STATE ECONOMIC OVERVIEW

MARCH 2022

National Australia Bank

Photo **Mai Thai**

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STATE ECONOMIC OVERVIEW

National Australia Bank

COVID disruptions have continued but State economies have been resilient and labour markets are strong

The COVID-19 pandemic has remained a source of disruption, although impacts remain relatively transitory. There was a strong recovery in the states affected by lockdowns in Q3 2021 (NSW, Vic., ACT). Similarly, the large fall in hours worked in January due to the large number of people isolating as a result of the Omicron wave was largely reversed in February in NSW, Vic., SA, Tas and Qld (but with a fall in WA as their wave started later).

Even with the ongoing disruptions, state final demand in Q4 2021, was clearly above its pre-COVID-19 level. With population growth weak, this has been accompanied by a tightening in labour markets across the country. Unemployment rates have been trending down and for all states/territories are at or below their pre-pandemic level. Job vacancies are elevated with business reporting it is difficult to find suitable labour.

Looking forward, we expect ongoing strength in overall consumption spending (albeit slightly disrupted in Q1 by Omicron and floods). Business investment as well as government spending should support growth in the near term, while trade is expected to be a small drag on growth. However, we do expect to see a rebalancing in goods and services spending, as well as a recovery in services trade (education and tourism).

Growth should be broad-based across the state and territories, albeit with some re-balancing back to NSW and Vic. whose recovery has been relatively sluggish so far. This should also lead to further falls in the unemployment rate, with the national unemployment rate expected to reach 3.5% by mid-2022.

The recovery in activity has also been accompanied by rising inflation pressures; this has been broad based but particularly so in Perth, Brisbane, Darwin and Hobart (with higher inflation broadly seen in areas with stronger growth over the pandemic). We expect these pressures to persist in the near-term taking the year-ended rate (nationally) to 3.7% by mid-year and for headline CPI inflation to 4.2% by Q3 2022 before easing. The lift in actual and expected inflation, alongside an increasingly tight labour market, leads us to expect that the RBA will start lifting the cash rate in August and this will be followed by further increases out to 2024.

NAB growth forecasts for the states & territories

	Gross State Product (y/y%)			
	19-20	20-21	21-22f	22-23f
NSW	-0.6	1.4	3.1	4.4
VIC	0.1	-0.4	3.4	4.9
QLD	-0.6	2.0	4.0	3.8
SA	-1.0	3.9	3.1	3.1
WA	1.0	2.6	4.3	1.4
TAS	0.6	3.8	4.9	2.7
NT	6.0	-0.6	2.6	4.9
ACT	3.7	2.8	2.8	4.4
Australia	**0.0**	**1.5**	**3.5**	**3.8**

This will have implications for housing markets across the country as it is one of the more interest sensitive sectors. Dwelling investment has come off its recent peaks in all states and building approvals (ex ACT) have been trending down. However, a large pipeline of work in most states should sustain a solid level of activity going forward. Dwelling price growth has started to slow although it remains strong in Brisbane, Adelaide and Hobart. We expect price growth to eventually turn negative across all the capital cities, with falls of around 10% to end-2023 nationally but with larger falls in Sydney & Melbourne.

Business conditions and confidence strengthened in February as the Omicron virus wave eased and the late 2021 momentum was regained. Most states shared in the upswing, except WA and Tas where conditions fell. In trend terms, conditions across the states are clustered around their historical average (but with WA and Tas a bit above). Capacity utilisation is generally at very high levels across the states as are future capex intentions, suggesting a positive outlook for business investment.

Population growth remained weak over 2021 (to Q3) reflecting negative net overseas migration, with Vic., NT & ACT seeing a population decline in this period (and Tas basically unchanged). Population growth in Qld and WA has held up better, supported by interstate arrivals. The re-opening of international borders has led to a lift in net arrivals to Australia which, as it gathers steam, should boost the education and tourism sectors (particularly important for NSW and Vic. given the importance of both sectors pre-COVID).

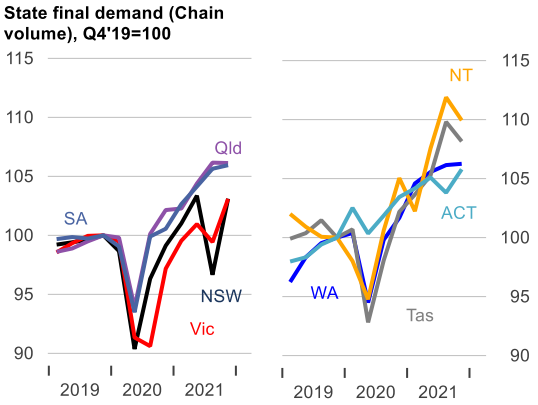
Agriculture remains a positive story as the combination of high prices and another strong winter crop in 2021-22 boosts farm incomes.

The key risks for the economy have shifted significantly over the past 6 months or so. Lockdowns and border closures appear to now be in the rear-view mirror and the key uncertainty is how quickly spending patterns, international services trade and population growth normalises. In addition, the Russian/Ukraine war poses risks. It led to a lift commodity prices which could benefit some regions, but higher prices will weigh on incomes in other parts of the country (and rising fuel/fertiliser prices will affect business costs). While affected prices are very volatile they have come off their peaks and the duration/extent of the conflict is unknown.

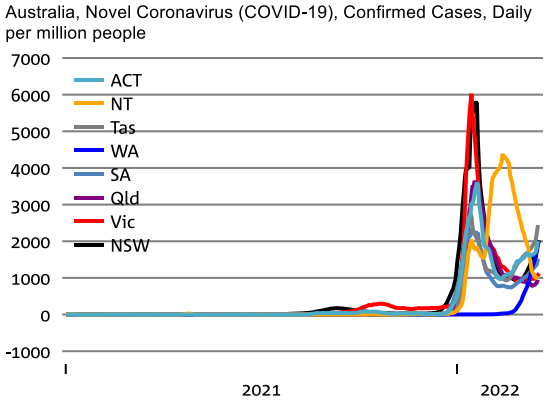
STATE OVERVIEW – SOME KEY DEVELOPMENTS

State demand clearly above pre-COVID-19 levels, but COVID still causing disruptions in early 2022. Population growth & service exports well down but internat. border re-opening a boost.

