

Australia's economy

Recession or rebound?

Grant Thornton – Bankers' Boot Camp

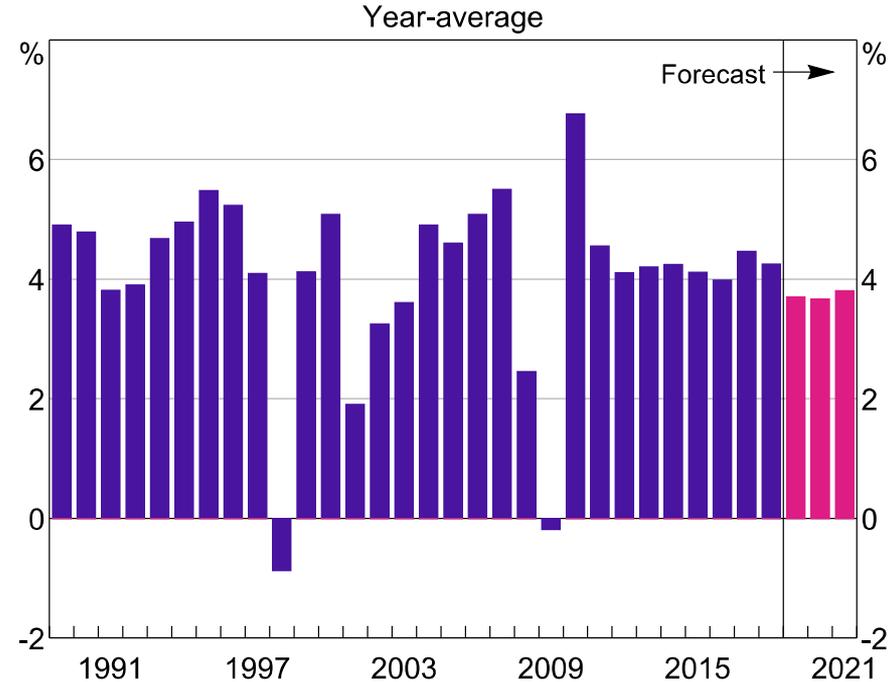
October 2019

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Market Economics

A favourable global outlook despite the headwinds

- Global growth remains solid and the outlook for 2020 & 2021 is positive
- There are risks – US-China trade, Eurozone dislocation, geopolitics - but central banks will come to the rescue with easy money

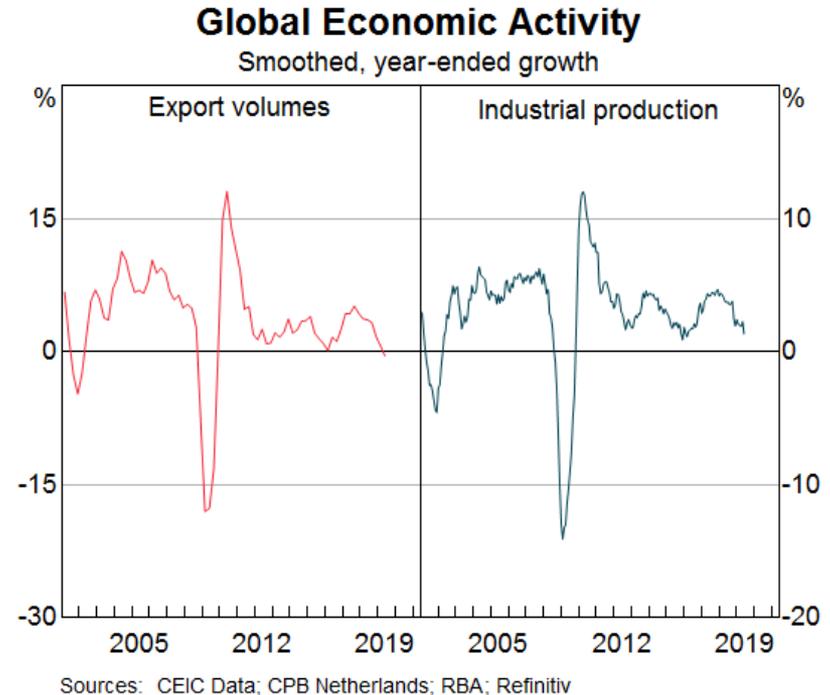
Australia's Trading Partner Growth



Sources: ABS; CEIC Data; RBA; Refinitiv

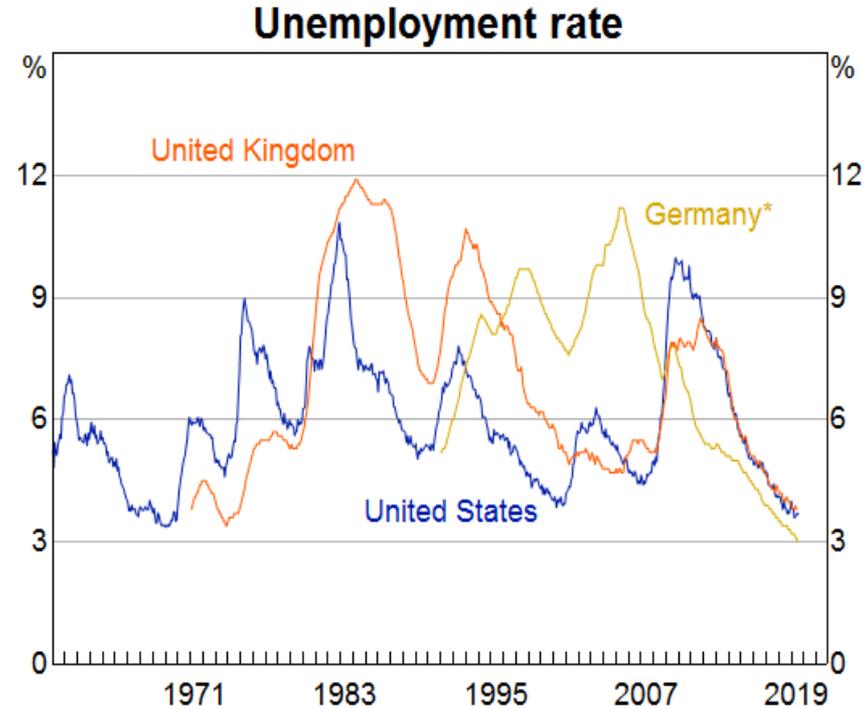
Some signs of downside risks to global growth

- Export orders have weakened as the tariff and trade wars escalate
- Manufacturing is also weaker than a year ago, but it is still growing – will it turn higher as easier monetary policy starts to impact?



