



# WA Budget: the envy of the world... but for how long?

IPAA WA 2023-24 Budget Briefing



Danielle Wood  
CEO, Grattan Institute

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**GRATTAN**  
Institute

## **WA's budget is the envy of the nation (if not the world)**

- Huge help from commodities
- Spending growth has historically restrained but high this year and capital spending well up
- WA's net debt forecast to grow as a share of the economy

## **Economic and fiscal headwinds are coming**

- Activity will slow over the next six months – double whammy for WA as commodity prices come off
- Challenges in delivering a very full infrastructure pipeline

## **Can't ignore the federal dimension**

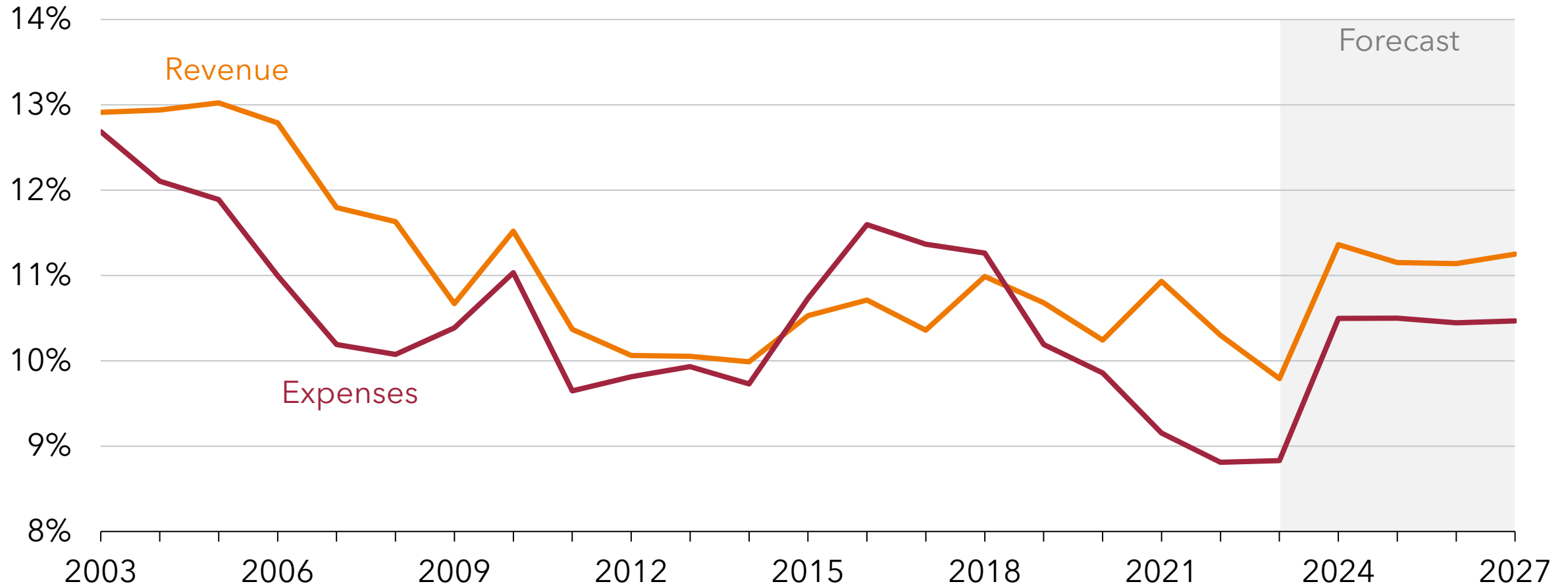
- The Commonwealth budget faces bigger medium-term challenges than might be apparent
- Areas like infrastructure spending will (rightly) be on the front line
- The GST deal is hugely expensive and is raising more heckles around the country

## **Housing will be a growing headache for both levels of government**

- Rental affordability and supply concerns are probably going to get worse before they get better
- Some things on the agenda but need to be bolder

# Another budget surplus for WA, with more expected to come

WA Government revenue and expense, per cent of GSP



Note: Data are for the financial year.

Sources: WA Budget 2023-24, Budget Paper No. 3, Chapter 1, Tables 1 and 2; PBO, National Fiscal Outlook 2022-23, D11; ABS, Australian National Accounts: State Accounts (2021-22).

# WA budget – the envy of the country?

Expected net operating balance in 2022-23, per cent of GSP

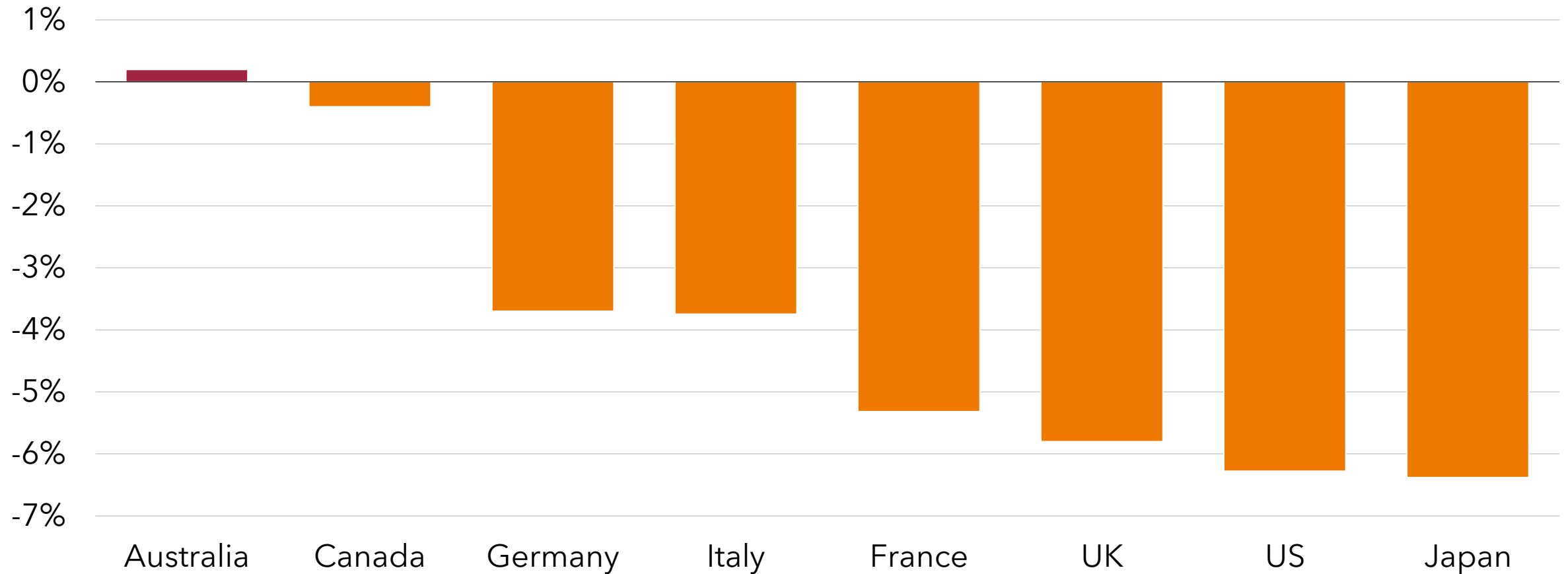


Note: Forecasts from mid-year updates to 2022-23 budgets except for WA, whose estimate is from the 2023-24 WA Budget.

Source: Grattan Institute analysis of state budgets.

# If not the world.....

International comparison of budget balances in 2023 (per cent of GDP)



Notes: For all countries except Australia, data are IMF staff's April 2023 estimates of fiscal balances for all levels of government in calendar year 2023. Australia is Treasury's 2022-23 estimate of the federal government's underlying cash balance.

Source: Commonwealth Budget 2023-24, Budget Paper No. 1, Chart 3.3.

# Debt has peaked lower than many other states

Expected net debt for the general government sector in 2022-23, per cent of GSP

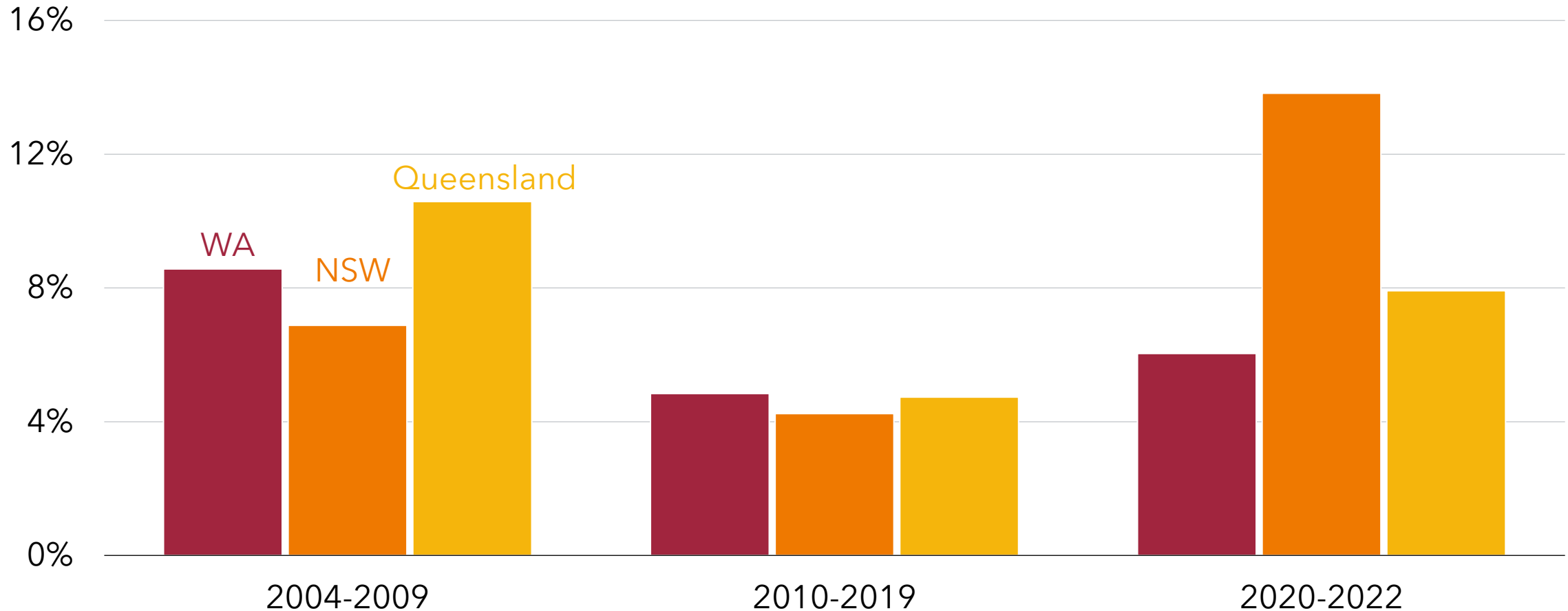


Note: Forecasts from mid-year updates to 2022-23 budgets except for WA, whose estimate is from the 2023-24 WA Budget.

Source: Grattan Institute analysis of state budgets.

# WA's expense growth has been contained historically

Average annual growth in state expenses (nominal)



Note: Simple averages of annual growth rates in nominal expenditure. Data are for the financial year.

Source: Grattan Institute analysis of PBO, 2022-23 National Fiscal Outlook; WA Budget 2023-24, Budget Paper No. 3, Chapter 1, Table 2; NSW Budget 2022-23 Half-Yearly Review, Table 3.1; Queensland Budget 2022-23 Update, Table 3.

# But expense growth is very high this year, and recent decisions have taken the leash off

**Expense growth of 9% in 2022-23** due to a number of one-off factors (including Cyclone Ellie relief and public sector cost-of-living bonus) and increase in recurring spending

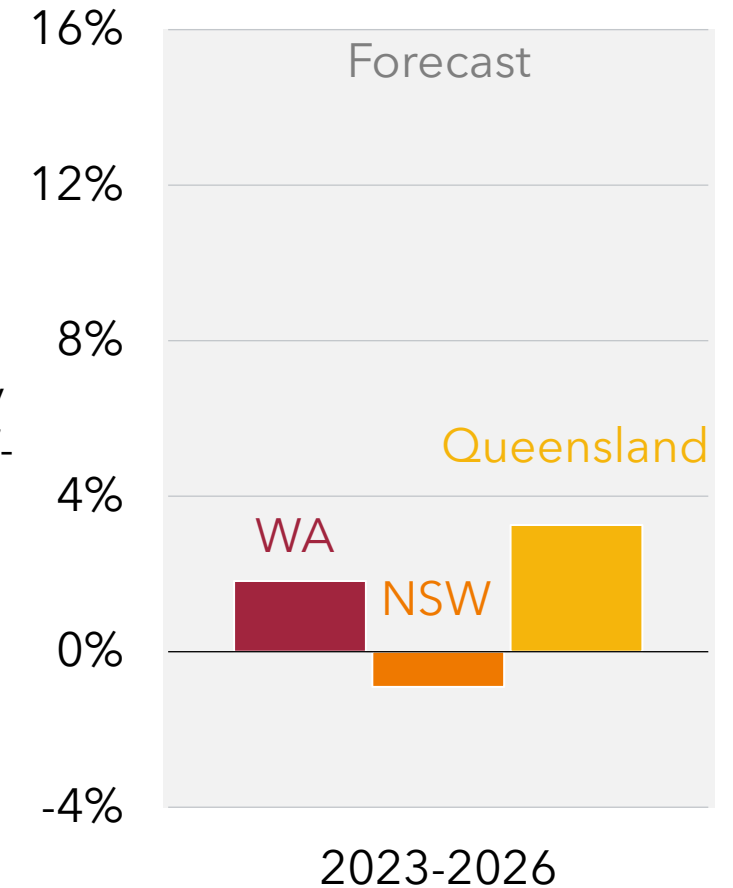
Changes since the mid-year review for 2023-24 to 2025-26 :

- General government **revenue** estimates **up** by **\$4.3 billion** since the Mid-year Review (mainly because of higher royalty income and Commonwealth grant funding)
- General government **expenses** have been revised **up** by **\$6.6 billion** mainly because of higher health spending, additional NDIS participants, and cost-of-living package

