June 2017

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| **Scope:** This monthly newsletter outlines economic and financial developments in Victoria, nationally and globally. | **By David Martine, Secretary, Department of Treasury and Finance** |

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| **Highlights**   * Growth in Victorian state final demand outpaced all other states in both quarterly and annual terms in March. * Victorian labour market conditions remain strong. * Melbourne's house price growth was the highest among the mainland state capitals in May. * The US Federal Reserve raised rates in June as expected. The Fed also introduced its plan for reducing its balance sheet over time. * China’s manufacturing sector remains robust, with growth maintained by increased spending on infrastructure and property construction. * The UK election resulted in a hung parliament in June with no party able to win a majority. | |
|  | Domestic developments | |

The Victorian economy had another strong quarter in March following the rebound in the December quarter.

Victoria’s state final demand (SFD) grew by 1.4 per cent in the quarter and 4.5 per cent over the year to the March quarter. This represented the highest growth in state final demand of all the states. The quarterly growth was led by public investment (16.8 per cent), followed by dwelling investment (1.6 per cent), government expenditure (1.0 per cent) and household consumption (0.7 per cent). However, business investment declined 3.7 per cent due to a large asset transfer to the public sector.

International trade continued to drag on growth as imports grew faster than exports. Victorian goods and services export volumes increased by 1.8 per cent (7.0 per cent over the year) and imports of goods and services increased 2.8 per cent in the March quarter.

Victorian labour market conditions are strong. Employment in Victoria grew for the fourth consecutive month in May. Over the year, Victorian employment rose by 3.9 per cent (118 800 persons).

The labour force participation rate remained steady at an elevated 66.1 per cent in May which contributed to the unemployment rate drop of 0.1 percentage points to 6.0 per cent.

Surveyed conditions for business investment remain solid in Victoria and bodes well for future investment activity. **NAB** **business conditions** for Victoria were upbeat at +10 index points in May and **business confidence** remained positive at +3 index points.

Residential property prices continue to rise with the **CoreLogic RP Data Home Value Index** for Melbourne increasing by 11.5 per cent over the year to May. Melbourne's annual price growth for residential property was the highest among the mainland state capitals.

**Building approvals** rebounded in April led by increases in both residential and non‑residential building approvals. The value of non-residential building approvals increased by 52.8 per cent and residential building approvals rose by 2.3 per cent.

Victoria's value of **retail sales** grew by 1.0 per cent in April led by growth in general merchandise. Over the year, the value of retail sales increased by 4.2 per cent.

The RBA, in its latest decision, has left the **cash rate** unchanged at 1.50 per cent. The RBA Board noted that the unchanged policy stance is consistent with sustainable growth in the economy and the achievement of the inflation target.

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| H:\temp\Economic Policy Newsletter\Stockmarket.png | Global developments |

In June, the **Federal Reserve** raised rates by 25 bps to 1.00‑1.25 per cent, in line with market expectations. The Fed also announced plans to gradually start reducing its bond holdings later this year, which could cause long-term rates to rise.

**US** economic indicators were subdued in the past four weeks. Real GDP growth in the first quarter of 2017 was revised up 0.5 percentage points but remained weak at an annual rate of only 1.2 per cent. The revision reflected higher business investment, consumer spending and state and local government spending.

The US labour market continues to improve. **Non-farm payrolls** increased by 138 000 in May and the unemployment rate declined to its lowest level (4.3 per cent) since May 2001.

In early June, the **US** President announced his intention to withdraw the US from the Paris climate accord, a landmark global agreement to lower greenhouse gas emissions and minimise the impact of climate change.

China’s manufacturing sector remains robust. The official Manufacturing **Purchasing Managers' Index (PMI)** remained steady at 51.2 in May. China’s recent growth is being maintained by increased spending on infrastructure and property construction including the ‘belt and road’ initiative.

**China’s** inflation rate reached a four‑month high in May.Consumer prices rose 1.5 per cent over the year to May 2017, driven mostly by increases in non‑food items.

Economic activity in the **Euro zone** expanded for the 16th consecutive quarter in March. Real GDP grew by 1.7 per cent over the year to the March quarter 2017. The labour market also continues to improve with the unemployment rate falling to its lowest level since 2009.

The **UK** election in June resulted in a hung parliament with no party able to win a majority. The incumbent Prime Minister Theresa May intends to stay on as the Conservatives’ leader and advance Brexit negotiations but there is some uncertainty about her role.

The **Japanese** economy remains weak as household consumption has failed to pick up. The economy advanced by only 0.3 per cent in the March quarter 2017, below preliminary estimates of 0.5 per cent.

*Note: All data reported in the newsletter is as at 25 June 2017.*

Movements\* in financial data over the past month\*\*

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|  | 31-May-17 | 28-Apr-17 | Change |
| AUD/USD | 0.7450 | 0.7475 | -0.3 per cent |
| ASX 200 | 5,724 | 5,924 | -3.4 per cent |
| S&P 500 | 2,412 | 2,384 | +1.2 per cent |
| 90 day bank bill rate | 1.73 | 1.74 | -0.01 percentage points |
| 10 year Commonwealth bond rate | 2.39 | 2.58 | -0.19 percentage points |

*Notes: \*Changes are based on the movement in unrounded figures. \*\*Month-end dates are the last trading day of the month.*

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