

# The Forward View: Australia Sep 2024



## Growth weak as consumers remain on sidelines

### NAB Economics

#### Overview

- Recent data continue to show the economy experiencing a period of weak growth – with private sector activity impacted by the soft consumer. The Q2 national accounts showed modest growth of 0.2% q/q (1.0% y/y) – led by the public sector, with household consumption falling slightly and business and dwelling investment making little contribution.
- The NAB Monthly Business survey for August suggests that momentum has seen little improvement in Q3, with business conditions below average and confidence in negative territory. That said, capacity utilisation remains elevated, consistent with the view that aggregate demand and supply in the economy are yet to fully come into balance.
- Overall, our forecasts are largely unchanged in terms of growth, the labour market and inflation.
- Feeding through the Q2 National accounts data and slightly lowering our outlook for consumption sees GDP growth of 1.0% this year, 2.2% in 2025 and 2.3% in 2026.
- Our assessment of the labour market is that it continues to cool, even though trend employment growth has remained very strong over recent months. This has been reflected in a gradual rise in the unemployment rate, which we expect to continue over the next 6 months. The unemployment rate is expected to reach 4½% by end 2024 and remain there through 2025 but importantly employment growth is expected to remain positive.
- Our inflation profile is unchanged. We see trimmed-mean inflation falling to 3.5% by end 2024 and back into the top of half of the RBA’s target band by end 2025.
- On rates, our view is also unchanged, where we expect the RBA to remain on hold at next week’s meeting and until May 2025. However, the recent data flow skews the risk around our call to February. We still expect the RBA to cut rates by around 125pbs over a year or so once the cutting phase begins, taking the cash rate back to around neutral at 3.1%
- Overall, our forecasts still imply a soft landing for the economy and a gradual easing of the cash rate back towards neutral. This contrasts with some other advanced economies, including NZ, where growth has slowed more, and the labour market has loosened more significantly.

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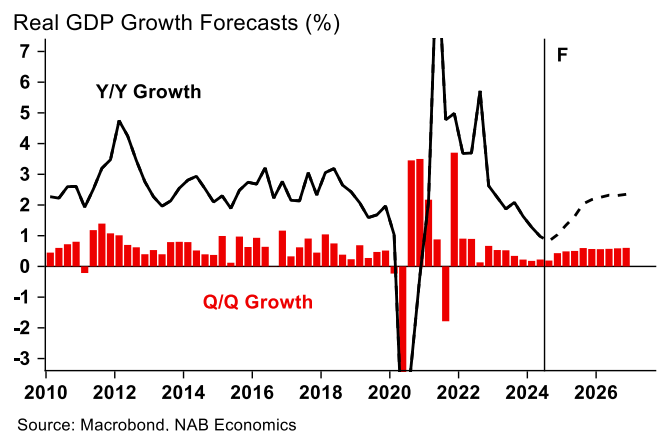
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#### Key Economic Forecasts

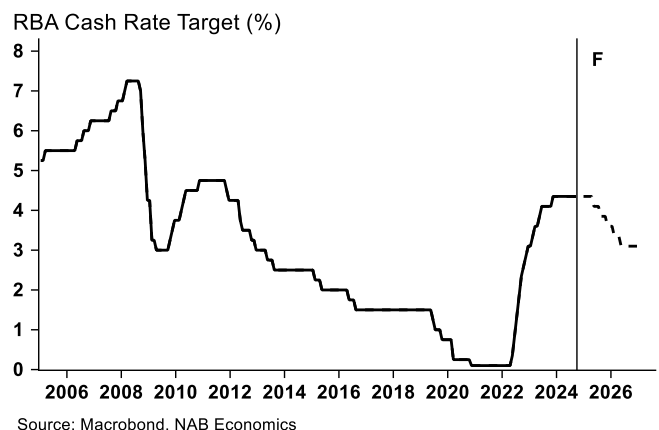
	2023	2024(f)	2025(f)	2026(f)
Domestic Demand (a)	2.8	1.6	1.8	2.4
<b>Real GDP (annual ave)</b>	<b>2.0</b>	<b>1.0</b>	<b>1.8</b>	<b>2.3</b>
<b>Real GDP (year-ended)</b>	<b>1.6</b>	<b>1.0</b>	<b>2.2</b>	<b>2.3</b>
Employment (a)	3.4	2.5	1.6	1.7
Unemployment Rate (b)	3.9	4.5	4.6	4.4
Headline CPI (b)	4.1	2.9	2.9	2.3
Core CPI (b)	4.3	3.5	2.6	2.3
RBA Cash Rate (b)	4.35	4.35	3.60	3.10
\$A/US cents (b)	0.68	0.69	0.75	-

(a) annual average growth, (b) end-period

#### Chart 1: GDP forecasts



#### Chart 2: Cash rate profile



## Labour Market & Household Consumption

**The labour market continues to show signs of cooling, though employment growth has remained robust.**

Despite very slow economic growth confirmed in the Q2 National Accounts, employment growth has remained positive over recent months. Nonetheless, the unemployment rate has gradually risen reflecting the strength of population growth and record participation. This is very much in line with our expectations for how the labour market would evolve and we expect this pattern to continue for the remainder of the year, taking the unemployment rate to around 4½% before growth begins to strengthen in 2025.