**Not ideal** given point in **fiscal and economic cycle**

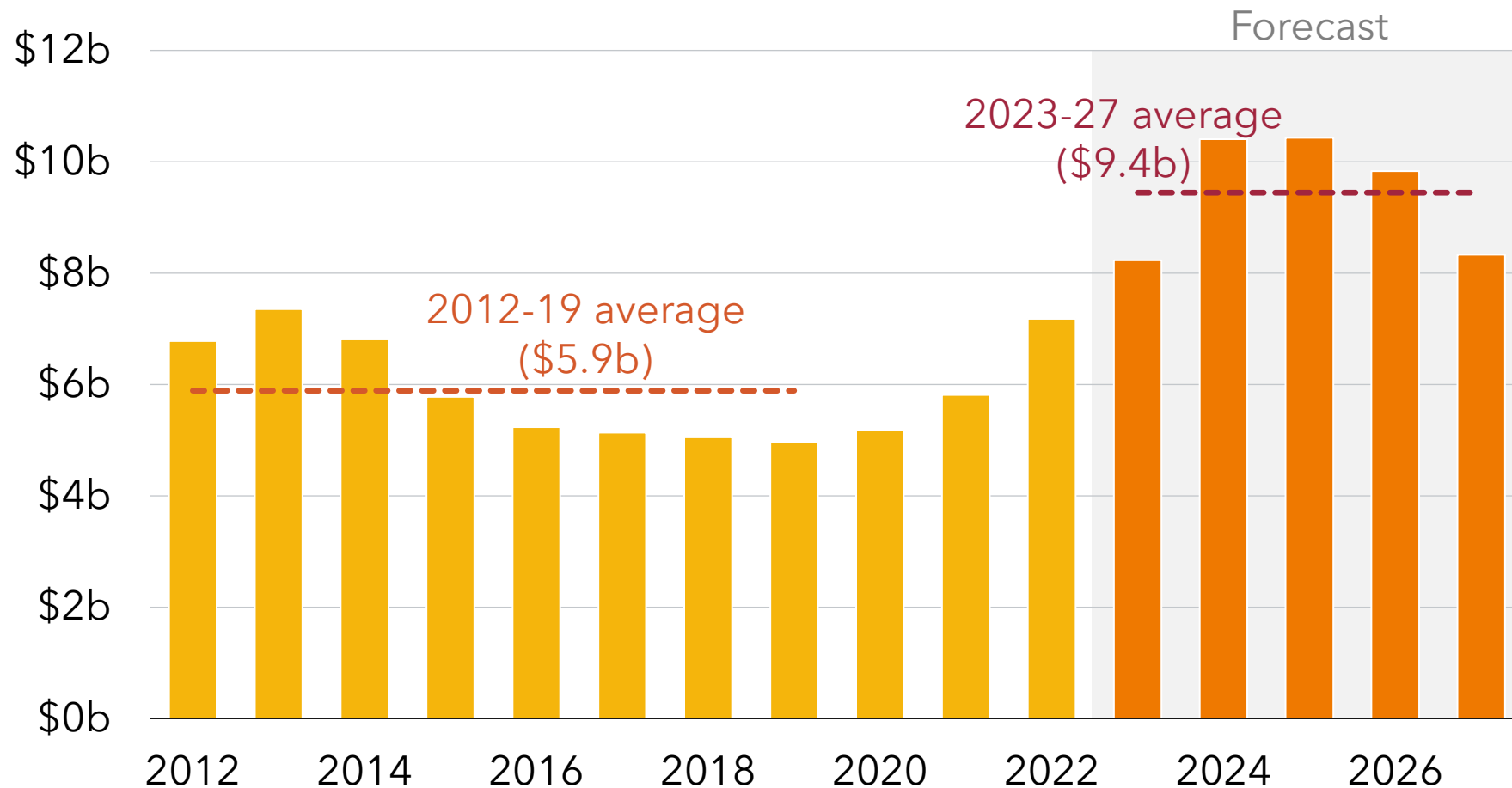
- \$2 billion+ a year new policy decisions adds 0.6% GSP to spending, compounding inflationary pressures
- Much more restraint anticipated in the final two years (see how that holds up in an election campaign)

Average annual growth in state expenses (nominal)



# And capital spend is considerable – comes with future expense implications

## WA Asset Investment Program



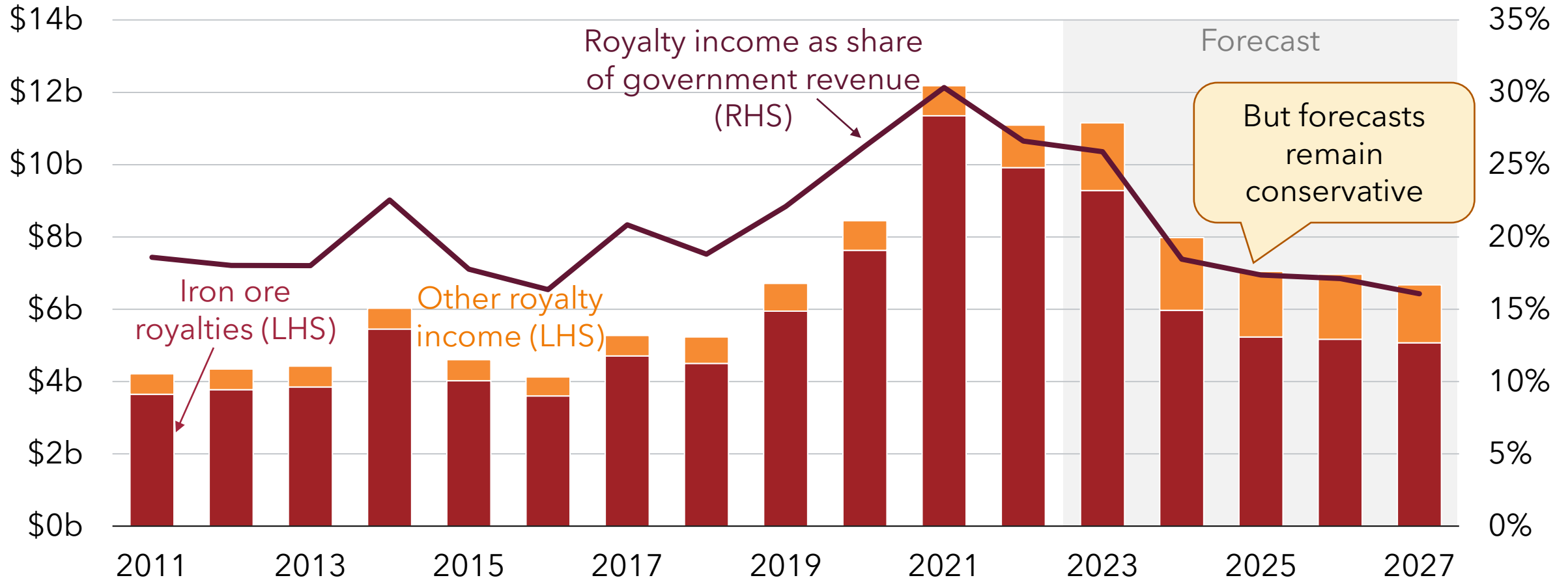
- Historically high capital spend bite in future through depreciation and interest costs but also recurrent spend (e.g. staffing for hospitals)

Note: Figures are for the total public sector, which includes general government and public corporations. Data are for the financial year.

Source: WA Budget 2023-24, Budget Paper No. 3, Chapter 3, Figure 2.

# Royalties have boosted revenues but will shrink as commodity prices soften

Royalty income for WA

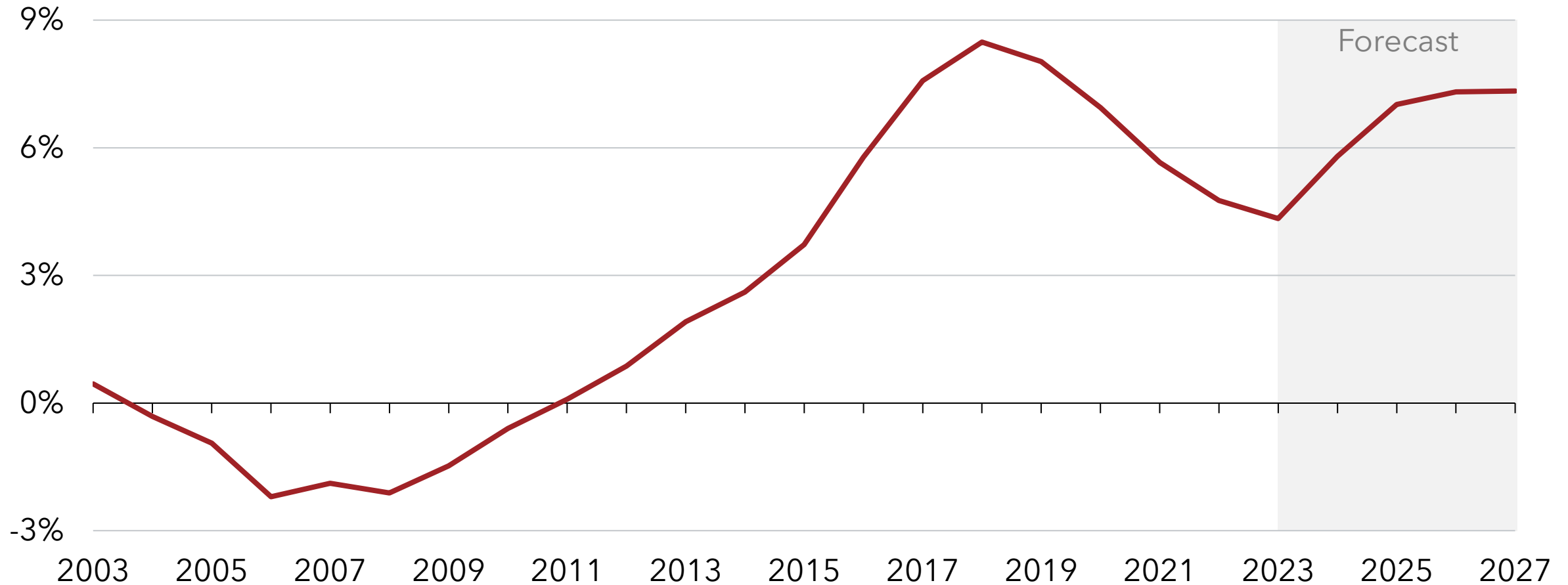


Note: Data are for the financial year.

Source: WA Budget 2023-24, Budget Paper No. 3, Chapter 4, Figure 4.

# Net debt is (slightly) rising when we would expect it to be falling

Net debt of the WA general government sector, per cent of gross state product



Note: Data are for the financial year.

Sources: WA Budget 2023-24, Budget Paper No. 3, Appendix 1, Table 1.2; PBO, National Fiscal Outlook 2022-23, D11; ABS, Australian National Accounts: State Accounts (2021-22).

# Beware of hubris.....



I suspect [other state treasurers] will be green with envy, some of them will look like they've swallowed a bumblebee... All the other states have not run their finances as well as Western Australia, that's the reality and so they need to cut their costs to meet their circumstances.

May 2022

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- Activity will slow over the next six months – double whammy for WA as commodity prices come off
- Challenges in delivering a very full infrastructure pipeline

## **Can't ignore the federal dimension**

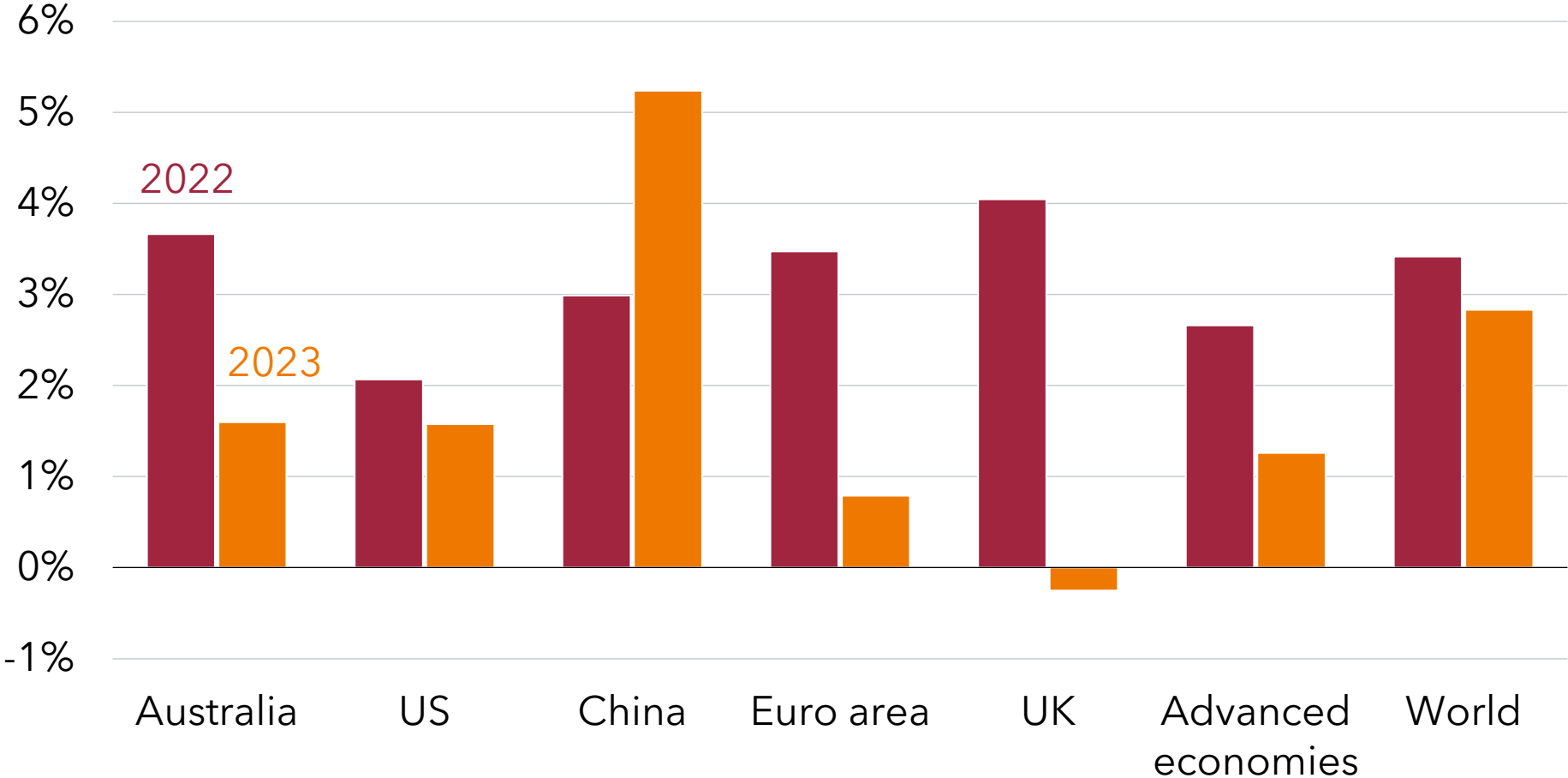
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# Global growth outlook is increasingly anaemic, with multiple headwinds

