Australian Economic Update

GDP Q2 2023 – Growth remained subdued in Q2

NAB Group Economics

Bottom line

GDP rose by 0.4% q/q (2.1% y/y) – a tenth lower than we had expected but in line with consensus and slightly stronger than the RBA's August SMP (0.2%). With an upward revision to Q1 (now 0.4%), today's release shows that the economy broadly maintained momentum, despite a further small slowing in consumption growth, helped by government infrastructure and business investment spending. More broadly, the GDP release confirms our understanding of the unfolding dynamics in the economy evident in other data – the key being the ongoing fall in discretionary spending and also goods consumption (ex-motor vehicle purchases), while services spending was flat. It also reflects the ongoing impact of post-pandemic dynamics with higher than usual volatility in some components including trade and business inventories.

Today's result will have little direct implication for monetary policy in the near term. The RBA has become increasingly confident that higher rates are working to slow demand and see a better balance within the economy – and today's data provides further evidence of this. On the nominal side, price pressures remain elevated but broader measures of wages remain well within the RBA's tolerance. However, the productivity picture remains unhelpful – though is difficult to read on a quarterly basis.

We continue to see below trend growth over each of the next two years, driven by weak household consumption and softness in dwelling investment. While the pandemic continues to fade, an ongoing recovery in trade and a rebalancing in consumption continues to play out which could lead to ongoing volatility in measured output in the near-term.

Key points

- **On activity**, **a further small slowing in consumption growth was offset by strength in public and business investment** – meaning domestic final demand maintained its quarterly momentum – while trade and inventories were volatile. Dwelling investment showed further weakness, though there was a small rebound in new building – likely supported by a large pipeline of work and ongoing recovery in supply chains. On the production side this was mirrored in notable gains in the construction and transport industries. Again, the rebalancing of goods and services remained evident with both retail and wholesale detracting while accommodation & food services saw a small gain.
- **Broader wage and labour cost growth measures continue to track at higher rates than pre-pandemic but do not appear excessive.** In annual terms non-farm average earnings per hour picked up to 3.1% y/y (but was down in the quarter) - notably below the WPI. Growth in nominal unit labour costs (average earnings adjusted for productivity) remains elevated but edged lower in the quarter. In annual terms, this measure continues to track at its strongest rate since pre-GFC (outside of the volatility impacted COVID period) at 7.6%.
- **Domestic price pressures remain elevated.** The consumption and DFD deflators ticked up on a quarterly basis, increasing 1.3% and 1.2% respectively (both 0.1ppts higher than in Q1) although they are still falling in over-the-year terms. The broader GDP deflator fell in the quarter, driven by a large fall in the terms of trade.
- **For households, the pressure of higher rates and inflation remain evident. The savings rate continued to fall, though by less than last quarter, and at 3.2% remains positive**. This suggests that while real incomes are being pressured, households are adjusting both savings and consumption. How they use the remaining stock of saving built up during the pandemic remains a key unknown but will be important going forward given the weak outturn in consumption over the past two quarters.

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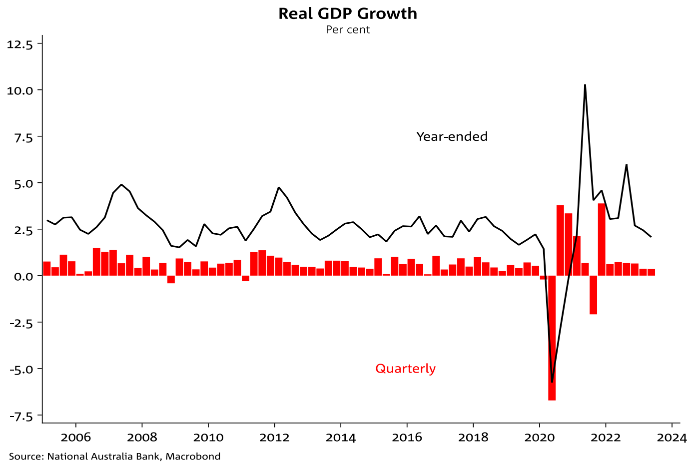
Key figures

