

Tasmania's economy: lots of progress but lots still to do

Presentation to the
Economic Society of Australia's
Tasmanian Economic Forum

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ANZ Bank

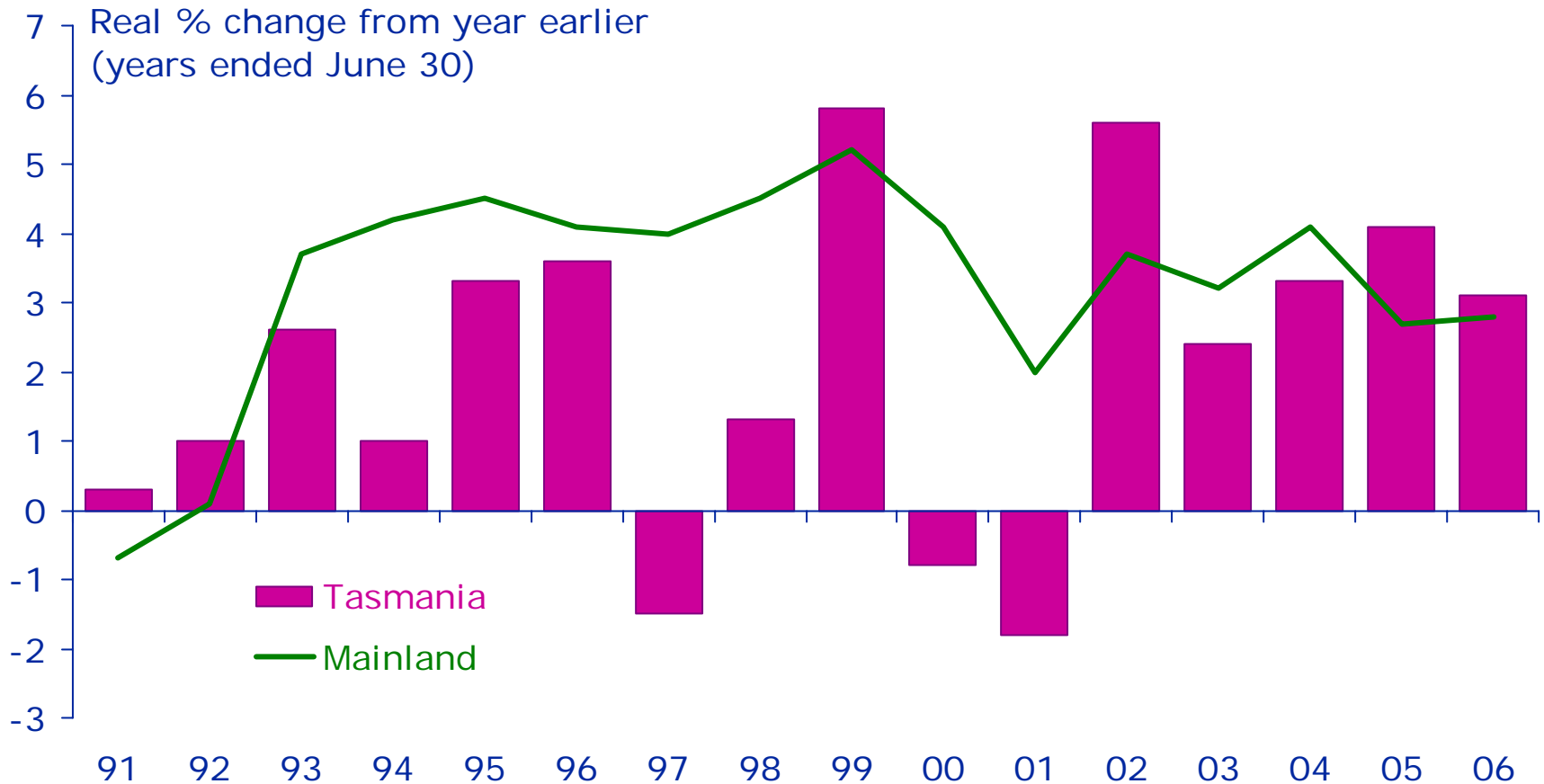
**Tasmanian Function
& Conference Centre**
Hobart
8th December 2006

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Tasmania's economy has grown faster than that of the mainland for two consecutive years

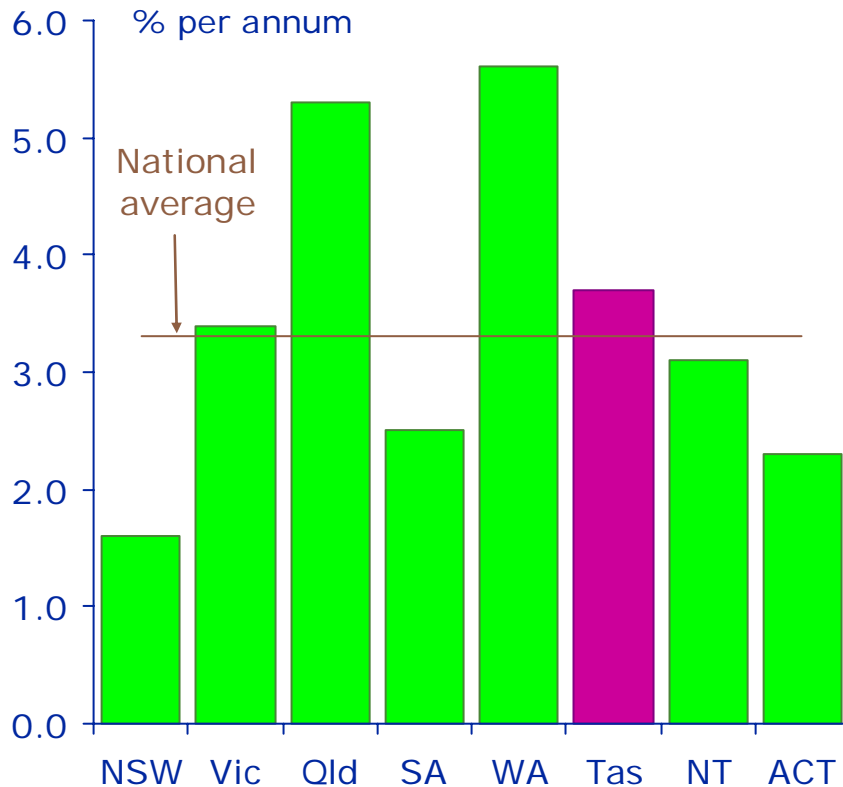
Growth in real gross State product



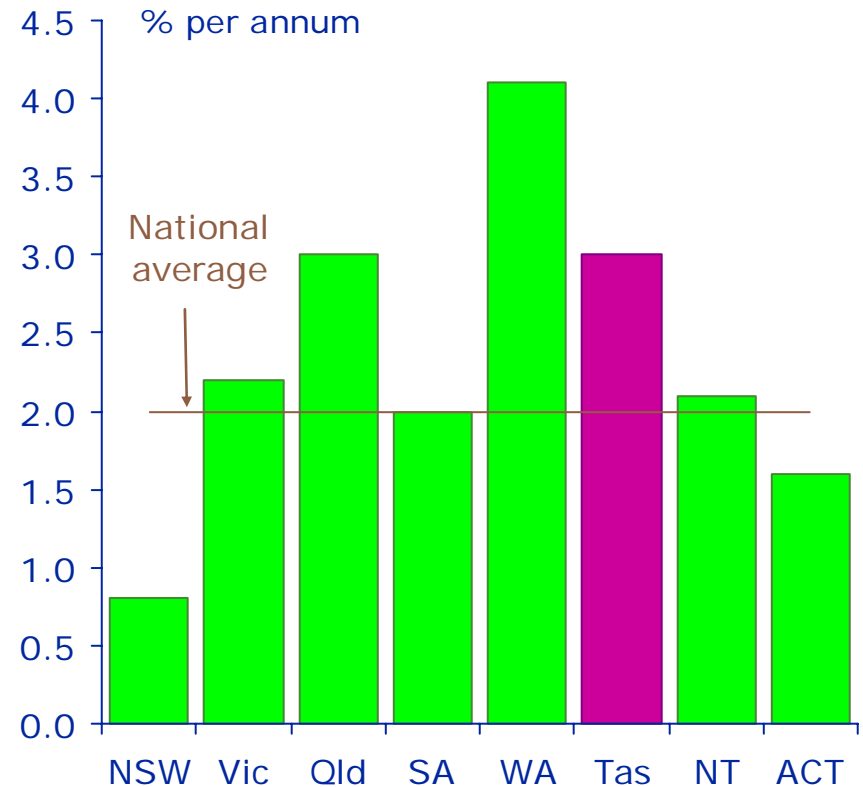
Sources: ABS State Accounts (5220.0) 2005-06;
Economics@ANZ

Tasmania has again grown faster than the other 'non-resource' States

Real GSP growth five years to 2005-06



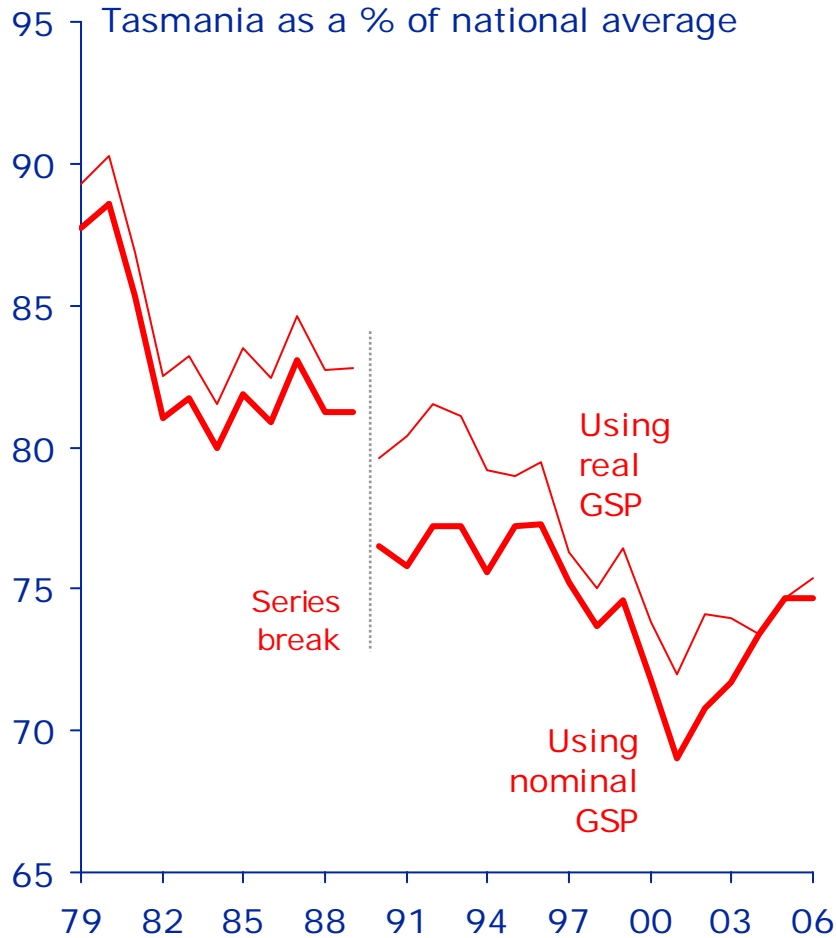
Real per capita GSP growth five years to 2005-06



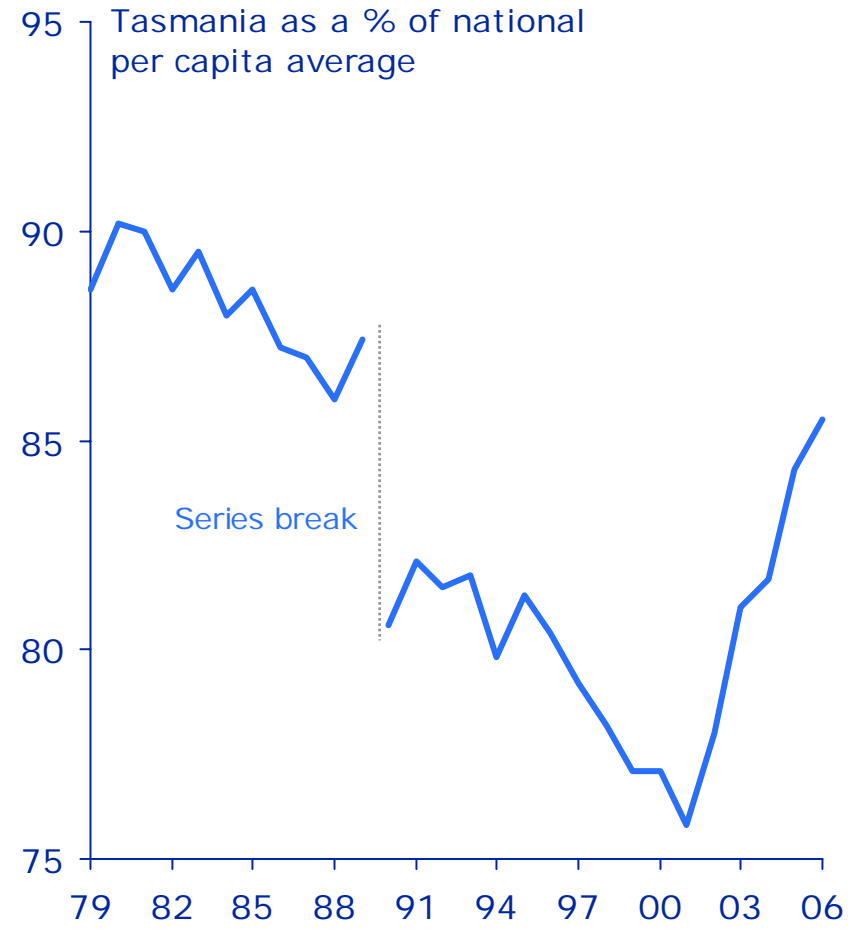
Sources: ABS State Accounts (5220.0) 2005-06;
Economics@ANZ

