FAIR WORK COMMISSION

ANNUAL WAGE REVIEW 2021

NSW GOVERNMENT SUBMISSION

Contents

Introduction

1. The NSW Government makes this submission to assist the Panel in the Annual Wage Review 2020-21.

2. Since formulating our submission to the preceding review, New South Wales has endured one of the most challenging periods since the middle of the last century, with the ongoing impacts of drought, bushfires and the COVID-19 pandemic combining to have a substantial impact on the NSW economy.

3. In this Annual Wage Review, the Expert Panel is required to review the national minimum wage order and modern award minimum wages.[1] The Panel must then make a national minimum wage order, and may make one or more determinations varying modern awards to set, vary or revoke modern award minimum wages.[2]

4. In addition, the Panel must set special national minimum wages for all award/agreement free employees who are junior employees, employees to whom training arrangements apply, and employees with a disability, as well as setting the casual loading for award/agreement free employees.[3]

5. In arriving at its decision, the Panel must balance the economic, social and industrial considerations, relevantly provided for in the *Fair Work Act 2009* (Cth). These are:
   - the performance and competitiveness of the national economy, including productivity,
   - business competitiveness and viability, inflation and employment growth; and
   - promoting social inclusion through increased workforce participation; and
   - relative living standards and the needs of the low paid; and
   - the principle of equal remuneration for work of equal or comparable value; and
   - providing a comprehensive range of fair minimum wages to junior employees, employees to whom training arrangements apply and employees with a disability.[4]

6. In addition, the Panel is required to ensure that modern awards, together with the National Employment Standards, provide a fair and relevant minimum safety net of terms and conditions.[5]

[1] Fair Work Act 2009 s285(1)
[2] Fair Work Act 2009 s285(2)
[3] Fair Work Act 2009 s294
[4] Fair Work Act s284(1)
[5] Fair Work Act s134, also ss3(a), (b), (f) and (g)

Submission

7. The NSW Government believes that the minimum wage is an important safety net for low income households. It also plays a significant role in establishing a benchmark for many other awards and enterprise bargaining agreements in NSW and Australia more broadly. This is particularly important in NSW where significant numbers of workers are reliant on awards.[6]

8. Any approach to setting minimum wages must be balanced and sensitive to prevailing economic and labour market conditions to ensure minimum wage increases do not have a negative effect on employment.

9. Over the last 12 months the NSW economy has faced its most challenging period since the Second World War. A devastating bushfire season was followed by a global pandemic that plunged the world economy into a deep recession. In line with the sharp contraction in the national economy, the NSW economy recorded its first recession in nearly 30 years.

10. The recession in New South Wales has been less severe than witnessed in many other countries. The State's containment measures, and world class health system have been effective in slowing the virus and the worst of the shock appears to be behind us — although recent outbreaks on the Northern Beaches and interstate demonstrates the ongoing risk to the outlook. The careful easing of restrictions in New South Wales and coordinated policy support from the Reserve Bank, Commonwealth and state governments have put the economy in a position to rebound strongly.

11. Gross State Product contracted by 0.7 per cent in 2019-20, the weakest outcome since official statistics were published in the early 1990s. Suppression of the virus and easing of containment measures saw state final demand rebound by 6.8 per cent in the September quarter and a further 2.9 per cent in the December quarter. Much of this reflects a bring forward of activity, so once this initial rebound has run its course, the pace of growth is projected to ease. The level of economic activity (state final demand) remains on track to recover to pre-COVID levels in 2021-22, more than six months sooner than previously expected.

12. Any adjustment to the minimum wage should have regard to the need to support future economic and labour market performance, particularly in the context of recovery from the 2020 COVID recession.

13. The unemployment rate remains well above estimates of full employment and is not expected to return to pre-COVID-19 levels over the forecast horizon. Stimulus from the NSW Government is expected to support a decline in the unemployment rate to 5¼ per cent by June quarter 2024.

