

AUSTRALIAN MARKETS WEEKLY

2018 Wrap and 2019 Thoughts



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- Last week, the global news flow dominated local markets with the drama of Brexit negotiations generating uncertainty, while Chinese monthly activity data and EZ Flash PMIs painted a relatively soft picture for global growth. These developments have caused further falls in equity markets in the US and Australia, and the \$A is trading back below US\$0.72 at the time of writing.
- As such, it's fitting that in today's Weekly – our last for 2018 – we cover these developments as we wrap up 2018, and look forward to 2019.
- Domestically, recent home loan approvals data was stronger-than-expected in October, with the number of loans for owner occupiers jumping 2.2% in the month. It's a sign that, perhaps, the decline in home loan approvals may be slowing – although we'll need a few more months of data before saying anything for certain. Special questions released in the latest *NAB Business Survey* suggest that businesses are less concerned about the impact of moderately lower house prices in Sydney and Melbourne housing than media reports would indicate. When asked about the key drivers of business conditions, only roughly 10% cited slowing housing prices, while around 55% cited consumer demand. 75% indicated no impact from slower house prices and only around 2% a significant impact.
- In the week ahead, besides today's just-released MYEFO (see your inbox shortly for our note, which shows the Australian budget continues to improve faster than expected), the RBA Minutes (Tuesday) and Labour force data (Thursday) are the focal points. NAB expects employment grew 20k in November and that the unemployment rate stayed at 5% (alongside an unchanged participation rate). For us, there's a risk that the unemployment rate could even tick down to 4.9% if the participation rate continues the oscillating pattern evident for the past six to eight months (and ticks down a little).
- Abroad, the Fed remains likely to implement a 25bp hike in policy rates on Wednesday (Thursday morning AEDT), unless equity markets become significantly more unsettled over the interim. Markets will be focused on the Fed's expectations for interest rates year (the so-called Fed dots), and whether they are lowered given markets now only price one rate hike in 2019 compared to the Fed's current dots of three hikes. It's likely the Fed will formally be more driven by developments in the date and remove the statement that "further gradual increases [in rates]" are likely to be required, from its post-meeting Statement.
- We wish all our readers a safe holiday period. Thank you for your support of NAB Research over the past year. Please send us an email with any suggestions about topics that you would like to see covered more in Australian Markets Weekly next year.

To contact NAB's market experts, please click on one of the following links:

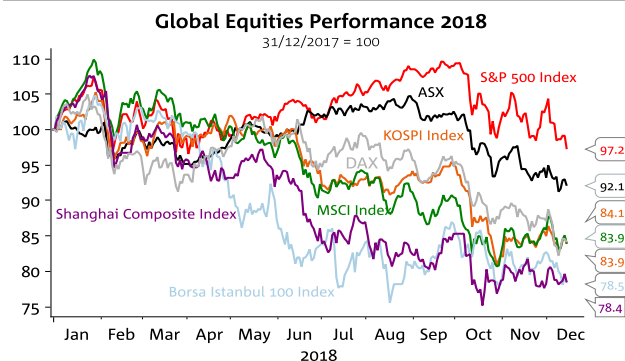
- [Ask the Economists](#)
- [Ask the FX Strategists](#)
- [Ask the Interest Rate Strategists](#)

Key markets over the past week

	Last	% chg week		Last	bp / % chg week
AUD	0.7172	-0.3	RBA cash	1.50	0
AUD/CNY	4.95	-0.4	3y swap	2.04	2
AUD/JPY	81.4	-0.2	ASX 200	5,600	0.9
AUD/EUR	0.634	0.2	Iron ore	68	5.1
AUD/NZD	1.056	0.9	WTI oil	51.4	0.8

