



# CHDC ECONOMIC FUTURES FORUM

15 MARCH 2022

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# AGENDA

- Global economy
- National economy
- Central Highlands economy
- Financial markets

# Key themes for economy and interest rates

Supply-demand to normalize (slowly), inflation moderating but high, central banks in a complicated cycle

## Supply-demand:

- Demand higher: rundown of excess savings to satisfy pent-up demand; policy settings still loose despite tightening
- Demand lower: tighter policy settings; higher energy prices; past peak goods consumption
- Supply higher: consumption switching from goods to services; logistics adjusting; production belatedly lifting; labour supply increases as virus restrictions & government support ends

## Inflation:

- Demand-supply imbalances to see inflation stay stubbornly high initially
- Both to normalise such that inflation heads back towards central bank targets
- Unlikely to get there though and could end next year above-target

## Monetary policy:

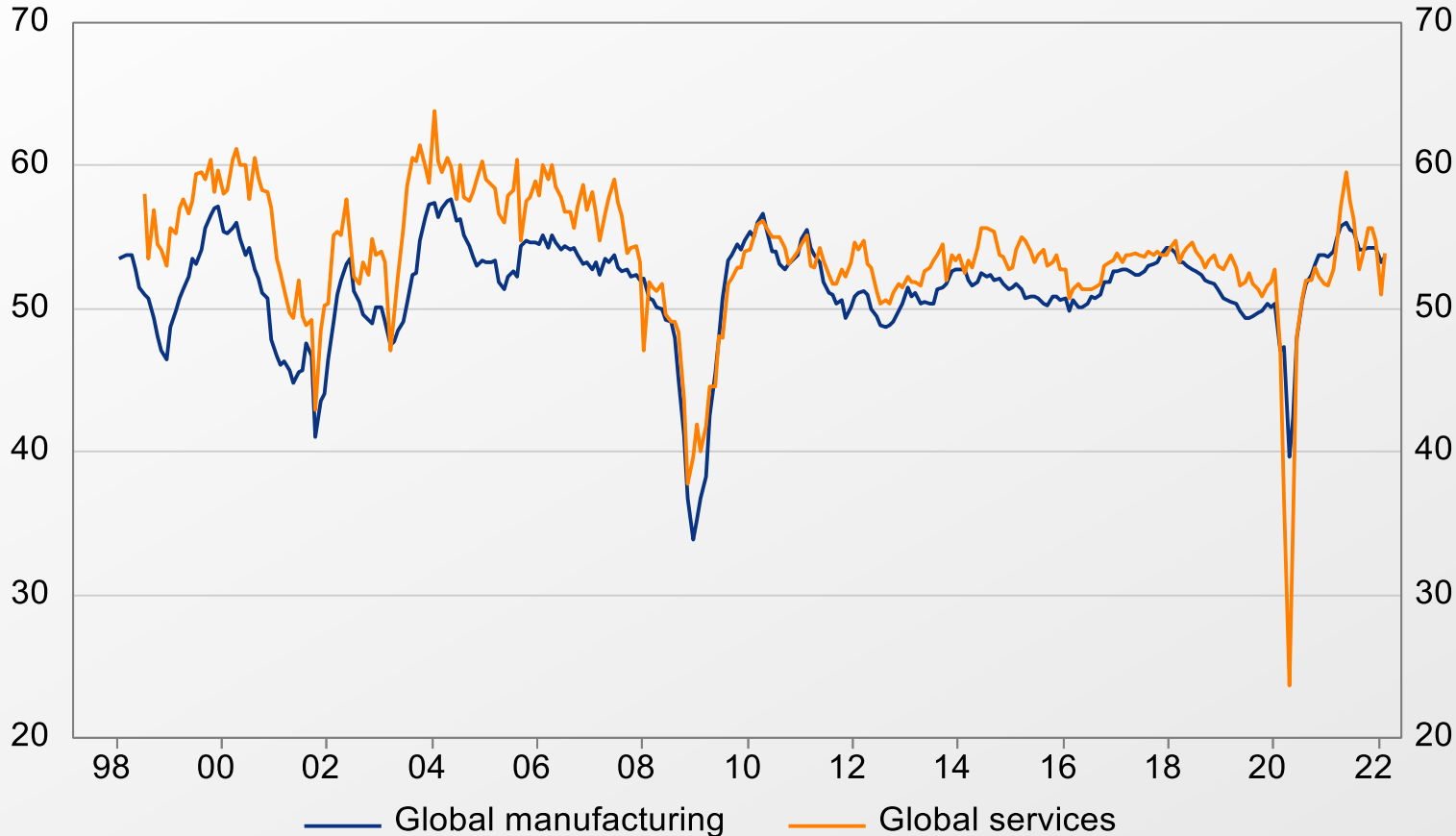
- Removing extraordinary policy support (phase 1)
- Get policy settings to neutral (phase 2)
- Tighten policy to contain medium-term inflation (phase 3)



# GLOBAL ECONOMY

# Global economic activity

JP Morgan global PMIs



*Global economic momentum faded in 2021:*

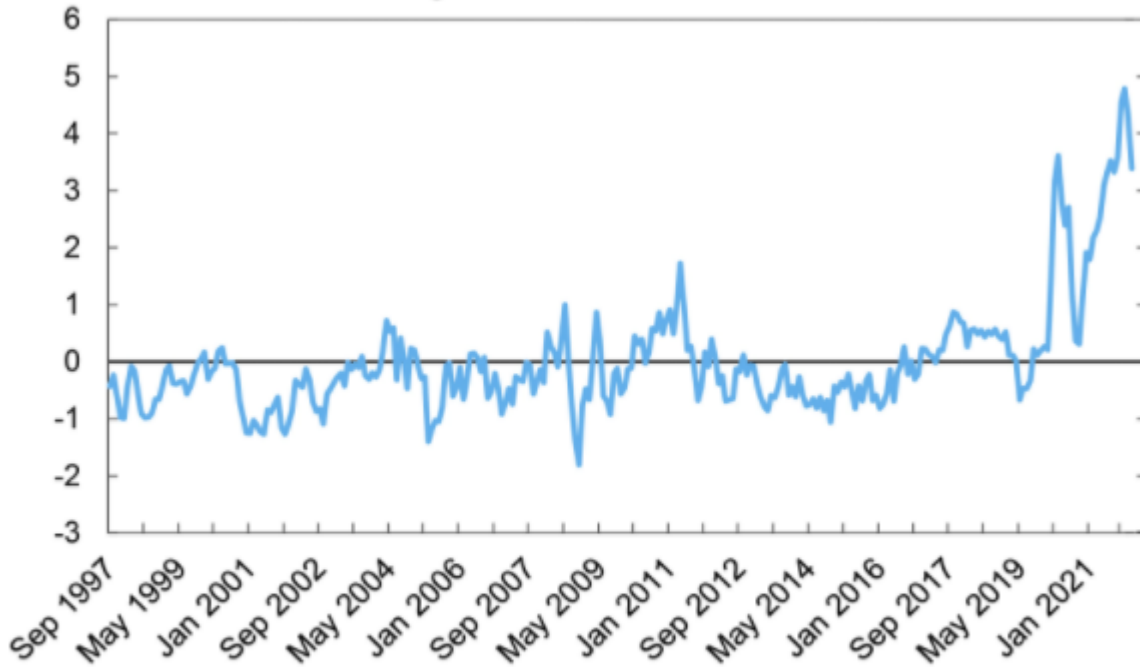
- COVID
- Supply chain disruptions
- Recovery had reached maximum velocity
- Tightening of fiscal & monetary policies
- Base effects