Key aggregates	q/q % ch		y/y % ch
	Mar-23	Jun-23	Jun-23
GDP (A)	0.4	0.4	2.1
GDP (E)	0.5	0.4	2.5
GDP (I)	0.3	0.3	2.1
GDP (P)	0.3	0.4	1.7
– Non-Farm GDP	0.3	0.3	2.2
– Farm GDP	2.1	1.1	-3.0
Nominal GDP	2.2	-1.2	3.6
Real gross domestic income	1.1	-1.5	-1.1
Real net national disposable income per capita	0.8	-2.1	-2.1
Terms of trade	2.7	-7.8	-12.7



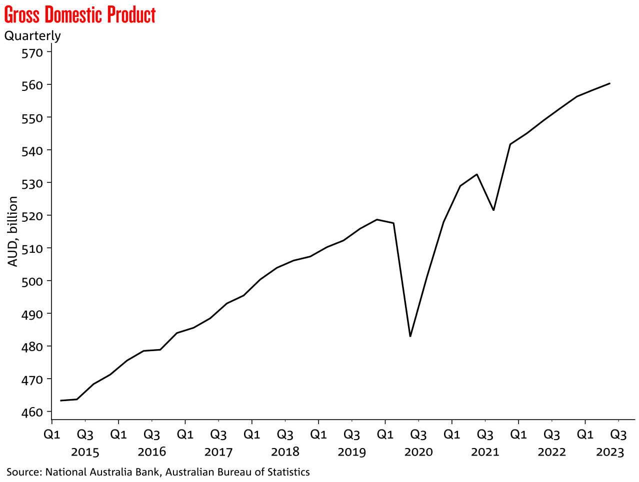
Details

- **Household consumption** growth edged down to 0.1% q/q (1.5% y/y), from a revised 0.3% q/q growth rate in Q1. A 5.8% q/q increase in vehicle purchases supported the result, likely reflecting some supply chain normalisation, without which, overall consumption would have been flat. Discretionary consumption declined for the third consecutive quarter, down 0.5% q/q, with falls in recreation and culture (down 2.5%), household furnishings (down 2.5%) and tobacco and alcohol – though transport services consumption continued to recover, rising 3.2%. Essential consumption remained robust, rising 0.5%, including increases in dwelling services and utilities. Overall goods consumption rose 0.3% q/q while services consumption was flat.
- **Business investment** again grew at a robust pace, up 2.1% q/q (underlying basis). Q1 growth was also revised up to 3.6% (from 2.9%) and underlying business investment grew by 8% over the year. New machinery & equipment investment increased 4.3% q/q, assisted by improved availability of motor vehicles and other equipment because of supply chain improvements (including reduced port backlogs). Intellectual property product investment increased by 2.2% q/q - its strongest growth in two years - and new building construction also rose (0.3%). In contrast, new engineering construction fell 0.4% q/q. As has generally been the case since the start of 2022, the non-mining sector was the key driver, with mining sector investment falling in the quarter.
- **Dwelling investment** fell for the third consecutive quarter, down 0.2% q/q to be 1.1% lower y/y. New dwelling investment rose 1.2% q/q but was more than offset by a 2.3% fall in alterations & additions which have consistently trended down from stimulus-related highs seen in 2021. Overall, dwelling investment is down around 6% from its peak in mid-2021.
- **Public demand** grew by a robust 1.8% q/q (1.3% on an underlying basis). Its fastest pace since March quarter 2022. This was largely driven by strong public investment (up 8.2% q/q or 5.5% ex transfers). According to the ABS this reflected work on large-scale transport, health and education projects, but was also due to a 16% q/q increase in the very volatile national defence investment component. Public consumption also grew, but by a more moderate 0.4% q/q, as state and local government consumption declined in the quarter.
- **Net exports** made a significant contribution to GDP growth, adding 0.8 ppts. Export volumes rose by 4.3% q/q. While reasonably broad-based, there were particularly large increases in coal, helped by improved weather conditions (11% q/q after -9% in Q1), and travel service credits (18% q/q) again grew strongly. The ABS notes that the international student numbers are now above their pre-pandemic level; with total travel credits still 12% below the end 2019 level, this implies overseas tourism and business traveller numbers are still well off their pre-COVID-19 level. Imports only grew by 0.7% q/q, including a fall in goods imports (-0.2% q/q) due to weakness in consumer and capital goods, but with services debits up 4.7% (mainly travel).
- On the **production side** of the accounts, most sectors saw small increases with the largest coming in electricity, gas, water & waste (up 2.9% q/q), rental, hiring and real estate (up 2.6%), construction (2.2%) and administrative and support services (1.8%). A 0.9% increase in healthcare & social assistance also contributed to overall growth. Wholesale trade saw a fall, down 1.5%, as did mining, down 1.3%.
- **State final demand (SFD)** growth was generally strong, led by Qld and SA at 1.3% q/q. Vic (0.7%), NSW (0.8%) and WA (0.4) also rose but NT (-1%) and Tas (-0.2%) continued to decline. Across the larger states a clear story was the strength in public demand which grew strongly, supported by a pickup in spending on investment projects. Household consumption fell slightly in Vic (-0.2%) and was flat in NSW but continue to rise in the other states.

