AUSTRALIA & NEW ZEALAND WEEKLY.

Week beginning 31 October 2022

Editorial: RBA Board to raise the cash rate by 50bps on November 1.

RBA: policy decision, Governor speaking, Statement on Monetary Policy.

Australia: housing updates (prices, finance, dwelling approvals), retail sales, credit, trade balance.

NZ: unemployment rate, LCI, building consents, GlobalDairyTrade auction.

China: various PMIs, current account balance.

Europe: Q3 GDP, CPI, unemployment.

UK: BoE policy decision.

US: FOMC policy decision, ISMs, non-farm payrolls, trade balance, Chicago PMI, factory orders.

Key economic & financial forecasts.

INFORMATION CONTAINED IN THIS REPORT CURRENT AS AT 28 OCTOBER 2022.

WESTPAC INSTITUTIONAL BANK

RBA Board to raise the cash rate by 50bps on November 1

The September quarter inflation report has come as such a major surprise that we think the Reserve Bank Board will decide to raise the cash rate by 50bps at the next Board meeting on November 1.

The quarterly CPI print was an increase of 1.8% for the trimmed mean (the accepted measure for underlying inflation) well above market expectations of 1.5%. Annual trimmed mean inflation lifted to 6.1%yr. This is the highest quarterly and annual increase in underlying inflation since the ABS began producing estimates in 2002. Historical estimates compiled by the RBA show the quarterly rise is the biggest since 1988.

Of particular concern is the widening distribution of gains across Index components. We find that 90% of expenditure items have increased by 2.5% or more in the quarter. That compares with only 63% at the height of the mining boom.

During this period of rising inflation we have been most concerned about a strong inflationary psychology becoming entrenched in the Australian psyche. As this develops, businesses become more confident that they can raise their prices; consumers become more accepting of such action and see significant wage increases, in the context of tight labour markets, as necessary to compensate, sustaining the whole inflation process.

Evidence from the survey that pricing power is becoming widespread across expenditure items should be of considerable concern to an inflation-targeting central bank.

The Budget papers have raised the prospect of a 50%+ increase in electricity prices over 2022 and 2023. This means inflation overall will remain more elevated and poses further pressures on inflation psychology.

The best way for the central bank to break this nexus is to adopt strong rhetoric and strong action.

The Board should also be concerned about the unusual nature of this cycle as the economy emerges from the pandemic. Labour markets are uncharacteristically tight while the household sector has accumulated significant savings which can buffer higher rates. Evidence from business surveys that business conditions and capacity utilisation are remarkably strong also point to unusual resilience.

We do not believe that the Board has backed itself into a corner with its surprise, lower than expected 25bp increase at the October meeting. Note the final paragraph in the October Board Minutes: “The size and timing of future interest rate increases will continue to be determined by the incoming data and the Board’s assessment of the outlook for inflation and the labour market.”

That provides ample justification for speeding up the pace of increases again in response to a significant upside shock to the inflation outlook.

It seems very likely that the RBA staff, which is providing a full update to forecasts for the November meeting, will be meaningfully lifting its inflation outlook.

We would also expect some stronger guidance from the RBA Governor’s decision statement around the outlook. More emphasis on its clear determination to return inflation to the target is likely rather than the current message of a balancing act between achieving the target and keeping the economy ‘on an even keel’. Perhaps the line “Members saw this path to achieving this balance as a narrow one clouded in uncertainty” may not figure in the narrative going forward.

The discussion on policy deliberations in the October Minutes pointed to a close-run decision between the 25bp path and continuing with another 50bp move with “finely balanced arguments.”

In discussing the case for a 50bp move, the Board noted that: “Inflation was high, broadly based and expected to increase further” and that “If the Board were to reduce the size of the rate increase … [T]his might in turn prompt an unhelpful reaction in inflation expectations”.

The Governor clearly recognises the risks of embedding an inflationary psychology into the system.

We pointed out in a note “Unintended Consequences” (October 14) that there had been a significant lift in Consumer Sentiment and House Price Expectations following the decision to pivot to a 25bp move.

With markets and the media, to date, not embracing the prospect of a 50bp move in November there can be expected to be an appropriately adverse impact on Confidence to a decision to go by 50bps.

If the inflation report had been in line with expectations, then continuing the sequence of 25bp moves would have been appropriate. But not responding firmly to this genuine shock would risk the impression of a central bank that is less than fully committed to the inflation task.

This would risk further embedding a high inflation psychology into the Australian economy.

The level of interest rates does not appear to be a major issue for the Board.

When considering the October decision the Board described the cash rate, which at the time was 2.35%, as “not at an especially high level.” With the rate now at 2.6% there is still genuine uncertainty as to whether the Board views that level as above ‘neutral’.

The Governor has referred to ‘neutral’ as a positive real cash rate with the nominal component being assessed as 2.5% – a nominal cash rate above 2.5%.

A recent speech by Assistant Governor Ellis set out the RBA’s estimates of neutral in more detail – the conclusion from nine separate models used to generate estimates is that the average neutral rate appeared to be around 1% real or 3.5% nominal. But the Assistant Governor did emphasise that the neutral concept was most useful as a long-term guide and was not applied mechanistically to policy, along the lines of the ‘short term’ and ‘long term’ real concept deployed at one point by the Federal Reserve.

A decision to push the cash rate to 3.1% would certainly, in our view, put policy firmly in contractionary territory but the academic discussion is not definitive.

The Board decision to only raise rates by 25bp in October was also partly to assess the effect of the significant cumulative increase to date. Without the inflation shock that was a defensible position but given the risks to inflation psychology we have set out above, that strategy seems to be no longer appropriate.

Looking forward, after the 50bp move in November we expect a further 25bp move in December but with no meeting scheduled for January there will be a two month break to provide some time to assess the cumulative impact of rapid rate increases.

By the time of the February meeting, the Board will have raised the cash rate by only 25bps over the previous three months since the November move – an adequate and appropriate break.

We were impressed with the argument in the October Minutes that: "Dragging out policy adjustments would also help to keep public attention focussed for a longer period on the Bank's resolve to meet the inflation target." That is a reasonable view in a context where inflation is gradually easing while remaining above the target but not when inflation, as we saw in the latest report, is surging.

The wording in the Minutes gave more prominence to the global economy than we had seen in the past. The concluding paragraph noted that: "The Board will continue to monitor the global economy, household spending, and wage and price setting behaviour."

Recall that the meeting was held at a time of the huge volatility in financial markets associated with reactions to the UK mini–budget. Those concerns have largely settled down. Recent GDP data out of China has also exceeded market expectations. While there will no doubt continue to be justifiable global concerns, the immediate issues that were likely to have framed the Board in October have eased.

We obviously have considerable concerns about the eventual impact of these policies on Australians. Without doubt the Reserve Bank shares those views.

But globally, central banks have correctly signalled the overwhelming need to rein in inflation pressures – a delay in achieving that objective will only lead to unnecessary additional pain further down the road – as Australia experienced during the deep recession of the early 1990s following its failure to address the inflation issue during the 1980s.

