

ECONOMIC OUTLOOK FOR 2011-12, 2012-13 AND 2013-14

DECEMBER 2011

(THIS REPORT INCORPORATES DOMESTIC AND INTERNATIONAL DATA RELEASED UP TO
14 DECEMBER 2011)

Overview.....3
MYEFO Forecast Update4
International Economic Outlook.....4
Domestic Economic Outlook5

OVERVIEW

The economic outlook is broadly unchanged from the September JIEFG and Mid-Year Economic and Fiscal Outlook (MYEFO) updates.

International growth prospects remain highly uncertain. The European sovereign debt crisis continues to pose considerable risks to financial stability and is undermining global confidence. Economic indicators have improved recently in the US, although the prospect of substantial near-term fiscal tightening remains a threat to the strength of the US recovery. Growth in emerging Asia remains robust, although weak external demand and deleveraging by European financial institutions are starting to weigh on industrial activity and affect the availability of trade finance, contributing to weakness in global commodities markets.

These developments are being transmitted to the Australian economy through a number of channels, including considerable volatility of the exchange rate, reductions in equity prices, lower prices of some of Australia's key export commodities – particularly iron ore and coal – and weaker consumer and business confidence. This has contributed to a reduction in momentum in some parts of the Australian economy and a slowdown in employment growth.

Still, the Australian economy is expected to grow at around its trend rate over the next three years. Growth is expected to be driven by mining-related activity, with no evidence as yet that the deterioration in international conditions has dented the record pipeline of resources investment. Conditions are, however, expected to remain uneven across the economy, with global weakness and the high Australian dollar continuing to weigh heavily on some sectors.

Consistent with the MYEFO, the Australian economy is forecast to grow 3¼ per cent in 2011-12 and 2012-13 (Table 1). Employment is forecast to grow 1 per cent through the year to the June quarter of 2012 and 1½ per cent through the year to the June quarter of 2013. The unemployment rate is forecast increase to 5½ per cent by the June quarter of 2012, before remaining broadly unchanged through to the June quarter of 2013.

Table 1: Key Domestic Forecasts

	2010-11	2011-12		2012-13		2013-14
	Outcome (a)	Sept JIEFG	Dec JIEFG	Sept JIEFG	Dec JIEFG	Dec JIEFG
Real GDP (b)	1.9	3 1/4	3 1/4	3	3 1/4	3
Nominal GDP (b)	8.3	6 1/2	6	4 1/2	5 1/4	5 1/4
Unemployment rate (c)	4.9	5 1/2	5 1/2	5 3/4	5 1/2	5 1/2
Employment (d)	2.2	1	1	1 1/4	1 1/2	1 1/2
CPI (d)	3.6	2 1/2	2 1/4	3 1/4	3 1/4	2 1/2
Underlying inflation (d)	2.8	2 1/2	2 1/4	2 3/4	2 3/4	2 1/2
WPI (d)	3.8	3 3/4	3 3/4	3 3/4	3 3/4	3 3/4
Terms of trade (b)	20.6	3	1 3/4	-6 3/4	-5 1/4	-2 3/4

(a) Calculated using original data except for employment, the unemployment rate and WPI.

(b) Year average.

(c) June quarter.

(d) Through-the-year growth rate to the June quarter.

Source: ABS cat. No. 5206.0, 5302.0, 6202.0, 6345.0, 6401.0 and Treasury.

The December JIEFG report includes 2013-14 as a forecast year for the first time, with real GDP growth expected to moderate slightly to 3 per cent, or around trend. Following exceptional growth in resources investment and non-rural commodities exports in 2011-12 and 2012-13, the mining sector is also expected to make a substantial contribution to growth in 2013-14, but less than in the previous two years. Trend economic growth would be consistent with a steady unemployment rate and inflation of around 2½ per cent.

The world economy is expected to grow at an around-trend 4¼ per cent in 2014, supported by a continued moderate recovery in the US, robust growth in emerging Asia and an assumption that there will be a return to weak, but positive, growth in Europe.

The possibility of a major financial collapse in Europe represents a significant downside risk to the forecasts. While Australia's trade is primarily with Asia and direct exposures to European financial institutions are low, the past few months have again highlighted the importance of financial market and confidence channels. It is also likely that growth in the Asian region, and therefore our trade with emerging Asia, would be affected by a sharp deterioration in Europe. Events in Europe are evolving rapidly, posing a risk that the economic outlook could deteriorate quickly.