Alongside a cooling labour market, the data continues to support our assessment that wage growth has peaked with National Accounts measures of labour costs easing in Q2. Total COE growth edged down to 0.9% q/q (albeit it remains up 6.3% y/y) and non-farm average earnings per hour rose a modest 0.3% q/q. We expect underlying hourly wage growth to continue to ease, stabilising in the 3-3.5% range over time.

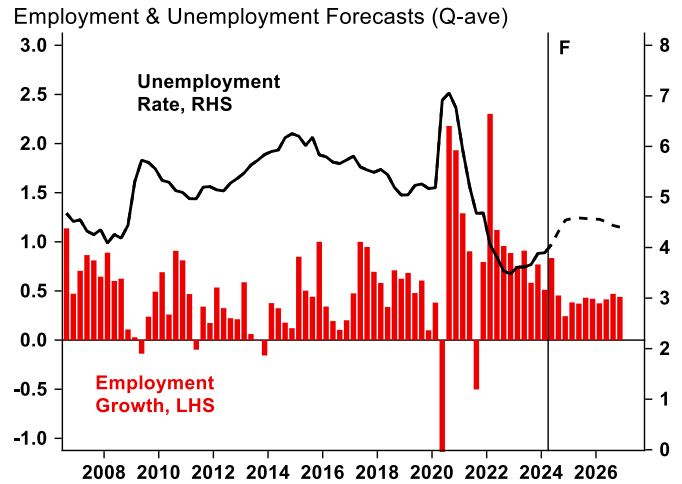
**As expected, Q2 consumption growth was very weak and we have tempered our expectations for a rebound – at least in the near term.**

Real household consumption fell 0.2% in the quarter, leaving year-ended consumption growth very weak at just 0.5%. The decline was driven by a substantial 1.1% q/q fall in discretionary categories including transport services (down 4.4%) clothing & footwear (down 1.6%), and hotels, cafes & restaurants (down 1.5%). Purchases of vehicles also declined 2.6% q/q, though furnishings & household equipment rose 4.0% q/q. Partly offsetting the discretionary consumption decline was a 0.5% q/q rise in essential consumption, led by a 2.4% rise in electricity, gas & household fuels as some government subsidies unwound.

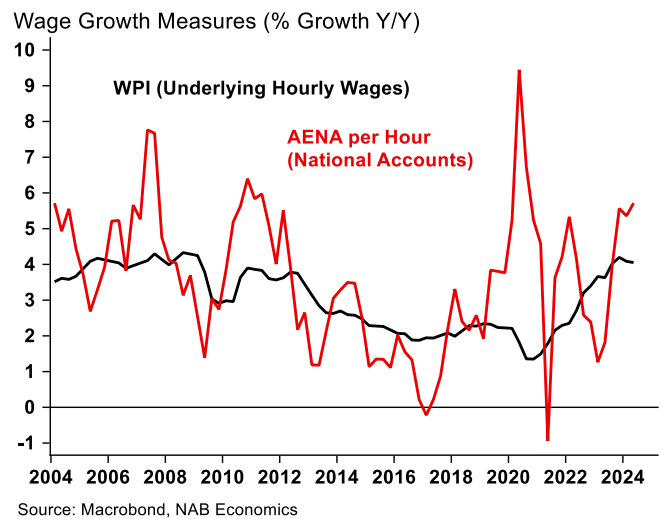
A bigger-picture view of the patterns of essential and discretionary spending shows that the level of aggregate discretionary consumption has remained broadly steady since its peak in early 2022, reflecting a period in which households have gradually rebalanced their consumption behaviours back towards essentials after the initial post-pandemic rebound, and as inflation and interest rates have eroded buying power.

Easing inflation, tax cuts and energy subsidies will all help to put households in a better position through the second half of 2024 but the early indications of how this will affect consumption are mixed, with retail spending flat in July but NAB transaction data showing a pickup in August. This aligns with our expectation for some of the boost to incomes to show up as a rise in savings rates at first before consumption strengthens over time. There will also be some mechanical volatility in household and government consumption growth as subsidy effects flow through. Nonetheless, we see consumption growth eventually normalising especially as rate cuts begin – which we expect in H1 2025.