Source: Refinitiv Datastream, QTC

# Supply pressures

### Global Supply Chain Pressure Index

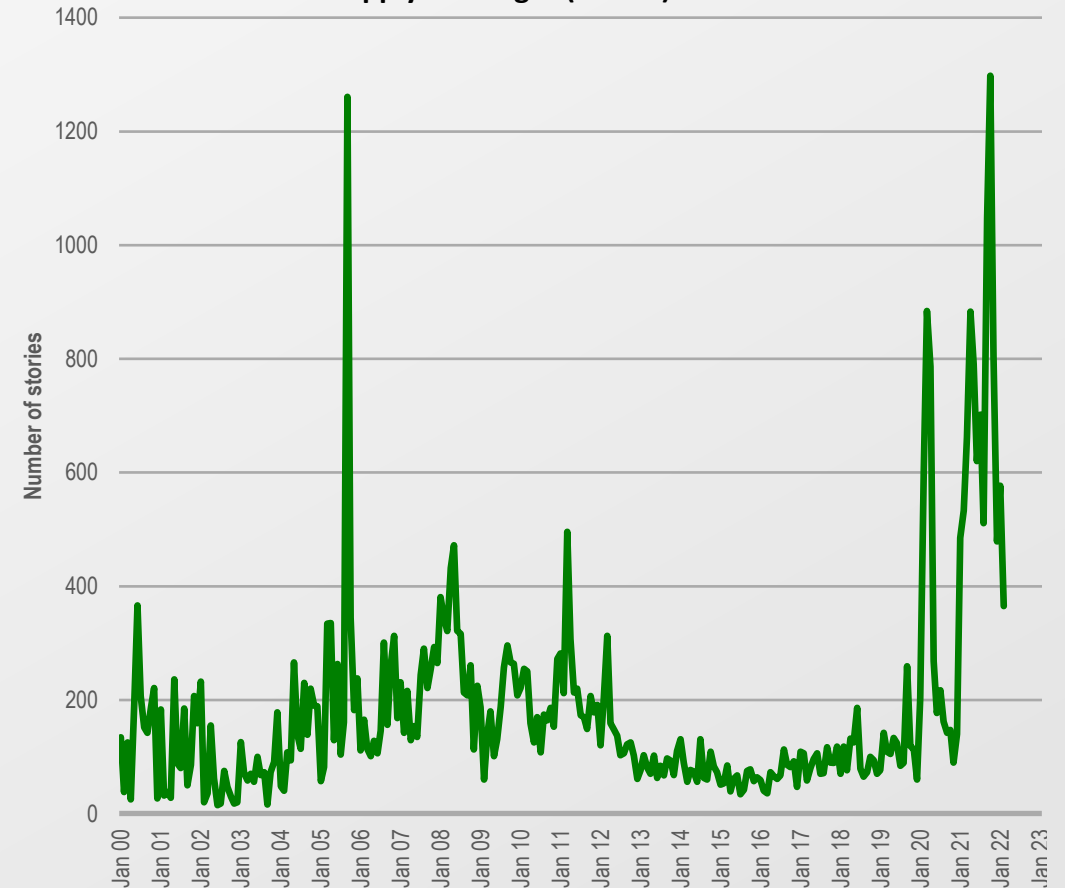
Standard deviations from average value



Sources: Bureau of Labor Statistics; Harper Petersen Holding GmbH; Baltic Exchange; IHS Markit; Institute for Supply Management; Haver Analytics; Bloomberg L.P.; authors' calculations.  
Note: Each index is scaled by its standard deviation.

*Supply chains globally are under unprecedented pressure...*

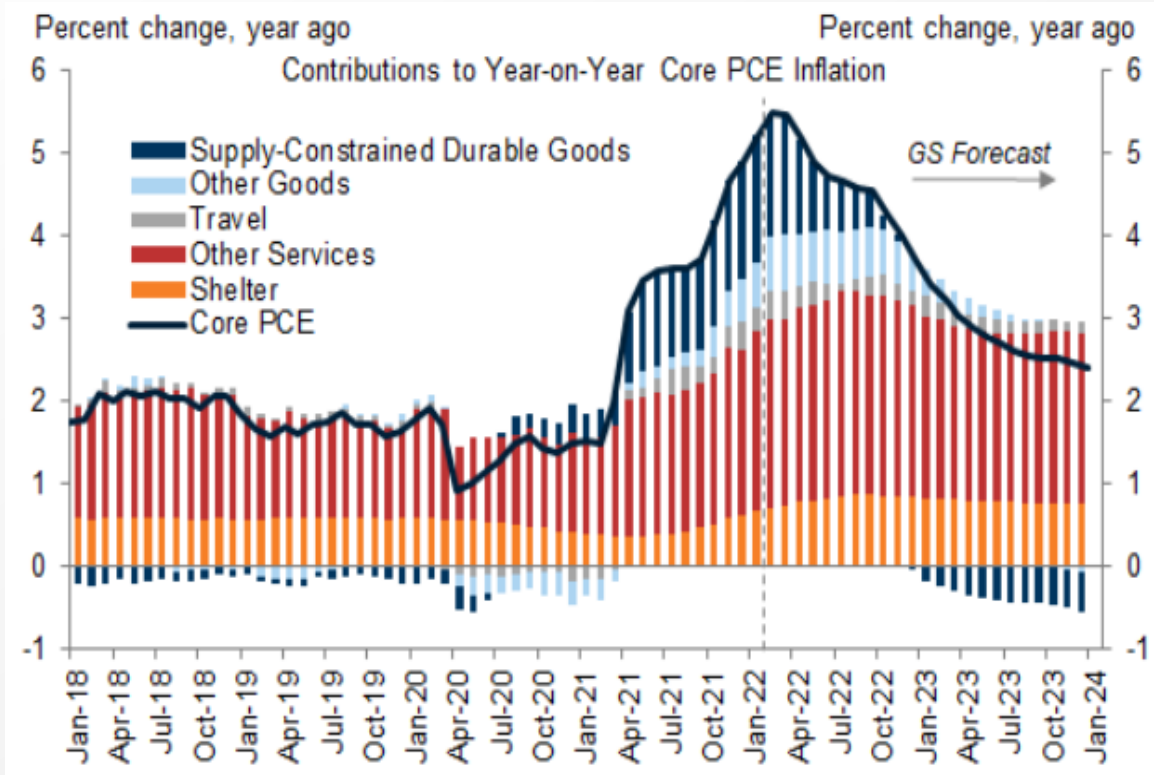
### Supply Shortages (Global)



