Global Overview
&
Australia

Impact of COVID-19 in near and medium term.

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Date: September 2021

Global - *Macroeconomic summary.*

- **COVID-19 continues to be the main driver of growth – both in the recovery phase and as the Delta variant spreads. With vaccines looking promising 2021 looks like being a bounce back year.** 2022 likely to be above average. 2023 trend growth.

- In the **US** huge fiscal stimulus has seen very strong growth in the first half of 2021 – which we expect to continue into the second half – bringing growth up to 6.2% in 2021 and around 4.3% in 2022. **The combination of stimulus and supply shortages have seen very strong increases in wage and price pressures. The Fed thinks this is temporary and recent data supports this.** We expect the Fed to announce tapering intentions in November (subject to reasonable Payrolls in October) and actual tapering in late 2021 or early 2022. Rate rises are probably 12 months beyond that.

- **China** was one of the few economies to grow in 2021. Lots of stimulus that is now being withdrawn. Growth easily above 6% target. In 2021 more like 8.5%. But recently the virus has returned and the economy may slow significantly if lockdowns continue. Evergrande a new issue – but probably wont see Government action unless threatens systemic issues

- Growth in **Europe, UK appear to have bounced back significantly. Japan is more a concern but we expect a better second half in 2021 and into 2022**.

- Developing world hard hit by the virus (eg India and Indonesia).

- **Other theme globally is the return of inflation from supply-side problems (and stimulu Markets v the Fed and other central banks.**

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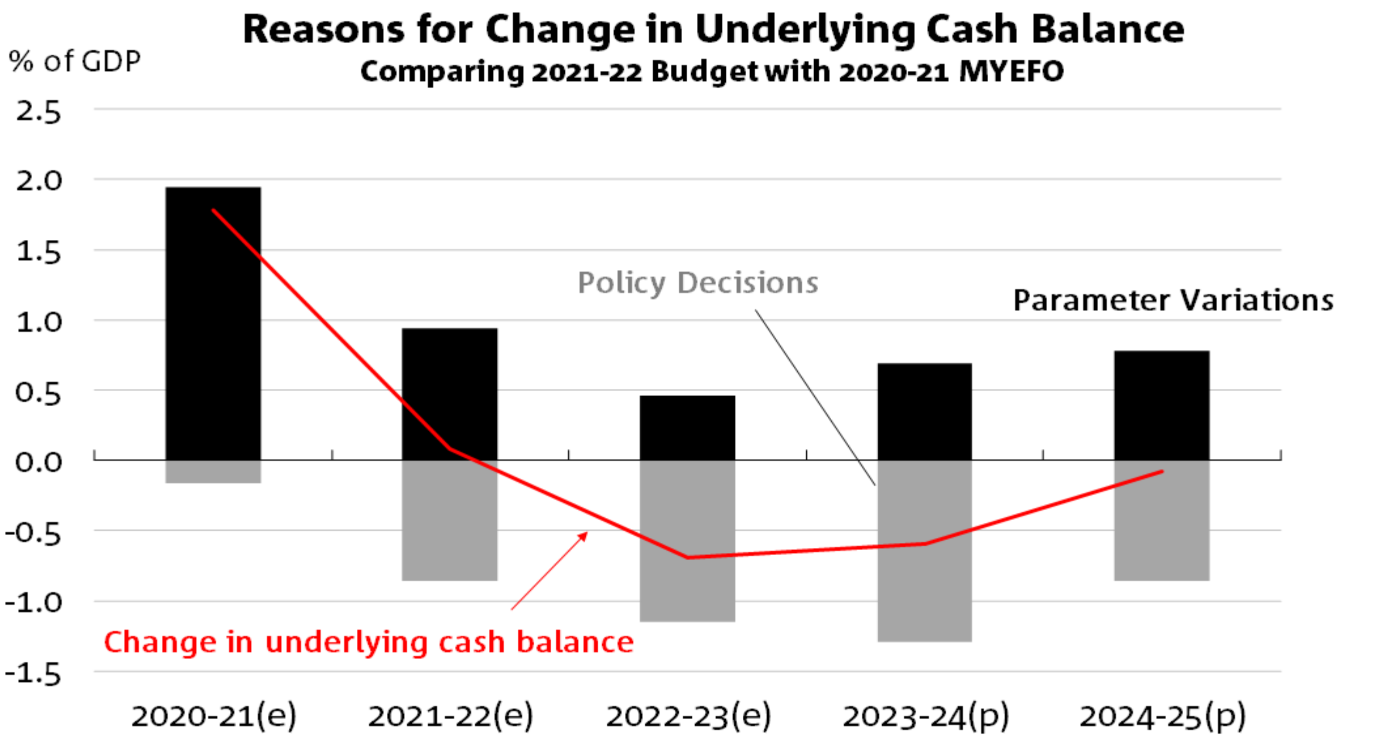
Global economic forecasts.

	2019	2020	2021	2022	2023
US	2.3	-3.4	6.0	4.1	2.1
Euro-zone	1.5	-6.5	5.2	4.0	2.1
Japan	0.0	-4.7	2.6	3.3	1.0
UK	1.4	-9.8	7.1	6.1	2.3
Canada	1.9	-5.3	5.5	4.0	2.5
China	6.0	2.3	8.7	5.9	5.7
India	4.8	-7.0	8.0	6.8	5.6
Latin America	0.1	-6.7	5.8	2.4	1.7
Other East Asia	3.5	-2.9	4.8	4.8	4.7
Australia	1.9	-2.4	3.4	3.0	2.2
NZ	2.4	-2.9	3.5	4.2	1.9
Global	**2.8**	**-3.3**	**6.0**	**4.6**	**3.5**

Australia - *Macroeconomic summary.*

- **Domestic growth obviously has been very sensitive to the virus and lockdowns. Typically lockdowns see consumption fall by around 15%. Now likely to see negative growth in Q3 (down around -3.5% in the quarter) and the recovery very driven by the timing of reversal of lockdowns. But H2 of 2020 likely to be negative even with a bounce in Q4 2020.**
- **Last 12 months however shows once lockdown ceases, recovery snaps back quickly.**
- **The last 12 months also shows the effectiveness of fiscal policy. And the Government is spending a lot. And more is likely in the election.**

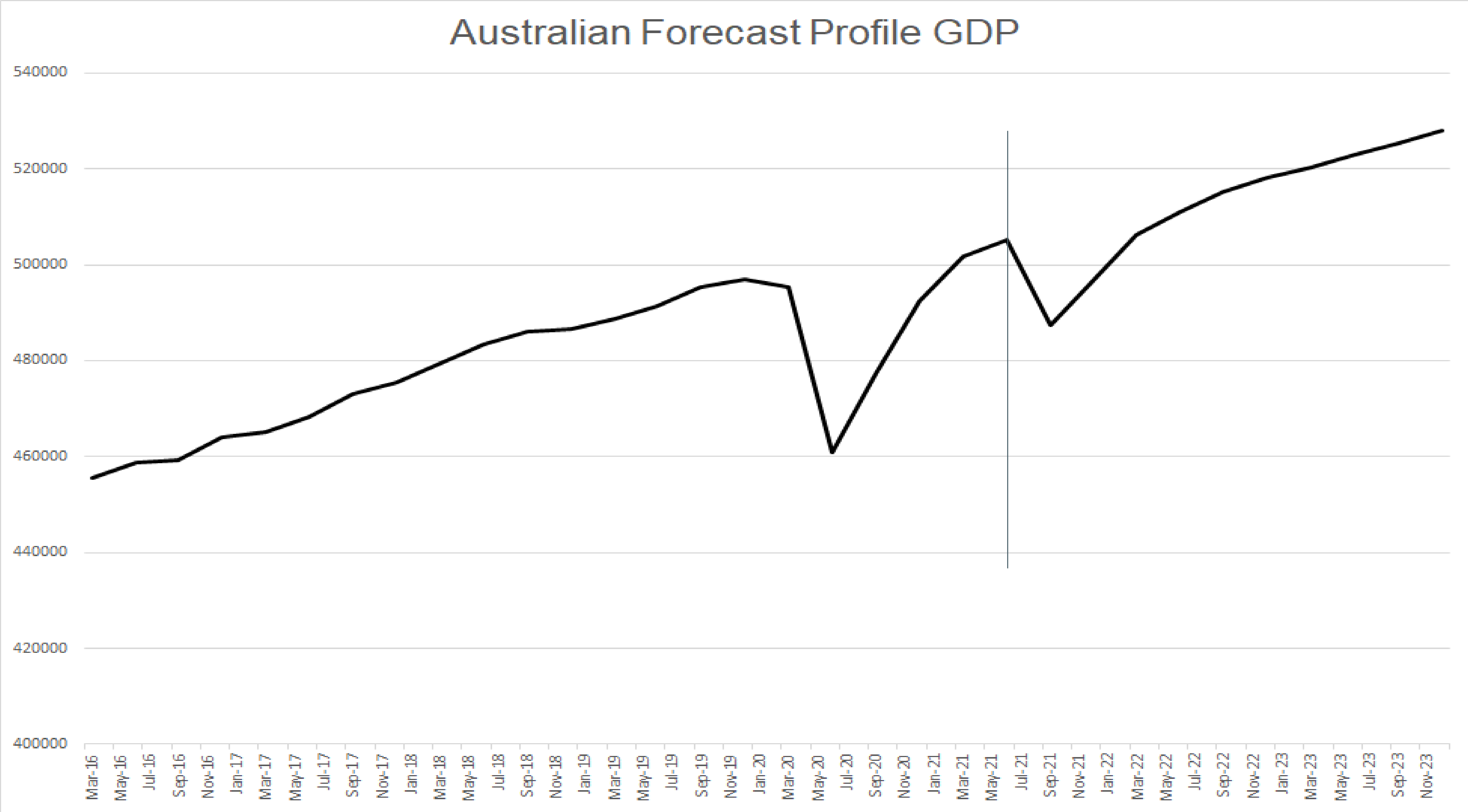


Source: Commonwealth Treasury, NAB calculations

Australia - *Macroeconomic summary (continued)*

- **Overall, we see:**
  - **Growth has been significantly hit by the most recent lockdowns. We now expect a fall in Q3 GDP of around -3.5% after modest growth in Q2. Provided restrictions ease by mid October then Q4 can come back strongly. But that is clearly a risk – which would put the bounce back into Q1. But looks like second half of 2021 will be negative.**
  - **That would see growth of around 1.0% through 2021. A lockdown result. Unemployment could rise to around 51/4 % by year end or early 2022.**
  - **For 2022 we see growth accelerating and implies growth of around 4% in 2022 or nearly 4.8% through the year. Unemployment would then be around 4.5%.**
  - **Not much change is expected to the forecasts for 2023 – growth of around 2¼% and unemployment around 4%.**
  - **Fundamentally the recovery path is consumption post the lockdowns but investment in dwellings (building houses) and manufacturing (eg. whitegoods) are accelerating as is plant and equipment investment.**
  - **Wages and prices forecasts not much changed. That is, core inflation at 2¼% by end 2023 and wages approaching 3%. So, we still have rate increases scheduled for early 2024.**
  - **Budget very stimulatory and an election package still to go.**

Australian growth path. – *Now above end 2019 levels.*



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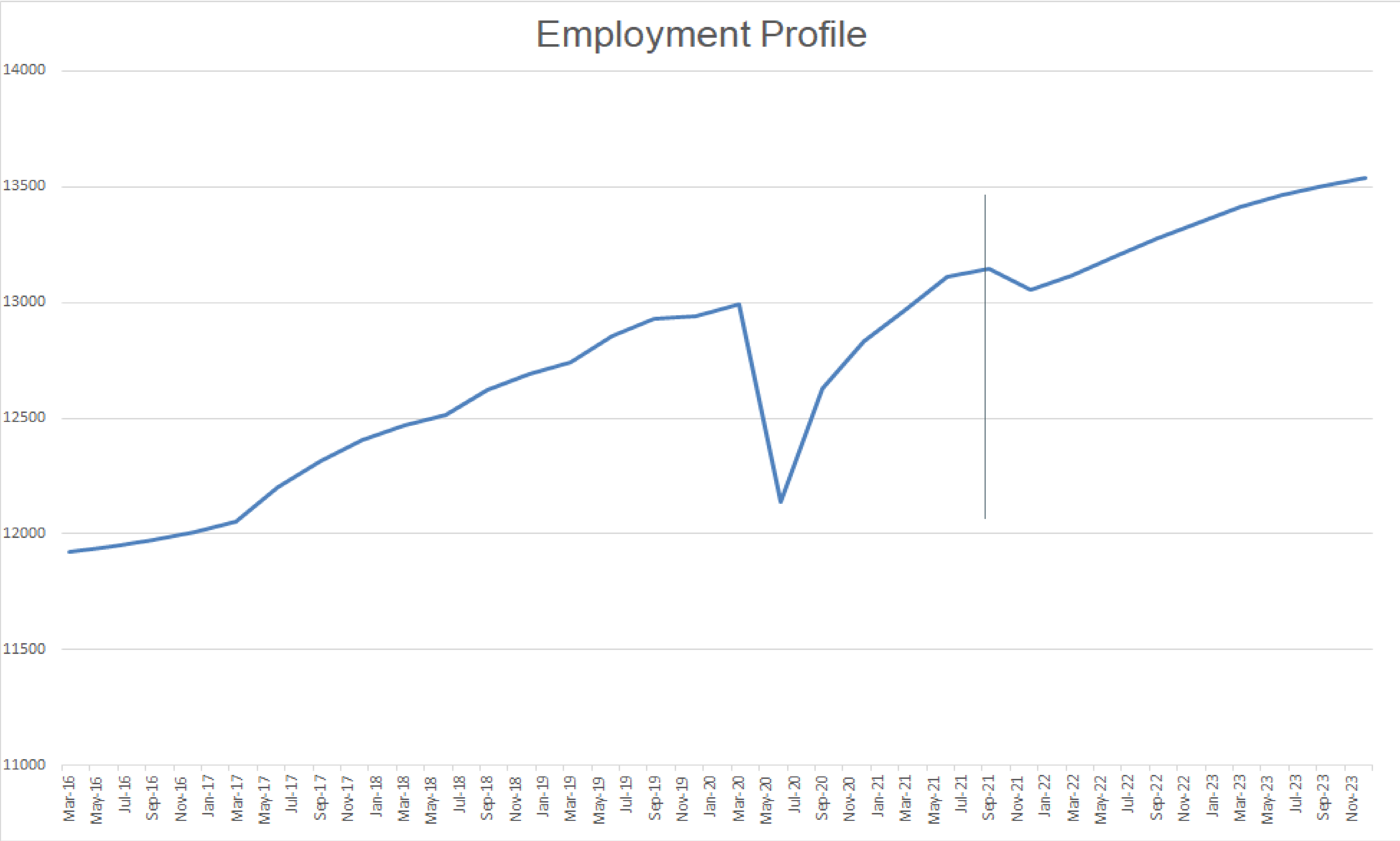
Employment profile



