



OUTLOOK

September 2022 | Chamber of Commerce and Industry of Western Australia Limited

What goes up...

About Outlook

Outlook is the Chamber of Commerce and Industry of Western Australia's biannual analysis of the WA 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.

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Chamber of Commerce
and Industry WA



Outlook at a glance

The world economy is at a turning point. More than two years of strong economic momentum has come to an end, and it is clear we are in a very different environment to this time six months ago.

Gone are the days of large fiscal stimulus, rock-bottom interest rates and exuberant cash-splashing: key ingredients fuelling the global recovery from COVID-19.

Indeed, many of the factors that previously insulated economies from the impact of COVID-19 have now morphed into a new compendium of challenges, and global commentators are forecasting a sharp decline in global growth toward the end of this year.

So, what has poured cold water on a previously red hot global economic recovery? Three key factors.

First, sharp increases in the price of almost everything.

In a desperate effort to get inflation back under control, governments and central banks have broken the emergency glass – launching into a synchronised chorus of interest rate hikes and fiscal consolidation. In good news, the pace of inflation in the USA has started to ease, perhaps an early indication that contractionary monetary policy is doing its job.

Second, war erupted among nations that, together, play a significant role in the supply of key agricultural and energy commodities – triggering global food shortages and adding fuel to the inflationary fire.

Third, Australia's largest trading partner continued to double down on its commitment to achieve 'COVID-zero', slowing domestic economic activity and exacerbating issues in the construction and manufacturing sectors. Geopolitical tensions have also escalated, posing additional risks to the stability of our two-way trading relationship.

Western Australia is not immune to these global developments. CCIWA's quarterly *Business Confidence Survey* has revealed nine out of ten businesses are experiencing supply chain disruptions, with higher input costs and delivery delays identified as the two largest impacts. Ongoing skilled labour shortages inflict additional pain, with nearly four in five WA businesses struggling to fill skilled positions.

All together, these factors have damaged the growth plans and financial viability of many local businesses, with some labelling the current 'high-cost, high-demand' operating environment a 'profitless boom'.

But amidst an increasingly turbulent and unpredictable global economic backdrop, Western Australia's economic fundamentals remain on a solid footing.

The size of our domestic economy remains 9.3 per cent higher than pre-COVID levels and a record number of Western Australians are in full-time employment.

The strength of the household sector has been a fundamental driver of WA's economic performance. Initially underpinned by significant levels of government stimulus and closed international borders, WA's strong jobs market and higher wages have more recently played a leading role in stimulating consumer spending.

Looking ahead, the outlook for WA's economy remains largely positive and we are well positioned to navigate the next 12 months and beyond.

WA's resources sector will drive growth, but China remains a key risk

Business investment is expected to pick up materially this financial year, primarily underpinned by big ticket items like Woodside's Scarborough and Pluto 2 projects. The pipeline of investment in the critical minerals (e.g. lithium) sectors is also strong, which we expect will support growth in the years ahead.

At the same time, non-mining investment is expected to soften this financial year, as rising cost pressures and supply issues reduce project feasibility and force many businesses to re-think growth strategies.

On balance, the outlook for WA's iron ore export volumes remain favourable - with the Chinese government continuing to roll out policy support to boost domestic activity and achieve growth targets. Aggressive local government bond issuance has helped to finance a pick-up in fixed infrastructure investment and the government intends to launch a state-backed liquidity vehicle to support struggling developers.

A key source of uncertainty, however, is whether the Chinese government can achieve enough industry buy-in to offset the economic deceleration. With recent factory output and retail sales data coming in lower than expected, as well as ongoing weakness in the real estate and financial sectors - risks appear tilted to the downside.

Escalating geopolitical tensions have added to these anxieties, with our latest *Business Confidence Survey* revealing 2 in 5 businesses are looking to revisit their business strategy as result of trade issues in overseas markets.

Strong workforce demand will keep WA's jobs market tight and underpin wages growth

WA's robust investment pipeline – as well as an expected ramp up in the State Government's Asset Investment program - is expected to support strong demand for WA-based workers. As such, we expect the unemployment rate to average 3.75 per cent this financial year.

Sustained tightness in the jobs market will continue to flow through to wages growth, with an increasing number of WA businesses lifting base salaries to attract and retain skilled workers. Skilled labour shortages remain the top barrier to growth among WA businesses, and there are currently more job vacancies in WA than unemployed people (see chart).

We expect wages to grow 3.0 per cent this financial year before accelerating to 3.25 per cent in 2023-24.

