WESTPAC
Coast-to-Coast September 2022.

AUSTRALIA AND
THE GLOBAL ECONOMY

WESTPAC INSTITUTIONAL BANK

CONTENTS

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Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.

Sharp slowdown in growth in 2023

The Australian economy expanded by 0.9% in the June quarter for annual growth of 3.6%. For 2023 we expect growth to slow to 1.0%. That solid growth in the June quarter was driven by strong household spending (around 54% of GDP) as the reopening of the economy saw a further boost to expenditure, particularly on discretionary services. This was accompanied by a substantial fall in the still elevated savings rate. We had anticipated growth in household spending of 2.6%, compared to the actual result of 2.2%. But spending growth in the March quarter was revised up from 1.5% to 2.2%, confirming our positive view of the household sector.

The detail around household spending was also in line with our thinking – the savings rate fell from 11.1% to 8.7%, effectively freeing up $7.6bn to finance the additional $10.8bn in spending during the quarter. Discretionary services boomed – transport services up 37%; hotels, cafés and restaurants up 8.8%; and recreation and culture up 3.6%.

As we discuss in this Report, the reopening effect over the first half of 2022 was most apparent in NSW and Victoria, as well as the ACT, as they emerged from the delta lockdowns of last year. Consumer spending in these states, relative to pre-covid levels and on a per capita basis, is getting closer to that in the other states - albeit still trails a little.

But residential construction contracted by 2.9% and non–residential construction (private and public) was down by 1.8%. This unexpected contraction in construction (subtracted 0.3ppt from growth in the quarter) represented around a 0.6ppt turnaround from our prior. As we note in this report, it is striking that new home building activity in the 'delta states' of NSW and Victoria, has remained below 2019 levels throughout the pandemic - despite the substantial policy stimulus. That is in sharp contrast to strong upswings in other states, cycles which have now moved into a downward trend.

Looking forward, we expect to see a slowdown in the growth rate of consumer spending in the September and December quarters. The reopening effect will begin to fade, and the recent interest rate increases will start to impact households. There were two rate hikes in the June quarter (0.25% in May and 0.5% in June). The impact on household finances from those two rate hikes in the June quarter will have been minimal. But by the September and December quarters, which has seen rate 0.5% increases in July; August; and September the impact will be substantial. We expect the cash rate to rise by a further 125bps, to a peak of 3.60% in February 2023.

We recently lifted our forecast for the terminal rate from 3.35% to 3.6%, reflecting the ongoing upward pressure on world interest rates and, with the exception of house prices, Australia's current resilience in the face of rising rates – strong business confidence; record high capacity utilisation; a really tight labour market; anecdotal evidence of accelerating wage pressures; and acceptance from the Reserve Bank that the cash rate (as at early September) was likely still below that neutral level and therefore in stimulatory territory.

Although around one third of households hold a mortgage; one third are renters; and one third own their properties outright, rate increases impact all groups through a range of channels – the cash flow of borrowers; the indirect impact from investors who pass on higher funding costs to renters, particularly as rental vacancy rates are near record lows in many cities and regions; the wealth effect of falling house prices on those who own their properties outright and borrowers; and the recent collapse in Consumer Confidence. Nationally, house prices have already fallen by 4%, with our forecast of another 12% likely to follow through to the second half of 2023.

The contraction in construction in the June quarter has been attributed to weather delays and supply constraints. We expect to see construction lifting modestly through the second half of 2022 reflecting the build-up in the construction pipeline. A further contraction can be expected in 2023 as rising rates weigh on demand – effectively reducing the pipeline.

Reflecting these changes, we have lowered our growth forecast for 2022 from 4.4% to 3.4%.

Growth in consumer spending during 2022 is expected to slow from 4.4% in the first half of the year to 1.8% in the second half. But with the expected recovery in the construction cycle, with improving weather and easing supply chains, we see dwelling construction lifting by 5.4% in the second half of this year, a turnaround from a contraction of 3.4% in the first half of 2022.

Overall, with the expected short term recovery in the construction cycle partially offsetting the slowdown in the pace of consumer spending, we expect growth in the second half of 2022 to hold around the same 3.2% annualised pace as we saw in the first half – albeit conditions in the final quarter of 2022 are likely to more subdued than those during the September quarter.

On the trade front, with the reopening of the national border in the first half of this year, we have lift-off on international travel - both inbound and outbound. As we discuss in this Report, this is a boost for service exports across the various states - with the education and tourism sectors to benefit. Equally, as more Australians holiday overseas, they will take some of their spending dollars with them.

We have not changed our downbeat view for growth in 2023. We expect GDP growth in 2023 to slow to 1.0% with private domestic demand growth slowing to 0.2% (a sharp deceleration from an expected 5.4% expansion in 2022). We cannot rule out a negative quarter of growth in 2023 but do not expect a classic recession.

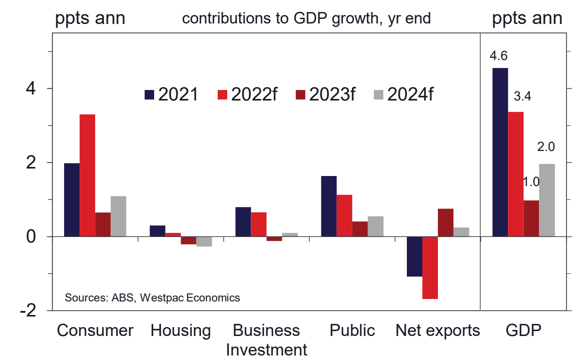
Consumer spending growth is expected to slow from 6.3% in 2022 to 1.2% in 2023; business investment growth slows from 5.8% to -1.0%; while dwelling construction growth swings from +2.0% to -4.0%. That slowdown in consumer spending will include a very modest further fall in the savings rate from 3.6% by the end of 2022 to 2.3% through 2023 - below the "equilibrium" rate of 6%. This will see the stock of "excess savings" accumulated during the pandemic, currently at $275 billion, wound back to around $200 billion by end 2023.

The economy in 2023 will experience the full accumulated effect of the lift in the cash rate from 0.1% in April 2022 to 3.60% in February 2023. Other negatives for growth in 2023 are: a total fade out of the "reopening" effect; a limited further fall in the savings rate to below equilibrium as households continue to draw down those excess savings albeit at a slower pace than in 2022; a rise in the unemployment rate from 3.0% to 4.2%; and a fall in house prices from peak to trough of around 16%.

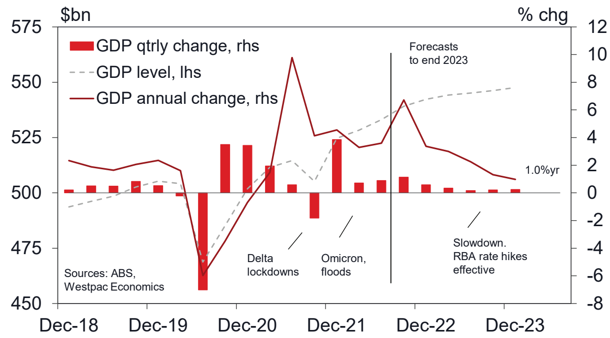
Bill Evans, Chief Economist

Australian Economic Outlook

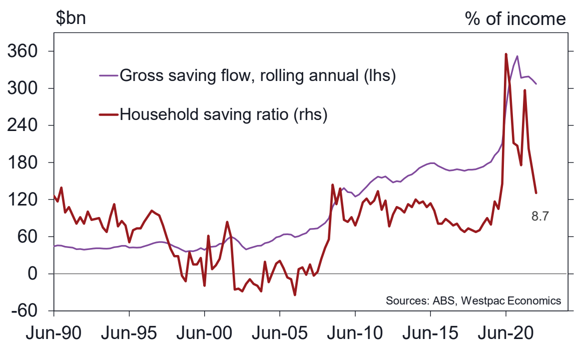
Australia: the growth mix



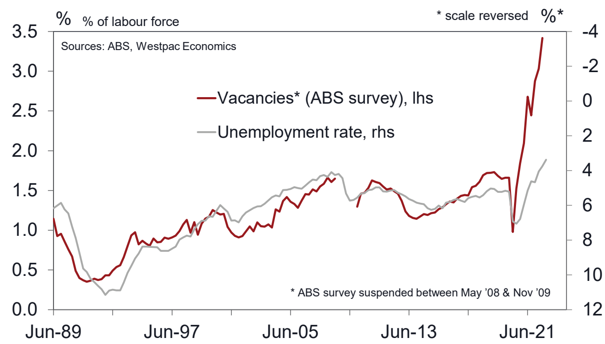
Australia: volatile path navigating covid



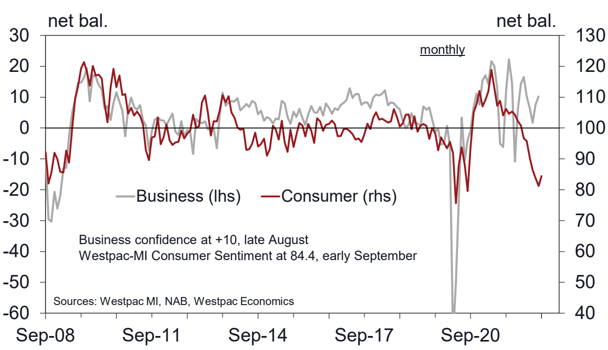
Household saving ratio and gross saving flow



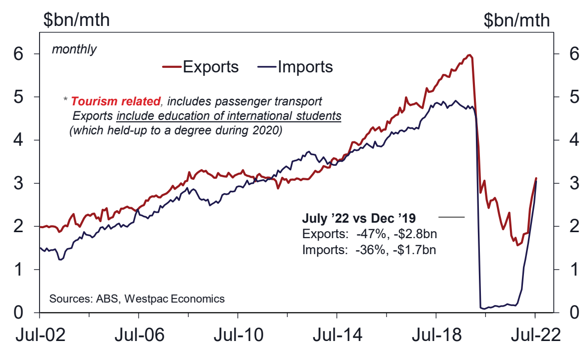
Job vacancies aplenty



Confidence: consumers and businesses

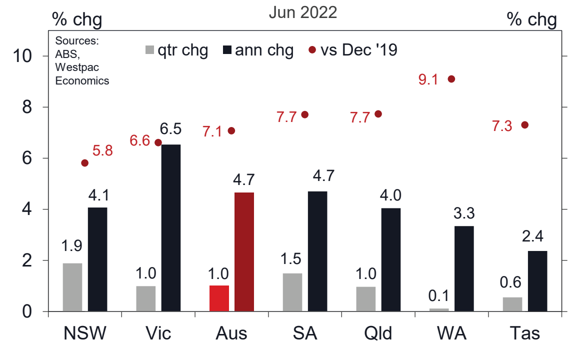


International tourism sharp rebound on reopening



Reopening, led by NSW and Victoria ...

