AUSTRALIA & NEW ZEALAND WEEKLY.

Week beginning 31 July 2023

Editorial: RBA to raise the cash rate by 25bps next week.

RBA: policy decision, Statement on Monetary Policy.

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

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

China: NBS and Caixin PMIs.

Eurozone: Q2 GDP, CPI, unemployment rate, retail sales.

UK: BoE policy decision.

US: nonfarm payrolls, unemployment rate, ISMs, factory orders, Chicago PMI.

Key economic & financial forecasts.

INFORMATION CONTAINED IN THIS REPORT
CURRENT AS AT 28 JULY 2023.

WESTPAC INSTITUTIONAL BANK

RBA Board to raise the cash rate by 25 basis points at the August meeting – maintain tightening bias

The Reserve Bank Board meets next week on August 1.

Westpac has consistently argued that a further increase in the cash rate should be the appropriate policy response at the August meeting and we confirm that view.

We also believe that the Board should maintain its tightening bias, repeating the sentence: "Some further tightening of monetary policy may be required to ensure that inflation returns to target in a reasonable timeframe."

Previously we had a firm view that a follow-up increase in September would be required. We are now comfortable that maintenance of the tightening bias beyond August should be sufficient.

Markets and most commentators have concluded that the better print on headline inflation for the June quarter will be sufficient for the Board to extend the pause that it began in July for another month.

That is a quite reasonable position to take given the policy approach taken by the Board at the June and July meetings. For both meetings the key factor behind the decision to hike in June and pause in July centred around the monthly headline inflation reports.

In June, the annual headline from the monthly indicator lifted from 6.3% to 6.8%, prompting an increase of 0.25%; whereas in July the monthly indicator slowed from 6.8% to 5.6% prompting the decision to pause.

In both months other developments, particularly around the labour market and services inflation, were arguably consistent with a different decision (the most notable exception being the minimum wage decision delivered just prior to the June Board meeting).

So, how can we possibly not go with the market for August when the quarterly headline Inflation report was softer than expected and the monthly indicator showed a further modest reduction from 5.6% to 5.4%?

Headline inflation printed 6.0% for the year to June compared to the RBA's forecast of 6.3% when it released its forecasts in the May Statement on Monetary Policy, and down from 7.0% in the year to March.

The RBA Board will undoubtedly look more deeply into the June quarterly report for inflation than is possible with the monthly indicator.

It will find that the 5.9% print for core inflation (trimmed mean) compared to the RBA's forecast of 6.0% – a much closer result. That print was down from 6.6% in the year to March.

Annual goods inflation fell from 7.6% to 5.8%. On the other hand, annual services inflation lifted from 6.1% to 6.3%.

The ABS calculated that quarterly services inflation slowed from 1.7% in March to 0.8% in June. June is a low seasonal quarter for services – June 2023 was in fact higher than the gain in June 2022 (0.6%).

A more reliable measure of services inflation is "market services ex volatile items". This measure excludes the government administered prices therefore capturing the economic cycle. The quarterly increase in this measure lifted from 0.9% to 1.2%, while annual growth held steady at 6.8%.

The detail around services inflation and core inflation is less encouraging than the headline result.

Central banks favour the core number because it is a more reliable indicator of ongoing inflation momentum.

While the decision at the last two meetings was reliant on the monthly indicator, the decision at the August meeting can draw on the much more reliable and detailed information from the quarterly report.

We had a similar situation at the May Board meeting.

Following a material fall in annual headline inflation in the March inflation report, markets dismissed the possibility of a rate increase in May. After all, headline inflation had fallen from 7.8% to 7.0% in a single quarter.

But the Board surprised with a hike, having the benefit of the more detailed quarterly report, which showed a further lift in services inflation (5.5% to 6.1%).

The theme behind much of the Board's concern around its inflation challenge, at the May meeting and continuing, has been that "inflation was not expected to reach the top of the target band until mid-2025 … although this was consistent with the Bank's mandate and objectives, it left little room for upside surprises to inflation given that inflation would have been above target for around four years by that time." (May minutes).

This explanation was given as a central reason for the surprise rate hike in May.

Notably also, despite the March result, the staff did not lower its forecast track for inflation – with underlying inflation still projected to reach 2.9% by June 2025.

The key to the August policy decision is whether the Board and staff feel comfortable enough to lower their inflation forecasts following the June inflation result.

The Bank' refreshed forecasts in August – to be published in Fridays' Statement on Monetary Policy – will be extended out to December 2025. It would be very difficult for the Board if the forecasts still did not have inflation reaching the 2.5% mid-point of the target by end 2025.

During my recent trip to the East Coast of the US; Europe; and London, I noted consistent criticism of the Board's approach of being comfortable to reach the top of the target band after being outside the band for so long.

The current forecasts only have the core inflation rate falling from 3.1% to 2.9% (–0.2ppts) over the first six months of 2025. Arguing for a much faster fall in the second half of 2025 is not credible given that growth is forecast to be picking up in 2025.

So, to justify an earlier achievement of the target, the progress will need to be in 2023 H2 and 2024.

Following the analysis of the June quarter report, particularly taking account of the stickiness of services inflation, we see some moderation in the pace of inflation in the second half of 2023 as goods inflation unwinds at a faster pace but the services story still holds inflation at an elevated pace in 2024 – our forecasts for both headline and trimmed mean inflation in that year remain unchanged at 3.2%yr and 3.3% respectively.

Other factors create inertia for inflation in 2023H2 and 2024.

