



Economic & Financial Markets Outlook

AAAC Outlook Day

John Kyriakopoulos

Senior Currency Strategist – Global Markets Research

John.Kyriakopoulos@nab.com.au

+612 9237 1903

25 November 2011

Key messages: The Global Outlook

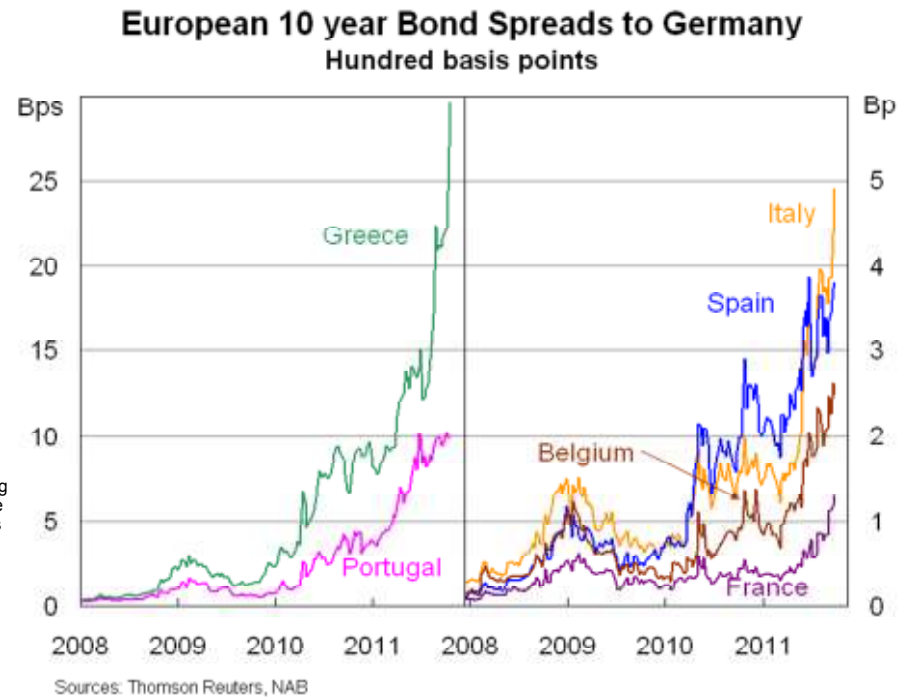
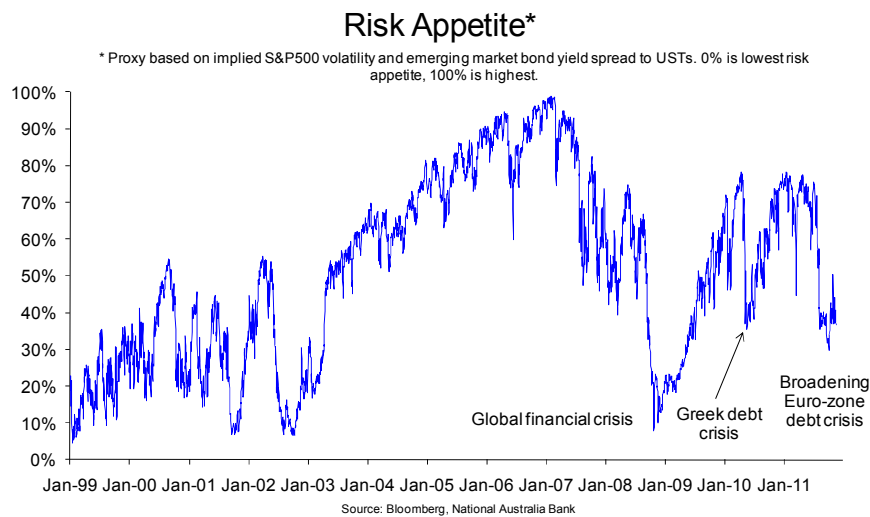
Developed world in very slow growth phase with lots of risks

- US didn't fall into recession again as feared but not growing fast enough & big headwinds - "politics poor" re policy. Unemployment unlikely to fall much.
- European core now moving into mid double dip with periphery very high risk
- Globally consumer and business "afraid" and "cautious"

Emerging economies fuelling growth

- Ongoing China strength - with Chinese more concerned about inflation. Similar story for India
- Non Japan Asia strong on back of China, but slowing
- While European debt issues could cause massive disruption if things go badly - Chinese still have lots of policy flexibility