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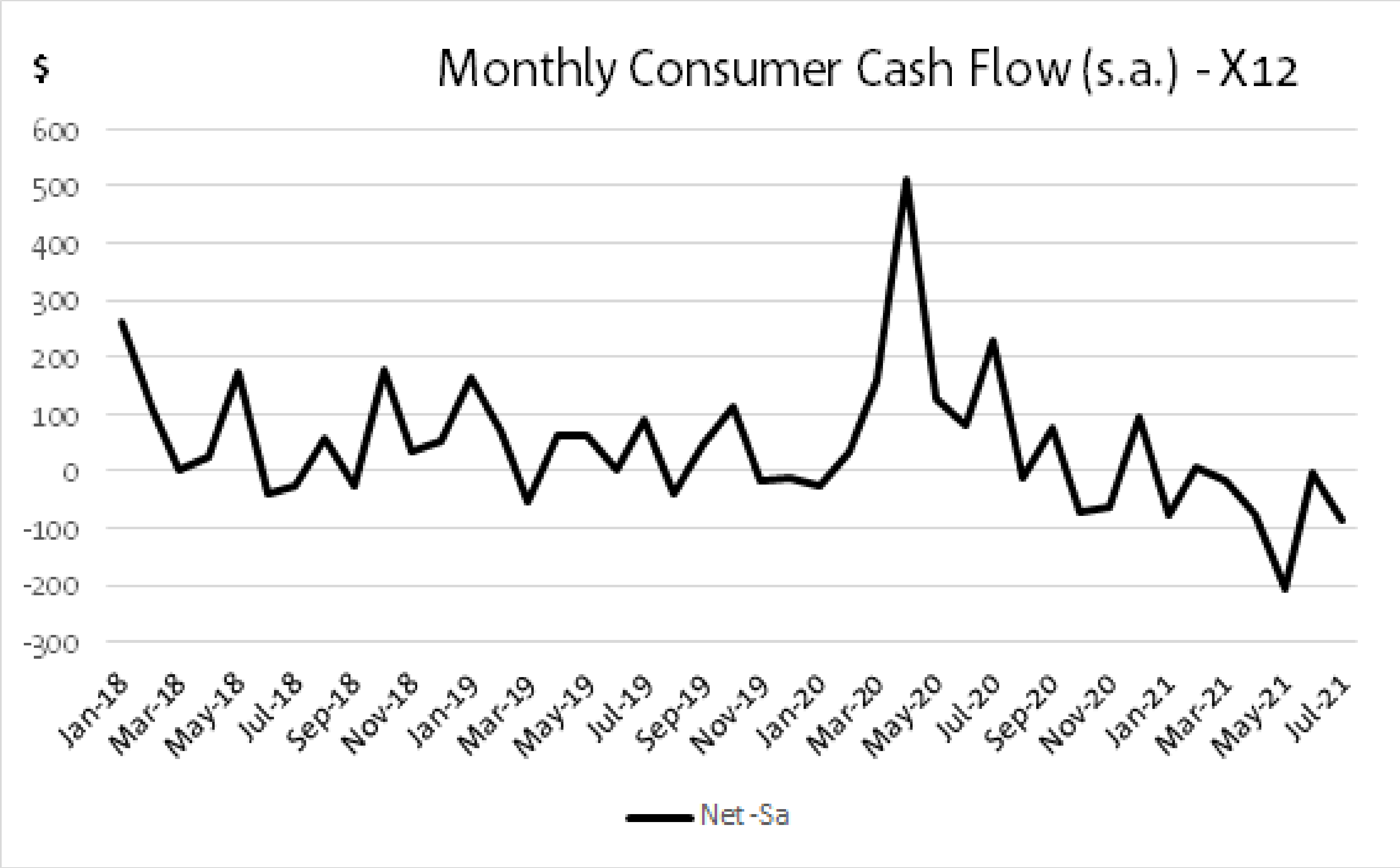
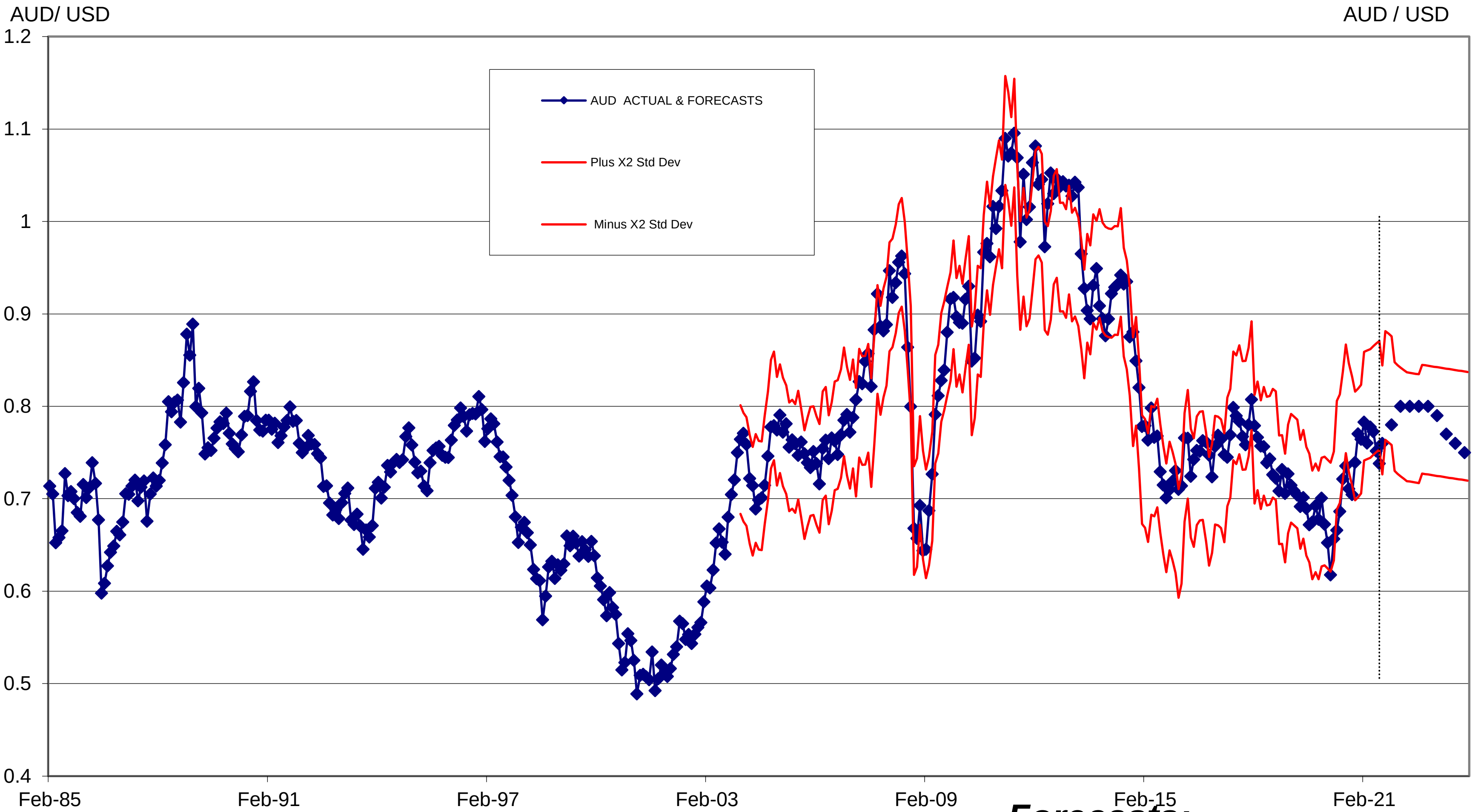
And you can see the importance of Government support in 2020*- to the average consumer. But fading into 2021*



Currency model. USD .79+/- 5c. *– so AUD below where you would expect. Australia seen as a proxy in virus hit world. But Australia doing better than most and US the reverse. We expect the AUD to continue to go higher in the near term. But back to LR average in 2023*

Currency Model* and AUD / USD



- Model driven by: commodity prices; US TWI – as measure of USD strength; long and short run rates; relative unemployment; relative equity markets and VIX.

Forecasts:

End 2021 = 78c AUD/USD
End 2022 = 80c AUD/USD
End 2023 = 75c AUD/USD

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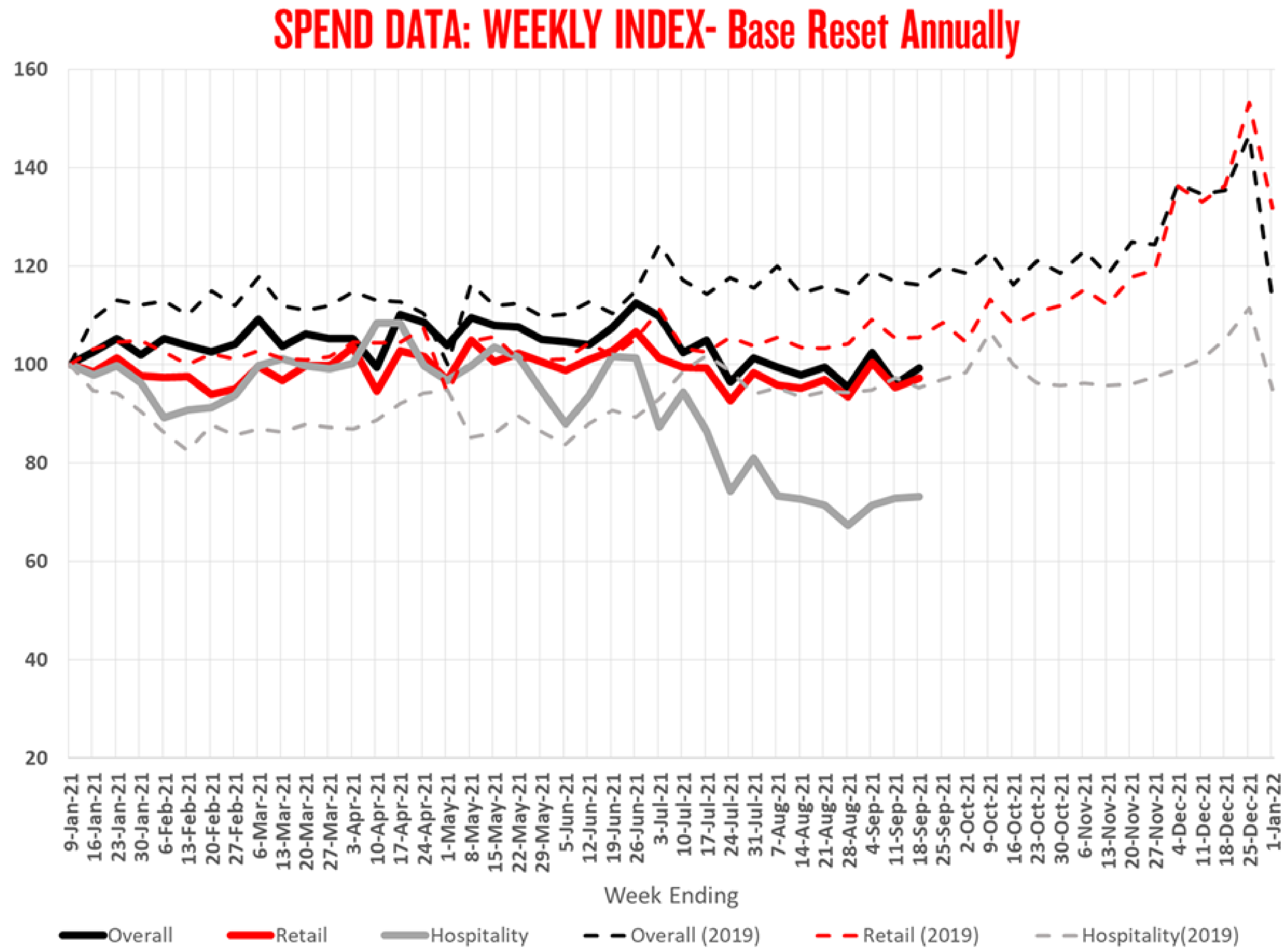
Data Insights

- NAB Data
- Business Survey

On NAB's internal data: Consumption to 18 September. Lockdowns hurt - from June consumption and retail down 16%+ and hospitality down around 25%. *But might be nearing a turning point - Using 2019 seasonality and comparing to the start of the year.*