[6] ABS, Employee Earnings and Hours, May 2018, Cat.No.6306.0

14. Ensuring that the employment impacts of the coronavirus are minimised should be of paramount importance, and the effects of the Panel's decision should ensure that the economic fallout is minimised.

15. In the 2019-20 Review, the Panel crafted the NMW adjustment with regard to the impact of the pandemic, concluding that:

    'We have decided to award a substantially lower increase this year than that awarded last year due to the marked change in the economic environment and the tax-transfer system and other changes which have taken effect in the current Review period which have benefitted low-paid households. The increases we have awarded are likely to maintain the real value of the wages of NMW and award-reliant employees.'[7]

16. Further, the Panel determined that the timing of the adjustment should have regard to the differential impacts of the pandemic across different industries. To this end, the NMW adjustment was delayed in response to the degree to which industries were most affected by the pandemic.

17. The NSW Government strongly endorses this approach and particularly the careful consideration of the relevant economic circumstances which supports it.

18. While signs of recovery from the recession are becoming evident, the Panel should continue to take a cautious approach to setting the minimum wage. Over the long term, Governments should seek to drive wages growth primarily through other available levers, such as lowering the tax burden, reducing red tape, and implementing productivity enhancing reforms which can contribute to a sustainable increase in wages.

19. In 2018, the NSW Government established the NSW Productivity Commission to examine ways to drive microeconomic reform, make it easier to do business, and lower the cost of living. Following the Commission's Green Paper and the Thodey review of Federal Financial Relations, the NSW Government has initiated a suite of reforms. These reforms are designed to take the first steps in reforming inefficient taxes, deliver a more streamlined and timely planning system to accommodate new businesses, improve student outcomes and ensure workforce flexibility and usher in regulatory changes to support innovation, competition and economic growth.

Economic Outlook

20. The NSW economy has faced unprecedented challenges over the last 12 months. The devastating bushfire season was followed by a global pandemic that plunged the world economy into recession. In line with the sharp contraction in the national economy, the NSW economy has recorded its first recession in nearly 30 years and its worst economic shock in living memory.

21. The recession in New South Wales has been less severe than witnessed in many other countries. The effective containment of the virus allowed for careful easing of restrictions,

[7] [2020] FWCFB 3500 at [130]-[131]; [139]

while a coordinated policy support from the Reserve Bank, Commonwealth and state governments has put the economy in a position to rebound strongly.

22. Gross State Product contracted by 0.7 per cent in 2019-20, the weakest outcome since official statistics were published in the early 1990s. Suppression of the virus and easing of containment measures saw state final demand rebound by a solid 6.8 per cent in the September quarter and a further 2.9 per cent in the December quarter. Much of this reflects a bring forward of activity, so once this initial rebound has run its course, the pace of growth is projected to ease. The level of economic activity (state final demand) remains on track to recover to pre-COVID levels in 2021-22, more than six months sooner than had previously been expected.

23. The unwinding of key Commonwealth support measures will put pressure on the labour market over coming months, but recent momentum suggests that the impact should be manageable—even though the unemployment rate is still not expected to return to pre-COVID-19 levels over the forecast horizon. It will take time for the labour market to fully recover—the unemployment rate is expected to decline to 5¼ per cent by June 2024.

24. The economic outlook is currently subject to an unusually high degree of uncertainty and risk. The Commonwealth has linked the timing of an effective vaccine rollout for COVID-19 to the reopening of international borders – the most significant COVID-19 containment measure remaining, in terms of economic impact. Elevated rates of COVID-19 cases overseas and recent outbreaks within Australia's borders highlight the precarious nature of virus containment.

25. The closure of international borders has lowered the state's population growth to the slowest rate in more than 100 years. This is weighing heavily on short-term economic growth and has severely constrained the state's education and tourism exports. This has had a flow on effect to many other industries.

26. A careful balancing of COVID-19 containment measures and freedom to undertake economic activities—supported by the NSW Government's comprehensive stimulus plan, productivity enhancing reforms, and record investment in infrastructure—will be critical to the continued rebound in confidence and employment in New South Wales.

