Data Snapshot

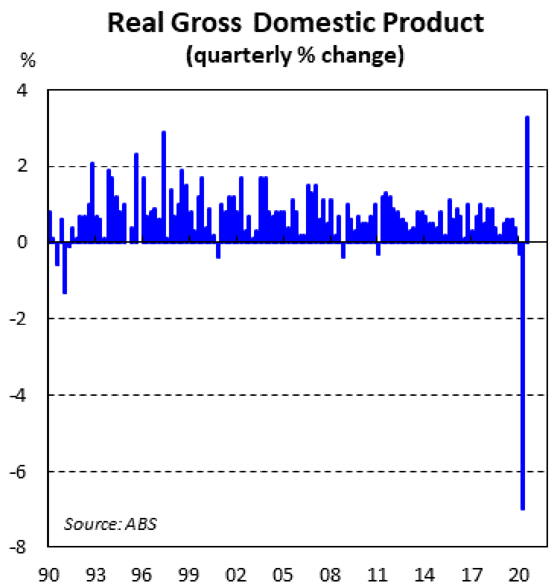
bankSA

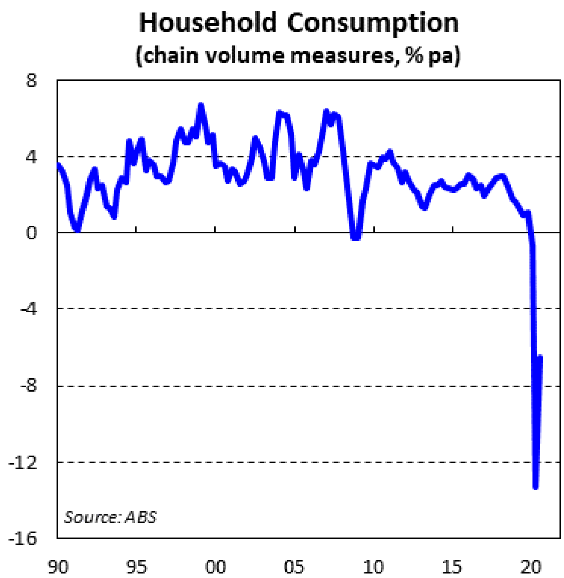
Wednesday, 2 December 2020

National Accounts - GDP

The COVID Recession Recedes

- **The Australian economy expanded 3.3% over the September quarter. The recession may be technically over, but the pain and disruption remain.**
- **Consumer spending led the rebound in economic activity. Household consumption surged by a record 7.9% in the September quarter after a record plunge of 12.5% in the June quarter.**
- **A recovery is underway in Australia and today's data confirms this, but Australia remains in the grips of the pandemic. Without significant stimulus from the Federal government, State governments and the central bank, the economic picture would no doubt have looked far uglier.**
- **The recovery in the September quarter was held back by Victoria's second wave of infections and the associated second lockdown. Victoria was the only State to not recover in the September quarter. NSW and Queensland experienced the strongest comebacks. Queensland also wins another award - it was the only State to fully regain the economic output lost over the first half of this year.**
- **Caution remains. The household saving ratio, shot up to 22.1% during the June quarter and has only fallen back to 18.9% in the September quarter. On the flip side, it suggests that Australian consumers have significant 'firepower' for when they are ready to spend or invest.**





Key Themes & Summary:

The year 2020 will not be easily forgotten. It sounds like a cliché but it's true. It will take 101 years before there is another year where the first two digits are the same as the second two digits. It hopefully will take this long or more before we see a black-swan event of this nature.

The pandemic has delivered a massive shock to economies around the world. Lockdowns and restrictions have ensued.

The Australian economy entered a severe recession in the first half of this year. It was the first recession in nearly 29 years, ending an enviable recession-free run. Gross domestic product (GDP) declined 0.3% in the March quarter and by a record-sized 7.0% in the June quarter.

GDP recovered 3.3% in the September quarter, close to our forecast of 3.0%, as the economy emerged from a national lockdown and some restrictions were relaxed. It is the biggest quarterly growth rate since early 1976! But it still leaves economic output 4.2% lower than at the end of 2019 and it will take at least another year to return to pre-pandemic output levels.

Consumer spending led the rebound in economic activity. Household consumption surged by a record 7.9% in the September quarter after a record plunge of 12.5% in the June quarter. Spending on services steered the increase in consumption, especially spending on eating out and domestic holidays.

