

WALGA Economic Briefing

October 2021



Overview



- The **WA economy continues its recovery from the COVID-19 pandemic**, with the domestic economy growing for the fourth consecutive quarter in June 2021, albeit at a slower pace than in the previous quarter. In the last year, the domestic economy grew 12.4% compared to the COVID induced low last June.
- The **private sector continues to strengthen** as business investment grows with private capital expenditure increasing 11.9% in the year to June 2021.
- In the last year, **the housing market has experienced strong growth** with dwelling values increasing 18.1% in Perth and 19.9% in Regional WA, broadly in-line with national trends. However, growth has slowed in recent months as Government stimulus is withdrawn and affordability decreases. Record low interest rates and low levels of supply will ensure price pressures remain in the near-term.
- With the lowest underutilisation rate (unemployment + underemployment) and highest participation rate of all States, the **WA labour market is tightening**. Combined with reduced labour mobility due to closed borders, it is expected that challenges will continue for businesses seeking to hire workers with specialised skills. Total hours worked in WA is now at an all-time high having more than recovered the hours lost at the conclusion of Jobkeeper.
- The WA Treasury forecasts an **increase in Gross State Product of 3.5% in 2021-22**, following on from an estimated 3.25% in 2020-21. Growth is expected to slow in the following years as Government stimulus is unwound.
- In the short-term, the **major risk to peoples' jobs and the broader WA economy remains an outbreak of the Delta strain of COVID-19**. In August, NSW lost more than 170,000 jobs and business confidence dropped to the lowest levels this year. It is expected that due to the lockdown in NSW, Victoria and ACT Australia's GDP will fall in the September quarter.

Overview

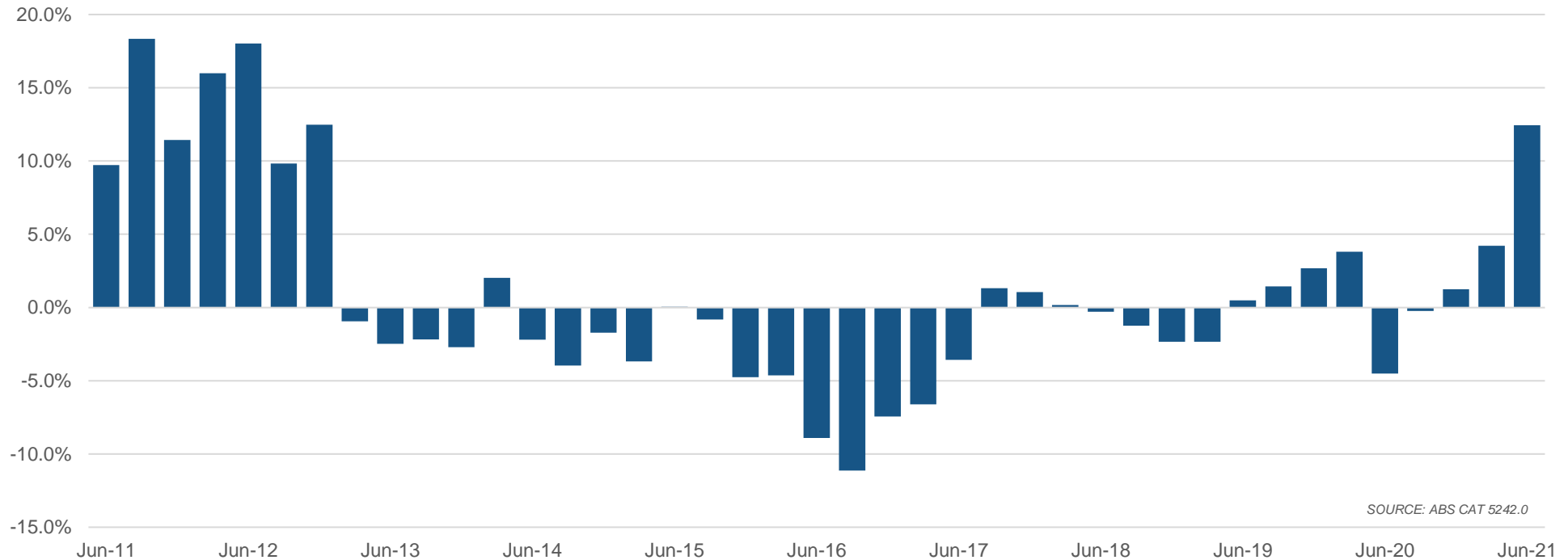


- The strength of the WA economy and constraints on labour and materials will see **costs increase in the near term.**
- Increases to the Local Government Cost Index (LGCI) in 2020-21 were below expectations as COVID-19 impacted the economy in unforeseen ways. **In 2021-22 the LGCI is predicted to rise** as the increase in economic activity, capacity constraints and labour mobility challenges impact prices.
- WALGA's latest base case forecasts indicate that the **LGCI is expected to grow by 3.5% in 2021-22, and 2.6% in 2022-23**, driven by higher construction costs for roads and bridges, non-road infrastructure and non-residential buildings and elevated costs for materials and contracts in the short-term.
- It should be noted that there are significant challenges with forecasting in the current economic environment, and so **the LGCI should be used with caution.**
- Based on recent responses to tenders and requests for quotation, Local Governments indicate that they are facing **significantly higher costs**, particularly in relation to construction. As higher costs are reflected in official data, this will see the index revised upwards.
- **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 coming years.