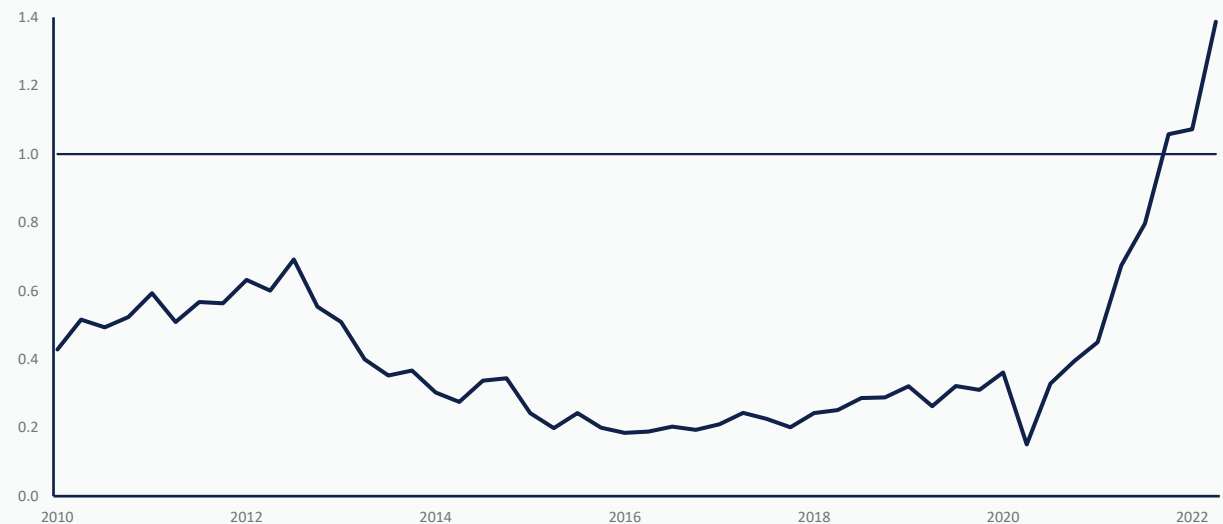
Consumer spending will slow as interest rates rise, but WA's jobs boom will cushion the blow

A range of competing forces make the consumption outlook particularly uncertain. On the one hand, a prolonged period of strong savings are providing a buffer to many households experiencing financial stress, and WA's tight labour market and strong wages outlook are expected to maintain healthy baseline levels of consumption.

On the other, rising interest rates and cost of living pressures will continue to tighten household budgets over the coming year. Our latest *Consumer Confidence Survey* revealed around three in four WA mortgage holders will cut back discretionary spending if the cash rate hits 2.5 per cent.

The return of international travel is also expected to weigh on spending as households save for their first overseas trip in over two years.

Job Vacancies per Unemployed Person - WA



Cash rate at which spending will be cut back



On balance, we expect consumption to slow to 1.75 per cent this year, before stabilising in 2023-24 and 2024-25.

The global war for talent will rage on, lifting the imperative to attract skilled workers

Net overseas migration will continue to recover throughout 2022-23 but will likely remain below pre-COVID levels as young and highly skilled workers relocate abroad, and ongoing visa processing delays curtail the inflow of long-term migrants. Global competition for skilled workers and international students will continue, lifting the imperative for WA to market itself as a destination of choice.

Cost blowouts and labour shortages will continue to stymie construction activity

WA's enormous pipeline of new housing construction is expected to support growth over the coming year, but two key challenges will remain.

First, rising interest rates and input cost escalation have applied significant pressure on prospective homeowners to meet construction obligations, leading to reports of higher fallover rates and uncompleted builds.

Second, lack of certainty around the cost outlook has increased project risk margins and significantly compromised the greenfield development pipeline. As such, we expect few major residential developments to commence in the next 12-18 months. With rising interest rates adding to cash-flow pressure, an uptick in business insolvencies remains likely over the coming year.

Inflationary pressures are set to ease in 2023

It's not just the construction sector; higher operating costs are a major concern for businesses across all sectors of the economy. Our latest *Business Confidence Survey* showed that rising costs are eviscerating the profits of Western Australian SMEs.

We expect inflationary pressures to persist throughout the rest of this year, before gradually easing as the global economy slows and commodity prices continue to stabilise.

Reflecting this view, we expect the RBA's cash rate to peak at around 2.85 per cent at the end of this calendar year before gradually unwinding in late-2023.



While risks to the overall outlook have intensified, WA's economy remains grounded on a solid foundation. Our strong economic and social resilience – reinforced throughout the COVID-19 pandemic – has positioned us well to traverse the next phase of economic, social and political uncertainty.

Amidst gloomy world economic headlines, it is important that we do not lose sight of Western Australia's unique advantages. We have world-leading resources and agricultural sectors, strong public finances and a stable political system - among many other attractive conditions.

