

Week Commencing April 16, 2007



AUSTRALIA & NEW ZEALAND WEEKLY

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NZ CPI key for Australia as well as NZ

NZ CPI predicts later Australian number

Wednesday's New Zealand first quarter CPI arguably matters more to Australia than to New Zealand itself. This is because the Reserve Bank of Australia pays more attention to contemporary core inflation as a guide to future inflation than does the Reserve Bank of New Zealand, the New Zealand release precedes the Australian number by six days, and in recent quarters it has predicted the subsequent Australian number.

In the three readings from the second to the fourth quarter of last year the quarterly headline changes in New Zealand were 1.5%, 0.7% and -0.2%, very close to the Australian outcomes of 1.6%, 0.9% and -0.1%. The trimmed mean measure was even closer. This core measure discards the 15% of CPI components which increased most and the bottom 15% which increased least (or fell) and finds the weighted average outcome of the remaining 70% of components. The five readings from the fourth quarter of 2005 to the fourth quarter of 2006 ran 0.5%, 0.8%, 1.0%, 0.5% and 0.4% in New Zealand, compared to 0.5%, 0.8%, 0.9%, 0.7% and 0.5% in Australia. In every case the New Zealand move was in the same direction as the Australian move. In two cases the change was identical, and in the remaining three within one or two tenths of a percentage point.

Though the RBNZ pays little attention to it, Statistics New Zealand publishes a range of trimmed means along with the headline measure. In Australia, by contrast, the RBA pays a good deal of attention to the trimmed mean, but the ABS does not compute it. (This may change, not least because the new head of the ABS, Brian Pink, was up to recently running Statistics New Zealand)

Petrol prices rose in New Zealand in the first quarter, as they did in Australia. Taken from the middle of the fourth quarter last year to the middle of the first quarter this year, the increase was fairly modest and should add only 0.14 percentage points to NZ CPI and around 0.1 percentage points in Australia. We expect the headline measure for New Zealand's Wednesday number to be 0.6%, well above the RBNZ forecast of 0.3%. It would leave the annual headline rate at 2.6%. (The annual rate will plummet in the following quarter, when a 1.5% increase in the June quarter last year drops out). We expect the trimmed mean to be 0.5%.

If the outcomes are as we expect it will increase our confidence that the Australian headline outcome will also be around 0.6% and the Australian trimmed mean will be 0.6%. If it is, the annual trimmed mean rate in Australia will fall to 2.7%. The annualised quarterly rate would be 2.4% - a very satisfactory outcome which would suggest that core inflation has moderated after the upswing in the first half of last year. A

trimmed mean outcome of 0.6% would we think make it tough for the RBA to announce a tightening the following week. A reading of 0.5% would make it very difficult indeed, but anything over 0.6% would rationalise a tightening.

RBA, RBNZ differ on currency

Appreciation more important to Bollard than Stevens

Speaking in 1996, the then deputy governor of the Reserve Bank of Australia Ian Macfarlane observed that Australian monetary policy worked most quickly and effectively through the exchange rate, which over two years had risen from USD0.66 to USD0.79 as the cash rate increased. In interviews around his retirement as governor over a decade later, however, Mr. Macfarlane had changed his thinking. He said the Bank was no longer quite as attentive to the exchange rate. He emphasised that it certainly could not and would not ignore the exchange rate, but that in its recent experience the impact of an appreciation on the consumer price index was reversed in the medium term by the subsequent depreciation. Over the forecast period in which monetary policy actions were supposed to take effect, the exchange rate effect would more often than not wash out. It was also true that while the relationship between exchange rate changes and import prices remained strong, the link between import prices and retail prices had become tenuous. Compared to decade ago, the Bank therefore places less weight on the exchange rate when deciding changes in the cash rate. Over that same decade household debt has trebled compared to household income, so that the monetary policy channel from the cash rate through the variable mortgage rate to household spending has become very much more influential while the exchange rate channel has become less influential.

While the RBA's view of the exchange rate has changed the view of the Reserve Bank of New Zealand has not. Partly because the trade sector is rather larger in New Zealand than Australia, partly because successive econometric studies show that the relationship between exchange rates and consumer prices continues to be important, and partly because New Zealand households have insulated themselves from the short term impact of monetary policy by almost universally switching to fixed rate loans, the RBNZ today places very much more emphasis on the exchange rate than does its counterpart across the Tasman. Indeed, at a RBNZ conference last year an eminent visiting academic economist said the exchange rate was pretty well the only channel through which New Zealand monetary policy worked, and the RBNZ would just have to accept it.

If the RBNZ thinks the inflation impact of its cash rate decisions works significantly through the exchange rate channel, it follows that independent or at least unexpected increases in the exchange rate will substitute for a tightening that might otherwise be prescribed by RBNZ modeling. This is one big reason we doubt RBNZ Governor Alan Bollard will increase the cash rate at the April 26 review. Last week's stupendous and broad based 1.9% increase in New Zealand February retail sales would have rightly alarmed the RBNZ. But the cash rate has already been increased by 25 basis points since February, and

more importantly three year mortgage rates are markedly higher. Trading well above USD0.70, the New Zealand dollar is at stellar levels. Cash might well be tightened further in New Zealand later in the year, but not this month.

