STATE ECONOMIC OVERVIEW

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National Australia Bank

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COVID disruptions continue to fade while growth remains strong and labour markets are tight everywhere

The impacts of capital city lockdowns and state border closures continue to fade, but the lingering impacts of the pandemic in terms of inflation, migration and international travel continue to play out across the states.

Generally, economic growth has been strong across the country, even accounting for the impact of a rebound in activity as lockdowns fade. State final demand is now well above its pre-COVID level in every state. The rebound has been led by strength in household consumption but also supported by strong government spending. However, reflecting the lagged reopening in NSW and Vic, the two largest states rebounded more slowly than the others, while elevated commodity prices have also supported WA, NT and Qld.

Looking forward, we expect growth to slow across the states as the measured impacts of the rebound and closed borders fades, and high inflation and interest rate increases weigh on household budgets, slowing consumption. These forces are expected to have a broad impact across the states as is the ongoing rebalancing away from goods spending. Both dwelling and business investment are also expected to slow as the impact of pandemic-related stimulus fades.

The strong recovery in activity has also seen very strong labour demand across the states – with employment now well above pre-COVID levels in many states and labour markets now very tight. The unemployment rate has declined sharply across the states, with NSW and Vic around 1 ppt below their pre-COVID trends, while QLD, WA and SA have seen even larger falls of around 2 ppt. Job ads and vacancies data suggests labour demand remains strong across all states with close to one vacancy for every unemployed worker.

NAB growth forecasts for the states & territories

	Gross State Product (y/y%)			
	20-21	21-22f	22-23f	23-24f
NSW	1.4	2.1	4.5	2.0
VIC	-0.4	5.7	3.4	1.5
QLD	2.0	3.8	2.9	2.0
SA	3.9	3.8	2.4	1.5
WA	2.6	4.7	2.1	0.9
TAS	3.8	4.7	2.9	2.2
NT	-0.6	5.0	3.9	-0.8
ACT	2.8	3.8	3.2	2.2
Australia	**1.6**	**3.9**	**3.4**	**1.6**

With global factors having been the key driver of recent inflation all states have seen increasing price pressures. Building costs have been a key part of this, with slightly stronger outcomes in WA and QLD boosting the capital city indexes in those states. Over time, many of the international factors will fade and state specific factors such as rents growth and the impact of faster wage growth will increase in importance.

Housing markets across the states are experiencing a large adjustment. House price falls have now broadened out across the states – driven by reductions in borrowing power. So far, the capitals most impacted by affordability constraints (Sydney and Melbourne) have fallen the most. While borrowing power has declined substantially, strong labour markets and very tight rental markets (and accelerating rents growth) are key offsets.

Population growth is showing early signs of a rebound after slowing to its slowest rate in 100 years while the international border was closed. All states saw significantly softer population growth but Q1 2022 data shows a solid rebound in overseas migration across the states Interstate migration trends will also be important as the pandemic-related dynamics unwind. WA, SA and the NT have also seen a boost with lower than usual interstate departures.

The impetus from the agriculture sector may have peaked – while estimates point to a good 2022-23 winter crop, they are down from 2021-22. Similarly, while rural commodity prices remain high, they have fallen in recent months.

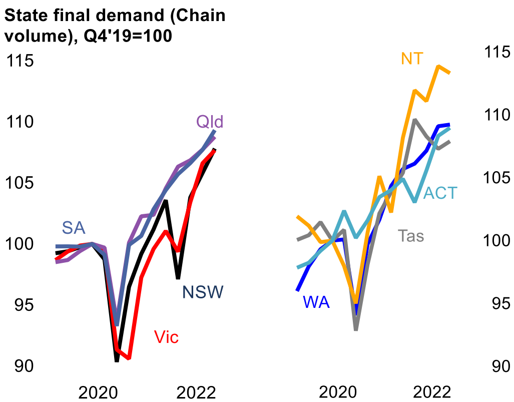
While growth is expected to slow across the states, the NAB business survey suggests that business conditions have remained resilient everywhere, and that firms remain relatively optimistic. While this may fade as growth slows, capacity utilisation is also high across the states, and points to ongoing price pressures in the economy in the near term before the impact of higher rates feeds through the economy more fully.

The key risks for the state economies continue to evolve. Locally, the threat of lockdowns and border closures is firmly behind us, though overseas the COVID Zero approach in China (and property market fallout) poses a risk for global growth. Similarly, while the war in the Ukraine will provided a boost for energy exporting states in the near-term, energy prices have fallen back over recent months and the impact on global growth in the medium term will ultimately weigh on trade. Likewise, the global monetary tightening underway will serve to significantly slow global growth more broadly over the next two years.

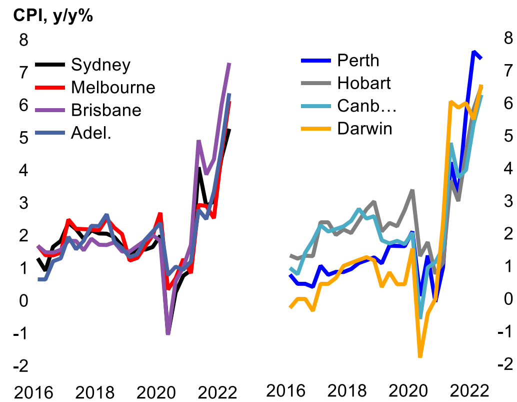
STATE OVERVIEW – SOME KEY DEVELOPMENTS

State demand continues to recover, and population growth is starting to pick-up. But inflation is high across the board and state governments are starting to repair budgets, although they continue to push infrastructure spending higher

