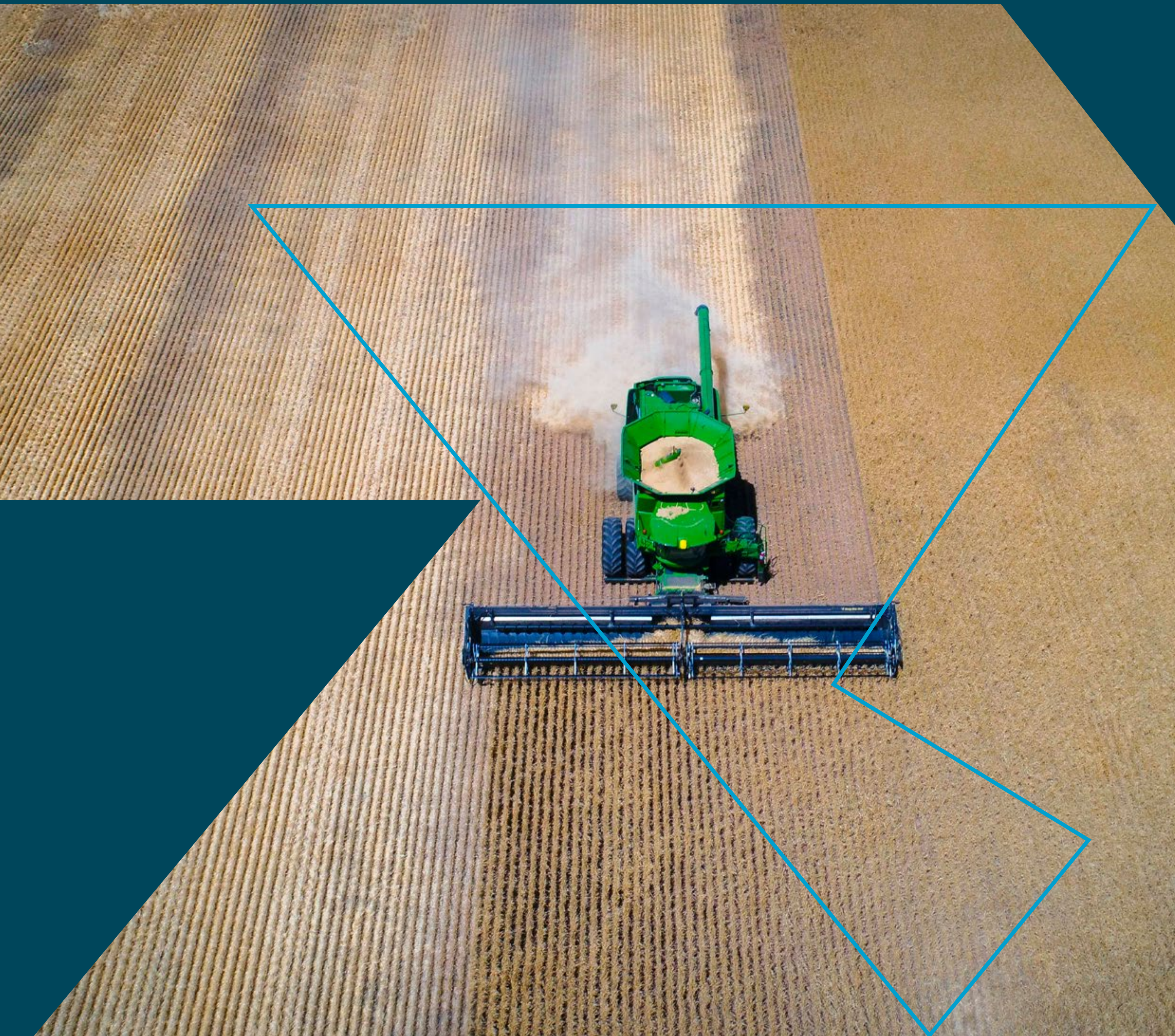

Economic Briefing June 2024

WALGA

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Overview

Since the last Economic Briefing, the pace of the decline in inflation has slowed, pushing out expectations of interest rate cuts and further narrowing the already 'narrow path' to the Reserve Bank of Australia's (RBA) inflation target. Economic growth has also slowed, whilst the labour market is yet to significantly loosen.

The May Federal and Western Australian budgets had a strong focus on providing cost of living relief that did not add to inflationary pressures and on investing in infrastructure, housing and industry development.

Western Australia continues to outperform the nation, with a strong budget position and a robust domestic economy. The global economic slowdown remains a risk for WA given the importance of the resources sector and its exposure to global shocks.

The Federal Budget forecast a second consecutive surplus, with deficits predicted in future years. Expenditure is focused on addressing the cost of living, increasing housing supply and supporting industry development. Slow growth in the **Australian economy** is forecast across the forward estimates in-line with a subdued global economy.

WA Treasury forecast a sixth consecutive surplus of $3.2 billion in 2023/24 in the State Budget. The **WA economy** is the strongest in the nation, with public and private investment driving economic growth. This is expected to continue, albeit at a slower pace.

Inflation is falling slower than expected, however the RBA has reinforced it will do what is necessary to bring inflation back into the target range. Rising rents and house prices are major drivers of inflation in WA and across the nation.

WA's **labour market** is the tightest in Australia with an unemployment rate of 3.7%. As a result, wages have been growing quickly, although there are early indications that they may have peaked. The slowing economy and the impact of rate rises are expected to increase unemployment in the coming quarters.

WA's **population** increased 3.3% in 2023, the fastest in the nation. While new arrivals are filling skills shortages in the labour market, **housing** has not kept pace, resulting in rents and house prices skyrocketing.

The **Local Government Cost Index** (LGCI) increased 0.7% in the March quarter and 3.3% in the last year. Looking forward, LGCI growth is forecast to ease to 3.1% in 2024/25. The LGCI is now being driven by wages growth as the growth in construction costs slows.