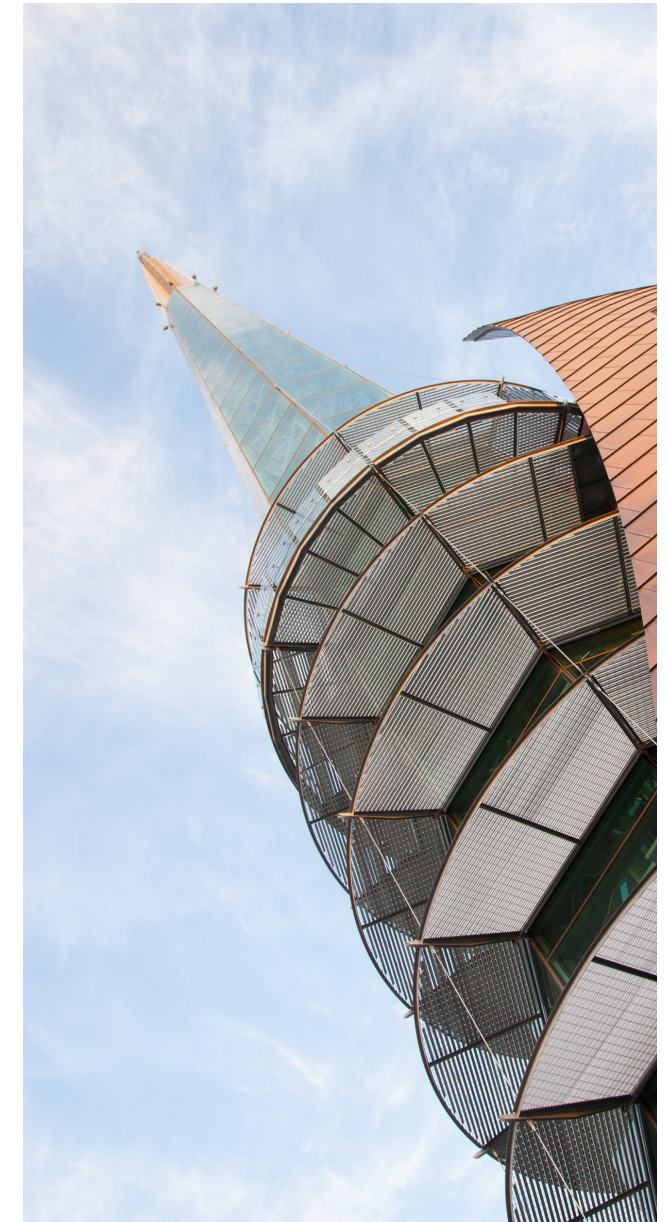
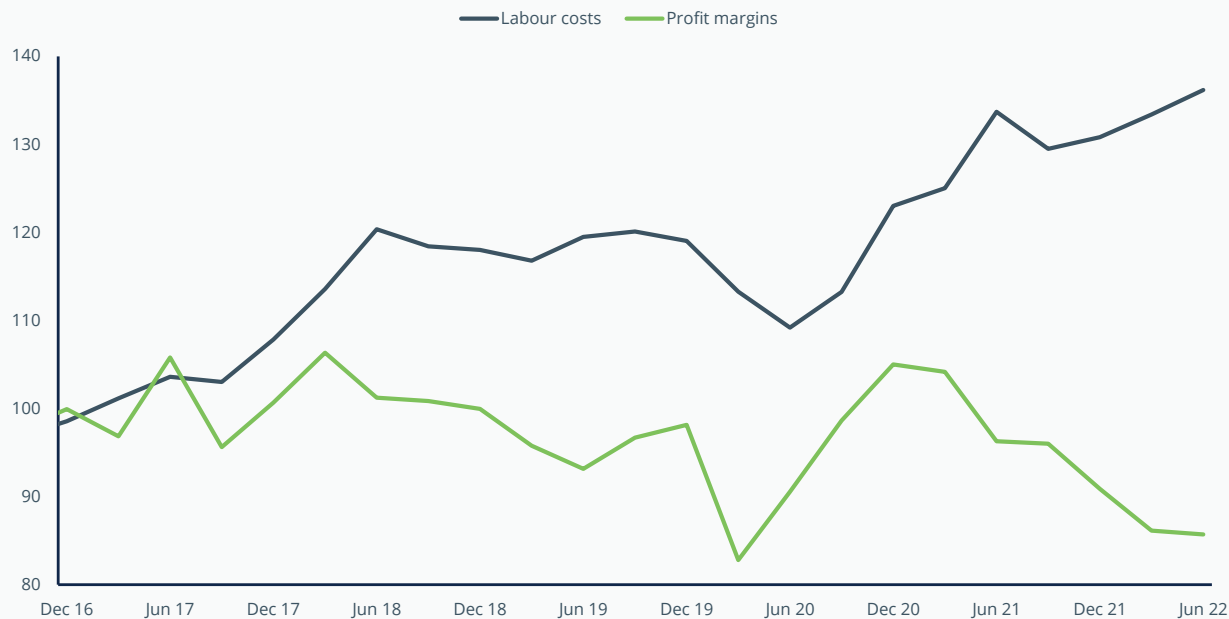
Global economic risks are largely out of our control, so to ensure WA's strong potential is fully realised, it is critical that government, industry and the broader community work together to capitalise on new and emerging opportunities.

To that end, CCIWA has developed a raft of reform proposals that, if adopted, would help to strengthen and diversify WA's economy over the longer term. They include:

- **Reform WA's payroll tax model to provide relief for small and medium sized businesses facing significant cost escalation.** WA businesses currently pay more payroll tax than those in any other State across a range of taxable wages.
- **Address weaknesses in the migration system to alleviate skilled labour shortages.** This includes streamlining the Federal migration system to make skilled migration channels more easily accessible.
- **Support WA businesses to mitigate and adapt to the risks associated with climate change and capitalise on growth opportunities.** There is immense opportunity for

WA businesses to be leaders in innovating to decarbonise, but there are barriers to investment that need to be addressed at both Federal and State levels of government.

