AUSTRALIAN ECONOMIC UPDATE

GDP Q3 2019 – Consumer Growth Slows Further

4 December 2019

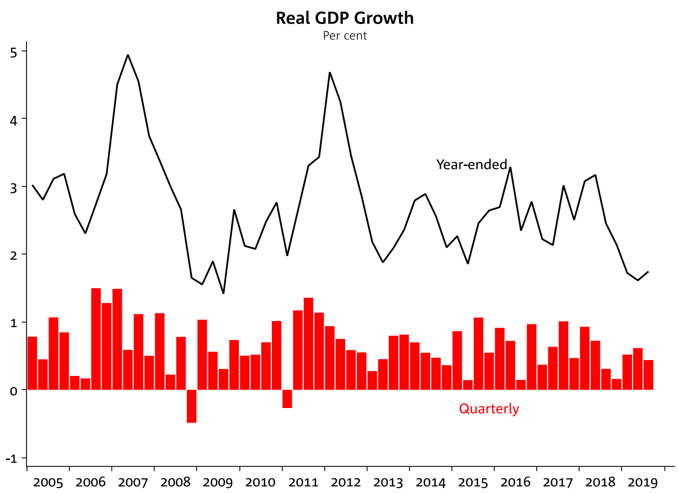
Bottom line: Headline GDP growth rose 0.4% q/q% to be 1.7% higher over the year. In headline terms, year-ended growth has improved marginally over the past three quarters but private sector demand continues to fall – subtracting 0.3ppt from growth over the past year. The pattern of growth in the quarter was similar to recent quarters with household weakness offset by rising exports and public spending, alongside falling dwelling investment. The RBA's forecast of a return to above-trend growth, driven by a recovery in household consumption and stabilisation in dwelling investment is challenged by these figures, particularly when consumption barely grew in the quarter. Also, there appears to be significant downside risk to the Bank's optimistic outlook for business investment based given investment fell again in the quarter and with ongoing weakness in the NAB business survey. While public spending and exports have underpinned the increase in GDP, this is unlikely to lead to ongoing strong growth in employment. The unemployment rate unlikely to fall further and it is likely that the RBA will need to ease policy further to boost employment and reduce unemployment; we have changed our rate call (see the our rates note also released today) to include a further cut to 0.25% by June 2020, with the prospect of a move to QE in H2 2020 should the data play out weaker than we forecast.

In Q2, weak private demand was again driven by a fall in dwelling investment which is now down 9.6% over the year and consumption growth which slowed to 1.2% y/y – its weakest outcome since the global financial crisis. Business investment recorded another weak outcome in the quarter falling by 2.0%. Public-sector spending made a solid 0.3ppt contribution, as did net exports, which added 0.2ppt to GDP. Both the production and income measures of GDP were weaker than the expenditure side in this set of accounts but in year-ended terms GDP(P) continues to outpace the growth in the other two measures

Looking forward, we expect year-average growth of around 1¾% in 2019, rising to around 2.0% in 2020 and a little higher in 2021 – an improvement but still below trend. We expect household sector weakness to persist, with dwelling investment to record another significant fall in 2020. Consumption growth is expected to remain weak, with the constraints of slow income growth to persist and debt levels to remain high. The outlook for business investment is clouded, with business confidence and conditions at low levels. While mining sector investment should soon reach a trough, there is some risk that the non-mining sector remains weak. Key offsets to the weakness in private demand will be ongoing strength in public sector spending. The continued roll-out of the NDIS will likely see further rises in government spending and the pipeline for infrastructure remains high. In the near term, exports will contribute to growth before they plateau when LNG production reaches full capacity.

Key figures

Key aggregates	q/q % ch		y/y % ch
	Jun-19	Sep-19	Sep-19
GDP (A)	0.6	0.4	1.7
GDP (E)	0.5	0.5	1.7
GDP (I)	0.7	0.4	1.6
GDP (P)	0.7	0.4	1.9
– Non-Farm GDP	0.6	0.5	1.9
– Farm GDP	-0.2	-1.4	-5.9
Nominal GDP	1.5	1.1	5.5
Real gross domestic income	1.0	0.5	3.6
Real net national disposable income per capita	1.2	0.5	3.3
Terms of trade	1.4	0.4	7.8