Note

The significant challenges of forecasting in the current economic environment, mean **the LGCI should be used with caution**. The LGCI will be subject to revisions in coming months, as the impact of major economic shocks such as COVID-19, wars in Ukraine and the Middle East, and the impact of recent rate rises become clearer. An increase in wage pressures may also see the index revised higher.

It is important that Local Governments take into account their own local issues and experiences when considering cost pressures. It would also be prudent for Local Governments to prepare for multiple scenarios for cost increases in coming years.

Australian Budget and Economic Update

Key points

- **The Federal Budget forecast a second consecutive surplus for 2023/24 and deficits over the forward estimates**
- **Expenditure is focused on addressing the cost of living, increasing housing supply and supporting industry development**
- **Support for Local Governments was mixed, with the promise of a 'fair increase' in Financial Assistance Grants not delivered**
- **Slow economic growth is forecast across the forward estimates in-line with a subdued global economy**

The Federal Budget was handed down in May against a backdrop of global economic uncertainty and still elevated levels of inflation. The focus of the Budget was on providing cost of living relief, increasing housing supply and investing in new industries.

The Budget forecast a $9.3 billion surplus for 2023/24. This is the first time since 2007/08 that consecutive surpluses have been recorded. The surplus was driven by higher tax revenues from a strong labour market, elevated commodity prices, and increased company taxes. However, these surpluses are expected to be short-lived with the Budget falling back into deficit in 2024/25 with no path back to surplus over the forward estimates.

Forecast deficits over the out years are attributed to a significant rise in spending, which is expected to increase by 11% over the next two years, outpacing a 4% growth in revenue during the same period. This trajectory will likely push national debt above $1 trillion by 2026, posing challenges for managing escalating interest payments.

Measures to address the cost of living pressures on households include adjustments to tax cuts, a $300 energy bill rebate (in addition to State Government rebates), increased rent assistance and initiatives to reduce medicine costs. Additionally, substantial investments are earmarked for housing, healthcare, mental health, aged care, and disability support.

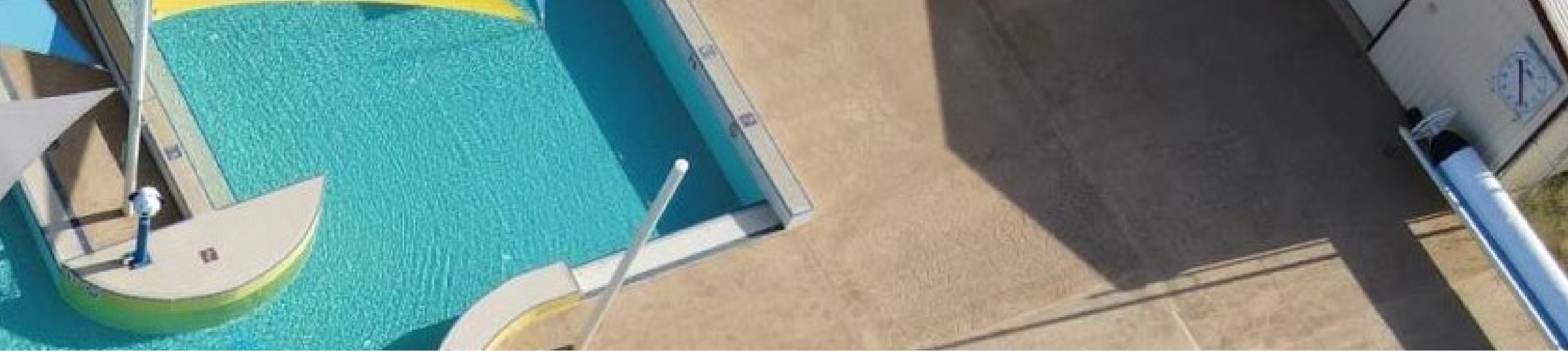
A cornerstone of the budget is the 'Future Made in Australia' policy, aiming to bolster industry competitiveness in global markets through $22.7 billion in investments over the next decade. This policy focuses on clean energy and advanced manufacturing sectors.

Funding for Local Governments in the Budget was mixed. Financial Assistance Grants increased only slightly, falling well short of the Government's election promise of a 'fair increase'. There has been a moderate increase in the Black Spot Program, while the Roads to Recovery Program has been boosted significantly, doubling by 2027/28. The Safer Roads and Infrastructure Program has seen a modest increase in funding.

The Local Roads and Community Infrastructure Program continues to be wound down. Two new funds have been announced, the Active Transport Fund ($100 million over four years) and the Regional Roads Australia Mobile Program ($50 million over two years) aimed at improving mobile telecommunications on major roads. For more information see WALGA's Federal Budget night analysis on the WALGA website.

The Budget's Economic Outlook was cautious, forecasting subdued global economic growth in coming years. Particular concerns include the slowdown in the Chinese economy driven by its struggling property sector, the ongoing battle against inflation, and heightened geopolitical tensions and the consequent flow on effects to supply chains and global trade.

Gross Domestic Product (GDP) is forecast to end the year up just 1.75%, however this prediction is already at risk, with the economy growing just 0.1% in the March quarter. GDP per capita has now fallen for five consecutive quarters.

