Inflation In Focus Amid Busy Data Week

Inflation

This week will be a busy one for economists as the economic data flow picks up following a slower January period.

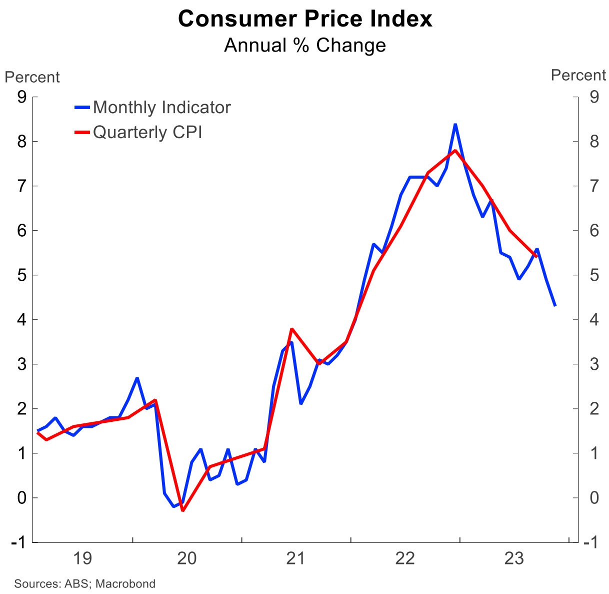
The Reserve Bank (RBA) will be watching closely, as it receives important updates on the state of inflation and the consumer going into the end of 2023.

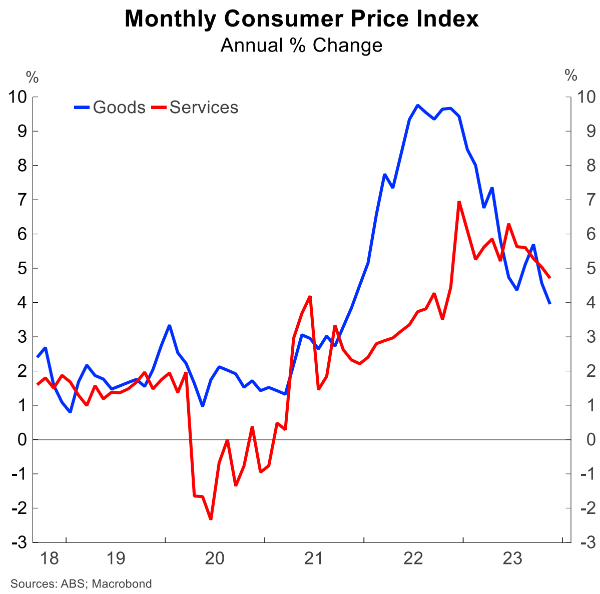
The December quarter inflation report, due Wednesday, is the highlight of the domestic calendar. Inflation continues to ease, as evidenced by the slowdown in the monthly inflation indicator over recent months. Specifically, the annual rate of inflation slowed to 4.3% in November, down from 4.9% in October and 5.6% in September.

The monthly indicator provides important insights on where the quarterly number is likely to land. However, it is more of an appetiser, with the quarterly inflation report being the main course.

The monthly inflation indicator isn't a true monthly measure of inflation. Not all categories are measured on a monthly basis. Some are measured quarterly, either in the first, second or third month of the quarter. A few are only measured once a year. The monthly indicator reports only the categories that are measured in that particular month, while those that are not measured are imputed from previous data (i.e. prices are assumed to be unchanged in the month).

The quarterly release aggregates the monthly information over the quarter.





We expect the headline measure of inflation to print at 0.8% in the December quarter and 4.3% in annual terms. This compares with quarterly and annual growth of 1.2% and 5.4%, respectively, in the September quarter.

This would be a material decline in inflation. Indeed, it would also be below the RBA's forecasts from their November Statement on Monetary Policy of 1.0% for the quarter and 4.5% for the year.

For the trimmed mean – which removes more volatile price changes – we expect growth of 0.9% in the quarter and 4.4% in annual terms. This would also be below the RBA's November forecast of 1.1% and 4.5% for the quarter and year, respectively.

