

16 June 2017

AUSTRALIAN ECONOMIC DEVELOPMENTS

This week the ABS estimated that Australia's headline unemployment rate dropped to 5.5% in April, with full-time employment and the participation rate also improving (seasonally adjusted). The underemployment rate however, climbed to a record high of 8.8% in May, indicating a high rate of spare capacity among part-time workers (35 hours or less per week), who now comprise 31.9% of the total workforce. Over half of the 194,000 jobs added over year to May have been located in Victoria. More detail on the industries, occupations and locations of work in May 2017 will be released by the ABS next week.

Business conditions in the National Australia Bank (NAB) Monthly Business Survey for May remain relatively buoyant, in line with Ai Group's monthly performance indexes in May. Business confidence eased but remains above average. In contrast, consumer confidence in the Westpac MI Index of Consumer Sentiment moved into firmly negative territory in June, possibly in response to pessimistic reports about economic growth and the economic outlook in early June.

The outlook for tourism and education export earnings continues to improve in 2017, with the number of short-term non-resident visitor arrivals (less than 12 months) entering Australia reaching a record high of 8.5 million over the year to April. Across all industries, the rate of IT and innovation activity by Australian businesses improved in 2015-16. Manufacturers are among Australia's most active businesses online and with regard to innovation activity.

The Queensland Government released its 2017-18 budget this week. More information about this budget is at: <https://www.aigroup.com.au/policy-and-research/mediacentre/releases/>

Australian labour market improves in May, but spare capacity remains high

Australia's labour market appears to be improving, but indicators of spare capacity remain relatively high. The headline unemployment rate declined to 5.5% in May, from 5.7% in April (seasonally adjusted), but the underemployment rate climbed to a record high of 8.8% (trend).

In trend terms¹, the unemployment rate was steady at 5.7%. The total number of people employed increased by 25,200 in May and 194,200 over the year to May. The employment growth rate

¹ The ABS continues to warn about volatility in the seasonally adjusted labour force data. It recommends that 'Trend estimates are considered the best indicators of the underlying behaviour in the labour market.' These data are therefore presented here in trend terms, unless otherwise stated.

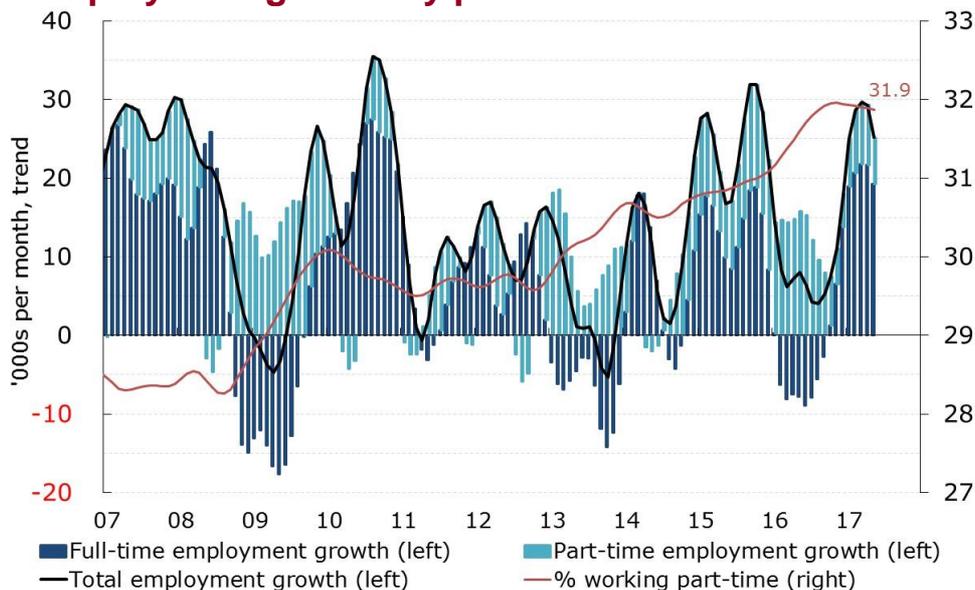
improved to 1.6% p.a. from a recent low of 0.8% in December (but still significantly slower than the recent high of 2.6% p.a. in November 2015). The employment to population ratio improved marginally (+0.1%) to 61.2% of the adult population in May, close to the recent peak of 61.3% in December 2015. The participation rate held steady at 64.8% in May (see table 1).

