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Invited Article

The Australian Economy in 2018–2019: Convergence in Economic Activity across Australia¹

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... [A]bstracting from the cyclical dynamics, there is a longer-run trend towards more similarity, rather than more divergence, in the underlying economic structure across the country. ~ Philip Lowe, Governor, Reserve Bank of Australia

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Abstract

Economic activity in Australia continued to improve in 2017–2018 with growth spreading across the mainland state economies. Labour market conditions in Australia improved markedly in 2017–2018 while the inflation rate was steady around the lower end of the Reserve Bank of Australia's 2–3 per cent target band. Real wage growth was weak and is likely to remain weak in 2018–2019, putting downward pressure on household consumption. Output growth in 2018–2019 is likely to be solid with prospects of the Chinese economy and trade tensions between China and the United States posing the greatest downside risk to the Australian economy.

1. Introduction

Growth in the Australian economy gained momentum in 2017–2018. Domestic final demand, and non-mining business investment and exports, identified in last year's report as emerging positive trends (Robinson and Wang 2018), all contributed positively to output growth. Conditions in the labour market also improved. The unemployment rate fell to 5.1 per cent in October 2018. However, wages growth remained weak.

The momentum was evenly spread across the state economies. In line with Philip Lowe's appraisal, all state economies grew in 2017–2018, with Victoria (VIC) overtaking New South Wales (NSW) as the best performing state. Queensland (QLD) and South Australia (SA) also posted solid growth while Western Australia (WA) emerged from the recession induced by the unwinding of mining investment.

Output growth in 2018–2019 is likely to be solid (Table 1) with contribution from developments in non-mining business investment. One caveat would be that while a pick-up in real wage growth is critical to support household consumption,

the prospect of stronger wages growth is unclear in the current environment of subdued inflation and accommodative financial conditions.

Notes: (a) forecasts, (b) Melbourne Institute's estimates, (c) MI denotes Melbourne Institute, (d) based on published forecasts in Asia Pacific Consensus Forecasts, October 2018, (e) as at the end of November 2019.

Sources: Melbourne Institute and *Consensus: A Digest of Economic Forecasts*

Prospects for the Chinese economy remain a key source of risk to the Australian economy compounded by trade tensions between Australia's key trading partners—the United States and China.

Section 2 of this article is devoted to a discussion of international economic developments. We focus on developments in the United States and China as their prospects and interaction have important implications for Australia. In Section 3, we summarise developments in the real economy and inflation, as well as developments in labour and financial markets for Australia.

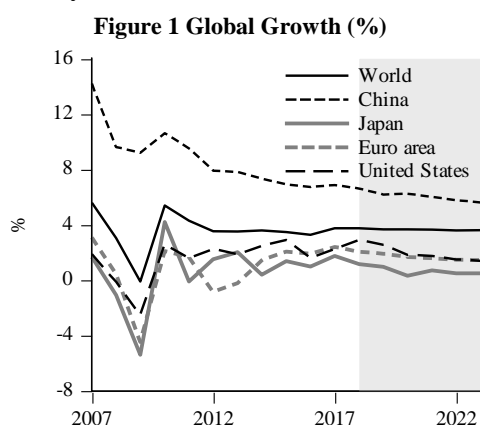
This issue of the *Review* is devoted to a discussion of the performance of the mainland States, which account for roughly 95 per cent of national GDP. Section 4 discusses developments in state final demands and in state labour and housing markets. We also note the growth of population in each state and highlight the differences in gross state product per capita. A brief review of how the industrial base of each state has changed follows. The last section concludes the article.

2. International Influences

World economic growth was solid in 2017–2018. Since the second half of 2018, however, the global outlook has tilted from positive to negative. The IMF (2018) projects global economic growth in 2018–2019 to be 3.7 per cent. While this forecast

is the same as the forecast made last October, it is 0.2 percentage points lower than forecasts made in April this year (IMF 2018) (Figure 1).

The downward revision of growth forecasts from April reflects uneven developments in some major economies and the increased risks and uncertainty arising from trade tensions in the global economy.



Note: Grey area denotes IMF forecasts.
Source: IMF (2018).

For the United Kingdom and the Euro area, growth remains weaker than expected due to slower export growth in 2018. Furthermore, the potentially negative consequences from a failed Brexit negotiation have yet to be taken into account. For Japan, a downward trend in economic growth is expected, due partly to uncertainty from weaker external demand, especially from China.

Medium-term growth prospects are likely to remain strong for emerging Asia, but less so for the rest of the emerging and developing countries due to a hostile trade environment and tight credit conditions.

2.1 The United States

The US economy grew strongly in 2018 due to favourable fiscal stimuli. The labour market remains tight, with the unemployment rate staying at a historically low level. The IMF forecasts the US GDP growth in 2018 to be 2.9 per cent, a

noticeable rise of 0.5 percentage points from their last October forecast. The IMF forecasts growth of 2.5 and 1.8 per cent in 2019 and 2020, respectively. This downward revision of growth in the US economy reflects the likely negative effects of trade wars, the normalisation of monetary policy and the tapering of fiscal stimulus (IMF 2018).

In 2018, the United States announced trade restrictions on several of its trading partners. In January, it announced tariffs on a number of products worth around US\$10 billion, most of which are manufactured in China. In July, August and September, the United States announced additional tariffs imposed on imports from China worth, in total, about US\$250 billion. China has since retaliated with a proportionally similar tariff on US imports. While the impact of trade wars has yet to be played out,¹ surveys of purchasing managers in China, the Euro area, Japan and the United States point to an expectation of softer growth in export orders (IMF 2018).