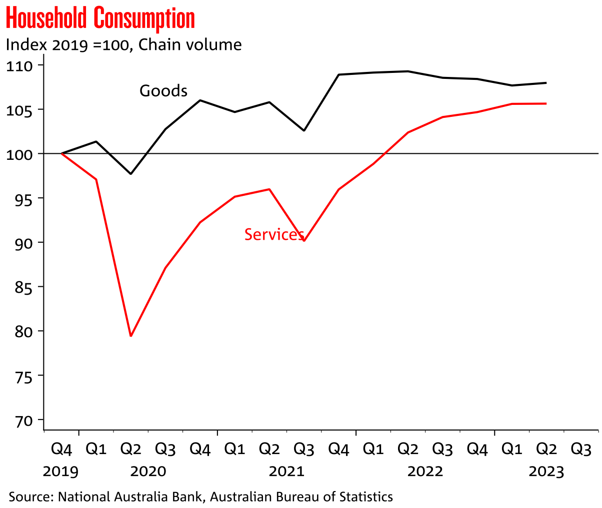
- **Household disposable income** rose 1.1%, following a 0.8% rise in Q1. Incomes were supported by continued growth in compensation of employees, up 1.6%, though underlying average earnings per hour fell 0.5% with growth in hours worked driving the increase in aggregate wages. Interest paid by households rose 10.5% in the quarter, reflecting the ongoing pass through of higher interest rates, with interest payments rising to 7.1% of gross disposable income. Adjusting for inflation (using the household consumption deflator), real disposable income declined 0.2% in the quarter. The savings rate also declined further, to 3.2%.
- The **nominal side** of the accounts continued to reflect strong inflation with growth in the domestic demand deflator picking up slightly to 1.2% q/q. However, there was a significant fall in the terms of trade in the quarter, down 7.9% q/q as export prices declined sharply, causing overall nominal GDP to fall 1.2% q/q (still up 3.6% y/y).

