7	11.5	10.3
India	7.3	8.7	9.1	8.5	7.8
World	5.0	4.5	5.1	4.7	4.2
Non-Japan E Asia	8.8	8.2	9.1	9.4	9.4
Latin America	5.5	4.1	4.7	4.5	4.2
G10	3.0	2.4	3.0	2.2	1.8

At peak in 2006 and still good in 2007. Slowing in 2008 but still reasonable.
However very much driven by China. Will slowing US have more spill-overs than we expect?

G-10 v Global Economy

G10 GDP - 12 Mths to %

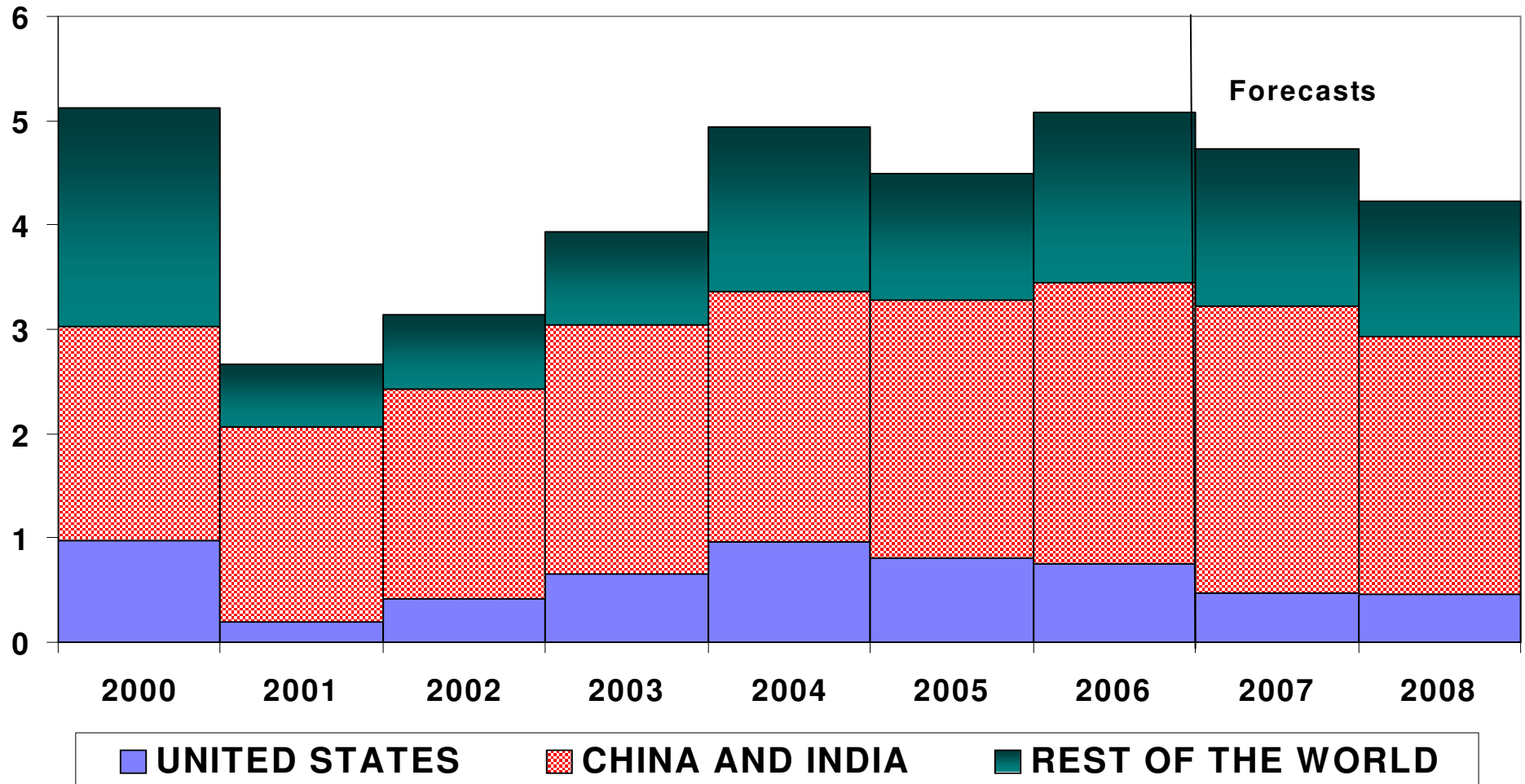


G-10 forecasts paint a more sober outlook than global economy (China & India).

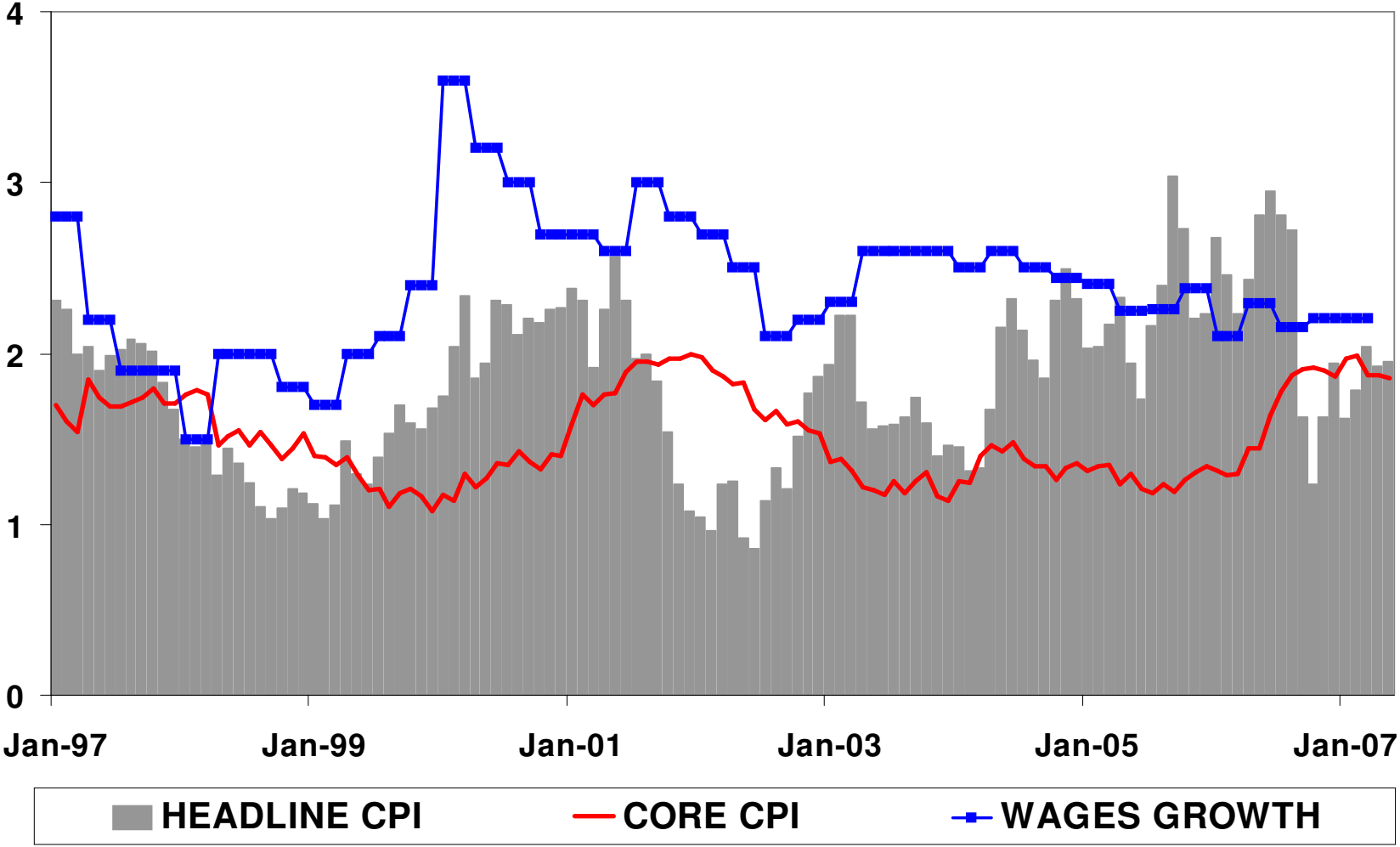
Global outlook for 2008 slowing to trend. G-10 now expected to be significantly sub trend and weak.

