# Global Overview & Australia

## COVID, supply chain difficulties and the impact of higher rates. Challenging times ahead.

Alan Oster, Group Chief Economist, December 2022

# Global macroeconomic summary

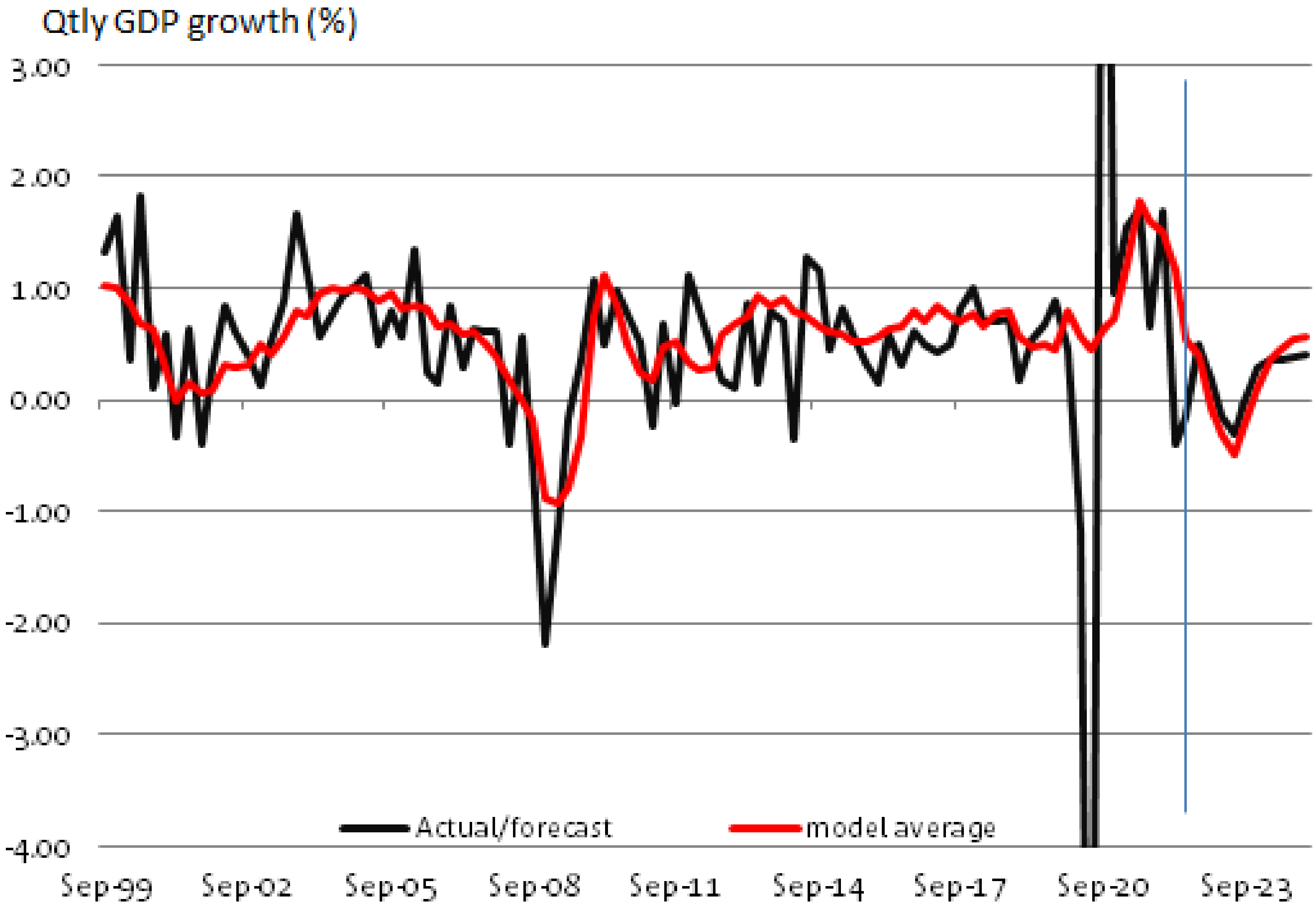
Problems ahead

- There are 3 areas of concern emerging on the global economy:
  1. **China** has seen recent data soften as the combination of the virus and problems in the property market have slowed activity. The central bank has cut rates and added extra liquidity. That said, Chinese vaccines are not providing protection against Omicron – so more lockdowns for longer. We have dramatically cut forecasts to 3.25% in 2022 with a recovery in 2023.
  2. **Russian responses to Ukraine war (effectively closed off gas supplies to Europe) has seen commodity prices spike**. With Ukraine war likely to continue, commodity prices to stay high for some time.
     - Japan is also a concern with growth currently going backwards and only weak growth (1.5%) expected in 2022 and beyond. India also slowing. And obviously, Russia collapsing.
  3. **In the US** the domestic economy weakened a lot in first half of 2022 (now have a "technical recession") and private demand very weak in Q3 (GNE negative again). Fed is very aggressive and seems not to care about the economy. We now see the Fed reaching 4.5 - 5% by early 2023 and cuts in 2024.

     A big worry is that the models point to more trouble ahead with declines in activity in early – mid 2023. And no real growth over 2022 or 2023. Unemployment near 4.5% by Dec 2023 and over 5% by Dec 2024.

# Global macroeconomic summary

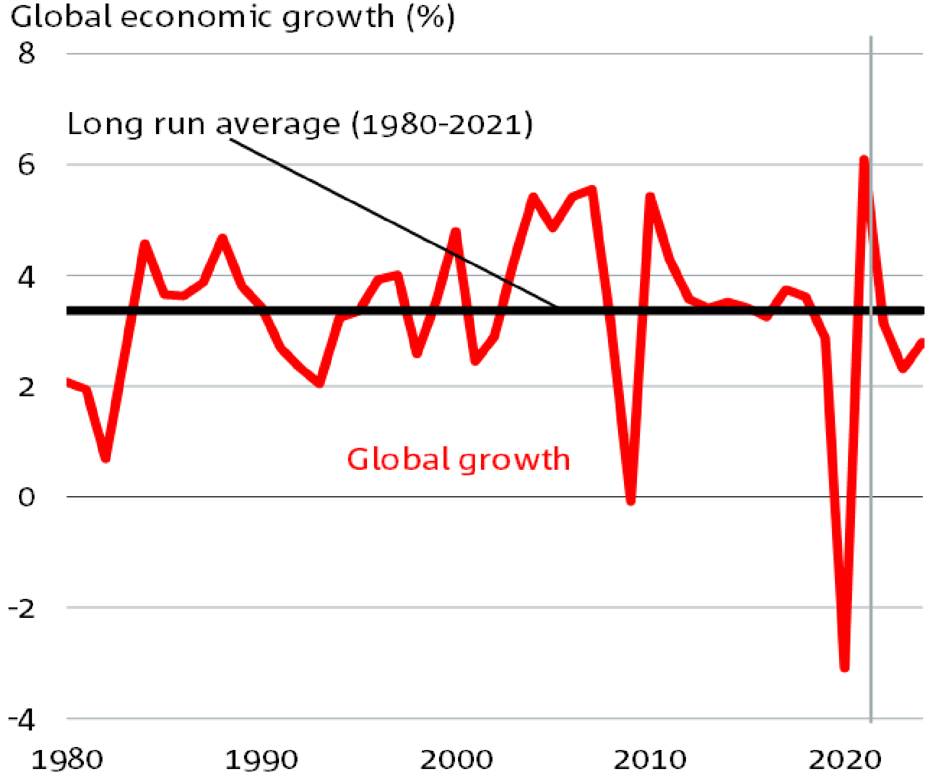
## Problems ahead



# Global economic forecasts

2023, outside of GFC and COVID, the lowest since 1993. We now see major recessions in UK, Europe and the USA in 2023.

| | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|
| US | -2.8 | 5.9 | 1.9 | 0.1 | 1.1 |
| Euro-zone | -6.3 | 5.3 | 3.2 | 0.2 | 1.2 |
| Japan | -4.6 | 1.7 | 1.5 | 1.4 | 0.9 |
| UK | -11.0 | 7.5 | 4.2 | -0.6 | 0.9 |
| Canada | -5.2 | 4.5 | 3.2 | 0.7 | 0.9 |
| China | 2.2 | 8.1 | 3.4 | 5.0 | 4.5 |
| India | -6.6 | 8.3 | 7.3 | 4.4 | 5.6 |
| Latin America | -7.0 | 6.2 | 3.1 | 0.8 | 1.3 |
| Other East Asia | -2.8 | 4.3 | 4.2 | 2.7 | 3.7 |
| Australia | -2.1 | 4.9 | 3.9 | 1.2 | 0.9 |
| NZ | -2.1 | 5.5 | 2.4 | 1.0 | 1.5 |
| **Global** | **-3.1** | **6.1** | **3.3** | **2.2** | **2.8** |



# Australia macroeconomic summary

Still robust but will slow a lot

- **GDP growth to slow to less than 1% during 2023 and 2024 respectively - currently 2.3% through 2022**
  - Economy still robust but either slowing now (NAB internal transaction data) or about to (NAB Business confidence). Near stalling speed by late 2023 and early 2024.
  - Key drivers: slower global growth and rate rises (including fixed loan maturities in mid 2023).
  - Business investment will slow. House prices down another -14% in 2023.

- **Unemployment to remain around current levels (3.4%) for around 6 months**
  - Shortage of skilled labour at record highs.
  - But will rise thereafter to around 4% by end 2023 and 4.5% by late 2024.
  - That is still a good outcome, but risks could be worse.

- **Price inflation to peak soon but stay high**
  - Purchase costs still very high and business is fully passing on prices (maintaining profit margins).
  - Headline around 8% by end 2023 and around 6.8% in core terms.
  - High energy costs and faster wages growth see only moderate slowing in out years – headline around 3% by end 2024 and core 3.2%.

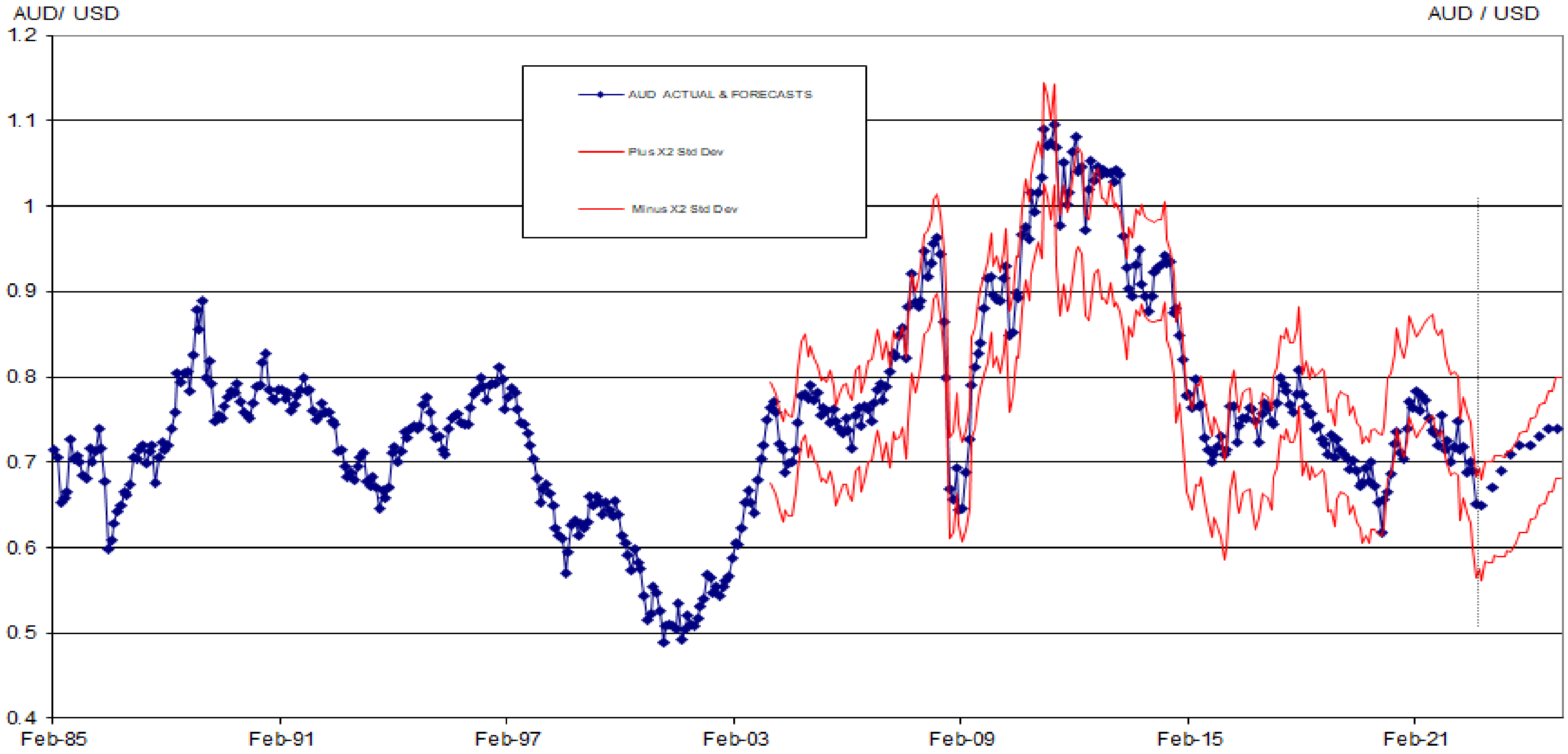
- **Wages growth to accelerate further from here (currently 3.1%)**
  - National wages case has boosted recent numbers and shortage of labour driving wages higher.
  - We see wages growth of 3.8% to 4% going forward.

