Economics@ANZ

States and Territories Economic Update

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Inside:

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Overview

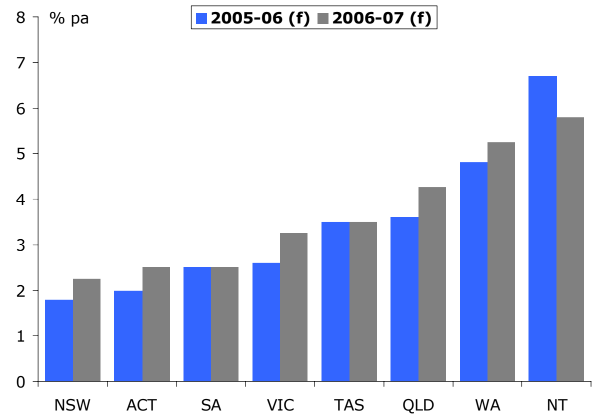
Australian Outlook

Economic conditions continue to vary markedly between the states and territories. Those regions which have a high exposure to the mining boom are enjoying generally favourable conditions, with strong economic activity, strong jobs growth, high population growth, relatively buoyant housing markets, and solid government revenues. In contrast, those regions with relatively small mining sectors (with the notable exception of Tasmania) are being largely bypassed by the boom. They are experiencing more subdued economic activity, softer housing markets, and lower employment and population growth. Budgets in these states are also under pressure, with revenues negatively impacted by lower turnover in the market for dwellings and with no offset from increased mining revenues.

This disparity in economic performance is unlikely to be substantively altered in 2006-07. The Reserve Bank of Australia will seek to cap Australian economic growth at no more than potential - around 3% to 3.25% - for the next three years in order to prevent inflation and inflationary expectations rising from a point where they are already at the top of their comfort zone. A range of data — March quarter GDP, retail sales, labour market — suggest economic activity was already at potential in early 2006. This suggests the RBA will need to tighten monetary policy again, to a slightly restrictive stance, to keep a lid on economic growth. We believe the RBA will lift the cash rate by another 25bp to 6.00% this year, possibly as early as August.

This capping of national growth will leave little room for an acceleration in the economies of the more slowly growing southeastern states and territories unless there is a commensurate slowing in the growth of the rapidly growing mining states. Activity levels in the mining states are unlikely to substantively slow. Although the construction phase of some mining and related infrastructure projects will come to a close, there remains a large backlog of construction work yet to be done, and this should be complemented by increased volumes of exports coming on stream. This suggests the significant growth differential between the mining "haves" and "have nots" will continue for the next year or two.

Relative growth of Gross State Product will not change much in 2006-07



Sources: Australian Bureau of Statistics, Economics @ ANZ

Sharing the fruits of the commodity boom

The Australian Government has initiated small steps to distribute the benefits of the commodity price boom more evenly. In the May 2006 budget it distributed the windfall gains from higher company taxes to households in all states and territories through a mixture of tax cuts and increased family payments, worth $40bn over 4 years.

Of greater long-term significance, the Commonwealth Grants Commission has flagged a redistribution of GST funding away from the revenue rich states towards those states which are under greater revenue pressure. Interestingly, this involves a distribution away from those states and territories which traditionally have been subsidized – WA, NT, Queensland – towards those which have traditionally subsidized the rest of Australia (NSW and Victoria).

Having said that, the redistribution for next year is minor and doesn't alter the basic status quo. (And please, we do not want any correspondence on the fairness or otherwise of the GST distribution!)

Source of change in the redistribution of GST Pool Revenue between 2005-06 and 2006-07

	1	2	3	4
	$mn	$mn	$mn	$mn
NSW	848.1	-44.1	72.7	876.7
Vic	647.4	-7.4	221.4	861.4
Qld	590.0	69.6	-174.1	485.5
WA	293.2	20.0	-89.3	224.5
SA	260.3	-27.5	-55.4	177.4
Tas	107.1	-11.1	-4.0	91.9
ACT	53.1	-4.2	1.9	50.8
NT	126.2	4.1	26.8	157.2

1. Changes arising from an increase in the size of the pool.
2. Changes arising from changes in population.
3. Changes arising from adjusted relativities.
4. Total changes to GST share.
Source: Commonwealth Grants Commission

In 2006-07 NSW will receive an additional $72.7mn as a result of rejigging the GST distribution formula, while Victoria will receive an additional $221.4mn. Queensland, WA and SA will be the biggest "losers" under the redistribution, contributing respectively an additional $174.1mn, $89.3mn and $55.4mn. These changes mainly reflect changes in the revenue raising capacities of the states and territories, in particular softer residential property markets in NSW and Victoria, and the strength of the mining industry in WA, NT and Queensland.

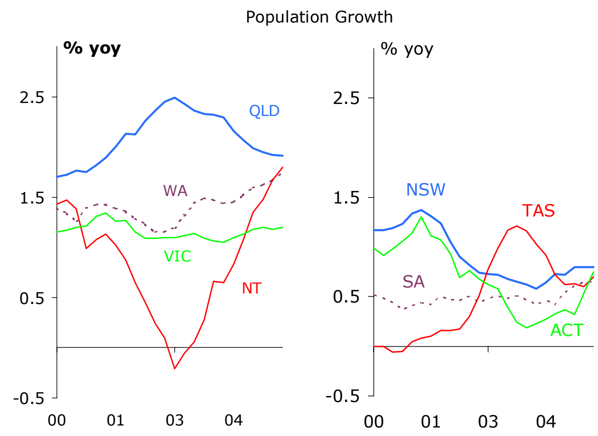
Despite these changes, in 2006-07 NSW will remain the state which provides the greatest subsidy to other states and territories. The NT will remain the most heavily subsidized region.

