



THE UNIVERSITY OF  
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# Melbourne Institute Monthly Bulletin of Economic Trends

July 2009



MELBOURNE INSTITUTE®  
of Applied Economic and Social Research



## Outlook for Australia<sup>1</sup>

	Actual			Forecasts					Actual	Forecast
	2008 Jun	2008 Sep	2008 Dec	2009 Mar	2009 Jun	2009 Sep	2009 Dec	2010 Mar	Calender Year 2008	2009
<b><i>Economic Activity</i></b>										
GDP	3.0 (0.3)	2.2 (0.2)	0.8 (-0.6)	0.4 (0.4)	0.1 (0.1)	0.1 (0.2)	0.9 (0.2)	0.9 (0.3)	2.3	0.4
Household Consumption	2.7 (-0.1)	1.8 (0.1)	0.8 (0.3)	0.8 (0.6)	1.1 (0.2)	1.4 (0.3)	1.3 (0.3)	1.0 (0.2)	2.2	1.2
Private Dwellings	3.7 (1.5)	4.7 (1.1)	1.4 (-2.6)	-5.7 (-5.6)	-7.5 (-0.5)	-7.3 (1.3)	-3.2 (1.7)	6.0 (3.4)	2.5	-5.9
Business Investment	15.0 (4.4)	14.3 (2.4)	13.0 (0.8)	1.1 (-6.1)	-4.3 (-1.3)	-5.3 (1.4)	-4.6 (1.4)	3.0 (1.5)	13.8	-3.3
Imports of Goods and Services	14.9 (3.7)	13.0 (0.6)	1.4 (-7.6)	-10.3 (-7.0)	-16.2 (-3.2)	-18.0 (-1.4)	-9.6 (1.8)	-1.2 (1.7)	10.3	-13.6
Exports of Goods and Services	5.6 (2.5)	3.3 (-0.9)	2.9 (-0.8)	3.5 (2.7)	1.6 (0.7)	3.4 (0.9)	5.5 (1.1)	4.1 (1.3)	3.9	3.5
<b><i>Inflation &amp; Financial Market</i></b>										
Underlying inflation <sup>2</sup>	4.3 (1.2)	4.6 (1.2)	4.2 (0.6)	3.9 (1.0)	3.9 (0.8)	3.1 (0.8)	3.2 (0.6)	2.8 (0.6)	4.3	3.4
Headline Inflation	4.5 (1.5)	5.0 (1.2)	3.7 (-0.3)	2.5 (0.1)	1.5 (0.5)	0.8 (0.5)	1.5 (0.4)	1.8 (0.4)	4.4	1.5
90-day Bill Rate <sup>3</sup>	7.3	7.3	4.4	3.3	3.3	3.3	3.4	3.5		
Trade Weighted Index	71.7	69.0	55.1	54.7	61.7	63.6	63.0	62.4	61.1	59.9
\$/A/\$US rate (100)	0.95	0.87	0.67	0.66	0.76	0.79	0.79	0.78		
<b><i>Labour Market</i></b>										
Unemployment Rate <sup>4</sup>	4.2	4.2	4.5	5.3	5.7	6.2	6.4	6.6	4.3	5.9
Employment <sup>5</sup>	2.4 (0.4)	2.1 (0.2)	1.6 (0.1)	0.6 (-0.2)	0.1 (-0.1)	-0.1 (0.0)	-0.1 (0.1)	0.3 (0.2)	2.2	0.1
Participation Rate <sup>4</sup>	65.5	65.4	65.3	65.5	65.4	65.3	65.2	65.0	65.4	65.3
Wage Price Index	4.2 (0.9)	4.1 (1.2)	4.3 (1.2)	4.1 (0.7)	3.8 (0.7)	3.3 (0.7)	2.8 (0.6)	2.9 (0.8)	4.2	3.5

1: Actual in black and forecasts in blue; values in parentheses are quarterly growth rates.

2: As measured by the Reserve Bank's trimmed mean measure of inflation.

3: Average over last month in quarter.

