The Global & Australian Economic Outlook in Brief: July 2023

NAB Group Economics

Global Economic Outlook

China was the first of the major economies to report Q2 GDP, foreshadowing a slowdown in global growth that likely included India and Latin America. Although global inflation has continued to ease, it has done so gradually, remaining well above the targets of most major central banks in May – although US CPI provided a positive surprise in June, coming in around the Fed's target level. Further rate increases are likely – primarily in advanced economies – and the tightening in monetary policy will continue to weigh on demand this year and into 2024. There remains uncertainty both around how high policy rates will be lifted, and how long they will remain at these levels. In contrast, some emerging markets are preparing to loosen their policy. Our forecasts for the global economy are largely unchanged this month – with an upward revision to US growth offset by a downgrade to China. We expect growth of around 2.8% in 2023 before slowing to 2.7% in 2024 and edging up to 3.1% in 2025 – with this outlook below the long run average (of 3.4%).

- **China**'s economy grew by 0.8% on a quarter-on-quarter basis in Q2, down from 2.2% in Q1, as its post-zero-COVID rebound faded. Consumer demand remains tepid (as evidenced by both retail sales and consumer prices), demand for credit has been soft (in part related to ongoing weakness in the residential property sector) and goods demand in major trading partners has continued to ease.
- The China GDP data is the first released for the quarter, but **global growth** appears to have slowed more broadly in Q2, including India and Latin America, although major advanced economy growth was likely similar to that seen in Q1. That said, beyond Q2, year-average growth for the major AEs is expected to be soft until 2025 as the full impact of monetary policy tightening works its way through.
- **Global inflation** has continued to gradually ease – with our measure of consumer prices increasing by 5.8% yoy in May 2023, the slowest rate of increase since December 2021. That said, inflation remains well above the targets of most major central banks, although US June CPI provided a positive downside surprise – with the monthly growth rate around the Fed's target level (on an annualised basis).
- Further increases in **policy rates** are likely in the near-term. Despite pausing at its June meeting, the US Federal Reserve remains on a tightening bias – with various Fed speakers indicating that two further hikes may be necessary, most likely including July, and that rates may be sustained at their peak for some time. In contrast, the outlook is more mixed for EM central banks, with some either having cut rates or soon expected to do so.
- Business surveys for June point to a deeper contraction in major **advanced economy** (AE) manufacturing. Our GDP weighted AE manufacturing measure has been below 50 (the break-even point) since late 2022, and a new low was reached in June. Offsetting this, the service sector rebounded over this period, but even this has started to fade, particularly in Europe. For the US, signals were mixed with the S&P Global PMI easing in July while the services ISM spiked higher, continuing its recent volatility.
- Similarly, business surveys for **emerging markets** (EMs) were softer in June, with the EM composite PMI dropping down to a still relatively strong 53.6 points (from 55.6 points previously). The key driver of this weaker result was the EM services PMI – reflecting weaker readings in both China and India (albeit India's measure remains at extremely strong levels by historical standards). In contrast, the EM manufacturing PMI was only slightly softer. Inflation in East Asia rose comparatively modestly – peaking at around 5.4% in September 2022, and has now retreated below 3%.
- Overall, our **forecast for global growth** in 2023 is unchanged at 2.8%, with a downward revision to China's growth offset by an upwards revision to the US forecast. Only small changes have been made to our 2024 forecast but this is enough to push growth up to 2.7% (from 2.6%). Excluding the outliers of the Global Financial Crisis and initial wave of COVID-19, this would be the slowest rate of growth since 2001. We expect a modest upturn in 2025 to 3.1%.
- **Risks around this outlook** have become more balanced. As we have noted previously, a downside risk comes from AE monetary policy, and the potential for rates to rise further than expected (or stayer higher for longer) if inflation outcomes disappoint central bank expectations. The full impact (and timing) of the large increase in rates is also highly uncertain. There are still various geopolitical risks and, while a longer-term story (in terms of growth), growing impediments to trade and the risks that trading blocs emerge, are a concern.
- For more detail on the global outlook, please see the , released yesterday.