*...but there are signs this could be fading*

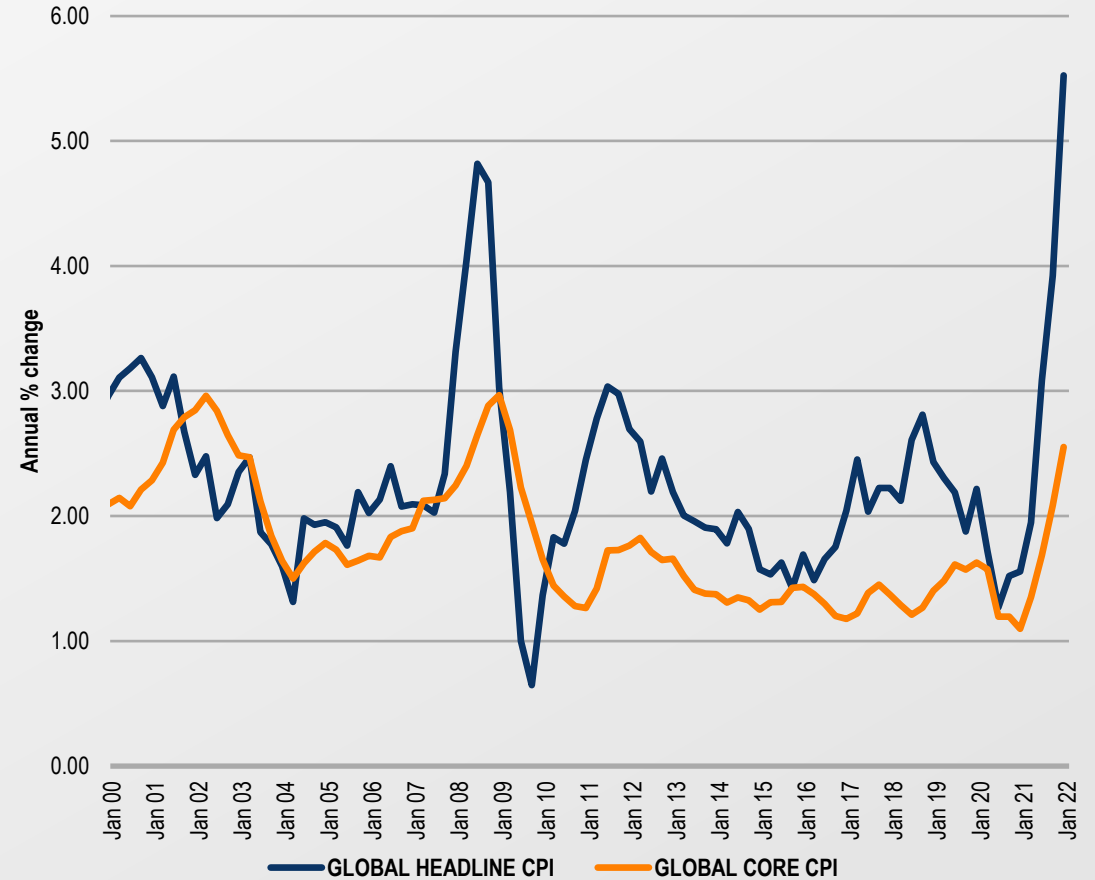
# Inflation

US inflation



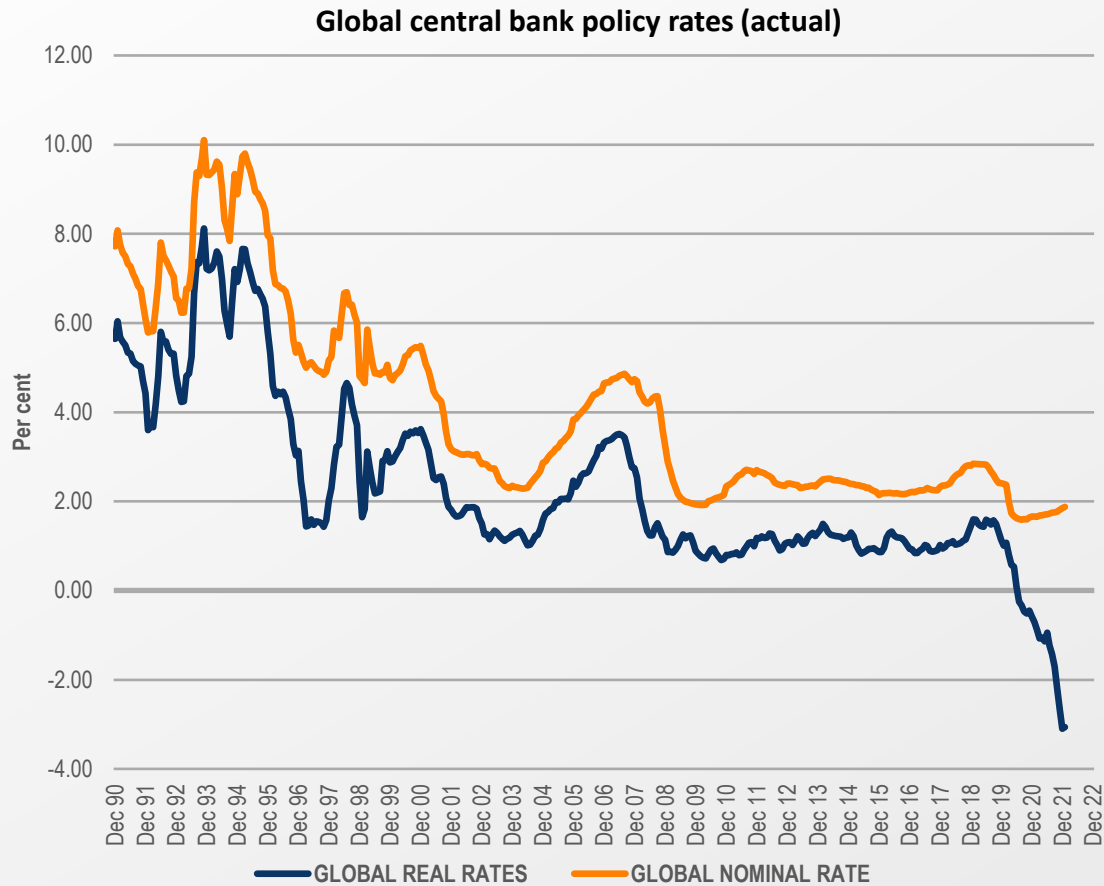
*Transitory factors to weigh on inflation for longer than previous thought...*

