AUSTRALIAN ECONOMIC UPDATE

GDP Q1 2022 – A solid result despite virus disruptions early in the year

1 June 2022

Bottom line: GDP rose by 0.8% q/q (3.3% y/y), a fairly solid result considering the disruptions to domestic activity in early 2022, following the strong pickup in Q4. Today's data shows that goods consumption remains elevated despite the continued recovery in services spending. It also confirms that services trade remained depressed despite both state and international borders opening in the quarter – but larger gains will likely occur in Q2. The impact that supply chain disruptions may have on growth this year also remains evident, with both dwelling and business investment constrained by the price and availability of materials. Today's release doesn't alter our view for growth over 2022 – which is expected to remain strong at over 3.0% before moderating in 2023. It also doesn't alter our view on monetary policy, with the exceptionally easy stance of policy amidst a tightening labour market and pickup in domestic pressures the key focus. That said, the high level of savings will help households weather the headwinds from higher rates and rising prices in the near term.

In terms of today's release, the data show ongoing strength in household consumption despite the headwinds from Omicron and floods and comes after a very strong rise in Q4. Elsewhere on the expenditure side outcomes were more mixed. Government spending was strong, driven by both consumption and investment while dwelling investment was slightly weaker after being constrained on the supply side. Business investment was mixed with M&E stronger, but buildings & structures softer. By industry, recreational, transport & postal and hospitality led the gains reflecting a recovery in services as the impact of lockdowns fade. Professional services also made a notable contribution in the quarter while weather impacted agriculture, forestry & fishery which was weaker following a strong outcome in Q4.

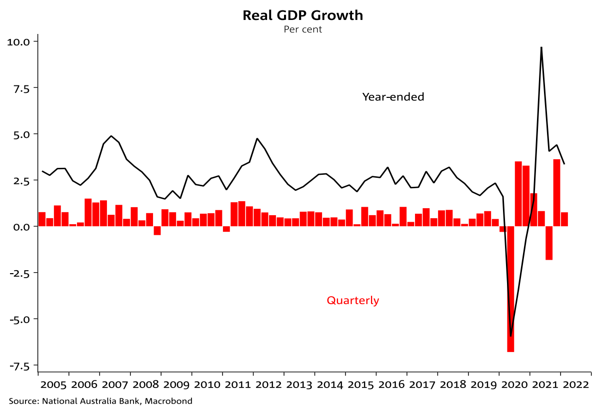
The impact of both **price pressures and supply constraints** were again evident in today's accounts. The domestic final demand and consumption deflators strengthened further – with DFD at its highest level since the early 2000s in annual terms. Measures of labour costs were mixed, with average earnings per head softer while average earnings per hour was significantly stronger, but likely impacted by the volatility in hours worked. Overall, unit labour costs rose slightly but were broadly flat over the previous 6 months.

Of note was the strong rise in the terms of trade in the quarter, now at a record high – and impressive in the context of the strong price growth on the imports side. This reflects the strength in prices of a number of Australia's key commodities and will support national income but is unlikely to see a significant response in terms of mining investment in the near term. Ultimately, higher energy and petrol costs for households will likely have a more direct impact via a reduction in consumption as household budgets are stretched.

Looking forward, we expect solid growth to continue in the near-term, in part supported by strong consumption as the household savings rate normalises. Business investment should also pick up, while dwelling investment and public demand are expected to remain elevated. That sees GDP growth of over 3.0% this year before growth slows to around 2.1% over 2023 and 2.25% in 2024. With lockdowns now in the past, and with state and international borders open, we expect the balance between goods and services consumption to normalise and for services trade to lift. However, the timing and pace of the normalisation in these components remains highly uncertain. Ultimately, we still see the high level of aggregate demand putting further pressure on what is already a tight labour market and, with inflation elevated, expect the RBA to continue normalising policy.

Key figures

Key aggregates	q/q % ch		y/y % ch
	Dec-21	Mar-22	Mar-22
GDP (A)	3.6	0.8	3.3
GDP (E)	3.8	0.8	2.9
GDP (I)	3.7	0.8	3.6
GDP (P)	3.3	0.7	3.5
– Non-Farm GDP	3.5	1.0	3.2
– Farm GDP	8.7	-6.7	9.8
Nominal GDP	3.5	3.7	10.2
Real gross domestic income	2.2	2.1	5.0
Real net national disposable income per capita	2.5	1.0	1.6
Terms of trade	-4.9	5.9	8.3



