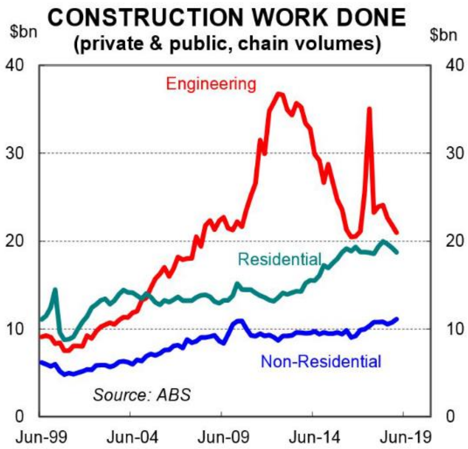
# WEEKLY ECONOMIC COMMENTARY

**Week beginning 27th May 2019**

## ECONOMIC DATA ROUNDUP

### DATA RELEASED LAST WEEK

| Economic Data | Period | Actual | Previous |
|---|---|---|---|
| Construction Work Done | March quarter | -1.9% | -3.1% |
| Skilled Internet Vacancies Index | April | -1.6% | -1.5% |




**Construction work done** fell 1.9% in the March quarter, the third consecutive quarterly fall and although the previous quarter was revised up to +2.1%, construction work done is now down 6.0% over the year.

Housing (-2.5%) and engineering construction (-3.9%) continued to decline in the quarter while non-residential building strengthened (+3.6%). Private residential construction was down 2.5% while non-residential construction increased by 3.6%.

The **Internet skilled vacancy index** decreased by 1.6% (or 2,800 job advertisements) in April 2019, with the index now down 5.9% (or 10,800 job advertisements) over the year. Job advertisements decreased in all eight occupational groups this month with the strongest falls recorded for Labourers (-2.2%), Machinery Operators and Drivers (-2.0%) and Technicians and Trades Workers (-1.9%).

The minutes of the RBA's May board noted that members had reassessed the disinflationary impact of the weak housing market which had prompted a downward revision to their outlook. The minutes also emphasised that the RBA's forecasts for GDP and inflation assumed that interest rates would move in line with the path implied by financial markets, which currently forecast the cash rate to fall to 1.0%. If interest rates were kept unchanged, GDP and inflation would be even weaker.

The RBA clearly indicated it was focussed on the labour market and would lower rates if the labour market does not continue to improve. The latest data saw employment rise a further 28,400 in May (better than expected) while the unemployment rate increased to 5.2%. Initial thoughts were that the rise in the unemployment rate was not significant enough for the RBA to cut rates.

However, last week's speech by RBA Governor Philip Lowe suggested that the RBA sees it differently. From Lowe's speech: *"A lower cash rate would support employment growth and bring forward the time when inflation is consistent with the target. Given this assessment, at our meeting in two weeks' time, we will consider the case for lower interest rates."*

This appears to be a very clear forward guidance from the RBA and as such, financial markets are now set for the RBA to deliver a rate cut in early June.

In other news, the six-month annualised growth rate in the **Westpac/Melbourne Institute Leading Index**, which indicates the likely pace of economic activity relative to trend three to nine months into the future, fell to -0.47% in April from -0.13% in March. The **NAB cashless retail sales index** gained 1.2% in April compared to a 0.5% fall in March with sales now up 6.6% annually.

Data over the next week

| Economic Data | Date | Period | Forecast | Previous |
|---|---|---|---|---|
| Private New Capital Expenditure (Capex) | 30 May | March quarter | +0.5% | +2.0% |
| Building Approvals | 30 May | April | +2.0% | -15.5% |
| Private Sector Credit | 31 May | April | +0.3% | +0.3% |

# ECONOMIC COMMENTARY

## LAST WEEK

There was a defensive start to last week ahead of important RBA commentary with risk appetite remaining under pressure as investors continued to react to negative US-China trade headlines. There was also a noticeable reaction to the election result in financial markets, equity markets have risen, as did bond yields.

The sell-off was quickly reversed after the release of the minutes from the May RBA board meeting and a speech by RBA Governor Lowe which strongly suggested that the RBA will cut interest rates at its next meeting on the 4th June. Lowe repeated the message from the RBA board minutes that the RBA's forecasts had already built in two 25 basis point rate cuts (market view on rates), without which "the forecast for unemployment would have been higher".