Global inflation



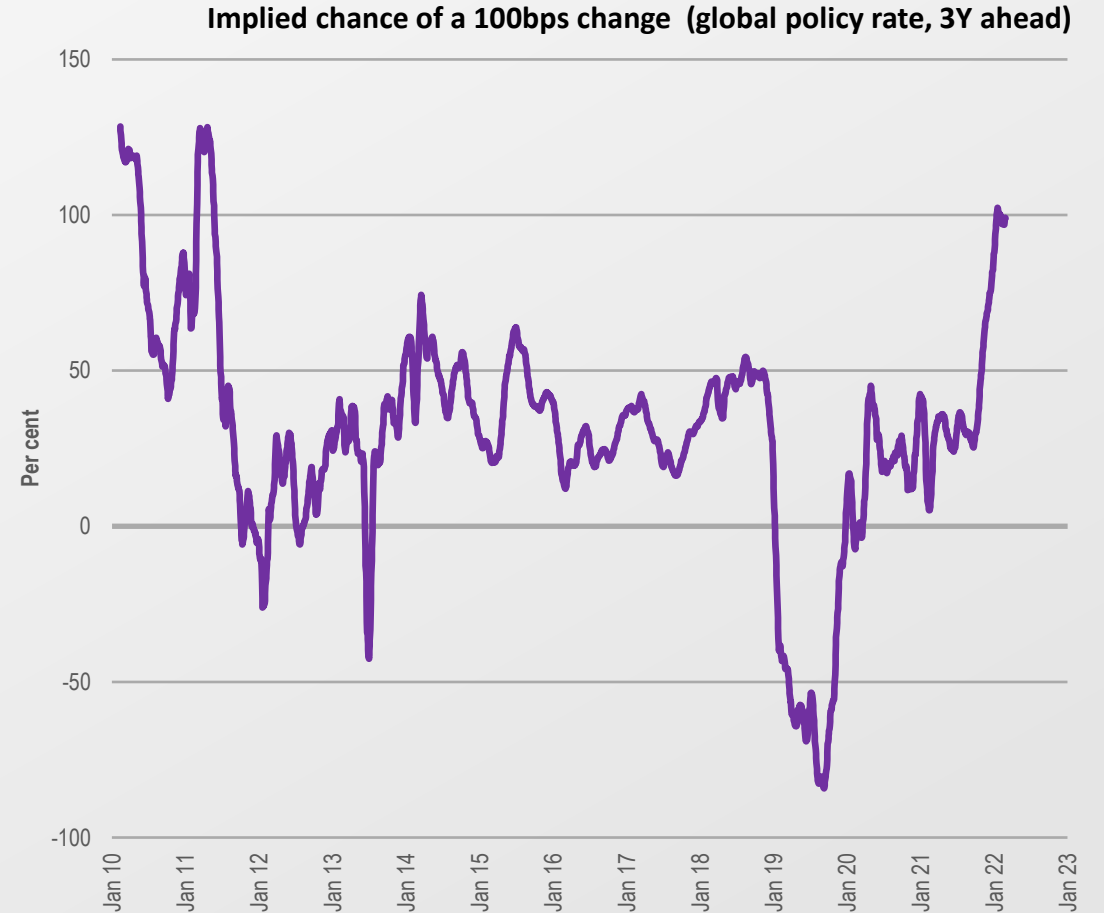
*...with these already having a big impact on global inflation*

# Monetary policy (global)



Source: QTC Economic Research, Bloomberg, Refinitiv

*Central banks have started raising rates...*



Source: QTC Economic Research, Bloomberg, Refinitiv

Note: Displays the probability implied by market pricing of a 100bps rate change

*...with more expected*

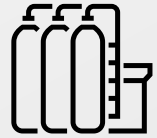


# Russia-Ukraine

*The invasion of Ukraine will see higher oil prices and global inflation*

## Energy

- 12% of global oil production
- 16% of global natural gas production



## Food/agriculture

- Russia and Ukraine account for 25% of global wheat production
- Ukraine accounts for 13% of global corn production
- Russia is the largest producer of ammonium nitrate, a critical component in fertiliser



## Impact on inflation (source: Deutsche BankB)

- In *'moderate scenario'* (gas & oil prices increase by 50% & 20% respectively)
  - EU inflation to increase 1 ppts & GDP growth slow 1.0 ppt
- In *'severe scenario'* (gas & oil prices increase by 100% & 50% respectively)
  - EU inflation to increase 2 ppts & GDP growth slow 2.5 to 3.0 ppt

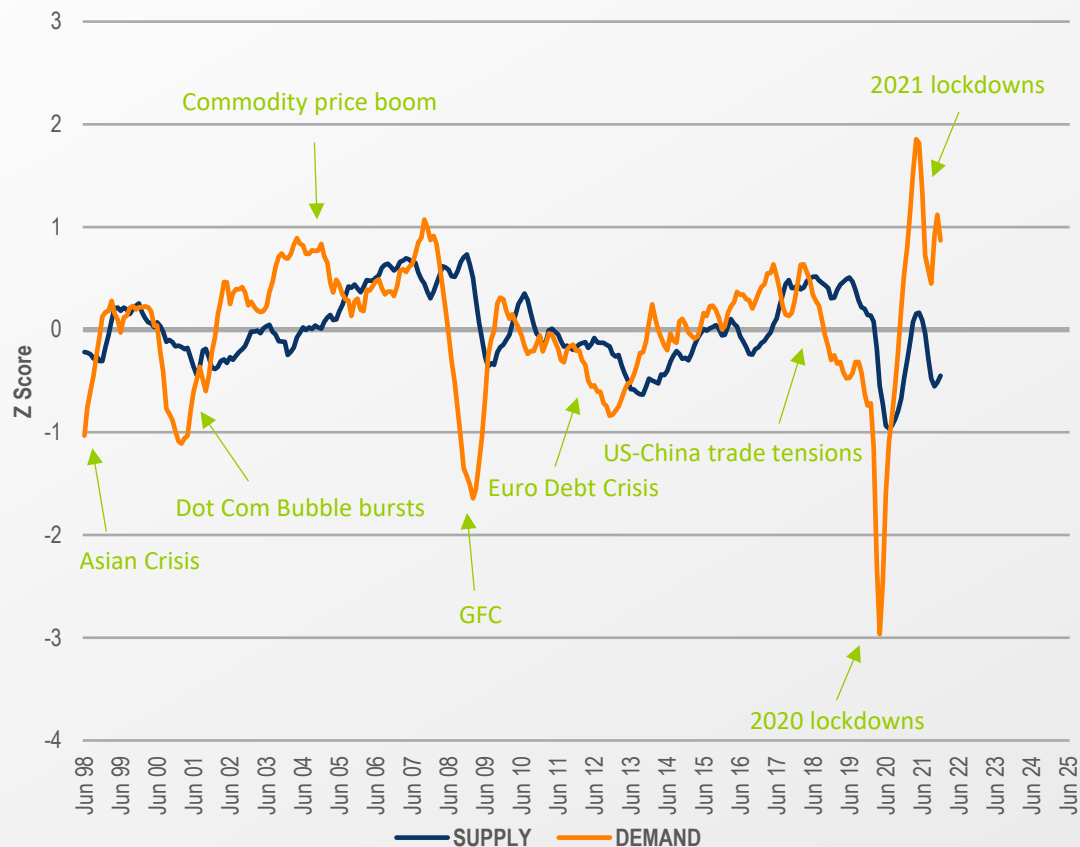




## AUSTRALIAN ECONOMY

# Supply-demand

Estimates of Demand & Supply (Australia)



