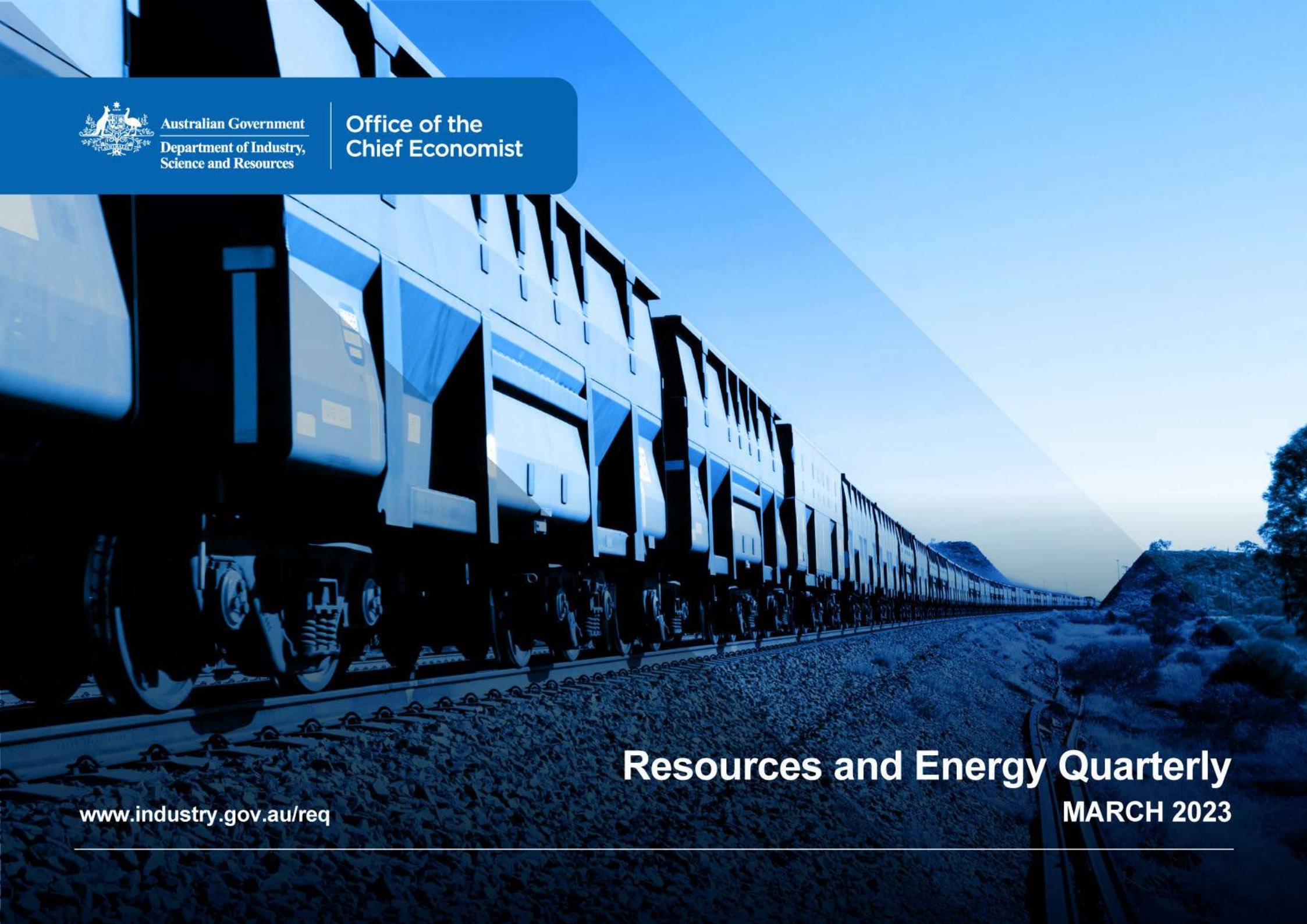

Australian Government
Department of Industry, Science and Resources

Office of the Chief Economist

Resources and Energy Quarterly

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Further information

For more information on data or government initiatives please access the report from the Department's website at: www.industry.gov.au/oce

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Foreword

Australian resource and energy exports are forecast to set a record of $464 billion in 2022–23. This is the result of a new wave of surging bulk commodity revenues: the second such wave to benefit Australia in the past 2-3 years.

The first extraordinary wave in Australian resource and energy export revenue came in 2021, as iron ore prices pushed to record highs. Ongoing problems with Brazilian iron ore supply combined with strong iron ore demand from China.

The latest wave of bulk commodity revenues came from the spectacular surge in energy prices in 2022, mainly originating from the fallout over Russia's invasion of Ukraine. Gas/LNG and (metallurgical and thermal) coal prices easily surpassed previous record highs, as many Northern Hemisphere nations scrambled to secure alternatives to Russian supplies.

Bans on Russian exports of oil and other fossil fuels by most advanced Western nations have now taken effect. Transport and infrastructure constraints will likely prevent a full diversion of Russian energy exports to nations with no sanctions. The net result is a drop in world energy supply, as some Russian output becomes stranded. Russia has recently moved to cut oil exports. Barring much weaker demand, the prices of energy commodities are likely to remain relatively high over the outlook period.

LNG earnings are forecast at $91 billion in 2022–23, as high LNG prices more than offset the impact of slightly weaker LNG export volumes. This is three times the revenue of 2020–21. Record prices will see thermal coal exports reach $65 billion this financial year, up from around $16 billion in 2020–21.

Energy prices have generally fallen sharply in recent months, as the world economy slows and supply chains reorganise further. COVID- and weather-induced supply disruptions among major producers are also easing, lowering prices. Australian resource and energy export earnings are thus set to fall noticeably.

A number of factors suggest our resource and energy export earnings should nevertheless hold at relatively healthy levels over the outlook period. Firstly, the end of China's zero-COVID policy will likely trigger a pick up in sales to China, given that nation's large share of world usage and the pent-up demand resulting from three years of COVID-19 restrictions. Low unemployment/underemployment in Western nations is likely to persist for some years, stoking the demand for resource and energy commodities. Third, the global energy transition is expected to boost our exports of lithium and base metals. Lithium product exports are expected to exceed $18.5 billion in 2022–23, up from $4.9 billion in 2021–22. Lithium and base metals (and their raw material inputs) will account for almost as much export revenue as all coal types by 2027–28. India's appetite for resource/energy commodities is likely to show strong growth over the outlook period, as the nation develops. Australia is well placed to supply India with these products. Finally, stranded Russian commodity production should help sustain Australian resource and energy commodity exports.

After 2023–24, earnings from LNG and thermal coal are likely to fall back towards pre-COVID levels. However, thermal coal miners are likely to enjoy relatively high prices over the outlook period, as a lack of spending to bring on new supply matches the impact of diminishing world demand.

The La Niña weather pattern has ended and the Indian Ocean Dipole has normalised. Together, this means there is a much lower chance of wetter-than-normal conditions in eastern Australia in 2023–24 — and thus less likelihood of disruptions to the mining/transportation of bulk commodities. These disruptions helped drive coal prices higher in 2022. Statistically, a La Niña weather pattern is unlikely in the first few years of the outlook period. The other risks to the forecast for Australia's resource and energy export earnings after 2022–23 are evenly skewed. Markets have priced in weaker world economic growth and the loss of some Russian resource and energy commodity output from world supply in 2023. Should inflation prove harder to tame, central banks may have to hold monetary policy tighter — and for longer — risking slower than expected growth and thus lower commodity demand.

Overview

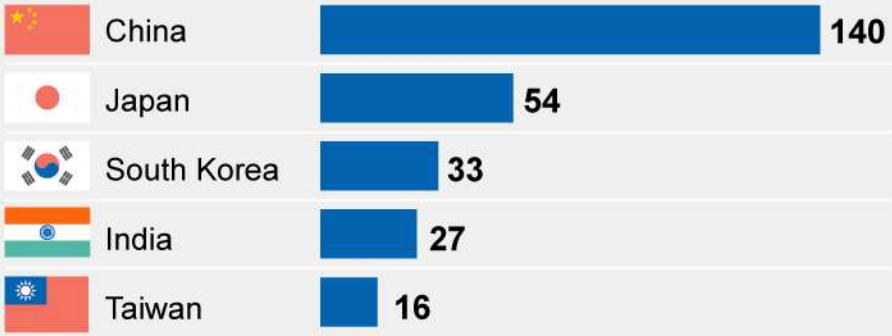
Australia's mining sector

Contributes to around ***13.7% of GDP***

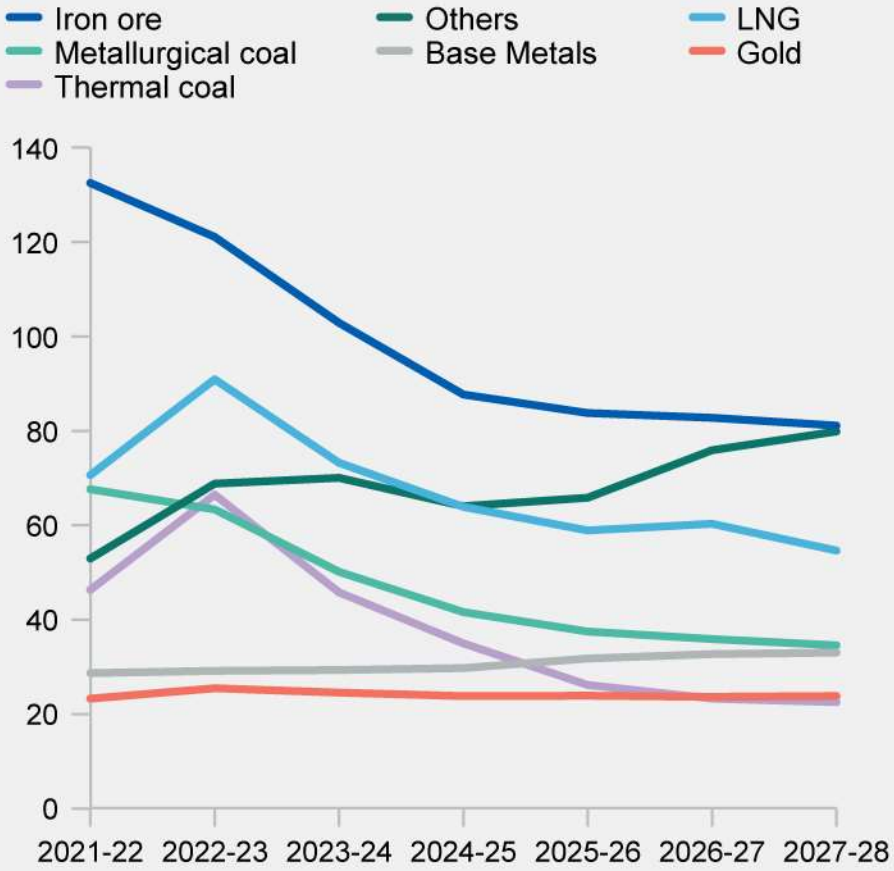
Makes up more than ***two-thirds*** of Australia's total merchandise exports

Directly employs ***over a quarter of a million people***

Major markets for Australia's resources and energy exports in 2021-22, A$billion



Australia's resource and energy exports, A$billion (real prices)



SOURCE: ABS; OCE

1.1 Summary

- High energy commodity prices and strength in the US dollar have driven another surge in export earnings. After a record $422 billion in 2021–22, resource and energy export earnings are forecast to lift to $464 billion in 2022–23, before falling back over the outlook period.
- Energy commodity prices continue to unwind from the war-driven spike of 2022, as energy markets and usage rearranges. But with China ending its COVID lockdowns, commodity prices should level out in 2023.
- By 2028, the export value of lithium and base metals (and their raw material inputs) will equal the export value of all coal types combined.

