

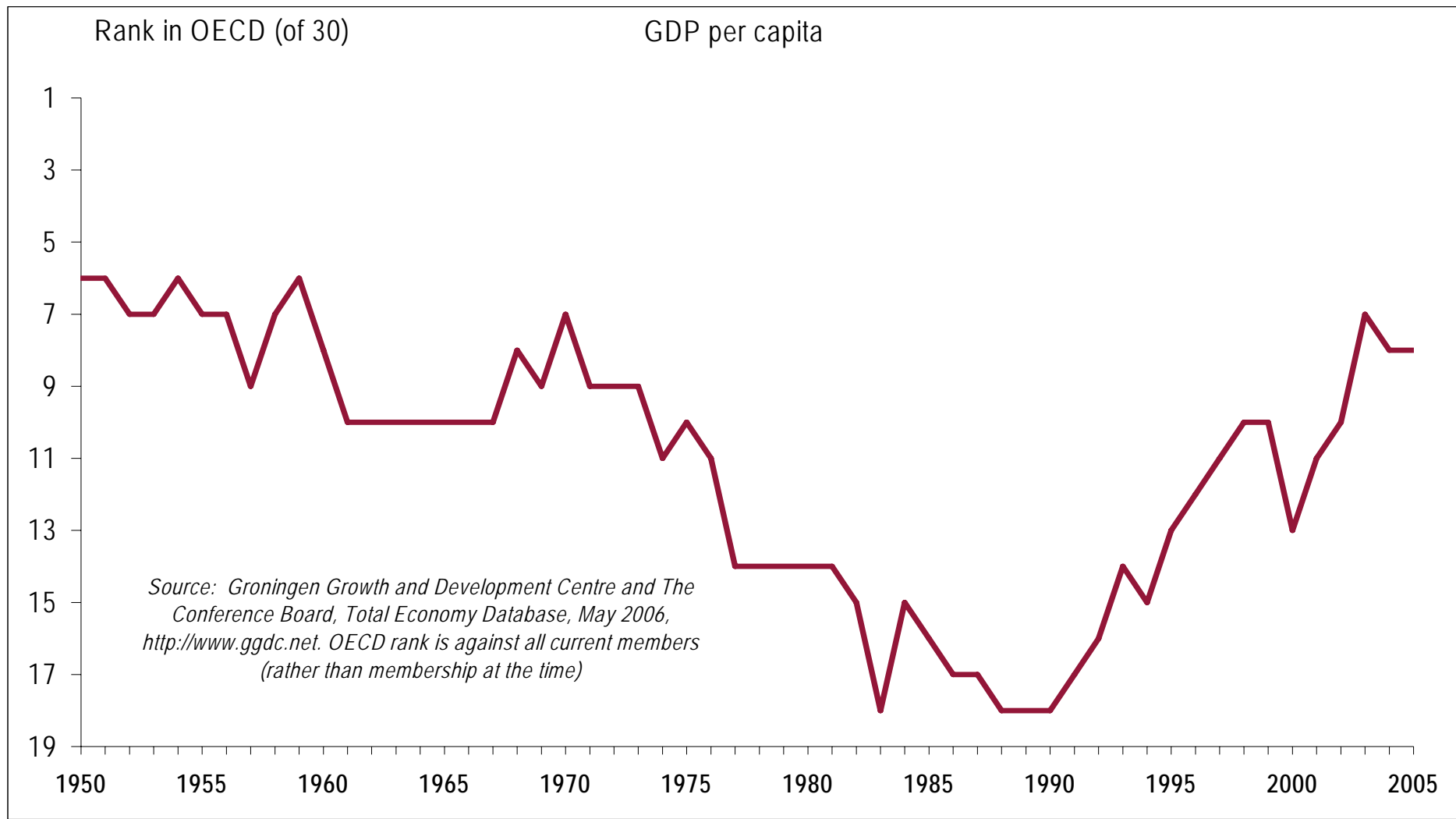
Making the boom pay

November 2006

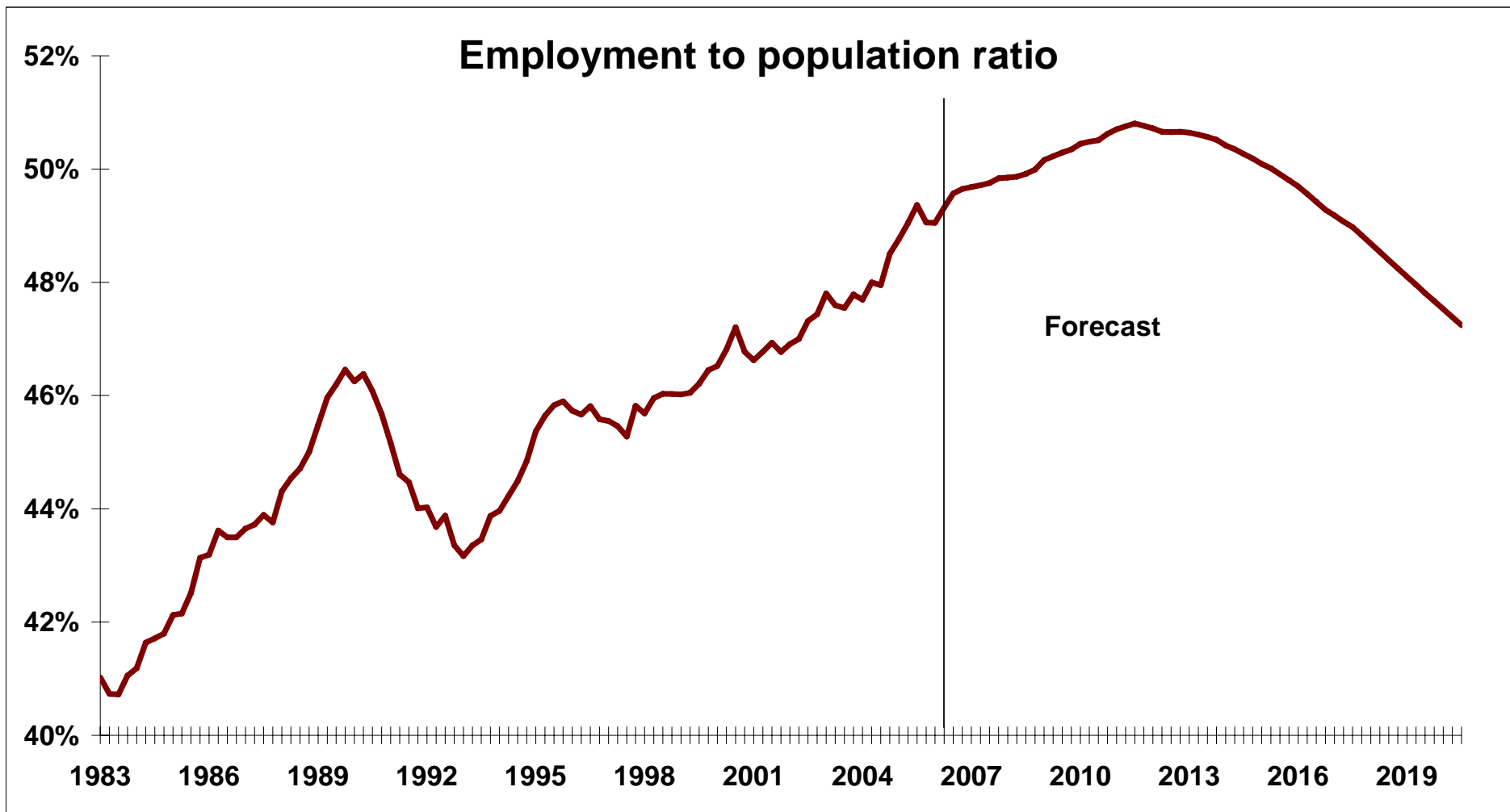