Table 1: Key labour force numbers, May 2017 (trend)

| trend | people (000's) | % change m/m | % change p.a. |
|--------------------------------|----------------|--------------|---------------|
| Employment | 12,122 | 0.2 | 1.6 |
| Full-time | 8,259 | 0.2 | 1.2 |
| Part-time | 3,864 | 0.2 | 2.5 |
| Aggregate hours worked | - | 0.2 | 1.5 |
| Labour force | 12,851 | 0.2 | 1.6 |
| % of labour force | | | |
| Unemployment | 729.2 | 5.7 | |
| Underemployment | 1,129.6 | 8.8 | |
| Underutilization | | 14.5 | |
| % of population | | | |
| Participation rate | - | 64.8 | |
| Employment to population ratio | - | 61.2 | |

Full-time employment picked up through early 2017, but the monthly pace of growth might already be slowing again (see chart 1). Over the past eight months, full-time employment grew by 123,800, while the number of part-time jobs increased by 50,400. In annual growth terms, part-time employment (35 hours or less per week) is still stronger (+2.5% p.a.) than full-time employment (+1.2% p.a.). The proportion of the workforce employed on a part-time basis remains near record highs (31.9%). Reflecting this large share of part-time workers, the underemployment rate (the proportion of the labour force reporting themselves as employed but willing and able to work more hours) increased to a record high of 8.8% in May (up from 8.7% in the quarter to February), suggesting that there is still significant spare capacity in the labour market.

Chart 1: employment growth by part-time and full-time status (trend)



Across the states, annual employment growth was strongest in Victoria (+3.4% p.a.), with over half of all jobs added over the past year located in Victoria. Employment growth elsewhere was more modest, with jobs in South Australia (+0.9% p.a.), Western Australia (+0.8% p.a.) and New South Wales (+0.6% p.a.) all growing by less than 1.0% over the year to May (trend).

Table 2: Key labour force numbers by state, May 2017 (trend)

| Trend | Annual employment growth | | Unemployment | Participation |
|------------------|--------------------------|------------|--------------|---------------|
| | number y/y | % p.a. | rate % | rate % |
| NSW | 23.6 | 0.6 | 4.8 | 63.2 |
| VIC | 103.9 | 3.4 | 6.1 | 66.1 |
| Qld | 31.1 | 1.3 | 6.3 | 64.7 |
| SA | 6.9 | 0.9 | 7.1 | 62.3 |
| WA | 10.5 | 0.8 | 5.8 | 67.5 |
| Tas | 6.7 | 2.8 | 5.9 | 60.5 |
| NT | 6.9 | 5.2 | 3.2 | 77.7 |
| ACT | 3.3 | 1.6 | 3.5 | 69.9 |
| Australia | 194.2 | 1.6 | 5.7 | 64.8 |

