OUTLOOK

July 2019 | Chamber of Commerce and Industry of Western Australia (Inc)

Invested in the WA economy

ABOUT OUTLOOK

Outlook is CCIWA's biannual analysis of the Western Australian economy. All growth rates cited in **Outlook** are calculated in terms of year-on-year growth, comparing four quarters of data to the previous four quarters of data, unless otherwise stated. The editor of **Outlook** is Dan Norrie, Senior Economist.

Chamber of Commerce and Industry WA

Outlook at a glance

Western Australia is still struggling to find its groove. Lower business investment has affected employment and consumption in the WA economy since 2012. We expect resources investment to pick up in 2019-20, however a looming trade war between our largest trading partner and largest foreign direct investor, combined with an already slowing China presents longer term concerns for the future of the economy. In the short term, China's policy response will affect growth in the WA economy. If China stimulates its economy with Government funded infrastructure spending, WA's exports will capitalise off this investment from increased demand for iron ore, or alternatively the State's growth could remain subdued.

Two consecutive reductions in the cash rate by the RBA, combined with income tax relief for income taxpayers, will provide stimulatory increases in disposable income for WA households. Cost of living remains the most commonly cited barrier to confidence growth for West Australians so this relief will be welcome. Retailers, among other sectors, continue to report low demand as their key barrier to growth, and given that unemployment in the retail sector remains higher than other sectors, an increase in demand from changes in national policy will support employment.

Youth unemployment remains a significant issue for the State and currently sits at 11.2 per cent. A combination of struggling retail, which is an important employer of entry level young people looking for work, and low commencements in training are contributing to our higher than expected youth unemployment.

Declining business investment and dwelling investment, flat consumption growth and lacklustre population growth have weighed on the economy in 2018-19. It's difficult to see the financial year just passed end in anything other than a contraction of the domestic economy, with State Final Demand expected to decrease by 1 per cent in 2018-19.

Surging iron ore prices are driving unexpected growth in the value of WA's exports. Weather events in the north west that temporarily prevented exports have resulted in an overall decline in exports of $0.7 billion in March, but we expect export volumes will recover on the back of increasing capacity and higher prices. Even though the domestic economy is expected to shrink, we forecast that Gross State Product, which includes exports, to have grown by 2 per cent in 2018-19 and will continue to grow over the forecast period.

Over the last ten years, investment in resources projects in WA has accounted for around 80 per cent of total investment in the WA economy (and around 25 per cent of national business investment). These investments have been the primary drivers of employment growth and labour productivity. Since 2013, the fall in headline business investment has reduced demand for labour. Disposable income per capita and total hours worked are no higher than they were in 2012, which in part explains why employment and consumption growth in WA is sluggish.

The magnitude of resources investment has concealed issues affecting investment by small and medium-size enterprises (SME) which account for around 50 per cent of total employment. It appears that SME investment has been falling by

The importance and magnitude of business investment in large projects in Australia has concealed issues affecting small and medium-size businesses

2 per cent per year on average since 2013, based on bank lending to businesses for construction and real property. Low profit growth is affecting the ability of businesses to invest and generate additional employment. Since 2013, unincorporated real gross operating profits have increased at just 1.6 per cent per year on average. Higher costs of production and inflation in the wider economy, combined with minimal demand growth, has limited profitability for SME business owners.

Falling connections by business to the electricity network (11.8%) and gas network (2.1%) in 2017-18 signal the closure of physical shops and premises in net terms. Across WA, business exits have been concentrated in construction and agriculture, while headline business counts have been supported by significant growth in business registrations for rideshare drivers in metro areas. We take a deep dive into some of these issues in the special section: *Invested in the WA economy.*

Looking forward, the main factors that will drive the WA economy include:

- increased business investment in major resources projects – which will support an improvement in employment and consumption;
- a fall in dwelling investment in 2019-20 and then an increase in dwelling investment to respond to increasing population growth; and
- growth in export volumes in 2019-20, and lower growth in export volumes in 2020-21 and 2021-22.

We believe demand for skilled workers will place upward pressure on some wages but this will not result in broad based growth in wages in the next few years. Until the unemployment rate falls closer to the RBA (recently revised) level of full employment of 4.5 per cent it is difficult to see more sustained growth in wages.

Section 1: Economic Outlook

Economic forecasts for Western Australia

Forecasts[1]	**2017-18[2] Actual**	**2018-19 Forecast**	**2019-20 Forecast**	**2020-21 Forecast**	**2021-22 Forecast**
Economic Activity					
Household Consumption	1.6%	0.7%	1.2%	1.5%	2.0%
Dwelling Investment	-2.8%	-2.0%	-1.0%	2.0%	4.0%
Business Investment	0.1%	-12.0%	6.0%	9.0%	5.0%
State Final Demand	1.1%	-1.0%	2.0%	3.0%	2.0%
Exports[3]	4.3%	5.0%	4.0%	2.5%	2.5%
Imports[3]	-3.6%	-4.0%	3.0%	5.0%	2.0%
Gross State Product	1.9%	1.75%	3.0%	2.5%	2.5%
Labour Market					
Unemployment	6.1%	5.8%	6.0%	5.9%	5.9%
Inflation	0.9%	1.2%	1.5%	1.7%	1.9%
Wages	1.5%	1.6%	1.7%	1.9%	2.0%

Footnotes:

1 Forecasts are produced in terms of year-on-year growth, comparing four quarters of data to the previous four quarters of data.

2 Actual outcomes as reported in the 2017-18 State Accounts (ABS Cat. 5220.0).

3 Exports and imports figures are for goods and services trade measured on a Balance of Payments basis.

Economic Growth

Forecasts	**Economic Activity: State Final Demand**	**Economic Activity: Gross State Product**
2017-18 Actual	1.1%	1.9%
2018-19 Forecast	-1.0%	1.75%
2019-20 Forecast	2.0%	3.0%
2020-21 Forecast	3.0%	2.5%
2021-22 Forecast	2.0%	2.5%

A fall in business investment, flat consumption growth of 0.9 per cent (driven by population growth of 0.9 per cent) and low dwelling investment have weighed on the WA economy in 2018-19. Our forecast for a one per cent reduction in State Final Demand is on track.

Due to weather events in the Pilbara in March, iron ore exports fell by $0.7 billion. However, we expect exports will recover strongly in the June quarter of 2019 on the back of high iron ore prices. We consider that our forecasts for 5 per cent growth in exports and 2 per cent growth in GSP in 2018-19 are on track.

The WA economy will expand more robustly as a result of major investments in resources projects over the next three years. It appears that this will be supported over the medium term by higher iron ore prices, held up by strong Chinese demand (and some low port inventories) and more persistent supply issues in Brazil than previously expected following the tailings dam disaster in January.

Household consumption grew 0.9 per cent over the year to March 2019, which includes the most recent quarter of 0.1 per cent growth

Household Consumption

Forecasts	Economic Activity Household Consumption
2017-18 Actual	1.6%
2018-19 Forecast	0.7%
2019-20 Forecast	1.2%
2020-21 Forecast	1.5%
2021-22 Forecast	2.0%

We have revised down our forecasts for consumption growth due to low growth in income and consumer spending. We forecast that consumption will grow by 0.7 per cent in 2018-19 (0.8 percentage points lower) and 1.2 per cent in 2019-20 (0.3 percentage points lower).