This inertia in inflation, particularly in 2024, is due to the range of other factors that have become more apparent in recent months and the market appears to be overlooking. These include:

- The continued strength of labour markets – we have recently upgraded our forecasts for employment growth and lowered our unemployment rate forecasts, to reflect the consistent upside surprises on jobs and the persistence of 50-year lows in the unemployment rate. The strength reflects the extraordinary backlog of unfilled jobs with job vacancies remaining at extreme highs. This is another direct legacy from the pandemic – and an issue being faced by many developed economies coming out of COVID. This resilience in labour market outcomes boosts incomes and demand adding to pressure on wages growth.

- Slow productivity growth – the 'productivity challenge' has been at the top of the Board's considerations consistently in the meeting minutes. This was most clearly identified in the minutes to the meeting in May, which noted: "Members observed that the forecast for inflation to return to the top of the target band by mid-2025 was predicated on productivity growth returning to around the modest pace recorded prior to the pandemic. If this did not occur, growth in unit labour costs would be uncomfortably fast." The latest update on unit labour costs – wages adjusted for productivity – saw annual growth lift 7.0%yr to a very strong 7.9%yr in the March quarter.

- A resurgent housing market – nationally house prices have lifted by around 5% since February, and the Westpac-MI House Price Expectations Index shows consumers expect gains to continue over the next year, which will anchor and support current momentum. Activity, inflation and wealth effects resulting from the improving housing market will tend to make it more difficult for the RBA to achieve its inflation target. The May Board meeting minutes picked up on some of these concerns: "Members also reviewed recent developments in asset markets – in particular, they noted the depreciation of the exchange rate and the increase in house prices … the decision to hold rates steady in April was likely to have contributed".

- Emerging risks around commodities – oil prices are lifting and electricity costs already look like being a persistent source of high inflation; global food prices are being impacted by Russia's blockade of Ukraine's agricultural exports and are at risk of more weather-related impacts as an El Nino forms.

The RBA's forecasts of reaching the top of the band by mid-2025 already envisage a very significant fall in inflation through the remainder of 2023. Underlying inflation is forecast to fall from 6% in June to 4% in December. That entails a slowdown in semi-annual inflation from 2.2% in 2023 H1 to 1.8% in 2023 H2 – we think that is achievable but expect progress in 2024 to be much slower as goods disinflation runs its course, and the emphasis moves to more persistent services inflation.

Conclusion

Markets are convinced that the slowdown in inflation apparent in the June quarter inflation report will see an extension of the Board's July pause.

The headline inflation picture has been the key driver of recent decisions in both June and July. But that was not the case in May when the detailed quarterly report allowed for deeper and more reliable insights that were more concerning.

This time around, the June quarter report highlights the stickiness of services inflation while other information around the labour market and productivity pose questions about whether the staff can credibly lower the inflation profile to allow for an earlier achievement of the inflation target. Most importantly it needs to reach the mid-point of the target range by the extended forecast end-point of December 2025.

If, as we consider likely, the RBA's revised forecasts show little progress in this regard then the Board should take out more 'insurance' with an additional 25bp rate hike at its August meeting.

A combination of one last hike in August complemented with the ongoing 'soft' tightening bias seems to be the best approach to a difficult challenge.

Bill Evans, Chief Economist (WestpacGroup)

THE WEEK THAT WAS

The Australian Q2 CPI report provided a constructive update on inflation, highlighting a broad-based moderation in the pace of price increases across the consumption basket. The main results were a 0.8% (6.0%yr) lift in headline inflation and a 0.9% (5.9%yr) rise in trimmed mean inflation, both of which were below the market's expectation and our own. Highlighting the extent of the underlying moderation, the six-month annualised pace of core inflation has fallen from 6.0%yr to 4.3%yr, driven not only by a slowing in goods inflation but also services, including household services such as childcare as well as medical and hospital services. This is a welcome development for the RBA, with the easing in both headline and underlying inflation now running ahead of their forecasts from May.

In light of this update, as discussed by Chief Economist Bill Evans, we have lowered our forecast for the peak in the cash rate from 4.60% to 4.35%. That said, the persistence of services inflation and historically-tight labour market still present clear upside risks to the inflation outlook, concerns which Governor Lowe has consistently emphasised in recent months. In our view, this warrants additional insurance to be taken in the form of one further 25bp rate hike next week. A tightening bias is also likely to remain in place in coming months as the Board continue to assess the pace and breadth of disinflation across the services sector as well as the labour market's strength.

Concluding the week in Australia, nominal retail sales came in much weaker than expected, the broadly-based 0.8% decline in June having left quarterly nominal sales up only 0.4%. After accounting for the effect of inflation, we estimate that Q2's real retail sales volumes posted a contraction similar in size to that of Q1, in the order of –0.6%. The ABS' official estimate is due to be released on August 3.

Offshore, the US FOMC and European Central Bank (ECB) both raised their policy rates by 25bps at their July meeting as expected. In the press conference, FOMC Chair Powell made clear that the Committee will be closely scrutinising the strength and capacity of the economy in the months ahead, with subsequent decisions 'data dependent'. Notably, between the July and September meetings, two CPI reports and two employment reports are due, giving the Committee clarity on whether June's below-expectations CPI is a sign of the emergence of broad-based and sustainable disinflation or just a one-off reading. The former requires a further deceleration in employment and spending into 2024, and for inflation expectations to remain well anchored.

While the Q2 advanced GDP estimate came in at an above-trend 0.6%qtr, 2.6%yr annualised, the component detail was consistent with a disinflationary outlook. Services consumption slowed to a near-trend pace and growth in goods consumption was negligible in the quarter. Business investment meanwhile surprised to the upside as equipment spending surged following a protracted period of weakness and non-residential construction continued to grow strongly. Note the investment outcomes are not a concern for inflation on their own; to the contrary, greater capacity and efficiency will aid the fight against inflation. Housing investment remains a source of concern though, with activity continuing to contract at a time when additional supply is necessary. Also worthy of note is that both the consumer and aggregate GDP deflator came in below expectations, the GDP deflator noticeably so. This result may be the result of dissipating supply frictions, but it could also be statistical – a point to watch as revisions are received.

