Australia Economic Outlook Q3 2024

KPMG Australia

September 2024

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Executive summary

The Australian economy has stalled at an aggregate level while continuing to slide backwards when considered on a per capita basis. Private demand is falling, while public demand is running too hot, making policy decisions more challenging for the RBA in addressing inflation.

The global economy has reached an inflection point with monetary policy now facing an easing pathway in the near term, although the extent and length of this easing remains unclear. Headline inflation has seemingly been largely tamed, although concerns remain over whether core inflation will follow the same downwards trajectory, or in fact record a bounce-back within the next year due to a wage-price spiral.

The US has just commenced its easing cycle with a double-jump 50bp cut to the Federal Funds Rate (FFR), following earlier reductions in the policy rate in multiple developed countries including the UK, Switzerland, Canada and New Zealand.

Australia will follow suit and start to reduce our cash rate, but not just yet. Despite various commentators suggesting more extreme monetary policy settings should be being made by the RBA - ranging from the need for successive raising of the cash rate by a further 75bp as inflation remains "out of control' to dropping the cash rate immediately by 50bp because the domestic economy is 'tanking' - KPMG's view is that current settings are appropriate and should be maintained until inflation falls to the point that our real policy rate is sustainably around 1.5%.

This is not likely to occur until early 2025, meaning the RBA Board is unlikely to be in a position to cut the cash rate until its first or second meeting of next year. Even then, the challenge for the RBA will be disentangling the reduction in headline and core inflation due to fundamental falls in prices as opposed to reduction in final prices due to cost-of-living relief measures recently enacted by the Commonwealth and various state governments.

At the time of preparing this report (late September 2024) the futures market is pricing in five 25bp cuts to the cash rate through 2025 and early 2026, with four 25bp cuts occurring in successive RBA Board meetings between February and August 2025, and a further 25bp cut in early 2026.

Australia's GDP growth is expected to remain tepid on an aggregate level and moribund on a per capita level. That being said, KPMG believes we are either at the bottom (or close to the bottom) of the current economic cycle and we should see a slight lifting in economic activity as the remainder of the year progresses, albeit well below historic trends.

The weakness in the private side of the domestic economy is forecast to remain in the near term, unable to revive due to the combination of weakening labour market outcomes and worsening disposable household income. Interest payments on dwellings and income tax payments are now consuming more of household income than at any time since 1959, the start of the ABS data series. The commencement of the Stage 3 tax cuts from 1 July 2024 may in theory bring this ratio down slightly, but early evidence from ADI banks is that Australian households have saved and not spent this clawback in personal income tax payments.

Higher public demand, now representing 27.6% of GDP (compared to the average of 23% achieved during the second decade of this century) has contributed to inflation remaining slightly higher than it otherwise would have been over the last two years. KPMG's macroeconomic scenario modelling suggests this incremental inflation associated with higher-than-average public demand has been around +0.1 ppts and +0.3 ppts per quarter, which is modest, but in an environment where the RBA has been fully focused on bringing inflation back to within its target band as quickly (and painlessly) as possible, every bit of counter-cyclical stimulation to aggregate demand makes that task more challenging.

The other important point to note with this issue is that if the private side of the economy has not started to lift once growth in public demand settles (or potentially even contracts back to long-run averages) then the Australian economy is likely to return to a period of persistently low inflation. Such a scenario is difficult to imagine at the moment but is not impossible given the general malaise being felt across the domestic economy currently.

	Jun-23	Dec-23	Jun-24	Dec-24	Jun-25	Dec-25	Jun-26
GDP (Real)	3.2%	2.1%	1.5%	1.4%	1.7%	2.2%	2.3%
Inflation*	6.0%	4.1%	3.8%	3.0%	2.7%	3.1%	2.8%
Unemployment*	3.6%	3.9%	4.2%	4.6%	4.7%	4.7%	4.6%
AUD/USD*	0.67	0.66	0.67	0.69	0.70	0.71	0.73

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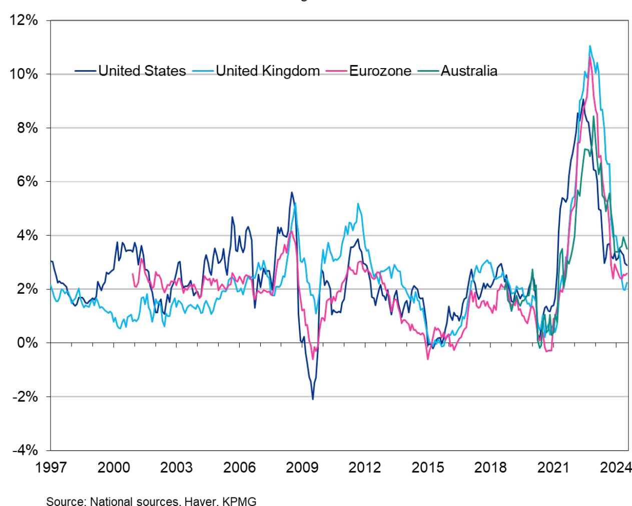
Global landscape

Central banks have broadly commenced the easing of monetary policy settings in light of at or near target range inflation outcomes and macroeconomic weakness.

Conflicts intensifying and trade tensions escalating within a soft global economy

The conflicts in the Middle East and Ukraine are seemingly deepening, as are conflicts in Sudan, South Sudan, Somalia, Ethiopia and Yemen. There are also broader geopolitical tensions, with trade restrictions continuing to rise – the WTO estimates around 9.7% of world imports are subject to form of action, up slightly from 9.5% in 2023. The latest high-profile action relates to numbers of developed countries, including Canada, US and EU, applying significant tariffs to Chinese made EV's.

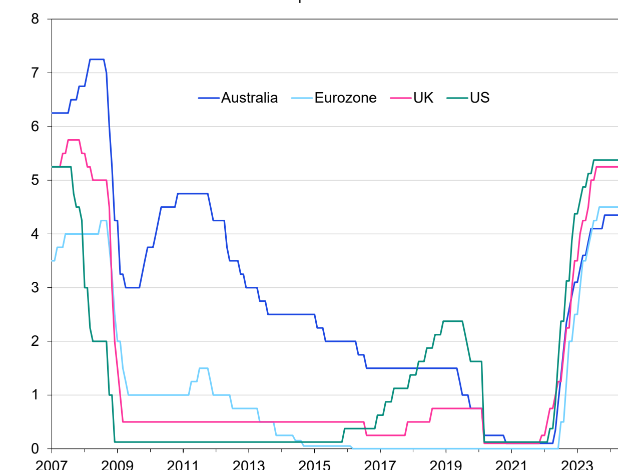
Chart 1: Inflation in Selected Advanced Economies
Year-ended growth



Source: National sources, Haver, KPMG

Contrasting against this challenging backdrop is a world economy that is soft, with rising concerns that the 'narrow path' of maintaining positive economic growth is becoming more and more difficult. This risk of economies tipping into recession has been the primary driver for numerous Central Banks to start easing policy rates down from their relatively high contractionary settings. For example, the US Federal Reserve, arguably the most influential central bank globally, commenced its easing pathway this month by cutting the Federal Funds Rate by 50bp.

Chart 2: Policy Rates in Advanced Economies
End of period



Source: BoE, ECB, FRB, RBA, Haver, KPMG

While the market anticipated the cuts, given the commentary by Chairman Powell at the recent Jackson Hole Economic Symposium and the August 2024 inflation read, the double-jump reduction in the FFR – the first multiple 25bp reduction by the FOMC since December 2008 – still surprised various market commentators.

Soft but resilient economic growth

The shift in policy mix is occurring against a backdrop of moderating world economic growth, and in an environment where monetary and fiscal policy settings across many countries have been simultaneously positioned in conflict with each other (i.e. contractionary monetary policy operating at the same time as expansionary fiscal policy), even though global institutions like the IMF, World Bank and OECD have been highlighting these incongruous arrangements to political leaders for some time.

