

Global downturn causes downgrade to our state and territory growth forecasts

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## No escape

In the wake of recent global events, we have substantially downgraded our forecasts for economic activity and employment growth for Australia's state and territory economies.

All state and territory economies will be impacted by the negative impacts of the global financial crisis and the associated slowing in global growth.

The mining heavy states of **Western Australia, Queensland and the Northern Territory** will be most directly affected by recent heavy falls in commodity prices and some easing in growth of demand from key customers. This will impact business investment through the deferral and cancellation of some expansion and infrastructure projects. But with long pipelines of engineering construction work still outstanding (at least in WA and Qld), this is likely to see investment merely cool to more sustainable levels from the frantic pace of recent years, rather than to stop completely. Business profitability will also fall, although the sharply lower A\$ is expected to offset much of the fall in global commodity prices (mainly priced in US\$), helping to maintain A\$ income flows. Tourism, of particular importance to Queensland, will continue to face strong headwinds, as it has for some years. Although the lower A\$ has made Australia more cost competitive for international visitors, and lower fuel prices have reduced local driving costs, both international and domestic desire to travel is expected to be muted by the tougher economic times. Overall however, growth in these states' economies is expected to remain buoyant relative to the states and territories of the south eastern seaboard.

We remain concerned about **New South Wales**. In our last full quarterly review of the States (released in Sept 2008), we reported that NSW was on the brink of recession, with falling household consumption, very weak residential construction, soft business investment and falling employment. The potential saviour at the time of this year's state budget was a planned substantial boost to infrastructure spending, but that option fell by the wayside with the subsequent failure of the government's pitch to privatise the state's substantial electricity assets. That failure, coupled with a severe deterioration in the state's fiscal position in the first two months of 2008-09 (a deficit of \$163 million in July and August), suggests the state mini-budget scheduled for early November will be very tight, with slashed spending and perhaps increased taxes. This will only exacerbate the downward economic spiral. While we appreciate the government's desire to retain its AAA rating and to get its finances in order, we would argue that now is not the time for contractionary state fiscal policy, but rather for some old fashioned pump priming. Perhaps the Federal Government will ride to the rescue through the forthcoming infrastructure program, but the details of that are yet to be announced, and there are many other competing claims from around the nation. The one sector of the NSW economy that should be capable of delivering an impetus to growth is housing construction. The state is suffering the most acute shortage of housing of any of the states and territories, and dwelling construction approvals are at their weakest since the early 1980s. With mortgage interest rates now falling, we would normally expect a rapid and sizeable lift in home building. This may be delayed however, by a flat outlook for prices, high developer taxes and charges, and fragile household and investor confidence.

In **Victoria** the manufacturing sector is experiencing heavy weather. The motor vehicle industry is on shaky ground again, with domestic demand for large passenger vehicles continuing to fall in response to relatively high fuel prices, changing consumer tastes, and more recently, low consumer confidence. Job losses at automotive manufacturers and component suppliers are continuing. For other manufacturers, the lower A\$ will make exports more competitive, but that is of little relief when demand in international markets is also declining. Victoria's northern rural regions will also continue to struggle, as the endless dry rolls on. Nevertheless, Victoria is expected to continue to grow more quickly than New South Wales, supported by a diverse economy, stronger population growth, higher dwelling construction, and more buoyant government spending.

**South Australia** had been performing strongly this year, relative to the other south eastern seaboard states, with economic activity boosted by increased investment and development activity associated with the substantial mineral deposits in the north of the state. This has led to high wages growth, strong household consumption and a buoyant housing market. Continued strong infrastructure spending will help to underpin economic activity, even as some chilling in confidence and a desire to rebuild household balance sheets leads to a cooling in household spending. Water availability will remain a critical issue, particularly for irrigators along the Murray, but this is not expected to further suppress rural output, since irrigation allocations are already at their minimum.

**Tasmania** has entered this downturn in a stronger position than the other non-mining states, with buoyant (relative to Tasmanian history) population growth, solid dwelling and business investment and an unemployment rate lower than the national average. Household consumption will be softer over the next two years, in line with the rest of Australia. Another dry Tasmanian summer will depress rural producers and may also affect electricity generation costs and 'export' potential to the mainland from the state's mainly hydro-electric system.

The **Australian Capital Territory** will be less impacted than most by the global uncertainty. The primary influence will be decisions on the required number of public servants, with the need for efficiency dividends already leading to slowing employment growth.

**Figure 1: State economic and employment growth will slow**

	% change p.a.	2007-08	2008-09	2009-10
NSW	GSP	2.50	0.50	1.25
	Emp	2.37	0.50	-0.35
VIC	GSP	3.25	1.25	2.00
	Emp	2.66	1.00	0.25
QLD	GSP	4.25	3.00	3.00
	Emp	2.78	2.00	0.50
WA	GSP	6.25	3.00	3.00
	Emp	3.55	2.25	0.50
SA	GSP	4.00	1.75	2.00
	Emp	2.13	1.25	0.25
TAS	GSP	4.00	0.75	1.75
	Emp	2.73	1.25	0.25
ACT	GSP	2.25	0.50	1.50
	Emp	0.86	0.25	0.00
NT	GSP	3.75	2.50	3.00
	Emp	5.65	2.25	0.40
AUST	GDP	3.66	1.47	2.06
	Emp	2.64	1.20	0.11

Source: ANZ Economics and Markets Research

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