

SEPTEMBER QUARTER 2022

Newsletter

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SEPTEMBER 2022

From the CEO's Desk



2022 is flying by, with the September quarter almost a distant memory and the race to December picking up pace with Christmas decorations already in stores and bookings being finalised for end of year holidays! This year however, continues to be marked by mixed experiences, with economies and communities around the world remaining stoic in the face of rising recession concerns and geopolitical tensions.

The quarter saw an acceleration of central bank activity, as policy makers raced to get in front of inflation. Domestically, the RBA raised rates by 150 basis points in the quarter, taking the cash rate to 2.35% as at 30 September 2022. While this level is a return to more normal monetary policy from the artificial lows during the COVID-19 pandemic, the pace of these increases was the quickest in almost three decades.

Financial markets continue to price in further rate hikes in response to strong economic data and persistently high inflation, although the volatility has moderated since the large spikes at the beginning of the calendar year. The WATC October 2031 bond (our closest to the 10 year part of the curve) traded at 4.45% at the quarter close, up from 4.15% at the beginning of the quarter.

Currency markets continue to respond to global economics, with major currencies now reflecting fears of a widespread recession. The Australian dollar fell against the greenback by over 7.3% for the quarter, and the British pound slipped to its lowest level against the US dollar since the 1980s. Currency fluctuations of this size point to more market volatility in the coming months.

The Western Australian economy continues to be strong, with almost record low unemployment and close to record high labour force participation supporting strong business and household spending. The Perth CPI increased by 7.4% through the year, although this number is partially distorted by the one-off electricity subsidy and strongly impacted by supply side cost impacts in the new dwelling sector.

The Annual Report on State Finances was released in September 2022, reflecting a slight improvement on the 2021-22 general government operating surplus to \$6 billion. Net debt continued to trend downwards reflecting the strong cash surplus of the public sector, and agency borrowings through WATC were reduced by \$2.2 billion year on year.

A key focus of the period has been progressing the work on the

Bond Financing Framework. During August we were happy to welcome ANZ and UBS to the role of joint sustainability advisors to assist us with this important work. The Bond Financing Framework will create the foundation for WATC to engage with the investor community on our approach to labelled issuance, and set out the process and governance we will follow to support the identification, reporting and communication of future labelled issuances. This work builds on the 2021 ESG Information Pack and the more recent update as part of the 2022-23 State Budget.

During 2021-22 WATC engaged with over 450 clients through our education and training programs. This trend is continuing into the current year, where we recently hosted an online economic presentation looking into the global drivers affecting infrastructure projects and technology procurements.

From 1 July 2022 new documentation and information requirements were put in place for local government loan applications. This enhancement of WATC processes is part of the broader review into our lending practices during the previous year, and seeks to support continued lending to the local government sector in a responsible and sustainable manner. A series of resources have been developed to assist and support our local government clients to navigate the new lending framework, including guidance on how to complete a new loan application.

Internally at WATC, we have waved goodbye to a number of our long standing team members. Julia Tyzack, Chief Accountant, Adrian Koelewyn, Chief Dealer Offshore Markets and Financial Markets, and Steve Luff, Chief Financial Officer all retired during the quarter. Taking with them an almost 90 years of combined service to WATC, their contribution will be long felt and missed. We wish them all the very best for a long and healthy retirement.

While sad, the retirement of long standing staff has created an opportunity to recruit some new faces to WATC – I welcome all of our newcomers and know they look forward to engaging with our stakeholders through their various roles.

A handwritten signature in dark ink, appearing to read 'Kaylene Gulich'. The signature is fluid and cursive, written in a professional style.

Kaylene Gulich
CEO



THE ECONOMY

The Cost of Price Stability

'While higher interest rates, slower growth, and softer labour market conditions will bring down inflation, they will also bring some pain to households and businesses. These are the unfortunate costs of reducing inflation. But a failure to restore price stability would mean far greater pain.'

Fed Chair Jerome Powell, 26 August 2022

The Global Economy

The US data has been mixed in Q3, but generally pointed to the resilience of the economy to the acute cost and price pressures.

In Q2, US GDP saw the second quarterly decline in a row, which marks a technical recession. This

appears to have been a false signal, however, with economic data for Q3 so far being largely on the strong side. Retail sales and personal consumption expenditures rose in August, though this followed declines in the previous month. The reports on industrial production and the PMI surveys suggest that manufacturing growth has softened in recent months.