The GST revenues are key sources of funding for the states. In 2004-05, the GST pool provided $43bn, 42% of state budget revenue, varying from 37% for NSW to 75% for the NT.

Population

Demographic drivers will continue to be important determinants of the relative economic performance of the states and territories. Population growth is converging at around 1.7% to 1.8% p.a. in WA, NT and Queensland, not coincidentally the three regions with the relatively highest exposure to mining. This is a rate of population growth well above the rest of Australia, and will continue to boost demand for housing, as well as to underpin domestic demand in those states and territories.

Population growth is highest in mining oriented states and territories



Source: Australian Bureau of Statistics

Budgets

A defining feature of the 2006-07 state and territory budgets is a loosening in fiscal stringency, with reduced general government operating surpluses in three states (Victoria, Queensland, and WA), and a move from surplus to deficit in two states (NSW and Tasmania). Only the two territories have projected slightly tighter fiscal policy in 2006-07, with the NT moving from a small deficit to a small surplus, and the ACT aiming for a reduced deficit (SA will not deliver its 2006-07 Budget until mid to late September). All states bar one will record a deterioration in general government net debt, with increased net debt in NSW, Victoria, and NT, and with a reduction in net assets in Queensland and WA. Tasmania stands alone in projecting an increase in net financial assets in 2006-07.

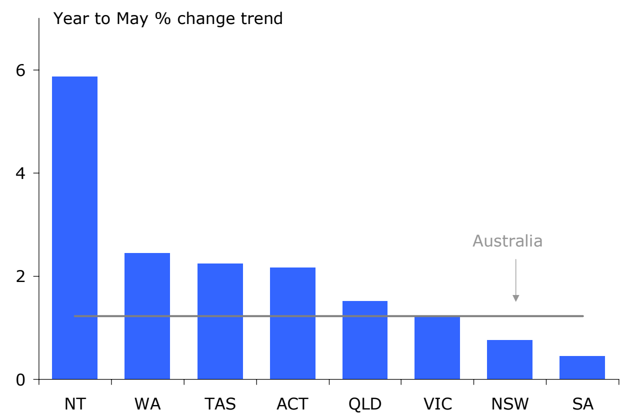
New South Wales

NSW remains Australia's largest state economy, with gross state product contributing one third of the Australia total. NSW had the weakest growth in gross state product of any state and territory in the second half of 2005. Growth in state final demand decelerated steadily in trend terms over the past 5 quarters, and in the March quarter increased by just 0.3%. The weakness lies in private gross fixed capital formation, which was negative in the past two quarters, with the pace of decline deteriorating rather than improving. This is solely the product of the very weak residential housing sector; private business investment remains robust.

On the residential sector, Sydney property prices continue to fall, declining by a further 1.2% in the March quarter, taking the cumulative decline since the end of 2003 to nearly 10%. Dwelling construction activity continues to wane, with trend local council approvals to build new dwellings in May at just over half the peak of late 2002, and now at the lowest level since monthly records began in mid 1984.

The soft economic performance is reflected in the labour market. Trend data show that employment growth over the year to May was the second weakest of the states behind only SA, with the unemployment rate of 5.3% being above the Australia average of 5%.

Big differences in employment growth

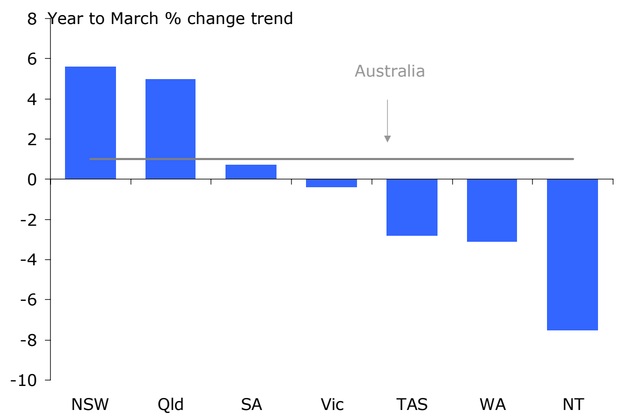


Source: Australian Bureau of Statistics

On a more positive note, one point that is generally not appreciated is that, despite all the talk of the high-growth export states, NSW is the second largest exporter of goods, behind only WA, but ahead of Queensland and well ahead of the NT. The "problem" for NSW is that its economy is still the largest, so that its net contribution from exports is not as marked, and also that the composition of NSW exports is more diverse and less focused on mining. Having said that, the NSW export sector is strong, with goods exports growing by more than any other state and territory over the year to the March quarter (although WA and Queensland exports were negatively impacted by cyclones in the March quarter 2006).

