

OUTLOOK

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Who Dares Wins



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.

The editor of Outlook is James Walsh, Senior Economist.



Chamber of Commerce
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Outlook at a glance

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If navigating the COVID-19 pandemic was a marathon, Western Australia's economy now has its eye on the finish line. Our race plan so far has been largely successful - with performance fuelled by three key factors.

An injection of government stimulus

Over the past 24 months, significant levels of government support have shored up household balance sheets, unlocked business investment and boosted confidence - triggering an avalanche of consumer spending. Housing subsidies and record low interest rates enabled many Western Australians to enter the established market for the first time, creating a substantial pipeline of new residential construction.

The strength of the mining sector

The WA mining industry now comprises 47 per cent of the State's economy - the highest proportion on

record. This means that we've never been more reliant on a single sector for our economic prosperity.

And while favourable conditions in the iron ore sector made up the lion's share of our mining firepower last year, lower borrowing costs and strong global demand triggered an explosion of exploration and investment activity in other key sectors - like gold, copper and lithium.

Fewer restrictions on personal activity

WA's relatively lower levels of restrictions, due to minimal COVID-19 cases throughout the pandemic, helped to tie all of this together. It enabled households to spend their accumulated savings, ensured the mining industry could continue to operate without disruption and supported a sharp increase in intrastate travel.

The upshot of all this is that the size of WA's domestic economy remains well above the level it was before the pandemic, and many economic indicators are flashing green. We expect these tailwinds to continue building into this calendar year, with the WA domestic economy (measured by State Final Demand) forecast to grow 3.75 per cent in 2021-22.

While the story so far has been largely positive, significant headwinds remain that risk curtailing WA's strong trajectory.

Labour shortages

A combination of closed borders and robust demand for workers has triggered acute labour shortages in nearly every industry across the State. According to our latest *Business Confidence Survey*, 79 per cent of businesses were struggling to fill a skilled occupation in December 2021 - up from 54 per cent in the March survey.

Labour shortages inflict deep and far-reaching impacts on the business community. And the longer they persist, the greater the chance they could lead to structural, longer term downgrades in the productive capacity of WA's economy.

While the reopening of WA's borders will take some of the heat out of the labour market - with large mining companies set to move first in attracting talent - solving WA's labour crisis won't be a quick fix. As such, our expectation is that tightness in the labour market will persist for some time.

Supply chain disruptions

Throughout 2021, a global surge in demand for goods ran up against a supply side that was simply not flexible enough, triggering acute supply bottlenecks and a gridlock in the global shipping and logistics system.

As we emerge from COVID-19, those businesses and governments that dare to take on global markets and aggressively seek new trade and investment opportunities will come out of top, while those who remain insular to world of opportunity will be left behind

The result was a sharp increase in shipping costs globally, increased delivery times and large rises in the price of raw materials and other manufactured goods. More recently, the war in Ukraine has underpinned an across the board rise in energy prices, which if sustained for any length of time will act as a material headwind to global growth.

The WA economy has not been immune to these factors, with rising cost pressures and operational delays damaging production, thinning profit margins and halting the growth prospects of many WA businesses. Those tied to contractual obligations – particularly in the construction and manufacturing sectors - have been the hardest hit.

Looking ahead, our expectation is that these pressures will not ease any time soon. There will be some relief when WA's borders reopen, however, as increased passenger aircraft opens up freight capacity for small, high value and perishable items.



COVID-19

The Omicron variant has created new challenges – many of which WA has yet to experience.

While the absolute impact of Omicron on household spending remains to be seen, real-time mobility data suggests Western Australians are scaling back visits to retail and recreational premises. So far, this reflects people voluntarily reducing their social interactions to reduce risk of infection, additional restrictions on personal activity (i.e. mask mandates) and isolation requirements.

All this points toward a tougher few months for many WA businesses – particularly those in the retail, hospitality and events sectors. However, with WA's high vaccination rates, lower-density urban sprawl and ongoing baseline COVID-19 restrictions, our central expectation is that Omicron will dent, not derail WA's strong economic trajectory.

Looking beyond Omicron – the outlook for WA's economy remains largely positive.

COVID-19 is expected to gradually progress into an 'endemic' phase, softening the impact of future variants on our economy and community.