Source: ABS

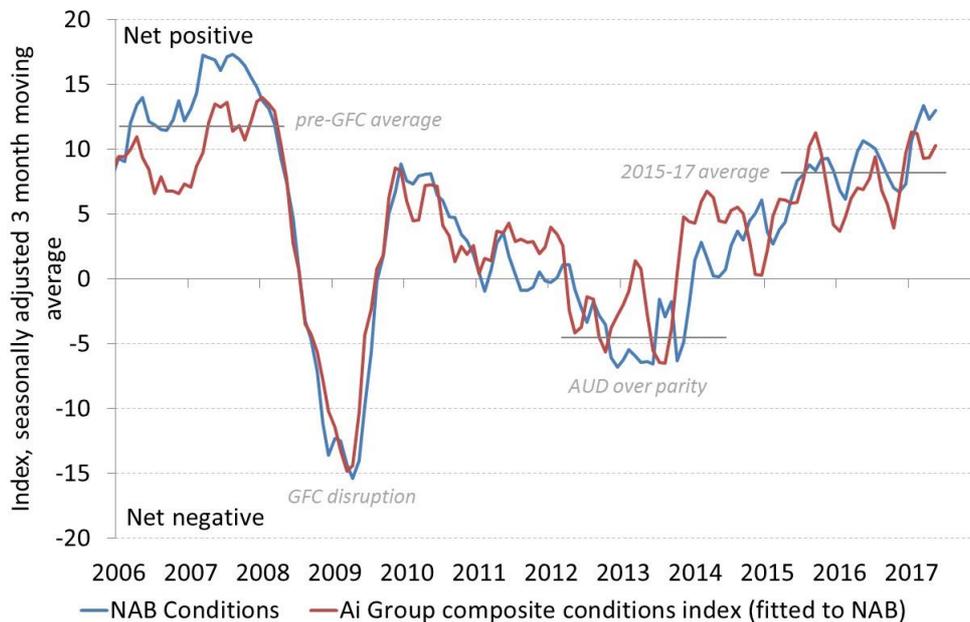
Looking ahead, the SEEK index of online job advertisements show total online job ads increased by 1.9% m/m in May, to be up 8.5% over the year. The strongest growth in May was in the Northern Territory (+9.7% m/m, +9.0% p.a.), followed by Western Australia (+3.2% m/m, +16.1% p.a.) and South Australia (+2.7% m/m, +20.1% p.a.). Online job ads growth was more modest for New South Wales (+1.7% m/m, +4.6% p.a.), Victoria (+1.4% m/m, +9.1% p.a.) and the ACT (+0.9% m/m, -0.5% p.a.). This suggests that employment growth may be returning to the mining-oriented states and balancing out more evenly across the economy.

Business conditions and confidence ease but remain positive in May

The latest **National Australia Bank (NAB) Monthly Business Survey** eased by 1 point to +12 points in May (results over zero indicate 'net positive' conditions in this survey). Even so, conditions remain well above the long-run average for this survey of +5 points. This aligns with the broadly positive results in Ai Group's **Australian PMI®**, **Australian PSI®** and **Australian PCI®** in recent months (see Chart 2). NAB says the recovery from weather related disruptions earlier in 2017 is under way, with conditions likely to improve further in the second half of 2017.

Within the NAB conditions index, trading conditions remained elevated in May (+17), while profitability dropped (to +10 from +14) but remained firmly positive. Employment eased slightly (to +6 from +7), while capacity utilisation increased to 82.4%. Capital expenditure appears to be slowing from higher levels in previous months.

Across industries (in three month moving average terms), finance/business/property services and recreation & personal services continue to outperform other sectors, while conditions in mining, construction, wholesale and transport/utilities remained relatively buoyant. The retail sector remains weak but marginally improved. This pattern was also evident in the **Australian PSI®**, with the retail subsector stable in May after slumping through 2016 and early 2017. Better conditions for manufacturers are apparent in both Ai Group's **Australian PMI®** and the NAB survey in 2017.

Chart 2: Composite PMI, PSI & PCI index and NAB business conditions


Source: Ai Group and NAB

The NAB **business confidence** index fell by 6 points to +7 in May, just above the long-term average (+6). According to NAB, confidence has been less buoyant than conditions of late. This reflects local and international events that are affecting business perceptions of their own outlook. Business confidence was elevated for construction businesses, miners and manufacturers in May. Confidence was more modest for retailers, wholesalers, transport/utilities businesses and finance/business/property services firms and lowest in recreation & personal services.

