December Monthly Economics and Markets Review

QUEENSLAND TREASURY CORPORATION

Overview

Domestic economy

Measures of consumer and business confidence weakened according to data released in December. This implies softness in the economy, something that was evident in the Q3 GDP outcome, though not in labour market data for November. Ongoing resilience in the labour market may make it harder for the RBA to cut interest rates in the near-term. However, dovish shifts in the Bank's communications over the month certainly indicate a willingness to consider such a move.

International economy

Political developments dominated headlines in December, though of more relevance to markets, the trend toward further easing by central banks remains intact – so much so that now there is an even split between major central banks around the world lowering rates and those keeping them on hold. Chinese officials flagged a greater sense of urgency in terms of the prospective policy support to be provided.

Interest rates

Australian Government three-year yields fell nine basis points in December while 10-year yields rose three basis points. Yields dipped early in December following a softer than expected reading on US service sector conditions and Q3 GDP report for Australia. Stronger-than-expected Australian labour market data and the US Federal Reserve signalling that the pace of interest rate cuts in 2025 is likely to be slower than previously indicated then saw yields rise over the balance of the month. Yields then fell again into year-end.

MATURITY	ISSUER	YIELD	1 MONTH BPS CHANGE	1 YEAR BPS CHANGE
3 Year	QTC	4.05	-13	18
	Australian Government	3.82	-9	22
	US Government	4.27	18	19
5 Year	QTC	4.29	-8	35
	Australian Government	3.93	-4	29
	US Government	4.38	33	47
7 Year	QTC	4.62	-3	45
	Australian Government	4.14	0	36
	US Government	4.48	37	54
10 Year	QTC	5.05	1	59
	Australian Government	4.35	3	40
	US Government	4.57	40	64

AUSTRALIAN DOLLAR CROSSES	RATE	1 MONTH % CHANGE	1 YEAR % CHANGE
AUD/USD	0.6218	-3.5%	-7.4%
AUD/EUR	0.5976	-3.0%	-3.0%
AUD/GBP	0.4955	-3.0%	-6.8%
AUD/JPY	97.6265	1.1%	1.3%

MAJOR CURRENCIES	RATE	1 MONTH % CHANGE	1 YEAR % CHANGE
EUR/USD	1.0406	-0.5%	-4.6%
GBP/USD	1.2549	-0.6%	-0.7%
USD/JPY	157.00	-4.8%	-9.4%
USD/CNY	7.2991	-0.4%	-2.6%

Prices sourced from Macrobond and QTC 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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Ask our economist

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Domestic economy

SUMMARY:

Measures of consumer and business confidence weakened according to data released in December. This implies softness in the economy, something that was evident in the Q3 GDP outcome, though not in labour market data for November. Ongoing resilience in the labour market may make it harder for the RBA to cut interest rates in the near-term. However, dovish shifts in the Bank's communications over the month certainly indicate a willingness to consider such a move.

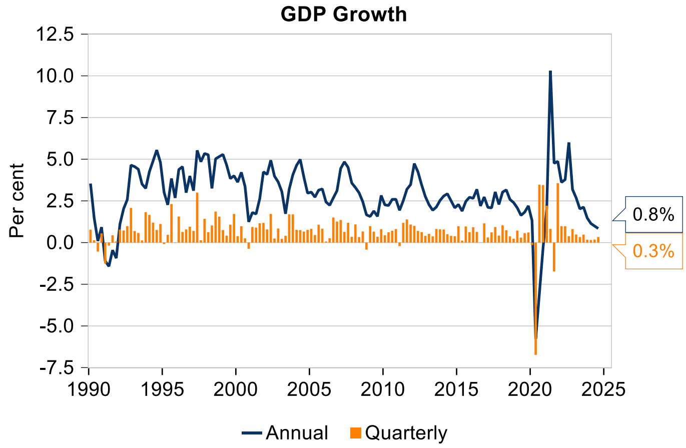
REVIEW:

- The **RBA** held the cash rate steady at 4.35 per cent in December as widely expected. However, the commentary accompanying the decision shifted to be more dovish. The Board noted that it is '*gaining some confidence that inflation is moving sustainably towards target*', with some of the upside risks to inflation having eased. Governor Bullock also acknowledged that some of the recent data on the real economy has been soft and that the Board's views are evolving. This became even clearer in the Minutes to the Board meeting which saw an easing bias introduced. Specifically, it was noted that '*if the future flow of data continued to evolve in line with, or weaker than, their expectations, it would further increase their confidence that inflation was declining sustainably towards target. If that were to occur, members concluded that it would, in due course, be appropriate to begin relaxing the degree of monetary policy tightness*.'
- Ahead of the RBA meeting, the national accounts showed that **GDP** lifted 0.3 per cent in Q3 to be 0.8 per cent higher over the year. This was below consensus expectations and indicates that economic growth remains subdued. Illustrating this, GDP per capita has contracted for seven straight quarters. Regarding the drivers of growth:
  - For the second straight quarter, the private sector made zero contribution to GDP growth with the public sector instead driving virtually all the growth (though part of this reflects state and federal government electricity rebates shifting expenditure from the household sector to the public sector).
  - Real household disposable income growth improved due to Stage 3 income tax cuts. However, the response of consumers was muted, with household consumption remaining flat in the quarter.
  - Business investment decreased in Q3, while dwelling investment and net exports contributed positively to GDP growth.
- The **labour market** was stronger-than-expected in November with the unemployment rate falling two-tenths to 3.9 per cent against market expectations for it to increase to 4.2 per cent. The decline was due to both stronger-than-expected employment growth (+35,600) and a decline in the participation rate. Other favourable indicators in the *ABS Labour Force Survey* included the employment-to population ratio rising one-tenth to 64.4 per cent, the highest level on record, and the underemployment rate falling one-tenth to 6.1 per cent, its lowest since April 2023.
- The **NAB Business Survey** suggests that economic activity eased in November with a dip in business conditions and sharp fall in business confidence. Forward orders also declined and remains well below its long-run average. NAB's measure of price pressures have gradually trended lower, though the pace of improvement has slowed.
- According to the Westpac-Melbourne Institute, **consumer sentiment** fell two per cent in December. Consumers were more downbeat on the outlook compared to November, with both the 12-month and 5-year ahead outlook sub-indexes unwinding around half of the rally seen over the previous two months.

WHAT TO WATCH:

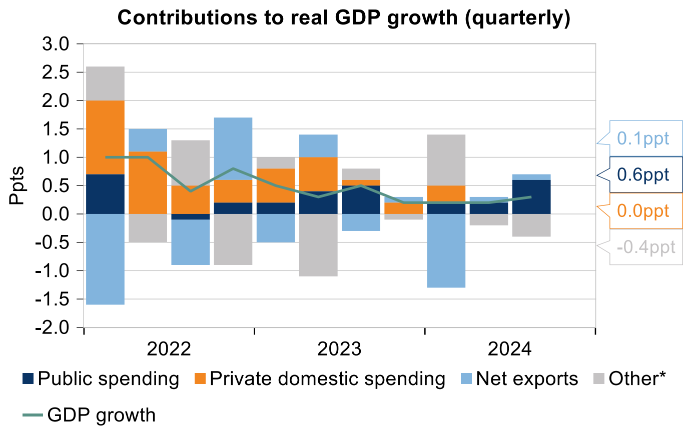
The RBA has flagged that the Q4 CPI report (due out late January) is likely to be on the soft side. This alone may be enough for it to cut rates in February, though the Board will also be very keen to see if the resilience observed in the November Labour Force Report is repeated in the December edition (due out in mid-January). A repeat of that outcome could make communicating the rationale for a February rate cut challenging for the Bank. A reversal in the unemployment rate back to being on an upward trend would however make justifying a rate cut an easier proposition.