The strength of the US labour market continues. Non-farm payrolls still posted solid monthly gains and are now 240 thousand higher than when COVID-19 hit. The unemployment rate edged up to the still low 3.7% in August, but this was due to a rise in labour force participation. Average hourly earnings growth remains at a rapid 5.2% YoY.

At the same time, US inflation is still high. The annual rate of headline PCE inflation declined to the still elevated 6.2% in August, but core inflation rose back to 4.9% (the highest level since April). CPI inflation rates are also high, at 8.3% and 6.3%, respectively. Fed officials have been stressing that restoring price stability will likely be at the cost of sub-trend economic growth going forward.

Europe, more directly impacted by the spill-overs from the war in Ukraine, is definitely in a mild contraction that is likely to get worse. Inflation is also establishing new record highs in the euro area.

The Chinese economy continues to struggle with multiple headwinds. In Q2, real GDP declined by 2.6% QoQ, to be just 0.4% up through the year. The PMIs and external trade figures for July and August generally pointed to ongoing weakness, amid the COVID-zero policy and power supply shortages due to the drought. However, the weakness was not confirmed by the official activity data. The troubles in the property sector

continue, despite the attempts from the Chinese government and the central bank to support the crippled sector.

The Australian Economy

Australian economic conditions remain sound. Real GDP rose by another 0.9% in Q2, thanks to resilient household consumption and strong exports amid increased demand for fossil fuels and iron ore. Investment showed some weakness, mainly due to the underperformance of construction amid high costs of materials and labour.

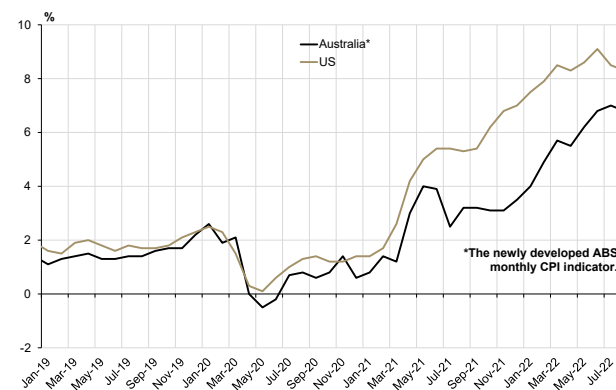
Economic data for July showed the continuation of trends from the national accounts report, with strong retail trade and consumer goods imports as well as solid, though slightly weaker, commodity exports. Building approvals have been volatile, with a drop in July more than fully reversed in August. These mixed results notwithstanding, the business surveys suggest the construction sector is facing tough conditions, despite business conditions and confidence remaining strong across most other industries. House prices declined throughout Q3, but remain well and truly above the pre-pandemic levels.

Annual CPI inflation rose to 6.1% in Q2 and the experimental monthly CPI indicator as well as the Melbourne Institute inflation gauge suggest that

inflation picked up further in Q3. Consumer inflation expectations and the perception of inflation by households remain elevated compared to the previous years, feeding into depressed consumer confidence.

The labour market conditions are still very strong. Employment rose by another 33.5k in August, following a drop of 40.9k in July, to be up 4.4% YoY. The unemployment rate was 3.5% in August and the labour force participation remains high at 66.6%. The low underemployment rate and near-record hours worked suggest that the labour market is very tight.

Annual Rates of US and Australian CPI Inflation



Source: ABS, BLS

Despite the tightness in the labour market, aggregate wage growth remains subdued in Australia. The wage price index picked up by just 2.6% YoY in Q2. The business surveys continue to suggest strong labour cost growth, supported by a 5.2% hike in the minimum wage.

The Western Australian Economy

Western Australian real state final demand rose 0.1% in Q2, to be up by 3.3% YoY. This followed strong increases in the previous quarters. Household consumption remained solid, rising by 1.4% in Q2, though this was almost fully offset by declines for other expenditure categories.

The strength in household consumption continued into Q3, with nominal retail trade rising by 1.6% MoM and 10.5% YoY in July. However, in the case of nominal data, it is hard to disentangle the higher real spending from the impacts of the surge in retail prices.

Western Australia continues to boast the strongest labour market of the states. The unemployment rate of 3.1%, is the lowest and the participation rate of 69.3% the highest of the states.