The good news is record low unemployment

- Even though growth in many countries has been moderate, unemployment rates are at record lows
- This is helping consumer incomes and spending and is a strong positive signal for growth in 2020



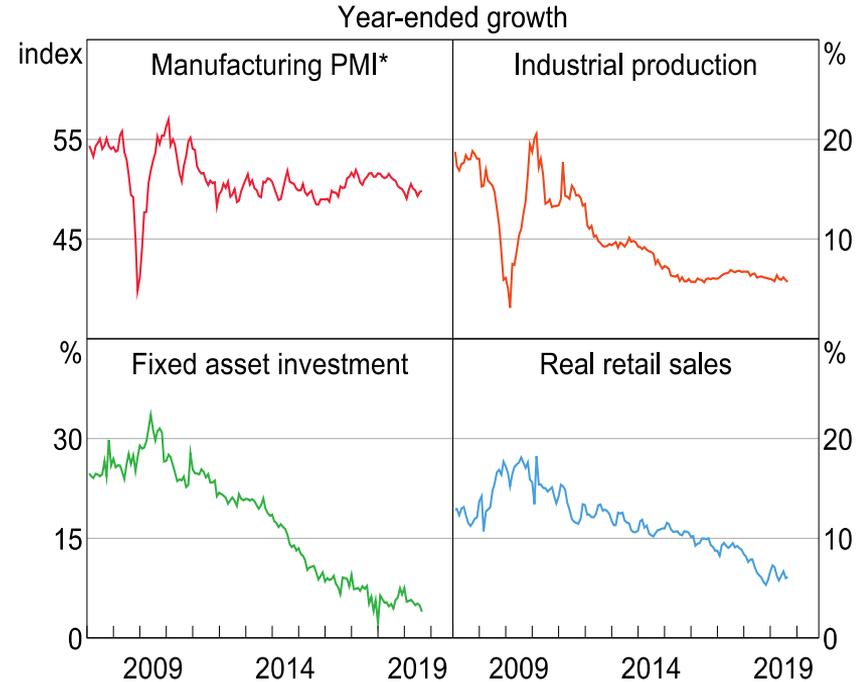
* Harmonised measure

Sources: Eurostat, Refinitiv

China has slowed, but is now consolidating

- China's miraculous economic boom continues, but as it matures growth will slow
- Policy has been eased (the exchange rate, interest rates & credit) which should support the economy into 2020
- While the impact of the trade war is uncertain, growth is starting to edge higher

China – Activity Indicators



* Diffusion index; average of the official and Caixin

Sources: CEIC Data; Markit Economics; RBA

Australia's "dream" economy – it has slowed, but is there light at the end of the tunnel?

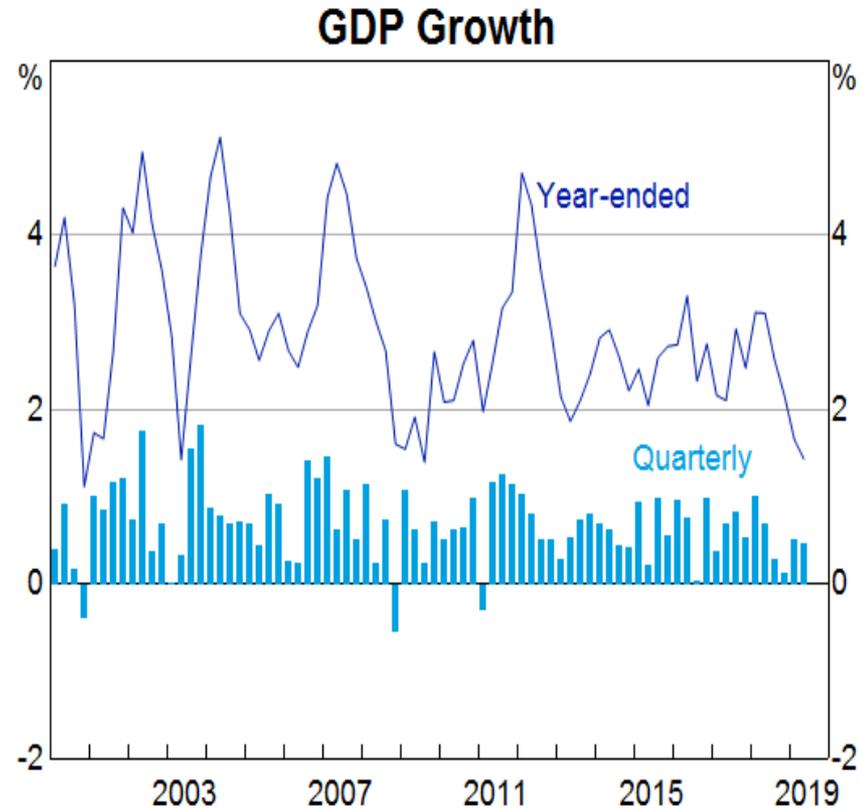
- The economy stalled in the middle of 2018 & in 2019, it remains weak
- Downside pressures – housing, consumer spending – are showing tentative signs of bottoming
- Light at the end of the tunnel? Interest rate cuts, tax cuts, exports, business investment, public sector spending?
- The consumer is vital if we are ever to see 3% GDP growth

Recession?

Close to zero per cent chance

First some sobering news

- GDP growth has slowed to a pace rarely seen since the early 1990s recession
- Tighter fiscal policy (the unexpected balanced budget) and RBA sluggishness in cutting interest rates are to blame

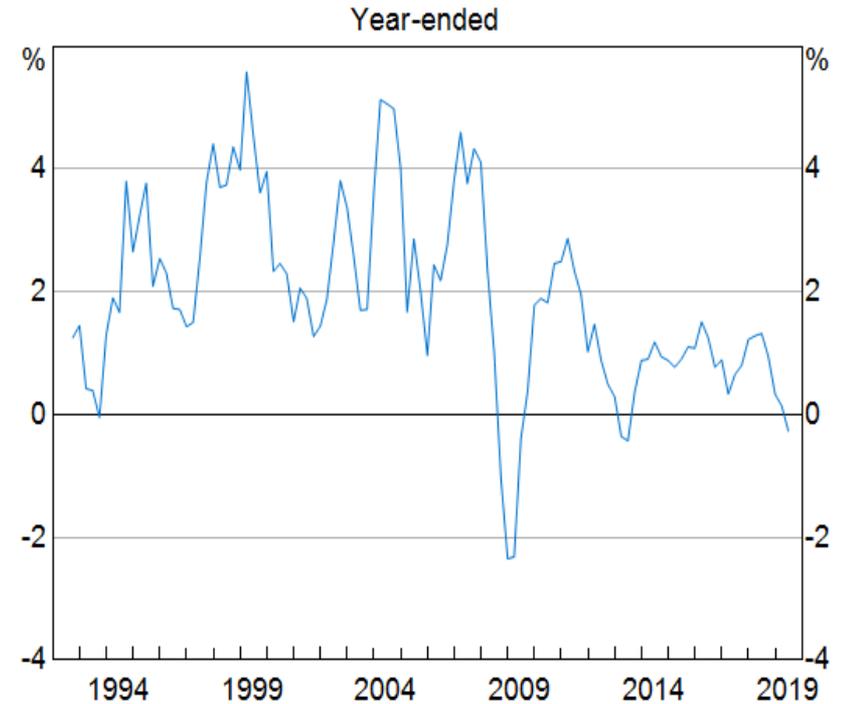


Source: ABS

You and me – we are to blame!

