Data Snapshot

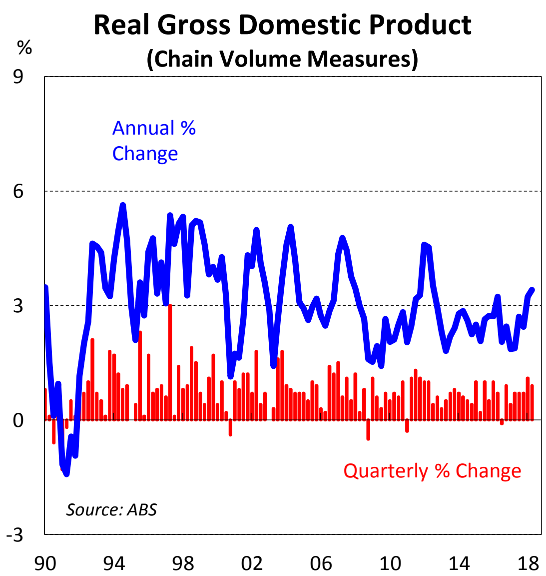
Wednesday, 5 September 2018

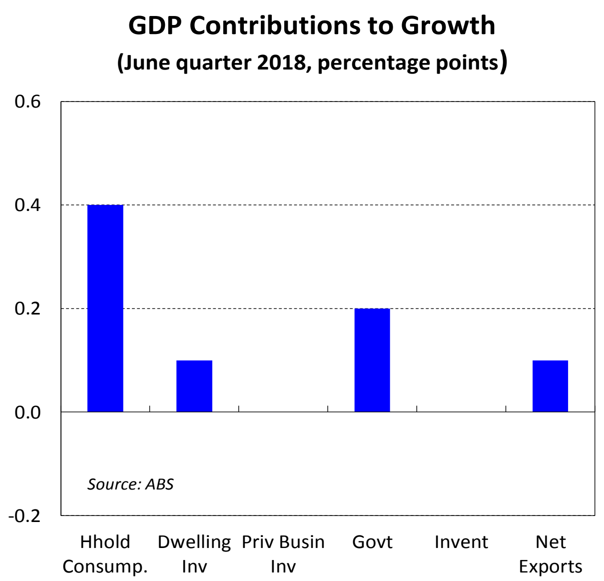
Bank of Melbourne

National Accounts - GDP

All Fired Up

- **Gross domestic product (GDP) rose by a larger than expected 0.9% in the June quarter. Annual growth stepped up from 3.2% to 3.4%. It is the fastest annual rate of growth in five-and-a-half years and is above the 20-year average of 3.1%.**
- **GDP growth in the quarter was broad-based and was led by household and government spending. Together, these categories contributed 0.6 percentage points to GDP growth.**
- **Household consumption was solid despite high levels of household debt and slow wages growth. A decline in the household savings ratio indicated consumers continued to dip into their savings buffer to fund spending. Households are unlikely to be able to sustain this over the longer-term suggesting households will struggle to maintain its current pace of spending growth.**
- **The economy has grown at a robust pace over the first half of 2018, and above most estimates of potential growth. In light of today's data we now have greater confidence that economic growth over 2018 will sit above 3%. We continue to expect that the economy will grow at a pace which will be at or close to the potential rate of growth over the medium-term. That said, there are downside risks to the RBA's expectation for growth to average 3.25% in 2019.**





GDP Expenditure Measure:

Gross domestic product (GDP) rose by a larger than expected 0.9% in the June quarter. This followed upwardly revised growth of 1.1% in the March quarter, previously reported as an increase of 1.0%.

Annual growth stepped up from 3.2% to 3.4%. It is the fastest annual rate of growth in five-and-a-half years and is above the 20-year average of 3.1%.

GDP growth in the quarter was broad-based and was led by household and government spending. Together, these categories contributed 0.6 percentage points to GDP growth. Additionally, dwelling investment and net exports contributed to GDP growth in the quarter. Business investment detracted from growth.

Private business investment was disappointing, falling 0.7% in the June quarter, following growth of 2.0% in the March quarter. The weakness was driven by non-mining investment, which fell 2.4% in the June quarter, with weakness in machinery and equipment, following strong growth in the previous quarter. Mining investment, on the other hand, jumped 5.1% in the June quarter, its first increase in over a year. This reflected an increase in petroleum exploration which was not captured in last week's capex data.

The weakness in non-mining investment comes amid increased uncertainty about the outlook for non-mining investment. There had been hopes non-mining investment would increase at a time when growth in other sectors of the economy, including dwelling investment and household spending, were likely to wane. The most recent capex intentions survey cast doubts on this story, with businesses' intentions suggesting non-mining investment spending would flat line this financial year.