Household consumption grew 0.9 per cent over the year to March 2019, which includes the most recent quarter of 0.1 per cent growth. These small increases were driven by increased spending on rent and other dwelling services, food, health and insurance and financial services. There was negative spending growth in discretionary categories, including furnishings and household equipment, purchase of vehicles and hotels, cafes and restaurants.

Consumption growth is flat because gross disposable household income per capita is no higher than it was in 2012 at the peak of business investment in WA. Additional factors that have contributed to flat disposable income include:

- the total number of hours worked in WA is the same as it was in 2012 (despite population growth);
- although total hourly rates of pay excluding bonuses have increased by 11.5 per cent since 2013 (or 2 per cent per year on average), total average weekly earnings are at the same level they were in 2013.
- costs continue to increase and directly reduce disposable income. For example, since 2012, council rates have been growing around 5 percentage points higher each year than growth in average weekly earnings, on average.

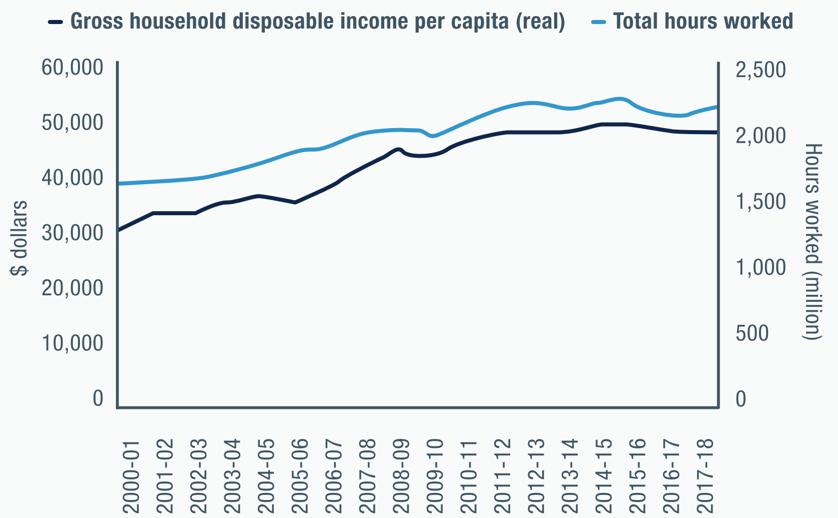
This has meant that growth in household consumption spending has been driven by population growth (both 0.9 per cent) and underemployment remains a major issue in the WA economy.

The *CCIWA Consumer Confidence Survey* shows that consumers have become more confident about the WA economy but remain concerned about cost of living pressures. This aligns with electricity network data which shows that the number of people on electricity instalment plans has doubled over the past two years to 1.9 per cent, and the average bill debt is higher in regional areas.

Recent reductions in the cash rate, along with Federal Government income tax cuts, will act as stimulus to households and support additional discretionary spending. Consumption growth will also be supported by increased employment of skilled workers that are required for major projects that will ramp up in the coming years.

The *WA Super - CCIWA Business Confidence Survey* shows that retail businesses cite weak demand as the most significant barrier to growth.

Chart 1: Gross Disposable Income Per Capita (Real) and Total Hours Worked



Source: ABS, CCIWA

Business Investment

Forecasts	Economic Activity Business Investment
2017-18 Actual	0.1%
2018-19 Forecast	-12.0%
2019-20 Forecast	6.0%
2020-21 Forecast	9.0%
2021-22 Forecast	5.0%

Business investment has fallen significantly so far in 2018-19 (down 8.4 per cent as of March 2019) because major LNG projects that were under construction have finished and new projects have not made up the difference. However, we may have underestimated the ramp up of spending on major new or replacement projects in the January Outlook.

We forecast that investment will increase by 6 per cent in 2019-20 due to increased spending on various resources projects. We forecast that spending will increase by 9 per cent in 2020-21 and by 5 per cent in 2021-22. This bout of investment includes:

1. projects to maintain existing export capacity (e.g. to replace existing mines);
2. new projects to commercialise new resources (e.g. due to sustained demand for lithium or rare earths due to the electric vehicle boom – see our *WA's Future in the Lithium Battery Value Chain* report); and
3. possible LNG projects, depending on world LNG prices and timing.

Small and medium sized enterprises (SME) account for around half of total employment in WA but a far smaller share of business investment, which has meant that changes to SME investment are obscured by changes in spending on major projects (e.g. iron ore and LNG). One proxy for SME investment at a state level is bank lending to businesses for construction or purchase of real property. This is a good proxy because SMEs rely more on banks for finance, while large businesses are less dependent on banks to access capital.

Using this proxy, we believe that SME investment has been falling by 2 per cent per year on average over the past five years. Given these businesses employ half of WA workers, it presents a worrying sign of confidence in the future of the economy. Bank lending for property also fell by 10.3 per cent over the year to March 2019 in WA.

Low profit growth is affecting the ability of businesses to invest and generate additional employment. Since 2013, unincorporated real gross operating profits have increased at just 1.6 per cent per year on average.[1] Higher costs are not helping.

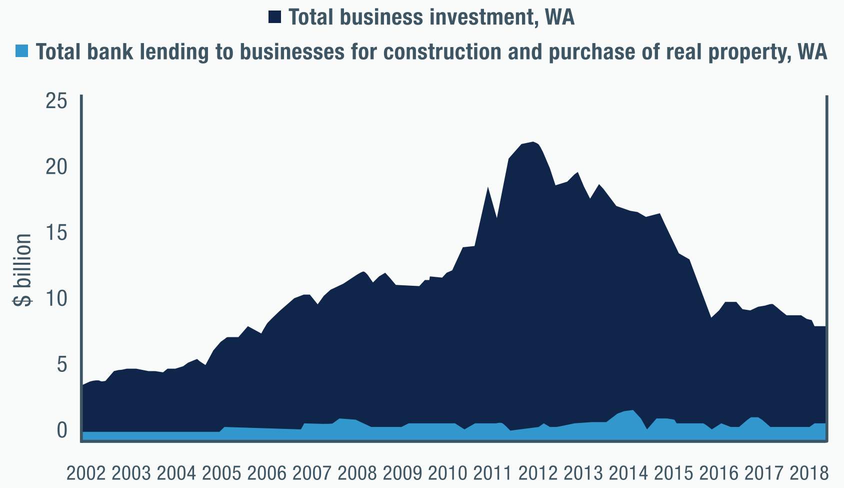
Businesses across various sectors have experienced low or negative growth in revenue. At the same time, costs are growing faster than revenue. This is affecting the ability of businesses to invest and generate additional employment, particularly in industries outside of the resources sector that are not exposed to relatively high world commodity prices (see Table 2: 2013-2018 Industry performance on page 12).

This is seen in the retail industry where producer prices for the output of the retail industry have fallen by 0.4 per cent per year on average since 2013, but input costs have increased. For example, total hourly rates of pay excluding bonuses have increased by 2.1 per cent per year on average and council rates have increased by 6.2 per cent per year on average.

Retail revenue has fallen. Since 2013, total factor income has fallen by 0.6 per cent per year on average, total employment has fallen by around 1.6 per cent per year on average and total compensation of employees has been flat (0.1 per cent). Profits have also fallen – retail gross operating surplus and gross mixed income has fallen by 0.6 per cent per year on average.

