Australia & New Zealand weekly.

Week beginning 17 June 2019

- Notes from Europe: the cost of quantitative easing.
- RBA: Minutes, Governor Lowe speaking on the labour market.
- Australia: Westpac–MI Leading Index, AusChamber–Westpac business survey.
- NZ: Westpac McDermott Miller Consumer Confidence, Q1 GDP, current account.
- Europe: EU Summit, ECB Sintra conference, consumer confidence.
- US: FOMC policy decision.
- Central banks: BOJ and BOE policy decisions.
- Flash PMIs for Japan, Europe and the US.
- Key economic & financial forecasts.

Information contained in this report current as at 14 June 2019.

Westpac Institutional Bank

Notes from Europe: the cost of quantitative easing

Over the last two weeks, I have been visiting institutional investors, real money managers, and hedge funds in Europe and London.

There has been extraordinary interest in the Australian story on this visit. Westpac has received considerable credit for its views over the last eighteen months. A year ago, when market pricing and most commentators, including the central bank, signalled higher rates, Westpac took a strong stand that rates would remain on hold. Customers also recognised that Westpac was the first of their advisers to predict rate cuts – a forecast made back in February this year.

Whilst it is understandable that Australia is of interest at the moment due to the RBA being "in-play", it is also important to note that many institutional investors see the Australian dollar as an integral part of their investment portfolios. Investors support Australia because it still provides relatively high yields, deeply liquid markets, competitive pricing, and reliable research.

In my discussions, I highlighted the evolution of the approach to policy from the RBA. This started with the RBA Governor's view late last year that household debt was a bigger threat to the Australian economy than a long period of low inflation. His approach to policy was that while rates were on hold for the time being, the next move in rates was likely to be up.

Around the end of last year, when the housing market deteriorated more rapidly than expected and GDP growth slowed abruptly, there were clearly second thoughts emerging in the RBA. That culminated in a speech in February in which the Governor indicated that rates could either rise or fall. This was an important signal for Westpac, since for some time we had suspected that the RBA did not think rate cuts would be particularly effective. Clearly that approach had changed. Shortly after the speech, Westpac shifted to forecasting two rate cuts, in August and November 2019.

RBA rhetoric then switched to highlighting the 'tension' between the labour market data and the GDP (and other spending partials) data. Westpac pointed out that this tension could be resolved by noting that employment in cyclical parts of the labour market was indeed in decline, and the overall employment figures were holding up due to government spending driven sectors including health and education. In late May, the Governor finally switched his target towards stimulating the labour market, indicating more could be done to drive the unemployment rate down from its current 5.2% with the NAIRU also being seen as lower than the previously assessed 5% (later confirmed as being closer to 4.5%).

That switch in policy objectives was confirmation of our view that rates were about to fall, and given that the RBA's current forecasts, which incorporate two rate cuts, were for a 5% unemployment rate this year and next, only ticking down to 4.75% by mid 2021, we expected that more than two cuts were going to be required. Today our view holds that two more cuts will be delivered in August and November – a total of three cuts for 2019.

By far the most interesting discussions with those customers who closely follow the RBA rate cycle is what action is likely to follow the move to a 0.75% cash rate target. Westpac's view has been that the risks to that forecast are to the downside, although we do anticipate a more constructive economic environment in 2020 as the housing market stabilises; fiscal policy plays a more stimulatory role; and the global economy improves following two FOMC rate cuts in 2019, the impending US election also motivating the US President to play a less disruptive role.

We also speculated that if the RBA saw a continuing need to stimulate the economy, it would embrace some form of quantitative easing (QE) rather than drive the cash rate below that 0.5–0.75% range seen as the likely floor beyond which the transmission to lending rates becomes ineffective.

There were a range of opinions from customers about the appropriateness of QE for Australia. Coming from a European base, these customers held that the challenges facing Australia were totally different to those faced by the ECB and the BoE, where credit conditions and liquidity were the major constraints on the economy.

One view was that Australia's flexible exchange rate could be expected to play the constructive role, unlike say a country like Italy where the necessary exchange rate flexibility was not possible. This argument pointed to the preferable policy being to drive interest rates down to 0% and rely on the currency reaction to deliver the bulk of the stimulus. In fact, the general view in Europe was that negative interest rates were mainly beneficial through the currency rather than any response from the banking system.

A second view questioned the process of moving from interest rate cuts to quantitative easing. The most likely form of quantitative easing, as we have discussed, is for the RBA to provide cheap long-term funding to banks secured by mortgages registered with the RBA under the Committed Liquidity Facility. This policy was questioned since, as we have discussed, the signal that the transmission from lower rates was not working would come through the banks' muted response to interest rate cuts. Customers questioned whether it would be a politically viable policy to switch to QE, which would effectively be supporting the banks with low cost funding. Naturally, as we have seen in the UK and Europe, these facilities would be tied to new lending, but with around 80% of mortgages in Australia linked to a variable rate, the real transmission effect should come from lower rates on existing mortgages rather than new loans. This policy approach was assessed by these customers as being overly ambitious.

Finally, there was a view that QE has a range of unintended and unpredictable costs. Such a policy should only be adopted when a credit crisis has emerged. It should not be adopted as a form of stimulus, particularly when the stimulus is aimed at chasing a NAIRU that cannot be known in advance. Evidence around the world indicates that NAIRUs are much lower than anticipated, with the US unemployment rate of 3.6% still not generating clear wage pressure. This criticism is questioning the link between unemployment, wages and inflation. For Australia, perhaps, the better lead indicator for policy should be the response of the housing market. Ironically, that implies RBA policy would be reverting back to where we were a year ago, when the most important aspect of economic welfare related to household debt and housing markets.