Source: Bloomberg

Chart of the week: equities end weakly

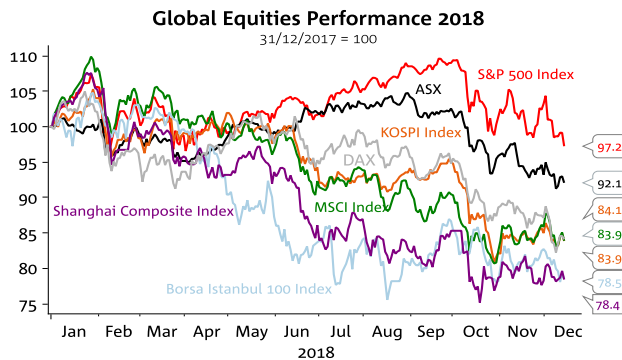


2018 Wrap and 2019 Thoughts

As the year draws to a close, our final Australian Markets Weekly looks back at some of the main developments in economies and markets this year, along with some thoughts on some of the key themes that will likely occupy markets in the early months of 2019.

The year ends with equity markets continuing to display significant volatility and weakness. As chart 1 shows, this was a year-long trend for emerging markets and European equity markets, with the S&P and Australian markets impacted more significantly later in the year.

Chart 1: Equity markets end the year weakly



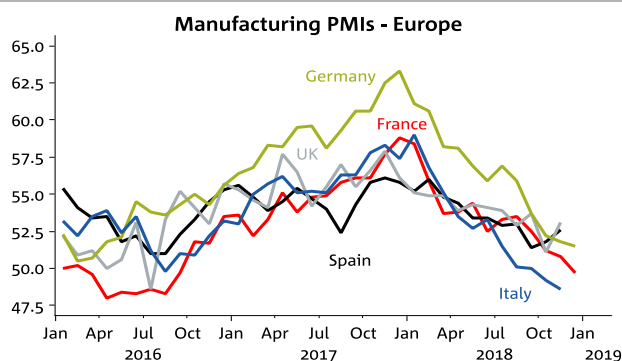
Source: National Australia Bank, Bloomberg

These developments seem to reflect two primary forces: (i) rising US interest rates; and (ii) signs of slower economic growth in Europe and China.

The Fed has lifted the Fed funds rate on three occasions so far this year and a further rate rise is widely expected later this week. These moves likely impacted emerging market and broader equities markets both via the valuation channel and via the impact on the outlook for growth and earnings in emerging markets, which are sensitive to movements in both US interest rates and the US\$, the latter moderately stronger as a result of a strong US economy and higher US interest rates.

Signs of slower European growth were evident throughout the year in the European Market Manufacturing PMI series. These were initially thought to reflect poor weather, then auto shutdowns, and also in part likely reflect continuing uncertainty around Brexit, Italy and Turkey.

Chart 2: Signs of slower European growth

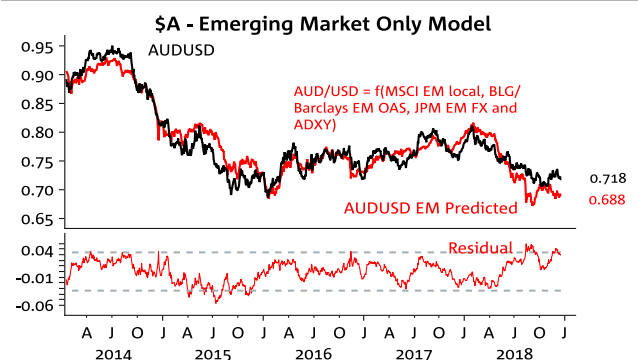


Source: National Australia Bank, Macrobond

Key monthly Chinese growth indicators: retail sales, fixed assets investment and retail sales have all suggested growth in the Chinese economy eased later in the year, in part likely reflecting the somewhat softer European outlook, but perhaps also some effects from the ongoing trade dispute between the US and China.