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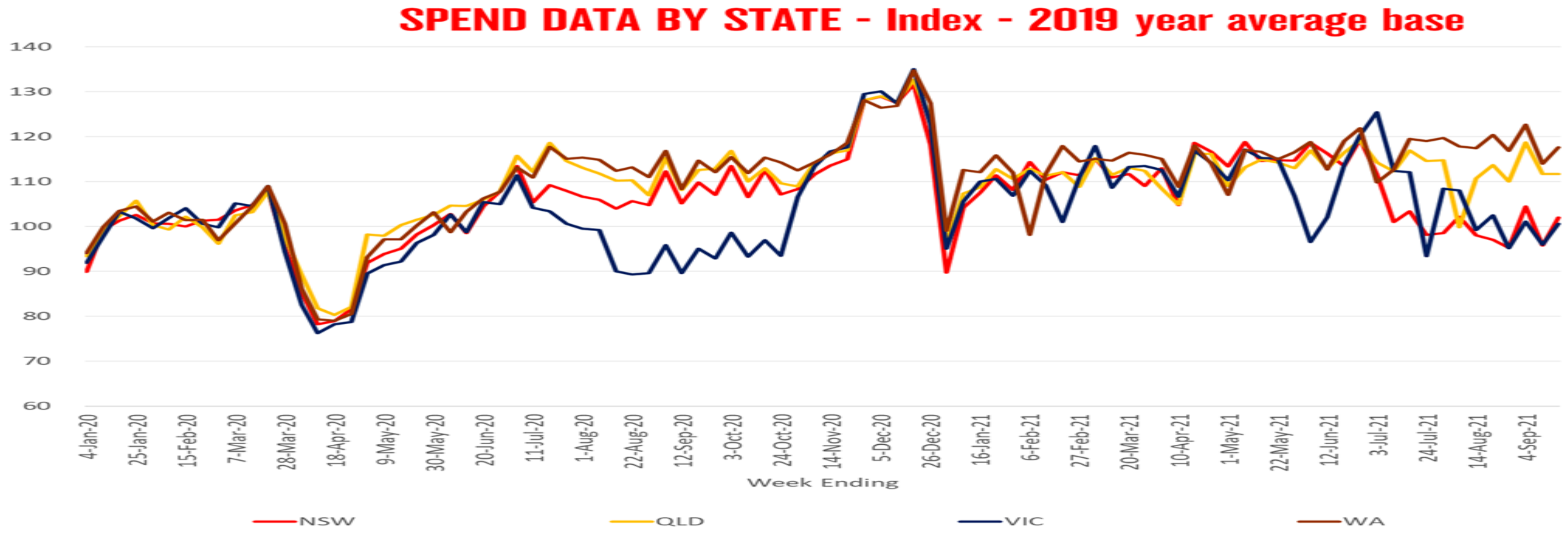
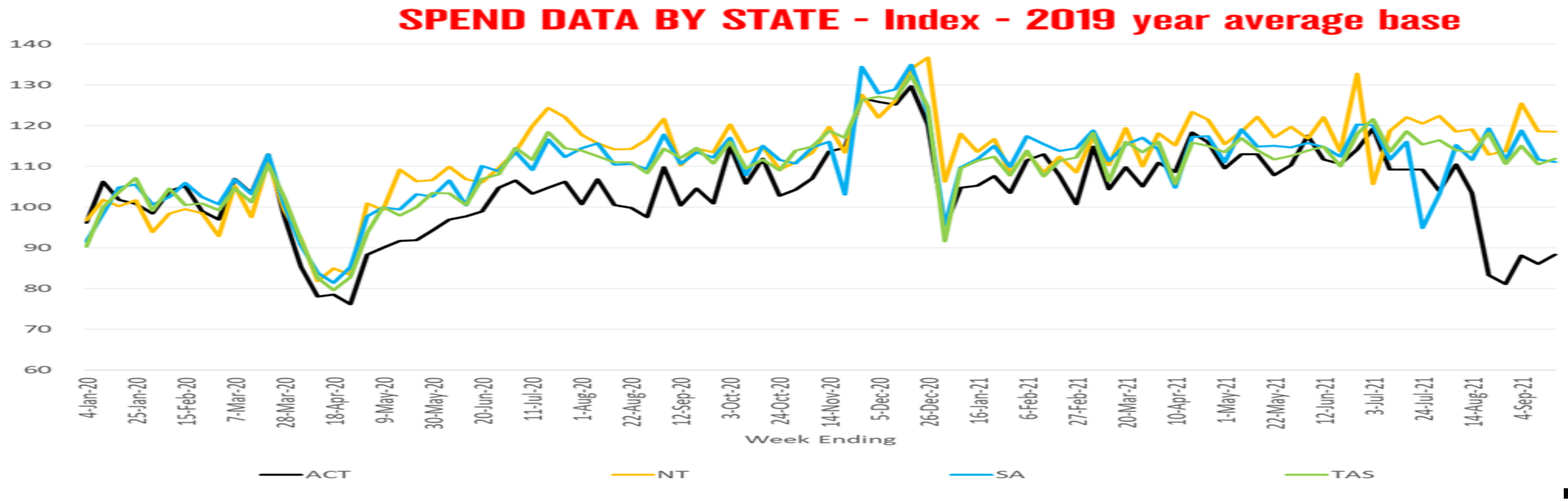
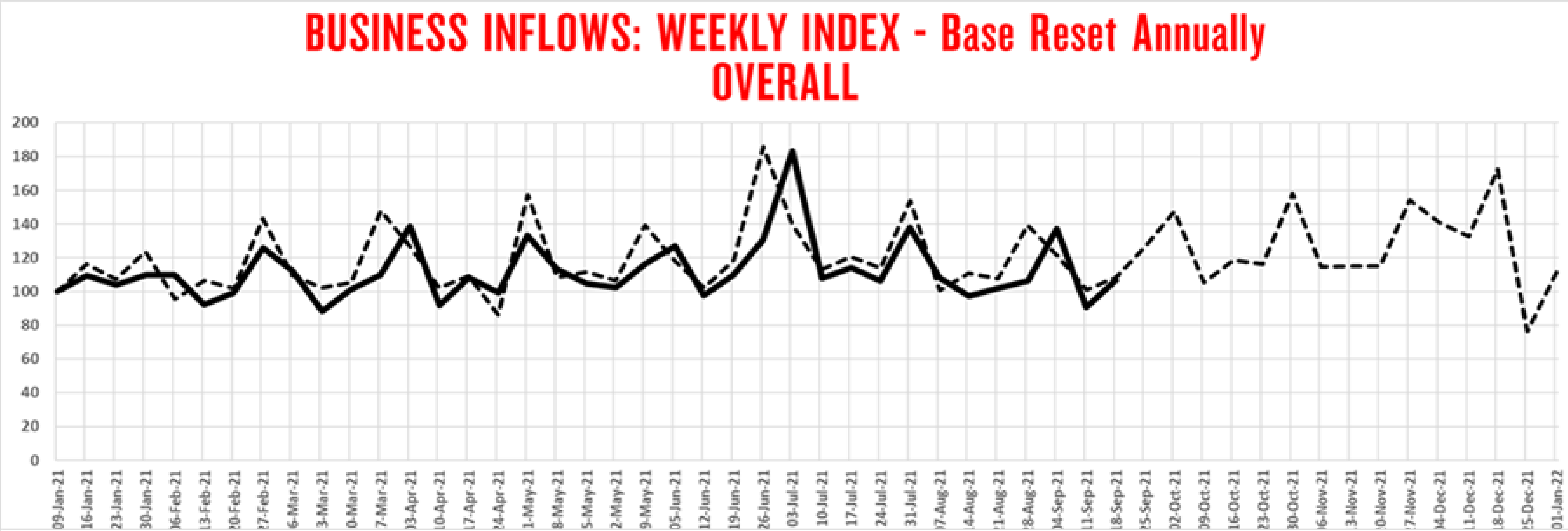
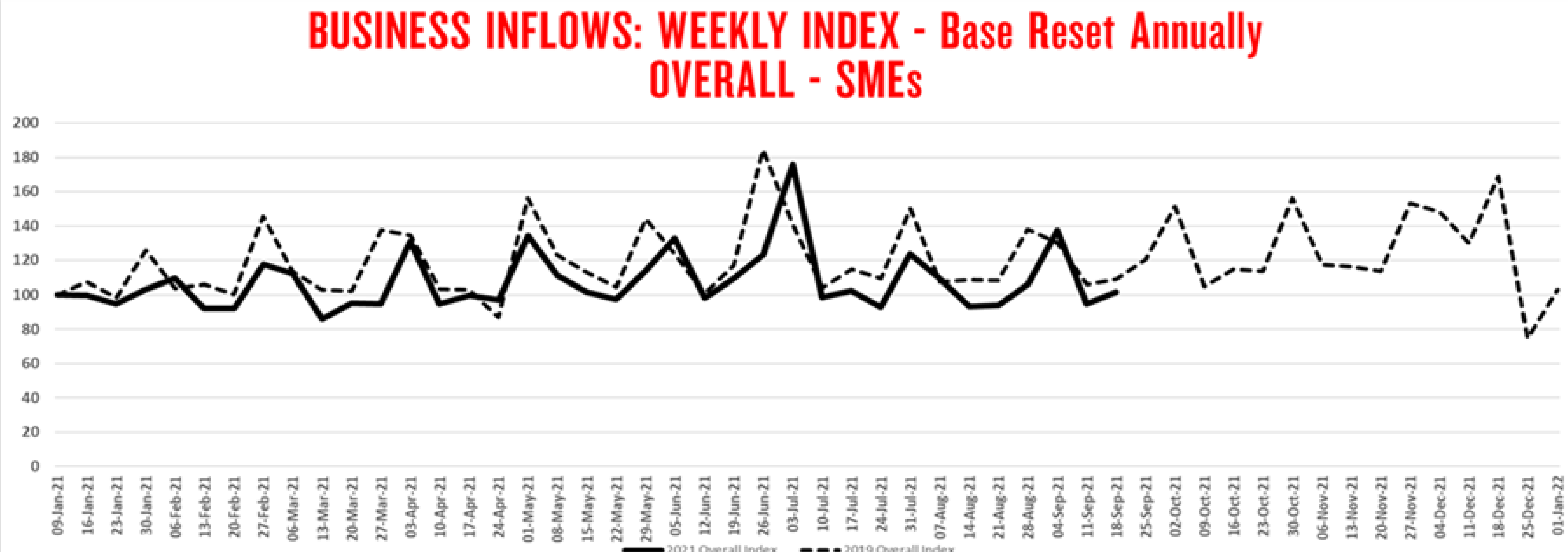
And again most states poor especially NSW and Vic but maybe they are stabilising . Qld improving and WA not much hurt. Also Tassie good and SA helped by end of lockdown *WA and Tassie harder to get to their borders*





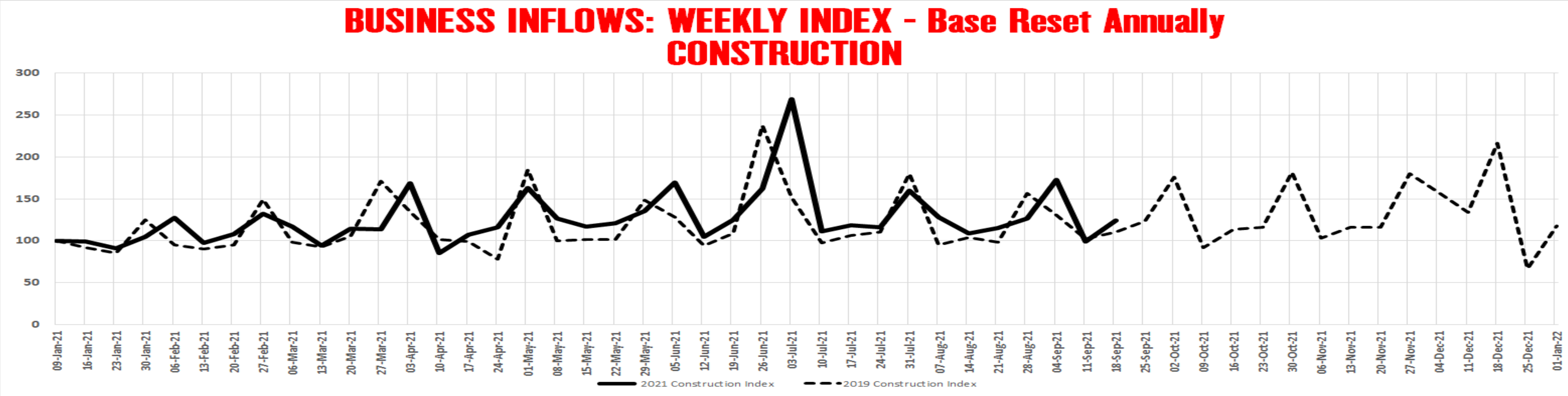
Business inward cash has been under pressure recently but improving. Looks like hospitality, and Arts and Rec improving a lot.   SMEs also doing OK

