

Westpac Coast-to-Coast December 2017

An update on Australia's state economies

Westpac Institutional Bank

200



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Westpac Economics

Sydney

Level 2, 275 Kent Street
Sydney NSW 2000
Australia
Telephone (61-2) 8254 8720
Facsimile (61-2) 8254 6907

Bill Evans

Chief Economist
Global Head of Economics &
Research

Andrew Hanlan

Senior Economist

Matthew Hassan

Senior Economist

Justin Smirk

Senior Economist

Elliot Clarke CFA

Senior Economist

Simon Murray

Economist

Auckland

Takutai on the Square
Level 8, 16 Takutai Square
Auckland, New Zealand
Telephone (64-9) 336 5671
Facsimile (64-9) 336 5672

Dominick Stephens

Chief Economist, New Zealand

Michael Gordon

Senior Economist

Satish Ranchhod

Senior Economist

Shyamal Maharaj

Economist

Paul Clark

Industry Economist

London

Camomile Court,
23 Camomile St,
London EC3A 7LL
United Kingdom

Singapore

12 Marina View
#27-00, Asia Square Tower 2
Singapore, 018961

New York

39th Floor
575 Fifth Avenue
New York, 10017 USA

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Editors: Andrew Hanlan, Elliot Clarke, and Matthew Hassan, Senior Economists

Email: economics@westpac.com.au

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Australian economic outlook

As we contemplate 2018 there are a number of key national themes that we believe will dominate economic and market developments. Our advice to customers throughout 2017 has been to expect Australia's growth rate to be anchored below trend in both 2018 and 2019. That has contrasted with the Reserve Bank's forecasts which anticipate growth picking up to 3.25% in both 2018 and 2019. We have recognised a solid ongoing boost to growth from non-residential construction; government spending and exports. However we are much more downbeat than official forecasts on the consumer; residential construction and equipment investment.

Signals from the September quarter national accounts are not encouraging for the official view. There is some evidence that households are reassessing prospects for income growth, particularly with respect to a lift in wages growth. Ongoing positive expectations for a boost in income growth have encouraged households to cut their savings rate from 7.5% in 2013 to 3.2% in September 2017 (up from 3.0% in June). We believe that household labour income growth will ease again in 2018 as wages growth remains benign and hours worked start to slow. Households which are also constrained by high debt and high energy prices are unlikely to be able to lift spending to allow the official growth forecasts to be reached.

Resulting below trend consumption growth will also discourage any recovery in equipment investment. Residential housing and alterations and additions have also started to slow and, based on the downturn in high rise approvals, we expect this downturn has further to run. Large increases in supply and a marked slowdown in sales to foreigners are weighing on the outlook for residential building.

House price inflation is disappearing. On a six month annualised basis prices are now falling in Sydney and Perth while price gains are slowing in Melbourne, Brisbane and Adelaide. The regulator's macro prudential policies are restricting interest only loans and tighter guidelines for all new loans are slowing house price inflation and credit growth.

In previous cycles the authorities have relied on raising interest rates to slow the highly cyclical housing market. This time, the same effect has been achieved by the regulator as banks have independently raised loan rates, with the downturn in foreign demand also weighing on activity.

Inflation is expected to remain benign holding a little below the bottom of the Reserve Bank's 2-3% target band. In this regard we are in agreement with the Reserve Bank which is forecasting that underlying inflation will hold at 1.75% in 2018 before lifting modestly to 2% in 2019.

Full time employment is growing near its fastest pace since the Global Financial Crisis. Jobs growth has been solid right across the country as outlined in this Report. The participation rate is also markedly higher as women and older workers stay in the workforce longer. While short term indicators point to jobs growth remaining strong into the new year we are more circumspect about the sustainability of this recent surge in jobs. Slowing residential construction, which has been responsible for a surge in new jobs, and cautious households are likely to restrict jobs growth through 2019.

While global growth has provided a solid boost to jobs we expect a marked slowdown in China in 2018 as the authorities enforce deleveraging and accelerate financial market reform.

Political uncertainty will remain a feature of the Australian economic picture in 2018 and 2019. Businesses will become somewhat more circumspect around investment and employment. In response the government is likely to embrace expansionary policies, particularly around tax, and may be prepared to compromise the proposed 2021 budget surplus to achieve a more constructive fiscal stance.

Under these circumstances we can not fall into line with most other economists who continue to anticipate that the Reserve Bank will begin to raise rates in 2018. Indeed we have been of the view through 2017 that the official cash rate will remain on hold in both 2018 and 2019. With rates on hold in Australia and the US Federal Reserve continuing to raise rates, Australia's cash rate is set to fall below the Federal funds rate by mid-2018.

The US economy is operating with much less 'slack' in its labour market (an unemployment rate of 4.1% compared to an estimated full employment rate of 4.75%) than Australia (unemployment rate of 5.4% compared to a full employment rate of 5.0%) but little wage pressure has emerged. Over the course of 2017 the USD has fallen by around 8% despite four rate hikes since December 2016. With financial conditions also easing via a 20% rally in the US equity market, the Fed has seized on the opportunity to raise rates in anticipation of rising inflation. Without access to an effective macro prudential policy (due to the highly regionalised and low concentration of lenders in the market) it has relied on higher rates to deal with the threat of financial instability.

We expect the Fed's tightening cycle to continue in 2018, with two more 25 basis point hikes in June and December. That would see the AUD/USD yield differential in the overnight market contract to minus 38 basis points - a situation we have not seen since early 2000. A heavy toll will be taken on the AUD with the currency forecast to fall to USD 0.70 by the end of 2018. With upward pressure on the USD in 2018 and inflation remaining benign we expect that the Fed will hold rates steady through 2019 ensuring that the negative yield differential with Australia holds through 2019 and that the AUD will fall further. We expect a move down to USD 0.68 in 2019, with downside risks.

Bill Evans, Chief Economist

Australian economic outlook

Chart 1.

GDP growth: year-end contributions

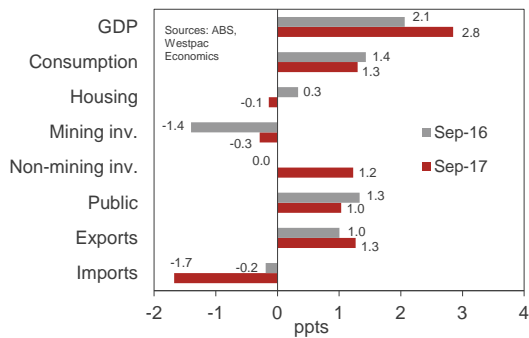


Chart 2.

Australian outlook: year-end contributions

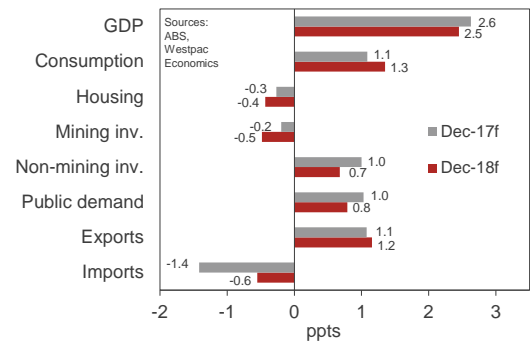


Chart 3.

Household labour income underperforming

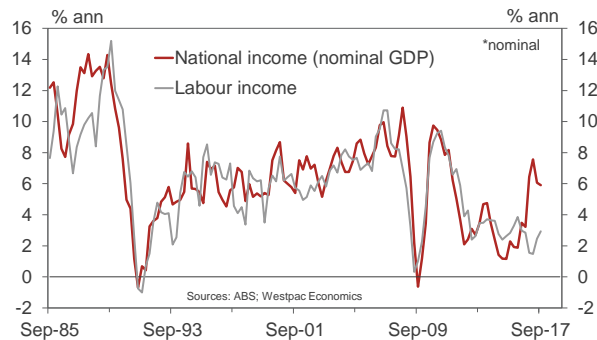


Chart 4.

Consumer spending slows

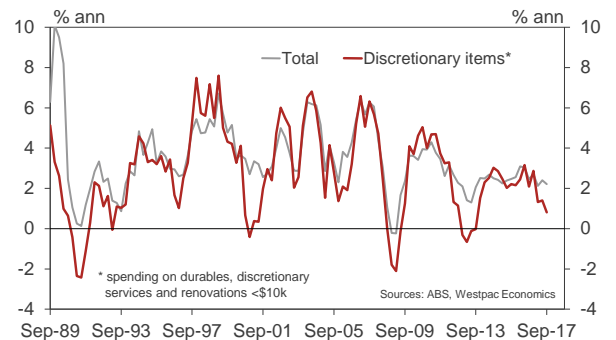


Chart 5.

Non-residential building approvals climb

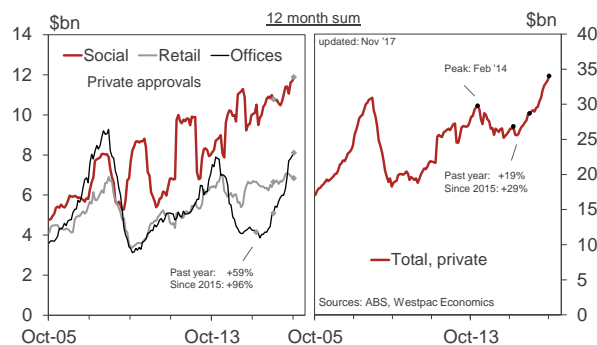
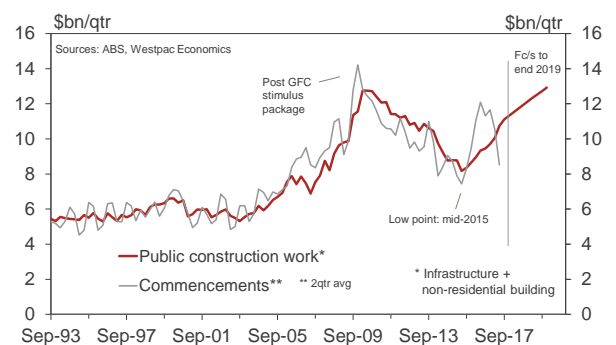


Chart 6.

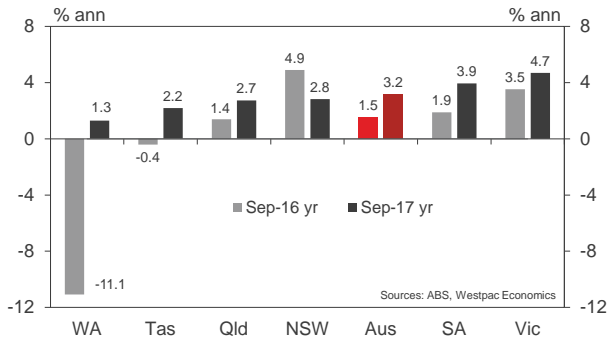
Public construction strong upswing



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States overview

Domestic final demand



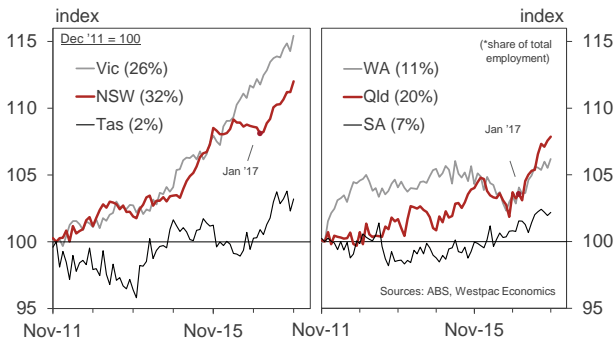
Domestic demand has accelerated across Australia, with annual growth lifting to 3.2% in the September quarter, up from 1.5% a year ago, a result around the long-run average of 3.4%. The acceleration is evident across each of the states, with the exception of NSW, which is set to gain momentum near-term.

In general, business investment and public demand are making a larger contribution to growth, at a time of stronger world growth, offsetting a slowing in household demand.

The Victorian economy is the clear pace setter, with annual demand growth a brisk 4.7%, supported by strong population growth of 2.3%.

Conditions in the mining states of WA and Qld have improved. There is a diminished drag from the mining investment wind-down and company profits are up on higher commodity prices. Annual state demand growth is positive in WA, after 16 negatives in the past 18 quarters.

State jobs markets

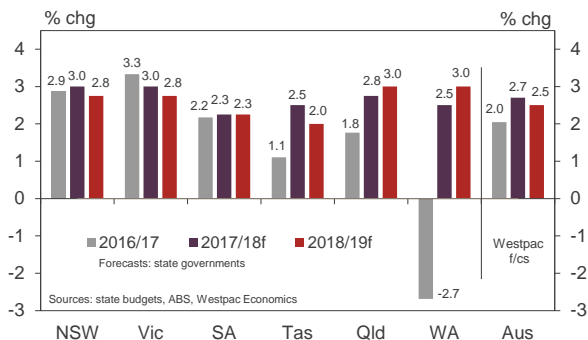


NSW annual state demand growth has moderated to 2.8%, but is set to rebound led by a looming acceleration in public demand, with the government committing to additional transport infrastructure.

The jobs market heated up in 2017, with a rare instance of synchronised strength across the four major states. Employment nationally advanced by 3.2% in the year to November, accelerating from 0.9% for 2016, a result impacted by uncertainty around the July Federal election. Annual jobs growth by state currently is: 4.0% Qld; 3.5% Victoria; 3.1% NSW; 2.9% Tasmania; 2.7% WA and 1.4% SA.