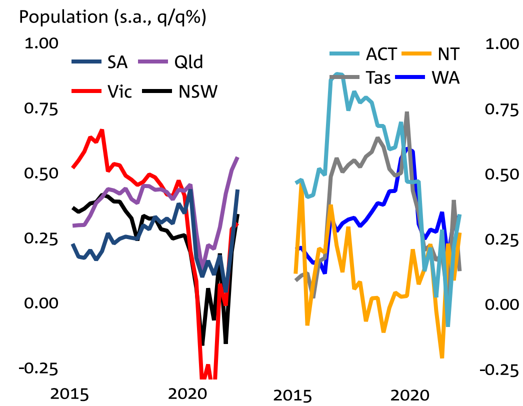
Vic and NSW – the post COVID recovery laggards, starting to close the gap while Tas has struggled over recent quarters



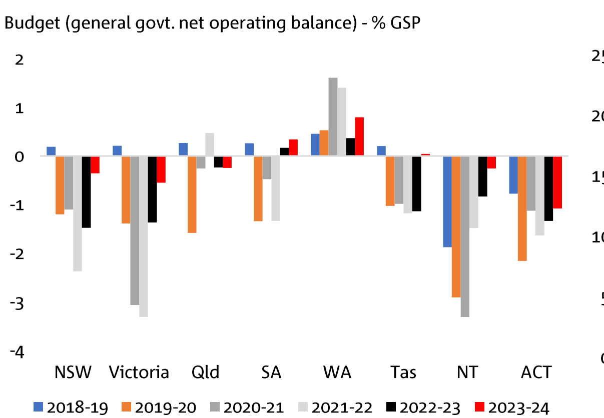
Inflation elevated across all states



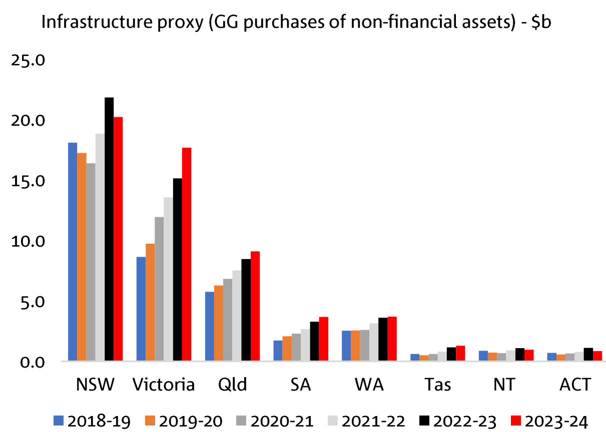
Population growth starting to rebound; at or above pre-COVID levels in Qld, NSW, SA, NT



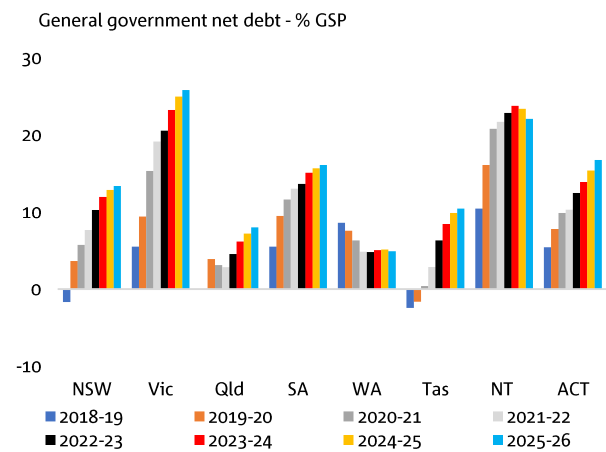
Some states moving to repair budget positions (particularly NSW, Vic, NT, ACT, SA); WA stands out as the state where the Budget did not deteriorate during the pandemic



States increasing infrastructure spend; although rising construction costs will constrain actual infrastructure delivered



Slow speed of fiscal repair and elevated capex spend means state government net debt is rising; WA the exception



Sources: ABS, Department of Health, Macrobond, State Budget papers and annual financial reports, NAB

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New South Wales

The NSW economy rebounded strongly from the Delta lockdowns which came to an end in late 2021, despite challenges in early 2022 from the Omicron wave (which came largely through a temporary hit to hours worked) and severe flooding in some parts of the state.

The Q2 national accounts shows SFD is now 7.8% above its pre-COVID level, led by strong gains in household consumption. Dwelling investment has also risen, though business investment growth has remained muted. Public spending has also been a key support.

Alongside the rebound in activity, the labour market has performed strongly. Employment is now 3.7% above pre-COVID levels and the unemployment rate has fallen to 3.4%. Despite the strong growth in employment over the past year, job vacancies remain elevated in the state at 151k.

More recent data suggests that activity has remained resilient with business conditions and capacity utilisation high in the state, while ABS retail sales data also suggest that household spending has remained resilient.

The impact of higher rates has fed through sharply to Sydney's housing market where prices have fallen 9.2% after peaking in January. While house prices are declining at a brisk pace, this follows a rapid rise of 25% over 2021. More broadly, activity and construction indicators have slowed. This comes despite a notable tightening in the rental market, with the vacancy rate now around 1.3%.

On the non-residential construction side the weather has also impacted construction with a 3rd La Nina likely to see further disruption.

Victoria

The Victorian economy has rebounded strongly from the extended lockdowns in the state over the past few years with little lasting impact on activity in aggregate and a full recovery in the labour market.

SFD is now 7.7% above pre covid levels. While Victoria saw softer growth than other states following the initial lockdowns in 2020, household consumption and government investment spending have driven the strength since late 2021 – both up well over 13%.

Retail sales data suggests that eating out & takeaway continues to rebound strongly reflecting the broader recovery in services spending. Business conditions have also held at a high level through Q3 suggesting that growth has remained resilient.

