

Economics Weekly

This week's economic highlights

- The RBA released its **latest monetary policy decision**, lifting interest rates for the fifth time since November 2010 to 2.35 basis points.
- **Real GDP** increased by 0.9% quarter-on-quarter and 3.6% year-on-year. This indicates **the strong performance of the economy continued** in the June quarter after a return to more normal growth levels in the last quarter.
- 15 of Australia's 19 **major industries** grew in Q2 of 2022, as did all **states and territories** except the Northern Territory.
- Both the **Australian PCI**[®] and **Australian PSI**[®] rose modestly in August. However, the construction sector reflected weak conditions while the services sector indicated mild growth. Cost pressures remain elevated.
- Lower iron ore, gold, coal and LNG exports contributed to a **weaker trade surplus** in July. Import volumes rose modestly in July 2022.

Australian economic forecasts

This week the RBA lifted interest rates for the fifth time since November 2010, up 50 basis points to 2.35 basis points. The RBA also increased the rate on Exchange Settlement balances by 50 basis points to 2.25 per cent.

One prominent source of **ongoing uncertainty** about the economic outlook is the behaviour of household spending. Higher inflation and interest rates are putting pressure on household budgets. Consumer confidence has also fallen, and housing prices are declining in some markets after the large increases in recent years.

The Board believes many households have also built up large financial buffers, and the saving rate remains higher than it was before the pandemic. The Board will be paying close attention to how these various factors balance out as it assesses the appropriate setting of monetary policy.

RBA also said:

"The Board is committed to returning inflation to the 2–3 per cent range over time. It is seeking to do this while keeping the economy on an even keel. The path to achieving this balance is a narrow one and clouded in uncertainty, not least because of global developments. The outlook for global economic growth has deteriorated due to pressures on real incomes from high inflation, the tightening of monetary policy in most countries, Russia's invasion of Ukraine, and the COVID containment measures and other policy challenges in China."

Latest Australian economic data

The **Ai Group Performance of Construction Index (Australian PCI®)** rose by 2.6 points to 47.9 points in August (seasonally adjusted). This indicates contraction in activity across the construction sector for the third month, but the rate of decline eased compared to July (see chart 1).

- Three of the four construction sectors – housing, apartments and commercial – were in contraction in August. Activity improved in the engineering and commercial sectors.
- Demand side pressures – arising from rising interest rates and lower customer demand – are an emerging concern for respondents across all sectors.
- Supply side constraints, including labour and input costs, continue to inhibit the sector. The selling prices indicator eased but remains elevated.
- Capacity utilisation rose slightly to 82.6% and remains elevated as it has been since the start of 2021.

The **Ai Group Performance of Services Index (Australian PSI®)** rose by 1.6 points to 53.3 points (seasonally adjusted) in August 2022 indicating mild growth and an improvement on the three previous months (see chart 2).

- Consumer oriented sectors generally fared better in August. Retail trade & hospitality, improved as did health, education & community services.
- Most services activity indicators were mildly positive, but all price indicators – wages, input prices and sales prices – slowed from record highs.
- Services capacity utilisation rose to 83.7%, the highest result since May 2021. Labour shortages and concerns that future demand will decline were key themes for businesses.

Australia recorded a trade surplus of \$9 billion in July 2022, a decrease of \$8.4 billion (-49%) from the previous month. Overall export volumes were down by 9.9% in the month driven by sharp falls in iron ore, gold, coal and LNG exports, while import volumes grew by 5.2% due to a rise in travel debits.

GDP in Q2 2022: Spending, production & income

The National Accounts show economic performance held in the June quarter of 2022, after a return to more normal growth levels in the Q1 2022. In aggregate, **real GDP expanded by 0.9% q/q in Q2 of 2022, taking it 3.6% higher than in the same quarter one year earlier** (see charts 4 and 5).

All states and territories except the Northern Territory recorded increases in state final demand in Q2 2022. NSW saw a very large growth in household demand and private sector investment. Household consumption also rose substantially in Victoria and Queensland. The strong lift in private sector investment was confined to NSW, South Australia, the ACT and the Northern Territory, with falls across the rest of the country.

The components of the *National Accounts* indicate that the performance in Q2 2022 was due to a combination of domestic consumption, and a rise in certain private sector investments and public sector investments.