Final domestic demand: across the states



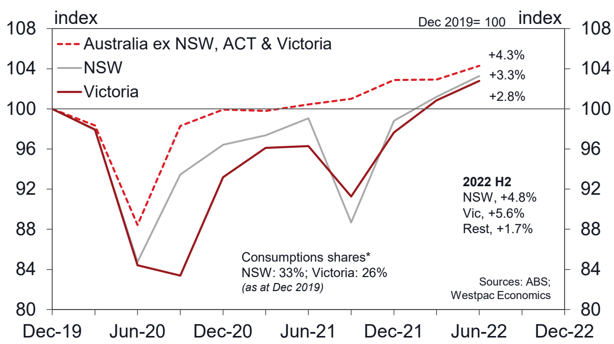
In the June quarter, robust economic conditions were evident across much of the nation - with the reopening effect, as well as the boost from earlier stimulus.

State demand grew by 1% in both Victoria and Qld, matching the national figure. NSW and SA outperformed in the period, with gains of 1.9% and 1.5% respectively.

WA and Tasmania have cooled, after sprinting ahead, up 0.1% and 0.6%. Relative to the end of 2019, pre-covid, remote fortress WA still leads the way, with activity higher by some 9.1% - well above the national figure of 7.1%. Qld and SA are next at +7.7%.

Broadening the focus to the first half of 2022, it is apparent that NSW and Victoria made up some lost ground, aided by the relaxation of covid restrictions - with state demand growth of 3.9% and 4.1%, respectively. For the rest of Australia (ex the ACT), state demand expanded by a more modest, but still solid, 1.9% over the half year.

Consumer spending per capita

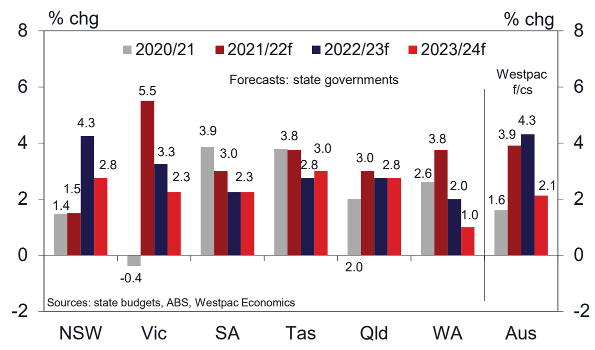


The catch-up effect on the reopening in NSW and Victoria is centred on consumers, who have been able to spend more freely as restrictions are eased. Consumer spending in NSW and Victoria, relative to pre-covid levels and on a per capita basis, is getting closer to that in the other states - albeit still trails a little - at +3.3%, +2.8% and +4.3%, respectively. There is the potential for some further catch-up in the September quarter.

The reopening is also around the opening of the national border. We now have lift-off on international travel and population growth is recovering. Service exports, tourism and education, across the states will benefit - but, equally, as more of us holiday abroad some spending dollars will flow overseas.

Over the first half of 2021, business equipment spending (+7.2%) was a key growth driver. Again, this included an element of post delta recovery (notably in NSW). Public investment (+5.6%) was also a growth driver over the half year - again, NSW was a stand-out, +9.6%, with the reopening.

Growth outlook by state: GSP



Recall that the state governments handed down their annual budgets, across May and June.

Understandably the contours of the forecast profile differ by state reflecting the varied covid experiences. NSW anticipates year average growth will be strongest in 2022/23. The other states (including Victoria) expect year average growth to slow between 2021/22 and 2022/23. Taken together, the weighted average view of the states is that growth holds steady at 3.25% for the two financial years. Growth slows to 2.1% in 2023/24.

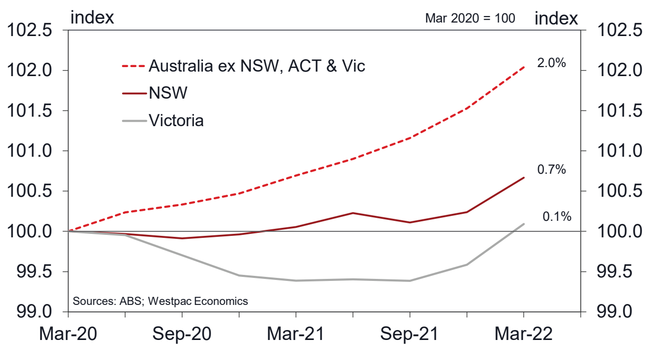
At the time we noted: “That outlook (for 2021/22 and 2022/23) appears to be on the cautious side - although given the uncertainties globally and domestically, some caution in framing government budgets is understandable.”

The 2021/22 outcome came in at 3.9%, stronger than the states expected, and Westpac expects growth of 3.8% for 2022/23.

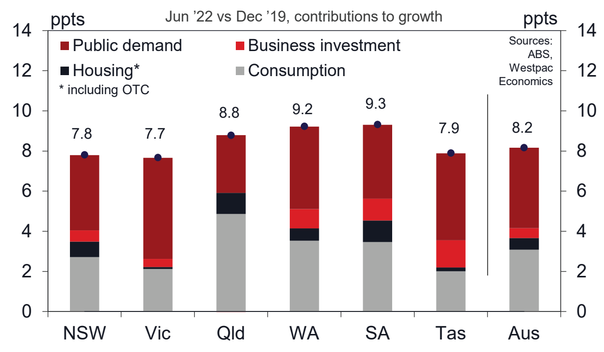
Prospects for 2023/24 year average growth have deteriorated materially, with the more aggressive RBA rate tightening cycle - which will impact conditions across the nation. Westpac expects growth to be 1.1% (downgraded from an expected 2.1% in June).

... rate hikes to impact all states in 2023

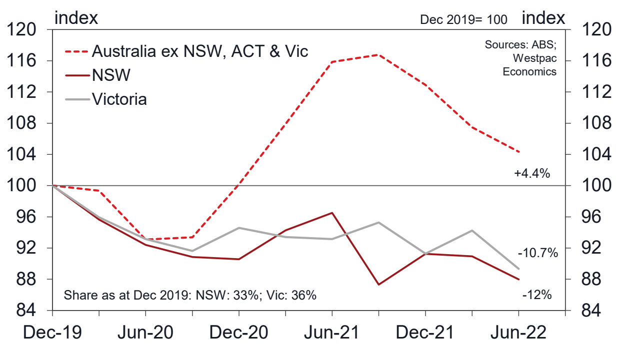
Population trends



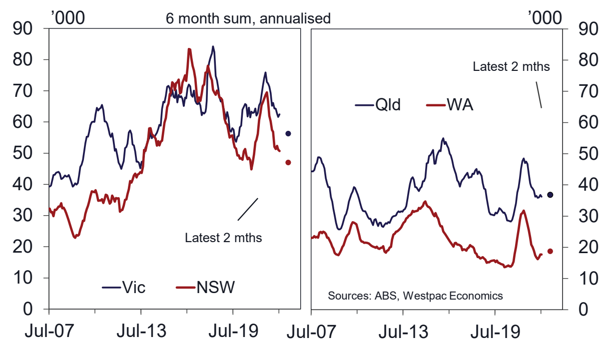
State final demand: vs pre covid



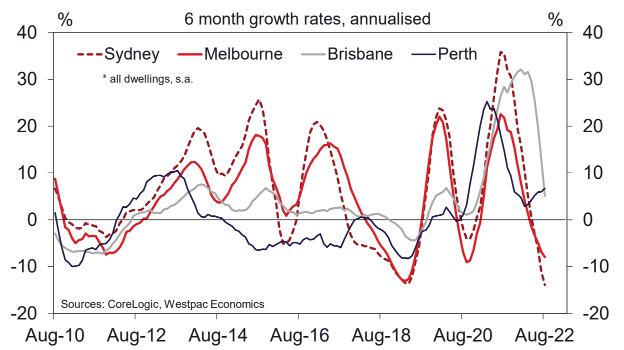
New home building activity



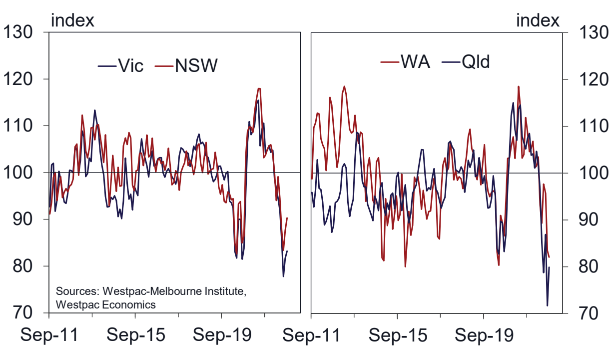
Dwelling approvals: post HomeBuilder let down



Dwelling prices: retreat as rates rise

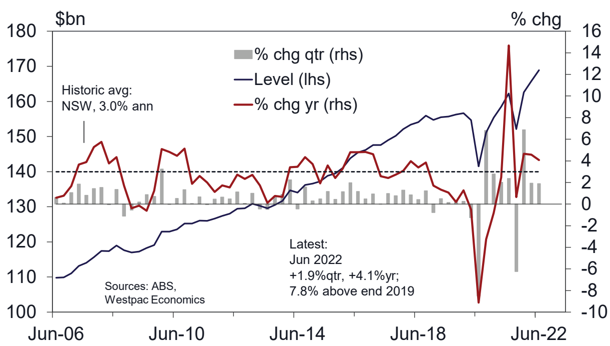


Consumer sentiment



Making up lost ground ...

