

## 2021 State Wage Case – Economic Conditions and Outlook<sup>1</sup>

### 1. Overview

The State's economic outlook was last published in the 2020-21 Pre-election Financial Projections Statement (PFPS), which was released on 8 February 2021. The 2021-22 Budget will be published in September this year, consistent with the timing of budgets in recent election years.

The Western Australian economy was significantly impacted by the onset of the COVID-19 pandemic in March 2020. The introduction of social distancing and other restrictions required to suppress community transmission of the virus forced many businesses to operate below capacity, to close for a period, or to close. Many workers unable to transition to work from home were stood down temporarily, or lost employment.

The June quarter 2020 saw the largest ever contraction in the State's domestic economy, as State Final Demand (SFD) declined by 6.2%. Similarly, the scale of job losses during the height of COVID-19 restrictions far outweighed any previous economic downturn. There was a fall in employment of around 103,300 people (between February and May 2020) in Western Australia, while the unemployment rate reached a peak of 8.7% in June 2020.

In the months that followed, conditions in the Western Australian economy have improved more rapidly than was anticipated at the onset of the pandemic. The recovery has been assisted by unprecedented levels of Government support, as well as activity continuing in some of the key industries in the State, most notably mining. The effective suppression of the virus underpinned a strong rebound in both household and business confidence which has in turn underpinned the recovery. Key labour market parameters have strengthened significantly since the initial impact of COVID-19. For instance, in aggregate terms, all of the initial loss in employment was recouped by March 2021.

A faster than expected recovery has generally occurred across all Australian jurisdictions, notwithstanding additional temporary lockdowns for individual States, including a five-day lockdown in early February and a three-day lockdown in April in Western Australia.

The PFPS forecast is for the Western Australian economy, as measured by Gross State Product (GSP), to grow by 2% in 2020-21, supported by growth in the domestic economy, including slight growth in household consumption. The impact of the recent lockdown is not sufficient to change the forecast.

COVID-19 continues to pose a significant risk to the economic outlook. Any further outbreaks are likely to result in further lockdowns or restrictions that will further impact the operation of businesses and may weigh on investment or hiring decisions. The timing of the rollout of vaccines domestically and in other countries is uncertain and will determine when it is possible to reopen borders and reinstate widespread international travel.

This attachment outlines recent changes in various aggregates and outlines the risks around the latest economic forecasts. A table providing detailed forecasts as at 2020-21 PFPS is provided at the end of this Attachment.

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<sup>1</sup> Data for historical levels of activity and historical growth rates are based on data published by the Australian Bureau of Statistics, unless otherwise stated.

**Table 1 – Major Economic Aggregates, Annual Growth (%)**

	2019-20	2020-21	2021-22	2022-23	2023-24
	Actual	PFPS Estimate	Forward Estimate	Forward Estimate	Forward Estimate
State Final Demand	0.8	2.25	3.75	2.25	3.0
Gross State Product	1.4	2.0	2.75	1.25	1.5
Employment	0.4	1.5	1.5	1.75	1.5
Unemployment rate <sup>(a)</sup>	6.1	6.5	6.0	5.5	5.5
Consumer Price Index <sup>(b)</sup>	1.3	1.5	1.75	1.75	2.0
Wage Price Index	1.7	1.5	1.75	2.0	2.25
Population <sup>(c)</sup>	1.5	0.8	0.7	1.0	1.3

(a) Data expressed as annual average during the financial year.

(b) CPI growth rates in 2020-21 and 2021-22 are based on the total index excluding the electricity sub-sector.

(c) Actual for 2019-20 based on ABS Cat. No. 3101.0

Source: Western Australia 2020-21 Pre-election Financial Projections Statement and Australian Bureau of Statistics

## 2. Global Outlook

The COVID-19 pandemic has had a substantial impact on global economic activity, with the International Monetary Fund (IMF) estimating that the world economy contracted by 3.3% in 2020 – the largest decline since 1945-46. All the major economies other than China contracted in 2020.

The global outlook has improved in recent months due to the roll-out of COVID-19 vaccines. Reflecting this, the IMF recently revised up its forecast for world growth in calendar 2021 and 2022.

**Table 2 – IMF Global Economic Forecasts April 2021**

Annual GDP Growth, %

				Difference from	
	Estimates	Projections		January 2021 WEO	
	2020	2021	2022	2021	2022
World Output	-3.3	6.0	4.4	0.5	0.2
Advanced Economies	-4.7	5.1	3.6	0.8	0.5
Australia*	-2.4	4.5	2.8	1.5	-
United States	-3.5	6.4	3.5	1.3	1.0
Euro area	-6.6	4.4	3.8	0.2	0.2
Emerging Market and Developing Economies	-2.2	6.7	5.0	0.4	0.0
China	2.3	8.4	5.6	0.3	0.0

\* Relative to the October 2020 WEO, as the IMF did not provide a forecast for Australia in the January 2021 WEO.

Source: IMF World Economic Outlook (WEO), April 2021

According to the IMF, the upward revisions reflect “additional fiscal support in a few large economies, the anticipated vaccine-powered recovery in the second half of 2021”, and continued adaptation of economic activity to the challenging health situation. The United States and Australia are expected to be amongst the few Advanced Economies to surpass their pre-COVID GDP levels in 2021.

