

6.1 ECONOMIC CONDITIONS

Introduction

This chapter reviews the ACT's current economic conditions, outlines the ACT Government's economic strategy and provides forecasts of major economic parameters for the Budget period.

In examining the data in this chapter it must be remembered that caution should be exercised when using data from the ABS for the ACT. This is mainly due to the small size of the ACT, where single transactions or small changes in the sample can create large variations. Some data series, which are available for other States, are not published for the ACT, because of the ABS's own concerns about their accuracy.

Overview

During 1999-2000 the ACT economy continues to experience strong economic growth, with State Final Demand (SFD) increasing at a faster rate than any other Australian State in the year to December 1999. This illustrates the success of the Government's strategy of creating and maintaining a positive environment for businesses to locate here, and for existing businesses to invest, grow and expand. It also demonstrates the inherent strength of the ACT economy, and the advantages of an increasingly diversified private sector underpinned by a strong public sector.

The economic forecasts underpinning the 2000-01 Budget are summarised below.

**Table 6.1.1
ACT Economic Forecasts**

	1998-99 (Actual)	1999-2000 (Forecast)	2000-01 (Forecast)	3 Year Planning Assumptions 2001-02 to 2003-04^(b) (Average annual growth)
	Percentage change on the previous year ^(a)			
Gross State Product ^(c)	2.6	3.6	3.8	3.5
Employment Growth ^(c)	1.7	3.1	1.7	1.1
Consumer Price Index ^(d)	0.2	2.5	5.5	2.5
State Final Demand	4.5	5.0	2.3	2.6
Population ^(c)	0.7	0.7	0.7	0.8

- (a) Based on original data currently available, with financial data expressed in real terms. Percentage changes are expressed in year average or year total terms unless otherwise indicated.
- (b) The planning assumptions used in this document represent the estimated average annual change for the period 2001-02 to 2003-04. As such they do not represent expectation of actual annual changes.
- (c) As at June each year.
- (d) Represents forecast 'Headline' CPI inflation, including factors affected by policy changes. The underlying increase in the CPI in 2000-01 is expected to be 2.5%. In addition, consumer prices are expected to increase by an additional 3.0% as a result of the GST. Since the incidence of the GST falls entirely on the final consumers of goods and services, prices facing producers of goods and services, including governments, will not increase by this additional 3.0%.

ACT Current Economic Conditions

Economic Growth

During 1998-99, there was an increase in real Gross State Product (GSP) of 2.6%. State Final Demand (SFD) also grew strongly during 1998-99, at an average of 4.5%. This is higher than in 1997-98, and indications available at this time are that the growth rate has accelerated further in the first half of 1999-2000.

Employment

Original series data from the ABS show that total employment in the ACT during the first ten months of 1999-2000 was 5.0% above the average level in 1998-99. The average unemployment rate for the first ten months of 1999-2000 was 5.6%, compared with an average of 6.4% during 1998-99.

Population

Net interstate migration out of Canberra will continue to steadily diminish over the next few years, as more confidence in the economy and labour market encourages more people to move to Canberra, and fewer to leave. In the medium term, this will return Canberra to higher rates

of population increase, although still lower than the national average. After an increase of 0.7% in 1998-99, the ACT population is expected to increase by 0.7% in 1999-2000 and 2000-01, compared with national growth of 1.0%.

Business Conditions

Business conditions in the ACT are extremely buoyant. The national conditions of low inflation and low interest rates are supplemented in the ACT by the lowest unemployment rate in nearly a decade, and the government's focus on constraining expenditure to ensure that Canberrans are not paying more than necessary for services.

The continuing positive mood in business is reflected in surveys of business confidence such as the ACT and Region Chamber of Commerce and Industry business expectations survey for the March quarter 2000. This survey revealed that more than three-quarters of Canberra businesses believe that the local economy will remain strong until at least the middle of the year 2000. The survey also indicated that 100% of exporters expect sales to improve or at least remain the same.

The ANZ Job Advertisements Series shows that the average trend weekly number of job ads for the first ten months of 1999-2000 is 23.3% higher than in 1998-99. In April 2000, the trend series was at its highest level, at an average of 562 job ads per week, since the ANZ began recording a Job Advertisements series for the ACT.

The Yellow Pages Small Business Index released in February 2000 found that a net 54% of ACT small business proprietors are confident about their business prospects for the coming 12 months. Following last year's high of 66%, the Index continues to perform well above the Australian average.

Economic Strategy

While the public sector remains a source of strength for the ACT economy, the diversification of the economy away from this sector is making the economy less vulnerable to changes in Commonwealth budget policies. With this in mind, the Government is still focussing on creating an environment that will encourage investment by both businesses and the household sector. This is being achieved through the dual strategy of ensuring that the economic fundamentals are conducive to greater private sector investment on a sustainable basis, and where appropriate, providing incentives targeted at the relocation and expansion of private sector firms.

The Government's economic strategy focuses on five key elements:

Diversification of the Economic Base

The impact of significant cutbacks within the Australian Public Service in 1996-97 underlined the need to stimulate private sector employment opportunities and reduce the dependency of

the ACT economy on the Commonwealth. Key strategies have included actively working with major outsourcing companies to ensure outsourced jobs stay in Canberra and targeting industry sectors with strong growth potential, including information and advanced technology, corporate services and light manufacturing.

