AUSTRALIAN ECONOMIC UPDATE

GDP Q3 2020 – A strong rebound as the recovery begins

2 December 2020

Bottom line: **GDP rose by a large 3.3% in Q3, following the sharp 7% fall in Q2. As expected consumer spending drove the rebound amid the reopening across most of the economy as the virus was contained. Victoria was the clear exception, with spending falling a further 1% in the quarter, after seeing strict lockdowns for much of Q3 –in contrast with the sharp 11% rise across the rest of Australia. Nevertheless, the overall turnaround in consumer spending, housing activity and stocks, supported by ongoing strength from the public sector, more than offset a large drag from net exports and another notable fall in business investment. As a result, today's data mark a strong start to the economic recovery, although the level of activity remains 4.2% below pre-virus levels and down 3.8% from a year ago. NAB continues to expect another strong rise of around 2% in Q4, as Victoria exits lockdown and solid growth over 2021 so that activity recovers to pre-virus levels by the end of next year.**

Today's result was driven by a strong rebound in consumer spending, which rose 7.9% and added 4pp to GDP, after a record 12.5% fall in Q2. Spending had collapsed in Q2 amid COVID-19 restrictions and fears, but the easing of restrictions across most of the country, saw spending rebound 11% outside of Victoria. In contrast, the strict stage 4 lockdown in Melbourne saw Victorian consumer spending fall a further 1% in Q3, after a 14% fall in Q2. That said, with the Victorian outbreak eliminated, NAB expects Q4 to see a strong rebound in Victorian consumer activity, where our transactional data has already shown a strong uplift in the state.

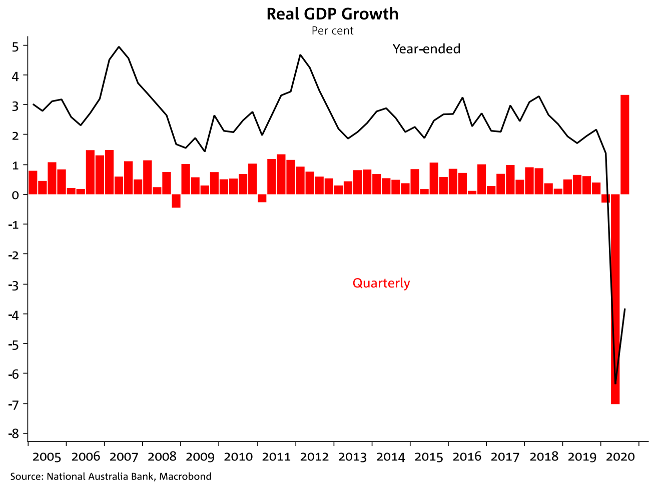
Dwelling investment rose modestly (+0.6%), likely supported by the governments Homebuilder program, and a turnaround in sales activity saw a sharp rise in residential transfer costs, adding 0.3pp to GDP. In combination with the strength in consumer spending, these factors more than offset drags from business investment (-4.1%) and net exports (1.9pp from growth). Elsewhere, the public sector remains strong, up 1.8% in Q3, as key health services (including elective surgeries) resumed.

Looking forward, we expect another strong rise of around 2% in the December quarter and solid growth over 2021. Additional gains in consumer spending, supported by the end of Victoria's lockdown, should support a healthy recovery in activity. Further, dwelling investment has begun to rise again and business investment should turn, where both are likely to be supported by government incentives. As such, NAB forecasts GDP to have recovered pre-virus levels by the end of 2021.

That said, the recovery will face the ongoing headwind of high unemployment. NAB forecasts a peak of around 7.4% in Q4 2020, followed by a decline to under 6% at the end of 2022. Despite the steady improvement, high unemployment will weigh on wages growth, which is extraordinarily weak, and limit the strength of consumer spending. As such, beyond the momentum of the initial recovery, growth is likely to slow into 2022. There also remains a large number of risks to the outlook, although on the health front a potential vaccine and close to zero new case numbers in Australia is promising. In our view, fiscal support will still be needed to ensure a sustainable recovery, where to date fiscal stimulus has been key for limiting the hit to employment and supporting household income. We expect the RBA will assist, at the margin, with an extension to its QE program likely next year.