There is a high degree of uncertainty surrounding the IMF’s projections with the global outlook dependent on the deployment and effectiveness of vaccines. In late April 2021, daily new COVID-19 cases globally reached their highest levels.

Risks to the global economic outlook are discussed in the risks section.

## 2.1 Global commodity markets

The improved global outlook and relatively quick recovery in China, particularly its industrial sectors, have contributed to rising prices for commodities most relevant to Western Australia. Whilst volatile, the iron ore price has risen sharply, reflecting strong demand from China and constrained supply from Brazil.

Prices for other commodities have also been supported by fiscal and monetary stimulus in China. Oil prices have recovered to pre-pandemic levels as global demand recovers and oil production continues to be curtailed by key oil producers. Lithium prices are recovering with the growing demand for electric vehicles in Europe and China. Copper prices have also been supported by the increasing demand for electric vehicles as they use about four times more copper than conventional combustion engines.

The Treasury index of commodity prices, which is weighted by export value, has risen over recent quarters (see Chart 1).<sup>3</sup>

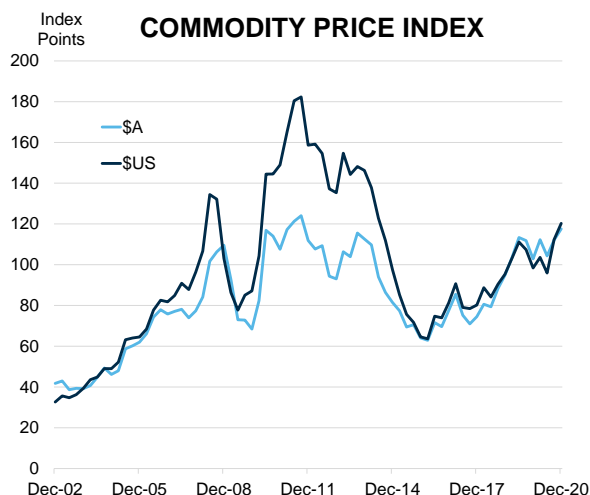
Demand for commodities has remained strong over the past year, with the value of Western Australian exports rising by 8.5% (or \$15.8 billion) to \$200.6 billion over the year to March 2021 primarily due to higher \$A commodity prices. China accounted for 55.8% of the total value of Western Australia’s exports over the year to March 2021, at \$111.9 billion, recording 14.5% annual growth.

After averaging \$US108 per tonne during 2020 the iron ore price has risen further to an average of \$US167 per tonne in the March quarter 2021 and \$US180 per tonne in April. Chinese crude steel output has reached record levels over the last few months and steel production in the rest of the world is now above pre-COVID levels.

Brazilian miner Vale, the world’s largest iron ore producer, is yet to recover from its January 2019 dam disaster. Its recovery has been slower than expected, partly due to the high levels of COVID in Brazil. The shortfall in iron ore supply has been largely met by higher cost producers in China and the seaborne market. Western Australian major iron ore producers are already operating near full capacity.

The iron ore price is expected to fall as stimulus-induced Chinese demand eases and Brazilian supply recovers. However, the pace and timing of the price decline is uncertain.

Chart 1<sup>2</sup>



<sup>2</sup> The Commodity Price Index is weighted index of prices of iron ore, gold, oil, LNG, copper, nickel, zinc, alumina and lithium. Source: Refinitiv, the Department of Mines, Industry, Regulation and Safety and WA Treasury.

<sup>3</sup> December 2020 is the last available value on the index.

### 3. National Economic Conditions and Outlook

The Australian economy (as measured by Gross Domestic Product, GDP) contracted by 2.4% in calendar 2020, due largely to a 7% decline in output in the June quarter, which was the largest quarterly decline on record. There was a strong recovery in each of the two subsequent quarters, as economic activity resumed following a widespread national lockdown. However, GDP in the December quarter 2020 remained lower than in the same period a year earlier.

In its Mid-Year Economic and Fiscal Outlook 2020-21 (MYEFO), Commonwealth Treasury forecast the national economy to grow by 0.75% in 2020-21 before strengthening to 3.5% growth in 2021-22. However, economic conditions have improved markedly in the months since its publication. For example, the monthly unemployment rate in Australia eased to 5.6% in March compared to the MYEFO forecast of 7.25% on average in the June quarter 2021. Commonwealth Treasury will provide updated forecasts in its 2021-22 Budget to be published on 11 May 2021.

In its April 2021 *World Economic Outlook (WEO)*, the International Monetary Fund revised up its growth projections for Australia to 4.5% in 2021 (up 1.5 percentage points (pp) from the October 2020 WEO) with growth expected to moderate to 2.8% in 2022.