KPMG expects global growth is forecast to decelerate from 3.1% average annual growth in 2023 to 2.9% in 2024 before edging higher to 3.0% in 2025 and 3.2% in 2026.

Purchasing Managers' Indices (PMIs) for manufacturing have generally shown positive outcomes globally, albeit the readings for the first half of 2024 have been just above the balanced threshold. For services, PMI readings have also been steady rather than strong, with weaker outcomes in the eurozone relative to the US and China.

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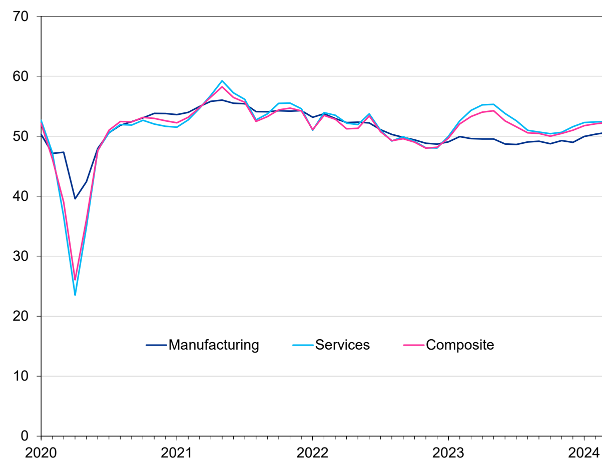
From a regional perspective:

- Asia is poised to slow from nearly 5% growth in 2023 to 4.4% in 2024 and 4.3% in 2025 and 4.4% in 2026. The two largest economies in the region, China (weak output) and Japan (inflation concerns), are driving the regional slowdown; notwithstanding some countries, like Taiwan (semiconductor production), are booming. For China the short-term economic outlook is challenging: measures of factory output, consumption, and investment, have all slowed more than anticipated, while the unemployment rate rose to a six-month high of 5.3% in August, and the urban youth unemployment rate rose to 17.1% in July, up from 13% in June. Economic growth in India is forecast to slow from last year's phenomenal pace of nearly 9%. Unexpected turnover among top levels of leadership and the death of the government's general secretary are likely to bring short-term uncertainty to Vietnam.

- Europe, including the eurozone and Eastern Europe, is forecast to achieve economic growth of 1.6% in 2024, 1.7% in 2025 and 1.8% in 2026. Germany, the foundational economic powerhouse for the region, continues to struggle. The return of tourism has helped buoy the economies of Greece, Italy and Spain. Across most of Eastern Europe, inflation is approaching or has reached various central bank targets; real wage growth is boosting consumption. Poland and Hungary are likely to hold rates flat through the end of year, while Romania and Czechia may cut sooner.

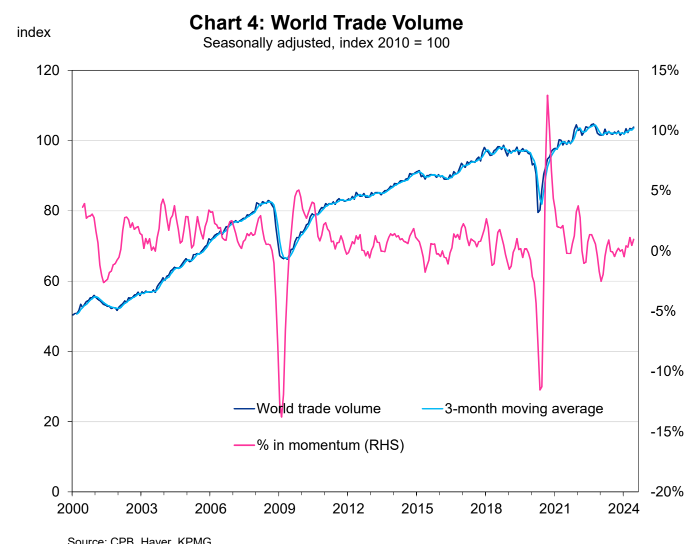
- The Middle East and Africa are expected to see growth accelerate from 1.6% in 2023 to 2.0% in 2024, 3.9% in 2025 and 4.0% in 2026. Inflation has already decreased substantially from its peak and is expected to hit its pre-pandemic lows in 2026. Maritime traffic through the Suez Canal remains well down, with trade volumes in August 2024 only sitting at around 23% of those achieved in November 2023.



- North American growth is expected to slow from 2.5% in 2023 to 2.3% in 2024 and 1.8% in 2025 before edging back up to 2.2% in 2026. The US economy has been holding up on the back of strong consumer demand, although the expectation is that this source of growth will weaken as higher monetary policy finally bites. Canada's growth has stalled in response to higher rates but should rebound in 2025 and 2026. The Bank of Canada has already cut its policy rate three times, but with inflation now back at 2% there is an expectation further rate cuts could follow double-jumps given the move by the US Fed. Mexico's output growth is forecast to slow in 2024 and 2025 and bounce back in 2026. Following national elections in June, the peso and equity markets sold off on concerns about future economic policy. The central bank cut rates a second time in early August to address the economic slowdown and given Mexico's policy rate is at 10.75% it does have substantial headroom to cut rates further, albeit at a relatively slow pace given inflation is still at 5%.

- Growth in South America is forecast to slow from 1.5% in 2023 to 1.2% in 2024 and rebound to 2.3% in 2025 and 2.9% in 2026. High interest rates are a hurdle and limit fiscal stimulus; recent depreciations in currencies have spurred hawkishness at central banks. Argentina has embarked on a unique period of fiscal consolidation, which triggered a rapid and deep recession, with three quarters of negative growth occurring from Q4 2023. Brazil's central bank has bucked the trend by increasing its policy rate by 0.25% (to 10.75%) in early September as a mechanism to help bring back down the country's rate of inflation which has been heading higher since April. Commodity prices have supported Peru and Chile's expansions in 2024 following a disappointing 2023. Copper is one of the largest exports from the Andean economies and will retain its high demand as chips and green tech products grow in importance.

The latest WTO Goods Trade Barometer shows global goods trade has continued to recover in the third quarter of 2024 after traded goods activity flatlined in 2023. All of the barometer's component indices are currently showing on or above trend, with the notable exception of the electronic components index (95.4), which is below trend and falling. Component indices for automotive products (103.3), container shipping (104.3) and air freight (107.1) are all firmly above trend. New export orders (101.2) is marginally positive but has turned down, while the index of raw materials (99.3) is nearly on trend but has declined sharply over the last three months.



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Australia overview

The Australian economy has stalled in the first half of 2024, with private demand falling and GDP being propped up by public sector demand.

The June quarter 2024 national accounts painted a picture of an anaemic economy, and although the challenges do not necessarily present themselves in the key headlines, the 0.2% quarterly real GDP growth was more tepid than expected, and the annual growth figure of 1% was the lowest recorded since the early 1990s recession (excluding the recent COVID pandemic period).

GDP per capita fell 0.4% during the quarter – the sixth quarter in a row where this broad indicator of living standards has declined. Other telltale measures, like real household disposable income and real household consumption, have also gone backwards in recent quarters, further confirming the challenging economic environment many Australian households and businesses are currently facing.

