9.1 ECONOMIC CONDITIONS

Overview

Economic growth in the Territory has moderated since 2010-11, and is forecast to moderate further in 2012-13 reflecting planned withdrawal of fiscal stimulus by the Commonwealth in the current year, and further fiscal consolidation in 2012-13.

The level of economic activity, however, remains high due to its strong fundamentals including a low unemployment rate and a high labour force participation. The economy is expected to continue to grow in 2012-13, but at a slower rate, mainly due to a decrease in public consumption expenditure and below-trend household consumption growth and investment growth.

The near-term outlook for the global economy has improved, but growth is expected to remain below-trend in 2012 with divergent conditions across the various regions. The euro area is affected by sovereign debt problems and is expected to experience a mild recession in 2012, though significant measures have been taken in response to the crisis. The US economy is expanding at a moderate pace, but remains fragile. Growth in China has slowed and is likely to be maintained at a more sustainable pace. Risks of a renewed upsurge of the crisis in Europe, as well as higher oil prices, pose downside risks to global economic prospects.

The outlook for national Gross Domestic Product (GDP) growth remains positive, underpinned by prospects of strong growth in mining investment and continuing high commodity prices. The latest forecasts from the Commonwealth Government, as well as the Reserve Bank of Australia (RBA), reflect national economic growth reaching close to trend in 2012-13.

Despite the favourable national economic outlook, conditions remain subdued in a number of sectors of the Australian economy due to the high exchange rate, weak consumer confidence, changes in household spending behaviour and the scaling back of public investment.

The Outlook for the ACT Economy

The prospects for the **ACT economy** in 2012-13 will be influenced by the Commonwealth Government's fiscal consolidation.

The measures necessary for the Commonwealth Government to achieve its fiscal targets have been stronger than previously envisaged due to its weaker than expected revenues. The Commonwealth Government's expenditure is expected to decrease in 2012-13.

This is reflected in the modest growth outlook for the ACT economy in the short term. The key economic aggregates for the ACT are summarised in Table 9.1.1.

Table 9.1.1
Economic Forecasts, Year-Average Percentage Change

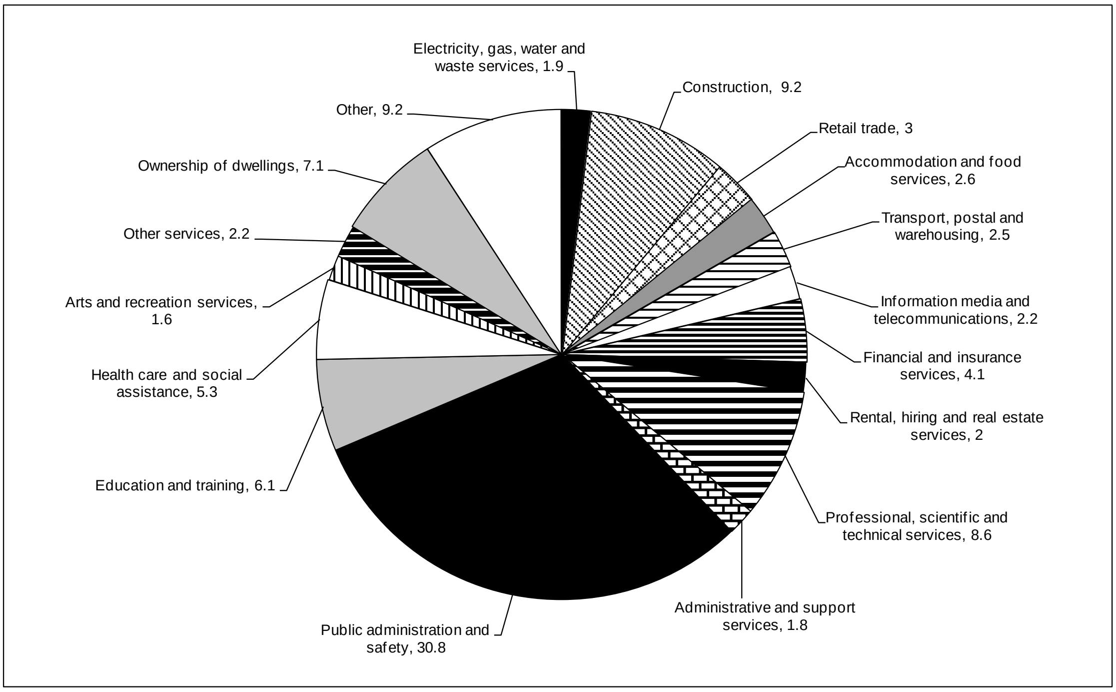
	Actual	Forecasts[1]	
	2010-11	**2011-12**	**2012-13**[2]
ACT			
Gross State Product	2.8	2½	2
Employment	2.2	½	0
State Final Demand	4.3	2	½
Consumer Price Index	2.7	2½	2¼
Wage Price Index[3]	3.6	3½	3½
Population[4]	1.9	1½	1½
Australia			
Gross Domestic Product[5]	1.9	3	3¼