Higher costs are eviscerating profits



Economic Outlook

Economic forecasts for Western Australia

Forecasts ^{1,2}	2020-21 Actual	2021-22 Forecast	2022-23 Forecast	2023-24 Forecast	2024-25 Forecast
Economic Activity					
Household Consumption	2.6%	5.0%	1.75%	2.0%	2.25%
Dwelling Investment	2.7%	5.0%	7.25%	-0.5%	0.75%
Business Investment	5.1%	1.75%	8.25%	3.0%	1.0%
State Final Demand	4.5%	4.5%	3.0%	2.0%	2.0%
Exports	-1.1%	-0.9%	2.0%	1.25%	0.5%
Imports	-8.2%	-1.75%	11.0%	6.0%	1.75%
Gross State Product	2.6%	2.75%	1.75%	1.0%	1.25%
Labour Market					
Unemployment	6.1%	3.7% ³	3.75%	4.0%	4.0%
Inflation	1.6%	6.0% ³	5.75%	3.25%	2.5%
Wages	1.5%	2.20%	3.0%	3.25%	3.5%

Notes:

¹ Actual outcomes are as reported in the 2020-21 State Accounts, updated with the latest State Final Demand and Balance of Payments data.

² Forecasts for economic activity are produced in terms of annual average growth, comparing four quarters of data to the previous four quarters of data.

³ Actual outcomes.

While risks to the overall outlook have intensified, WA's economy remains grounded on a solid foundation. Our strong economic and social resilience – reinforced throughout the COVID-19 pandemic – has positioned us well to traverse the next phase of economic, social and political uncertainty.



Economic Growth

Economic Activity		
Forecasts	State Final Demand	Gross State Product
2020-21 Actual	4.5%	2.6%
2021-22 Forecast	4.5%	2.75%
2022-23 Forecast	3.0%	1.75%
2023-24 Forecast	2.0%	1.0%
2024-25 Forecast	2.0%	1.25%

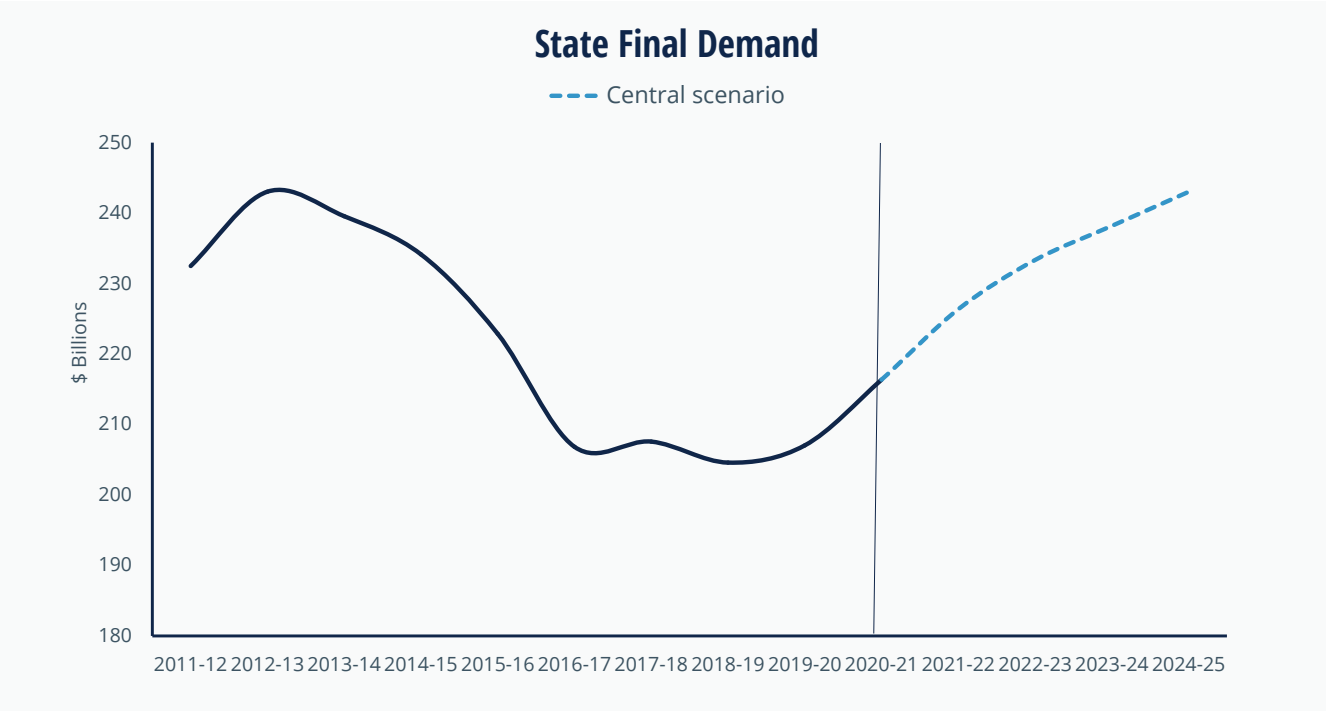
The Western Australian economy has emerged from COVID-19 the envy of the world. Robust household consumption, solid activity in the mining sector and a strong

jobs market have all fuelled strong economic momentum over the past 18 months.

Looking ahead, the outlook for WA's economy remains generally positive. We expect growth to be underpinned primarily by large-scale business investment, the State Government's Asset Investment program and a strong pipeline of residential construction.