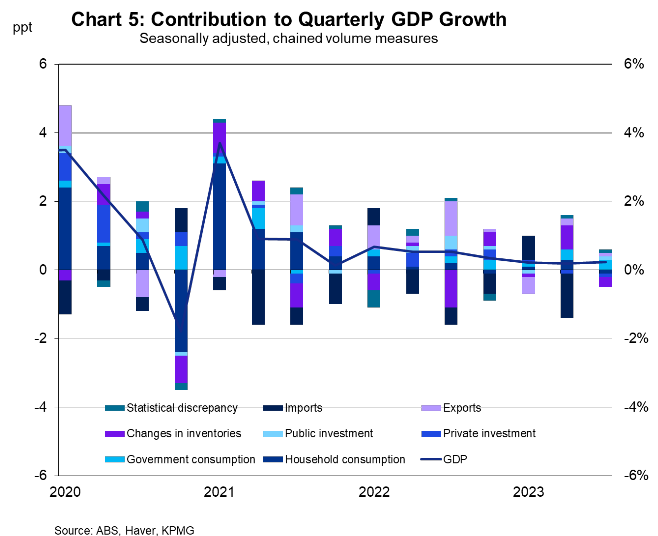
Headline economic activity has only remained positive in recent quarters due to the combination of high levels of net overseas migration and government spending. On one hand this strong public sector demand has underpinned consumption activity; however, this labour-intensive public sector spending has also crowded out more capital-intensive private sector activity and has also hampered the RBA's efforts to control inflation.

The ray of light in an otherwise relatively bleak economic narrative remains the resilience of Australia's labour market, notwithstanding the comments above regarding public sector crowding out. Australia's unemployment rate remains very low by historical standards and relative to our developed economy peers. The flip side of this labour market strength has been falling productivity, the fundamental building block to economic prosperity.

One related argument for these poor productivity outcomes relates to businesses holding onto (previously) scarce labour during a period of poor growth in economic output due to low demand. Such a scenario is simply unsustainable as businesses record falling (and potentially negative) profits, triggering businesses to start to shed labour in order to achieve a better balance between outputs and inputs.

The latest national accounts data shows:

- GDP per hour worked fell by 0.8%, after falling 0.1% in the March quarter.
- Real unit labour costs picked up again, increasing by 1.3% during the June quarter after falling 0.1% in the December quarter 2023 and falling 0.5% in the March quarter 2024.
- Gross disposable income rose 0.9% after growing 1.1% in the March quarter.



Source: ABS, Haver, KPMG

- Net trade contributed 0.2% to GDP, with a rise in exports (0.5%) and a fall in imports (-0.2%). The rise in exports was driven by services from higher expenditure by international students; while imports declined due to falls in the importation of machinery and industrial equipment and processed industrial supplies.
- Household goods consumption fell 0.1% in the June quarter – the third fall out of the previous four quarters. Household services consumption remains volatile, dropping 0.2% this quarter after increasing 1.3% in the March quarter.
- Household discretionary consumption fell 1.1% this quarter, while the household saving-to-income ratio remained the same at 0.6%.

From an income perspective the latest national accounts show:

- Compensation of employees (COE) rose 0.9% over the June quarter; essentially on-par with 1.0% growth recorded in the March quarter, and also consistent with the latest Wage Price Index (WPI). More interesting is the divergence in growth rates between the private and public sectors, with private sector COE rising 0.7% and public sector COE rising 1.4%.
- Gross operating surplus (GOS) fell 0.6% over the quarter after recording a rise of 1.6% during the March quarter. Private non-financial corporations saw GOS fall -2.8% over the quarter, with the mining sector leading the drop in corporate profitability (7.8%) due to lower commodity prices.
- Taxes on production and imports rose 0.3%, with taxes on financial and capital transactions, land tax, and excise tax being responsible for the majority of this growth.

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Production

The second quarter of 2024 saw contractions of Gross Value Added (GVA) over the quarter in 6 out of 19 industries, with the largest drop recorded in *Arts and recreation* (-0.7% q/q), in line with the decline in discretionary spending.

Some others recording the largest q/q reduction included:

- *Accommodation and food services* (-0.3%) and *Retail services* (-0.3%) again because of the softening in household consumption on discretionary goods. These two sectors have now recorded consecutive falls in quarterly IGVA for the past three and two quarters respectively, meaning they are both in technical industry recessions.
- *Mining* (-0.3%) has also recorded two consecutive quarters of negative growth largely due to falling commodity prices, with Australia's Terms of Trade about 4% lower by the end of June than it was at the start of 2024.

In contrast, those with the largest q/q growth were:

- *Information, media and telecommunications* (+1.6%), driven in part by growth in the penetration of streaming services and a 3% increase in average revenue per user.
- *Electricity, gas, water and wastewater services* (+1.3%) due to substantial increases in the water and wastewater service turnover.

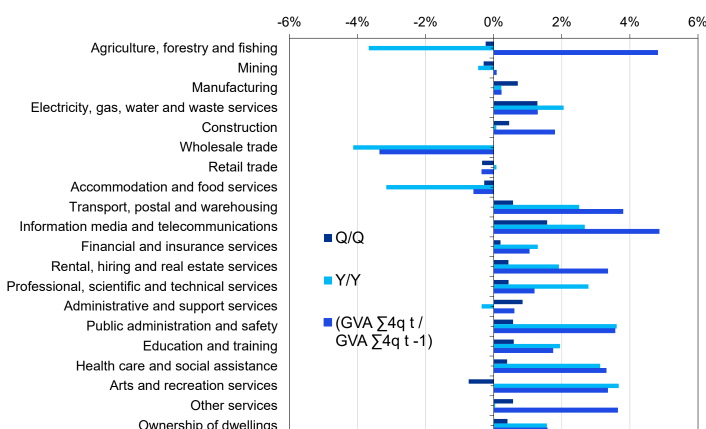
NAB monthly business surveys show business confidence and conditions both fell in August, with bleaker trading conditions, profitability and employment outlook. The RBA will be noticing that capacity utilisation remained above average and actually ticked up a little in August, with capital expenditures also jumping. Forward orders look weakest in the *Retail* and *Wholesale* sectors, which also matches the sectors with the lowest employment outlook. The NAB survey also shows price pressures remain on the input side, although labour cost growth has begun to ease.

This has also borne out in the Producer Price Index (PPI), with the ABS measure of Final Demand seeing growth of 1.0% in the June quarter, up from 0.9% in both of the previous two quarters. In terms of output prices:

- Building construction prices rose 1.3% this quarter, with most of this growth reflecting higher labour costs associated with the ongoing labour shortages for skilled tradespeople. In contrast, material prices remained stable except for those associated with energy intensive materials.
- Prices received for domestic gas extraction increased in line with renegotiated East Coast production contract prices.
- Basic non-ferrous metal manufacturing (+12.0%), due to higher gold prices prompted by buying activity from central banks. Higher commodity prices for base metals also contributed to the rise.
- Meat and meat product manufacturing (+4.9%), due to strong export demand for beef driven by a shortage in the US.
- Accommodation services saw output prices fall by nearly 9.0% as demand dropped off following Easter school holidays and the traditional fall away in domestic travel during the colder months.

The latest Agricultural Commodities Report prepared by the Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) forecasts gross value of agricultural production to increase by 4% in 2024–25, driven by higher livestock product values and increased crop production. The Department of Industry, Science and Resources (DISR) has revised up the near-term outlook for Australian resource and energy commodity exports since the March quarter 2024 forecasts, although DISR still expects Australian resources and energy exports to continue to ease after the record peak seen in 2022–23.

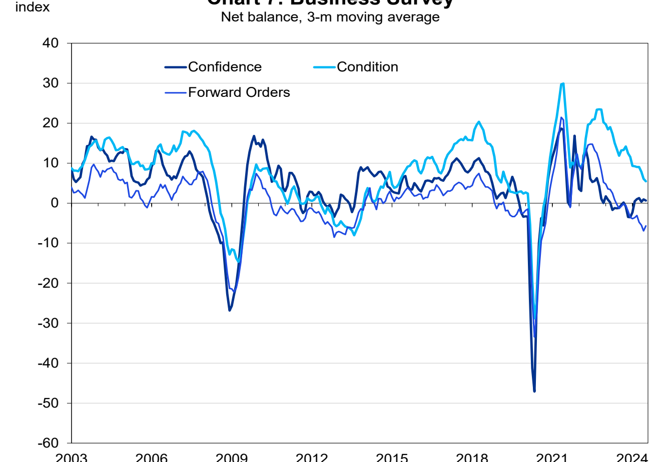
Chart 6: Industry Gross Value Added, Jun-24



Source: ABS, Haver, KPMG

Chart 7: Business Survey

Net balance, 3-m moving average



Source: NAB, Haver, KPMG

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Household consumption

Household final consumption expenditure in Q1 2024 fell slightly by -0.2% over the quarter, following relatively strong growth of 0.6% (revised) in the previous quarter. This decline was relatively broad based, with 10 of the 17 expenditure categories registering falls in real spending over the quarter, including *transport services* (-4.4%), *purchase of vehicles* (-2.6%), *cigarettes and tobacco* (-2.4%), *alcoholic beverages* (-2.0%), *hotels, cafes and restaurants (-1.5%)* and *food* (-1.0%).

