WA Economic Outlook
Time to steepen the economic curve

May 2020
WA appears to have successfully mitigated the immediate health impacts of COVID-19. Now attention must turn to the State’s economic recovery.

Containing the spread of COVID-19 in Western Australia is a remarkable achievement. At the time of writing, only 1% of cases were still active, with new cases reported on just four days over the last four weeks.

Notwithstanding the potential for a ‘second wave’ of cases as venues reopen and people cautiously return to work, the likelihood of a catastrophic number of cases overwhelming our health system has been diminished greatly. But there’s no room for complacency on the health front, which means for the time being, certain economic restrictions will be unavoidable.

The extent of the economic damage wrought by COVID-19 is difficult to compare to anything most of us have experienced before. The immediate effect on headline economic indicators is more akin to the Second World War than of any financial crisis or recession in recent decades.

Certain parts of the economy will bounce back quickly. Some will recover slowly, and others perhaps not at all. The virus has wiped out several years’ worth of job gains and industry growth in WA. The labour market impacts, and the consequences for household income and confidence, are particularly devastating.

Overall, we expect the State’s economic recovery to be slow. Consumer confidence has been shattered. Investment appetite among business will be diminished for some time. The conventional monetary policy arsenal – usually deployed early and with great effect in an economic crisis – is empty. Fiscal stimulus has helped soften the blow and will need to continue.

But the crisis has also thrown up opportunities, and now is the time to seize them. Many employees and businesses have been forced to change the way they work, adopting technology required to work remotely or deliver services to customers digitally. Many health experts suggest the new normal is more likely to be ‘living with COVID’ rather than returning to a world without COVID, meaning these innovations and improvements should be locked in for the long term.

Government is also presented with opportunities. The crisis will expose areas of weakness in our tax system and the way all levels of government deliver services. Growth-boosting reforms, perhaps difficult to implement in normal times, may be easier to pursue now. Balancing the tax system away from inefficient taxes in favour of less distortionary ones, slashing red tape and regulation that stifles business and innovation, and improving the delivery of critical services should all be priorities for government right now.

We have seen this in the approach to policy responses to COVID-19 – for example, the adoption of the National Cabinet model for decision-making and the collaboration between government and industry to pivot manufacturing to critical products like personal protective equipment for the health sector. But this efficiency in policy development will need to be retained for the long term, to ensure we don’t lapse into a ‘business as usual’ mindset once the immediate threat of COVID-19 has passed.

**The global economy has taken a body blow from COVID-19**

The global economy finished 2019 with accelerating momentum. COVID-19 has thwarted that, completely altering the outlook for the short and medium term. The most severe economic impacts, coinciding with the necessary shutdowns to control the spread of the virus, are expected to be felt in 2020.

The IMF expects the global economy to contract by around 3% in 2020 (Chart 1), almost twice the 1.7% contraction observed in 2009 in the wake of the global financial crisis.

Those countries that have faced greater difficulty in containing the virus will experience the greatest economic pain. In the United States – with 1.7 million COVID-19 cases and around 100,000 deaths at the time of writing – real GDP is projected to decline by around 6% in 2020. Across the euro area, the contraction is expected to be almost 8%.

![Chart 1: Global gloom](chart1)

**Real GDP, year-on-year growth**

- **2020 forecast**
- **2019 actual**

China was hit harder and earlier by COVID-19 than most countries, manifesting as a 6.8% decline in real GDP over the first quarter of 2020 – the first (official) contraction in more than 40 years. As its economy reopens and recovers, supported by significant stimulus, the IMF expects full-year GDP growth of 1.2% – a much better outcome than many advanced economies still struggling to contain the virus.

Sources: IMF World Economic Outlook Apr 2020
Early signs of recovery in China is generally good news for WA. China accounts for more than 80% of iron ore exports from Western Australia, worth $78 billion in 2019. Despite the short-term disruption, the immediate outlook for iron ore remains positive: it will be a key input for those jurisdictions seeking to mitigate the COVID-19 economic fallout through infrastructure investment.

Prices for iron ore and gold, WA’s first- and third-largest export earners respectively, remain well above recent averages, despite the COVID-19 disruption (Chart 2). Both prices have benefited from persistent demand: iron ore for its importance in steelmaking, gold for its status as a haven asset in times of economic uncertainty.

**Chart 2: A tale of two metals**  
*Key export commodity prices, index January 2018 = 100*

Prices for WA’s second most valuable export – LNG – have fared poorly through the COVID-19 outbreak, reinforcing a period of consistent decline over the last 18 months. Having peaked above US$8/mmbtu in October 2018, LNG had fallen to around US$2/mmbtu as of mid-May 2020. That’s bad news for WA’s $35bn LNG export sector.