Chris Richardson
ACCESS ECONOMICS



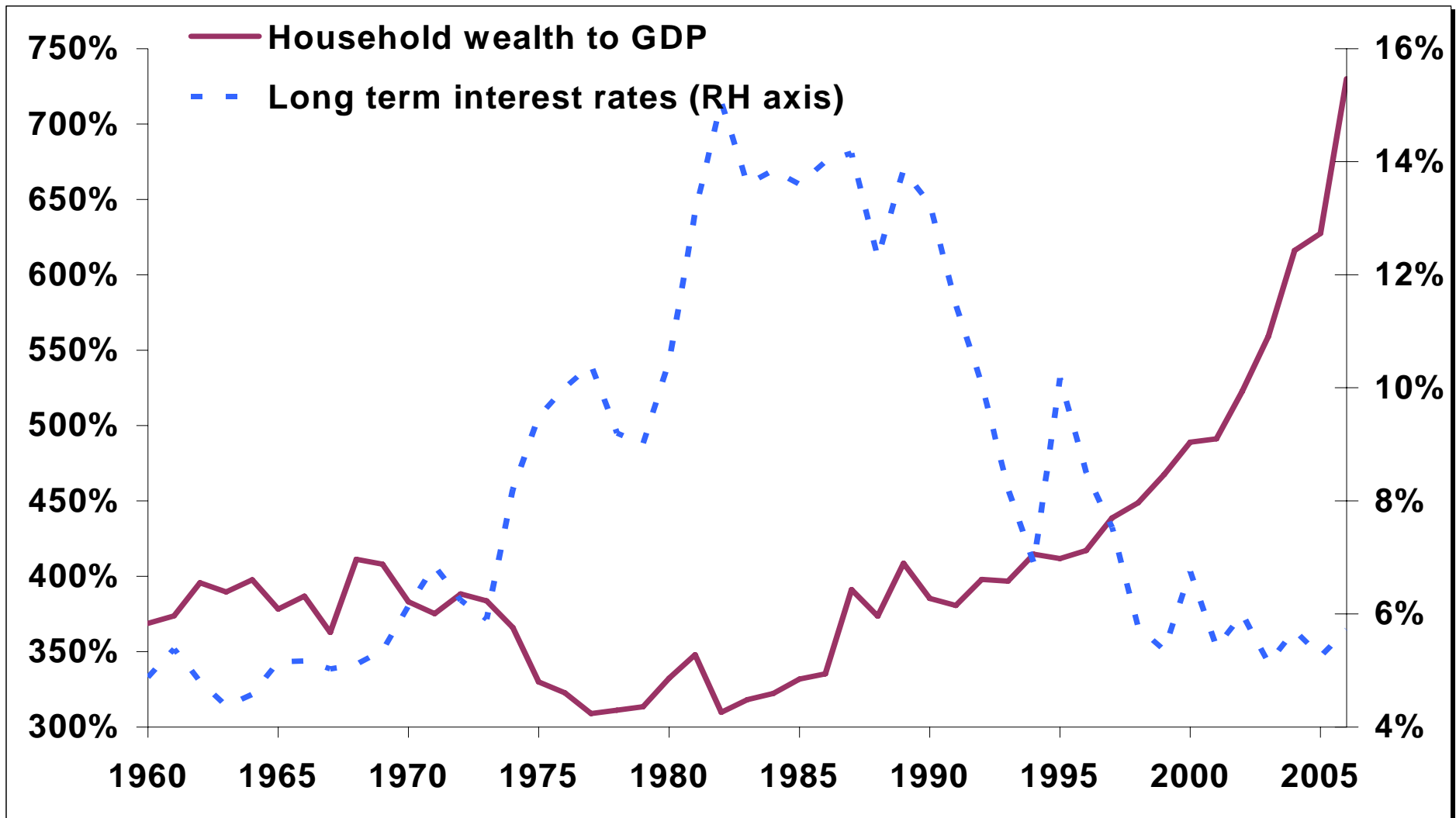
Has Australia turned history's tide?