The inflation report has clearly highlighted that Australia is not different to other countries. Inflation in Australia looks set to exceed US inflation by the end of the year.

The RBA faces the same inflation challenges as other central banks.

A decision to speed up the rate hike cycle in November is the appropriate action.

Bill Evans, Chief Economist

THE WEEK THAT WAS

This week, the second Australian Federal Budget for 2022 and the Q3 CPI report gave the market a lot to consider regarding Australia's outlook. The same was true offshore, with the Bank of Canada and ECB respectively delivering 'dovish' 50bp and 75bp hikes as US Q3 GDP made clear US private demand growth is slowing rapidly.

Beginning with October Budget 2022. Our Bulletin and conversation with Chief Economist Bill Evans provides a full view of the new Government's priorities and their economic expectations for the next four years. Most notable is that, while the starting point for October Budget 2022 is materially improved, the economy is expected to be weaken while spending grows rapidly, particularly interest costs and funding for the NDIS. As a result, net debt is forecast to continue rising to 2025/26, the last year of the forward estimates. Consistent with the policies Labor took to the election, October Budget 2022 focuses on providing cost of living relief for families through support for childcare; improving essential services, particularly aged care; and also commits to long-term investment in Australia's capacity and productivity.

The day after Budget 2022, the Q3 CPI print came in well above the market's expectation and our own. Critically, not only did headline inflation print at a challenging 1.8% (7.3%yr), so did the trimmed mean core (1.8%; 6.1%yr). Key contributors to the rise were housing (utilities and dwelling construction) and food. However, there was evidence of robust-to-strong inflation across the rest of the consumer basket.

In our view, it is therefore appropriate for the RBA to increase the cash rate by 50bps at the November meeting, and to follow that move with a further 75bps of cumulative tightening at the next three meetings to a peak of 3.85% in March (previously 3.60%). An on-hold posture will then be required over the remainder of 2023 to suppress inflation expectations and related risks. Chief Economist Bill Evans' bulletin provides a detailed assessment of our expectations regarding the RBA.

Turning to the US. The Q3 GDP outcome was, more or less, as we anticipated, with a circa 3ppt contribution from net exports masking a continued deterioration in private demand growth. From 2.2% annualised in Q1, private demand growth has slowed to just 0.6%. As the service sector re-opening fades and durable purchases come under greater pressure from interest rates and cost of living, this downtrend will persist – note that in Q3, dwelling construction declined at a 26% annualised rate and business investment growth was sub-par.

We remain of the view that the US is likely to see cumulative GDP growth of only 0.5% through 2022 and 2023, with risks skewed to the downside. It will be interesting to see whether the FOMC take a more cautious view on the outlook for the economy at their November meeting next week as they deliver another outsized 75bp hike. For the US, inflation risks are still acute, but the probability of a hard landing in 2023 is on the rise.

Regarding the forward view for monetary policy globally, both the Bank of Canada and ECB delivered what were perceived to be 'dovish' extraordinary hikes this week, the Bank of Canada (BoC) raising 50bps and the European Central Bank (ECB) 75bps. For the BoC, growth in 2023 is clearly at risk, but excess demand remains and inflation is yet to show definitive signs of slowing. Ergo, further measured hikes are expected to prove necessary. Meanwhile in Europe, the ECB affirmed their resolve to combat inflation whilst being cognisant of the immediate and medium-term risks to growth. There is still a need to raise interest rates, but with domestic demand already showing clear signs of weakening in H2 2022 under the weight of historic inflation and collapsed confidence, a slowing in the pace of rate hikes is becoming increasingly likely. We expect another 75bp of rate hikes into early 2023, leaving the refi rate at a peak of 2.75% through the rest of that year and into early 2024.

Finally then to China. The end of the National Party Congress was as expected, with President Xi being confirmed for a third term and the Standing Committee re-shaped to cement his authority. The initial reaction of markets was unfavourable, though this has dissipated somewhat. The hold that President Xi has over the party, China's development and COVID management is unnerving for many market participants. That said, the GDP and partial data for Q3 points to underlying economic strength.

In Q3, growth was more than a percentage point stronger than the market's expectation, the 3.9% gain reversing Q2's 2.7% loss. Year-to-date growth consequently bounced back to 3.0%, we expect on its way to 3.5% for the full year to be followed by 6.0% growth in 2023. From the GDP detail and monthly partial data, it is clear COVID management continues to pressure consumption and that residential construction is only starting to form a base after the provision of considerable stimulus. Supporting growth currently is fixed asset investment ex-housing and trade.

While trade with the US and Europe is under pressure as these economies stall and/or enter recession, Asia has capacity to offset. Not only does China stand to benefit from the region's organic growth, they are also looking to take a greater share of these markets for both consumer and industrial goods. China's decision to invest in and promote their own brands domestically over the past decade provides a strong foundation for their nascent Asian export expansion. So too the capital, production and know-how they are developing with respect to the green transition – a process Asia stands to benefit materially from. Of course, the greater China's interest in Asia becomes, the stronger their footing on the global stage. Geopolitical uncertainty is then expected to persist and potentially escalate in the years ahead.

Week ahead & data wrap

The labour market is red hot. And if anything, it has heated up further over recent months. Those signs of heat are also manifesting increasingly in pressure on wages. And while that's good news for workers in light of similarly red-hot inflation, this trend presents a fresh set of problems for businesses as well as the Reserve Bank.

Indeed, the labour market is crucial to the Reserve Bank's efforts to bring inflation under control. With the unemployment rate close to a record low, and employers desperate to fill labour shortages, pay rates have been the big labour market mover over the last year or so.

Those labour costs are in turn being passed through into prices – the latest CPI report shows that price rises are increasingly widespread across all categories. That's seen local forces starting to take over from global ones as the main source of overall inflation pressures.

With that in mind, the September quarter labour market surveys, released next Wednesday, are unlikely to give much comfort to the RBNZ. We expect a solid 0.6% rise in employment for the quarter, and a small dip in the unemployment rate back to its record low of 3.2%.

On top of that strong jobs growth, we also expect a 1% rise in the Labour Cost Index (LCI). That rise will see the annual growth rate jump to a 14-year high of 3.6%.

Our employment forecast is stronger than what the RBNZ assumed in its August Monetary Policy Statement. On the other hand, our wage growth forecast is a little softer – the RBNZ is already braced for some very strong wage growth, so it would take a lot to surprise them to the upside. That said, we're on the same page in expecting wage growth to head sharply higher.

Recent indicators, including tax data, suggest that jobs growth has regained some momentum in recent months after an earlier softer patch. While this measure doesn't entirely correspond with the Household Labour Force Survey – it measures jobs rather than workers, and some people will work more than one job – it has proven to be a reasonable guide on a quarterly basis. Notably, our forecast of 0.6% employment growth is actually to the low side of what the tax data would suggest.