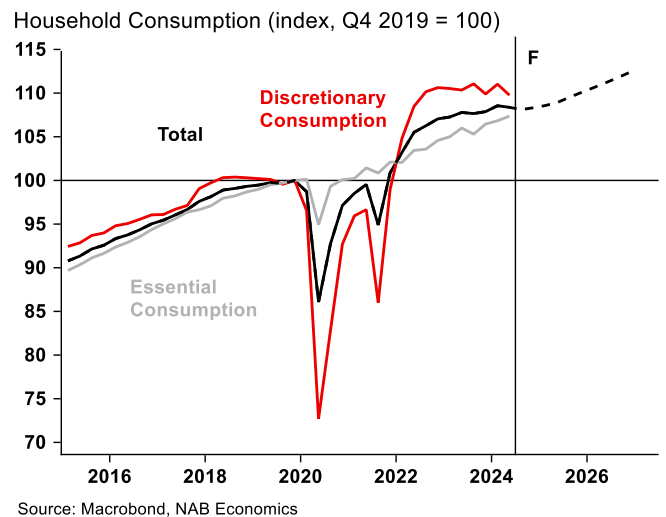
**Chart 3: The unemployment rate is expected to rise to around 4½%**



**Chart 4: Wage growth appears to have peaked**



**Chart 5: Discretionary consumption fell in Q2, driving a small fall in overall consumption**



## Housing & Construction

**The national accounts showed only a small tick-up in dwelling investment in Q1 despite the ongoing strength in housing demand.**

By state, investment rose in Vic (2.4%) and QLD (4.3%) and WA (4.7%). Dwelling investment declined in NSW (down 4.0%). It rose by less in SA (up 1.5%) and declined 2.4% in Tasmania. Dwelling commencements and completions data for Q2 will not be available until mid-October but these data overall suggest we are unlikely to have seen a major pickup in completions – with new supply continuing to track around 160k dwellings p.a.

Building approvals data paint a slightly more positive picture having trended higher through mid-2024. However, while they appear to have come off their low point and are broadly around 2019 levels, they remain significantly lower than the mid-2010s, and well below the rate required to match population growth.

**Despite the ongoing undersupply of new housing (and potential hangover from recent strong population growth) both house price and rents growth continue to moderate.**

The CoreLogic 8-capital city house price index rose by 0.5% in August – up slightly on the 0.3% increase in July - which saw annual growth ease further to 7.1%. Prices continue to rise very strongly in Perth, up another 2% in the month, while Brisbane and Adelaide also continued to rise briskly, increasing 1.1% and 1.4%, respectively. Sydney prices continue to gradually increase, up 0.3%, while conditions in Melbourne remain significantly weaker – with prices falling for the 5th consecutive monthly – down 0.2% m/m.

Prices in Perth, Adelaide and Brisbane are now between 65-72% higher than their pre-COVID levels. In Sydney prices have risen almost 30% and, in contrast, Melbourne prices have risen just 10% since early 2020. Prices in Melbourne also remain around 5% below their previous peak in March 2022 - prior to the sharp increase in interest rates. This contrasts with Sydney, Perth, Adelaide and Brisbane which continue to reset all-time highs.

In the rental market, capital-city advertised rents growth continued to cool (falling 0.1% in the month) with a second consecutive fall in Sydney rents, and a flat outcome in Brisbane after a decline last month. Growth in Melbourne, Adelaide and Perth has also slowed over the past two months. Overall, annual rents growth has now slowed to 7.2% y/y. Rental vacancy rates have increased a little from their lows over recent months (in part due to seasonal effects) but generally remain low. That suggests while rents growth is slowing, like house prices, rents will continue to be supported by strong demand and a softer supply back drop in the near term.

Chart 6: Signs dwelling approvals stabilising at a low level

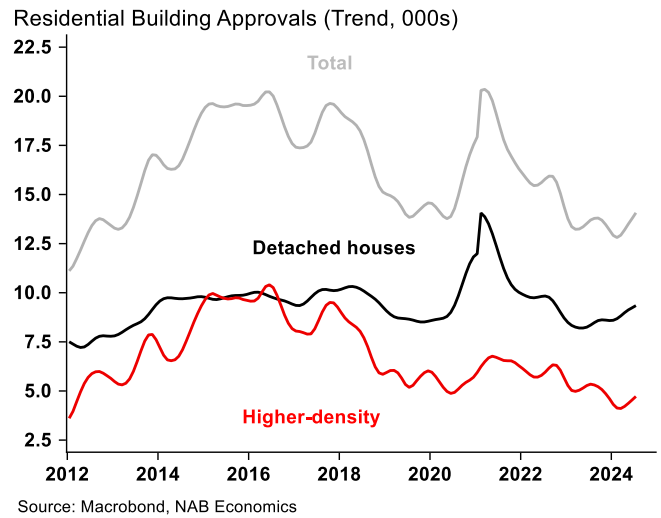


Chart 7: Price growth moderating overall, but large differences across the capital cities