27. More detailed analysis and forecasting of NSW economic performance appears at **Attachment A**.

Award Reliance

28. As noted in paras 2 and 4 above, the Panel is required to review the national minimum wage order and modern award minimum wages, as well as considering relative living standards and the needs of the low paid.

29. In terms of identifying low paid workers, in the 2020 Decision the majority said that '[a] threshold of two-thirds of median adult full-time ordinary earnings is the benchmark we

use to identify who is ‘low paid’ within the meaning of ss 134(1)(a) and 284(1)(c).’[8] According to the most recent ABS Characteristics of Employment (CoE) survey[9], the full-time median wage as at August 2020 is $1,433 leading to a low paid benchmark figure of $955. The corresponding figures for NSW are $1,426 and $951.

30. In terms of estimating numbers of low paid employees, this has been made more difficult for this review as the statistical series most usually relied upon, ABS Employment Earnings and Hours has not issued a release since May 2018. In the absence of more recent figures, the 2018 figures are again quoted by way of background.

31. In its submission to the 2020 Review, the Australian Government estimated that 1.7 per cent (or around 180,200 employees) were paid the adult rate of the NMW in 2018, using ABS EEH 2018 data[10]. It was further submitted that ‘[i]n 2018, up to 21.0 per cent of Australian employees (or 2.2 million) had their pay set by an award[11].

32. In relation to award reliant employees, the most recently available ABS data[12] (2018) indicated that there are 10,647,200 employees in Australia, of which 9,916,500 are non-managerial. 22.5 per cent of non-managerial employees – 2,232,900 persons – are award reliant. This proportion of award reliant employees had decreased from the 2016 figure of 24.5 per cent.

33. Further, in NSW, approximately 3.07 million employees were situated in the national industrial relations system. Of these, 28 per cent were award reliant[13].

34. NSW had the highest numbers of award reliant employees (904,000) and the second highest on a proportionate basis (28.5%)[14].

35. The majority of award reliant employees were women – 60.9 per cent nationally, and the majority of female award reliant workers were part-time[15].

36. Award reliance was particularly prevalent in the retail, health care and social assistance and accommodation and food services industries where around a third or more of employees were award reliant[16].

37. Over 47 per cent of award reliant employees were casuals[17].

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[8] [2020] FWCFB 3500 at [359], also FWCFB 3500, [2017] FWCFB 1001, [2013] FWCFB 4000
[9] ABS Characteristics of Employment 6333.0 August 2019
[10] Australian Government Submission AWR 2019-20 para 14
[11] Ibid, para 17
[12] ABS Employee Earnings and Hours May 2018
[13] ABS Employee Earnings and Hours May 2018; NSW Public Service Commission *Workforce Profile Report 2019*
[14] ABS Employee Earnings and Hours May 2018
[15] Ibid
[16] Ibid
[17] Ibid

38. Low paid and award reliant employees displayed common characteristics such as gender and casual status[18].

Promoting Social Inclusion

39. The Panel is required to take account, in giving effect to the minimum wage objective, 'promoting social inclusion through increased workforce participation'[19].

40. In the 2019-20 Review, the majority reaffirmed the position put in previous reviews, that being:

    'The recent research, and that discussed in previous Reviews, is consistent with the position adopted by the Panel that modest and regular minimum wage increases do not result in disemployment effects or inhibit workforce participation… The assessment of what constitutes a 'modest' increase has developed over time and the research and available evidence confirms that the increases granted by the Panel in the previous 2 Reviews, and as we have adopted in this Review, fall within that category. Further, the research is supportive of the notion that increases in minimum wages do increase the earnings of the low paid.'[20]

41. While higher minimum wages can provide incentives to workers not in the labour market to seek paid work, that needs to be balanced against potential negative impacts on the supply of jobs for low paid workers.