Despite the current hiring burst, which we expect to moderate in 2018, consumer spending has slowed, impacted by weak wages growth, high debts and a cooling housing market. Nationally, consumer spending rose only 0.1% in Q3, with falls in the southern states, broadly flat outcomes in Qld and WA, and +0.2% in Vic and +0.4% in NSW.

Growth outlook by state: GSP



As we go to press, the four major states have released their mid-year budget updates, while updates from SA and Tasmania are pending. Each of the four states upgraded their employment forecasts for 2017/18. Victoria upgraded their output growth forecast to 3.0% for 2017/18, up from 2.75%, while WA lowered their forecast to 2.5% from 3.0%. NSW and Qld confirmed their 2017/18 output growth forecasts at 3.0% and 2.75% respectively.

Taken together, the state governments expect economic growth to lift to 2.8% in 2017/18, up from 2.0% for 2016/17. We are in broad agreement with this view. We also broadly agree with the spread of forecasts across the states. The major non-mining states of NSW and Victoria, with a greater focus on service exports, are set to outperform.

Turning to 2018/19, Westpac is a little less optimistic, expecting output growth of 2.5% vs the 2.8% by the states. A turning down of home building activity, ongoing sub-par consumer spending and a likely decline in commodity prices will act to temper conditions, in our view.

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States overview

Chart 1.

State final demand, contributions

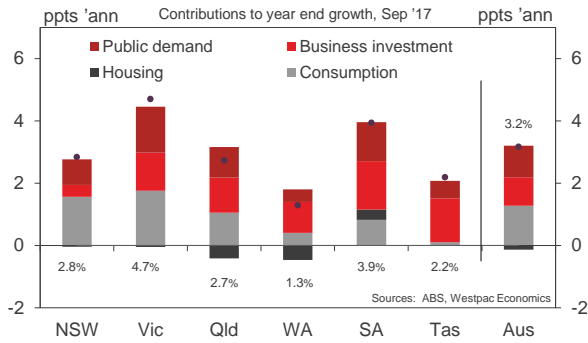


Chart 2.

Consumer spending slows

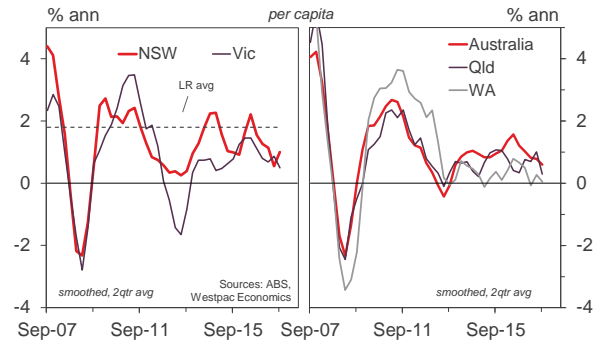


Chart 3.

Dwelling approvals: off highs

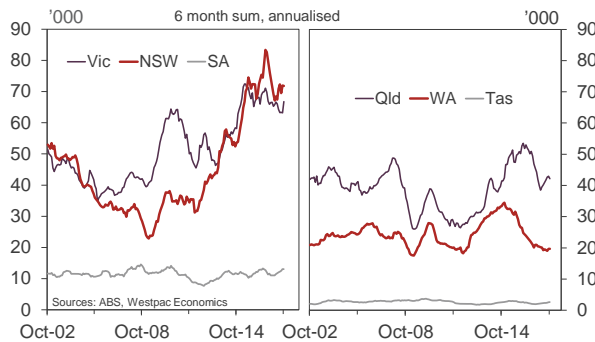


Chart 4.

Dwelling prices: housing markets cool

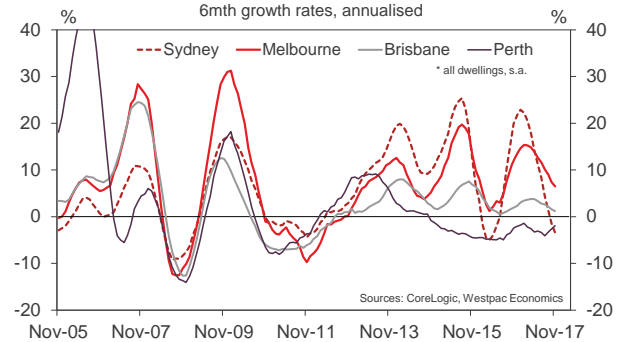


Chart 5.

Non-residential building approvals lift

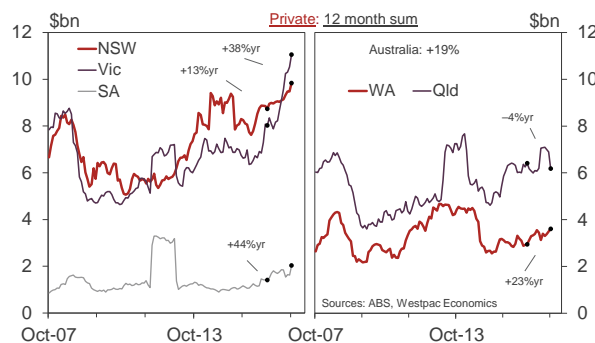
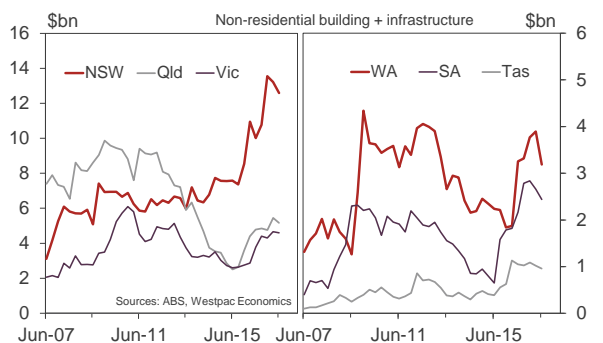


Chart 6.

Public construction: growing work pipeline



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State demand: shifting mix

Chart 1.

NSW state demand

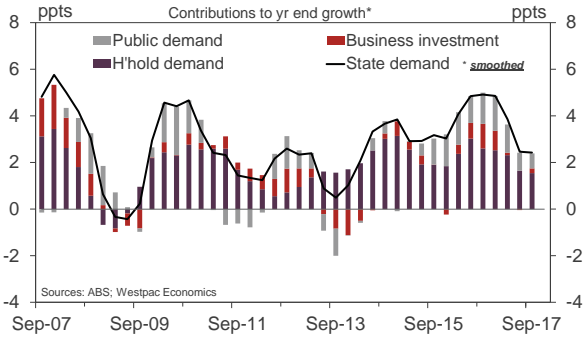


Chart 2.

Victoria state demand

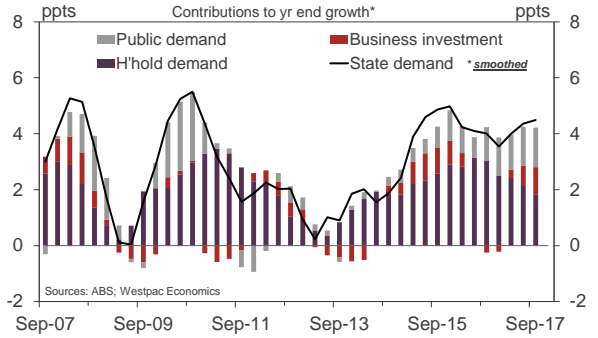


Chart 3.

Qld state demand

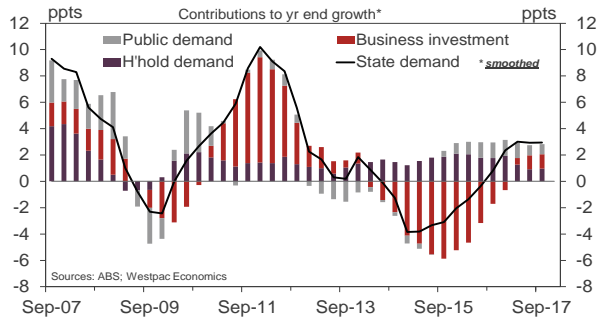


Chart 4.

WA state demand

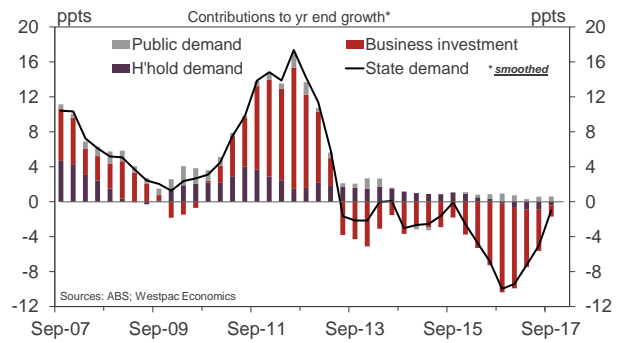


Chart 5.

SA state demand

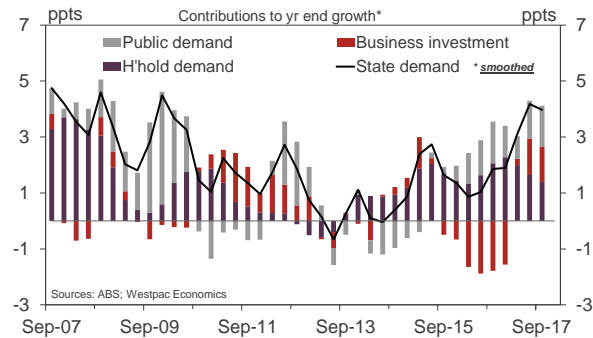
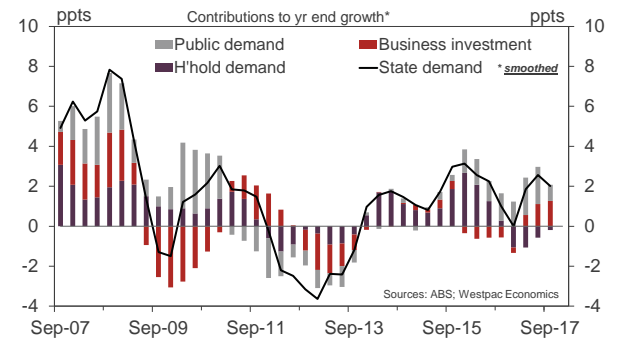


Chart 6.

Tasmanian state demand



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Population growth lifts in south-east

Chart 1.

Australia's population boosted by o/s migration

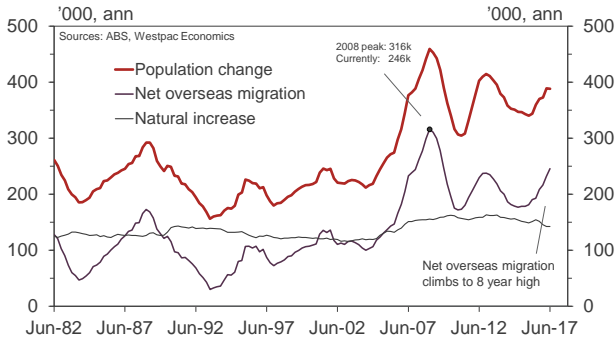


Chart 2.

Population growth nationally lifts to 1.6%

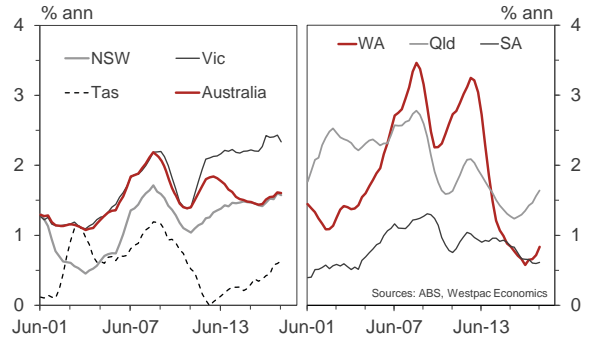


Chart 3.

Overseas migrants flock to NSW & Victoria

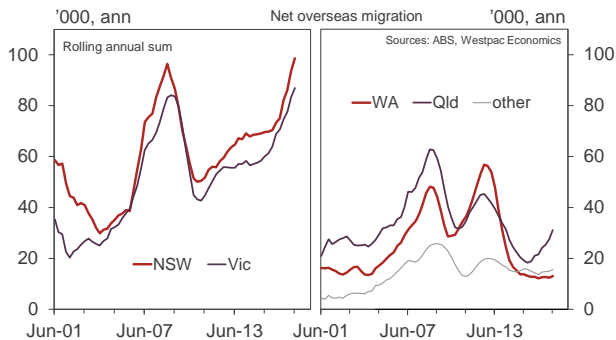


Chart 4.

Population growth: south-east

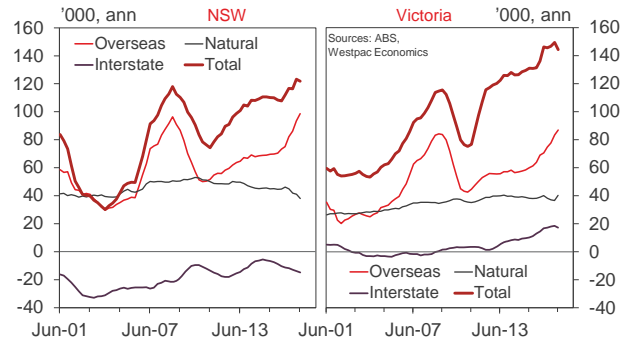


Chart 5.