A recovery is underway in Australia and today's data confirms this, but it is clear Australia remains in the grips of the pandemic. Without significant stimulus from the Federal government, State governments and the central bank, the economic picture would no doubt have looked far uglier. The household savings ratio tells the story.

The household savings ratio shot up from 5.3% in the final quarter of last year to a record high of 22.1%. It came down to just under 19% in the September quarter, but remains incredibly elevated. It tells us that consumers remained cautious in the September quarter, reflected in elevated savings and a desire to continue repairing household balance sheets. Businesses also remained in their shells, not even poking a head out. Business investment again in the September quarter, taking the string of quarterly falls to six.

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The recent news around an effective vaccine is encouraging. If this vaccine can be effectively deployed, then the economic recovery will gather momentum next year. For now, the economic recovery remains lopsided, fragile and bumpy. The economy also remains reliant on policy stimulus; without it the economy could stumble.

GDP Expenditure Measure:

Economic activity picked up in the September quarter as COVID-19 related restrictions were eased across most States and territories. The lifting of restrictions flowed through to solid gains in household spending and a pick-up in investment in dwellings. Government spending also rose, adding to the overall economic recovery.

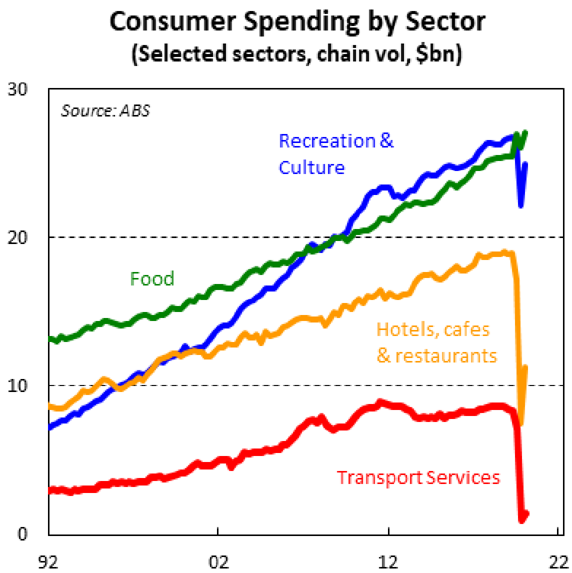
Household consumption rose 7.9% in the quarter, the largest quarterly increase since the series began in 1959. This followed the largest ever decline, of 12.5%, in the previous quarter. Household consumption fell 6.5% over the 12 months to the end of September 2020, a third successive decline, something never seen before in the history of the series. The extent and duration of the decline in consumer spending during the pandemic provides a good indicator of the severity of the 2020 recession.

There were large swings in spending between the June and September quarters. Spending in hotels, cafes & restaurants fell 56.3% in the June quarter then rebounded 49.7% in the September quarter. While this looks impressive, it still leaves spending in that sector well down on pre-pandemic levels.

Spending on recreation and cultural activities fell 15.9% in the June quarter but then rose 12.8% in the September quarter. Again, this leave the sector well below pre-pandemic levels of activity and reflects the impact of restrictions on gatherings and social-distancing rules.

Sectors that saw a decline in spending in the September quarter included alcoholic beverages (-0.5%) and furnishings and household equipment (-0.9%). Both sectors recorded very substantial increases in spending at the height of the pandemic in the June quarter, possibly reflecting rising stress in the community and people setting themselves up to work from home.

Communications was one area of household spending that grew throughout the recession. It grew 2.2% in the March quarter, 1.6% in the June quarter and then a further 1.2% as the economy moved out of recession in the September quarter. Given the various state lockdowns and increased use of personal video 'conferencing' and internet usage, such figures should not come as a surprise.



A disappointing, but understandable, aspect of the national accounts was the weakness of business spending. Total private business investment fell 3.0% in the September quarter and has now fallen for four consecutive quarters. Prior to the pandemic, business optimism was modest with businesses questioning the source of future demand. When the pandemic struck, many businesses went into survival mode with new investment projects placed on the backburner.

With the Federal Budget announcing incentives to bring forward business investment it is hoped that projects will come off the backburner and put into action. According to the survey recently published by the Australian Bureau of Statistics (ABS) capex spending plans for 2020-21 remain weak with an 8.0% decline expected.

Business investment in the September quarter 2020 was down 9.2% on the September quarter 2019.

New dwelling investment posted a modest 0.6% rise following eight quarters of declines but remains 7.6% down on the September quarter 2019. With interest rates now at historic lows and not set to rise for at least three years, some pickup in dwelling invest is likely. Recent figures on building approvals suggest that the trough in dwelling construction is behind us, however, slow population growth would act as a headwind.

