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Melbourne Institute Nowcast of Australian GDP

April 2022

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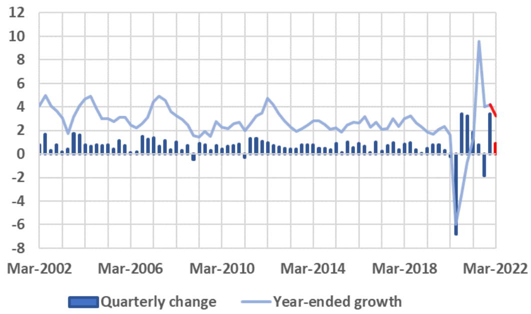
March Quarter GDP – Second Nowcast

- The Australian economy grew strongly in the December quarter (3.4 per cent, Figure 1), reflecting the re-opening of the economy after the Delta COVID-19 outbreak and the associated lockdowns. Household consumption made a sizable contribution (Figure 2). Growth over the year was a strong 4.2 per cent.
- Drawing on timely monthly indicators, our second nowcast for growth in the March quarter is 0.9 per cent, taking year-ended growth to 3.2 per cent (Figure 1).
- This nowcast mainly reflects data up to February and is stronger than our first nowcast last month (0.5 per cent). Underpinning the revision is the strong recovery in the labour market in February from Omicron-related disruptions. This was maintained in March, which is a good outcome as floods affected the Eastern coastline, including Brisbane and Sydney.
- The other sector making a sizable contribution was trade. Commodity prices have been boosted by the ongoing war in the Ukraine.
- The official March quarter GDP data will be released by the ABS on Wednesday 1 June.
- Anticipations of an imminent rate rise have increased, in part as the RBA Governor omitted reference to being patient in the last monetary policy statement. Underlying inflation, which the RBA focusses on, increased by 1.4 per cent in the March quarter, to be 3.7 per cent higher over the year. This is its highest annual rate since early 2009.

Likely Impacts of a Monetary Policy Tightening

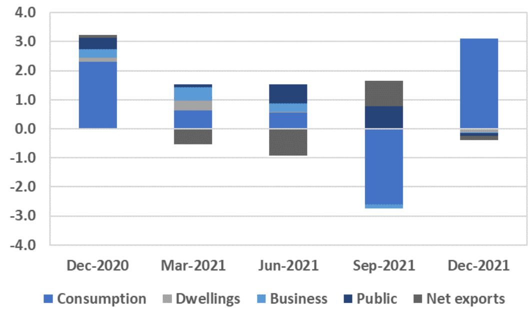
- Interest rates are expected to rise and there are numerous channels through which monetary policy affects economic activity. For example, one channel works through the open-economy aspects as the real exchange rate appreciates, decreasing the competitiveness of Australian exports. Another is to increase the cost of borrowing, thereby reducing the demand for houses and likely lowering house prices. Different channels vary in the speed in which they impact on economic activity.
- In general, inflation is likely to fall and prospects for wages growth are contingent on continuing improvements in the labour market.
- While the economy is recovering, the pace of recovery is still uncertain, given the state of the global economy.

Figure 1: GDP Growth
(chain volume, per cent)



Sources: ABS, up to December quarter 2021, and Melbourne Institute.

Figure 2: Selected Contributions to GDP Growth in the December Quarter (ppt)



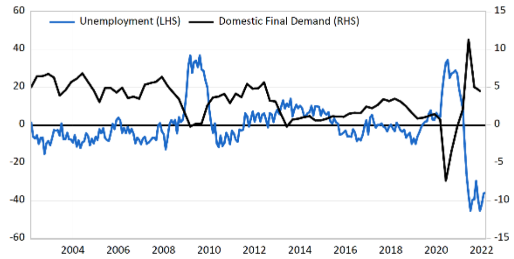
Source: ABS, up to December quarter 2021.