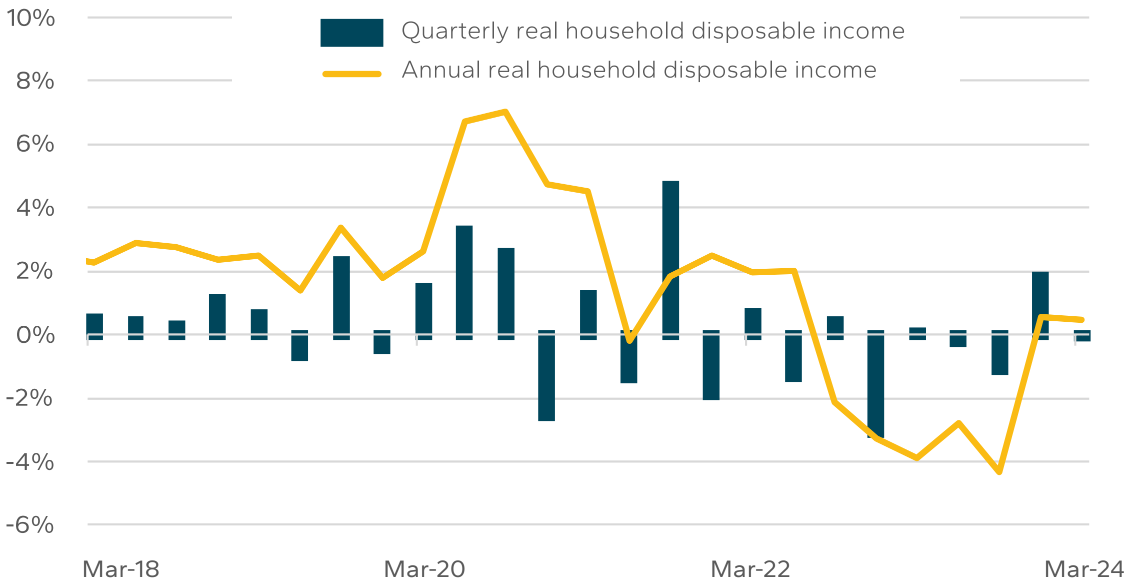


Looking forward, the Australian economy is forecast to continue to grow moderately, up 2.0% in 2024/25 and 2.25% in 2025/26. As this is below the current annual population growth of 2.5%, there is a risk that GDP per capita will continue to go backwards.

Despite the growing economy, household living standards went backwards between September 2022 and September 2023 as measured by Real Household Disposable Income. Since then, inflation has fallen and wages have risen leading Real Household Disposable Income back into positive territory, reaching 0.5% annualised growth in the March quarter. Notably this is only a return to the level of Household Disposable Income in 2020. Households have almost stopped saving with the Household Saving Ratio averaging just 1.1% over the last 12 months, well below the pre-pandemic average of 6%. The lowering of household living standards will have flow on impacts to communities and local economies.

Real Household Disposable Income, Australia, Annual v Quarterly % Change

SOURCE: ABS; WALGA



WA State Budget and Economic Update

Key points

- **The State Budget forecast a sixth consecutive surplus of $3.2 billion in 2023/24**
- **The WA economy is the strongest in the nation with public and private investment driving economic growth**
- **Economic growth is expected to continue but at a slower pace**

The Western Australian Government's 2024/25 Budget handed down in May forecast a sixth consecutive operating surplus of $3.2 billion for 2023/24. A surplus of $2.6 billion is forecast in 2024/25 with surpluses expected throughout the forward estimates. Total public sector net debt is projected to decrease to $28.6 billion by June 2024, and then increase gradually over the out years due to the high levels of infrastructure investment.

The State Budget had a similar focus to the Federal Budget - cost of living relief, boosting housing supply and economic diversification. Health and mental health, addressing skills shortages and METRONET also received increased funding.

On Budget night, WALGA provided detailed insights into the impact of the Budget on Local Governments which is available on the WALGA website.

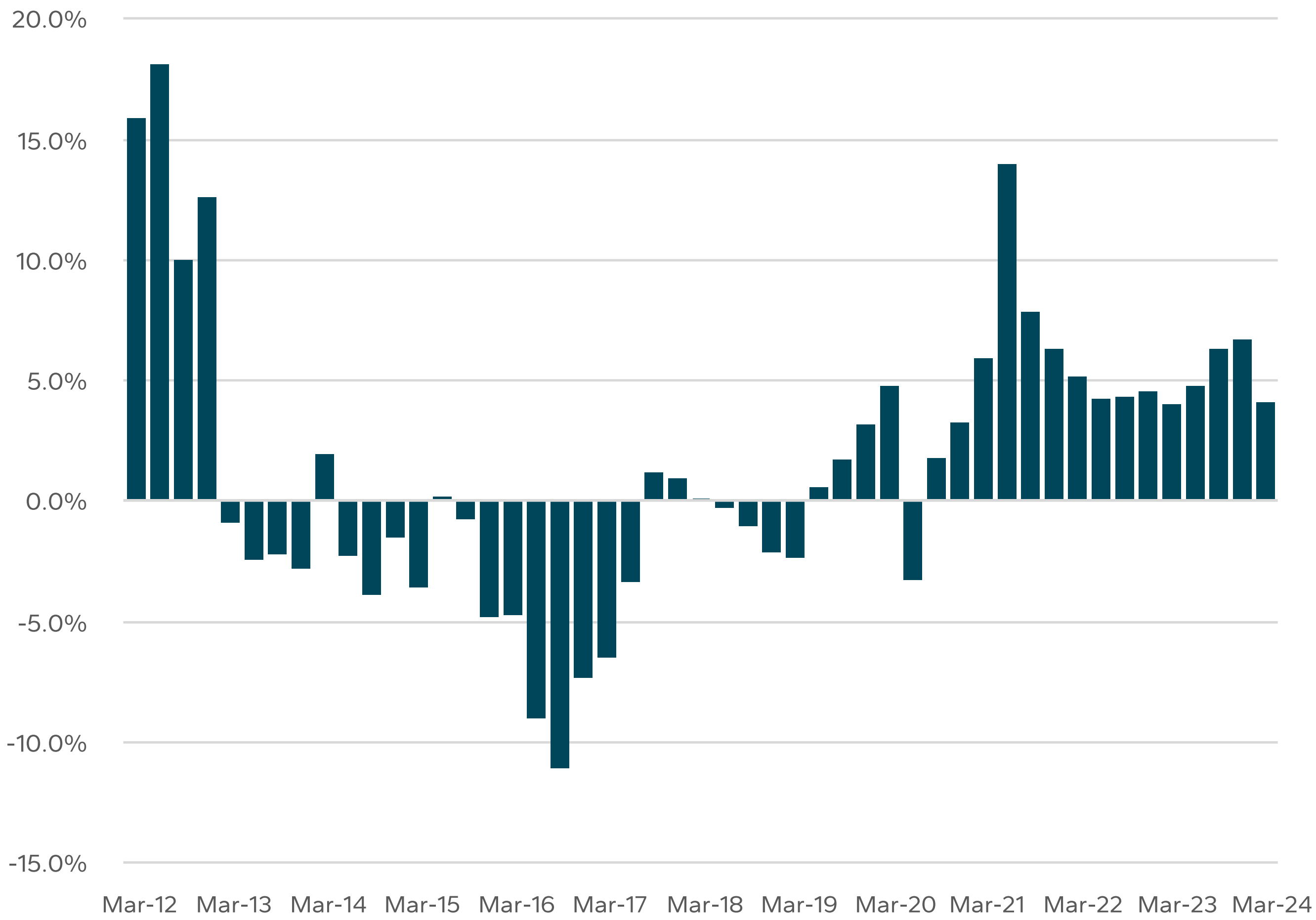
Western Australia's economy has been growing strongly, with the domestic economy, measured by State Final Demand, up 4.7% in 2023, more than double the national growth rate. This growth was underpinned by elevated levels of business investment, in particular investment in resource projects and machinery and equipment. Large resource projects that have ramped up include Scarborough/Pluto, Onslow Iron and Western Range. Public investment was also strong with the delivery of the Asset Investment Program.

