# Weekly Economic Outlook

Tuesday, 9 June 2020

# Everything is Fine

There has been a major shift in sentiment over the past couple of weeks in financial markets where risk has been significantly reassessed. Market participants view a stronger recovery for the global economy, with restrictions lifting and economies reopening.

Share markets have come up a long way from their lows – the S&P500 has lifted 44.5% from its low hit on March 23, and is just 4.5% down from its record high hit earlier this year. In Australia, the ASX200 is up around 35.2% from its low also on March 23 and is down 14% from this year's peak.

The improvement in sentiment has also been reflected in the Australian dollar, which hit a high of 70.41 US cents this morning, its highest so far this year and meeting our short-term target outlined in our daily morning report on April 30. The successful containment of COVID-19 in Australia and the RBA ruling out the prospect of negative interest rates are other factors helping to prop up the Australian dollar.

There is reason to be more optimistic .The focus is mostly on recovery, which is suggesting that this global recession is deep, although shorter than previous downturns.  The expectations of ongoing easy monetary policy measures and ultra-low interest rates are also likely playing a part in propping up sentiment.

A surprising lift in US jobs in May also highlights that recovery is probably occurring quicker than previously expected. Expectations were for a decline of 7.5 million jobs and for the unemployment rate to rise to 19.0%. Instead, jobs lifted 2.5 million, and the unemployment rate fell from 14.7% to 13.3%. There was a classification error but even accounting for this error, the jobless rate would have fallen short of consensus expectations.

But just as when we tell ourselves and everyone else 'everything is fine', there are factors which continue to make us wary that a correction in sentiment could occur soon.

The prospect of further escalating tensions between the US and China remains a risk for the global economy. It will take some time to recover the jobs and economic activity that has been lost. COVID-19 cases remain high globally, including in the US, although there hasn't been much sign of delay in lifting restrictions as yet.  Markets might be under-estimating the level of risks to the global economy.

Nonetheless, recovery is likely to be in place and even if we do not return to the same levels of economic activity prior to the crisis any time soon, the uncertainty and fear with regards to the outlook has significantly improved from a few months ago.

This recovery and lifting of restrictions are expected to be reflected in measures of sentiment to be released this week. Business confidence and conditions, released today, revealed another improvement in May, but they remain at very low levels. The Westpac-Melbourne Institute consumer sentiment index is to be released tomorrow. The index bounced significantly in May, although it remains firmly in pessimistic territory.

The other key local data will be housing finance, which is also due to be released tomorrow. April is expected to show a large decline in the number of loans approved for both owner occupiers and investors. Housing turnover has dropped sharply, and there may have delays to processing in transitioning work environments safe from COVID-19.

Overseas, the key highlight is the Federal Reserve meeting on Wednesday night. Federal Reserve Chair Powell has indicated an openness to do more for a stronger recovery, but the question lies in what measures these could entail. Negative interest rates do not seem like a popular option for most Fed officials, although a paper from the St.Louis Fed has argued that they should be considered. Recent commentary has hinted at yield-curve control as a possibility, which is similar approach to the RBA's style of quantitative easing. The RBA targets around 0.25% on the 3-year government bond yield.

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*Forecasts are detailed on the following page*

## Forecasts

*Please note that due to the unprecedented nature of the coronavirus's impact on the economy and the rapid change of developments, there is greater than usual variability attached to these forecasts.*

| | | | 2020 | | | 2021 |
|---|---|---|---|---|---|---|
| **End Period:** | **Close (June 8)** | **Q2 (f)** | **Q3 (f)** | **Q4 (f)** | **Q1 (f)** | **Q2 (f)** |
| **Aust. Interest Rates:** | | | | | | |
| RBA Cash Rate, % | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 |
| 90 Day BBSW, % | 0.10 | 0.10 | 0.10 | 0.15 | 0.20 | 0.25 |
| 3 Year Swap, % | 0.28 | 0.25 | 0.30 | 0.30 | 0.35 | 0.35 |
| 10 Year Bond, % | 1.09 | 0.90 | 0.90 | 0.95 | 1.00 | 1.10 |
| **US Interest Rates:** | | | | | | |
| Fed Funds Rate, % | 0.125 | 0.125 | 0.125 | 0.125 | 0.125 | 0.125 |
| US 10 Year Bond, % | 0.88 | 0.65 | 0.65 | 0.70 | 0.75 | 0.80 |
| **USD Exchange Rates:** | | | | | | |
| AUD-USD | 0.7021 | 0.68 | 0.66 | 0.68 | 0.70 | 0.70 |
| USD-JPY | 108.43 | 107 | 105 | 106 | 107 | 107 |
| EUR-USD | 1.1294 | 1.11 | 1.09 | 1.10 | 1.11 | 1.11 |
| GBP-USD | 1.2724 | 1.25 | 1.23 | 1.24 | 1.25 | 1.26 |
| NZD-USD | 0.6560 | 0.63 | 0.60 | 0.61 | 0.62 | 0.62 |
| **AUD Exchange Rates:** | | | | | | |
| AUD-USD | 0.7021 | 0.68 | 0.66 | 0.68 | 0.70 | 0.70 |
| AUD-EUR | 0.6216 | 0.61 | 0.61 | 0.62 | 0.63 | 0.63 |
| AUD-JPY | 76.13 | 72.8 | 69.3 | 72.1 | 74.9 | 74.9 |
| AUD-GBP | 0.5518 | 0.54 | 0.54 | 0.55 | 0.56 | 0.56 |
| AUD-NZD | 1.0703 | 1.08 | 1.10 | 1.11 | 1.13 | 1.13 |

| | **2019** | **2020 (f)** | **2021 (f)** |
|---|---|---|---|
| GDP, % | 2.2 | -4.0 | 3.0 |
| CPI (Headline), % | 1.8 | 0.3 | 2.4 |
| CPI (Trimmed mean), % | 1.6 | 1.1 | 1.8 |
| Unemployment Rate, % | 5.2 | 8.3 | 7.1 |
| Wages Growth, % | 2.2 | 1.8 | 1.6 |

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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