



WA Budget: the lucky state in the lucky country

IPAA WA Budget Briefing

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WA Budget: the lucky state in the lucky country

WA has partly made its own luck

- WA projects strong surpluses and low net debt
- WA's zero COVID strategy contributed to WA's economic outperformance

But WA has also been very lucky

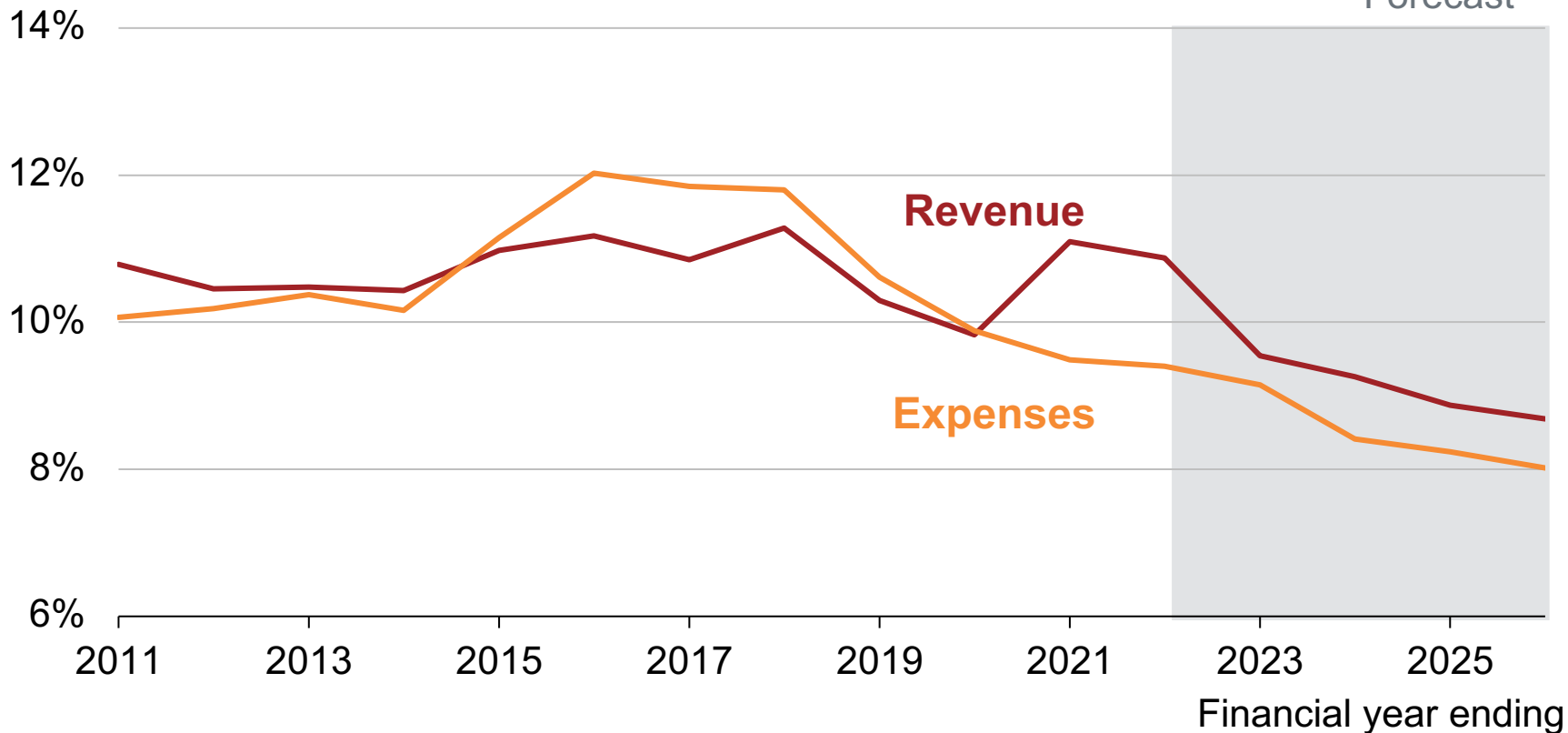
- Record high commodity prices have helped a lot
- WA benefited a lot from macro policies calibrated for lockdown states
- The 2018 GST deal is also having a big impact

Will WA's luck hold into the future?

- COVID is still with us
- Inflation is now on the rise: in Australia and around the world
- China geopolitical risks are intensifying
- Commonwealth finances are under pressure
- State fiscal pressures will rise in coming decades: ageing, climate
- Time for a WA IGR?

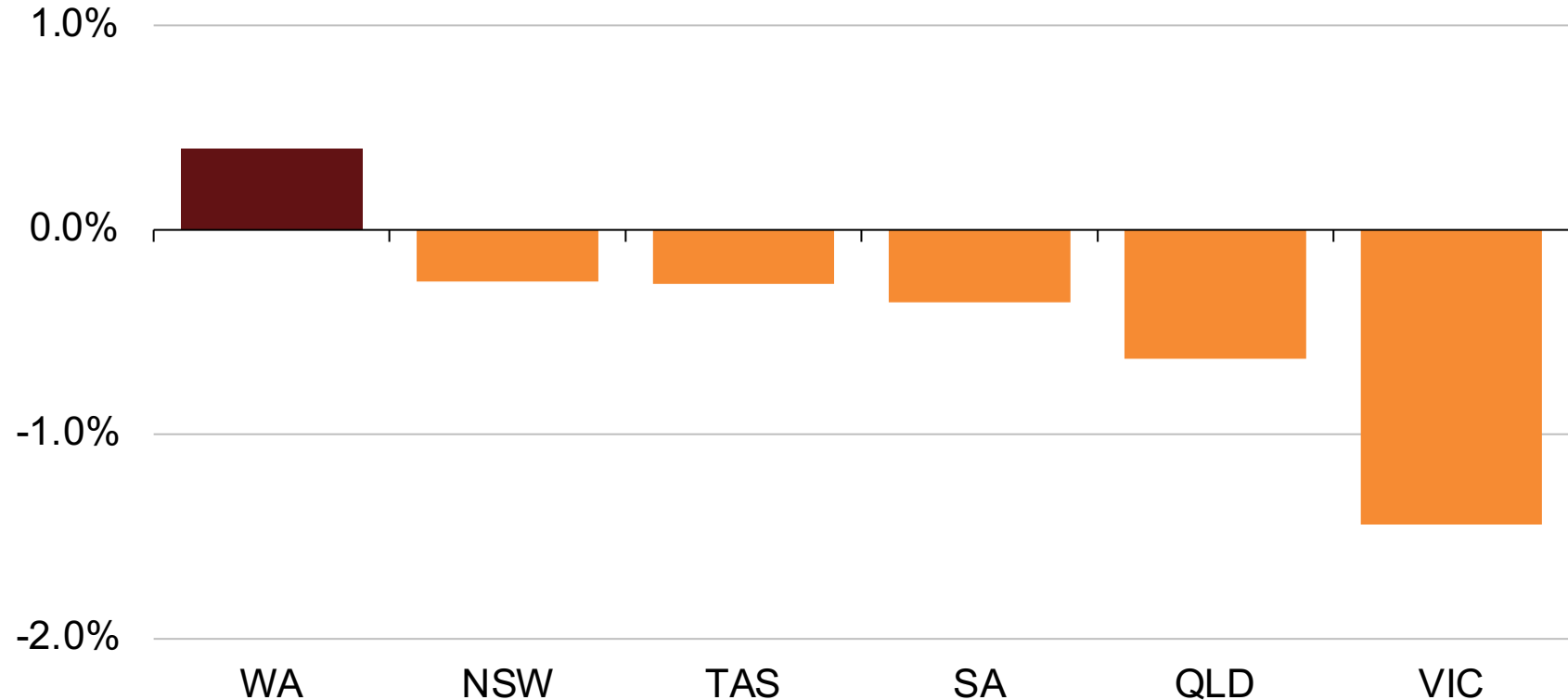
The WA Budget is in surplus. Notable spending restraint in the outyears

