AUSTRALIAN ECONOMIC UPDATE

GDP Q3 2021 – A short and sharp fall, now firmly in the rear-view mirror

1 December 2021

Bottom line: **Q3 GDP fell by 1.9% q/q a sharp, but importantly smaller fall than expected. The decline was driven by a sizeable fall in household consumption, concentrated in services where lockdowns have the most significant impact. Government support again played an important role cushioning household and business balance sheets. While these data show the significant disruption caused by lockdowns in the two largest states, they are now firmly in the rear-vision mirror with higher frequency data suggesting that a very solid rebound is already underway. State final demand also showed solid growth in non-lockdown states. We expect Q4 GDP to rise by 2%, which would see the pre-Delta level of GDP almost recovered by year's end. The hit to Q3 GDP is less than what the RBA's -2.5% expectation was in the November SoMP. Further out our view is unchanged. We expect above-trend growth to continue in 2022 and the unemployment rate to resume its prior downwards trajectory (4.2% at end 2022), with the RBA beginning to lift rates in mid-2023. In addition, we see the RBA having enough evidence on progress towards its goals to end purchases in the QE program by February.**

In terms of today's release, the data show a notable decline across all three measures of GDP. On the expenditure side, household services consumption led the decline (though goods spending also fell) and inventories made a significant subtraction. Aggregate business investment also detracted slightly, while dwelling investment was largely flat. A strong rise in government consumption provided support, while net exports also rebounded in the quarter, offsetting some of the decline in private demand and inventories.

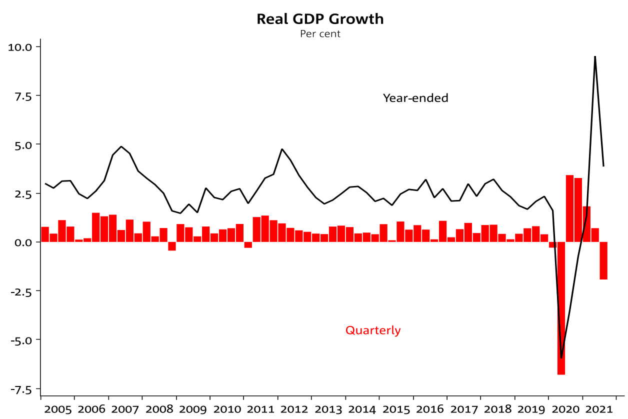
By industry, the production side of the accounts reflected the hit to services consumption with accommodation & food, rec & personal, transport and other services seeing notable declines. The income side reflected the support provided by all levels of government with a sharp increase in subsidies in the quarter, while compensation of employees and business profits held up reasonably well given the wider result.

Of note was a sharp spike in the household savings rate, also reflecting the support provided by the government and reduced spending during lockdown. This provides us with confidence that with the economy opening up, household spending will recovery sharply, and while the balance between goods and services spending will normalise over time, the near-term will continue to see a solid contribution to growth from the consumer.

Looking forward, we expect GDP to see a solid rebound in Q4, rising 2.0% consistent with a range of high frequency data including the NAB business survey, measures of labour demand and transactions data. We expect the rebound to continue into Q1 2022, which will see the pre-Delta level of GDP recovered in Q1 next year. We see above trend growth continuing through 2022, with GDP rising by over 4% in the year. Growth should then return to around trend in 2023 with the rebound complete and policy stimulus beginning to fade. This outlook for growth sees a corresponding recovery in the labour market with the focus over 2022 being how quickly a tightening labour market translates into wage growth and when this begins to show up in consumer prices on an ongoing basis.

Key figures

Key aggregates	q/q % ch		y/y % ch
	Jun-21	Sep-21	Sep-21
GDP (A)	0.7	-1.9	3.9
GDP (E)	0.5	-2.0	3.9
GDP (I)	0.6	-1.8	3.8
GDP (P)	0.9	-1.9	3.8
– Non-Farm GDP	0.6	-2.0	3.2
– Farm GDP	3.5	0.3	43.4
Nominal GDP	3.3	-0.6	11.2
Real gross domestic income	2.4	-1.7	9.0
Real net national disposable income per capita	2.2	-3.8	7.4
Terms of trade	7.7	0.5	23.1



