

Week Commencing July 17, 2006



# AUSTRALIA & NEW ZEALAND WEEKLY

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## NZ braced for higher CPI

### Global trends now work for the central bank

With higher oil prices and a weaker currency we expect today's New Zealand second quarter consumer price increase to come in at 1%, a little higher than the 0.8% projected by the RBNZ in March and a little below the current consensus of 1.2%. An increase of the size we expect will take annual headline inflation from 3.3% last time to 3.4%, well above the RBNZ target of 1% to 3% in the medium term. But despite high headline inflation and despite last week's reported pickup in May retail sales confirming that NZ has dodged the recession threatened in the second half of last year, we doubt the RBNZ will seriously ponder any further tightening for the scheduled cash rate review Thursday next week.

In common with most inflation targeting central banks, the RBNZ has been prepared to look through the oil price component of inflation, so long as it does not flow through to general inflation. It is not a perfect measure, but consumer price inflation excluding transportation has been remarkably modest. It was 2.8% in the year to the March quarter, and it has been essentially unchanged for the last five years. This is still somewhat higher than the informal target of 2.5% for headline inflation, but the persistence of the outcome does suggest that despite very low unemployment and a period of very strong demand growth earlier in the decade, inflation remains very well controlled.

It was telling that in a speech last week RBNZ Governor Alan Bollard flatly said that the RBNZ "finished its tightening cycle" at the beginning of 2006. His speech contrasted the difficulties of running a tightening policy in New Zealand while cash rates in the rest of the world were unusually low, to the circumstances today where rates are steadily increasing in the major economies. The global rise in rates helps by taking bond rates up and the NZ dollar down, encouraging the shift from domestic demand to exports which Dr Bollard has long sought. The argument is not entirely convincing, in that the increase in the key five year bond rate has been only 20 basis points in the last year. But the New Zealand dollar has dropped 15%, which helps.

## Numbers point to Australian tightening

### RBA wants controlled expansion

We don't expect much increase in the core rate but even so Australia's second quarter consumer price index next week is unlikely to impede a Reserve Bank tightening at the beginning of the August. The headline result alone will be sufficient excuse for a tightening decided on other grounds. If only because of higher petrol prices it's very probable the quarterly headline number will be over 0.6%, enough to take the headline annual rate over the 3% recorded last time. The weighted and trimmed mean measures used by the Bank will highly likely remain under 3% in annual terms and may well show no acceleration in quarterly terms. Whether headline or core, however, contemporary inflation is not the motive for tightening. It is a useful rationale. The real motive is the likelihood of inflation being above the band in a year's time. In that respect the important fact is that Australian demand and output are both growing robustly, at a time when the rate of unemployment is at a thirty year low.

Despite the high headline rate, inflation is well under control. As RBA Deputy Governor (and likely Governor in two months) Glenn Stevens said last week, wages growth has been slower than one might have expected given the strength of the labour market. It is also true that Australian consumer price inflation ex transportation have persistently fallen over the last five years, from over 3% to a steady 2.5%. If contemporary inflation was all that mattered, the RBA would not need to respond to the headline rate.

But as Mr. Stevens also explained, the Bank's decision are based on a "least regrets" criterion, in which the policy action selected is the one that is assessed as having the least risk of proving seriously wrong. Given that the May 25bp increase had very little impact, there is not much chance that another agreed at the August 1 board meeting will seriously injure growth. But there is a risk that if the RBA leaves the rate unchanged it will fall behind in controlling the upswing as it runs into capacity constraints. The strength of growth is apparent across most of the numbers in recent weeks. Jobs growth totaled 100,000 through May and June, and there have been nearly 200,000 full time jobs added since October last year. On both the RBA credit measures and Australian Bureau of Statistics housing finance numbers, home lending growth has bottomed out and is beginning to increase – a trend which suggests the national downturn in housing construction will also turn up by the end of the year. It's true that export growth has been deeply disappointing, and was again in the May numbers published last Friday. Exports fell 3% for the month, creating a trade deficit well over twice the size we expected. It's strange indeed that in a

concerted and robust global upswing the value of Australian seasonally adjusted exports in May should be below of those of December, but it won't stop the RBA tweaking the overnight rate to 6% the week after next.