Population growth: southern states

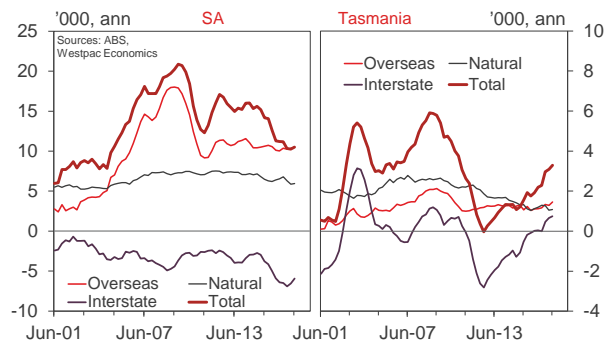
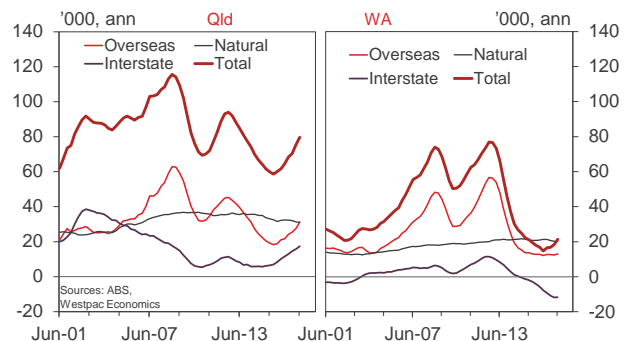


Chart 6.

Population growth: mining states



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Employment and activity: by state

Chart 1.

NSW: jobs & household demand

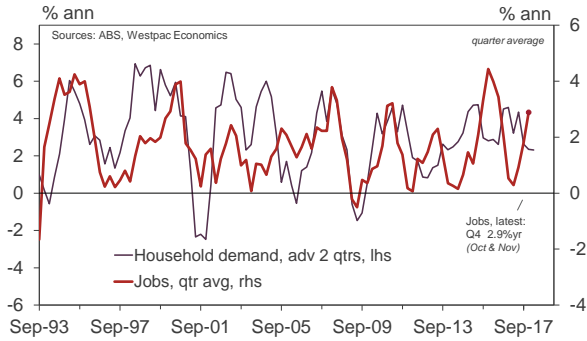


Chart 2.

Victoria: jobs & household demand

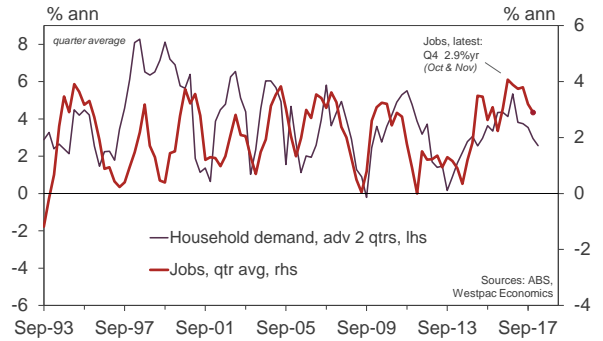


Chart 3.

WA: jobs & household demand

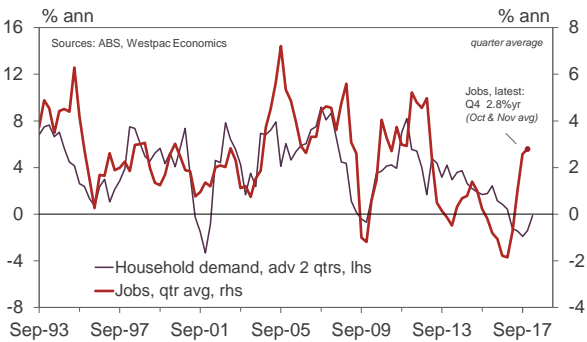


Chart 4.

Qld: jobs & household demand

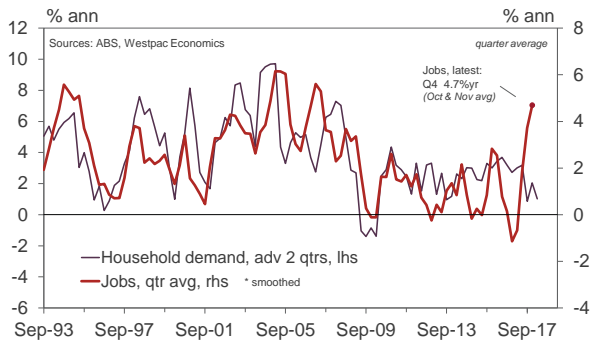


Chart 5.

Tasmania: jobs & household demand

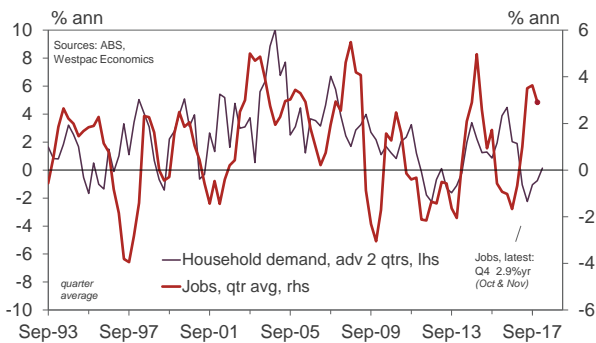
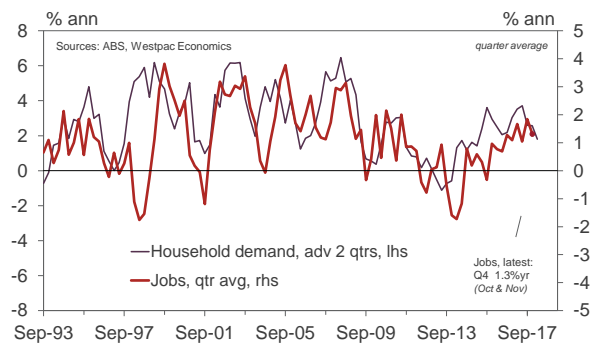


Chart 6.

SA: jobs & household demand



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Employment by industry: NSW & Victoria

Here we turn our attention to employment trends on a state basis, with a particular focus on jobs by industry.

The NSW jobs market moved through a soft patch in 2016, with employment up only 0.2% in the year, an outcome dented by uncertainty around the July Federal election, as well as a temporary consolidation in public investment. In the year to November 2017, employment increased by a stellar 3.1%. That saw the unemployment rate fall to 4.6%.

Employment in the health sector resumed its strong upward trend in the second half of 2017, after a temporary consolidation in 2016. The construction sector continues to be a jobs generator, with an upswing in work across both the public and private sectors. The leisure and hospitality sector has also made gains in 2017 as international tourism and foreign student numbers climb.

The Victorian jobs market is powering ahead for a fourth consecutive year, with the state experiencing well above trend population growth, currently at 2.3%.

Employment increased by 3.5% in the year to November 2017, building on gains of 3.1%, 2.0% and 4.4% for the three previous years. The trend unemployment rate is 5.7% currently, not greatly different from level prevailing during 2016.

Employment in the labour intensive leisure and hospitality sector is surging, up around 8% in 2016 and a further 8% in 2017, with international holiday makers and foreign students flocking to Melbourne. Construction employment is also trending strongly higher, as the state builds new homes, offices and infrastructure for the rapidly growing population.

Chart 1.

NSW: employment by sector

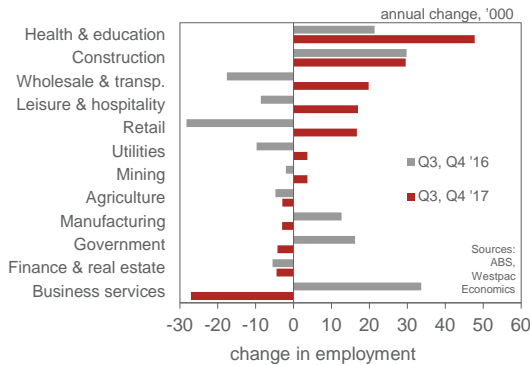


Chart 2.

Victoria: employment by sector

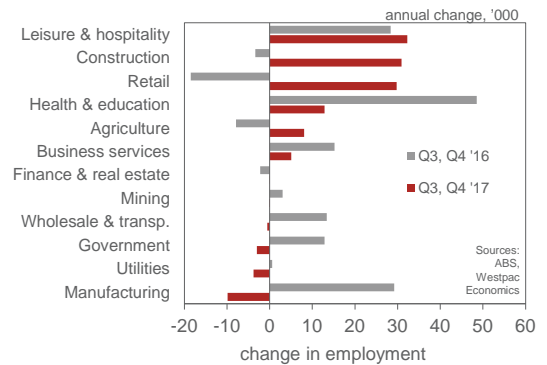


Chart 3.

NSW employment by sector

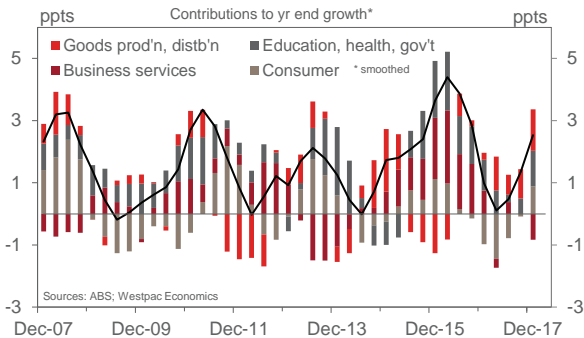
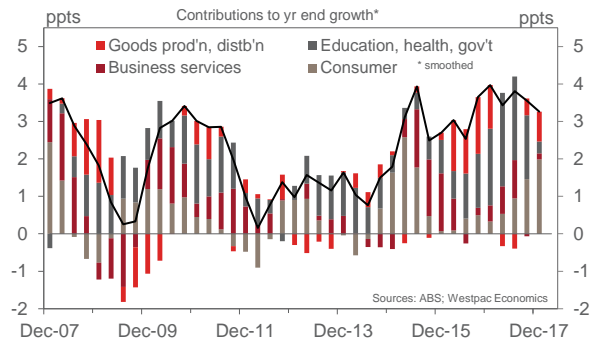


Chart 4.

Victoria employment by sector



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Employment by industry: Qld & WA

The mining states improved in 2017, a development which translated into stronger job creation.

In Qld, there was a stark turnaround, with employment advancing by a brisk and unsustainable 4.0% in the year to November 2017, correcting for a surprisingly sharp 1.1% decline in 2016. The unemployment rate has edged lower, dipping below 6.0%.

As in NSW, employment in the health sector resumed its strong upward trend, after a surprise consolidation in 2016. The introduction of the National Disability Insurance Scheme is contributing to the lift in health sector employment. Construction sector employment is advancing, reversing the pull-back from 2013 to 2015. The leisure and hospitality sector is also performing well, leading to a lift in employment.

The jobs market in WA moved ahead in 2017, as the drag from the mining investment wind-down was greatly reduced. Employment increased by 2.7% in the year to November, reversing a sharp 2.2% fall during 2016, which was preceded by flat outcomes for the three years 2013 to 2015. The trend unemployment rate is still elevated, at 6.2%.

A turnaround in construction employment was a key positive, with a flurry of work on the last of the major gas projects, which are to be progressively completed this year and into 2018. Employment levels are expanding in health, as well as leisure and hospitality, as is occurring nationally. However, impacts from the end of the mining investment boom are still evident, with trend declines in employment levels across mining, manufacturing and professional services.

Chart 1.

Queensland: employment by sector

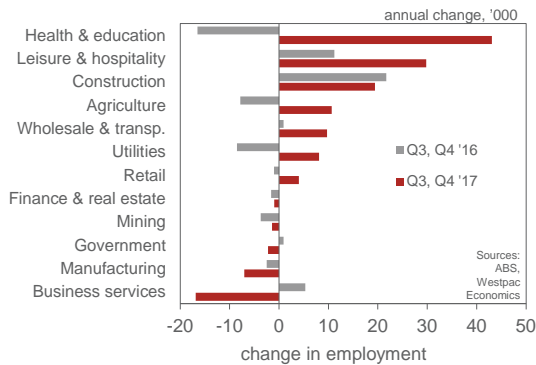


Chart 2.

Western Australia: employment by sector

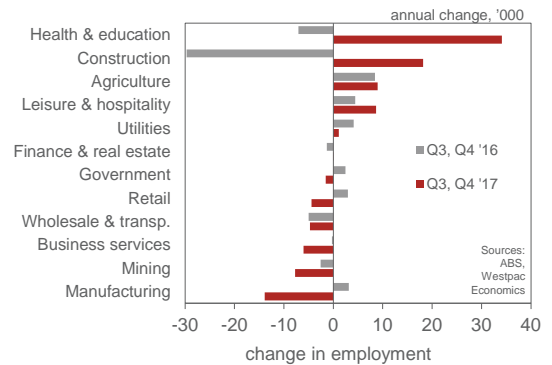


Chart 3.