Clearly, we find ourselves at a very interesting stage of policy. While we are aware that the RBA has done considerable work on quantitative easing, certainly during the GFC period, sensible people are warning that the practicality and the unknown costs of quantitative easing policies do not justify their use when the target is not credit and liquidity but instead chasing an uncertain NAIRU.

I also addressed the European Securitisation Conference and noted that a further dimension to QE would be the RBA buying asset backed securities issued by non-banks. The response of a number of issuers was surprising. They claim that unnecessarily driving down the rates on these assets would disadvantage them with other investors and therefore not be welcomed. That theme is a clear example of the so–called hidden costs of quantitative easing.

Secondly, banks receiving extensive low cost funding from the RBA would therefore restrict their support for their traditional funding markets, be they wholesale or retail depositors. Temporarily moving away from traditional funding sources, which still remain available, may be an appropriate example of the costs that QE creates in a well–functioning financial system.

Conclusion

Westpac remains comfortable with its forecast that there will be two more rate cuts in August and November. In 2020, the risks are to the downside for another cut. We see that 0.5–0.75% as the effective policy floor. The issue of whether the RBA moves into a 'QE–mode' beyond that floor will be a very difficult one for them to consider. It is not our central view that QE will be adopted, and certainly, some of the arguments discussed above are significant themes that the RBA will be considering should it see the need for further stimulus next year.

I will now be away for a few weeks but will continue to watch closely as these fascinating markets continue to challenge us.

Bill Evans, Chief Economist

The week that was

This week, updates for business conditions and consumer sentiment as well as the labour market highlighted how challenging Australia's outlook is. Offshore, US trade relations and geopolitical tensions remained in focus ahead of the FOMC's June meeting.

For the business sector, this was the first post-election reading for the NAB business survey, with interviewing beginning on 20 May, straight after the poll. Confidence certainly rallied on the election result and ahead of the June RBA cut, rising 7pts to +7 – a level just above the long-run average. By state and industry, the lift in sentiment was broad based with the exception of manufacturing, where sentiment was little changed. The two subsequent RBA rate cuts we see in August and November will provide support for confidence hence. However, this easing is occurring because the economy is weak. On this point, business conditions actually deteriorated in May, falling 2pts to +1 – a level well below the long-run average. The election may have biased this outcome down as elections can create a lull in new orders and activity while the sector awaits the result. That said, the weakness in conditions was broad based across the states and industry, and is consistent with other partial data to hand.

Turning to the consumer sector, the Westpac-MI consumer sentiment index fell 0.6% to 100.7 in June despite the RBA rate cut. From the detail of the report, it is apparent that household finances remain under significant pressure. While there is an expectation that rate and tax cuts will provide relief, it is difficult to foresee this benefit having a meaningful impact on consumers' willingness to spend, with 'time to buy a major household item' well below average. A large portion of said benefit is instead expected to be saved, particularly if expectations around the labour market deteriorate.

On the housing market, price expectations certainly responded to the June rate cut and expectations of more to come. However, this index still remains well below average, and the response of 'time to buy a dwelling' to the rate cut was subdued versus history. This highlights that concerns over affordability and general uncertainty will remain lasting headwinds for housing.

Then to the labour market. The May labour force report was a real mixed bag. Employment exceeded expectations, rising 42k. However, hours worked contracted 0.3% in the month and the unemployment rate remained at 5.2%, the latter as a result of a further increase in participation. The important point to note here is that, if offset by an increase in participation, strong employment growth does nothing to reduce labour market slack. Notably, the underemployment rate (which measures the share of workers who are willing and able to work more hours) now sits at 8.6%, 1.1ppts above the level seen post-GFC.

This highlights the considerable challenge before the RBA as they seek to lift wages, and consequently GDP growth and inflation. To our call for two more rate cuts in this cycle, risks are clearly to the downside. While offshore in Europe and the UK, Westpac Chief Economist Bill Evans had extensive discussions with investors over these risks and the implications for policy, as detailed in this week's essay.

Looking offshore, our latest Market Outlook highlights the deterioration seen in trade and global growth over the past year, in large part because of US trade policy. This is a global headwind which is unlikely to dissipate anytime soon. While President Trump has "indefinitely suspended" his threat to tariff Mexico, we have since seen the President make new threats against Europe, while the US also continues to investigate other countries such as Japan and India. The good news is that monetary and fiscal policy can and will respond in the US and China respectively, and that these actions will most likely sustain robust growth. For Australia, the risk is that the two rate cuts we expect in the US to end-2019 reduce the effectiveness of the RBA's own policy easing, limiting the downward pressure lower Australian rates have on our dollar. We still believe that the Australian dollar will fall to USD0.66, but now not until the first half of 2020, after the FOMC halts rate cuts and as domestic risks to Australia's economy linger.