- **RBA has more to do in the short term**
  - We see 25 point rises in February and March. Cash rate at 3.6% by early 2023.
  - Then wait and see. But remember the effects of rates normally take 12-18 months.
  - RBA less inflation hawks than other central banks.
  - Rate cuts to start by early 2024.

# Currency model USD 0.63+/- 5c

Very much reflecting strength of the USD. Australia a proxy for risk in uncertain world with aggressive central banks. See AUD moving back up as recession hits USD - unemployment moves up and US rates move down.

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 2022 = 65c AUD/USD**

**End 2023 = 72c AUD/USD**

**End 2024= 74c AUD/ USD**

# Data Insights

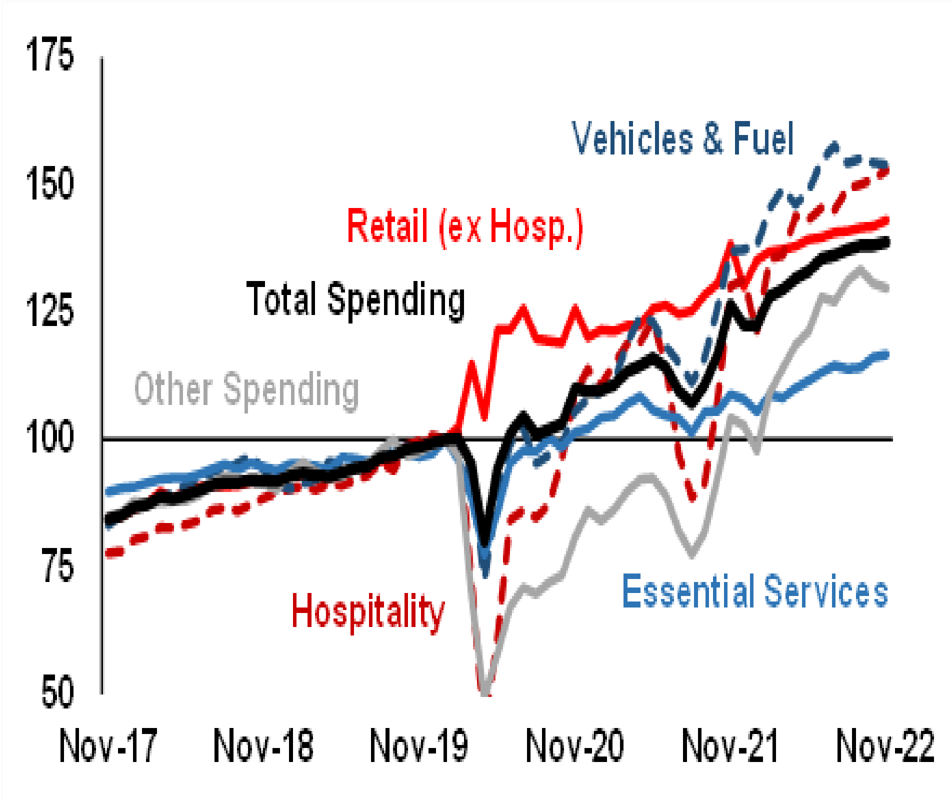
- NAB Data
- Business Survey

# NAB transaction data using monthly data and seasonal factors.

Slowing trend started in retail in October but offset by Black Friday sales in November. Consumption data (including services) softer.

| | Sep-22 | Oct-22 | Nov-22 | | |
|---|---|---|---|---|---|
| | m/m | m/m | m/m | 3m/3m | y/y |
| Goods Retail | 0.4 | 0.2 | 0.9 | 1.2 | 7.3 |
| Hospitality | 0.5 | 0.7 | 1.2 | 3.2 | 37.8 |
| **Total Retail** | **0.4** | **0.3** | **1.0** | **1.7** | **12.9** |
| Vehicles & Fuel | 0.6 | -0.5 | -0.3 | -0.7 | 22.3 |
| Essential Services | 4.5 | 1.5 | -0.3 | 5.9 | 13.6 |
| Other Spending | 1.7 | -2.0 | -0.8 | 2.0 | 41.2 |
| **Total Spending** | **1.2** | **0.0** | **0.4** | **2.0** | **17.9** |

Excludes taxes, rent, mortgages, gambling, finance, insurance, and other non-consumer transactions. Data are seasonallyadjusted and subject to revision.



# Key findings for consumption transaction data based on weekly data.

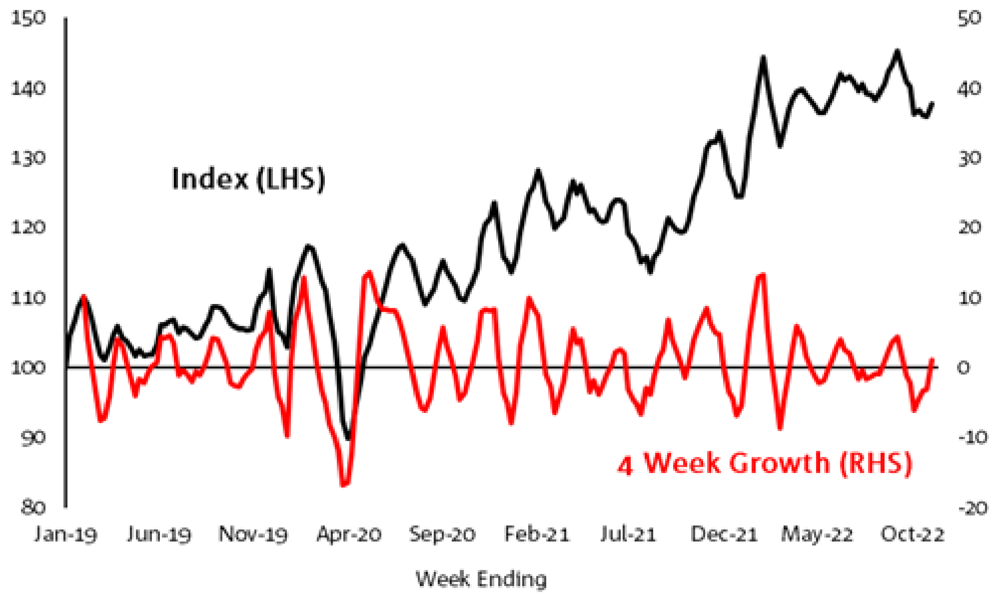
Trend slowing developed during November. But has been erased by Black Friday sales. But this year kick was less than last year. But early days and data volatile.

| | 12/11/2022 | 19/11/2022 | 26/11/2022 |
|---|---|---|---|
| **Total Spending (4wma, s.a.)** | | | |
| 4-week Growth | -3.4 | -3.1 | 1.1 |
| **Sector Growth (4wma, s.a.)** | | | |
| Retail | -2.9 | -2.6 | 3.1 |
| Hospitality | -10.4 | -6.7 | -1.2 |
| Essential Services | 1.2 | -0.9 | 0.1 |
| Other Services | -3.1 | -3.3 | -2.1 |
| **State Growth (4wma, s.a.)** | | | |
| NSW | -1.7 | -1.1 | 3.0 |
| VIC | -3.1 | -3.4 | 0.7 |
| QLD | -0.8 | -0.3 | 3.5 |
| WA | -2.1 | -0.8 | 3.7 |
| Other | -0.6 | -1.0 | 2.0 |

Essential services includes health, education, utilities and communications. Other spending includes arts & rec, transport, construction, and other services. All data seasonally adjusted using monthly factors and subject to revisions.

## Total consumer spending (4wma, s.a.)

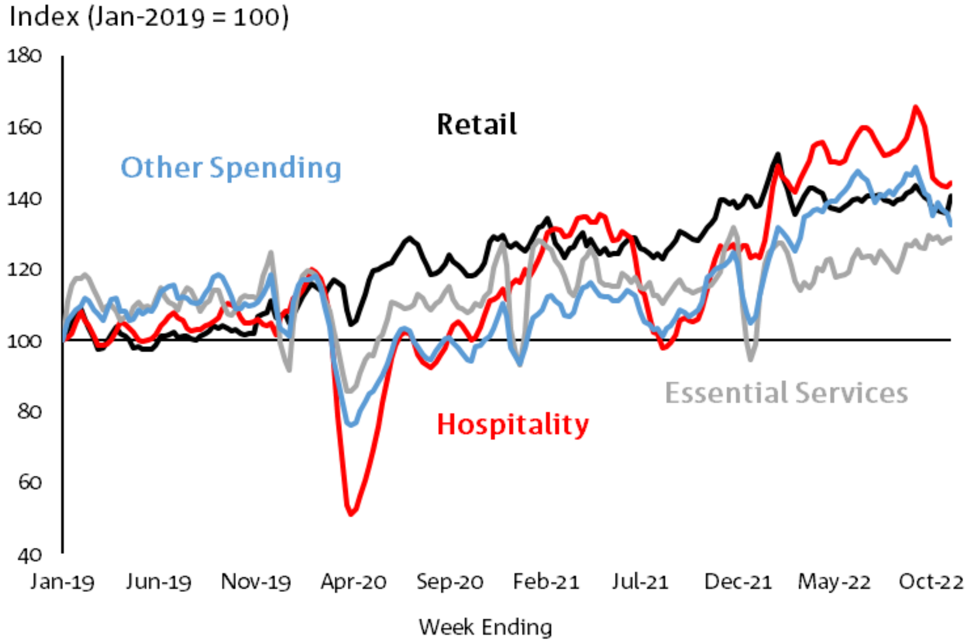
Index (Jan-2019 = 100)



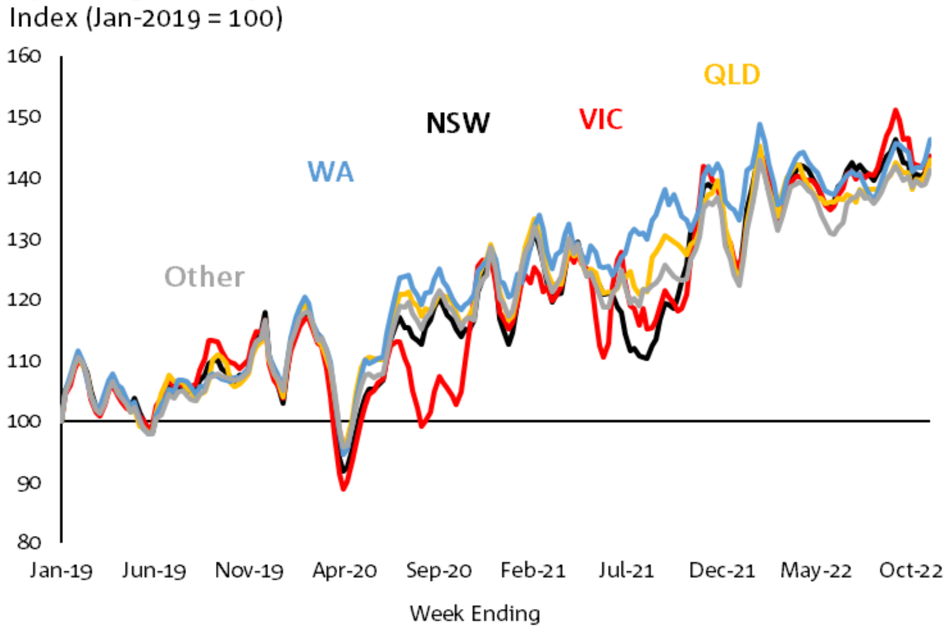
# Key findings for consumption transaction data