While key headwinds have intensified over the past six months, an economic 'cliff' remains unlikely. We expect domestic economic growth to slow to 3.0 per cent this financial year as rising interest rates and inflationary pressures take the heat off consumer spending, and ongoing labour shortages and elevated input costs soften the outlook for non-mining investment.

Growth in the overall economy (Gross State Product) is expected to slow to 1.75 per cent this financial year, primarily due to a rebound in overseas travel and a recovery in goods imports.



Household Spending

Economic Activity	
Forecasts	Household Consumption
2020-21 Actual	2.6%
2021-22 Forecast	5.0%
2022-23 Forecast	1.75%
2023-24 Forecast	2.0%
2024-25 Forecast	2.25%

Western Australian household consumption has defied gravity throughout 2021-22. A cocktail of high savings rates, near-record low unemployment and strong income growth

unlocked a tidal wave of spending in our communities, and this momentum has shown little sign of slowing down.

Looking ahead, we expect consumption to ease as rising interest rates and inflationary pressures tighten household budgets. The reopening of international borders is also expected to weigh on domestic spending as Western Australians save for their first overseas holiday in over two years.

At the same time, high savings buffers, a tight labour market and a pick-up in wages growth will cushion the fall and help to maintain solid baseline consumption levels.

Key risks to this outlook include a more aggressive path for the RBA's cash rate, higher and more persistent inflationary pressures and softer net migration levels.



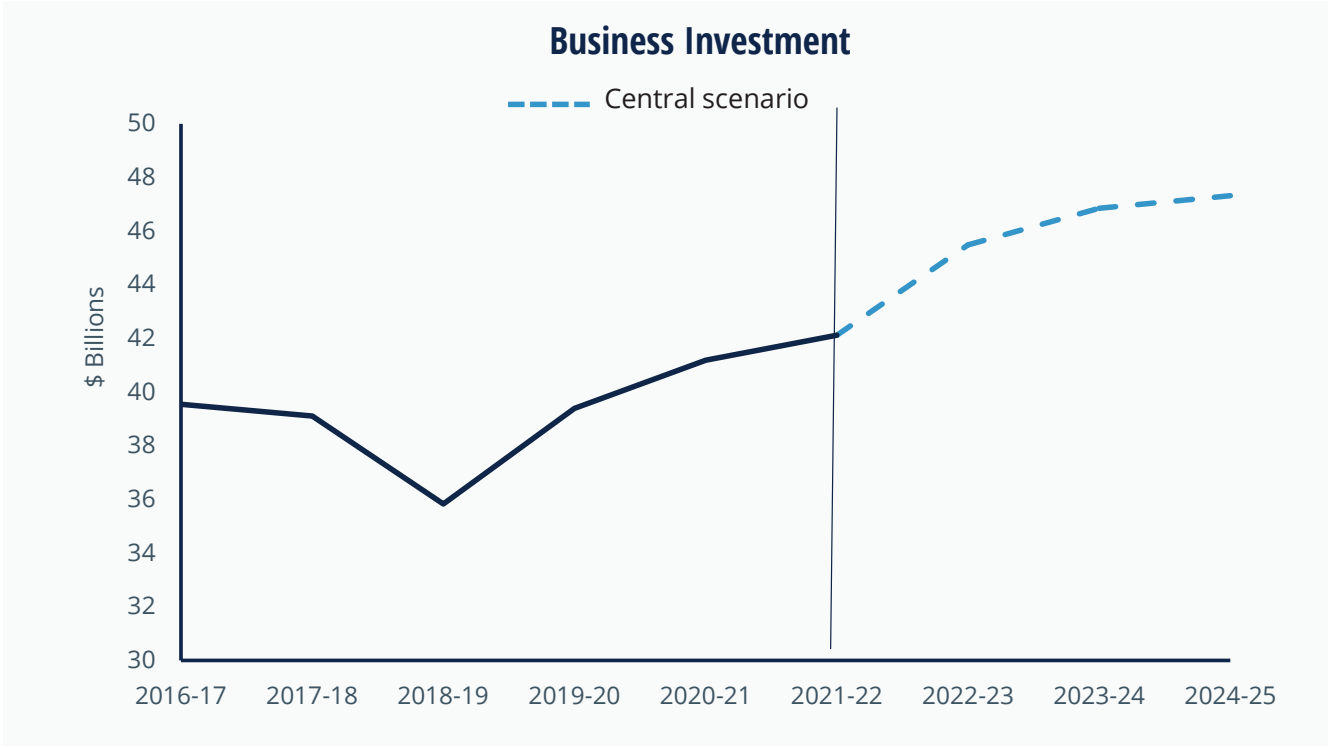
Business Investment

Economic Activity	
Forecasts	State Final Demand
2020-21 Actual	5.1%
2021-22 Forecast	1.75%
2022-23 Forecast	8.25%
2023-24 Forecast	3.0%
2024-25 Forecast	1.0%

Challenging operating conditions have weighed on WA's private investment pipeline over the past 12 months. Supply chain disruptions, rising operating costs and labour shortages have delayed investment spending and weighed on new project feasibility – particularly among smaller non-mining businesses.

While many of these factors are expected to persist throughout this financial year, headline business investment is set to accelerate as construction ramps up on major LNG projects – namely Woodside's Scarborough and Pluto 2 extension.