Like the global oil trade, LNG has been hit by twin headwinds. First, economic shutdowns have led to a collapse in demand for energy. Second, having failed to reach agreement on production cuts to meet the fall in demand, Saudi Arabia and its OPEC partners initiated a price war with Russia in March. Many LNG contracts have prices linked to oil indices.

Despite the low price outlook, there is potential upside for WA’s LNG export sector. While the European gas market is increasingly saturated, almost all of WA’s exports go to Asia where the long-term demand outlook is stronger.

Current low energy prices also benefit local industry in WA, supporting the immediate task of increasing output and creating jobs in the aftermath of the crisis. Policy action to support new technologies in energy supply can keep this sector as a growth engine of the State in future (think hydrogen).

In addition to mitigating the economic fallout, the decision to keep WA’s mining and gas industries operating will have a positive fiscal impact. Iron ore and gold producers continue to pay royalties to State coffers, and amid the shutdown of some of Australia’s largest businesses, profitable resources companies will continue to pay company tax to the Commonwealth.

But clouding the potential for exports to lead the State out of the COVID-19 economic rut is a risk of growing trade tensions with China. At the time of writing, China had imposed 80% tariffs on Australian barley exports, an industry worth $1bn to WA, and the risk of further restrictions on exports like meat and dairy products remains.

However, while geopolitical sparring has the potential to dampen the State’s trade relationship with China, our key export – iron ore – is unlikely to be greatly affected. In 2019, China sourced an estimated 53% of its total iron ore requirement from Australia, drawing around 18% from Brazil and 16% from its own production.

Neither of these alternative sources is likely to be sufficient to displace Australian supply. China’s own iron ore supply is low-grade and expensive to process, presenting challenges for large-scale and cost-effective mining.

Australian iron ore also has a cost advantage over Brazilian product thanks to shorter shipping distances, and Brazilian supply continues to face challenges both from the spread of COVID-19 in that country and the Brumadinho tailings dam disaster in early 2019.

While exports have been the main driver of growth in WA over the last six years, the above risks – and the sheer scale of the economic cost of COVID-19 globally – mean that plenty of heavy lifting will need to occur in the domestic economy too to drag WA growth back into positive territory.

**COVID-19 has thwarted WA’s improving economic prospects**

Based on forecasts compiled in early April, we expect the WA economy to contract by 0.2% in 2019-20, noting that the impacts of COVID-19 have occurred mostly in the last quarter of the current financial year. The second half of 2020 is likely to be the most difficult period for WA, as recent sharp falls in employment and income work their way through the economy. As a result, we expect real gross state product (GSP) to contract by around 6% in 2020-21.

To put those numbers into context, our expectation is that around $17 billion will be wiped off the State economy in 2020-21, returning it to roughly the same size (in real terms) as it was in 2013-14.

Accounting for lost growth, we expect the State economy to be $27 billion smaller in 2020-21 than our previous forecast from December 2019 (Chart 3).

No part of the economy will be left unscathed by COVID-19, but the
That would wipe around $12 billion off the State economy in 2020-21 and see business investment returning roughly to the same level (in real terms) as in 2001-02.

There is a role for increased public investment to fill part of the gap left by private business, but a significant increase would be required. We expect more than $9bn to be lost in private construction investment in 2019-20 and 2020-21. This compares to $11.8bn that the State Government intends to spend in total as part of its Asset Investment Program over those two years, according to its mid-year budget update in December 2019.

In other words, the State Government would need to almost double its planned infrastructure spend to offset the decline in private construction activity in the coming two years. To date, most announcements by the State Government have related to bringing forward already planned projects. To materially move the dial on construction activity, this will need to be complemented with new projects too, made shovel-ready in quick time.

**Virus thrashes WA labour market**

April 2020 marked the largest month-on-month reduction in WA employment since records began, with more than 62,300 jobs lost in the State.

That follows more than 8,400 jobs lost in March. Over those two months, three years of employment gains were wiped out, taking the number of jobs back to where it was in March 2017 (Chart 5).

The official unemployment rate rose from 5.4% in March to 6.0% in April, in seasonally adjusted terms. That doesn’t sound too bad, but it has more to do with the technical accounting of the labour force statistics than it does with the real impact of joblessness. While 62,300 jobs were lost, only 4,700 were counted as additional ‘unemployed’ with 57,600 deemed to have left the labour force (technically not ‘unemployed’). That means the unemployment rate is only telling half the story and needs to be looked at in the context of another key indicator: the participation rate. The labour force participation rate fell from 68.0% in March to 65.2% in April, the largest reduction on record.

**Chart 3: Economic pain**

WA real gross state product (constant 2017-18 dollars)

Source: Deloitte Access Economics

Though the trajectory for investment had been improving in WA (the December 2019 quarterly accounts showed the fastest growth in several years), the outbreak of COVID-19 has drained cash from corporate balance sheets and generated tremendous uncertainty, depleting investor appetite. Our forecast is for private engineering and construction investment to fall by 46% in 2020-21 (Chart 4), with a similar reduction in equipment investment.

