

Westpac Coast-to-Coast September 2018

An update on Australia's state economies

Westpac Institutional Bank

200



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Westpac Economics

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Australian economy

The June quarter GDP report was released recently. Due to upward revisions of around 0.5 percentage points, the Australian economy was revealed to be much stronger than we had been led to believe. Real GDP expanded by a solid 0.9% in the June quarter and annual growth printed 3.4%. Domestic demand also grew by 3.4%.

As discussed in this report, which dissects growth across the states, this national growth out performance was distributed across most of the states. With the exception of Western Australia, domestic demand expanded by 3.4% or better in each state. Peak growth was experienced in Victoria, at 5.2%, with NSW registering a very respectable 3.5%. There was broad based spending strength across the states with contributions from consumers; home building; business investment and, in particular, government infrastructure spending, where Victoria and NSW are standouts.

The accounts prompted a review of our growth outlook. We have lifted our growth forecasts: for 2018, from 2.7% to 3.3%; for 2019, from 2.5% to 2.7%; and the 2020 forecast has increased from 2.8% to 3.0%. While the levels of the growth forecasts have been lifted, the profile of an economy that will slow into 2019 and lift modestly in 2020 remains.

Our key themes shaping the outlook remain intact, around: house prices; home building; wages; political uncertainty; and global growth.

House prices in Sydney and Melbourne are now falling and this process is expected to persist through the remainder of 2018, 2019, and well into 2020. The adjustments will be shallow but persistent. That process will see consumption, which has been running at a pace slightly above household incomes, to drop below that pace. We also expect labour income growth to slow from 5% in 2017, to 4% in 2018, 3.6% in 2019, and drift back to 4% in 2020. Slower income growth, complemented by the expected wealth effect, should see consumer spending growth slow from 3% currently to 2.6% in 2019 and 2.8% in 2020.

While we have been surprised by the strength of the housing construction cycle a slowdown seems highly likely. Strong population growth will be insufficient to counter slowing foreign investment; credit tightening by the Australian banks; current increases in mortgage rates; and prospects of tax changes following next year's Federal election.

Political uncertainty looks set to weigh on firms' investment and employment intentions through the remainder of 2018 and 2019. These factors have played out clearly during the Federal election campaigns of 2013 and 2016.

We expect global growth to slow from 3.8% in 2017 to 3.5% in 2020, against the backdrop of international trade disruptions. That slowdown in global growth through 2019 and 2020 reflects China on a steady downswing (down to 6.0% growth in 2020); US slowing from mid-2019 (partly under the weight of persistent Fed tightening - US growth to slow to 1.7% in 2020); Japan responding badly to the introduction of a consumption tax in 2019 (growth slowing to 0.7% in 2020); European growth moderating back to trend as the ECB stops QE (back to 1.5% in 2020); and ongoing adjustments being required in those emerging markets that may be exposed to US interest rates, a strong US dollar, and higher oil prices.

The state break down of this expected slowdown will be difficult to accurately attribute. But some factors are apparent from our inspection of the state spending data.

The dominant weakness in the housing price and construction cycles is likely to centre on NSW and Victoria. The sustained migrant led population growth in Victoria (2.2% for the year) and NSW (1.4% for the year) might not slow too much but spending per capita is likely to moderate in both states as falling house prices; tighter credit conditions; and political uncertainty weigh on employment and confidence. On the other hand government spending by the states is likely to remain robust particularly as we are entering election periods for both Victoria (November 2018) and NSW (March 2019).

Conditions in the mining states are improving and they are not expected to experience anything like the reversals in the housing markets that we are seeing in NSW and Victoria. Nevertheless dwelling investment has contracted in Queensland while house prices continue to fall in Perth.

On wages, evidence from the US and UK, which have flexible labour markets, has been that despite the unemployment rate falling well below previous estimates of full employment wages growth has remained benign. The states will provide an interesting test case of whether similar results can be expected in Australia. In the case of the boom state of Victoria, the unemployment rate has now fallen below 5% to 4.8% and wages growth has lifted a little above the national average but still remains benign. With the momentum in overall activity set to moderate, the risk is that wages growth continues to disappoint.

Overall our revised growth forecasts for national growth do not change our forecasts for monetary policy. We still expect the RBA cash rate to remain on hold through to the end of our forecast horizon, which extends to December 2020.

The key here is that following a 2.4% growth rate in 2017, the economy will only register a single above potential growth performance before slowing back to slightly below potential in 2019 with a modest above potential lift in 2020. There is unlikely to be much sustained progress in closing the output gap and delivering higher wage and price inflation outcomes.

Bill Evans, Chief Economist

Australian economic outlook

Chart 1.

Domestic demand: year-end contributions

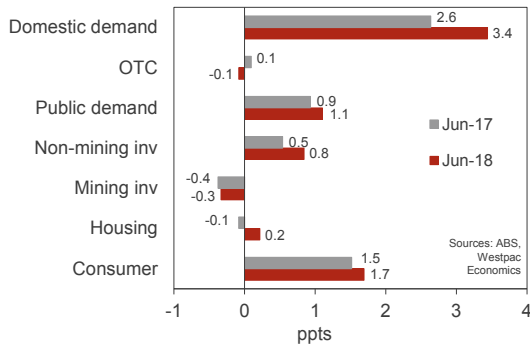


Chart 2.

Output growth lifts to 6 year high, 3.4%

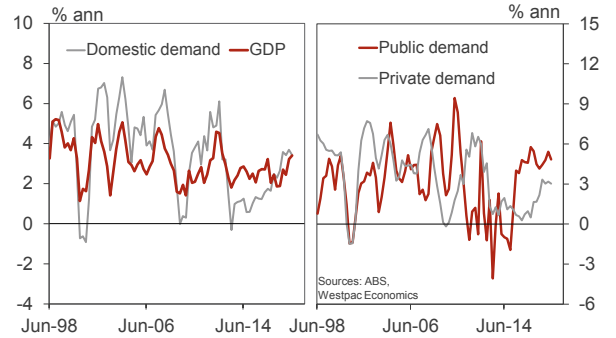


Chart 3.

Australia: the growth mix

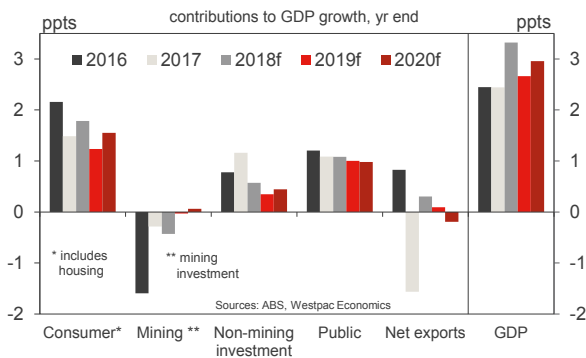


Chart 4.

Australia: growth still expected to moderate

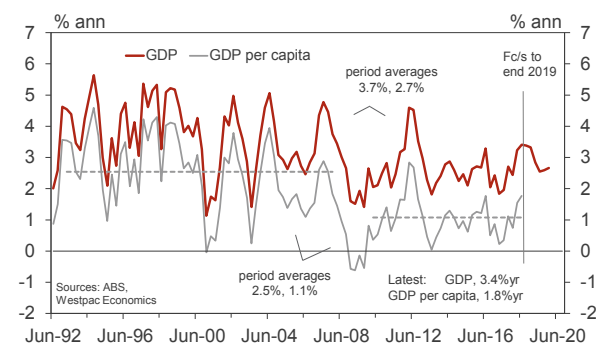


Chart 5.

Nominal wages growth: off lows but still weak

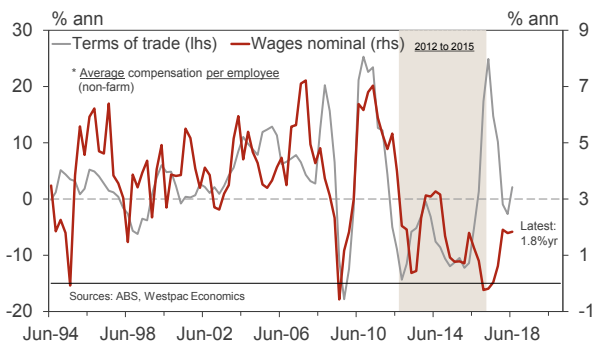
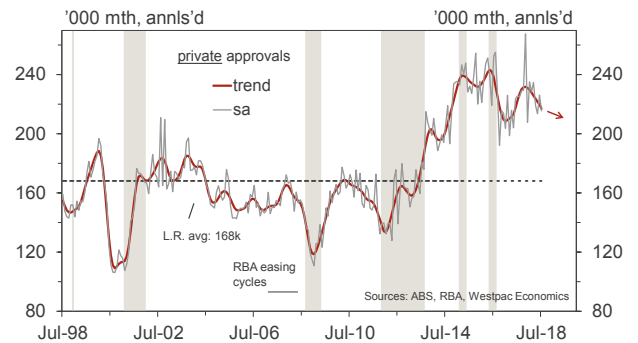


Chart 6.

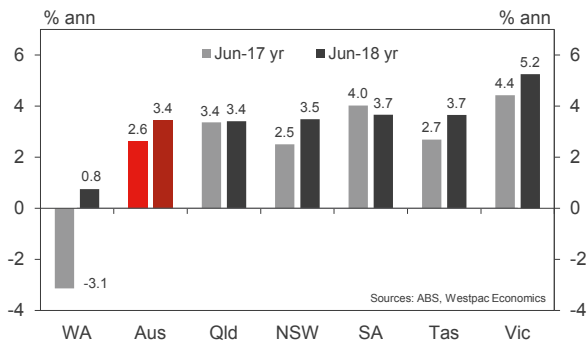
Dwelling approvals: downtrend to resume



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States overview

Domestic final demand



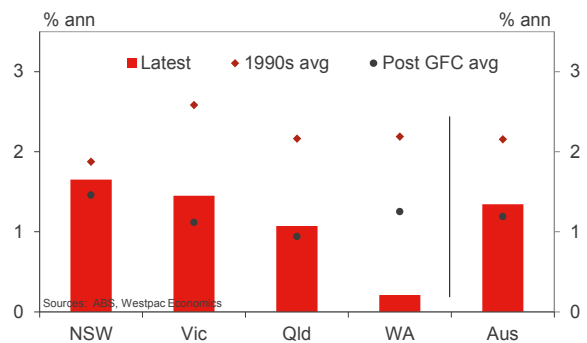
In the June quarter, nationally domestic demand grew by 0.6% to be 3.4% above the level of a year ago. It is striking that annual domestic demand growth is 3.4% or more in each of the states, with the exception of WA, where activity expanded by a more modest 0.8% - a turnaround from a contraction of 3.1% over the previous year

The economy gained momentum over the past year - a development nationally that was mirrored in NSW and Victoria, as well as in WA and Tasmania.

Victoria, currently experiencing a population boom, is the standout economy, with state demand growth in excess of 5% - the strongest pace for the state since 2010 and before that 2007/08, ahead of the GFC.

Broad based spending strength, across consumers, home building, business investment and government is evident in both Victoria and NSW. Strength is also reasonably broadly based in South Australia and Tasmania.

Consumer spending, per capita

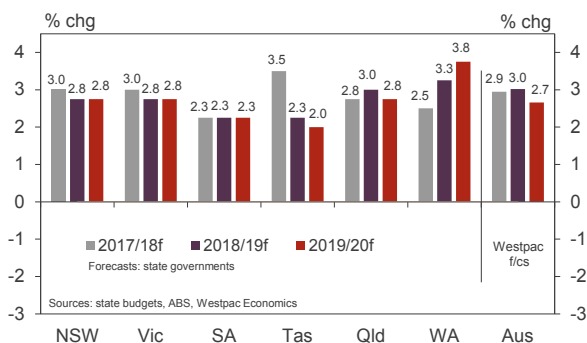


In the mining states of Qld and WA, new home building activity is either still falling (as in Qld) or is stabilising at historic lows (in WA). Looking ahead, home building activity is set to weaken in NSW (near-term) and in Victoria (more a 2019 development).