Unemployment rate unchanged and hours worked decline only slightly[1]

In February the labour market recovered strongly from an Omicron-related sharp downturn in January. Encouragingly, these were maintained in March, with the unemployment rate constant at 4 per cent, which is low by historical standards. The underemployment rate is a broader measure of slack in the labour market and it improved, reaching its lowest level for around 13 years. The employment-to-participation ratio was unchanged at well-above its immediately pre-pandemic levels.

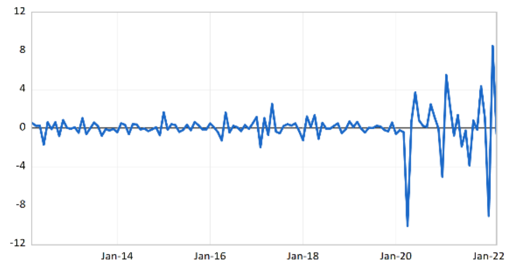
The nowcasting model contains two labour market indicators. The first is year-ended growth in unemployment; it was broadly similar to last month and continues to point to strong growth in domestic final demand (Figure 3). The second indicator is monthly growth in hours worked, which following the strong recovery in February fell only marginally (Figure 4).

Figure 3: Unemployment and DFD
(year-ended growth, per cent)



Source: ABS, up to March 2022 (unemployment).

Figure 4: Growth of hours worked
(monthly, per cent)



Source: ABS, up to March 2022.

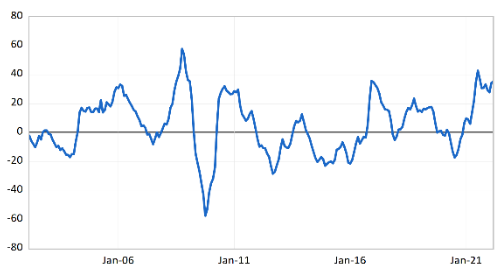
Commodity prices weaken while the trade surplus widens

The RBA Index of Commodity Prices in A$ increased by nearly 4 per cent in March, reflecting both higher rural and non-rural prices. It is around 43 per cent higher over the year (Figure 5). This measure is based on export prices, which include a combination of contract and spot prices. If instead the bulk commodities (such as iron ore and coal) are measured using spot prices only the Index is around 68 per cent higher over the year.

Making substantial contributions to growth over the year are LNG, which are closely linked to crude-oil, coking and thermal coal prices. The war in Ukraine has been boosting energy and some rural prices.

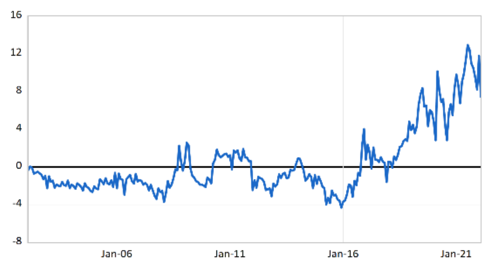
The trade surplus narrowed in February, with the value of exports being flat whereas imports increased by 12 per cent. This increase reflected greater imports of some processed industrial supplies and fuels and lubricants, with higher energy prices contributing.

Figure 5: Commodity Prices
(year-ended growth, per cent)



Source: RBA, up to March 2022 (commodity prices).

Figure 6: Trade balance
($ billion)



Source: ABS, up to February 2022.

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[1] Our nowcast model uses monthly information regarding labour market conditions, housing and business lending, retail sales, housing approvals, consumer expectations, trade conditions and commodity prices to gauge current economic conditions. **We note that the nowcast is currently in the experimental stage.**

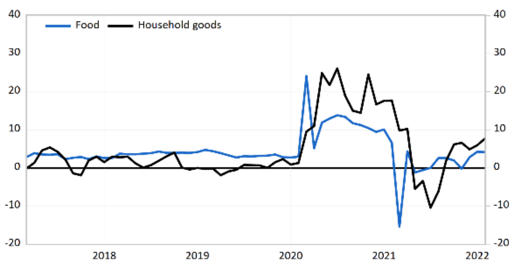
Retail trade improves, whereas consumer sentiment weakens

The value of retail trade grew by 1.8 per cent in February, which is broadly similar to last month, to be 9.1 per cent higher over the year. The nowcast model includes two components of retail trade: food and household goods. These are volatile on a monthly basis; over the year the value of household goods is 7.8 per cent higher, which is strong by pre-pandemic levels (Figure 7).