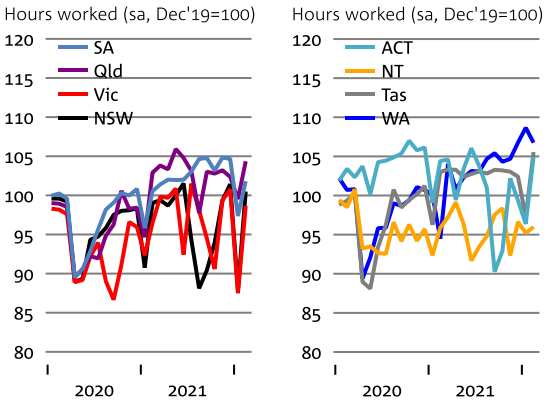
Strong rebound from lockdowns in Q4 for Vic and NSW, but pandemic recovery still more advanced elsewhere



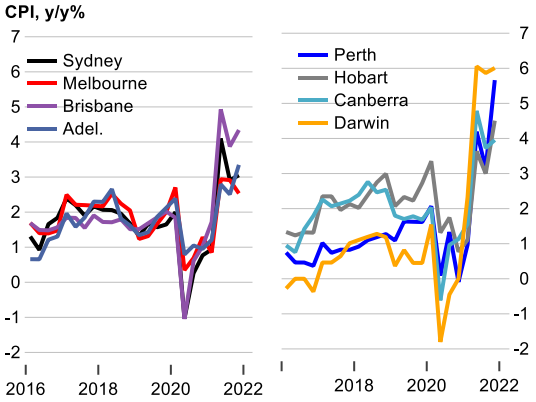
Early 2022 COVID wave caused business disruptions; WA now in midst of wave but picking up again in other states



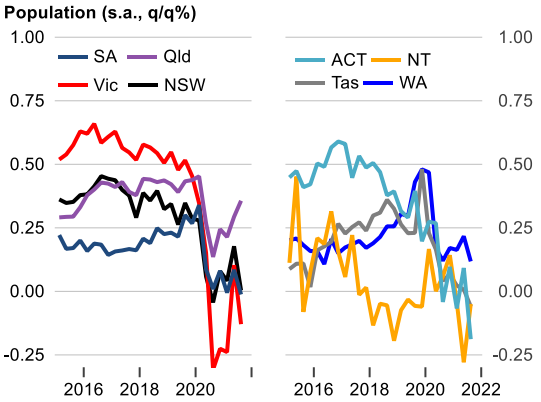
Resulting falls in hours worked in some states around same extent seen in lockdown periods but strong Feb rebound



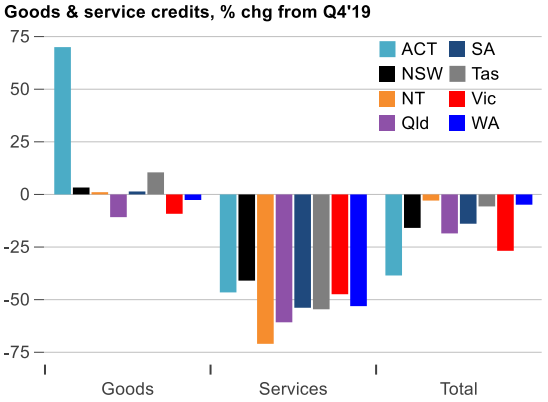
States with strongest activity (relative to pre-pandemic) generally experiencing higher inflation



Population growth weak in Q3 2021 with several states losing people; Qld, WA holding up best. Internat. border re-opening a possible boost in 2022…



…also to exports which were still well below pre-COVID-19 levels in 2021 Q4 with services (travel) hardest hit



Sources: ABS, Department of Health, Macrobond, Refinitiv, NAB

STATE BY STATE

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New South Wales

The NSW economy has rebounded strongly since the Delta lockdown came to an end in November with activity recovering quickly and the labour market seeing further gains.

As was the case in previous lockdowns, the hit to activity came mostly through household consumption (down 10.8% in Q3) – but this saw a significant rebound in Q4. Overall, state final demand (SFD) was up 6.7% in Q4 (4.0% y/y) to be only just short of the level seen pre-Delta and 3.1% above pre-COVID levels.

Retail spending edged up further in January despite the Omicron outbreak and business conditions in the NAB Survey remained around average at +6 index points in trend terms in February, indicating that momentum should carry through to 2022. Still, recent flooding will impact on Q1, and elevated inflation of 3.1% y/y in Sydney could also weigh on consumption if sustained.

The strong rebound has carried over to the labour market, with the unemployment rate falling to 3.7% in February. With labour demand strong, employment should continue to grow which could see unemployment fall further. Wage growth is also gradually picking up, at 0.7% in Q4 (2.4% y/y).

Sydney's housing market has boomed with property prices up 22.4% y/y to February 2022, although price growth has slowed in recent months and we expect prices to eventually fall by more than 10% as interest rates begin to rise. Dwelling investment has also been subdued as lockdowns and labour and materials constraints have taken a toll, although Q4 saw an increase as lockdowns lifted.

Victoria

There was a hit to activity from the Delta outbreak in Q3 of 2021 – albeit less severe than in NSW – but its economy rebounded strongly in Q4.

SFD fell 1.4% in Q3 before rising 3.7% in Q4 on the back of a rebound in consumption, putting Victoria's SFD back above its pre-COVID level.

Effects of the virus on activity in the new year appear to have been limited, with retail spending up 2.5% in January and business conditions in the NAB Survey above average at +6 index points in February. The return of major events, reopening of international borders, and strong pipeline of public and private investment should support the Victorian economy through 2022.

In terms of the labour market, the Omicron outbreak saw hours worked fall in January but there was a strong rebound in February with employment growing and the unemployment rate down to 4.2%. Victoria's population was still contracting in Q3 but is likely now growing with borders open, and with job vacancies at record levels employment should keep rising over coming months.

Wage growth remains moderate in the state, at 0.5% in Q4 (2.3% y/y) but should gradually pick up. Inflation is also more modest in Melbourne than the other capital cities, at 2.5% y/y in Q4.