Chart of the week: Westpac Market Outlook

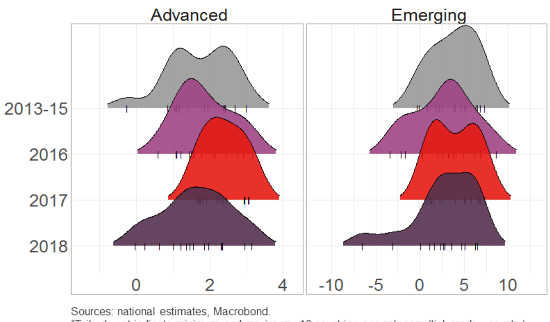
Our June Market Outlook provides our latest thinking on Australia, markets and the global economy.

Central banks and a reassessment of downsides risks to the globe from ongoing international trade tensions were key this month for markets. Against this backdrop, US and global bonds rallied sharply to fresh lows.

With that in mind, topics explored in this month's release are: the Australian national accounts, global growth and FX markets, the US-China trade dispute, and much more.

See here for the full report.

Density estimate of world growth



Sources: national estimates, Macrobond.
*Tails do not indicate minimum and maximum. 13 countries per category (tick mark = country).

Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.

New Zealand: week ahead & data wrap

The New Zealand economy has lost some steam with softness in both the household and business sectors. However, we expect to see economic growth starting to firm again through the back half of this year, supported by low interest rates and fiscal spending.

Some of the wind came out of the economy's sails in late 2018, and it looks like the pace of economic growth has remained subdued through the first half of this year. We're expecting next week's GDP report will show that the economy expanded by 0.6% in the March quarter following a similarly modest gain in December. That would see economic growth in the year to March slipping to 2.6% – its slowest annual pace since 2014.

Much of the recent softness in economic activity has been centred on the business sector. Although there's been a pick-up in food manufacturing, other manufacturing activity has been shrinking for three quarters now. We're also seen sluggish conditions in a number of service industries.

Moving into the June quarter, things aren't looking much better. The latest BusinessNZ PMI fell to 50.2 in May – its lowest levels since 2012 – with businesses reporting weakness in both production and orders.

There's also been softness in the household sector in recent months, with core (ex-fuel) retail spending essentially flat through April and May. In part, that's because high petrol prices have syphoned funds out of households' wallets, constraining spending in other areas. On top of that, weakness in the housing market has been dampening spending appetites in some regions, with spending on durable items broadly flat since November.

But while overall economic conditions are looking soft, there are still some bright spots. One of those is export earnings, with strong prices for a number of our key agricultural exports including meat and horticulture products. The other area of strength has been construction. Building activity rose by 6.2% in the first quarter of this year, with strong increases in both residential and non-residential work. Those increases have been widespread with particularly large gains in Auckland.

Putting all of this together leaves the economic landscape looking a bit soggy. However, as we head into the back half of the year, we expect to see economic growth starting to re-accelerate. Some of that will come on the back of continued increases in construction activity, with a large amount of residential and non-residential work consented over the past year. More generally, economic growth will also be boosted by low interest rates and increases in Government spending. Combined, those factors signal a broad-based boost to demand and employment.

One area where we expect to see a very noticeable turn around over the coming year is the housing market. That's coming on the back of two big changes in the economic environment. First is the Government's decision back in April to not proceed with its long touted plan to introduce a capital gains tax on investment properties. This was a flagship policy for the Government and, while it didn't get beyond the planning phase, its spectre had a significant dampening impact on investor demand. Now that the policy has been shelved, we expect a rapid improvement in market sentiment and a "relief rally" in prices.

The second big change which we expect to boost the housing market is the very sharp drop in mortgage rates since May. Wholesale fixed interest rates have plunged following the Reserve Bank's recent change of tack towards lowering the OCR. The consequence has been a near 40 basis point drop in the average two-year fixed mortgage rate. Two year fixed rates are now sixty basis points lower than a year ago. Five year rates have fallen even more sharply, and are now 120 basis points lower than a year ago. These declines have made housing more affordable for owner occupiers. They will also make the yields on investment housing look more attractive to investors, especially compared to bank deposits.

Together, we think those two changes portend a pickup in the housing market over the year ahead. We're forecasting nationwide house price inflation will rise from around 2% currently, to around 7% in 2020. And with New Zealanders holding a large proportion of their wealth in housing assets, this also signals a more general boost to household demand.

But while we are expecting a pickup in the nationwide housing market, we continue to expect some big regional differences. As we discuss in our recent Bulletin,[1] we expect Auckland will continue to under-perform relative to other regions, with a number of policies continuing to dampen investor demand in the region (including restrictions on foreign buyers).

We expect the boost to demand from the above policy changes will become evident through the back of this year, with a recovery in house sales likely to precede a lift in price growth. However, at least for now, the housing market remains soft. The May update from REINZ showed that sales remains low, especially in Auckland. Price growth also remains muted, with annual house price inflation running at 1.8% – a far cry from the rates of around 16% per annum that we saw in 2016.

One notable development in recent months has been the varied housing market trends across the country. Until recently, weakness was concentrated in Auckland and Canterbury, while prices in other regions had been powering ahead. However, we're now seeing signs that housing markets are cooling in other regions, with house price inflation slowing in Waikato, the Bay of Plenty, Gisborne/Hawke's Bay and Otago. We'll be watching to see if this continues over the next few months.