One curiosity to this data is the question of where these workers have come from. The closure of the border over the last couple of years has meant a regular and key source of workers has been absent. Indeed, the working-age population has barely grown at all over this period. In addition, Jobseeker benefit numbers have been fairly flat, which suggests that not many of these additional workers have come out of the ranks of the unemployed. The tax data does, however, point to one group flooding into the labour market: over the past year, 40% of the growth in jobs has been among teenagers.

Altogether, this suggests to us that the lift in employment will be largely matched by a rise in the labour force participation rate, and as such the fall in the unemployment rate is likely to be modest. Participation has been high but choppy over the last several quarters, with a tug-of-war between rising youth participation and a growing share of the population hitting retirement age. That said, it pays to remember that any fall in the unemployment rate will see the rate either match or surpass the previous record low.

Digging into wage pressures a little more, we've assumed a 1% rise in the LCI for the September quarter. That follows a 1.1% rise in the June quarter (including a 1.3% rise in private sector wages), which was boosted by the 6% increase in the minimum wage for this year. On an annual basis, our forecast implies a further acceleration in labour costs, and we think that these costs will continue to run higher over the rest of the year and into next.

Meanwhile, the Quarterly Employment Survey measure of average hourly earnings comes closer to capturing what workers are actually getting in hand. This measure has risen even more sharply than the LCI, reaching 6.4% growth in the year to June (and 7% for the private sector). We expect to see a further acceleration in this measure for September as well.

The tight labour market and surging wages is one factor leading to economic pessimism amongst New Zealand businesses. Indeed, this week's ANZ business survey for October showed that a net 43% of businesses now expecting that economic conditions will weaken over the coming year. That's a deterioration from the already weak level that we saw in September.

The majority of businesses also expect that trading conditions on their own shop floors will remain subdued over the coming months. That pessimism is widespread across sectors.

The low level of confidence among New Zealand businesses isn't a surprise. While spending levels in the economy have held up, businesses are grappling with a range of challenges, including rising interest costs and the aforementioned ongoing shortages of staff. At the same time, wider operating costs have been charging higher, squeezing margins for many firms.

On this cost front, nearly 90% of businesses expect their operating costs will rise over the next few months, and 65% of them are planning on raising their prices. Both of those figures have eased back a little from their recent highs, but they still point to red-hot inflation pressures.

All up, weak business sentiment and the prospect of a red-hot labour market read next week are reinforcing that inflation pressures remain intense. Moreover, we're not seeing any material signs that they have started to abate despite the large rise in borrowing costs over the past year. With that in mind, we expect the RBNZ to match these intense pressures with a jumbo-sized 75bp OCR hike at its upcoming November policy meeting.

Nathan Penny, Senior Agri Economist

Round-up of local data released over the last week

Date	Release	Previous	Actual	Westpac f/c
Wed 26	Oct ANZ business confidence	-36.7	-42.7	–
Fri 28	Oct ANZ consumer confidence	85.4	85.4	–
	Sep employment indicator	0.4%	0.4%	0.5%

DATA PREVIEWS

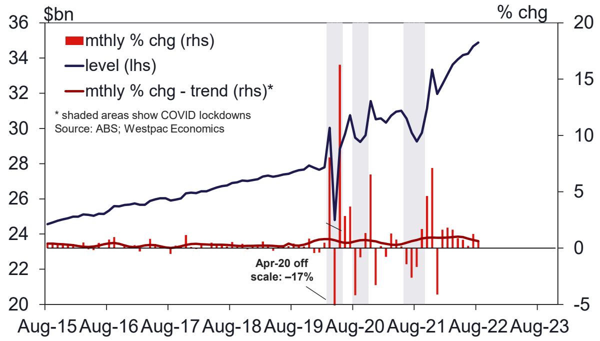
Aus Sep retail trade

Oct 31, Last: 0.6%, WBC f/c: 0.3%
Mkt f/c: 0.5%, Range: 0.3% to 0.9%

Retail sales posted a 0.6% gain in Aug, with rate rises still having little discernible impact. Growth has slowed since the RBA began lifting the cash rate in May but is still averaging 0.6–0.7%/mth. Moreover, much of that slowdown is due to 'cycling' the post-delta reopening rebound that saw much stronger gains at the start of the year.

Sep may start to show more rate rise impacts. However, indicators are fairly mixed. Retail components of our **Westpac Card Tracker Index** are only showing a gentle moderation so far and retail responses to private sector business surveys have been very mixed, some cooling in Sep but others remaining very strong. On balance, we expect nominal sales to show some slowing with a 0.3% gain in the Sep month, most, if not all, of this due to higher prices. Note that the final estimates, including Q3 real retail sales will be released at the end of the week (see page 8 for our preview).

Monthly retail sales



Aus Sep private sector credit

Oct 31, Last: 0.8%, WBC f/c: 0.7%
Mkt f/c: 0.7%, Range: 0.7% to 0.8%

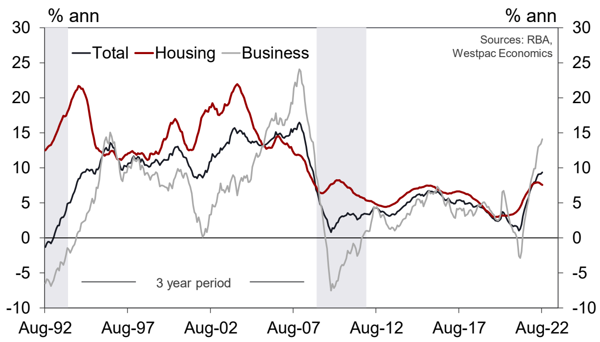
Annual credit growth lifted to 9.3% in August – the fastest annual pace since October 2008. Over the past year, businesses and households responded to very expansionary policy settings.

Currently, that stimulus is being unwound – leading to an emerging gradual slowing in the monthly pace of credit growth. For September, credit is expected to expand by 0.7% – edging down from outcomes of 0.8% for July and August, and from 0.9% gains each month through the June quarter.

Housing is cooling as borrowing capacity is reduced in the face of rising interest rates – new lending is down 17.5% over the past seven months. Housing credit grew 0.5% in August, down from gains of 0.7% at the start of the year.

Business lending grew by an unsustainable 19.6% annualised pace in the June quarter. Subsequently, the pace has moderated somewhat, but remains robust, as firms boost investment to expand capacity.

Credit: annual growth at 9.3%, a 14 year high



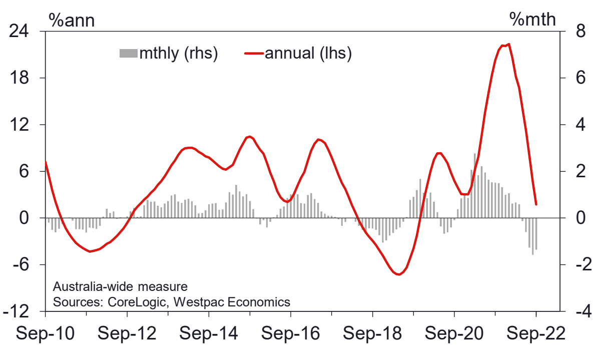
Aus Oct CoreLogic home value index

Nov 1, Last: –1.4%, WBC f/c: –1.2%

The housing market correction that began in May and accelerated through June–July, continued to run at a rapid pace in Aug–Sep, with declines of 1.6% and 1.4% respectively for the CoreLogic measure. The RBA's aggressive interest rate tightening is the dominant driver, with price weakness now spreading to most jurisdictions.