Qld employment by sector

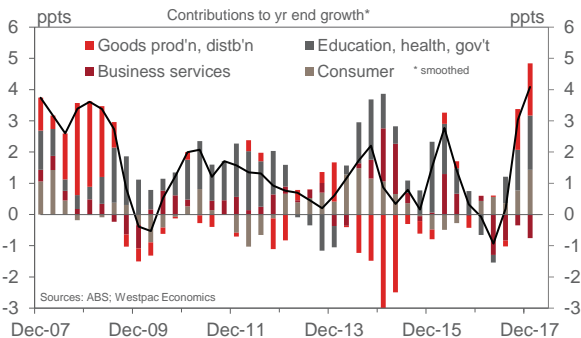
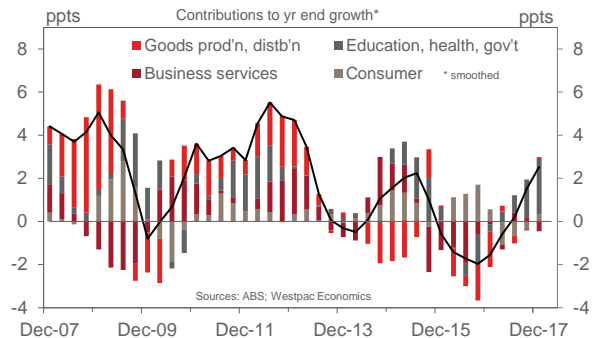


Chart 4.

WA employment by sector



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Employment by industry: SA & Tasmania

Employment trends in South Australia remain choppy quarter to quarter. In the year to November 2017, employment rose by 1.4%, up from 0.9% for 2016 and outpacing population growth of 0.6%. The unemployment rate continues to trend lower, moderating to 5.8%.

Construction work is increasing, leading to an upward trend in employment through 2016 and 2017. Employment levels in the transport, postal & warehousing sector has rebounded sharply, more than reversing a pronounced decline through 2015/16. The health sector is also notching up strong job gains, mirroring the national trend. The leisure and hospitality sector is also expanding, with the lower dollar a boost for the state's tourism sector. However, employment in the manufacturing sector ended 2017 on a soft note with the closure of Holden's Elizabeth factory.

The Tasmanian jobs market was a stand-out in 2017, with employment expanding by a brisk 2.9% in the year to November. Keep in mind that population growth is a modest 0.6%, well below the national figure of 1.6%. This represents a sharp improvement on a 0.7% rise in employment in 2016. A little surprisingly, the trend unemployment rate was relatively stable in 2017, at 5.9%.

Key was the health sector, which saw employment levels bounce back in 2017, reversing a sharp pull-back in 2016. Construction sector employment advanced, with work trending higher, supported by public investment and an emerging upswing in home building activity. More generally, employment gains in 2017 were broadly based across: business services; retail; mining; manufacturing; leisure and hospitality; and agriculture.

Chart 1.

South Australia: employment by sector

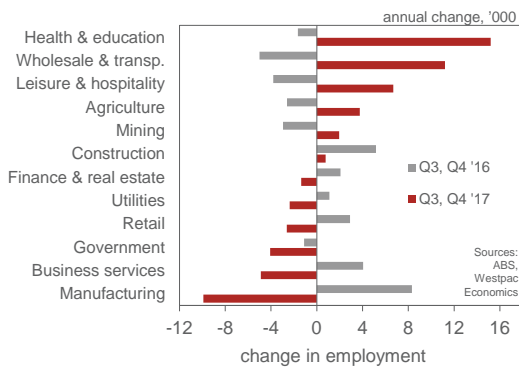


Chart 2.

Tasmania: employment by sector

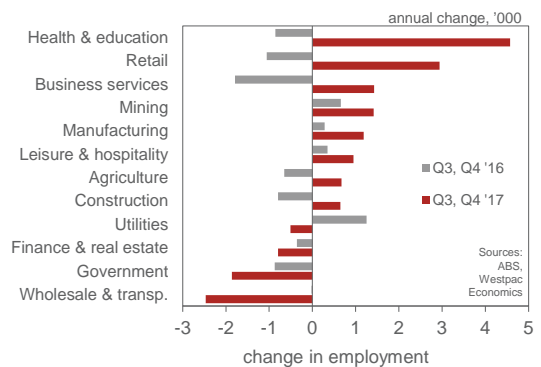


Chart 3.

South Australia employment by sector

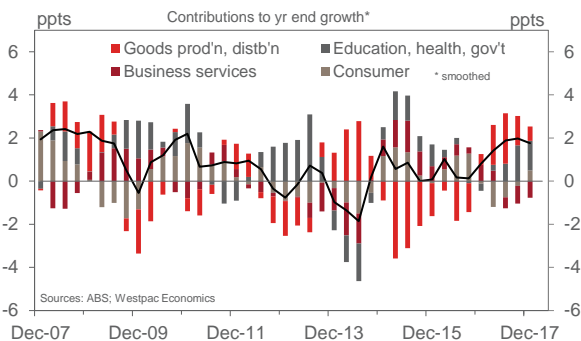
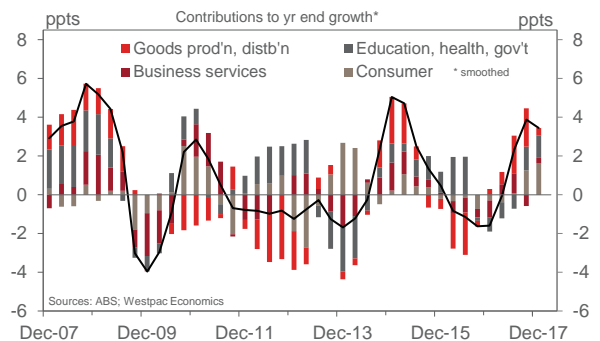


Chart 4.

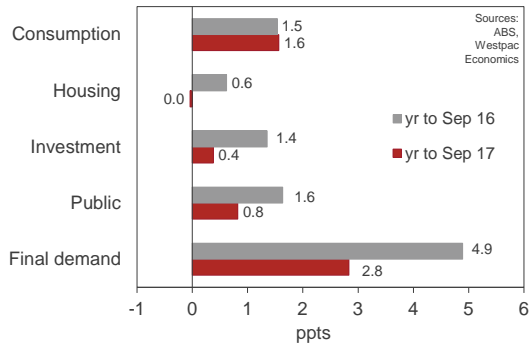
Tasmania employment by sector



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NSW: above trend output growth ...

NSW: contributions to state final demand

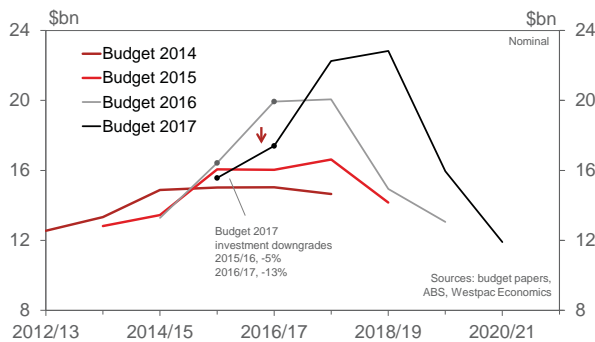


The NSW economy accelerated in the second half of 2017 after a subdued start to the year, hampered by adverse weather. In the September quarter, state demand increased by 1.0%qtr, 2.8%yr.

Population growth is 1.6% currently and will be above the long-run average of 1.1% for a 6th consecutive year in 2017. Plentiful job opportunities are encouraging increased migration from both interstate and overseas.

Business investment is advancing, adding to the capital stock to meet the needs of a growing population. Private infrastructure investment leapt 46% over the past year, rebounding from the low at end 2015. Private non-residential building having eased back from mid-2016 to mid-2017 is set to advance. Approvals for the year to October are 13% above that for the year prior as more office projects proceed. As to equipment spending, the environment is mixed, constrained by patchy household demand.

NSW public investment: budget forecasts

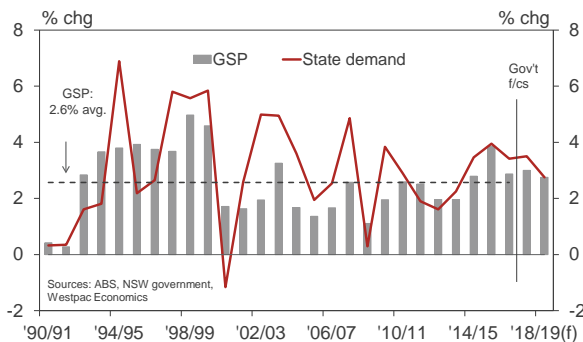


Expansionary fiscal policy is a key support for the state economy, with a focus on investment in transport infrastructure. The state fiscal position is sound, with revenues boosted by the housing boom and asset recycling enabling better use of the balance sheet.

Public demand grew by 3.9% over the past year and is now 14.5% higher than at the start of 2015, some 2½ years ago. Public investment is part way through an extended, strong upswing. Investment climbed 15% in the year to mid-2016, followed by a consolidation, up only 2% in the year to mid-2017. The upswing has resumed and the mid-year budget update confirms considerable further upside.

No surprise jobs growth has been brisk in 2017, at 3.1% currently. However, consumer spending is subdued, at 0.4%qtr, 2.6%yr in September constrained by weak wages growth, high debt and cooling house prices. The home building boom is set to turn, with activity to moderate from high levels, consistent with the decline in approvals.

NSW economic performance & outlook



State real output expanded by 2.9% in 2016/17. While a moderation from the brisk 3.9% increase in 2015/16, it was still the third above trend year, with trend 2.6%.

The international backdrop has been a plus, with world growth strengthening in 2017 and the Australian dollar well down from the highs of earlier in the decade. Service exports are performing strongly, adding 0.8ppts to annual activity, well above the national average of 0.5ppts. This is to meet rising demand from the Asian region, with Sydney a magnet for holiday makers and students.

In their December mid-year budget update, the state government confirmed their forecasts for real GSP of 3.0% and 2.75% for the next two fiscal years - a continuation of above trend growth. Strong population growth, rising business investment and expansionary fiscal policy will be key growth drivers. However, upside will be constrained by lacklustre consumer spending and a cooling housing market.

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... led by government, businesses and exports

Chart 1.

NSW state final demand: rebounding

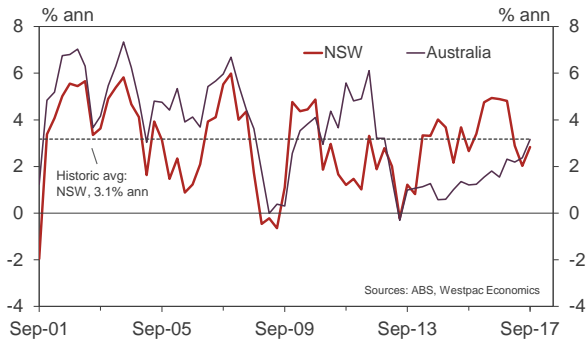


Chart 2.

NSW consumer spending below trend

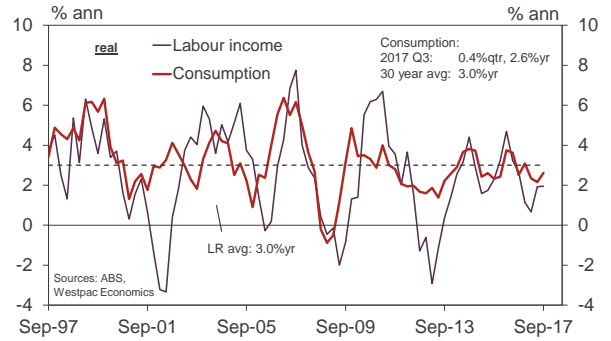


Chart 3.

Dwelling approvals: down from highs

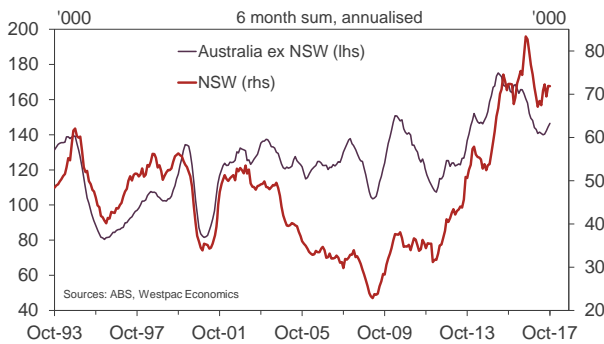


Chart 4.

New dwelling activity: set to moderate

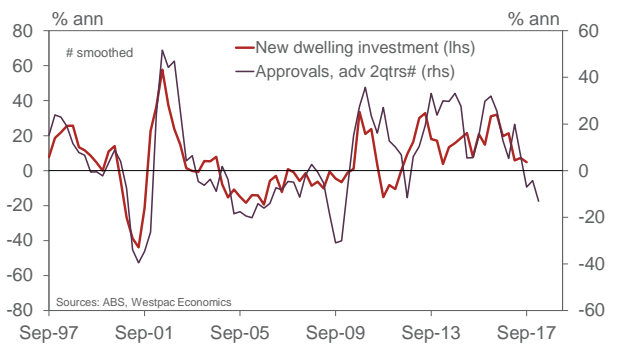


Chart 5.