Geographic Sources of Global Growth

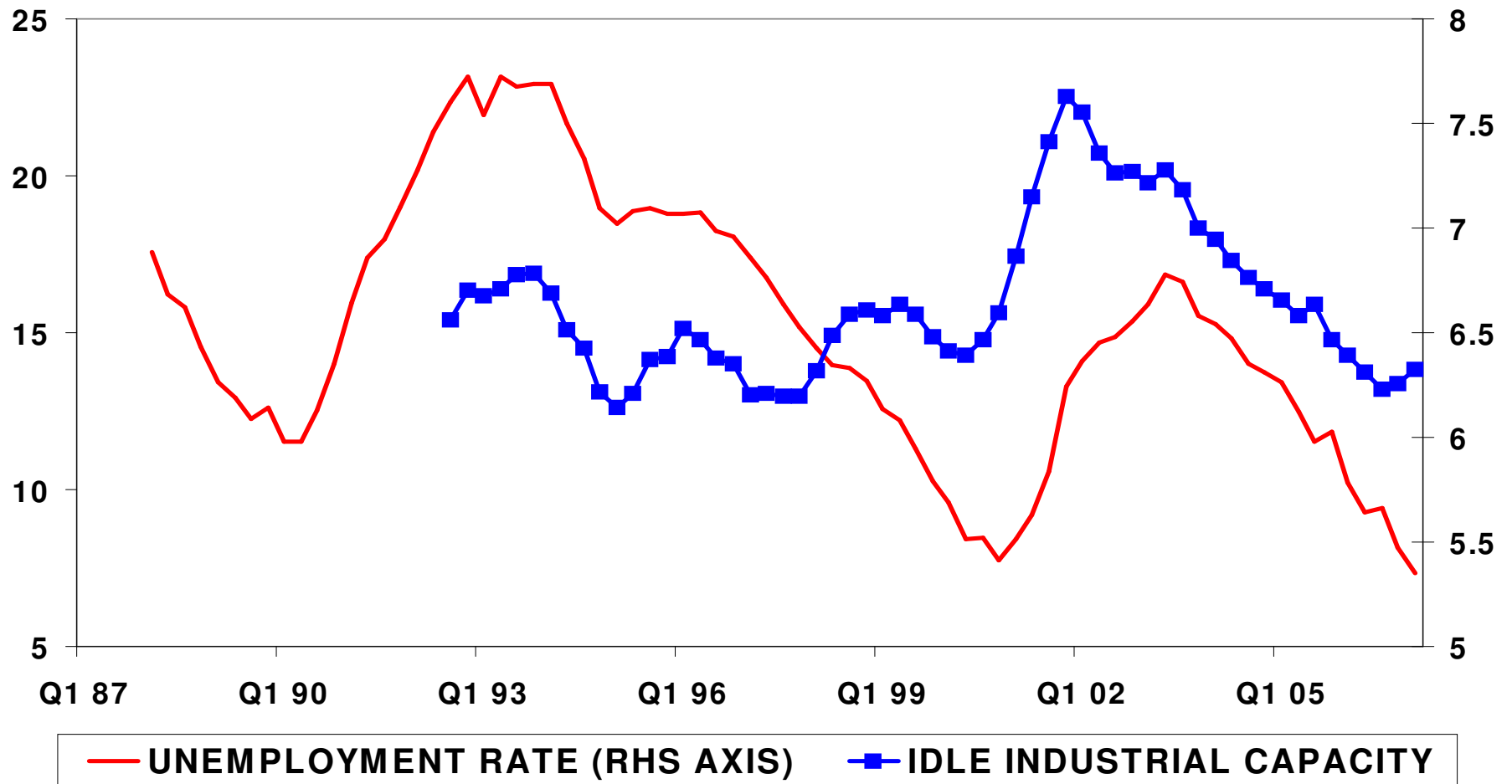
Geographic sources of global growth



Global Inflation Up ...Central Banks on Watch



G7 Capacity & Labour Market Pressures



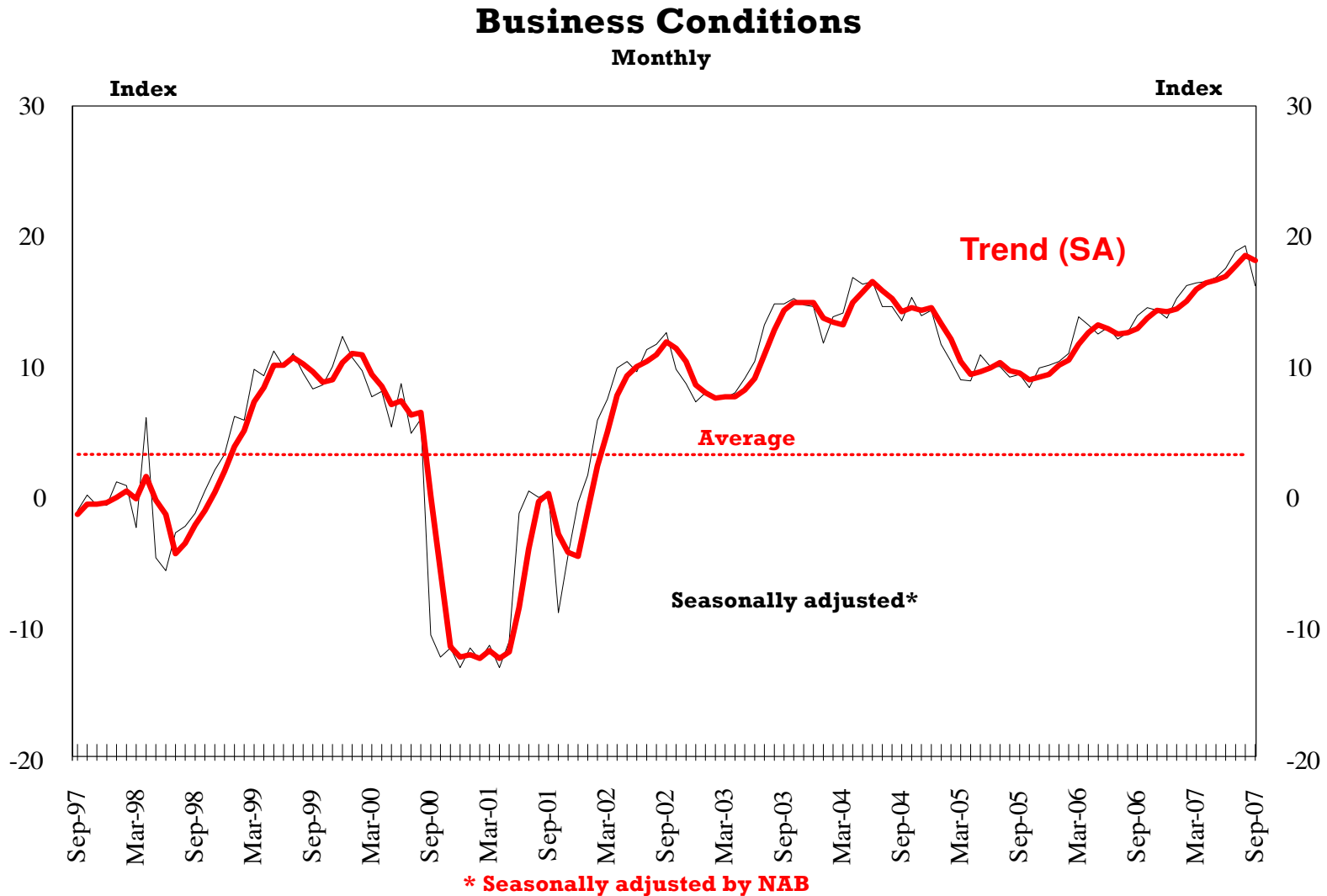
Australian Economy



Key Themes – Australian Economy

- To date, the Australia relatively unaffected by financial market turmoil.
- Record Commodity Prices Ease....But Slower Growth, Rising Costs....Smaller Gains
- Rebalancing of Growth/Activity
 - Household Spending Stabilises – Bit Below Average (incl. subdued housing activity)
 - Business Investment - Moderates to A Bit Below Average
 - Export Volumes Pick Up - New Resource Investment
- Overall, GDP Growth Sustained at About Healthy Trend
- Disparate Performances Across Business, Households & Regions
 - Mining v Farming etc,
 - WA v NSW, Western Sydney v Eastern Sydney, HINI's/Top End v Battlers
- Capacity Constraints (Labour mkt, water, infrastructure, construction, property, etc)
- RBA focus on Inflation Risks

Business Conditions



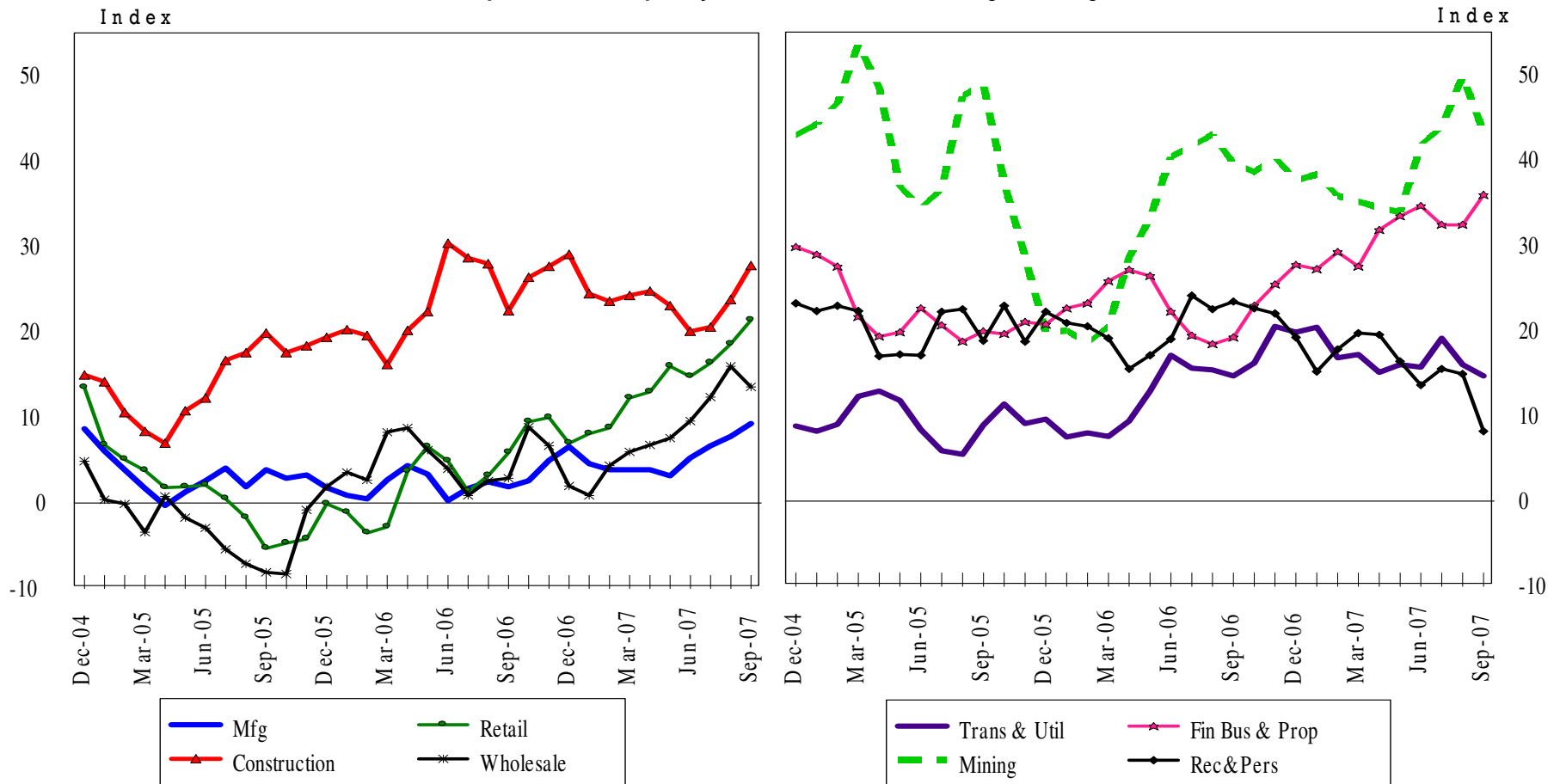
Source: Group Economics



Business Conditions by Industry

Business Conditions by Industry

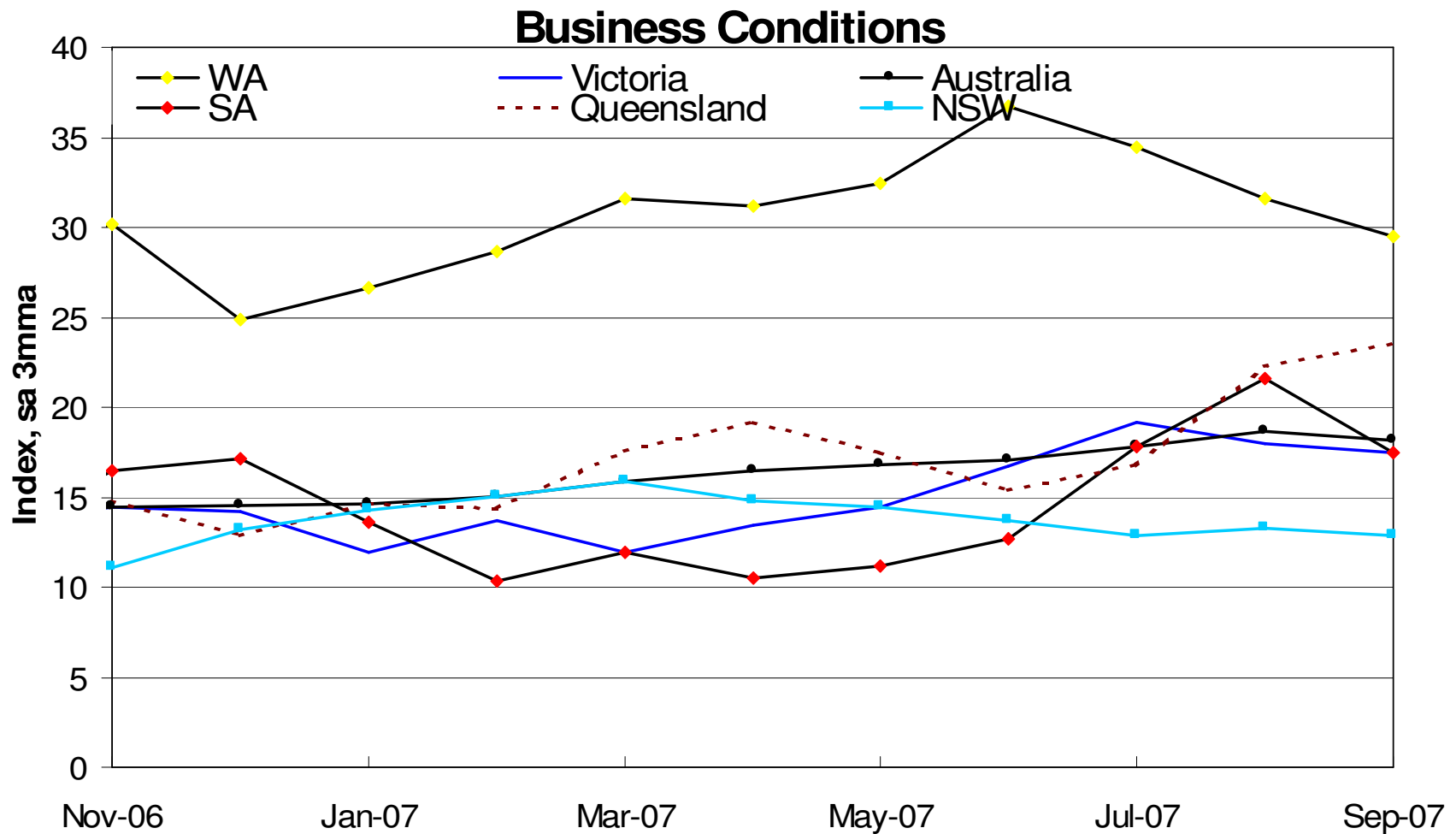
Monthly, Seasonally Adjusted 3 month Moving Average*



