October 2024

THE RED BOOK

Quarterly update on the Australian consumer

CONTENTS

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A promising improvement

The gloom that descended on Australian consumers two and a half years ago is finally starting to show more convincing signs of lifting.

Our October **Red Book** finds the consumer mood has become considerably less bleak, buoyed on the one hand by the additional cash in hand as tax cuts and other support measures flow through, and on the other by turning expectations for interest rates. The renewed rate rise fears that emerged a few months ago have subsided, consumer expectations for mortgage rates now back at levels seen when the RBA was actively easing rates in the past.

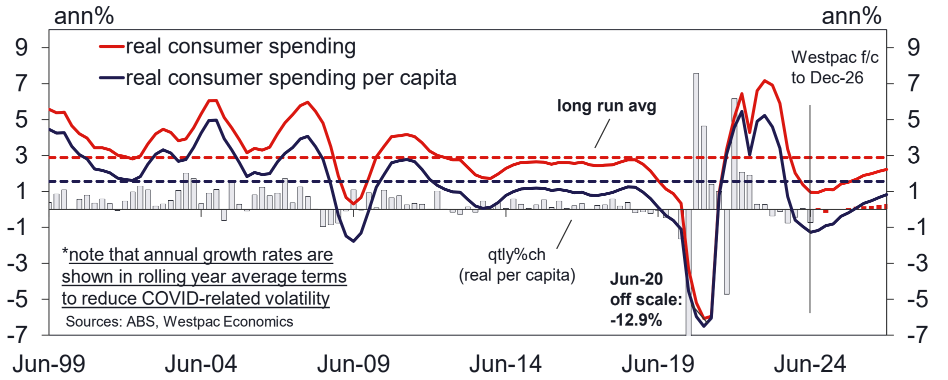
Looking ahead, the inflation and interest rate situation offers the best hopes for a further recover in sentiment. Westpac expects improving reads on inflation and the wider economy – particularly relating to productivity and the domestic cost pace – to soothe many of the RBA's current concerns. That should in turn allow for a shift in the Bank's messaging in coming months and an eventual move to begin lowering interest rates gradually in early 2025.

Each of these steps should provide additional comfort to consumers as well and, in turn, more support for sentiment.

That said, it may not be smooth sailing from here. There is still significant uncertainty around the path of inflation and other aspects of the economy. This includes some uncertainty around the consumer. While the picture from both sentiment and Westpac customer activity is that tax cuts have done little to boost demand, that may change. Add significant risks of political turbulence around elections in the US and locally and we may be in for a more unsettled period for sentiment.

More generally, the medium term recovery process looks likely to be a slow one. The RBA's easing cycle is expected to be gradual and modest. Household disposable incomes will be slow to recover the ground lost over the last 2½ years, with less support available from saving reserves accumulated during COVID and an additional headwind coming from slowing population growth. Despite some more promising signs, the consumer recovery still has a long way to go.

Consumer spending: low point has passed



"Despite some more promising signs, the consumer recovery still has a long way to go."

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Quick update

The **Westpac–Melbourne Institute Consumer Sentiment Index** rose 8.6% over the three months to October, to 89.8 from 82.7 in July.

While pessimism still dominates, the latest lift marks the most promising rise over the cycle to date. It reflects two main developments: 1) fiscal boosts that came into effect in July, the 'stage 3' tax cuts in particular; and 2) an improving inflation situation and an associated easing in rate rise fears.

Risk aversion remains very high but is off the extremes seen in 2023 and early 2024. The **Westpac Risk Aversion Index** held at 46 in September, little changed from the 48 in June but still well above the long run average of 18. Despite some small shifts, 'safe-haven' options continue to be heavily favoured as the 'wisest place for savings'.

The sentiment mix continues to point to declining per capita spend. **CSI±**, a modified indicator that correlates well with spending, remains at weak levels consistent with per capita spend contracting 3%yr. Actual spend has shown milder declines, partly due to support from savings reserves carried over from the pandemic.

The most striking sentiment shift over the last three months has again been around consumer expectations for interest rates. The **Westpac-Melbourne Institute Mortgage Rate Expectations Index** fell by a third between July and October, more than reversing the 23% surge over the previous three months. At 106.4, the Index is now at its lowest level since the RBA was actively easing policy during COVID and is on a par with the lows seen during previous periods of interest rate cuts over the last 14 years.

Consumers continue to gradually mark down their expectations for inflation and wage growth. Inflation expectations remain broadly consistent with headline inflation slowing to 2.5%.

Expectations for wages growth have ticked down to be in line with long run averages.

The **'time to buy a major item'** index posted a more muted lift than other component sub-indexes, rising just 3.6% over the last 3mths. At 85.1, the index is still in the bottom 5% of observations historically. This is despite a clear stabilisation in prices, suggesting buyer sentiment may be slow to improve.

Homebuyer sentiment continues to bump around historical lows. The **'time to buy a dwelling'** index rose 3% over the 3mths to October but at 78 remains deeply pessimistic. Buyer sentiment is much weaker in WA at just 61.4.

Consumer house price expectations are still positive but bullishness is starting to wane. The **Westpac–Melbourne Institute Consumer House Price Expectations Index** declined 4.9% over the 3mths to October but at 153.2 remains near cycle highs, about 20% above the long run average of 128. Expectations have seen a more pronounced softening in states where price growth has seen more of a slowdown, Vic in particular.

Consumers are still not overly-concerned about potential job loss, with a brief mini-flash of concern in recent months, dissipating in October. The **Westpac–Melbourne Institute Unemployment Expectations Index** is relatively unchanged compared to July. At 129.8 it remains in the 125-133 range that has prevailed since mid-2023 and close to the long run average of 129. The reading remains consistent with a flat labour market.

Hints of a turn

- Consumer sentiment has shown a clear improvement over the last 3mths. The **Westpac Melbourne Institute Index of Consumer Sentiment** has risen 8.6% since Jul, reaching 89.8 in Oct.

- This marks the most promising lift over the cycle to date. While pessimism still dominates, the latest Index read is the best we have seen since the RBA interest rate tightening phase began 2½ years ago. Sentiment is now about one standard deviation below its long run average.

- The gains reflect two main developments: 1) fiscal boosts that came into effect in July, the 'stage 3' tax cuts in particular; and 2) an improving inflation situation and an associated easing in rate rise fears.

- Component-wise, the biggest improvement has been in the sub-index tracking assessments of 'finances vs a year ago', which surged 16.2% over the 3mths to Oct. Tax cuts and 'cost of living' support measures from both state and federal governments have added over $30bn to annual household disposable income nationally (a boost of over 1.8%).

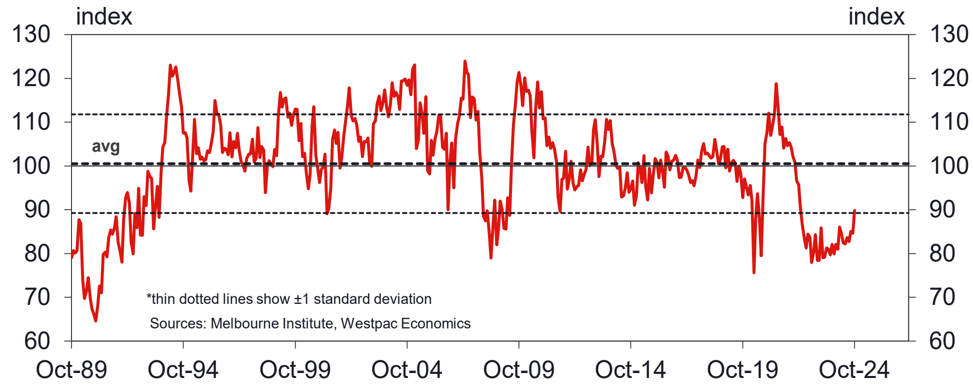
- The improved assessment of finances likely reflects other drivers as well, including: the stabilisation in official interest rates over the last year, up only 25bps compared to 150bp rise over the previous 12mths; lower fuel prices, average pump prices having declined over 20¢/litre since May; and rising dwelling prices which across the major capital cities are now up over 16% since the start of 2023.

- Across forward-looking components, the main driver appears to be reduced fears that persistent high inflation will lead to even higher interest rates.

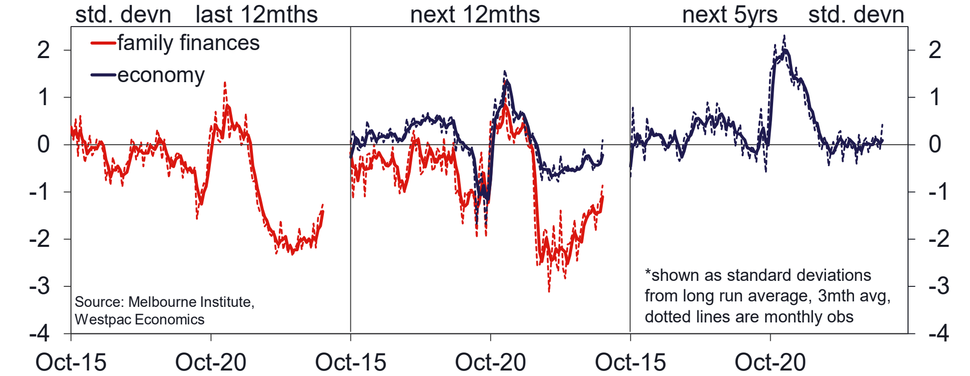
- While the RBA has maintained a 'vigilant' stance on inflation risks, it has continued to keep rates unchanged. Meanwhile, recent monthly CPI updates suggest the moderation in inflation that seemed to stall in the first half of the year has resumed.

- That easing in rate hike fears would have been supported by central banks moving rates lower abroad, especially the eye-catching 50bp cut by the US FOMC, and by a move lower in advertised fixed mortgage rates locally (3yr rates down over 50bps since Jun).

