

# AUSTRALIAN MARKETS WEEKLY



## Unemployment & wages heading in right direction

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- Markets open this week to a hint of light on the trade war and tariff front. Trade talks between senior US and China officials are due to take place in Washington from this Wednesday. The press is reporting this is a precursor to talks between President Xi and President Trump in November.
- This has given markets some reason for optimism that a de-escalation of Sino-US trade tensions is possible one side or the other of November's US mid-term elections. The AUD/USD has opened this week just above 0.73, after testing close to 0.72 last week.
- On Friday, RBA Governor Lowe again reinforced his view that the next movement on Australian interest rates is more likely to be up, that he is sticking with his 2-3% inflation target, and that some further softness in the Australian dollar would be "helpful", commenting that the fall in the currency to date "hadn't been that much".
- Q2 Construction Work Done on Wednesday is the only Australian data release this week. This is one of the building blocks for Q2 GDP due Wednesday fortnight. NAB's expectation for Q2 GDP is 0.7%. Recent communications have revealed the RBA expects another solid quarter for growth (we can infer a 0.9% q/q outcome from their forecasts). There are several RBA speakers, Lowe tomorrow at an ASIC event and DeBelle speaking on Low Inflation in Brisbane on Wednesday. The RBA Board Minutes are also out tomorrow. Offshore most interest will be in the FOMC Minutes on Wednesday ahead of the annual Jackson Hole central bank symposium that gets underway on Thursday. Fed Chair Powell is scheduled to speak on Friday morning (Saturday AEST) on "Monetary policy in a changing economy".
- Last week provided an update on two variables of key importance to the RBA's monetary policy deliberations, namely wages and unemployment. Both at the margin surprised slightly favourably, the unemployment rate falling to a six-year low of 5.3%, while wages growth picked up very slightly to 2.1% y/y.
- The RBA Governor highlighted in his opening comments to a Parliamentary Committee that the RBA Board expects to remain on hold for a while yet, as it will be some time before unemployment is back to full employment (which the RBA currently puts at 5%) and inflation is sustainably back within the 2-3% target range.
- The course of the unemployment rate is important both in terms of achieving the RBA's aim of full employment and in helping lift wages growth somewhat, so that the RBA can be confident that inflation will return sustainably to the target range.
- Importantly, we note in recent months that growth in employment has begun to outpace growth in the labour force. This has allowed the unemployment rate to decline a little. Our previous work has shown that Net Overseas Migration has been an important explainer of the participation rate. The slowing in Net Overseas Migration in recent quarters suggests the unemployment rate may fall a little more quickly than the RBA expects.

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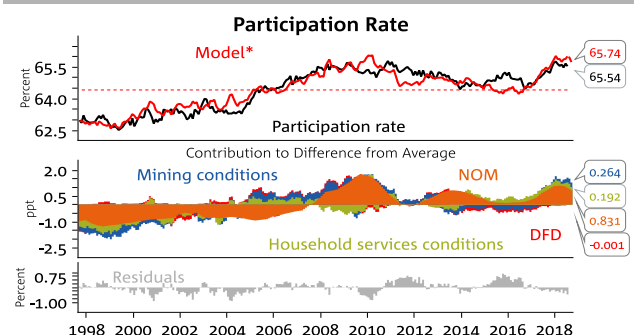
[Ask the Interest Rate Strategists](#)

### Key markets over the past week

	Last	% chg week		Last	bp / % chg week
AUD	0.7308	0.4	RBA cash	1.50	0
AUD/CNY	5.01	0.1	3y swap	2.08	-4
AUD/JPY	80.7	0.5	ASX 200	6,346	1.5
AUD/EUR	0.639	0.0	Iron ore	68.19	-0.5
AUD/NZD	1.103	-0.2	WTI oil	65.9	-2.0

