August Monthly Economics and Markets Review

QUEENSLAND TREASURY CORPORATION

Overview

Domestic economy

The RBA kept policy settings unchanged at its August meeting, with the market split on what the Bank would do heading into the meeting. Though despite this, the Bank again suggested that *'some further tightening of monetary policy may be required to ensure that inflation returns to target in a reasonable timeframe.'*

Data over the month were mixed, with some weakness in the labour market.

International economy

Developments in China took centre stage over the month, with weaker economic data resulting in the People's Bank of China easing policy conditions. Elsewhere, inflation conditioned to moderate across advanced economies, though underlying inflation is proving to more sticky.

Short-term interest rates

The three-year Australian Government Bond yield started the month around 3.75 per cent. Rates initially rose as the RBA maintained its tightening bias, briefly trading around 4.0 per cent, before softer data (both domestically and offshore) saw yields decline into the end of the month to finish largely unchanged.

Long-term interest rates

Meanwhile longer-end bond yields followed a similar pattern, with the ten-year Australian Government Bond yield starting the month around 4.0 per cent, before trading up above 4.3 and then ultimately finishing the month little changed.

MATURITY	ISSUER	YIELD	1 MONTH BPS CHANGE	1 YEAR BPS CHANGE
3 Year	QTC	4.07	-9	42
	Australian Government	3.79	-9	52
	US Government	4.55	11	113
5 Year	QTC	4.13	-4	37
	Australian Government	3.82	-2	44
	US Government	4.25	12	96
7 Year	QTC	4.32	-3	40
	Australian Government	3.94	0	45
	US Government	4.20	12	94
10 Year	QTC	4.64	-1	51
	Australian Government	4.06	1	47
	US Government	4.11	7	92

AUSTRALIAN DOLLAR CROSSES	RATE	1 MONTH % CHANGE	1 YEAR % CHANGE
AUD/USD	0.6472	-2.2%	-4.6%
AUD/EUR	0.5967	-1.0%	-12.6%
AUD/GBP	0.5110	-1.5%	-13.2%
AUD/JPY	94.2566	-0.6%	-0.8%

MAJOR CURRENCIES	RATE	1 MONTH % CHANGE	1 YEAR % CHANGE
EUR/USD	1.0847	-1.2%	9.2%
GBP/USD	1.2666	-0.7%	9.9%
USD/JPY	145.63	-1.6%	-4.0%
USD/CNY	7.2587	-1.2%	-5.1%

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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FUNDING AND MARKETS DIVISION
Economic Research

Ryan Millar
T: 07 3842 4907
E: rmillar@qtc.com.au

HAVE A QUESTION?
Ask our economist

QUEENSLAND TREASURY CORPORATION
GPO Box 1096 Brisbane Queensland 4001
T: 07 3842 4600 www.qtc.com.au

Domestic economy

SUMMARY:

The RBA again kept rates on hold at its August meeting to allow more time to assess the impact of previous moves. It again noted that some further tightening may be required.

REVIEW:

- The RBA left the cash rate steady at 4.1 per cent at its August meeting. Expectations were split heading into the meeting, with 18/30 economists surveyed by *Bloomberg* expecting a 25-basis point hike while markets factored in a 30 per cent chance of a move. The post-meeting statement noted holding rates unchanged in August *'will provide further time to assess the impact of the increase in interest rates to date and the economic outlook'*, while noting that the four percentage points of tightening to date is *'working to establish a more sustainable balance between supply and demand in the economy and will continue to do so'*. The forward guidance was broadly unchanged, again suggesting that *'some further tightening of monetary policy may be required'*.
- The Minutes to that meeting suggested the decision to hold rates at 4.1 per cent reflected signals inflation was *'heading in the right direction'* and the labour market *'might be at a turning point'*. The Minutes noted policymakers again debated keeping rates unchanged or hiking by 25-basis points, ultimately concluding the argument for holding steady rates *'was the stronger one'*. However, the Minutes again suggested *'it was possible that some further tightening of monetary policy might be required'*.
- The RBA released its quarterly Statement on Monetary Policy. The Statement reiterated the Bank's tightening bias, *noting 'some further tightening of monetary policy may be required'*. The Statement also showed the Bank's forecasts for growth, inflation and the labour market were broadly unchanged from those in the previous update in May.
- Governor Lowe gave a final testimony before Parliament his term ends this month. Lowe reiterated the RBA's tightening bias but suggested the Bank was in a *'calibration phase'* as it assesses the impact of prior tightening on spending and inflation. The Governor suggested the Bank could return inflation to its two-to-three per cent target by 2024 if it delivered an additional 100-basis points of hikes, but that it was comfortable being more patient and having inflation return to target by 2025.
- The July *Labour Force Survey* was softer than expected as employment fell by 14,600. This is the second decline in the last four months, though the ABS suggested seasonal volatility may have impacted the July outcome. The unemployment rate rose two-tenths to 3.7 per cent, despite the participation rate easing one-tenth to 66.7 per cent. Meanwhile, on a more positive note, hours worked lifted over the month, even with the fall in employment, as hours worked per employee continued to rise.
- The Wage Price Index (excluding bonuses) rose +0.8 per cent in Q2, with the annual growth rate easing one-tenth to 3.6 per cent (against expectations it would be unchanged). The details showed private-sector wages growth increased +0.8 per cent (+3.8 per cent year-on-year), while public-sector wages growth rose +0.7 per cent (+3.1 per cent year-on-year). By industry, 11 of 18 industries saw a rise in the pace of annual wage growth. Fewer workers than usual received a pay rise this quarter, but for those that did, the size of the increase was higher than previously.
- The ABS's monthly read on inflation eased to +0.25 per cent in July (from +0.7 per cent in June) to be 4.9 per cent higher over the year (was +5.4 per cent). The details of the report showed much of the deceleration was driven by a decline in volatile categories such as holiday travel and accommodation, fruit and vegetables, and fuel. Looking through the volatility, the CPI excluding volatile items and holiday travel measure eased by slightly a more moderate three-tenths to +5.8 per cent year-on-year.
- The *NAB Business Survey* for July showed that conditions eased slightly, while confidence improved. Labour costs accelerated strongly following the increase in minimum and award wages at the start of the new financial year. Meanwhile *NAB* noted there was some evidence of firms passing through wage costs into higher prices.
- The *Westpac-Melbourne Institute Consumer Sentiment Index* fell in August, with key components mixed. Consumer's outlook for the labour market improved slightly, with unemployment expectations falling.

WHAT TO WATCH:

Key data to watch in the period ahead include the Q2 GDP report (6 September), the monthly Labour Force Survey (14 September) and the Q3 CPI release (25 October). In addition, current RBA Deputy Governor Michele Bullock will take over as Governor on 18 September. While this isn't expected to impact policy materially, the change in leadership along with the Bank implementing some of the findings of the RBA Review could see some shift in its communication.

