Q3 National Accounts

Resilience Running Out

BankSA Economics
6 December 2023

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Overview and Outlook

- The economic resilience displayed over the first half of 2023 ran out of puff in the September quarter. Economic activity expanded by a subdued 0.2% over the quarter to be 2.1% higher in annual terms.
- This was below the record 2.4% increase in the population over the year, driving a 0.3% annual fall in GDP per capita. Population growth initially supported demand and provided a source of resilience. That now looks to be fading with the drag on incomes from headwinds including elevated inflation, higher income tax and higher interest payments weighing on spending.
- Household incomes are under intense pressure. Real household disposable income fell 4.3% over the year to the September quarter – the largest fall since the 1980s!
- While there was some relief from the moderation in inflation and higher earnings, it was not enough to offset a larger drag from taxes. The total tax take as a share of gross income hit a record high of 17.7% in the quarter. This was driven by bracket creep and the unwinding of low and middle income tax offset (LMITO). As a result, nominal household disposable income barely budged, despite strong growth in labour income.
- Reflecting the pressure on households, consumption stalled in the September quarter. The weak number was also flattered by the ongoing catch up in vehicle deliveries. Income growth was even weaker than consumption, necessitating a further fall in the savings ratio to 1.1% – the lowest savings rate since December quarter 2007.
- Business investment cooled but remained elevated. The slower investment was driven by an expected pull-back in machinery and equipment investment coinciding with the end of generous tax incentives in the June quarter. Mining investment drove the quarterly gain, while non-mining investment eased.
- Measured productivity took an initial step in the right direction – rising 0.9% in the quarter. As foreshadowed, a fall in hours worked as the economy shifts gears and a catch up in the capital stock will drive a mechanical improvement in productivity growth. This process appears afoot.

GDP Expenditure Measure – GDP (E) – 1 of 2

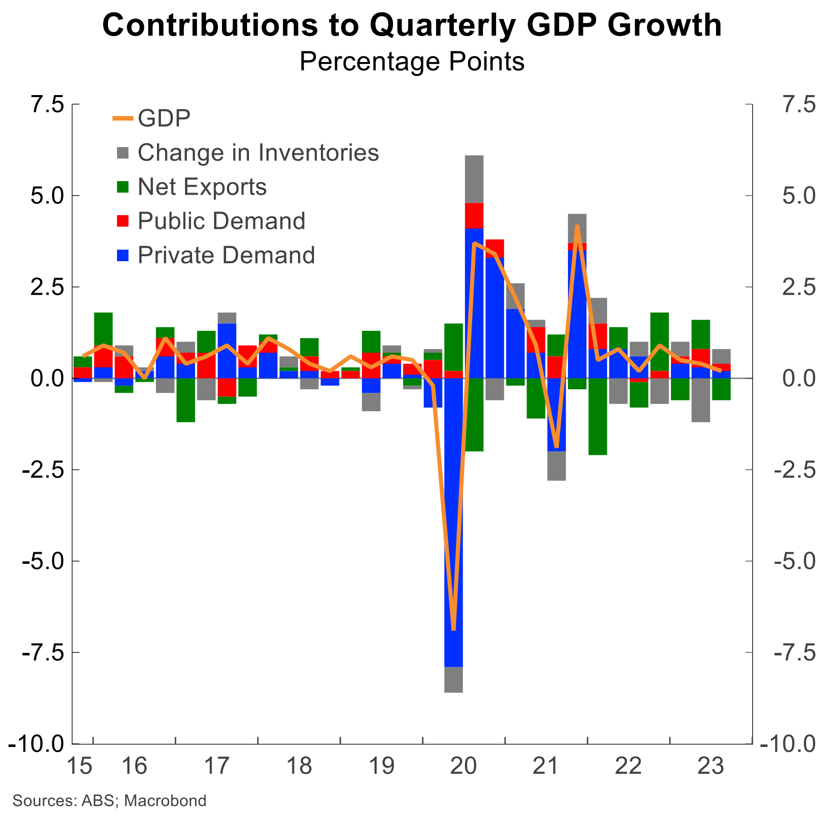
Selected Expenditure Items on GDP, Chain Volume Measures

	Quarterly % Change
Household Consumption	0.0
Public Consumption	1.1
Dwelling Investment	0.2
New Business Investment	0.6
New Public Investment	2.8
	Contribution to GDP, ppt
Inventories	0.4
Net Exports	-0.6

- Annual GDP growth rose to 2.1% in the September quarter – a tad below the long-run average.
- This is against the backdrop of record annual population growth of 2.4%.
- GDP per capita fell 0.5% in the quarter and 0.3% in annual terms. The largest annual fall since the GFC (outside of COVID).

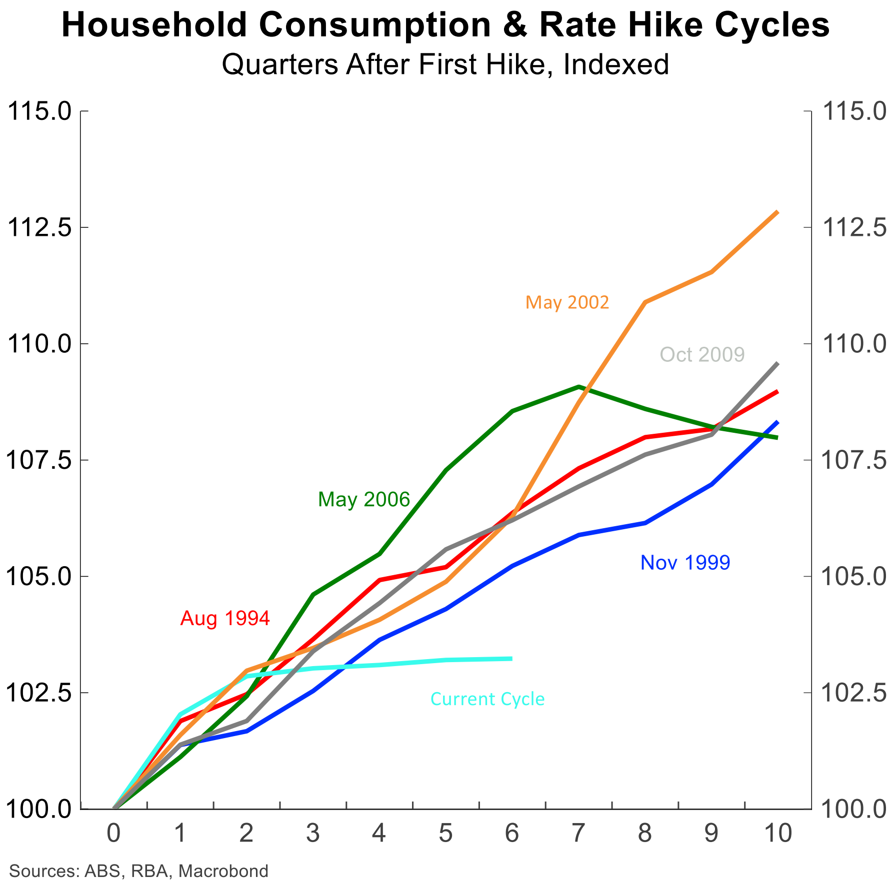
- GDP rose an anaemic 0.2% in the September quarter. Consumer spending stalled, investment slowed and government spending picked up the pieces.
- **Household consumption** hit a wall as real household disposable incomes took an unprecedented hit. The end of the Low-Middle Income Tax Offset (LMITO) dragged heavily on household income. Taxes as a share of household gross income rose to a record high of 17.7%. This more than offset the relief from falling inflation and higher earnings.
- Businesses lost some of their recent investment enthusiasm. **New business investment** rose 0.6% in the quarter, compared to respective gains of 2.5% and 4.2% over the first two quarters of the year. Annual growth in business investment slowed from 10.1% to 8.0%. Spending on machinery and equipment slowed significantly alongside the expiry of generous tax incentives. However, new engineering construction remained robust, rising 2.3% in the quarter. New business investment contributed 0.1 percentage points to growth in the quarter.
- The **government sector** – consumption and new investment collectively – added 0.3 percentage points to growth in the quarter. Government spending was supported by defence and large outlays on subsidies including for energy and childcare.