Source: National Australia Bank, Macrobond

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HIGHLIGHTS

- **Household consumption** growth printed a weak 0.1% q/q in Q3 – even with the significant boost to income from tax cuts early in the quarter. At 1.2% y/y consumption growth has slowed to its weakest rate since the GFC. The drivers of consumption growth in the quarter were increases in health, rec & culture and financial services. This was offset by weakness in largely discretionary categories (as well as transport). Over the year, spending on 'discretionary' items has been very weak, though growth in spending on essentials has also slowed. Similarly, spending on goods has weakened significantly, with services holding up better.
- **Underlying business investment** declined by -2.0% q/q, following on from a (smaller) fall in the previous quarter. Both underlying machinery & equipment (-4.5% q/q) and non-dwelling construction (-1.6% q/q) investment declined. Within non-residential construction, engineering construction saw a large fall while new building construction increased. The overall fall in business investment was largely driven by mining. Mining sector investment declined 7.8% q/q while non-mining sector investment increased 1.2% q/q.
- **Dwelling investment** fell 1.7% in the quarter driven by a fall in investment in new dwellings (-2.8%) which was partially offset by an increase in alterations & additions (0.6%). Over the year dwelling investment has fallen 9.6%. This result is unsurprising given the weakness in work done, and the ongoing weakness in dwelling approvals suggests there may be more to come. The decline was driven by a fall in NSW, though also declined across each of the other states, with the exception of Victoria in the quarter.
- **Government demand** again grew strongly. Underlying public demand grew by 1.7% q/q (the same pace as in the September quarter), contributing 0.4ppts to GDP growth. While government consumption growth moderated (to a still decent 0.9% q/q) there was a notable rebound in underlying public investment which grew by 5.4% q/q (but is only 2.1% higher than a year ago – largely unchanged from recent quarters). The slowdown in public consumption growth was driven by a fall in state & local consumption, while federal government spending remained robust which the ABS attributes to spending on disability and aged care services.
- **Net exports** added 0.2ppts q/q to GDP growth with export volumes rising (0.7% q/q) while imports declined (-0.2% q/q). Over the year to Q3 net exports have added 1.1 ppts to GDP growth. The decline in import volumes included a large fall in capital goods imports (-5.6% q/q), while consumption goods imports again declined consistent with the weakness in consumer spending. Export growth was driven by non-monetary gold exports (up 31% q/q) with other goods exports falling as resource exports eased (after the strong growth in Q2) as did manufacturing and rural exports. Rural export volumes have now fallen 11% over the last year. In contrast, services exports continue to perform strongly (1.6% q/q).
- **Compensation of employees rose by 1.1% in the quarter.** While employment continued to rise, average COE per employee also rose a solid 0.7% in the quarter. COE per hour declined sharply in year-ended terms in the quarter. Household income growth saw a significant boost from tax cuts in the quarter, but an increase in the savings rate saw households hold onto these tax cuts and consumption growth slow further.
- **Nominal unit labour costs growth eased in the quarter, to a moderate 0.6% q/q.** Over the year labour costs have risen 3.0%. Though volatile, this suggests that there has been some pickup in inflationary pressure since early 2018, notwithstanding the slowing in Q3. Our assessment is that overall inflationary pressure remains weak.
- **By industry,** healthcare & social assistance provided the biggest contribution to growth (0.2ppt on a quarterly basis), followed by public administration and safety, professional services and mining (each 0.1ppt). Strong public spending, underlined by programs such as the NDIS, alongside mining production, continues to be the major source of growth in the Australian economy. Meanwhile, construction continues to contract, while industries dependent on consumer spending, such as retail, remain very weak. The weakest industry in Q3 was agriculture, forestry and fishing – hardly surprising given the impact of the drought.
- **By state,** growth was largely confined to the south-east of the country. The ACT was the strongest performer, growing 1.1% q/q, followed by Tasmania (0.8%), Victoria (0.4%) and New South Wales (0.3%). The ACT and Tasmania enjoyed above average household consumption (0.4% and 0.5% respectively), while Victoria and New South Wales saw much more subdued household consumption, instead being buoyed by private investment in Victoria and public investment in New South Wales. The situation outside the south-east was much weaker in Q3. Queensland saw state final demand growth of just 0.1%, with higher government investment, lower government consumption and flat household consumption. The Northern Territory was flat while Western Australia fell 0.2%, largely reflecting a lower mining investment. South Australia fell 0.3%, with a slowdown in energy and mining related investment detracting from growth.
- **Farm GDP** continues to contract amid a severe drought in New South Wales and parts of Queensland and weakening conditions in the west. Farm GDP fell 1.4% q/q and 5.9%y/y. Lower livestock slaughter and poor winter crop production were the major contributors to the fall in the national accounts measure. We see a national wheat crop of 15.5mmt (well below the "average" season of around 24mmt), led by a moribund season in New South Wales but also a poor finish in Western Australia. Forecasts point to a hot and dry summer.

