

## ACCI SUPPLEMENTARY, POST BUDGET SUBMISSION 2008 AFPC REVIEW

### 2008-09 Federal Government Budget Forecasts

The 2008-09 Federal Government Budget forecasts a significant slowing in Australia's rate of growth over the 2008-09 financial year. Treasury have forecast growth of 2.75 percent for 2008-09 before recovering slightly to 3 percent in the projection period.

#### Major economic parameters<sup>(a)</sup>

	Forecasts		Projections		
	2007-08	2008-09	2009-10	2010-11	2011-12
Real GDP	3 1/2	2 3/4	3	3	3
Employment	2 1/2	1 1/4	1 1/4	1 1/4	1 1/4
Wage Price Index	4 1/4	4 1/4	4	4	4
CPI	4	3 1/4	2 1/2	2 1/2	2 1/2
Nominal GDP	7 3/4	9 1/4	4 1/4	4 1/4	5 1/4

(a) All parameters except the CPI are year average percentage changes. The CPI parameter is through the year growth to the June quarter. As in previous budgets, projections assume a two-year step down in non-rural commodity prices.

The slowing of economic growth is also accompanied by a reduction of employment growth. Employment growth is forecast to fall to only 1.25 percent in 2008-09 and to remain low over the projection period. Treasury stated that:

“After a sustained period of strong growth, the global economy is expected to slow in 2008 and 2009. A sharp slowdown in the US economy is now evident in official data, with implications for growth in other countries, including Australia. Turbulence in global financial markets also remains an impediment to global growth, particularly in advanced economies.”<sup>1</sup>

Unemployment is forecast to rise. The budget has forecast unemployment to average 4.5 percent in the 2008-09 financial year further increasing to 4.75 over the 2009 calendar year. Treasury surmised that:

“The slowdown in global growth, tighter credit conditions and significantly higher interest rates are expected to slow growth in the Australian economy. As a result, conditions in the labour market are expected to ease, with some rise in the unemployment rate.”<sup>2</sup>

These forecasts highlight that while the economy will continue to expand it is expected to do so only modestly for the foreseeable future.

Specifically on global growth, Treasury indicated:

<sup>1</sup> Commonwealth of Australia, *Budget Strategy and Outlook 2008-09*, Budget Paper No. 1, 13 May 2008.

<sup>2</sup> Ibid.

“**Global growth**, in real terms, is expected to be 4 per cent in 2008 and 2009. Growth in the advanced economies is expected to slow significantly, while the emerging economies are forecast to grow robustly, notwithstanding some slowing from growth rates recorded in recent years.”<sup>3</sup>

## Small Business

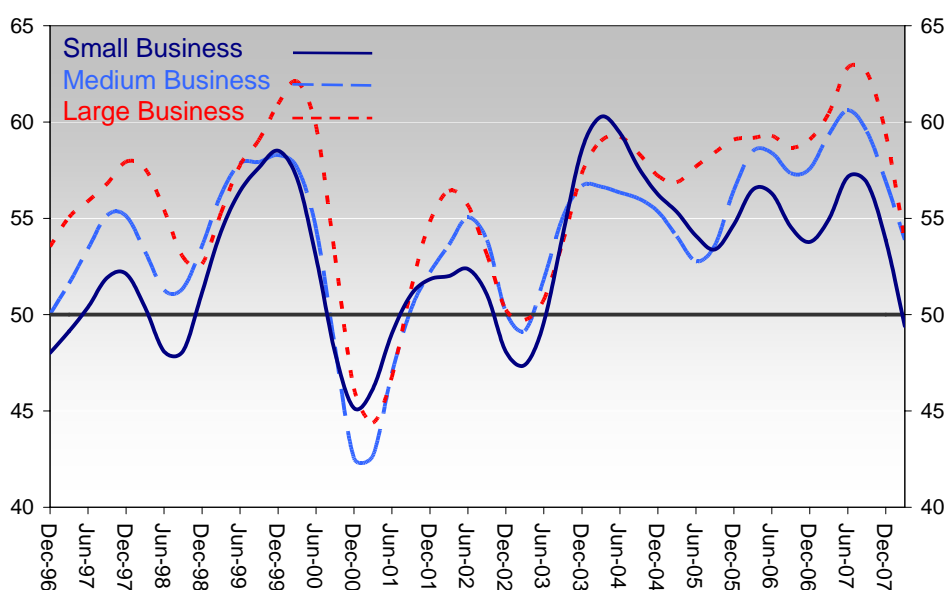
Recent data shows that conditions have continued to moderate. The latest ACCI survey, the *ACCI Small Business Survey*, was released on May 20. The ACCI Small Business Survey shows that small business conditions moderated over the March 2008 quarter, while labour costs continued to rise. At the same time, there was a moderation in the overall growth of employment.