[1] Available here: https://www.westpac.co.nz/assets/Business/Economic-Updates/2019/Monthly-Files-2019/NZ-Home-Truths-June-2019.pdf

Round-up of local data released over the last week

Date	Release	Previous	Actual	Mkt f/c
Wed 12	Apr net migration	4630	4870	–
	May card spending	0.6%	–0.5%	0.5%
Fri 14	May REINZ house sales	0.2%	–0.2%	–
	May REINZ house prices, %yr	1.4%	1.8%	–
	May manufacturing PMI	52.7	50.2	–
	May food price index	–0.1%	0.7%	–

Data previews

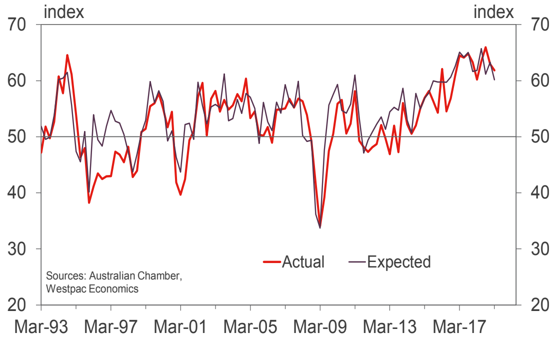
Aus Q2 AusChamber–Westpac business survey

Jun 18, Last: 61.8

- The Australian Chamber–Westpac survey of the manufacturing sector provides a timely update on conditions in the sector and insights into economy–wide trends.
- The Q2 survey was conducted after the May 18 Federal election, from May 20 to June 6.
- In Q1, the Actual Composite declined to 61.7 from 62.9 in December, extending the loss of momentum evident from around mid–2018. The Composite is supported by rising new orders, albeit at a slower pace, output, and order backlog.
- Confidence softened early in 2019, ahead of the election.
- Cross currents are impacting the sector. Negatives are around the housing downturn and spill–over effects from severe drought in NSW and Qld. Positives are the boost from the lower dollar and from the upswing in public infrastructure investment.

Westpac-AusChamber Composite indexes

Actual & expected, sa

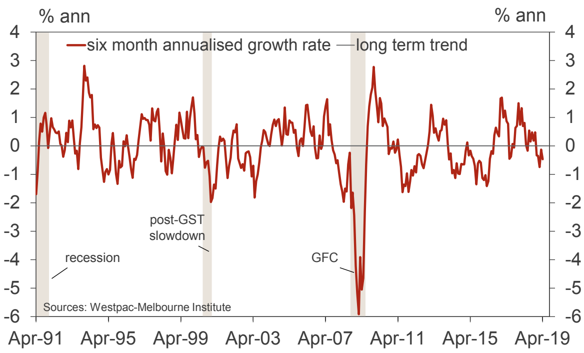


Aus May Westpac–MI Leading Index

Jun 19, Last: –0.47%

- The six month annualised growth rate in the Westpac–Melbourne Institute Leading Index, which indicates the likely pace of economic activity relative to trend three to nine months into the future, declined from –0.13% in March to –0.47% in April. The monthly move was mainly due to an unwinding spike in dwelling approvals, which fell 15% after a 19% jump the previous month. The underlying picture has been consistently negative over the last five months, a clear signal that economic growth through the three quarters of 2019 is likely to be below trend.
- The May update should show a similar story. Component updates will include slight positives around the ASX200 (up 1.1%) and commodity prices, up 2.5% (in AUD terms) but negatives across all other components.

Westpac-MI Leading Index

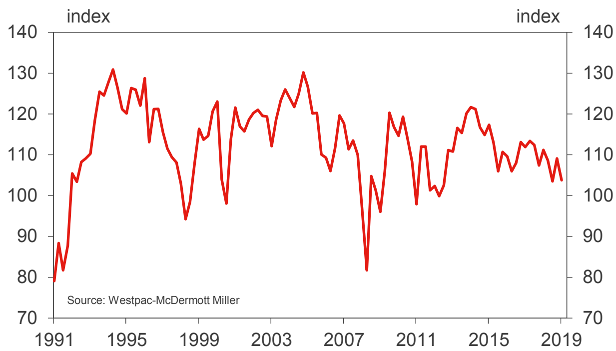


NZ Q2 Westpac McDermott Miller Consumer Confidence

Jun 18, Last: 103.8

- Consumer confidence fell to a below average level in the March quarter. Confidence was down across all income brackets, age groups and regions. Households noted increased concerns about their personal financial situation and the trajectory of the economy over the next few years.
- Since the time of the last survey, we've seen falls in mortgage rates. We've also seen the cancelation of the proposed capital gains tax and the announcement of increased fiscal spending as part of the Government's Well Being Budget.

Westpac-McDermott Miller consumer confidence



Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.

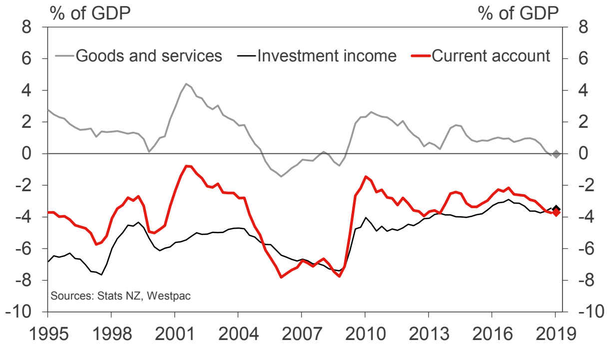
Data previews

NZ Q1 current account % of GDP

Jun 19, Last: –3.7%, Westpac f/c: –3.7%, Mkt f/c: –3.5%

- We expect the annual current account deficit to hold steady at 3.7% of GDP. This would leave the deficit at its widest since September 2013.
- The goods trade deficit improved marginally in the March quarter, with a strong lift in export volumes helping to offset lower dairy export prices and higher oil import prices.
- In contrast, we expect the balance on services to soften, reflecting the drop in tourist numbers. We also expect a widening in the investment income deficit, due to higher profits for overseas–owned firms.