42. The NSW Government is investing $107 billion on vital infrastructure across NSW over the next four years, supporting the construction of productivity enhancing assets to boost economic growth. Investment decisions have been made in relation to Sydney Metro West, Western Harbour Tunnel, Warringah Freeway Upgrade and the Sydney Fish Market, and initial funding has been allocated.

43. Given, the level of National Minimum wage and the magnitude of minimum award rates of pay will have a significant bearing on the success of these projects and these long-term goals, a stable wage environment is therefore critical.

44. The NSW Government submits the maintenance of a safety net of fair minimum wages must reflect general economic conditions, the needs of business and employment stability.

45. While the virus containment phase had a very significant negative impact on the NSW labour market, with more than 80 per cent of jobs that were lost at the peak of the COVID-19 pandemic in NSW have now been regained. In 2020, unemployment jumped to 6.4 per cent in May, from the year and peaked at 7.2 per cent in July. The NSW Government has ensured that job performance remains strong with the second lowest

[18] Yuen K, Ellis G & Nelms L (2018), *Characteristics of workers earning the national minimum wage rate and of the low paid*, FWC Research Report 3/2018.
[19] FW Act s284(1)(b)
[20] [2020] FWCFB 3500, quoted at [336], footnotes omitted

unemployment rate across the States (6 per cent in January 2021). The NSW participation rate was 65.3 per cent in January 2021..

46. Minimum wage jobs provide employment for low skilled workers, function as an important stepping-stone for new entrants into the labour market, particularly young people, and provide opportunities to develop employability skills that facilitate progression to higher paying jobs.

47. The NSW Government submits that the best way of promoting increased workforce participation is to ensure that the level at which minimum wages are set is appropriately balanced with the continuing provision of employment opportunities.

48. In this context, it is also noted that the tax-transfer system plays a role in relation to the maintenance of an effective safety net for the low paid. The NSW government endorses the view expressed by the majority in the 2020 decision:

    '[357] Consistent with previous Reviews, we have taken account of the interaction between wages and the tax-transfer system in our consideration of 'the needs of the low paid', … and have had regard to various assistance packages introduced by the Australian Government in response to the COVID-19 pandemic. We affirm the position taken by the Panel in previous Review decisions, that it is not appropriate to apply a direct, quantifiable discount to the increase we would have awarded in the absence of such changes; but these changes are a moderating factor in our assessment of the appropriate level of the NMW and modern award minimum wages arising from this Review.

    [358] We also affirm the Panel's previously expressed view that the tax-transfer system can provide a more targeted and efficient approach to addressing poverty among low-income individuals, increasing low-paid households' disposable incomes and sustaining their relative living standards. However, while minimum wage increases are not fully reflected in household disposable income, minimum wages continue to play a large role in improving household income for low-income minimum wage families.'[21]

49. Minimum wages must not act as an impediment to affected workers securing and maintaining employment or regaining employment once out of the workforce. Nor should a minimum floor be set such that it raises costs to a level that hinders an enterprise's competitiveness.

Encouraging Collective Bargaining

50. As noted above, the absence of an ABS EEH data release more recent than 2018, or other relevant data make an understanding of current numbers of award and/or agreement reliant employers difficult. Once again, the 2018 figures are noted by way of background.

[21] [2020] FWCFB 3500 at [357]-[358], footnotes omitted

51. While agreement reliant employees significantly outnumber their award reliant counterparts, in 2018 the proportion of employees whose pay was set by awards rose (from 20.6% in 2016 to 21.0% in 2018), while that whose wages were set by collective agreements fell (from 38.5% in 2016 to 37.7% in 2018)[22].

52. In NSW, the proportion of employees whose pay was set by awards fell from 32.2 per cent in 2016, to 28.5 per cent in 2018. The corresponding figure for 2012 was 18.9 per cent. Collective agreements covered 30.9 per cent of employees, much the same as the 30.8 per cent figure in 2016, which is a decrease from 40.5 per cent in 2012.