Melbourne dwelling prices were up 12.5% y/y to February 2022. As in Sydney, we expect prices to moderate across 2022 and fall by more than 10% in 2023. Dwelling investment has remained below pre-COVID levels despite a large pipeline of work which should support activity.

Queensland

Queensland continued to weather the storm in 2021, growing solidly through much of the year despite border closures and virus outbreaks. SFD was flat in Q4 as falling investment offset a small rise in consumption, but was still up 3.9% y/y and 6.1% on pre-COVID levels.

Business conditions have remained fairly strong at +4 index points in trend terms, and while the state will see some impacts in Q1 from Omicron and the recent floods, the outlook for 2022 is strong particularly with both interstate and international borders now fully reopen – although how fast tourism returns remains uncertain.

Queensland's population continued to grow through 2021, up 0.4% in Q3. The labour market also continues to strengthen with unemployment down to 4.3% in February – not quite the low levels seen in some other states but impressive nonetheless. As the economy strengthens in 2022, there should be further employment gains. Wage growth has also picked up to 0.8% in Q4 (2.4% y/y).

Brisbane dwelling prices rose 29.7% over the past year, the fastest of any capital city. Price growth is now moderating and we expect a fall of around 6% through 2023. Dwelling investment in Queensland softened in Q4 but was still well above pre-COVID levels, especially when compared to the other eastern states.

South Australia

The SA economy performed strongly over 2021; SFD was up 5.4% to be 5.9% above its pre--COVID level. Business conditions fell in January during the Omicron wave but rebounded in February. While the outlook remains positive, growth is likely to slow in 2022 given the state's recovery is well advanced.

Household consumption growth was robust in Q4 '21 after a lockdown affected Q3. Indications for early 2022 are mixed - retail sales rose strongly in January, while NAB spending data has been eased recently but the trend still appears broadly positive.

Net exports were a drag over 2021 as export volumes fell. International tourism remains moribund and overseas student numbers

continue to fall but international border re-opening should assist these sectors.

SA had another solid winter crop in 2021-22 and agricultural prices have also been high.

After a period of rapid growth, dwelling investment fell towards end 2021. While building approvals are falling, a substantial pipeline of work should sustain a solid level of activity. Business investment, even with a fall in Q4, grew strongly over 2021 and capex intentions in NAB's business survey are high; similarly the state government plans to increase its investment spending.

SA's labour market has performed well with the unemployment rate trending down, although at 5.0% in February it was the highest of any state. A high level of job vacancies and an above average NAB Survey employment reading suggests that momentum remains positive.

Western Australia

With major COVID outbreaks and lockdowns largely avoided through 2021, WA's economy has continued to grow – albeit at a slowing pace with border closures in place until very recently. While reopening will likely mean more cases, the state is well positioned for 2022 with elevated commodity prices likely to provide an income boost.

SFD edged up 0.1% in Q4 as higher consumption was offset by falling public and private investment, to be 4.5% higher over the year and 6.3% up on pre-COVID levels.

WA businesses have consistently reported amongst the strongest conditions of any state since mid-2020, although confidence fell recently as border closures were extended and Omicron cases began to rise. How the state manages the current wave, and how consumers respond, will be important.

As in other states, WA's labour market is tight. The unemployment rate reached 4.1% in February and participation is almost 70%, close to a record high. In the Q4 NAB Business Survey, 60% of WA firms reported that finding suitable labour is a significant constraint on output, more than in any other state.

Still, wage growth remains fairly modest at 0.5% in Q4 (2.0% y/y). However, consumers in Perth have faced some of the strongest rates of inflation in the country with prices rising 5.7% y/y to Q4.

The Russia/Ukraine conflict has caused commodity prices to spike, with elevated oil and gas prices potentially boosting incomes in WA's energy sector. WA's agriculture sector is also well positioned with a strong winter grain crop and elevated agricultural commodity prices providing further support.

Tasmania

A strong middle of the year for Tasmania was offset somewhat in Q4 as falling investment saw state final demand slip 1.5% q/q. Still, over the year SFD grew 5.8% to be 8.2% larger than it was prior to COVID, a standout among the states.

Business conditions have remained strong into the new year according to the NAB Survey, and retail spending rose in January. With the state border open since December, an inflow of tourism is likely to support the economy in 2022.

Population is also growing and Hobart has seen some of the strongest house price growth in the country, though this should moderate as elsewhere.

Tasmania's labour market has also continued to strengthen with unemployment down to 3.9% in February to be among the lowest across the states. With a tight labour market, wage growth reached 3.0% in Q4 (y/y), the fastest of any state.

Northern Territory

Reduced public sector spending and the impact of local lockdowns on consumption saw SFD fall 1.8% in Q4 in the NT, but the territory's economy still grew 4.7% over the year. In a steady start to 2022, retail spending rose through December and January.

Both private and public investment were considerably higher across the past year as infrastructure and defence projects were undertaken alongside some new mining construction and equipment investment.

The territory's population fell slightly through the middle of 2021 but should start to stabilise. The labour market has also remained strong with the unemployment rate down to 3.5% in February.

ACT

State final demand rebounded strongly in Q4 (+1.9% q/q) from the lockdown affected Q3 (-1.2% q/q). Relative to its pre-pandemic level SFD is up 5.8%. This mainly reflects public sector demand, with consumption and, in particular, dwelling investment below their end-2019 levels. That said, in contrast to other states, dwelling approvals have risen since around mid-2021. Dwelling price growth has been solid but it appears to be slowing.

On a positive note, business investment has strengthened after falling to a low level at end 2020/early 2021. The unemployment rate in February (3.0%) was back to around its pre-COVID level and is the lowest of any state/territory.

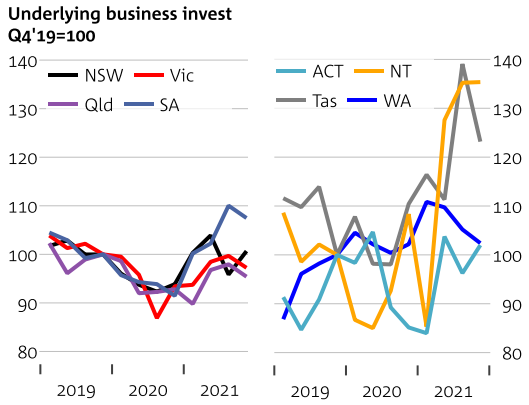
Lockdown caused the population to fall in Q3 but the re-opening of the border should see this begin to turn around with the return of students in 2022 to also provide support.