Victoria continues to see the impact of slower population growth from the pandemic, closure of the international border as well as a reversal in the usual net interstate migration trends – though Q1 population data show a rapid turn around.

The labour market has tightened significantly in the state with the unemployment rate at 3.7%, close to record high labour force participation at 67.0% and employment now 2.8% (95k) above pre-Covid levels. Even after the strong growth in the labour force over the past year, there are 56k job vacancies unfilled.

Dwelling prices have also begun to fall as interest rates have risen – down by 5.6% from their recent peak in February but remain 18% higher than mid-2109 levels. After rising through the peak of the pandemic to as high as 4.7%, the rental vacancy rate has declined sharply in 2022 and at 1.4% is back around pre-pandemic levels. Therefore, while interest rates will likely continue to drive prices lower, a strong labour market and growth in rents will be key supports.

Queensland

While not suffering lockdowns of the magnitude and duration of the other states, the economy has grown strongly as state borders reopened. Though like other states it faces challenges from global economic factors on the supply side and has seen some disruption to activity in the south east due to weather – in the near term it stands to benefit from being a net energy exporter.

SFD demand is now 9% higher than its Q4 2019 level (though it did not see as large a decline in Q2 2020 as the other states), leaving QLD second only to SA (amongst the states) in economic performance over the period.

Similar to other states, the labour market has tightened with strong labour demand pushing employment up 8% on pre-COVID levels. with the unemployment rate falling to 3.2% marking the first time it has persisted below 5% since prior to the GFC. Strong labour demand is set to persist, with job vacancies still 123% above pre-COVID levels at 86k.

Qld has also benefited from stronger net interstate migration through the pandemic, and while still heavily impacted by weaker international migration has seen population growth hold up relatively more strongly than other states at 1.0% in the year to March.

Brisbane dwelling prices have turned down more recently than the larger capitals, but have fallen 4.3% since June. Nonetheless, they remain 13.4% higher than a year ago. The rental market has tightened sharply and now sees as vacancy rate of just 0.7% which has resulted in rents growth reaching 13.5% y/y at present.

Overall, like elsewhere, higher interest rates are expected to slow consumption growth but still high commodity prices, strong employment conditions and recovering international tourism will provide supports.

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South Australia

The SA economy performed strongly over the last year. SFD rose 4.7% and is well-above its pre--COVID level (+9.3%, outperforming the national average).

The strong performance reflects robust growth in consumption (particularly by government but also by households), and dwelling and underlying business investment. Public investment, in contrast, declined over the past year. Exports have also increased rapidly but imports have risen more quickly. Service imports have rebounded more strongly than exports (consistent with little upturn yet in foreign student enrolments).

SA's labour market Is very tight. Even with recent flattening out in employment, the August unemployment rate (3.9%) was an (equal) historical low (data since 1978) and job vacancies are high.

However, growth is likely to slow. This in part reflects the same factors expected to weigh on the national economy – weak global growth, rising interest rates and a fading boost from post pandemic re-opening.

There are some signs of a slowdown already. While trend business conditions remain around their historical average (trend terms) they have eased while business confidence is soft. For agriculture, ABARES expectations point to a slightly smaller (but still good) winter crop in 2022-23, while prices have started to come off from their recent high levels.

However, there are also some positive indicators. Population growth has rebounded, businesses are signalling strong capex and employment expectations for the next 12 months, and the state government is also expecting a further lift in public infrastructure spending. Moreover, while housing will come under pressure from rising interest rates, building approvals have stabilised in recent months and there is a still a large pipeline of work.

Western Australia

After weathering the pandemic relatively well compared to other states through 2020 and 2021, WA bore the impact of the Omicron wave early in 2022 but has been buoyed by a strong commodity prices through the middle of the year.

Consumption was flat early in the year as Omicron impacted behaviour, but SFD still grew by a strong 1.8% in Q1, supported by government spending on the pandemic response and business investment, driven by machinery and equipment.

Since then, the reopening of borders and passing of the Omicron wave has seen consumption rebound including travel and recreation spending. Investment in machinery & equipment has also continued to grow as the mining sector has sought to boost production, although overall investment softened in Q2 as new projects and exploration slowed.

On net, SFD grew by a more modest 0.1% in Q2 to be up 3.3% y/y. Overall, WA's economy is 9.2% larger than it was pre-COVID, reflecting the overall outperformance of the state during a difficult period.

With commodity prices elevated and borders open, business conditions remained strong at around +20 index points in August. Confidence has been softer, around +2 index points, with inflation and interest rate increases likely weighing on firms' outlook alongside global growth concerns, which may see commodity prices soften further.

As in other states, WA's labour market has become increasingly tight over the year. The unemployment rate was down to just 3.1% in August – the lowest of the major states – and participation remains close to 70%. Wage growth is also picking up, with a 0.8% rise in Q2 WPI the strongest of the states, leaving wages 2.7% higher over the year.

Property prices have risen by around 24% in Perth since early 2020, after a long period of more muted growth when compared with the other capitals. We expect slightly less dramatic price falls over the coming year than in other cities as higher interest rates flow through the market nationally. The pipeline for residential construction is extremely elevated in WA, which will take time to work through given supply constraints.

Looking ahead, commodity prices have begun to decline as global growth concerns weigh on the outlook, likely dampening some of the strength in WA's resources sector. Still, another strong crop should support the agriculture sector and the ongoing strength of the local economy in the wake of COVID will likely provide some support, albeit interest rates and inflation will weigh on consumers as elsewhere.

STATE BY STATE

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Tasmania

SFD declined between Q3 2021 and Q2 2022, as the economy hit a soft patch. This mainly reflected falls in business and dwelling investment (although the former still remains solid and well above its pre-COVID level). Compared to its pre-COVID level, SFD is still up 7.9%, but after having previously experienced a relatively fast recovery, Tasmania is now only slightly below the national average.