Markets now clearly focused on risk of global recession from European debt crisis



Europe's debt crisis spreading beyond periphery

- > Initial phase of the crisis was on risk of disorderly default by Greece, Portugal, Ireland
- > We now have European Governments trying to leverage up European Financial Stability Fund to EUR1 trillion but facing problems
- > Major issues
 - This is enough for PIG debt but not Spain and especially Italy
 - Italy is the big unspoken fear (around EUR1.9 trillion) in bonds
 - And in particular the solvency of European banks when they have to take a haircut on defaulting bonds
 - Main risk of GFC-style contagion is the possibility of European / global banking crisis via *European banks capital positions*
- > The end game involves greater fiscal integration and common EU bond issued (years away perhaps?) or ECB printing money and buying debt (“lender of last resort”)

Global Economic Forecasts

	2010	2011(f)	2012(f)	2013(f)
United States	3.0	1.8	2.4	3.1
Japan	4.0	-0.6	3.3	1.9
Euro-zone	1.7	1.7	0.4	1.1
Asia ex. Japan & China	7.8	4.8	4.2	3.9
China	10.4	9.2	8.2	8.0
India	9.0	7.5	6.9	6.0
World	5.1	3.8	3.7	3.6
Australia's MTPs	6.2	4.3	4.6	4.3

Key messages: The Australian Outlook

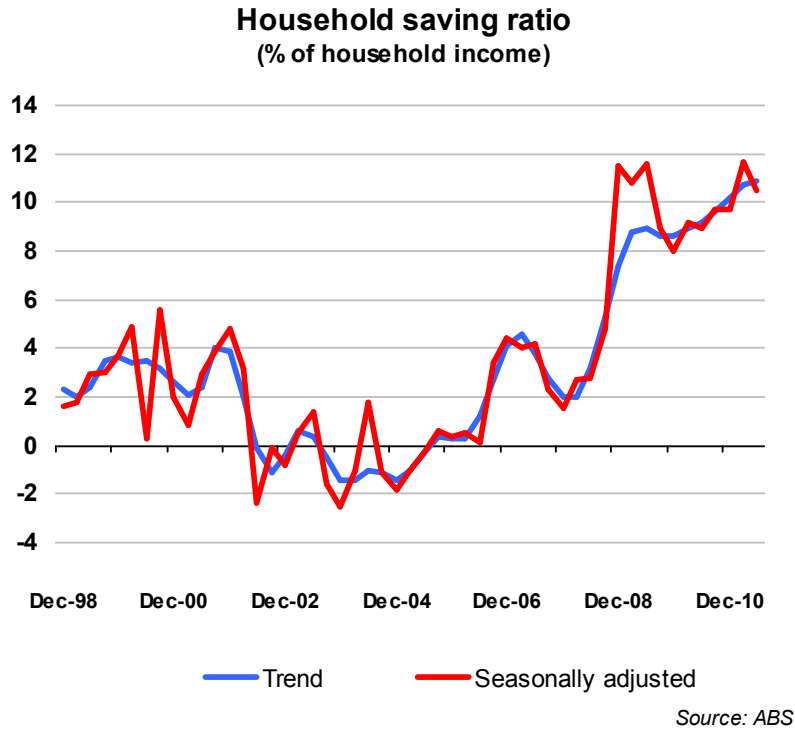
- > Australia is slowing below trend with multi speed economy becoming more pronounced as restructuring occurs
- > Longer run outlook: Accelerating growth but significant rebalancing challenges
- > Our economic forecasts don't point to significant cuts in official interest rates which would require a global recession/financial crisis
- > We expect AUD/USD to trade around parity assuming no global recession or RBA slashing of interest rates

Economic growth to improve but constrained by strong AUD and higher household savings

- **Natural disasters** had bigger impact than expected (especially coal) - transferring 2% of GDP
- **Consumers** are extremely cautious. Pressure on retail and some discretionary spending. High dollar (here to stay) which is hurting manufacturing, tourism and construction.
- The surprise has been that **the weak are getting weaker.**
RESTRUCTURING.
- But miners, professional services, health and personal services strong. **Not just mining.**
- **Terms of trade, Qld rebuild,** and mining investment plans unprecedented
- Overall, accelerating (but mixed) growth, sluggish credit demand
- Key risk is external, Euro-zone driven global recession

