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# Melbourne Institute Nowcast of Australian GDP & Dating the Business Cycle

June 2021

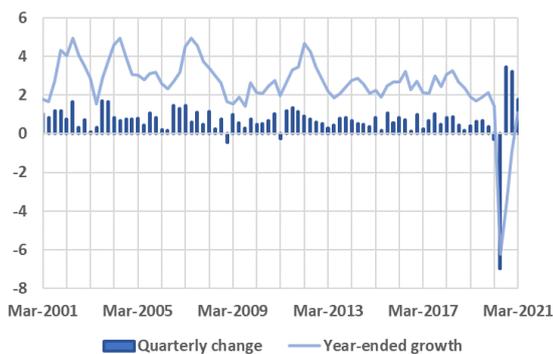
## Melbourne Institute Nowcast of Australian GDP & Dating the Business Cycle

Released June 24, 2021

### ***GDP grew by 1.8 per cent in the March quarter of 2021***

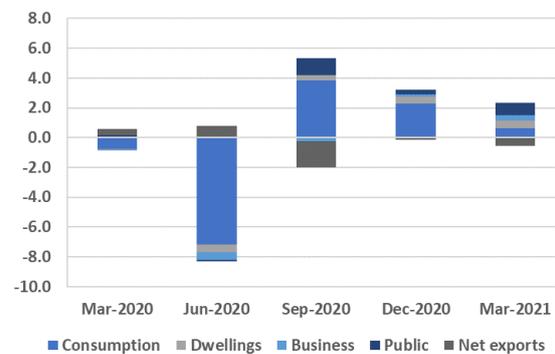
On June 2, the ABS reported that GDP grew by 1.8 per cent in the March quarter of 2021, giving an annual growth rate of 1.1 per cent and showing signs of continued recovery. According to the ABS, household consumption rebounded further, albeit moderately, in the first quarter as restrictions further eased, contributing 0.6 percentage points to GDP. Public expenditure, dwellings and business investment all contributed positively and moderately to growth, while net exports subtracted 0.6 percentage points from GDP. The next release of the National Accounts, covering the June quarter of 2021, will be on September 1.

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



Source: ABS, up to Mar quarter 2021.

**Figure 2: Contributions to GDP Growth** (ppt)



Source: ABS, up to Mar quarter 2021.

### ***First nowcast for June Quarter GDP (released in June 2021)***

The first nowcast for the June-2021 quarter projects quarterly GDP growth of 0.6 per cent, giving a year-ended growth rate of 9.4 per cent. The nowcast for Q2-2021 further confirms the return-to-normal for households and business activity, although we note the on-going uncertainty of COVID-19 on economic activity. In July 2021, the second nowcast for Q2 will be released.

Strong housing market activity was the primary positive contributor to the GDP growth nowcast for Q2-2021. Improvements in labour market conditions and commodity prices also contributed positively to the first nowcast for Q2. However, business lending are extremely weak and international economic conditions remain uncertain, both posing risks for growth in 2021/22.

### ***Subdued Activity After a Strong end to the March quarter....***

The Australian economy grew at a well-above trend pace in the March quarter. The Monthly Activity Index suggests that this was concentrated in February and March. This momentum appears to not have been maintained, which is not unexpected given the March quarter reflected recovery from the COVID recession.

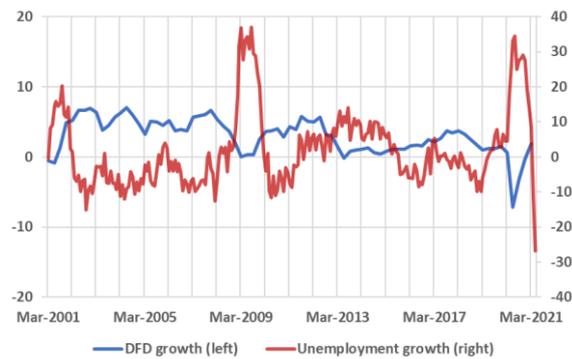
While our nowcast for the June quarter is a little below trend, the Westpac-Melbourne Institute Leading Index continues to suggest that output growth will be above trend over the next 3 to 9 months. Growth in the Leading Index has moderated recently.