US monetary policy normalisation is expected to continue in 2018. The Federal Reserve increased interest rates three times in 2018, taking the federal funds rate to 2.5 per cent. Two rate hikes are expected in 2019. The tightening of monetary policy in the United States has led to an appreciation of the US dollar against a broad range of major currencies. There is concern that these policy moves will lead to tighter global financial conditions with likely negative consequences for trade and possibly sudden capital outflows in other countries.

2.2 China

The IMF projects China's output growth in 2018 to be 6.6 per cent, unchanged from the projection made in April. However, the IMF has revised down the 2019 growth

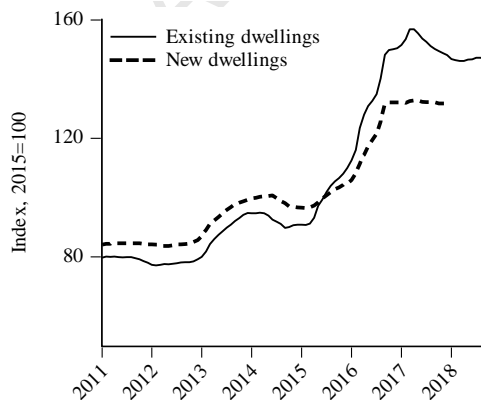
prospects to 6.2 per cent, citing concerns about the likely negative impacts of trade tensions between the United States and China. Growth in the Chinese economy is likely to come from a focus on domestic markets and from efforts to manage financial risks.

Conditions in the industrial sector have been subdued while growth in the service sectors, especially in information technology, software and business service industries, remains relatively strong. Crude steel production is also at a high level, and this continues to support Australia's exports of bulk commodities.

Regulatory tightening of the property sector to reduce the inventories level and to curb speculative investment continues in 2018. Residential housing prices for new dwellings in Tier-1 cities such as Beijing remained flat in the first half of 2018, while prices for existing dwellings grew slightly (Figure 2).

China's credit and financial risks remained considerable in 2018. The non-financial sector total credit to GDP ratio rose to 261 per cent in the March quarter, with government and household debt contributing to the increase. Corporate debt to GDP ratio, on the other hand, fell since March 2017, but bounced back a little to 164 per cent by the first quarter of 2018 (Figure 3).

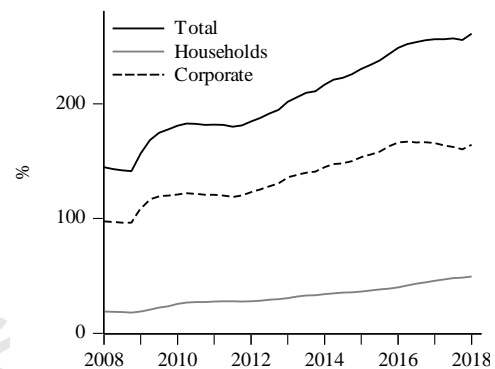
Figure 2 China's Residential Property Price for Beijing (Index, 2015=100)



Source: National sources, BIS Residential Property Price database.

Monetary policy remained accommodative in 2018. The People's Bank of China lowered the reserve requirement ratios four times (January to October) in response to global stock market turbulences and trade tensions between the United States and China to fill in the induced liquidity gaps of banks. It also injected liquidity through its medium-term lending facility with the aim of easing financing conditions for small and micro businesses.

Figure 3 China's Credit as Percentage of GDP (%)



Source: Bank for International Settlements.

Inflation fell to 1.8 per cent in 2017 and is expected to rise to around 2 per cent by the end of 2018. The renminbi appreciated against the US dollar in the first half of 2018 but depreciated in the second half due partly to the interest rate hikes by the Fed as monetary policy normalises in the United States.

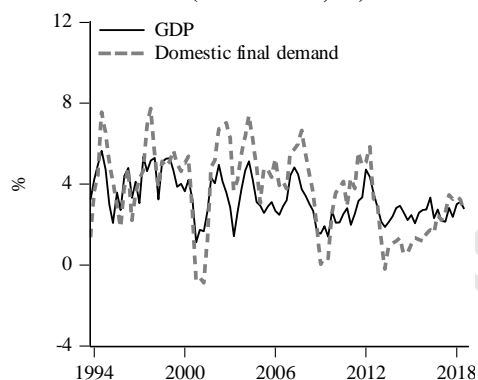
Fiscal policy became expansionary in the second half of 2018 in response to weaker growth in some parts of the economy. However, this is targeted expenditure with due consideration for financial and debt risks. For example, in July the Chinese Government issued guidelines on urban transport planning to support public infrastructure investment.

3. Australia

Overall conditions in the Australian economy remain positive. Output growth was 2.8 per cent in 2017–2018, a noticeable pick-up from 2.3 per cent in 2016–2017. GDP year-end growth in June 2018 at 3.1 per cent was the highest since September 2016 (Figure 4). Output growth in 2018–2019 is expected to be around 2.8 per cent (IMF 2018). The momentum in output growth is mainly due to growth in exports, non-mining business investment and public demand in a low interest rate environment.

The momentum of domestic final demand gained last year remained strong in 2017–2018, with the March quarter year-ended growth reaching 3.4 per cent, before sliding to 3.2 per cent in the June quarter (Figure 4).