The ACT as a Regional Economic Centre

The ACT's geographical location, its importance as a regional economic centre and its proximity to Sydney all underline the need to maintain a competitive taxation system that does not create disincentives to invest or create jobs in the ACT. By keeping taxes in line with, or slightly below those that apply in surrounding New South Wales the Government will help to maintain the competitiveness of ACT business.

Sound Financial Management and Service Delivery

Moving the ACT Budget from an operating loss to a sustainable operating surplus requires the maintenance of revenue raising efforts, subject to the competitiveness issues outlined above. Sound financial management also requires that the Government constantly seek more efficient and effective methods of service delivery.

The intention has been to shift the focus to results achieved and away from the traditional public service focus on resources consumed. The result is a clear separation in government of the purchaser role, the owner role and the provider role. These reforms enable the Government to specify the quantity, quality and timeliness of services and to identify opportunities for improved technical efficiency.

The Government's financial management performance is reflected in the recent reaffirmation of the ACT's AAA credit rating, the highest achievable.

Creation of a Sound Business Environment

The Government is developing a business environment that positively encourages the operation of existing businesses and is attractive to potential new businesses. Government processes that adversely affect the performance of ACT businesses continue to be identified and either streamlined or removed. Proposals for new regulations are subject to Regulatory Needs Analyses, which seek to ensure that where regulations are adopted they are necessary, there are no better alternatives and that the regulatory cost burden is minimised. This aims to ensure that the level of red tape imposed upon Canberra businesses remains minimal.

Proposals for new regulations are also examined to ensure that they would not constrain competition in markets and breach the Government's obligations under the National Competition Policy Agreement.

Microeconomic Reform and National Competition Policy

The 1995 national competition policy agreements entered into by all Australian governments included a suite of reforms that have been pursued by the Council of Australian Governments (COAG) in electricity, gas, water and road transport.

Each party is required to publish an annual report of its progress in achieving the reforms, for assessment by the National Competition Council (NCC). In all aspects of reform the ACT has been assessed as meeting its commitments in the agreements, and hence has received all the tranche payments. In 1999-2000 and 2000-01 the estimated payment is \$7.2m per year. The main issues for the ACT in this, the second tranche assessment, related to the implementation of a package of nationally agreed road reforms. Legislation in December 1999 has ensured that the agreed commitments have been met, with some further developments in regulatory information systems to take place over the next several years.

Over the past several years the ACT has been involved in the development and implementation of the national electricity market (NEM). The market has been in operation since December 1998. Customers consuming more than 160 MWh per annum are already contestable. From 1 January 2001, the last tranche of retail contestability will occur when customers below 160 MWh per annum will become contestable. This will be consistent with the extension of full retail contestability to the electricity supply market in New South Wales. The changes, anticipated to take effect from 1 January 2001, will apply to residential consumers who, while the largest proportion of the market in numbers, are the lowest consumers of total electricity supplied.

The ACT also continues to participate in the creation of a free and competitive market in gas. AGL is the monopoly supplier of gas in the ACT, subject to regulated prices determined by the Independent Competition and Regulatory Commission (ICRC). During 2000-01 it is expected that the ICRC will deliver its report on AGL's access to infrastructure arrangements. That report will further promote the development of a competitive market for gas in the ACT, as will progress on the construction of the East Coast gas pipeline. The new pipeline will link the ACT with potential supply from Gippsland and Bass Strait, bringing potential new competitors into the gas distribution and retail markets in the Territory and providing a degree of security in supply. Currently security is not assured because all supply enters the ACT through a single pipeline connecting with the distribution system at Watson.

A new package of legislation addressing the regulation of utilities in the ACT is expected to be resolved during the year, with benefits to consumers including more transparent licensing arrangements, independent administration of licence conditions and more effective safety net provisions. The processes will involve the administration of licensing by the independent regulator and separation of the technical regulatory and emergency service functions.

In 1999-2000 the Government agreed to a revised Guideline on Regulatory Reform, which will affect the assessment of regulatory risks for the first time in 2000-01. The revised arrangements will ensure that all regulatory risks are considered in the same document, rather

than in three separate statements, as was the case previously. The effect of regulatory proposals on business will have the same prominence under the new arrangements as under the arrangements recommended by the Red Tape Task Force in 1997. Regulatory Impact Statements will be required for all regulatory proposals and subjected to independent analysis, to ensure robust and comprehensive analysis, clear demonstration of net benefits to the community, and clear consideration of all effective alternatives.

To provide business and the community with certainty about the regulatory activity anticipated in the year, the Government has produced annually Agency Regulatory Plans since 1997. The Plans will be produced again in 2000-01 in late September or October. This year it is anticipated that the plans will include references to regulatory performance against the estimates included in the previous year, as well as projections about regulatory activity during the current year.

By the end of 2000 the ACT will have completed its scheduled reviews of legislation that restricts competition and, where appropriate, introduced or foreshadowed reforms. This activity, which has been pursued since 1996, builds upon the reductions in the regulatory burden commenced under the Red Tape Task Force reforms process and is a commitment in the national competition policy. In the second half of 2000 reviews into such areas as medical professions, the legal profession, land legislation and taxis will be completed. In addition, a new program of legislation reviews can be foreshadowed in the second half of the year, covering legislation that has been enacted since 1996.