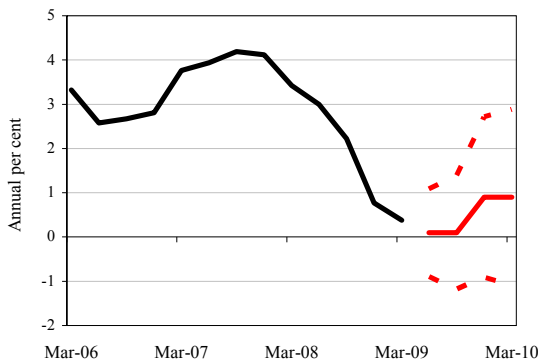
4: Average of 3-months in the quarter.

5: Calculated from quarterly employment numbers that are averaged over the 3 months in the quarter.

## Economic Activity

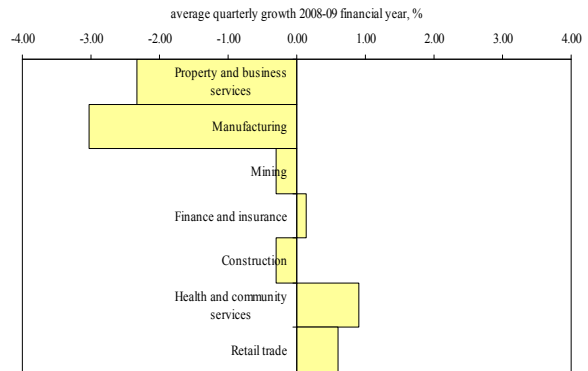
- GDP in Australia grew 0.4 per cent in the March quarter 2009, thus avoiding two consecutive quarters of negative growth or technical recession. While the slow-down seems to have bottomed out we do not expect a sharp rebound in growth in coming quarters. We expect year-end GDP growth of around zero in the June and September quarters followed by a soft rebound in activity of 0.9 per cent and 0.9 per cent in the December and March quarters (see Figure 1).
- Signs are strengthening that the economy is on a path to recovery. The annualised growth rate of both Westpac – MI Indexes of Economic Activity continued to rebound in May while the Westpac – Melbourne Institute consumer sentiment index jumped 9.3 per cent in July.
- The impact of the current slow-down has not been uniform across the different sectors of the Australian economy. Hardest hit have been manufacturing and property and business services partly reflecting the sharp slow-down in activity internationally. Resonating the resilience of the Chinese economy, declines in mining have been much less pronounced than those in manufacturing. The finance and insurance industry also steered clear of the global financial unrests and has posted a small rise so far for the 2008-09 financial year (see Figure 2).
- Looking ahead and using sectoral employment growth as an indicator for developments in the June quarter, activity in construction is expected to rebound from its weak performance (see Figure 8 in the Labour Market section).
- Reflecting the outlook for the country as a whole, we expect a gradual rebound in economic growth at the state level. The year-on-year growth rates reported on page 7 are largely driven by actual outcomes in the March quarter with a relatively large negative for Queensland and a relatively large positive quarterly growth rate for state final demand for South Australia.

**Figure 1: Growth in real GDP (per cent) (actual and forecast)**



The dashed lines are the 90% confidence bands.

