AUSTRALIAN ECONOMIC UPDATE

GDP Q4 2021 – A strong rebound in activity as lockdowns end

National Australia Bank

2 March 2022

<u>Bottom line:</u> Q4 GDP rose by 3.4% q/q (4.2% y/y), broadly in line with our estimate of 3.5%. Household consumption drove the result as lockdowns eased in Q4 with both goods and services spending increasing by over 6%, which saw overall consumption more than recover the Q3 fall and exceed pre-COVID levels for the first time. The production side of the accounts and data for the states also reflect the impact of easing lockdowns in NSW and Vic, with the services industries seeing large gains in the quarter. The domestic final demand and consumption deflators strengthened, reflecting the price pressures seen in other data (albeit these measures are volatile and affected by compositional changes). On the labour costs side, AENA per hour has been buffeted by swings in hours worked but continues to track above the WPI in year-ended terms, though the more volatile unit labour costs measure fell in the quarter.

Today's release doesn't alter our expectations for growth going forward, with Q1 to be impacted by Omicron early in the quarter but signs suggest activity has already rebounded. We continue to see growth of around 3.5% over 2022, and closer to trend growth of around 2.1% in 2023. With GDP now above pre-COVID levels and activity to remain healthy through 2022, the focus for the RBA will continue to be on the nominal side. We expect unemployment to fall to around 3.5% by mid-2022 and wage growth to pick up, with the RBA having enough evidence that inflation is sustainably within the target band to begin normalising rates in the second half of 2022.

In terms of today's release, the data show a strong rebound in activity as lockdowns ended in the two largest states. The expenditure side was driven by a strong increase in household consumption, contributing 3.2ppts to growth. Business and dwelling investment as well as net exports made small subtractions, which were offset by a solid contribution from inventories. Government spending was also slightly softer after a very strong rise in the previous quarter. The impact of the removals of lockdowns was evident with NSW and Vic seeing the largest increases in state final demand, while on the production side the household services industries led the gains by industry.

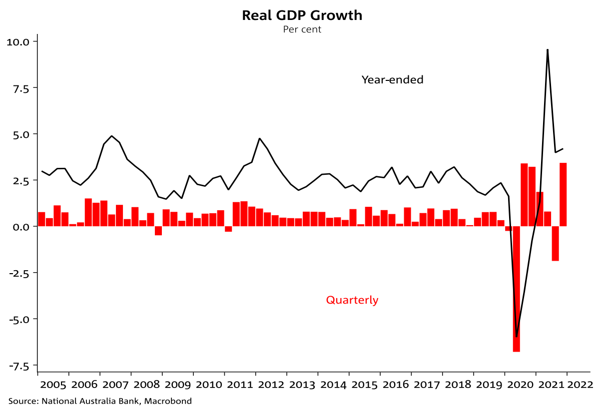
The impact of both **price pressures and supply constraints** was evident in today's accounts. The domestic final demand deflator continued to strengthen as did the consumption deflator. Measures of labour costs were mixed, with average earnings continuing to track just above 3% while unit labour costs softened slightly. Supply constraints were particularly evident in dwelling construction which saw large declines in all states other than NSW & the ACT.

Of note was a large fall in the savings rate following a spike in Q3. The decline was driven by a fall in household income as government support payments pulled back, as well as increased consumption. Nonetheless, the savings rate remains elevated at 14% and households have accumulated a large stock of savings through the pandemic. Pent-up demand for discretionary spending was evident in today's data, signalling households will continue to spend in 2022.

Looking forward, we expect to see growth slow in Q1 with Omicron impacting early in the quarter, although high frequency indicators suggest the hit was not as large as initially feared and activity has already rebounded. We see growth continuing at an above trend rate in 2022 supported by elevated household consumption and rising dwelling and business investment. Government spending is also expected to provide support. Overall, that sees growth of around 3.5% in 2022 before closer to trend growth in 2023. That said, while aggregate GDP is now notably above pre-COVID levels, a number of pandemic impacts remain including elevated goods spending and lagging services trade. The extent to which these imbalances normalise, and how quickly, will only become apparent as 2022 goes on.

Key figures

Key aggregates	q/q % ch		y/y % ch
	Sep-21	Dec-21	Dec-21
GDP (A)	-1.9	3.4	4.2
GDP (E)	-2.0	3.6	4.1
GDP (I)	-1.7	3.4	4.4
GDP (P)	-1.8	3.3	4.2
– Non-Farm GDP	-2.0	3.2	3.8
– Farm GDP	1.8	11.1	20.9
Nominal GDP	-0.6	3.4	10.2
Real gross domestic income	-1.7	1.9	6.4
Real net national disposable income per capita	-3.8	1.6	3.5
Terms of trade	0.2	-5.1	10.3