Source: Bloomberg

### Model participation rate beginning to decline?

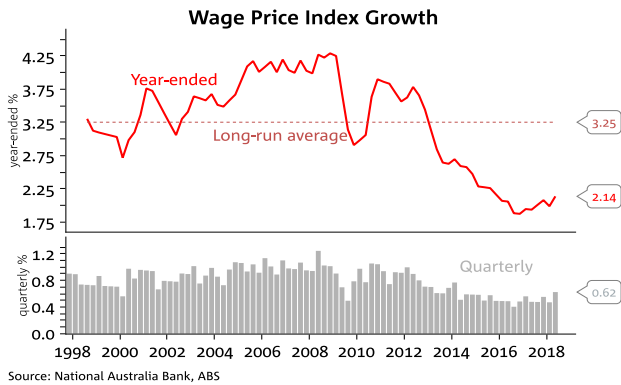


\* Model includes: 12mma net overseas migration; year-ended DFD growth; 3mma business conditions for mining and household services  
Source: National Australia Bank, ABS

### Unemployment and Wages Heading in the Right Direction

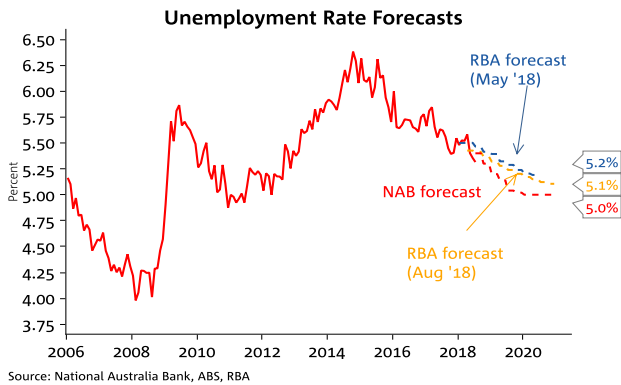
Last week’s data revealed the slightest improvement in annual wages growth to 2.1% y/y (from 2.0%) and a welcome further decline in the unemployment rate to a six-year low of 5.3% (from 5.4% in June). Progress on both of these fronts is important to the RBA. As Governor Lowe reminded the market Friday: “The Board’s view is that it is likely that we will hold steady for a while yet. It is likely to be some time before we are at full employment and the inflation rate is comfortably within the target range on a sustained basis”.

**Chart 1: Slight uptick in wages growth in Q2**



Source: National Australia Bank, ABS

**Chart 2: Unemployment rate lowest since 2012**



Source: National Australia Bank, ABS, RBA

While welcome, the data of recent quarters offers little hope of seeing wages growth back above 3% in the near term. Higher wages growth is likely needed before inflation is sustainably back within the RBA’s target range of 2 to 3%.

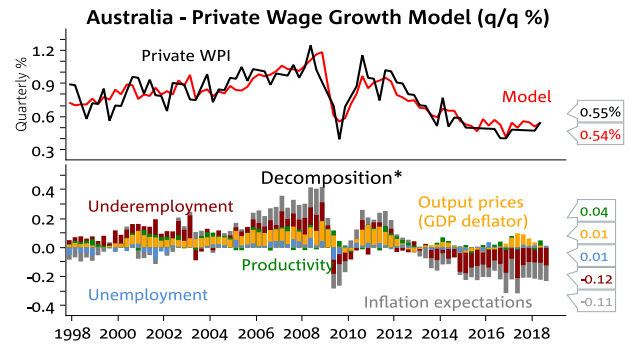
Such tepid growth in wages has been a global phenomenon and a concern for some time. A number of explanations have arisen to explain this new era of low wages growth, including: a post-GFC ‘wages hangover’, rising automation, an increasingly globalised workforce and declining unionisation.

Low wages growth has prompted some to claim the Phillips Curve is dead – ie. that wages no longer respond to low unemployment. Neither NAB, nor the RBA shares this view, though we would expect that these developments will likely constrain the degree of upside in wages as the labour market tightens.

As our previous research has shown, the course of the unemployment rate – and the underemployment rate –

along with inflation expectations, explain much of the slowdown in Australian wages in recent years (the terms of trade as reflected by the GDP deflator was also important during the mining boom). With inflation expectations remaining relatively low, this implicitly means that reductions in unemployment and underemployment are likely still to be the most likely sources of any uptick in wages growth.