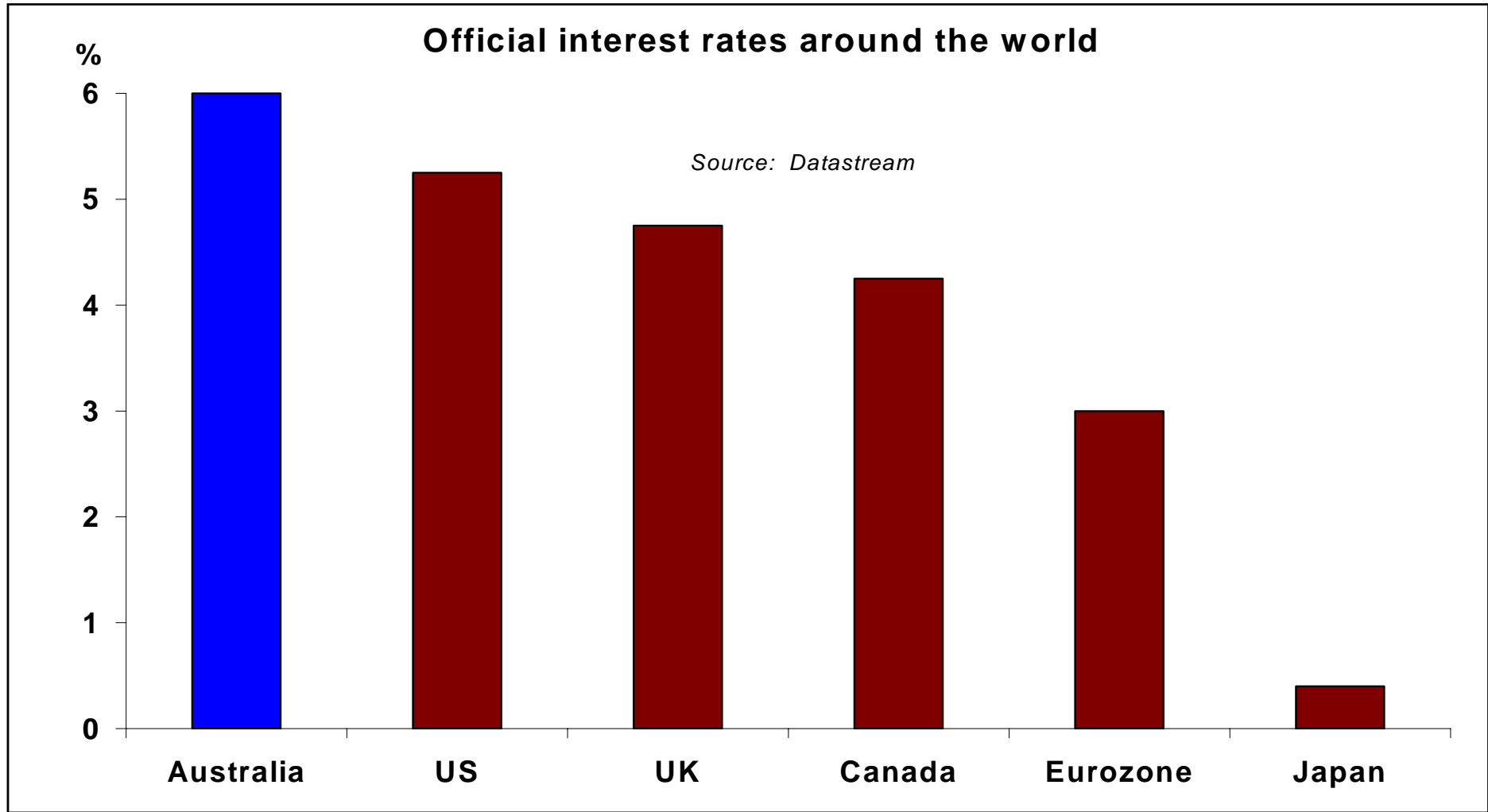
Yet gains will be temporary if we stay in slow lane on reform



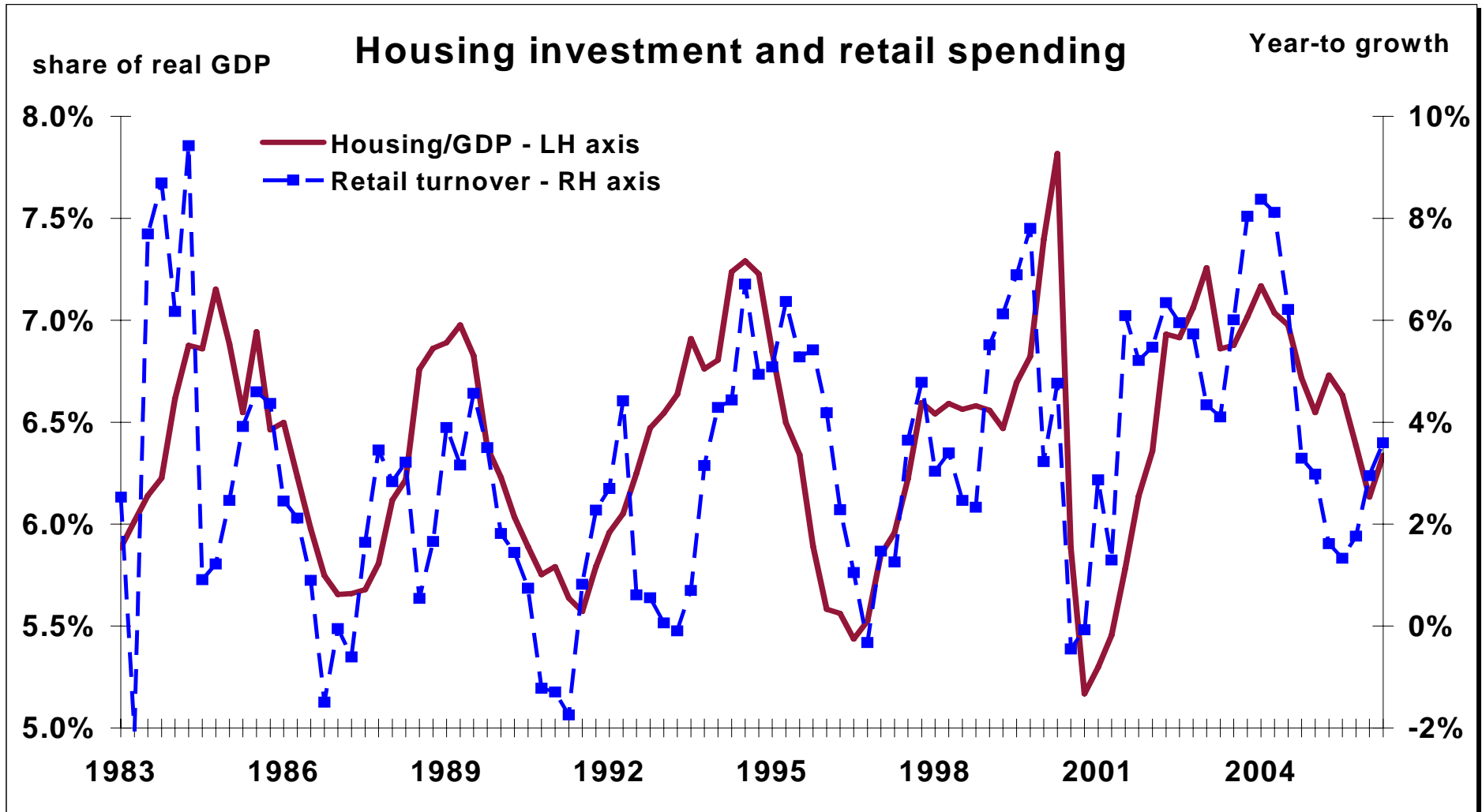
Indeed, overall wealth is at full stretch