Notes:
1. Forecasts and projections are rounded to a ¼ of a percentage point to reflect the relative level of accuracy used in forecasting economic parameters.
2. The forecasts incorporate the estimated impact of the Commonwealth carbon price scheme commencing in 2012-13.
3. Total hourly rates of pay excluding bonuses.
4. The population forecasts and projections reflect Chief Minister and Cabinet Directorate estimates. The forecasts are based on the rate of growth from the June quarter compared to the June quarter of the previous year, rather than 'year average' as with all other forecasts.
5. 2012-13 Commonwealth Budget forecasts for 2011-12 and 2012-13.

The Territory's economic growth in 2012-13 is expected to be significantly constrained by Commonwealth Government spending restraint. Household consumption expenditure growth and investment growth are also expected to remain below trend.

Gross State Product (GSP), the Australian Bureau of Statistics' (ABS) headline measure of the ACT economy is forecast to grow by 2 per cent in 2012-13, reflecting the weaker short term outlook. On the expenditure side, the growth in GSP will be supported by private consumption and total investment.

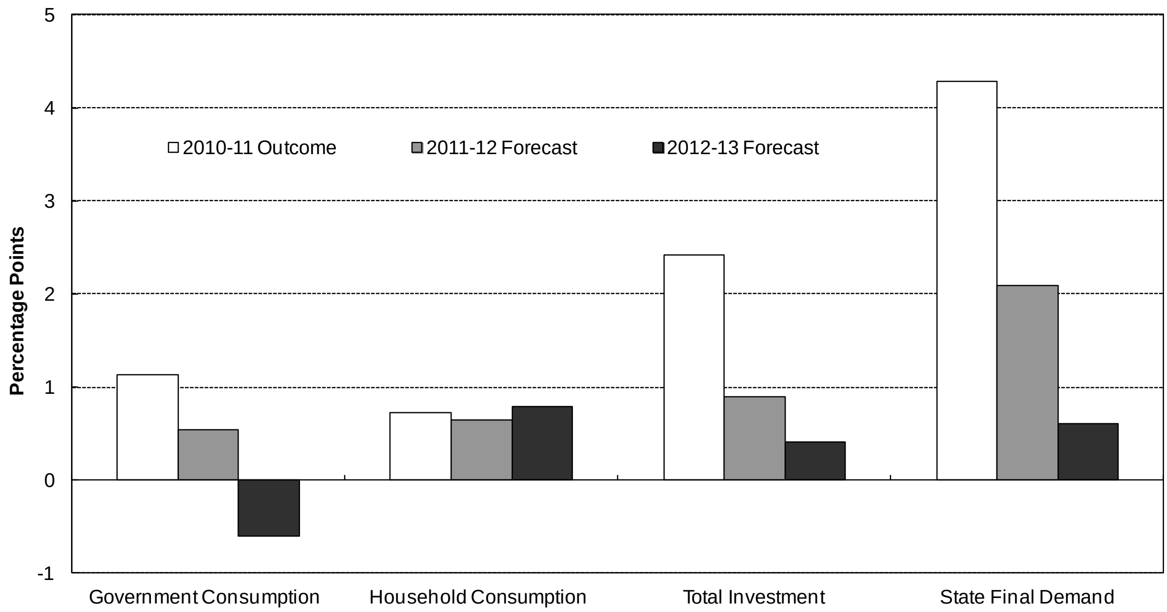
Figure 9.1.1
Share of Gross State Product 2010-11 Current Price Industry Value Added



Source: ABS Cat No. 5220.0. 'Other' includes Agriculture, Forestry & Fishing, Mining, Manufacturing, Wholesale trade and Taxes less subsidies on products.

State Final Demand (SFD) growth is forecast to moderate to ½ per cent in 2012-13. The forecast growth reflects contributions from household consumption and total investment, partly offset by a negative contribution from public consumption. The decrease in Commonwealth Government expenditure, combined with below trend private consumption growth and investment growth are expected to lead to the lowest SFD growth in more than two decades. Contributions to SFD growth from the various components are shown in Figure 9.1.2.