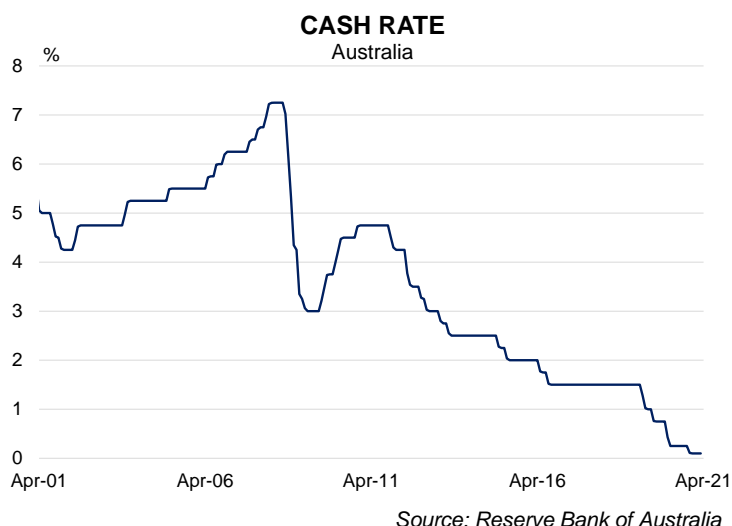
In line with this, the Reserve Bank of Australia (RBA) noted in its May 2021 *Statement on Monetary Policy (SMP)* that 'the Australian economy is transitioning from recovery to expansion phase earlier and with more momentum than anticipated', supported by low COVID-19 infection rates, substantial fiscal and monetary policy support and a lift in confidence. The RBA further states that 'household spending, dwelling investment and exports have all contributed to the snap back in activity'.

However, the RBA cautions that, while households and businesses appear to be adjusting well to the tapering of fiscal and other temporary support measures, the next phase of growth remains characterised by uncertainty. The RBA notes that the outlook is also likely to be uneven across industries for some time yet, reflecting the closed international border, restrictions in parts of the services sector, large shifts in consumer preferences, ongoing supply disruptions and slower population growth.

The RBA cut the cash rate to a record low 0.1% in November 2020 (Chart 2) and has maintained this position since. In its April 2021 Monetary Policy Decision, Governor Philip Lowe stated that the Board does not expect to raise rates 'until 2024 at the earliest', noting that an increase required further improvements in the labour market, and materially higher wages growth to push inflation to within the RBA's target band of 2-3%.

The May 2021 SMP forecasts that the national economy will recover from the initial impact of COVID-19 by the March quarter 2021, growing by 1% in 2020-21, supported by strong increases in household consumption and dwelling investment, The RBA then forecasts the Australian economy to strengthen further, growing by 5% in 2021-22 and 3.25% in 2022-23.

The recovery of the national labour market has outpaced the expectations of almost all forecasters. Employment recovered to exceed pre-COVID levels in March 2021. The unemployment rate eased to 5.6% and the participation rate reached a record 66.3% during the month. While the unemployment rate remains higher than prior to COVID-19, it has moderated significantly from a peak of 7.5% in July 2020.

**Chart 2**

## 4. Western Australia's Economic Outlook and Risks

The 2020-21 PFPS forecasts the Western Australian economy, as measured by GSP, to grow by 2% in 2020-21 following 1.4% growth in 2019-20. Economic growth is then forecast to strengthen to 2.75% in 2021-22.

The economic recovery to date has been more rapid than initially expected, highlighted by strong household spending (including in the residential construction market), and mining sector activity amidst elevated commodity prices. Overall, household consumption and business investment is anticipated to remain strong in the near term, as measures of confidence (which initially fell but subsequently recovered quickly) remain elevated. While the recent lockdowns in February and April did not have a significant enough impact to change the forecast outlook, the recent outbreaks highlight that risks to the outlook remain.

**Table 4 – Components of Economic Growth (Seasonally Adjusted)**

Annual Average Growth to December 2020, %

	Western Australia (%)	Australia (%)
Household consumption expenditure	-3.7	-5.8
Business Investment	7.3	-5.1
Dwelling Investment	-12.4	-5.4
Government Consumption	5.6	7.3
Government Investment	-0.6	0.9
State/Domestic Final Demand	0.1	-2.5
International exports <sup>(a)</sup>	-2.6	-10.3
International imports <sup>(a)</sup>	N/A	-13.0
Gross Product	N/A	-2.4

(a) Exports/imports refers to merchandise (goods) and services exports/imports.

Source: ABS Catalogue 5206.0 and 5302.0

A more detailed analysis of the outlook for the individual components of GSP is contained in the remainder of this section.

## 4.1 Consumer Spending

The 2020-21 PFPS projects household consumption to grow by 0.25% in 2020-21 (compared to a 1% decline forecast at Mid-year Review), largely reflecting a stronger than expected result for the September quarter 2020, positive consumer sentiment, and robust retail spending. Household consumption is then forecast to increase by 3.0% in 2021-22, as consumption lifts across all expenditure components and is boosted by an assumed recovery in hospitality and tourism. In 2022-23 and 2023-24, household consumption is projected to grow more moderately (by 2.5% per annum), underpinned by a gradual rise in population and income growth.

