2 Economic performance and outlook

Features

- Growth in Queensland gross state product (GSP) is expected to strengthen to 2¾% in 2017-18, largely reflecting a rebound in business investment and a recovery in coal exports following the impacts of Severe Tropical Cyclone (STC) Debbie in 2016-17.
- Economic growth is forecast to strengthen further to 3% in 2018-19. In 2019-20, while domestic activity should strengthen and support stronger jobs growth, it will also boost imports. Combined with a moderation in export growth, this will constrain the trade sector's contribution to growth and result in GSP growth easing to 2¾%. From 2020-21, GSP is expected to grow 2¾% per annum, consistent with the State's longer run potential.
- Stronger global economic conditions have boosted industrial production across Queensland's major trading partners, lifting demand for and prices of several of the State's key commodity exports. A rebound in coal exports following STC Debbie and the final year of the LNG ramp-up have also supported growth in overseas exports in 2017-18.
- Growth in household consumption has remained subdued in 2017-18, despite a strong pick up in full-time jobs. Growth is then expected to gradually strengthen over the forecast period. Meanwhile, dwelling investment is on track for a 'soft landing', with a slight decline in activity in 2017-18 and 2018-19 before returning to modest growth in 2019-20.
- Business investment has rebounded strongly in 2017-18, to be a key driver of economic growth. The recovery was initially driven by spending on machinery and equipment, but has since become broader-based, with improved business conditions and ongoing growth in tourism and education exports supporting a recovery in non-dwelling construction.
- However, largely reflecting the strong ramp up in business investment, overseas import growth is expected to be considerably higher than the growth in overseas exports, resulting in the trade sector detracting from overall growth in 2017-18.
- From 2018-19 onwards, growth in commodity exports is expected to be modest, while prices, particularly for coal, are expected to decline from current elevated levels. However, with imports expected to ease in 2018-19 following the surge in 2017-18, the trade sector should contribute to growth in 2018-19.
- Employment growth has been stronger than expected in 2017-18, driven largely by health, construction, transport and education. While growth has eased in early 2018, the strong gains in late 2017 mean growth over the year to June quarter 2018 is estimated to be 2¾%. Partially reflecting a lower level of activity in dwelling construction, employment is expected to grow at more sustainable rates of 1½% and 1¾% over the next two years.
- The entry of jobseekers encouraged by greater opportunities has seen the participation rate rise sharply and the unemployment rate stabilise in the short-term, with the unemployment rate forecast to remain at 6¼% in June quarter 2018 and 2019. However, stronger domestic activity is expected to see the rate fall to 6% by June quarter 2020.

2.1 International conditions

Global conditions improved significantly in 2017 and, on balance, the economic prospects of Queensland’s major trading partners are positive over the forecast period. However, while the recent stronger growth is likely to extend into 2018, the pace of growth is expected to moderate in later years.

In addition to monetary policy settings by major central banks remaining accommodative, stronger global trade drove a rebound in industrial production in almost all of Queensland’s major trading partners in 2017. This in turn has led to a strong recovery in mineral and energy prices.

However, the current outlook suggests that coal, iron ore and oil prices will decline to more sustainable levels in the coming year, in line with an anticipated slowing in global industrial production growth following its rebound in 2017.

Meanwhile, a widening interest rate differential between the US and Australia saw the A$ fall back towards the lower end of the 75-80USc range by mid-May 2018. A sustained lower exchange rate will support the incomes and international competitiveness of Queensland exporters. However, higher US interest rates could see funds flow more towards the US and other overseas capital markets.

Growth in the **United States**, supported by expansionary monetary and fiscal policy, has seen the US labour market at or near full employment and inflation close to the Federal Reserve’s (the Fed) target. While the Fed has continued to reverse some monetary stimulus, the recent fiscal stimulus provided by tax cuts and spending legislation is likely to support growth in the short-term. However, the tight labour market may increase inflationary pressure and cause the Fed to raise interest rates further and faster than anticipated, while any future balance sheet repair required due to the impact on US government debt may offset some of the short-term stimulus.