1. Consumer sentiment: long slump coming to an end?

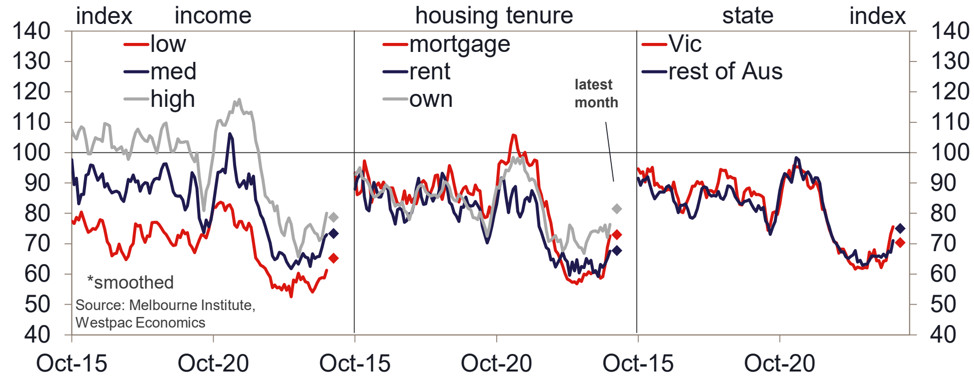


2. Consumer sentiment: finances, economic conditions

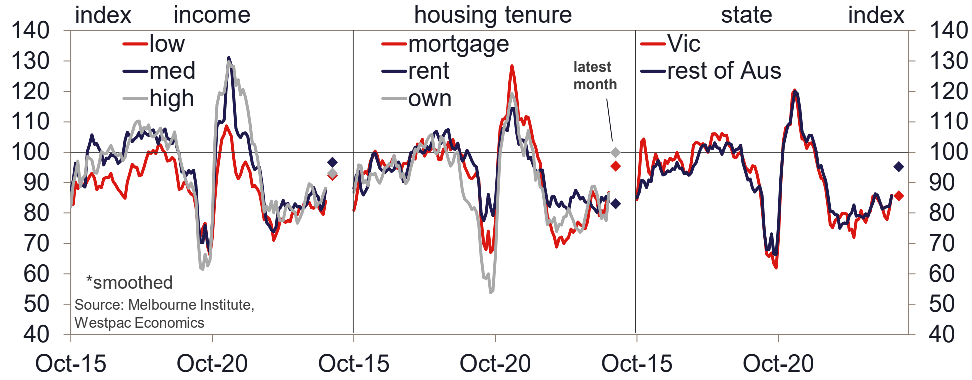


- These shifts are reflected in our measures of consumer inflation expectations (detailed on p16) and a particularly sharp fall in consumer interest rate expectations (detailed on p15). The themes were also evident in consumer assessments of news coverage in Sep (discussed on p9).
- The sub-group detail also provides evidence of the fiscal and monetary factors at play, plus a couple of notable sub-plots in the state and industry detail.
- Across the 100-odd sub-groups we track regularly, barely a dozen recorded sentiment declines over the 3mths to Oct. Charts 3 and 4 show how some of this sub-group detail looks for the 'finances vs a year ago' and 'economic outlook, next 12mths' sub-indexes that have seen the largest moves since Jul.
- Assessments of finances have improved across all income bands since Jul but with slightly bigger gains amongst middle-income earners and slightly smaller gains for those on low incomes. This is broadly consistent with the pattern of tax cuts, noting that many in the 'low income' band will be retirees ineligible for tax relief.
- By tenure, assessments of finances have shown a particularly sharp improvement amongst households with a mortgage, moving from consistently weaker reads over the last 18mths to being more in line with assessments nationally. Aside from the factors already mentioned, some of the rise may also be due the roll-offs from very low COVID-era fixed rates coming to an end.
- Not surprisingly, shifting expectations for rates have also done more to boost expectations for finances amongst consumers with a mortgage.
- It is a similar story for near term expectations for the economy, although here the absence of a lift amongst renter households has been a notable exception over the last few months. Similarly, Vic continues to be a significant underperformer with lacklustre expectations for the economy and jobs still a stand-out (we discussed Vic in more detail in our last report).
- Lastly, the industry breakdown also has some notable exceptions, sentiment failing to rise amongst those employed in the health, tech and manufacturing sectors, suggesting there are some sector-specific drags in play.

3. Family finances vs a year ago, selected sub-groups



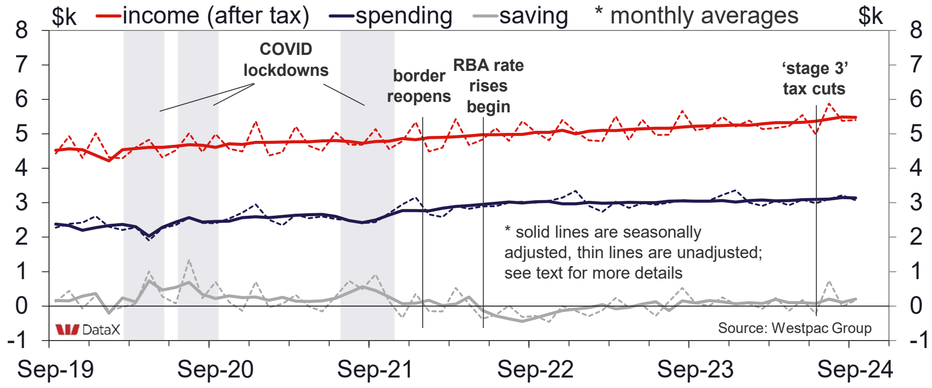
4. Economic outlook next 12mths, selected sub-groups



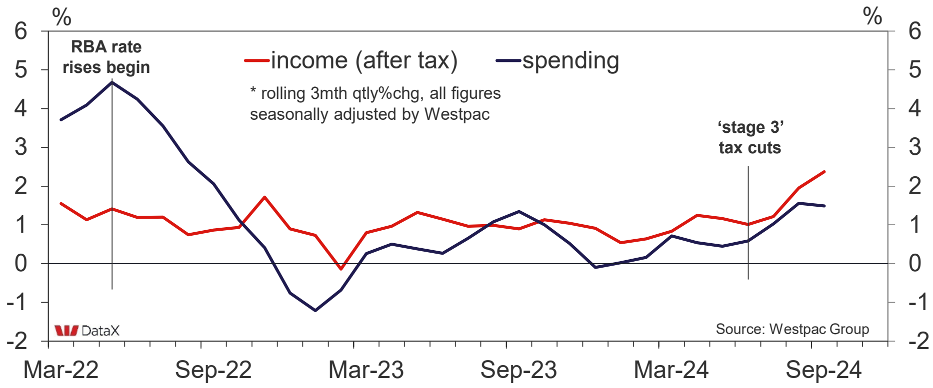
Westpac-DataX Consumer Panel

- The **Westpac-DataX Consumer Panel** provides a new source of detailed and timely information on the Australian consumer. This topic provides an overview of the Panel and a summary of what it is telling us about consumer trends and behaviour, particularly in relation to the 'stage 3' tax cuts that came into effect from July 1.
- Developed by DataX, Westpac's data analytics service for institutional and business banking customers, the Panel is a dataset that links transaction activity with balance sheet information to give a more complete view of income, spending, saving and borrowing flows. All information is de-identified and aggregated to ensure the privacy of our customers. To gain the most accurate picture of consumer activity, the panel is restricted to only include connection observations where we have the most visibility of income, spending, saving and borrowing activity. The resulting sample of over 1 million customers provides an accurate representation of trends across the wider Australian consumer. Monthly observations are available back to July 2019 with timely updates provided a few weeks after the end of each month.
- Chart 8 shows average income, spending and net saving flows with chart 9 showing quarterly growth in income and spending.
- It should be noted at the outset that there are significant definition and coverage differences between these panel measures and standard measures produced by the ABS. All Panel figures are customer averages and so exclude the effects of population growth and will be affected by compositional differences between the customer mix and the broader population. Moreover, income in the Panel is after tax income including government benefit payments but excludes net interest payments. 'Saving' is the net of transaction flows into deposit and offset accounts rather than the savings measure used in the ABS national accounts (i.e. income after tax, net interest payments, spending and depreciation of fixed assets). There are also a range of technical issues around payment frequencies and seasonal adjustment. All of which is to say that the Panel results should be viewed as an indicative guide to per capita flows and behaviour rather than a 'hard and fast' estimate of income, spending and savings.

8. Westpac-DataX Consumer Panel: income, spending, saving

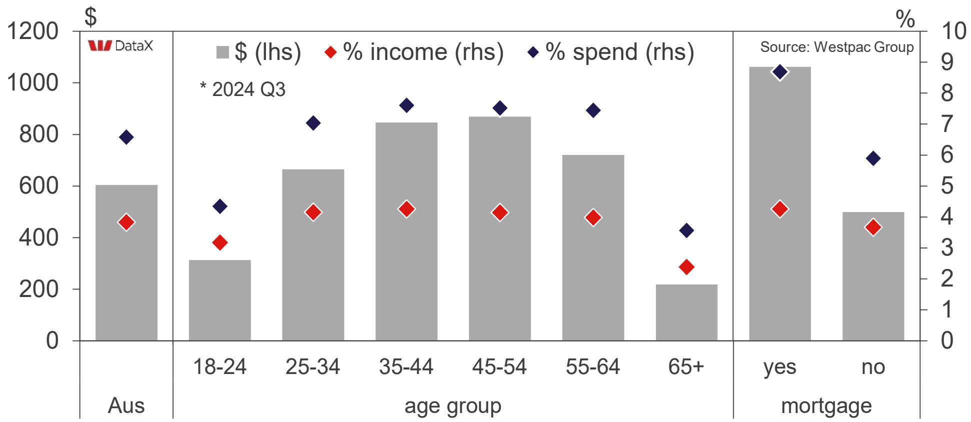


9. Westpac-DataX Consumer Panel: income, spending growth

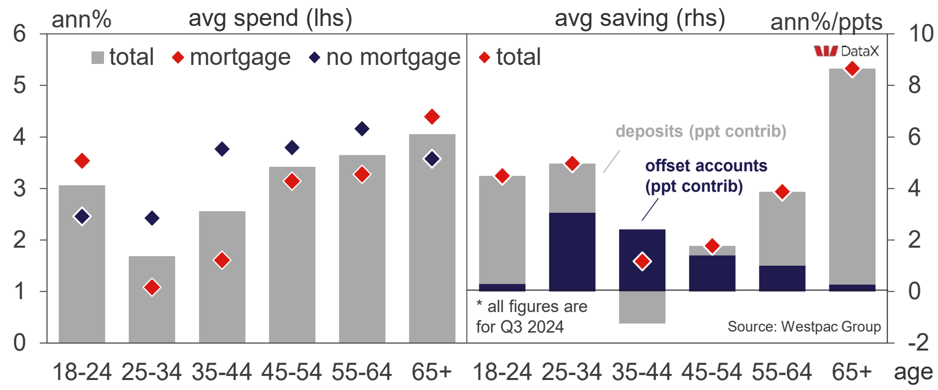


- So what can we glean from the Sep quarter results? Average income has shown a clear lift, rising an estimated 2.4%qtr in seasonally adjusted terms, the strongest quarterly gain since COVID. Average spending has shown a more muted 1.5%qtr rise in seasonally adjusted terms, albeit an improvement on the 0.5%qtr average over the previous six quarters. Meanwhile net saving inflows have shown a clear lift.
- The Panel is particularly well suited to tracing the impact of the stage 3 tax cuts. Chart 6 shows the estimated boost to incomes from tax cuts. The average boost of $604 accounted for around two thirds of the total increase in average income in the quarter. That was closer to $1k for consumers with a mortgage and over $1.8k for those in the top income quintile. Our estimates suggest the total boost to aggregate incomes was around $6.4bn.
- Putting this together, and allowing for some baseline trend growth in spending and incomes, consumers look to have only spent about 16% of the tax cut boost to date, i.e. a marginally propensity to consume (MPC) of just 0.16.
- While more may yet be spent, the boost to spending to date is low. Our last [Red Book](#) reported on responses to additional questions on the 'stage 3 tax cuts' that indicated consumers at the time were planning to spend just 20% of the income boost. That seemed low at the time with the experience of previous fiscal measures and the general 'rule of thumb' suggesting closer to half ends up being spent. However the Q3 flows suggest it has been even lower to date.
- The panel provides a range of cross-sectional information as well. Spending increased across all age cohorts but was a little firmer for those 18-44. Across income buckets, the largest increase was across the lowest income group although this is less likely to relate to tax cuts as this group tends to be dominated by retirees and those receiving government assistance. Among the other income groups, spending growth was slower for the second income band while the top three income bands experienced broadly similar growth.
- For a more detailed discussion, see our full report [here](#).