The total new passenger and SUV motor vehicle sales continue to trade at sub-peak (August 2023) levels of around 230,000 to 240,000 units per month. The June quarter saw a 5% increase in sales activity compared to the first quarter of 2024, with SUVs still dominating with consistently around 75% of sales activity.

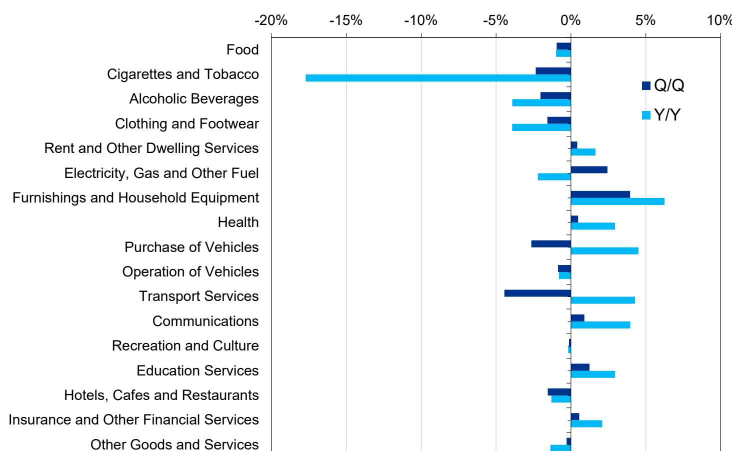
The financial challenges facing many households appears to be worsening as the year progresses with gross disposable income now growing at a slower pace than households' use of that income. The fall in spending on *food* highlights how households are adapting their expenditure to realise savings beyond pulling back on discretionary items, with anecdotal evidence suggesting this is being achieved by more households purchasing lower cost white-label products instead of higher cost branded food items.

KPMG's Retail Health Index (RHI) showed, consistent with the national accounts IGVA data, that the recovery in the sector stalled in the first quarter of 2024 as discretionary retail slowed amidst the cost-of-living crisis and has continued to face additional setbacks. The delay is primarily driven by the increase in producers' costs and subdued consumer sentiment, as sticky inflation has created a considerable amount of uncertainty about the cash rate outlook, resulting in consumers remaining cautious about every dollar they spend.

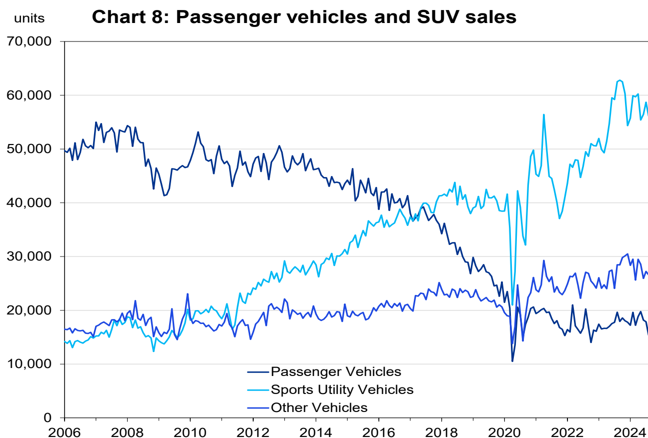
Renters and those struggling with mortgage payments are hit hardest by rising costs, while outright homeowners continue to spend, though not always in stores or local restaurants. Instead, the post-Covid bounce in overseas travel appears to have reset spending patterns, with 'cashed-up' consumers seemingly preferring to allocate 'big ticket' spending towards overseas holidays and leisure rather than on major household goods. In fact, the number of Australian travellers increased by 7.3% in the 12 months to June 2024

The latest Westpac–Melbourne Institute Consumer Sentiment Index dropped 0.5% to 84.6 in September, with ongoing pessimism seemingly cemented in the psyche of households. The latest survey does suggest, however, the cause of this negative outlook appears to be shifting away from cost-of-living pressures and further interest rate rise fears towards concerns over the general economic outlook and the consequence this may have on employment and income.

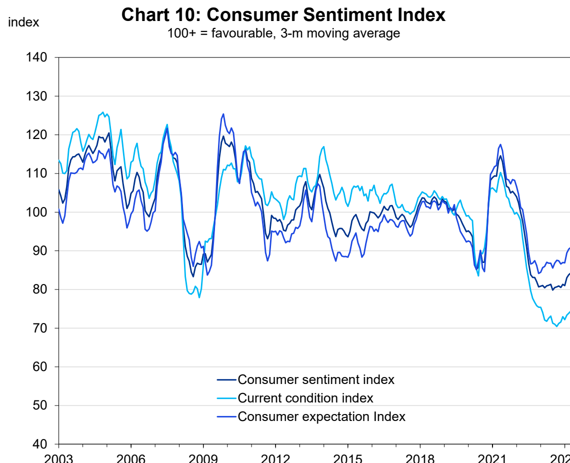
Chart 9: Household Final Consumption Expenditure, Jun-2024



Source: ABS, Haver, KPMG



Source: Federal Chamber of Automotive Industries, Haver, KPMG



Source: Westpac - Melbourne Institute, Haver, KPMG

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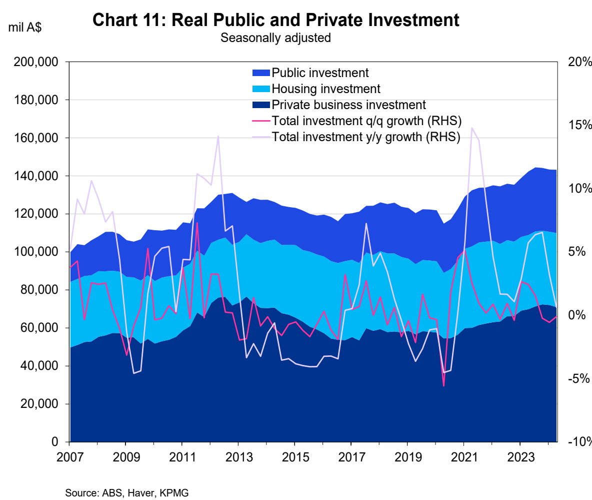
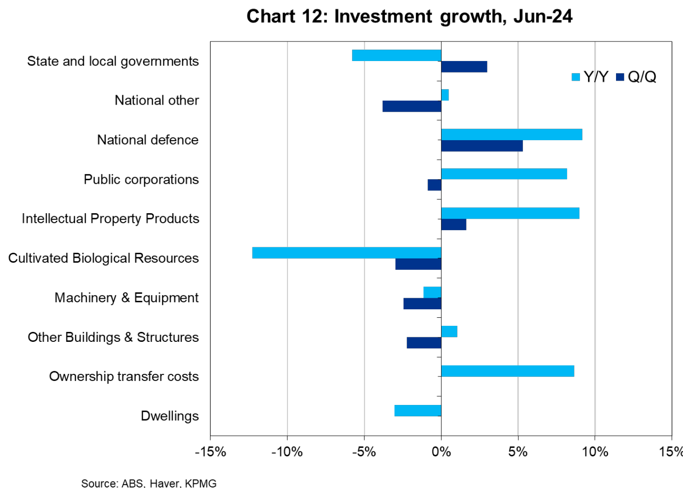
Investment

Investment activity, as measured by gross fixed capital formation in the national accounts, fell for the third consecutive quarter, down 0.1% q/q in Q2 2024, largely as a result of a continued withdrawal of private investment activity.