Looking ahead, the latter part of Q2 experienced a loss of momentum and further tightening in credit conditions, pointing to a materially weaker pace of growth through the second half and into 2024. Constructively though, Chair Powell's forward guidance on 2024 and beyond went as far as to envision a need to 'stop raising long before you got to 2% inflation and… start cutting before you got to 2% inflation too'. He also went on to signal an eventual return to neutral or expansionary monetary policy. We view these comments as broadly in line with our current forecasts for a first rate cut in March 2024 and significant easing thereafter through 2024 and 2025 to a fed funds rate of 2.625%. You can read our full analysis on the FOMC's decision and US outlook here.

Mirroring the US FOMC's decision, the ECB also raised their three policy rates by 25bps as widely expected, though the statement carried a more doveish tone. President Christine Lagarde signalled that little forward guidance would be given from here, with future rate hikes data-dependent. Lagarde expanded upon the change of verb describing the path of interest rates from 'the key ECB interest rates will be brought to levels sufficiently restrictive to achieve a timely return of inflation' to 'set to'. She explained this change of verb was deliberate and the two inflation readings alongside indicators of policy transmission would guide the decision in September. Additionally, the ECB announced it would cease remuneration for minimum reserves to make monetary policy transmission more 'efficient'.

The ECB's projections suggest inflation is expected to average 5.4% in 2023, while growth thus far would put inflation at 4.9%yr in 2023. In addition to a weaker inflation print, the second quarter Bank Lending Survey released this week, showed that credit standards had tightened for enterprises and house purchases. Demand for credit has also fallen further for enterprises, though the net percentage of banks reporting an increase in home loan demand had become less negative. The latter was a result of less pessimistic housing market prospects.

Should data continue to come in mild, further rate hikes may not be needed. However, much like the RBA, a tight labour market and momentum in services inflation could justify the ECB take additional precautions in coming months.

The Bank of Japan amended its yield curve control framework effectively extending the 10-year government bond yield corridor from +/-50bp around the 0% target to 100bps. The came as inflation expectations rose alongside firms' wage and price setting behaviour. Forecasts for inflation were revised up marginally however the BoJ stuck to its dovish stance saying "…sustainable and stable achievement of the price stability target of 2 percent, accompanied by wage increases, has not yet come in sight, and thus the Bank needs to patiently continue with monetary easing…"

Week ahead & data wrap

New Zealand labour market pressures easing, but only gradually

A projected loosening of the labour market forms the lynchpin of the RBNZ's forecast that inflation will return to the target range next year. However, we expect the coming week's key labour market data will point to very little easing in the June quarter, with wage growth likely to have remained at elevated levels. In our view, the risk of further OCR hikes will remain until more concrete signs of easing labour market pressures emerge.

The RBNZ's current forecast that inflation will return to the target range next year is heavily conditioned on a projected loosening of the labour market. Therefore, the most important entry in next week's local economic diary is the release of key labour market data for the June quarter. With last week's CPI report pointing to stronger than expected inflation pressures in the non-tradables sector, the RBNZ will surely be keener than ever to see clear signs of a major turning point in the jobs market. However, we expect next week's data to reveal only a modest lift in the unemployment rate, which will remain at an historically low level.

Despite a slowdown in general economic activity, employment growth is likely to have remained robust. The monthly employment indicator – which despite conceptual differences broadly tracks the household measure of employment – pointed to a 1.0% lift in filled jobs in the June quarter. Allowing for the possibility that some people might have taken second jobs in response to increasing pressures on household finances, we estimate a 0.8% lift in household employment. We think the current strength owes in large part to the substantial inflow of migrant arrivals since late last year, which has allowed some employers to fill long-standing vacancies. Employers in the hospitality and transport sectors are likely to have added to their workforces, irrespective of weakening demand conditions in the economy.

Importantly, the surge in migrant arrivals has also lifted the pool of potential labour. Indeed, the working age population increased by a strong 0.7% in the June quarter. With growth in the previous quarter recently revised up to 0.8% – double that estimated previously – annual growth seems set to rise to a new high of 2.2%. The labour force participation rate increased by 0.3% to a new record high of 72.0% in the March quarter (perhaps also due to migrants' labour force participation exceeding that of the general population). After such a large increase last quarter, we are hesitant to assume a further increase in the June quarter. As a result, we estimate that the unemployment rate will edge up by 0.1ppts to 3.5%, continuing the very slight uptrend evident since early last year.

Turning to wages, we expect that the overall Labour Cost Index (LCI) will increase 1.3% in the June quarter, stepping up from 0.9% in the March quarter, and lifting annual growth to a new cyclical high of 4.5%. Contributing to this lift in growth is the Government's decision to lift the minimum wage by 7% from 1 April, with official estimates indicating that this increase will have lifted the wages of about 7.5% of the workforce as pay rates are brought up to the new floor. However, for the most part the solid lift in the LCI will reflect the lagged impact of past tightness in the labour market. Significant declines in wage growth are more likely to be a story for 2024, rather than this year. It is worth noting that the unadjusted Labour Cost Index – which more closely represents workers' take-home pay – is likely to have grown by around 6% in the year to June.

If the labour market data pan out as we expect they will likely have little impact on the RBNZ's policy outlook. We expect employment growth to be slightly stronger than forecast by the RBNZ back in May – reflecting migrant inflows – but our estimate of the unemployment rate is in line with the RBNZ's forecast. Our forecast for the increase in the private sector LCI is a notch above the RBNZ's May forecast, which might attract some focus should the unemployment rate surprise on the downside. Looking ahead, in order to remain comfortable with the present OCR setting, we think the Bank will need to see much greater progress in reducing labour market tightness in the second half of this year.

