June Monthly Economics and Markets Review

QUEENSLAND TREASURY CORPORATION

Overview

Domestic economy

Despite further signs that the economy is slowing, the process of inflation having seemingly stalled. The persistence of inflation and upside risks to it are increasingly of concern to the RBA. A strong monthly CPI outcome for May was taken by the market as a strong sign that further rate hikes might be needed, though the Q2 CPI report will be the deciding factor.

International economy

June was a month of action from central banks, either actual or prospective. Some begun lowering rates (for example, those in Canada and the euro area) while noting that further cuts would be data dependent. The US Federal Reserve is in a similar boat in terms of monitoring inflation when deciding the timing and extent of its easing cycle. Favourable inflation developments in the US in June have investors considering that this could begin in the coming months. Finally, other central banks guided that policy settings might be loosened (Bank of England) or tightened (Bank of Japan) in coming months.

Interest rates

Bond yields fell in the first week of June due to a weaker than expected ISM manufacturing report (with little respite from better-than-expected service sector conditions), softer details in the core PCE inflation data, lower US job openings as well as the Bank of Canada lowering interest rates. Yields were then up and down in the second week of the month, rising early in the week alongside similar moves in European markets as investors became concerned about an increase in risk following the snap election called by French President Macron. Weaker-than-expected outcomes for core CPI and PPI in the US helped push yields lower over the rest of the week, though this was partially offset by what were considered hawkish revisions to interest rate guidance from FOMC participants. Yields then rose in the third week of the month on a mixed set of news and data before increasing more forcefully in the final week of June on a stronger than anticipated May CPI report for Australia.

MATURITY	ISSUER	YIELD	1 MONTH BPS CHANGE	1 YEAR BPS CHANGE
3 Year	QTC	4.37	6	23
	Australian Government	4.08	12	22
	US Government	4.55	-24	2
5 Year	QTC	4.47	3	37
	Australian Government	4.07	9	29
	US Government	4.38	-26	22
7 Year	QTC	4.69	2	47
	Australian Government	4.17	7	35
	US Government	4.37	-26	38
10 Year	QTC	5.02	1	55
	Australian Government	4.31	5	44
	US Government	4.40	-22	56

AUSTRALIAN DOLLAR CROSSES	RATE	1 MONTH % CHANGE	1 YEAR % CHANGE
AUD/USD	0.6686	1.0%	0.5%
AUD/EUR	0.6241	1.9%	2.3%
AUD/GBP	0.5289	1.6%	1.0%
AUD/JPY	107.5396	3.1%	11.8%

MAJOR CURRENCIES	RATE	1 MONTH % CHANGE	1 YEAR % CHANGE
EUR/USD	1.0712	-1.0%	-1.8%
GBP/USD	1.2641	-0.6%	-0.6%
USD/JPY	160.85	-2.1%	-11.3%
USD/CNY	7.2673	-0.3%	-0.2%

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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HAVE A QUESTION?
Ask our economist

Domestic economy

SUMMARY:

Despite further signs that the economy is slowing, the process of inflation having seemingly stalled. The persistence of inflation and upside risks to it are increasingly of concern to the RBA. A strong monthly CPI outcome for May was taken by the market as a strong sign that further rate hikes might be needed, though the Q2 CPI report will be the deciding factor.

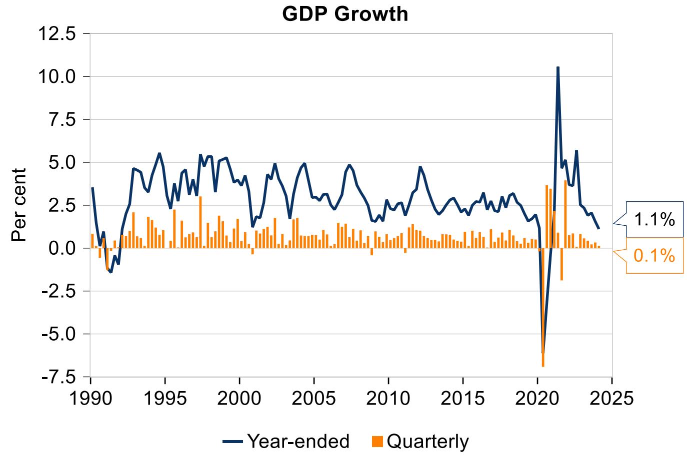
REVIEW:

- On monetary policy, the RBA kept the cash rate at 4.35 per cent in June:
  - The post-meeting statement painted the picture of a mixed to slowing economy continuing to be impacted by persistent inflation with risks to future price outcomes skewed to the upside.
  - The RBA retained its neutral forward guidance by indicating that '*the path of interest rates that will best ensure that inflation returns to target in a reasonable timeframe remains uncertain and the Board is not ruling anything in or out*.' Though, in talking about the Board being resolute in its determination to return inflation to target, the statement also added that it '*…will do what is necessary to achieve that outcome*'.
  - On the economy, the RBA suggested that since the last forecast update in May, '*there have been indications that momentum in economic activity is weak'* and that recent data have been '*mixed*'.
  - On inflation, the RBA changed the heading of the section of this topic from '*inflation remains high and is falling more gradually than expected*' to '*inflation remains above target and is proving persistent*'. It also highlighted that '*the revisions to consumption and the saving rate and the persistence of inflation suggest that risks to the upside remain*'.
  - In the post-meeting press conference RBA Governor Bullock noted that, '*We need a lot to go our way to get inflation in the 2-3 per cent target range*' and that '*We still think we're on the narrow path [though] … the narrow path is getting narrower*'.
  - In parliamentary testimony RBA Governor Bullock pointed out that, given the lags of monetary policy, it is possible that there are 50 basis points worth of tightening still to flow through to the economy. Meanwhile, in a speech, RBA Assistant Governor (Financial Markets) Christopher Kent, indicated that the range of models maintained by the Bank suggested that the neutral interest rate was estimated to be around 3.5 per cent.
- GDP rose by just 0.1 per cent in Q1 2024 with the annual rate of growth slowing from 1.6 per cent to 1.1 per cent, the slowest rate of expansion since the early 1990s recession. With population growth again exceeding that in production, output shrank on a per capita basis. This was the fifth straight quarter that this has happened (a record). Household consumption rose in Q1, but it was revisions to previous outcomes which captured attention. Here the ABS marked its estimates of household consumption higher over the past year as spending by inbounded tourists was reincorporated. While this paints a more constructive picture of consumption (the annual growth rate nearly doubled after the change), GDP was not affected as higher consumption was offset by higher imports.
- While the headline CPI fell 0.08 per cent in May, annual growth lifted to 4.0 per cent. This was above economists' expectations of 3.8 per cent which marked the third straight month that this has happened. In seasonally adjusted terms, the headline measure rose 0.24 per cent in May, the same as in April, to be up 4.1 per cent over the year. The monthly rate of core inflation (excluding volatile items and travel prices) rose 0.24 per cent on the month to be up 4.05 per cent over the year. In seasonally adjusted terms, core inflation accelerated from 0.24 per cent to 0.33 per cent.

WHAT TO WATCH:

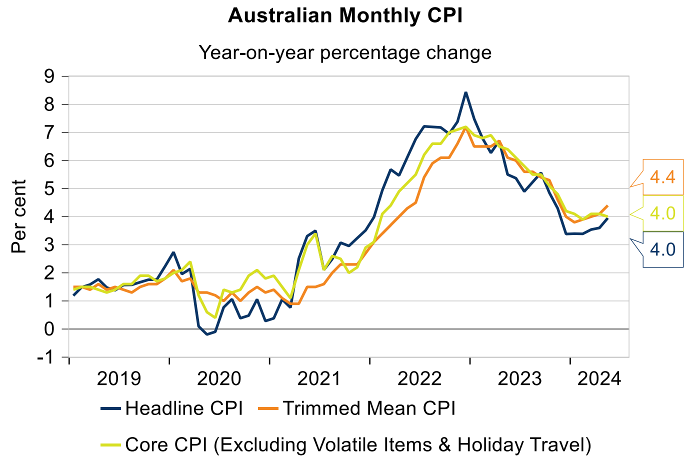
While markets have to some degree run ahead of the data by extrapolating recent firm monthly inflation outcomes ahead of the more widely focussed on quarterly CPI print, RBA Governor Bullock was quite clear in trying to divert attention from the former to the latter and noted that the quarterly release will provide an '*important*' marker for the Bank to get a sense of the trajectory for inflation. It is due in the final week of July.