**Chart 4: Construction disruption**

WA real private construction and engineering investment (constant 2017-18 dollars)

Source: Deloitte Access Economics

If every person who lost employment between March and April was counted as having stayed in the labour force and unemployed, the jobless rate would instead be around 9.3% in WA. That would be the highest in almost 30 years, since the early 1990s recession.

April also saw a sharp increase in the number of underemployed people in WA – those who are employed but working fewer hours each week than they would like. An additional 61,900 became underemployed in April, adding to an increase of 12,500 in March. WA’s underemployment rate (as a share of the labour force) is now 14.6%, up from 8.7% in February.

That suggests that more than 20% of WA’s labour force is either unemployed or underemployed – an

**Chart 5: Jobs decimation**

Monthly change in seasonally adjusted WA employment (thousands)

Source: ABS Cat. 6202.0
extraordinary level of underutilisation of the labour force.

The reference period for the April 19 labour force statistics was the fortnight ending 11 April. That means job losses occurring in the last three weeks of April are not necessarily reflected in these figures. Instead, some insight can be gained from experimental weekly data released by the ABS.

This data suggests that over the seven-week period from 14 March to 2 May, employment in WA declined by approximately 6% (Chart 6). Applying this change to the entire workforce, that would imply total job losses in the State of around 81,000 jobs over that period.

**Chart 6: Generational (jobs) gap**
**Estimated change in WA employment, 14 March to 2 May**

<table>
<thead>
<tr>
<th>Age Group</th>
<th>Under 20</th>
<th>20-29</th>
<th>30-39</th>
<th>40-49</th>
<th>50-59</th>
<th>60-69</th>
<th>70+</th>
</tr>
</thead>
<tbody>
<tr>
<td>All employees</td>
<td>-15%</td>
<td>-5%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>Males</td>
<td>-15%</td>
<td>-5%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>Females</td>
<td>-15%</td>
<td>-5%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
</tr>
</tbody>
</table>

Source: ABS Cat. 6160.0

The distribution of job impacts has not been even in demographic terms. Employment among males fell by an estimated 6.0%, compared to 5.4% for females, over that seven-week period. And jobs among those aged under 20 fell by an estimated 14%, with losses for those aged 20-29 at 9% and those aged 70 and above at 10%. In contrast, jobs among those aged 50-59 have declined by just 3%.

These are worrying signs for the long-term workforce impacts of COVID-19. Even when the economy begins to recover in earnest, older workers are likely to face challenges in re-entering the workforce. And young people who have become jobless have a higher chance of remaining unemployed in the long term.

For example, as of December 2019, around one in five Australian jobseekers aged 15-24 was already in ‘long term unemployment’ – that is, seeking a job without success for more than a year. That speaks to an important role for government to play in ensuring these young Western Australians have access to education and training opportunities and do not remain entirely idle, so they can emerge in the post-COVID world with new and valuable skills.

Naturally, those industries most affected by the lockdown measures have suffered the greatest losses in jobs. Over the seven weeks from 14 March to 2 May, employment in WA’s hospitality sector fell by more than a quarter (Chart 7), suggesting the loss of around 27,000 jobs in that sector alone.

**Chart 7: Services slump**
**Estimated change in WA employment, 14 March to 2 May**

<table>
<thead>
<tr>
<th>Industry</th>
<th>Hospitality</th>
<th>Real estate</th>
<th>ICT</th>
<th>Admin services</th>
<th>Other services</th>
<th>Arts &amp; rec</th>
<th>Prof. services</th>
<th>Agriculture</th>
<th>Manufacturing</th>
<th>Retail trade</th>
<th>Wholesale trade</th>
<th>Mining</th>
<th>Construction</th>
<th>Transport</th>
<th>Education</th>
<th>Finance</th>
<th>Utilities</th>
<th>Pub. admin/safety</th>
<th>Health</th>
</tr>
</thead>
<tbody>
<tr>
<td>Percent Change</td>
<td>-30%</td>
<td>-20%</td>
<td>-10%</td>
<td>0%</td>
<td>10%</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
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<td></td>
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</tr>
</tbody>
</table>

Source: ABS Cat. 6160.0

The impact in education (dominated by the public sector) has been more moderate, while in public administration and health – two industries critical to the immediate COVID-19 response – employment is estimated to have increased by 2% and 4%, respectively, over the seven weeks to 2 May.

WA has fared slightly better than the national average in terms of jobs lost since 14 March, with a cut of 7.3% to employment nationally. Victoria has been worse affected, with employment declining by more than 8%. Still, there are no winners: every state and territory has been affected and around 600,000 jobs were lost across the country between March and April alone.