This view is now close to the consensus in financial markets with several local and international banks revising their forecasts on the back of Lowe's speech to now expect rate cuts in June and August.

By the close on Friday, the 90-day bank bill was trading at 1.44% compared to 1.56% a week earlier. In the long-term maturities, three and ten year bond yields closed at 1.10% and 1.52% respectively, from 1.19% and 1.64% a week earlier.

## CURRENCY

After experiencing a surprise election result honeymoon rally to almost 70 cents early last week, the Australian dollar took a massive dive after the RBA Governor Philip Lowe signalled that a rate cut was on the cards at the upcoming June RBA board meeting. The AUD traded as low as USD0.6865 last week, consolidating near the five-month low just below the 69-cent level.

There was another big move in the British pound last week as the Brexit concerns leapt back onto centre-stage, falling to its lowest level against the US dollar since 4th January as UK Prime Minister again struggled to win support for her latest Brexit plan.

By the close last Friday, the Australian dollar was trading at USD0.6897 compared to USD0.6889 a week earlier.

## EQUITIES

There was quite a large market reaction last Monday and one that outstripped what many had expected. Given the ALP was widely expected to win, investors had priced discounts into major bank stocks since the end of last year as expectations grew that Labor would abolish negative gearing tax breaks, franking credits, overhaul mortgage broker pay and tighten lending regulations. The Coalition win saw markets reverse this sentiment with the finance sector leading a solid rally early last week, bank stocks alone rallying over 10% last week. US equities however fell as concerns over the strength of global economic activity and escalating trade tensions continued to dampen sentiment.

By the close last Friday, the S&P/ASX200 Index was trading at 6,456.0 compared to 6,365.3 a week earlier.

## THIS WEEK

The focus this week is on the March quarter Capital Expenditure data which will give an indication of what firms spent on investment over the first quarter of 2019 as well as updates to capex plans going forward. Monthly building approvals and credit data for April are also released.

### INTEREST RATE VIEW

Following commentary from the RBA last week, financial markets are now convinced there appears to be no sense in waiting with the consensus now being that the RBA will deliver a 25 basis point rate cut in early June and a further rate cut to follow, probably in August, with a 'terminal' cash rate of 1.0% expected to remain through 2019 and 2020.

| Economic Data | 12 months ago | 6 months ago | 3 months ago | 1 month ago | Now |
|---|---|---|---|---|---|
| Official Cash Rate | 1.50 | 1.50 | 1.50 | 1.50 | 1.50 |
| 90 day Bank Bill | 1.94 | 1.94 | 1.88 | 1.56 | 1.44 |
| 180 day Bank Bill | 2.06 | 2.12 | 2.00 | 1.61 | 1.44 |
| 1 year swap | 1.96 | 1.96 | 1.81 | 1.42 | 1.26 |
| 3 year swap | 2.23 | 2.15 | 1.77 | 1.38 | 1.19 |
| 5 year swap | 2.61 | 2.48 | 2.01 | 1.64 | 1.41 |
| 10 year swap | 2.96 | 2.83 | 2.33 | 2.02 | 1.77 |
| AUD/USD | 0.7564 | 0.7248 | 0.7156 | 0.7028 | 0.6897 |
| S&P/ASX200 Index | 6,032.8 | 5,671.6 | 6,128.4 | 6,385.6 | 6,456.0 |

