

Media release

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Leading Index remains subdued

The annualised growth rate of the Westpac–Melbourne Institute Leading Index, which indicates the likely pace of economic activity three to nine months into the future, was 2.3% in December 2011, below its long term trend of 3.0%. The annualised growth rate of the Coincident Index which gives a pulse of current activity was 2.5%, also below its long term trend of 3.0%.

Westpac Senior Economist, Matthew Hassan, commented, "Despite a slight up-tick in December, the growth rate in the Index remains relatively subdued after dropping back sharply from a 4.6% pace recorded in August. There was a loss of momentum over the second half of last year with the growth pulse heading into 2012 materially below trend. That said, the Index is pointing to sub-par growth rather than a more pronounced weakening. Growth in the Index is still well above the extreme lows seen in 2008 and in the early-90s recession, and the levels seen in mid-cycle slowdowns in 2000-01 and the mid-90s."

"The Index growth rate swung from above trend to below trend over the second half of 2011, falling from 3.6% in July to 2.3% in December. The main components driving that slowdown were: overtime worked (–0.9ppts); manufacturing prices (–0.7ppts); the All Ordinaries index (–0.4ppts) and US industrial production (–0.2ppts). These

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negatives were partially offset by stronger positive contributions from productivity (+0.5ppts) and growth in real money supply (+0.3ppts). The positive contribution from company profits and the drag from dwelling approvals were unchanged over the period.

Mr Hassan said: "Just like the real economy, the Leading Index was buffeted by severe weather events at the start of 2011 with a sharp drop and subsequent rebound. Those effects have now mostly washed out of the measure which suggests underlying growth momentum was fairly lacklustre through the year.

"For the December month, the level of the Index rose 1.3 points from 282.1 in November to 283.4. Two of the monthly components rose and two fell: the real money supply rose 1% and US industrial production was up 0.4%, but the All Ordinaries dropped 1.5% and dwelling approvals were down 1.0%.

"The growth rate of the Coincident Index also continues to track well below trend. The level of the Index rose from 270.4 to 270.6. Real retail trade continued to decline, falling 0.3%, employment fell 0.3% and the unemployment rate was unchanged. As with the Leading Index, the growth rate in the Coincident Index is below trend but still comfortably above lows seen in recessions and mid-cycle slowdowns.

"The Board of the Reserve Bank next meets on March 6. With the RBA Governor indicating that demand conditions would have to "weaken materially" and a surprisingly strong January labour market report, a March move is highly unlikely. However, we still expect the current easing cycle to see further rate cuts as global growth concerns re-emerge and domestic fragility becomes more apparent across non-mining sectors and the labour market. Overall, we expect a further 50bps in easing with the next 25bp cut likely to come in May", Mr Hassan said.

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