Additionally, WA's iron ore majors are expecting to sustain strong levels of production over the coming year, which will



support robust baseline levels of capital expenditure.

Over the longer-term, the global acceleration toward decarbonisation and associated uptake of electric vehicles is expected to support growth in WA's critical and battery minerals sectors.

As such, we expect business investment to grow 8.25 per cent this financial year, before moderating in 2023-24 and 2024-25.

Key risks to the outlook include escalating geopolitical tensions, worsening inflationary pressures and protracted labour shortages.



Dwelling Investment

Economic Activity

Forecasts	Dwelling Investment
2020-21 Actual	2.7%
2021-22 Forecast	5.0%
2022-23 Forecast	7.25%
2023-24 Forecast	-0.50%
2024-25 Forecast	0.75%

WA's construction sector has had a wild ride over the past 18 months. Record low interest rates and generous government support payments incentivised many Western

Australians to enter the property market throughout 2021 – triggering an explosion in WA's construction pipeline.

Conditions have since changed, with rapid cost escalation, supply delays and rising interest rates creating significant challenges for prospective homeowners to meet contractual obligations. As a result, we are now hearing reports of increased fall over rates and cancelled contracts.

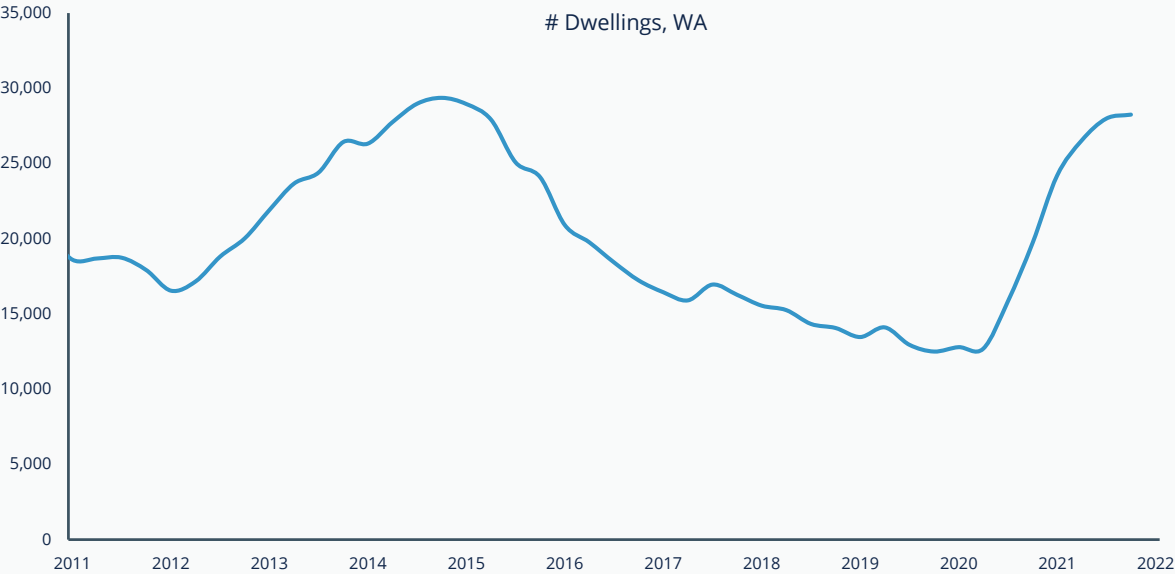
Construction businesses are bearing the brunt, with higher input costs and labour shortages crushing profit margins and stifling the ability for many businesses to bid for work.

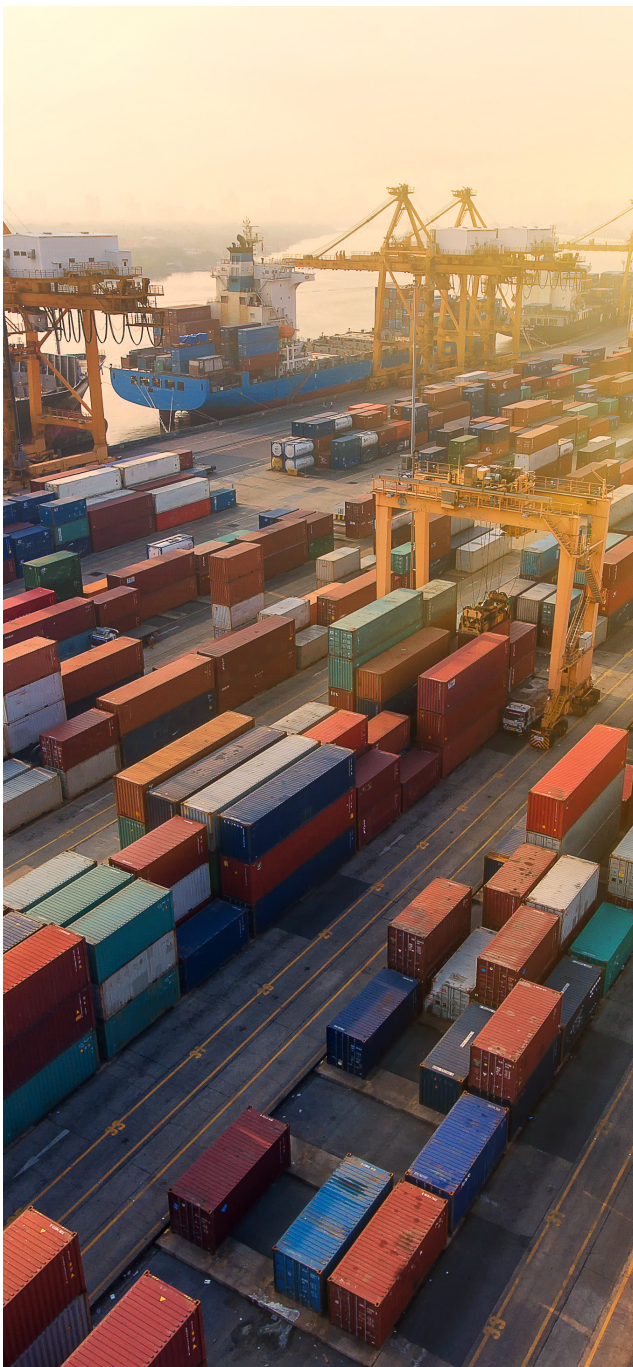
Reflecting this, the greenfield development pipeline remains particularly gloomy. Lack of certainty around the future cost outlook has blown out risk margins and significantly compromised the feasibility of new projects. As such, we expect few major residential developments to commence in the next 12-18 months.