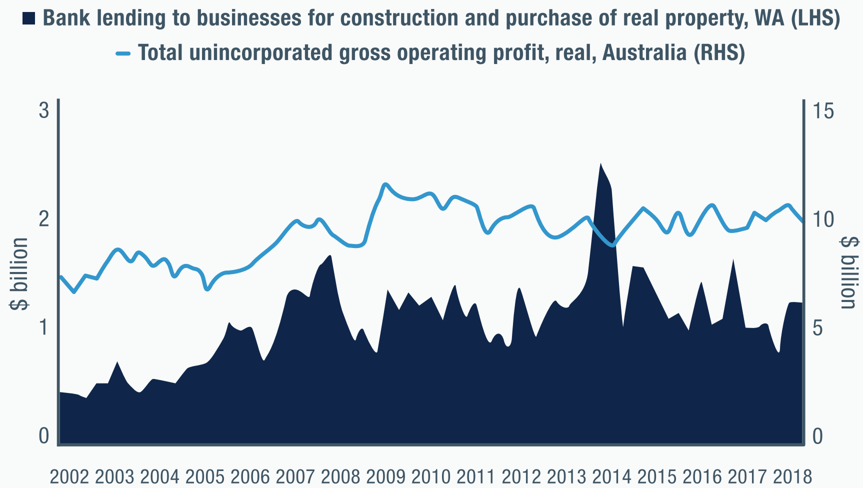
The Productivity Commission has highlighted that Australia wide business investment in capital is at a worryingly low level and is negatively affecting labour productivity and output in the economy. We explore some of these issues affecting business investment and their impacts in the special section: *Invested in the WA economy.*

Chart 2: Business Investment and Bank Lending to Business for Construction and Purchase of Real Property, WA



Source: ABS, CCIWA

Chart 3: Lending to Businesses and Total Unincorporated Real Gross Operating Profit



Source: ABS, CCIWA

Note: Current prices adjusted using implicit price deflator

1 Measured as a cumulative average growth rate. Current prices adjusted using implicit price deflator.

Dwelling Investment

	Economic Activity
Forecasts	**Dwelling Investment**
2017-18 Actual	-2.8%
2018-19 Forecast	-2.0%
2019-20 Forecast	-1.0%
2020-21 Forecast	2.0%
2021-22 Forecast	4.0%

We forecast a 2 per cent decrease in dwelling investment in 2018-19 (revised down 1 percentage point). Dwelling investment has fallen in each quarter in FY 2018-19 and fell by 3.5 per cent in the March quarter. Some factors that continue to impact dwelling investment include reductions in housing finance commitments (down 10 per cent) and the effect of a soft national housing market.

We forecast that dwelling investment will fall by 1 per cent in 2019-20 (down 2 percentage points), due to a 14 per cent reduction in the number of building approvals to May 2019. Builders have attributed this fall to a soft lending market and also regulatory delays. For example, the new *Apartment Design Guide* will require applicants to go through an additional approval process, causing additional requests for information prior to the issuance of permits and conditions. It is estimated that this will delay some projects by an additional six months.

Recent interest rate cuts will make it more attractive for people to invest in dwellings. A relaxation of Australian Prudential Regulation Authority lending standards will make it possible for people to take out larger loans. These factors will bring forward some dwelling investment. Although the vacancy rate has declined, it appears that this has been driven by slow supply growth, rather than higher demand, given soft population growth.

We forecast that dwelling investment will increase by 2 per cent in 2020-21 and by 4 per cent in 2021-22 because of some additional spending to respond to population growth and increased business investment in WA. Changes to Keystart eligibility may also bring forward some dwelling investment. However, some downside risks include a fall in construction traineeships (see page 17), credit conditions and the expiry of interest only loans (described below).

> Factors that continue to impact dwelling investment include reductions in housing finance commitments and the effect of a soft national housing market

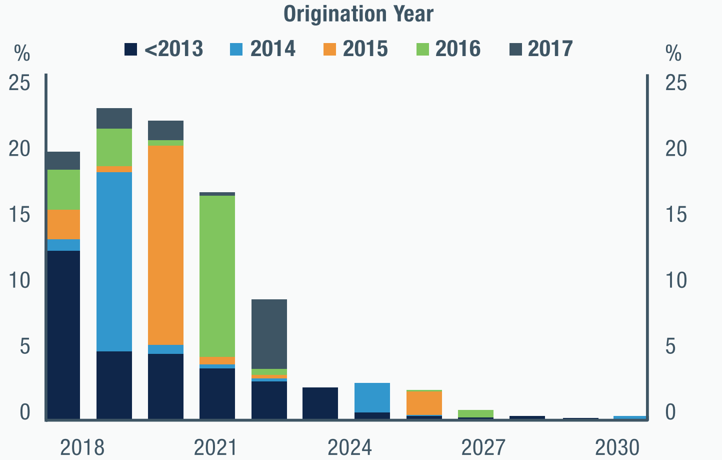
Interest-only loans

An interest-only loan is a loan in which the borrower services the interest component of an amount borrowed during a fixed time period, while the principal balance remains unchanged. When the interest-only period expires (commonly 5 years), the borrower must then repay both the interest and principal balance components.

According to the Reserve Bank of Australia, around two-thirds of Australian interest-only loans will expire and roll over into principal-and-interest loans by 2020. In value terms, this equates to around $360 billion over the next three years, or around 7 per cent of the total stock of housing credit available.

When this occurs, these borrowers will be required to service the interest component plus reduce the principal balance (initial amount borrowed). The immediate effect is that the borrower must reduce consumption spending to afford the additional payments or take other measures to repay the loan. These measures could include drawing down savings accounts, working more hours or selling their property or other investments.

Chart 4: Interest-Only Period Expiry
Share of Outstanding Securitised IO Mortgages; December 2017



Source: RBA

It is likely that many borrowers are smoothing their consumption levels and boosting their savings accounts to prepare for higher repayments when their interest-only period expires. This aligns with ABS data that shows weak discretionary spending in WA and suggests that the savings rate is higher than the national average.

However, subdued wages growth, cost of living pressures and a higher incidence of properties entering negative equity may limit the ability of some households to afford increased debt requirements or negotiate an extension to their interest-only period. This could apply downward pressure to household consumption growth and slow the recovery of WA's housing market.

International Trade

Forecasts	Economic Activity Exports	Imports
2017-18 Actual	4.3%	-3.6%
2018-19 Forecast	5.0%	-4.0%
2019-20 Forecast	4.0%	3.0%
2020-21 Forecast	2.5%	5.0%
2021-22 Forecast	2.5%	2.0%

Our forecast for 5 per cent growth in exports in 2018-19 is roughly on track. Due to weather events, total WA exports in March fell by $0.7 billion. A fall in iron ore exports accounted for 72 per cent of this decrease, but we expect exports will recover strongly in the June quarter 2019, in part due to higher prices that incentivise increased production.

High iron ore prices directly increase the value of exports in absolute terms. However, the Chain Volume measure used by the ABS removes these price effects in order to give a clearer picture on changes in total output or production in WA over time.

