Bulletin

28 February 2014

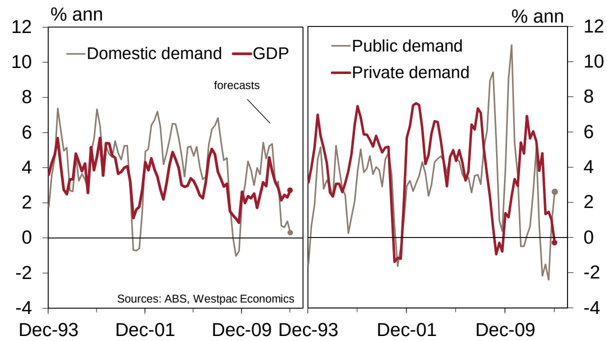
Australian Q4 GDP, a preview: Lopsided growth, with exports the key support

2013 Q4(f): 0.9%qtr, 2.7%yr

- **The Australian National Accounts, to be released on Wednesday March 5, will provide an estimate of economic activity in Q4.**
- **GDP growth is forecast to strengthen to 0.9%qtr in Q4, up from 0.6% in Q3. That would be the strongest result since 2012 Q1. Annual growth ticks higher to 2.7% from 2.3%.**
- **There were mixed messages from various key indicators for late 2013, potentially evidence that growth was particularly lopsided in this quarter.**
- **Labour market conditions were weak, employment stalled in Q4 and hours worked contracted, down 0.3%. Australia's terms of trade was neutral for national income in the quarter, with the index broadly flat on our estimate.**
- **By contrast, consumer and business confidence improved in the second half of 2013, buoyed by the Federal election on September 16. Low interest rates, a lower AUD and a lift in household wealth also supported confidence.**
- **Private surveys reported a lift in business conditions from below average levels in Q3, to near average in Q4. This trend was driven largely by the consumer. Accordingly, we anticipate some improvement in household consumption.**
- **Net exports will add 0.8ppts to Q4 GDP, on our estimate, led by resource exports as capacity expands. Inventories are expected to make a small contribution, partially reversing a sizeable negative in Q3.**
- **Elsewhere conditions were disappointing: housing construction, down; business cut investment; and we anticipate a decline in public demand. Thus, we expect domestic demand to contract by 0.3% and annual growth to slow to only 0.3%, the weakest since 2009.**
- **We and the RBA expect GDP growth to be below trend in 2014. Housing construction and resource exports will perform well. But we see three significant exogenous headwinds: a downturn in mining investment; sub-par public demand as governments look to improve their budgets; and a negative income shock via a declining terms of trade associated with a slowing of China.**
- **The balance of these forces, and a still high currency leading to structural change, points to sluggish jobs growth. A negative feedback from the labour market to the household sector will restrain consumer spending and in turn stifle an upturn in non-mining investment.**

Household consumption (0.7%): We expect consumption growth to improve from a sluggish 0.4%qtr in Q3 to 0.7%qtr in Q4. Consumers were more positive during the second half of 2013, with the Westpac-MI Consumer Sentiment index averaging 102 in Q2, 106 in Q3 and 108 in Q4, then retreating to 100.3 in February.

Australian economic conditions



This spike in confidence appears to have translated into stronger spending. Real retail sales rose 0.8% in Q3 and a further 0.9% in Q4, lifting annual growth to 3.5%. Motor vehicle sales edged higher in the final months of the year after edging lower in Q3. Services spending was soft in Q3, limiting total consumption growth to only 0.4%. Private business surveys suggest that services spending firmed in Q4.

Dwelling investment (–0.4%): The new dwelling construction upswing that emerged in the second half of 2012 stalled in 2013. The Construction survey reports that such work declined by 2.5% in Q4, and that this was largely offset by a 3% rise in renovations.

New business investment (–3.5%): Firms placed investment plans on hold, possibly in part due to policy uncertainty associated with the Federal election. Quarterly partial data report that: equipment spending fell by 8.6% in Q4; infrastructure work declined by 1.6%; and non-residential building fell by 2.8%. We expect the remaining segment, intellectual property products, to inch higher, restrained by a drop in exploration.

Public spending (–0.3%): Public spending has been volatile around a weak trend. We anticipate a soft end to 2013, forecasting a 0.3% decline. That follows a 0.2% contraction in Q2 and would see annual growth at 2.6%, subject to revisions.

Net exports (0.8ppts): Export volumes expanded by an estimated 3½% in Q4, with this strong result largely centred on resources (iron ore and coal). Imports contracted further, down an estimated 0.5% following a sharp 3.3% drop in Q3.

Private non-farm inventories (flat, +0.2ppt contribution): Stock levels are expected to stabilise following a run-down in Q3. That would see inventories add 0.2ppts to Q4 GDP, partially reversing a 0.4ppt subtraction last quarter.

The Business Indicators survey (Mon), the Balance of Payments (Tue) and Public Demand data (Tue) will provide further clues as to the risks surrounding our forecast for Q3 GDP (published Wed).

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