Turning to the rest of the diary, Monday will bring an update on business confidence and building consents. Last month, the ANZ Business Outlook Survey reported a further lift in firms' expectations of activity – indeed the first net positive reading in 14 months – and a modest decline in firms' expectations of inflation, which nonetheless remained very elevated. As far as dwelling consents are concerned, despite a strong lift in population growth, we think that the bottom of the cycle is yet to be seen and so the June report may reveal a third consecutive monthly decline. Finally, we will also be interested in the results of Wednesday's GDT dairy auction. Indeed, in light of the declines seen in recent auctions – which we attribute to soft demand from China – this week we revised down our forecast of the 2023/24 season return for dairy farmers to $7.80kg from $8.90kg. For many farmers, this would put the milk price below their break-even point. That said, farm balance sheets are generally strong and given previous experiences of downturns, we expect that farmers are well-placed to manage through this milk price cycle.

Darren Gibbs, Senior Economist

Round-up of local data released over the last week

Date	Release	Previous	Actual	Westpac f/c
Mon 24	Jun trade balance $m	52	9	–450
Fri 28	Jul ANZ consumer confidence	85.5	83.7	–
	Jun employment indicator	0.0%	0.4%	0.4%

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.

Aus Jun private sector credit

Jul 31, Last: 0.4%, WBC f/c: 0.4%
Mkt f/c: 0.4%, Range: 0.3% to 0.6%

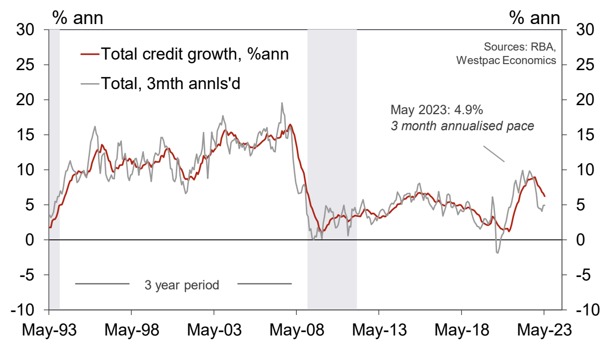
Over the first half of 2023, the monthly pace of credit growth broadly stabilised at a subdued average of 0.4% – against the backdrop of an emerging stabilisation in the housing market and late cycle resilience in business investment.

Prior to that, the appetite for credit diminished significantly as sharply higher interest rates impacted, reducing borrowing capacity. Monthly credit growth was running at an average pace of 0.7% over the second half of 2021 and through January to September 2022.

The May 2023 credit figure printed a rise of 0.4%, 6.2%yr, including: housing 0.3%, 5.0%yr and business 0.5%, 9.7%yr. In three month annualised terms, credit growth is 4.9%, including housing 4.2%, business 7.5% and personal 0.1%.

For June, we anticipate a reading of 0.4%, which would see annual credit growth moderate to 5.8%.

Credit: growth pulse at a modest 4.9%



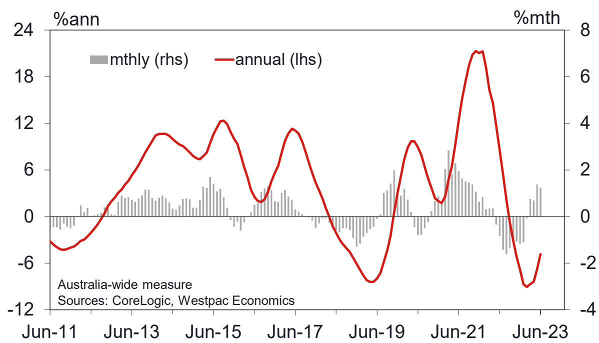
Aus Jul CoreLogic home value index

Aug 1, Last: 1.2%, WBC f/c: 0.9%

The CoreLogic home value index rose 1.2% in June, following a 1.4%mth gain in May, and 0.7-0.8% gains in April and March. The cumulative 4.1% lift since Feb comes after a 9.7% decline over the previous ten months. All major capital city markets recorded gains in June, albeit with most seeing the pace slowing a touch compared to May.

The CoreLogic daily index shows prices continued to rise in July but with a further moderation, the major capital city index tracking a 0.9% gain for the full month. The main slowing has been in Sydney after particularly strong 1.8%mth gains in May and June.

Australian dwelling prices



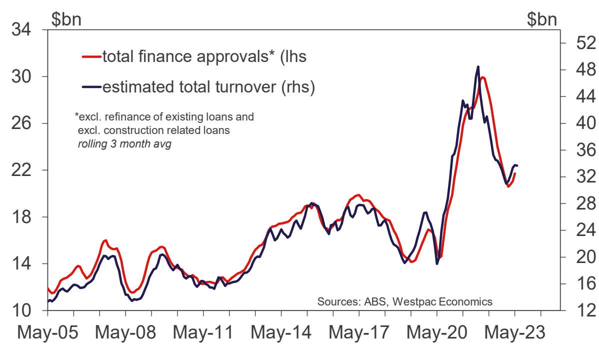
Aus Jun housing finance approvals

Aug 1, Last: 4.8%, WBC f/c: 1.5%
Mkt f/c: 1.8%, Range: –1.5% to +3.0%

Housing finance approvals posted a solid 4.8% rise in May extending on the gains seen since the low in Feb, the profile is consistent with the price-led recovery in established markets and, more recently, an up-tick in new construction, albeit with all housing metrics coming from weak starting points.