Household consumption and public infrastructure spending drives domestic growth



State Final Demand, WA, Annual % Change

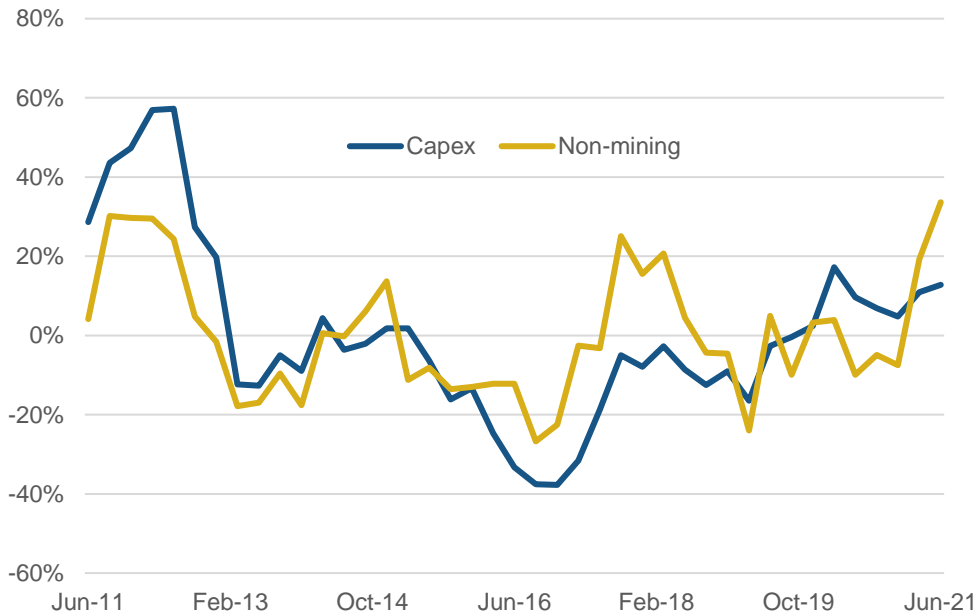


- The Western Australian domestic economy (State Final Demand) grew 1.2% in the June quarter, below the national final demand growth rate of 1.7%. In annual terms, State Final Demand is up 12.4% from the COVID-19 induced drop in June 2020 and is at a level not seen since 2016.
- Household consumption had the second-highest growth rate in the country at 1.9% for the quarter. This was offset by a 0.9% drop in Government expenditure as the electricity credit scheme concluded.

Private sector activity continues to increase, contributing to jobs growth



Private New Capital Expenditure, WA, Annual % Change



SOURCE: ABS CAT 5625.15

Retail turnover, WA, Annual % Change



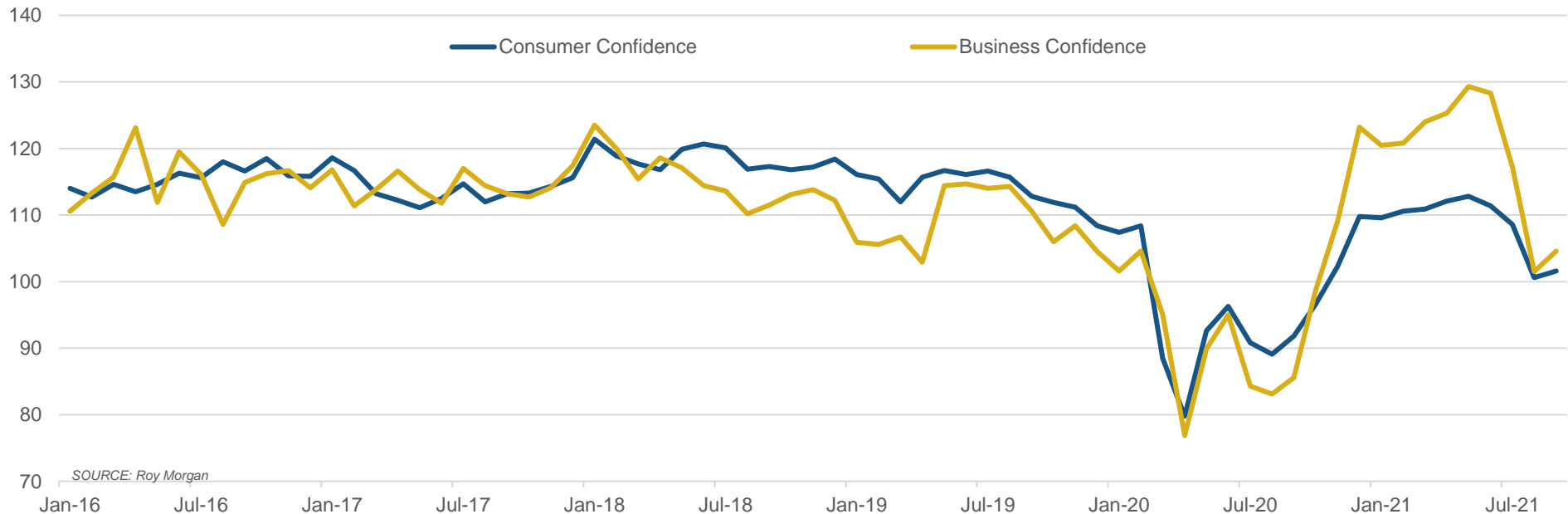
SOURCE: ABS CAT 8501.0

- Private sector spending remains critical to economic growth in WA.
- Total capital expenditure in WA increased by 11.9% in the year to June 2021.
- Mining expenditure is above the pre-pandemic levels of 2018 and 2019 and continues to grow steadily whilst non-mining expenditure in the June quarter is at levels not seen since the tail-end of the mining boom. Whilst the trend is promising, the numbers are volatile in the short-term as expenditure deferred by the pandemic washes through the economy.
- WA Retail turnover was positive for the fourth consecutive month in August increasing 2.8% in contrast to the nation where retail turnover declined by 1.7%, led by large falls in states experiencing lockdown.