Key figures

Key aggregates	q/q % ch		y/y % ch
	Jun-20	Sep-20	Sep-20
GDP (A)	-7.0	3.3	-3.8
GDP (E)	-7.0	3.2	-3.9
GDP (I)	-7.2	3.5	-3.8
GDP (P)	-6.9	3.3	-3.7
– Non-Farm GDP	-7.1	3.4	-3.7
– Farm GDP	-2.4	-2.3	-11.7
Nominal GDP	-7.4	3.7	-3.9
Real gross domestic income	-6.8	3.5	-4.5
Real net national disposable income per capita	-7.6	4.8	-4.5
Terms of trade	0.8	0.7	-2.5



HIGHLIGHTS

- **Household consumption** rebounded by 7.9% (4ppt contribution) in Q3 following the 12.5% decline in Q2. At over 50% of GDP, household spending was the key driver of the strong rebound in Q3, although it is yet to fully recover. Services consumption rose strongly, unwinding some of the restriction-driven declines in Q2. Spending on *health*, *hotels, cafes & restaurants* and *recreation & culture* made the largest contributions to growth in the quarter. Overall consumption remains around 6.8% below its pre-COVID level and while tourism-heavy transport services will be weak for some time, it is likely consumption will continue to rebound strongly in Q4 as restrictions (particularly in Victoria were eased further).
- **Underlying business investment** was a weak spot in Q3, declining by 4.1% q/q (as it did in Q2). While the weakness in business investment pre-dates COVID it materially worsened over the last two quarters. Machinery and equipment, new building and new engineering construction all recorded large falls. After defying the general slowdown in business investment in previous quarters, mining sector investment was down 5.2% q/q as the fall in global demand and commodity prices caught up with it.
- **Dwelling investment** rose 0.6% in the quarter, with a fall in new construction (-2.1%) offset by a notable increase in renovation activity (+5.1%). By state, NSW and QLD saw increases in dwelling investment – with falls in new construction more than offset by increased renovations. Investment was flat in WA , while SA, VIC saw falls in investment.
- **Government demand** was again robust (1.8% q/q following 1.9% q/q in Q2). Government consumption growth moderated to 1.4% q/q due to fall in state & local government spending (although the latter was still 6% higher than a year ago). However, after falling in Q2, underlying public investment rebounded (3.3% q/q).
- **Net exports** subtracted 1.9ppts from quarterly GDP growth as exports recorded another large fall while imports rebound strongly. The 6.5% q/q rise in real imports was driven by goods imports and is consistent with the rebound in domestic demand in the quarter. Goods imports are basically back at the their pre-COVID-19 (q4 2019) level while service debits are still down more than 50% due to the collapse in travel. In contrast, exports fell by 3.2% q/q; their fourth consecutive quarterly decline, leaving them almost 15% lower than a year ago. While service exports have seen the largest decline due to travel restrictions, goods exports have also weakened. In Q3, commodity exports again fell (mainly in rural and resources ex non-monetary gold) despite a partial recovery in the global economy, and possibly reflects still depressed global demand and China trade restrictions.
- The **savings rate** decreased slightly to 18.9% but remains elevated after reaching a record high last quarter. Household disposable income grew 3.4% reflecting increases in both labour and non-labour income in the quarter. This was more than offset by the increase in consumption in the quarter. As consumption continues to recover we expect the savings rate will normalise and fall back towards pre-COVID levels. The waning in household support will also contribute to a normalisation going forward.
- **State final demand** rebounded strongly in all states and territories in Q3 except Victoria, reflecting a strict lockdown in Victoria as the rest of the country reopened. NSW and Queensland (+6.8% q/q) recorded the largest increases in state final demand, with SA (+6.7%) close behind. Queensland and the ACT are the only jurisdictions where state final demand was higher than a year ago. In contrast, state final demand declined by 1.0% q/q in Victoria, although a bounce in Victorian state final demand is likely in Q4 given the easing in restrictions.
- The September quarter saw large swings across many **industries** as most states (excluding Victoria) bounced back following the end of lockdowns. Accommodation and food services rose 41% q/q, seeing the second biggest contribution to growth (0.6ppt, just below health care and social assistance on 0.7ppt), although it is still down 20% y/y. Five industry categories (accommodation and food services, transport, postal and warehousing, administrative and support services, arts and recreation services and other services) recorded double digit falls over the past year. Retail trade continued to stand out as a strong performer (up 5.6% q/q), given elevated sales. Construction bounced back, led by residential, while mining was the biggest subtraction from GDP in the quarter (-0.2ppt contribution to GDP growth).
- **Farm GDP** fell 2.3% q/q and by 11.7% y/y in the September quarter. While these figures appear rather lacklustre, the substantially better climate conditions this year is driving herd rebuilding. This sees lower throughput through abattoirs, such that lower meat production is a drag on farm GDP in the near term. However, overall, we are optimistic about agricultural production, particularly with ABARES forecasting the second biggest winter crop on record this season and the prospect of a wetter than average summer in line with the La Nina event currently underway.

