

Monday, 11 September 2023

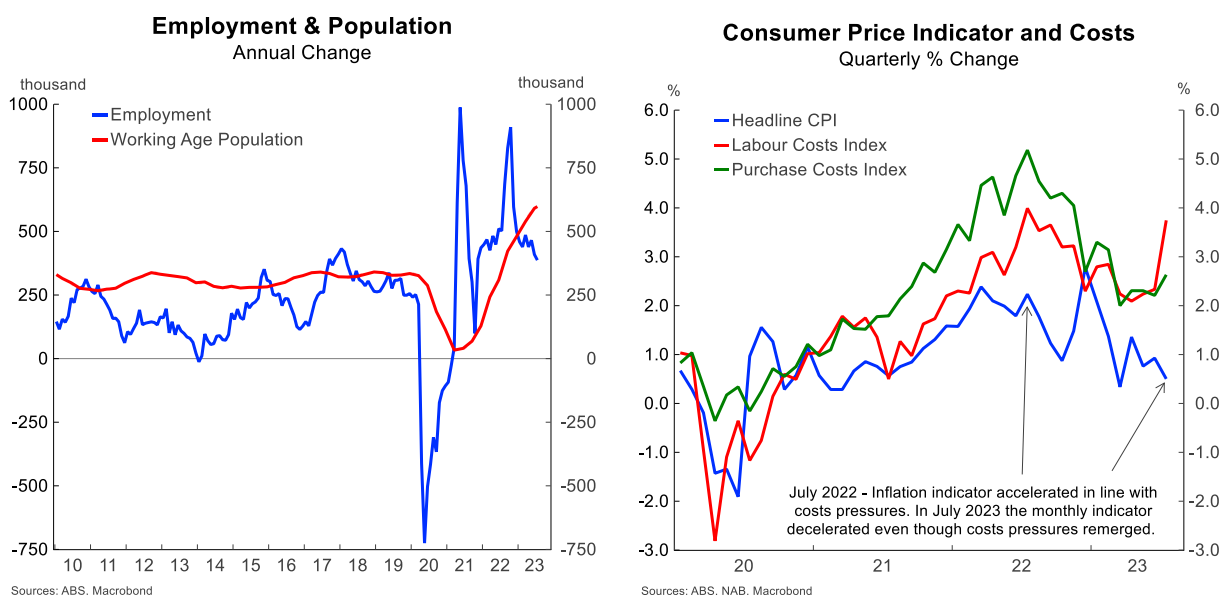
# Labour Market Poised to Bounce Back

After a massive local economic news week, this week will be confined to a small number of important data points, which will help inform the Reserve Bank’s (RBA) next Board meeting in early October.

To recap, last week the RBA left rates on hold for the third consecutive month at 4.10%. There were only a small number of changes to the RBA’s policy statement, but the changes were telling – they point to an RBA that is becoming more confident that inflation is on its way back down to target as the economy is slowing, and labour market conditions are easing.

The June quarter National Accounts confirmed that the Australian economy is slowing. Economic activity expanded by 2.1% over the year to the June quarter, below the rate of 2.3% recorded in March. Growth over the quarter was driven by services exports, business investment, and public investment mainly in infrastructure.

This week we will get an updated read on the health of the labour market. In July we saw a downside surprise in labour market conditions with the number of people employed falling by 14.6k and the unemployment rate ticking up to 3.7%, from 3.5% in June. The outcome was likely impacted by seasonality related to school holidays, which alters when people take their leave and start or leave a job. We’re expecting an unwinding of this seasonal impact and for employment to have increased by 40k over August. We are also expecting the unemployment rate to have ticked down slightly to 3.6%.



Notwithstanding this volatility, we have seen conditions in the labour market ease at the margins. Over the past three months there has been an average monthly job gain of 31k, down from the average monthly gain of 42k over the previous 3 months. As spending slows, we expect to see the

pace of job gains slow further, which will make it harder for people entering the labour force (mostly net overseas migrants) to gain employment. As a result, we see the unemployment rate ticking up to 3.8% by the end of 2023 and 4.7% by the end of 2024.