Figure 9.1.2
Contributions to Growth in ACT State Final Demand



Source: ABS Cat No. 5206.0 and ACT Treasury calculations.

Government consumption expenditure in the ACT is forecast to decrease in 2012-13 given the Commonwealth Government's planned fiscal consolidation as it seeks to return its budget to surplus. Risks continue to be on the downside.

Household consumption expenditure growth is expected to remain below trend in 2012-13. The interest rate environment and solid population growth is supportive of household consumption expenditure, however, the softening in the labour market and ongoing consumer caution are restraining spending. Households are prudently managing their balance sheets and are spending a smaller proportion of their disposable income – a legacy of the global financial crisis.

Total investment growth is expected to moderate further in 2012-13, following a number of years of robust growth, but with the level of investment as a ratio of SFD remaining at record levels.

Dwelling investment remains at a high level, supported by the ACT Government's residential land release program and solid population growth. However, the residential building cycle is expected to soften further in 2012-13 from the strength seen in recent years, nevertheless with activity remaining at high levels. Residential building approvals have now fallen to below the five year average level, mainly due to a weakening in approvals for townhouses, flats and apartments which were running at record levels in 2010-11.

The ACT Government continues to pursue policies to improve housing affordability in the Territory. The 2012-13 indicative residential land release program includes the release of 19,500 dwelling sites in the next four years.

With large investment projects nearing completion, **non-dwelling construction** is expected to return to a more normal level in 2012-13.

Public investment growth is expected to remain below trend in 2012-13, given the significant growth recorded in 2009-10 and 2010-11, notwithstanding significant new investments being made by the ACT Government and some major projects continuing, such as the enlargement of the Cotter Dam as well as the commencement of construction of the Majura Parkway.

ACT **labour market** activity is forecast to ease in 2012-13 consistent with moderating economic growth and the Commonwealth Government's planned reduction in average staffing levels.

Population growth of 1½ per cent is forecast in 2011-12 and 2012-13. This is slightly stronger than the historical long-run average of 1¼ per cent. These forecasts take into account Estimated Resident Population data, as released by the ABS, as well as the most recent estimates of fertility, mortality and migration. These assumptions indicate the ACT's population growth will be predominantly influenced by natural increase and net overseas migration, with net interstate migration projected to have little effect on overall population growth.

Labour Market

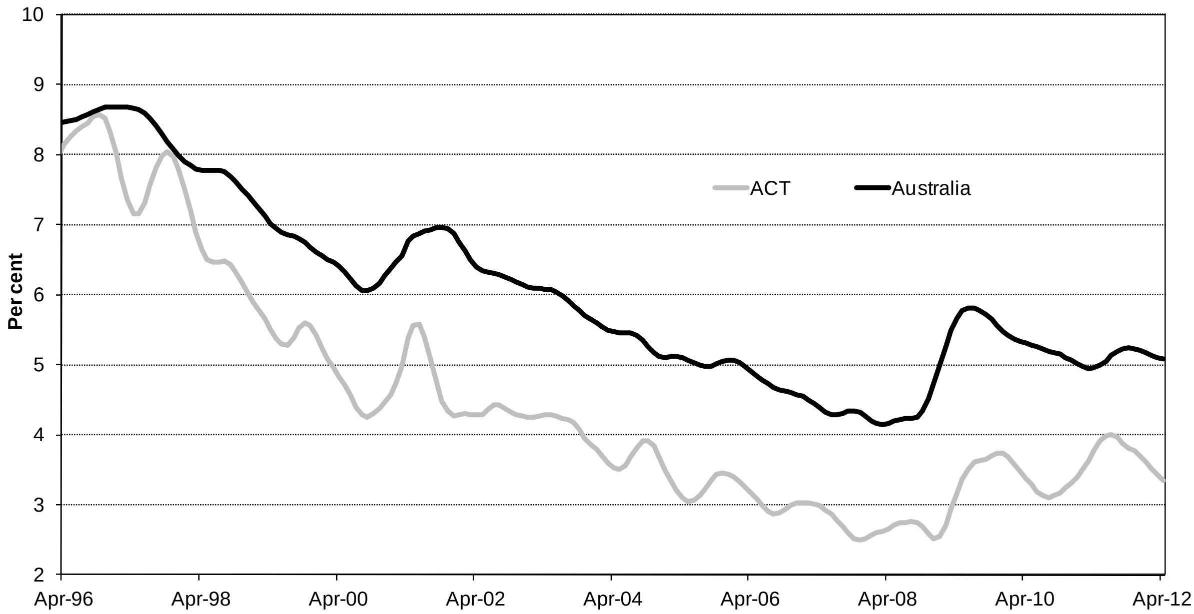
Employment

ACT employment growth has moderated noticeably in line with the slowdown in broader economic activity, following relatively strong employment growth in recent years. Employment growth is also restrained by private sector caution in light of ongoing global economic risks and the uncertainty with respect to the strength of the Commonwealth Government's fiscal consolidation.

