

Monday, 9 December 2019

Turning to the Point

Last week's domestic data deluge contained little to cheer. Notably, there was no material evidence of the "gentle turning point" in economic growth predicted by the Reserve Bank (RBA). Consumers appear to be saving all of the income windfalls provided by tax breaks and RBA rate cuts, highlighting the limited impact of stimulus measures to date on the real economy.

GDP growth eased to 0.4% in the September quarter, its slowest pace in three quarters and below market expectations. Net exports and the government spending remained the crutches for the economy while weakness prevailed elsewhere.

The major source of disappointment was in household consumption, which rose just 0.1% in the September quarter. Given that one of the main transmission mechanisms of monetary policy is through the household sector, it suggests that monetary policy is yet to have a meaningful impact.

Other data for retail sales suggests that households are yet to respond to stimulus in the December quarter. Retail sales were flat in October, after recording soft growth of just 0.2% in the month before.

The RBA next meets in February next year, ample time for more evidence that the "long and variable lags of monetary policy" are taking effect. At this rate, it appears likely that the RBA's growth forecasts for 2019 have proven too optimistic, and further stimulus will be required. We expect two more rate cuts in February and June, at which point unconventional monetary policy will need to be seriously considered.

This week is relatively quiet, with the major data being the Westpac-Melbourne Institute consumer sentiment survey released on Wednesday. Consumer confidence has been soft, limiting the appetite of households to spend. So far, the reaction to the RBA's rate cuts has been in the wrong direction, with consumers seemingly spooked by record low interest rates and the prospect of worsening economic growth. December's reading will provide valuable insight into consumer confidence heading into the Christmas spending period, given the disappointing outturn for retail sales in October.

Other data to be released is the Australian Bureau of Statistics's (ABS) measure of house prices. House prices have been the one area in which the three rate cuts this year have had a clear impact, with a sharp recovery in housing prices in Sydney and Melbourne. In recent months, the increase in prices has begun to spread to other capital cities as well.

Abroad, the US Federal Open Market Committee (FOMC) will announce its interest rate decision on Thursday morning. Strong US labour market data, among other positive developments has meant that the market is pricing in a 0% chance of a further cut to the target rate. The UK heads to polls on Thursday, in a race to determine the future path of Brexit.

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Forecasts

End Period:	2019		2020			2021
	Close (Dec 2)	Q1 (f)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)
Aust. Interest Rates:						
RBA Cash Rate, %	0.75	0.50	0.25	0.25	0.25	0.25
90 Day BBSW, %	0.89	0.70	0.45	0.45	0.50	0.50
3 Year Swap, %	0.74	0.65	0.50	0.50	0.60	0.65
10 Year Bond, %	1.13	0.90	0.90	0.90	0.90	0.95
US Interest Rates:						
Fed Funds Rate, %	1.625	1.375	1.125	0.875	0.875	0.875
US 10 Year Bond, %	1.84	1.50	1.45	1.40	1.50	1.55
USD Exchange Rates:						
AUD-USD	0.6841	0.66	0.66	0.67	0.67	0.68
USD-JPY	108.58	107	106	105	105	106
EUR-USD	1.1060	1.09	1.10	1.11	1.12	1.13
GBP-USD	1.3140	1.33	1.32	1.32	1.31	1.31
NZD-USD	0.6566	0.62	0.62	0.63	0.63	0.64
AUD Exchange Rates:						
AUD-USD	0.6841	0.66	0.66	0.67	0.67	0.68
AUD-EUR	0.6185	0.61	0.60	0.60	0.60	0.60
AUD-JPY	74.27	70.6	70.0	70.4	70.4	72.1
AUD-GBP	0.5207	0.50	0.50	0.51	0.51	0.52
AUD-NZD	1.0419	1.06	1.06	1.06	1.06	1.06

	2018	2019 (f)	2020 (f)
GDP, %	2.1	2.1	2.1
CPI (Headline), %	1.8	1.7	1.9
CPI (Trimmed mean), %	1.8	1.6	1.9
Unemployment Rate, %	5.0	5.3	5.6
Wages Growth, %	2.4	2.5	2.5

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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