WA Government revenue and expenses, per cent of GSP



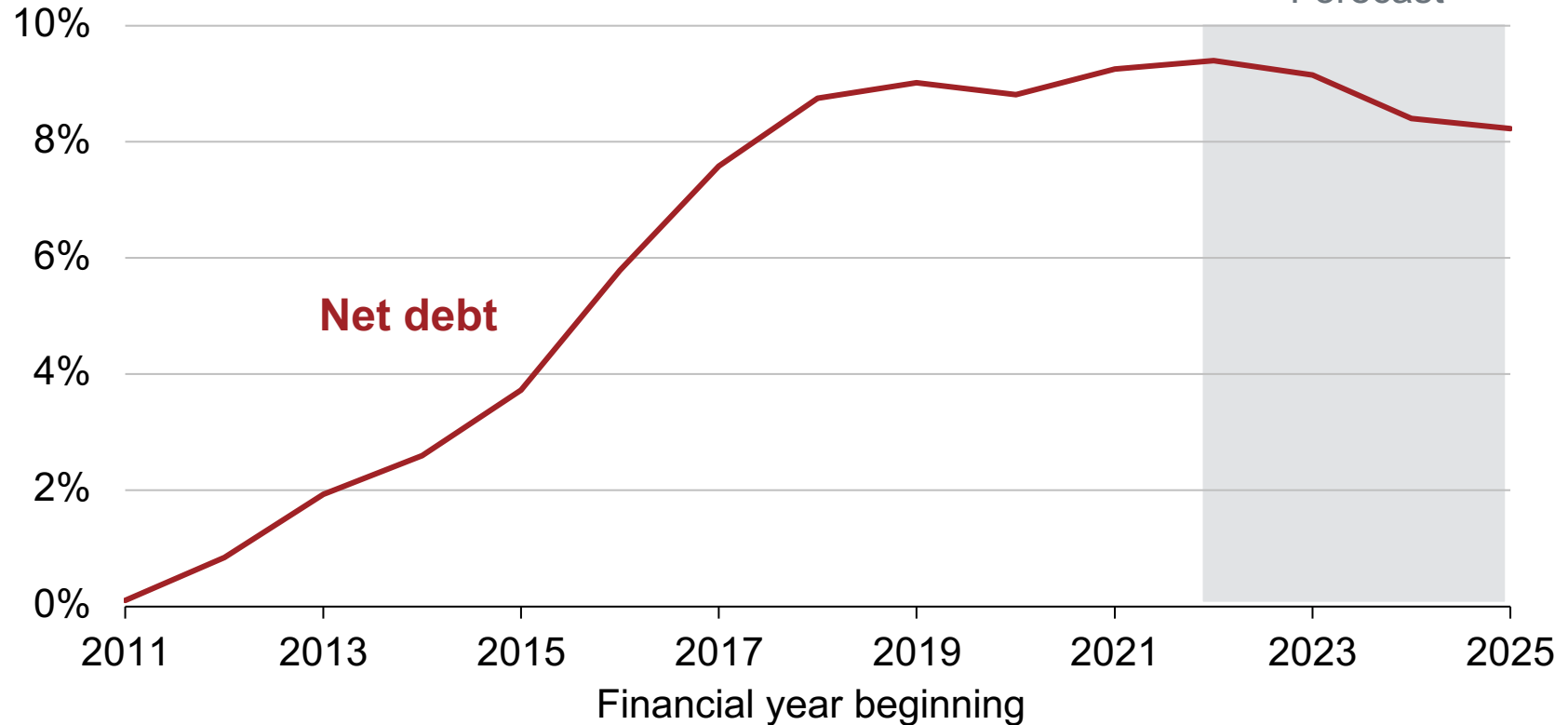
WA is the only state government in surplus

Forecasted net operating balance as a per cent of GSP, 2022-23



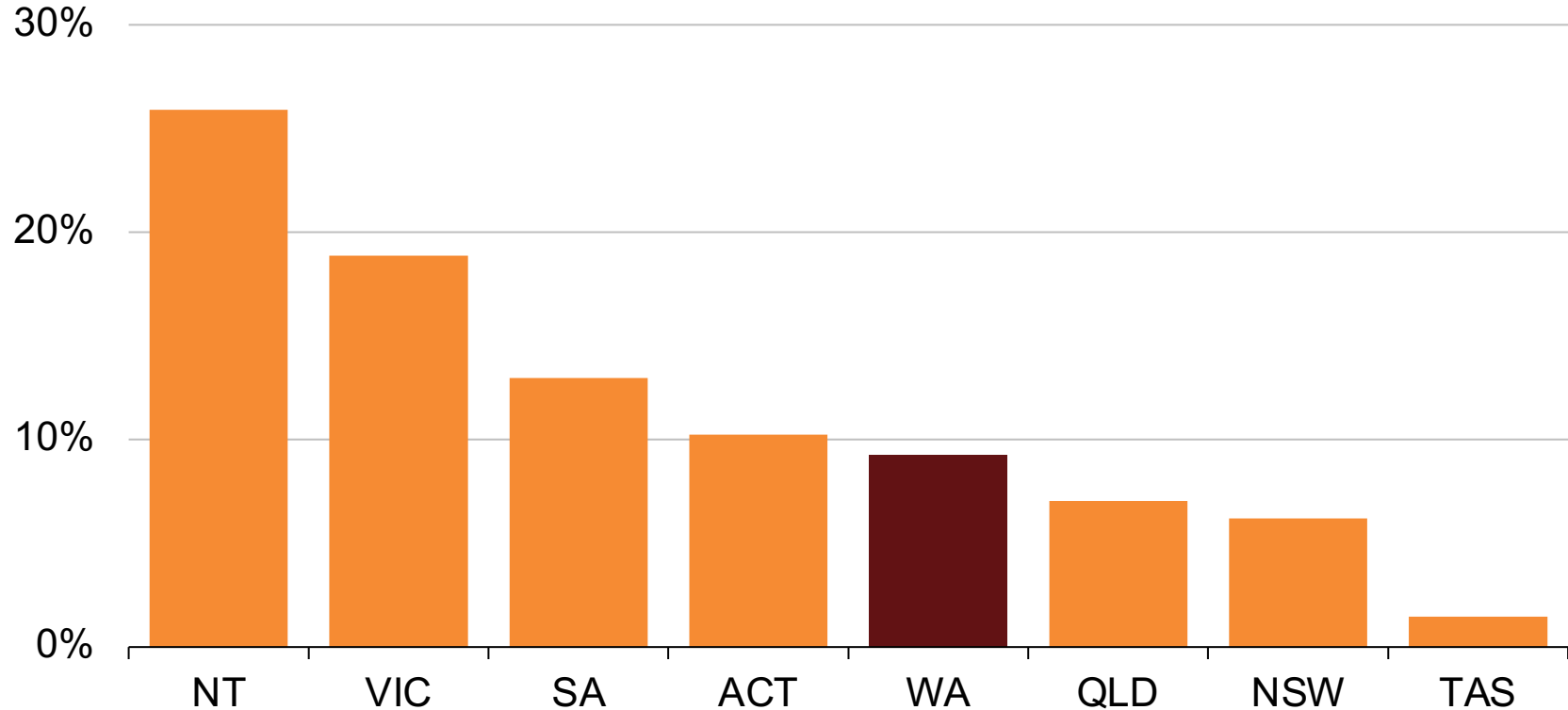
WA's net debt is projected to fall as a share of GSP to 2025

