# June Monthly Economics and Markets Review

QUEENSLAND TREASURY CORPORATION

## Overview

### Domestic economy

The RBA surprised by increasing rates at its June policy meeting, with commentary from RBA Governor Lowe suggesting the Board would not tolerate higher inflation persisting. Meanwhile, the Fair Work Commission delivered an increase to the award and minimum wages that was stronger than many had expected. Data released in June showed a small increase in GDP in Q1, a slowdown in inflation in May as well as a rebound in labour market conditions in May.

### International economy

It was a mixed story internationally, with some central banks increasing the pace of tightening, others pausing hikes and one even loosening policy. The OECD revised up its growth expectations, while moderating its inflation forecast for this year.

### Short-term interest rates

Front-end bond yields rose over the month as the RBA delivered a surprise rate increase. The three-year Australian Government Bond yield finished the month 60 basis points higher at around 4.03 per cent, trading above 4.00 per cent for the first time since 2011.

### Long-term interest rates

Longer-end bond yields also rose following the RBA decision, though less than those at the front end. The ten-year Australian Government Bond yield finished the month around 34 basis points higher at 4.02 per cent.

| MATURITY | ISSUER | YIELD | 1 MONTH BPS CHANGE | 1 YEAR BPS CHANGE |
|---|---|---|---|---|
| 3 Year | QTC | 4.31 | 55 | 81 |
| | Australian Government | 4.03 | 60 | 89 |
| | US Government | 4.53 | 48 | 167 |
| 5 Year | QTC | 4.26 | 47 | 53 |
| | Australian Government | 3.95 | 51 | 59 |
| | US Government | 4.16 | 40 | 128 |
| 7 Year | QTC | 4.37 | 39 | 44 |
| | Australian Government | 3.98 | 43 | 47 |
| | US Government | 3.99 | 29 | 108 |
| 10 Year | QTC | 4.60 | 31 | 44 |
| | Australian Government | 4.02 | 34 | 39 |
| | US Government | 3.84 | 19 | 96 |

| AUSTRALIAN DOLLAR CROSSES | RATE | 1 MONTH % CHANGE | 1 YEAR % CHANGE |
|---|---|---|---|
| AUD/USD | 0.6655 | 2.8% | -1.7% |
| AUD/EUR | 0.6100 | 0.5% | -6.4% |
| AUD/GBP | 0.5235 | 0.3% | -7.2% |
| AUD/JPY | 96.1992 | 6.4% | 5.1% |

| MAJOR CURRENCIES | RATE | 1 MONTH % CHANGE | 1 YEAR % CHANGE |
|---|---|---|---|
| EUR/USD | 1.0910 | 2.3% | 5.0% |
| GBP/USD | 1.2713 | 2.6% | 5.9% |
| USD/JPY | 144.55 | -3.5% | -7.0% |
| USD/CNY | 7.2538 | -2.1% | -8.2% |

*Prices sourced from Macrobond & QTC and are correct at the time of publication*

The tables above show yields on bonds issued by the Queensland, Australian and US Governments as well as values for the Australian Dollar against a range of currencies and US Dollar against major currencies. The change in yields and exchange rates over different time periods are also included.

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# Domestic economy

## SUMMARY:

The RBA delivered a second consecutive surprise rake hike in June with the Minutes to the meeting suggested the decision was again a close call.

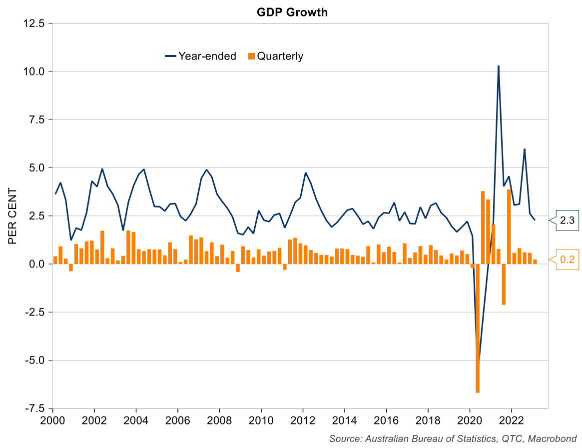
## REVIEW:

- The RBA increased the cash rate by 25-basis points to 4.1 per cent at its June meeting, an outcome which was at odds with the expectations of most economists and market pricing. The Bank acknowledged the lift in award and minimum wages and reiterated that *'unit labour costs are also rising briskly, with productivity growth remaining subdued.'* On inflation, it removed the comment that *'medium term inflation expectations remain well anchored'*. The Bank continues to note that *'some further tightening of monetary policy may be required to ensure that inflation returns to target in a reasonable timeframe'*. However, this phrase was not evident in the more detailed Minutes to the June meeting with these suggesting that the decision to hike rates was *'finely balanced'*.
- Speaking the day after the June meeting, RBA Governor Lowe indicated *'the desire to preserve the gains in the labour market does not mean that the Board will tolerate higher inflation persisting'.* Lowe stated the Board could not just *'sit idle'* given these risks to inflation and that *'there is a limit to how long inflation can stay above the target band',* opining that the Board's patience on inflation *'has a limit'.*
- RBA Deputy Governor Bullock suggested the labour market remains tight, but that supply-demand imbalances have improved somewhat. On this Bullock cited an increase in net arrivals from overseas (more supply) and a moderation in the post-pandemic recovery (less demand). On the relationship between inflation and employment, she stated that the RBA has been '*willing to accept a somewhat more gradual return of inflation to target*' as a faster return 'would mean more job losses in the short term'.
- The Fair Work Commission announced a 5.75 per cent increase for the nations' 2.6 million workers on award wages. It also lifted the minimum wage and adjusted classifications that will result in an 8.6 per cent pay rise for 180,000 workers. These increases were firmer than widely expected.
- It was also a busy month for data:
  - GDP rose 0.2 per cent over Q1 2023 to be 2.3 per cent higher over the year. Household consumption slowed further, dwelling investment declined, and net exports were a drag on growth, though business investment and government spending were solid.
  - The labour cost of producing a unit of output was up almost eight per cent over the year. Outside of a spike during COVID, this is the fastest growth since Q3 1990. A key factor behind this has been the collapse in productivity with growth in output per hours worked down 4.5 per cent over the year, the weakest on record (data back to 1979).
  - According to the ABS' monthly CPI report the annual rate of headline inflation slowed to +5.6 per cent in May (from +6.8 per cent in April). However, much of the moderation was driven by volatile fuel and holiday travel prices. Core measures moderated too, though by less. The trimmed mean CPI dipped to +6.1 per cent (from +6.7 per cent) and the CPI excluding volatile items and travel eased by only one-tenth to +6.4 per cent.
  - Employment increased by 75,900 in May, following a small decline in April. Similarly, the unemployment rate dipped to 3.6 per cent after having increased from 3.5 per cent to 3.7 per cent in the prior month. The reversal could in-part reflect issues flowing from the survey period for the ABS' April *Labour Force Survey* falling entirely during the Easter break. Abstracting from statistical noise, this month's report showed that Australian labour market conditions remain firm. Reinforcing this, both the participation rate and the employment-to-population ratio reached record highs on the month.
  - Job vacancies fell for a fourth consecutive quarter in the three-months to May, however despite the recent weakness the level of job vacancies remains historically elevated at around 90 per cent above pre-pandemic February 2020 levels.
  - Consumer confidence was marginally higher in June according to the *Westpac-Melbourne Institute Consumer Sentiment Survey.* The mixed result likely reflected the combination of key factors (the Fair Work Commission wage decision and RBA rate rise) have offsetting impacts on consumer perceptions. Unemployment expectations also rose to its highest level since September 2020, an outcome which if sustained points to upwards pressure for the unemployment rate in the months ahead.
  - Both business conditions and confidence as measured in the *NAB Business Survey* fell in May. This as forward orders also declined, and capacity utilisation dipped.

