BULLETIN

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Consumer Sentiment remarkably resilient in January

The Westpac-Melbourne Institute Index of Consumer Sentiment fell by 2.0% to 102.2 in January from 104.3 in December.

This is a surprisingly solid result given the rapid spread of the omicron COVID variant over the last month. The 2% decline compares to the 5.2% drop seen in the first month of the delta outbreak in NSW, a 6.1% drop heading into Victoria's 'second wave' outbreak in 2020 and the epic 17.7% collapse when the pandemic first hit in early 2020.

Note that the headline Index and its components are all seasonally adjusted to remove a regular holiday-related January lift – the 2% decline in the headline index essentially means this regular lift failed to materialise in 2022. State and sub-group measures are not seasonally adjusted.

While the January sentiment result was resilient overall, responses over the course of the survey week – from January 10 to January 14 – did show a deterioration suggesting some increased anxiety as the week progressed.

The state breakdown provides some clues to the resilience of sentiment overall. Whereas confidence increased in NSW (1.7%) and Victoria (4.1%), it posted significant falls in Queensland (–2.7%), Western Australia (–5.1%) and South Australia (–3.9%). Consumers in states impacted by 'delta' lockdowns appear to have been less unsettled by the rapid spread of the omicron variant than those in states experiencing their first major wave of COVID infections.

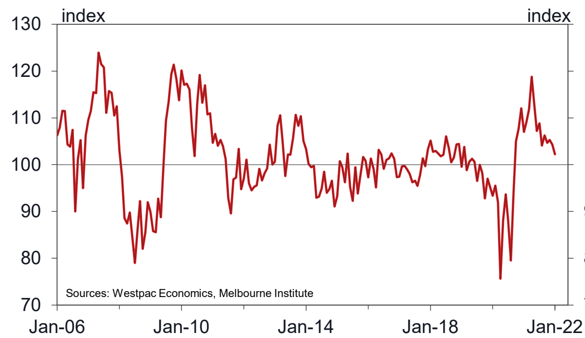
The component detail shows increased concerns about the outlook for both the economy and family finances. These were partially offset by a strong improvement in actual family finances and a slightly more positive attitude towards major purchases.

Consumers' near-term expectations for the economy showed the biggest fall.

he 'economic conditions, next 12 months' sub-index dropped 9.6% from 104.9 in December to 94.8 in January, a swing from cautious optimism to cautious pessimism. Medium-term expectations for the economy were also pared back but remained optimistic overall, the 'economic conditions, next five years' sub-index falling 6.1% to 103.6.

Consumers reported a significant improvement in their finances relative to a year ago This sub-index lifted by 7.5% to 95.6, a nine-month high. That likely reflects a combination of improving incomes – particularly as labour markets rebound – wealth gains from a resurgent housing market and the accumulation of significant 'reserves' due to very high savings rates during lockdowns over the last two years. The latter, estimated to be worth around $250bn, may now be providing consumers with comfort given the return of virus disruptions. These savings will also be important when the omicron threat eases, providing the basis for a strong rebound in spending.

Consumer Sentiment Index



The survey detail gives some evidence that consumers remain inclined to spend despite the omicron surge with the 'time to buy a major household item' sub-index rising 2.8% to 108.9 in January. However, this sub-index has still shown a larger decline on a year ago basis, down 8.3%, than the headline sentiment Index, which fell by 4.5%.

Consumers are unsettled about the outlook for their finances. The 'finances, next 12 months' sub-index fell 2.8% to 108.1.

That nervousness would be consistent with the sharp deterioration in the economic outlook but may also reflect shifting expectations for interest rates. We are now asking consumers about their interest rate expectations every month given the sensitivity and uncertainty around the rate outlook.

In January, 55% of respondents, an outright majority, expected mortgage interest rates to rise over the next 12 months. That compares with 41% when we last ran the question in August and 36% when we ran the question about a year ago in February 2021. This is the highest proportion expecting interest rate rises since February 2018, when, of course, those expected rate increases failed to materialise.