Week to 26 November saw retail jump on Black Friday. But suspect softness still there – especially in hospitality. Trends common across all states

## Spending data by sector (4wma, s.a.)




## Spending data by state (4wma, s.a.)



# Black Friday sales in retail strong but not what they were

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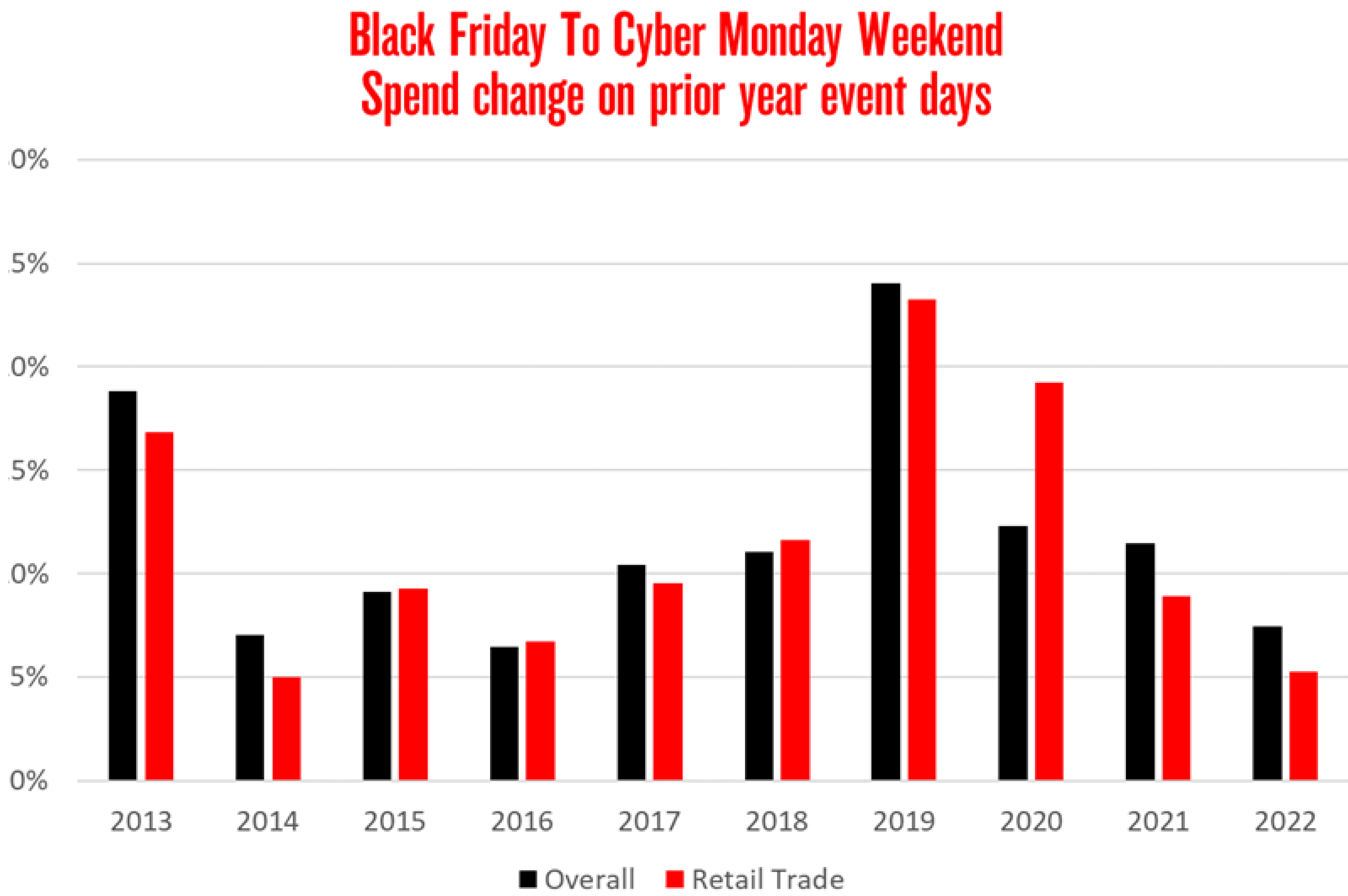
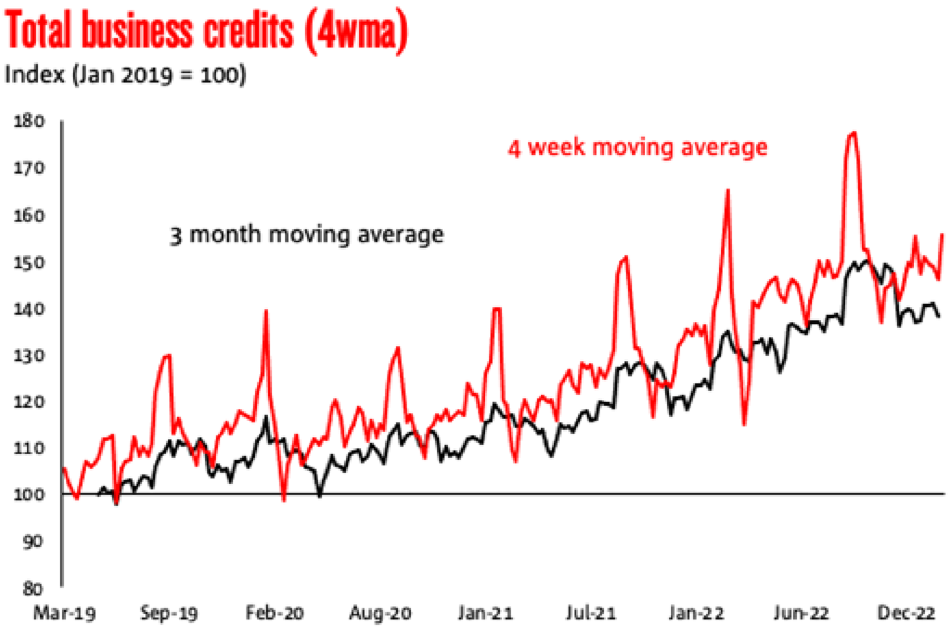
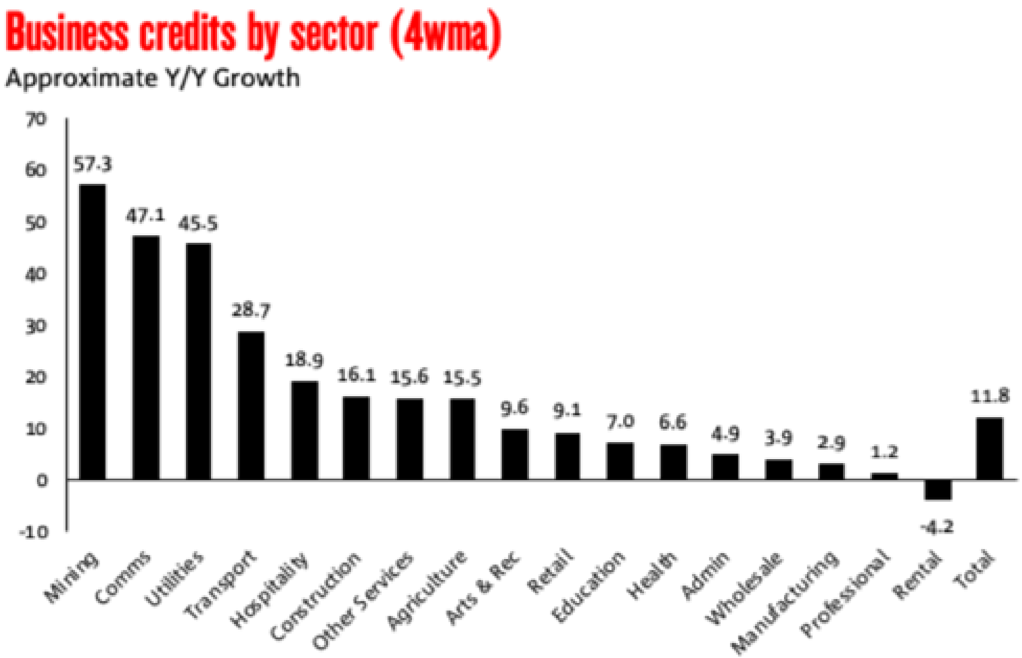


# Business inward credits (business revenues)

Recent trends are still strong. Profit margins are being protected.

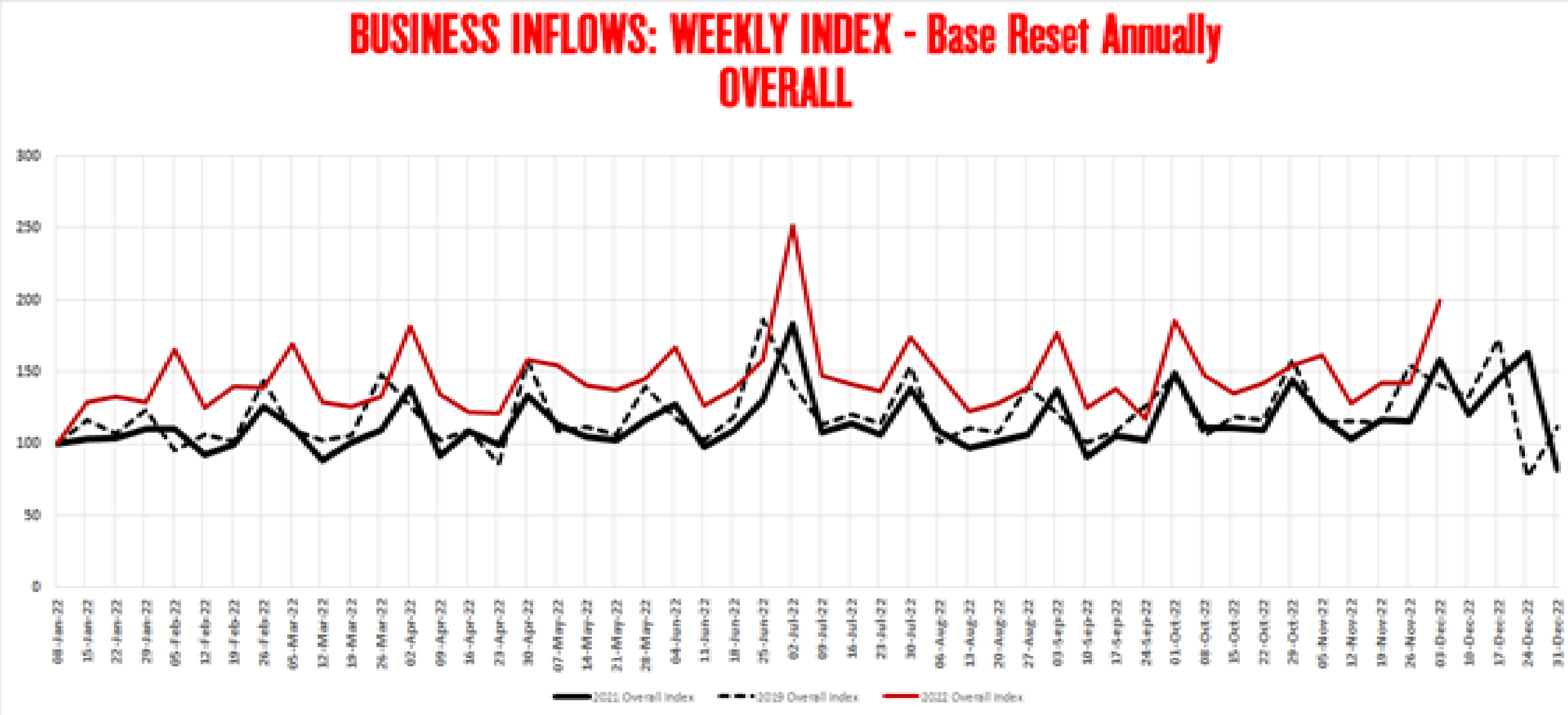
But are differences across sectors over the last year - with utilities and mining strongest.