- **Household spending** increased by 2.2% q/q and 6.0% y/y (see chart 8 and 9). It contributed 1.1 percentage points to GDP growth in Q2 2022. This gain further reflected stronger trading conditions post-COVID.

- **Government spending** on consumption decreased by 0.8% q/q. Falls in state, local and national level spending all contributed (see chart 10). Public sector consumption was up 6.3% over the year. State and national government consumption surged in 2020 and 2021 in response to the COVID-19 pandemic, and lower government spending in Q2 2022 reflects a withdrawal of this support.
- **Total investment** rose by 0.2% q/q and by 0.3% y/y, driven by falls in building and construction only partly offset by strong machinery and equipment investment (see chart 11). This included:
 - An increase of 4.0% q/q in business spending on machinery & equipment investment (up 5.4% from one year earlier),
 - A decline of 0.5% q/q in business spending on intellectual property (up 4.0% from one year earlier),
 - A fall in dwelling investment of 2.9% q/q to be down by 4.6% from a year earlier.
- 15 of Australia's 19 major industries recorded **growth in output volumes** in Q2 of 2022 (see chart 12):
 - Manufacturing declined by 1.1% q/q and detracted 0.1 ppts from growth in Q2. Food & beverage production rose by 4.3% q/q, metal products decreased by 7.0% q/q while machinery & equipment production decreased by 7.9% q/q.
 - Manufacturing (-1.1% q/q), construction (-0.4% q/q), wholesale trade (-2.2% q/q) and public administration (-0.5% q/q) all showed reduced output.

Table 1: Composition of GDP growth: expenditure and trade, 2021-2022

real volumes <i>Inflation adjusted, seasonally adjusted</i>	Quarter change, q/q				Annual, % y/y Q2-2022
	Q3-2021	Q4-2021	Q1-2022	Q2-2022	
Real GDP (expenditure)	-1.8	3.9	0.7	0.9	3.6
Real GDP per capita	-1.8	3.5	0.3	0.5	2.7
Household consumption	-4.7	6.5	2.2	2.2	6.0
General government consumption	3.4	1.0	2.6	-0.8	6.3
Total investment	0.3	-0.8	0.7	0.2	0.3
Dwelling investment	0.8	-2.0	-0.5	-2.9	-4.6
Private Business investment	0.8	0.6	1.0	-0.8	1.7
<i>New building</i>	3.7	1.4	-1.2	-0.3	3.6
<i>New engineering construction</i>	-3.9	1.3	-0.7	-3.4	-6.6
<i>New machinery and equipment</i>	-1.5	-1.0	3.1	3.9	4.5
<i>Intellectual property investment</i>	1.1	2.0	1.4	-0.5	4.0
Public (government) investment	-2.1	-2.1	2.0	5.9	3.5
Domestic final demand	-1.7	3.5	1.9	1.0	4.7
International trade, volumes and prices					
Exports (volumes)	1.5	-1.1	-0.8	5.5	4.9
Imports (volumes)	-2.4	0.6	11.3	0.7	10.0
Terms of trade (relative prices)	0.7	-5.1	7.5	4.6	7.5

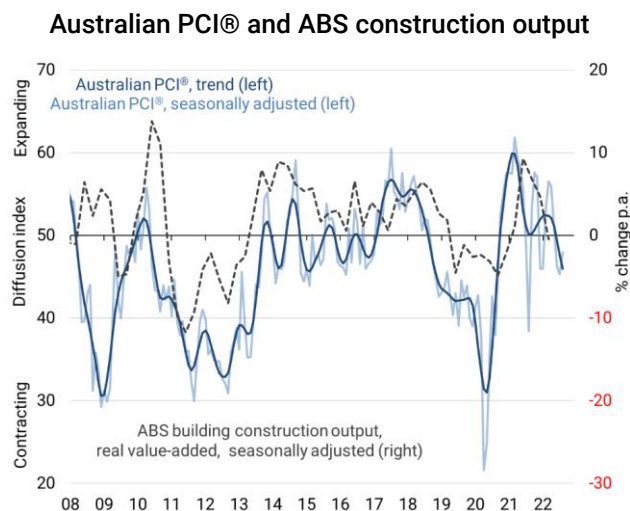
Source: ABS, *National Accounts*, Jun 2022.