WA net debt as a per cent of GSP



... and is middle of the pack compared to other states

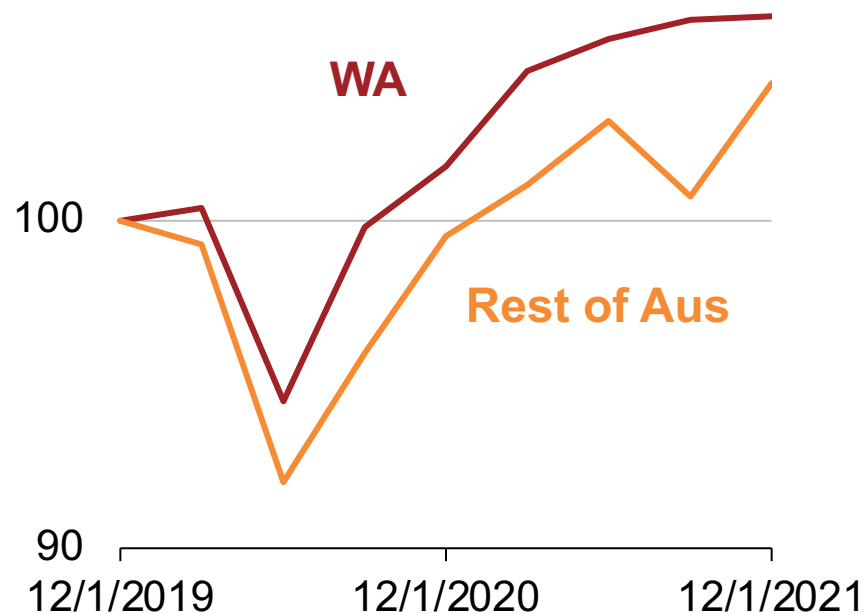
Net debt as a per cent of GSP, 2020-21



WA's economy has fared better than the rest of the country during COVID

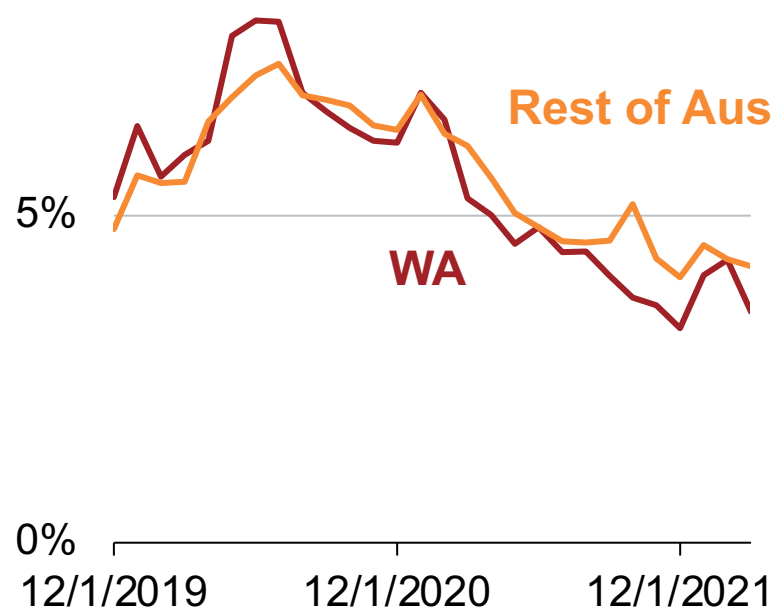
State final demand, index, 100 = Dec 2019

110



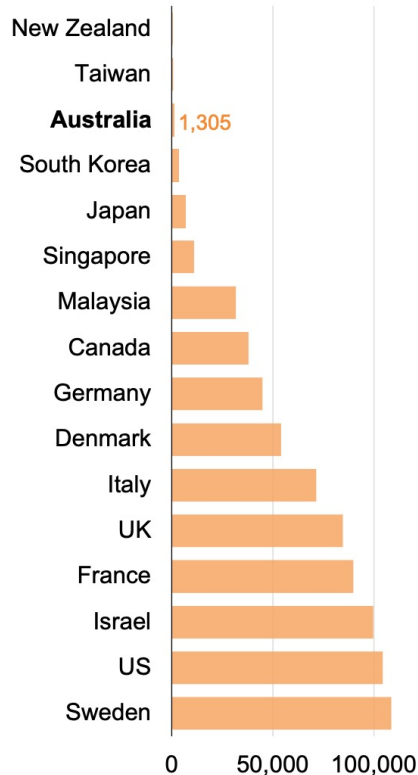
Unemployment rate

10%

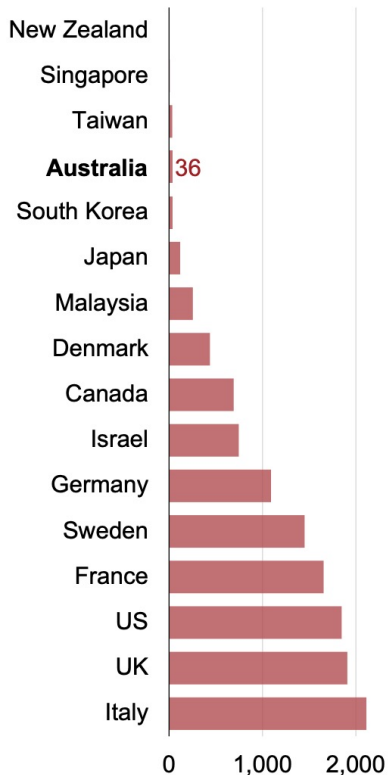


WA's "COVID Zero" strategy was the best of a bad set of choices, at least until vaccines arrived

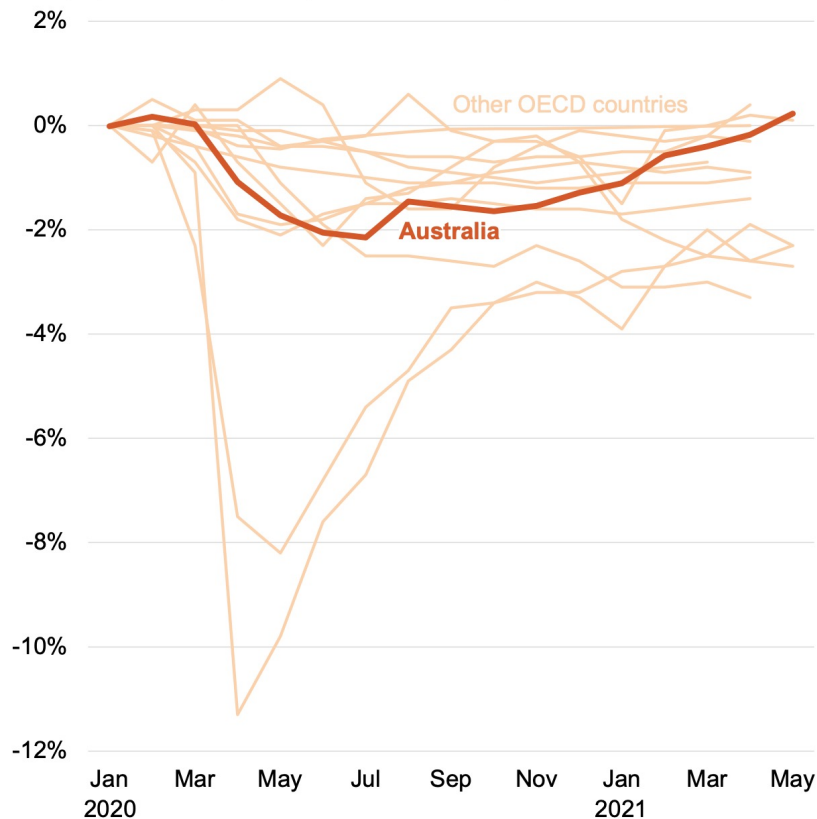
COVID **cases** per million people



COVID **deaths** per million people

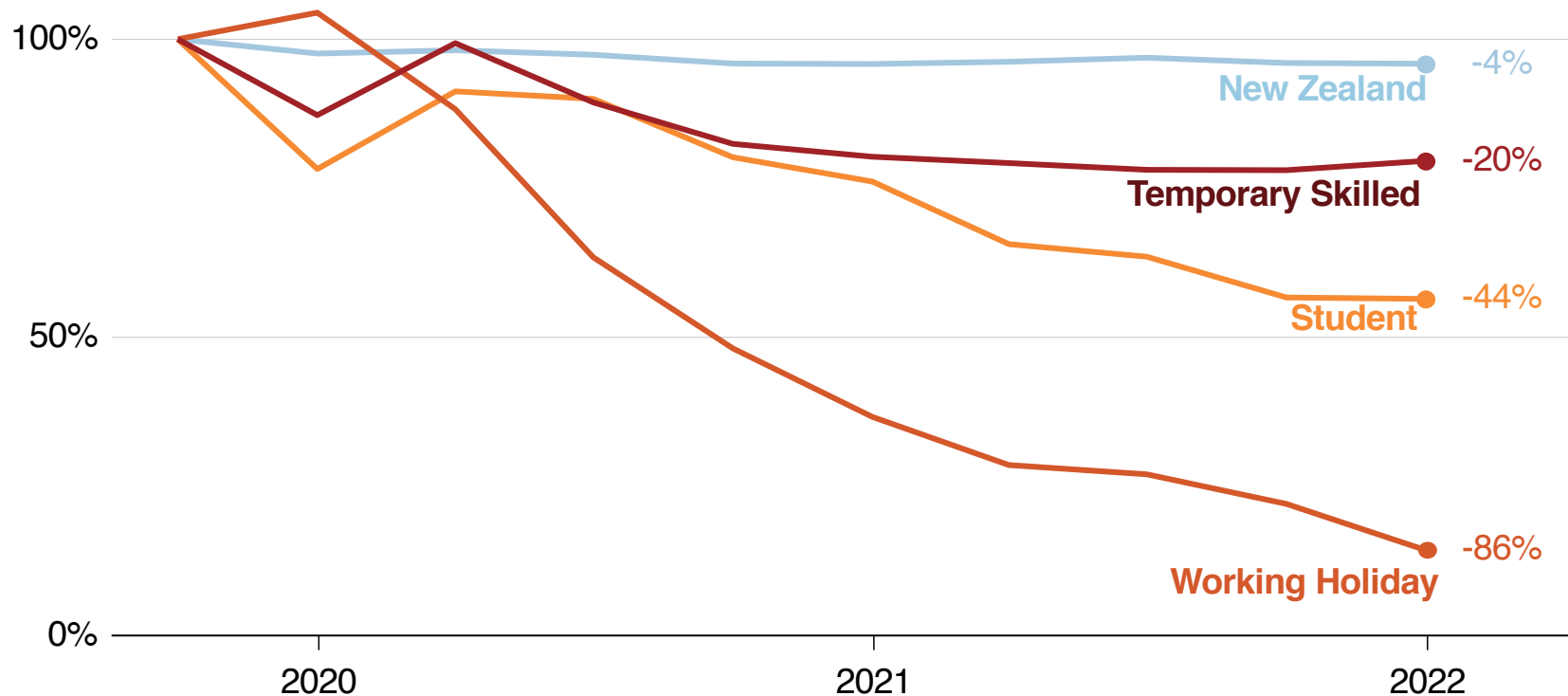


Unemployment rate (inverted) relative to January 2020 levels



COVID border closures greatly reduced the numbers of *unskilled* temporary migrants in Australia