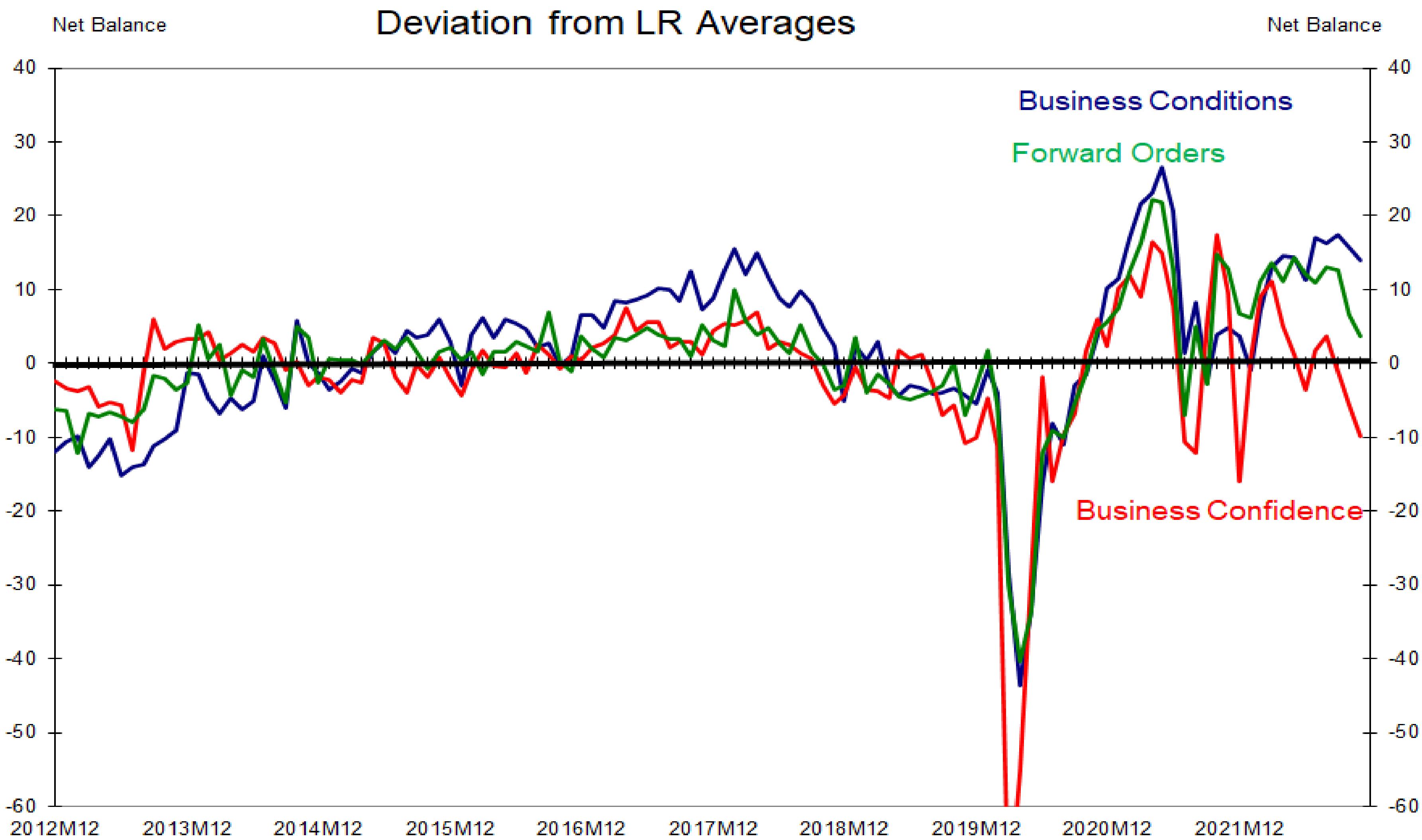
# Business inward credits (business revenues)

Annual reset data. 2019 benchmark to avoid y/y distortions. Again good and better than expected recently.



# Obviously Omicron crunching confidence and conditions during the pandemic.

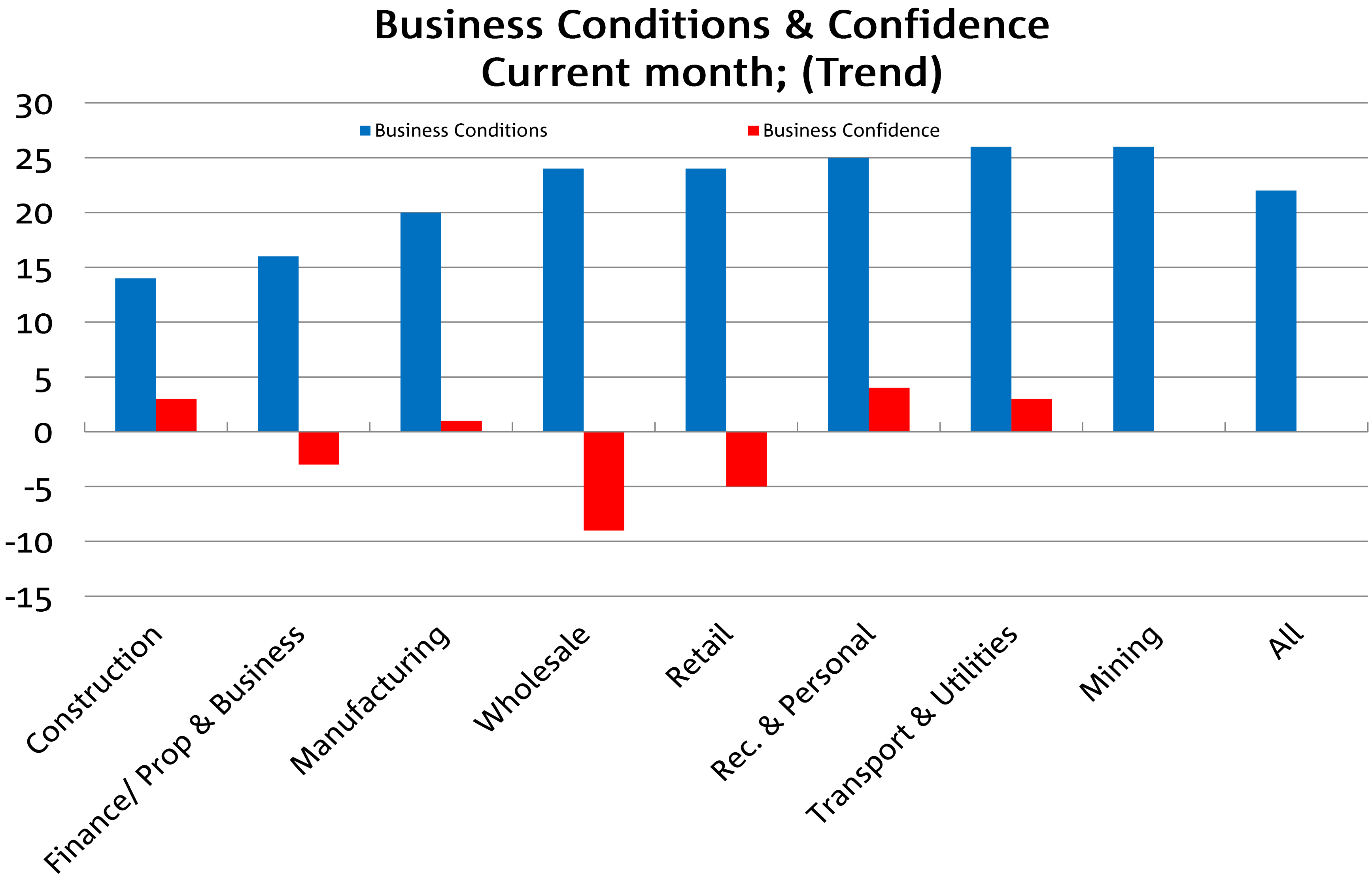
But now interesting re the future. Conditions still very strong. Forward orders good but off a touch. But confidence slipping - purchase costs, supply difficulties and rates. Business expecting a slowdown and seeing it re orders.



# By industry

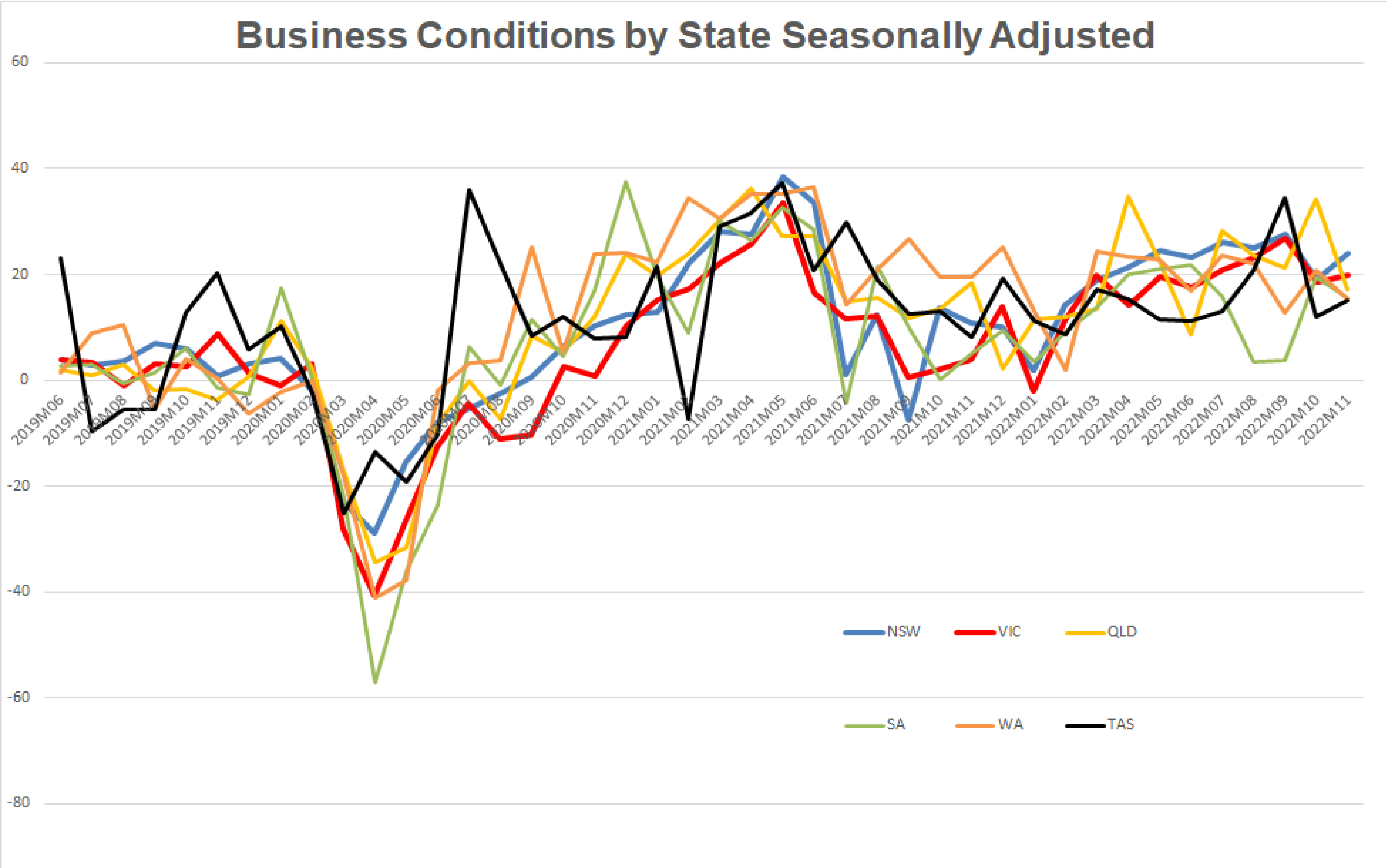
Have seen big improvements in hospitality (personal & rec services). Now middle of the pack. And mining (especially) and retail/wholesale outcomes still strong but confidence an issue. Construction relatively weaker but ok.