**Figure 2: Changes in GDP(P) by component, ranked by share in GDP**

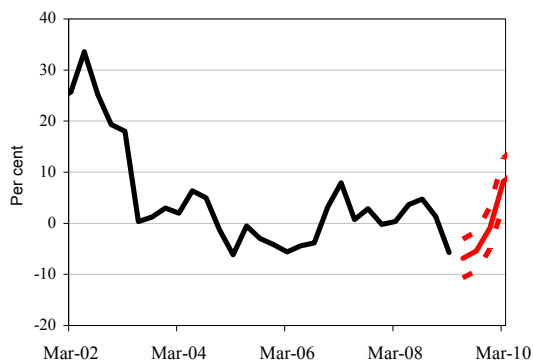


Source: ABS

## Housing and Finance

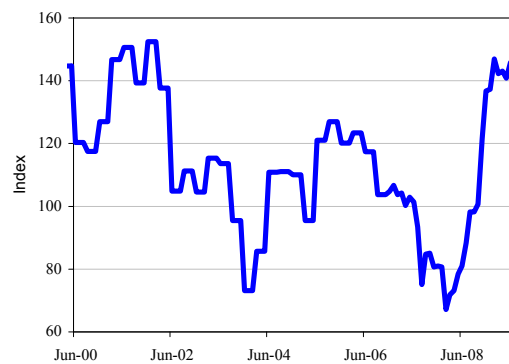
- The Time to Buy a Dwelling Index fell below 100 in July 2007 and stayed in the pessimistic region till October 2008. Since then more and more people are indicating that ‘now is a good time to buy a dwelling’. This Index is now at about the level observed in 2001 (see Figure 4).
- More importantly the perception of favourable conditions in the housing market is translated into financial and real activity. The value of dwelling commitments for both owner-occupied and investment housing increased in May 2009, for the sixth consecutive month, by 2.3 per cent. This commitment includes a high of \$17045m for owner occupied housing; alternatively a 36.3 per cent growth since May 2008.
- In terms of original numbers, the number of first home buyer finance commitments increased by 10.8 per cent to 19527 in May 2009; alternatively a 102.5 per cent change from May 2008. The number when expressed as a percentage of the total is a record 29.5 percent (compared to 17.2 in May 2008).
- Even more telling, the value of dwelling commitments for construction increased by about 7.0 per cent in May 2009 (or 46.4 per cent from May 2008). Given that dwelling construction lags financial commitments, a pick-up in dwelling construction activities is expected in the next few months.
- The Melbourne Institute forecasts a rebound in private gross fixed capital formation in dwellings starting in the September quarter 2009 (see Figure 3).
- However, there is a risk - the emergence of a housing price bubble is a possibility as the bulk of housing activity revolves around established dwellings (only about 15 per cent is concerned with the construction and purchase of new dwellings).

**Figure 3: Growth in Dwelling Gross Fixed Capital Expenditure (actual and forecast)**



The dashed lines are the 90% confidence bands

**Figure 4: Time to Buy a Dwelling Index**

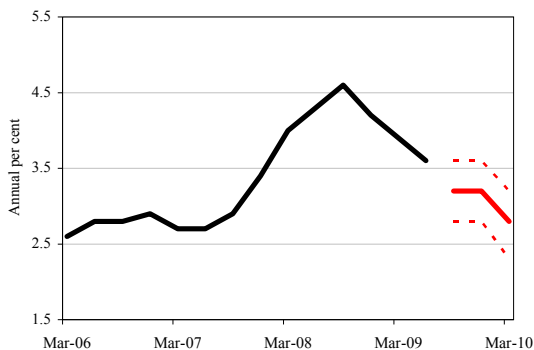


Source: Melbourne Institute

## Inflation and Interest Rates

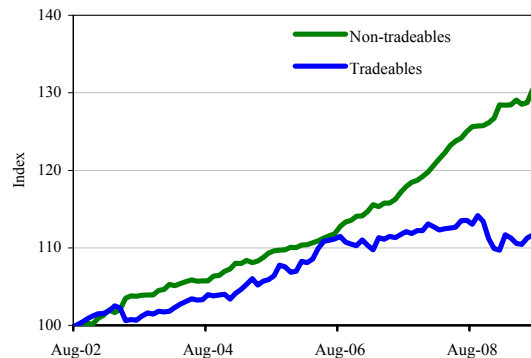
- Underlying inflation, as measured by the Reserve Bank of Australia’s trimmed mean measure of inflation, rose by 0.8 per cent in the June quarter to be 3.6 per cent higher than a year ago. Headline inflation also grew by 0.5 per cent in the June quarter, resulting in a fall in year-end inflation from 2.5 per cent in March to 1.5 per cent in June.
- Updated information regarding headline and underlying inflation is provided by the July TD – MI Monthly Inflation Gauge report. According to the Gauge, headline inflation rose 0.9 per cent in July, resulting in an increase in year-end inflation from 1.4 per cent in June to 1.9 per cent in July. Similarly, year-end trimmed mean inflation rose from 2.0 per cent in June to 2.9 per cent in July. Consumer inflationary expectations in June rose to 2.8 per cent from May’s 2.3 per cent.
- The increase in the July TD-MI Monthly Inflation figure was largely the result of a series of once per annum price hikes in utilities, and council rates and charges (as well as a price increase in telecommunications). It is, therefore, unlikely, that the significant monthly inflation observed in July will be repeated in August. These hikes have, however, further contributed to the large divergence observed between tradeable and non-tradeable inflation, which clearly shows the relevance of non-tradeables in determining the path of inflation. (Figure 6). The figures also provide an initial indication that the September quarter ABS CPI will be higher than the 0.5 per cent observed in the June quarter.
- Given the TD-MI Inflation Gauge and Consumer Inflationary Expectations data, the Melbourne Institute continues to expect trimmed mean inflation to continue declining in year-end terms over 2009 and 2010, probably falling to within the RBA’s target band in the first quarter of 2010 (Figure 5).
- The Reserve Bank has maintained the 3.0 per cent cash rate target in its last three meetings. Barring the growth effects stemming from a large positive unemployment shock, the 3.0 per cent cash rate target appears sufficient to generate consumer spending and production growth for 2009 notwithstanding higher unemployment. As such, we expect a 3.0 per cent cash rate target for the rest of 2009.