China’s economy has maintained growth close to 7% in the past three years. The country’s brisk pace of economic and social development has coincided with an ageing population, widening income inequality, high corporate debts and rising pollution. China’s economic growth is expected to ease in the near-term, with trade tensions with the US providing a risk to the outlook.

Japan’s economy has been expanding moderately in recent years, with the country’s exports increasing on the back of stronger global economic growth. Japan’s monetary policy is likely to remain accommodative for some time and, along with spending related to the 2020 Tokyo Olympics, Japan’s economy is likely to grow moderately in the near-term.

Industrial production growth in **Korea** moderated in 2017, partly due to the appreciation of the Korean Won against the Japanese Yen over the course of 2017. Overall economic growth in Korea is expected to moderate slightly in 2018 and 2019.

India’s economy has seen a rebound in growth, as investment and consumption continue to drive the cyclical recovery. The Reserve Bank of India expects India’s economy to grow by 7.4% in 2018-19, which would likely see India as the world’s fastest growing major economy.

2.2 National conditions

The national economy continues to transition towards broad-based growth. Australian Treasury forecasts GDP growth to strengthen to 2¾% in 2017-18 and to 3% in both 2018-19 and 2019-20.

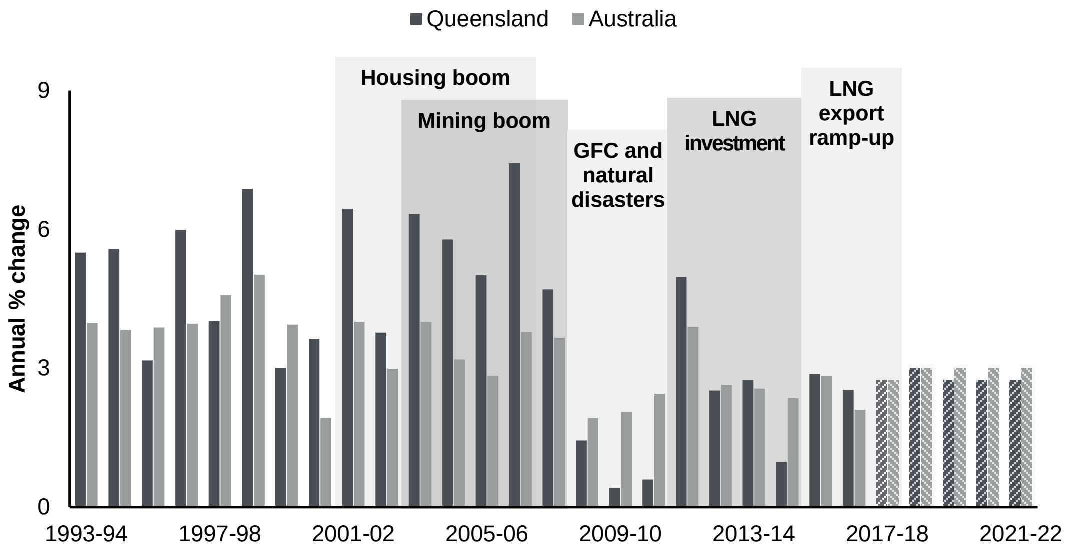
A pick-up in household consumption is supported by strengthening wage growth and solid employment outcomes, while dwelling investment is expected to remain elevated by historical standards. Australian Treasury expects business investment to return to growth in 2017-18, driven by a lift in non-mining business investment and a diminishing drag from mining investment.

Goods exports nationally continue to be supported by the expansion of mining capacity, primarily in Western Australia (iron ore and LNG) and the Northern Territory (LNG), while services exports are benefiting from opportunities in the Asian region. Australian Treasury expects employment growth to moderate from current rates and the unemployment rate to ease gradually.