SUMMARY CHARTS AND TABLES:

GDP (E) by component

GDP Expenditure Components	q/q % ch		y/y % ch	Contribution to q/q % ch
	Jun-19	Sep-19	Sep-19	Sep-19
Household Consumption	0.3	0.1	1.2	0.1
Dwelling Investment	-3.7	-1.7	-9.6	-0.1
Underlying Business Investment^	-0.4	-2.0	-1.7	-0.2
Machinery & equipment	3.1	-4.5	-2.2	-0.2
Non-dwelling construction	-4.5	-1.6	-4.6	-0.1
New building	-4.9	3.0	4.2	0.1
New engineering	-4.0	-5.9	-12.2	-0.2
Underlying Public Final Demand	1.7	1.7	5.2	0.4
Domestic Demand	**0.3**	**0.2**	**0.9**	**0.2**
Stocks (a)	-0.4	0.1	-0.3	0.1
GNE	**0.0**	**0.3**	**0.6**	**0.3**
Net exports (a)	**0.5**	**0.2**	**1.1**	**0.2**
Exports	1.3	0.7	3.3	0.2
Imports	-1.1	-0.2	-1.5	-0.1
GDP	**0.6**	**0.4**	**1.7**	**0.4**

(a) Contribution to GDP growth ^ Excluding transfers between the private and public sector

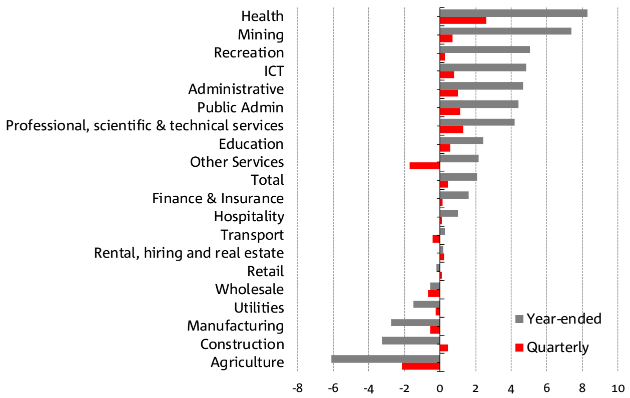
INCOME MEASURES

Income measures	q/q % ch		y/y % ch
	Jun-19	Sep-19	Sep-19
Real GDI	1.0	0.5	3.6
Real net disposable income per capita	1.2	0.5	3.3
Compensation of employees	1.4	1.1	5.0
Average compensation of employees (average earnings)	1.0	0.7	2.9
Corporate GOS	2.1	1.5	10.3
Non-financial corporations	2.5	1.7	11.9
Financial corpoarations	0.7	0.5	4.7
General government GOS	1.4	1.3	5.9
Productivity & unit labour cost			
GDP per hour worked	0.5	-0.2	-0.2
GVA per hour worked mkt sector	0.4	-0.1	-0.2
Non-farm nominal unit labour cost	1.4	0.6	3.0
Non-farm real unit labour cost	0.4	0.0	-0.9

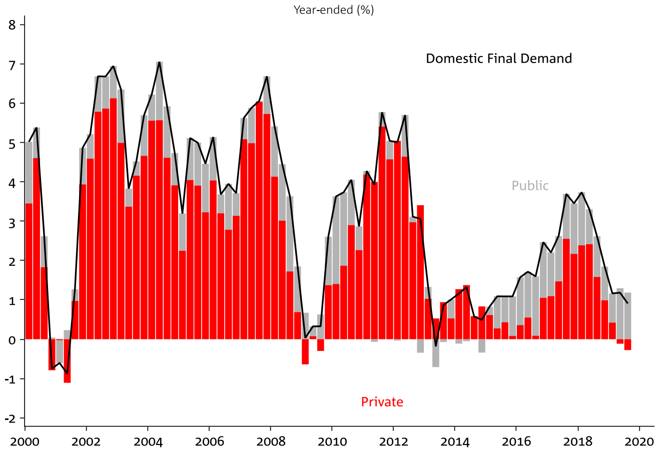
State final demand

State/ Territory	Q/Q		Y/Y
	Jun-19	Sep-19	Sep-19
TAS	0.4	0.8	3.3
ACT	0.6	1.1	2.4
VIC	0.6	0.4	1.8
QLD	0.1	0.1	1.3
NSW	0.1	0.3	0.6
SA	-0.1	-0.3	0.2
WA	1.4	-0.2	0.0
NT	-1.0	0.0	-5.5