Tasmania's per capita GSP relative to national average unchanged, but income rose further

Per capita State product



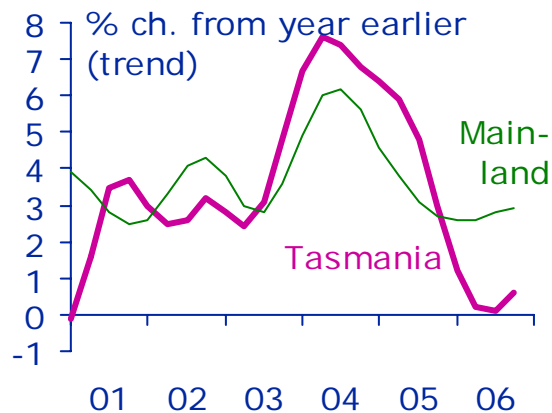
Household disposable income



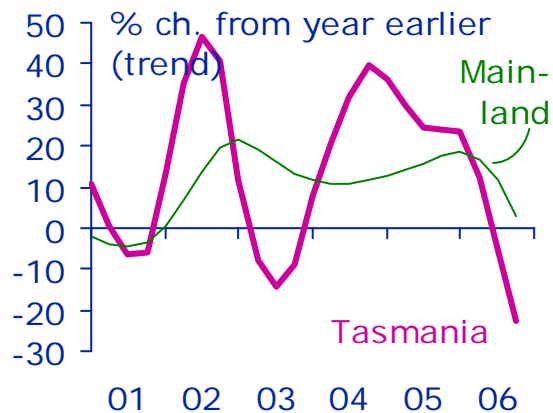
Sources: ABS State Accounts (5220.0) 2005-06;
Economics@ANZ

However growth in most components of final demand has softened over past three quarters

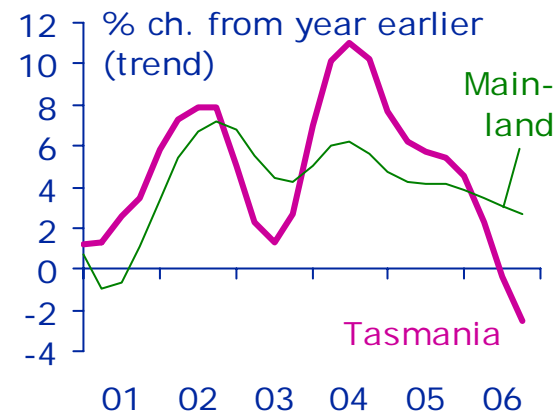
Household consumption



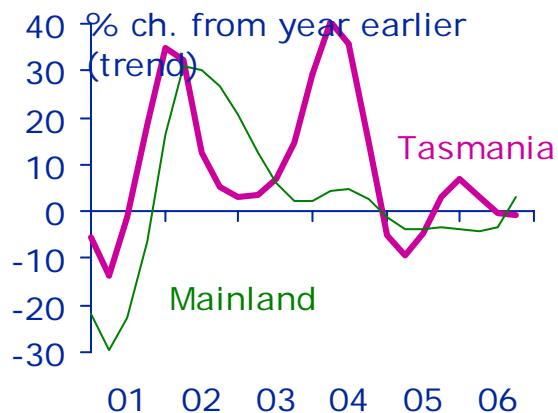
Business investment



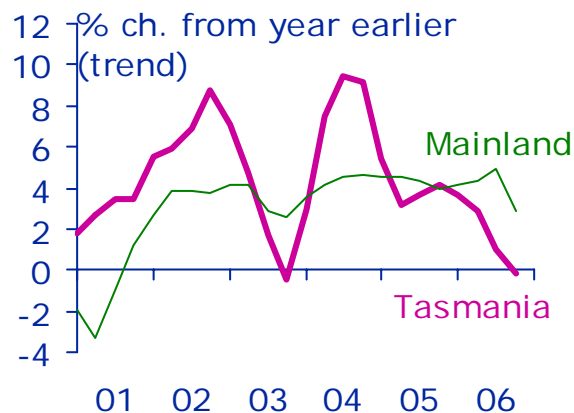
State final demand



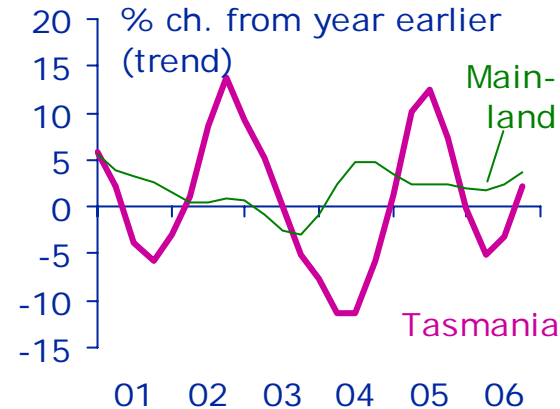
Dwelling investment



Public final spending



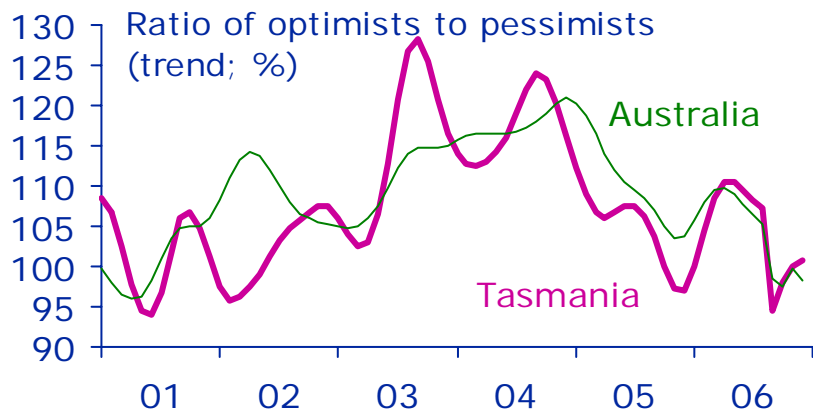
Overseas exports



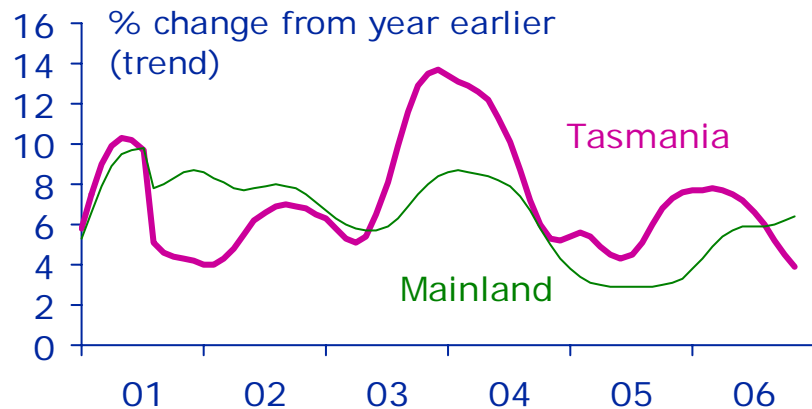
Sources: ABS, Australian National Accounts: State Details (5206.0); Economics@ANZ.

Tasmanian household confidence and spending have eased

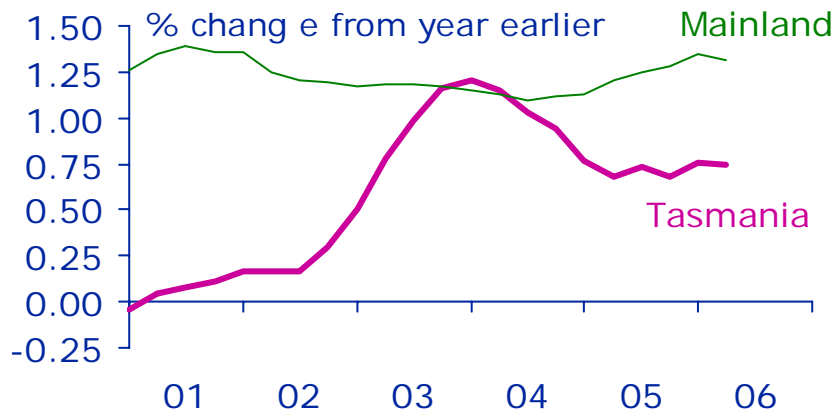
Consumer confidence



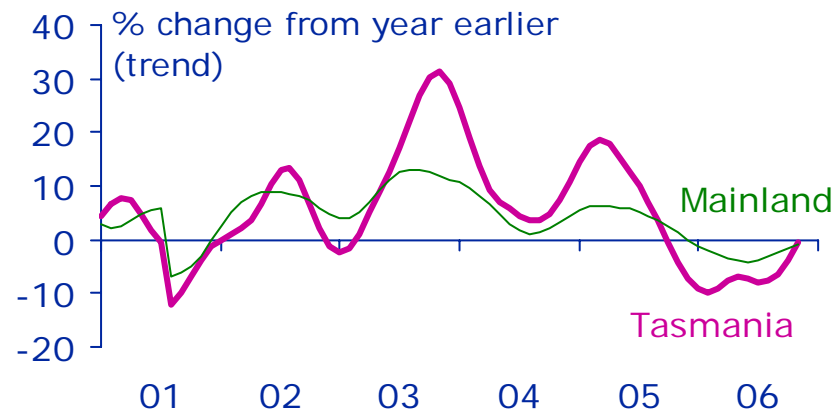
Retail sales



Population growth



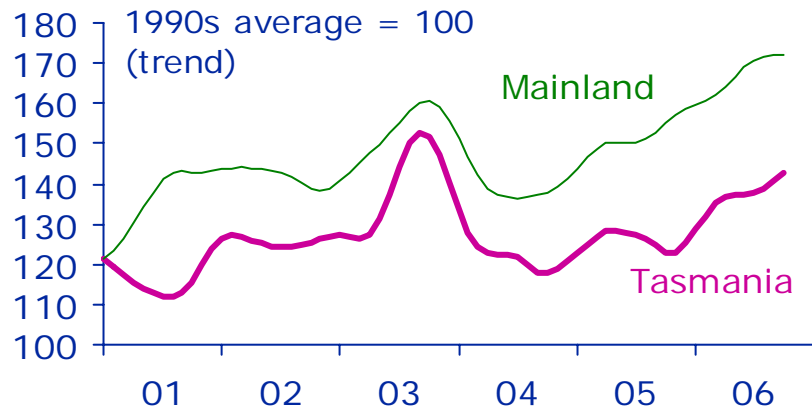
New motor vehicle sales



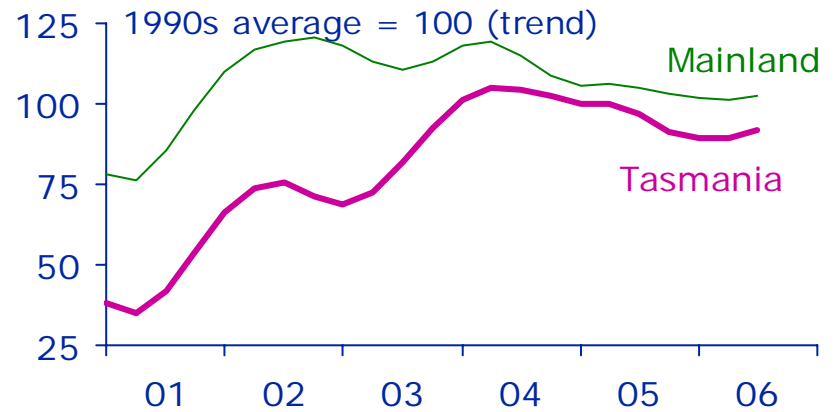
Sources: Westpac / Melbourne Institute; ABS Demographic Statistics (3101.0) Retail Trade (8501.0); Sales of New Motor Vehicles (9314.0)

Tasmania's housing boom is over although activity seems to be holding up fairly well