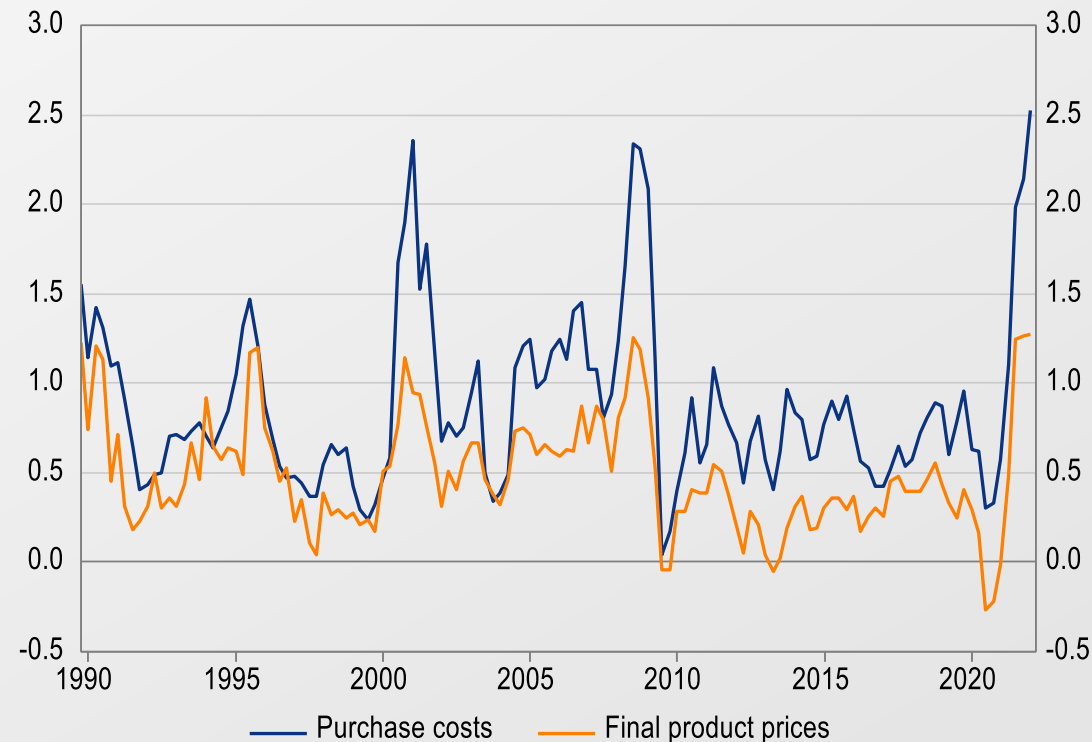
*It's not just constrained supply that's the issue, it's the combination of this with strong demand...*

Source: QTC Economic Research, Westpac-ACCI, Refinitiv

Input & Output Prices

Australian businesses purchase costs & product prices

Both axes are quarterly % change

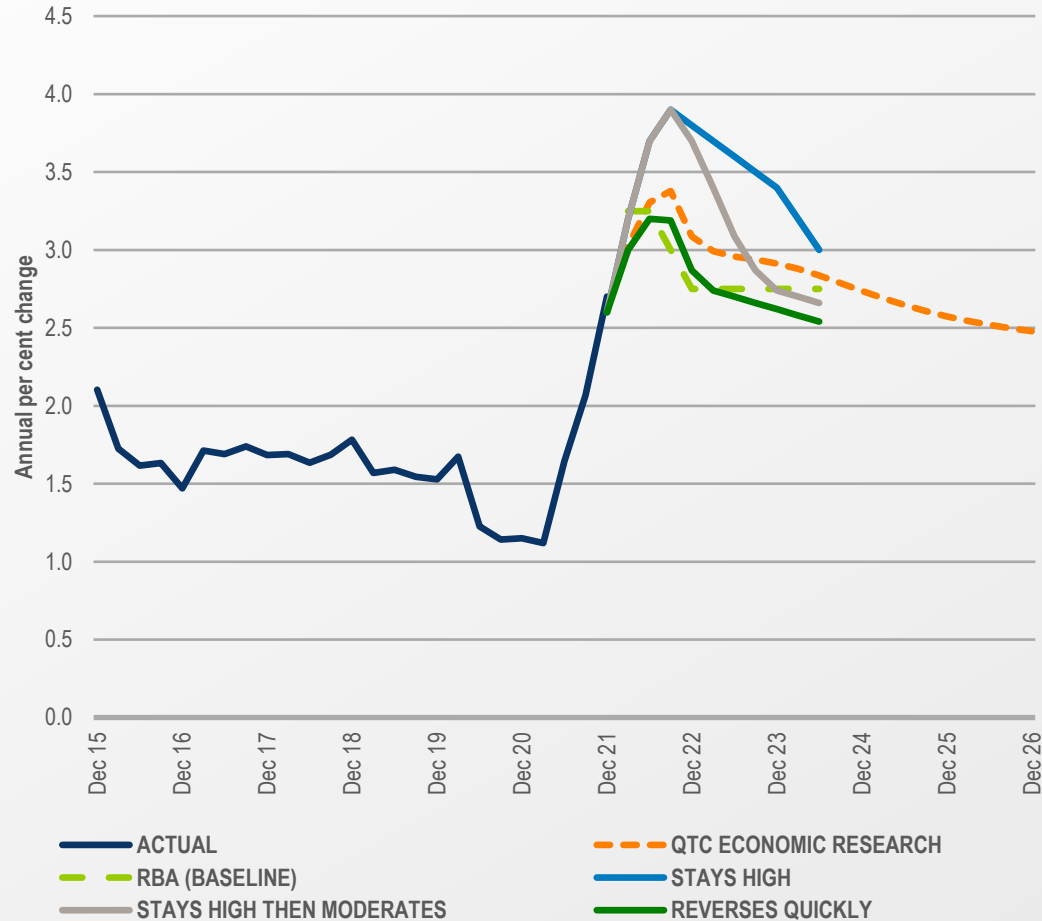


*...this is evident in both inflation in firm's purchase costs and selling prices*