Business investment is expected to pick up pace throughout the rest of this financial year and next, fuelled by government tax incentives, relatively lower borrowing costs and – the big ticket items – Woodside's Scarborough and Pluto 2 projects. The outlook for WA's iron ore exports remains favourable, with the Chinese Government looking to strengthen its economy this year.

Non-mining investment is expected to increase over the forecast horizon, reflecting a solid pipeline of investment in the critical minerals (e.g. lithium) and property development sectors. Indeed, a focus on ESG and climate mitigation will continue to grow as central investment priorities for WA businesses in the years ahead.

Household consumption is expected to remain robust over the coming years, underpinned predominantly by sustained tightness in WA's labour market and a recovery in population growth.

While net overseas migration is likely to remain below pre-COVID levels – reflecting an anticipated outflow of young, skilled Western Australians – we believe this will only partially offset the uplift associated with opening the borders to long-term migrants and international students.

History has shown that when there's an abundance of stable, well-paying jobs in WA, inbound migration levels lift. And with a backdrop of strong business investment, solid household consumption and an anticipated ramp up of the State Government's Asset Investment Program – demand for WA based workers is expected to remain strong.

Indeed, we expect WA's unemployment rate to average 3.8 per cent this financial year – the lowest in 13 years – with the jobs market set to remain tight throughout the forecast horizon.

Sustained tightness in the labour market has translated into a stronger outlook for wages, but an economy-wide spike remains unlikely. While an increasing number of businesses are lifting base wages in response to labour shortages, many continue to lean on other measures – like sign-on bonuses - to attract workers. All up, we expect headline wages growth to hit 2.25 per cent this financial year, before accelerating to 2.5 per cent in 2022-23.

The significant pipeline of new housing construction will act as another key support for the economy over the medium term, with supply disruptions and labour shortages smoothing completion timelines into 2022-23 and early 2023-24. At the same time, rising input costs and expectations of cash rate rises this year have reduced the feasibility of some new development opportunities, dimming the outlook for greenfield investment.

Higher costs are quickly becoming a central concern for WA businesses. Supply-side disruptions and labour shortages have triggered a surge in both headline and underlying inflation (globally) in recent months – with higher prices starting to flow through to local WA consumers.

While there remains considerable uncertainty about how and when these issues will subside, our expectation is that inflationary pressures will continue to heat



up throughout this financial year. Looking ahead, we expect these pressures to ease in 2022-23 as global demand rebalances back to services and WA's borders reopen - alleviating pressures on domestic and international supply chains.

All told, WA's economy has entered 2022 on a solid footing. Robust domestic demand, a red-hot labour market and strong resources sector have set the scene for an encouraging year ahead – with the impact of Omicron expected to be short-lived.

While we expect WA's strong economic momentum to continue, significant challenges remain that, if left unaddressed, pose material risks to WA's economic and social prosperity. Rising operating costs, acute labour shortages and the lack of economic diversification are all central issues that must be resolved before WA can realise its potential.

To this end, it's critical all economic stakeholders – all tiers of government, industry and community – stand ready and willing

to capitalise on new and emerging opportunities once COVID-19 starts to fade and WA re-joins the world.

Ramping up our trade and investment strategy and undertaking meaningful tax reform would be great places to start.

Indeed, WA businesses currently pay more payroll tax than those in any other state over a wide range of taxable wages, and organisations around the country have identified that this severely damages their perception of WA as an attractive place to invest.

As we emerge from COVID-19, those businesses and governments that dare to take on global markets, aggressively seek new trade and investment opportunities and play hard for highly skilled migrants will come out of top, while those who remain insular to world of opportunity will be left behind.

Section 1: Economic Outlook

Economic forecasts for Western Australia

Forecasts ¹	2020-21 Actual	2021-22 Forecast	2022-23 Forecast	2023-24 Forecast
Economic Activity				
Household Consumption	2.7%	2.75%	2.0%	2.50%
Dwelling Investment	2.0%	10.0%	7.50%	-10.0%
Business Investment	4.6%	2.0%	7.75%	1.25%
State Final Demand	4.4%	3.75%	3.25%	2.0%
Exports	-0.8%	-0.5%	1.75%	0.75%
Imports	-7.1%	-2.75%	10%	6.25%
Gross State Product	2.6%	2.75%	2.0%	1.0%
Labour Market				
Unemployment	6.1%	3.8%	3.75%	3.75%
Inflation	1.6%	3.75% ³	2.75%	2.25%
Wages	1.5%	2.25%	2.5%	2.75%

