

UK & EUROPEAN ECONOMIC UPDATE

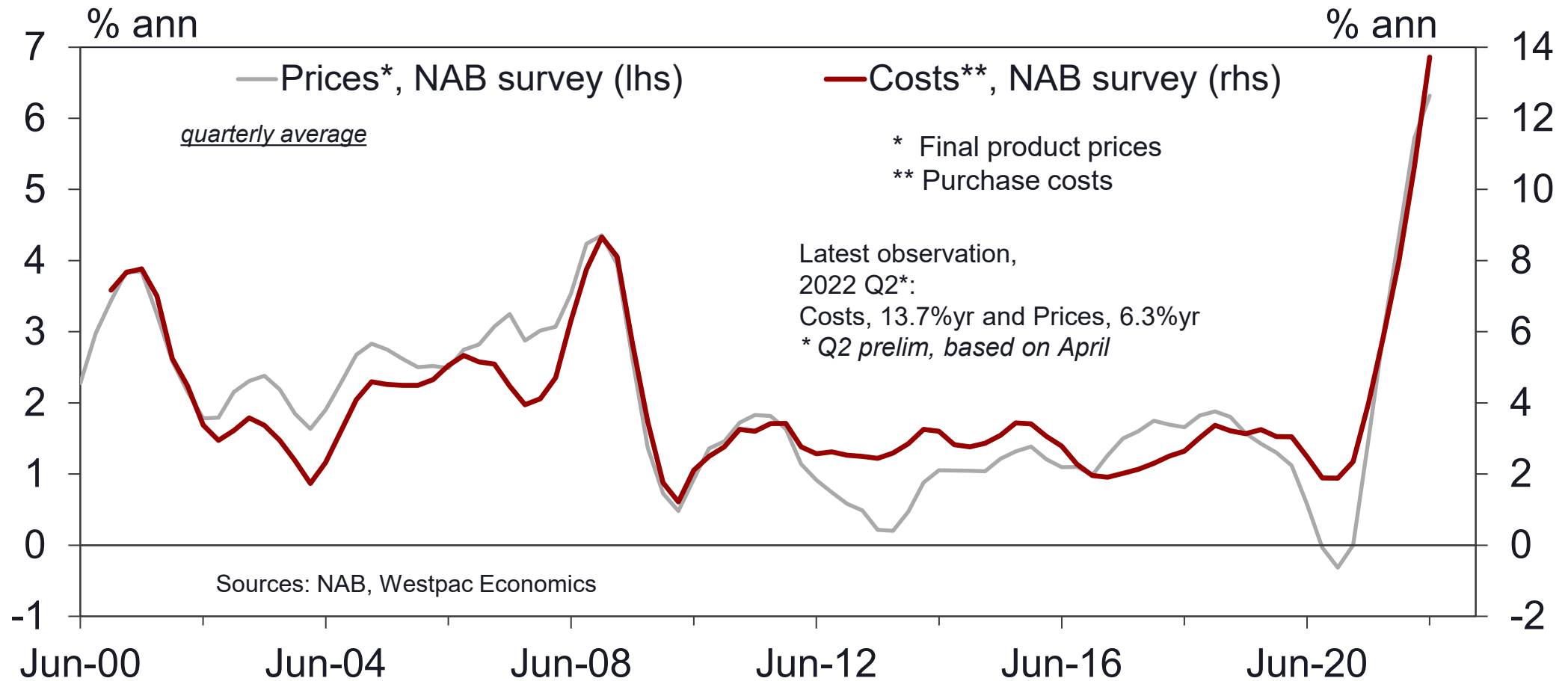
Presented by Westpac Chief Economist, Bill Evans

Westpac Institutional Bank

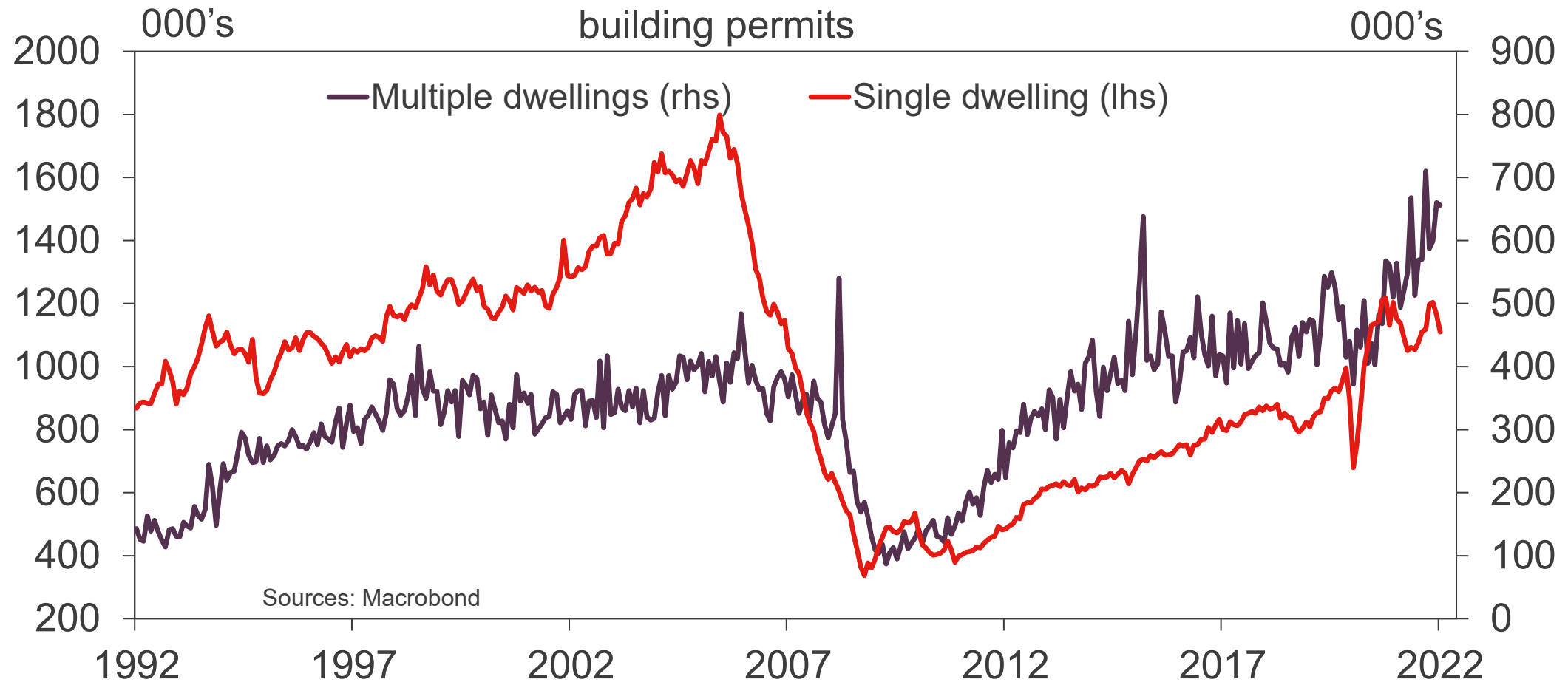
June 2022



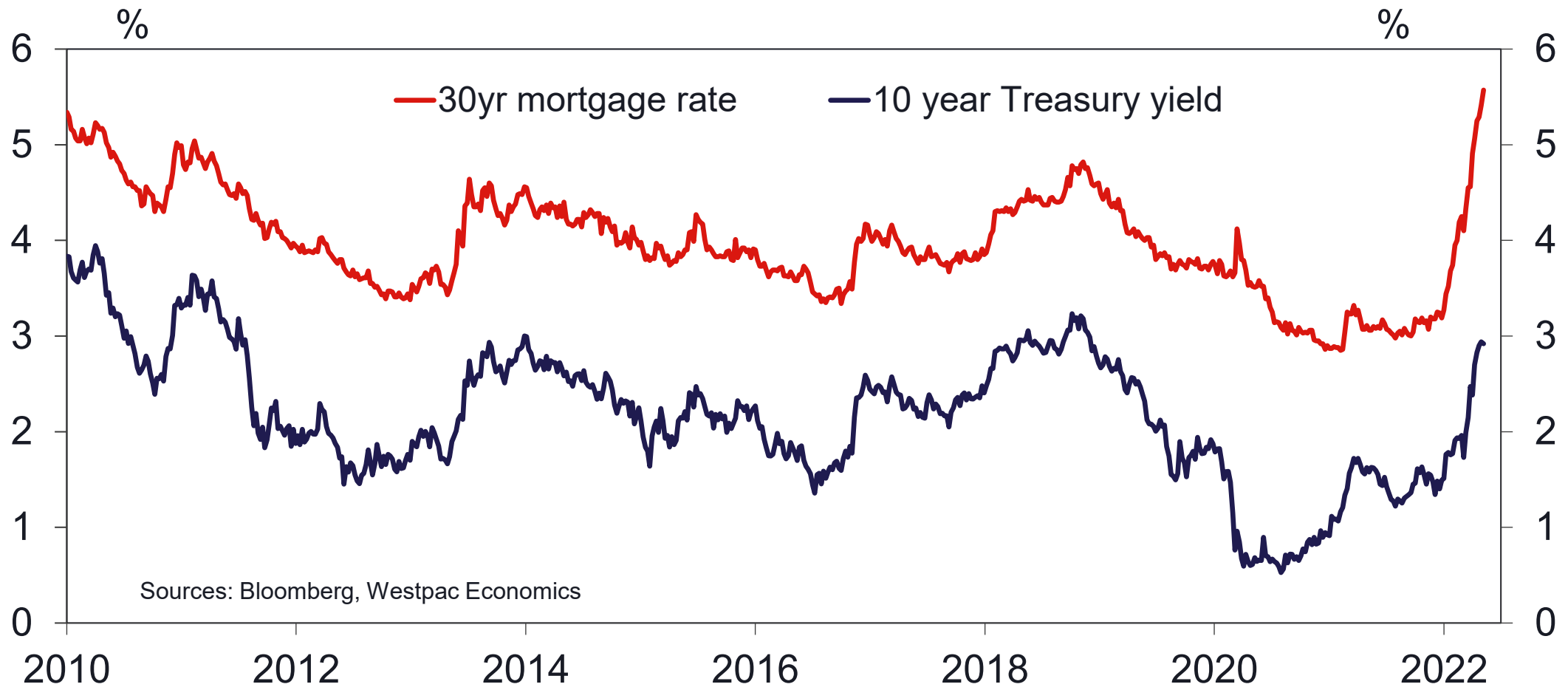
Surging costs leading to price pressures



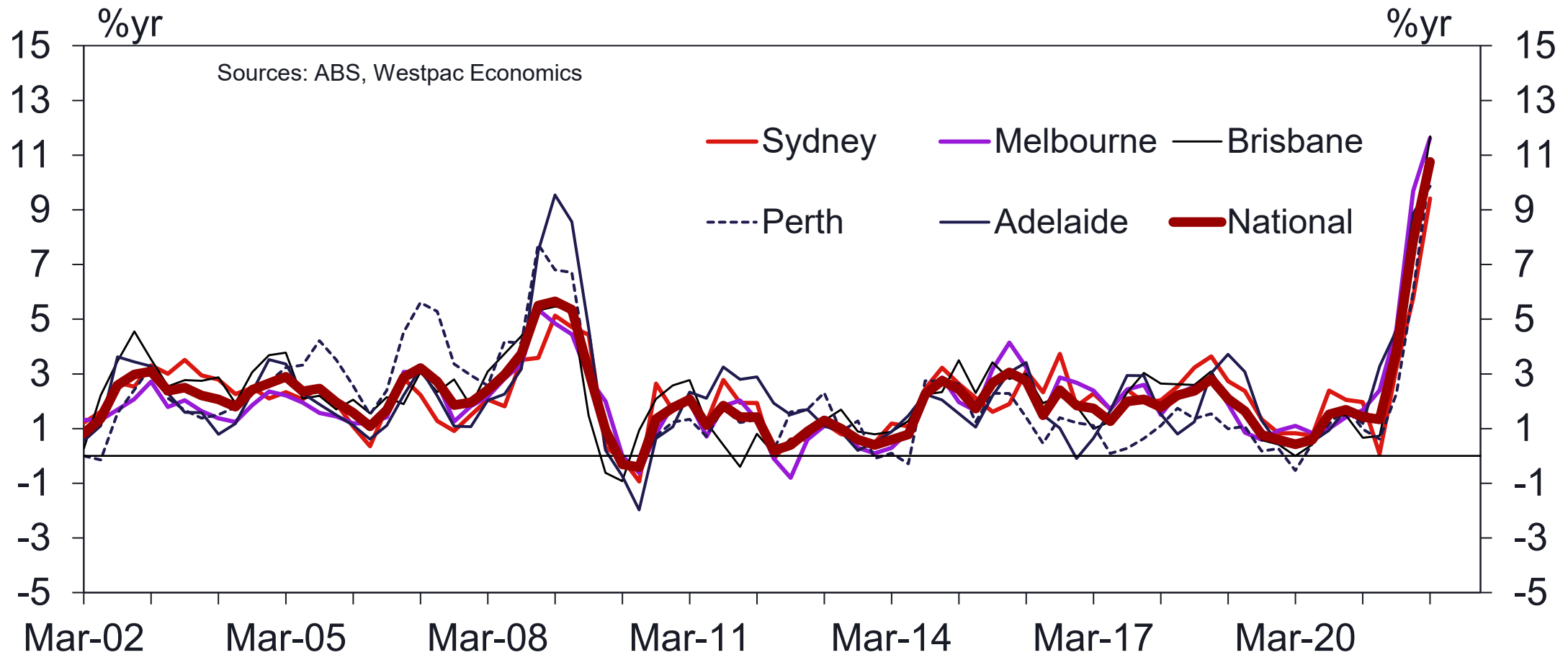
US Housing construction outlook pressuring Australian supplies