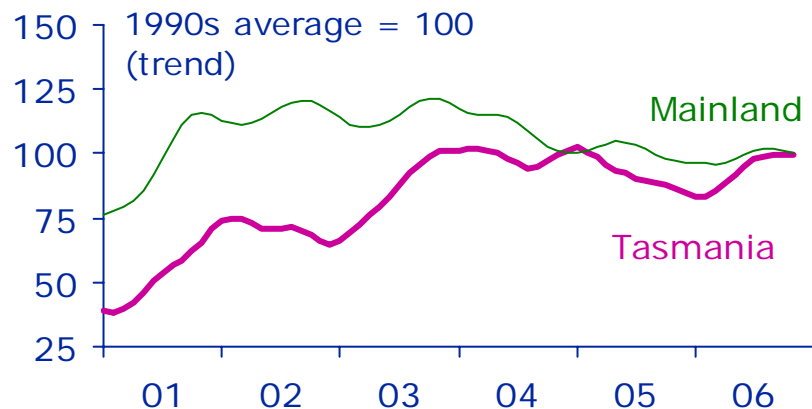
Housing finance commitments



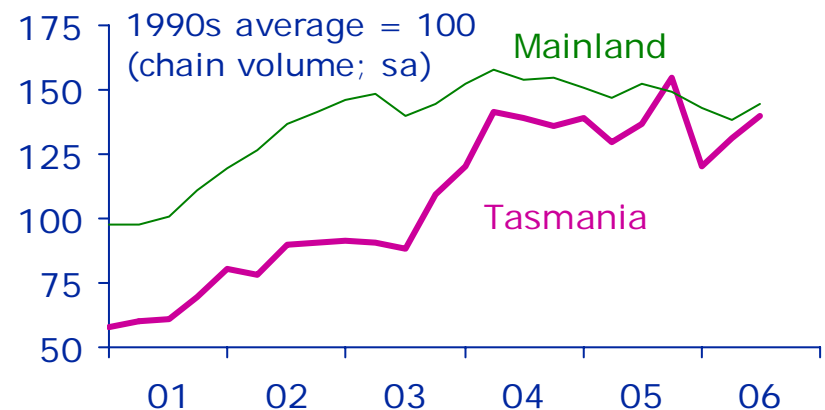
Dwelling commencements



Residential building approvals



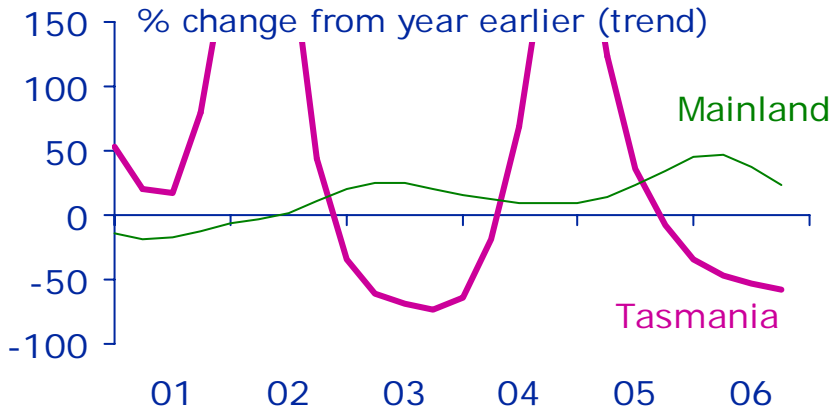
Residential building work done



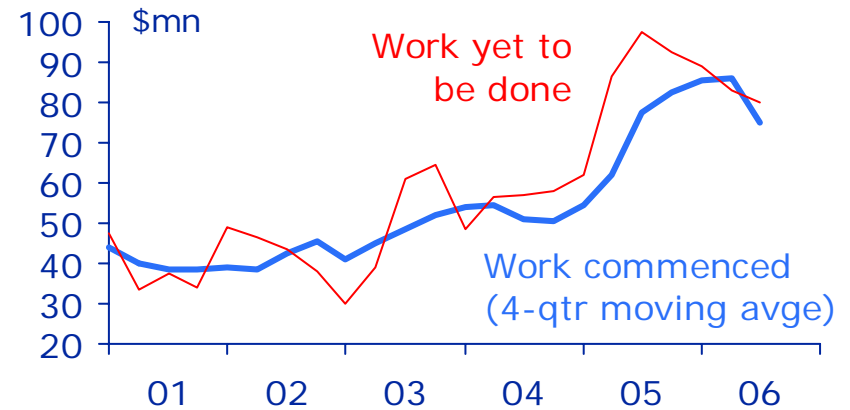
Sources: ABS, Housing Finance (5609.0); Building Approvals (8731.0); Construction Work Done (Preliminary) (8755.0); Economics@ANZ.

However most categories of business investment appear to be slowing

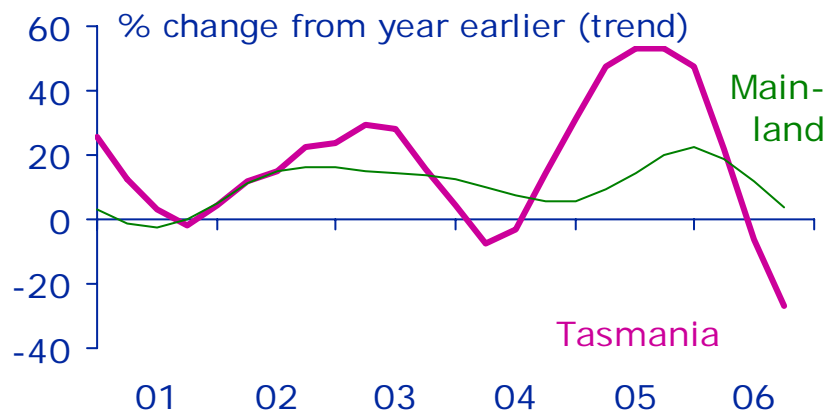
Buildings and structures



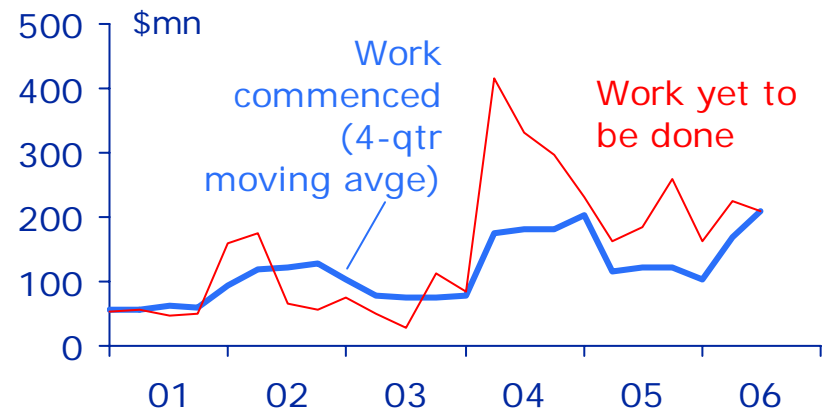
Non-residential building



Equipment, plant and machinery



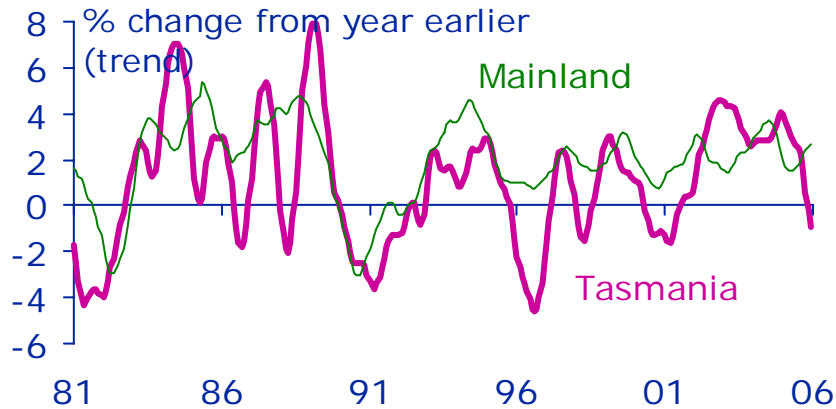
Engineering construction



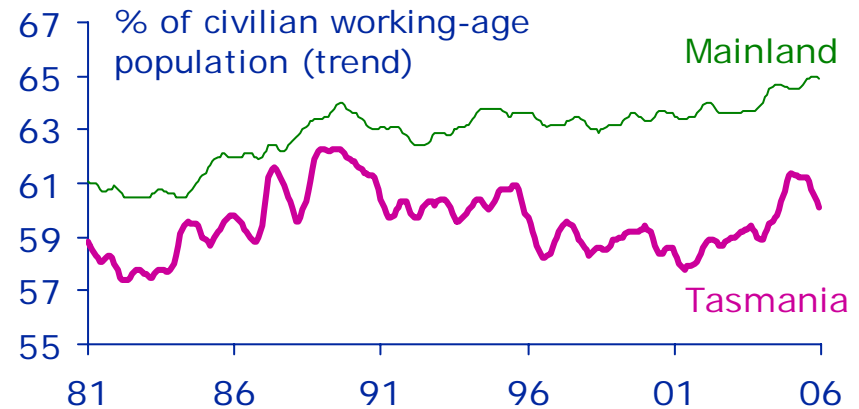
Sources: ABS, Private New Capital Expenditure (5625.0); Building Activity (8752.0); Economics@ANZ.

Slowing in Tasmanian economy is also apparent in labour force indicators

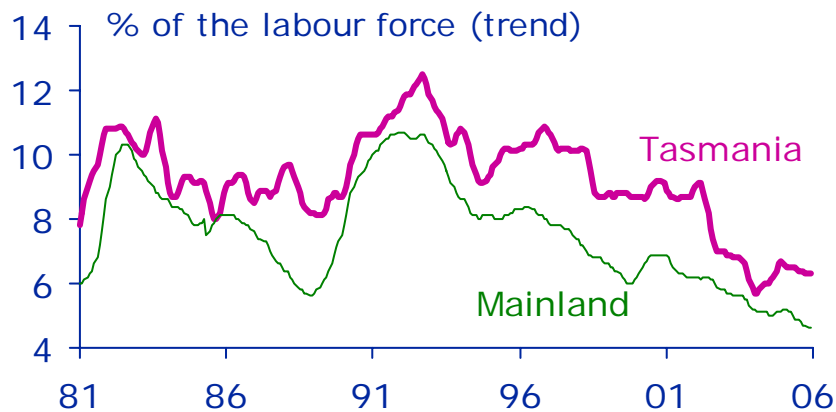
Employment growth



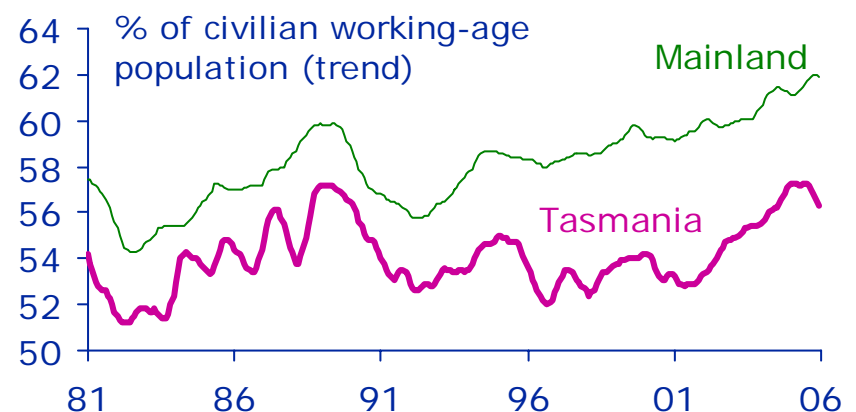
Participation rate



Unemployment rate



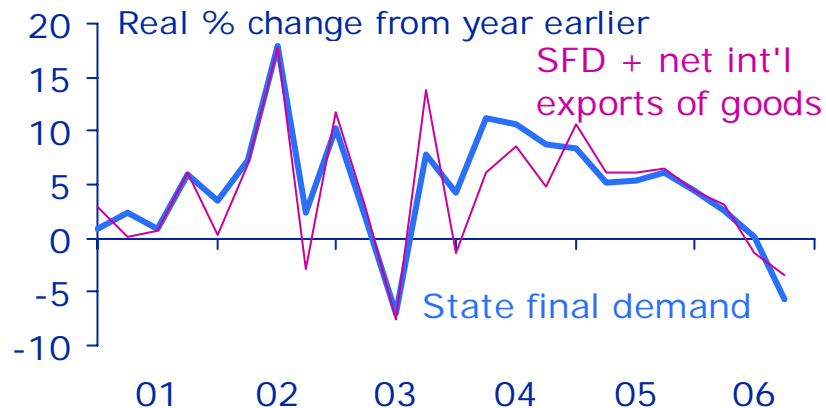
Employment-population ratio



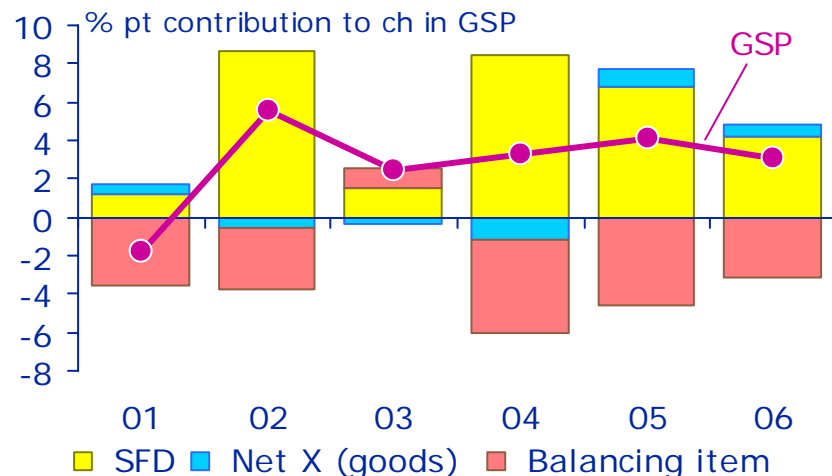
Sources: ABS *The Labour Force* (6202.0);
Economics@ANZ

It's difficult to see how Treasury's forecast of 3½% growth in 2006-7 will be attained