Household spending declined by 3.7% in 2020 due to a decline in household consumption in the March (-1.3%) and June quarters (-11.1%) of 2020. The largest declines over 2020 were in transport services, including international and to a lesser extent, interstate air traffic (detracting 2.3 percentage points (pp) from growth) and hotels, cafes and restaurants (detracting 1.5 pp) spending. Declines in a range of other categories of spending (operation of vehicles; electricity, gas and other fuel; cigarettes and tobacco; clothing and footwear; and health) were offset by modest contributions from other spending categories, most notably: furnishings and household equipment; food; rent and other dwelling services; and purchase of vehicles.

The forecast for modest growth in 2020-21 reflects that while household consumption has yet to recover to pre-COVID levels it did recover strongly in the September quarter (11.7%) and continued growing in the December quarter (0.3%). The level of household spending is expected to be sustained in the March and June quarters. The expectation that household spending will be sustained is supported by the high level of retail trade in the March quarter, notwithstanding that it declined from the December quarter.

Despite the lockdowns in February and April, consumer confidence in Western Australia remains elevated. The monthly Westpac Melbourne Institute series shows that consumer sentiment remains at an eight year high in April 2021, while the latest Chamber of Commerce and Industry of Western Australia *Consumer Confidence Survey* reported that short-term consumer confidence was at an 11-year high in March 2021. While those surveys were compiled prior to the April lockdown, the ANZ Roy Morgan weekly series indicates that confidence in Western Australia has generally trended upward in recent months. It also shows that although confidence did decline as a result of the April lockdown, it remained the second highest of all States after the April lockdown.

The strong rebound in household consumption in the September quarter and high levels of spending in subsequent quarters has been supported by government policies such as early access to superannuation, JobKeeper payments and the Coronavirus Supplement to income support recipients. Additionally, restrictions on overseas travel are likely to have translated to many people substituting towards domestic consumption.

While key Commonwealth support measures have concluded (with JobKeeper ending in March 2021), it is anticipated that an increase in household savings through 2020, together with on-going record low interest rates, will assist with the transition as Government support abates and help to sustain consumption levels through 2021-22.

## **4.2 Dwelling Investment**

The Commonwealth and State Government announced construction grants in response to COVID-19 in June 2020 in order to support the building industry. These policies have seen the demand for new dwellings lift significantly. As such, the 2020-21 PFPS forecasts dwelling investment to recover by 0.75% in 2020-21 before increasing by 21.75% in 2021-22 as high levels of land sales in the second half of 2020 begin translating into new dwelling construction.

This large forecast increase in dwelling investment is evidenced by substantive growth in lead indicators of dwelling investment. For instance, building approvals in the March quarter reached their highest level since December 2014. First Home Owner Grant applications in March 2021 were almost three times as large as the number recorded in March 2020.

## **4.3 Business Investment**

In the 2020-21 PFPS, business investment was forecast to grow by 2.5% in 2020-21 after increasing in annual terms for the first time in seven years in 2019-20 (by 9.5%). Business investment is expected to increase by 2.5% in 2021-22, before strengthening to 4.75% by 2023-24.

Investment levels have recently been supported by the construction of several large iron ore backfill projects. Strong business confidence and conditions, and more resilient non-mining investment than previously anticipated have supported overall investment. Over the out-years, investment is expected to be supported by spending to maintain current levels of output of mining and oil and gas operations, with non-mining investment also contributing to growth given improving overall economic conditions.

Importantly, the monthly NAB Business Survey showed that confidence in Western Australia rose to over a ten-year high in March 2021 and notwithstanding a decline in April, was still at its second highest level (after March) in more than ten years (since October 2010). After initially declining to a record low following the onset of COVID-19, confidence amongst the State's businesses rebounded strongly and has remained positive for eleven consecutive months

The latest Private New Capital Expectations survey results for the December quarter 2020 imply business investment growth (in real terms) of around 2.5% in 2020-21 (in line with Treasury's expectations). More markedly, this data points to a rise of more than 10% in 2021-22, well above the current Treasury projection of 2.5% annual growth.

## **International Trade**

### **4.4 Exports**

The 2020-21 PFPS forecast merchandise exports to remain steady in 2020-21 with modest increases in iron ore and gold production expected to be offset by an assumed decline in LNG volumes due to Gorgon project shut-downs for critical equipment repairs. In 2021-22, exports are forecast to grow by 1.5% as LNG production returns to capacity, lithium exports lift and iron ore exports continue to increase modestly.

In 2020, merchandise exports declined by 2.6%. However, exports increased by a very strong 11% in the December quarter 2020. The strong quarterly result, together with monthly trade data and data from the Department of Mines, Industry Regulation and Safety suggests that the forecast for unchanged levels of merchandise exports in 2020-21 remains reasonable.

The COVID-19 related travel restrictions have introduced downside risks to services exports, particularly the State's two largest service exports - tourism and education. As pandemic travel restrictions unwind, the services sector is expected to recover with trade and business services moving in both directions.

## 4.5 Imports

Merchandise imports at the 2020-21 PFPS were forecast to increase by 0.25%, an improvement from the Budget forecast of a 2.5% fall in imports in line with promising trends in household consumption and business investment. Further growth is expected from 2021-22 as COVID-19 trade disruptions unwind.

