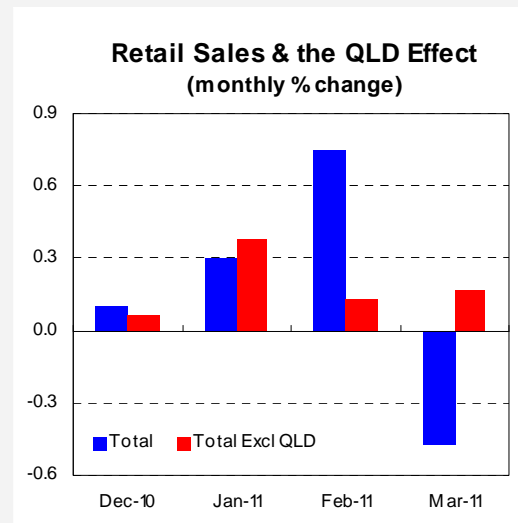
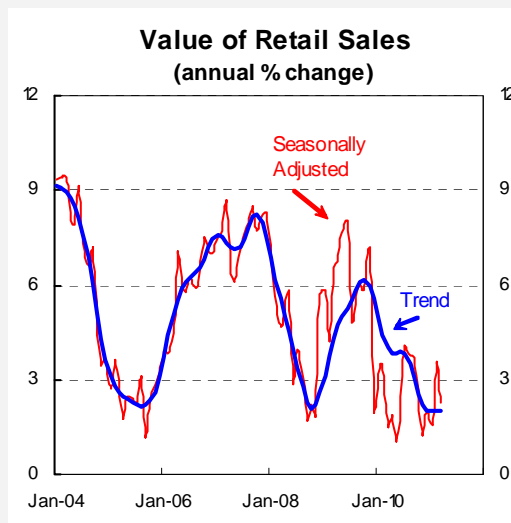


DATA SNAPSHOT

Retail Trade: Consumers Wrapped Up in Cotton Wool

5 May 2011

- Today's data makes it clear that consumers are continuing to wrap themselves up in cotton wool. Consumers are saving more and spending less and this is being reflecting in soft retailing trends.
- The value of retail sales unexpectedly fell 0.5% in March, raising worries that the caution among consumers is deepening. The impact of the natural disasters is still washing through the data and a late Easter also likely played havoc with the seasonal adjustment process. But even in trend terms (which smooths the data), retail spending growth was soft, albeit steady, growing 0.1% in March and by 2% in the year to March.
- Retail sales volumes were flat in the March quarter, suggesting downside risk to the March quarter GDP numbers when they are released in early June.
- The consumer is the swing variable for the domestic economic outlook this year. The Reserve Bank has previously welcomed the caution exhibited by consumers because it has helped the RBA do its job in fighting inflation. However, if consumers dig a deeper burrow in coming months, the growth outlook for the Australian domestic economy will be tempered. It then brings the risk that the RBA will have less tightening to do.



Retail Sales – Value:

Retail sales unexpectedly fell in March, raising worries that the caution among consumers is deepening. Retail sales dropped 0.5% compared with consensus expectations for a rise of 0.5%. We were on the low side of market estimates forecasting 0.2% growth.

There are some factors complicating analysis of the data. Firstly, the impact of the floods is still washing through the data. The Bureau of Statistics noted that the seasonal adjustment of several Queensland series and the total series now includes a large extreme correction for February. The outcome for February was accordingly revised higher from 0.5% growth previously reported to 0.8% growth. January's outcome was revised slightly lower. Looking at the Queensland effect, retailing in the State dropped 2.9%, the weakest decline since July, but it follows a 3.2% rise in February.

The retailing picture excluding QLD is still, however, a weak one. To illustrate this point, if we exclude QLD, total retail sales rose by 0.2% in March and by 0.7% in the March quarter. Including QLD, retail sales in the three months to March were up 0.6%. So the difference QLD makes over the three months to March is only marginal.

The second complicating factor relates to the late Easter this year, which the seasonal adjustment factors may not be appropriately capturing. That means there is some risk of a correction in retail spending in April.