**Chart 3: Underemployment needs to decline**

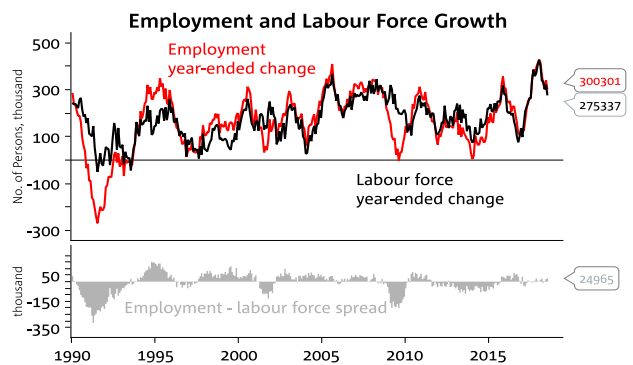


\* Decomposition excludes the constant term  
Source: National Australia Bank, ABS, IMF

### Supply: the participation rate may be peaking (for now)

The rising participation rate was a key reason that unemployment remained elevated over late 2017/early 2018. Importantly, in recent months, labour force growth has begun to slip behind employment growth, which has allowed the unemployment rate to decline in recent months.

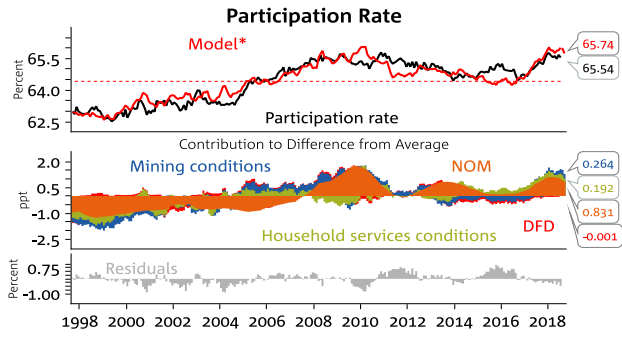
**Chart 4: Employment exceeding labour supply growth**



Source: National Australia Bank, ABS

Previous analysis by NAB has shown that a combination of cyclical and structural factors drove the rapid increase in the participation rate. These factors included cyclical conditions as reflected in Mining, Healthcare and Recreation and Personal Services business conditions, Net Overseas Migration and Domestic Final Demand. Importantly, Net Overseas Migration has begun to decline in recent quarters, reportedly as the Government has tightened up on visa processing. This is likely in part behind the slowing in the participation rate in recent times and holds out the prospect that the unemployment rate may fall more quickly than the RBA forecasts, if labour demand holds up. So far, both the NAB Survey Employment Question and SEEK Job Ads show labour demand remaining quite healthy.

Chart 5: Model participation rate starting to decline?



\* Model includes: 12mma net overseas migration; year-ended DFD growth; 3mma business conditions for mining and household services  
 Source: National Australia Bank, ABS

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# CALENDAR OF ECONOMIC RELEASES