Growth of investment in plant and equipment slowed from previous high rates, while the growth rate for investment in buildings and structures was negative.

The ACCI Small Business Survey has also found that:

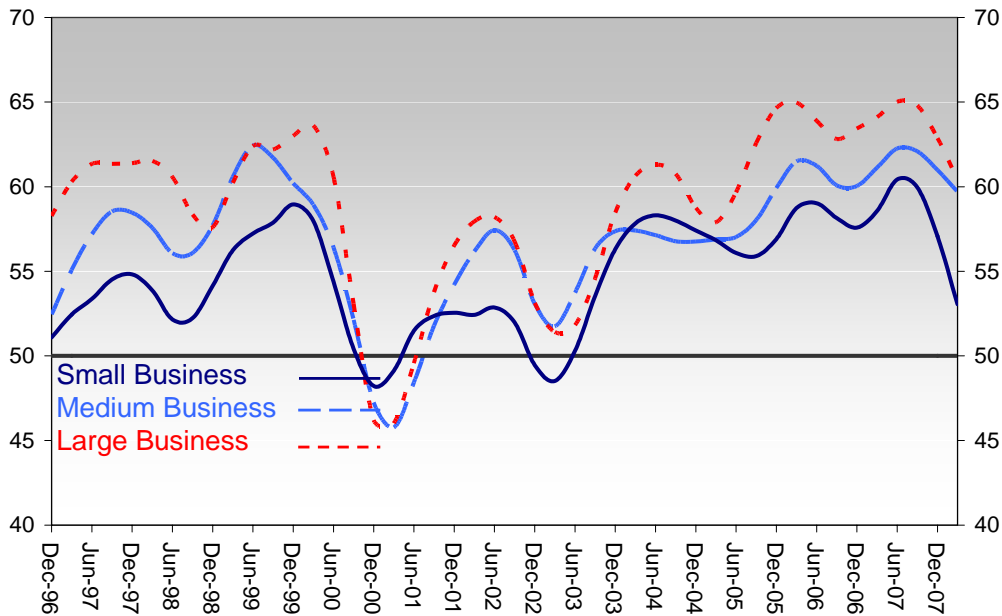
- Business expects a further moderation in Australian economic growth over the next twelve months relative to the current annual growth rate;
- The growth of sales revenue was lower over the quarter. Expectations also moderated from previous figures;
- The growth of wage and non-wage labour costs continued to be high;
- Price growth moderated over the quarter from the previous all time high level;
- Profit growth declined further below the key 50.0 level and expectations for the March quarter were also negative indicating small business was not confident of a quick turnaround.