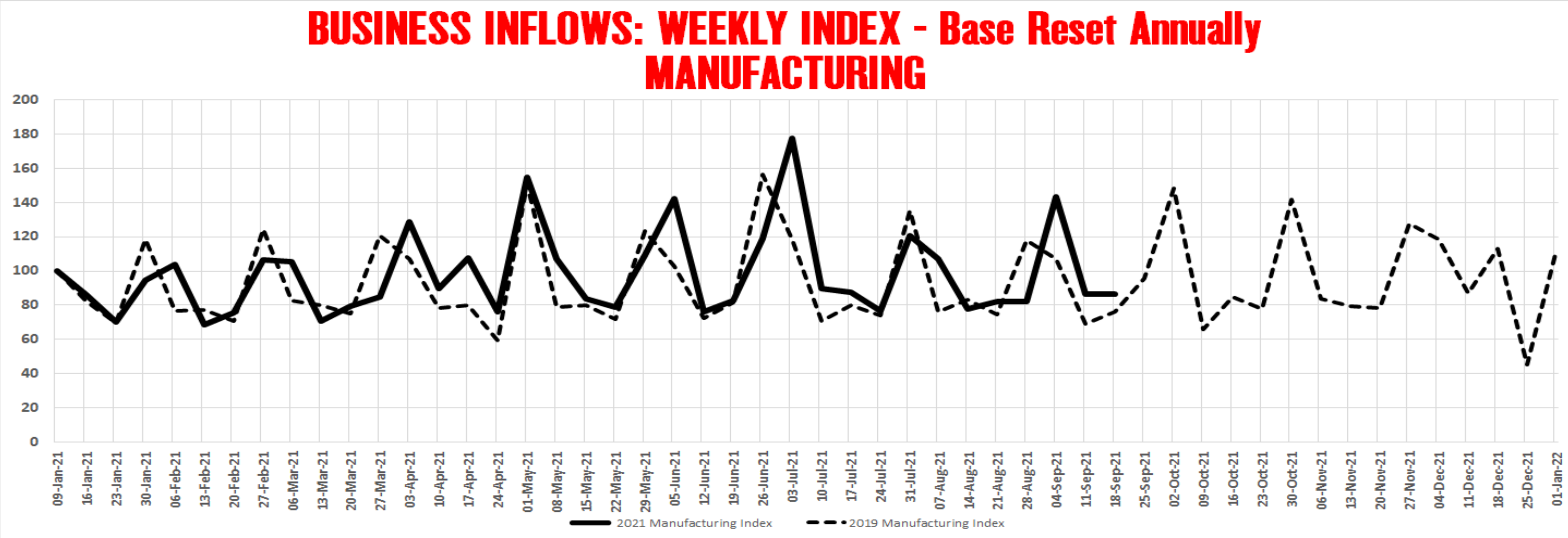




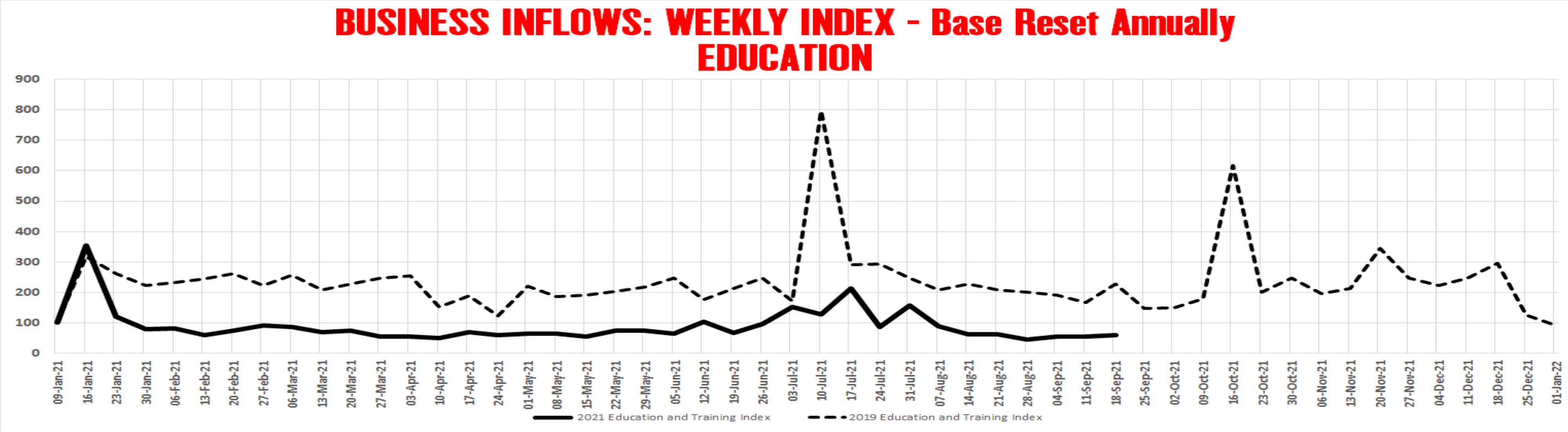
Some industries are doing relatively better.

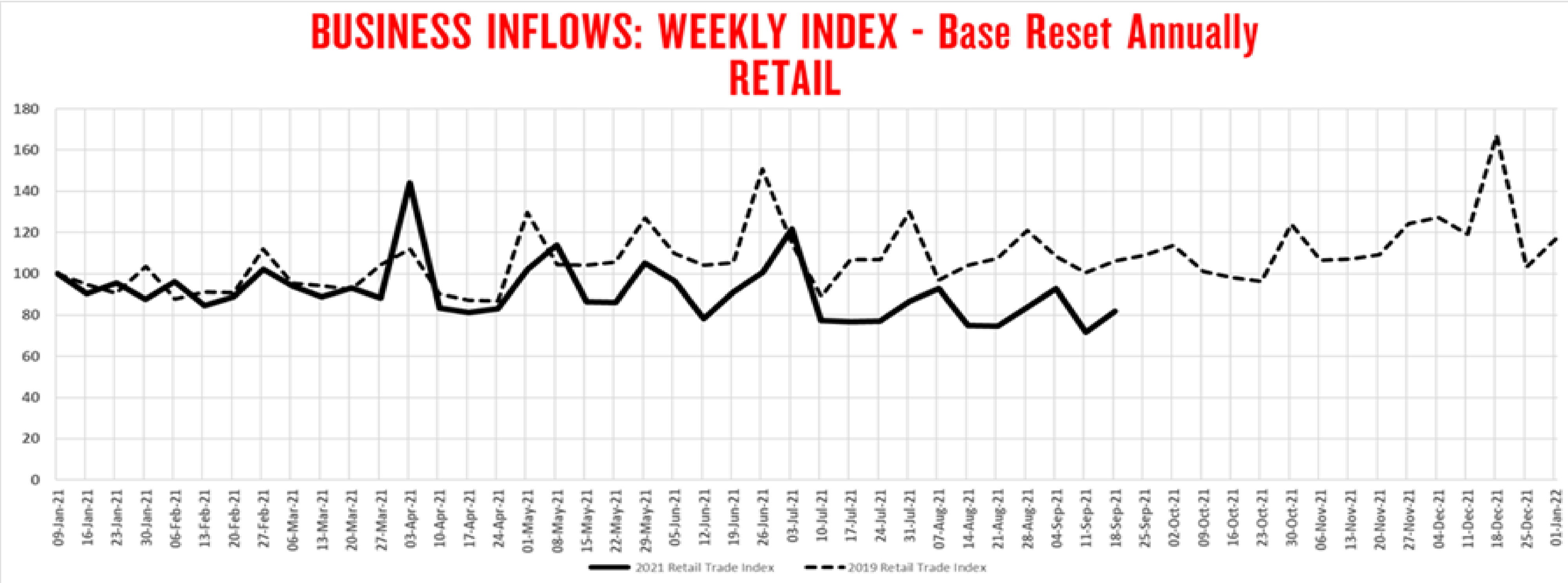
Better performers are – *Agri and more recently Manufacturing and construction*





But Education is a mess So was hospitality until recently (but bouncing back now)
Retail not great either – *but may be turning up.*





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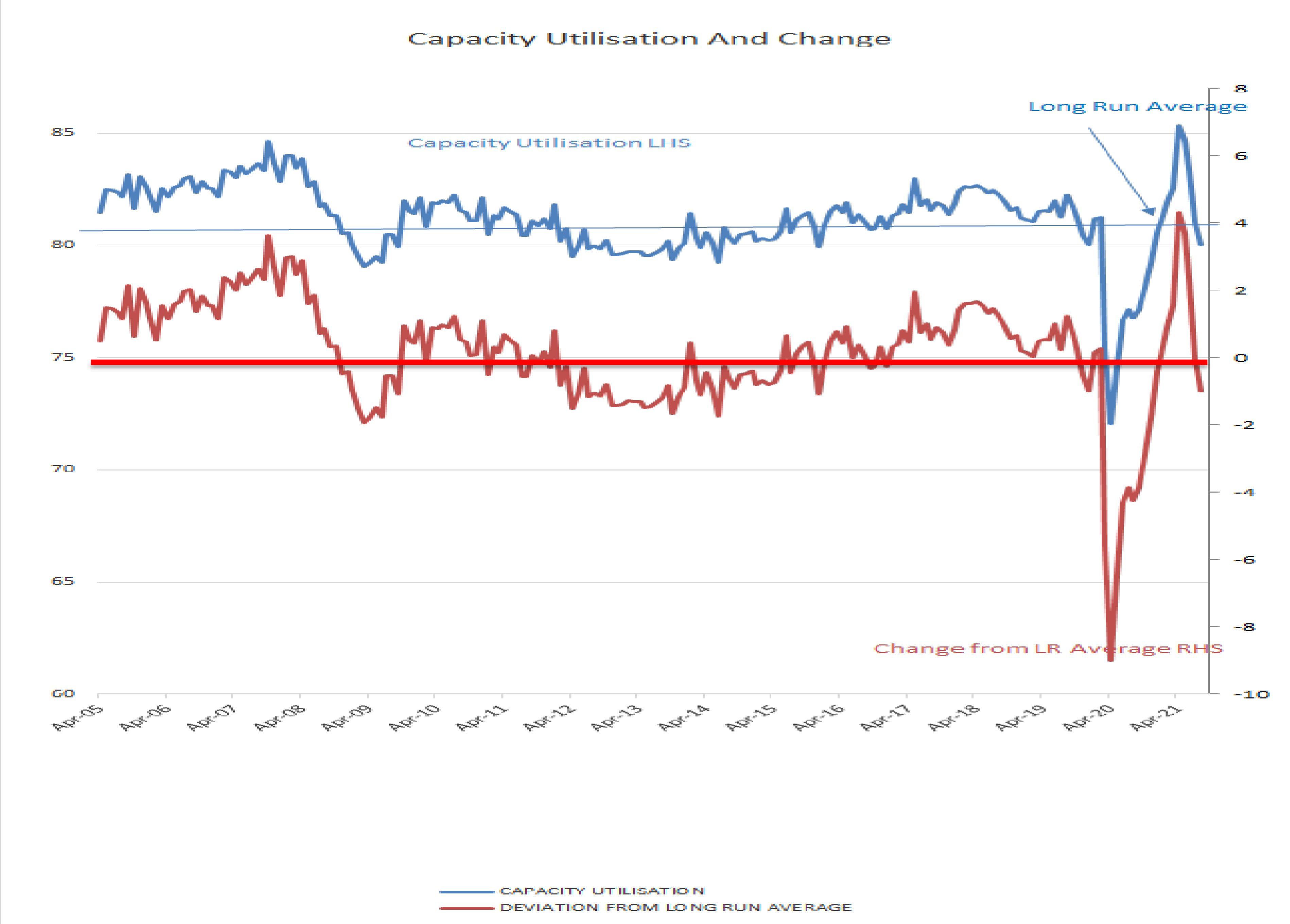
Capacity utilisation fell around 9% in the crisis, then recovered during the year. Got to 4% above, but recent lockdowns hurt. Now below long run average - *but further falls to come.*