Key Charts

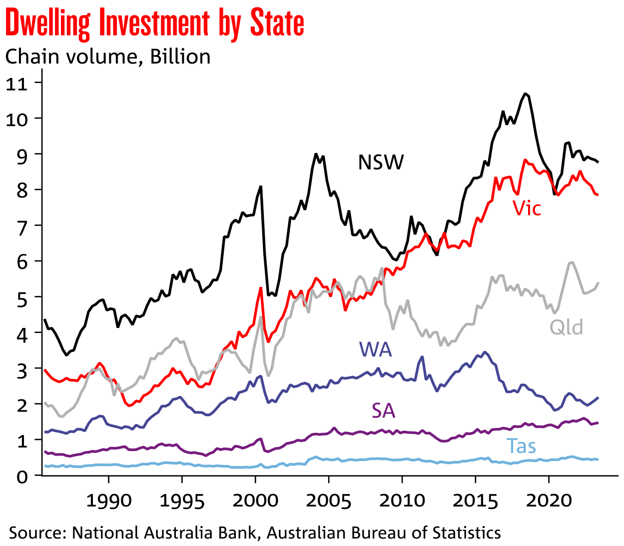
GDP is now 8% above pre-COVID levels



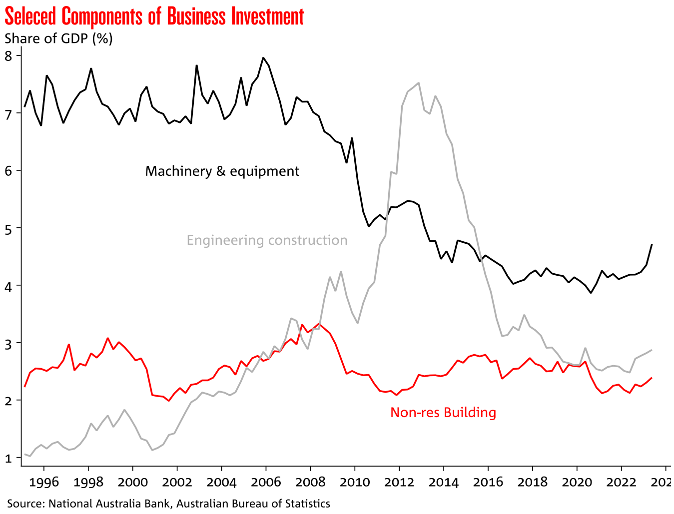
Goods spending was supported by easing in supply chains for motor vehicles



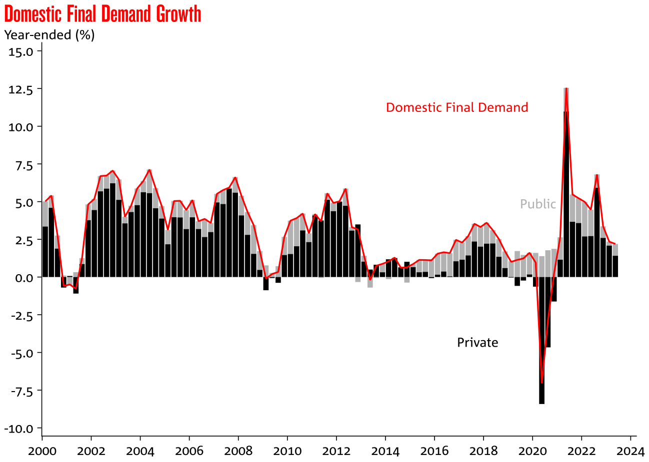
Dwelling investment still weak but picked up in Qld & WA



Business investment was an important support in the quarter.

