

26th October 2015



ACT Economic Outlook

Summary

- Economic growth in the ACT has picked up in recent quarters. State final demand in the ACT grew at 5.4% in the year to June 2015 up from 1.2% in the year to December 2014. The full set of Gross State Product figures for 2014-15 will become available in November.
- Government activity will continue to play a large role in the ACT. Over time the need for a larger public service will rise as Australia's population continues to grow. While the ACT will not see all the increases in public sector employment, it remains at the heart of policy development and power. In the short term, budgetary pressures seem likely to cap rapid growth in public sector job numbers.
- Canberra dwelling prices have recovered from a dip towards the end of 2014 but the subsequent rise has been modest. House prices in Canberra have performed relatively better than units. House prices were up 1.1% in the year to September while unit prices have fallen 6.2%.
- Canberra house prices are likely to continue to trend sideways or modestly higher as they have done over the past few years. Low interest rates will provide support, but there are factors which are weighing on demand.
- After a period of good growth in retail spending from February to June, consumer spending in the ACT weakened in July and August. Over the year to August 2015 retail sales rose 4.0%. This was above the 10 year average of 3.8% but below the national pace of 4.5%.
- The Budget, released in June, expects a deficit of \$407.6 million for 2015-16 and a deficit of \$116.1 million in 2016-17. The Budget is estimated to return to surplus in 2018-19. Apart from the Asbestos Eradication Scheme, changes to Federal funding have added \$143.5 million to the 2015-16 ACT budget deficit.
- Private business capital expenditure, which includes spending on plant & equipment and buildings & structures, rose in the June quarter 2015 to its highest level since March 2013.
- The \$783 million Capital Metro project, if it proceeds as planned, would provide a considerable boost to construction work in the ACT.

Economic Growth

Economic growth in the ACT has picked up in recent quarters. State final demand in the ACT grew at 5.4% in the year to June 2015 up from 1.2% in the year to December 2014. The full set of Gross State Product figures for 2014-15 will become available in November.

The increase in State final demand appears to be a result of ongoing construction activity and reasonable growth in retail spending (see below for further detail).

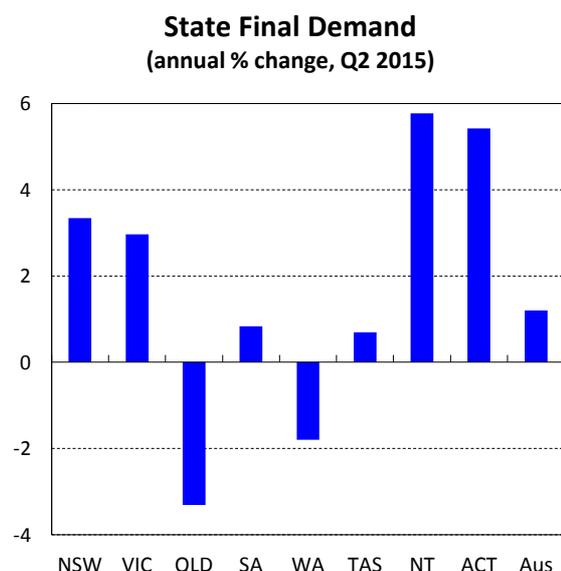
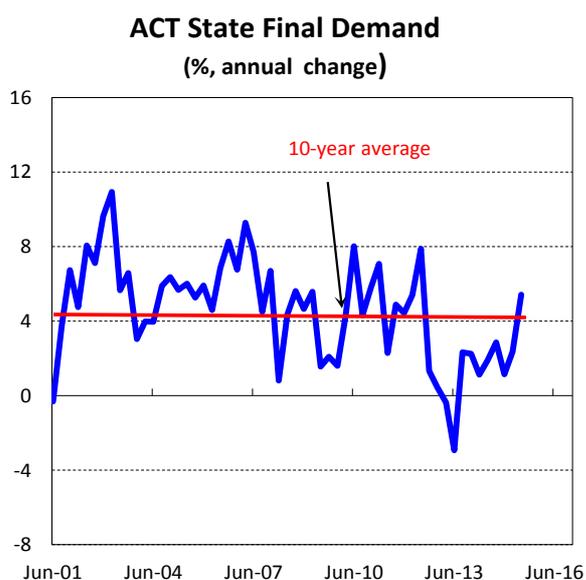
Where will future growth come from?