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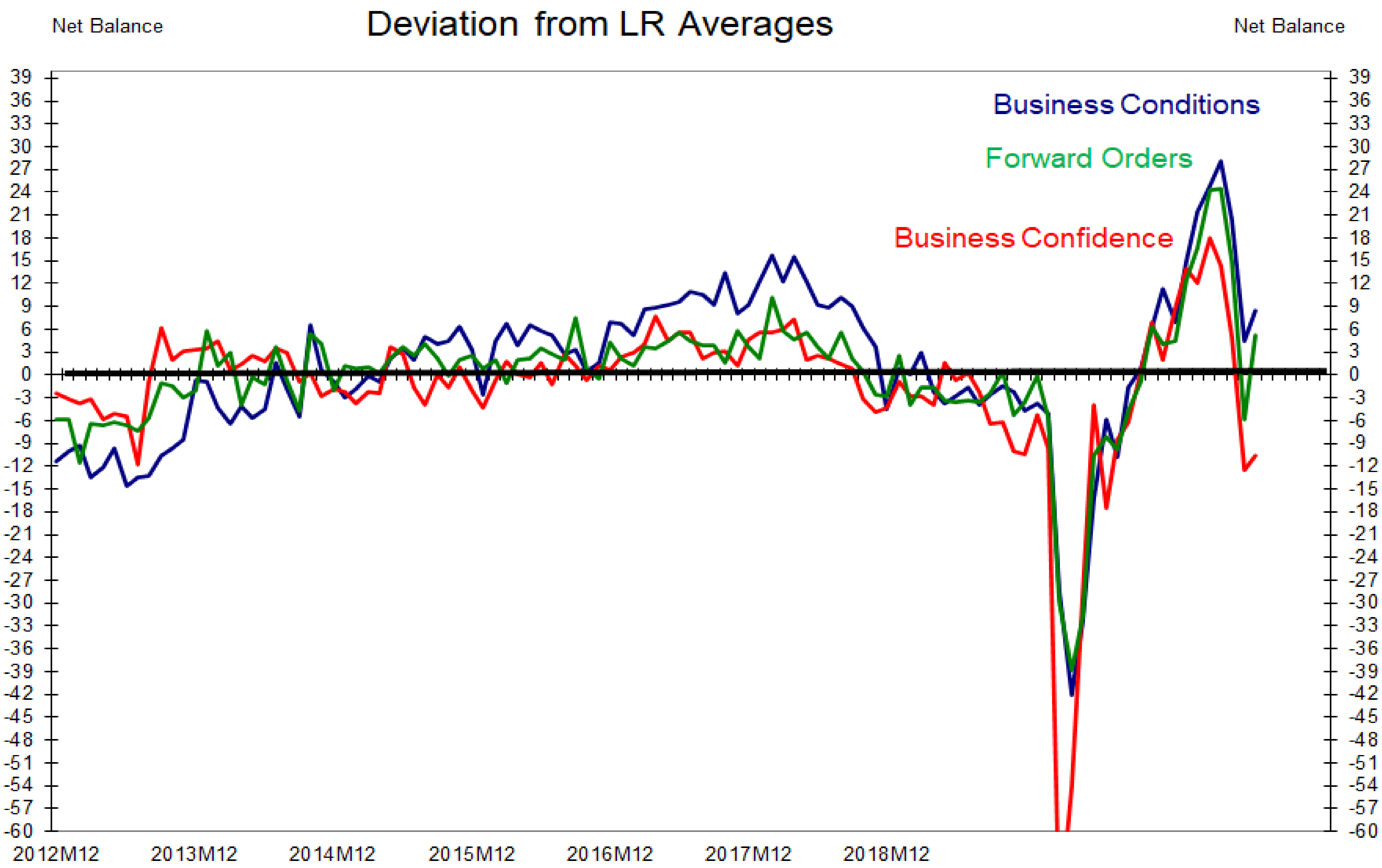
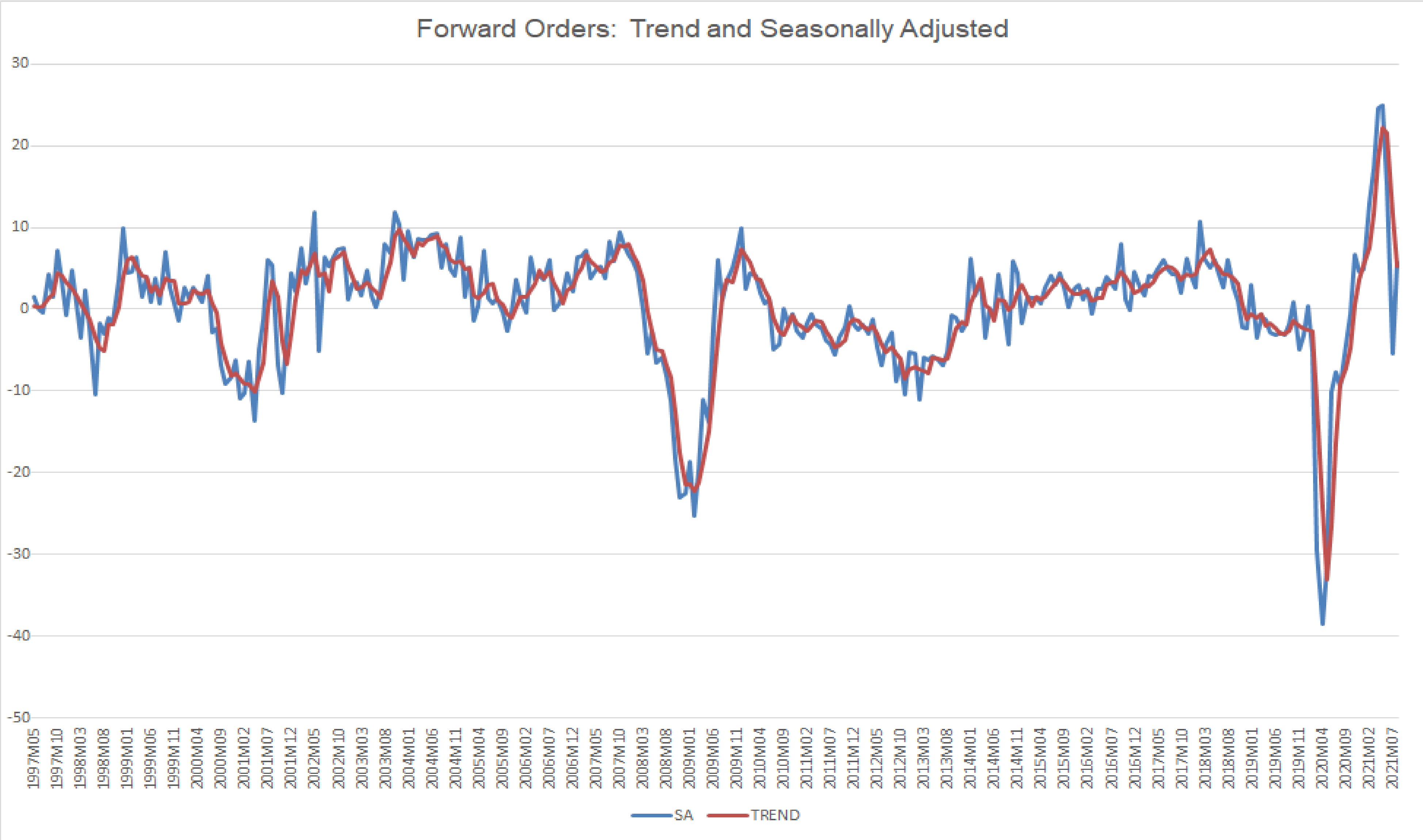
And it's a similar story - *for all the main indexes. All series reached record levels but have been seriously hurt by recent lockdowns.* August was a bit better than expected given lockdowns but….



My favourite indicator of activity in the Survey is forward orders. *- Not looking good. But again August a bit better than expected*



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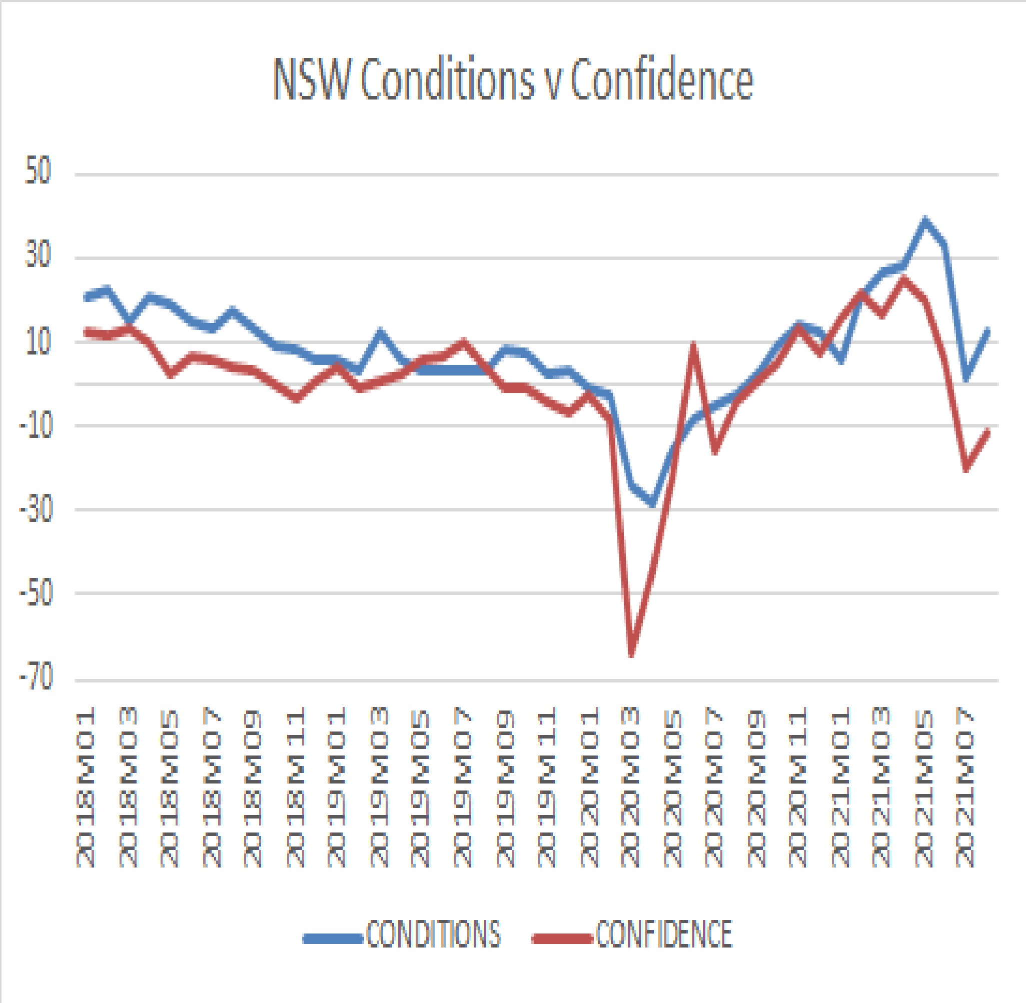
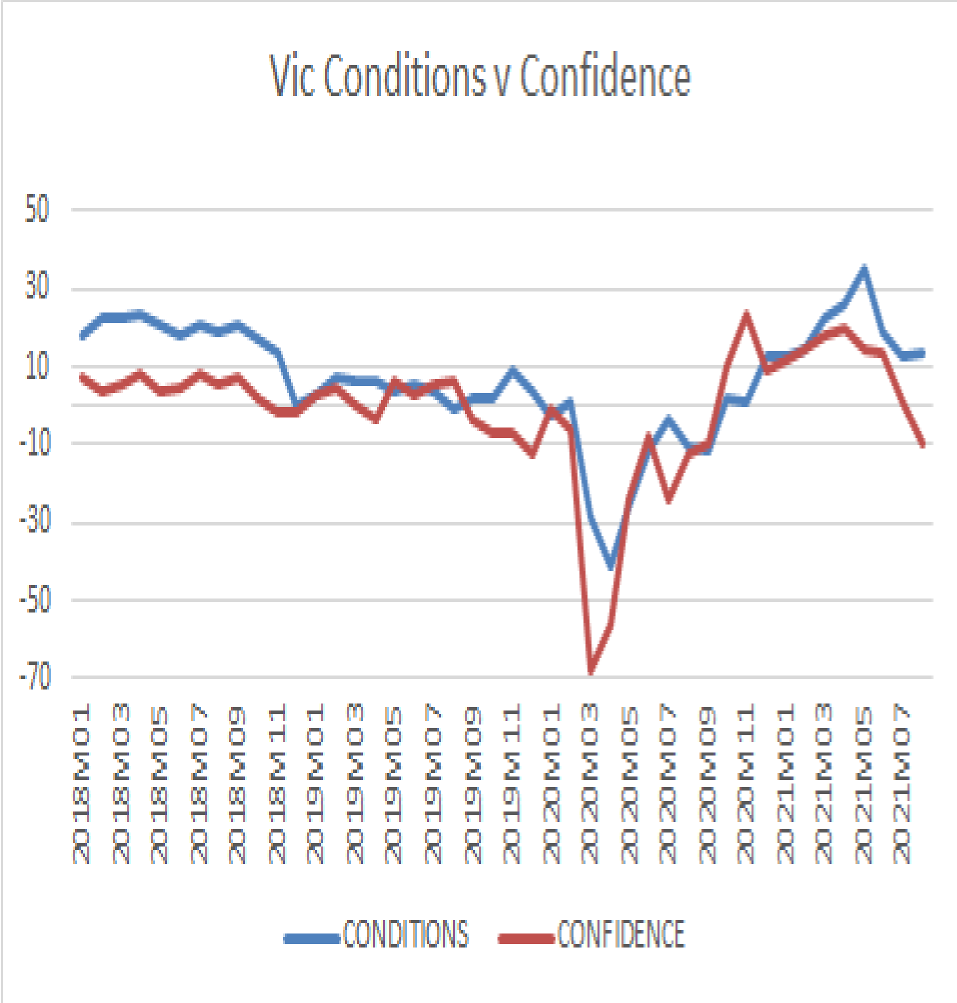
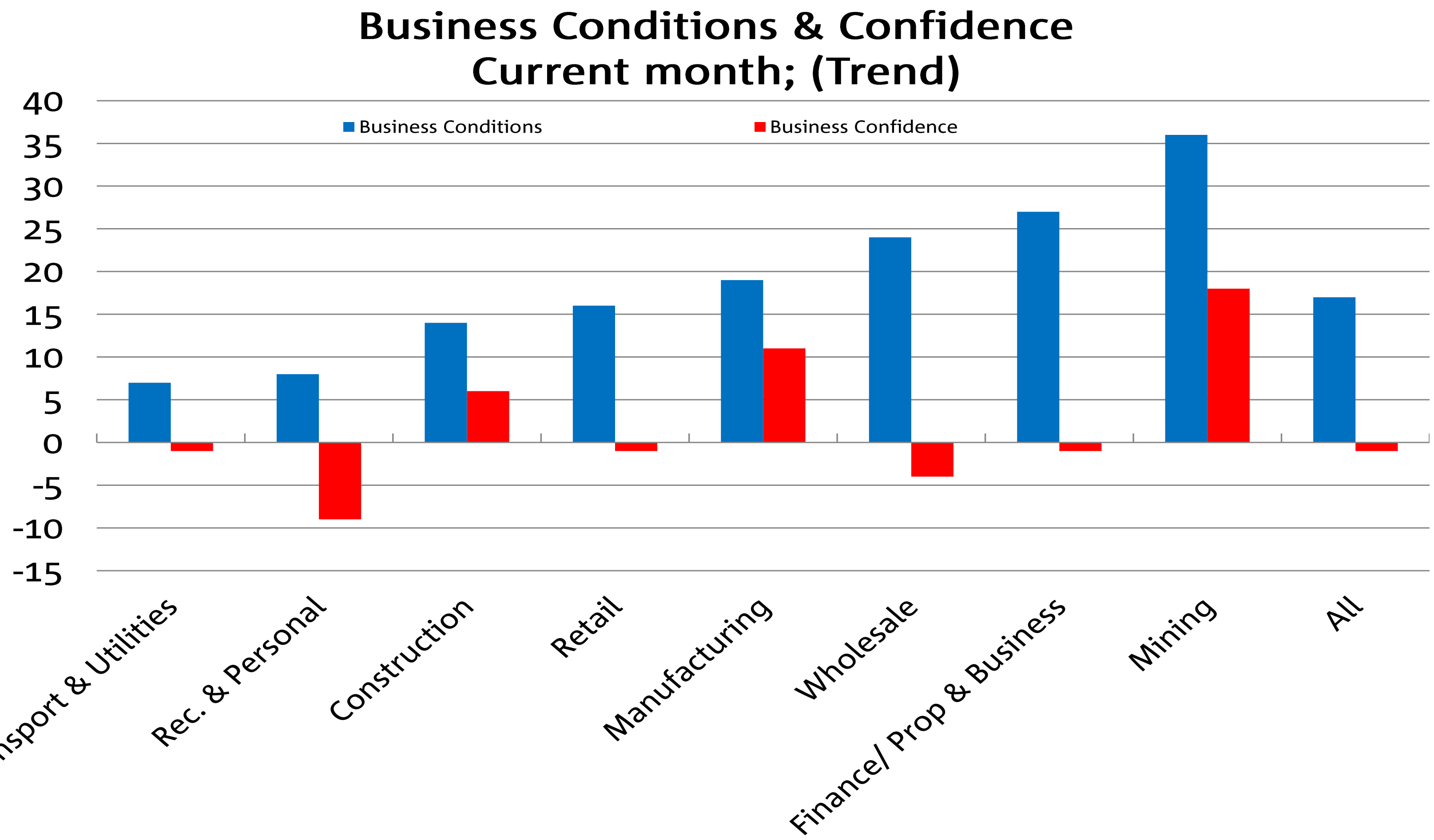
Confidence really shaken in NSW but a bit better in August as outcomes improved a touch. Vic now more worried about on going lockdown but activity was OK. But…