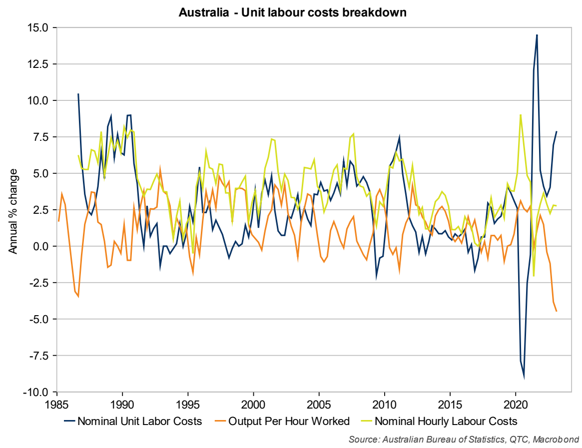
## WHAT TO WATCH:

The RBA's next policy meeting on 4 August will be key to understanding the Board's appetite for future rate hikes. Beyond this, the Q2 CPI (released 26 July) and June Labour Force Survey (20 July) will be key to monitor.

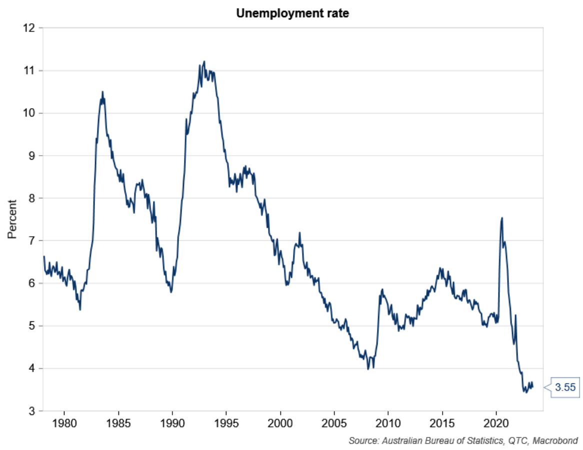
### CHART 1: DOMESTIC GDP GROWTH HAS SLOWED OVER THE PREVIOUS FEW QUARTERS




### CHART 2: THE LABOUR COST OF PRODUCING A UNIT OF OUTPUT IN AUSTRALIA IS INCREASING DUE TO A COLLAPSE IN PRODUCTIVITY




### CHART 3: THE UNEMPLOYMENT RATE REMAINS NEAR 48-YEAR LOWS



# International economy

### SUMMARY:

It was a particularly busy month for central banks globally, with some delivering further rate hikes, others pausing policy tightening and one even loosening policy.

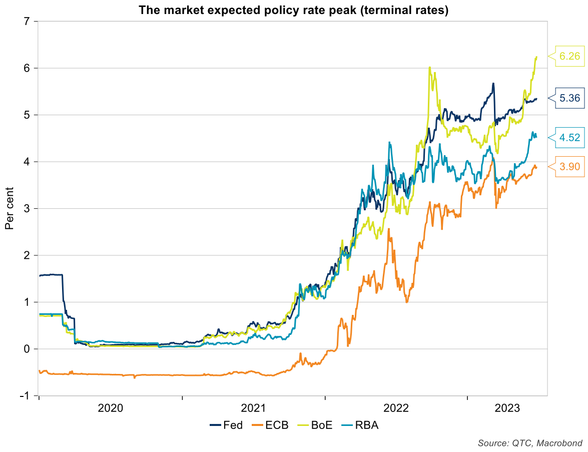
### REVIEW:

- The FOMC, the policymaking arm of the US Federal Reserve, kept rates unchanged at its June meeting, with the Fed Funds Target Rate range at 5.0 to 5.25 per cent. This follows ten consecutive rate hikes for a cumulative 500 basis point increase. There were few edits to the post-meeting statement though there were notable changes to participants' forecasts. Updates to participants' forecasts pointed to a more constructive near-term view for the economy with 2023 expectations for GDP growth revised higher and those for them unemployment taken lower. Meanwhile, the resilience in core inflation was acknowledged with forecasts for this marked higher. On interest rates, the FOMC 'Dot Plot' revealed that the median expectation for this year was lifted to 5.625 per cent. This is 50 basis points higher than the current rate. In the post-meeting press conference Chair Powell highlighted that views on rates were upped due to slow progress in getting core inflation down. He also said slower hikes made sense with rates now closer to their likely peak.
- The ECB lifted rates by 25 basis points to 3.5 per cent with its President, Christine Lagarde, flagging a further increase at its July meeting. The hike was accompanied by upwards revisions to core inflation forecasts, but few changes were made to the GDP outlook. The prospect of higher inflation and an economy resilient to rate hikes was interpreted by markets and economists as the ECB flagging that it can take rates even higher. So far, the ECB has lifted rates by 400 basis points in this hiking phase with the level of rates now the highest since 2001.
- The Bank of England surprised the market by lifting rates by 50-basis point to 5.0 per cent, The Monetary Policy Committee citied a significant upside surprises in recent inflation data as well as a persistently tight labour market and continued resilience in demand.
- The Bank of Canada lifted rates by 25-basis points to 4.75 per cent, bringing to a surprise end the Bank's *'conditional pause'* which began in January 2023. In justifying the decision, the post-meeting statement noted *'underlying inflation remains stubbornly high'* and that policy was not sufficiently restrictive to align supply and demand and return inflation sustainably to the two per cent target.
- In other major central bank news, the central banks of Norway (the Norges Bank) increased rates by 50-basis points, while those for Sweden and Switzerland did so by 25 basis points.
- The Bank of Japan voted unanimously to maintain its ultra-easy monetary policy, as was widely expected (though there was an outside chance of a surprise policy adjustment).
- Meanwhile, as China's post-pandemic economic recovery appears to be stalling, the People's Bank of China cut the one-year and five-year Loan Prime Rates by 10-basis points. These cuts follow the Bank's decision the prior week to cut the seven-day reverse repo rate and medium-term lending facility rate.
- The OECD revised up its global GDP growth forecast for 2023 by one-tenth to +2.7 per cent. Outside of the 2020 pandemic period, this is the lowest annual rate since projected since the GFC. Growth is then forecast to pick-up to +2.9 per cent in 2024. Global headline inflation is expected to ease from 7.8 per cent in 2022 to 6.1 per cent over 2023 and then 4.7 per cent in 2024. The moderation in inflation is driven by lower food and energy prices.
- President Biden signed an agreement early in June to suspend the US debt ceiling through 2024 and limit federal spending for two years, averting a US debt default.
- Data over the month were mixed, with inflation easing in the US and euro area though it picked up the UK. Euro area growth was disappointing, with a downward revision to Q1 2023 GDP implying that the bloc was in a 'technical' recession over the northern winter.

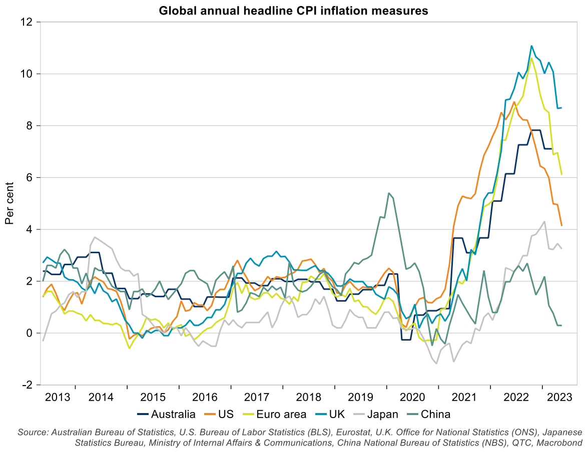
### WHAT TO WATCH:

There are some signs of a moderation in global price pressures, though these are not yet uniform as to their size, composition, and geography. Greater uniformity in this will be likely needed for central banks to feel comfortable that interest rates have increased sufficiently.

### CHART 3: MAKRET PRICING IS FOR FURTHER RATE INCREASES FROM THE FED, ECB, BOE AND RBA




### CHART 4: HEADLINE INFLATION APPEARS TO HAVE PEAKED GLOBALLY…




### CHART 5: … WHILE CORE INFLATION REMAINS MUCH STICKIER (PARTICULARLY IN THE UK)