Population growth is set to continue, albeit at a slightly slower pace than in earlier years. Within the next 10 years the population of the ACT is expected to grow towards 500,000, up from the current 388,000. This will require new infrastructure and new housing both of which will create new jobs and new incomes. Capital Metro, if it proceeds, has the potential to create jobs and stimulate activity along its proposed corridor.

The lower AUD is expected to lead to increased activity in overseas visitors, domestic tourism and international education. Canberra's arts and cultural activities are expected to continue looking for opportunities to attract visitors to the region.

Low interest rates support economic activity and investment. Further investment in housing seems likely from Sydney and Melbourne as well as from overseas as interest rates and the currency remain low by past standards.

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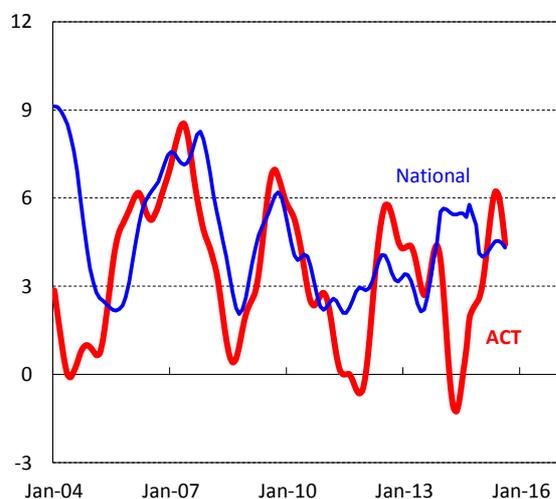


Percentage Shares of the Economy*		
Industries	ACT	Australia
Public administration and safety	34.5	6.3
Construction	11.3	9.4
Professional, scientific and technical services	10.0	7.3
Education and training	7.9	5.4
Health care and social assistance	6.9	7.6
Financial and insurance services	4.0	9.9
Electricity, gas, water and waste services	3.3	3.1
Accommodation and food services	3.2	2.8
Retail trade	3.2	5.3
Rental, hiring and real estate services	2.9	3.3
Transport, postal and warehousing	2.8	5.3
Information media and telecommunications	2.2	3.3
Other services	1.9	2.1
Administrative and support services	1.7	3.3
Arts and recreation services	1.7	0.9
Wholesale trade	1.3	4.6
Manufacturing	1.2	7.4
Mining	0.1	9.9
Agriculture, forestry and fishing	0.1	2.7

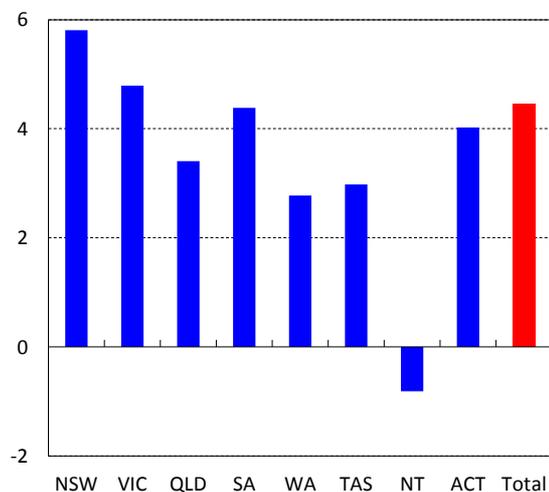
* As % of GSP and GDP less ownership of dwellings 2013-14

Source: ABS, St.George

Value of Retail Sales
(trend, annual % change)



Retail Sales by State
(August 2015, annual % change)



