2. Domestic Economic Conditions

The labour market remains tight, though the balance between labour supply and demand has improved since late 2022. Strong growth in the working-age population has continued to support employment gains over the first half of 2023. By contrast, economic activity was subdued as high inflation, higher interest rates and earlier declines in wealth weighed on growth. GDP growth has slowed considerably since mid-2022 and GDP per capita declined in the March quarter. Consumption growth was weak in recent quarters and timely indicators suggest it continued to be so in the June quarter. Headwinds to real household income growth remain, but the recent increase in housing prices has supported household wealth.

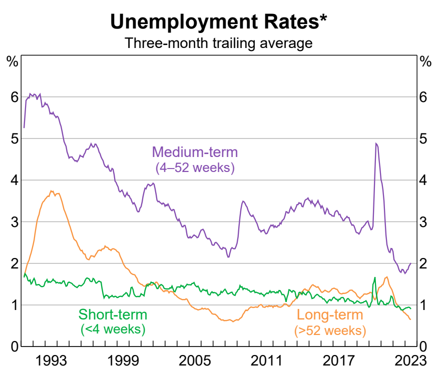
Measures of spare capacity in the labour market remain near multi-decade lows but have started to ease

The labour market was tight during the first half of 2023, though a broad range of measures suggest that the labour market is not as tight as it was in late 2022. The unemployment rate has been near its 50-year low of 3½ per cent since mid-2022 and is below 4 per cent in most states. The medium-term unemployment rate – a measure of cyclical unemployment that typically has the closest relationship with wages growth – has increased slightly in recent months but remains very low (Graph 2.1). The long-term unemployment rate has continued to decline to be around its lowest level in decades; much of the decline over recent years has been driven by long-term unemployed people finding jobs. More recently, there has been an increase in the share of long-term unemployed people leaving the labour force.

Broader measures of labour underutilisation have increased a little in recent months, consistent with the balance between labour demand and supply improving, but they remain near multi-decade lows (Graph 2.2). An increase in the underemployment rate (people with jobs but working fewer hours than they want) has driven most of the increase in these broader measures, though it likewise remains close to its lowest level in several decades.

Tight labour market conditions also manifest through higher job mobility (when a person changes jobs). Actual and expected job mobility have declined in recent months to levels observed immediately prior to the COVID-19 pandemic. Actual job mobility is around pre-pandemic levels in most industries but remains slightly elevated in healthcare. The share of

Graph 2.1



* Seasonally adjusted by the RBA.
Sources: ABS; RBA.

people leaving their jobs voluntarily has declined but remains above pre-pandemic levels; messages from firms in the Bank's liaison program suggest that the rate of job turnover has also declined relative to last year (Graph 2.3).

More people have a job than ever before

Employment growth remained robust in the June quarter, broadly keeping pace with strong growth in the working-age population and resulting in a record high employment-to-population ratio (Graph 2.4). More than one million people have found jobs since February 2020.

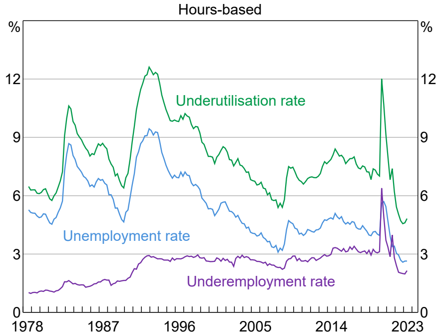
Strong labour demand has encouraged people to enter the workforce, with the participation rate remaining near its record high in recent months. Women and young people have driven the increase in participation since the start of 2020. Strong population growth has contributed to labour supply, as arrivals from overseas have increased to around pre-pandemic rates and fewer people than usual have departed the country (Graph 2.5).

People increasing their average hours worked and taking on second jobs have also played an important role in the adjustment of labour supply to strong demand over recent years. Full-time employment has accounted for all of the increase in employment since early 2020 (Graph 2.6). The share of employed people

Graph 2.2

Labour Underutilisation

Hours-based

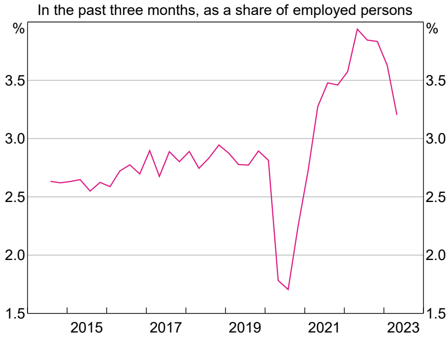


Sources: ABS; RBA.