WA consumer and businesses remain upbeat, despite East Coast Delta outbreak



Consumer and Business Confidence, Australian Monthly Index



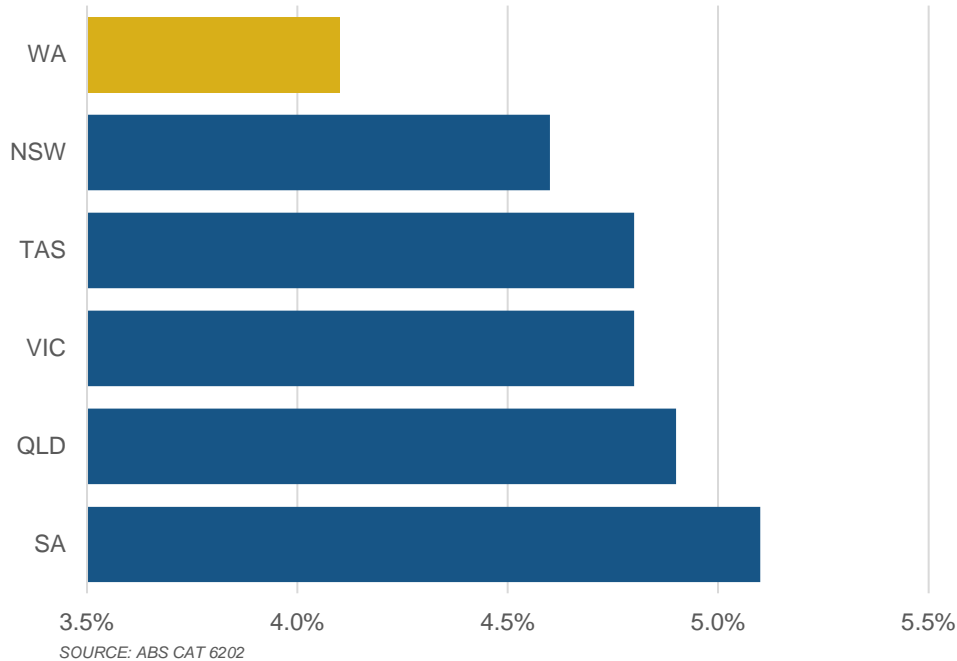
SOURCE: Roy Morgan

- The strength in private sector activity in WA reflects high levels of consumer and business confidence.
- In June 2021, CCIWA's local business confidence survey hit record highs, although businesses warned of struggles to fill skilled roles. Similarly CCIWA found consumer confidence at record highs, driven by the successful containment of COVID-19 in WA.
- Western Australian consumers and businesses are more upbeat than the rest of the country. After record low numbers at the height of the pandemic, business confidence in Australia soared to record highs in early 2021. East coast lockdowns reversed this trend in recent months, although there was a slight bounce back in September.
- Consumer confidence followed the same path downwards and has since bounced back to pre-pandemic levels. It has also been impacted by the lockdowns in NSW and Victoria.

Strength of the economy has seen participation rates increase



Unemployment Rate, September 2021



Monthly Hours Worked, WA, Millions

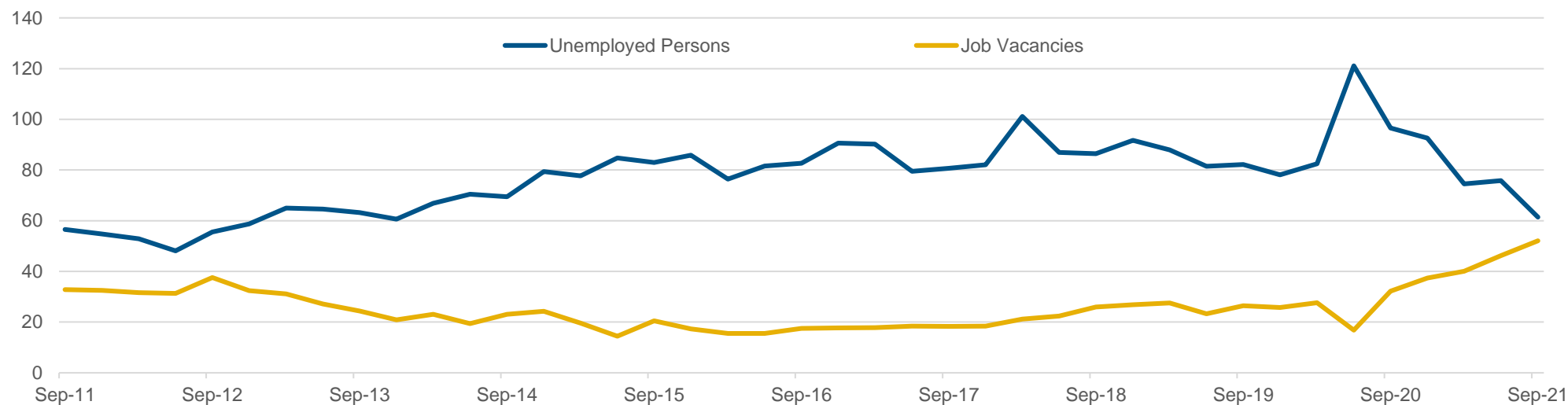


- The strength of the labour market saw WA's participation rate at 68.8% in September 2021, well above the national average of 64.5%
- In the September quarter, 7,000 people entered the labour market in WA whilst 21,400 found a job, driving down the unemployment rate. This contrasts with a loss of 281,200 jobs for the quarter across Australia, centred around large job losses in the Delta hit states of New South Wales and Victoria.
- The WA unemployment rate of 4.1% is below the national unemployment rate (4.6%), as is the underemployment rate (employed people who would like to work additional hours) which at 7.2% is significantly below the national rate of 9.2%.
- Total hours worked in WA continued to grow, increasing to above pre-pandemic levels.



