

JULY 2010 – SEPTEMBER 2010

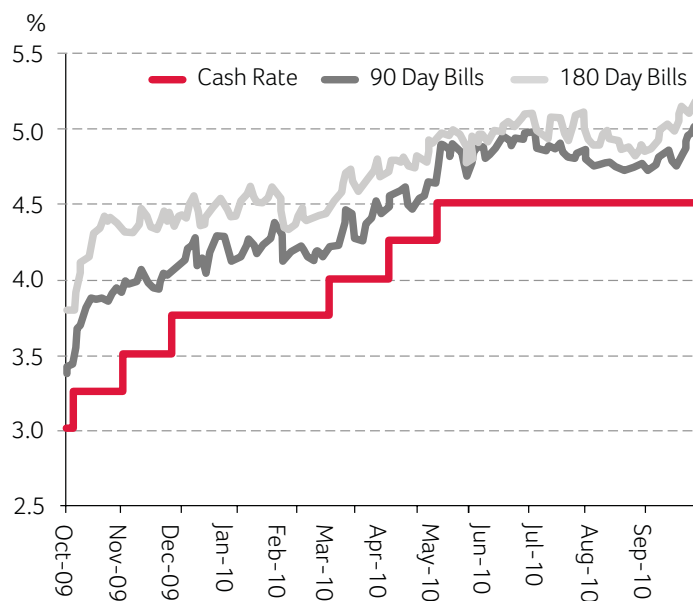
Cash & fixed interest are generally considered relatively low risk investments when compared to shares and property. Consequently the expected returns are lower, and modest returns are generally made over long time periods. One thing to bear in mind is inflation. For example, if the interest rate earned on a cash investment is 5% p.a. and the annual inflation rate is 3% p.a., the real return is 2% p.a.

Quarter Review

In the September quarter the RBA left the cash rate unchanged at 4.5% and the market was generally priced with a small tightening premium for the next twelve months. Following strong growth and employment data and rhetoric from the RBA that was viewed as hawkish, the market moved to price in an October rate hike and the chance of a follow up hike in November – as a result, bill yields rose.

Domestically, the economy continued to diverge from the rest of the industrialised world, with activity reported to have grown at a very strong rate in the June quarter. More recent data points to robust growth continuing into the second half of the year, led by a rapid rise in Australia's terms of trade and a sharp increase in planned business investment, especially in the mining sector. The resulting strength in employment saw the unemployment rate remain at 5.1% and has helped drive a pickup in discretionary retail spending. While consumer price data for the June quarter was benign, the strengthening in activity against the back drop of low levels of spare capacity in the economy have raised concerns over the outlook for inflation in Australia. In response, the RBA left rates on hold throughout the quarter, although recent communications have focused on the likelihood of further rate rises being required over coming months.

Australia Bank Bill Yields



Outlook

Early in October contrary to market expectations, the cash rate was held at 4.5%. It is likely that the next move will be higher and this month's consumer price data will likely prove important for determining whether any monetary policy tightening will occur this year.

A note from our legal team

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