There is continued need for monitoring compliance with the Trade Practices Act 1974. Since the passage of the Competition Policy Reform Act 1996, the Territory's businesses and business activities of government have been subject to the Trade Practices Act. Since that time a compliance education and awareness program has been operating in departments and agencies, including the preparation of agency guidelines for the management of trade practices risks. That process will receive continuing attention during 2000-01, with the potential to introduce a consistent training and awareness package across all agencies.

Throughout the year, the Government will continue to pursue microeconomic reforms at both the regional and national levels by maintaining its participation in a range of intergovernmental forums. The ACT has participated in these forums for a number of years in order to protect the progress made in the development of the ACT economy and to ensure that the advantages achieved from microeconomic reform are shared by the Territory equally with the other States and the NT.

ACTEW/AGL Partnership

Negotiations are underway to establish a joint venture partnership between ACTEW and AGL. The Legislative Assembly's agreement to the ACTEW/AGL Partnership Facilitation Act 2000 was gained on 9 March 2000. The Budget does not pre-empt the result of these negotiations, however the potential implications of the proposal are discussed below.

The Australian Competition and Consumer Commission (ACCC) considers that the growing contestability in the gas and electricity markets means that the proposal would not have an adverse affect on competition.

The ACCC also noted that the Utilities legislative reform package will provide enhanced consumer protection and was reassured by the role the Government will play in ensuring that ACT energy consumers are protected. This legislation establishes minimum quality standards including drinking water quality and energy supply performance standards and will prohibit arbitrary disconnection or unfair debt collection practices.

It is expected AGL may be required to make a valuation equalisation payment of at least \$100m. The equalisation payment would allow ACTEW and AGL to obtain equal shares in the partnership. However, the actual amount of the equalisation payment cannot be determined until the due diligence process has been finalised and there has been an independent review of the valuation assessment made by ACTEW and AGL. It is intended that the Government will invest the equalisation payment in the Territory's Superannuation Provision Account as part of its strategy to address the unfunded superannuation liability. This strategy is discussed further in chapter 5.2 Superannuation.

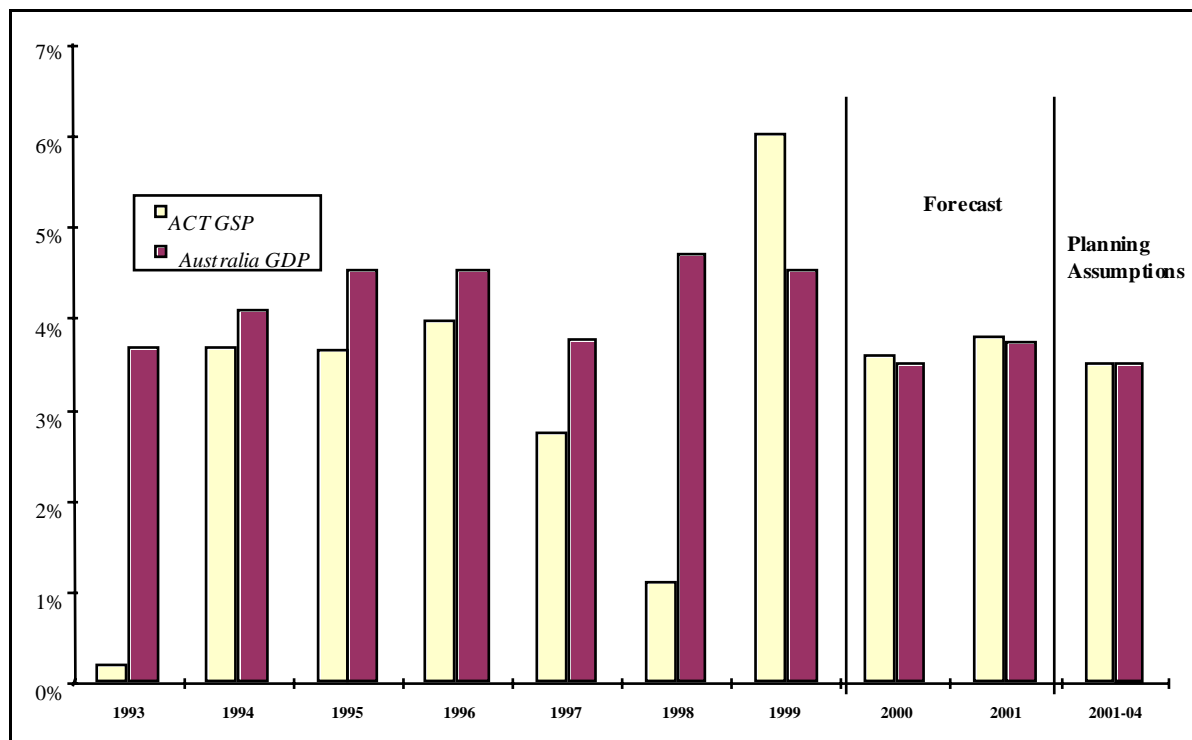
Economic Forecasts

Gross State Product (GSP)

GSP is the principal measure of aggregate economic performance at the State and Territory level. GSP estimates the total value of goods and services produced in the economy.

Economic growth in 1999-2000 is expected to remain high at around 3.6% and 3.8% in 2000-01. An average of 3.5% is expected from 2001-02 to 2003-04, as increasing population growth allows GSP growth to accelerate on the back of increasing employment growth. It is expected that the ACT will continue to experience relatively high levels of growth in GSP per capita.