Figure 4 Real GDP and Domestic Final Demand Growth (Year-Ended, %)



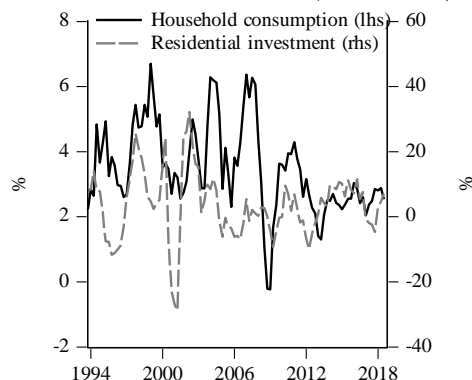
Source: Australian Bureau of Statistics.

Consumption growth picked up a little compared to last year, with a year-end growth rate of around 2.8 per cent throughout 2017–2018 (Figure 5). The trend increase in consumption growth in 2017–2018 is likely to be short lived without the support of a strong wages growth.

Residential investment picked up in 2018, with the year-ended growth in June 2018 reaching 4.7 per cent (Figure 5). The prospects are that residential construction will likely remain steady at the current

level for the next year or so, as dwelling approvals, a leading indicator for residential construction, changed little over the previous year.

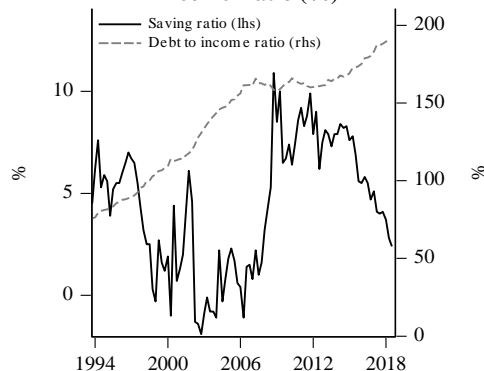
Figure 5 Real Household Consumption and Residential Investment Growth (Year-Ended, %)



Source: Australian Bureau of Statistics.

The household saving ratio has been falling in recent years and the trend continued in 2017–2018 (Figure 6). Given the high household debt to income ratio and weak wages growth, if this continues, the prospect of a falling household saving ratio remains a risk to the outlook of household consumption.

Figure 6 Trend Household Saving Ratio and Debt to Income Ratio (%)



Source: Australian Bureau of Statistics.

Public demand remained strong in 2017–2018, due both to public investment and public consumption. Public infrastructure work remains a large share of GDP and infrastructure spending on transport will remain particularly strong in the year to come. Year-ended growth in public consumption reached 5.1 per cent in June

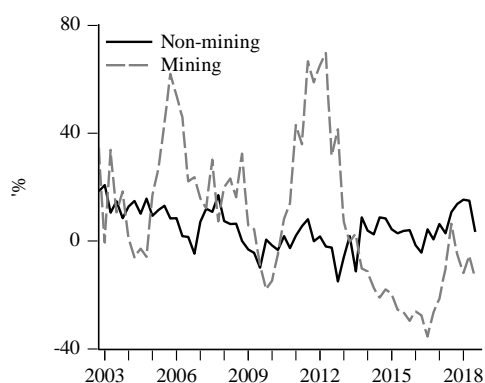
2018 and was seen as broad-based at both the state and federal levels (RBA 2018b).

3.1 Business Investment

Non-mining business investment increased by 15 per cent in the 12 months to June 2018 (Figure 7). It was mainly in non-residential construction activity including private sector spending on both non-residential building (offices, hotels and age care facilities), and infrastructure-related projects, such as renewable energy projects.

Non-mining business investment is expected to continue to expand in the next year or two, but at a slower rate than over the past year. The NAB Monthly Business Survey indicates a positive outlook for business conditions.

Figure 7 Non-mining and Mining Business Investment Growth (Year-Ended, %)



Source: Australian Bureau of Statistics.

Mining investment continued to fall in 2017–2018, with the year-end growth declining by 12 per cent in the March quarter and by 5 per cent in the June quarter (Figure 7). The decline in mining investment has almost run its course as construction work on the remaining liquefied natural gas (LNG) facilities is close to completion.

Mining investment is expected to stabilise and then gradually increase as firms invest to sustain production (Jenner et al. 2018). The RBA's liaison program also supports this projection as there was a

pick-up in mineral exploration activity over the year, although the level of the exploration is below historical levels.

3.2 Terms of Trade, Exchange Rate

Australia's terms of trade, namely the ratio of export to import prices, remained around their recent high levels in 2017–2018. The Index in the 2018 June quarter is 20 per cent above its trough in March 2016. This is largely due to the rising prices of energy and other bulk commodities supported by the stronger-than-expected global demand in the past year.

Global energy demand has supported prices for oil, LNG and thermal coal, while China's strong demand for steel has supported both exports and the prices of iron ore and coking coal. The terms of trade are expected to decline in the next year or so as Chinese demand for bulk commodities gradually weakens and further low-cost global supply comes on line.

On a trade-weighted basis, the Australian dollar remained relatively stable in 2017–2018 as it had been for the past couple of years. Although rising commodity prices would normally be associated with a stronger Australian dollar, the appreciation in 2018 so far was small due to the offsetting effect from the narrowed yield differential between bonds in Australia and those in major markets.

Overall, resource exports growth was solid in 2018, after rebounding from the March 2017 quarter fall due to adverse weather conditions. Metal ore exports also grew steadily, contributing to the pick-ups in year-ended growth in exports in the March and June quarters of 2018. Rural production was, to some extent, weakened by the drought conditions in some parts of the country, but this was offset by an increase in meat production (resulting in a

small net fall in rural exports in the March quarter). Service and manufactured exports have grown steadily over recent years, and export of services, in particular, is expected to remain a significant contributor to exports growth in the near term.

