

Monday, 24 August 2020

Onwards and Upwards

It's been another week, another gain for US equities. Australian shares haven't performed quite as well, but a 34% increase in the ASX 200 in five months since its pandemic low is nothing to be scoffed at.

Driving the increase has been unprecedented stimulus, record low bond yields and confidence that an effective, safe COVID-19 vaccine is nearing reality. The economic data has not been so rosy, although the worst of the economic shock appears to be over. Investors have been pleasantly surprised by the US economic recovery. The housing market has been a bright spot with existing home sales in July surpassing the level recorded in February before the onset of the pandemic.

The economy-wide report card for Australia in Q2 is due to be released on Wednesday next week. We are expecting a 7% fall in GDP over the quarter as lockdown directives forced consumption to grind to a halt and business investment was scuttled.

Victoria's stage 4 lockdown will prove a major drag to growth in Q3, however, activity is nonetheless expected to recover. We are expecting flat growth in GDP in Q3 before the economy rebounds by 2.8% in the final quarter of 2020. After falling 4.7% over 2020, Australian GDP is expected to rebound by 3.0% in 2021.

In line with the improved risk appetite evident in equity markets and strength in our major commodity export prices, the Australian dollar has risen steadily from US\$0.57 on 19 March to breaking above US\$0.72 on a few occasions over the past month.

There continues to be downside risks for the global economy, however, some of these risks have dissipated given a stabilisation in COVID-19 cases worldwide. We expect a more rapid appreciation in the Australian dollar than in our previous forecast. Our end of 2020 forecast for the AUD has been lifted from US\$0.72 to US\$0.75. We now expect the Australian dollar to reach US\$0.80 by the end of 2021. Ongoing strength in the Chinese economic recovery, improved sentiment towards vaccine developments and a recovery in the global economy will continue to bolster the Australian dollar.

Important partials into Q2 Australian GDP will be released this week, which will show the impact of the nationwide lockdown on economic activity. Construction work done released on Wednesday is expected to show that activity contracted 3.4% over the quarter while private capital expenditure released on Thursday is expected to show an 8.2% decline in investment in Q2. Weekly payrolls data for the week ending 8 August will provide a timely indication of developments in the labour market. The improvement in labour market conditions since its lows in late March has stalled. We will be watching data for Victoria closely for an indication on how Stage 4 restrictions has impacted its labour market.

Internationally, the key event will be a speech from US Federal Reserve Chair Powell on Thursday where investors will be searching for clues about how the Fed will manage the long-term recovery

of the economy from the COVID-19 pandemic.

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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 (Aug 21)	Q3 (f)	Q4 (f)	Q1 (f)	Q2 (f)	Q3 (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	0.15	0.20	0.25	0.30
3 Year Swap, %	0.20	0.25	0.30	0.35	0.35	0.40
10 Year Bond, %	0.88	0.90	0.90	0.95	1.05	1.20
US Interest Rates:						
Fed Funds Rate, %	0.125	0.125	0.125	0.125	0.125	0.125
US 10 Year Bond, %	0.63	0.60	0.60	0.65	0.75	0.85
USD Exchange Rates:						
AUD-USD	0.7161	0.73	0.75	0.76	0.76	0.78
USD-JPY	105.80	105	105	105	106	106
EUR-USD	1.1797	1.19	1.21	1.22	1.23	1.24
GBP-USD	1.3090	1.32	1.33	1.34	1.35	1.37
NZD-USD	0.6541	0.66	0.67	0.66	0.66	0.68
AUD Exchange Rates:						
AUD-USD	0.7161	0.73	0.75	0.76	0.76	0.78
AUD-EUR	0.6071	0.61	0.62	0.62	0.62	0.63
AUD-JPY	75.54	76.7	78.8	79.8	80.6	82.7
AUD-GBP	0.5471	0.55	0.56	0.57	0.56	0.57
AUD-NZD	1.0949	1.11	1.12	1.15	1.15	1.15

	2019	2020 (f)	2021 (f)
GDP, %	2.2	-4.7	3.0
CPI (Headline), %	1.8	0.7	2.1
CPI (Trimmed mean), %	1.6	0.8	1.7
Unemployment Rate, %	5.2	8.6	7.4
Wages Growth, %	2.2	1.9	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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The Detail

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