BUSINESS SECTOR

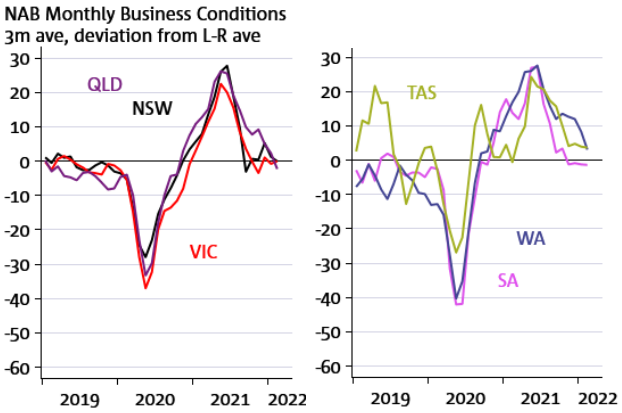
Business conditions have rebounded strongly and the investment outlook has brightened

National Australia Bank

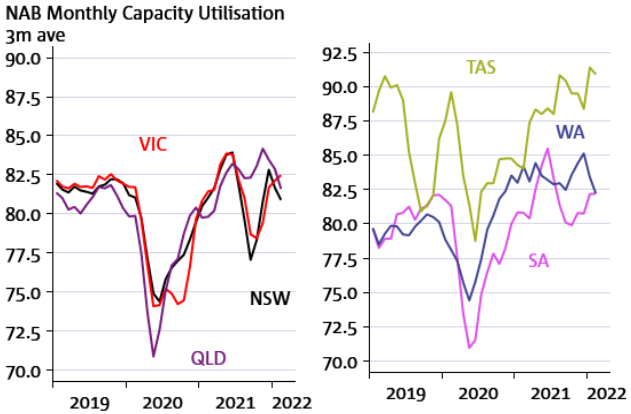
Business investment has recovered, particularly in NT, Tas but also the other states apart from Vic and Qld



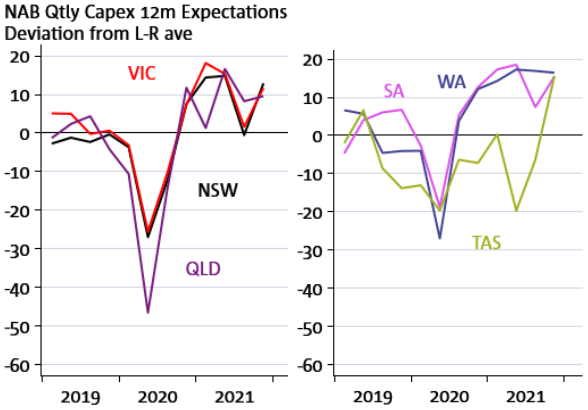
Despite the disruptions from the Delta and Omicron virus waves, business conditions have remained above or around the long-run average across all states



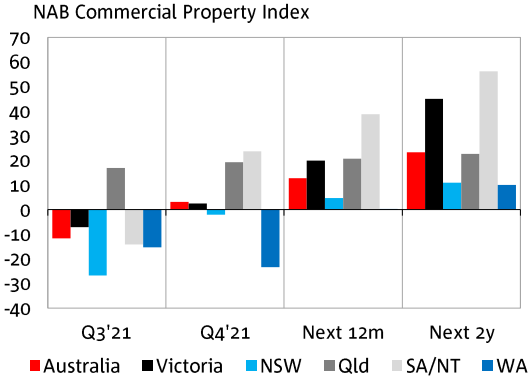
Capacity utilisation has recovered from lockdowns in Vic and NSW and is generally at very high levels across the states, particularly in Tasmania



Investment expectations were high across 2021 for the mainland states, and all states finished 2021 with a strong outlook

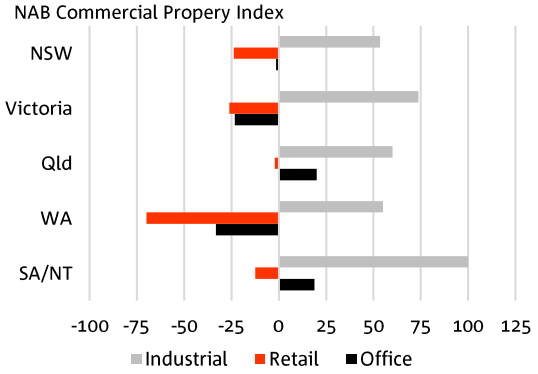


Commercial property sentiment improved in Q1 outside of WA which remains weak; conditions are expected to improve



Industrial properties strongest sector in all states while retail weak; office sentiment mixed – weak in WA and Vic but Qld/SA/NT more positive

(Q4 2021 NAB Commercial Property Survey)



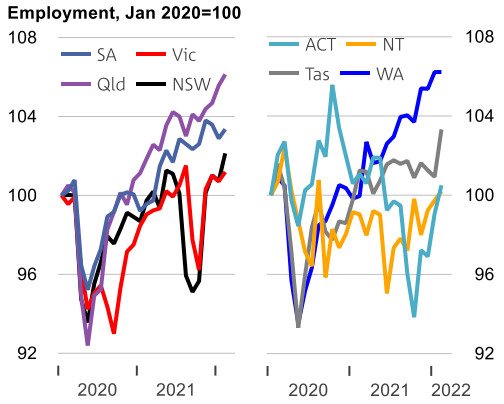
Sources: ABS, Macrobond, NAB

LABOUR MARKET

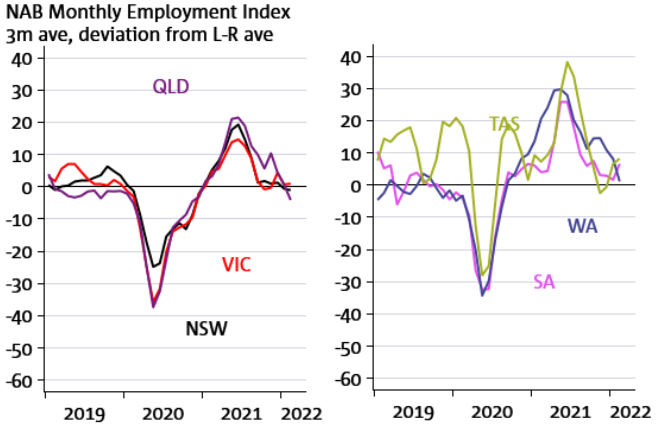
Labour markets are very tight in most states and territories