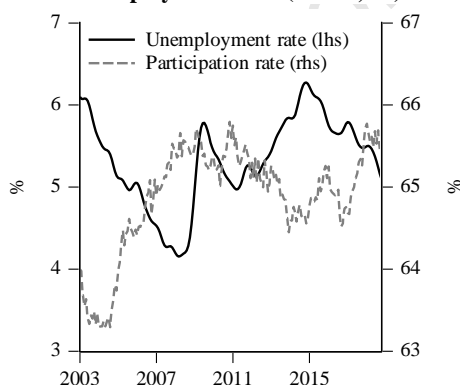
Exports growth is expected to remain solid although the trade tensions between the United States and China may present problems as both are significant trading partners.

Imports growth remained steady in 2017–2018 due mainly to stronger domestic final demand. Imports growth in the June quarter reached 6.2 per cent over the year, with all categories of imports, including capital goods, consumption goods, services and intermediate goods, contributing positively.

3.3 Labour

The Australian labour market further improved in 2017–2018. Year-ended employment growth was 2.6 per cent in June. Full-time employment grew strongly in the first quarter of 2018, while part-time employment accounted for most of the growth in the second quarter.

Figure 8 Participation Rate (%) and Unemployment Rate (Trend, %)



Source: Australian Bureau of Statistics.

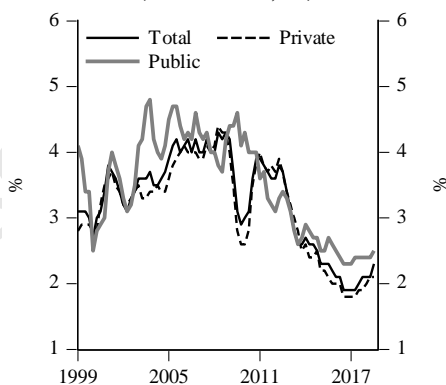
Consistent with the improvement in employment growth, the unemployment rate remained steady at 5.5 per cent over

the year, with the October rate reaching yet another historically low level (5.1 per cent) (Figure 8). The participation rate, namely the share of the working-age population that is in the labour force, remained high in 2017–2018. Despite improvement in the labour market, however, average hours worked did not rise.

3.4 Wages and Inflation

Wages growth picked up very little in 2017–2018 compared to the previous year, despite the improvements in the labour market. In particular, growth in the Wage Price Index—the main measure focused on by policymakers—has remained around its lowest rate since the late 1990s (Figure 9).

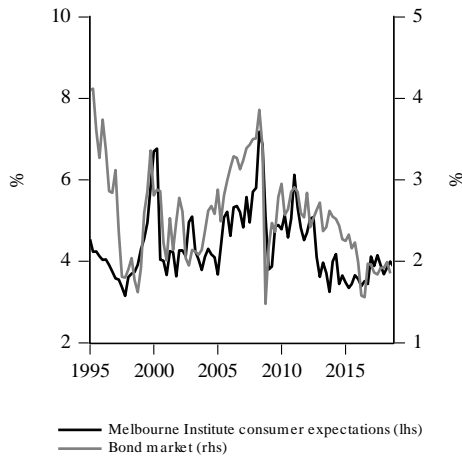
Figure 9 Wage Price Index Growth (Year-Ended, %)



Source: Australian Bureau of Statistics.

One of the main contributors to weak wage growth is low inflationary expectations. This is evidenced by a batch of measures, including the Melbourne Institute consumer inflationary index and a financial market measure (the implied difference between indexed and nominal bonds) (Figure 10). Meanwhile, underlying inflation remains at a low level (standing at 1.75 per cent in the September quarter). It reflects the spare capacity in the economy and the associated low wage growth. The upshot is that both price and wage changes are likely to remain subdued.

Figure 10 Inflation Expectations (Year-Ended, %)

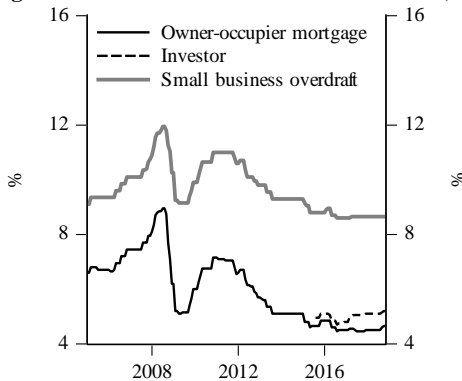


Sources: Melbourne Institute, Reserve Bank of Australia
 Note: Melbourne Institute measure is a 30 per cent trimmed mean.

3.5 Financial Markets

Financial conditions remained accommodative in 2017–2018. Inflation expectations are generally in line with the inflation target of around 2 per cent. Given the concerns about low wage growth and possible housing market overheating, there was little impetus for a change in monetary policy settings. The RBA’s cash rate has been maintained at 1.5 per cent since August 2016, and it is expected to remain unchanged in 2018–2019.

Figure 11 Indicator Variable Interest Rates (%)

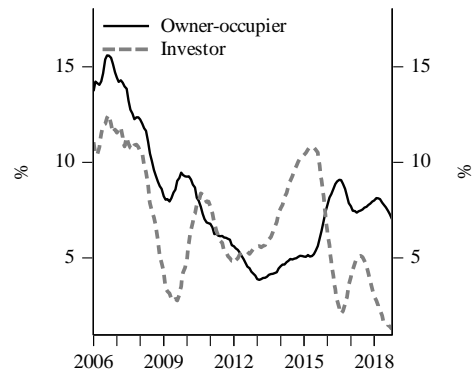


Source: Reserve Bank of Australia.