Annual current account balance

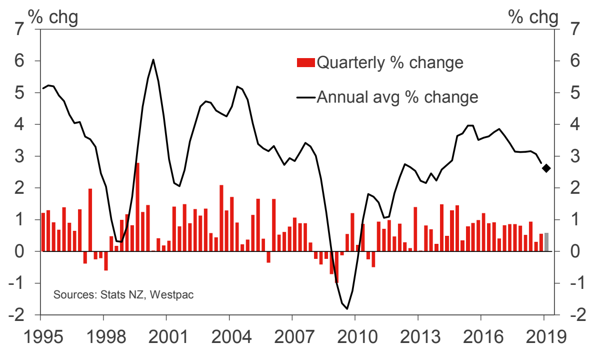


NZ Q1 GDP

Jun 20, Last: 0.6%, Westpac f/c: 0.6%, Mkt f/c: 0.5%

- We expect a 0.6% rise in the production measure of GDP for the March quarter, matching the average pace seen over the last year.
- A burst of construction activity enlivened what was otherwise shaping up to be a subdued quarter. Primary sector activity was mixed, and service sector growth has slowed noticeably in recent quarters.
- The RBNZ was already braced for a soft 0.4% result when it cut the OCR last month. A stronger outturn in line with our forecast would not take further rate cuts off the table, but would be enough to leave the RBNZ in watch and wait mode for now.

Production-based GDP

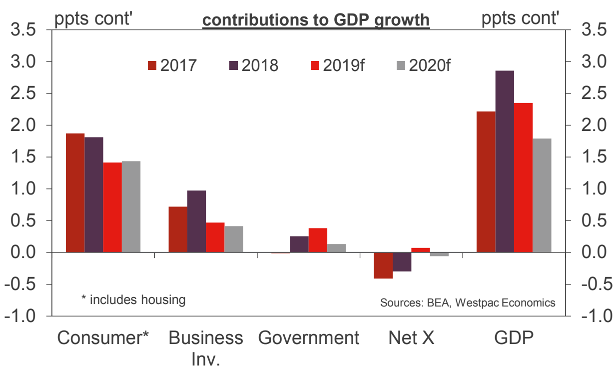


US June FOMC meeting

Jun 18–19, last 2.375%, WBC 2.375%

- Market participants clearly believe there is a need for the FOMC to respond to global uncertainty, and to do so quickly. Between now and Nov 2020, four cuts are priced in, with the first to come (on the market's expectation) in Jul.
- To occur, a material shift in FOMC communication has to be seen at the Jun meeting. Not only does the median fed funds rate expectation for 2020 and beyond have to shift from a hike to cuts, but the Committee's growth and inflation forecasts will have to be marked down materially.
- While mindful of the risks, as this threat to growth has only just started showing up in business investment, and given the consumer remains on a strong footing, we believe the Committee will limit the scale of its Jun revisions and try to buy time. We do anticipate rate cuts, but only two rather than the market's four, and likely not until Sep (then Dec).

Shock to US GDP from global tensions key



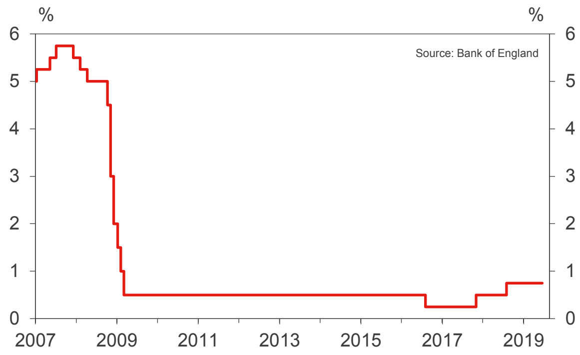
Data previews

UK Bank of England Bank rate

June 20, Last: 0.75%, WBC f/c: 0.75%, Mkt f/c: 0.75%

- The Bank of England left the bank rate on hold in May, but maintained its very modest (and Brexit dependent) tightening bias.
- We expect that the Bank Rate will again be left on hold at the June meeting. However, there is some risk that the BOE's rhetoric in the accompanying statement will become more hawkish. The recent weakness in the GBP will boost near term inflation. There have also been hawkish comments from several MPC members despite Brexit related headwinds and related softness in real activity.
- We remain circumspect about the strength of inflation pressures and expect an extended period of subdued GDP growth. As a result, we expect the BOE to remain on hold for the foreseeable future.

Bank of England Bank Rate



Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.