2.3 Queensland conditions and outlook

Growth in the Queensland economy is expected to strengthen to 2¾% in 2017-18, reflecting further improvement in domestic demand (as business spending has rebounded) and a recovery in coal exports following STC Debbie. Economic growth is forecast to accelerate further to 3% in 2018-19, with household consumption gaining momentum and a contribution to growth from the trade sector as imports ease (Chart 2.1).

Chart 2.1 Economic growth[1], Queensland and Australia



Note:

1. CVM, 2015-16 reference year, 2017-18 onwards are forecasts/projections.

Sources: ABS 5206.0, Australian Government Budget 2018-19 and Queensland Treasury.

Domestic activity is forecast to strengthen in 2019-20, supporting stronger jobs growth, but also boosting imports. When combined with a forecast moderation in exports growth, as some key commodities approach production capacity, this is expected to constrain the trade sector's contribution to growth in 2019-20 and result in overall growth easing to 2¾% in the year. From 2020-21, Queensland GSP is expected to grow by 2¾% per annum, consistent with the State's longer-run potential (Table 2.1).

Table 2.1 Queensland economic forecasts/projections[1]

	Actual	Est. Act.	Forecasts		Projections	
	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
Gross state product[2]	**2.5**	**2¾**	**3**	**2¾**	**2¾**	**2¾**
Nominal gross state product	9.3	5½	4	3¾	4½	4¾
Employment[3]	1.8	2¾	1½	1¾	1¾	2
Unemployment rate[4]	6.2	6¼	6¼	6	6	5¾
Inflation[5]	1.7	1¾	2	2½	2½	2½
Wage Price Index[5]	1.9	2¼	2½	3	3	3
Population[5]	1.5	1¾	1¾	1¾	1¾	1¾

Notes:

1. Unless otherwise stated, all figures are annual percentage change.
2. Chain volume measure (CVM), 2015-16 reference year.
3. Through-the-year growth rate to the June quarter (seasonally adjusted).
4. Seasonally adjusted rate for the June quarter.
5. Annual percentage change, year-average.

Sources: ABS 3101.0, 6202.0, 6345.0, 6401.0 and Queensland Treasury.

Household consumption

Constrained by moderate growth in household incomes, Queensland household consumption grew by 2.4% in 2016-17. While a marked improvement in labour market conditions in 2017-18 has aided a pick-up in overall compensation of employees, wage pressures in the economy remain low and households continue to be cautious about spending.

Further, with the State's household savings rate in 2016-17 at its lowest since 2003-04, any growth in income will likely be utilised to pay off household debt, rather than translate into increased consumption in the short-term.

With the terms of trade expected to moderate and jobs growth forecast to soften following the exceptionally strong gains in 2017-18, household consumption growth is again forecast to be subdued in 2018-19. Additionally, the slowing in apartment construction is expected to both constrain spending on household goods and furnishings and reduce consumption due to falls in associated construction employment. In later years, consumption growth is forecast to pick up gradually, but remain below the average growth rates recorded prior to the GFC.

Dwelling investment

After several years of sustained growth, Queensland's dwelling investment cycle peaked in 2016-17. Driven by a decline in the construction of attached dwellings (units, apartments, etc.), dwelling investment is forecast to contract in 2017-18 and 2018-19, as the large amount of new apartment supply is absorbed into the market. However, the decline across these years is expected to be moderate relative to previous cycles. Modest growth is expected to return from 2019-20 onwards, as the decline in attached dwelling construction slows and is offset by the construction of new houses and ongoing growth in alterations and additions.

Business investment

Following the LNG construction boom, Queensland business investment fell rapidly in 2014-15 and 2015-16 before stabilising in 2016-17, driven by a return to growth in machinery and equipment investment. Business investment is expected to rebound strongly in 2017-18, driven by growth across all components.

Growth in engineering construction is expected to be supported by investment in renewable energy projects, including wind and solar farms, in 2017-18 and 2018-19. However, with few major resources projects currently committed or under construction, growth in heavy industry investment will likely be subdued in the medium-term.

