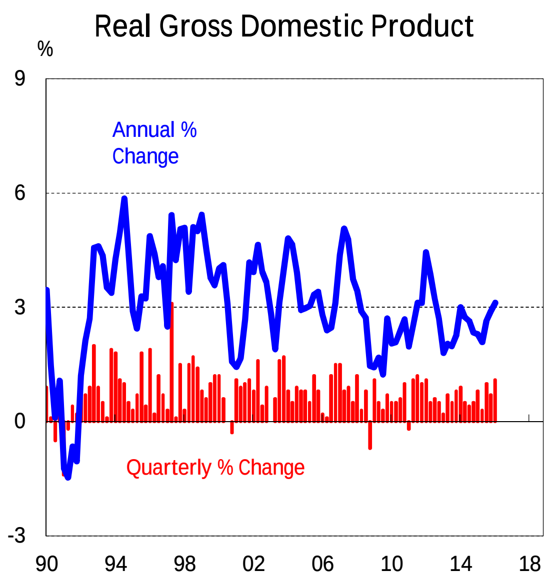
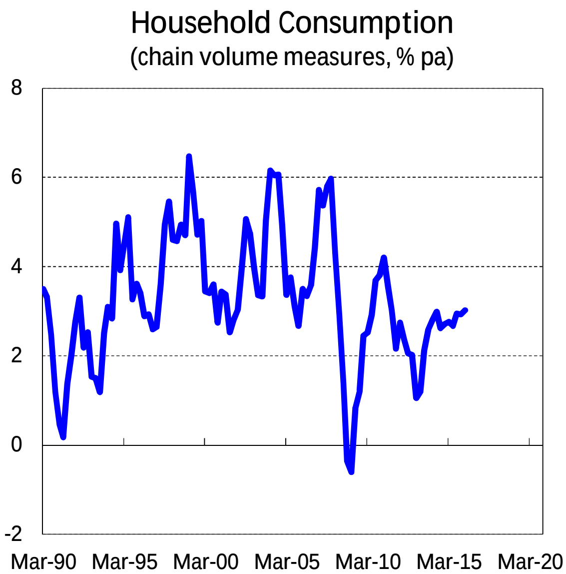
National Accounts - GDP

“Above Trend”Economic Growth?

- GDP growth was stronger than expected, rising by 1.1% in the March quarter. This followed an increase of 0.7% in the December quarter. It was the largest two-quarter increase since the March quarter 2012.
- For the year to the March quarter, GDP rose to 3.1%. This followed downwardly revised growth of 2.9% in the year to the December quarter. Today’s data indicates the economy grew at an above trend pace over the March quarter.
- Economic growth in the March quarter was driven by strong net exports, although household spending, government spending and dwelling investment all contributed to the solid pace of growth.
- The drag on mining investment has continued to weigh on State final demand in resource States. Final demand contracted in Western Australia and the Northern Territory and was flat in Queensland South Australia. The transition to non-mining sectors of the economy however, remains uneven as reflected in weak State final demand in other States. Final demand in Victoria and Tasmania was subdued. NSW and the ACT were the only States or territories to post solid demand growth for the quarter.
- Despite the release of strong economic growth figures today, the domestic economy still faces challenges including weak income growth and subdued domestic demand.





GDP grew 1.1% in the March quarter, which was above our own forecasts (0.9%) and consensus forecasts (0.8%). In addition, GDP growth from the December quarter last year was revised slightly higher, to a 0.7% increase. It was the largest two-quarter increase since the March quarter 2012.

The annual pace of growth pick up from a revised 2.9% in the year to the December quarter (previously reported as a 3.0% increase) to 3.1% for the year to the March quarter. This is an above-trend pace of economic growth and was the strongest annual pace since September 2012. The Australian economy completed its 24th consecutive year of uninterrupted gains in annual GDP growth in the March quarter.

There were some promising signs in today's data. Net exports made a significant contribution to economic growth in the quarter. Domestic economic growth (or domestic final demand) benefited from growth in household and government spending and dwelling investment. Business investment remains an ongoing source of weakness as the resource investment boom continues to unwind. Overall, the economy still faces challenges in its transition to growth driven by the non-mining sector. However, today's data provided an encouraging sign that non-mining sectors are picking up some of the slack.

GDP Expenditure Measure:

While the detail behind the GDP data was less positive than the headline number, it reveals some underlying grit in the domestic economy.

