Monday, 13 November 2023

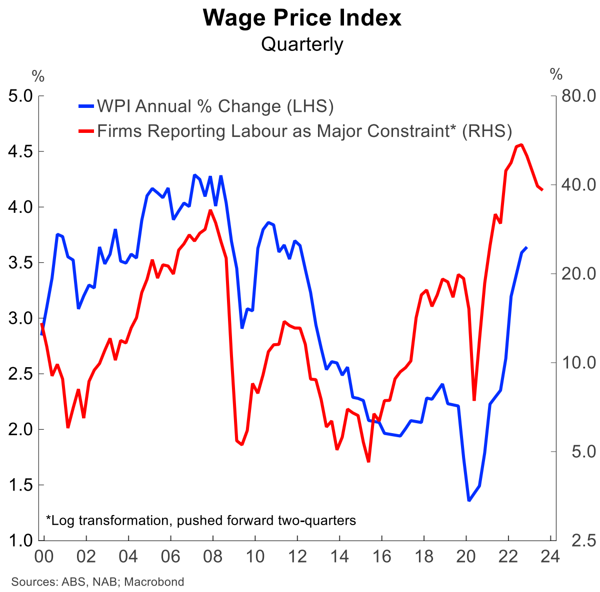
‘Data-Dependent’ RBA to Get Their Fix

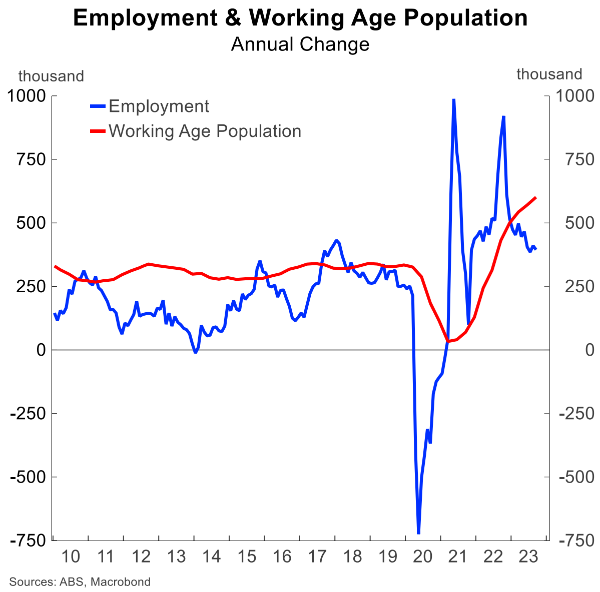
The attention rested squarely on the Reserve Bank (RBA) last week with the November monetary policy meeting and the release of the quarterly Statement on Monetary Policy (SoMP). But this week will be more about the data - the premier consideration for a ‘data-dependent’ RBA Board.

The focus will be on the labour market and wages. The September quarter wage price index (WPI) comes out Wednesday. In the June quarter, the WPI rose 0.8% and 3.6% in annual terms. The result underwhelmed expectations and provided an early signal that momentum in wages growth might be waning alongside a surge in labour supply.

We expect the September quarter to be a lofty number, 1.3% in the quarter and 3.9% in annual terms. This is largely due to the 2023-24 Fair Work Commission (FWC) minimum and award wage decision which took effect on July 1. The decision granted a 5.75% wage increase for around 2.7 million workers on a minimum wage, award or enterprise agreements tied to an award.

The flow-through of the minimum and award wage decision is a known entity, but the evolution of wages elsewhere in the economy will be important. We are expecting to see some evidence that wage growth for workers on individual arrangements – who experienced larger increases in their wages earlier in the cycle – is beginning to cool alongside the improving balance of supply and demand in the labour market. The outcome for workers on individual arrangements and the dynamic of bonus and other incentive payments will be of critical interest to the RBA and could make or break their assessment of the inflation risks posed by a tight labour market.