GDP Expenditure Measure – GDP (E) – 2 of 2



- **Inventories** continued to fall, but with less vigour compared to the substantial run down in the June quarter. A fall in public and farm inventories was partially offset by expanding inventories in the mining, manufacturing and retail sectors.
- A slower run-down in inventories contributed 0.4 percentage points to GDP growth in the September quarter.
- Providing a substantial drag on growth was **net exports** which detracted 0.6 percentage points from growth.
- Export volumes slipped 0.7% over the quarter, driven by weaker commodity demand. Services exports partly offset some of this weakness, rising 1.9% as tourism related exports rose to be more than 5% above pre-pandemic levels and international student number hit a record high. Imports rose 2.1%, underpinned by an 8.4% surge in services imports as Australian's flocked overseas in droves.

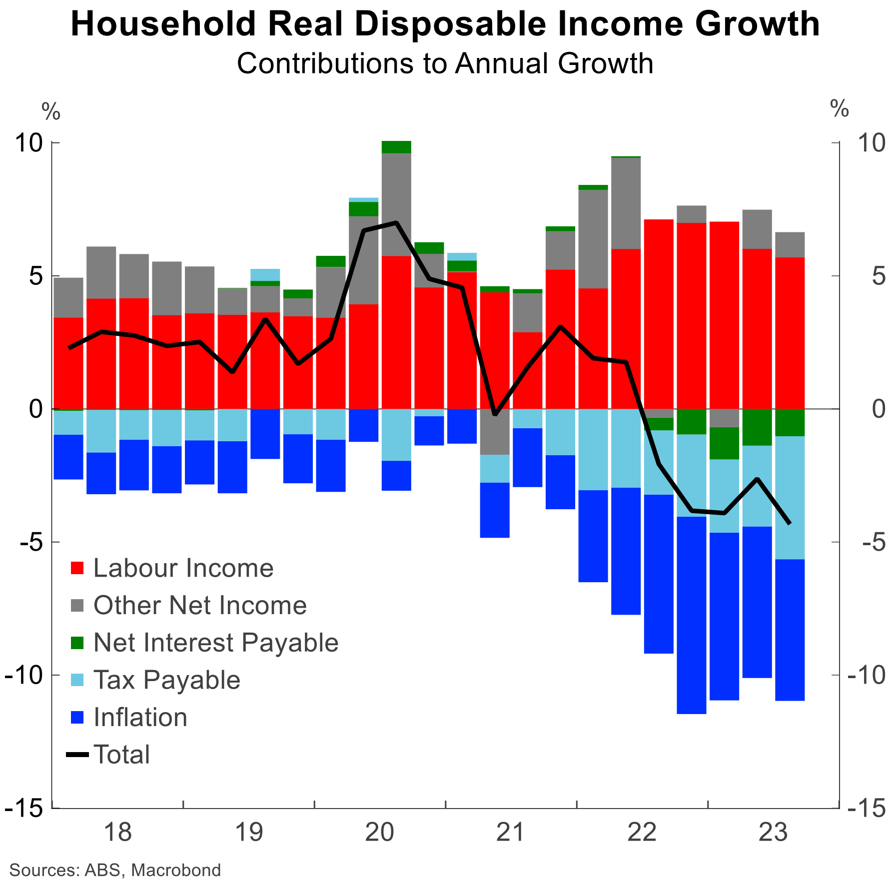
Household Consumption Unmistakably Weak



- Household spending stalled in the September quarter as incomes remained under heavy pressure.
- The flat outcome saw annual growth in household consumption slow to just 0.2%, the weakest reading since the GFC (outside of COVID).
- Large government rebates for electricity and childcare impacted the numbers as a chunk of consumption was shifted from households to governments. i.e. households are still consuming electricity and childcare, but the government is footing part of the bill.
- When excluding spending on electricity and utilities, household consumption rose 0.4% in the quarter.
- This was almost entirely driven by a whopping 13.0% quarterly increase in spending on the purchase of motor vehicles. This increase is related to the ongoing improvement in vehicle deliveries following significant disruptions since the pandemic. Motor vehicle purchases made up a record 3.2% of household spending the September quarter and were around 60% higher than pre-pandemic levels.
- Elsewhere, consumption is unmistakably weak. It’s long been argued that we will reach a point in the cycle where households spending collapses. There is little doubt we have now passed the precipice.