Government spending, in the form of public demand, is expanding at a brisk pace, led by health and investment in public infrastructure. Nationally, growth is 5%, a pace evident in NSW and Qld, while Victoria is in excess of 8% as the state counts down to the November 24 state election.

Consumer spending per capita is running at 1.3% annual growth nationally, in line with the post GFC average of 1.2% but still well below the 1990s average of 2.2%. This broad pattern is evident across most states, with spending per capita particularly weak in WA. While jobs growth has generally been robust, real wages growth is weak and house prices are falling in key markets, constraining consumer spending.

Growth outlook by state: GSP



The economic outlook is robust in the view of the states. The weighted average of the state budget forecasts points to growth nationally at 2.9% for 2017/18 and then little changed at 2.8% for both 2018/19 and 2019/20. Westpac Economics anticipates growth at a similar pace, with the risks as we move into 2019 tilted to the downside.

The states are less upbeat than the RBA and Federal Treasury, who expect growth nationally of 3%, 3% plus.

Victoria and NSW both assess that real output growth was above trend in 2017/18, at 3.0%, and both anticipate a moderation to 2.75% in 2018/19 and in 2019/20. The cooling of the housing sector will weigh on the outlook. We concur.

WA expects output to rebound in 2017/18, +2.5%, after a 2.7% fall in 2016/17, and to then strengthen to 3.25% in 2018/19 - on an emerging stabilisation in demand and a lift in LNG exports. Qld expects growth to improve to 3.0% in 2018/19 and then moderate to 2.75% in 2019/20.

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States overview

Chart 1.

State jobs markets: above par gains in 2018

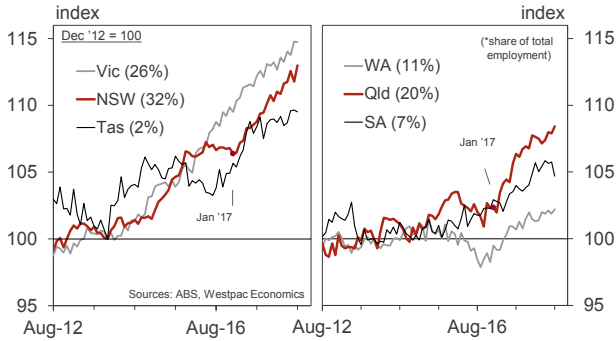


Chart 2.

State final demand, contributions

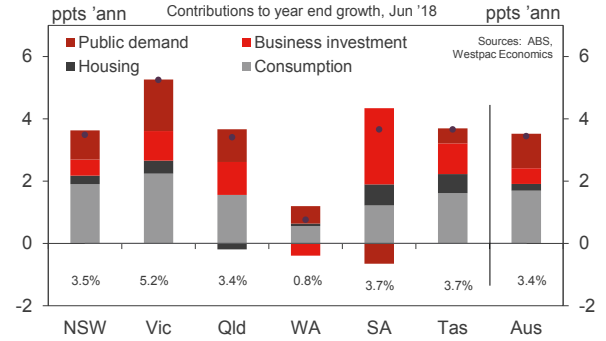


Chart 3.

Dwelling prices: housing markets cool

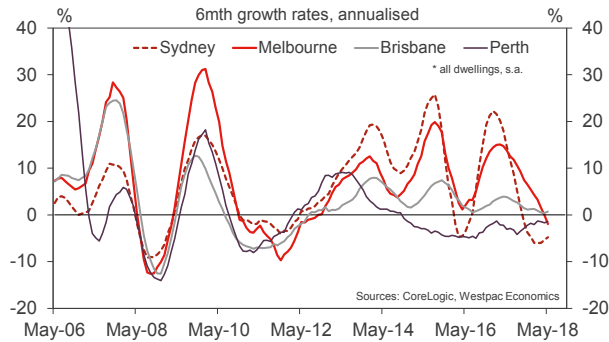


Chart 4.

Dwelling approvals by state

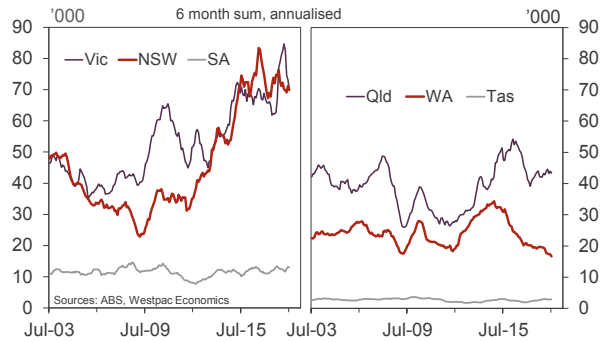


Chart 5.

Strong population growth: 1.6% nationally

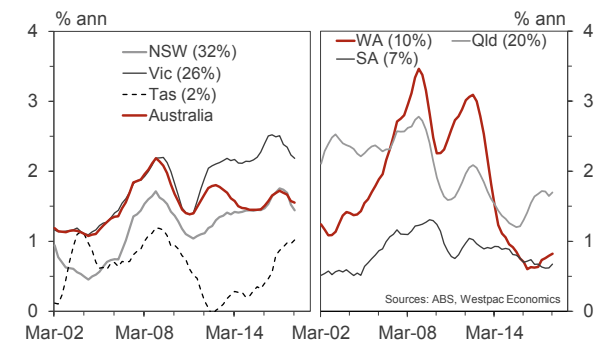
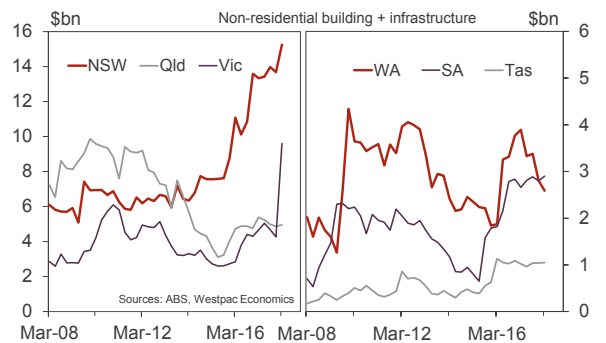


Chart 6.

Public construction work pipeline: surging



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Employment and activity: by state

Chart 1.

NSW: jobs & household demand

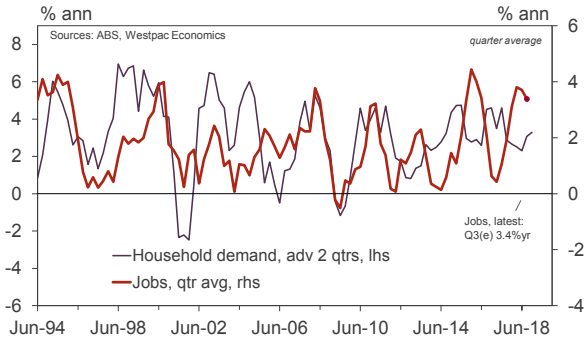


Chart 2.

Victoria: jobs & household demand

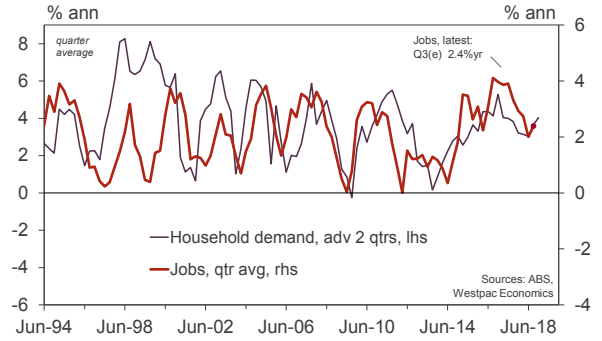


Chart 3.

Qld: jobs & household demand

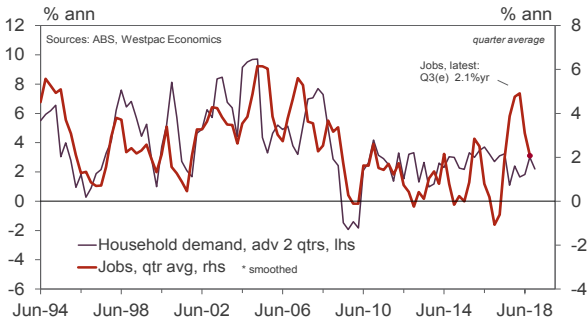


Chart 4.

WA: jobs & household demand

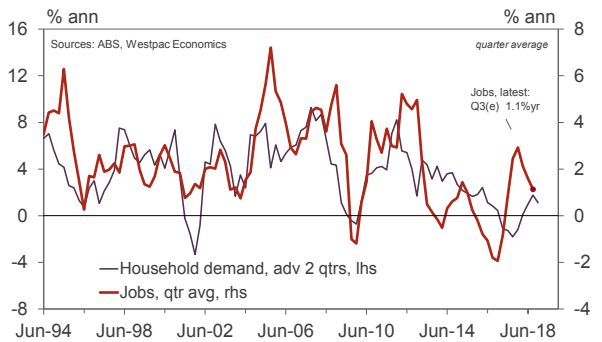


Chart 5.

SA: jobs & household demand

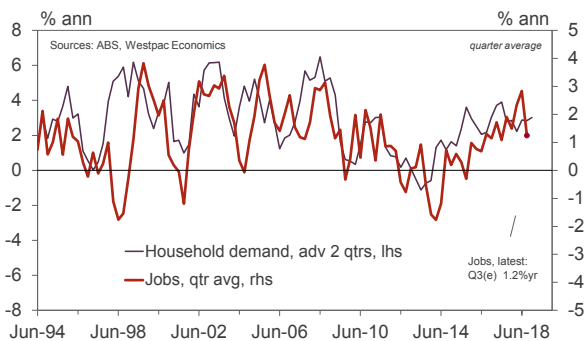
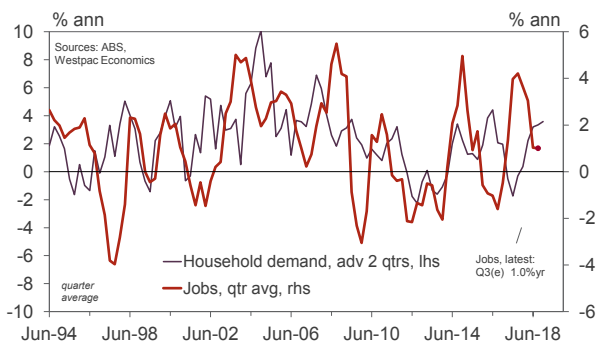


Chart 6.

Tasmania: jobs & household demand



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Employment by industry: NSW & Victoria

The labour markets of NSW and Victoria have experienced robust employment gains during 2017 and 2018, consistent with buoyant economic conditions.

In NSW, employment surged 3.7% in 2017, in part a catch-up following a gain of only 0.3% in 2016. For the year to date in 2018, employment has increased by 3% annualised.

The upswing in construction activity - including public transport infrastructure projects - is generating jobs in the sector, as well as having positive spill-over effects to other sectors. Employment strength over the past year is evident across construction, manufacturing, and financial services - both of which have emerged from a round of cost cutting during 2017. The health sector, which has been a key engine of jobs growth in recent years, has consolidated of late.