Exports have been a major driver behind the recent volatility in quarterly economic growth and the March quarter was no exception, with net exports the major contributor to growth. Net exports contributed 1.2 percentage points to GDP growth in the March quarter. This follows no contribution in the December quarter last year, a 1.5 percentage point contribution in the September quarter last year and a 0.8 percentage point detraction in the June quarter last year. Exports jumped 4.4% while imports fell 0.8% in the March quarter. The increase in resource production capacity following the resource investment boom is enabling strong growth in resource exports.

The flip side of this is the ongoing reversal in resource investment, as the economy continues to unwind from the mining investment boom. Business investment fell 4.2% in the March quarter, the eighth consecutive quarterly decline. For the year to the March quarter, business investment fell 13.0%, the largest annual decline since the December quarter 2000. Business investment detracted 0.6 percentage points from GDP growth in the March quarter.

The weakness in business investment is weighing on domestic demand. Domestic demand eked out a 0.1% gain, following a 0.5% rise in the December quarter last year. For the year to the March quarter domestic demand increased 0.9%, down from 1.1% annual growth in the previous three quarters.

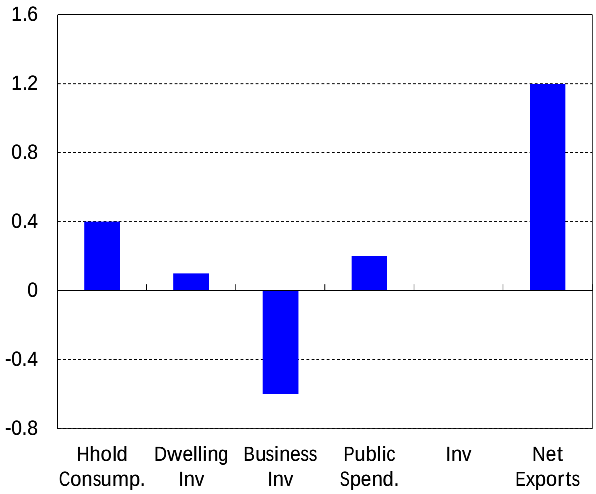
Household consumption rose 0.7% in the March quarter, after rising 0.8% in the December quarter. Low interest rates are supporting consumption and the rate cut delivered by the RBA in May will continue to support economic growth in the current quarter. Additionally, employment gains over the past year may have improved job security for those employed and employment prospects for those looking for work. This has given households the impetus to spend, despite very low wages growth.

Dwelling investment, which has been a key driver of growth, rose 1.4% in the March quarter, following an increase of 2.8% in the December quarter. Solid growth in building approvals in recent months suggests growth in housing construction will continue, although the momentum provided to economic growth over the past year is likely to slow. Low interest rates have supported the housing market and the RBA's rate cut in May will provide further support.

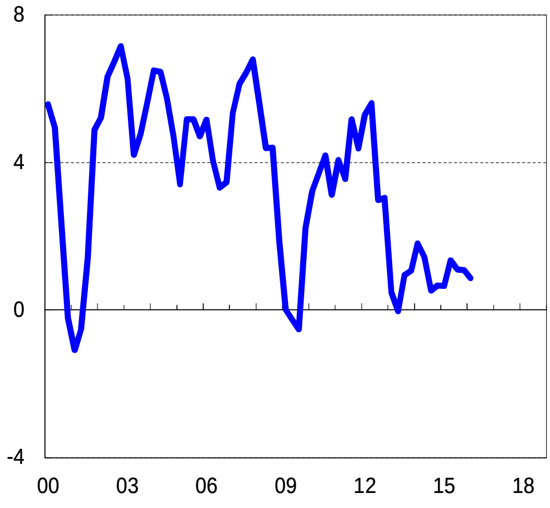
Government expenditure supported economic growth in the quarter. Government investment rose 0.7% in the March quarter, while Government consumption spending lifted 0.9% for the quarter.

Selected Expenditure Items on GDP, Chain Volume Measures	
	Quarterly % Change
Household Consumption	0.7
Public Consumption	0.9
Dwelling Investment	1.4
Business Investment	-4.2
Public Investment	0.7
	Contribution to GDP ppt
Inventories	0.0
Net Exports	1.2

GDP Contributions to Growth
(March quarter 2016, percentage points)



Domestic Final Demand
(Annual % Change)



GDP Income Measure:

Despite the broad strength in the headline growth rate, GDP growth based on incomes was relatively soft in the March quarter. Incomes in nominal terms (or unadjusted for inflation) grew just 0.5%. Over the year, the income component of GDP grew just 2.1%, unchanged from the December quarter 2015.

This measure largely comprises wages and profits, which have been hit by soft wage growth and falling commodity prices.

