BULLETIN

8 August 2023

Consumer sentiment dips despite easing rate hike fears

- **Westpac-Melbourne Institute Consumer Sentiment dips 0.4% to 81.**
- **Index remains in deeply pessimistic territory.**
- **RBA's rate hike pause again does little to boost confidence.**
- **Inflation still dominating, including recent fuel and energy price rises.**
- **Housing sentiment mixed: deeply negative on purchase, bullish on prices.**
- **Confidence in labour market improves a touch.**

The Melbourne Institute of Consumer Sentiment index dipped 0.4% to 81 in August from 81.3 in July.

Sentiment continues to show only a muted response to the RBA Board's decision to leave the cash rate on hold in recent meetings. The Board opted to leave rates unchanged for a second month in a row at its August meeting, the first consecutive 'on hold' decisions since the tightening cycle began in May last year. Consumer sentiment has only lifted 2.3% in response, with continued pressures on family finances and concerns about the interest rate and economic outlook still weighing heavily on confidence.

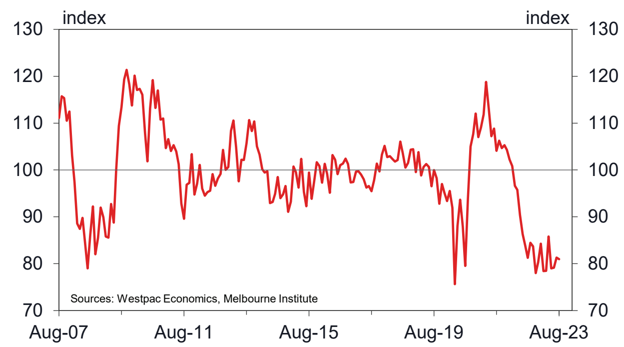
The August survey detail pointed to little or no impact from the RBA's decision to pause. Responses showed no improvement over the course of survey week, sentiment instead declining 4.9% between those surveyed prior to the RBA decision and those surveyed after. The sub-group detail also continued to show a disappointing reaction from the mortgage belt – sentiment amongst consumers with a mortgage down 7.2% in the August month and, 0.8% below its June level despite the two-month pause.

The lacklustre response may be partly due to the RBA's continued warnings that further tightening may still be required. Most consumers are still bracing for further rate rises with over two thirds of those surveyed after the RBA decision expecting rates to move higher over the year ahead, nearly half of this group expecting a rise of over 1ppt. That is an improvement on the July survey, which found nearly three quarters of consumers expecting rates to rise, but in line with the mix of responses seen when the RBA first actively paused its rate rise cycle back in April.

Consumer nerves about the interest rate outlook are likely being compounded by ongoing cost-of-living pressures. While the June CPI report showed slightly better-than-expected reads for inflation, the annual pace of price rises remains high at 6%yr. Consumers may also have been impacted by more recent rises in fuel prices and energy costs.

On fuel: average pump prices surged 17¢ to $1.82/litre between the July and August surveys. This almost certainly contributed to the sharp 12.8% drop in sentiment amongst 18-24 year olds – a sub-group that is unaffected by interest rate changes and more sensitive to petrol prices (sentiment actually rose slightly across other age-groups, up 0.9% on a combined basis).

Consumer Sentiment Index



On energy: regulated power prices rose significantly in July 1, with 'benchmark maximum' rates increasing 20-25% across the major eastern states. On average, electricity costs nationally are expected to rise by less, by just over 7% in the September quarter. But many consumers will be starting to see these price rises impacting their electricity bills.

We have argued previously that sentiment is unlikely to stage a sustained lift from current deeply pessimistic levels until inflation – both as measured officially and experienced by consumers day to day – is much lower and interest rates are more firmly on hold.

For the August month, the component sub-indexes showed deteriorating near-term expectations for the economy offset by a partial recovery in assessments of current finances, other components largely unchanged.

The 'family finances vs a year ago' sub-index rose 3.4% to 64.3, reversing much of the 4.9% fall in July but remaining at an extremely weak level overall. The detail showed particularly strong rises for those in NSW (+16%); amongst freehold homeowners without a mortgage (11%); and consumers with investment properties (+10%) – all pointing to the recovery in housing markets as a significant positive.

The forward view on family finances showed less of an improvement, the 'family finances, next 12 months' sub-index edging up just 0.2% to 89.9. This component showed the biggest pull-back between pre and post-RBA samples (down 11.3%) suggesting there may have some hope of a firmer 'on hold' signal from the Bank. Expectations have still improved 7% over the last two months but have shown a slightly more muted gain for consumers with a mortgage (+5.6%).

