



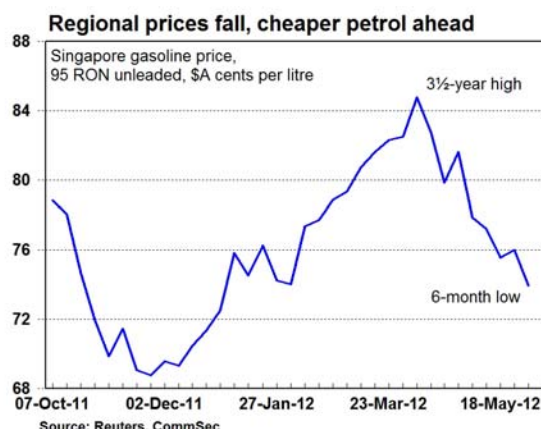
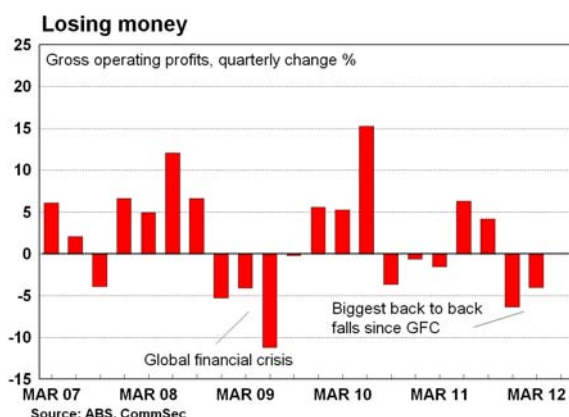
# Convincing case to cut rates again

## Latest economic indicators; Petrol prices

- **Inflation at 2½ -year low:** The TD Securities-Melbourne Institute monthly inflation gauge was unchanged in May and stood just 1.8 per cent higher than a year ago – equalling the 2½ year low set in March.
- **Bad news for job seekers:** The number of job advertisements fell for the second straight month, dropping by 2.4 per cent in May to stand 4.3 per cent lower for the year.
- **Profits slump:** Company profits slumped by 4.0 per cent in the March quarter to stand 0.5 per cent lower than a year ago.
- **Tourist arrivals and departures ease:** The number of tourists arriving in Australia in April eased by 0.5 per cent from record highs. And the number of Australians travelling overseas for holidays or business fell by 0.3 per cent in the month. A record 580,400 Chinese tourists came to Australia over the past year.
- **Fuel prices fall:** According to the Australian Institute of Petroleum, the national average Australian price of unleaded petrol fell by 1.7 cents per litre to 145.1 cents a litre in the week to June 3. Melbourne has the lowest capital city petrol price. In Australian dollar terms the Singapore gasoline price stands at 6-month lows.

### What does it all mean?

- Not a lot of good news in the economy at present. The latest data showed profits, job ads and tourist arrivals all fell. The main piece of good news is that consumer prices were flat in the latest month and annual inflation is at 2½ year lows. And petrol prices continue to decline with more falls on the way.
- With inflation under control and the economy effectively trading water, the Reserve Bank is well placed to cut interest rates again. We expect a rate cut tomorrow of at least 25 basis points or a quarter of a per cent. At the same time that rates are falling, the Aussie dollar is also softening, delivering a healthy dose of stimulus to the economy.
- The wholesale price of petrol in Australia has fallen 8.8 cents a litre from the highs in mid April. But so far the retail price has come down by 7.1 cents a litre. CommSec expects pump prices to keep dropping. The national retail petrol price should ease another 2 cents over the next 7-10 days and given that Asian regional gasoline prices are



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still falling, there is further good news ahead for motorists. In some capital cities, petrol signboards could show 128 cents a litre by late this week. A petrol price war is adding to the good news for Melbourne motorists.

- You have to scratch your head at the Bureau of Statistics profits series. Apparently retailers are doing OK and mining profits are slumping. It certainly doesn't line up with other data or anecdotal reports.

## What do the figures show?

### Business indicators

- Company gross operating profits** fell by 4.0 per cent in the March quarter after sliding by 6.4 per cent in the December quarter. Profits have risen in just two of the past seven quarters and are down 0.5 per cent on a year ago.
- Profits** fell in 7 of the 15 industry sectors in the March quarter, led by Professional, scientific and technical services (down 13.7 per cent) and mining (down 13.3 per cent). In key sectors, manufacturing profits fell by 9.8 per cent with construction down 2.3 per cent but retail profits surprisingly rose by 3.3 per cent.
- Sales** rose in 10 of the 15 industry groupings in real (inflation-adjusted) terms in the March quarter. Of the major sectors, sales rose by 0.5 per cent in Retail trade, rose 1.2 per cent in Wholesale trade, rose 2.2 per cent in Mining, and rose 0.1 per cent in both Manufacturing and Construction. **Total real sales** rose by 0.9 per cent in the March quarter to stand 2.8 per cent higher over the year. Excluding mining, sales rose by 0.8 per cent in the quarter to be up 2.4 per cent for the year.
- Inventories rose by 0.9 per cent** in the March quarter, led by a 6.0 per cent lift in Mining. Inventories fell in just Retail trade (down 0.5 per cent) and Accommodation & food services (down 10.5 per cent).