NSW population growth: continues above trend

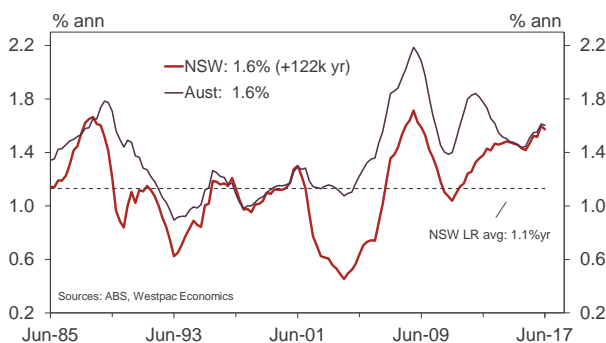
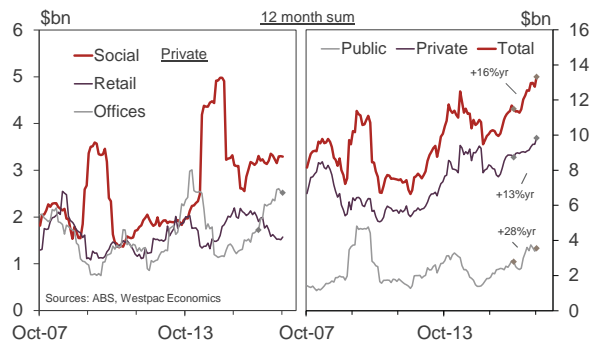


Chart 6.

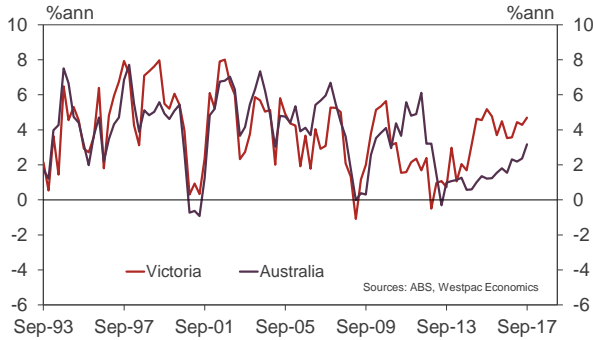
Non-residential building approvals climb



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Victoria: consumer pauses, housing slows ...

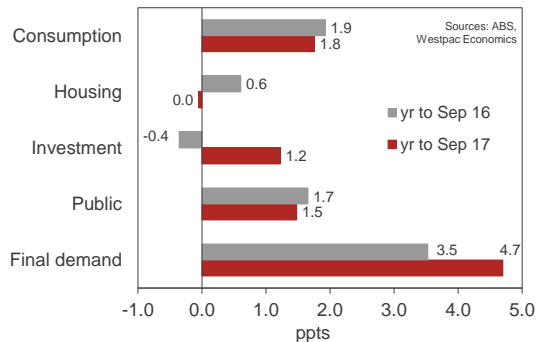
Vic domestic demand



Victoria has consistently outperformed the rest of Australia over the past 3 years. Although the gap is now narrowing, the move is coming via improvements in other states rather than a slowdown in Vic. It may be a different story in 2018 though with the state's housing market moving into a clear downturn. That said, the housing slowdown looks to be relatively mild with the state continuing to benefit from key positives: strong population growth, surging service exports and increased government spending in particular.

State demand throttled back in Q3 with a 0.4% gain in the quarter. At 4.7%yr, annual growth remained strong though, well above the state's long run average of 3.4%yr. The Vic labour market also points to some moderation from the 'red-hot' growth in 2016 – employment gains have slowed to 3%yr, in line with the national pace but considerably cooler than the state's 4.1%yr peak in 2016. The unemployment rate has been relatively steady throughout, mainly reflecting the state's migration-led population boom which is showing no signs of abating.

Vic: contributions to state final demand

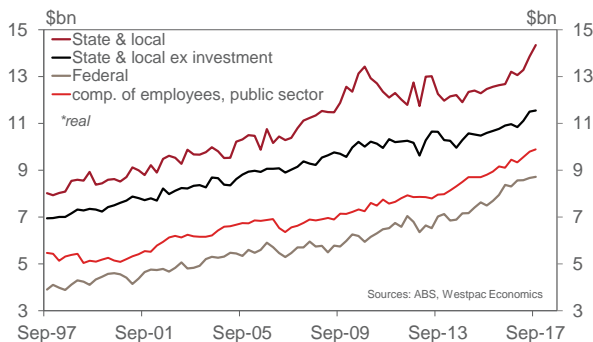


Consumers were the main source of softness in Q3. Consumption rose just 0.2%, a decline of 0.4% in per capita terms, after averaging gains of 0.8% a quarter over the previous year.

Housing investment also fell sharply in Q3, led by a 13% drop in renovation work. That partly reflects the more cautious consumer tone. However, it likely also reflects the material slowing in the state's housing market and changes to depreciation allowances available for property investors introduced in the Federal Budget. New dwelling investment has held up better (-2.5%qtr, +1.9%yr) but is set to decline. Approvals are pointing to a 5-10% contraction – our analysis of the project pipeline in Vic (dominated by high rise) suggests the decline will be spread over 2018 and 2019.

Business investment continues to show strength, rising 11%yr. Gains are concentrated in construction: non-residential up 30%yr and engineering work 13%yr, but equipment up just 2.5%yr. An office-led surge in approvals points to more non-residential construction strength ahead.

Government demand & wage spend



Rising government activity has supported growth over the last year, total public final demand up 7.1%yr led by a big surge in public investment (up 19%yr). Solid growth in baseline spending – at both Federal and state level – is combining with a surge in state government investment. The lift looks set to carry through 2018 – although growth is likely to slow as the boost from new projects levels out.

The Vic state government's mid-year update upgraded its 2017-18 GSP growth forecast from 2.75% to 3% with employment growth now seen tracking at 3% vs 2% previously. As noted in our last report, Vic's population growth has been revised up significantly by the ABS. The state government expects this elevated pace to continue keeping the unemployment rate slightly higher with an expected lift in wages growth also expected to come through more slowly. The latest data shows foreign student enrolments up 17.5% over the year to October, suggesting little or no slowing in Vic's migration influx. With a healthy surplus and 'AAA' rating the state government also has plenty of scope to add additional support to growth.

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... but popn, services, govt drivers power ahead

Chart 1.

Vic housing construction moves into downturn

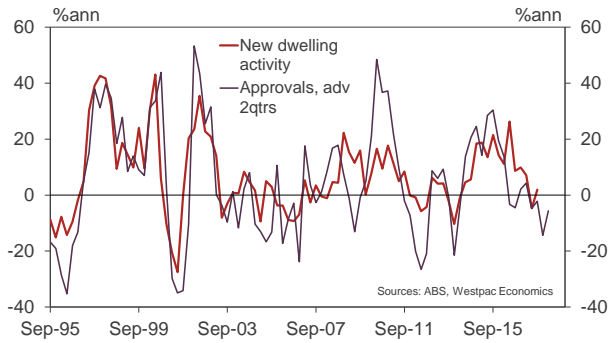


Chart 2.

Melbourne house prices

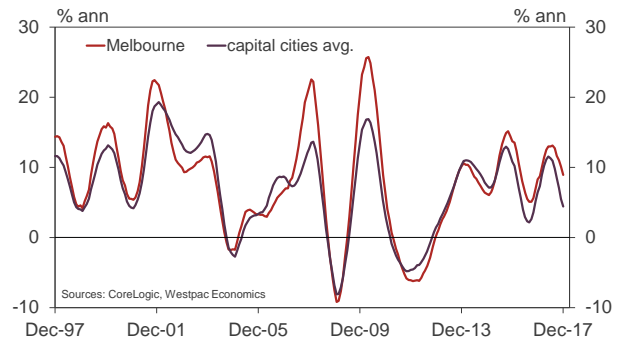


Chart 3.

Vic population growth strong and on the rise

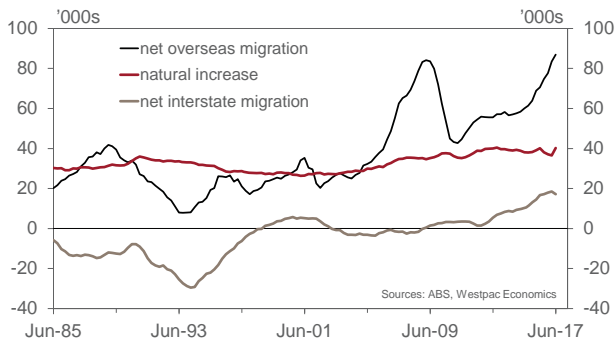


Chart 4.

Vic labour market

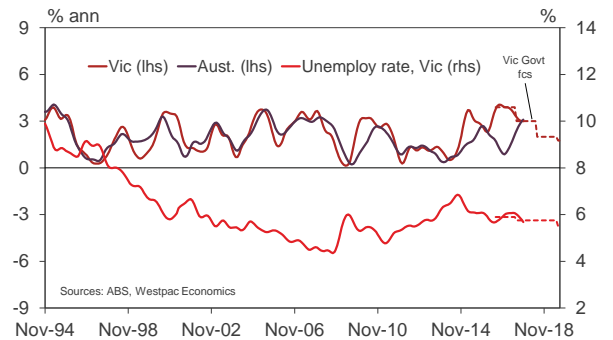


Chart 5.

Vic business investment: mixed gains

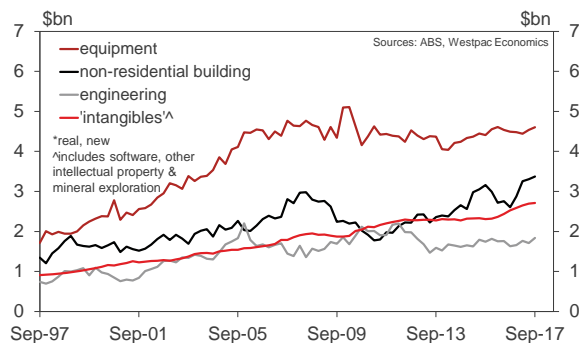
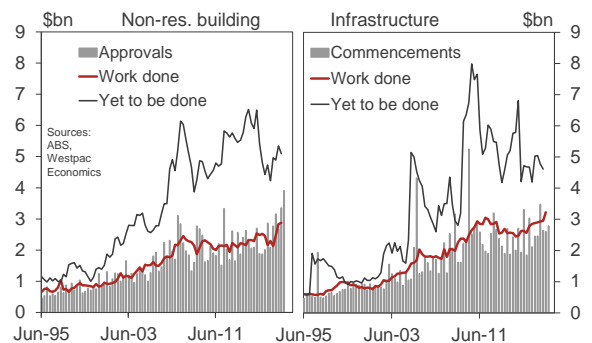


Chart 6.

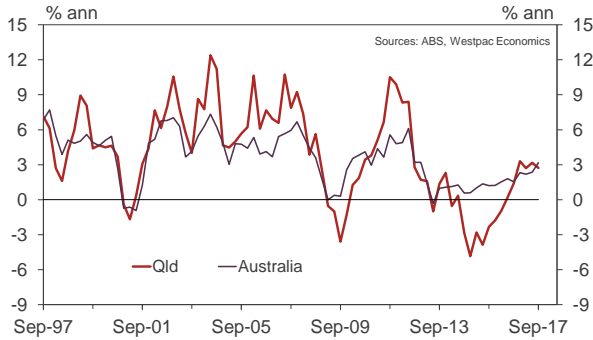
Vic's non-res construction pipeline



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Queensland: opportunities are building...

Qld domestic demand has rebounded

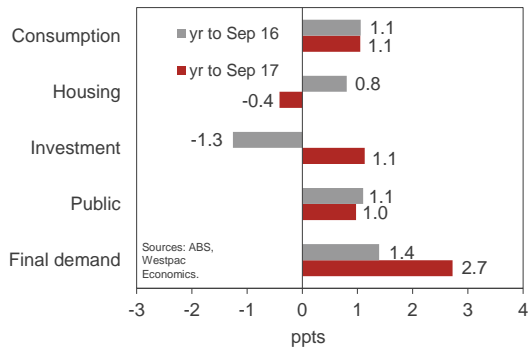


Queensland state demand has remained fickle over the past year, a strong outcome immediately being followed by a soft print.

In sequence, Q3 was a soft quarter, activity rising 0.2% (2.7%yr). This volatility has primarily been driven by household demand which was flat in Q3 after a 1.2% rise in Q2. The weakness in Q3 was broad based across consumption and residential investment, with both components broadly unchanged in the quarter. Over the year, consumption is up 1.9%; however, housing construction is down 6.8%.

Underlying demand in Qld has been held back for a number of years by unfavourable population and labour market dynamics. The above outcomes are evidence of the lingering influence of these factors. That said, opportunity for the state is building, both with respect to domestic and external demand.

Qld: contributions to state final demand

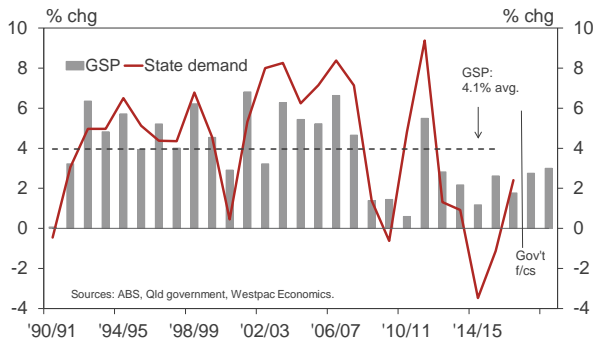


To begin with, population growth is strengthening, with interstate and international migration moving higher. From a low of 1.2%yr in Q3 2015, total growth in the population has since risen to 1.6%yr (Q2 2017). This is still below the historic average, but momentum is positive nonetheless.