While business conditions reported in the NAB Business survey are well above average, confidence is on the low side. Support should come from a ramping up in state infrastructure investment and despite coming off its peak, the pipeline of residential construction work remains high.

Tasmania's labour market remains strong, but there are signs of easing. Employment has levelled out and the unemployment rate has drifted higher. That said, the unemployment rate remains very low by historical standards and job vacancies are elevated

Northern Territory

While SFD fell in Q2, it reflected a pull back in Government COVID-19 related spending. Household consumption bounced back strongly from its Q1 fall, with COVID-19 sensitive sectors seeing a large rebound while fixed investment also rose.

SFD, relative to its pre-pandemic level, remains stronger in the NT than elsewhere. A big part of this has been strength of private investment, reflecting mining investment (particularly LNG via the Barossa Project) as well as defence spending. Public investment has also been increasing.

The labour market remains strong, with a low level of unemployment. Population growth also strengthened in early 2022, reflecting border re-opening which will also boost tourism. Darwin house prices have held up so far but will not be immune to rising rates.

ACT

SFD growth slowed in Q2, but was still up a solid 3.9% over the year and well above (+9.0%) its pre-pandemic level. This reflects public sector consumption – boosted by COVID-19 - which the ACT government expects will moderate. However infrastructure spending should increase this year and business investment has also grown solidly.

Dwelling investment is below its pre-COVID-19 level, but there was strong growth in Q2 and the pipeline of work remans high. Dwelling prices have fallen modestly in recent months but are still over 30% above their early 2020 level.

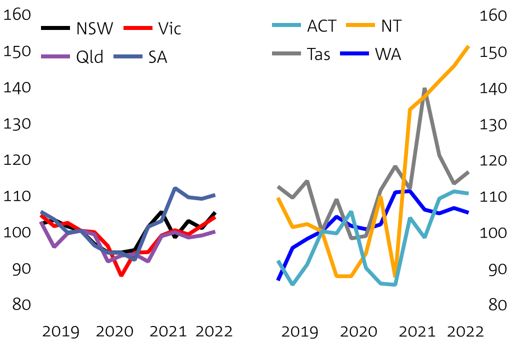
The labour market has struggled post COVID-19; while the unemployment rate remains low, employment is only around its pre-COVID-19 level. Population growth has been soft, although it showed signs of picking up early in 2022 despite a loss of population to other states.

BUSINESS SECTOR

Business conditions have remained elevated through the year and investment is picking up.

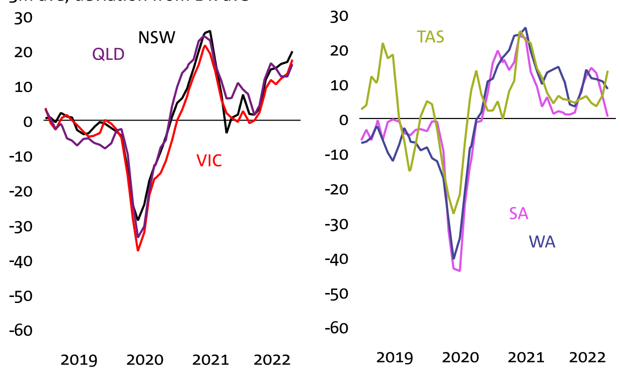
Business investment moved higher since end '19, particularly in NT but also SA, ACT & TAS with some recent momentum in NSW but Qld lagging

Underlying business invest
Q4'19=100



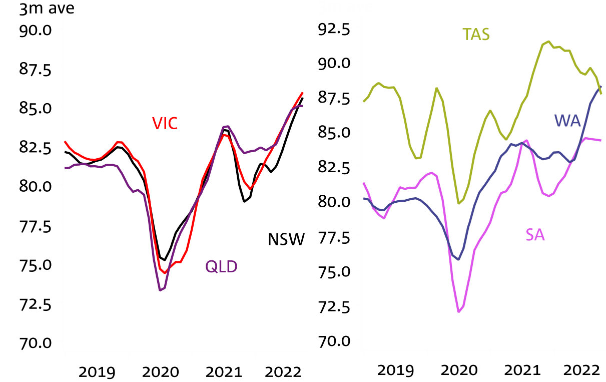
Business conditions have been very strong across the major states through the middle of the year. Conditions have recently picked up in Tas but softened in SA.

NAB Monthly Business Conditions
3m ave, deviation from L-R ave



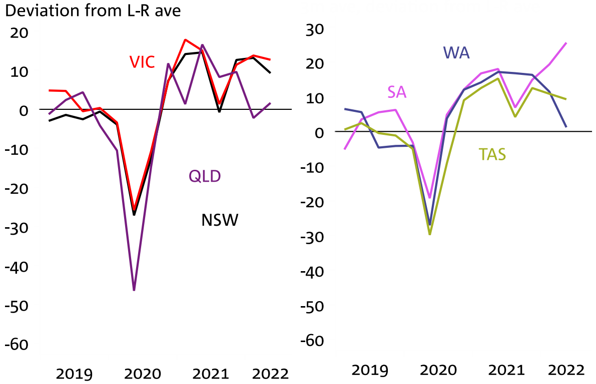
Capacity utilisation is at record levels in NSW, VIC, Qld, and WA, reflecting the tight labour market and broadly strong conditions. It has also been elevated in Tas but softer in SA.