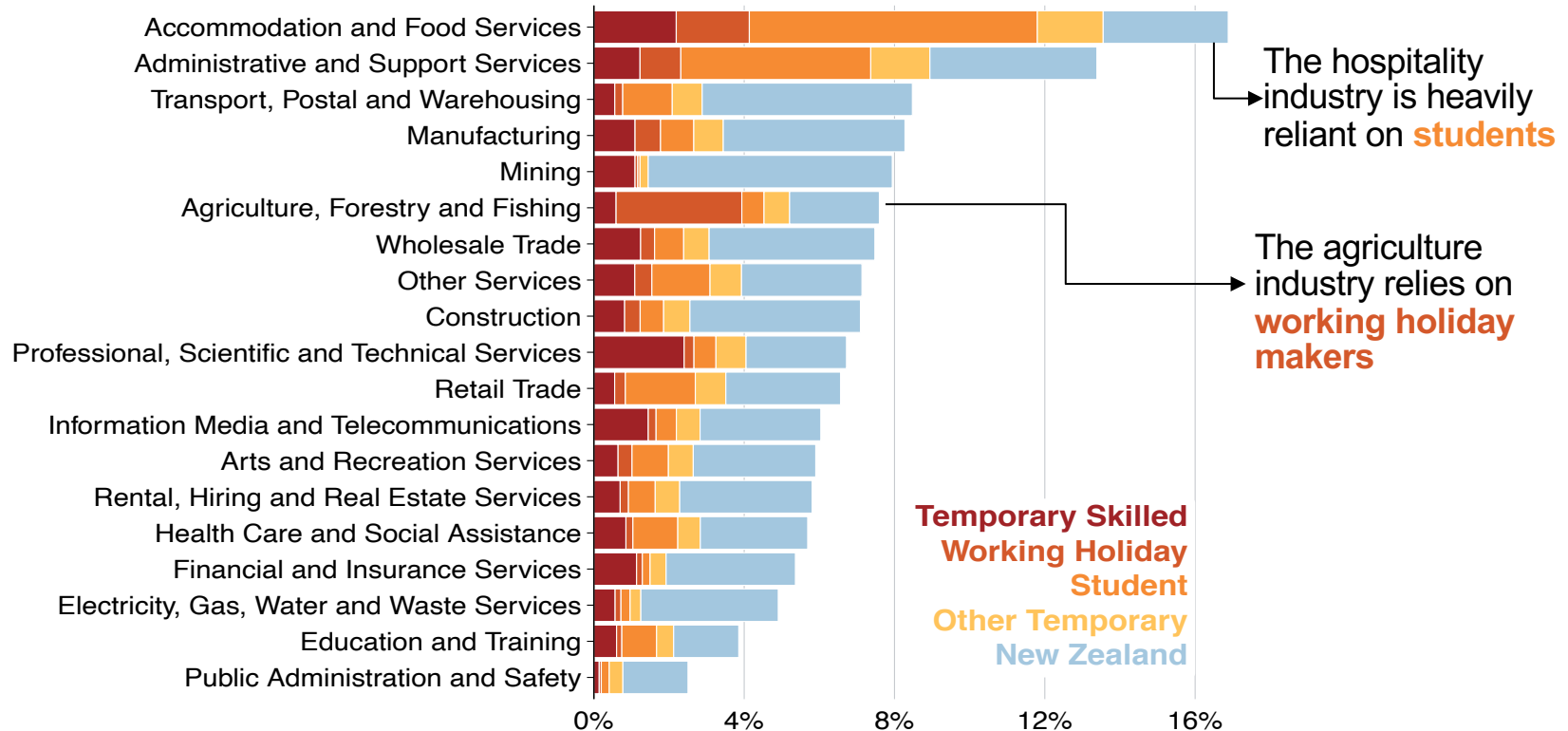
Change in temporary visa-holders in Australia since 2019



Source: DHA (2022).

Some industries were more exposed to border closures than others

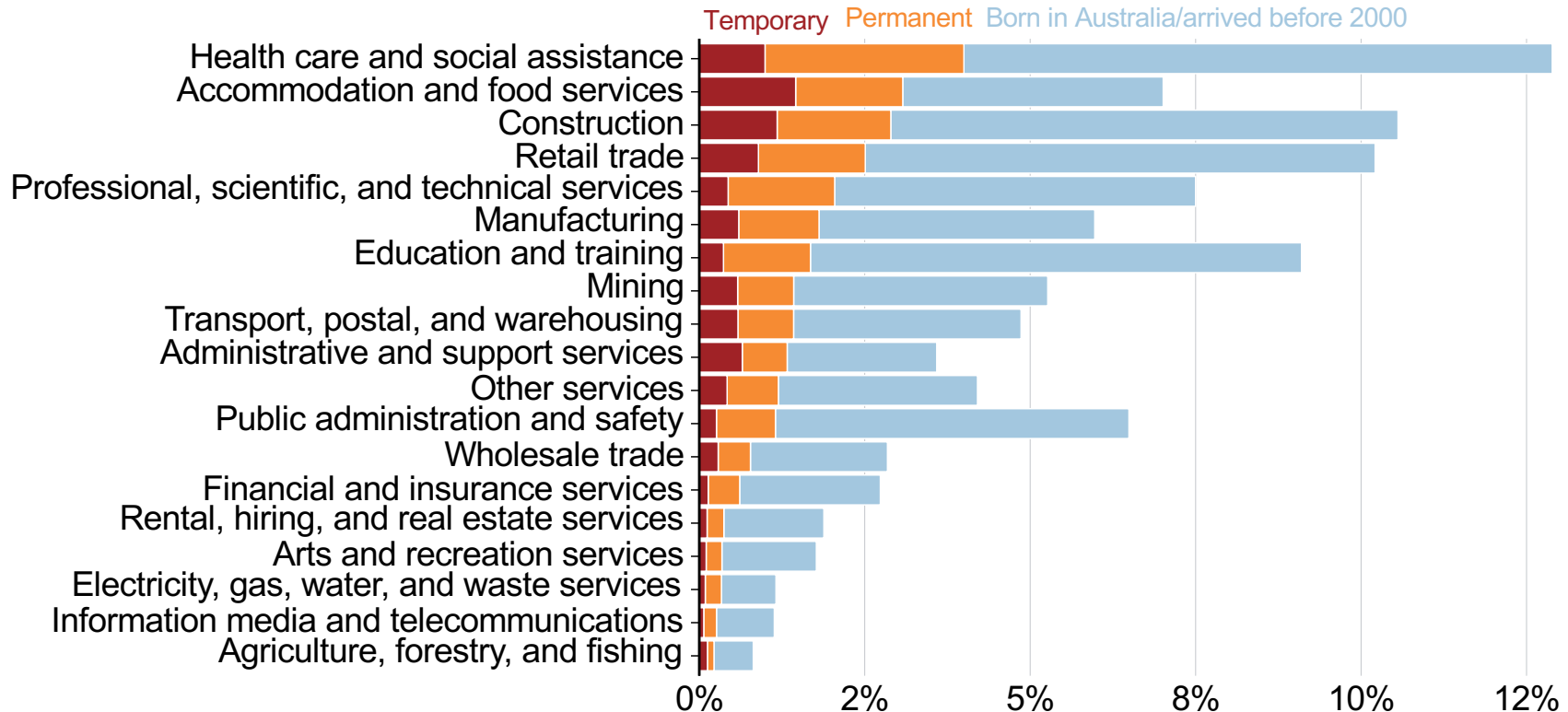
Temporary workers, share of industry (All Aus)



Source: Grattan analysis of ABS Census (2016).

