

TREASURY EXECUTIVE MINUTE

Minute No.

5 January 2011

Deputy Prime Minister and Treasurer

EFFECTS OF THE RECENT FLOODS ON THE MACROECONOMIC FORECASTS

Timing: At your convenience.

Recommendation/Issue:

- That you note this briefing.

Noted

Signature:/...../2011

KEY POINTS

- The recent flooding in Queensland is likely to have a substantial impact on the macroeconomic forecasts.
- With events still unfolding it is too early to put a precise figure on the impact. As a guide, however, it appears that the flooding will reduce real annual GDP growth in 2010-11 by between $\frac{1}{4}$ and $\frac{1}{2}$ of a percentage point.
- The effect on GDP growth is likely to be spread over the December and March quarters (with perhaps some small backcasting into the September quarter because of the way that rural production is estimated).
- The key areas of economic activity that are likely to be affected are:
 - coal production – lower by about \$1 billion to \$2 billion;
 - crop production, particularly horticultural, broadacre, sugar and cotton – lower by about \$1 billion;
 - retail trade, including related activity such as wholesale trade, transport and storage – lower by about \$1 billion to \$1½ billion
 - manufacturing – down by around \$400 million;
 - construction – lower by around \$200 million; and
 - tourism – down by about \$60 million.¹
- Rebuilding activity will add a little back to GDP growth in subsequent quarters.

¹ Tourism Queensland is expected to provide a substantially higher estimate, but its estimates include weaker demand in other areas, such as the Gold Coast and Brisbane, which are not directly affected by the floods.

- Nominal GDP growth is also expected to be lower, but the fall is likely to be partly moderated by higher coal and agricultural prices.
 - It is likely to take some time for changes in metallurgical coal prices (the most important affected price for GDP calculations) to emerge. These prices are set in confidential fixed price contracts – there is no spot market.
- Other things being equal, weaker nominal GDP growth for 2010-11 will flow through to slower growth in profits and wages and salaries (through temporarily weaker employment/hours growth); headline inflation is likely to be temporarily higher.
- Note that estimates of ‘damage/loss’ reported in the media often refer to changes in the *stock* of assets (houses, infrastructure and so on), rather than to changes in the *flow* of economic activity (GDP) which is the focus of the macroeconomic forecasts.
- Estimates of the effects of the flooding are likely to evolve as more information becomes available. The next National Accounts, which will record the impact in the December quarter, will be released on 2 March 2011.

[This content has been redacted under Section 22]

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