

## The Close Call for the Peak of the Antipodean Rates

### Kiwi

**The RBNZ rate decision will be released tomorrow at 5am local time. Our call is for the RBNZ to remain on hold at 8.25%. However, we view the decision as a close call as while growth data since the last meeting has continued to worsen, there is no clear easing in upside price pressures. Reflecting this uncertainty, the OIS market is attaching a 50% chance of a 25bp rate cut.**

The RBNZ left interest rates unchanged at its 5 Jun policy meeting but released a more dovish than expected statement, affirming that the bank was likely to lower interest rates going forward. The RBNZ statement said specifically that 'we are now likely to be in a position to lower the OCR later this year, which is sooner than previously envisaged.'

Since then, Q1 GDP number has confirmed the worsening outlook, posting a -0.3%qoq (1.9%yoy) growth from a Q4 growth of 0.8%qoq (3.5%yoy). The housing market has remained weak with Jun REINZ house sales turning in a reading of -42.4%yoy from a May reading of -52.9% and QV house prices also sliding to 0.1%yoy from a prior 2.4% reading. The slowing economy, high interest rates and elevated food and oil prices have kept a lid on consumption. May retail sales came in significantly below expectations at 1.2%mom against expectations for a -0.1% reading and falling from a positive 1.2% in Apr. Excluding autos, retail sales performed better, coming in at 0.7%mom against expectations for a 0.5%mom read. Forward indicators point to tougher conditions ahead. The 2Q Westpac NZ consumer confidence fell to 81.7, its lowest since Sep1991 and the 2Q NZIER business opinion survey remained flat at -64, a 33yr low.

Against clearly softening growth, inflation has remained elevated with 2Q CPI rising 1.6%qoq (4.0%yoy) from 0.7%qoq (3.4%yoy) and against expectations for a 1.4% (3.8%yoy) reading. While the headline number came in above expectations, the non-tradable (domestic) inflation rose 0.9%qoq (3.4%yoy), slowing from a rise of 1.1%qoq (3.5%yoy).

**We see the direction of policy as clearly a move downwards in rates but the timing of the cut remains contentious. Our call is for the RBNZ to remain on hold this time ahead of 2Q Employment change data due early Aug and we expect the RBNZ to signal intentions to ease in Sep in its statement release. As a result, either way the RBNZ moves, we expect the Kiwi to be plagued by downside pressures. We think NZD/USD is likely to trend downwards post meeting to break the 0.75 levels to the 0.74 levels. And we expect the pair to move lower across the year to end 2008 lower at the lower 0.71 level.**

### Aussie

**Today saw the release of the key inflation number for the AU economy. AU 2Q CPI today came in higher than expected at 1.5%qoq (4.5%yoy) from 1.3%qoq (4.2%yoy) in 1Q. Increases in both the trimmed mean and weighted median measures were more muted with the average of both measures coming in at 1.1%mom (4.4%yoy) against expectations for a reading of 1.1%qoq (4.3%yoy) from a 1Q reading of 1.25%qoq (4.25%yoy). On Mon, we saw 2Q PPI come in weaker than expected at 1.0%qoq (4.7%yoy) below expectations for a 1.6% (5.3%) reading and coming off a 1Q reading of 1.9% (4.8%).**

**We see the numbers as indicating still elevated inflationary pressures, although the acceleration in inflation appears to have eased somewhat which we think could defer any rate cut views. An Aug rate hike is unlikely to be imminent on the cards at this point in time given that the RBA has indicated that it believes that demand is slowing and prices will ease over time.**