NSW state final demand: a burst of activity



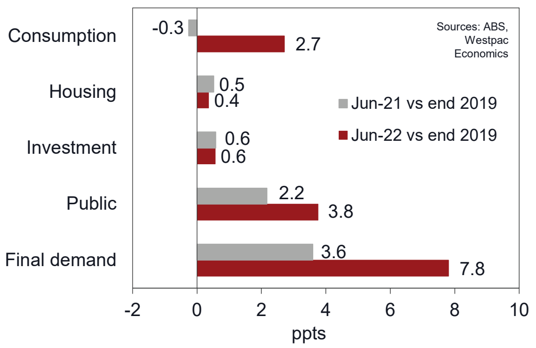
The NSW economy experienced a burst of activity over the first half of 2022 - centred on consumers - as it made up some lost ground following the extended lockdown of 2021.

State demand grew by 3.9% over the first half of this year (including outcomes of 1.9% for both Q1 and Q2). That was in line with the performance of Victoria over the half year, +4.1%, and twice the pace across the rest of Australia (ex ACT), of 1.9%.

While covid is still with us and sick leave levels are elevated at times, fewer covid related restrictions is enabling consumers to spend more freely, particularly on services. Consumer spending grew by 5.4% over the past two quarters, accounting for 3ppts of the 3.9% increase in state demand.

In the March quarter, consumer spending lifted to above pre-pandemic levels for the first time. By June it was 4.7% above that at end 2019 outcome. In per capita terms, spending is 3.3% above pre-pandemic levels - approaching the national figure (ex NSW, ACT and Victoria) of 4.3%.

NSW: contributions to state final demand

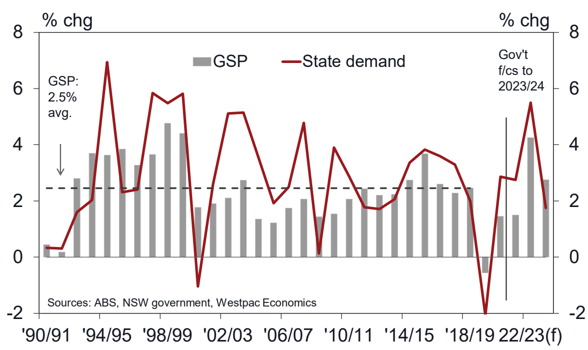


With the return towards greater normality, spending on hospitality in NSW jumped by 22% over the first half of this year - almost back to pre-pandemic levels, some 1.9% below. However, spending on transport & services and on the operation of vehicles are both well below pre-pandemic levels, -34% and -9.6%, with ongoing more flexible work arrangements for many.

New home building activity in NSW has been a significant underperformer - hit by labour and material shortages. Activity in the sector fell by 3.3% in the June quarter and is 12% below pre-pandemic levels. By contrast, renovation work rose by a further 6.7% over the past half year to be a staggering 38% above pre-pandemic levels - with NSW a clear stand-out.

Government spending remains a growth driver. Notably, public investment surged by 9.6% over the first half of 2022 - with a focus on transport infrastructure projects. The sector will continue to support activity going forward, given a large pipeline of work yet to be done.

NSW economic performance & outlook



The business mood is positive - at least for now - encouraged by this consumer led burst of activity. Rising demand, limited spare capacity, and generous tax incentives are encouraging businesses to invest. Equipment spending jumped by 9.3% in the June quarter, to be 16% above pre-pandemic levels.

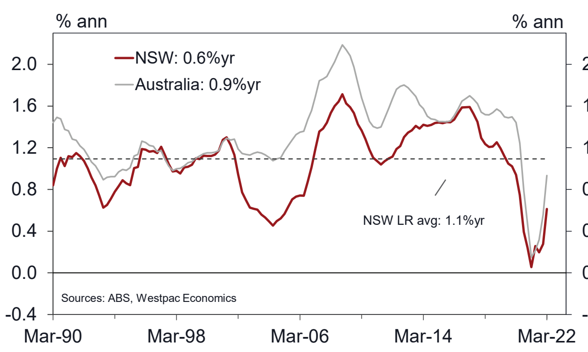
While conditions are positive currently, a sharp slowdown looms. Rapid fire interest rate increases from the RBA will - with a lag - dampen activity. The risk is that spending by the private sector slows to a sluggish growth pace in 2023.

The consumer mood in NSW is fragile, with Sentiment in the pessimistic zone at 90.3 in September. Although, that is well above the national reading of 84.4 and views on job security remain very positive - given the strength of the labour market, with the unemployment rate in the state at only 3.4%.

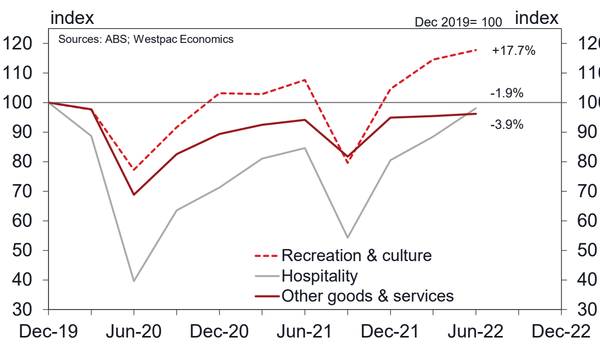
A cooling of the property market is underway. Sydney dwelling prices peaked in January, 25% above that in March 2022, retreating 7.5% by August, with further falls to come. The combination of high inflation, higher interest rates and falling property prices points to the emergence of subdued consumer spending growth during 2023.

... but sharp slowdown looms in 2023 as rate rises bite

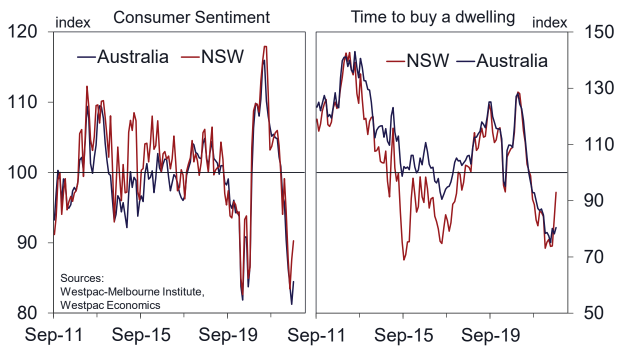
NSW population: a return to growth



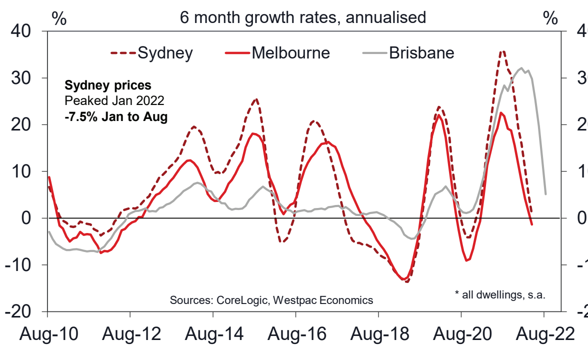
NSW: consumer spending trends



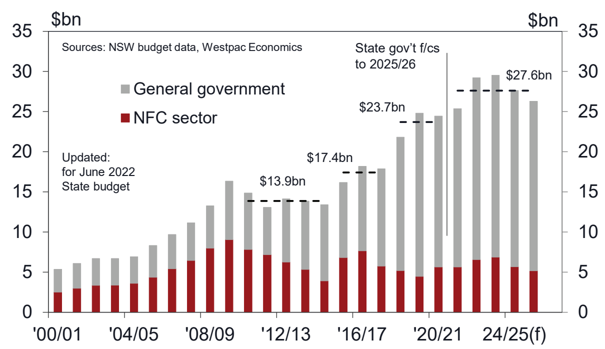
Consumer confidence: NSW off lows in Sep



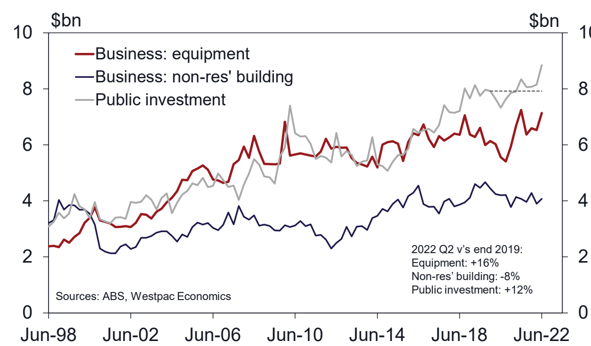
Sydney dwelling prices: a rapid retreat



NSW government capital expenditure

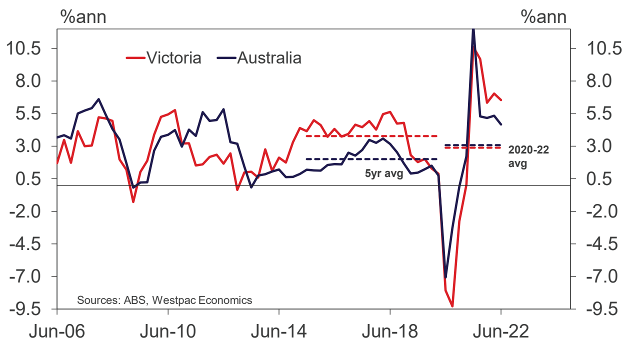


Investment cycles: a post delta lift in Q2



Post-delta catch-up largely over ...

