# Outlook Q2 2024 & Quarterly review

BlackRock

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## Economic Outlook Q2

The Reserve Bank of Australia (RBA) kept the cash rate unchanged over Q1'24 and signaled in the March meeting that the prospect of further rate hikes from here on is diminishing. Their preference is naturally to not rule anything in or out given the level of uncertainty around services inflation, in particular. The greater than expected resilience in the US economy and several large emerging market economies along with fiscal support measures in China would no doubt be adding an extra layer of caution to the RBA's current thinking.

Australian inflation has eased considerably and broadly in with the RBA's own estimates. The decline in inflation has been broad based highlighting a weakening consumer and labour market falling back into balance. While the RBA's growth and inflation forecasts have been revised lower, they retain a clear sensitivity towards inflation threats. The RBA still characterize the overall inflation mix as indicative of an economy with excess demand and the labour market being tighter than "sustainable" levels. Rents remain "sticky" which may keep services inflation risks elevated.

Wages growth was solid in Q4'23 rising by 0.9% (4.2% y/y). This put annual wages growth at the highest since Q1'09 and highlighted significant wages growth in the public sector. Despite this the RBA retains the view that wages growth is currently around its peak for the cycle but is not expected to decline quickly.

GDP for Q4'23 was positive at 0.2% (1.5% y/y) and in line with the RBA's assumption. The data reflected that Government spending and private business investment remained the main drivers of GDP growth supported by a large pipeline of construction and public infrastructure work. Household consumption remains weak due to ongoing cost-of-living pressures, higher interest rates and higher taxes weighing on disposable income. GDP will remain sub trend in 2024 but should improve over the course of the year due to falling inflation, scheduled income tax cuts, and government rebates/subsidies.

National house price growth remains strong with annual growth remaining resilient at 9.7% y/y. Expectations are for prices to ease due to record poor affordability levels and slowing population growth. However, building approvals and construction weakness is set to continue through the year.

Our thinking had been the RBA would hike a final time in Q1'24 tightening financial conditions a little more and instilling the bank with more confidence around hitting their 2-3% inflation target. However, the RBA thinks overall financial conditions in Australia are restrictive enough for households.

It now feels like a very high hurdle to get the RBA hiking again. Accordingly, we expect the cash rate to be held at the current level for an extended period, at least until Q4'24. The risks to our view are that cuts are delayed into 2025 due to ongoing "sticky" services inflation. Conversely, an unexpected weakening in the labour market could bring about an earlier than expected cut in interest rates.

## Credit Outlook Q2

The demand for credit was extremely strong in Q1'24 with investors' chasing the relatively high outright yields on offer. The high demand for credit assets was met with a wall of supply from issuers more than willing to sell debt at tight spreads and in large volume. It seems the global 'carry' trade is in full swing now that economic growth, while muted, looks OK, inflation continues to fall and global central banks shift their rhetoric towards prospective rate cuts in 2024.

Credit spread tightening has been fairly consistent and forward-looking total returns still look relatively attractive. However, falling interest rates will be an important driver of total returns in credit.

The main risk to ongoing positive investor sentiment is the timing and magnitude of rate cuts in 2024. Any delays will make it a challenge to support spreads at their current very tight levels. Geopolitical risks also abound and there is a busy global election calendar later in the year.

## Currency Outlook Q2

The AUD continued to trade in a remarkably tight US$0.65-0.66 cent range in Q1'24. Despite the dovish rate outlook from the major global central banks the AUD has consistently failed to benefit. This is a worrying sign and likely points to concerns around the China growth outlook and some general investor risk aversion.

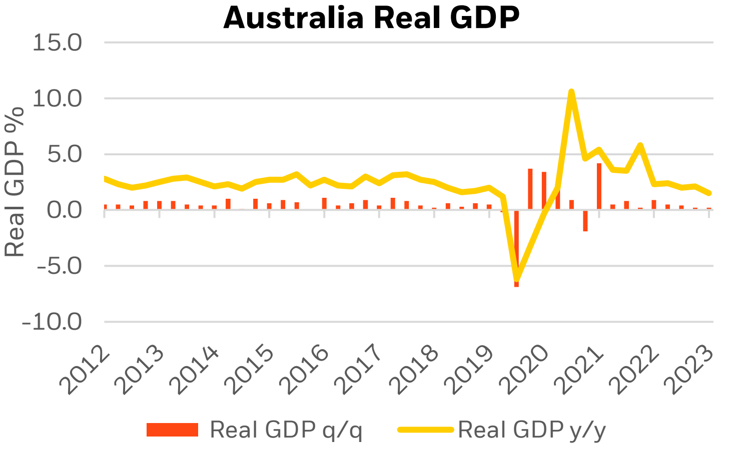
The RBA's recent pivot to more dovish language in response to softer-than-expected data will make it a challenge for the AUD to test recent highs. Local economic data or events that cause the market to price more RBA easing will see the AUD trend lower, albeit in a tight trading range.