### **Both hours worked and the number of unemployed improved in May<sup>1</sup>**

The number of unemployed declined by 26.8 per cent over the year to May. The noticeable improvement is partly due to the high number of unemployed recorded last May amid the pandemic and subsequent lockdown in Australia. Nevertheless, it is also slightly below the value observed in the same month in 2019 (pre-COVID). Consistently, Domestic Final Demand grew by 1.9 per cent over the year to the March quarter, showing signs of recovery from the pandemic shock.

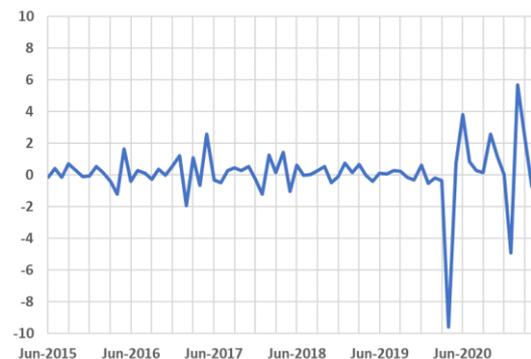
Hours worked increased by 1.4 per cent from April to May, back to its recovery trend after temporarily losing momentum last month. Moreover, hours worked have recovered from the COVID-19 shock, with their current value well above the values observed in the same month in 2020 or 2019 (pre-COVID). Overall, improved labour market conditions made a positive contribution to the first Q2 nowcast for 2021.

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



Source: ABS, up to May 2021.

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



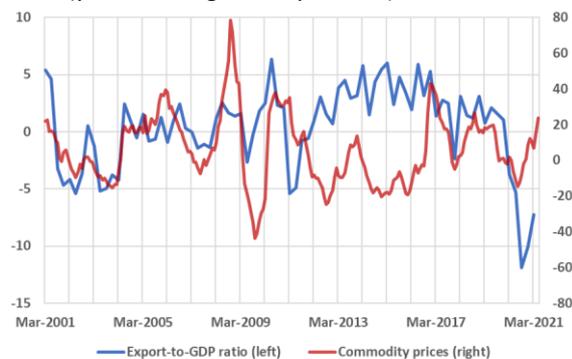
Source: ABS, up to May 2021.

### **The rising trend of commodity prices continues, while trade remains weak**

The index of commodity prices continued to rise, growing by a sizeable 24 per cent over the year to May. This is largely due to the ongoing improvement in bulk commodity prices, especially elevated iron ore prices in recent months. As expected in last month's report, the exports-to-GDP ratio picked up somewhat in the March quarter (to -7.2 per cent from -10.1 per cent in Dec-20) due to the recent improvement in commodity prices, although it is still below its historical level.

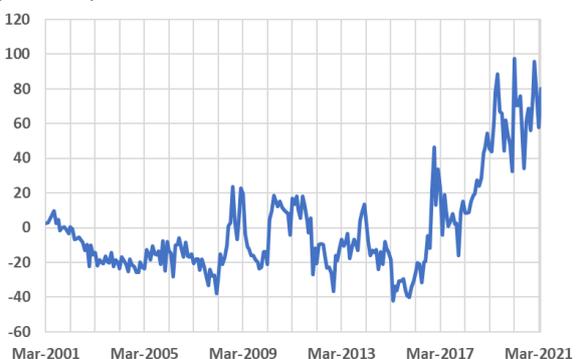
Net exports expanded in April, thanks to an increase in total exports and a decrease in total imports. Overall, the growth of commodity prices made a positive contribution to this month's nowcast but the trade sector remains weak, posing risks for growth in 2021/22.

**Figure 5: Commodity Prices and Exports-to-GDP Ratio**  
(year-ended growth, per cent)



Source: ABS, up to May 2021.

**Figure 6: Trade balance**  
(\$ billion)



Source: ABS, up to Apr 2021.