Making higher rates a particular risk



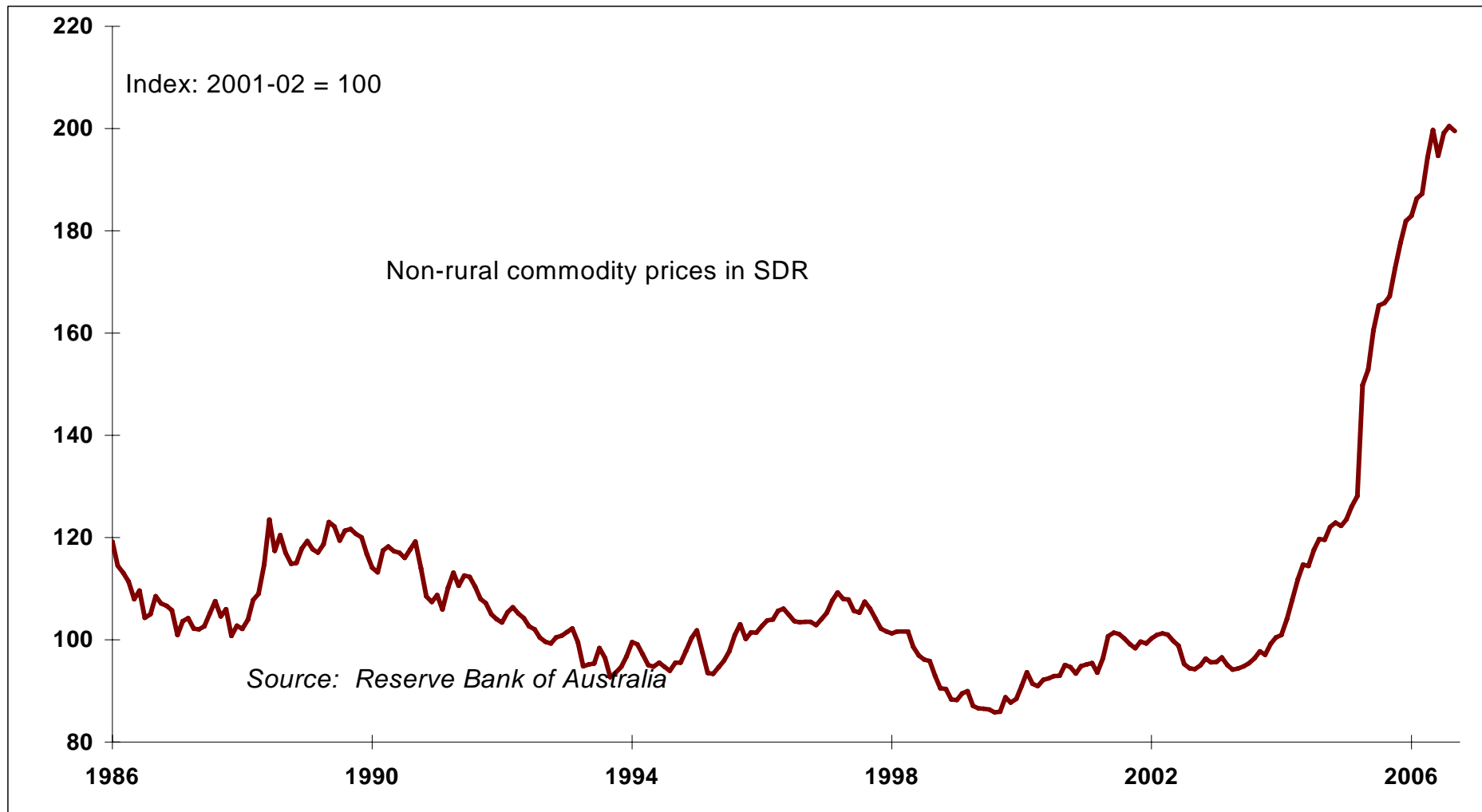
The domestic heart (retail/housing) slowed when housing prices did