Consumer confidence heads lower in June

The **Westpac MI Index of Consumer Sentiment** declined further into 'net pessimism' in June, falling to 96.2 points from 98.0 in May (100 divides the optimists from the pessimists in this survey). Consumer confidence has been neutral to slightly negative since mid-2015. The June result is now firmly pessimistic and is the weakest level for this survey since June 2016.

Westpac highlighted that widespread speculation about weak (or negative) economic growth in Australia took a toll on consumer confidence in early June. While the actual results for Australian GDP in Q1 were not as bad as many had expected, annual GDP growth in Q1 was the weakest since 2009, at 1.7% p.a.. This slow growth in national activity (and non-mining incomes) is unlikely to see an uptick in consumer sentiment.

The detailed consumer sentiment data reveals that households expectations about the economic outlook soured in June. Key consumer sentiment indexes for June included:

- 'family finances compared to a year ago' fell by 1.5% to 81.4 points;
- 'family finances over the next 12 months' improved by 3.1% to 102.8 points;

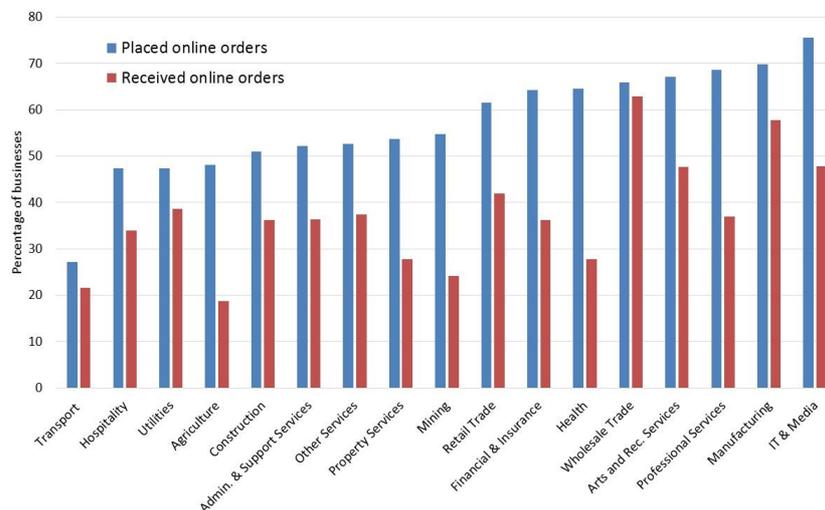
- ‘economic conditions over the next 12 months’ fell by 4.8% to 91.3 points;
- ‘economic conditions over the next 5 years’ fell by 8.3% to 88.6 points;
- ‘time to buy a major household item’ improved by 1.7% to 117.1 points;
- ‘time to buy a dwelling’ improved by 1.0% to 90.9 points; and
- ‘unemployment expectations’ increased by 3.5% (indicating less confidence about job security) to 140.3 points, indicating growing concerns about job security.

Business online activity and innovation improved in 2015-16

Although somewhat dated, new ABS data about businesses’ use of IT and innovation in 2015-16 show a significant and welcome improvement in these key aspects of business activity, with more businesses making use of online channels and participating in innovative activities.

More than half of all Australian businesses had a web presence in 2015-16 (50.1%), while over a third had a social media presence (38.2%). Just 4.7% of Australian businesses did not have access to the internet. On e-commerce, over half of businesses placed orders via the internet (57.0%), while over a third (36.8%) of businesses received orders via online channels. Total income from online ordering in 2015-16 was estimated at \$321 billion, up 12.6% from 2014-15. Perhaps unsurprisingly, larger businesses are more engaged than smaller businesses with these online business activities.