Non-residential building construction work has risen, strengthened by accommodation and educational facilities amid increased education enrolments and tourism activity. This trend is likely to continue. Elevated vacancy rates mean new investment in office space is likely to be subdued.

Machinery and equipment expenditure has risen solidly, buoyed by increased company profits, low lending rates to businesses and the lower A$ benefiting exporters. Recent strength in employment growth and elevated capacity utilisation rates suggest this component should continue to grow in 2018-19. Overall, business investment is forecast to pick up steadily over the forecast period, consistent with a steady acceleration in non-dwelling construction growth.

Public final demand

Public final demand is forecast to continue to grow strongly. A range of large expenditure programs (such as the National Disability Insurance Scheme) and infrastructure projects, including the Queensland Government's $11.6 billion capital works program in 2018-19, will underpin this growth.

Overseas exports and imports

A rebound in coal exports following STC Debbie and the final year of the LNG production ramp-up have supported growth in overseas exports in 2017-18. However, the unexpected strong growth in overseas imports will result in net exports detracting from overall growth in 2017-18. In 2018-19, net exports are expected to contribute modestly to growth, but an increase in imports to support domestic growth in 2019-20 will constrain the overseas trade sector's contribution to growth in that year.

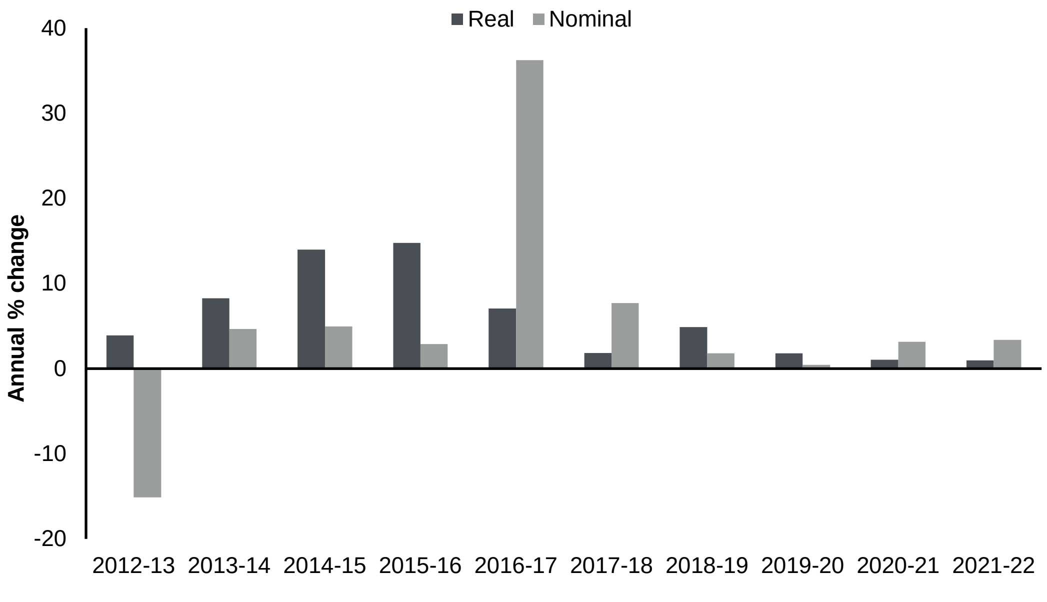
Coal export volumes have rebounded in 2017-18, following the loss of 11 million tonnes in April and May 2017 due to STC Debbie. However, this recovery has been tempered somewhat by the impacts of Tropical Cyclone Iris in early April 2018 and maintenance across port and rail infrastructure. Looking ahead, while coal exports volumes are forecast to continue to grow strongly in 2018-19, partly due to a resumption of full operation at the Dalrymple Bay Coal Terminal, the rate of growth will most likely be moderate in later years. Increased industrial production in Asia, particularly Japan and Korea, is expected to underpin demand for hard-coking coal, while new coal fired power stations in Japan will support demand for thermal coal.