Victoria is experiencing a population boom and well above trend domestic demand growth. The labour market has performed well in this environment.

Employment in Victoria increased by 2.8% in 2017, bringing the cumulative increase for the four years 2014 to 2017 to an impressive 13%. So far in 2018, employment has expanded at a 2.3% annualised pace.

Once again, a strong upswing in construction activity, including public infrastructure, is a key jobs generator. Employment in the sector has reportedly leapt by 23% since the end of 2016. An uptrend in employment is also evident in professional & business services, public administration, as well as hospitality and arts & recreational services. However, retail remains patchy and employment in the sector has weakened of late.

Chart 1.

NSW: employment by sector

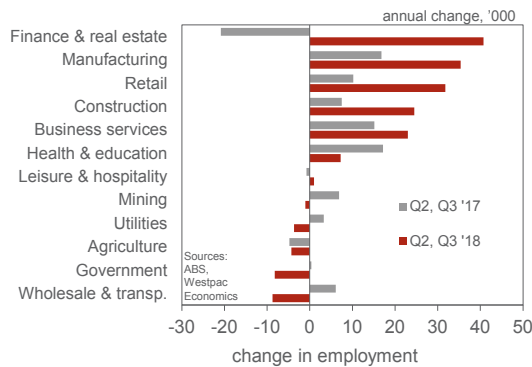


Chart 2.

Victoria: employment by sector

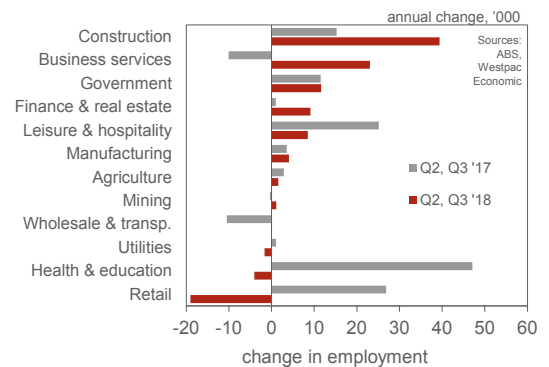


Chart 3.

NSW employment by sector

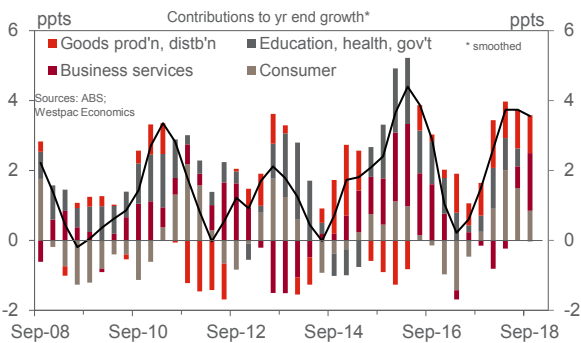
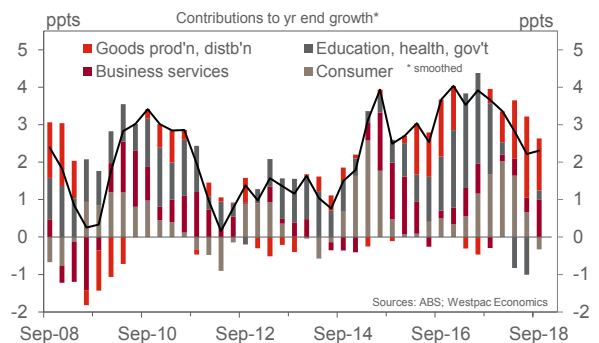


Chart 4.

Victoria employment by sector



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Employment by industry: Qld & WA

In 2016, Qld and WA felt the impact of a wave of cost-cutting in the mining sector after commodity prices slumped to historic lows. However, as commodity prices rebounded it became clear that cost cutting was overdone.

In Qld, employment rebounded by a sharp 4.4% in 2017, more than correcting for a 1% contraction in 2016. Employment levels have expanded further in 2018, increasing at a 2.3% annualised pace.

Mining sector employment levels have rebounded partially in 2018, with coal prices surprising to the high side. Construction employment is well up from the lows of 2015, albeit consolidating of late. The manufacturing sector has experienced a burst of jobs growth, as evident in NSW. Professional & business services has rebounded in 2018, following cost cutting in 2017.

In Western Australia, employment levels were cut sharply in 2016, contracting by 2.3%. That followed three years of broadly flat employment as the mining investment boom peaked in 2012.

As in Qld, the 2017 year saw a rebound, with employment up a brisk 3.8%. However, the follow through in 2018 has been less impressive, with jobs growth running at only 0.3% annualised - which is the weakest of the states.

Construction sector employment is trending lower in WA - in contrast to the eastern states - as work on the major projects winds-down. Retail employment has moved lower, with consumer spending soft in WA, so too jobs in the finance sector. By contrast, public administration staffing levels have rebounded from cost cutting with higher commodity prices providing some relief to tax collections.

Chart 1.

Queensland: employment by sector

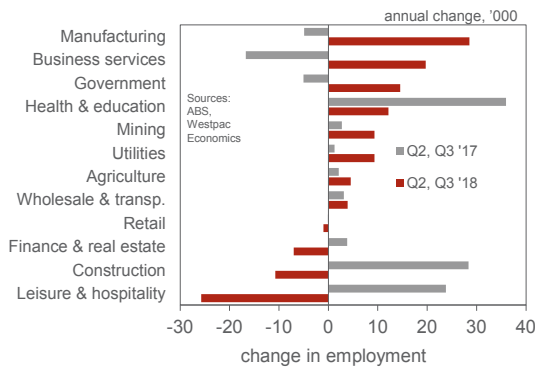


Chart 2.

Western Australia: employment by sector



Chart 3.

Qld employment by sector

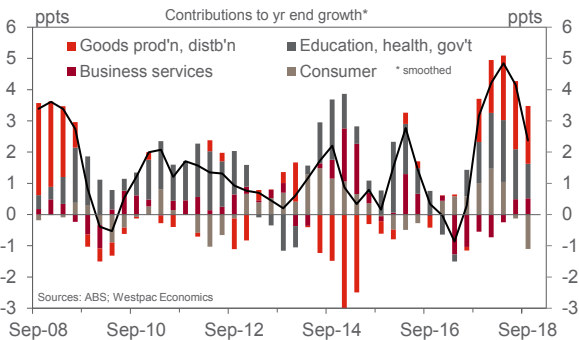
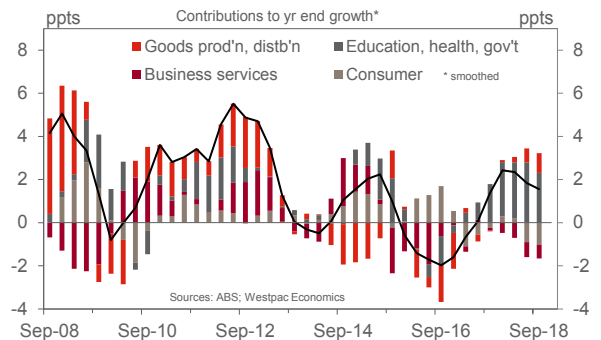


Chart 4.

WA employment by sector



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Employment by industry: SA & Tasmania

From 2016, South Australia's labour market emerged from a period of stagnation. Employment levels had moved broadly sideways through the five years 2011 to 2015, impacted by structural headwinds.

In 2017, employment grew by a robust 1.7% in the state, building upon a 1.0% gain in 2016. The uptrend had continued into 2018, with jobs growth 1.0% annualised.

Construction, as in most states (except WA), is a key jobs generator, with employment levels kicking higher in 2018. The hospitality sector is performing well, with the lower dollar boosting visitor numbers. Public administration staffing numbers have also moved higher. The manufacturing sector may be beginning to stabilise, with employment levels moving sideways in 2018. However, health employment levels have slipped after strong gains.

Tasmania's labour market appears to run 'hot and cold', as suggested by the official jobs data - although we caution about potential measurement errors for a small economy.

The state experienced a hiring burst in 2017, with employment levels increasing by 3.8%, the strongest performance since a 5.6% jump in 2014. The 2018 year has seen employment increase at a 0.8% annualised pace, not greatly different from population growth.

Construction sector employment levels continue their uptrend, albeit with some volatility. Hospitality employment levels have moved higher in 2018, again the lower AUD is boosting visitor numbers. Gains are also evident in real estate, as the housing market performs well, and in business services. However, the health sector has consolidated and farm employment levels have weakened.

Chart 1.

South Australia: employment by sector

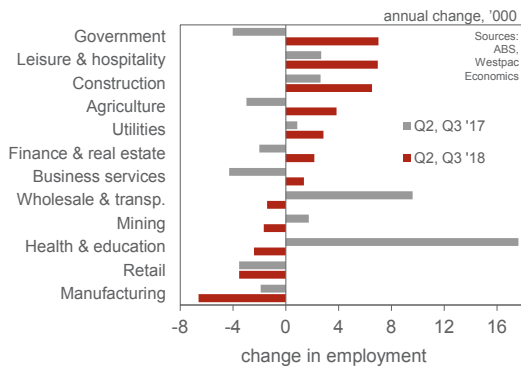


Chart 2.

Tasmania: employment by sector

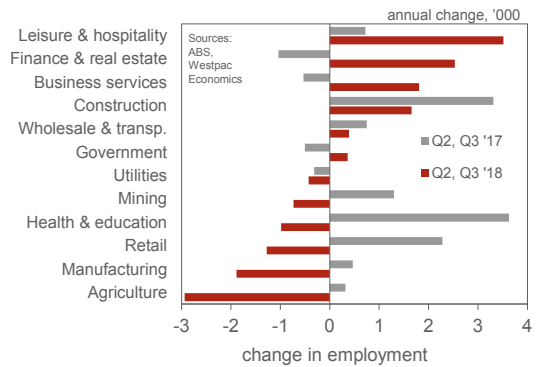


Chart 3.

South Australia employment by sector

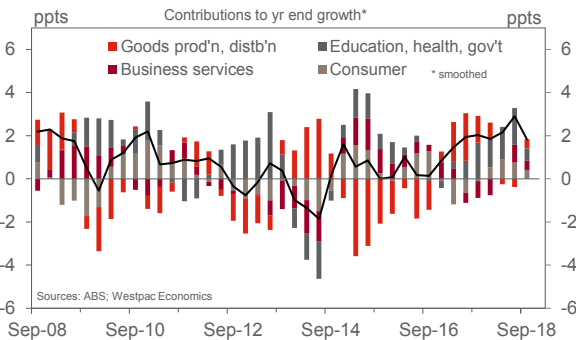
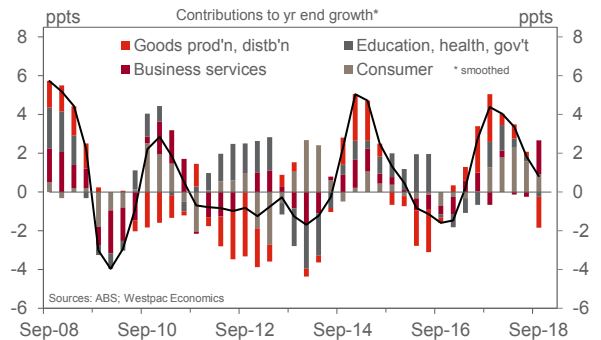


Chart 4.