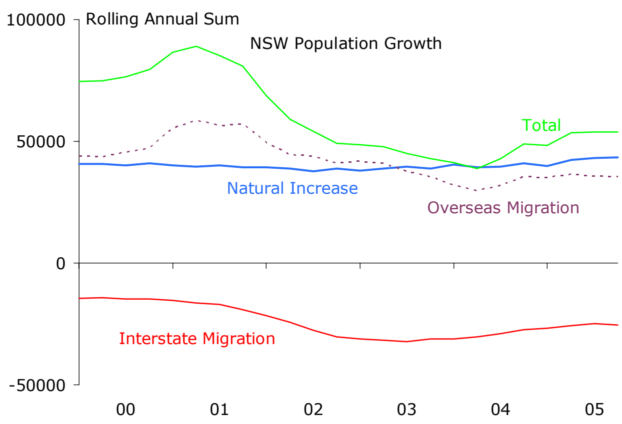
Another area where there is some good news is population growth. The annual rate of population growth reached its nadir at 0.6% in June 2004, but has since accelerated slightly to 0.8%. This was due to a small reduction in interstate emigration – slightly fewer New South Welshmen and women are seeking greener pastures in other states, although the net exodus remains heavy – coupled with a slight increase in international immigration, probably a result of the lift in overall immigration numbers for Australia.

NSW leads growth in goods export volumes



Source: Australian Bureau of Statistics

Sources of NSW population growth



Source: Australian Bureau of Statistics

The 2006-07 NSW Budget projects an increase in gross state product of 1.75% in 2005-06, lifting to 2.5% in 2006-07. This is predicated on dwelling investment bottoming out, steady growth in private consumption and improved net exports. Business investment growth is expected to slow, but business investment will remain at historical highs both in level and as a share of gross state product (GSP).

The Budget qualifies these projections by noting that further increases in interest rates could compromise growth. We expect there will be another 25bp interest rate increase this year, further delaying the recovery of the NSW dwelling sector, and the economy more generally. Nevertheless, there should be sufficient momentum from stronger exports and a slight lift in household spending arising from the July 1 tax cuts to boost growth to around 2.25% in 2006-07.

NSW Budget

The NSW Budgetary position will weaken in 2006-07. NSW is the only state to project an operating deficit in 2006-07, with a forecast figure of $696mn. This is a substantial turnaround from the estimate at the time of the 2005-06 budget of a surplus of $481mn, and the mid-year review estimate of a deficit of $533mn. The further increase in the deficit is not so much a function of the business cycle, but rather mainly reflects reductions in taxes totaling $481mn from measures announced in 2005-06 and in the 2006-07 Budget. These include the winding back of poker machine taxes and the abolition of property vendor exit duty. Where the business cycle does show through is in reduced stamp duty from the continuing downturn in the residential property market. On the expenses side there are additional payments associated with 5,000 public sector redundancies and minor spending increases in various portfolios.

The Budget projects a return to an operating surplus of $378mn in 2007-08, underpinned in part by a recovery in the residential property market. As noted above, another RBA interest rate increase is likely to delay that recovery. The return to surplus also requires a sharp deceleration in the growth of expenses, from 5.7% in 2006-07 to just 1.9% in 2007-08.

The Government also plans to ramp up infrastructure spending by 22.8% to $9.9bn in 2006-07. To support this it will engage in new borrowings of $5.4bn.

The budgetary pressure in NSW in 2006-07 will be relieved only slightly be the redistribution of GST funding. But to put that into perspective, the GST system has not been the cause of the deterioration in the NSW budgetary position in 2006-07, nor has it been a factor in the deterioration in the relative economic performance of NSW over the 2000s.

NSW retains its AAA rating.

Victoria

Victoria is the second largest state economy, with output about 30% lower than NSW. Victoria's growth had been holding up well through 2004-05, but economic activity has progressively decelerated through 2005-06 as private investment has waned. Trend growth in state final demand in the March quarter was just 0.4%, only marginally ahead of NSW.

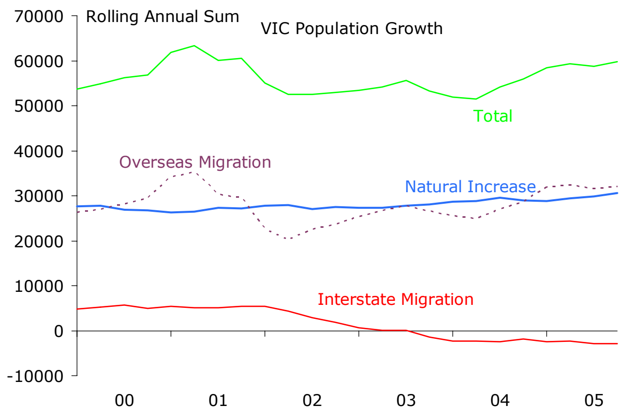
Victoria has a large export sector – goods exports rank fourth behind WA, NSW and Queensland. However, its composition is different in that it has virtually no mining exports and a much heavier emphasis on manufactured goods. As such, it is not benefiting from the current strong global demand for heavy commodities. It could even be argued that the relatively high level of the Australian dollar – in large part reflecting high commodity prices – is inhibiting the Victorian export sector.