NAB Monthly Capacity Utilisation
3m ave



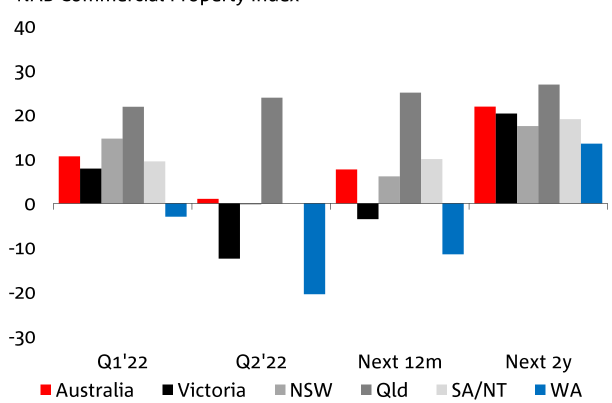
Investment expectations remain elevated in NSW and Vic and have lifted in SA, but are around average in Qld and WA

NAB Qtly Capex 12m Expectations
Deviation from L-R ave



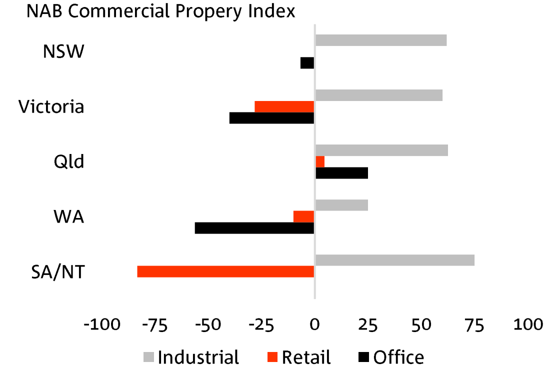
Commercial property sentiment deteriorated in Q2 outside of Qld. Vic and WA very weak

NAB Commercial Property Index



Industrial properties strongest sector in all states, while retail and office generally weak
(Q2 2022 NAB Commercial Property Survey)

NAB Commercial Propery Index

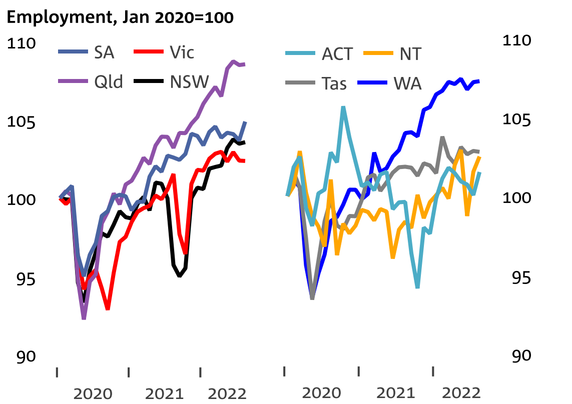


Sources: ABS, Macrobond, NAB

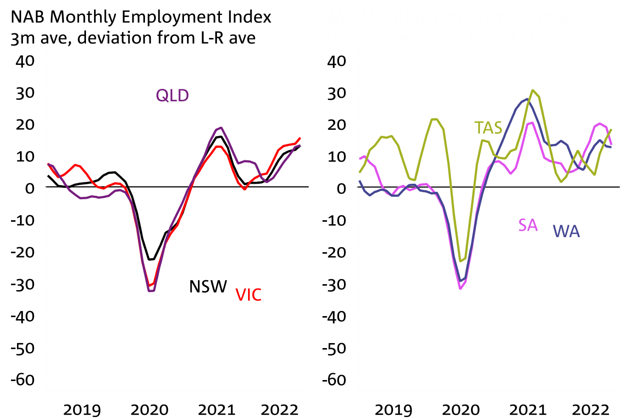
LABOUR MARKET

Labour markets are very tight, with labour hard to find and wage growth strengthening, in most states

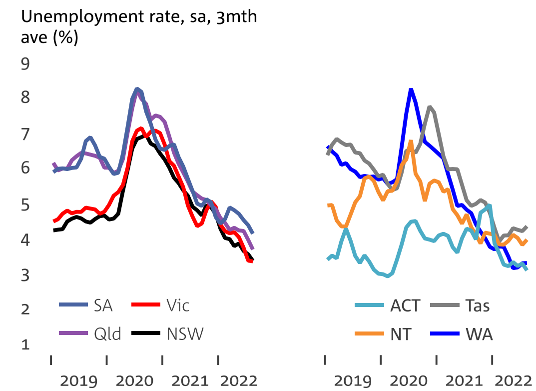
Wide divergence in employment recovery – Qld, WA, SA in particular have been strong



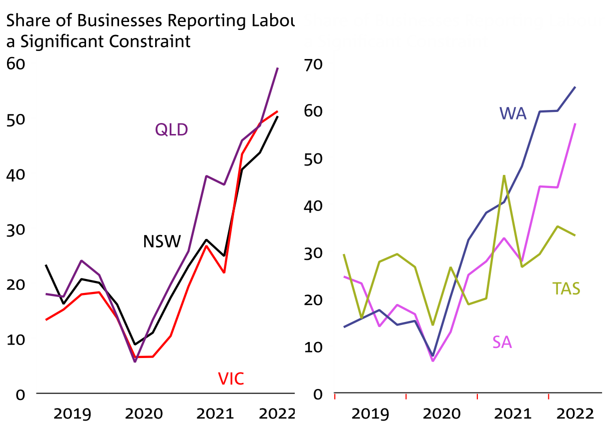
The NAB survey measure of job creation is now well above average in every state, reflecting the strength of labour demand.



