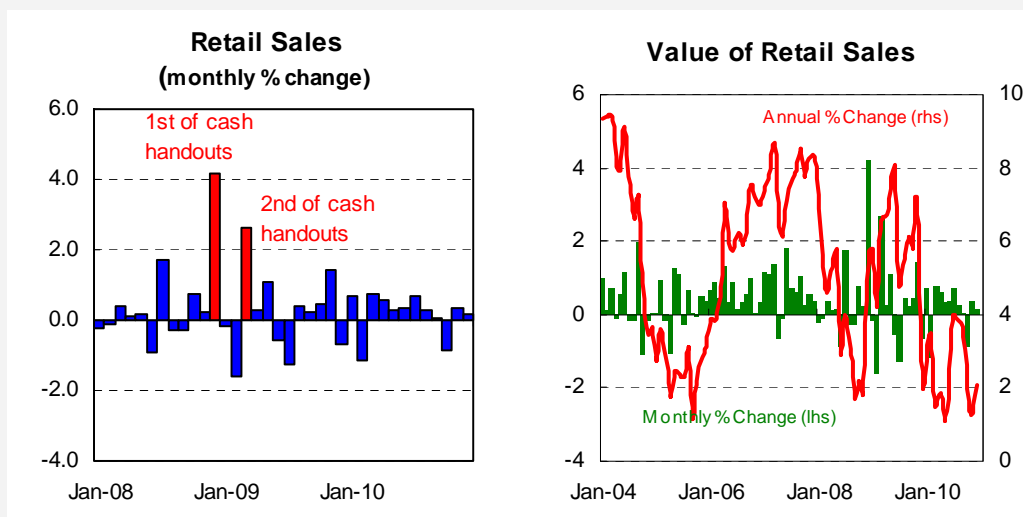


DATA SNAPSHOT

Caution Shackles the Consumer

Monday, 7 February 2011

- Consumers continue to be shackled by caution. Nominal retail sales were weaker than expected in December, rising by just 0.2%. While incomes are growing strongly and the labour market is tight, consumers are still cautious. Rate rises over last year are likely to have affected consumer-spending habits. Further, the hangover from the global financial crisis appears to have dented consumers' appetites.
- Retail sales volumes declined 0.3% in the December quarter, following four consecutive quarters of expansion. The data shows there have been marked discounting across household goods, clothing and department stores. Retailers have been able to cut prices as the Aussie dollar continues to appreciate.
- In a separate release, job advertisements continued to climb, despite the floods. Job ads rose by 2.4% in January to a 2-year high. It was the 12th consecutive monthly increase in job ads, which are now 40.5% higher than January 2010. It suggests we could see the unemployment rate decline further later this year.



Retail Sales – Value or Nominal

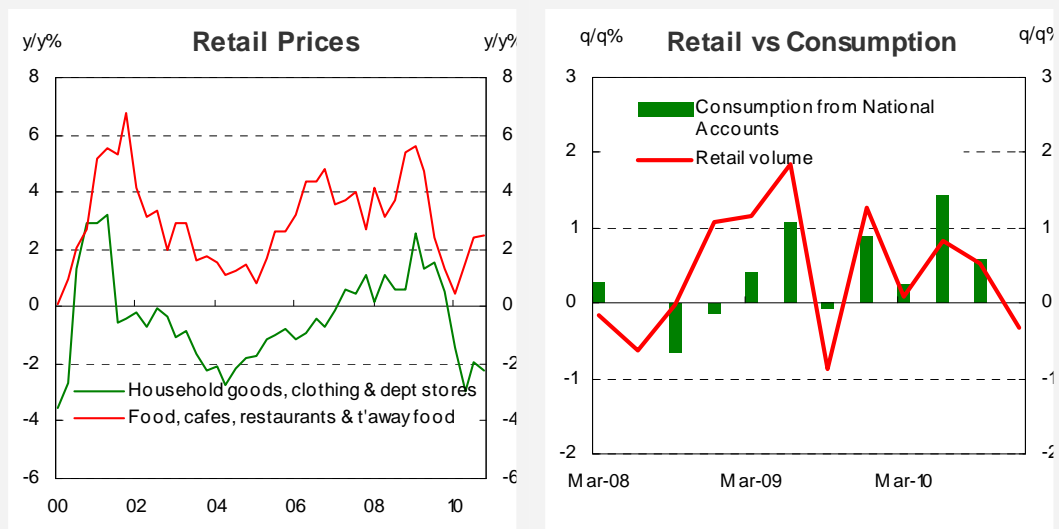
Retail sales edged up 0.2% in December, led by strength in clothing, footwear and personal accessory retailing (+2.7%) and household goods retailing (+1.5%). Spending at cafes, restaurants and takeaway food services also gained (0.8%). Meanwhile, on the weaker side, department store sales fell 1.2% for the month and food retailing also softened (-0.5%). However, with food prices likely to have spiked in January, due to the impact of the Queensland flood and Cyclone Yasi, the value of food retailing may pick up. In annual terms, total retail sales rose just 2.1%, compared to annual growth of 6.1% in 2009 before the Reserve Bank (RBA) began raising official interest rates.

