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# *Australian Economic Trends*

# Lumley



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## **Insurance • Finance**

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# Miscellaneous Items

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1. **The economy** Australia's energy costs rose 13.4% in the September quarter compared with an OECD average of 21.1%.
2. As a result of higher oil prices Australian companies reported the weakest business conditions in 3 ½ years in October.
3. The OECD has forecast that Australia's economic growth rate will rise from 2.6% this year to 3.2% in 2005 and 3.6% in 2007.
4. In its quarterly monetary policy statement the Reserve Bank said the economy would grow at a robust 3-3.5% by mid 2007, helped by a recovery in export volumes, the biggest improvement in the terms of trade since the 1970s and a milder than expected "soft landing" housing slowdown. It noted that monetary policy will need to be responsive to any sign that demand and inflation pressures are stronger than currently expected. The last increase in official interest rates was in March from 5.25% to 5.5%.
5. NSW Premier Morris Iemma is breaking with Bob Carr's policies by launching a drive to attract double the intake of skilled migrants to NSW.
6. **Trade** The economic planning and marketing services manager of Meat and Livestock Australia has forecast that with the return of the US to global beef markets there will be an easing of the price for beef over the next decade, away from the current record level. There will also be increasing competition from Brazil.
7. **Insurance** Swiss Re will purchase US reinsurer GE Insurance Solutions in a combined cash and share deal worth \$US6.8b, making it the world's largest reinsurer with premium income of \$US 34b and assets of \$US200b.
8. US state insurance regulators are calling on the US government to limit insurers' losses from catastrophes. "This is not a bail-out for the insurance industry. The goal first and foremost is to protect the consumers by ensuring there is available and affordable insurance to protect against catastrophic risk."
9. NSW has reduced workers' compensation premiums for the first time in 15 years. Premiums are now about 70% above those in Queensland and 35% above Victoria, approximately in line with WA and Tasmania and about 20% below SA and ACT.
10. The judge trying three former executives of FAI Insurance has directed the jury to acquit the defendants of 5 criminal charges relating to exaggeration of company profits, on the grounds that the prosecution would be unable to prove one "essential element" of the case.
11. **Superannuation** Under an approval announced by the taxation Commissioner, taxpayers aged between 55 and 64 will be allowed to draw a retirement pension as they continue to work while at the same time paying as much as 100% of their salary into superannuation.
12. Addressing the Association of Superannuation Funds, American Jack Bogle, founder of the \$US 1 trillion Vanguard investment group has warned that equity risk premiums are at historically low levels, and the risk of investors being disappointed was high.
13. **International** The US Federal Reserve has lifted interest rates for the 12th consecutive time, by 0.25% to 4% - the highest rate since May 2001.
14. In a bankruptcy hearing, Delta Airlines is seeking court approval for the airline to withdraw from its contract with its 6,000 pilots.
15. Merck, the third largest drug manufacturer in the US, plans to close five manufacturing plants by 2008 and lay off 7,000 employees (11% of its workforce).
16. According to the UK Financial Services Authority chairman, "There is increasing evidence of organised criminal groups placing their own people in [UK] financial services firms. They can increase their knowledge of firms' systems and controls and thus learn how to circumvent them to commit their frauds." Fraud within the financial industry is estimated to cost Britain 14b pounds each year.