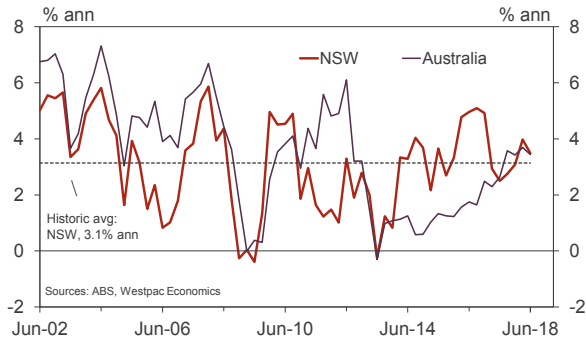
Tasmania employment by sector



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NSW: robust conditions ...

NSW state final demand: above trend growth



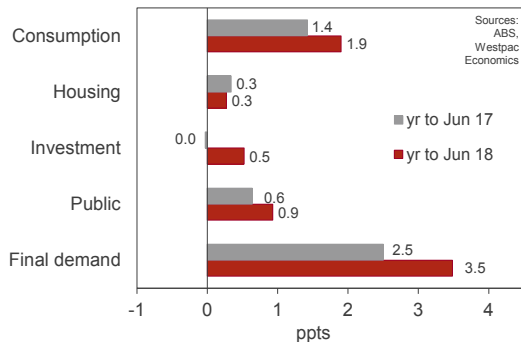
NSW is experiencing a period of robust economic conditions. Arguably, this suggests that the economy is relatively well placed to meet the challenges ahead, notably a cooling housing market.

Strong population growth, rising business investment, expansionary fiscal policy, a low dollar and a positive global backdrop are all positives. These tailwinds will act to offset the emerging slowdown in housing.

Over the past year, state domestic demand grew by an above trend 3.5%, in line with the national figure of 3.4%. Indeed, the past five years has been a period of sustained strength for the NSW economy, with annual state demand growth averaging 3.6%.

Spending strength during the past year was broadly based: consumer spending, 3.2%; home building, 4.3%; business investment, 4.8%; and public demand, 4.4%.

NSW: contributions to state final demand



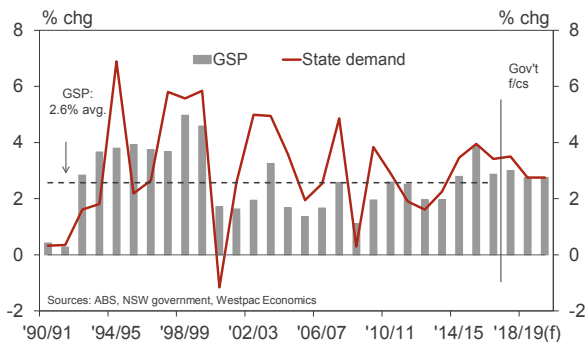
NSW population growth remains above trend, with Sydney (like Melbourne) attracting high levels of overseas migration. This is adding to the need to expand investment, by government and businesses, as well as housing.

Government spending, in the form of public demand, is particularly expansionary, increasing by 4.4% over the year and averaging 4.5% for the past four years. Stronger tax revenues and more efficient use of balance sheets has given governments the scope to lift spending.

The upswing in public investment has considerable further upside. Governments are playing catch-up and the need for additional transport infrastructure in our key capital cities is substantial - and the state government is responding by continuing to add new projects to the investment pipeline.

Home building activity, up strongly over the first half of 2018, is set to moderate. Residential property prices have eased after a strong run and have yet to form a base.

NSW economic performance & outlook



The slowing housing market has the potential to weigh on consumer sentiment. This development, along with weak wages growth, will act to constrain consumer spending. Having said that, employment growth remains supportive, at 3.7% in 2017 and running at a 3.1% annualised pace over the initial 8 months of 2018.

In the 2017/18 financial year, state demand grew by 3.3%, falling a little short of the budget forecast of 3.75%. Net international exports were a drag in the year but interstate trade was likely a positive.

The state government anticipates that output growth will moderate a notch to 2¾% in 2018/19 and 2019/20, from an estimated 3.0% in 2017/18. Housing and constrained household consumption are headwinds. Growth drivers are expected to rotate towards business investment and more broad-based strength in exports. We are broadly in agreement with this assessment, and note a lower Aussie dollar would provide a further fillip to the export sector.

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... but housing in a slowdown

Chart 1.

NSW: population growth above par, but off highs

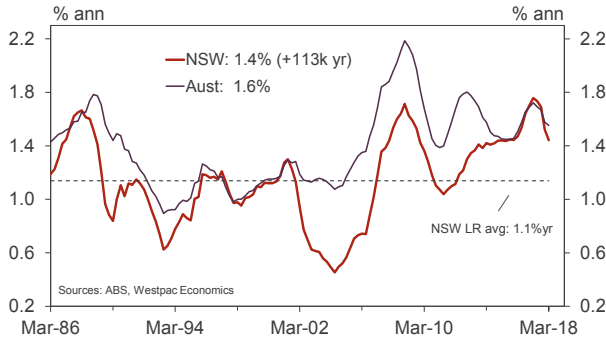


Chart 2.

NSW consumer spending

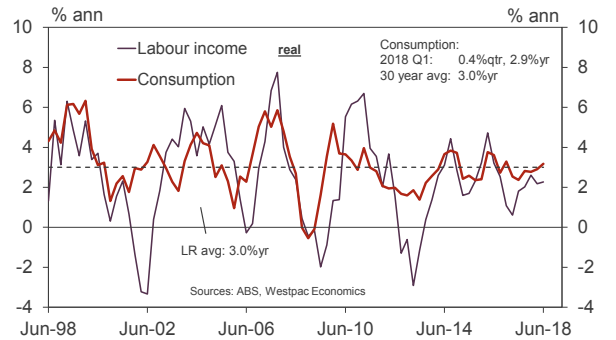


Chart 3.

NSW home building activity set to moderate

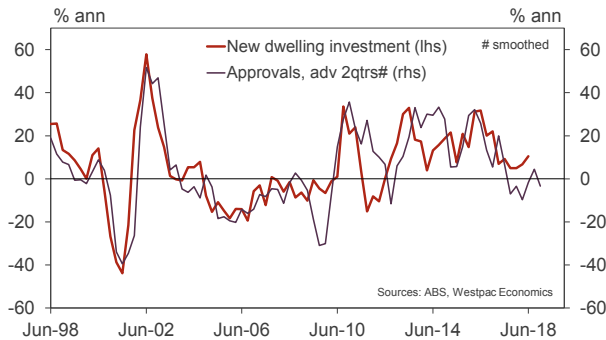


Chart 4.

Dwelling prices: housing markets cool

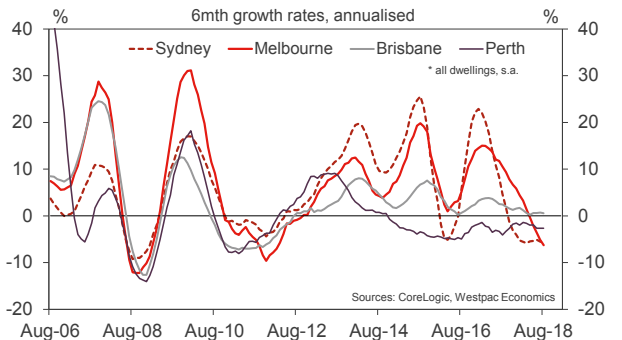


Chart 5.

NSW public investment: budget forecasts

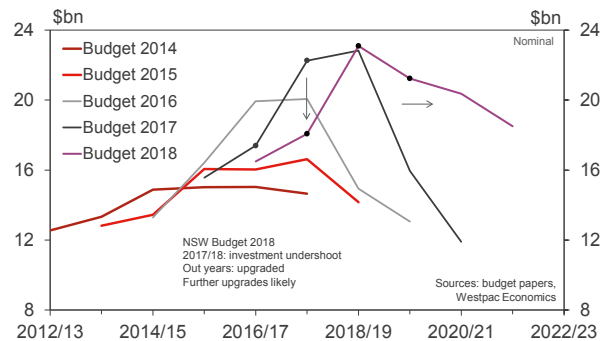
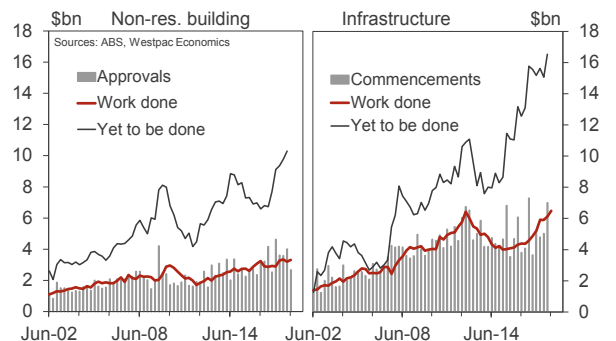


Chart 6.

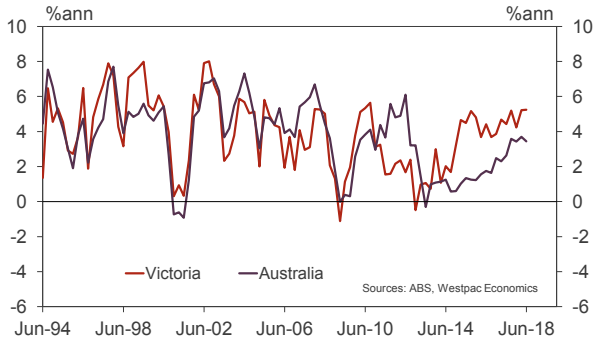
Non-residential construction boom



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Victoria: powerhouse expansion continues ...

Victorian state demand: well above trend growth

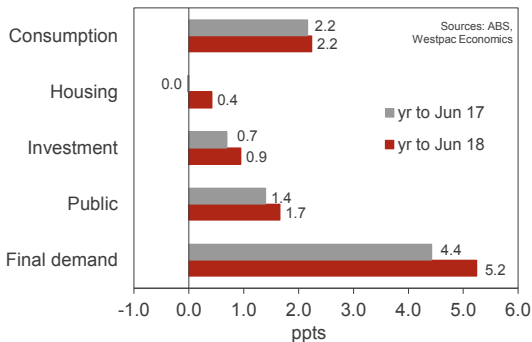


After a powerhouse four year expansion, the Victorian state economy is looking a little shakier with Melbourne's housing market entering a price correction. However, other indicators remain positive with a large pipeline of building and infrastructure projects set to keep growth tracking at a robust pace.

A sustained migration-led surge in population continues to be the main underlying driver, the expansion centred on Vic's education and services sectors but with associated pressures on capacity indirectly driving investment across a range of other areas.

Vic GSP growth outstripped national growth by 0.7ppts over the four years to 2016-17 (only annual figures are available). The latest quarterly data shows growth in state demand remained strong in the first half of 2018 with a 1.2% gain in Q1 and a 2.5% jump in Q1. Annual growth now stands at 5.2%, well ahead of national domestic demand growth of 3.4%yr.

Vic: contributions to state final demand

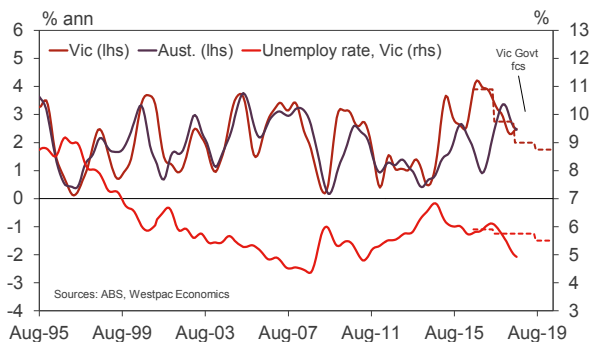


Vic consumer spending growth continues to track above trend – 3.8%yr versus a historic average of 3.3%yr – although much of this reflects stronger population growth with per capita gains in both spending and income less impressive. The price correction underway in Melbourne's housing market is likely to restrain demand near term.