Mortgage rates on housing loans increased a little due to increased lending costs for banks while interest rates to small businesses remained unchanged over the year. All borrowing rates remained at historically low levels (Figure 11). The increases in interest rates on housing loans, both for owner-occupiers and investors, partially reflect the tightening effect of

Australia’s macroprudential policies in the past two years. This is consistent with the suppressed housing prices growth and declined housing credit growth (Figure 12).

Figure 12 Housing Credit Growth (Year-Ended, %)



Source: Reserve Bank of Australia.

4. Economic Activity in the Major States

4.1 Economic Activity

All the mainland state economies grew in 2017–2018. Measured by State Final Demand (SFD), VIC overtook NSW as the best performing state economy and posted the strongest SFD growth of 4.7 per cent (Table 2). NSW, QLD and SA all posted strong SFD growth rates between 3.4 and 3.5 per cent. The WA economy has emerged from the recession induced by the unwinding mining investment. WA’s SFD increased by 1.1 per cent in 2017–2018 after four years of consecutive declines.

Notes: (a) for Australia, it is domestic final demand (equivalent to SFD) and GDP (equivalent to GSP).

Source: ABS Cat. 5220.

Turning to gross state product (GSP) (which measures activity including net trade and change in inventories), Table 2 shows that strong economic activity in NSW, VIC and SA has been driven mainly by domestic demand as partly reflected in the trade deficits for NSW and VIC. NSW and VIC ran large international trade deficits in 2017–2018 (\$70.0 billion for NSW and A\$53.6 billion for VIC).

Improved activity in WA has been driven mainly by infrastructure spend and

exports growth (which has been helped by higher commodity prices and a more favourable exchange rate). In 2017–2018, WA posted a trade surplus of \$93.0 billion. Meanwhile, improved activity in QLD has been driven by both improved domestic demand and exports growth (Table 2).

4.2 Population and Housing

Strong domestic demand in NSW and VIC in the past several years has been in part due to considerable population increase, particularly in the last few years with overseas migration accounting for the majority (around 76 per cent in NSW and 60 per cent in VIC) (Table 3). QLD has also experienced a strong increase in population though this increase has been shared more evenly between natural increase and inter-state and overseas migration.

Notes: (a) rounded up to thousands; owing to unavailability of June 2018 data, the quarterly growth for June 2018 was projected to be the same as in March 2018.

Source: ABS Cat 5220 and Cat 3101.

The upshot of the strong population growth has been the strong demand for housing and services. A strong demand for housing stimulates investment in housing and leads to positive spillover effects in related sectors like financial, real estate and insurance services. In particular, VIC's GSP and SFD growth rates have been well above the national average. However, the average GSP per capita of VIC over the last three years (Table 3) at 1.3 per cent is just above the national average of 1.1 per cent. Also, by this measure, the SA and WA economies have been the weaker among the major states, recording average growth rates of 0.8 and -0.3 per cent, respectively.

Strong economic activity in the housing construction sector has been key to strong economic activity in NSW and VIC over

the past five years. However, it has also led to elevated house prices in the capital cities of these two states, raising concern about possible collapses in prices. The June 2018 ABS's residential property price indexes show consecutive declines in Sydney's and Melbourne's house prices in the last several quarters. To gauge 'how long' and 'by how much?' house prices will move, we turn to a quick review of the fundamentals—housing demand and supply.

Dwelling approvals and investment in both NSW and VIC have been at historic highs and appear to have reached their peak. Investor activity, to some extent, may have contributed to the unprecedented level of housing investment and construction in NSW and VIC. However, the fundamental driver has been robust population growth in both states.

The information from dwelling approvals indicates that housing investment and housing construction activity in NSW and VIC are likely to level off gradually over the next year or two. Beyond that, trends in population growth will have important implications, especially whether it will be a soft or a hard landing, for housing construction activity in both NSW and VIC and house prices in their capital cities.

Housing market activity in QLD and SA has been more moderate in the last few years, compared to that in NSW and VIC. Year-ended growth rates in the Brisbane and Adelaide residential property price indexes average around 4.0 and 3.7 per cent, respectively, over the past five years (as compared 10.7 and 8.7 per cent for Sydney and Melbourne, respectively). In contrast, the year-ended growth in the Perth residential property price index has been negative since March 2015. Overall, housing market activity across major states is likely to ease in 2019.

4.3 Labour Market by State

Labour market conditions in NSW, VIC and, to some extent, SA continued to improve in 2018. VIC recorded the biggest improvement in the past year as VIC's unemployment rate fell from 5.7 per cent in December 2017 to 4.5 per cent in October 2018. SA's unemployment rate also declined, but at a lesser extent, from 6.0 per cent to 5.5 per cent over the same period. Some of the declines in the VIC and SA unemployment rates, though, are attributable to declines in the participation rates of these two states over this period (Table 4).

In contrast, after a gradual improvement towards the end of 2017, labour market conditions in WA worsened in the first half of 2018. This worsening was mainly attributable to the fading impact of infrastructure spend following the 2017–2018 State and Federal Budgets. Labour market conditions in WA, however, are likely to improve in 2019 due to further infrastructure spending following the 2018–2019 Federal and State Budgets (Government of Western Australia 2018).

Source: ABS Cat. 6202.