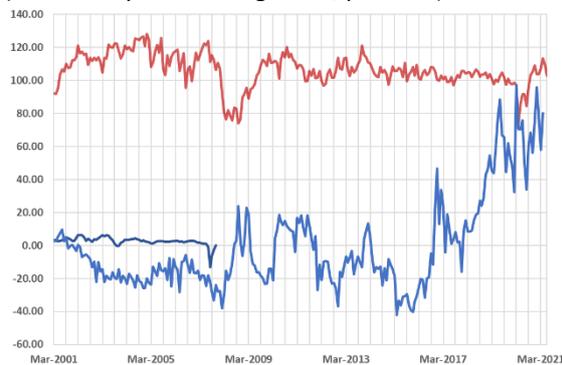
<sup>1</sup> Our nowcast model uses monthly information regarding labour market conditions, housing and business lending, retail sales, housing approvals, consumer expectations, trade conditions and commodity prices to gauge current economic conditions. **We note that the nowcast is currently in the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

## Consumer sentiment fell in June

The seasonally adjusted current conditions component of consumer sentiment fell by 6.7 points in June, after falling again by 3.7 points in May. The declines eliminate the gains in sentiment observed in March and April. Although the Current Conditions Index has exceeded 100 for a ninth consecutive month, the index is now only slightly above the neutral point of 100, indicating that the number of optimists only marginally exceeds the number of pessimists.

The latest retail trade data shows that both food and non-food related retail spending increased in April, following sharp declines in March. We note that last month's fall was largely expected given the COVID-related spike observed in March 2020. Annual growth in non-food related retail trade is now a relatively 'normal' 4.5 per cent, whereas growth in household-related retail trade is still elevated at 11 per cent. Overall, however, the data show a normalisation of retail trade growth.

**Figure 7: Consumer Sentiment and Consumption**  
(index and year-ended growth, per cent)



Source: ABS and Melbourne Institute, up to Jun 2021.

**Figure 8: Retail trade**  
(year-ended growth, per cent)



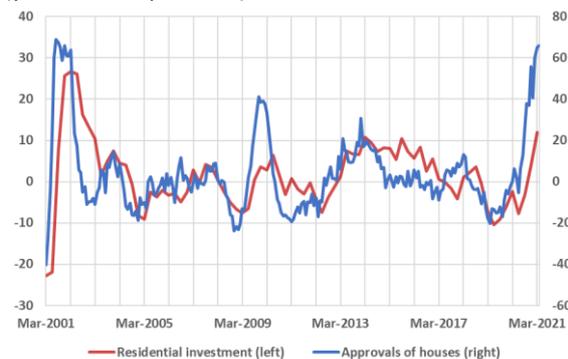
Source: ABS, up to Apr 2021.

## The housing market continues its strong run

Dwelling approvals continued to surge in April, with its rate of annual growth rising from 62 per cent in March to 66 per cent. Monthly building approvals in April also breached last month's record of over 14,500 to reach over 15,000 in April. As in previous months. Housing activity is a major positive factor in the nowcast for Q2.

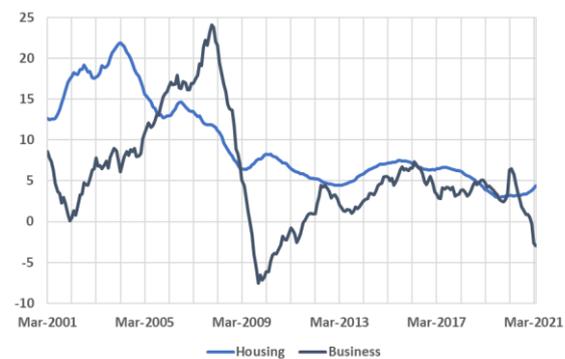
Consistent with record dwelling approvals, annual growth in housing credit rose to 4.4 per cent in April from 4.1 per cent in the previous month. Housing credit growth is now at its highest since January 2019. Business lending growth, however, continues to be extremely weak, with annual growth falling from -2.7 per cent in March to -3.0 per cent in April. Business lending growth is now at its lowest point since 2011.

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



Source: ABS, up to Apr 2021.

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



Source: ABS, up to Apr 2021.

## Dating the Australian Business Cycle

The Melbourne Institute uses a Monthly Activity Index, together with the nowcast and a rule to identify turning points, to date whether the Australian economy may be in a recession.<sup>2</sup>

The Monthly Activity Index is constructed so that at the quarterly frequency, it coincides with the log of real quarterly GDP to ensure that both data set exhibits similar turning points. Essentially our approach interpolates the quarterly values in history, guided by monthly partial indicators of the state of the economy.<sup>3</sup> Table 1 identifies the turning points (as in peaks and troughs) and the periods of contractions and expansions in business cycle analysis using monthly data.

