WEEKLY ECONOMIC COMMENTARY

Week beginning 29th July 2013

ECONOMIC DATA ROUNDUP

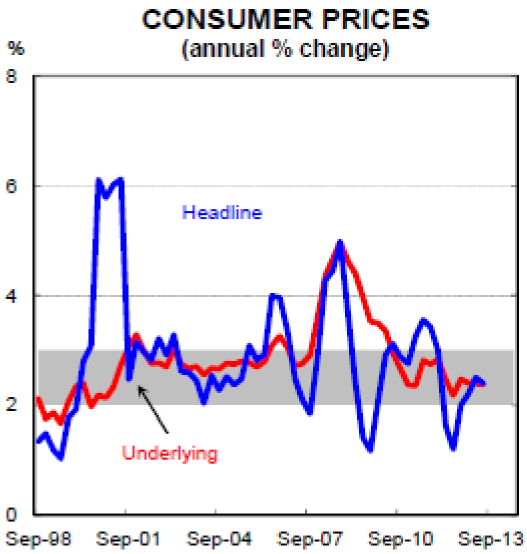
DATA RELEASED LAST WEEK

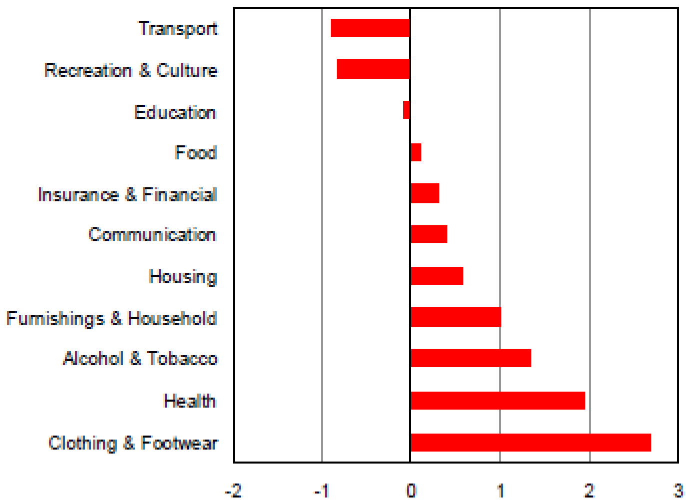
Economic Data	Period	Actual	Previous
DEWR Internet Skilled Vacancies	June	-1.8%	-0.5%
CPI – Headline Quarterly	June quarter	+0.4%	+0.4%
CPI – Headline Annually	June quarter	+2.4%	+2.5%
CPI – Underlying Quarterly	June quarter	+0.6%	+0.5%
CPI – Underlying Annually	June quarter	+2.4%	+2.6%

The **DEWR Internet Skilled Vacancies Index** fell 1.8% in June to be down 23.1% over the year. Falls were recorded in all sub-categories this month, the largest in machinery/drivers (-2.7%), professionals (-2.6%) and administration (-2.2%).

Headline inflation for the June quarter was up 0.4% for an annual rate of 2.4% (down from 2.5% previously). The Reserve Bank of Australia's preferred statistical measure of **underlying or core inflation** was slightly higher than expected, rising 0.6% in the quarter for an annual read of 2.4%.

On the upside, the surprises were in clothing and footwear and furniture (+2.7%), medical and hospital services (+1.9% due to a substantial rise in private health insurance premiums), rents (+1.1%), house purchase costs (+0.9%) and alcohol and tobacco (+1.3%). Fruit and vegetables were lower than expected (+0.3%) and there were strong falls in domestic holiday travel (-2.0%) and automotive fuel (-3.1%). Both readings of CPI are clearly within the RBA's inflation target band of 2% to 3%.





In other news, the Australian Financial Review reported that the Australian Government faces a budget revenue shortfall of $20bn over the next four years. The Federal Government has refused to come clean on what areas of the budget could be cut as Treasurer Chris Bowen puts together an economic statement ahead of the looming election.

Data over the next week

Economic Data	Date	Period	Forecast	Previous
Dwelling Approvals	30 July	June	+3.0%	-1.1%
Private Sector Credit	31 July	June	+0.3%	+0.3%
International Trade – Import Prices	01 Aug	June quarter	+2.0%	+0.0%
International Trade – Export Prices	01 Aug	June quarter	+0.3%	+2.8%
Producer Price Index	02 Aug	June quarter	+0.6%	+0.3%

ECONOMIC COMMENTARY

LAST WEEK

The release of the June quarter CPI data last week gave a mixed result leaving the market none the wiser as to whether the RBA will cut the cash rate at the next Board meeting. The initial response was to reduce expectations of a possible rate cut on 6 August, with the overnight futures market moving from a 73% chance just before the CPI data release to 55%. The CPI result is not a trigger to cut interest rates in August but it does not prevent the RBA from cutting if they decide activity data suggests it is needed.