MYEFO FORECAST UPDATE

Subsequent to the September JIEFG, Treasury's economic forecasts were updated in November for the Mid-Year Economic and Fiscal Outlook (MYEFO). Treasury's forecasts for euro area growth were downgraded at that time, with the prospect of a recession in 2012 elevated from a risk at September JIEFG to the central forecast at MYEFO. This was partly offset by a minor upgrade to forecast growth in the US, leaving world GDP growth ¼ of a percentage point weaker in 2012 than forecast at September JIEFG. The MYEFO also captured the significant decline in iron ore prices between September and November, leading to a reprofiling of Treasury's terms of trade forecasts. In response to unfolding events, the Reserve Bank of Australia reduced the official cash rate by 25 basis points in November and market economists adjusted their interest rate expectations, factoring in a further 25 basis point reduction in the official cash rate by the first quarter of 2012 (realised in December).

Notwithstanding the deterioration in international conditions, a lower interest rate profile, further growth in the resources investment pipeline (including the final investment decision on the \$29 billion Wheatstone LNG project), and survey data pointing to a stabilisation of business conditions and consumer sentiment, underpinned a minor upgrade to Treasury's economic forecasts in 2012-13. Treasury's real GDP and employment growth forecasts were increased at MYEFO by ¼ of a percentage point in 2012-13, reducing the forecast unemployment rate to 5½ per cent in the June quarter 2013. There have been no material changes to the economic forecasts since that time.

INTERNATIONAL ECONOMIC OUTLOOK

The international growth outlook is largely unchanged from MYEFO. World GDP growth forecasts have been downgraded by ¼ of a percentage point in 2011 since MYEFO to 3¾ per cent, reflecting additional weakness in Japan, but are unchanged at 3½ per cent in 2012 and 4 per cent in 2013. World GDP growth is forecast to strengthen slightly to 4¼ per cent in 2014, underpinned by continued robust growth in the emerging market economies and a slight pickup in growth in the US and Europe. While the forecasts are for growth in the major advanced economies to strengthen somewhat, the forecast growth rates would not be sufficient to make substantial inroads into high unemployment.

Table 2: International GDP growth forecasts^(a)

	2010	2011		2012		2013		2014	
	Actual	Sep JIEFG	Dec JIEFG						
United States	3.0	1 1/2	1 3/4	1 3/4	2	2 1/4	2 1/4	n.a.	2 1/2
Euro area	1.9	1 1/4	1 1/2	3/4	- 1/4	1 1/4	1	n.a.	1 1/4
Japan	4.4	-1	- 3/4	2 1/4	2 1/4	1 1/4	1 1/4	n.a.	1
China ^(b)	10.4	9	9 1/4	8 3/4	8 1/4	8 1/2	8 1/2	n.a.	8 1/4
India ^(b)	9.9	7 1/2	7 1/4	6 1/2	6 1/2	8	8	n.a.	7 1/2
Other East Asia ^(c)	7.7	4 1/2	4 1/2	4	3 3/4	4 3/4	4 3/4	n.a.	5
Major Trading Partners	6.7	3 3/4	4	4 1/4	4 1/4	4 1/2	4 1/2	n.a.	4 1/4
World	5.2	3 3/4	3 3/4	3 3/4	3 1/2	4 1/4	4	n.a.	4 1/4

(a) Calculations for World, euro area and other East Asia growth rates use GDP weights based on purchasing power parity (PPP). Calculations for Major Trading Partners use export trade weights.

(b) Production-based measure of GDP.

(c) Other East Asia comprises the newly industrialised economies (NIEs) of Hong Kong, South Korea, Singapore and Taiwan and the Association of Southeast Asian Nations group of five (ASEAN-5), which comprises Indonesia, Malaysia, the Philippines, Thailand and Vietnam.

n.a. - Not available.

Source: National statistical publications, IMF *World Economic Outlook* September 2011, Thomson Reuters and Treasury.

Notwithstanding two major summits in October and December, the threat of financial contagion from the euro area sovereign debt crisis has continued to rise. Market concerns remain focused on Italy, with its high debt levels, weak growth prospects, and its poor economic reform record. The shape of further financial assistance to Greece, and the degree of sovereign debt write-down required, both remain unresolved, leaving open the possibility of a disorderly Greek default. Fiscal austerity implemented in response to the crisis will drag on euro area growth in 2012, and will be exacerbated if increased bank capital requirements are met by deleveraging. With the ongoing inability of European policymakers to adequately address the crisis and restore market confidence, the euro area is expected to return to recession in 2012.