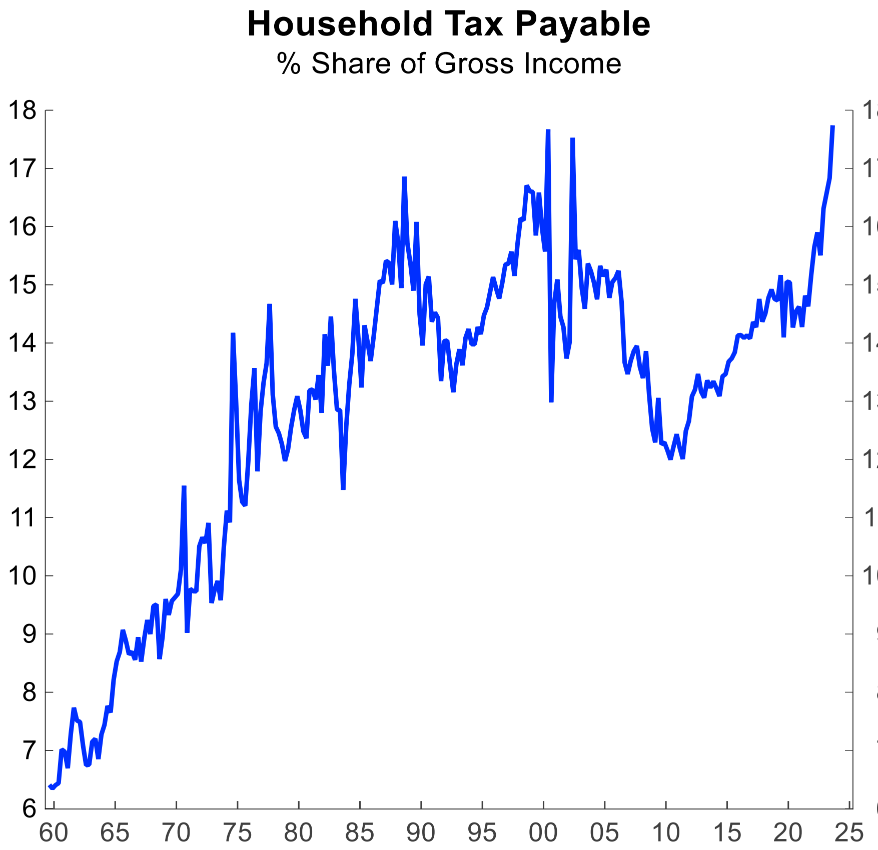
Household Budgets Are Under Intense Pressure

- Nominal household disposable income was essentially flat, increasing by just 0.1% in the September quarter. In annual terms, disposable income grew by 1.0% – the slowest rate since the December quarter 2002.
- This is despite strong growth (6.5%) in labour income over the year.
- While higher earnings are proving households with some support, this has been more than offset by elevated inflation, higher income tax payable due to bracket creep and the unwinding of COVID-related measures, and higher interest payments.
- Elevated inflation continues to act as a drag on household disposable incomes. When accounting for inflation, household disposable income fell by 4.3% over the year to the September quarter – the sharpest annual fall since the 1980's.
- Households continued to draw down on accumulated savings to finance their spending. Reflecting this, the household savings ratio eased to 1.1% from 2.8% in the June quarter. This was the lowest savings rate since December quarter 2007.



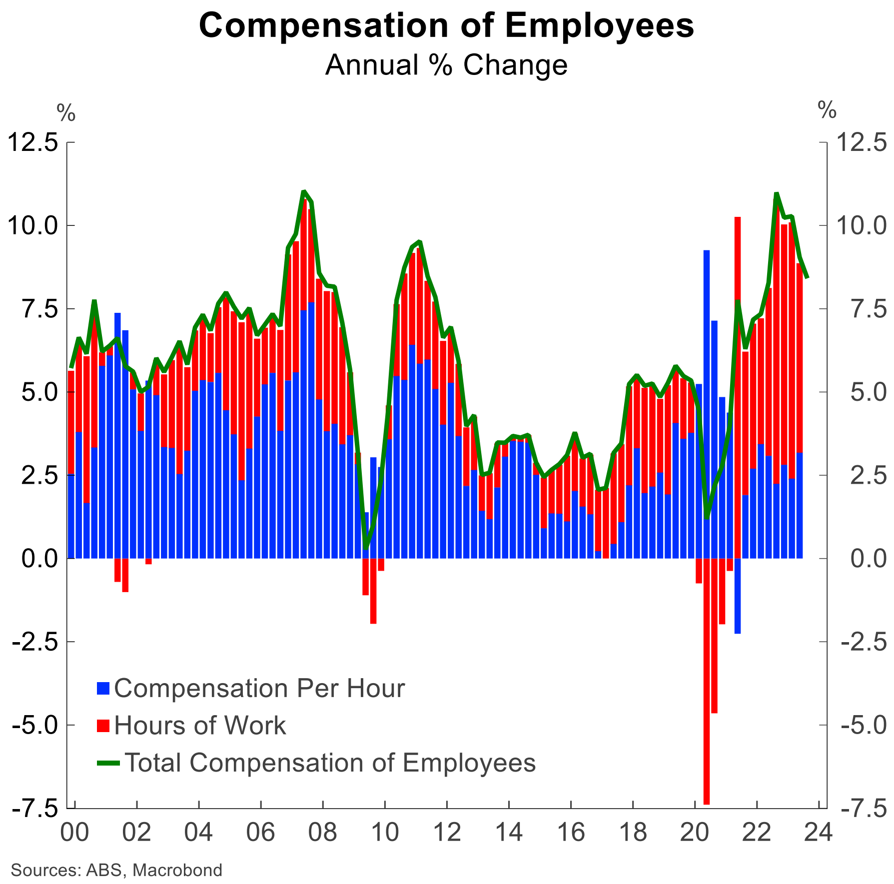
Record Share Of Income Spent On Tax

- Tax payable as a share of household income increased to a record high of 17.7% in the quarter. This was driven by bracket creep and the unwinding of low and middle income tax offset (LMITO).
- The 2022-23 income year was the first since 2018-19 that the LMITO was unavailable. As a result, households were unable to claim the tax offset. This would have increased tax payable for some individuals by as much as $1,500 compared to the 2021-22 income year.
- In addition, income tax brackets are not indexed in Australia. As a result, when income growth picks up, bracket creep increases the average tax paid by households.
- Non-income tax has also increased substantially, this includes stamp duties, land taxes, etc.