17. Daimler-Chrysler has sold the last of its shares in Mitsubishi Motors.
18. In 2004 Japan had the world's biggest stock of robots (350,000), followed by Germany (121,000) and USA (115,000). Australia had 4,000. Europe had three quarters as many as Japan, compared with one third a decade before. (UN)
19. In 2005 to date the world's top private equity firms have invested US\$229b in buyouts, 25% more than in all 2004. \$1 in every \$8 spent on M&A this year has come from private equity. The top firms this year are Goldman Sachs Capital Partners (US\$33.5b), Kohlberg Kravis Roberts (\$26.6b), Bain Capital (\$23.3b), Texas Pacific (\$20.7b) and Carlyle Group (\$20.7b).
20. The world's largest corporate spenders on R&D are, in order, Daimler Chrysler (US\$7b), Pfizer, Ford, Toyota, Siemens, GM, Microsoft, Matsushita Electric, IBM and VW.
21. **Social** The number of babies born in Australia in 2004 (254,200) was the highest in almost a decade, and 3,100 more than in 2003. The median age of mother was 30.6 years.
22. In 2004, Australia produced more municipal waste per person (690kg) than any other OECD country except the US (730kg). The comparable figures for Canada, NZ, Japan, Britain and Sweden were 350kg, 400kg, 410kg, 580kg, and 470kg.
23. One in five Australians with ongoing health problems opted not to fill a script over a 12 month period or skipped doses because of the cost.
24. The Evatt Foundation ranks the Australian states each year on environmental, economic and social performance, using ABS and Commonwealth Grants Commission data. This year WA was again first overall, followed by SA (up from 4th), NSW, Victoria, Queensland and Tasmania. Biggest improvers were SA in social (4th to 1st) and Tasmania in environmental (5th to 1st).
25. 60% of NSW 15-25 year olds say debt is only slightly less problematic than drinking and on a par with drugs. (NSW Office of Fair Trading)
26. Young Australians are equal second with Japan (just behind Hong Kong) in mobile phone ownership. 45% of 13-15 year old Australians own one.
27. **Nuclear power** Federal Education Minister Brendon Nelson and Industry Minister Ian Macfarlane have put a formal proposal to the Prime Minister for a \$1m study on the viability of a home-grown nuclear power industry. Brendon Nelson: "We cannot responsibly dig ... 30% of the world's uranium out of the ground, export it overseas and allow some 440 reactors to operate and expand in other parts of the world and not seriously consider this as an option for ourselves."
28. **Other** If NSW were detached from the rest of Australia, it would be the world's 27th largest economy, measured in US dollars at current exchange rates.
29. Major companies such as BHP-Billiton, News Corp, James Hardie, AMP, Burns Philp, and Patrick Corporation now pay their general legal council more than \$1m.
30. From 28 November, stockbrokers will no longer be able to see on their screens which firms are placing orders or making trades. Supporters of the change say it will bring greater liquidity to the market and place all investors on a level playing field. Detractors claim it will remove transparency and increase market volatility.
31. Under a deal with the Commonwealth Director of Public Prosecutions the ACCC will seek penalties of up to two years in jail in cases where executives have misled an ACCC investigation.
32. New York mayor Michael Bloomberg spent US\$70m on his re-election campaign. His winning margin was the highest since 1933.

### Australian Share Market (at 30 November 2005)

Share price index	One month change (%)	12 month change (%)
All ordinaries	+3.9	+16.3
ASX 100	+4.0	+17.9
Mid cap 50	+5.5	+21.2
Small ordinaries	+2.9	+13.2
Consumer discretion	+0.9	-4.2
Consumer staple	+1.6	+9.8
Energy	+6.3	+46.0
Financials (ex. Property)	+4.0	+22.5
Financials	+3.8	+18.5
Health care	+8.0	+42.8
Industrials	+5.7	+11.2
Information technology	+4.2	+21.4
Materials	+5.8	+32.3
Property trusts	+3.2	+7.6
Telecom services	-6.9	-18.6
Utilities	+4.1	+28.8

### Interest rates

Category		Current rate (%)	One month change (%)	12 month change (%)
Central bank short term rates	Europe	2.00	0.00	0.00
	Japan	0.10	0.00	0.00
	UK	4.50	0.00	-0.25
	USA	4.00	+0.25	+2.00
	Australia	5.50	0.00	+0.25
90 day bank bills		5.68	-0.03	+0.22
180 day bank bills		5.70	-0.03	+0.22
3 year Comm. Bonds		5.27	-0.05	+0.32
10 year Comm. bonds		5.35	-0.09	+0.11

### Labour market

Item		Current Figure	One month change	12 month change
Employed	('000)	10,032	-56	+233
Unemployed	('000)	515	-32	+4
Not in workforce	('000)	5,849	+108	-31
Popl'n 15 & over	('000)	16,395	+19	+205
Unemployed	(%)	4.9	-0.2	-0.1
Seas. adj	(%)	5.2	+0.1	-0.1

## Overseas share markets (at 30 November 2005)

The following changes (%) have taken place over (i) the last month and (ii) the last 12 months in the share price indices of overseas markets. Figures are also given for the changes from an Australian investor's perspective ie when the indices are expressed in \$A by adjusting for changes in exchange rates.