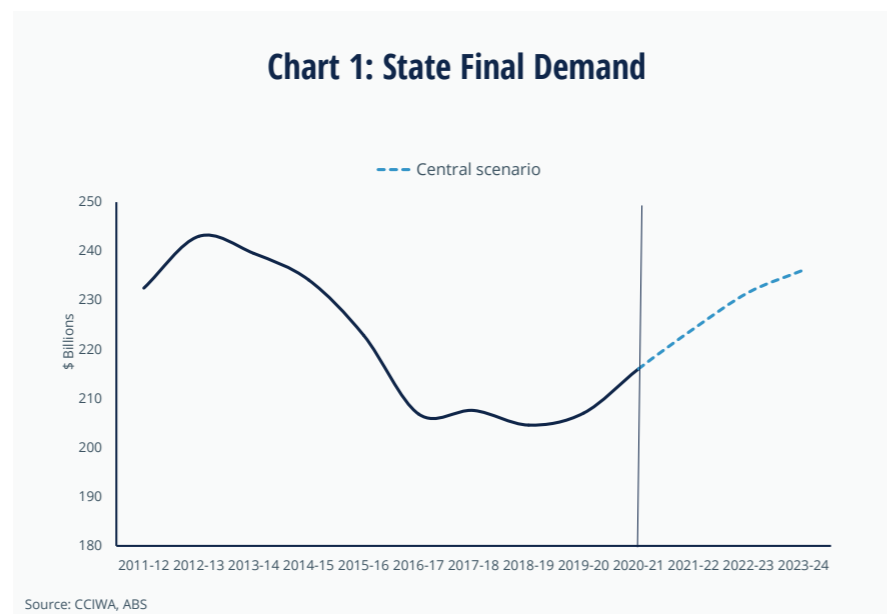
Notes:
 1 Actual outcomes are as reported in the 2020-21 State Accounts, updated with the latest State Final Demand and Balance of Payments data.
 2 Forecasts for economic activity are produced in terms of annual average growth, comparing four quarters of data to the previous four quarters of data.
 3 In line with the approach taken by WA Treasury, the 2021-22 CPI estimate excludes the 'electricity' sub-index to remove volatility associated with government subsidies in 2020.

Economic Growth

Forecasts	Economic Activity	
	State Final Demand	Gross State Product
2020-21 Actual	4.4%	2.6%
2021-22 Forecast	3.75%	2.75%
2022-23 Forecast	3.25%	2.0%
2023-24 Forecast	2.0%	1.0%

WA's economy has gone from strength to strength throughout the COVID-19 pandemic. Fundamentally, growth has been underpinned by robust household consumption, solid activity in the mining and construction sectors and low levels of unemployment.

As such, we expect WA's domestic economy (State Final Demand) to grow by 3.75 per cent this financial year. Looking beyond, we're



expecting growth of 3.25 per cent in 2022-23, before easing slightly to 2.0 per cent in 2023-24.

Global supply disruptions and ongoing border closures have impacted import volumes of both goods and services this financial year (relative to expectations), which we

expect will help the overall economy to grow by 2.75 per cent in 2021-22. The growth figure is expected to moderate in 2022-23 and 2023-24 as borders reopen and goods imports increase in line with the anticipated pick-up in business investment.

Closure of international borders forced travel-hungry Western Australians to redirect much of their travel funds to the regions – adding up to \$6 billion to the economy