Graph 2.3

People Voluntarily Quitting Their Job*

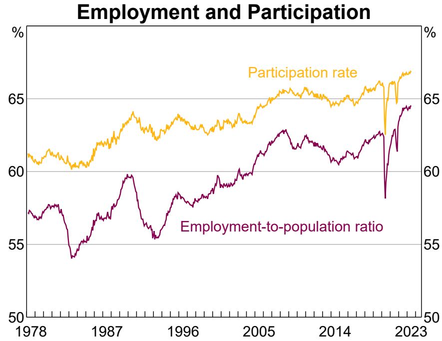
In the past three months, as a share of employed persons



* Excluding retirements and 'other' reasons; seasonally adjusted.
Sources: ABS; RBA.

Graph 2.4

Employment and Participation

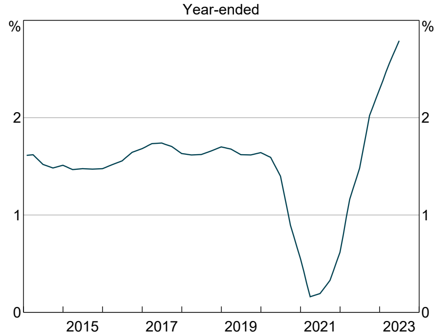


Source: ABS.

Graph 2.5

Working-age Population Growth*

Year-ended



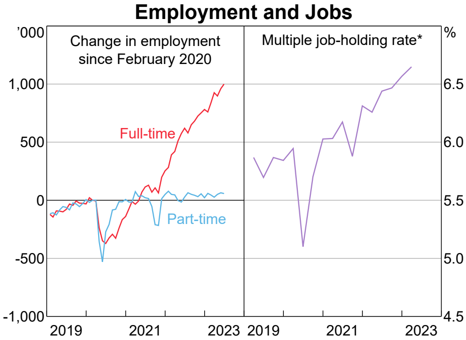
* Population aged 15 years and over.
Source: ABS.

holding more than one job has increased to a record high of 6.6 per cent.

Measures of job advertisements and vacancies have moderated since mid-2022 but remain much higher than prior to the COVID-19 pandemic. There are still nearly as many vacancies as unemployed people, even as the number of vacancies has declined (Graph 2.7). Firms in the Bank's liaison program have reported an improvement in labour availability in some sectors, with some linking this to the arrival of foreign workers, though finding suitable labour continues to be difficult. Hiring intentions of firms in the Bank's liaison program have also eased since mid-2022.

Graph 2.6

Employment and Jobs

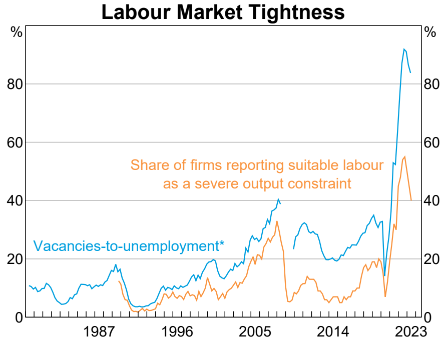


* As a share of employed persons.

Source: ABS.

Graph 2.7

Labour Market Tightness



* The ABS vacancies survey was suspended between May 2008 and November 2009.

Sources: ABS; NAB; RBA.

Domestic activity growth continued to moderate in the first half of 2023

Growth in the Australian economy has slowed significantly since mid-2022 (Graph 2.8). GDP growth in the March quarter was well below the pre-pandemic average as cost-of-living pressures, higher interest rates and earlier declines in wealth weighed on household incomes and consumption growth. The household saving ratio also declined to below its pre-pandemic decade average (Graph 2.9).

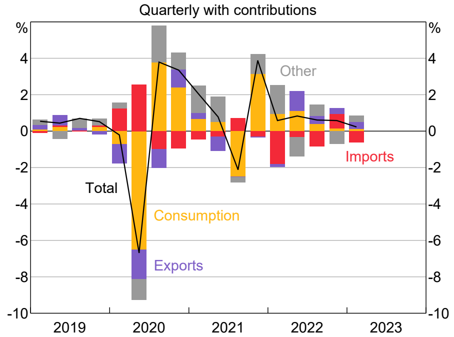
While consumption growth remained subdued and dwelling investment declined, growth in domestic demand in the quarter was resilient due to strong growth in business investment. The post-pandemic rebound in international students and tourists continued to boost net exports; this was more than offset by a bounce-back in goods imports as supply chain issues eased, particularly for passenger vehicles and telecommunications equipment. Timely indicators suggest domestic activity will remain subdued through mid-2023.