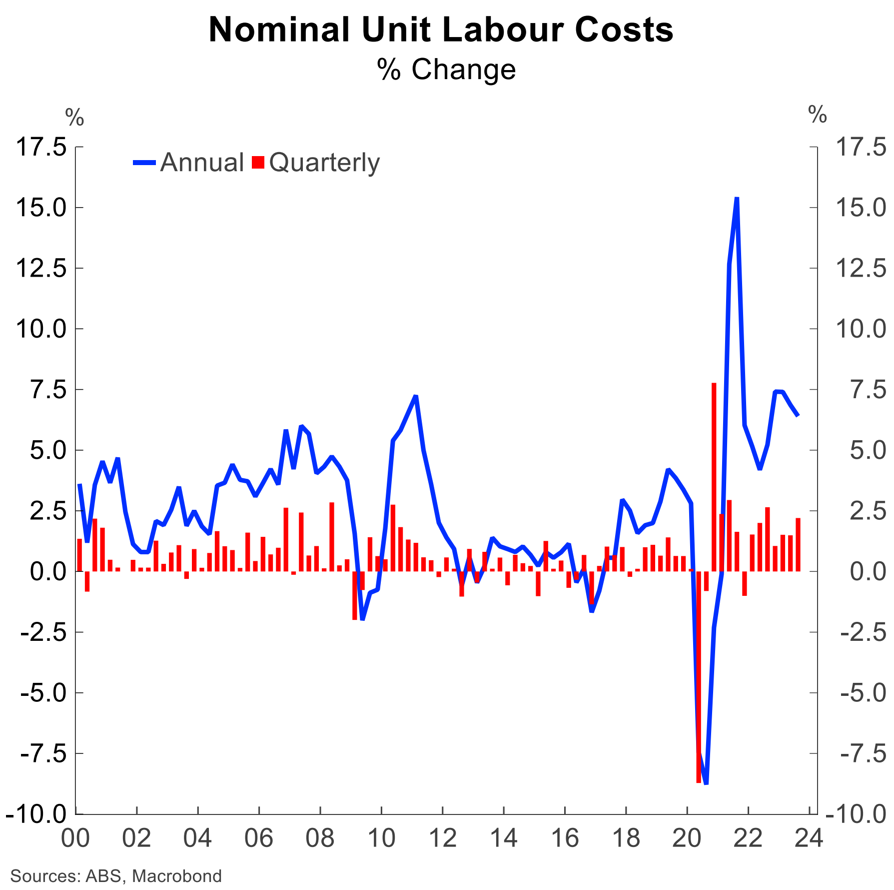
Sources: ABS, Macrobond

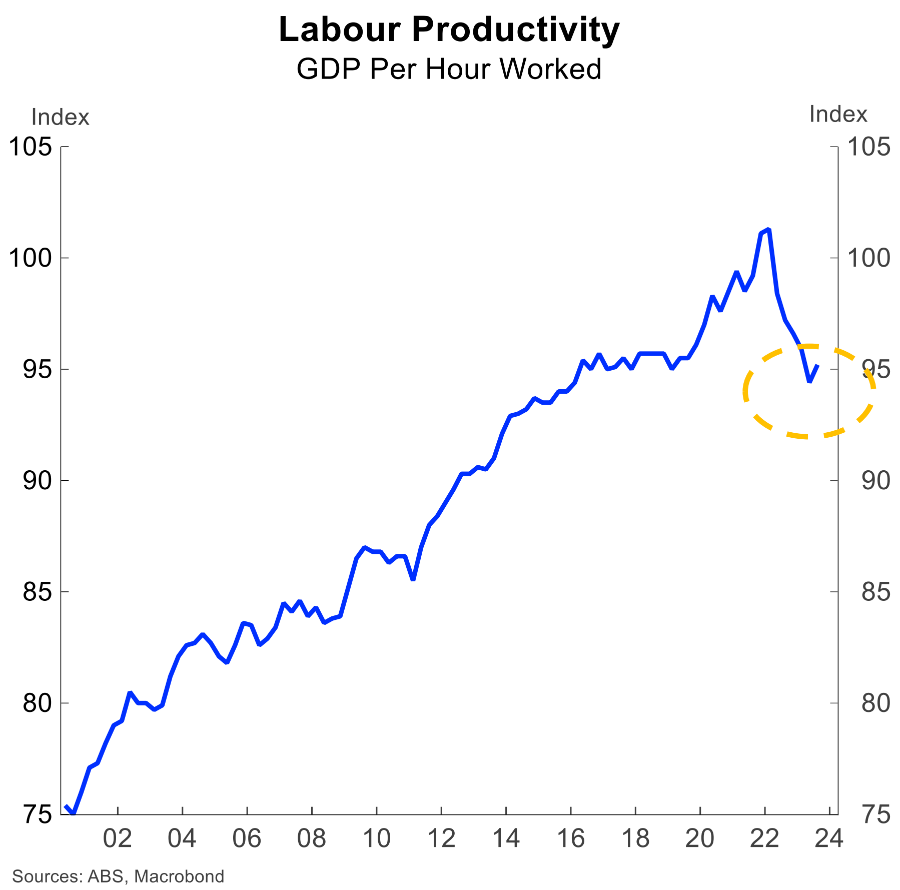
Earnings Providing Some Support



- Total compensation of employees (CoE i.e. total wages) grew 2.5% in the quarter. This represents an acceleration from the 1.6% recorded in the June quarter.
- The growth over the quarter was driven by a 3.1% increase in earnings per hour worked – outside of COVID this was the strongest quarterly increase since the December quarter 2000. The strong outcome was supported by the Fair Work Commission 2023-24 award wage increase.
- The number of hours worked across the economy declined by 0.5% in the quarter, reflecting slightly softer labour market conditions.
- In annual terms, CoE rose 8.1% – down from the peak of 10.6% recorded in the September quarter 2022.