- Household spending per capita is falling & is structurally weaker than in the decades before the GFC
- Weak wages growth, high debt levels, falling wealth (house prices) and lower savings rates impact consumer behaviour

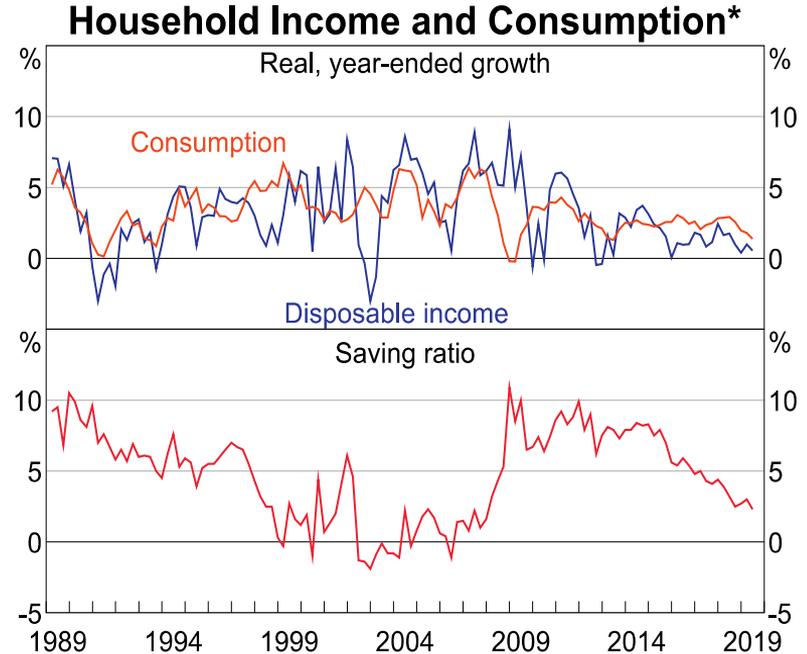
Household Consumption Growth per Person



Source: ABS

Household spending is constrained by income

- Household consumption growth continues, but it has been based on weak foundations – lower savings & higher debt
- Wages (incomes) growth **must** pick-up for consumer spending growth to be sustained even at these moderate levels

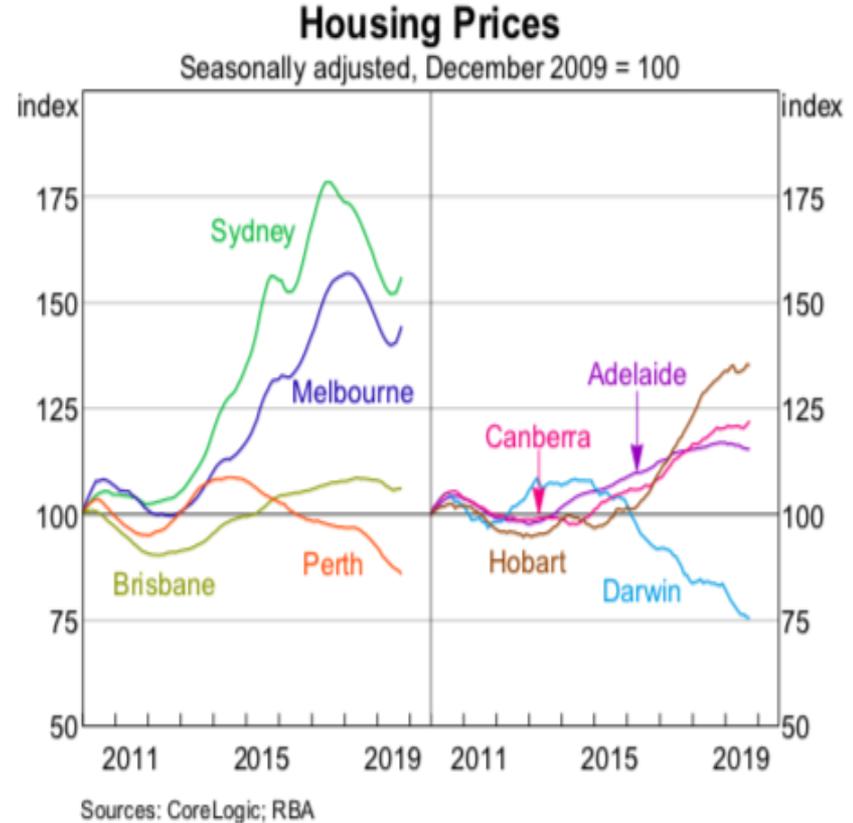


* Household sector includes unincorporated enterprises; disposable income is after tax and interest payments; saving ratio is net of depreciation