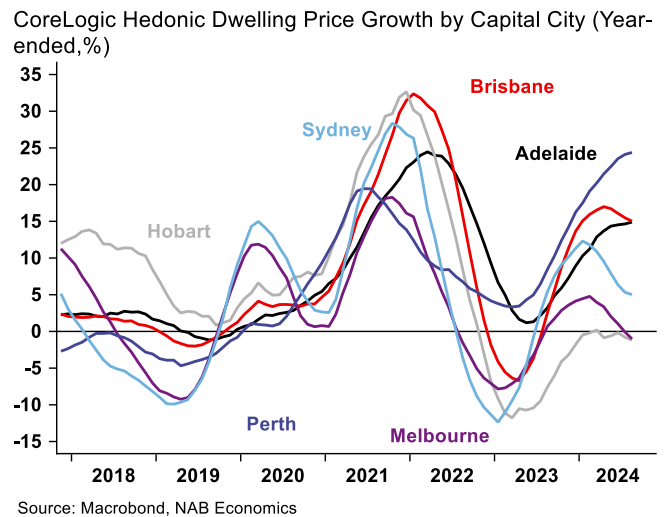
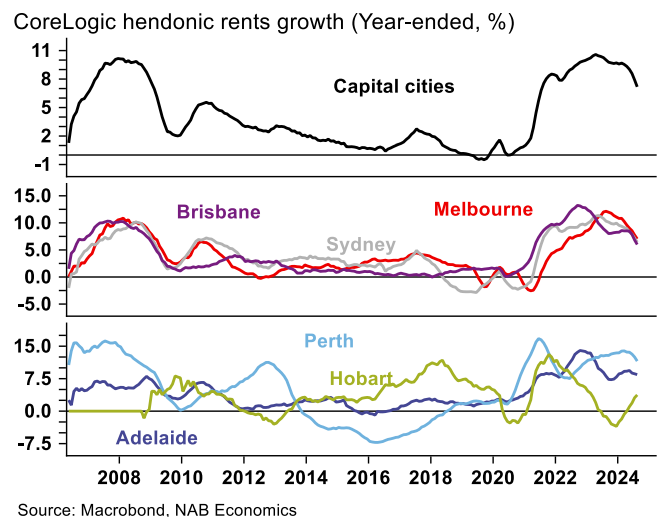


Chart 8: Rents growth easing from a high level



## Business, Trade & FX

### Business investment growth remained limited in Q2 while business conditions continued to ease in August.

Underlying business investment edged up 0.1% q/q in Q2. New machinery and equipment investment declined (-2.4% q/q) with new building construction (+0.5 q/q), new engineering construction (1.4% q/q) and intellectual property products (+1.6% q/q) providing offsets. On a year-ended basis, underlying business investment only grew 2.2% y/y - the softest it has been since 2020. The level of business investment remains high outside of the mining investment boom period.

The latest ABS Capex Survey results continue to point to a slowdown in nominal capex growth in 2024-25, around 1.7% (based on historical realisation ratios) after a nominal outcome of 10.2% in 2023-24. However, at least some of this slowing is likely to reflect easing cost growth. In Q2 the national accounts growth in the business investment deflator eased to 2.2% y/y, the lowest it has been since mid-2021.

The August [NAB Monthly Business Survey](#) showed business conditions easing to +3 index points while confidence remained low at -4 index points – suggesting activity in the private sector has remained under pressure through the beginning of Q3. However, capacity utilisation remains above average which should provide some ongoing support for business investment.

### Services exports picked up in Q2 as net exports contributed 0.2ppts to GDP growth.

Exports were up by 0.5% q/q, largely reflecting an increase in service credits as travel (+9.9% q/q) bounced back after falls in the previous two quarters. In contrast, there was a small fall in resource export volumes (-0.4% q/q) while rural export volumes again declined (-1.7%). Imports also edged down 0.2% q/q in the quarter.

The national accounts also reinforced that freight costs as a share of total goods imports have stabilised in recent quarters around 3.8%, well down on the 6.6% peak in 2022.