Government consumption spending rose a solid 1.4% in the September quarter following a 3.0% rise in the June quarter. The increase in government consumption over the year was 7.8%, the largest annual increase since the June quarter 1985.

As in the March and June quarters, government consumption spending was boosted by its response to COVID-19. Government consumption spending in the September quarter was strongest in the Northern Territory (4.0%), Victoria (3.2%) and NSW (2.2%).

As suggested above, overall, demand in the economy rose significantly. **Domestic demand** was up 4.5% in the September quarter, the largest quarterly increase since the series began in 1959. These are very encouraging numbers, but there is still some way to go before demand reaches its pre-pandemic levels.

Selected Expenditure Items on GDP, Chain Volume Measures

	Quarterly % Change
Household Consumption	7.9
Public Consumption	1.4
Dwelling Investment	0.6
Business Investment	-3.0
Public Investment	0.3
	Contribution to GDP, ppt
Inventories	0.8
Net Exports	-1.9

Net exports detracted from growth in the September quarter. Exports of goods and services fell 3.2% while imports rose 6.5%. Exports of goods and services have fallen for four consecutive quarters. Exports of travel services fell 16.7% in the quarter while there was a 5.9% decline in the exports of mineral ores. On the imports side, there was an 18.3% increase in textile, clothing and footwear imports and an 11.0% rise in imports of fuel & lubricants.

Exports of goods and services were down 14.9% on the September quarter 2019 while imports of goods and services were down 13.9%.

GDP Income Measure:

When excluding the impact of prices, GDP based on income measures rose by 3.5% in the

September quarter, after a record drop of 7.2% in the June quarter.

Nominal GDP, as measured by incomes rose by 3.7%, the largest increase in 10 years. The annual rate improved in the September quarter but still contracted. The annual rate moved from a decline of 6.2% in the June quarter to a fall of 3.9% in the September quarter.

Employee wages (compensation of employees) recovered 2.3% in the quarter, after a loss of 2.3% in the June quarter. A bigger bounce back has not been recorded for more than 8½ years.

An indication of how much work was done in the quarter is provided by the **hours worked** measure, which rose 4.4% after falling by a whopping 10.1% in the June quarter. It highlights the significant impact of JobKeeper, and other government measures are playing in supporting household incomes.

Government support also boosted company incomes through subsidies, with **profits** from private non-financial corporations lifting 3.8% in the quarter after a near-record rise of 18.7% in the June quarter. The increase in profits was driven by non-mining companies. Mining companies were especially hurt by the falls in prices and demand for coal and LNG.

Nonetheless, the “increase” in company profits was offset by a 50.9% fall in taxes less subsidies on production and imports. This fall follows the enormous fall of 118.3% in the June quarter. Subsidies paid out to firms were more than the tax intake over the quarter for only the second time on record. The first time was last quarter!

The increase in government assistance has been substantial. Household incomes have been supported by social assistance and initiatives such as the early access to superannuation. Consumers have increased spending in the September quarter but not by running down household savings significantly. These behaviours are reflected in a **household savings ratio** that has declined only slightly in the September quarter to remain very elevated at 18.9%. It was at a record high of 22.1% in the June quarter. If we exclude the June quarter, September quarter’s result is the highest since the mid-1970s when the world and Australia were in recession, triggered by a worldwide oil crisis and the collapse of the Bretton Woods system.

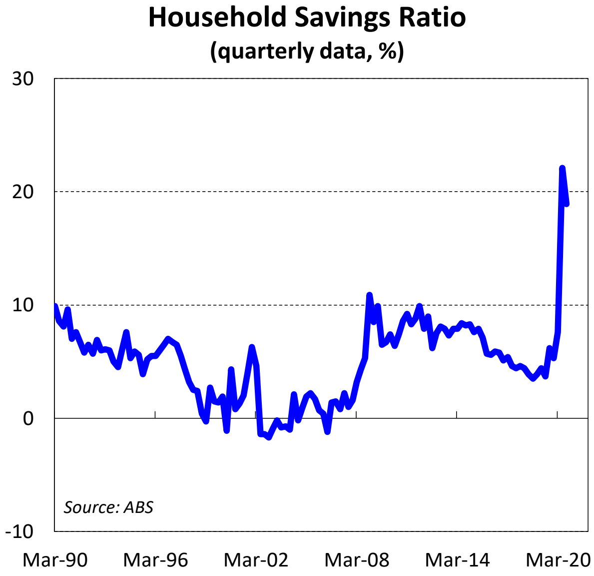
Consumer spending is likely to improve over the following year, but some caution is likely to cling to consumers whilst uncertainty remains high and a vaccine is yet to be distributed. Furthermore, social-distancing and international-border restrictions will continue to hurt spending until they lift. When concerns regarding the pandemic subsides further, the support to incomes will encourage a faster recovery and bring down unemployment quicker.