Following several price spikes throughout 2016-17 and 2017-18 (due to regulatory supply restrictions in China, STC Debbie and increased demand in China), hard-coking prices are forecast to decline throughout 2018-19, but remain higher than 2015-16 levels. Similarly, thermal coal prices, which have been elevated throughout 2016-17 and 2017-18, are expected to decline in 2018-19, but remain above 2015-16 prices.

LNG export volumes have grown significantly in recent years, as all six LNG production trains on Curtis Island were completed and began exporting. However, reflecting strong domestic demand for gas, LNG exports have plateaued slightly below nameplate capacity and growth is expected to moderate in the coming years. With 2017-18 being the first full year in which all six LNG trains are in production, any further growth in LNG exports will be driven by new gas developments which will also provide additional supply into the eastern domestic gas market.

Metals export volumes are expected to return to growth in 2018, after closures of depleted mines and production cuts. With several new projects and increased production encouraged by a sustained rally in prices, metals exports are forecast to grow solidly in 2018-19 and 2019-20.

Chart 2.2 Overseas goods exports, Queensland



Source: Queensland Treasury.

Beef export volumes are expected to return to growth from 2017-18 onwards. With seasonal conditions expected to return to normal, restocking activity is forecast to gradually wane.

Sugar exports are expected to decline in 2017-18 following STC Debbie. Some recovery is expected in the near-term with only modest growth in the medium-term. **Cotton exports** are forecast to grow further in 2017-18, following a large increase in 2016-17. **Other crop exports** are forecast to decline substantially in 2017-18, due to large falls in wheat and chickpeas.

With the A$ remaining at a more competitive level for an extended period**, tourism exports** are expected to grow solidly over the forecast period. However, with national tourism growth being underpinned largely by growth from Chinese and Indian tourists visiting friends and relatives, Queensland tourism is expected to continue to grow more moderately than the southern states.

Queensland's international **education exports** have grown strongly in recent years. A competitive A$, rising demand for education from Asia and increasing popularity amongst South American students are all expected to support continued strong growth.

Imports have picked up strongly in the first half of 2017-18 as business investment growth increased the demand for imported capital goods. However, the significant growth in imports has been stronger than the growth in machinery and equipment investment, possibly reflecting pent-up demand as business confidence continues to recover following the GFC.

Following the strong rebound in 2017-18, business investment is forecast to return to more moderate growth from 2018-19, while household consumption is expected to remain subdued over the forecast period. Reflecting these trends, imports are forecast to fall from elevated levels in 2018-19, before returning to modest growth in 2019-20.

Labour market

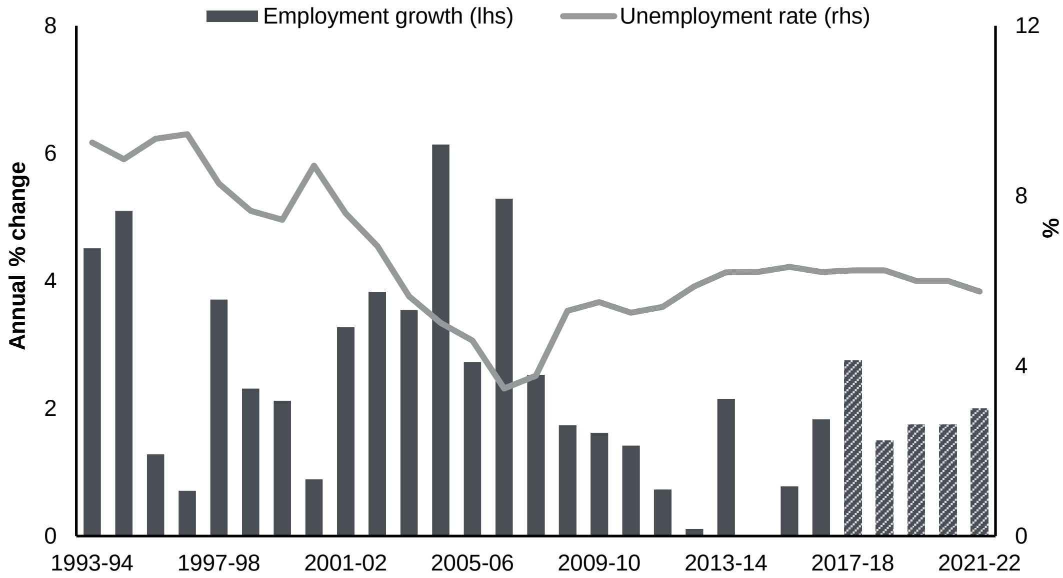
Employment growth has been stronger than expected in 2017-18. While employment growth has moderated in early 2018, the exceptional gains in late 2017 mean growth over the year to June quarter 2018 is estimated to be 2¾%. Employment growth is expected to return to more sustainable rates of 1½% and 1¾% respectively over the next two years (Chart 2.3).