Population growth outpaced output growth in the March quarter and so GDP per capita declined (Graph 2.10). In nominal terms, the economy continued to grow strongly in the quarter, driven by growth in domestic prices and the terms of trade.

Graph 2.8

GDP Growth

Quarterly with contributions



Sources: ABS; RBA.

There have been several headwinds to household spending …

Real household disposable income in the March quarter was 4 per cent lower than a year ago (Graph 2.11). Real incomes have been weighed down by continued high inflation, strong growth in tax payments and higher net interest payments, as well as declines in small business incomes (led by decreases in the farm sector). These factors were partly offset by strong growth in labour income. Real household net wealth decreased by 8 per cent over the year to March, driven by lower housing prices.

While higher interest rates have weighed on aggregate household disposable income, the effects are being felt unevenly. Households that are net savers are receiving higher returns on their deposits, which is boosting their disposable income, while households that are net borrowers are facing higher interest payments (Graph 2.12). Aggregate interest receipts and payments will increase over the year ahead as the effect of earlier increases in the cash rate continue to be passed through to interest rates faced by households (see Chapter 3: Domestic Financial Conditions).

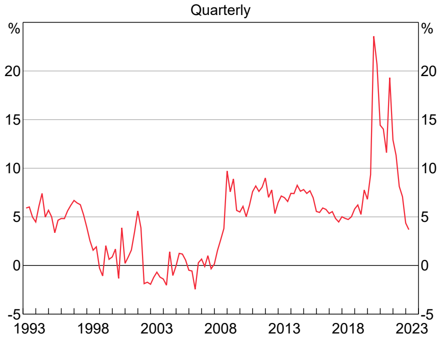
Growth in household consumption has been weak

Household consumption growth has slowed materially since mid-2022, with average growth of only ¼ per cent in recent quarters. This is well below the pre-pandemic average. The

Graph 2.9

Household Saving Ratio*

Quarterly



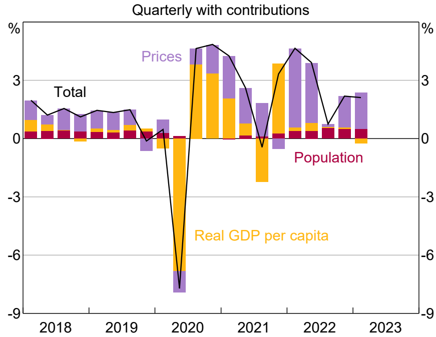
* Saving as a share of disposable income; net of depreciation.

Sources: ABS; RBA.

Graph 2.10

Nominal GDP Growth

Quarterly with contributions

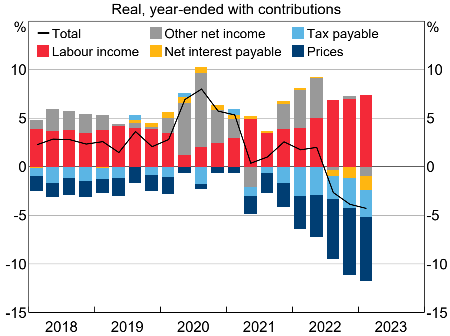


Sources: ABS; RBA.

Graph 2.11

Household Disposable Income Growth

Real, year-ended with contributions

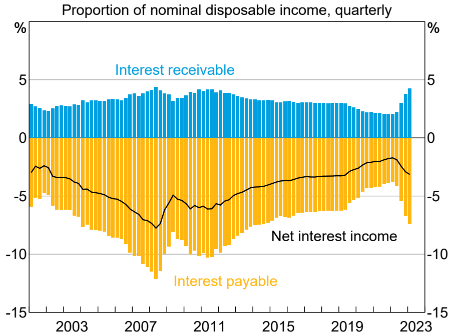


Sources: ABS; RBA.

Graph 2.12

Household Net Interest Income

Proportion of nominal disposable income, quarterly



Sources: ABS; RBA.