Growth in the US has picked up as the temporary factors impeding activity in the first half of the year abated. While the US GDP growth forecasts for 2011 and 2012 were revised up by $\frac{1}{4}$ of a percentage point between September JIEFG and MYEFO, the US recovery remains sluggish and vulnerable to further shocks. The failure of the 'Super Committee' to agree to a medium-term deficit reduction plan means the fiscal support measures passed in December 2010 may not be extended into 2012. Accordingly, there is a risk of a substantial near-term fiscal tightening, undermining the still fragile recovery.

Japan's growth forecast for 2011 has been revised down from a $\frac{1}{4}$ of a percentage point contraction at MYEFO to a $\frac{3}{4}$ of a percentage point contraction at December JIEFG, reflecting downward revisions to real GDP in the first half of 2011. Earthquake reconstruction will boost growth in 2012, but once this has flowed through, growth is expected to return to the weak growth rates experienced since the early 1990s.

While emerging economies are expected to continue growing at solid rates, growth is still likely to be affected by the weaker outlook for Europe. Partly reflecting this, China's growth forecast for 2012 was revised down to $8\frac{1}{4}$ per cent at MYEFO. Similarly, the expected impacts on export-dependent Asian economies in the ASEAN-5 and the NIEs resulted in the forecast for other East Asia's growth for 2012 being revised down to $3\frac{3}{4}$ per cent.

While the central forecasts continue to assume that the European sovereign debt crisis will not precipitate a major destabilising event, the risk of such an event occurring remains significant and the potential damage to the global economy would be severe.

DOMESTIC ECONOMIC OUTLOOK

Australia's economic outlook is also largely unchanged since MYEFO. Growth over the forecast horizon is expected to be driven by mining-related activity, underpinned by a record pipeline of resources investment and strong growth in commodity exports. While global prices for Australia's key non-rural commodity exports are down between 10 and 30 per cent from their peaks in early-September, coal and iron ore prices are still at historically high levels, underpinning high levels of profitability in the resources sector. However, the weak international environment is expected to continue to weigh on Australia's economic outlook and exacerbate existing pressures on some sectors. The Australian dollar remains elevated, some businesses continue to have difficulty accessing credit and ongoing consumer caution is expected to see the household saving ratio remain elevated in the face of global instability, declines in household wealth and a slowing domestic labour market.

September quarter real GDP growth was broadly in line with the MYEFO forecasts, notwithstanding differences in some of the components. The Australian economy grew 1.0 per cent in the September quarter and 2.5 per cent through the year. Growth was driven by an unanticipated surge in resources investment and stronger-than-expected growth in household consumption, although the implications for aggregate real GDP growth were offset by related strength in imports. Changes in inventories and public final demand also detracted from growth in the September quarter, with the reduction in public final demand reflecting lower consumption and investment across all levels of government.

Recent survey data suggest that business conditions and consumer sentiment stabilised in the December quarter, but remain below their long-run averages. Commodity markets have been less volatile in recent weeks, with iron ore and coal prices currently trading within a relatively narrow band. Likewise, the

Australian dollar has remained within 2-3 per cent of parity with the US dollar since the MYEFO. Recent labour market outcomes and forward-looking labour demand indicators are also consistent with the MYEFO forecasts for a slight increase in the unemployment rate in the near term.

