Monday, 8 May 2023

Budget Night – Biggest Night of the Year

Tomorrow the Federal Treasurer hands down the Budget at 7:30pm AEST. It is the biggest night of the year for economists and the longest, as we digest the Budget papers.

As the night has drawn closer, speculation has been rife that the government will deliver a surplus for 2022-23. It follows monthly finance statistics data revealing that in the month of March and over the 12 months to the end of March, the budget was in surplus. If the Government prints a surplus tomorrow night, it will be the first in 15 years (since 2007-08).

One thing is certain, the budget's bottom line will show a sharp improvement, more so in the near-term years, due to a stronger nominal economy. The lift in nominal economic activity has helped deliver higher tax revenues from low unemployment, bracket creep, higher commodity prices and a sharp recovery in net overseas arrivals.

Our leading Budget expert, Pat Bustamante, has published a 5-part series on the Budget ahead of its release tomorrow. The series highlighted that Jim Chalmers has a difficult budget to frame because there are mounting pressures pulling the public purse in opposite directions.

On the one hand, Chalmers needs to ensure his budget does not add fuel to the inflation fire just as it is showing some early signs of dying down. Inflation peaked at 7.8% in the December quarter of last year and has stepped down to 7.0% but still has a way to go to the Reserve Bank's (RBA) target of 2-3% per annum.

On the other hand, there are vulnerable households facing challenges from the higher cost of living, which adds pressure on Chalmers to announce spending for households. Household incomes have gone backwards at a record pace due to high inflation, rising mortgage rates and accelerating rents. The Government has flagged that it will provide a highly targeted $14.6 billion cost-of-living package. We await to see specific details and how the package fits in with the broader fiscal strategy. While it may be appropriate to provide vulnerable Australians with cost-of-living support, untargeted spending risks adding to inflationary pressures.

Inflation won't be far from Chalmers' mind. Last week, the RBA unexpectedly hiked the cash rate from 3.60% to 3.85% to further tighten monetary policy as they aim to bring down inflation over time. Financial markets had not expected the hike because recent data shows a slowing in economic activity and the latest consumer price index release suggested that inflation was tracking in line with the trajectory outlaid by the RBA in its February forecasts. However, the RBA's accompany statement revealed concerns around the pick up in services inflation and a focus on inflation expectations. Our Group view is that there will be no further rate hikes, however, one cannot completely rule out the possibility of another hike. A lot will depend on the data flow.

The RBA was not alone in raising rates last week. Indeed, it was a week of rate hikes with the US Federal Reserve and the European Central Bank also raising rates by 25 basis points to 5.00-5.25% and 3.75%, respectively. The US Federal Reserve flagged that they may stop hiking, but made it conditional on the data. Markets are widely anticipating the Fed to start cutting before September with a US recession also priced (the US-2-10-year curve is deeply inverted).

Economic data locally this week will take a backseat to the Budget.

The business survey out today showed business confidence and conditions are holding up. The building approvals data also out earlier today suggested housing supply won't be forthcoming in the near term, sustaining the growing imbalance between demand and supply in the housing market.

Tomorrow, consumer confidence is likely to remain downbeat. Recall last month, confidence bounced 9.4% to 85.8 but the outcome remained under 100 and so firmly in 'pessimistic' territory. With the RBA recently hiking the cash rate unexpectedly, we would expect an unwind of this bounce to occur.

To round out the week, there is inflation expectations on Thursday.

Besa Deda, Chief Economist
+61 404 844 817

Group Forecasts

		2023			2024		
End Period:	**Close (5 May)**	**Q2 (f)**	**Q3 (f)**	**Q4 (f)**	**Q1 (f)**	**Q2 (f)**	**Q3 (f)**
Aust. Interest Rates:							
RBA Cash Rate, %	3.85	3.60	3.60	3.60	3.35	3.10	2.85
90 Day BBSW, %	3.87	3.70	3.70	3.72	3.47	3.22	2.97
3 Year Swap, %	3.48	3.50	3.50	3.40	3.30	3.10	2.90
10 Year Bond, %	3.32	3.40	3.30	3.20	3.00	2.80	2.70
US Interest Rates:							
Fed Funds Rate, %	5.125	5.125	5.125	4.875	4.375	3.875	3.375
US 10 Year Bond, %	3.44	3.50	3.40	3.30	3.10	2.90	2.80
USD Exchange Rates:							
AUD-USD	0.6749	0.69	0.72	0.74	0.75	0.76	0.76
USD-JPY	134.80	130	129	128	127	126	125
EUR-USD	1.1019	1.10	1.11	1.12	1.13	1.14	1.15
GBP-USD	1.2636	1.23	1.24	1.25	1.26	1.27	1.28
NZD-USD	0.6292	0.64	0.66	0.67	0.68	0.68	0.68
AUD Exchange Rates:							
AUD-USD	0.6749	0.69	0.72	0.74	0.75	0.76	0.76
AUD-EUR	0.6126	0.63	0.65	0.66	0.67	0.67	0.66
AUD-JPY	91.05	89.7	92.9	94.7	95.3	95.8	95.0
AUD-GBP	0.5345	0.56	0.58	0.59	0.60	0.60	0.59
AUD-NZD	1.0721	1.08	1.09	1.10	1.11	1.13	1.13

	2021	**2022**	**2023 (f)**	**2024 (f)**
GDP, %	4.6	2.7	1.0	1.5
CPI (Headline), %	3.5	7.8	4.0	3.1
CPI (Trimmed mean), %	2.7	6.9	3.7	3.1
Unemployment Rate, %	4.7	3.5	4.5	5.0
Wages Growth, %	2.4	3.3	4.0	3.2

AUD cross exchange rates have been rounded.

Financial forecasts are quarter end.

GDP, CPI, employment and wage growth forecasts are year end.

Contact Listing

Chief Economist
Besa Deda
dedab@stgeorge.com.au
+61 404 844 817

Senior Economist
Pat Bustamante
pat.bustamante@stgeorge.com.au
+61 468 571 786

Senior Economist
Jarek Kowcza
jarek.kowcza@stgeorge.com.au
+61 481 476 436

Economist
Jameson Coombs
jameson.cooombs@stgeorge.com.au
+61 401 102 789