Household Spending

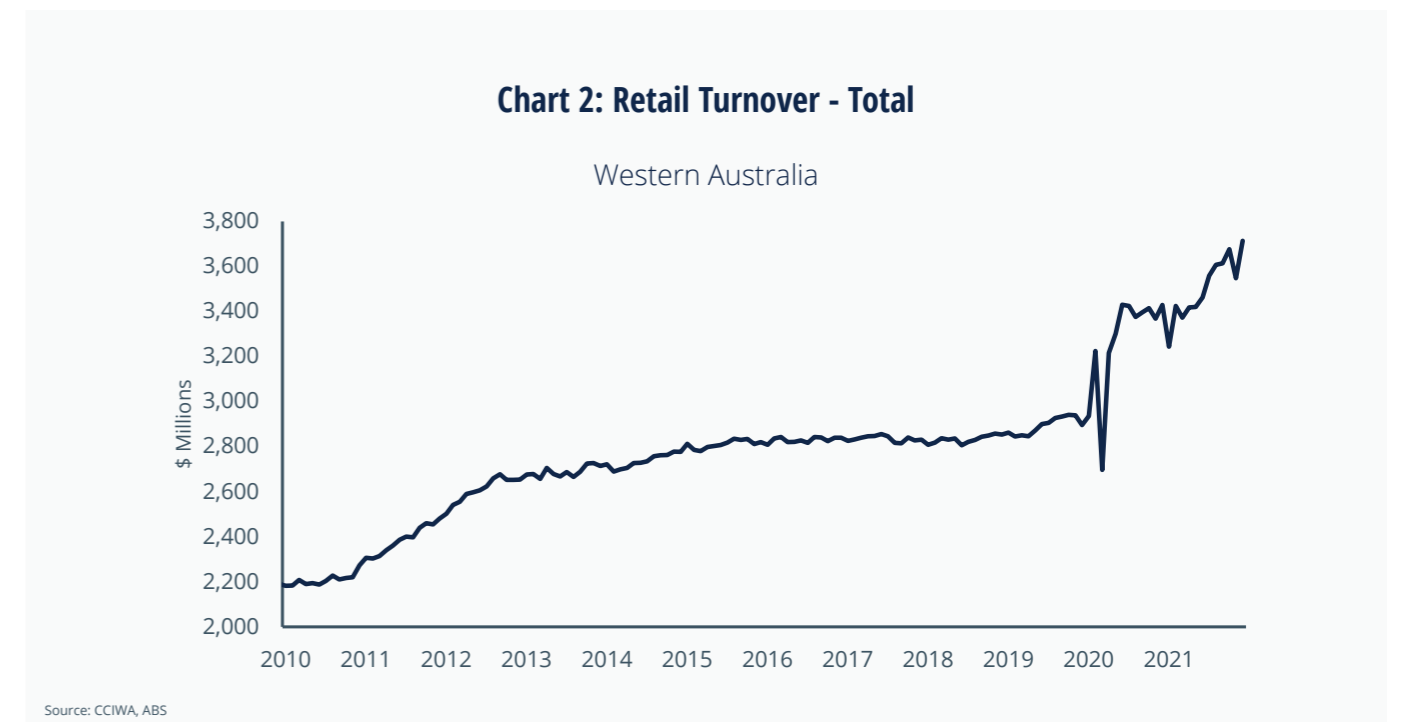
Forecasts	Economic Activity
	Household Consumption
2020-21 Actual	2.7%
2021-22 Forecast	2.75%
2022-23 Forecast	2.0%
2023-24 Forecast	2.5%

2021-22 has been the year of the WA consumer. An enormous amount of pent up demand has been unlocked over the past 12 months, with retail turnover currently up 128 per cent on pre-COVID levels (Chart 2). Sharp rises in non-wage remuneration (e.g. sign on bonuses) have helped to underpin a tidal wave of discretionary spending – think Jet Skis, caravans and eating out.

And it hasn't all been spent in the cities. Ongoing border closures have forced travel-hungry Western Australians to redirect much of their travel funds to the regions – adding up to \$6 billion to the economy.

As a result, we expect household consumption to grow 2.75 per cent in 2021-22 and hold firm throughout the forecast horizon.

Key risks to this outlook include the reintroduction of harsher containment measures as COVID-19 cases rise, higher than anticipated inflationary pressures (curbing appetite to eat out) and softer net migration levels when borders reopen.





Business Investment

Economic Activity

Forecasts	Business Investment
2020-21 Actual	4.6%
2021-22 Forecast	2.0%
2022-23 Forecast	7.75%
2023-24 Forecast	1.25%

Soaring commodity prices, robust global demand and government tax concessions helped to underpin a sharp rise in Western Australian business investment in the first half of 2021.

While private investment softened toward the end of the last year – with machinery and equipment investment down 10 per cent over the December quarter – forward looking indicators point towards a pickup in activity in H1 2022. As such, we expect business investment to grow 2.0 per cent this financial year.