The labour market tightens as job vacancies rise and unemployment falls

Job Vacancies vs Unemployed Persons, WA Public and Private, '000s



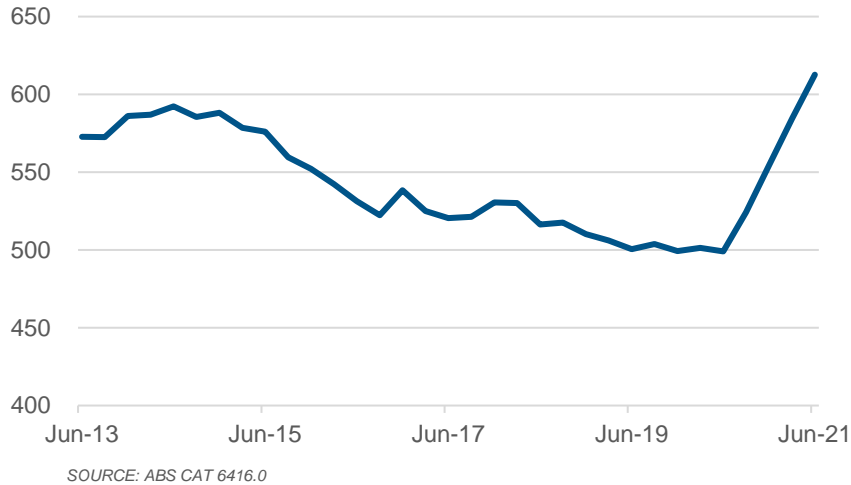
SOURCE: ABS CAT 6354.0; 6202.0

- WA job vacancies increased by 12.7% in the September quarter to 52,100. Nationally, quarterly job vacancies decreased by 9.8%, influenced by the COVID-19 related lockdowns in NSW (down 15.6%) and Victoria (down 7.1%). This is the first drop in Australia's job vacancy data since May 2020.
- The number of unemployed Western Australians in September was 61,400. The gap between job vacancies and unemployed persons is at historically low levels, demonstrating the challenge of matching skills with jobs. With limited labour mobility across State borders, and close to none internationally, this tightness will be a drag on the State's economy.
- The WA private sector saw its fifth consecutive quarter of job vacancy growth (up 12.1%) reflecting the confidence of the private sector in the state economy. Private sector job vacancy data is a strong indicator of business confidence. Nationally, private sector job vacancies decreased 10.9% in the September quarter with drops in Australia's two largest economies of 17% (NSW) and 8.5% (Victoria) as business hiring intentions abate.
- WA public sector job vacancies increased 20.3% after a drop in the May quarter. WA public sector job vacancies remain below the equivalent quarter in 2019 by 1.5%. Public sector hiring is less impacted by the Delta outbreak reflected in the 2.3% national growth of public sector vacancies.

Housing market growth slows but pressures increase on renters



Mean Dwelling Price, WA, Thousands



Residential Housing Commencements, WA, Annual % Change

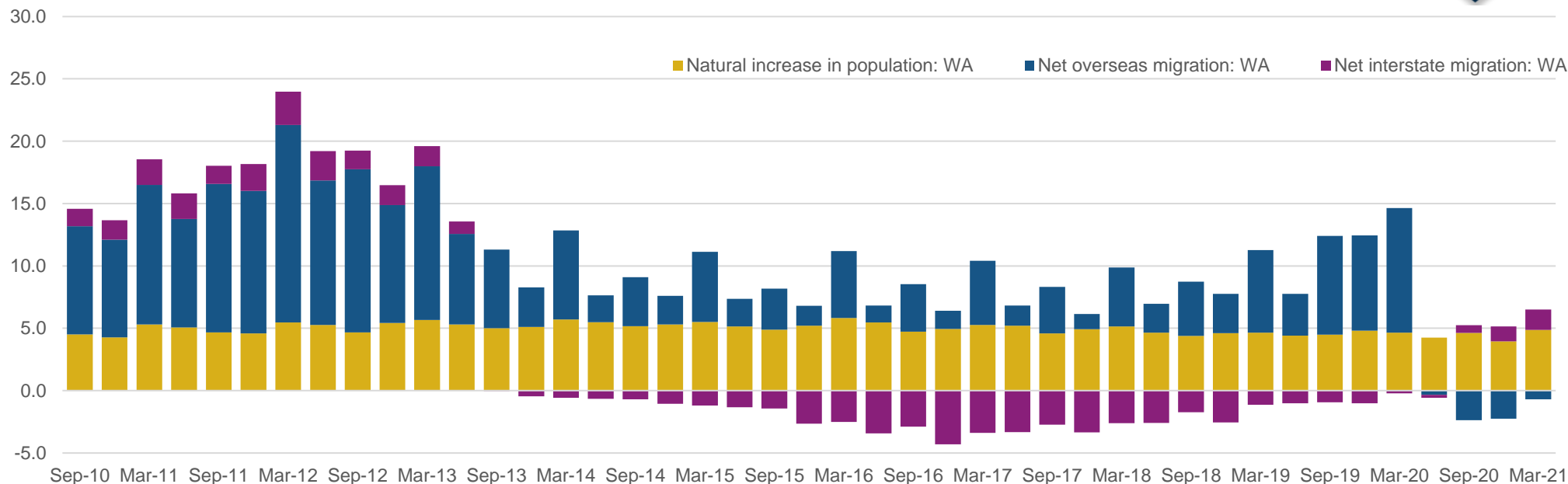


- House prices in Perth and Regional WA continue to rise albeit at a slower rate as Government stimulus is withdrawn and affordability decreases for those seeking to enter the housing market. The ongoing attractiveness of low interest rates and a comparatively low level of listings is maintaining upwards pressure on prices. These conditions have also led to a residential building spike.
- Perth house prices increased 1.2% for the September quarter, below the national average of 4.8%. On an annual basis, Perth house prices have risen 18.1%, broadly in-line with the combined capitals (19.5%).
- It is a similar story for regional WA with house prices up 1.8% for the quarter and 19.9% for the year compared with the combined regionals across Australia of 5.1% for the quarter and 23.1% for the year.
- In the year to June 2021 Perth rents increased 16.7%, well above the combined capital average of 5%. Perth residential vacancies remain historically low at 1% suggesting ongoing price pressures that may drag on household consumption in the medium-term.
- These pressures are reflected regionally as well with Bunbury, Busselton and Albany returning vacancy rates of 1% or below, and rates of between 1% and 2% in Broome, Kalgoorlie and Geraldton.
- The extent to which pressures remain in the housing market in coming years will depend on the impact of population growth as borders reopen.

COVID-19 subdues population growth despite positive net interstate migration



Population Change, WA, '000s



SOURCE: ABS CAT 3101.0

- Interstate net migration (the number of people moving to WA from other states less those moving from WA to other states) has been positive for three consecutive quarters after seven years of more people moving interstate than coming to WA. For WA, net interstate migration closely follows the economic cycle as people move to WA when jobs are plentiful and leave when there is a downturn.
- In the quarter to March 6,216 people moved to Regional WA, the majority (73%) from Greater Perth. 6,131 moved from Regional WA for a quarterly increase of 85 people. Despite its modest population, the next most common previous location for new arrivals was Regional QLD, also a strong mining region.
- In the same quarter Greater Perth's net increase from interstate migration was 1,554. 42% of arrivals were from Regional WA, 14% were from Greater Melbourne and 12% from Greater Sydney.

