The Global & Australian Economic Outlook in Brief: September 2023

NAB Group Economics

Global Economic Outlook

Global inflation was higher in July, although this uptick was not broad based – concentrated in a few key emerging markets. Importantly, inflation in advanced economies continued to trend lower, increasing the likelihood that the tightening cycle of most major central banks has come to an end (following the ECB's hike in mid-September). That said, the recent upturn in energy prices presents a risk. Energy prices have been trending higher since the end of June, in part reflecting the efforts of OPEC+ to put a floor under oil prices and drive them higher. If energy prices cause the slowing inflation trend to falter, then central banks could lift rates further – reflecting that they still have a tightening bias. Our outlook for the global economy remains comparatively weak – with growth of 3.0% in 2023 (revised slightly higher this month on a stronger forecast for India), before slowing to 2.6% in 2024 and a modest recovery to 3.1% in 2025 – with growth over this period remaining below the long-term average of 3.4%.

- **Global inflation accelerated in July** – up by 6.4% yoy (from 5.8% yoy in June) – ending the trend of disinflation exhibited over the previous nine months, albeit this largely reflected an uptick in emerging markets, led by India and Türkiye. **Inflation among advanced economies continued to ease** – edging down to 4.4% yoy – albeit trends have been mixed among these countries, with inflation having decelerated more rapidly in North America than Europe in recent months.
- The slowing inflation trend in advanced economies has increased the likelihood that most **major central banks have either reached the end of their tightening cycle or are near the peak**. We believe that the Fed has finished hiking (though one more hike is possible), while the ECB has indicated that rate hikes might have ended, following a 25 basis point increase in mid-September. While Bank of England rates may also be near their peak, wages growth and inflation remain comparatively strong in the UK, which may force further action. The assumption that central banks have finished tightening is predicated on inflation continuing to trend lower, and near-term risk around policy rates is still to the upside. There is considerable uncertainty around when central banks will start to cut rates.
- The downward pressure on headline inflation from **global commodity prices** has started to reverse, led by energy prices. As measured by the S&P GSCI, energy commodity prices fell between early June 2022 and early May 2023, but they have been trending higher since the end of June, with the index rising in early September to its highest levels since November 2022. In part this reflects discipline from OPEC+, which cut its oil production in an attempt to put a floor under global crude prices and drive them higher.
- Momentum across the **major advanced economies** was mixed in Q2 – with economic growth solid in the US and Japan but more modest in the Euro-zone and UK. In the US, the recent strong consumption readings appear unsustainable and business surveys are broadly soft, meaning that we see a material slowdown in growth from Q4 and into 2024, including a small contraction in GDP growth at some point.
- Similarly, we have seen differing trends in the two largest **emerging markets** – China and India. The deteriorating conditions in China's property sector and weakening external demand remain headwinds, while domestic demand appears to remain subdued. Chinese authorities have modestly relaxed monetary policy but this may have little impact due to weak loan demand. In contrast, India has been stronger than anticipated in the first half of the year – however existing drought conditions will likely worsen due to the emerging El Nino event. This could drive inflation higher and trigger intervention by the Reserve Bank of India.
- We have revised our **global growth forecast** for 2023 to 3.0% (from 2.9%), reflecting an upgrade to India that more than offset a small downward revision for China. Among AEs, there were mostly small downward revisions, but these were offset by a lift in expected US growth. For 2024 we expect growth to be even weaker (at 2.6%), particularly in the AEs, before a recovery in 2025 to 3.1%, assisted by the unwinding of monetary policy from its current tightness. This outlook is weaker than the long-term average of 3.4% (since 1980).
- Risks around the outlook have become increasingly balanced, however much will depend on the path of inflation and central bank patience (particularly as energy price risk is re-emerging) along with various geo-political pressures (Russia-Ukraine conflict and US-China tensions).
- For more detail on the global outlook, please see the Forward View – Global, released yesterday.

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Australian Economic Outlook

For Australia, our forecasts for GDP growth have strengthened marginally, reflecting a slightly stronger than expected result for Q2, an upward revision for Q1 and small improvement to our outlook for Q3. Nonetheless, we continue to expect growth to be well below trend at 1.1% over 2023 and 1.4% in 2024, weighed down primarily by sluggish growth in household spending as inflation and monetary policy weigh on households. The unemployment rate is expected to edge higher over Q4 to 3.9% before increasing to around 4.9% by the end of 2024. We also see inflation moderating to 4.4% by end 2023 and 3.1% by end 2024. On rates, we continue to pencil in one last hike in November before the RBA remains on hold until mid-next year.