Key data & event risk for the week ahead

		Last	Market median	Westpac forecast	Risk/Comment
Mon 17					
NZ	May BusinessNZ PSI	51.8	–	–	Businesses continue to note a range of headwinds.
UK	Jun Rightmove house prices	0.9%	–	–	While still soft, the housing market has stabilised recently.
US	Jun Fed Empire state index	17.8	12.0	–	Manufacturing coming under greater pressure.
	Jun NAHB housing market index	66	67	–	Housing market supported by job gains and low rates.
	Apr total net TIC flows	–8.1	–	–	Treasuries remain in demand despite decline in rates.
Tue 18					
Aus	Q2 AusChamber–Westpac survey	61.8	–	–	Manufacturing conditions, a loss of momentum from mid–2018.
	RBA minutes	–	–	–	Colour re June rate cut decision & prospect for further cuts.
	RBA Kearns speaks	–	–	–	Head of Financial Stability in Canberra, 9:15 am.
NZ	Q2 WBC MM Consumer Confidence	103.8	–	–	The March survey recorded a widespread drop in confidence.
Chn	May new home prices	0.6%	–	–	Strong momentum in tier 2 and 3.
Eur	May core CPI %yr	0.8%	–	–	Fell back sharply post Easter boost.
	Jun ZEW survey of expectations	–1.6	–	–	Has stabilised but heightened trade disputes likely to weigh.
	ECB Sintra conference	–	–	–	ECB President Draghi and BOE Governor Carney speak.
US	May housing starts	5.7%	0.4%	–	Stabilisation evident in residential construction…
	May building permits	0.2%	0.8%	–	… though future growth likely to be modest.
Wed 19					
Aus	May Westpac–MI Leading Index	–0.47%	–	–	A negative read, pointing to sub–trend growth in coming qtrs.
NZ	Q1 current account % of GDP	–3.7%	–3.5%	–3.7%	Stronger dairy exports but weaker tourism.
UK	May CPI	0.6%	–	–	Core well contained, just below 2%.
US	FOMC policy decision, midpoint	2.375%	2.375%	2.375%	Forecasts and tone of press conference key.
Can	May CPI %yr	2.0%	–	–	Core inflation remains close to 2%.
Thu 20					
Aus	RBA Governor Lowe speaks	–	–	–	"The labour market & spare capacity", Adelaide, 11:15 AEST
	RBA Bulletin	–	–	–	RBA research articles.
NZ	Q1 GDP	0.6%	0.5%	0.6%	Construction surge enlivened an otherwise subdued quarter.
Jpn	BOJ policy decision	–0.1%	–	–	To emphasise dovishness but little room to move.
Eur	Jun consumer confidence advance	–6.5	–	–	Has been stabilising. Robust labour market a support.
	EU Summit	–	–	–	Key decisions to be made on EU Commission leadership.
	ECB bulletin	–	–	–	ECB research articles.
UK	May retail sales	–0.2%	–	–	Retailers have been reporting softness in demand.
	BoE policy decision	0.75%	0.75%	0.75%	Risk that the BOE's rhetoric becomes more hawkish.
	BOE Gov Carney speaking	–	–	–	Annual Mansion speech, text to be released.
US	Jun Phily Fed index	16.6	10.0	–	Manufacturing coming under greater pressure.
	Initial jobless claims	–	–	–	Still very low.
	May leading index	0.2%	0.1%	–	Pointing to growth around trend.
	Fedspeak	–	–	–	Fed Listens Event with Brainard and Mester.
	Fedspeak	–	–	–	Daly holds podcast on 'community economics'.
Fri 21					
Jpn	May CPI %yr	0.9%	–	–	Core ex fresh food and energy up slightly to 0.6%yr.
	Jun Nikkei manufacturing PMI	49.8	–	–	Soft as per the rest of the world.
Eur	Jun Markit manuf. PMI flash	47.7	–	–	Weakness has persisted…
	Jun Markit services PMI flash	52.9	–	–	… while services has so far been resilient.
Ger	Jun Markit manuf. PMI flash	44.3	–	–	Divergence between manufacturing…
	Jun Markit services PMI flash	55.4	–	–	… and services even more pronounced in Germany.
UK	May public sector borrowing £bn	–7.1	–	–	Borrowing has been lower than expected.
US	Jun Markit manuf. PMI flash	50.5	–	–	Manufacturing is clearly coming under greater pressure…
	Jun Markit services PMI flash	50.9	–	–	… services a little more resilient given domestic demand.
	May existing home sales	–0.4%	1.4%	–	Supply remains a material headwind for existing sales.

Economic & financial forecasts

Interest rate forecasts

	Latest (14 Jun)	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20
Cash	1.25	1.00	0.75	0.75	0.75	0.75	0.75
90 Day BBSW	1.30	1.25	1.00	1.00	1.00	1.00	1.00
3 Year Swap	1.07	1.15	1.10	1.15	1.20	1.25	1.30
10 Year Bond	1.38	1.40	1.40	1.45	1.60	1.70	1.75
10 Year Spread to US (bps)	-70	-70	-65	-65	-60	-55	-55
International							
Fed Funds	2.375	2.125	1.875	1.875	1.875	1.875	1.875
US 10 Year Bond	2.09	2.10	2.05	2.10	2.20	2.25	2.30
US Fed balance sheet USDtrn	3.85	3.80	3.80	3.80	3.80	3.82	3.84
ECB Deposit Rate	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.30
New Zealand							
Cash	1.50	1.50	1.50	1.50	1.50	1.50	1.50
90 day bill	1.58	1.65	1.65	1.65	1.65	1.65	1.65
2 year swap	1.38	1.55	1.60	1.65	1.70	1.75	1.80
10 Year Bond	1.66	1.65	1.70	1.75	1.85	1.95	2.00
10 Year spread to US	-43	-45	-35	-35	-35	-30	-30