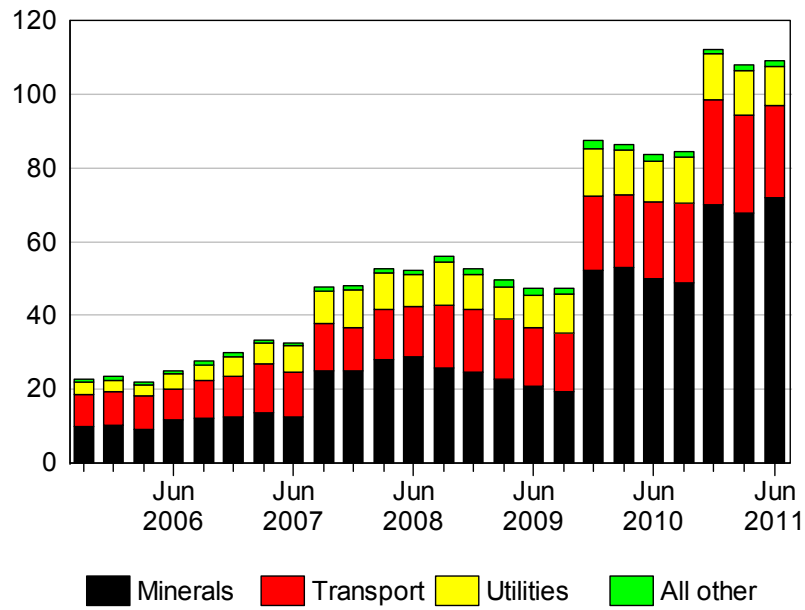
Consumer still cautious but spending still rising

- > Consumers are still wary and de-leveraging. Saving ratio has moved up significantly
 - And while internet growing it's not the main driver
- > NAB business survey suggests that retail overall is experiencing extremely weak conditions
- > But households are happy to spend on overseas travel, cafes & restaurants & other services



Pipeline of future mining investment is massive

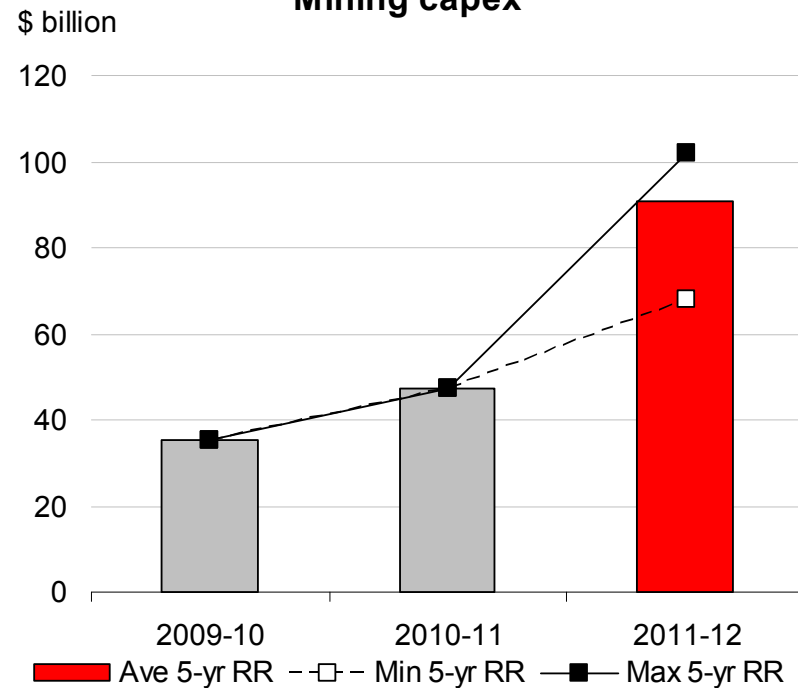
Engineering construction work yet to be done
\$ billion