Consumer Spending

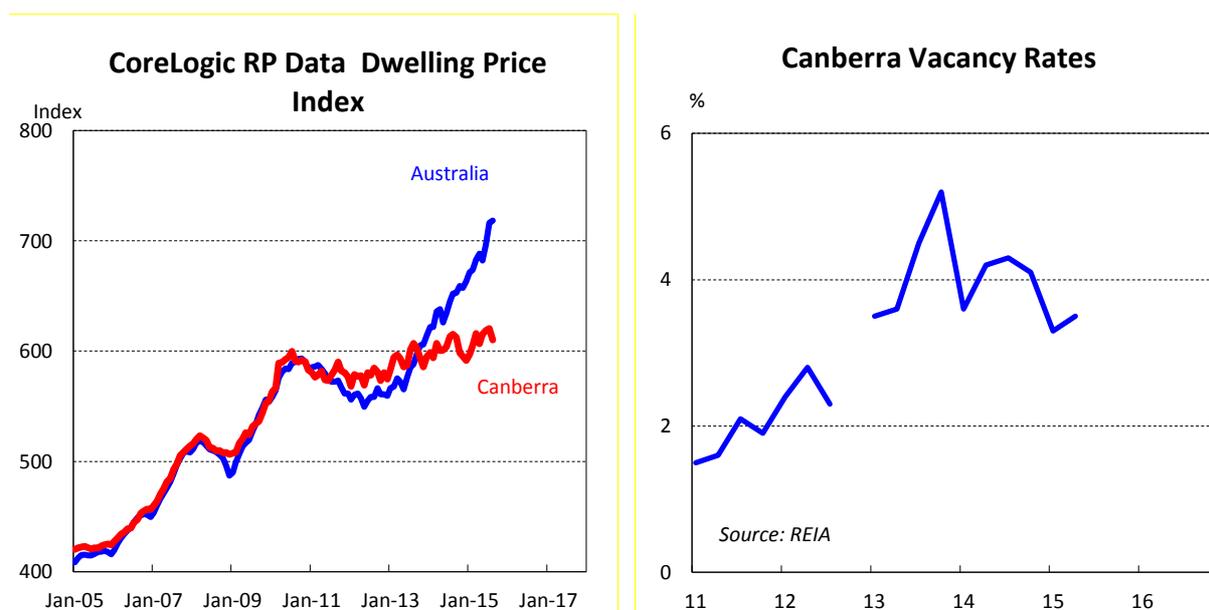
After a period of good growth from February to June, retail spending in the ACT weakened in July and August. Over the year to August 2015 retail sales rose 4.0%. This was above the 10 year average of 3.8% but below the national pace of 4.5%.

Sectors that have experienced solid growth over the past year, in trend terms, include furniture, floor coverings, housewares and textile goods (12.7%) and footwear and other personal accessories (16.1%). Takeaway food services (20.0%) had a very strong year and the newspaper and books sector (32.0%) has seen better growth after several relatively poor years.

On the other side of the retail sales ledger, liquor (-9.4%) and pharmaceutical, cosmetic and toiletry goods (-20.8%) retailing have seen a slump in sales over the year. Sales of specialty foods (-4.2%) and electrical and electronics goods (-0.6%) were also weak.

Can we look forward to a pick-up in sales over the year ahead? Retail spending is closely linked to job security, growth in wages, increases in employment, growth in the population and housing activity. While growth in wages and the population are expected to remain modest, job security appears to have improved and consumer sentiment has lifted. Provided the next Federal Budget is neutral or even positive, in terms of public service employment, retail sales should improve or at least maintain their current pace of growth.

The Westpac-MI index of consumer sentiment does not have a separate measure for the ACT, however, national consumer sentiment has picked up from a low of 92.3 in July 2015 to 97.8 in October. That said, result below 100 indicated that there are more pessimists than optimists among consumers.



Housing

Canberra dwelling prices have recovered from a dip in prices towards the end of 2014 but the subsequent rise has been modest. CoreLogic RP Data dwelling prices for September were 0.6% higher than a year earlier. Canberra dwelling prices have continued to underperform capital city prices Australia-wide. By comparison, the average of Australian capital cities grew at an annual pace of 11.0% in September, largely driven by prices in Sydney and Melbourne.

Prices of houses in Canberra have performed relatively better than units. House prices were up 1.1% in the year to September while unit prices have fallen 6.2%.