State final demand



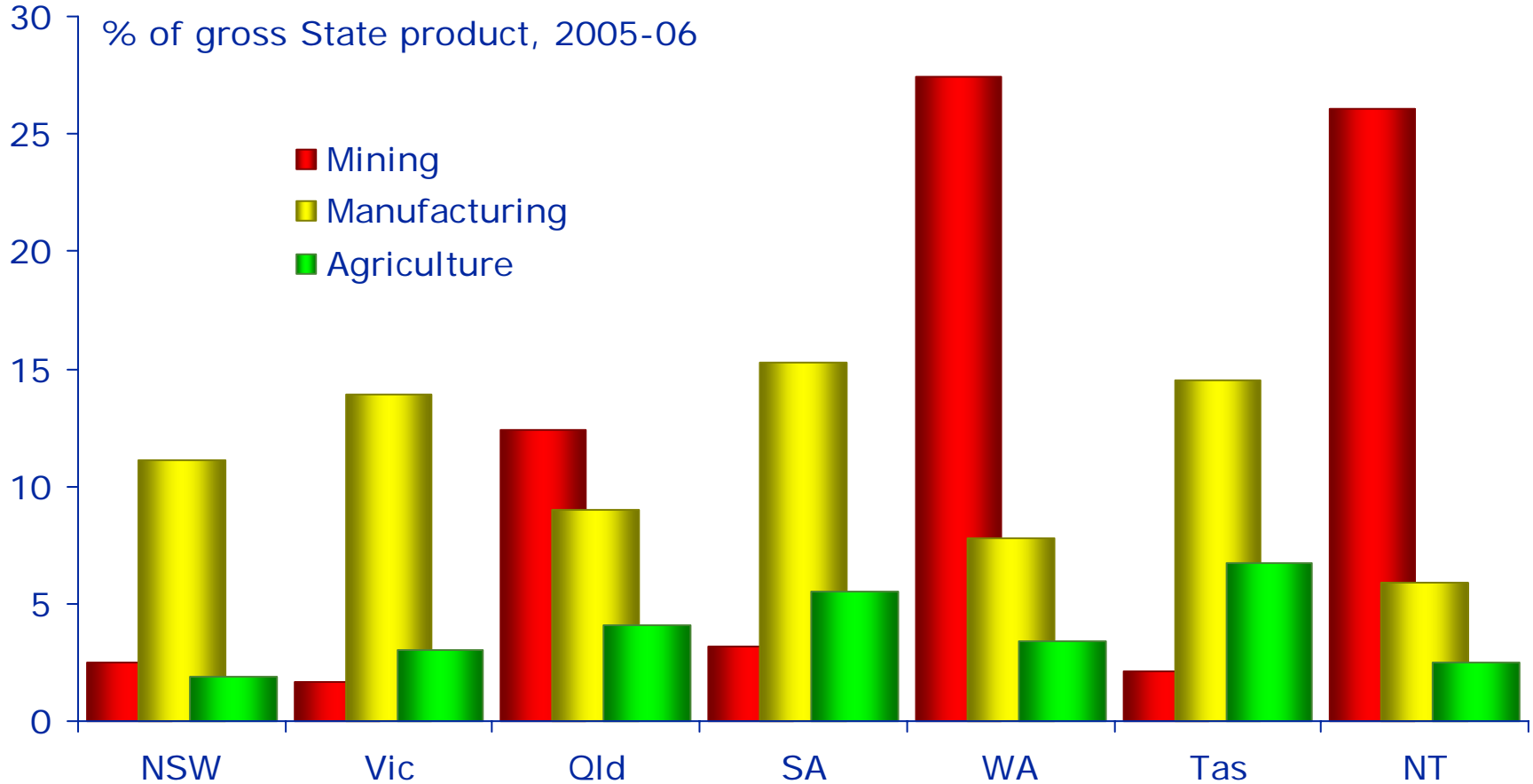
Components of GSP



- The 'balancing item' in the State accounts for Tasmania (inventories, net interstate exports and net international services exports) typically subtracts 3-4 pc points from annual GSP growth
- So State final demand (SFD) + net international exports of goods (NIXG) would need to grow by 6½-7½% in 2006-07 if GSP growth is to be around 3½%
- Given the slowdown in SFG + NIXG over the past three quarters it would need to grow by an average of 6-6½% per qtr over the next three qtrs for the Budget forecast to be attained (in terms of GSP)

It's inevitable that different States will grow at different speeds

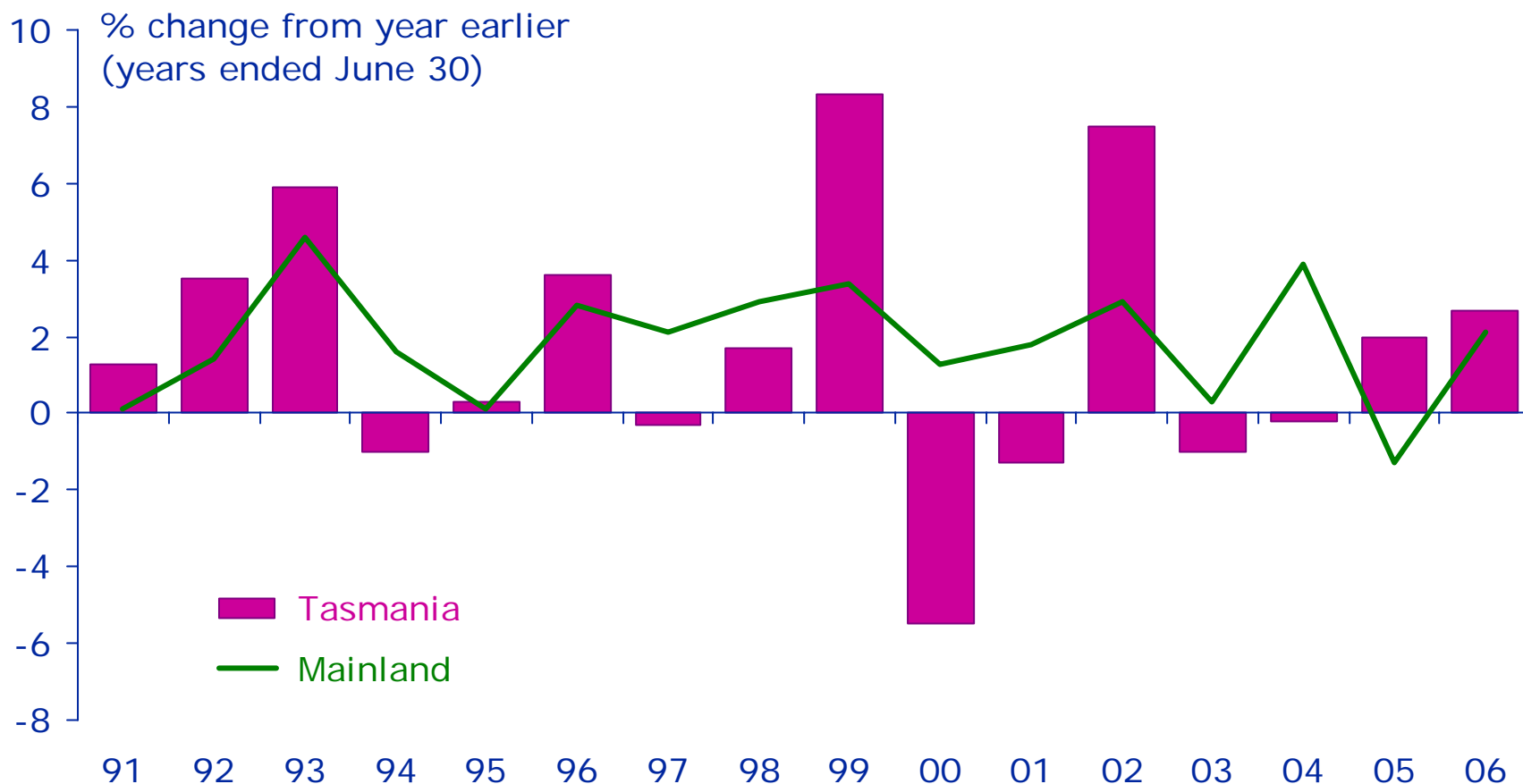
Mining, manufacturing and agriculture as a share of State economies



Sources: ABS; Economics@ANZ.

Tasmanian labour productivity has risen for a second consecutive year

Labour productivity growth – Tasmania vs the mainland

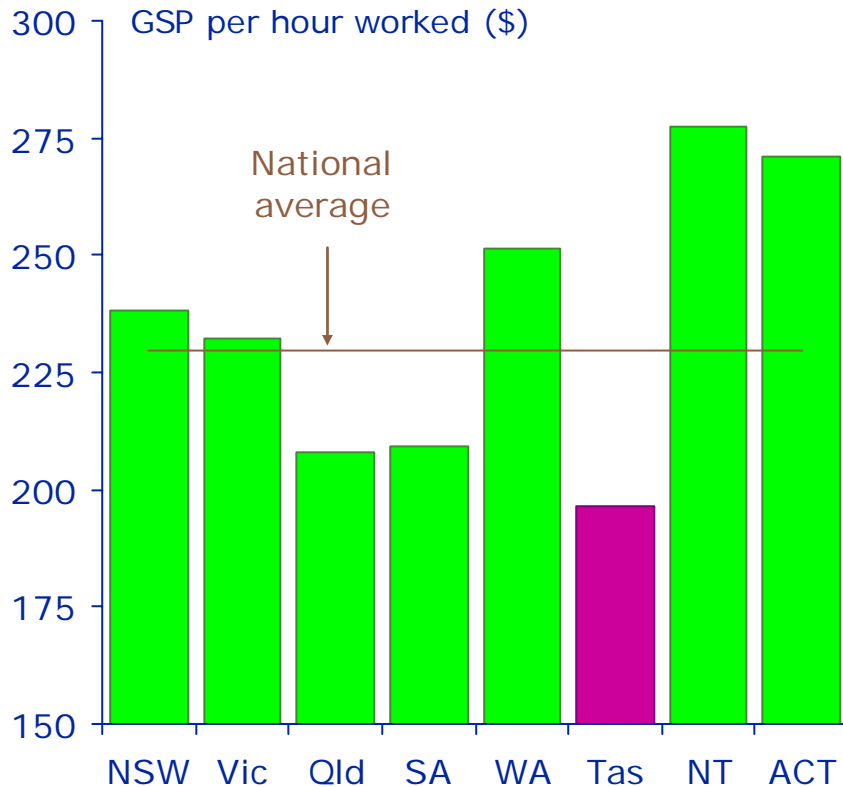


* Labour productivity defined as real gross State product per hour worked.

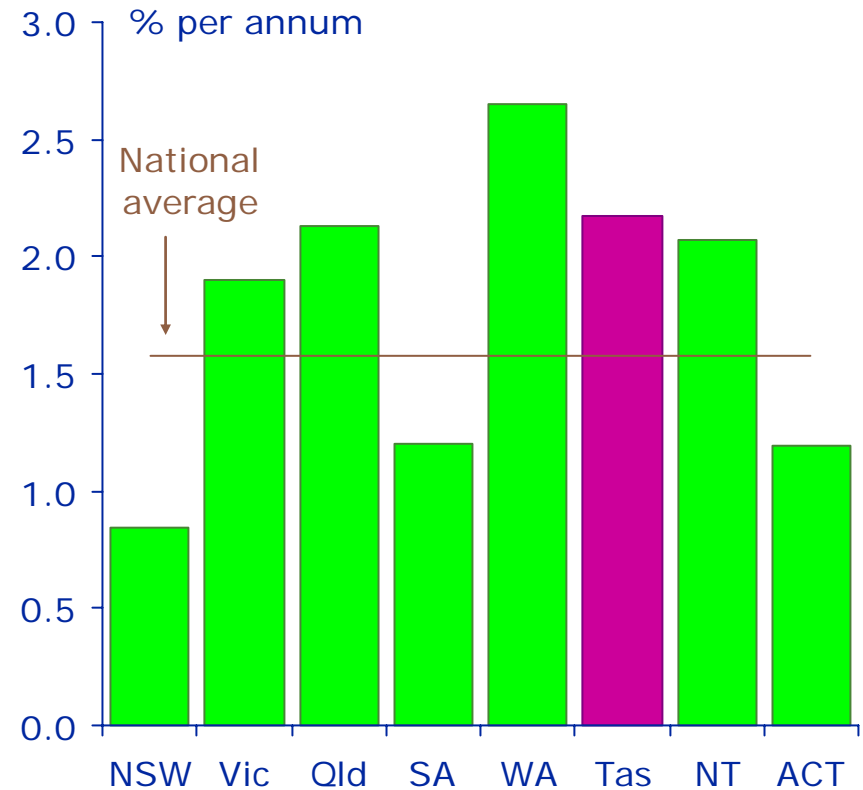
Sources: State Accounts (5220.0); ABS *Employed persons by sex, age, hours worked, state* (6291.0.55.001); Economics@ANZ.