1.2 Macroeconomic, policy, trade and other factors

World economic growth has continued to slow in recent months, but the abrupt ending of China's zero-COVID policy in late 2022 has seen an improvement in sentiment in resource and energy commodity markets. Notwithstanding Western trade sanctions on Russia, global supply chains have been clearing, helping to lower goods inflation. Periodic supply problems could emerge, as China is hit by outbreaks of COVID infections. Central banks have continued to raise official interest rates, to try to make sure that medium/long term inflation expectations don't rise unacceptably. Robust labour markets in many major economies are cooling gradually, reducing wage pressures.

It is likely to take some quarters before the Chinese economy grows strongly on the back of pent-up consumer demand: fresh COVID-19 outbreaks will likely cause significant disruption throughout 2023. As Chinese economic growth picks up, the chances of a soft landing in the world economy in 2023 rise. China's current relatively low inflation rate gives the Chinese authorities better scope to stimulate the domestic economy than other major economies. Such measures would support global resource and energy commodity prices in the first half of the outlook period. Less favourable demographic trends and the debt problems beleaguering the Chinese property sector will likely hamstring the demand for metals over the same period.

India is likely to grow as a source of resource and energy commodity demand over the outlook period, as the economy grows and develops further.

The European economy is recovering from the spike in energy prices that did much to hurt both sentiment and activity in 2022. Since the December 2022 *REQ,* the US Federal Reserve has slowed the pace of monetary tightening further, as the US inflation rate starts to fall back from 30-year highs. Services inflation remains a problem though; with further Fed rate hikes thus likely, the US dollar will remain well supported. A slowing in core inflation pressures in major economies seems likely over the first half of the forecast horizon. This should allow the major Western central banks to cease monetary tightening in 2023.

The impacts of the COVID-19 pandemic and the Russian invasion of Ukraine are likely to fade over the forecast period. The IMF forecasts world GDP growth of 2.9% in 2023 and 3.1% in 2024, down from growth of 3.4% in 2022. World growth of 3.3% is forecast over the rest of the outlook period — down from the 2000-19 average of 3.8%. The IMF expects China to grow by 5.2% in 2023 and 4.5% in 2024.

The loss of much of the Western European market — the largest and closest pre-invasion market for Russia's energy exports — prohibitions on the transfer of key technology and equipment to Russian industry, and the withdrawal of Western investment, will all weigh heavily on Russian exporters over the outlook period. China and India will benefit from relatively cheap Russian fossil fuel supply. Unlike crude oil sales, Russia will find it more difficult to sell diesel and other refined oil products to China and India, since those countries have their own large oil refining operations.

The ongoing fallout from the Russian invasion of Ukraine is expected to see energy prices remain elevated in 2023 at least. With many nations pushing to achieve net zero by/before 2050, low investment in new fossil fuel supply will act to keep fuel prices relatively high, despite poor demand.

The high price of fossil fuels is likely to accelerate the push towards low emission technologies over the outlook period. Commodities used in low emission technologies (lithium, copper and nickel) also seem set to trade at relatively high prices, as supply struggles to keep up with demand.

The recent trend towards trade blocs will likely intensify over the outlook period. Investment flows will help cement these trends. An example will be the large amount of US gas liquefaction capacity coming onstream in the first half of the outlook period: the US will become the world's largest LNG supplier, likely displacing Russian fossil fuels sales to the West. Many nations/regional blocs will continue to seek to become self sufficient in critical technologies and commodities, as a way of enhancing national security.

The US Inflation Reduction Act will be a major driver of this trend. But economic nationalism will come at a cost to the world economy: rather than the lowest-cost producers/manufacturers (usually China) dominating world production, output of critical technologies and commodities will consume more of the world's resources and be much more diversified than at present.

The Australian dollar has regained some of the ground lost against the US dollar in the first ten months of 2022. The AUD/USD is assumed to head towards the mid USD0.70's over the first half of the outlook period, and then average USD0.75 (its post float average) over the rest of the forecast horizon.

Higher global interest rates pose a downside risk to global economic activity — and thus Australian resource and energy exports — in the early part of the outlook period. Geopolitical tensions are likely to remain an ongoing risk to the outlook for world economic growth — and hence resource and energy commodity demand. War and the threat of war, impact adversely on household and business confidence. Falling confidence tends to see expenditure on 'big ticket' items deferred as a precaution. Big ticket items (vehicles, plant, buildings) often have a large metal content.

1.3 Export values

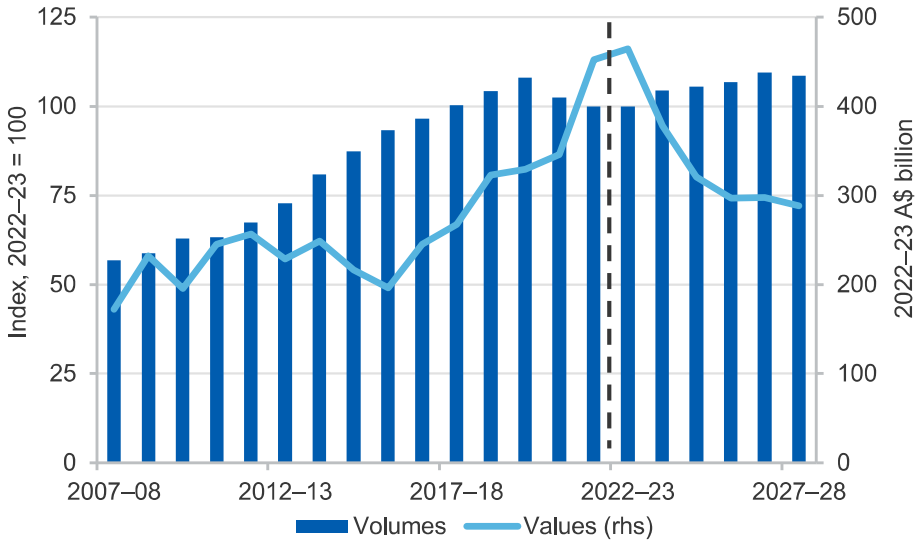
Australia's export values are forecast to be $464 billion in 2022–23

In the March quarter 2023, the Resources and Energy Export Values Index rose by 13% from the March quarter 2022; a rise in volumes added to the impact of a gain in prices.

Despite a slowing world economy, resource and energy exports of $464 billion in 2022–23 are set to easily break last year's record of $422 billion (Figure 1.1). However, exports are forecast to fall to $378 billion (real terms) in 2023–24, as commodity prices settle back at levels seen before the recent spikes.

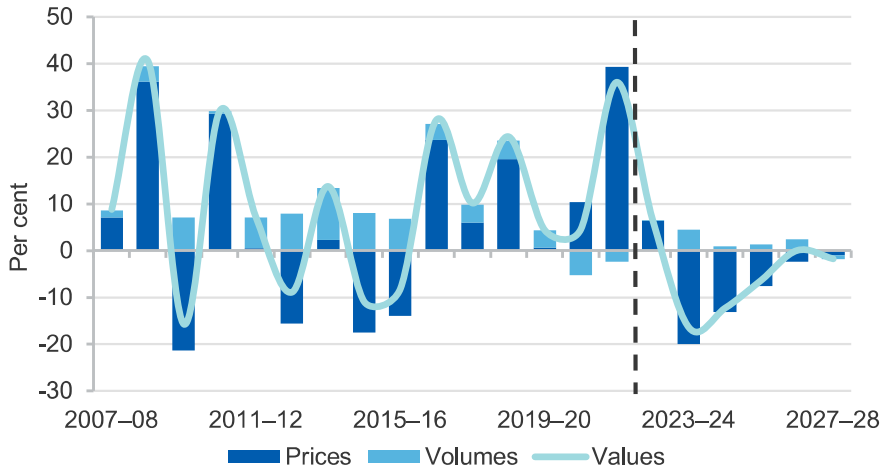
As prices gradually start to level out in 2025–26, so too will the decline in resource and energy earnings (Figure 1.2).

Figure 1.1: Australia's resource and energy export values/volumes



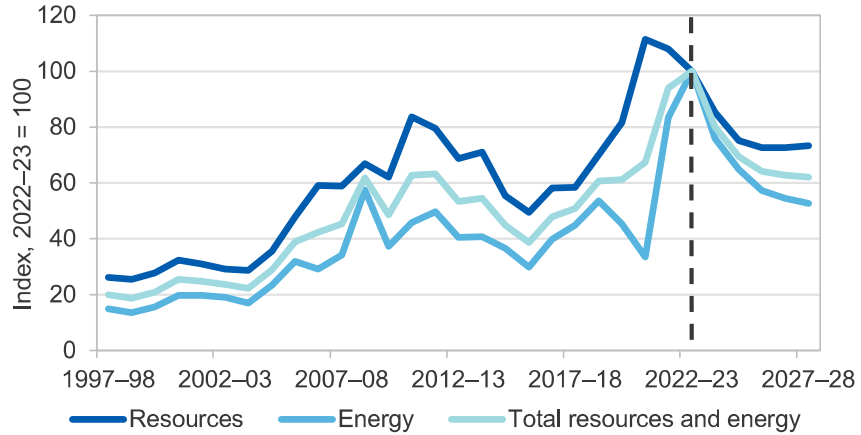
Source: ABS (2023) International Trade in Goods and Services, 5368.0; Department of Industry, Science and Resources (2023)

Figure 1.2: Annual growth in Australia's resources and energy export values, contributions from prices and volumes



Source: ABS (2023) International Trade in Goods and Services, 5368.0; Department of Industry, Science and Resources (2023)

Figure 1.3: Resource and energy export prices, AUD terms



Notes: The export price index is based on Australian dollar export unit values (EUVs, export values divided by volumes); the export price index is a Fisher price Index, which weights each commodity's EUV by its share of total export values.

Source: ABS (2023) International Trade in Goods and Services, 5368.0; Department of Industry, Science and Resources (2023)

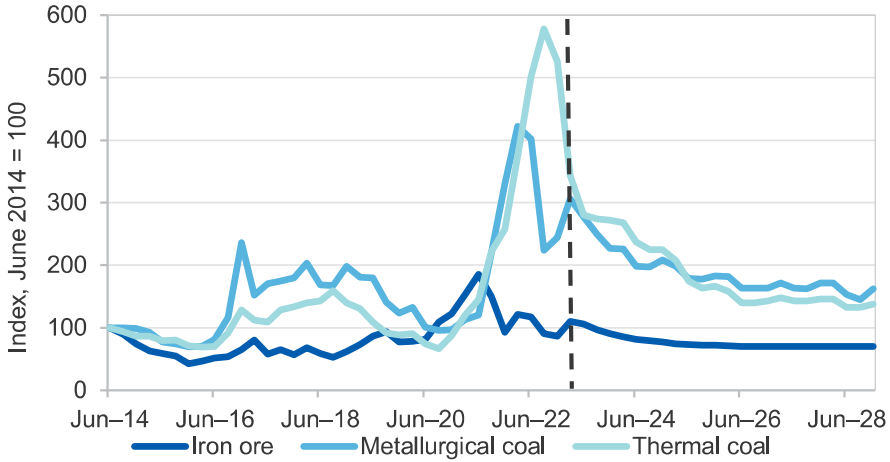
Energy shortages have eased and the world economy is slowing

The slowdown in the world economy and the re-organisation and improvement in energy commodity supply has reduced generally reduced commodity prices. In Australian dollar terms, the OCE's Resources and Energy Commodity Price Index fell by 6% (preliminary estimate) in the March quarter 2023, but was up 2% on a year ago. In US dollar terms, the index fell by 2% in the quarter, to be down 3% on a year ago. Resource export prices (Australian dollar terms) fell by 2% in the year to the March quarter 2023, while energy commodity prices rose by 6% (Figure 1.3).

