2022 Federal Election: economic and market impact

The 2022 Federal Election continued the trend seen in the last two decades of no single Prime Minister being able to win consecutive elections, making Anthony Albanese our seventh PM this century.

The national two-party preferred split of roughly 52 % Labor vs 48 % Coalition was very close to pre-poll forecasts, and at the time of writing makes a narrow majority government for Labor the most likely outcome- probably taking 77 seats. This was a swing of around 3.9 % from the Coalition to Labor vs 2019; however, most election commentary has focussed on the sharp rise in votes for 'other' parties (with only 68 % of the primary vote going to the major parties).

The Greens and 'Teal independents' enjoyed the largest swing and won a number of key seats, including Monique Ryan in Kooyong (over Josh Frydenberg) and Elizabeth Watson-Brown for the Greens in the inner Brisbane seat of Ryan. The Green (and independent) focus on climate change appears to have resonated far more strongly than in 2019, including in flood impacted regions making the issue far more tangible and current. Other factors that clearly drove voting trends included gender equity, cost of living and the need to establish a federal integrity commission.

The change in government does not materially impact our economic and market forecasts for FY23. Going into election day the unemployment rate had already fallen to 3.9 % (its lowest level since 1974) with expectations of further falls to around 3.5 %. GDP growth was brisk at 4.2 % for 2021 with a similar pace expected for 2022, and the Wage Price Index (for the first quarter) is up to 2.4 %.

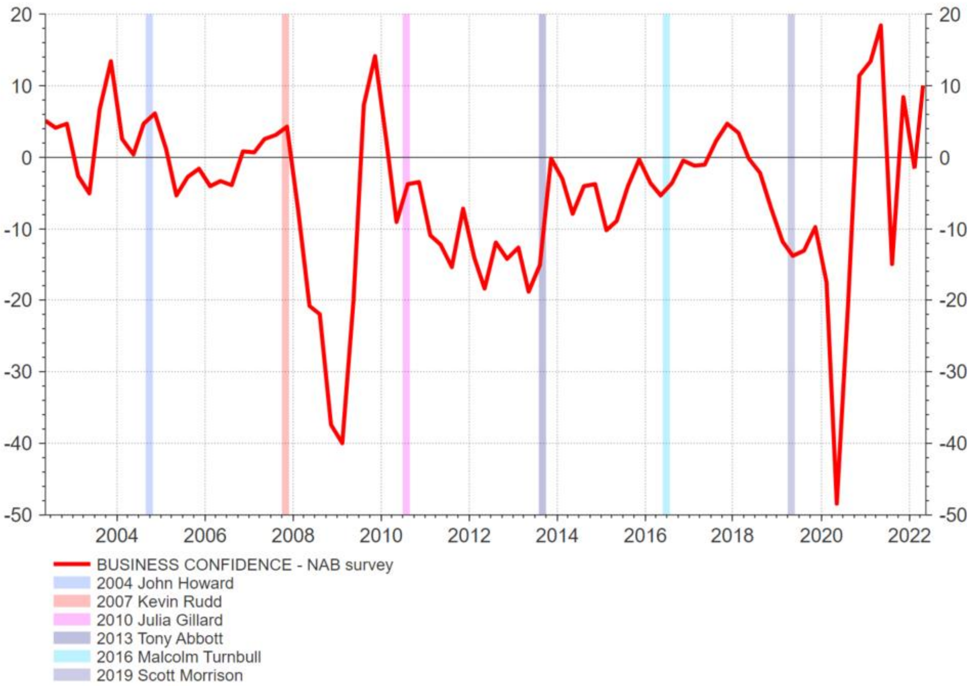
The economy is experiencing strong demand, but in many areas supply is unable to keep up, hence the inflation rate is on the rise. The primary drivers of inflation have been supply-chain bottlenecks, sharply higher energy and commodity prices, and the tail-end of border restrictions from the pandemic. These factors won't change with a change in government, as they primarily come from overseas.

The independence of the Reserve Bank (who have the responsibility of managing inflation) means RBA rate hikes will keep coming irrespective of the election. As a result, our expectations of strong GDP growth in the 4's this year but down to only 2 % next year are unchanged, as is our forecast for jobs growth to strongly continue next financial year.

One impact that may be seen from the election is in business confidence, which had rebounded strongly in mid-2021 (before the Delta lockdowns) and was again above its long-run average in April at +10. Previous elections had typically only seen brief periods of rising confidence after the event, with the exception of the Turnbull victory (refer chart below) - until his replacement in 2018.

At present business confidence is being supported by expectations of the rebound in tourism and the services sector post-pandemic, and as retail trade continues to perform strongly- retail sales are up around 20 % on pre-pandemic levels. Business investment will be very important to ensure that the economic recovery continues as stimulus measures are wound back, including monetary policy.

Business confidence and federal elections



Source: Refinitiv Datastream

Consumer confidence has also been fickle historically after elections, although there have been external factors at play- the GFC in 08/09, the European sovereign debt crisis in 2011 and then the bushfires and the pandemic from late 2019. The latest fall in consumer confidence (refer chart) has been driven by the prospect of sharply higher interest rates- primarily a function of global events such as the Russian invasion of Ukraine.

