The Global & Australian Economic Outlook in Brief: October 2023

NAB Group Economics

Global Economic Outlook

Global inflation again picked up in August. A key contributor to recent inflation trends has been energy prices, with oil prices increasing since June. Market expectations around central bank policy rates have shifted, with rates generally expected to stay at around current levels for longer in the major advanced economies (AEs). This has contributed to a tightening in financial conditions with equity markets weakening since mid-September and bond yields moving higher. Growth across the major AEs appears to have diverged significantly in Q3 2023, with it set to be strong in the US but weak (if not negative) elsewhere, while for EMs the softening evident in business surveys since May continued into September. Our forecasts for global growth are little changed this month and we continue to expect sub-par growth, by historical standards, out to 2025.

- **Global consumer price inflation** increased again in August, with consumer prices rising by 6.0% y/y (compared to the recent cycle low of 5.3% y/y in June). Emerging markets drove the pick-up, with Türkiye the main contributor as prices surged almost 59% y/y in August. Inflation also picked up in advanced economies, but only marginally, to 4.5% y/y in August (from 4.4%), and various trend measures of core inflation continue to ease.
- **Energy prices** has been a factor in recent inflation trends. From below US$70 a barrel in late June, WTI crude oil prices moved above US$90 a barrel in late September (before a subsequent dip). Any escalation in the conflict in the Middle East, following the terror attacks in Israel in early October, could add further upward pressure to oil prices. In contrast, **non-energy commodities** (as measured by the S&P GSCI) have largely tracked sideways since mid-2022.
- Interest rate settings by most **central banks** appear to be either at or near their peak. Market pricing implies the chance of the Fed increasing rates again by December is under 50% and it is even lower for the ECB. However, with growth resilient and inflation still high, expectations of when rate cuts might occur have been pushed out (i.e. they are expected to be high for longer). This shift in future rate expectations has contributed to a tightening in **financial conditions** – equity market indices in both advanced economies and emerging markets have weakened significantly since mid-September while 10-year bond yields have trended higher in recent months.
- Growth across the major **advanced economies** (AEs) appears to have diverged significantly in Q3 2023, with it set to be strong in the US and soft elsewhere (including a likely decline in Euro-zone GDP). The strength of the US economy means that major AE growth has held up this year so far (averaging around 0.4% q/q to Q3), but we expect this to ease, most likely starting in Q4. US growth should be held back by some idiosyncratic factors but more fundamentally we still expect that restrictive monetary policy will further impact growth, a point reinforced by the recent tightening in financial conditions. Fiscal policy is also becoming less supportive, particularly in the US.
- In **emerging markets** (EMs), business surveys were softer in September – with the EM composite PMI down to 52.0 points (from 52.7 in August); this measure has been trending down since May 2023. That said, China GDP growth regained some momentum in Q3, up 1.3% q/q (from just 0.5% q/q in Q2), although the annual growth rate slowed to 4.9% which is low by historical standards. As this was stronger than we expected, we have revised up our 2023 forecast for China GDP growth to 5.2% (from 5.0%) but 2024 (4.5%) and 2025 (4.8%) are unchanged. EM industrial production growth has remained relatively strong in recent months, somewhat at odds with the weaker trends in export volumes and it is hard to see it being sustained, particularly if AE growth eases as anticipated.
- Compared with expectations at the start of the year, **global economic growth** has generally held up better than anticipated. That said, indicators are pointing to a slower trend more recently – the JPMorgan global composite PMI in September moved to its lowest level since January 2023. Our forecasts have not substantially changed this month. We still expect global growth of 3.0% and 2.6% in 2023 and 2024 respectively. However, we have slightly lowered our 2025 forecast to 3.0% (from 3.1%) mainly due to a downward revision US forecast for that year. Rates of growth at these levels are below the long-term average growth rate of 3.4% (since 1980).
- The **risks** around our forecasts appear balanced. The resilience to-date in growth highlights the upside risk. A key factor will be how inflation evolves, which will drive central bank policy decisions. There are also geopolitical risks including conflict between Russia-Ukraine and in the Middle East (which could further impact energy markets), US-China tensions and the US Presidential election in 2024.