The ongoing downturn in labour-intensive residential construction over 2018 and 2019 will be a key factor in the moderation of employment growth from its current high rate, with dwelling investment having considerable flow on effects to household consumption.

Rather than generating a similar reduction in the State's unemployment rate, much of the recent strength in Queensland employment has been absorbed by increased labour force participation. The strong jobs growth has encouraged jobseekers to re-enter the labour force, seeing the participation rate climbing to its highest rate in three years. As a result, the unemployment rate is forecast to remain at 6¼% in the near term (June quarter 2018 and 2019).

With improved business investment, ongoing public spending programs and a slowly strengthening household sector, employment growth is forecast to improve in 2019-20 to be at or slightly above growth in the working age population. As the dwelling investment cycle matures and domestic economic activity strengthens, employment growth is expected to strengthen and the unemployment rate is forecast to move slightly lower later in the forecast period, improving to 6% in June quarter 2020 as spare capacity in the labour market is absorbed.

Chart 2.3 Employment growth[1] and unemployment rate[2], Queensland[3]



Notes:

1. Through-the-year growth rate to the June quarter (seasonally adjusted).
2. Seasonally adjusted rate for the June quarter.
3. 2017-18 onwards are forecasts/projections.

Sources: ABS 6202.0 and Queensland Treasury.

Regional labour markets

With agriculture, mining and construction accounting for a significant portion of economic activity in regional Queensland, the operating environment of these few industries are crucial to the conditions and outlook for labour market outcomes in regional Queensland.

While farmers continue to face challenging conditions due to widespread drought, those regions exposed to the resources sector have improved. Meanwhile, continued growth in tourism activity has also supported a return to solid employment growth in regional Queensland (Chart 2.4).

As a result, the unemployment rate across many regional centres has declined and the overall gap between regional and South East Queensland has narrowed substantially in 2017-18. After stabilising between 2015 and early 2017, the aggregate unemployment rate in regional Queensland fell 0.6 percentage point (to 7.2%) over the year to April 2018, compared with a 0.1 percentage point increase in the South East (to 5.7%).

Areas such as Mackay and Cairns have shown considerable improvement. Over the year to April 2018, employment has risen in Townsville (up 10,300 persons), Mackay (up 6,900 persons) and Cairns (up 4,900 persons). Meanwhile, these regions' unemployment rates have fallen by 2.3 percentage points (to 8.5%), 2.0 percentage points (to 3.8%) and 0.8 percentage point (to 6.3%), respectively.