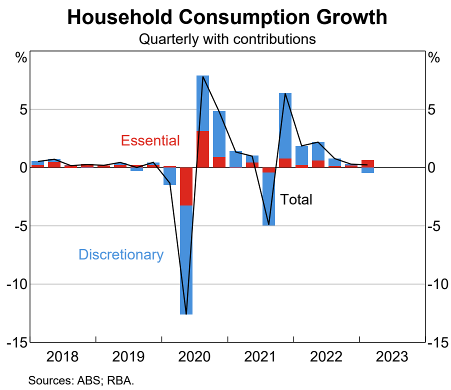
slowdown has been driven by weaker consumption growth for discretionary items (Graph 2.13). A range of timely indicators suggests that household consumption growth remained subdued in the June quarter. Retail sales values increased a little in the quarter but have been broadly unchanged since late last year; sales have been declining in real terms over this period (Graph 2.14). These outcomes are consistent with the weak conditions reported in liaison (see Box B: Insights from Liaison).

Sales of new cars have been relatively resilient to the softness in consumer spending. Cars are one of the categories of consumption most sensitive to changes in housing wealth; however, a large backlog of orders, as a result of earlier supply chain issues, has supported sales even as household wealth has declined. Car sales to households have remained strong in recent months, supported by orders that were placed several months earlier. Wait times for some models remain much longer than before the pandemic, although the ongoing easing in supply constraints could see more demand realised in sales in coming months.

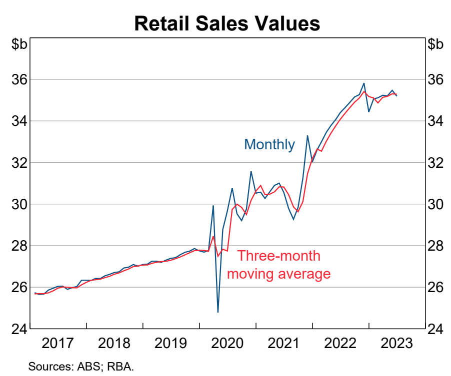
Despite slowing growth, household consumption per capita was close to its pre-pandemic trend level in the March quarter when excluding international travel (Graph 2.15). Nominal spending by Australian tourists overseas has picked up in recent months but remains around 20 per cent below pre-pandemic levels; real spending is even further below pre-pandemic levels because of strong price increases since 2019.

In contrast to the subdued growth in Australians' spending overseas, the recovery in international tourists and students coming to Australia continued to support economic activity (spending by tourists and students is treated as services exports rather than consumption in the national accounts). A large number of people entered the country to commence their studies in early 2023; the total number of international students in Australia is back to around pre-pandemic levels (Graph 2.16). Inbound tourism has also increased further in recent quarters but

Graph 2.13



Graph 2.14



Graph 2.15

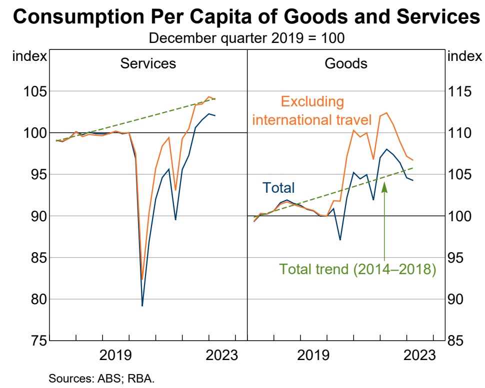


Table 2.1: Growth in Housing Prices

Per cent, seasonally adjusted

	July	June	May	Since recent peak	Year-ended	Since Feb 2020
Sydney	1.3	1.5	1.3	–8	–2.3	16
Melbourne	0.6	0.8	0.6	–8	–4.1	3
Brisbane	1.5	1.1	0.9	–7	–6.4	31
Adelaide	1.3	0.9	0.6	0	0.9	46
Perth	1.1	1.0	1.0	0	3.2	29
Darwin	0.2	0.1	0.5	–2	–1.2	30
Canberra	–0.2	0.2	0.3	–9	–8.0	26
Hobart	0.2	–0.6	–0.2	–13	–11.5	19
Capital cities	1.1	1.2	1.0	–5	–2.8	16
Regional	0.5	0.5	0.3	–6	–5.7	33
National	1.0	1.0	0.9	–5	–3.5	20

Sources: CoreLogic; RBA.

remains below the levels seen prior to the pandemic, because of fewer tourists from China and constrained airline capacity.