Country	Economic Indicator	Period	Forecast	Consensus	Actual	Previous	GMT	AEST
<b>Monday, 20 August 2018</b>								
CA	Bank of Canada's Wilkins Speaks in Frankfurt						11.15	22.15
US	Fed's Bostic Speaks on U.S. Economic Outlook in Tennessee						14.00	1.00
<b>Tuesday, 21 August 2018</b>								
AU	RBA Governor Lowe speaks at ASIC's National Financial Capability Strategy 2018 event						21.00	8.00
NZ	Net Migration SA	Jul				4840	21.45	8.45
AU	RBA August Meeting Minutes						0.30	11.30
NZ	Credit Card Spending YoY	Jul				5.7	2.00	13.00
JN	Machine Tool Orders YoY	Jul F				13	5.00	16.00
UK	Public Sector Net Borrowing Ex Banking	Jul		-1.1		5.4	7.30	18.30
CA	Wholesale Trade Sales MoM	Jun		0.9		1.2	11.30	22.30
<b>Wednesday, 22 August 2018</b>								
NZ	Dairy Auction Avg. Winning Price MT	21 Aug	circa flat			3136	early am	
NZ	Retail Sales Ex Inflation QoQ	2Q	0.2	0.4		0.1	21.45	8.45
AU	Westpac Leading Index MoM	Jul				0.01	23.30	10.30
AU	Construction Work Done	2Q	0.8	0.8		0.2	0.30	11.30
AU	RBA's Debelle Speaks on Low Inflation at Economic Society event in Brisbane						2.10	13.10
JN	All Industry Activity Index MoM	Jun		-0.8		0.1	3.30	14.30
US	MBA Mortgage Applications	Aug-17				-2	10.00	21.00
CA	Retail Sales MoM / Ex Auto MoM	Jun		-0.2		2	11.30	22.30
US	FOMC Meeting Minutes						17.00	4.00
<b>Thursday, 23 August 2018</b>								
JN	Nikkei Japan PMI Mfg	Aug P				52.3	23.30	10.30
AU	RBA's Boulton Speaks on RBA's Government Banking Business at Business Banking Summit in Sydney						1.45	12.45
JN	Leading Index CI	Jun F				105.2	4.00	15.00
GE	Markit/BME Germany Manufacturing PMI	Aug P		56.5		56.9	6.30	17.30
GE	Markit Germany Services PMI	Aug P		54.3		54.1	6.30	17.30
EC	Markit Eurozone Manufacturing PMI	Aug P		55.2		55.1	7.00	18.00
US	Initial Jobless Claims	18 Aug		215		212	11.30	22.30
US	FHFA House Price Index MoM	Jun		0.3		0.2	12.00	23.00
US	Markit US Manufacturing PMI	Aug P		55		55.3	12.45	23.45
US	Markit US Services PMI	Aug P		56		56	12.45	23.45
US	New Home Sales	Jul		648		631	13.00	0.00
EC	Consumer Confidence	Aug A		-0.7		-0.6	13.00	0.00
US	Annual Jackson Hole Economic Policy Symposium starts: Changing Market Structure and Monetary Policy (Growth, Productivity, Techno							
<b>Friday, 24 August 2018</b>								
NZ	Trade Balance NZD	Jul	-426	-400		-113	21.45	8.45
JN	Natl CPI YoY / Ex Fresh Food YoY	Jul		1		0.7	22.30	9.30
GE	GDP SA QoQ/ YoY	2Q F		0.5/2		0.5/2	5.00	16.00
US	Durable Goods Orders	Jul P		-0.5		0.8	11.30	22.30
US	Cap Goods Orders Nondef Ex Air	Jul P		0.5		0.2	11.30	22.30
<b>Saturday, 25 August 2018</b>								
US	Fed's Powell discusses "Monetary policy in a changing economy" at Jackson Hole						15.00	2.00
<b>Upcoming Central Bank Interest Rate Announcements</b>								
Australia, RBA		4-Sep	1.5%	1.5%			1.5%	
Canada, BoC		5-Sep	1.5%	1.5%			1.5%	
Europe, ECB		13-Sep	-0.4%	-0.4%			-0.4%	
UK, BOE		13-Sep	0.75%	0.75%			0.75%	
Japan, BoJ		19-Sep	-0.1%	-0.1%			-0.1%	
US, Federal Reserve		26-Sep	2-2.25%	2-2.25%			1.75-2%	
New Zealand, RBNZ		27-Sep	1.75%	1.75%			1.75%	