6. Estimated boost from 'stage 3' tax cuts: selected sub-groups



7. Spending and saving behaviour: by age group



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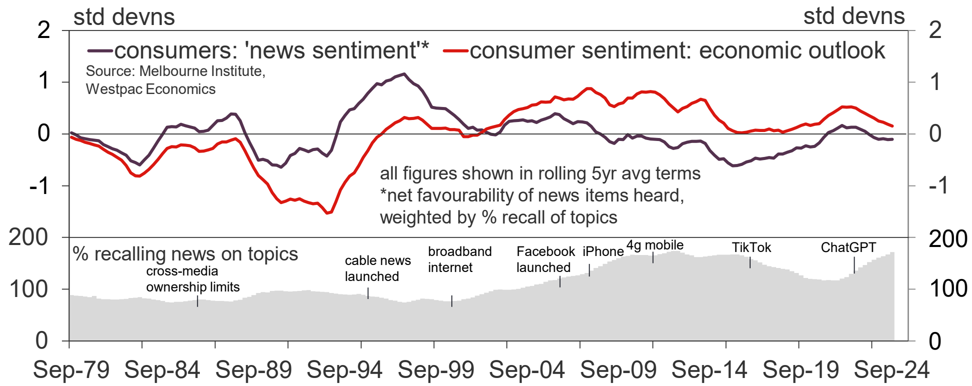
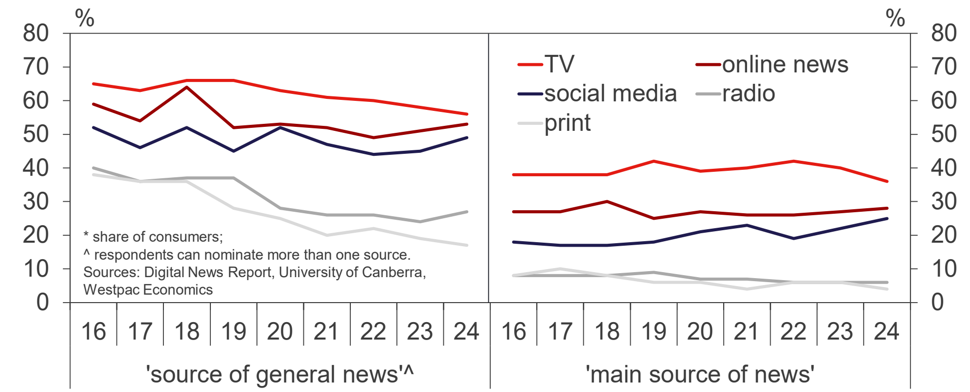
News sentiment

- In this special topic, we explore how consumer engagement with news has evolved over time and how it shapes expectations for the economy.
- Our Mar, Jun, Sep and Dec surveys include additional questions asking consumers which topics they recall hearing news about and whether that news was favourable or unfavourable. Chart 8 shows rolling 5yr average reads of the total recall of news across all topics and a 'news sentiment' measure capturing how favourable assessments were across all topics. This is plotted alongside consumer assessments of the 'economic outlook'.
- Overall, the data suggests consumers have become more engaged with news since the 1990s but have also tended to perceive news as more unfavourable, particularly when compared with actual expectations for the economy. This holds across almost all topics but is most evident in news related to economic conditions, interest rates and inflation. Note that GDP growth was slightly firmer during the 1990s than over the last 10yrs. That said, the earlier period was marked by a deep recession at the start of the decade.
- Some of the increased negativity around news may reflect changes in the way consumers engage with media. The launch of cable-TV in Australia in the mid-90s and the proliferation of internet-based and mobile services since then has transformed the media landscape over the last 45 years. News is now available 'on-demand' but faces a wider array of alternatives competing for consumer attention.
- The Digital News Report – a survey of how Australians engage with news conducted by the University of Canberra since 2015 as part of an international study – provides some fascinating insights. Over half of consumers now nominate online news or social media as their main source of news, up 8ppts on a decade ago with the rise led by 'social media'. Remarkably, this particular channel is now the main news source for over 60% of 18-26 year olds.
- Exactly how this may be affecting news engagement and sentiment is unclear. Different channels may ultimately lead to the same news items but will often lead to news feeds being filtered and framed very differently.

8. Consumer news recall and sentiment: long run trends

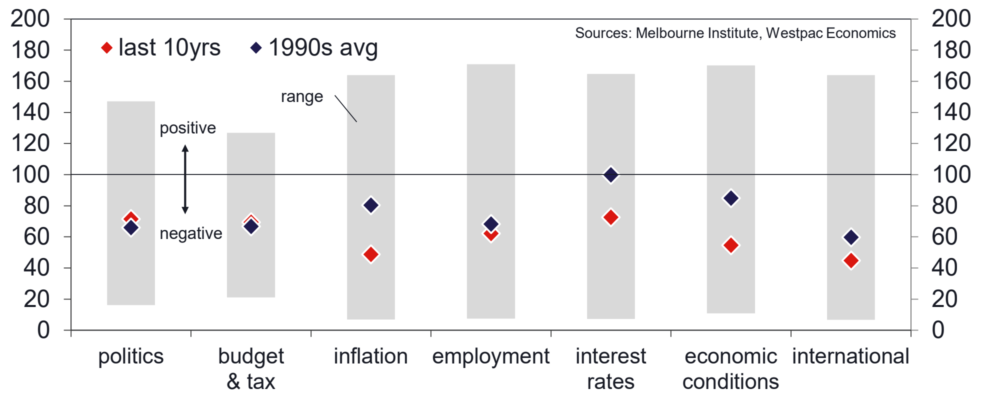


9. Consumers: sources of news

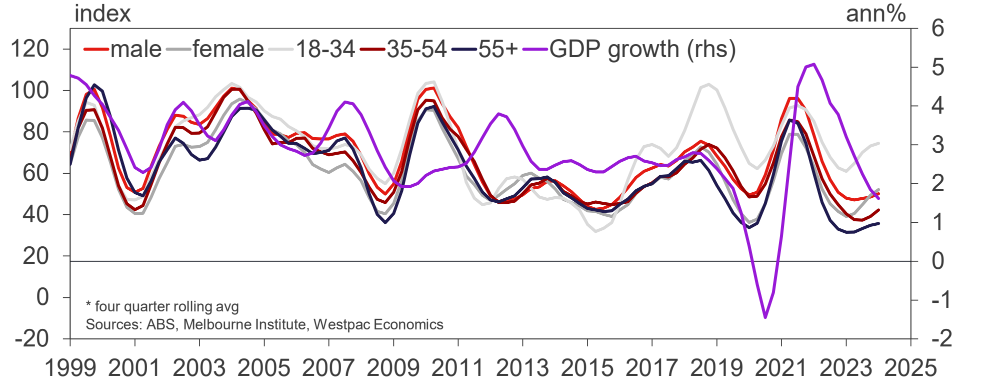


- Online forums, for example, can be a source of more diverse viewpoints but can also function as a narrow 'echo-chamber' that reinforces views.
- There is an interesting divergence in news assessments across age groups. All age groups have become more engaged with news compared to the 1990s. However, younger cohorts view news more favourably than both their late-1990s counterparts and older cohorts. This pattern holds for all topics except for interest rates and economic conditions. In contrast, older cohorts view news less favourably across all topics, especially inflation, economic condition and politics.
- Some of these differences will have 'real world' sources. For example, the high unemployment of the 1990s may have been a much bigger negative for younger age groups at the time. Different age groups will also have different frames of reference. A 7% unemployment rate would be considered a disaster for those that began their working lives since the turn of the century but not that bad for those that experienced the double-digit rates of the early-90s.
- Correlations with other sentiment components provide some additional insight. 'News sentiment' has a clear link with economic expectations but this breaks down somewhat during periods of higher engagement where the linkages become more topic specific. For example, unemployment expectations are closely linked to sentiment on employment news while interest rate expectations are closely linked to sentiment on inflation news. Inflation expectations are somewhat related to sentiment on inflation news but more closely linked to news about employment and economic conditions.
- Most significantly, consumers' 12mth economic outlook is highly correlated with news on economic and international conditions.
- Current sentiment on news related to economic conditions also has some correlation with future GDP growth (see Chart 11). This is true across all age and gender cohorts although there are some indications that males and those aged over 55 can detect shifts slightly earlier. This may be partly attributable to higher news engagement.

10. Consumer news sentiment: selected topics



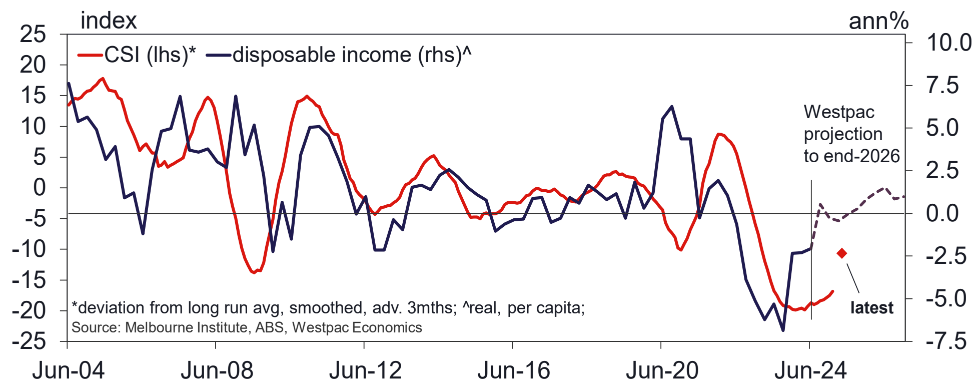
11. Consumer 'economic news sentiment': selected sub-groups



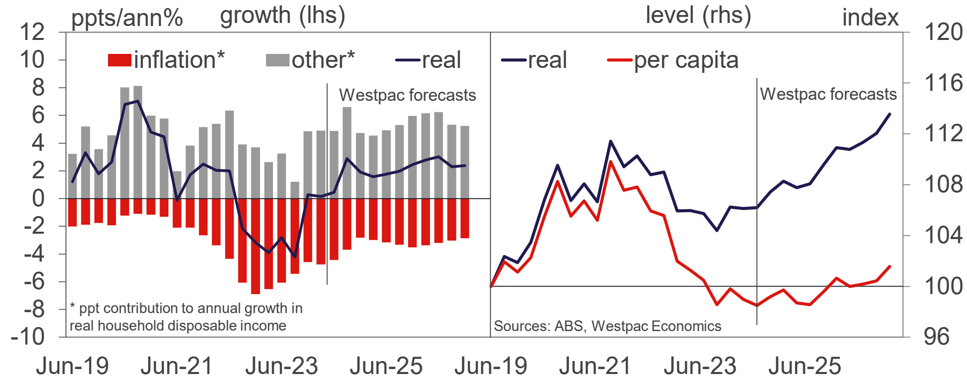
Rebooting the consumer

- Consumers finally look to be coming out of what has been a protracted period of weakness. Positive as that is, a closer look at household disposable incomes suggests the recovery from here is likely to be a gradual one.
- Real household disposable income – total income after tax, interest payments and inflation – has captured the full extent of the 'triple squeeze' on consumers over the last 2½ years. The combined effect of rising income tax payments, higher interest and the surge in inflation has produced a 4.8% drop in aggregate terms since Sep 2021 and an eye-watering 10% plunge in per capita terms. That is about double the size of the decline seen during the recession in the early-1990s (when the average mortgage interest rate was 15% and the unemployment rate spiked 4ppts on its way to an eventual peak of over 11%).
- Thankfully, the contraction has moderated significantly over the first half of 2024 with a slight recovery forming over the second half of the year – the latest lift in consumer sentiment a sign that this is starting to register with consumers (Chart 12).
- We can get a better sense of how this recovery might look by stepping through some of the components that have contributed to the squeeze on disposable incomes and some others that have acted as a buffer. The charts right and overleaf show several of these in isolation. The bottom line however, and as shown in the right panel of chart 13, is that even after two years of recovery, aggregate real disposable income is likely to only just be returning to its previous peak while per capita income will still be substantially below 2021 levels.
- Inflation accounts for most of the improvement to date. As the left panel of chart 13 highlights, the drag from rising prices has roughly halved since 2022, CPI inflation tracking back from its 7.8%yr peak to 3.8%yr as at mid-2024. As such, a further move to sub-3% annual inflation will only generate about a 1ppt improvement in real household disposable income growth from here. And, needless to say, all of this is in the form of a reduced drag rather than an improvement in level terms. Price growth is slowing but prices are not declining in outright terms.