We will also get an updated read on business conditions over August. We expect conditions to continue to moderate overtime as spending slows. Confidence is also likely to remain subdued given economic headwinds. We will be looking particularly closely at input and labour costs. In July, we saw costs spike mainly on the back of wage increases from the Fair Work Commission's 2023-24 minimum and award wages decision – the decisions took effect from 1 July. The key question is whether businesses can pass on higher costs, or whether the higher costs will eat into margins. If the latter occurs, businesses may be more inclined to scale back employment and output levels, which will reduce inflationary pressures. The monthly inflation gauge showed that the higher costs had limited impact on inflation in July. However, as the inflation gauge shifts toward measuring the prices of services in August and September, we will get a clearer read on the price setting behaviour of firms.

Finally, we will also be keeping a close eye on the impact of three consecutive rate pauses on consumer confidence. The Westpac consumer confidence index showed that households were unfazed over the July rate pause with confidence continuing to remain in deeply negative territory. Since then, we have had a further rate pause and expectations that the RBA has reached the cash rate peak have grown. We have also seen the monthly inflation gauge fall to under 5% (at 4.9%), which was the lowest annual growth rate since January 2022. We could see a bounce in confidence on the back of these positive developments. However, confidence is likely to remain in negative territory, which is consistent with the three consecutive quarters of declines in per capita consumption we saw in the National Accounts. A sustained improvement in confidence would be needed to see a meaningful turnaround in per capita spending – this is a way off in our view.

There will also be important global economic news. Firstly, the US Consumer Price Index (CPI) will be released on Wednesday. The US economy has proven to be more resilient with investors now expecting the Fed to keep rates higher for longer. A stronger than expected inflation read could see equity, foreign exchange and bond markets continue to price in higher rates for longer, which could pose a headwind for the Aussie dollar.

There will also be partial activity data on the Chinese economy. If retail sales and industrial production underwhelm when released on Friday, the Aussie could come under renewed selling pressure.

Finally, the European Central Bank (ECB) meets on Thursday and will deliberate on whether a further rate hike is required to ensure inflationary pressures remain contained. Markets have pencilled in a 40% chance of another 25-basis point hike to a policy target rate of 4.0%. The ECB will need to weigh continued elevated inflation above 5% in annual terms (well above the ECB's 2% target) on the one hand, and slowing growth across the bloc which is showing activity is effectively stagnating, on the other hand.

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## Group Forecasts

End Period:	2023			2024			
	Close (8 Sep)	Q3 (f)	Q4 (f)	Q1 (f)	Q2 (f)	Q3 (f)	Q4 (f)
<b>Aust. Interest Rates:</b>							
RBA Cash Rate, %	4.10	4.10	4.10	4.10	4.10	3.85	3.60
90 Day BBSW, %	4.12	4.30	4.30	4.30	4.22	3.97	3.72
3 Year Swap, %	4.05	4.00	3.95	3.90	3.80	3.70	3.60
10 Year Bond, %	4.08	3.75	3.55	3.45	3.30	3.25	3.20
<b>US Interest Rates:</b>							
Fed Funds Rate, %	5.375	5.375	5.375	5.125	4.625	4.125	3.625
US 10 Year Bond, %	4.26	3.80	3.60	3.40	3.20	3.10	3.00
<b>USD Exchange Rates:</b>							
AUD-USD	0.6376	0.67	0.68	0.69	0.71	0.73	0.74
USD-JPY	147.83	140	138	135	132	130	128
EUR-USD	1.0700	1.11	1.12	1.12	1.13	1.14	1.15
GBP-USD	1.2468	1.28	1.28	1.29	1.29	1.30	1.30
NZD-USD	0.5884	0.62	0.63	0.63	0.64	0.65	0.66
<b>AUD Exchange Rates:</b>							
AUD-USD	0.6376	0.67	0.68	0.69	0.71	0.73	0.74
AUD-EUR	0.5960	0.60	0.61	0.62	0.63	0.64	0.64
AUD-JPY	94.27	93.8	93.8	93.2	93.7	94.9	94.7
AUD-GBP	0.5115	0.52	0.53	0.53	0.55	0.56	0.57
AUD-NZD	1.0838	1.07	1.08	1.09	1.10	1.12	1.12

	2021	2022	2023 (f)	2024 (f)
GDP, %	4.6	2.6	1.0	1.4
CPI (Headline), %	3.5	7.8	3.9	3.2
CPI (Trimmed mean), %	2.6	6.9	3.8	3.1
Unemployment Rate, %	4.7	3.5	3.8	4.7
Wages Growth, %	2.3	3.4	3.8	3.2

AUD cross exchange rates have been rounded.

Financial forecasts are quarter end.

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

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