The scale of the employment challenge is unprecedented. Official estimates of job losses to date do not reflect jobs that might have been lost were it not for JobKeeper and other stimulus measures. When those temporary measures expire, the usual policy response of trying to create jobs through growing demand may not work.

Rather, more innovative approaches to employment policy will be needed, including an emphasis on providing those out of work with the right training opportunities to upskill or reskill and adapt to new ways of working (both the WA and Commonwealth Governments had identified workforce training and development as a focus area in late May).

Direct support for employees and those who have been stood down will need to be complemented by support for the demand side of the labour market – starting or restarting businesses that have shut down due to COVID-19. An ABS survey of business impacts of COVID-19 found that more than half of Australian businesses had been adversely affected by social distancing requirements, with 69% experiencing reduced demand for goods and services and 72% reporting reduced cash flow.

Though some insolvency laws have been temporarily relaxed for six months, these business impacts will eventually flow through to a greater number of business exits. There is
an opportunity for government to support the (re)starting of businesses affected by COVID-19. For example, the State Government could leverage its New Industries Fund to support business starts and job creation and – by supporting investment in critical areas – both diversifying the State economy and making it more resilient to future crises.

**Retail a short-term beneficiary**
Retail turnover in WA grew by around 10% in March in seasonally adjusted terms – the largest monthly increase in 40 years. But that boost in turnover was mostly driven by the panic-buying that characterised the early period of the outbreak.

Turnover growth was highest among liquor stores (26% month-on-month), followed by significant growth in spending on groceries, pharmaceutical and cosmetic products, and other household goods (Chart 8).

**Chart 8: Panic-buy high**
*WA retail turnover (seasonally adjusted terms), month-on-month change, March 2020*

On the other hand, signifying the slump in non-necessity spending and the shuttering of many retail businesses, turnover at department stores and takeaway food outlets fell by more than 10%, at cafes and restaurants by more than 20%, and by around 37% on clothing.

But the boost for retail was temporary only. Preliminary data suggest that retail turnover fell by 18% across Australia in April 2020, wiping out gains in March, as the full force of lockdown measures hit the sector.

Some relief should come for the worst-affected sectors - like retail, hospitality and tourism – as the State Government begins to reopen the economy and dismantle regional borders in the second-half of May.

WA is well-positioned to take advantage of a period in which interstate and international borders remain closed, but intrastate restrictions are relaxed. In 2019, of the total $13.5 billion spent in WA’s tourism industry, almost two thirds ($8.5 billion) was spent by Western Australians on intrastate travel. WA had the highest share of intrastate tourism expenditure of any state or territory in 2019, and consequently, more to regain by easing restrictions on regional travel sooner (Chart 9).

**Chart 9: Staycation**
*Tourism expenditure by type of traveller, 2019*

The impact of the COVID-19 shutdown on tourism has been catastrophic. That’s one area where the State Government has topped up Commonwealth support for struggling businesses.

The economic recovery will be long and slow. For example, we don’t see employment returning to pre-COVID levels in WA until 2024 – likely long after we have adapted to living with the virus itself.

As then-White House Chief of Staff Rahm Emmanuel said during the GFC, "never let a crisis go to waste". In this case, the opportunity for business and government will be to use the lessons learned from this crisis to steepen the curve of economic recovery, to power job creation and drive productivity growth in post-COVID WA.

In dealing with an unprecedented crisis, all possible solutions should be on the table. There are several key questions for government and business to consider in developing solutions to address the COVID-19 impacts outlined in this note:

- How can we accelerate public sector investment in the short to medium term, to fill some of the gap left by private business (and still ensure value for money for taxpayers)?
- As we emerge from the crisis, how can government support the private sector to invest in areas that are critical to the State’s recovery?
- How can business and government partner to identify and provide education and training opportunities to workers stood down due to COVID-19? Which skills will be critical in the ‘post COVID’ world?
- What areas of red tape and regulation will inhibit the recovery, and how can they be removed or revised? Which State tax settings need rethinking?
- How will government and business work together to reduce the risk of a ‘second wave’, and make the economy more resilient to future crises like COVID-19?
Contacts

Noel Richards
Partner
Deloitte Access Economics
Tel: +61 8 9365 7303
norichards@deloitte.com.au

James Campbell-Sloan
Director
Deloitte Access Economics
Tel: +61 8 9365 7110
jcampbell-sloan@deloitte.com.au

Aiden Depiazzzi
Senior Economist
Deloitte Access Economics
Tel: +61 8 9365 7853
adepiazzzi@deloitte.com.au

Deloitte Access Economics
Level 9, Brookfield Place, Tower 2
123 St Georges Terrace
Perth WA 6000 Australia
Tel: +61 8 9365 7000
www.deloitte.com/au/deloitte-access-economics

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