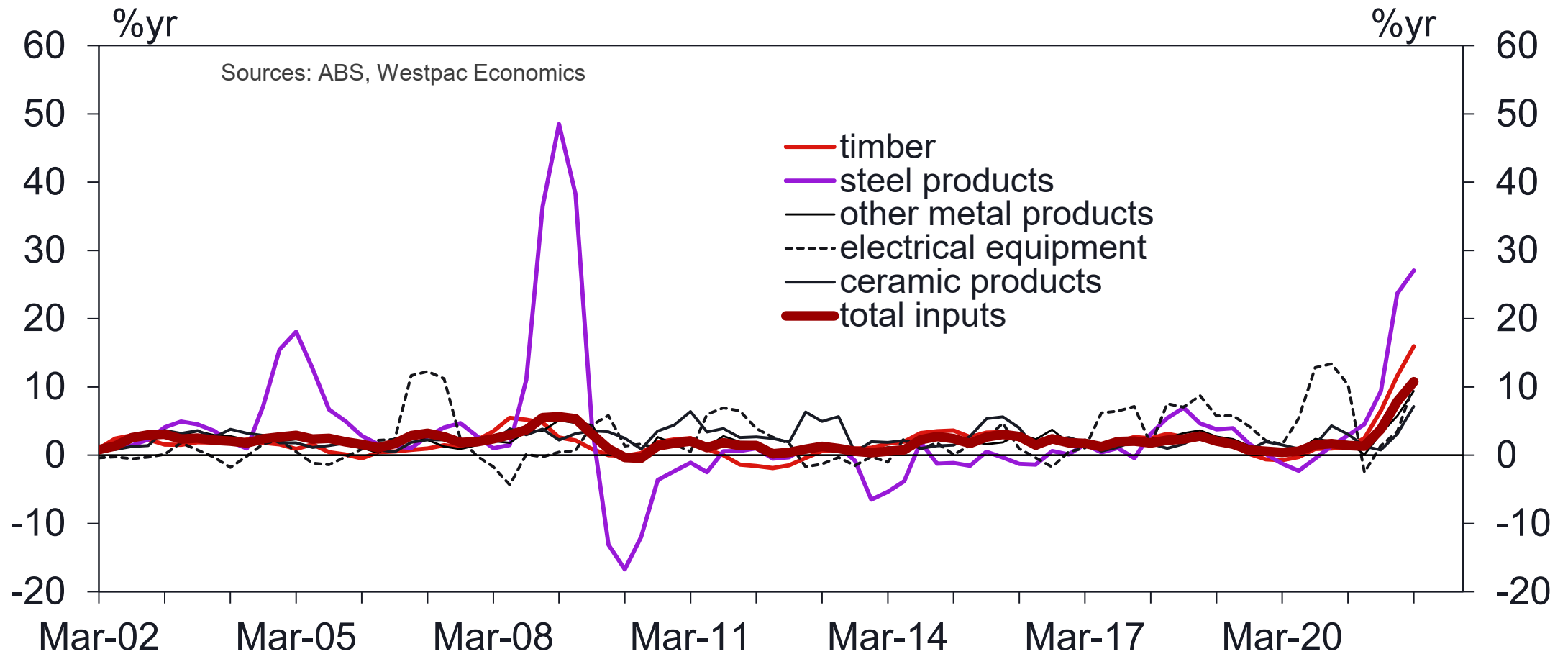
US :Mortgage rates hit recent highs ; weigh on housing



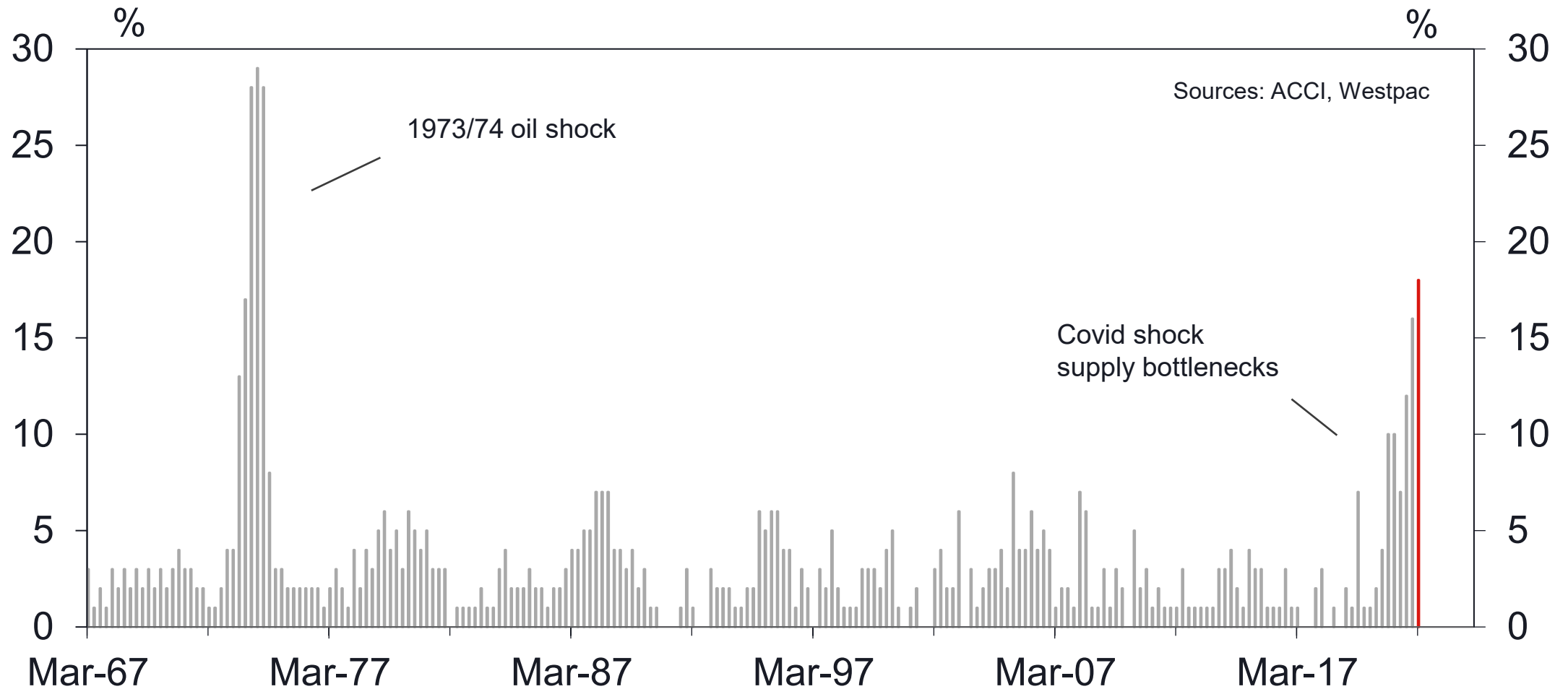
Housing construction input price inflation – without recent precedent



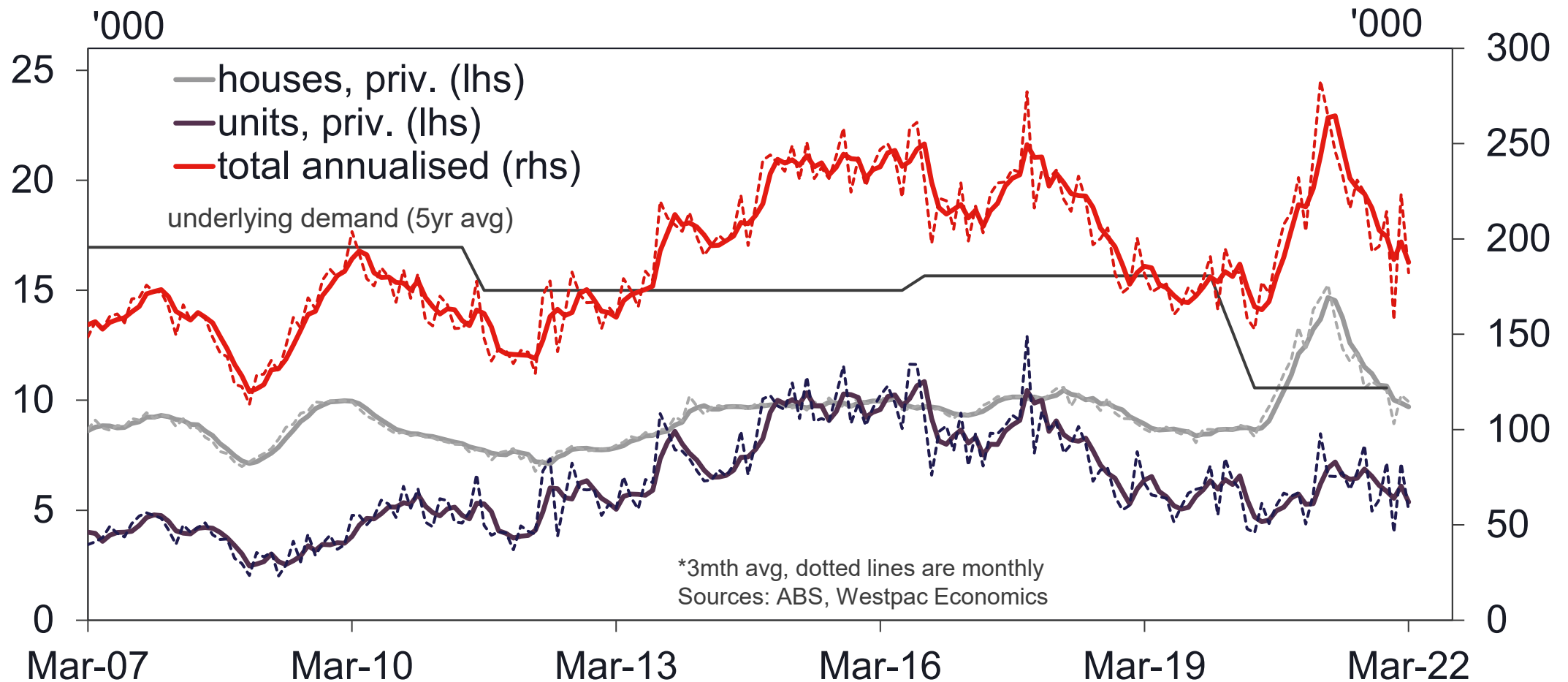
Housing construction inflation- steel and timber pressures



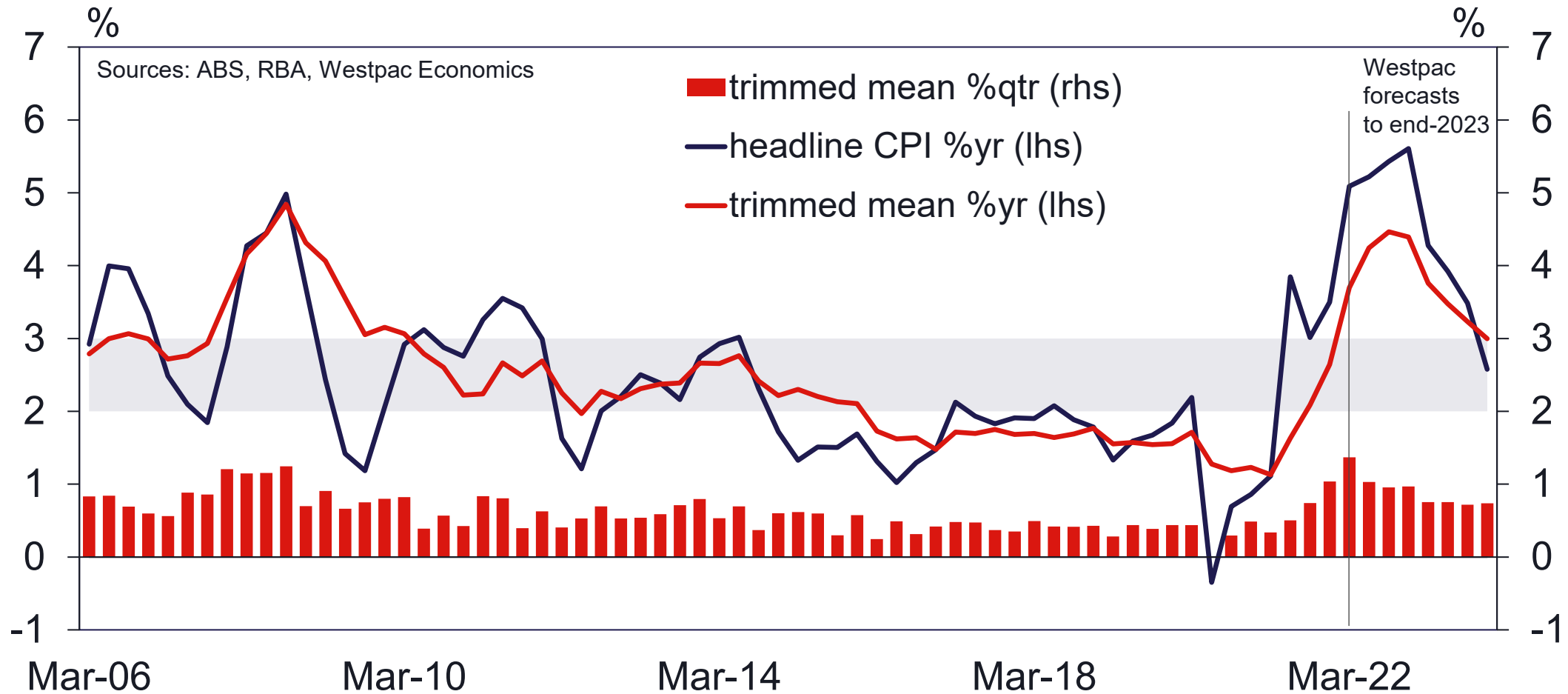
Biggest “materials” constraint since 1974 oil shock