The Perth CPI rose by 1.7% in Q2, slightly less than the national average of 1.8%. Despite this, it was still 7.4% up through the year, partly due to higher out-of-pocket expenses for electricity

and new dwellings after the expiration of the government support programs.

Financial Markets

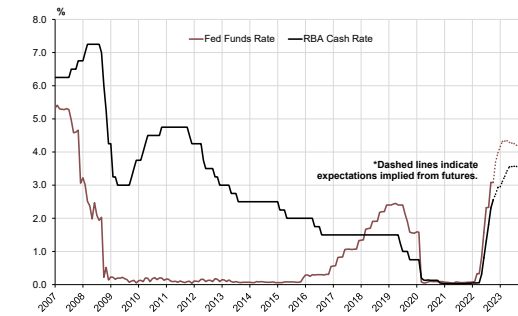
Trade on financial markets has remained volatile in Q3, as monetary policy tightening continues across the advanced economies.

The Fed has increased the fed funds rate target range by a total of 150bps this quarter, to 3.00-3.25% and, starting from September, doubled the pace of reduction of its balance sheet to US\$95b a month from US\$47.5b in the previous three months. The FOMC members, including Fed Chair Jerome Powell, continue to declare their commitment to bringing inflation down to its 2% goal and stress that this will likely require a period of sub-trend economic growth. The markets expect that the fed funds rate target range will peak at around 4.50% in Q2 2023.

Monetary policy tightening also continues in the other major advanced economies, with the notable exception of the Bank of Japan. In Q3, the European Central Bank increased its deposit rate from -0.50% to 0.75%, the highest rate since early 2009, and signalled more large increases in the coming months. The Bank of England's bank rate is now at 2.25%.

The Bank of Japan continues to maintain ultralow interest rates, including the

Effective Central Bank Benchmark Rates*



Source: Refinitiv

10-year Government Bond Yields



Source: Refinitiv

AUD/USD Closing Rates



Source: Refinitiv

complimentary deposit rate at -0.10%. However, it has decided to intervene in the foreign exchange market for the first time since 1998.

At home, the RBA has increased its cash rate by a cumulative 175bps in Q3 and early October, taking the cash rate target to 2.6%, which is the highest level since 2013. RBA Governor Philip Lowe has signalled that further interest rate increases can be expected in the months ahead, but stressed that decisions will be data-dependent. The markets expect that the cash rate will peak at around 3.50% by mid-2023.

The further increase in central bank interest rate expectations saw government bond yields resume their ascent after a temporary decline in June and July. The rise in bond yields gathered pace over the last week of the quarter, driven by contagion from a sell-off in the UK after the government announced a huge expansionary fiscal package, including the largest tax cuts in 50 years. The sentiment stabilised somewhat after the Bank of England stepped in with temporary long-term gilt purchases and the British government itself eventually abandoned the tax cuts in early October.

Equity prices are somewhat down for the quarter, both in the US and Australia. The scale of declines was limited by a rally in the first half of the quarter, which was fully reversed amid concerns over the

negative impacts of monetary policy tightening on economic growth.

Growth concerns, coupled with multiple headwinds faced within the Chinese economy, have also translated into a 23.4% drop in oil prices in the quarter. Iron ore futures plunged as well, by 20.1%. This was reflected in a 7.9% fall in the CRB index in Q3, despite the 12.4% rise in coal prices and a 13.3% increase in LNG prices, amid further geopolitical disruptions in Europe.

The weaker global market sentiment towards the end of the quarter, as well as the decline in iron ore prices and troubles in China, weighed on the AUD in Q3. The scale of depreciation was particularly strong against the US dollar, as the USD index reached a record high towards the end of the quarter. The AUD/USD slid 7.2%, to touch the lowest level since May 2020 at the end of the quarter. ■