Overall, the nominal current account deficit widened to \$10.7b in the quarter as softer commodity prices saw the nominal trade surplus narrow and increased interest payments drove a widening primary income deficit.

### Our outlook for the AUD/USD is unchanged, with the currency expected to rise to around US69c by the end of this year before rising to around US75c over 2025.

The key to this outlook continues to be a broader softening in the USD, as the US economy slows and the Fed begins to ease its policy rate from September. However, the global growth back drop, commodity prices and sentiment around the Chinese economy will also be key factors.

Chart 9: Business conditions remain broadly around average

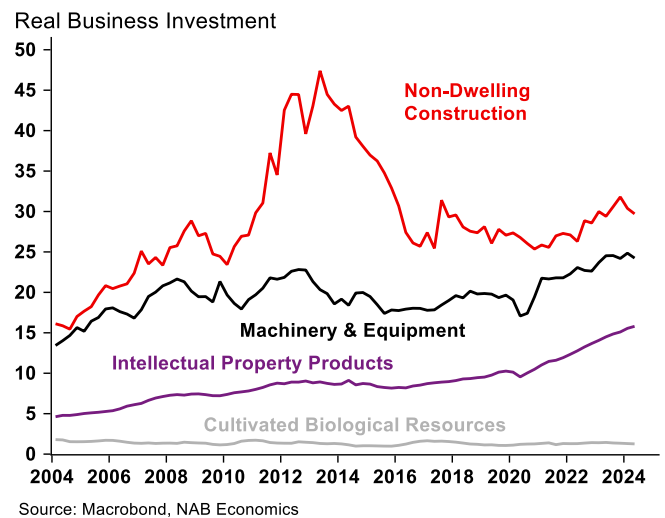


Chart 10: A rise in services credits saw net exports contribute modestly to GDP growth in Q2

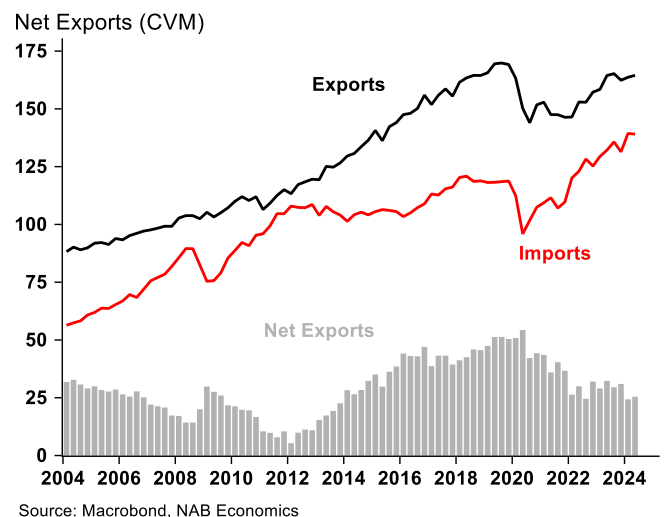
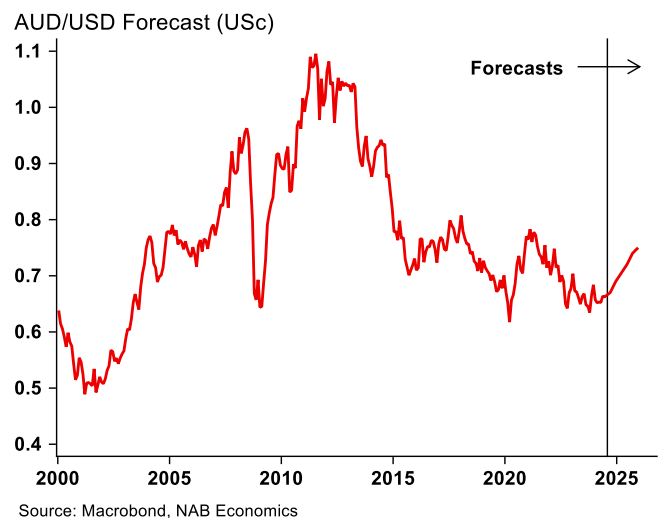


Chart 11: The AUD is expected to appreciate into 2025



## Inflation

**The monthly CPI indicator for July showed headline inflation fall to 3.5% y/y (driven by falls in electricity) while the underlying/analytical measures also eased but remain a little higher.**

However, the monthly CPI indicator is only a partial indicator – and the focus largely remains on the 2<sup>nd</sup> and 3<sup>rd</sup> months of each quarter where a larger proportion of services components are updated. Further, the analytical measures, including the monthly trimmed-mean, are by construction different to the quarterly equivalent. While nuanced underlying trends can be gleaned from the monthly indicator, the full quarterly CPI remains the key benchmark for the RBA in assessing inflationary pressure.