It's set to be a similar story for Oct, the daily index pointing to a further 1.2% decline for the month. That will take annual growth to –3.4%yr with a fall of 6.7% since Apr. While the slightly milder monthly pace and marginal improvement in auction markets suggest the correction is moderating, it continues to run at a relatively quick pace with little prospect of an end to rate rise pressures near term.

Australian dwelling prices



DATA PREVIEWS

Aus RBA policy decision

Nov 1, Last: 2.60%, WBC f/c: 3.10%
Mkt f/c: 2.85%, Range: 2.85% to 3.10%

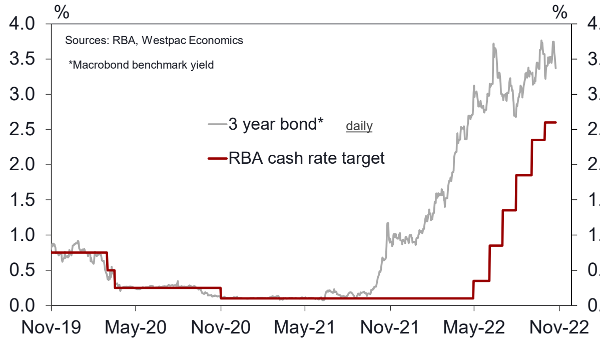
At the November Board meeting, Westpac anticipates that the RBA will lift the cash rate by 50bps, to 3.10%. This is a non consensus view – most commentators anticipate a move of 25bps.

In October, the RBA slowed the pace of tightening, raising rates by 0.25% after four consecutive moves of 0.50%. With rates arguably back in the neutral zone, the RBA felt that it was time to pivot. At the same time, the RBA kept its options open, with the decision statement indicating: “the size and timing of future interest rate increases will continue to be determined by the incoming data …”.

It is significant then that Q3 inflation data on October 26 was much higher than anticipated. The 1.8%qtr, 6.1%yr increase in trimmed mean inflation was a shock result. It demands a more urgent response from the RBA. With inflation higher for longer the concern is that a strong inflationary psychology may become entrenched.

For a more detailed discussion, see page 2.

RBA cash rate and 3 year bonds



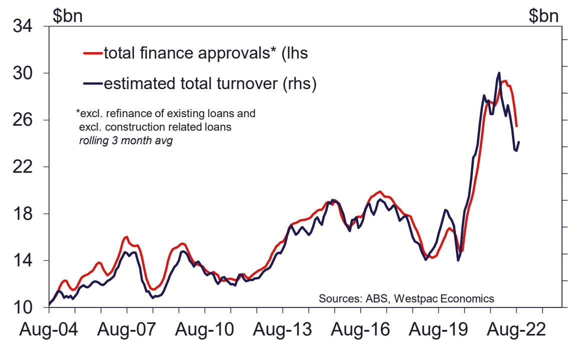
Aus Sep housing finance approvals

Nov 2, Last: –3.4%, WBC f/c: –2.5%
Mkt f/c: –3.0%, Range: –6.0% to +2.0%

Housing finance approvals posted a further 3.4% decline in Aug to be off 19.6% from their peak at the start of the year. Recent falls have centred on investor loans but owner occupiers have still been the main driver of the cycle in ‘dollar for dollar’ terms

Latest data on turnover and prices point to more weakening in Sep albeit at a slightly slower pace with some levelling out in turnover volumes since mid-year. We expect the total value of new finance approvals to be down 2.5%, investor loans continuing to run slightly weaker (–3%) than owner occupiers (–2.3%).

New finance approvals vs value of sales



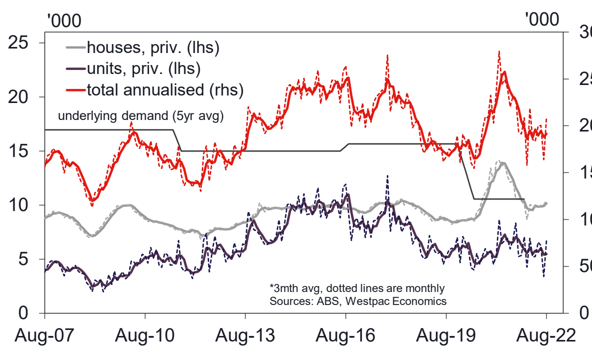
Aus Sep dwelling approvals

Nov 2, Last: 28.1%, WBC f/c: –5.0%
Mkt f/c: –10.0%, Range: –16.0% to –5.0%

Dwelling approvals produced a large upside surprise in Aug, with a much stronger than expected 28.1% rebound out of July’s 17.2% slump. Total approvals were 4.8% above their June level and up 1% for the three months to Aug vs the three months to May. This is despite numerous headwinds including: aggressive rate rises; a material correction across wider housing markets; sharp rises in the cost of building and associated strains on builders still working through a large backlog of unprofitable work; and uncertainties around the timing and ultimate cost of new builds due to widespread supply issues affecting both materials and labour.

We expect Sep to show a much weaker tone as the these negatives start to come more to the fore. Approvals are forecast to decline 5% but given recent volatility, particularly around high rise, there is a risk that they show a sharper move lower.

Dwelling approvals



Aus Sep trade balance, AUDbn

Nov 3, Last: 8.3, WBC f/c: 9.1
Mkt f/c: 9.0, Range: 7.0 to 10.5

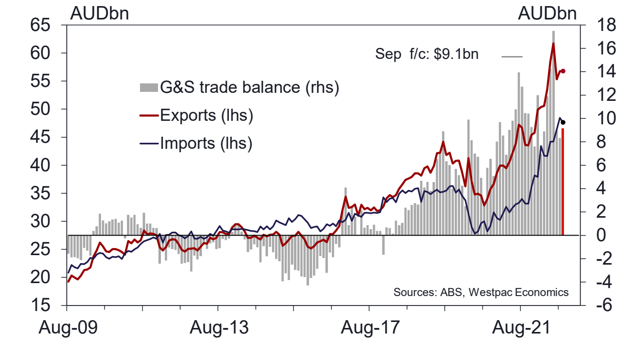
Australia's trade surplus ballooned to back-to-back fresh record highs of $14.3bn and $17.5bn in May and June – inflated by the spike in commodity prices, in part triggered by the Ukraine war.

Subsequently, global recession fears have sent commodity prices lower. The trade surplus narrowed to $9.0bn in July and then $8.3bn in August. For September, we anticipate a surplus of $9.1bn.

