Monday, 30 October 2023

Local Data to Firm RBA Rate Decision

This week features a spurt of local data ahead of the Reserve Bank's (RBA) Melbourne Cup Day meeting next Tuesday. The data will be important in informing the Board's final decision but will likely play second fiddle to the hot-inflation data released last week. The domestic data is also likely to be trumped by international developments, including a string of central bank policy meetings.

Domestic data flow

Retail Trade

The Australian Bureau of Statistics (ABS) kicked off a busy data week with the release of the September retail sales report this morning. Retail turnover jumped a solid 0.9% in September following a 0.3% gain in August. This was the strongest monthly increase in retail spending since January. Nominal retail spending continues to be supported by surging population growth and elevated inflation.

Retail spending rose 1.8% over the September quarter, which suggests that quarterly spending growth remained positive even after adjusting for rising prices over the period. This will be confirmed on Friday, with the release of retail trade volume data for the September quarter. A rise in real (i.e. inflation adjusted) retail spending may give the Board further confidence that the economy remains resilient, potentially negating some of the downside risks to growth which might otherwise support a rate pause.

Private sector credit

Tomorrow, private sector credit figures for September will be released. Credit growth has decelerated gradually since the second half of 2022 alongside higher interest rates. But the slowdown has been orderly and gradual; indeed, there remains a decent level of underlying credit demand. We expect credit to have expended 0.3% over September, broadly in line with the pace of recent months.

Tuesday will also feature a speech from the RBA's Assistant Governor (Financial System), Brad Jones. The address is unlikely to give much away when it comes to monetary policy, but we will be gleaning over the words of Jones' speech nonetheless, just in case of some important nuance to the RBA's messaging. Jones will appear again as part of a panel discussion on Friday.

Housing data

In recent commentary the RBA has highlighted the importance of considering the implications of rising dwelling prices for monetary policy. They have drawn two important implications. Firstly, that increasing dwelling prices could support household consumption via the 'wealth channel'. That is, higher prices may contribute to some households feeling relatively wealthier and, therefore, more likely to spend. And secondly, resilient demand for housing and relatedly housing credit, may suggest that the current level of the cash rate is not as restrictive as expected. Both would suggest higher dwelling prices support the case for a further rate hike, albeit at the margin. Rising dwelling prices alone are unlikely to provide a catalyst for further hikes.

Wednesday and Thursday will feature three important data releases updating us on the dynamics in Australia's housing market. First cab off the rank will be dwelling prices data for October, which is expected to confirm that the price upturn remains alive and well. We expect dwelling prices rose 1.0% in October, accelerating from September's 0.8% gain. Importantly, October marks the beginning of a seasonal lift in advertised supply. We will be closely monitoring whether this was realised given the current tight supply dynamic and, if so, how well demand soaked up the increase in supply.

September building approvals will also be out Wednesday. Detached house approvals appear to be establishing a gradual uptrend from a low level. Reflecting this, we expect dwelling approvals rose 5.0% in September. Australia has a critical need to expand the housing stock, however, a range of headwinds remain an obstacle including labour shortages, construction insolvencies and elevated interest rates. As these headwinds abate and we begin to see some pull-forward from government policies, we are likely to see a more meaningful resurgence in approvals. Finally, housing finance data for September is due out on Thursday. We expect new housing finance rose 4.0% in September, supported by a 4.2% in owner-occupier borrowing and a 3.5% increase for investors.

Global developments

The Fed's November policy meeting early Thursday morning (AEDT) is likely to dominate market moves this week. However, the release of the US Treasury's quarterly refunding statement just hours earlier could have just as significant an impact on bond markets.

The Fed is largely expected to stand pat on rate increases but will continue to underscore that further tightening may be necessary to ensure rates are sufficiently restrictive to tame inflation. The incoming data will again be hailed as the north star. To date, the data has largely suggested that the Fed remains on track to achieve its soft-landing objective. Inflation is continuing to moderate, while growth has proven resilient. However, there remains important risks which could derail this goldilocks scenario and the Fed is prudently remaining vigilant rather than declaring victory too early.