State Final Demand is forecast to normalise in 2024/25, increasing 3.25%. Government investment will continue to be a major driver of growth as the rapid increase in business investment eases as producers approach capacity and expansion slows. Household consumption is forecast to grow modestly, supported by the growing population. Looking ahead, the WA economy is expected to stabilise at around 3.0% annual growth as household consumption returns, business investment steadies and the sharp growth in government investment levels off.

Deloitte Access Economics' Investment Monitor notes that although Engineering Work Done grew by 27% over the last 12 months, the value of Work Commenced in the mining industry fell by 15% over the same period. In the short term there is significant work underway, however further down the pipeline there is some uncertainty around the progress of major projects.

There are other key risks to the WA Economy. Almost 50% of total output from the State is delivered by the mining industry, which is also WA's second largest employer. Commodity prices, which drive business investment, are volatile and are a risk to major projects, as well as the State's coffers, if they experience significant falls. Despite the State and Federal Governments pulling policy and financial levers, housing continues to be a challenge with skills shortages impacting the construction pipeline. Increasing the supply of housing is critical to dampening the rapidly increasing rents and the cost of new dwellings that is driving inflation (see Inflation and Interest Rates section).

State Final Demand, WA, Annual % Change SOURCE: ABS; WALGA



WA Treasury Economic Forecasts

State Budget 2024/25	2022/23 % actual	2023/24 % estimated actual	2024/25 % forecast	2025/26 % forecast	2026/27 % forecast
Gross State Product	3.5	1.75	2.0	2.0	2.25
Household Consumption	3.5	2.0	2.25	2.75	3.0
Business Investment	4.5	13.25	1.75	3.75	4.25
Dwelling Investment	-2.7	6.75	7.5	2.5	3.25
Goods Exports	4.7	-0.5	1.5	1.25	1.25
Goods Imports	7.8	10.0	1.25	2.0	2.25
Employment Growth	3.1	3.75	1.75	1.5	1.5
Unemployment Rate	3.6	3.75	4.0	4.25	4.5
Wage Price Index	4.2	4.25	3.75	3.5	3.0
Population	3.2	2.8	1.8	1.7	1.7

Inflation and Interest Rates

Key points

- **Inflation is not falling as fast as forecast**
- **The RBA will do what is necessary to bring inflation back into the target range**
- **Rising rents and house prices are major drivers of inflation in WA**

The Reserve Bank of Australia (RBA) met on 18 June 2024 and decided to keep the cash rate target at 4.35%. For some time, the RBA has talked about the narrow path it is seeking to navigate to bring down inflation to the target band of 2-3% without the economy falling into recession. With national economic growth in the last quarter of just 0.1% and inflation remaining stubbornly high above the target band, this path continues to narrow.

The RBA is adopting a neutral stance on future movements in interest rates, not ruling anything in or out but reinforcing its position that it will do what is necessary to return inflation to target. The RBA's central forecast is for inflation to fall below 3% in the second half of 2025 and return to 2.5% by 2026.

Despite the slowing of the economy, household consumption is higher than the RBA had expected and the labour market remains strong. With tax cuts starting in July, the RBA is concerned that consumption may be stronger than is required to put downwards pressure on inflation. Global risks to the RBA's mandate include uncertainty about the strength of the Chinese and US economies, and the ongoing conflicts in Ukraine and the Middle East.

Australian headline inflation fell to 3.6% in March, down from 4.1% in the December quarter. However, on a quarterly basis, inflation rose 1.0% in March, up from 0.6% in December. Critically the Trimmed Mean, which strips out the more volatile components and is the RBA's preferred measure, remains at 4.0% in March, down just 0.1% from December. Inflation has fallen substantially since its 2022 peak, but the pace of the decline is slower than previously forecast. As a result, market expectations of a rate cut have moved from late 2024 into 2025.