CHART 1: THE ANNUAL RATE OF GDP GROWTH IN AUSTRALIA JUST REACHED THE SLOWEST PACE SINCE THE EARLY 1990S RECESSION



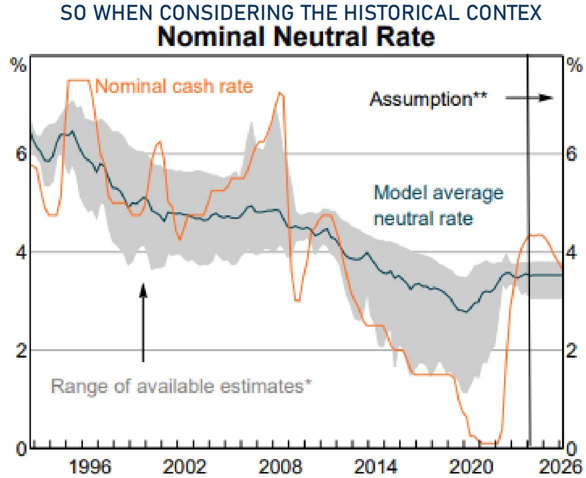
Source: Australian Bureau of Statistics, Reserve Bank of Australia, QTC, Macrobond

CHART 2: THE PERSISTENCE OF INFLATIONARY PRESSURES WAS EVIDENT WHEN LOOKING AT ANNUAL RATES IN MAY



Source: Australian Bureau of Statistics, QTC, Macrobond

CHART 3: THE RBA'S ESTIMATES OF THE NOMINAL NEUTRAL RATE SUGGEST THAT CURRENT POLICY SETTINGS ARE RESTRICTIVE BUT NOT ESPECIALLY SO WHEN CONSIDERING THE HISTORICAL CONTEX



* Range of central estimates corresponding to available models. Nominal neutral rates are defined using trend inflation expectation.

** The nominal cash rate assumption is based on market pricing for overnight indexed swaps (OIS) on June 24, 2024.

Sources: LSEG; RBA.

International economy

SUMMARY:

June was a month of action from central banks, either actual or prospective. Some begun lowering rates (for example, those in Canada and the euro area) while noting that further cuts would be data dependent. The US Federal Reserve is in a similar boat in terms of monitoring inflation when deciding the timing and extent of its easing cycle. Favourable inflation developments in the US in June have investors considering that this could begin in the coming months. Finally, other central banks guided that policy settings might be loosened (Bank of England) or tightened (Bank of Japan) in coming months.

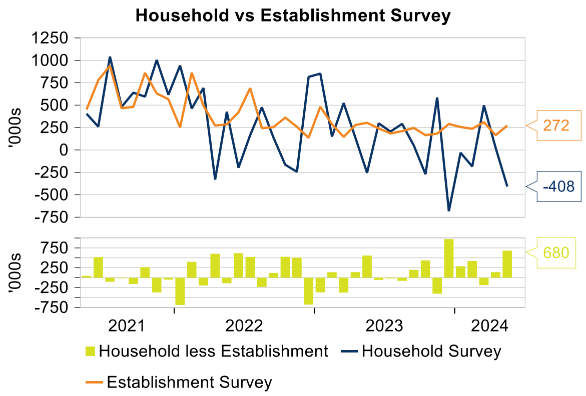
REVIEW:

- In the **US**, the US economy added 272,000 jobs in May according to the Establishment Survey. This was 92,000 more than expected and a very different outcome to the 408,000 drop in employment as per the Household Survey. The unemployment rate increased one-tenth to 4.0 per cent.
- In **China**, annual growth in industrial production and fixed asset investment were lower than expected in May. Conditions in the property sector remain weak with ongoing contraction in floor space sold and under construction, new home starts and completions as well as overall real estate investment and dwelling prices. In contrast, retail sales were firmer than anticipated.
- On **inflation**:
  - In the US, the monthly increase in core CPI in May was less than expected and the smallest since August 2021. Core PCE inflation increased by less than expected in May and there were further encouraging signs of moderation in the pace of market-based price changes.
  - In the euro area, the annual rate of both headline and core inflation rose more than expected in May. Services prices continue to grow strongly.
- In **central bank** news,
  - The Federal Reserve's FOMC left the target range for the federal funds rate unchanged at 5.25-5.5 per cent at its June meeting, with the Committee acknowledging that there has been '*modest progress*' towards the two per cent inflation objective in recent months. FOMC participants revised their outlook for the federal funds rate with the median now suggesting only one rate cut this year (versus three beforehand). However, an additional rate cut is now foreseen for 2025 and 2026 such that the cumulative change in the policy rate over the entire period is the same as before.
  - The Bank of Canada cut interest rates by 25 basis points to 4.75 per cent in what was its first move in this easing phase of the policy cycle. Further cuts could be forthcoming if inflationary pressures continue to ease.
  - As expected, the European Central Bank (ECB) delivered its first rate cut in the easing phase of its policy cycle by lowering the deposit rate by 25 basis points. This reflected actual progress on lowering inflation and some additional confidence in its forecasts that this process would continue. However, while cutting rates, the Governing Council removed the easing bias that was introduced at the April meeting. This seemingly reflected some ongoing caution about the moderation in inflation.
  - The Bank of England kept rates on hold at its June meeting. A day prior, while annual headline and core inflation for May slowed as expected, the moderation in services prices was less pronounced. Members of the Bank's Monetary Policy Committee suggested that this '*somewhat higher*' than forecast outcome was impacted by annual price resets in come items and volatile movements in others. Also pointing in the 'dovish' direction were comments that, for those members which elected to vote for no change, their decision was '*finely balanced*'. The Bank also noted that the MPC would re-assess things as part of the next forecasting round in August. This was interpreted that a rate cut will be on the table at that meeting.
  - The Bank of Japan also kept rates on hold but indicated future tightening. For example, it flagged that an announcement would be forthcoming at its July meeting around the monthly pace of Japanese Government Bond purchases. The Governor flagged that this reduction could be '*meaningful*'.