We forecast that exports will increase by 4 per cent in 2019-20 and 2.5 per cent in 2020-21 and 2021-22. This growth will come from new projects and projects that are ramping up output to respond to prices. Enhanced Chinese stimulus expectations have resulted in declining iron ore port inventories and supply issues in Brazil continue to persist. This indicates that higher than expected iron ore prices could be sustained beyond the immediate future, benefiting WA.[2]

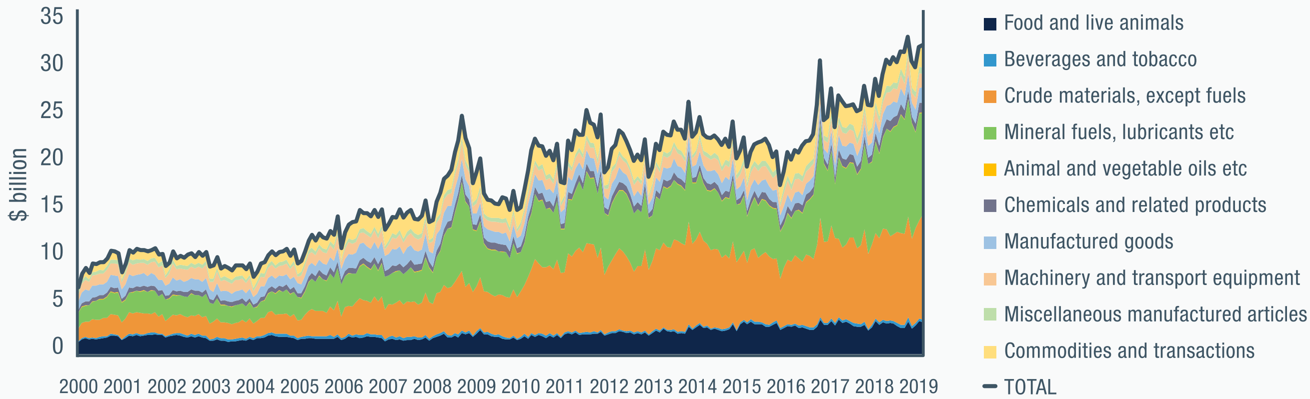
There are a range of projects in planning, discussed in the latest edition of *WA Works*. However, some of these projects maintain existing capacity (rather than add to export volumes) and others will take years for planning and construction.

The trade dispute between the USA and China is affecting international trade. According to the OECD, growth in global trade is expected to fall from 3.9 per cent in 2018 to 2.1 per cent in 2019.

It is not easy to identify the most likely outcome of global geopolitics and their effects on a network of WA's trading relationships given China's expanding integration in each corner of the global economy. For example, as a proportion of global trade, China's trading relationship with the European Union is at a similar level to China's trading relationship with the United States (around 3 per cent). Any falls in international trade that affect Europe will also affect Australia through their effect on production in the Chinese economy.

Our expectations of a China/US trade war and its impact on the WA economy remain unchanged from the last edition of *Outlook* – that WA has more to lose than any other state.

Chart 5: WA Merchandise Exports, Monthly



Source: ABS, CCIWA

2 However, price effects will be smoothed out in the State Accounts as exports in chain volume terms are adjusted for price inflation.

Unemployment

	Economic Activity
Forecasts	**Unemployment**
2017-18 Actual	6.1%
2018-19 Forecast	5.8%
2019-20 Forecast	6.0%
2020-21 Forecast	5.9%
2021-22 Forecast	5.9%

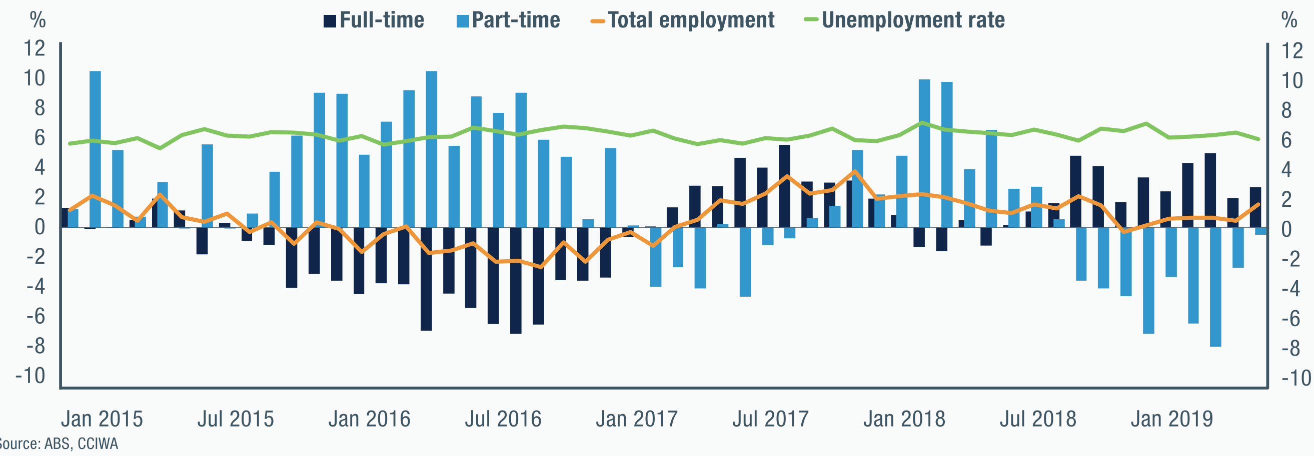
Since 2015, the unemployment rate has averaged 6.0 per cent. The unemployment rate fell to 5.8 per cent in June 2019.

This year has seen growth in full-time employment and a loss of part-time positions. The number of full-time employees increased by 2.6 per cent since this time last year. The number of part-time employees fell by 0.5 per cent since this time last year.

We forecast that the unemployment rate will remain at 6.0 per cent throughout 2019-20. We expect that increased mining investment will stimulate full-time employment in this industry, which is currently reflected in high job advertisements for mining-related trade qualifications. However, we are concerned by low consumption growth, dwelling investment and investment by small businesses (who account for around 40 per cent of employment in WA).

> We are concerned by low consumption growth, dwelling investment and investment by small businesses (who account for around 40 per cent of employment in WA)

Chart 6: Growth in Full Time and Part Time Employment and the Unemployment Rate, WA, 2015-2019



Source: ABS, CCIWA

Wages and Inflation

	Economic Activity	
Forecasts	**Inflation**	**Wages**
2017-18 Actual	0.9%	1.5%
2018-19 Forecast	1.2%	1.6%
2019-20 Forecast	1.5%	1.7%
2020-21 Forecast	1.7%	1.9%
2021-22 Forecast	1.9%	2.0%

Private sector wages have grown, increasing by 1.7 per cent to March 2019. Competition for skills in resource projects will continue to place some upward pressure on wages. However, these projects and their employment represent a small fraction of total employment which will limit their ability to grow wages across the entire WA economy in the short term.