Figure 6.1.1
Real Annual Change in GSP/GDP, ACT and Australia



Source: ABS Cat Nos 5220.0 & 5206.0 and DTI and Commonwealth Treasury forecasts.

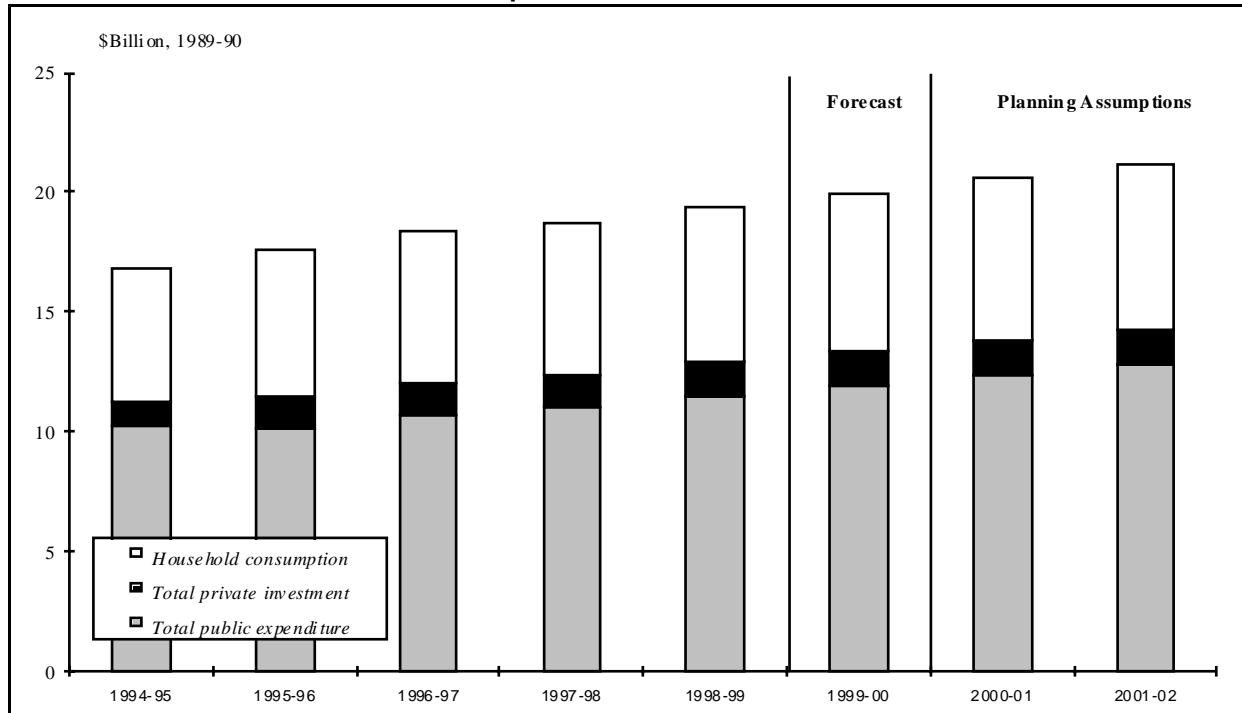
State Final Demand

The implementation of the GST is boosting growth in 1999-2000, as the Commonwealth spends money formulating policy and the private sector prepares for the new tax system. Such a high rate of growth cannot be sustained in the long term, and growth will moderate to 2.3% in 2000-01, from a higher base. The medium term outlook is for growth to accelerate to an average of 2.6% through the forward years.

Private consumption growth was 3.7% in 1998-99, coming off a boom year in 1999-2000. With their higher incomes, Canberrans will tend to enjoy the income tax cuts associated with tax reform more than the average Australian, and private consumption growth is expected to remain strong in the medium term, at 3.0% per annum. This tendency will be boosted as the growing private sector seeks export opportunities, earning more money which flows through to consumption.

Private investment decreased by 0.2% in 1998-99, as purchases of buildings from the Commonwealth decreased. This has been followed by a boom in 1999-2000 as business equips itself for export opportunities and the new tax regime, with investment expected to grow by 18%. This will moderate in 2000-01, growing at 0.4% off a high base. The medium term outlook is for strong growth of 4.4%, as construction improves and the burgeoning private sector prepares to take advantage of opportunities by investing in equipment and intangibles such as IT.

Figure 6.1.2
Components of ACT SFD



Source: ABS Cat Nos 5206.S, Table 28 and DTI forecasts.

Indicative predictions of the components of ACT SFD are summarised below.

Table 6.1.2
Indicative Predictions of the Components of ACT SFD

	1998-99 (Actual)	1999-2000 (Forecast)	2000-01 (Forecast)	3 Year Planning Assumptions 2001-02 – 2003-04 (Average annual growth) ^(b)
	Percentage change on the previous year ^(a)			
Private Consumption	3.7	3.0	3.0	3.0
Private Investment:	-0.2	18.0	0.4	4.4
Dwellings	13.8	20.0	-3.0	4.0
Other buildings and structures	-7.6	-6.0	-5.0	0.0
Machinery and equipment	-23.5	2.8	1.5	3.1
Intangible fixed assets	32.2	30.0	7.0	8.5
Ownership transfer costs	8.5	15.0	3.5	4.0
Total Public Expenditure:	5.5	4.7	2.1	2.1
Public Fixed Capital	110.6	-2.0	3.5	3.5
Public Consumption	4.0	5.0	2.0	2.0
Total State Final Demand	4.5	5.0	2.3	2.6

Source: ABS Cat Nos 5206.S, Table 28 and DTI forecasts

(a) Based on original data, with financial data expressed in real terms. Percentage changes are expressed in year average or year total terms (4 quarters of one year to the previous year) unless otherwise indicated.