Exchange rate forecasts

	Latest (14 Jun)	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20
AUD/USD	0.6905	0.68	0.68	0.66	0.66	0.67	0.67
NZD/USD	0.6538	0.64	0.66	0.66	0.66	0.66	0.66
USD/JPY	108.31	107	106	107	108	109	110
EUR/USD	1.1276	1.13	1.14	1.13	1.13	1.12	1.12
GBP/USD	1.2674	1.27	1.28	1.28	1.29	1.29	1.30
AUD/NZD	1.0562	1.06	1.03	1.01	1.01	1.02	1.02

Australian economic growth forecasts

	2018			2019				Calendar years			
	Q2	Q3	Q4	Q1	Q2f	Q3f	Q4f	2017	2018	2019f	2020f
GDP % qtr	0.9	0.3	0.2	0.4	0.5	0.6	0.7	–	–	–	–
% yr end	3.1	2.8	2.4	1.8	1.4	1.7	2.2	2.4	2.4	2.2	2.5
Unemployment rate qtr avg, yr end	5.4	5.2	5.0	5.0	5.2	5.3	5.4	5.5	5.0	5.4	5.6
CPI % qtr	0.4	0.4	0.5	0.0	0.6	0.6	0.6	–	–	–	–
% yr end	2.1	1.9	1.8	1.3	1.6	1.8	1.8	1.9	1.8	1.8	1.6
CPI trimmed mean %yr	0.5	0.4	0.5	0.3	0.4	0.3	0.5	–	–	–	–
% yr end	1.7	1.7	1.8	1.6	1.5	1.4	1.4	1.8	1.8	1.4	1.8

New Zealand economic growth forecasts

	2018			2019				Calendar years			
	Q2	Q3	Q4	Q1f	Q2f	Q3f	Q4f	2017	2018f	2019f	2020f
GDP % qtr	0.9	0.3	0.6	0.6	0.6	0.7	0.8	–	–	–	–
Annual avg change	3.2	3.1	2.8	2.6	2.4	2.3	2.5	3.1	2.8	2.5	3.1
Unemployment rate %	4.4	4.0	4.3	4.2	4.3	4.3	4.2	4.5	4.3	4.2	3.9
CPI % qtr	0.4	0.9	0.1	0.1	0.6	0.6	0.4	–	–	–	–
Annual change	1.5	1.9	1.9	1.5	1.7	1.4	1.7	1.6	1.9	1.7	1.9

Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.

Start receiving your usual Westpac research and strategy reports from **Westpac IQ.**
https://wibiq.westpac.com.au/Subscribe

Disclaimer

Things you should know.

Westpac Institutional Bank is a division of Westpac Banking Corporation ABN 33 007 457 141 ('Westpac').

Disclaimer

This material contains general commentary, and market colour. The material does not constitute investment advice. Certain types of transactions, including those involving futures, options and high yield securities give rise to substantial risk and are not suitable for all investors. We recommend that you seek your own independent legal or financial advice before proceeding with any investment decision. This information has been prepared without taking account of your objectives, financial situation or needs. This material may contain material provided by third parties. While such material is published with the necessary permission none of Westpac or its related entities accepts any responsibility for the accuracy or completeness of any such material. Although we have made every effort to ensure the information is free from error, none of Westpac or its related entities warrants the accuracy, adequacy or completeness of the information, or otherwise endorses it in any way. Except where contrary to law, Westpac and its related entities intend by this notice to exclude liability for the information. The information is subject to change without notice and none of Westpac or its related entities is under any obligation to update the information or correct any inaccuracy which may become apparent at a later date. The information contained in this material does not constitute an offer, a solicitation of an offer, or an inducement to subscribe for, purchase or sell any financial instrument or to enter a legally binding contract. Past performance is not a reliable indicator of future performance. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

Country disclosures

Australia: Westpac holds an Australian Financial Services Licence (No. 233714). This material is provided to you solely for your own use and in your capacity as a wholesale client of Westpac.

New Zealand: In New Zealand, Westpac Institutional Bank refers to the brand under which products and services are provided by either Westpac or Westpac New Zealand Limited ("WNZL"). Any product or service made available by WNZL does not represent an offer from Westpac or any of its subsidiaries (other than WNZL). Neither Westpac nor its other subsidiaries guarantee or otherwise support the performance of WNZL in respect of any such product. The current disclosure statements for the New Zealand branch of Westpac and WNZL can be obtained at the internet address www.westpac.co.nz. For further information please refer to the Product Disclosure Statement (available from your Relationship Manager) for any product for which a Product Disclosure Statement is required, or applicable customer agreement. Download the Westpac NZ QFE Group Financial Advisers Act 2008 Disclosure Statement at www.westpac.co.nz.

China, Hong Kong, Singapore and India: This material has been prepared and issued for distribution in Singapore to institutional investors, accredited investors and expert investors (as defined in the applicable Singapore laws and regulations) only. Recipients in Singapore of this material should contact Westpac Singapore Branch in respect of any matters arising from, or in connection with, this material. Westpac Singapore Branch holds a wholesale banking licence and is subject to supervision by the Monetary Authority of Singapore. Westpac Hong Kong Branch holds a banking license and is subject to supervision by the Hong Kong Monetary Authority. Westpac Hong Kong branch also holds a license issued by the Hong Kong Securities and Futures Commission (SFC) for Type 1 and Type 4 regulated activities. This material is intended only to "professional investors" as defined in the Securities and Futures Ordinance and any rules made under that Ordinance. Westpac Shanghai and Beijing Branches hold banking licenses and are subject to supervision by the China Banking Regulatory Commission (CBRC). Westpac Mumbai Branch holds a banking license from Reserve Bank of India (RBI) and subject to regulation and supervision by the RBI.

