

Monday, 3 June 2019

RBA and GDP in the Limelight This Week

This week is data packed with no less than eight key economic-data releases due and a bunch of minor economic releases also slated. The limelight will be firmly shining on the Reserve Bank (RBA) board meeting decision (tomorrow 2:30pm AEST) and the gross domestic product (GDP) outcome for Q1 (Wednesday).

There is not a lot that has not been said about tomorrow's RBA meeting. A rate cut of 25 basis points seems a lay down misere. The accompanying statement will be closely gleaned for clues about forthcoming monetary-policy decisions. We think the RBA will need to cut another two times this year, in August and November, taking the cash rate to 0.75%. Some analysts believe the RBA might need to cut deeper than this, but we remain wary of becoming too pessimistic. There are positive factors supporting economic activity, including large plans for infrastructure spending, firm population growth and robust export growth.

The downturn in the housing market has been dragging on economic activity, including negative wealth effects on the consumer. But even with housing, the data is showing some promising signs that dwelling prices might be nearing a bottom in the key markets of Sydney and Melbourne. Rate cuts, the Federal election out of the way and proposed changes to the 'hard' servicing rate imposed by APRA should alleviate some of the pain still to come in the housing market.

GDP data on Wednesday should confirm that we have to wary of becoming too pessimistic on the economy and throwing the baby out with the bathwater. We are expecting GDP to show the Australian economy expanded by 0.6% in the March quarter. This is a solid rate of growth in the quarter. Data already released, including capex (last week) and business indicators (earlier today) leave us comfortable with this forecast. Tomorrow, the balance of payments and government finance statistics will give us more information. The partials for domestic demand in Q1 so far suggest that consumer spending was sluggish, residential housing construction fell further and business investment was mixed. Public demand and exports should be firm.

Consensus forecasts centre on GDP growth of 0.4% in the quarter and the range of estimates are 0.2%-0.6%. If our forecast of 0.6% is correct, annual growth will slow from 2.3% in the December quarter to 1.9%, the softest annual pace in six years. This annual pace remains below the long-run average and underpins our expectation the RBA needs to cut rates to provide some support to growth.

Also on Wednesday, retail sales for April will be published. We are expecting a soft outcome of only 0.2% growth, after a 0.3% gain in March. Consumers remain income constrained from the sluggish pace of wages growth and high household debt. The savings rate of households has declined in recent years, but can only fall so far. The vacancy rates in retail shopping centres and neighbourhood centres is elevated and incentives are high, reflecting the difficult trading conditions prevalent in retailing land.

On Thursday, we receive an update on the trade balance for April. The trade data has been a beacon of light in the economy. Commodity prices rose in the March quarter and remain elevated, underpinning national income growth. We are forecasting a trade surplus of \$5.4 billion in April, which would be the biggest on record. Such an outcome might help underpin demand for the Australian dollar, against a backdrop of increasing trade tensions and a fragile global growth outlook. The AUD/USD has remained somewhat resilient, despite expectations of a near-term RBA cut and the deterioration in trade tensions. Recently, speculation the US Federal Reserve might be open to cutting the federal funds target rate has caused the US dollar to sell off, giving support to AUD/USD.

Finally, on Friday, we receive an update on housing finance commitments for April.

Forecasts

End Period:	2019				2020			
	Close (May 31)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)	Q2 (f)	Q3 (f)	Q4 (f)
Aust. Interest Rates:								
RBA Cash Rate, %	1.50	1.25	1.00	0.75	0.75	0.75	0.75	0.75
90 Day BBSW, %	1.42	1.45	1.25	1.00	1.00	1.00	1.00	1.00
3 Year Swap, %	1.18	1.20	1.15	1.10	1.15	1.20	1.25	1.30
10 Year Bond, %	1.46	1.60	1.65	1.70	1.75	1.80	1.85	1.90
US Interest Rates:								
Fed Funds Rate, %	2.375	2.375	2.375	2.375	2.375	2.375	2.375	2.375
US 10 Year Bond, %	2.12	2.40	2.50	2.60	2.60	2.60	2.55	2.50
USD Exchange Rates:								
AUD-USD	0.6938	0.6900	0.6800	0.6600	0.6600	0.6700	0.6700	0.6800
USD-JPY	108.29	110.00	111.00	112.00	112.00	112.00	111.00	110.00
EUR-USD	1.1169	1.1100	1.1000	1.1000	1.1100	1.1200	1.1300	1.1400
GBP-USD	1.2629	1.2700	1.2800	1.2800	1.2800	1.2900	1.2900	1.3000
NZD-USD	0.6531	0.6500	0.6400	0.6500	0.6500	0.6600	0.6600	0.6700
AUD Exchange Rates:								
AUD-USD	0.6938	0.6900	0.6800	0.6600	0.6600	0.6700	0.6700	0.6800
AUD-EUR	0.6211	0.6220	0.6180	0.6000	0.5950	0.5980	0.5930	0.5960
AUD-JPY	75.12	75.90	75.50	73.90	73.90	75.00	74.40	74.80
AUD-GBP	0.5493	0.5430	0.5310	0.5160	0.5160	0.5190	0.5190	0.5230
AUD-NZD	1.0625	1.0200	1.0200	1.0200	1.0400	1.0200	1.0200	1.0100

	2018	2019 (f)	2020 (f)
GDP, %	2.3	2.2	2.5
CPI (Headline), %	1.8	1.8	1.6
CPI (Underlying), %	1.7	1.3	1.7
Unemployment Rate, %	5.0	5.4	5.6
Wages Growth, %	2.3	2.6	2.8

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

The Detail

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