Bulletin

9 June 2021

Consumer confidence fades in response to Melbourne lockdown

- **The Westpac-Melbourne Institute Index of Consumer Sentiment fell 5.2% to 107.2 in June from 113.1 in May.**

The Index has now fallen by 9.7% over the last two months. We think the initial 4.8% fall in May can be mainly attributed to a combination of a statistical correction following a very strong surge in April to an eleven-year high, and some disappointment around the Budget given high expectations leading into the announcement.

The latest fall in June is almost certainly due to concerns around the two-week lockdown in Melbourne. The survey was conducted during the first week of the lockdown.

The Index is now back at the level we saw back in January when the country was impacted by significant lockdowns in parts of Sydney and Queensland. The fall in the Index between the surveys in early January and December – when the country had been comfortably reopening with memories of lockdowns fading – was 4.5%, comparable to the fall we are now experiencing.

Of course, just as we saw in January, the falls this month are not uniform across the nation. In January, the state most affected by the lockdown, NSW, suffered the biggest hit (–5.3%).

In today's survey we have seen a fall of 7.5% in Victoria, 4% in Queensland, 9% in Western Australia, and 10.9% in South Australia. While the fall in Victoria is to be expected, the significant declines elsewhere may be pointing to considerable insecurity in the small states with respect to their vulnerability to further outbreaks as well, in some cases, to their particular reliance on Victoria for tourism.

In contrast, the Index in NSW fell by a meagre 1.1% highlighting the confidence the state has in its capacity to contain the virus. Sentiment in NSW is now 15.4% above Victoria; 11% above Queensland; 19.3% above Western Australia; 14.4% above South Australia and 29.6% above Tasmania.

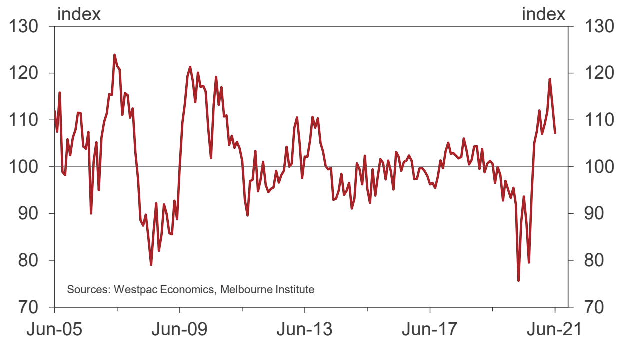
That resilience in NSW, our largest state, will be very important for supporting national sentiment and, in turn, sustaining the economic recovery.

Our detailed questions also detected an emerging concern with inflation potentially providing a further explanation for the fall in the Index, although at this stage there is no related concern about interest rates.

This month we asked our respondents about the major news items that caught their attention and whether they were favourable or unfavourable. These questions have been run in the survey since its inception in the early 1970s. There is no news category for 'pandemic' – the closest we come is 'economic conditions'. Not surprisingly, this had the highest levels of recall in June (21%).

Other most recalled news items were around employment (17.3%); Budget and tax (15%); inflation (11.4%); and international conditions (7.9%).

Consumer Sentiment Index



The assessment of domestic economic conditions deteriorated compared to March, swinging from net favourable to slightly unfavourable. However, while respondents were still buoyed by news on the labour market there was a sharp deterioration in respondents' assessments of international conditions and a marked increase in concerns about inflation.

All components of the Index fell in June, most moving back into line with their levels back in January. The 'family finances, last 12 months' sub-index fell 8.5% but some of this may reflect changes in the point of comparison – taken literally, last month's responses would have been on comparisons with the national lockdown in April-May last year.

The 'family finances, next 12 months' sub-index declined by 2%.

The 'economy, next 12 months' sub-index deteriorated by 10.3% as respondents were alerted to the increased lockdown risks.

On the other hand, the five-year outlook hardly moved – the 'economy, next 5 years' sub-index down by 1.4%.

The 'time to buy a major household item' sub-index fell by 4.1%. This sub-index which underperformed during the period earlier in the year, when the overall Index reached an eleven-year high, continues to signal that the 12.5% lift we saw in spending on durables over the last year is likely to slow in 2021.

The latest lockdown has also dented optimism around labour market prospects. The Westpac Melbourne Institute Index of Unemployment Expectations jumped 8.2% in June (recall that higher readings on the Index mean more consumers expect unemployment to rise in the year ahead). 'Jobs confidence' is still positive, the index was coming off its best read in a decade in May, but the fall has taken the index nationally back to the levels seen leading into last Christmas.