### Job advertisements:

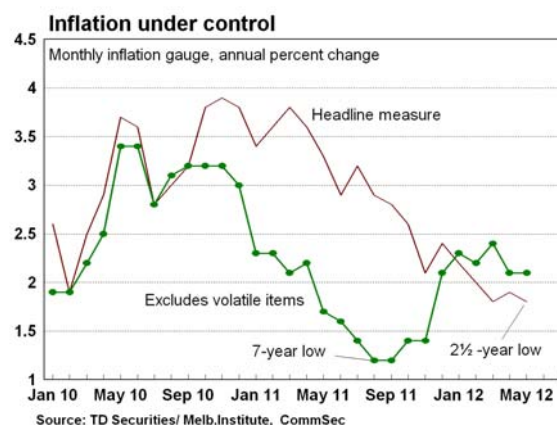
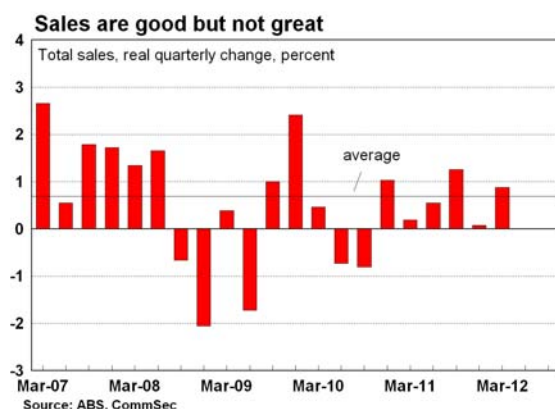
- The combined number of internet and newspaper job advertisements, as tracked by ANZ, fell for the second straight month, dropping by 2.4 per cent in May after a 3.1 per cent decline in April. Job ads are down 4.3 per cent on a year ago.
- Newspaper job ads fell by 2.0 per cent in May while the far larger component of internet job ads fell by 2.4 per cent.
- ANZ provides data on newspaper job ads by state but given their minor importance in relation to internet ads and poor record in tracking total advertisements, the data is not useful for analytical purposes.

### Inflation gauge:

- The monthly inflation gauge was flat in May following a 0.3 per cent rise in April. The annual rate of inflation fell from 1.9 per cent to a 2½ year low of 1.8 per cent.
- The underlying rate (trimmed mean) was also unchanged in May following a 0.4 per cent rise in April. The annual rate fell from 2.3 per cent to 1.9 per cent.
- Excluding volatile items like petrol and fruit & vegetables, the inflation gauge rose just 0.1 per cent in May after a 0.2 per cent rise in April. The annual rate was unchanged at 2.1 per cent.
- TD Securities noted that *"Contributing to the overall change in May were price rises for fruit and vegetables, alcoholic beverages, and furniture and furnishings. These were offset by falls in automotive fuel, holiday travel and accommodation, and bread and cereal products. The price of automotive fuel fell by 2.8 per cent in May, almost reversing the 3.1 per cent rise in April."*

### Overseas arrivals/departures

- The number of people coming to Australia for holidays or business** fell for the first time in three months, easing by 0.5 per cent in April from record highs. Arrivals are up 3.1 per cent on a year ago.



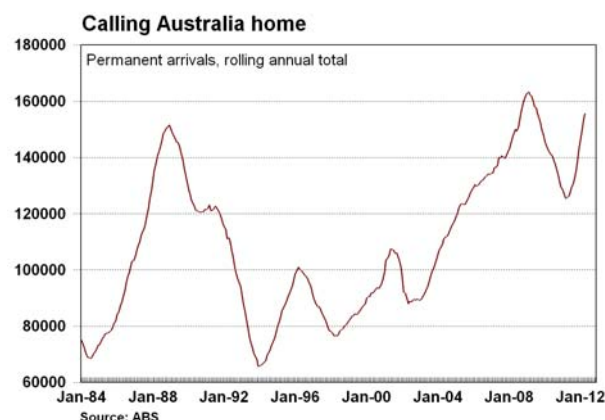
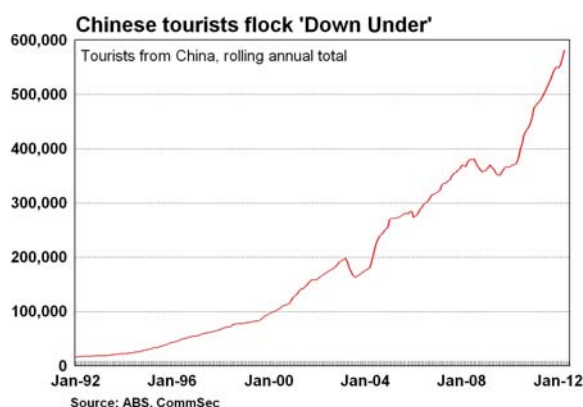
- **The number of Aussies travelling overseas for holidays or business** fell for only the second time in five months, easing by 0.3 per cent in April. Tourist departures were down 1.9 per cent on a year ago in seasonally adjusted terms (up 5.6 per cent in trend terms).
- In seasonally adjusted terms the **tourism deficit** – the gap between departures and arrivals rose from 165,000 in March to 165,800 in April. In trend terms the tourism deficit stood at a 9-month high of 165,300.
- **The rolling annual number of net permanent and long-term arrivals** to Australia has risen for the 13th straight month. In the year to April net long-term arrivals stood at a 26-month high of 274,060. The record high was net-long term arrivals of 341,280 in the year to July 2009.
- **The actual number of permanent settlers** entering Australia eased from a 43-month high of 14,670 in March to 13,330 in April. Over the past year 155,530 people came to Australia as permanent settlers – a 32-month high.