12. Consumer sentiment vs household disposable income

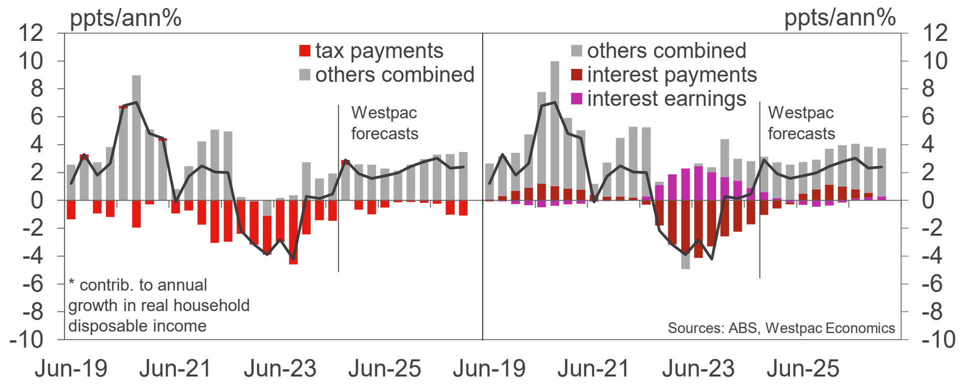


13. Household disposable income: inflation effects

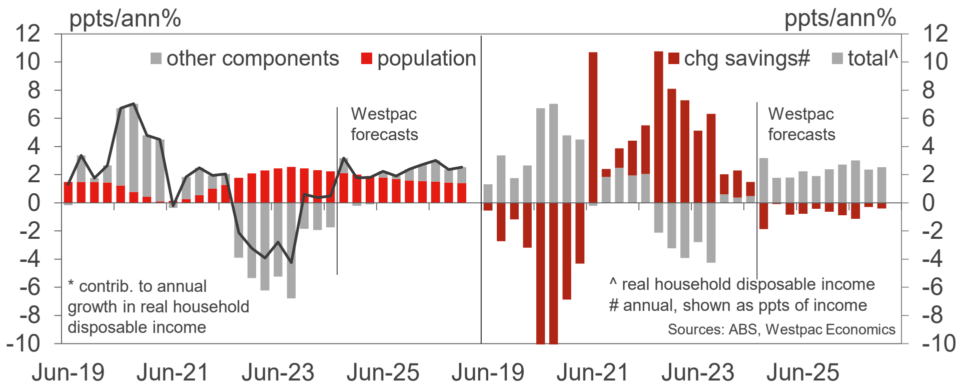


- Tax is the big swing factor coming through in the second half of 2024. As discussed, Westpac data shows the 'stage 3' tax cuts are already providing a substantial boost to incomes in the Sep quarter. However, as the left panel of Chart 14 highlights, this is coming against a big rise in tax payments that has been a substantial drag on incomes. While a softer labour market should see a less pronounced drag going forward, our indicative projections suggest tax will return to being a slight drag on incomes in 2025 and 2026.
- Interest rate declines should start to provide some support as we move into 2025. However, as highlighted in the right panel of chart 14, the scale of this support is fairly modest with the RBA expected to lower rates by 1ppt in total, taking the cash rate to a 'neutral' rather than 'stimulatory' level. This partly reflects the relatively low level of spare capacity coming into the easing cycle, in labour markets especially. Overall, our estimates suggest this will reduce mortgage payments by the equivalent of 1.1ppts of real household disposable income over 2025, partially offset by a 0.4ppt boost to interest income.
- Population growth has been a small indirect positive for income growth over the last two years. That support is starting to wane and will continue to subside over 2025 and 2026 (see left panel chart 15). The shift is small in growth terms – worth 0.4ppts in 2025 and a further 0.2ppts in 2026 – but a slight headwind nonetheless that will overlay the core slowing.
- Potentially larger is the headwind that could form around savings behaviour. Technically, this impact is on spending rather than real disposable incomes. However, we can show how fluctuations in saving look relative to incomes to get a sense of scale (right panel chart 15). A sharp savings run-down has had a major cushioning effect on the shock to incomes over the last two years – that run-down only possible because of the large carry-over reserves from the pandemic. Going forward, saving is expected to normalise, both as these reserves get depleted and as the income squeeze eases. The gradual normalisation we have factored in is an effective drag equivalent to about 0.5ppts a year on incomes. A faster rebuild could easily see a drag that is twice as large.

14. Household disposable income: tax, interest rate effects



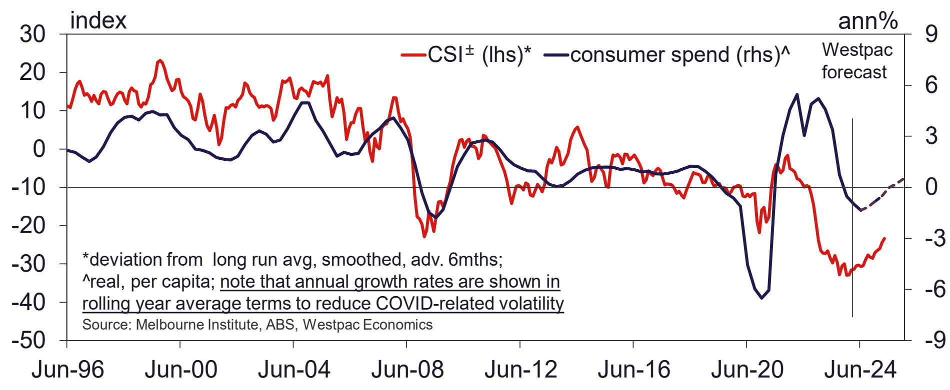
15. Household disposable income: population, savings support



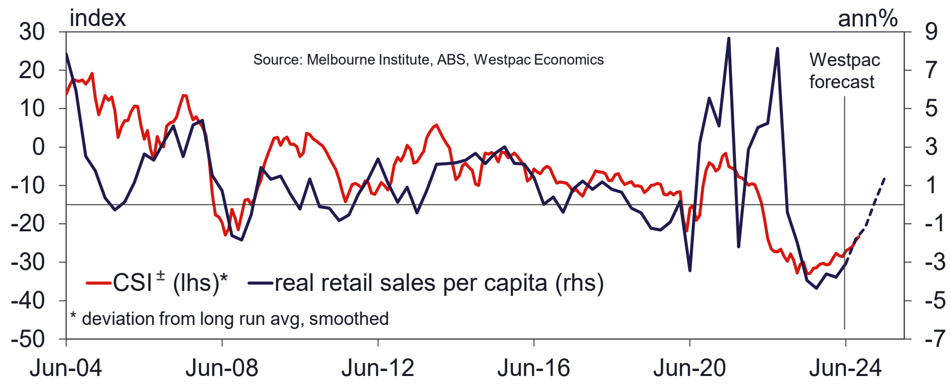
Spending

- Our CSI± composite combines sub–indexes tracking views on 'family finances' and 'time to buy a major item' with the Westpac Consumer Risk Aversion Index and usually provides a good guide to trends in spending over the next 3–6mths.
- The composite has been of more limited use recently due to pandemic-related factors that are cushioning the extent to which the shock to sentiment is flowing through to spending. In particular, the large pool of extra savings accumulated during the pandemic period has allowed many consumers to maintain spending despite a deep shock to real disposable income.
- Bearing this in mind, our CSI± indicator should be viewed as a guide to where per capita spending growth momentum may land once these buffer effects drop out of the picture.
- The latest updates suggest this 'underlying' momentum remains extremely weak but is continuing to show a noticeable improvement. The index rose 7% to 77.8 over the 3mths to Oct. The index has now risen 16.8% from the low seen in mid-2023.
- As Chart 16 shows, even with that improvement, the index is still exceedingly weak, consistent with per capita spending contracting at a 3% annual pace, or a 0.5% decline allowing for population growth running at 2.5%yr. The improvement is in the order of 0.5ppts when mapped to growth rates.
- The current pace of spending is weak but still considerably firmer than the signal from the CSI±. Household consumption declined 0.2%qtr, the weak result and downward revisions lowering annual growth to just 0.5%yr (growth was tracking towards 1%yr prior to the update). The June quarter weakening was widespread but most pronounced for 'discretionary' items, down 1.1%qtr on a combined basis.
- Across the detailed categories, the biggest drags came from transport (–4.4%qtr), vehicles (–2.6%qtr), clothing (–1.6%qtr), alcohol (–2%qtr) and cafes & restaurants (–1.5%qtr). There were also declines in some 'essentials' including basic food (–1%qtr) and fuel (–0.9%qtr).
- Where there were gains, some of these are unlikely to be sustained, e.g. relating to energy rebates and EOFY sales.