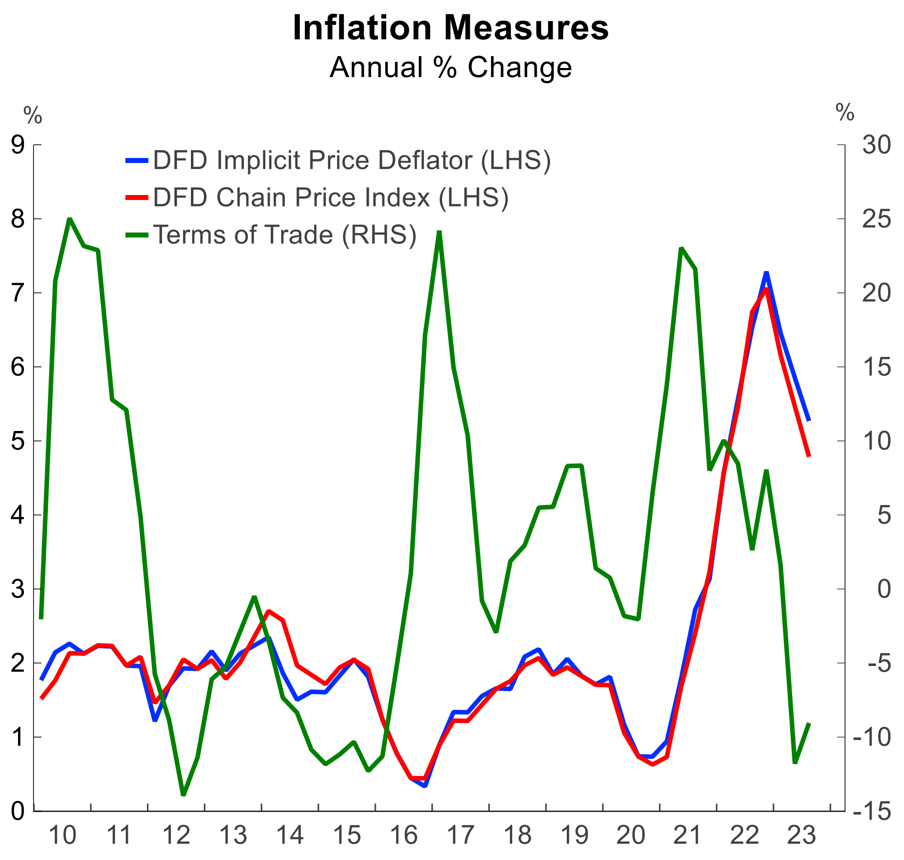
Measured Productivity Recovery Underway





- Quarterly growth in unit labour costs – wages adjusted for productivity – accelerated in the quarter reflecting higher earnings per hour. However, in annual terms unit labour costs are moderating.
- A fall in hours worked in the quarter marked the start of the anticipated normalisation in measured productivity outcomes.

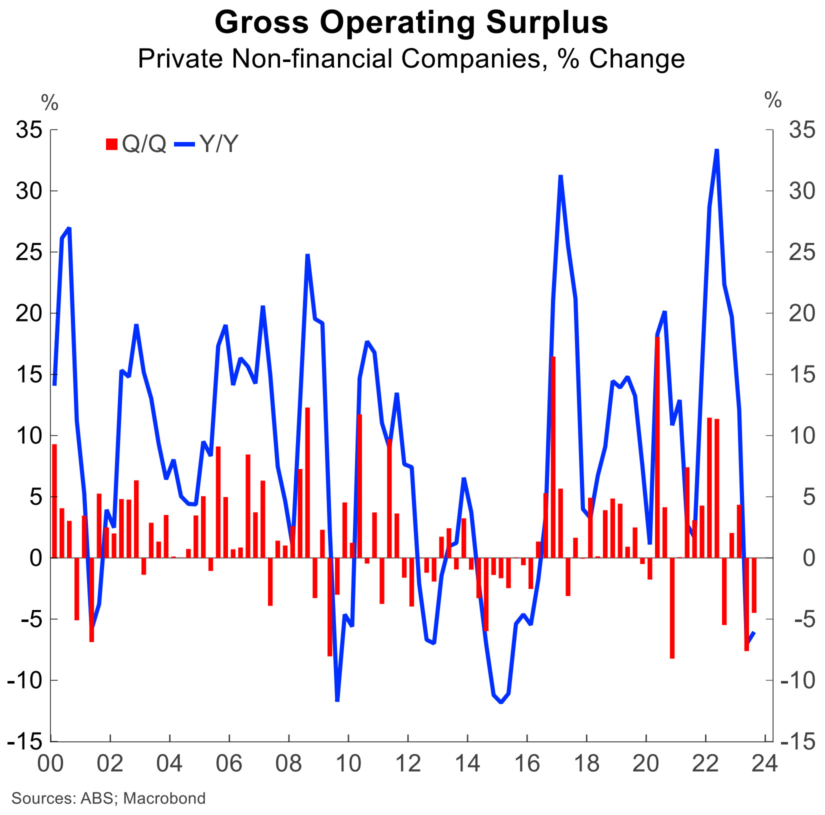
Domestic Inflation Measures & Terms of Trade

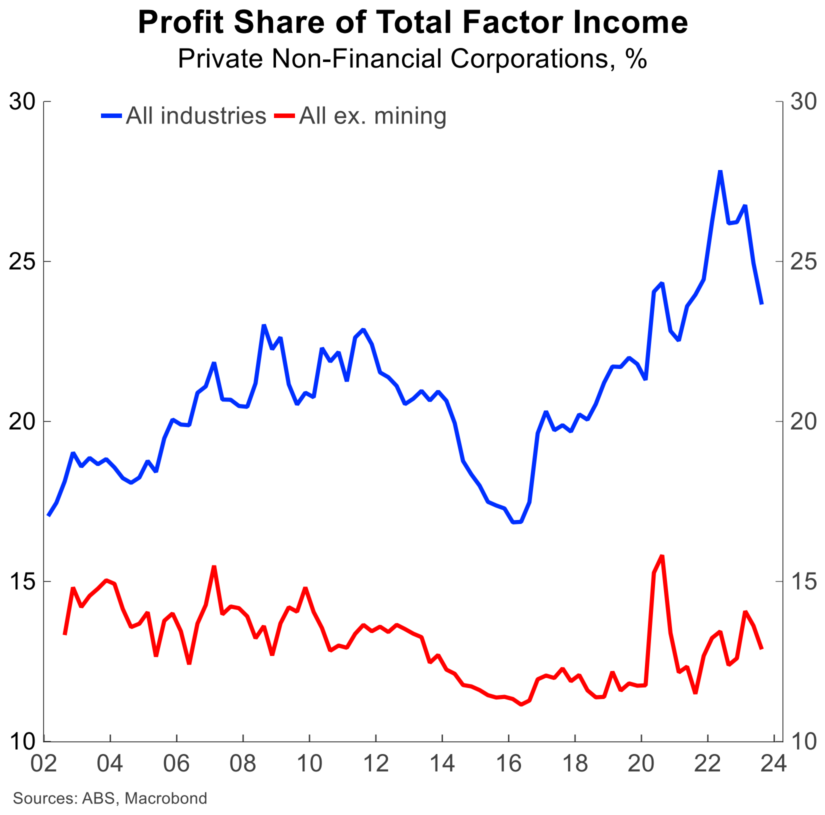


Sources: ABS, Macrobond

- Domestic price pressures continued to gradually ease.
- However, domestic measures of inflation found some renewed momentum in quarterly terms, validating the RBA's concerns around 'homegrown' inflation.
- The **Domestic Final Demand (DFD) Implicit Price Deflator**, which measures domestic price changes but also the effects of compositional changes in DFD, rose 1.3% in the quarter and 5.3% in the year.
- The **DFD Chain Price Index**, which removes the impacts of compositional changes and is a pure measure of domestic prices changes only, rose 1.4% in the quarter. Annual growth eased from 5.5% to 4.8%.
- The terms of trade (i.e. ratio of export to import prices) fell further, led by significant declines in commodity prices. The ToT slipped 2.6% following a 7.9% fall in the June quarter. In annual terms, the ToT dropped 9.0%.