Looking through these complicating factors, it is still clear that consumers are continuing to wrap themselves up in cotton wool. In trend terms (which smooths the data), retail spending grew by 0.1% in March for the third consecutive month and annual growth remained steady and soft at 2.0%. Consumers are saving more and spending less and this is being reflecting in the soft retailing trends. The household savings ratio is rising and is now at levels not seen since the late 1980s.

Consumer sentiment is healthy, household incomes are growing strongly and unemployment is at a low level. However, these influences are being partially offset by higher petrol prices and higher mortgage repayments (from the rate rises last year).

The weakness in retailing in March was broad based; five of the six sectors reported declines. The biggest decline in the month was recorded in department store sales, which fell 3%, the biggest fall in more than a year. Clothing, footwear & personal accessory retailing was the only sector to record growth in March, but this growth was very modest at 0.1%.

Across the States and territories, the biggest fall was posted in QLD of 2.3%. It is the biggest fall since July 2000 but follows a steep rise of 3.2% in the previous month. With the exception of WA and VIC, all other States and territories recorded falls.

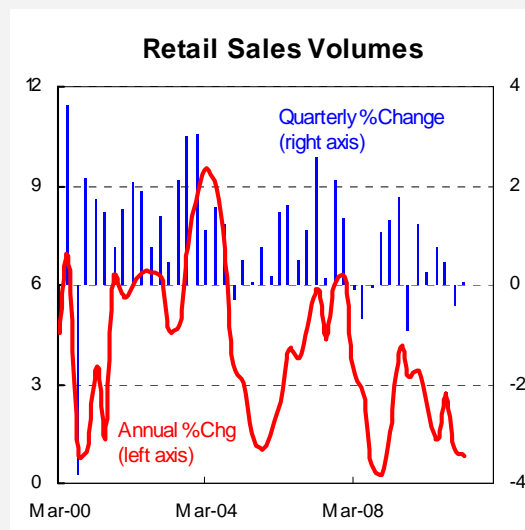
Retailing Sectors	Monthly % Change	Annual % Change
Food	-0.4	3.7
Household Goods	-0.3	1.7
Clothing, footwear & personal accessories	+0.1	0.6
Department store sales	-3.0	-4.3
Other retailing	-0.1	3.9
Cafes, restaurants & takeaway food services	-0.1	2.1

Retail Sales – Volumes:

Retail sales volumes were flat in the March quarter and 2.3% growth on a year ago. Retailing volumes on a year ago grew by only 0.8%, which is the softest pace in more than two years.

The picture among the sectors in terms of retailing volumes was more mixed. Food and other retailing posted the firmest quarterly growth rates of 0.6% and 1.5%, respectively. Meanwhile, household goods and cafes, restaurants & takeaway food services fell 1.3% and 0.6%, respectively.

In the March quarter, retail sales volumes in Queensland were strong, rising by 0.7%, reflecting the impact of stockpiling from the natural disasters. WA was also strong while NSW and VIC retailing volumes were weak.



Weak retail sales volumes for the March quarter suggest that there is downside risk to the GDP numbers for the March quarter (via the household consumption variable). We've long been forecasting a contraction for GDP in the March quarter, driven by the near-term negative impact on economic activity from the floods. Today's retailing data suggests the contraction may be bigger than previously thought.

Interest Rate Outlook:

The consumer is the swing variable for the domestic outlook this year. Private investment spending is the growth engine of the Aussie economy but a soft patch is retail spending. The Reserve Bank has previously welcomed the caution exhibited by consumers because it has helped it do its job in fighting inflation. However, if consumers dig a deeper burrow in coming months, the outlook for the Australian domestic economy will be tempered. It brings the risk that the RBA will have less tightening to do this year.

Tightening in the second half of this year remains on the cards, but the debate about the timing and how much tightening will heat up after today's retail data.

Longer Term Issues:

A trend underway which will affect retailing over a longer time frame is the lift in online spending. Today's data does not include online spending but the high level of the Australian dollar is likely to have encouraged greater online spending among consumers.

Currently, online spending is a growing but small proportion of overall retailing. Looking into the future, the need for multiple shopfronts for a chain is likely to become redundant.

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