16. CSI± vs total consumer spending

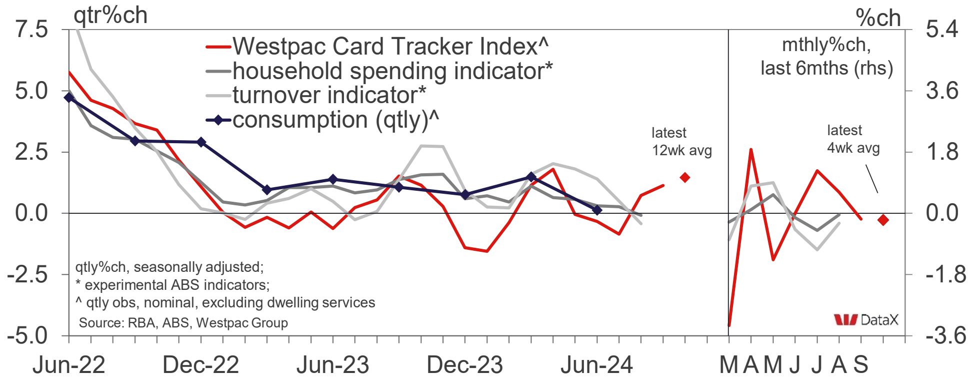


17. CSI± vs retail sales

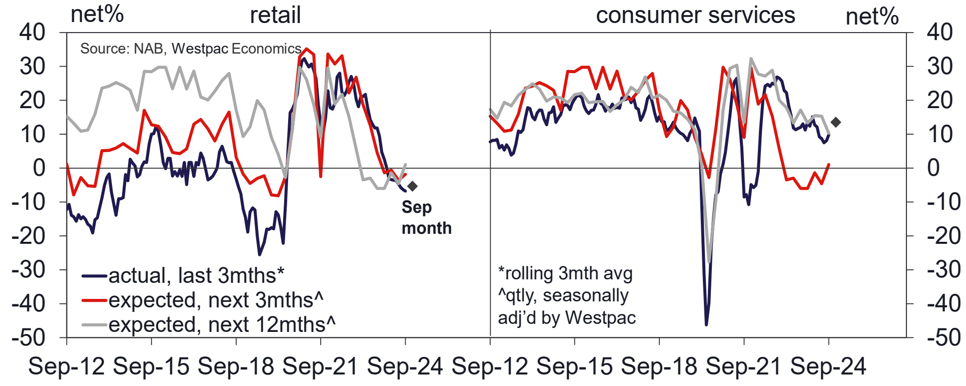


- The Q2 update was even more disappointing around incomes. Disposable income, after tax and interest, rose 0.9%qtr, 4.9%yr in nominal terms, tax payments taking another sizeable $3bn bite out of incomes (almost as large as the $3.3bn increase in labour income). Nearly all of the rise in disposable income was absorbed by higher prices, real disposable income rising just 0.1%qtr and 0.4%yr. The household savings ratio remained very low at just 0.6% of income, implying that households are continuing to draw down on reserves to maintain spending.
- It should be noted that the subsequent release of new annual national accounts benchmarks has improved the 'tone' slightly. Growth in spending for the full year was revised up from 5.9% to 6.3% for 2022-23, and while there was no change to 2023-24, the change to the previous year and to income lifted the savings rate from a 0.7% average to 2.5%. See here for more details.
- Timely indicators suggest spending has lifted in Q3. However, most suggest momentum is still relatively subdued.
- As noted already, our **Westpac Consumer Panel** showed average spend up 1.5%qtr. Allowing for population growth, that suggests aggregate spending may be up 2%qtr. Our **Westpac Card Tracker** points to a something milder gain of 1.1%qtr, albeit with the latest weekly pace tracking around 1.5% (see here).
- Other monthly ABS indicators have been mixed. Both the household spending indicator and the turnover based measure are tracking flat-to-down-slightly for Jul and Aug. The ABS retail survey is a little better, with nominal sales up 0.7% in Aug and 0.1% in Jul but still not strong. Sep updates due in coming weeks may see more of a lift and should provide a cleaner comparison for the quarter as a whole. Consumer sector responses to private sector business surveys also suggest conditions remained lacklustre. Retail respondents to the NAB survey showed conditions stable as soft levels with consumer service sector firms reporting a bit more of a lift (see here for more).
- All up, the theme appears to be of a tax cut boost that has largely been saved so far.

18. Consumer spending: selected indicators



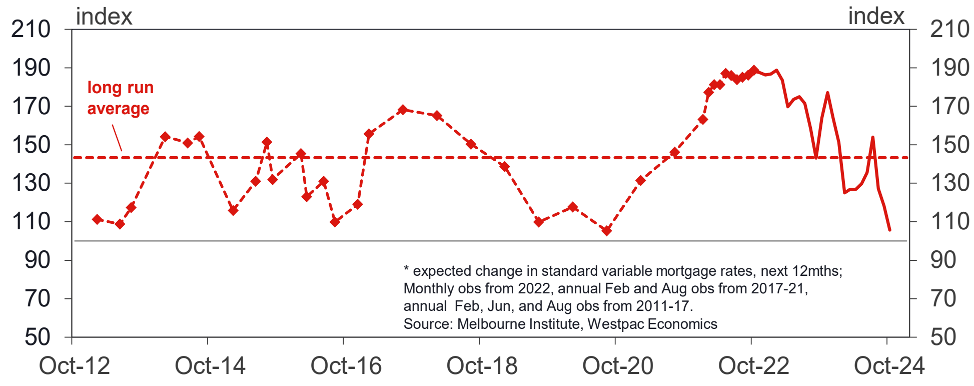
19. Business conditions: retail and consumer services



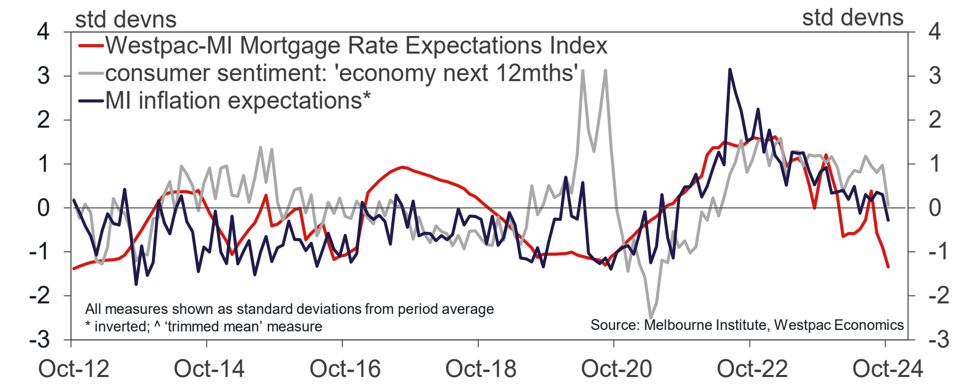
Interest rates

- The most striking sentiment shift over the last 3mths has again been around consumer expectations for interest rates, this time in the form of a veritable collapse in rate rise fears. The **Westpac-Melbourne Institute Mortgage Rate Expectations Index**, which tracks consumer expectations for variable mortgage rates over the next 12mths, fell by a third between Jul and Oct.
- At 106.4, the Index is now at its lowest level since the RBA was actively easing policy during the COVID pandemic and is on a par with the lows seen during previous periods of interest rate cuts over the last 14 years (the question was first added to the consumer survey in 2010).
- The detailed responses show 34% of consumers expect mortgage rates to rise over the next year. Just over 22% expect no change, 28% expect declines and 15% reported 'don't know'. This compares to a 60%/20%/8% rise/same/fall mix of responses back in Jul and a 40%/24%/21% in Apr.
- Financial markets are currently pricing in 85bps of rate cuts by the end of 2025.
- Our previous analysis of consumer mortgage rate expectations suggests the 'true' visibility for consumers is more like six months than 12 months ahead. As such, if we assume expectations are being formed on the basis of actual outcomes over the last 12yrs, current readings are consistent with a 69bp decline in mortgage rates.
- As already discussed, the easing in rate hike fears likely reflects several developments including: central banks moving rates lower abroad; the RBA continuing to leave rates unchanged; tentative signs of a further moderation in inflation locally; and a move lower in advertised fixed mortgage rates. Judging by the fairly muted down-shift in consumer inflation expectations, the inflation element has played a fairly minor part in the shift (see Chart 21).
- All sub-groups recorded declines in interest rate expectations, ranging from 10-20% declines across younger age groups and tenants to 40-50% drops amongst homeowners and older age groups.
- Across the mortgage belt, the latest index read is 93.5, the lowest since 2012.

20. Mortgage interest rate expectations



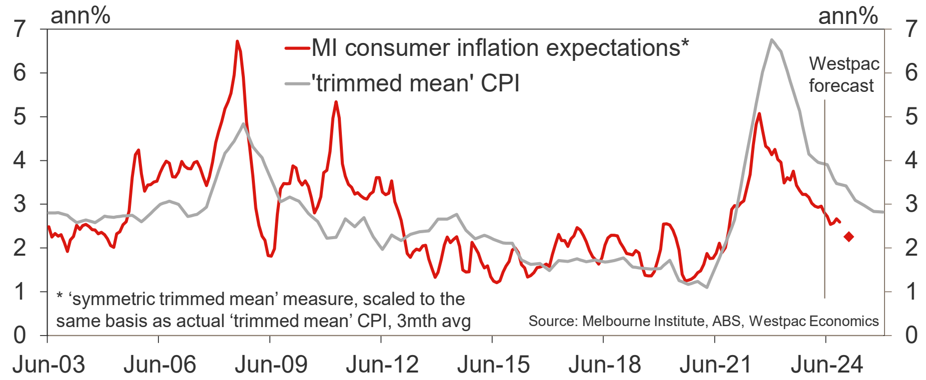
21. Consumer expectations for mortgage rates



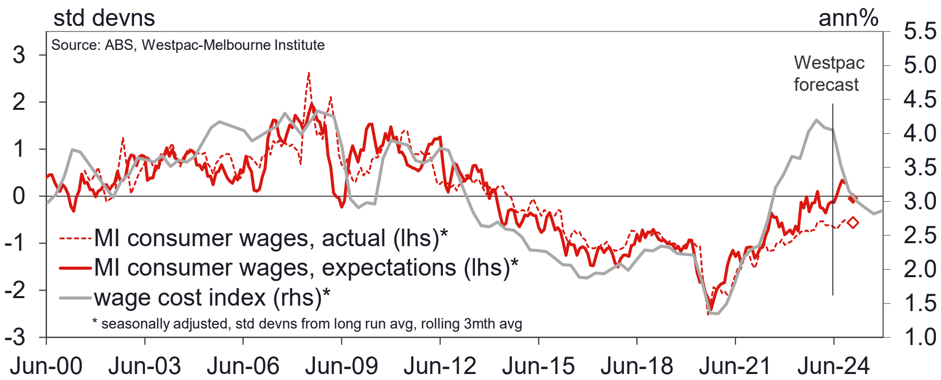
Inflation

- Consumers have continued to mark down their inflation and wage expectations although monthly volatility means the latest moves are not quite 'decisive'.
- The Melbourne Institute's 'symmetric mean' measure of consumers' year-ahead inflation expectations ticked up slightly from 4.33% in Jul to 4.47% in Aug but dropped back to 3.97% in Oct, a new cycle low going back to Aug 2021.
- Consumer inflation expectations are typically higher than observed inflation – Chart 22 gives a sense of how expectations look adjusted for this bias. On this basis, current expectations are broadly consistent with headline inflation tracking towards 2.5%yr, perhaps slightly below if the Oct drop is sustained.
- The Melbourne Institute's 'symmetric mean' measure of consumers' year–ahead wage growth expectations declined from 1.43% in Jul to 1.26% in Oct. The same measure of actual wage changes nudged up slightly from 1.20% to 1.40%. Both are at or slightly below historical averages.
- Recent RBA research provides some important insights into how consumer inflation and wage expectations are formed. The findings suggest wage expectations tend to be forward looking. However, inflation expectations tend to be more backward looking, especially for lower income households, and place a disproportionate weight on past fuel prices. Households also associate higher wages growth with good economic outcomes but higher inflation with worse economic outcomes (see here for more details, and a related speech here).
- This could pose problems for policy if inflation expectations are slow to respond and not formed on the basis of wider economic conditions.
- For now though, the main conclusions appear to be positive. Short term inflation expectations are moving lower, coming into line with well-anchored long term expectations. There does not look to be a more persistent divergence with some evidence that households may have been less backward looking through the latest episode. Currently, fuel prices are also assisting the move lower.