WA relies comparatively more on migrants in healthcare, hospitality and construction

Major industries, share of all workers (Greater Perth Area)



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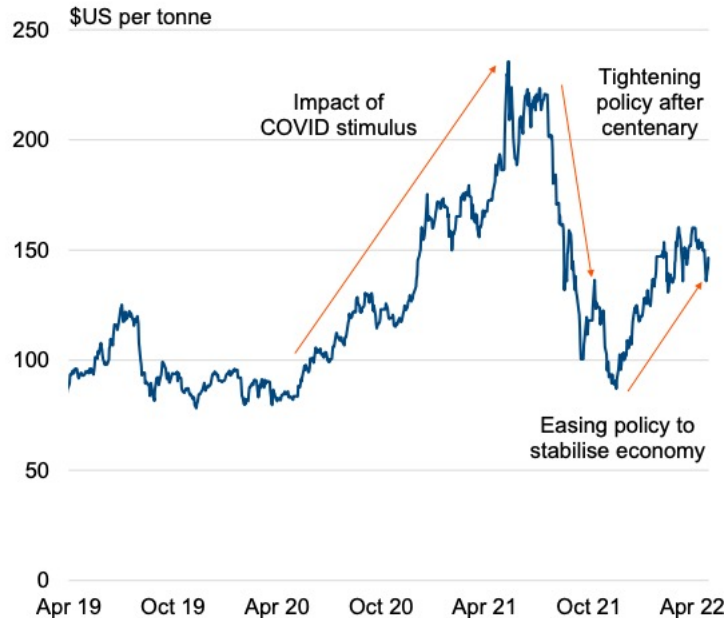
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Will WA's luck hold into the future?

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WA's budget bottom line driven by strong iron ore prices

IRON ORE PRICE Delivered to North China



Iron ore prices have risen to US\$151 / tonne by mid-April

Each US\$1 / tonne increase in iron ore prices adds \$81m to the WA budget bottom line

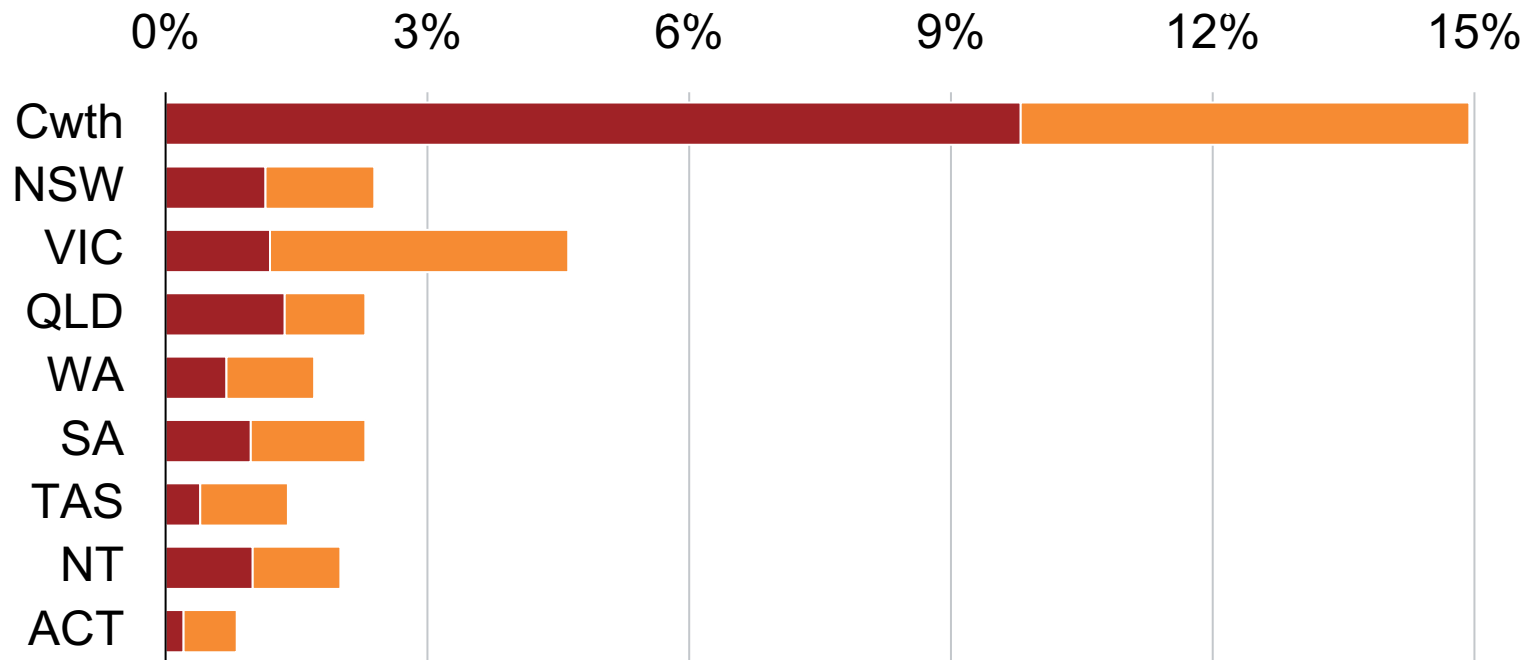
WA Treasury assumes decline to US\$66 / tonne in the outyear forecasts

Federal Treasury assumes decline to US\$55 / tonne

What's the federation done for us lately?

Big federal stimulus helped all states bounce back quickly

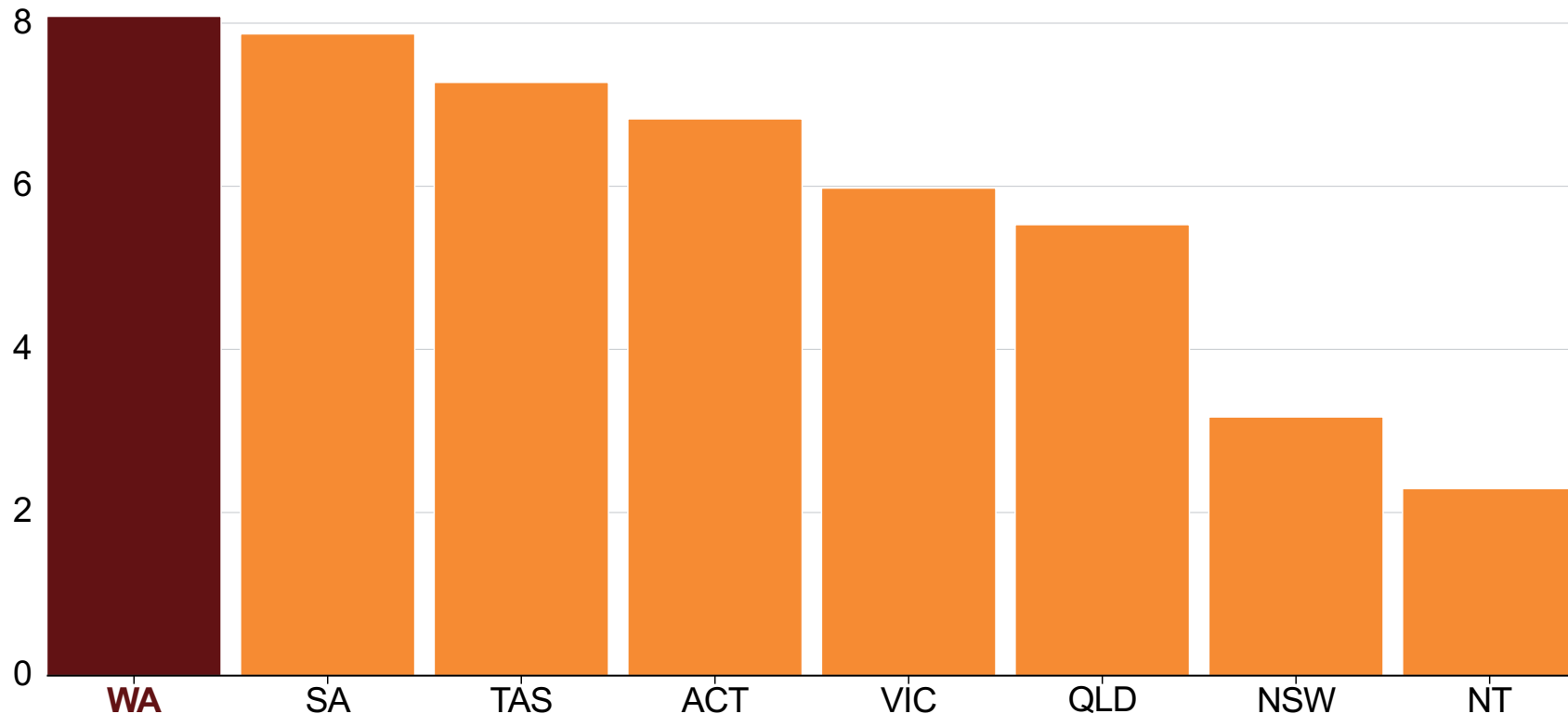
COVID spending commitments by government in 2020-21, as a % of pre-crisis GDP/GSP



Notes: 'Rescue' spending includes measures to help households and businesses stay afloat during the shutdowns (such as JobKeeper). 'Recovery' spending includes stimulus and other initiatives to create jobs and boost activity (such as JobMaker). Source: Grattan analysis of Commonwealth and state budget papers.