SUMMARY CHARTS AND TABLES:

GDP (E) by component

GDP Expenditure Components	q/q % ch		y/y % ch	Contribution to q/q % ch
	Jun-20	Sep-20	Sep-20	Sep-20
Household Consumption	-12.5	7.9	-6.5	4.0
Dwelling Investment	-5.2	0.6	-7.6	0.0
Underlying Business Investment^	-4.1	-4.1	-9.2	-0.5
Machinery & equipment	-8.1	-3.2	-11.6	-0.1
Non-dwelling construction	-0.1	-7.4	-9.3	-0.4
New building	-3.2	-6.1	-11.8	-0.2
New engineering	3.0	-8.5	-6.8	-0.2
Underlying Public Final Demand	1.9	1.8	6.2	0.5
Domestic Demand	**-7.5**	**4.5**	**-3.5**	**4.3**
Stocks (a)	-0.5	0.8	0.2	0.8
GNE	**-8.1**	**5.4**	**-3.3**	**5.1**
Net exports (a)	**0.8**	**-1.9**	**-0.7**	**-1.9**
Exports	-7.5	-3.2	-14.9	-0.7
Imports	-12.8	6.5	-13.9	1.2
GDP	**-7.0**	**3.3**	**-3.8**	**3.3**

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

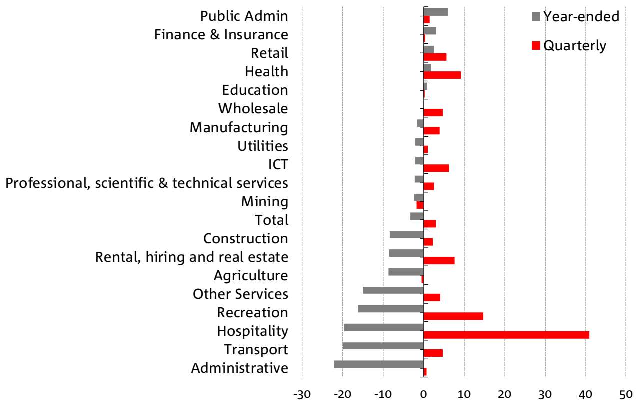
INCOME MEASURES

Income measures	q/q % ch		y/y % ch
	Jun-20	Sep-20	Sep-20
Real GDI	-6.8	3.5	-4.5
Real net disposable income per capita	-7.6	4.8	-4.5
Compensation of employees	-2.3	2.3	1.5
Average compensation of employees (average earnings)	3.2	0.4	4.0
Corporate GOS	13.9	3.2	14.4
Non-financial corporations	17.9	3.8	17.8
Financial corporations	-0.9	0.8	1.1
General government GOS	1.4	1.5	5.5
Productivity & unit labour cost			
GDP per hour worked	3.4	-1.1	3.1
GVA per hour worked mkt sector	4.4	-2.0	2.8
Non-farm nominal unit labour cost	-9.7	-0.4	-9.4
Non-farm real unit labour cost	-9.4	-0.8	-9.3