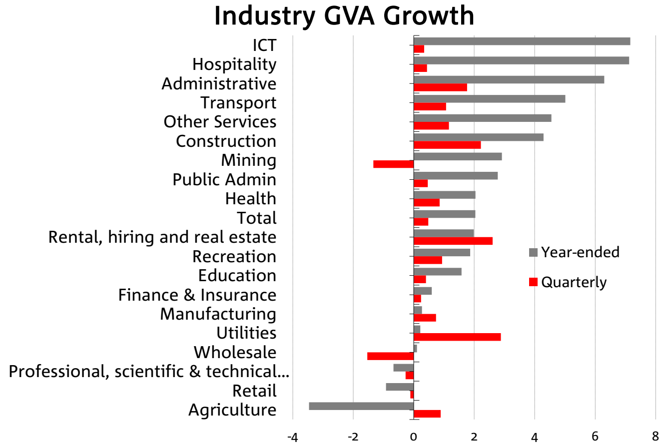


Domestic demand growth was flat in Q2

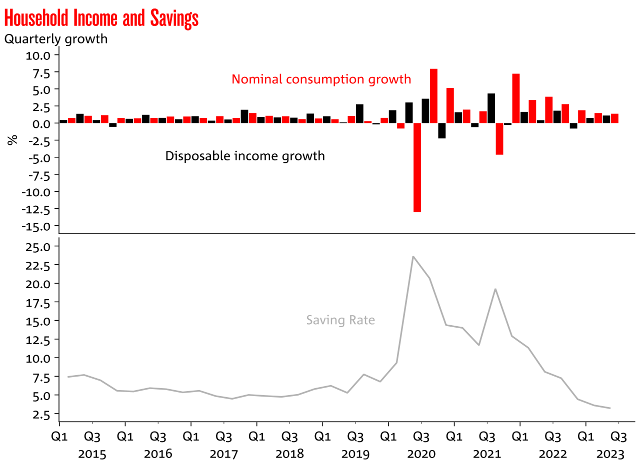


Source: National Australia Bank, Australian Bureau of Statistics

Mixed story at industry level

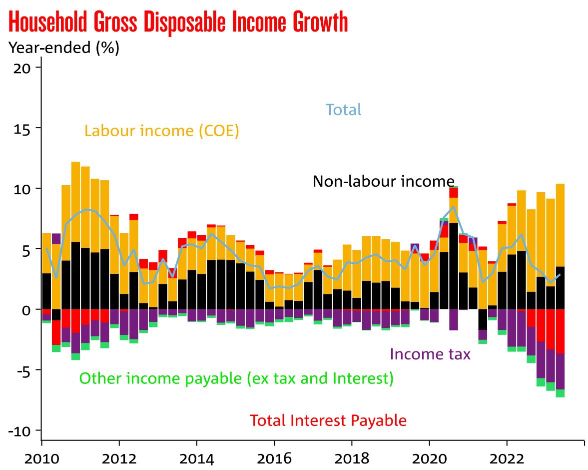


The savings rate continues to fall



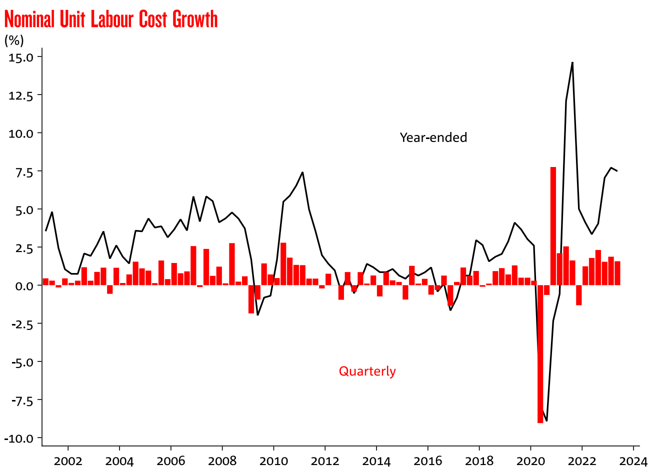
Source: National Australia Bank, Australian Bureau of Statistics

Building rates impact on disposable income



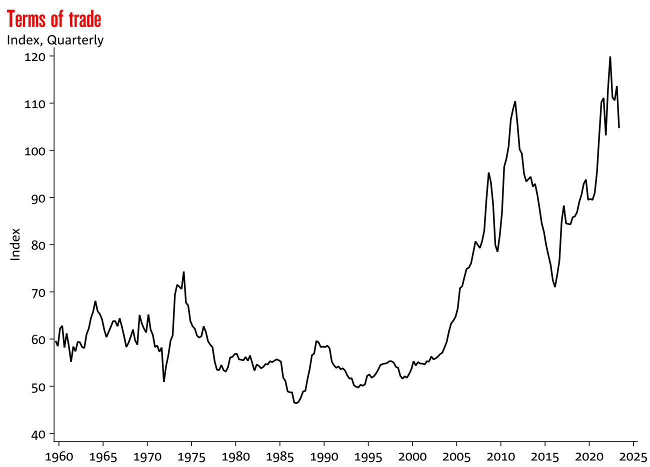
Source: National Australia Bank, Australian Bureau of Statistics

Nominal unit labour cost edged lower but remains elevated



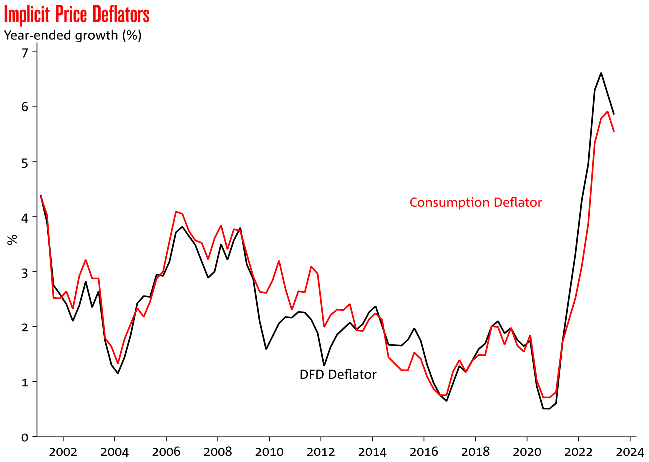
Source: National Australia Bank, Australian Bureau of Statistics