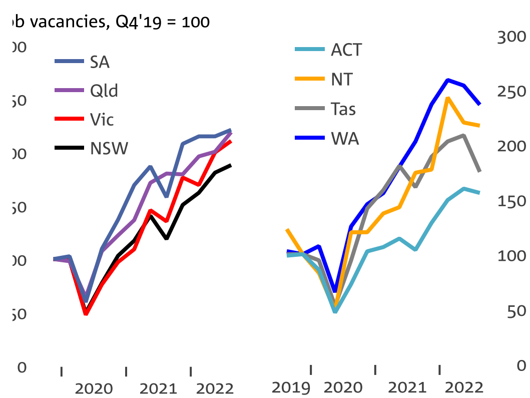
Unemployment rates have been trending down, but appear to have stabilised in the WA and Tas and NT



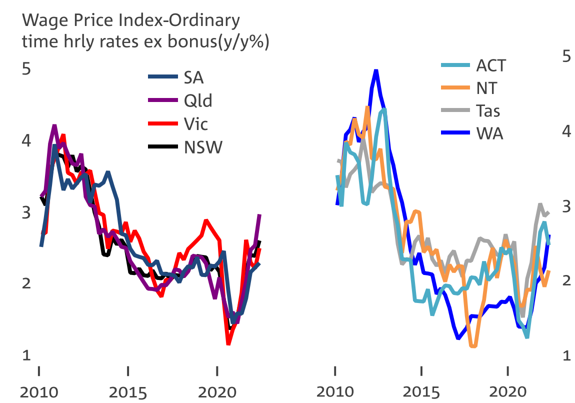
Labour is a significant constraint for half or more of all firms in all states (except Tas) – a record level of labour tightness.



Job vacancies remain at very high levels, though WA and some smaller states appear to have peaked.



Wage growth strengthening and generally at or above pre-COVID growth rate (ex NT)



Sources: ABS, Macrobond, NAB

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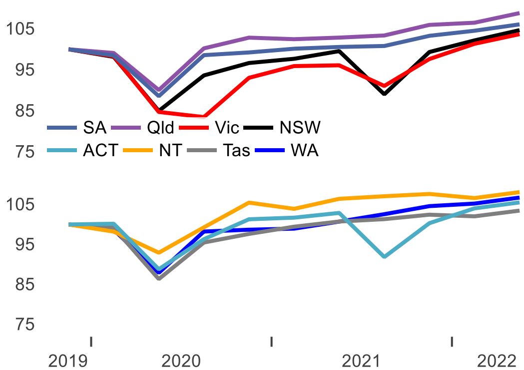
HOUSEHOLDS – CONSUMPTION

Consumption still trending higher, aided by ongoing rebound in COVID affected service sectors, despite low consumer confidence

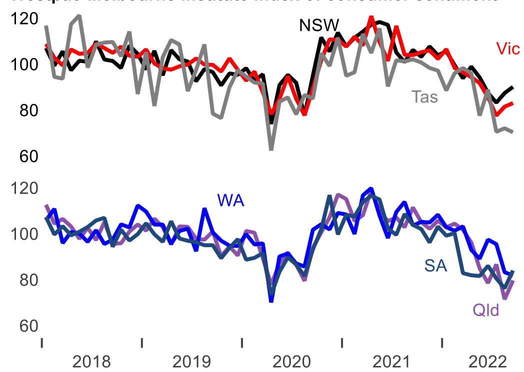
Consumption growth was robust in all states in Q2.

H'hold consump., Q4'19 = 100



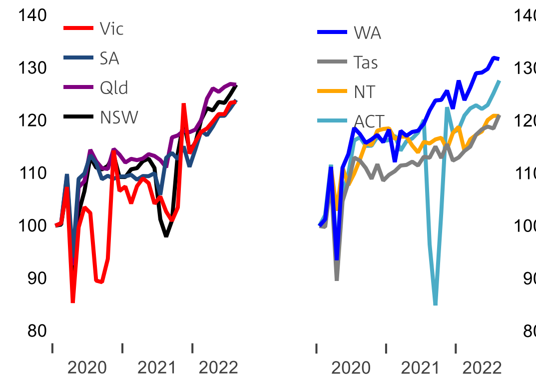
Consumer confidence at low levels across all states as inflation and rising interest rates weigh on households' outlook.

Westpac-Melbourne Institute index of consumer sentiment



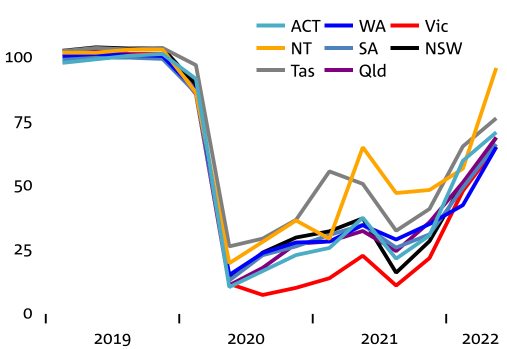
Nominal retail sales continue to outperform, supported by inflation and underlying strength in demand.

Retail sales, Jan 2020 = 100

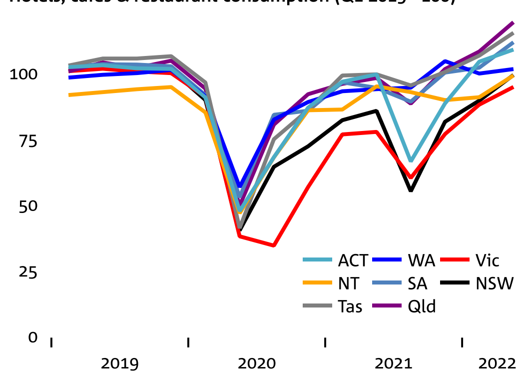


COVID affected service sectors see a rebound across most states while goods consumption has levelled off (but remains elevated compared to its pre-COVID level except in the NT)

