BULLETIN

21 May 2024

Consumer pessimism continues as inflation fears dominate

- **Westpac Consumer Sentiment Index dips 0.3% to 82.2.**
- **Expectations gradually improving but offset by renewed pressure on finances.**
- **Budget's cost-of-living support measures relatively well-received.**
- **Consumers more uneasy about inflation following Q1 upside surprise.**
- **Just over half expect rate rises to resume over the next 12 months.**
- **Those in line for stage 3 tax cuts plan to save 80¢ of every dollar.**
- **Job market confidence slips back to long run average levels.**
- **Housing sentiment remains stuck between extremely weak 'time to buy' assessments and strong price expectations.**

The Westpac Melbourne Institute Consumer Sentiment Index dipped 0.3% to 82.2 in May, from 82.4 in April.

Renewed cost-of-living pressures and inflation concerns have more than offset what looks to have been a relatively well-received Federal Budget. Consumer sentiment remains deeply pessimistic. While expectations improved a touch in May, this was overshadowed by a further deterioration in current conditions and fears that persistently high inflation may require further interest rate rises. Importantly, the sentiment level and mix, and responses to additional questions about July's tax cuts point to continued spending restraint by consumers heading into the second half of the year.

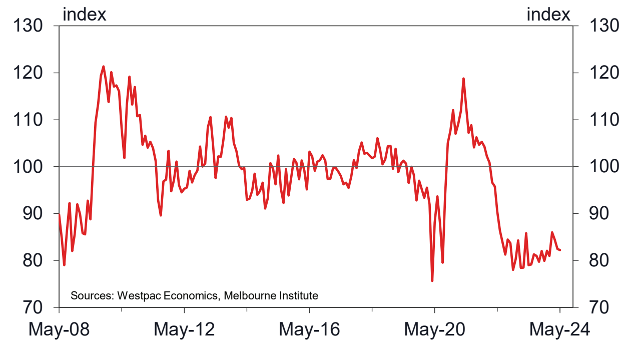
Sentiment-wise, the two big developments over the last month have been the higher-than-expected inflation outcome reported in late April, and the Federal Budget.

Our May survey was in the field during budget week, allowing for clear 'pre and post' Budget comparisons. The results suggest there was some disappointment, although a closer reading of the survey suggests this may have been more around the difficult economic context that the Budget highlighted than its content.

Sentiment amongst those surveyed pre-Budget showed an index read of 86.8, up a solid 5.3% compared to April. Sentiment amongst those surveyed after the announcement came in at 76.6, down 7% compared to April. That 11.8% deterioration compares to a 7.4% drop last year. Sentiment typically falls a few points between pre- and post-Budget samples. Some consumers may have had more unrealistic expectations going into Budget 2024 – especially around the scope to deliver cost-of-living relief without adding to the task of reining in high inflation (a theme that was also prominent last year).

Responses to an extra question on the impact of the Budget on family finances suggest fiscal measures were relatively well-received. Since 2010, our budget month surveys have asked consumers whether they expect their finances to improve

Consumer Sentiment Index



or worsen as a result of the Budget. We usually find a heavy negative bias to this question – those expecting to be worse off outnumbering those expecting to benefit by 20-25%. This year, the gap was just 3% with 18% of consumers expecting to be better off and 21% expecting to be worse off. With the exception of the big stimulus budgets of the COVID period, this is the least negative response we have seen in the last fourteen years.

The Budget also appears to have eased inflation and rate rise concerns rather than added to them. The Westpac-Melbourne Institute Mortgage Rate Expectations Index tracks consumer expectations for variable mortgage rates over the next 12 months. For the May survey as a whole, the index jumped 8.3% to 133 from 122.8 in April. However, most of that move occurred prior to the Budget, with those surveyed before showing a combined index read of 136.5, while those surveyed after had a combined index read of 128.5. This strongly implies that the source of renewed rate rise fears was the higher-than-expected March quarter inflation outcome and more 'vigilant' inflation-fighting rhetoric from the RBA Governor following the Board meeting in early May.

In terms of the component detail in May, consumers were slightly more positive about the outlook for both family finances and the economy, but this was completely offset by a deterioration in current assessments of family finances and buyer sentiment.

The 'finances compared to a year ago' sub-index dropped 3.6% to just 63.2 in May, taking it back to the low end of the very weak range that has prevailed since late 2022. The 'time to buy a major item' sub-index also declined, falling 2.8% to 76.5, an extremely weak level for this component which has been capturing the impact of sharply rising prices on consumers' purchasing power. Over its fifty-year history, there have only been about a dozen sub-80 reads on 'time to buy a major item' – ten of these have been in the last sixteen months.

The forward view on family finances continues to show the most promising gains. The 'finances, next 12mths' sub-index rose another 0.7% to 96.1 in May. It is now just a few points below the 'neutral' 100 level, having rallied 14.4% from last year's low. Tax cuts and cost-of-living support measures are providing a clear lift, with those on lower incomes reporting particularly strong gains in May (+13.8% amongst consumers with annual incomes of less than $60k).