- Gross Operating Surplus

Profits (gross operating surplus) for private non-financial corporations fell 2.9% in the March quarter, largely reflecting the squeeze on mining profits in the quarter. Profits for all sectors declined 0.9% in the quarter, while the annual pace contracted 0.6%, the weakest in three quarters.

A recent stabilising in commodity prices should help limit further declines in mining profits in the near-term especially given production capacity is continuing to increase. A lower Australian dollar should continue to provide support to company profits across all sectors. Moreover, businesses continue to report above-average conditions in surveys.

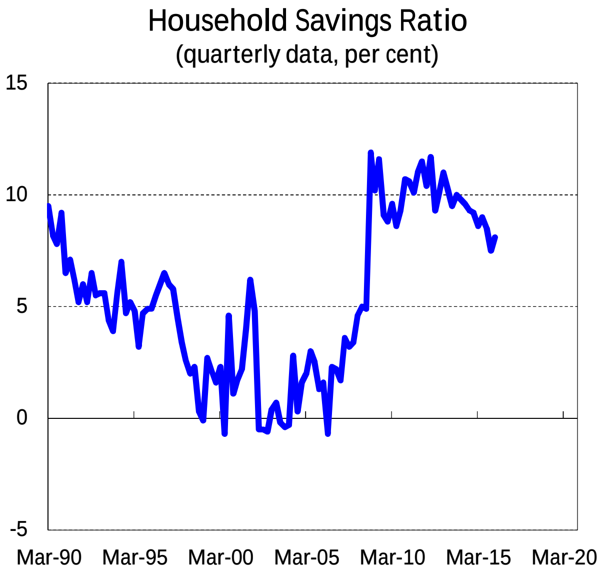
- Wages

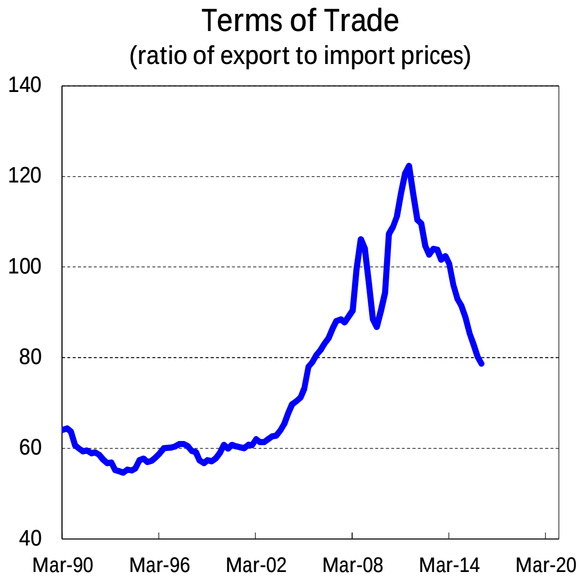
Wages (including employer's social contributions) grew 0.8% in the March quarter, which was a touch stronger than implied by other data.

The annual pace of growth lifted from 2.9% in the December quarter to 3.6% in the March quarter. This was the strongest in over three years, although well below the long-run average. We will wait to see whether this trend continues over the coming year as wage data in the national accounts tends to be volatile quarter to quarter.

It is possible that the healthy job gains over the past year may be behind the pickup. While wage growth for individuals remains subdued, in aggregate, income growth could be relatively stronger because more Australians would now be employed.

Household disposable income, which includes non-wage income, was also relatively firm with growth of 1.2% in the March quarter. This saw the annual pace of growth edge up from 3.0% to 3.8% in the March quarter.





- Household Saving Ratio

The pickup in household incomes and slightly slower growth in household spending has led to a lift in the household savings ratio from 7.5% in the December quarter to 8.1% in the March quarter.

The pickup in incomes raises the prospect that household spending will continue to grow at a healthy pace, although a pullback in consumer confidence is not an encouraging sign for the outlook.

The household savings ratio however, remains above the long-run average.

- Terms of Trade

The terms of trade (ratio of export to import prices) declined 1.9% in the March quarter, the ninth consecutive quarter of decline. The terms of trade is now 2.3% lower than its 20-year average. The good news is that the stabilisation of commodity prices in recent months suggests that there will be less pressure on incomes in coming months.

