MELBOURNE INSTITUTE
Applied Economic & Social Research

Melbourne Institute Nowcast of Australian GDP

October 2023

THE UNIVERSITY OF MELBOURNE

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Released 26 October 2023

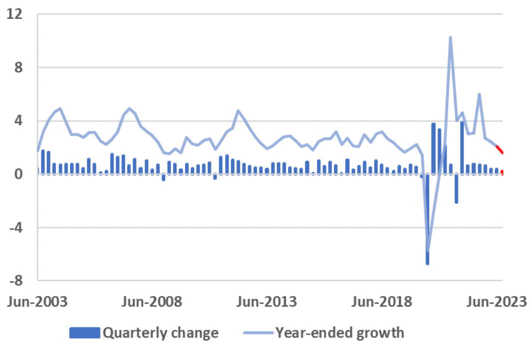
September quarter – second nowcast

- The Australian economy grew by 0.4 per cent in the June quarter, to be 2.1 per cent higher over the year.
- Our second nowcast for growth in the September quarter is 0.2 per cent (Figure 1), which is slightly lower than last month (0.3 per cent). Recent indicators for the Australian economy have been mixed; it appears unlikely that the substantial contribution from trade which occurred in the June quarter will be repeated. On the other hand, inventories being drawn down were a major drag on growth and while scant timely indicators on inventories exist, this drag may be less in the September quarter. Our nowcast corresponds to year-ended growth slowing further and reaching 1.6 per cent.
- The official September quarter GDP data will be released by the ABS on Wednesday 6 December.
- While we have lowered our nowcast, prospects further out have improved. The Westpac-Melbourne Institute Leading Index this month moved higher, although it still signals that below - trend growth will extend well into 2024.
- Long yields in the U.S. have continued to move higher, with FRB Governor Powell attributing this to factors including the "resilience" of the real economy to higher rates, the fiscal situation, and higher term premia. Long yields have also increased in Australia, with the yield spread turning positive, after having been negative for around 6 months. A negative yield spread is often use as an indicator of a likely downturn.

Australian underlying inflation too high – further rate hike in play …

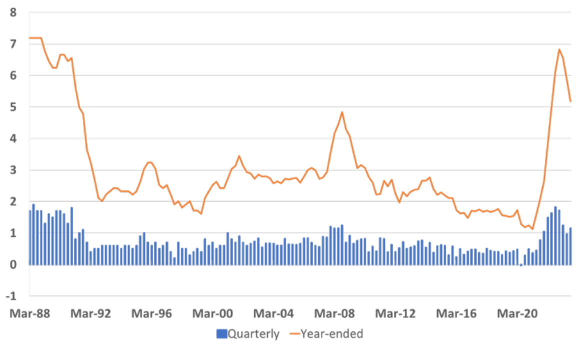
- Headline inflation was 1.2 per cent in the September quarter, and 5.4 per cent over the year. This is down from 6 per cent in the June quarter.
- Growth in rents continued to be very strong in the capital cities – for example, in Brisbane it was 9.5 per cent over the year – despite being dampened by an increase in Commonwealth Rent Assistance. Higher rebates for childcare and electricity also moderated inflation.
- Higher petrol and diesel prices were a contributing factor. Alternatively, annual growth in both the prices of food and non-alcoholic beverages and new dwelling purchases by owner-occupiers moderated further, although quarterly growth in the latter remained strong.
- The Reserve Bank focusses on underlying inflation, which attempts to provide an indication of the inflation pressures which are likely to persist. This was 1.2 per cent in the September quarter – a pick up from the June quarter, and at the upper end of market forecasts – and 5.2 per cent over the year (Figure 2). This probably is uncomfortably high for the RBA, and the Governor recently highlighted that "The Board will not hesitate to raise the cash rate further if there is a material upward revision to the outlook for inflation".

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



Sources: ABS, up to June quarter 2023, and MI.

Figure 2: Underlying Inflation
(per cent)



Sources: ABS, RBA and calculations.