Export earnings are expected to be flat in September. Coal shipments were again disrupted by flooding. This hit will potentially be offset by higher iron ore volumes and a lift in service exports.

For imports, we've factored in a –1.7% decline, –$0.8bn. Global energy prices were lower in the month. In addition, import volumes potentially eased a little after a burst over July and August – which appeared to include an element of catch-up in deliveries from China, recovering from earlier disruptions.

Australia's trade balance



Aus Q3 real retail sales

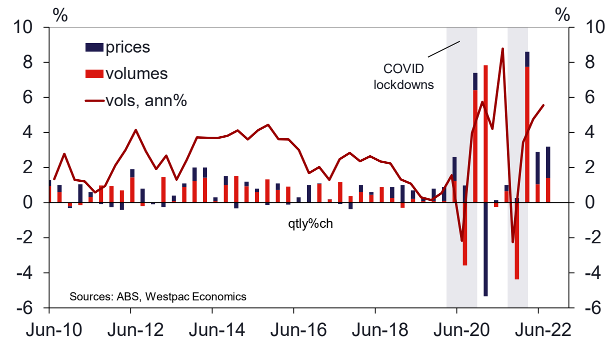
Nov 4, Last: 1.4%, WBC f/c: 0.2%
Mkt f/c: 0.4%, Range: 0.0% to 1.7%

Real retail sales posted a robust 1.4% gain in Q2 but are expected to have nearly stalled flat in Q3 as a sharp spike in retail prices rolls through.

Nominal sales are tracking a decent 2.2%qtr gain for the quarter, down marginally on the very strong re-opening supported 3.2% rise in Q2. The Q3 CPI detail points to a big rise in retail prices which are expected to be up 2%qtr, 6.5%yr. That points to a real retail sales gain of just 0.2%qtr. Annual growth will tick over 10%yr but is flattered by base effects, Q3 last year being affected by 'delta' lockdowns.

Note that the final Sep retail report will also include more granular detail by state and industry, and by channel and business size.

Quarterly retail volumes and prices



NZ Sep residential building consents

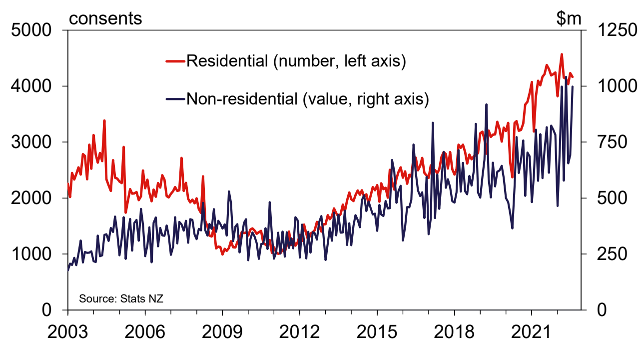
Nov 1, Last: –1.6%, Westpac f/c: –5.0%

We expect that dwelling consent issuance will fall by around 5% in September. That drop is mainly related to consents for retirement village units which spiked higher over the past few months, and we expect a return to more normal levels in September.

Underlying the volatility in 'lumpy' categories like retirement units, the monthly trend in consent issuance has effectively been tracking sideways for around a year now. However, under the surface, we have seen a switch in the composition of homes that are being built, with fewer standalone houses and increasing numbers of medium density developments like townhouses.

We expect that less favourable financial incentives for both purchasers and developers will see consent issuance start to trend down over the year ahead.

NZ building consents



NZ GlobalDairyTrade auction, whole milk powder prices

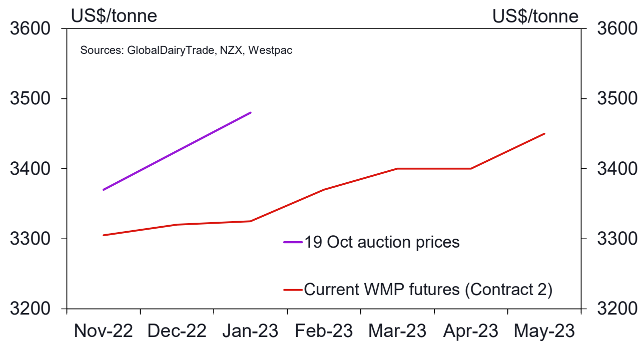
Nov 2, Last: –4.4%, Westpac: –2.0%

We expect whole milk powder prices (WMP) to fall by around 2% at the upcoming auction. This follows a 4.4% price slide at the previous auction.

Our pick is in line with futures market pricing (as at 10am Friday 28 October).

Fundamentally, very weak global dairy supply is underpinning the medium term global dairy price outlook. However, weak demand on the back of a soft Chinese economy led global dairy prices lower over October. We expect that this trend will continue in the short term.

Whole milk powder prices



NZ Q3 Household Labour Force Survey

Nov 2, Employment last: Flat, Westpac f/c: +0.6%, Mkt: +0.5%
Unemployment rate last: 3.3%, Westpac f/c: 3.2%, Mkt: 3.2%

We expect a solid 0.6% lift in employment for the September quarter. The demand for workers remains red-hot, and tax data suggests that jobs growth has regained some momentum in recent months.

That rise in employment is expected to be largely matched by a rise in labour forecast participation, with the unemployment rate expected to dip back to the record low of 3.2% that we saw earlier in the year.

Our employment forecast is stronger than what the RBNZ assumed in its August Monetary Policy Statement.

NZ Household Labour Force Survey

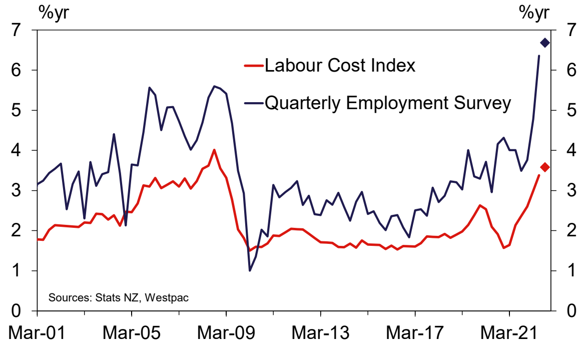
NZ Q3 Labour Cost Index

Nov 2, Private sector last: 1.3%, Westpac f/c: 1.0%, Mkt: +1.1%

Wage growth has been picking up over the last year, reflecting the tight jobs market. We're forecasting a 1% rise in the Labour Cost Index over the September quarter. That would see annual private sector wage inflation rising to 3.7% (up from 3.4% in the June quarter). That would be the fastest pace of wage growth in fourteen years, and we think that there is more to come over the coming year.

Similarly, we expect the Quarterly Employment Survey will show that average hourly earnings (a better measures of what workers get in the hand) has risen by 7.6% over the past year. That's been boosted by the high level of consumer price inflation and related adjustments to wages.