Source: NAB, Refinitiv

Source: Refinitiv Datastream, QTC

# Inflation

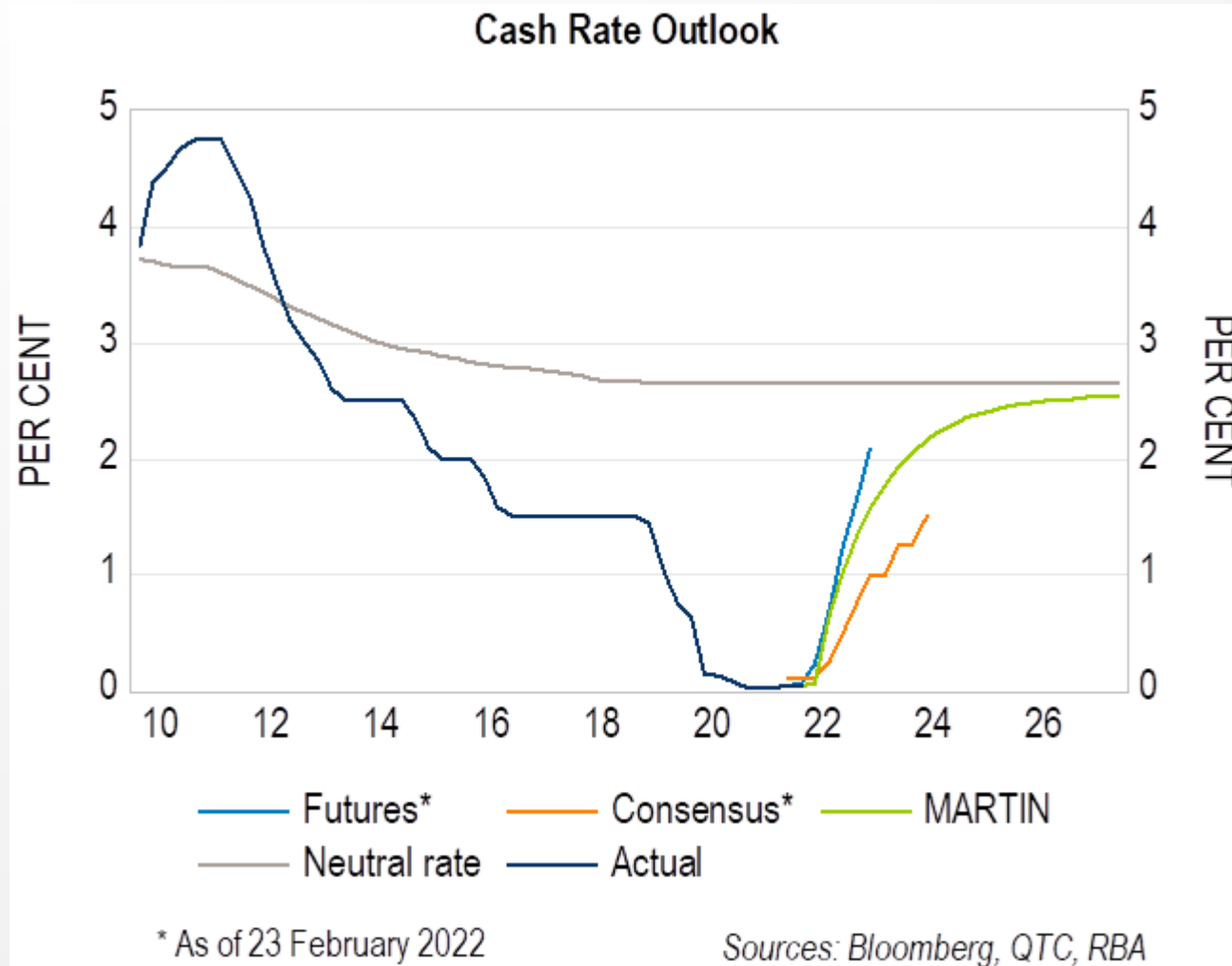


Simple scenarios – QOQ trimmed-mean inflation assumptions

|         | Stays high | Stays high then moderates | Reverses quickly |
|---------|------------|---------------------------|------------------|
| Q4 2021 | 1.0        | 1.0                       | 1.0              |
| Q1 2023 | 1.0        | 1.0                       | 0.8              |
| Q2 2023 | 1.0        | 0.9                       | 0.7              |
| Q3 2023 | 0.9        | 0.8                       | 0.7              |
| Q4 2023 | 0.9        | 0.8                       | 0.7              |
| Q1 2024 | 0.9        | 0.7                       | 0.7              |
| Q2 2023 | 0.9        | 0.7                       | 0.7              |
| Q3 2023 | 0.8        | 0.7                       | 0.7              |
| Q4 2023 | 0.8        | 0.7                       | 0.6              |
| Q1 2024 | 0.7        | 0.7                       | 0.6              |
| Q2 2024 | 0.7        | 0.7                       | 0.6              |

*It is easy to make the case for above target inflation across all of 2023*

# Monetary policy



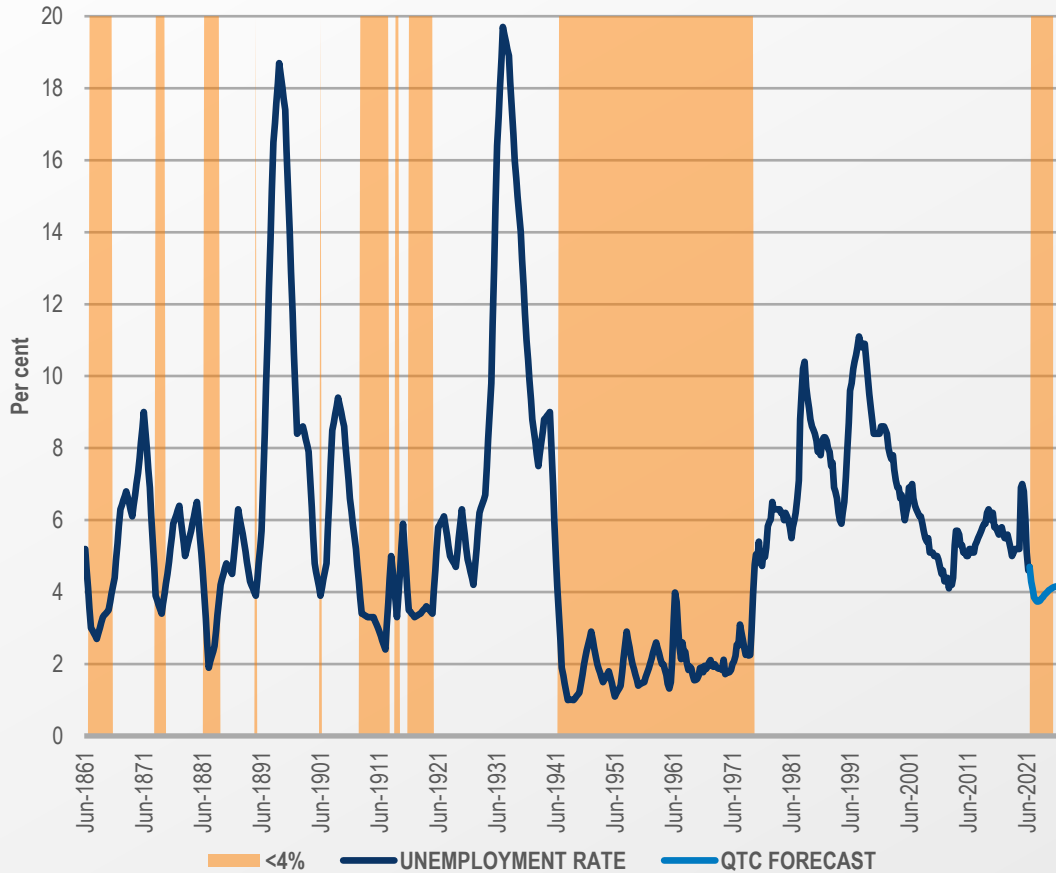
*These inflation outcomes should prompt RBA hikes*

*Scenarios run using the RBA's MARTIN model suggest 170-180bps of cash rate hikes over the next two years*