1.4 Prices

Since the December 2022 *Resources and Energy Quarterly*, resource and energy prices have generally fallen, as fears grow of a world slowdown. The iron ore price has bucked the trend, and remains well above the cycle low of November 2021. Expectations of a lift in Chinese demand have added to the impact of supply issues in major exporting nations (Figure 1.4). Prices are likely to fall over the outlook period, as world supply lifts faster than world demand.

Figure 1.4: Bulk commodity prices



Notes: Prices are in US dollars, and are the international benchmark prices

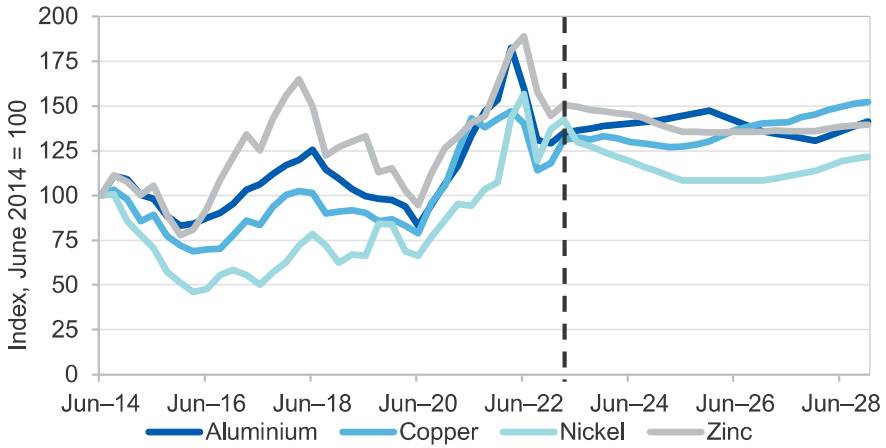
Source: Bloomberg (2023); Department of Industry, Science and Resources (2023)

Weaker demand and improved supply have seen Australian thermal coal prices fall sharply in early 2023, but they are high in historical terms. Bad weather and flooding in major producing regions added to the impact of high demand for non-Russian cargoes in 2022. Prices are expected to fall over the outlook period, as trade flows re-organise further and supply lifts. Metallurgical coal prices are high, as the market looks to stronger future Chinese demand. Prices are likely to fall from here, as supply lifts.

Oil prices have steadied in a US$70-90 a barrel range in recent months. The end of zero-COVID in China has seen consumption forecasts raised. Artificial and operational constraints on OPEC+ supply continue, keeping the market tight. Spot LNG prices have dropped back to levels seen before the Russian invasion of Ukraine, helped by a warmer than normal Northern Hemisphere winter. Prices are likely to be elevated in the first half of the outlook period, as some Russian gas output is stranded.

The price of gold has risen significantly since the last REQ, helped by a small number of bank failures. Record central bank net purchases in 2022 are unlikely to be repeated over the forecast period. The price is likely to fall modestly in the next five years, as real bond yields hold their gains.

Figure 1.5: Base metal prices



Notes: Prices are in US dollars, and are the international benchmark prices

Source: Bloomberg (2023); Department of Industry, Science and Resources (2023)

Base metal prices have risen, as hopes of a soft landing in the world economy add to the impact of low inventories. The loss of some Russian supply (especially nickel and aluminium) from world markets would boost prices (Figure 1.5). Prices should be flat over the forecast period, as supply slowly catches up with demand and stockpiles stop falling.

1.5 Export volumes

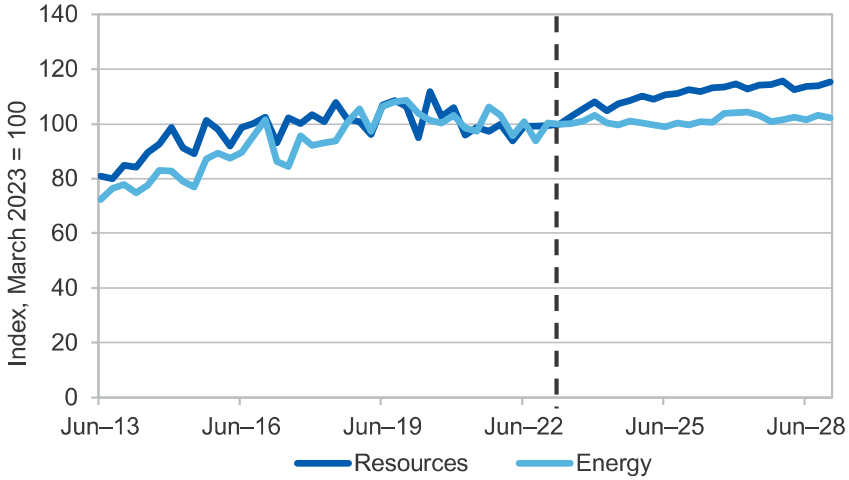
March quarter export volumes rose marginally

The Resources and Energy Export Volumes Index (preliminary estimate) rose 0.3% in the March quarter 2022 from the December quarter, and was 6% higher than a year before.

Within this total, resource commodity volumes fell by 0.3% in the year to the March quarter 2023, while energy commodity volumes rose by 4.8% (Figure 1.6).

Energy exports were impacted by production and transport problems in the March quarter 2022, lowering the base: operational, weather and COVID-19 related workforce issues were central to these disruptions.

Figure 1.6: Resource and energy export volumes



Source: Department of Industry, Science and Resources (2023)

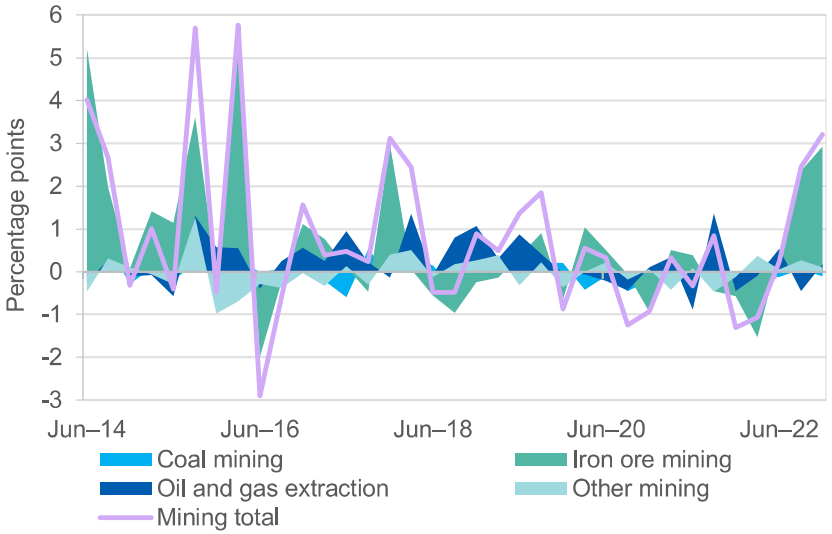
In volume terms, resource exports are likely to show further significant growth over the outlook period, particularly in 2023 and 2024. The volume of energy exports has been constrained by weather conditions and problems associated with the pandemic. High prices will likely cause some demand destruction in the outlook period, and the global energy transition will also impact adversely on export volumes.

1.6 Contribution to growth and investment

Mining output grew strongly while the overall economy grew modestly

Australia's real Gross Domestic Product rose by 0.5% in the December quarter 2022, to be up 2.7% from the December quarter 2021. Mining value-added rose by 3.2% in the December quarter, to be up 4.8% over the previous year (Figure 1.7). The quarterly gain was driven by rises in Iron Ore Mining (up by 4.8%), Oil and Gas Extraction (up by 1.0%), Exploration and Mining Support Services (up by 2.5%) and Other Mining (up by 0.9%). The rises were partly offset by a fall in Coal Mining (down by 1.4%), due to continued wet weather and flooding on the East Coast.

Figure 1.7: Contribution to quarterly growth, by sector



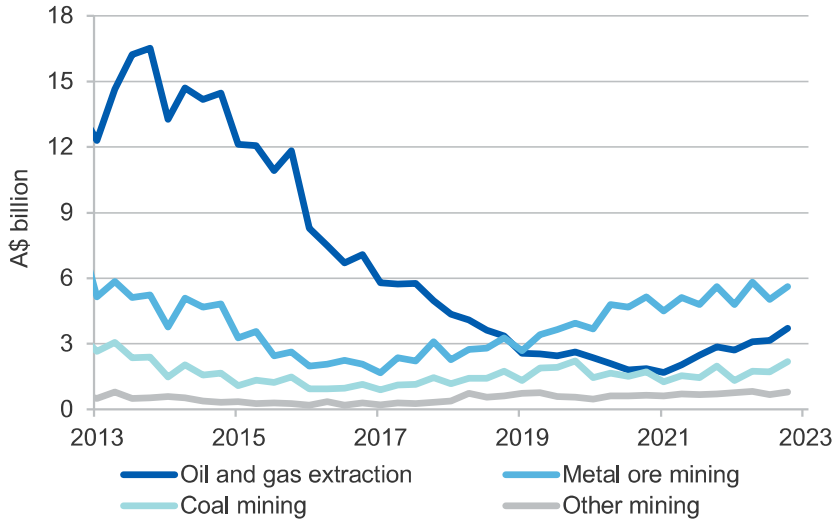
Source: ABS (2023) Australian National Accounts, 5206.0

In the coming five years, while the resource sector will make a significant contribution to real GDP growth, the contribution of the energy sector may diminish. The disruptions to production of the past few years — due to the COVID-19 pandemic and weather-related issues — are likely set to ease. Coal and LNG producers will benefit from relatively high prices. Metal production (ferrous and non-ferrous) should experience healthy growth.

Mining investment is picking up

The latest ABS Private New Capital Expenditure and Expected Expenditure survey shows that Australia's resources industry invested $12.3 billion in the December quarter 2022. This was up 10.0% from the December quarter 2021. In quarterly terms, investment rose across the board: for oil and gas, metal ores, coal, and other mining (Figure 1.8). The December quarter is typically a strong one for capex.