(b) The planning assumptions used in this document represent the estimated average annual change for the period 2001-02 to 2003-04. As such they do not represent expectation of actual annual changes.

Private Investment

This section discusses expected changes in private sector investment in the ACT, one of the major drivers of long term growth in the economy.

Dwellings

The trend number of residential building approvals rose by 13.8% during 1998-99 after a 7.5% reduction in the previous financial year. This trend has strengthened significantly during the first eight months of 1999-2000, with the number of residential approvals 41.9% higher than during the first eight months of 1998-99, in anticipation of an increase in the cost of construction after the GST is introduced. Residential investment is expected to increase by 20% in 1999-2000. The bringing forward of construction into 1999-2000 will result in a brief decline, estimated at around 3.0%, in 2000-01. This is a common pattern expected throughout Australia. The forward years will see an improvement as population growth accelerates, with growth expected to average 4.0%.

Other Buildings and Structures

Private capital expenditure on other buildings and structures decreased 7.6% in real terms in 1998-99. This is mainly a result of a reduction in Commonwealth asset sales. After a further gradual decline in 1999-2000 this is expected to stabilise and resume growing in the medium term.

However, it is difficult to forecast accurately the non-residential sector in the ACT, given its particularly uneven nature and the significant impact that individual projects can have.

Proposed and continuing projects include:

- BRL Hardy winery development;
- TransACT fibre-optic network;
- National Museum;
- Mitchell Resource Recovery and Waste Transfer Station;
- Canberra Centre extensions, Civic;
- Section 56 redevelopment, Civic;
- MacPherson Court redevelopment;
- School of Music extensions, ANU;
- Section 41 carpark redevelopment at Manuka to include a supermarket, shops, offices, underground car parking, health facilities and residential apartments; and
- ACT Prison, Symonston.

Machinery and Equipment

Investment in machinery and equipment fell in 1998-99 by 23.4%, but is bouncing back in 1999-2000 with growth of 30.0% expected. Continuing high levels of business confidence and the development of export markets will see this level of investment sustained into 2000-01, with average growth through the forward years of 4.0% per annum as business starts to see the benefits of the reformed taxation system.

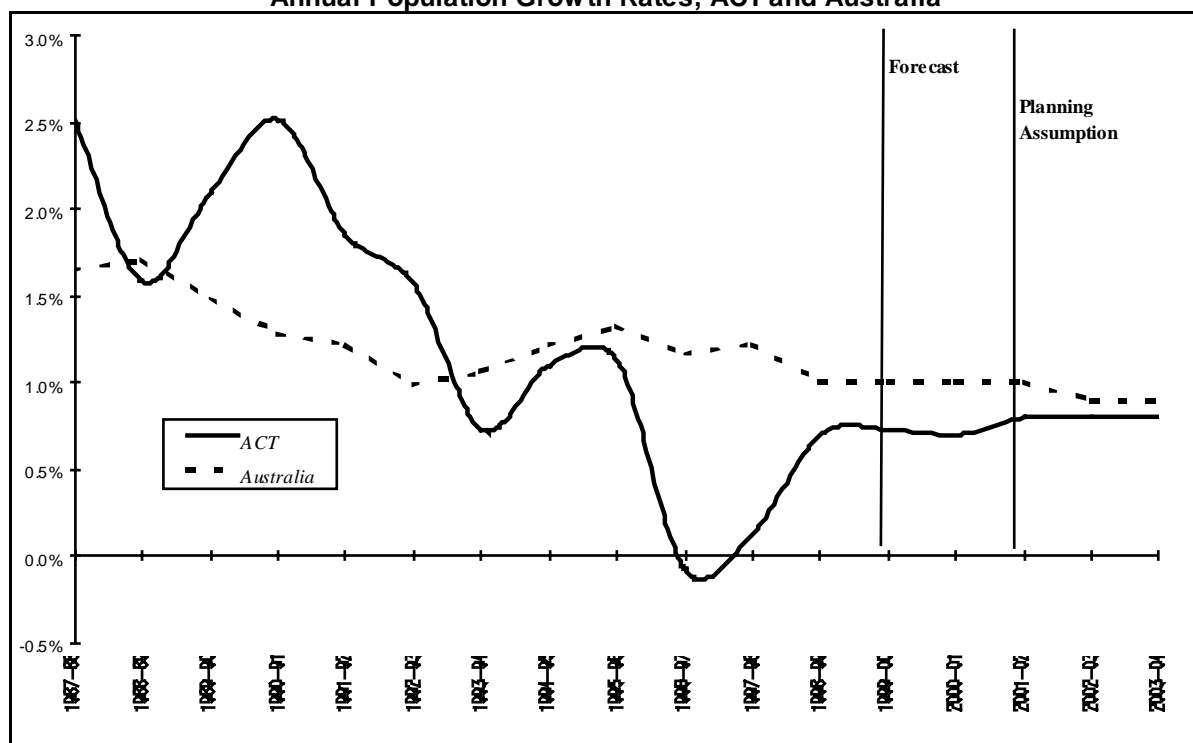
Intangible Fixed Assets

Following Y2K remediation work and investment required to make systems GST compliant during 1999-2000, 2000-01 will see a relative slowdown in investment in intangible fixed assets such as software. In the medium term this will continue to increase steadily, reinforced by the expansion of high technology information businesses in the Territory.