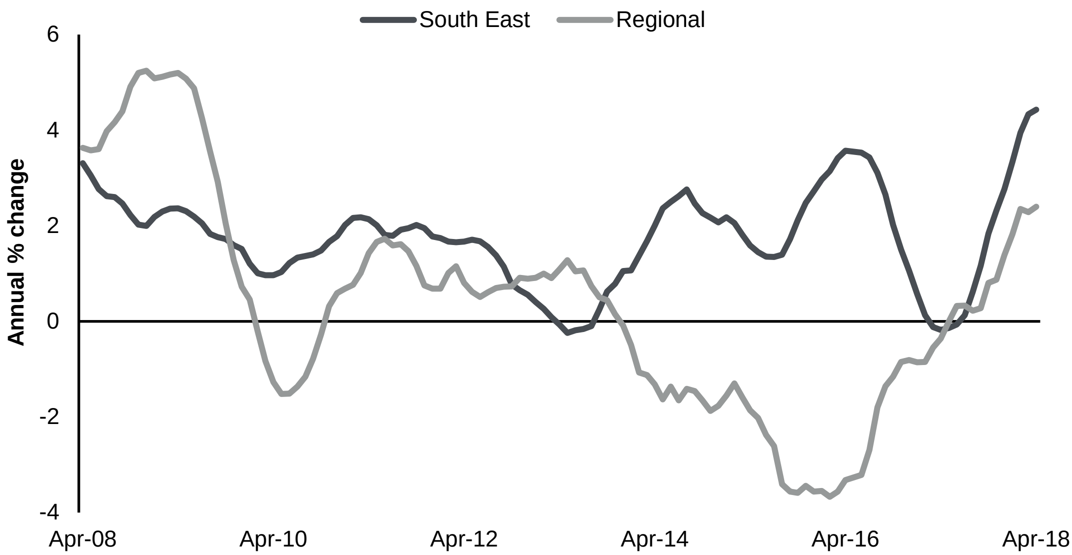
The improvement in Cairns is consistent with stronger tourism activity in recent years which has encouraged new investment projects and additional direct flights from China and Japan. Labour market conditions for younger workers in Cairns, closely linked to conditions in the region's tourism industry and opportunities for lower-skilled workers, have also improved.

Meanwhile, Fitzroy appears to be adjusting following the wind-down in LNG construction investment and lingering impacts of the drought on beef production. Similar to Mackay, coal operations in the Fitzroy region have benefited from higher coal prices.

Labour market outcomes in Townsville have improved over the past year. However, while Townsville is a reasonably diversified economy, it continues to be influenced by prospects in the resources sector, directly through fly-in fly-out workers and indirectly via its processing infrastructure.

Conditions in the diverse Queensland-Outback region also remain challenging. The Outback faces ongoing drought conditions in the south and central west, and elevated levels of unemployment across some Indigenous communities.

Chart 2.4 Employment growth[1] by region, Queensland



Note:

1. Year-average. South East Queensland is defined as Greater Brisbane, Gold Coast, Sunshine Coast and Toowoomba.

Source: ABS 6291.0.55.003

Prices and wages

Brisbane consumer price growth is expected to remain subdued in 2017-18, with inflation largely due to the scheduled 12.5% annual increase in the Australian Government’s tobacco excise, higher purchasing costs for new dwellings and higher automotive fuel prices. A modest acceleration in inflation is forecast for 2018-19, with a further increase in the tobacco excise and increased new dwelling purchase prices again contributing strongly to increases in the CPI.

Despite nominal wage growth remaining low by historical standards, real wages have continued to rise. As conditions in the domestic economy and spare capacity in the labour market declines, wage growth is expected to improve over the medium-term.

Population

Queensland’s population growth is forecast to average around 1¾% in 2017-18 and over the remainder of the forecast period.

Housing affordability has seen a strengthening in net interstate migration from New South Wales, while the end of the Western Australian resources investment boom has seen an increase in net inflows over recent years, after a period of outflows to that state between 2008 and 2015.

Net overseas migration in Queensland has grown strongly but is expected to moderate in 2018, consistent with national policies. However, rising incomes in Asia and the competitive A$ will continue to help drive growth in net overseas migration over the medium-term.