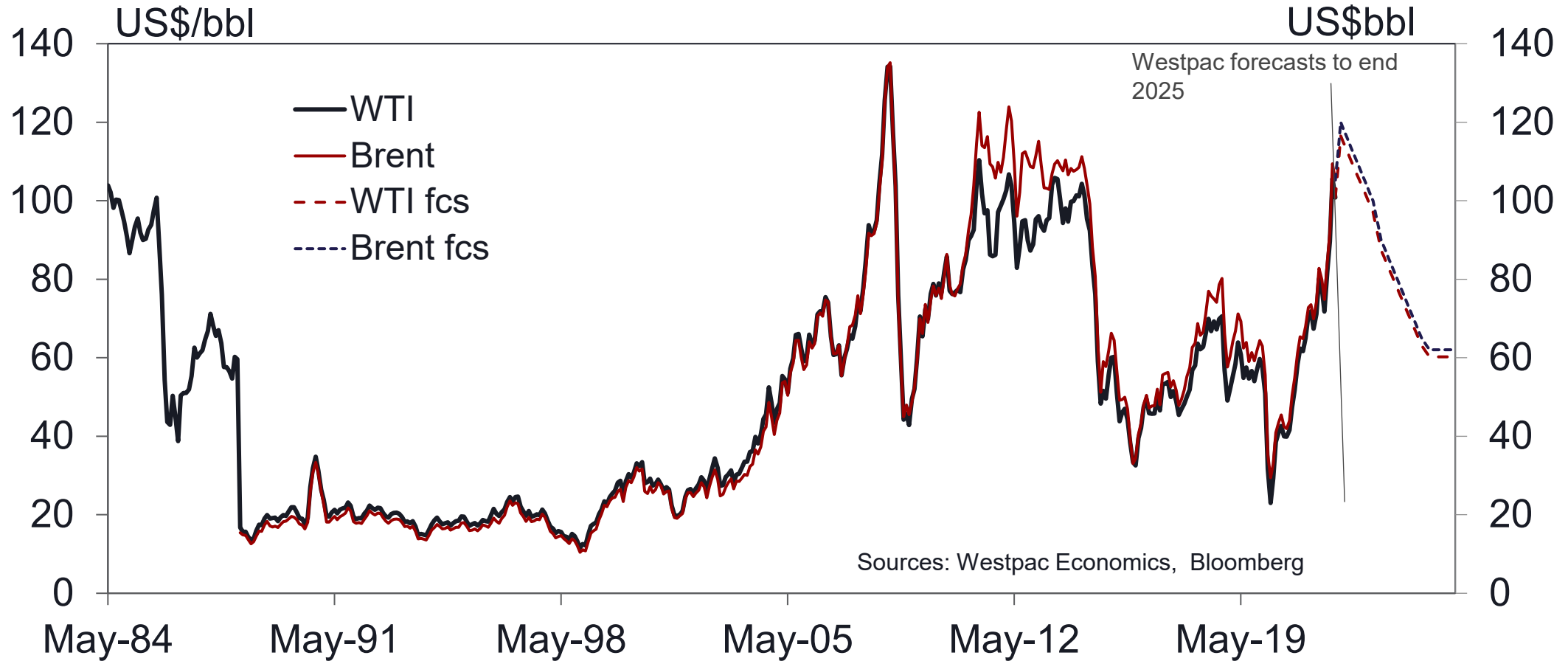
Home Builder pressures capacity at the wrong time



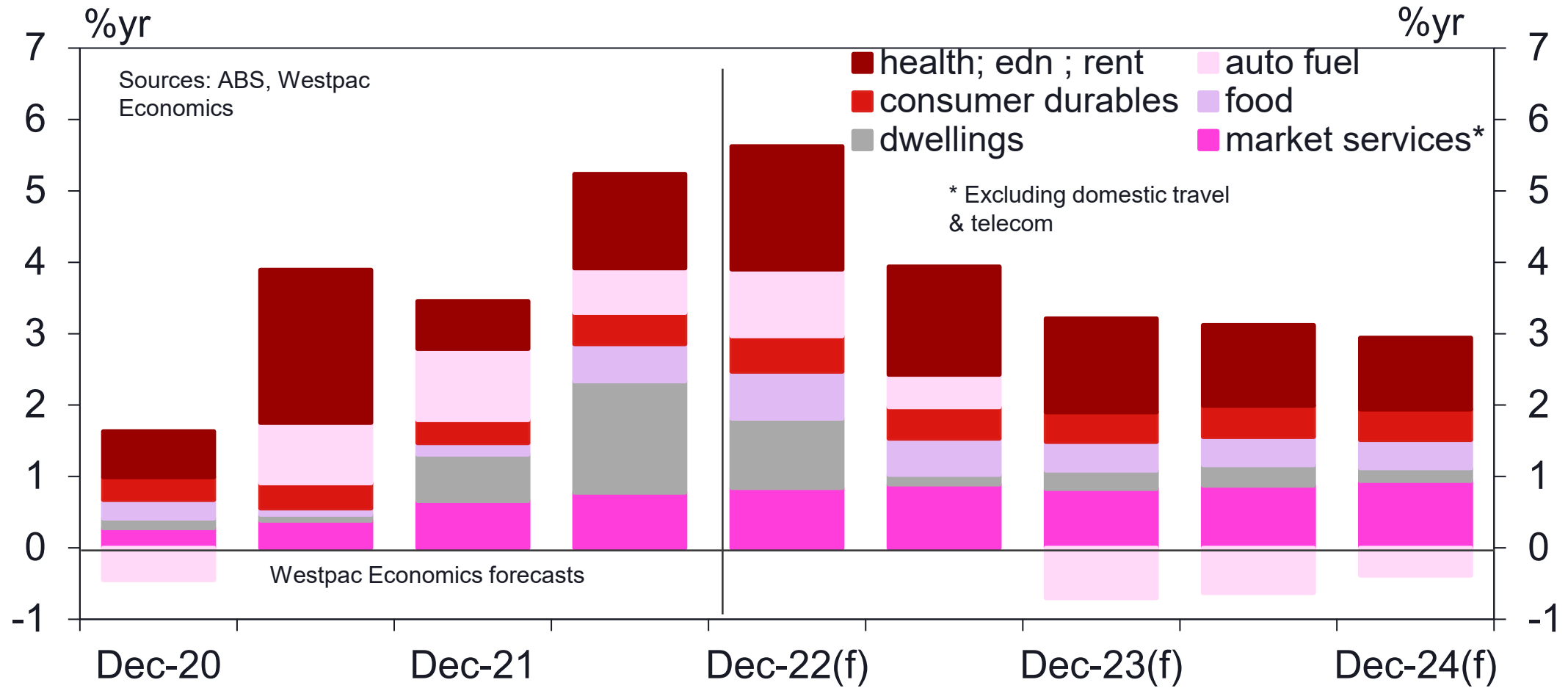
Aust CPI inflation – peaking in 2022



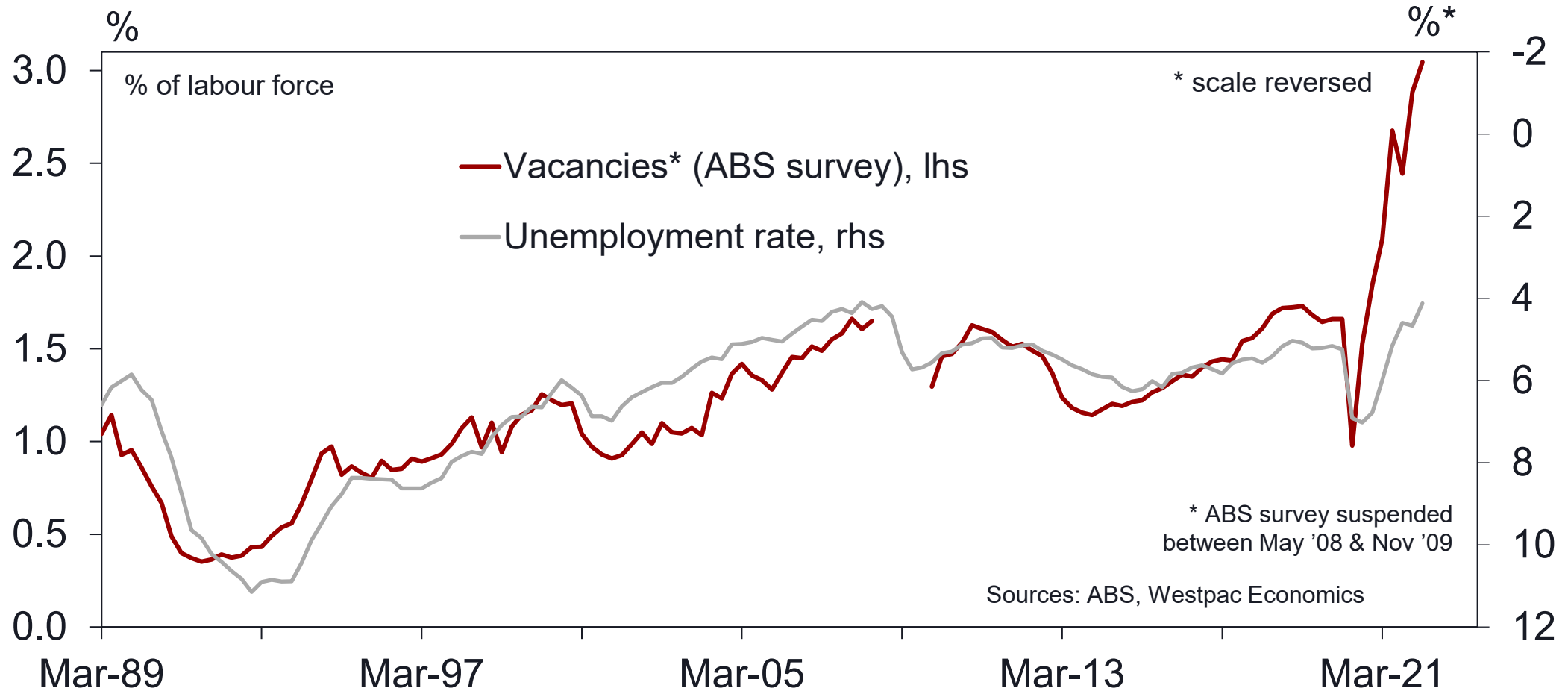
Oil prices likely to be moderating in 2023 and beyond



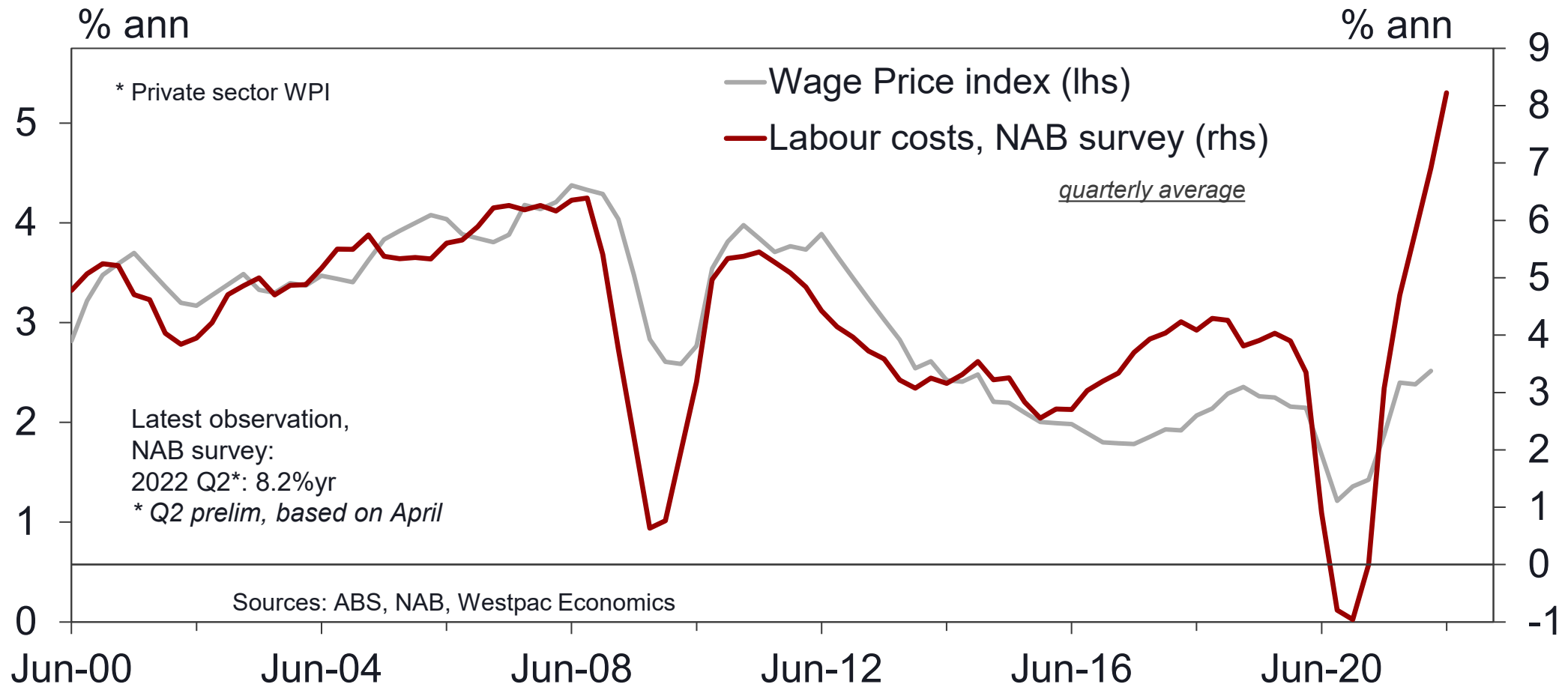
Contributions to annual inflation- slowdown in fuel; housing costs