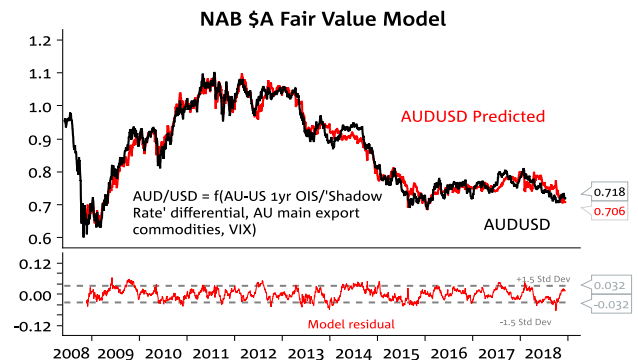
Signs of these developments have been evident in both Australian interest rate and currency markets. The \$A has broadly been tracking the weakness in emerging market equity and currency markets, despite important Australian commodity prices, for the most part remaining elevated. This has contributed to an emerging-market-based model of the \$A suggesting an even lower \$A, while NAB's traditional fair value model suggests a fair value of around \$US0.7050, still below the current trading level near US\$0.72.

Chart 3: \$A tracking emerging markets closely



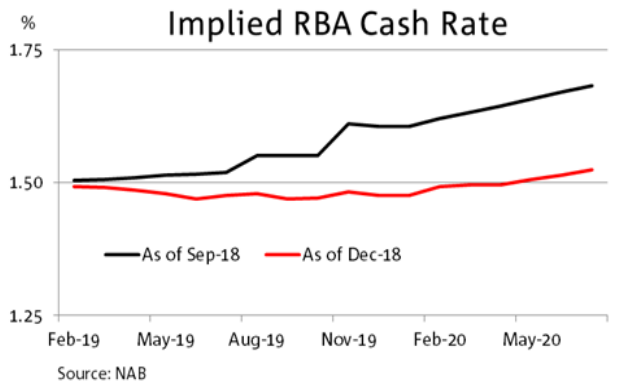
Source: National Australia Bank, Macrobond

Chart 4: Traditional NAB \$A fair value model



Source: National Australia Bank, Macrobond

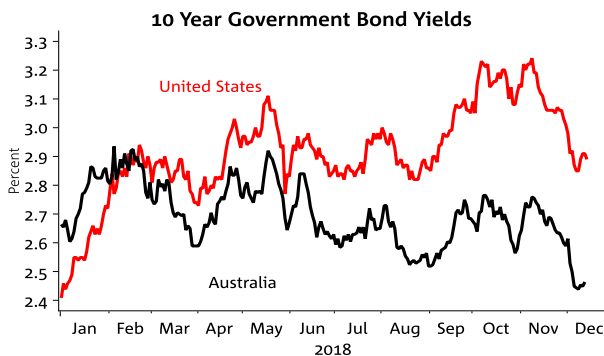
Chart 5: No change to cash rate expected for some time



Source: NAB

Interest rate markets for most of the year were pricing that the next move in interest rates by the RBA would be a hike, but not for some time. Markets have made some adjustment to that view recently and are now suggesting if there is a move in the next six or so months, it is more likely to be a rate cut, while still holding to the medium-term view that interest rates are more likely to increase.

Chart 6: Longer-dated borrowing costs drop recently



Looking ahead to 2019

Thinking about how next year will unfold, the continued moderation in a number of global growth indicators increases the risk that the US Federal Reserve is close to some sort of pause for US interest rates, especially as the level of interest rates nears neutral and US inflation shows few signs of moving significantly above the Fed's 2% target. NAB expects the Fed to become more data dependant, but still currently forecasts a further three rate rises next year. It would only take one Fed Governor to change their mind, to reduce the median expectation from three rate rises to two.

The short term outlook for expectations about growth – and for markets – is likely to continue to be driven by developments in equity markets. Like Australian housing markets, despite some weakness, the adjustment to date has been relatively orderly, though technical set-ups suggest that further equity market weakness lies ahead.

The major macro discussion points for the Australian economy continue to revolve around the housing market and the impact of tighter bank lending conditions. These are likely to be secondary in the medium-term, to developments in global growth, though are getting a lot of air time in the media at present.

NAB's view remains that the decline in Sydney and Melbourne prices remains orderly. And even though we expect some further price falls in both markets – especially in unit prices - these are not seen as having a major negative impact on the Australian economy, while unemployment and interest rates remain low.