Global commodity prices are lower year-to-date and the lack of policy support by Chinese policy officials to stimulate the economy continues to weigh on iron ore prices. Geopolitical developments, including developments in the Red Sea, and the Middle East and Russia-Ukraine conflicts, continue to influence commodity prices.

# GDP – Q4 2023

▲ QoQ GDP **grew 0.2%**. This was **in line with** expectations.
▼ YoY GDP fell from **2.1%** to **1.5%**.

Despite the overall slowdown to GDP over 2023, the increase in growth marked the ninth straight rise in quarterly GDP. However, YoY GDP growth was the lowest since Q4 2020, highlighting the impact of elevated rates. The largest contribution to growth was net exports due to a -3.4% fall in imports driven by weakness in consumption goods. The weakness in real household disposable income has continued to underpin the weakness in consumption. Household spending remained subdued increasing by +0.1% QoQ, with a rise in spending on essentials offset by a fall in discretionary spendings. Economic growth this year was also supported by public and private investment which is expected to continue.

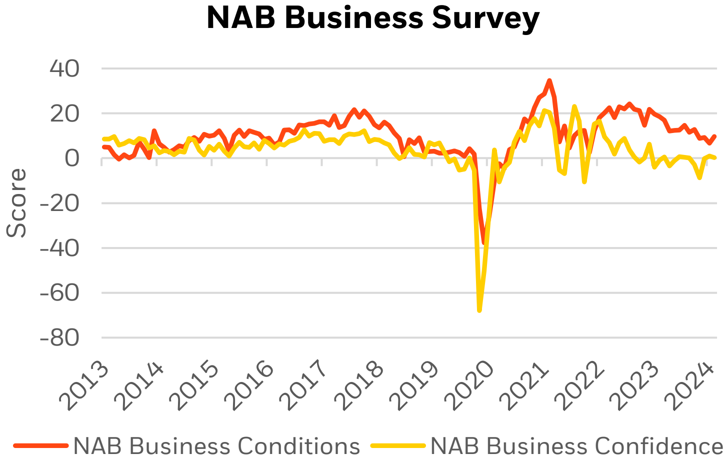



Source: ABS, Bloomberg, BlackRock as of 04/04/2024

# Business Conditions – Feb 2024

▲ **Conditions rose by 3pts** from +7pts (Jan) to +10 pts (Feb)
▼ **Confidence fell by 1pt** from 1pt (Jan) to 0pts (Feb)

The February NAB business survey saw business conditions rise 3pts to +10pts, driven by conditions and profitability rising by 4pts each while the employment index remained broadly unchanged. The survey signaled that the economy remained resilient in the new year and that inflation is still a challenge despite slowing growth. While business conditions strengthened to be marginally above the long-run average, business confidence remained weak and below the long-run average. Notably, retail price growth jumped to 1.4% from 0.9% previously. This reversed some of the easing seen towards the end of 2023, a sign that further progress on inflation is unlikely to be smooth over the months ahead.

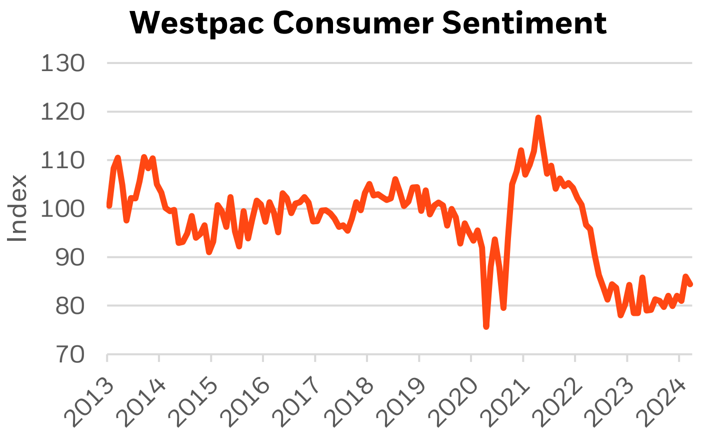



Source: NAB, Bloomberg, BlackRock as of 04/04/2024

# Consumer Sentiment – Mar 2024

▼ The Westpac-M.I. Index of Consumer Sentiment **decreased by 1.8%** from 86.0 in February to **84.4 in March**.

