

Data Review

5 April 2006

RBA still on hold: consumers under the spotlightMarket
Economics

- **RBA leaves rates on hold again**
- **No trigger yet for RBA action but tightening bias remains**
- **Retailing bounce a surprise but might have legs**
- **Upcoming inflation, wages, house prices key litmus tests**
- **AiG Services index pokes its head back above 50**

It was no surprise at 9.30 this morning that the RBA announced that it left the cash rate unchanged at 5.50%, where it has been since March 2005.

This month's Reuters interest rate poll published last Friday shows that the majority of analysts continue to expect that rates will remain on hold this year. Of the 17 surveyed analysts, 11 see rates as remaining on hold this year, five are expecting a rise, while one is expecting a decline. That is very similar sentiment to the probability of a change in the cash rate priced into local interest rate futures. The local market for example, while priced for almost no change in the cash rate for the next three months has been pricing toward a rise within the next 12 months. Just before the March RBA Board meeting, the market was priced for steady to lower rates for the next twelve months, with the curve pricing for a very small chance of a rate cut.

The tone of the data over the past month or so has pointed to the economy regathering some momentum in the March quarter. Employment has stabilised, retail trade has been clearly better than expected pointing to some upside risk to our Q1 consumption forecast of 0.7% and possibly to our Q1 GDP forecast of 0.6%, depending on how the net exports contribution to growth is buffeted by the cyclones in the North West. Add in steady to rising house prices and the consumer outlook is somewhat brighter. And even on the export front, while the net exports contribution to growth may be stifled in the short term, non-rural exports in December and February were noticeably higher suggesting that resource sector output might be rising at last.

We also note comments from the Treasurer yesterday that the economy has gained some momentum in the first quarter compared to the second half of last year. "It looks to me as if the domestic economy has got a little more momentum than it had in the second half of last year". You'd expect that such sentiments to have been expressed by Treasury Secretary Henry at the RBA Board meeting yesterday.

At the least, the run of better data of late will give the RBA confidence that its forecast of 3¼% for this year is within reach. If the consumer is stepping up to the plate again then that is a solid underpinning to growth overall. We are yet to see that this retailing improvement will have continued legs in the months ahead in the face of higher petrol prices and even talk of higher rates. Industry reports suggest that retailing has improved, if still patchy in parts. It's conceivable that the uplift in retailing has come from discounting after last year's first half.

The RBA does not as yet have any real trigger to move the cash rate with well-behaved underlying inflation and wages not yet beyond the tolerance of the RBA. Tomorrow's employment data takes on more importance for local interest rate markets in the short term but the upcoming Q1 CPI data at the end of this month (due 26 April), Q1 wage costs (May 17) and Q1 ABS house prices (May 25) are all important, and likely more decisive, signposts.

While we continue to expect that rates will remain on hold – for example from our expectation that the underlying inflation rate will remain contained – we will continue to watch such developments closely. We would currently rate the probability of a rise within three to six months as around a 25% chance. Bank bill futures are pricing around a 60% chance of a hike in the same time frame.

AiG PSI

The AiG Performance of Services Index (PSI) poked its head back above 50 at 51.0 in March. In the past four months, the index has averaged 52.1. Interestingly, while sales and new orders remained below 50, one component that did rise was the employment index from 49.6 to 55.5.

David.de.Garis@nab.com.au

Main Offices

Sydney

Level 26, 255 George Street, SYDNEY NSW 2000
T +(61 2) 9295 1166 F +(61 2) 9237 1559

Melbourne

Level 32, 500 Bourke Street, MELBOURNE VIC 3000
T +(61 3) 9277 3321 F +(61 3) 9641 4194

Wellington

BNZ, 1 Willis Street/P.O. Box 2392, WELLINGTON NZ
T +(64 4) 473 3791 F +(64 4) 474 6266

London

88 Wood Street, London EC2V 7QQ
T +(44 20) 7710 2100 F +(44 08) 70 2 06302

New York

National Australia Capital Markets LLC
Level 28, 245 Park Avenue, New York, NY 10167
Toll free 877-377-5480 T +(1 212) 916 9677

Hong Kong

1 Pacific Place, 88 Queensway, Hong Kong
T +(85 2) 2822 9801

Singapore

5 Temasek Boulevard #15-01
Suntec City Tower, Singapore 0103 88
T +(65) 6332 2993 F +(65) 6338 2918

Tokyo

National Australia Capital Markets (Japan) Co.
Mitsui Nigokan, 2-1-1 Nihonbashi-Muromachi
Chuo-ku 103-0022
T +(81 3) 3270 5691 F +(81 3) 3241 7930

Research Contacts

Peter Jolly	Head of Research	+(61 2)	9295 1199
Alan Oster	Group Chief Economist	+(61 3)	8641 3464
Market Strategy			
John Kyriakopoulos	Currency Strategist	+(61 2)	9237 1903
Credit Research			
Michael Bush	Head of FI Credit Research	+(61 3)	8641 0575
Ken Hanton	Senior Analyst	+(61 2)	9237 1405
Economics			
Rob Henderson	Chief Economist, Markets	+(61 2)	9237 1836
Jeff Oughton	Head of Economics – Australia	+(61 3)	8641 3469
Tom Taylor	Head of Economics – International	+(61 3)	8641 3475
Spiros Papadopoulos	Senior Economist, Markets	+(61 3)	8641 0978
David de Garis	Senior Economist, Markets	+(61 2)	9237 1180
Stephen Toplis (NZ)	Head of BNZ Market Economics	+(64 4)	474 6905
Craig Ebert (NZ)	Senior Markets Economist	+(64 4)	474 6799
Dean Ford (NZ)	Market Economist	+(64 4)	474 6923
Tom Vosa (UK)	Market Economist	+(44 20)	7710 1573
Kris Bernie (UK)	Dollar Bloc	+(44 20)	7710 2910