Source: ABS

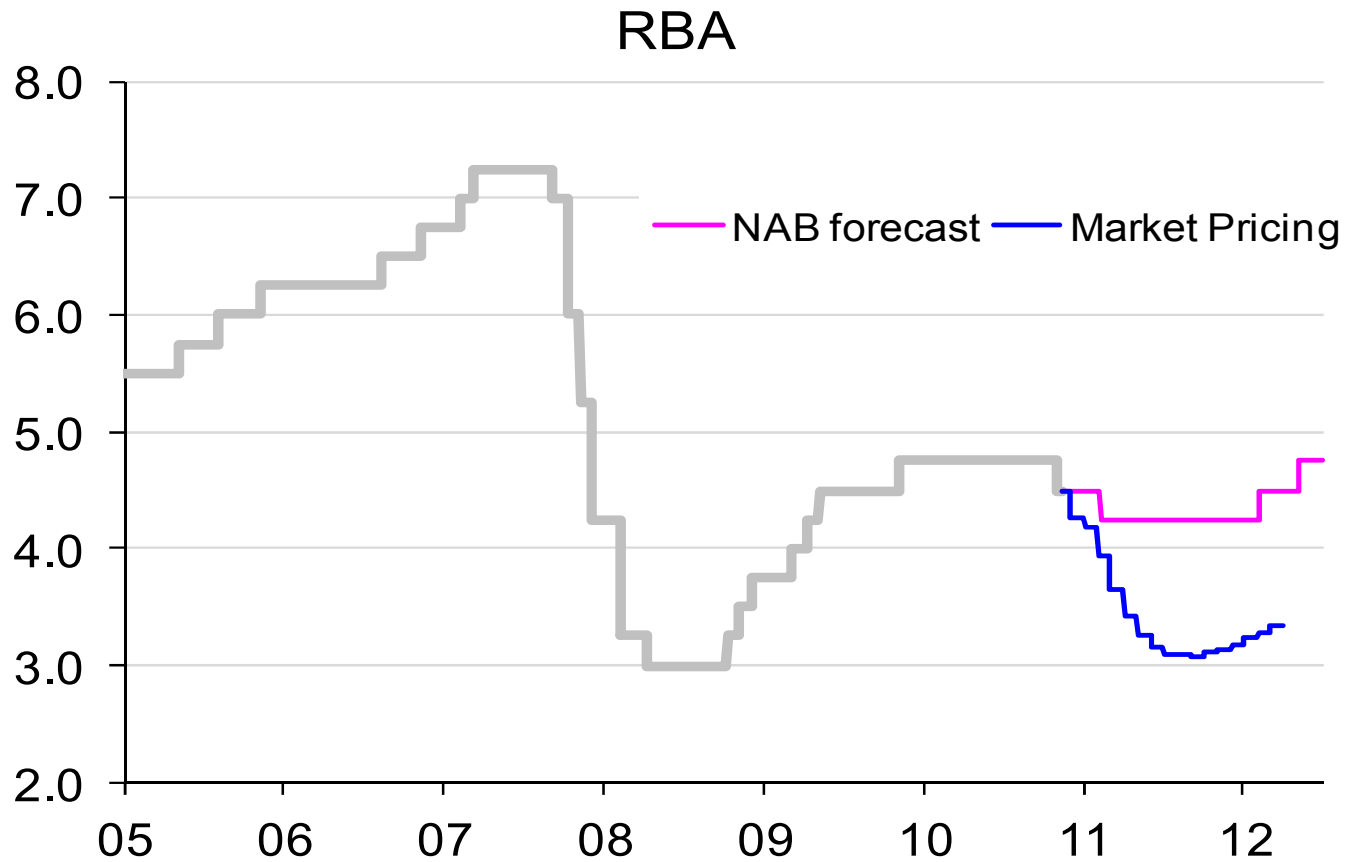
Transport inc. pipelines; Utilities inc. telecommunications