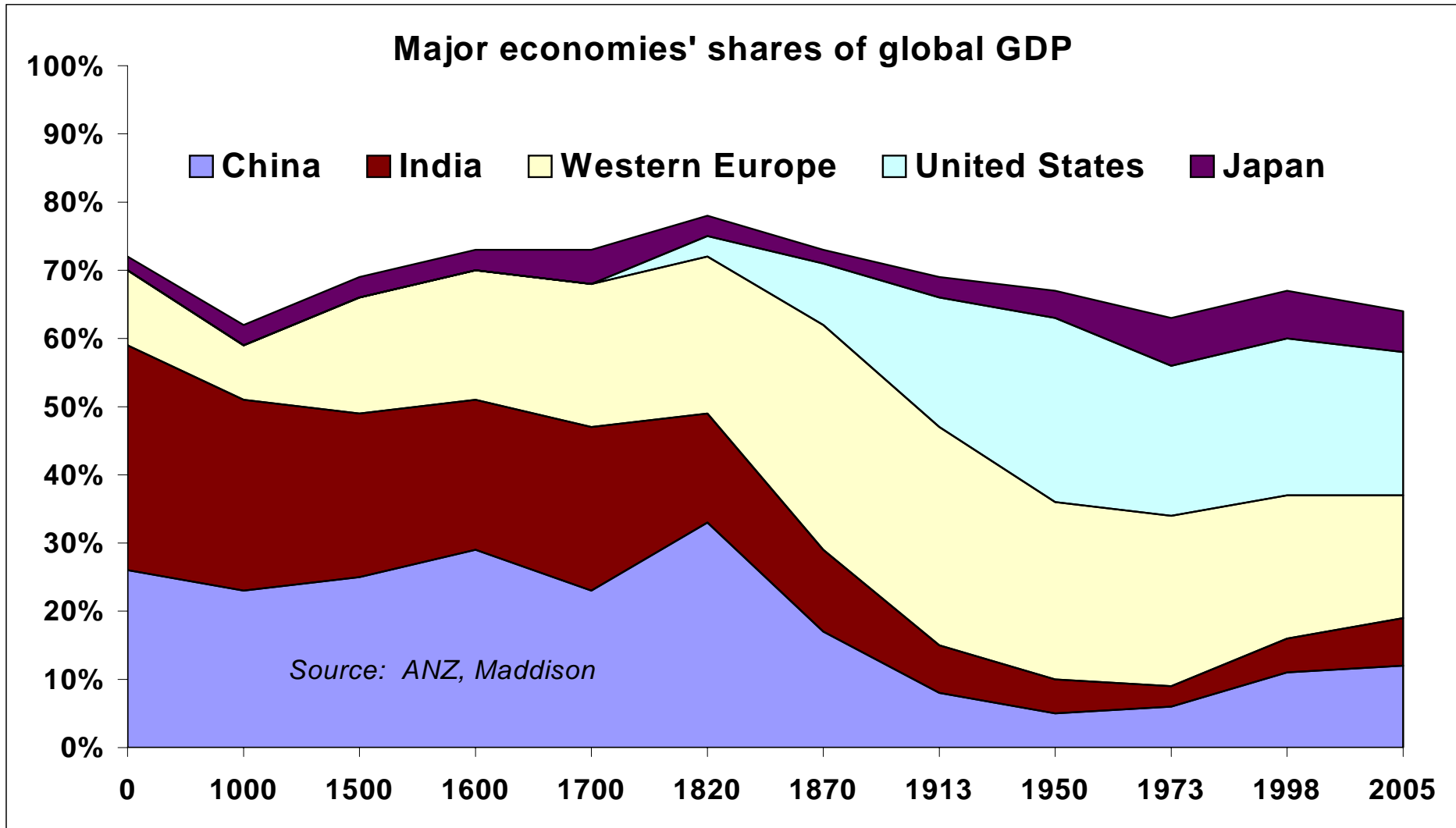
Yet not disastrously so ...

- Most housing price booms end in recessions.
- So why didn't Australia's housing prices see a bust in 2004 and 2005 – and our economy a recession?
- After all, NSW saw a pretty bad bust.
- But it didn't happen, as we went straight from a housing boom to a commodity price boom.

Because the lift in commodity prices has been remarkable



Thanks to a reversion to the norm



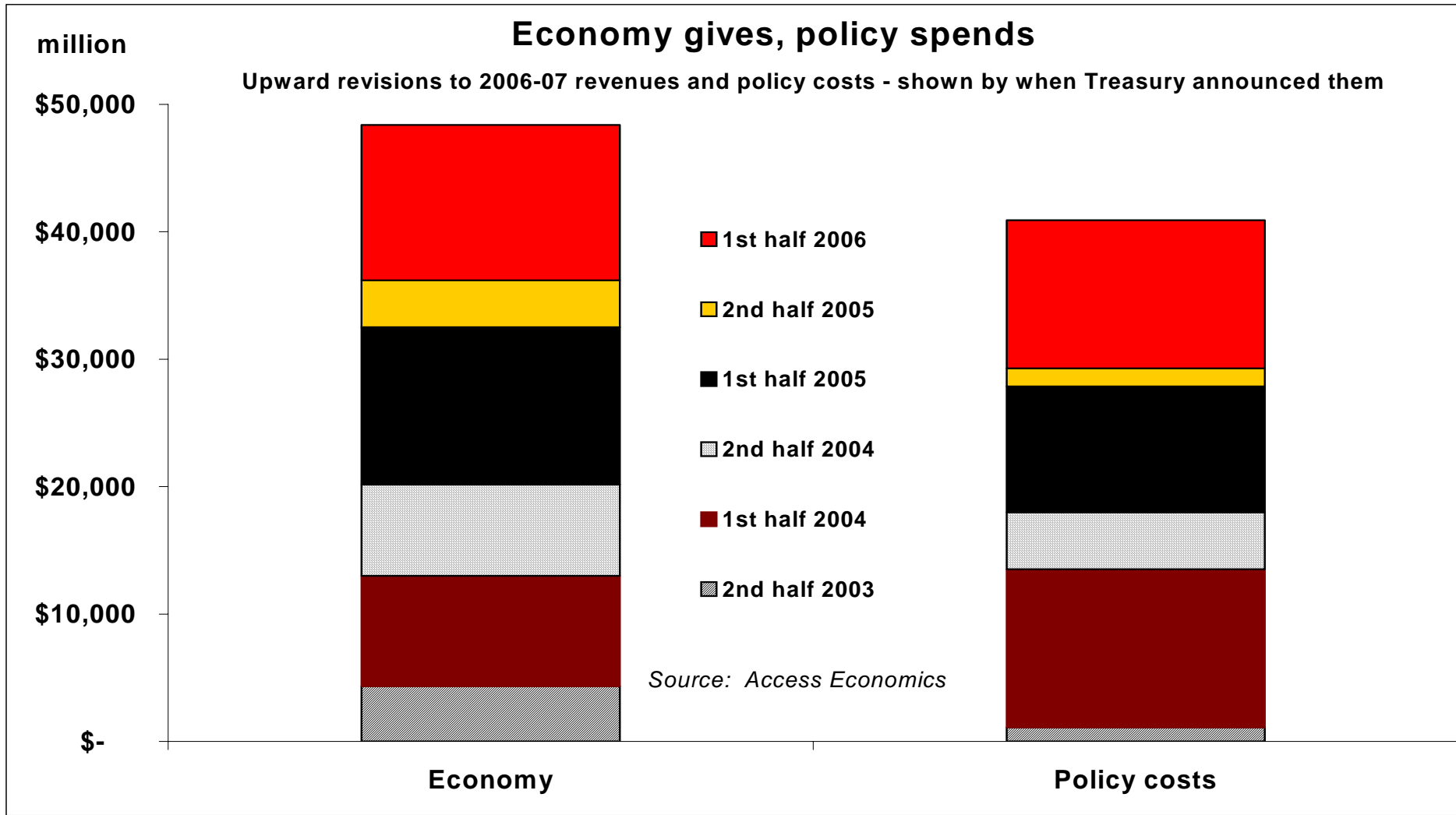
So we got lucky: the world gave us a pay rise, with perfect timing