Housing-related sentiment continues to show significant signs of stress. The 'time to buy a dwelling' index recorded its fifth monthly decline in a row, dropping 7.1% in June to be 27% below its November level. At 96.1 the index is now in outright pessimistic territory for the first time since April last year, and prior to that, late 2017, when housing was entering a difficult period marked by slowing activity and falling prices, particularly in Sydney and Melbourne.

Surging prices and rapidly deteriorating affordability are clearly starting to weigh heavily on buyers, suggesting owner occupier activity, particularly first home buyers, is likely to fade.

Victoria was again a standout, with buyer sentiment recording an 11% drop in the month and a 24% slump over the last two months.

Price expectations are also showing signs of turning lower although consumers are still very bullish on the house price outlook. The Westpac-Melbourne Institute House Price Expectations Index declined 3.6% in June but remains in strongly positive territory at 157.

The June update highlights the message the sentiment survey has been sending for some months – of a major rebalancing in housing activity towards investors and away from owner occupiers.

Every quarter we ask additional questions about where consumers see the 'wisest place for their savings'.

Safe' options continue to dominate with 29% of consumers nominating 'bank deposits' and 19% nominating 'pay down debt' – comparable to the average reads in the years following the Global Financial Crisis.

Where consumers are a little more open to risk, they continue to favour shares where the proportion has lifted from 10.5% to 12.1% over the last three months whereas 'real estate' has only risen from 9.3% to 9.5%. That continues the run of very low reads seen for real estate over the last year – the long run average is 25.9%.

This result might seem at odds with our expectation that investors will assume a dominant role in the current surge in housing activity. While 'real estate' is still not viewed favourably, bullish price expectations will still be enough of a drawcard for many investors. The extent to which we see a wider shift in sentiment towards the asset class remains a key uncertainty.

The Reserve Bank Board next meets on July 6. The Governor is holding a press conference after the meeting indicating that we can expect some significant policy changes.

Westpac anticipates that the Board will decide against extending the Yield Curve Targeting policy from the April 2024 bond to the November 2024 bond. That means it will have passed on an opportunity to reverse the gradual tightening in fixed rates that has occurred since late 2020.

When assessed in conjunction with the withdrawal of the Term Funding Facility, although banks still have around $64 billion to draw down by the end of the month, the clear signal is that financial conditions are likely to gradually tighten.

We also expect the Governor to announce a more flexible approach to Quantitative Easing (QE) with a weekly target of $5 billion being adopted. He is still likely to encourage the market to anticipate a significant purchase program.

The Board assesses the impact of QE in terms of the actual size of the RBA's balance sheet as a proportion of GDP and total bonds on issue. In that regard Australia is well behind other developed economies allowing adequate scope to increase the program.

Westpac expects that purchases will eventually total around $150 billion bringing the RBA's holdings of bonds to around 36% of the total bond supply and around 18% of GDP.

These ratios are modest when compared with other developed economies indicating that the RBA has considerable flexibility to continue with its support of Australia's economic recovery.

As indicated in this survey sustaining that recovery will continue to be reliant on health outcomes over the next year or so until Australia reaches adequate levels of vaccination coverage.

Bill Evans, Chief Economist

Consumer Sentiment – June 2021

	avg*	Jun 2019	Jun 2020	May 2021	Jun 2021	%mth	%yr
Consumer Sentiment Index	101.4	100.7	93.7	113.1	107.2	-5.2	14.5
Family finances vs a year ago	89.3	83.2	77.0	97.9	89.6	-8.5	16.3
Family finances next 12mths	107.5	107.0	105.3	109.5	107.3	-2.0	1.8
Economic conditions next 12mths	91.0	99.3	77.2	121.1	108.7	-10.3	40.8
Economic conditions next 5yrs	91.7	98.2	102.4	115.6	114.0	-1.4	11.3
Time to buy a major household item	126.7	115.5	106.3	121.5	116.5	-4.1	9.6
Time to buy a dwelling	119.2	116.9	107.6	103.5	96.1	-7.1	-10.7
Unemployment Expectations Index	130.0	127.0	127.2	100.2	108.4	8.2	-14.8
House Price Expectations Index	124.8	109.7	80.6	163.8	157.8	-3.6	95.9

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 31 May to 5 June 2021. 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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