

Australia Watch

GDP review: Soft growth and softer prices

GDP rises by 0.2%, annual growth is down to 1.5%

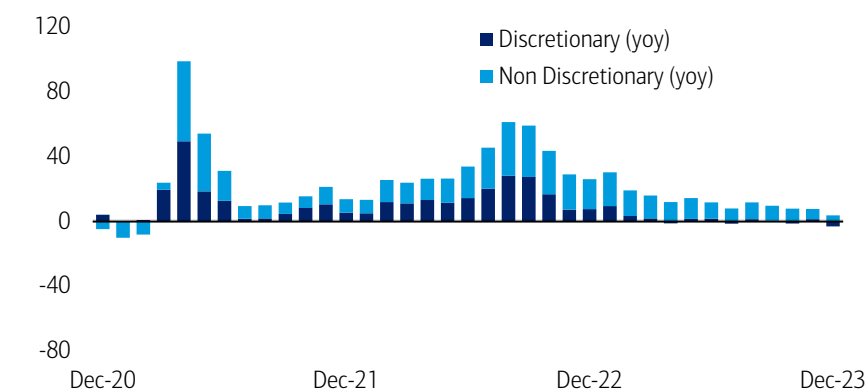
The soft GDP outcomes were no surprise to us, consensus, and the Reserve Bank of Australia (RBA). However, the composition of growth reflects traction from high rates and high living costs continues to weigh on the consumer and the overall economic momentum. Government spending and private sector investment were the key drivers of growth in the quarter while household spending remained subdued at 0.1%qoq, following zero growth in 3Q. Growth remains well below trend.

More constraints in the household sector, but softer prices

Households increased spending on essential items like electricity, rent, food and health while discretionary spending in hotels, cafes and restaurants softened. Notably, following eight quarters of falls, the household saving to income ratio rose to 3.2%, with income received by households outpacing their income paid as tax returns flow into households' accounts and real wages growth turns [slightly positive](#) (see report).

Exhibit 1: Consumers spend on non-discretionary

Non-essential spending weakens further



Source: ABS

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Price measures slow, focus shifts to unemployment

Consistent with softer inflation of late (see: [monthly CPI review](#)), the implicit price deflator of domestic demand experienced the softest rise since Dec 2021. Weak growth over the last six month along with encouraging signs that inflation continues to move back into target will place the RBA's focus on near-term labour market outcomes.

Softer employment growth and rising unemployment would likely test our view for 75bps of cuts from February 2025. [As previously discussed](#) (see report), a sustained rise in unemployment along with weak household spending could trigger modest but earlier easing than we currently expect. Should the current trends continue, we see risk for easing in 2H 2024.

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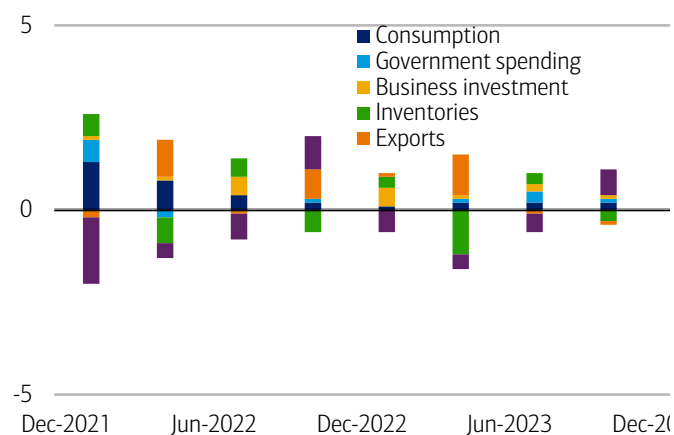
Soft data at odds with RBA guidance

Growth was soft as expected. Yet both public and private business spending contributed to growth in the quarter. Public consumption expenditure was up 0.6% in the quarter while public investment rose 0.2%. Private business investment was up 0.7% driven by non-dwelling construction. Investment on non-dwelling building construction in the private sector rose 5%. Meanwhile, new machinery and equipment detracted from growth, falling for the first time since September 2022 due to lower levels of spending on agricultural equipment.

The external sector contributed 0.6% to GDP growth this quarter as imports fell 3.4%. Goods imports fell 2.8% with consumption, capital and intermediate goods all experiencing falls. Services imports fell 5.3% driven by travel services as Australians spent less on overseas travel. Exports fell 0.3%, primarily from a 0.4% fall in goods exports that were partly offset by rises in coal (3.9%) and mineral ores 0.5% exports. Services exports rose 0.5% driven by an increase in travel services 1.2% as visitors continued to return to Australia (Exhibit 2).