Population

In June 1999, the ACT's population represented 1.64% of the total national population. In the past decade the Territory's population has increased by 11.9%, from 276,432 in June 1989 to 310,570 in June 1999. This compares with a national increase of 12.0% over the same period. The ACT's population is expected to increase to 312,844 by June 2000. The population growth rate is forecast to increase slightly in the forward years to an average of 0.8%, compared with the national growth of 0.9%.

Figure 6.1.3
Annual Population Growth Rates, ACT and Australia



Source: ABS Cat No 3201.0, Tables 3H and 3I and Demography ACT & Commonwealth Treasury forecasts.

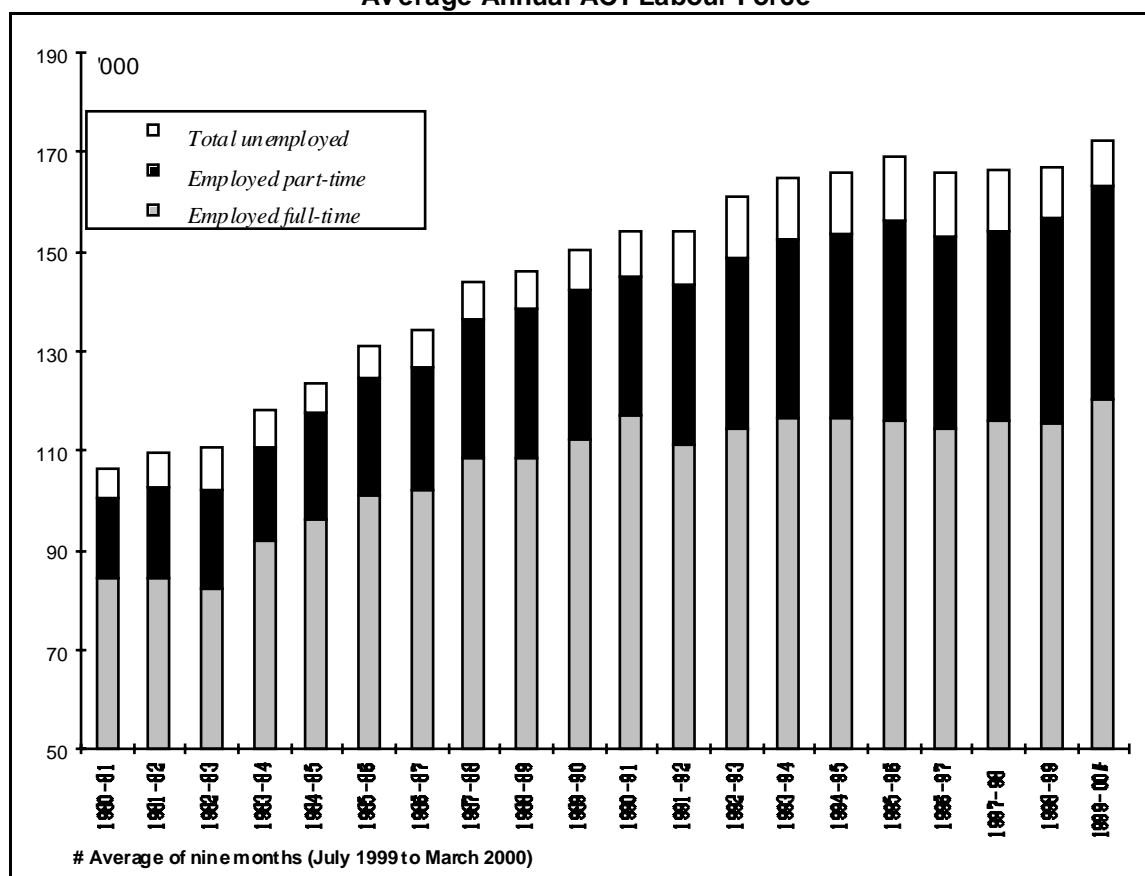
As a result of the increasing employment opportunities in Canberra, the flow of migration out of the Territory is expected to reverse in the medium term. In the meantime, Canberra's population growth is being maintained by natural increase, although this is gradually slowing. The Government will continue to diversify and develop the economy so that net interstate migration contributes to, rather than reduces, the rate of population growth in the ACT.

Labour Market

Labour Force

The Territory's labour force increased by 0.4% in 1998-99, following an increase of 0.7% in 1997-98. During the first nine months of 1999-2000 the labour force increased by 3.25%. This indicates that the local economy is performing very well. The ACT labour force participation rate declined slightly from 71.4% in 1997-98 to 71.2% in 1998-99, but has picked up further for the first nine months of 1999-2000, averaging 72.7%. This remains significantly above the national rate of 63.3%.

Figure 6.1.4
Average Annual ACT Labour Force



Source: ABS Cat No 6202.0, Tables 8H.

