

Weekly Economic Outlook

10 February 2020

Trend (Growth) is Your Friend

It was a busy week last week for the Reserve Bank (RBA). The Board delivered its cash rate decision where it kept the cash rate on hold at 0.75% and released its updated economic forecasts in its quarterly Statement on Monetary Policy (SoMP). Additionally, Governor Philip Lowe gave his semi-annual testimony to parliament.

One of the key surprises for the week was the more upbeat tone on the economic outlook. The RBA made only minor revisions to its growth outlook, maintaining its forecast for annual growth to return to trend (2.75%) this year. Given the poor reading of GDP in the September quarter, which showed annual growth at just 1.7%, we were expecting the forecast for growth to be downgraded. Our forecast for GDP in 2020 is more pessimistic, at 2.1%. Lacklustre consumer spending and a slower recovery in business and construction investment are expected to hold back growth.

The bushfires and recent coronavirus outbreak are also expected to weigh on growth. The economic impact of the bushfires will likely be contained to the final quarter of 2019 and the first quarter this year, with a recovery bounce later in the year as the rebuilding effort gathers pace. Even assuming that the coronavirus is contained in the first quarter, the hit to economic growth could be more severe. Australia's services exports are likely to be hit especially hard through the tourism and education sectors. Globally, the impact is being felt through exports, transportation and supply chain disruptions.

Reflecting these concerns, on Friday the Australian dollar fell to US\$0.6662, its lowest since March 2009. The Australian dollar is often traded as proxy for global sentiment. The AUD is also highly sensitive to movements in commodity prices and the outlook for Chinese economic growth. As new developments emerge about the coronavirus, the impact has been felt in the AUD. Given it has been testing key levels of support at around US\$0.6662, any further negative news about the coronavirus or other global uncertainties such as the US-China trade war could risk the Australian dollar shifting a further leg down.

In the past the RBA has noted that a low Australian dollar provides a cushion for the domestic economy. Whether or not the weaker currency will be enough to offset the negative shock from the coronavirus amid an already soft growth environment remains to be seen. We expect the RBA will need to cut the cash rate two more times in 2020 in order to make satisfactory progress on its objectives.

Last week, Governor Lowe said that the RBA was balancing the stimulatory effect of monetary easing with the risks attached to low interest rates, primarily runaway household debt. Tomorrow, figures for new housing lending will be released, providing an indication of how quickly new loans are being provided as house prices continue to soar. We forecast a 1.6% increase in the value of new loans in December, led by a 1.7% increase in owner-occupier loans and a 1.6% rise in investor loans. Internationally, the key event is on Wednesday night when Fed Chair Powell testifies before the Senate Banking Panel.

Nelson Aston, Economist

Ph: 02-8254-1316

Forecasts

End Period:	2020					2021
	Close (Feb 7)	Q1 (f)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)
Aust. Interest Rates:						
RBA Cash Rate, %	0.75	0.75	0.50	0.25	0.25	0.25
90 Day BBSW, %	0.92	0.85	0.70	0.45	0.45	0.50
3 Year Swap, %	0.72	0.70	0.60	0.50	0.55	0.60
10 Year Bond, %	1.04	1.00	0.95	0.90	0.80	0.80
US Interest Rates:						
Fed Funds Rate, %	1.625	1.625	1.375	1.125	0.875	0.875
US 10 Year Bond, %	1.58	1.60	1.50	1.45	1.40	1.45
USD Exchange Rates:						
AUD-USD	0.6673	0.68	0.66	0.67	0.67	0.68
USD-JPY	109.75	107	106	105	105	106
EUR-USD	1.0946	1.09	1.10	1.11	1.12	1.13
GBP-USD	1.2892	1.30	1.30	1.30	1.30	1.31
NZD-USD	0.6400	0.66	0.66	0.66	0.66	0.66
AUD Exchange Rates:						
AUD-USD	0.6673	0.68	0.66	0.67	0.67	0.68
AUD-EUR	0.6097	0.62	0.60	0.60	0.60	0.60
AUD-JPY	73.23	72.8	70.0	70.4	70.4	72.1
AUD-GBP	0.5178	0.52	0.51	0.52	0.52	0.52
AUD-NZD	1.0424	1.03	1.00	1.02	1.02	1.03

	2018	2019 (f)	2020 (f)
GDP, %	2.1	2.1	2.1
CPI (Headline), %	1.8	1.8	1.7
CPI (Trimmed mean), %	1.8	1.6	1.9
Unemployment Rate, %	5.0	5.2	5.4
Wages Growth, %	2.3	2.3	2.3

AUD cross exchange rates have been rounded.

Financial forecasts are quarter end.

GDP, CPI, employment and wage growth forecasts are year end.

Contact Listing

Chief Economist

Besa Deda
dedab@banksa.com.au
(02) 8254 3251

Senior Economist

Janu Chan
chanj@banksa.com.au
(02) 8253 0898

Economist

Nelson Aston
nelson.aston@banksa.com.au
(02) 8254 1316

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