Craig McGuinness
CHIEF ECONOMIST



Patrycja Beniak
ECONOMIST

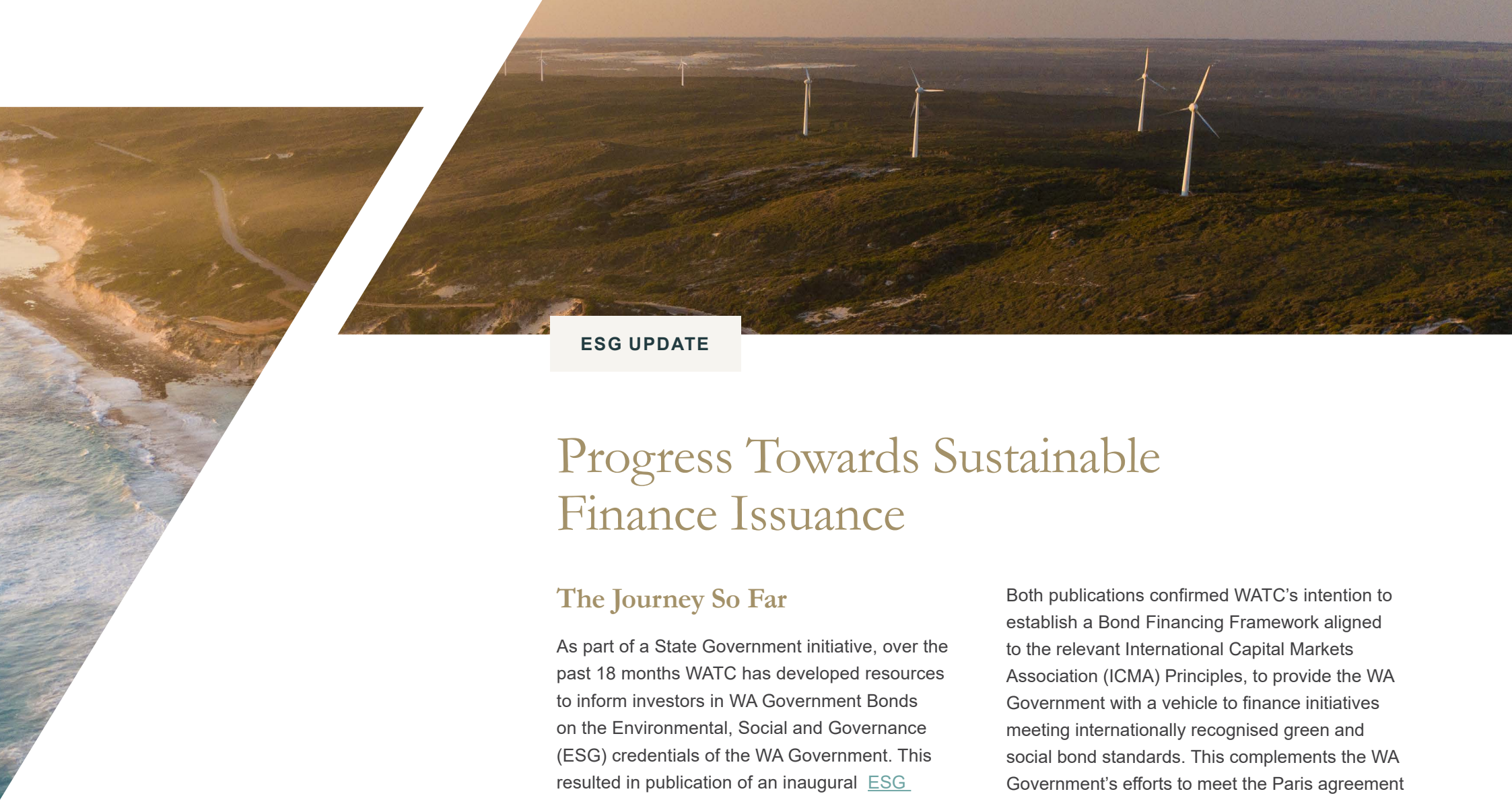
For More Publications

Access an extensive range of economic and market-related updates via the WATC website.

[View Market Updates](#) →

[View Economic Indicators](#) →





ESG UPDATE

Progress Towards Sustainable Finance Issuance

The Journey So Far

As part of a State Government initiative, over the past 18 months WATC has developed resources to inform investors in WA Government Bonds on the Environmental, Social and Governance (ESG) credentials of the WA Government. This resulted in publication of an inaugural [ESG Information Pack](#), launched by the Premier in November 2021 and a subsequent update following the May 2022 budget release.

