

9 October 2019

## Consumer Sentiment drops to four year low

• **The Westpac-Melbourne Institute Index of Consumer Sentiment fell 5.5% to 92.8 in October from 98.2 in September.**

This is the lowest level of the Index since July 2015. The Index has fallen by 8.4% since the Reserve Bank started cutting rates in June and is down by 8.6% over the last year.

The fall comes despite a further 25bp cash rate cut from the RBA at its October meeting – the third rate cut since June taking the cash rate to a new historical low of 0.75%.

This result will be of some concern to the monetary authorities. Typically, an interest rate cut boosts confidence particularly around consumers' expectations for and assessments of their own finances. In this survey these components of the Index fell by 3.7% and 4.9% respectively. This may be because, despite the rate cut, assessments for the economy overall plunged by 6% (the twelve month outlook) and 9.1% (the five year outlook).

Consumers are looking behind the reason for the rate cut and, arguably, the absolute level of rates and getting nervous.

The Index has now been in the range where pessimists outnumber optimists for three of the last four months. As discussed, the October update marks the lowest read since July 2015, when a sudden 30% plunge in the Chinese share market sparked concerns around the Chinese economy and resulted in a 3.3% fall in the Index. However this was more than reversed by an 8% recovery in the Index in the following month.

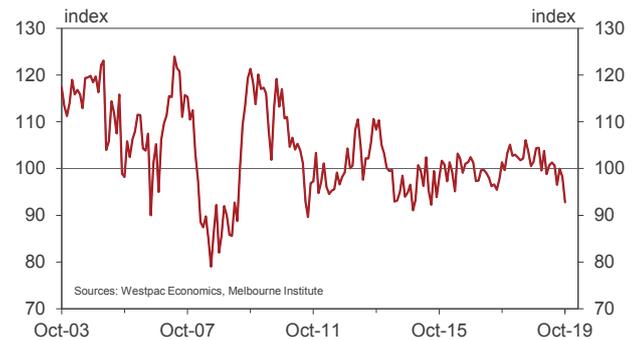
Global events have, again, contributed to the weak result in October with the deterioration in US-China trade relations weighing on the global economy amid speculation of a recession in the US. In fact, during the week of the survey the US share market fell by 2.6% and the Australian market was down by 3%.

But these events are unlikely to fully explain the sharp fall in the Index. Issues that may also be unnerving consumers include the debate around the lack of response of fiscal policy to the deteriorating outlook; the banks' partial (13 to 15 basis points) pass through to the standard variable mortgage rate of the recent official rate cut; and the realisation amongst Australians that wages growth is likely to remain 'stuck' at a modest 2%/yr or less for the foreseeable future.

All index components recorded material declines in October. Consumer expectations for the economy recorded the biggest falls – the 'economy, next 5 years' sub-index plunged 9.1% and the 'economy, next 12 months' sub-index dropped by 6%. October marks the first month both sub-indexes have been below their long run average levels since April 2016.

Assessments of family finances also took a heavy knock, the 'finances vs a year ago' sub-index was down by 4.9% and the 'finances, next 12 months' sub-index was down by

**Consumer Sentiment Index**



3.7%, the latter hitting a five year low. Both moves came despite the series of interest rate cuts since June and the LMITO tax relief rolled out since July.

Note that despite the cut in the official cash rate confidence amongst respondents with a mortgage dropped by 4%.

While the biggest falls this month were around consumer views on the economy, it is consumer views around family finances that remain the clear weak spot with the combined reading across these two indexes 12 points below its long run average compared to a combined reading across economic sub-indexes that is 3 points below average.

Consumer attitudes towards spending also deteriorated in October. The 'time to buy a major household item' sub-index declined 4.2%, also moving to a four year low. Spending on discretionary and big ticket durable items has been particularly weak over the last year.