- **The unemployment rate ticked up from 3.5% to 3.7% in July and remained there in August.** The rise partly reflected record participation rates as employment growth remains robust. We continue to see employment growth slowing as the year progresses, and the unemployment rate rising back to around 4% by end-2023 and 5% by end-2024. The Q2 WPI was slightly softer than expected at 0.8% q/q (3.6% y/y) and the broader Q2 National Accounts measure of average wages was also subdued. We still expect a pickup in Q3, enough to see growth over 4% by the end of 2023 before the softening labour market begins to ease wage pressures in 2024.
- **Consumption growth was very weak in Q2, and we expect this to continue into 2024.** Household consumption growth edged lower to 0.1% q/q (1.5% y/y) in Q1 and without a 5.8% q/q increase in vehicle purchases, overall consumption would have been flat. Discretionary consumption declined for the third consecutive quarter, down 0.5% q/q, while consumption of essentials remained robust, rising 0.5%. Overall per capita real consumption has been falling for two consecutive quarters as individual households cut back in the face of inflation and interest rate pressures. More timely data on nominal spending suggest consumption has been resilient through the first part of Q3. However, in real terms consumption likely remains subdued and we forecast this to remain the case into 2024, with per capita spending continuing to contract.
- **Business investment continued to rise in Q2 and business conditions remain resilient through August.** Business investment again grew at a robust pace in Q2, up 2.1% q/q and 8% over the year on an underlying basis. New machinery & equipment investment increased 4.3% q/q and new building construction also rose, up 0.3%, while new engineering construction fell 0.4% q/q. More recently, business conditions in the NAB Monthly Business Survey rose 3pts in August to +13 index points, still well above long-run average levels. The confidence and forward orders measures both edged up though they remain below average, weighed down by deep negatives in the retail sector.
- **The housing market continues to face the opposing forces of higher interest rates and strong demand from the rebound in population growth.** The Corelogic 8-Capital City dwelling price index rose by 1% in August after slowing to 0.8% m/m in July, and has now regained more than half its losses after falling by 9.4% from its peak in early 2022. Rents growth has slowed slightly over recent months but remains up 9% y/y across the capitals with vacancy rates declining slightly in August after ticking up over recent months. National accounts data shows the volume of new building investment rose in Q2, however this was offset by falling work on alterations & additions. Building approvals appear to have stabilised in trend terms.
- **Net exports made a significant contribution to Q2 GDP growth, adding 0.8 ppts as exports rose sharply.** Export volumes rose by 4.3% q/q in Q2 supported by coal and services exports, while imports only grew 0.7% q/q, including a fall in goods imports (-0.2% q/q) offset by tourism-related services debits (up 4.7%). The monthly nominal trade balance declined by $2.2b in July, falling to $8.0b, with exports falling and imports rising. Further ahead, we continue to expect weak demand to weigh on imports.
- **The monthly CPI indicator for July showed further improvement in inflation but this is likely to regress in coming months as more services prices are updated.** The headline monthly measure eased to 4.9% (from 5.3%) though the ex-volatiles measure continues to track at a higher rate 5.8% (from 6.1%). Petrol prices have risen and the broader impact of higher energy costs remains a risk. Likewise, the large minimum wage rise in July will likely add pressure on the cost side for Q3. That said, as the labour market loosens and consumer demand growth slows we expect to see an ongoing moderation in inflation through 2024, falling to around 3% by the end of the year.
- **We continue to see one further hike by the RBA – likely in November.** The recent run of activity data suggests there may be some downside risk to this, but the resilience in the labour market and potential for 'sticky' services still present an upside risk. The RBA now clearly sees rates working to slow the economy alongside the impact of inflation weighing on households' real income growth – seeing a period of below trend growth over this year and next. We continue to see the RBA shifting back towards neutral from mid-2024 with inflation clearly returning to target and unemployment up near 5% on our forecasts.
- **The AUD/USD weakened further over the month, currently trading around US64.5c.** We continue to see the Aussie ending the year at around US66c before tracking higher over 2024 – ending 2024 at around US73c.

For more detail on the Australian outlook, please see the Forward View – Australia, released on Tuesday.

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