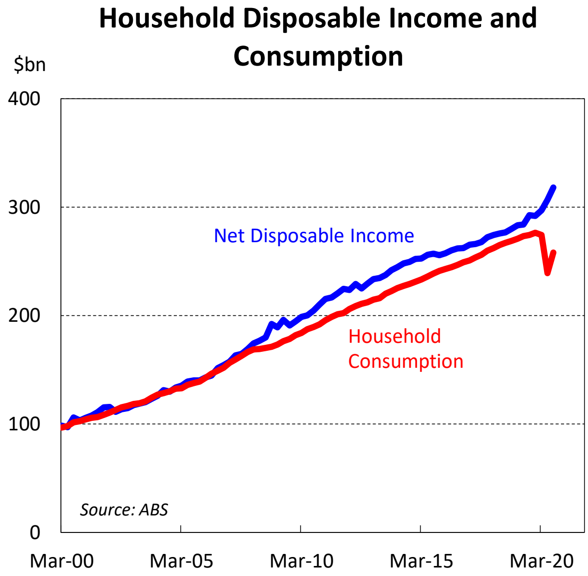
The **terms of trade** (or the ratio of export prices to import prices) lifted 0.7% in the September quarter, which is the third consecutive quarter of improvement. An improvement means there is a net transfer of income from the rest of the world to Australia. This boost to income helps support economic activity.

Most commodity prices recovered through much of the September quarter, following a recovery in the June quarter, reflecting major economies emerging from their first lockdowns earlier in the year. Some of these economies experienced another wave of infections near the end of the quarter and re-entered lockdowns or imposed fresh restrictions. Prices of iron ore have been especially resilient. They have risen by an average of 27.4% in the September quarter and are currently trading at nearly US$129 a tonne – the highest since early 2014.

A strong V-shaped recovery in China and spending on infrastructure has been extremely supportive for demand of commodities, particularly for iron ore. However, the deterioration in the relationship between the Australian and Chinese governments has hurt several agricultural commodities and there is a risk the net widens.

On a year ago, the terms of trade index is weaker, despite the string of recent improvements. It is down 2.5%, which is only a slight improvement from the annual contraction of 2.6% recorded in the June quarter.





State Final Demand:

All States and territories recorded growth in the September quarter, except Victoria, where strict lockdown restrictions were put in place to combat the second wave of infections. Growth mainly stemmed from strong increases in household consumption, although capital formation and government consumption also contributed to final demand in some States and territories.

New South Wales and Queensland recorded the strongest growth rates in the quarter (6.8% each), as restrictions in these states were eased and new infections were successfully controlled. In both States, household consumption was the main driver of growth, rising 10.8% in NSW and 11.6% in Queensland. These strong results reflect the rebound in spending in areas including hotels, cafes & restaurants and recreation and culture. Government consumption spending and private capital formation continued to support growth in NSW, rising 2.2% and 1.6% in the September quarter, respectively.

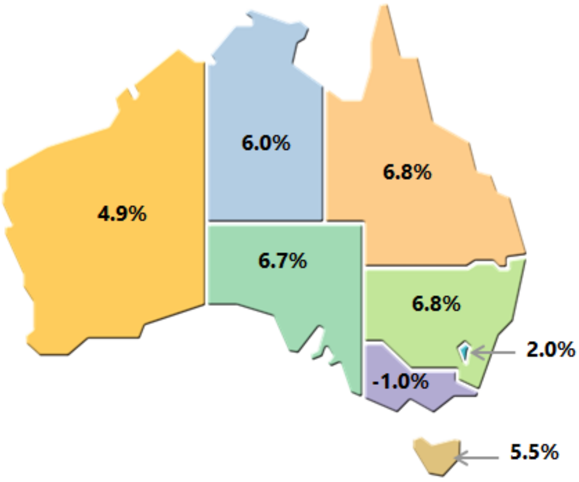
South Australia recorded a 6.7% increase in final demand in the September quarter. Like NSW and Queensland, growth was mainly driven by household consumption (11.0%). After an extraordinary decline in the June quarter, final demand for the services of hotels, cafes & restaurants soared 62.4% with the easing of COVID-19 restrictions.