The RBA will be watching closely for any signs that domestic inflationary pressures are remaining sticky. However, the data flow since the RBA's last meeting in December has largely surprised slightly to the downside. The monthly inflation indicator has also showed some positive developments regarding services inflation. Services prices are more closely impacted by domestic supply and demand factors. Encouragingly, the rate of services inflation has been slowing in the last few months of 2023, according to the monthly inflation indicator.

This suggests that the risk of a significant upside surprise for inflation on Wednesday is low. Indeed, we think there is downside – rather than upside – risk to our forecast.

Assuming the inflation numbers come in broadly in line with our forecasts, they should add further weight to our expectation that the RBA is done with its tightening cycle and that the next move in rates is down. At this stage, we expect that the RBA will be able to begin cutting rates in the September quarter of 2024.

Consumer

On Tuesday, we will receive an update on retail spending for the month of December. The consumer remains under significant pressure from inflation, higher interest rates, and an increasing tax take from bracket creep. As a result, per capita spending has been incredibly weak. However, aggregate spending has been supported by strong population growth.

Seasonality has also had an impact on the numbers in recent months. Black Friday sales in November have become increasingly popular in Australia. This means that shopping which would have previously occurred in December has been brought forward to November. This impacts the seasonal factors produced by the Australian Bureau of Statistics (ABS). Eventually, this seasonal impact will be less acute once the popularity of Black Friday sales stabilises, as highlighted by the ABS. However, while this stabilisation process is still underway, there will continue to be an impact on the seasonal numbers from this transition.

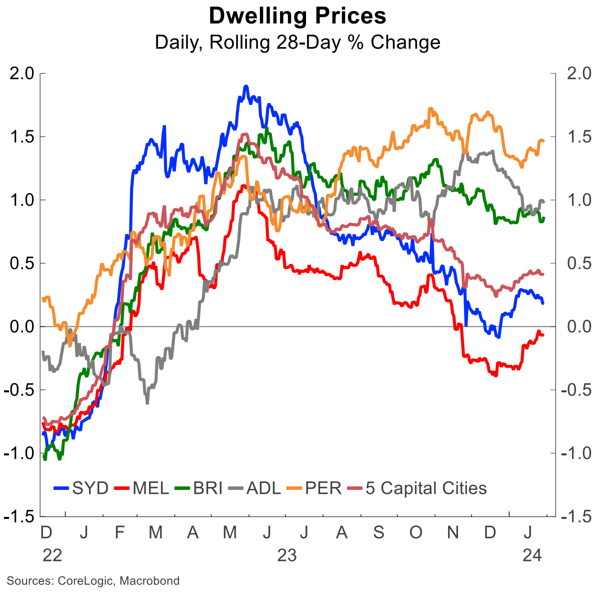
In November, sales jumped by 2.0%. We expect part of this strength to reverse in December, owing to some of the factors noted above. We expect sales to fall by 0.5% in the month.

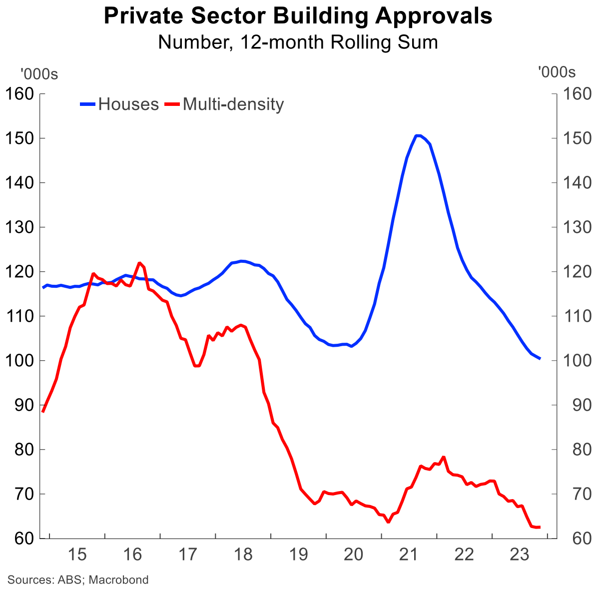
Housing

A range of housing-related data will be released this week.