Though the Australian dollar is also trading at stellar levels, it will not be as decisive in RBA counsels. Even so, if the April 24 first quarter CPI discloses a quite moderate increase in core inflation and the Australian dollar is still trading over USD0.80, we think it will be quite hard for RBA Governor Glenn Stevens to rationalise a proposed cash rate increase to his board on May 1, or to the public subsequently. The import price impact of an 80 cent dollar over the next few quarters cannot be completely ignored. We doubt last week's March jobs increase will overwhelm these considerations. It's true that the number of full time jobs rose markedly, continuing the trend we have noted whereby part time jobs are being converted to full time jobs. But the overall increase at 10,500 was as we had expected, it was only a fraction of the very big increases we saw in the second half of last year, and it permitted the trend monthly increase to continue declining. While the unemployment rate of 4.5% is very low, the rate has been persistently moving down for over a year. In that year and the preceding year the private sector wage price index has ticked over at an average of 1% a quarter. The increase in wages in the last quarter of last year was the same as it had been six quarters earlier.

John Edwards

Weekly Calendar

Week commencing Monday April 16, 2007

Country/ Region	Event or Economic Release		Period	HSBC	Market F'casts Cons	Actual Previous
Monday April 16, 2007						
JP	Industrial production (05:30 BST)	Month	Feb, final	-0.2%	-	-0.2%
		Year		2.6%	-	2.6%
UK	DCLG house prices (09:30 GMT)	Year	Feb	10.5%	-	10.9%
US	Retail sales (13:30 BST)	Month	Mar	0.8%	0.5%	0.1%
		Ex-autos		0.9%	0.7%	-0.1%
		Ex-autos & gas		0.3%	-	-0.2%
US	Empire manufacturing (13:30 GMT)	Month	Apr	5.0	7.3	1.9
US	Net long-term TIC flows (14:00 GMT)	Net long-term flows	Feb	75.0	81.5	97.4
		Total net flows		65.0	-	74.6
US	Business inventories (15:00 GMT)	Month	Feb	0.3%	0.3%	0.2%
US	NAHB housing market index (18:00 GMT)	Month	Apr	35	35	36
Tuesday April 17, 2007						
UK	CPI (09:30 GMT)	CPI - year	Mar	2.7%	2.8%	2.8%
		RPI - month		0.3%	0.5%	0.7%
		RPI - year		4.5%	4.7%	4.6%
		RPIX		3.6%	3.7%	3.7%
GER	ZEW survey (10:00 BST)	Expectations	Apr	7.0	10.0	5.8
		Current conditions		68.0	69.5	69.2
US	CPI (13:30 GMT)	Headline Month	Mar	0.6%	0.6%	0.4%
		Year		2.8%	2.8%	2.4%
		Core Month	Mar	0.17%	0.2%	0.2%
		Year		2.6%	2.6%	2.7%
US	Housing starts (13.30 BST)	Housing starts (000's)	Mar	1490	1495	1525
		Building permits (000's)		1500	1513	1532
US	Industrial production (14:15 GMT)	Industrial production	Mar	0.0%	0.0%	1.0%
		Capacity utilisation		81.9%	81.9%	82.0%
Wednesday April 18, 2007						
AU	Westpac Consumer Confidence		Apr			
NZ	Consumer prices		Q1	0.6%	0.6%	-0.2%
UK	Bank of England (09:30 GMT)		Apr			
Thursday April 19, 2007						
AU	Consumer Inflation Expectation		Apr			
AU	Preliminary BoP Imports		Mar			
CHI	GDP (03:00 BST)	Year	Q1	11.0%	10.3%	10.4%
CHI	Industrial production (03:00 BST)	Year	Mar	16.9%	15.8%	18.5%
CHI	Fixed asset investment (03:00 BST)	Year	Mar	24.0%	23.8%	23.4%
EMU	ECB monthly bulletin (09:00 GMT)		Apr			
US	Leading indicators (15:00 GMT)	Month	Mar	0.2%	0.1%	-0.5%
US	Philadelphia Fed (17:00 GMT)	Month	Apr	0.0	1.0	0.2

Weekly Calendar (continued)

Week commencing Monday April 16, 2007

Country/ Region	Event or Economic Release	Period	HSBC	Market F'casts Cons	Actual Previous
Friday April 20, 2007					
AU	AU Import price index	Q1		-1.2%	-3.2%
AU	Export price index	Q1		-0.3%	0.2%
NZ	Visitor Arrivals	Mar			
UK	Retail sales (09:30 GMT)	Month	0.2%	0.4%	1.4%
			4.4%	-	4.9%