National Australia Bank

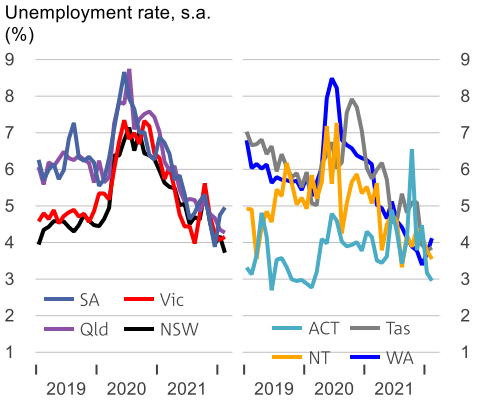
Wide divergence in employment recovery – Qld, WA, SA in particular have been strong, while ACT & NT have struggled



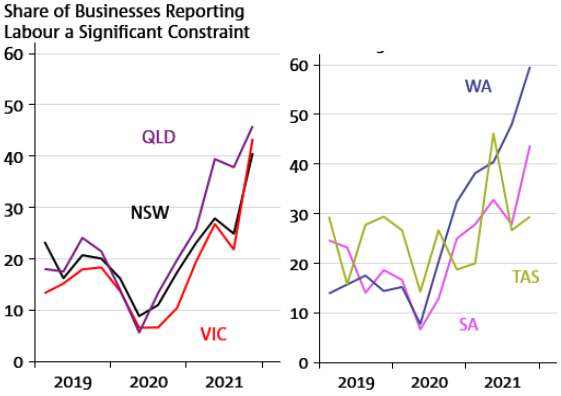
The NAB survey measure of job creation remains around the long-run average or higher in all states



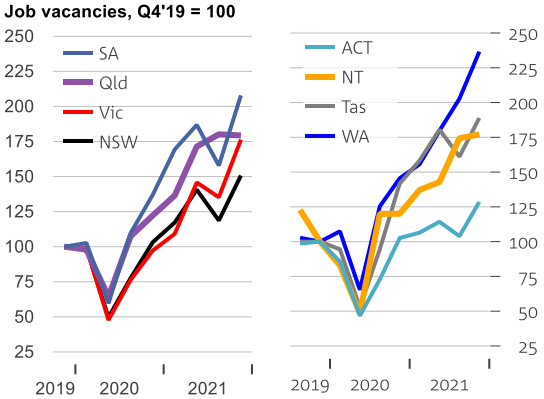
Unemployment rates have been trending – all jurisdictions below or, in the case of the ACT, around their pre-pandemic level



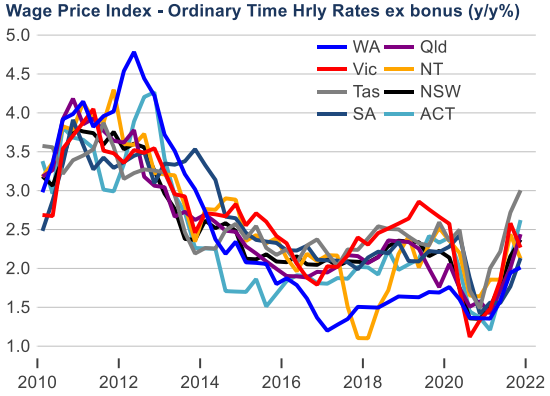
More firms than ever report that finding labour is a significant constraint on output, led by WA where 60% face labour constraints



Job vacancies generally at much higher levels than pre-COVID and still trending up



Wage growth generally back around pre-COVID level but modest strengthening in Q4 q/q not evident in all states/territories

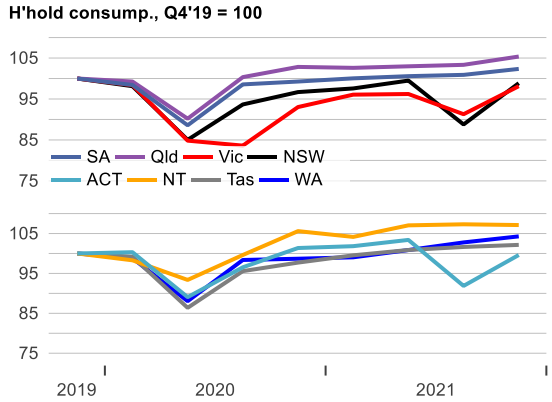


Sources: ABS, Macrobond, NAB

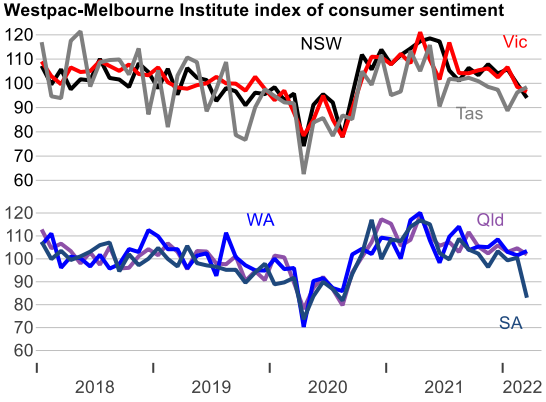
HOUSEHOLDS – CONSUMPTION

Consumption rebounded from lockdowns in Q4, early data for 2022 mixed but underlying trend remains positive