Real growth has slowed since housing prices peaked, but the commodity boom means the world is pumping extra income into Australia each year.

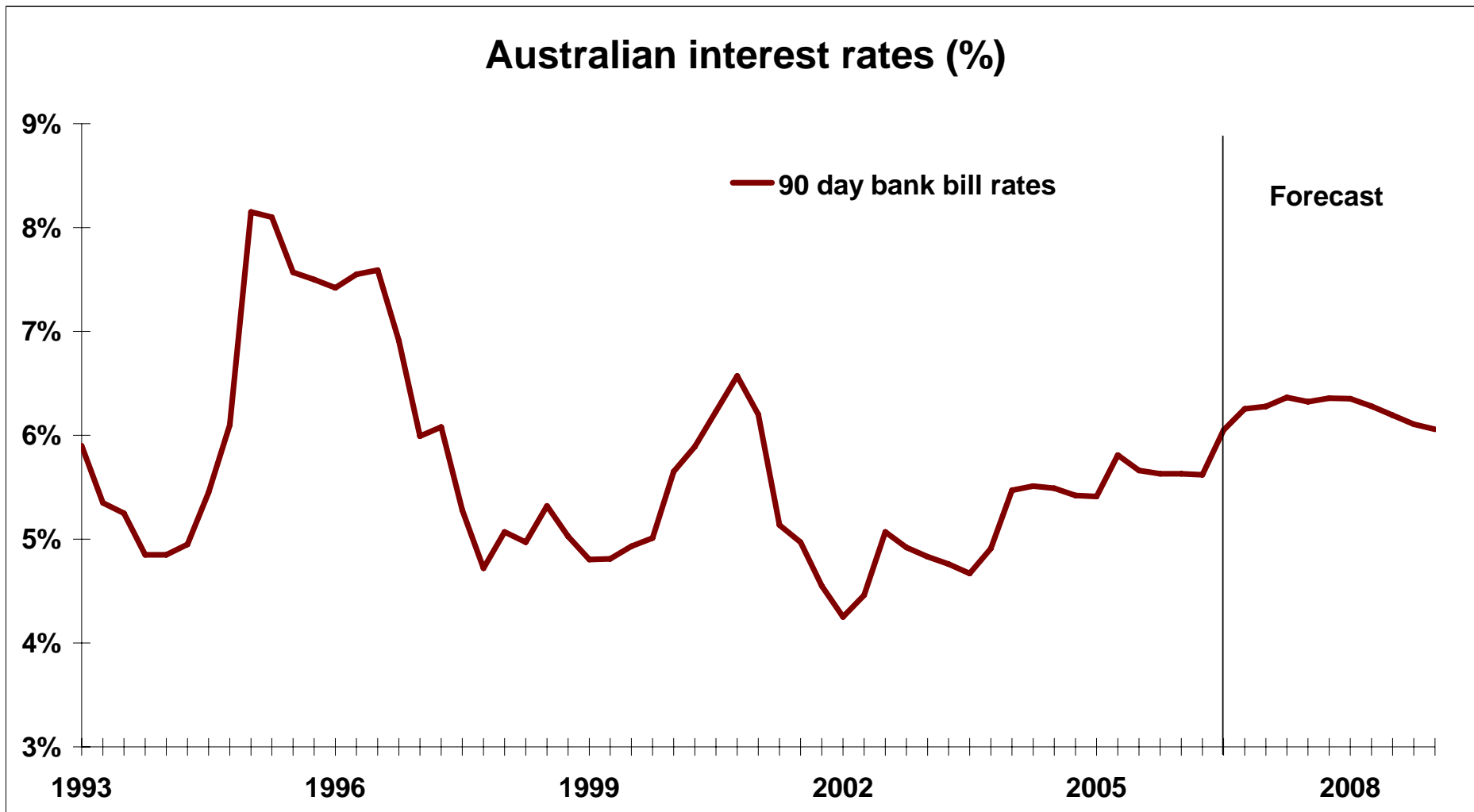
So it is no coincidence that:

- (1) the \$A is above its longer term fair value,
- (2) company profits are a record share of the pie,
- (3) resource stocks are near record highs,
- (4) business investment is leaping, and that
- (5) Federal revenues are so strong.