Source: National Australia Bank, Macrobond

HIGHLIGHTS

- **Household consumption** fell 4.8% q/q (up 1.8% y/y) as the impact of lockdowns in major states weighed on spending – but the hit to consumption was far less than the impact of lockdowns in 2020 (when consumption fell more than 12%). As expected, the fall in services consumption was greatest at 5.8%, with very large falls in spending on lockdown-affected sectors such as transport services, hotels, cafes and restaurants, and recreation. Goods consumption was down 3.3%, weighed primarily by spending on clothing and footwear as retail was also impacted by COVID-19 related-measures. Overall, the fall in household consumption detracted 2.5ppts from growth for the quarter, driving the overall GDP result. The fall in consumption, along with support for incomes from governments, saw the household savings ratio spike back up to 19.8%, almost as high as its 2020 peak and well above long run historical level.
- **Underlying business investment** fell 1.1% q/q. This followed three quarters of strong growth, leaving business investment 9.0% higher than a year ago. The fall off was at least partly due to lockdowns with the ABS citing them as a factor behind the fall in non-dwelling construction in NSW (and also a fall in investment in the ACT), although Victoria was seemingly less affected with underlying business investment rising. Machinery and equipment investment also declined (-3.1% q/q) as did mining investment (for the second consecutive quarter).
- **Dwelling investment** was largely flat, rising just 0.1% q/q to be up 11.4% y/y after strong quarters in December and March. Renovations rose in the quarter (+2.5%) as the HomeBuilder pipeline continued to be worked through, but new dwelling investment fell (-1.6%). NSW weighed on the result with the state seeing dwelling investment fall 5% as lockdowns impacted construction, although dwelling investment was up 2.3% in Vic despite similar measures affecting the sector.
- G**overnment spending**, on an underlying basis, grew at its strongest pace in almost 10 years (3.3% q/q). This reflected strong growth in both Federal and State/local consumption which the ABS attributes to health-related spending although there was also notable growth in Federal defence spending. Public underlying investment grew at its slowest pace since mid-2020, but growth was still robust (2.0% q/q).
- **Net exports** added 1.0ppts to quarterly GDP growth, the reverse of the previous quarter. Export volumes increased 1.2% q/q mainly due to a lift in commodities exports which offset declines in manufacturing and services. The fall in service credits was centred on the travel component – the modest recovery in Q2 was more than unwound as it fell to a new pandemic low. Import volumes fell 4.0% q/q, with declines in both goods and services imports. The fall in goods imports (-3.5% q/q) was despite robust capital goods imports and mainly reflected a large fall in imports of consumption goods. The ABS noted that imports were affected by global supply chain pressures. Non-industrial transport equipment imports fell -18%, consistent with global auto production constraints.
- **State final demand (SFD)** fell significantly in NSW (-6.5%) and to a lesser extent in Vic (-1.4%) and the ACT (-1.6%), while other jurisdictions saw SFD grow. The NSW result was driven by a large 10.8% fall in household consumption as well as falls in both in public and private investment, reflecting the significant impact of lockdowns. In Vic, the fall in household consumption was more limited (-5.2%) and private investment increased. Both states were supported by strong public consumption in response to the pandemic. Elsewhere, Qld (+1.8%), SA (+1.4%), Tas (+4.2%), and the NT (+4.0%) all saw SFD grow on the back of both household consumption and private investment. Growth in WA was softer (+0.6%) as private investment fell, weighing against the strength in household consumption.
- The **production side** of the accounts again showed the distinctive pattern of lockdown effects across industries. Accommodation and food services fell 26.4%, detracting 0.5ppts from GDP, while other personal services, arts and recreation, retail, wholesale, and transport also saw notable declines. Construction and administrative & support services were also down, although at -1.1% and -2.1% respectively the falls were more limited. Outside of the industries most obviously negatively impacted by health restrictions, manufacturing, healthcare, and professional and rental services all fell. On the other hand, mining and agriculture both grew, as did communications, finance, public administration, and education services.
- **Agriculture** continues to perform very strongly, reflecting another great season with widespread above-average rainfall in key cropping and livestock regions. Agriculture, forestry and fishing production was up 1.4% in the quarter, driven by higher livestock slaughter and the best cotton production in years. While the industry did not provide much contribution to GDP growth over the quarter, it is up 36.5% over the year – the best performing industry over this period by a substantial margin. Q4 2021 and Q1 2022 are likely to remain strong on a big winter crop, although given last year's wheat crop was a record, actual growth may be a little slower. Looking further into next year, it is increasingly likely that agriculture will become a drag on growth, unless we see a third strong year of production in a row.

SUMMARY CHARTS AND TABLES:

GDP (E) by component

GDP Expenditure Components	q/q % ch Jun-21	q/q % ch Sep-21	y/y % ch Sep-21	Contribution q/q % ch Sep-21
Household Consumption	1.0	-4.8	1.8	-2.5
Dwelling Investment	0.6	0.1	11.4	0.0
Underlying Business Investment^	2.7	-1.1	9.0	-0.1
Machinery & equipment	1.6	-3.1	17.6	-0.1
Non-dwelling construction	3.6	0.1	3.0	0.0
New building	3.2	1.4	-0.4	0.0
New engineering	4.0	-1.0	6.1	0.0
Underlying Public Final Demand	2.0	3.3	7.2	0.9
Domestic Demand	**1.6**	**-1.8**	**5.2**	**-1.7**
Stocks (a)	-0.1	-1.3	-0.8	-1.3
GNE	**1.5**	**-3.1**	**4.4**	**-3.1**
Net exports (a)	**-1.0**	**1.0**	**-0.4**	**1.0**
Exports	-3.4	1.2	3.3	0.2
Imports	1.1	-4.0	5.8	0.8
GDP	**0.7**	**-1.9**	**3.9**	**-1.9**