Importantly, those arriving in the state have found work. The employment to population ratio has risen from a low of 60.1% at November 2016 to 62.0% as annual growth in full-time employment rebounded from -2.0%yr to +3.7%yr - its fastest pace since late-2007.

Qld will continue to benefit from resource income, but for job creation, the future is centred on the services sector, particularly tourism and education. If we are correct in anticipating a lower Australian dollar, these sectors will benefit materially. However, these gains may be offset by a reduced call for workers in residential construction over the coming year.

Qld economic performance & outlook



To aid the state's ongoing transition towards service-led growth, and offset residential construction's unwind, the recently re-elected state government has increased their capital expenditure plans to 2021 by \$1.6bn to \$44bn. Employment in essential services is also being increased to meet the growing population's needs.

It is clear from the government's latest forecasts that there remains a degree of caution over the outlook. They confirmed their forecasts for output growth of 2.75% in 2017-18 and 3.00% in 2018-19. Positives are the strengthening of firming population growth and robust external demand, while the NAB's business survey points to further gains for business investment ahead.

However, consumer sentiment is lagging, implying that more robust strength in household spending could be a while coming. In addition, home building activity is set to moderate, weighing on the outlook.

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... with services to the fore

Chart 1.

Qld net migration has rallied off historic lows

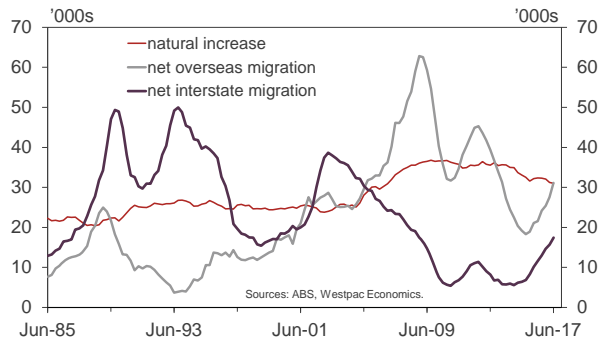


Chart 2.

Qld: employment's share of population rising

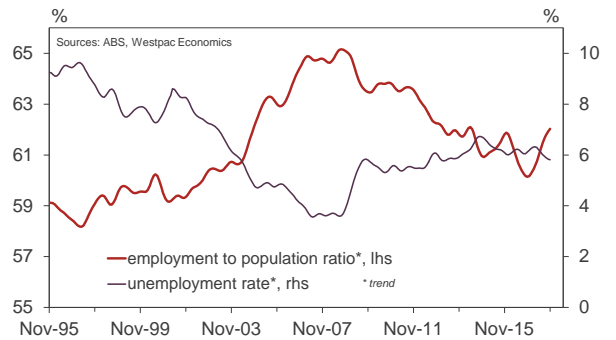


Chart 3.

Weak incomes still restricting spending

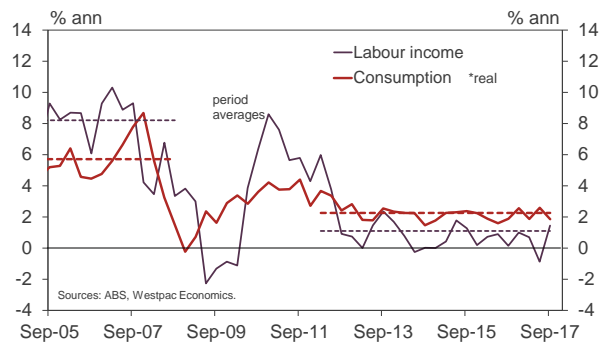


Chart 4.

Qld dwelling approvals pipeline to rundown

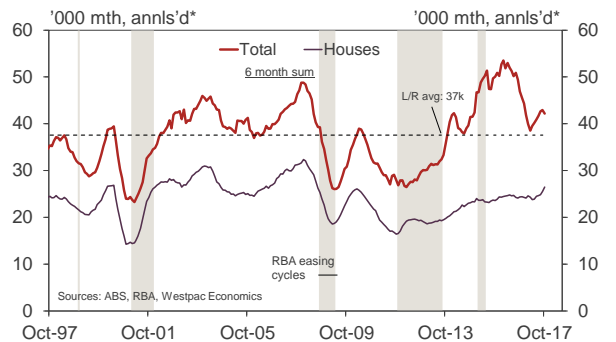


Chart 5.

Qld business investment: now in uptrend

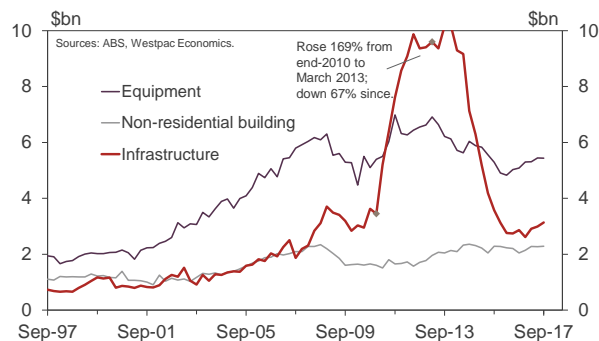
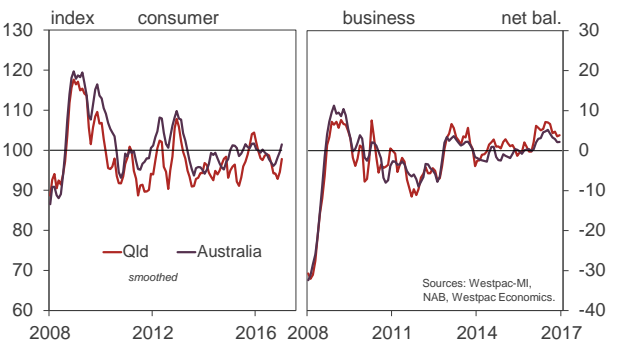


Chart 6.

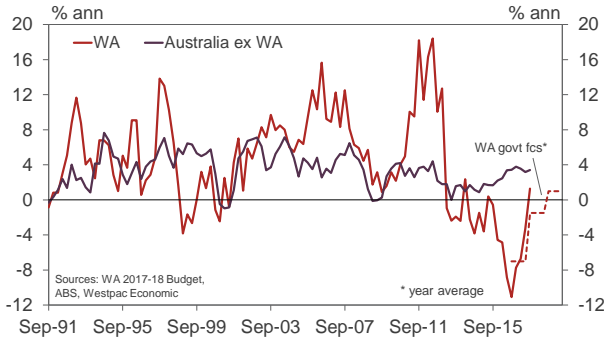
Business confidence robust; consumer lags



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Western Australia: the comeback begins...

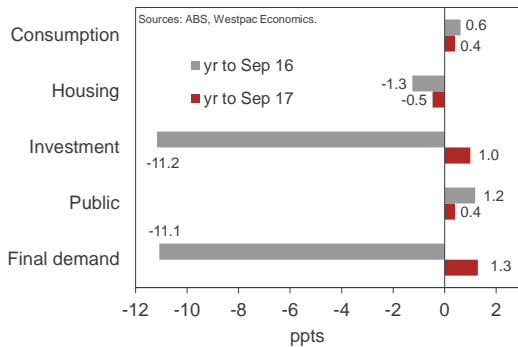
WA state demand: deep contraction ends



After much hope and several false starts, WA's economic recovery finally looks to be coming through. Having scaled extreme highs during the resources boom, the at times precipitous, wind down in mining investment now looks to have largely run its course. Meanwhile the extended slump in commodity prices that accompanied the downturn, putting, at times, severe pressure on incomes in the sector and state, also looks to have ended. Indeed, prices have for the moment at least, turned positive.

Conditions outside WA's mining sector are not as uniformly improved - while labour markets provide the most convincing evidence of a turnaround, the downturn in housing markets has yet to stabilise and consumers remain under significant income pressures. Weak population growth, subdued wages growth and continued fiscal restraint from the state government also remain clear headwinds. Overall, while a recovery is now more clearly underway, an immediate resurgence back to strong growth rates looks unlikely.

WA: contributions to state final demand

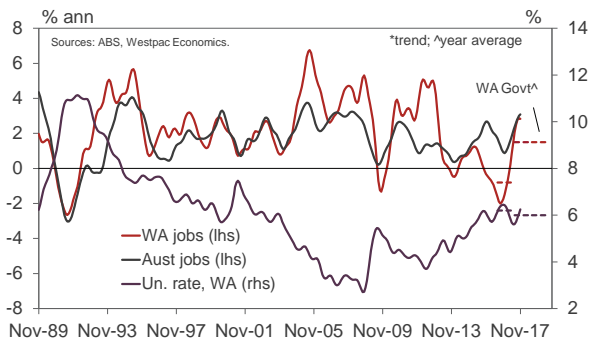


The WA economy had its best quarter in a long time in Q3. State final demand rose 0.9%, taking annual growth to 1.3% - the first positive outcome since June 2015 and only the second positive recorded since March 2014.

The turnaround is even starker in labour markets. After contracting 2% in the year to September 2016, employment has rebounded strongly, annual growth turning positive in April and hitting 2.7% in November, the strongest pace since January 2013 and essentially bringing WA job growth in line with the robust national pace. The unemployment rate has broadly levelled out, outright improvements being capped by a rising participation rate (most likely reflecting 'marginally attached' people re-entering the labour market in response to improved job prospects).

The catalyst for the turnaround has been business investment. Annual growth in investment has risen from a low of -40%yr a year ago, effectively slicing 11ppts off demand, to +4.6%yr currently.

Jobs market showing a clear resurgence



The picture across WA's household and housing sectors is less positive. Household consumption remains weak, up just 0.8%yr. Even with renewed jobs growth, aggregate labour income is still contracting, reflecting very weak wage inflation (running at just 1.4%yr) and a major drag from 'structural' factors, the shifting mix in particular (i.e. gains in 'low wage' jobs but losses of 'high wage' mining jobs). Even if the latter diminishes, the subdued wage environment is likely to cap any near term resurgence in labour incomes.

On housing, there are more tentative signs of stabilisation. Housing investment reported its first positive quarter since September 2015 (+3.7%, the pace of annual decline moderating to -10%yr from -30% at its peak). Approvals suggest new dwelling investment should stabilise by mid-2018. Although Perth prices are still down 2.1%yr the pace of annual declines has moderated with the four months of rises since September, the best run of gains since 2014. As with the household sector, 'structural' negatives remain significant, a large overhang of vacant stock in particular.

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... income, jobs lift; consumer, housing lag

Chart 1.

WA households: still under pressure

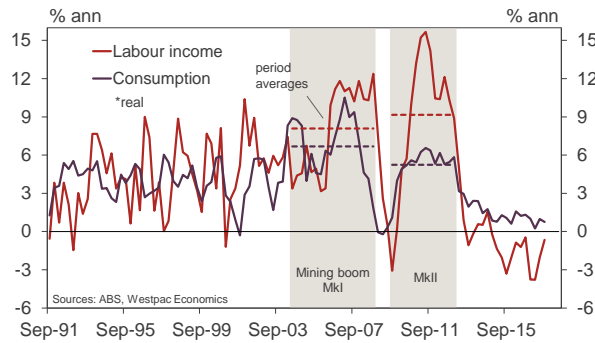


Chart 2.

WA wages growth

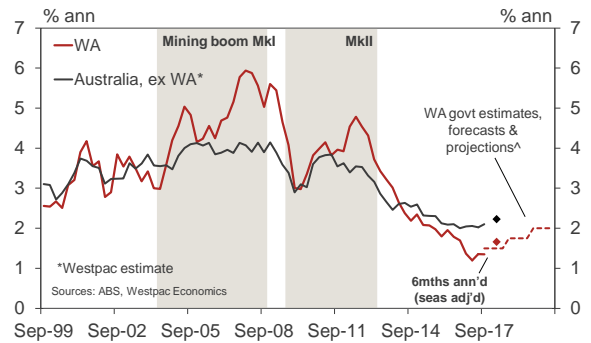


Chart 3.

New home building: yet to stabilise

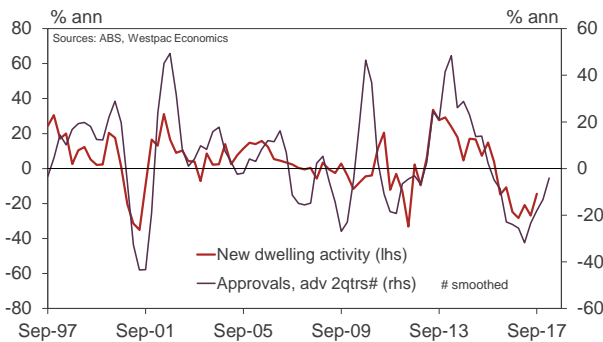


Chart 4.

House prices: Perth price declines moderate

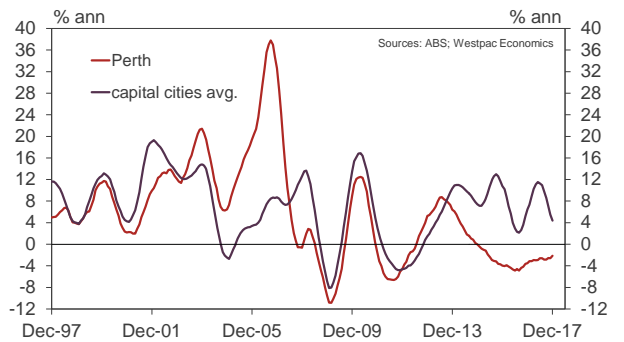


Chart 5.