Indeed, the declines so far, do not seem to have had a major impact on either consumer confidence or consumer spending (see last week's *Australian Markets Weekly* for a fuller discussion of these issues). The *NAB Business Survey for November* released last week also contained a number of special questions that interestingly revealed that house prices were well down the list of concerns for businesses reporting less strong business conditions, with three quarters of all businesses reporting no impact from lower house prices in Sydney or Melbourne.

NAB recently revised its RBA cash rate forecasts reflecting slower progress on wages growth than expected, despite unemployment falling faster than generally expected last year. That said, we still expect that the next move in interest rates will more likely be a rise, than a cut in interest rates, though we now do not expect that until the second half of 2020. On the \$A, we continue to see the currency trading mainly between US\$0.70 and US\$0.75, though the risk may be that it spends some time below US\$0.70, especially if equity market weakness continues in the near term.

Finally, thank you to all our regular readers of the Australian Markets Weekly. We're always happy to receive feedback on our products: what you'd like to see more of, what's particularly useful, what's not as useful, so feel free to drop us an email at one of the addresses below, if you've got any strong views.

The Australian Markets Weekly will return on Monday 14 January. The team at NAB Australian Economics wish you and your families a safe holiday season.

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CALENDAR OF ECONOMIC RELEASES

Country	Economic Indicator	Period	Forecast	Consensus	Actual	Previous	GMT	AEDT
Monday, 17 December 2018								
NZ	Performance Services Index	Nov				55.4	21.30	8.30
EC	Trade Balance SA	Oct		14		13.4	10.00	21.00
EC	CPI YoY	Nov F		2		2.2	10.00	21.00
US	Empire Manufacturing	Dec					13.00	0.00
US	Total Net TIC Flows	Oct				-29.1	21.00	8.00
Tuesday, 18 December 2018								
NZ	Dairy Auction Avg. Winning Price MT	43435				2819	early am	
NZ	ANZ Business Confidence	Dec				-37.1	0.00	11.00
AU	RBA Dec. Meeting Minutes						0.30	11.30
NZ	Non Resident Bond Holdings	Nov				57.1	2.00	13.00
GE	IFO Business Climate / Current Assessment	Dec		101.7/104.9		102/105.4	9.00	20.00
CA	Manufacturing Sales MoM	Oct		0.5		0.2	13.30	0.30
US	Housing Starts / Building Permits	Nov		1230/1260		1228/1263	13.30	0.30
Wednesday, 19 December 2018								