Firstly, January dwelling price data will be released on Thursday. Dwelling prices rose 0.4% in December and ended 2023 8.1% higher. Conditions across the housing market became more varied towards the end of 2023. The smaller capital cities of Perth, Brisbane, and Adelaide continue to demonstrate robust price growth. Affordability is less stretched across these capital cities than the major cities of Sydney and Melbourne. Demand also remains robust against an environment on constrained supply and low listings. In comparison, price growth in Sydney and Melbourne slowed towards the end of 2023. Listings in Sydney and Melbourne have risen to be closer to average levels, in stark contrast to the smaller capital cities.

Daily price growth data suggests that these broad trends continued through January. For the month, we expect that dwelling prices rose 0.5% in January – on par with the December rise.





December building approvals data will also be released on Thursday. Building approvals continue to be volatile, driven by large swings in approvals for multi-density dwellings, such as apartments and townhouses. Approvals for detached houses have been less volatile. Looking through the volatility, approvals have broadly stabilised at a historically low level. The data continues to paint a challenging picture for the supply side of the housing market. Demand continues to be robust, led by strong population growth. However, the supply response is likely to be muted compared to previous cycles due to elevated construction costs, ructions in the construction industry and higher interest rates. In November, approvals rose 1.6%. For December, we expect some of this strength to unwind and for approvals to fall 0.5% in the month.

December housing finance data will be released on Friday. Housing finance has been recovering through 2023 after hitting a cycle low in February. Lending activity has broadly mirrored the recovery in dwelling prices. For December, we expect that housing finance rose 2.5% in the month. This would follow growth of 1.0% in November.

Other

Another piece of domestic data to be released this week is the December private sector credit statistics. The annual pace of credit growth progressively slowed over 2023. Monthly growth rates have been averaging around 0.4% per month over 2023, with some volatility from month to month. In November, credit grew by 0.4%, for an annual rate of 4.7%. We expect the pace of growth in December to remain steady at 0.4% for the month.

International

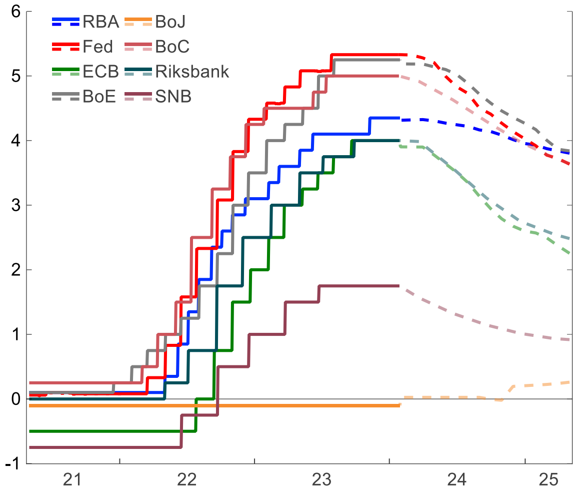
The key international events this week are meetings of the Federal Reserve (Fed) and the Bank of England (BoE). Expectations are firmly for both central banks to remain on hold. However, the focus will not be on the decision itself.

Instead, economists and financial market participants will focus closely on any changes in the narrative and whether there are any clues for the path of monetary policy in 2024.

Financial markets are currently pricing aggressive rate cutting cycles from most major central banks in 2024. For the Fed, financial markets are currently pricing around 135 basis points of cuts in 2024. For the BoE, markets currently have around 107 basis points of cuts in the profile.