Victoria continues to enjoy higher population growth than all but the three "high growth" states; its population growth of 1.2%pa is roughly double that of SA, Tasmania and the ACT, and about two thirds greater than NSW. However, this is an issue that needs to be watched, because interstate emigration has turned negative. This might be part of the wider Australian trend to move to the high jobs growth regions of WA and NT. Employment growth has slowed to 1¼% trend over the year to May, but remains well above that of NSW. The unemployment rate of 5.2% is the lowest (just) of the "low growth" states and territories (excluding the ACT) although that might be because job seekers are moving elsewhere.

House price growth in Melbourne remains subdued, but at least prices are not falling. Prices of established houses increased by 0.8% in the March quarter and by 3.8% over the year. Dwelling construction approvals had been falling for about 3½ years, and by early 2006 were running 30% lower than the mid 2002 peak. More recently they have shown signs of lifting, although this has all been in multi unit dwellings.

The 2006-07 Budget projects gross state product accelerating from 2.5% to 3.25% on the back of a pick up in consumer spending and some recovery in exports. This seems about right to us, and would see Victoria continue to perform well for a "non-mining" state.

Sources of Vic population growth



Source: Australian Bureau of Statistics

Victorian Budget

Victoria continues to enjoy a sound fiscal position. The operating surplus in 2006-07 is projected at $317mn, 29.5% lower than in 2005-06. This change reflects a 4.5% rise in expenses against a 4% increase in income – this is not unexpected given that it is a pre election budget. Operating surpluses are projected to remain fairly steady, at above $300mn over the next three years. Within this framework, there will be some trimming of business taxes including land tax, progressive reductions in payroll tax from 5.25% to 5% over 3 years, and cuts to workcover premiums. Other pro-business measures include additional spending to continue to attract events to Victoria, and a plan to reduce red tape by 25% over the next five years.

There is also $4.9bn in capital works in 2006-07, which should help to expand the state's productive capacity. This will involve some additional borrowing. General government net debt is projected to increase from $2bn at June 2006 to $7.1bn at June 2010. These are low debt levels – the June 2010 projection is equivalent to only 2.5% of GSP.

Victoria retains its AAA rating.

Queensland

Queensland ranks as the third largest state economy. It continues to record a strong economic performance. In the March quarter, state final demand increased in trend terms by 1.9%, the second strongest pace behind WA. All components of demand remained solid – private consumption, private investment and government spending. Queensland also has a strong export sector, with the volume of exports ranking third behind WA and NSW.

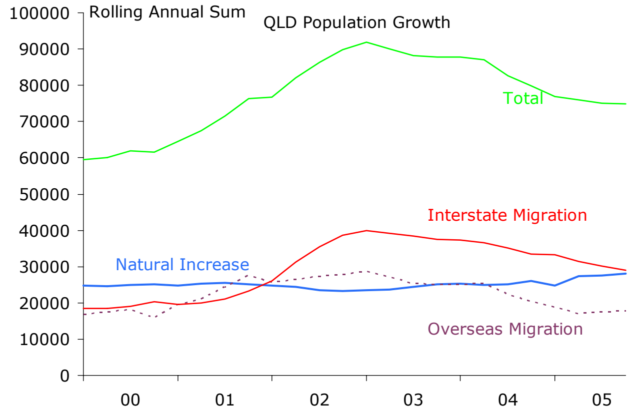
This robust economic performance has not impacted on the labour market to the extent that might have been expected. Trend employment growth over the year to May was 1.5%, in the middle of the pack. The unemployment rate of 4.9% is about on par with the national average.

Brisbane house price growth remains subdued, with existing house prices increasing by only 2.8% over the year to March, well down from the increase of 38.8% over the year to December 2003. Housing construction has weakened over the past 2½ years, with dwelling construction approvals down about 20% from the late 2003 peak.

Population growth remains the strongest of all the states, although there has been some deceleration over the past two years, and WA and NT have nearly caught up. Both interstate and overseas migration have cooled a touch.

In 2006-07 growth in gross state product is projected to lift from 3.5% to 4.25%. This will reflect steady consumption, waning dwelling and business investment, offset by stronger public spending and a smaller detraction from growth from the external sector as exports begin to increase.

Sources of Queensland population growth



Source: Australian Bureau of Statistics

Queensland Budget

Queensland's budget position was strong in 2005-06, but is projected to deteriorate in 2006-07. The estimated surplus for 2005-06 is a huge $2.8bn, well above the $718mn surplus projected at the time of the October mini-budget, and continuing the massive surpluses of the two previous years. The strong revenue flows are supported by mining royalties ($1.5bn in 2006-07), continued property stamp duties (supported by what is still the highest population growth in the country) and higher investment returns from Queensland Investment Corporation. The surplus is projected to narrow substantially to $245mn in 2006-07, with even smaller surpluses in the out years, although those projections are based on what seem to be conservative estimates of revenue growth. Revenue is projected to *fall* by 1.74% in 2006-07 after *increasing* by 7.2% in 2005-06. This projected narrowing of the surplus is after a winding back of growth in expenses from 12.9% in 2005-06 to 7.8% in 2006-07.

The 2006-07 Budget includes minor reductions in taxes, with cuts to some stamp duties, lifting of thresholds for payroll tax and for land taxes, and a new first home owner transfer duty concession for the purchase of vacant land.