Source: Group Economics



Business Conditions by State

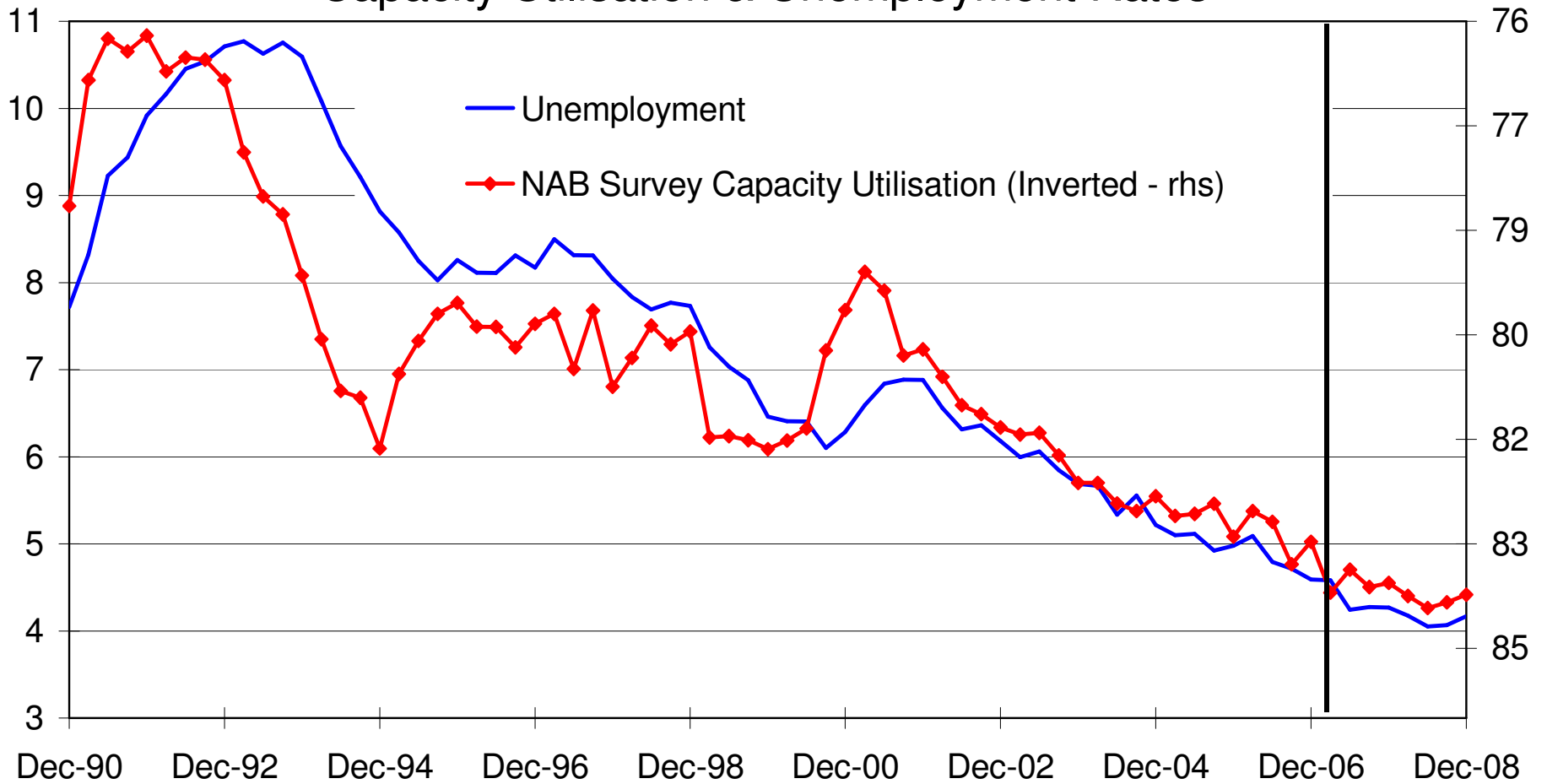


Source: Group Economics



Unemployment falls to 30 year lows

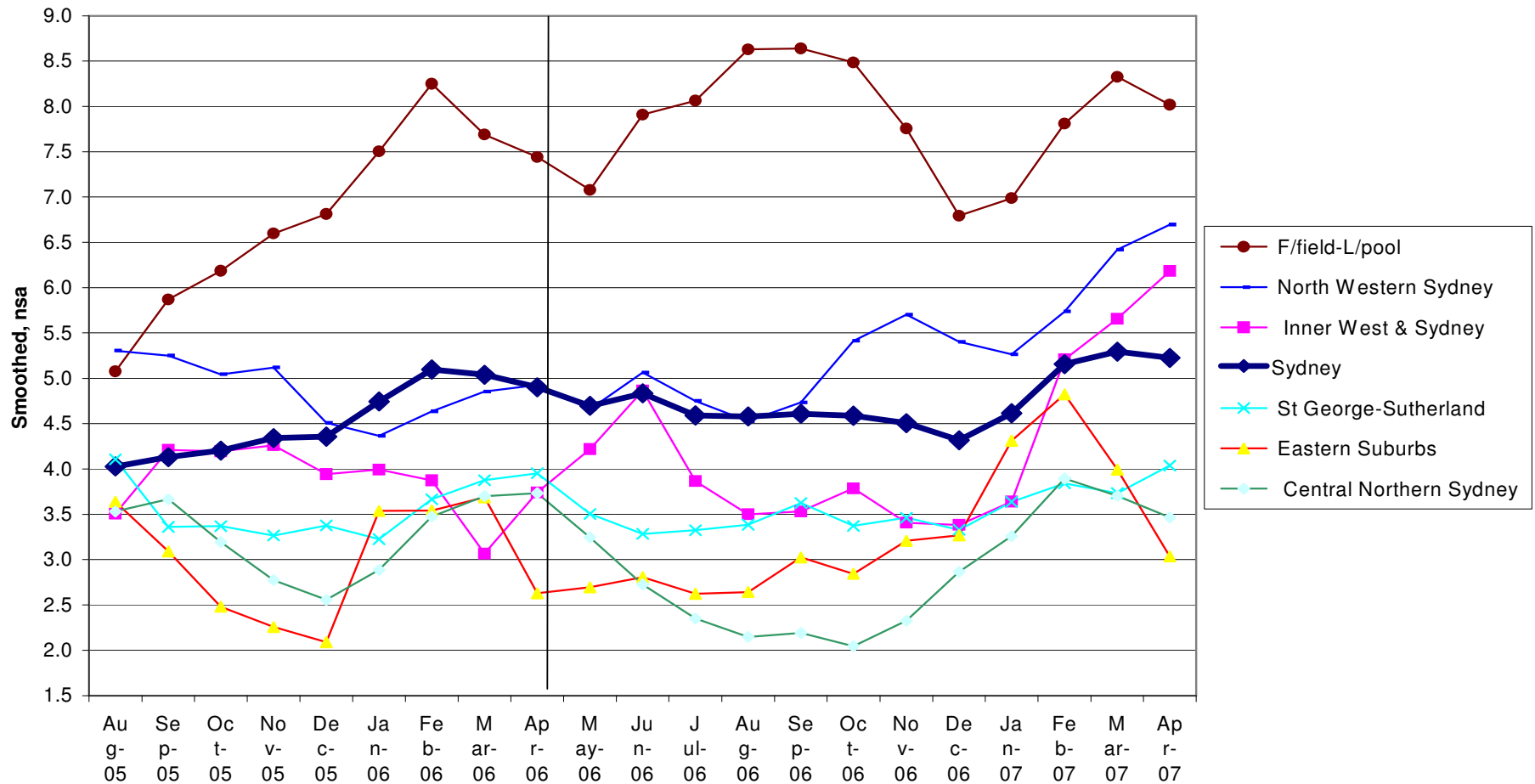
Capacity Utilisation & Unemployment Rates



Source: ABS, NAB Economics

Unemployment Low...But Disparate Eg. Sydney - West v East, State v City

Sydney Unemployment - Selected Regions



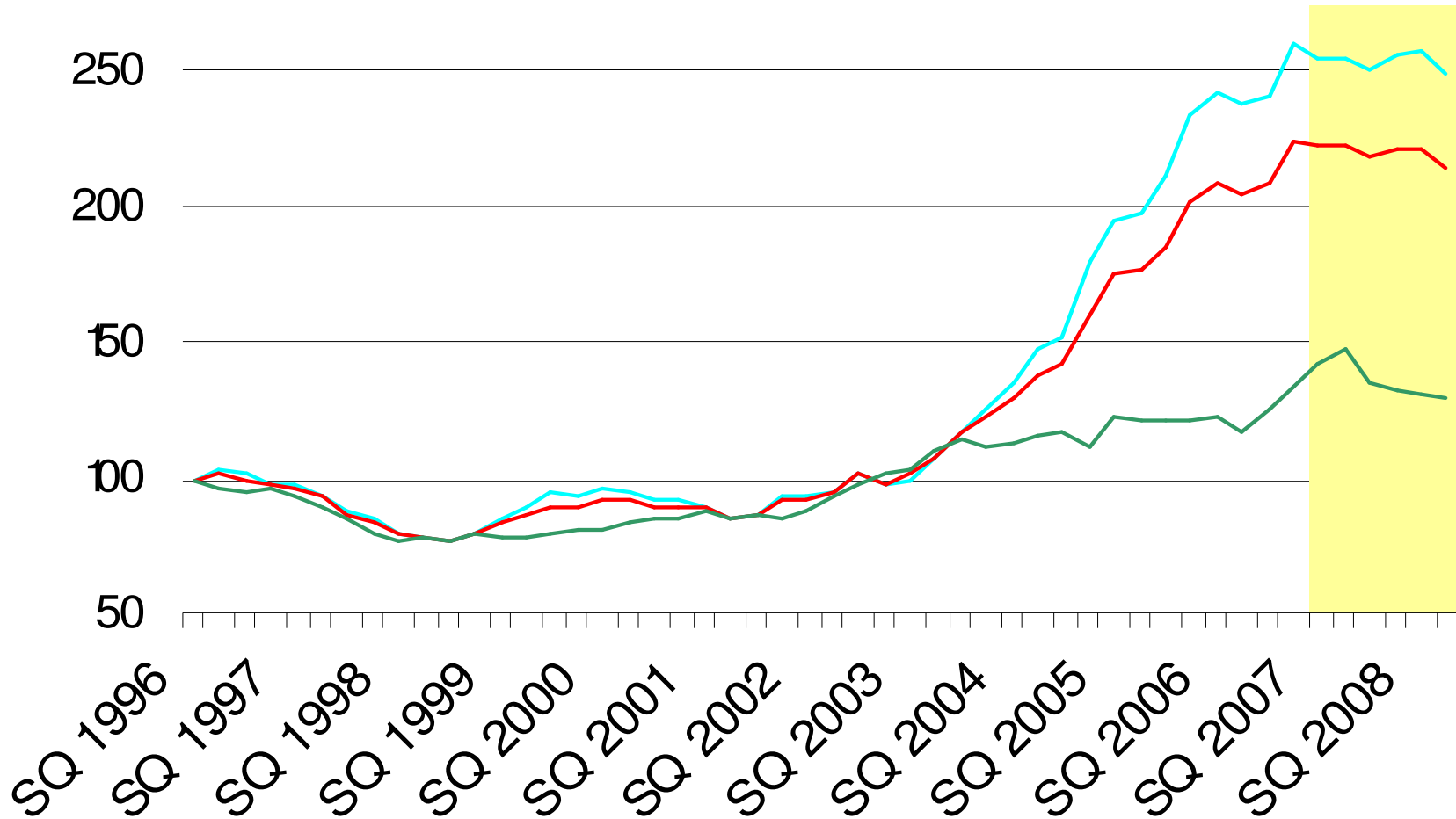
Source: ABS



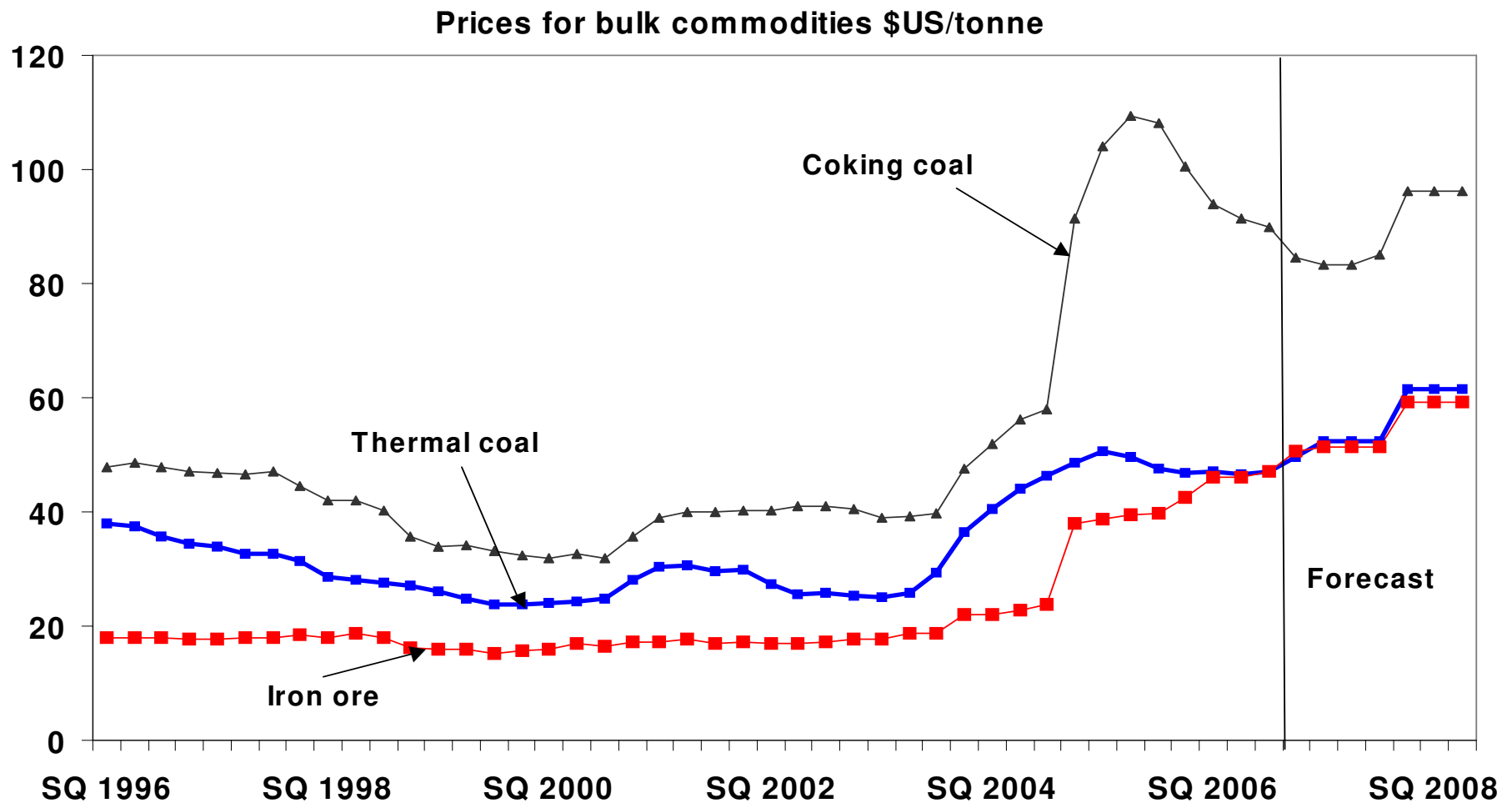
Strong World - Positive for Commodity Prices