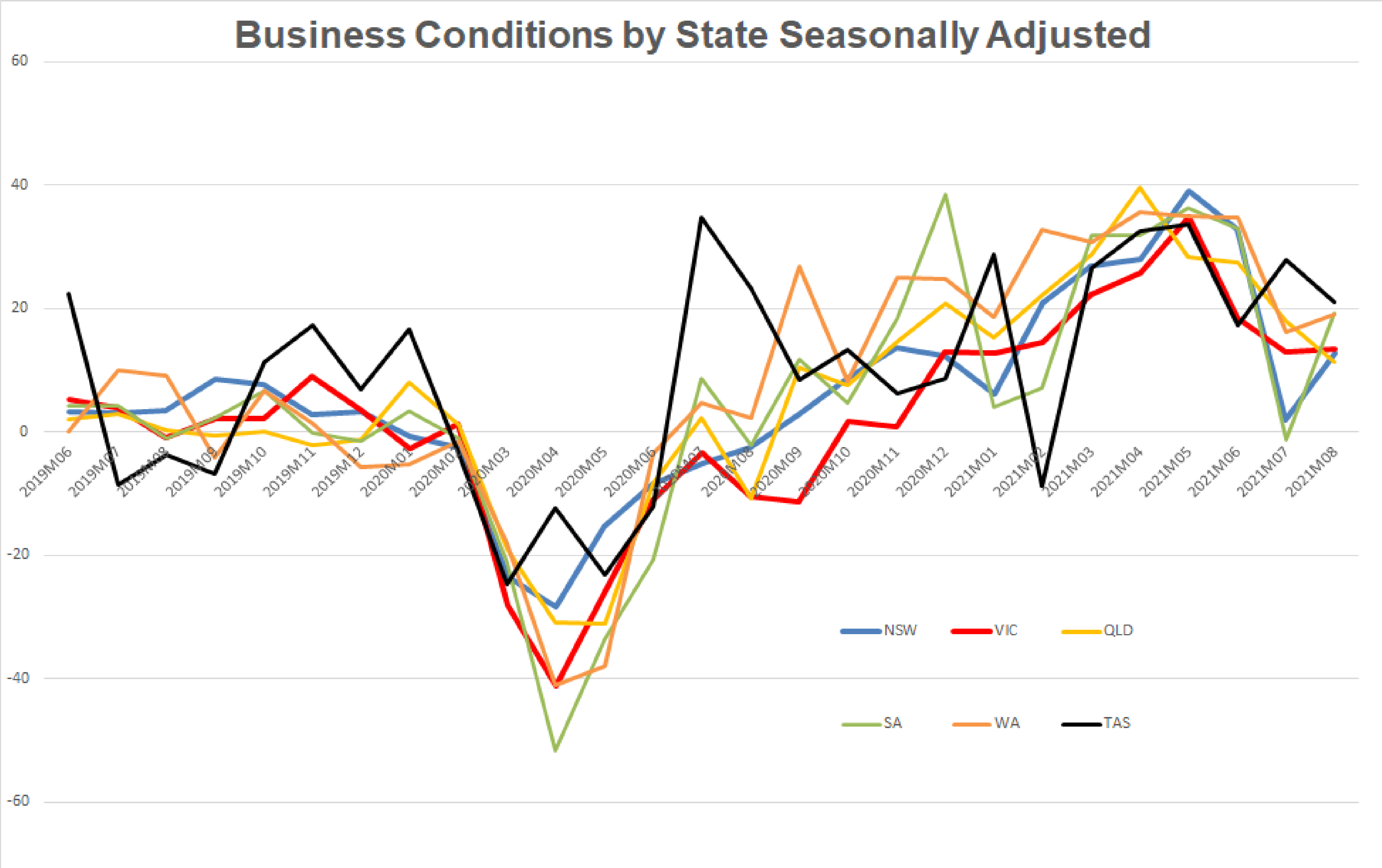


By industry the hits to confidence and conditions very much driven by hospitality.
– Personal and Recreational services in this chart, Transport and Finance also worried.

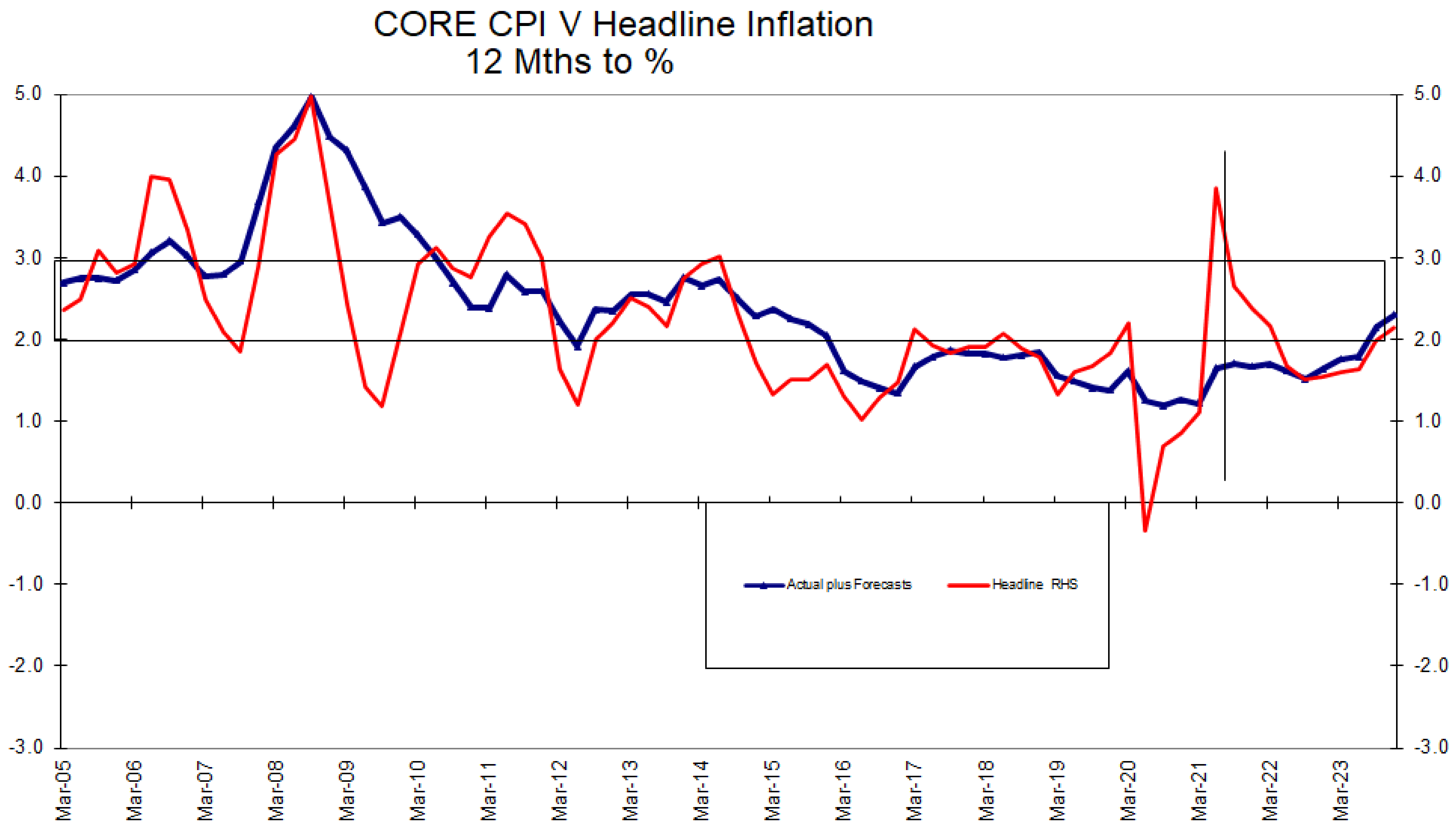
Business confidence and Conditions in August



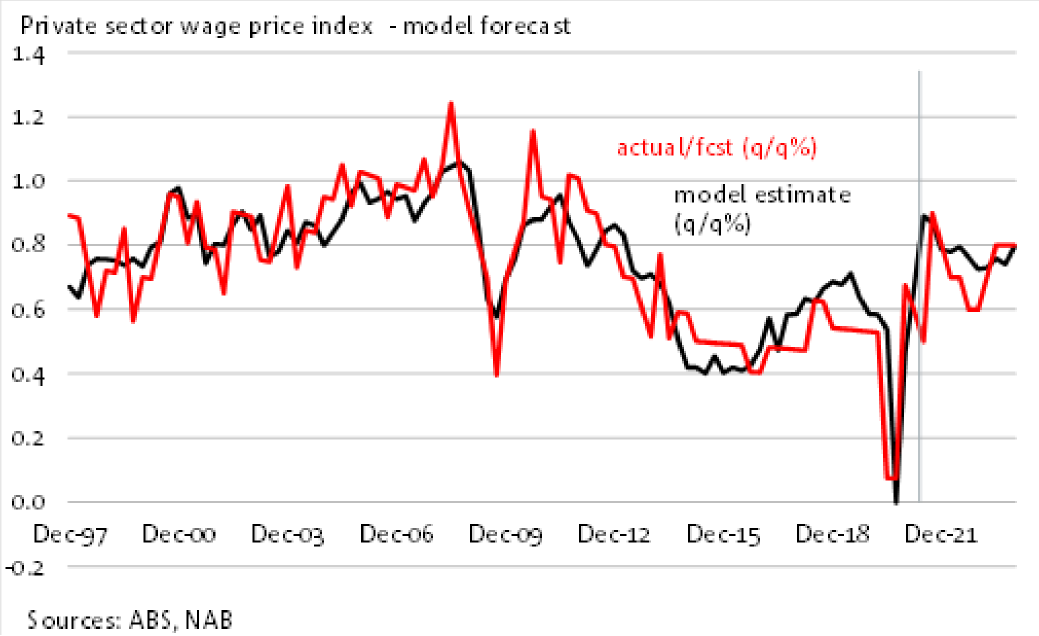
State data jumpy by month *– but trend data hides turning points. Overall NSW (after a bounce), Vic (relatively stable) and QLD the worst. The latter likely to be a flow on from hospitality hit. WA and Tassie the best (most isolated).*