Chart 3: Online ordering and purchasing by Australian businesses in 2015-16



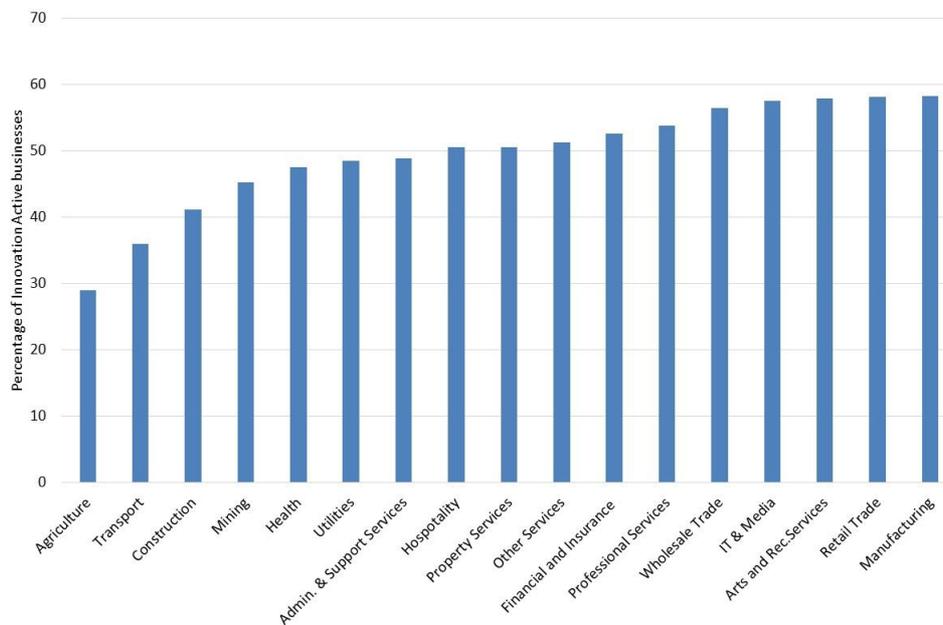
Source: ABS

Looking across industries, the most active online businesses in 2015-16 were in arts & recreation services (75.9% online presence, 69.9% social media presence), IT & media (74.2% web presence, 63.7% social media presence). Manufacturers were also relatively more active online than most other industries, with 65.1% online presence, 69.8% placing online orders and 57.8% receiving online orders.

On innovation, around half (48.9%) of Australian businesses were innovation-active (i.e. undertook any innovative activity) in 2015-16. By industry, manufacturing was the most 'innovative active' sector, with 58.3% of manufacturing businesses active in 2015-16. This was followed by retail trade (58.1%), arts & recreation (57.9%) and IT & media (57.5%). The lowest proportions of 'innovation active' businesses were in agriculture (29.0%), transport (36.0%) and construction (41.1%). Larger businesses were also the most innovation active in 2015-16 (77.0%).

43.1% of business introduced some type of innovation in 2015-16, with the most common type of innovative activity being organisational/managerial processes (22.6%), followed by goods or services innovations (22.4%). Over half (52.7%) of manufacturers introduced some innovation in 2015-16, with over a third (34.7%) introducing operation process improvements.

Chart 4: Innovation active businesses in 2015-16



Source: ABS

This week's data and events, 12 June – 16 June 2017

| Day | Date | Data/event | Data period | Previous release |
|-----|--------|--|----------------|--|
| Tue | 13 Jun | ABS short-term arrivals and departures | Apr (M) | arriv: 746,700; dep: 849,300 |
| | | NAB monthly business survey | May (M) | conditions: +12 points confidence: +7 points |
| Wed | 14 Jun | Westpac-MI consumer confidence index | Jun (M) | 96.2 |
| Thu | 15 Jun | ABS labour force statistics | May (M) | empl. +1.6% p.a. unempl. 5.7% (trend) |
| | | ABS IT use and innovation | 2015-16 (A) | - |

M = monthly. Q = quarterly. H = half-yearly. A = annual. All data are seasonally adjusted unless otherwise noted.