Treasury predicts the WA economy to continue to grow in future years



	2020-21	2021-22	2022-23	2023-24	2024-25
	%	%	%	%	%
Gross State Product	3.25	3.5	1.0	1.25	1.5
Household Consumption	2.5	2.5	2.25	2.75	2.5
Business Investment	8.0	9.75	3.25	1.0	0.5
Dwelling Investment	4.75	27.25	-21.75	-3.5	6.0
Exports	0.5	2.25	1.5	0.5	0.25
Imports	5.25	4.75	2.0	1.5	1.25
Unemployment Rate	6.1	4.75	4.5	4.5	4.5
Population	0.8	0.7	0.8	1.1	1.3

SOURCE: WA Government Budget Papers

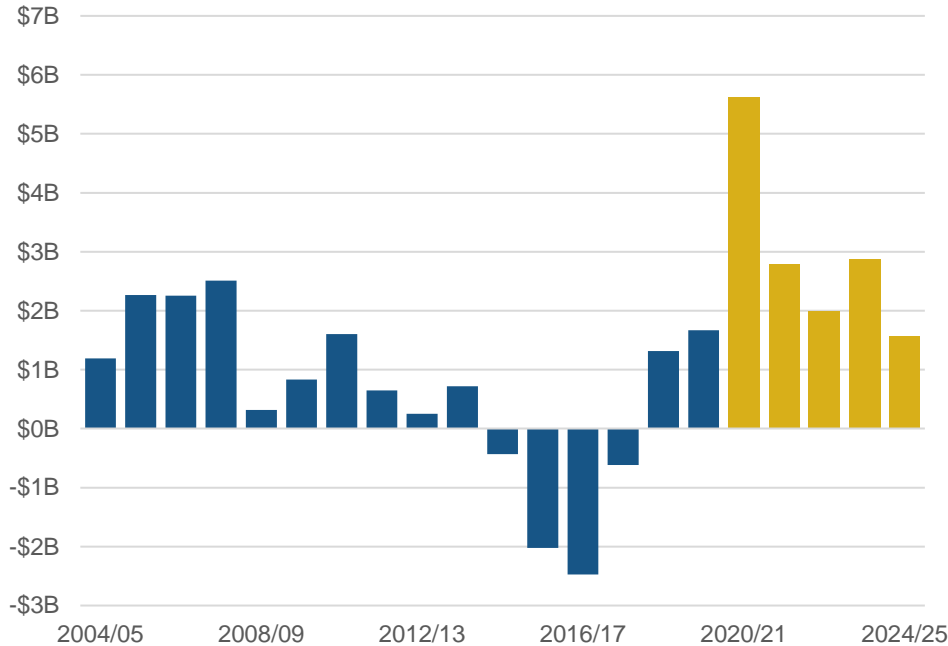
- Treasury estimates in the State Budget were for another strong year of economic growth for WA. Gross State Product (GSP) was estimated to be 3.25% in 2020-21, growing to 3.5% in 2021-22.
- This compares favourably with Australia's economy which grew 1.4% in 2020-21. It is expected that lockdowns in NSW and Victoria will lead to a national contraction in September quarter as WA continues to grow.
- In following years it is expected that GSP will drop as stimulus expenditure is unwound, major iron ore projects are finalised and Western Australians redirect their discretionary spending to international travel