Table 2: Composition of GDP growth: production by major industries, 2021-2022

real value-added output volumes <i>Inflation adjusted, seasonally adjusted</i>	Quarter change, q/q				Annual, %	Share of
	Q3-2021	Q4-2021	Q1-2022	Q2-2022	y/y Q2-2022	GDP*, % Q2-2022
Real GDP (production)	-1.8	3.9	0.7	0.9	3.6	100
Agriculture, forestry and fishing	8.2	7.9	-6.4	1.6	11.0	2.9
Mining	1.7	-1.3	-1.3	0.2	-0.7	9.2
Manufacturing	-1.5	2.1	1.0	-1.1	0.6	5.5
Utilities	0.7	-1.2	1.7	4.1	5.3	2.3
Construction	-0.8	2.8	0.7	-0.4	2.2	6.9
Wholesale Trade	-5.8	4.4	3.5	-2.2	-0.5	3.8
Retail Trade	-3.5	7.0	0.8	0.4	4.5	4.3
Food & Accommodation Services	-24.8	23.9	3.8	10.7	7.0	2.1
Transport, Post & Warehousing	-2.3	3.4	4.2	7.5	13.1	4.5
IT, Media & Telecommunications	0.9	5.8	0.2	1.6	8.7	2.3
Finance & Insurance	0.4	1.4	-0.1	0.9	2.6	7.5
Rental & Real Estate services	-0.2	1.9	-1.3	1.0	1.3	2.8
Professional services	0.3	5.0	3.6	1.3	10.5	7.6
Administrative services	-1.1	5.3	1.1	2.8	8.3	3.4
Public Administration & Safety	0.8	1.6	0.2	-0.5	2.2	5.3
Education	0.4	0.4	0.4	0.4	1.7	4.7
Health	-2.2	5.9	-0.7	2.5	5.4	7.9
Arts & Recreation	-5.8	9.1	4.4	3.6	11.1	0.8
Personal & Other Services	-13.6	17.6	-0.5	1.9	3.2	1.7

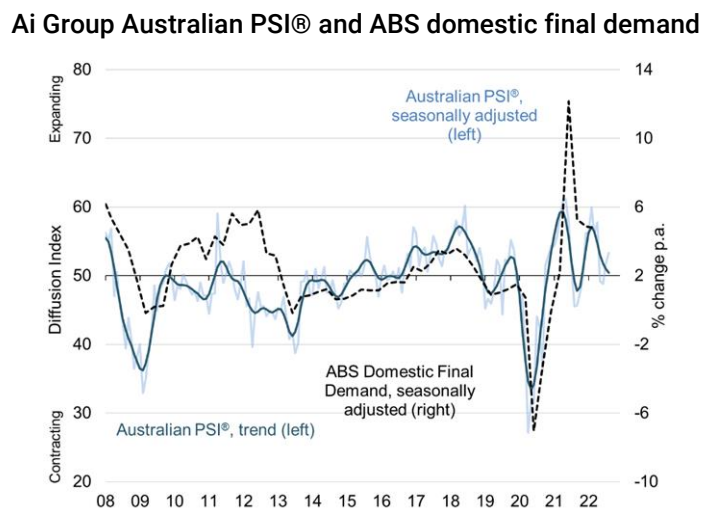
* All industries do not sum to 100% of GDP due to individual seasonal adjustment of industries and other accounting items that are included in total GDP such as 'ownership of dwellings', 'taxes less subsidies' and 'statistical discrepancy'. Source: ABS, *National Accounts*, Jun 2022.

Chart 1: Ai Group-HIA Australian PCI® rose by 2.6 points to 47.9 points in August (seasonally adjusted). This indicates contraction in activity across the construction sector for the third month, but the rate of decline eased compared to July.