Sources: ABS; RBA

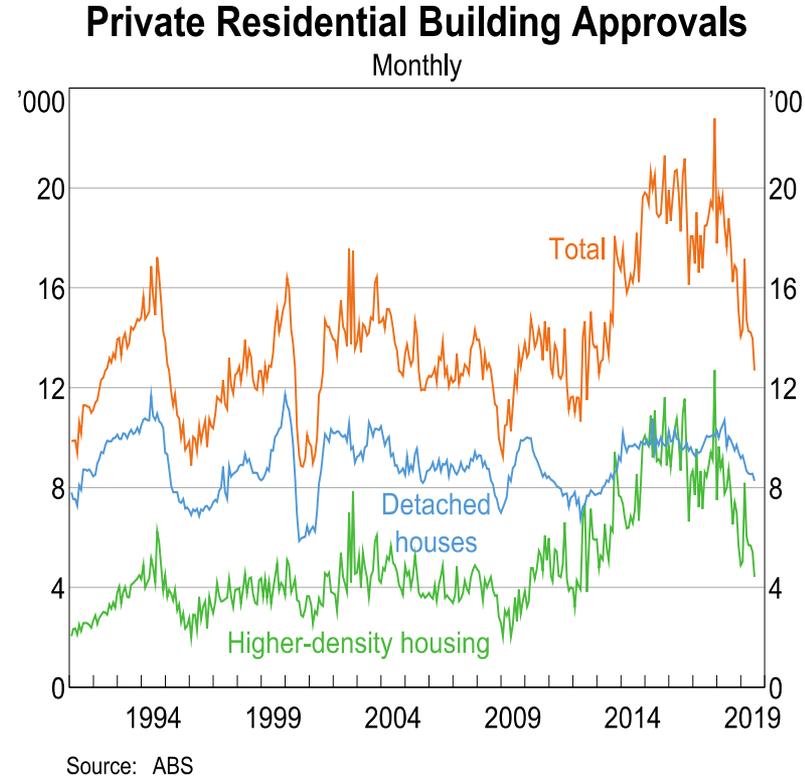
House prices are turning higher

- From the peak in late 2017 to the middle of 2019, Australia-wide house prices fell 10%
- Since mid-2019, prices have edged higher, particularly in Melbourne & Sydney
- The only weak cities are Perth & Darwin



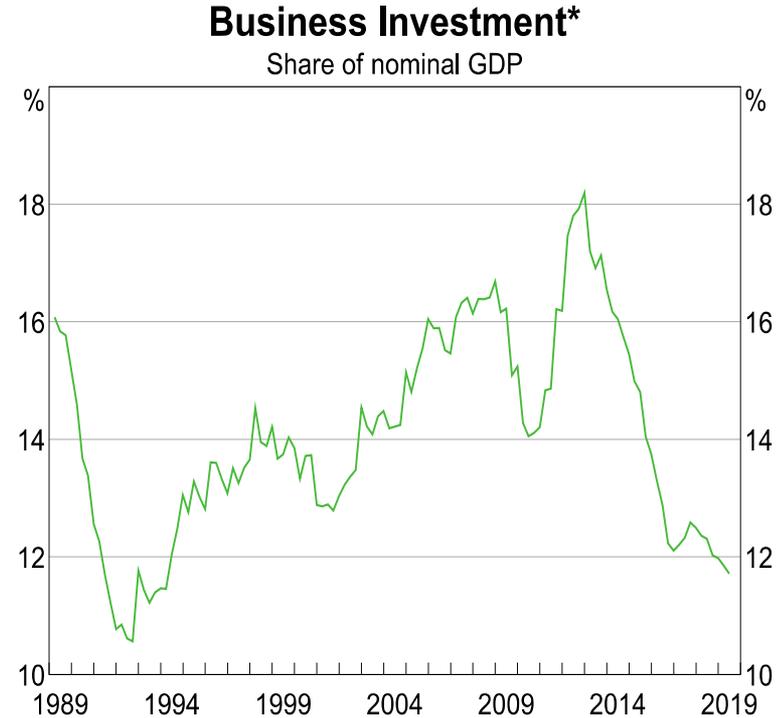
Dwelling construction is falling sharply

- The fall in new residential building approvals is severe. It will see new construction activity fall through 2019 & 2020
- The falls will undermine growth in new supply which, in time, will support prices, even though the GDP impact will be negative



Business investment – the only way is up

- Business investment has slid to near recessionary lows – mining has been the main area of weakness
- According to the ABS survey of expectations, private sector capex will rise by around 10% in FY2019-20