New housing construction continues to hold up better than expected, with rapid growth in Q2 (7.4%qtr, 15%yr). Some of this reflects several very large inner city developments coming through although there has also been surprising underlying strength to dwelling approvals in 2018. Renovation work has weakened, falling -12%yr. While the housing cycle has turned, residential building should remain reasonably supportive near term.

Business investment is also outperforming. Both infrastructure and non-residential building up strongly (14%yr and 12%yr respectively) with project pipelines looking very healthy. Equipment investment has also risen 6.1% in the past 12 months.

Vic labour market



Public demand is running well ahead of the national pace, recording 8.1%yr growth compared to 4.8%yr for Australia overall. Investment is driving the gains, with construction and infrastructure work up 13% over the past year, and 50% since June 2015. Again, the forward view is very positive with the Melbourne Metro Rail and West Gate Tunnel driving a big jump in the infrastructure pipeline in Q2.

Employment growth has tracked in line with the solid gains nationally, a somewhat slower pace compared to the spectacular 4%+ surge in 2016. Despite this, Victoria's labour market has shown a material tightening over the last year, the unemployment rate falling to 4.8% and underemployment also showing a notable decline.

Wages growth has also shown tentative signs of lifting in Vic as well. Indeed, the extent to which Vic wages growth lifts in coming quarters is shaping up as a key test of how the wider Australian labour market is functioning and how entrenched low wages growth may be nationally.

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... despite housing market correction

Chart 1.

Vic household income & spending well balanced



Chart 2.

Melbourne house prices

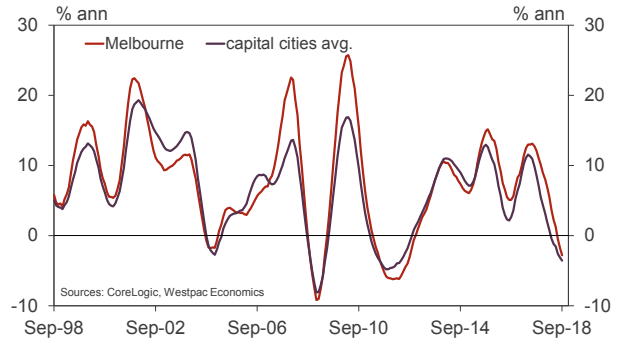


Chart 3.

Vic housing construction downturn delayed

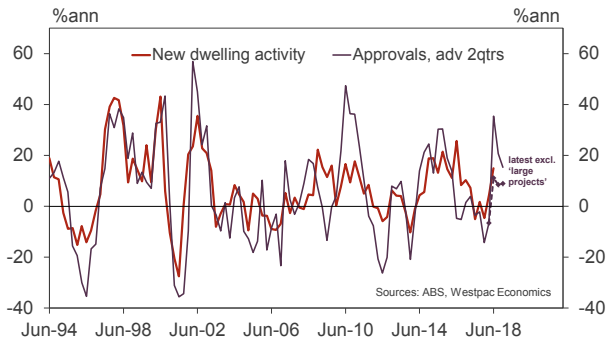


Chart 4.

Vic's non-res construction pipeline soars

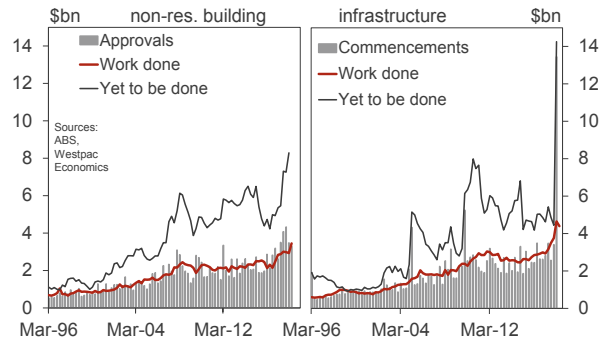


Chart 5.

Vic population growth: 2.2%yr currently

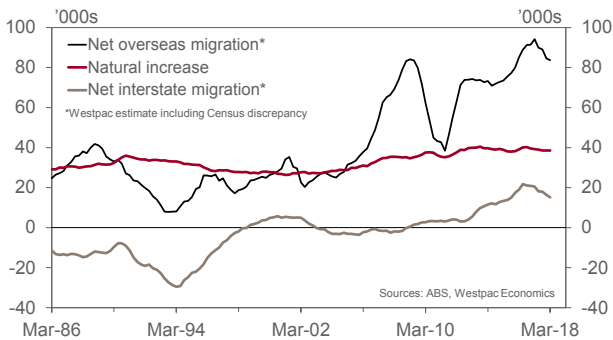
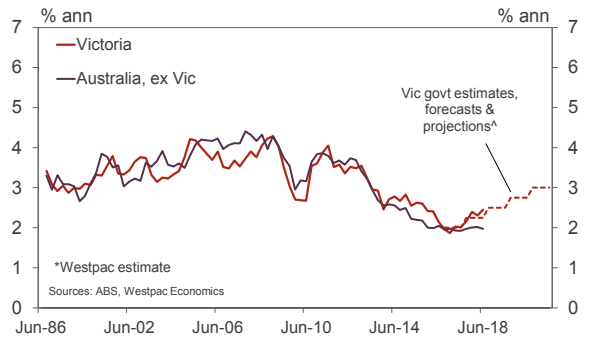


Chart 6.

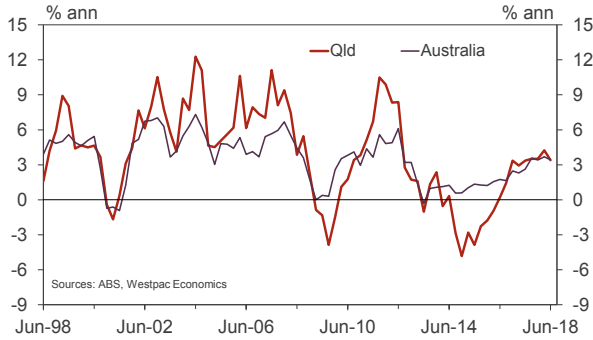
Vic wages growth



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Queensland: economy remains upbeat...

Qld domestic demand has rebounded

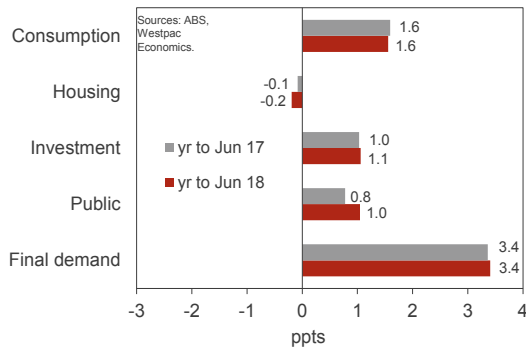


Though Queensland state demand growth stalled in Q2, growth in the year to June remains robust at 3.4%. This marks back-to-back strong financial years of growth, a stark turnaround from the stagnation/contraction in the years prior during the post mining boom transition. Both private demand and public demand are seeing growth, up 3.1% and 4.5% in annual terms.

Critical to reinforcing the state's resurgence in growth is the uplift in net interstate migration. Housing affordability is a key factor in attracting population movement up the east coast from the more expensive cities.

Businesses are meeting the higher demand from population growth with increased hiring as well as more recently, a recovery in physical investment. The exporting sector is also on a solid footing with demand for tourism and education services supported by the cheaper Australian dollar. Gas exports are also on the rise as new facilities come on stream.

Qld: contributions to state final demand

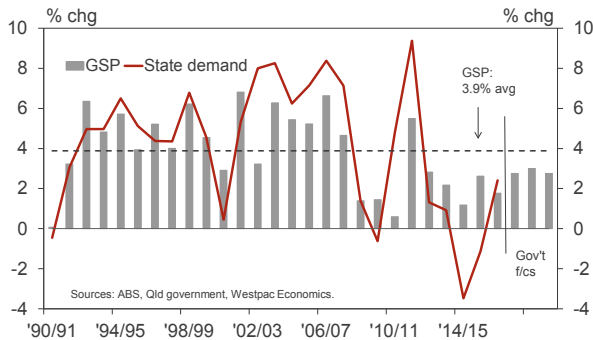


Business investment is recovering, up 8.0%yr driven by an increase in engineering construction and new equipment. Dwelling investment has softened from its peak but is still above average approvals pipeline and continued population growth suggests a solid outlook for residential construction. Given the degree of apartment oversupply in the Brisbane market, construction will be more dispersed in the period ahead.

Public investment has been moderate of late but a considerable spending package was hallmarked in the State Budget. Going forward, \$46bn in infrastructure spending is planned for the four financial years to 2021/22. 2018/19 is set to see \$11.6bn of spending with early works on the Cross River Rail already under way.

Public consumption, as with the nation in aggregate, has been a key driver of growth as demand for health services continues to increase. In the year to June, Queensland public consumption rose by 5.5%.

Qld economic performance & outlook



A healthy Queensland labour market has accommodated the lift in population with annual trend employment growth tracking at 2.3%yr, ahead of population growth of 1.7%yr. In addition, it appears that the post mining boom compositional shift in employment that had been weighing on incomes has abated. Together, that's seen consumption growth hold up at 2.8%yr, around a trend pace.

Looking forward, there are some uncertainties for the consumer particularly given that house price growth remains subdued amidst the roll-out of tightening credit conditions. That combined with some political uncertainty at the Federal level has seen consumer confidence in Queensland pull back to an even greater extent than the national aggregate. Accordingly, business confidence too has eased back to average levels. With the consumer likely to be a more important driver of business investment than mining in the period ahead, a recovery in consumer confidence is paramount if above-trend growth is to be sustained.

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... but the consumer is an uncertainty ahead

Chart 1.

Qld net migration has rallied off historic lows

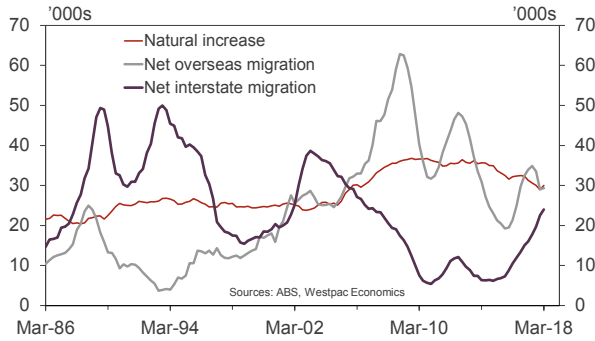


Chart 2.

Qld: employment's share of population up

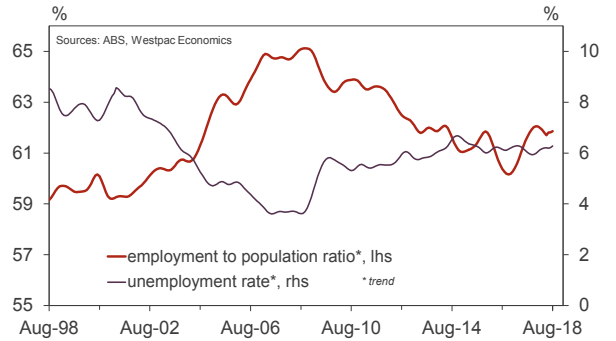


Chart 3.

Labour incomes have gained as a result

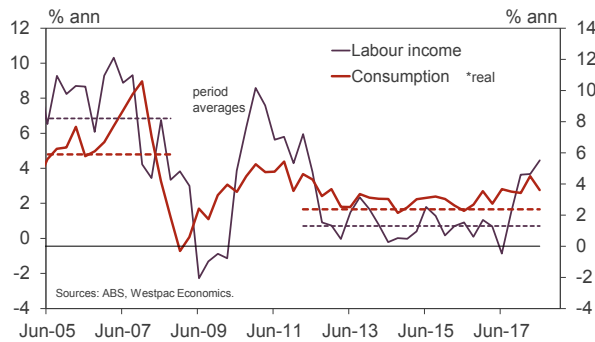


Chart 4.