Selected Expenditure Items on GDP, Chain Volume Measures

	Quarterly % Change
Household Consumption	0.7
Public Consumption	1.0
Dwelling Investment	1.7
Business Investment	-0.7
Public Investment	0.0
	Contribution to GDP ppt
Inventories	0.0
Net Exports	0.1

Household consumption growth was solid in the June quarter, rising by 0.7% and adding 0.4 percentage points to growth in the quarter. Annual growth eased to 3.0%, from 3.2% in Q1.

Spending on clothing & footwear (1.6%), alcoholic beverages (1.6%) and communications (1.6%) were the strongest categories in the June quarter. Spending on vehicle purchases (-1.8%) and cigarettes & tobacco (-1.1%) were the weakest categories.

Household consumption was solid despite high levels of household debt and slow wages growth. A decline in the household savings ratio indicated consumers continued to dip into their savings buffer to fund spending. Households are unlikely to be able to sustain this over the longer-term suggesting households will struggle to maintain spending growth at this pace.

The **housing cycle** is turning down, as illustrated by auction rates, loan volumes and dwelling approvals. While the downturn is expected to negatively impact dwelling investment and economic growth over the next 18 months, this was not evident in the June quarter. Dwelling investment rose 1.7% in the June quarter, comprising a 3.6% rise in new dwelling investment and a fall in alterations and additions. Dwelling investment added 0.1 percentage points to growth in the quarter.

The **government sector** overall contributed 0.2 percentage points to GDP growth in the June quarter. Government consumption rose by 1.0% in the June quarter. Government investment was unchanged for the quarter.

Inventories were little changed for the June quarter and made no contribution to GDP growth.

Exports are trending higher, as new capacity in the resources sector comes on stream and as firmer global growth leads to greater demand for Australian exports. Export volumes lifted 1.1% and import volumes by 0.4%, so net exports added 0.1 percentage points to growth.

GDP Income Measure:

Nominal GDP rose 1.0% in the June quarter, a more modest pace after a 2.4% increase in the March quarter. A fall in the terms of trade (-1.3%) weighed on incomes in the quarter.

Wage incomes (total compensation of employees) rose 0.7% in the quarter, a modest increase given the strength of recent employment gains. The slow pace of wage growth is continuing to keep a lid on incomes. On an annual basis, growth in wage incomes remained firm, but stepped down from 5.1% in the March quarter to 4.8% in the June quarter.

Company profits also grew moderately, lifting 0.8% in the June quarter for annual growth of 7.2%. Above-average business conditions continued to support company profits.

When excluding the impact of prices, GDP based on incomes rose a solid 0.9% in the June quarter.

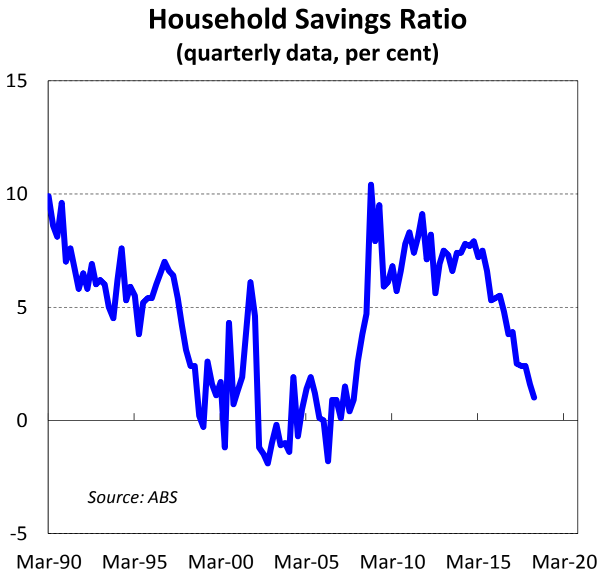
- **Household Savings Ratio**

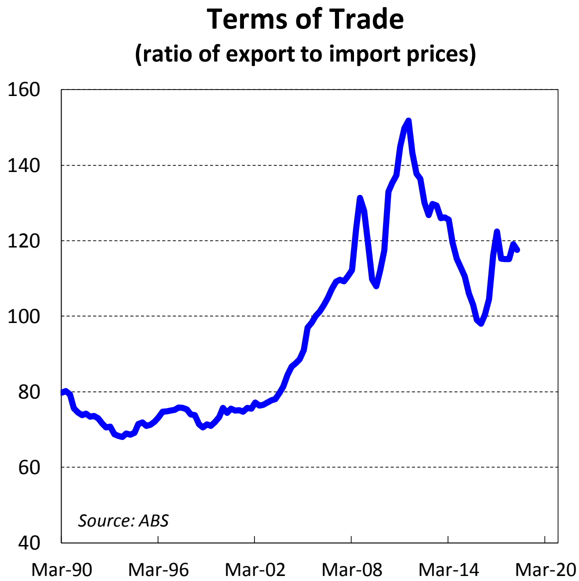
With incomes growing below the pace of consumer spending, the household savings ratio fell to 1.0% in the June quarter, the lowest in 10½ years. It suggests that there remains an uncertain outlook for consumer spending, particularly given that household debt is at high levels. Growth in household spending will be increasingly limited by the pace of income growth. The strength of the labour market should continue to provide support to incomes, but it will likely be a while before we expect to see stronger growth in wages.