State final demand

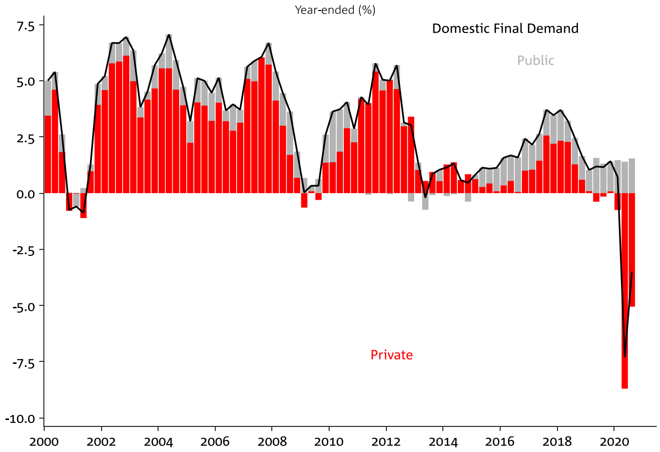
State/ Territory	Q/Q		Y/Y
	Jun-20	Sep-20	Sep-20
ACT	-1.7	2.0	3.6
QLD	-6.1	6.8	0.7
NT	-4.9	6.0	-0.1
WA	-6.4	4.9	-0.7
SA	-6.3	6.7	-0.8
TAS	-8.0	5.5	-3.2
NSW	-8.8	6.8	-3.3
VIC	-8.5	-1.0	-9.8

Industry GVA Growth



Domestic Final Demand Growth

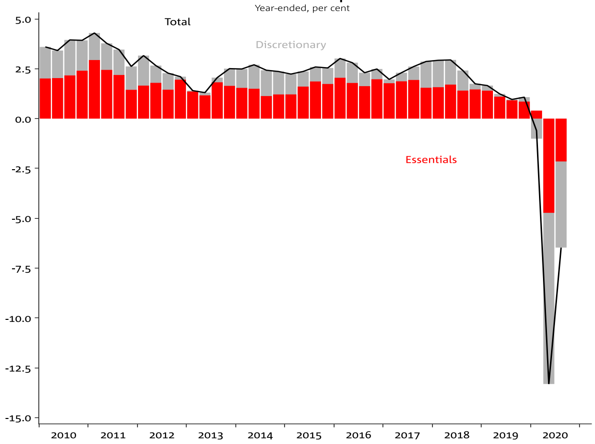
Year-ended (%)



Source: National Australia Bank, Macrobond

Real Household Consumption Growth

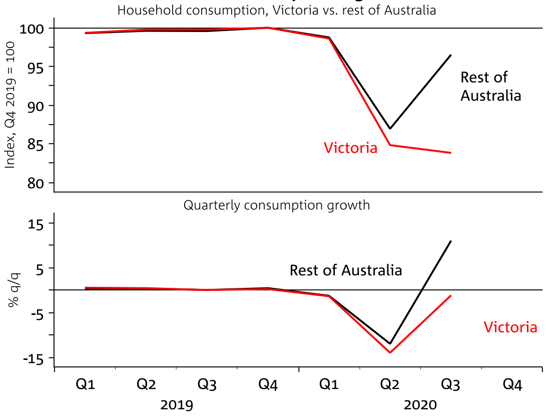
Year-ended, per cent



Source: National Australia Bank, Macrobond

Consumer spending

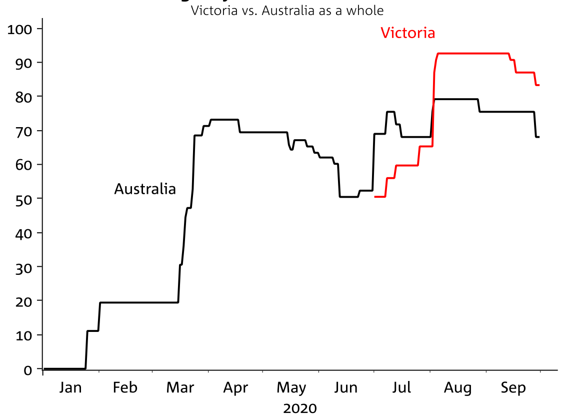
Household consumption, Victoria vs. rest of Australia