GDP growth in 2022 and 2023 (IMF forecast)



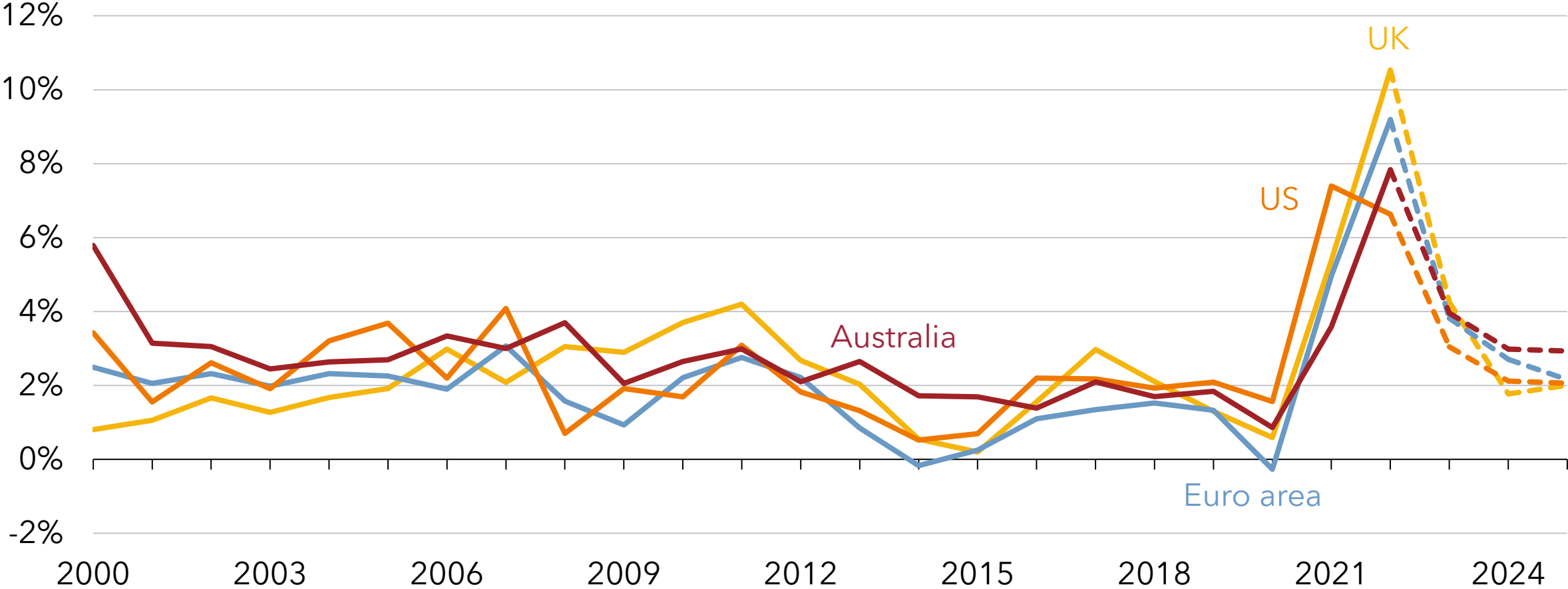
Turbulence is building, and the situation is quite fragile... Inflation is much stickier than anticipated even a few months ago... core inflation has not yet peaked in many countries. More worrisome is that the sharp policy tightening of the past 12 months is starting to have serious side effects for the financial sector... We are therefore **entering a perilous phase during which economic growth remains low by historical standards and financial risks have risen, yet inflation has not yet decisively turned the corner.**

Pierre-Olivier Gourinchas,  
IMF Economic Counsellor  
April 2023

Source: IMF World Economic Outlook (April 2023).

# Inflation is expected to moderate across advanced economies in 2023...

Consumer price inflation at year-end

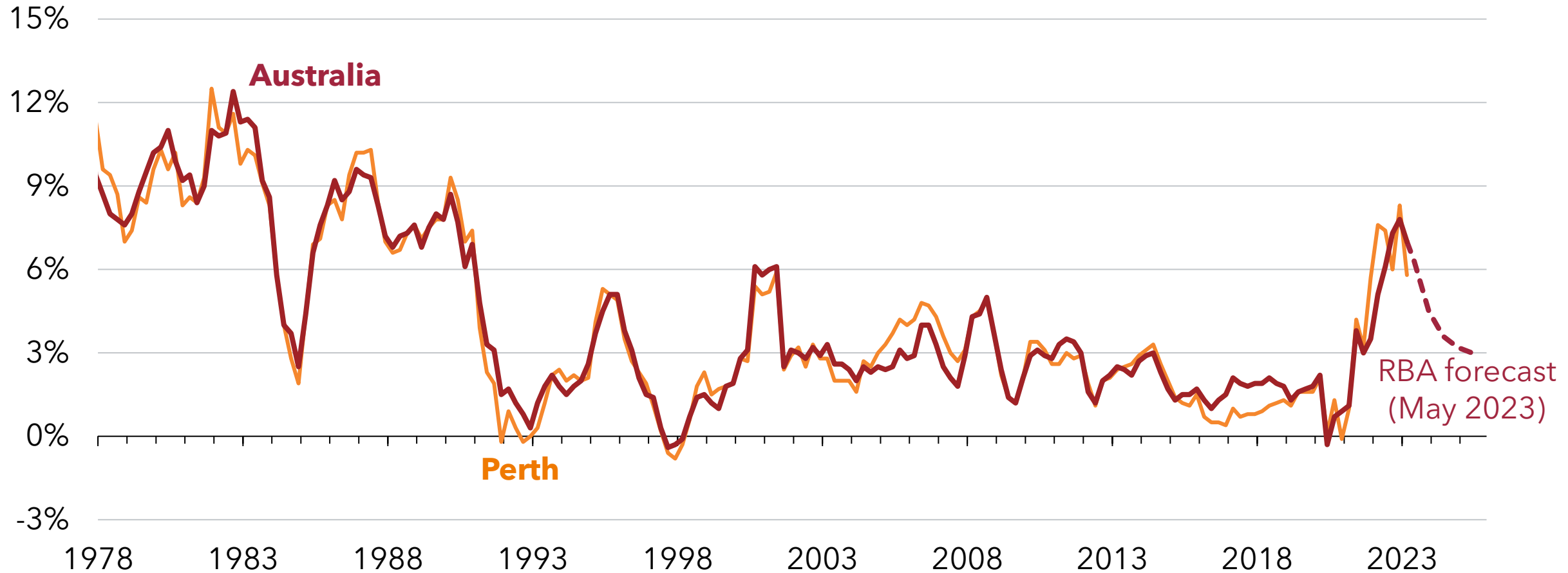


Note: Dashed lines represent the IMF's forecast.

Source: IMF World Economic Outlook (April 2023).

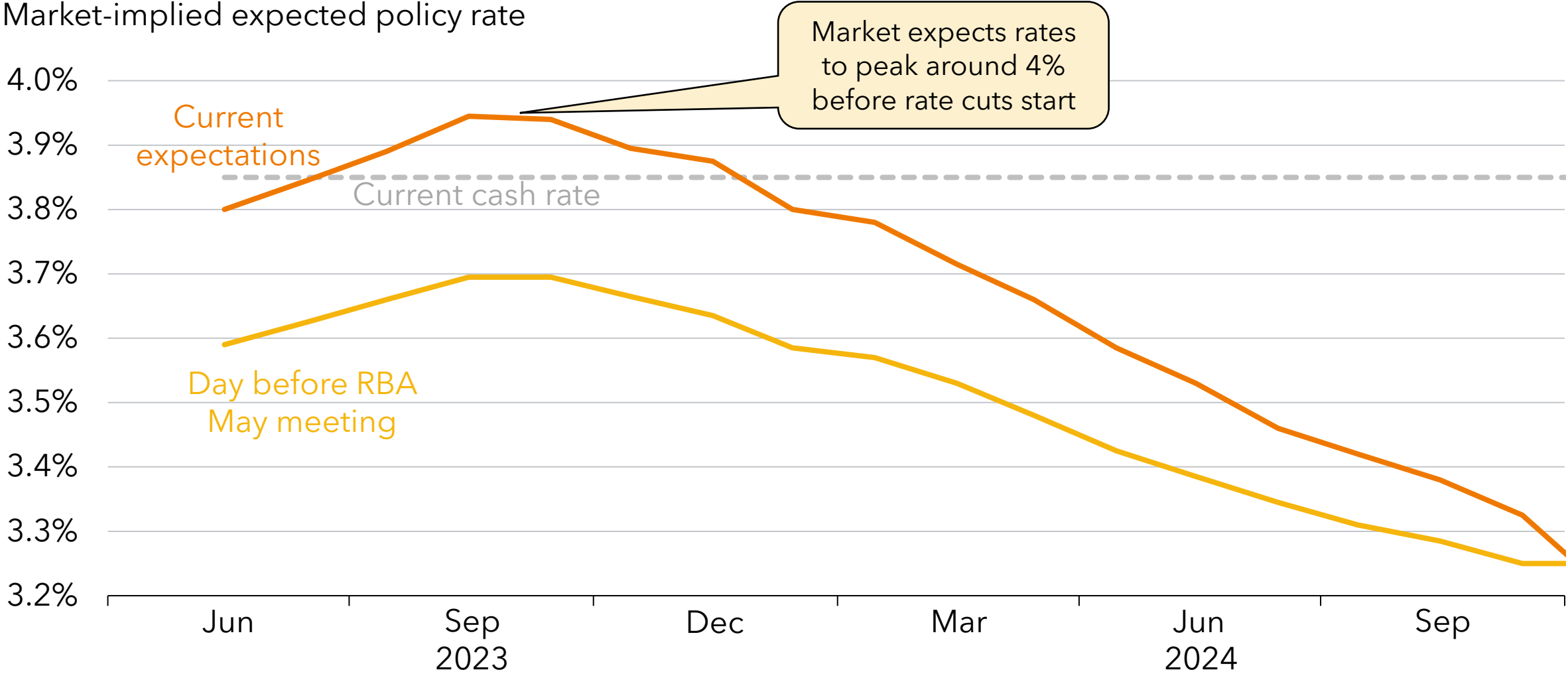
# Inflation in Australia has proved more enduring than hoped but is expected to have peaked

Change in consumer price index from same quarter of previous year



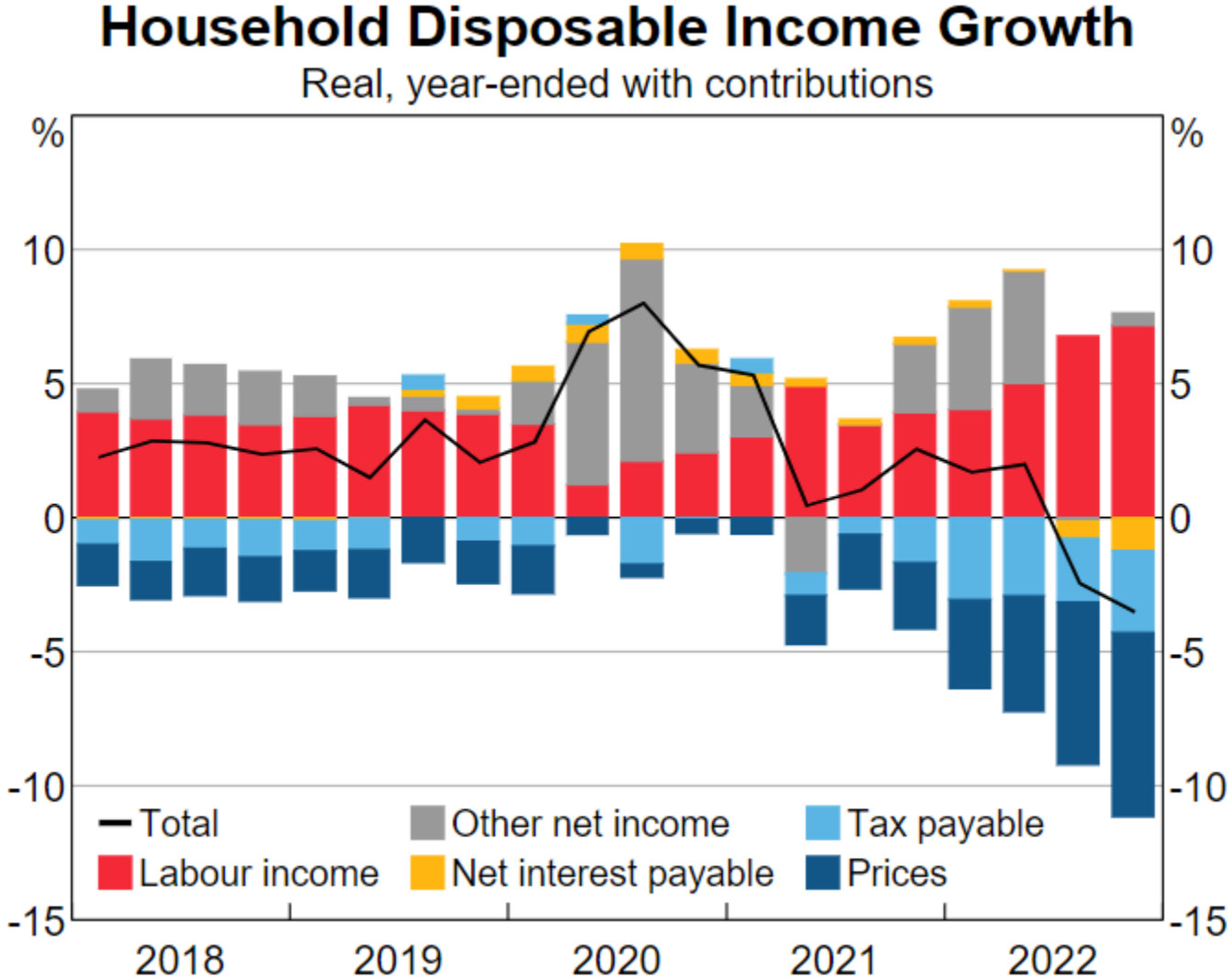
# Expectations of further RBA hikes have tempered despite May surprise