Iron ore windfall drives state budget surplus as economic growth remains high



Net Operating Balance, \$Billion

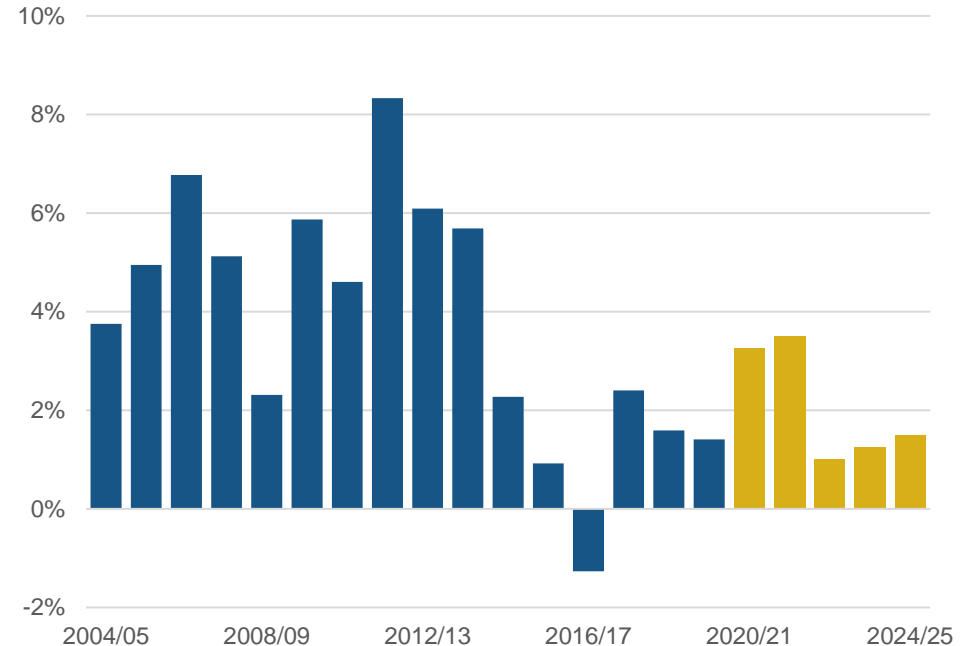
Forecast



SOURCE: WA Government Budget Papers

WA Gross State Product, Annual % Change

Forecast

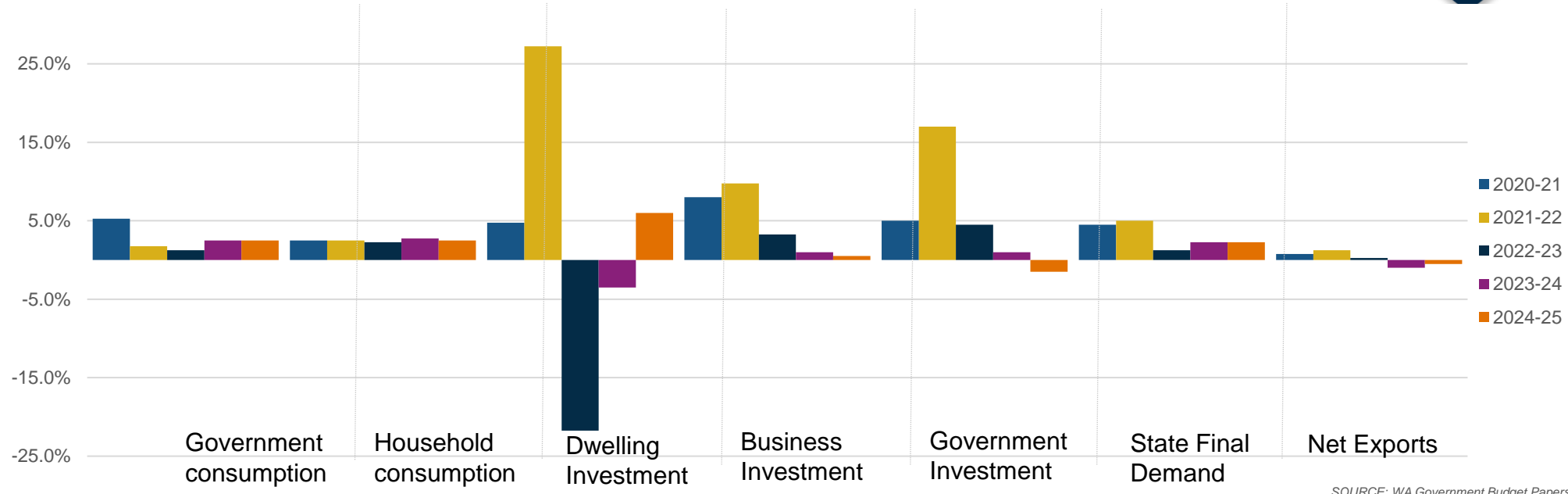


SOURCE: WA Government Budget Papers

- WA's stronger than expected economy saw a record \$5.6 billion operating surplus in 2020-21, driven by higher than expected iron ore royalties; stronger than expected tax receipts; and an increase in GST receipts.
- The State's financial position is expected to remain strong, with a \$2.8 billion surplus expected in 2021-22 and further surpluses across the forward estimates.
- WALGA is advocating for the State Government to use its strong financial position to fund priority programs as outlined in the "[Immediate Priorities for the State Government](#)" budget submission.

Government, business and housing investment will continue to drive activity in the near term

WA Government Forecasts, Annual % Change



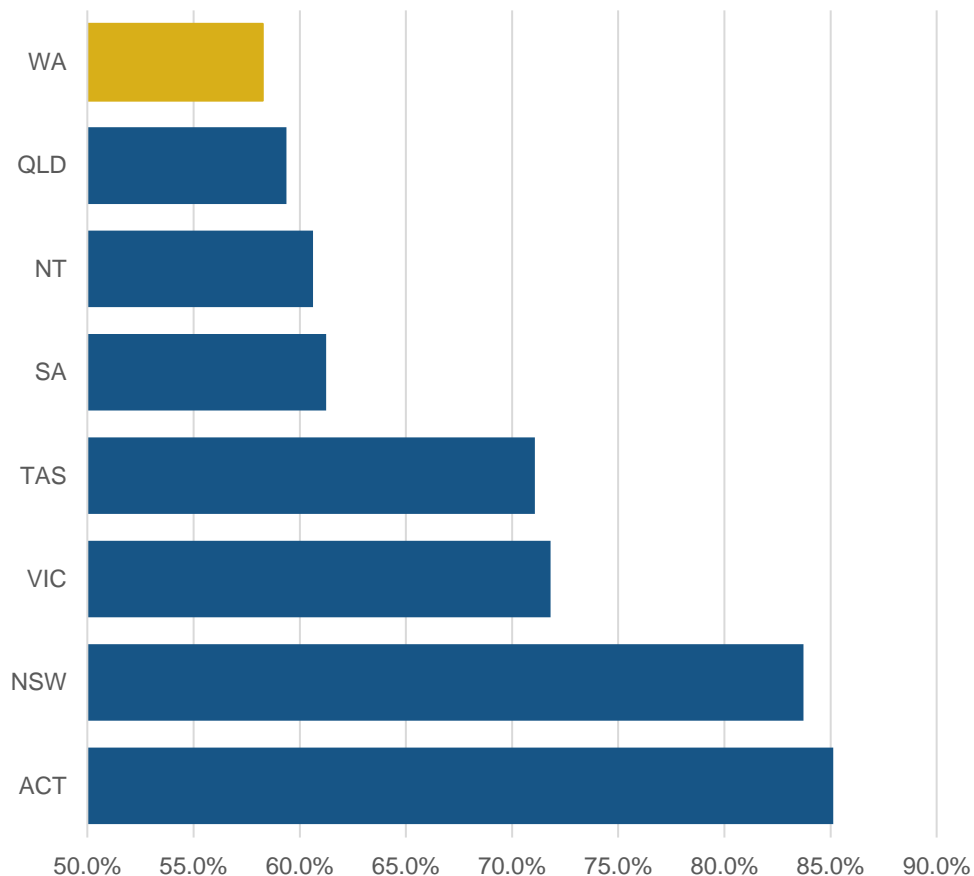
SOURCE: WA Government Budget Papers

- After high levels of State and Commonwealth stimulus in 2020-21, **Government consumption** will return to a steady growth rate.
- **Household spending** returned to growth after declining in 2019-20 as a result of COVID-19. People are spending on domestic goods and services as a result of travel restrictions.
- **Dwelling investment** is expected to spike in 2021-22 as the impact of State and Federal stimulus flows through the economy, returning to normal levels in the following years.
- Large mining projects will continue to drive high levels of **business investment** in 2021-22
- **Government investment** is expected to peak in 2021-22 due to large spending on non-residential construction projects such as road, rail and utility projects as part of COVID-19 stimulus programs.