This year's survey also included additional questions on the Stage 3 tax cuts. Just over 37% of consumers expect to pay less tax from July 1, 27% expect to see no impact, a relatively high 20% are unsure, with the remaining 15% reporting 'not applicable'. Of the respondents who expect to receive a tax cut, 30% plan to save all of it, while a further 50% expect to save at least half.

Overall, using responses across income groups and Treasury figures on the distribution of tax relief we estimate that households plan to save around 80% of the Stage 3 tax cuts. Similar questions run when fiscal payments were made during COVID and when LMITO payments were introduced in 2019 found consumers had saved or planned to save about half of those fiscal measures, while a similar question run during the GFC in 2009 found consumers only saved about 30% of fiscal payments at the time.

The results suggest consumers will use tax relief as an opportunity to repair their finances and rebuild saving buffers rather than spend. If they follow through on this plan, only $4.7b of the $23.3bn in tax relief will be spent, giving a spending boost of 0.35ppts. If they instead opted to save half, the boost would be closer to 0.9ppts.

Naturally, there is some uncertainty here. Plans change, and intentions to save may fall by the wayside once the boost to incomes appears. The mix of responses also suggests there is a sizeable group that are set for a positive tax cut 'surprise' – about 20% of consumers were not sure if they would receive cuts, and a relatively high proportion of middle-income earners (45%) and high-income earners (33%) did not expect to see any tax relief.

Despite inflation concerns, consumers were a little more positive on the economic outlook. The 'economy, next 12mths' sub-index lifted 0.7% to 83.2 and the 'economy, next 5yrs' sub-index posted a solid 2.6% gain to 92.2, reversing just over half of April's fall.

The state measures showed a notable divergence in May with sentiment posting a particularly strong 11% surge in Queensland (where the state government recently announced large cost-of-living support measures around energy bills) but notably weaker in New South Wales (down 9.8%). The latter likely reflects a higher sensitivity to inflation and interest rate risks.

Consumers remain relatively comfortable about the jobs outlook, although the outright confidence that was starting to emerge earlier this year has evaporated. The Westpac-Melbourne Institute Unemployment Expectations Index rose 4.1% to 129.8, slightly above the long run average of 129 (recall that higher index reads mean more consumers expect unemployment to rise over the year ahead). The May deterioration centred on New South Wales (+14.4%) and Victoria (+6.9%) with unemployment expectations improving 4-7% across the other major states.

Housing-related sentiment was broadly unchanged, with buyer sentiment slightly higher but still deeply pessimistic and price expectations continuing to hold at very positive levels.

The 'time to buy a dwelling' index rose 1.6% to 76.5 in May, reversing about half of April's dip but staying well below the 'neutral' level of 100 and a very long way from the historical average of 121. Meanwhile, the Westpac Melbourne Institute Index of House Price Expectations was again essentially unchanged at just over 161, well above the long run average of 126.5.

The Reserve Bank Board next meets on June 17-18. We expect it to again leave the official cash rate unchanged.

While it clearly remains vigilant on further upside surprises to inflation, the Board will draw some comfort from recent updates showing a gradual softening in the labour market and a slight moderation in wage growth. The March quarter national accounts, to be released on June 6, should also provide more comfort that softening demand is coming more into line with supply across the wider economy, and that domestic cost pressures will not prevent a return to low inflation.

The main takeaways from the May Consumer Sentiment survey are that there has been no let-up in the weak consumer environment; and that, given the weak starting point and a very cautious mindset, consumers are more likely to use funds from fiscal measures to repair their finances than go on a spending spree that could undermine the RBA's efforts to bring inflation back to target.

Matthew Hassan, Senior Economist, Westpac Group

Consumer Sentiment – May 2024

Item	avg*	May 2022	May 2023	Apr 2024	May 2024	%mth	%yr
Consumer Sentiment Index	**100.6**	**90.4**	**79.0**	**82.4**	**82.2**	**-0.3**	**4.1**
Family finances vs a year ago	88.3	79.6	63.0	65.5	63.2	-3.6	0.2
Family finances next 12mths	106.8	93.3	85.8	95.5	96.1	0.7	12.0
Economic conditions next 12mths	90.7	90.4	77.3	82.7	83.2	0.7	7.7
Economic conditions next 5yrs	92.0	96.2	87.2	89.8	92.2	2.6	5.7
Time to buy a major household item	124.5	92.6	81.7	78.7	76.5	-2.8	-6.5
Time to buy a dwelling	120.7	77.5	76.3	75.3	76.5	1.6	0.2
Unemployment Expectations Index	129.0	109.6	123.2	124.6	129.8	4.1	5.4
House Price Expectations Index	126.5	121.4	144.3	161.2	161.1	-0.1	11.7
Interest Rate Expectations Index	152.5	187.2	176.2	122.8	133.0	8.3	-24.5

Source: Westpac–Melbourne Institute.
*avg over full history of the survey, all indexes except 'time to buy a dwelling', 'unemployment expectations' and 'house price expectations' are seasonally adjusted

The survey is conducted by OZINFO & DYNATA. Respondents are selected at random. This latest survey is based on 1200 adults aged 18 years and over, across Australia. It was conducted in the week from 13 May to 16 May 2024. The data have been weighted to reflect Australia's population distribution.

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