53. In the 2020 Review, the majority concluded that:

> '[397] When the wide range of factors which impact on collective bargaining are taken into account, it is unlikely that the adjustments to wages made by the Panel in recent Reviews have discouraged collective bargaining, particularly in light of the increase in collective agreement coverage in at least some of the award-reliant industries. It is also likely that the impact of the COVID-19 pandemic will be felt in the extent and nature of bargaining in the immediate future, although the precise impact is difficult to predict with any certainty at this juncture.
>
> [398] For the reasons given, it is likely that an increase we determine in a Review may impact on bargaining in different sectors in different ways and we cannot be satisfied that the increase we have determined will encourage collective bargaining. We have taken this into account along with the other statutory considerations in determining the outcome in this Review.'[23]

54. The most recent available data from the federal Attorney General's Department[24] indicates that the number of agreements approved in the September 2020 quarter has decreased to 715, from 762 in the previous quarter. The number of employees in the September 2020 quarter covered has decreased to 60,600, from 142,600 in the June quarter.

55. Data from different sectors displays a mixed picture: construction agreements decreased significantly (from 370 to 305 March – September), as did manufacturing (from 180 to 111), accommodation and food services (8 to 4) and retail trade agreements (from 13 to 6). Transport postal and warehousing and wholesale agreements remained steady (from 86 to 83 and 20 to 19 respectively) while agriculture, forestry and fishing was the only sector to see an increase in the last two quarters (from 5 to 12).

56. Further, private sector agreements approved in the September quarter provided an average 2.7 per cent pay rise over 2.8 years, a reduction from 3.0 per cent in the June quarter and 2.9 per cent in March 2020[25].

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[22] ABS Employee Earnings and Hours 2018
[23] [2020] FWCFB 3500 at [397]-[398]
[24] Trends In Enterprise Bargaining September Quarter 2020 Report, published 18 December 2020
[25] Ibid

57. The NSW Government submits that it is critical that a sustainable safety net of minimum wages is one that supports enterprise bargaining at NSW workplaces. In particular, the Panel should continue to set minimum wages at a level that continues to maintain incentives for enterprise bargaining that rewards flexible and productive work practices.

Conclusion

58. The ongoing recovery from the 2020 pandemic recession in NSW should not be jeopardised or inhibited by overly generous wage outcomes that are out of step with the economy. On the other hand, it must be acknowledged that the national minimum wage is an important safety net for low income households, as well as being a significant benchmark for awards and enterprise agreements.

59. The NSW Government submits that the correct approach to addressing these issues is for the Panel to take a cautious approach to this Review, on the basis that governments should seek to drive wages growth by means of a vigorous productivity agenda, including measures such as lowering the tax burden, reducing red tape, and implementing forward looking regulation to support competition and innovation.

Attachment A - The NSW Economy

Performance of the NSW Economy

The NSW economy has faced monumental challenges over the last 12 months. The devastating bushfire season was followed by a global pandemic that has plunged the world economy into deep recession. In line with the sharp contraction in the national economy, the NSW economy has recorded its first recession in nearly 30 years.

The recession in New South Wales has been less severe than witnessed overseas. The effective containment of the virus allowed for careful easing of restrictions, while a coordinated policy support from the Reserve Bank, Commonwealth and state governments has put the economy in a position to rebound strongly.

Gross State Product contracted by 0.7 per cent in 2019-20, the weakest outcome since official statistics were published in the early 1990s. Suppression of the virus and easing of containment measures saw state final demand rebound by a solid 6.8 per cent in the September quarter. Much of this reflects a bring forward of activity, so once this initial rebound has run its course, the pace of growth is projected to will ease. The level of economic activity (state final demand) remains on track to recover to pre-COVID levels on 2021-22, more than 6 months sooner than previously expected.

The unwinding of key Commonwealth support measures will put pressure on the labour market over coming months, but recent momentum suggests that the impact should be manageable—even though the unemployment rate is still not expected to return to pre-COVID-19 levels over the forecast horizon (expected to decline to 5¼ per cent by June 2024).