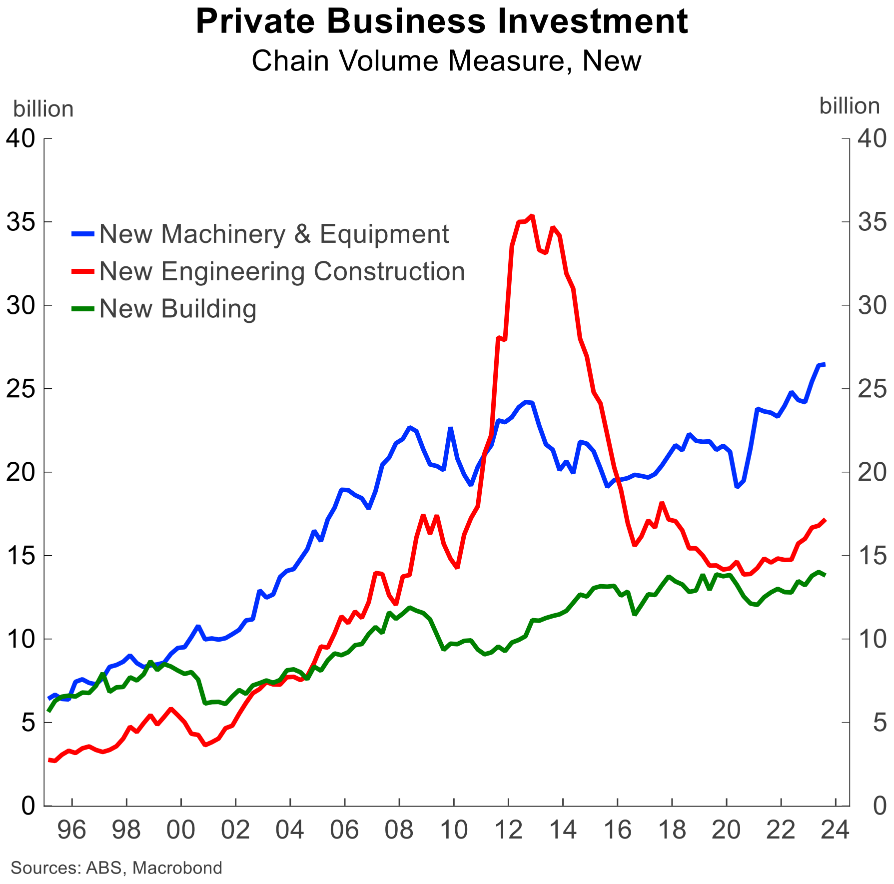
Weak Profits Concentrated in Mining





- **Gross operating surplus** (i.e. profits) for non-financial corporations fell 4.5% in the quarter, to be 6.0% lower over the year. This was driven by a 6.5% drop for mining companies as commodity prices fell. Specifically, coal and gas prices declined in the quarter, which was partly offset by higher iron ore prices.
- Conversely, profits for non-mining non-financial corporations rose 0.3%, to be 8.1% higher over the year.

Business Investment Eases, Mining Drives Gains



- Businesses are rebuilding capital stocks to accommodate the larger population. This is being supported by easing global supply chain disruptions.
- New private business investment grew 0.6% over the quarter to be 8.0% higher over the year. This was led by mining investment, which rose 9.6% in the quarter. Non-mining investment slid 1.0%, partly unwinding the 1.5% gain in the previous quarter.
- Investment in new machinery and equipment grew by 0.2% to be 8.8% higher than a year ago. This was boosted by the improved availability of motor vehicles and other equipment.
- New engineering construction increased 2.3% but remained 9.3% higher than a year ago. Large transfers to the public sector impacted the quarterly outcome.
- New building construction fell 1.5% over the September quarter to be 2.5% higher than a year ago.

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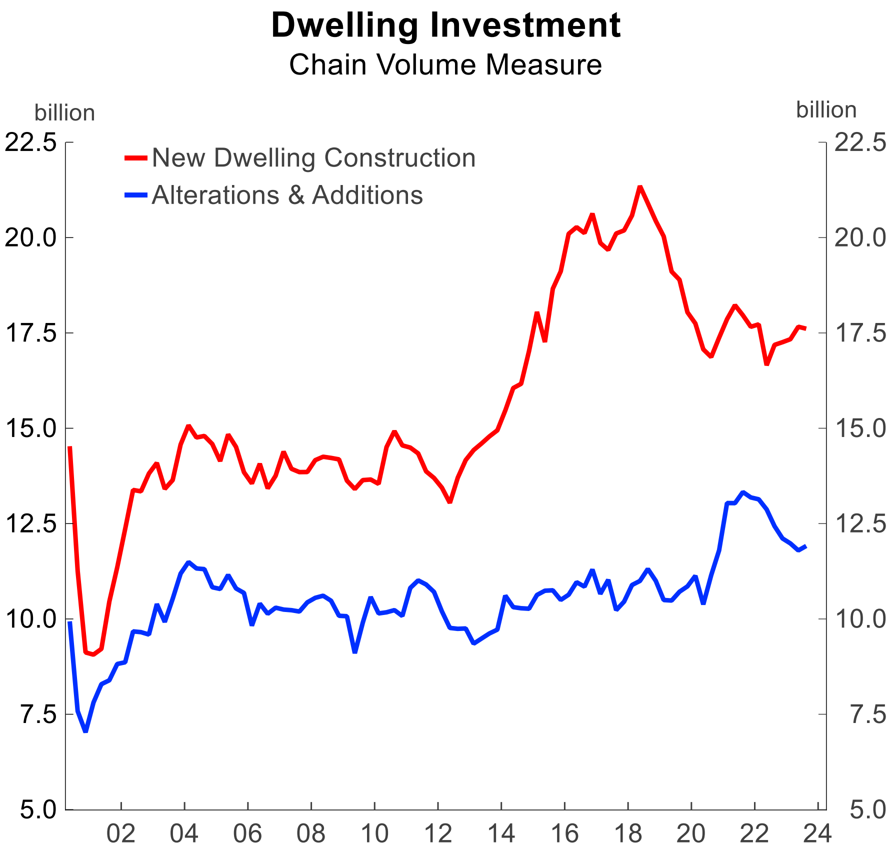
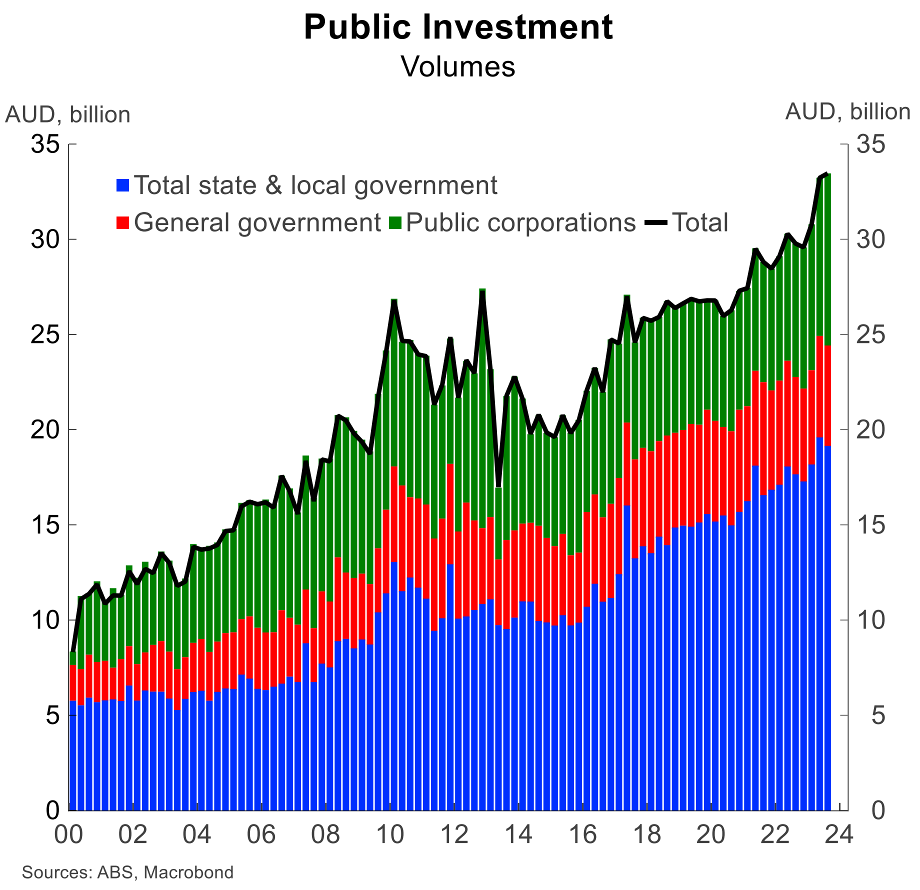
Housing Investment Still in the Doldrums



