Weekly Economic Outlook

Bank of Melbourne

Monday, 9 August 2021

Shifting Signposts

Uncertainty in the near term has increased. New South Wales recorded its highest ever number of daily infections on the weekend of over 300 on Saturday. The outbreak and lockdown measures have spread to the Hunter, Armidale and Tamworth regions of New South Wales. Victoria is also in lockdown and Queensland just emerged from its snap lockdown.

New South Wales is due to end its lockdown on 28 August. However, there remains a growing risk of an extension to the lockdown will be needed, especially as there are no convincing signs of a peak in daily infections yet. The seven-day moving average of daily infections in NSW hit a new record today.

Our forecasts have baked in a lockdown in Greater Sydney until the end of September.

However, the NSW government's signposts appear to be shifting. Previously, the NSW government appeared to be adopting an elimination strategy. That is, the message was that restrictions would not lift until the number of new cases not in full isolation was zero or as close to zero as possible.

Again in today's press conference, the NSW Premier suggested some restrictions would ease when 50% of NSW's population is fully vaccinated. The NSW government seems to be coming to the realisation that achieving zero community transmission with Delta could be challenging.

A 50% share seems low. It is unlikely to be enough to lift restrictions in a meaningful way based on the experience of other developed countries grappling with delta. Some major economies around the world are facing rising infections and tightening restrictions, despite having more than 50% of their population vaccinated.

Encouragingly, the rate of vaccinations is accelerating in Australia, as vaccines have become more available and as people become less reluctant about getting vaccinated. Supply issues of Pfizer have not fully vanished, however. Currently, around 22% of Australia's adult population is fully vaccinated.

What does it all mean for economic growth?

We expect economic growth nationally will contract by almost 3% in the September quarter and there will be a rebound in the December quarter. Previous lockdowns tell us that economic activity rebounds quickly once lockdowns lift. But the situation is evolving. This forecast profile relies on the NSW lockdown not lasting beyond September. It also relies on a limited spill over to other states and territories.

The ongoing rise in case numbers in NSW and the recent reimposition of lockdowns in Victoria and Queensland highlight the growing risk that the downturn in the September quarter will be deeper and the bounce back in the December quarter more muted.

We anticipate growth for 2021 in the low 3% range, down from our forecast of almost 5% before the outbreak began. It is a big slice to the forecast, but it is worth noting 3% is still a solid rate of growth.

The Reserve Bank (RBA) met last week and published its quarterly Statement on Monetary Policy. The RBA surprised markets and left the plan for tapering bond purchases unchanged. It has stuck to its plan to reduce the rate of bond purchases from September. We thought the near-term uncertainty would have led the RBA to delay the start date.

The RBA is looking through recent lockdowns as a temporary disruption to economic activity. However, the RBA also appears to be wearing rose-tinted glasses. The RBA is betting on growth of 4% this year. That seems too optimistic given the likely downturn in this September quarter and the growing risks that some of the economic activity in the December quarter will also be adversely impacted.

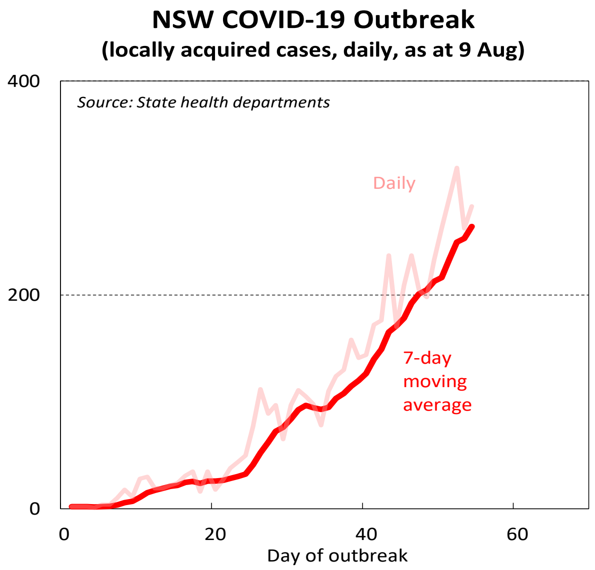
This week in Australia, data is thin on the ground. The two key pieces of data are updates on sentiment for businesses (tomorrow) and consumers (Wednesday).