Around the economy, near-term expectations were dented significantly but medium term views were largely unchanged. The 'economic outlook, next 12 months' sub-index fell 4% to 78.2, unwinding most of the 5.4% lift in July. The 'economic outlook, next five years' sub-index dipped 0.8% to 93.5.

The improving picture around interest rates and inflation has so far done little to shift attitudes towards spending. The 'time to buy a major household item' sub-index nudged 0.3% higher to 79 in August, up 3.4% since June but still holding around very weak levels by historical standards. The latest retail sales figures show consumers are continuing to rein in spending with a 0.5% decline in real retail sales in the June quarter marking a third consecutive quarterly fall. Our Westpac Card Tracker suggests these cuts continued into July.

Consumers were slightly more positive on labour market prospects in August, although still much less confident than they were at the start of the year. The Westpac-Melbourne Institute Unemployment Expectations Index declined 3.1% to 127.2, a marginal improvement to slightly below the index's long run average (recall that lower index reads mean more consumers expect unemployment to fall in the year ahead). This is broadly consistent with a slowdown in hiring rather than a sharp spike in job-loss fears. That said, there was a notably sharp rise in unemployment expectations amongst those employed in the construction sector, suggesting ongoing difficulties and high-profile business collapses are weighing more heavily on job-loss fears within this industry.

Consumer views on housing show a further widening between bullish price expectations and deteriorating buyer sentiment.

The 'time to buy a dwelling' index fell 5.7% to 72.1 in August, reversing all of the previous month's gain and remaining near extreme historical lows (the long run average is 121). The combination of high interest rates and high prices remains deeply discouraging for buyers. However, regional variations point to a more nuanced picture, buyer sentiment actually improving in Sydney (+7.9%) and relatively steady in Melbourne (–0.2%) but weakening more markedly everywhere else (–12.9% on a combined basis). If nothing else, this suggests there may be 'fear of missing out' factor coming into markets with already very stretched affordability that are starting to see renewed price gains.

Certainly, consumers remain very bullish on the house price outlook. The Westpac Melbourne Institute House Price Expectations Index rose a further 1.3% to 151.2, a new cycle high. Expectations are particularly bullish in NSW (155.2) and South Australia (+160.8) but less so in Victoria (+147.7) and Queensland (149.9).

The Reserve Bank Board next meets on September 5. We expect the Board to again leave rates on hold at 4.1%, with the current cash rate eventually proving to be peak of the cycle.

The decision to leave the cash rate on hold in August made it clear that the Board is now more confident about achieving its objective of returning inflation to the 2-3% target band over a reasonable timeframe. That more confident view was reinforced by revised forecasts in the RBA's August Statement on Monetary Policy which do not support a case for additional tightening. Today's consumer sentiment survey will add to this confidence, showing continued weakness across the consumer that is not suddenly dissipating now that interest rates have gone on hold.

The onus is now on data-flow and economic developments to make a case for any further tightening. And for that case to be strong enough to draw a response from the RBA, surprises will need to be substantial – enough to threaten the RBA's medium term view. While there are risks around the next batch of inflation, wage and labour force updates, these are unlikely to pose enough of a concern to trigger a September hike from the RBA. Beyond September, the case for further moves will become even harder to make as more evidence a slowing inflation and weak consumer spending emerges.

Consumers may not be convinced but we have very likely reached the peak in the interest rate tightening cycle.

Matthew Hassan, Senior Economist, Westpac

Consumer Sentiment – August 2023

Item	avg*	Aug 2021	Aug 2022	Jul 2023	Aug 2023	%mth	%yr
Consumer Sentiment Index	**100.9**	**104.1**	**81.2**	**81.3**	**81.0**	**–0.4**	**–0.3**
Family finances vs a year ago	88.7	91.9	72.1	62.2	64.3	3.4	–10.8
Family finances next 12mths	107.0	107.0	88.2	89.7	89.9	0.2	1.9
Economic conditions next 12mths	90.8	100.4	73.9	81.4	78.2	–4.0	5.7
Economic conditions next 5yrs	92.0	109.2	90.7	94.3	93.5	–0.8	3.2
Time to buy a major household item	125.2	112.0	81.4	78.8	79.0	0.3	–2.9
Time to buy a dwelling	121.4	88.9	78.2	76.4	72.1	–5.7	–7.8
Unemployment Expectations Index	129.2	124.6	103.4	131.2	127.2	–3.1	23.0
House Price Expectations Index	125.8	155.8	97.1	149.3	151.2	1.3	55.7
Interest Rate Expectations Index	154.1	146.1	185.0	174.8	164.3	–6.0	–11.2

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

The survey is conducted by OZINFO & DYNATA. Respondents 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 July to 4 August 2023. 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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