Figure 1.8: Mining capex by commodity, not seasonally adjusted



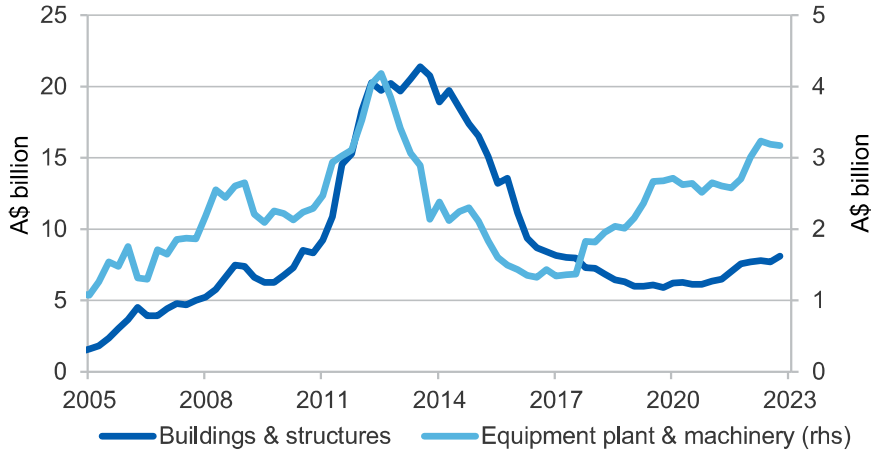
Notes: Other mining includes non-metallic mineral mining and quarrying and exploration and other mining support services; chart data is in nominal, original terms

Source: ABS (2023) Private New Capital Expenditure and Expected Expenditure, 5625.0

Expenditure for equipment, plant and machinery softened in the December quarter, but investment in buildings and structures rose (Figure 1.9).

Spending on equipment, plant and machinery has risen steadily since 2016, with spending on buildings and structures rising more recently.

Figure 1.9: Mining industry capital expenditure by type, quarterly



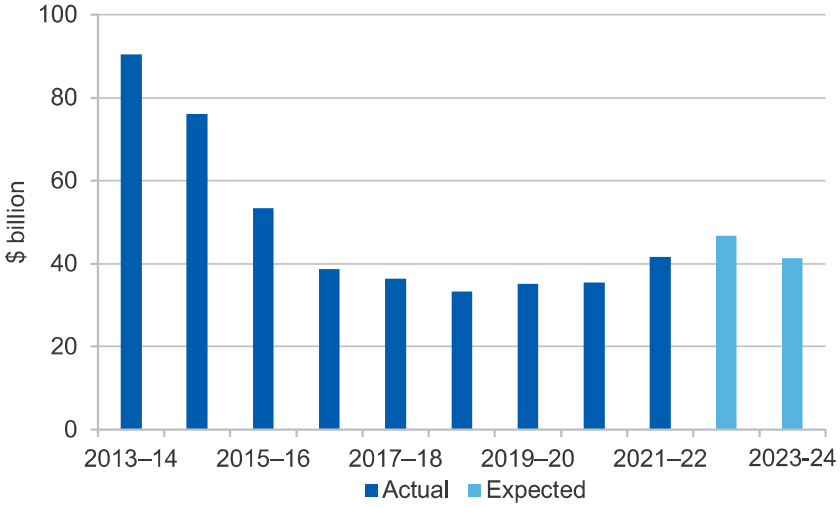
Notes: Chart data is in nominal terms, seasonally adjusted.

Source: ABS (2023) Private New Capital Expenditure and Expected Expenditure, 5625.0

Forward expectations suggest that total mining industry investment in 2022–23 will be higher than in 2021–22 (Figure 1.10). The first estimate for 2023–24 has been released, and suggests the mining industry will invest $41 billion over the year. This is 7% higher than the first estimate for 2022–23, but is below the fourth estimate (estimates tend to gain with each update). Strong prices for gold and various minerals used in low-emissions technology have supported a recent uptick in investment.

Exploration expenditure (adjusted for inflation) edged down to $930 million in the December quarter 2022. Exploration has been trending down since mid-2022, but remains well above the recent low of $783 million recorded in the June quarter 2020. Notwithstanding the December quarter decline, exploration spending remains solid, and generally aligned to the recent positive trend for capital spending (Figure 1.11) reflecting a solid outlook for minerals used in low emission technologies.

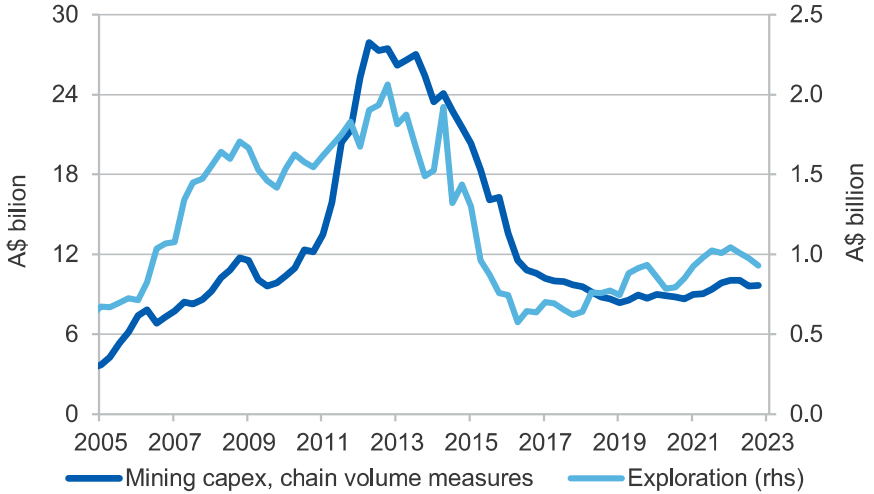
Figure 1.10: Mining industry capital expenditure, fiscal year



Notes: Chart data is in nominal terms

Source: ABS (2023) Private New Capital Expenditure and Expected Expenditure, 5625.0

Figure 1.11: Mining capital expenditure vs exploration (real, quarterly)



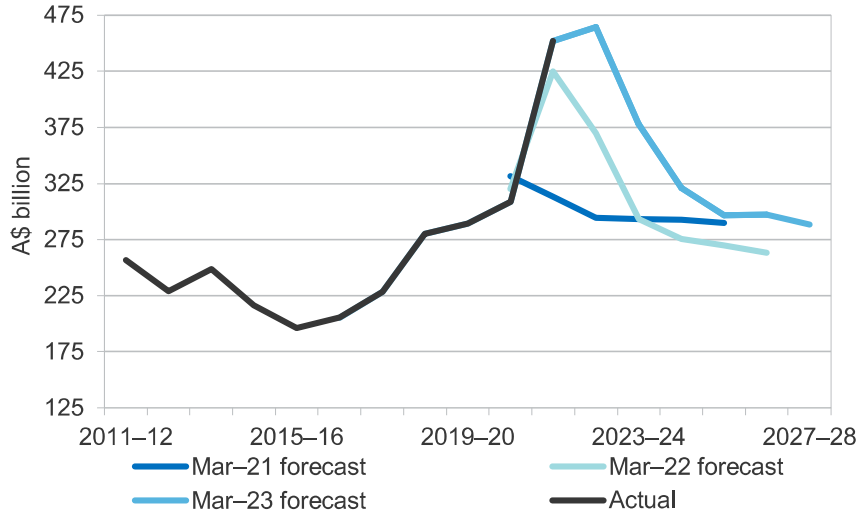
Source: ABS (2023) Private Capital Expenditure Survey, Chain Volume measure, 5625.0

1.7 Revisions to the outlook

The estimate for Australia's resources and energy exports in 2022–23 is $5 billion higher than the forecast contained in the December quarter 2022 *Resources and Energy Quarterly*. The forecast for 2023–24 (nominal prices) is up by $4 billion from the same report (Figure 1.12). This upward revision has been driven by a lift in forecast iron ore and metallurgical coal earnings and a weaker than expected exchange rate against the US dollar (AUD/USD). Thermal coal earnings have been revised down, partly in light of the sharp price falls of recent months.

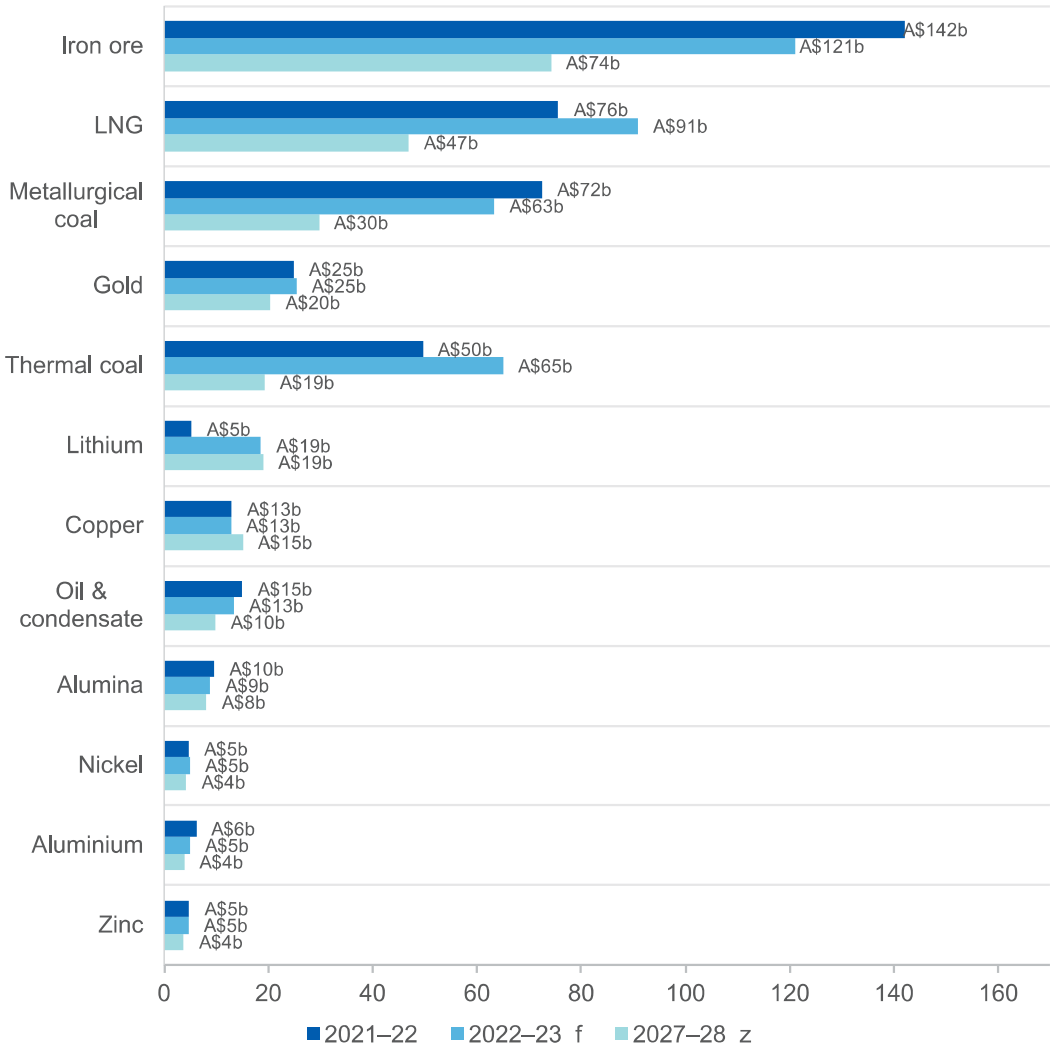
Iron ore earnings in 2022–23 have been revised up by $8 billion, and by $7 billion in 2023–24. The revisions reflect forecasts of a shallower fall in prices than envisioned in the December 2022 REQ. Chinese iron ore demand in 2023 is likely to be stronger than previously expected. Further out, earnings are expected to decline at a similar rate and at a similar time as envisaged in March 2022.