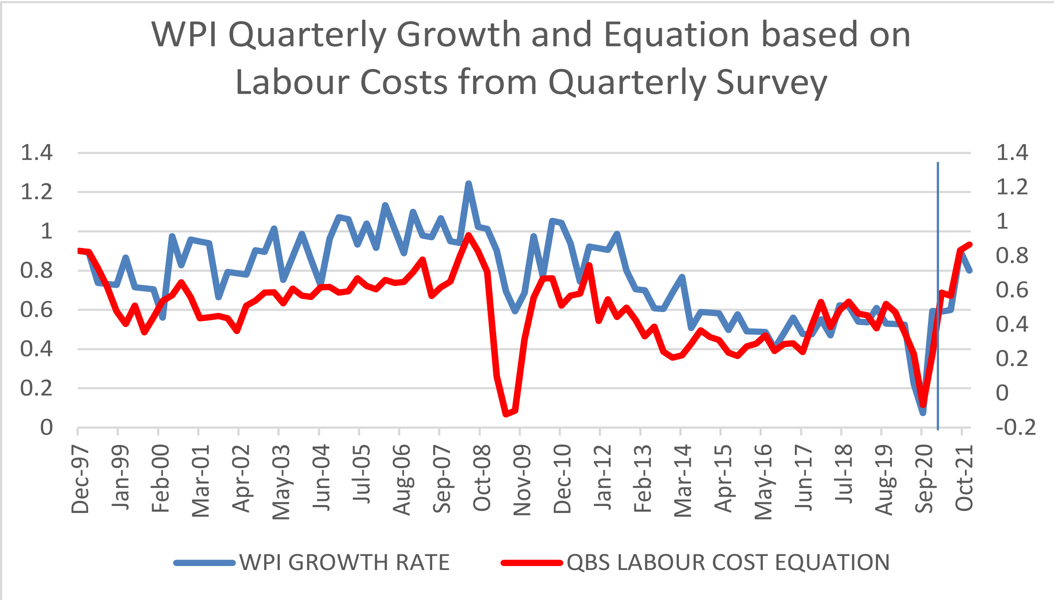


Expectation for wages growth is critical in the current environment. *– To get core inflation back on target you need 3%+ in wages. We expect core inflation of around 1.6% by end 2022 – with stronger AUD helping. We also see core inflation around 2¼% by end 2023.*



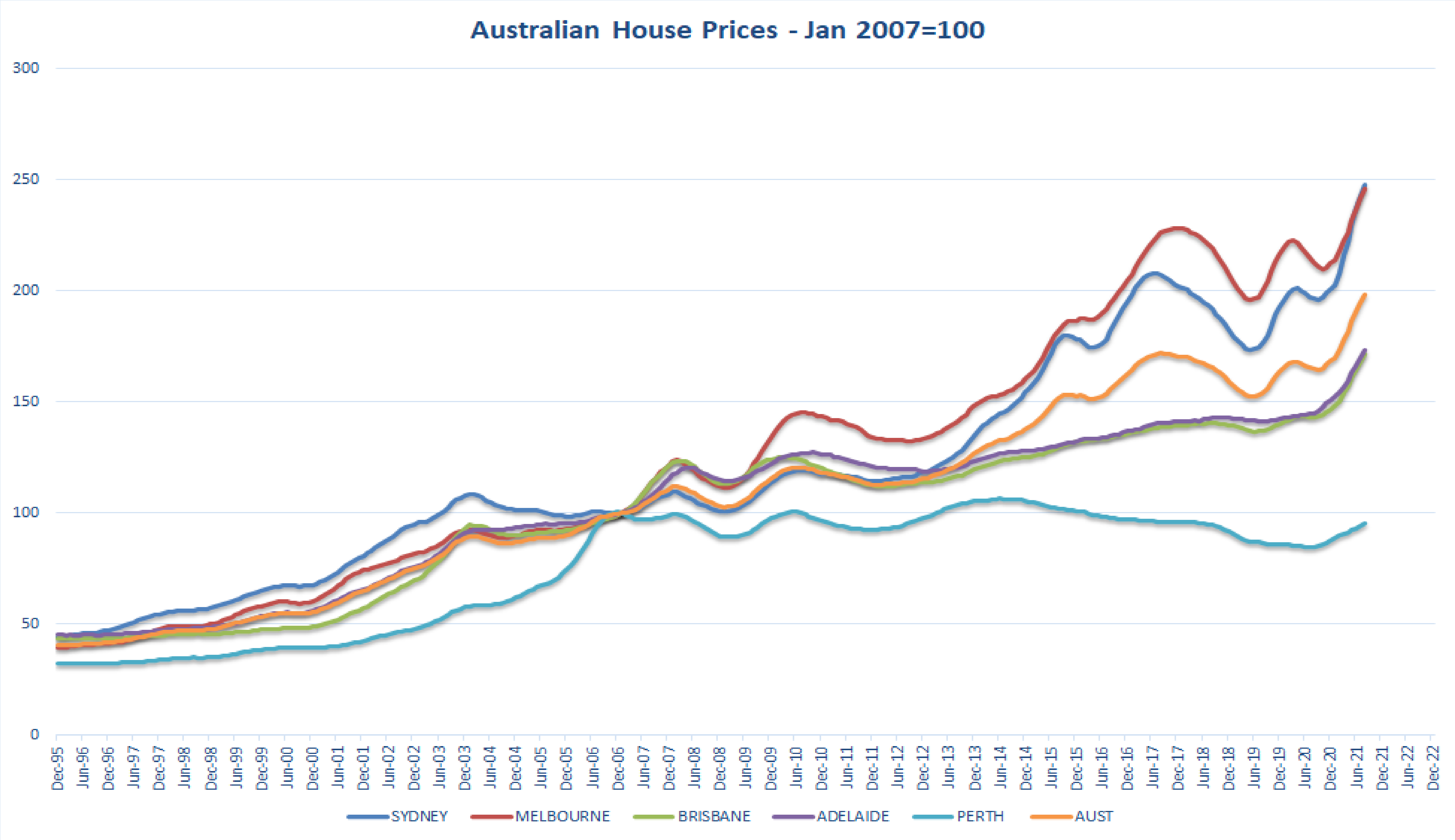
Wages pressures will build given the speed of the fall in unemployment. But temporary initially. - *Not sustainable above 3% till late 2023.*





- Our models of wages pressures typically driven by:
  - Productivity (2.5 year rolling average);
  - Level of underutilisation;
  - Change in underutilisation;
  - Change in terms of trade;
  - and inflation.
- Key driver is the speed of the change in the labour market (change in underutilisation of labour). But temporary.
- Our Business Survey also gives guides on labour costs and skill shortages.
- They point to a short term pick up in H2 2021.

On house prices – *first an historical perspective. Basically all capital cities ex Perth are now above their previous peak – Perth still the laggard.*



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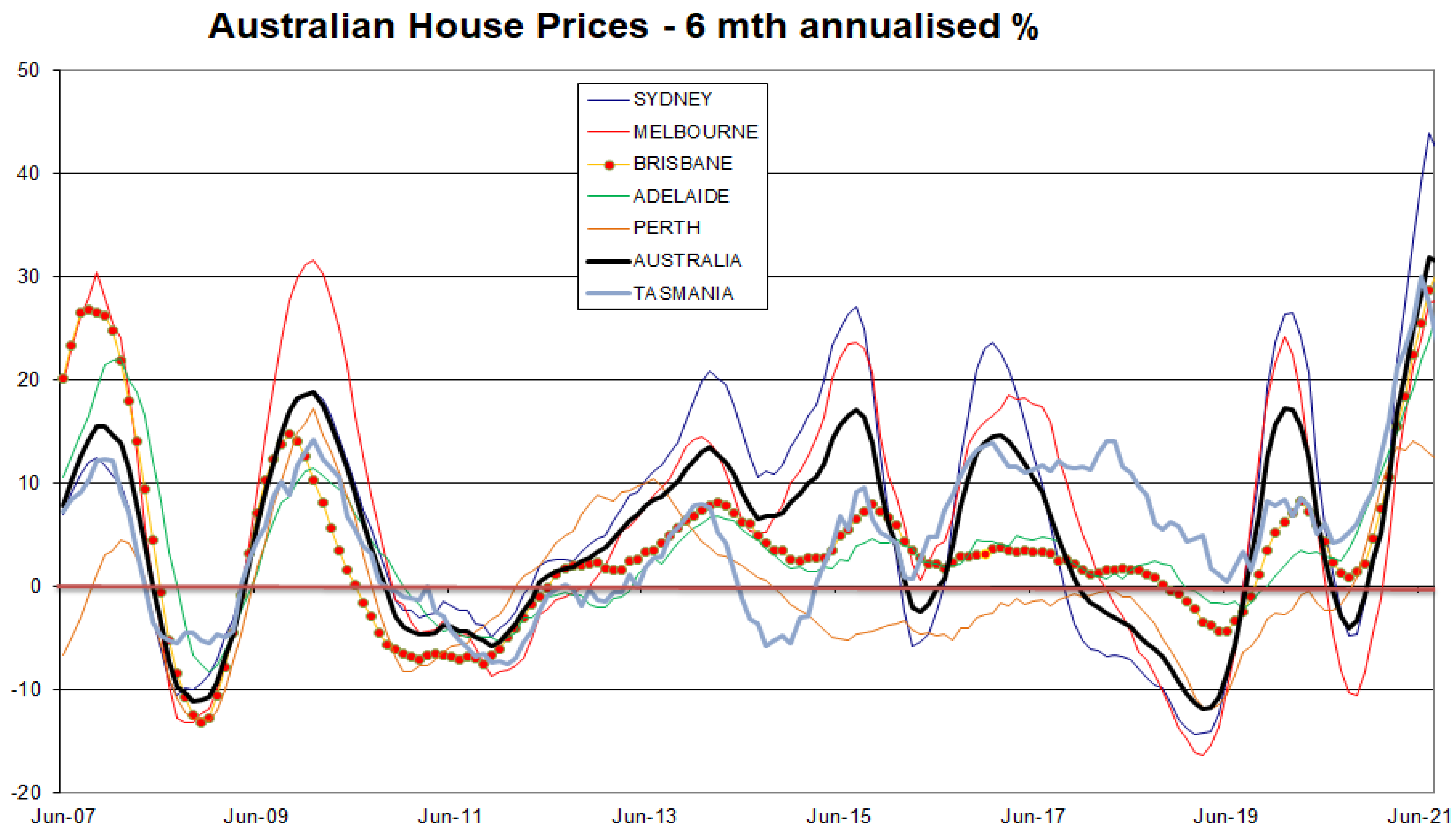
House prices clearly have significantly bounced from initial virus hit. And are now accelerating away very strongly *– Sydney up 40% at annualised rate while Australia near 30%. Only Perth lagging, on this measure – but still up 14%.*



Key drivers - of *house prices.*

- Population and under-over supply:
  - Australia to record the slowest growth of population for 100 years;
  - Very negative for some sectors (Sydney/Melbourne CBD).
- Unemployment:
  - Unemployment has come down a lot but is still elevated;
- Rents:
  - Were falling in most capitals but not any more.
- New ways of work:
  - Zoom changing work practices;
  - House prices in regional hubs with good internet will be boosted.
- Interest rates:
  - Will remain low/unchanged for at least 3 years;
  - Assets more attractive in attempt to try to get more yield;
  - Early vaccine may help sentiment further.