NZ	Westpac Consumer Confidence	4Q				103.5	20.00	7.00
NZ	BoP Current Account Balance NZD	3Q		-5.935		-1.619	21.45	8.45
AU	Westpac Leading Index MoM	Nov				0.08	23.30	10.30
JN	Trade Balance	Nov		-630		-449.257	23.50	10.50
UK	CPI MoM / YoY	Nov		0.2/2.3		0.1/2.4	9.30	20.30
UK	CPI Core YoY	Nov		1.8		1.9	9.30	20.30
UK	Retail Price Index MoM / YoY	Nov		0.1/3.2		0.1/3.3	9.30	20.30
UK	PPI Output NSA MoM / YoY	Nov		-0.1/3		0.3/3.3	9.30	20.30
US	MBA Mortgage Applications	14 Dec				1.6	12.00	23.00
CA	CPI NSA MoM / YoY	Nov		-0.4/1.8		0.3/2.4	13.30	0.30
CA	CPI Core- Trim YoY% / Median YoY%	Nov		/		2.1/2	13.30	0.30
CA	CPI Core- Common YoY%	Nov		1.9		1.9	13.30	0.30
US	FOMC Rate Decision	19 Dec	2.25/2.5	2.25/2.5		2/2.25	19.00	6.00
US	Interest Rate on Excess Reserves	20 Dec		2.4		2.2	19.00	6.00
US	Fed's Powell Holds Press Conference Following FOMC Decision						19.30	6.30
Thursday, 20 December 2018								
NZ	Trade Balance NZD	Nov		-880		-1295	21.45	8.45
NZ	GDP SA QoQ / YoY	3Q		0.6/		1/	21.45	8.45
AU	Employment Change / Unemployment Rate	Nov	20k / 5	20/5		32.8/5	0.30	11.30
AU	Participation Rate	Nov	65.6	65.6		65.6	0.30	11.30
NZ	Credit Card Spending YoY	Nov				6.3	2.00	13.00
JN	BOJ Policy Balance Rate	20 Dec	-0.1	-0.1		-0.1	around 2pm	
JN	All Industry Activity Index MoM	Oct		2		-0.9	4.30	15.30
JN	Machine Tool Orders YoY	Nov F				-16.8	6.00	17.00
UK	Retail Sales Inc Auto Fuel MoM / YoY	Nov		0.3/2		-0.5/2.2	9.30	20.30
UK	Bank of England Bank Rate	20 Dec	0.75	0.75		0.75	12.00	23.00
UK	BOE Asset Purchase Target	Dec		435		435	12.00	23.00
CA	Wholesale Trade Sales MoM	Oct		0.4		-0.5	13.30	0.30
US	Philadelphia Fed Business Outlook	Dec		15.5		12.9	13.30	0.30
US	Initial Jobless Claims	15 Dec		219		206	13.30	0.30
US	Leading Index	Nov					13.00	0.00
Friday, 21 December 2018								
NZ	ANZ Consumer Confidence Index	Dec				118.6	21.00	8.00
JN	Natl CPI YoY	Nov		0.8		1.4	23.30	10.30
JN	Natl CPI Ex Fresh Food YoY	Nov		1		1	23.30	10.30
JN	BOJ 3Q Money Flow						23.50	10.50
GE	GfK Consumer Confidence	Jan		10.3		10.4	7.00	18.00
UK	Public Sector Net Borrowing ex Banking Groups	Nov		7.7/7		8.8/8	9.30	20.30
UK	GDP QoQ / YoY	3Q F		0.6		0.6	9.30	20.30
Upcoming Central Bank Interest Rate Announcements								
US, Federal Reserve		19-Dec	2.25-2.5%	2.25-2.5%		2-2.25%		
UK, BOE		20-Dec	0.75%	0.75%		0.75%		
Japan, BoJ		20-Dec	-0.1%	-0.1%		-0.1%		
Canada, BoC		9-Jan	2%	2%		1.75%		
Europe, ECB		24-Jan	-0.4%	-0.4%		-0.4%		
Australia, RBA		5-Feb	1.5%	1.5%		1.5%		
New Zealand, RBNZ		13-Feb	1.75%	1.75%		1.75%		