An outbreak of COVID-19 is the greatest threat to the WA economy



Vaccination rate, % double-dosed aged 16+



SOURCE: Commonwealth of Australia, Department of Health

- An outbreak of COVID-19 remains the greatest threat to the WA economy in the short-term.
- In the State Budget, WA Treasury noted the flow-on effects that an outbreak may have on supply chains and confidence levels which would have negative impacts across the breadth of the economy.
- The greatest protection against COVID-19 is vaccination. At October 22, WA is the least vaccinated state in the country with 58.3% of residents aged 16+ fully vaccinated compared with the national average of 71.7%.
- WA is on track to reach 80% double-vaccination by December 9, a month after the nation (November 8) and almost two months after NSW and ACT. It is expected that the recent announcement of mandatory vaccines in WA will accelerate this timetable.
- The Federal Government has announced that the international border will reopen progressively from November 1.
- As international and interstate borders are eased across the country, pressure will increase on the WA Government to ease their border restrictions.

Regional and remote WA is lagging the nation for vaccinations



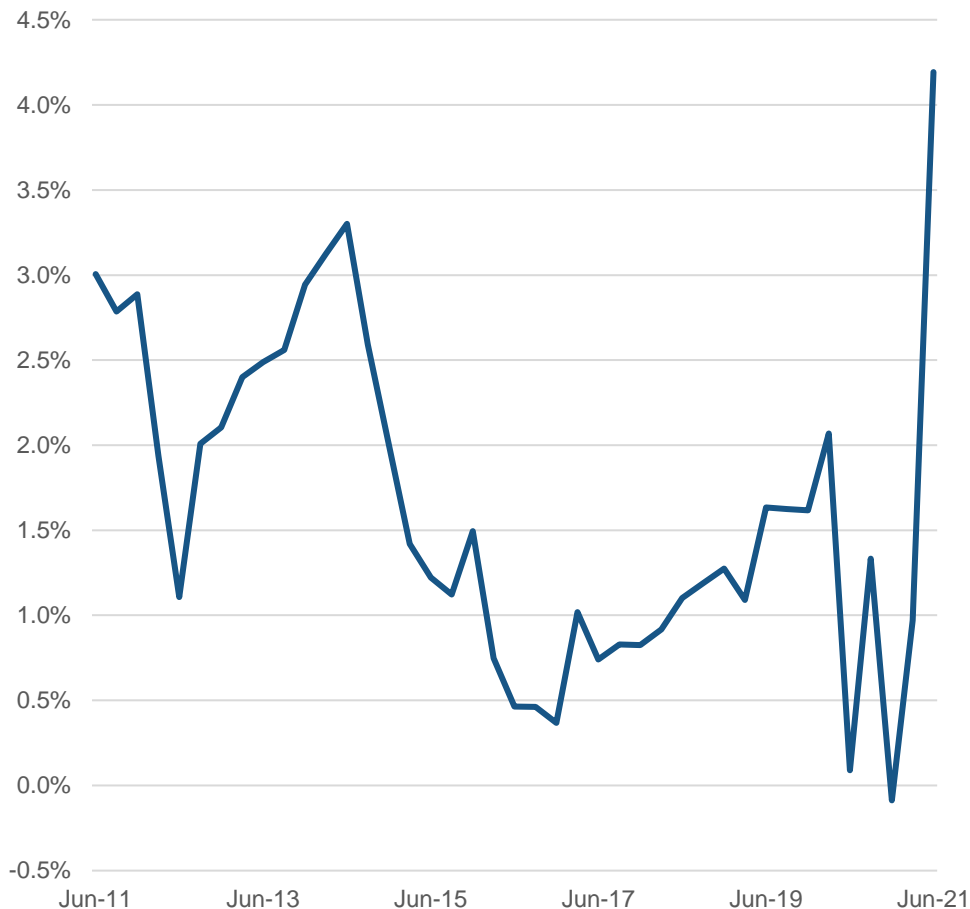
Region	Fully Vaccinated (at October 17)	Weekly increase (to October 17)
Outback (North)	29.2%	2.6%
Outback (South)	45.7%	3.9%
Perth – North East	52.8%	4.4%
Wheatbelt	54.3%	4.0%
Mandurah	55.2%	4.1%
Perth – South East	55.3%	4.4%
Bunbury (South West)	56.3%	3.7%
Perth – South West	58.2%	4.0%
Perth – North West	59.0%	4.0%
Perth – Inner	71.6%	4.0%

- Vaccination rates are not consistent across regions.
- The Outback North region (Kimberley and Pilbara zones) is the least vaccinated region in the country at 29.2%. It is also being vaccinated at the slowest rate in WA.
- The Outback South region at 45.7% (approximately the Gascoyne, Murchison, Goldfields Esperance and Northern Country zones) is also below the State average in both total vaccinations and vaccination growth rates.
- This highlights the importance of improving accessibility of vaccines to regional and remote WA and the susceptibility of these regions as the status of Australia’s external and internal borders normalise and the likelihood of COVID-19 returning to WA increases. This is equally critical to the economy as Regional WA contributes 39% of Gross State Product (DPIRD: 2019) with a high level of labour mobility due to the prevalence of FIFO workers.