Services imports were forecast to decline in 2020-21 (-55.5%) as travel restrictions largely eliminated tourism imports (primarily Western Australians' spending overseas). These are expected to rebound in line with the eventual reopening of borders which would result in a gradual recovery across international tourism, education and business services.

## 5. The Labour Market

In line with the broader economic recovery, the State's labour market has been recovering at a faster pace than previously anticipated from the largest deterioration in conditions on record resulting from restrictions put in place to mitigate risks associated with COVID-19. In March 2021, employment in Western Australia exceeded pre-COVID levels for the first time. Other labour market indicators also show an improvement relative to pre-COVID conditions in the month.

**Table 5 – Population and Labour Force Forecasts**

Western Australia

	2019-20	2020-21	2021-22	2022-23	2023-24
<b>Annual Level</b>					
Total population ('000)	2,651	2,672	2,691	2,718	2,753
Working age population (15-64) ('000)	1,733	1,736	1,745	1,760	1,782
Employment ('000)	1,349	1,370	1,390	1,414	1,436
Unemployment ('000)	88	95	89	82	84
Unemployment rate (%)	6.1	6.5	6.0	5.5	5.5
Participation rate <sup>(a)</sup> (%)	67.5	68.2	68.2	68.2	68.3
<b>Annual growth (%)</b>					
Total population growth	1.5	0.8	0.7	1.0	1.3
Working age population (15-64)	0.8	0.2	0.5	0.9	1.2
Employment	0.4	1.5	1.5	1.75	1.5

(a) Based on the population aged 15 years and over.

Source: ABS and WA Treasury



## 5.1 Employment

The PFPS forecast for employment growth in 2020-21 is 1.5%, following 0.4% growth in 2019-20. Employment is then forecast to increase further in each year of the forward estimates.

Employment declined by 1.1% in annual average terms in March 2021, due to substantial job losses in the initial stages of the COVID-19 pandemic. Employment in Western Australia declined by a record 103,300 jobs between February and May 2020. Many of the initial job losses were part-time, due to the industries directly impacted employing a large share of part-time workers, such as in hospitality and retail. The largest falls in employment by industry in Western Australia over the period were in 'accommodation and food services' (-28,000 people) and 'retail trade' (-18,800).

There has been significant policy assistance throughout the COVID-19 period, which mitigated the impact of COVID-19 restrictions and initial household spending caution, on the labour market. Most notably, the Commonwealth's JobKeeper<sup>4</sup> program, one of the largest fiscal and labour market interventions in Australia's economic history, helped to maintain a connection between many employers and employees through the period April 2020 to the end of the program in March 2021. The program supported many employers by reducing labour costs, provided income and employment to employees, and allowed a rapid ramping up of hours worked as economic conditions improved through 2020.

After growing strongly in the September and December quarters, employment growth moderated in the March quarter 2021 – although employment increased by 2.4% in March. As a result, employment in March exceeded the pre-COVID level for the first time (Chart 3). The recovery in employment has been stronger for part-time employment. In March 2021, part-time employment was almost 5% above pre-COVID levels (in February 2020). By comparison, full-time employment remains slightly below pre-COVID levels (by -0.2%). Despite this trend towards part-time employment growth, total hours worked in Western Australia during March was the highest monthly figure on record. The recovery in hiring since the onset of the pandemic has occurred across most industries and occupations, though some sectors, such as those reliant on international travel, remain subdued.

Employment is expected to continue growing in 2021, supported by a high level of job vacancies (which in April 2021 was at its second highest level since June 2012). Closed interstate borders (until late 2020) and continued closed international borders has meant that the flow of skilled labour across borders has been restricted, and there have been reports of skills shortages emerging in select industries, particularly in the construction and mining industries.

As with the broader economy, there may be some risk to businesses' hiring intentions if further lockdowns were to arise in response to COVID-19. However, if these disruptions are short-lived, it may impact the timing of hiring decisions more so than the overall trajectory of employment growth.