Industry Break Down:

Industry Gross Value Added, Chain Volume Measures

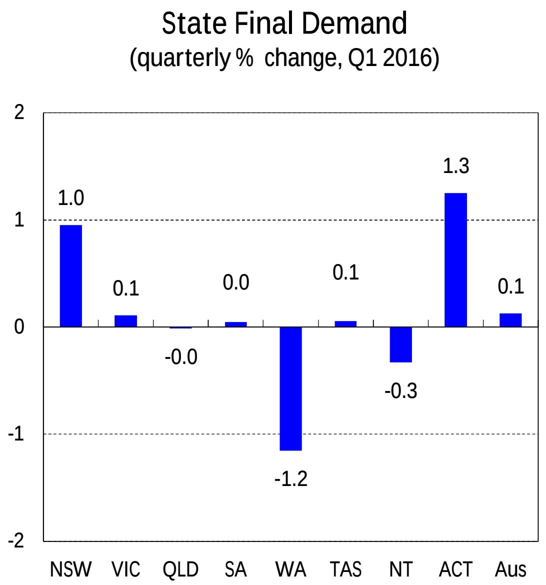
By Industry Sector	Quarterly % Change	Annual % Change
Public Admin & safety	5.9	10.4
Accommodation & food services	1.9	0.6
Financial & insurance services	1.7	5.0
Professional, scientific & technical services	1.5	-1.7
Agriculture, forestry & Fishing	1.3	1.8
Mining	1.1	10.7
Wholesale Trade	1.0	2.0
Retail Trade	0.8	3.5
Education & training	0.7	2.7
Arts & recreation services	0.6	5.1
Construction	0.5	3.5
Manufacturing	0.5	-2.4
Information media & telecommunications	0.0	5.5
Healthcare	-0.1	3.6
Transport,postal & warehousing	-0.2	0.5
Electricity gas, water & waste services	-0.7	2.0
Administrative & support services	-1.6	-3.0
Rental, hiring & real estate services	-2.4	7.8
Other services	-3.2	-1.9

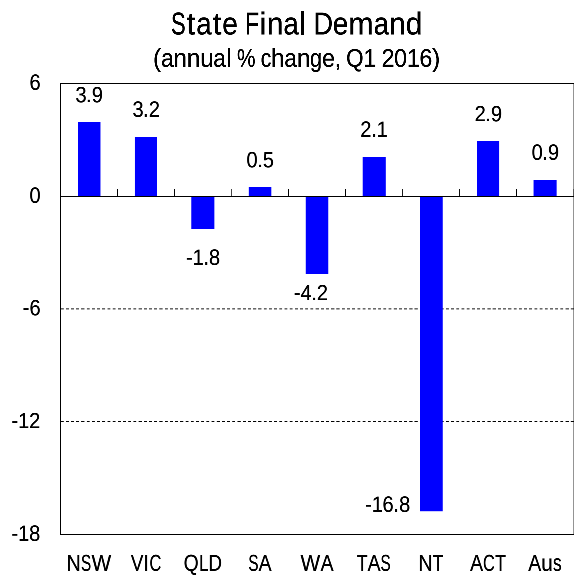
State Final Demand:

The drag on mining investment has continued to weigh on State final demand in resource States.

Final demand contracted a further 1.2% in Western Australia in the March quarter, the third consecutive quarter of decline. Demand also contracted 0.3% in the Northern Territory and was flat in Queensland and South Australia. The transition to non-mining sectors of the economy however, remains uneven as reflected in weak State final demand in other States. Final demand in Victoria (0.1%), and Tasmania (0.1%) was subdued. NSW (1.0%) and the ACT (1.3%) were the only States or territories to post solid demand growth for the quarter.

On an annual basis, final demand was strongest in NSW (3.9%), followed by Victoria (3.2%), which are benefiting significantly from low interest rates and the fall in the Australian dollar in recent years. Final demand in the ACT (2.9%) and Tasmania (2.1%) grew at a moderate pace in quarter but remained subdued in South Australia (0.5%). Western Australia (-4.2%), Queensland (-1.8%) and the Northern Territory (-16.8%) saw declines in State final demand in the year to the March quarter.





Outlook

Economic growth has been stronger than expected in recent quarters. Net exports have been a strong driver of growth. Most other parts of the domestic economy have been mixed and were brought down by continued weakness in business investment. The headline numbers were stronger than the detail and the economy continues to face challenges in making the transition to non-mining led growth. Domestic demand remains weak which provides some uncertainty for the labour market outlook. Moreover, income growth remains subdued.

Low interest rates and the low Australian dollar are supporting the economy. The rate cut from the RBA in May will further support economic growth this year. Low inflation was a key factor in the RBA's decision to cut interest rates in May. Although economic growth is above trend, the economy still faces challenges. Combined with the low inflation outlook, another rate cut from the RBA cannot be ruled out.

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The Detail