The rebound in housing prices is supporting household wealth

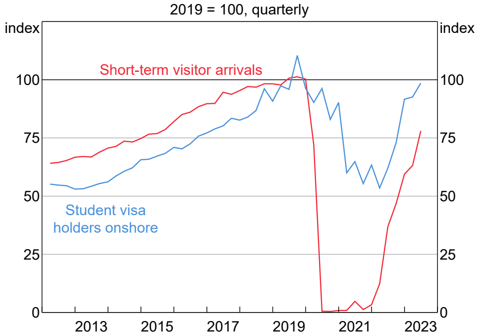
National housing prices have increased over recent months, following an 8 per cent decline from the April 2022 peak (Graph 2.17, Table 2.1). These increases have been broadly based across capital cities and most regional areas and have provided support to household wealth. The rebound in housing prices reflects a combination of stronger demand, partly due to the pick-up in population growth, and ongoing limited supply of new and established dwellings.

Other measures of housing market activity have been mixed in recent months. Housing turnover and residential listings are at low levels, although new listings have increased in some capital cities in recent months and auction clearance rates are higher than at the start of the year. Survey measures of housing price expectations have risen to be above their long-run average.

Graph 2.16

Inbound Travellers*

2019 = 100, quarterly



* Seasonally adjusted by the RBA.

Sources: ABS; Home Affairs; RBA.

The rental market remains very tight

Rental vacancy rates remain below their long-run average levels in Melbourne and Sydney and are around record lows in most other capital cities. Strong population growth has added to demand for rental properties, particularly in Sydney and Melbourne. Average household size has increased over recent months in capital cities, likely reflecting tight rental market conditions; this partially unwinds the decline in average household size observed since the onset of the COVID-19 pandemic (Graph 2.18). Average household size outside of capital cities has already returned to pre-pandemic levels.

Growth in advertised rents (for new leases) has been strong in capital cities, with advertised rents rising at their fastest pace in at least two decades in Sydney and Melbourne (Graph 2.19). By contrast, advertised rents growth has eased in most regional areas over the past year. Rents have grown more strongly for units than houses. Rental yields remained above pre-pandemic levels in all capital cities, though they have declined for Sydney and Brisbane in recent months as increases in housing prices have outpaced growth in rents.

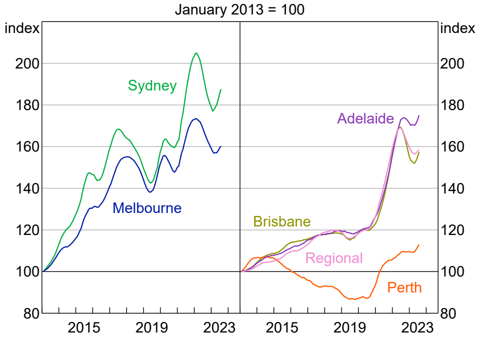
Capacity constraints continue to weigh on dwelling investment

Dwelling investment has declined by 5 per cent over the past year (Graph 2.20). While constraints on the supply of materials have eased, poor availability of tradespeople – particularly for the latter stages of construction – has continued to limit the pace of work done. These delays have contributed to the elevated pipeline of residential construction and, along with substantial increases in costs, have reduced cash flows for some firms and increased insolvencies in the industry over the past year. Construction insolvencies in the June quarter were at their highest level since the series began in 2013.

Graph 2.17

Housing Prices

January 2013 = 100

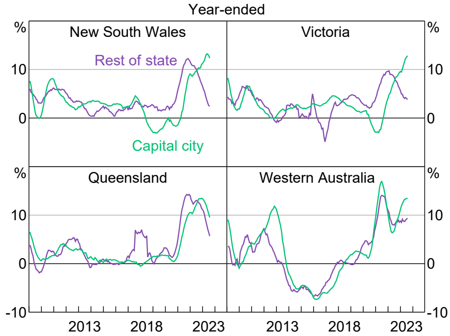


Sources: CoreLogic; RBA.

Graph 2.19

Advertised Rents Growth*

Year-ended

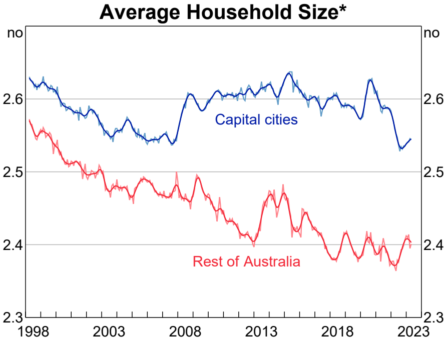


* Hedonic; seasonally adjusted.