Qld dwelling approvals remain at elevated level

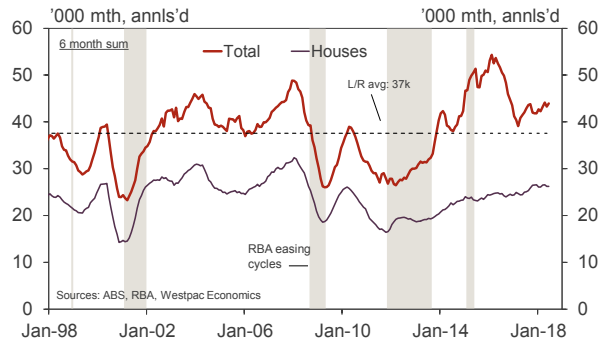


Chart 5.

Consumer & business confidence ease back

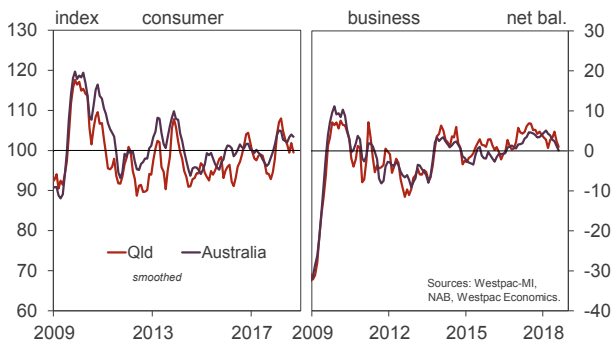
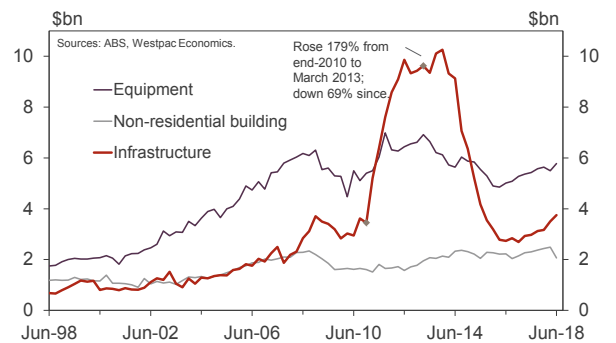


Chart 6.

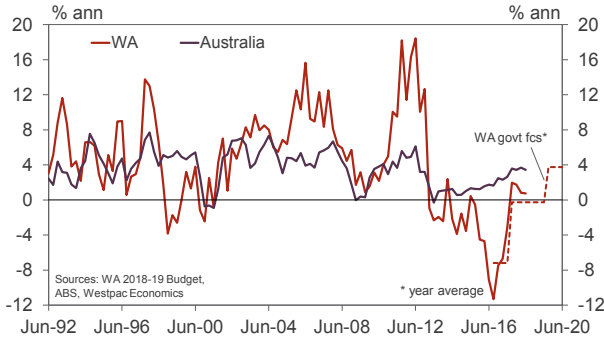
Qld business investment: in modest uptrend



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Western Australia: recovery still anaemic ...

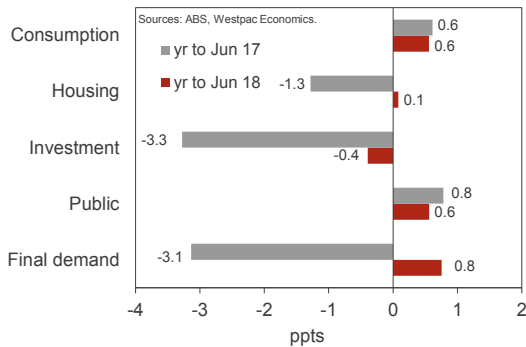
WA state demand: deep contraction ends



With the WA economy finally lifting out of recession and the mining sector benefitting from the sustained lift in key commodity prices, sentiment has started to turn strongly positive in the west. Despite this, growth has yet to establish convincing momentum with the state continuing to carry notable weaknesses around housing and migration flows.

WA state demand eked out a 0.2% gain in Q2, holding annual growth at 0.8%, unchanged from Q1. While slightly better than expected - the WA state government's budget forecasts were for a 0.25% contraction over the full financial year - growth is still anaemic at best. The more positive news is around incomes. Our estimates suggest the state's terms of trade are up around 10%yr, buoyed by a lift in commodity prices that has lasted longer than most expected. That in turn suggests state income growth is likely to post a further lift, a welcome result after the somewhat tentative recovery in 2016/17 from large back to back declines in the previous two years.

WA: contributions to state final demand

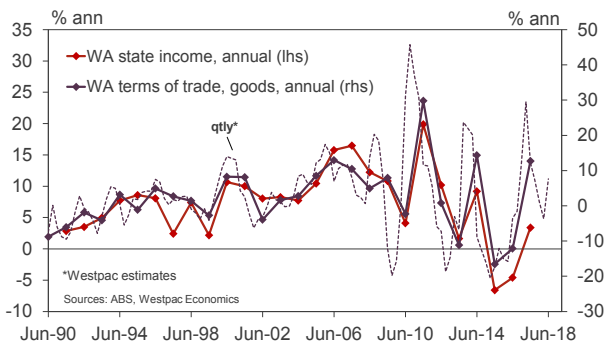


That income lift has yet to play through to activity. Business investment is still in the process of troughing (-2.1%yr) rather than turning up (although the mining producers have reportedly increased spending on maintaining and replacing older sites).

Public demand continues to provide some support, recording growth of 2.5% over the year to June, but is tracking well behind the strong gains being seen in the eastern states.

Consumer spending remains lacklustre. Consumption barely grew over the 6 months to June and is up just 1.0%yr, a third of the pace nationally and a quarter of the state's trend rate historically. Having weathered several difficult years of contracting incomes and balance sheets, the welcome turnaround in income growth looks to have mostly gone towards shoring up finances so far with little pass through to spending. Improving population dynamics are likely to aid household demand as we move into 2019.

WA's terms of trade vs state income



WA's housing sector remains a source of disappointment. The Perth market still has not managed to pull out of its five year price correction. Similarly, after showing tentative signs of stabilising, approvals point to some further weakening in new dwelling construction over the second half of 2018.

For housing, the improved economic performance and lift in incomes is being offset by a continued overhang of stock (though down from last year's 6.8% peak, rental vacancy rates remain very high at 5.6%) and the tightening in credit conditions and lending standards.

Weak population growth remains a significant restraining factor for both housing and consumer demand. That may start to turn with the state economy's return to growth, but it could take some time yet. WA's labour market has turned the corner but employment growth is still not particularly strong and wages growth remains sub-par. Without the drawcard of boom time mining sector wages, migrants will likely remain difficult to attract.

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... as income lift yet to flow through to activity

Chart 1.

Commodity prices: iron ore & crude oil

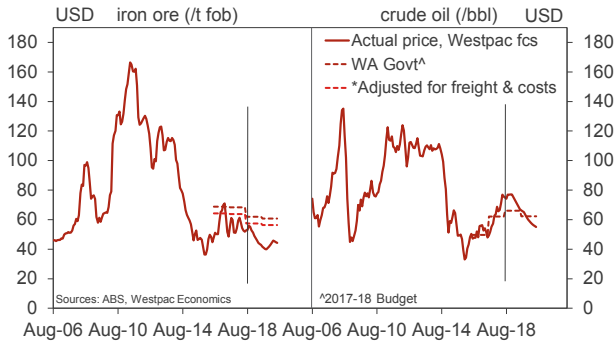


Chart 2.

WA households: income recovery continues

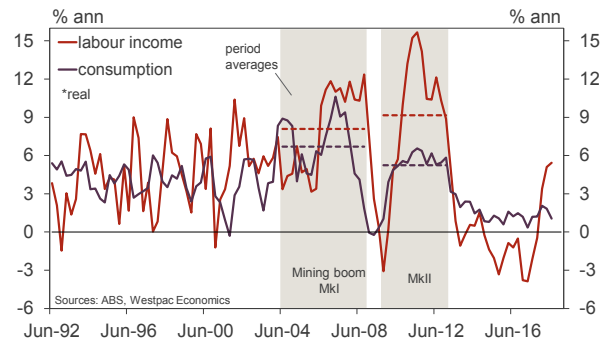


Chart 3.

New home building: starting to stabilise

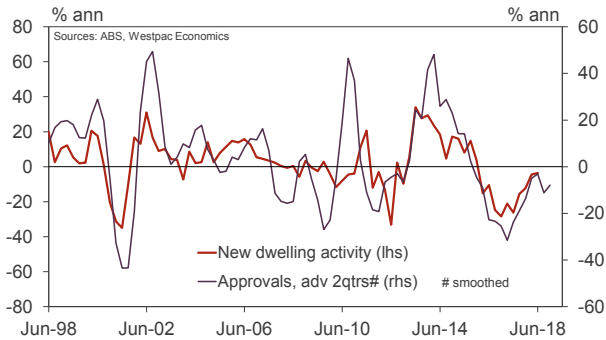


Chart 4.

House prices: Perth price declines moderate

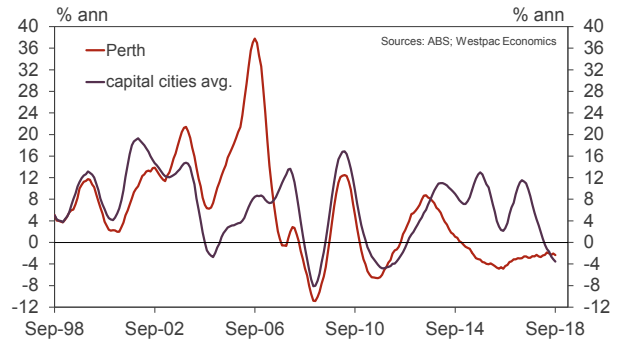


Chart 5.

Jobs market: initial rebound losing momentum?

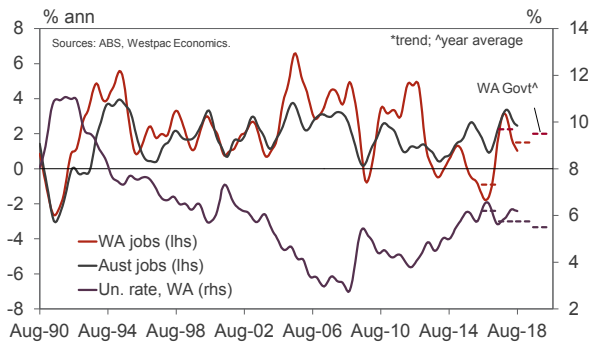
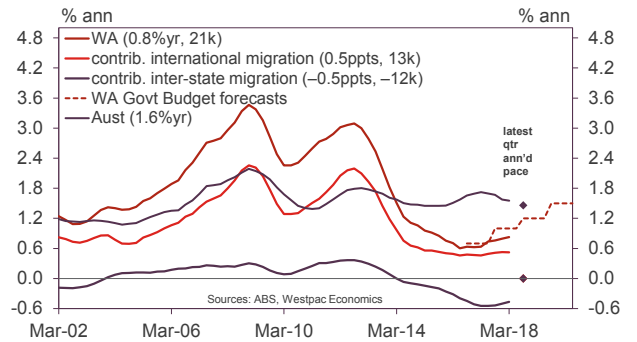


Chart 6.