Market-implied expected policy rate



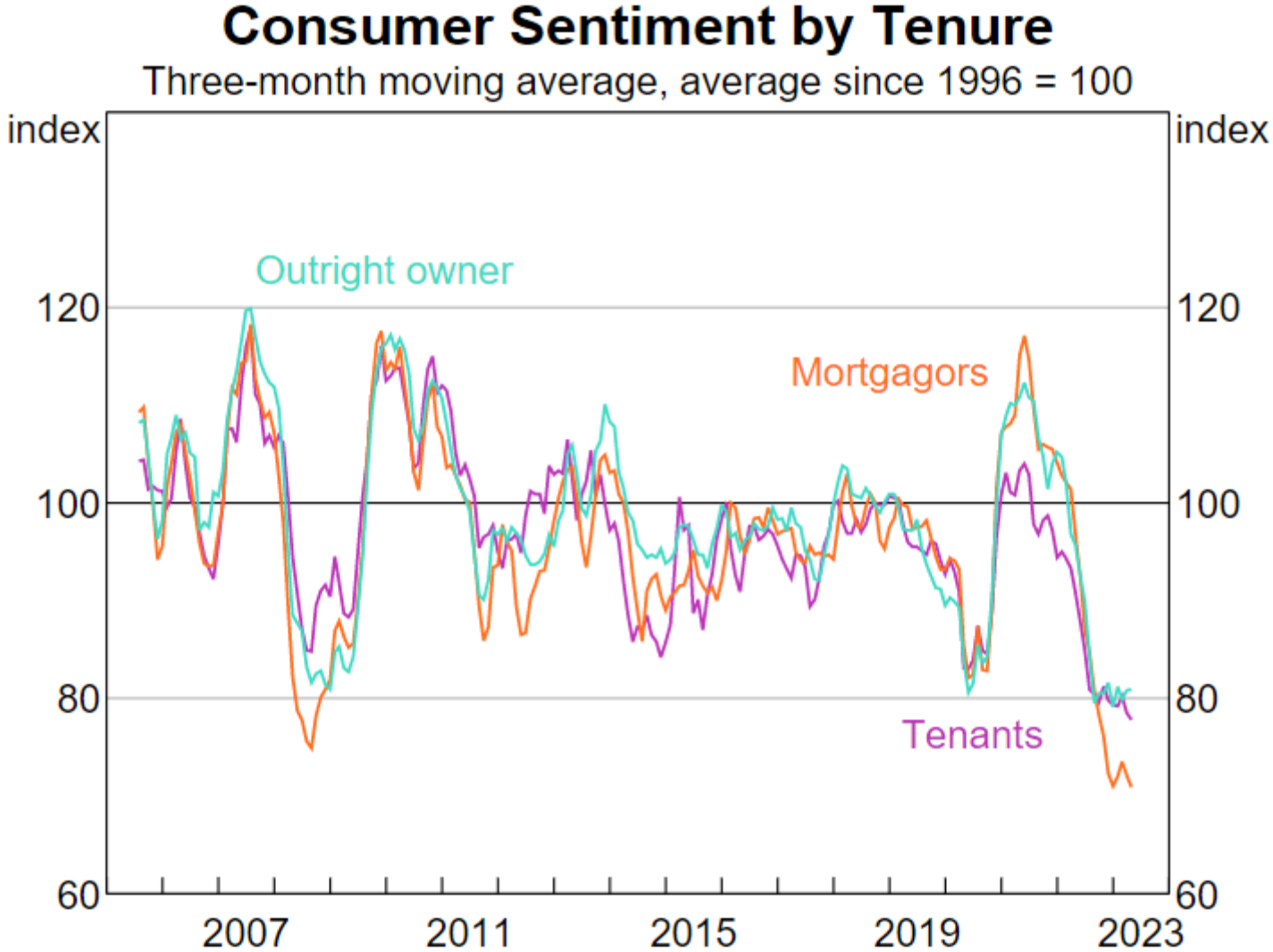
Source: ASX 30-day interbank cash rate futures implied yield curve; 'current' curve as at 17 May 2023.

# Household incomes have gone backwards because of inflation and higher rates



Source: RBA, *Statement on Monetary Policy*, May 2023, Graph 2.13.

# Consumer sentiment is at GFC lows

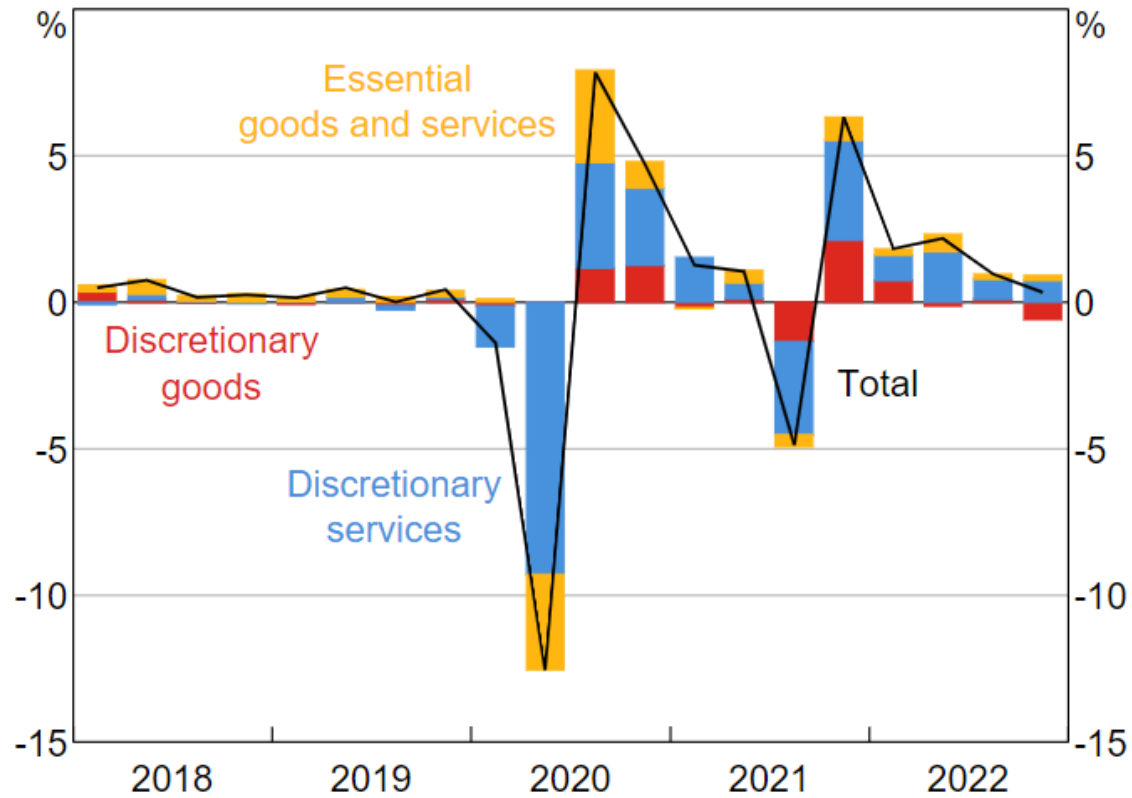


Source: RBA, *Statement on Monetary Policy*, May 2023, Graph 2.15.