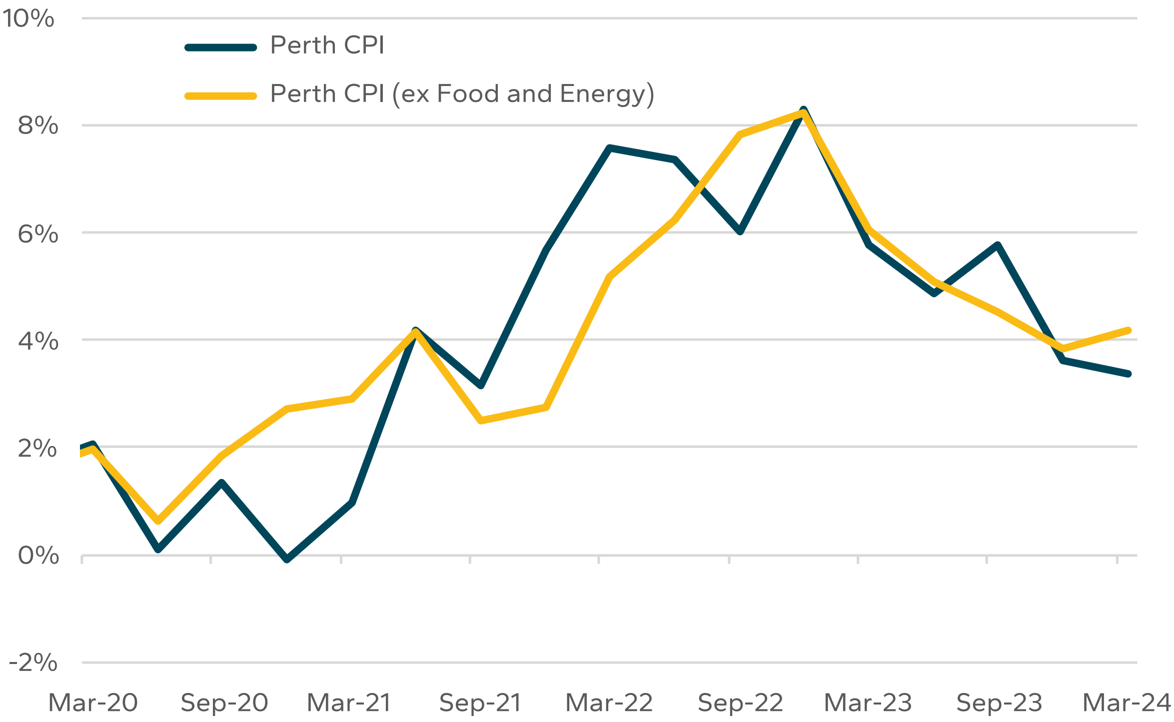
As flagged in previous Economic Briefings, the cost of services (+4.3% in the year to March) is higher than goods (+3.1% in the year to March). Goods peaked at 9.6% in annual terms in September 2022, whereas Services peaked lower and more recently at 6.3% in June 2023. Services are influenced more by the increases in wages, whereas Goods have benefited from the easing of supply chains with some items such as footwear and appliances cheaper than a year ago. The RBA is closely watching the Services sector for signs of slowing price increases.

The Perth Consumer Price Index (CPI) increased 0.6% in the March quarter and 3.4% in the last 12 months. This continues to be kept low by the impact of the State Government's Electricity Credit which saw the reported price of electricity fall 18% in March. The announcements in May's State and Federal Budgets of further electricity credits will see a continued impact on the Perth CPI through 2024/25. When looking at the Perth CPI excluding Food and Energy, it increased 4.2% over the last 12 months, up from 3.8% in the previous quarter. This supports the RBA's analysis that there is still a way to go until inflation returns to the target band.

Housing costs continue to drive the Perth CPI, with rents up 2.9% for the quarter (9.9% for the year) and new housing costs up 3.6% for the quarter (12.1% for the year). With low vacancy rates and dwelling construction not keeping pace with population growth, it is expected that housing will continue to be a major driver of inflation in WA in the near term (See Population and Housing section).

While much of the focus on the impact of interest rate rises has been on households, Local Governments have also been impacted by the rising interest rates when taking out new loans or using a short-term loan facility. Local Governments with cash investments should expect to see higher returns.

CPI vs CPI (ex Food and Energy), Perth, Annual % Change



SOURCE: ABS; WALGA

Labour Market and Wages

Key points

- **WA's labour market is the tightest in Australia, with an unemployment rate of 3.7%**
- **As a result, wages have been growing quickly although there are early indications that they may have peaked**
- **The slowing economy and the impact of rate rises is expected to increase unemployment in the near term**

The labour market in WA continues to be the tightest in the nation with an unemployment rate of just 3.7% in May. 28,000 new jobs have been created in the last year, 17,600 of them full time positions. The participation rate of 69.2% is close to record highs, suggesting that there is little spare capacity.

The number of unemployed persons has increased from its low in April 2022, but at 61,200 in May 2024, is well below the pre-pandemic level. The number of job vacancies has fallen from its peak, but are still at elevated levels, with 47,800 jobs advertised.

The impact of rate rises and the slowing economy are expected to drive up unemployment, but despite some large and high profile job cuts in WA, there is little evidence of this in the labour statistics to date. Looking forward, May's State Budget forecast the unemployment rate to rise to 4.0% in 2024/25 with employment growth easing from 3.75% to 1.75%.

This tight labour market means that organisations are competing for the same pool of employees, putting pressure on remuneration. The SEEK Advertised Salary Index shows advertised salaries in WA increasing by 4.4% in the year to April 2024. There is a suggestion that this is easing with growth in advertised salaries of just 0.8% for the quarter. There is also a variation in advertised salaries across industries with in-demand industries seeing higher growth rates such as Community Services (+8.1% over 12 months off the back of Aged Care wage increases), Education (+7.1%), Healthcare (+4.9%), and Mining (+4.9%), whilst weaker industries see salaries going backwards after inflation, including Information Technology (+0.8%) and Financial Services (+0.7%).