June is likely to see the upturn consolidate. In established markets, nominal turnover is tracking higher at about 2%mth – led by price gains with volumes about flat. Construction-related activity also looks to be seeing a gradual firming. Overall, we expect the total value of loans to be up 1.5%mth with investor lending likely a touch firmer than owner occupier lending.

New finance approvals vs value of sales



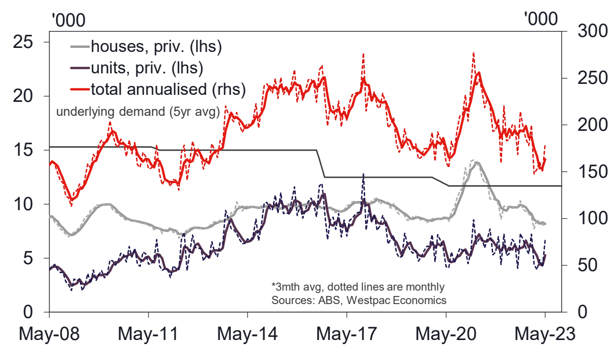
Aus Jun dwelling approvals

Aug 1, Last: 20.6%, WBC f/c: –7.0%
Mkt f/c: –8.0%, Range: –15.0% to flat

Dwelling approvals jumped 20.6% in May driven by a big spike in apartment developments in NSW (+150%). Excluding this, 'residual' dwelling approvals were up about 5%mth – reversing about a third of the steep fall seen through March and April – a much more subdued underlying picture pointing to, at best, a flattening at weak levels rather than a sustained upturn.

Non high-rise approvals look to be on a gentle up-trend – HIA new home sales firming despite a dip back in June. If high rise approvals re-trace to their March-April average and non high rise approvals rise 3%, we get a –7% fall overall.

Dwelling approvals



Aus RBA policy decision

Aug 1, Last: 4.10%, WBC f/c: 4.35%
Mkt f/c: 4.35%, Range: 4.10% to 4.35%

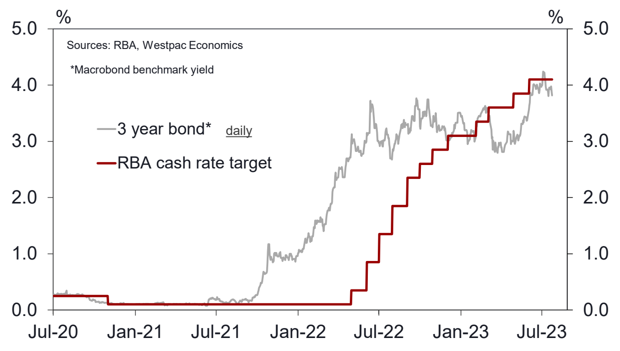
At the August Board meeting, Westpac anticipates that the RBA will raise the cash rate by 25bps to 4.35%.

The Q2 CPI provided a constructive update on headline inflation in Australia, down from 7.0%yr to 6.0%yr. However, the detail around services was not as promising. Not only did the overall services index lift from 6.1%yr to 6.3%yr, but the services index that excludes volatile items and government administered prices – which get knocked around by rebates/subsidies in health and childcare – rose by 1.2% in June (up from 0.9% in March), holding at 6.8%yr.

Given the lasting stickiness in services inflation, the RBA should take out more 'insurance' with a 25bp increase in August, reaching a terminal rate of 4.35%. Thereafter, the Board can retain a tightening bias while assessing inflation's downtrend and the evolution of risks.

For more detail, see Page 2.

RBA cash rate and 3 year bonds



Aus Q2 real retail sales

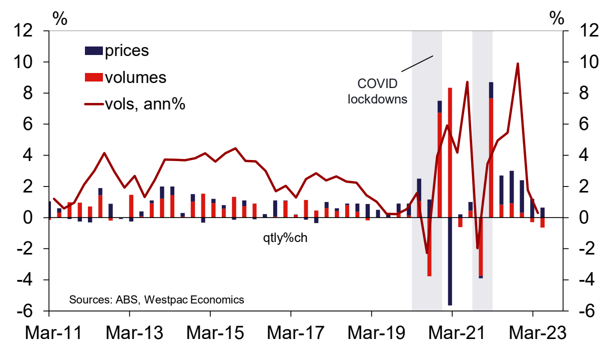
Aug 3, Last: –0.6%, WBC f/c: –0.6%
Mkt f/c: –0.5%, Range: –0.7% to +0.5%

Real retail sales fell 0.6% in Q1 following on from a 0.3% decline in Q4. The back-to-back falls marked the biggest six-month contraction in retail sales volumes since 1986 (excluding the COVID and GST introduction periods).

Preliminary estimates show nominal sales rose 0.4% in Q2 after having stalled flat in Q1. However the Q2 CPI detail suggests retail prices posted an even stronger gain, food prices alone up 1.5%qtr and total retail prices likely to be up around 1%qtr.

That in turn implies 0.6%qtr contraction in real retail sales – a third successive quarterly decline in volumes that has only been seen one other time historically: when interest rates peaked just prior to the GFC.

Quarterly retail volumes and prices



DATA PREVIEWS

Aus Jun trade balance, $bn

Aug 3, Last: 11.8, WBC f/c: 10.4
Mkt f/c: 10.8, Range: 10.0 to 13.0

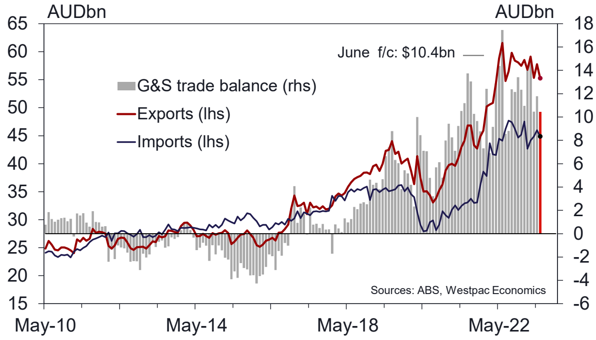
Australia's trade surplus hit $14.97bn in March, the second highest on record. Since then, with commodity prices pulling back by almost 12% in two months, the surplus moderated to be at a still elevated $11.8bn in May.