# Spending has slowed, especially in goods

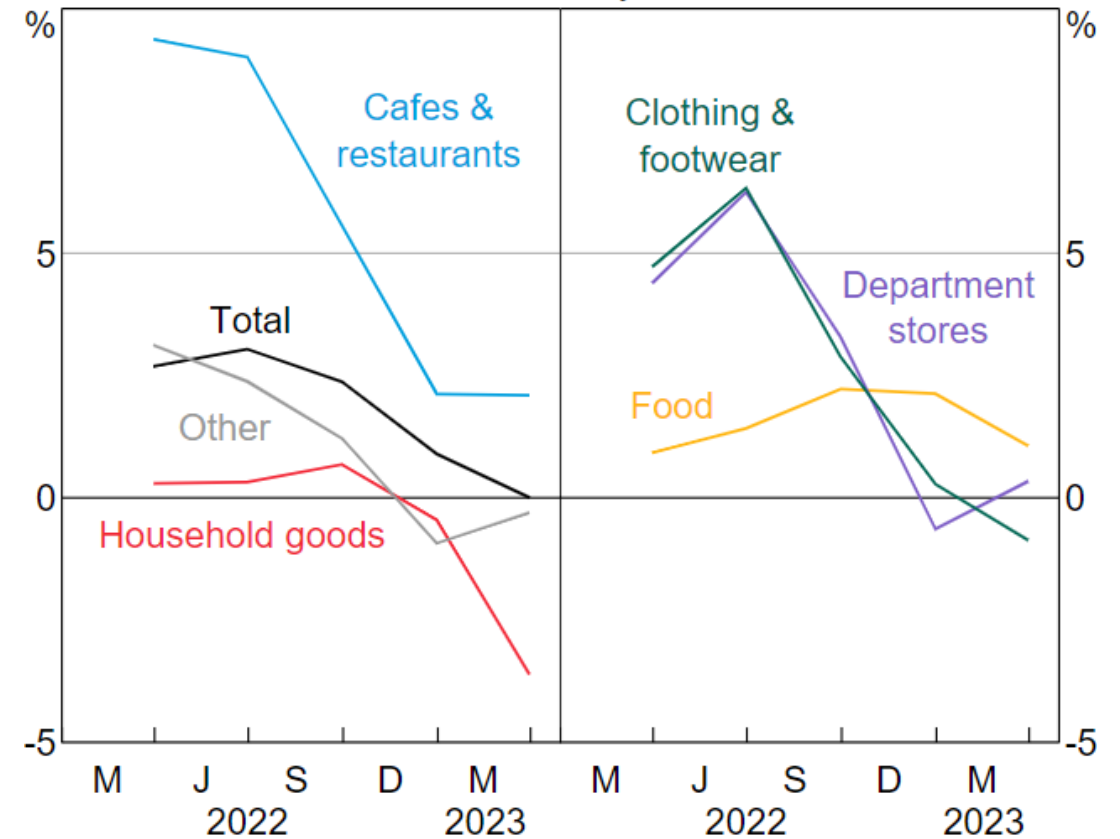
## Household Consumption Growth

Quarterly with contributions



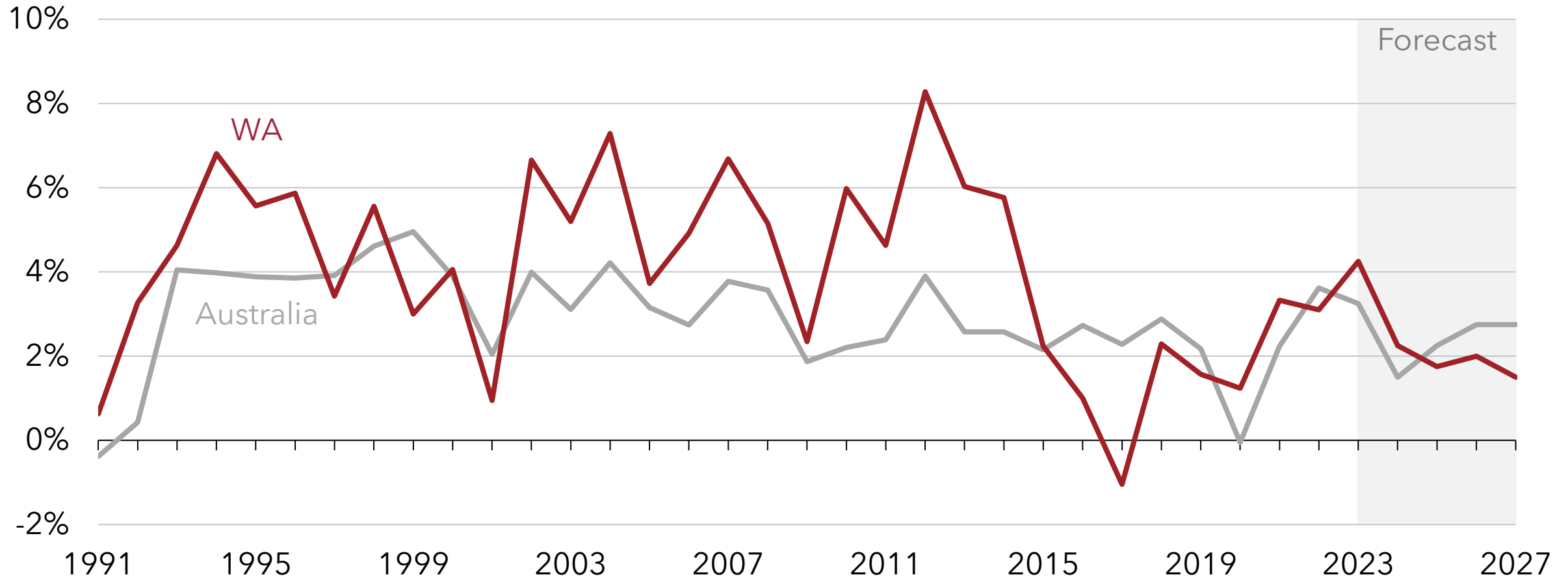
## Growth in Retail Sales Values

Quarterly



# Moderation expected in WA's growth outlook, particularly because of slow down in net exports

Real annual growth in GDP and GSP

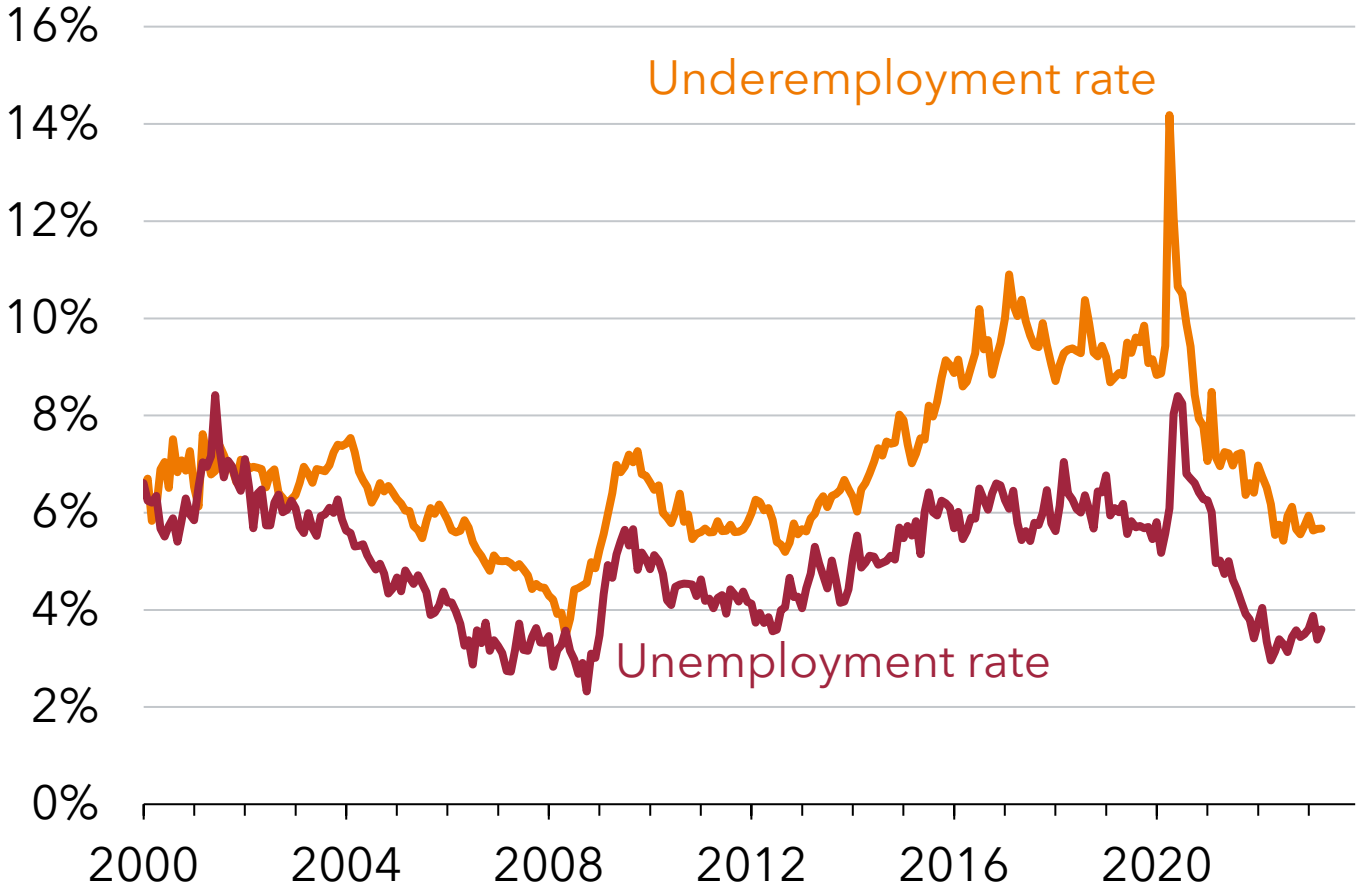


Notes: Data are for the financial year. Forecasts are from the 2023-24 budgets of the Commonwealth and WA Government.

Sources: WA Budget 2023-24, Budget Paper No. 3, Chapter 2, Table 1; Commonwealth Budget 2023-24, Budget Paper No. 1, Table 1.1; ABS, Australian National Accounts: State Accounts (2021-22).

# Infrastructure pipeline challenges: the labour market remains very tight

Labour underutilisation rates in WA



Source: ABS, Labour Force (April 2023).

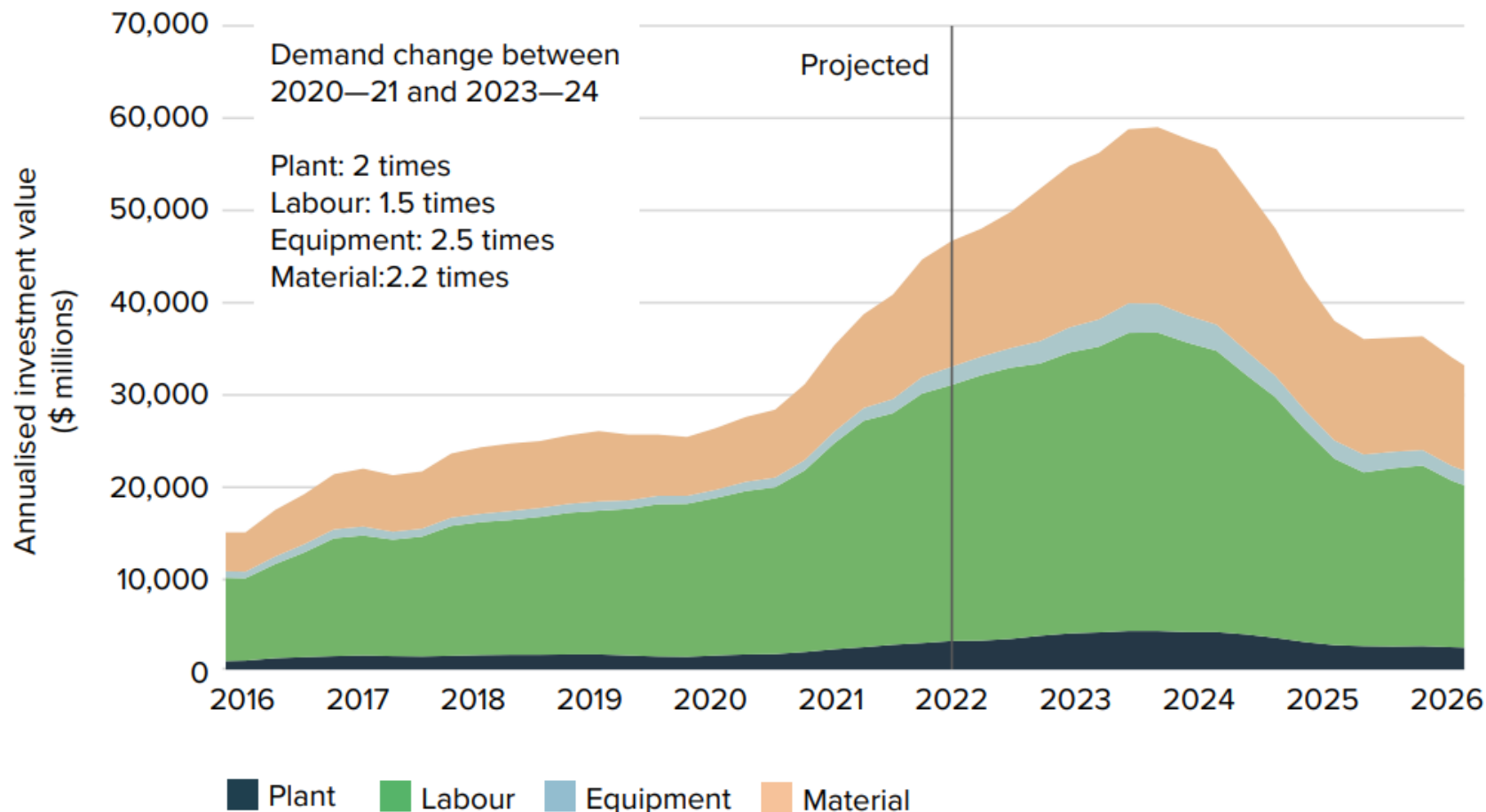
There are extremely limited short-term opportunities to address [the labour shortage]. Demand-side solutions are the only realistic short-term solution, including data-driven, proactive demand management via intelligent pipeline sequencing.

Significant action is needed both in public infrastructure planning and workforce training and supply to ensure Australia can meet its infrastructure ambitions.

Infrastructure Australia,  
December 2022

# Much more consideration needed as to how to coordinate scarce resources across sectors

## Major public infrastructure expenditure profile



The market is arguably at capacity, so project slippage is now expected: The pressure the industry is experiencing to supply labour and materials in step with demand creates unprecedented uncertainty on project outcomes, and the opportunities to adapt and pivot will take time to realise. As such, it is no longer a question of if a project will slip, but more likely when, by how long and at what cost.

Infrastructure Australia,  
December 2022

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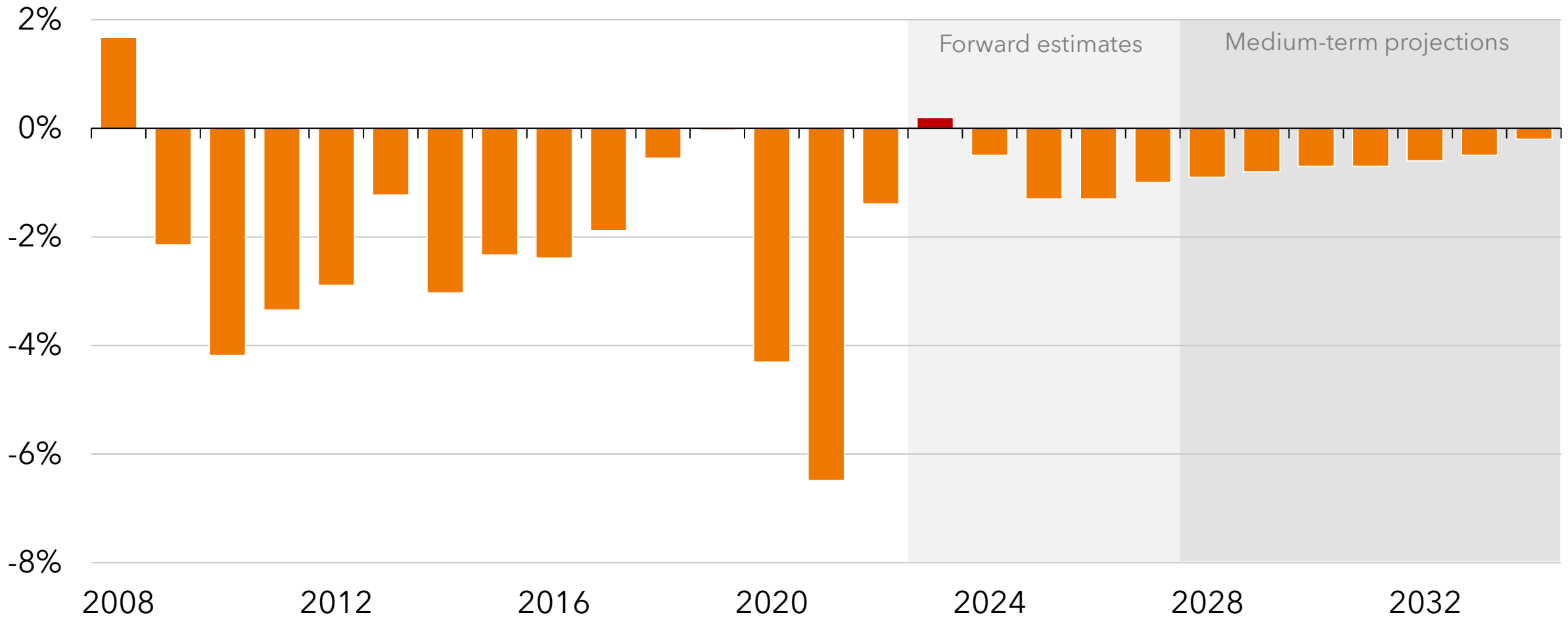
- Rental affordability and supply concerns are probably going to get worse before they get better
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# Commonwealth had some good news of its own