Growth is set to accelerate to 7.75 per cent in 2022-23, underpinned predominantly by Woodside's Scarborough project and Pluto 2 extension.

Looking beyond the big-ticket items, WA mineral exploration spending remains solid. ABS data suggests total deposit expenditure in WA hit a record high in September 2021 at \$553 million (**Chart 3**).

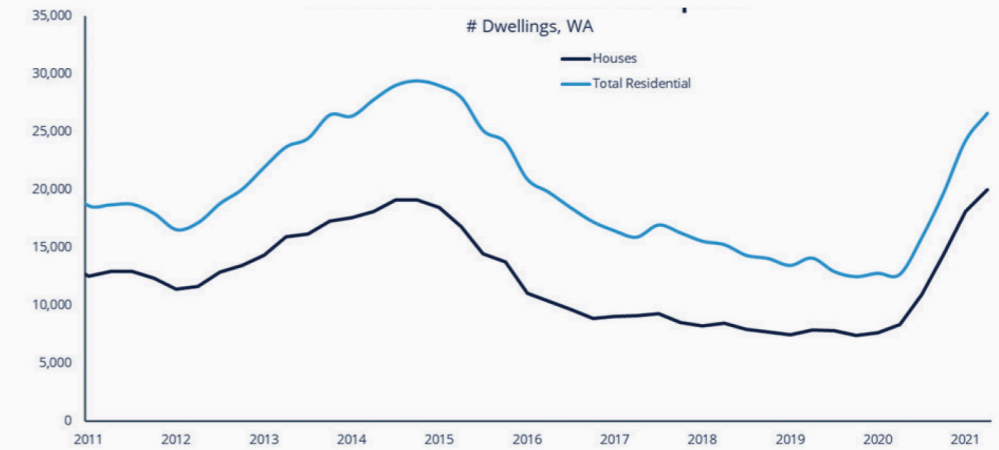
Over the longer term, the global acceleration toward decarbonisation and associated uptake of electric vehicles will support growth in WA's critical and battery minerals sectors.

Key risks to the outlook include worsening trade disputes with China, prolonged disruptions to global supply chains (pushing up operating costs), and ongoing labour shortages.

Chart 3: Mineral Exploration Expenditure



Chart 4: Residential Construction in the Pipeline



All up, we expect exports to decline marginally in 2021-22 before accelerating to 1.75 per cent in 2022-23

Dwelling Investment

Economic Activity

Forecasts	Dwelling Investment
2020-21 Actual	2.0%
2021-22 Forecast	10.0%
2022-23 Forecast	7.5%
2023-24 Forecast	-10.0%

Generous support from the State and Commonwealth Governments, record low interest rates and soaring confidence sparked an explosion in demand for residential properties in 2021 – lighting a fuse under WA's construction pipeline (**Chart 4**).

For many of these builds, construction will commence this financial year. However, shortages of both skilled labour and key materials have pushed back completion timelines, smoothing the construction pipeline further along the forecast horizon.

International Trade

Economic Activity

Forecasts	Exports	Imports
2020-21 Actual	-0.8%	-7.1%
2021-22 Forecast	-0.5%	-2.75%
2022-23 Forecast	1.75%	10.0%
2023-24 Forecast	0.75%	6.25%

Conditions remain mixed for Western Australia's exporters. While producers of agricultural and food commodities have had a bumpy ride over the past 24 months – triggered by the imposition of strict import tariffs by China – our key iron ore players have enjoyed favourable demand-side conditions.

Looking ahead, scheduled maintenance, seasonal weather disruptions and COVID-19 isolation requirements are expected to dim shipping volumes this quarter, before recovering in Q2 2022. Iron ore export volumes are expected to hold firm in 2022-23, with China signalling a pull-forward of policy easing to support domestic economic growth this year.

What's more, foreign central banks are expected to tighten monetary policy sooner and more aggressively than the

RBA in order to combat skyrocketing inflation in their domestic markets. We expect this to widen Australia's interest rate differential and apply downward pressure to the AUD over the coming year, in turn supporting the competitiveness of our exporters.

All up, we expect exports to decline marginally (-0.5%) in 2021-22 before accelerating to 1.75 per cent in 2022-23 as international students and foreign tourists return to WA shores.

