

Economic Update

August 2018

By David Martine, Secretary, Department of Treasury and Finance.
This monthly newsletter outlines economic and financial developments.

Highlights

- ▶ Economic indicators released over the past month point to strong economic conditions in Victoria
- ▶ The value of Victoria's retail trade increased by 3.7 per cent over the year to May
- ▶ The Victorian consumer sentiment index rose 4.0 per cent to 109.2 in July, and is up 12.2 per cent over the year
- ▶ The NAB business confidence index for Victoria fell in June, while business conditions were unchanged
- ▶ The number of dwelling units approved was up 18.6 per cent over the year to May
- ▶ The US unemployment rate rose slightly to 4.0 per cent in June



Domestic developments

According to the July edition of the CommSec State of the States report, Victoria was the best performing economy due to strong population growth and construction activity. Victoria ranked first among the other States and Territories on economic growth, population growth, dwelling starts and construction work done, and exceeded the national average on six of eight indicators. Victoria was ranked second on retail spending and housing finance, and fourth in equipment investment and unemployment.

Inflation in Melbourne – measured by the consumer price index – rose 0.4 per cent in the June quarter, contributing to a rise of 2.5 per cent over the year. The June quarter result was driven largely by price rises across health (1.8 per cent), alcohol and tobacco (1.7 per cent) and transport (1.4 per cent), offsetting falls in communication (-1.3 per cent) and recreation and culture (-0.8 per cent).

Victorian employment fell 6 600 in June but was up by 60 100 (or 1.9 per cent) over the year. Despite the decline in total employment over June, full time employment grew by 20 400, driving an increase in hours worked.

Victoria's unemployment rate rose by 0.5 percentage points to 5.6 per cent in June. The unemployment rate has declined by 0.4 percentage points over the year but remains above the national average of 5.4 per cent.

Victoria's participation rate increased by 0.1 percentage points to 65.7 per cent in June but is 0.5 percentage points lower over the year. The annual decline has been driven by both female and male participation, which are down 0.2 and 0.8 percentage points respectively.

Victoria's regional employment increased by 4 200 persons in the three months to June. Rising employment in Shepparton, Bendigo and Ballarat was partly offset by declines in Warrnambool and South West, North West and Geelong.

The unemployment rate in regional Victoria decreased by 0.8 percentage points to 4.9 per cent in the three months to June, and is below the Australian regional average of 5.7 per cent.

The value of Victoria's retail trade increased by 0.2 per cent in May and 3.7 per cent over the year. The annual result was the highest growth among the mainland states. The key drivers

of growth in May were 'department stores' and 'clothing, footwear and personal accessories', which were partly offset by declines in 'cafes, restaurants and takeaway food' and 'other retailing'. Retail volumes grew 0.9 per cent in the March quarter and 4.8 per cent over the year.

The Westpac-Melbourne Institute consumer sentiment index for Victoria increased 4.0 per cent to 109.2 in July and is up 12.2 per cent over the year. The index has been above 100 for 11 of the last 12 months.

Three of the five component indices for Victoria increased in July. The largest increase was recorded in 'Family Finance vs a Year Ago' which rose by 20 per cent, while 'Economic Conditions in Next 5 Years' increased by 8.1 per cent and 'Time to Buy Major Household Items' increased by 3.8 per cent.

The national consumer sentiment index rose 3.9 per cent in July to 106.1, and is up 9.8 per cent over the year. Westpac noted that the latest national reading is the most positive result since November 2013, but remains below pre GFC levels.

The NAB business confidence index for Victoria fell by 2 points to +3 index points in June, 4 points lower than a year ago. The Victorian business confidence index is below the 2017 average of +7.5 points. Victoria's business conditions index was unchanged at +14 index points in June. Although this was 1 point lower than a year ago, business conditions remain comfortably in positive territory (slightly below the average level of +15.9 points recorded in 2017).

AiG's Performance of Manufacturing Index (PMI) for Victoria fell by 8.5 points to 47.2 points in July (a value below 50 indicating contraction). The July result followed 17 months of expansion in the sector.

The total value of building approvals increased by 9.0 per cent to \$3.45 billion in May 2018, and is up 17.4 per cent over the year. The number of dwelling units approved rose by 0.3 per cent in May, and is up 18.6 per cent over the year. The number of dwelling unit approvals in Victoria has been the highest among the states for seven of the past eight months. Nationally, the number of dwelling unit approvals fell by 3.2 per cent in May, in contrast to market expectations of flat growth.

The Melbourne CoreLogic Home Value Index decreased 0.9 per cent in July, and was down 0.5 per cent over the year, marking the first annual decline in Melbourne since late 2012. This compared to national annual falls of 2.4 per cent, driven largely by a fall of 5.4 per cent in Sydney (the second weakest capital city market behind Darwin). The national index (combined capitals and regional areas) has now fallen for ten consecutive months.

The Melbourne sub-index for houses fell 1.0 per cent in July, and 1.4 per cent over the year. The sub-index for units fell 0.7 per cent in July, but remained 2.3 per cent higher over the year.

The RBA left its policy rate unchanged at 1.5 per cent in July. It noted that non mining business investment, and public infrastructure investment had contributed strongly to economic growth over early 2018, although the outlook for consumption was a source of uncertainty, given that household income had continued to grow slowly and debt levels remained high.



Global developments

Key global economic indicators improved in the month, confirming a further strengthening in global economic conditions.

Real gross domestic product in the United States (US) grew 4.1 per cent in annualised terms in the second quarter of 2018, up from a revised 2.2 per cent in the first quarter. The second quarter increase reflected increases in consumer spending, exports, business investment, and government spending, which each grew 4.0, 9.3, 5.4 and 2.1 per cent in annual terms, respectively. This growth was partly offset by falls in housing investment (-1.1 per cent), and imports (0.5 per cent).

Non farm payrolls in the US increased by 213 000 persons in June, following an upwardly revised 244 000 in May — well above market expectations of 195 000. Job gains occurred in professional and business services, manufacturing, and health care, while employment in retail trade fell. The US unemployment rate rose 0.2 percentage points to 4.0 per cent in June.

The RBA noted in its minutes of the July Board meeting that long-term government bond yields in a number of major markets declined slightly over June, partly reflecting risks to

international trade. Nonetheless, long term US bond yields remained higher than at the end of 2017, reflecting strong economic growth and expectations of rising inflation and monetary policy tightening in the US.

The unemployment rate in the Euro Area was 8.4 per cent in May 2018, unchanged from April's revised figure and down from 9.2 per cent a year earlier. The unemployment rate in May was at its lowest level since December 2008.

China's annual consumer price inflation was 1.9 per cent in June, in line with market expectations, while producer price inflation was 4.7 per cent over the year to June, the highest since January. The Chinese Caixin manufacturing PMI fell 0.1 percentage points to 51.0 points in June, slightly below market expectations of 51.1.

Note: Data reported in the newsletter are current as at 31 July 2018.

Chart 1: Movements in financial data over the past month

	29-Jun-18	31-Jul-18	Change
AUD/USD	0.739	0.743	0.5%
ASX 200	6 194	6 280	1.4%
S&P 500	2 718	2 816	3.6%
90-day bank bill rate*	2.12	1.97	-0.15
10-year Commonwealth bond rate*	2.63	2.65	0.02

Notes: Changes are based on the movement in unrounded figures.

* Changes are calculated as percentage points.

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