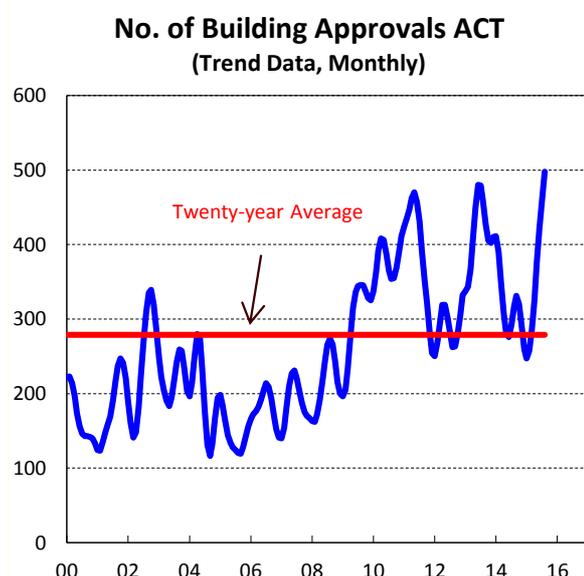
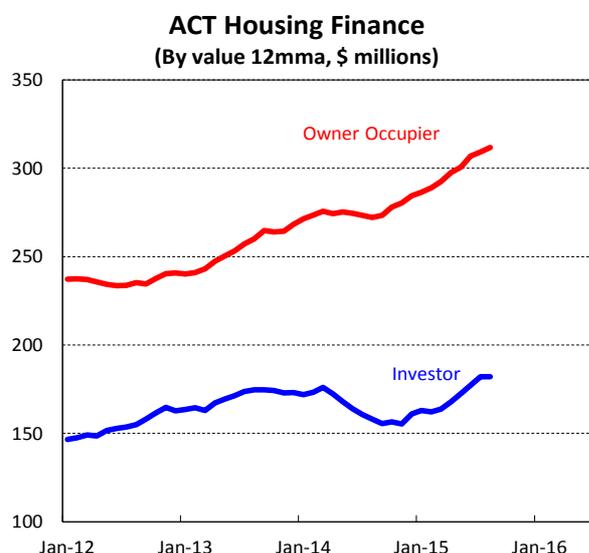
The growth in house prices appears to be a mixture of factors. On the upside, the downward pressure on public sector jobs appears to have abated with some new hiring being reported. The relocation of people affected by the 'Mr. Fluffy' also appears to be adding upward pressure in parts of the Canberra market.

On the downside, a slowdown in population growth in the ACT could well be keeping a lid on the growth in house prices. After annual population growth of 2.0% in in September 2012, the pace of growth slowed to 1.1% December 2014 before picking up marginally to 1.3% in March 2015.

The pace of population growth has fallen from around 7000 per year in late 2012 to around 4800 in the year to March 2015. Of the growth in the year to March 2015, there was a natural increase (births less deaths) of 3600, overseas migration added 2300 while interstate migration saw 1000 people leave the ACT. A resumption of growth in the public service labour market could see a reversal in the interstate migration figures which might then add to demand for housing.

We expect house prices in the ACT to continue to trend sideways or modestly higher as they have done over the past few years. Low interest rates will provide support as will growth in the population and a stabilization of employment in the public sector.

The decline in unit prices likely reflects a mix of increased supply and softer demand following previous public sector job cuts.



A period of historically high residential building activity over the past five years has raised concerns about oversupply, particularly at a time when demand appears to be softer than in previous years. However, changes in vacancy rates suggest these concerns could ease.

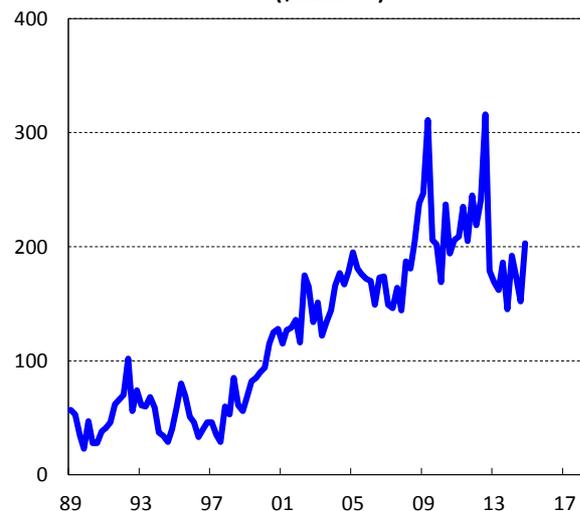
Vacancy rates in the ACT stood at 5.2% in the December quarter 2013. By the December quarter of 2014 they had fallen to 4.1% and as at the June quarter 2015 stood at 3.5%. This is still indicative of excess supply in rental accommodation and higher than Sydney (2.1%) and Melbourne (2.9%) but lower than Perth (4.7%) and Darwin (6.9%). Since March 2011, the vacancy rate in the ACT has averaged 3.2%.

Changes in rents and vacancy rates in the ACT paint a mixed picture. Median rents for three bedroom houses in Canberra were lower in 2014-15 (\$432pw) than they were in 2013-14 (\$443pw). A similar picture emerges for two bedroom units with rents down 4.3% in 2014-15.