The employment level is nevertheless around 6 per cent higher than that prior to the Global Financial Crisis, with the unemployment rate in the ACT remaining well below the national average. The ABS measure of job vacancies, a forward-looking indicator of labour demand, increased in the February quarter 2012, with the vacancy rate remaining well above its long-run average level.

Employment growth in the ACT in 2012-13 is expected to be flat given the moderation in economic growth and planned Commonwealth Government fiscal consolidation. Risks continue to be on the downside as heightened uncertainty around the outlook for demand may lead businesses to hold off hiring.

Figure 9.1.3
Unemployment Rate, ACT and Australia, Monthly Trend Data



Source: ABS Cat No. 6220.0.

Labour Costs

Labour cost pressures are likely to remain contained in the ACT, given the modest outlook for economic growth due to planned Commonwealth Government fiscal consolidation. Delays in implementing new enterprise bargaining agreements in the public sector has led to weaker-than-expected wages growth in the first half of 2011-12. Wage restraint is expected to continue in the public sector in the short term.

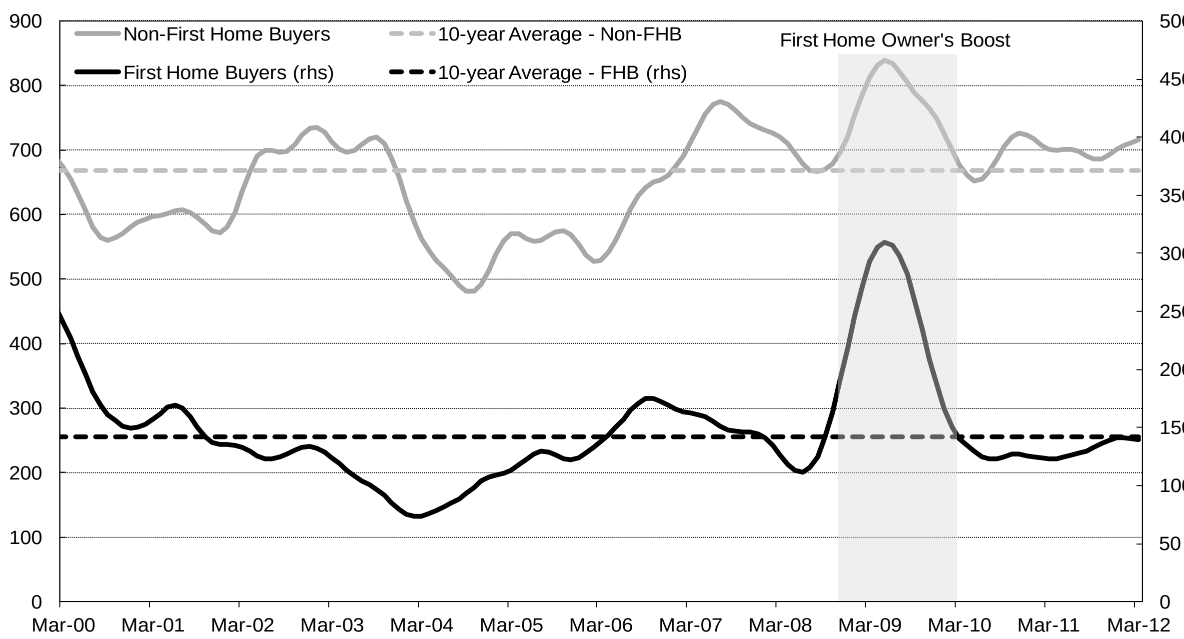
Wages, as measured by the Wage Price Index (WPI), are forecast to grow by 3½ per cent in both 2011-12 and 2012-13 with the moderation in labour market conditions reducing the likelihood of a sharp acceleration in wage inflation. The WPI growth forecasts are lower than the average growth rate of around 4 per cent in the last five years.