# But forecast to be a once only... although medium-term outlook is pretty rosy

Underlying cash balance, per cent of GDP

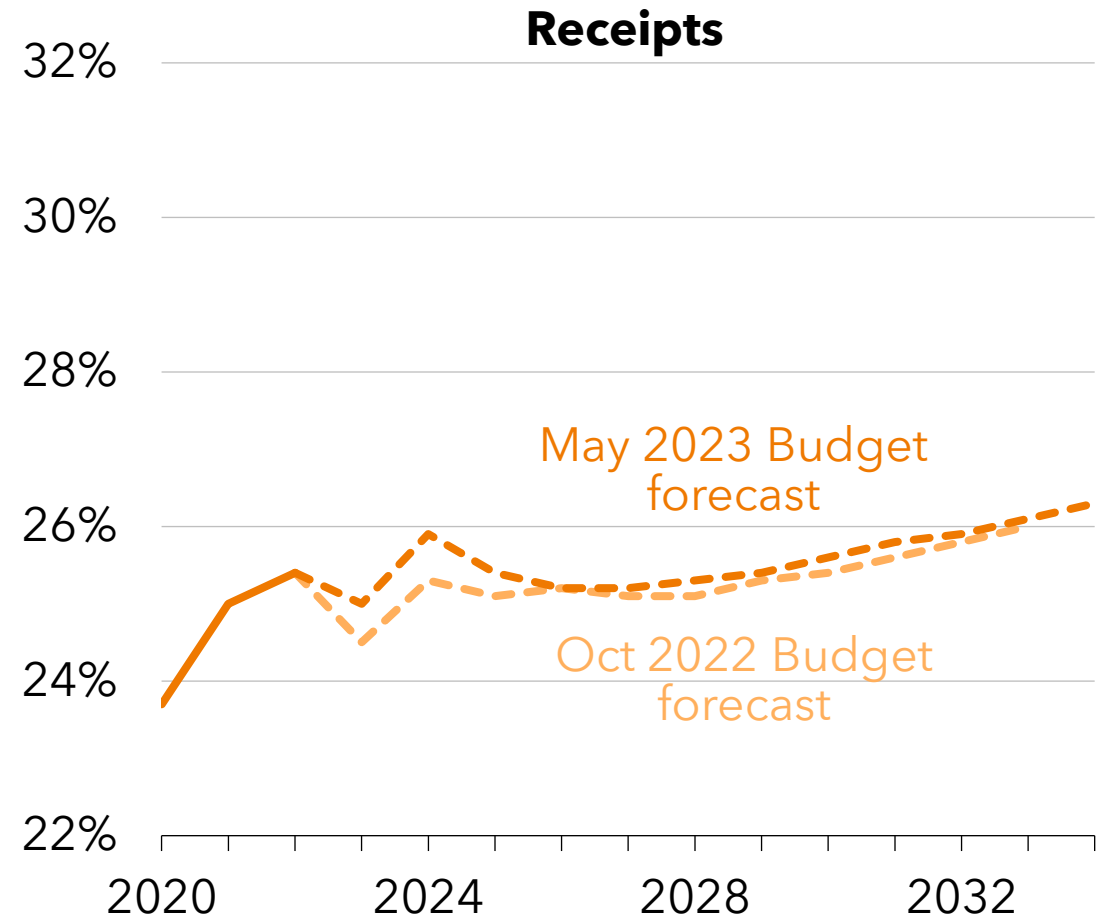
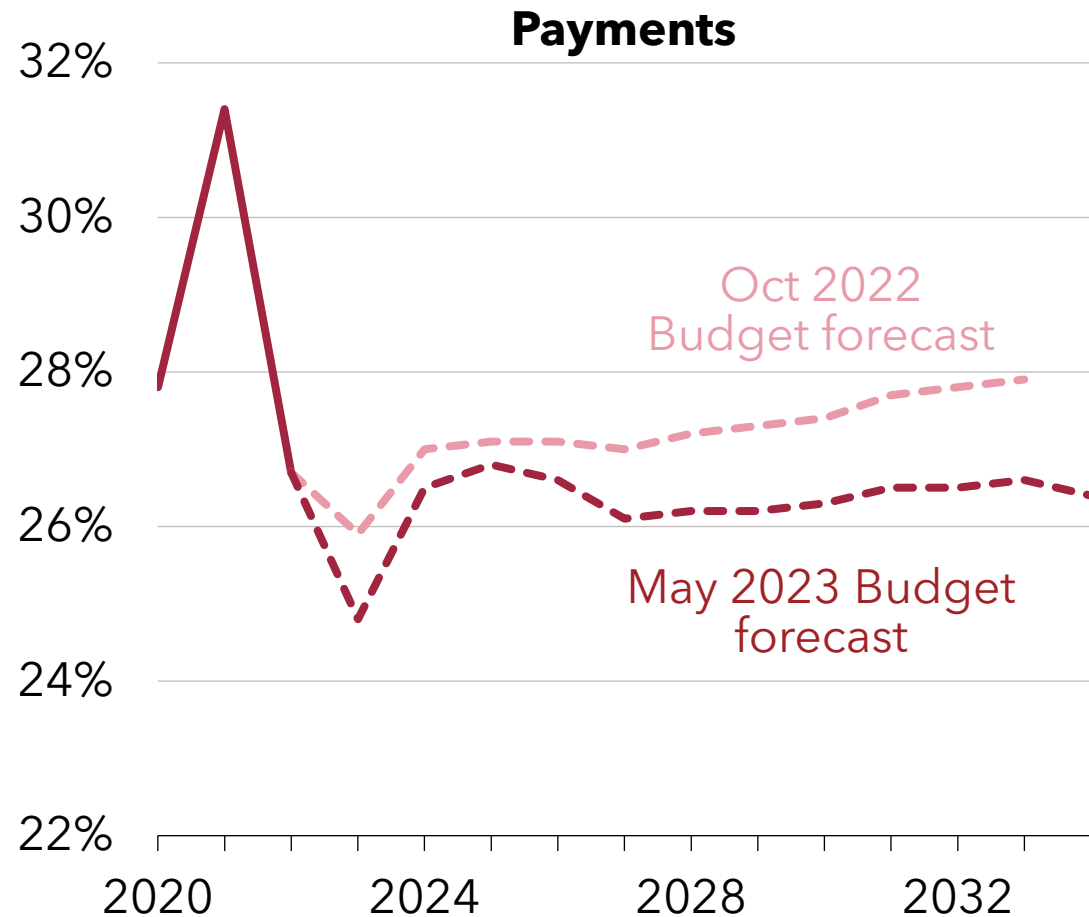


Note: Data are for the financial year.

Source: Budget 2023-24, Budget Paper No. 1, Chart 3.4.

# BUT relies on much stronger payments restraint

Total payments and receipts projected compared with October 2022 Budget, per cent of GDP

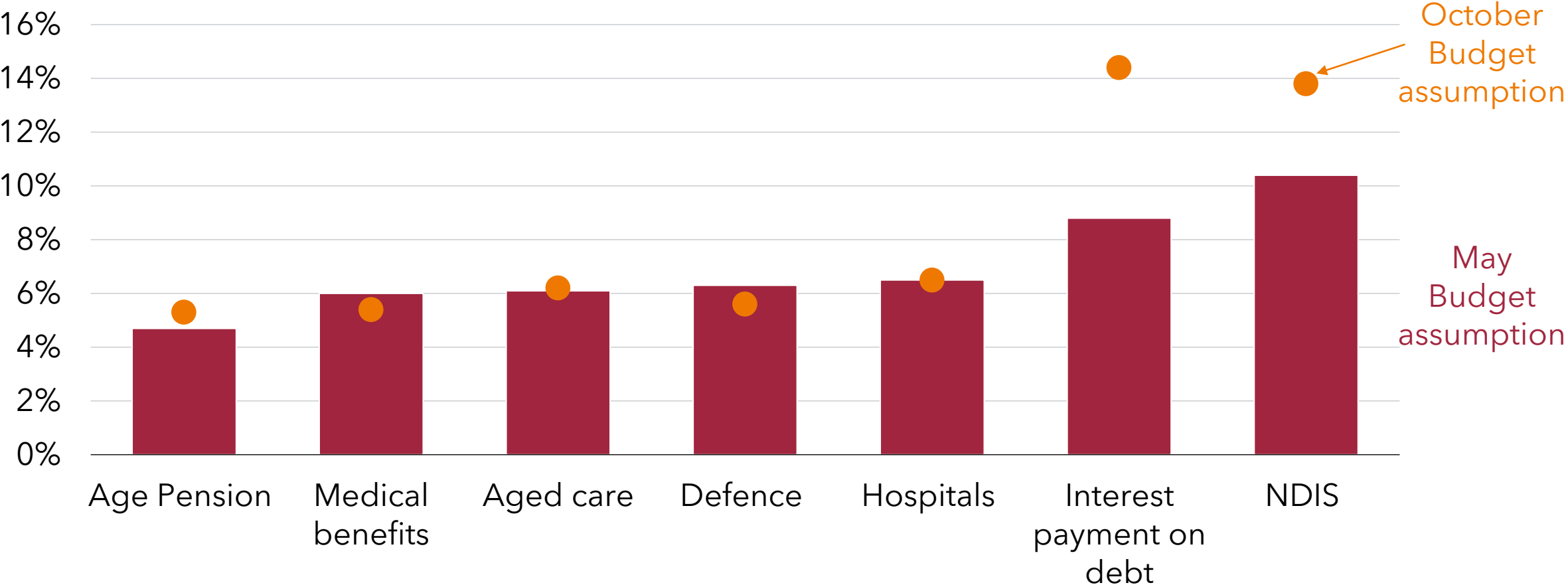


Note: Data are for the financial year.

Sources: Budget 2023-24, Budget Paper No. 1, Charts 3.9 and 3.10.

# Restraint in the 'speedy 7' is part reality, part optimism

Average annual growth in major payments 2023-24 to 2033-34, per cent

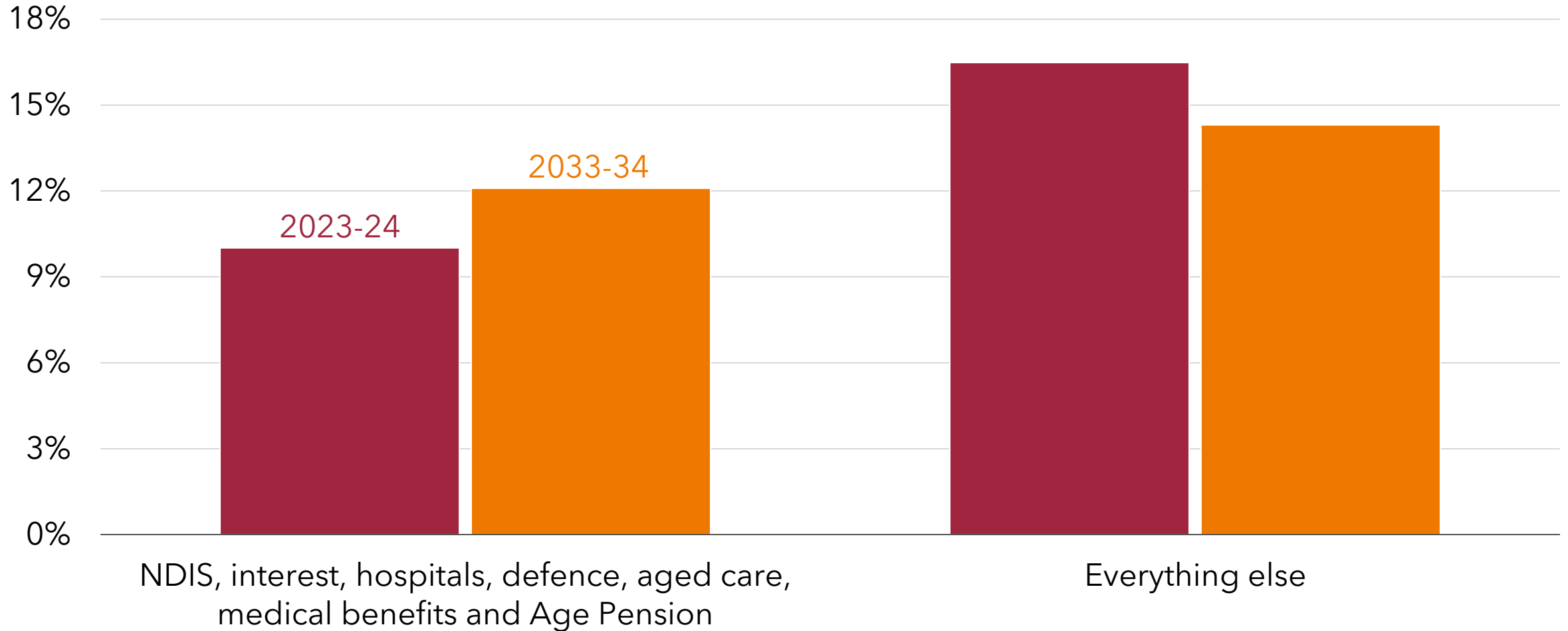


Notes: Growth rates from the October 2022-23 Budget are for 2022-23 to 2032-33. NDIS refers to the Commonwealth's contribution to payments for NDIS participant supports.

Source: Budget 2023-24, Budget Paper No. 1, Chart 3.8.

# It relies on strong spending restraint across all other areas

Spending in selected categories, per cent of GDP



# Medium-term challenges aren't going away

## Why does it matter for WA?

Number of Commonwealth Agreements up for renegotiation in near future - risks that Commonwealth will squeeze funding

### **Commonwealth-State Agreements up for renegotiation in 2023-24**

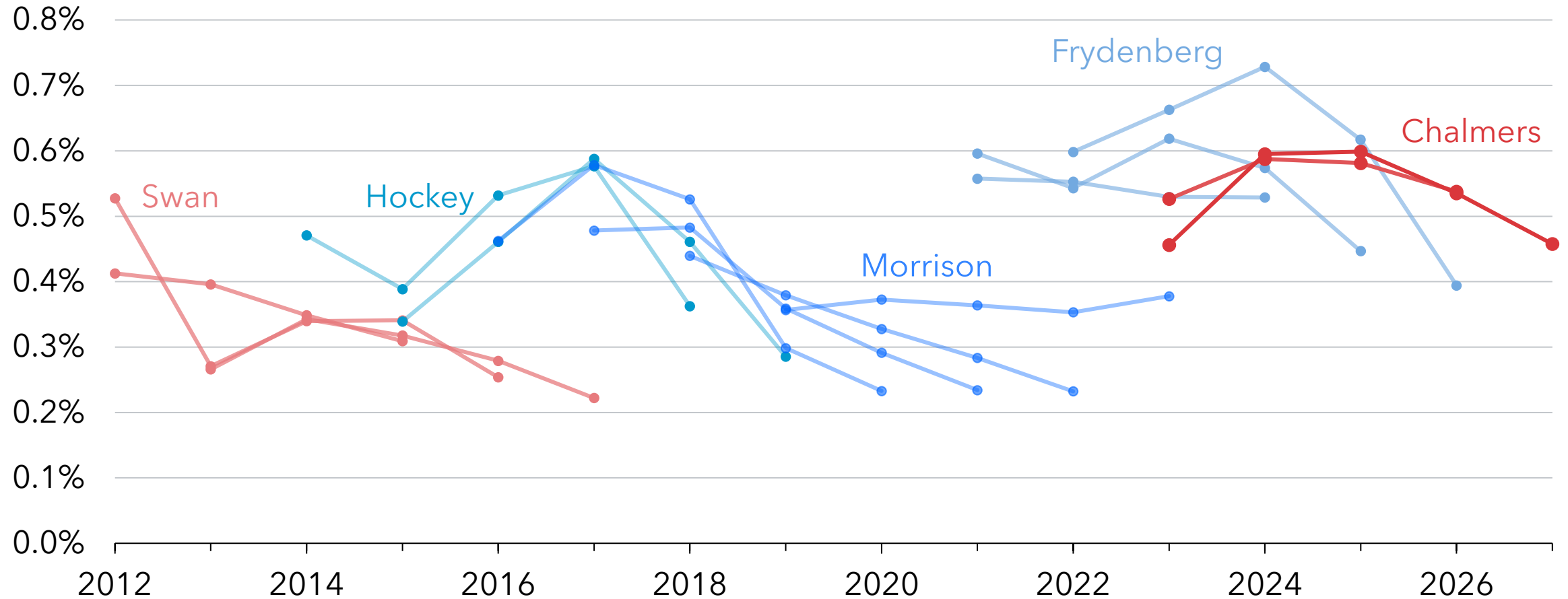
- National Skills and Workforce Development Agreement
- National School Reform Agreement
- National Disability Insurance Scheme
- National Housing and Homelessness Agreement
- Natural Disaster Recovery Funding Arrangements

### **In 2024-25**

- National Health Reform Agreement

# No impact on transport infrastructure spending yet but....

Estimated transport infrastructure spend, per cent of GDP



Note: Each budget includes spending estimates spanning the previous financial year to the financial year in three years' time. Data are for the financial year.