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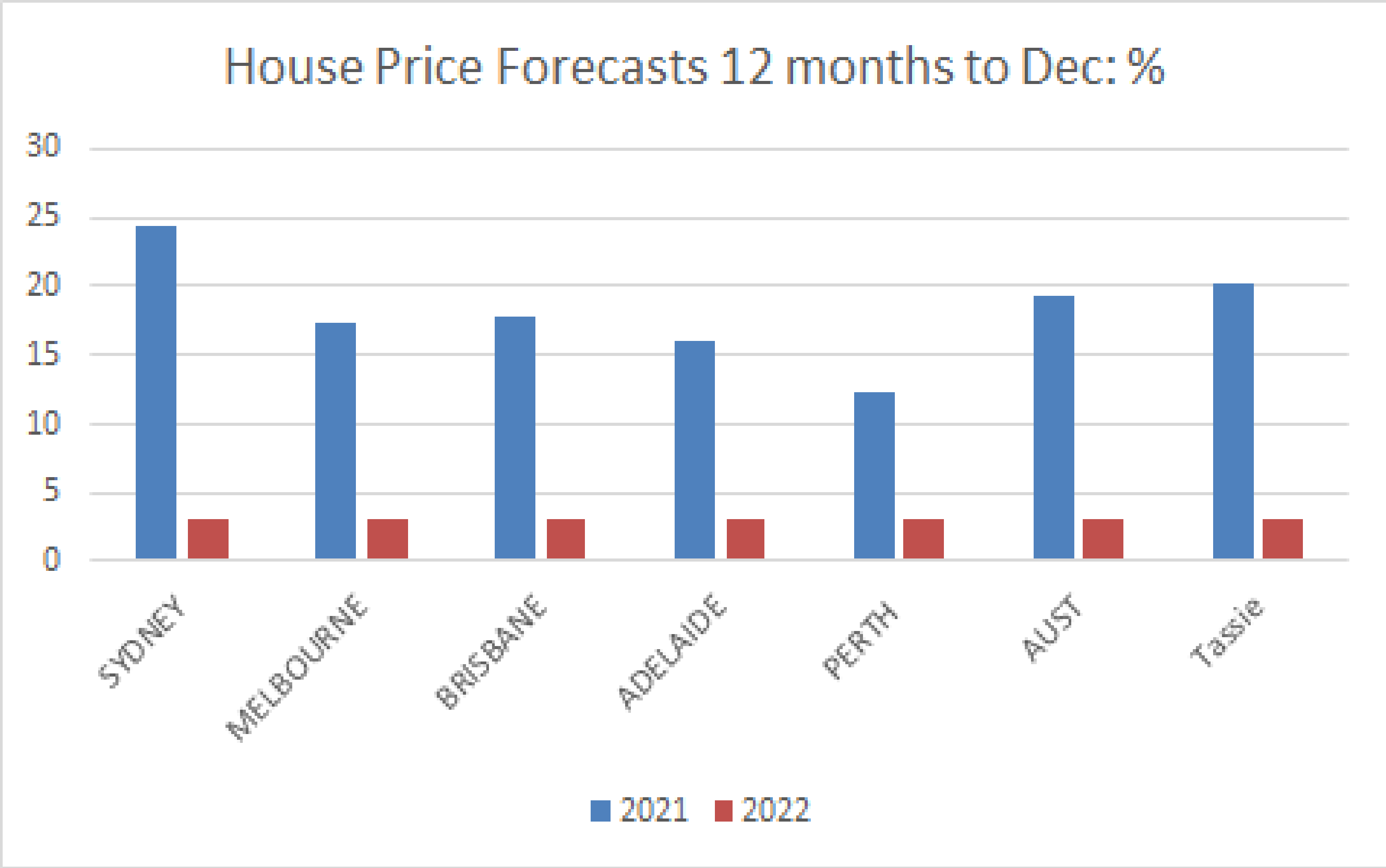
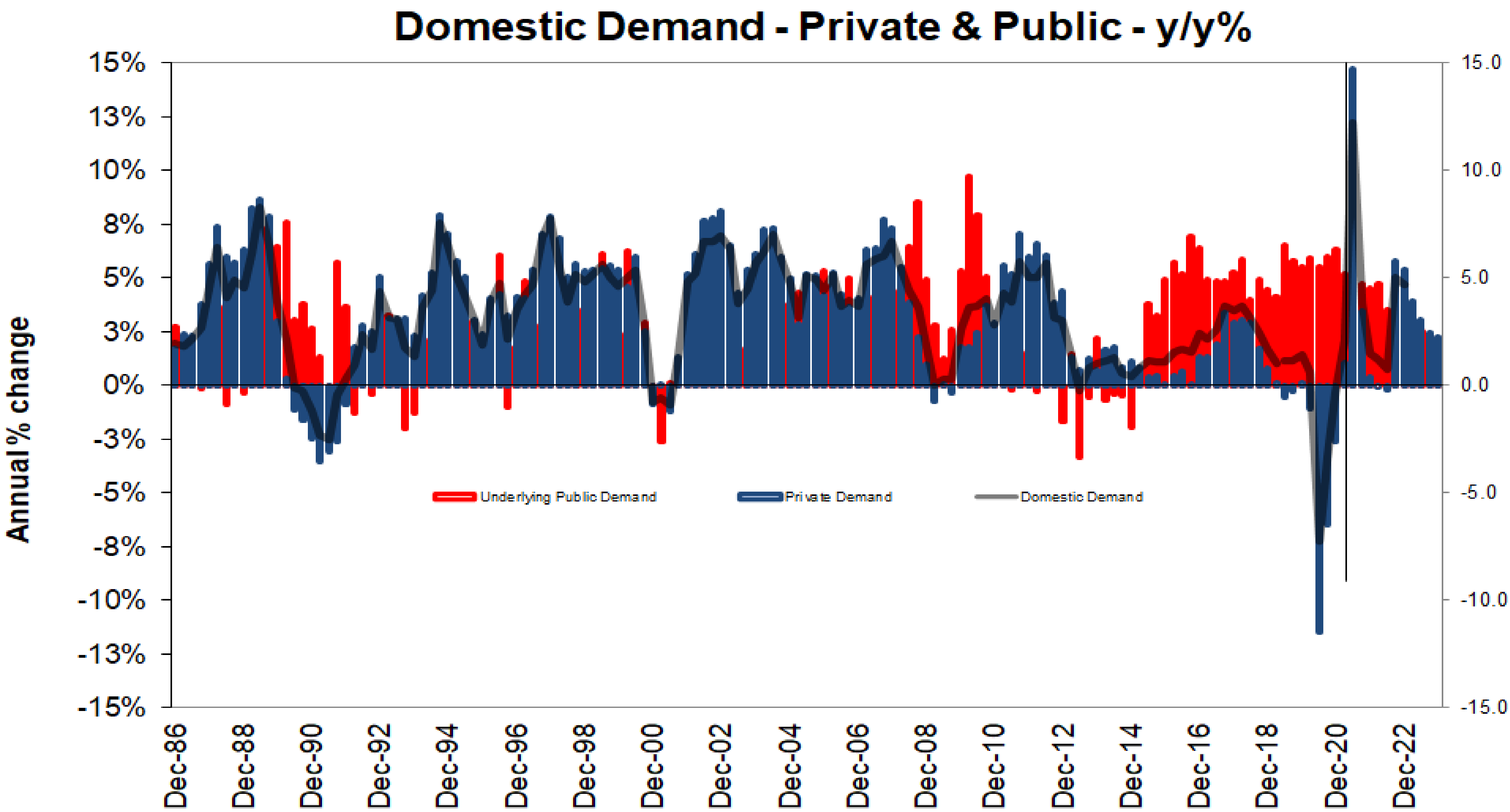
House Price Forecasts. - *We now expect house prices to rise by around 19% in most capital cities in 2021 (stronger in Syd and Hobart) & around 3% in 2022. Faster in the regions. But weaker unit prices in Sydney/Melbourne. Macro prudential coming.*



Going back to the big picture: *- The hit to private demand has been massive. Public spending critical to surviving. Private sector now taking over and investment, dwellings construction and manufacturing very important as consumption moderates.*



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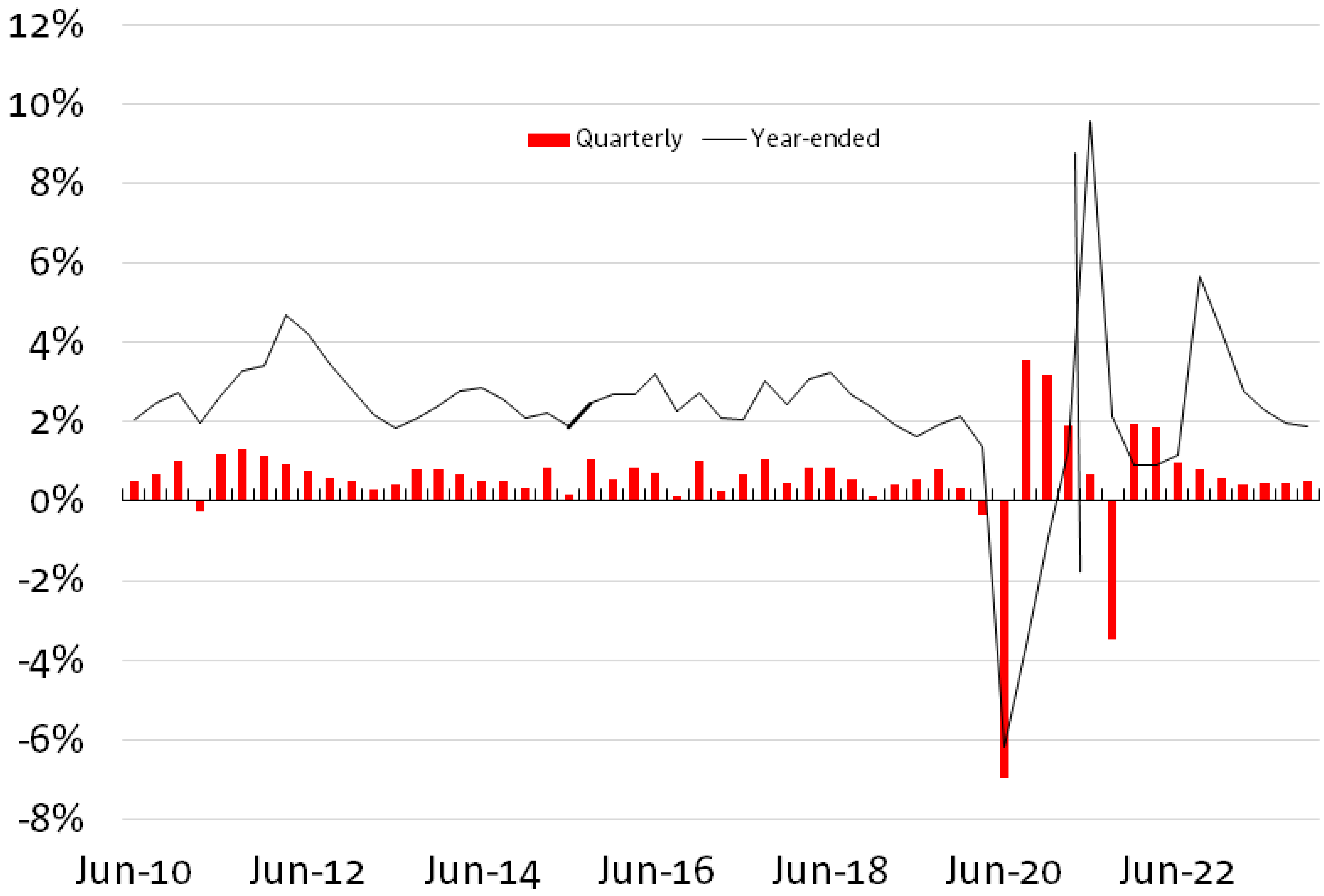
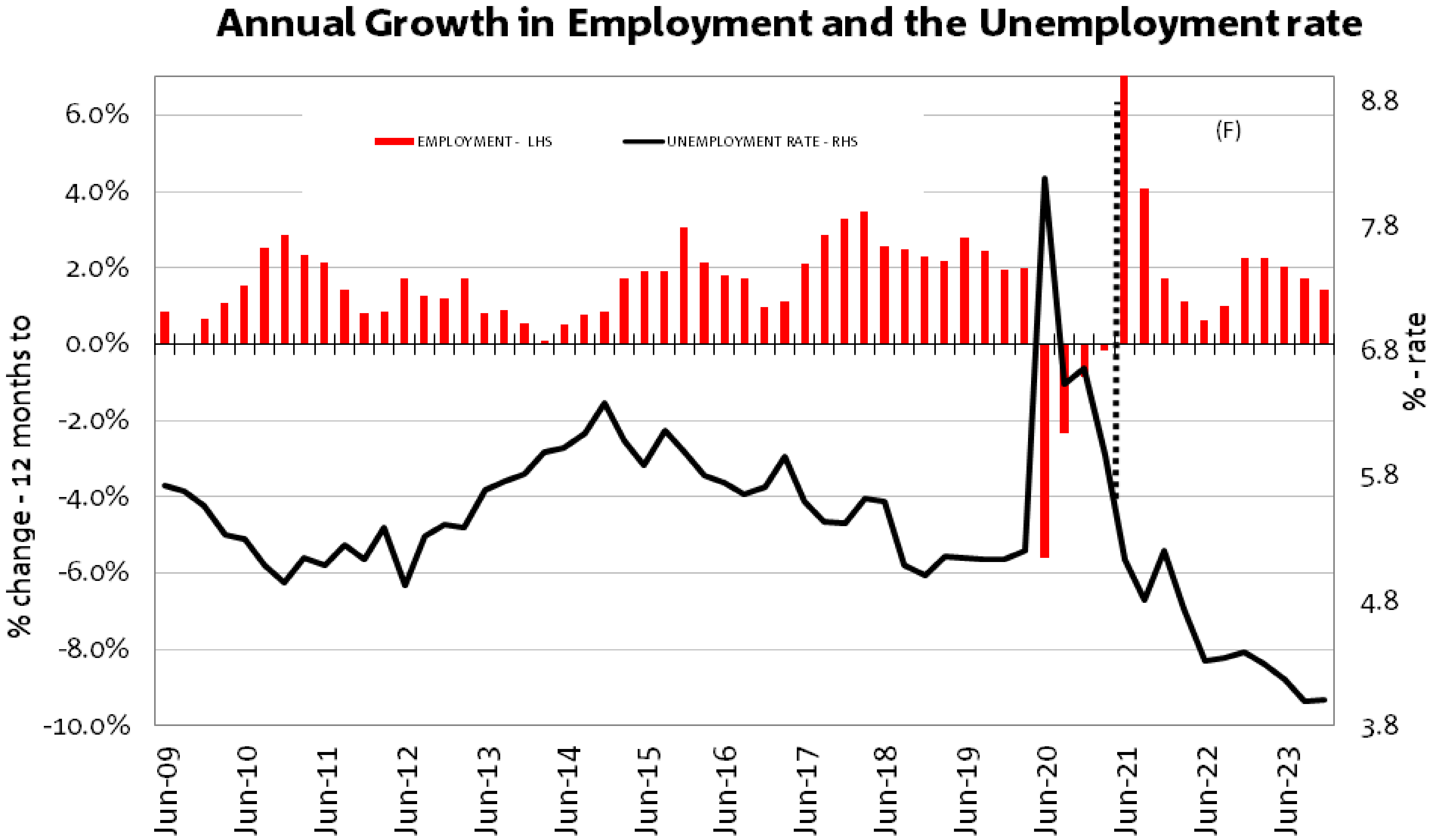
Our Growth Expectations. Obviously the lockdowns will severely dint Q3 GDP – with Q2 OK. Thereafter we expect a better Q4 – but still negative H2 2021. And finally a strong bounce back in 2022. *By 2023 a return to potential growth.*



Despite impressive labour market return the short term outlook is for a moderate deterioration but then improving as growth accelerates.

- Around 4% unemployment by end 2023.



On RBA

- RBA unlikely to increase rates till 2024
- Latest decisions :
  - Did not change rates;
  - Did not role YCC till late 2024 – stayed at April 2024. Implying rates will not be unchanged in late 2024;
  - Did announce a taper in bond buying. From September will buy at $4bn per week (or at a $75bn for 6 months rate compared to the current $100bn per 6 months or $5bn per week). Now to be reviewed in February 2022.
  - The critical variable re timing of rate rises is wages (when will it accelerate to 3%+). We think it will pick up temporarily in H2 this year but not in a sustained way till the second half of 2023. And lockdowns might mute short term increases in wage pressures
- So bottom line, RBA keeping policy as stimulatory as possible – and will respond to actions of other central banks. Markets more sceptical
- But when the RBA moves, suspect it will go hard initially
  - First rise to 50 points
  - And Cash rate to 2% after 12-18 months.

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