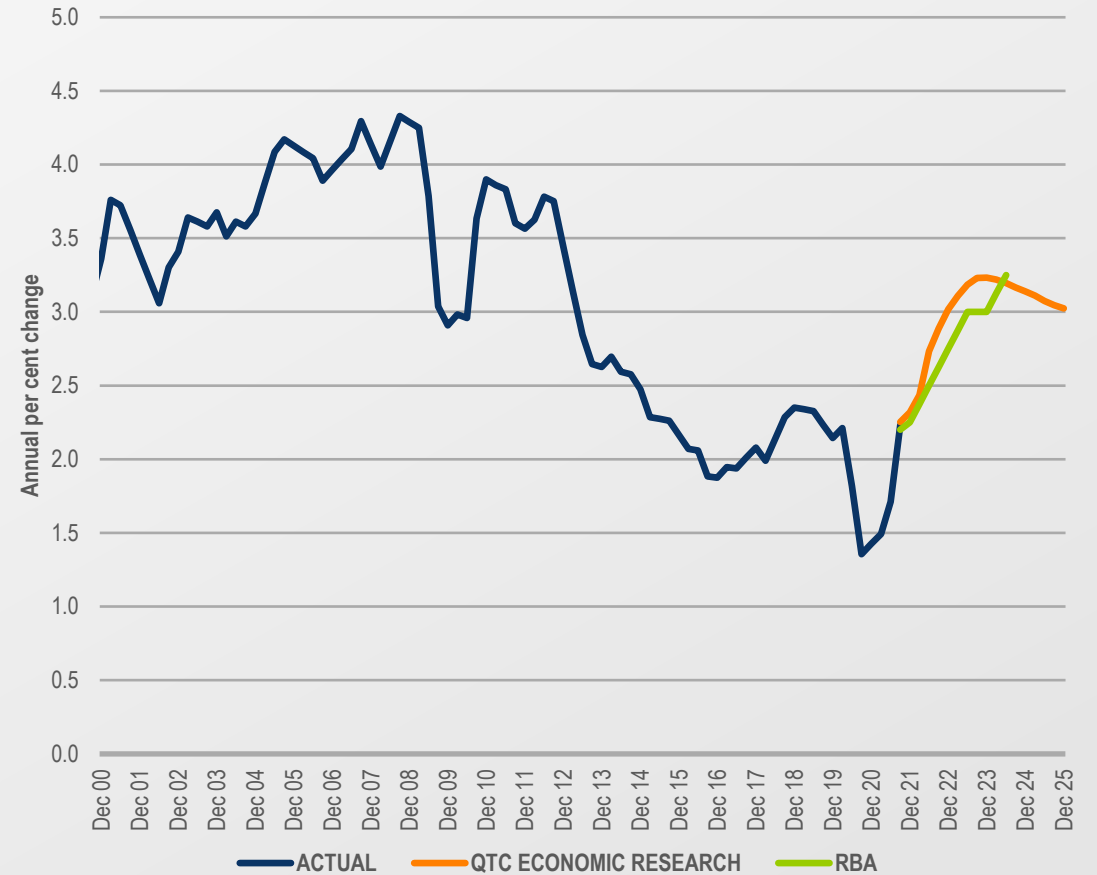
*This is broadly in line with market pricing*

# Australia – Labour markets

## Unemployment rate



## Wages outlook

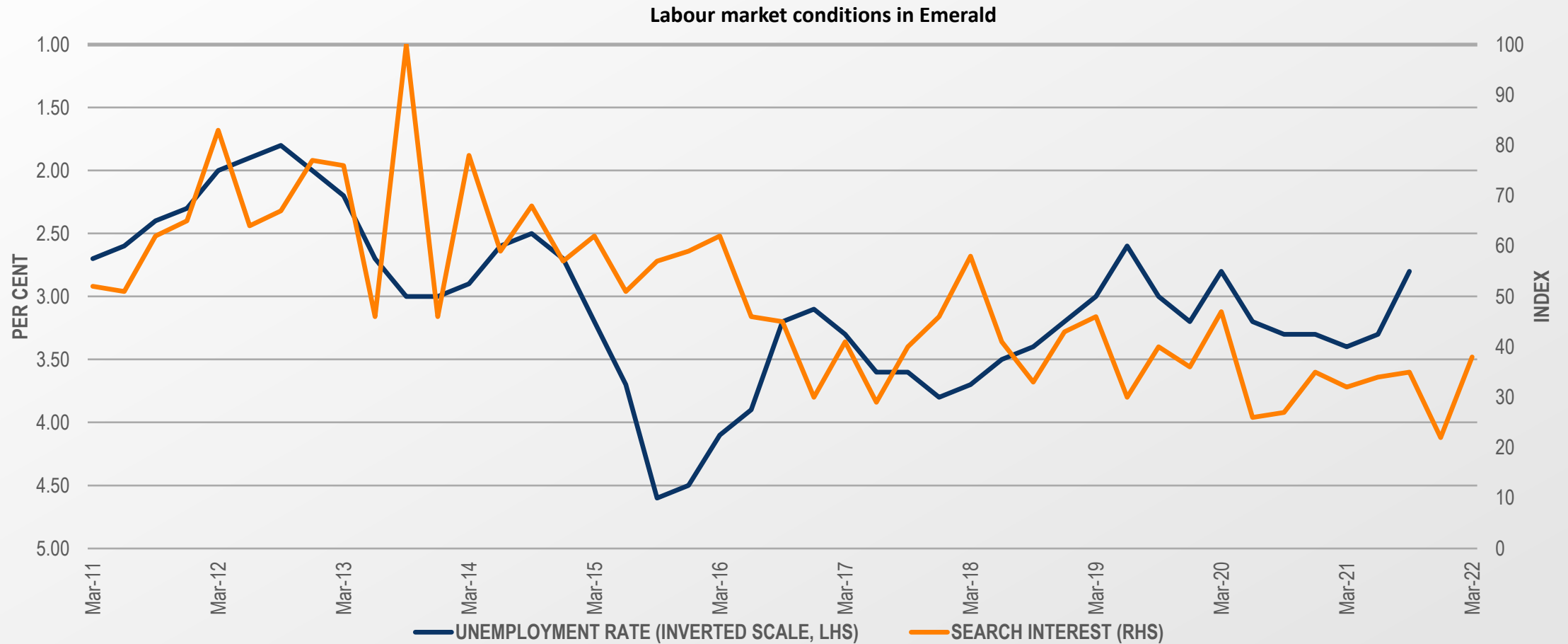


How low could the unemployment rate go? What could it mean for wages?