While consumer sentiment improved in February, rising by +6.2%, this month's survey shows that progress remains slow with renewed concerns about the economy's near-term outlook. Inflation continues to dominate the news cycle, but the cost-of-living crisis is becoming less acute, with news recall levels dropping to 43% from last year's 60%+ highs. Consumers are still wary of the potential for more rate rises with 40% still expecting mortgage rates to move higher over 2024. Sentiment among those surveyed prior to the RBA decision was stronger at 94.9 compared to 79.3 post-decision, suggesting that many consumers hoped for a more positive message on inflation and the interest rate outlook. Safe-haven assets continue to remain the preferred choice for savings.

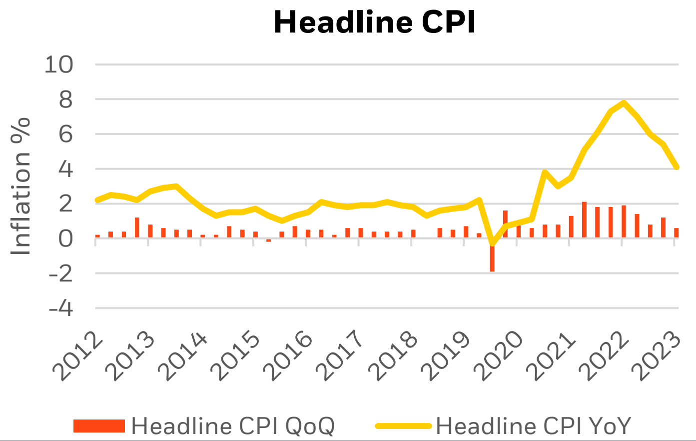



Source: Westpac, Bloomberg, BlackRock as of 04/04/2024

# Inflation – Q4 2023

▲ Headline CPI **increased by 0.6%** QoQ. This was **0.2% lower** than market consensus.
▼ Annual inflation **fell 1.3%** from to 5.4% to **4.1% YoY**.

The annual pace of inflation declined to 4.1%, slightly lower than market expectations of 4.3% YoY. This marked the fourth consecutive quarter of lower annual inflation, down from the peak of 7.8% in December 2022. Annual inflation is now at its lowest level since December 2021. Key contributors to rising prices in Q4 were housing (+1.0%), alcohol & tobacco (+2.8%), and insurance and financial services (+1.7%). Price falls were recorded only for education (-0.1%), transport (-0.2%) and furniture and household equipment (-1%). Inflation is expected to continue to ease, however service inflation may prove to be sticky in 2024 particularly if subsidies roll off.



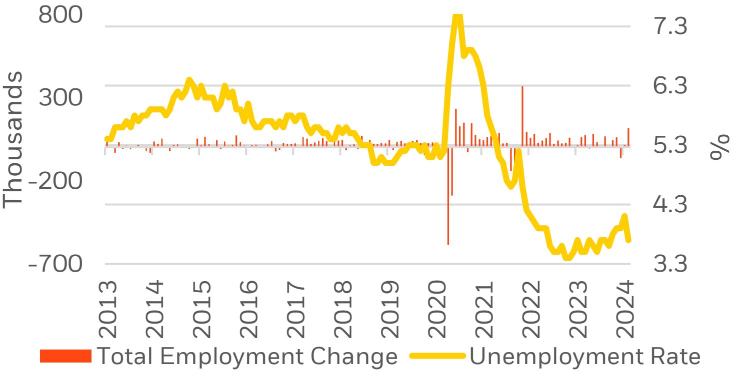

Source: ABS, Bloomberg, BlackRock as of 04/04/2024

# Labour Market – Feb 2024

▲ Employment data saw 116,500 **new jobs gained**. This was **76,500 more** than market consensus.
▼ The unemployment rate **fell 0.4%** from 4.1% to **3.7%**.

Australian employment surged in February, surprising again to the upside with 116.5k new jobs added. Employment growth was driven by full-time workers rising +78.2k, whilst part time increased by +38.3k. The unemployment rate also declined to 3.7% from a two-year high of 4.1%, while the participation rate fell to 66.7%. The ABS stated that “The large increase in employment in February followed larger than usual numbers of people in December and January who had a job that they were waiting to start or return to.” Falling hours worked, rising part-time employment and underutilisation are all symptomatic of an easing in the tightness of the labour market.