**John Edwards**

# Weekly Calendar

Week commencing Monday July 17, 2006

Country/ Region	Event or Economic Release	Period	HSBC	Market F'casts		Range	Actual Previous
				Cons			
<b>Monday July 17, 2006</b>							
NZ	Consumer Price Index	Quarter	Q2	1.0%	1.2%	-	0.6%
		Year	Y2 June	3.4%	3.6%	-	3.3%
JPN	Public holiday Marine Day						
EMU	CPI (10:00 BST)	Year	Jun	2.5%	2.5%	-	2.5%
EMU	Industrial production (10:00 BST)	Month	May	1.1%	1.4%	-	-0.6%
		Year		4.2%	4.2%	-	1.9%
US	Empire manufacturing (13:30 BST)	Month	Jul	16	21	-	29
US	Industrial production (14:15 BST)	Month	Jun	0.6%	0.4%	-	-0.1%
		Capacity utilization		82.1%	81.9%	-	81.7%
<b>Tuesday July 18, 2006</b>							
UK	RICS house prices (00:30 BST)	Prices rising / falling	Jun	+15	+20	-	+20
UK	CPI (09:30 BST)	RPI – month	Jun	0.0%	0.1%	-	0.6%
		RPI – year		2.8%	2.9%	-	3.0%
		RPIX		2.7%	2.9%	-	2.9%
		CPI – year		2.1%	2.2%	-	2.2%
GER	ZEW Survey (10:00 BST)	Expectations	Jul	40.0	34.0	-	37.8
		Current conditions		15.0	N/A	-	11.9
US	PPI (13:30 BST)	<b>Month</b>	Jun				
		Headline		0.2%	0.3%	-	0.2%
		Core		0.2%	0.2%	-	0.3%
		<b>Year</b>					
		Headline		4.5%	4.6%	-	4.5%
		Core		1.9%	1.9%	-	1.5%
US	Net foreign security purchases (14:00 BST)	Month (USDbn)	May	46.7	-	-	55.0
<b>Wednesday July 19, 2006</b>							
NZ	Migration (June)						
UK	Bank of England minutes (09:30 BST)						
US	CPI (13:30 BST)	<b>Month</b>	Jun				
		Headline		0.2%	0.2%	-	0.4%
		Core		0.2%	0.2%	-	0.3%
		<b>Year</b>					
		Headline		4.3%	4.3%	-	4.2%
		Core		2.6%	2.6%	-	2.4%
US	Housing starts (13:30 BST)	Month ('000)	Jun	1890	1910	-	1957
US	Bernanke testimony (15:00 BST)						
<b>Thursday July 20, 2006</b>							
UK	Retail sales (09:30 BST)	Month	Jun	0.3%	0.2%	-	0.5%
		Year		2.8%	2.7%	-	4.0%
US	Jobless claims (13:30 BST)	Week ('000)	Wk 15	320	-	-	332
			July				
US	Philadelphia Fed (17:00 BST)	Month	Jul	13.0	12.5	-	13.1
US	FOMC minutes (19:00 BST)		Jun 29				

# Weekly Calendar (continued)

Week commencing Monday July 17, 2006

Country/ Region	Event or Economic Release	Period	HSBC	Market F'casts Cons	Range	Actual Previous
<b>Friday July 21, 2006</b>						
AU	International Trade Price (Q2)					
JPN	All industry activity index (00:50 BST)	Month	May	-0.5%	-	1.3%
		Year		2.4%	-	2.1%
UK	GDP (09:30 BST)	Quarter	Q2, 1 <sup>st</sup> estimate	0.8%	0.7%	0.7%
		Year		2.6%	2.5%	2.3%
<b>During the Week</b>						
CH	GDP	Year	Q2	11.3%	10.4%	10.3%
CH	PPI	Year	Jun	2.8%	2.7%	2.4%
CH	CPI	Year	Jun	1.5%	1.5%	1.4%
CH	Retail Sales	Year	Jun	14.8%	14.2%	14.2%
CH	Industrial Production	Year	Jun	18.5%	17.3%	17.9%
CH	Fixed Asset Investments	Year	Jun	33.0%	30.0%	30.3%

