

Monday, 7 February 2022

## Confidence Stabilising As Cases Drop?

Confidence is an important factor in an economy and supports growth. When consumers feel confident about the economic outlook, they are more inclined to get out and about and spend, take a risk by taking on that new job or starting that entrepreneurial venture, and help drive economic growth. Likewise, confident businesses are more likely to expand capacity to meet greater demand, invest in new products and services, and hire more people.

The spike in COVID-19 cases following the spread of the Omicron variant towards the end of 2021 and into January 2022 dented consumer and business confidence. This week, we will get an update on how businesses and consumers are feeling after case numbers peaked in mid January.

In December, business confidence plunged by 25 points to -12, its lowest level since May 2020. This was the sharpest monthly decline since March 2020 and was broad-based across the states. The sudden increase in case numbers contributed to labour shortages as workers were forced to isolate after contracting the virus or being a close contact. This resulted in many businesses having to temporarily close their doors or reduce opening hours. Businesses were also impacted by supply-chain disruptions due to worker shortages across the supply chain.

January data on business confidence and conditions is being released tomorrow. The survey is taken in the second half of the month, and so captures the period when case numbers began declining. As a result, confidence is likely to have improved modestly, consistent with the lift recorded in the weekly consumer confidence measure over the past two weeks. Indeed, our own customer liaison with businesses suggests that the mood has lifted since case numbers peaked in mid January.

Encouragingly, in the absence of lockdowns, the Omicron variant has had a smaller impact on spending than previous variants. High vaccination rates and a rollout of booster doses have helped reduce the health impact. However, there has been considerable temporary disruptions as millions of Australians were forced into isolation, exacerbating labour shortages and supply-chain disruptions. These temporary disruptions may have negatively impacted business conditions in January but are expected to ease, at least partly, as case numbers drop. Businesses have noted to us that staff shortages remain a major issue, beyond the temporary Omicron impacts. Staff turnover has risen due to increases in job switching as people take the opportunity to move to a higher paid role.

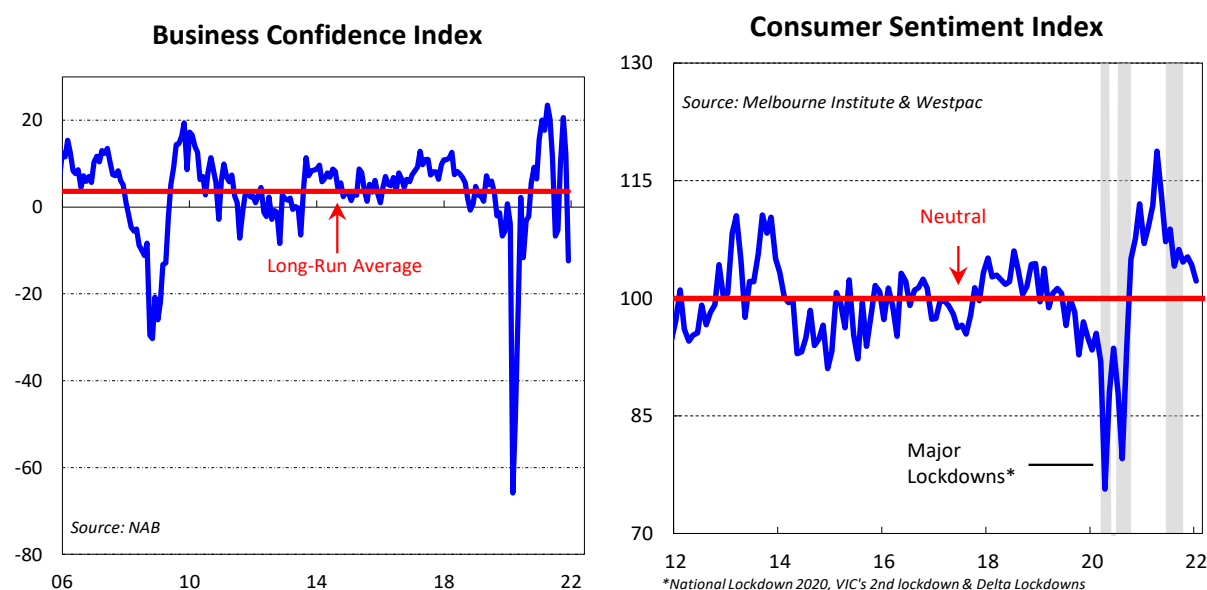
Supply-chain disruptions remain a significant issue for businesses, impacting product availability and contributing to high shipping costs. Additional concerns noted by businesses include price and interest rate pressures.