Victorian demand: post-delta rebound ends

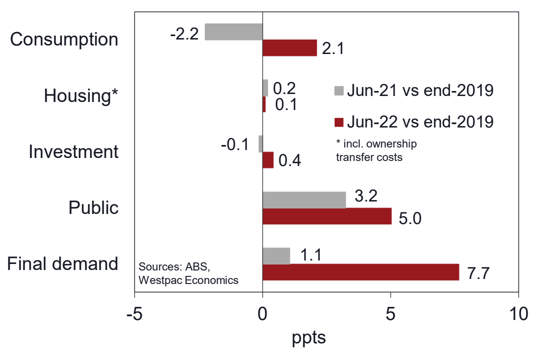


Vic's post-delta reopening rebound looks to have largely run its course. While virus disruptions continue to affect activity, hours worked especially, the broad picture through Q2 has been of moderate gains more in line with growth nationally rather than the strong outperformance through the March and Dec quarters.

As noted previously, how the Vic economy fares beyond this catch-up – and whether there is a return to the sustained outperformance seen over the five years prior to the pandemic – depends in large part on the extent to which the state's previously strong migration-driven population growth resumes. The picture here is starting to look more promising, net migration swinging back to a strong inflow in Q1, gains running ahead of official forecasts.

Against this, rising interest rates and a deepening housing downturn may be bigger negatives for the state given stretched affordability and higher average household debt levels.

Vic: contributions to state final demand

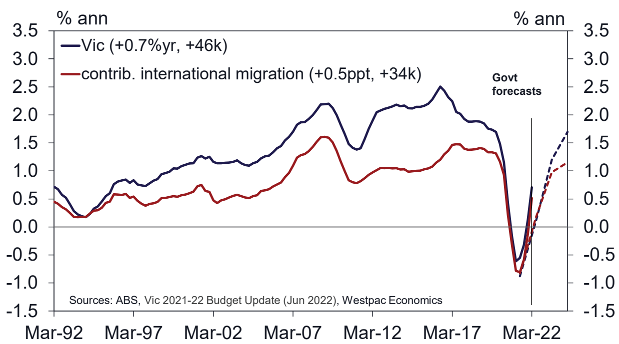


State final demand rose 1% in Q2, a step down on the 3.1% gain in Q1 and the 4.1% rise in Q4. Annual growth dipped to 6.5%yr, coming in above the 4.5% gain nationally. That said, annual growth rates are being tossed around by COVID disruptions in base periods. Comparing to pre-COVID levels in Q4 2019, Vic demand is up 7.7%, now only a touch behind the 8.2% gain seen nationally.

On the consumer, the Q2 detail still showed some residual boost from reopening but with the 2.3% gain in Vic more in line with the 2.2% rise nationally – suggesting the boost from reopening international borders was the main dynamic in the quarter rather than post delta rebounds.

Labour income gains have been a little more subdued in the state, up 2.2%yr compared to a 2.6% gain nationally. The gap looks to have widened a little in Q3 with employment growth moderating to around 1.9%yr vs 3.6%yr nationally.

Vic's population growth: promising rebound



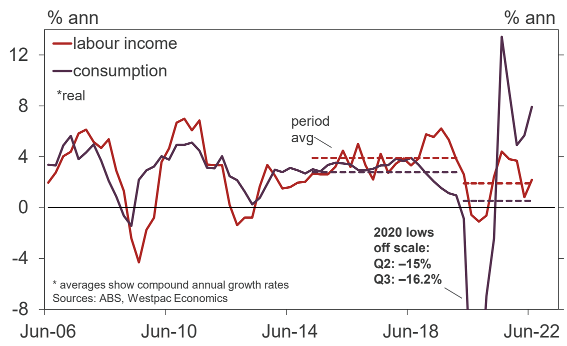
Supply shortages and COVID-related disruptions had a heavy impact on housing construction in Q2, new building posting a 5.2% drop and renovation work down 1.0%. While there will be some catch up in coming quarters, approvals point to a slowdown coming through as interest rate rises, higher building costs and the wider market downturn all start to bite.

The same disruptions look to have had a slight impact on non-residential building and infrastructure work in Q2 although a strong rise in equipment spending saw total business investment post a solid 2.4% gain. Labour shortages and historically high capacity utilisation levels are likely to encourage further investment. Vic's public investment has also been a notable source of support over the past year (+2.2%qtr; 8.7%yr).

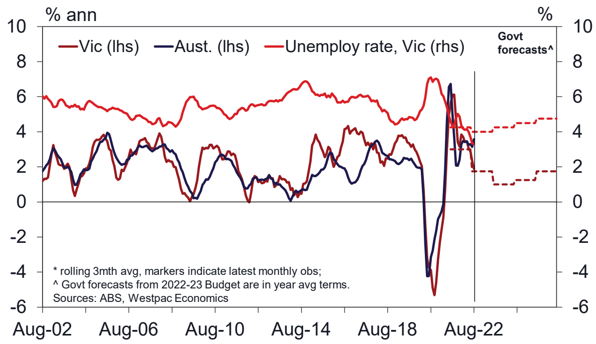
Population growth lifted back into positive in Q1 but at 0.7%yr is still well below the 2% pace seen prior to COVID. Student visa applications surged strongly through March-July, although a much milder gain in grants points to major processing delays.

... promising lift in migration but a troubling housing outlook

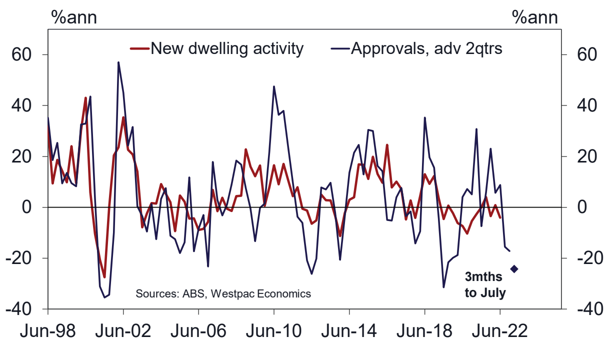
Vic households: incomes and spending



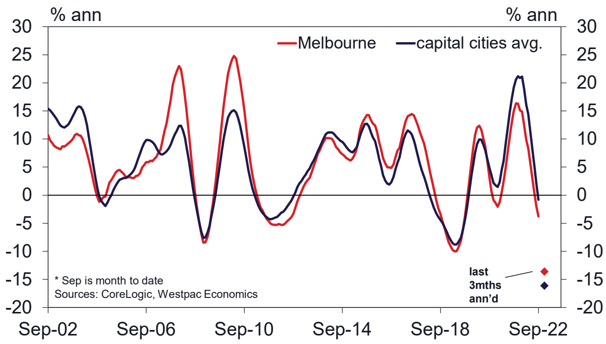
Victoria: jobs growth and unemployment



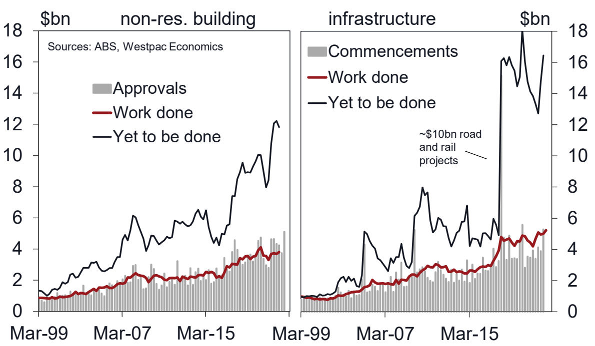
Vic housing construction



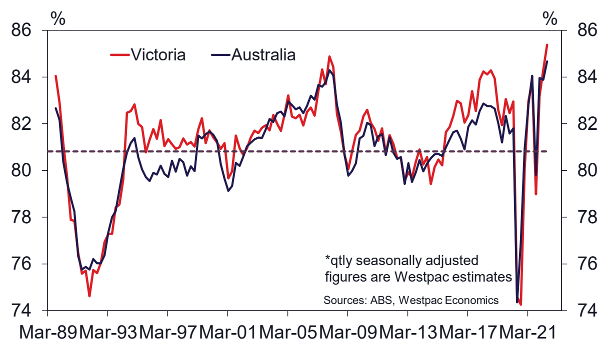
Melbourne house prices



Vic's non-res construction pipeline: cost rises

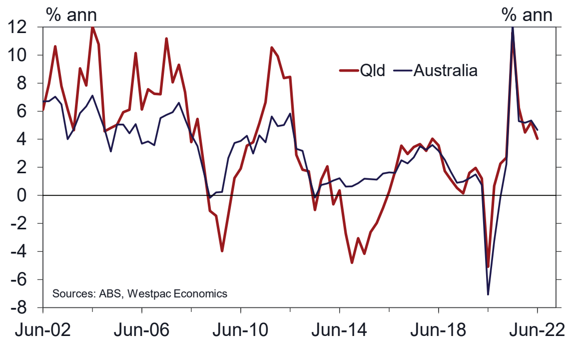


Capacity utilisation: Vic vs Australia



Strength in investment ...

Qld: state demand resilient through disruptions



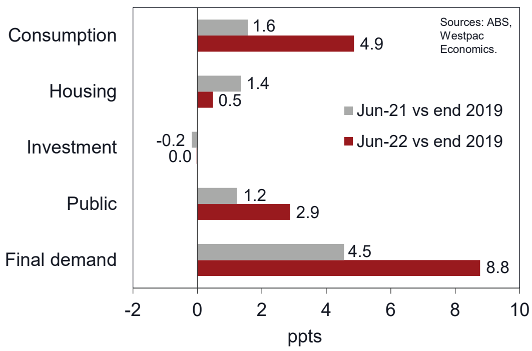
Queensland continued to show robust momentum in Q2 2022, state demand rising 1.0% in the three months to June to be 4.0% higher over the year.