## 5.2 Unemployment

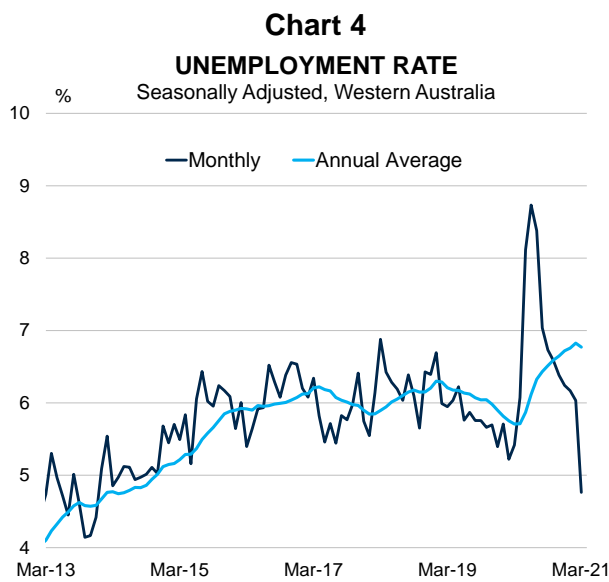
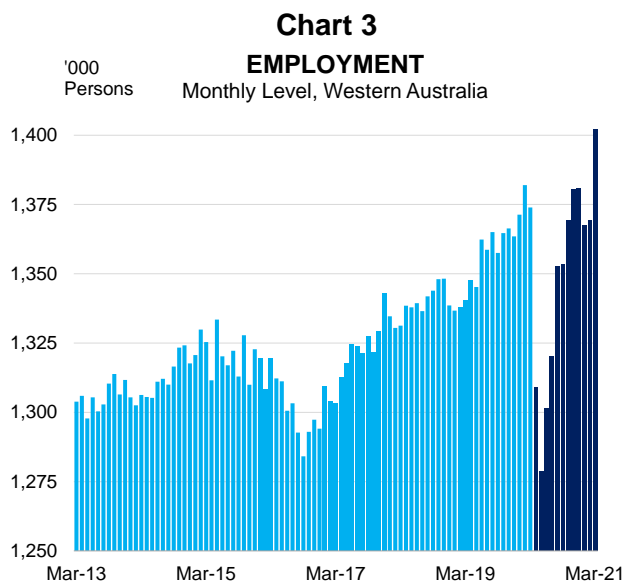
The PFPS forecasts the unemployment rate to average 6.5% in 2020-21, before easing to 6% in 2021-22 and to 5.5% by 2022-23.

The monthly unemployment rate peaked at 8.7% in June 2020 but has trended downward since then, falling sharply in March 2021 to 4.8% (Chart 4). As a result, the unemployment rate averaged 6.8% over the year to March 2021. The pace of recovery in the labour market to date, combined with the expectation that further hiring is likely to continue, means that the unemployment rate is likely to be lower than forecast in 2020-21 and 2021-22.

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<sup>4</sup> JobKeeper provided a wage subsidy to help firms affected by COVID-19 retain their staff. Initially this was \$1,500 per eligible employee per fortnight.

It is likely that the Commonwealth’s JobKeeper program mitigated job losses as a result of COVID-19. At its peak, there were more than 87,500 Western Australian businesses that applied for JobKeeper payments in the initial phase of the program that concluded in September 2020. The number of business applications in the State eased to around 35,000 during the December quarter 2020 and to around 24,000 in the final phase of the program in January 2021 (latest data). While data is not currently available to show the impact of the end of the policy, the transition away from JobKeeper has been relatively smooth thus far in Western Australia, and there is reason to expect that this should continue, given the high number of available job vacancies and elevated levels of business confidence.



Source: ABS 6202.0

## 6. Wages

### 6.1 Wage Price Index<sup>5</sup>

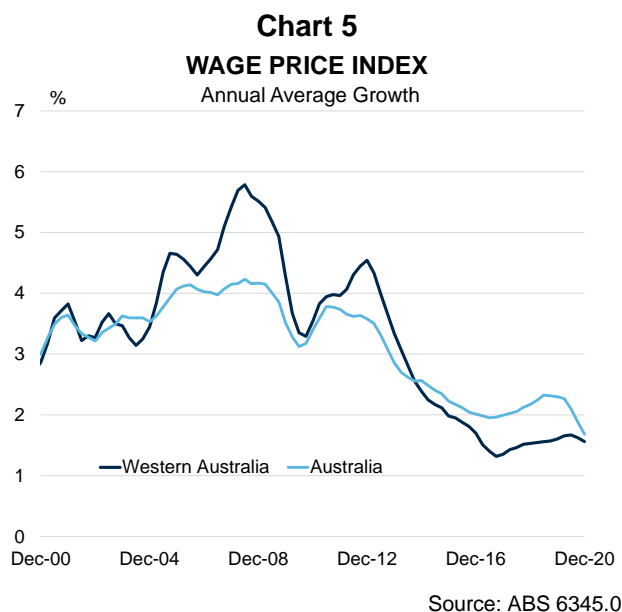
The PFPS forecast for growth in Western Australia’s Wage Price Index (WPI) in 2020-21 is 1.5%, which follows an increase of 1.7% in 2019-20. WPI growth is then forecast to progressively increase to 2.25% by 2023-24.

Wages growth has remained subdued in Western Australia for several years, with annual (financial year) growth in the WPI remaining below 2% since 2014-15 (Chart 5). The latest data shows that annual average growth in the WPI eased to 1.6% in 2020, which is broadly in line with the forecast for 2020-21. Year-ended growth, which tends to lead annual average growth, moderated to 1.4% in the December quarter 2020, indicating that annual average growth is likely to ease further in the remaining quarters of the financial year.

<sup>5</sup> Of the various wage indicators published by the Australian Bureau of Statistics, the WPI is generally viewed as the preferred measure of underlying wage growth. This is because the WPI is designed to measure wage changes for a fixed quantity and quality of labour, and thus abstracts from changes in average hours worked and other compositional changes in the labour market.

Tightening in the State's labour market and reports of emerging skilled labour shortages have yet to translate to widespread pressure on wages. Industry consultation has revealed that some firms may be opting to pay one-off bonuses to attract and retain staff rather than grant permanent salary increases. This would not be captured in the WPI measure.