CHART 1: ANNUAL GDP GROWTH SLOWED TO 0.8%, WHICH (OUTSIDE OF THE PANDEMIC) IS ITS SLOWEST PACE SINCE THE 1990S RECESSION



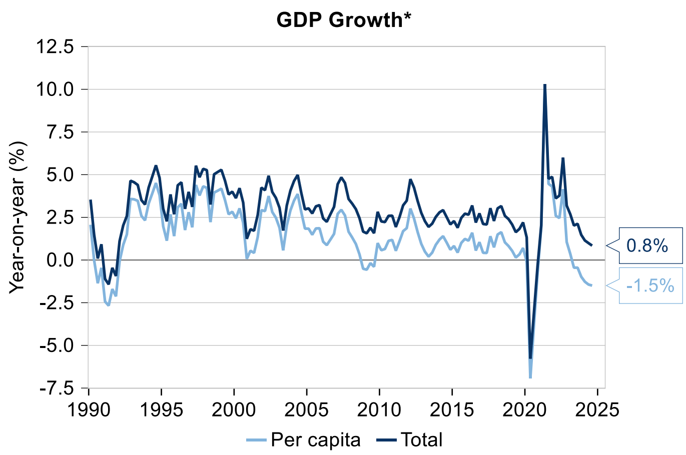
Source: Australian Bureau of Statistics, Reserve Bank of Australia, QTC, Macrobond

CHART 2: GROWTH CONTINUED TO BE SUPPORTED BY STRONG PUBLIC SPENDING, WITH PRIVATE DEMAND REMAINING FLAT IN THE QUARTER



** Includes inventories and the statistical descrepency*
Source: Australian Bureau of Statistics, QTC, Macrobond

CHART 3: ON A PER CAPITA BASIS, GDP HAS NOW FALLEN FOR SEVEN CONSECUTIVE QUARTERS



Source: Australian Bureau of Statistics, QTC, Macrobond

International economy

SUMMARY:

Political developments dominated headlines in December, though of more relevance to markets, the trend toward further easing by central banks remains intact – so much so that now there is an even split between major central banks around the world lowering rates and those keeping them on hold. Chinese officials flagged a greater sense of urgency in terms of the prospective policy support to be provided.

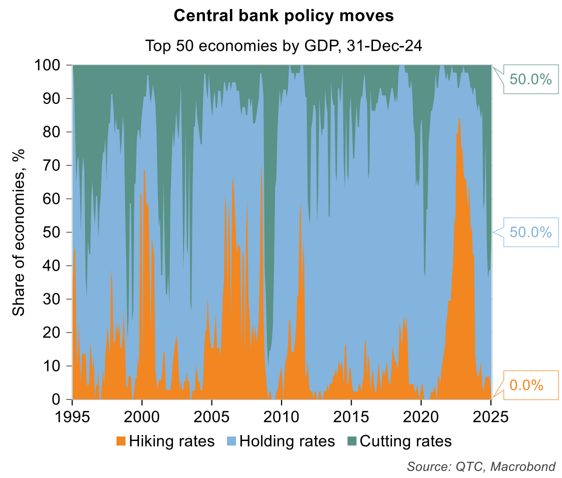
REVIEW:

- There were notable **political** developments in France and South Korea.
  - In France, Prime Minister Barnier's government has been toppled after just three months in power after a no-confidence vote triggered by Barnier using a special measure of the French Constitution to pass a social security bill. President Macron appointed a new PM, Francois Bayrou, whose priority will be to pass a budget. The need to consolidate the country's finances (the budget deficit is expected to be twice EU-mandated levels) in a fractious political environment means the new PM faces an uphill battle.
  - South Korea's President Yoon Suk Yeol invoked martial law on 3 December in response to 'anti-state forces', with the aim being to halt political activities, ban strikes by labour groups, and control media content. The declaration was voted down by Yoon's own party and the opposition with the President ultimately impeached. Less than a fortnight later his replacement was also impeached after refusing to promptly appoint judges to fill vacancies on the bench of the constitutional court set to determine the legality of the impeachment of Yoon.
- In **China**, the post-meeting statement following the December Politburo meeting pointed towards more stimulus being provided. For example, it called for '*more proactive fiscal policy*' (vs '*proactive fiscal policy*'); for '*moderately loose*' monetary policy (vs '*prudent*' monetary policy, a characterisation which had been in place since 2011); to '*vigorously boost consumption, improve the investment efficiency, and expand domestic demand on all fronts*' (new); and to strengthen 'unconventional counter-cyclical policy adjustments' (new).
- Several **central banks** cut interest rates including:
  - The US Federal Reserve by 25 basis points to 4.25-4.50 per cent. In doing so a slower pace of cuts over the coming year was flagged. The median outlook for the Fed funds rate from FOMC members was revised higher, with members now only seeing two 25 basis point rate cuts in 2025 (from four previously and three expected). Chair Powell said that while monetary policy is still restrictive, the Fed funds rate is getting closer to 'neutral'.
  - The Bank of Canada (BoC) cut its policy rate by 50 basis points to 3.25 per cent, marking its second consecutive 50 basis point cut. The BoC has now reduced interest rates by 175 basis points since June.
  - The European Central Bank cut its key policy rates by 25 basis points, with the post meeting statement indicating the possibility of further cuts in coming months, albeit perhaps at a slightly slower pace.
  - The central banks of Switzerland (-50 basis points to 0.50 per cent), Denmark (-25 basis points to 2.60 per cent) and Sweden (-25 basis points to 2.50 per cent) all cut interest rates.
- Other **central banks** held rates including the Bank of Japan at 0.25 per cent, the Bank of England at 4.75 per cent (though policymakers were split 6-3 on whether to cut) and Norway's central bank at 4.50 per cent.
- Highlights of **US economic data** released in December were that the ISM services index fell from 56 in October (well below market expectations) to 52.1 in November. The decline was underpinned by weaker outcomes for new orders and employment. Non-farm payrolls rose 227k in November and the unemployment rate edged one-tenth higher to 4.2 per cent.

