Media release

20 August 2019 **Strict Embargo 10:30am**

Leading Index back at 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 –0.09% in June to +0.05% in July.

Westpac Chief Economist, Bill Evans, commented, “This is first above trend read since November last year. Further confirmation of this around trend reading would be consistent with the economy growing around trend for the last three or four months of 2019 and well into the first half of 2020.

“The Reserve Bank recently lowered its growth forecast for 2019 from 2.75% to 2.5%. With growth momentum in the first half of the year around 2% annualised the RBA is expecting momentum in the second half to lift to 3% annualised – above the trend pace of 2.75%.

“Westpac accepts that an improving housing market, tax cuts and lower rates are likely to boost momentum in the second half to around 2.5% annualised – somewhat below trend.

"That pace is a little below the current 'at trend' signal from the Leading Index. However developments so far in August around the share market, commodity prices and the inversion of the yield curve point to a likely softer August reading for the Index. That is likely to dent the current 'at trend' growth signal from the July report.

"The Leading Index growth rate has improved over the last six months from –0.71% in February to +0.05% in July. The main components driving the 0.76ppt turnaround have been the S&P/ASX 200 (+0.53ppts), dwelling approvals (+0.37ppts), and a stabilisation in the yield spread (+0.23ppts) with continued gains in commodity prices providing underlying support (+0.02ppts).

"However, since the beginning of August, global share markets have sold off sharply, the ASX is down 4% over the month to date after posting a 17% rally over the year to July. Yield spreads have also narrowed sharply again, inverting in early August as global concerns have seen long term bond yields sink to historic lows. Key commodity prices have also shown sharp falls in recent weeks, most notably spot iron ore and coking coal prices.

"Meanwhile the contribution to the Index growth rate coming from other components has deteriorated since February, including a weakening picture around US industrial production (–0.17ppts); more downbeat reads on other domestic components – the Westpac-MI CSI expectations index (–0.09ppts); aggregate hours worked (–0.08ppts) and the Westpac-MI Unemployment Expectations index (–0.06ppts).

"The Reserve Bank Board next meets on September 3. The Board is expected to keep rates on hold. The minutes of the August Board meeting noted "the Board judged it appropriate to assess developments in the global and domestic economies before considering further change to the setting of monetary policy".

"Westpac still expects the next rate cut at the October Board meeting. The Bank's recent forecast revisions assumed market pricing of one rate cut before year's end and another in the first half of 2020. Despite these assumptions the Bank was forced to lower its inflation and wages growth forecasts while raising the expected path for the unemployment rate.

"With global economic conditions deteriorating and progress towards a lower unemployment rate and a lift in wages growth seeming to be stalling the case for another rate cut in the near future is strong", Mr Evans commented.

Issued by: Westpac Banking Corporation

Bill Evans

Chief Economist

Westpac Banking Corporation

Ph: (61-2) 8254 8531

Dr. Tim Robinson

Melbourne Institute

Ph: (61-3) 83442325