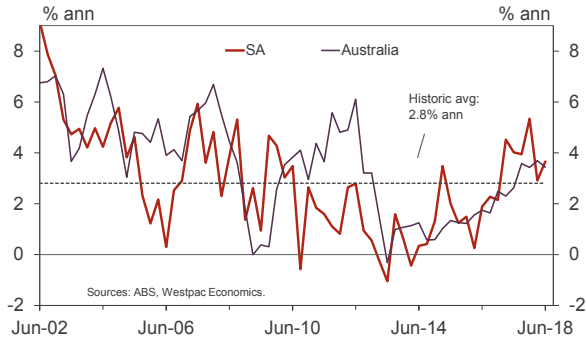
WA's population growth



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South Australia: state demand robust...

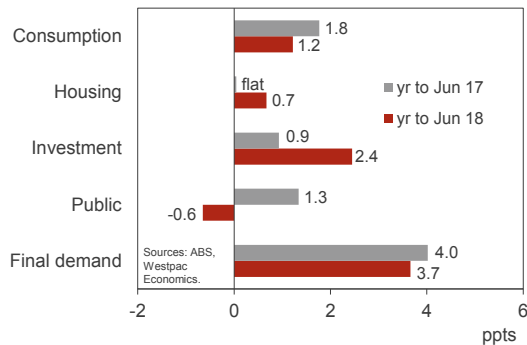
State final demand growth lifts in Q2



The South Australian economy has been tracking along at an above-trend pace. State final demand rose by 1.3% in the June quarter, while Q1 was revised up to 0.4% from a 0.2% contraction. This brought annual growth to 3.7%. In contrast to recent history, annual growth in private demand is now moving quicker than public demand, 5.8% compared to -2.6%. Business conditions are reported to be positive with exporters benefitting from a lower AUD, while public consumption is still trending up driven by health.

The improved economy provided a solid backdrop for the newly elected State Government's budget. As the first Liberal Party budget for sixteen years, there were some changes in the fiscal-mix. Small businesses will see a payroll tax cut, and the land tax-free threshold will be increased, while a number of cost efficiency savings measures were also announced. Public investment is set to continue to support growth with \$11.3bn allocated to infrastructure spending for transport, new schools and health.

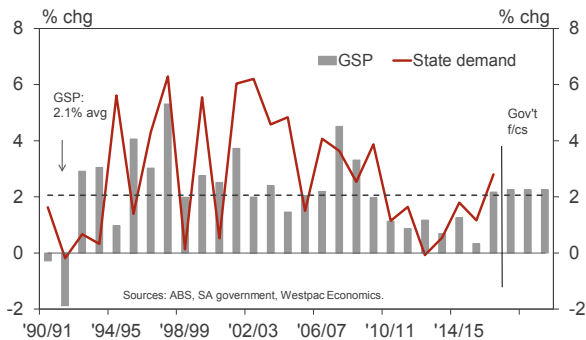
SA contributions to state final demand



Business investment has resurged from a period of subdued activity. It drove gains in private demand in the first half of 2018, accounting for more than two thirds of the increase over the period despite making up only a sixth of total private output. A strong uplift across construction - in particular engineering works - as well as equipment spending are responsible. However caution is warranted given that the result could be inflated in the near term by the completion of a few large projects. Dwelling investment also picked up and the approvals pipeline is looking promising. The policy move to reduce land taxes will provide further impetus.

Public demand had a softer quarter with both government consumption and investment pulling back. Health spending has been a key driver of employment gains and the Government has allotted \$800mn over five years on health and hospital services. Nonetheless, public consumption cost savings are in the pipeline with the Government targeting operating surpluses from 2018-19 onwards.

SA economic performance & outlook



Household consumption is growing at a moderate pace, well up from the depths of the car manufacturing closure period, albeit still below that of the national economy. It rose 2.1%yr in the year to June coinciding with a slowdown in SA employment growth in the first half of 2018. Key here is the relatively slow 0.7% annual population growth.

Though domestic consumption growth is modest, businesses have been successful in selling goods and services overseas. The wine industry in SA is moving from strength to strength, while demand for tertiary education continues to grow. A lower Australian dollar offers further support for the export sectors.

Overall, it is important to note that while State Final Demand (SFD) is quite strong, it differs to Gross State Product (GSP) in that it does not include inventories or net exports. GSP estimates are only updated annually. The State Budget estimated 2017-18 SFD at 3%, but GSP of 2.25% - a trend pace expected to hold through to 2021-22.

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... as policy transition begins

Chart 1.

South Australia: resurgence in private demand

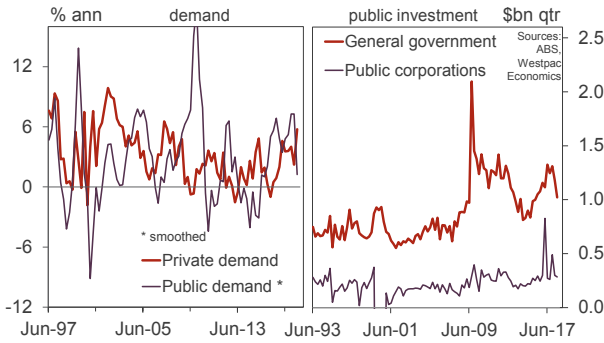


Chart 2.

As business investment bounces back

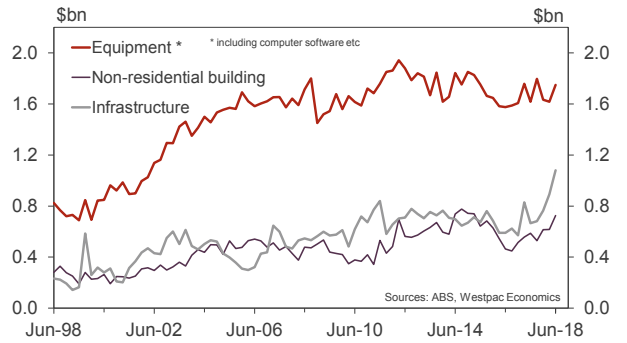


Chart 3.

Adelaide house prices holding up better

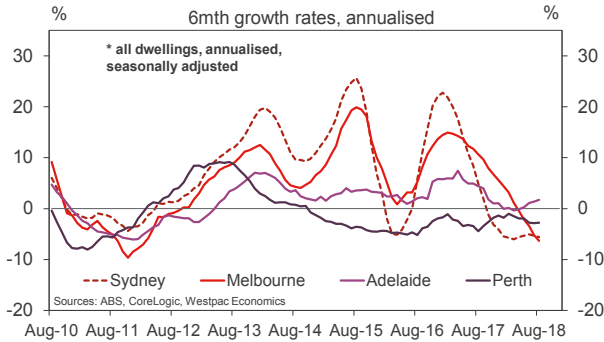


Chart 4.

Dwelling approvals: SA vs Aus

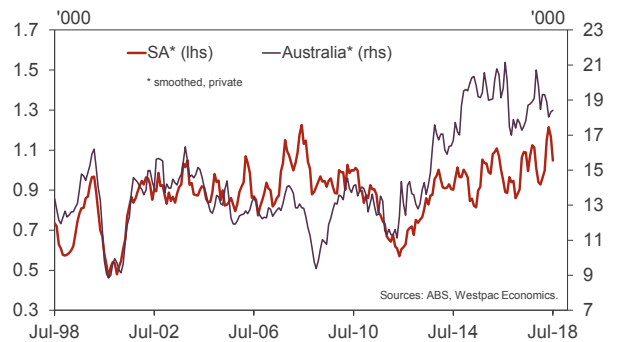


Chart 5.

SA jobs growth has cooled

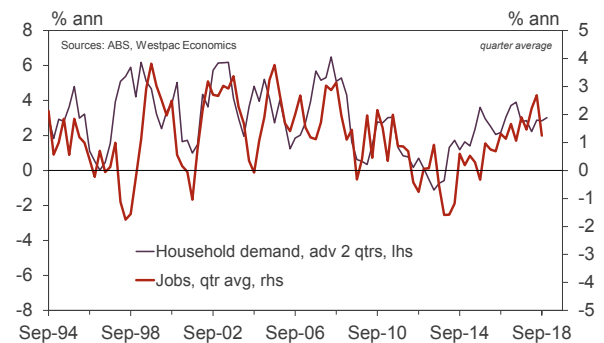
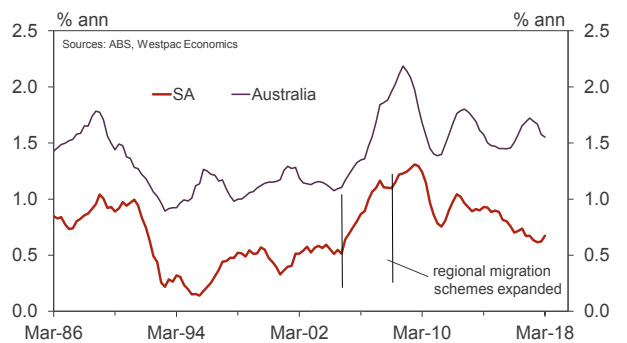


Chart 6.

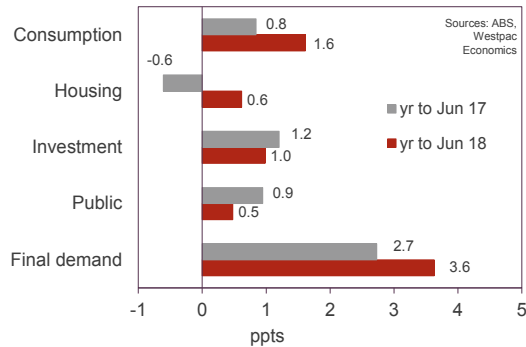
Weak population growth a lasting concern



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Tasmania: businesses lift investment ...

Tasmania: contributions to state demand



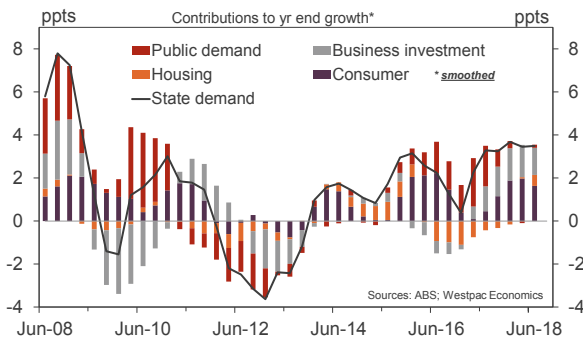
Tasmanian is experiencing a period of robust economic activity and the outlook is broadly positive.

State population growth has strengthened, home building is in an upswing, businesses are investing, the lower Australian dollar is providing a significant boost to sectors such as tourism and external conditions (including on the mainland) are supportive.

State demand grew by a brisk 3.7% in the year to June 2018. Indeed, over the past four years, demand growth has averaged 2.9%, an above par pace, with the long-run average at 2.3%.

Private sector demand has accelerated, expanding by a brisk 4.4% over the past year - the strongest period of growth since 2007, ahead of the GFC. Strength is broadly based, with: consumer spending up 2.7%; home building activity rebounding by almost 19%; and business investment increasing at a double digit pace, up 11%.

Tasmanian state demand

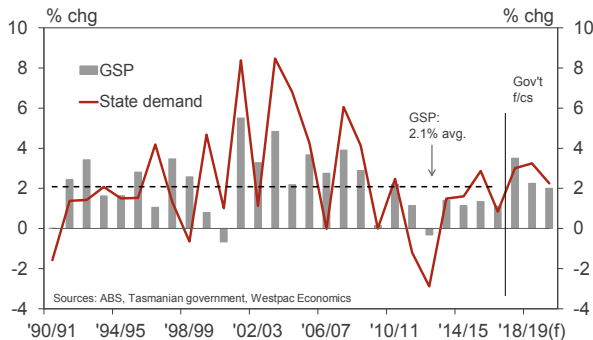


Business investment has rebounded sharply from the lows at the end of 2016, increasing by 28% over the past 18 months. This directly accounted for 2.2ppts of the 6.6% increase in state demand over this period - largely centred on a revival in equipment spending.