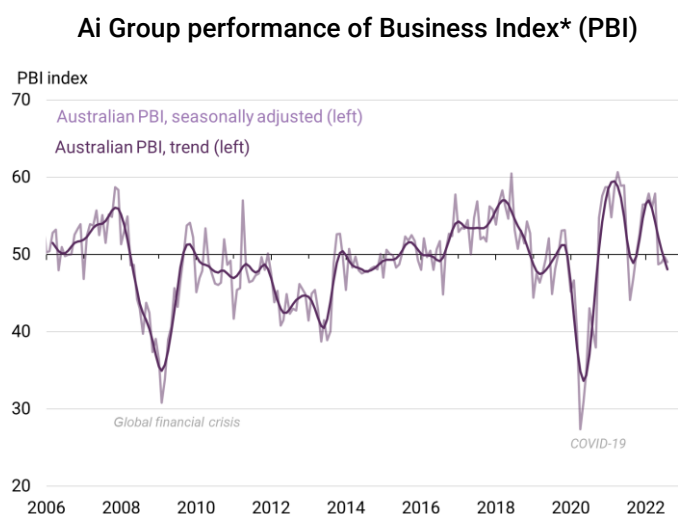
Results below 50 points indicate contraction, with lower results indicating a stronger pace of contraction. Sources: ABS, *National Accounts*, March 2022 and Ai Group-HIA *Australian PCI*, August 2022.

Chart 2: Ai Group's Australian PSI® rose by 1.6 points to 53.3 points (seasonally adjusted) in August 2022 indicating mild growth and an improvement on the three previous months (results above 50 points, seasonally adjusted indicate expansion).



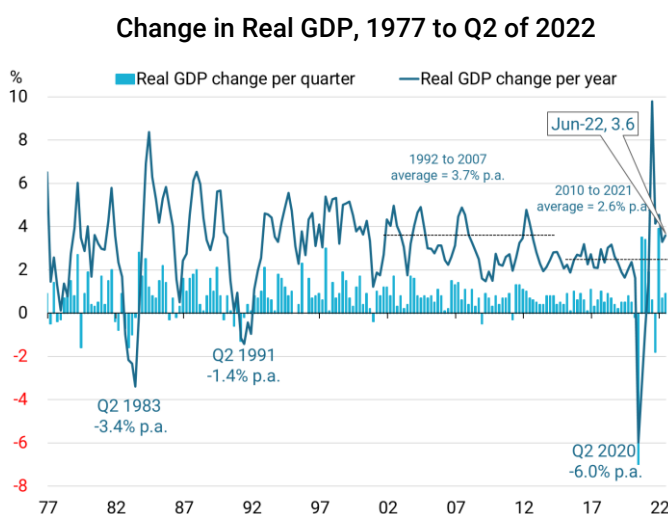
Results above 50 points indicate expansion, with higher results indicating a stronger pace of expansion. Sources: ABS, *National Accounts*, March 2022 and Ai Group *Australian PSI*, August 2022.

Chart 3: The Ai Group performance of Business Index* fell by 0.7 points to 49.0 points in August 2022 indicating flat results in August (seasonally adjusted). This reflects a reversal of the mild growth recorded in July.



* Composite of Ai Group Australian PMI, PCI and PSI. Net balance indexes. 50 = neutral. Sources: Ai Group, August 2022.

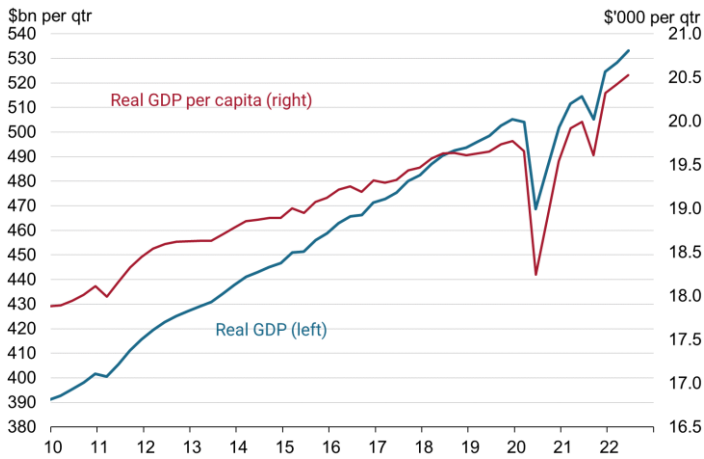
Chart 4: Real GDP moderated in the March 2022 quarter (+0.8% q/q) after rebounding in December 2021 (+3.6% q/q). The moderated but strong performance recorded in Q1 2022 continued in the June 2022 quarter, maintaining the normal trend of growth. This result may be impacted by stronger inflation and interest rate increases in Q3 2022.