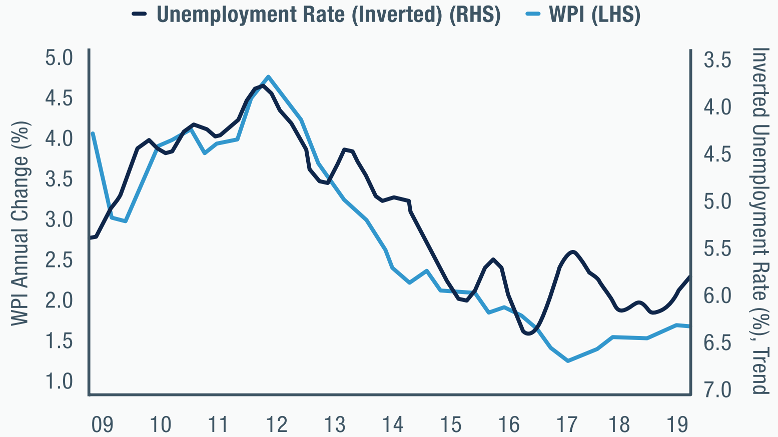
SMEs are experiencing difficult operating conditions, as seen in low unincorporated gross operating profit and low investment (see *Invested in the WA economy* on page 10). This will limit the ability of small and medium size businesses to grow employment and to pay higher wages. Small businesses account for around 40 per cent of employment in WA.

Chart 7 displays the relationship between wages and the unemployment rate (inverted). When businesses have a lot of work and demand and experience profitable conditions, this places upward pressure on wages (and vice versa). Since we are conservative about employment growth, we do not consider that employment pressure will place much upward pressure on wages.

To grow employment, actions are required that make it easier for businesses to invest in profitable projects. Results from the *WA Super – CCIWA Business Confidence Survey* suggest that demand is not keeping up with growth in business costs. Other issues include access to skills and risks and uncertainty that deter businesses from starting new projects.

We believe inflation will remain low while wages growth remains subdued as a result of elevated unemployment. The reduction of the cash rate will result in some additional discretionary spending, providing some inflationary pressure. However, we are conservative about issues affecting employment and wage growth and their impacts on consumer spending. Retailers will continue to use discounting to compete with increasing online spending and attract customers and this will continue to place downward pressure on CPI.

Jobs and Wages in WA
Unemployment Rate (%) and Wage Price Index (WPI)



Source: Refinitiv Datastream; CCIWA (2019)

Special section: Invested in the WA economy

Growth in the Australian economy has been driven by corporate businesses, particularly in mining. Mining capital expenditure has accounted for 80 per cent of total capital expenditure in WA over the last ten years. The driver of this investment has been higher world prices for commodities, including iron ore.

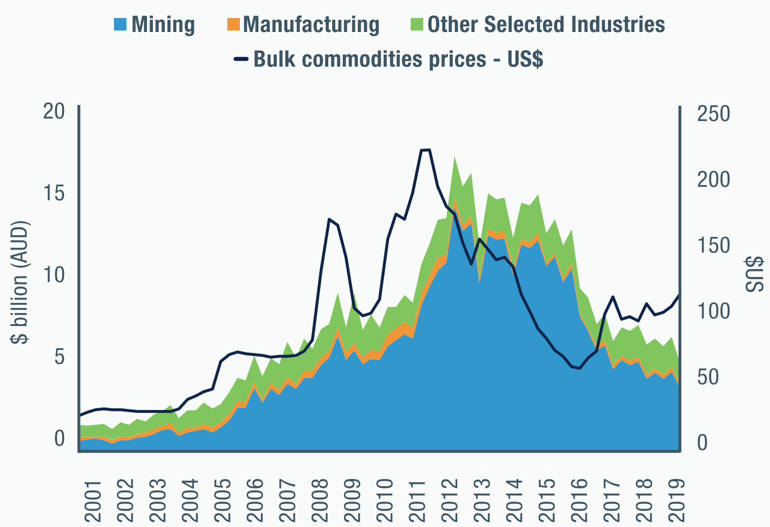
SMEs account for around 98 per cent of businesses in WA and half of total employment, but a small share of total investment. This means that it is difficult to understand changes in SME investment based on aggregated investment data. However, bank lending to businesses for construction or purchase of real property can act as a proxy. This is because SMEs rely more on banks for finance. Based on this, it appears that SME investment has remained a small share of total business investment in WA.

Over the past five years, SME investment has been falling by 2 per cent per year on average, based on bank lending to businesses for construction and real property. Bank lending for property fell by 10.3 per cent over the year to March 2018 in WA.

This is associated with concerns expressed by the Productivity Commission about capital shallowing in the Australian economy.

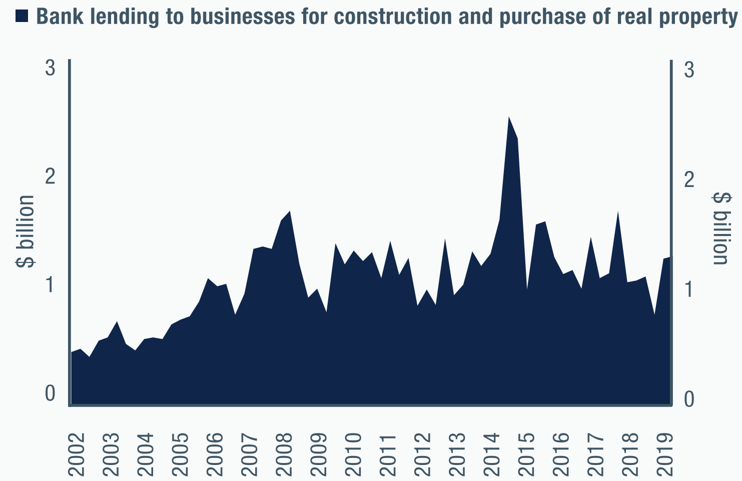
It appears that these investment issues are associated with low profitability of unincorporated businesses and changes in the composition of businesses in WA.

Chart 8: Actual Capital Expenditure, Western Australia



Source: ABS, CCIWA

Chart 9: Bank Lending for Property in WA



Source: ABS, CCIWA

Profits and investments

There is a strong relationship between business profits and investment. An entrepreneur who is considering an investment in a new project must expect to earn profits to put savings and earnings at stake and face risk and uncertainty.[3]

There has been a divergence between the profitability of large businesses and SMEs in Australia over the last 20 years (Chart 10). Over the past five years, in real terms:

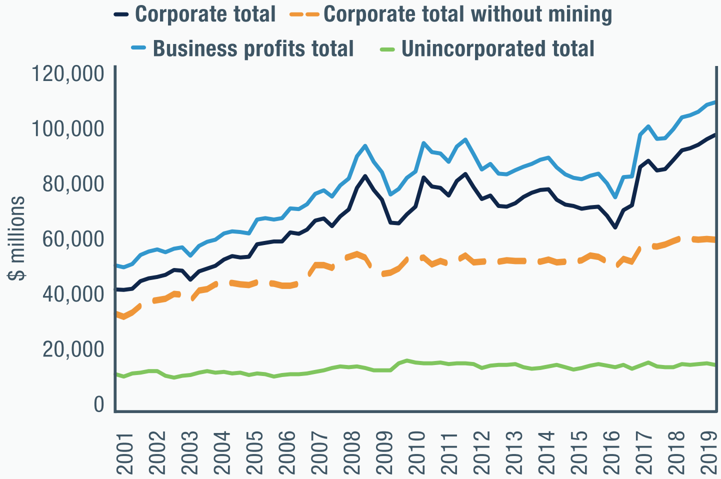
1. total business gross operating profits have increased by 4.1 per cent per year on average;
2. when we take out the mining industry, total business profits have increased at 2.8 per cent per year on average; and
3. total unincorporated gross operating profits have increased by 1.6 per cent per year on average.[4]

This suggests that corporate businesses, particularly miners, have supported most of Australia's economic performance, employment growth and labour productivity. Miners have been incentivised by high world prices for commodities to take on debt (i.e. earn negative profits) and fund significant capital expenditure and are now earning profits, helping to repay their original investments.