While interest rates look to be more of a concern, confidence amongst respondents with a mortgage has held up well. Sentiment across this sub-group is only down 1.8% over the year and lifted by 2.3% in the January survey.

Growing expectations of interest rate rises may also be starting to impact consumer assessments of the housing market outlook.

Consumers are becoming less bullish on the outlook for house prices. The Westpac Melbourne Institute House Price Expectations Index fell 4.8% to 143.4 in January, its lowest level since November 2020. That said, most Australians still expect prices to rise over the next year rather than fall. Expectations deteriorated in all the major eastern states – down 2.3% in NSW, 10.8% in Victoria and 8.5% in Queensland – but posted a solid 12.6% gain in Western Australia.

Interestingly, consumers that own investment properties reported a significantly larger 12% decline in price expectations and are considerably more downbeat than owner occupiers.

Homebuyer sentiment improved in the month. The 'time to buy a dwelling' index lifted 6.3% but is still down 34% from its November 2020 peak, the latest month only partially reversing a 10.2% decline in December.

This measure is particularly sensitive to shifts in affordability. The January gain may be an early sign that an actual and expected moderation in house prices is starting to see buyer sentiment stabilise. However, any stabilisation is likely to be at relatively low levels, particularly given growing consumer expectations of a rise in mortgage interest rates.

The Westpac Melbourne Institute Unemployment Expectations Index increased by 8.2% to 112.7, marking a significant deterioration (recall that lower reads mean more consumers expect the unemployment rate to fall over the next 12 months). Despite the rise, the index remains well below the long run average of 130 implying that consumers still have significantly better than average expectations for the labour market.

The Reserve Bank Board next meets on February 1. The Governor has indicated that the future of the bond purchase program will be considered at the meeting. He has identified three criteria for the decision: 1) the actions of other central banks; 2) the functioning of the government bond market; and 3) progress towards achieving the Board's inflation and employment objectives. If that expected progress is in line with the Bank's November forecasts, the purchase pace is likely to be scaled back from $4 billion to $2 billion per week. Improved forecasts would see the curtailment of the program altogether.

The decision by the FOMC to accelerate its tapering and some reports that the Bank's actions in the bond market are constraining liquidity support the case for a full wind down.

Developments around omicron in January point to a scaling back in consumer spending in the month of January and a likely downward revision to the Bank's near-term growth forecasts. But this may not be sufficient to indicate 'no net progress' on the employment and inflation front. That will also depend on the employment and inflation reports due this week and next.

Despite evidence in recent speeches that the Governor appears to favour a full wind down Westpac retained its long- held view that it would still choose to scale back rather than fully wind down. That was in response to the sudden emergence of the omicron variant.

The data flow over the next week will determine whether progress on the employment and inflation objectives has been sufficiently encouraging to allow that full wind down and Westpac will review its current forecast.

Bill Evans, Chief Economist, ph (61–2) 8254 8531

Consumer Sentiment – January 2022

Item	avg*	Jan 2020	Jan 2021	Dec 2022	Jan 2022	%mth	%yr
Consumer Sentiment Index	**101.4**	**93.4**	**107.0**	**104.3**	**102.2**	**–2.0**	**–4.5**
Family finances vs a year ago	89.3	82.0	89.3	89.0	95.6	7.5	7.1
Family finances next 12mths	107.5	99.0	108.6	111.2	108.1	–2.8	–0.4
Economic conditions next 12mths	91.1	84.8	102.7	104.9	94.8	–9.6	–7.7
Economic conditions next 5yrs	91.9	87.9	115.6	110.4	103.6	–6.1	–10.4
Time to buy a major household item	126.5	113.4	118.8	105.9	108.9	2.8	–8.3
Time to buy a dwelling	118.5	118.8	124.5	81.9	87.0	6.3	–30.1
Unemployment Expectations Index	129.7	134.0	119.0	104.1	112.7	8.2	–5.3
House Price Expectations Index	124.8	151.5	145.2	150.6	143.4	–4.8	–1.3

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 10 January to 13 January 2022. The data have been weighted to reflect Australia's population distribution.

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