US\$ Index

— Non-rural — Total — Rural



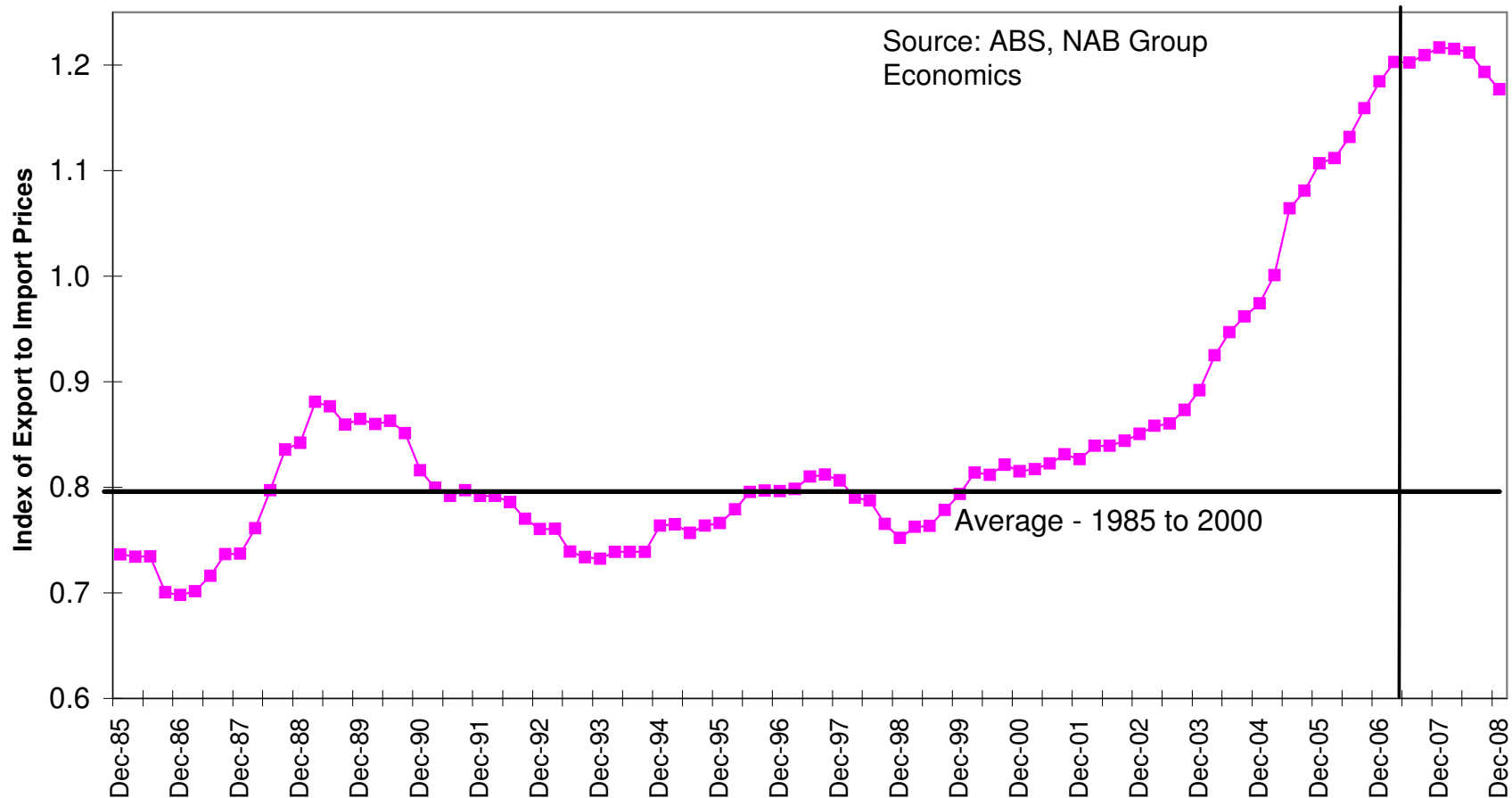
High contract prices for bulks sustain aggregate prices



Australian Terms of Trade...50 yr high

Australia - a net energy & other resource exporter....go China!!!

Australia's Terms of Trade

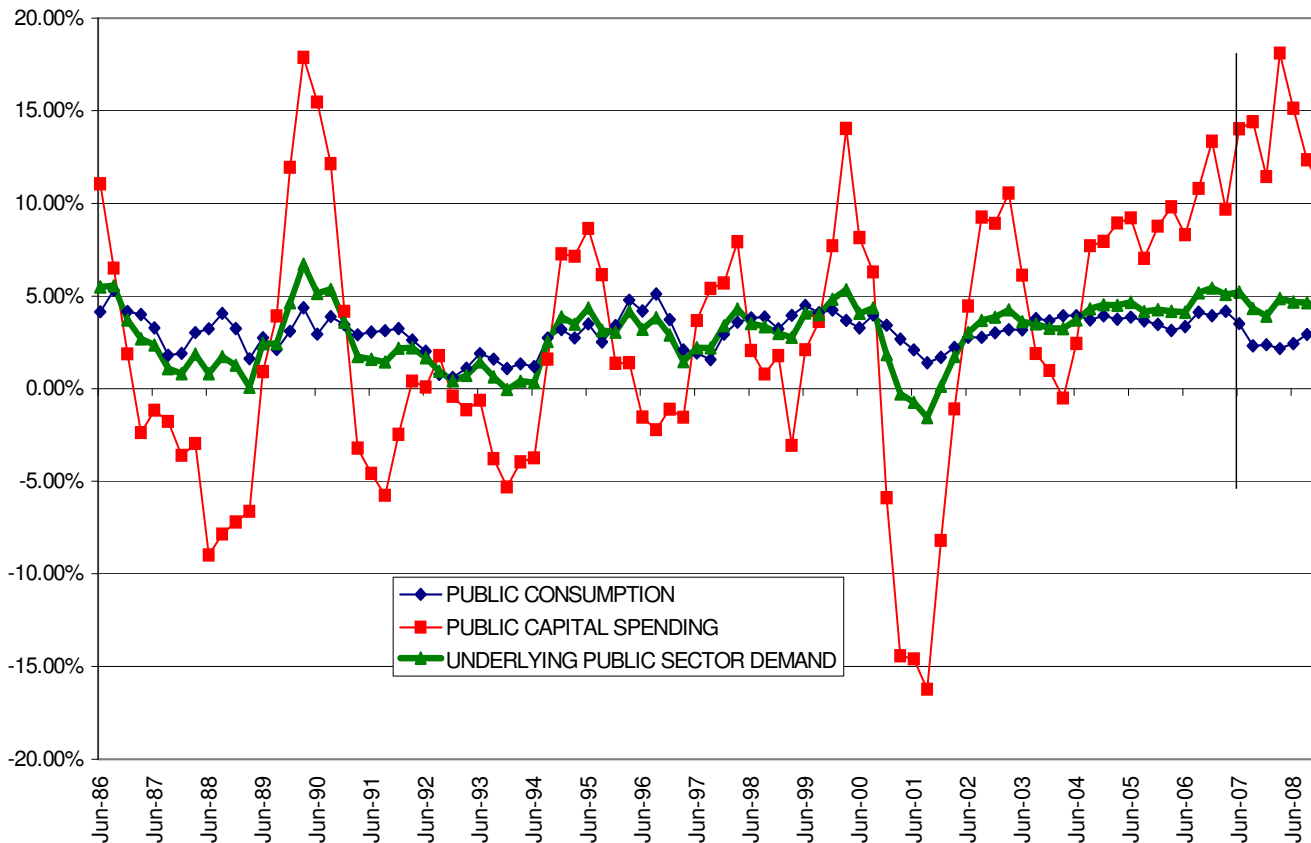


Australian terms of trade are expected to peak around current levels for next year then down 10 % per annum over next 2 years. But levels still firm.



Public Sector - very rapid growth – particularly in Capital Spending (especially in States).

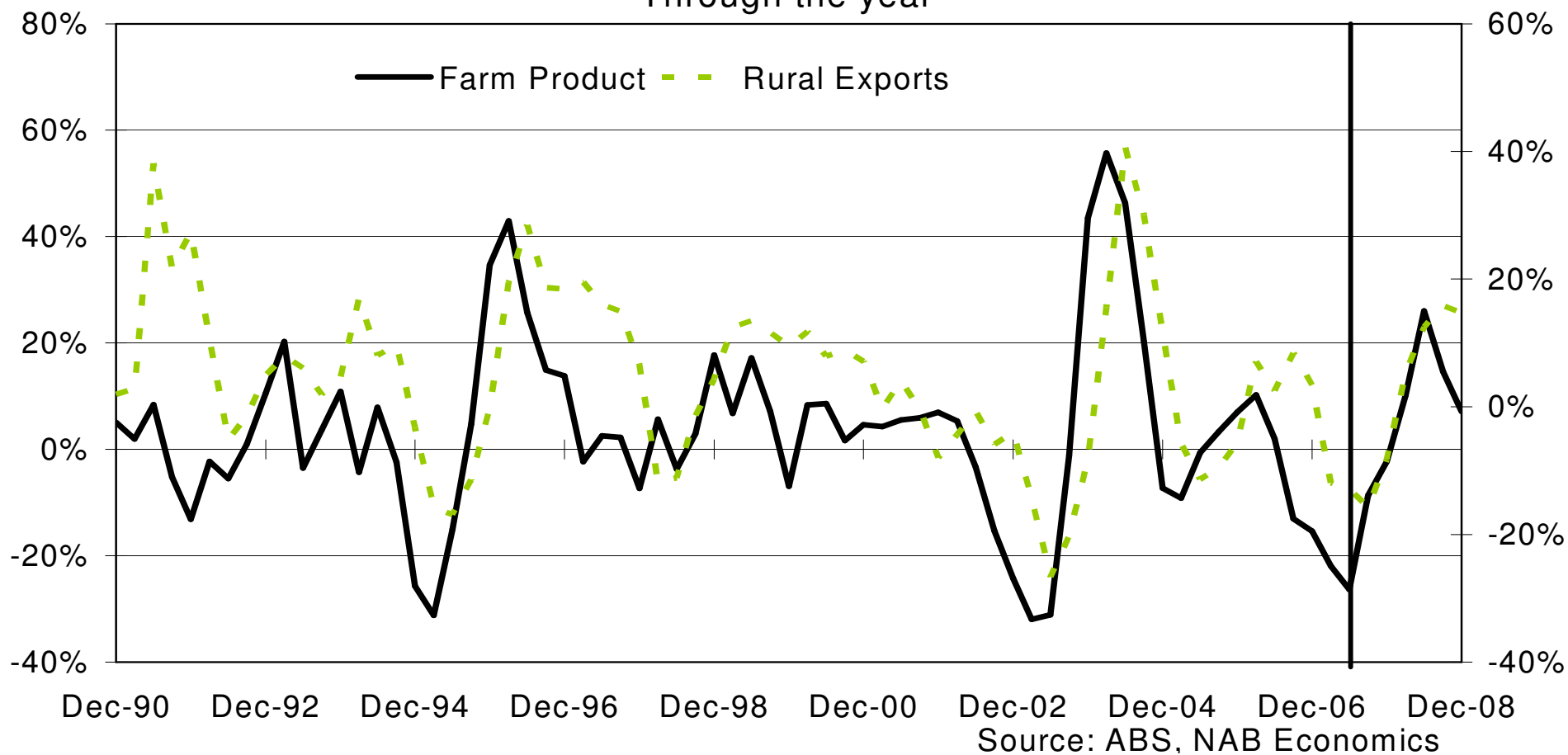
Public Demand - Annual Growth Rates%



- Underlying public demand at 5% And expected to stay there.
- Not equalled since 2000 Olympics and 1990s recession.
- This time capital orientated.
- State Capital spending up 15% in June qtr alone!!!