Both publications confirmed WATC's intention to establish a Bond Financing Framework aligned to the relevant International Capital Markets Association (ICMA) Principles, to provide the WA Government with a vehicle to finance initiatives meeting internationally recognised green and social bond standards. This complements the WA Government's efforts to meet the Paris agreement objective of net-zero greenhouse gas emissions by 2050 and progresses the objectives of the United Nations Sustainable Development Goals.

September Quarter Progress

Following a formal procurement process, WATC recently appointed ANZ and UBS as Joint Sustainability Advisors to work with WATC to establish a contemporary Bond Financing Framework, aligned with the relevant ICMA Principles. The Framework will underpin WATC's initial green or sustainability bond issuance, expected in the second half of this financial year.

Good progress has been made on the Framework, with ANZ and UBS assisting WATC to:

- Review a preliminary list of projects as potential candidates for sustainable finance. This has involved applying detailed screening criteria from the relevant international guidelines;
- Develop an outline of documentation that will describe WATC's sustainable finance issuance process as relied on by investors; and
- Procure a Second Party Opinion provider to assess compliance to international standards of WATC's proposed approach which supports investor participation.

A governance reporting process has also been established through the Portfolio Oversight Group for Climate Action and the Environment, chaired

by the Department of Water and Environmental Regulation (DWER) and supported by an agency working group coordinated by WATC.

Agencies formally represented in the working group include the Department of Transport and Treasury, together with Energy Policy WA. Broader engagement includes key delivery agencies such as Western Power, Synergy, Horizon Power, Water Corporation and Department of Communities and policy agencies such as the DWER. Several projects targeted for inclusion are aligned to delivery of the WA Climate Policy, such as Metronet, the Electric Vehicle Strategy and Energy Transformation Strategy – the latter being reinforced by the Government's recent commitment to \$3.8 billion in expenditure on renewable energy to assist in the phasing out of coal fired power stations by 2030.

Want to find out more?

Contact Richard McKenzie, Head of Strategy for more information. Call (08) 9235 9127 or email rmckenzie@watc.wa.gov.au. ■



Richard McKenzie
HEAD OF STRATEGY

‘WATC recently appointed ANZ and UBS as Joint Sustainability Advisors to work with WATC to establish a contemporary Bond Financing Framework, aligned with the relevant ICMA Principles’.

More ESG Releases

Access additional environment, social and governance-related publications via our website.

[View Sustainability Page →](#)