Source: National Australia Bank, ABS

Stringency of COVID-19 measures

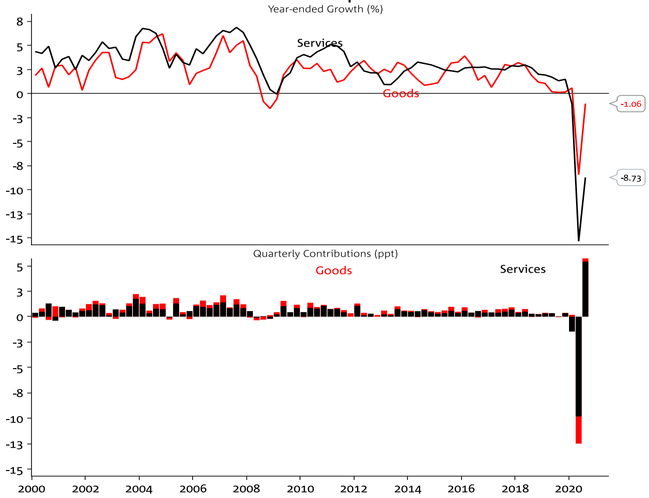
Victoria vs. Australia as a whole



Source: National Australia Bank, ABS, University of Oxford

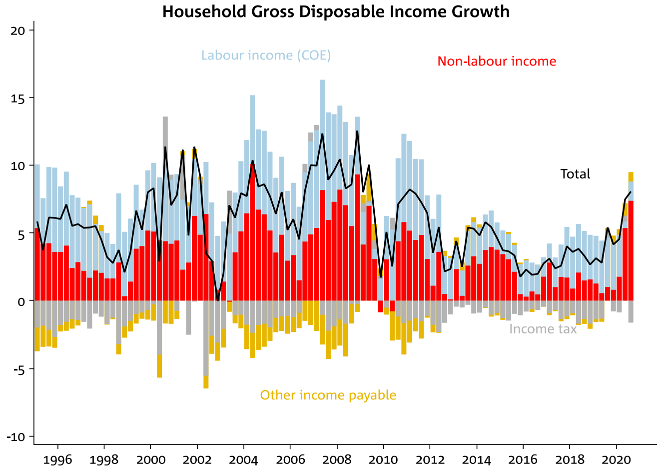
Household Consumption Growth

Year-ended Growth (%)



Source: National Australia Bank, Macrobond

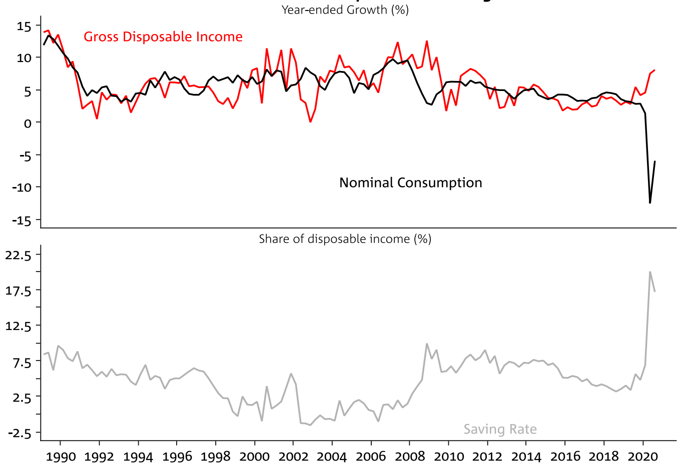
Household Gross Disposable Income Growth



Source: National Australia Bank, Macrobond

Household Consumption and Saving

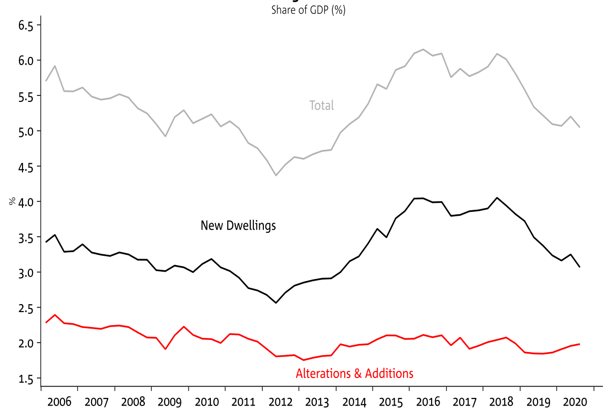
Year-ended Growth (%)