Profit conditions are markedly different across sectors and locations, with construction, retail and accommodation and food services experiencing particularly difficult conditions (Chart 11).

> There has been a divergence between conditions experienced by corporate businesses and unincorporated businesses (mostly small and medium-size businesses)

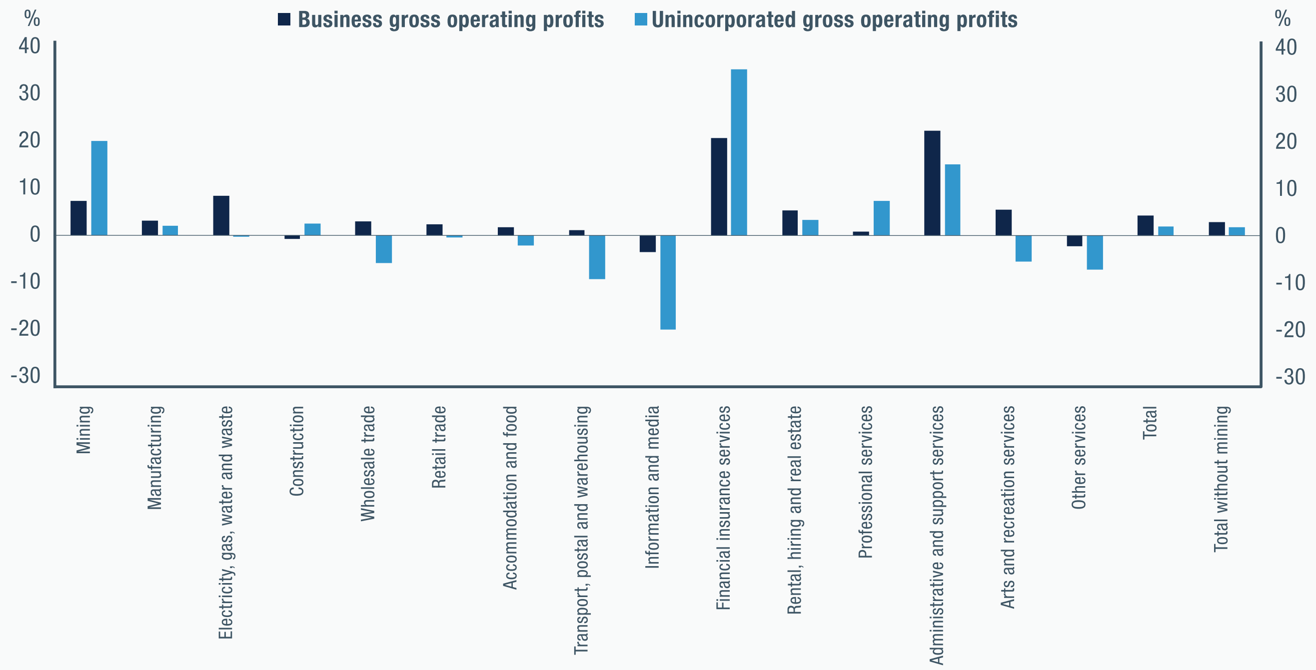
Chart 10: Total Business, Corporate and Unincorporated Gross Operating Business Profits, Real , Australia



Source: ABS, CCIWA

Note: Current prices adjusted using implicit price deflator

Chart 11: Change in Business and Unincorporated Gross Operating Profit, Real, 2013-2018



Source: ABS, CCIWA

Note: Current prices adjusted using implicit price deflator

3 Knight, F. H. (1921). Risk, uncertainty and profit. Courier Corporation.

4 Unincorporated profit data is not available at a state level. Current prices adjusted using implicit price deflator.

WA businesses have been experiencing tougher conditions than the national average, as seen in data on the construction, retail and accommodation industry

On average, SMEs are not earning much more profit or reward than they did in 2001 (despite innovation and entrepreneurial activity). Since 2001, the profit earned by an average unincorporated business in Australia has increased at just 0.2 per cent per year on average (Chart 12).[5]

WA businesses have been experiencing tougher conditions than the national average, as seen in data on the construction, retail and accommodation industry (Table 2). Revenue growth is poor (due to factors including reduced business investment and low population growth) and higher costs have not been helping. This has meant that businesses' costs have been growing faster than revenue.

For example, since 2013 producer prices for the output of building construction have increased by 0.3 per cent per year on average. Input costs have increased at a faster rate: total hourly rates of pay excluding bonuses have increased by 2.1 per cent per year on average and construction material costs have increased in Perth by 1.6 per cent per year on average.

This is associated with a fall in construction revenue – since 2013 total factor income has fallen by 6.7 per cent per year on average, total employment has fallen by around 3 per cent per year on average and construction sector total compensation of employees has fallen by 4.6 per cent per year on average. Profits have also fallen – construction sector gross operating surplus and gross mixed income has fallen by 10 per cent per year on average.

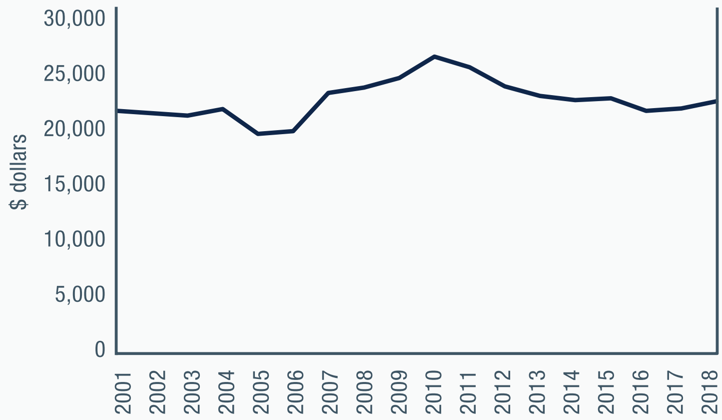
Since 2013, growth in council rates in WA has been around 5 percentage points higher each year on average than growth in real unincorporated profits.

Changes in the number and composition of businesses in WA

These issues are also seen in data on business premises in WA. There was an 11.8 per cent net reduction in business connections to the electricity network in WA in 2017-18 and a 2.1 per cent net reduction in business connections to the gas network.[6]

Australian Securities and Investments Commission data indicates that the number of companies entering external administration in WA increased from 700 companies on average from 2010-11 to 2013-14 to 930 on average from 2014-15 to 2017-18. However, this only explains some of the business disconnections.