Which, in turn, has underwritten yet more tax cuts & family benefits



That makes the tug of war between tax cuts & rate rises vital for Aust



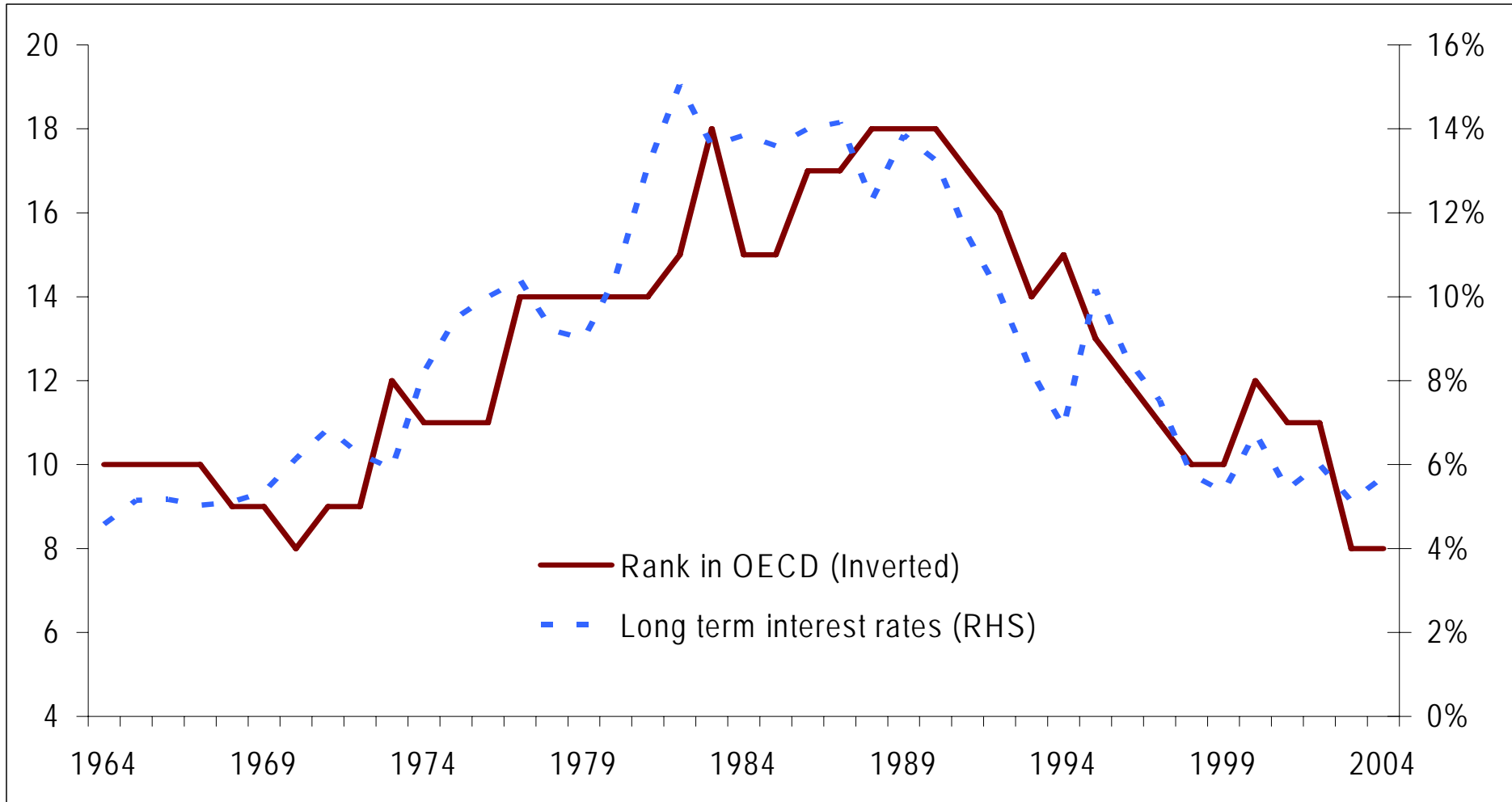
And it raises key policy questions

- What should policymakers do if:
 - (1) housing prices are still stretched, and yet
 - (2) Australia still runs a big current account deficit amid these great commodity prices?
- The answer is that interest rates should be on the low side (so as not to pull the rug out from under Sydney and Melbourne housing prices).
- While the Budget surplus should be as large as politics will allow (so as to take as much pressure as possible off the current account).

But that isn't what we're getting on the policy front

- Yet instead of interest rates being lower and Budget surpluses being higher, we're getting the exact opposite.
- 2005 saw a tax cut and a rate rise. For many retailers (especially those on the eastern seaboard), that was a 'nil-all draw'.
- And 2006 is shaping up the same way ...