Market	Last month			Last 12 months		
	Local currency	Exchange effect	In \$A	Local currency	Exchange effect	In \$A
UK (FT 100)	+5.0	-1.3	+3.7	+15.6	-5.9	+9.7
USA (Dow Jones)	+4.7	+2.2	+6.9	+3.9	+4.6	+8.5
USA (NASDAQ)	+6.8	+2.4	+9.2	+6.0	+4.7	+10.7
Germany (XETRA DAX)	+7.5	-0.6	+6.9	+25.0	-8.7	+16.3
Japan (NIKKEI 225)	+9.4	-1.2	+8.2	+36.4	-13.3	+23.1
HK (Hang Seng)	+4.3	+2.0	+6.3	+6.2	+5.9	+12.1
MSCI World (\$US)	+4.6	+2.3	+6.9	+9.3	+4.8	+14.1

## Exchange rates

The amount of foreign currency which the \$A will now buy and the changes (%) in purchasing power over (i) the last month and (ii) the last 12 months are shown below.

Country	\$A will purchase	Change (%) since last month	Change (%) over 12 months
USA	0.740	-2.2	-5.9
UK	0.429	+1.2	+2.7
Canada	0.864	-2.4	-6.8
EURO	0.626	+0.4	+5.5
Japan	88.220	+1.1	+9.0
NZ	1.054	-1.4	-3.9
Switzerland	0.969	+0.6	+7.8
Trade weighted index	63.7	-1.2	-0.9

## Commodity prices

The following changes (%) have taken place over (i) the last month and (ii) the last 12 months in commodity prices. Figures are also given for the changes when the prices are expressed in \$A by adjusting for exchange rates.

Commodity	Last month		Last 12 months	
	Unadjusted	In \$A	Unadjusted	In \$A
Oil	-6.1	-4.0	+15.3	+22.6
Aluminium	+9.9	+12.3	+15.5	+22.8
Copper	+7.1	+9.5	+36.7	+45.3
Lead	+2.0	+4.3	+5.0	+11.6
Nickel	+7.8	+10.2	-9.4	-3.7
Silver	+5.9	+8.2	+7.8	+14.5
Zinc	+10.2	+12.6	+48.8	+58.2
Gold	+4.6	+6.9	+10.0	+16.9
Sugar	+4.8	+7.1	+31.6	+39.9
Cotton	-6.3	-4.2	+0.9	+7.3
Wool	-2.7	-2.7	-9.9	-9.9



## **Global warming – a major issue for business**

In their August 2005 Portfolio Strategy USA publication, Goldman Sachs stated:

“Whether or not an individual investor is convinced that manmade greenhouse gases (GHGs) are leading to changes in the earth’s climate, this issue will have implications for the financial markets and for corporate performance.... Even those investors without a “socially responsible investing” mandate need to consider the financial ramifications of climate change.... There are hard dollars involved, both expenses and revenue opportunities.... Climate change is a topic that should be on the agenda of every Board of Directors.”

By way of example they noted: “In May 2005 GE launched its “ecomagination” initiative to develop new technologies to help customers meet pressing environmental needs, reduce its own GHG emissions and commit to publicly report on its progress in these areas. When a company of GE’s stature launches a large-scale program on environmental issues, it speaks to the growing focus on this topic by corporate America.”

### **“The Weather Makers” by Tim Flannery**

In his recently released book Australian scientist, explorer and conservationist Tim Flannery examines the evidence of climate change, its causes and implications. Selected summarized extracts follow.