Industry GVA Growth

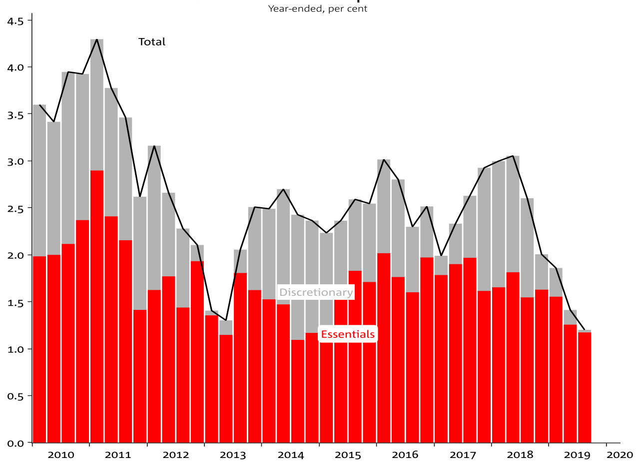


Domestic Final Demand Growth
Year-ended (%)



Source: National Australia Bank, Macrobond

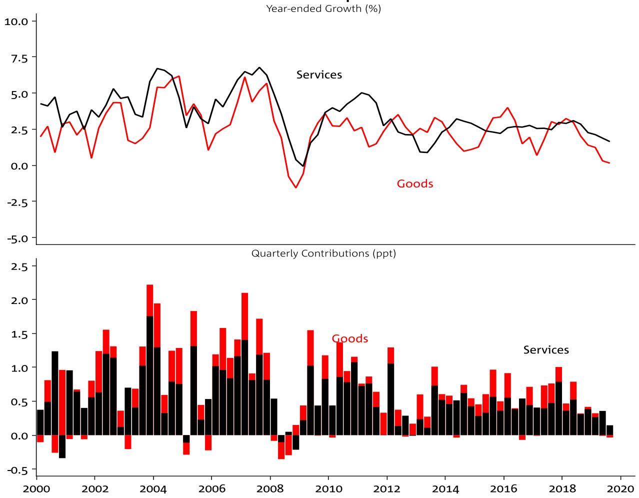
Real Household Consumption Growth
Year-ended, per cent



Source: National Australia Bank, Macrobond

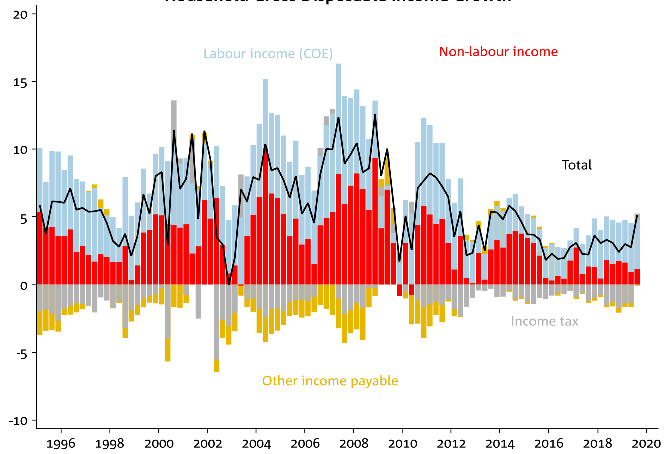
Household Consumption Growth

Year-ended Growth (%)



Source: National Australia Bank, Macrobond

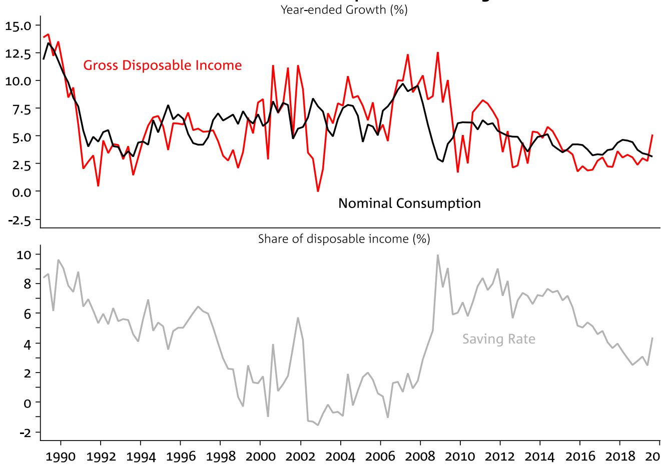
Household Gross Disposable Income Growth