#### Petrol prices:

- According to the Australian Institute of Petroleum, the national average Australian price of unleaded petrol fell by 1.7 cents a litre to 145.1 cents a litre in the week to June 3. The metropolitan price fell by 1.9 c/l to 142.5 c/l, while the regional average price fell by 1.1 cents per litre to 150.5 c/l. The national weekly average weekly retail diesel price was down by 0.5 cents a litre to 152.2 cents a litre.
- Average petrol prices across states over the past week were: Sydney (down 0.3 cents to 142.3 c/l), Melbourne (down 5.3 cents to 136.6 c/l), Brisbane (down 1.1 cents to 146.3 c/l), Adelaide (up 0.4 cents 143.4 c/l), Perth (down 0.8 cents to 144.8 c/l), Darwin (down 0.1 cents to 157.8 c/l), Canberra (down 1.0 cents to 154.8 c/l) and Hobart (down 0.5 cents to 151.8 c/l).
- The weekly average of the national wholesale (terminal gate) unleaded petrol price fell from 137.0 cents per litre to a 3½ month low of 136.1 cents per litre last week. CommSec expects the national average retail petrol price (pump price) to fall by around 2 cents a litre in the next 7-10 days.
- Last week the key Singapore unleaded petrol price fell by US\$3.72 (3.2 per cent) to US\$114.05 a barrel. It was the lowest price since December 20 last year. In Australian dollar terms the Singapore gasoline price fell by \$3.29 (2.7 per cent) last week to a 6-month low of \$117.58 a barrel.

#### **What is the importance of the economic data?**

- The quarterly **Business Indicators** publication by the Bureau of Statistics contains measures such as inventories, company profits and income from sales. Higher inventory (stock) levels can be either intentional or unintentional. If stocks are low and sales are expected to rise in the future, businesses will seek to build up stocks. However an unintentional build-up in stocks is where sales fall short of expectations, leaving more goods on the shelves than desired. If profits are increasing then this may point to increased capital spending and employment in the future. Rising profits are also a sign of favourable business conditions.
- The monthly **Job Advertisements** release is a leading employment indicator. Employers only seek additional staff if business activity is strong, and more importantly, if they expect that conditions will remain favourable in coming months. It takes around 5-6 months for the new staff to be added to the payrolls. But a fall in job advertisements would have a more immediate impact on monthly employment estimates.
- The **TD Securities/Melbourne Institute Monthly Inflation Gauge** is designed to “provide a timely and accurate monthly measure of inflation in Australia”. The Bureau of Statistics only releases the Consumer Price Index on a quarterly basis.
- **Weekly figures on petrol prices** are compiled by ORIMA Research on behalf of the Australian Institute of Petroleum (AIP). National average retail prices are calculated as the weighted average of each State/Territory's metropolitan and non-metropolitan retail petrol prices, with the weights based on the number of registered petrol vehicles in each of these regions. AIP data for retail petrol prices is based on available market data supplied by



MotorMouth.

### What are the implications for interest rates and investors?

- The Reserve Bank has a rock solid case to cut interest rates. The latest data shows that the economy is barely growing while inflation is solidly under control. The only question now is whether the Reserve Bank cuts by 25 or 50 basis points.
- The job market is interesting. There are plenty of anecdotes that businesses can't get the staff they want and are bringing in migrants. At the same time there are high-profile job losses in manufacturing, construction and retailing. Unemployment could edge slightly higher in coming months, but we don't see it as a major concern at present.
- The lift in migration is clearly good news for retail and housing sectors. If more people are coming to our shores, they will need somewhere to stay, and the income they have from day one in Australia represents latent spending power.

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