Meanwhile, the worsening labour market conditions in QLD during 2018 were mainly attributed to weak job creation. Had it not been for the decline in its participation rate, the unemployment rate in QLD would have been higher.

Table 6 provides the jobs added across industries in each of the five major states between August 2017 and August 2018. Over these 12 months, the NSW economy added 150,000 jobs—the most among major states (and about half of the total jobs added in Australia). This strong job creation, underpinned by strong economic

activity, has kept the NSW unemployment rate under 5 per cent since early 2017.

A large proportion of the jobs created in NSW were in construction (added 25,000) and financial and real estate services (a combined total of added 46,000). Professional, scientific and technical services (added 54,000) and manufacturing (added 34,000) were the other main job sources in NSW.

Similar to NSW, construction (added 29,000) and financial and real estate services (added a combined total of 15,000) were the main job creators in VIC,

Source: ABS, Labour Force, Australia, Detailed, Quarterly, August 2018, Table EQ05.

Source: ABS, Labour Force, Australia, Detailed, Quarterly, August 2018, Table EQ03.

together with public administration (added 21,000) and healthcare and social assistance (added 18,000). For QLD, the top three industries were: mining (added 10,000), manufacturing (added 34,000) and public administration (added 28,000). Mining and manufacturing (added a total of 35,000) were the main job sources in WA while job creation was weaker in SA as compared to other states.

4.4 Changing Industry Composition

Table 6 provides a snapshot of employment share by industry across the major states. By this metric, major state economies share many similarities. In particular, healthcare and social assistance accounts for the biggest share in all major states, ranging from 12.8 per cent (NSW) to 15.1 per cent (SA), followed by retail trade, construction, education and training, and manufacturing.

At the turn of the current century, major State economies, while sharing some

similarities, had their distinctive core strengths. Financial and real estate services were the biggest industry in NSW by gross value added (GVA) share (Table 7). Manufacturing was the backbone of the VIC and SA economies. Mining, manufacturing and construction had similar GVA shares in QLD while mining was the dominant force in WA.

With improved activity in QLD, SA and WA and moderating housing construction activity in NSW and VIC (RBA 2018a), economic growth across the major states appears to be converging. Annual growth in GSP across the major states ranged between 1.9 and 3.5 per cent in 2017–2018 (with a standard deviation of 0.75 per cent), as compared to 0.4–3.7 per cent averaging between 2015–2016 and 2017–2018 (with a standard deviation of 1.3 per cent), and similarly when measured by annual SFD growth.

Notes: (a) sales includes: wholesale and retail trade; (b) all services includes: accommodation and food services; financial and insurance services; rental, hiring and real estate services; professional, scientific and technical services; administrative and support services; health care and social assistance; arts and recreation services; other services.

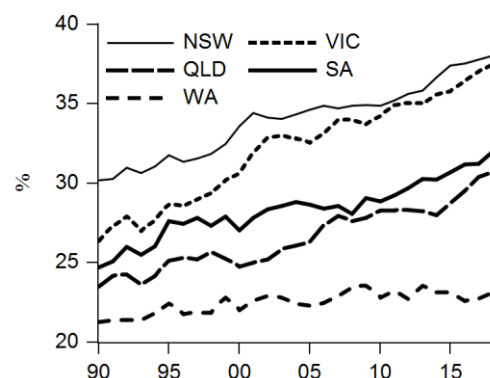
Source: ABS Cat 5220.

One reason for the convergence is the changing composition of industries in the states. While the composition of the WA economy has changed little, that of the other mainland state economies appear to share more similarities. With the decline of mining, financial and real estate services and health services have risen to claim the major shares in VIC, QLD and SA (Table 7), moving them towards services-based economies, like NSW. NSW, VIC, QLD and SA now share more similarities than they did at the turn of the century.

Figure 13 charts the GVA share of the services sector in all five major state economies and shows that they have all increased, though at a slower pace in WA.

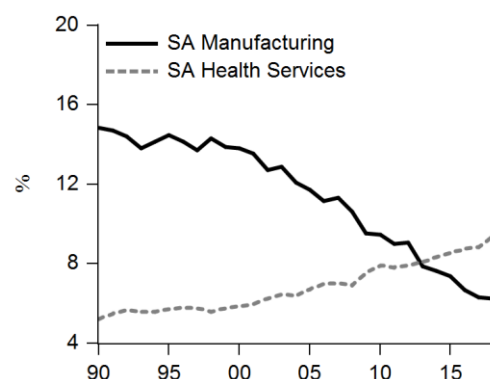
Much of the difference between NSW and VIC and the others is due to their larger financial and real estate services sector. Much of the difference between WA and the other states is due to the size of its mining sector. Going forward, convergence among the state economies is likely to be driven by their rising Services sectors (Lowe 2018).

Figure 13 Service Share by GVA (%)



Source: ABS Cat 5220.

Figure 14 SA Manufacturing and Health Services (%)



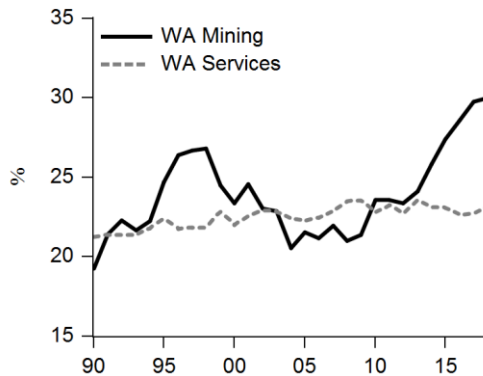
Source: ABS Cat 5220.