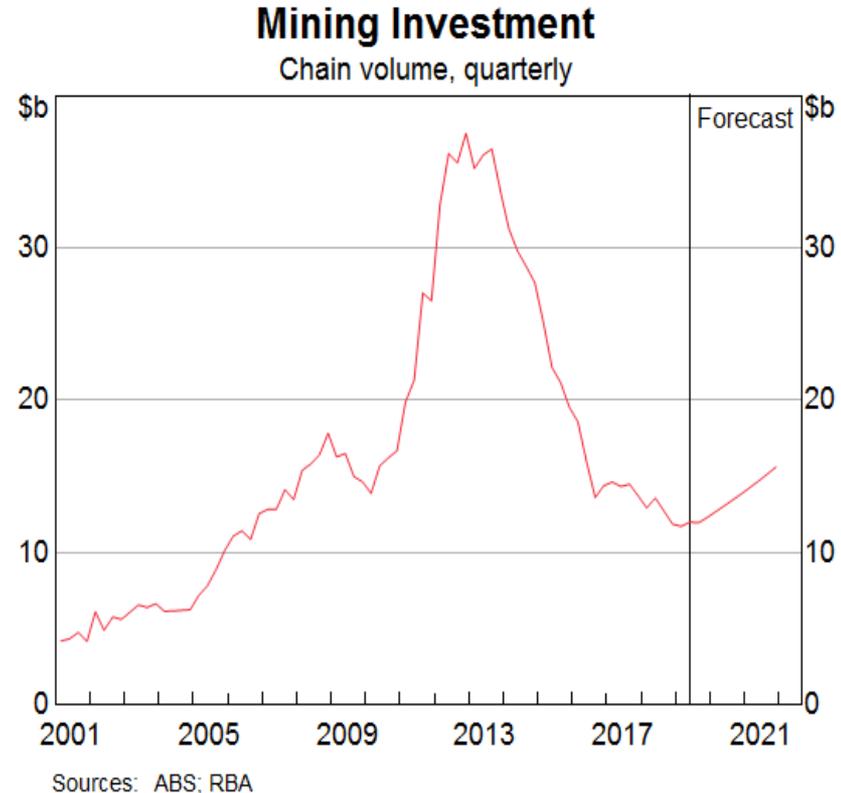


* Adjusted for second-hand asset transfers between the private and other sectors

Source: ABS

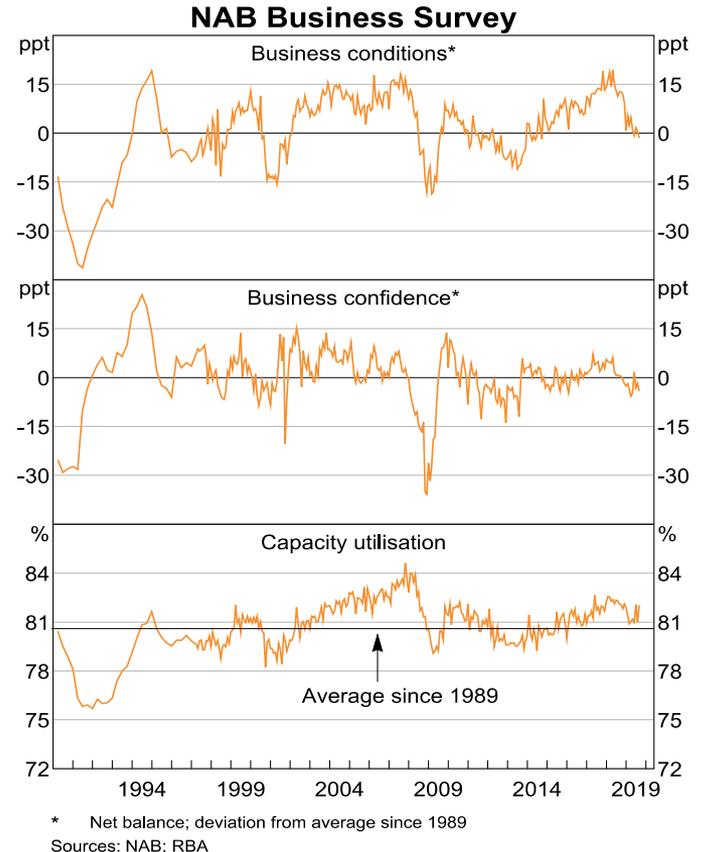
Mining sector investment is turning the corner

- Mining investment is turning higher. Mining companies are ramping up capacity in existing productive mines & are poised to open new mines
- It is a positive outlook based on strong export volumes & generally buoyant prices



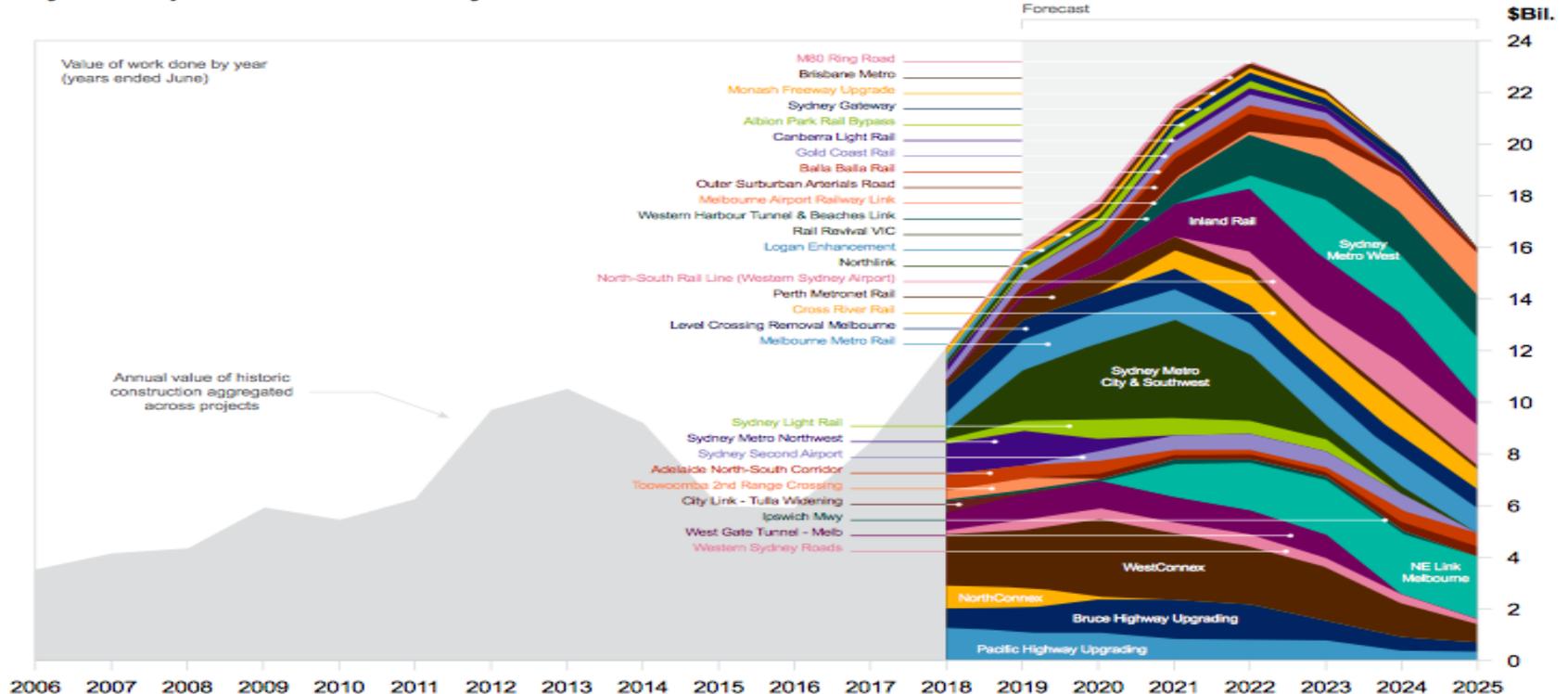
Business sentiment is ticking lower

- The economic slowdown is being reflected in measures of business sentiment which are lower, but not yet too concerning
- Business confidence lifting immediately after the election but this was not sustained. Global issues & uninspiring domestic policy have impacted



Pipeline of new infrastructure remains solid

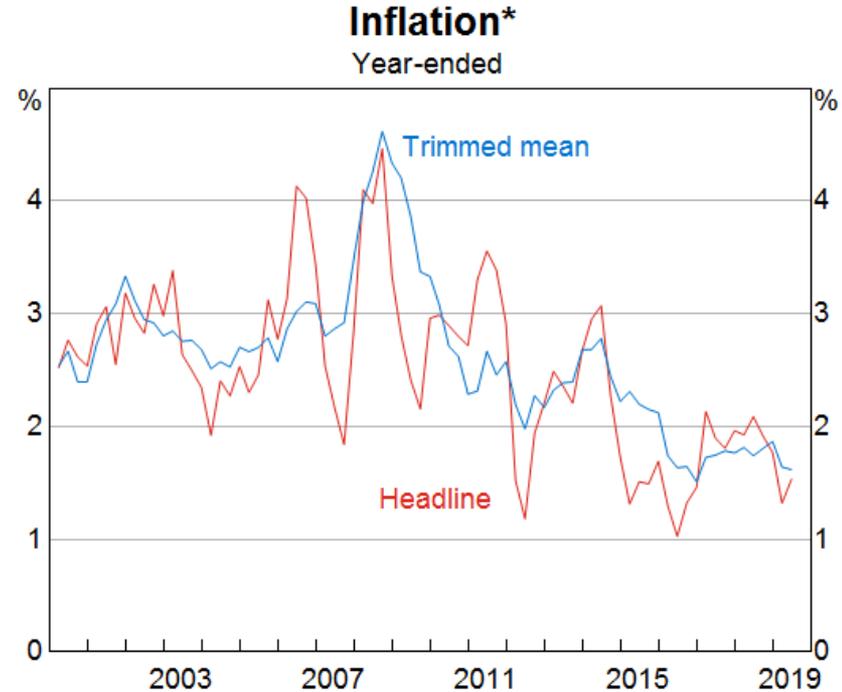
Major Transport Infrastructure Projects - Australia



Source: Macromonitor – Australian Construction Outlook Overview, December 2018.