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

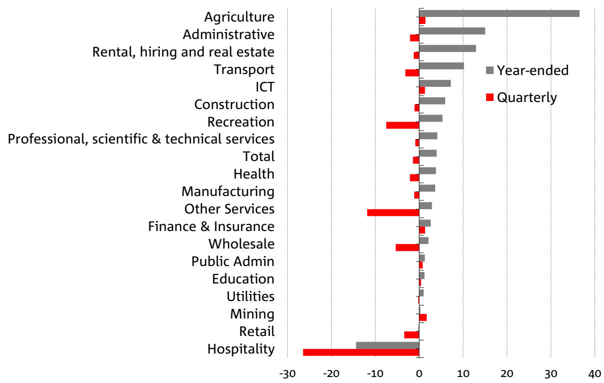
INCOME MEASURES

Income measures	q/q % ch Jun-21	q/q % ch Sep-21	y/y % ch Sep-21
Real GDI	2.4	-1.7	9.0
Real net disposable income per capita	2.2	-3.8	7.4
Compensation of employees	1.2	0.5	4.7
Average compensation of employees (average earnings)	-0.2	1.6	1.1
Corporate GOS	5.8	4.2	1.3
Non-financial corporations	6.7	4.8	0.7
Financial corporations	1.7	1.3	4.7
General government GOS	0.8	1.0	3.0
Productivity & unit labour cost			
GDP per hour worked	-1.8	3.7	1.7
GVA per hour worked mkt sector	-1.8	5.3	3.1
Non-farm nominal unit labour cost	2.0	1.5	15.4
Non-farm real unit labour cost	0.2	0.2	7.8

State final demand

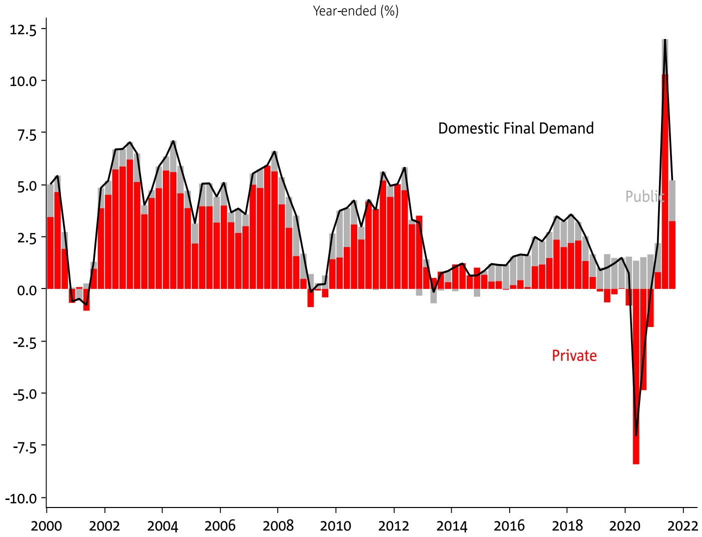
State/ Territory	Q/Q Jun-21	Q/Q Sep-21	Y/Y Sep-21
TAS	1.5	4.2	11.7
NT	5.3	4.0	11.6
VIC	1.4	-1.4	9.9
WA	0.9	0.6	6.4
QLD	2.0	1.8	6.1
SA	1.4	1.4	5.7
ACT	0.8	-1.6	1.6
NSW	2.3	-6.5	0.3

Industry GVA Growth



Domestic Final Demand Growth

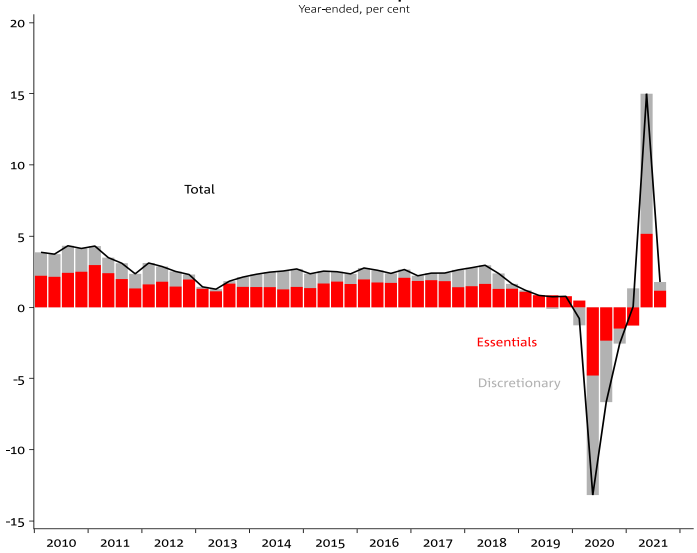
Year-ended (%)



Source: National Australia Bank, Macrobond

Real Household Consumption Growth

Year-ended, per cent



Source: National Australia Bank, Macrobond

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