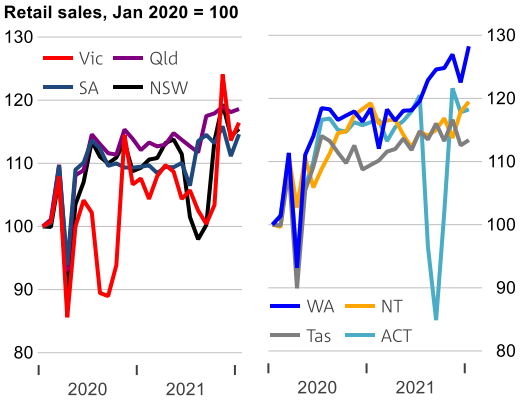
H'hold consumption in Q4 rebounded from long lockdowns in Vic, NSW & ACT; growth strong elsewhere other than NT



Consumer confidence has been easing but at or above pre-pandemic level outside of SA

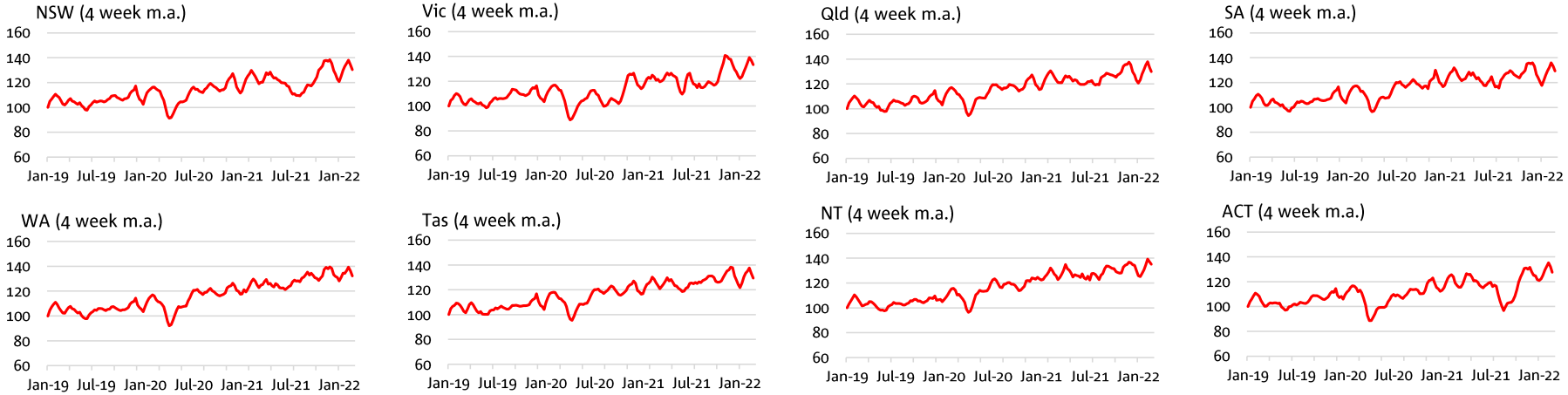


Retail sales – mainly goods consumption – have flattened out at a high level (except WA/NT where still moving higher)



NAB spending data has softened in early March although the underlying trends are still encouraging– likely reflecting technical parameters around seasonality from February to March; flooding in large areas of eastern Australia; and heightened COVID-19 concerns in Western Australia

(data to 12 March '22, 4 week moving average; data seasonally adjusted by applying monthly seasonal factors to weekly data ending in that month)