For the first time in five years the Government will borrow to fund its infrastructure program. Capital investment is budgeted to rise by 23% to $10.1bn in 2006-07. To fund this the Government will borrow $4.6bn in 2006-07, including $1.8bn in the general government sector and $2.8bn for government-owned corporations. The Government proposes to borrow $17bn over four years to support $34bn of direct capital works.

Queensland retains its AAA rating.

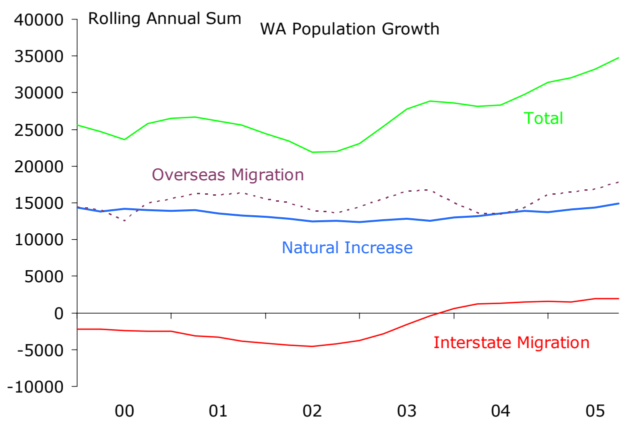
Western Australia

It might only be the fourth biggest economy in the nation, but if you want to experience a boom state, go to WA. State final demand rose by 2.7% in trend terms in the March quarter, the strongest result of all the states and territories. This was the fourth consecutive quarter of growth above 2%. The surge in economic activity is being driven by private sector investment, which increased by 32% over the year to March. Private household consumption is not booming, oddly enough, although it still rose by a solid 4% over the year to March.

The economic story is even stronger if trade flows are taken into account, with WA having the highest volume of exports of any state, contributing 31% of total Australian exports of goods in the March quarter. Of interest, trend data show the volume of WA exports peaked in June quarter 2005 and has subsequently declined. That story may have been impacted by disruptions to export shipments in the March quarter due to cyclone activity; we would expect trend growth to resume as backlogs are cleared and as new capacity comes on stream.

Population growth has accelerated over the past two years, and is now only slightly below that of Queensland. This has been mainly due to a lift in interstate migration as buoyant demand for labour and solid wages growth have attracted workers from other states.

Sources of WA population growth



Source: Australian Bureau of Statistics

Employment increased by 2.5% over the year to May, second in growth only to the NT. This led to the lowest unemployment rate of all the states of 3.7% (and just slightly above the ACT).

The strong economy and high rate of population growth has supported a booming housing sector. Established house prices in Perth rose by 28.8% over the year to March, the strongest housing market in the nation. And this has been matched by buoyant housing construction, with building approvals rising strongly from early 2001.

The Government projects growth in 2006-07 to accelerate from 4.75% to 5.25% on the back of a 10% lift in export volumes as additional capacity begins to generate increased production. The rate of growth of household consumption, dwelling investment and business investment will cool, not because of any inherent weakness, but simply because the current torrid pace cannot continue indefinitely. This growth path seems achievable.

Western Australian Budget

The WA Government is facing the same fortuitous circumstances as the Australian Government, in that the commodity boom is leading to a big boost to revenues.

Revenue rose by a huge 13.4% in 2005-06, but growth will taper sharply in 2006-07 and through the outyears. This will partly reflect a topping out of the commodity price boom, but will also flow from a reduction in WA's share of the GST pool due to its improved circumstances. (Note that royalties will total $42.27bn or 14% of state revenue next year).

Recurrent expenses rose by less than revenue in 2005-06 - although still by a very healthy 8.5% - but, less pleasing, they are projected to increase faster than revenue in 2006-07 and the out years. There is only a minor increase in capital works of $100mn proposed for 2006-07.

The operating surplus in 2005-06 will be a record $1.981bn, up $680mn on the mid-year review and $789mn better than in 2004-05. Surpluses are then projected to deteriorate (as expenses increase faster than revenue), with the 2006-07 surplus $706mn lower, at $1275mn.

Despite the fortuitous revenue flows, net debt levels are projected to rise, with the net debt to revenue ratio projected to increase from 25% in 2004-05 to 40% in 2009-10. Having said that, the general government sector is net debt free - all the net debt is in public corporations (water and electricity utilities). Nevertheless, at a time of record revenue growth, it could be argued that the Government should be putting more aside for a rainy day and repaying debt. WA public sector net debt levels as a proportion of GSP are already high relative to other states. In the short term this won't threaten WA's AAA status.

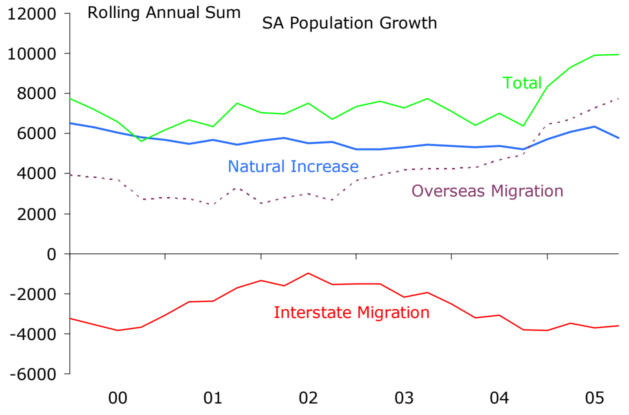
South Australia

South Australia has lost economic momentum over the past year, with trend quarterly growth in final demand slowing to 0.4% in the March quarter. This puts it among the pack of the slower growth south eastern states, on par with Victoria and slightly ahead of NSW. This reflects slower growth in private investment, and a fall in public sector investment. Private household spending has held up reasonably well at a moderate pace, while public sector spending has slowed. The volume of exports has fallen over the past two quarters in trend terms, although this has been broadly matched by a decline in imports.