Mining capex



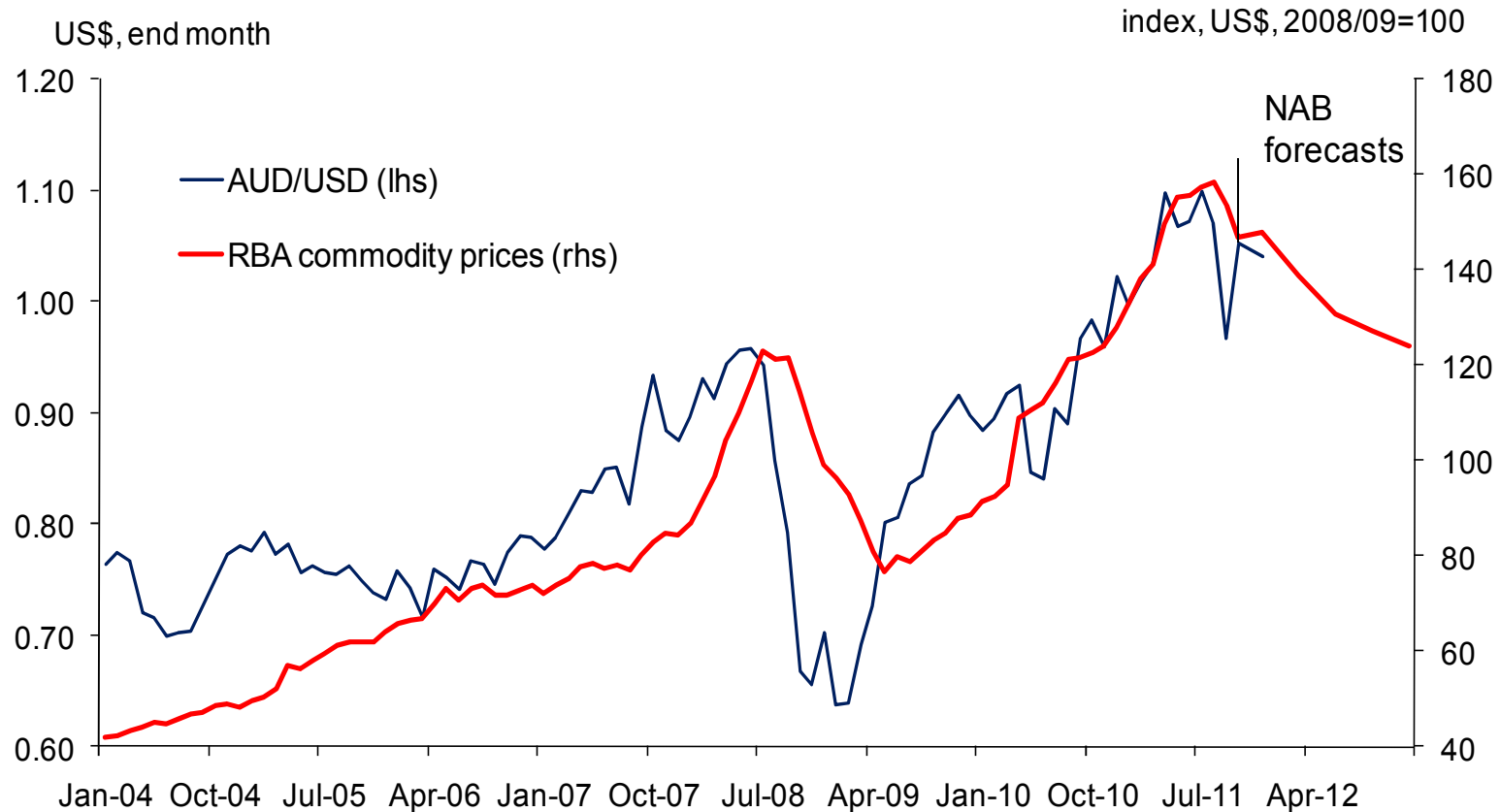
Source: ABS & NAB calculations

RBA has a little more room to cut but markets price asymmetric risks



Commodity prices have peaked and so has the AUD, both to remain historically high

AUD and Commodity prices



Source: RBA, National Australia Bank



Australian economic and financial markets forecasts

	2011-12	2012-13	2011	2012	2013
GDP	3.8	3.3	1.7	3.9	3.1
Employment^{†**}	1.9	1.9	0.7	2.4	1.7
Unemployment rate[*]	4.8	4.9	5.2	4.9	5.1
Average earnings	4.6	4.8	4.0	5.0	4.6
CPI (Ex carbon underlying)^{**}	2.0	3.0	2.5	2.7	3.1
RBA cash rate[*]	4.25	4.75	4.5	4.25	4.75
AUD/USD[*]	1.05	0.98	1.02	1.02	0.96

Important Notices

Disclaimer: This document has been prepared by National Australia Bank Limited ABN 12 004 044 937 AFSL 230686 ("NAB"). Any advice contained in this document has been prepared without taking into account your objectives, financial situation or needs. Before acting on any advice in this document, NAB recommends that you consider whether the advice is appropriate for your circumstances. NAB recommends that you obtain and consider the relevant Product Disclosure Statement or other disclosure document, before making any decision about a product including whether to acquire or to continue to hold it. Products are issued by NAB unless otherwise specified.