Source:- Dow Jones, Reuters, Bloomberg

Notes:- p=preliminary, r=revised, n.f.=not forecast, n.s.a.=not seasonally adjusted, ann.=annualised, bn=billion, m=million

# Monthly Economic Calendar

Week commencing July 24, 2006

Monday July 24, 06	Tuesday July 25, 06	Wednesday July 26, 06	Thursday July 27, 06	Friday July 28, 06
AU Producer Price Index (2Q)		AU Consumer Prices (2Q) NZ Trade Balance (Jun) US Existing Home Sales (June) US Richmond Fed Manufact. Index (Jul) JPN Mercnds Trade Balance Total (Jun) UK CBI July Industrial Trends  26-31 July UK Nationwide House Prices (Jul)	NZ RBNZ Official Cash Rate (Jul 27) US Fed's Beige Book US Durable Goods Orders (Jun) US Initial Jobless Claims (Jul 23)	US New Home Sales (Jun) US GDP Price Index (2Q A) US Personal Consumption (2Q A) US Employment Cost Index (2Q) US U. of Michigan Confidence (Jul F) JPN National Consumer Prices (Jun) JPN Retail Trade (Jun P)
Monday July 31, 06	Tuesday August 1, 06	Wednesday August 2, 06	Thursday August 3, 06	Friday August 4, 06
AU TD Securities Inflation (Jul) JPN Industrial Productions (Jun P) UK Net Consumer Credit (Jun) UK Net Lending Sec. on Dwellings (Jun) UK Mortgage Approvals (Jun) EC Euro-Zone Indust. Confidence (Jul) EC Euro-Zone Consumer Confidence (Jul) EC Euro-Zone CPI Estimate (Jul) US Fed's Poole Speaks to Southern Legislative Conference	AU Reserve Bank August Policy-setting meeting AU AiG Performance of Mfg Index (Jul) AU Building Approvals (Jun) UK PMI Manufacturing (survey) (Jul) EC PMI Manufacturing (survey) (Jul) US Chicago Purchasing Manager (Jul) US Personal Income (Jun) US Personal Spending (Jun) US PCE Deflator (Jun)	AU RBA Cash Target (Aug) AU Retail Sales Ex Inflation (2Q) AU Retail Sales (JUN) JPN Monetary Base (Jul) UK Bank of England's Monetary Policy Committee Meets EC Euro-Zone PPI (Jun) US ISM Manufacturing (Jul)	AU AiG Performance of Service Idx (Jul) UK BoE Announces Rates (Aug 4) EC ECB Announces Interest Rates (Aug) EC Euro-zone July Services PMI US Initial Jobless Claims (Jul 30)  3 – 9AUG UK HBOS Plc house prices (Jul)	AU Reserve Bank Quarterly Monetary Policy Statement US Factory Orders (Jun) US ISM Non-Manufacturing (Jul) US Non-farm Payrolls (Jul)
Monday August 07, 06	Tuesday August 08, 06	Wednesday August 09, 06	Thursday August 10, 06	Friday August 11, 06
AU ANZ Job Advertisements (JUL) NZ Labor Cost Private Sector UK Industrial Production (JUN) UK Industrial Production (JUN) JPN Leading Economic Index (JUN P)	UK BRC July Retail Sales Monitor US Consumer Credit (JUN) US Nonfarm Productivity (2Q P) US Unit Labor Costs (2Q P) US Fed's Open Market Committee Meets on Interest Rates, Economy JPN Bank Lending (JUL) JPN Machine Tool Orders (JUL P)	AU Home Loans (JUN) UK Bank of England Quarterly Inflation Report US FOMC Rate Decision Expected (AUG 9) US ABC Consumer Confidence (AUG 8)	AU Employment Change (JUL) NZ Unemployment Rate (2Q) NZ ANZ-Business NZ PMI (JUL) US Trade Balance (JUN) US Initial Jobless Claims (AUG 6) US Continuing Claims (JUL 30) JPN Current Account Total (JUN) JPN BoJ Monetary Policy Meeting EC ECB Publishes Aug. Monthly Report	AU Trade Balance (JUN) US Import Price Index (JUL) US Import Price Index (JUL) US Advance Retail Sales (JUL) JPN Gross Domestic Product (2Q P) JPN BoJ Monetary Policy Announcement JPN Industrial Production (JUN F) JPN Capacity Utilization (JUN F) JPN BoJ Monthly Report