### Small Business Conditions

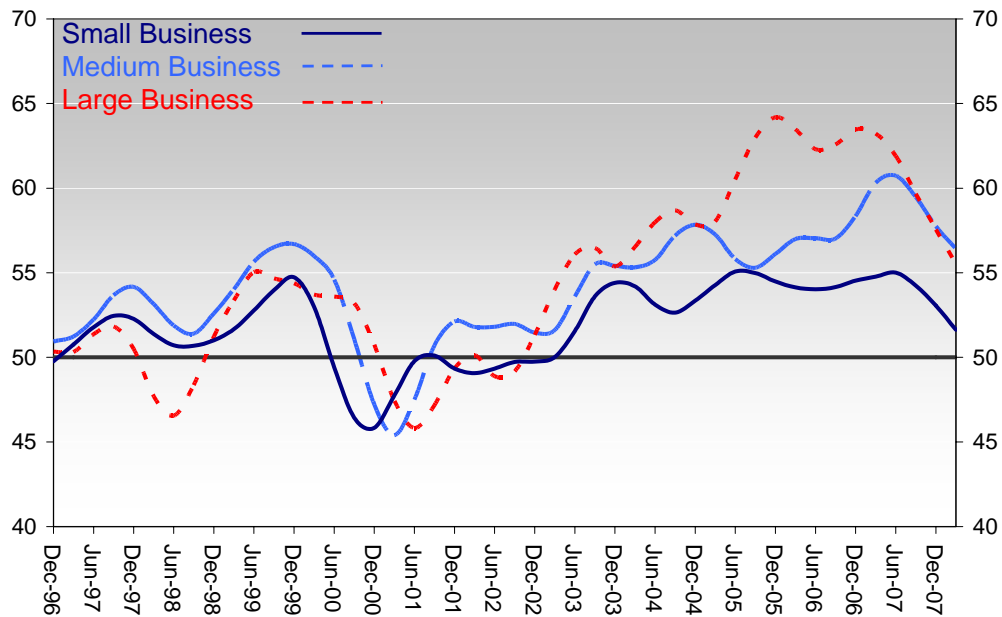


<sup>3</sup> Ibid.

### Small Business Sales Revenue Growth

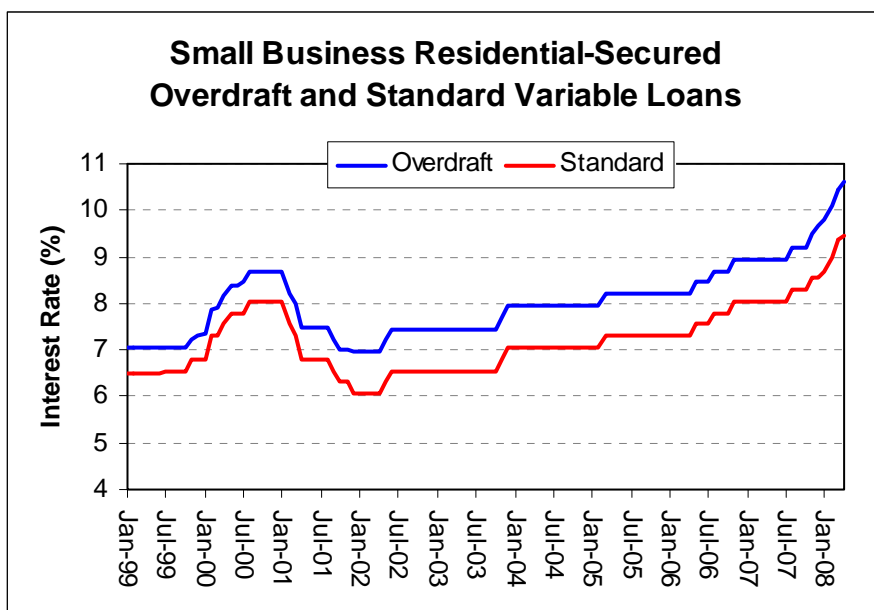


### Small Business Employment Growth



### Small Business Interest Rates

Interest rates have risen considerably over the past year. Small business residential secured overdraft interest rates have risen from 8.95 percent in April 2007 to 10.6 percent in April 2008. Households have also had increases in their borrowing costs, with the standard variable interest rate rising from 8.3 percent to 9.45 percent over the year to April 2008.



The sharply increasing interest rates for both households and business shows a clear upward trend but looking at interest rate spreads in more detail gives a more full picture of the increases.