That said, the Q3 quarterly CPI will also be impacted by electricity subsidies and therefore print on the low-side, while also likely dragging the trimmed-mean measure down to a degree. Therefore, a clear overall read of both headline and trimmed mean will remain challenging in the near term. However, the Q2 data showed encouraging signs that a number of components of market services inflation are now easing and further evidence of that will be important in the Q3 data. The housing component remains a key risk. Rents growth remains elevated despite showing some early signs of having peaked – with monthly rental CPI inflation easing from 0.7% m/m to 0.6% m/m. That said, in annual terms rents inflation remains elevated at 7.9%. New dwelling costs in the CPI also continue to track strongly.

The broader set of price measures in the national accounts also point to price growth having remained elevated in Q2. In annual terms, both the household and domestic final demand deflators continue to rise more strongly than the CPI measure of inflation and in quarterly terms also showed little further easing.

The NAB Monthly Business Survey saw retail price growth edge up to 1.2% in quarterly terms, though rec & personal price growth eased to 0.8% in August. The overall products price measure across all sectors continues to track more softly and is broadly around pre-pandemic rates.

Our assessment is that the inflation backdrop continues to cool. While progress on disinflation has been slower in the first half of 2024 – with the bulk of disinflation prior to this driven by an easing in goods/imported inflation – we know that wage growth has likely already peaked and other cost push pressures are begging to ease (though some remain high). Further, the slightly weaker than expected consumer backdrop also suggests that businesses will be unlikely to fully pass through any ongoing pressures as demand growth cools. This has been evident particularly on the goods side to date. In terms of forecasts we continue to see underlying inflation falling to around 3.5% y/y by end 2024 and 2.7% by end 2025. By 2026 we see inflation firmly around the middle of the RBA’s target band.

Chart 12: Monthly CPI inflation eased to 3.5% in July

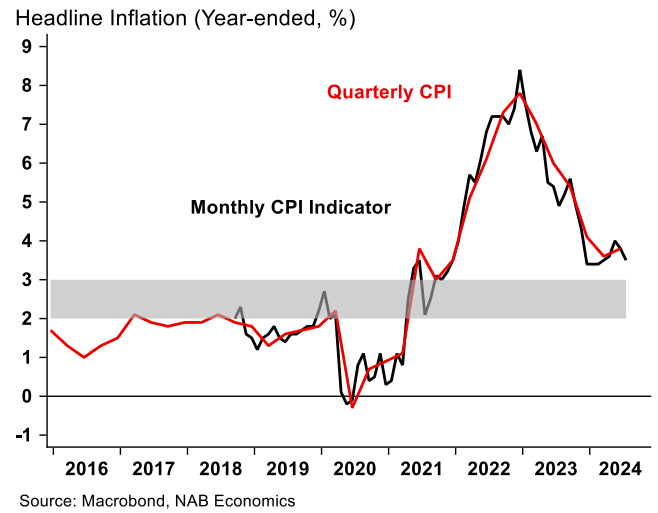


Chart 13: Survey measures of prices and costs continue to trend lower

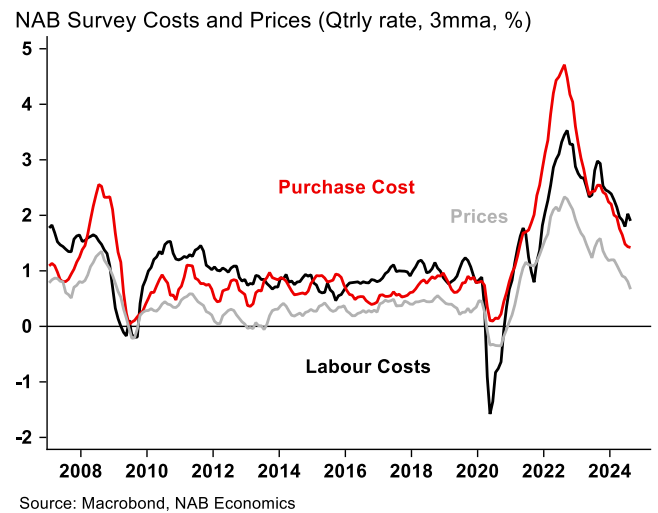
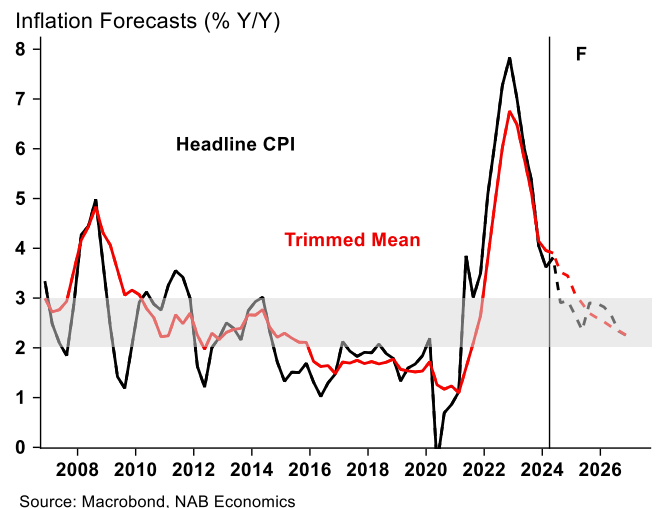