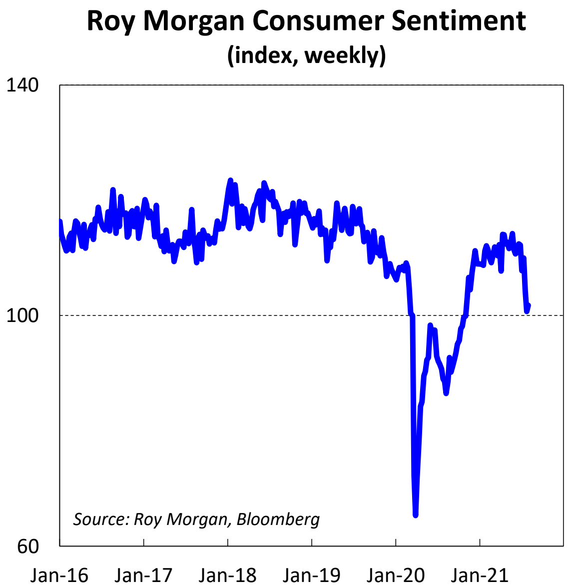
Anecdotes from our customers suggest that most businesses are cashed up and liquid, which is helping them navigate through the disruption from lockdowns. Some of smaller businesses are drawing on temporary support facilities, but so far customers have generally suggested this is more of a precautionary measure than out of necessity.

Business conditions and confidence indices will be released tomorrow with July data. During July, NSW was in lockdown and there were snap lockdowns in Victoria, South Australia and parts of Queensland.

Business conditions hit a record high in May at 35.8 but fell almost 12 index points in June to 24.1. Another fall in July is likely. Government support measures for businesses announced through July should help prevent a deeper decline in the index than otherwise would be the case.

The survey also has a business confidence index component. This gauge peaked in April. It has fallen nearly 55% since then but remains above zero at 10.7, suggesting businesses are still optimistic about the outlook.





Similar to the business survey, the monthly consumer sentiment survey published by the Melbourne Institute on Wednesday should show a decline in consumer confidence in August. In July, this index rose by 1.5%, but it follows a drop of almost 10% from the pandemic high of 118.8 in April. July's rise will likely prove to be no more than a dead-cat bounce; a resumption of the decline in consumer sentiment appears likely for August.

Indeed, the more frequent, weekly measure of consumer sentiment published by Roy Morgan shows a marked decline since the Melbourne Institute survey was last conducted in early July.

Like business sentiment, consumer sentiment has been hit hard but has come off very elevated levels, leaving more consumers still optimistic about the outlook (with the reading above 100.0).

Turning to the share market and half-year reporting also ramps up this week with over 30 ASX-listed companies due to report. The Australian share market has continued to hit fresh highs through July and August, despite the outbreak in New South Wales. Low interest rates, the vaccine roll out and fiscal stimulus are supporting the bottom line of companies and helping the share market move higher. However, the fears over the spread of the Delta variant offshore could cause global share markets to step back in the near term and that could flow onto Australia's share market.

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Forecasts

		2021		2022			
End Period:	**Close (6 August)**	**Q3 (f)**	**Q4 (f)**	**Q1 (f)**	**Q2 (f)**	**Q3 (f)**	**Q4 (f)**
Aust. Interest Rates:							
RBA Cash Rate, %	0.10	0.10	0.10	0.10	0.10	0.10	0.10
90 Day BBSW, %	0.01	0.04	0.07	0.10	0.15	0.20	0.40
3 Year Swap, %	0.43	0.50	0.55	0.70	0.80	0.95	1.10
10 Year Bond, %	1.18	1.55	1.80	1.95	2.00	2.05	2.10
US Interest Rates:							
Fed Funds Rate, %	0.125	0.125	0.125	0.125	0.125	0.125	0.375
US 10 Year Bond, %	1.23	1.60	1.80	1.95	2.00	2.05	2.10
USD Exchange Rates:							
AUD-USD	0.7396	0.75	0.78	0.80	0.82	0.82	0.82
USD-JPY	109.87	111	111	112	112	112	113
EUR-USD	1.1826	1.21	1.22	1.23	1.22	1.21	1.21
GBP-USD	1.3923	1.41	1.42	1.43	1.44	1.45	1.44
NZD-USD	0.7044	0.71	0.74	0.76	0.77	0.77	0.77
AUD Exchange Rates:							
AUD-USD	0.7396	0.75	0.78	0.80	0.82	0.82	0.82
AUD-EUR	0.6252	0.62	0.64	0.65	0.67	0.68	0.68
AUD-JPY	81.08	83.3	86.6	89.6	91.8	91.8	92.7
AUD-GBP	0.5303	0.53	0.55	0.56	0.57	0.57	0.57
AUD-NZD	1.0499	1.06	1.05	1.05	1.06	1.06	1.06

	2019	**2020**	**2021 (f)**	**2022 (f)**
GDP, %	2.1	-1.0	3.2	4.2
CPI (Headline), %	1.8	0.9	2.6	2.4
CPI (Trimmed mean), %	1.6	1.2	1.9	2.6
Unemployment Rate, %	5.2	6.8	5.1	4.0
Wages Growth, %	2.2	1.4	2.4	2.7

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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