Business cycles based on quarterly ABS GDP data are shown in Table 2. A better measure of the living standards of Australians is GDP per capita. Expansions and contractions in GDP per capita are shown in Table 3. With the addition of the March quarter data and the revisions to history there have been changes to the GDP per capita based cycle dates. GDP per capita is currently in an expansionary phase; in the March quarter it was around 8.5 per cent higher than at its trough last year.

**Table 1: Monthly Business Cycle Dates**

Peak	Trough	Contraction	Expansion	Cycle	
		peak to trough (months)	trough to peak (months)	peak to peak (months)	trough to trough (months)
Sep-1981	Jan-1975	20	80	102	100
Mar-1990	May-1983		82		97
Mar-2020	Jun-1991		345		347
	May-2020		<i>Ongoing</i>		
<b>Averages</b>		<b>10</b>	<b>130</b>	<b>231</b>	<b>181</b>
<b>Standard deviations</b>		<b>9</b>	<b>147</b>	<b>182</b>	<b>143</b>

Note: The average durations are rounded to full months. Includes the ongoing phase. Sample is 1974:09- 2021:06.

<sup>2</sup> The rule is known as Bry-Boschan Quarterly (BBQ). See A. R. Pagan and D. Harding (2002) 'Dissecting the cycle: a methodological investigation', *Journal of Monetary Economics*, 49(2), p. 365-381. Also see <http://www.ncer.edu.au/data/data.jsp>. The commonly quoted "two-quarters of negative growth" rule to define a recession is an approximate way of identifying turning points in the level of economic activity.

<sup>3</sup> The data used are: the Westpac-Melbourne Institute Consumer Sentiment Index (time to buy a major household item and family finances versus a year ago); retail trade; the trimmed-mean CPI; the Melbourne Institute Inflation Gauge; monthly imports; the real and nominal trade-weighted exchange rate and aggregate hours worked. We construct the Monthly Activity Index from 1974:09 onwards due to availability of the monthly data. The MI Monthly Activity Index is currently still in development (particularly its open economy aspects).

**Table 2: Real GDP Business Cycle Dates**

Peak	Trough	Contraction	Expansion	Cycle	
		Peak to trough (quarters)	Trough to peak (quarters)	Peak to peak (quarters)	Trough to trough (quarters)
Mar-1961	Sep-1961	2			
Jun-1965	Mar-1966	3	15	17	18
Sep-1971	Mar-1972	2	22	25	24
Jun-1975	Dec-1975	2	13	15	15
Jun-1977	Dec-1977	2	6	8	8
Sep-1981	Jun-1983	7	15	17	22
Jun-1990	Jun-1991	4	28	35	32
Dec-2019	Jun-2020	2	114	118	116
			ongoing		
<b>Average durations</b>		<b>3</b>	<b>25</b>	<b>30</b>	<b>34</b>
<b>Standard deviations</b>		<b>2</b>	<b>34</b>	<b>37</b>	<b>37</b>

Note: The average durations and standard deviations are rounded to full quarter. Includes the ongoing phase. Sample is 1959:Q3 – 2021:Q1.

**Table 3: Cycles in Real GDP per Capita**

Peak	Trough	Contraction	Expansion	Cycle	
		Peak to trough (quarters)	Trough to peak (quarters)	Peak to peak (quarters)	Trough to trough (quarters)
	Jun-1974				
Jun-1975	Dec-1975	2	4		6
Jun-1977	Dec-1977	2	6	8	8
Sep-1981	Jun-1983	7	15	17	22
Sep-1985	Sep-1986	4	9	16	13
Dec-1987	Jun-1988	2	5	9	7
Sep-1989	Dec-1991	9	5	7	14
Jun-2000	Dec-2000	2	34	43	36
Dec-2005	Jun-2006	2	20	22	22
Mar-2008	Dec-2008	3	7	9	10
Sep-2019	Jun-2020	3	43	46	46
			ongoing		
<b>Average durations</b>		<b>4</b>	<b>14</b>	<b>18</b>	<b>17</b>
<b>Standard deviations</b>		<b>2</b>	<b>13</b>	<b>15</b>	<b>13</b>

Note: The average durations and standard deviations are rounded to full quarter. Includes the ongoing phase. Sample is 1973:Q3 – 2021:Q1.

## Melbourne Institute Nowcast of Australian GDP & Dating the Business Cycle

The Melbourne Institute Nowcast of Australian GDP and the Monthly Index 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 and the dating methodology are currently in the experimental stage.**

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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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