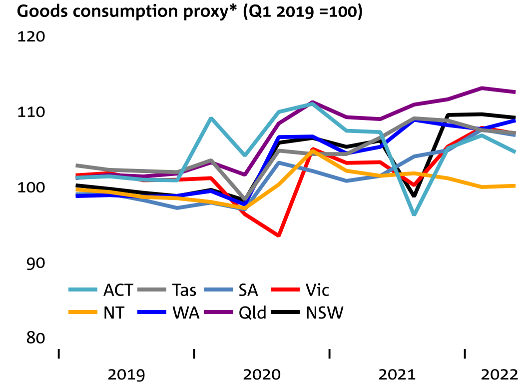
Transport services consumption (Q1 2019 =100)



Hotels, cafes & restaurant consumption (Q1 2019 =100)



Goods consumption proxy* (Q1 2019 =100)



Sources: ABS, CoreLogic, Macrobond, NAB

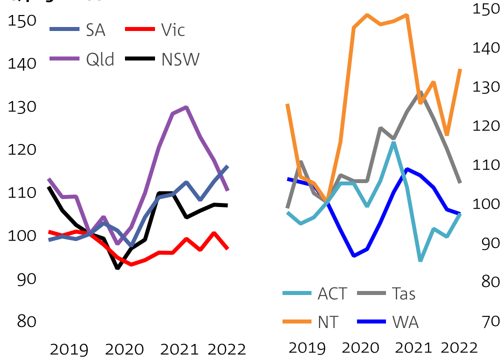
* Proxy comprises food, cigarettes & tobacco, alcoholic beverages, clothing & footwear, furnishings & household equipment, vehicle purchases

HOUSEHOLDS – HOUSING MARKET

Housing markets under pressure from rising interest rates, but elevated construction pipeline and rental mkts tight

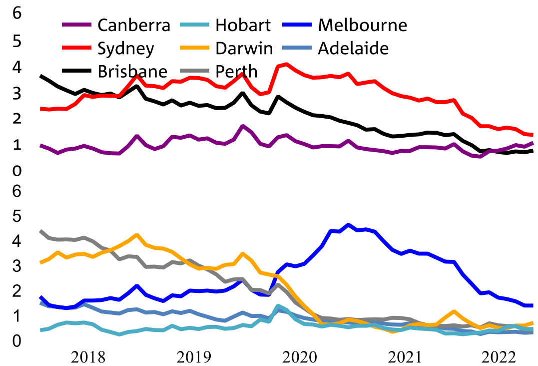
Dwelling investment – mixed trends recently partly due to weather events in some states. Above pre-pandemic level except in Vic, WA and ACT

Dwelling investment, Q4'19 = 100



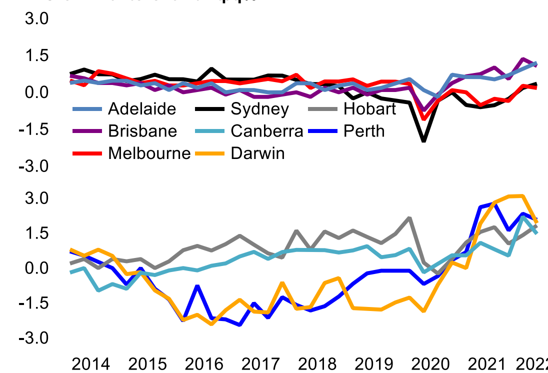
Vacancy rates have moved down but, outside Melbourne and Sydney appear to be stabilising at a low level

SQM Research Capital City Vacancy Rates, sa.



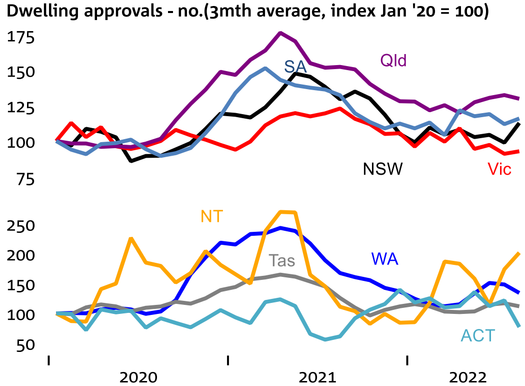
Pace of rental increases has picked up

ABS CPI Rents Growth q/q%

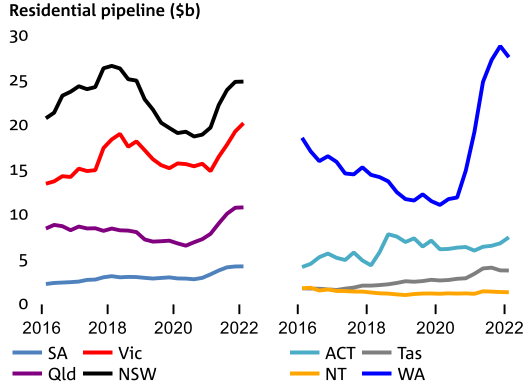


Rising interest rates are putting pressure on the housing sector. Building approvals have fallen but showing signs of stabilising (for now) in recent months and there is still a large pipeline of work. House prices now falling and we expect this to continue over the rest of 2022 and into 2023.

