

**From:**

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**To:**

**Cc:** MEG DED ForecastingTeam

**Subject:** FW: BR11/003 - UNALLOCATED - Briefing request - Macquarie Bank lunch

**Attachment:**

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## **Attachment**

### **What is the outlook for the Australia economy?**

- Prospects for the Australian economy remain positive, with an underlying profile over the next year of solid growth, low unemployment, moderate inflation and a surge in business investment.
- In the 2010-11 MYEFO, real GDP was expected to grow strongly over the next two years, by 3¼ per cent in 2010-11 and 3¾ per cent in 2011-12. This implies that the economy will return to full capacity within the forecast period.

### **How will recent floods impact the outlook for economic activity?**

- The recent flooding in Queensland, Victoria and northern NSW is likely to have a substantial impact on the Australian economy, although it is too early to put a precise figure on the impact given that events are still unfolding.
  - There are currently a number of estimates in the public domain as to the effect of the recent floods on GDP growth. These estimates range from a detraction of 0.2 to one percentage point from GDP growth in 2010-11.
  - : The key areas of economic activity that are likely to be negatively affected are coal production, crop production (particularly horticultural, broadacre, sugar and cotton) and retail trade (including related activity such as wholesale trade, transport and storage).
  - : There has also been significant damage to the stock of assets, such as housing and infrastructure, which may take some time to rebuild.

### **How will the terms of trade boom affect business investment and exports?**

- The terms of trade are forecast to rise by 15½ per cent in 2010-11, underpinned by high prices for Australia's non-rural bulk commodity exports. However, the terms of trade are expected to fall by 4½ per cent in 2011-12 as more global commodity supply comes online.
- New business investment is expected to increase significantly over the forecast period, returning to around 40-year highs as a proportion of GDP. In the mining sector, rapid growth in profits is supporting strong capital expenditure intentions. More broadly, investment intentions have also improved as the outlook for the economy has strengthened.
  - With a large pipeline of investment, the main risks centre around capacity constraints and timing. Non-residential building investment is expected to remain subdued.
- Exports are forecast to grow by a solid 7 per cent in 2010-11 and by 5 per cent in 2011-12, reflecting a strong outlook for both rural and non-rural commodity exports. For non-rural commodity exports, strong growth is being driven by expanding mining production and port capacity in response to strong demand from Asia and high international prices.

### **What impact is fiscal stimulus having on the economy?**

- Fiscal and monetary stimulus helped support the economy through 2009 and is now being withdrawn as private activity builds momentum.
  - The withdrawal of fiscal stimulus (which affects not only public final demand, but also household consumption and business investment) is expected to detract around 1 percentage point from GDP growth in 2010-11 and  $\frac{1}{2}$  of a percentage point from GDP growth in 2011-12.
- Public final demand is forecast to grow  $1\frac{1}{2}$  per cent in 2010-11, before falling by a  $\frac{1}{4}$  of a percentage point in 2011-12 as fiscal stimulus continues to be withdrawn.

#### **What is the outlook for the labour market?**

- The Australian labour market has been remarkably resilient in the face of the global downturn and is now staging a solid recovery.
  - Australia's unemployment rate, at just 5.0 per cent, is lower than any of the major advanced economies.
- The unemployment rate is expected to continue to fall, reaching  $4\frac{3}{4}$  per cent by the end of 2010-11 and  $4\frac{1}{2}$  per cent by the end of 2011-12.
- Employment is expected to grow by  $2\frac{1}{2}$  per cent through the year to the June quarter 2011 and 2 per cent through the year to the June quarter 2012, consistent with the strong outlook for activity.

#### **What is the outlook for inflation?**

- Inflation is also expected to rise over the forecast horizon, reflecting the strength in domestic demand, a buoyant labour market and anticipated increases in administered prices. Underlying and headline measures of inflation are expected to be  $2\frac{3}{4}$  per cent through the year to the June quarter 2011 and 3 per cent through the year to the June quarter 2012.