Source: Grattan Institute analysis of Commonwealth budget papers.

# Rightly under review

- The Federal Government has announced a 90 day independent review of its infrastructure investment spending
- Focussed on removing congestion in pipeline - examining priorities and costs for projects not yet underway
- Addressing explosion of smaller projects (160 federal commitments to projects with a budget of \$5 million or less)

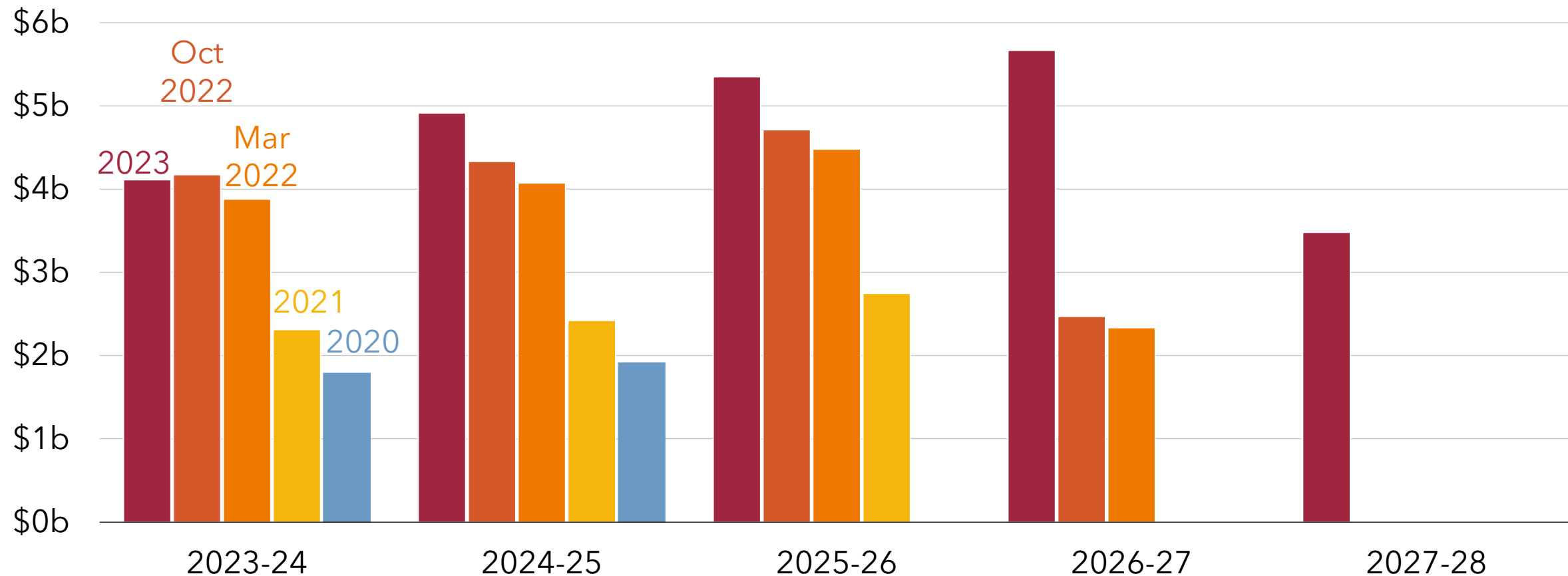


"It is time to clean up the mess left by the Liberals and Nationals clogging the pipeline with 'press release projects' - announced but unable to be delivered. "This review will put confidence back into the investment pipeline, benefitting the states and territories and the communities we all serve."

# Why does it matter for WA?

## WA's GST deal is costing federal government a lot

Expected horizontal fiscal equalisation transition payments in last five budgets



# Beauty is in the eye of the beholder...

NSW gets back more than they put in, whereas we only get back 75c for every dollar we put in.

March 2023



Anything less than the current 70 cent GST floor - rising to 75 cents in 2024-25 - would be contemptible and offensive... It's a red line that should not be crossed by any future Federal Government.

Other States will attempt to erode Western Australia's share of GST in upcoming reviews. We cannot let that happen. We will not let that happen.

May 2023



So you want to keep... the sweetheart deal for WA, then don't think that we are paying for it, because we are not. We are just not.

You need to keep compensating us for that... it's just fairness. It's just the right thing to do. We will not be worse off so that WA can be better off, we will not stand for that.

March 2023

[The deal] prejudiced every other state and territory in the country... When states like Victoria and NSW have had their budgets hit hard by the pandemic, giving WA more GST this year was totally unjustifiable.

Dec 2021



We're entitled to more - and that is an implicit criticism of the current arrangement.

It's all up for negotiation in the next few years, and I'm not going to take a backward step from the perspective of taxpayers in [NSW].

March 2023

# The ultimate question is: do you believe in comparable services across states or not?



*....all Australians, regardless of the state in which they live, should be able to receive comparable levels of health, education, justice, welfare, public housing and other services.*

*The Australian Government helps put state governments in a position to provide their residents with comparable services by distributing revenue from the Goods and Services Tax (GST) pool according to need.*

*It is the job of the Commonwealth Grants Commission to advise the Australian Government on how the GST pool should be distributed to ensure each state can provide comparable services, if they all make a similar effort to raise revenue from their own taxes.*

# WA has much more revenue raising capability than other states

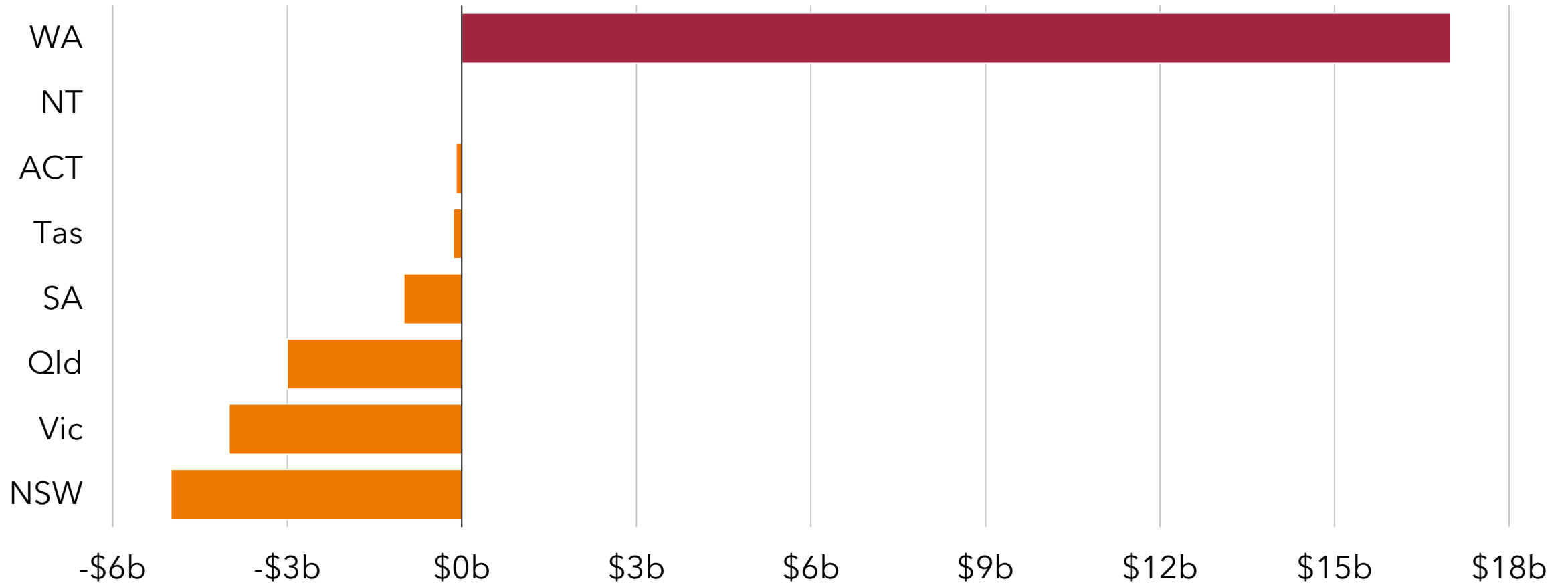
Gross state product per capita in June 2022 (in 2023 dollars)



Sources: ABS, Australian National Accounts: State Accounts (2021-22); ABS, Consumer Price Index (March quarter 2023).

# A return to that principle would significantly reduce WA's take

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



# Other states will get louder as 2026-27 gets closer

## 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.

### 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.

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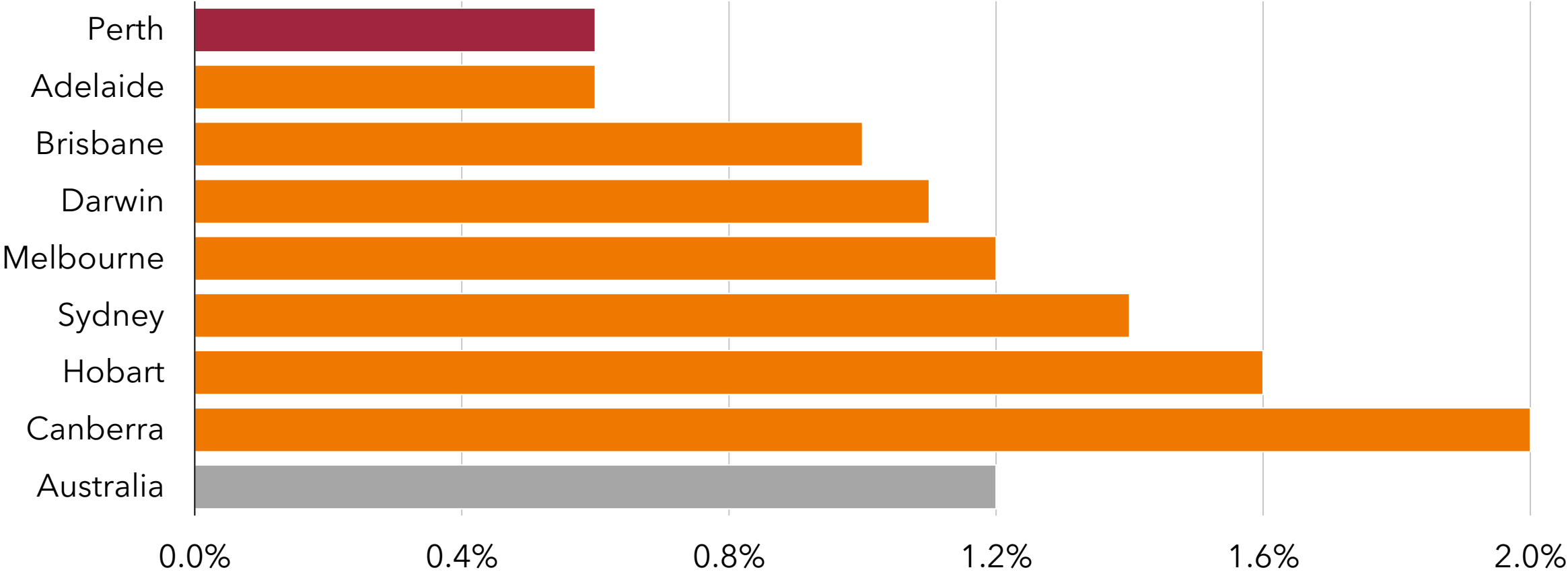
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## **Housing will be a growing headache for both levels of government**

- Rental affordability and supply concerns are probably going to get worse before they get better
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# Housing is biting: Australian cities are now facing a genuine rental crisis