Looking ahead, we expect dwelling investment to rise 7.25 per cent in 2022-23 as much of the existing construction pipeline is completed, before slowing markedly in 2023-24 and 2024-25.



Residential Construction in the Pipeline





International Trade

Economic Activity

Forecasts	Exports	Imports
2020-21 Actual	-1.1%	-8.2%
2021-22 Forecast	-0.9%	-1.75%
2022-23 Forecast	2.0%	11.00%
2023-24 Forecast	1.25%	6.00%
2024-25 Forecast	0.50%	1.75%

Strong global commodity prices and a bumper agricultural harvest underpinned a successful year for WA's exporters last financial year. While overall conditions remained accommodative, seasonal weather disruptions and scheduled maintenance activity dampened iron ore export volumes in Q1 2022, weighing on WA's annual production estimate. The lack of international travel also dragged on

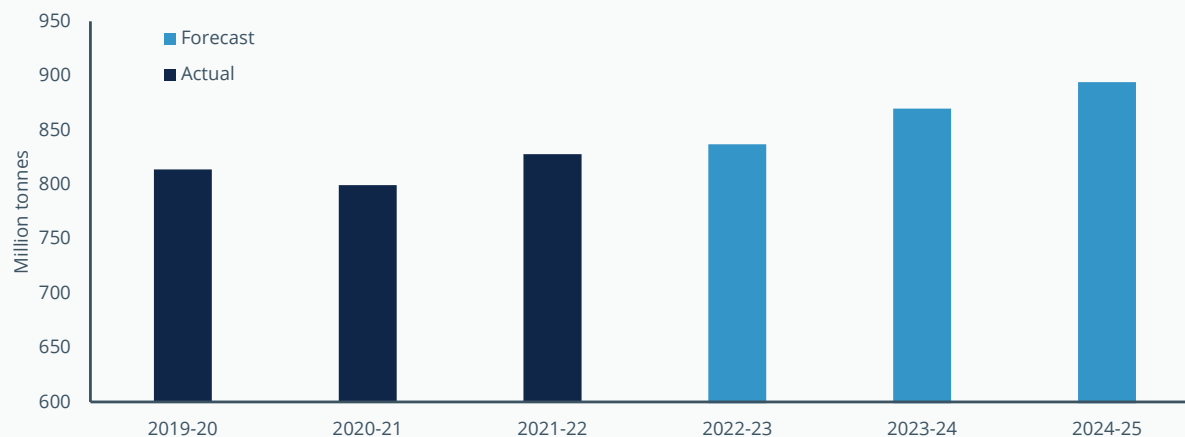
WA's exports last financial year.

Export volumes are expected to recover throughout the rest of this year and stabilise into 2022-23. While challenges in China's property sector and broader economy pose key risks to this outlook, leading indicators of steel consumption point toward ongoing demand for WA's seaborne iron ore over the coming year and Chinese policy support continues to remain accommodative. Balancing these risks, our central view is that China will remain a source of stability for WA's resources sector over the next 12 months.

All up, we expect exports to decline marginally (-0.9%) in 2021-22 before accelerating to 2.0 per cent in 2022-23 as international students and foreign tourists return to WA shores.

Imports of goods are expected to rise by 3.75 per cent this year, in line with the anticipated pick up in business investment and strong conditions in the agricultural sector. The return of international travel will boost imports of services as many Western Australians enjoy their first overseas holiday in over two years.

WA Iron Ore Production Outlook



Source: CCIWA, Macquarie Research

Unemployment

Economic Activity	
Forecasts	Unemployment
2020-21 Actual	6.1%
2021-22 Forecast	3.7%
2022-23 Forecast	3.75%
2023-24 Forecast	4.0%
2024-25 Forecast	4.0%

Western Australia's jobs market is red hot. Our unemployment rate dropped to 3.2 per cent in July – the

second lowest in the nation - and for the first time there are now more job vacancies than there are unemployed people.