**Figure 5: Trimmed mean CPI (actual and forecast)**



The dashed lines are the 90% confidence bands.

**Figure 6: Tradeable versus non-tradeable price indices**

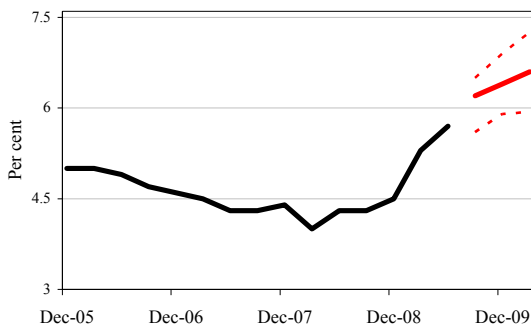


Source: Melbourne Institute.

## Labour Market

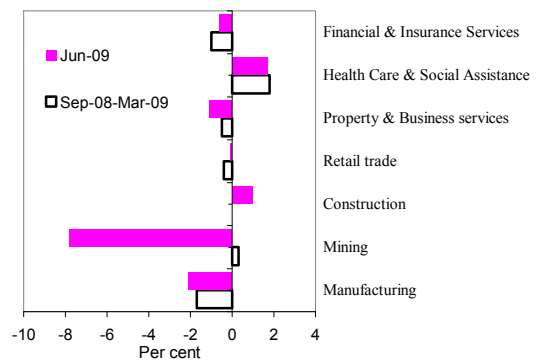
- The small increase in the unemployment rate from 5.7 per cent in May to 5.8 per cent in June was a pleasant surprise. While this rate was below the market expectation of 5.9 per cent, a closer examination of the labour flows show that the small increase in the unemployment rate was to some extent due to net exits from the labour force (about 14000).
- Since the global financial crisis, employment in several key industries has contracted (see Figure 8 for average quarterly growth rates over the 3 quarters September 2008 and March 2009). A key exception is employment in the Health Care and Social Assistance Sector which is still posting positive growth. In the June quarter of 2009, the positive employment growth in the Construction sector along with smaller contractions in the labour-intensive sectors - Financial and Insurance Services, and Retail Trade - provide some positive signs that the aggressive fiscal stimulus and monetary easing may be helping to prevent massive job losses.
- However, inflationary pressure is on the rise and attention needs to be paid to the growth in wages to ensure that the cost of labour is not detrimental to further job creations.
- Given the current economic environment, the Melbourne Institute expects an increase in the unemployment rate over the next three quarters, rising to 6.6 per cent by March 2010, with the upper bound below 8 per cent (see Figure 7).
- The Melbourne Institute expects unemployment rates in all States to rise in tandem with the National rate. The rates in New South Wales and Victoria, in particular, are forecasted to be above the expected national rate for the next three quarters.

**Figure 7: Unemployment Rate (actual and forecast)**



The dashed lines are the 90% confidence bands.