A large fall in the terms of trade – but still high



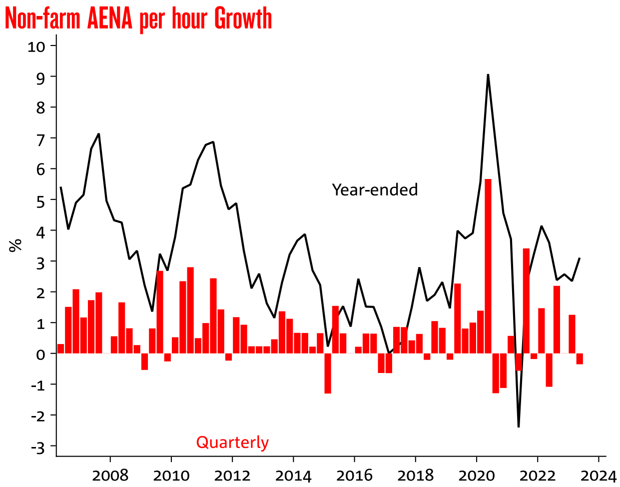
Source: National Australia Bank, Australian Bureau of Statistics

Annual domestic demand price deflator fell again even with the quarterly rate ticking up



Source: National Australia Bank, Australian Bureau of Statistics

Year-ended average earnings growth rose



Source: National Australia Bank

Summary Tables

Key variables

GDP Expenditure Components	q/q % ch		y/y % ch	Contribution to q/q % ch
	Mar-23	Jun-23	Jun-23	Jun-23
Household Consumption	0.3	0.1	1.5	0.1
Dwelling Investment	-0.7	-0.2	-1.1	0.0
Underlying Business Investment^	3.6	2.1	8.0	0.2
Machinery & equipment	4.8	4.3	6.3	0.2
Non-dwelling construction	3.6	0.3	10.8	0.0
New building	3.8	1.2	8.6	0.0
New engineering	3.5	-0.4	12.6	0.0
Public Final Demand	0.8	1.8	2.8	0.5
Domestic Demand	**0.7**	**0.7**	**2.2**	**0.7**
Stocks (a)	0.1	-1.1	-0.9	-1.1
GNE	**0.8**	**-0.4**	**1.2**	**-0.4**
Net exports (a)	**-0.3**	**0.8**	**1.3**	**0.8**
Exports	1.8	4.3	9.8	1.0
Imports	3.6	0.7	4.4	-0.1
GDP	**0.4**	**0.4**	**2.1**	**0.4**

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

Income measures

Income measures	q/q % ch		y/y % ch
	Mar-23	Jun-23	Jun-23
Real GDI	1.1	-1.5	-1.1
Real net disposable income per capita	0.8	-2.1	-2.1
Compensation of employees	2.4	1.6	9.6
Average compensation of employees (average earnings)	1.9	0.9	5.9
Corporate GOS	3.3	-6.8	-4.7
Non-financial corporations	3.9	-8.3	-6.7
Financial corporations	-0.1	1.6	7.2
General government GOS	1.4	1.5	5.4
Productivity & unit labour cost			
GDP per hour worked	-0.4	-2.0	-3.5
GVA per hour worked mkt sector	0.9	-1.6	-2.3
Non-farm nominal unit labour cost	1.9	1.6	7.3
Non-farm real unit labour cost	-0.4	3.3	4.9

State final demand

	Q/Q		Y/Y
State/ Territory	Mar-23	Jun-23	Jun-23
WA	1.1	0.4	3.7
QLD	0.5	1.3	2.9
ACT	0.4	0.8	2.1
VIC	0.9	0.7	1.9
NSW	0.6	0.8	1.7
SA	0.2	1.3	1.7
TAS	-0.2	-0.2	1.0
NT	-1.1	-1.0	0.7

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