Household consumption was the main driver, lifting 2.2% in Q2. Travel-related categories such as recreation, hospitality and transport services saw strong gains as household's took advantage of fewer weather/virus disruptions over the period.

The public sector was less supportive in Q2 (+0.1%), the lift in public investment (+1.1%qtr) on defence spending being offset by weaker public consumption (-0.1%qtr) after Q1's flood relief.

Although business investment was robust in Q2 (+1.1%qtr), it still lags the broader recovery, having not added to growth since December 2019. By type of investment, gains in equipment (+4.9%yr) and non-residential investment (+3.3%yr) have been largely offset by declines in engineering construction (-4.4%yr).

Qld: contributions to state final demand

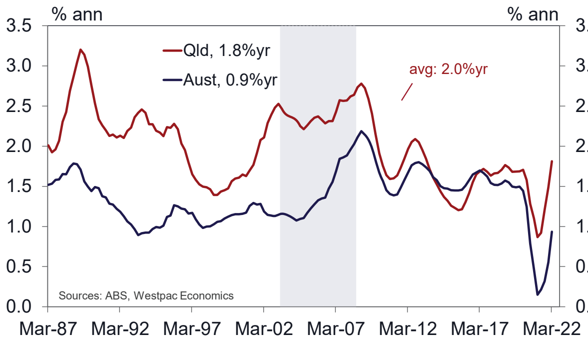


Dwelling construction has been a major drag on Qld's state growth. New housing construction and renovations experienced persistent and significant declines over the year (-15.9%yr and -11.8%yr respectively) on lower approvals, providing clear evidence that Qld's home building cycle is well past it's peak.

Regarding house prices, Qld's property market has begun to experience an abrupt turnaround. As discussed in our latest Housing Pulse, the RBA's rapid tightening cycle has seen turnover begin to decline and housing sentiment fall lower, house prices having now declined 2.3% in Qld over the three months to August.

Importantly, Qld's housing market is distinguished by an extremely tight supply-demand balance, which should see Brisbane's house prices little changed in 2022, followed by a relatively mild 6% decline in 2023 - a much more favourable outlook than for NSW and Vic.

Pop. growth rebound above national average



Also constructive to the outlook, Qld is a clear front-runner in the population growth recovery. At 1.8%yr in March, it is double the national average of 0.9%yr. Net interstate migration, predominately from NSW and partly from Vic, continues to be the main driver over the year, though the recovery in overseas migration looks to be well underway.

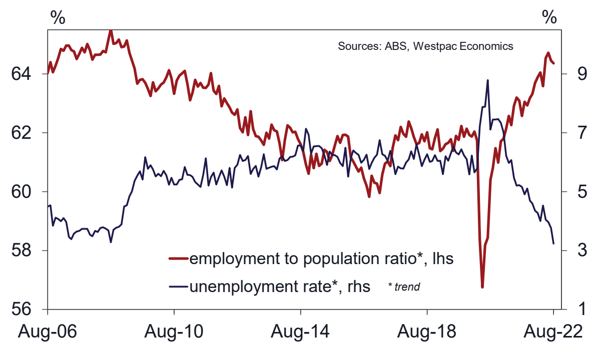
Given the progressive return to pre-pandemic rates of international migration and the state's relatively attractive housing outlook, on balance, Qld's near-term economic outlook is positive, albeit fragile as rate hikes begin to impact.

To provide a robust foundation for healthy growth in state demand, investment across the states key sectors such as resources, agriculture and tourism is necessary.

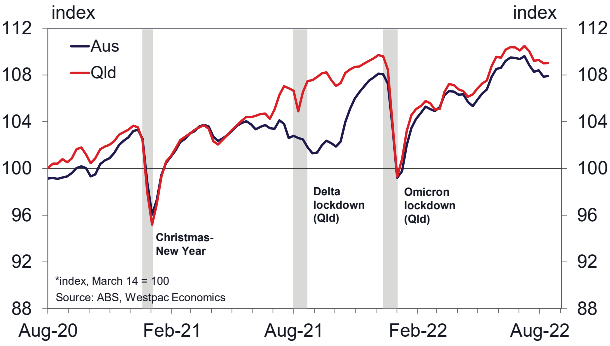
However, to prove sustainable, the investment being undertaken needs to broaden across new industry, to grow and diversify job creation and household income.

… foundational for medium term success

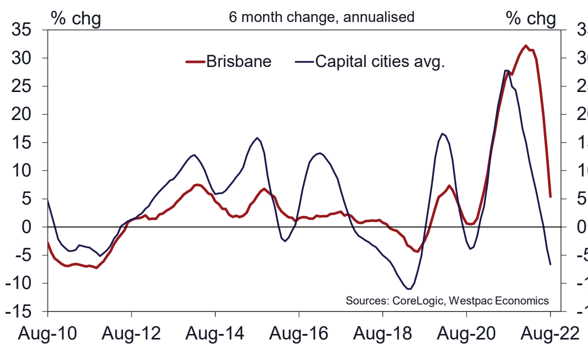
Qld labour market in robust health



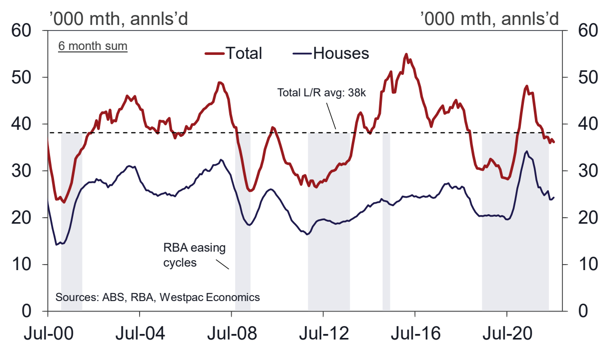
Payrolls: Qld continues to outperform



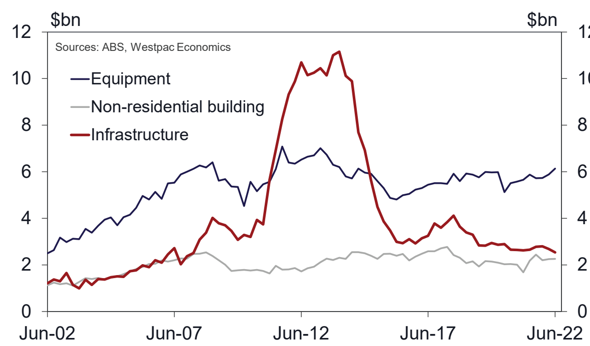
Brisbane housing market correction underway



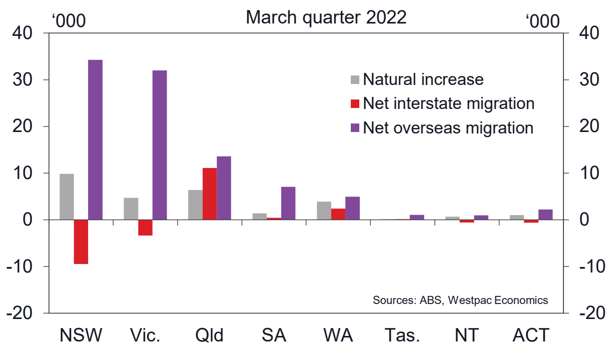
Dwelling approvals: supply limiting new pipeline



Qld business investment has nascent strength

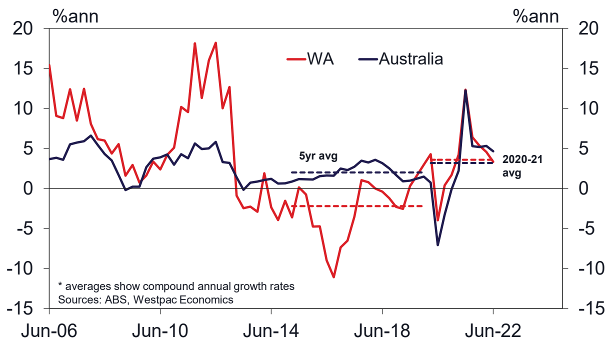


Promising return of overseas migration



Gains moderate …

State final demand: WA vs Australia

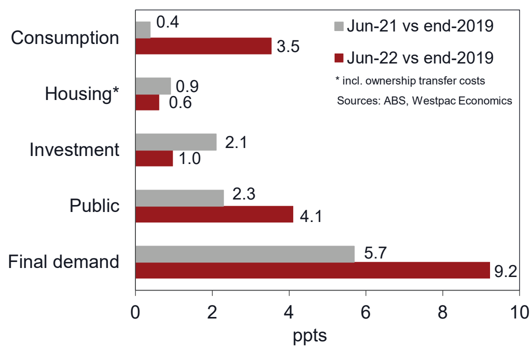


WA's mild and brief pandemic disruptions in 2020 and 2021 mean the reopening dynamics driving conditions elsewhere are less of a factor. As such, the state may be a pointer to how conditions may evolve once these dynamics have played out in the east.

That said, WA, as always, has its own idiosyncrasies. Currently, the key points of distinction look to be: buoyant, but volatile, conditions in the mining sector; a very large pipeline of residential building set for a sharp run-off (but a somewhat firmer house price situation); an extremely tight labour market; and what looks to be a milder lift in net migration inflows.

The state's large mining sector is a particularly important wildcard. Despite relatively high prices, mining investment remains dormant. That is probably just as well given the state's already badly stretched capacity and acute labour shortages. A lift in mining investment would be difficult to sustain.