Sources: ABS; Macrobond

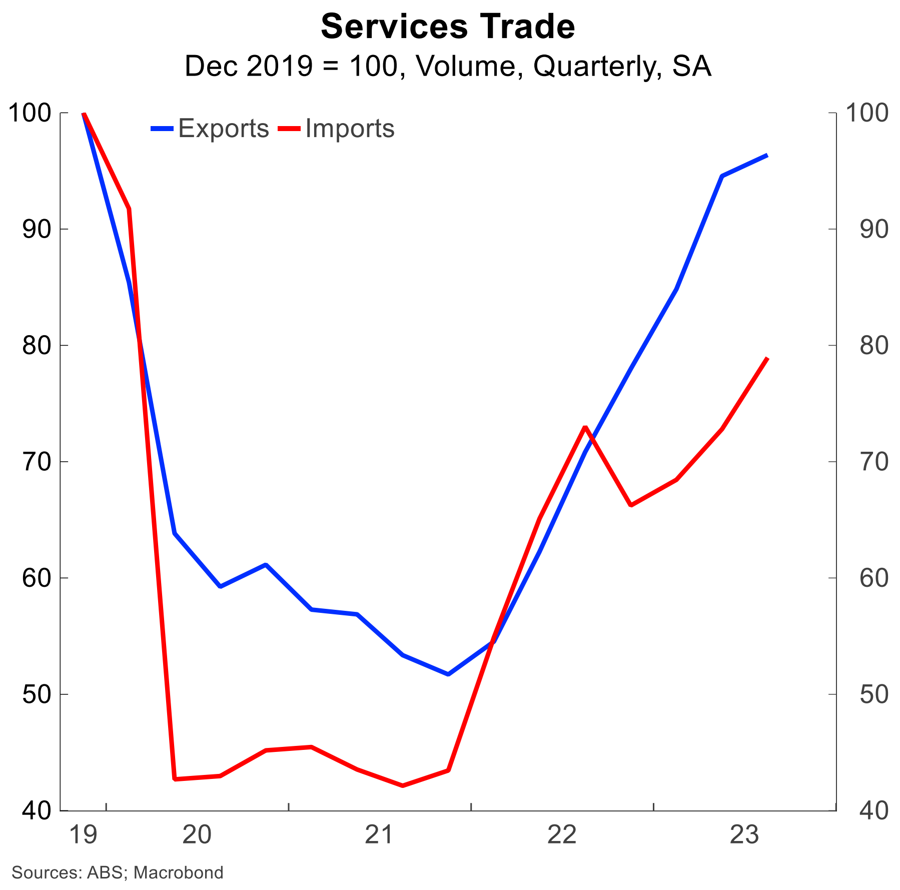
- The construction sector is facing a raft of challenges that have impacted dwelling investment. This is despite a strong existing pipeline of projects accumulated following the surge in building approvals during the pandemic period.
- Activity in the sector rose 0.2% in the quarter but remains subdued. Elevated costs, including materials and labour, in addition to weather and other factors have impacted work.
- Investment in new dwellings slid 0.3% but was 2.5% higher in annual terms.
- Renovation activity rebounded by 1.0% in the quarter but was 4.2% lower than a year ago.
- There have been some early signs that forward indicators, such as approvals, are stabilising at weak levels. However, the supply picture remains a challenging one, as the supply response is expected to come with a larger lag than previous cycles.