Low inflation = low interest rates

- Inflation has been below the bottom of the RBA 2 to 3% target range for nearly 4 years. The latest data show it remaining low
- Current forecasts have it remaining at or below 2% for at least the next 2 years



* Excludes indirect deposit & loan facilities; adjusted for the tax changes of 1999–2000

Sources: ABS; RBA

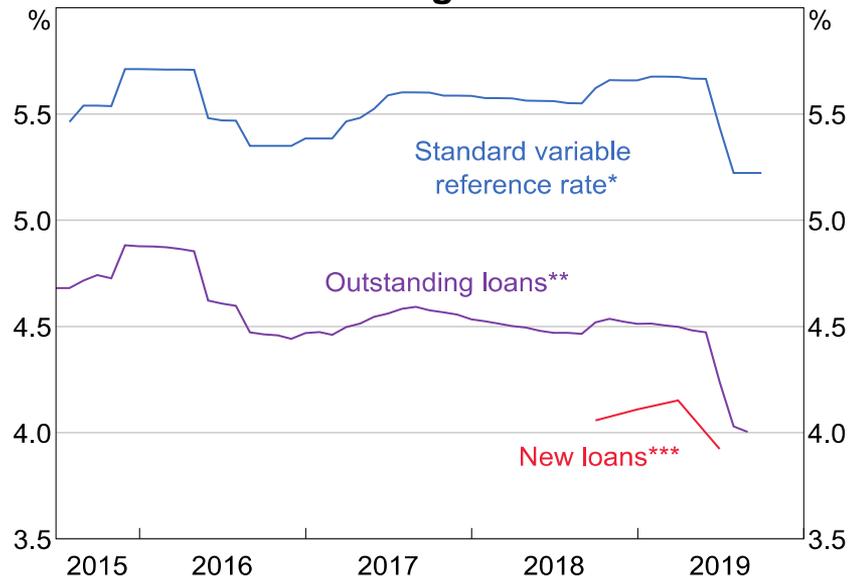
Interest rates – at historic lows

10-year Australian Government Bond Yield



Sources: RBA; Yieldbroker

Variable Housing Interest Rates



* Average across major banks' rates; data to September

** Data from the Securitisation Dataset, re-weighted using housing credit shares; data to August

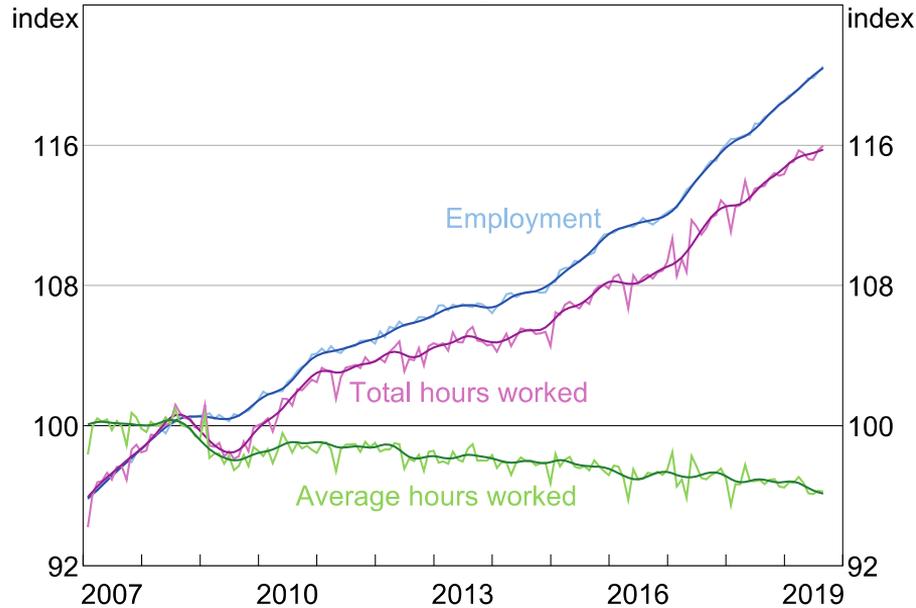
*** Quarter-average data from APRA (to June quarter)