**Figure 8: Quarterly Growth in Full-time Employment by Selected Industries**



Source: ABS

**Outlook for States\***

	Actual				Forecasts				Actual	Forecast
	2008 Jun	2008 Sep	2008 Dec	2009 Mar	2009 Jun	2009 Sep	2009 Dec	2010 Mar	Calender Year 2008	2009
<i>New South Wales</i>										
Final Demand	3.2 (0.2)	3.5 (0.8)	1.4 (-0.4)	0.5 (-0.2)	0.3 (0.0)	-0.4 (0.1)	0.2 (0.2)	0.5 (0.1)	3.2	0.1
Consumption	2.1 (-0.5)	0.9 (0.0)	-0.1 (0.0)	-0.1 (0.3)	0.4 (0.0)	0.7 (0.3)	0.8 (0.2)	0.6 (0.1)	1.4	0.5
Unemployment Rate	4.6	4.8	5.2	6.1	6.3	7.0	7.3	7.6	4.8	6.7
Employment	2.7 (0.1)	1.3 (-0.7)	0.7 (0.0)	-0.9 (-0.3)	-0.9 (0.1)	0.0 (0.2)	0.4 (0.3)	0.8 (0.1)	2.0	-0.3
<i>Victoria</i>										
Final Demand	5.0 (1.5)	2.4 (-1.3)	2.7 (2.0)	0.0 (-2.1)	-1.0 (0.4)	0.2 (-0.1)	-1.5 (0.2)	0.6 (0.1)	3.5	-0.6
Consumption	2.3 (-0.4)	0.4 (-1.1)	0.3 (1.0)	-0.1 (0.3)	0.5 (0.2)	1.7 (0.1)	0.8 (0.2)	0.6 (0.1)	1.4	0.8
Unemployment Rate	4.5	4.4	4.6	5.4	5.9	6.5	7.0	7.3	4.4	6.2
Employment	2.0 (0.1)	1.3 (0.0)	0.5 (-0.1)	-0.3 (-0.3)	-0.6 (-0.3)	-1.1 (-0.5)	-1.6 (-0.6)	-1.6 (-0.2)	1.7	-0.9
<i>Queensland</i>										
Final Demand	6.1 (1.5)	6.5 (0.6)	3.2 (-0.7)	-1.7 (-3.1)	-1.9 (1.3)	-2.0 (0.5)	-0.8 (0.6)	2.9 (0.5)	5.7	-1.6
Consumption	4.5 (1.1)	3.1 (0.0)	0.2 (-1.1)	0.8 (0.9)	0.1 (0.4)	0.4 (0.4)	1.9 (0.3)	1.4 (0.3)	2.9	0.8
Unemployment Rate	3.8	3.6	3.9	4.6	5.2	5.5	5.5	5.5	3.7	5.2
Employment	1.8 (0.9)	2.7 (1.1)	2.4 (0.2)	2.6 (0.3)	1.1 (-0.5)	0.0 (0.0)	0.3 (0.6)	0.7 (0.6)	2.1	1.0
<i>Western Australia</i>										
Final Demand	7.8 (2.9)	6.8 (1.2)	7.1 (1.1)	2.9 (-2.3)	0.7 (0.7)	0.0 (0.5)	-0.2 (0.9)	3.2 (1.0)	7.6	0.9
Consumption	3.4 (-0.5)	4.2 (2.0)	4.2 (1.2)	3.5 (0.8)	4.7 (0.6)	3.2 (0.7)	2.6 (0.6)	2.4 (0.6)	4.3	3.5
Unemployment Rate	3.3	2.9	2.8	4.2	4.9	5.4	5.6	5.7	3.0	5.0
Employment	3.0 (0.1)	4.0 (2.3)	4.7 (0.9)	2.1 (-1.2)	2.0 (0.1)	0.5 (0.7)	0.2 (0.6)	1.8 (0.4)	3.9	1.2
<i>South Australia</i>										
Final Demand	2.7 (1.1)	7.1 (3.3)	3.6 (-1.7)	4.6 (2.0)	3.7 (0.2)	0.8 (0.4)	2.9 (0.3)	1.3 (0.4)	3.9	3.0
Consumption	3.1 (-0.7)	5.2 (2.3)	4.6 (1.4)	4.2 (1.2)	5.5 (0.5)	3.4 (0.3)	2.4 (0.4)	1.6 (0.4)	4.3	3.9
Unemployment Rate <sup>†</sup>	4.7	5.0	5.4	5.6	5.5	5.8	6.1	6.3	5.0	5.8
Employment <sup>†</sup>	3.1 (0.4)	2.6 (0.5)	1.5 (-0.0)	0.7 (-0.1)	0.8 (0.5)	0.9 (0.6)	1.4 (0.4)	1.7 (0.2)	2.5	1.0
<i>Tasmania</i>										
Final Demand	6.0 (3.6)	6.8 (0.4)	6.1 (1.4)	2.8 (-2.5)	0.2 (1.0)	0.5 (0.7)	-0.9 (-0.1)	1.8 (0.1)	5.8	0.6
Consumption	0.5 (0.1)	-0.6 (-0.1)	1.4 (0.8)	1.8 (1.0)	2.6 (0.8)	3.3 (0.6)	2.9 (0.4)	2.2 (0.3)	0.5	2.7
Unemployment Rate <sup>†</sup>	4.3	4.0	4.2	4.8	5.2	5.5	5.7	5.7	4.3	5.3
Employment <sup>†</sup>	4.0 (1.8)	5.2 (1.7)	4.2 (-0.1)	2.5 (-0.9)	-0.4 (-1.2)	-2.9 (-0.8)	-3.4 (-0.5)	-2.7 (-0.2)	4.1	-1.1