WA: contributions to state final demand

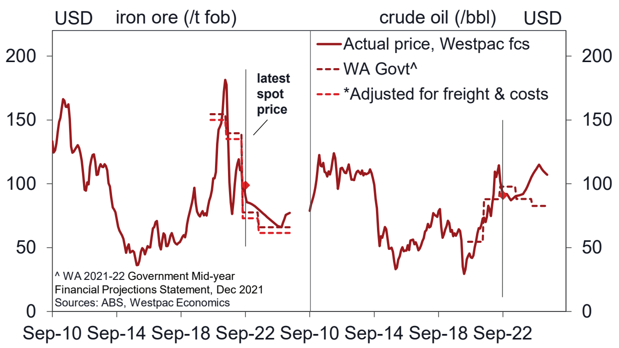


State final demand basically stalled flat in Q2, annual growth also coming in a touch under the national pace (3.3%yr vs 4.7%yr). That said, a milder pandemic means cumulative gains have been considerably stronger, WA up 9.2% compared to December 2019, compared to an 8.2% rise nationally.

Consumer spending posted a relatively subdued 1.4% gain, reflecting the absence of domestic reopening tailwinds, but with some support coming from the opening of external borders. Labour incomes have shown strong gains over the last year, up over 4% in real, inflation adjusted terms.

This solid gain was offset by more mixed performances for other demand components with notable declines for housing construction (–2%), business investment (–1.2%) and public demand (–0.9%). Data on total hours worked suggest disruptions from COVID-related sickness were a factor, and that this pattern extended into early July-August.

Commodity prices: iron ore & crude oil



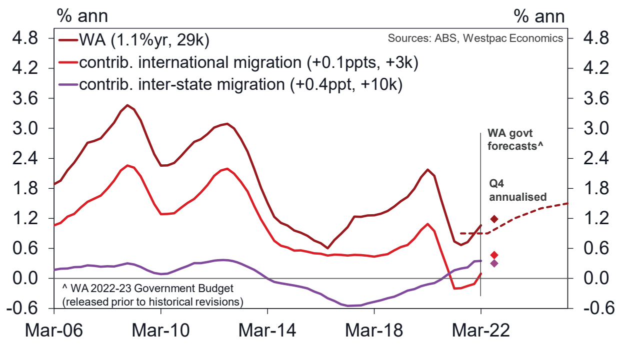
That said, some sectors are clearly moving into a downturn phase. Dwelling approvals have fallen sharply from last year's HomeBuilder-related peak – the pipeline of residential work now moving into what is likely to be a steep run-off, give or take delays.

A lift in business investment may well plug the gap. Investment declined 5.4% over the year to June but a variety of factors point to a likely lift. Labour supply is extremely tight, with just over 65k job vacancies and less than 48k unemployed left in the state. Capacity utilisation is also operating at acute levels.

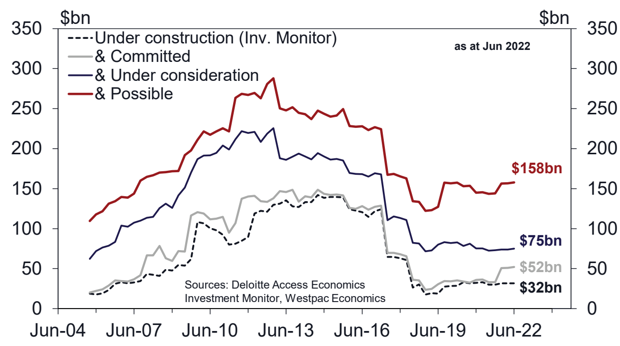
For the mining sector, high prices are an added incentive to invest, although the last three months has seen a sharp pull-back in iron ore and some cooling in oil prices. Uncertainty around the impact of global efforts to reduce carbon emissions are a clear inhibiting factor in many segments – although they should also be a major positive for resources required to drive the transition to 'net zero'.

… mining sector a major wildcard

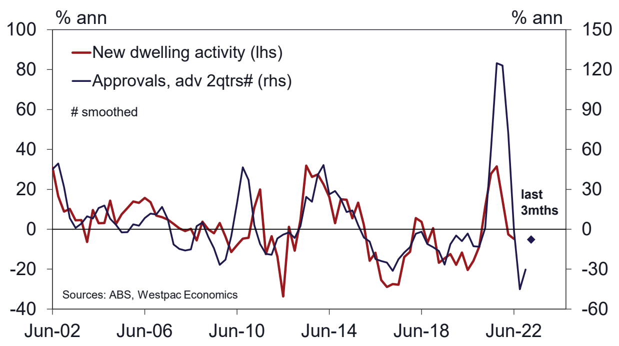
WA's population growth



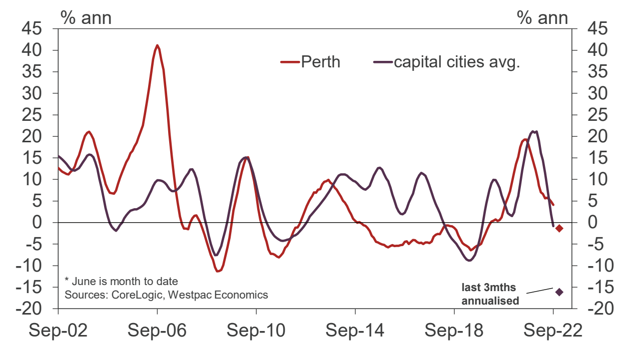
WA's project pipeline: slight lift



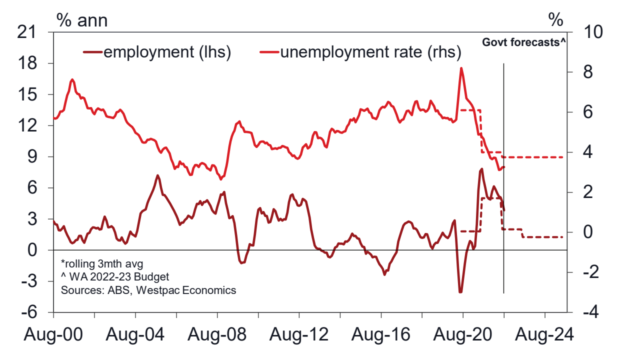
New dwelling inv. cycling big HomeBuilder surge



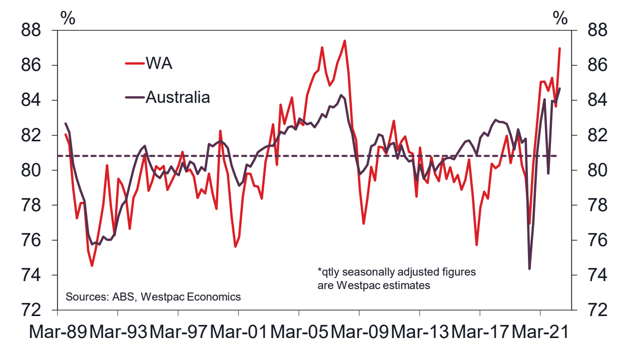
Perth house prices: less exposed to correction



WA labour market extremely tight

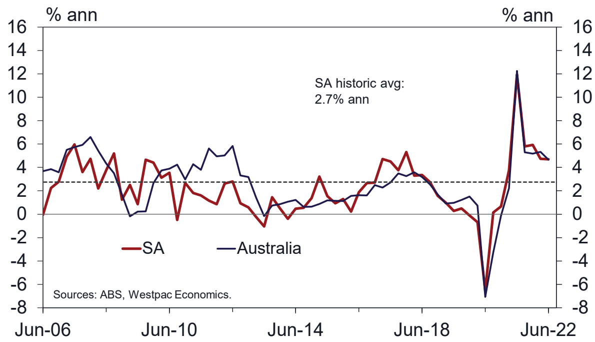


Capacity utilisation: WA vs Australia



Broad-based gains ...

State final demand well above pre-COVID level



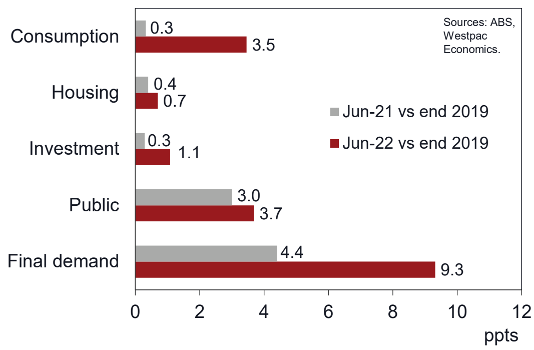
South Australia continued to forge ahead in Q2, state demand rising 1.5% to be up 4.7%yr. Underlying these results was broad-based momentum across the state's economy.

Growth in household consumption has been a key positive in SA (+1.5%qtr; +5.5%yr), which similar to Qld and WA has been buoyed by their insulation from the 'delta' outbreak back in Q3, as NSW and Vic continues playing 'catch-up'.

Meanwhile, public investment subtracted from growth (-2.1%qtr) though public consumption more than made up for this weakness, leaving public demand up 1.7%qtr/2.3%yr.

With respect to productivity, total business investment rose 1.0% in Q2 2022 to be up 7% versus June 2021. Underlying this result was considerable strength in non-residential construction (+21.9%yr), solid engineering work (+7.5%yr) and a marginal contribution from equipment spending (+1.7%yr).

SA: contributions to state final demand

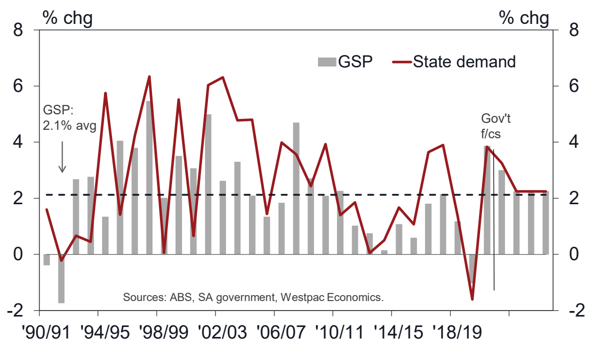


SA's housing market is bucking the wider trend, remaining the clear stand-out among the states, as evinced by: supportive new dwelling construction (+10.8%yr); elevated private detached housing approvals at 16.3% in the three months to July; and dwelling prices still tracking a stunning 21.8%yr, Adelaide experiencing its first monthly decline only in August.