CHART 1: EMPLOYMENT IN JULY FELL THE MOST SINCE SEPTEMBER 2020, THOUGH SEASONAL ISSUES MAY HAVE DISTORTED THE RESULT

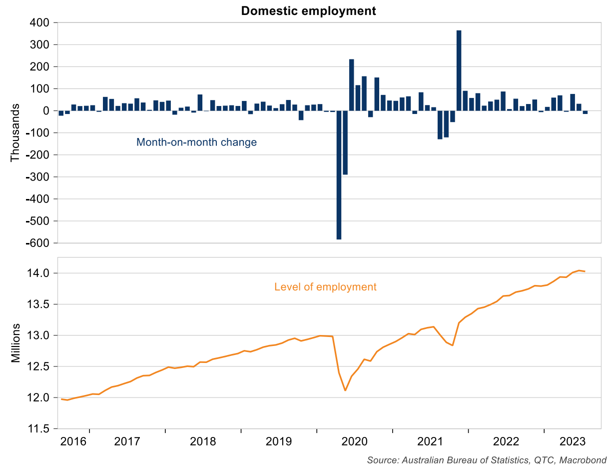


CHART 2: THE ANNUAL PACE OF WAGES GROWTH EASED A LITTLE IN Q2, BUT REMAINS NOTABLY ABOVE AVERAGE

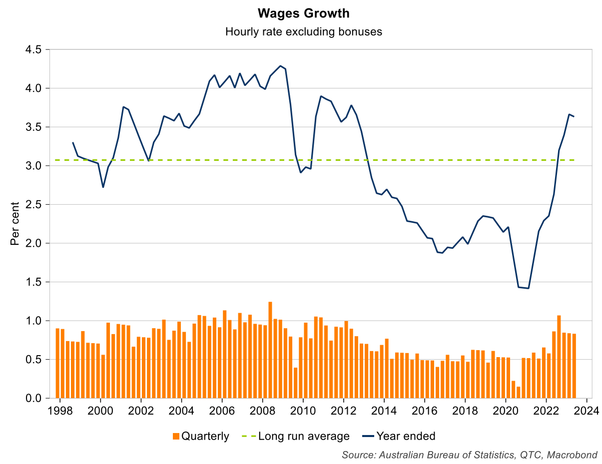
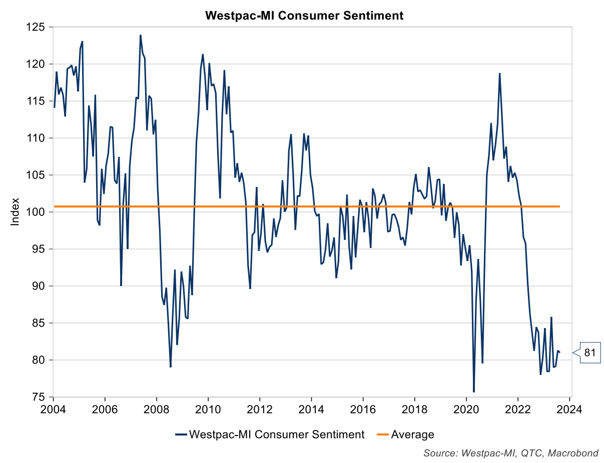


CHART 3: THE *WESTPAC-MELBOURNE INSTITUTE CONSUMER SENTIMENT INDEX* IS ~20 PER CENT BELOW THE LONG-TERM AVERAGE...



International economy

SUMMARY:

It was another particularly busy month for central banks globally with divergent policy outcomes across nations. Economic momentum in China continued to soften and in response, authorities there proceeded to roll-out further policy easing measures.

REVIEW:

- In **global central bank** news:
  - There were some divergent views from Fed officials on the policy outlook. Some suggested rates needed to be raised further while others believe there is no need for additional hikes. Various members argued the next decision is an open question and that policymakers need to be guided by the data.
  - Following a 50-basis point increase at its previous meeting, the Bank of England lifted rates by 25-basis points to 5.25 per cent. The Bank remains concerned about persistent price pressures and retains a tightening bias.
  - The Bank of Japan kept policy rates unchanged, but somewhat surprised the market by also allowing greater flexibility around its 10-year Japanese Government Bond yield target, allowing it to move up to a yield of 1.0 per cent (rather than 0.5 per cent). This is the second widening of the band around the yield target in the last seven months.
  - The People's Bank of China stated Chinese banks should lift corporate lending to boost economic growth and promote consumption. The Bank also called for adjustments to home lending, though did not elaborate further on any policy incentives. Over the month the Bank reduced the Medium-term Lending Facility rate by 15 basis points (to 2.5 per cent), while cutting the one-year Loan Prime Rate (LPR) by 10 basis points (to 3.45 per cent) and leaving the five-year LPR unchanged at 4.20 per cent.
- In **US** related news:
  - The Fed's Senior Loan Officer Survey revealed tightening lending standards and weaker demand across commercial, industrial, consumer and real estate loans. Meanwhile, the regional Dallas Fed's *Banking Conditions Survey* for August showed US loan volumes again declined, though at a slower pace relative to recent months.
  - Credit rating agency *Fitch* downgraded its assessment of the US, from "AAA" to "AA+". In justifying the decision, the agency pointed to an expected fiscal deterioration over the coming years, a high and growing government debt burden, and the *'erosion of governance'* relative to peers that has culminated in repeated debt limit standoffs.
  - The annual pace of US inflation continues to moderate, though some core measures (particularly with relation to services) appear sticky. The US labour market is mixed. While monthly payroll growth was the weakest since late 2020 and job openings declined for a second month, both outcomes remain at historically very strong levels.
- In data outside of the US:
  - **Chinese** activity data for July disappointed already low expectations with annual growth in retail sales, industrial production, fixed asset investment as well as property investment and property sales easing further. The unemployment rate rose one-tenth to 5.3 per cent. Credit growth was lacklustre, import and export growth fell notably in July due to weaker internal and external demand as well as base effects. Meanwhile, the annual rate of headline consumer inflation eased to -0.3 per cent year-on-year in July, from 0.0 per cent in June. The annual rate of producer inflation improved to -4.4 per cent year-on-year in July (from -5.4 per cent in June).
  - Both the **euro area** and **UK** saw consumer price inflation continue to ease for July and positive GDP growth for Q2.
  - **Japanese** inflation was mixed with the annual inflation rate picking up for some measures but moderating for others. Real GDP growth was much more than expected, however, the details were less positive with much of the upside surprise driven by strong net exports with domestic consumption and capital expenditure slowing.

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: INFLATION APPEARS TO HAVE PEAKED GLOBALLY…

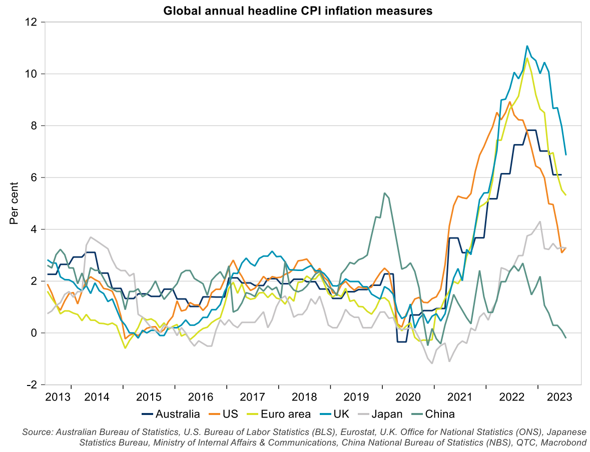


CHART 4: … THOUGH CORE INFLATION REMAINS STICKIER

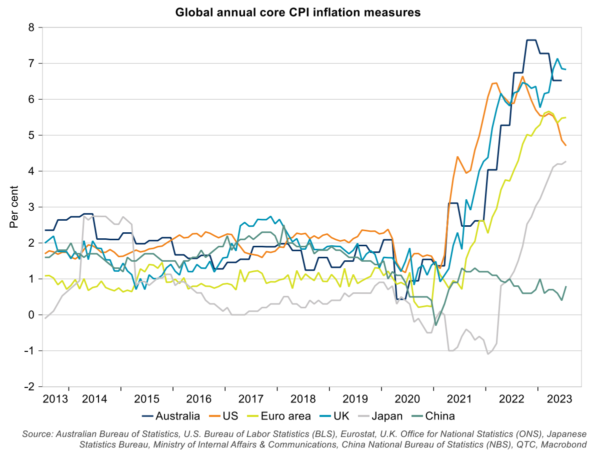


CHART 5: US JOBS GROWTH HAS SLOWED