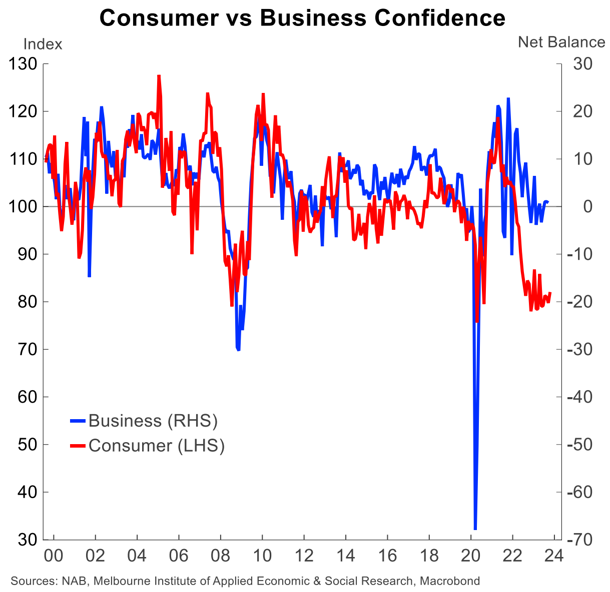


The release of the October Labour Force Survey on Thursday will compliment this information. A very gradual easing in conditions is underway in the labour market. Labour supply is continuing to roar ahead at a rapid clip, driven by population growth and elevated participation, but the desire of firms to employ workers is gently moderating.

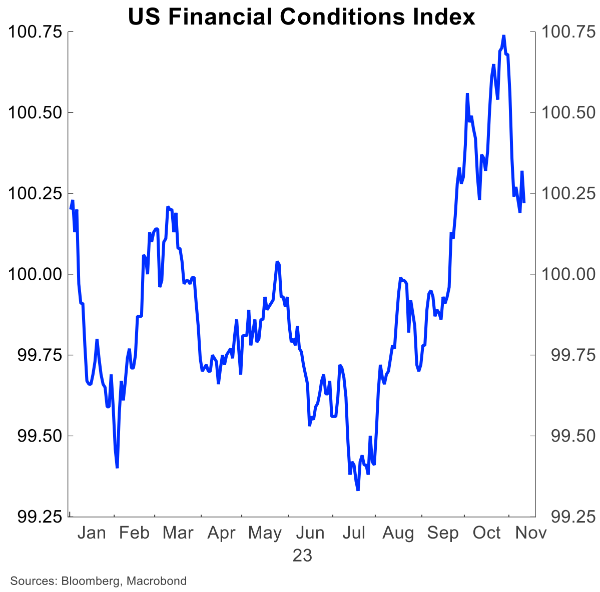
We are yet to see meaningful evidence of softening in the unemployment rate, but we are beginning to see some emerging weakness in other important labour market indicators, including hours worked, employment intentions, and surveyed hires and separation rates. This is expected, and we anticipate that much of the forecast adjustment in the labour market could occur through hours worked rather than headcount. The recent experience of businesses struggling to find workers is a key reason for this, but the outsized share of multiple jobholders and large number of employees who transitioned from part-time to full-time working hours mean the adjustment could be significant.

In October, we expect employment rose by around 25.0k – in line with the current trend pace – leaving the unemployment rate unchanged at 3.6%. This assumes a tick up in the participation rate to 66.8% after a surprise fall in September, but as usual this remains a wildcard.

The other domestic data in the RBA's sightlines will be the consumer and business sentiment reports. These measures have diverged wildly for some time now and the gap is unlikely to close significantly in Tuesday's data. Household income is under significant pressure from inflation, tax and interest rates and that's being reflected in very weak consumer confidence. Meanwhile, business conditions are being supported by surging population growth, which is driving a wedge between per-capita and aggregate spending outcomes. This is cushioning the usual transmission of monetary policy from households through to businesses and underpinning the resilience we are seeing in businesses investment. Note that there are other direct transmission channels through which monetary policy impacts businesses but the feedback between households and businesses is being interrupted. Solid conditions for businesses are fuelling optimism, but a dull outlook is working in the other direction leaving business confidence in unimpressive but equally unconcerning territory.