Population growth has accelerated over the past year in response to increased international immigration as employers (including the Government) have sought to fill skilled vacancies. Intrastate emigration looks to have stabilised, although there are still significant numbers of people leaving the state.

Adelaide house price growth has slowed from the 2003 highs, but is still positive, with existing house prices increasing by 5.3% over the year to March. The dwelling construction industry is healthy, with dwelling construction approvals rising gently from early 2005.

Sources of SA population growth



Source: Australian Bureau of Statistics

The South Australian economy is facing challenges on several fronts. The automotive sector, the mainstay of the manufacturing industry, is suffering weak sales as consumers shun vehicles perceived to have high fuel usage (which unfortunately encompasses most vehicles manufactured in Australia). This is having flow on effects to component suppliers. The fishing industry is under pressure as the state and federal governments reduce allowable catches. The wine industry is suffering an over-supply of grapes and weak prices. The big potential saviour is an expansion of uranium mining. This may entail increased production from the Olympic Dam mine – the world's largest proven uranium deposit – or the opening of new mines should South Australian and Australian Government policy so permit.

South Australian Budget

The State budget for 2006-07 was delayed due to the state election in March 2006 and is now expected to be delivered in mid to late September.

Tasmania

Tasmania continues to punch well above its weight in the economic performance stakes. Trend growth in state domestic demand in the March quarter was the third strongest, behind only WA and Queensland. Over the past year household consumption slowed, although it remains robust, and private investment eased, although this tends to be volatile. Government spending has continued to grow at a solid pace.

Part of Tasmania's resurgence reflects stronger population growth, with positive inflows from other states through 2002 and 2003. That in turn lifted demand for housing, house prices, and construction activity. House prices in Hobart rose by 10% over the year to March. Dwelling construction approvals eased through 2005 after rising strongly over the previous four years, but have strengthened again in 2006. Investment has been boosted by a series of major infrastructure projects, including the Tasmanian Natural Gas Project, Basslink, and windfarms. The proposed new Gunns pulp mill at Longreach is expected to provide further impetus from 2007-08, with Budget Papers suggesting an investment value of $1.4bn and the creation of thousands of direct and indirect jobs. Increased tourism resulting from the expansion of discount air carriers and additional ferry services has also been an important driver; the recent cessation of the Sydney to Devonport ferry service is not expected to substantively compromise growth in this market.

Tasmania has also reaped the benefits of high quality economic management. Tasmania has paid off what was 10 years ago the highest net debt of any state. Over the past decade the Government has also been enthusiastic in its implementation of national competition reforms.

Increased business activity has boosted employment, which increased by 2¼% over the year to May, the third strongest of the states. Nevertheless, the unemployment rate remains the highest of all the states and territories because stronger employment opportunities have led to a rise in the participation rate.

Over the past four months trend employment growth has turned negative. Population growth is now also waning as the interstate inflows have dried up. This in part reflects the end of the residential property price boom in Melbourne and especially Sydney, and continued house price growth in Tasmania, reducing the relative cost attractiveness of Tasmania. It may be that the demographic drivers of growth are now ebbing.

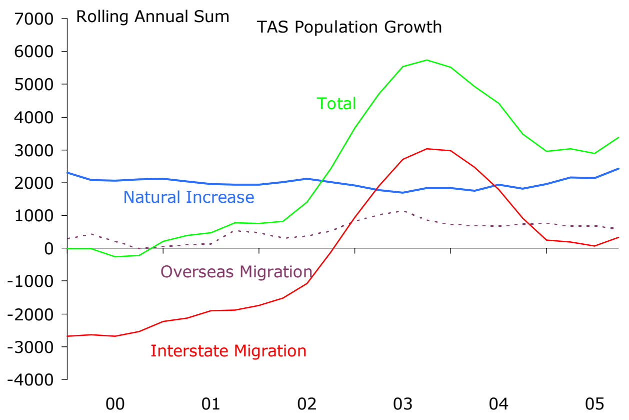
Budget papers project growth in 2006-07 to remain at around the current pace. This may be a little optimistic given the recent cooling in key drivers.

Tasmanian Budget

The new fiscal strategy announced in the post election 2006-07 Budget provides a number of medium term parameters to ensure continued sound fiscal management. Among other things it provides that the net operating budget be kept in surplus over a rolling 4-year average. The logic is that expenditure increases tend to be fairly constant while revenue can fluctuate more widely. The published forward estimates show that the 4-year target will not be met. The net operating surplus is projected to deteriorate on an annual basis from a surplus of $117mn in 2005-06 to a deficit of $90mn in 2006-07, with continued deficits in the three following years. The 4-year average falls into deficit by 2008-09. The Budget papers explain that further fine tuning will be undertaken to ensure the 4-year target is met.