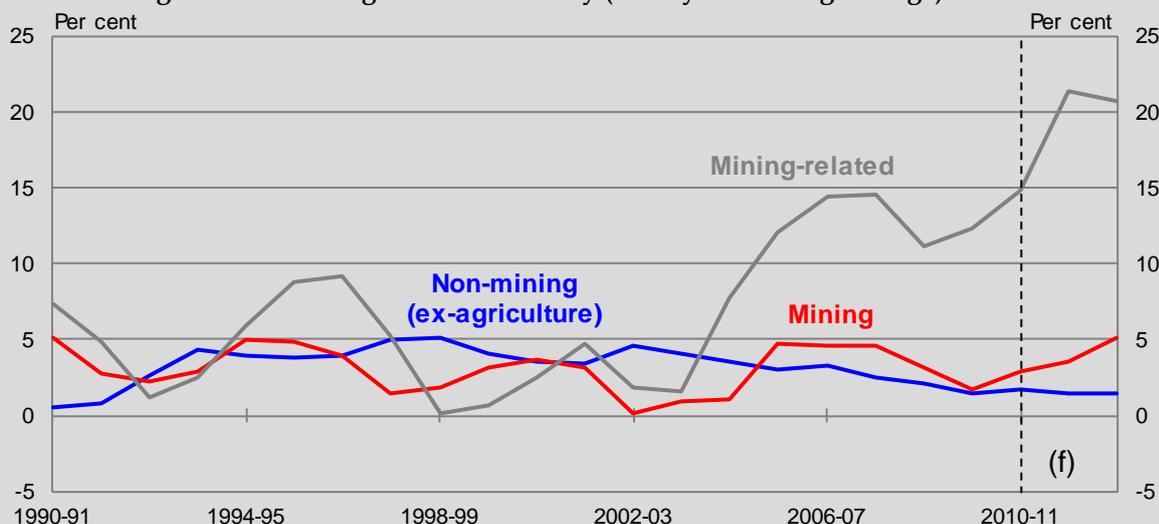
The Reserve Bank Board reduced official interest rates for a second time in 2011 at its December meeting, with the median expectation of market economists predicting a further 25 basis point reduction in official interest rates in the March quarter of 2012. While this represents an additional 25 basis point cut in official interest rates relative to the MYEFO assumption, the impact is neutralised by the change in international and domestic conditions that the Reserve Bank Board is responding to, leaving the aggregate outlook for Australia's economic growth largely unchanged since MYEFO.

Box 1: Mining and Non-Mining Economy

The forecasts can also be decomposed on a production basis to calculate implied growth in the mining, mining-related and non-mining economies. Chart 1 shows the 3 year moving average of real GDP growth for these 3 sectors, highlighting the sustained weakness in the non-mining economy implied by the forecasts.

The forecasts imply average annual growth of 5 per cent in mining output over the three years 2011-12 to 2013-14, but 20 per cent in mining-related output, driven by the forecast strength in mining-related construction. By contrast, the forecasts imply average annual growth of around 1½ per cent for those parts of the non-farm economy not benefiting directly from the resources boom over the same three years, which would be the weakest since the 1990s recession. This is a direct consequence of the high exchange rate on the competitiveness of trade-exposed industries, cautious household spending behaviour and the continuing difficulty some businesses have in accessing finance.

Chart 1: Mining and non-mining economic activity (three year moving average)



Source: ABS Catalogue Number 5206.0 and Treasury.

Australia's **real GDP** is forecast to grow ¾ per cent in 2011-12 and 2012-13, unchanged since MYEFO, before moderating to 3 per cent in 2013-14. However, the composition of the economic growth forecasts has shifted further towards private business investment and household consumption since MYEFO, offset by higher forecast growth in imports.

New **private business investment** is forecast to grow 16½ per cent in 2011-12, 13½ per cent in 2012-13 and 9½ per cent in 2013-14, reaching record highs as a share of GDP. The key driver is resources investment, with the Bureau of Resources and Energy Economics (BREE) estimating that the pipeline of resources investment rose to \$455 billion in October, of which \$232 billion of projects are at an advanced stage of development. The resources sector underpinned a 12.7 per cent surge in new private business investment in

the September quarter, driven by 31.0 per cent growth in engineering construction and a 6.7 per cent increase in new machinery and equipment investment. However, the September quarter CAPEX survey and project level analysis indicate that resources investment intentions for 2011-12 have not changed materially since MYEFO, suggesting that the unanticipated strength in the September quarter reflects a bring-forward of activity. Consequently, the outlook for mining investment and related non-rural commodity exports is largely unchanged from MYEFO.

Paradoxically, forecast growth in private business investment has been upgraded since MYEFO due to additional strength in non-mining investment. Applying long-run realisation ratios to capital expenditure intentions in the September quarter CAPEX survey implies 6.4 per cent growth in manufacturing investment and 4.8 per cent growth in investment by 'other selected industries' in 2011-12 (nominal), albeit off a low base. While some of this investment would appear to be mining-related (around half of the increase in capital expenditure intentions by 'other selected industries' in 2011-12 is attributable to 'rental, hiring and real estate services' and 'professional, scientific and technical services'), it also suggests greater strength in non-mining investment than was factored into the MYEFO forecasts, notwithstanding the generally weak outlook for large parts of the non-mining economy. Business liaison provides some evidence of firms in ailing industries (e.g. manufacturing) undertaking capital investment to refocus their business operations.