Date: **1 June 2022**

HIGHLIGHTS

- **Household consumption** rose 1.5% q/q (up 4.0% y/y), continuing the rebound that began in Q4 despite the disruptions from Omicron and flooding. In a sign that consumption patterns are beginning to normalise, services consumption was up 2.3% on the back of a large increase in transport services and further gains in recreation and hospitality spending, while goods consumption was more subdued, up just 0.3% (supported by a 13% increase in spending on new vehicles as supply constraints eased). In total, consumption contributed 0.8ppts to GDP growth. The household savings ratio continued to ease but households appear to be adjusting their saving behaviour only gradually, with the savings rate falling from 13.4% to 11.4%.
- There was a modest acceleration in underlying **business investment** (up 1.4% q/q, after 0.7% q/q in Q4). This reflected a rebound in machinery and equipment (3.2% q/q on an underlying basis, after falling in the two previous quarters), while research & development, mineral exploration and software investment each grew by around 1.5% q/q. In contrast, non-building construction was basically flat (-0.1% q/q, underlying basis) as a rise in engineering construction was offset by a fall in the new building category. On a sectoral basis, non-mining investment rose 2.4% q/q, to be up 5.3% over the year. However, mining investment declined 2.3% q/q; investment by miners has been broadly flat for several years and is showing no signs (other than a modest rise in exploration expenditure) of responding to the strong run up in commodity prices seen since mid-2016.
- **Dwelling investment** fell 1.0% q/q (5.3% y/y) following last quarters decline. This decline came despite a solid pipeline of work build up through the pandemic – as a result of Homebuilder and other state programs – as supply shortages weighed. Outcomes were mixed across the states, with NSW, Vic and SA up, while QLD, WA and Tas declined.
- P**ublic demand**, after a small fall in Q4 2021, returned to robust growth, as has often been the case over the pandemic period. Underlying public demand increased by 2.6% q/q, reflecting increases in both general government consumption and public investment. The ABS reports increased health expenditure was again a factor, but flood relief efforts also provided a lift (with the 5.6% q/q rise in national defence expenditure in part due to the deployment of military personal to flood affected areas).
- **Net exports** detracted 1.7 ppts from quarterly GDP growth, mainly due to a surge in import volumes. Import volumes increased 8.1% q/q, reflecting demand for consumption goods and rapid COVID-19 tests, and the build-up of inventories in the quarter. Growth was strongest for consumption good imports (+14.9% q/q) but capital and intermediate good imports also increased by around 5% q/q. At the same time, export volumes declined (-0.9% q/q) as resource exports fell (-2.2% q/q) and the run up in rural exports that started late 2020 came to end (-2.0% q/q). Both service credits (2.3% q/q) and services debits increased (6.8% q/q) but are still only around half of their pre-pandemic level, although it is still too early to see the impact of the February overseas border re-opening.
- **State final demand (SFD)** grew in Vic (up 2.4%), NSW (up 1.2%), Qld (up 0.8%), SA (up 0.8%) and the ACT (up 1.7%), All were supported by higher household spending as well as government consumption, particularly government spending on the flood response in NSW and Qld. Vic also saw a strong lift in investment while NSW and Qld saw investment decline. In WA the story was a little different, with a 2.2% increase in SFD driven largely by health-related government spending, while household spending was flat. Defence-related investment also increased in WA. Tas saw SFD fall 0.6% with higher government consumption not enough to offset falls in household spending and private investment, while the NT economy grew 2.2%, supported by public demand.
- The **production side** of the accounts saw continued growth across services sectors including transport, postal and warehousing (up 4.3%), accommodation and food (up 3.7%), professional services (up 3.1%), and arts and recreation (up 4.4%). Wholesale also grew 3.2%, while retail was up 0.9%. Manufacturing production rose 1.1% while construction was largely steady (up 0.2%) and mining production fell 1.5%. Healthcare also fell, down 0.9%, as elective surgeries and health appointments were delayed due to the Omicron outbreak.
- **Agriculture, forestry and fishing** was weaker in the quarter with production impacted by weather disruptions to both crops and livestock. This follows a strong outcome in the Q4 which was boosted by a bumper grain harvest.
- On the **nominal side**, significant price pressures were evident, with the household consumption deflator up 1.5% and the domestic demand deflator up 1.4%, both the strongest quarterly rise since 2000. The terms of trade also rose sharply, up 5.9%, with the increase in export prices exceeding the rise in import prices. Overall, nominal GDP grew 3.7% q/q (10.2% y/y). In terms of incomes, total compensation of employees rose 1.9% as employment and wages increased, more than compensating for the fall in average hours worked. Measures of labour costs were mixed, with average earnings per employee softer while average earnings per hour was significantly stronger but likely impacted by the volatility in hours worked. Overall, unit labour costs rose slightly but were broadly flat over the previous 6 months.

SUMMARY CHARTS AND TABLES:

GDP (E) by component

GDP Expenditure Components	q/q % ch		y/y % ch	Contribution to q/q % ch
	Dec-21	Mar-22	Mar-22	Mar-22
Household Consumption	6.4	1.5	4.0	0.8
Dwelling Investment	-1.9	-1.0	-1.3	-0.1
Underlying Business Investment^	0.7	1.4	3.6	0.2
Machinery & equipment	-0.8	3.2	0.7	0.1
Non-dwelling construction	0.9	-0.1	4.4	0.0
New building	0.6	-2.6	5.1	-0.1
New engineering	1.3	2.3	3.7	0.1
Underlying Public Final Demand	-0.1	2.6	8.0	0.7
Domestic Demand	**3.2**	**1.6**	**4.8**	**1.6**
Stocks (a)	1.0	1.0	0.7	1.0
GNE	**4.3**	**2.6**	**5.4**	**2.5**
Net exports (a)	**-0.3**	**-1.7**	**-2.4**	**-1.7**
Exports	-0.9	-0.9	-4.2	-0.2
Imports	0.7	8.1	7.6	-1.5
GDP	**3.6**	**0.8**	**3.3**	**0.8**