The monthly consumer sentiment series published by the Melbourne Institute and Westpac will be released on Wednesday. Despite falling in January, consumer sentiment remained resilient. The index fell 2.0% to 102.2, after a 1.0% dip in December. This was the lowest level since September 2020. Encouragingly, optimists continued to outweigh pessimists as the index remained above 100. The drop in sentiment was particularly evident in states that had not previously experienced

high infection levels, including Queensland, SA and WA.

In February, sentiment will be impacted by several factors. Falling case numbers after the peak in mid January and positive news around the less severe health impacts from Omicron will support sentiment. On the other hand, confidence may be negatively impacted by a shift in rhetoric from the Reserve Bank (RBA), as it slowly turns the ship and prepares for earlier than previously indicated rate hikes. This comes after stronger-than-expected inflation and labour market outcomes showed that the economy is progressing more quickly towards the RBA's goals of full employment and inflation being sustainably within the 2-3% band.

We expect a rate-hike cycle to begin in August. The economy is growing above trend as it recovers from the Delta lockdowns. Unemployment is expected to continue to fall and have a '3' at the front over 2022, and wage and inflationary pressures are likely to continue to build.



We also received updated retail sales volumes data for the December quarter of 2021 this morning. Delta-related lockdown restrictions were lifted across our two largest states during the December quarter. Pent-up demand was unleashed as consumers eagerly returned to their favourite shops and cafes and had long-overdue catch ups with family and friends. Retail sales volumes surged 8.2% over the quarter, the strongest quarterly growth on record, driven by a jump in discretionary spending. This follows a 4.4% fall in the September quarter. Sales volumes are now at their highest quarterly level in the history of the series. The strong result over the December quarter suggests that demand in the economy is very robust, indicating that there may be upside risks to growth in the March quarter of 2022.

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## Forecasts

End Period:	2022				2023		
	Close (4 Feb)	Q1 (f)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)	Q2 (f)
<b>Aust. Interest Rates:</b>							
RBA Cash Rate, %	0.10	0.10	0.10	0.25	0.50	0.75	1.00
90 Day BBSW, %	0.07	0.10	0.10	0.35	0.60	0.95	1.20
3 Year Swap, %	1.58	1.60	1.65	1.70	1.75	1.90	2.05
10 Year Bond, %	1.93	2.15	2.40	2.40	2.50	2.50	2.40
<b>US Interest Rates:</b>							
Fed Funds Rate, %	0.125	0.375	0.625	0.875	1.125	1.375	1.625
US 10 Year Bond, %	1.83	2.00	2.30	2.40	2.50	2.50	2.40
<b>USD Exchange Rates:</b>							
AUD-USD	0.7137	0.70	0.70	0.71	0.73	0.75	0.76
USD-JPY	114.97	116	116	117	117	118	118
EUR-USD	1.1438	1.10	1.08	1.09	1.10	1.11	1.12
GBP-USD	1.3597	1.36	1.37	1.38	1.38	1.37	1.37
NZD-USD	0.6662	0.65	0.65	0.66	0.68	0.69	0.70
<b>AUD Exchange Rates:</b>							
AUD-USD	0.7137	0.70	0.70	0.71	0.73	0.75	0.76
AUD-EUR	0.6240	0.64	0.65	0.65	0.66	0.68	0.68
AUD-JPY	82.054	81.2	81.2	83.1	85.4	88.5	89.7
AUD-GBP	0.5249	0.51	0.51	0.51	0.53	0.55	0.55
AUD-NZD	1.0715	1.08	1.08	1.08	1.08	1.09	1.09

	2020	2021 (f)	2022 (f)	2023 (f)
GDP, %	-0.8	3.2	5.5	2.7
CPI (Headline), %	0.9	3.5	3.1	2.8
CPI (Trimmed mean), %	1.2	2.6	2.8	2.8
Unemployment Rate, %	6.8	4.7	3.8	3.9
Wages Growth, %	1.4	2.3	3.2	3.5

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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