Chart 14: Trimmed mean inflation is still expected to return to the target band in 2025



## Monetary Policy

**We expect the RBA to remain on hold at the September meeting, and until May 2025. That said, we acknowledge the current data flow skews the risk to February.**

We don't see the RBA as having the full confidence to begin easing by November with a clean read of inflation remaining difficult and the fact it will take some more time for the RBA to become confident that demand and supply have sustainably come back into better balance.

Indeed, Assistant Governor Hunter's speech on the labour market showed that despite the gradual rise in unemployment over the past year or so, the labour market remains tight and continues to operate above capacity – acknowledging the fact that while wage growth has peaked it remains elevated.

This is consistent with the NAB Monthly Business Survey of capacity utilisation which remains well above its long run average but has trended down since late 2022.

However, private sector growth has slowed sharply and higher frequency indicators such as the NAB Monthly Business Conditions index suggest that growth has likely remained soft in Q3. That suggests that despite being difficult to assess in real time, that the output gap is closing.

Further, for the RBA slower growth will feed into slower labour demand and likely further increases in the unemployment rate. While we remain optimistic (and the RBA shares this outlook) that employment growth can remain positive while the labour market loosens the risks for the RBA have become two sided through mid-2024.

With the inflation back drop cooling and growth clearly slower the risk of a larger than expected deterioration in the labour market has become an offsetting risk to the uncertainty around how quickly inflation moderates over the next 18 months. The RBA's strategy of bringing inflation back to target while minimising any cycle in the labour market remains intact for now.

Though we expect the RBA to remain on hold, likely with a tightening bias, at next week's Board meeting, the statement and press conference will provide further indicators on how quickly the RBA assesses the output gap is closing following the release of the Q2 national accounts as well as an update on the risks around the labour market following the release of the August labour force data later this week. That said, we don't see an imminent change in tone from the Board with little new inflation data released over the past month.

Ultimately, we see the RBA lowering the cash rate by 125bps to around 3.1% once the Board has the comfort that inflation is moving sustainably back towards the middle of the 2-3% target band.