HIGHLIGHTS

- **Household consumption** rose 6.3% q/q (up 3.5% y/y), more than recovering the large fall caused by lockdowns in the prior quarter to be above pre-COVID levels for the first time. The rebound was driven by surging spending on both goods and services, including large increases in spending on hotels, cafes, and restaurants, recreation and culture, and health, as well as items such as clothing and footwear. Consumption contributed 3.2ppts to GDP growth, almost fully accounting for the quarterly total. The household savings ratio eased as consumption rose, but still remains well above its pre-pandemic level.
- **Underlying business investment** disappointed, falling 0.3 q/q. This was the second consecutive fall and while it remains 5.4% higher than a year ago, it is barely above its pre-COVID level, a weak result over a two-year period. Moreover, the decline is despite some boost due to the end of lockdowns (with the ABS citing this as a positive factor in NSW). The fall was driven by machinery and equipment (-1.5%q/q, underlying basis) and new engineering construction (-1.6% q/q), only partially offset by some new building construction growth (0.3% q/q) and continued solid growth in intellectual property products (research, software etc).
- **Dwelling investment** fell 2.2% q/q after slowing in the prior quarter, to be up 5.3% y/y. Investment in both new dwellings and renovations declined as HomeBuilder effects continued to fade and labour and materials shortages impacted construction. Most states saw dwelling investment fall, with the exceptions of NSW where activity rose as lockdown-related construction restrictions lifted, as well as the ACT.
- Underlying **public demand**, was down 0.4% q/q, although this followed the strongest q/q growth in over 10 years in the prior quarter. Compared to a year ago underlying public demand was still up 5.6%. Both Federal government defence and non-defence consumption and investment fell, while at a state and local government level consumption moderated to a still solid 1.2% q/q.
- **Net exports** detracted 0.2ppts from quarterly GDP growth. Export volumes declined 1.5% q/q as further strong growth in rural exports (2.9% q/q) was more than offset by resource (-2.5%), manufacturing (-4.1%) and service credit (-4.6%) falls. The latter was largely due to travel services and was in contrast to a rise in travel debits (albeit from an exceptionally low level) with the divergence likely reflecting the importance of overseas students on the credits side. The 0.9% q/q fall in imports was driven by falls in imports of consumption and capital goods, as well as transport and other services, although intermediate goods imports increased. The ABS noted that "supply chain disruptions, shipping constraints and a sharp increase in freight costs continued to impact trade this quarter."
- **State final demand (SFD)** rebounded strongly in NSW (up 6.7%) and Vic (up 3.7%) as well as the ACT (up 1.9%) as lockdowns were lifted and household consumption rallied (up 11.4% in NSW and 7.5% in Vic). NSW also saw private investment increase (up 4.1%) as construction restrictions lifted. Other jurisdictions saw largely flat or falling final demand. Qld (0.0%), SA (0.3%) and WA (0.1) held steady but Tas (-1.5%) and the NT (-1.8%) declined, with declining private investment weighing across the board.
- The **production side** of the accounts saw strong results for sectors impacted by lockdowns as reopening allowed consumption to resume and also showed an element of pent-up demand. Accommodation & food services rose 26.1% as cafes and restaurants reopened and travel restrictions eased, largely retracing the fall in Q3 and contributing 0.4ppts to GDP. Professional services and healthcare also contributed significantly, while personal services (up 15.4%), arts & recreation (up 8.2%), and retail (up 7.4%) all made large gains after falling in Q3. Wholesale, communications, transport, and administrative services all also rose, while construction rose 1.9% and manufacturing rose 1.8%. Mining declined (down 1.0%), as did utilities.
- **Agriculture, forestry and fishing** recorded yet another strong print in Q4, up 9.0% q/q and 19.4% y/y - the strongest annual growth for any industry sector. The result was driven by phenomenal seasonal conditions delivering a record grain harvest - cereal exports were up almost 24%.
- On the **nominal side**, domestic prices rose, as did import prices, with the latter enough to see the terms of trade deteriorate 5.1%. Nominal GDP grew at 3.4%, in line with real GDP, as a result. The consumption deflator rose 2.4% over the year – weaker than the headline CPI increase of 3.5%. In terms of incomes, a strong labour market rebound saw total compensation of employees rise 2.0%, and average earnings (compensation per employee) grew 1.8% as hours worked rose. Growth in average earnings per hour softened but remained above WPI in annual terms, but unit labour costs, which are more volatile, declined in both nominal and real terms in the quarter.

SUMMARY CHARTS AND TABLES:

GDP (E) by component

GDP Expenditure Components	q/q % ch		y/y % ch	Contribution to q/q % ch
	Sep-21	Dec-21	Dec-21	Dec-21
Household Consumption	-4.8	6.3	3.5	3.2
Dwelling Investment	0.4	-2.2	5.3	-0.1
Underlying Business Investment^	-1.4	-0.3	5.4	0.0
Machinery & equipment	-3.0	-1.5	6.5	-0.1
Non-dwelling construction	-0.6	-0.7	2.9	0.0
New building	3.6	0.3	7.3	0.0
New engineering	-4.2	-1.6	-1.0	0.0
Underlying Public Final Demand	3.5	-0.4	5.6	-0.1
Domestic Demand	**-1.7**	**2.9**	**4.6**	**2.9**
Stocks (a)	-1.2	0.9	0.3	0.9
GNE	**-2.9**	**3.8**	**5.0**	**3.7**
Net exports (a)	**0.9**	**-0.2**	**-0.8**	**-0.2**
Exports	1.5	-1.5	-2.6	-0.3
Imports	-2.8	-0.9	1.0	0.2
GDP	**-1.9**	**3.4**	**4.2**	**3.4**