Figure 1.12: Resource and energy exports, by forecast release



Source: Department of Industry, Science and Resources (2023)

Figure 1.13: Australia's major resources and energy commodity exports, 2022–23 dollars % change from 2021–22 CAGR % change from 2021–22



	2022–23 f			2027–28 z		
	volume	EUV	value	volume	EUV	value
Iron ore	▲ 1	▼ -16	▼ -15	▲ 2	▼ -12	▼ -10
LNG	▼ -2	▲ 22	▲ 20	▼ -1	▼ -7	▼ -8
Metallurgical coal	▲ 1	▼ -14	▼ -13	▲ 1	▼ -15	▼ -14
Gold	▲ 9	▼ -6	▲ 2	▲ 5	▼ -7	▼ -3
Thermal coal	▼ -7	▲ 41	▲ 31	→ 0	▼ -14	▼ -15
Lithium	▲ 37	▲ 158	▲ 254	▲ 12	▲ 10	▲ 24
Copper	▲ 8	▼ -9	▼ -2	▲ 3	▼ -1	▲ 2
Oil & condensate	▼ -6	▼ -6	▼ -11	▲ 1	▼ -7	▼ -7
Alumina	▼ -1	▼ -7	▼ -8	▲ 1	▼ -3	▼ -3
Nickel	▲ 3	▲ 2	▲ 5	▲ 5	▼ -7	▼ -2
Aluminium	→ 0	▼ -19	▼ -19	→ 0	▼ -8	▼ -7
Zinc	▲ 13	▼ -14	▼ -3	▲ 4	▼ -8	▼ -4

Notes: f forecast. EUV is export unit value.
Source: ABS (2023) International Trade in Goods and Services, 5368.0; Department of Industry, Science and Resources (2023)

Table 1.1: Outlook for Australia's resources and energy exports in nominal and real terms

Exports (A$m)	2021–22	2022–23 [f]	2023–24[f]	2024–25[f]	2025–26[f]	2026–27[f]	2027–28[f]	CAGR[g] %
Resources and energy	421,618	464,267	395,320	346,369	328,767	337,715	335,865	-3.7
– real[b]	452,036	464,267	378,017	321,022	296,738	297,380	288,537	-7.2
Energy	204,056	238,265	185,473	157,047	139,017	136,865	129,787	-7.3
– real[b]	218,777	238,265	177,355	145,554	125,473	120,519	111,498	-10.6
Resources	217,563	226,002	209,847	189,322	189,750	200,850	206,078	-0.9
– real[b]	233,259	226,002	200,662	175,468	171,265	176,861	177,039	-4.5

Notes: **b** In 2022–23 Australian dollars; **f** forecast; **g** growth rate on 2022-23 levels.
Source: ABS (2023) International Trade in Goods and Services, 5368.0; Department of Industry, Science and Resources (2023)

Table 1.2: Australia's resource and energy exports, selected commodities

	Prices				Export volumes				Real export values, A$b, 2022–23 prices		
	Unit	2021–22	2022–23[f]	2027–28[f]	Unit	2021–22	2022–23[f]	2027–28[f]	2021–22	2022–23[f]	2027–28[f]
Iron ore	US$/t	119	97	69	Mt	874	887	989	142	121	74
LNG	A$/GJ	16	21	13	Mt	83	82	80	76	91	45
Metallurgical coal	US$/t	387	296	185	Mt	163	164	172	72	63	30
Thermal coal	US$/t	245	313	103	Mt	196	182	195	50	65	19
Gold	US$/oz	1,832	1,798	1,713	t	248	269	323	25	25	20
Crude oil	US$/bbl	91	89	75	kb/d	290	274	299	15	13	10
Copper	US$/t	9,645	8,406	9,954	kt	808	873	970	13	13	15
Alumina	US$/t	381	345	350	Mt	17,739	17,571	18,381	9.6	8.8	8.1
Aluminium	US$/t	2,891	2,388	2,391	kt	1,368	1,369	1,404	6.1	4.9	3.8
Lithium	US$/t	1,488	4,104	2,700	kt	2,248	3,080	4,462	5.3	19	19
Zinc	US$/t	3,506	3,124	2,841	kt	1,220	1,378	1,546	4.8	4.7	3.8
Nickel	US$/t	23,594	24,414	21,313	kt	159	164	215	4.7	5.0	4.2
Uranium	US$/lb	45	51	67	t	4,933	5,697	7,915	0.6	0.8	1.2

Notes: **a** Export data covers both crude oil and condensate; **f** forecast. **Price information:** Iron ore fob (free-on-board) at 62 per cent iron content estimated netback from Western Australia to Qingdao China; Metallurgical coal premium hard coking coal fob East Coast Australia; Thermal coal fob Newcastle 6000 kc (calorific content); LNG fob Australia's export unit values; Gold LBMA PM; Alumina fob Australia; Copper LME cash; Crude oil Brent; Aluminum LME cash; Zinc LME cash; Nickel LME cash; Lithium spodumene ore.
Source: ABS (2023) International Trade in Goods and Services, Australia, Cat. No. 5368.0; LME; London Bullion Market Association; The Ux Consulting Company; US Department of Energy; Metal Bulletin; Japan Ministry of Economy, Trade and Industry; Department of Industry, Science and Resources (2023)

Macroeconomic Outlook

Global GDP and economic change in 2022

Country	China	US	EU	India	ASEAN	Japan	S Korea	Taiwan	**Australia**
Per cent share of global GDP (PPP)	**19**	**16**	**15**	**7**	**6**	**4**	**2**	**1**	**1**
Yearly change	▲ 3.0%	▲ 2.0%	▲ 3.2%	▲ 6.8%	▲ 5.3%	▲ 1.4%	▲ 2.6%	▲ 3.3%	**▲ 3.6%**
Share of Australia's two-way trade	30%	6%	9%	4%	10%	12%	7%	4%	–

Global overview

- In 2022, global economic activity **increased by 3.4%.**
- Growth is expected to slow to **2.9% in 2023** and **3.1% in 2024.**

Global risks

The world macroeconomic environment improved slightly in early 2023.

- **Inflation rates look to have peaked** in key markets, and **energy shortages and COVID-related disruptions have eased**.
- **Tighter fiscal and monetary conditions** in most major economies — aimed at curbing still-high inflation rates — are **expected to slow global economic growth** over 2023 and early 2024.

SOURCE: IMF; ABS; OCE

2.1 Summary

- The world macroeconomic environment improved slightly in early 2023, as inflation rates look to have peaked in key markets, and as energy shortages and COVID-related disruptions eased.
- However, tighter fiscal and monetary conditions in most major economies — aimed at curbing still-high inflation rates — are expected to slow global economic growth over 2023 and early 2024. The potential for spreading instability in global financial markets following recent volatility in the US and European banking sectors poses a downside risk to the global outlook.
- In January 2023, the IMF forecast the world economy to grow by 2.9% in 2023 and 3.1% in 2024, down from 3.4% in 2022. The 2023 forecast represented an upward revision of 0.2 percentage points from the previous forecast (published in October 2022).

2.2 World economic outlook

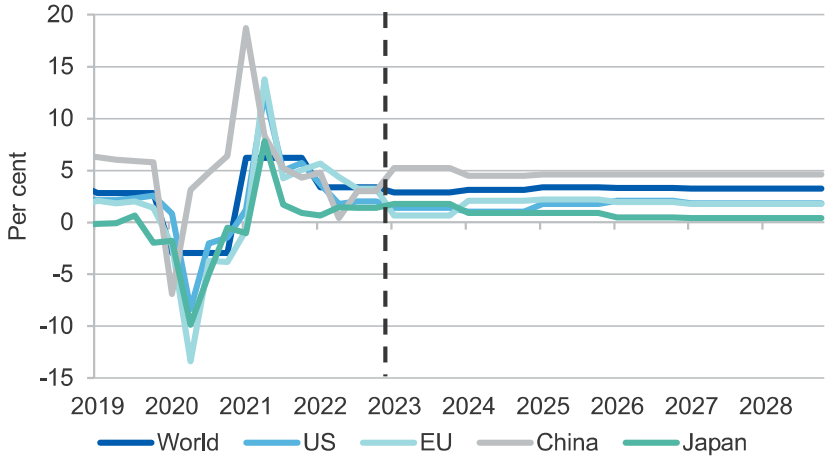
Tighter fiscal and monetary conditions weighing on global growth.

The International Monetary Fund (IMF) forecasts the world economy to grow by 2.9% in 2023, rising to 3.1% in 2024 after growth of 3.4% in 2022 (Figure 2.1). This represents an upward revision of 0.2 percentage points in 2023, and a downward revision of 0.1 percentage points in 2024 from the October 2022 World Economic Outlook.

A substantial divergence between the performance of advanced and emerging economies is expected by the IMF over the next two years. After recording growth below the global average last year — for the first time in more than 40 years — China's economy is expected to exceed 5% growth this year. However, the US and European economies are expected to slow in 2023.

While the global economic uncertainty triggered by the fallout from Russia's invasion of Ukraine is set to continue into 2023, a number of downside risks to the global outlook have moderated in recent months. Headline inflation appears to have peaked in several countries, China has removed many COVID-19 restrictions, and energy prices have fallen sharply.

Figure 2.1: GDP growth forecasts



Source: IMF (2023)

Global price pressures are expected to fall further in the coming months, as supply chain pressures ease and shipping costs fall as global consumer demand continues to weaken.

Weaker consumer demand in the US and Europe will also weigh on growth of manufacturing exporters — including China, Japan and Korea.

Labour markets remain resilient, with near full employment conditions persisting in many major advanced and emerging economies. Labour market tightness has been reflected in decade-high wage growth across advanced economies. However, job vacancy-to-unemployment ratios have moderated across several advanced economies in recent months, pointing to a modest easing in labour demand across economies.

Over the 5-year outlook, growth rates for the global economy are expected to return to around the long-run average of 3.2–3.3% a year. Faster growth in emerging economies is expected to support global growth rates. However, population ageing in China is expected to weigh on growth in

coming years, with growth in China's economy of around 4.5% projected by the IMF over the outlook to 2027–28 (Figure 2.1). Advanced economies are projected to return to their lower pre-pandemic growth trajectories, reflecting their demographic profiles and economic maturity.

In the latter half of the 5-year outlook period, world economic growth should receive a boost from investment in the global energy transition, as governments and businesses focus on 2030 emissions targets.