Drought Effects

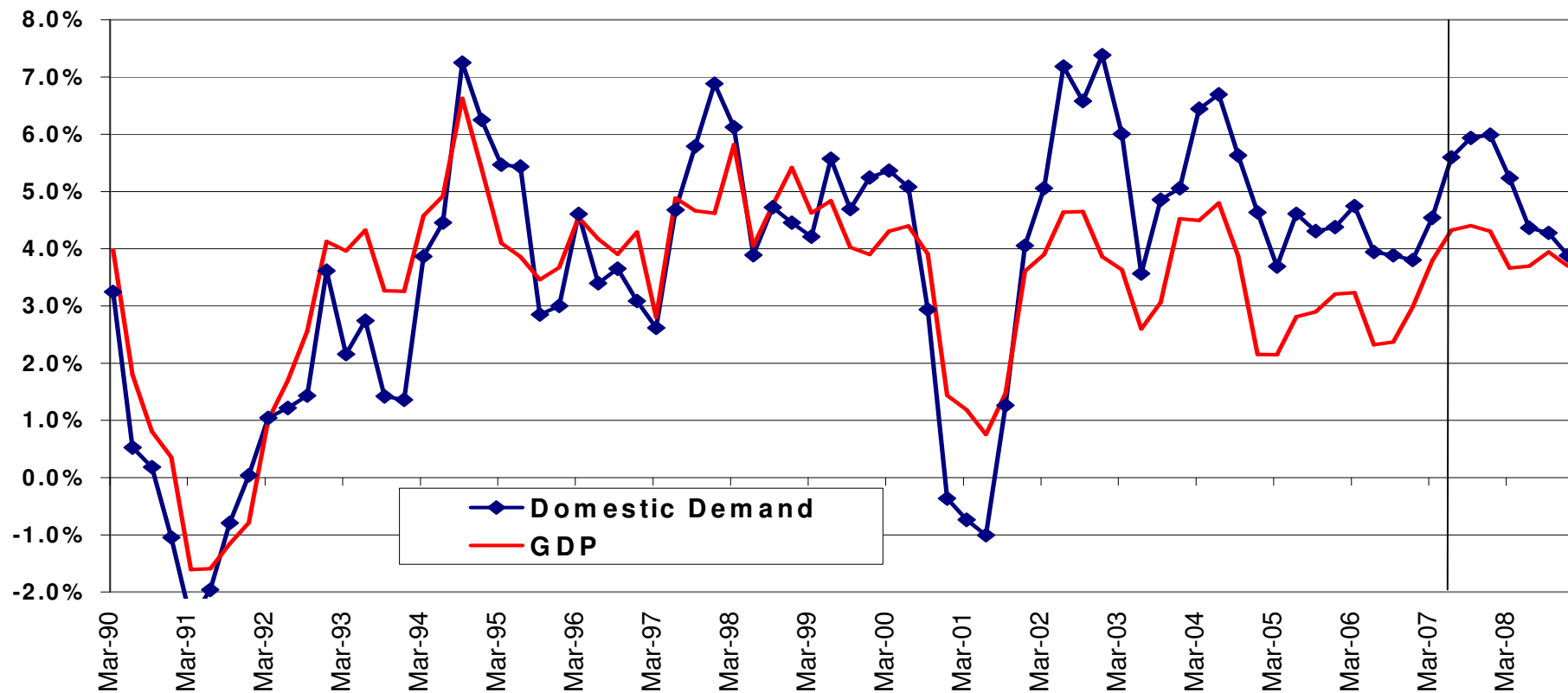
Drought Effects Through the year



Australia's Economic Outlook

Real Output & Domestic Demand

- 12 Mths to %



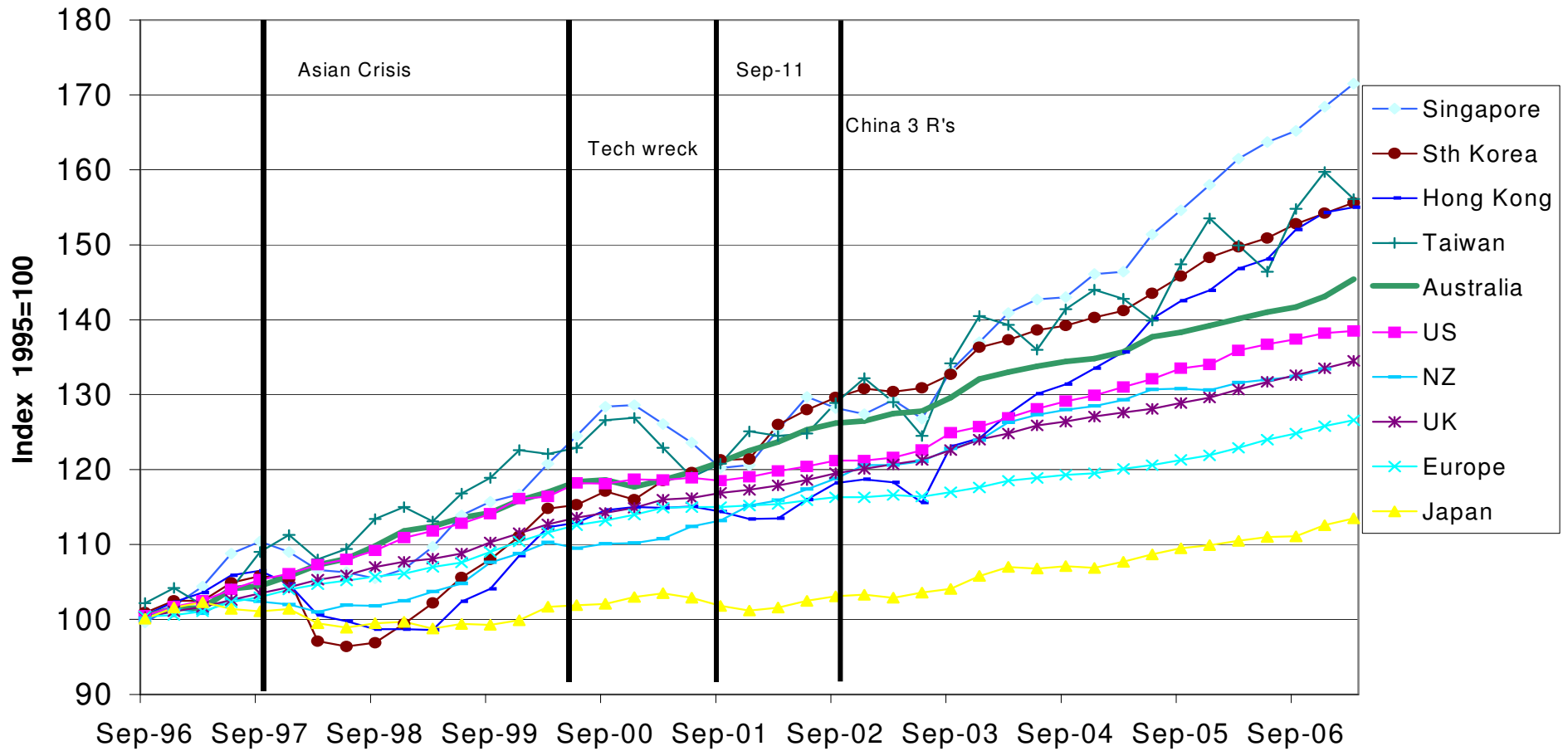
2007 we see growth at around 4 ¼ %.

Demand much higher – around 5 ½%. Non farm GDP around 4 ¾%

2008 around 3.8 % (higher housing construction & farm) but more normal growth in domestic demand.

International Growth Stakes

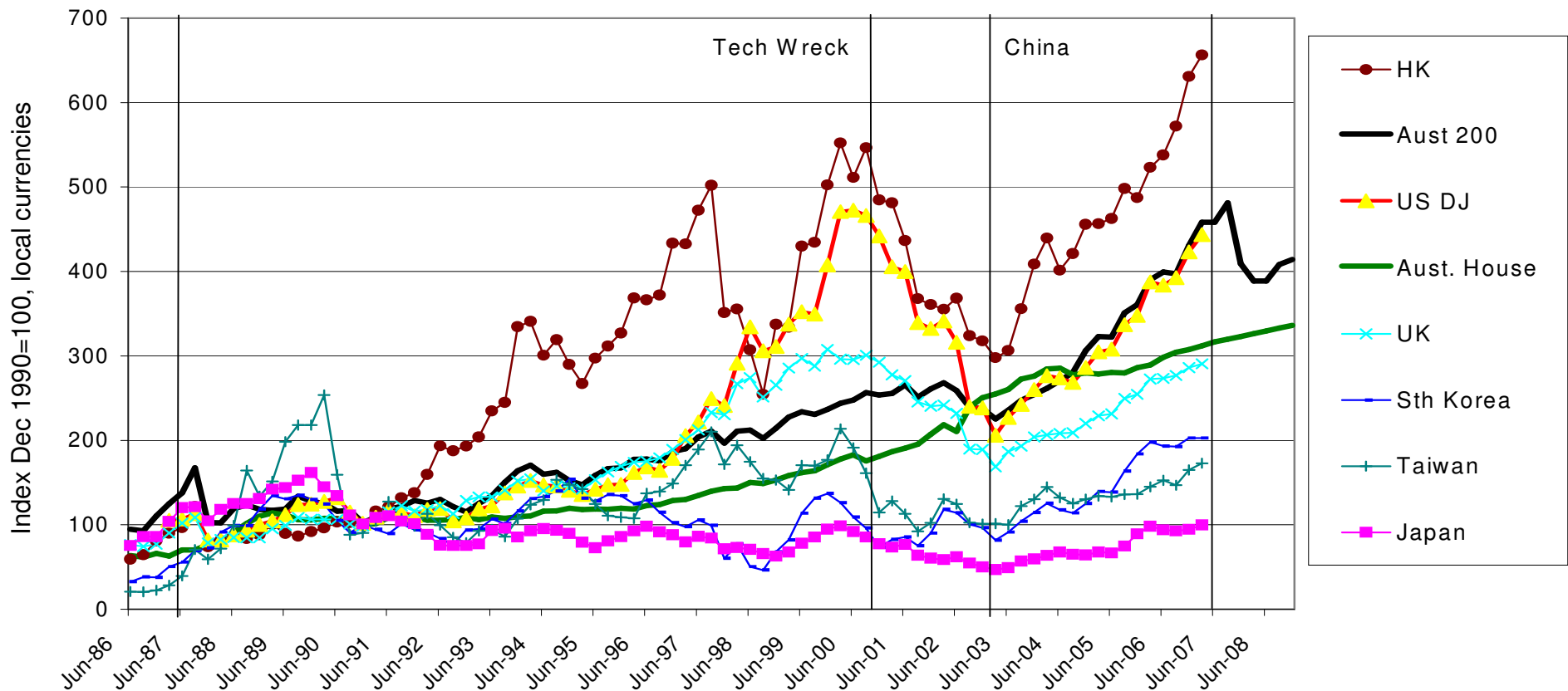
Real Output/Income (GDP) - Selected Industrialised Economies



Global & Australian share prices... Australia outstanding

➤ Slower Growth, Higher Costs & Interest Rates.....Smaller Gains, still impressive!!