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 are unchanged. Recent data all point to continued resilience but the ongoing pass through of higher rates and high inflation still suggest consumption growth will soft in H2 2023. As such, we continue to expect below trend GDP growth of 1-1.5% in 2023 and 2024. The labour market remains very tight with the unemployment rate edging back down to 3.6% in September, but we continue to expect a gradual easing over time, to be approaching 5% by late 2024. On inflation, we expect to see a 1.1% q/q increase in Q3 CPI for both the headline and trimmed mean measures and, given the RBA's limited tolerance for a slower-than-expected return to target, continue to expect this to push the RBA Board to one further rate rise at the November meeting. Further out, inflation should continue to moderate but domestic factors including wages will be a central focus. We see rates beginning to move back towards neutral from mid-2024.

- **The labour market remains very tight with the unemployment rate edging back down to 3.6% in September.** The move was driven by a fall in the participation rate – from a record high in August – with employment growth of just 7k in the month. There are some other signs of easing with job vacancies falling 8.9% in the three months to August (albeit still very elevated) and hours worked declining slightly over the past couple of months. We continue to expect the unemployment rate to gradually rise as the economy slows, approaching 5% by late 2024. On wages, we continue to expect to see a material pickup in hourly wage growth in Q3 which should see year-ended wage growth surpass 4% by the end of 2023, before the softening labour market begins to ease wage pressures later in 2024.
- **Retail trade growth was soft in August though price movements may have played a role in the result**. The level of spending is high but households' discretionary spending is under pressure. Nominal retail trade rose 0.2% in August, softening from a more solid 0.5% in July. More recently, transaction data analysis in NAB's *Monthly Data Insights* suggested retail spending grew 0.4% in September. More broadly, the transaction data suggests overall consumer spending grew around 3% in nominal terms for Q3 as a whole. Fuel price increases contributed to spending growth in August and September, but overall spending still rose with fuel excluded. This suggests consumption growth likely remained positive in real terms for the quarter, although the result is still expected to be subdued in a continuation of the slow consumption growth seen in Q2.
- **Business conditions in the NAB Monthly Business Survey eased but remained above the long-run average** at +11 index points. Capacity utilisation remains high and there has been gradual improvement in forward orders, while confidence was steady and remains below average. The survey also showed some positive signs for inflation with cost pressures and price growth easing though both remain elevated. Business credit growth picked back up in August, rising 0.6% m/m after a softer 0.2% rise in July.
- **House prices continue to rise at a brisk pace and the very low rental vacancy rate continues to support strong rents growth.** The CoreLogic 8-capital city dwelling price index rose by 0.9% in September while the combined regional index continues to track at a lower rate, rising by 0.4% m/m. Prices are likely to end the year 8-10% higher and we continue to see gains of around 5% over 2024. The ongoing increase in prices, from a high level, amidst the sharp increase in interest rates has led to a very sharp deterioration in housing affordability over the past year – and rental vacancies remain very low across the capitals. Amidst strong demand, the supply side remains challenged. Building approvals rose 7% in August but total building approvals remain 23% lower over the past year.
- **The trade balance rose by $2.3 billion in August, driven by a rise in non-monetary gold exports.** Freight services costs continued to moderate, falling to 3.8% of good imports. More broadly, Q2 balance of payments data showed goods import prices have continued to gradually decline but remain elevated. Looking ahead, trade volumes remain a key source of volatility for the forecasts.
- **We expect the Q3 CPI to show a quarterly print of 1.1% for both headline and underlying inflation, seeing the year-ended rates fall to 5.2% and 5.0% respectively.** The key drivers of the headline are a large rise in fuel prices which were up sharply in the quarter, offset by declines in fruit & veg and childcare. Of some concern is our expectation for services inflation (ex telco and travel) to continue to strengthen in annual terms. The moderation in year-ended inflation from its peak has been reasonably sharp, and inflation will likely moderate quickly to around 4% – but bringing it back into the RBA's target band from there could be more challenging.
- **We continue to see the RBA hiking a further 25bps in November, before staying on hold until the second half of 2024.** The RBA remained on hold in October for the fourth consecutive month and made very few changes to the post meeting statement. However, the post-meeting minutes stated the Board had very low tolerance for a slower return of inflation to target, and we expect the Q3 CPI data to push the Board to do more. 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 US63c and at times lower.** 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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