NZ salary and wage growth, all sectors



US Nov FOMC meeting

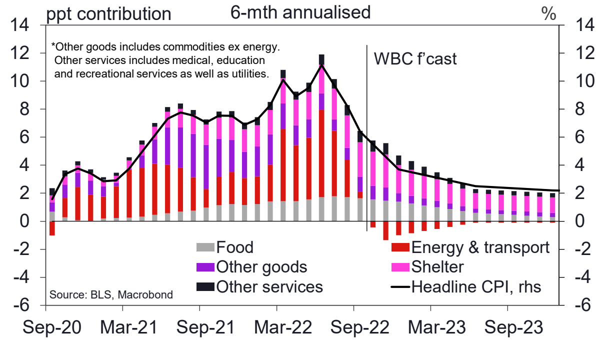
Nov 2–3, Last: 3.125%, Mkt f/c: 3.875%, WBC f/c: 3.875%

The past week has seen a slightly more dovish line taken by both the Bank of Canada and European Central Bank. While not yet ready to stop hiking, they are considering slowing down.

The market will keenly assess if the FOMC is in a similar frame of mind after the November meeting, when they are expected to deliver another outsized 75bp hike.

Q3 GDP and the deceleration in job creation and wages apparent in recent data certainly argues that the FOMC should begin to consider growth as well as inflation, though we still expect another 75bp of hikes over December and January before the Committee go on hold. The October payrolls survey on Friday will also evince the risks to 2023 from the FOMC's tightening, with the pace of job creation to be watched very closely.

US inflation is past its peak



Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.

For the week ahead

		Last	Market median	Westpac forecast	Risk/Comment
Mon 31					
Aus	Sep retail sales	0.6%	0.5%	0.3%	Gentle slowdown in nominal sales, partly reflecting price rises.
	Sep private sector credit	0.8%	0.7%	0.7%	Emerging gradual slowdown as policy stimulus reversed.
	Oct MI inflation gauge %yr	5.0%	–	–	Inflation well above RBA's target band.
Jpn	Sep industrial production	3.4%	–0.8%	–	Interim fragility on weather; softer global demand still a risk.
Chn	Oct manufacturing PMI	50.1	50.0	–	Ongoing virus risks are headwinds for mfg activity...
	Oct non-manufacturing PMI	50.6	50.1	–	... and holding back momentum in services.
Eur	Oct CPI %yr	10.0%	–	–	Core inflation remains uncomfortably high.
	Q3 GDP	0.8%	–	–	Clearer weakening in domestic demand to be evident.
US	Oct Chicago PMI	45.7	47.2	–	Weakening of conditions is becoming...
	Oct Dallas Fed index	–17.2	–16.8	–	... more broadly-based across the nation.
Tue 01					
Aus	Oct CoreLogic home value index	–1.4%	–	–1.2%	Correction continues to run at a relatively quick pace.
	RBA policy decision	2.60%	2.85%	3.10%	RBA to respond to deteriorating inflation outlook.
	Melbourne Cup	–	–	–	Public holiday (Vic). Deuville Legend favoured by bookies.
	RBA Governor speaking	–	–	–	RBA Board Dinner, Hobart, 7:20pm AEDT.
NZ	Sep building permits	–1.6%	–	–5.0%	Pullback in retirement village numbers, other categories flat.
Jpn	Oct Nikkei manufacturing PMI	50.7	–	–	Final estimate.
Chn	Oct Caixin manufacturing PMI	48.1	48.5	–	Pointing to downside risks for smaller/mid-sized firms.
UK	Oct S&P Global manufacturing PMI	45.8	–	–	Final estimate.
US	Oct S&P Global manufacturing PMI	49.9	49.9	–	Final estimate.
	Sep JOLTS job openings	10053k	9750k	–	Job openings off peak but still strong.
	Sep construction spending	–0.7%	–0.5%	–	Near-term weakening in demand weighing on construction.
	Oct ISM manufacturing	50.9	50.0	–	Mfg sector is in a fragile state.
Wed 02					
Aus	Sep housing finance	–3.4%	–3.0%	–2.5%	Down sharply since the start of the year and more falls...
	Sep owner occupier finance	–2.7%	–	–2.3%	... to come, albeit with some stabilisation in sales volumes...
	Sep investor finance	–4.8%	–	–3.0%	... pointing to a more moderate pace in the Sep month.
	Sep dwelling approvals	28.1%	–10.0%	–5.0%	Defied the downturn so far but set to weaken, downside risks.
NZ	GlobalDairyTrade auction (WMP)	–4.4%	–	–2.0%	Global dairy prices to fall on soft Chinese demand.
	RBNZ Financial Stability Report	–	–	–	Six-monthly review of the financial system's health.
	Q3 employment	0.0%	0.5%	0.6%	Jobs have regained some momentum in recent months...
	Q3 unemployment rate	3.3%	3.2%	3.2%	... suggesting a further dip in the unemployment rate.
	Q3 LCI wage inflation (pvte, ord. time)	1.3%	1.1%	1.0%	Annual wage growth accelerating in a tight labour market.
Eur	Oct S&P Global manufacturing PMI	46.6	46.6	–	Final estimate.
US	FOMC policy decision, midpoint	3.125%	3.875%	3.875%	Strength of core CPI warrants fourth consecutive 75bp hike.
Thu 03					
Aus	Sep trade balance $bn	8.3	9.0	9.1	Exports flat (coal vols down), imports to dip after strong burst.
	RBA Head of Domestic Markets	–	–	–	Kearns, panel participant, ASIC Forum, Sydney, 4pm.
NZ	Oct ANZ commodity prices	–0.5%	–	–	Dairy prices fell over October.
Chn	Oct Caixin services PMI	49.3	48.9	–	Virus risks continue to loom over services growth.
Eur	Sep unemployment rate	6.6%	6.6%	–	Holding at record lows.
UK	BoE policy decision	2.25%	3.00%	3.00%	Another 75bp rate hike locked in.
	Oct S&P Global services PMI	47.5	–	–	Final estimate.
US	Sep trade balance US$bn	–67.4	–70.2	–	Decline in domestic demand weighing heavily on imports.
	Q3 productivity	–4.1%	–0.1%	–	Challenging productivity outlook into year-end.
	Initial jobless claims	217k	–	–	Likely to remain at low levels, at least for time being.
	Oct S&P Global services PMI	46.6	46.6	–	S&P Global materially weaker than ISM...
	Oct ISM non-manufacturing	56.7	55.5	–	... pointing to clear downside risks for the sector.
	Sep factory orders	0.0%	0.4%	–	Drag on capital investment...
	Sep durable goods orders	0.4%	–	–	... extending into Q3.
Fri 04					
Aus	RBA Statement on Monetary Policy	–	–	–	Forecast update.
	Q3 real retail sales	1.4%	0.4%	0.2%	Sharp slowdown as price surge impacts.
Jpn	Oct Nikkei services PMI	53.0	–	–	Final estimate.
Chn	Q3 current account balance US$bn	77.5	–	–	Weaker trade into year-end on cooling global demand.
Eur	Oct S&P Global services PMI	48.2	48.2	–	Final estimate.
US	Oct non-farm payrolls	263k	200k	220k	Slowdown in jobs growth to crystalise...
	Oct unemployment rate	3.5%	3.6%	3.6%	... but U/E likely to remain little-changed near-term...
	Oct average hourly earnings %mth	0.3%	0.3%	0.3%	... putting off the next leg down in wages growth.
	Fedspeak	–	–	–	Collins.