Level of Tasmanian productivity remains low but it's now growing at an above-average rate

Level of labour productivity 2005-06



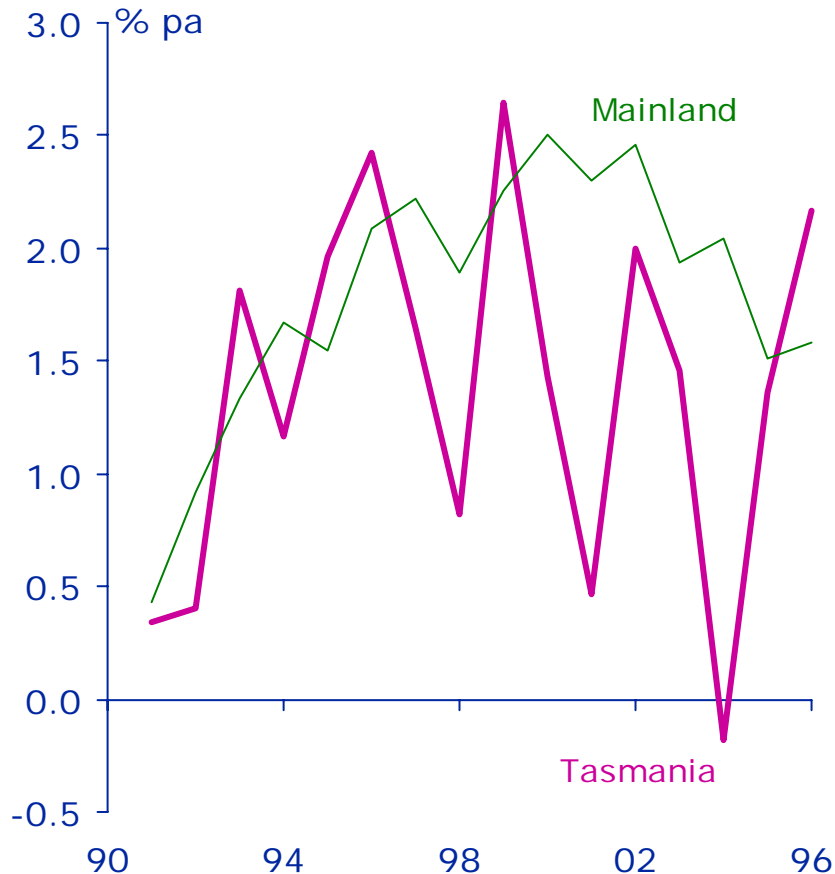
Labour productivity growth 2000-01 to 2005/06



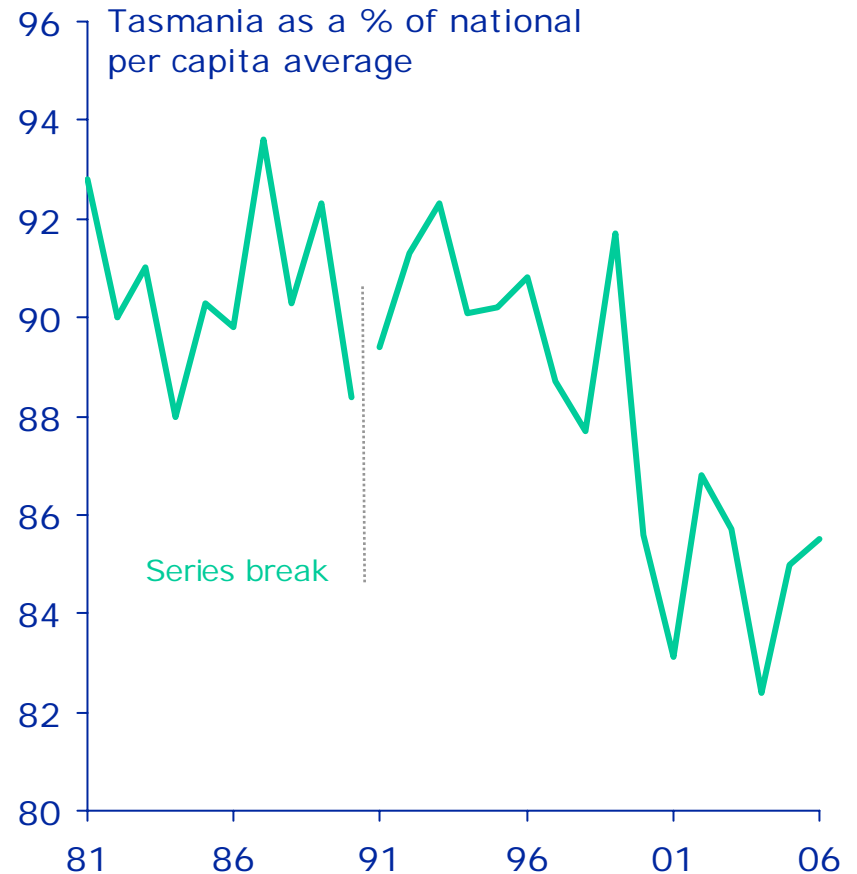
* Productivity defined as real gross State product per hour worked.
Sources: State Accounts (5220.0); ABS Employed persons by sex, age, hours worked, state (6291.0.55.001); Economics@ANZ.

It will take many years of above-average growth in productivity to reverse the 1990s decline

Productivity growth over rolling 5-year periods



Tasmanian productivity relative to national average

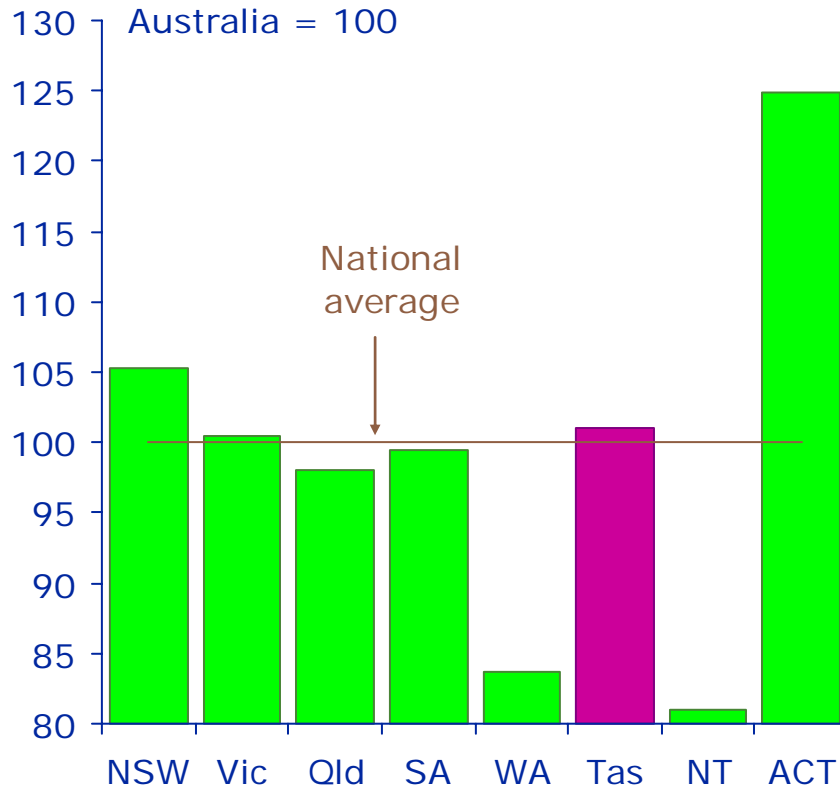


* Productivity defined as real gross State product per hour worked.

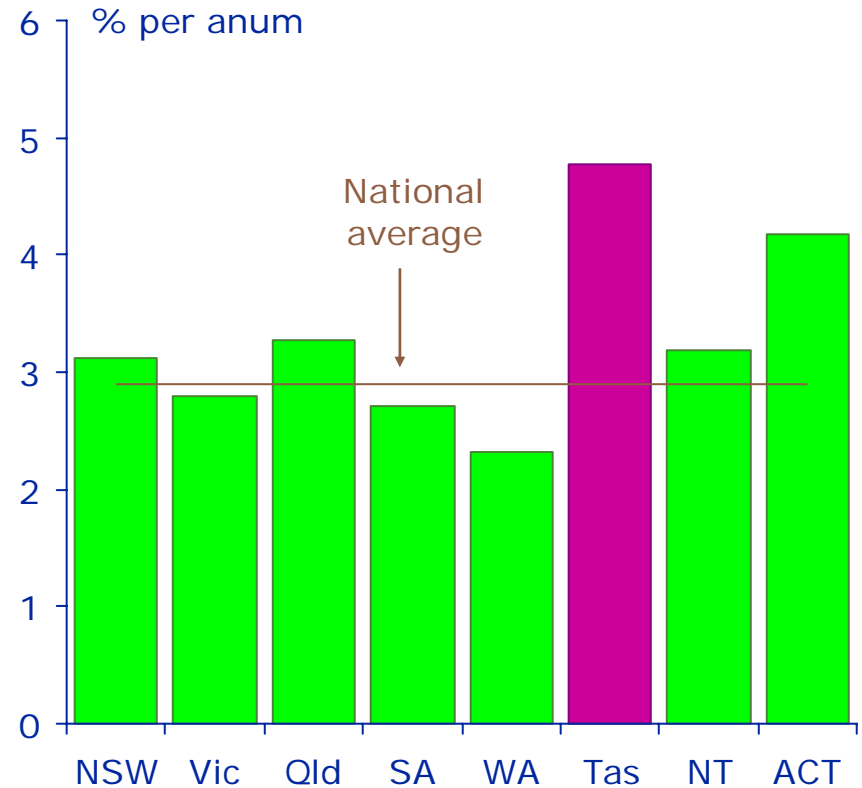
Sources: State Accounts (5220.0); ABS Employed persons by sex, age, hours worked, state (6291.0.55.001); Economics@ANZ.

Having the lowest average wages in Australia may not actually be a source of comparative advantage

Unit labour costs*,
2005-06



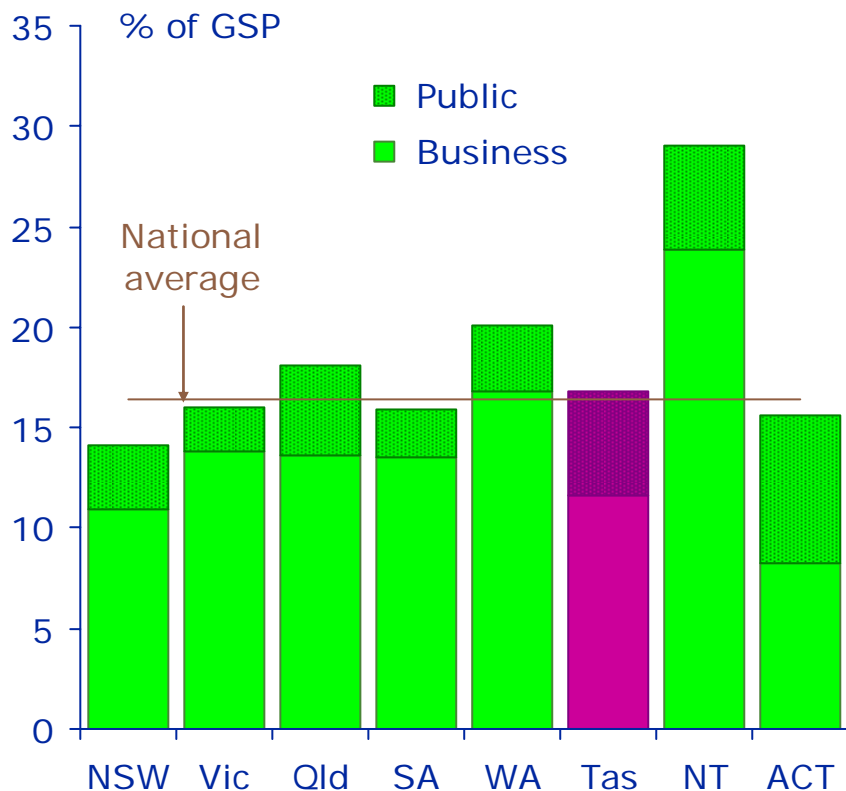
Unit labour cost growth
2000-01 to 2005-06



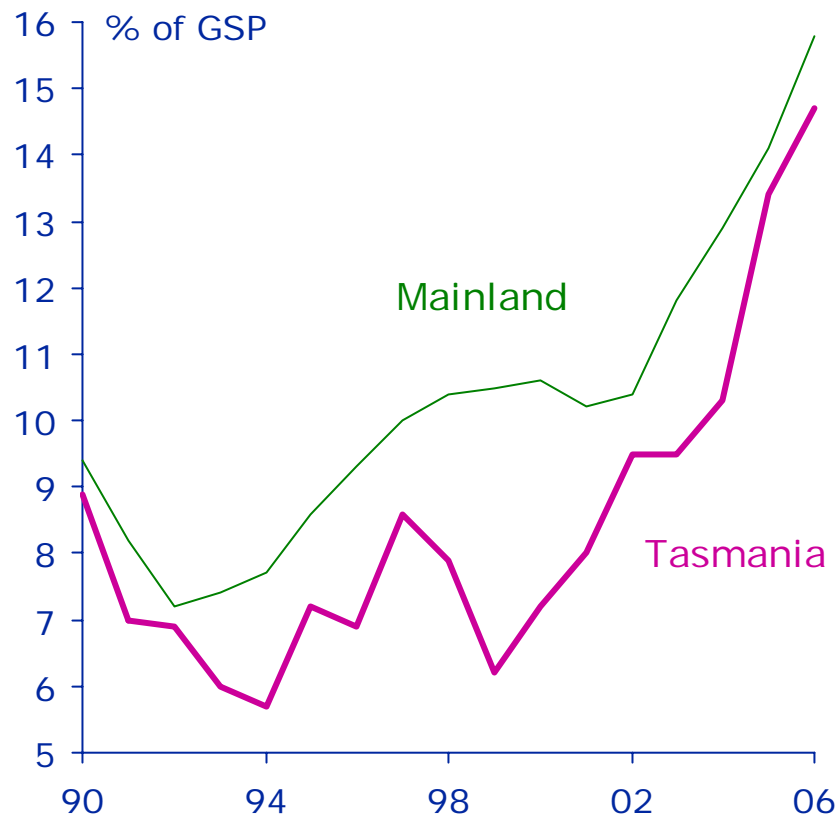
* Unit labour costs defined as employee compensation per hour worked divided by gross state product per hour worked. Sources: ABS State Accounts (5220.0); Employed persons by sex, age, hours worked, state (6291.0.55.001); Economics@ANZ.