Sources: APRA; major banks' websites; RBA; Securitisation System

The labour market is faltering

Employment and Hours Worked*

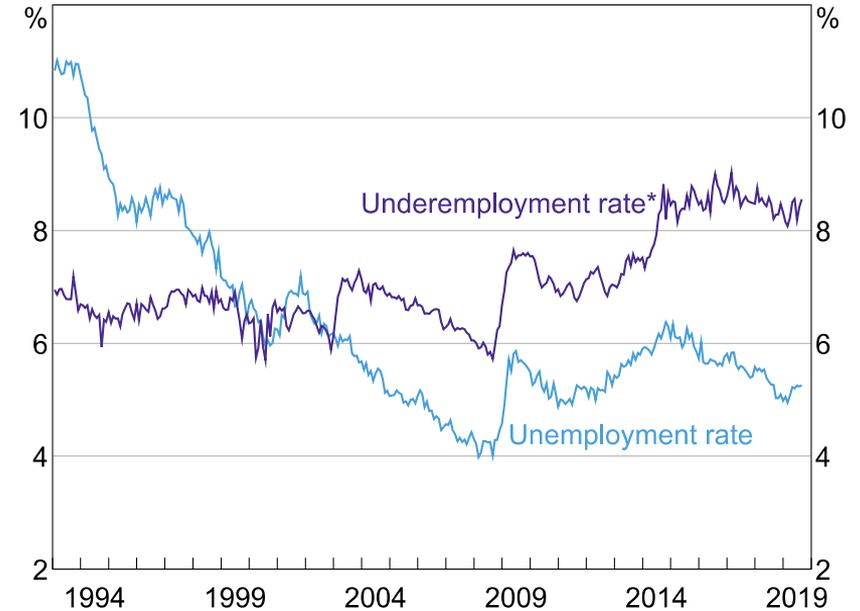
2008 average = 100



* Smoothed lines are 13-period Henderson trends

Sources: ABS; RBA

Labour Market

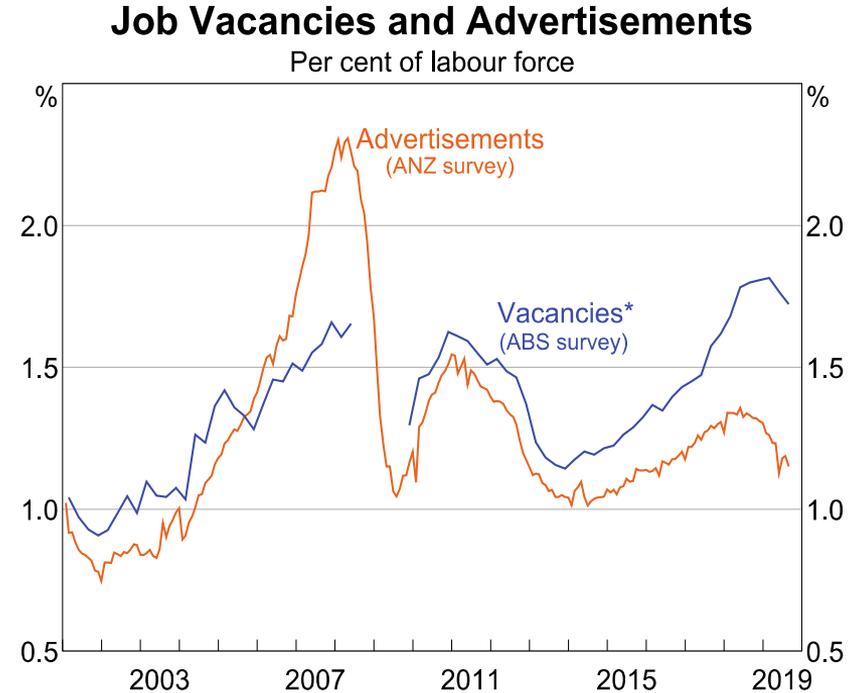


* Full-time workers on reduced hours for economic reasons and part-time workers who would like, and are available, to work more hours

Source: ABS

Falling job ads points to higher unemployment

- Reflecting the economic slowdown, job vacancies and ads are turning lower
- Changes in the job vacancies/ads tend to lead changes in the unemployment rate by about 3 months – higher unemployment seems inevitable

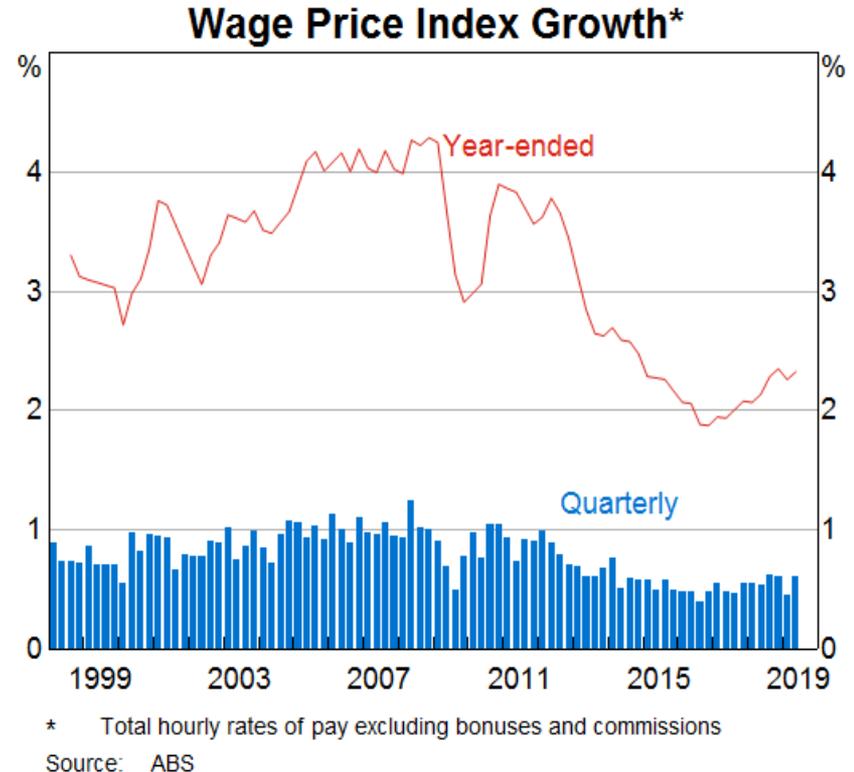


* This survey was suspended between May 2008 and November 2009

Sources: ABS; ANZ

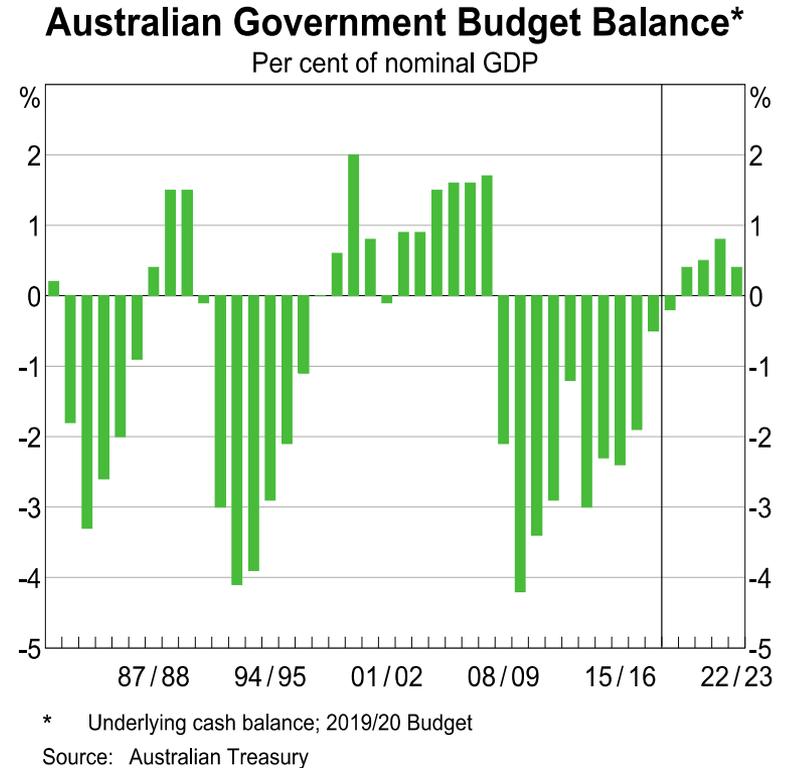
Wage growth - edging up from record lows