So far as laws and regulatory requirements permit, NAB, its related companies, associated entities and any officer, employee, agent, adviser or contractor thereof (the "**NAB Group**") does not warrant or represent that the information, recommendations, opinions or conclusions contained in this document ("**Information**") is accurate, reliable, complete or current. The Information is indicative and prepared for information purposes only and does not purport to contain all matters relevant to any particular investment or financial instrument. The Information is not intended to be relied upon and in all cases anyone proposing to use the Information should independently verify and check its accuracy, completeness, reliability and suitability obtain appropriate professional advice. The Information is not intended to create any legal or fiduciary relationship and nothing contained in this document will be considered an invitation to engage in business, a recommendation, guidance, invitation, inducement, proposal, advice or solicitation to provide investment, financial or banking services or an invitation to engage in business or invest, buy, sell or deal in any securities or other financial instruments.

The Information is subject to change without notice, but the NAB Group shall not be under any duty to update or correct it. All statements as to future matters are not guaranteed to be accurate and any statements as to past performance do not represent future performance.

The NAB Group takes various positions and/or roles in relation to financial products and services, and (subject to NAB policies) may hold a position or act as a price-maker in the financial instruments of any company or issuer discussed within this document, or act and receive fees as an underwriter, placement agent, adviser, broker or lender to such company or issuer. The NAB Group may transact, for its own account or for the account of any client(s), the securities of or other financial instruments relating to any company or issuer described in the Information, including in a manner that is inconsistent with or contrary to the Information.

Subject to any terms implied by law and which cannot be excluded, the NAB Group shall not be liable for any errors, omissions, defects or misrepresentations in the Information (including by reasons of negligence, negligent misstatement or otherwise) or for any loss or damage (whether direct or indirect) suffered by persons who use or rely on the Information. If any law prohibits the exclusion of such liability, the NAB Group limits its liability to the re-supply of the Information, provided that such limitation is permitted by law and is fair and reasonable.

This document is intended for clients of the NAB Group only and may not be reproduced or distributed without the consent of NAB. The Information is governed by, and is to be construed in accordance with, the laws in force in the State of Victoria, Australia.

Analyst Disclaimer: The Information accurately reflects the personal views of the author(s) about the securities, issuers and other subject matters discussed, and is based upon sources reasonably believed to be reliable and accurate. The views of the author(s) do not necessarily reflect the views of the NAB Group. No part of the compensation of the author(s) was, is, or will be, directly or indirectly, related to any specific recommendations or views expressed. Research analysts responsible for this report receive compensation based upon, among other factors, the overall profitability of the Global Markets Division of NAB.

United Kingdom: If this document is distributed in the United Kingdom, such distribution is by National Australia Bank Limited, 88 Wood Street, London EC2V 7QQ. Registered in England BR1924. Head Office: 800 Bourke Street, Docklands, Victoria, 3008. Incorporated with limited liability in the State of Victoria, Australia. Authorised and regulated in the UK by the Financial Services Authority. This document is intended for Investment Professionals (as such term is defined in the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005), such persons having professional experience in matters relating to investments, and should not be passed to, or relied upon by, any other person who does not have professional experience in matters relating to investments, including but not limited to persons defined as retail clients by the rules of the United Kingdom's Financial Services Authority.

USA: This information has been prepared by National Australia Bank Limited or one of its affiliates or subsidiaries ("NAB"). If it is distributed in the United States, such distribution is by nabSecurities, LLC which accepts responsibility for its contents. Any U.S. person receiving this information wishes further information or desires to effect transactions in any securities described herein should call or write to nabSecurities, LLC, 28th Floor, 245 Park Avenue, New York, NY 10167 (or call (877) 377-5480). The information contained herein has been obtained from, and any opinions herein are based upon, sources believed to be reliable and no guarantees, representations or warranties are made as to its accuracy, completeness or suitability for any purpose. Any opinions or estimates expressed in this information is our current opinion as of the date of this report and is subject to change without notice. The principals of nabSecurities, LLC or NAB may have a long or short position or may transact in the securities referred to herein or hold or transact derivative instruments, including options, warrants or rights with securities, or may act as a market maker in the securities discussed herein and may sell such securities to or buy from customers on a principal basis. This material is not intended as an offer or solicitation for the purchase or sale of the securities described herein or for any other action. It is intended for the information of clients only and is not for publication in the press or elsewhere.

Hong Kong: In Hong Kong this document is for distribution only to "professional investors" within the meaning of Schedule 1 to the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) ("SFO") and any rules made thereunder and may not be redistributed in whole or in part in Hong Kong to any person. Issued by National Australia Bank Limited, a licensed bank under the Banking Ordinance (Cap. 155, Laws of Hong Kong) and a registered institution under the SFO (central entity number: AAO169).