Tasmania retains its AA+ credit rating.

Sources of Tasmanian population growth



Source: Australian Bureau of Statistics.

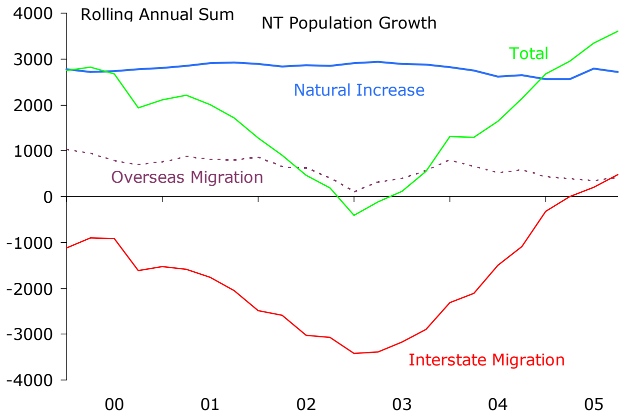
Northern Territory

The NT economy is the smallest in the nation. Growth has slowed in 2005-06, reflecting a moderation of household spending, an easing in what had been frenetic growth in private investment, and a fall in public sector capital works. Trend growth in state final demand in the March quarter of 0.6% ranked fourth, behind WA and Queensland, but also behind Tasmania. NT is viewed as one of the states benefiting from the commodity price boom – which it is – but it is interesting that the volume of exports is relatively small, with goods exports ranking second smallest in the March quarter (even behind Tasmania). What makes exports important to the NT is that they are large relative to the size of the economy, contributing about one fifth of gross state product.

Population growth has accelerated over recent years as the previous emigration from NT to other states has slowed and then reversed. Population growth is now the same as WA, and not much below that of Queensland, at about 1¾%. The key to the improved demographic story is jobs. Employment growth over the year to May was by far the strongest of any state, at close to 6%. But the continued strong population inflows are exceeding the capacity of even the NT economy to create jobs, and so the unemployment rate has edged up to 6%, about one percentage point above the Australian average.

The strong demographic drivers have continued to boost demand for housing, with prices in Darwin rising by 17.5% over the year to the March quarter, second only to Perth. Dwelling construction is strong, although dwelling construction approvals have eased over the first five months of 2006.

Sources of NT population growth



Source: Australian Bureau of Statistics

Growth in 2006-07 is expected to cool slightly to a still robust 5.8% from 6.7% in 2005-06. This will reflect a decline in business investment as work on the Alcan expansion and LNG plant finishes. Exports are projected to continue to expand, with a full year of LNG production, peak production at the Bayu-Undun gas and condensate fields, and increased alumina production from the Alcan G3 refinery. Dwelling construction is expected to remain robust.

Northern Territory Budget

The NT budget recorded a small operating deficit of $19mn in 2005-06. The 2006-07 budget projects a return to a small surplus in that year, but then a fall back into small deficits for the following two years. The inability to sustain significant surpluses will prevent a reduction in debt. Net debt is expected to remain at around $1.8bn out to 2009-10. The operating surplus/deficit projections have deteriorated since the 2005-06 budget due to an actuarial reassessment of superannuation liabilities.

The Northern territory is rated Aa2 by Moody’s.

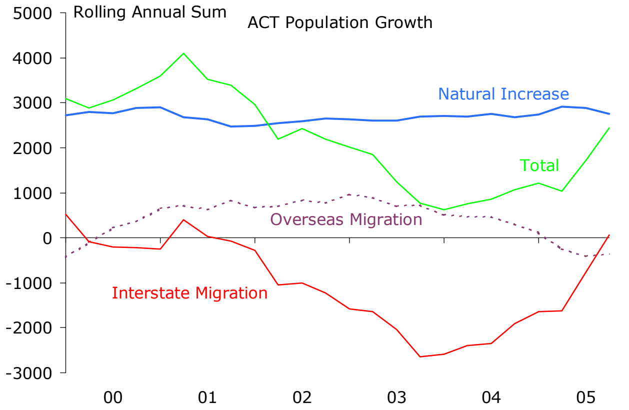
ACT

The ACT has no mining industry and so has been largely by-passed by the commodity price boom and associated infrastructure development. As such, it is one of the south eastern seaboard low growth states. But it is nevertheless performing a little better than the other states in this group, recording trend growth in state final demand of 0.5% in the March quarter 2006. The ACT economy is unique in that government expenditure exceeds that of the private sector – together public sector consumption and investment contributed 55% of March quarter state final demand. Although relatively small, private sector activity remains robust, with household consumption running at quite high levels of 1% per quarter and private investment also recording a robust pace of growth.

ACT population growth lifted a touch over the past year in response to reduced interstate emigration, although this was in part offset by reduced international inflows. Employment growth remains critically dependent on the Commonwealth Government. The unemployment rate is the lowest of the states and territories at 3.4%.

House prices in Canberra rose by only 1.4% over the year to the March quarter, the second weakest result after Sydney, but at least they didn't fall. Dwelling construction approvals rose through 2005 from low levels, but appear to have steadied in 2006.