GMT: Greenwich Mean Time; AEST: Australian Eastern Standard Time

# FORECASTS

		Annual % change				Quarterly % change												
		2017	2018	2019	2020	2017			2018			2019			2020			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	
<b>Australia Forecasts</b>																		
Household Consumption	2.7	2.6	2.4	2.4	0.3	1.0	0.6	1.0	0.3	0.7	0.5	0.6	0.6	0.6	0.7	0.6	0.6	0.7
Underlying Business Investment	3.0	3.2	5.8	6.0	3.1	0.0	3.7	-0.5	-0.1	2.1	0.0	1.1	2.1	1.3	1.8	1.5	1.3	1.8
Residential Construction	-2.2	-1.4	-2.6	0.4	-3.2	0.3	-2.1	-0.1	0.9	-1.1	-0.6	-0.7	-1.0	-0.5	-0.2	-0.2	0.2	0.3
Underlying Public Spending	4.5	4.8	4.3	4.5	1.0	1.3	1.4	1.2	1.5	0.8	0.9	1.0	1.1	1.1	1.1	1.1	1.1	1.1
Exports	3.5	4.2	4.7	2.5	-1.9	2.9	0.7	-1.5	2.4	0.9	1.7	1.0	1.4	1.3	0.7	0.6	0.5	0.6
Imports	7.8	4.1	4.2	5.3	3.1	-0.1	2.6	1.6	0.5	0.7	0.5	0.9	1.1	1.2	1.4	1.3	1.2	1.4
Net Exports (a)	-1.0	-0.1	0.0	-0.7	-1.1	0.6	-0.4	-0.7	0.3	0.0	-0.2	0.0	0.0	0.0	-0.2	-0.2	-0.2	-0.2
Inventories (a)	-0.1	0.0	-0.1	0.0	0.4	-0.5	0.1	0.0	0.2	-0.1	-0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Domestic Demand - qtr%					0.7	0.9	0.9	0.8	0.6	0.7	0.5	0.7	0.8	0.7	0.8	0.8	0.7	0.8
Dom Demand - ann %	3.0	2.8	2.8	3.2	2.3	2.6	3.6	3.3	3.2	3.0	2.6	2.5	2.6	2.6	3.0	3.1	3.1	3.2
Real GDP - qtr %					0.3	1.0	0.5	0.5	1.0	0.7	0.5	0.7	0.8	0.7	0.7	0.6	0.6	0.7
Real GDP - ann %	2.2	2.9	2.8	2.5	1.8	2.0	2.8	2.4	3.1	2.8	2.8	3.0	2.7	2.8	3.0	2.8	2.6	2.6
CPI headline - qtr %					0.5	0.2	0.6	0.6	0.4	0.4	0.6	0.5	0.5	0.4	0.6	0.7	0.6	0.6
CPI headline - ann %	1.9	2.0	2.0	2.6	2.1	1.9	1.8	1.9	1.9	2.1	2.0	1.9	2.0	2.0	2.0	2.2	2.3	2.5
CPI underlying - qtr %					0.4	0.6	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.6	0.6	0.7
CPI underlying - ann %	1.8	1.9	2.0	2.4	1.7	1.8	1.9	1.9	2.0	1.9	1.9	1.9	1.9	2.0	2.0	2.1	2.2	2.4
Wages (Pvte WPI - qtr %)					0.5	0.5	0.5	0.5	0.5	0.6	0.6	0.6	0.6	0.7	0.7	0.7	0.7	0.7
Wages (Pvte WPI - ann %)	1.8	2.1	2.5	2.7	1.8	1.8	1.9	1.9	1.9	2.0	2.1	2.2	2.4	2.5	2.5	2.6	2.6	2.7
Unemployment Rate (%)	5.6	5.5	5.1	5.0	5.9	5.6	5.4	5.4	5.5	5.5	5.4	5.4	5.3	5.1	5.0	5.0	5.0	4.9
Terms of trade	12.3	-0.9	-0.6	-0.1	5.4	-6.0	-0.1	0.4	3.3	-1.3	-3.1	-2.4	-0.4	-1.2	-0.9	0.2	-0.4	0.3
Annual % change (hide)					24.9	14.7	10.1	-0.7										
G&S trade balance, \$Abn	10.2	6.6	-14.5	-31.7	6.4	3.4	1.4	-1.0	4.1	3.0	1.0	-1.5	-1.7	-2.8	-4.6	-5.3	-6.6	-7.2
% of GDP	0.6	0.4	-0.7	-1.6	1.4	0.8	0.3	-0.2	0.9	0.6	0.2	-0.3	-0.4	-0.6	-0.9	-1.1	-1.3	-1.4
Current Account (% GDP)	-2.5	-2.8	-3.8	-4.6	-1.6	-2.4	-2.6	-3.2	-2.3	-2.5	-2.9	-3.4	-3.5	-3.7	-4.0	-4.2	-4.4	-4.5