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 Monday April 23, 2007

Monday April 23, 07	Tuesday April 24, 07	Wednesday April 25, 07	Thursday April 26, 07	Friday April 27, 07
AU Producer Price Index (1Q) AU Producer Price Index (1Q)	AU Consumer Prices (1Q)	UK GDP (1Q P) US Richmond Fed Manufact. Index (APR) US Consumer Confidence (APR) US Existing Home Sales (MAR) US ABC Consumer Confidence (APR 23) US MBA Mortgage Applications (APR 21) US Durable Goods Orders (MAR) JN Merchnds Trade Balance Total (MAR)	AU HIA New Home Sales (MAR) NZ RBNZ Official Cash Rate (APR 26) NZ Trade Balance (MAR) US New Home Sales (MAR) US Fed's Beige Book US Initial Jobless Claims (APR 22) US Continuing Claims (APR 15)	NZ NBNZ Business Confidence (APR) US GDP Annualized (1Q A) US Employment Cost Index (1Q) JN Natl SA CPI (MAR) JN Industrial Production (MAR P) JN Retail Trade (MAR) JN BoJ Monetary Policy Meeting JN BOJ Target Rate (Apr 27)
Monday April 30, 07	Tuesday May 01, 07	Wednesday May 02, 07	Thursday May 03, 07	Friday May 04, 07
AU Private Sector Credit (MAR) NZ Building Permits (Mar) UK BBA Loans for House Purchase (MAR) UK GfK Consumer Confidence Survey (APR) US Personal Income (Mar) US PCE Deflator (MAR) US Chicago Purchasing Manager (APR)	AU AiG Performance of Mfg Index (APR) UK PMI Manufacturing (survey) (APR) US Construction Spending (MAR)	AU DEWR Skilled Vacancies (APR) UK Mortgage Approvals (MAR) US Pending Home Sales (MAR) US ISM Manufacturing (Apr) US Bernanke Speaks at Montana Economic Development Summit US ABC Consumer Confidence (APR 30) US MBA Mortgage Applications (APR 28)	AU AiG Performance of Service Ind (APR) US Factory Orders (MAR) US Initial Jobless Claims (APR 29) US Nonfarm Productivity (1Q P) US Unit Labor Costs (1Q P) US Continuing Claims (APR 22)	AU Trade Balance (MAR) AU Reserve Bank Quarterly Monetary Policy Statement AU Exports (MAR) AU Imports (MAR) US ISM Non-Manufacturing (APR) US Change in Nonfarm Payrolls (APR)
Monday May 07, 07	Tuesday May 08, 07	Wednesday May 09, 07	Thursday May 10, 07	Friday May 11, 07
AU AiG Perf of Construction Index (APR) AU ANZ Job Advertisements (APR) NZ Labor Cost Private Sector (1Q) JN BoJ Monetary Policy Meeting Minutes for March	AU Retail Sales (MAR) AU Building Approvals (Mar) AU Federal Government Budget US Consumer Credit (MAR)	AU House Price Index (1Q) AU House Price Index (1Q) UK Bank of England's Monetary Policy Committee Meets US MBA Mortgage Applications (MAY 5) US Fed's Open Market Committee Meets on Interest Rates, Economy	AU Employment Change (APR) NZ Unemployment Rate (1Q) UK Industrial Production (MAR) UK BOE Announces Rates (MAY 11) US FOMC Rate Decision Expected (MAY 10) US Trade Balance (MAR) US Initial Jobless Claims (MAY 6) US Import Price Index (APR) US Continuing Claims (APR 29) EC ECB Announces Interest Rates (MAY 11)	AU Home Loans (MAR) AU Investment Lending (MAR) NZ ANZ-Business NZ PMI (APR) US Producer Price Index (APR) US Retail Sales Less Autos (APR)

Monthly Economic Calendar (continued)

Week commencing Monday April 23, 2007

Monday May 14, 07	Tuesday May 15, 07	Wednesday May 16, 07	Thursday May 17, 07	Friday May 18, 07
NZ Retail Sales (MAR) UK DCLG UK House Prices (MAR) JN Current Account Total (MAR) EC Euro-Zone Ind. Prod. (MAR)	UK RICS House Price Balance (APR) UK CPI (APR) US Consumer Price Index NSA (APR) US Bernanke Speaks at Atlanta Fed Financial Markets Conference US Empire Manufacturing (MAY) US Net Long-term TIC Flows (MAR) JN Machine Orders (MAR) EC Euro-Zone GDP (1Q A)	AU Westpac Consumer Confidence (MAY) AU Imports (APR) AU Wage Price Index (1Q) UK Bank of England Quarterly Inflation Report US NAHB Housing Market Index (MAY) US ABC Consumer Confidence (MAY 14) US Fed's Geithner Speaks at Atlanta Fed Conference on Derivatives US MBA Mortgage Applications (MAY 12) US Housing Starts (APR) US Building Permits (APR) US Industrial Production (APR) JN BoJ Monetary Policy Meeting JN Industrial Production (MAR F) JN Consumer Confidence (APR) EC Euro-Zone CPI (APR)	US Initial Jobless Claims (MAY 13) US Continuing Claims (MAY 6) US Bernanke Speaks at Chicago Fed Banking Conference JN BoJ Target Rate (MAY 17) JN BOJ Monthly Report	UK Retail Sales (APR) US Philadelphia Fed. (MAY)

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