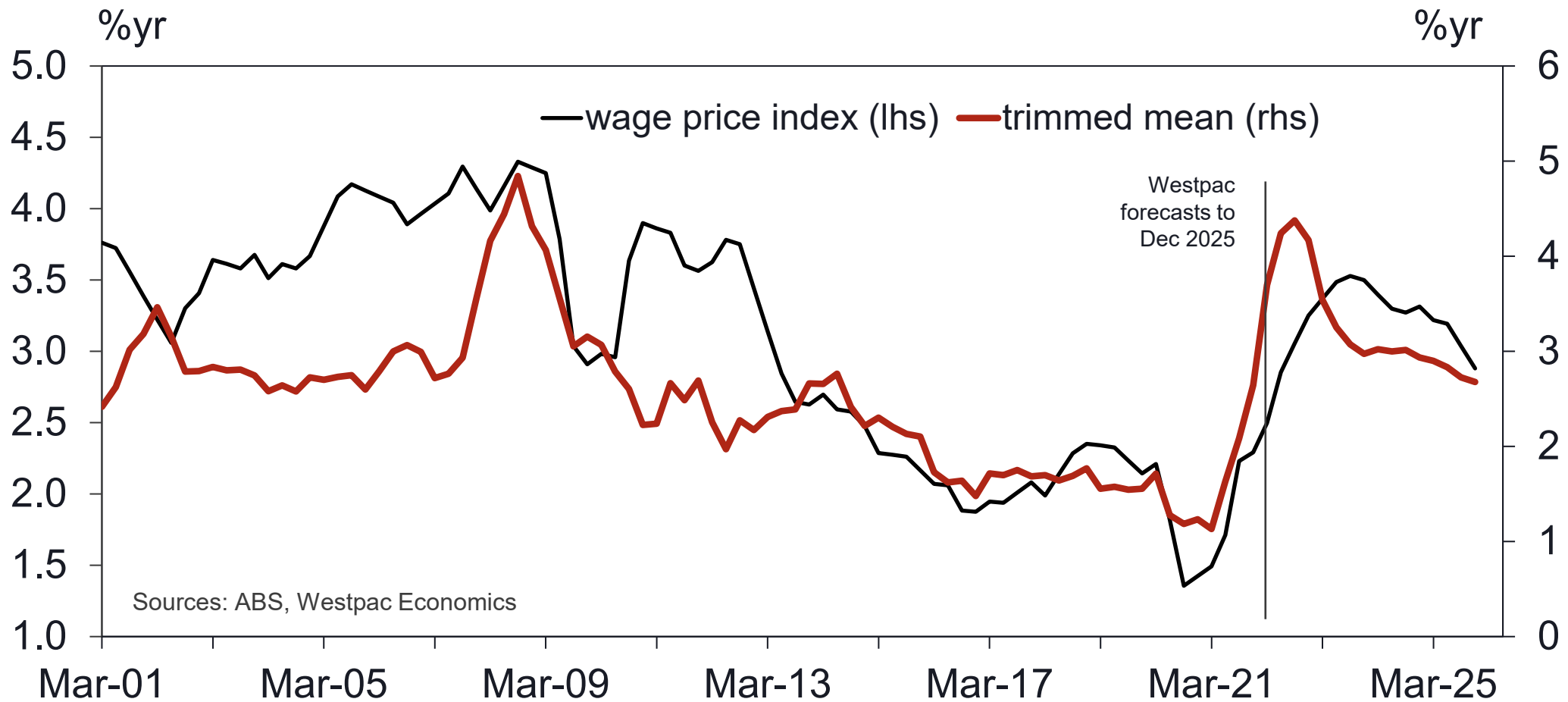
Job vacancies pointing to explosive market



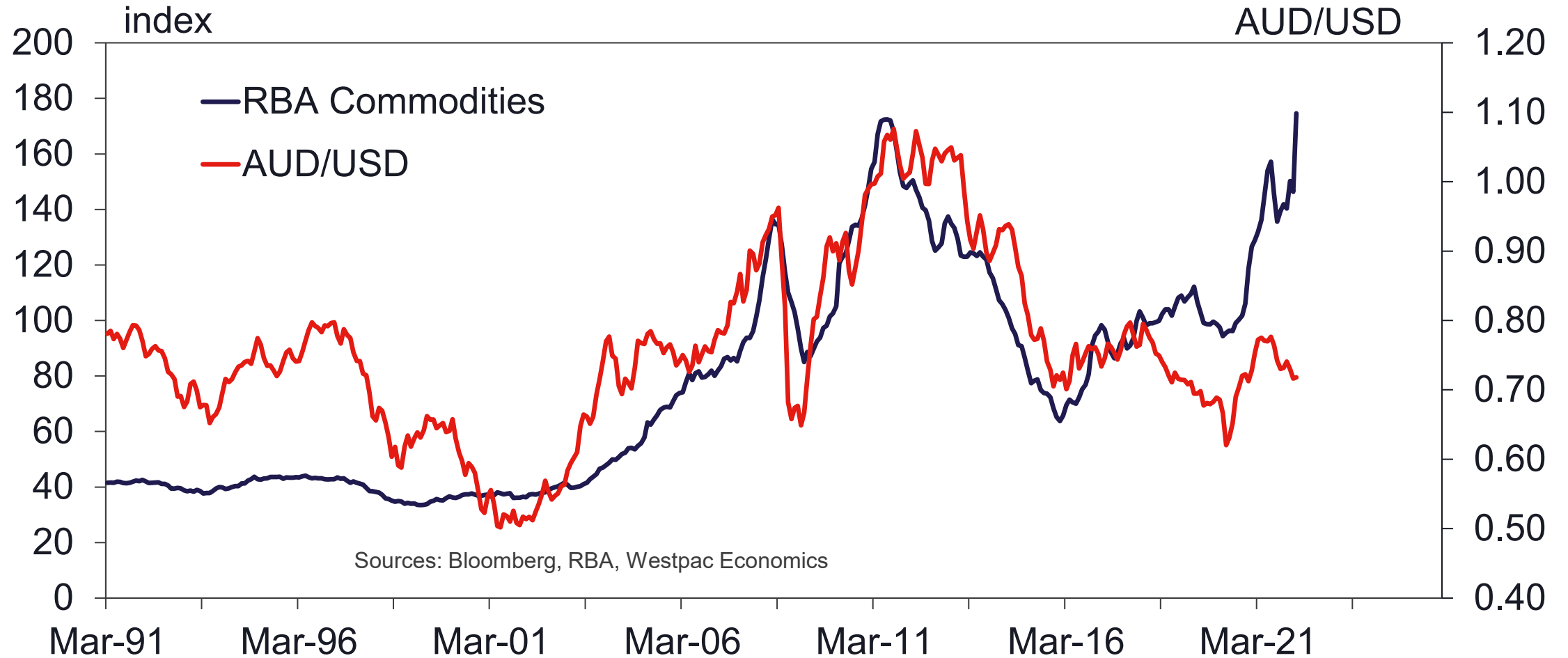
Labour costs (& wages): significant pressures



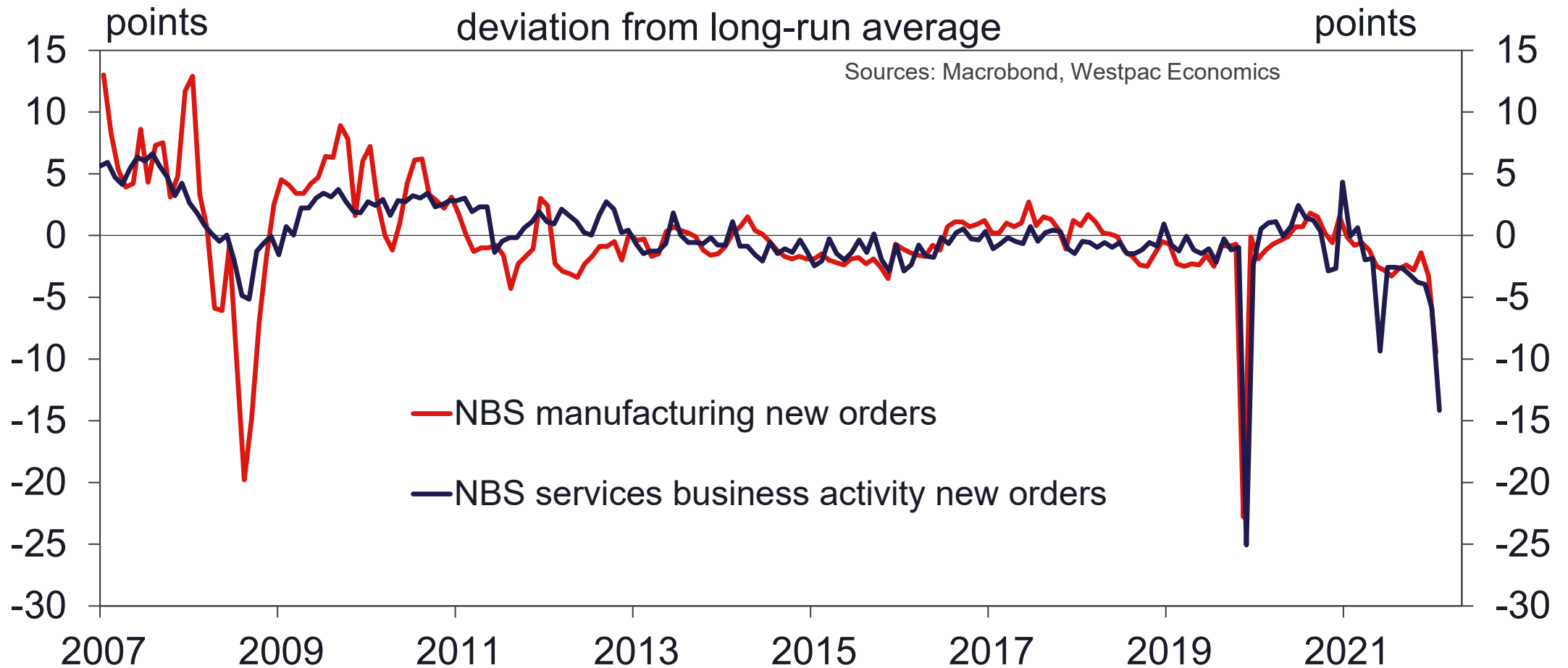
Core inflation pointing to wages catch up



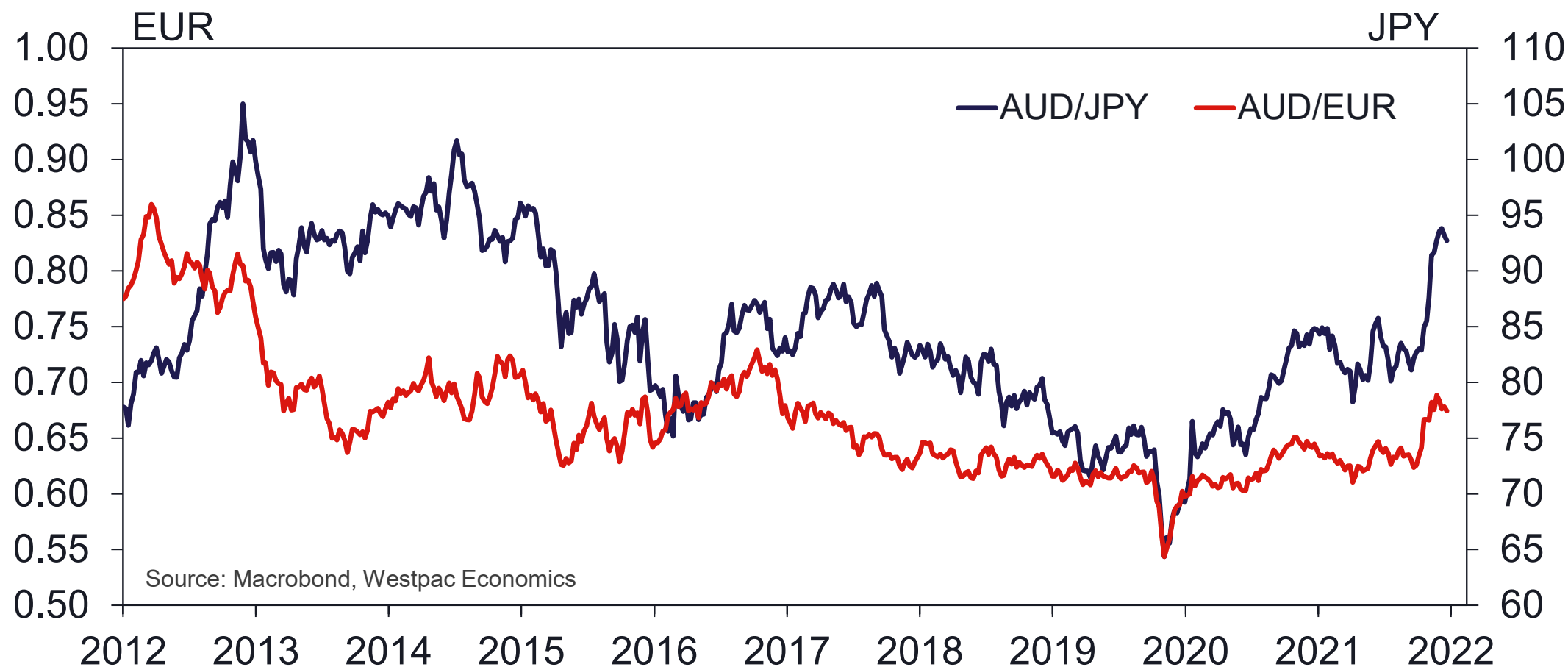
Commodities back to when AUD was above parity