Exhibit 2: Soft and narrow-based growth

Consumers remain very soft

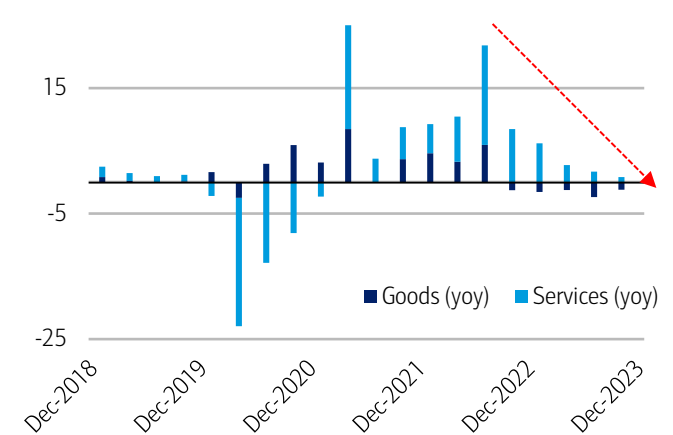


Source: ABS, Macrobond

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Exhibit 3: No more resilient services spending

Consumers continue to struggle



Source: ABS

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Household spending rose 0.1% in the December quarter with increases across all essential categories. Yet, services spending remained positive but has weakened sharply, suggesting little resilience left in the household sector (Exhibit 3). Indeed, production in industries supplying essential goods and services rose including in health care and social assistance (0.5%) and electricity, gas, water and waste services (0.9%). Following eight quarters of declines, the household saving to income ratio rose to 3.2% with income received by households outpacing their income paid.

Price measures and labour costs seem to have peaked

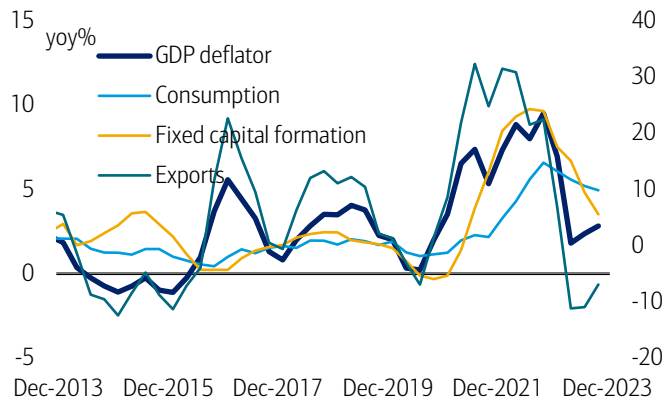
The domestic final demand deflator (+1.0%) experienced its softest rise since December quarter 2021. Prices for household consumption increased 0.8%, driven by prices for services which grew by 1.3%. Prices for goods declined for the first quarter since the September quarter 2021 COVID lockdowns as supply chains improved (Exhibit 4). The latter is consistent with recent CPI outcomes and suggests price pressures continue to ease. Nominal GDP rose 1.4%.

The RBA will focus on measures of wages and compensations to employees as well as unit labour costs. While these remain elevated, both indicators suggest pressures have peaked (Exhibit 5). We expect the cash rate to remain on hold in March as data has been

largely in line with the RBA's assumptions. However, guidance will likely continue to shift to a less hawkish stance given the overall weakness in economic momentum and clear signs that inflation is easing. While we see rates on hold until February 2025, risk is for cuts in 2H 2024 if this trend in the data continues. We will watch labour market data for a confirmation that spare capacity is increasing before revisiting this call.

Exhibit 4: Deflators show inflation is slowing

Consistent with CPI

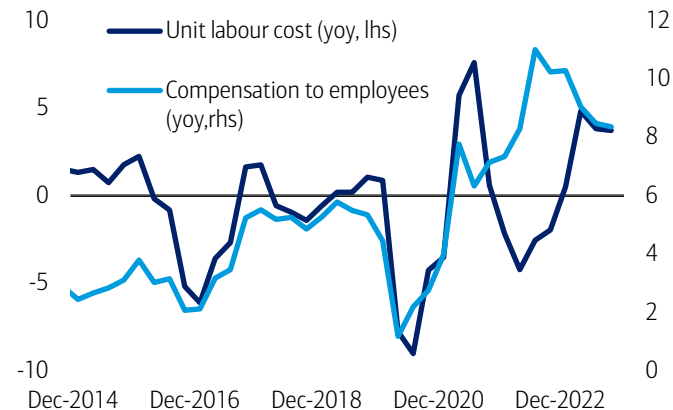


Source: ABS

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Exhibit 5: Measures of wages seem to have peaked

But remain elevated



Source: ABS

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