A less positive signal for the outlook for consumption growth is given by the more timely Westpac-Melbourne Institute Consumer Sentiment Index, which remained below 100 in April, indicating the number of pessimists outweighed optimists. This weakening was in the Current Conditions Index, which is in the nowcasting model (Figure 8); alternatively, the Expectations Index improved modestly. The fall in the former was due to less optimistic responses about both the state of family finances relative to a year ago and whether it was a good time to buy major household items.

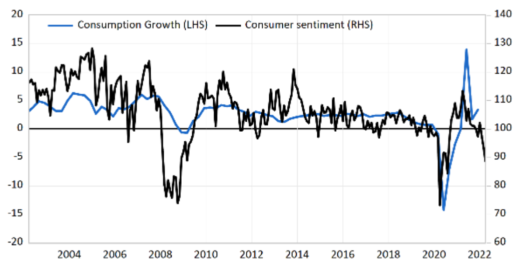
Consumption growth was exceptionally strong in the December quarter as the economy recovered from Delta-related disruptions, and therefore a considerable slowing is to be expected. One possible reconciliation of the different messages from the retail trade and consumer sentiment data is that the former is nominal, whereas higher inflation may be weighing on sentiment.

Figure 7: Retail trade
(year-ended growth, per cent)



Source: ABS, up to February 2022.

Figure 8: Consumer Sentiment and Consumption
(index and year-ended growth, per cent)



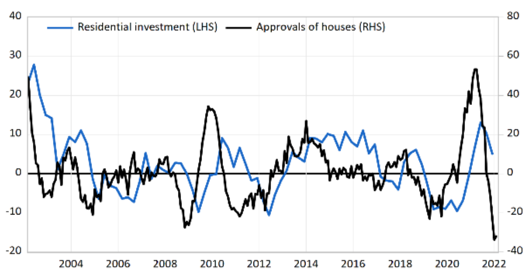
Source: ABS and Melbourne Institute, up to April 2022 (consumer sentiment).

Building approvals improve and credit growth strengthens

Building approvals rose sharply in February. However, they are volatile, and approvals for houses, which appear in our nowcasting model, remained substantially below their level a year ago and continue to point to an imminent decline in residential investment (Figure 9). Alternatively, growth in housing credit, which also is in the nowcasting model, edged higher in February (Figure 10). Some of this momentum may be lost in the future as the RBA begins to tighten monetary policy.

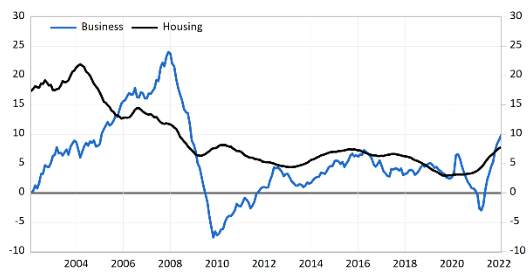
The upswing in business credit growth continued in February (Figure 10). This is encouraging as business investment's share of GDP has been falling since the peak of the mining boom a decade ago.

Figure 9: Dwelling Approvals and Residential Investment
(year-ended, per cent)



Source: ABS, up to February 2022 (approvals).

Figure 10: Housing Credit and Business Credit
(year-ended growth, per cent)



Source: RBA, up to February 2022.

Next release: 28 May 2022.

Melbourne Institute Nowcast of Australian GDP

The Melbourne Institute Nowcast of Australian GDP used to date the business cycle use monthly information regarding labour market conditions, housing and business lending, retail sales, housing approvals, consumer expectations, trade conditions and commodity prices in order to gauge current economic conditions.

We note that the nowcast methodology currently is in an experimental stage.

For information on the data contained in the report contact the Melbourne Institute, The University of Melbourne, on (03) 8344 2196.

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