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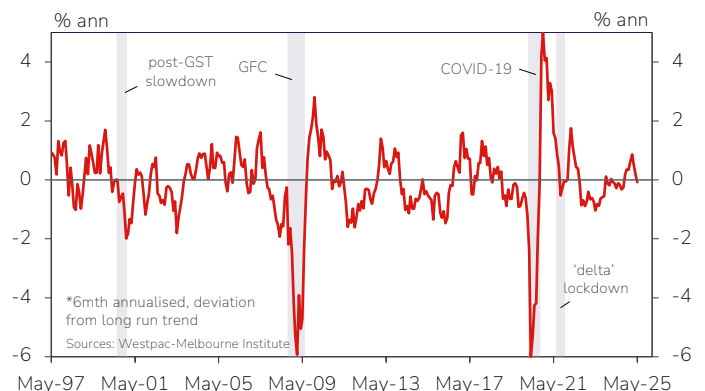
WESTPAC-MI LEADING INDEX BULLETIN

Latest insights into economic momentum

Key points

- Leading Index growth rate dips back into negative at -0.08% .
- Domestic factors becoming more prominent in slowing.
- 'Shaky' performance set to continue over the second half of 2025.

Westpac-MI Leading Index



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Leading Index shows growth dropping back below trend



Matthew Hassan
Head of Australian Macro-Forecasting

The six-month annualised growth rate in the Westpac–Melbourne Institute Leading Index, which indicates the likely pace of economic activity relative to trend three to nine months into the future, dropped to -0.08% in May from 0.19% in April.

The growth pulse has shown a significant deterioration since February, with May marking the first below-trend read since September last year. The detail suggests what was mainly an external drag on momentum is becoming more domestically focussed. That said, some of these drags are likely to be temporary.

The overall picture is consistent with Australia's gradual recovery entering a shakier period. Westpac expects GDP growth to reach 1.7% yr by year-end, a sub-par result by historical standards and marked down slightly from a month ago. Weaker global growth and uncertainty around trade policy are combining with a bumpier handover in domestic drivers as government-driven activity moderates and private demand is slower to pick up," commented Westpac Economics' Head of Australian Macro-forecasting, Matt Hassan.

The Leading Index growth rate has deteriorated over the last six months, dropping from $+0.35\%$ in November to -0.08% currently. Six of the eight components have contributed to the turnaround.

Notably, the biggest shifts have come from domestic and sentiment-related indicators. Over three quarters of the 0.43ppt deterioration has come from a weakening in dwelling approvals (-0.21ppts) and slowing growth in hours worked (-0.13ppts). Softer reads from the Westpac–Melbourne Institute Consumer Expectations Index and the Westpac–Melbourne Institute Consumer Unemployment Expectations Index have taken an additional 0.24ppts off the headline growth rate over the same period.

Other components have been more mixed. Financial markets have been volatile over the year to date. Currently that volatility is seeing a bigger drag from the S&P/ASX200, which has taken an additional -0.16ppts off the index growth rate and a small negative contribution from commodity prices (albeit slightly improved on six months ago). Those drags should dissipate near term as the share market recovery feeds into six-month growth rates although some commodity prices are seeing more volatility due to escalating conflict in the Middle East.

The Westpac–Melbourne Institute Leading Index of Economic Activity is designed to assist in identifying turning points in the economy. The index combines variables that reflect different aspects of the economy into a single index that generally produces a more reliable cyclical indicator than any single component taken individually. The Leading Index of Economic Activity provides advance information on the state of the economy and gives early warnings of cyclical turning points.

Interestingly, the main positive has come from a lift in US industrial production, which has added 0.29ppts to the Index growth rate. The clear caveat here is that protectionist tariff policies are likely to see US economic growth weaken near term and will also limit the extent to which any growth benefits the wider global economy and Australia.

The Reserve Bank Monetary Policy Board next meets on July 7–8. The Board's increased confidence around inflation allowed for a further 25bp rate cut in May. With the March quarter national accounts showing growth tracking slowly domestically and the latest Leading Index read suggesting conditions will remain subdued through to year-end there is a solid case for further policy easing. However, we expect the RBA to continue to proceed cautiously given its evolving view of the economy and the tightness of the labour market. As such we expect the Board to leave the cash rate unchanged at its July meeting, with the next 25bp cut coming in August, once the RBA has refreshed its economic forecasts.



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