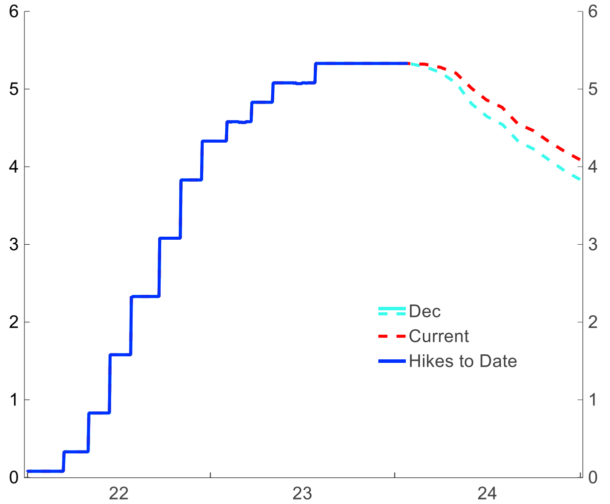
Of note, this pricing has been somewhat pared back from the levels towards the end of 2023. For example, towards the end of 2023, financial markets were pricing nearly 160 basis points of cuts by the Fed in 2024.

Central Banks Policy Rates
Historical & Market Expectations, %



Sources: RBA, ASX, New York Fed, CME Group, ECB, ICE, BoE, BOJ, TFX, BoC, TMX, Riksbanken, Nasdaq OMX Nordic, SNB, Macrobond

Federal Funds Rate Market Pricing
Fed Funds Rate Futures



Sources: New York Fed, CME Group, Macrobond

Any changes in the narrative are likely to be quickly reflected in market pricing and may lead to volatility in bond yields, as investors and traders try to narrow in on the most likely outcomes for 2024.

Jarek Kowcza, Senior Economist
Ph: +61 481 476 436

Group Forecasts

		2024				2025	
End Period:	**Close (26 Jan)**	**Q1 (f)**	**Q2 (f)**	**Q3 (f)**	**Q4 (f)**	**Q1 (f)**	**Q2 (f)**
Aust. Interest Rates:							
RBA Cash Rate, %	4.35	4.35	4.35	4.10	3.85	3.60	3.35
90 Day BBSW, %	4.35	4.55	4.47	4.22	3.97	3.72	3.47
3 Year Swap, %	3.95	4.15	4.10	4.05	4.00	3.90	3.70
10 Year Bond, %	4.24	4.35	4.30	4.20	4.15	4.10	4.05
US Interest Rates:							
Fed Funds Rate, %	5.375	5.125	4.875	4.625	4.375	4.125	3.875
US 10 Year Bond, %	4.14	4.25	4.20	4.15	4.10	4.05	4.05
USD Exchange Rates:							
AUD-USD	0.6575	0.67	0.68	0.69	0.70	0.71	0.72
USD-JPY	148.15	145	144	141	138	135	132
EUR-USD	1.0853	1.09	1.11	1.13	1.14	1.15	1.16
GBP-USD	1.2703	1.26	1.27	1.28	1.29	1.30	1.30
NZD-USD	0.6090	0.62	0.62	0.62	0.63	0.63	0.63
AUD Exchange Rates:							
AUD-USD	0.6575	0.67	0.68	0.69	0.70	0.71	0.72
AUD-EUR	0.6057	0.61	0.61	0.61	0.61	0.62	0.62
AUD-JPY	97.40	97.2	97.9	97.3	96.6	95.9	95.0
AUD-GBP	0.5175	0.53	0.54	0.54	0.54	0.55	0.55
AUD-NZD	1.0792	1.08	1.11	1.11	1.11	1.13	1.14

	2021	**2022**	**2023 (f)**	**2024 (f)**
GDP, %	5.4	2.3	1.4	1.6
CPI (Headline), %	3.5	7.8	4.3	3.2
CPI (Trimmed mean), %	2.6	6.8	4.4	3.2
Unemployment Rate, %	4.7	3.5	3.8	4.5
Wages Growth, %	2.4	3.3	4.1	3.2

AUD cross exchange rates have been rounded.

Financial forecasts are quarter end.

GDP, CPI, employment and wage growth forecasts are year end.

Contact Listing

Chief Economist
Besa Deda
dedab@banksa.com.au
+61 404 844 817

Senior Economist
Pat Bustamante
pat.bustamante@banksa.com.au
+61 468 571 786

Senior Economist
Jarek Kowcza
jarek.kowcza@banksa.com.au
+61 481 476 436

Economist
Jameson Coombs
jameson.cooombs@banksa.com.au
+61 401 102 789