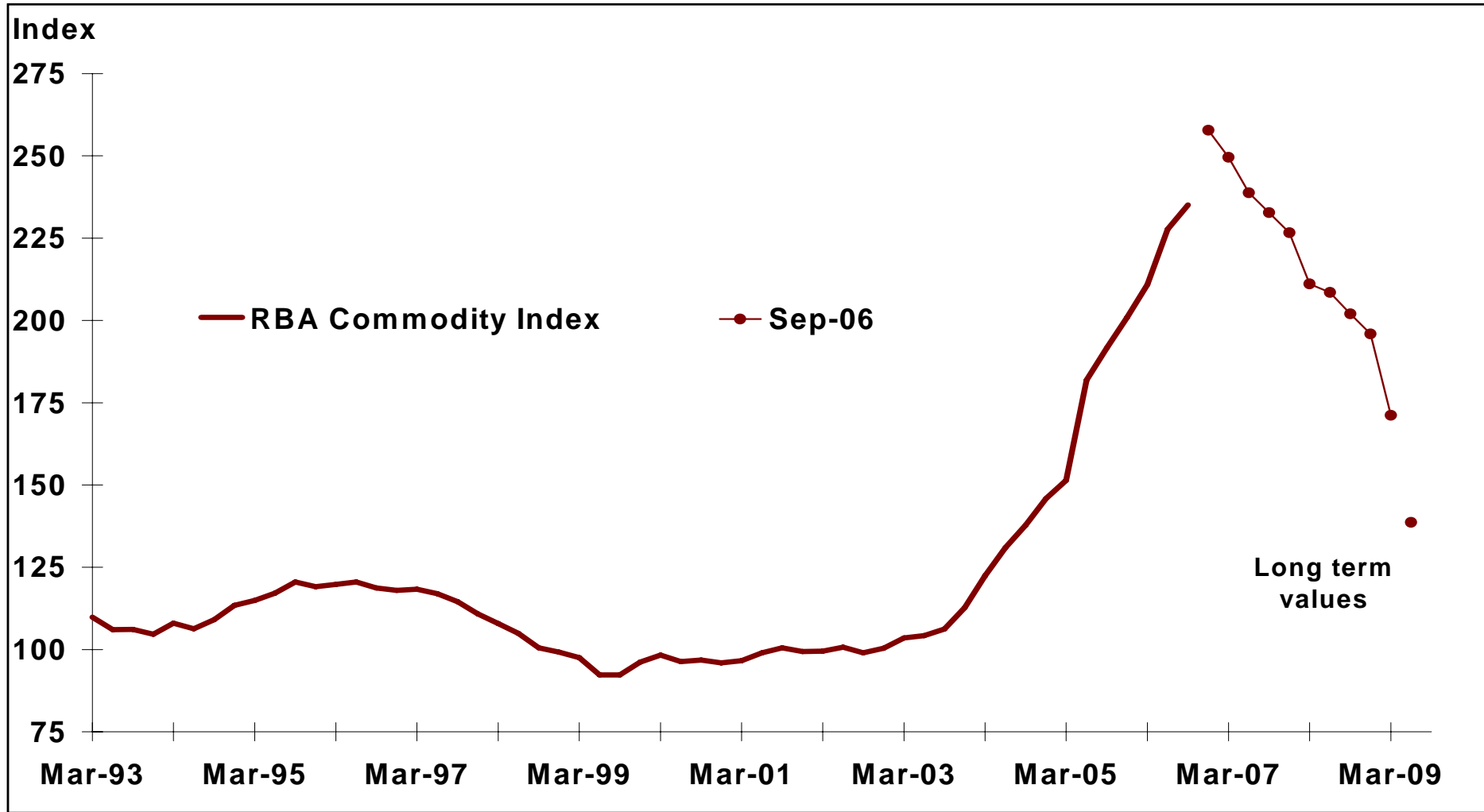
... we are playing with fire instead



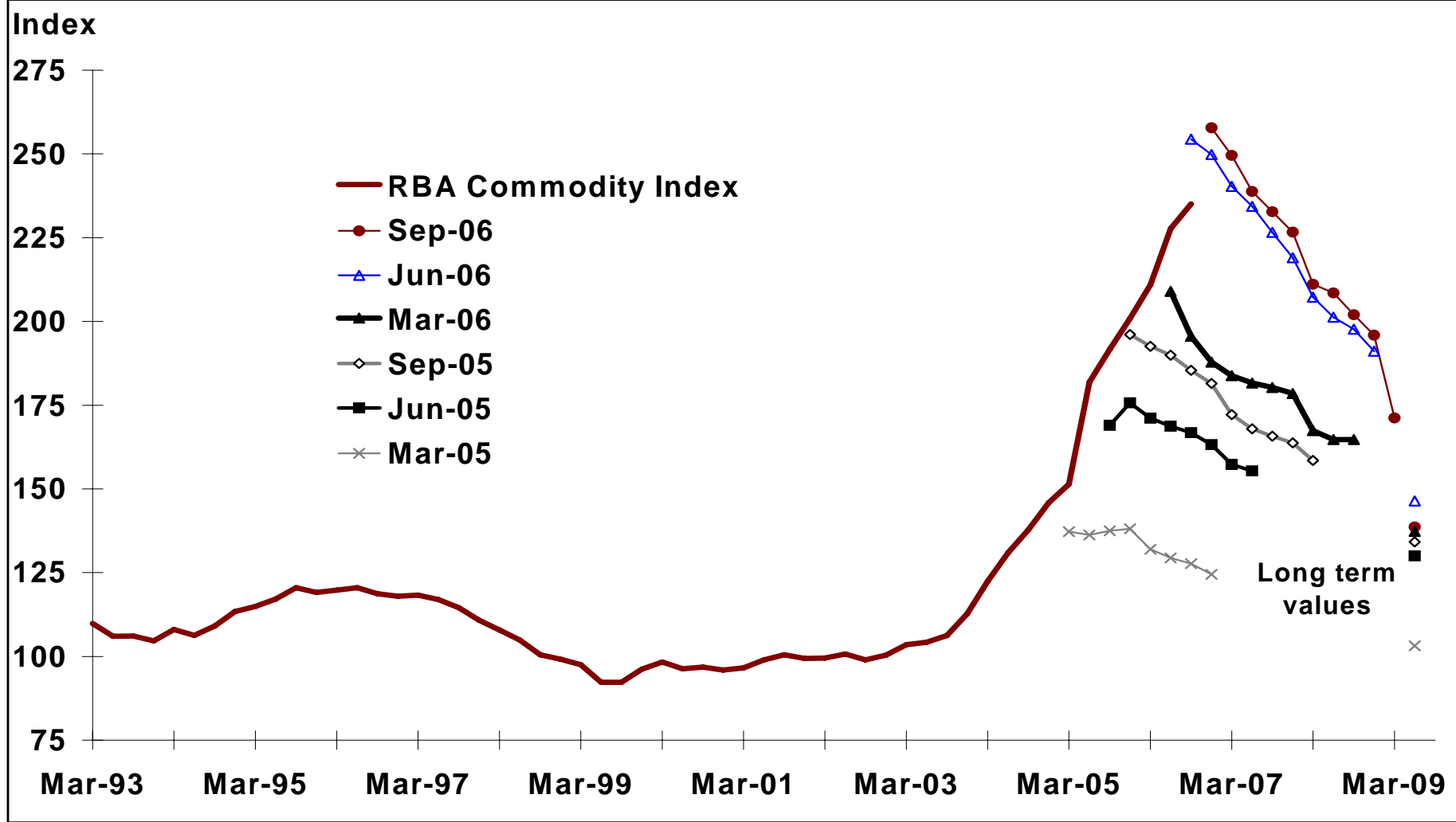
That is a waste – and a dangerous one, if we're on borrowed time (and money)

- Good times are rolling – but reforms are not.
- In times past we have squandered booms.
- Now it seems that, once more, we are wasting a golden opportunity.
- Both the States and the Feds need to trust the punters enough to let them know there is a case for further reform: it's time for us to invest in supply, not demand.
- As our luck may run out sooner than you think.

As forecasters are gloomy – seeing prices falling sharply by 2008-09



That raises risks for Australia. Yet we've been wrong so far ...



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