### **Carbon Dioxide (CO<sub>2</sub>) and Global Warming**

Since 1800 a global warming of 0.63°C has occurred and the principal cause is an increase in atmospheric CO<sub>2</sub>. CO<sub>2</sub> is very long-lived in the atmosphere: about 56% of all the CO<sub>2</sub> that humans have liberated by burning fossil fuel is still aloft, which is the cause – directly and indirectly – of around 80% of all global warming.

Prior to 1800 (the start of the Industrial Revolution) there were about 280 parts per million CO<sub>2</sub> in the atmosphere; today 380 parts per million. If we wished to stabilize CO<sub>2</sub> emissions at a level double that which existed before the Industrial Revolution (widely considered the threshold of dangerous change), we would have to limit all future human emissions to less than half the 1990s levels – in a world where the human population is projected to rise mid-century to 9 billion. If we pursue business as usual, an increase of 3°C (give or take 2°C) over the 21st century seems inevitable.

### **CO<sub>2</sub> released by burning of fossil fuels**

From a climate change perspective, there’s a world of difference between using gas or coal to fuel an economy. Burning coal to generate electricity results in between 67% and 130% more CO<sub>2</sub> emissions per unit of electricity than does methane. Of the CO<sub>2</sub> released into the atmosphere by the burning of fossil fuels, 41% is contributed by coal, 39% by oil and 20% by gas.

Only 30 years ago gas supplied just 20% of the world’s energy from fossil fuel, coal 31% and oil nearly half. By the beginning of the 21st century however, gas supplanted coal in importance and, if current trends continues, by 2025 it will have overtaken oil as the world’s most important fuel source. Proven reserves of gas are sufficient to last 50 years.

Even so, about 1500 coal-fired power stations are projected to be built worldwide between now and 2030. The average life of a coal-fired power station is 50 years and the CO<sub>2</sub> they produce will continue to warm the planet for centuries after they shut down.

Approximately 100 tonnes of ancient plant life is required to create four litres of petrol. Given the vast amounts of sunlight needed to grow 100 tonnes of

plant matter, over each recent year of our industrial age, humans have required several centuries' worth of ancient sunlight to keep the economy going.

## **Global warming and species distribution**

Global warming could not have come at a worse time for biodiversity. In the past when abrupt shifts of climate occurred, trees, birds and insects would migrate the length of continents to track suitable conditions. In the modern world with 6.3b humans such movements are not possible.

Since 1950 there has been an average poleward shift in species distribution of around 6 kilometres per decade, a retreat up mountainsides of around 6 metres per decade and an advance of spring activity of 2.3 days per decade. Not all species react uniformly to climate change (eg a key food item may arrive too late or move too far north for the predator to use it; or for some species biased sex ratios at birth are determined by temperatures at which eggs are incubated. Crocodiles produce only males at higher temperatures and only females at lower ones).

A University of Leeds project examined the fate of 1100 plants and animal species in the face of climate change to 2050. It found that, at the high range of predicted temperature change, over half of the species examined are "committed to extinction".

Coral bleaching was a small scale phenomenon till the 1970s. The 1998 El Nino triggered global dying of coral. The Great Barrier Reef is the most vulnerable reef in the world to climate change. 42% of the Reef bleached in 1998 and 18% suffered permanent damage. After a renewal of El Nino conditions in 2002, live coral cover in 2003 had dropped to less than 10% on half of the Reef's area. The Australian government announced that 30% of the Reef would be protected by banning commercial fishing and severely curtailing other human activities in the protected zone. But the principal killer of the Reef, is spiraling CO<sub>2</sub> emissions. Reef scientists believe that a further rise of 1°C would see 82% of the reef bleached, 2°C 97% and 3°C total devastation.

Should Australia's temperature rise by only 3°C over his century (a realistic figure if we go on with business as usual) half of Australia's Eucalyptus species would find themselves outside their temperature zone. If they are to survive they must migrate, yet numerous barriers including the Southern Ocean and human modified landscapes lie in the way.

## **Global warming and agriculture**

Under existing projections just 2 countries (Canada and Russia) will reap 90% of the benefit that global warming brings to food crops, while other regions such as Africa and India will lose out heavily with only a small degree of warming.