**November**



# Similar trends across the states

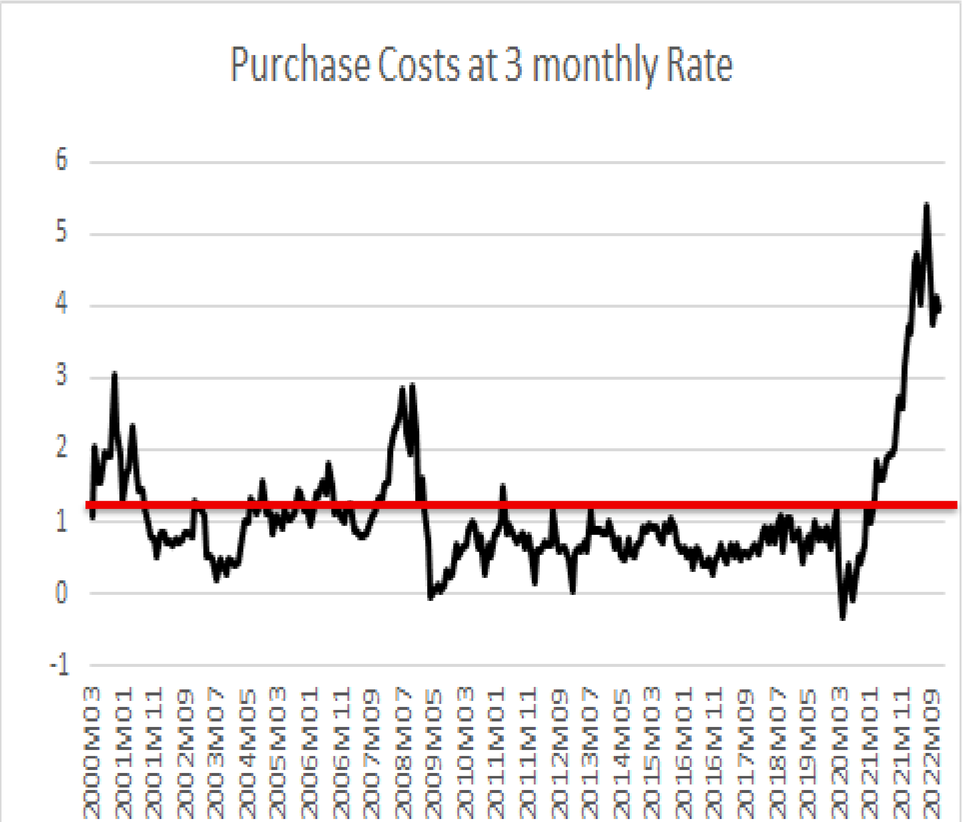
With Qld dropping back and NSW and Vic still strong in November



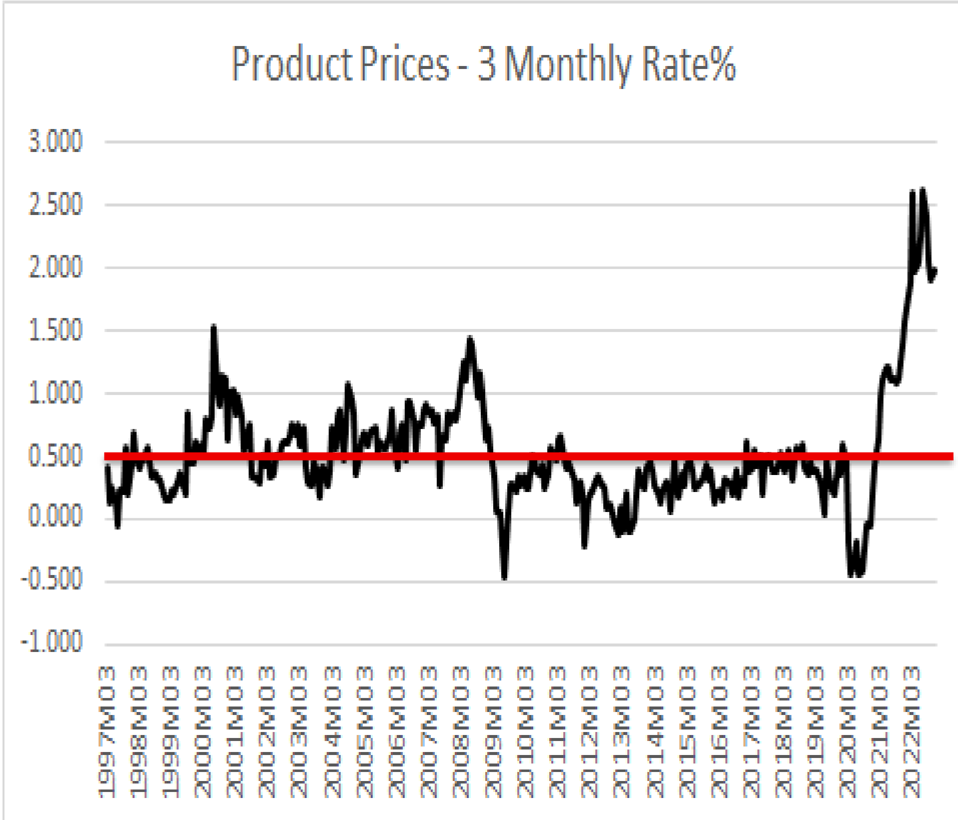
# NAB Business Survey

Clearly showing very high purchase costs, especially construction, manufacturing, wholesale & transport.  Maybe a touch off recent peaks. General prices also still very strong but off a touch as well – including retail.

**Purchase Costs – November NAB Survey**

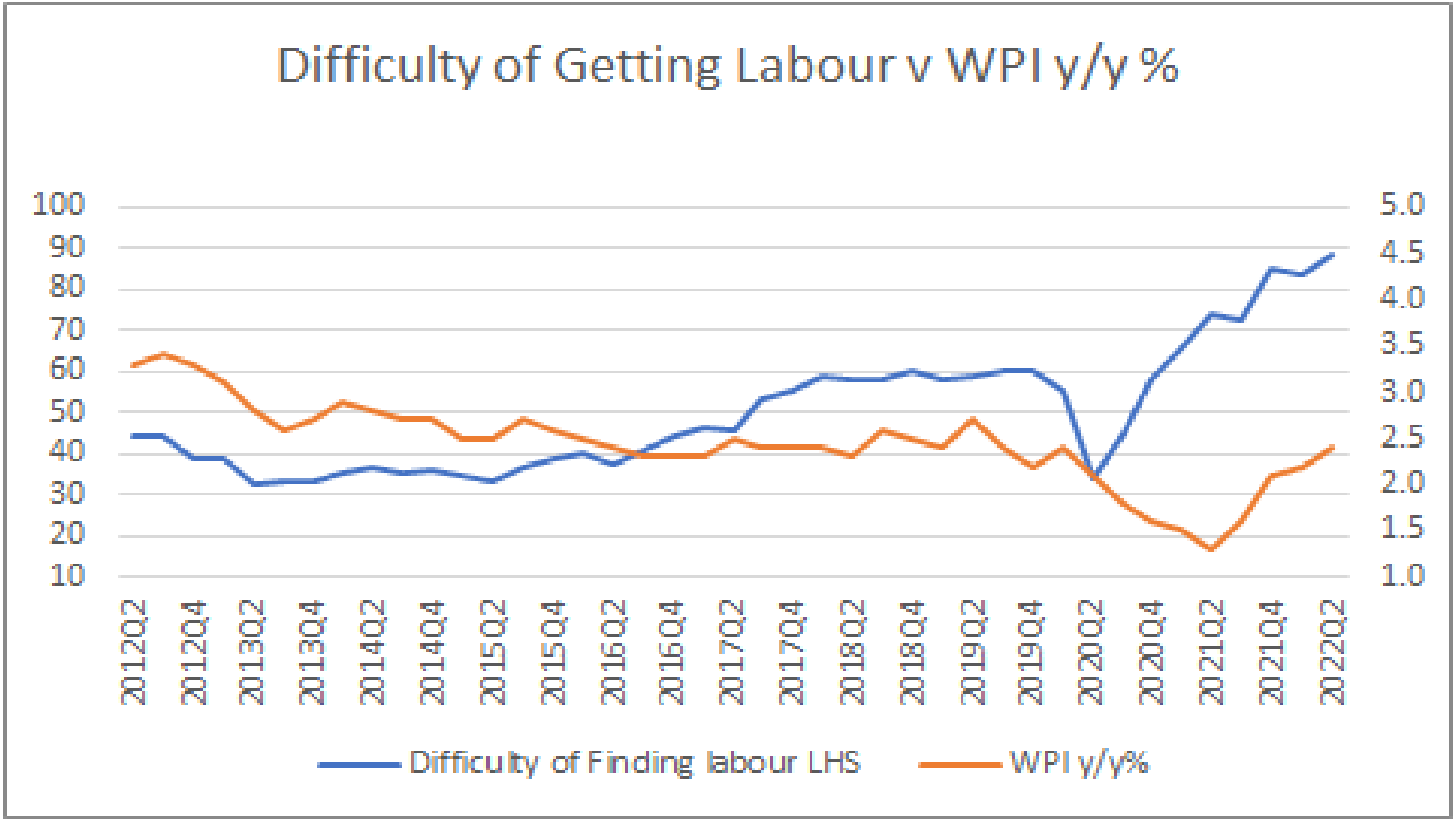



**Goods Costs – November NAB Survey**



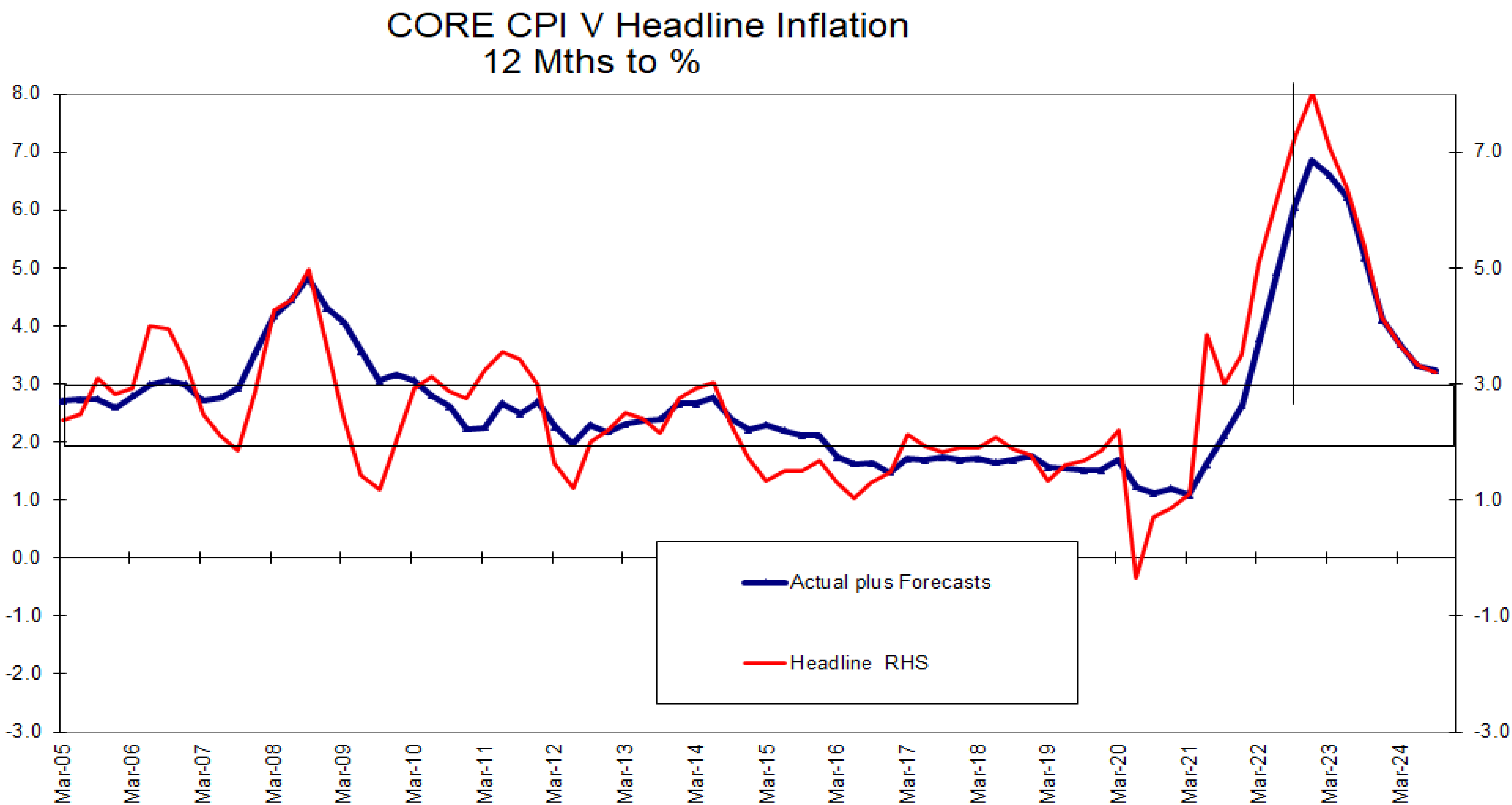
# Obviously labour shortages are a huge issue for business now.