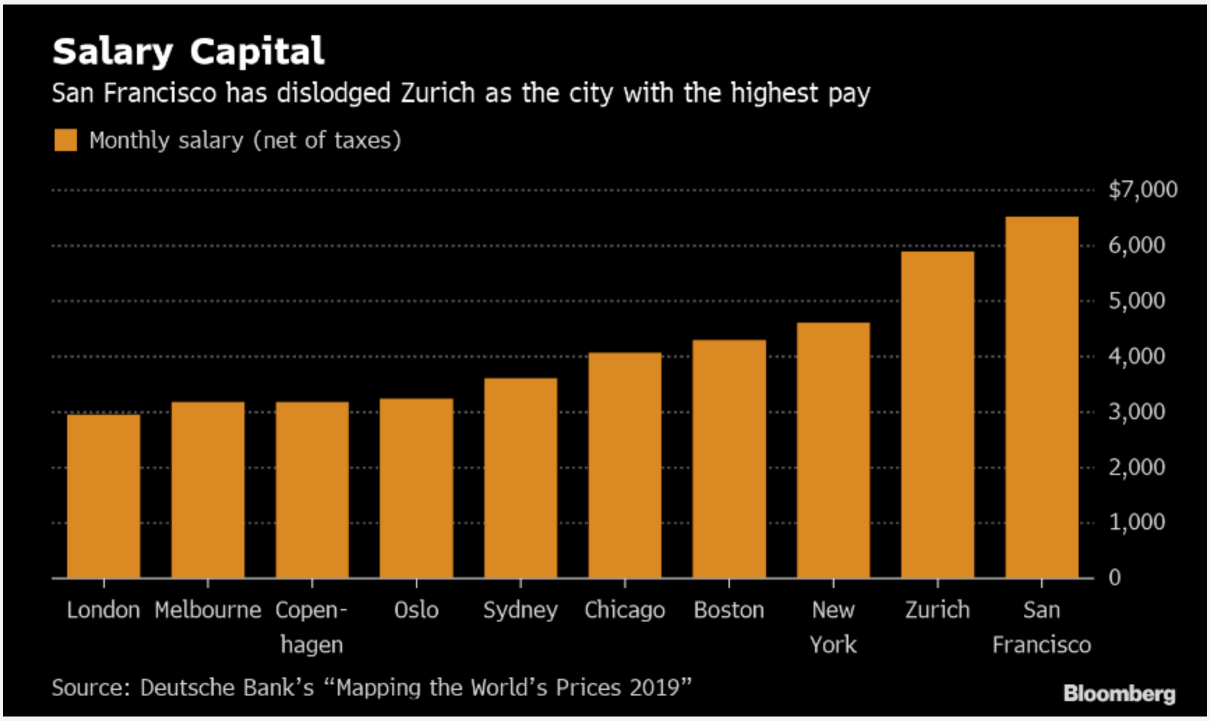
## CHART OF THE WEEK

### Mapping the world's prices 2019

Looking for a bump in salary and lifestyle? Then try San Francisco. The US West Coast city has soared up the rankings to dislodge Zurich as the location with the highest salaries and disposable income after rent, according to Deutsche Bank's "Mapping the World's Prices 2019."

This is the eighth DB Research annual survey of global prices and living standards from various countries and cities around the world.

In 2019, the long-standing dominance of Zurich as the city with the highest salaries and disposable incomes (after rent) is over. We have a new city to send our CVs to and that's San Francisco. Zurich drops to number two. San Francisco has climbed a stunning seven and 21 places on these two measures over the last five years. It's also climbed seven places to number nine over both the last one and five years in our quality of life index.




Overall, this shows that the rapid growth of the US tech sector is helping San Fran beat traditional capital cities for incomes. While its cost of living is increasing each year and rising up the cost rankings on most measures we cover, it still lags major global capitals. In terms of two-bed rents however, it is only behind Hong Kong.

Part of the five-year climb of San Fran is also a US and USD story as New York, Boston and Chicago fill out the rest of the top five in terms of salaries and disposable incomes. They have all entered the top five recently as the US economy/USD powers ahead helping edge out Australian and major European cities.

If Zurich has lost its top spot on incomes/salaries, it still tops the charts or gets close in many of the most expensive goods and services. It is generally followed by Nordic/Scandinavian countries with other European cities not far behind. Zurich though has climbed one place to top of our quality of life series edging Wellington back to second place. Copenhagen, Edinburgh, Vienna, Helsinki, Melbourne, Boston, San Fran and Sydney fill out the top ten.

The Swiss city still tops the survey for quality of life, just don't expect love to come cheap - it remains the most expensive place to go on a date.

*Source:* *Bloomberg, 21 May 2019*
*Deutsche Bank Research, 16 May 2019*

## About Rural Bank

Rural Bank has been a wholly-owned subsidiary of Bendigo and Adelaide Bank Limited since 2010. It is the only Australian-owned and operated dedicated agribusiness bank in the country, providing exceptional financial services, knowledge and leadership for Australian farmers to grow.

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