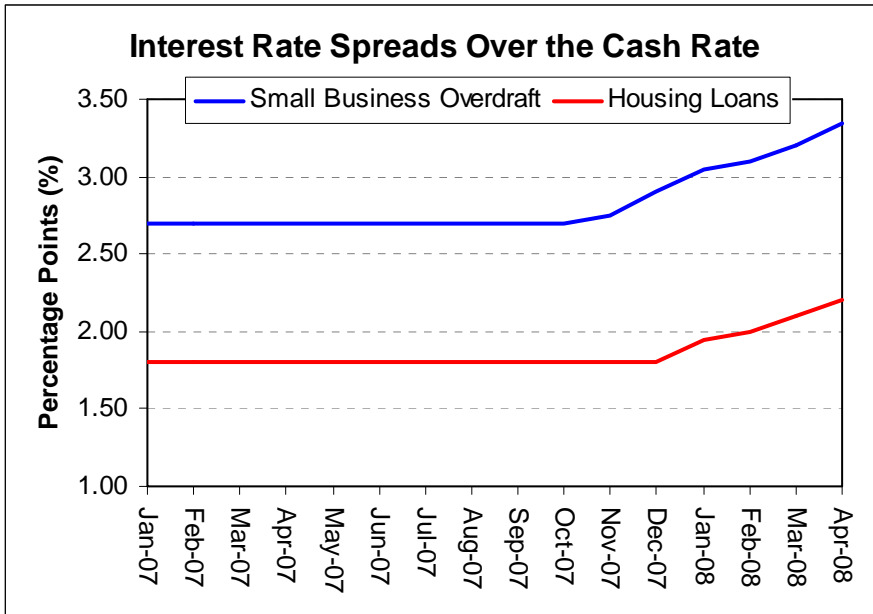
Lending interest rates compared with the RBA cash rate have increased as banks' sources of funds have been more difficult to procure.

Small business operators with secured overdrafts have had their average spread over the RBA cash rate increase by 0.65 percentage points or a 24.1 percent increase since October 2007<sup>4</sup>. The rise of the spread coupled with 'official' interest rates increases has meant that residential secured small business overdraft rates have risen from 9.2 percent in October 2007 to 10.6 percent in April 2008.

Households, despite more extensive media coverage, have had an increase of 0.4 basis points or a 22.2 percent increase<sup>5</sup>. Residential secured overdrafts for small business reached 10.45 percent in March 2008 compared with a standard variable mortgage of 9.35 percent.

<sup>4</sup> Source Data: RBA, F05 Indicator Lending Rates.

<sup>5</sup> Source Data: RBA, F05 Indicator Lending Rates and A02 Reserve Bank Of Australia - Monetary Policy Changes

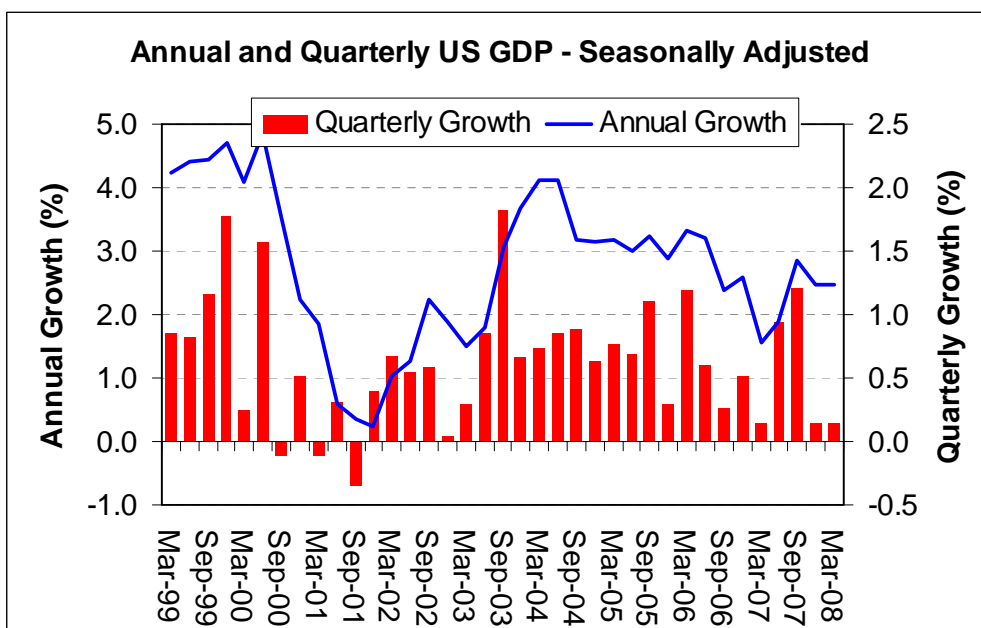


This increase above and beyond the rises imposed on the economy by the RBA will also serve to reduce growth and investment and raise the likelihood that unemployment will be higher than it otherwise would be.