- **Terms of Trade**

The terms of trade (ratio of export to import prices) fell 1.3% in the June quarter, the first drop in three quarters. Higher commodity prices drove up export prices, but a much larger increase in oil prices boosted import prices to a greater extent.

On a year ago, the terms of trade was 2.1% higher.





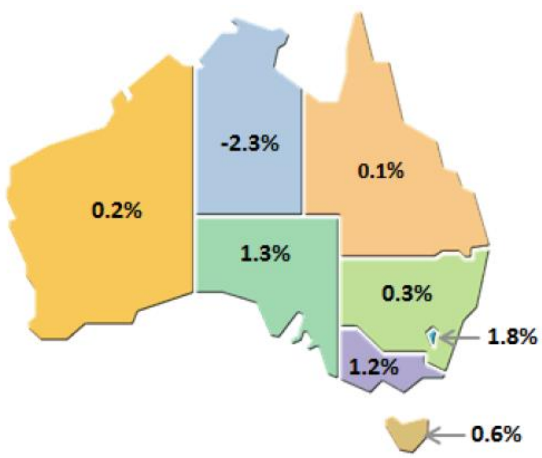
State Final Demand:

Economic activity by State and territory is provided by Gross State Product (GSP). GSP is the closest measure to GDP. However, GSP is only published annually. State final demand is published more frequently (i.e. quarterly), but it excludes the trade sector.

In the June quarter, State final demand grew across all States and territories, with the exception of the Northern Territory. There was strong growth in the ACT (1.8%), South Australia (1.3%) and Victoria (1.2%). Final demand was modest in Tasmania (0.6%), and subdued in NSW (0.3%), Western Australia (0.2%) and Queensland (0.1%). The Northern Territory (-2.3%) is still being impacted as LNG-related construction wraps up.

On an annual basis, growth was strongest in the ACT (5.8%) and Victoria (5.2%). However, South Australia (3.7%), Tasmania (3.7%), NSW (3.5%) and Queensland (3.4%) also had firm growth. Annual growth in State final demand remained subdued in Western Australia (0.8%) and in contraction in the Northern Territory (-8.2%)

State Final Demand
(Quarterly % Change, June Quarter 2018)



Source: ABS

Industry Break Down:

Out of the 19 industries, all but two industries recorded growth in the June quarter.

The strongest performing industry in the quarter was other services (2.2%), but there was also solid growth in professional, scientific & technical services (1.9%) and construction (1.9%).

Annual growth was strongest in other services which grew 7.3% in the year to the June quarter. This includes personal care services, repairs and maintenance services, among other services.

Industry Gross Value Added, Chain Volume Measures

By Industry Sector	Quarterly % Change	Annual % Change
Other services	2.2	7.3
Professional, scientific & technical services	1.9	4.5
Construction	1.9	5.5
Info, media & telco	1.8	2.3
Rental, hiring & real estate services	1.7	1.0
Mining	1.5	5.1
Healthcare & social assistance	1.3	7.2
Electricity, gas, water & waste services	1.2	3.1
Accommodation & food services	1.2	2.1
Arts & recreation services	1.2	5.5
Retail Trade	1.1	2.3
Agriculture, Forestry & Fishing	0.8	-8.8
Financial & insurance services	0.7	2.7
Public admin & safety	0.6	4.1
Education & training	0.6	2.2
Administrative & support services	0.5	4.2
Transport, postal & warehousing	0.4	1.3
Wholesale Trade	-0.2	0.8
Manufacturing	-1.5	1.9

Outlook

The economy has grown at a robust pace over the first half of 2018, and above most estimates of potential growth. After today's data we now have greater confidence that economic growth over 2018 will sit above 3%.

However, there are signs that this momentum will not be sustained. It is unlikely consumer spending will continue to grow at its recent pace, particularly given income growth is not expected to pick up significantly and household debt levels remain high. The downturn in the housing market poses another downside risk to consumer spending. Additionally, dwelling investment will undergo a more pronounced downturn at some point.

Another downside risk comes from the global economy and the impact of trade tensions on business sentiment. The outlook for non-mining investment, which has been a key support for growth in recent times, is less bright now than it has been over the past year.

Nonetheless, the strong pipeline of public infrastructure spending should continue to boost economic growth, and the drag from the downturn in mining investment will dissipate further.

We continue to expect that the economy will grow at a pace which will be at or close to the potential rate of growth over the medium-term. That said, there are downside risks to the RBA's expectation of growth 3.25% for 2019.

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