China : Services tanking ; need for new stimulus; ease lockdowns



AUD strong against EURO and YEN

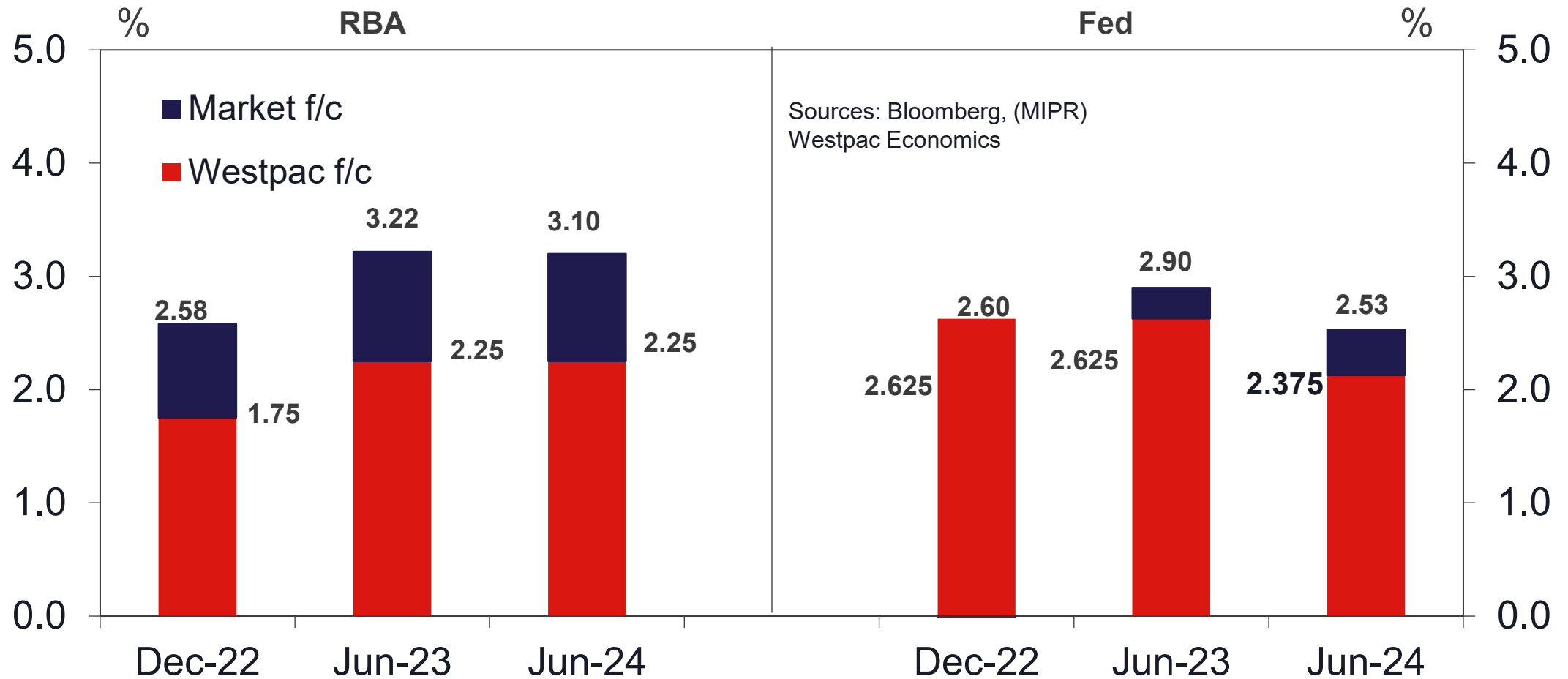


Detailed Forecasts out to end 2024 – June

	Latest	Sep-22	Dec-22	Dec-23	Dec-24
RBA Cash	0.35	1.25	1.75	2.25	2.25
3yr swap rate	3.14	3.15	3.10	2.75	2.75
AU10yr bond	3.32	3.15	2.80	2.30	2.05
Fed Funds	0.875	2.125	2.625	2.625	2.125
US 10yr bond	2.80	2.80	2.60	2.10	2.00
AUD/USD	0.72	0.74	0.76	0.80	0.80

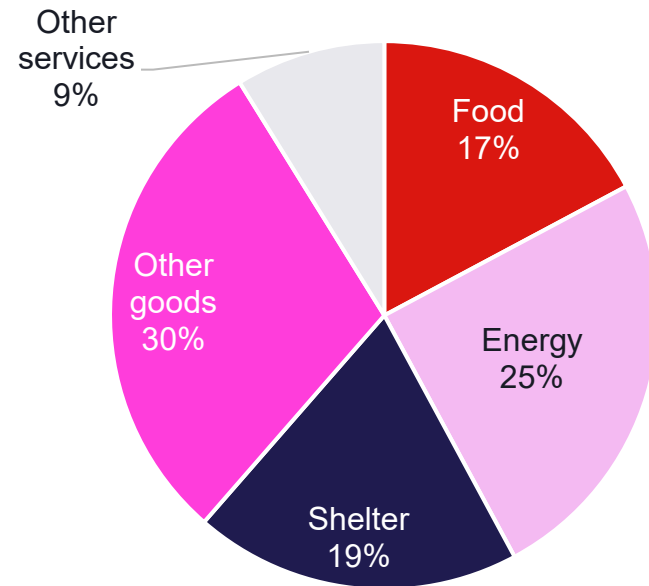
Sources: Bloomberg, Westpac Economics

Market Expectations for RBA & US Fed

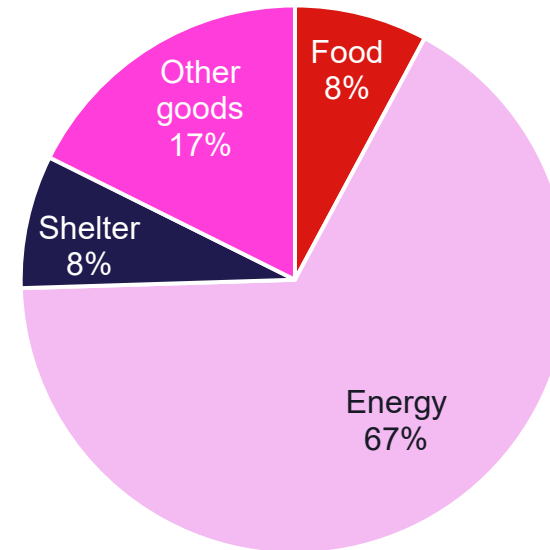


Acceleration and deceleration in US CPI 2021–2023

2021-22 CPI acceleration to
10.1% ann'd March '22

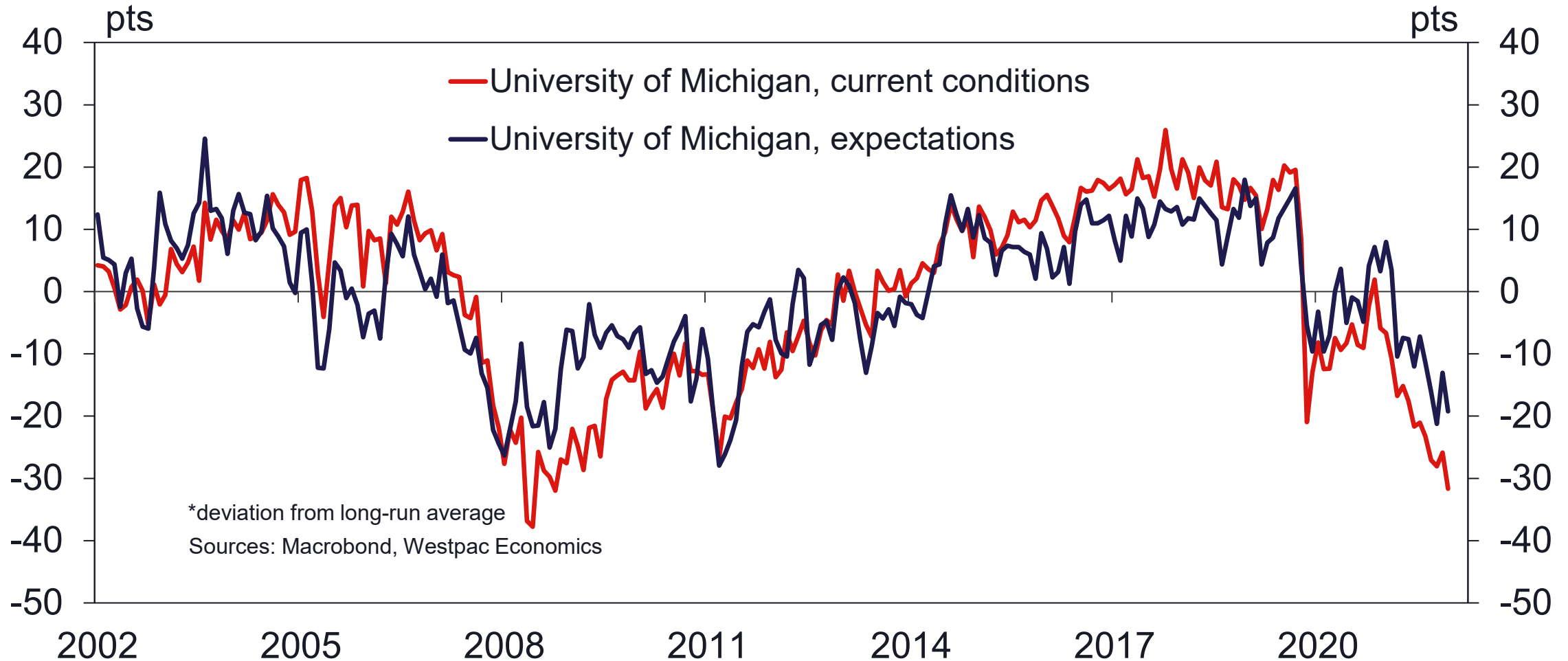


2022-23 CPI deceleration to
2.5% ann'd March '23

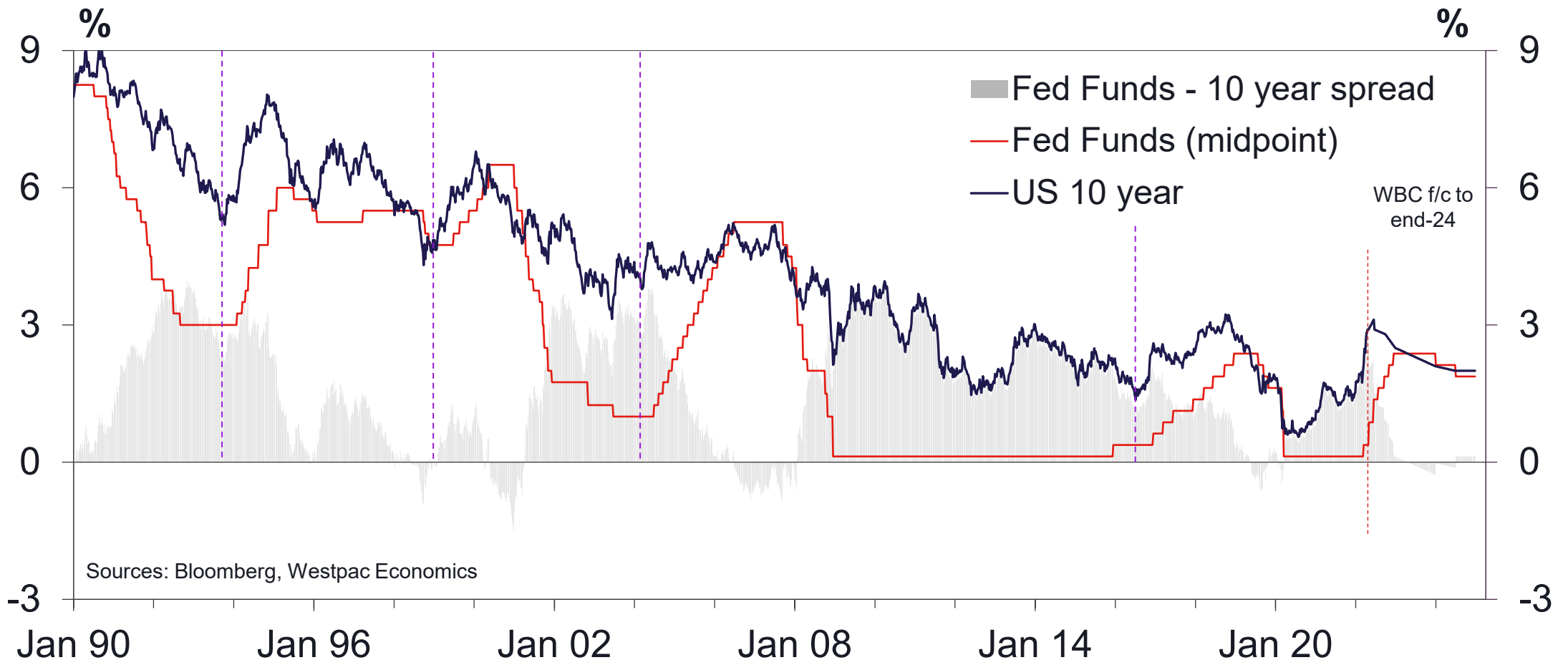


Sources: US BLS, Westpac Economics
Percentage change in 6-month contribution to headline CPI from March
one year to the next by key contributing sectors. 2022–23 is a forecast.

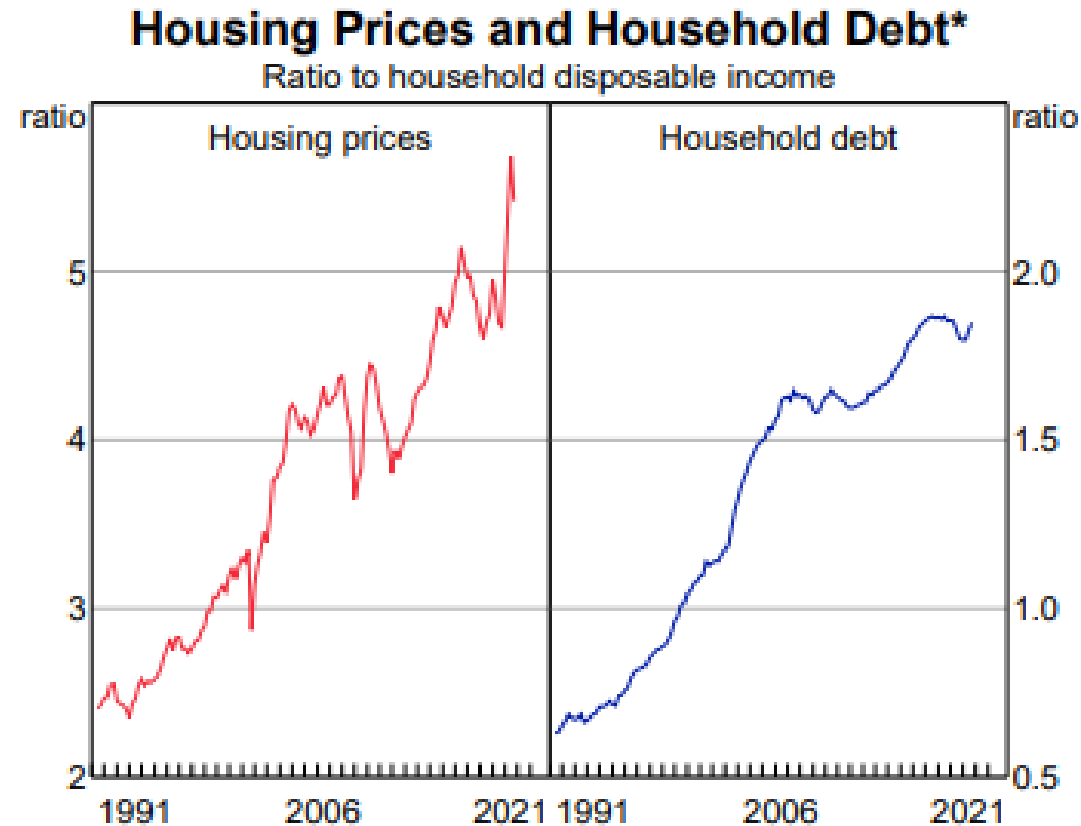
US :Concentration of inflation in essentials hitting sentiment