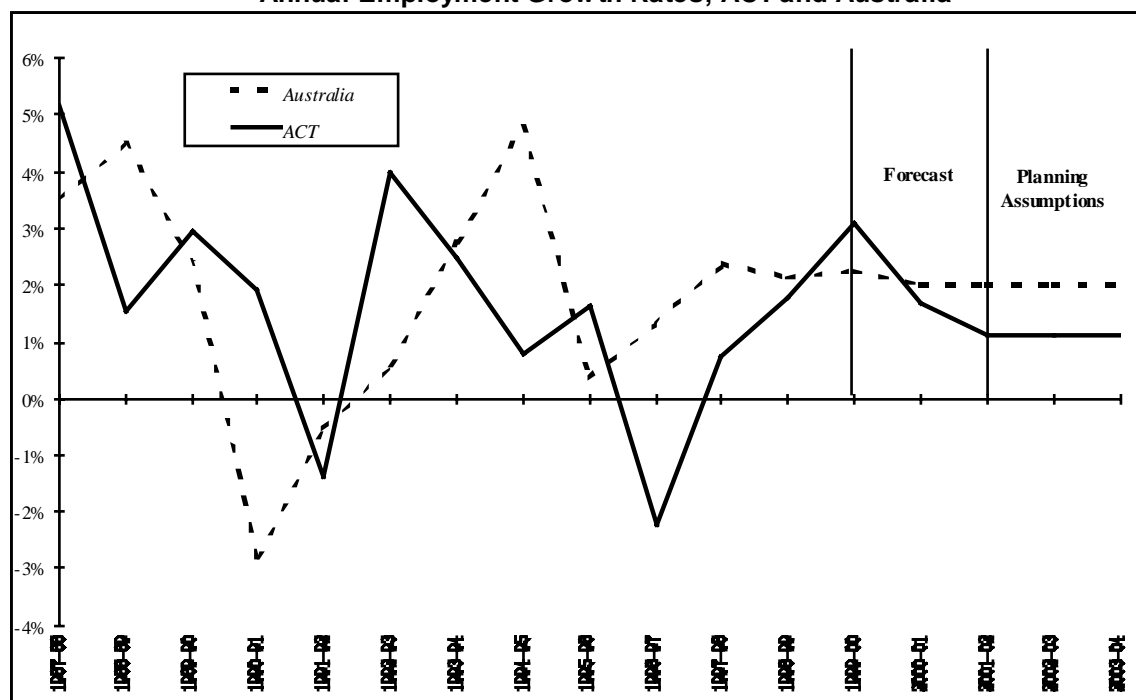
The participation rate is expected to increase even further in 1999-2000 and future years, as the low unemployment rate and increasing employment opportunities result in the return of people who had previously left the labour market.

Figure 6.1.4 shows the size of the Territory's annual average labour force for the period 1980-81 to 1999-2000.

Employment Growth

ACT employment is forecast to increase by 3.1% in 1999-2000, following an increase of 1.7% in 1998-99. This period of significant employment growth and low unemployment is expected to continue during 2000-01 but not at the same rate. With the Territory's unemployment rate already low, those workers who have become discouraged over the past couple of years will have a greater opportunity to re-enter the labour force, hence increasing the participation rate. This will allow employment growth to exceed population growth over the forward years, although the strong economy and excellent employment prospects will contribute to a steadily increasing rate of population growth (see figure 6.1.5).

Figure 6.1.5
Annual Employment Growth Rates, ACT and Australia



Source: ABS Cat No LF-Emp-Aust-Mthly, Table 8I and 9I, and DTI, Commonwealth Treasury and Econtech (2002-03) forecasts.