Over the longer term, Queensland Treasury projections show that Queensland’s population, which is estimated to have recently topped 5 million, will reach 6 million by 2029 and 7 million by 2038, with much of this growth anticipated to occur in the south east of the State.

Substantial investment in transport, health and education infrastructure, from both the public and private sectors, will be required to support the productive capacity of this increased population base. The Palaszczuk Government’s $45.8 billion capital works program is designed to help meet the demands of the State’s growing population.

2.4 Risks and opportunities

Key risks to the international outlook include the timing of monetary policy normalisation in major economies, particularly the US. Further interest rate differentials between the US and Australia may have an adverse flow-on effect to the Australian economy in general, particularly on borrowing costs.

Further, there are still uncertainties surrounding global trade conflicts which may impair demand for key industrial commodities.

Domestically, uncertainty remains around the extent of oversupply in the apartment market, and any concurrent downturn in major southern capitals could exacerbate the downturn in Queensland.

There are ongoing uncertainties surrounding changes to coal transport scheduling and any potential response by coal miners, other above-rail providers and ports. The current assessment is that the impact may not be significant, and that the issue is expected to be resolved this year. Overall, coal exports are expected to be higher in 2018-19 compared to last year. Notwithstanding this, the uncertainty provides a risk to the outlook.

More than 50% of the State remains drought declared. While a return to normal seasonal conditions is assumed, if current drought conditions continue, it could negatively impact on agricultural investment, production and exports.

Upside risks include the possibility that business investment may be stronger than currently predicted if company profits continue to remain at high levels or more large scale renewable energy projects are committed. Further, if commodity prices remain relatively high for longer than anticipated, it may rekindle some additional interest in other mining-related investment.

Table 2.2 Queensland economic forecasts[1], by component

	Actual	Est. Act.	Forecasts	
	2016-17	2017-18	2018-19	2019-20
Economic output[2]				
Household consumption	2.4	2	2¼	2½
Private investment	1.3	4½	1¼	2½
Dwelling investment	3.2	-4¼	-1½	1
New and used	4.2	-7¼	-3¾	-½
Alterations and additions	1.1	3	3	4
Business investment	-1.9	10¾	3¼	3¾
Non-dwelling construction	-6.8	10	1½	3½
Machinery and equipment	5.3	11½	5¾	4
Private final demand	2.1	2¾	2	2½
Public final demand	5.2	4	3¾	3
Gross state expenditure	3.0	3	2¼	2¾
Net overseas exports[3]	0.4	-1¾	1¼	0
Overseas exports	6.8	2½	4¾	2¼
less Overseas imports	5.8	12	-1	2¾
Gross state product	**2.5**	**2¾**	**3**	**2¾**
Nominal gross state product	9.3	5½	4	3¾
Other economic measures				
Employment[4]	1.8	2¾	1½	1¾
Unemployment rate[5]	6.2	6¼	6¼	6
Inflation[6]	1.7	1¾	2	2½
Wage Price Index[6]	1.9	2¼	2½	3
Population[6]	1.5	1¾	1¾	1¾

Notes:

1. Unless otherwise stated, all figures are annual percentage changes.
2. CVM, 2015-16 reference year, except nominal GSP. Components not separately reported are other investment (cultivated biological resources, intellectual property products and ownership transfer costs), the balancing item (including interstate trade and inventories) and the statistical discrepancy.
3. Goods and services, percentage point contribution to growth in gross state product.
4. Through-the-year growth rate to the June quarter (seasonally adjusted). The comparable growth rates in year average terms are 0.0%, 4%, 1½% and 1¾% from 2016-17 through to 2019-20.
5. Seasonally adjusted rate for the June quarter.
6. Annual percentage change, year-average.

Forecast assumptions include: a gradual rise in the RBA cash rate from 2019; a broadly stable A$; oil prices to fall in the near term and then be relatively stable; and a neutral outlook for weather conditions.

Sources: ABS 3101.0, 6202.0, 6345.0, 6401.0 and Queensland Treasury.