## International Risks

### US GDP

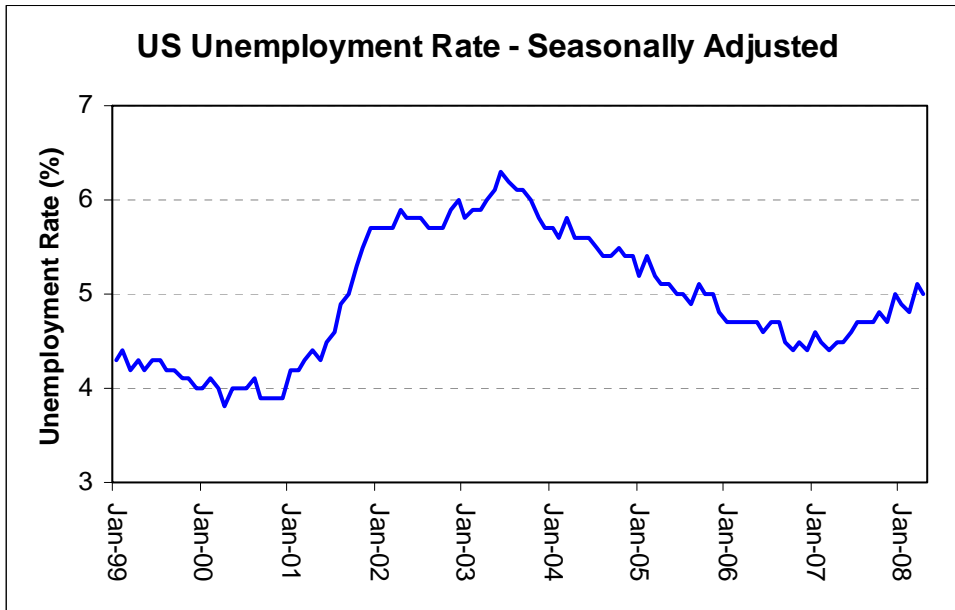
US GDP growth was very subdued over both the December 2007 and March 2008 quarters. While annual growth has held up quarterly growth has fallen off considerably. Annual growth will continue to fall should quarterly growth remain low. The annualised rate of growth given the recent growth rates is 0.6 percent for the year.



The slowdown taking place in the US economy remains a significant issue for the Australian and world economy.