The trend in Western Australia is consistent at the national level. The RBA has noted that national wage pressures have generally been subdued across both the private and public sectors. It notes that wage growth in the December quarter 2020 was supported by the reversal of some temporary wage cuts in the private sector which had been implemented in 2020 and the implementation of award wage increases which had been delayed in recognition of the economic downturn.<sup>6</sup>



## 7. Inflation

The 2020-21 PFPS projects Perth's Consumer Price Index (CPI) inflation of 1.5% in 2020-21 and 1.75% in 2021-22, before lifting to 2% annual growth in 2023-24<sup>7</sup>.

The CPI series has been particularly volatile in recent quarters, due to various policies that have impacted prices. The largest impact has been the State Government's \$600 Household Electricity Credit<sup>8</sup>, as 'electricity' prices reduced headline inflation in the December quarter 2020 by 1.9 pp and boosted headline inflation by 0.4 pp in the March quarter 2021. However, the Commonwealth provision of free childcare during the height of COVID-19 restrictions (which detracted considerably from Perth CPI inflation in the June quarter 2020 and was subsequently reversed over the next two quarters), and strong demand resulting from government stimulus in the residential construction sector (which has pushed up the price of new dwellings) have also impacted on headline CPI.

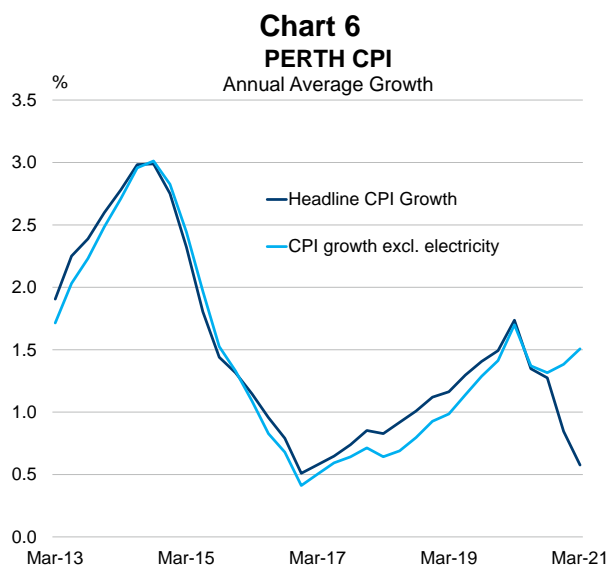
Given the impact of the \$600 Household Electricity Credit, the PFPS forecasts for CPI growth in 2020-21 and 2021-22 are based on the total index excluding the electricity sub-index. Excluding the electricity sub-index, Perth's CPI increased by 1.5% in annual average terms in the March quarter, down from 1.7% growth a year earlier (Chart 6). The annual increase was supported by elevated prices for 'alcohol and tobacco', 'food and non-alcoholic beverages' and 'new dwelling purchases'. These contributions were partially offset by a large decline in 'automotive fuel' prices.

<sup>6</sup> Reserve Bank of Australia - *Statement on Monetary Policy* – May 2021

<sup>7</sup> Consumer Price Index growth rates in 2020-21 and 2021-22 are based on the total index excluding the electricity sub-index.

<sup>8</sup> The \$600 Household Electricity Credit was introduced in November 2020. It provides each household with a \$600 credit on its electricity which the ABS treats as a reduction in the out-of-pocket expense to households and therefore detracts from CPI growth.

Volatility has also impacted national CPI inflation, which increased by 0.6% in annual average terms in the March quarter 2021, the weakest annual growth since September 1998. This compares with 1.8% annual average growth a year earlier. The RBA highlights the impact of policy on recent inflation data in its May 2021 *Statement on Monetary Policy*. The RBA's forecasts national CPI inflation of 3.25% in the June quarter 2021 relative to the same period a year earlier, though it notes that underlying inflation pressures are low.



Source: ABS 6401.0

The RBA has previously noted that the unwinding of government support measures such as free childcare provided at the height of COVID-19 restrictions boosted inflation significantly in the second half of 2020.<sup>9</sup> There was some housing inflation in the December quarter 2020 due to increased demand for detached houses, supported by government grants and the reversal of some temporary rent reductions.

Nationally, the weighted CPI of the eight capital cities increased by 0.6% in the March quarter and by 0.6% in annual average terms (or 1.1% in year-ended terms, the measure primarily quoted by the RBA).

The RBA's May 2021 *Statement on Monetary Policy* states that higher automotive fuel prices accounted for around half of the increase in CPI inflation in the March quarter. 'The large and temporary price changes arising from policy responses to the COVID-19 pandemic have mostly dissipated and are not expected to influence quarterly inflation outcomes much further' but will continue to impact annual growth rates in the near term. The RBA warns that it is expecting a temporary spike in inflation in year-ended terms in the June quarter 'as the effects of last year's temporary free childcare program and fuel price declines drop out of the calculation'. However, it also notes that 'other recent pockets of price pressures are abating, or are expected to do so in coming quarters, because heightened demand for some goods over the past year has eased a little and global supply chain disruptions are being worked through'. Additionally, underlying wages growth remains subdued, which mitigates pressure on inflation.

