

Media release

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Leading Index points to steady growth around trend

The six month annualised growth rate in the Westpac-Melbourne Institute Leading Index, which indicates the likely pace of economic activity relative to trend three to nine months into the future, rose from -0.01% in July to $+0.20\%$ in August.

Westpac's Chief Economist, Bill Evans, commented, "The August reading is consistent with a trend that has been building for some months now. The positive Index growth rate follows 15 consecutive months where growth has been below trend. It is the first above trend result since early last year and the second strongest since December 2013. The Leading Index is clearly signalling that the economy is likely to continue growing around its long run trend rate of about 3% a year.

"That outlook is consistent with Westpac's forecast for growth holding steadily around a 3% pace over the course of both this year and next.

"The Leading Index growth rate has lifted sharply over the course of 2016, from a 1.44% below trend reading in March to 0.20% above trend in August.

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“Almost all components have contributed to the improvement. The biggest lift has come from: commodity prices (+0.64ppts); US industrial production (+0.36ppts); the sharemarket (+0.30ppts); and the Westpac–MI Unemployment Expectations Index (+0.26ppts). However, there have also been small positives from: the yield spread (+0.09ppts); dwelling approvals (+0.04ppts) and the Westpac-MI Consumer Sentiment Expectations index (+0.03ppts). The only offset to these improvements has been from a deterioration in aggregate monthly hours worked (−0.08ppts).

“The bulk of the improvement in Index since the start of the year has come from improved international conditions (commodity prices; US industrial production; share market; and yield spread). However it has been pleasing this month to see some improvement also coming locally from unemployment expectations and consumer confidence.

“The Reserve Bank Board next meets on October 4. This will be the first meeting under the new Governor Lowe. It is extremely unlikely that there will be any change to rates at that meeting.

“Since the cash rate returned to its historical low of 3% in 2013 all six subsequent cuts have occurred at meetings in February, May, August or November when the Bank has a ‘fresh’ print on inflation and is able to communicate any forecast changes in its quarterly Statement on Monetary Policy. That suggests that the next ‘live’ meeting will be November 1.

“We expect rates will be held steady in November as well. Signs of stability in the real economy, as signalled in this report, point to steady rates being the most appropriate

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policy. Of course there is always the possibility of a shock from the inflation report on October 26 but both our inflation forecasts and our assessment of current high RBA ‘inertia’ around moving again this year point to stability in November”, Mr Evans said.

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