

Weekly Economic Outlook

Monday, 8 February 2021

Confidence: Can It Be Maintained?

This week is relatively light on domestic economic statistics. However, the corporate reporting season is now underway with companies presenting their outlook and dividend payments. It could also be an interesting week for the AUD as the US haggles over an economic aid package and China prepares for the Lunar New Year.

On Tuesday, the latest NAB survey of business confidence is released, followed on Wednesday by the Westpac / Melbourne Institute Index of Consumer Sentiment. Both have lifted in recent months, but has that optimism been maintained?

COVID-19 hammered business confidence back in April and May. Lockdowns, social distancing, border closures and uncertainty lead to a sharp fall in business confidence. Since then, confidence has picked up. Vaccines are on the way, internal border restrictions have been eased, social distancing restraints have been adjusted and government spending has lifted substantially. On top of these factors, interest rates are at records lows and are set to stay that way until at least 2024. There are good reasons for most businesses to be confident.

The risks to confidence, and to an ongoing economic recovery, are the closure of international borders, the upcoming cutbacks to JobKeeper and JobSeeker and the possibility of new COVID-19 outbreaks. As the RBA continues to tell us, the recovery will be bumpy and uneven and that will flow through into measures of confidence.

The RBA has become more confident in the economic outlook. On Friday it released its latest forecasts. It upgraded GDP in 2020 from a previously expected fall of 4.5% to a fall of 2.0%. Reflecting the pull-forward of activity, the central bank downgraded GDP growth for 2021 from 4.5% to 3.5%. It left GDP growth for 2022 unchanged at 3.5%. It also revised lower its unemployment forecasts. It now expects the unemployment rate to end this year at 6.0% (from 6.5% previously) and end next year at 5.5% (from 6.0% previously).

Consumers have been reacting to the same factors that have lifted business confidence. While one can never predict exactly how consumers are feeling, we suspect that the February reading of consumer sentiment will remain elevated. That would be good news for future retail spending and employment growth.

Since briefly pushing above \$US0.78 in early January, the AUD has drifted lower. This reflected slightly weaker iron ore prices and renewed confidence in the US following the change of administration. With the Lunar New Year period approaching, commodity prices could see some volatility. We expect the AUD to move towards \$US0.79 during the Q2 and then towards \$US0.80 in Q3 as firmer global economic growth sustains commodity prices and the US works to keep its interest rates close to zero.

The corporate reporting season is upon us. Given the rebound in economic activity over the past six months, expectations are relatively high for earnings growth and improved dividends. Should this eventuate, it would be a further positive factor for both consumer and business confidence.

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Forecasts

End Period:	2021					2022	
	Close (5 Feb)	Q1 (f)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)	Q2 (f)
Aust. Interest Rates:							
RBA Cash Rate, %	0.10	0.10	0.10	0.10	0.10	0.10	0.10
90 Day BBSW, %	0.01	0.02	0.02	0.02	0.02	0.04	0.06
3 Year Swap, %	0.14	0.15	0.15	0.15	0.15	0.18	0.22
10 Year Bond, %	1.19	1.05	1.05	1.15	1.25	1.40	1.75
US Interest Rates:							
Fed Funds Rate, %	0.13	0.125	0.125	0.125	0.125	0.125	0.125
US 10 Year Bond, %	1.16	1.10	1.25	1.40	1.50	1.60	1.65
USD Exchange Rates:							
AUD-USD	0.7678	0.78	0.79	0.80	0.82	0.85	0.85
USD-JPY	105.39	104	104	104	104	105	105
EUR-USD	1.2046	1.22	1.23	1.24	1.25	1.26	1.27
GBP-USD	1.3735	1.37	1.37	1.38	1.39	1.41	1.41
NZD-USD	0.7198	0.73	0.74	0.75	0.76	0.78	0.78
AUD Exchange Rates:							
AUD-USD	0.7678	0.78	0.79	0.80	0.82	0.85	0.85
AUD-EUR	0.6372	0.64	0.64	0.65	0.66	0.67	0.67
AUD-JPY	80.92	81.1	82.2	83.2	85.3	89.3	89.3
AUD-GBP	0.5591	0.57	0.58	0.58	0.59	0.60	0.60
AUD-NZD	1.0663	1.07	1.07	1.07	1.08	1.09	1.09

	2019	2020 (f)	2021 (f)	2022 (f)
GDP, %	2.2	-2.0	4.0	3.0
CPI (Headline), %	1.8	0.9	2.6	2.2
CPI (Trimmed mean), %	1.6	1.2	1.9	2.0
Unemployment Rate, %	5.2	6.8	6.0	5.3
Wages Growth, %	2.2	1.0	1.1	1.5

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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