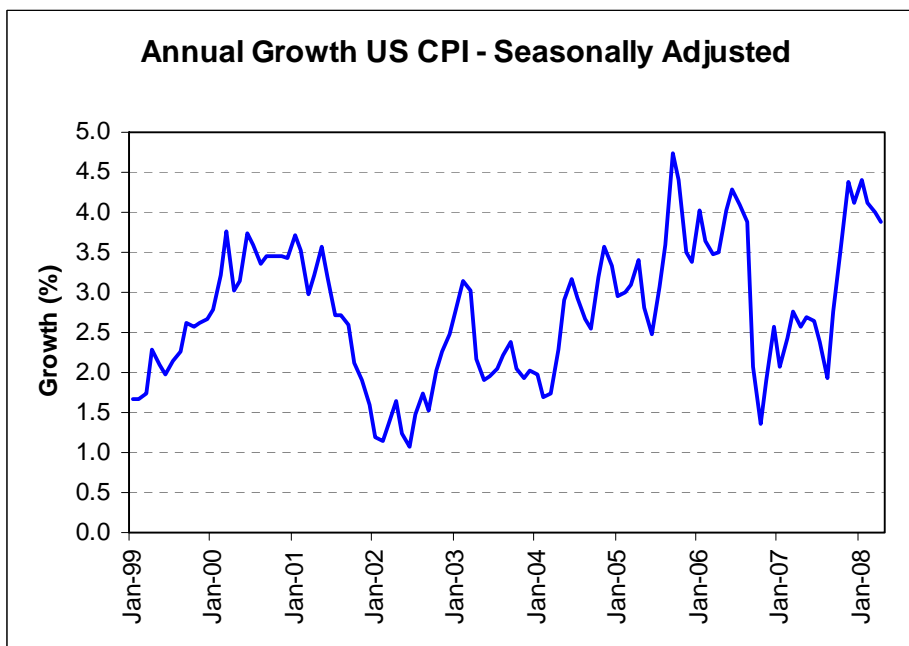
## Unemployment

The unemployment rate has been on an upward trend in the United States since the beginning of 2007. The persistent upward trend reflects slowing rates of growth in the US economy.



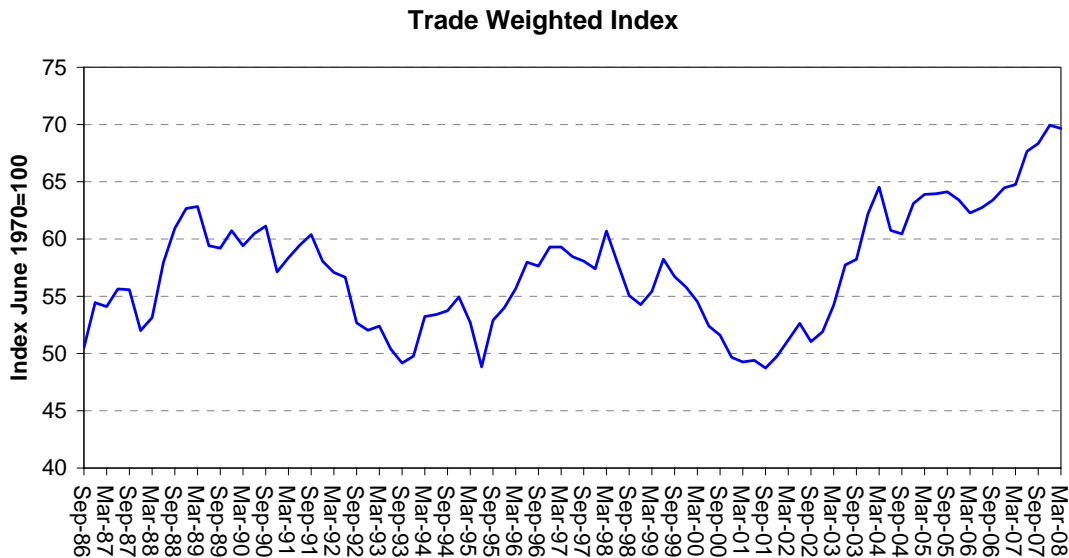
## Inflation

US Inflation data shows that some moderation has taken place but the overall rate has remained relatively high over the past six months.



## Domestic Risks

The rise of the Australian exchange rate relative to our trading partners has been a benefit to consumers through reduced import prices but has also resulted in a squeeze on domestic import competing producers in both goods and services.



The effect of exchange rate appreciations can have dramatic effects on local industry for instance the article in **Attachment A** shows the effect of the rising exchange rate on the local film industry.

## Domestic Inflation Issues

At the last RBA board meeting on May 6 the RBA left interest rates at 7.25 percent and noted that: “In the short term, inflation is likely to remain relatively high, but it should decline over time provided demand evolves as expected.”

However the bank then cautioned that: “Should demand not slow as expected or should expectations of high ongoing inflation begin to affect wage and price setting, that outlook would need to be reviewed.”

The ‘outlook’ which the Governor is referring to is the inflationary outlook given expected international and domestic factors. However there is an express warning that should wages and prices begin to be based on inflationary expectations the Bank may need to review its settings. The implication is of course that with higher inflation expectations and high wage increases interest rates would need to be higher than they otherwise would be.



## Attachment A

# Lights, camera and . . . No action!

What if you organised a mammoth film industry and nobody came? **Michaela Boland** explains how the strong dollar will hurt everyone in local movies.