This is especially evident in SA. As manufacturing in this state has been declining (GVA share down by 8 percentage points since 1990), the health services sector has been rising to fill half of this decline (Figure 14). Health care and social assistance is now the biggest sector in SA by GVA.

The situation is less clear-cut for WA. Figure 15 charts the GVA shares of mining

and services in the WA economy. The share of services has been roughly constant, while the share of mining reflects the mining investment cycle. While mining will remain the backbone of the WA economy, which sector will rise to make up for this decline in the longer term is unclear.

Figure 15 WA Mining and Services Share (%)



Source: ABS Cat 5220.

In the short and medium terms, infrastructure spending is vital to smooth the transition in WA.² In the longer term, the services sector is likely to be the key to growth in the WA economy and health and education services are the growth sectors.

9. Concluding Remarks

Growth in the economy was 2.8 per cent in 2017–2018 and likely to pick up slightly in 2018–2019, mainly due to growth in resource exports. Real wage growth and inflation are likely to be low and stable, mostly due to weak growth in household income and hence household consumption.

Risks are mostly on the downside. Trade tension between the United States and China poses the greatest external risk leading to higher uncertainty in international financial markets which will negatively affect trade and investment across the global economy.

Two major downside risks in the domestic economy are weak household consumption and the unwinding of

housing investment and housing construction activity. Elevated household debt, low wage growth and the decline in some asset prices have put downward pressure on household consumption. Household consumption is likely to remain weak in the coming year and poses a non-negligible downside risk to growth. Meanwhile, population growth and infrastructure spending could help offset the unwinding of housing investment in NSW and VIC.

Economic conditions across the major states appear to be converging cyclically (as measured by economic growth) and structurally (based on the profile of industries) though their labour market conditions still vary despite recent improvement. A more synchronised level of economic activity across the states makes it easier to set macroeconomic policies, especially monetary policy as the economy-wide policy is more likely to benefit all the states.³

Meanwhile the Australian population is projected to grow at an annual rate between 1.4 (low projection) and 1.8 (high projection) per cent over the next 10 years to June 2027 (Australian Bureau of Statistics, 2018). As with the population growth in the last decade to June 2017, 60 per cent of growth⁴ in the next decade is projected to come from net overseas migration with the remainder from natural increase.

On the one hand, strong population growth without adequate infrastructure investment will place increasing stress on public services and transport systems as well as living standards. This, to some degree, has led to the recent debate about limiting overseas migration, in particular lowering the annual permanent immigration intake of 190,000. On the other hand, the IMF estimates suggest that the current migration program will add

0.5–1 percentage points to the annual average GDP growth between 2020–2050. This is because strong population growth, spearheaded by overseas migration, reduces the negative influence of Australian’s ageing population on the economy (IMF 2017).

In the short term, such a strong projected population growth (by advanced economy standards) will help sustain domestic demand and hence is likely to continue to underpin underlying growth in the economy in the years to come, absent dramatic negative shocks.

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Endnotes

1. During the G20 Summit in Argentina, the United States and China reached a 90-day trade truce, that is, on 1 January 2019 the United States will leave the tariffs on \$200 billion worth of China’s product at the 10 per cent rate, and not raise it to 25 per cent. This is a short-term solution and has not eliminated all trade tensions. The potential negative impacts of a global trade war remain a threat to global growth.

2. Recovery in the WA economy over the past year has been mainly driven by a considerable increase in public infrastructure spending. WA year-ended growth in public investment average at 4.9 per cent between September 2016 and June 2018.

3. The Eurozone debt crisis offers an example of how varying economic conditions among member states, under a single monetary policy setting, could lead to a massive build-up of economic imbalances between the slow-growing core economies and the more dynamic peripheral economies as capital flew from the former to the latter (Baldwin and Gros 2015).

4. The bulk of Australian net overseas migration over the past decade has been skilled permanent migrants through the current migration program.

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Table 1 Indicators of Australian Activity

	2018 ^b	2019 ^a		
		MI ^c	Low ^d	High ^d
GDP	2.9	3.0	2.5	3.2
Consumption	3.0	2.6	1.8	2.8
Domestic final demand	3.5	2.9	-	-
Unemployment rate	5.5	5.2	4.8	5.6
Employment growth	3.0	2.1	-	-
Wage cost index	2.1	2.3	2.0	2.7
Headline inflation	1.9	1.9	1.7	2.6
Underlying inflation	1.9	1.9	-	-
90-day bill rate ^e	2.0	2.4	1.9	2.6

Table 2 Annual Indicators of State Economic Activity, 2017/18

	SFD growth (%)	GSP growth (%)	International trade balance (billion \$)
NSW	3.4	2.6	-70.0
VIC	4.7	3.5	-53.6
QLD	3.5	3.4	23.6
SA	3.4	2.0	1.5
WA	1.1	1.9	93.0
AUS^a	3.4	2.8	-0.6

Table 3 Population Growth and GSP Per Capita

	Average 2015/16, 2016/17, 2017/18			
	GSP per capita growth (%)	Population growth (%)	Net overseas migration ^a ('000)	Population increase ^a ('000)
NSW	1.7	1.6	96,000	125,000
VIC	1.3	2.4	87,000	151,000
QLD	1.1	1.6	31,000	80,000
SA	0.8	0.7	13,000	13,000
WA	-0.3	0.8	13,000	20,000
AUS	1.1	1.7	248,000	403,000