Chart 15: Capacity utilisation is above average

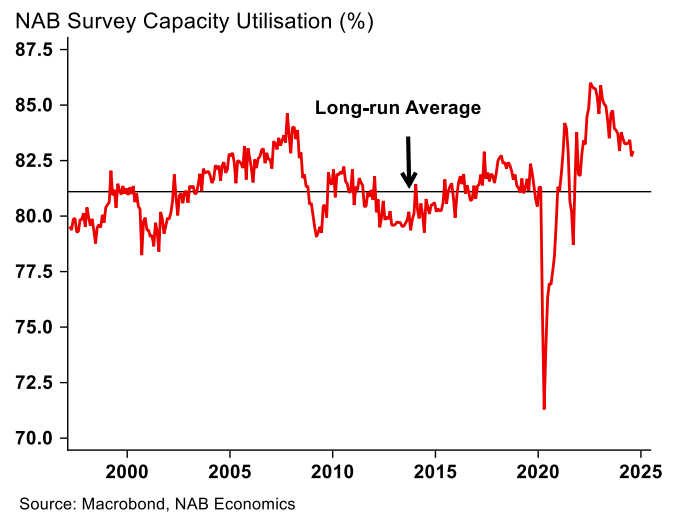


Chart 16: National accounts price growth remains strong

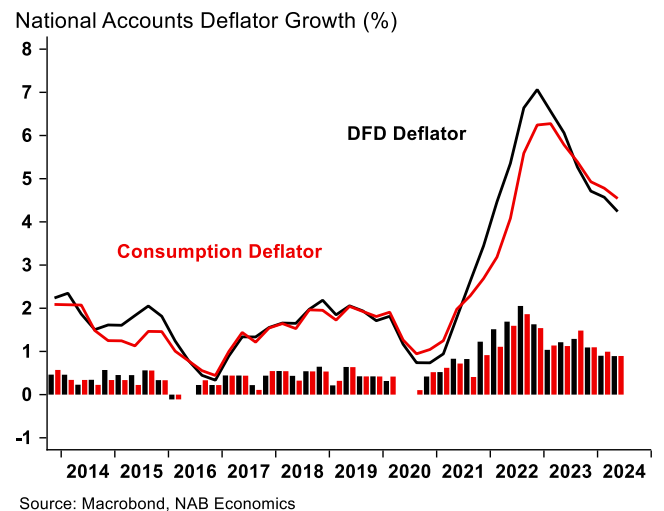
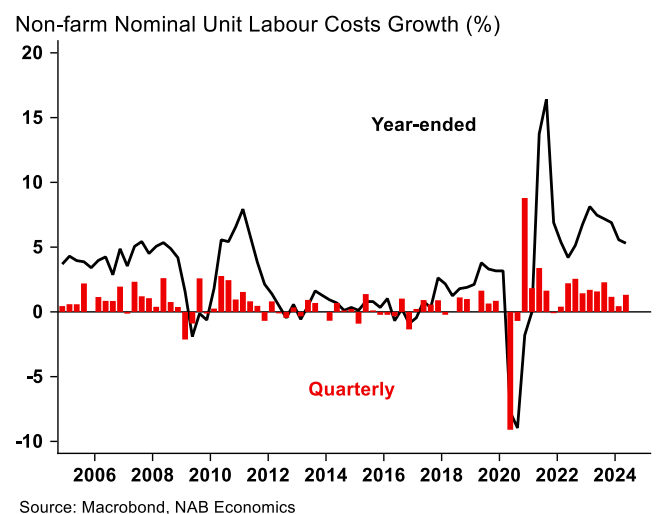


Chart 17: Unit labour costs continue to ease in annual terms but remain high



## Table of Economic Forecasts

	% Growth q/q			% Growth y/y			
	Q2-24	Q3-24 (f)	Q4-24 (f)	2023	2024 (f)	2025 (f)	2026 (f)
<b>GDP and Components</b>							
Private Consumption	-0.2	-0.2	0.2	0.8	0.4	1.6	2.1
Dwelling Investment	0.1	0.0	0.1	-2.9	0.2	0.9	2.0
Underlying Business Investment	-0.2	-0.6	0.3	9.2	-1.7	1.8	2.2
Underlying Public Final Demand	1.4	1.2	0.8	4.4	4.3	2.7	2.5
<b>Domestic Demand</b>	<b>0.2</b>	<b>0.3</b>	<b>0.5</b>	<b>2.7</b>	<b>1.4</b>	<b>2.2</b>	<b>2.5</b>
Stocks (Cont. to GDP)	-0.5	-0.1	0.0	-0.9	0.2	-0.1	0.0
<b>Gross National Expenditure</b>	<b>-0.1</b>	<b>0.2</b>	<b>0.5</b>	<b>1.8</b>	<b>1.7</b>	<b>2.2</b>	<b>2.5</b>
Exports	0.5	0.3	0.4	3.3	2.1	2.1	2.2
Imports	-0.2	0.1	0.5	4.9	6.5	2.3	2.7
Net Export (Cont. to GDP)	0.2	0.1	0.0	-0.2	-0.8	0.0	0.0
<b>Real GDP</b>	<b>0.2</b>	<b>0.2</b>	<b>0.4</b>	<b>1.6</b>	<b>1.0</b>	<b>2.2</b>	<b>2.3</b>
Nominal GDP	0.2	1.4	1.6	4.6	4.4	3.7	3.7
<b>Labour Market</b>							
Employment	0.8	0.5	0.2	3.1	2.1	1.6	1.7
Unemployment Rate (Q-Ave, End of Period)	4.1	4.3	4.5	3.9	4.5	4.6	4.4
Wage Price Index (WPI)	0.8	1.0	0.9	4.2	3.6	3.4	3.2
<b>Inflation and Rates</b>							
Headline CPI	3.8	2.9	2.9	4.1	2.9	2.9	2.3
Trimmed-mean CPI	3.9	3.5	3.4	4.1	3.4	2.6	2.3
RBA Cash Rate (End of Period)	4.35	4.35	4.35	4.35	4.35	3.60	3.10
10 Year Govt. Bonds (End of Period)	4.33	4.25	4.20	3.96	4.20	4.00	4.05
\$/US cents (End of Period)	0.66	0.67	0.69	0.68	0.69	0.75	0.75

Data are percentage growth rates over the quarter or year as noted, except where specified otherwise.

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