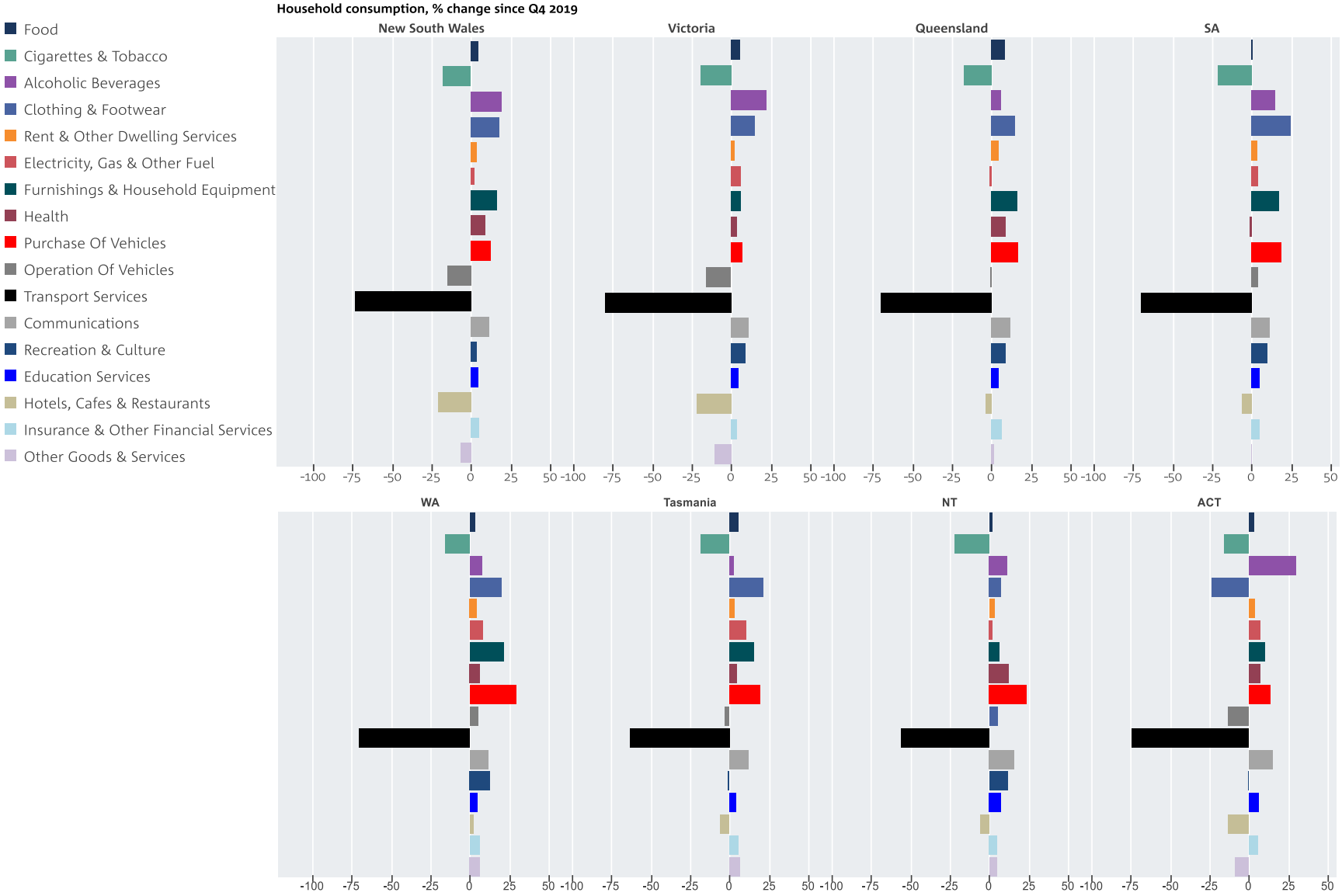


Sources: ABS, CoreLogic, NAB

* See https://business.nab.com.au/nab-economics-data-insights-week-ending-12-march-2022-52191/ for more detail

HOUSEHOLDS – CONSUMPTION DETAIL

Consumption recovery remains mixed across sectors with enduring weakness in transport services, as well as hotels, cafes & restaurants (hospitality). With lockdowns still in place early in Q4, hospitality and vehicle operations and other goods & services consumption weakest in NSW, VIC and ACT relative to pre-pandemic level

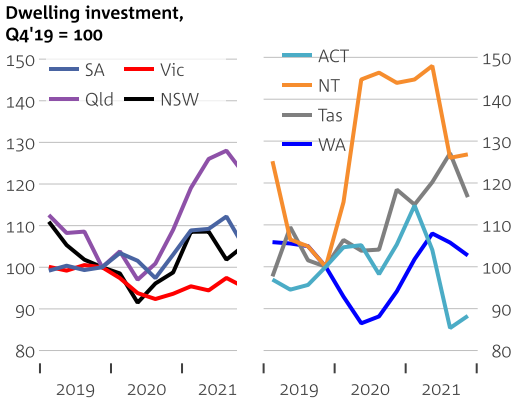


Source: ABS, Macrobond

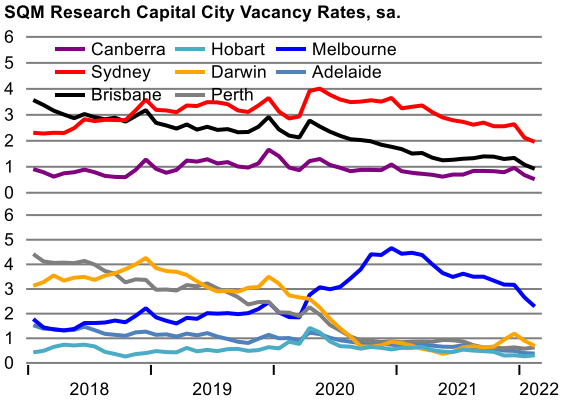
HOUSEHOLDS – HOUSING MARKET

Housing markets showing signs of peaking with approvals coming off and price growth slowing

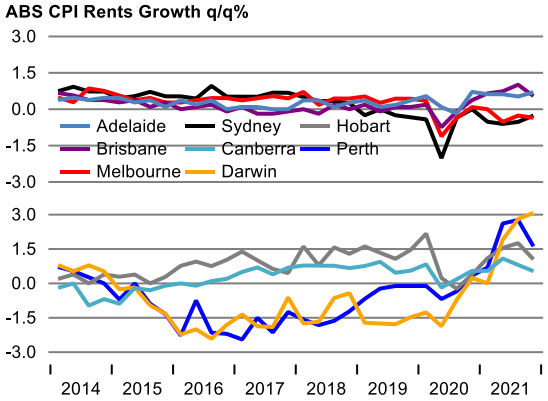
Dwelling investment softened in Q4 except in NSW and ACT where there was a post-lockdown boost. Above pre-pandemic level except in Vic and ACT.



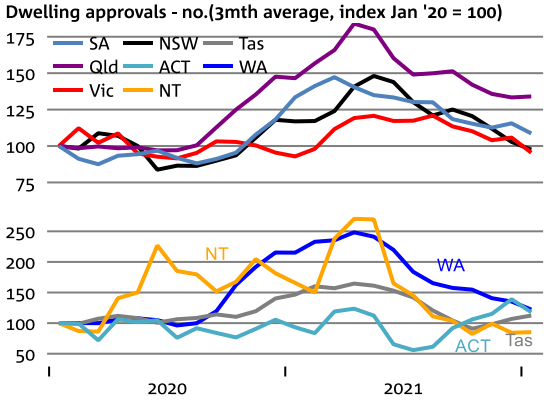
Vacancy rates still trending down – only Vic above pre-pandemic level.

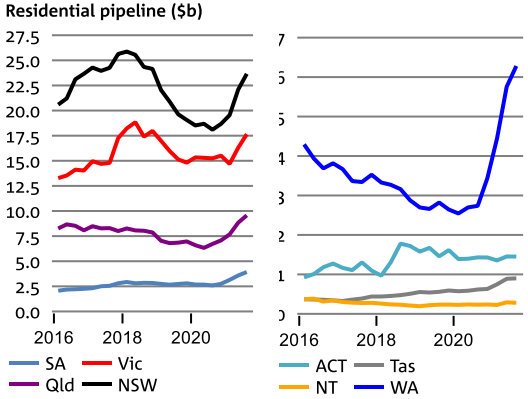


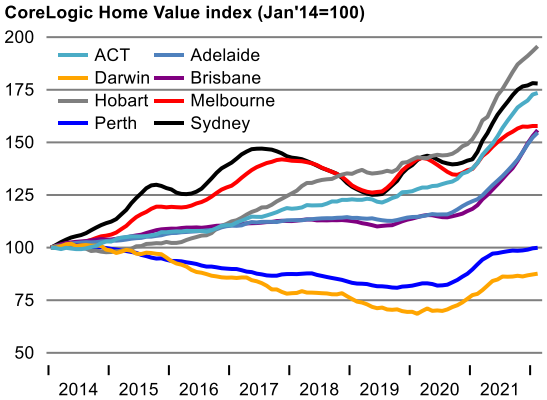
Rents growth strengthened (from pre-COVID levels) in some capital cities but this may have peaked