The Northern Territory recorded a 6.0% increase in state final demand in the September quarter, driven by strong public and private capital formation. Work done in regional areas was the main contributor to the 7.7% increase in public capital formation. For private capital formation (+6.2%), non-dwelling construction and machinery & equipment demand were the main drivers.

Tasmania recorded a growth rate of 5.5% in the September quarter, partially offsetting the sharp 8.0% fall in the June quarter. The pattern by sector was similar to other States and territories with household consumption increasing 10.6% in the quarter. Spending in hotels, cafes & restaurants rose 86.1%, after a 62.7% tumble in the June quarter. Although private capital formation declined

2.0% in the quarter, public capital formation increased by 4.5%, driven by investments in energy infrastructure.

State Final Demand
(quarterly % change, September quarter 2020)



Source: ABS

Final demand in Western Australia rose 4.9% in the September quarter. Household consumption increased 11.7%, notably in health (40.6%) as elective health services resumed after the easing of restrictions. Private capital formation decreased 2.1% in the quarter, led by a 5.6% contraction in investment in machinery & equipment in the mining industry.

The ACT had the smallest increase in demand among the States and territories. Final demand rose 2.0% in the September quarter, after a mild 1.7% contraction in the June quarter. Household consumption expenditure rose 8.7% as COVID-19 restrictions eased. While public capital formation increased 4.4% in the quarter, mostly driven by infrastructure projects, private capital formation declined 11.4%. Reduced investment in construction and machinery & equipment were the underlying factors behind the contraction in private capital formation.

Victoria was the only State to register a contraction in the September quarter. Victoria has now recorded contractions in state final demand for four successive quarters. Final demand declined 1.0%, after the sharp 8.5% decline in the June quarter. Household consumption fell 1.2%, led by decreases in clothing & footwear, recreation and furnishings & household equipment. However, the fall in household consumption was partially offset by food expenditure, which rose 6.6% as households prepared for the second lockdown. Government consumption increased 3.2%, preventing final state demand from falling even more.

On an annual basis, the results were mixed. Unsurprisingly, Victoria recorded the weakest growth rate of all States and territories. The 9.8% fall over the year to September is the largest contraction recorded in Victoria. NSW recorded the second highest decline at 3.3%, closely followed by Tasmania (3.2% fall). South Australia, Western Australia and the Northern Territory recorded mild contractions at 0.8%, 0.7% and 0.1%, respectively. On the positive side, Queensland recorded a 0.7% increase relative to September 2019, although the fastest pace remained with the ACT at 3.6%.

Industry Break Down:

The lifting of restrictions during the September quarter was evident in the industry breakdown of activity shown in the table below. Accommodation and food services, and arts and recreation were the clear beneficiaries. Despite their remarkable rebounds during the September quarter, both sectors remain well below the levels of activity seen a year earlier. Both sectors appear to be candidates for further government attention and assistance in the new year.

Most industries reported growth during the September quarter, and those that contracted did so by relatively small amounts. However, on an annualised basis the situation is mixed with 14 of the 19 industry groups having contracted since the September quarter 2019.

When the Reserve Bank speaks of the recovery being uneven, the industry breakdown is one element of that description.

Industry Gross Value Added, Chain Volume Measures

Ranked by Quarterly % Change

By Industry Sector	Quarterly % Change	Annual % Change
Accomm & Food Services	41.0	-19.7
Arts & recreation services	14.7	-16.2
Healthcare	9.1	1.8
Rental, hiring & real estate services	7.7	-8.5
Info, media & telco	6.3	-2.1
Retail trade	5.6	2.6
Wholesale trade	4.7	-0.2
Transport, postal & warehousing	4.7	-19.9
Other services	4.1	-14.9
Manufacturing	4.0	-1.7
Professional, scientific & technical services	2.5	-2.2
Construction	2.2	-8.3
Public admin & safety	1.5	6.0
Elec, gas, water & waste services	1.0	-2.0
Administrative & support services & safety	0.8	-22.1
Financial & insur services	0.4	3.0
Education & training	0.2	0.9
Agri, forestry & fishing	-0.6	-8.7
Mining	-1.7	-2.3

Source: ABS

Contact Listing

Chief Economist
Besa Deda
dedab@banksa.com.au
(02) 8254 3251

Senior Economist
Hans Kunnen
hans.kunnen@banksa.com.au
(02) 8254 1316

Economist
Felipe Pelaio
felipe.pelaio@banksa.com.au
(02) 8254 0646