Chart 12: Mean Unincorporated Business Profit in Australia, Real



Source: ABS, CCIWA

Note: Current prices adjusted using implicit price deflator

Table 2: 2013-2018 Construction, retail and accommodation and food services industry performance in cumulative average growth rates (average annual per cent growth per year)

	Construction	Retail	Accommodation and food services
Output prices			
Producer prices	0.3%	-0.4%	2.1%
Input prices			
Total hourly rates of pay excluding bonuses	2.1%	2.1%	2.3%
Other costs - construction material costs	1.6%		
Total revenue			
Total factor income	-6.7%	-0.6%	0.1%
Total costs			
Total compensation of employees	-4.6%	0.1%	4.3%
Total profits			
Gross operating surplus and gross mixed income	-10.0%	-0.6%	-8.4%
Employment	-3.0%	-1.6%	4.4%

Source: ABS, CCIWA

5 Current prices adjusted using implicit price deflator.

6 Electricity and gas connections have increased in net terms, driven by increases in residential connections.

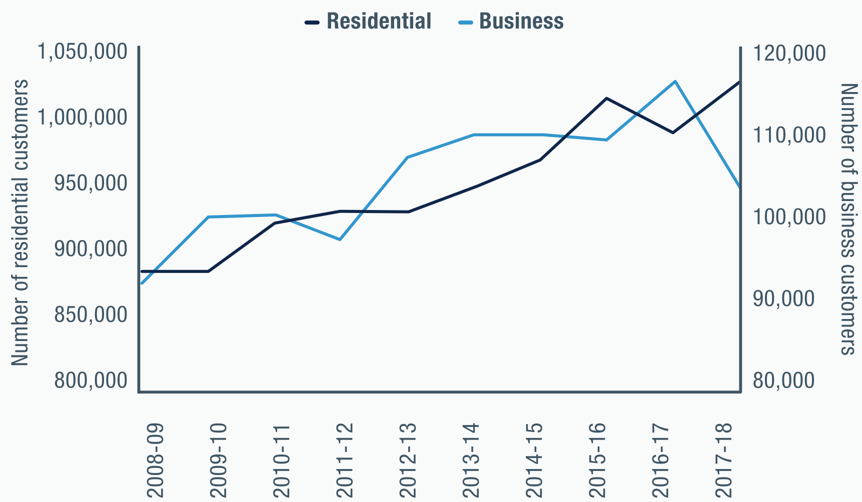
Business entries and exits

Chart 14 displays the largest changes in the number of business entries and exits by industry class (in net terms) for FY 2017-18. This shows that in FY 2017-18 in net terms:

- 1,600 additional transport businesses were added in WA in net terms in 'Other Transport Support Services n.e.c' and 'Taxi and Other Road Transport'. Rideshare drivers have driven growth in the ABS headline total business numbers, which have continued to increase at 1 per cent per year. These two categories alone accounted for the entire top 20 exits (in net terms);
- WA business exits have been concentrated in construction and agriculture. The top 10 exit categories accounted for 1,100 businesses (in net terms).

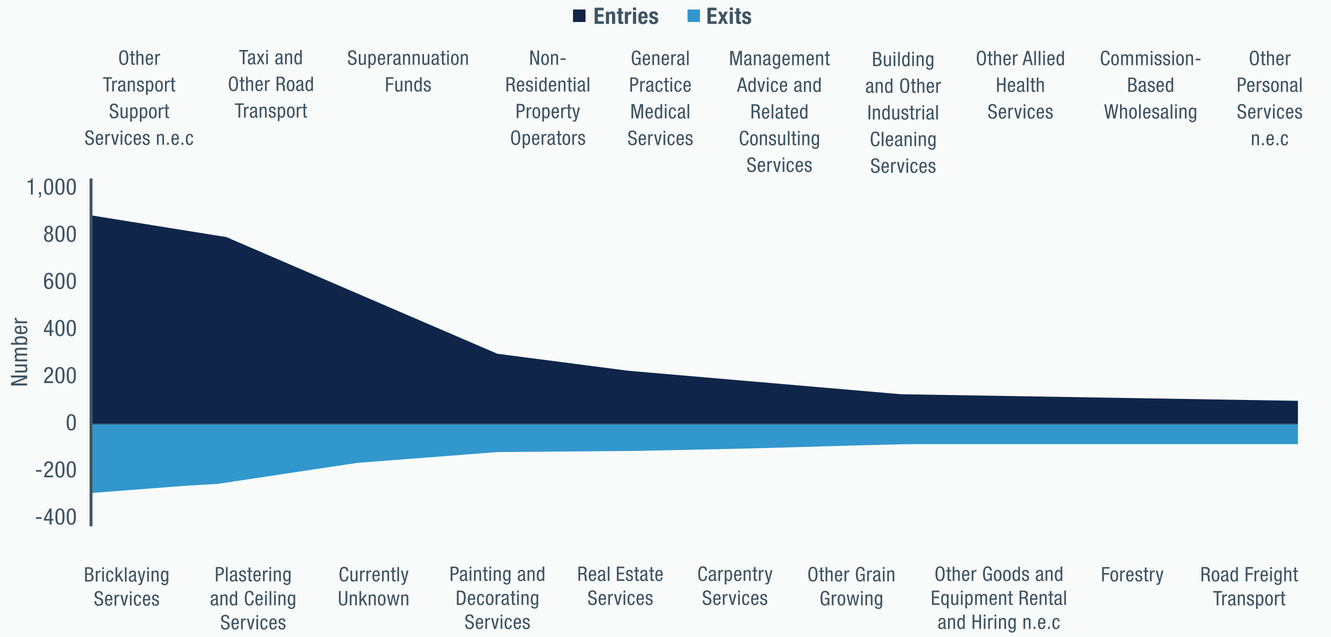
It appears that businesses who exited in FY 2017-18 may have been more likely to own or lease property and require an electricity connection, while those who have entered are less likely to require a fixed premises or an electricity connection (ie. rideshare drivers and services-based businesses). We expect that this will reduce investment levels by SMEs in the WA economy, particularly in property and construction.

Chart 13: Total Number of Residential and Business Electricity Customers 2009-2018



Source: ERA

Chart 14: Highest Entries and Exits by Industry Class in Net Terms, FY 2017-18, WA



Source: ABS, CCIWA

Apprenticeship and traineeship commencements in WA have fallen 38.9 percent between 2014 and 2018, driven in large part by falling business investment

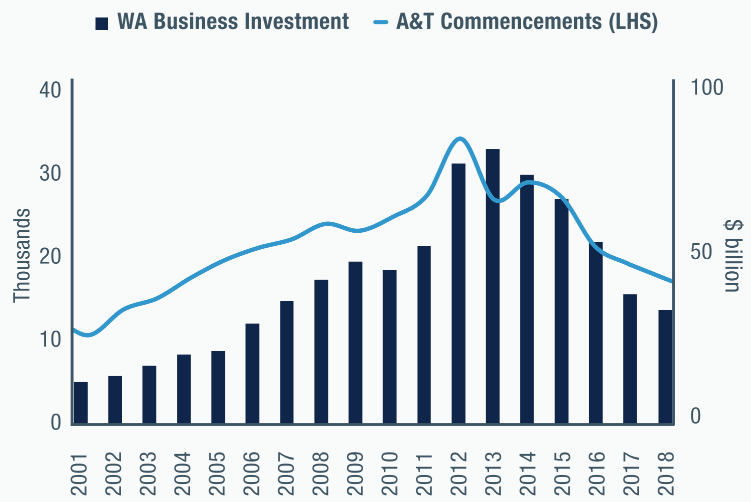
Impacts of business investment on employment, training and productivity

Investment has had a significant effect on enrolment in education and training in WA. Apprenticeship and traineeship commencements in WA have fallen 38.9 percent between 2014 and 2018, driven in large part by falling business investment.

Trade qualification commencements have fallen by 40.9 percent in the four years to December 2018, with construction industry trade commencements falling by 57.5 percent over the same period. However, commencements in automotive and engineering trade qualifications have grown by 13.2 per cent. This, combined with non-trade qualifications for machinery operators and drivers growing by 32 per cent since 2014, reinforces our view that the resources sector continues to drive improvements in the economy, but other activity remains subdued.