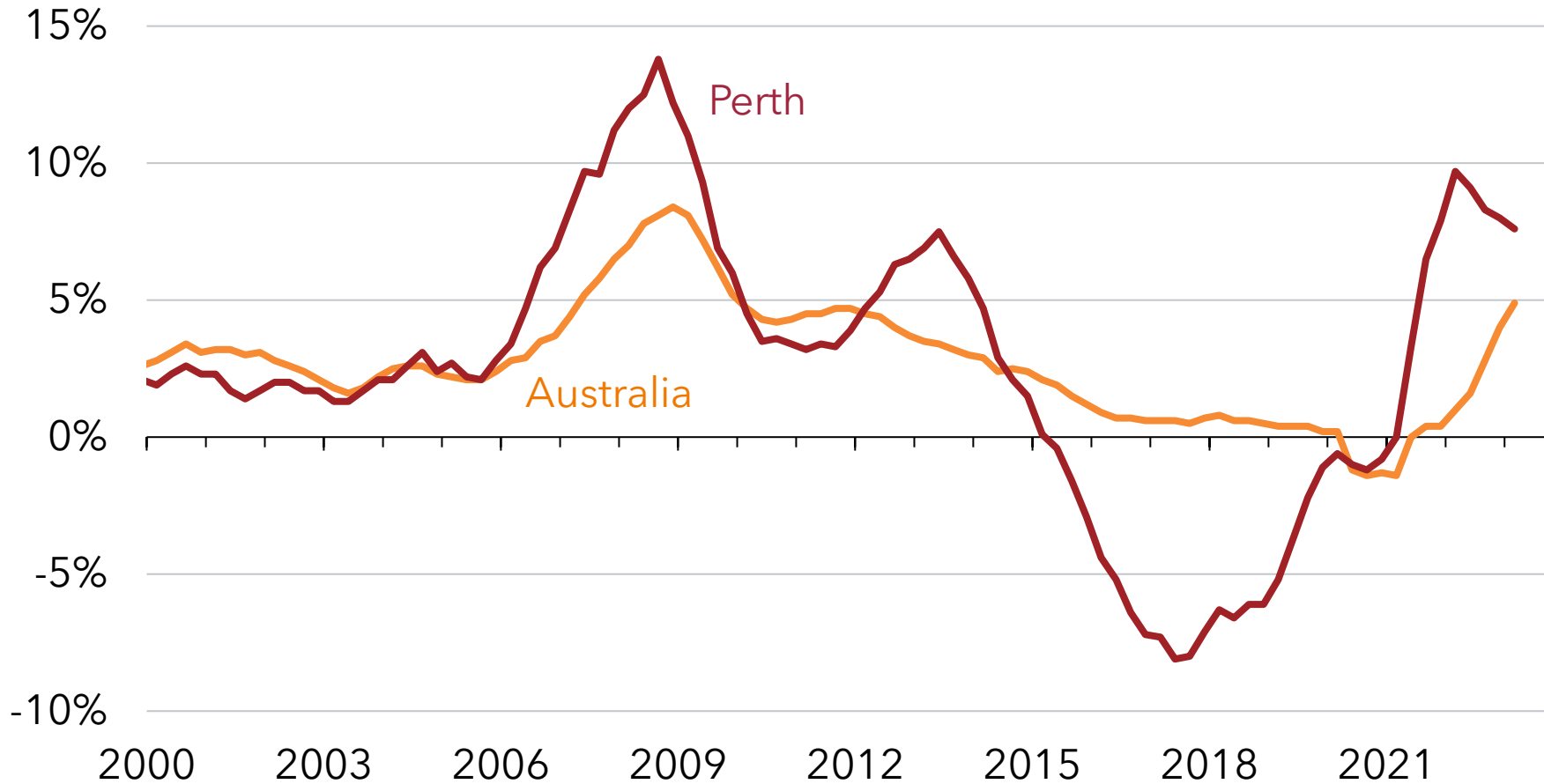
Private rental vacancy rate, April 2023



Source: SQM Research

# Rental pressures are going to get worse before they get better

Rental price growth, annual

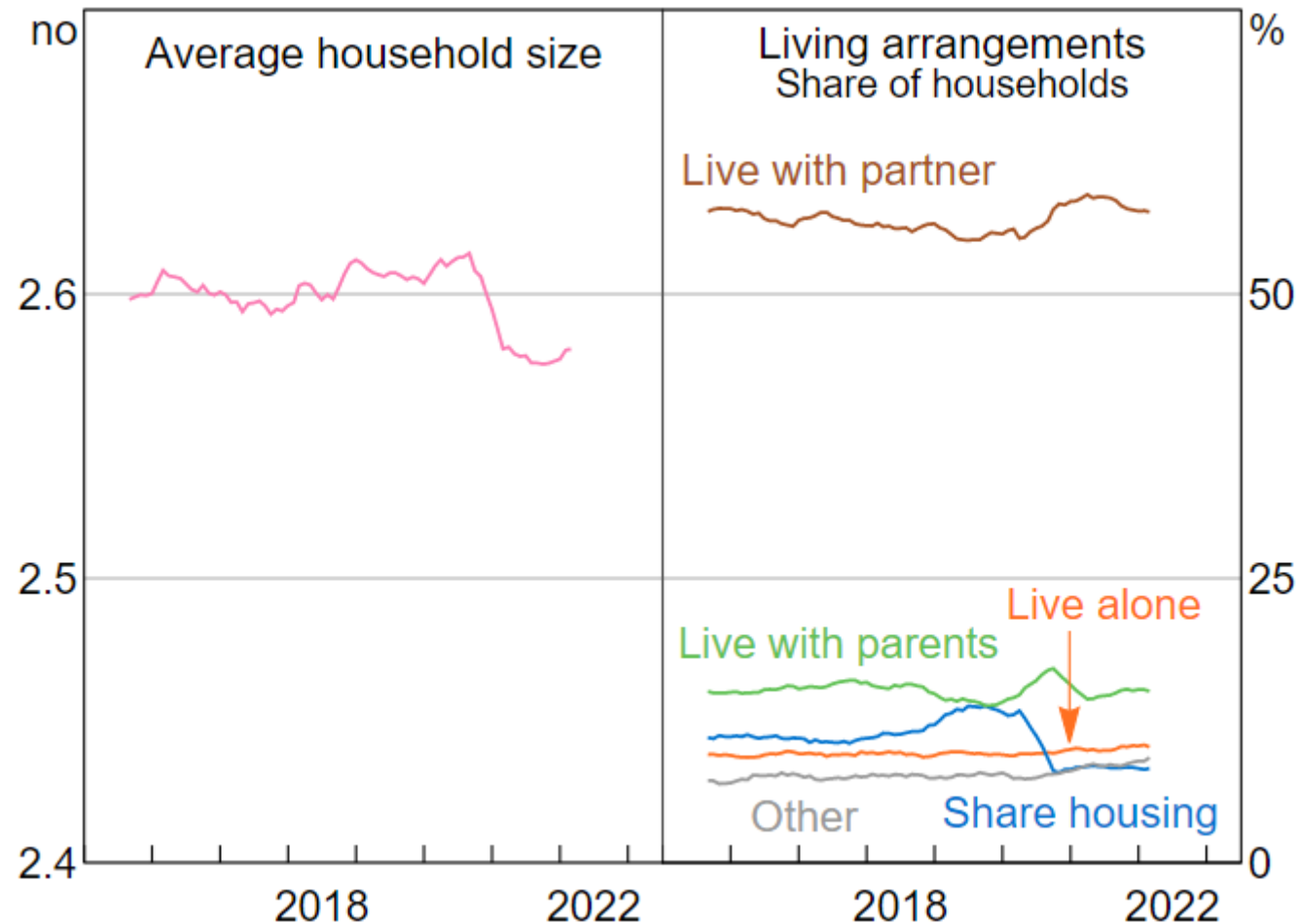


- Actual rent paid by new tenants grew by over 14 per cent over the year to February 2023
- That is feeding through into the rents paid by all renters (measured by CPI rent subcomponent)
- For example, US rental inflation is currently 8.1% y.o.y

# What's happening? COVID resulted in greater demands for housing space

## Household dynamics

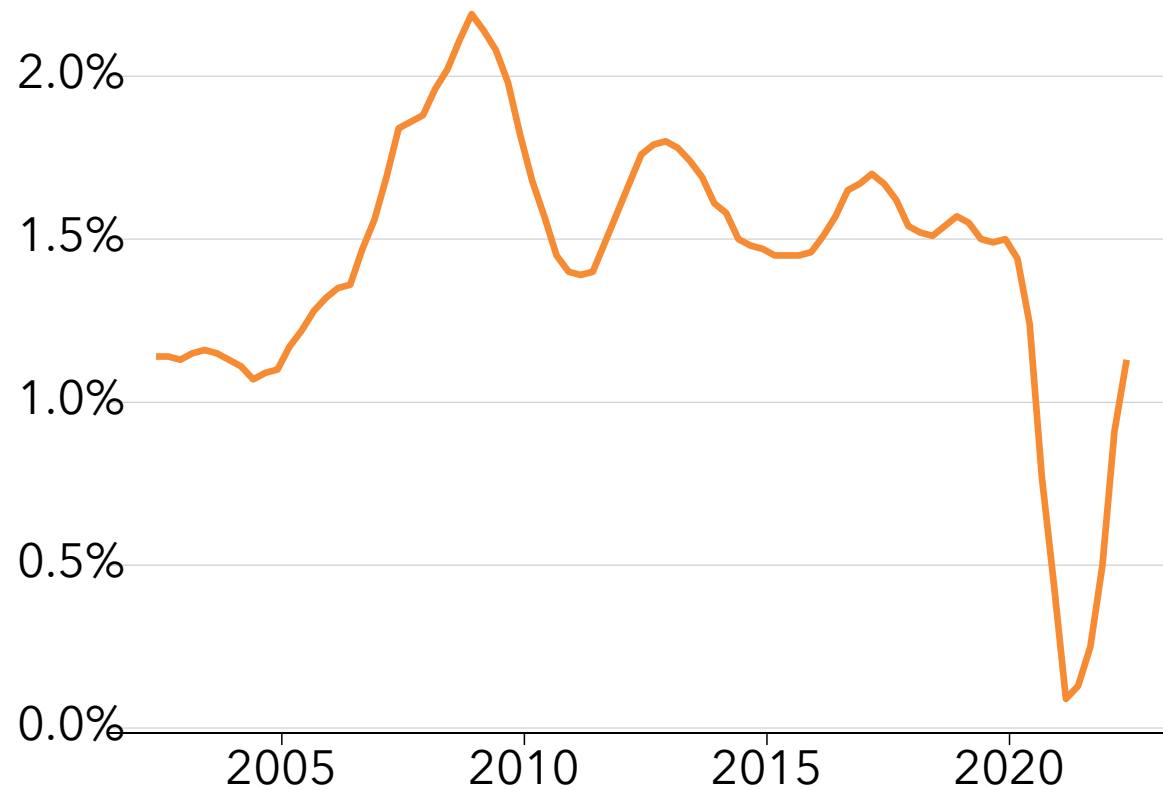
Average household size fell



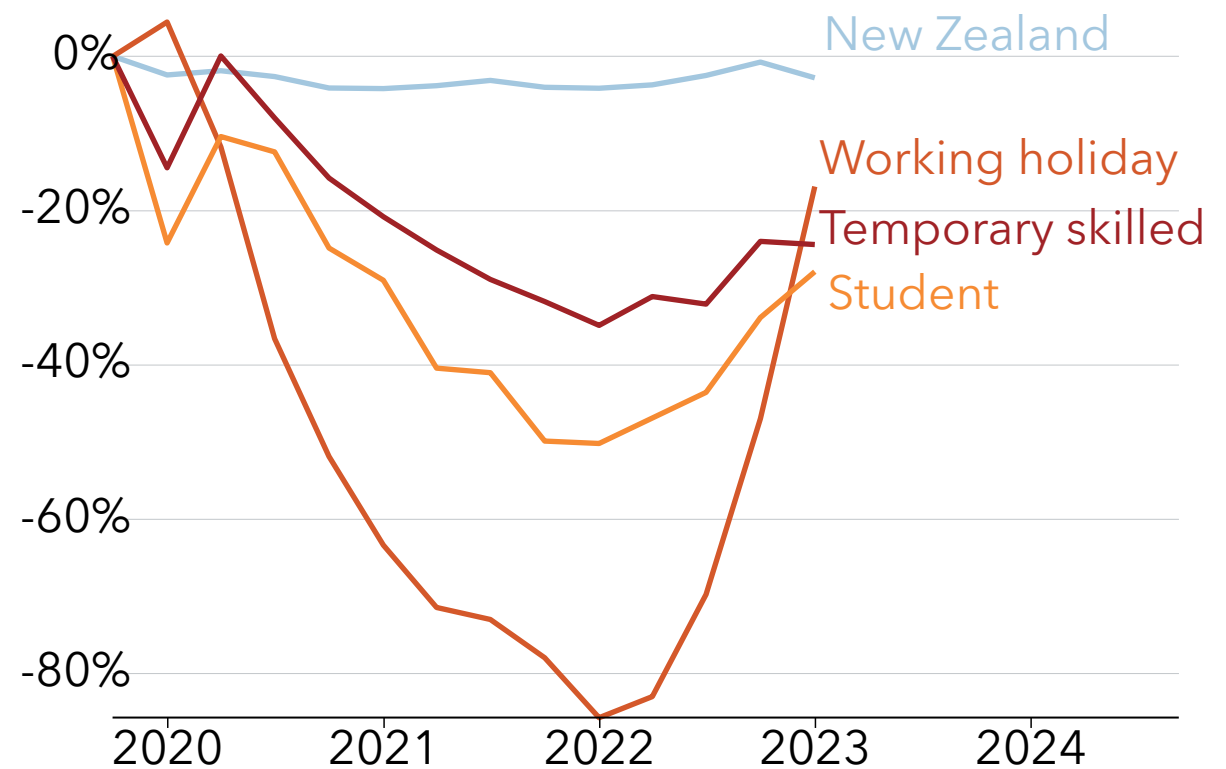
Share-houses dissolved and people moved in with partners and parents

# Exacerbated by higher demand as borders have reopened....

## Annual population change



## Change in temporary visa-holders in Australia since 2019 Q3



# More social housing investment is welcome but also need to boost market supply

## WA social housing commitment

**\$450 million** top-up to the Social Housing Investment Fund, increasing the Government's commitment to deliver an additional **4,000 social houses by 2026-27**

## Federal social housing commitment

Government is seeking to legislate for a **\$10 billion** Social Housing Future Fund

- **\$500m** from fund earnings directed to social and affordable housing each year
- Expected to build **30,000 social housing** properties in the **first five years**

Other **housing initiatives** in this budget:

- Funding to facilitate an urban infill development project in Bentley and infill sewerage to unlock development of sites across Perth,
- extending the existing off-the-plan transfer duty rebate to 30 June 2025, and
- increasing the Regional Development Assistance Program to boost regional housing and land supply

Ultimately, need to add **more supply** in inner and middle ring suburbs with low density

- Propose the **federal government payments to states tied to housing targets** (akin to the National Competition Policy Payments of the 1990s)
- Reduces the political cost to state governments of making hard decisions

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