Better than expected US manufacturing and housing data out mid last week was the now familiar story of “good news is bad news” as the good data turned into a sell-off in bond yields, a stronger US Dollar and a stock market downturn. This was because it means the US Fed’s plan to start tapering bond purchases sooner rather than later remains a possibility.

Chinese Premier Li Keqiang last week stated that GDP growth below 7% this year won’t be tolerated and the acceptable range for Chinese growth this year would be between 7% and 7.5%. A positive story for the market, however a day later, Chinese manufacturing data was released showing its weakest number in almost a year.

By the close of trading on Friday, the 90-day bank bill was trading at 2.74% compared to 2.73% last week. At the long end, 3 and 10 year bond yields closed the week higher at 2.66% and 3.78% from 2.65% and 3.68% a week earlier.

CURRENCY

The Australian Dollar lost ground after the CPI data release last week as the market interpreted the number as slightly reducing the chance of a rate cut in August. The currency came under further selling pressure after the release of weak Chinese manufacturing data and as a result of a stronger US Dollar. The AUD did however recover late in the week as the US Dollar reversed earlier gains. These gains followed a Wall Street Journal article suggesting that this week’s US Federal Open Market Committee (FOMC) meeting will deliver no quantitative easing tapering and more reassurance that US rate hikes are a distant prospect.

By the close on Friday, the AUD was trading at USD0.9259 up almost a cent from USD0.9163 a week earlier.

EQUITIES

Our sharemarket rallied through the psychological 5,000 level and posted its highest point in almost two months last week, initially spiking higher following the release of CPI data and then pushing higher, assisted by strong gains in the mining and energy sectors. News that China’s central bank will give lenders more control to set interest rates appeared to boost commodity prices, which helped local mining companies.

By the close on Friday, the S&P/ASX200 Index was trading at 4,972.1, up 70 points (or 1.4%) over the week compared to 4,972.1 a week earlier.

THIS WEEK

The highlight in the week ahead will be a speech by RBA Governor Glenn Stevens to an Australian Business Economists luncheon in Sydney on Tuesday. We will be eager to see whether the Governor gives any hints on the current thinking around monetary policy ahead of next week’s RBA Board meeting. On the data front, we have June Building Approvals data (which is expected to rebound from a 1.1% fall in May) as well as June quarter international trade price indices and July private sector credit. The Producer Price Index (PPI) for the June quarter is also out on Friday but is unlikely to get much attention given that the release now follows the release of the CPI.

Offshore, we have the US Federal Open Market Committee meeting which, although not expected to deliver a rate change, will receive market attention given the possibility of some news about the timing of the US Fed’s plan to taper their bond-buying program. The Bank of England and the European Central Bank also meet this week.

INTEREST RATE VIEW

Last week’s release of the June quarter CPI data makes calling a rate cut at next week’s RBA Board meeting “tricky” to say the least. While the latest CPI number was in line with the RBA’s forecast, there was a slight upward revision to the previous quarter’s data and inflation over the year to June is now 2.40% – the RBA was looking for inflation to run at 2.25% through the year to June.

Financial markets currently have the probability of a rate cut next week at just over 70%, with almost two rate cuts factored in by early next year.

Economic Data	12 months ago	6 months ago	3 months ago	1 month ago	Now
Official Cash Rate	3.50	3.00	3.00	2.75	2.75
90 day Bank Bill	3.57	2.97	2.94	2.82	2.74
180 day Bank Bill	3.53	2.94	2.93	2.84	2.68
1 year swap	3.36	2.94	2.89	2.78	2.71
3 year swap	3.36	3.13	3.10	3.21	3.15
5 year swap	3.61	3.46	3.44	3.72	3.66
10 year swap	3.94	3.98	3.97	4.44	4.41
AUD/USD	1.0419	1.0448	1.0300	0.9257	0.9259
S&P/ASX200 Index	4,209.8	4,835.2	5,097.5	4,802.6	5,042.0