It is important to recognise that, although the RBA's tightening cycle will continue to pressure South Australia's housing market into year-end, the state's strong fundamentals will provide key support. Indeed, an extremely tight supply-demand balance, alongside less stretched affordability, should see Adelaide dwelling prices hold out an impressive 8%yr gain in 2022, followed by a 6% decline in 2023 - a more mild correction relative to other states.

Also constructive to the outlook, the state's labour market is proving to be key a positive this year.

SA economic performance & outlook



Most notably, South Australia's unemployment rate fell under 4% in August - the first time in nearly 50 years. Driving this trend is strong and persistent employment growth, the share of the population employed having risen to a historic high of 60.7%, matching the peak during the 2000's commodity boom.

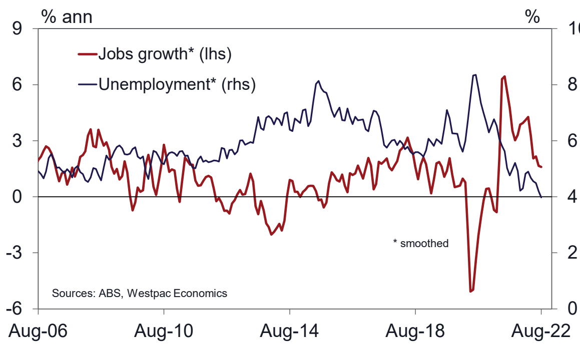
Of course, how tight the labour market has become is as much about the earlier weakness in population growth as it is the job creation seen over the past year.

It is promising to see a rebound in overseas migration on the border reopening, lifting the state's population growth to 0.8%yr in March, a fraction below the national figure of 0.9%.

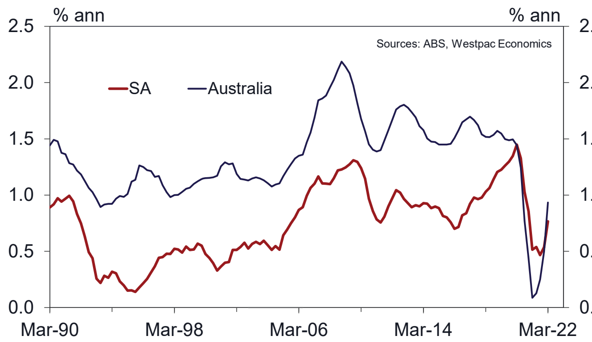
Therefore, as the housing market correction ensues and labour market pressures ease, robust investment across key industries such as energy; resources and health will be a key support over the medium-term.

... solid foundation for medium-term

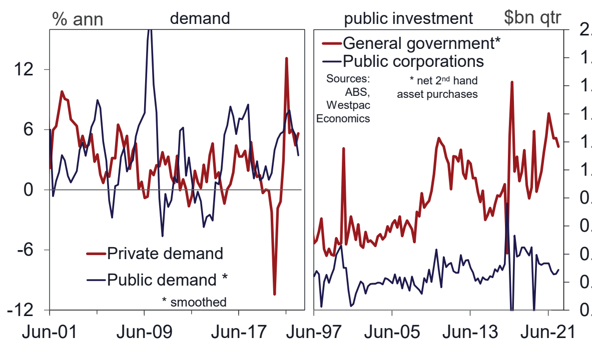
SA's labour market is tight



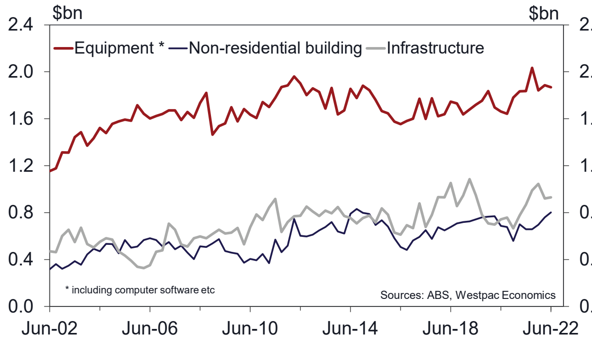
SA population growth off lows



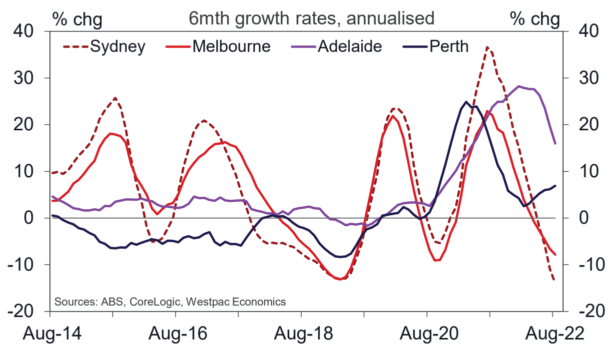
SA private sector momentum robust



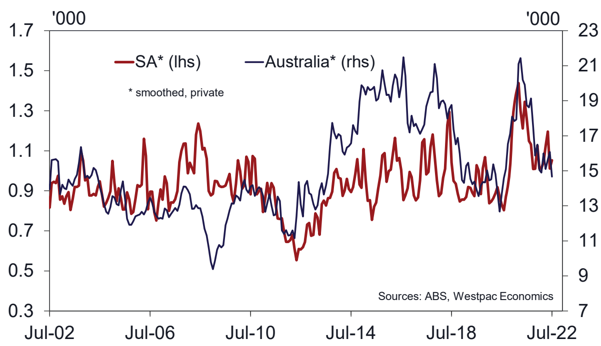
Business investment has strength



Home affordability in Adelaide's favour

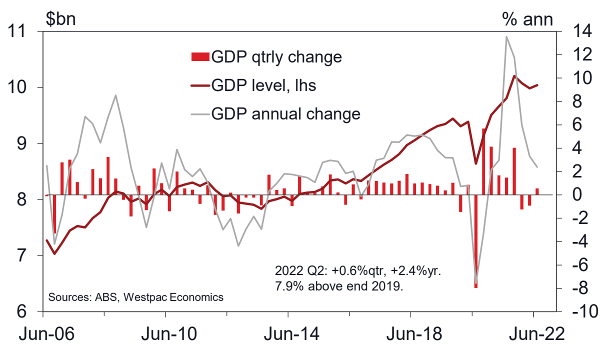


SA housing construction: pipeline positive



In transition ...

Tasmania: in transition

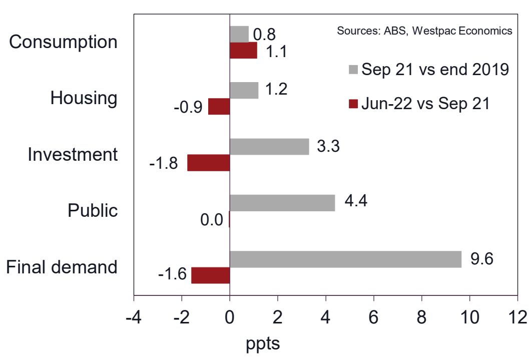


Tasmania's economy is transitioning away from the boost of earlier policy stimulus. State demand posted a 0.6% gain in the June quarter, but that represents only a partial rebound following declines of -1.2% in Q4 2021 and of -0.9% in Q1 2022.

As at September 2021, annual state demand growth was 11.3% and the level of activity was 9.6% above that at the end of 2019, prior to the pandemic. At that time, Tasmania was outperforming all other states - followed by daylight and then Qld (at 6.3%) and WA (at 6.1%). Tasmania benefited most from aggressive policy stimulus and fewer covid disruptions.

The let down from earlier stimulus is evident across housing, business equipment spending and public demand. By contrast, consumer spending exhibited resilience over the past three quarters, up by 2.1% - notwithstanding a 0.4% dip in the March quarter, associated with the omicron wave. The willingness of consumers to spend going forward, and draw down their savings buffer, is a key uncertainty for the outlook.

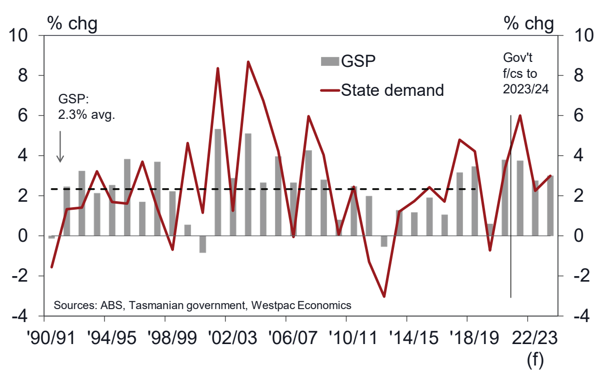
Tasmania: contributions to state demand



Home building activity is in a downturn after peaking in September 2021. Work declined by 18% over the past three quarters, including a 21% drop in new dwelling activity and a 15% fall in renovations. The level of new dwelling activity is currently still elevated, in line with the previous peak of 2018. From here, there is further downside - given the let down in approvals already evident and with the RBA's aggressive interest rate cycle, which has already undermined confidence in the sector in Tasmania (see chart opposite).

Businesses in Tasmania responded to generous investment tax incentives, going on an equipment spending spree - increasing by 104% between end 2019 and September 2021. Firms are still showing a willingness to invest, with the level of equipment spending in June above the peaks of 2011 and 2018 - albeit 29% down from the September 2021 high.

Tasmania economic performance & outlook



Recall that the Tasmanian government handed down the annual state budget on May 26. At the time, they expected state demand in the 2021/22 financial year to be 6% above that in 2020/21. The outcome is broadly in line with that, at 5.8%.