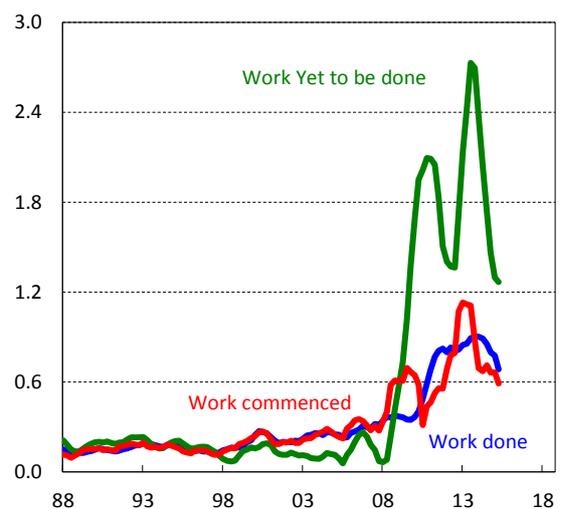
Modestly higher prices and slightly lower rents appear to have diminished investor appetite for Canberra property. As the earlier charts shows, there has been a slight decline in investor housing finance in recent months. However, a word of caution is appropriate here. As noted by the RBA, there has been some reclassification of loans from investor loans to owner occupier loans.

Following a soft patch in late 2015, building approvals have picked up throughout 2015 and now stand at a record level. Approvals in trend terms were almost 500 for the month while the twenty year average is 279 per month. This level of approvals suggests the ACT will continue to see high levels of building activity in the coming months. Over time the reconstruction of around 1000 'Mr Fluffy/asbestos' affected homes will also support the residential construction sector.

ACT Total Capital Expenditure
(\$millions)



ACT Engineering Construction
(4qtr sum, \$bn)



Business Investment

Private business capital expenditure, which includes spending on plant & equipment and buildings & structures, rose in the June quarter 2015 to its highest level since March 2013. The

ABS reports a total of \$203 million in capital expenditure in the June quarter, a lift of 40.0% on a year earlier. As the chart above illustrates, this is well down the capital expenditure that occurred from 2009 to 2012 but is the highest in over two years.

Engineering construction activity in the ACT took a turn for the worse during the June quarter 2015. Following a promising upturn in the March quarter, engineering construction work done fell 30.5% in the June quarter to be down 38.3% on a year earlier. The \$288 million Majura Parkway project remains under construction with a completion date of mid-2016. The \$783 million Capital Metro project, if it proceeds as planned, would provide a considerable boost to construction work in the ACT.

Commercial construction continues to centre on the \$600 million Australian National University's business and research precinct, the University of Canberra Public Hospital and a new CIT Campus in Tuggeranong. Work is now complete on the ADFA refurbishment, the Manuka Oval redevelopment, the Vibe Airport Hotel and the IKEA facility at Majura.

Labour Market

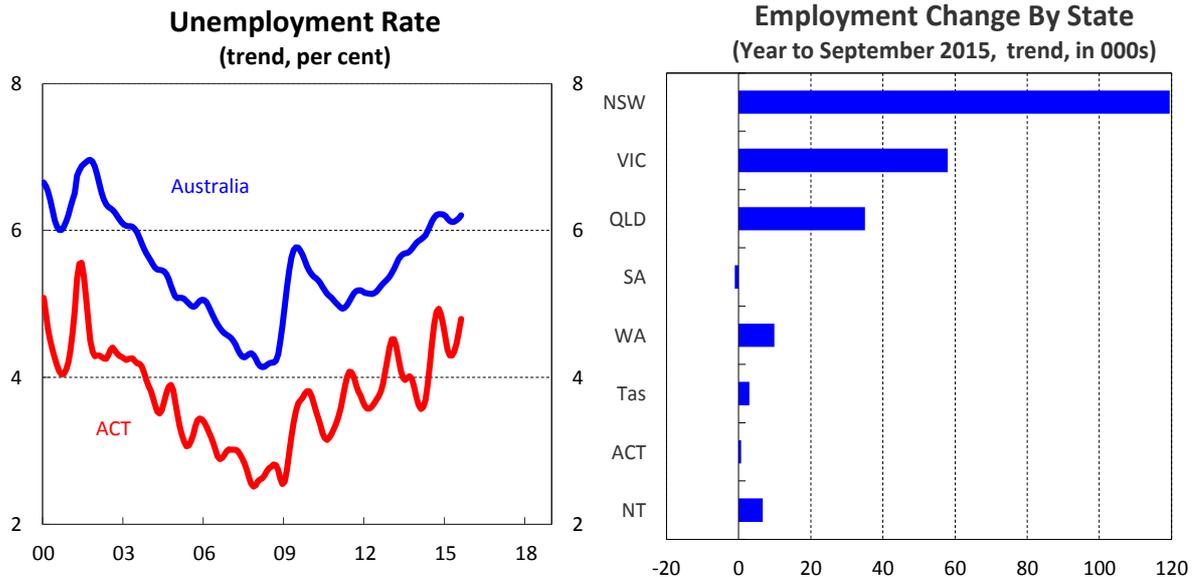
The ACT labour market has picked up marginally, in trend terms, over the past year. In seven of the past twelve months, employment has risen and in the year to September, the ACT created 700 jobs. While this may not appear impressive, it follows 15 consecutive months in which the annual rate of job growth declined. It appears that the worst of labour shedding in Canberra is now behind us.