# Monthly Economic Calendar...(continued)

Week commencing July 24, 2006

Monday July 14, 06	Tuesday July 15, 06	Wednesday July 16, 06	Thursday July 17, 06	Friday July 18, 06
<a href="#">NZ Retail Sales (Jun)</a> <a href="#">UK PPI. (Jul)</a> <a href="#">EC Euro-Zone GDP s.a. (2Q A)</a>	<a href="#">NZ Producer Prices-Inputs (2Q)</a> <a href="#">NZ Producer Prices Outputs (2Q)</a> <a href="#">UK RICS House Price Balance (Jul)</a> <a href="#">UK CPI (Jul)</a> <a href="#">US Producer Price Index (Jul)</a> <a href="#">US Empire Manufacturing (Aug)</a> <a href="#">US Net Foreign Security Purchases (Jun)</a>	<a href="#">AU Westpac August Consumer Confidence</a> <a href="#">AU Wage Price Index (2Q)</a> <a href="#">NZ Non Resident Bond Holdings (Jul)</a> <a href="#">UK Bank of England Minutes</a> <a href="#">UK Avg Earnings inc bonus (Jun)</a> <a href="#">UK ILO Unemployment Rate (Jun)</a> <a href="#">UK Manu.Unit Wage Cost (Jun)</a> <a href="#">US NAHB Housing Market Index (Aug)</a> <a href="#">US ABC Consumer Confidence (Aug 15)</a> <a href="#">US MBA Mortgage Applications (Aug 12)</a> <a href="#">US Consumer Price Index (Jul)</a> <a href="#">US Housing Starts (Jul)</a> <a href="#">US Building Permits (Jul)</a> <a href="#">US Industrial Production (Jul)</a> <a href="#">US Capacity Utilization (Jul)</a> <a href="#">JPN BoJ Monetary Policy Meeting Minutes</a>	<a href="#">AU Melbourne Institute Consumer Inflation Expectations for August</a> <a href="#">AU Reserve Bank of Australia July Bulletin</a> <a href="#">AU Average Weekly Wages (May)</a> <a href="#">UK Retail Sales (Jul)</a> <a href="#">US Initial Jobless Claims (Aug 13)</a> <a href="#">US Continuing Claims (Aug 6)</a> <a href="#">EC Euro-Zone CPI (Jul)</a> <a href="#">EC Euro-Zone CPI (Jul)</a> <a href="#">EC Euro-Zone Ind. Prod. sa (Jun)</a>	<a href="#">AU RBA Governor Macfarlane Speaks: House Economics Committee</a> <a href="#">NZ Visitor Arrivals (Jul)</a> <a href="#">UK CML, BBA &amp; BSA Mortgage Lending Figures</a> <a href="#">US Philadelphia Fed. (Aug)</a> <a href="#">US U. of Michigan Confidence (Aug P)</a> <a href="#">EC Euro-Zone Trade Balance (Jun)</a>

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