The economic outlook is subject to an unusually high degree of uncertainty and risk. The Commonwealth has linked the timing of an effective vaccine rollout for COVID-19 to the reopening of international borders – the most significant COVID-19 containment measure remaining, in terms of economic impact. Elevated rates of COVID-19 cases overseas and recent outbreaks within Australia's borders also highlights the precarious nature of virus containment.

The closure of international borders has lowered the state's population growth to the slowest rate in more than 100 years. This is weighing heavily on short-term economic growth and has severely impacted the state's education and tourism industries

A careful balancing of COVID-19 containment measures and freedom to undertake economic activities—supported by the NSW Government's comprehensive stimulus plan, productivity enhancing reforms, and record investment in infrastructure—will be critical to the continued rebound in confidence and employment in New South Wales.

Household consumption

Household spending has been impacted by several factors, including social distancing restrictions, changes to business operations, major job losses and volatile confidence. The result was a plunge in household consumption of almost 14 per cent in the June quarter 2020. Subsequently, the success in bringing COVID-19 under control allowed social distancing restrictions to be relaxed whilst buoying confidence in New South Wales. In response, consumer spending rebounded by nearly 11 per cent in the September quarter.

Subsequent clusters of COVID-19 cases likely disrupted consumer spending in the December quarter, as social distancing requirements were partially tightened. However, household consumption still increased by more than 3 per cent in the quarter, and consumer confidence has held up. While the recovery in household consumption is expected to continue, similar and potentially more severe outbreaks cannot be ruled out in the future.

A coordinated effort at both the State and Commonwealth levels of government to support the economy was instrumental in smoothing the severity of the initial downturn. Commonwealth support has been principally delivered through the JobSeeker and JobKeeper programs, which have provided direct income support to households and businesses. While the winding up of these support measures presents some potential risk to the near-term outlook, the labour market has improved more than expected at the time of Budget, while other government measures—including $29 billion in NSW Government stimulus—will help manage the transition away from emergency support measures.

Dwelling investment

The closure of the international border is reducing the level of net international migration to New South Wales. The reduction in population growth is a drag on housing demand and, therefore, is a headwind to the outlook for dwelling investment.

By the December quarter 2020, new dwelling investment in New South Wales had declined for ten consecutive quarters after reaching a record high in mid-2018. A high level of new dwelling completions combined with rapidly diminishing population growth, reductions to income and jobs due to COVID-19 and a shift of short-term rentals into the long-term market all placed upward pressure on the rental vacancy rate in Sydney last year. As a result, rents in Sydney have been falling. In contrast, Sydney dwelling prices have shown incredible resilience with the support of very low interest rates.

Rising prices and government stimulus measures, such as the extension of the Commonwealth's HomeBuilder grant, are providing partially offsetting support for dwelling investment in the near-term – contributing to an 2.1 per cent increase in dwelling investment for the December quarter, primarily driven by renovation activity. Nonetheless, much of this represents a pull-forward of demand and dwelling investment is still expected to see further declines over coming years.

Public final demand & business investment

The public sector was one of the few sources of growth for NSW in 2019-20, as health spending was increased in response to the virus and economic support/stimulus measures were deployed at all levels of government. Underlying public demand contributed more than 1½ percentage points to Gross State Product (GSP) growth in 2019-20, almost three time its historical average. A further large contribution is expected in 2020-21.

Aside from other income support measures (such as the acceleration of personal income tax cuts and $29 billion in stimulus measures from the NSW Government), the state governments record $107 billion (over four years) infrastructure program will also make a meaningful contribution to economic growth.

Along with an ambitious reform agenda, these measures will also help to support private business and investment. Businesses will benefit from reduced red tape, faster planning approvals, reforms to credit and insolvency laws, subsidised training, improvements in labour mobility, loss carry back provisions and full asset write-offs.