What's the federation done for us lately? Federal stimulus calibrated for lockdown states gave an outsized boost to WA

HomeBuilder applications per 1000 population

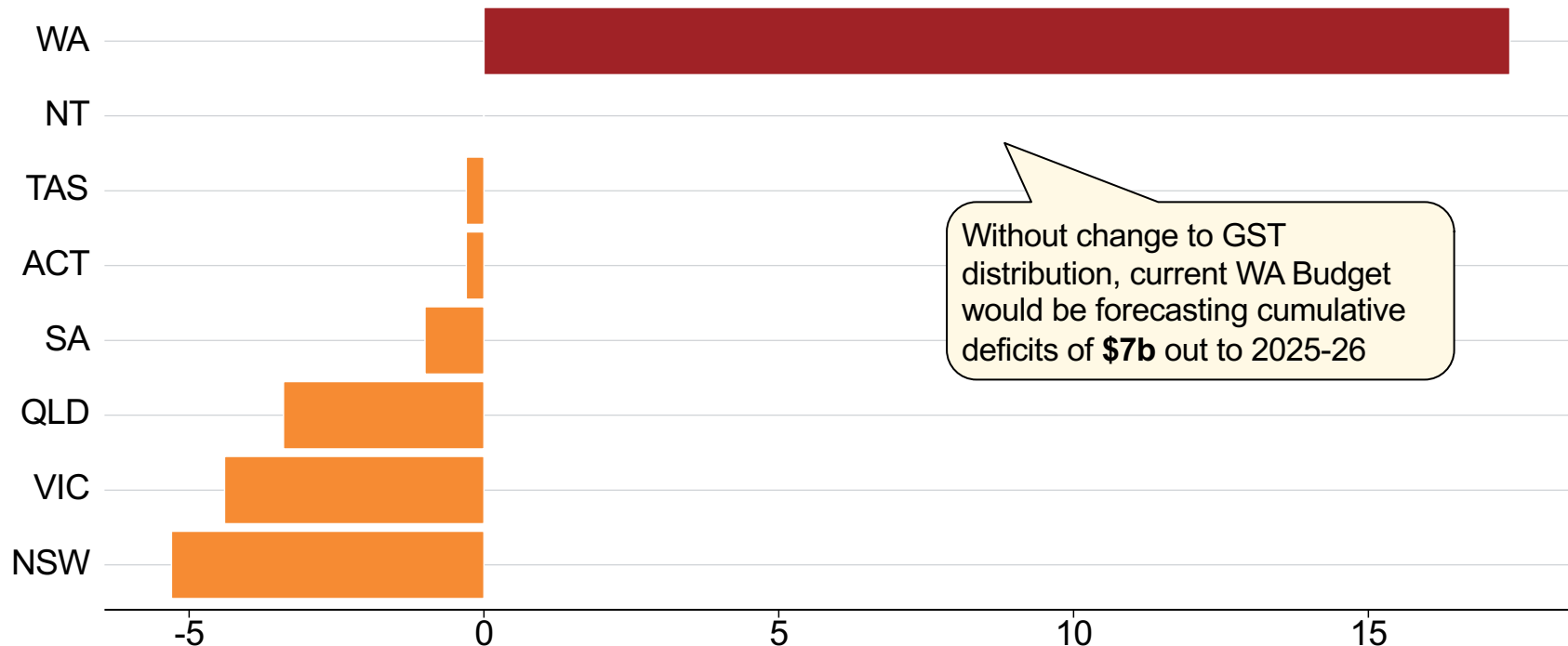


Notes: HomeBuilder applications as at 11 Feb 2022 and population as at September 2021.

Sources: ABS National, State and Territory Population; Treasury; Grattan Analysis

WA Budget benefits massively from the 2018 changes to the GST distribution

Impact on GST distributions from the change to the new system, excluding the no-worse-off-guarantee (\$ billions), 2022-23 to 2025-26



The debate over the GST may not be over...

CHAPTER 3 – VICTORIA'S ECONOMIC RECOVERY DESPITE INSUFFICIENT COMMONWEALTH SUPPORT

- The COVID-19 pandemic caused a major disruption to Victoria's economy – as it did to Australia and the world. Yet Victoria's economic recovery has been impressive, and the Victorian Government's health and economic responses have been crucial to this recovery.
- The Victorian economy was leading the nation prior to the onset of the COVID-19 pandemic in early 2020. Over the five years to 2018-19, Victoria's economic and employment growth rates were higher than in any other state.
- The Victorian Government responded quickly to address the impacts of the COVID-19 pandemic on the state's economy, supporting the public health response as well as workers, businesses and the community.
- Investment in major infrastructure projects has been critical in supporting the state's economic recovery. However, the state continues to receive inadequate infrastructure funding from the Commonwealth. Victoria's share of Commonwealth infrastructure funding has consistently been well below the state's population share.
- The **GST** is a vital source of funding for Victoria. However, the Commonwealth Government has not allowed the independent GST umpire, the Commonwealth Grants Commission, to account for the impacts of the COVID-19 pandemic on GST distribution. In addition, changes made to the GST system in 2018 to benefit Western Australia continue to pose a significant fiscal risk to Victoria, and all other states, if the no-worse-off guarantee is not extended beyond 2026-27.
- Changes to the GST distribution put at risk Victoria's capacity to support recovery from the pandemic and fully fund essential services such as schools and hospitals, given GST funding accounts for almost a quarter of Victoria's total revenue.

Source: Victorian State Budget, 2022-23.

Box 4.4: Commonwealth changes to how GST is distributed under horizontal fiscal equalisation (HFE) are inequitable and unsustainable

In 2018, the Commonwealth Government legislated changes that changed how GST is distributed amongst states and territories. This included the introduction of a relativity floor (that is, a minimum share of GST) that a state or territory receives. The changes will be implemented over a six-year transition period from 2021-22 to 2026-27.

For New South Wales the changes are expected to reduce GST revenue by around \$1.3 billion in both 2022-23 and 2023-24. However, New South Wales is currently protected from the reduction in GST by a temporary, legislated 'no worse off guarantee'. This guarantee requires the Commonwealth to compensate states' shortfalls in GST revenue between the old and new arrangements until 2026-27. All states and territories, other than Western Australia, are reliant on these no worse off payments.

In the meantime, Western Australia is benefiting on two fronts – receiving a GST top-up payment of \$1.5 billion in 2021-22, while also enjoying record growth in iron ore royalty revenue. Directing GST revenue to Western Australia, at a time when it is running an average surplus of \$1.9 billion, is inequitable and unfair to other states.

Under the Commonwealth's changes, the cost of these payments is progressively transferred onto other states and territories through foregone GST revenue. Once fully implemented by 2026-27, GST will be distributed in a way that effectively subsidises the state with the greatest fiscal capacity. This means the Western Australian Government can provide greater access to potentially higher quality services and more infrastructure to its residents at a lower taxation burden.

The affordability of the changes is also a major concern. The cost of the changes is currently almost twice as much as originally anticipated. The 2021-22 Commonwealth Budget estimates the total cost of the new arrangements will be over \$10 billion from 2019-20 to 2023-24. This is significantly more than the \$3.7 billion originally estimated by the Commonwealth in 2018. This is contributing to the Commonwealth's own deficit at a time when these dollars could have been better spent on productivity-enhancing reforms that support the post-pandemic recovery.

New South Wales will continue to advocate for a fairer GST distribution that supports productivity growth and economic efficiency, and ensures states and territories can continue to fund and deliver high-quality services and infrastructure in a sustainable way.

Source: NSW State Budget, 2021-22.