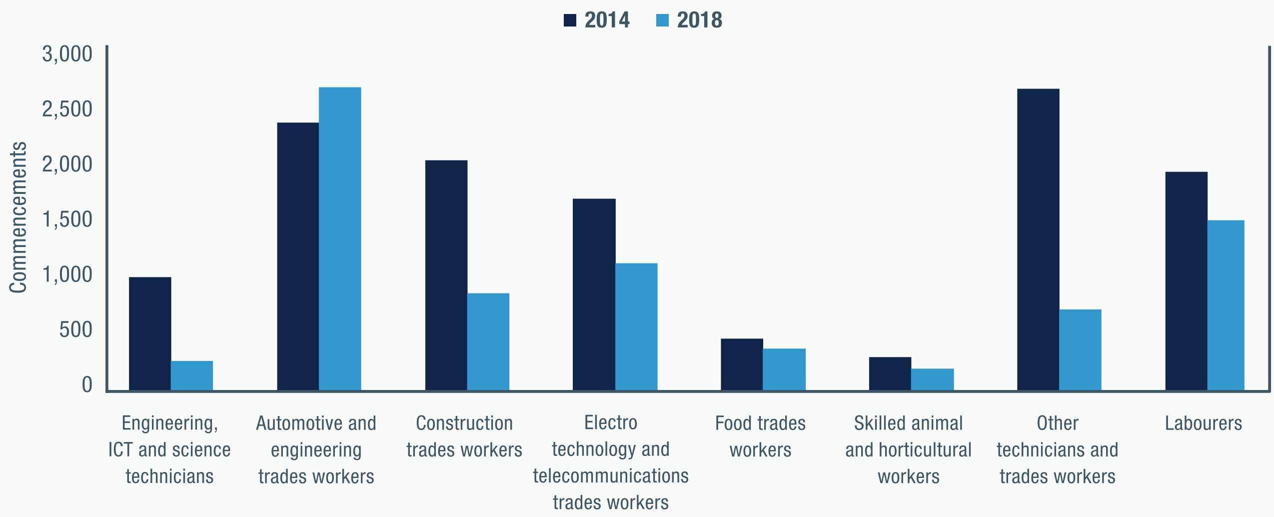
The removal of the payroll tax exemption has also impacted non-trade commencements, which have fallen by 37.6 per cent. Non-trade qualifications in areas that are usually seen as non-discretionary training have been the most impacted. Qualifications for managers and clerical workers have experienced the largest falls of 53.8 and 63.5 per cent respectively. Non-trade qualification commencements in the health and community sector fell 37 per cent in the four years to December 2018, whilst still being WA's largest non-trade commencement class in 2018. This reflects a growing demand for health and community services workers to support the roll out of the National Disability Insurance Scheme and an ageing population.

Chart 15: Business Investment and Apprenticeship and Traineeship Commencements in WA



Source: NCVER, CCIWA

Chart 16: Trade Commencements, WA



Source: NCVER, CCIWA

Source: NCVER, CCIWA

Impacts on WA productivity performance

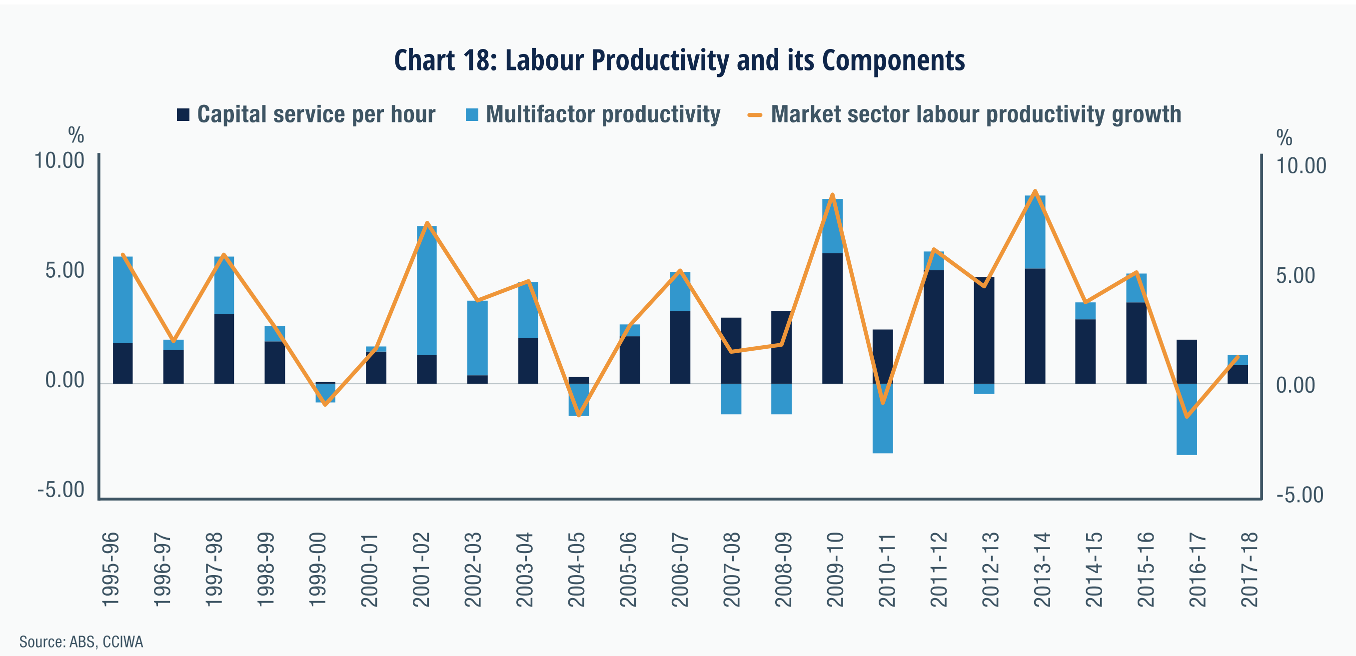
Business investment and skills training issues will continue to affect productivity growth in WA. Businesses that have invested in capital and machinery in the WA resources industry (and skilled workers and managers) are responsible for improvements in measures of WA labour productivity.

ABS data shows that labour productivity has grown at a compound annual growth rate of 3.5 per cent per year on average over the past ten years in WA. ABS data shows that this has been driven by business investment in capital (such as new projects, plant and machinery). Since 2008-09:

- Capital service per hour has grown at 3.4 per cent per year on average; while
- Multifactor productivity has grown at 0.2 per cent per year on average.

Low investment levels by SMEs do not bode well for productivity. Businesses that invest and adopt new technology are more likely to achieve productivity gains and employ additional workers, compared with those that do not.[7] This is associated with concerns expressed by the Productivity Commission about capital shallowing in the Australian economy.

Some productivity issues that are affecting businesses include continuity of work, rising costs for inputs including raw materials, longer delays starting projects including planning delays and more costly requirements to start new projects. A focus on identifying these problems and actions that address their causes will help to improve productivity and employment in WA.



Source: ABS, CCIWA

7 See: Koch, M, I Manuylov and M Smolka (2019), “Robots and firms”, CESifo Working Paper 7608. Summary available at https://voxeu.org/article/robots-and-firms

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