- Wages growth is edging up, but it remains near historical lows
- Any acceleration in wages growth is likely to be constrained by slack in the labour market, the soft economy & global competition



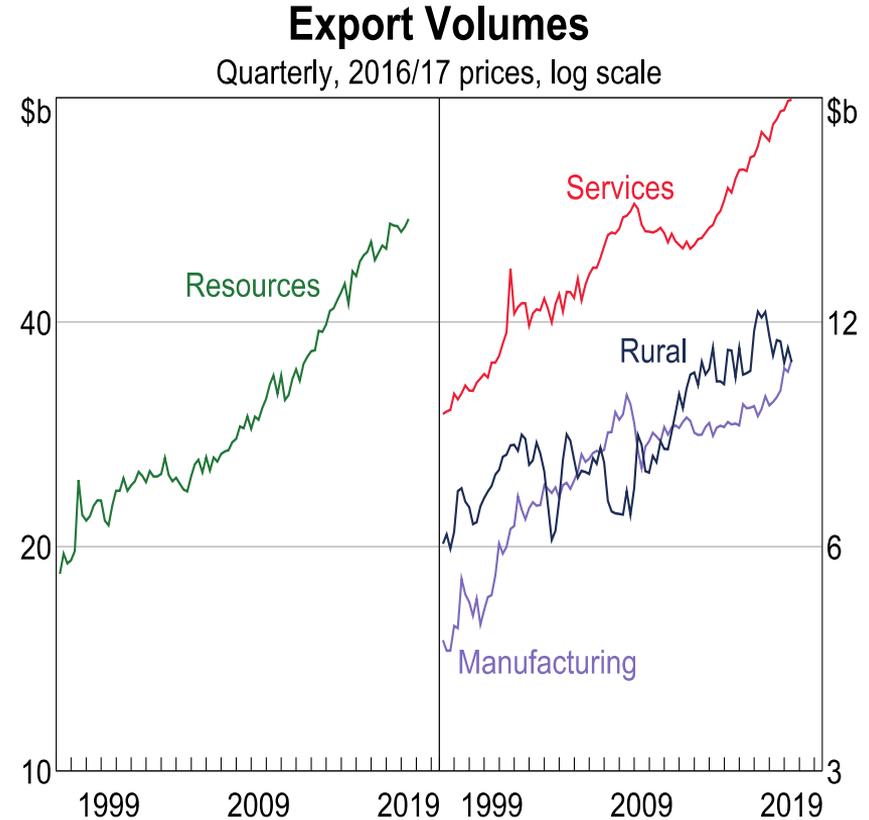
A balanced budget vs jobs and growth

- Politics vs policy
- The path to surplus looks assured, but is this good policy?
- With RBA constrained as interest rates approach zero, pressure is building on the government to use fiscal policy to add to growth



Exports boom!

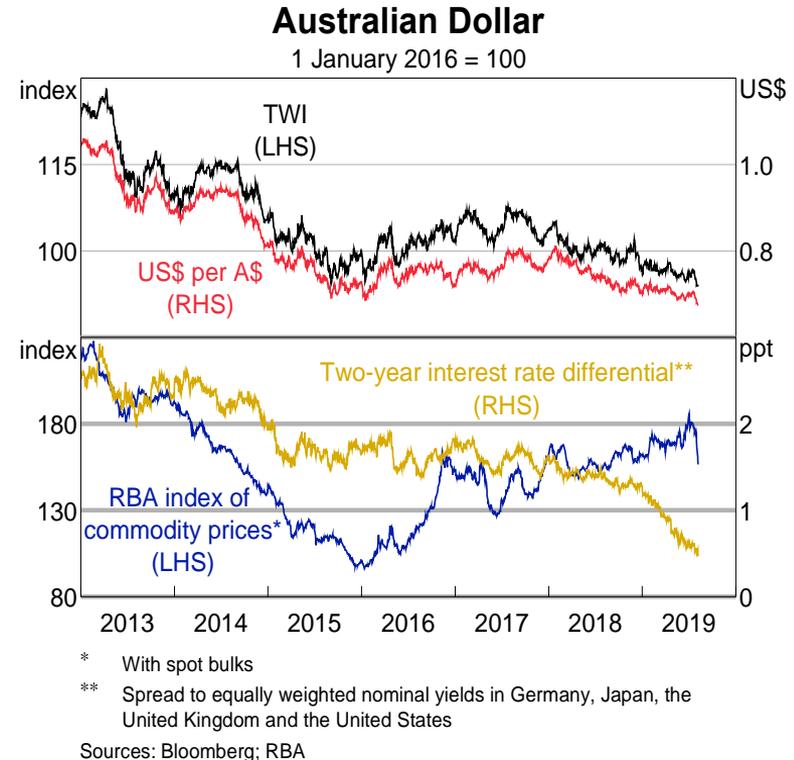
- Resources exports are booming, aided by high prices but also solid demand from China
- Services exports (mainly tourism & education) are also buoyant aided by the low AUD
- Rural exports have weakened recently as the drought has impacted. Manufacturing exports have been strong, from a low base



Sources: ABS; RBA

The Aussie dollar is still drifting lower

- The AUD has been drifting lower against the USD & recently it has fallen on the cross rates
- A wide negative interest rate gap to the US should see it drift lower, even as the Fed cuts rates
- The path to US65 cents looks assured, but will that be the low?



The outlook – risks and issues: Evenly balanced

- Global events loom large: Trade war, 2020 US election, China / Hong Kong, Brexit, Europe, to name a few
- Policy is reacting – look at central banks cutting interest rates right around the world
- The risks are evenly balanced:
 - 2020 could be a very strong year for the global economy

The outlook – some light at the end of the tunnel

- A **moderate** economic pick-up is in prospect for 2020 – but more policy stimulus is needed to lock this in
- The big question is whether it will be sufficiently robust to see unemployment fall, wages and inflation accelerate
- Growth supported by exports, public sector spending & business investment
- A retail recovery is the dark horse – could it be the positive X-factor? Housing weak until late 2020
- Interest rates to remain low for a long time – RBA to cut some more

QUESTIONS