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

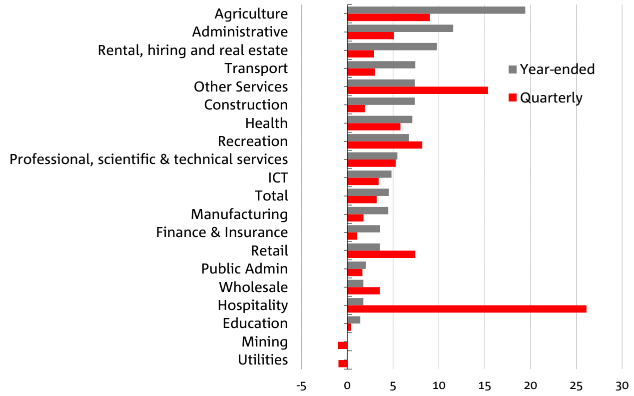
INCOME MEASURES

Income measures	q/q % ch		y/y % ch
	Sep-21	Dec-21	Dec-21
Real GDI	-1.7	1.9	6.4
Real net disposable income per capita	-3.8	1.6	3.5
Compensation of employees	0.5	2.0	5.3
Average compensation of employees (average earnings)	1.6	1.8	3.4
Corporate GOS	3.9	0.4	8.5
Non-financial corporations	4.5	0.3	9.2
Financial corporations	1.4	1.2	5.2
General government GOS	1.0	0.8	3.3
Productivity & unit labour cost			
GDP per hour worked	3.0	-0.8	2.0
GVA per hour worked mkt sector	4.7	-2.0	2.0
Non-farm nominal unit labour cost	2.6	-0.3	6.1
Non-farm real unit labour cost	0.3	-0.2	0.7

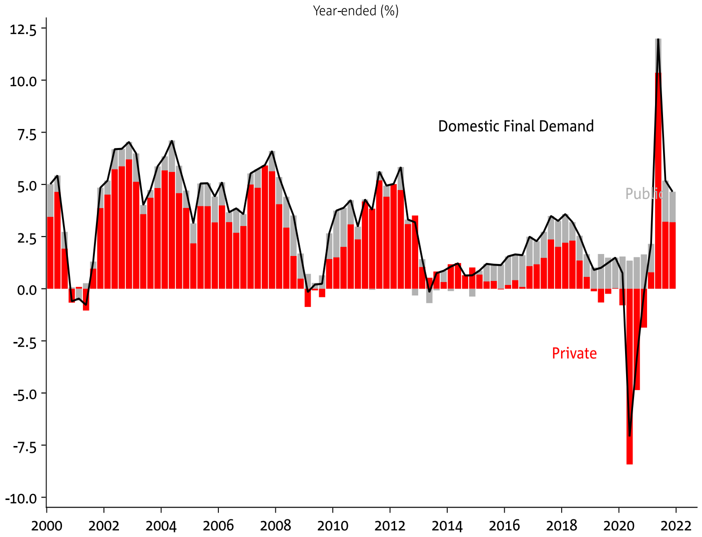
State final demand

State/ Territory	Q/Q Sep-21	Q/Q Dec-21	Y/Y Dec-21
VIC	-1.5	3.7	6.1
TAS	4.3	-1.5	5.8
SA	1.4	0.3	5.4
NT	4.0	-1.8	4.7
WA	0.6	0.1	4.5
NSW	-6.5	6.7	4.0
QLD	1.7	0.0	3.9
ACT	-1.2	1.9	2.3

Industry GVA Growth

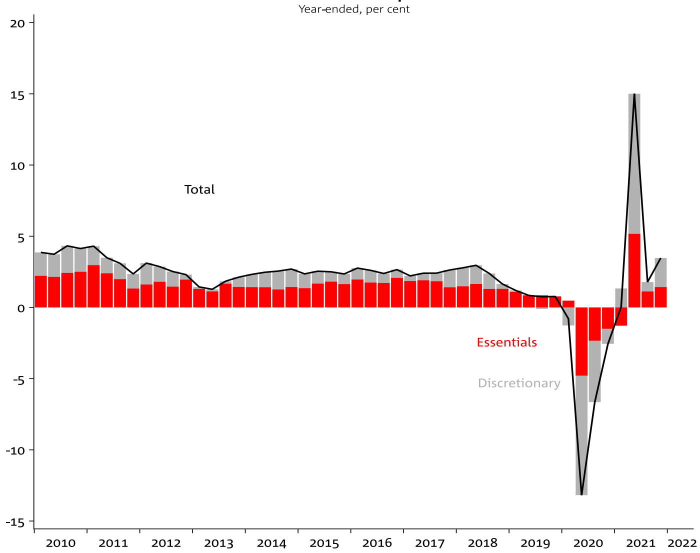


Domestic Final Demand Growth
Year-ended (%)



Source: National Australia Bank, Macrobond

Real Household Consumption Growth
Year-ended, per cent



Source: National Australia Bank, Macrobond

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