US 10 year rates are near peak– fed funds to peak 6 months later



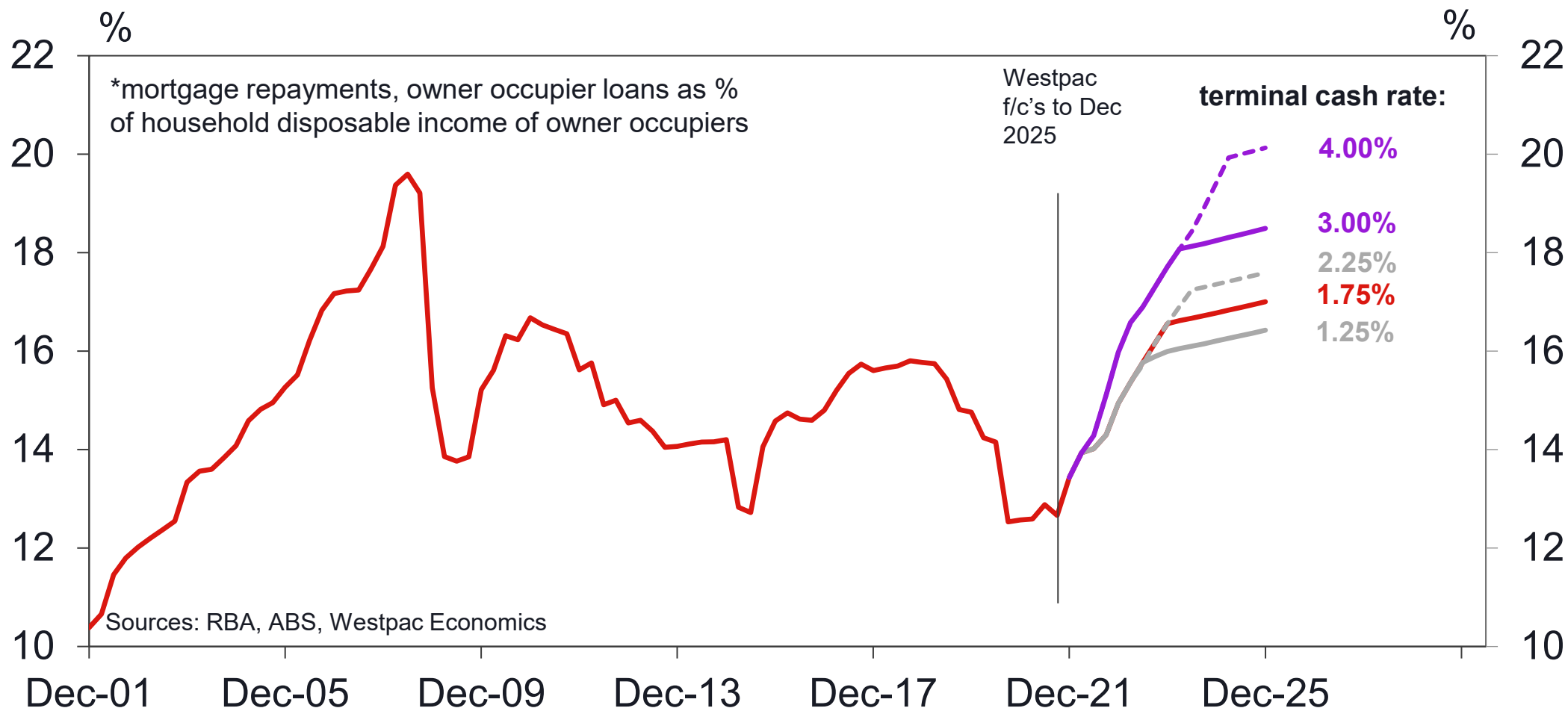
Housing prices and household debt* – really stretched



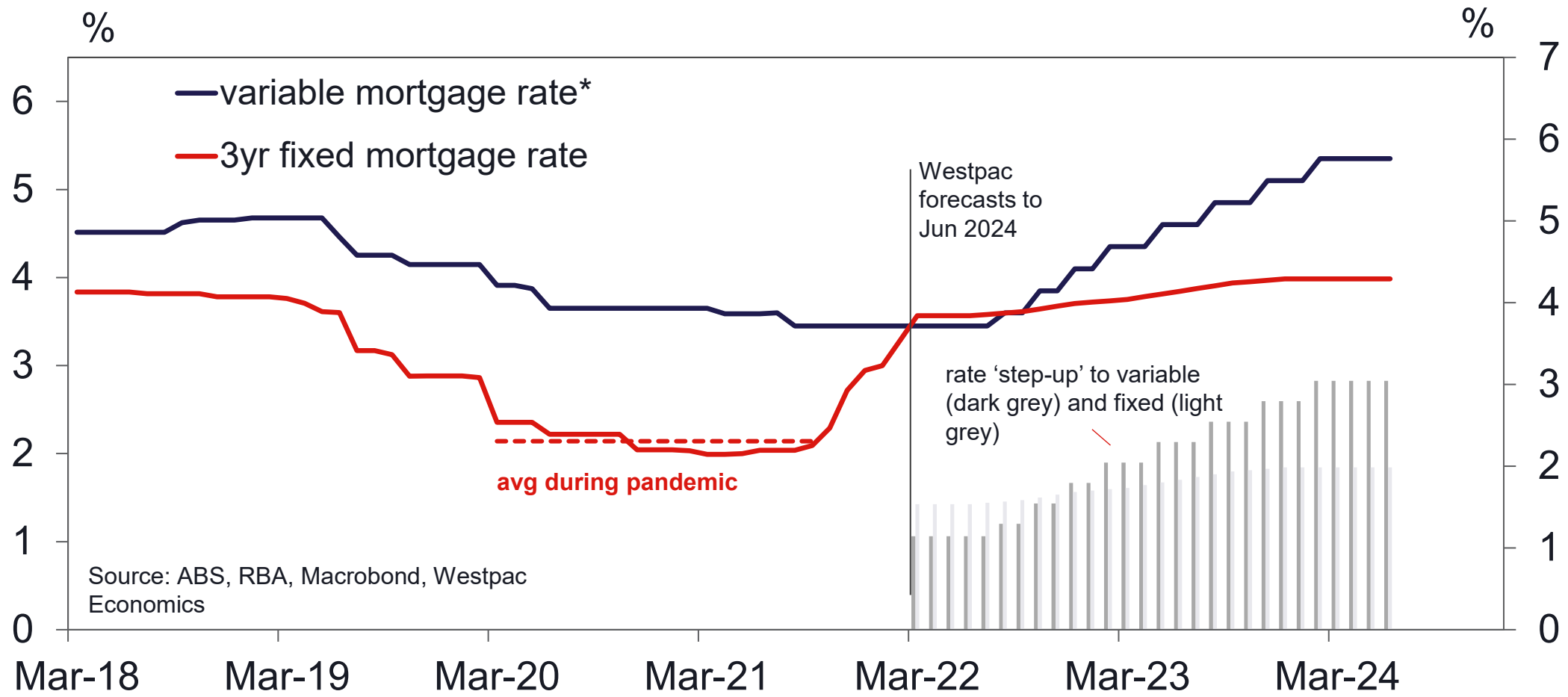
* Household disposable income is after tax, before the deduction of interest payments, and includes income of unincorporated enterprises.

Sources: ABS; CoreLogic; RBA

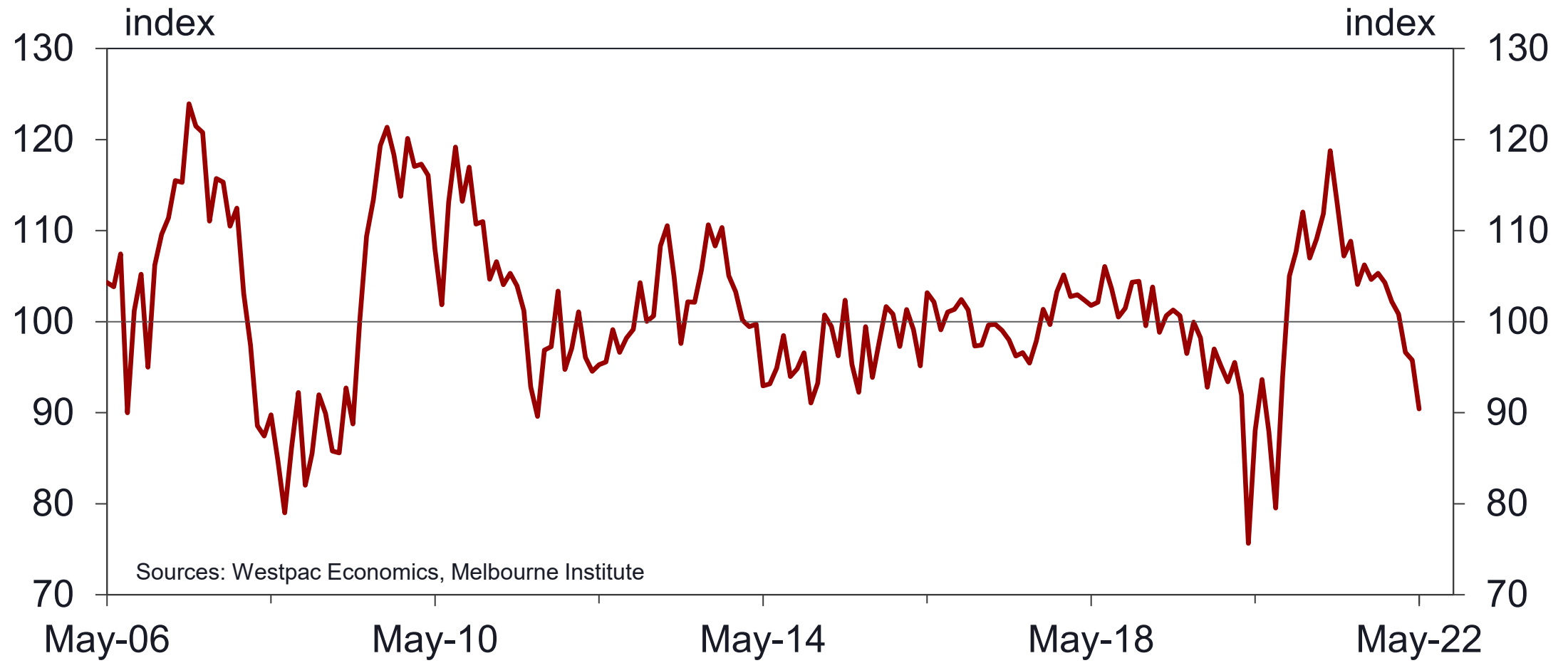
Australia's Debt servicing ratio to limit RBA cycle



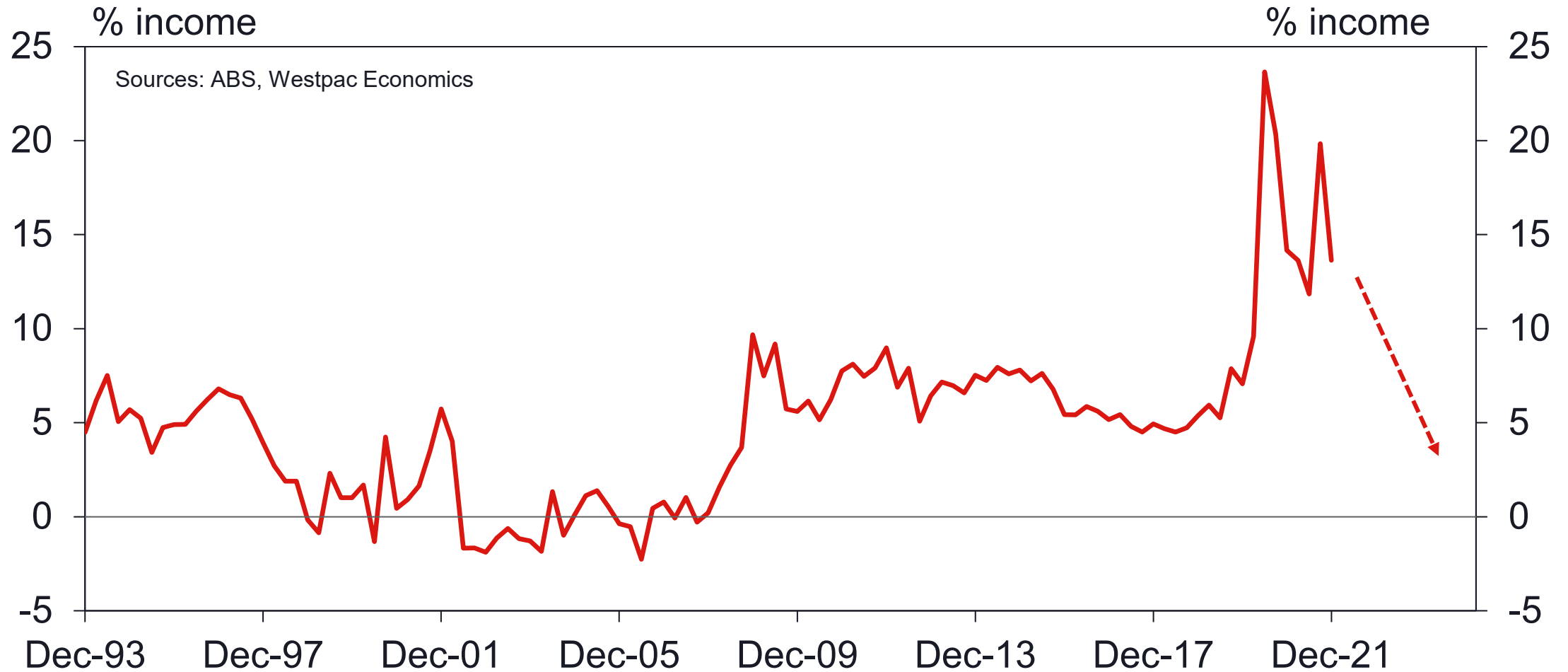
Mortgage: fixed rate 'reset': (\$0.63tr of \$2.1tr by end 2023)