The fall in private investment activity was centred on declining business investment in both non-residential construction (-2.2%) and machinery and equipment (-2.4%). There is a small glimmer of hope that the downturn in dwelling investment may have bottomed, with both new construction activity and ownership transfer costs lifting in the June quarter.

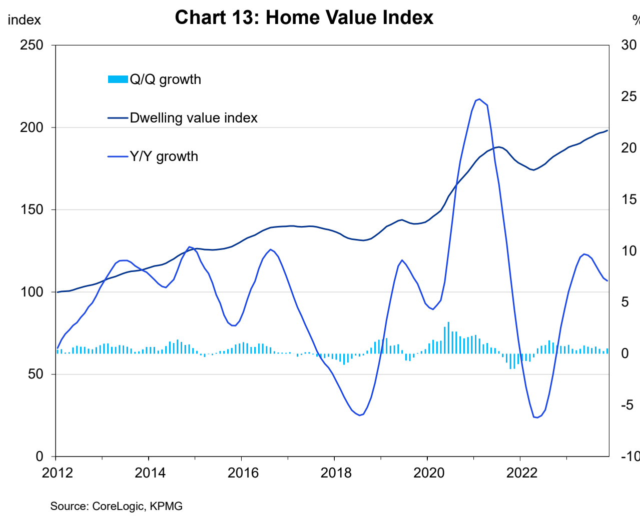


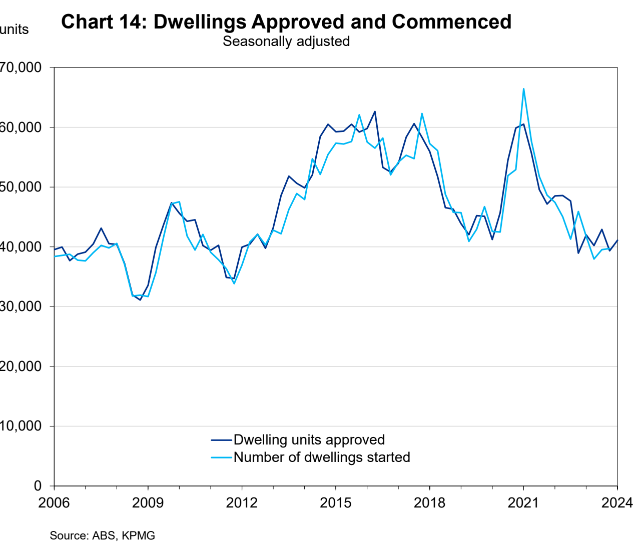
The residential property market in August continued to advance (+1.3% on a rolling three-month basis) although there remains a clear divergence in price growth across capital cities due to differences in housing demand, population growth and housing supply. Significantly stronger gains continue to be observed on a rolling three-month basis in Perth (+5.6%), Adelaide (+4.0%) and Brisbane (+2.9%), while price growth remain weakest in Melbourne (-1.2%), Hobart (-0.4%) and Darwin (-0.3%).



KPMG remains of the view that the pace of dwelling price growth will slow down gradually over the remainder of 2024 as the market adjusts. While limited new housing construction will lead to further price gains, the prolonged contractionary interest rates and a more balanced population growth are expected to exert a cooling effect on the market and partly offset the gains, resulting in a more tempered growth trajectory for dwelling prices.

Housing investment is expected to remain subdued, albeit positive, in 2024 as signalled through the lacklustre number of dwelling approvals, which has been on a downward trend since mid-2022, reflecting the effects of higher building costs. Into 2025, anticipated lower interest rates, government initiatives to boost supply, and improved conditions for builders, are expected to drive a sustained rebound in dwelling investment.





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The June quarter survey of private capital expenditure showed a -2.2% drop-off in actual investment during the second three months of 2024 across both buildings and structures (-3.8% q/q) and plant, equipment and machinery (-0.5% q/q). The survey results also revealed Estimate 3 in current prices for FY25 ($170.7 billion in actual spend) was revised up by around 10% compared to Estimate 2 for the same year. If the average realisation rate is maintained for FY25, then the likely private sector spend on new capital would be around $194 billion, a nominal increase of around 6.7%.

Administrative and support services achieved the strongest growth due to increased investment in plant, machinery and equipment, albeit this uplift in capex only amounted to $68 million for the quarter. Rather, *Mining* saw investment activity contract by nearly $1.1 billion over the quarter, and *Transport, postal and warehousing* and *Retail* sectors recorded lower investment of nearly $300 million each during the June quarter.

In contrast to the experience in the private side of the economy, public investment rose by 1.5% over the quarter with state and local governments leading the uptick in spending across both public corporations and general government sectors. At a Commonwealth level, defence-related investment activity rose by 5.3% during the quarter, although this rise was closely offset by the fall in defence consumption activity (-$133 million).

The Australian Government has recently awarded three projects major project status: the Murchison Green Hydrogen project, the NiWest Nickel Cobalt project, and the Australian Renewable Energy Hub.

- The Murchison Green Hydrogen project is a large-scale wind, solar, hydrogen and ammonia plant expected to cost an estimated $15 billion. The project aims to generate 6 gigawatts of renewable energy and produce around 2 million tonnes of green ammonia each year. Construction is anticipated to take five years.
- The NiWest Nickel Cobalt project aims to produce 90,000 tonnes of nickel sulphate and 6,800 tonnes of cobalt sulphate. The estimated project cost is $1.26 billion, with construction anticipated to take two years.
- The Australian Renewable Energy Hub consists of two sites, including a hydrogen processing facility capable of producing around 1.6 million tonnes of hydrogen and 9 million tonnes of green ammonia each year, and a 6,500 square kilometre solar array and wind farm expected to produce up to 26 gigawatts of combined solar and wind power each year. The project has been forecast to cost approximately $30 billion, with construction taking around 10 years.

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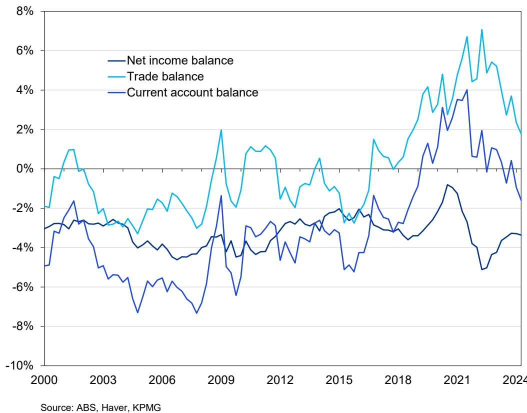
Net exports

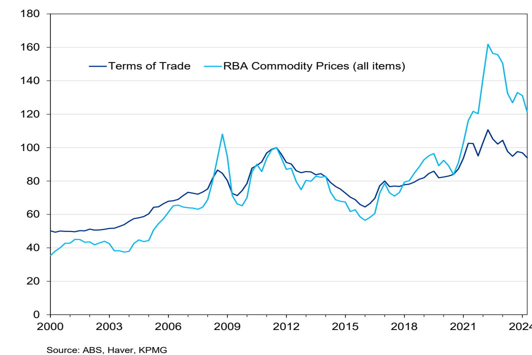
With exports increasing 0.5% q/q and imports falling 0.2% q/q net trade contributed 0.2 ppts to real GDP growth in Q2 2024, after contracting 1.1 ppts from real GDP growth in the March quarter.



Exports of goods fell 4.4%, with lower prices for iron ore and coal driving the decrease. Exports of cereal also fell due to reduced wheat production in the 2023–24 season. The fall in exports of goods was partly offset by growth in exports of services increasing by 6%, largely as a result of higher education-related travel service income.