The increase in advertised salaries has been reflected in wages data, with the WA Wage Price Index (WPI) increasing 4.2% in the year to March 2024. The fall from 4.7% rise in December is the first time that wages growth has slowed in three years and the first evidence that wages growth has peaked.

Private sector wages increased by 0.6% in the March quarter and 4.3% for the year, falling from 4.6% in December. Public sector wages increased just 0.3% in the March quarter and 3.4% for the year, a large drop from the 5.2% recorded in the December quarter. The reason for this drop was that the massive 2.1% quarterly growth in public sector wages in March 2023, caused by the unfreezing of the State Government's wage cap, was no longer counted in the 12 monthly figure.

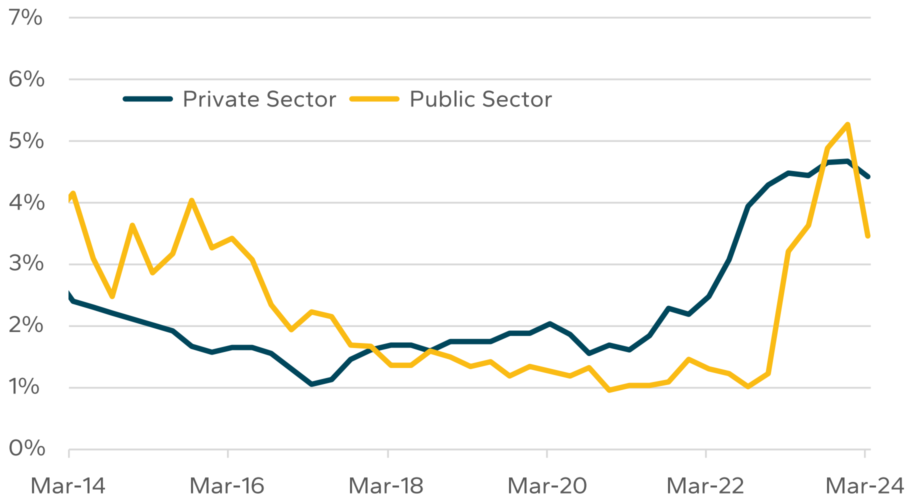
The WA Industrial Relations Commission announced that the minimum wage will increase 6.3% from 1 July in their State Wage Case. Around 27,000 employers and 300,000 employees are impacted by this decision. At a national level, the Fair Work Commission increased the National Minimum Wage by 3.75%. The impact of these increases will be seen in the September quarter.

In the May State Budget, Treasury forecast wages growth to continue its robust performance in 2024/25, increasing by 3.75%. This is sufficiently above the forecast CPI of 3.0% to deliver real wages growth after a period of declining purchasing power. Wages growth is forecast to continue to ease in the out years to be 3.5% in 2025/26 and then 3.0% in the following two years.

Employee costs make up a third of Local Government costs on average across the State. As a result, the Economic Briefing will continue to report on trends in the labour market and its impact on wages.

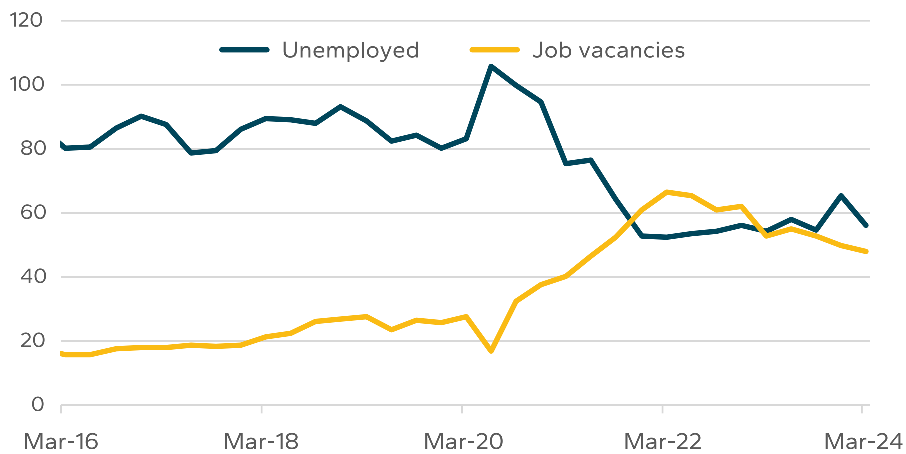
Wage Price Index
Private vs Public, WA,
Annual % Change

SOURCE: ABS; WALGA



Job Vacancies vs
Unemployed Persons,
WA, ’000s

SOURCE: ABS; WALGA



Population and Housing

Key points

- **WA's population increased 3.3% in 2023, the fastest in the nation**
- **New arrivals have filled skills shortages in the labour market**
- **Housing supply has not kept pace, with rents and house prices skyrocketing**

Australia's population is growing at the fastest rate since records began in 1981, up 2.5% in 2023. More than half a million of this 651,200 person increase is attributable to Net Overseas Migration. Overseas Arrivals peaked at a record of 214,300 in the March 2023 quarter, however there are early signs that Arrivals are returning to pre-pandemic levels with the number of Arrivals in December 2023 slightly less than the December quarter in 2019.

It is the low level of Overseas Departures that is now driving Net Overseas Migration, with just 54,300 departing in the December quarter, well below the pre-pandemic level of 114,400 in December 2019. The level of Overseas Departures in 2023 was the lowest since 1999. Throughout 2020 and 2021 the number of international students starting their studies fell during the pandemic. As a result, a lower number of international students have completed their studies and returned home. As the number of international student completions normalises, Overseas Departures will return to its long-term average. This, along with the Federal Government's efforts to reduce Overseas Arrivals, means that Net Overseas Migration is forecast in the Federal Budget to fall to an increase of 260,000 in 2024/25 and 255,000 in 2025/26.

