AUSTRALIAN GDP PREVIEW

Q3 2018 – Healthy Momentum Continues

NAB Group Economics

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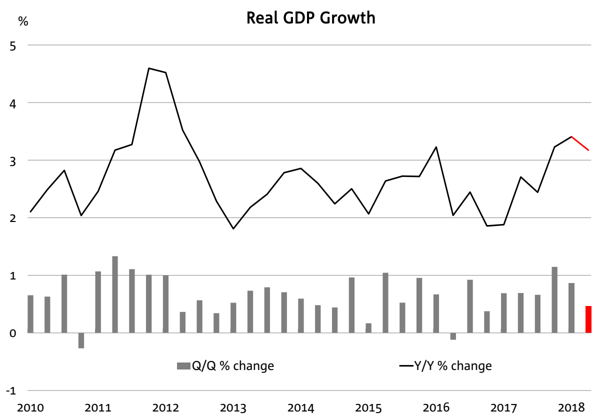
<u>Bottom line</u>: Quarterly growth appears to have slowed in Q3 following strong outcomes in the first half of the year. We expect output to rise by +0.5% q/q and 3.2% y/y. Despite slowing in quarterly terms, the economy looks to have performed relatively well over the past year – growing well above trend - with growth supported by net exports, non-mining business investment and the government sector. Consumption was stronger than expected in the first half but we expect a slowing from here - closer to 2½% annually. While growth looks to be continuing at a healthy rate, the level of remaining spare capacity and how quickly this is reduced through labour market tightening while feeding into faster wage growth and inflation is key to the timing of any rate increase by the RBA.

- **Next Wednesday's GDP figures are forecast to show the economy growing at slightly slower quarterly rate of 0.5% q/q but that year-ended growth will still show a solid 3.2% y/y.** Consumption looks to have slowed following two better than expected prints and we expect dwelling investment to make a small subtraction from growth alongside the cooling in the housing market. Business investment looks to have weakened slightly this quarter – though we think this is related to quarterly volatility rather than an underlying weakness. Against this, we expect net exports and government spending to record solid outcomes in Q3. That said, there may be some downside risk to government investment with the weak outcome in public sector work done released earlier in the week.
- **Looking forward**, we expect growth over the next two years to be driven by public infrastructure investment, business investment and further growth in net exports, with consumption to only see modest growth. Falling house prices remain a risk, though the extent of spill overs to both household consumption and dwelling investment remains highly uncertain. Our outlook for dwelling investment is for a small decline over the forecast period, with approvals for new dwellings having eased, though the current pipeline of work yet to be done will provide some support.
- The **uncertainty around our forecasts** is still centred on **consumption.** We have 0.5% q/q for Q3 though both official retail sales volumes and our NAB Cashless Retail Sales index suggest there is some downside to this. Indeed, consumption has surprised on the upside in the previous two quarters given the headwinds faced by households. Going forward, we expect only modest growth in consumption with weak wage growth, high indebtedness, a low savings rate and slower growth in housing wealth continuing to weigh.
- National accounts measures of **wages** and **inflation** will be another marker of whether growth in household earnings and disposable income are seeing a lift from an increase in wage growth. The WPI for Q3 showed a small increase in the pace of wage growth, but overall it indicated wage pressure remains low. Q3 data for the CPI suggest that inflation pressure also remains meek. The trend in unit labour costs – a measure of wage pressure adjusted for productivity growth – will be an important indicator of how wage pressures evolving for business.
- **Monetary policy implications**: While the release for Q3 will provide an update on the overall pace of growth, as well as some insights into how different sectors are travelling, it will not be a view changer for monetary policy. These data are now dated and will be best viewed as a check-point along the way. The latest set of RBA forecasts continue to point to the next move in rates being up, but that any move is likely some time away. Embodied in these forecasts is a relatively strong rate of economic growth and further, gradual, erosion of spare capacity in the economy. The starting point for inflation is relatively weak and price pressures are still expected to lift only slowly. The pace at which spare capacity in the economy is reduced, and how this translates to wage growth and inflation remains key.



Real GDP Forecasts

	Q/Q		Y/Y	Contribution to Q/Q
	Jun-18	Sep-18	Sep-18	Sep-18
Household Consumption	0.7	0.5	2.8	0.2
Dwelling Investment	1.7	-1.5	4.1	-0.1
Underlying Business Investment	-0.7	-0.7	-0.4	-0.1
Underlying Public Final Demand	0.6	1.0	4.2	0.2
Domestic Final Demand	**0.6**	**0.3**	**2.8**	**0.4**
Stocks (a)	0.0	-0.2	0.1	-0.2
GNE	**0.5**	**0.1**	**2.9**	**n.a.**
Net exports (a)	**0.1**	**0.3**	**0.0**	**0.3**
Exports	1.1	0.6	3.3	0.1
Imports	0.4	-0.8	3.0	0.2
Real GDP	**0.9**	**0.5**	**3.2**	**n.a.**

(a) Contribution to GDP growth

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