GMT: Greenwich Mean Time; AEDT: Australian Eastern Daylight Savings Time

FORECASTS

		Annual % change				Quarterly % change															
		2017	2018	2019	2020	2017				2018				2019				2020			
Australia Forecasts						Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Household Consumption	2.4	2.5	2.3	2.5	0.4	0.8	0.6	1.1	0.3	0.9	0.3	0.5	0.7	0.6	0.7	0.6	0.6	0.6	0.6	0.7	0.7
Underlying Business Investment	3.7	1.9	3.2	5.1	3.3	0.3	3.7	0.4	0.8	-0.8	-1.1	0.2	1.7	1.1	1.8	1.3	1.1	1.5	0.8	1.0	1.0
Residential Construction	-2.4	4.7	-7.7	-8.6	-3.8	0.2	-1.3	0.3	3.8	1.9	1.0	-2.5	-2.6	-3.1	-2.9	-2.3	-2.2	-1.9	-2.0	-0.9	-0.9
Underlying Public Spending	4.5	4.3	4.1	4.5	1.1	1.4	1.0	1.1	1.4	0.5	1.5	0.6	1.0	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
Exports	3.5	5.4	4.0	2.8	-1.9	2.8	0.8	-1.5	4.3	1.2	0.1	0.7	1.5	1.4	0.8	0.7	0.6	0.7	0.5	0.8	0.8
Imports	7.7	3.8	1.7	3.7	3.0	0.2	3.3	0.6	1.9	0.5	-1.5	0.3	0.8	0.7	1.0	0.8	0.8	1.0	0.9	1.1	1.1
Net Exports (a)	-0.8	0.4	0.5	-0.2	-1.0	0.5	-0.5	-0.5	0.5	0.2	0.3	0.1	0.2	0.2	0.0	0.0	0.0	-0.1	-0.1	-0.1	-0.1
Inventories (a)	-0.1	0.1	-0.1	0.0	0.4	-0.7	0.3	0.1	0.1	0.1	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic Demand - qtr%					0.7	0.9	0.8	0.8	0.8	0.7	0.3	0.4	0.6	0.5	0.7	0.6	0.6	0.7	0.6	0.7	0.6
Dom Demand - ann %	2.9	2.9	2.1	2.5	2.2	2.5	3.5	3.2	3.4	3.2	2.7	2.2	2.0	1.8	2.2	2.4	2.3	2.5	2.5	2.6	2.6
Real GDP - qtr %					0.4	0.8	0.6	0.5	1.0	0.9	0.3	0.5	0.8	0.6	0.6	0.5	0.5	0.6	0.5	0.7	0.7
Real GDP - ann %	2.4	2.9	2.4	2.3	2.2	2.1	2.8	2.4	3.0	3.1	2.8	2.7	2.4	2.2	2.6	2.6	2.3	2.3	2.2	2.3	2.3
CPI headline - qtr %					0.5	0.2	0.6	0.6	0.4	0.4	0.4	1.0	0.6	0.4	0.4	0.8	0.5	0.6	0.6	0.6	0.7
CPI headline - ann %	1.9	2.0	2.4	2.4	2.1	1.9	1.8	1.9	1.9	2.1	1.9	2.2	2.4	2.4	2.4	2.2	2.1	2.3	2.5	2.5	2.5
CPI underlying - qtr %					0.5	0.6	0.3	0.5	0.5	0.4	0.3	0.5	0.5	0.5	0.5	0.6	0.6	0.6	0.6	0.6	0.6
CPI underlying - ann %	1.9	1.8	2.0	2.3	1.7	1.9	1.9	1.9	2.0	1.8	1.7	1.8	1.8	1.9	2.1	2.1	2.1	2.2	2.3	2.3	2.3
Wages (Pvte WPI - qtr %)					0.5	0.5	0.5	0.5	0.6	0.5	0.5	0.6	0.6	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7
Wages (Pvte WPI - ann %)	1.9	2.1	2.5	2.7	1.8	1.8	1.9	1.9	2.0	2.1	2.1	2.3	2.3	2.4	2.5	2.6	2.6	2.7	2.7	2.8	2.8
Unemployment Rate (%)	5.6	5.3	4.8	4.8	5.9	5.6	5.5	5.4	5.5	5.6	5.1	4.9	4.8	4.7	4.8	4.7	4.8	4.7	4.8	4.8	4.8
Terms of trade	12.1	-0.1	-0.7	0.0	5.3	-5.9	-0.1	-0.1	3.1	-1.1	0.9	-3.4	-0.8	-1.2	-0.9	0.3	-0.4	0.3	-0.4	0.2	0.2
G&S trade balance, \$Abn	9.6	18.0	8.7	1.8	6.7	3.3	0.9	-1.2	4.2	3.9	6.6	3.3	3.2	2.6	1.4	1.5	0.9	0.9	0.1	0.0	0.0
% of GDP	0.5	1.0	0.4	0.1	1.5	0.7	0.2	-0.3	0.9	0.8	1.4	0.7	0.7	0.5	0.3	0.3	0.2	0.2	0.0	0.0	0.0
Current Account (% GDP)	-2.6	-2.5	-3.1	-3.5	-1.6	-2.4	-2.9	-3.4	-2.3	-2.6	-2.2	-2.9	-2.9	-3.1	-3.3	-3.3	-3.4	-3.4	-3.5	-3.5	-3.5