Inflation rates have increased after low levels during the COVID-19 recession



Perth Consumer Price Index, Annual % change



SOURCE: ABS CAT 6401.0

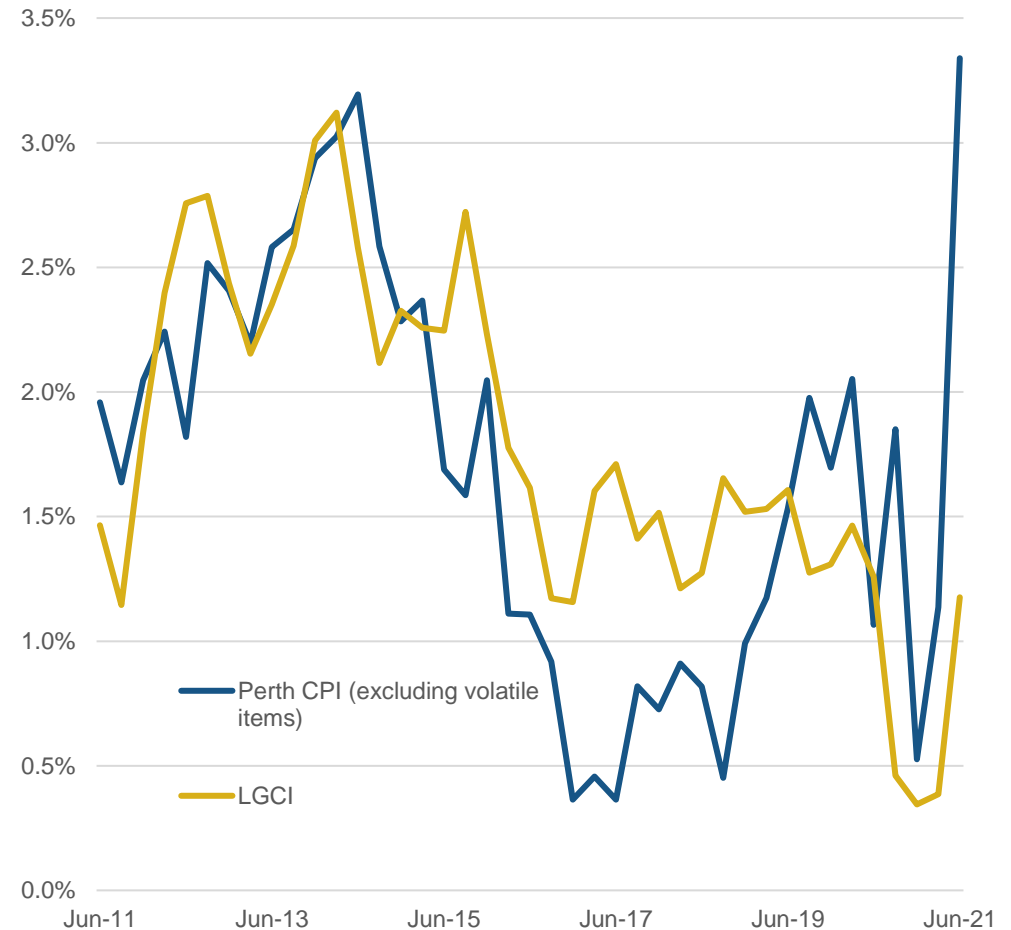
- In the June quarter, Perth CPI rose 1.9%, the highest of all capital cities. The increase was amplified by the unwinding of the WA State Government \$600 household electricity credit which led to a quarter-on-quarter increase in electricity costs of 91.2%. Electricity costs remain slightly below the pre-stimulus level.
- Other key contributors to the quarterly increase were a rise in fuel costs (+7.3%) which was reflected nationwide and a rise in household rents (+2.6%). Whilst house prices are not included in CPI calculations, the tightness in the housing market is flowing through into increasing household rents.
- On an annual basis, Perth CPI rose 4.2% which is slightly above the national increase of 3.8%. These annual figures are enlarged by their comparison to the low rate of inflation in June 2020, mid-recession. Nationally, key contributors to the rise include increases in fuel prices and the unwinding of the free child care stimulus.
- Whilst inflation is higher than it has been in a decade, the elevated level is expected to be temporary. However, global pressures on freight movements, the threat of lockdowns and northern hemisphere energy supply challenges may impact future prices. In the longer term, the Reserve Bank of Australia expects inflation to remain below the 2% to 3% target range until 2024.

Costs facing Local Governments are also set to rise



- As anticipated, the Local Government Cost Index (LGCI) increased in the June quarter as observed price increases manifested in the data.
- In the June quarter the index grew by 0.9%, the highest quarterly jump since 2015. On an annual basis the LGCI grew 1.2%.
- In 2020-21 the index increased 1.4%, driven by inflation in Non-residential building (5.6%), Non-road infrastructure (5.2%) and Road and bridge construction (3.5%). This was offset by modest increases in Employee costs (1.5%) and a fall in Materials and contracts (-0.9%).
- Looking forward, WALGA anticipates the LGCI will accelerate in coming periods.
- The LGCI forecast shows an increase of 3.5% in 2021-22, 2.6% in 2022-23 and 2.2% in 2023-24.
- Costs for the infrastructure and construction components of the index will remain elevated, with capacity constraints driving inflation. There are also expected to be upwards pressures on prices of Materials and Contracts as well as a modest increase in Employee costs.
- In line with RBA forecasts, the rate of price inflation across the LGCI components is expected to slow after the initial spike.

LGCI vs Perth CPI, Annual % Change



SOURCE: ABS CAT 6401.0; WALGA

LGCI Components – Forecast % Change



Component	2020-21	2021-22(f)	2022-23(f)	2023-24(f)
Employee costs	1.50	2.25	2.25	2.50
Materials and contracts	-0.9	4.2	2.8	1.3
Furniture	-0.1	1.4	1.4	1.4
Non-residential building	5.6	5.3	3.3	2.9
Machinery and Equipment	-0.5	3.4	2.6	2.6
Non-road infrastructure	5.2	5.2	3.2	2.8
Road and bridge construction	3.5	4.6	3.0	2.7
Utilities	0.0	1.4	1.4	1.4
Insurance	2.2	3.1	3.0	2.9
Other costs	1.6	1.9	2.0	2.0
LGCI	1.4	3.5	2.6	2.2

Data volatility means that the LGCI forecasts should be used with caution



- The significant challenges of forecasting in the current economic environment, mean **the LGCI should be used with caution.**
- The LGCI is a guide for economy-wide cost pressures, and **doesn't take into account local or regional issues** which may impact costs for individual Local Governments.
- Local Governments have reported significantly higher costs, particularly in relation to construction. As these become reflected in official data, the index could be revised higher.
- **It is important that Local Governments take into account their own local issues and experiences when considering cost pressures.** It will also be prudent for Local Governments to prepare for multiple scenarios for cost increases coming years.
- Downside risks also exist, particularly if another wave of COVID-19 hits WA and causes extended periods of lock down.
- WALGA will continue to monitor cost pressures and provide updates to the forecasts as more information becomes available.

Questions



If you have any question on the contents of this report, please direct them to the WALGA Economics team:

- Daniel Thomson – dthomson@walga.asn.au or (08) 9213 2015
- Dana Mason – dmason@walga.asn.au or (08) 9213 2020