For June, we anticipated a surplus of $10.4bn, lower by $1.4bn.

Export earnings are expected to decline by 4.3%, –$2.5bn. The pullback in commodity prices continued, down 1.3% in June. Goods volumes, after a strong one-off showing in May, likely corrected lower, with potential falls across LNG and gold, as well as manufactured goods. Services recovery continues.

On the import side, we have limited partials. On this occasion, we are going out on a limb and factoring in a sizeable decline of 2.4%, –$1.1bn. Global fuel prices fell again, -5.9%, and auto imports spiked in May, +$0.9bn, with the potential for a June correction. The AUD rose 0.9% against the USD in June, thereby dampening prices.

Australia's trade balance



NZ Jul ANZBO business confidence

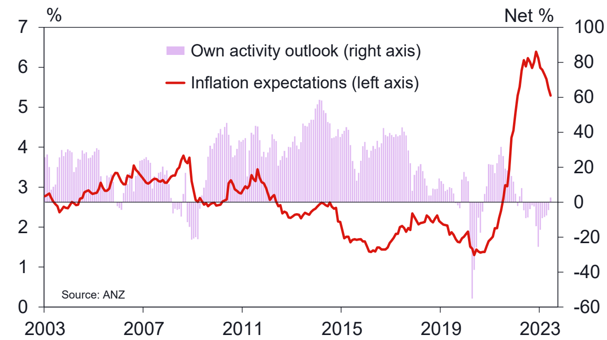
Jul 31, Last: –18.0

While businesses remain downbeat about the economic landscape, the June confidence survey showed that some of that nervousness has been dissipating.

We expect that the July confidence survey will again highlight that, although business sentiment remains weak, some of the malaise is dissipating. On the downside, many businesses are struggling with challenging trading conditions as they and their clients grapple with higher borrowing costs and other headwinds. But at the same time, recent months have seen cost pressures moderating, while the recovery in net migration is helping to alleviate labour shortages and is adding to demand.

The survey's cost and pricing gauges will be closely watched. While those continue to point to strong inflation pressures, they have been trending down for several months now. We expect that trend will continue in this month's survey.

NZ business confidence



NZ Jul building consents

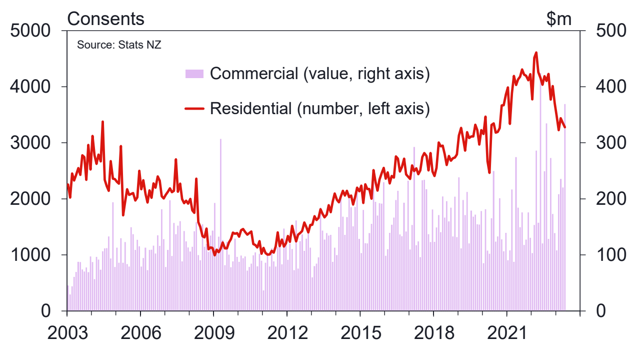
Aug 1, Last: –2.2%, Westpac f/c: –5.0%

The number of new dwelling consents fell 2.6% in May, with annual consent issuance dropping back to 45,200. While that is still high compared to history, it's down 11% from the peak we saw in 2022.

We expect consents issuance will fall by a further 5% in June with tighter financial conditions (including higher interest rates) continuing to dampen new housing development.

The housing market is now finding a base, with house sales and prices starting to turn upwards. Even so, we still expect consent issuance and building activity to continue softening for some time yet.

NZ building consents



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DATA PREVIEWS

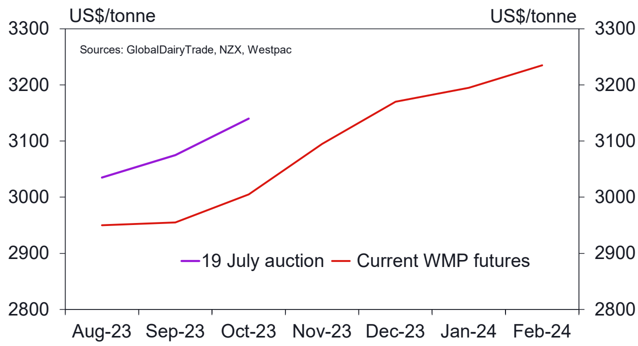
NZ GlobalDairyTrade auction, whole milk powder prices

Aug 2, Last: –1.5%, Westpac: –2.0%

We expect whole milk powder prices (WMP) to fall 2% at the upcoming auction. If prices fall as expected, then this would continue the downward trend seen over the past year. Our pick is between the circa 1% fall at last week's mini (GDT pulse) auction and the fall of about 3% that the futures market is pointing to. We note that Fonterra has announced a reduction in auction volumes on offer and this has swayed us towards a slightly smaller price decrease.

In the short term, we expect that underwhelming Chinese dairy demand and recent New Zealand production strength will continue to put downward pressure on prices. By late 2023 and early 2024, we expect that soft underlying global dairy production and improving Chinese dairy demand will lift dairy prices.

Whole milk powder prices



NZ Q2 labour market surveys

Aug 2, Unemployment rate, Last: 3.4%, Westpac f/c: 3.5%
Aug 2, Labour Cost Index, Last: 0.9%, Westpac f/c: 1.3%

Indicators suggest a solid 0.8% lift in employment in the June quarter with surging migrant arrivals allowing employers to fill long-standing vacancies. However, with those arrivals also boosting the labour force, we expect the unemployment rate to edge up to 3.5%, continuing a very gradual uptrend from last year's historic low.