Consumer confidence and federal elections

Source: Refinitiv Datastream

The policy differences between the two major parties were arguably less pronounced than previous elections, but the Labor victory is expected to see a more aggressive agenda for emission reductions, the establishment of a $15 billion National Reconstruction Fund (for advanced manufacturing, biotech etc), and more investment in tertiary education and aged care. The 'stage three' coalition's tax cuts are not impacted.

New Treasurer Jim Chalmers is expected to hand down his first budget by October, and while government debt is a hot topic and fiscal policy will naturally be important, our AAA sovereign credit rating is very safe with 'net debt to GDP' only around 30 %. Labor have committed to a review of the RBA (as had the Coalition) which Chalmers will oversee in the coming months.

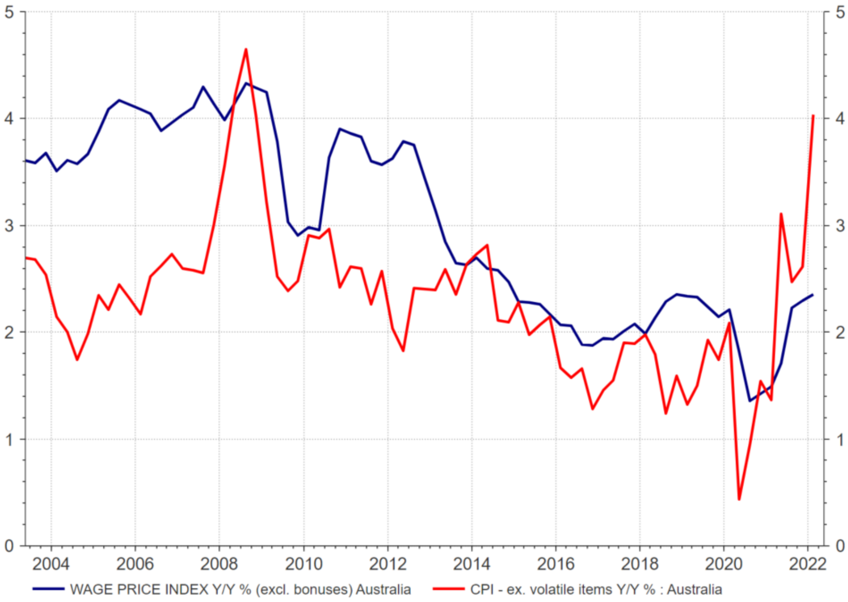
Election implications for financial markets are somewhat limited (assuming a majority government) with the Aussie Dollar, equity markets and bond markets primarily being driven by global factors- the war In Ukraine, China's 'zero-COVID strategy' and the risks of the US economy failing to achieve a soft landing as their interest rates quickly rise. Diplomacy will be quickly in focus with the imminent Quad meeting in Tokyo, and the geopolitical landscape will remain challenging- but with scope for rebuilding diplomatic and trade relations with China.

The Aussie Dollar is currently being supported by commodity prices, but partially offset by the weaker outlook for the Chinese economy. If Labor fails to reach a majority of 76 seats, so would have to rely on the independents or Greens for policy support, this could be a drag on the Aussie Dollar amid political uncertainty, however a small majority (with healthy crossbench debate) is more likely based on the latest data .

Two hot topics in the election were the recent increase in cost of living, and the lack of wages growth. As the chart below shows, the Wage Price Index had been increasing at a slower pace for some time (from above 4 % pre-GFC to below 1.5 % in the pandemic) although inflation also trended lower over this period: it is only since early 2021 that inflation has started to outpace wages growth. Over the next year inflation will remain elevated (CPI approaching 6 % and core inflation in the 4's) while wages growth will probably reach the high 3's thanks to tight labour markets. The bigger issue is how to achieve sustainable real wages growth in the medium term, which in a recent speech Albanese indicated would be assisted by productivity enhancement (via renewable energy, infrastructure investment, skills and training, and other reform).

The appetite for more aggressive structural reform (tax, education, healthcare and IR) will be very interesting to observe in the months ahead - but in the short term the cost of living (i.e. inflation) will remain high and above wages growth, while RBA rate hikes will reduce demand next year, slowly reducing inflationary pressures. By early 2024 hopefully wages growth will exceed inflation, i.e. real wages growth, as had been the case for most of the last two decades.

Wages growth vs Inflation



Source: Refinitiv Datastream

In summary, our most recent baseline forecasts for the rest of 2022 and for 2023 are unchanged despite the change in government; namely

- GDP growth of around 4.5 % over 2022 but only 2 % growth in 2023
- Unemployment down to 3.5 % by Q3 2022 but slightly higher (around 3 ¾ % in 2023)
- RBA rate hikes to 1.75 % by year end, peaking (or plateauing) below 2.75 % in 2023
- AUD / USD back up to 78 c by year end, and above 80 cents by mid-2023

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