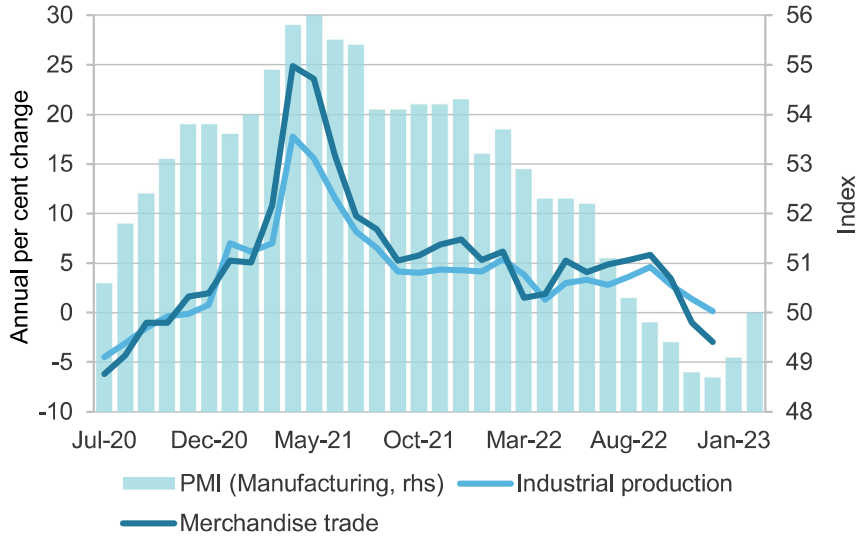
Despite the moderation in some downside risks in recent months the global outlook remains highly uncertain. The IMF notes that key risks include the potential for China's recovery to stall if low population COVID-immunity and limited hospital capacity results in widespread adverse health consequences. China's vulnerable real estate market remains a risk to its financial stability. Another source of global economic vulnerability stems from the risk of the war in Ukraine escalating, and the potential for further geopolitical fragmentation. Tighter monetary policy remains a risk if inflation pressures, particularly in services, prove more persistent than expected. Finally, the potential for spreading instability in global financial markets following recent volatility in the US and European banking sectors poses a downside risk to the global outlook.

Global industrial production and trade weaken as orders drop

Global industrial production and trade growth dipped in the December quarter 2022, due in part to COVID-related shutdowns in China. Global trade recorded negative year-on-year growth in the final two months of 2022, the first falls since 2020. Weaker demand for goods in advanced economies, especially electronic equipment, has seen exports from China, South Korea and other east Asian economies fall in recent months. However, growth in world industrial output remained positive, albeit very weak (Figure 2.2).

Forward indicators of manufacturing activity indicate a recovery in 2023. The JP Morgan global manufacturing Purchasing Managers Index (PMI) slipped into negative territory (signalling contraction) in the final quarter of last year driven by falls in the US, Eurozone, China and Japan. However, the outlook strengthened in February 2023, as the Chinese economy recovered. Results for individual countries are discussed below.

Figure 2.2: World industrial production, trade and PMI



Notes: PMI data is to February 2023; IP and trade data only available to December 2022.
Source: IHS Markit (2023); CPB Netherlands Bureau for Economic Policy Analysis (2023)

Global supply chain pressures normalising

Global supply chain pressures continue to moderate. The Global Supply Chain Pressure Index — a composite measure of cross-border transportation costs, delivery times, and order backlogs — continued the sharp falls over the past year, falling to below the historical average in February 2023 (Figure 2.3). The fall in the index was broad-based, with the largest negative contribution from European Area delivery times.

Global freight costs continue to decline, with the average price for a 40-foot shipping container (Drewry's composite World Container Index) falling to US$1,800 in March 2023. Freight costs are down more than four-fifths from the peaks of over US$10,000 in late 2021, but remain around 25% higher than average 2019 (pre-pandemic) rates.

Figure 2.3: Global supply chain pressure index

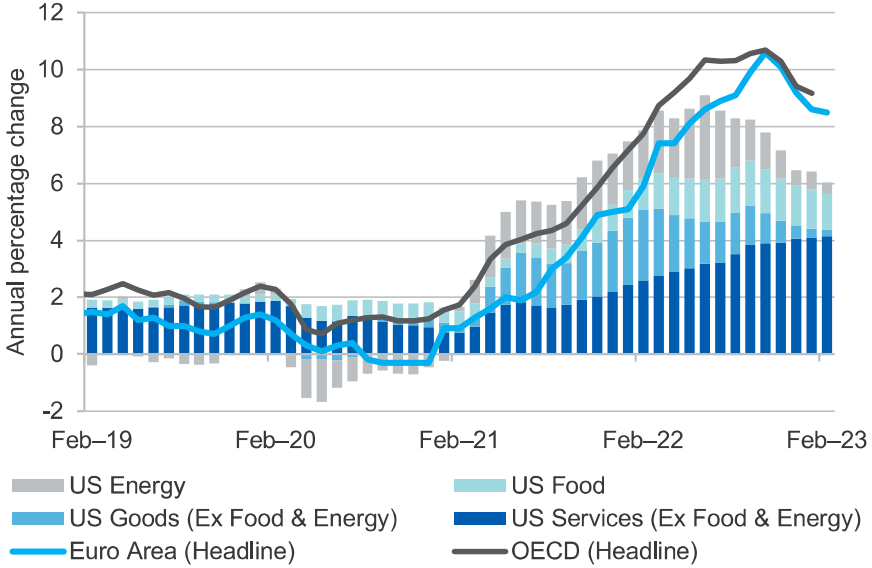
Source: Bloomberg (2023); New York Federal Reserve (2023)

As goods/energy prices ease, the focus shifts to services inflation

Headline inflation has been falling in major economies, due to reductions in energy prices and the easing of lingering supply-demand imbalances and supply chain bottlenecks. In January 2023, the IMF forecast global inflation to fall from 8.8% last year to 6.6% in 2023 and 4.3% in 2024. However, inflation would remain above pre-pandemic levels, which were around 3.5%. As inflation rates continue to be well above central bank targets in most economies, reining in inflation continues to be the primary concern for policymakers in most economies.

US CPI, for example, has fallen for eight consecutive months since the peak in June 2022. US core inflation — which excludes food and energy — has also begun to ease, driven by falling goods inflation. Eurozone inflation, while still high, has also peaked, with sharp monthly reductions in recent months driven by falling energy prices (Figure 2.4). In contrast to easing goods inflation, services inflation — particularly housing and consumer services — has increased in the US, and will be a key focus for American policymakers over the year.

Figure 2.4: Consumer Price Indices — US, Europe and OECD



Source: Bloomberg (2023); Board of Governors of the Federal Reserve System (2023); U.S. Bureau of Economic Analysis (2023); OECD (2023)

Monetary policy tightening by central banks continues, although some have slowed the pace of tightening. The US Federal Reserve lifted rates by 25 basis points at its February and March meetings, following a 50 basis points increase in December and four consecutive 75 basis point increases during 2022.

The European Central Bank (ECB) raised its key policy rate by 50 basis points in February and again in March. In announcing the March rate increase, which was announced days after a plunge in the value of Credit Suisse, the ECB stated that it was monitoring current market tensions closely and indicated that it was ready to respond if required to preserve financial stability in the euro area.

Market pricing is consistent with expectations that policy rates will peak around mid-2023 and then decline later in the year.

2.3 Major trading partners' economic outlook

The outlook for Australia's major trading partners remains weak, with their GDP growth in 2023 forecast by the RBA to be around 3.5%, well below its pre-pandemic decade average.[1] Slower growth in Australia's major trading partners will reduce demand for Australia's exports. However, the expected recovery in China's economy and ongoing development in India will support resource and energy export earnings over the outlook period. Macroeconomic developments for selected economies are provide below.

Chinese GDP expected to rebound in 2023 as economy reopens

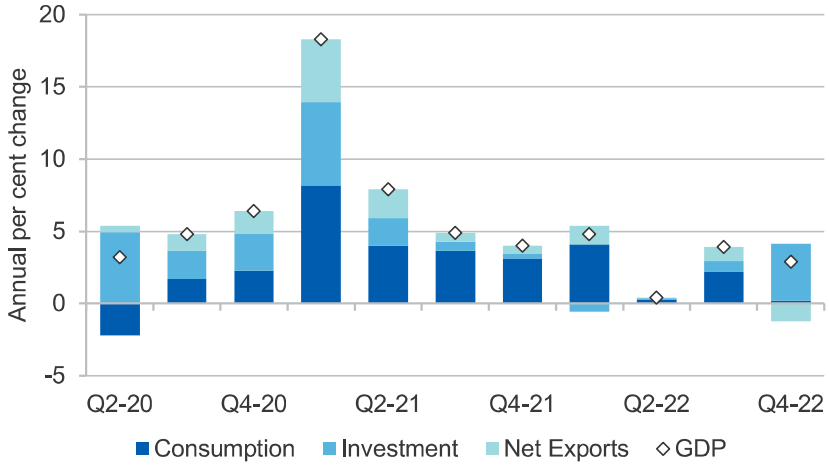
China's economy grew by 2.9% year-on-year in the December quarter 2022 (Figure 2.5). Aside from the lockdown-affected June quarter 2022, this was the slowest year-on-year growth since the 2020 pandemic recession. The December quarter result reflected weak exports and consumption (both government and household), which weighed on the substantial contribution from manufacturing and infrastructure investment. The weak result partly reflected the impact of COVID-19 restrictions in November, and disruptions due to surging COVID-19 cases in December.

Weakness in residential investment, sales and prices continues to weigh on economic activity. In the year to December 2022, the value of sales of residential buildings fell by over 25%, while new house prices fell (year-on-year) for the 9th consecutive month in January. In volume terms (measured in square metres of floor space), newly started residential property fell 40% in 2022, and residential building sales were down 27%.

Chinese authorities have continued efforts to support growth in the property sector, by building on the substantial fiscal and monetary policy backing provided in 2022 — particularly through additional infrastructure spending. In February, the People's Bank of China (PBC) injected around 500 billion yuan into one-year medium-term lending facility (MLF) loans to support banking system liquidity. The stimulus follows multiple cuts during 2022 to key policy rates.

The Government announced a growth target of around 5% for 2023 in the government work report released at the opening of the National People's Congress in March. Following the Congress, the PBC again reduced the bank reserve requirement ratio — the amount of funds banks have to hold in reserve — following a similar cut in December. The PBC stated the March cut was aimed at maintaining liquidity and ensuring the money supply increases in line with nominal economic growth. The government also eased restrictions on developers' access to finance, and financial institutions were encouraged to boost lending for infrastructure projects (see December 2022 *Resources and Energy Quarterly*).

Figure 2.5: China contributions to quarterly real GDP



Notes: Consumption is made up of both household and government sectors.
Source: Bloomberg (2023); National Bureau of Statistics of China (2023)

China's industrial production was relatively weak in December, up 1.3% year-on-year. This was the weakest result since the April-May shutdowns, with rising COVID infections and containment measures a key worry for Chinese companies. China's Caixin General Manufacturing PMI indicated that manufacturing returned to growth in February, recording the first

[1] *RBA Statement on Monetary Policy* — February 2023.

improvement in business conditions in 7 months. The February PMI result was the highest reading in more than a decade, with businesses reporting a strong rebound in both production and new orders driven by rising customer demand.

The return to more normal business operations in early 2023, and hopes that the economy and new business will rebound, helped lift business confidence. Among manufacturers surveyed, optimism was the highest recorded since early 2021.

Passenger vehicle production weakened in the final months of 2022, down 16% year-on-year in December. Vehicle sales were also down, although the decline was less marked than in production.

The IMF forecasts Chinese GDP growth of 5.2% in 2023 — reflecting improving mobility — and 4.5% in 2024. China is expected to grow at around 4.5% a year over the 5-year outlook period. However, the IMF warns that declining business dynamics and slow progress on structural reforms could slow Chinese growth over the medium term.

Demographic change will increasingly weigh on China's economic growth. In January, China's National Bureau of Statistics released data showing China's population fell in 2022, the first annual fall since the Great Leap Forward in 1961. Population aging and a shrinking workforce has seen China's old-age dependency ratio — total elderly population relative to the working-age population — rose from 10% in 2000 to 19% in 2021. Over the outlook period, China is expected to continue to look to shift toward quality- rather than quantity-oriented consumption-led growth.