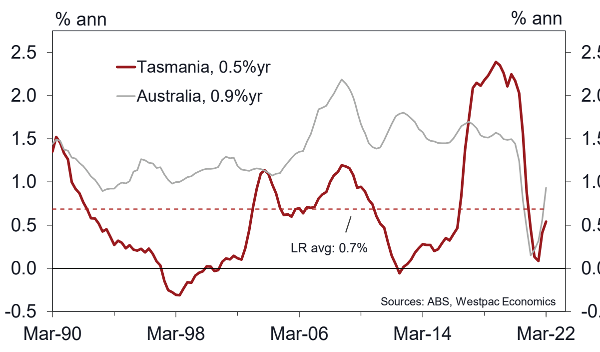
The state budget foreshadowed that state demand growth would slow sharply, to 2.25% for 2022/23. The risks to this appear to be skewed to the downside, given current momentum and a more aggressive than expected tightening cycle by the RBA.

The state budget papers expected the expansion to be driven by strong government expenditure, household consumption and increases in exports.

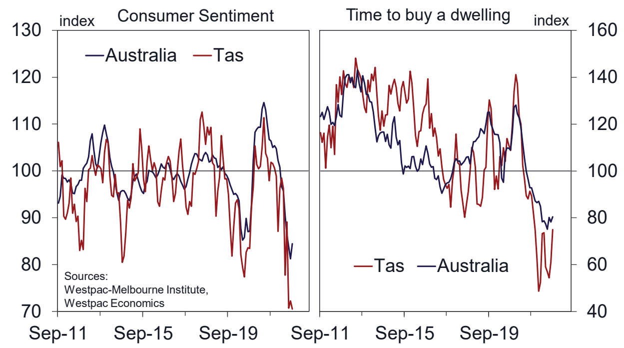
Certainly, the outlook for service exports is positive. The tourism and education sectors will be beneficiaries of the reopening of the national border, as well as increased domestic travel by those on the mainland. In terms of the exchange rate, the news is mixed - the Australian dollar is relatively weak against the US dollar, at around 66¢ of late, but elevated against many other currencies.

... service exports a key positive for 2023

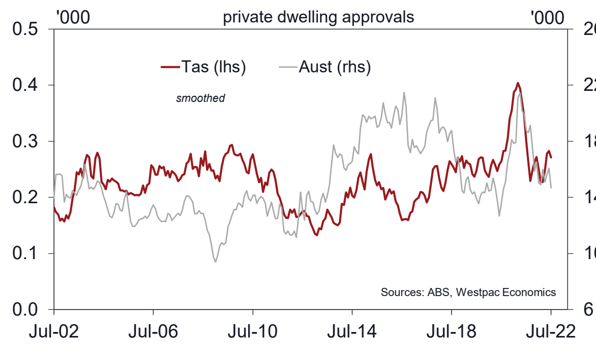
Tas population growth; bouncing back



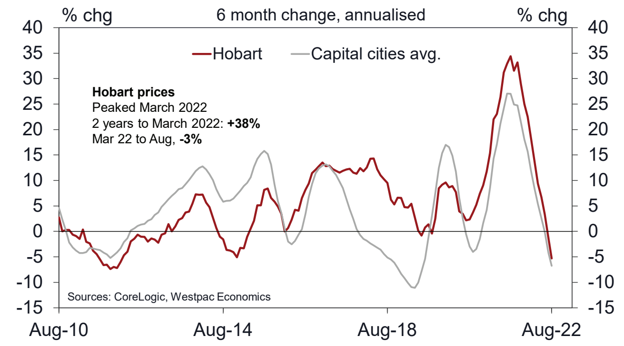
Consumer confidence



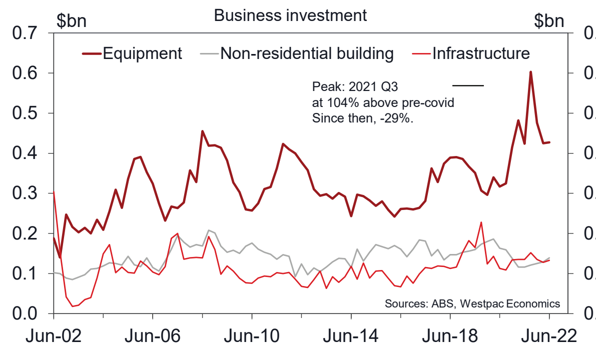
Dwelling approvals: post HomeBuilder let down



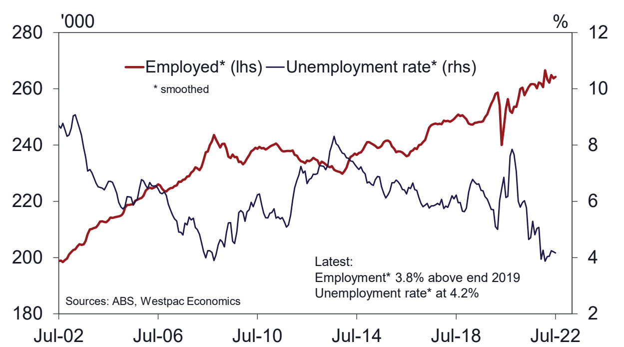
Hobart dwelling prices: down from peak



Equipment spending spree runs out of steam

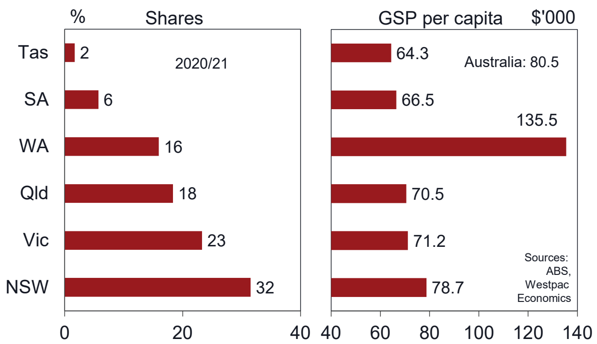


Tasmania: employment, consolidation in 2022

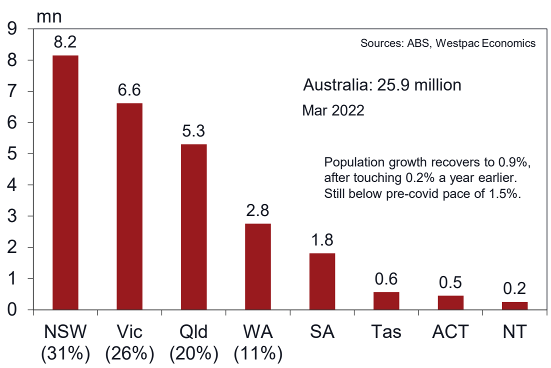


SUMMARY INDICATORS

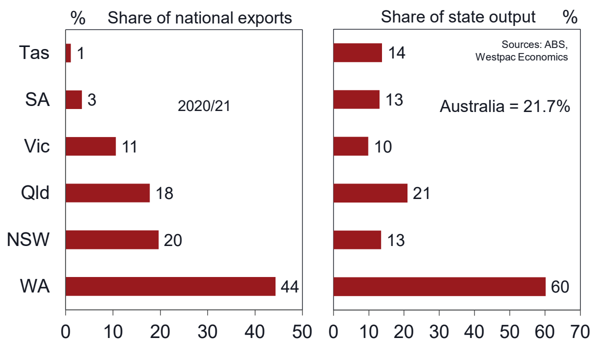
Gross State Product



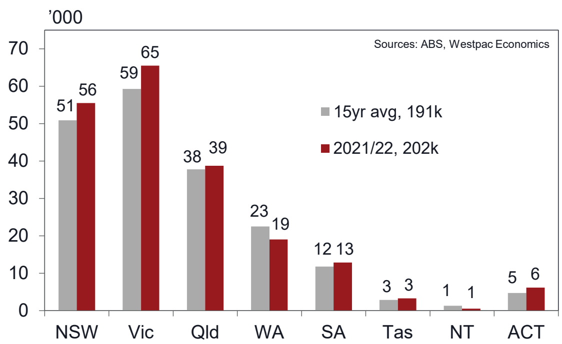
Population



Exports of goods & services



Dwelling approvals



Industry mix share of gross value add

	Australia	NSW	Vic	Qld	WA	SA	Tas	NT	ACT
Agriculture	2.6	1.9	2.4	2.9	2.1	5.6	11.2	3.7	0.1
Mining	10.6	2.3	1.1	11.0	42.5	3.6	4.0	25.6	0.1
Manufacturing	6.0	5.8	7.0	6.4	5.2	7.0	5.8	3.9	1.0
Construction	7.4	7.8	8.2	7.6	5.7	7.3	7.0	5.8	6.8
Transport, utilities	6.8	6.8	7.4	8.1	4.7	7.5	7.3	5.0	3.5
Wholesale, retail	8.8	9.6	10.5	8.6	5.4	10.2	7.7	6.3	4.7
Health, social assistance	8.2	7.6	8.8	9.2	5.5	11.0	13.9	8.4	9.5
Education	5.2	5.3	5.8	5.5	3.2	6.4	6.2	5.1	6.0
Household services	4.6	4.8	4.5	5.3	3.4	5.0	4.9	5.7	4.3
Finance	8.2	11.4	10.2	5.9	3.6	7.2	5.1	2.4	2.8
Business services	16.3	20.9	18.4	14.1	9.5	12.7	9.8	7.0	20.4
Public administration	5.9	5.1	5.6	6.0	3.4	6.4	7.1	12.4	32.0
Ownership of dwellings	9.4	10.8	10.0	9.4	5.7	9.9	10.1	8.6	9.0

Sources: ABS, Westpac Economics. For the 2020/21 financial year.

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Things you should know.

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