\* Actual in black and forecasts in blue.

† ABS has advised, starting from July 2008, that there will be a 24 per cent reduction in the sample size of the Labour Force Survey. They foresee an increase in volatility in the original and seasonally adjusted estimates and have encouraged users to focus on trend estimates. Thus, trend series have been used to forecast labour market conditions for the two smaller states of Tasmania and South Australia.

## Around the world<sup>†</sup>

- Leading and coincident indexes for key economies are shown in the Table below. Consensus is rising that the worst may be over but global economic growth is unlikely to rebound rapidly.
- Recent data suggest that the pace of economic contraction may be slowing in the US. Consumer spending, which dropped sharply in the second half of 2008, has been roughly flat since the turn of the year, and consumer sentiment has improved. But a weak labour market and declines in equity and housing wealth continue to weigh on consumer spending. Businesses remain very cautious and continue to reduce their workforces and capital investments. On a more positive note, firms are making progress in shedding the unwanted inventories that they accumulated following last year's sharp downturn in sales.
- Economic activity in the euro area is likely to remain weak for the remainder of this calendar year but is expected to decline less strongly than was the case in the March quarter 2009. Further deteriorations in labour markets are likely. Annual inflation turned negative in June and continued deflation may become a real worry.
- In Japan, exports are expected to bottom out and start recovering. Domestic private demand and business fixed investment have declined substantially and are likely to continue falling. Private consumption continues to weaken as employment and income continue to deteriorate.
- In China, the deceleration of the economy seems to have stopped. Although exports continue to decline, domestic demand is growing rapidly. Economic conditions in the NIEs and the ASEAN countries continue to deteriorate, but the pace of decrease in exports and production is moderating. Economic growth in India has been decelerating significantly.

## International indicators

	Leading indexes: per cent growth rates				Coincident indexes: per cent growth rates			
	One month ago	Latest month		Annual rates (per cent)	One month ago	Latest month		
United States	1.7	6.0	May	Slow	-7.0	-6.8	May	Recessionary
Canada	0.2	1.7	Apr	Recessionary/Slow	-6.0	-5.5	Apr	Recessionary
Mexico	-1.3	-0.4	Apr	Recessionary/Slow	-8.7	-8.7	Apr	Recessionary
Germany	-13.9	-14.0	Apr	Recessionary	-14.0	-14.6	Apr	Recessionary
France	-7.2	-6.4	Apr	Recessionary	-10.0	-9.2	Apr	Recessionary
United Kingdom	-0.1	3.5	Apr	Slow	-4.8	-3.8	Apr	Recessionary
Italy	-25.3	-25.9	Apr	Recessionary	-12.3	-11.8	Mar	Recessionary
Spain	-16.2	-16.1	Apr	Recessionary	-20.4	-14.8	Apr	Recessionary
Switzerland	-5.8	-8.3	Apr	Recessionary	-3.8	-5.1	Mar	Slow
Sweden	-5.6	-4.1	Apr	Recessionary	-13.9	-14.7	Apr	Recessionary
Japan	-15.8	-12.8	Apr	Recessionary	-16.8	-15.8	Apr	Recessionary
China	5.2	6.2	Apr	Slow/Average	8.2	7.6	Mar	Slow
India	6.2	3.3	Apr	Slow/Average	1.6	4.1	Mar	Slow
South Korea	2.1	8.1	Apr	Slow	-9.3	-7.5	Apr	Recessionary
Taiwan	0.2	7.2	Apr	Slow/Average	-20.6	-17.7	Apr	Recessionary
New Zealand	-4.5	-2.9	Apr	Recessionary/Slow	-11.3	-11.4	Mar	Recessionary

Source: Economic Cycle Research Institute, *International Cyclical Outlook*, June 2009

<sup>†</sup> This is an extract from the Westpac – Melbourne Institute Indexes of Economic Activity, July 2009.