Despite the loss of confidence this month, consumers' job loss fears improved slightly. The Westpac-Melbourne Institute Unemployment Expectations Index declined 1.3% to 131.8 in October, holding slightly above the long run average of 130 (recall that lower readings indicate that more consumers expect unemployment to fall in the year ahead). However, the state detail shows the improvement overall was due to sharply improved reads in Queensland and WA offsetting slight deteriorations in NSW and Victoria. Even with the slight improvement the index nationally has still deteriorated by 9% since the middle of the year, consistent with a slowdown in jobs growth and steady increases in unemployment and underemployment rates.

Housing-related sentiment continues to show more mixed results with softer reads on 'time to buy' but more bullish expectations for prices suggesting affordability constraints may be starting to re-emerge.

The 'time to buy a dwelling' index declined a further 5.4% in October to be down 8.1% from its August peak (a five year high). At 116.6, the index is now below its long run average



of 120. NSW and Victoria have shown particularly sharp deterioration, down 12% and 14% respectively since August.

In contrast, the Westpac-Melbourne Institute Index of House Price Expectations Index posted a further 5.9% rise in October following the 3.9% rise in September to be up a spectacular 54.4% since May.

Not surprisingly, the state detail on price expectations is the mirror image of the picture from assessments of 'time to buy' with the biggest gains over the last two months again coming in NSW (+12.5%) and Vic (+16.6%). More consumers nationally now expect prices to rise than fall – the first 'net positive' consensus since mid-2018.

The Reserve Bank Board next meets on November 5. Westpac expects the Board will decide to keep the cash rate on hold. Despite this unexpected plunge in the Index the Board is likely to take some time to assess the impact of the three rate cuts before deciding to move again. As we discussed in this report, they will also be alerted to the impact that reductions in the cash rate to well below historical lows may be having on consumers' assessments of the economy.

In particular, the signals around how consumers are assessing their own finances are worthy of detailed consideration before the Board embarks on its next move.

Westpac expects that next move will be a further cut in the cash rate to 0.5% in February next year although a case can be made for an earlier cut in December depending on developments in the labour market and the global economy.

While we expect the Bank will also be studying various types of unconventional monetary policy measures it is to be hoped that the signals from this survey highlight the possible unintended consequences that may result from the option of resorting to negative interest rates.

**Bill Evans**, Chief Economist

## Consumer Sentiment – October 2019

	avg*	Oct 2017	Oct 2018	Sep 2019	Oct 2019	%mth	%yr
Consumer Sentiment Index	101.5	101.4	101.5	98.2	92.8	-5.5	-8.6
Family finances vs a year ago	89.4	83.7	87.4	84.3	80.2	-4.9	-8.2
Family finances next 12mths	107.6	102.4	102.8	96.9	93.3	-3.7	-9.3
Economic conditions next 12mths	91.0	102.6	102.5	92.6	87.1	-6.0	-15.1
Economic conditions next 5yrs	91.3	95.2	94.9	97.8	88.9	-9.1	-6.4
Time to buy a major household item	127.2	122.8	119.8	119.6	114.5	-4.2	-4.4
Time to buy a dwelling	119.7	95.1	102.6	123.3	116.6	-5.4	13.7
Unemployment Expectations Index	130.0	129.2	122.8	133.6	131.8	-1.3	7.3
House Price Expectations Index	125.5	140.5	101.4	130.3	138.0	5.9	36.1

Source: Westpac-Melbourne Institute

\*avg over full history of the survey, all indexes except 'time to buy a dwelling', 'unemployment expectations' and 'house price expectations' are seasonally adjusted

Survey interviews are conducted by OZINFO Research on the telephone using trained interviewers. Telephone numbers and the household respondent are selected at random. This latest survey is based on 1200 adults aged 18 years and over, across Australia. It was conducted in the week from 30 September to 3 October 2019. The data have been weighted to reflect Australia's population distribution. Copyright at all times remains with the Melbourne Institute of Applied Economic and Social Research.



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