Table 4 Labour Market Conditions by State

Oct 2018	Unemployment rate (%)	Participation rate (%)	Employ/Pop. ratio
NSW	4.6	65.2	62.2
VIC	4.5	65.5	62.5
QLD	6.2	65.6	61.6
SA	5.5	62.3	58.9
WA	5.9	68.5	64.5
AUS	5.1	65.6	62.3
Dec 2017	Unemployment rate (%)	Participation rate (%)	Employ/Pop. ratio
NSW	4.8	64.3	61.3
VIC	5.7	66.0	62.2
QLD	6.0	66.0	62.1
SA	6.0	62.4	58.7
WA	5.9	68.4	64.3
AUS	5.5	65.6	62.0

Table 5 Employment by Industry ('000): Full-Time (FT) and Part-Time (PT)

	Change between Aug 2016 and Aug 2017			Change between Aug 2017 and Aug 2018			Ratio of FT to PT		
	FT	PT	Total	FT	PT	Total	Aug 2016	Aug 2017	Aug 2018
Agriculture, forestry, fishing	27	1	27	-7	0	-8	2.6	2.9	2.9
Mining	-4	2	-1	34	-2	32	26.9	19.9	27.1
Manufacturing	3	-2	1	73	12	85	5.3	5.4	5.4
Electricity, gas, water, waste services	4	3	7	1	5	6	13.6	10.7	10.7
Construction	92	12	104	15	16	30	5.6	5.8	5.8
Wholesale trade	10	-	-1	-7	-2	-10	4.1	4.9	4.9
Retail trade	30	8	37	-32	21	-11	1.0	1.0	1.0
Accommodation, food services	11	29	40	-16	3	-12	0.7	0.7	0.7
Transport, postal, warehousing	34	-3	30	-13	16	2	3.6	4.0	4.0
Information media, telecommunications	5	3	9	-1	3	2	4.1	3.9	3.9
Financial, insurance services	-14	-2	-16	36	-1	35	4.6	4.5	4.5
Rental, hiring, real estate services	-1	-6	-7	10	6	16	2.9	3.3	3.3
Professional, scientific, technical serv.	-26	-	-43	42	24	66	3.3	3.4	3.4
Administrative, support serv.	-42	-2	-44	13	-17	-4	1.3	1.1	1.1
Public administration, safety	-14	-	-27	74	12	86	4.3	4.7	4.7
Education, training	33	30	62	-1	-7	-8	1.5	1.5	1.5
Health care, social assistance	101	37	137	-10	16	6	1.2	1.3	1.3
Arts, recreation services	-7	15	8	10	-2	7	1.2	1.0	1.0
Other services	15	-1	14	-22	3	-19	2.1	2.2	2.2
Total (industries)	258	81	339	199	103	303	2.1	2.2	2.2

Table 6 Employment by Industry and State: Jobs Added (Jobs, '000) and Industry Share (Share, %)

	Change in employment between Aug 2017 and Aug 2018					Employment share by Industry								
	NSW	VIC	QLD	SA	WA	NSW	VIC	QLD	SA	WA				
Agriculture, forestry, fishing	-3	-7	0	3	1	1.9	2.2	1.1	1.3	1.6	1.4	1.4	1.4	1.4
Mining	3	1	10	-1	20	1.1	0.7	0.7	1.0	4.9	7.9	5.5	5.7	6.3
Manufacturing	34	7	34	-4	15	7.5	8.8	7.7	8.2	4.9	6.3	5.8	5.1	6.0
Electricity, gas, water, waste services	-2	1	5	4	-2	0.9	1.4	1.3	1.6	1.4	1.4	31.9	25.0	27.8
Construction	25	29	-8	8	-20	9.6	9.7	9.4	8.7	9.1	9.1			
Wholesale trade	-19	-9	14	2	4	3.1	3.1	3.1	3.7	3.8	3.8			
Retail trade	26	-22	-5	-4	-5	9.8	9.9	9.9	10.4	9.0	9.0			
Accommodation, food services	-8	-9	-3	10	-6	6.5	6.7	6.7	7.8	5.4	6.9			
Transport, postal, warehousing	0	2	0	-7	5	5.1	5.1	5.1	4.7	7.2	5.1			
Information media, telecommunications	-9	15	-6	1	0	2.2	2.2	1.1	1.3	8.3	1.0			
Financial, insurance services	28	13	2	-1	-8	5.2	3.1	3.1	2.6	4.4	1.9			
Rental, hiring, real estate services	18	2	-3	3	-5	1.9	1.1	1.1	1.5	6.0	1.5			
Professional, scientific, technical serv.	54	4	10	1	-1	10.7	8.7	7.0	6.3	6.7	6.7			
Administrative, support serv.	-4	0	-2	-5	3	3.0	3.3	3.3	3.1	3.5	3.5			
Public administration, safety	-9	21	28	11	22	5.1	5.4	6.9	7.7	7.0	7.0			
Education, training	-7	5	11	-3	-10	8.1	8.2	9.1	7.2	7.6	7.6			
Health care, social assistance	0	18	-12	-8	9	12.8	13.6	13.4	15.1	13.1	13.1			
Arts, recreation services	14	13	-11	-2	-3	2.0	2.2	1.4	1.8	1.8	1.8			
Other services	8	-11	-17	-3	1	3.5	3.8	3.9	3.6	4.4	4.4			
Total (industries)	150	73	48	6	20	100.0	100.0	100.0	100.0	100.0	100.0			

Table 7 Gross Value-Added Share by Major Industries (%)

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