

Monday, 1 June 2020

Awaiting the Results

It is a big week for us economists, as we receive the quarterly report card on Australia's economy on Wednesday. We call it "GDP day", and it takes on great importance as we attempt to assess the impact of COVID-19 on the economy.

The data will cover the first quarter of the year, so it will not capture the bulk of the impact from restrictions aimed at preventing the spread of COVID-19.

However, we expect that it will be a weak quarter. Tourism and education were negatively impacted earlier in the year when lockdown measures were imposed in China. The bushfires also negatively impacted tourism, and affected sectors such as agriculture and construction.

A contraction in economic activity is expected for the first quarter, although the largest contraction is likely to occur in the second quarter of the year, when social distancing measures were in full swing.

The outlook is fraught with challenges, even as restrictions are lifting.

In part, this reflects the high likelihood that restrictions will remain in place for some time. However, it is the hit to confidence which is likely to hurt spending by consumers and businesses.

Along with the threat of COVID-19 still in the background, the world is becoming increasingly volatile. There was apprehension ahead of a press conference on Friday by US President Trump, after China had ruled to impose a national security law in Hong Kong. Trump said that "we will take action to revoke Hong Kong's preferential treatment as a separate customs and travel territory from the rest of China". In addition, Trump said that sanctions would be imposed on certain individuals seen as "smothering" Hong Kong's freedom.

However, Trump did not provide a timeline of when this would happen, nor did he impose additional hard line action against China, such as further tariffs. Financial markets seemed to take this in a positive light, judging by the reaction in equity markets and the Australian dollar, which have rallied this morning. The Australian dollar has pushed past 67 US cents at the time of writing.

Nonetheless, Trump's comments do not suggest any de-escalation in global tensions. The risk of rising conflict between the two largest economies in the world remains heightened. Unrest in the US adds to the air of uncertainty.

We also face more uncertainties back home, as the economy looks to recover from COVID-19-related restrictions.

The major test is how the economy will cope after temporary support measures expire, including the Government's JobKeeper payment.

There is likely to be immense pressure on the Government to provide additional assistance or other alternatives to transition away from this payment.

The Government is expected to unveil home buyer grants to help the residential construction

sector this week. It would not be surprising if other forms of support were to be announced over coming months.

Along with GDP on Wednesday, we will receive some of the key inputs to its calculation tomorrow, including company profits, the current account and net exports. Company profits are expected to be flat, reflecting the early impact of COVID-19. Net exports are however, expected to show a positive contribution to growth, but both export and import volumes are expected to have weakened sharply. In particular, service imports have been hit particularly hard.

The RBA will hold its monetary policy meeting on Tuesday, but is widely expected to keep policy settings unchanged. Building approvals and retail sales will be released on Wednesday and Thursday. Both sets of data are data for April and are expected to show sharp falls when social distancing measures were in full force.

This morning, we received data on dwelling prices for May which have declined modestly. Sales volumes have recovered as restrictions on physical auctions and open homes have lifted. But the uncertainty with regards to the outlook, loss of incomes and concerns about weaker population growth are weighing on housing demand and are beginning to bring down prices.

Janu Chan, Senior Economist
Ph: 02-8253-0898

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 29)	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	0.10	0.10	0.15	0.20	0.25
3 Year Swap, %	0.27	0.25	0.30	0.30	0.35	0.35
10 Year Bond, %	0.89	0.85	0.90	0.95	1.00	1.10
US Interest Rates:						
Fed Funds Rate, %	0.125	0.125	0.125	0.125	0.125	0.125
US 10 Year Bond, %	0.65	0.60	0.65	0.70	0.75	0.80
USD Exchange Rates:						
AUD-USD	0.6667	0.64	0.66	0.68	0.70	0.70
USD-JPY	107.83	107	105	106	107	107
EUR-USD	1.1101	1.08	1.09	1.10	1.11	1.11
GBP-USD	1.2343	1.22	1.23	1.24	1.25	1.26
NZD-USD	0.6205	0.59	0.60	0.61	0.62	0.62
AUD Exchange Rates:						
AUD-USD	0.6667	0.64	0.66	0.68	0.70	0.70
AUD-EUR	0.6007	0.59	0.61	0.62	0.63	0.63
AUD-JPY	71.92	68.5	69.3	72.1	74.9	74.9
AUD-GBP	0.5398	0.52	0.54	0.55	0.56	0.56
AUD-NZD	1.0748	1.08	1.10	1.11	1.13	1.13

	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	8.0	7.0
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.

Contact Listing

Chief Economist

Besa Deda

dedab@bankofmelbourne.com.au

(02) 8254 3251

Senior Economist

Janu Chan

chanj@bankofmelbourne.com.au

(02) 8253 0898

Economist

Nelson Aston

nelson.aston@bankofmelbourne.com.au

(02) 8254 1316

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