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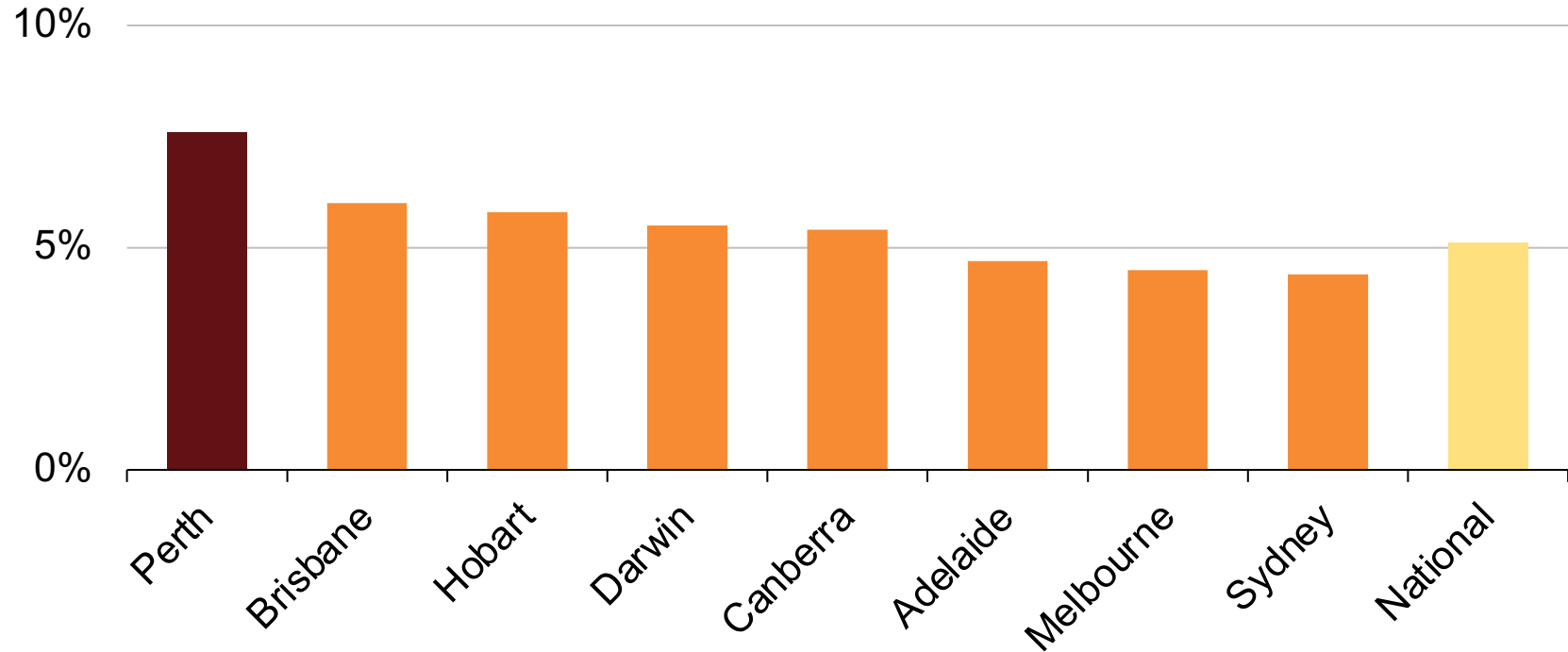
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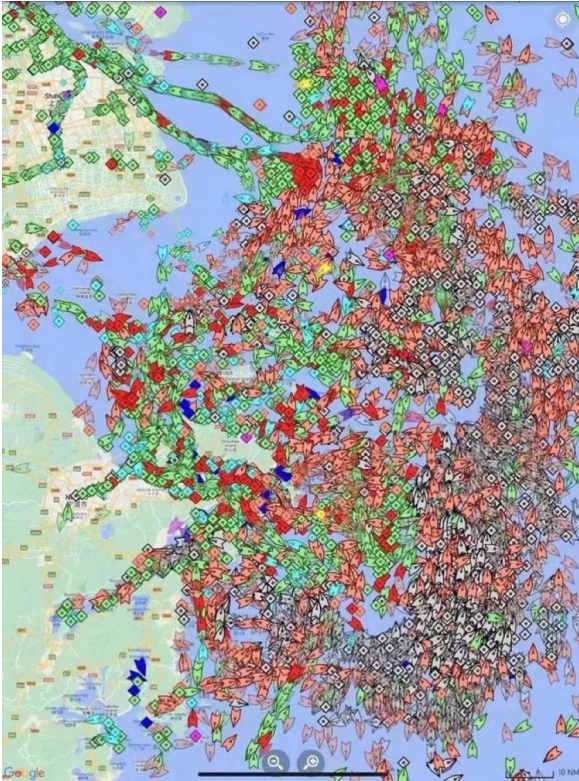
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WA inflation is running hotter than the rest of the country

CPI, annual change, March 2021



Further inflationary pressures are building, driven largely by international developments

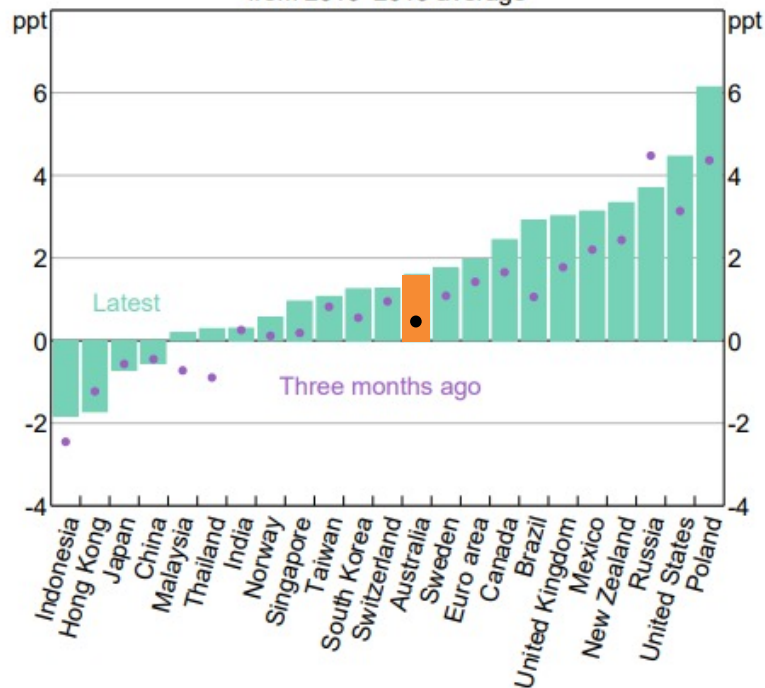


- International **supply constraints** are the main driver
 - Conflict in Ukraine
 - Zero COVID in China
 - Supply chain overhang from 2 years of COVID restrictions
 - 60% of WA business' identify supply chain disruption as a barrier to growth (CCIWA)
- The Commonwealth is adding 'fiscal fuel to the fire'
 - Extra discretionary stimulus of **1%+ of GDP** in the 2022-23 Budget

Growing signs that US / EU inflation is becoming entrenched

Core Inflation*

Year-ended, deviation of three-month average
from 2010–2019 average

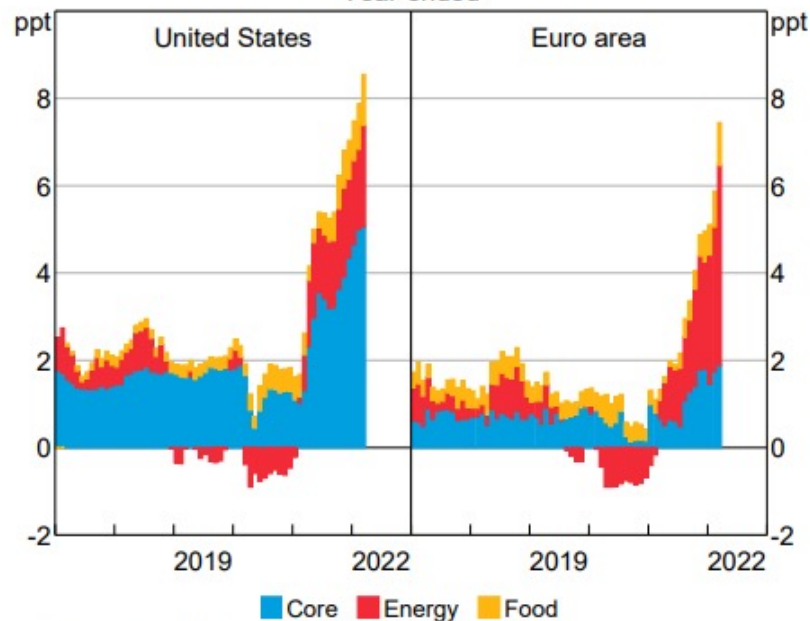


* Headline measure used for Hong Kong.