From a peak 211.8k jobs in the ACT, in September 2012, the number of jobs, in trend terms, fell to 207.8k in November 2014. However, by September 2015 the number of jobs had risen back to 209.2k. The decline from 2012 until 2014 reflected the decision by the government of the day to make significant cuts to employment levels in the Commonwealth public service.

Statistics on employment by industry are only available on a quarterly basis, with figures for August 2015 the latest available. These show that in the year to August, job gains of 2.5k were made in education and training; 3.0k were created in construction and a further 3.3k were created in public administration and safety. On the other side of the ledger, 6.2k job losses occurred among professional and scientific services, 1.9k in the retail sector and 5.6k in healthcare and social assistance.

With only modest job gains over the year to September, the unemployment rate, in trend terms, is a touch higher than same month a year earlier. In September 2014 the unemployment rate in the ACT stood at 4.9%. In September 2015 it was 5.1% - which is still well below the national average of 6.2%.

The outlook for job growth in the ACT is modest. Ongoing 'productivity dividends' in the public service will make rapid jobs growth difficult as will moves to get the Federal Budget back to surplus. However, the lower AUD should provide support for the accommodation and tourism sectors and for the international education sector. A moderation in population growth should also assist in keeping the unemployment rate in check.



The 2015-16 ACT Budget

The ACT Budget was handed down in June. As noted in the previous ACT Economic Outlook, costs associated with the Asbestos Eradication Scheme have lifted the 2014-15 budget deficit and the estimates for 2015-16. A deficit of \$332.8 million was expected in the 2014-15 Budget. This was lifted to \$770.5 million at the December review. The final outcome for 2014-15 was a deficit of \$597.4 million.

The latest Budget expects a deficit of \$407.6 million for 2015-16 and a deficit of \$116.1 million in 2016-17. The Budget is estimated to return to surplus in 2018-19.

Apart from the Asbestos Eradication Scheme, changes to Federal funding have added \$143.5 million to the 2015-16 ACT budget deficit.

Major new initiatives were missing from the Budget but spending on capital works in the infrastructure, health and education sectors should assist in underpinning economic activity.

The net debt of the ACT government for 2014-15 was estimated at 3.7% of Gross State Product. This is estimated to rise to 6.4% in 2015-16 and peak at 7.5% in 2017-18.

St. George Banking Group Forecasts

The weaker AUD and low interest rates are supporting economic activity in the ACT. Population growth has moderated but remains positive. A major challenge facing the ACT is the pipeline of construction and engineering work. Apart from the creation of new infrastructure, the construction sector provides jobs and incomes to support consumer demand. Positive but sub-trend growth is expected for the ACT economy over the next two years.

The ACT Government is expecting marginally stronger Gross State Product (GSP) growth than

our forecasts. They expect growth of 1.5% in 2015-16 and 2.5% in 2016-17. The ten year average of ACT's GSP growth is 2.8%.

St George Banking Group Forecasts:

Economic Indicators, % Change (year average)				
	2013-14	2014-15 (e)	2015-16 (f)	2016-17 (f)
Gross State Product	0.70	1.10	1.10	2.10
State final demand	1.90	1.50	1.90	2.50
Employment	-0.20	-0.80	0.20	1.00
Unemployment rate (year average)	3.80	4.60	4.70	4.60
Canberra CPI	2.20	1.20	2.20	2.50
Wage Price Index	2.40	2.00	2.30	2.90

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