Public Investment the Strongest Since 2018



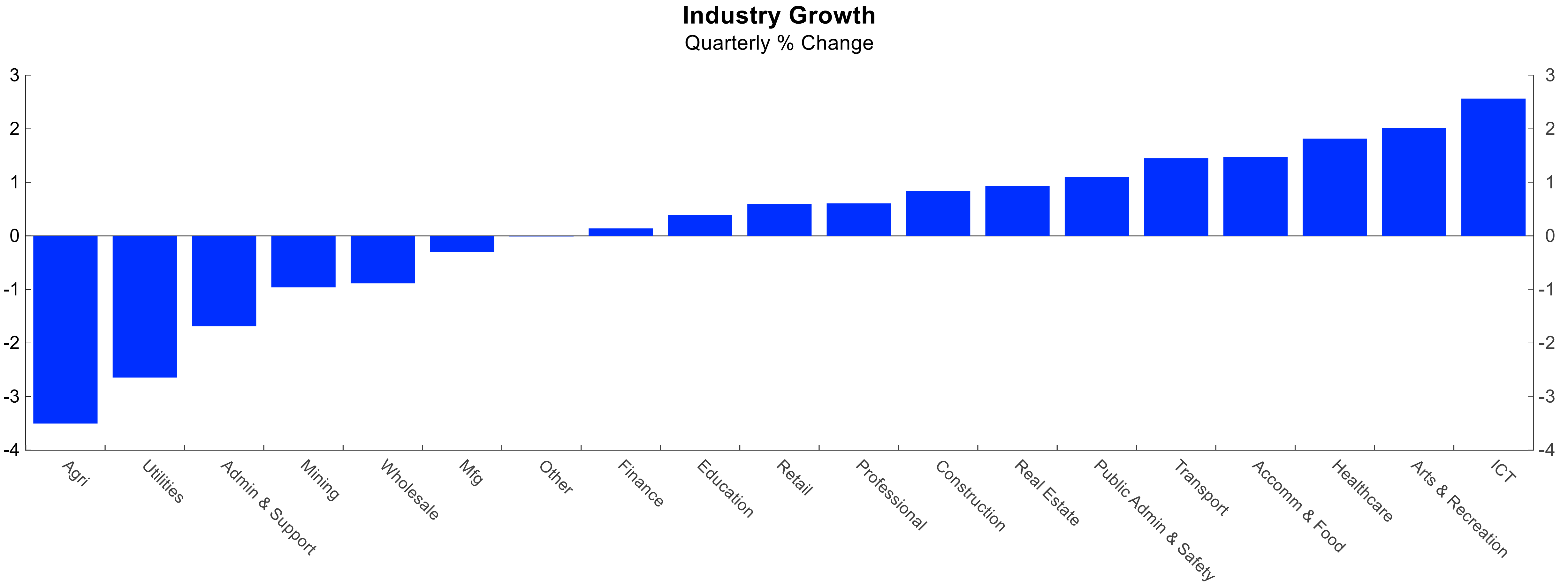
- Public demand increased by 1.4% in the September quarter – this was driven by both investment and consumption.
- New public investment increased 2.8% over the September quarter to be 11.6% higher in annual terms – the strongest since the March quarter 2018.
- The pipeline of infrastructure projects at the state and federal level will continue to support investment. The pipeline includes projects such as Snowy 2.0, the Western Sydney Airport, Inland Rail, Sydney's new metro and Brisbane's Cross River Rail.
- Public consumption also expanded 1.1% in the quarter, driven by an increase in state and local government (1.2%) and national government consumption (1.1%) – this included social benefits to households, such as the energy rebates.
- New public demand added 0.3 percentage points to growth.

Slowing Global Growth Weighing on External Sector



- The external dragged on growth in the September quarter, as import growth outstripped exports.
- **Net exports** detracted 0.6 percentage points from growth.
- **Exports of goods and services** fell 0.7% in the quarter, largely driven by a fall in our major commodity exports.
    - Services exports continued to grow, though at a milder pace, increasing 1.9% in the quarter. Tourism-related exports (in value) are now 5% above pre-pandemic levels, underpinned by a record inflow of international students.
    - Goods exports slid 1.2% in the quarter.
- **Imports of goods and services** grew strongly, rising 2.1%.
    - Our affinity for travel continued, driving an 8.4% quarterly jump in services imports. However, services imports remain around 21% below pre-COVID levels.
    - Growth in goods imports was less impressive, rising a modest 0.5%. This reflects slowing but resilient demand.

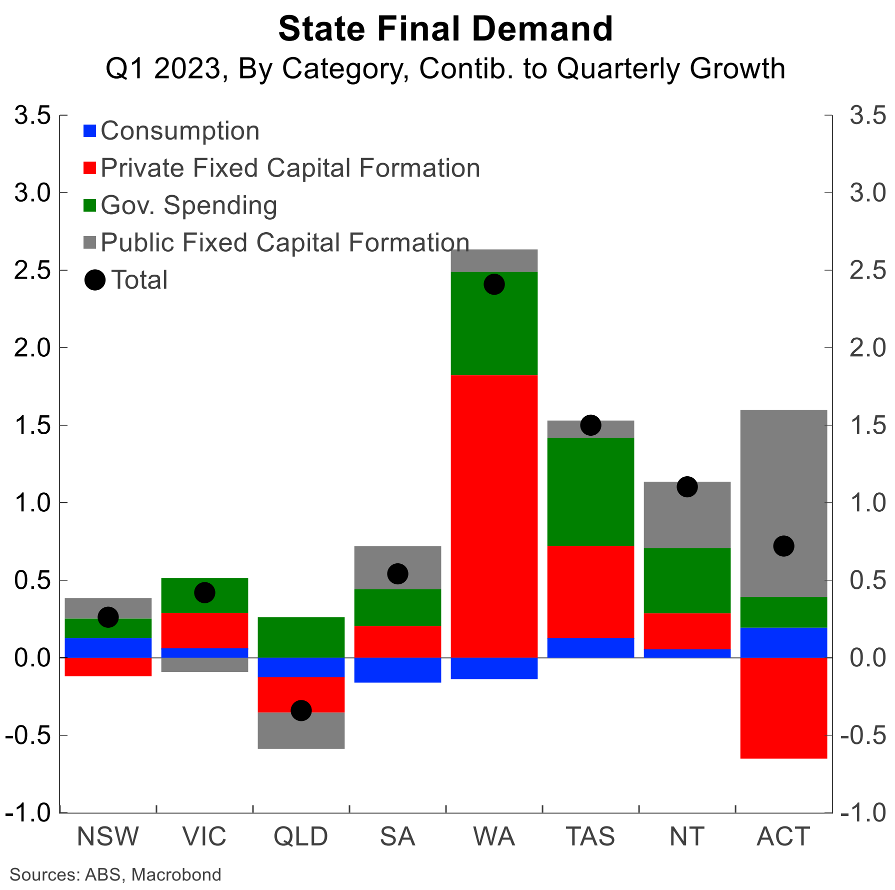
GDP Production Measure - GDP(P)



Sources: ABS; Macrobond

- 12 of 19 industries grew in the September quarter, down from 15 in the previous quarter.

States Picture



- Activity was broadly positive across the states and territories with the exception of Queensland.
- WA and Tasmania recorded the strongest quarterly growth at 2.4% and 1.5%, respectively. Both economies were supported strongly by business investment and government spending.
- Public spending contributed positively to growth across all states and territories. Stronger government spending was underpinned by social benefits to households, including the Energy Bill Relief Fund rebates, and extra payments for childcare, aged care and pharmaceutical products.
- Private investment was mixed. Dwelling investment dragged on activity in most states, save NSW and Victoria. Business investment expanded in WA, Tasmania, the NT, SA and Victoria but fell in NSW, Queensland and the ACT.
- Growth in household consumption was muted or negative in the September quarter, reflecting the pressure on household incomes. The ACT, NSW and Tasmania recorded the strongest increase in household consumption.

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