Wage growth typically lags the broader economic cycle. And with a 7% increase in the minimum wage on 1 April also in the mix, we expect the Labour Cost Index to increase a strong 1.3%. This will lift annual growth to a new high of 4.5% - likely the peak for this cycle.

Our forecasts are not materially different to the RBNZ's. So if the data meet our expectations, they are unlikely to have much impact on the Bank's outlook for the economy and monetary policy.

NZ labour market indicators

US Jul employment report

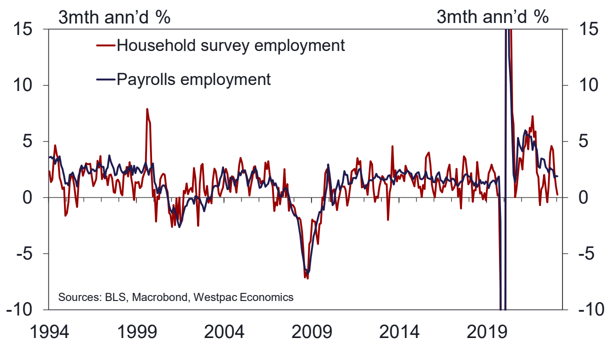
Aug 4: nonfarm payrolls Last: 209k, Mkt f/c: 190k, WBC: 210k
Aug 4: unemployment rate Last: 3.6%, Mkt f/c: 3.6%, WBC: 3.6%

The US labour market continues to show resilience, employment growth having slowed from a well above-trend pace to a rate consistent with a broadly stable unemployment rate given rising participation. This is despite a decline in manufacturing activity, persistent weakness in construction and sub-par consumption growth.

Employment growth is likely to slow further, though the upside surprise to activity through Q2 suggests the next leg down will appear towards the end of Q3. Even at that point, we only anticipate a sub-par pace of employment not meaningful declines.

With the supply of labour sufficient to meet demand, wages growth is due to ease further, albeit only slowly.

US job growth to slow further into year end



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For the week ahead

		Last	Market median	Westpac forecast	Risk/Comment
Mon 31					
Aus	Jun private sector credit	0.4%	0.4%	0.4%	Growth stabilised at a modest pace, as housing market stirs.
	Jul MI inflation gauge %yr	5.7%	–	–	Provides a general view of risks.
NZ	Jul ANZ business confidence	–18	–	–	Still weak, but has been rising.
Jpn	Jun industrial production	–2.2%	2.4%	–	Global slowdown to increasingly weigh on output growth.
Chn	Jul NBS manufacturing PMI	49.0	48.9	–	Greater resilience relative to developed nations…
	Jul NBS non-manufacturing PMI	53.2	53.0	–	… only marginally below pre-pandemic averages currently.
Eur	Q2 GDP	0.0%	–	–	Consumers feeling pressure from cost-of-living and rates.
	Jul CPI %yr	5.5%	–	–	Attention remains firmly centred on core/services trend.
UK	Jun net mortgage lending £bn	–0.1	–	–	High rates dissuade new borrowing for housing.
US	Jul Chicago PMI	41.5	43.5	–	Business conditions are exceedingly fragile…
	Jul Dallas Fed index	–23.2	–22.5	–	… particularly in the manufacturing sector.
Tue 01					
Aus	Jul CoreLogic home value index	1.2%	–	0.9%	Another solid gain, albeit with momentum slowing a touch.
	Jun dwelling approvals	20.6%	–8.0%	–7.0%	High rise spike unwinding, non-high rise firming slowly.
	Jun housing finance	4.8%	1.8%	1.5%	Upturn consolidating – established market seeing price-led…
	Jun owner occupier finance	4.0%	–	1.3%	… gains with volumes flat, new building firming gradually…
	Jun investor finance	6.2%	–	1.5%	… investor activity to outperform slightly.
	RBA policy decision	4.10%	4.35%	4.35%	Final 25bp hike to provide insurance against services inflation.
NZ	Jun building permits	–2.2%	–	–5.0%	Tighter financial conditions still a drag.
Jpn	Jun jobless rate	2.6%	2.6%	–	Labour market conditions remain conducive for wages g'th.
Chn	Jul Caixin manufacturing PMI	50.5	49.8	–	Robust investment detail offers medium-term support.
Eur	Jun unemployment rate	6.5%	–	–	Holding firm at a historically low level.
UK	Jul Nationwide house prices	0.1%	0.4%	–	High rates dissuade new borrowing for housing.
US	Jul ISM manufacturing	46.0	46.9	–	Demand risks a lasting slump below pre-pandemic levels.
	Jun JOLTS job openings	9824k	–	–	Only tracking a gradual softening.
	Jun construction spending	0.9%	0.6%	–	New capacity needed, but uncertainty a material headwind.
Global	Jul S&P Global manufacturing PMI	–	–	–	Final estimate for Japan, Eurozone, UK and US.
Wed 02					
NZ	GlobalDairyTrade auction (WMP)	–1.5%	–	–2.0%	Weaker prices to reflect still sluggish Chinese demand.
	Q2 unemployment rate	3.4%	–	3.5%	Very gradual uptrend continues, but still very low
	Q2 LCI wage inflation (pvte, ord. time)	0.9%	–	1.3%	Wages lag the cycle, so another solid lift is likely
	Q2 employment	0.8%	–	0.8%	Filled jobs indicator points to another robust quarter
US	Jul ADP employment change	497k	185k	–	Often at odds with BLS.
Thu 03					
Aus	Q2 real retail sales	–0.6%	–0.5%	–0.6%	Nominal sales +0.4%qtr, but prices +1%qtr -> vols –0.6%qtr.
	Jun trade balance $bn	11.8	10.8	10.4	Export decline (price & vol) to outpace that of imports; see textbox.
NZ	Jul ANZ commodity prices	–2.3%	–	–	All main commodity prices remain under downward pressure.
Chn	Jul Caixin services PMI	53.9	52.4	–	Cooling but still benefitting from post-reopening dynamics.
UK	BoE policy decision	5.00%	–	–	25/50bps a 50/50 proposition.
US	Jul ISM non-manufacturing	53.9	53.0	–	Near-term strength likely but outlook uncertain.
	Jun factory orders	0.3%	0.1%	–	Downside risks to demand present in core orders' weakness.
	Initial jobless claims	221k	–	–	Likely to remain at historic lows.
	Q2 productivity	–2.1%	1.2%	–	Wages growth robust at a time of weak productivity.
Global	Jul S&P Global services PMI	–	–	–	Final estimate for Japan, Eurozone, UK and US.
Fri 04					
Aus	RBA Statement on Monetary Policy	–	–	–	Forecast update – end-point extended from Jun-25 to Dec-25.
Chn	Q2 current account balance US$bn	81.5	–	–	Developed world demand to weigh on surplus in time.
Eur	Jun retail sales	0.0%	–	–	Discretionary spending capacity clearly under pressure.
US	Jul nonfarm payrolls	209k	190k	210k	The rise in participation and willingness of labour….
	Jul unemployment rate	3.6%	3.6%	3.6%	… to work 2+ jobs increasingly is providing adequate…
	Jul average hourly earnings %mth	0.4%	0.3%	0.3%	… supply, limiting wage gains and inflation pressures.