Sources: NAB, Melbourne Institute of Applied Economic & Social Research, Macrobond



Sources: Bloomberg, Macrobond

The RBA has made it clear that they are becoming more attentive to domestic developments when considering the outlook for the economy and the balance of risks. But this does not mean the global backdrop can be swept under the rug. There are several important releases offshore this week which will be on the RBA's radar.

Inflation readings in both the US and UK will be released on Tuesday and Wednesday night, respectively. Australia's inflation cycle is less progressed than some other countries, so monitoring the overseas experience is important for considering our own inflation trajectory. But in the US the market reaction to the inflation release may be just as important as the release itself. This is because of financial conditions, which have become an important feature of the policy debate in the US.

Financial conditions are important because they reflect how monetary policy conditions are transmitting to a broader set of financial variables. Since the end of July, financial conditions in the US tightened substantially, predominantly due to a surge in longer-dated bond yields. This has since partly unwound, but conditions remain tighter than they were a few months ago. Fed Chair Jerome Powell recently introduced financial conditions as a specific consideration for monetary policy, elevating their importance. A surprise in the inflation data could evoke a response in bond and equity markets, moving the dial on financial conditions. This has implications for policy.

Finally, fresh industrial production and retail spending data out of China will be run under the microscope. Recent data has been mixed. The Chinese economy is clearly stabilising and there are signs of a tentative recovery developing. But the economy remains fragile, and risks are ever-present. Retail spending data will be important. Authorities are trying to engineer a more 'organic' economic recovery rather than relying on large infrastructure spending. Consumers lie at the centre of this approach, but confidence remains weak as fragilities in the property sector have hit dwelling values, eroding household wealth and prompting a lift in precautionary saving.

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Group Forecasts

		2023	2024				2025
End Period:	**Close (10 Nov)**	**Q4 (f)**	**Q1 (f)**	**Q2 (f)**	**Q3 (f)**	**Q4 (f)**	**Q1 (f)**
Aust. Interest Rates:							
RBA Cash Rate, %	4.35	4.35	4.35	4.35	4.10	3.85	3.60
90 Day BBSW, %	4.41	4.55	4.55	4.47	4.22	3.97	3.72
3 Year Swap, %	4.46	4.50	4.40	4.30	4.20	4.10	3.90
10 Year Bond, %	4.62	4.70	4.60	4.50	4.40	4.30	4.15
US Interest Rates:							
Fed Funds Rate, %	5.375	5.375	5.125	4.875	4.625	4.375	4.125
US 10 Year Bond, %	4.65	4.80	4.70	4.60	4.50	4.40	4.20
USD Exchange Rates:							
AUD-USD	0.6361	0.66	0.67	0.68	0.69	0.70	0.71
USD-JPY	151.52	149	147	144	141	138	135
EUR-USD	1.0686	1.08	1.09	1.11	1.13	1.14	1.15
GBP-USD	1.2227	1.23	1.24	1.25	1.26	1.27	1.28
NZD-USD	0.5891	0.60	0.61	0.62	0.62	0.62	0.63
AUD Exchange Rates:							
AUD-USD	0.6361	0.66	0.67	0.68	0.69	0.70	0.71
AUD-EUR	0.5952	0.61	0.61	0.61	0.61	0.61	0.62
AUD-JPY	96.38	98.3	98.5	97.9	97.3	96.6	95.9
AUD-GBP	0.5202	0.54	0.54	0.54	0.55	0.55	0.55
AUD-NZD	1.0797	1.09	1.10	1.11	1.11	1.12	1.13

	2021	2022	2023 (f)	2024 (f)
GDP, %	4.6	2.7	1.2	1.6
CPI (Headline), %	3.5	7.8	4.6	3.4
CPI (Trimmed mean), %	2.6	6.8	4.4	3.3
Unemployment Rate, %	4.7	3.5	3.8	4.7
Wages Growth, %	2.3	3.4	3.8	3.2

AUD cross exchange rates have been rounded.

Financial forecasts are quarter end.

GDP, CPI, employment and wage growth forecasts are year end.

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