Forecasts

Interest rate forecasts

Australia	Latest (28 Oct)	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24
Cash	2.60	3.35	3.85	3.85	3.85	3.85	3.60	3.35
90 Day BBSW	3.05	3.80	4.05	4.05	4.05	3.97	3.72	3.47
3 Year Swap	3.88	3.90	4.00	3.85	3.70	3.60	3.55	3.50
3 Year Bond	3.27	3.55	3.70	3.60	3.50	3.40	3.35	3.30
10 Year Bond	3.76	3.70	3.50	3.40	3.20	3.00	2.80	2.70
10 Year Spread to US (bps)	-16	-10	-10	-10	-10	-10	-10	0
US								
Fed Funds	3.125	4.375	4.625	4.625	4.625	4.625	4.375	3.875
US 10 Year Bond	3.92	3.80	3.60	3.50	3.30	3.10	2.90	2.70
New Zealand								
Cash	3.50	4.25	4.75	5.00	5.00	5.00	5.00	5.00
90 day bill	4.06	4.55	5.00	5.10	5.10	5.10	5.10	4.80
2 year swap	4.97	5.30	5.20	5.10	4.90	4.70	4.40	4.10
10 Year Bond	4.21	4.70	4.60	4.50	4.30	4.10	3.90	3.80
10 Year Spread to US	29	90	100	100	100	100	100	110

Exchange rate forecasts

Australia	Latest (28 Oct)	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24
AUD/USD	0.6458	0.65	0.66	0.67	0.69	0.72	0.73	0.74
NZD/USD	0.5829	0.58	0.59	0.60	0.62	0.65	0.66	0.66
USD/JPY	146.11	143	141	139	137	134	132	130
EUR/USD	0.9972	1.00	1.01	1.02	1.04	1.07	1.09	1.10
GBP/USD	1.1572	1.14	1.15	1.16	1.17	1.20	1.22	1.24
USD/CNY	7.2260	7.00	6.80	6.60	6.40	6.30	6.20	6.15
AUD/NZD	1.1071	1.12	1.12	1.12	1.11	1.11	1.11	1.12

Australian economic growth forecasts

	2021	2022				2023		Calendar years			
% change	**Q4**	**Q1**	**Q2**	**Q3f**	**Q4f**	**Q1f**	**Q2f**	**2020**	**2021**	**2022f**	**2023f**
GDP % qtr	3.9	0.7	0.9	1.1	0.6	0.3	0.2	–	–	–	–
%yr end	4.5	3.3	3.6	6.7	3.4	3.0	2.2	-0.7	4.5	3.4	1.0
Unemployment rate %	4.7	4.0	3.8	3.5	3.3	3.4	3.8	6.8	4.7	3.3	4.5
Wages (WPI)	0.7	0.7	0.7	1.1	1.2	1.1	1.0	–	–	–	–
annual chg	2.3	2.4	2.6	3.1	3.7	4.2	4.4	1.4	2.3	3.7	4.5
CPI Headline*	1.3	2.1	1.8	1.8				–	–	–	–
annual chg*	3.5	5.1	6.1	7.3				0.9	3.5		
Trimmed mean*	1.0	1.5	1.6	1.8				–	–	–	–
annual chg*	2.6	3.7	4.9	6.1				1.2	2.6		

** Inflation forecasts under review, following Q3 update.*

New Zealand economic growth forecasts

	2021	2022				2023		Calendar years			
% change	**Q4**	**Q1**	**Q2**	**Q3f**	**Q4f**	**Q1f**	**Q2f**	**2020**	**2021**	**2022f**	**2023f**
GDP % qtr	3.0	-0.2	1.7	0.4	0.6	0.6	0.5	–	–	–	–
Annual avg change	5.5	4.9	1.0	2.4	2.2	2.8	3.2	-2.1	5.5	2.2	2.2
Unemployment rate %	3.2	3.2	3.3	3.2	3.3	3.5	3.6	4.9	3.2	3.3	3.8
CPI % qtr	1.4	1.8	1.7	2.2	0.5	1.3	0.9	–	–	–	–
Annual change	5.9	6.9	7.3	7.2	6.2	5.7	4.9	1.4	5.9	6.2	4.1

Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.

DISCLAIMER

Things you should know.

Westpac Institutional Bank is a division of Westpac Banking Corporation ABN 33 007 457 141 (‘Westpac’).

Disclaimer

This material contains general commentary only and is not intended to constitute or be relied upon as personal financial advice. To the extent that this material contains any general advice, it has been prepared without taking into account your objectives, financial situation or needs, and because of this, you should, before acting on it, consider the appropriateness of the advice, having regard to your objectives, financial situation and needs, and, the disclosure documents (including any product disclosure statement) of any financial product you may consider. Certain types of transactions, including those involving futures, options and high yield securities give rise to substantial risk and are not suitable for all investors. We recommend that you seek your own independent legal or financial advice before proceeding with any investment decision. This material may contain material provided by third parties. While such material is published with the necessary permission none of Westpac or its related entities accepts any responsibility for the accuracy or completeness of any such material. Although we have made every effort to ensure the information is free from error, none of Westpac or its related entities warrants the accuracy, adequacy or completeness of the information, or otherwise endorses it in any way. Except where contrary to law, Westpac and its related entities intend by this notice to exclude liability for the information. The information is subject to change without notice and none of Westpac or its related entities is under any obligation to update the information or correct any inaccuracy which may become apparent at a later date. The information contained in this material does not constitute an offer, a solicitation of an offer, or an inducement to subscribe for, purchase or sell any financial instrument or to enter a legally binding contract. Past performance is not a reliable indicator of future performance. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

Country disclosures

Australia: Westpac holds an Australian Financial Services Licence (No. 233714). This material is provided to you solely for your own use and in your capacity as a client of Westpac.

For XYLO Foreign Exchange clients: This information is provided to you solely for your own use and is not to be distributed to any third parties. XYLO Foreign Exchange is a division of Westpac Banking Corporation ABN 33 007 457 141 and Australian credit licence 233714. Information is current as at date shown on the publication. This information has been prepared without taking account of your objectives, financial situation or needs. Because of this you should, before acting on this information, consider its appropriateness, having regard to your objectives, financial situation or needs. XYLO Foreign Exchange’s combined Financial Services Guide and Product Disclosure Statement can be obtained by calling XYLO Foreign Exchange on 1300 995 639, or by emailing customercare@XYLO.com.au.