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Forecasts

Interest rate forecasts

Australia	Latest (28 Jul)	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24
Cash	4.10	4.35	4.35	4.35	4.10	3.85	3.60
90 Day BBSW	4.28	4.55	4.55	4.47	4.22	3.97	3.72
3 Year Swap	4.19	4.30	4.15	4.00	3.80	3.60	3.50
3 Year Bond	3.88	4.00	3.85	3.75	3.55	3.40	3.30
10 Year Bond	4.06	3.80	3.70	3.50	3.30	3.20	3.10
10 Year Spread to US (bps)	6	10	20	20	20	20	20
US							
Fed Funds	5.375	5.375	5.375	5.125	4.625	4.125	3.625
US 10 Year Bond	4.00	3.70	3.50	3.30	3.10	3.00	2.90
New Zealand							
Cash	5.50	5.75	5.75	5.75	5.75	5.25	4.75
90 day bill	5.67	5.85	5.85	5.85	5.55	5.05	4.75
2 year swap	5.48	5.30	5.00	4.70	4.40	4.20	4.00
10 Year Bond	4.73	4.60	4.40	4.20	4.00	3.90	3.80
10 Year spread to US	73	90	90	90	90	90	90

Exchange rate forecasts

Australia	Latest (28 Jul)	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24
AUD/USD	0.6665	0.69	0.69	0.71	0.72	0.73	0.74
NZD/USD	0.6177	0.62	0.62	0.63	0.64	0.65	0.66
USD/JPY	138.57	138	136	134	132	130	128
EUR/USD	1.0974	1.11	1.12	1.12	1.13	1.14	1.15
GBP/USD	1.2786	1.28	1.28	1.29	1.29	1.30	1.30
USD/CNY	7.1563	7.10	7.00	6.80	6.70	6.60	6.50
AUD/NZD	1.0815	1.11	1.11	1.13	1.13	1.12	1.12

Australian economic growth forecasts

	2022	2023				2024		Calendar years			
% change	**Q4**	**Q1**	**Q2f**	**Q3f**	**Q4f**	**Q1f**	**Q2f**	**2021**	**2022**	**2023f**	**2024f**
GDP % qtr	0.6	0.2	0.1	0.2	0.1	-0.2	0.2	–	–	–	–
%yr end	2.6	2.3	1.5	1.1	0.6	0.2	0.3	4.6	2.6	0.6	1.0
Unemployment rate %	3.5	3.6	3.6	3.7	4.0	4.2	4.8	4.7	3.5	4.0	5.3
Wages (WPI)	0.8	0.8	1.0	1.1	1.2	0.8	0.7	–	–	–	–
annual chg	3.4	3.7	3.8	3.8	4.1	4.1	3.8	2.3	3.4	4.1	3.3
CPI Headline	1.9	1.4	0.8	1.0	0.7	1.0	0.7	–	–	–	–
annual chg	7.8	7.0	6.0	5.2	4.0	3.6	3.5	3.5	7.8	4.0	3.2
Trimmed mean	1.7	1.3	0.9	0.8	0.8	1.0	0.9	–	–	–	–
annual chg	6.9	6.6	5.9	4.7	3.8	3.6	3.5	2.6	6.9	3.8	3.3

New Zealand economic growth forecasts

	2022	2023				2024		Calendar years			
% change	**Q4**	**Q1**	**Q2f**	**Q3f**	**Q4f**	**Q1f**	**Q2f**	**2021**	**2022**	**2023f**	**2024f**
GDP % qtr	-0.7	-0.1	0.5	0.5	0.1	0.0	0.0	–	–	–	–
Annual avg change	2.7	2.9	3.0	1.5	1.2	0.9	0.8	6.0	2.7	1.2	0.5
Unemployment rate %	3.4	3.4	3.5	3.7	3.9	4.2	4.5	3.2	3.4	3.9	4.9
CPI % qtr	1.4	1.2	1.1	2.0	0.5	0.6	0.6	–	–	–	–
Annual change	7.2	6.7	6.0	5.9	4.9	4.3	3.8	5.9	7.2	4.9	2.9

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