In the Darfur region of western Sudan the Sahelian climate shift has driven people to desperation. Camel-herding nomads have been forced to drive their herds on to agricultural land, where they have come into conflict with farmers. The UN is now feeding 1.3 million people there and the West is focusing on religion and politics as the problem, rather than its ultimate cause – a sudden and prolonged decline in rainfall in the region. A single climatic variable was principally responsible: rising sea-surface temperatures in the Indian Ocean, which resulted from an accumulation of GHGs. The Indian Ocean is the most rapidly warming ocean on earth and as it warms the conditions that generate the Sahelian monsoon weaken.

During the first 148 years of European habitation of southwest WA (1829-1975) reliable winter rainfall brought prosperity. Since 1975 the region's average annual rainfall has been 15% lower. About half the decline results from global warming, which has pushed the temperate weather zone southward. The other half is thought to result from destruction of the ozone layer, cooling the

stratosphere over the Antarctic, hastening the circulation of cold air around the Pole and drawing the southern rainfall zone even further southwards. The 15% reduction in rainfall hides more catastrophe: winter rainfall has declined by more than 15% while summer rainfall has increased. Because summer rain is far more erratic, farmers do not plant summer crops, so the rain falls on bare fields, allowing the water to soak down to the watertable. There it meets salt, which steady westerly winds have been blowing in from the Indian Ocean for millions of years. Before land-clearing this didn't matter, for the diverse native vegetation used every drop of water that fell and the salt stayed in its crystalline form. As the summer rains began to fall on vacant wheatfields, however, water far saltier than the sea began to creep upward, killing everything it touched. Today, farmers there face the world's worst dry-land salinity.

With the decline in winter rainfall the amount of water flowing into the Perth dams dropped, initially to one half and then to one third of the 20th century average. While Perth's situation was eased by its access to subterranean water in the Gnangara Mound, declining rains mean that even it is not being recharged and its condition is now also critical.

### **Global warming and extreme weather events**

Over the past decade we have seen the most powerful El Nino ever recorded (1997-8), the most devastating hurricane in 200 years (Mitch, 1998), the hottest European summer on record (a one in 46,000 year event in which 26,000 people died), the first South Atlantic hurricane ever (2002) and one of the worst storm seasons ever experienced in Florida (2004). (Since the book went to press we have witnessed the even worse 2005 US storm season.) In the 1960s around 7m people worldwide were affected by flooding annually; today 150m.

### **Global warming and malaria**

The parasites that cause malaria will benefit enormously from climate change. Mountain valleys in the tropics support human populations in high densities. Just below these communities – in the case of PNG around 1400 metres – are great forests where no one lives because malaria is so prevalent. Future global warming will grant access to the malarial parasite and its vector mosquito to those high mountain valleys. There they will find people without any resistance to the disease. As earth warms a degree or two the percentage of humans exposed to malarial parasites will rise from 45% to 60%.

### **Alternative energy sources**

Oil and gas companies have discovered in the deserts of SA, nearly 4km below the surface, the hottest near-surface non-volcanic rock ever. The rocks are bathed in super-heated water which is under great pressure and readily recyclable. This one SA rock body is estimated to contain enough heat to supply Australia's power needs for 75 years at a cost equivalent to that of brown coal, without the CO<sub>2</sub> emissions.

Hybrid fuel vehicles match a petrol-driven engine with a revolutionary electric motor. For example, when the Toyota Prius slows or stops in traffic, the 1.5 litre petrol engine shuts down and doesn't commence until speed has been built up. The silent electric motor takes over, powered by energy generated in part from braking – energy wasted in a normal car. Relative to a 4-wheel drive the Prius cuts fuel use and CO<sub>2</sub> emissions by about 70% - the amount scientists consider is required by the world economy by 2050 in order to stabilize climate change.

### **Global warming and Australia**

Australia has been severely disadvantaged by climate change. Australia has the highest per capital greenhouse gas emissions of any industrialized nation. Ninety per cent of Australia's electricity is generated by burning coal.