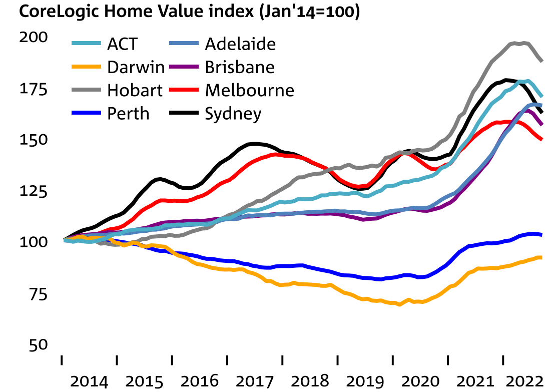
Dwelling approvals - no.(3mth average, index Jan '20 = 100)



Residential pipeline ($b)



CoreLogic Home Value index (Jan'14=100)

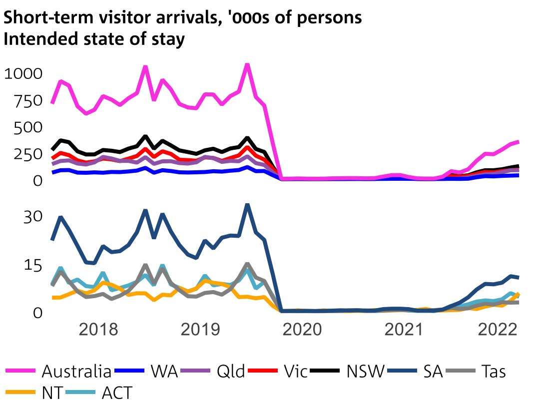


Sources: ABS, CoreLogic, NAB.

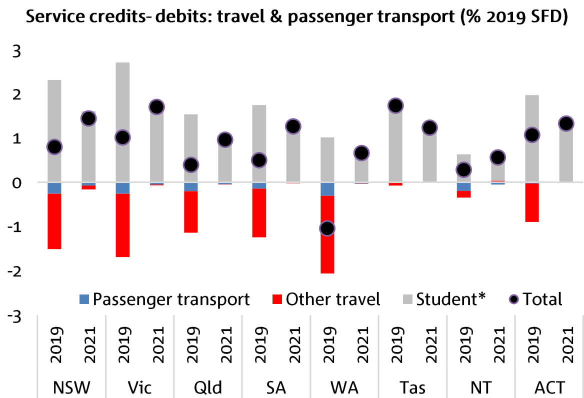
TRAVEL AND COMMODITIES

Tourism and international students starting to recover, while commodity prices coming off but still high

International short-term visitor arrivals still depressed but recovering following border re-opening

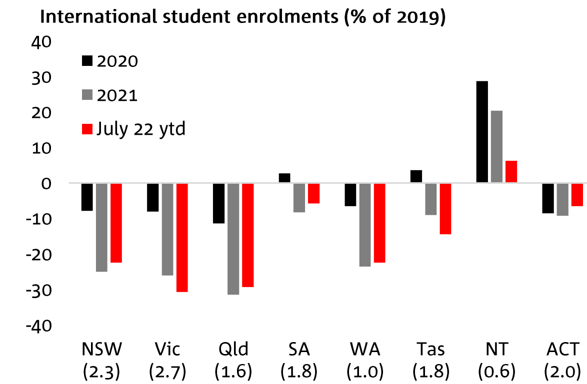


Border closures, due to bigger impact on Aust. travelling overseas, arguably supported domestic spending (except Tas.) – will reverse



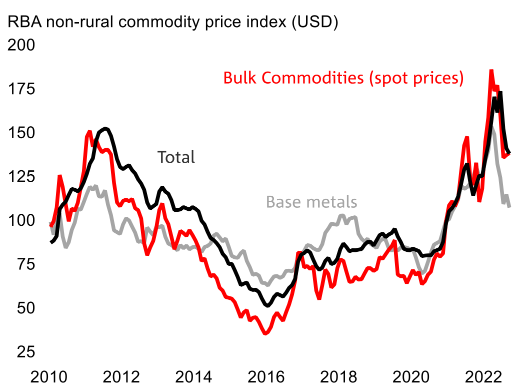
* Adjustment to 2021 student travel to include change in 'other cultural, personal & rec. services' which include foreign students studying abroad

Overseas student enrolments still well down in NSW, Vic and Qld and WA but starting to turn around (ex Vic)

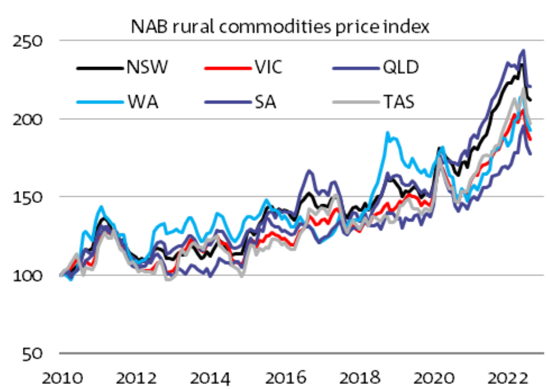


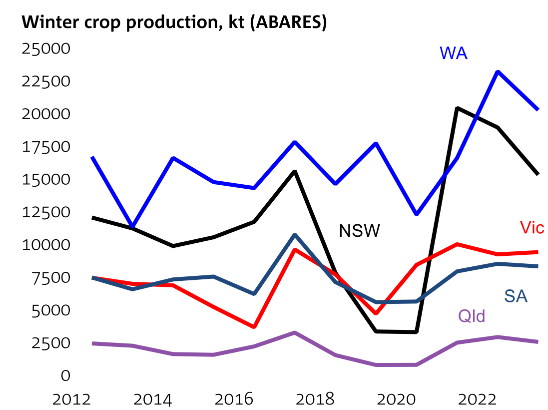
Number in brackets is 2019 education credits - % of 2019 state final demand

High commodity prices have benefited the resource states (WA/NT) – but now coming off due to weakening global outlook



Rural commodity prices still high but have started to fall; similarly winter crop again expected to be elevated in 22-23 even if smaller than in 21-22 (except Victoria)





Sources: ABS, Department of Education, Skills and Employment, ABARES (September 2022 Crop Report; '21-22 data are an estimate, '22-23 a forecast), Macrobond, NAB

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