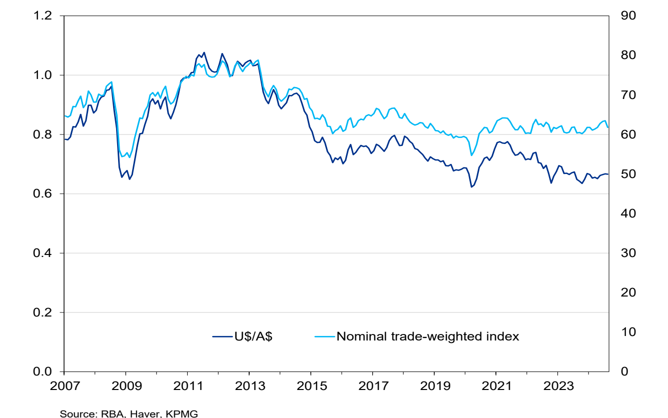
Imports of goods fell 0.6% due to fewer imports of mining equipment. Imports of services rose 1.1% bolstered by an increase in the number of Australians travelling overseas.

Australia recorded a consecutive current account deficit in Q2 2024, falling by $4.4 billion to a deficit of $10.7 billion (seasonally adjusted, current prices). The June 2024 quarter's current account deficit was the largest since the June quarter 2018, primarily due falls in bulk commodity prices and higher income paid to non-residents.



Australia's terms of trade fell 3% from last quarter and was down 3.8% lower than the June quarter 2023 index value. While import prices remaining unchanged, lower mining commodity prices, driven by falling global demand, resulting in declining export prices.

The Australian Dollar has risen from USD 0.651 at the end of April 2024 to be trading at around USD 0.667 in late August. Market views regarding the delayed timing of policy cuts in Australia compared to other advanced economies, especially the expectation that the US Fed will commence a steep decent in the FFR over the coming 12 months, has resulted in a stronger AUD. This strengthening can also be seen in the AUD on a Trade Weighted Index Basis, which has appreciated by 1.6 index points since the end of April.



The World Bank commodity price index fell by 3% between May 2024 and August 2024, led by large falls in energy prices (crude oil and natural gas), food prices and metal prices.

Commodity prices in 2024 are expected to fall 3% relative to last year's levels, while the market also expects volatility in commodity prices to continue until the end of 2025 due to several factors including elevated geopolitical risks and uncertainty regarding the strength of the Chinese economy.

External demand assumptions

	2023 Q4	2024 Q1	2024 Q2	2024 Q3	2024 Q4
Exchange rate: Australian dollar/US dollar	0.66	0.65	0.68	0.69	0.69
Thermal coal price (US$/tonne)	147	129	151	148	150
Semi soft coking coal price (US$/tonne)	278	342	256	269	273
Gold price (US$/oz)	2,045	2,178	2,306	2,350	2,371
Dalian Iron Ore 62% Futures	141	100	117	114	111
Brent Spot Average (US$/barrel)	79	82	84	83	81
West Texas Intermediate Spot Average (US$/barrel)	74	78	79	78	76

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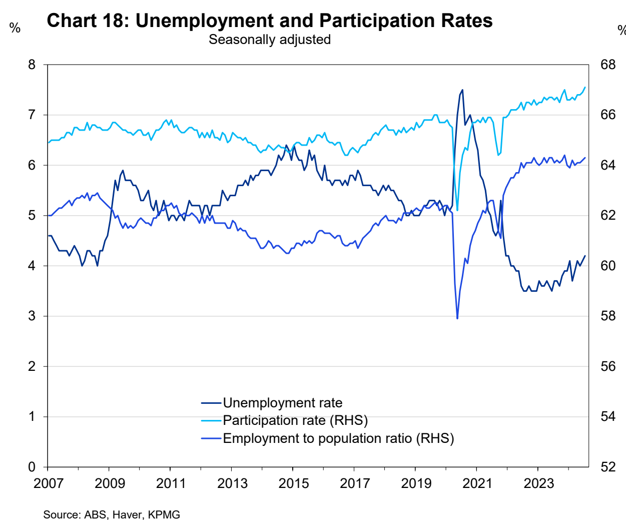
Labour market

The seasonally adjusted unemployment rate increased slightly over the past three months, from 4.1% in April to 4.2% in July; the highest level it has been since November 2021. Australia's labour market, which has shown a much higher degree of resilience than most market analysts, including KPMG, is now starting to (slowly) show signs of easing with the ratio of unemployed people to vacant jobs now sitting closer to 2 as compared to 1.1 in May 2022. Despite this the number of unemployed persons remains around 70,000 below pre-pandemic levels.

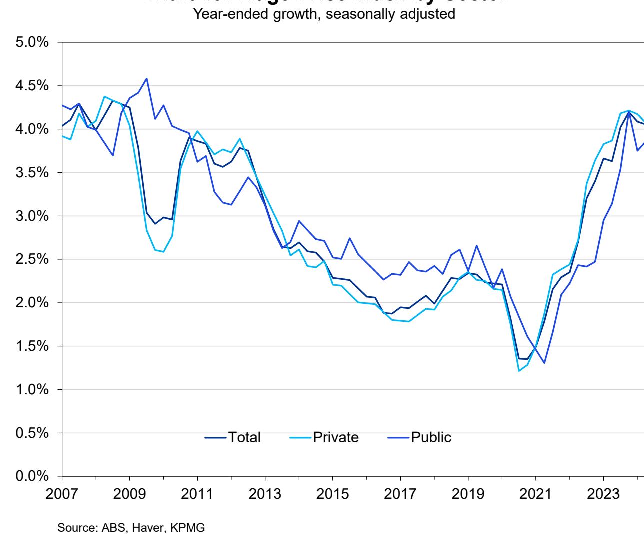
Increases in both employment and unemployment in July boosted the participation rate to a record high of 67.1%, with female participation rising by 0.3 ppt and male participation rising by 0.2 ppt. The employment-to-population ratio rose 0.1 ppt over the month to 64.3 a level slightly below the historical high of 64.4% recorded in November 2023.



Wages growth appeared to have peaked in the December quarter 2023. The recent data for the June quarter show the WPI rose by 4.1%, unchanged from March but slightly lower than the peak of 4.2% recorded in the December 2023 quarter.

Wages growth in the private sector softened in the June quarter 2024, down from 4.2% to 4.1%. Public sector wages rose slightly to 3.9% from 3.8% and contributed 25% of overall wage growth this quarter, and much higher than the contribution the same time last year (19%), enabled by changes to new state and federal wage policies introduced across 2023.

67% of all jobs that recorded a wage change over the previous 12 months received an annualised increase above 3%, compared to 53% in the June quarter 2023. The last time the share of jobs with an annualised increase above 3% was the June quarter 2009 (68%).



By method of setting pay, jobs covered by an individual arrangement contributed over half of WPI quarterly growth in the June quarter 2024. By industry, annual wage growth was the highest in *Health care and social assistance* (5%). The mining industry recorded the highest quarterly rise (1.3%). Wage growth was also broad-based at a state level. Tasmania recorded the highest annual growth of 5.1%. Three states (Victoria, South Australia and Northern Territory) recorded annual growth of less than 4%, with Victoria recording the lowest (3.3%).

The strength of the labour market is expected to gradually weaken given the lag between the real economy and the labour market. Leading labour market indicators, such as SEEK's jobs ad index, indicate a softening in labour demand. While job ads in July rose for the first time since March this year (+1.7% m/m), job vacancies remain down 15.3% y/y. The latest data also reveals that applications per job ad rose 2.5% m/m and are 60% higher y/y.

The expected increase in net overseas migration will continue to help address some of the tightness in Australia's labour market. As a result, KPMG expect the unemployment rate to gradually rise from its current low levels to reach the natural rate of unemployment by the end of this year.

While unemployment rates have increased from their recent lows, wage growth has not yet declined significantly from its peaks, most likely due to the cyclical pattern of enterprise bargaining in the public sector. As such, KPMG expects nominal wages growth in this economic cycle to have peaked but will stay elevated before declining gradually in line with the easing in the labour market.