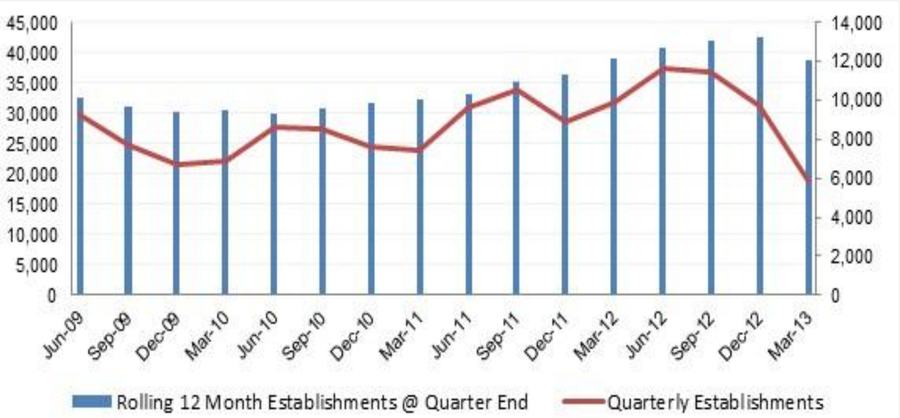
CHART OF THE WEEK

Spotlight on SMSF's

The recent Self-Managed Super Fund (SMSF) March quarter data released by the ATO showing a sharp 40% drop in SMSF establishments, appears to indicate growth in the sector may not only be slowing but may actually be on the decline. I think this is a false alarm.

For starters there tends to be a pick-up in establishments in the final quarter of the financial year, so we should expect a lift, but even then the latest March results are likely to improve after further revisions by the ATO.

Focusing on the quarterly data is interesting; however, too short term in nature for us to be drawing any meaningful conclusions, unless a longer term pattern was to appear. It's more relevant to look at the longer term trend, which as the accompanying chart shows, has seen SMSF establishments (on a rolling 12 month basis) rise steadily over the past three years. Yes, the trend has dipped, seeing the total number of establishments in the past 12 months fall to 38,664 from 42,687(a 9.4% drop), but this is hardly a cause for concern and remains above the average.



Another interesting and relevant data point from the ATO's release, missed in the headlines, is that wind ups have reached a historical low, falling rapidly from 3,251 in the 2012 June quarter, to a low of 62 in the March quarter – that's a total of 4,446 wind ups in the past 12 months, another low.

That's not to say that the latest data doesn't indicate uncertainty with regards to Government policy hasn't had an impact. I'm sure it has; however, this uncertainty is not specific to the SMSF sector.

As CoreData's recent Member Engagement and Post-retirement studies have shown, this uncertainty is impacting the majority of super fund members' confidence in the superannuation system more broadly and also influencing their decisions on whether to make extra contributions to their super over the next 12 months.

If anything, the SMSF sector's growth profile remains healthy. While it will likely experience a slowdown in future, all indications are that the sector will continue its growth trajectory, and move to account for more than just one third of the Australian superannuation sector – with the number of SMSFs having now past half a million, and the number of SMSF members just short of one million.

Any glimmer of hope that super funds may see in the latest drop in quarterly SMSF establishments, shouldn't last. If anything, what should be of concern to super funds is that the fastest growing SMSF segment by age cohort isn't the 50+ segment, but the 41-50 year old segment, followed by the 31-40 year old cohort – as highlighted by CoreData's research. Demand from these segments will continue to drive SMSF growth.

That these are the fastest growing SMSF segments may be news to some and should be of concern to those super funds (and there are many of these) that are only beginning to have a conversation with members around financial planning and retirement when they are in their 50's – thinking that this is the most appropriate time to do so and of the view that it's in this phase and later when SMSFs are predominantly established.

Wrong. The problem with this view of the world issue is that despite the offer of direct investment options, these funds will continue to be blindsided by SMSF specialists such as accountants who will get to their high balance members first before they even realise what's happened.

Source: Core Data's burningpants //
Advice & Wealth Management
19th June 2013

Resurgent markets saw the median growth super fund return 15.6% in the 2012/13 financial year, the best performance in the past 16 years according to research firm Chant West's annual survey. The best performing asset classes in the 2012/13 period were unhedged international shares (up 33.1%), Australian shares (up 21.9%), Australian real estate investment trusts (up 24%) and global property securities (up 17.2%).
The performance of unhedged international shares was aided by the Australian dollar's decline from USD1.02 to USD0.91, said Chant West.

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