The tourism sector is an important contributor to the improved economy. Further growth in visitor numbers and spending is providing employment opportunities and is attracting investment in tourism accommodation.

Other industries to enjoy positive conditions include several areas of agriculture and some specialist manufacturing. The forestry-related industries are also experiencing a recovery, with improved prices, increased exports and the development of new processing plants. The aquaculture industry is also set for further growth, with several major new projects under consideration which could potentially double the State's salmon output over the next 12 years.

Tasmanian economic performance & outlook



The state government was understandably positive in their annual budget update of June 14.

In 2017/18, state final demand grew by 3.6%, comfortably eclipsing the budget forecast for an increase of 3.0%. The budget papers expected demand growth of 3.25% for 2018/19, supported by an increase in home building, before moderating to a projected and more sustainable 2.25% in 2019/20.

The government expects output growth to be a stellar 3.5% in 2017/18, well in excess of the long-run average of about 2.0% and the strongest outcome since 2007/8. Growth is expected to moderate to 2.25% in 2018/19 and then moderate to a trend 2.0% in 2019/20.

A key risk, as always, is business investment, given the lumpy nature of such spending in a small economy.

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... responding to positive backdrop

Chart 1.

Domestic demand accelerates

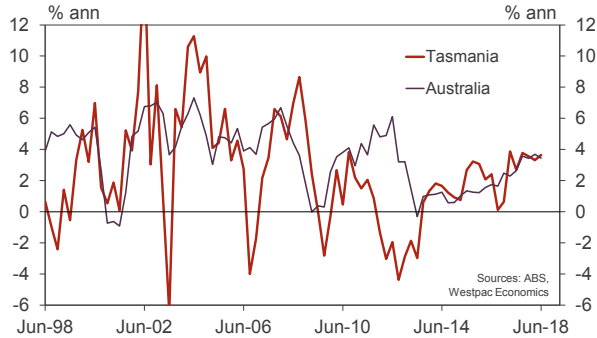


Chart 2.

Tasmania: employment advancing

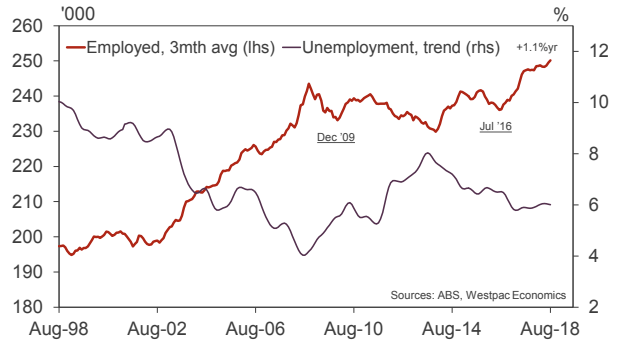


Chart 3.

Hobart house prices: still rising

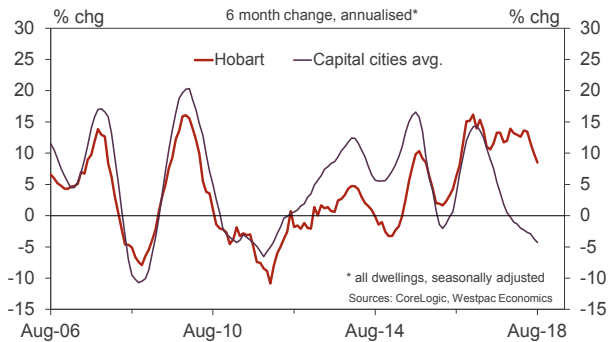


Chart 4.

New dwelling activity: further upside

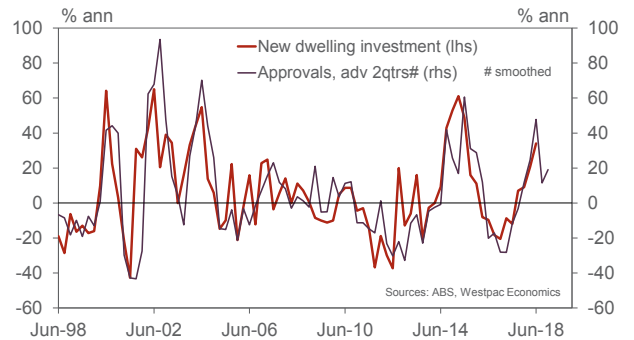


Chart 5.

Non-residential construction: sizeable pipeline

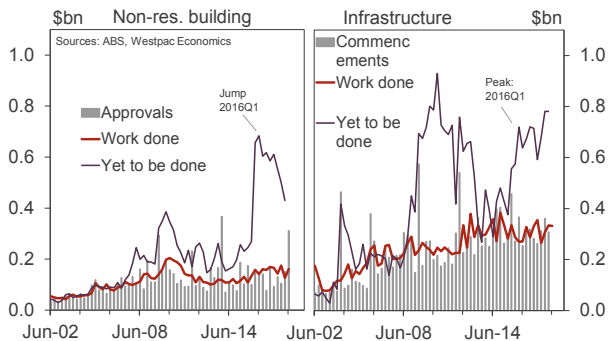
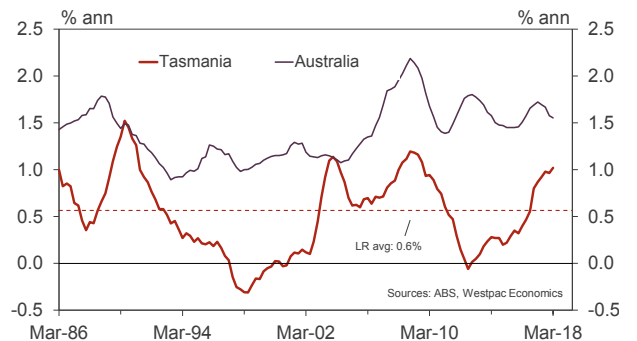


Chart 6.

Tasmania: population growth, near historic highs



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Summary indicators

Chart 1.

Population

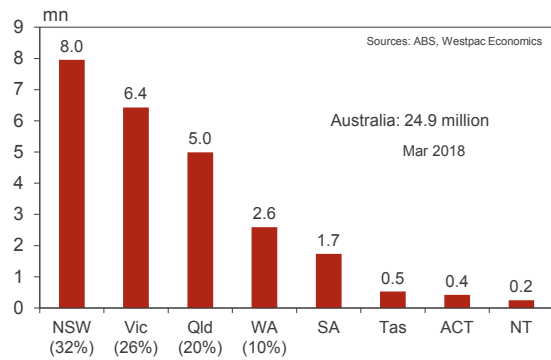


Chart 2.

Gross State Product

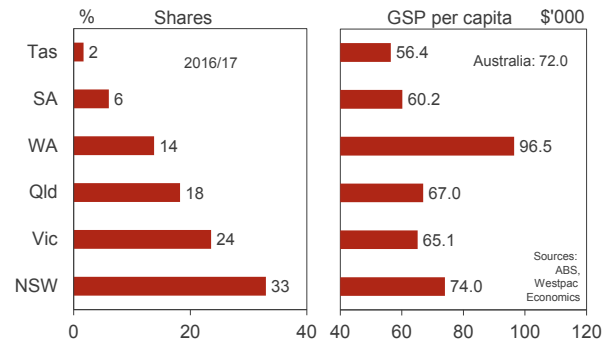


Chart 3.

Population growth 1.6% nationally

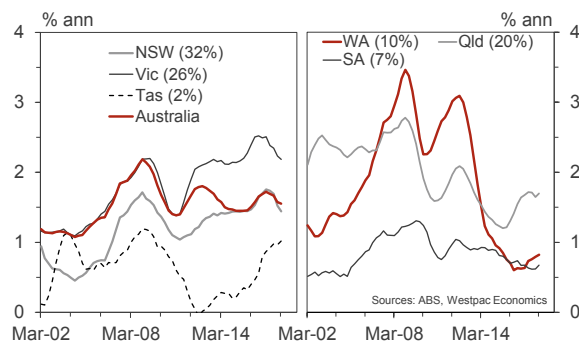
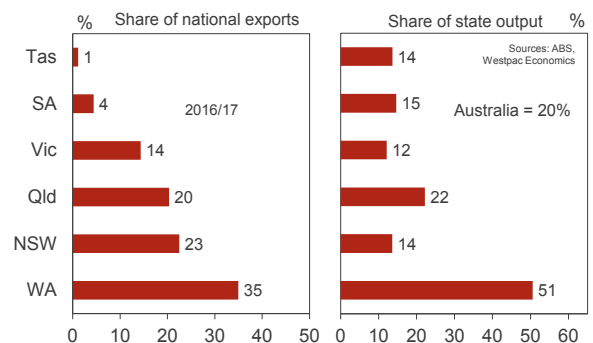


Chart 4.

Exports of goods & services



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

		2017/18f		2018/19f		2019/20f	
		Govt f/cs	Westpac	Govt f/cs	Westpac	Govt f/cs	Westpac
Australia *	GDP	2.9	2.9	2.8	3.0	2.8	2.7
	Employment	2.7	3.0	1.7	2.0	1.6	1.7
NSW	GSP	3.00	3.0	2.75	3.0	2.8	2.7
	Employment	3.00	3.1	1.75	2.1	1.5	1.7
Vic	GSP	3.00	3.0	2.75	3.0	2.8	2.8
	Employment	2.75	2.7	2.00	2.1	1.8	1.9
Qld	GSP	2.75	2.6	3.00	3.0	2.8	2.5
	Employment	2.75	4.2	1.50	1.7	1.8	1.6
WA	GSP	2.50	2.4	3.25	3.0	3.8	2.7
	Employment	2.25	2.3	1.50	1.5	2.0	1.2
SA	GSP	2.25	2.1	2.25	2.3	2.3	2.0
	Employment	2.10	2.1	1.50	1.3	1.0	1.0
Tasmania	GSP	3.50	3.3	2.25	2.3	2.0	2.0
	Employment	2.25	3.0	0.50	1.2	1.0	1.0

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

Gross State Product

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18*
NSW	2.6	2.5	2.0	2.0	2.8	3.9	2.9	-
Vic	2.9	1.8	1.1	2.0	2.9	3.5	3.3	-
Qld	0.6	5.5	2.8	2.2	1.2	2.6	1.8	-
WA	4.3	9.4	6.0	5.9	2.7	1.0	-2.7	-
SA	1.1	0.9	1.2	0.7	1.3	0.3	2.2	-
Tas	2.2	1.1	-0.3	1.4	1.1	1.3	1.1	-
Australia	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 2017/18 update is to be released in late November.

Employment

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18
NSW	2.5	0.7	1.7	0.5	1.3	3.8	1.1	3.1
Vic	2.8	1.1	1.2	0.9	2.5	2.7	4.0	2.7
Qld	1.8	1.3	0.2	1.3	0.2	1.7	0.1	4.2
WA	3.4	4.0	3.1	-0.0	1.0	-0.5	-0.9	2.3
SA	1.5	0.5	0.1	-1.3	0.4	0.5	1.3	2.1
Tas	1.3	-1.3	-1.0	-0.4	2.8	-0.2	0.8	3.0
Australia	2.4	1.2	1.3	0.6	1.3	2.3	1.5	3.0

Sources: ABS, Westpac Economics

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