

Ai GROUP ECONOMICS WEEKLY

Week in Review: 27 April – 29 April 2011

- The **National Australia Bank Quarterly Business Survey** revealed that business conditions remained soft in the March quarter 2011, although business confidence improved strongly. The overall business conditions index (a composite index of trading performance, profitability and employment) remained steady at a +2 points index level. Despite an increase in the business confidence index of 6 points (to a +11 points index level), forward orders, which give a indication of future demand for goods and services, were again weak at a minus 2 points level and stocks edged down. Orders were particularly subdued in the construction, manufacturing, wholesale and recreation & personal services sectors. The survey also found that profit margins fell sharply in the March quarter, although short term expectations for margins were more optimistic.
- The **Consumer Price Index (CPI)** released by the ABS showed that annual headline inflation was 3.3% in the March quarter 2011, up from 2.7% in the year to the December quarter 2010. This exceeded the market expectation of a 3.0% rise. The quarterly rate of growth was 1.6% compared with a 0.4% increase in the December quarter. The increase in headline inflation was driven by one-off factors related to the impact of natural disasters, seasonal influences and higher petrol prices. The underlying measures of inflation, the trimmed mean and weighted median, remove volatile price items. The average of these two measures showed an increase in the quarter of 0.9% and 2.3% on a year ago, to remain in the lower half of the Reserve Bank's target annual inflation band of 2-3%. By category, food prices rose strongly by 2.9% in the March quarter due to production and supply disruptions that resulted from the impact of the recent floods and Cyclone Yasi. There were also large upward movements in the education (+5.7%) and health (+3.9%) categories, while automotive fuel increased by 5.7% reflecting tensions in the Middle East and in North Africa which have driven up world oil prices.
- Reserve Bank of Australia **Financial Aggregates** data showed that total credit provided to the private sector by financial intermediaries rose by 0.6% in March 2011. This was slightly below the market forecast of a 0.4% increase. The rise in total credit in March was underpinned by a 1.0% increase in business credit, the largest monthly increase since October 2008 and an early sign that businesses are starting to increase their borrowings to fund a lift in investment spending. However, other personal credit which includes credit cards continued to exhibit sluggish growth, rising by 0.6% in the month while housing credit growth at 0.4% was also subdued reflecting higher interest rates and weaker investor activity.

How this affects you

The data over the past week indicated that despite the influence of one-off factors that drove the spike in headline inflation during the first quarter of the year, price pressures in the Australian economy appear to be rising with growth becoming broader based and stronger across a range of expenditure categories. While underlying inflation has remained in the lower half of the Reserve Bank's 2-3% target range, recent trends suggest that a cyclical low point has been passed with the March quarter rise of 0.9% exceeding the more subdued increases of between 0.4% and 0.6% recorded during the three quarters to December 2010. Moreover, cost-push risks to inflation remain, particularly given the intensification of skill shortages and the continued increase in private investment in the resources sector which is set to draw strongly on labour, equipment and materials. Although the latest inflation data does provide the RBA with time to assess developments before making any further move on interest rates, the likelihood of a further step-up in the underlying rate in coming quarters, has led financial markets to factor in a greater chance of a rate rise from the Reserve Bank by the end of October.

Latest data*

Official cash rate	4.75 per cent -
AUD/USD exchange rate	\$1.0965 ▲
Oil price	USD 113.27 per bbl ▲
Annual growth in GDP	2.7 per cent -
Unemployment rate (%)	4.9 per cent -
Annual growth in headline CPI	2.8 per cent -
Copper price	AUD 8545.83 ▼
Australian PMI (March)	47.9 -
Australian PSI (March)	46.5 -
Australian PCI (March)	39.4 -

Week in Preview: 2nd May – 6th May 2011

- On Monday, Ai Group will release its Australian Performance of Manufacturing Index (**Australian PMI**[®]) for the month of April, while the Australian Performance of Services Index (**Australian PSI**[®]) and the Australian Performance of Construction Index (**Australian PCI**[®]) will be released on Wednesday and Friday respectively.
- The Reserve Bank of Australia (RBA) Board meeting and **monetary policy decision**, 2.30pm on Tuesday.
- On Thursday, the ABS will release data on **Building Approvals** for March 2011.
- Thursday will also see the release of ABS **Retail Trade** data for March.
- The Reserve Bank of Australia's latest **Quarterly Monetary Policy Statement** will be published on Friday.

* Arrows represent directional movement relative to previous week's issue. For further assistance from Ai Group's Economics & Research Unit or for any suggestions for economic information you would like to be included in the report, please email economics@aigroup.asn.au.