Treasury markets have been volatile over recent months, reflecting evolving interest rate expectations and supply and demand dynamics within the market. This has led treasury yields to increase materially across the curve, especially at the longer-end of the yield curve. Last week, the US 10-year treasury yield hit a high of 5.02% - its highest level since the GFC. While traders will be hanging off Jermone Powell's every word, the Federal Treasury's quarterly refunding statement could prove the dominant market mover. The refunding statement updates the market on the Treasury's issuance plans, including the schedule of new bond auctions and the profile of this issuance across different bond tenors. This will provide an important update on the supply of treasuries to the market, which could prompt some outsized moves if any announcements come as a surprise.

The Bank of England (BoE) and the Bank of Japan (BoJ) also have policy meetings this week. The BoJ on Tuesday is unlikely to make any changes to its policy settings, though there is some growing speculation that there could be a tweak to the Bank's yield curve control (YCC) parameters.

Currently, the BoJ is allowing the 10-year bond yield to fluctuate within 100 basis points of its 0.0% yield target. The 10-year yield has been drifting towards the top of this range over recent months and reached as high as 0.89% so far in today's trade. Markets will also be attentive to any changes to the BoJ's inflation and growth forecasts, which may precede any policy tweak.

The BoE meet on Thursday night and are widely expected to leave policy settings unchanged for a second consecutive meeting. Despite recent progress, inflation remains elevated in the UK, but the BoE is growing more attentive to downside risks to growth as the UK economy stagnates. This is likely to see the BoE remain on hold and allow time for the lagged impacts of monetary policy to take full effect. In a similar vein to the Fed, the BoE will likely continue to underscore its readiness to respond further should progress on inflation fall short of expectations.

If all evolves broadly as expected, the RBA could find itself in an unfamiliar position come next week. Other major central banks are expected to have left policy settings on hold in November, while the RBA will almost certainly be discussing a further increase in the cash rate.

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Group Forecasts

		2023	2024				2025
End Period:	**Close (27 Oct)**	**Q4 (f)**	**Q1 (f)**	**Q2 (f)**	**Q3 (f)**	**Q4 (f)**	**Q1 (f)**
Aust. Interest Rates:							
RBA Cash Rate, %	4.10	4.35	4.35	4.35	4.10	3.85	3.60
90 Day BBSW, %	4.31	4.55	4.55	4.47	4.22	3.97	3.72
3 Year Swap, %	4.54	4.40	4.30	4.20	4.10	4.00	3.80
10 Year Bond, %	4.81	4.70	4.60	4.50	4.40	4.30	4.15
US Interest Rates:							
Fed Funds Rate, %	5.375	5.375	5.125	4.875	4.625	4.375	4.125
US 10 Year Bond, %	4.83	4.80	4.70	4.60	4.50	4.40	4.20
USD Exchange Rates:							
AUD-USD	0.6335	0.66	0.67	0.68	0.69	0.70	0.71
USD-JPY	149.66	147	145	143	141	138	135
EUR-USD	1.0565	1.08	1.09	1.11	1.13	1.14	1.15
GBP-USD	1.2122	1.23	1.24	1.25	1.26	1.27	1.28
NZD-USD	0.5811	0.61	0.61	0.62	0.62	0.62	0.63
AUD Exchange Rates:							
AUD-USD	0.6335	0.66	0.67	0.68	0.69	0.70	0.71
AUD-EUR	0.5996	0.61	0.61	0.61	0.61	0.61	0.62
AUD-JPY	94.80	97.0	97.2	97.2	97.3	96.6	95.9
AUD-GBP	0.5225	0.54	0.54	0.54	0.55	0.55	0.55
AUD-NZD	1.0901	1.08	1.09	1.10	1.11	1.12	1.13

	2021	**2022**	**2023 (f)**	**2024 (f)**
GDP, %	4.6	2.7	1.2	1.6
CPI (Headline), %	3.5	7.8	4.6	3.4
CPI (Trimmed mean), %	2.6	6.8	4.4	3.3
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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