Selected Global Share Prices v Australian Share & House Prices



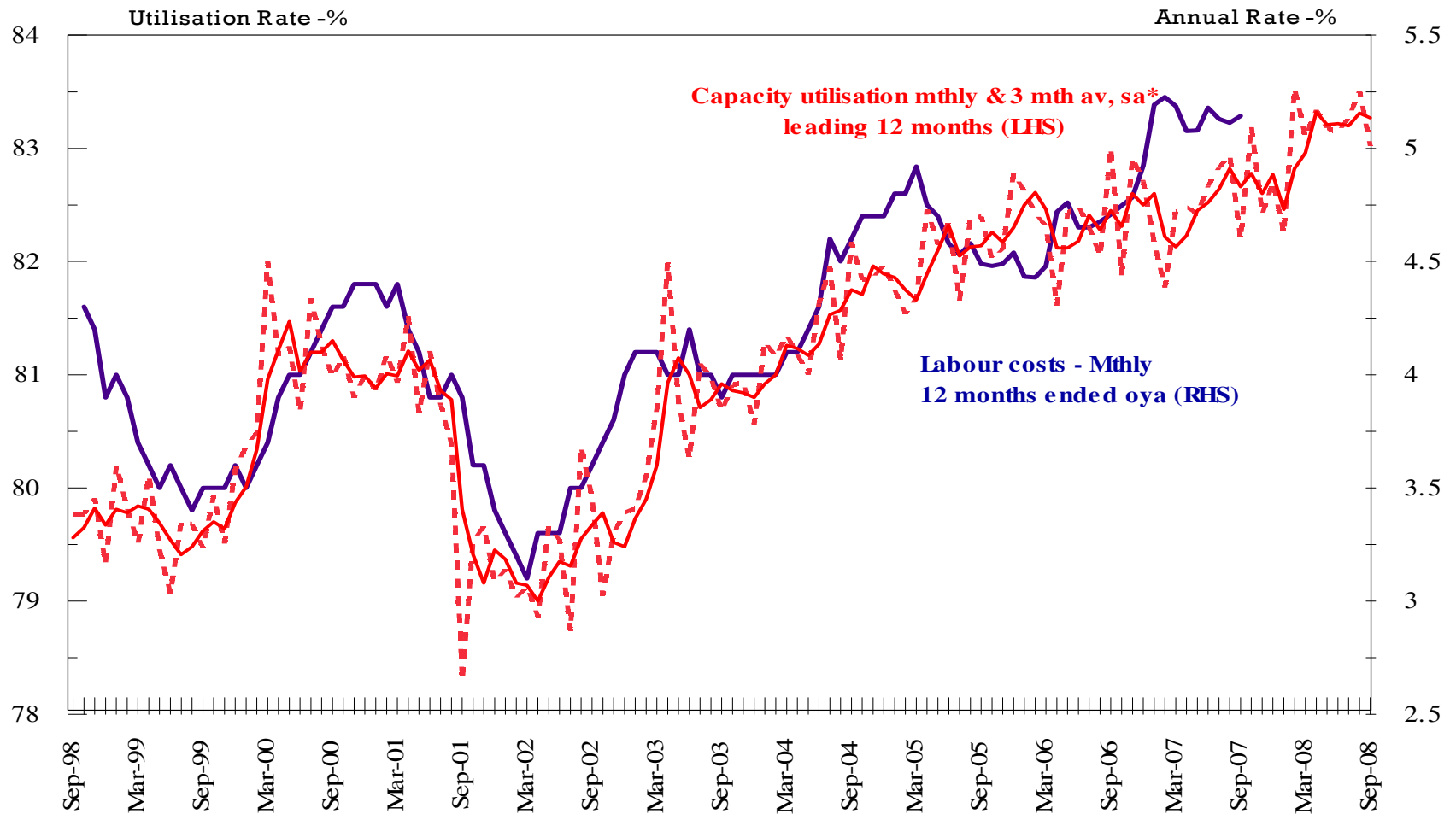
Financial Market Outlook



RBA ...On Guard.....Why?

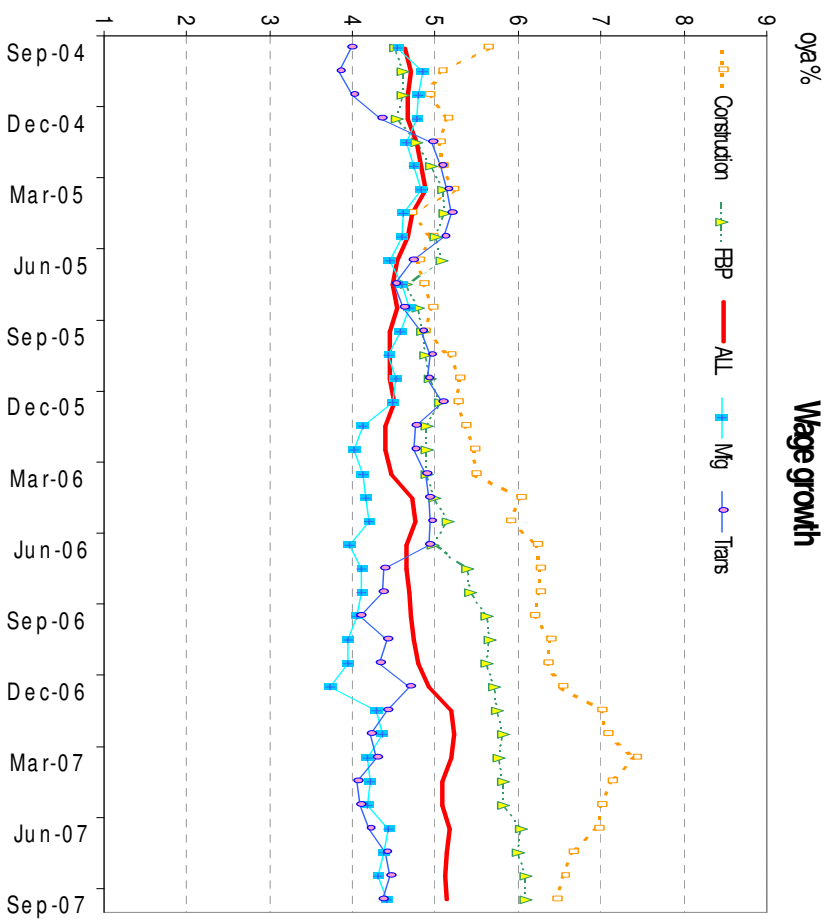
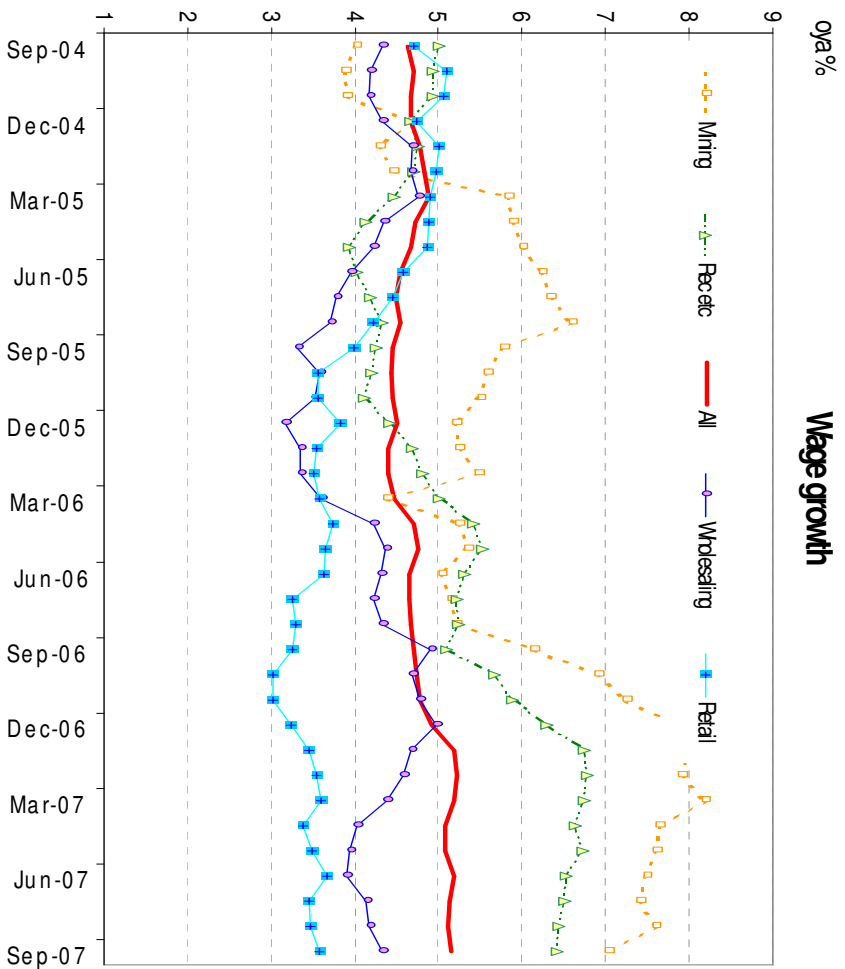
Excess demand pressures....on wages & input costs

Capacity & Labour Costs

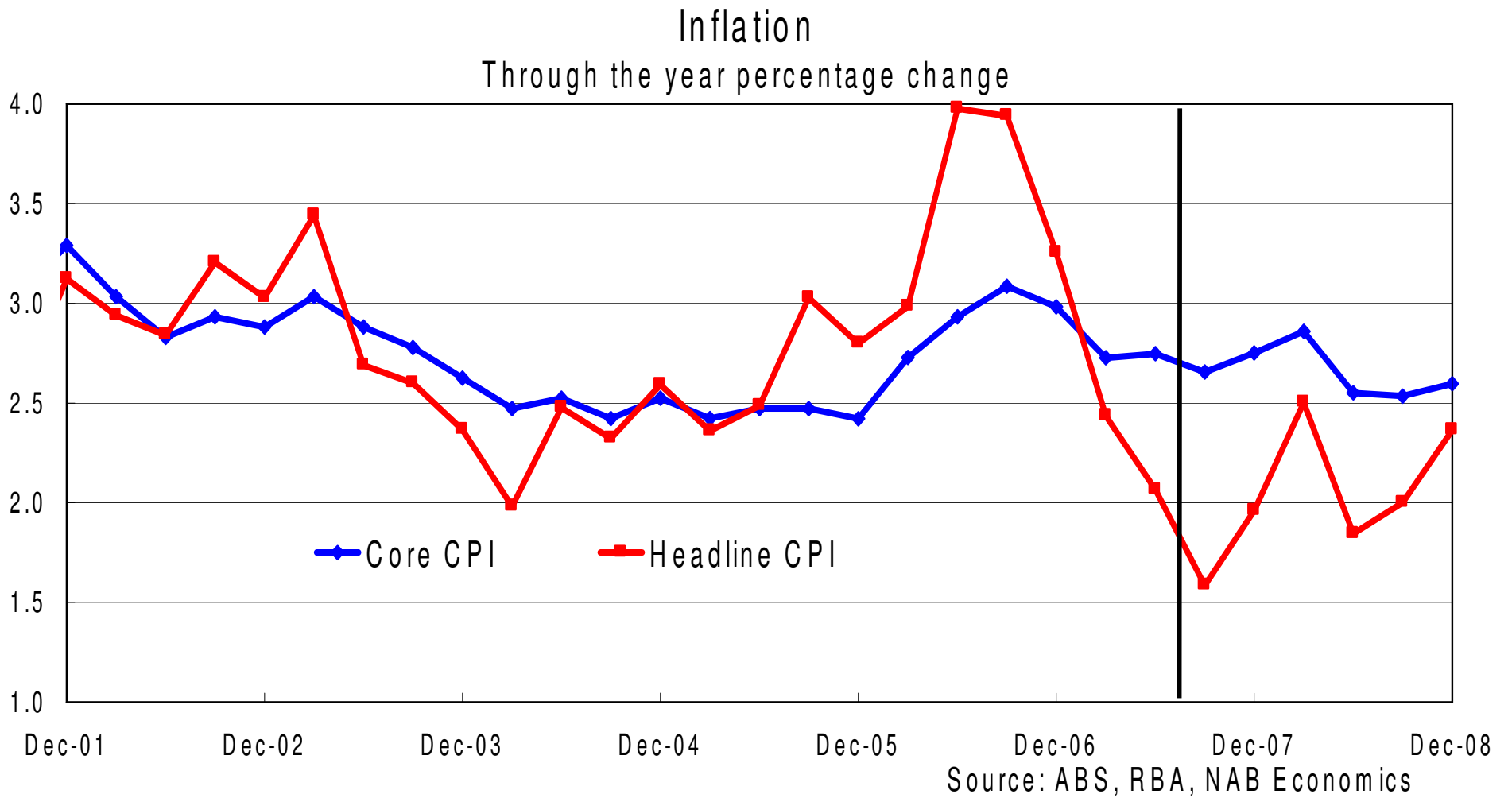


* Seasonally adjusted by NAB

Wages Growth by Industry



Inflation



Global Interest Rates...Central Banks on Watch

- **US** - Fed cut by 50 points in Sept. Expect another 75 points from here - bringing Fed funds to 4%. Likely by early 2008 (i.e. in next 3 meetings)
- **ECB** - still in rate rising mood (up to 4% in early June). Likely to wait till late 2007 for another 25 point hike & final one in early 2008 (peak at 4 ½ %).
- **BOJ** - no hurry (especially given weaker data recently). On hold in 2007. In 2008 up around ½ to around 1% by late 2008
- **BOE** - now done 75 points (latest in early July) - as extra insurance. Now on hold till mid 2008 when rates could be eased back.
- **RBNZ** - hiked in March, April, June and now July (cash rate at 8 ¼ %). After long period on hold likely to cut – 100 points over 2008/09.
- **China** - rates up 5 times this year (latest in Sept), by around 27 points each time. 1-yr lending rate = 7.29 (quite high - especially in real terms). But, not finished.