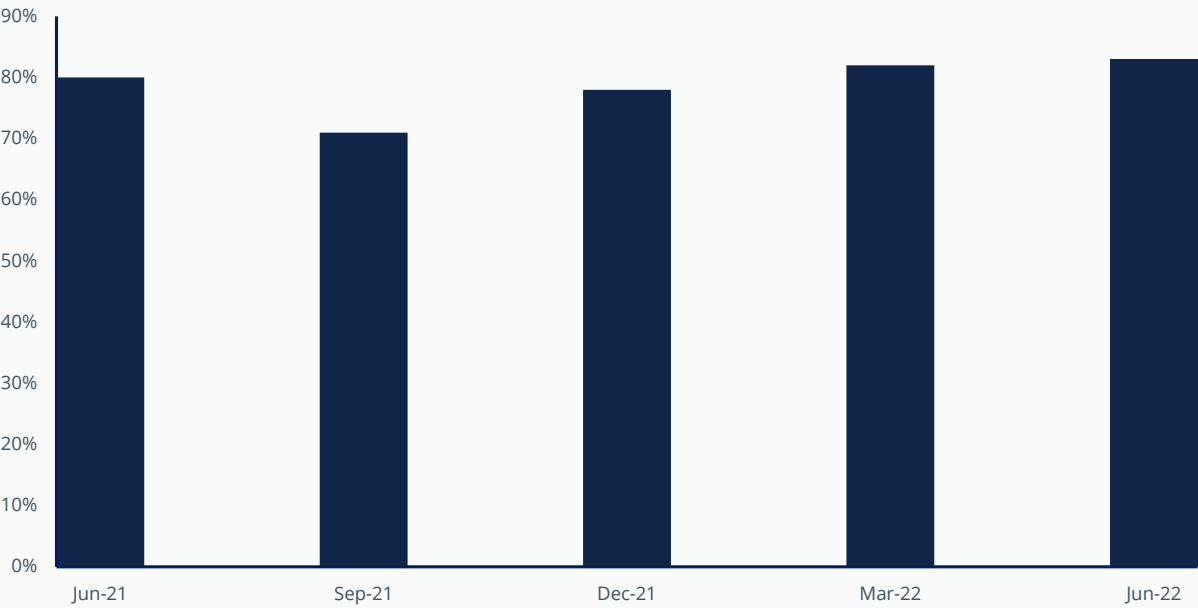
This is good news for job-hunters, but not so great for local businesses struggling to find staff. Our latest Business Confidence Survey revealed four in five WA businesses are struggling to fill a skilled occupation.

While the reopening of international borders will alleviate some of the pressure, significant visa processing delays and strong global competition for skilled workers are expected to weigh on WA's inbound migration pipeline.

These factors, combined with strong demand for WA-based workers, will sustain ongoing tightness in WA's jobs market. As such, we expect the unemployment rate to average 3.75 per cent this financial year, before rising to 4.0 per cent in 2023-24 and 2024-25.

Is your business struggling to hire for a particular skillset?

Proportion that responded 'yes'



Wages and Inflation

Economic Activity

Forecasts	Inflation	Wages
2020-21 Actual	1.6%	1.5%
2021-22 Forecast	6.0%*	2.2%
2022-23 Forecast	5.75%	3.0%
2023-24 Forecast	3.25%	3.25%
2024-25 Forecast	2.5%	3.5%

*Actual outcome

Inflation outlook

Inflation has quickly materialised as one of the most pressing challenges facing the world economy.

Global factors are primarily to blame for the recent bout of inflation. Strong global demand for goods throughout the pandemic triggered acute supply bottlenecks, and the invasion of Ukraine sent the prices of key energy and agricultural benchmarks skyrocketing. Nations directly exposed to the Russian energy market have been acutely affected, with UK CPI recently hitting a 40 year high.

Western Australia has not been immune to these global factors. Local steel prices increased 35 per cent over the year to June and cost of living pressures have intensified.

We expect broader inflationary pressures to persist throughout the rest of 2022, driven primarily by elevated food, fuel and rental prices. The State Government's \$400 electricity subsidy will take some of the heat off household budgets over the coming months.

Looking beyond, we expect inflationary pressures to gradually ease throughout 2023 as key global factors start to unwind – softening pressures on domestic and international supply chains.

As such, we expect headline Perth CPI to hit 5.75 per cent this financial year in annual average terms, before slowing to 3.25 per cent in 2023-24.

Wage outlook

Skilled labour shortages have applied sharp upward pressure to labour costs right across the WA economy.

Initially, WA businesses relied on short-term financial incentives to attract and retain staff. That game plan has since changed, with our June quarter Business Confidence Survey revealing two thirds (67%) of WA businesses are now lifting base wages to combat the skills crisis.

With sustained tightness in WA's labour market expected, we anticipate base wage pressures to continue building over the forecast horizon. Recent minimum and award wage decisions will also add to growth.

As such, we expect the headline Wage Price Index to hit 3.0 per cent this financial year in annual average terms, before rising to 3.25 per cent in 2023-24.

With sustained tightness in WA's labour market expected, we anticipate base wage pressures to continue building over the forecast horizon. Recent minimum and award wage decisions will also add to growth.





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