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

Exchange Rate Forecasts					
	17-Dec	Mar-19	Jun-19	Sep-19	Dec-19
Majors					
AUD/USD	0.7174	0.71	0.70	0.73	0.75
NZD/USD	0.6788	0.68	0.67	0.69	0.70
USD/JPY	113.49	113	113	110	108
EUR/USD	1.1308	1.17	1.18	1.20	1.23
GBP/USD	1.2580	1.35	1.40	1.43	1.45
USD/CHF	0.9979	0.98	0.98	0.99	0.97
USD/CAD	1.3384	1.31	1.31	1.27	1.27
USD/CNY	6.9004	7.10	7.20	7.20	7.15

Australian Cross Rates					
	17-Dec	Mar-19	Jun-19	Sep-19	Dec-19
AUD/NZD	1.0569	1.04	1.04	1.06	1.07
AUD/JPY	81.4	80	79	80	81
AUD/EUR	0.6344	0.61	0.59	0.61	0.61
AUD/GBP	0.5703	0.53	0.50	0.51	0.52
AUD/CNY	4.9503	5.04	5.04	5.26	5.36
AUD/CAD	0.9602	0.93	0.92	0.93	0.95
AUD/CHF	0.7159	0.70	0.69	0.72	0.73

Interest Rate Forecasts					
	17-Dec	Mar-19	Jun-19	Sep-19	Dec-19
Australia Rates					
RBA Cash rate	1.50	1.50	1.75	1.75	2.00
3 month bill rate	2.02	1.95	1.90	1.90	1.90
3 Year Swap Rate	2.04	2.15	2.15	2.20	2.15
10 Year Swap Rate	2.66	2.90	2.95	2.95	2.90
Offshore Policy Rates					
US Fed funds	2.25	2.75	3.00	3.25	3.25
ECB deposit rate	-0.40	-0.40	-0.40	-0.20	0.00
BoE repo rate	0.75	0.75	1.00	1.00	1.25
BoJ excess reserves rate	-0.10	-0.10	-0.10	-0.10	-0.10
RBNZ OCR	1.75	1.75	1.75	1.75	2.00
China 1yr lending rate	4.35	4.35	4.35	4.35	4.35
China Reserve Ratio	14.5	16.0	16.0	16.0	16.0
10-year Benchmark Bond Yields					
Australia	2.44	3.05	3.30	3.40	3.50
United States	2.89	3.25	3.50	3.50	3.50
New Zealand	2.48	2.85	3.10	3.20	3.30

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	2.4	2.9	2.4	2.3	3.4
US	2.9	1.6	2.2	2.9	2.3	1.6	2.6
Eurozone	2.0	1.9	2.5	1.9	1.7	1.6	1.5
UK	2.3	1.8	1.7	1.3	1.7	1.5	2.4
Japan	1.4	1.0	1.7	0.9	1.2	0.9	0.8
China	6.9	6.7	6.9	6.6	6.3	6.0	9.2
India	8.2	7.1	6.7	7.3	7.1	7.2	6.6
New Zealand	3.5	4.0	2.8	2.9	2.8	2.6	3.0
World	3.5	3.3	3.7	3.7	3.6	3.5	3.5
MTP Top 5	4.1	3.8	4.2	4.0	3.8	3.4	5.0

Commodity prices (\$US)					
	17-Dec	Mar-19	Jun-19	Sep-19	Dec-19
Brent oil	60.1	85	80	77	78
Gold	1237	1276	1297	1305	1318
Iron ore	68.7	63	60	61	62
Hard coking coal	226	180	175	160	165
Thermal coal	102	105	103	101	100
Copper	6129	6350	6500	6600	6700
Aust LNG (*)	15.6	14.3	14.6	13.4	13.0

(*) Implied Australian LNG export prices.

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