Western Australia's population growth continues to be the highest in the nation, up 3.3% in 2023. Like Australia, WA's current population is driven by Net Overseas Migration, which contributed 73% of the 93,800 new residents in 2023. WA is also one of two states in Australia (along with Queensland) that is currently experiencing positive Net Interstate Migration, which increased 10,709 in 2023. Both Overseas Migration and Interstate Migration are impacted by WA's boom-bust economic cycle, increasing when jobs are plentiful and falling when they are not.

To date, WA's labour market has absorbed this increase in the working population with unemployment rates remaining steady (see Labour Market and Wages section). Whilst this has been a positive in addressing the skills shortages across the State, it has increased pressure on infrastructure and services, most notably housing.

Real Estate Institute of Western Australia reports vacancy rates across WA at levels well below the 2.5 to 3.5 per cent that is considered a balanced market, with Perth vacancies at 0.5%; Albany 0.7%; Geraldton 1.2%; and Kalgoorlie 1.3%. Bunbury is reported to have a rental vacancy rate of 3.7%.

CoreLogic reports Australian median dwelling values increased by 8.3% in the year to May 2024. WA dwelling values have far exceeded this with Perth up 22.0% and Regional WA up 14.8%. Despite this rapid increase, Perth continues to be relatively affordable to those living interstate, with a median dwelling value of $736,649 the lowest of the five major capitals.

It is a similar story for renters, with house rents in Perth up 13.5% in the year to May according to CoreLogic, the highest growth of the capital cities. Regional WA is experiencing the fastest growing rents of all regional areas in Australia at 11.9%.

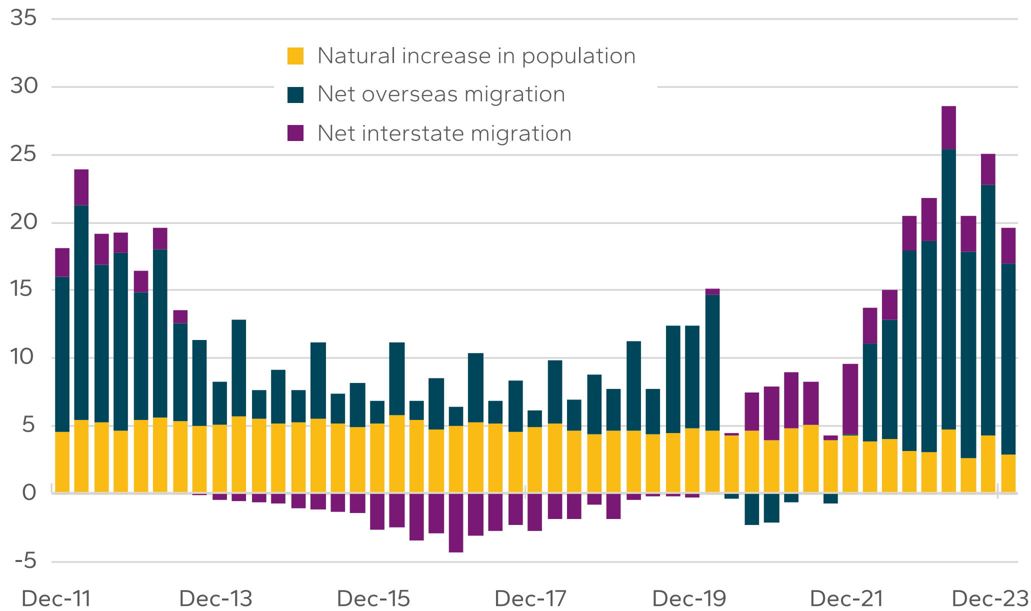
As a result of rising rents, the share of income required to service median rents has risen to 32.2% in Australia. For the lowest 25% of earners this increases to a challenging 54.3% of income going to rent. The rental crisis is disproportionately impacting those who can least afford it. Both Federal and State Governments have identified increased housing supply as a key focus of their budgets.

Additionally, the Australian Government is providing $1.9 billion over five years to those accessing Commonwealth Rent Assistance.

Looking forward, the WA Treasury projects population growth to ease as the economy cools, with an increase of 1.8% forecast for 2024/25 and 1.7% for the Budget outyears. This is down from 2.8% in 2023/24 and 3.2% in 2022/23. If this slowdown in population growth comes to pass and the Federal and State Governments' policies to increase housing supply are successful, the pressure on housing is likely to ease. In the short term however, it is expected that the pressure on housing stock will continue to challenge local communities.

Components of Population Change, WA, 000s

SOURCE: ABS; WALGA



Change in Regional City House Values and Rents

SOURCE: CoreLogic

	Values		Rents	
Regional Cities	Annual	5 year	Annual	5 year
Albany	12%	52%	14%	36%
Bunbury	21%	68%	16%	65%
Busselton	16%	68%	15%	60%
Geraldton	13%	61%	13%	55%
Kalgoorlie-Boulder	8%	32%	6%	55%

Local Government Cost Index

Key points

- **The Local Government Cost Index (LGCI) increased 0.7% in the March quarter and 3.3% in the last year**
- **Looking forward, LGCI growth is forecast to ease to 3.1% in 2024/25**
- **The LGCI continues to be driven by wages growth as construction costs ease**

The Local Government Cost Index (LGCI) increased by 0.7% in the March quarter, down slightly from 0.8% December quarter. In annual terms the LGCI increased by 3.3%, down from 3.5% in the December quarter.

