AUSTRALIA

ACTIVITY IS STILL CONSTRAINED

Australian growth is facing an undeniable slowdown, which is linked to the prolonged constraints on households as a result of rising prices and interest rates, as well as slowing demand from its Asian trading partners. Stubborn inflation is currently an obstacle to easing interest rates. On the other hand, the migratory influx is boosting a labour market which remains buoyant.

Australia's economic growth has slowed significantly since the end of 2022. GDP grew by +0.2% q/q in Q2 2024 for the third quarter in a row, with public spending as the principal contributor (+0.4pp if public investment is included), and +1.0% year-on-year, which is the lowest since Q1 2020 (or even since 1991, if we are to exclude the COVID-19 period). Demand continued to be adversely affected by rising inflation and interest rates, as illustrated by decreasing household consumption in Q2 (-0.2% q/q), against a backdrop of falling disposable income per capita and a drop in consumer confidence. In addition, after buoying activity in 2023, non-residential investment fell over the first two quarters of 2024 (-0.7%, followed by -0.8% q/q). Furthermore, during the first half of 2024, increasing imports contributed to the decline in the growth rate; while, more broadly, Australian foreign trade was grappling with falling prices in its commodity exports (iron, coal and gas) and with declining Japanese demand.

The short-term growth prospects are subdued. Nevertheless, the introduction of income tax cuts (from 19% to 16% and 32.5% to 30%, respectively, on the first two brackets) should prevent consumption from reducing further during the second half of 2024. The consensus view is that the average annual growth rate will be +1.2% in 2024, a drop of 0.8 pp from 2023.

THE BENEFITS OF IMMIGRATION ON THE LABOUR MARKET

However, the labour market is still buoyant. Even though the unemployment rate has risen markedly over the last few quarters, from 3.5% in December 2022 to 4.2% in August 2024, at the same time, the number of people employed and the participation rate have been on an almost uninterrupted rise since the end of 2021. Most notably, the participation rate in August 2024 was 1.4pp above its 2019 average (67.1%, compared to 65.7%). Population growth, which stood at +2.4% y/y at the end of 2023 and was mainly driven by immigration, has helped to increase the size of the workforce in absolute terms (15.0 million in August 2024, compared to 13.5 million before the pandemic) and, ultimately, to boost the overall level of consumption and production. As a result, despite the decline in volume per capita, GDP has remained the same overall.

IT'S NOT YET TIME FOR MONETARY EASING

During its September 2024 meeting, the Reserve Bank of Australia (RBA) decided to keep the cash rate at +4.35% for a sixth meeting in a row. As a result, Australia's central bank is still part of a small group of OECD member countries which have not yet started monetary easing. The decision to maintain such a restrictive approach is mainly due to a lack of developments around disinflation.

GROWTH AND INFLATION

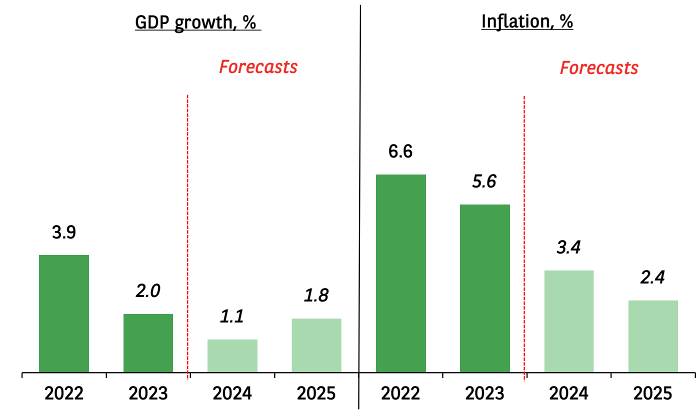

CHART 1

SOURCE: OECD, BNP PARIBAS

Although there has been a major slowdown in inflation since its peak of +7.8% y/y (the highest level since 1990) in Q4 2022, the consumer price index (CPI) has not really budged, with a year-on-year variation of +3.8% in Q2 2024, up on the previous quarter (+3.6% y/y), despite the target of 2%-3%. This has also been seen in the underlying price pressure measures, the CPI trimmed mean (which excludes the most volatile 30% of items) and the CPI weighted median (at the 50th percentile point of the distribution), despite their slowdown (+3.9% y/y and +4.1% y/y in Q2, respectively).

Although growth is slowing and the unemployment rate is heading higher, the RBA indicates that at this stage, the jobless rate remains "lower than estimates of rates that are consistent with full employment" and that "the output gap is positive but continues to narrow"[1]. The structurally-tight labour market is keeping wage pressure elevated, which in turn prevents inflation from falling more rapidly. Indeed, inflation is not expected to fall to midway between the 2%-3% target before 2026, according to both RBA and consensus expectations. Therefore, it is not yet a given that the monetary easing cycle will start in 2024. As at 24 September, market pricing is only 5bp down on the December meeting. As a result, the Australian currency is expected to strengthen against the US dollar in the short term.

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1 See Reserve Bank of Australia, Statement on monetary policy, August 2024.