WA business investment

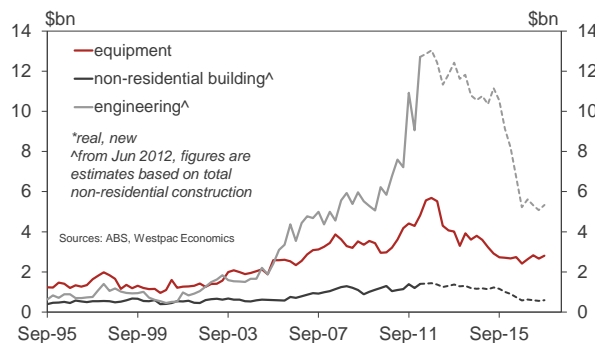
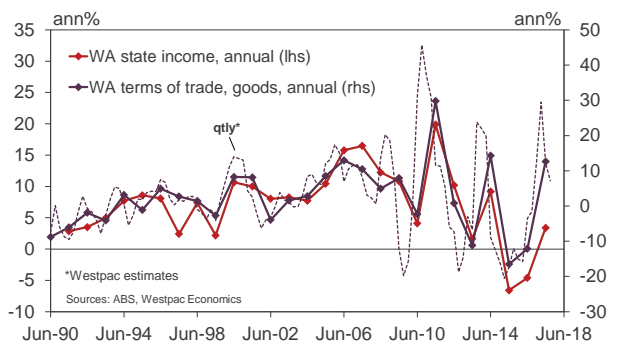


Chart 6.

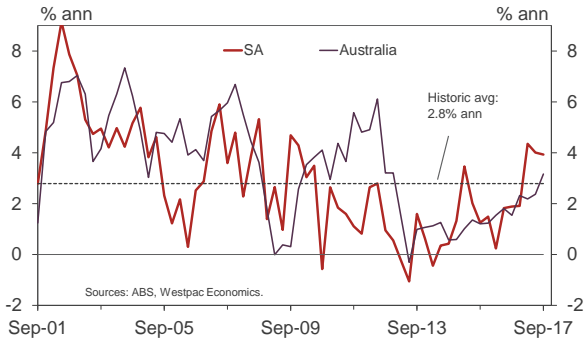
WA's terms of trade vs state income



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South Australia: jobs uptrend intact...

State final demand holding above average

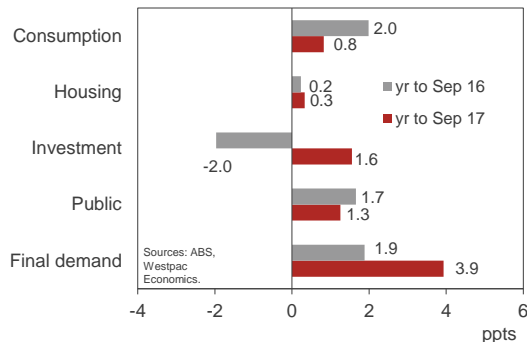


South Australian final demand has outperformed in 2017, led by the public sector's investment drive. At 3.9%, annual growth is more than three times the average of the five years to Q4 2016, and is also well ahead of the historic average of 2.8%.

As above, the public sector has been a key contributor to growth, adding 1.3ppts in the 12 months to September 2017 after contributing 1.7ppts in the prior 12 months. Private investment has also rebounded strongly in 2017, contributing 1.6ppts in the 12 months to September.

This surge in investment has been centred in the construction sector, including projects such as the Adelaide convention centre expansion. The issue is that a large portion of these projects are coming to an end. Notably in Q3, public investment fell 6.5% after rising 10.5% in the six months to June. The question is, where to next for SA?

SA contributions to state final demand

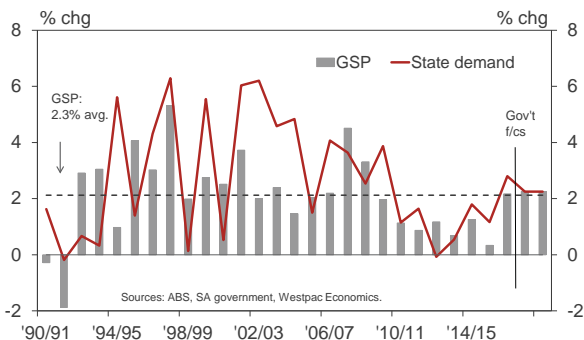


There is considerable work to be done on the engineering front, particularly for power and transport infrastructure. However, this pipeline alone won't offset the loss from construction. It will therefore be up to the household sector to drive growth.

In contrast to the south-east states of Victoria and NSW, Adelaide continues to experience weak population growth. But thankfully, since late-2015, there has been a marked improvement in job creation, supporting consumption. This has come despite the closure of automotive manufacturing firms, and while another historic contributor of jobs in the state, defence manufacturing, has been waiting for the next cycle of projects to begin.

The job opportunities available to the SA population are now much more likely to come in household services (education; health and retail) as well as service and agriculture-linked export industries. In both sectors, there is considerable long-term promise.

SA economic performance & outlook



The opportunity ahead of SA is certainly not guaranteed. While the employment to population ratio has risen 1ppt since its late-2015 low, it is still 2ppts below its 2008 peak. To foster sustainable robust activity growth, recent job gains need to persist.

Consumption is the most likely way that job gains will translate into demand. Currently, annual growth is only up 1.4%/yr after a volatile year. However, this does follow a particularly strong rebound in 2016.

A key positive for discretionary consumption in SA is that housing affordability has been kept in check. This may also mean that housing investment can be sustained better than in the south east, where a noticeable downtrend has taken hold. Currently, housing investment is up 7.4%/yr. Through the year, this growth has been primarily driven by an upswing in new construction as renovation work remained highly volatile and absent a clear trend.

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... aiding household demand

Chart 1.

South Australia: public investment strong

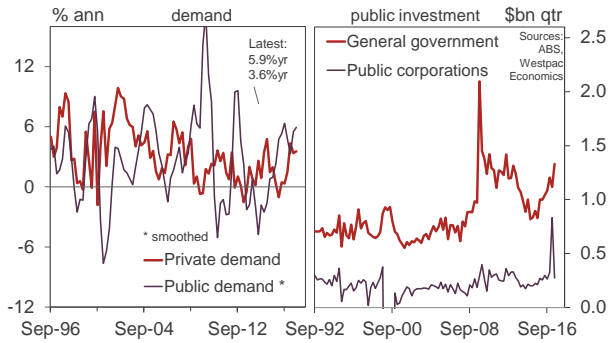


Chart 2.

Business investment: stable, outlook uncertain

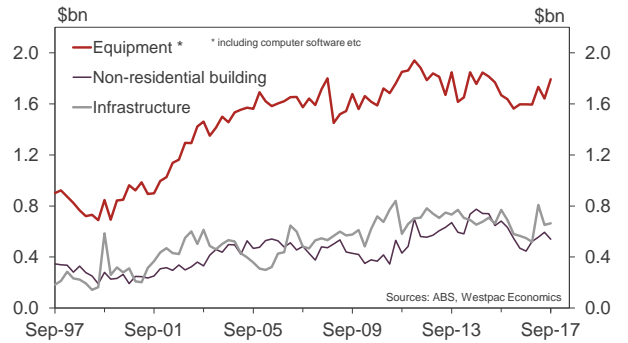


Chart 3.

Weak population growth a key concern

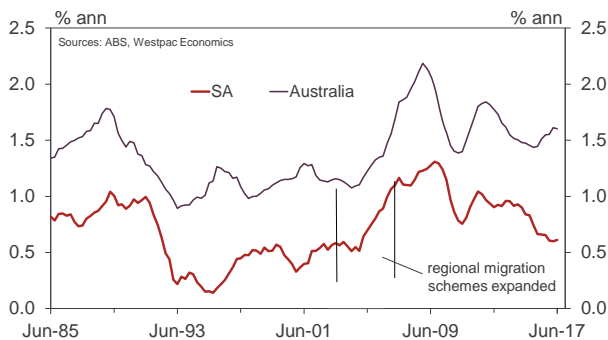


Chart 4.

SA job gains boost household demand

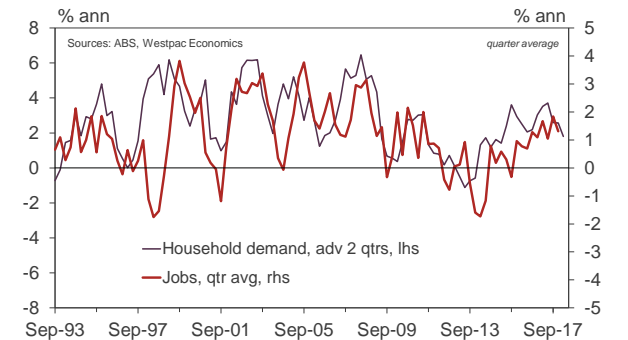


Chart 5.

Adelaide turning down with south east

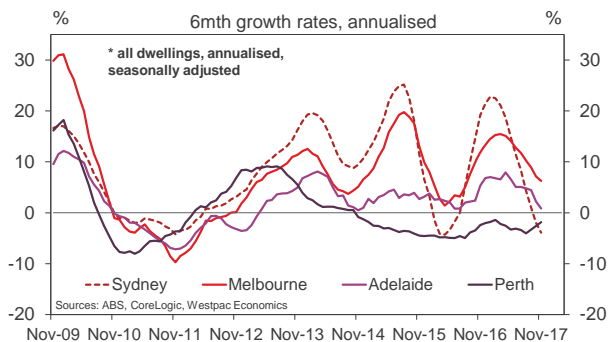
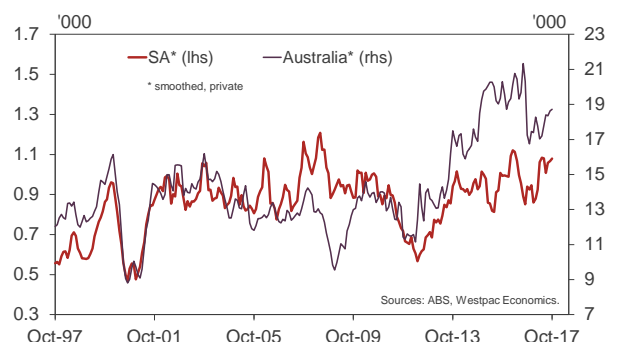


Chart 6.

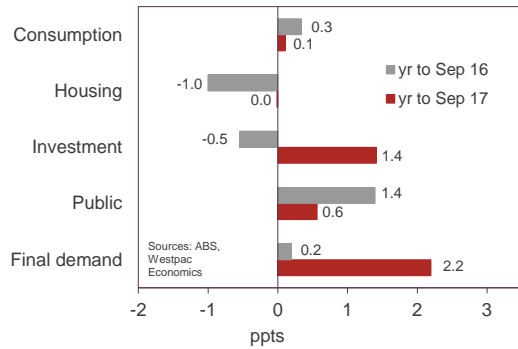
Dwelling approvals have lifted, but gains limited



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Tasmania: choppy conditions ...

Tasmania: contributions to state demand

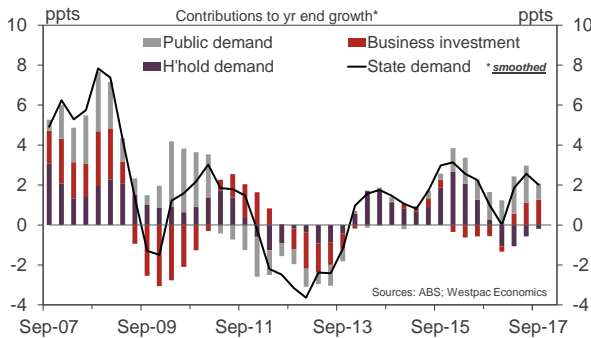


The Tasmanian economy turned in a mixed performance in the September quarter. State demand declined by 0.8% in the quarter, extending the choppy profile evident during 2016 and 2017 - being the 3rd fall in the past 7 quarters. Annual state demand growth is still a respectable 2.2%, in line with the long-run average for the state.

Consumer spending enjoyed a strong burst in 2015, increasing by a well above trend 3.6%. Since then, spending has consolidated, to be only 0.2% higher than a year ago. Household spending across the nation is lacklustre, constrained by weak wages growth and high debt levels.

However, the housing market is marching to a different beat to the rest of the nation. Hobart prices are rising, +10% annualised over the past half year. Dwelling approvals hit their low point around October 2016, subsequently rebounding by 46% - to still be 14% below the 2015 peak. This will see home building activity expand in 2018, in sharp contrast to the 16% decline in the year to mid-2017.

Tasmanian state demand

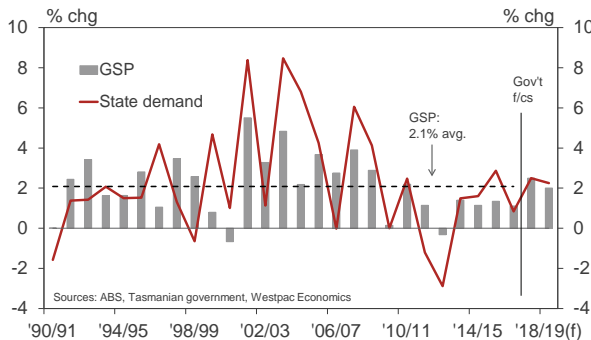


Population growth for Tasmania has rebounded gradually over recent years. It now stands at 0.6%/yr, which is the strongest pace since the start of 2011, but well below the national rate of 1.6%.