Household consumption growth is also expected to be stronger in 2011-12 than forecast at MYEFO, reflecting unanticipated strength in the September quarter. Household consumption grew 1.2 per cent in the September quarter to be 3.8 per cent higher through the year, with consumption of services such as international travel, recreation, accommodation, cafes and restaurants, health and education all growing at very strong rates. A notable development in recent quarters has been the increase in the net expenditure overseas component of household consumption, which has added around 1 percentage point to nominal consumption growth over the past year.¹ Along with the strength of services consumption, this is a factor behind the divergence between growth in retail trade and aggregate household consumption. Consumption growth has been supported by even stronger growth in gross household disposable income, which rose 2.4 per cent in the September quarter and 6.8 per cent through the year. Therefore, notwithstanding the strength of consumption growth, the household saving ratio rose from 9.1 to 10.1 per cent in the September quarter.

The strength of household consumption growth suggests that recent global uncertainty, declining household wealth and lower consumer confidence are yet to have a major bearing on consumer spending decisions. The strength of consumption growth in recent quarters has been somewhat surprising, given the falls in house and equity prices over this period. Therefore, consumption growth is expected to weaken in the near term – partly in response to recent falls in household wealth, but also to reflect weaker labour market conditions and forecasts for moderate wages growth. Household consumption growth is forecast to slow to ½ of a per cent in the December and March quarters before growing in line with household income over the remainder of the forecast period, implying that the household saving ratio will remain broadly steady. In year-average terms, household consumption is forecast to grow ¾ per cent in 2011-12, 3 per cent in 2012-13 and ¾ per cent in 2013-14.

The counterpart to stronger-than-anticipated growth in business investment and household consumption has been strong growth in **imports**. Imports are forecast to grow 13 per cent in 2011-12, 8 per cent in 2012-13 and 7 per cent in 2013-14, with the level of imports now expected to be higher across the forecast horizon than expected at MYEFO. This partly reflects the recent strength of capital and consumption goods imports, but also a reassessment of import penetration ratios in the context of the high Australian dollar and significant import content of the resources investment pipeline. On average, it is now estimated that around 30 per cent of household consumption and around 40 per cent of business investment will be imported over the forecast period, with an import penetration ratio of around two-thirds for LNG investment.

¹ This is the adjustment that the ABS makes to account for overseas expenditure by Australian residents travelling internationally (which counts as household consumption), less expenditure by foreign residents in Australia (which does not). These adjustments are matched by imports and exports.

Forecast growth in **exports** is unchanged over the forecast period since MYEFO. Non-rural commodity exports are forecast to grow around 9 per cent in both 2011-12 and 2012-13, followed by 5 per cent growth in 2013-14. The key drivers are expected to be iron ore and coal capacity expansions, with the export dividend from the substantial LNG investment currently underway expected to materialise from 2015-16. Rural exports are forecast to grow 15 per cent in 2011-12, consistent with forecasts by the Australian Bureau of Agriculture and Resource Economics (ABARES) for a second consecutive bumper wheat harvest, before declining in 2012-13 and 2013-14 on the assumption of a return to more normal seasonal conditions. Exports of services and manufactures are expected to be weak over the forecast horizon, reflecting the high exchange rate and weak external environment. Total exports are forecast to grow 6 per cent in both 2011-12 and 2012-13 and 4 per cent in 2013-14.

With higher forecast growth in imports and the outlook for exports growth unchanged, **net exports** are now expected to detract 1¼ percentage points from GDP growth in 2011-12 (up from 1¼ percentage points at MYEFO), ¾ of a percentage point in 2012-13 (down from 1 percentage point at MYEFO) and 1 percentage point in 2013-14.

The outlook for **dwelling investment** is largely unchanged from MYEFO. While growth in dwelling investment surprised on the upside in the September quarter, this was offset by downward revisions to history, leaving the level of dwelling investment lower than forecast. Forward indicators also continue to deteriorate: building approvals have fallen 30 per cent over the past year; the number of commitments for the construction of new dwellings continues to fall; and housing credit (which also includes credit for the purchase of established dwellings and refinancing) is growing at the lowest annual rate since the series began in 1976. Total returns on housing investment have also fallen over the past year in line with house prices, notwithstanding solid growth in rents. Nonetheless, there is a reasonable pipeline of activity still to be completed in the Victorian medium- and high-density market that will support activity in the near term. Moreover, the flipside to declining house prices is that affordability is improving, helped by lower interest rates, and recent estimates suggest that most capital cities remain undersupplied, supporting the outlook for the dwellings sector in the medium term. Therefore, growth in dwelling investment is forecast to strengthen modestly over the forecast horizon, from 1 per cent in 2011-12, to 1½ per cent in 2012-13 and 2½ per cent in 2013-14.