UK: The contents of this communication, which have been prepared by and are the sole responsibility of Westpac Banking Corporation London and Westpac Europe Limited. Westpac (a) has its principal place of business in the United Kingdom at Camomile Court, 23 Camomile Street, London EC3A 7LL, and is registered at Cardiff in the UK (as Branch No. BR00106), and (b) authorised and regulated by the Australian Prudential Regulation Authority in Australia. Westpac is authorised in the United Kingdom by the Prudential Regulation Authority. Westpac is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request. Westpac Europe Limited is a company registered in England (number 05660023) and is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

This communication is being made only to and is directed at (a) persons who have professional experience in matters relating to investments who fall within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the "Order") or (b) high net worth entities, and other persons to whom it may otherwise lawfully be communicated, falling within Article 49(2)(a) to (d) of the Order (all such persons together being referred to as "relevant persons"). Any person who is not a relevant person should not act or rely on this communication or any of its contents. The investments to which this communication relates are only available to and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such investments will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely upon this communication or any of its contents. In the same way, the information contained in this communication is intended for "eligible counterparties" and "professional clients" as defined by the rules of the Financial Conduct Authority and is not intended for "retail clients". With this in mind, Westpac expressly prohibits you from passing on the information in this communication to any third party. In particular this communication and, in each case, any copies thereof may not be taken, transmitted or distributed, directly or indirectly into any restricted jurisdiction. This communication is made in compliance with the Market Abuse Regulation (Regulation(EU) 596/2014).

Disclaimer continued

Investment Recommendations Disclosure

The material may contain investment recommendations, including information recommending an investment strategy. Reasonable steps have been taken to ensure that the material is presented in a clear, accurate and objective manner. Investment Recommendations for Financial Instruments covered by MAR are made in compliance with Article 20 MAR. Westpac does not apply MAR Investment Recommendation requirements to Spot Foreign Exchange which is out of scope for MAR.

Unless otherwise indicated, there are no planned updates to this Investment Recommendation at the time of publication. Westpac has no obligation to update, modify or amend this Investment Recommendation or to notify the recipients of this Investment Recommendation should any information, including opinion, forecast or estimate set out in this Investment Recommendation change or subsequently become inaccurate.

Westpac will from time to time dispose of and acquire financial instruments of companies covered in this Investment Recommendation as principal and act as a market maker or liquidity provider in such financial instruments.

Westpac does not have any proprietary positions in equity shares of issuers that are the subject of an investment recommendation.

Westpac may have provided investment banking services to the issuer in the course of the past 12 months.

Westpac does not permit any issuer to see or comment on any investment recommendation prior to its completion and distribution.

Individuals who produce investment recommendations are not permitted to undertake any transactions in any financial instruments or derivatives in relation to the issuers covered by the investment recommendations they produce.

Westpac has implemented policies and procedures, which are designed to ensure conflicts of interests are managed consistently and appropriately, and to treat clients fairly.

The following arrangements have been adopted for the avoidance and prevention of conflicts in interests associated with the provision of investment recommendations.

i. Chinese Wall/Cell arrangements;
ii. physical separation of various Business/Support Units;
iii. Strict and well defined wall/cell crossing procedures;
iv. a "need to know" policy;
v. documented and well defined procedures for dealing with conflicts of interest;
vi. reasonable steps by Compliance to ensure that the Chinese Wall/Cell arrangements remain effective and that such arrangements are adequately monitored.

U.S.: Westpac operates in the United States of America as a federally licensed branch, regulated by the Office of the Comptroller of the Currency. Westpac is also registered with the US Commodity Futures Trading Commission ("CFTC") as a Swap Dealer, but is neither registered as, or affiliated with, a Futures Commission Merchant registered with the US CFTC. Westpac Capital Markets, LLC ('WCM'), a wholly-owned subsidiary of Westpac, is a broker-dealer registered under the U.S. Securities Exchange Act of 1934 ('the Exchange Act') and member of the Financial Industry Regulatory Authority ('FINRA'). This communication is provided for distribution to U.S. institutional investors in reliance on the exemption from registration provided by Rule 15a-6 under the Exchange Act and is not subject to all of the independence and disclosure standards applicable to debt research reports prepared for retail investors in the United States. WCM is the U.S. distributor of this communication and accepts responsibility for the contents of this communication. All disclaimers set out with respect to Westpac apply equally to WCM. If you would like to speak to someone regarding any security mentioned herein, please contact WCM on +1 212 389 1269. All disclaimers set out with respect to Westpac apply equally to WCM.

Investing in any non-U.S. securities or related financial instruments mentioned in this communication may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the SEC in the United States. Information on such non-U.S. securities or related financial instruments may be limited. Non-U.S. companies may not subject to audit and reporting standards and regulatory requirements comparable to those in effect in the United States. The value of any investment or income from any securities or related derivative instruments denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related derivative instruments.

The author of this communication is employed by Westpac and is not registered or qualified as a research analyst, representative, or associated person under the rules of FINRA, any other U.S. self-regulatory organisation, or the laws, rules or regulations of any State. Unless otherwise specifically stated, the views expressed herein are solely those of the author and may differ from the information, views or analysis expressed by Westpac and/or its affiliates.