Over the last 12 months, growth in the LGCI was driven by quickly increasing wages in WA, which make up around one-third of the LGCI. Public sector wages rose quickly with the end of the State Government's wages freeze in 2023, peaking at 5.2% growth in the year to December 2023. This has now eased to 3.4% in the March quarter after quarterly growth of just 0.3%. Private sector growth has been more sustained, increasing 0.6% in the March quarter to record annual growth of 4.3%, the sixth consecutive quarter where annualised wages growth has surpassed 4%. There are early signs that wages growth has peaked with the WA Wage Price Index falling from 4.7% in the December quarter to 4.2% in the March quarter (see Labour Market and Wages section for more).

As highlighted in previous Economic Briefings, construction costs continue to grow at a slower pace after the rapid increases of over 20% for each category in the last three years. Road and bridge construction costs increased 1.3% in the year to March and are forecast to increase a further 2.0% in 2024/25 and 2025/26. Non-residential building costs increased 3.3% in the year to March and are expected to grow at around 2% in the coming years. Non-road infrastructure costs increased 2.2% in the year to March and is forecast to grow 2.2% in 2024/25 and 2.0% in 2025/26.

This construction cost data is an average across WA. Local Governments report receiving quotes that far exceed these averages which may be influenced by regional supply chain issues, the crowding out by major infrastructure projects increasing demand for materials and labour, or increased risk premiums due to the recent shocks to the construction industry.

In the March quarter, WA broke its run of 14 consecutive quarters of growth in the domestic economy as measured by State Final demand. The slowdown in the economy is expected to ease the recent increases in the cost of Machinery and Equipment and Materials and Contracts. There is a risk to the forecast in both categories if business investment takes off, particularly in the mining sector, or if State and Federal Governments considerably increase spending ahead of their respective elections.

As highlighted in the previous Economic Briefing, insurance and risk management costs remain high, although it is expected that cost increases will moderate in the coming years as inflation and capacity constraints ease.

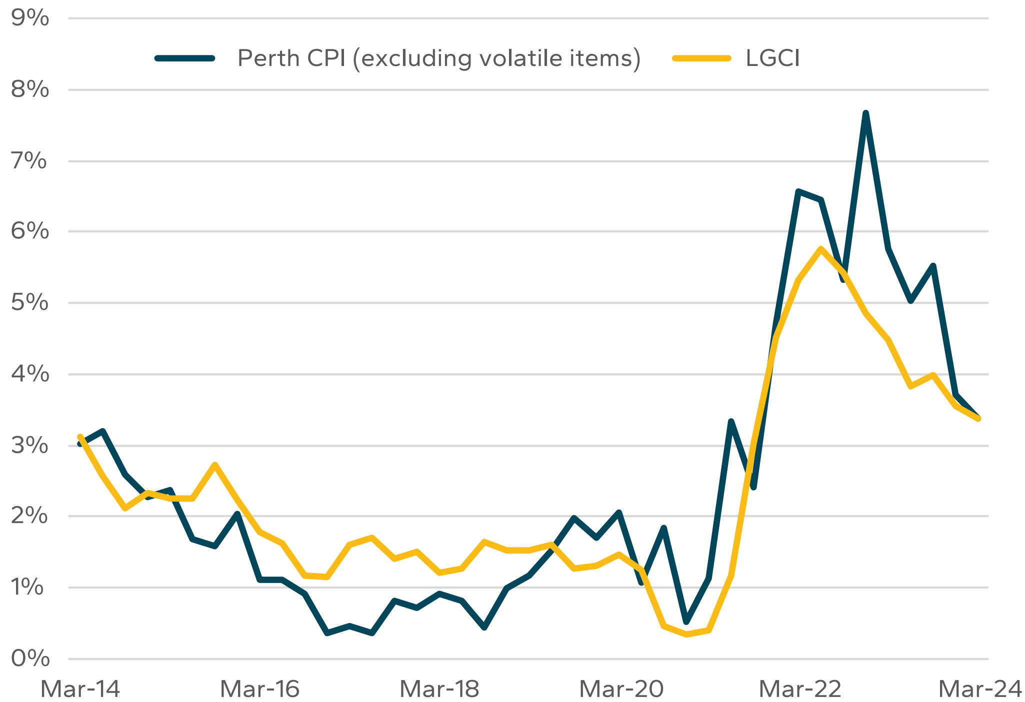
Local Governments are encouraged to prepare for multiple scenarios through their budgeting process and be ready to respond to changing economic conditions by building in flexibility to their projects and procurement processes. The LGCI uses statewide data and regional variances will impact each Local Government. Liaising with suppliers to understand the local economic conditions and constraints will enable Local Governments to effectively plan the timing of their projects.

LGCI Table

Component	Weighting	2022/23 (actual)	2023/24 (forecast)	2024/25 (forecast)	2025/26 (forecast)	2026/27 (forecast)
Employee costs	35%	4.2	4.3	3.8	3.5	3.0
Materials and contracts	28%	4.3	4.3	3.3	3.0	3.0
Furniture	1%	5.8	3.5	2.5	2.2	2.0
Non-residential building	5%	1.0	4.2	2.0	1.9	2.2
Machinery and Equipment	5%	11.5	4.0	2.4	1.9	1.7
Non-road infrastructure	9%	3.3	2.9	2.2	2.0	2.4
Road and bridge construction	10%	3.8	2.1	2.0	2.0	2.6
Utilities	3%	2.5	3.0	3.0	3.0	3.0
Insurance	1%	12.4	11.6	8.5	5.0	3.0
Other	3%	6.2	4.0	3.0	2.5	2.5
LGCI	**100%**	**4.4**	**3.9**	**3.1**	**2.8**	**2.8**

LGCI vs CPI (excluding volatile items), Annual % Change

SOURCE: ABS; WALGA



Questions

If you have any questions on the contents of this report, please direct them to the WALGA Economics Team.

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