Weekly Economic Outlook

Inflation Really Matters

A fortnight ago, the Reserve Bank Governor told us that 'actual' inflation, rather than expected or forecast inflation would sit at the heart future RBA policy.

Only when actual, observed inflation is sustainably within the RBA's target range of 2-3% per annum will the RBA tighten monetary policy. And that's no time soon! Indeed, we expect the RBA to ease policy at its meeting on 3rd November.

It is broadly accepted that RBA policy will not be tightened for at least three years.

The first read of inflation since the Governor's speech will occur on Wednesday when the Australian Bureau of Statistics releases the September quarter Consumer Price Index (CPI). This will be an 'actual' inflation result, and it will be well below the RBA's target.

We expect that inflation during the September quarter rose 1.1%. This would bring the annual rate of inflation to 0.3%.

Why 1.1% for the quarter? Part of the answer is that the full government subsidy for childcare was unwound in all states except Victoria. There was also a steep increase in petrol prices and increases in pre-school and primary education costs in most states.

There were some factors working to supress inflation. Government grants for the construction of new dwellings and renovations may have kept housing costs down and rents appear to have declined. Fruit and vegetable prices are also expected to have fallen.

If the changes in government policy towards early education and housing were excluded, our forecast for the increase in the CPI would be closer to 0.5% for the quarter.

Market expectations for the quarterly CPI range from 0.5% to 2.1% with a median of 1.5%. The range of forecasts for the annual rate of inflation is -0.4% to 1.4% with the median at 0.7%.

Even using the highest forecasts, actual inflation will be well below the RBA's 2-3% target range.

Part of the government's, and the RBA's, strategy for economic recovery is to lift business investment and business borrowing. This, in turn should create jobs. The Reserve Bank will release the private sector credit figures on Friday. These will tell us about new credit extended for businesses, for housing and for personal items such as credit cards and car loans.

The credit figures out on Friday will be for September, before the October Budget. Annual credit growth has been sluggish. We expect September saw no growth in credit with the annual rate falling to 2.0%. Hopefully borrowing will pick up in the months ahead as the economy reopens and businesses as well as individuals take advantage of the stimulus measures and lower interest rates.

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Forecasts

		2020		2021		
End Period:	**Close (Oct 25)**	**Q4 (f)**	**Q1 (f)**	**Q2 (f)**	**Q3 (f)**	**Q4 (f)**
Aust. Interest Rates:						
RBA Cash Rate, %	0.25	0.10	0.10	0.10	0.10	0.10
90 Day BBSW, %	0.06	0.04	0.04	0.04	0.04	0.04
3 Year Swap, %	0.09	0.08	0.08	0.08	0.08	0.08
10 Year Bond, %	0.86	0.75	0.75	0.75	0.80	0.85
US Interest Rates:						
Fed Funds Rate, %	0.13	0.125	0.125	0.125	0.125	0.125
US 10 Year Bond, %	0.86	0.70	0.65	0.65	0.70	0.75
USD Exchange Rates:						
AUD-USD	0.7139	0.75	0.76	0.76	0.78	0.80
USD-JPY	104.71	105	105	106	106	106
EUR-USD	1.1860	1.21	1.22	1.23	1.24	1.25
GBP-USD	1.3039	1.32	1.34	1.35	1.37	1.39
NZD-USD	0.6691	0.67	0.66	0.66	0.68	0.70
AUD Exchange Rates:						
AUD-USD	0.7139	0.75	0.76	0.76	0.78	0.80
AUD-EUR	0.6019	0.62	0.62	0.62	0.63	0.64
AUD-JPY	74.76	78.8	79.8	80.6	82.7	84.8
AUD-GBP	0.5472	0.57	0.57	0.56	0.57	0.58
AUD-NZD	1.0671	1.12	1.15	1.15	1.15	1.14

	2019	2020 (f)	2021 (f)
GDP, %	2.3	-3.5	2.8
CPI (Headline), %	1.8	0.3	1.9
CPI (Trimmed mean), %	1.6	0.6	1.7
Unemployment Rate, %	5.2	7.5	7.5
Wages Growth, %	2.2	0.9	1.0

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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