The unemployment rate improves, but other labour market indicators weaken …[1]

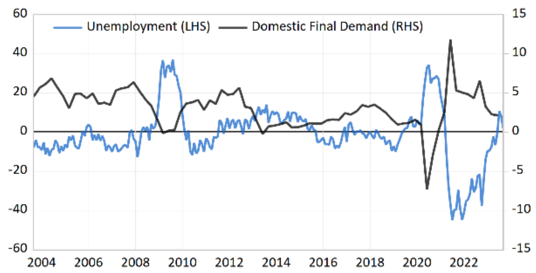
In September the unemployment rate improved, falling slightly to be a low 3.6 per cent. The underemployment rate, which captures people working less hours than they desire, also declined by 0.2 percentage points.

These improvements, however, were accompanied by a 0.3 percentage point fall in the participation rate, due to lower participation in the labour market by males (female participation increased). Nevertheless, at 66.7 per cent, the participation rate for all people remains at a high level by historical standards.

The nowcasting model includes two labour market indicators. The first, namely year-ended growth in unemployment, improved in November, but still indicates weak domestic final demand growth is likely (Figure 3). The second, hours worked, fell by 0.4 per cent (Figure 4).

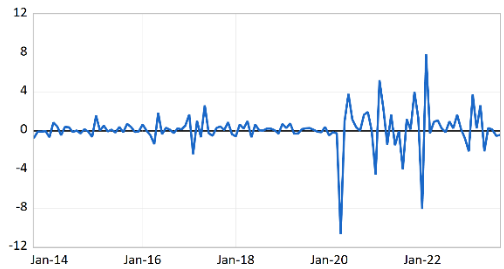
Overall, it appears that the labour market is cooling, but remains tight – as is signalled by the low unemployment rate. That the labour market has not weakened further, given the weak output growth which has occurred in 2023 to date and the sharp tightening in monetary policy, is surprising. A timelier labour market indicator is the Westpac-Melbourne Institute Unemployment Expectations Index, which recently improved, but remains considerably less optimistic than a year ago.

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



Source: ABS, up to September 2023 (unemployment).

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



Source: ABS, up to September 2023.

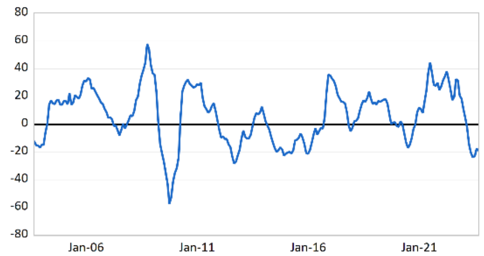
Global commodity prices strengthen…

The RBA Index of Commodity Prices in A$ increased by 3.9 per cent in September, underpinned by a lift in global (i.e. US$) commodity prices, with prices for the bulk commodities rising 5.7 per cent. Nevertheless, the Index in A$ was 17.1 per cent lower than a year ago.

Crude oil prices in US$ increased sizeably in September, and despite the conflict in the Middle East, this has only been partially unwound in October to date. Crude oil influences both Australian retail petrol prices – and hence inflation – and the prices received for Australia's substantial LNG exports.

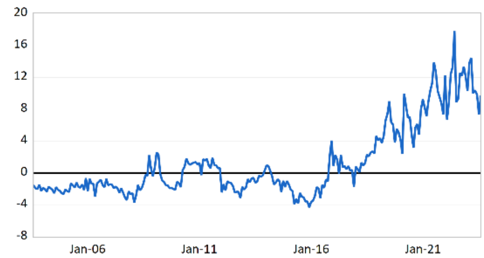
The narrowing in the trade balance which occurred in July was reversed in August (Figure 6). This was primarily due to a 4 per cent lift in the value of exports, although imports also fell, due mainly to lower capital imports. The relationship between these and business investment, however, is loose.

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



Source: RBA, up to September 2023.

Figure 6: Trade balance
($ billion)



Source: ABS, up to August 2023.

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[1] Our nowcasting 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.

