

Media release

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Growth in Leading Index back in negative territory

The six month annualised deviation from trend growth rate in the Westpac–Melbourne Institute Leading Index , which indicates the likely pace of economic activity three to nine months in the future declined by 0.64 percentage points to –0.14 in March from 0.50 in February.

Westpac Chief Economist, Bill Evans commented, “This is a disappointing but not surprising result. After being negative, and therefore projecting below trend growth in the three to nine month “window”, in the February to December period last year the growth rate lifted encouragingly in February to above trend. However that has proved to be short lived and the more “normal” consistent below trend signal has resumed.

“Below trend growth through the remainder of 2015 is certainly Westpac’s view.

We expect that through the year growth in 2015 will be around 2.5%. That will be marked by below trend growth in consumer spending; sharp falls in mining investment; and flat business investment outside the mining sector.

“Recent falls in commodity prices will weigh on Australia’s terms of trade and associated income growth. These falls are also likely to impact mining production as miners may reassess their strategies around lifting production.

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“Despite reaching high levels following the 16.5% increase in 2014 new dwelling construction is likely to continue to increase in 2015 as builders respond to high pent up demand and strong demand from domestic and foreign investors.

“The persistent negative prints from the growth rate of the Index in 2014 were consistent with the Reserve Bank revising down its growth forecast for 2015 in the February Statement on Monetary Policy. In November last year it had forecast 3% growth in 2015. That forecast was revised down to 2.75% in February this year, despite taking into account the February interest rate cut and an assumed additional cut by May. The minutes from the April board meeting are implying that the Bank may further revise down its growth forecast for 2015 (probably to 2.5%) in the upcoming May Statement on Monetary Policy.

“The sharp turnaround in the growth rate between February and March (–0.64ppts) was mainly due to US industrial production (–0.25ppts); Westpac–MI Unemployment Expectations Index (–0.23ppts); Westpac–MI Consumer Sentiment Expectations Index (–0.13ppts); dwelling approvals (–0.13ppts); and commodity prices (–0.10ppts).

“Despite the deterioration this month the index has improved over the past six months, from a deviation from trend of –0.62% to –0.14%. That improvement can be attributed to: the ASX 200 (0.31ppts); commodity prices (0.29ppts); aggregate monthly hours worked (0.27ppts); and dwelling approvals (0.16ppts). Partially offsetting those improvements have been US industrial production (–0.35ppts) and Westpac–MI UE index (–0.16ppts).

“The Reserve Bank Board next meets on May 5, one week before the release of the Commonwealth Budget. For the last two months the Board has held rates steady while adopting a very strong easing bias. As discussed, the Minutes from the April

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Board meeting imply that the Bank is likely to revise down its growth forecasts in its Statement on Monetary Policy which will be released on May 8. With the sharp fall in commodity prices; a resilient Australian dollar; and a disappointing outlook for business investment it seems likely that the Board will decide to cut rates by 0.25% at the May meeting”, Mr Evans said.

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