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

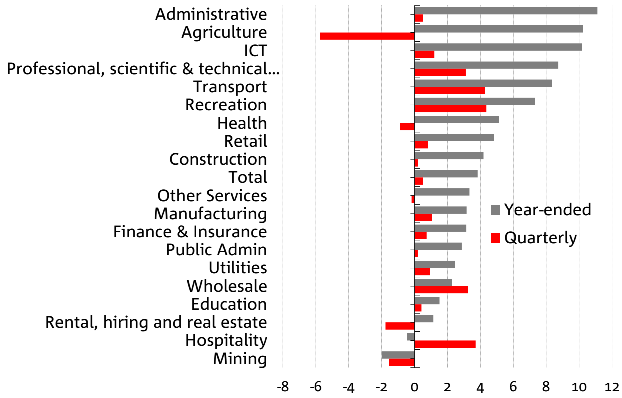
INCOME MEASURES

Income measures	q/q % ch		y/y % ch
	Dec-21	Mar-22	Mar-22
Real GDI	2.2	2.1	5.0
Real net disposable income per capita	2.5	1.0	1.6
Compensation of employees	2.0	1.8	5.5
Average compensation of employees (average earnings)	1.6	-0.7	2.2
Corporate GOS	1.2	6.0	18.1
Non-financial corporations	1.2	7.0	20.8
Financial corporations	1.3	0.9	5.4
General government GOS	0.8	0.8	3.5
Productivity & unit labour cost			
GDP per hour worked	-0.8	1.6	2.8
GVA per hour worked mkt sector	-2.0	1.3	3.0
Non-farm nominal unit labour cost	1.4	0.6	4.2
Non-farm real unit labour cost	0.4	-2.3	-1.9

State final demand

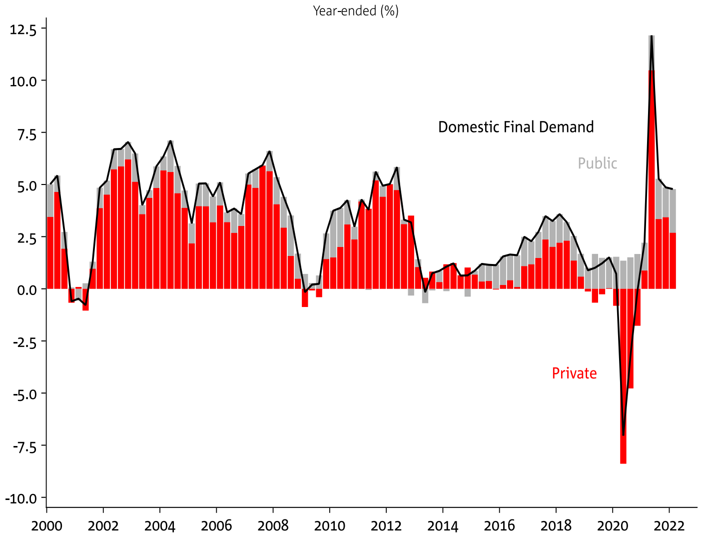
State/ Territory	Q/Q		Y/Y
	Dec-21	Mar-22	Mar-22
NT	-0.9	2.2	10.8
VIC	3.5	2.4	6.0
QLD	0.3	0.8	5.0
WA	0.8	2.2	4.9
SA	0.7	0.8	4.7
NSW	7.0	1.2	3.8
TAS	-1.6	-0.6	3.5
ACT	2.1	1.7	3.2

Industry GVA Growth



Domestic Final Demand Growth

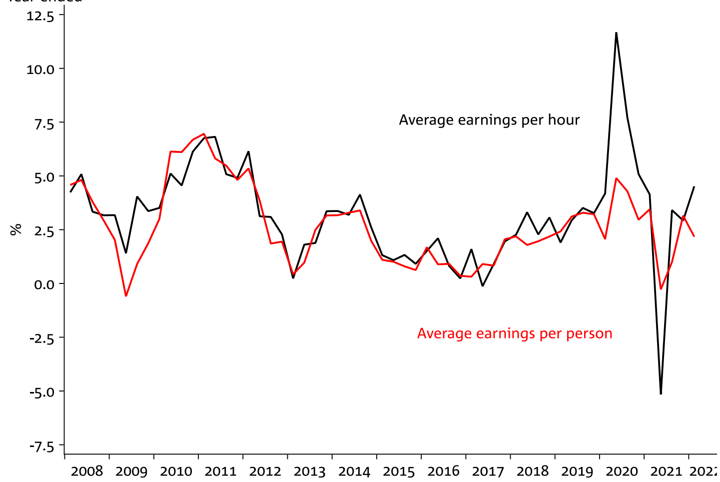
Year-ended (%)



Source: National Australia Bank, Macrobond

Growth Average Earnings

Year-ended



Source: National Australia Bank, Australian Bureau of Statistics

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