Source: ABS, *National Accounts*, June 2022.

Chart 5: Real GDP and Real GDP per capita continued on a strong path since the solid rebound in the December quarter of 2021.

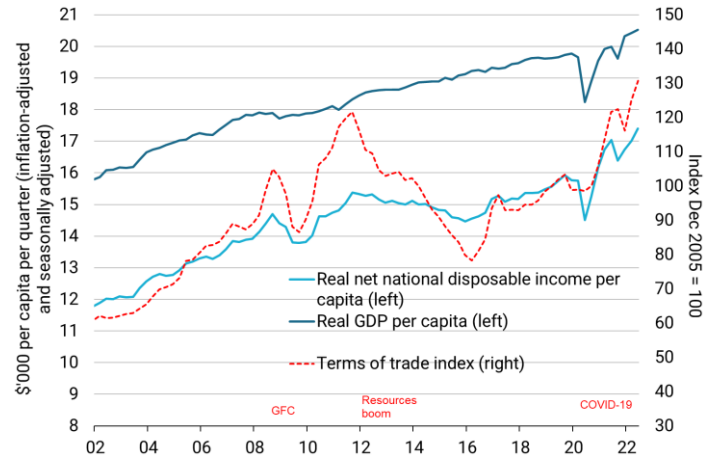
Real GDP and GDP per capita, 2010 to Q2 2022



Source: ABS, *National Accounts*, June 2022.

Chart 6: Real net national disposable income per capita (the best measure of changes in national income) grew modestly in Q2 2022 (+2.7% q/q and +3.0% over the year). This was supported by a further recovery in GDP per capita (+0.5% q/q and +2.7% y/y in Q2) and an increase in the terms of trade (+4.6% q/q and +7.5% over the year).

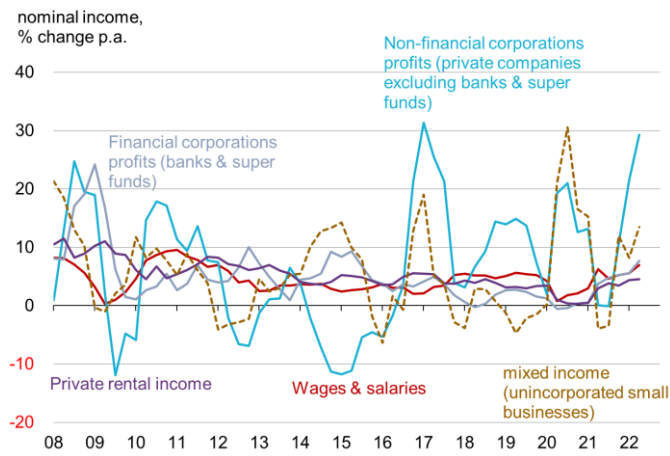
Real net national disposable income per capita, GDP per capita and terms of trade, 2002 to Q2 2022



Source: ABS, *National Accounts*, June 2022.

Chart 7: Total factor income (nominal) improved in Q2 2022 by 4.9% and by 12.6% relative to Q2 2021. Compensation of employees was up by 2.4% in Q2 and by 7.0% relative to Q2 2021.

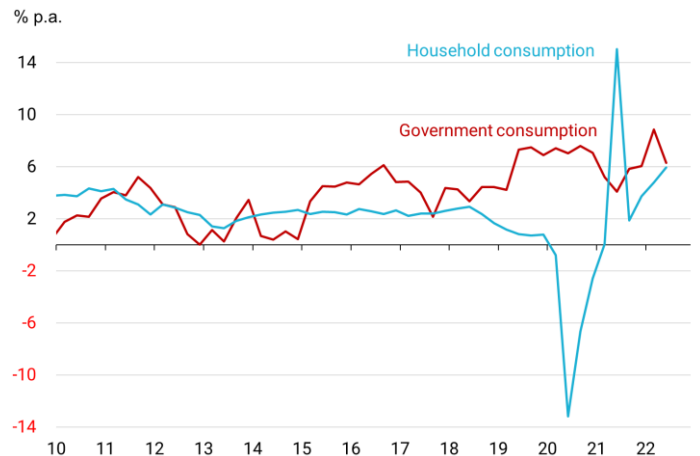
Total factor income growth, by source of income, 2008 to Q2 2022



Source: ABS, *National Accounts*, June 2022.

