Media release

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Building approvals lift the Leading Index

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 –0.54% in February to –0.09% in March.

Westpac Chief Economist, Bill Evans, commented, "Despite this recent lift the Index has still registered four consecutive months in which the growth rate has been negative. This continues to support the signal that growth through the first two to three quarters of 2019 is likely to be below trend.

"Moreover the lift in the growth rate was entirely due (0.44ppts of the 0.45ppt lift) to one component – dwelling approvals – which printed a 19.1% lift reflecting a boost in the volatile high rise sector in NSW and Victoria. Note that approvals for the stable 'private detached houses' sector were actually down by 3.6%.

"It is reasonable to expect a substantial reversal in the dwelling approvals series next month.

"The signal from the Index has been consistent with the weak momentum in the second half of 2018 revealed in the print of the December quarter national accounts.

In the second half of 2018 growth momentum slowed to an annualised pace of 1% from a 4% pace in the first half of the year.

"Westpac expects growth in the Australian economy in 2019 to be around 2.2% – significantly below trend which is generally assessed as 2.75%.

"Key to the ongoing slow growth will be a challenged consumer as households adjust to slower than expected wages growth and falling house prices. That will be compounded by a continuation of the contraction in residential house building activity that appears to have begun in the September quarter of 2018.

"We have consistently highlighted these risks which are coinciding with a slowdown in jobs growth and investment spending as both political uncertainty and global volatility weigh on firms' employment and investment decisions.

"The Index growth rate has deteriorated over the last six months, declining from +0.18% in October to –0.09% in March. Four components have contributed to this deterioration: the yield spread (–0.33ppts); commodity prices (–0.19ppts); US industrial production (–0.11ppts); and the Westpac-MI Unemployment Expectations index (–0.07ppts).

"On the other hand, dwelling approvals (+0.28ppts); aggregate monthly hours worked (+0.10ppts); and the ASX 200 (+0.07ppts) lifted the growth rate. The contribution from the Westpac –MI CSI expectations index was unchanged.

“The Reserve Bank Board next meets on May 7. The minutes of the April Board meeting have come close to setting out an easing bias. The minutes clarify that the Board believes that lower rates will assist the Australian economy through a lower currency and a boost to disposable income. It also sets out the case for lower rates around ongoing flat inflation and an uptrend in the unemployment rate.

“Conditions for lower rates are given much more consideration than the case for a rate increase. Surprisingly, there seems to be little discussion about the Bank’s ongoing poor performance around its inflation target or the likelihood that it will once again be lowering its growth forecasts when it releases its revised forecasts in its May Statement on Monetary Policy on May 10.

“Westpac sees no reason to change its forecast that the RBA will make its first cut to the cash rate at the August meeting to be followed by a second cut in November” , Mr Evans commented.

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