

Monday, 18 May 2020

The Road Ahead

The World Health Organisation (WHO) declared a global pandemic just over two months ago on March 11. Since then, COVID-19 has been ubiquitous. In the urgency to contain the health crisis, the economic consequences have been disastrous, with most economists agreeing that the unfolding recession is of a scale not seen since the Great Depression. The economic data is now catching up with this reality, resulting in numerous data releases being accompanied with the phrase “worst on record”.

As movement restrictions aimed at slowing the spread of COVID-19 are gradually relaxed, attention is becoming more focussed on the shape of the economic recovery. The enormous drop in economic activity needs to be viewed in the context of unprecedented stimulus, and a type of external shock not experienced in our lifetimes.

Last week, the April edition of the Australian labour force survey was released. The data showed that labour market conditions deteriorated sharply, with the unemployment rate increasing 1 percentage point to 6.2% and employment falling by 594k. These are startling numbers, but Australia’s labour market judgement day proved less severe than in some other countries. For example, in the US, non-farm payrolls fell by 20.5 million in April and the unemployment rate spiked to 14.7%.

The reason for the comparatively muted response in the unemployment rate was two-fold: a record 490k Australians left the labour market and the Federal Government’s JobKeeper wage subsidy incentivised employers to keep staff on, even if they weren’t working any hours. The Government said on Thursday that 860k businesses are currently receiving JobKeeper payments, supporting millions of workers.

It usually takes years for employment levels to return to normal after a large negative shock. A key question in terms of the recovery is whether or not those on JobKeeper will be able to seamlessly return to work as restrictions are eased. This is contingent on the absence of a “second wave” of infections, and activity quickly returning to normal.

If businesses can’t justify employing the same level of staff by September (when the subsidy is due to expire), there is a risk of a “second wave” shock to the labour market. If activity hasn’t recovered sufficiently, scarring in the labour market could result in a negative feedback loop of diminished household spending, weaker investment and soft private demand.

Weekly payrolls wages and jobs data for the week ending 2 May will be released tomorrow, providing an indication of whether or not the bleeding in the labour market has been stemmed. Tomorrow, the minutes of the RBA’s May meeting will also be released. There were no changes to policy settings at this meeting, but the minutes will provide valuable insight into the RBA’s assessment of the economy over this challenging period.

Preliminary data for retail sales in April will be released on Wednesday and there will be the opportunity to glean additional insight into the RBA’s thinking on Thursday when Governor Philip

Lowe takes part in a panel discussion.

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Forecasts are detailed on the following page

Forecasts

Please note that due to the unprecedented nature of the coronavirus's impact on the economy and the rapid change of developments, there is greater than usual variability attached to these forecasts.

End Period:	2020				2021	
	Close (May 11)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)	Q2 (f)
Aust. Interest Rates:						
RBA Cash Rate, %	0.25	0.25	0.25	0.25	0.25	0.25
90 Day BBSW, %	0.10	0.15	0.20	0.25	0.30	0.35
3 Year Swap, %	0.20	0.35	0.35	0.40	0.40	0.45
10 Year Bond, %	0.91	0.75	0.80	0.85	0.90	1.00
US Interest Rates:						
Fed Funds Rate, %	0.125	0.125	0.125	0.125	0.125	0.125
US 10 Year Bond, %	0.64	0.60	0.65	0.70	0.75	0.80
USD Exchange Rates:						
AUD-USD	0.6413	0.62	0.64	0.66	0.68	0.68
USD-JPY	107.06	107	105	106	107	107
EUR-USD	1.0820	1.07	1.06	1.06	1.07	1.08
GBP-USD	1.2116	1.22	1.23	1.24	1.25	1.25
NZD-USD	0.5935	0.60	0.61	0.61	0.63	0.64
AUD Exchange Rates:						
AUD-USD	0.6413	0.62	0.64	0.66	0.68	0.68
AUD-EUR	0.5927	0.58	0.60	0.62	0.64	0.63
AUD-JPY	68.67	66.3	67.2	70.0	72.8	72.8
AUD-GBP	0.5298	0.51	0.52	0.53	0.54	0.54
AUD-NZD	1.0810	1.03	1.05	1.08	1.08	1.06

	2019	2020 (f)	2021 (f)
GDP, %	2.2	-5.0	4.0
CPI (Headline), %	1.8	0.3	2.4
CPI (Trimmed mean), %	1.6	1.1	1.8
Unemployment Rate, %	5.2	7.6	6.3
Wages Growth, %	2.2	1.8	1.6

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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