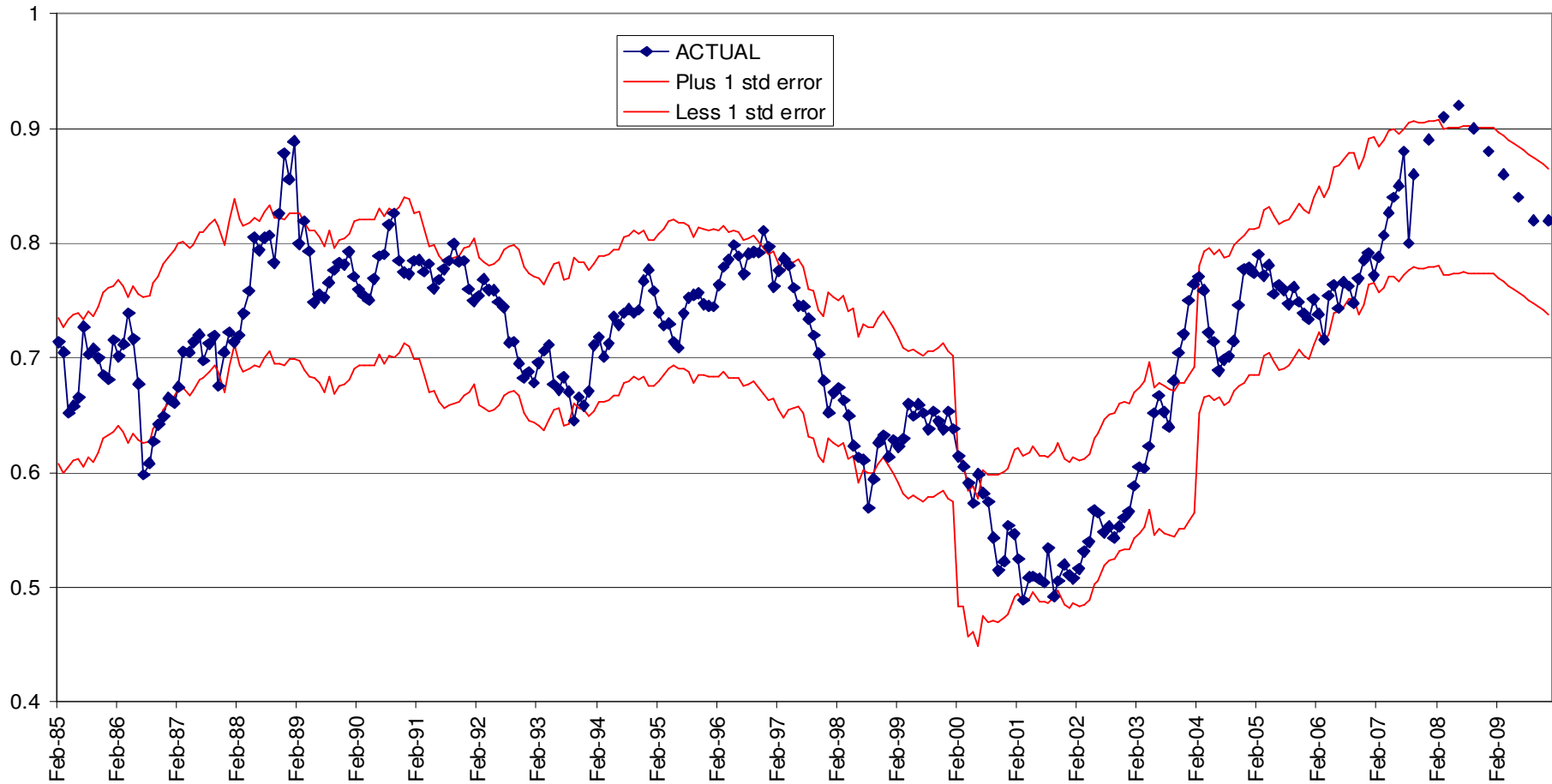
Australian Interest Rates

- So far US concerns not affecting global & Aust economic outlook
 - (with the exception of liquidity markets, but we assume this will be temporary).
- Hence, focus on local fundamentals
 - growth clearly strong and still accelerating.
- Stronger outlook has made us more concerned about RBA's unease
- Wage pressures still reasonable
- Near term inflation outlook - nearly 3% by early 2008
 - RBA more bearish - strong tightening bias
- We more optimistic on medium term inflation – 2.6% by mid/late 2008.
 - High currency, improving productivity and wages well behaved.
- Chance of another rate rise by late 2007 has increased to 45%
- Any extra stimulus – via irresponsible fiscal spending by Govt/ALP (and/or States) would tip RBA into another rise.

\$ Outlook...A Risky Business

Fundamentals Remain Supportive of \$A

Model AUD and Forecasts v Actuals

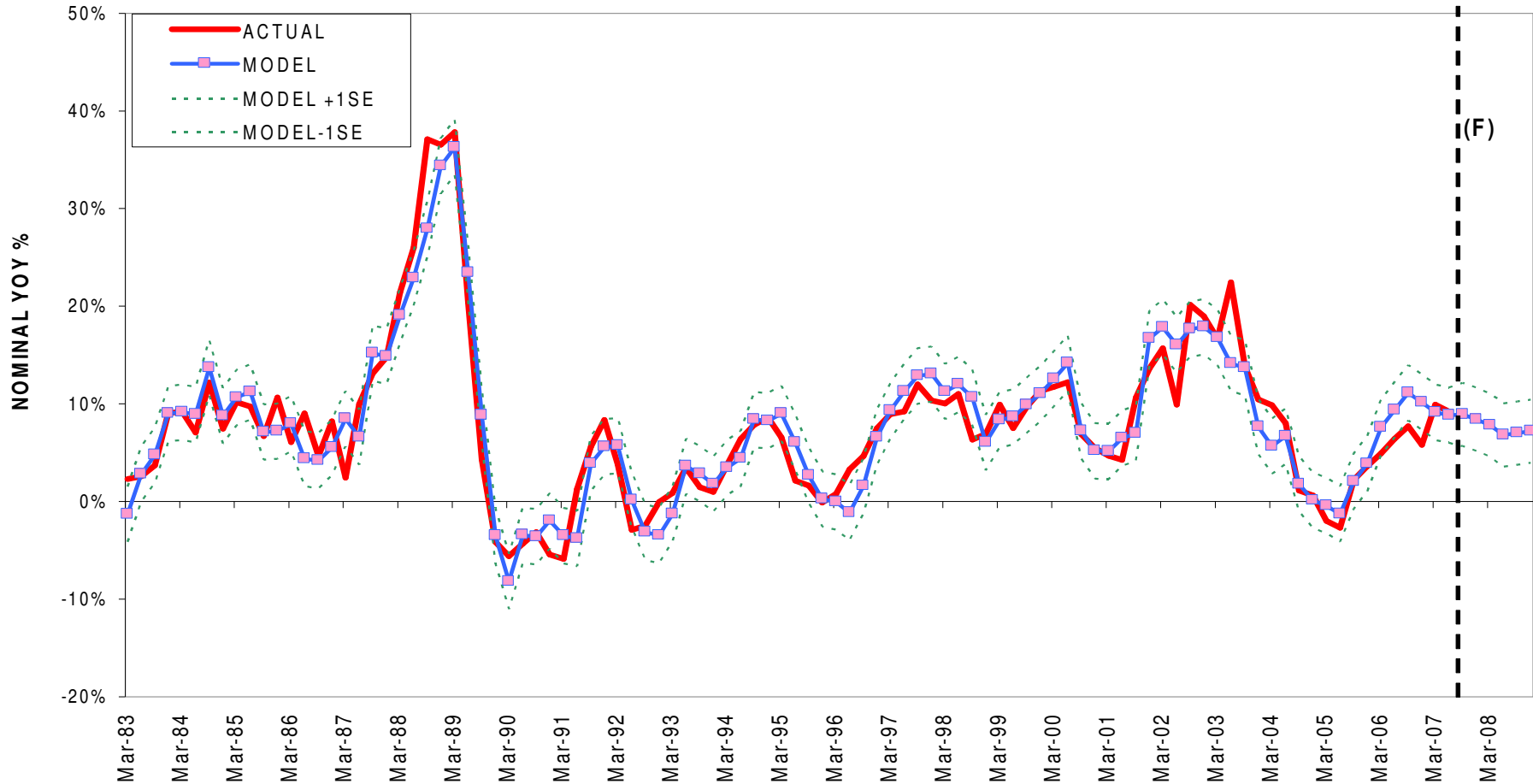


A Perspective on Property



National House Prices

NATIONAL HOUSE PRICES: MODEL AND FORECASTS (to Dec '08)

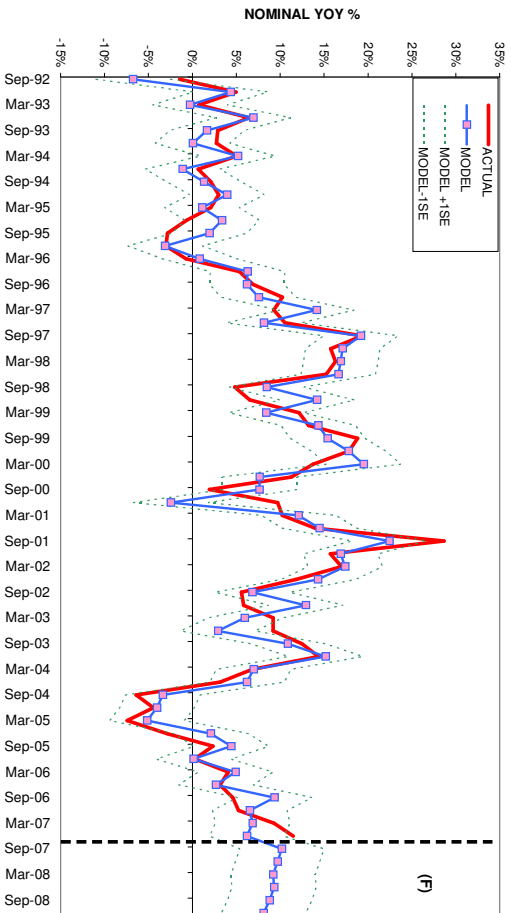


We expect growth rates going forward at around 9% easing back to around 7%

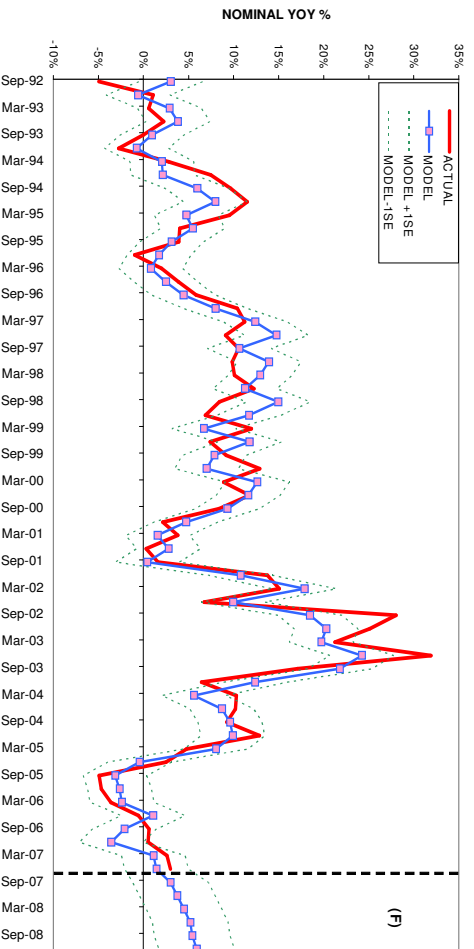


But very different across states...

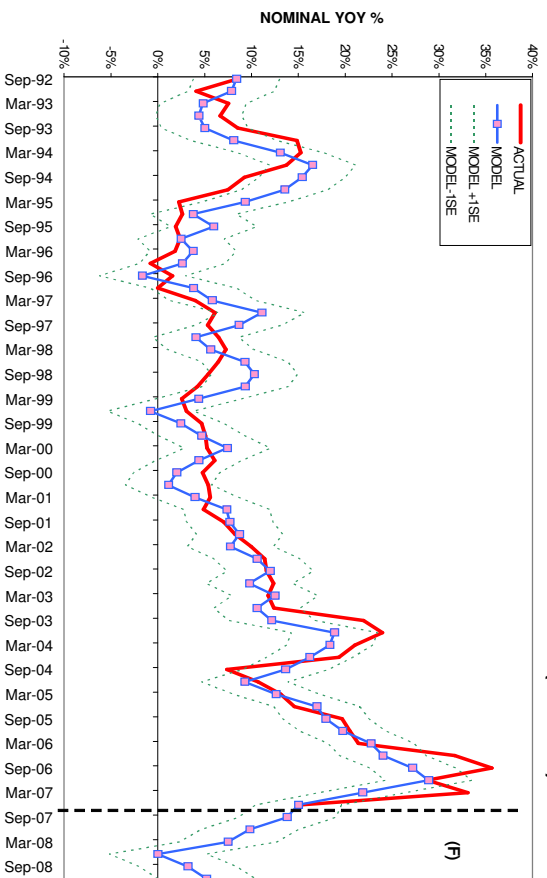
MELBOURNE HOUSE PRICES: MODEL AND FORECASTS (to Dec'08)