Labour market

Around 270,000 workers lost their jobs in New South Wales during the peak of the virus containment phase in April and May. The unemployment rate subsequently jumped to 6.4 per cent in May, from 4½ per cent at the start of 2020. While a significant increase, the result was tempered by the fact that most workers laid off in April and May temporarily left the labour market, driving the participation rate down to a more than 15 year low. Were it not for Government support measures and people leaving the labour market, the unemployment rate could have increased to more than 15 per cent in April.

The labour market has been recovering better than initially expected, with the unemployment rate peaking at 7.2 per cent in July 2020 before steadily improving to 6.4 per cent in December. The initial recovery in employment since the peak of the pandemic has varied across industries. Health Care and Social Assistance, the biggest employer, has contributed the largest drag to overall employment due to restrictions on elective surgeries, aged care services and social assistance. This was followed by the hospitality industry, which was significantly affected by social distancing measures and restrictions. While there is a risk of further deterioration once the JobKeeper program concludes in March, current momentum suggests any loss of jobs should be relatively contained.

At the time of the Half Yearly Review, the labour market recovery was projected to result in a 300,000 increase in employment by 2024, from the pandemic low in the June quarter 2020. This is forecast to contribute to a decline in the unemployment rate to 5¼ per cent by June 2024.

Population

The New South Wales population grew by 0.9 per cent over 2019-20, although there was almost zero increase in population during the June quarter 2020. The Commonwealth Budget and MYEFO indicated that almost no population growth was expected for the next two years, largely due to weak net overseas migration (NOM). A net outflow of migration is expected for the first time since 1946, with no catch-up in subsequent years, leaving the level of population permanently lower than expected prior to the pandemic.

Based on current Commonwealth policy settings and assumptions, this will reduce NSW population in 2023-24 by around 375,000 people compared to projections at the 2019-20 Half Yearly Review. The closed international border is the most significant remaining COVID-19 containment measure in place, in terms of the impact on population growth and flow-on effects for GSP over the forecast period.

Inflation

Headline inflation measures have experienced some short-term volatility due to the impact from one-off factors such as the waiver of childcare fees and delayed increases in other administered prices. Headline inflation subsequently spiked in the second half of 2020 as these factors began to unwind.

Measures of underlying inflation are much less volatile and have held up somewhat better than expected in an environment of uncertainty and significant spare capacity—as evidenced by the elevated unemployment rate.

Nonetheless, several factors are expected to keep inflationary pressures somewhat subdued going forward. The unemployment rate is forecast to remain above estimates of full employment until at least mid-2024, keeping wages growth muted. Additionally, elevated rental vacancy rates will continue to weigh on rental price growth, while spare global industrial capacity, the easing of drought conditions and a gradual appreciation of the Australian dollar will all help to keep consumer inflation contained.

Wages

Wages growth in NSW eased sharply to 1.4 per cent through the year to the September quarter 2020 and remained at this pace in the December quarter. In nominal terms, growth in the NSW private sector wage price index (WPI) was 1.4 per cent, while nominal growth in the NSW public sector WPI was 1.1 per cent—reflecting the wages of Commonwealth, State and Local Government workers (including the NSW Industrial Relations Commission's recent decision to grant a 0.3 per cent increase for many NSW public sector employees in 2020-21).

Improvements in the labour market have also improved the outlook for wages growth. However, the outlook for wages growth remains weaker than before the pandemic, with private sector wages growth expected to ease through the course of 2020-21, before gradually picking up as the labour market strengthens.

The change in the NSW wages policy cap to 1.5 per cent from the previous 2.5 per cent will also see public sector wages growth slower than in previous years. In addition, scheduled annual increases of 0.5 per cent in the superannuation guarantee starting from 1 July 2021 are expected to detract from wages growth.

Australian Economic Outlook

The overwhelming disruption from COVID-19 has been felt right across Australia, with the nation plunging into recession in the June quarter 2020. National Gross Domestic Product (GDP) contracted by 0.3 per cent in the March quarter then dropped 7 per cent in the June quarter, to be down 6.4 per cent over the year—the worst decline in recorded history. Household consumption contributed the most to the decline, although private investment also fell. In contrast, public spending increased, supported by the health response, while international trade actually contributed to growth as imports fell faster than exports.