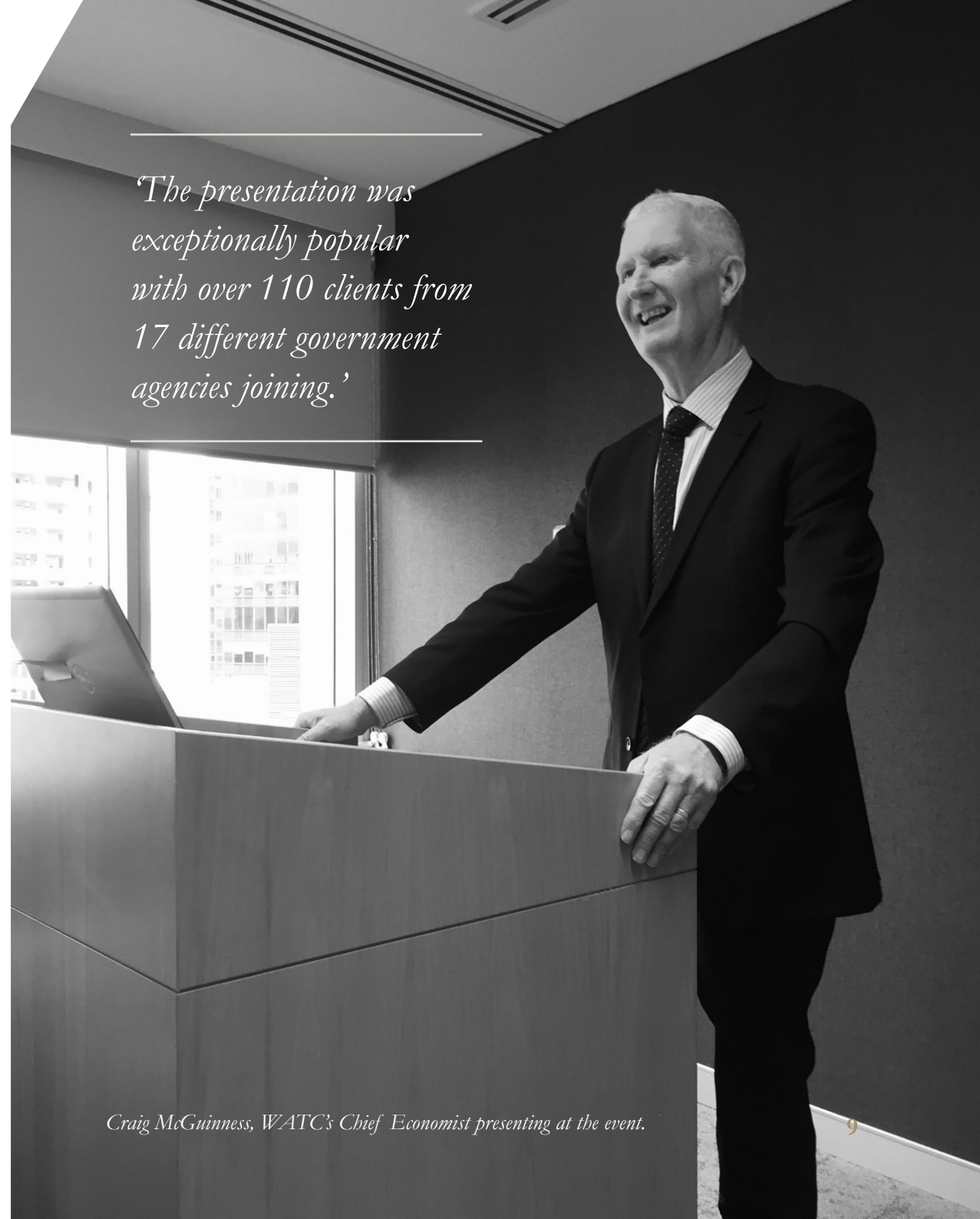
Online Economic Mini-series

The Economic Services Team at Western Australian Treasury Corporation (WATC) delivered our inaugural Online Economic Mini-series on Wednesday, 21 September 2022. Craig McGuinness, WATC's Chief Economist, provided valuable insights into the global drivers affecting the Western Australian government's infrastructure projects and technology procurements. The presentation was exceptionally popular with over 110 attendees from 17 different government agencies joining the 40-minute session.

At WATC, we are continually looking for ways to provide value for clients through leveraging our financial market and economic expertise. The mini-series concept is a contemporary approach to enhancing knowledge and understanding within the public sector, and to assist our clients make more informed financial decisions. This initiative will continue to evolve, and we hope to provide other online and in-person offerings in the future.

Do you have feedback?

If you have ideas for a mini-series topic or would like a tailored presentation delivered to your organisation, please contact your WATC relationship manager or email csoperations@watc.wa.gov.au. ■



'The presentation was exceptionally popular with over 110 clients from 17 different government agencies joining.'

New Local Government Lending Framework

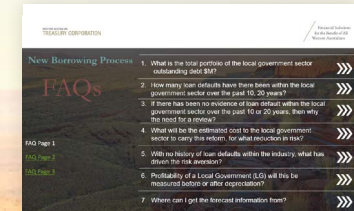
As the primary provider of term debt funding to local governments across the State, Western Australian Treasury Corporation (WATC) supports the financial sustainability of the local government sector and is committed to continue lending in a responsible and sustainable manner. In support of this commitment, on 1 July 2022 WATC implemented its new local government lending framework.

A series of resources have been developed to assist and support our local government clients to navigate the new lending framework, including guidance on how to complete a new loan application. All resources are available to view and download from the WATC client portal.

We recommended that our local government clients take the time to view the resources provided before applying for funding. The new loan application form, also available through the client portal, is required for all loan applications submitted after 1 July 2022.

Do you have a query?

Please email lglending@wac.wa.gov.au. ■



Accessing Client Resources

WATC's Local Government Clients can log into our portal to access a range of resources and instructional information.

[WATC Client Portal Login](#) →



PUBLICATIONS

WATC 2022 Annual Report Now Available Online

About This Report

For some months now, people across our organisation have been working hard to prepare a variety of contributions for our Annual Report.

The report itself is designed to provide information about the services and performance of Western Australian Treasury Corporation and includes strategic highlights, operational summaries, audited financial statements and performance indicators for the financial year ending 30 June 2022.