WHAT TO WATCH:

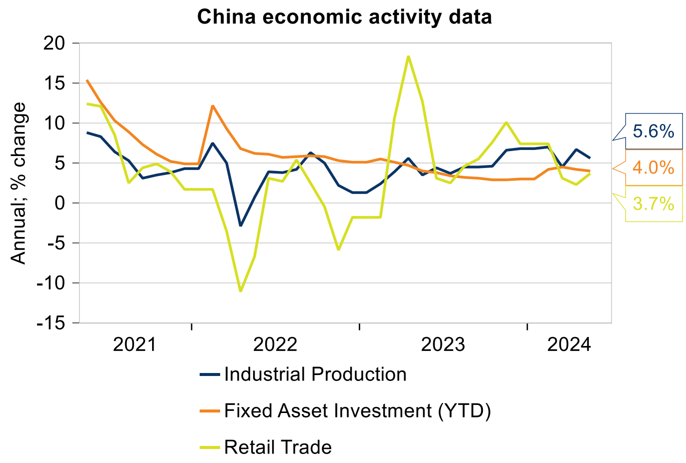
With an increasingly broad array of central banks now lowering interest rates, attention will shift squarely for more concrete signs from the US Federal Reserve as to when it will start to cut rates and how extensive this process will be.

CHART 4: THERE WAS AN UNUSUALLY LARGE GAP IN SERIES MEASURING US EMPLOYMENT GAINS IN MAY



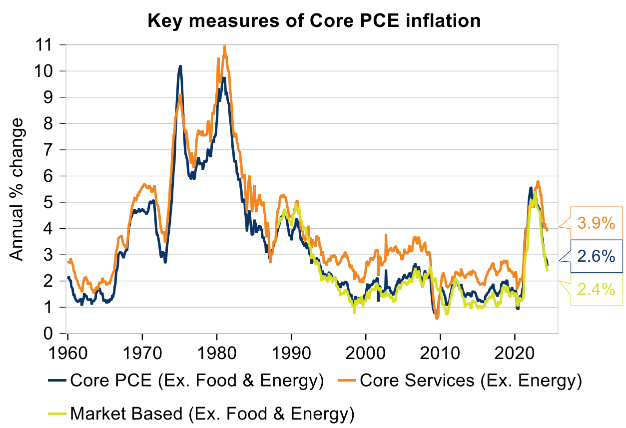
Source: U.S. Bureau of Labor Statistics (BLS), QTC, Macrobond

CHART 5: READINGS ON CHINESE ECONOMIC ACTIVITY WERE MIXED IN THE DATA FOR MAY



Source: China National Bureau of Statistics (NBS), QTC, Macrobond

CHART 6: SLOWING MONTHLY RATES OF CORE PCE INFLATION IN THE US ARE GIVING INVESTORS ADDITIONAL COMFORT THAT THE FED WILL BE ABLE TO GET INFLATION BACK TOWARD TARGET IN A REASONABLE TIMEFRAME SUCH THAT RATE CUTS MAY SOON BE FORTHCOMING



Source: U.S. Bureau of Economic Analysis (BEA), QTC, Macrobond