### Monthly Employment Change & Unemployment Rate



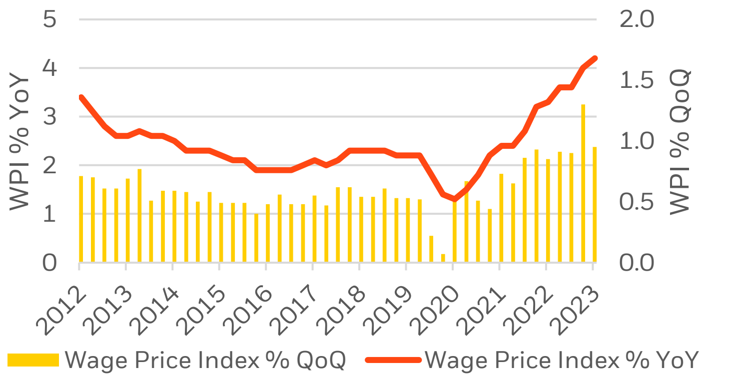

Source: ABS, Bloomberg, BlackRock as of 04/04//2024

# Wage Price Index – Q4 2023

▲ Wages **increased by 0.9%** over Q4. This was **in line** with market consensus.
▲ Annual wage growth **rose 0.2%** to **4.2%**

The annual wage growth is at its highest since Q1 2009, with the public sector rising 4.3% YoY, slightly above the private sector’s 4.2%. Public sector wages also had the highest quarterly increase in 15yrs, increasing by +1.3% QoQ. Higher growth in the public sector was primarily due to newly implemented enterprise bargaining agreements (EBA’s) for essential workers in the Health care and social assistance, and Education and training industries. WPI is likely to remain elevated due to lagged effects of new EBA’s rolling onto larger increases putting a floor under WPI. The significant increase in net overseas migration will help cap the upside as it eases tightness in the labour market.

### Wage Price Index



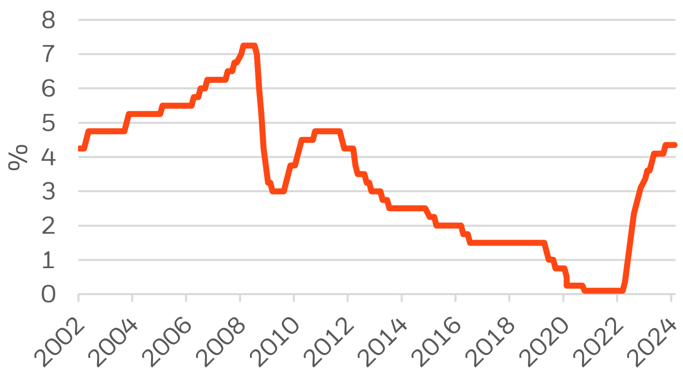

Source: ABS, Bloomberg, BlackRock as of 04/04/2024

# RBA Policy Rate – Mar 2024

▶ The RBA left the cash rate **unchanged at 4.35%** during the quarter.

The RBA left cash rate unchanged at 4.35% as expected but moved from a mild tightening bias to a neutral one where “the Board is not ruling anything in or out” vs previous “a further increase in interest rates cannot be ruled out”. The new guidance whilst not new language has more symmetry around the evolving risks that the RBA foresee. The RBA notes the progress on inflation despite the ongoing uncertainty but there is a note of caution with a new reference to continued high unit labor costs and uncertainty over the recent improvement in productivity. The RBA see the macro-economic environment as highly uncertain and is keeping all options open.

### RBA Cash Rate Target



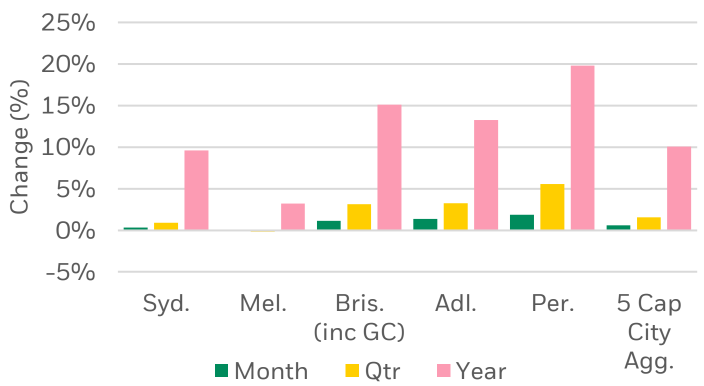

Source: RBA, Bloomberg, BlackRock as of 04/04/2024

# House Prices – Q1 2024

▲ The CoreLogic national HVI **rose 1.6% in Q1**
▲ The CoreLogic national HVI **increased 10.1% over the year**

House prices continued to rise over Q1, though the quarterly growth has halved compared to mid last year when home values rose 3.3% QoQ. Softer housing conditions since then were caused by rate hikes, cost of living pressures, and worsening housing affordability. Despite these challenges, undersupply relative to demand continues to exert upward pressure on home values. Perth's housing market experienced the highest growth, with values increasing by 1.9% over the month, followed by Adelaide and Brisbane increasing by 1.4% and 1.1% respectively. The remaining capitals showed much lower rates of change, with Melbourne being the only capital city to record a negative quarterly movement, decreasing by -0.2% over the first three months of the year.

### Core Logic Australian Home Value Index




Source: CoreLogic, Bloomberg, BlackRock as of 04/04/2024





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