New Zealand: In New Zealand, Westpac Institutional Bank refers to the brand under which products and services are provided by either Westpac or Westpac New Zealand Limited (“WNZL”). Any product or service made available by WNZL does not represent an offer from Westpac or any of its subsidiaries (other than WNZL). Neither Westpac nor its other subsidiaries guarantee or otherwise support the performance of WNZL in respect of any such product. The current disclosure statements for the New Zealand branch of Westpac and WNZL can be obtained at the internet address www.westpac.co.nz. For further information please refer to the Product Disclosure Statement (available from your Relationship Manager) for any product for which a Product Disclosure Statement is required, or applicable customer agreement. Download the Westpac NZ QFE Group Financial Advisers Act 2008 Disclosure Statement at www.westpac.co.nz.

China, Hong Kong, Singapore and India: This material has been prepared and issued for distribution in Singapore to institutional investors, accredited investors and expert investors (as defined in the applicable Singapore laws and regulations) only. Recipients in Singapore of this material should contact Westpac Singapore Branch in respect of any matters arising from, or in connection with, this material. Westpac Singapore Branch holds a wholesale banking licence and is subject to supervision by the Monetary Authority of Singapore. Westpac Hong Kong Branch holds a banking license and is subject to supervision by the Hong Kong Monetary Authority. Westpac Hong Kong branch also holds a license issued by the Hong Kong Securities and Futures Commission (SFC) for Type 1 and Type 4 regulated activities. This material is intended only to “professional investors” as defined in the Securities and Futures Ordinance and any rules made under that Ordinance. Westpac Shanghai and Beijing Branches hold banking licenses and are subject to supervision by the China Banking and Insurance Regulatory Commission (CBIRC). Westpac Mumbai Branch holds a banking license from Reserve Bank of India (RBI) and subject to regulation and supervision by the RBI.

UK: The contents of this communication, which have been prepared by and are the sole responsibility of Westpac Banking Corporation London and Westpac Europe Limited. Westpac (a) has its principal place of business in the United Kingdom at Camomile Court, 23 Camomile Street, London EC3A 7LL, and is registered at Cardiff in the UK (as Branch No. BR00106), and (b) authorised and regulated by the Australian Prudential Regulation Authority in Australia. Westpac is authorised in the United Kingdom by the Prudential Regulation Authority. Westpac is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request. Westpac Europe Limited is a company registered in England (number 05660023) and is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

This communication is being made only to and is directed at (a) persons who have professional experience in matters relating to investments who fall within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the “Order”) or (b) high net worth entities, and other persons to whom it may otherwise lawfully be communicated, falling within Article 49(2)(a) to (d) of the Order (all such persons together being referred to as “relevant persons”). Any person who is not a relevant person should not act or rely on this communication or any of its contents.

Disclaimer continued overleaf

DISCLAIMER

Disclaimer continued

The investments to which this communication relates are only available to and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such investments will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely upon this communication or any of its contents. In the same way, the information contained in this communication is intended for "eligible counterparties" and "professional clients" as defined by the rules of the Financial Conduct Authority and is not intended for "retail clients". With this in mind, Westpac expressly prohibits you from passing on the information in this communication to any third party. In particular this communication and, in each case, any copies thereof may not be taken, transmitted or distributed, directly or indirectly into any restricted jurisdiction. This communication is made in compliance with the Market Abuse Regulation (Regulation(EU) 596/2014).

Investment Recommendations Disclosure

The material may contain investment recommendations, including information recommending an investment strategy. Reasonable steps have been taken to ensure that the material is presented in a clear, accurate and objective manner. Investment Recommendations for Financial Instruments covered by MAR are made in compliance with Article 20 MAR. Westpac does not apply MAR Investment Recommendation requirements to Spot Foreign Exchange which is out of scope for MAR.

Unless otherwise indicated, there are no planned updates to this Investment Recommendation at the time of publication. Westpac has no obligation to update, modify or amend this Investment Recommendation or to notify the recipients of this Investment Recommendation should any information, including opinion, forecast or estimate set out in this Investment Recommendation change or subsequently become inaccurate.

Westpac will from time to time dispose of and acquire financial instruments of companies covered in this Investment Recommendation as principal and act as a market maker or liquidity provider in such financial instruments.

Westpac does not have any proprietary positions in equity shares of issuers that are the subject of an investment recommendation.

Westpac may have provided investment banking services to the issuer in the course of the past 12 months.

Westpac does not permit any issuer to see or comment on any investment recommendation prior to its completion and distribution.

Individuals who produce investment recommendations are not permitted to undertake any transactions in any financial instruments or derivatives in relation to the issuers covered by the investment recommendations they produce.

Westpac has implemented policies and procedures, which are designed to ensure conflicts of interests are managed consistently and appropriately, and to treat clients fairly.

The following arrangements have been adopted for the avoidance and prevention of conflicts in interests associated with the provision of investment recommendations.

I. Chinese Wall/Cell arrangements;

II. physical separation of various Business/Support Units;

III. Strict and well defined wall/cell crossing procedures;

IV. a "need to know" policy;

V. documented and well defined procedures for dealing with conflicts of interest;

VI. reasonable steps by Compliance to ensure that the Chinese Wall/Cell arrangements remain effective and that such arrangements are adequately monitored.

U.S.: Westpac operates in the United States of America as a federally licensed branch, regulated by the Office of the Comptroller of the Currency. Westpac is also registered with the US Commodity Futures Trading Commission ("CFTC") as a Swap Dealer, but is neither registered as, or affiliated with, a Futures Commission Merchant registered with the US CFTC. Westpac Capital Markets, LLC ('WCM'), a wholly-owned subsidiary of Westpac, is a broker-dealer registered under the U.S. Securities Exchange Act of 1934 ('the Exchange Act') and member of the Financial Industry Regulatory Authority ('FINRA'). This communication is provided for distribution to U.S. institutional investors in reliance on the exemption from registration provided by Rule 15a-6 under the Exchange Act and is not subject to all of the independence and disclosure standards applicable to debt research reports prepared for retail investors in the United States. WCM is the U.S. distributor of this communication and accepts responsibility for the contents of this communication. All disclaimers set out with respect to Westpac apply equally to WCM. If you would like to speak to someone regarding any security mentioned herein, please contact WCM on +1 212 389 1269. All disclaimers set out with respect to Westpac apply equally to WCM.

Investing in any non-U.S. securities or related financial instruments mentioned in this communication may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the SEC in the United States. Information on such non-U.S. securities or related financial instruments may be limited. Non-U.S. companies may not subject to audit and reporting standards and regulatory requirements comparable to those in effect in the United States. The value of any investment or income from any securities or related derivative instruments denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related derivative instruments.

The author of this communication is employed by Westpac and is not registered or qualified as a research analyst, representative, or associated person under the rules of FINRA, any other U.S. self-regulatory organisation, or the laws, rules or regulations of any State. Unless otherwise specifically stated, the views expressed herein are solely those of the author and may differ from the information, views or analysis expressed by Westpac and/or its affiliates.