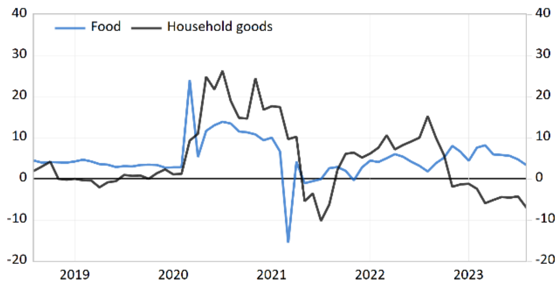
Consumer sentiment improves, but remains very weak…

The Westpac-Melbourne Institute Consumer Sentiment Index improved in October but remained below both its level at the beginning of the year and its long-run average.

The nowcasting model focusses on the Current Conditions Index (Figure 8). This improved substantially in October, particularly due to more positive responses about whether it is a good time to buy major household items. Nevertheless, the Current Conditions Index remains very weak and continues to suggest that a further slowing in consumption growth is likely (Figure 7).

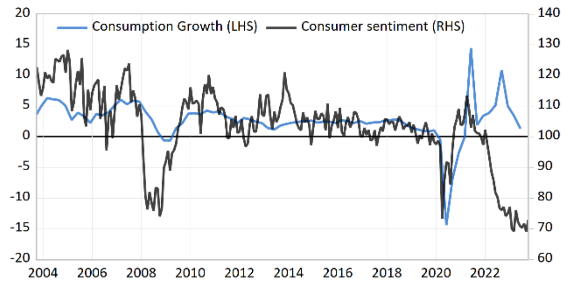
The ABS also produces an experimental consumption indicator, based on bank transaction data. Focussing on its year-ended growth (due to only a limited time series being available), this improved in August, but is much weaker than earlier in the year. Unsurprisingly, give the cost-of-living pressures facing many Australians, growth in discretionary spending has fallen markedly this year, although growth has also declined for non-discretionary spending.

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



Source: ABS, up to August 2023.

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



Source: ABS and Melbourne Institute, up to October 2023 (consumer sentiment).

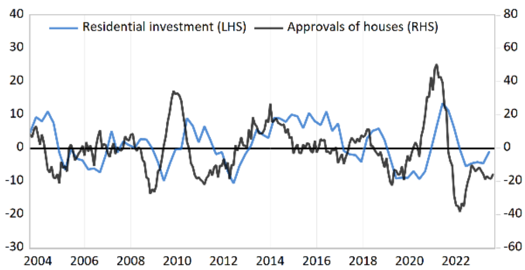
Dwelling approvals increase, whereas credit growth slows further…

Dwelling approvals increased by 7 per cent in August, with a lift in approvals for both private sector houses and particularly other dwellings, such as apartments. The nowcasting model focuses on the former, which while more than 15 per cent lower than a year ago, have fluctuated around a broadly similar level for most of 2023 (Figure 9).

Residential investment, despite Australia's strong population growth, appears unlikely to increase substantially in the September quarter. The other housing indicator included in the nowcasting model, namely year-ended housing credit growth, eased further in August (Figure 10), although its monthly growth has been roughly constant since late last year.

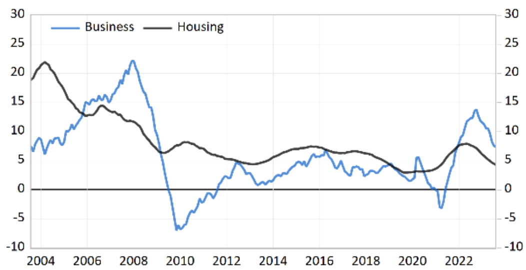
Year-ended business credit growth slowed in August (Figure 10). The September Monthly NAB Business Survey suggested that business conditions moderated but remained above average. Likewise, the survey's measure of capacity utilisation decreased, but continues to indicate that firms have little spare capacity. While a possible response may be firms investing to expand capacity, declining business credit growth seems to run counter to this.

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



Source: ABS, up to August 2023 (approvals).

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



Source: RBA, up to August 2023.

Next release: 30 November 2023.

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.

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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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