Building approvals have come off almost across the board – end of HomeBuilder early 2021, rising fixed mortgage rates, weak population growth – but still a large pipeline of work. House price growth slowing, albeit still strong in Brisbane, Adelaide & Hobart; we are expecting a fall in house prices to start later this year and into 2023*





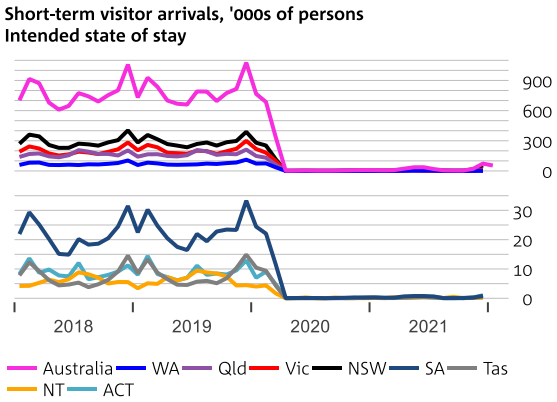


Sources: ABS, CoreLogic, NAB. *See the NAB Residential Property Survey Q4 2021

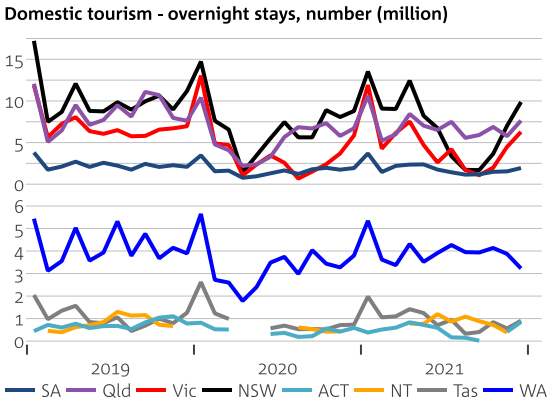
TRAVEL AND COMMODITIES

Tourism yet to recover but should be helped by borders (interstate & national) opening up, commodities doing better

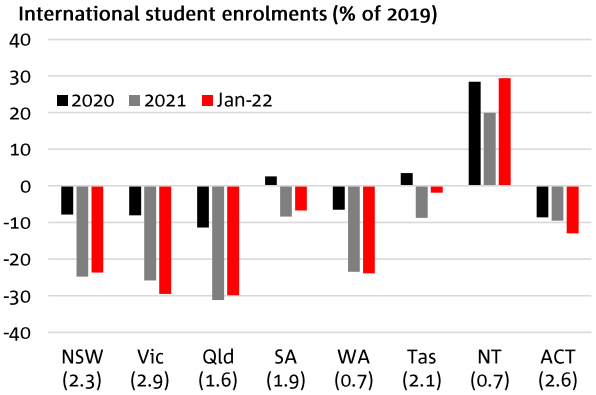
International short-term visitor arrivals still very depressed



Domestic tourism has not filled the gap – some improvement recently but mainly in NSW, Vic reflecting end to lockdowns

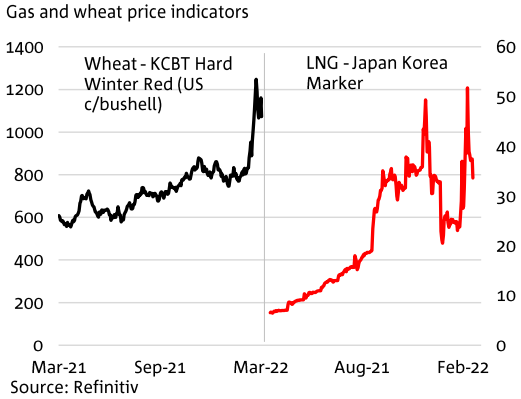


Overseas student enrolments still well down (ex NT) but signs of stabilisation in early 2022 (Vic, ACT the exceptions – a concern given importance of education sector)



Number in brackets is 2020 education credits as % of 2019/20 GDP

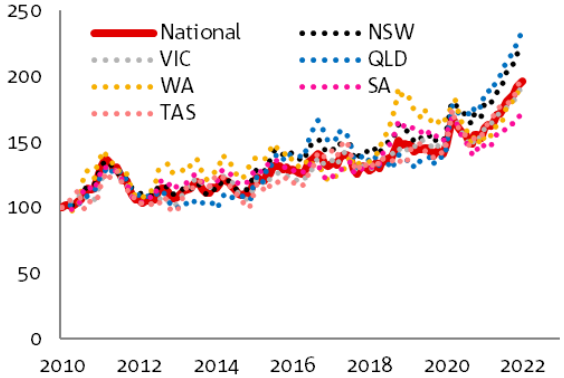
Russia/Ukr: spike in some commodity prices – particularly for grains & energy - potentially a boost for some producers but not consumers and prices already off peaks and a lot of uncertainty about conflict's duration/extent



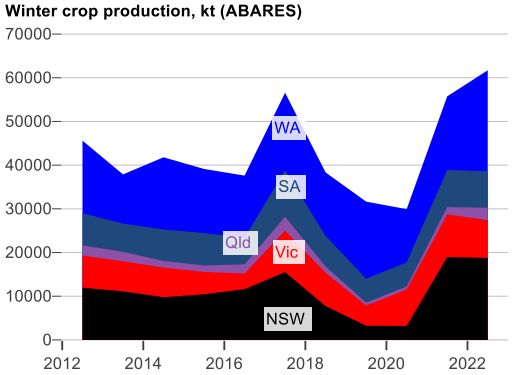
Source: Refinitiv

High rural commodity prices and another bumper winter crop in 2021/22 providing an income boost to farm sector

NAB rural commodities price index



Winter crop production, kt (21 & 22 estimates)



Sources: ABS, NAB, Department of Education, Skills and Employment, ABARES (March 2022 Crop Report), Macrobond

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