22. CPI Inflation: actual vs expected



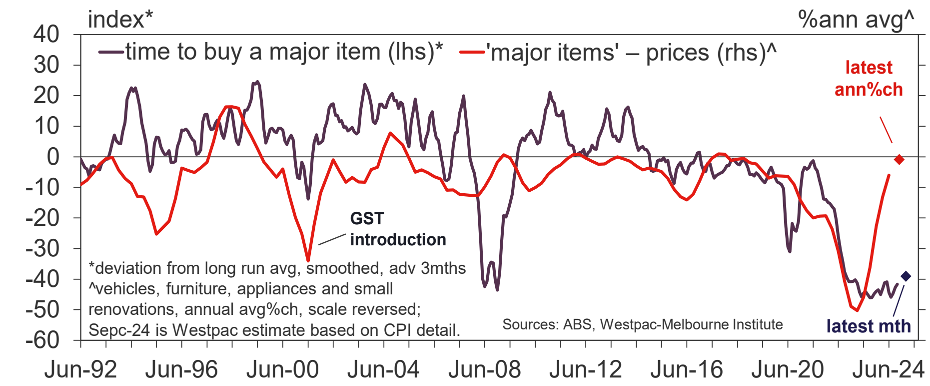
23. Wages growth: actual vs expected



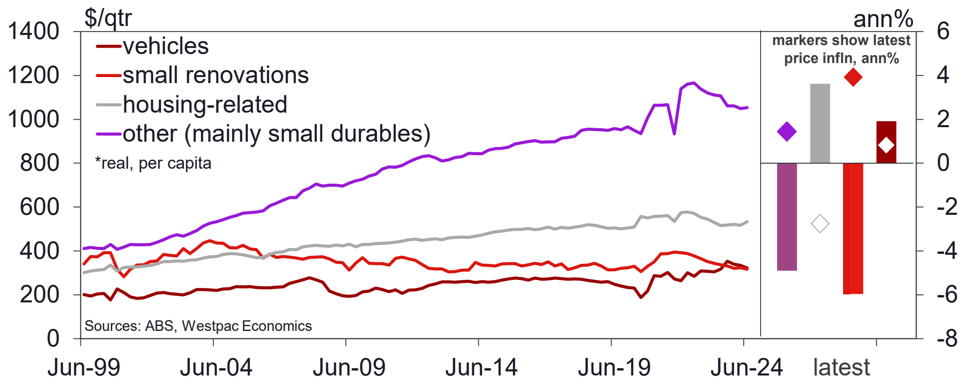
Durables

- The **'time to buy a major item'** sub-index has posted a more muted lift than other component sub-indexes over the last 3mths, rising just 3.6%. At 85.1, the index is showing a clear lift out of the very weak, sub-80 reads that prevailed through most of the first half of the year and 2023. However, it is still in the bottom 5% of observations historically.
- The continued weakness is despite a clearer improvement in prices. This sub-index was the main one to capture the impact of sharply rising prices on consumer purchasing power in 2022-23. The Q3 CPI detail is expected to confirm that – for major items such as vehicles, furniture and small renovations – prices are now flat on an annual basis (see Chart 24).
- That in turn suggests the price level, rather than just its change, will continue to weigh heavily on buyer sentiment going forward – an early sign that the consumer recovery may indeed proceed relatively slowly (see discussion on p13).
- For some time now, we have flagged that buyer sentiment may respond asymmetrically to prices, deteriorating sharply when prices spike but only improving slowly when they stabilise or fall, particularly when the price level is still well above its original starting point.
- Demand-wise, per capita durables spend has stabilised over the year to Jun-24, having slumped 7% over the previous two years. The last two quarters have even seen modest gains.
- However, performances vary significantly across sub-categories. Housing-related spend has seen relatively steady gains but 'small' renovations have continued to track lower. Vehicles spend has been uneven over the last year, lifting over the second half of 2023 but fading again in the first half of 2024 – monthly vehicle sales suggesting Q3 has seen another significant decline (sales down 9.7%yr). Other durables spend is also down 5%yr in per capita terms, albeit stabilising a little in recent quarters.
- Recent detail from both the ABS retail survey and the **Westpac Card Tracker** suggest durables spending has remained lacklustre in the Sep quarter and into early Oct with little or no boost from tax cuts to date.

24. 'Time to buy a major item' vs prices



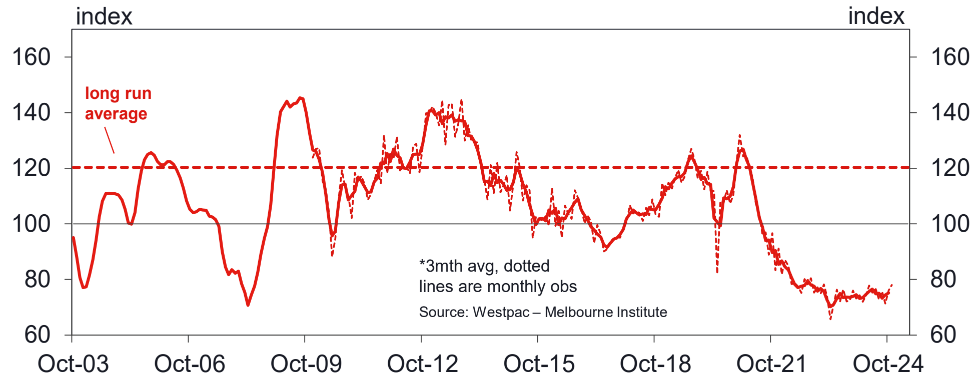
25. Consumer spending: 'big ticket' items



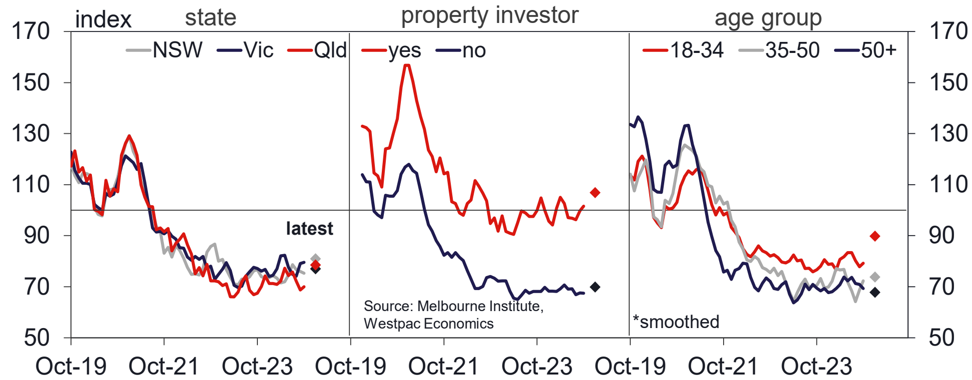
Dwellings

- Homebuyer sentiment continues to bump around historical lows. The **'time to buy a dwelling'** index rose 3% over the 3mths to Oct but at 78 remains in deeply pessimistic territory, particularly compared to the index's long run average of 120.
- While the easing in rate rise fears may have turned the dial a little for wider sentiment, they have done less to shift consumer views on housing.
- As noted previously, the 'time to buy a dwelling' index is closely linked to affordability. Previous research shows it is closely linked to measures based on the proportion of average income required to raise a deposit and make mortgage payments on a purchase of a median-priced dwelling. As such, it captures the effect of not just interest rate changes – actual or expected – but also changes in prices and incomes.
- As such, the boost to homebuyer sentiment from the shift in expectations for interest rates may have been be largely offset by actual and expected price rises and the still fairly downbeat consumer expectations for their own finances over the year ahead.
- While the sub-group detail showed a fairly clear consensus on improved sentiment overall, there was a much more mixed range of shifts for homebuyer sentiment. Nearly a third of the 100-odd sub-groups we track recorded a deterioration in homebuyer sentiment over the 3mths to Oct.
- By state, buyer sentiment rallied quite strongly in SA (+15.6%) and solidly in Qld (+5.2%), gains likely reflecting state government moves to provide more stamp duty concessions for first home buyers. Sentiment posted a smaller 1.8% gain in Vic, where prices have been slipping lower. Buyer sentiment tracked 2.5% lower in NSW but dropped 12.3% in WA to an extremely weak 61.4. By comparisons, other major state index reads are all in the 77-81 range.
- The sub-group detail suggests investor segments may be more amenable to purchases, buyer sentiment up 14.4% amongst freehold homeowners and up 5.7% amongst those that already owned an investment property – the latter still the only sub-group where those saying now is a good time to buy outnumbers saying it is bad.

26. 'Time to buy a dwelling'



27. 'Time to buy a dwelling': selected sub-groups

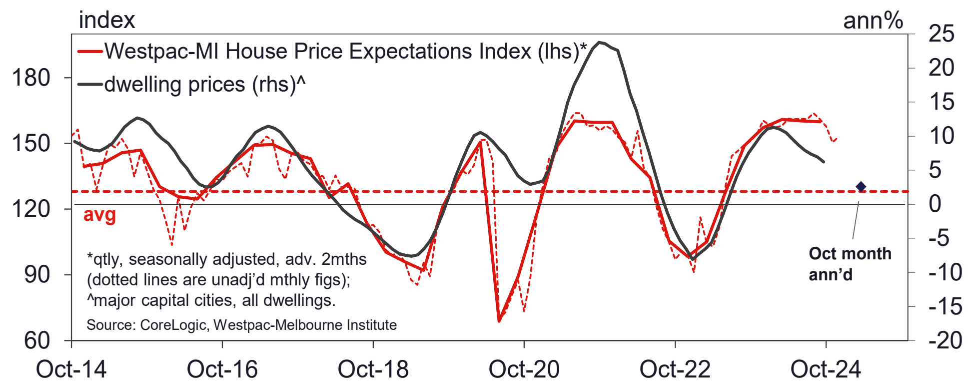


Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known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