Next week's data and events, 19 June – 23 June 2017

| Day | Date | Data/event | Data period due for release | Previous release |
|-----|--------|-------------------------------------|-----------------------------|----------------------------|
| Mon | 19 Jun | ABS sales of new motor vehicles | May (M) | Apr: +0.3% m/m, +0.1% p.a. |
| | | RBA meeting minutes | Jun (M) | - |
| Tue | 20 Jun | NSW state budget | 2017-18 (A) | - |
| Wed | 21 Jun | SA state budget | 2017-18 (A) | - |
| Thu | 22 Jun | ABS labour force detailed quarterly | May (Q) | - |

M = monthly. Q = quarterly. H = half-yearly. A = annual. All data are seasonally adjusted unless otherwise noted.

Australian economy: latest full-year growth rates and government forecasts

| RBA SoMP (May 2017) | 2015-16 actual | 2016-17 f | 2017-18 f | 2018-19 f | 2019-20 p | 2020-21 p |
|---|-------------------|--------------|--------------|--------------|--------------|--------------|
| GDP, % change p.a., year end | 3.1 | 1.5-2.5 | 2.75-3.75 | 2.75-3.75 | | |
| Unemployment rate, %, year end | 5.8 | 5.75 | 5-6 | 5-6 | | |
| Inflation (CPI), % change p.a., year end | 1.0 | 2.0 | 1.5-2.5 | 2.0-3.0 | | |
| Treasury 2017-18 Budget (May 2017) | | | | | | |
| GDP, % change p.a., year average | 2.6 | 1.75 | 2.75 | 3.0 | 3.0 | 3.0 |
| Household consumption, % p.a., year average | 2.9 | 2.5 | 2.75 | 3.0 | | |
| Dwelling investment, % p.a., year average | 10.6 | 4.5 | 1.5 | -4.0 | | |
| Business investment, % p.a., year average | -10.3 | -6.0 | 0.0 | 3.0 | | |
| Employment growth, % p.a., year end | 1.9 | 1.0 | 1.5 | 1.5 | 1.5 | 1.5 |
| Unemployment rate, %, year end | 5.8 | 5.75 | 5.75 | 5.5 | 5.5 | 5.25 |
| Terms of trade, % change p.a., year end | -10.2 | 16.5 | -2.75 | -4.25 | | |
| Inflation (CPI), % change p.a., year end | 1.0 | 2.0 | 2.0 | 2.25 | 2.5 | 2.5 |
| Wages (WPI), % change p.a., year end | 2.1 | 2.0 | 2.5 | 3.0 | 3.5 | 3.75 |

f = forecast. p = projection.

Sources: ABS various data; RBA *Statement on Monetary Policy* (SoMP), latest quarter; Australian Treasury, *Budget 2017-18* (May 2017).

Australian economy: latest indicators

| Economy | | | | FX and commodity prices (as of Friday) | | |
|-----------------------------|---------|------|---|--|--------------|---|
| RBA official cash rate, % | Jun (M) | 1.50 | - | AUD/USD exchange rate | US\$0.7589 | ▲ |
| Real GDP, % change p.a. | Mar (Q) | 1.7% | ▼ | Oil price (WTI light crude, USD/BBL) | US\$44.40 | ▼ |
| Headline CPI, % change p.a. | Mar (Q) | 2.1% | ▲ | Gold price (USD/OZ) | US\$1,254.45 | ▼ |
| Unemployment rate, % trend | May (M) | 5.7% | - | Copper price (USD/tonne, LME spot) | US\$5,684.00 | ▲ |

Australian Industry Group monthly performance of industry indexes

| | | | |
|-----------------|---------|------|---|
| Australian PMI® | May (M) | 54.8 | ▼ |
| Australian PSI® | May (M) | 51.5 | ▼ |
| Australian PCI® | May (M) | 56.7 | ▲ |

M = monthly. Q = quarterly. All data are seasonally adjusted unless otherwise noted.

Arrows represent direction of movement relative to last week for prices, and last observation for growth rates and indexes.

Sources: ABS various data; Ai Group; Australian Financial Review market prices (as of Thu); London Metals Exchange market prices (as of Fri).

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