WHAT TO WATCH:

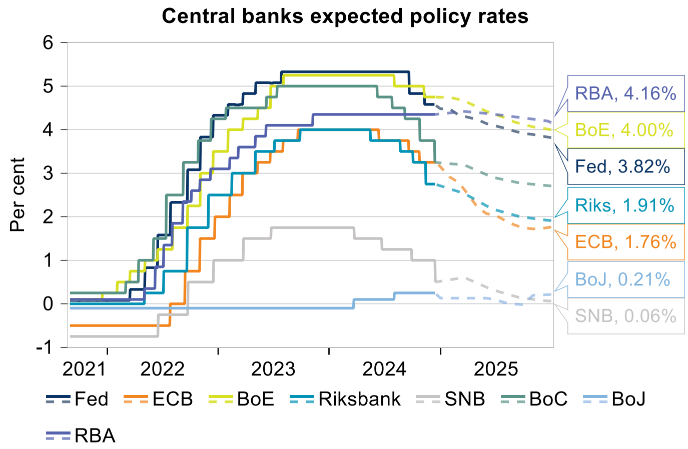
The Politburo meeting highlighted more urgency from Chinese policymakers. Some initial ideas around the types of support measures that may be forthcoming were flagged at the Central Economic Work Conference during the month. However, further details on these, the budget deficit needed to fund them as well as the GDP growth target these are in service of, will be revealed in the National People's Congress in March. This will be a key to focus on.

CHART 4: THERE IS A 50-50 SPLIT IN THE ACTIONS OF MAJOR GLOBAL CENTRAL BANKS BETWEEN HIKING AND HOLDING



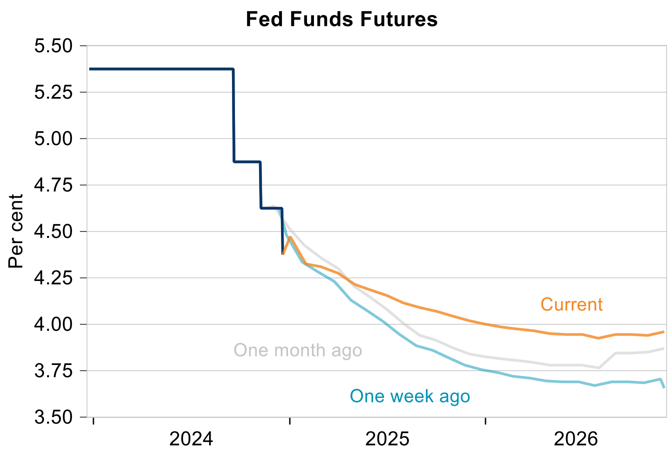
Source: QTC, Macrobond

CHART 5: GLOBAL CENTRAL BANKS CONTINUE TO CUT INTEREST RATES, THOUGH THE PACE OF RATE CUTS IS EXPECTED TO SLOW OVER THE COMING YEAR



Source: QTC, Macrobond

CHART 6: IN THE US, EXPECTATIONS FOR THE FED FUNDS RATE SHIFTED HIGHER IN RESPONSE TO THE FED SIGNALING A SLOWER PACE OF INTEREST RATE CUTS OVER THE COMING YEAR



Source: Bloomberg, QTC, Macrobond