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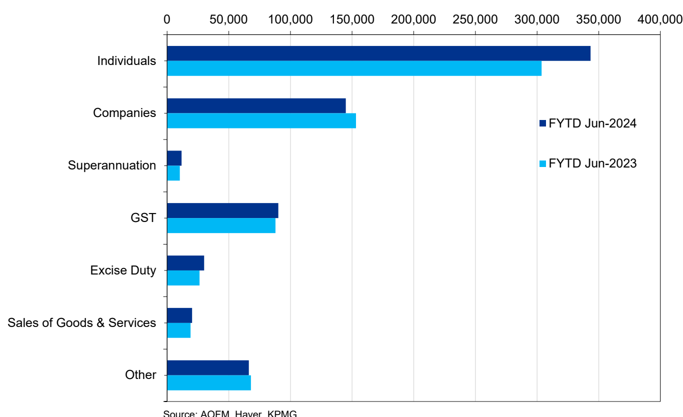
Government

Public demand was the single largest contributor to economic growth in the June quarter 2024, adding 0.4 ppt to quarterly GDP growth, with government consumption expenditure contributing 0.3 ppt over the quarter.

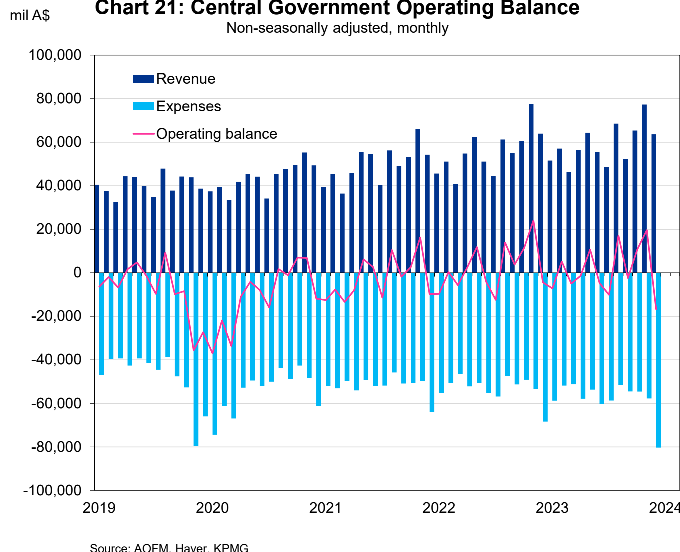
Government spending rose by 1.4% over the quarter, driven by higher spending on government benefits for households, particularly as large government programs continued to expand for health services. Public investment fell 1.4%, down for the third consecutive quarter, as work done on existing transport and health projects moved towards completion.



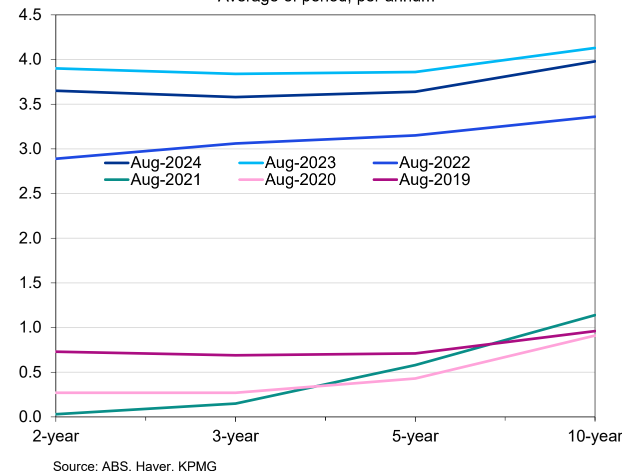
The latest Government Finance Statistics reveal that the net operating balance across all levels of Government in Australia was $11.6 billion in FY24, $23.3 billion lower than the FY23 outcome 2022–23 as growth in government expenses (8.1% or $71.5 billion) outpaced corresponding growth in revenue (5.3% or $48.3 billion).

The increase in Commonwealth taxation was largely due to an increase in personal income tax (11.5%), consistent with a resilient labour market and relatively solid growth in nominal wages (resulting in bracket creep) . While company income tax fell by 6.8% on the back of lower tax receipts from the mining sector because of lower commodity exports prices, company income tax remains much higher than the levels seen prior to FY23. State and local taxation increased by 10.5% over the year due to higher payroll tax receipts.

Government expenses increased by 8.1% ($71.5 billion) in FY24, with increases in social benefits, employee expenses, and current monetary transfers to households the primary costs driving this growth. Social benefits increased by 16.5% ($23.8 billion), whilst employee expenses and current monetary transfers to households increased by 9.2% ($21.5 billion) and 7.2% ($10.5 billion) respectively.



Commonwealth Government bond yields had started to move lower across the curve by the end of August 2024 as the financial markets started to price in interest rate cuts; a response similar to moves in financial markets for other advanced economies. The 10-year Commonwealth government bond yield in the June quarter 2024 averaged 3.98%, which represented a +33-basis point between difference over 2-year tenor bonds.



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Financial conditions

Considering financial conditions facing Australian households and businesses - beyond just the overall stance of monetary policy – is an important gauge in understanding the near and medium term outlook for consumption and investment.

KPMG's Financial Conditions Index (FCI) measures the state of financial conditions in Australia, not just for the overall economy but also for households and businesses. It is based on quarterly data from households, businesses, and macroeconomic sources.

We assess financial conditions by examining a broad set of complementary indicators, as detailed in the table below. A significant deviation of an indicator from the average of the sample means that the financial conditions are more restrictive/expansionary. An expansionary financial condition indicator (highlighted in blue) indicates that the greater that variable from its average, the more expansionary the financial conditions are. Conversely, a restrictive financial condition indicator (highlighted in pink) indicates that a larger deviation from the average corresponds to more restrictive conditions.

Given the extensive data available, we assess financial conditions for households, businesses, and the overall economy by computing the first principal component for household finance variables, business finance variables, and all variables combined, respectively.

These indicators are transformed to annual growth terms (or y/y changes for rate indicators such as interest rates or yields). All transformed series are then standardised to have a mean of zero and a standard deviation of one. Additionally, to ensure consistent interpretation, all restrictive variables (highlighted in pink) are reversed.

Indicators of Financial Conditions

Category	Indicator
Household	New housing finance commitment
	New personal finance commitment
	Housing credit
	Personal credit
	Discounted variable rates for owner-occupier
	Credit cards standard rates
	Household income spent on interest on dwellings
	Household income spent on consumer debt interest
Business	Lease finance commitment
	Commercial lending
	Business credit
	Non-financial 3-year A-rated bond yields
	Non-financial 10-year A-rated bond yields
	Non-financial 3-year BBB-rated bond yields
	Non-financial 10-year BBB-rated bond yields
Other Macro	Government lending
	Bond issued as a percentage of GDP
	Real trade-weighted index
	ASX 200 share price index
	Official cash rate
	10-year government bond yields

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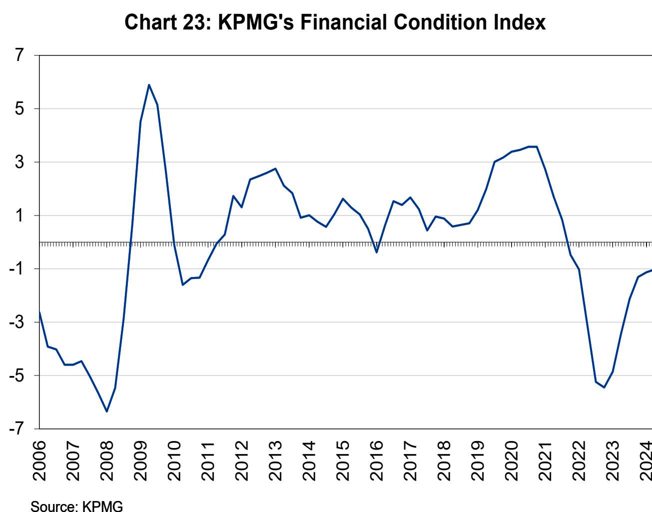
Financial conditions (cont.)