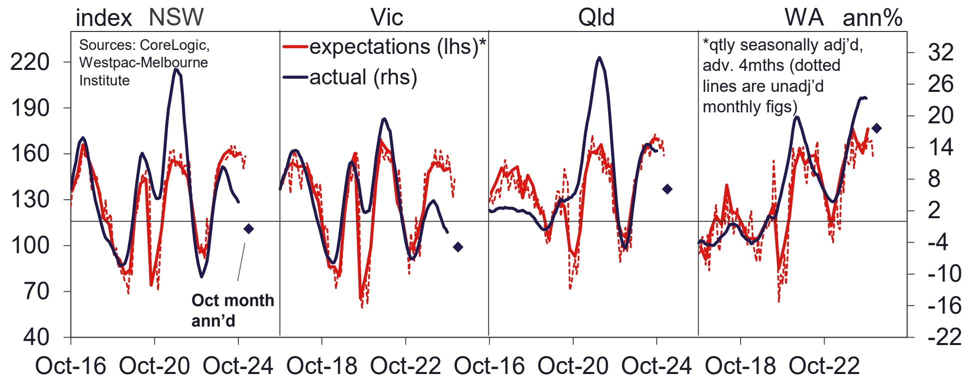
House prices

- Consumer house price expectations are still positive but the bullishness is starting to wane. The **Westpac Melbourne Institute House Price Expectations Index** declined 4.9% over the 3mths to Oct but at 153.2 remains near cycle highs, about 20% above the long run average of 128.
- The detailed responses show 64% of consumers expect prices to rise over the next 12mths, 21% expect no change and 10% expect prices to decline. That compares to a 70%/18%/8% mix in Jul.
- Actual price growth has continued to moderate. Nationally, price growth is running at just over 6%yr in Oct, down from a peak of over 11%yr at the start of 2024. The latest monthly gain is at an even slower 2.5% annualised pace.
- Not surprisingly, the softening in price expectations has been more pronounced in states that have seen a more pronounced slowing in price growth.
- Vic has seen the largest index decline, down 11.6% since the start of the year to just 143.3, only 5% above the long run average. Melbourne dwelling prices have declined 2% since late 2023.
- The NSW index has declined 4.1% over the same period, to a decidedly firmer 158.5. Sydney dwelling prices have also seen growth slow but are still posting small positive gains overall (the Oct month shaping as potentially the first monthly dip so far).
- Price growth has remained strong in the other major states, albeit with some tentative signs of moderation starting to show through in Qld and, to a lesser extent and from a stronger starting point, in WA – both state indexes are in the 155-160 range. SA has also seen more resilient price gains, the state index notably firmer at 163.8.
- The sub-group detail shows price expectations have seen more of a softening amongst homeowners and those aged 35–44 and 55–64.
- The slowdown in price growth offers another opportunity to gauge exactly how consumer house price expectations are formed. Indeed, the interest rate and house price expectations data looks ripe for conducting studies similar to the RBA's recently released work on consumer inflation and wage expectation.

28. Westpac-MI House Price Expectations Index



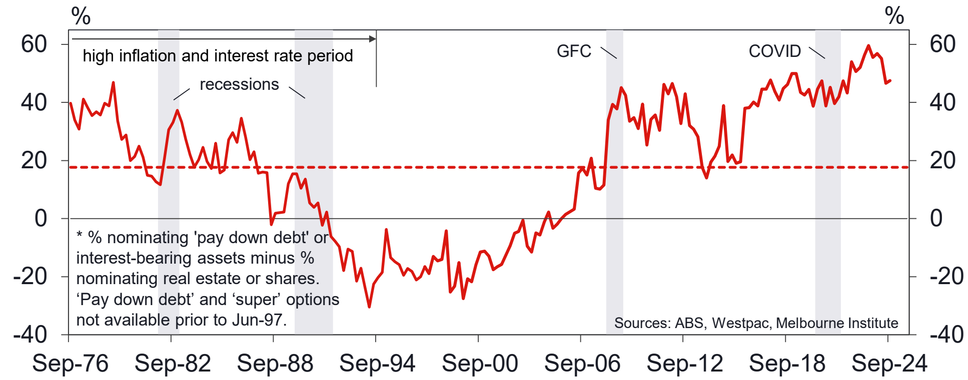
29. Dwelling prices: actual vs expected by state



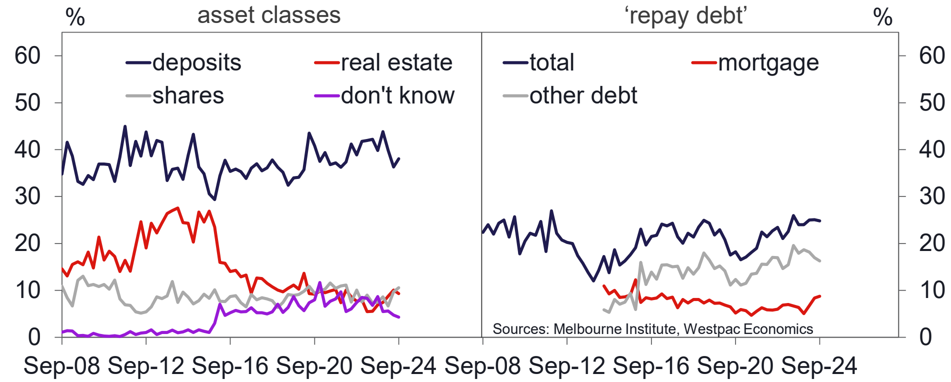
Risk aversion

- Consumer risk aversion is largely unchanged on three months ago. Aversion is still very high but has eased off the extremes seen in 2023. The **Westpac Consumer Risk Aversion Index** dipped to 46.3 in Jun from 47.7 in Mar. That compares to much higher reads in the 55-61 range over the previous five quarters. The long run historical average is 18.
- Recall that the index is based on responses to questions on the 'wisest place for savings'. These ask consumers to nominate from a range of options, the risk index being the difference between the share nominating 'safe' options such as 'deposits' and 'repay debt' and the share nominating 'risky' options such as 'shares' and 'real estate'.
- The main move since the start of the year has been a drop in the proportion favouring 'deposits' down 4.8pts to 29%, bringing it into line with the avg over the last 20yrs. Some of this may reflect a slight decline in term deposit rates, down 20bps on average since the start of the year. However, most of the move likely represents a shift in perceived relative risks.
- There was also a dip in the share nominating 'pay down debt', to 24% in Sep from 26.2% in Mar.
- The flip-side of this move is that consumers have become a little more favourable towards 'riskier' options, 10% nominating 'real estate' (vs 8.4% in Mar) and 10% nominating 'shares' (vs 7% in Mar). Compared to long run averages, the proportion favouring real estate remains very low while the proportion favouring shares is about average.
- The sub-group detail shows a significant difference between the mortgage belt and other consumers. Risk aversion has shown a more pronounced decline amongst renters (-14.6pts vs Mar) and homeowners with no mortgage (–11.5pts) but is largely unchanged amongst consumers with a mortgage (–0.8pts). This is interesting given the shift in interest rate expectations. The difference may tie back to the impact of tax cuts. As noted, most of this income boost has been saved rather than spent. The associated reduction in debt may have done more to reduce the urgency to repay debt amongst those without a mortgage than those with one.

30. Westpac Consumer Risk Aversion Index vs saving rate



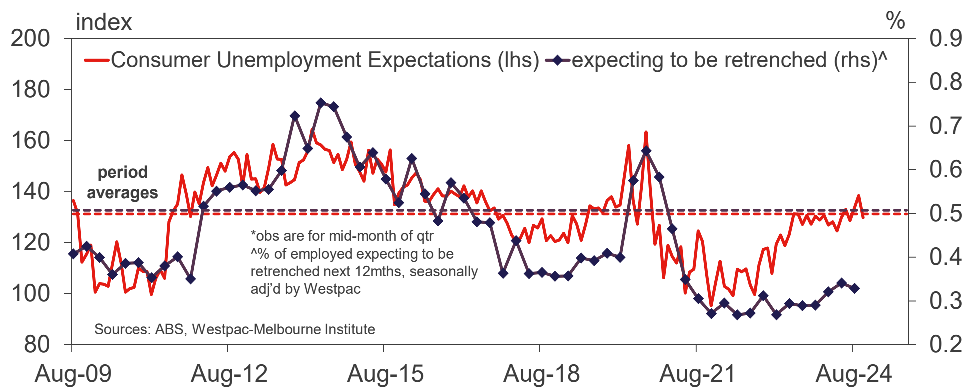
31. Consumer: 'wisest place for savings'



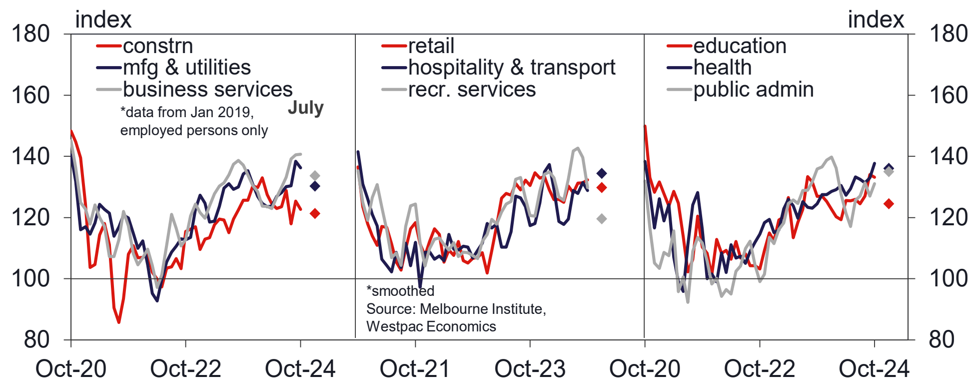
Job security

- Despite the general gloom, consumers are still not overly-concerned about potential job loss, with a brief mini-flash of concern in recent months, dissipating in Oct.
- The **Westpac-Melbourne Institute Index of Unemployment Expectations** was relatively unchanged on Jul with what was an unsettling rise through Aug-Sep largely reversing again in Oct (recall that higher reads mean more consumers expect unemployment to rise over the next 12mths). At 129.8, the Oct index read is in line with the long run average and within the 125-133 range that has prevailed since mid-2023. This is broadly consistent with expectations of flat conditions over the next year rather than a sharp labour market weakening.
- That is the same message coming from the latest ABS labour force survey updates. Employment rose 64.1k in the Sep month to be up 3.1%yr. Labour supply also seen robust growth, supported by strong population growth and a participation rate rising to new record peace-time highs going back over 100yrs, the up-trend over the last 2yrs helping to fill 800k jobs.
- Meanwhile, the unemployment rate held steady at 4.1% in Sep, the underemployment rate – which measures those that are willing and able to work more hours than they currently do – also dipping from 6.5% in Aug to 6.3% in Sep. All in all, the Sep update was a healthy one (see here for more).
- More specific measures of the incidence of job loss show both actual and expected retrenchments remain low. Just under 1% of employees reported being retrenched in the latest quarter, up slightly on the 0.8% average in 2022 and 2023 but below the 1.2% average historically. Only 0.3% of employees expect to be retrenched over the next year, again up every so slightly on recent lows but still miles below the long run average of 0.5%.
- The consumer sentiment survey detail shows some notable shifts across industries. There were particularly big improvements amongst those employed in hospitality and consumer services, suggesting tax cuts have bolstered expectations. Concerns also eased amongst construction and manufacturing workers.