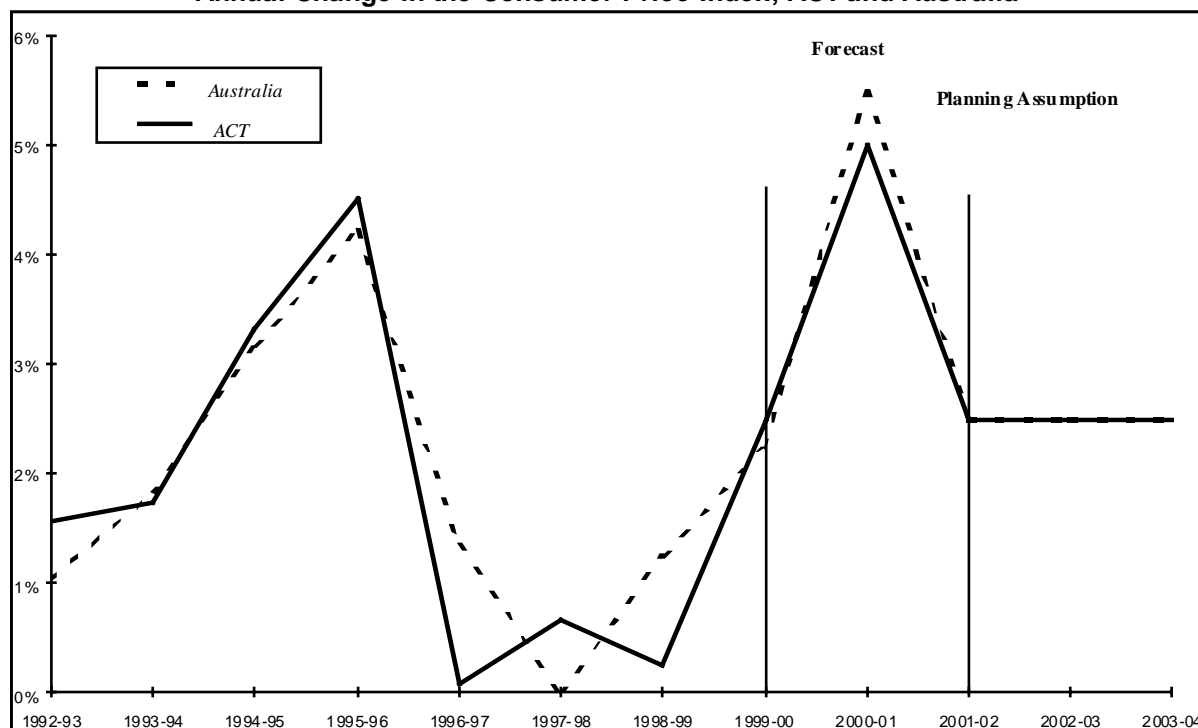
Prices

In line with the national trend, the ACT has experienced minimal inflation during the past two years. Consumer prices rose by only 0.2% during 1998-99 after falling by an average of 0.7% in the previous year. However for the first nine months of 1999-2000 the inflation rate has picked up, with the CPI increasing, on average, by around 2.8% higher than at the end of 1998-99. For the same period for the previous year the increase in prices was only 0.2%.

The ACT CPI forecast for 1999-2000 is 2.5%. This rate of annual price increase is expected to continue throughout the forward years. However, the ACT CPI for 2000-01 is expected to

be 5.5%, based on an underlying inflation rate of 2.5% and 3.0% for the impact of the GST. This additional 3.0% increase will occur only in relation to prices faced by the final consumers of goods and services. It will not affect the prices faced by the producers of these goods and services, or governments, because the GST is designed so that the full impact of the tax falls on final consumers. Consumers will be compensated for the price increase through income tax cuts, and producers and governments will not need additional compensation as they will not experience the additional 3.0% price increase resulting from the GST.

Figure 6.1.6
Annual Change in the Consumer Price Index, ACT and Australia

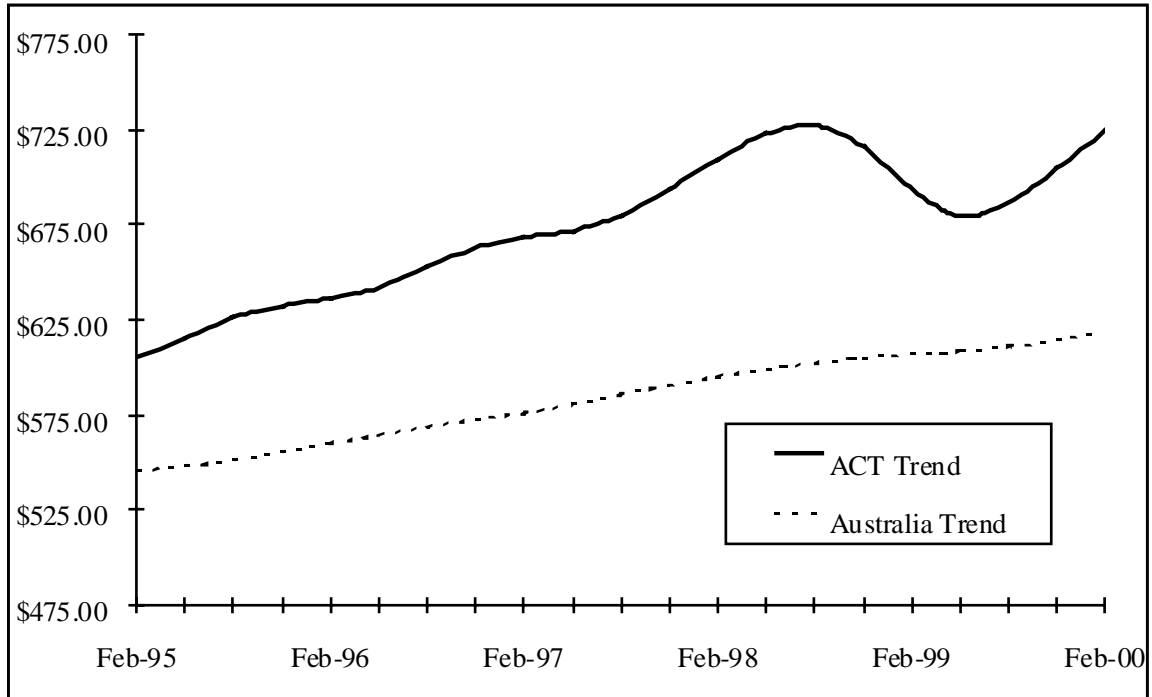


Source: ABS Cat No 6401.0, Table 1A and DTI and Commonwealth Treasury forecasts.

Wages

Together with changes in employment, changes in average weekly earnings (AWE) affect the levels of aggregate demand and economic activity. The ACT's AWE, during 1998-99, declined on average by 5.0% compared with 1997-98 levels. During the February quarter 2000 AWE increased by 2.9% from the previous quarter and increased by 4.5% from the same quarter in the previous year.

Figure 6.1.7
Annual Change in Average Weekly Earnings, ACT and Australia



Source: ABS Cat No 6302.0, Table 1 and 11H.