Financial conditions are particularly restrictive for households, but less so for businesses. Financial conditions for businesses are back to the neutral zone.

Chart 23 illustrates KPMG's Financial Condition Index (FCI) for the time period from the March quarter 2006 to the June quarter 2024. A positive index value indicates generally expansionary financial conditions, while a negative index value indicates restrictive financial conditions.

Chart 23: KPMG's Financial Condition Index



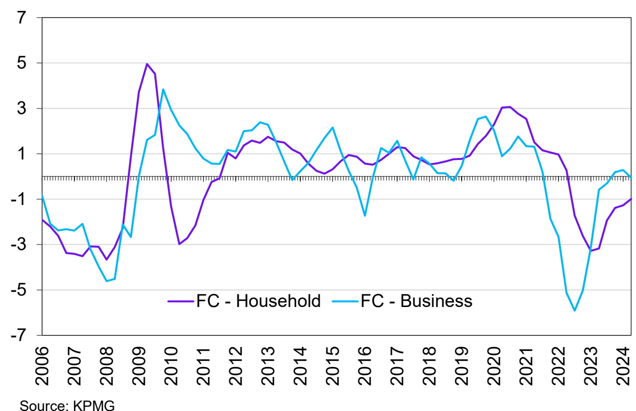
The FCI shows that financial conditions tightened significantly during the GFC. Despite the onset of the pandemic, financial conditions did not deteriorate as expected, due to historically low cash rates, rising asset prices and substantial fiscal stimulus.

The tightening in monetary policy across the advanced economies over the past two years has led to more restrictive financial conditions in Australia since the December quarter 2021, contributing to slower economic growth as a consequence.

In the past four quarters, KPMG's FCI has shown some signs of easing. This trend coincides with the Reserve Bank of Australia's pause on rate hikes, with the last rate increase potentially occurring in November 2023. Expectations of rate cuts next year have also contributed to a lower 10-year government bond yield compared to levels 12 months ago. Additionally, the ASX share price index has risen significantly over the past year, increasing from 7,234 to 7,743.

The effects of higher interest rates are felt directly across the roughly 40% of Australian households with a mortgage. Financial conditions for households have become more expansionary over the past 12 months but remain in the restrictive zone.

Chart 24: KPMG's Financial Condition Index Household vs Business



Source: KPMG

The discounted variable rate remains high at 7.12% in the June quarter 2024 but has slightly decreased from the peak of 7.31% observed between December 2023 and March 2024. Furthermore, interest on dwellings grew 20% y/y but moderated down from the 71% y/y growth rate recorded over FY23. Despite these elevated mortgage rates, new housing loan commitments increased 19% y/y in the June quarter and have been growing for three consecutive quarters.

The upwards trajectory of cash rate increases over the past 2 years did not result in interest rates being charged on credit cards moving in lock-step; rather credit card interest rates have only started to rise over the past 9 months. Interestingly credit card interest rates fell between December quarter 2021 to the December quarter 2023, a notable deviation from how banks adjusted mortgage rates relative to the change in cash rate over that time period.

The tightening of monetary policy also led to higher business lending rates and increased corporate bond yields (as investors demand greater yields to compensate for the increased risks associated with a slowing economy and high inflation). This increase in debt costs resulted in significantly more restrictive financial conditions for businesses in FY23. However, financial conditions for businesses have been returning to 'neutral' territory much more quickly than for households.

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Forecast

GLOBAL[4]	Annual GDP Growth[1]			Unemployment Rate[2]			Average Annual Inflation[3]		
	2023	2024	2025	2023	2024	2025	2023	2024	2025
World	3.1	2.9	3.1				5.8	3.5	2.2
Euro Area	0.5	0.8	1.5	6.5	6.8	6.4	5.4	2.5	2.0
UK	0.1	1.1	1.3	4.3	4.5	4.7	7.3	2.8	2.3
US	2.5	2.6	1.9	3.8	4.0	3.9	3.7	2.7	2.0
Brazil	2.9	1.9	2.0	7.5	7.7	7.0	4.6	4.0	3.6
China	5.2	4.9	4.5	5.0	5.3	5.5	0.2	0.5	1.6
India	7.7	7.2	6.9	8.9	6.1	7.4	5.7	4.5	4.0
Indonesia	5.0	5.0	5.1	5.2	6.6	6.6	3.7	2.8	2.8
Japan	1.8	0.2	1.2	2.6	2.5	2.4	3.0	2.5	2.1
Singapore	1.1	2.1	2.2	2.0	2.6	1.9	4.8	2.6	2.0
South Korea	1.4	2.5	2.2	2.8	3.2	3.0	3.6	2.3	2.3
Taiwan	1.3	3.1	2.6	3.4	3.9	3.8	2.1	2.3	2.2
Vietnam	5.0	5.7	6.2	2.4	2.6	3.9	3.3	4.1	4.1
Australia	2.1	1.4	2.2	3.9	4.6	4.7	5.8	3.4	2.8
New Zealand	0.8	0.7	1.8	4.0	4.0	3.3	5.6	3.1	2.7

[1] GDP growth calculated as (GDP q1-q4 t / GDP q1-q4 t -1) [2] Estimated unemployment rate at end of year. [3] Estimated average inflation though the year [4] Source: NIESR

AUSTRALIA	Dec-22	Jun-23	Dec-23	Jun-24	Dec-24	Jun-25	Dec-25	Jun-26
Consumption	7.1%	5.9%	2.1%	1.0%	1.3%	1.4%	1.3%	1.4%
Business investment	6.2%	8.5%	9.1%	5.7%	1.6%	0.9%	2.0%	2.7%
Housing investment	-4.8%	-7.8%	-4.4%	-1.8%	-1.0%	0.2%	2.0%	2.7%
Government	4.8%	2.5%	3.4%	4.4%	2.6%	1.4%	1.1%	1.1%
Exports	2.5%	6.7%	6.6%	3.6%	1.2%	1.2%	4.1%	5.7%
Imports	13.7%	12.0%	6.5%	5.9%	4.1%	0.9%	1.1%	3.0%
GDP	3.9%	3.1%	2.0%	1.5%	1.4%	1.7%	2.2%	2.3%
Headline CPI	7.9%	5.7%	4.1%	3.8%	3.0%	2.7%	3.1%	2.8%
WPI	3.4%	3.6%	4.1%	4.1%	3.5%	3.4%	3.3%	3.3%
Real WPI	-4.2%	-2.0%	0.0%	0.3%	0.5%	0.7%	0.2%	0.5%
Current account balance*	1.0%	0.4%	0.4%	0.6%	0.0%	-0.2%	-0.5%	-0.6%
Government budget*	-0.3%	-1.0%	-1.5%	-1.3%	-1.4%	-1.4%	-1.3%	-1.3%
RBA cash rate*	2.83%	3.83%	4.25%	4.35%	4.35%	3.60%	3.35%	3.1%
10-year government bond*	3.7%	3.6%	4.5%	4.3%	4.2%	3.9%	3.6%	3.5%
AUD/USD*	0.657	0.668	0.651	0.659	0.69	0.70	0.71	0.73
Terms of trade	7.2%	-12.7%	-3.1%	4.4%	-2.2%	-7.7%	-6.4%	-3.7%
Employment	5.4%	3.6%	3.1%	2.1%	1.1%	0.9%	1.0%	1.1%
Unemployment rate*	3.6%	3.6%	3.7%	4.2%	4.6%	4.7%	4.7%	4.6%
Dwelling price	-1.7%	0.4%	0.5%	0.2%	0.0%	0.7%	2.1%	3.1%

*=values at end of period

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