Source: National Australia Bank, Macrobond

Dwelling Investment

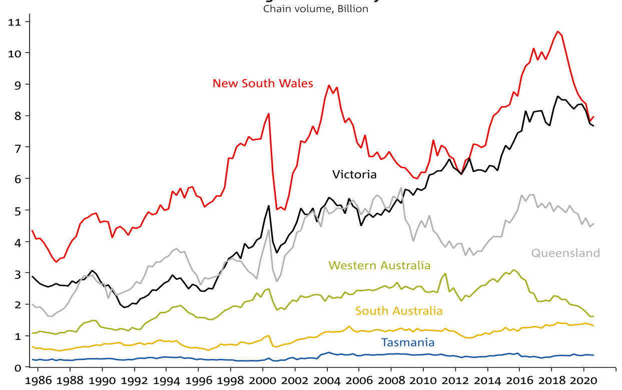
Share of GDP (%)



Source: National Australia Bank, Macrobond

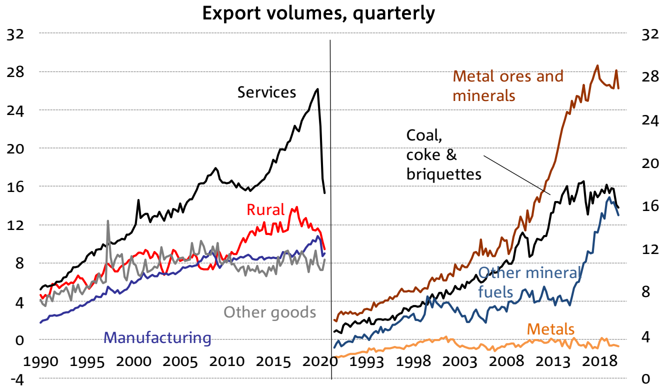
Dwelling Investment by State

Chain volume, Billion



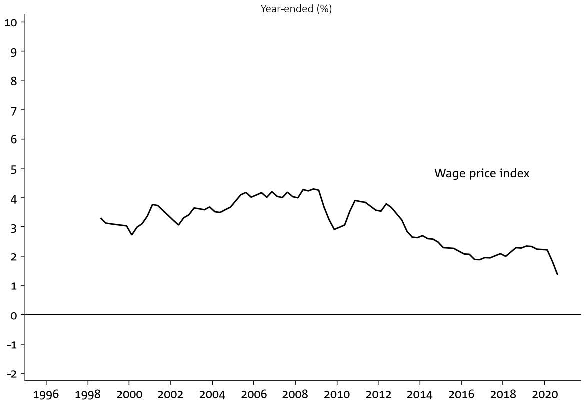
Source: National Australia Bank, Macrobond

Export volumes, quarterly



Income Growth

Year-ended (%)



Source: National Australia Bank, Macrobond

Social benefits payments to households

Share of household gross disposable income

Source: National Australia Bank, ABS

AUTHORS:

Alan Oster, Group Chief Economist
Gareth Spence, Senior Economist
Antony Kelly, Senior Economist
Kaixin Owyong, Senior Economist
Phin Ziebell, Economist

Group Economics

Alan Oster
Group Chief Economist
+(61 0) 414 444 652

Jacqui Brand
Executive Assistant
+(61 0) 477 716 540

Dean Pearson
Head of Behavioural & Industry Economics
+(61 0) 457 517 342

Australian Economics and Commodities

Gareth Spence
Senior Economist
+(61 0) 436 606 175

Kaixin Owyong
Senior Economist
+(61 0) 436 679 908

Phin Ziebell
Senior Economist
+(61 0) 475 940 662

Behavioural & Industry Economics

Robert De Iure
Senior Economist – Behavioural & Industry Economics
+(61 0) 477 723 769

Brien McDonald
Senior Economist – Behavioural & Industry Economics
+(61 0) 455 052 520

Steven Wu
Senior Economist – Behavioural & Industry Economics
+(61 0) 472 808 952

International Economics

Tony Kelly
Senior Economist
+(61 0) 477 746 237

Gerard Burg
Senior Economist – International
+(61 0) 477 723 768

Global Markets Research

Ivan Colhoun
Global Head of Research
+(61 2) 9293 7168