Housing Market

The Canberra housing market has softened during 2011-12. Turnover, however, remains at relatively high levels. In line with national trends, measures of house prices are lower over the year to the March quarter 2012. The Canberra housing market is still amongst the strongest in the nation.

The momentum of housing construction has slowed in the wake of record dwelling approvals that peaked in June 2011. The recent lower interest rates and solid population growth, however, are expected to support the housing market going forward. First home buyers are returning to the market, following a period of weaker activity since the withdrawal of the First Home Owner’s Boost. Non-first home buyer activity remains above the long-term average.

Figure 9.1.4
ACT Number of Housing Finance Commitments for Owner Occupation, Monthly Trend Data



Source: ABS Cat No 5609.0 and ACT Treasury calculations.

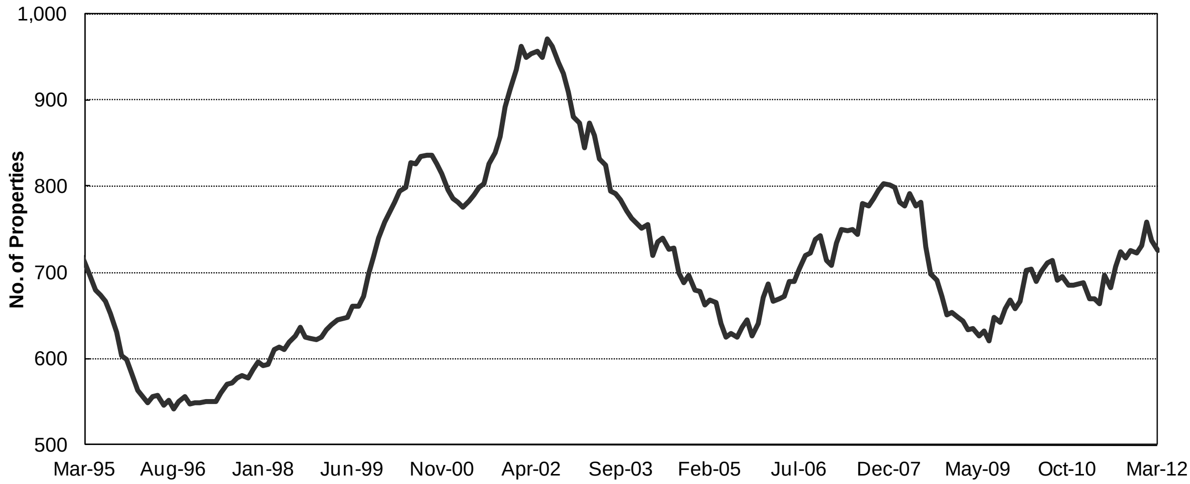
A major challenge facing the ACT property market is the Commonwealth Government’s expenditure constraint as part of its objective to return the Budget to surplus in 2012-13.

The ACT housing market, however, continues to provide an attractive investment option due to a tight rental market, gains in house prices and a stable labour market.

Turnover of New and Established Dwellings

Turnover of new and established dwellings in 2012-13 is expected to remain at a relatively high level, supported by the ACT Government's land release program, solid population growth and relatively low interest rates. Consumer caution and the softer labour market outlook, however, weigh on housing demand. The ACT Government's housing affordability initiatives and residential land release program will continue to provide improved access to housing.

Figure 9.1.5
ACT Residential Turnover, 12-Month Moving Average, Monthly Original Data