## 8. Risks to the Outlook

### 8.1 Global Risks

Uncertainty regarding the global economic outlook will likely remain elevated until the global COVID-19 pandemic is over.

Recent momentum in the global economy has been positive for Western Australia. In April 2021, the IMF upgraded its global growth forecast by 0.5 pp to a robust 6.0% in 2021 and by 0.2 pp to 4.4% in 2022, relative to its January 2021 update. This upgrade reflects the combined impact of policy stimulus and the rollout of effective vaccines in some of the larger economies.

<sup>9</sup> Reserve Bank of Australia - *Statement on Monetary Policy* – February 2021

Policy stimulus, particularly in China, has supported demand for commodities at a time when supply has been constrained by COVID-19 related disruptions and uncertainty. These dynamics have supported commodity prices and activity in Western Australia's mining sector.

However, the intensification of the pandemic in places such as India over recent months serves to highlight that downside risks remain substantial. Most of the world remains unvaccinated and new variants of COVID-19 may reduce the effectiveness of the vaccines currently being used. Another key risk is that the demand and supply factors currently supporting commodity prices unwind at the same time over the coming years - just as it did over the period 2014-16. In particular, demand for iron ore and other commodities in China could taper quickly if conditions there change and/or Brazilian supply could ramp up more quickly than currently anticipated.

## **8.2 Domestic Risks**

A key domestic risk is the potential of a more widespread outbreak of COVID-19 in Western Australia. Depending on the nature of such an outbreak and the policy response to that outbreak may result in a large economic contraction. For example, the 2020-21 Budget included a scenario where a second COVID-19 outbreak and a corresponding six-week State-wide lockdown resulted in a 1.25 percentage point deduction from the baseline GSP forecast for 2020-21.

While the economic recovery thus far has been strong, this has been supported by an extraordinary level of Government stimulus, including JobKeeper payments, which has recently ceased. While indicators to date suggest the pull-back in these measures since late September 2020 has not had a material impact on the overall economy, there may be some volatility as the economy adjusts.

**2020-21 PRE-ELECTION FINANCIAL POSITION STATEMENT FORECASTS  
COMPONENTS OF GROSS STATE PRODUCT**

Western Australia

**ECONOMIC FORECASTS**

Western Australia, Annual Growth (%)

	2019-20	2020-21	2020-21	2021-22	2022-23	2023-24
	Actual	Mid-year Review	PFPS Revision	Forward Estimate	Forward Estimate	Forward Estimate
<b>Demand and Output <sup>(a)</sup></b>						
Household Consumption	-2.3	-1.0	0.25	3.0	2.5	2.5
Dwelling Investment	-13.2	0.75	0.75	21.75	-13.25	-2.0
Business Investment	9.5	2.5	2.5	2.5	3.25	4.75
Government Consumption	4.9	3.5	3.5	1.5	2.5	2.5
Government Investment	-0.1	18.0	18.0	13.0	2.5	0.75
State Final Demand	0.8	1.75	2.25	3.75	2.25	3.0
Merchandise Exports	0.4	0.0	0.0	1.5	1.0	0.25
Merchandise Imports	1.3	-1.25	0.25	1.0	2.25	2.5
Net Exports <sup>(b)</sup>	2.4	2.75	2.25	1.0	-0.25	-1.75
Gross State Product <sup>(c)</sup>	1.4	2.0	2.0	2.75	1.25	1.5
<b>Labour market</b>						
Employment	0.4	1.0	1.5	1.5	1.75	1.5
Unemployment Rate <sup>(d)</sup>	6.1	7.0	6.5	6.0	5.5	5.5
Participation Rate <sup>(d)</sup>	67.5	68.2	68.2	68.2	68.2	68.3
<b>Population</b>						
Population	1.4	0.8	0.8	0.7	1.0	1.3
Working Age Population (15-64)	0.7	0.2	0.2	0.5	0.9	1.2
<b>Prices</b>						
Consumer Price Index <sup>(e)</sup>	1.3	1.5	1.5	1.75	1.75	2.0
Wage Price Index	1.7	1.5	1.5	1.75	2.0	2.25
Median House Price	-2.5	0.7	1.3	1.2	4.1	4.3
<b>Other key parameters <sup>(d)</sup></b>						
Exchange Rate \$US/\$A (US cents)	67.1	72.6	74.8	77.3	77.3	77.3
Iron Ore Price (\$US/t) cost and freight inclusive (CFR)	92.9	103.7	134.3	65.6	64.0	64.0
Crude Oil Price (\$US/barrel)	51.3	40.8	46.0	53.5	51.7	50.9

(a) Based on 2019-20 annual State Accounts data, updated with the latest State Final Demand and Balance of Payments data for the September quarter 2020.

(b) Net exports refer to international trade in both goods and services.

(c) Forecasts for ownership transfer costs, international trade in services and the balancing item are not separately reported.

(d) Data expressed as an annual average during the financial year.

(e) CPI growth rates in 2020-21 and 2021-22 are based on the total index excluding the electricity sub-index.