Sources: CoreLogic; RBA.

Graph 2.18

Average Household Size*



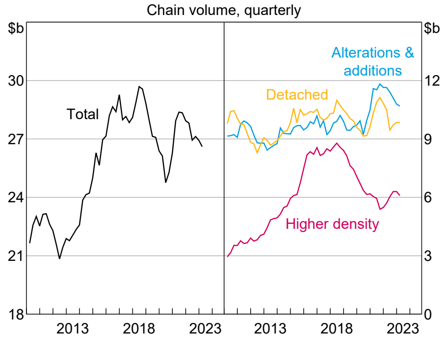
* Smoothed lines are 13-period Henderson trends.

Sources: ABS; RBA.

Graph 2.20

Private Dwelling Investment

Chain volume, quarterly



Sources: ABS; RBA.

Demand to purchase new detached dwellings has remained weak. Indicators such as building approvals, greenfield land sales and new home sales remained steady at low levels in the June quarter. Builders in the Bank's liaison program point to a range of factors weighing on demand, including higher interest rates, uncertainty around the cash rate path, higher construction costs and poor buyer sentiment due to construction delays and insolvencies. The recent weakness in demand for new detached dwellings is expected to weigh on dwelling investment once the backlog of dwelling construction is worked through (Graph 2.21).

Business investment remains strong but sentiment continues to ease

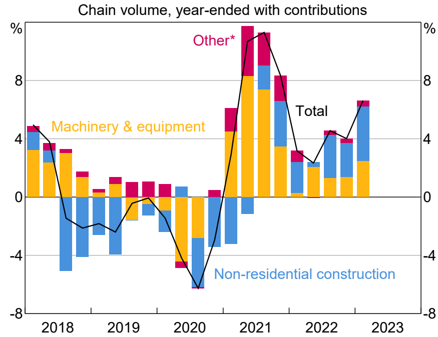
Business investment has increased strongly over the past year (Graph 2.22). Investment in machinery and equipment drove the pick-up in investment in the March quarter, reflecting strength in the agricultural, manufacturing, mining and transport sectors. Non-residential construction investment also increased, driven by expenditure on renewable and electricity projects in the eastern states.

Survey measures of investment intentions generally point to a positive short-term outlook for business investment, although the medium-term outlook has weakened. Measures of business conditions have softened further over recent months and business confidence is a little below its long-run average. The ABS Capital Expenditure Survey showed that, in aggregate, firms have revised down their expectations for investment in the 2023/24 financial year and nominal investment intentions are similar to 2022/23 (Graph 2.23). Information from the Bank's liaison program suggests that some firms anticipate delays to investment projects resulting from labour shortages, and some small firms are focusing on conserving cash rather than investing.

Graph 2.22

Private Business Investment Growth

Chain volume, year-ended with contributions

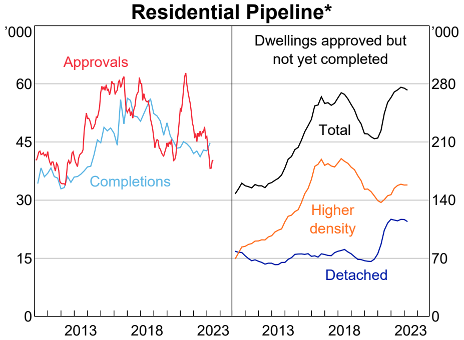


* Includes cultivated biological resources (mainly livestock, vineyards and orchards), computer software, research & development, mineral exploration and artistic originals.

Sources: ABS; RBA.

Graph 2.21

Residential Pipeline*



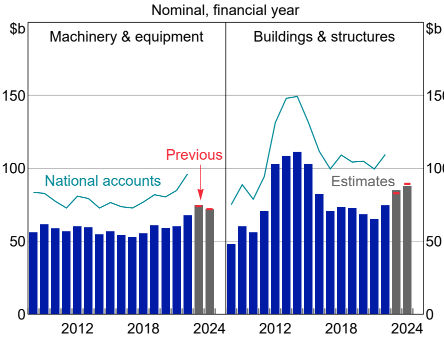
* Quarterly data except building approvals, which sum the three latest monthly observations.

Sources: ABS; RBA.