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Australian Economic Outlook

For Australia, we continue to expect quarterly GDP growth to be flat over the next three quarters, with growth of just 0.5% over 2023 and 0.9% in 2024 as the impact of rate rises flows through. The labour market is also expected to weaken through the second half, with the unemployment rate rising from the current 50-year low of 3.5% to reach 5% by end-2024. On inflation, we have nudged up our expectations for the trimmed mean with quarterly prints likely to be around 1.1% in both Q2 and Q3. We see this profile pushing the RBA to raise the cash rate as high as 4.6% over coming months, although there is a chance they remain on hold at 4.1% through August. The housing market has remained resilient despite rising rates, and we have raised our dwelling price forecast, now seeing a 4.5% increase over 2023 as a whole – though building approvals have weakened. Uncertainty remains elevated, particularly around the outlook for consumption as well as wage growth and the pace of goods disinflation.

- **Employment rose 33k in June, continuing a period of strong growth with the unemployment rate at 3.5%.** Participation also remains very elevated and total hours worked grew strongly. Labour demand remains very strong with job vacancies down slightly but still almost double their pre-COVID level in Q2. We continue to expect employment growth to slow (and vacancies to fall) over the second half of the year and through 2024, enough to see the unemployment rate rise to around 5% by end-2024. Wage growth should continue to strengthen in the near term, lifting to 4% by the end of the year before stabilising.
- **On inflation, we expect the Q2 CPI to print at 0.9% q/q and the trimmed mean measure at 1.1% q/q.** In underlying terms, this outcome would see little improvement in the quarterly pace of inflation (1.2% prior) and the outlook for Q3 suggests little further gains. Globally, upstream pressures continue to ease but how and when any easing in supply costs is passed through to goods prices remains to be seen. At the same time, a range of services side pressures – such as insurance services and rents - continuing to support inflation and there is also a risk of second round energy and wage impacts.
- **Though the RBA remained on hold in July, we still expect two further cash rate increases to 4.6%.** Like the pause in April, we see the RBA as waiting for the full quarterly CPI and an updated set of staff forecasts (to be released in the August SMP) before taking rates higher. With the pace of hikes slowing, the RBA Board clearly feels that rates are close to being restrictive enough, and there is a chance they remain on pause at 4.1%. However, in our view the risks around inflation will ultimately push them to raise rates slightly further.
- **Real household consumption growth will likely be flat or negative for much of the coming year** as the impact of higher rates continues to flow through to households. Nominal retail trade data for May showed a pickup, with spending rising 0.5% m/m after a flat April result, and NAB's transaction data showed overall spending eased back again in June. On net, that suggests Q2 spending was only marginally positive in nominal terms, and reasonably flat in real terms. Further out, we expect real consumption growth to decline slightly over the coming year, weighing on GDP growth overall. However, the outlook for consumption remains a major source of uncertainty.
- **Business conditions were steady in June but forward-looking indicators remain soft.** Business conditions in the NAB Monthly Business Survey were steady at +9 index points in June, still above the long-run average. Forward indicators in the survey remain soft with confidence sitting at 0 index points (up slightly from May) and forward orders negative at -2 index points. The weakness in the outlook, alongside elevated interest rates, does appear to be weighing on firms' borrowing with business credit growth slowing to 0.5% m/m in May.
- **We have upped our end of year expectation for house prices, while the outlook for activity remains clouded.** House prices continued to rise across almost all capital cities in June with the 8 capital city average rising 1.2% in the month to be 4.1% higher than February 2023. Given this resilience, we have revised up our outlook for house prices in 2023, now expecting prices to end the year up around 4.5% (from -6.4%).The pace of rents growth slowed slightly in monthly terms, up 0.7% nationwide in June, and the rental vacancy rate edged up further to 1.3% based on the SQM measure, but the rental market remains very tight. In terms of activity, building approvals rose in May but remain 10% lower over the year and in trend terms detached approvals continue to fall, likely weighing on future dwelling investment once the pipeline of work to be done is worked through.
- **The nominal trade surplus lifted to $11.8b in May (from $11.2b in April).** Goods exports rose 5% in May, boosted by a 77.1% m/m increase in non-monetary gold exports. Volumes for iron ore and coal appear to have lifted but there have been offsetting declines in prices. Goods imports also rose in the month. In terms of services, the ongoing recovery in tourism exports has seen Australia return to a small surplus in services trade. We continue to expect weak demand to weigh on imports more broadly over the period ahead.
- **The AUD has strengthened recently, trading in the high 68c range** after falling as low as $66c in late June. Our outlook for the AUD is unchanged, ending the year around US72c before still drifting up to US73c by the end of 2024.
- For more detail on the Australian outlook, please see the Forward View – Australia, released on Tuesday.

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