Bank of Japan maintains accommodative stance as inflation rises

Japan's GDP increased by 0.4% year-on-year in the December quarter 2022, down from 1.5% in the September quarter. Net trade contributed to growth, with exports increasing and imports declining for the first time since 2021.

Slowing growth in its major trading partners and higher inflation, hold downside risks for Japan's economy. Japan's core inflation — which excludes fresh food but includes fuel costs — was 4% in December 2022, exceeding the Bank of Japan (BoJ) inflation target of 2% for the ninth month in a row.

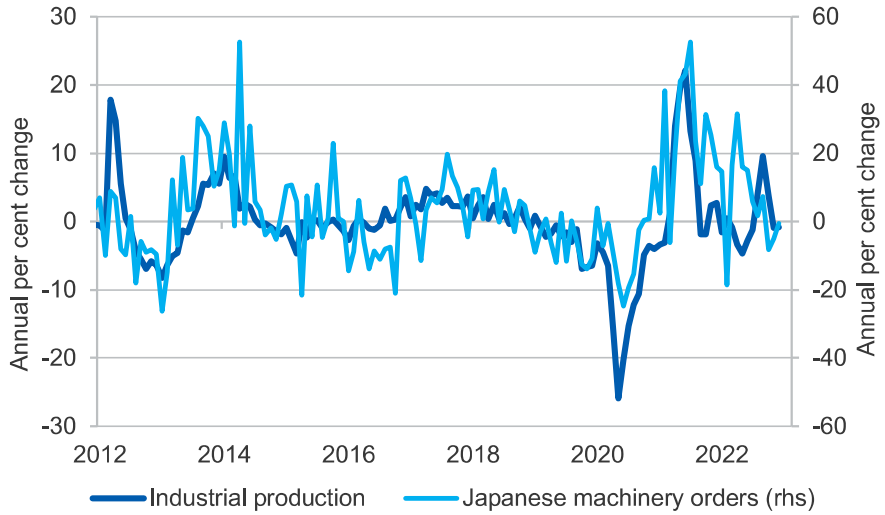
Inflationary pressures are being driven by higher raw material costs, particularly for imported materials — in the context of a weak yen which lost substantial value over the course of last year. The BoJ has maintained its accommodative monetary policy, and continues to hold the 10-year Japanese Government bond yield unchanged at -0.1%. In December, the BoJ announced that it would increase its regular monthly purchases of Japanese Government bonds while allowing yields on 10-year bonds to trade in a wider band to improve bond market functioning.

Japanese industrial production growth has been volatile, due to the base effects from COVID-related disruptions in 2021. In December, industrial output declined slightly in year-on-year terms, consistent with the post-pandemic trend — which has seen zero growth over the past two years. In addition, machinery orders, which have experienced similar levels of volatility, also fell for the third consecutive month in December (Figure 2.6).

Manufacturing conditions continued to weaken in early 2023. The Jibun Bank Japanese Manufacturing PMI remained in negative (contractionary) territory in January for the 3rd month in a row. The index has been falling steadily over the past year. Contributing to the weakness was subdued international demand for Japanese manufactures, with falling sales to customers across Asia — although this was mitigated to some extent by increased demand for Japanese goods from Europe.

Looking ahead, the IMF forecasts Japan's economic growth to rise to 1.8% in 2023, on the back of continued monetary and fiscal policy support. Business investment is expected to be supported by high corporate profits from the weaker yen (and hence higher prices received for exports) as well as delays in implementing some previous projects. However, as the effects of past stimulus fade, growth is expected to slow in 2024. In the latter half of the outlook period, growth is expected to settle below 0.5%, as Japan's demographic trends of an ageing and declining population and shrinking workforce continue to slow GDP growth.

Figure 2.6: Japan industrial production and machinery orders



Source: Bloomberg (2023)

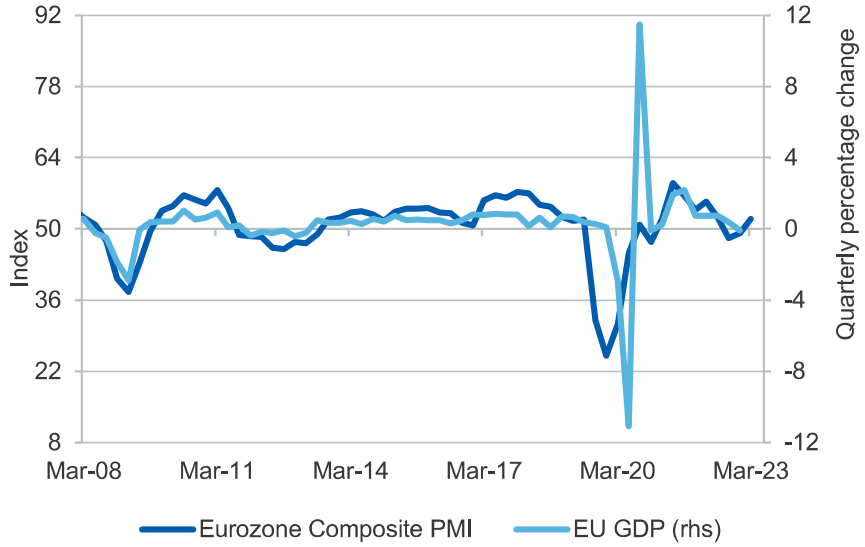
Eurozone economies face slower growth

Following surprisingly robust Eurozone GDP growth in the first few quarters of 2022, growth fell to zero in the December quarter 2022 (quarter-on-quarter) to leave it 1.8% higher year-on-year (Figure 2.7). Among the larger economies, Germany grew by 0.9%, France by 0.5% and Italy by 1.4%.

Despite the moderation in energy prices in recent months, European manufacturers — in particular energy-intensive metal smelting, refining and fabrication operations — remain very exposed to high energy prices. Industrial production in the Eurozone fell by 1.7% year-on-year in December 2022, down from 2.8% growth in November. While a drop in production was anticipated, the decline was larger than market expectations.

Leading indicators have improved in recent months. In February, the Eurozone Composite PMI Index increased to 52.0, the strongest result since May 2022. The improvement reflected an acceleration in service sector growth and improved supply chains. New orders increased, while input costs increased at a slower pace. Business confidence was the highest it has been since before the Russian invasion of Ukraine, as concerns about a potentially deep recession, spiralling energy prices and rising inflation, eased in the new year.

Figure 2.7: Eurozone GDP and Composite PMI (quarterly)



Notes: PMI for March quarter 2023 is average of January and February results.
Source: Bloomberg (2023)

In February 2023, the Eurozone manufacturing PMI fell to 48.5, the 8th consecutive 'contractionary' result. However, manufacturing output rose for the first time since May 2022. The pickup reflected improved supply chains, with delivery times shortening for the first time in 2 years. Optimism among manufacturers about the year-ahead outlook also lifted, with future output expectations at their most upbeat since Russia's invasion of Ukraine.

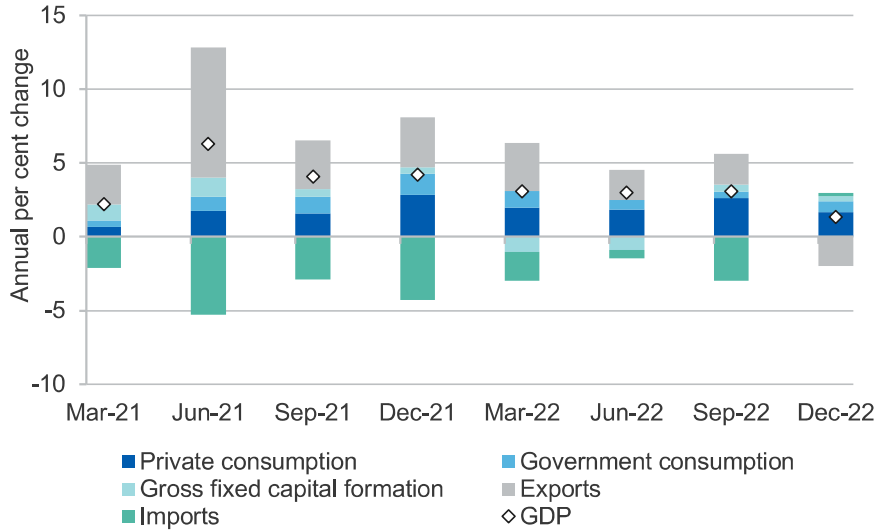
As noted above, the European Central Bank (ECB) raised its key policy rate by 50 basis points in February and again in March.

In January, the IMF lifted its forecast of European growth in 2023 by 0.2 percentage points to 0.7%. This reflected lower wholesale energy prices and additional announcements of fiscal purchasing power support — in the form of energy price controls and cash transfers. Growth in 2024 is expected to pickup to an estimated 1.6%. Over the remainder of the outlook to 2028, economic growth is projected to trend toward a longer-run annual level of about 1.7%.

South Korea's exports fall as global semiconductor demand plunges

South Korea's GDP increased by 1.3% year-on-year in the December quarter 2022. A sharp fall in exports — which have been the largest contributor to Korea's GDP growth over the past two years — weighed heavily on growth (Figure 2.8). The fall in exports also reflected base effects, due to the surge in real exports in the December quarter 2021.

Figure 2.8: South Korea contributions to quarterly real GDP



Source: Bloomberg (2023)

South Korea's industrial production fell sharply in the final months of 2022, down over 7% year-on-year in December 2022. Exports of computer chips declined by over 40% year-on-year in February, due to slowing demand and falling prices. South Korea's manufacturing PMI improved slightly in January, but remained in contraction territory for the 7th consecutive month. The negative January result was due to large falls in output and new orders, due to weak demand in domestic and foreign markets.

South Korean inflation increased slightly to 5.2% year-on-year in January, defying the general downward trend since inflation peaked at 6.3% in July 2023. The Bank of Korea raised its benchmark interest rate by an additional 25 basis points to 3.5% in January, for a cumulative gain of 3 percentage points since August 2021.

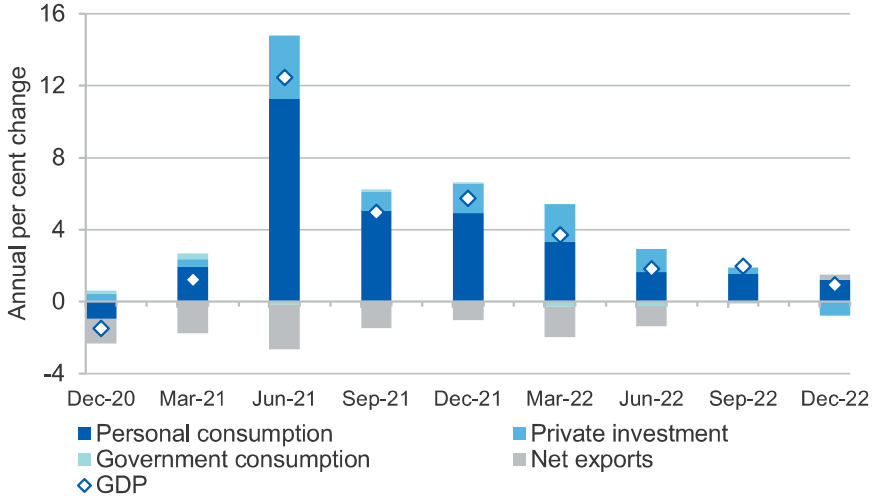
In January, the IMF lowered its forecast of South Korean economic growth to 1.7% in 2023 (down from 2.6% in 2022), a downward revision of 0.3 percentage points. Growth is expected to return to 2.6% in 2024, decreasing to 2.3% a year by 2028.