Tasmania is now investing the same share of its income as the mainland

Investment as a share of GSP 2001-02 to 2005-06



Business investment as a share of GSP

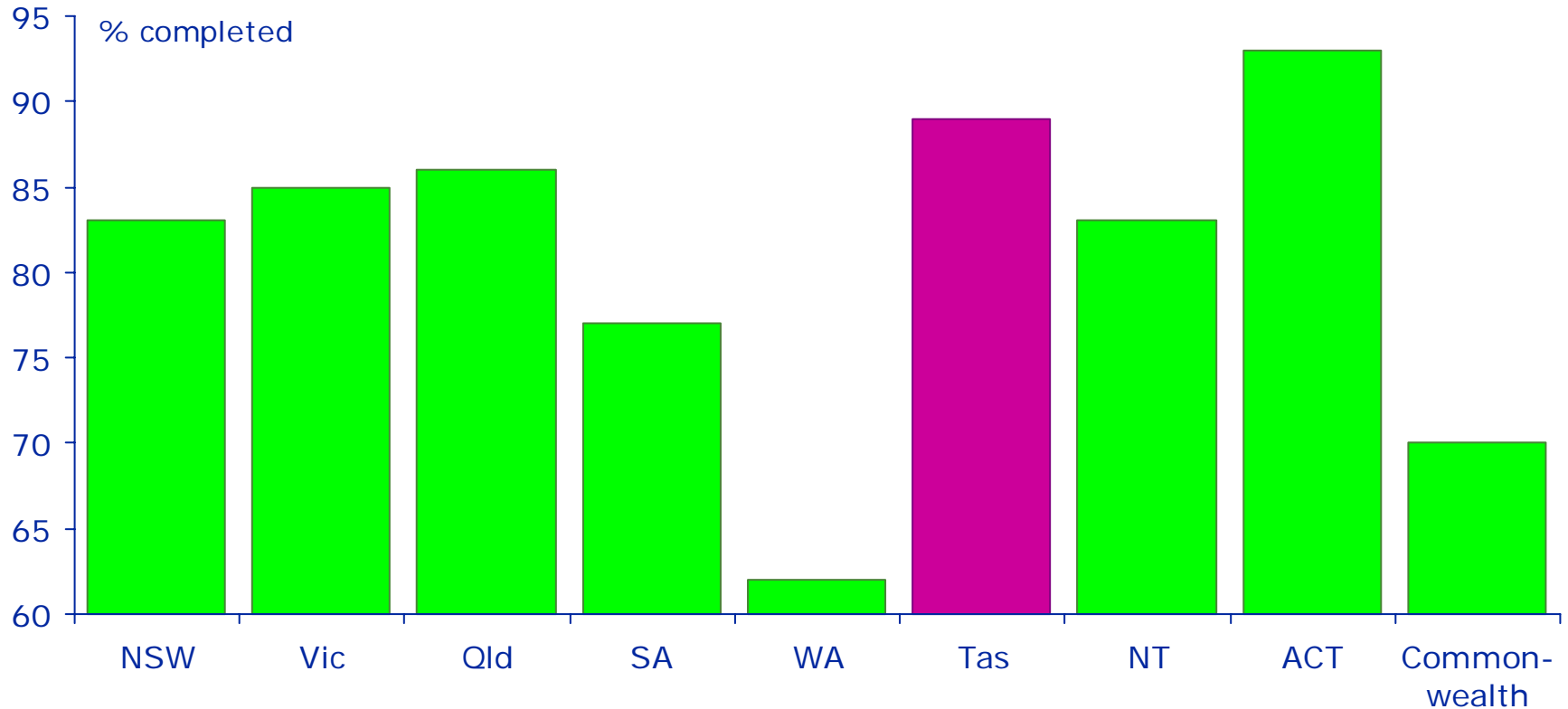


Note: 'Investment' refers here to non-residential fixed capital expenditure, ie excluding housing and stocks. Business investment excludes purchases of second-hand assets from the public sector.

Sources: ABS State Accounts (5220.0) 2005-06; Economics@ANZ

Tasmania has a good record in implementing productivity-enhancing competition reforms

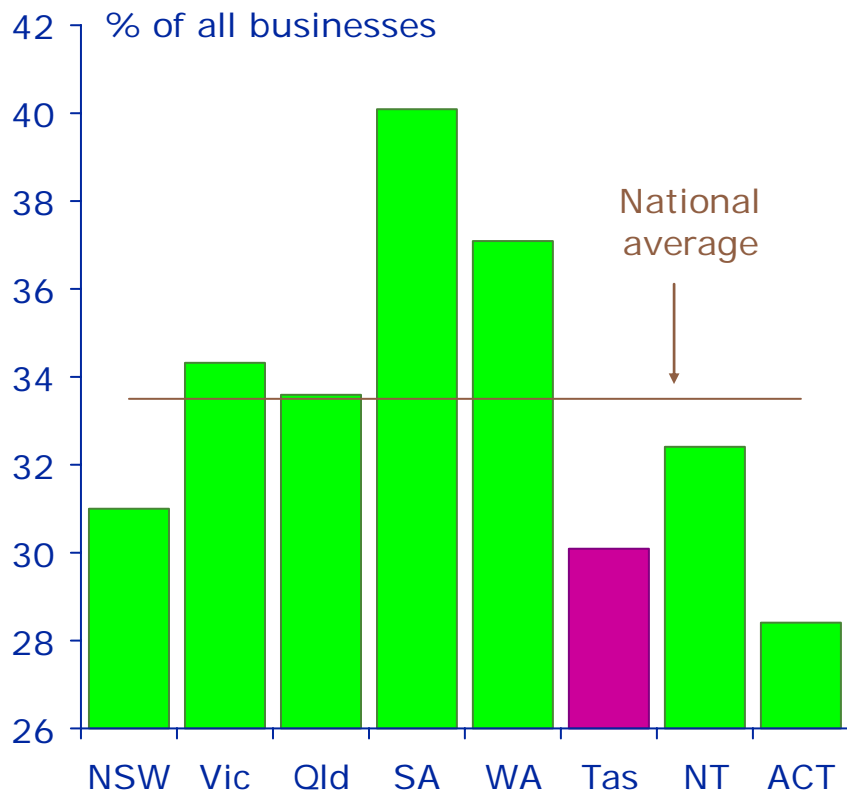
Progress in reviewing and reforming legislation for anti-competitive effects



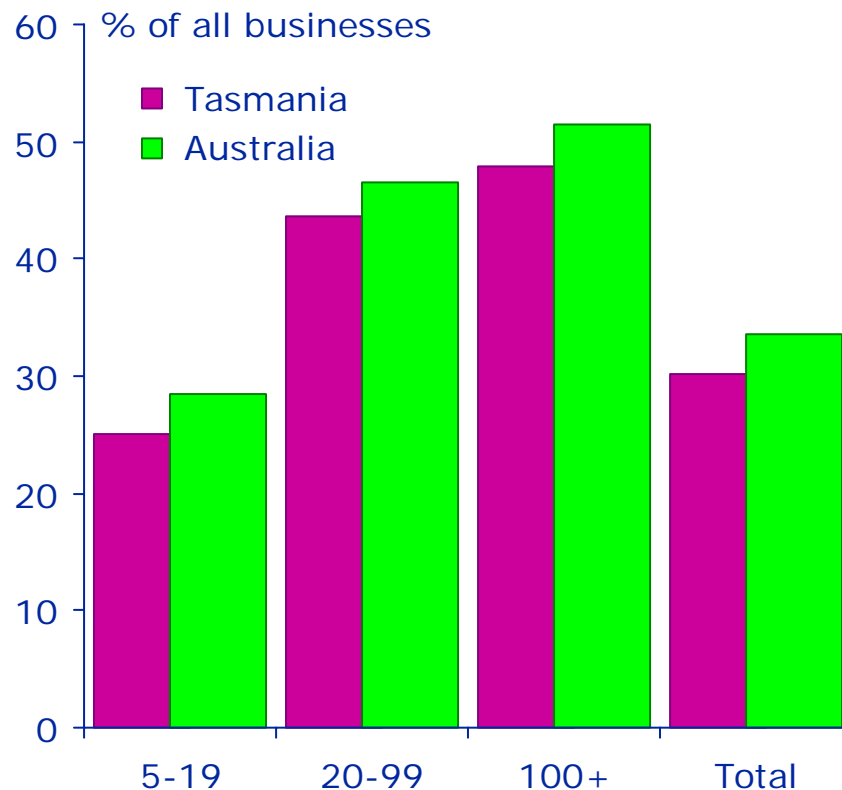
Source: National Competition Council, 2004 NCP Assessment.

Tasmanian businesses are the least innovative in Australia (apart from Canberra)

Businesses innovating, 2004 and 2005

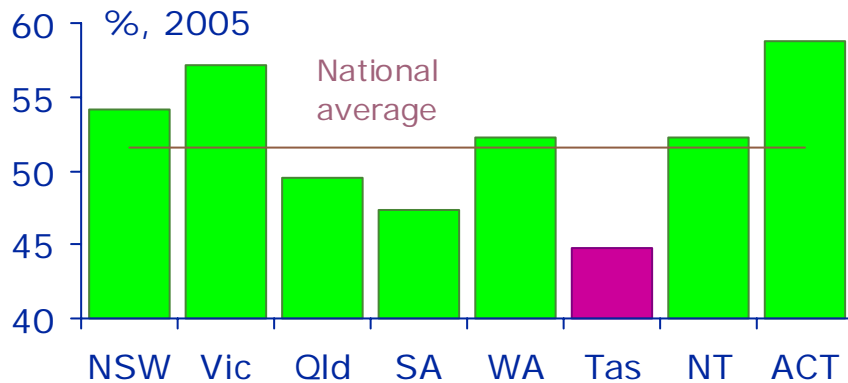


Businesses innovating, by number of employees

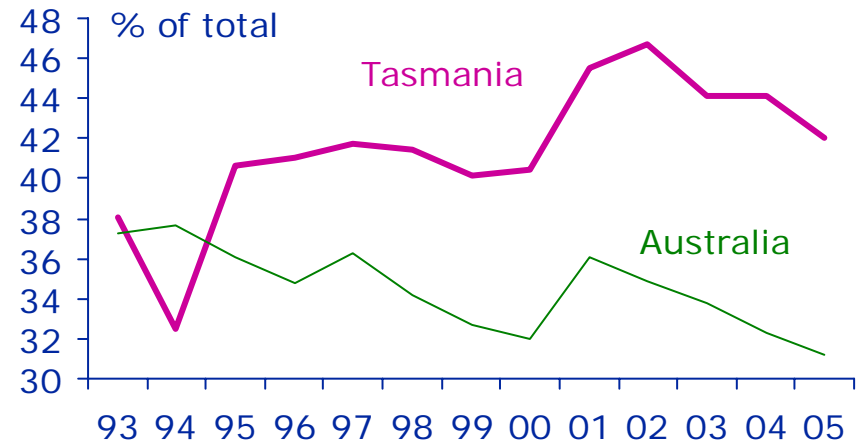
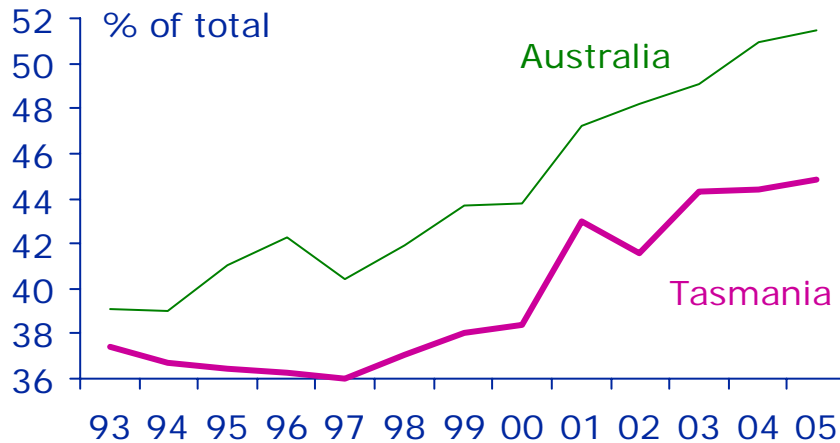
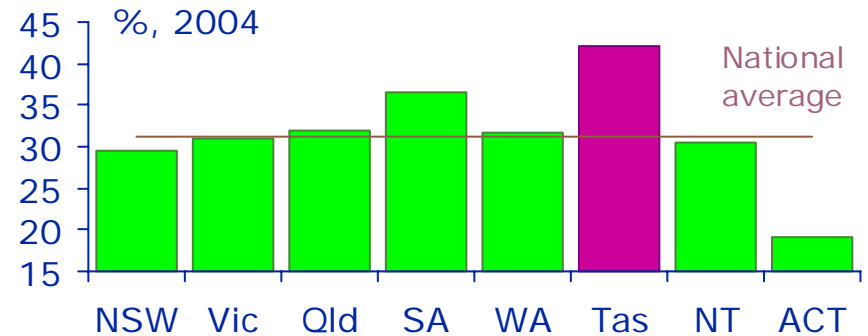


Tasmania has the poorest educational attainment rankings of any State or Territory

15-64 year olds with post-school qualifications



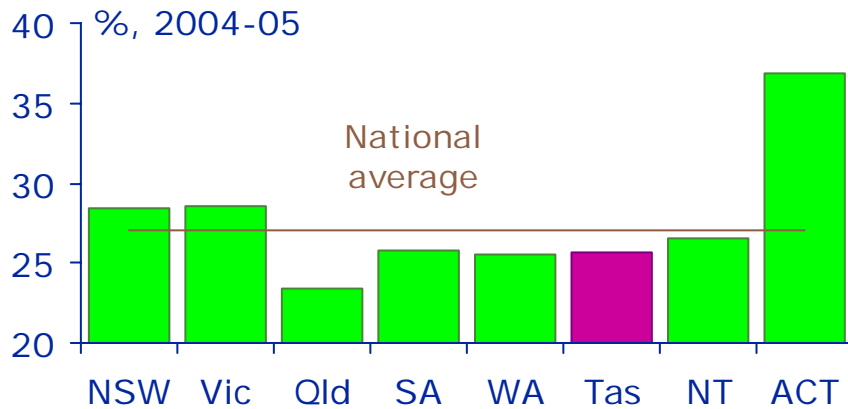
15-64 year olds who have not completed Year 12