By state, Victoria was the strongest performer, with an increase of 0.5% in retail sales, followed by NSW (0.4%). The sharpest declines in retail sales were seen in SA and Tasmania (both fell 1.3%), while sales in the ACT also declined (-0.5%). In annual terms, Victoria has shown very strong growth in retail sales, reflecting population growth and a robust housing market.

The retailing sector continues to under perform the wider economy. The RBA is likely to be comfortable with the continued caution from householders. Ultimately the RBA would prefer a more solid household balance sheet in the event that there is a commodity shock on the downside or a broad slow down in the economy.

Consumers have become more cautious despite a strong labour market, robust consumer sentiment and rising incomes. Recent interest rate increases from the RBA and the hangover from the GFC appear to have dented consumer's appetites.

Retail Sales – Volumes



Retail sales volumes contracted 0.3% from the previous quarter, in line with market consensus. It suggests that household consumption will be weak for the December GDP figures – although it is not a one-on-one correlation. Retail makes up only 34% of overall household spending.

The decline in volumes was felt across most categories except for a strong rebound in household goods (+3.1%). The pick-up comes off a significant drop in prices – see table over the page. Over the last twelve months, demand for household goods has been more choppy than usual and reflects the bringing forward of sales in both the June and December quarters. Retailers are able to do this given the appreciation of the Australian dollar which is reducing the price of imports. In the meantime households have become more price savvy when it comes to discounting.

While turnover in household goods rose, this was not the case for clothing (-0.6%), department stores (-0.3%) and other retailing (-1.1%). The declines in these categories occurred even with evidence of significant price cuts and is strong evidence that retailers are struggling. Households are either holding back on spending even with price cuts or believe there is more discounting to come as the Australian dollar edges higher.

The sharpest percentage decline in retail volumes is in cafes, restaurants and takeaway food (-4.7%). It follows a strong uptick in the September quarter which has been variously been put down to the "MasterChef effect". It would seem demand for restaurant food has returned to more normal levels or households too have become more price sensitive as to whether they dine in or out. Prices for this category rose 0.7% quarter-on-quarter. Food volumes also shrank in the December quarter - albeit marginally (-0.1%) - while prices continued to rise.

In the chart above we have created an index for food and restaurants. This index is more likely to reflect domestic price pressures. It includes rising wages and utility costs. Wages have generally been recovering since the global financial crisis. We would expect this category to spike up in March reflecting the floods in Queensland. The second plot is made up of the categories – household goods, other retailing, clothing and department stores. Together these will have a high imports ratio and as such are more likely affected by the strengthening dollar. The Australian dollar rose over 9% against the USD during the December quarter. With households being more savvy retailers have been forced to pass on the effects of the higher exchange rate in the form of lower prices. These same trends are being reflected in the consumer price index.

Retail – price and volume analysis

2010 %	Mar Quarter	Jun Quarter	Dec Quarter
Food			
Volumes	0.1	-0.5	-0.1
Price	1.2	0.7	0.5
Household goods			
Volumes	2.6	-0.5	3.1
Price	-1.0	0.0	-1.1
Clothing			
Volumes	3.1	-1.7	-0.6
Price	-1.6	1.8	-1.4
Department stores			
Volumes	-1.6	-0.6	-0.3
Price	-0.8	0.5	-0.7
Other retailing			
Volumes	-0.3	2.6	-1.1
Price	0.6	0.4	-0.1
Cafes, restaurants			
Takeaway food			
Volumes	1.0	5.6	-4.7
Price	0.6	0.6	0.7
Total Retail			
Volumes	0.8	0.5	-0.3
Price	0.1	0.7	-0.1

Job Advertisements

Job advertisements, according to the ANZ measure, rose by 2.4% in January, after a 1.2% rise in December. It takes the number of ads in newspapers and on the internet to a two-year high. The rise in job ads occurred during the flood-affected month of January. Job ads are likely to have risen further if the floods had not hit. It is estimated that job ads would have increased by more than 3% in January without the effect of the floods.

On a year ago, job ads are up 40.5%, the fastest pace of growth since online ads were included in the survey in July 2010.

The continuing increase in job ads suggests that the unemployment rate has further to fall in coming months (looking through the noise that the effect of the floods is likely to cause).

Monetary Policy Outlook

In terms of monetary policy, we still expect the Reserve Bank to raise rates later this year. Our forecast is for tightening to resume in June, but there remains a risk that it gets pushed out to Q3.

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