Key Highlights Snapshot

Despite the volatility of the last year, there were some solid achievements across our organisation. Some highlights from the last financial year include:

- **\$47.8 billion Client Debt**
We successfully managed and delivered on all client borrowing requirements during a year of heightened market volatility.
- **\$5.5 billion Client Funds Managed**
We successfully managed five client

investment portfolios in accordance with approved policy frameworks.

- **\$446.1 million Client Foreign Exchange**
We transacted in 11 currencies on behalf of 20 clients and assisted in effectively managing their foreign exchange risk.
- **450+ Building Knowledge**
We engaged with over 450 client contacts through our education and training programs, industry forums and economic presentations.

Performance Against Targets Snapshot

To ensure that WATC meets its objectives, our Board, with the agreement of the Premier, sets our annual performance targets. These targets are challenging and, when attained, ensure real benefits are delivered to our clients and the State.

Key Performance Indicators

To ensure we continue to deliver on client requirements we have a number of client focused key performance indicators. These indicators for last financial year included:

- **Estimated Interest Rate Savings**
At WATC, we aim to deliver value to our

clients and the State with target savings of greater than 0.00%. The outcome for the 2021/22 financial year was that **our target was achieved, with savings estimated in the range of 0.33% to 0.84%**. Through centralising the management of the State's debt we continued to deliver significant interest rate savings to our clients and the State.

- **Client Satisfaction**

We strive to be the best at providing financial solutions for our public sector clients and work to a target of 90% Client Satisfaction (with an aspirational target of 100%). Our Client Satisfaction result for 2021/22 was 100%, confirming that WATC continues to deliver valued financial solutions to clients.

Feedback received from clients who engaged with our advisory services was very positive. One hundred per cent of clients surveyed were very to extremely satisfied with the quality of advice we provided, the value we added to their project, our overall capability, and the service we provided.

To access a variety of insights into the work carried out at WATC over the last year, view the annual report in full via the link below.

Do you have feedback?

If you have any queries or would like to provide feedback on our 2022 Annual Report please email marketingandcommunications@wadc.wa.gov.au. ▀



WATC Annual Reports

To access our latest Annual Report, as well as Annual Reports from previous years, visit our website.

[2022 Annual Report](#) →

[Previous Annual Reports](#) →

New Appointments



Henry Cattan

Henry joined WATC in June 2022 as a Risk Analyst with the Risk Management team. He has a Bachelors Degree in Economics from the University of Arizona. Henry previously worked as a portfolio analyst for an electrical utility in the United States and as the Finance Coordinator for a paediatric therapy clinic in Karratha. Outside of work he enjoys watching movies and taking his dog for walks.



Mia Cara-Southey

Following a secondment from an Executive Assistant (EA) role at the Department of Treasury, Mia has been appointed as EA to the CEO in the WATC Business Administration team. Prior to Treasury, Mia worked as a Personal Assistant and Operations Administrator in an organisation providing opportunities for young people and adults with physical and learning disabilities in Devon, UK. Outside of work, Mia spends most of her time in the water and is a passionate open water swimmer (she swam solo to Rottneest in February) and loves the outdoors in general.

New Staff Roles



Dan Manning

Following an internal secondment from Advisory Services to Risk Management, Dan has been appointed to the role of Chief Risk Advisor in the Risk team. Dan is primarily responsible for Credit Risk Management activities and has recently been assisting with the delivery of the new local government lending application and assessment process. Prior to WATC Advisory Services Dan had extensive experience in risk management at both Western Power and NAB.



Carol Whitworth-Hird

STAFF SECONDMENT

Carol is on an internal secondment from her role as a Chief Advisor in WATC's Advisory Services team and is moving to the role of Chief Dealer Offshore Markets and Funds Management in WATC's Financial Markets Team for six months. Carol has more than 20 years of experience in Financial Markets, working in both London and Perth.

Getting in Touch

If you would like more information about a specific article, product or service at WATC, please contact the relevant team member using the details below.

For information on any products or services, please contact:

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WESTERN AUSTRALIAN
TREASURY CORPORATION

Western Australian Treasury Corporation (WATC) is the State's central financial services provider, working with its public sector clients to achieve sound financial outcomes.

WATC's principal activities involve:

- funding and debt management
- asset and investment management
- financial advisory services
- financial risk management
- treasury management services and systems.

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