Source: National Australia Bank, Macrobond

Household Consumption and Saving

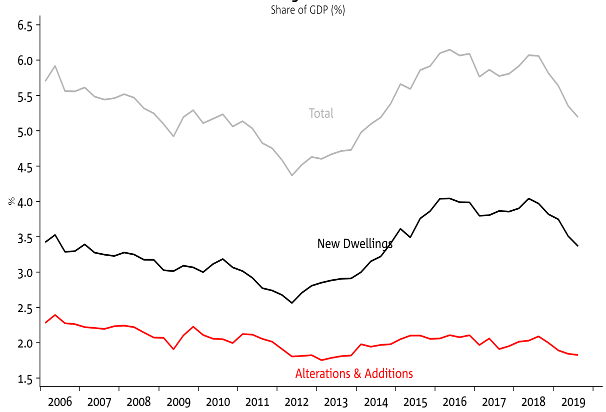
Year-ended Growth (%)



Source: National Australia Bank, Macrobond

Dwelling Investment

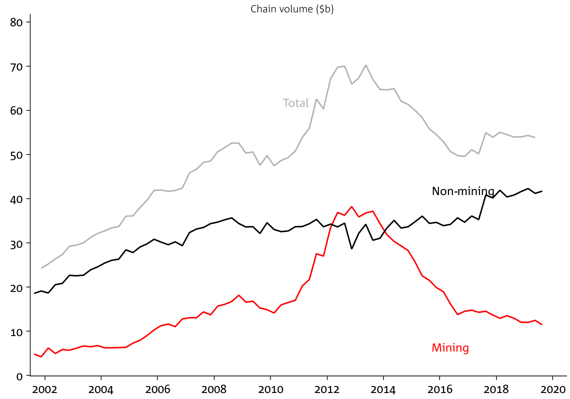
Share of GDP (%)



Source: National Australia Bank, Macrobond

Business Investment

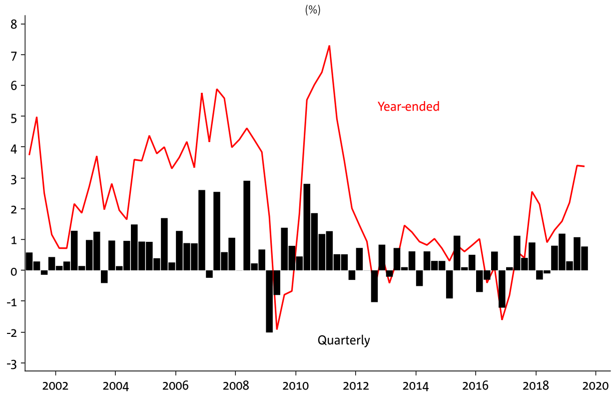
Chain volume ($b)



Source: National Australia Bank, Macrobond

Nominal Unit Labour Cost Growth

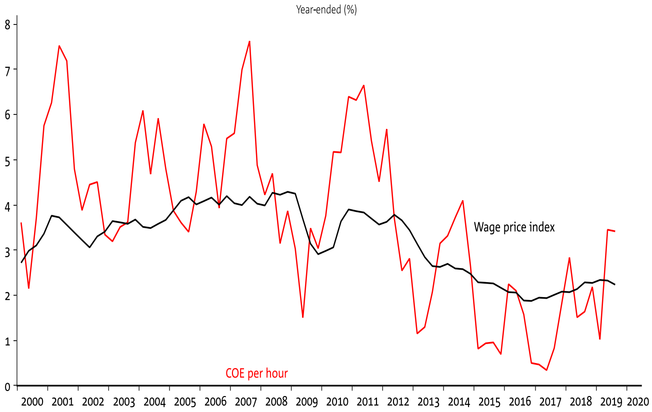
(%)



Source: National Australia Bank, Macrobond

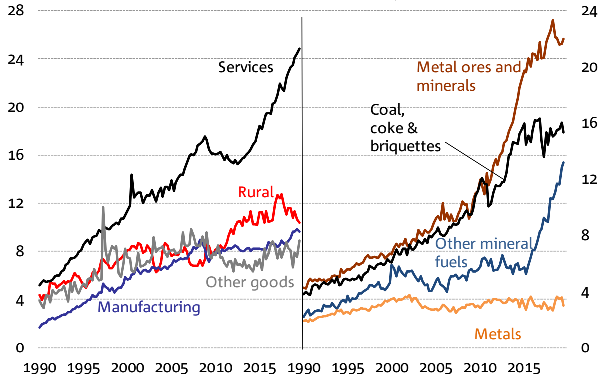
Income Growth

Year-ended (%)



Source: National Australia Bank, Macrobond

Export volumes, quarterly



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