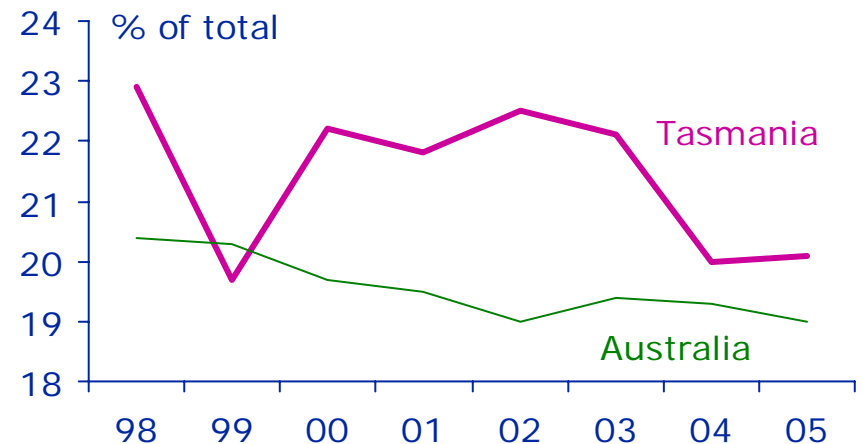
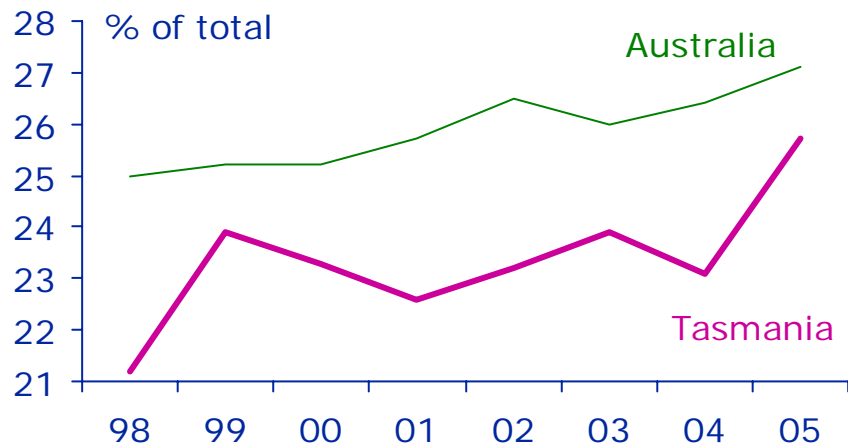
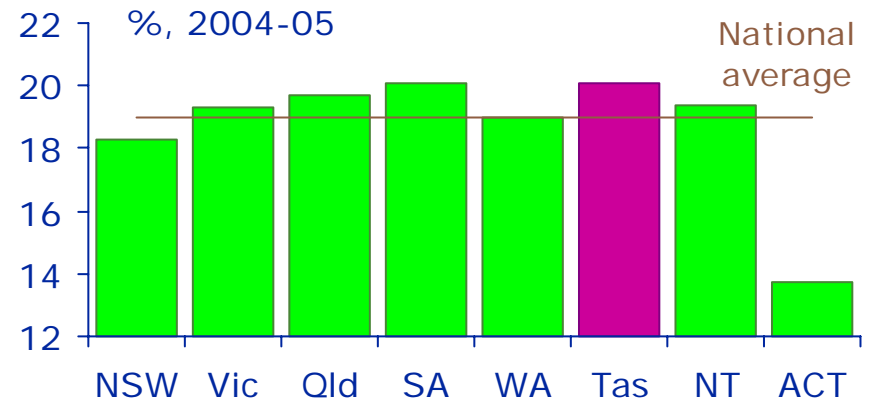
Source: ABS, Education and Work, Australia, (6227.0); Australian Social Trends (4102.0).

Tasmania has an above- (below-) average proportion of workers in high- (low-) skill jobs

Workforce employed in highest-skill occupations



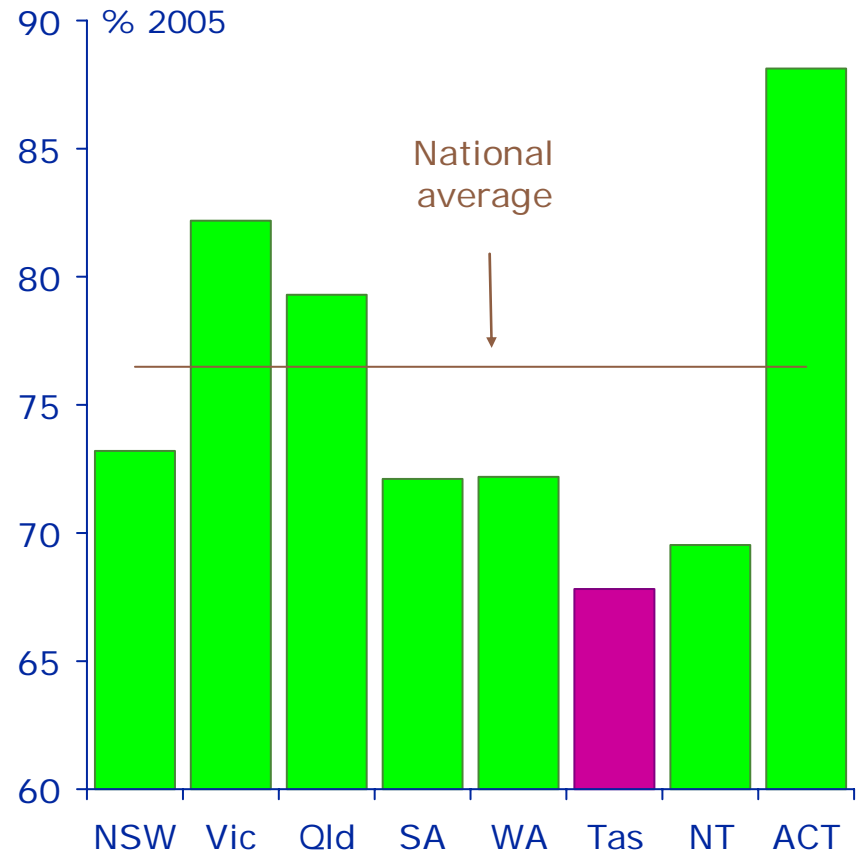
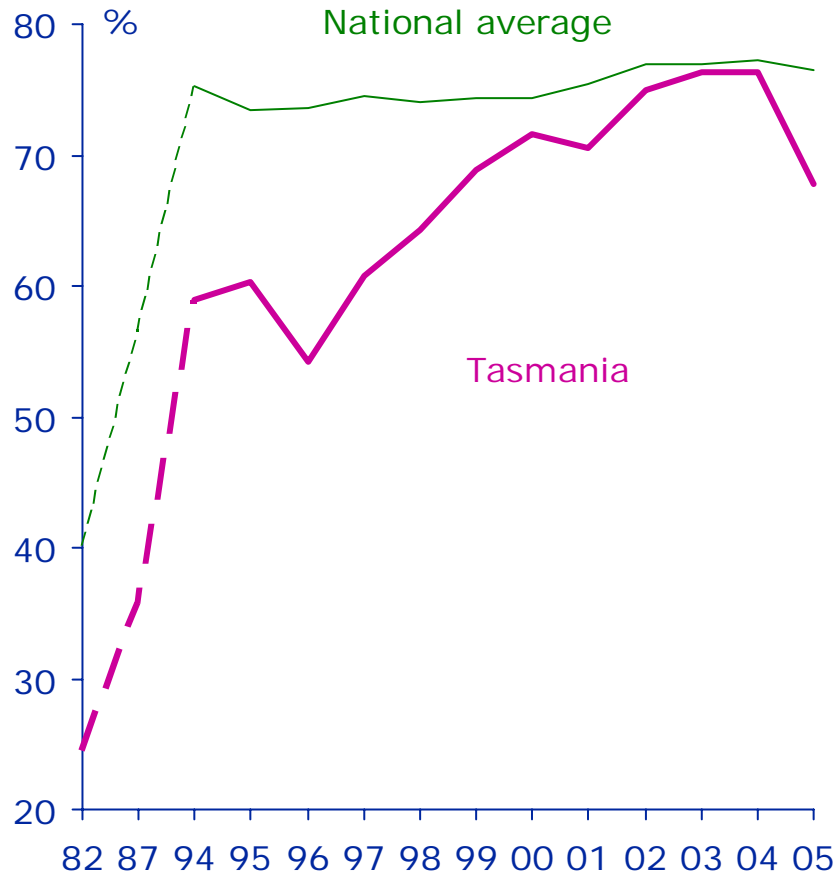
Workforce employed in lowest-skill occupations



Source: ABS, Australian Social Trends (4102.0).

Disturbingly, the Year 12 retention rate slipped back last year to its lowest since 1998

School retention rates to year 12

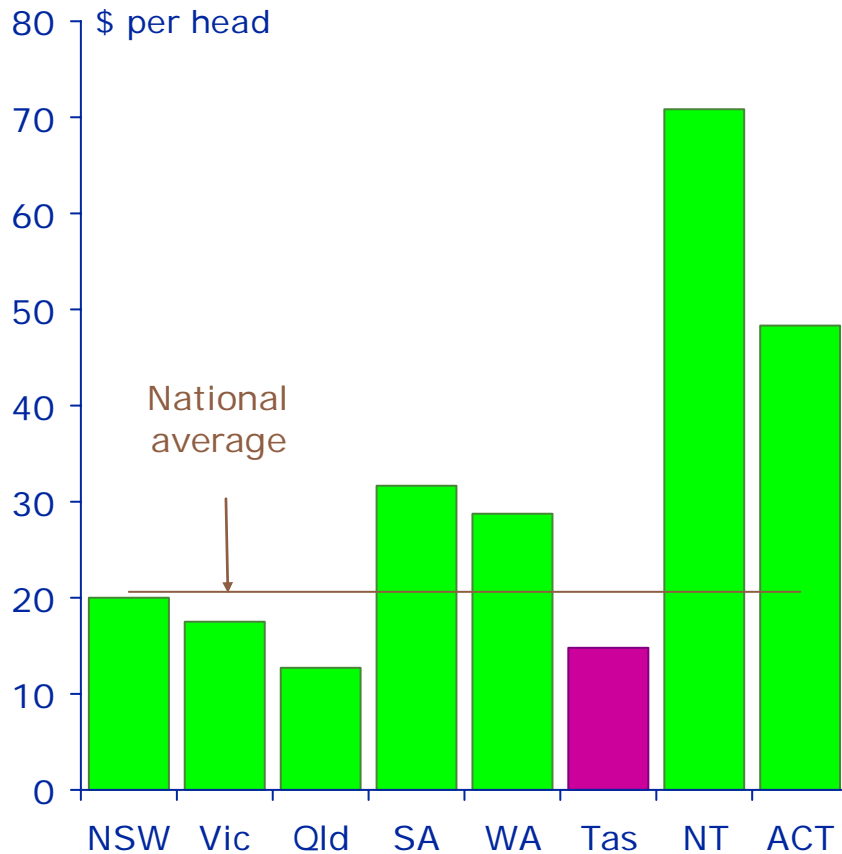


Education policy is heading in the right direction – but it needs more resources

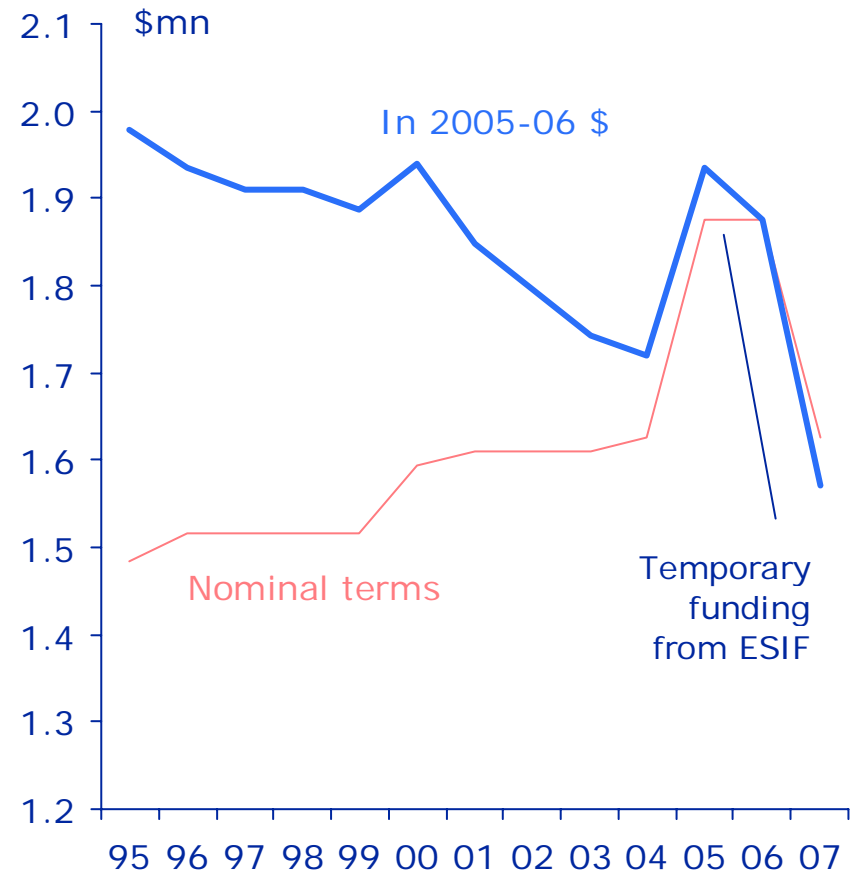
- Acceptance that Tasmania's education system has delivered poor outcomes for Tasmanian students
 - David Bartlett explicitly acknowledges 'need to improve performance in relation to literacy and numeracy benchmarks, particularly in relation to students in Year 7'
- Consciously seeking to raise the student retention rate to Year 12
 - Minister Bartlett again: 'we need to encourage and celebrate learning to the end of Year 10 and beyond; Year 10 is an entry point to further learning, not an end point'
- Curriculum reform
 - abandonment of EL framework in favour of 'a core focus on learners and schools at the front line'
- But education got a low priority in this year's Budget
 - education recurrent expenses up only 2¾% in 2006-07 cf health 7¾%, 'public order and safety' 6½%
 - education's share of the operating Budget will decline from 28.3% in 2005-06 to 26% in 2006-07

The arts could do with some extra funding too!