Associated with stronger population growth, the jobs market has been on a firmer footing in 2017, mirroring the national trend. Employment increased by around 3.0% over the past year, with the trend unemployment rate at 5.9%, well down from the 8.0% high of 2013.

Business investment and public demand are rising, making a sizeable contribution to growth. Together, they have added around 2ppts to annual activity, the largest contribution since 2008 (albeit well below the 5ppts in that period). Fiscal pressures have long since receded, providing the government with scope to boost investment from the lows of 2016. Business investment is being led higher by infrastructure projects and equipment spending.

Tasmanian economic performance & outlook



State output increased by 1.1% in 2016/17, meeting the state government's forecast. Output growth has been stuck at around 1.2% for the past four years. This is below the state's long run average of 2.1% and below the national pace over this period, of 2.4%.

The state government, in their May budget, was relatively positive about the outlook. State output growth was forecast to strengthen to an above trend 2.5% in 2017/18 and then be a solid 2.0% in 2018/19.

The view was that private activity would increasingly drive growth in 2017/18, centred on household spending and a return to growth in exports, with industries such as agriculture and tourism to outperform. The recent levelling out of consumer spending represents a clear downside risk. Prospects for a recovery in business investment, up from low levels, in response to improved economic conditions and at a time of greater business confidence has been an area of uncertainty, but risks appear to have diminished.

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... consumer spending levels out

Chart 1.

Tasmanian jobs market strengthens

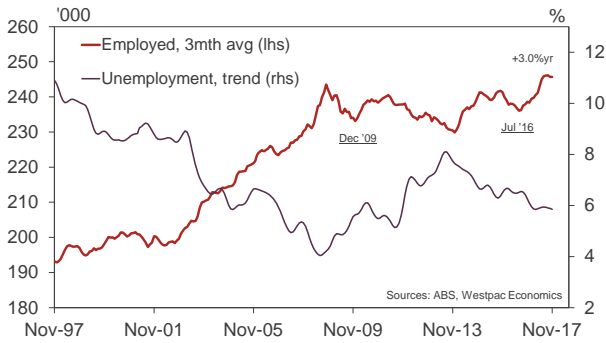


Chart 2.

Tasmanian population growth at 6 year high

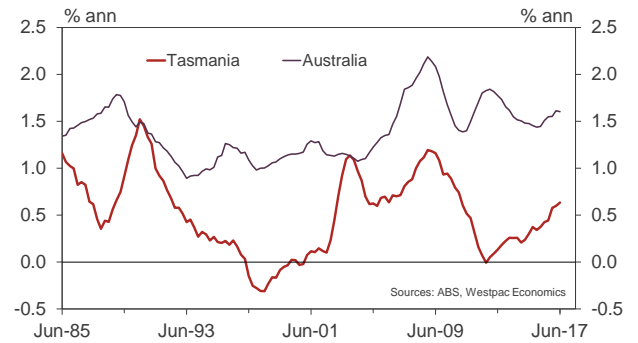


Chart 3.

House prices: Hobart market humming

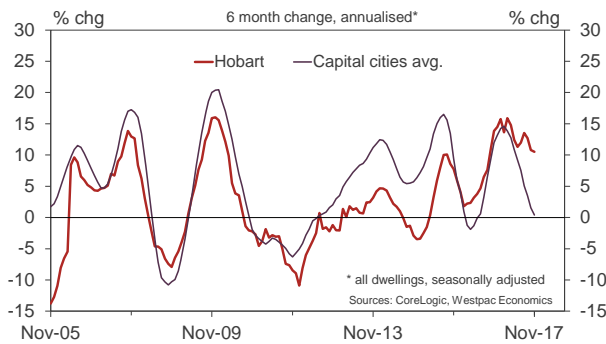


Chart 4.

New home building: rebounds

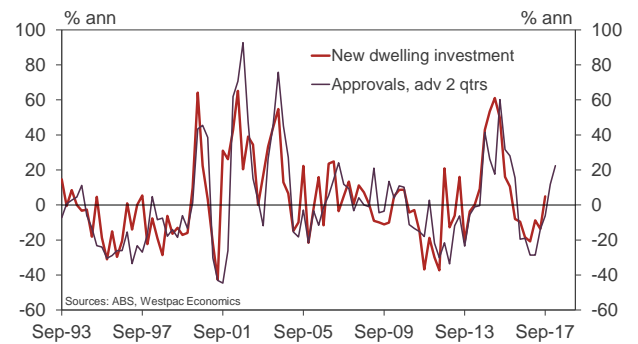


Chart 5.

Domestic demand accelerates

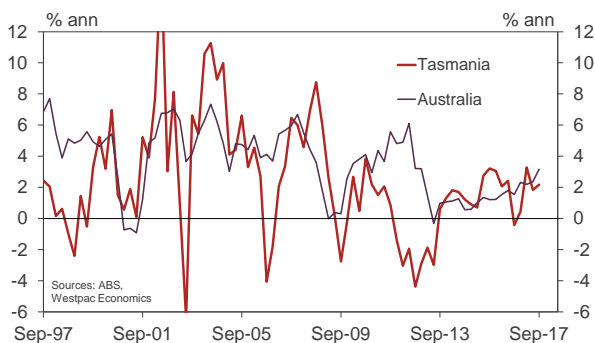
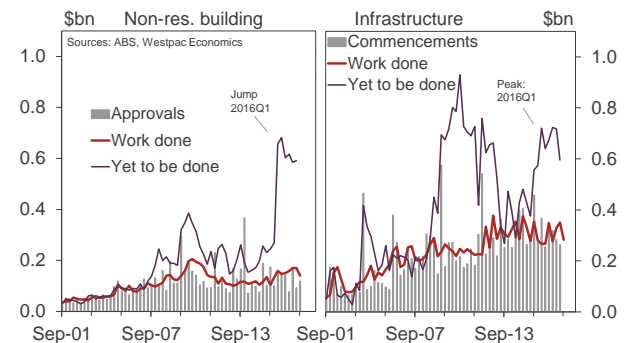


Chart 6.

Non-residential construction pipeline expands



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Summary indicators

Chart 1.

Exports of goods & services

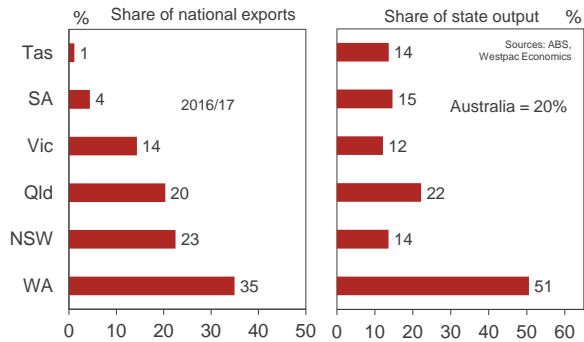


Chart 2.

Gross State Product

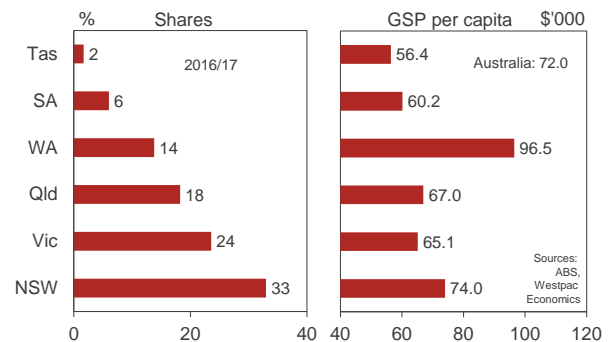


Chart 3.

Dwelling approvals

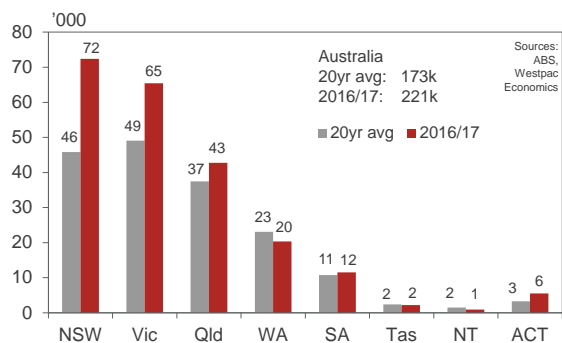
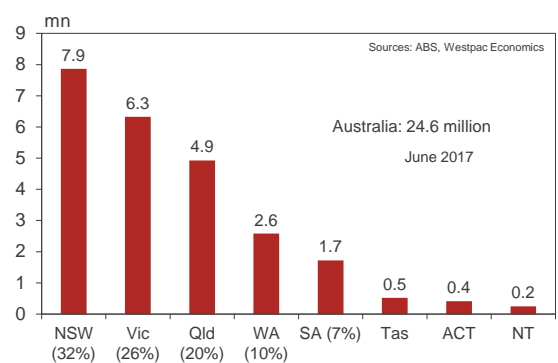


Chart 4.

Population



Industry mix: share of gross value add

	Australia	NSW	Vic	Qld	WA	SA	Tas	NT	ACT
Agriculture	3.0	2.0	2.7	3.6	3.0	6.4	10.2	3.1	0.1
Mining	6.3	1.9	0.8	6.8	26.3	3.8	3.7	13.5	0.1
Manufacturing	6.3	5.9	7.4	6.7	5.3	7.1	6.4	5.8	1.0
Construction	7.9	7.3	7.9	8.8	8.7	6.4	5.7	12.5	6.3
Transport, utilities	7.8	7.7	8.4	8.6	6.6	8.2	7.2	5.3	4.3
Wholesale, retail	9.3	9.4	10.6	9.3	7.4	10.7	8.7	5.6	4.7
Health, social assistance	7.6	6.6	7.9	8.2	6.0	10.0	13.3	7.3	11.9
Education	5.2	5.0	5.5	5.5	4.0	6.2	6.6	5.3	6.1
Household services	5.3	5.5	5.2	5.9	4.0	5.5	5.4	5.9	4.6
Finance	9.4	13.0	10.6	6.8	4.9	8.1	6.7	2.6	3.4
Business services	16.8	20.5	18.5	14.6	11.6	12.3	10.1	8.5	20.2
Public administration	5.9	5.0	5.1	6.1	4.5	6.0	6.7	13.9	29.3
Ownership of dwellings	9.3	10.2	9.3	9.1	7.8	9.4	9.1	10.7	8.1

Sources: ABS, Westpac Economics. For the 2016/17 financial year.

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Forecasts: state activity and employment

		2016/17	2017/18f		2018/19f	
			Govt f/cs	Westpac	Govt f/cs	Westpac
Australia *	GDP	2.0	2.8	2.7	2.8	2.5
	Employment	1.4	2.4	2.7	1.7	1.3
NSW	GSP	2.9	3.00	3.0	2.75	2.7
	Employment	1.0	2.50	2.7	1.75	1.5
Vic	GSP	3.3	3.00	3.0	2.75	2.7
	Employment	3.9	3.00	2.8	2.00	1.5
Qld	GSP	1.8	2.75	2.7	3.00	2.5
	Employment	0.0	2.25	3.5	1.50	1.2
WA	GSP	-2.7	2.50	2.4	3.00	2.5
	Employment	-0.8	2.00	2.2	1.50	1.2
SA	GSP	2.2	2.25	2.2	2.25	1.8
	Employment	1.3	1.00	1.2	1.00	0.6
Tasmania	GSP	1.1	2.50	2.2	2.00	1.8
	Employment	0.5	1.25	2.4	1.00	0.6

* Government forecasts for Australia are a weighted average of the state government forecasts. State government forecasts are from the most recent budget update. Westpac's state numbers are calculated to be consistent with the national forecasts.

Gross State Product

	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
NSW	2.0	2.6	2.5	2.0	2.0	2.8	3.9	2.9
Vic	1.6	2.9	1.8	1.1	2.0	2.9	3.5	3.3
Qld	1.4	0.6	5.5	2.8	2.2	1.2	2.6	1.8
WA	4.6	4.3	9.4	6.0	5.9	2.7	1.0	-2.7
SA	2.0	1.1	0.9	1.2	0.7	1.3	0.3	2.2
Tas	0.2	2.2	1.1	-0.3	1.4	1.1	1.3	1.1
Australia	2.1	2.5	3.9	2.6	2.6	2.4	2.8	2.0

Sources: ABS, Westpac Economics * GSP estimates are only on an annual basis. The 2016/17 update is to be released in late November.

Employment

	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
NSW	0.7	2.5	0.7	1.7	0.5	1.3	3.8	1.0
Vic	2.4	2.8	1.1	1.2	0.9	2.5	2.7	3.9
Qld	0.4	1.8	1.3	0.2	1.3	0.2	1.7	0.0
WA	0.0	3.4	4.0	3.1	-0.0	1.0	-0.5	-0.8
SA	0.6	1.5	0.5	0.1	-1.3	0.5	0.5	1.3
Tas	-1.4	1.3	-1.3	-1.0	-0.4	2.8	-0.2	0.5
Australia	1.0	2.4	1.2	1.3	0.6	1.3	2.3	1.4

Sources: ABS, Westpac Economics

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Notes

Notes

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