Forecast growth in **public final demand** is also unchanged from MYEFO. Indeed, there has been no material change to the public final demand forecasts since September JIEG. Some of the MYEFO measures were either transfers to the States or the deferral of tax measures; neither of which affect the national accounts measure of public final demand (although they may affect other components of spending). There have also been offsetting changes at the Commonwealth and state level since the Commonwealth May Budget, with higher Commonwealth consumption in 2011-12 offset by lower state consumption and the decrease in Commonwealth spending in 2012-13 offset by higher state investment. The latest Commonwealth and state budget updates suggest modest growth in public final demand in 2013-14, although these estimates are largely based on assumptions rather than forecasts.

Consistent with MYEFO, the **terms of trade** is forecast to grow 1¼ per cent to a record high in 2011-12, before falling 5¼ per cent in 2012-13 and 2¾ per cent in 2013-14 as additional global supply of coal and iron ore comes online. The MYEFO forecasts reflected a judgement that iron ore prices had fallen to a level that was not sustainable given the potential implications for global supply. Iron ore prices were forecast to pick up through to the end of the December quarter. So far, this has turned out to be the case, with the increase in iron ore prices since the MYEFO forecasts were finalised in mid-November exceeding expectations. However, coal spot prices (both metallurgical and thermal) are weaker than forecast at MYEFO, leaving the aggregate terms of trade forecasts unchanged.

The **current account deficit** is forecast to widen over the next three years, reflecting a rising net income deficit associated with growing net external liabilities and the movement of the trade balance into deficit. Viewed from a savings and investment perspective, the widening current account deficit reflects the strength of private business investment, more than offsetting expectations of continued high household saving and less government dissaving. The current account deficit is expected to be 3¼ per cent of GDP in 2011-12, 5¼ per cent of GDP in 2012-13 and 6¾ per cent of GDP in 2013-14.

The **labour market** outlook is unchanged from MYEFO. The easing in labour market conditions evident since the start of the year has continued through to November, with employment growth slowing from an average monthly pace of 30,000 in the second half of 2010 to 4,000 in 2011. Empirical models suggest that the weakness of employment growth in 2011 is partly the result of a significant bring-forward of hiring into 2010, when employment rose by 362,000 persons in the context of relatively weak output growth, perhaps in anticipation of tighter labour market conditions and greater difficulty sourcing labour in the period ahead. However, business surveys suggest that global uncertainty and pressures on some of the large employing sectors of the economy – such as manufacturing and retail – are also making employers more cautious about taking on new workers. One manifestation of this may be recent increases in average work hours, which could suggest that employers are meeting demand with longer hours from their existing workers, rather than committing to increasing their workforce.

The ANZ job advertisements series has fallen over 2½ per cent over the past 3 months, consistent with the MYEFO forecasts for continued relatively weak employment growth in the near term and a gradual rise in the unemployment rate to 5½ per cent by June 2012. Employment growth is forecast to strengthen to 1½ per cent through the year to the June quarters of 2013 and 2014, which would be consistent with the unemployment rate remaining steady at 5½ per cent through to the June quarter of 2014. The forecasts assume a gradual decline in average work hours over the forecast period, implying average annual labour productivity growth on an hours-worked basis of around 1¾ per cent over the forecast period.

Weaker labour market conditions have coincided with a decline in underlying **inflation**, which was 0.3 per cent in the September quarter to be around 2½ per cent through the year. Upstream price pressures were also weak in the September quarter, with intermediate and preliminary producer prices rising just 0.1 per cent in the September quarter. As at MYEFO, inflation and wages growth are expected to remain well contained over the next three years, in line with the trend growth in the economy and receding capacity pressures. The Wage Price Index is forecast to increase 3¾ per cent in both 2011-12 and 2012-13, with continued strong wages growth in resources-related industries partly offset on average by more modest increases in other parts of the economy. Abstracting from the one-off temporary impact of the carbon price, both headline and underlying inflation are forecast to rise from 2¼ per cent through the year to June 2012 to 2½ per cent through the year to both the June quarter 2013 and the June quarter 2014. In the current environment of easing capacity pressures, there would seem to be little risk of a substantial increase in market-driven inflation over the forecast horizon, although growth in administered prices is expected to remain firm.