Where is the next *Matrix*? Could *Superman Returns* return? Will Australia ever host production of another television series on the scale of Tom Hanks' and Steven Spielberg's year-long \$150 million shoot for *The Pacific*?

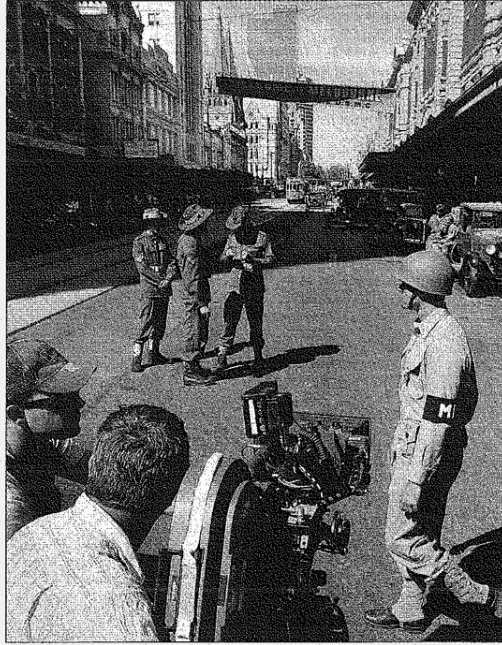
These are the questions being asked by Australia's international screen-production sector — the companies and individuals that service those big American films — as the high dollar makes this country more expensive for overseas filmmakers and deters them from filming here.

Their tone of inquiry is becoming increasingly desperate, and some companies are considering relocating to New Zealand.

It is also rumoured the producers of *The Pacific*, made for American cable channel HBO, seriously considered returning home for the last few months of that shoot as Australia was getting too expensive.

The dollar's high against the greenback has led to a big rethink of the viability of shooting US films in Australia and has rendered redundant the federal location offset, which only a year ago was raised from 12.5 per cent to 15 per cent.

In addition, many states in the US have implemented tax breaks to lure production from California and to attract shoots that had been going to Australia, Canada and elsewhere. And the three-month Writers Guild of America strike, which ended in February, has resulted in very few



Filming of *The Pacific* finishes in Melbourne this month.

Photo: CRAIG SILLITOE

projects being ready to go into production now.

"It's dead quiet right now," says Jane Griffin, spokeswoman for the NSW Film Makers Group, which represents over 1000 freelancers.

Martin Cayzer, managing director of camera equipment supplier Panavision and the chairman of Australia's

international lobby agency Ausfilm, says nothing is locked in beyond July this year.

The industry has accumulated vast overheads since 2001 when the federal government introduced the 12.5 per cent location rebate and the dollar was worth US\$5¢.

Contracts to produce the second two *Matrix* films, two *Stars Wars*

films and dozens of other major feature films and lesser productions followed. The resulting investment in cutting-edge technology, training studios and equipment enabled locals to pioneer some of the world's most advanced filmmaking.

"We have developed our infrastructure to service large American productions; individuals have invested in the most up-to-date equipment," says the NSW Film Makers Group's Griffin.

"Those outlays don't change when they are put onto a little film but they can't charge as much."

Domestic production is buoyant as a result of increased demand for drama series by local television networks, and also the domestic federal 40 per cent film offset announced in the 2007 budget now coming into effect.

*Sea Patrol*, *East of Everything* and *The Circuit* are just some of the television programs due to have a second series, as is *Underbelly* (in some form or other).

"But we need the big stuff to sustain all the little stuff," Griffin says.

*The Guardians of Ga'Hoole*, a big Warner Bros digital-animation film is in production at Animal Logic in Sydney; but because it is made mostly on computers it employs a different workforce from the one Griffin represents.

By the end of June Hugh Jackman will have ended his shoot for *Wolverine*, while in Melbourne *The Pacific* is finishing production this month.

Australian director Alex Proyas is filming *Knowing*, a US thriller with Nicholas Cage, but when that wraps there will be no more big foreign productions under way in Australia.

Millions of dollars in equipment will be sitting idle, its owners struggling with their repayments.