Sources: CEIC Data; RBA; Refinitiv

Contributions to Headline Inflation

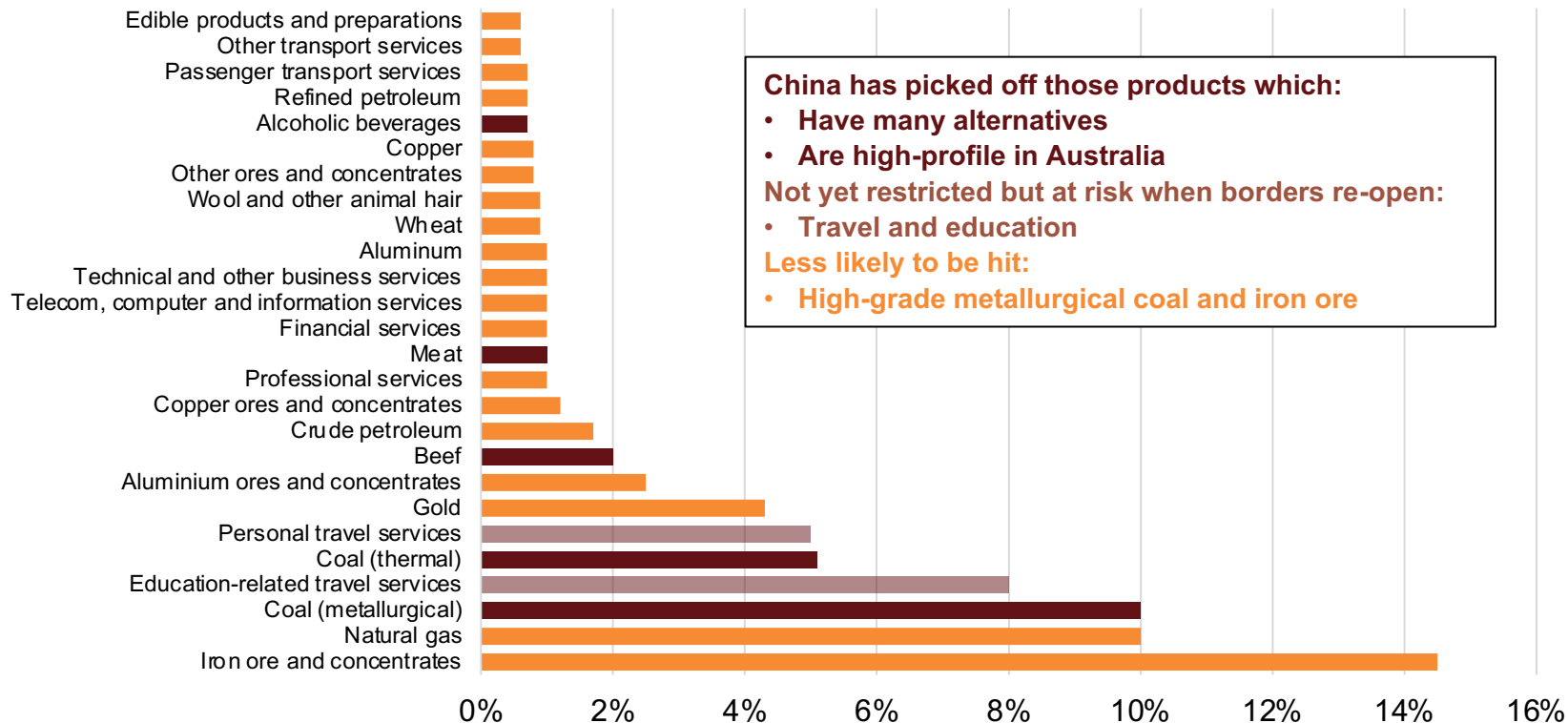
Year-ended



Sources: BLS; Eurostat; RBA; Refinitiv

China trade tensions are ramping up, but key WA exports appear safe

Australian exports by % of total export value, type, key risks



Commonwealth government comes out of COVID with significantly higher spending

Per cent of GDP

35%

30%

25%

20%

15%

1971

1981

1991

2001

2011

2021

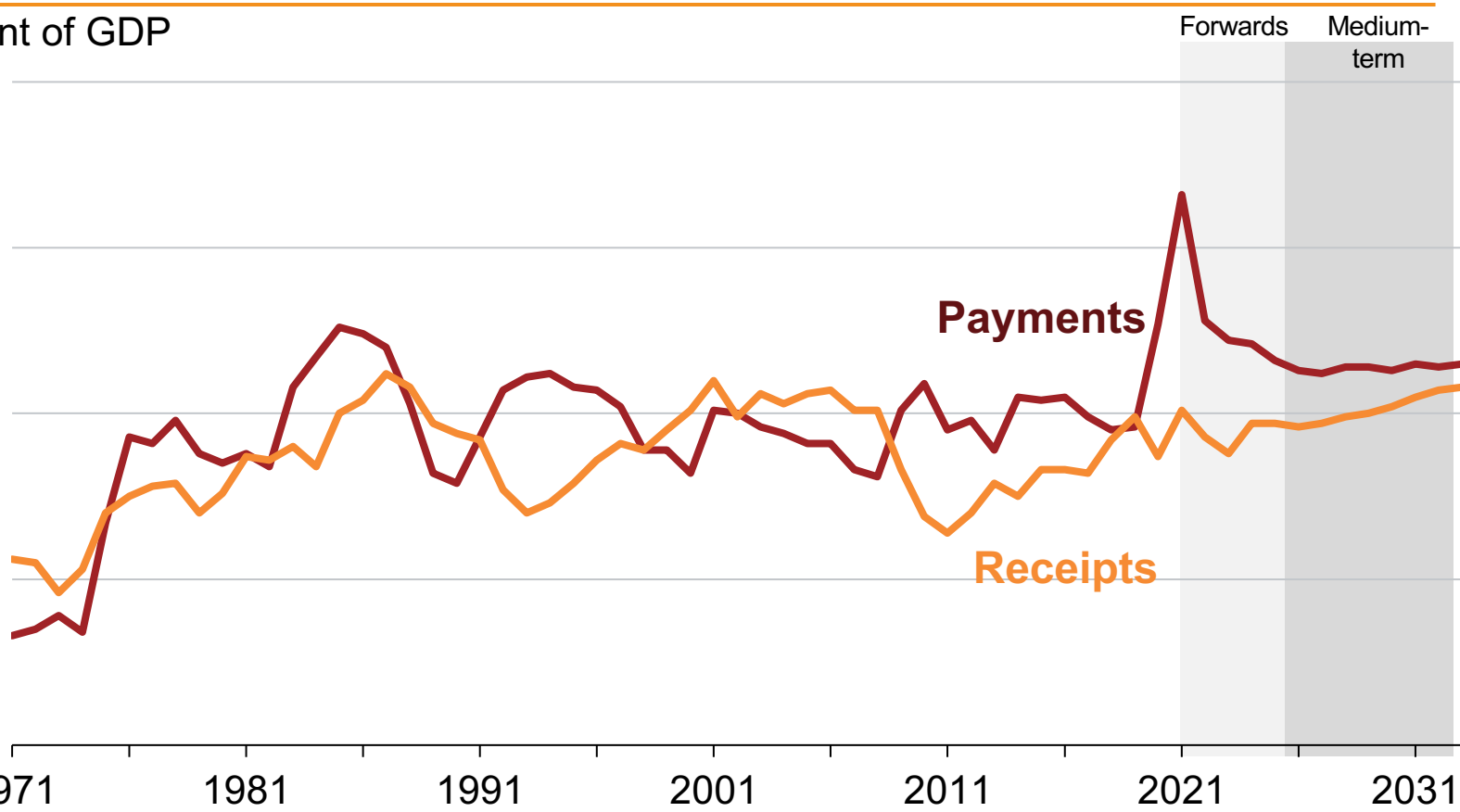
2031

Forwards

Medium-term

Payments

Receipts



And no evident appetite to raise more revenue

We will maintain our commitment to the [23.9 per cent GDP] tax cap as a form of fiscal discipline, and it's also consistent with our values of cutting taxes and rewarding effort



We have made it very clear that we don't have any proposals for tax increases beyond working with other countries to make the multinationals tax regime fairer