Graph 2.23

Capital Expenditure Intentions*

Nominal, financial year



* Estimates are firms' expected capital expenditure; adjusted for past average differences between expected and realised spending.

Sources: ABS; RBA.

Public demand growth has slowed

Public demand growth continued to slow in the March quarter as health expenditure associated with the COVID-19 pandemic continued to wind down (Graph 2.24). Public consumption as a share of nominal GDP remains at a high level compared with the pre-pandemic period, supported by public spending programs such as the National Disability Insurance Scheme and aged care. A large pipeline of infrastructure projects is expected to support public investment going forward.

The 2023/24 Australian Government Budget and various state budgets have reported an upgrade in the consolidated underlying cash balance in 2022/23 and smaller projected deficits over coming years (Graph 2.25). Higher commodity prices and a stronger-than-expected labour market have driven the improvement in budget positions.

Resources exports have been volatile in recent quarters

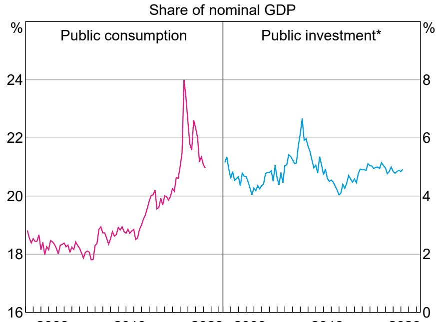
Net trade detracted slightly from GDP in March, as strong growth in goods imports more than offset growth in services exports (Graph 2.26). While rural exports rose following an exceptional year of growing conditions, this was offset by weakness in coal exports due to maintenance disruptions in the March quarter. Information from port authorities and trade data indicate that coal exports rebounded in the June quarter, with thermal coal exports to China returning to pre-pandemic levels.

Lithium export values have increased substantially in recent years to be Australia's fourth largest mineral export (behind coal, iron ore and gold) (Graph 2.27). The increase in lithium export values has been driven by higher prices on the back of increasing demand for

Graph 2.24

Components of Public Demand

Share of nominal GDP



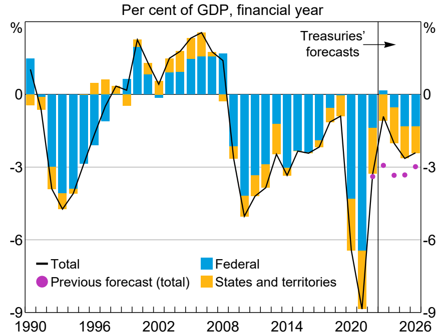
* Adjusted for second-hand asset transfers between public and other sectors.

Sources: ABS; RBA.

Graph 2.25

Consolidated Government Underlying Cash Balance

Per cent of GDP, financial year

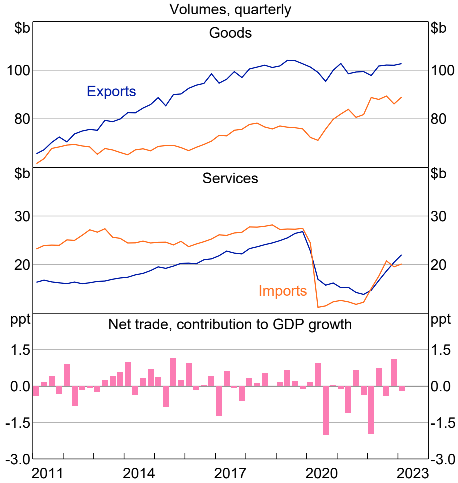


Sources: ABS; Australian Treasury; RBA; state and territory treasuries.

Graph 2.26

Trade in Goods and Services

Volumes, quarterly



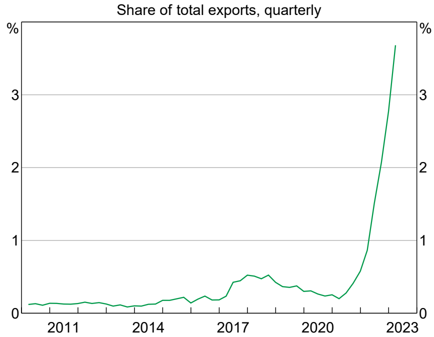
Sources: ABS; RBA.

batteries; export volumes have also increased as new mines have commenced production. ✠

Graph 2.27

Lithium Exports

Share of total exports, quarterly



Sources: ABS; RBA.