Nominal GDP is forecast to grow 6 per cent in 2011-12, 5¼ per cent in both 2012-13 and 2013-14. Compared with MYEFO, forecast growth in nominal GDP has been revised down ¼ of a percentage point in 2011-12 and revised up ¼ of a percentage point in 2012-13. The downward revision in 2011-12 reflects an unanticipated fall in domestic prices in the September quarter, with the gross national expenditure deflator falling 0.1 per cent – the weakest result since the June quarter 2009 – due to a decline in the public expenditure deflator. The fall in the public expenditure deflator reflected a decline in both the consumption and investment deflators, which is difficult to reconcile with growth in public sector wages and cost pressures on government capital budgets. Therefore, the forecasts offset the decline in the September quarter with additional strength in future quarters, resulting in a reprofiling of the nominal GDP growth outlook compared with MYEFO.

The possibility of a major financial collapse in Europe represents a significant downside risk for the domestic economy. While Australia's trade is primarily with Asia and our direct exposure to European financial institutions is low, the past few months have again highlighted the importance of financial market and confidence channels. Moreover, our trade with emerging Asia would not be immune to a sharp deterioration in Europe, with signs that weak external demand and reduced availability of trade finance is already weighing on growth in the region. Commodity markets could also be expected to weaken, raising the prospect of a sharper decline in Australia's terms of trade than currently forecast. While there is a large pipeline of committed LNG projects that would be expected to continue, some planned expansions to coal and iron ore capacity could be delayed, including those that are reliant on external financing. An additional downside risk concerns the possibility of a second consecutive year of rainfall-induced disruptions to coal and agricultural production, given the emerging La Nina weather pattern.