Interesting that the link from labour shortages to wages growth – hasn't been as strong as it used to be.



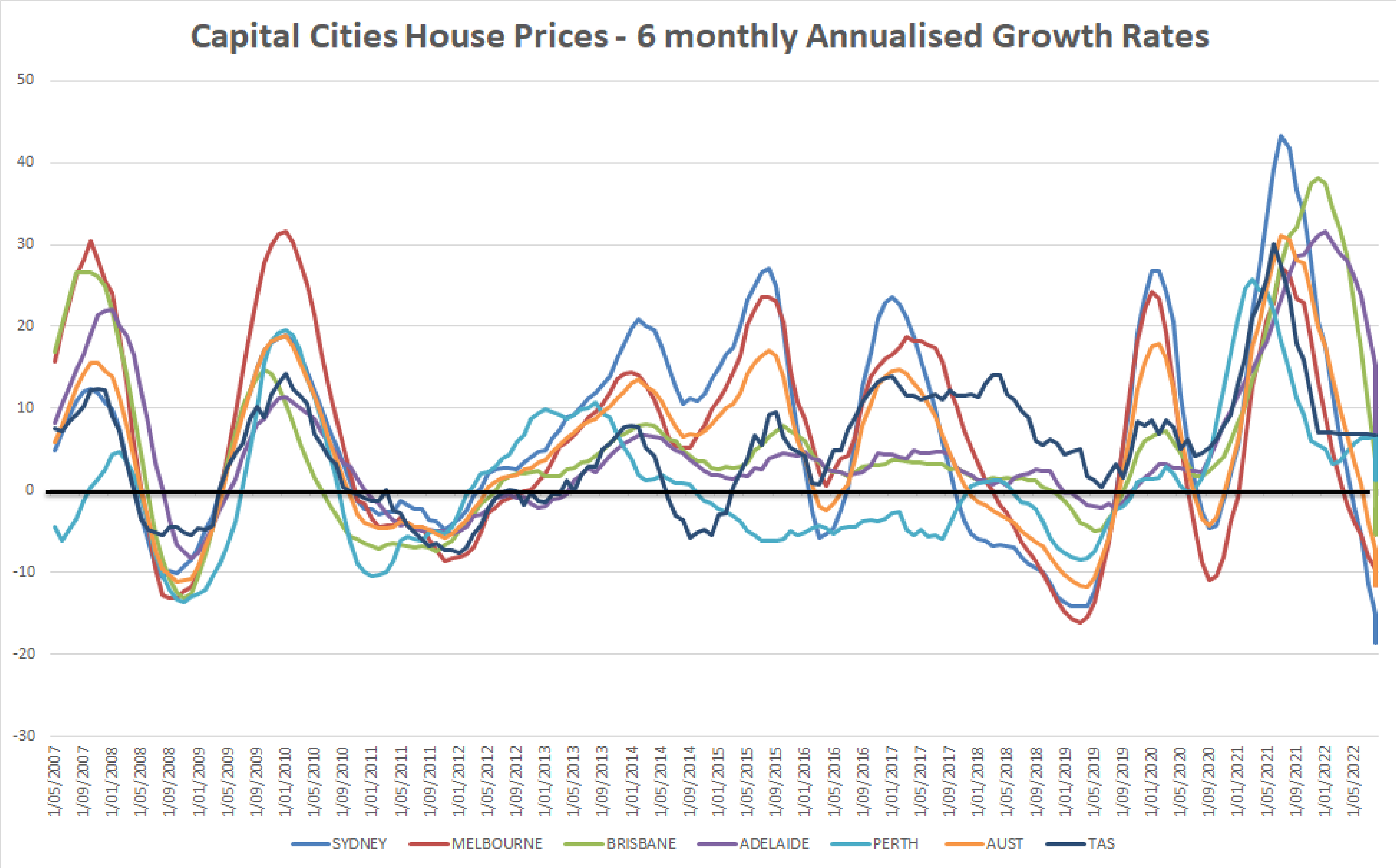
# Core inflation

Hit by supply side problems and higher commodity prices (Russia). Soon trimmed mean core inflation will jump to around 6.8% by end 2022. Core at 3% by end 2024. Headline even higher… around 8% by end 2022.



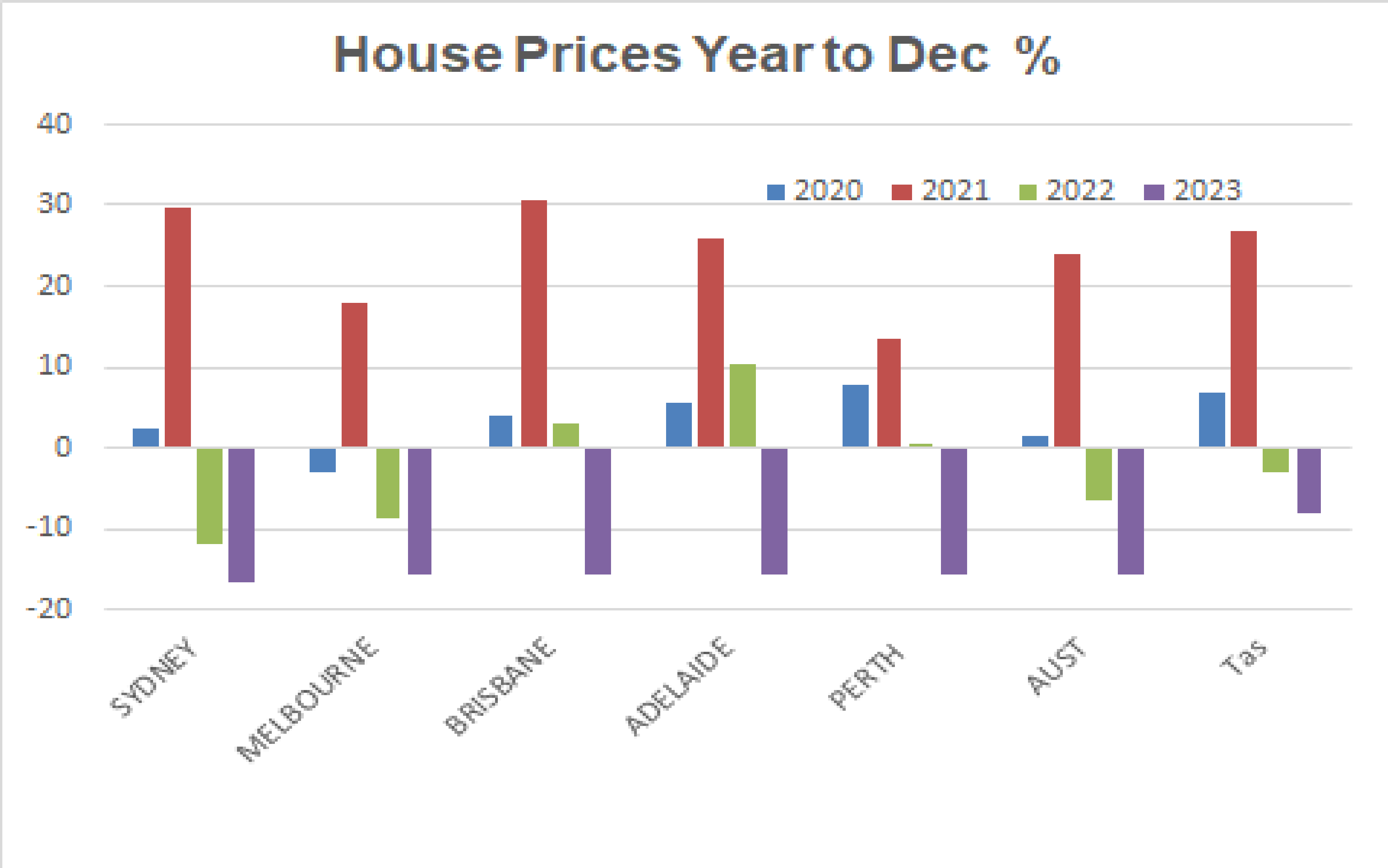
# House prices

Have fallen significantly in Sydney (-18% 6 month annualised) and most other capitals (Melbourne -12% on the same basis). Only Tassie is still ok. Overall annualised 6 monthly rate down -12% to September. Falling faster than we expected.



# House price forecasts

After increasing by around 23% we now expect house prices to be down around -6% in the year ending 2022 (with downside risks). And fall by around 15% during 2023 on the back of rate rises and falling affordability.