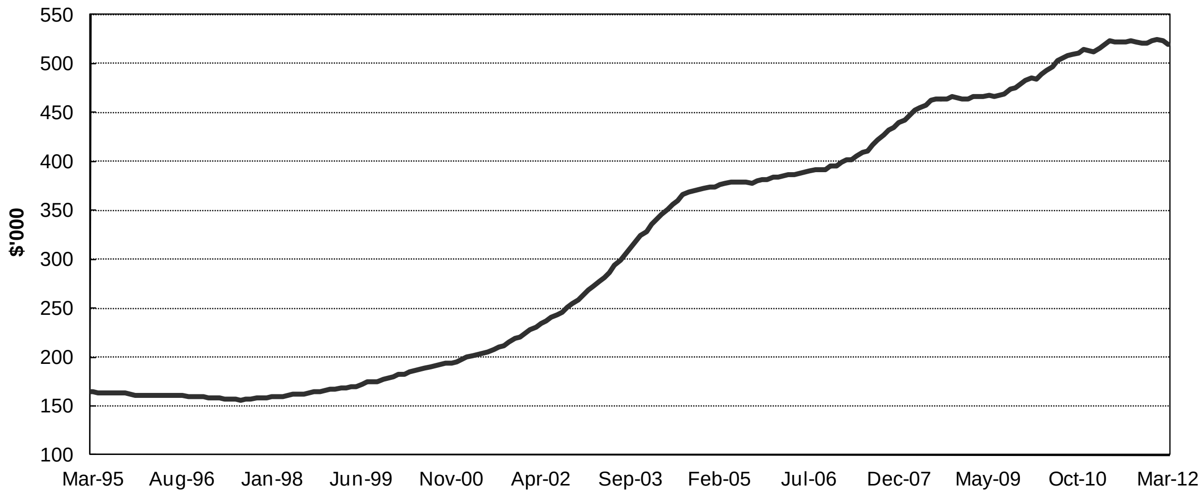


Source: ACT Planning and Land.

Price Movements

Growth in house prices has shown signs of stabilisation due to a range of factors including the withdrawal of Commonwealth Government stimulus measures and an increase in housing supply. Dwelling prices are expected to grow marginally in real terms.

Figure 9.1.6
ACT Residential Property Average Price, 12-Month Moving Average, Monthly Original Data



Source: ACT Planning and Land.

Rental Market

The weekly rent for a three bedroom house in Canberra in the year to the December quarter 2011 rose by 2.2 per cent, the second lowest growth rate of all jurisdictions. The ACT rental vacancy rate, at 1.9 per cent in the December quarter 2011 was the second lowest in the country, indicating ongoing strong demand for rental properties. The increase in housing supply and the easier monetary policy stance are expected to ameliorate pressure on the rental market in the medium term.

Consumer Prices and Interest Rates

Consumer Prices

In the year to the March quarter 2012, the Consumer Price Index (CPI) grew by a lower-than expected 1.6 per cent in both Canberra and nationally. The lower outcome was partly due to a base effect, with both Canberra and Australia recording high inflation in early 2011 due to natural disasters boosting fruit and vegetable prices significantly.

The Commonwealth Government has indicated that the national CPI inflation rate is likely to be 1¼ per cent through the year to the June quarter 2012 and 3¼ per cent through the year to the June quarter 2013.

While upward pressure on wages growth (particularly in the mining states), oil and utility prices is expected to flow through to higher consumer prices nationally, the high Australian dollar is expected to, in part, place downward pressure on inflation.

Underlying inflation pressures in the local economy were relatively subdued in the year to the March quarter 2012. Over the coming year, underlying price pressures in the ACT are expected to remain well contained in an environment of modest economic growth and a planned reduction in employment in Commonwealth Government agencies.

CPI inflation in Canberra is expected to moderate to 2½ per cent in 2011-12 and further to 2¼ per cent in 2012-13.

Interest Rates

With the inflation outlook having improved in late 2011, the RBA lowered the cash rate by a cumulative 50 basis points at its November and December meetings, after having maintained a mildly restrictive monetary policy stance throughout most of 2011.

The RBA lowered the cash rate by a further 50 basis points in May 2012, given the benign inflation outcome in the March quarter 2012. This confirmed that the inflation outlook has provided scope for a further easing of monetary policy given recent softer-than-expected domestic economic conditions.

The ACT Budget forecasts assume that interest rates in 2011-12 and 2012-13 will move broadly in line with market expectations.

Lower interest rates in the short term will support business investment, household spending and broader economic growth in the ACT and nationally.

Forward Year Projections

Forward year projections are included in Table 9.1.2 below. Projections are based on long-run averages and are provided for planning purposes only, and do not reflect an expectation (forecast) of actual outcomes.

Table 9.1.2
Economic Projections, Year-Average Percentage Change

	Projections [1]		
	2013-14	**2014-15**	**2015-16**
ACT			
Gross State Product	3	3	3
Employment	1¾	1¾	1¾
State Final Demand	4¾	4¾	4¾
Consumer Price Index	2½	2½	2½
Wage Price Index[2]	4	4	4
Population[3]	1½	1½	1½
Australia			
Gross Domestic Product[4]	3	3	3

Notes:

1. Projections are rounded to a ¼ of a percentage point to reflect the relative level of accuracy used in estimating economic parameters.
2. The population projections reflect Chief Minister and Cabinet Directorate estimates. The estimates are based on the rate of growth from the June quarter compared to the June quarter of the previous year, rather than 'year average' as with all other projections.
3. Total hourly rates of pay excluding bonuses.
4. 2013-14 is a forecast year in the 2012-13 Commonwealth Budget.