While goods imports have held up throughout the pandemic – driven primarily by robust machinery, equipment and vehicle consumption – ongoing supply disruptions have slowed momentum in recent months. We expect these disruptions to continue through the remainder of this financial year, before gradually unwinding in 2022-23.

The reopening of international borders is expected to trigger an outflow of Western Australians – boosting services imports – with many seeking to enjoy their first overseas holiday in two years.

Taken together, we're expecting imports to fall -2.75 per cent in 2021-22, before rebounding in 2022-23 and 2023-24.

There are now more Western Australians employed than before the pandemic

Unemployment

Economic Activity	
Forecasts	Unemployment
2020-21 Actual	6.1%
2021-22 Forecast	3.8%
2022-23 Forecast	3.75%
2023-24 Forecast	3.75%

Western Australia's jobs market is as tight as a drum. In December 2021, WA's headline unemployment rate fell to 3.4 per cent - its lowest in 13 years - and there are now more Western Australians employed than before the pandemic.

This has all been underpinned by a sharp rise in demand for WA-based workers and the closure of WA's interstate and international borders. As such, job vacancies continue to soar and are currently sitting at record highs (Chart 5).

While this is good news for job-hunters, the shortage of local talent has triggered acute economy-wide labour shortages - damaging the

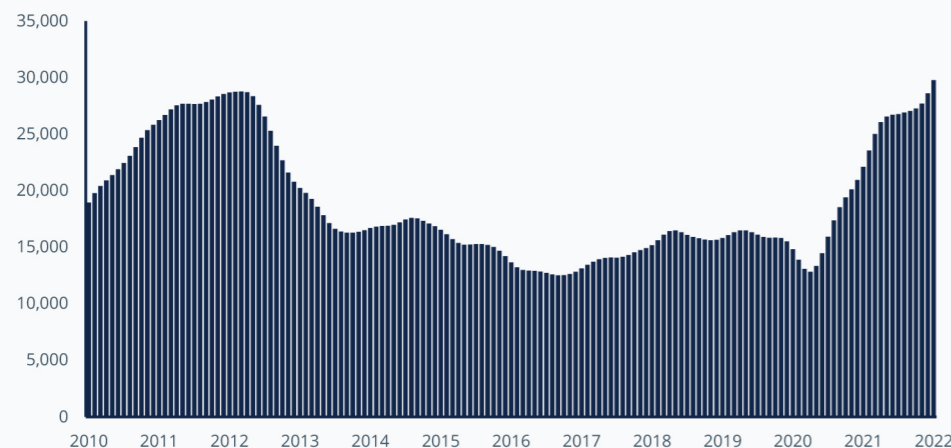


productive capacity and future growth prospects of many WA businesses.

average 3.75 per cent in 2022-23 and 2023-24.

Labour market conditions are expected to remain hot over the coming years, with the unemployment rate expected to

Chart 5: Internet Job Ads
Western Australia, Seasonally Adjusted



Source: ABS, CCIWA



Wages and Inflation

Economic Activity		
Forecasts	Inflation	Wages
2020-21 Actual	1.6%	1.5%
2021-22 Forecast	3.75% ¹	2.25%
2022-23 Forecast	2.75%	2.5%
2023-24 Forecast	2.25%	2.75%

Inflation outlook

Global supply disruptions, geopolitical tensions and chronic labour shortages have triggered a burst of inflationary pressures in recent months, with the Perth Consumer Price Index rising 2.2 cent over the 6 months to December 2021.

We expect these pressures to remain strong over the remainder

of this financial year. As such, we're forecasting CPI to hit 3.75 per cent in 2021-22 in annual average terms (excluding the electricity sub-index - see footnote). Looking ahead, we expect inflationary pressures to soften marginally in 2022-23 as global demand rebalances back to services and WA reopens to the world - easing pressures on domestic and international supply chains.

Given the significant level of uncertainty as to how and when supply disruptions, geopolitical factors and labour shortages will evolve, there is likely to be upside risk to our base case inflation estimates.

Wage outlook

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

With sustained tightness in WA's labour market expected over the coming months, we anticipate base wage pressures to rise throughout the remainder of this financial year.

All up, we expect growth in the headline Wage Price Index to hit 2.25 per cent this financial year, before rising to 2.5 per cent in 2022-23.

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