Sources of ACT population growth



Source: Australian Bureau of Statistics

ACT Budget

The ACT has changed its budget accounting practices to bring them into line with national standards. The changes entail the exclusion of income from land sales and superannuation investment earnings. As a result, the previously measured budget operating surpluses this year and next will now be recorded as deficits. The surplus for 2005-06 of $120mn now becomes a deficit of $162.3mn, with an $80.3mn deficit projected for 2006-07. The budget is projected to be back in surplus by 2008-09.

One of the parameters of the 2006-07 budget was to reduce dependence on land sale receipts and windfall gains from superannuation investments. The budget includes new sources of revenue and measures aimed at improving efficiency and achieving budget savings.

Nevertheless the overall fiscal position remains strong, with the ACT having negative net debt.

The ACT is rated AAA by Standard and Poors.

State Fiscal Parameters

		2004-05	2005-06	2006-07	2007-08
NSW	Operating Balance $mn	724	644	-696	378
	Gen Govt Net Debt $mn	2321	1856	6190	7781
	Public Sector Net Debt $mn (2)	15638	16862	24498	29393
	Public Sector Net Debt $mn (4)	43067	51267	55592	60538
VIC	Operating Balance $mn	792	450	317	305
	Gen Govt Net Debt $bn	1.5	2.0	2.8	4.4
	Public Sector Net Debt $bn (2)	4.0	5.2	6.6	8.6
	Public Sector Net Debt $bn (3)	20.3	17.7	19.7	21.7
QLD	Operating Balance $mn	3,926	2,853	245	247
	Gen Govt Net Debt $mn	-19446	-22130	-21054	-19779
	NF Public Sector Net Debt $mn (2)(5)	-5199	-9054	-4898	-1657
	NF Public Sector Net Debt $mn (3)(5)	15456	14028	19421	23973
SA (1)	Operating Balance $mn	224	27	9	77
	Gen Govt Net Debt $mn	144	194	319	383
	Public Sector Net Debt $mn (2)	2126	2319	2503	6667
	Public Sector Net Debt $mn (3)	9353	8920	9170	9307
WA	Operating Balance $mn	1192	1981	1275	889
	Gen Govt Net Debt $mn	-997	-1877	-1017	-724
	Public Sector Net Debt $mn (2)	4001	4501	5413	6204
NT	Operating Balance $mn	23	-19	17	-18
	Gen Govt Net Debt $mn		1209	1251	1277
	NF Public Sector Net Debt $mn (2)(5)	1656	1708	1776	1804
	NF Public Sector Net Debt $mn (3)(5)	3634	3814	3943	4028
ACT	Operating Balance $mn	52	-162.3	-80.3	-40.7
TAS	Operating Balance $mn	-45.4	117	-90	-101
	Gen Govt Net Debt $mn	229.7	-13.2	-232.4	-298.3

Sources: State Budget papers

1. 2006-07 mid year review. Budget for 2006-07 not scheduled for release until September 2006.
2. Public sector net debt excluding employee liabilities
3. Public sector net debt including employee liabilities
4. Public sector net debt including employee liabilities and insurance claims
5. NF = Non Financial

Gross State Product (GSP) and Employment Projections

		2003-04	2004-05	2005-06	2006-07
NSW	GSP (nominal $bn)	290.7	305.4	322.2	337.8
	GSP (real % pa)	1.4	1.1	1.8	2.25
	Emp (% pa)	1.7	2.0	0.8	1.3
VIC	GSP (nominal $bn)	212.2	222.0	236.0	249.3
	GSP (real % pa)	5.3	2.3	2.6	3.25
	Emp (% pa)	2.4	3.4	1.2	1.5
QLD	GSP (nominal $bn)	144.7	158.5	173.2	184.7
	GSP (real % pa)	5.2	4.1	3.6	4.25
	Emp (% pa)	4.3	5.8	1.5	2.5
SA	GSP (nominal $bn)	56.7	59.8	63.5	66.6
	GSP (real % pa)	2.8	2.6	2.5	2.5
	Emp (% pa)	0	3.1	0.5	0.5
WA	GSP (nominal $bn)	92.3	100.9	111.6	120.1
	GSP (real % pa)	8.1	2.7	4.8	5.25
	Emp (% pa)	2.2	6.3	2.5	3.0
NT	GSP (nominal $bn)	9.4	10.4	11.6	12.6
	GSP (real % pa)	0.2	3.6	6.7	5.8
	Emp (% pa)	0.2	-1.4	6.0	4.0
ACT	GSP (nominal $bn)	17.3	18.3	19.3	20.3
	GSP (real % pa)	0.4	3.0	2.0	2.5
	Emp (% pa)	1.6	2.3	2.2	1.50
TAS	GSP (nominal $bn)	14.8	16.1	17.3	18.3
	GSP (real % pa)	3.7	4.0	3.5	3.5
	Emp (% pa)	3.7	2.8	2.2	2.0
AUST	**GDP (nominal $bn)**	**838.3**	**894.2**	**957.7**	**1012.2**
	GDP (real % pa)	**4.0**	**2.5**	**2.8**	**3.3**
	Emp (% pa)	**2.3**	**3.4**	**1.3**	**2.0**

Sources: ABS cat no 3222.0 (scenario B); growth projections from Economics@ANZ.

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