Consumer Sentiment : AUST : -5.6% to 90.8 (rates; inflation)



Savings – \$250b in excess savings; \$25b if rate falls to 6%

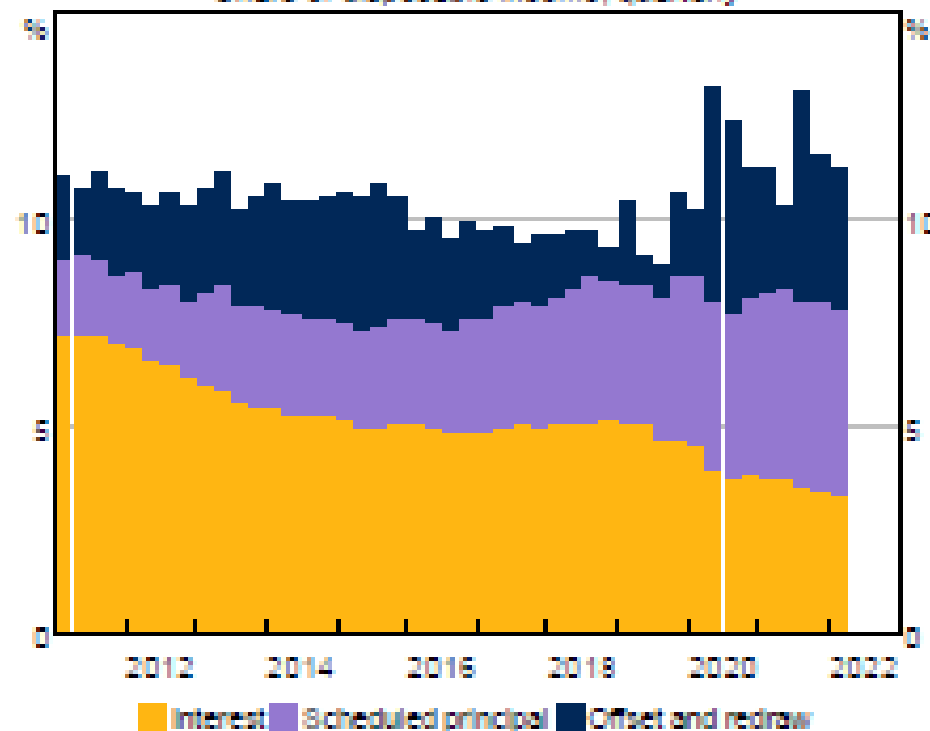


Flows into Housing Load and Offset Accounts*

Graph 3.23

Flows into Housing Loan and Offset Accounts*

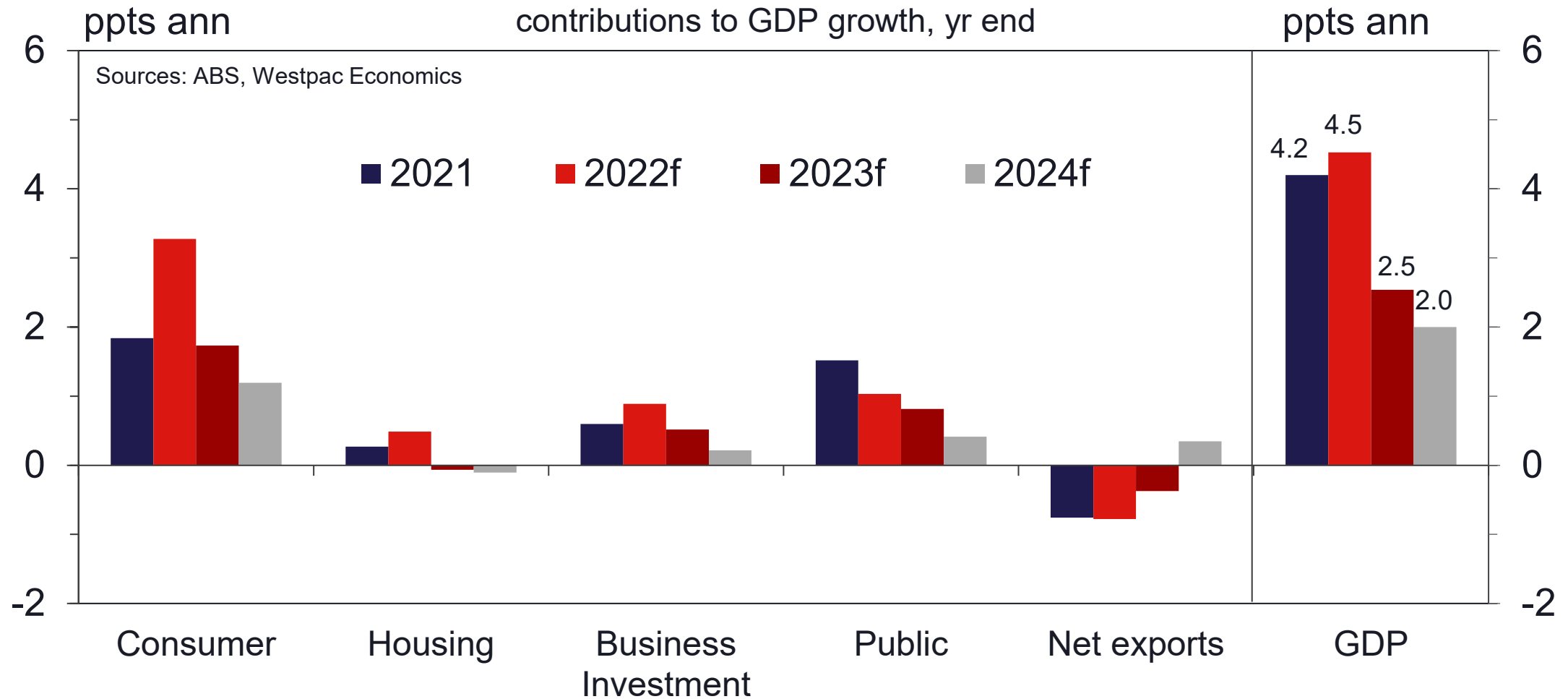
Share of disposable income; quarterly



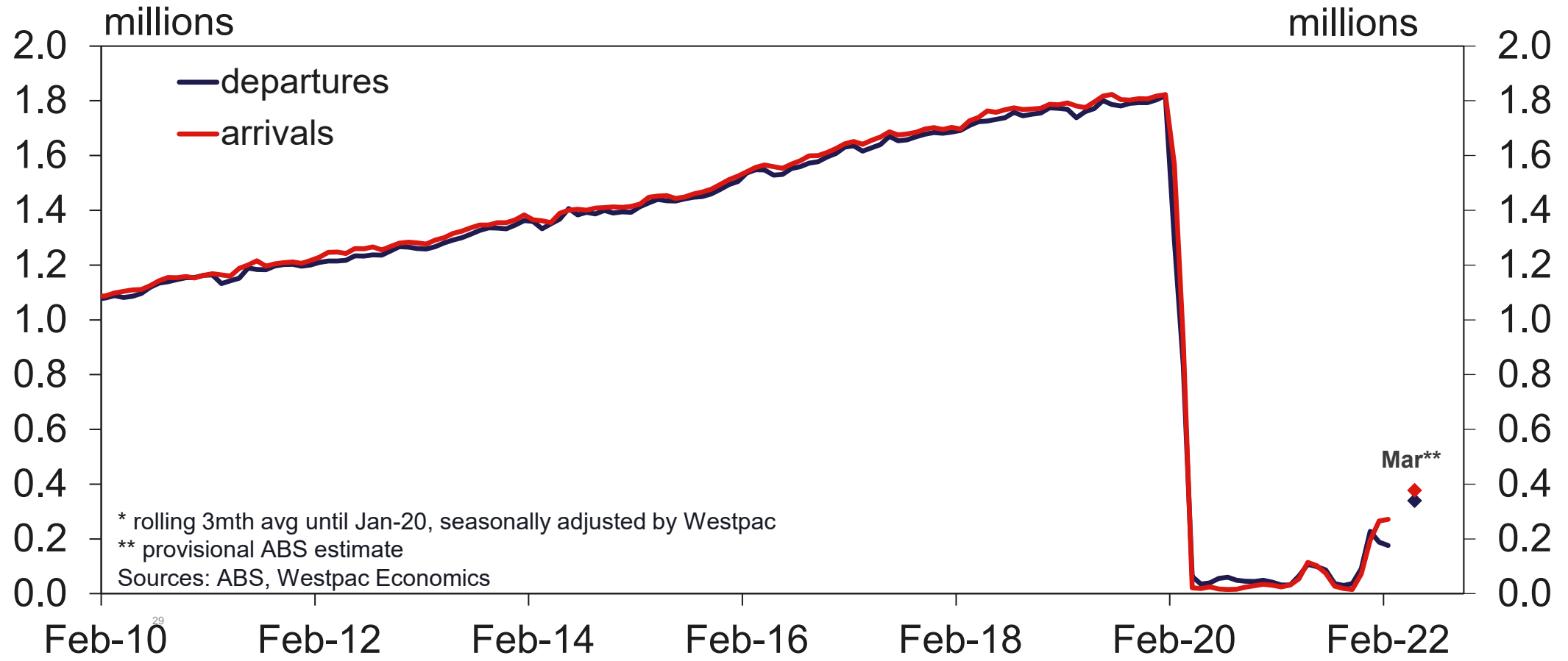
* Seasonally adjusted and break-adjusted.

Sources: ABS, APRA, RBA

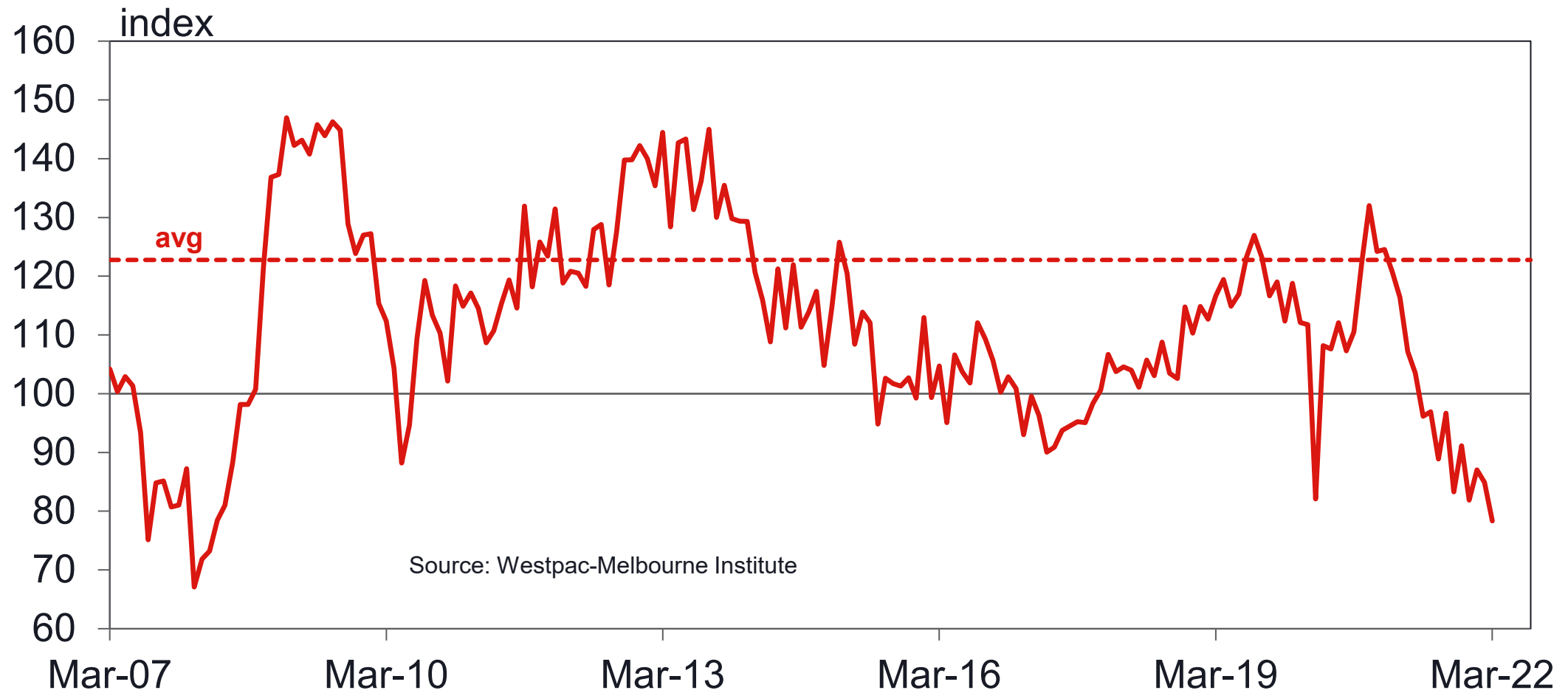
Australia: the growth mix- big slowdown in 2023 and 2024



