

Monday, 8 March 2021

Feeling Confident?

After last week's deluge of data, this week is almost a drought. But there will be two releases of note. Both focus on confidence.

Let's quickly digest last week. Economic growth was strong in the December quarter with GDP beating market expectations. House prices soared, as did home lending. The RBA kept rates on hold and promised to take action to curb rising bond yields. Building approvals pulled back but are well up on a year ago. And finally, retail sales grew while exports boomed. The economic recovery is well under way.

If the economy is going to grow sustainably it requires a lift in private business capital expenditure. This will occur as demand grows, capacity is absorbed and business owners grow in confidence.

On Tuesday, the NAB business survey for February will be released. Business confidence has grown with the index rising from a low of negative 65 in March 2020 to +10 in January. This is slightly above the long-run average level. There are no forecasts for business confidence but low interest rates, government incentives, the vaccine rollout and the relaxation of social distancing rules should at least maintain a positive outcome.

For demand to grow, consumers need to be confident. Confident about the security of their jobs, about their ability to move freely and about their finances.

On Wednesday, the Westpac / Melbourne Institute Index of Consumer Sentiment will be released. Consumer sentiment or consumer confidence was close to decade highs in February with an index reading of 109.1. Did the rollout of vaccines lift consumer confidence in March? Are consumers accepting that interest rates will stay low? Did the tens of thousands of jobs created in the past few months lift spirits? Were we encouraged by the surge in job ads? Are consumers nervous about the conclusion of JobKeeper?

The index of consumer sentiment captures the sum of these emotions and will itself add to our feelings of confidence or uncertainty depending upon the outcome.

Last week saw 10-year government bond yields rise. Growing optimism over a global economic recovery, further US fiscal stimulus and the abundance of cheap credit, has some investors fearing that inflation will emerge. We believe that, while there could be a temporary increase in inflation, a sustainable increase in inflation requires stronger growth in wages. Nevertheless, the lows in swap and bond yields are likely behind us.

In Australia, the US and Europe, unemployment is at levels that do not put upward pressure on wages. And, even as unemployment falls, there are other forces such as the adoption of technology and global competition that are likely to keep inflation subdued.

And what of the Australian dollar. Last week it briefly reached US 80 cents but fell back. Firm commodity prices, improving global growth and surging US debt suggest that US 80 cents will be regained and exceeded in the months ahead.

Forecasts

End Period:	2021				2022		
	Close (5 Mar)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)	Q2 (f)	Q3 (f)
Aust. Interest Rates:							
RBA Cash Rate, %	0.10	0.10	0.10	0.10	0.10	0.10	0.10
90 Day BBSW, %	0.03	0.02	0.02	0.02	0.04	0.06	0.08
3 Year Swap, %	0.34	0.30	0.30	0.30	0.30	0.18	0.22
10 Year Bond, %	1.83	1.85	1.85	1.90	2.05	2.20	2.35
US Interest Rates:							
Fed Funds Rate, %	0.13	0.125	0.125	0.125	0.125	0.125	0.125
US 10 Year Bond, %	1.56	1.65	1.70	1.80	1.95	2.10	2.25
USD Exchange Rates:							
AUD-USD	0.7686	0.79	0.80	0.82	0.85	0.85	0.84
USD-JPY	108.31	106	106	106	107	107	107
EUR-USD	1.1915	1.23	1.24	1.25	1.26	1.27	1.28
GBP-USD	1.3841	1.40	1.40	1.41	1.41	1.41	1.42
NZD-USD	0.7167	0.74	0.75	0.76	0.78	0.78	0.77
AUD Exchange Rates:							
AUD-USD	0.7686	0.79	0.80	0.82	0.85	0.85	0.84
AUD-EUR	0.6451	0.64	0.65	0.66	0.67	0.67	0.66
AUD-JPY	83.28	83.7	84.8	86.9	91.0	91.0	89.9
AUD-GBP	0.5554	0.56	0.57	0.58	0.60	0.60	0.59
AUD-NZD	1.0719	1.07	1.07	1.08	1.09	1.09	1.09

	2019	2020	2021 (f)	2022 (f)
GDP, %	2.2	-1.1	4.5	3.0
CPI (Headline), %	1.8	0.9	2.6	2.2
CPI (Trimmed mean), %	1.5	1.2	1.9	2.0
Unemployment Rate, %	5.2	6.8	6.0	5.3
Wages Growth, %	2.2	1.4	1.9	2.0

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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The Detail

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