Table 3: Domestic economy forecasts

	Outcomes (a)				Forecasts				Outcomes (b)				Forecasts			
	Year average		Year average		Through the year		Through the year		Through the year		Through the year		Through the year			
	2010-11	2011-12	2012-13	2013-14	June 2011	June 2012	June 2013	Jun 2014	June 2011	June 2012	June 2013	Jun 2014	June 2011	June 2012	June 2013	Jun 2014
Panel A - Demand and output(c)																
Household consumption	3.1	3 1/4	3	3 1/4	3.1	3	3 1/2	3 1/4	3.1	3	3 1/2	3 1/4	3.1	3	3 1/2	3 1/4
Private investment																
Dwellings	0.9	1	1 1/2	2 1/2	-2.9	4 1/2	- 1/2	4 1/2	-2.9	4 1/2	- 1/2	4 1/2	-2.9	4 1/2	- 1/2	4 1/2
Total business investment(d)	5.7	16 1/2	13 1/2	9 1/2	9.7	15	17 1/2	5 1/2	9.7	15	17 1/2	5 1/2	9.7	15	17 1/2	5 1/2
Non-dwelling construction(d)	9.1	20	16	13	8.5	16 1/2	28 1/2	5 1/2	8.5	16 1/2	28 1/2	5 1/2	8.5	16 1/2	28 1/2	5 1/2
Machinery and equipment(d)	3.0	17	12 1/2	8 1/2	13.3	17	11 1/2	7 1/2	13.3	17	11 1/2	7 1/2	13.3	17	11 1/2	7 1/2
Private final demand(d)	3.2	5 3/4	5 1/4	4 3/4	3.7	5 1/2	6 1/2	3 3/4	3.7	5 1/2	6 1/2	3 3/4	3.7	5 1/2	6 1/2	3 3/4
Public final demand(d)	3.4	1 1/4	-1 1/4	1/4	1.1	4 1/4	-7	4 3/4	1.1	4 1/4	-7	4 3/4	1.1	4 1/4	-7	4 3/4
Total final demand	3.2	4 3/4	3 3/4	3 3/4	3.0	5 1/4	3 1/4	4	3.0	5 1/4	3 1/4	4	3.0	5 1/4	3 1/4	4
Change in inventories(e)	0.6	0	0	0	1.4	0	0	0	1.4	0	0	0	1.4	0	0	0
Gross national expenditure	3.9	4 3/4	3 3/4	3 3/4	4.4	4 3/4	3 1/4	4	4.4	4 3/4	3 1/4	4	4.4	4 3/4	3 1/4	4
Exports of goods and services	0.3	6	6	4	-3.6	11	2	5	-3.6	11	2	5	-3.6	11	2	5
Imports of goods and services	10.4	13	8	7	9.1	11	7 1/2	5 1/2	9.1	11	7 1/2	5 1/2	9.1	11	7 1/2	5 1/2
Net exports(e)	-2.0	-1 3/4	- 3/4	-1	-2.6	- 1/2	-1 1/4	- 1/4	-2.6	- 1/2	-1 1/4	- 1/4	-2.6	- 1/2	-1 1/4	- 1/4
Gross domestic product	1.9	3 1/4	3 1/4	3	1.9	4 1/4	2	3 3/4	1.9	4 1/4	2	3 3/4	1.9	4 1/4	2	3 3/4
Non-farm product	1.8	3 1/4	3 1/4	3	1.9	3 3/4	2 3/4	3 1/2	1.9	3 3/4	2 3/4	3 1/2	1.9	3 3/4	2 3/4	3 1/2
Farm product	9.4	1	-3	-1	-3.3	35	-27	20	-3.3	35	-27	20	-3.3	35	-27	20
Nominal gross domestic product	8.3	6	5 1/4	5 1/4	6.0	6	4	6 1/2	6.0	6	4	6 1/2	6.0	6	4	6 1/2
Panel B - Other selected economic measures																
External accounts																
Terms of trade	20.6	1 3/4	-5 1/4	-2 3/4	12.8	-7 1/4	-3	-3	12.8	-7 1/4	-3	-3	12.8	-7 1/4	-3	-3
Current account balance																
\$billion	-33.2	-48 1/2	-82	-108 3/4	-6.7	-15	-22 3/4	-30 3/4	-6.7	-15	-22 3/4	-30 3/4	-6.7	-15	-22 3/4	-30 3/4
Percentage of GDP(f)	-2.4	-3 1/4	-5 1/4	-6 1/2	-1.9	-4	-5 3/4	-7 1/4	-1.9	-4	-5 3/4	-7 1/4	-1.9	-4	-5 3/4	-7 1/4
Labour market																
Employment (labour force survey basis)	2.9	1	1 1/2	1 1/2	2.2	1	1 1/2	1 1/2	2.2	1	1 1/2	1 1/2	2.2	1	1 1/2	1 1/2
Unemployment rate (per cent)(g)	5.1	5 1/4	5 1/2	5 1/2	4.9	5 1/2	5 1/2	5 1/2	4.9	5 1/2	5 1/2	5 1/2	4.9	5 1/2	5 1/2	5 1/2
Participation rate (per cent)(g)	65.7	65 1/2	65 1/2	65 1/2	65.5	65 1/2	65 1/2	65 1/2	65.5	65 1/2	65 1/2	65 1/2	65.5	65 1/2	65 1/2	65 1/2
Prices and wages																
Consumer Price Index (original)																
- headline	3.1	3	3	2 1/2	3.6	2 1/4	3 1/4	2 1/2	3.6	2 1/4	3 1/4	2 1/2	3.6	2 1/4	3 1/4	2 1/2
- underlying	2.5	2 1/2	2 3/4	2 1/4	2.8	2 1/4	2 3/4	2 1/2	2.8	2 1/4	2 3/4	2 1/2	2.8	2 1/4	2 3/4	2 1/2
Gross non-farm product deflator	6.0	2 1/4	2 1/4	2 1/2	3.6	1 3/4	2	2 1/2	3.6	1 3/4	2	2 1/2	3.6	1 3/4	2	2 1/2
Wage Price Index	3.8	3 3/4	3 3/4	3 3/4	3.8	3 3/4	3 3/4	3 3/4	3.8	3 3/4	3 3/4	3 3/4	3.8	3 3/4	3 3/4	3 3/4

(a) Calculated using original data unless otherwise specified.

(b) Calculated using seasonally adjusted data unless otherwise specified.

(c) Chain volume measure, except for nominal GDP.

(d) Excluding second-hand asset sales from the public sector to the private sector.

(e) Percentage point contribution to growth in real GDP.

(f) The outcomes and forecasts in the final four columns are the percentage of GDP in the June quarter.

(g) The outcomes and forecasts in the final four columns are the rate in the June quarter.

Note: The forecasts for the domestic economy are underpinned by several technical assumptions. The exchange rate is assumed to remain around its level at the time the forecasts were prepared, with a trade-weighted index of around 76 and a \$US exchange rate of around 102c. Domestic interest rates are assumed to decline over the forecast period, in line with expectations of market economists. World oil prices (Tapis) are assumed to remain around \$US118 per barrel. The farm sector forecasts are based on average seasonal conditions over the remainder of the forecast period.

Source: ABS Cat. No. 5206.0, 5302.0, 6202.0, 6345.0, 6401.0, unpublished ABS data and Treasury.