The economy partially rebounded in the September quarter as successful suppression of the virus in most states lifted confidence and allowed the more severe containment measures to be wound back. GDP increased 3.3 per cent in the September quarter. A COVID outbreak in Melbourne that resulted in additional lockdown for the state muted the size of the rebound. The recovery continued into the December quarter, with GDP increasing another 3.1 per cent in the quarter.

Similar to the experience in New South Wales, the national labour market saw a significant loss of employment over April and May (870,000 jobs), which caused the unemployment rate to spike to 7½ per cent by July—an outcome that would have been much worse without an emergency response by governments. However, the reopening of the economy has seen the unemployment rate improve to 6.4 per cent by early 2021.

The Australian economy is expected to see solid growth over coming years as the recovery continues, although there is considerable risk and uncertainty around the outlook. Ongoing support from emergency fiscal support measures, low interest rates, significant spending on infrastructure, economic reforms and tax cuts are helping to hasten the recovery. This should support solid employment growth, which would see the unemployment rate dip back below 6 per cent in coming years—although remaining well above the rate consistent with full employment.

World Economic Outlook

The International Monetary Fund released an updated World Economic Outlook in late January suggesting a relatively positive outlook (given the current situation) for the global economy. The global economy is projected to grow by 5.5 per cent in 2021 and 4.2 per cent in 2022. The 2021 forecast was revised up (0.3 percentage points) relative to expectations late last year, reflecting expectations of a vaccine-powered strengthening of activity later in the year and additional policy support in a few large economies. The upward revision was particularly large for advanced economies.

This outlook appears somewhat upbeat given still elevated levels of global COVID-19 infections, which led to renewed restrictions in some countries and jurisdictions from late last year. However, the IMF expect the softer economic momentum will only be temporary and contact intensive activity will strengthen in the June quarter as vaccines and therapies become more readily available.

Additional fiscal policy support is set to boost activity in some countries, while major central banks are assumed to maintain their current (highly accommodative) policy rate settings throughout the forecast horizon to the end of 2022.

Risks to the outlook

Uncertainty remains higher than usual despite an accelerated recovery. There are risks both to the upside and downside, although the unpredictable nature of the pandemic generally leaves the risks more weighted to the downside.

Risks around the health-related outcomes are the most notable. This includes expectations around the vaccine rollout and effectiveness. The implications of any deviation in vaccine assumptions are potentially significant as it could increase the chances of a large scale outbreak and/or require social distancing measures to remain in place for longer.

Forecasts do not anticipate an outbreak event requiring a Greater Sydney lockdown.

The virus situation overseas remains precarious. Any lack of progress towards containing (and reducing) infections globally could result in governments keeping international borders closed for longer – this would be a major drag on economic activity. It may also have longer-term implications for the economy through a faster ageing of our population, an increased skills mismatch, and may impact the long-term potential of industries like education.

A further escalation of geopolitical tensions with China is another significant risk that could have a sizeable impact on NSW exports. In many cases, goods subject to trade restrictions should find new export destinations, albeit probably at a lower price. That is unlikely to be the case for services exports, however. Therefore, if trade tensions persist beyond the reopening of international borders and incorporates travel warnings and further such restrictions, this would be a cause for greater concern.

More near-term risks revolve around the unwinding of temporary Commonwealth Government policy support. For example, around 165,000 firms in New South Wales were receiving JobKeeper late last year, albeit down from more than 350,000 in September. Current recipients represent more than 500,000 workers.

The dominant upside risk relates to households. There is potential for a faster recovery in household spending, the largest share of the state economy. Households may draw on their accumulated savings more quickly than has been forecast, now that the worst of the pandemic seems to have passed. Moreover, consumer confidence has recovered strongly and robust home construction activity often stimulates higher consumer demand. Finally, the falling jobless rate means more households will have the means to lift their spending. Each of these positive impacts could be more pronounced than currently is forecast.