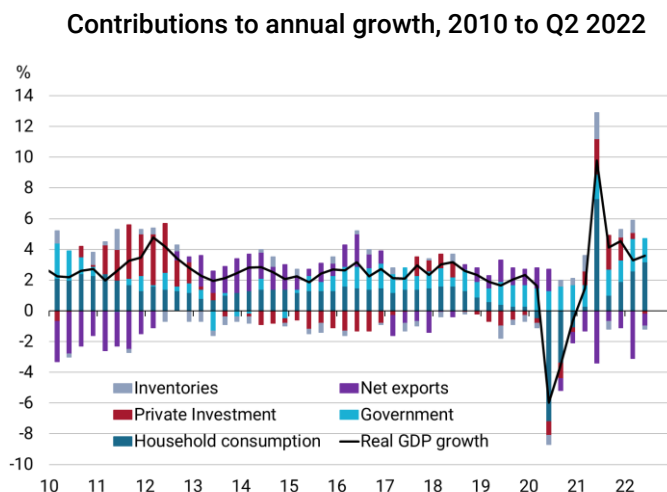
Chart 8: Growth in Q2 2022 was driven by a lift in household consumption. General government consumption expenditure fell in Q2 2022.

Household and government consumption growth (annual), 2010 to Q2 2022



Source: ABS, *National Accounts*, June 2022.

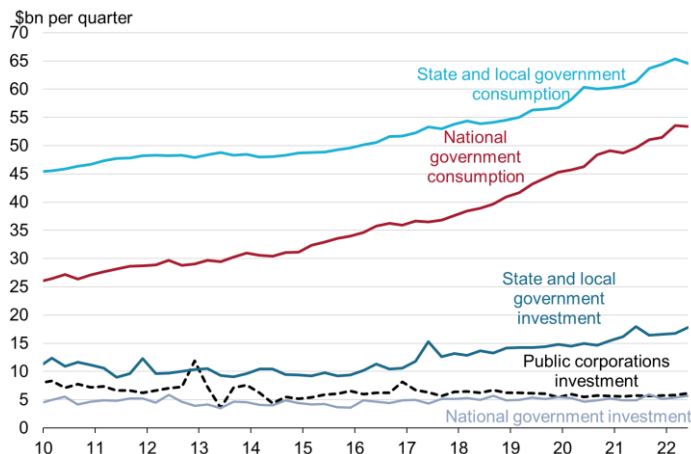
Chart 9: Higher household consumption and public sector investment contributed to growth in Q2 2022. Lower inventories detracted from growth.



Source: ABS, *National Accounts*, June 2022.

Chart 10: State and national government consumption fell in Q2 2022. On the other hand, state and national government investment rose in the quarter. Lower government spending in Q2 2022 may reflect a withdrawal of some support provided in response to the COVID-19 pandemic as businesses transition to a post-COVID setting.

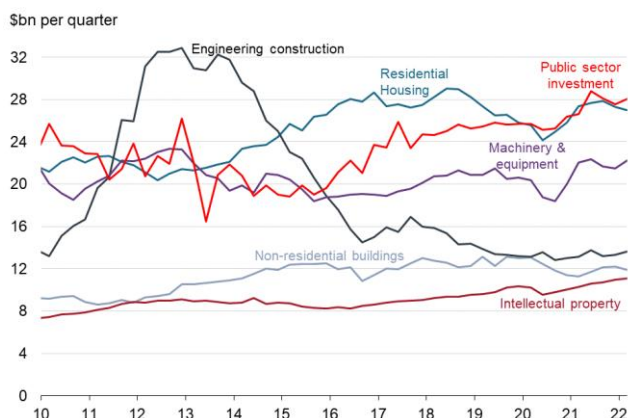
Government consumption and investment spending, 2010 to Q2 2022



Source: ABS, *National Accounts*, June 2022.

Chart 11: Investment in certain areas of the private sector and investment by the public sector were up in Q2 2022, but investment in residential and non-residential buildings was lower.

Household, business and government investment, 2010 to Q2 2022



Source: ABS, *National Accounts*, March 2022.

Chart 12: Production volumes were higher in Q2 2022 than one year earlier in all industries except mining and wholesale trade. The largest annual increase was recorded in transport, arts & recreation services and agriculture.