Important Notices

ANALYST CERTIFICATION: The person or persons named as the author(s) of this report hereby certify that the views expressed in the research report accurately reflect their personal views about the subject securities and issuers and other subject matters discussed. No part of their compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in the research report. Research analysts responsible for this report receive compensation based upon, among other factors, the overall profitability of the Markets Division which is part of the Institutional Markets & Services division of National Australia Bank Limited, a member of the National Australia Bank Group (the "National"). The views of the author(s) do not necessarily reflect the views of the National and are subject to change without notice. The National may receive fees for banking services provided to an issuer of securities mentioned in this report. The National, its affiliates and their respective officers, and employees, including persons involved in the preparation or issuance of this report (subject to the policies of the National), may also from time to time maintain a long or short position in, or purchase or sell a position in, hold or act as advisors, brokers or commercial bankers in relation to the securities (or related securities and financial instruments), of companies mentioned in this report. The National or its affiliates may engage in these transactions in a manner that is inconsistent with or contrary to any recommendations made in this report.

AUSTRALIAN DISCLAIMER: So far as the law allows, National Australia Bank Limited ABN 12 004 044 937 ("the National") disclaims any warranty or representations as to the accuracy or reliability of the information and statements in this document. The National expressly advises that, to the extent permitted by the law of Victoria, Australia, by which law use and all other matters relating to this document are governed, it shall not be liable in any way whatsoever (whether in negligence or otherwise) for any loss or damage which may be suffered by any person relying upon such information or any opinion, recommendations or conclusions contained in this document or otherwise arising in connection with the contents of or any omission from this document where the liability is made non-excludable by legislation. This document has been prepared for dissemination to professional investors. The opinions expressed herein are those of the author and not necessarily those of the National. The information on which those opinions are based has been gleaned from public sources or provided by the subject on a non-confidential basis. This document does not purport to contain all relevant information and any statement as to any future matter is a present prediction of a possible future outcome, the accuracy of which cannot be guaranteed. Past performance is not a guide to future performance. Recipients should not rely upon the contents of this document, but should make their own assessment and evaluation, undertake an investigation and enquire and seek advice to enable them to make any decision concerning their own risk. This material is not intended as an offer or solicitation for the purchase or sale of any financial instrument. The National, its affiliates, and employees may hold a position or act as price maker in the financial instruments of any issuer discussed within this document or act as underwriter, placement agent, adviser or lender to such issuer. © Copyright National Australia Bank Limited ABN 12 004 044 937.

UK DISCLAIMER: So far as the law and the Financial Services Authority Rules allow, National Australia Bank Ltd ("the Bank") disclaims any warranty or representation as to the accuracy or reliability of the information and statements in this Document. The Bank will not be liable (whether in negligence or otherwise) for any loss or damage suffered from relying on this Document. This Document does not purport to contain all relevant information. Recipients should not rely on its contents but should make their own assessment and seek professional advice relevant to their circumstances. The Bank may have proprietary positions in the products described in this Document. This Document is for information purposes only, is not intended as an offer or solicitation, nor is it the intention of the Bank to create legal relations on the basis of the information contained in it. No part of this Document may be reproduced without the prior permission of the Bank. This Document is intended for Investment Professionals (as such term is defined in The Financial Services and Markets Act 2000 (Financial Promotion) Order 2001) and should not be passed to any other person who would be defined as a private customer by the rules of the Financial Services Authority ("FSA") in the UK, or to any person who may not have experience of such matters. Issued by National Australia Bank Limited A.B.N. 12 004 044 937, 88 Wood Street, London EC2V 7QQ. Registered in England BR1924. Head Office: 500 Bourke Street, Melbourne, Victoria. Incorporated with limited liability in the State of Victoria, Australia. Authorised and regulated by the Financial Services Authority in the UK



US DISCLAIMER: This information has been prepared by National Australia Bank or one of its affiliates or subsidiaries (collectively, "NAB"). If it is distributed in the United States, such distribution is by National Australia Capital Markets, LLC (NACM) which accepts responsibility for its contents. Any U.S. person receiving this information wishes further information or desires to effect transactions in the securities described herein should call or write to NACM, 200 Park Avenue, New York, NY 10166 (or call (877) 377-5480). The information contained herein has been obtained from, and any opinions herein are based upon sources believed to be reliable and no guarantees, representations or warranties are made as to its accuracy, completeness or suitability for any purpose. Any opinions or estimates expressed in this information is our current opinion as of the date of this report and is subject to change without notice. The principals of NACM or NAB and/or its affiliates may have a long or short position or may transact in the securities referred to herein or hold or transact derivative instruments, including options, warrants or rights with securities, or may act as a market maker in the securities discussed herein and may sell such securities to or buy from customers on a principal basis. This material is not intended as an offer or solicitation for the purchase or sale of the securities described herein or for any other action. It is intended for the information of clients only and is not for publication in the press or elsewhere.