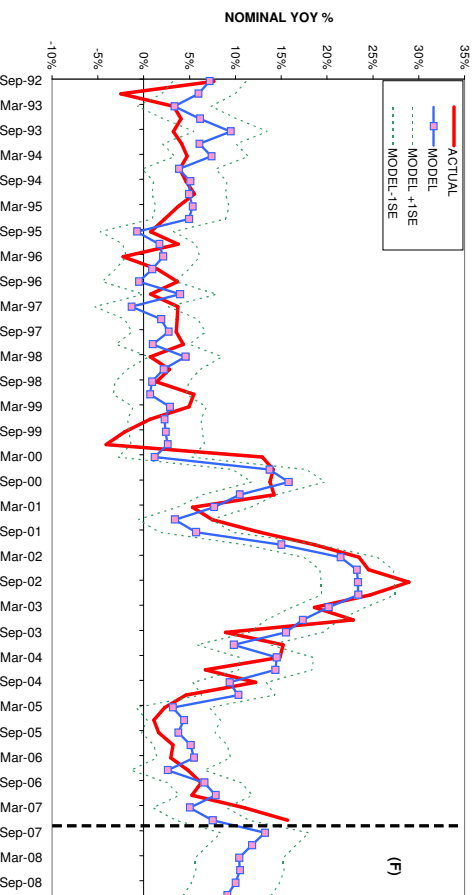
SYDNEY HOUSE PRICES: MODEL AND FORECASTS (to Dec'08)



PERTH HOUSE PRICES: MODEL AND FORECASTS (to Dec'08)

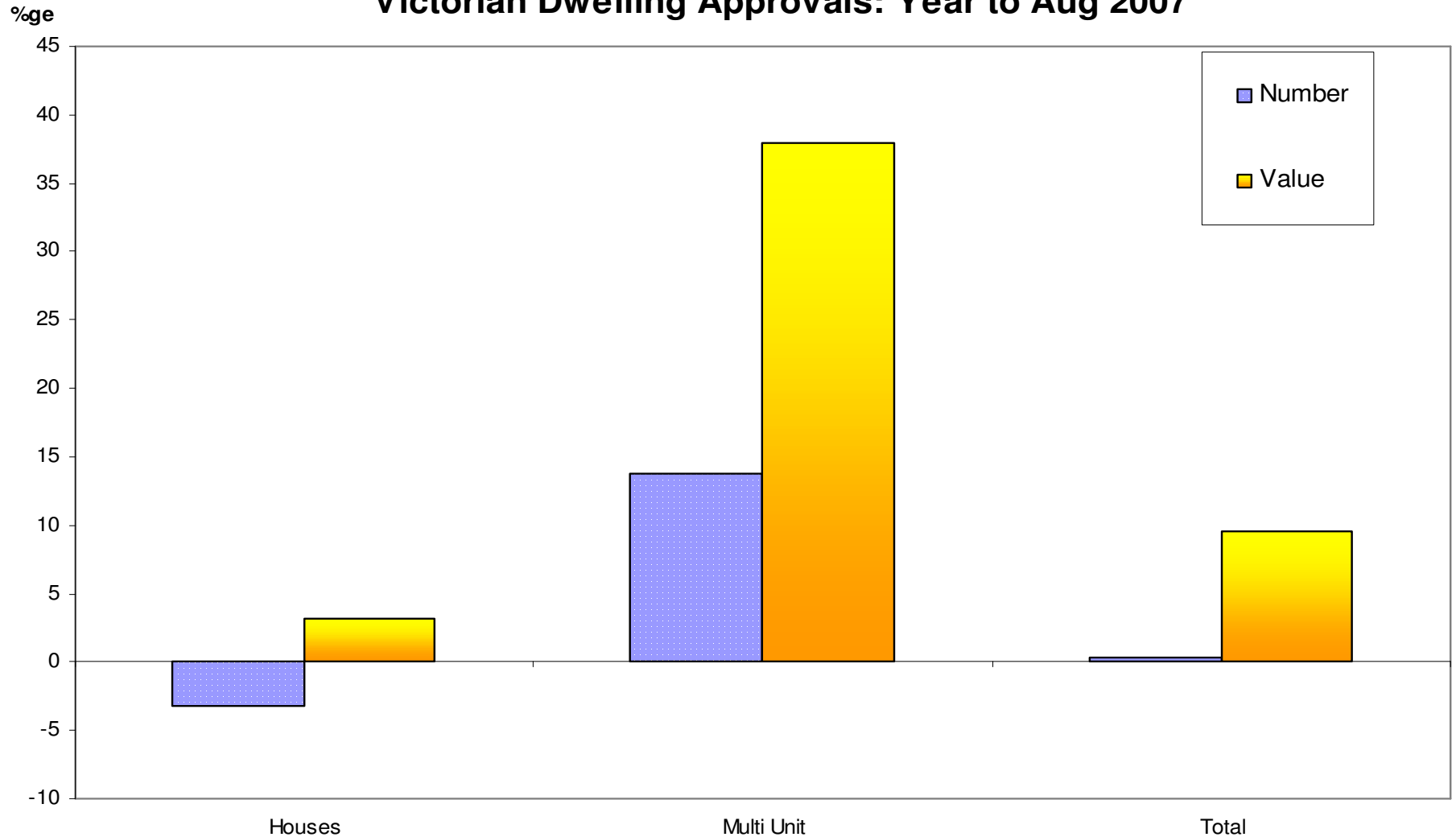


BRISBANE HOUSE PRICES: MODEL AND FORECASTS (to Dec'08)



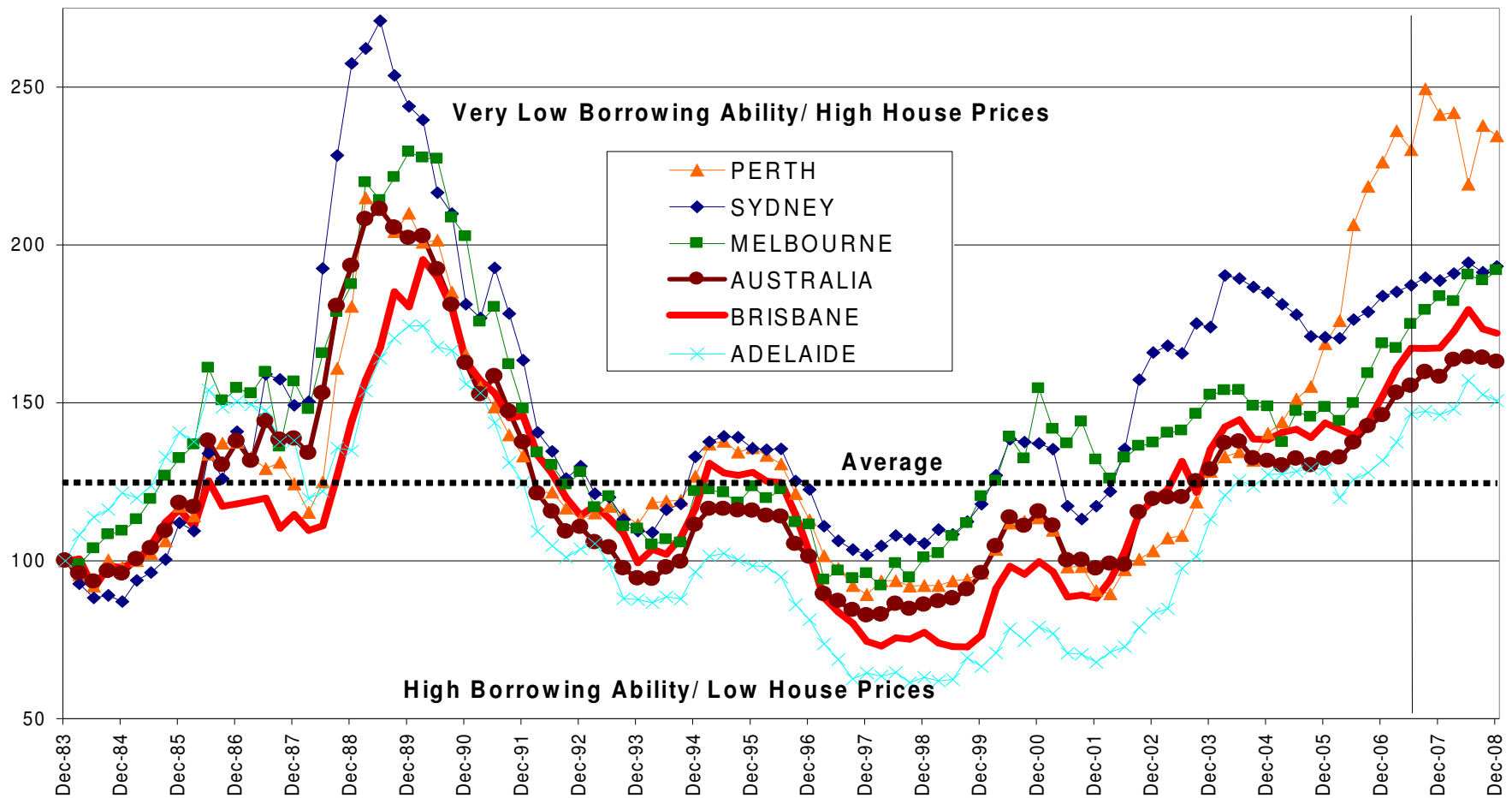
Dwelling Approvals - Victoria

Victorian Dwelling Approvals: Year to Aug 2007

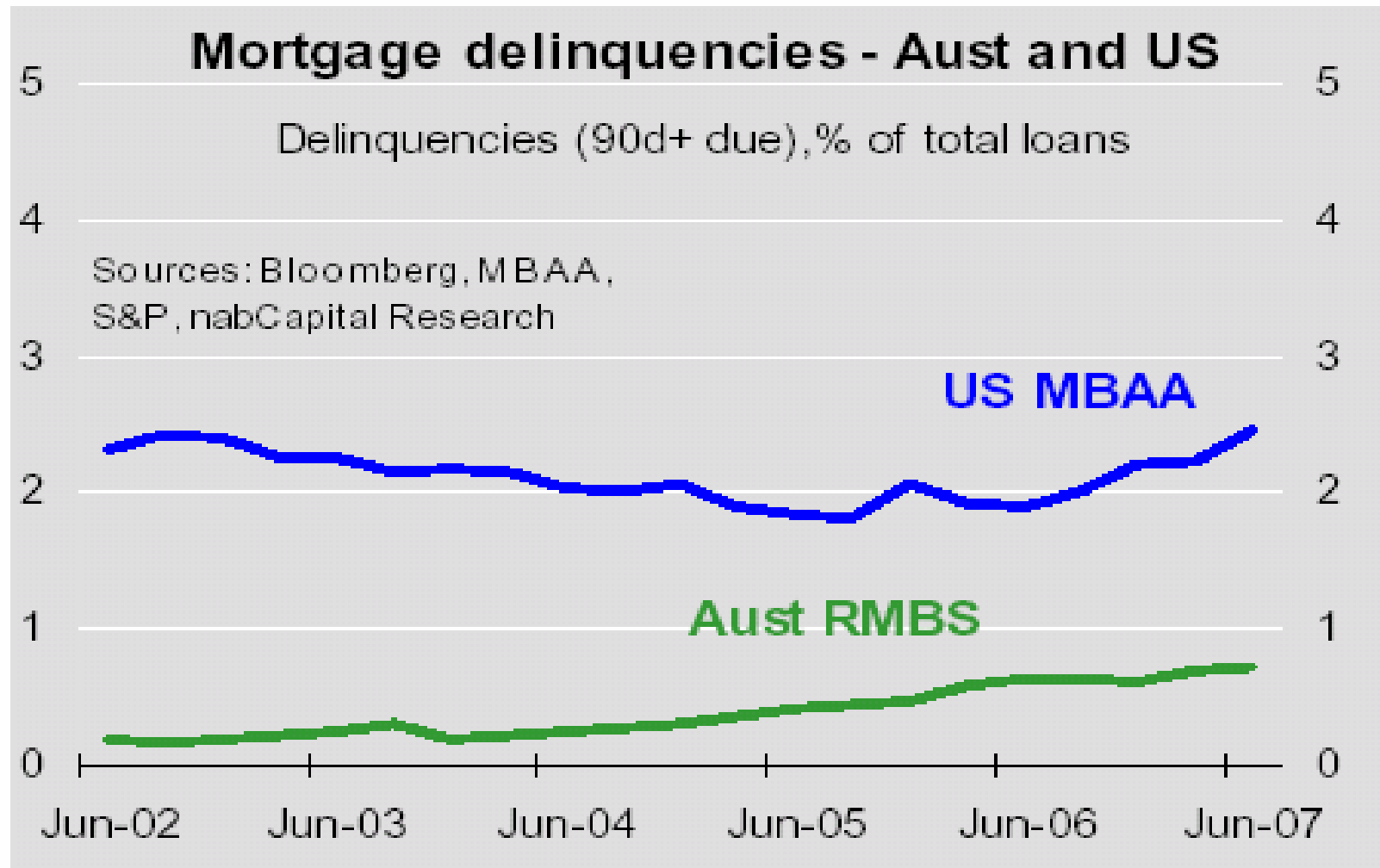


House Prices v Borrowing Ability

HOUSE PRICES TO HYPOTHETICAL BORROWING ABILITY



Mortgage Delinquencies - Australia v United States



Important Notices

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