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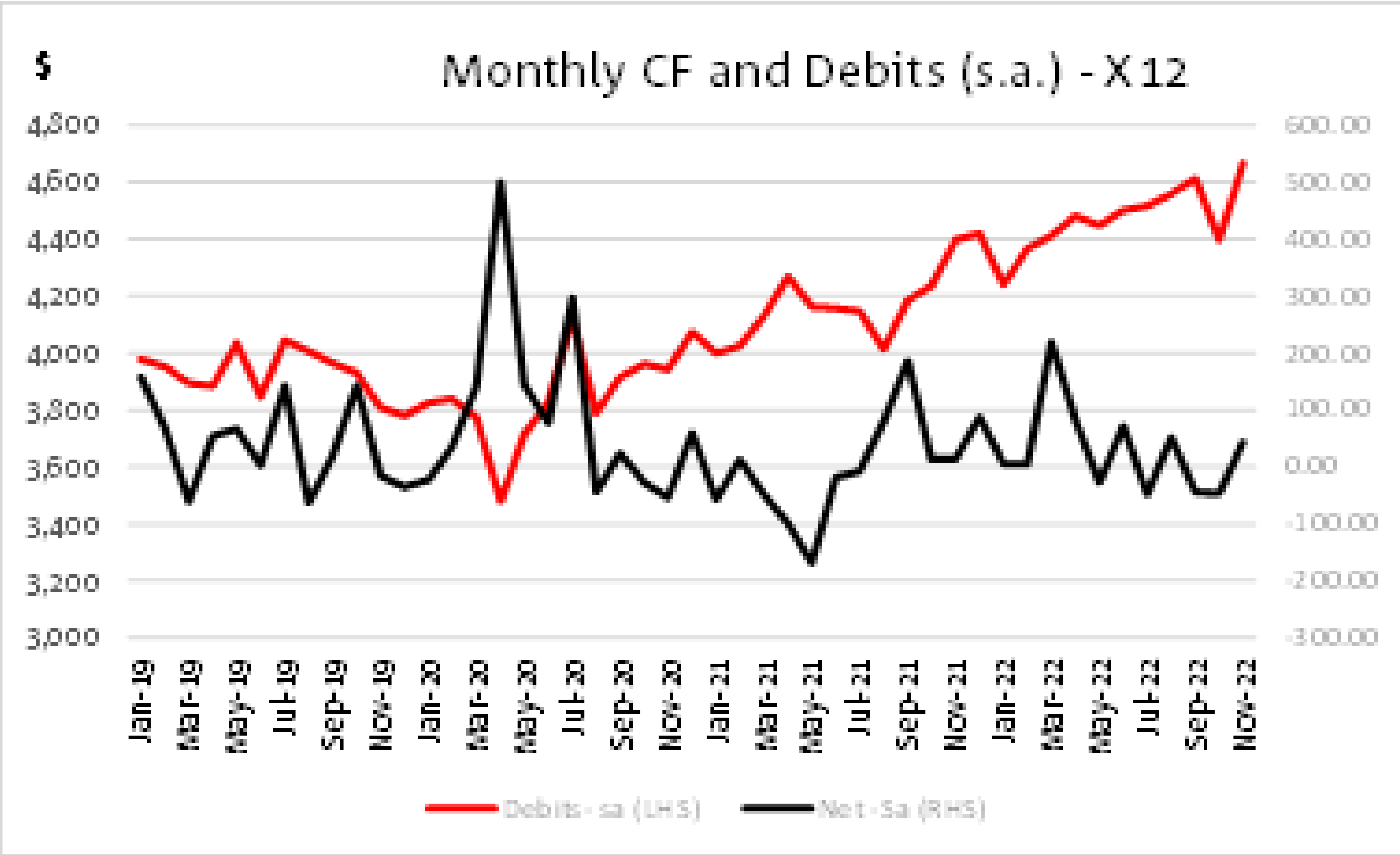
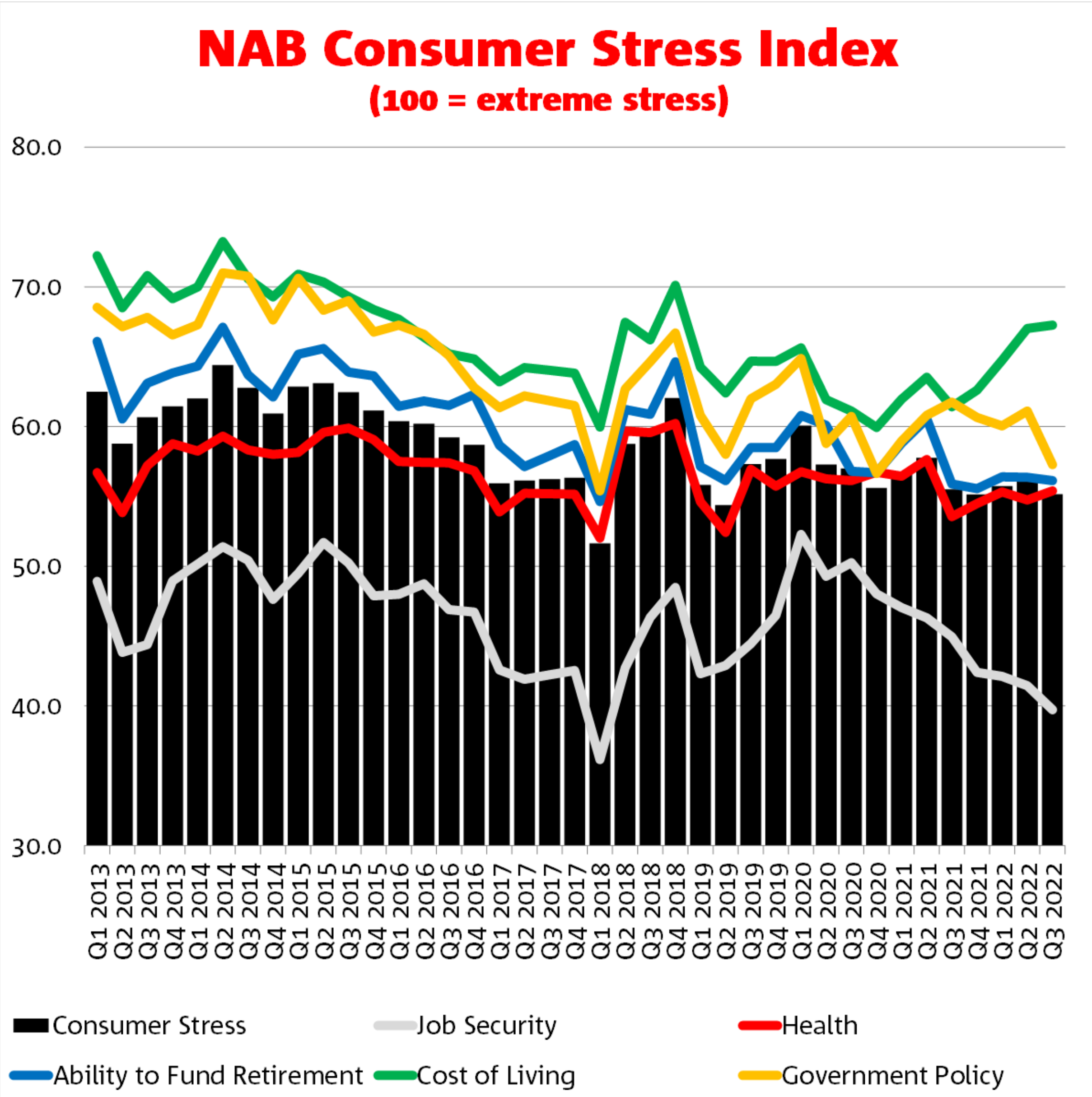
# The combination of falling house prices and global weakness could well see the consumer getting scared.

Already their cash flow is not great. Currently spending as much as they are getting.
Probably enough to sustain growth in 2022 but beyond that???



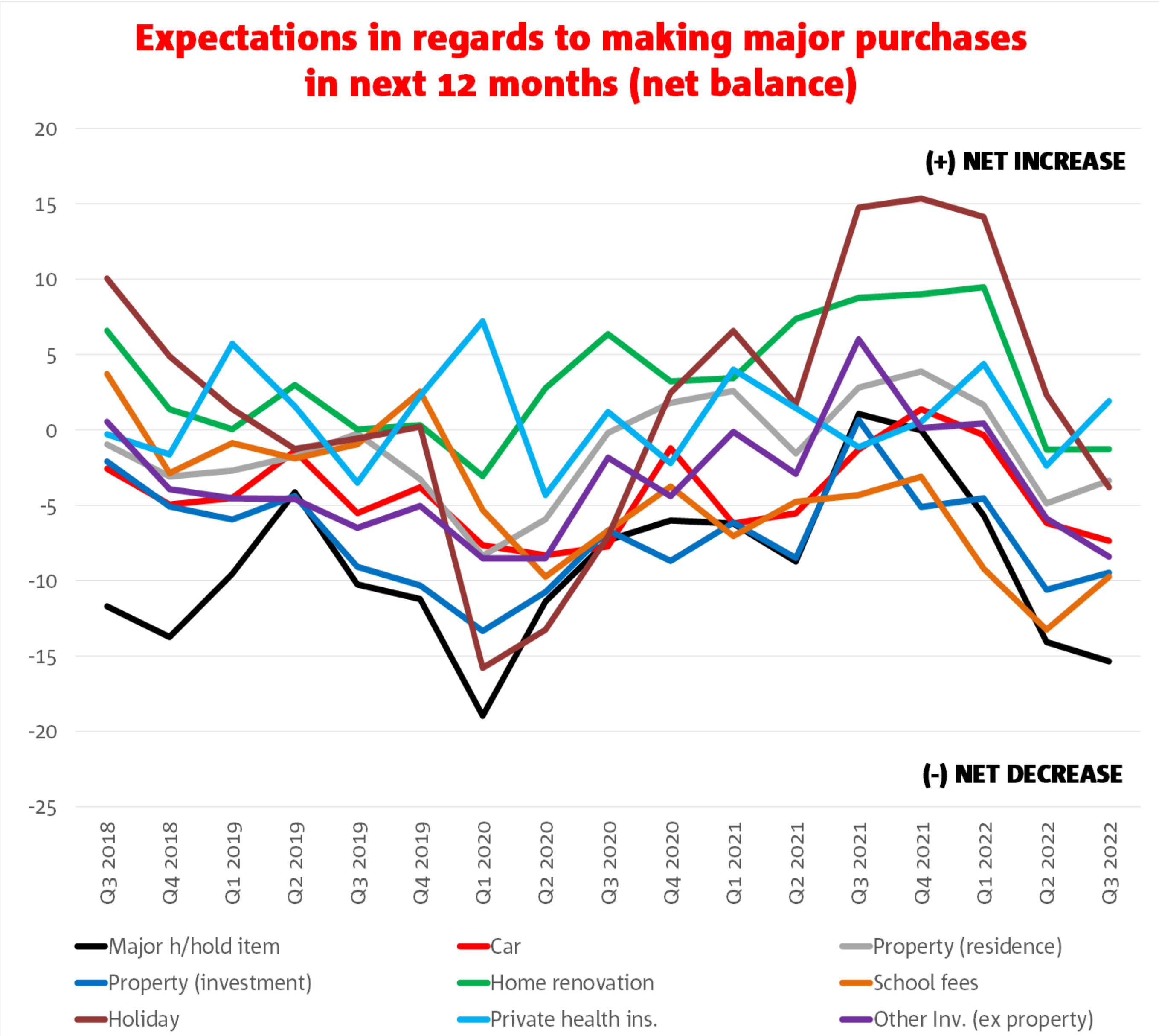
# Consumers are very worried about cost of living