Production volumes* by industry, Q2 2021 to Q2 2022



* real value added output volumes.

Source: ABS, *National Accounts*, June 2022.

This week's data and events 05 September – 09 September 2022

Day	Date	Data/event	Data period
Mon	05 Sep	ABS, Business Indicators	June 2022
Mon	05 Sep	RBA, Monetary Policy Decision	September 2022
Mon	05 Sep	Ai Group, Performance of Construction	August 2022
Wed	07 Sep	Ai Group, Performance of Services	August 2022
Wed	07 Sep	ABS, Australian National Accounts: National Income, Expenditure and Product	June 2022
Thu	08 Sep	ABS, Weekly Payroll Jobs and Wages	Week ending 13 August 2022
Thu	08 Sep	ABS, International Trade in Goods and Services	July 2022

Next week's data and events 12 September – 16 September 2022

Day	Date	Data/event	Data period
Tue	13 Sep	ABS, Overseas Arrivals and Departures	July 2022
Tue	13 Sep	NAB, Monthly Business Survey	August 2022
Tue	13 Sep	ANZ-Roy Morgan, Australian Consumer Confidence	September 5-11 2022
Wed	14 Sep	ABS, Labour Account	June 2022
Wed	14 Sep	Westpac – MI, Consumer Sentiment	September 2022
Thu	15 Sep	ABS, Labour Force	August 2022

Ai Group Industry Performance Indicators

Australian Performance of Manufacturing Index®	August 2022	49.3 ▼
Australian Performance of Construction Index®	August 2022	47.9 ▲
Australian Performance of Services Index®	August 2022	53.3 ▲

Seasonally adjusted. Arrows represent direction of movement relative to last observation. Source: Ai Group.

Australian economy: latest annual growth rates and RBA forecasts (as of Aug 2022)

% change over the year	Dec 2021	Jun 2022	Dec 2022	Jun 2023	Dec 2023	Jun 2024	Dec 2024
Gross domestic product (GDP)	4.2	3.6	3.2	2.3	1.8	1.8	1.7
Household consumption	3.5	6.0	4.9	2.8	2.4	2.3	2.2
Dwelling investment	5.3	-4.6	1.7	2.5	-0.1	-2.6	-4.8
Business investment	6.4	1.7	4.9	5.9	6.6	5.7	4.6
Public demand	5.1	3.5	3.6	-0.5	-0.7	0.8	1.8
Gross national expenditure	5.0	4.4	3.7	1.5	1.5	1.8	1.9
Imports	1.0	10.0	11.4	6.2	4.0	3.0	2.9
Exports	-2.6	4.9	8.6	9.8	5.1	2.8	2.2
Terms of trade	10.3	7.5	2.6	-14.6	-8.9	-4.4	-1.6
Real household disposable income	3.7	3.0	-0.9	-3.1	-0.9	0.9	1.5
Unemployment rate (qtr average, %)	4.2	3.8	3.4	3.4	3.5	3.7	4.0
Employment	2.1	3.2	4.4	2.2	1.4	1.1	0.9
Average wage rates (WPI)	2.3	2.6	3.0	3.4	3.6	3.8	3.9
Trimmed mean inflation (CPI)	2.6	4.9	6.0	5.0	3.8	3.3	3.0
Headline inflation (CPI)	3.5	6.1	7.8	6.2	4.3	3.5	3.0

■ = actual. □ = forecast. Sources: ABS, various data; RBA 'baseline scenario' in *Statement on Monetary Policy*, August 2022.

Forecasts 3 August. Forecasts are conditioned on a path for the cash rate broadly in line with expectations derived from surveys of professional economists and financial market pricing. Other forecast assumptions: TWI at 63, A\$ at US\$0.69 and Brent crude oil price at US\$94bbl. Assumed rate of population growth is broadly in line with the profile set out in the Aus Gov 2022/23 Budget.

Ai Group Research and Economics Team

Dr Jeffrey Wilson
Director of Research
and Economics

Colleen Dowling
Senior Research Analyst
& Team Leader

Dr Nike Adeoye
Economist

Dr Aneeq Sarwar
Senior Economist

Adiba Mohammed
Research Assistant

economics@aigroup.com.au