Per capita arts funding by State & Territory governments, 2004-05



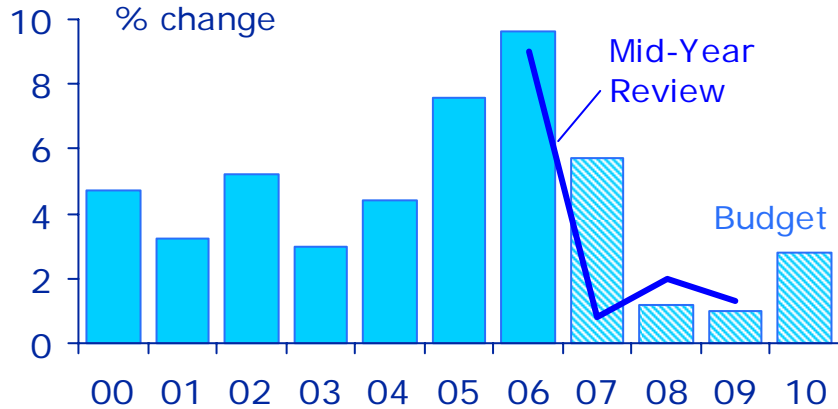
Arts grants administered by Tas Arts Advisory Board



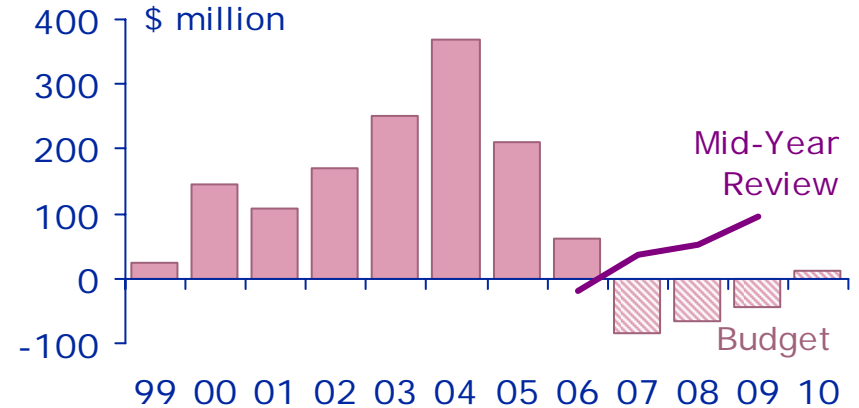
Source: ABS, Cultural Funding by Government 2004-05 (4183.0); Arts Tasmania.
 Disclosure: I'm also Chair of the Tasmanian Arts Advisory Board.

The State Government's fiscal position has deteriorated since the election (though it's still strong)

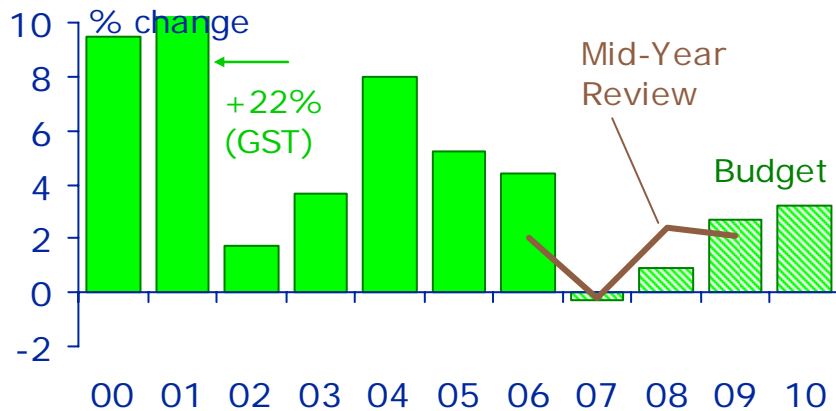
State budget expenses*



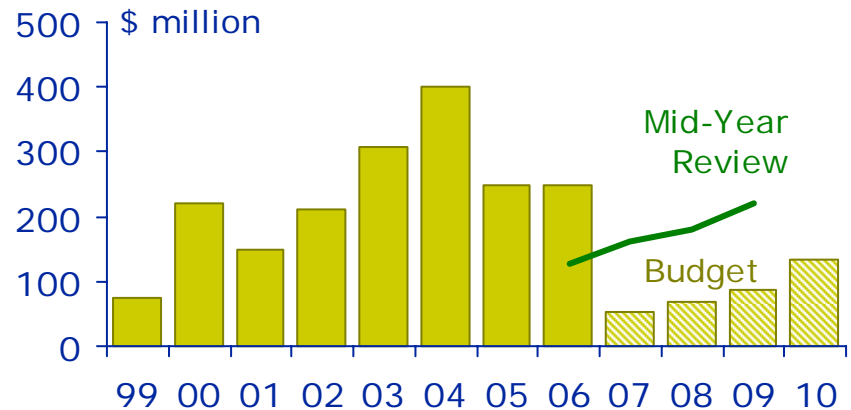
State budget fiscal balance*



State budget revenues*



State budget cash balance*



*General government sector. Sources: Department of Treasury & Finance, *Mid-Year Financial Report* (February 2006); 2006-07 Budget Papers (May 2006); Economics@ANZ.

There's no reason why asset sales shouldn't be part of the financing mix for the new RHH

Key numbers for State-owned enterprises (\$ mn)

Business	Net assets as at 30 June 2006	Net profit after tax (2005-06)	Dividend and tax equivalent payments to State Budget (2005-06)	Plausible range of sale values based on p / e ratios of	
				13x	16x
Aurora Energy	333	22	32	291	358
Transend Networks*	529	31	44	397	488
Hydro Tasmania	907	44	67	576	708
MAIB§	173	58	82	760	935
Forestry Tasmania	569	10	19	134	165
TT Line	188	24	20	313	385
RWSC	12	-1	-2	-17	-21

Note: * excludes gifted assets. § 2004-05 results.

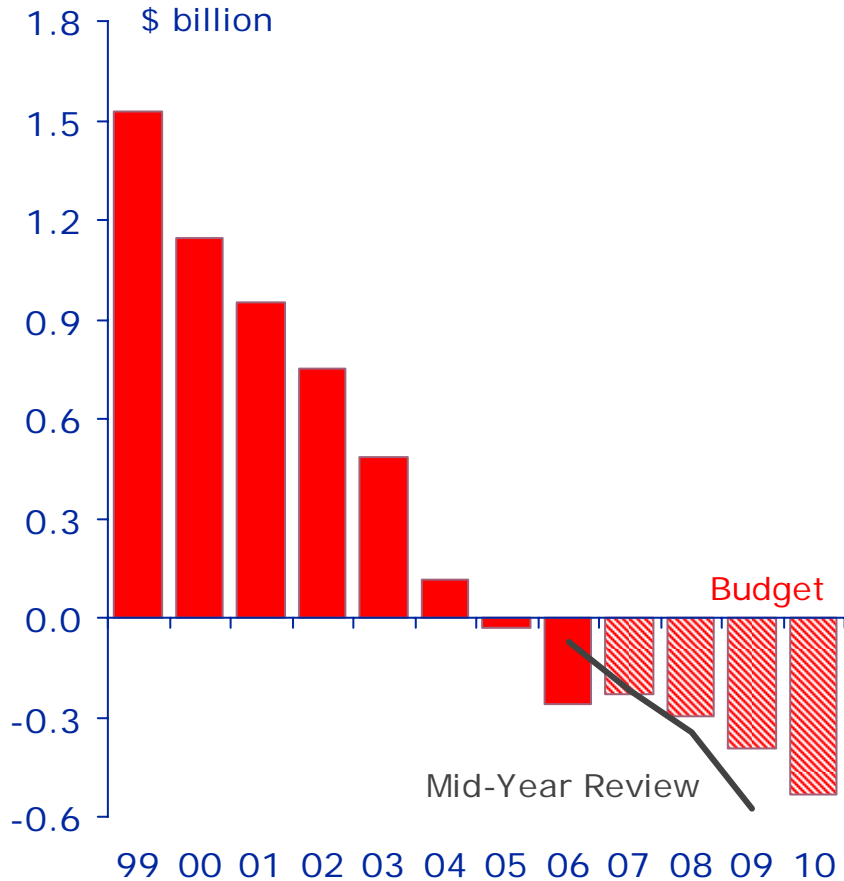
Sources: Annual Reports and Economics@ANZ calculations.

Some general observations on State finances (in the context of how to finance the new RHH)

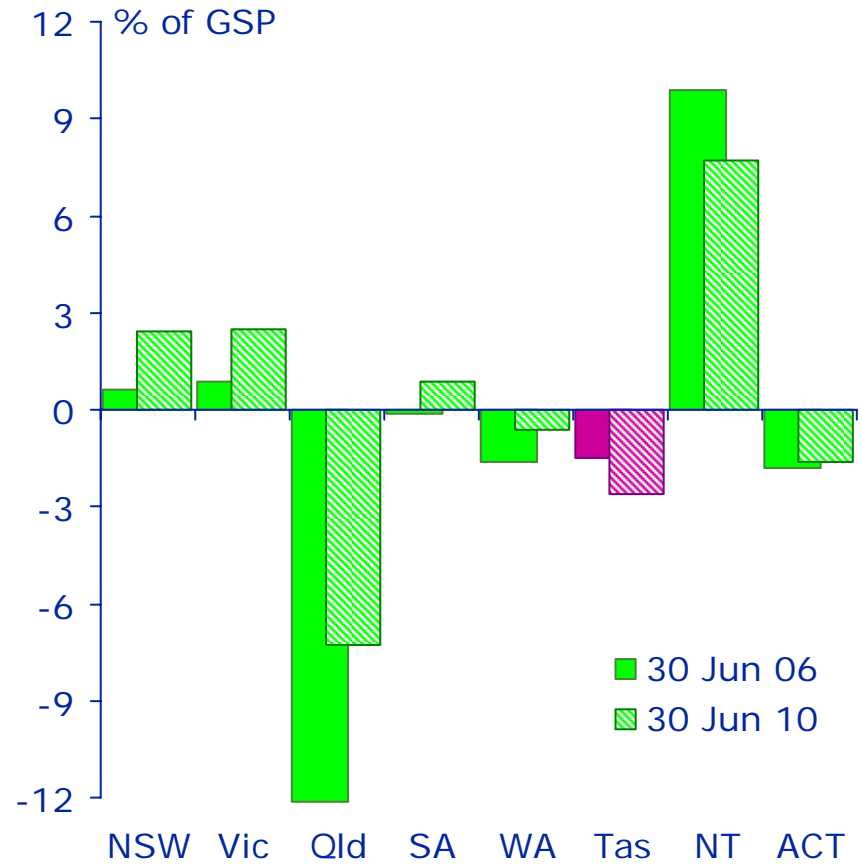
- In general, States should not run operating deficits
 - that is, recurrent expenses (wages & salaries, interest, grants etc) should not exceed revenue from taxes, Commonwealth grants, etc
 - States are not responsible for macro-economic policy
- There's nothing wrong, in principle, with States borrowing for capital expenditures (infrastructure)
 - there's no principle of economics or public finance which says the optimal level of debt for any government is zero
 - within reason, borrowing is an equitable way of ensuring that future generations of taxpayers contribute to the costs of creating assets from which they will benefit
- Borrowing some of the cost of building a new Royal Hobart Hospital would not imperil Tasmania's credit rating

Tasmania's net debt position will still be the second strongest of all States by 2010

Tasmanian 'general government' sector net debt



All States & Territories 'general government' sector net debt



Budget reforms to build on Premier's 'State of the State' commitments

- The Premier's SotS Speech foreshadowed wide-ranging budget and financial management reforms
 - a charter of Budget responsibility
 - new Financial Management & Audit Acts
 - enhanced independence for the Auditor-General
 - greater openness and transparency in government procurement
- A number of useful reforms could be made (without requiring legislation) to the presentation of next year's Budget Papers
 - totals of discretionary spending and revenue measures
 - reconciliation to previously published forward estimates showing separate impact of 'policy decisions' and 'parameter variations'
 - four-year projections of key economic parameters
 - sensitivity of budget aggregates to changes in economic parameters
 - four-year forward estimates for non-budget sector and public sector as a whole

Summary

- **Tasmania's economy again did well in 2005-06**
 - allowing some further narrowing of gaps with the mainland
- **However Tasmania's economy appears to have slowed – perhaps significantly – over the past few quarters**
 - this partly reflects factors common to other States (particularly those without large resource endowments)
 - but it is also partly due to the end of the 'housing boom' and the associated influx of mainland immigrants ...
 - ... and the completion of a number of major energy projects (with business investment falling away sharply)
 - it's difficult to see the Budget forecast of 3½% growth in Tasmanian economic activity in 2006-07 being attained
- **Tasmania has recorded some impressive productivity growth over the past two years**
 - but the level of productivity still remains very low relative to the rest of Australia
 - improving human capital and enhancing competition are the keys to sustaining improvements in productivity growth
- **Tasmania's public finances are in relatively good shape**
 - new RHH should ideally be funded via a mix of debt and asset sales