US labour market resilience continues

In year-on-year terms, the US economy grew by 0.9% in the December quarter 2022. This growth was primarily driven by personal consumption, as private investment made its first negative contribution to GDP in over two years. Faster growth in US exports, combined with slower growth in imports, meant that net exports contributed to overall GDP growth (year-on-year) for the first time since the onset of the pandemic (Figure 2.9).

US labour market resilience continues, with nonfarm payroll employment rising by 311,000 in February 2023. While the unemployment rate rose slightly in February, at 3.6% it remains close to the 53-year low achieved in January. The resilient labour market continues to support spending. However, US personal consumption spending — the main driver of GDP growth since mid-2021 — fell in the final months of 2023. Total inflation-adjusted spending on goods and services fell month-on-month in November and December 2022. Spending recovered strongly in January 2023, rising by 1% in real terms. However, the latest rebound may be short lived, with retail sales falling in February (month-on-month) as sales of furniture, cars and clothing and spending in restaurants and bars fell.

Figure 2.9: US contributions to quarterly real GDP



Source: Bloomberg (2023)

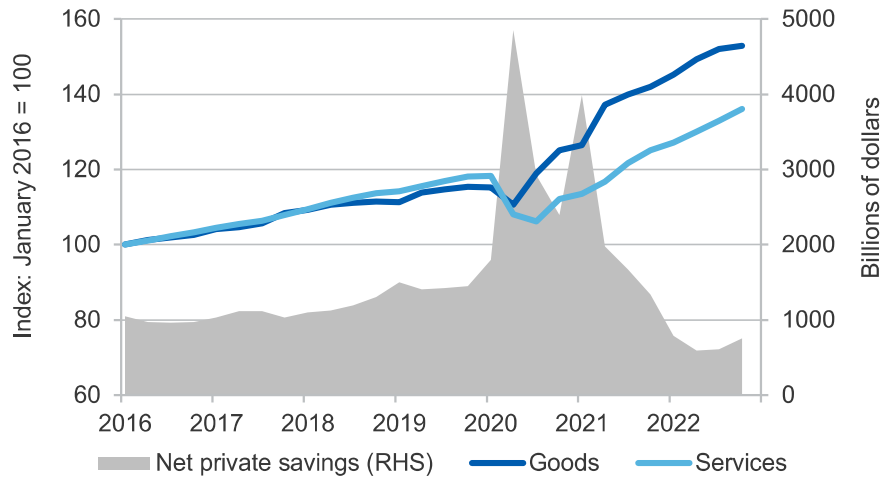
US housing demand has weakened further, with home sales around 35% lower than at the start of 2022. Advertised rents have fallen in recent months, which should see the rapid inflation of rents evident over the past year begin to moderate later in the year.

The US net private saving rate has fallen from the record rates achieved during the pandemic (Figure 2.10). Despite a slight pickup in the savings rate in the December quarter 2022, US Bureau of Economic Analysis data indicates the current savings rate is the lowest since the declines seen during the global financial crisis in 2009. Credit card balances have been rising sharply over the past year, with total US credit card debt reaching record levels of almost US$1 trillion in February 2023.

US households, particularly those in the top half of the income distribution, are estimated to continue to hold a buffer of excess savings. Despite drawdowns in savings over the past year, this is likely to help them navigate higher prices and the tightening rate cycle.[2]

[2] The Federal Reserve, *Excess Savings during the COVID-19 Pandemic,* October 2022.

Figure 2.10: US personal consumption and net private savings



Notes: Personal Consumption Expenditures; seasonally adjusted data; January 2016 =100; Net Private Savings: seasonally adjusted annual rate (quarterly data).

Source: FRED Economic Data (2023)

US industrial production fell by 0.2% year-on-year in February, the first negative result since the recovery commenced in early 2021. The US Manufacturing PMI dropped sharply late last year, and remained weak in early in 2023. The deterioration in manufacturers' operating conditions reflects sharp falls in output and new orders, as domestic and external demand weakens.

As noted earlier, the US Federal Reserve continues to lift rates, with the 25 basis point increase in March lifting the target range to 4.75–5%. However, in announcing the March increase Chair Powell noted that the Fed had changed its language on rate increases, no longer stating in its guidance that it anticipated ongoing rate increases would be appropriate to quell inflation. Projections of the policy rate required to achieve the Fed's inflation target were revised up at the December 2022 meeting to a median of 5.1 per cent and remained stable in March 2022.

In January 2022, the IMF upgraded its forecast for US economic growth for 2023 by 0.4 percentage points to 1.4%, reflecting carry-over effects from domestic demand resilience in 2022. Growth in 2024 was revised down slightly, due to the steeper path of Federal Reserve rate increases, — which the IMF expects to peak at just over 5% in 2023.

Over the rest of the outlook period to 2028, annual US economic growth is projected to trend toward a lower, longer-run level of about 1.9%. Factors affecting growth over this period will include future revenue and spending measures — employed to address significant increases in public debt — rising healthcare costs and population ageing. The global energy transition will also reshape the post-pandemic economy. The latter will also be affected by a range of measures included in the 2022 *Inflation Reduction Act*, which will ramp up over the outlook period.

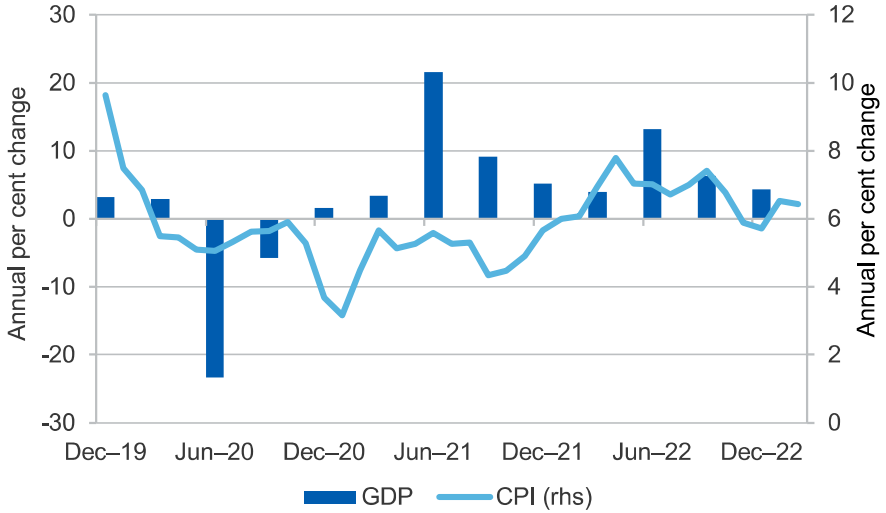
India's GDP slows as manufacturing weakens

India's GDP growth slowed to 4.4% year-on-year in the December quarter 2022, down from 6.3% in the September quarter (Figure 2.11). The growth was below market expectations (4.6%) and was supported by growth in agriculture and mining. Falls in manufacturing along with weaker private consumption demand weighed on growth.

Despite falling in January, India's PMI recorded its 19th month of expansion and remained above the long-run average — with production and domestic and foreign new orders continuing to rise. Price pressures faced by manufacturers were at a 3-month high, due to higher prices for energy, metals and electronics, but remained well below the long-run average.

India's retail price inflation remained above the Reserve Bank of India (RBI) target rate of 2–6% for the second consecutive month in February, reflecting higher food prices and housing costs while fuel prices remained elevated. The RBI raised interest rates in February, the sixth increase since May last year. The RBI is expected to continue with interest rate increases this year, dampening growth in domestic spending and investment.

Figure 2.11: India quarterly GDP and monthly CPI



Source: Bloomberg (2023)

The IMF forecasts India's economic growth to slow to 6.1% in 2023, down from 6.8% in 2022. Growth is then forecast to pick up to 6.8% in 2024, driven by resilient domestic demand despite external headwinds due to softer external demand (resulting from slower global growth). Further out, the IMF expects India's GDP growth will likely average just over 6.0% a year. This reflects a resumption of the healthy growth trajectory seen in the decade before the COVID-19 shock — where favourable demographics and rapid development helped push India's economy to among the fastest growing in the world.

Table 2.1: Key IMF GDP assumptions

	2022	2023[a]	2024[a]	2025[a]	2026[a]	2027[a]	2028[a]
Economic growth[b]							
Advanced economies	**2.7**	**1.2**	**1.4**	**1.9**	**1.9**	**1.7**	**1.7**
Australia	3.6	1.6	1.7	2.0	2.2	2.3	2.3
Eurozone	3.5	0.7	1.6	2.2	2.0	1.7	1.7
France	2.6	0.7	1.6	1.8	1.7	1.4	1.4
Germany	1.9	0.1	1.4	2.2	1.8	1.3	1.3
Japan	1.4	1.8	0.9	0.9	0.5	0.4	0.4
New Zealand	2.3	1.9	2.0	2.2	2.3	2.4	2.4
South Korea	2.6	1.7	2.6	2.6	2.5	2.3	2.3
United Kingdom	4.1	-0.6	0.9	2.3	2.2	1.5	1.5
United States	2.0	1.4	1.0	1.8	2.1	1.9	1.9
Russia	-2.2	0.3	2.1	1.0	0.8	0.7	0.7
Emerging economies	**3.9**	**4.0**	**4.2**	**4.3**	**4.3**	**4.3**	**4.3**
ASEAN-5[d]	5.2	4.3	4.7	5.2	5.1	5.0	5.0
China [e]	3.0	5.2	4.5	4.6	4.6	4.6	4.6
India	6.8	6.1	6.8	6.8	6.5	6.2	6.2
Latin America	3.9	1.8	2.1	2.5	2.5	2.4	2.4
Middle East	5.0	3.2	3.5	3.6	3.6	3.6	3.6
World [c]	**3.4**	**2.9**	**3.1**	**3.4**	**3.3**	**3.2**	**3.2**

Notes: a Assumption. Data for 2025–2027 are from October 2022 WEO database. Growth rates for 2028 are assumed equal to 2027 growth rates. b Year-on-year change. India projections are based on fiscal years, starting in April; **c** Calculated by the IMF using purchasing power parity (PPP) weights for nominal country gross domestic product. d Indonesia, Malaysia, Philippines, Thailand and Vietnam. e Excludes Hong Kong.
Sources: IMF (2022, 2023) World Economic Outlook; Bloomberg (2023).

Table 2.2: Exchange rate and inflation assumptions

	2022	2023[a]	2024[a]	2025[a]	2026[a]	2027[a]	2028[a]
AUD/USD exchange rate	0.69	0.71	0.75	0.75	0.75	0.75	0.75
Inflation rate[b]							
United States	8.0	3.5	2.2	2.0	2.0	2.0	2.0
	2021–22	**2022–23[a]**	**2023–24[a]**	**2024–25[a]**	**2025–26[a]**	**2026–27[a]**	**2027–28[a]**
Australia	7.2	4.6	3.2	2.7	2.5	2.5	2.5

Notes: a Assumption; **b** Average.

Sources: ABS (2023) Consumer Price Index, 6401.0; Bloomberg (2023); Department of Industry, Science and Resources; RBA (2023); IMF (2023).