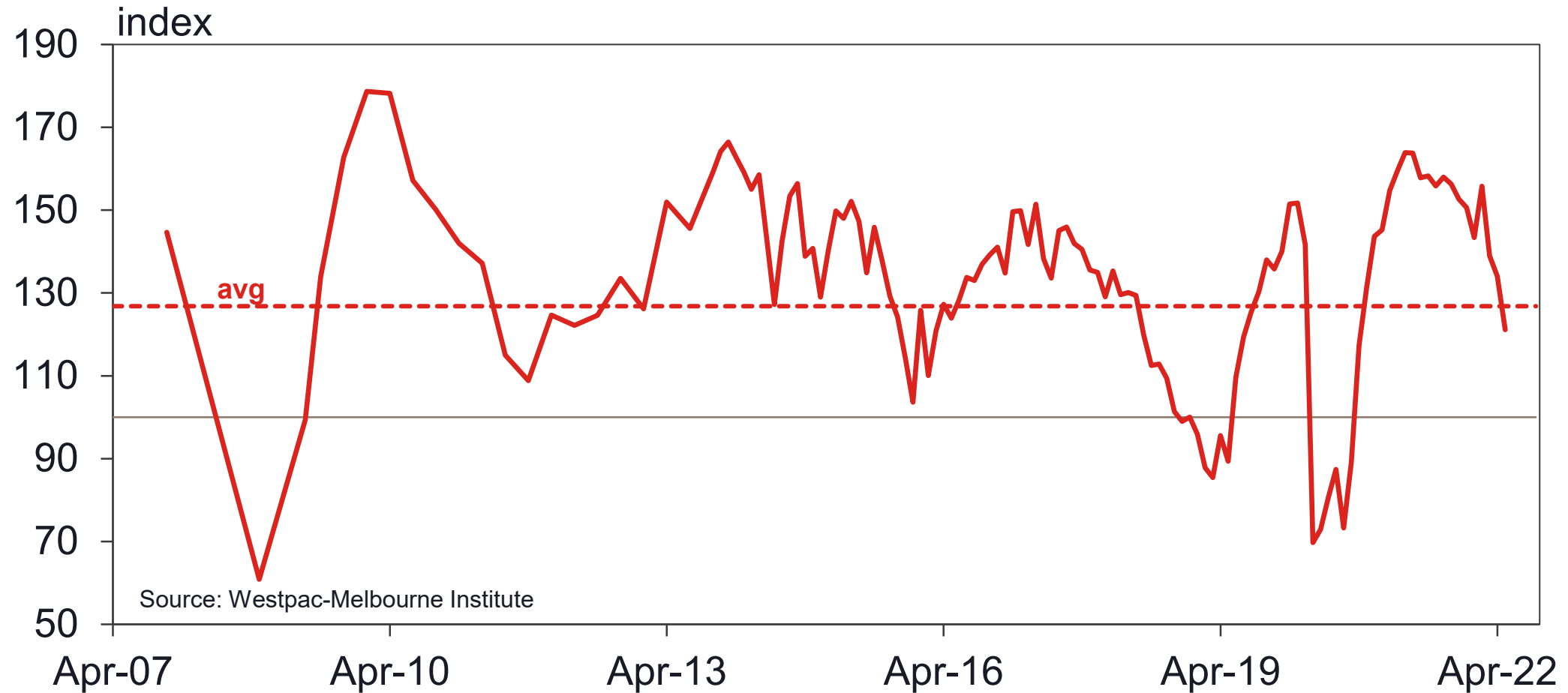
Total overseas arrivals and departures



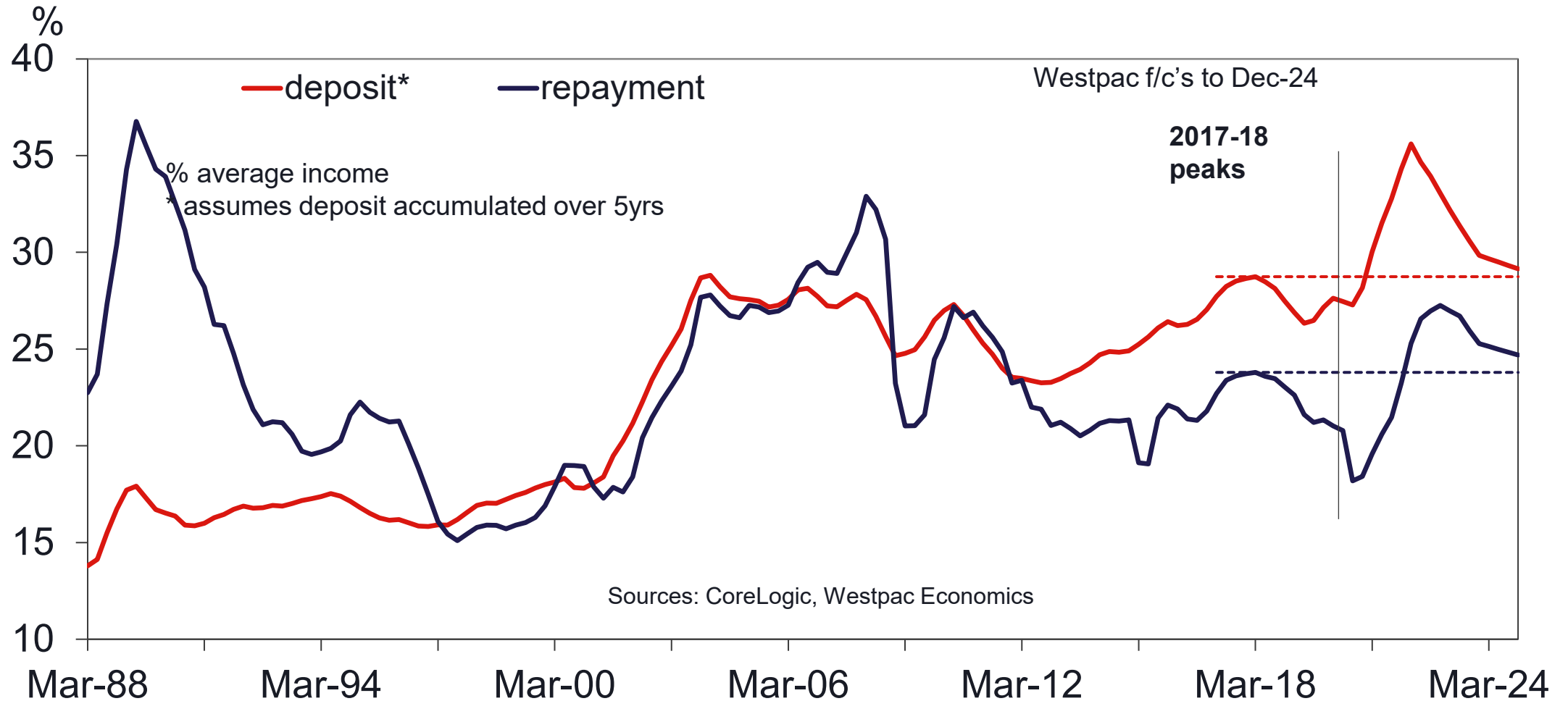
'Time to buy a dwelling' – off 40% (national)



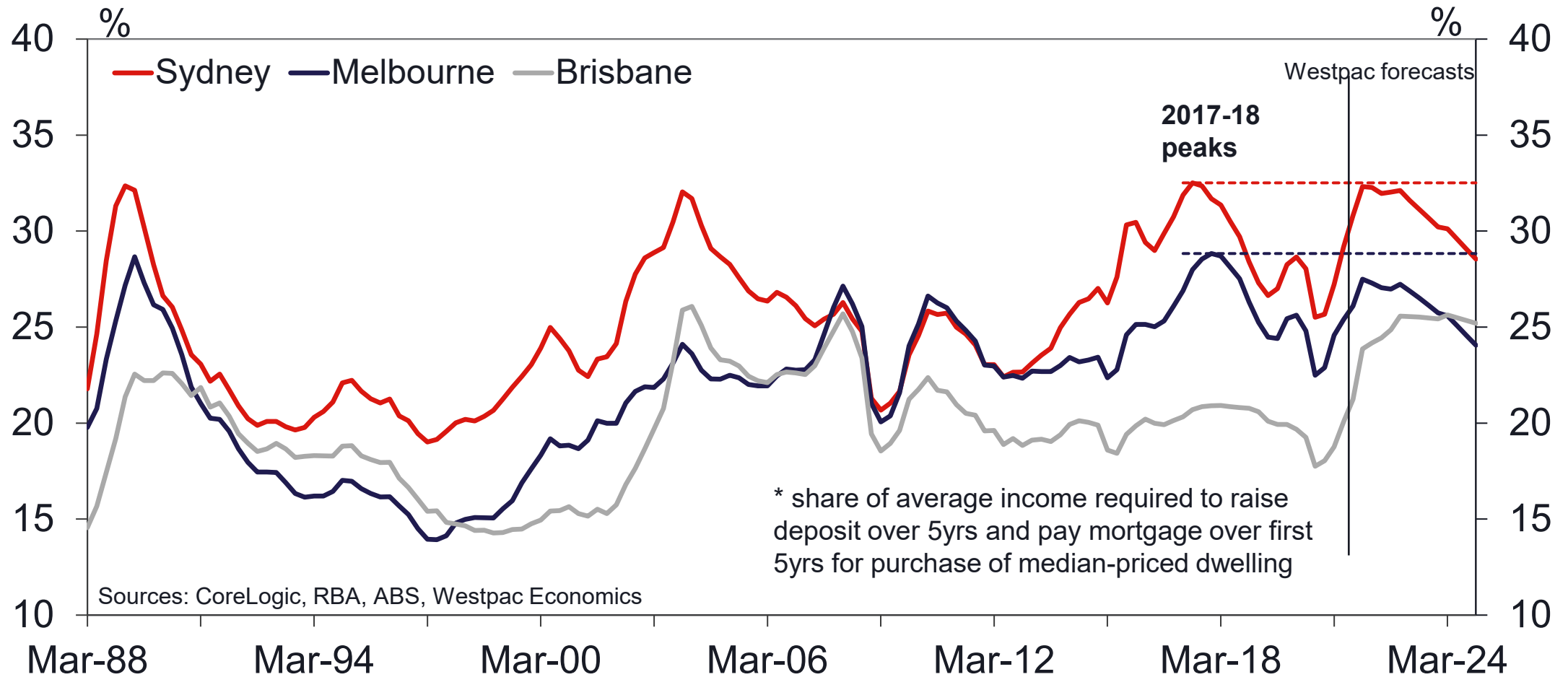
House Price Expectations (121 ; - 9.4% – Aust; 125 ; - 17% – Tas)



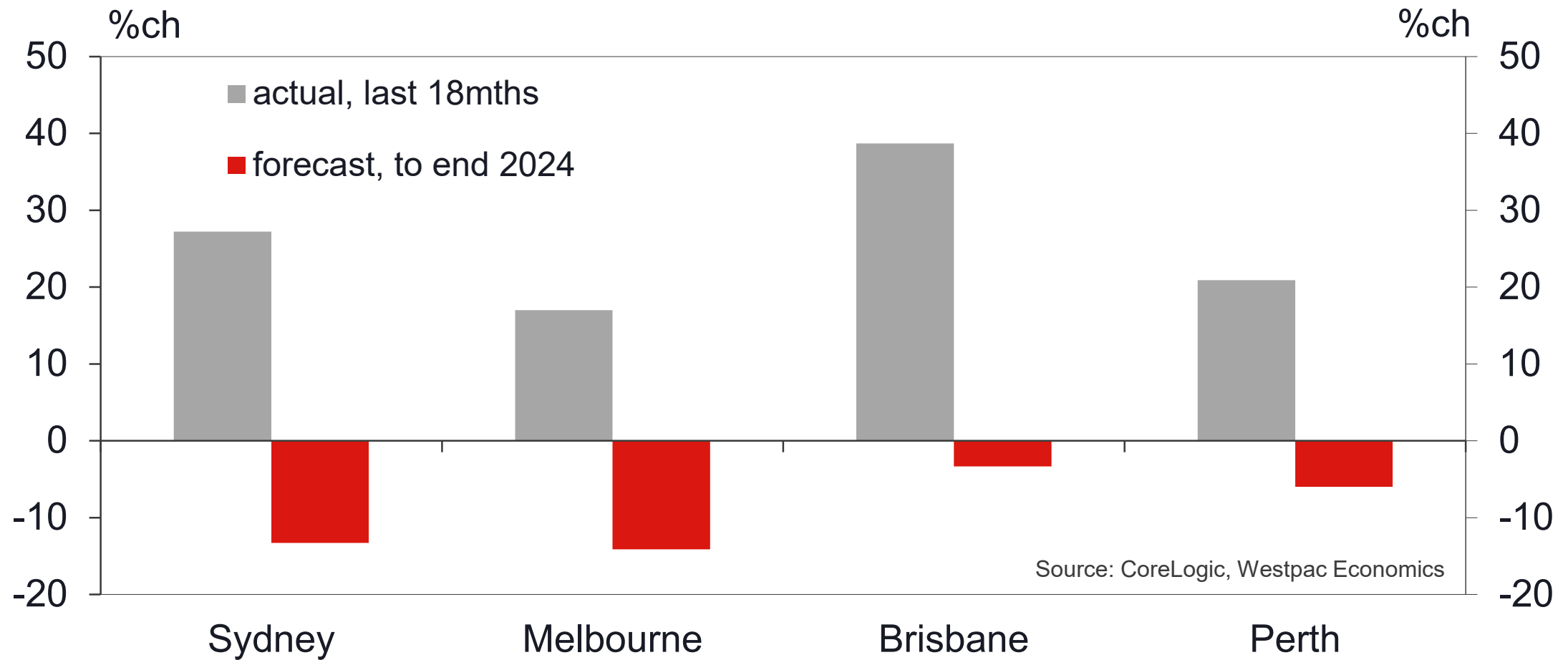
Affordability: upfront cost vs mortgage payment



Affordability: Sydney, Melbourne squeezed – need relief



House prices – turning point in 2022; back to April 2021 levels



Conclusion

- RBA to cut by 40 bp's in June – focus away from WPI; other central banks.
- Building sector under extreme pressure; inflation forces to ease in 2023
- Material and labour shortages at extreme levels – not seen since 70's; should ease by 2024; demand and supply shock slowdown key to easing in inflation.
- Unemployment rate to fall to 3.2% in 2022; rising by late 2023; wages peak in 2023.
- RBA cash rate to rise quickly in 2022 – 1.75% by year's end- peak at 2.25%; steady.
- High household debt will limit rate increases but offset by high savings – higher peak Debt Servicing Ratio than previous two peaks.
- With tight labour market inflation reduction relies on slowing interest sensitive sectors – housing; consumer spending; construction; house prices.
- US inflation slows in 2023; bond rates have peaked; rate cuts in 2024.
- Housing market appears to be coming under stress; confidence; price momentum.
- Housing stretched – supply; affordability; falling prices in 2023 and 2024.

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