32. Unemployment expectations



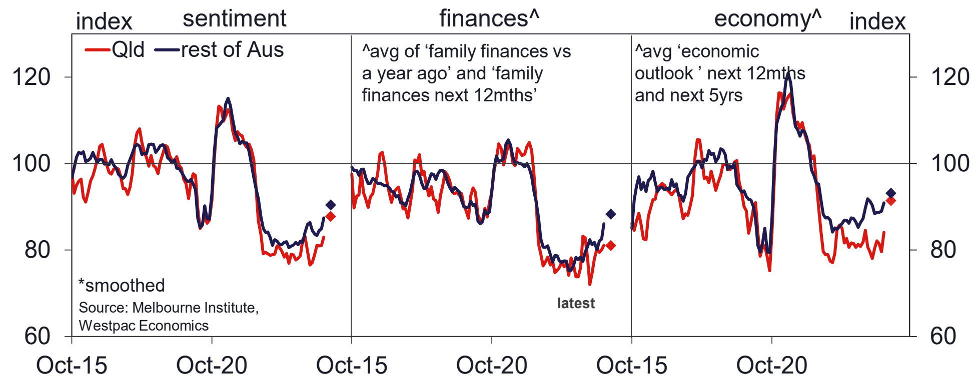
33. Unemployment expectations: selected sub-groups



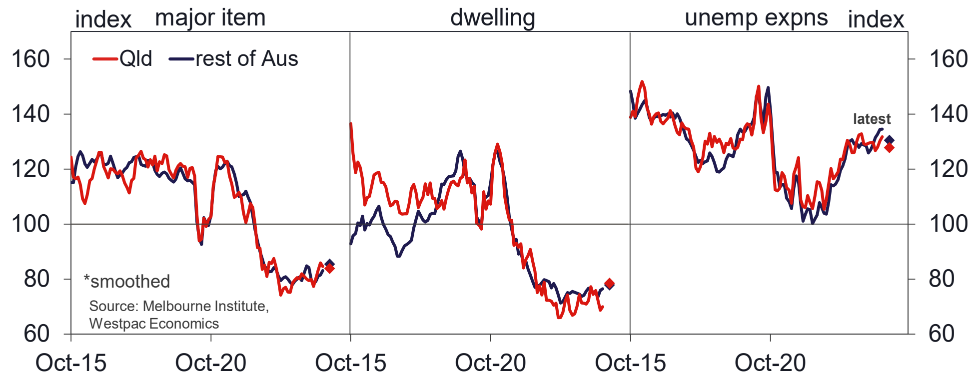
Queensland

- The last time we profiled consumer sentiment in Qld, a year ago, cost of living concerns were deepening a little with sentiment in the state posting a nasty 'wobble' in the Oct month that seemed to relate to some disappointing sporting results. A year on, Qld consumers are reporting a firming in sentiment in line with the path nationally but lagging behind in terms of levels.
- The persistent negative sentiment 'gap' is worth 4ppts overall and is equivalent in scale to the improvement seen over the last 3mths. The component detail shows the divergence has been across both assessments of family finances and the economic outlook. However, the latest monthly update showed a significant narrowing with expectations for the economy drawing more in line with views across the rest of Australia.
- The gap on finances remains though, with Qlders recording only a very muted improvement to date. That is despite more generous state government fiscal support measures rolled out since mid-year, including larger electricity subsidies than in other states, and 50c public transport fares.
- On other questions, the points of difference mostly look small - assessments of 'time to buy a major item' very similar; assessments of 'time to buy a dwelling' a touch weaker until the Oct month; and unemployment expectations actually slightly better in the state than across the rest of Australia.
- So what is going on? On most counts, Qlders do not appear to be suffering any more than their interstate peers during the current cost of living crisis. Indeed, if anything, they look to have outperformed particularly in terms of household net worth (dwelling prices rising relatively strongly) and labour incomes.
- There may well be a political element to the sentiment story in Qld. The latest reads have been in the run-up to a Qld state election in late Oct that has seen the incumbent ALP government replaced. It may be that electioneering has affected perceptions. If so, the negative drag may dissipate in coming months. That may in turn carry a bit of a warning heading into next year's Federal election due to be held by May next year.

34. Consumer sentiment, finances, economy: Qld vs rest of Aus



35. Consumer 'time to buy' unemp expns: Qld vs rest of Aus



Economic and financial forecasts

Interest rate forecasts

Australia	Latest (25 Oct)	Dec–24	Mar–25	Jun–25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
Cash	4.35	4.35	4.10	3.85	3.60	3.35	3.35	3.35	3.35	3.35
90 Day BBSW	4.38	4.42	4.19	3.96	3.73	3.50	3.55	3.55	3.55	3.55
3 Year Bond	3.91	3.60	3.60	3.55	3.55	3.50	3.50	3.50	3.55	3.60
3 Year Swap	3.90	3.55	3.50	3.45	3.40	3.35	3.30	3.30	3.35	3.40
10 Year Bond	4.40	3.90	3.90	3.90	4.00	4.05	4.05	4.10	4.10	4.15
10 Year Spread to US (bps)	23	15	15	10	10	5	5	5	5	5
US										
Fed Funds	4.875	4.375	3.875	3.625	3.375	3.375	3.375	3.375	3.375	3.375
US 10 Year Bond	4.17	3.75	3.75	3.80	3.90	4.00	4.00	4.05	4.05	4.10

Exchange rate forecasts

	Latest (25 Oct)	Dec–24	Mar–25	Jun–25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
AUD/USD	0.6623	0.69	0.70	0.71	0.72	0.73	0.73	0.73	0.74	0.74
NZD/USD	0.5997	0.62	0.63	0.63	0.63	0.64	0.64	0.64	0.64	0.64
USD/JPY	151.57	142	141	140	139	138	137	136	135	134
EUR/USD	1.0823	1.11	1.11	1.12	1.13	1.14	1.14	1.15	1.15	1.15
GBP/USD	1.2967	1.33	1.33	1.34	1.34	1.34	1.35	1.35	1.35	1.35
USD/CNY	7.1239	7.00	6.95	6.90	6.80	6.70	6.65	6.60	6.55	6.50
AUD/NZD	1.1044	1.11	1.11	1.13	1.15	1.14	1.14	1.14	1.16	1.16

Sources: Bloomberg, Westpac Economics.

Economic and financial forecasts

Australian economic growth forecasts

	2024				2025			
	Q1	Q2	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
GDP %qtr	0.2	0.2	0.6	0.5	0.5	0.5	0.6	0.6
%yr end	1.3	1.0	1.2	1.5	1.9	2.2	2.2	2.4
Unemployment Rate %	3.9	4.1	4.2	4.3	4.4	4.5	4.5	4.6
Wages (WPI) %qtr	0.9	0.8	0.8	0.7	0.7	0.7	0.7	0.7
%yr end	4.1	4.1	3.5	3.2	3.0	2.9	2.8	2.9
CPI Headline %qtr	1.0	1.0	0.3	0.4	0.6	0.9	1.2	0.8
%yr end	3.6	3.8	2.9	2.6	2.3	2.2	3.2	3.6
CPI Trimmed Mean %qtr	1.0	0.8	0.7	0.7	0.7	0.7	0.7	0.8
%yr end	4.0	3.9	3.5	3.3	3.0	2.9	2.8	2.9

	Calendar years			
	2023	2024f	2025f	2026f
GDP % yr end	1.6	1.5	2.4	2.4
%yr end	3.9	4.3	4.6	4.6
Wages (WPI) annual chg	4.2	3.2	2.9	3.4
CPI Headline annual chg	4.1	2.6	3.6	2.8
Trimmed mean annual chg	4.1	3.3	2.9	2.6

Calendar year changes are (1) period average for GDP, employment and unemployment, terms of trade (2) through the year for inflation and wages.
* GDP & component forecasts are reviewed following the release of quarterly national accounts.
** Business investment and government spending adjusted to exclude the effect of private sector purchases of public sector assets.

Consumer demand

	2023			2024				2025
% change	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3f**	**Q4f**	**Q1f**
Total private consumption*	0.5	-0.1	0.2	0.6	0.2	0.6	0.4	0.6
annual chg	2.2	1.3	0.8	1.2	0.9	1.6	1.8	1.8
Real labour income, ann chg	2.2	2.4	3.3	2.0	1.7	1.3	1.6	1.7
Real disposable income, ann chg**	-2.8	-4.2	0.6	0.4	0.5	3.2	1.8	1.8
Household savings ratio	1.7	0.1	1.4	0.6	0.6	1.9	1.4	1.4
Real retail sales, ann chg	-1.5	-1.7	-1.0	-1.3	-0.6	0.6	1.0	2.2
Motor vehicle sales ('000s)***	860	972	928	905	887	917	947	925
annual chg	14.6	21.9	15.6	11.8	3.2	-5.7	2.0	2.3

	Calendar years			
	2022	**2023**	**2024f**	**2025f**
Total private consumption, ann chg*	7.1	2.1	1.4	2.1
Real labour income, ann chg	3.5	2.7	1.7	1.1
Real disposable income, ann chg**	-0.4	-2.6	1.5	2.1
Household savings ratio, %	7.0	1.4	1.1	1.7
Real retail sales, ann chg	5.1	-1.0	-0.1	2.9
Motor vehicle sales ('000s)	781	892	914	938
annual chg	3.3	14.3	2.4	2.6

Notes to pages 24 and 25:
* National accounts definition.
** Labour and non–labour income after tax and interest payments.
*** Passenger vehicles and SUVs, annualised
^ Average over entire history of survey.
^^Seasonally adjusted. # Net % expected rise next 12 months minus % expecting fall (wage expectations is net of % expecting wages to rise and % expecting flat/decline).
Note that questions on mortgage rate and house price expectations have only been surveyed since May 2009.

Consumer sentiment

		2024									
% change	avg^	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct
Westpac–MI Consumer Sentiment Index	100.5	81.0	86.0	84.4	82.4	82.2	83.6	82.7	85.0	84.6	89.8
family finances vs a year ago	88.2	63.0	66.1	65.2	65.5	63.2	69.3	63.5	70.9	71.8	73.8
family finances next 12 months	106.7	93.0	95.3	93.8	95.5	96.1	96.5	92.1	96.8	97.0	99.7
economic conditions next 12 months	90.6	81.8	88.9	84.9	82.7	83.2	78.5	81.4	83.3	81.2	92.8
economic conditions next 5 years	92.0	89.1	93.0	94.0	89.8	92.2	94.1	94.5	91.5	90.6	97.8
time to buy major household item	124.1	78.0	86.8	84.2	78.7	76.5	79.7	82.1	82.6	82.6	85.1
time to buy a dwelling	120.3	72.0	74.2	77.8	75.3	76.5	72.8	75.7	71.4	76.1	78.0
Westpac–MI Consumer Risk Aversion Index^^	18.1	–	–	55.1	–	–	46.6	–	–	47.5	–
CSI±	100.2	69.4	73.1	72.0	71.9	71.6	74.7	72.7	75.8	76.0	77.8
Westpac–MI House Price Expectations Index#	128.1	158.1	161.4	161.1	161.2	161.1	163.8	161.2	157.8	150.5	153.2
consumer mortgage rate expectations#	40.5	47.0	21.6	20.9	22.8	33.0	41.2	59.2	35.5	23.8	6.4
Westpac–MI Unemployment Expectations	129.2	130.7	126.9	128.1	124.6	129.8	133.1	128.6	133.5	138.4	129.8
MI inflation expectations (trimmed mean)	4.4	4.5	4.5	4.3	4.6	4.1	4.4	4.3	4.5	4.4	4.0
MI wage expectations (trimmed mean)	1.3	0.9	1.2	1.4	1.0	1.2	1.3	1.4	1.5	1.4	1.3

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