**Precision of Forecasts for Australia and States**

	Forecasts				Calendar Year 2009
	2009 Jun	2009 Sep	2009 Dec	2010 Mar	
<b>Australia</b>					
<i><b>Economic Activity</b></i>					
GDP	0.6	0.9	1.1	1.2	<b>0.7</b>
Consumption	0.5	0.8	1.0	1.1	<b>0.7</b>
Dwelling	2.3	2.4	2.5	2.8	<b>1.9</b>
Business Investment	5.2	6.0	6.7	7.5	<b>4.6</b>
Import	2.5	4.2	5.8	6.6	<b>3.7</b>
Export	2.6	3.4	4.0	4.4	<b>2.9</b>
<i><b>Inflation &amp; Financial Market</b></i>					
Underlying Inflation		0.2	0.3	0.4	<b>0.3</b>
Headline Inflation		0.4	0.7	0.9	<b>0.6</b>
90 day bill		0.4	0.7	0.9	<b>0.6</b>
Trade Weighted Index		2.2	3.5	4.1	<b>2.3</b>
<i><b>Labour Market</b></i>					
Unemployment Rate		0.2	0.3	0.5	<b>0.3</b>
Employment		0.4	0.6	0.7	<b>0.5</b>
Participation Rate		0.2	0.3	0.4	<b>0.3</b>
Wage Price Index		0.3	0.4	0.4	<b>0.4</b>
<b>States</b>					
<i><b>New South Wales</b></i>					
Final Demand	1.0	1.5	1.9	2.3	<b>1.0</b>
Consumption	0.7	1.1	1.4	1.6	<b>0.5</b>
Unemployment Rate		0.2	0.3	0.5	<b>0.1</b>
Employment		0.5	0.8	1.1	<b>0.3</b>
<i><b>Victoria</b></i>					
Final Demand	1.2	1.7	2.2	2.7	<b>1.1</b>
Consumption	0.7	1.0	1.4	1.7	<b>0.6</b>
Unemployment Rate		0.3	0.5	0.6	<b>0.2</b>
Employment		0.5	0.8	1.1	<b>0.4</b>
<i><b>Queensland</b></i>					
Final Demand	1.4	2.0	2.5	3.0	<b>1.4</b>
Consumption	0.8	1.2	1.6	2.1	<b>0.8</b>
Unemployment Rate		0.3	0.5	0.7	<b>0.2</b>
Employment		0.6	1.0	1.4	<b>0.4</b>
<i><b>Western Australia</b></i>					
Final Demand	2.1	2.9	3.9	4.6	<b>2.2</b>
Consumption	0.9	1.3	1.6	1.9	<b>0.9</b>
Unemployment Rate		0.3	0.5	0.7	<b>0.2</b>
Employment		0.7	1.0	1.4	<b>0.5</b>
<i><b>South Australia</b></i>					
Final Demand	1.4	1.9	2.3	2.7	<b>1.5</b>
Consumption	0.9	1.3	1.6	1.9	<b>1.1</b>
Unemployment Rate		0.2	0.3	0.5	<b>0.2</b>
Employment		0.4	0.7	1.0	<b>0.5</b>
<i><b>Tasmania</b></i>					
Final Demand	2.5	2.9	3.3	3.7	<b>2.2</b>
Consumption	1.0	1.5	1.7	2.0	<b>1.2</b>
Unemployment Rate		0.3	0.5	0.6	<b>0.3</b>
Employment		0.6	1.1	1.5	<b>0.7</b>

**Melbourne Institute  
Monthly Bulletin of Economic Trends**

The *Melbourne Institute Monthly Bulletin of Economic Trends* provides forecasts of the state of the Australian economy. Variables forecasted include: the growth in GDP, consumption and the unemployment rate as well as the outlook for inflation, the 90-day bill rate and the exchange rate. The forecasts are generated using econometric techniques which combine both historical information and forward information contained in, for example, consumer expectations, leading indexes of economic activity, and financial futures. The monthly updates of forecasts four quarters ahead provides timely on-going information in advance of official quarterly data.

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For information on the data contained in the report contact the Melbourne Institute, The University of Melbourne, on (03) 8344 2196.

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