Source: NAB Group Economics; (a) Contributions to GDP growth

## Exchange Rate Forecasts

	20-Aug	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19
<b>Majors</b>						
AUD/USD	0.7308	0.73	0.75	0.75	0.75	0.75
NZD/USD	0.6626	0.69	0.70	0.70	0.71	0.71
USD/JPY	110.46	109.0	110.0	108.0	106.0	104.0
EUR/USD	1.1438	1.15	1.18	1.22	1.22	1.25
GBP/USD	1.2752	1.32	1.38	1.45	1.47	1.53
USD/CHF	0.9950	1.02	1.00	0.98	0.98	0.97
USD/CAD	1.3061	1.32	1.28	1.26	1.25	1.25
USD/CNY	6.8775	6.50	6.40	6.30	6.23	6.23

<b>Australian Cross Rates</b>						
	20-Aug	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19
AUD/NZD	1.1029	1.06	1.07	1.07	1.06	1.06
AUD/JPY	80.7	80	83	81	80	78
AUD/EUR	0.6389	0.63	0.64	0.61	0.61	0.60
AUD/GBP	0.5731	0.55	0.54	0.52	0.51	0.49
AUD/CNY	5.0261	4.75	4.80	4.73	4.67	4.67
AUD/CAD	0.9545	0.96	0.96	0.95	0.94	0.94
AUD/CHF	0.7271	0.74	0.75	0.74	0.74	0.73

## Interest Rate Forecasts

	20-Aug	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19
<b>Australia Rates</b>						
RBA Cash rate	1.50	1.50	1.50	1.50	1.75	1.75
3 month bill rate	1.96	1.95	1.95	1.95	2.15	2.15
3 Year Swap Rate	2.09	2.15	2.35	2.50	2.80	3.00
10 Year Swap Rate	2.73	2.95	3.20	3.30	3.60	3.70
<b>Offshore Policy Rates</b>						
US Fed funds	2.00	2.25	2.50	2.75	3.00	3.25
ECB deposit rate	-0.40	-0.40	-0.40	-0.40	-0.40	-0.20
BoE repo rate	0.75	0.75	0.75	0.75	1.00	1.00
BoJ excess reserves rate	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
RBNZ OCR	1.75	1.75	1.75	1.75	2.00	2.25
China 1yr lending rate	4.35	4.35	4.35	4.35	4.35	4.35
China Reserve Ratio	15.5	16.0	16.0	16.0	16.0	16.0
<b>10-year Benchmark Bond Yields</b>						
Australia	2.54	2.80	3.00	3.05	3.30	3.40
United States	2.87	3.10	3.25	3.25	3.50	3.50
New Zealand	2.57	2.95	3.10	3.20	3.45	3.60

Sources: NAB Global Markets Research; Bloomberg; ABS

## Global GDP

Dec year	2015	2016	2017	2018	2019	2020	20 Yr Avg
Australia	2.5	2.6	2.2	2.9	2.9	2.6	3.4
US	2.9	1.5	2.3	2.8	2.3	1.7	2.6
Eurozone	2.1	1.8	2.6	2.1	2.0	1.8	1.5
UK	2.3	1.9	1.8	1.5	1.7	1.6	2.4
Japan	1.4	0.9	1.7	0.9	1.0	0.7	0.8
China	6.9	6.7	6.9	6.5	6.3	6.0	9.2
India	8.2	7.1	6.7	6.8	7.2	6.9	6.6
New Zealand	3.5	4.0	2.8	2.9	2.9	2.7	3.0
World	3.5	3.2	3.8	3.8	3.7	3.5	3.5
MTP Top 5	4.1	3.7	4.2	3.9	3.7	3.1	5.0

## Commodity prices (\$US)

	20-Aug	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19
Brent oil	65.9	74	72	70	68	67	68
Gold	1177	1310	1340	1360	1370	1380	1400
Iron ore	68.2	61	60	58	60	62	63
Hard coking coal	181	155	150	155	145	140	130
Thermal coal	118	90	93	85	80	75	77
Copper	5912	6725	6825	6875	6950	7050	6900
Aust LNG (*)	13.6	12.6	12.3	11.9	11.6	11.4	11.3

(\*) Implied Australian LNG export prices.

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