But that is being tempered by the ease of getting a new job



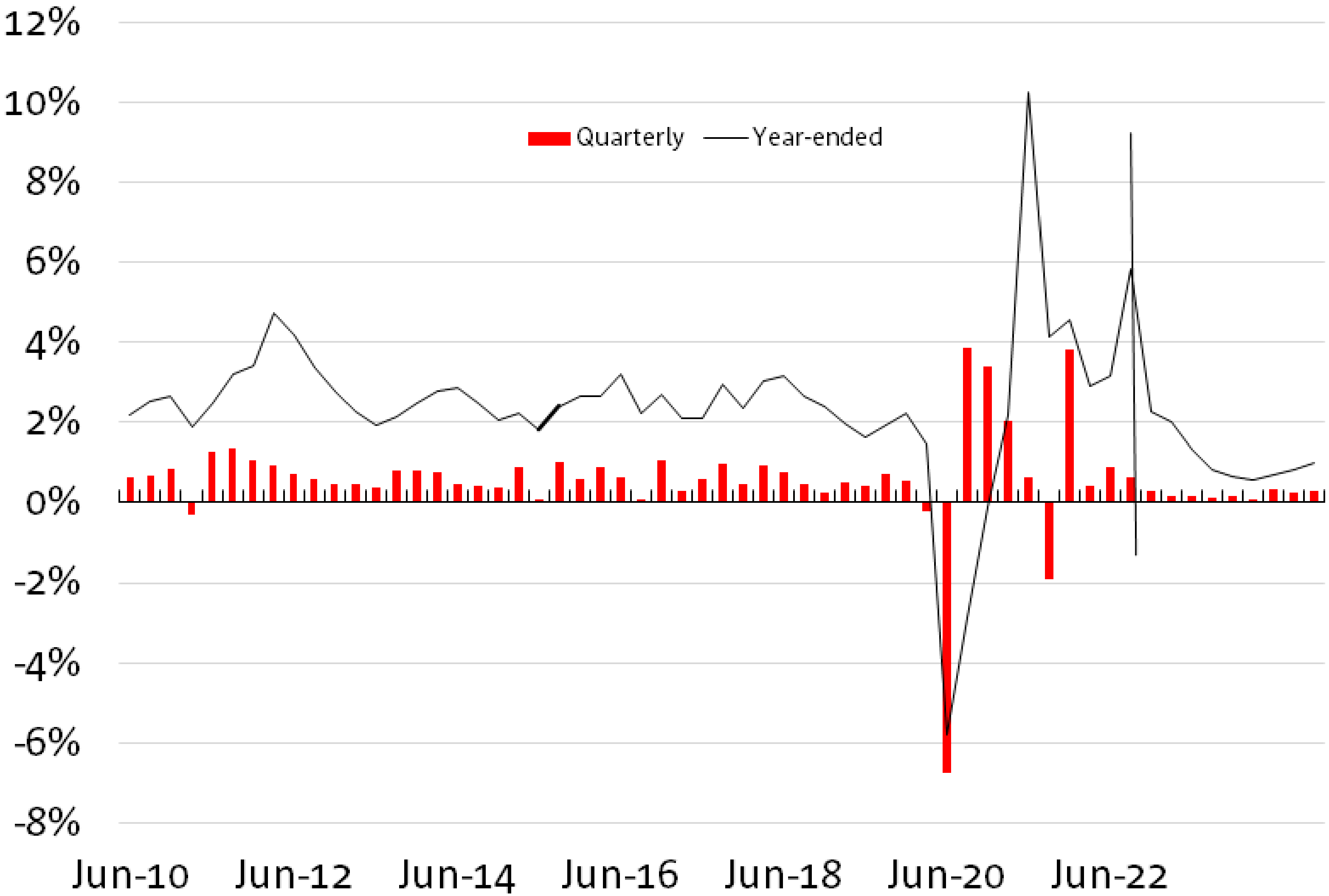
# But they are adjusting plans

Liquidity impact from rate rises to hit from October



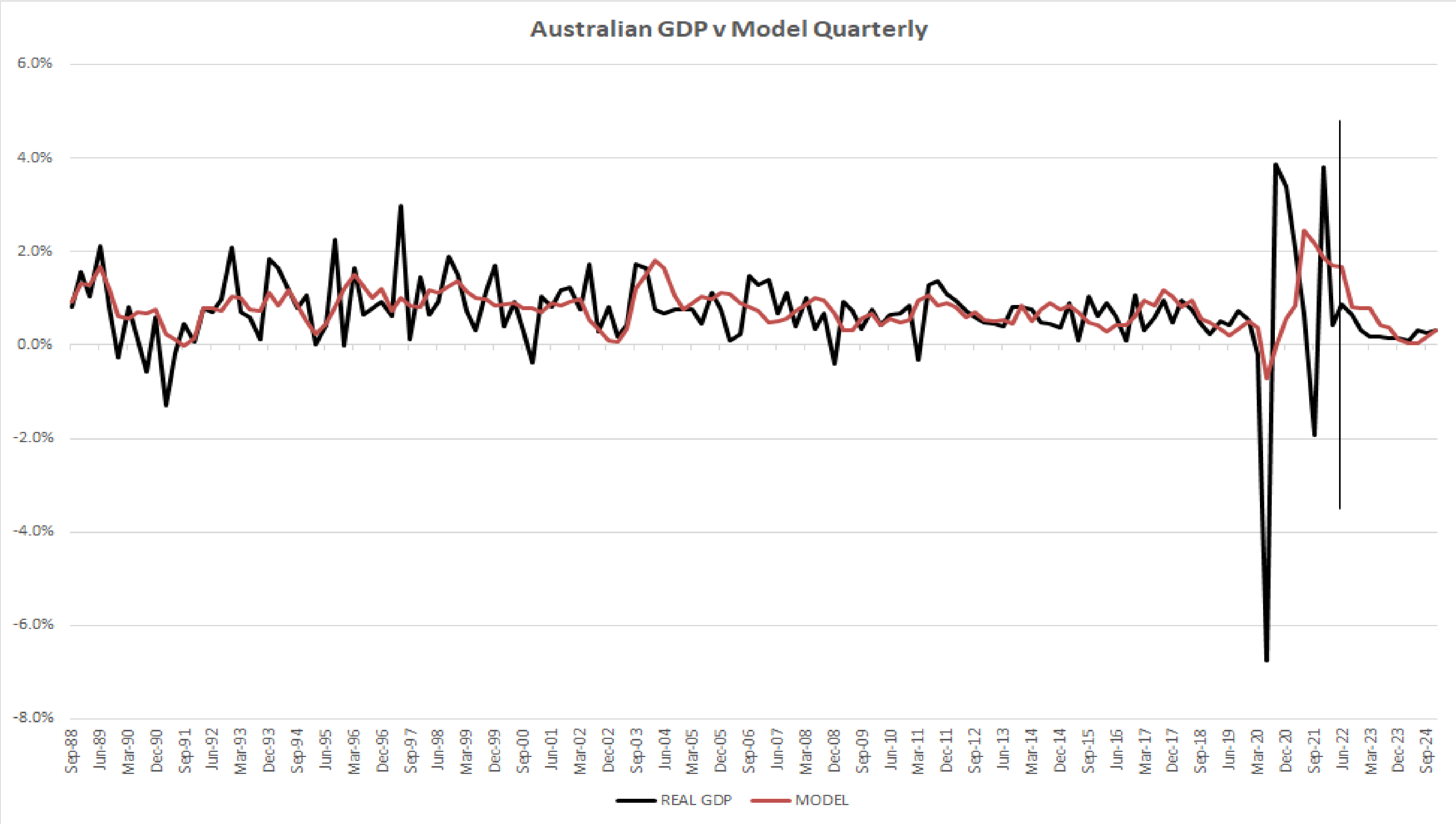
# Our growth expectations.

We see slower growth in late 2022. Economy very flat by late 2023/early 2024.
Not a recession but no room for error.



# My enhanced yield curve equation

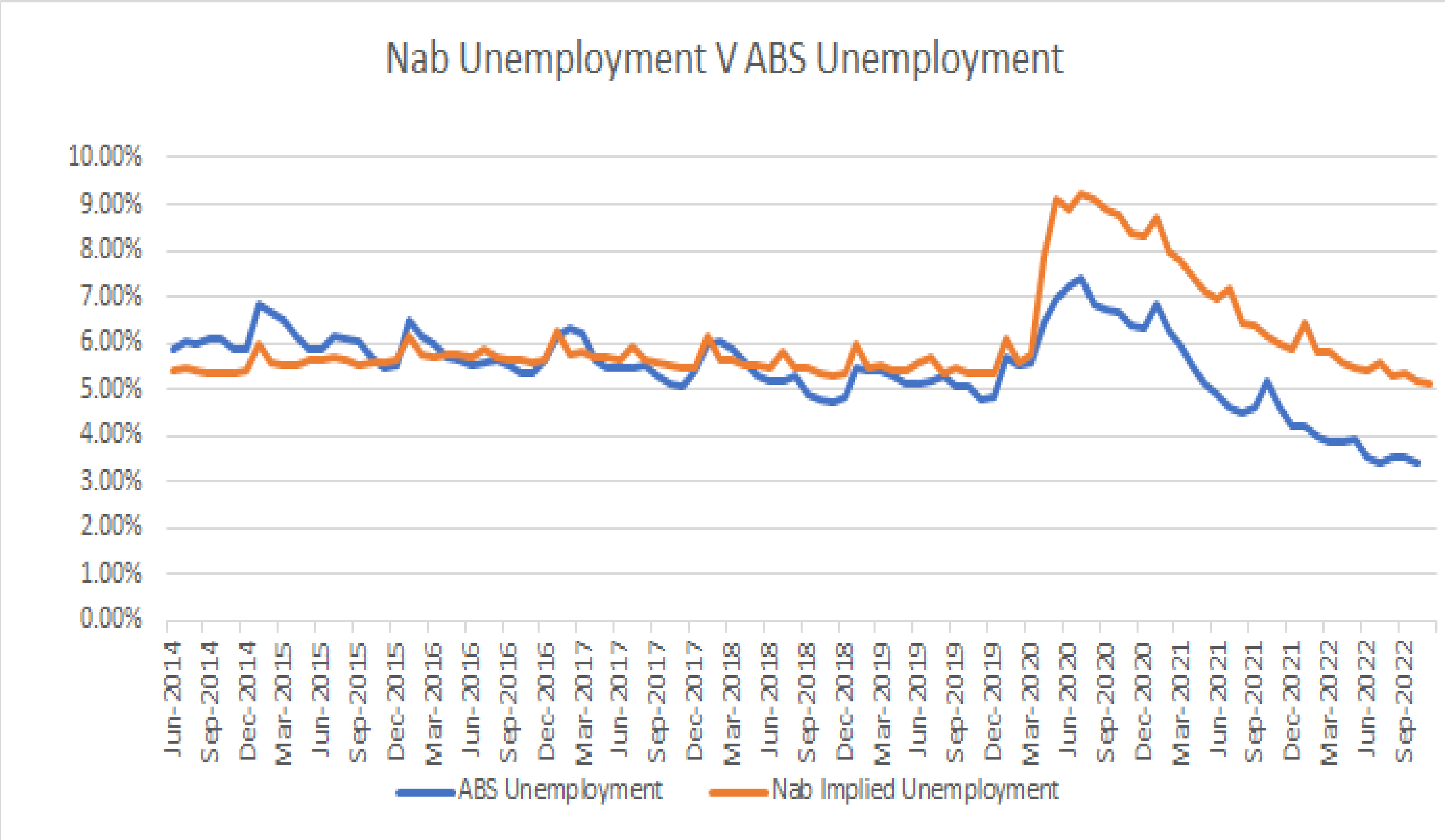
Obviously can't cope with COVID but as we move out of the virus, general trend consistent with the model.




- Model driven by change in real rates (or yield curves), asset prices (house prices and equities), commodity prices, and US growth.
- Quarterly modelled.

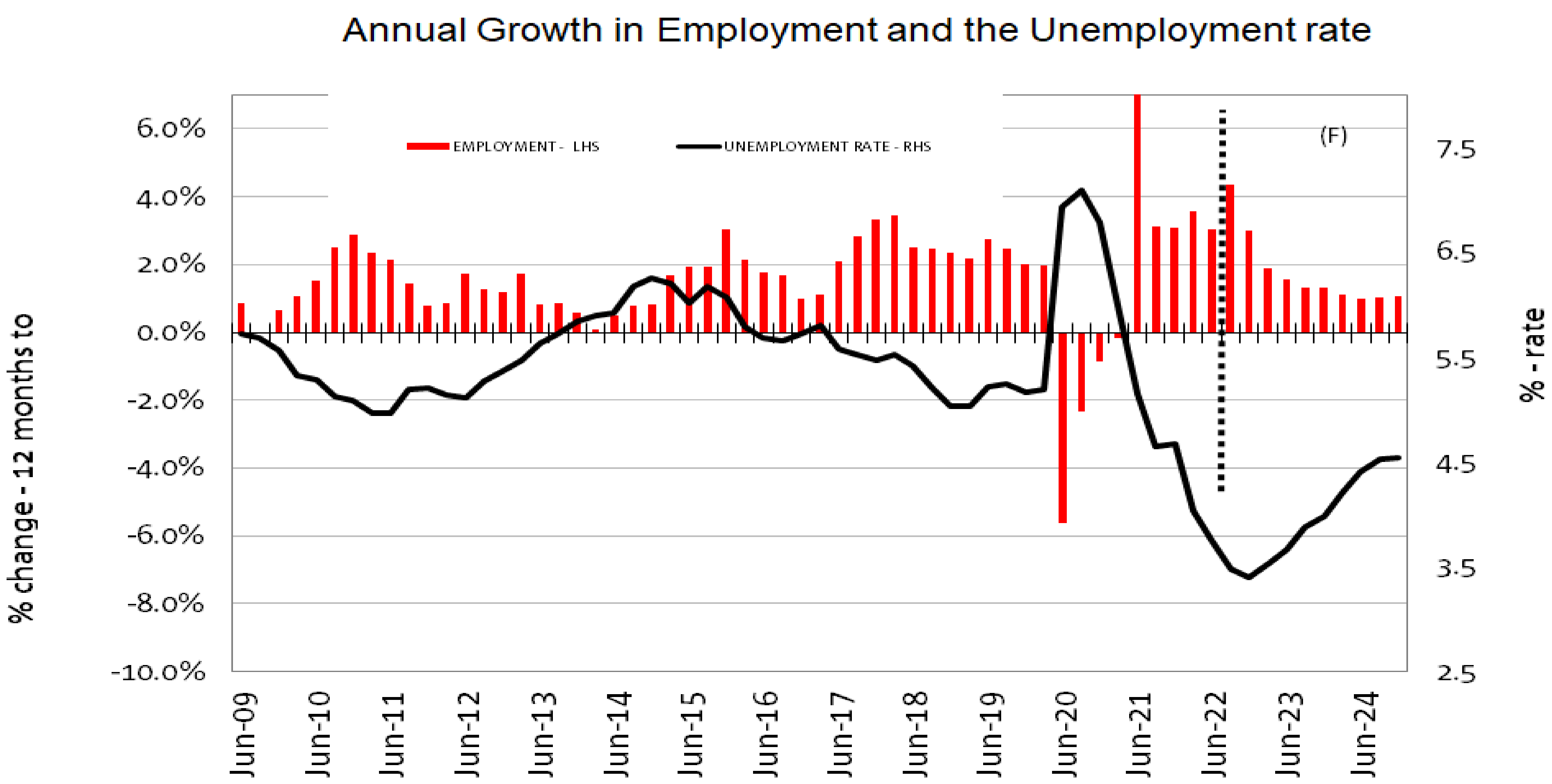
# NAB data on the Claimant Count

(NAB customers receiving JobSeeker) to 10 November. Still fundamentally improving.



# Labour market very impressive

While Omicron hasn't helped, unemployment has fallen to around 3.4% and likely to stay there for another 6 months or so. But as economy fades, unemployment moderately moving up to around 4.3% by end 2024.



# On RBA

- RBA has signalled that it wants to get closer to normal:
  - Fundamentally reflects higher inflation in near term at least;
  - And stronger economy still.
- After a run of rate rises:
  - The RBA has now moved to 25 point adjustments;
  - We see  a further 25 points in February and March;
  - **So a cash rate at 3.6% by early/mid 2023;**
  - RBA will then probably pause and look at reactions in H1 2023;
  - We see rate cuts from early 2024 as the economy struggles.
- Monetary policy takes around 12 months to impact:
  - But by then loan repayments will be up around $800 per month at least and the fixed loans will be rolling off with the peak roll off in early to mid 2023.
- That said, if rates move significantly above 3.6% an even harder landing is possible. Say 40/60 chance.