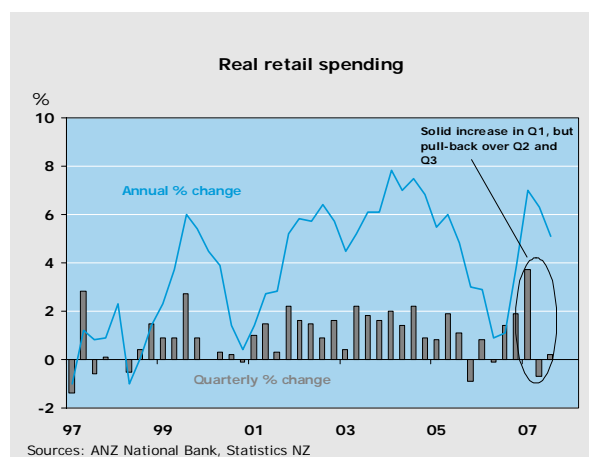


RETAIL SALES – SEPTEMBER QUARTER 2007

Key points

- Higher petrol prices boosted total retail sales in September, while core sales were more muted.
- Looking at the broad messages, a moderation in consumer spending looks to be continuing.
- Modest consumer spending is another indicator of soft Q3 GDP, following weak job figures.
- Net on net, it looks like another indicator that has failed to provide the smoking gun the market is fearful in terms of further hikes, although vigilance towards inflation continues to be required.

	Core Retail Sales (% change)		Total Retail Sales (% change)		
	nominal m/m	Trend	nominal m/m	Trend	real q/q
Mar-07	0.3	0.5	0.9	0.5	3.7
Apr-07	-1.0	0.3	-1.3	0.3	-
May-07	0.6	0.1	1.1	0.2	-
Jun-07	-0.4	0.1	-0.4	0.2	-0.7
Jul-07	0.0	0.1	0.2	0.2	-
Aug-07	0.8	0.2	0.3	0.2	-
Sep-07	0.5	0.2	1.0	0.2	0.2
ANZ	0.6	-	0.8	-	0.1
Market	0.6	-	0.6	-	0.4

Assessment and implications

Total nominal retail sales rose 1.0 percent in September, above market expectations. The increase looks to be boosted by petrol price increases over the month. Petrol sales accounted for close to half of the increase in total retail sales in the month, recording a 5.1 percent increase. Core sales (which exclude motor vehicle-related industries) rose a more modest 0.5 percent. Movements in other components were much more muted. Eight industries had small sales increases or decreases of less than \$1 million. Regionally, seasonally adjusted sales in the Waikato region decreased 0.4 percent, but increased in all other regions over September.

Quarterly volume growth was soft, increasing 0.2 percent. This comes after a 0.7 percent fall in the June quarter. These soft results need to be put in perspective, however, given strong growth of 1.9 percent and 3.7 percent in the December 2006 and March 2007 quarters, respectively. Across the quarter, the supermarket and grocery stores industry (up \$25 million) and accommodation (\$24 million) made the largest contributions to the increase in total retail volumes, while recreational goods retailing (down \$31 million) and clothing and softgoods retailing (down \$29 million) recorded the biggest decreases in volumes. The increase in the retail sales deflator was slightly below our expectations, rising 0.3 percent.

On balance, today's data shows ok momentum in retailing, although an underlying softening tone considering the general volatility in the series. Core sales have rebounded for two months following flat sales the months prior. However, monthly trend growth measures show a moderation in spending with the trend in both total and core measures tracking at 0.2 percent per month. Looking forward, we expect sales to moderate further into Christmas as less impetus is provided from the housing market, and higher mortgage rates and cost increases continue to bite on household incomes. Nonetheless, this has to be balanced against some strong support that remains from income growth. The Christmas sales period is likely to be critical for businesses in terms of assessing whether moderating housing activity is impacting the broader economy.

Today's soft quarterly volume result is another measure pointing to a soft growth outturn for Q3. If not for increased oil production from the Tui oil field, Q3 GDP would be looking decidedly weak. We have currently pencilled in Q3 GDP growth of 0.2 percent, decidedly below the Reserve Bank's September *Monetary Policy Statement* forecast of 0.8 percent. **In terms of the Reserve Bank,** we take today's data as supporting the stance that their job is done, failing to provide another smoking gun the market continues to look for. However, in the current inflation sensitive and cost-push risk environment, significant vigilance is required.

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