## CENTRAL HIGHLANDS ECONOMY

# Labour markets

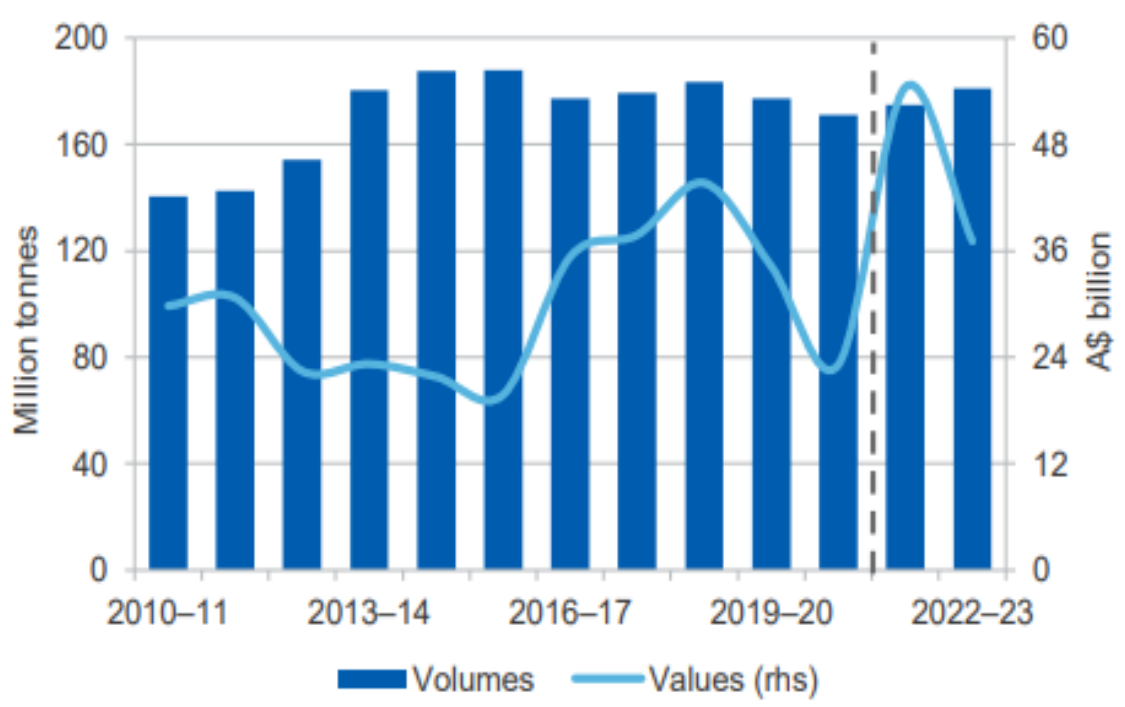


*Labour market conditions in Emerald are very strong*



# Metallurgical Coal

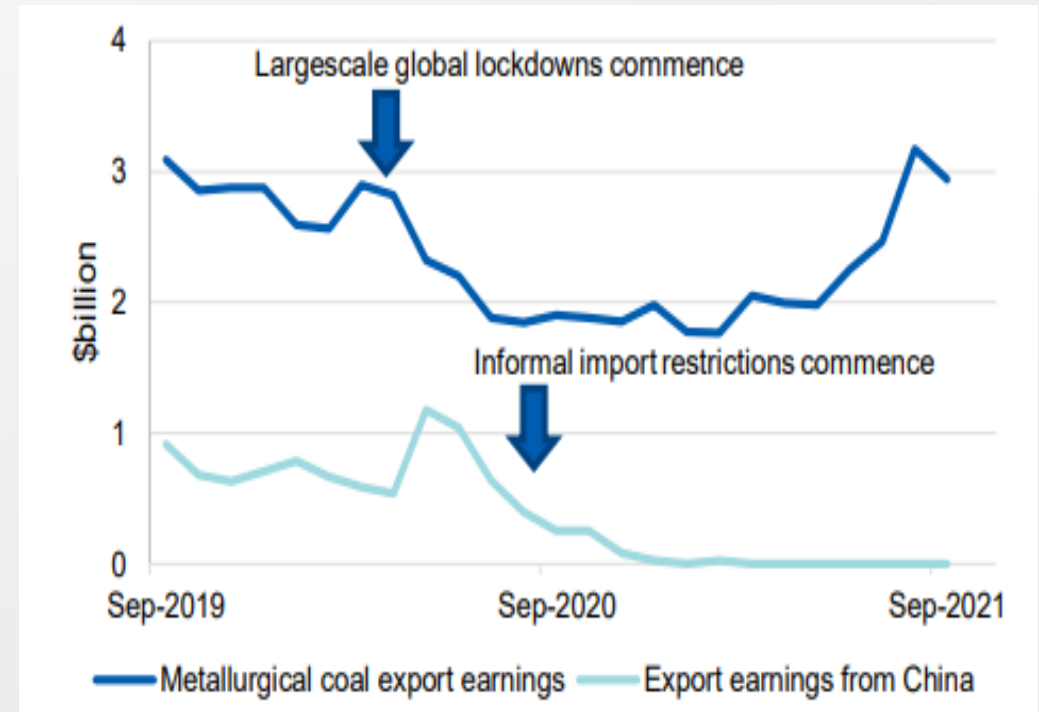
Australian metallurgical coal exports



Source: Department of Industry, Science, Energy & Resources' Resources & Energy Quarterly December 2021

*Met coal export volumes to rise but prices fall...*

Australia's metallurgical coal export values

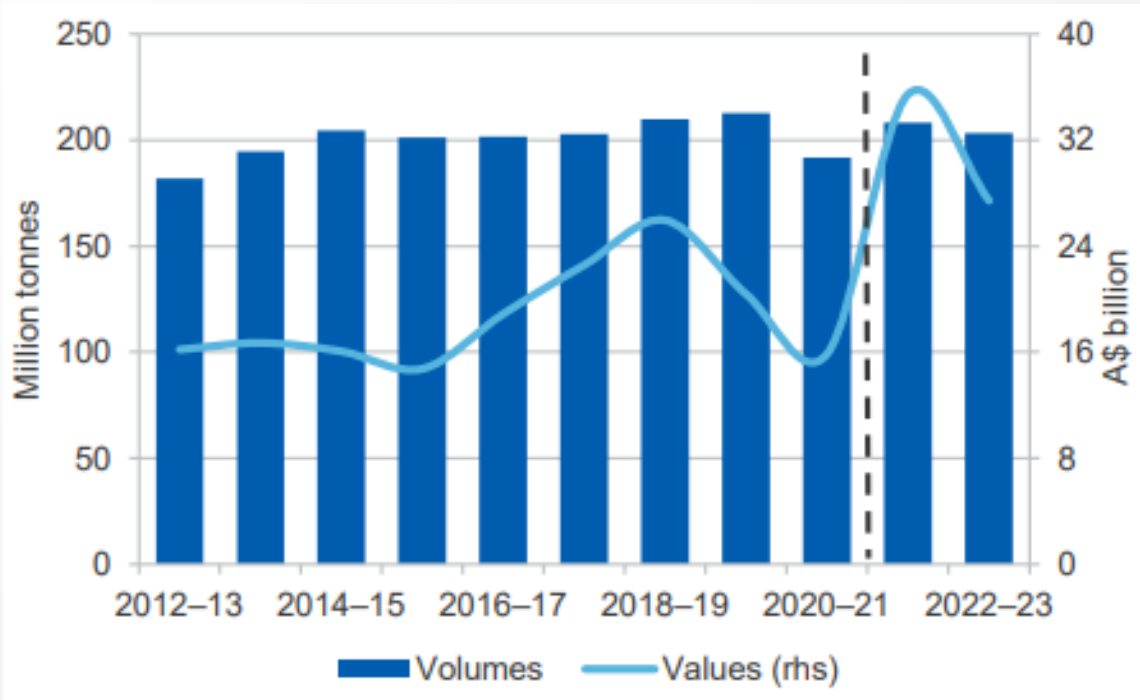


Source: Department of Industry, Science, Energy & Resources' Resources & Energy Quarterly December 2021

*...as Australia continues to diversify its customer mix*

# Thermal Coal

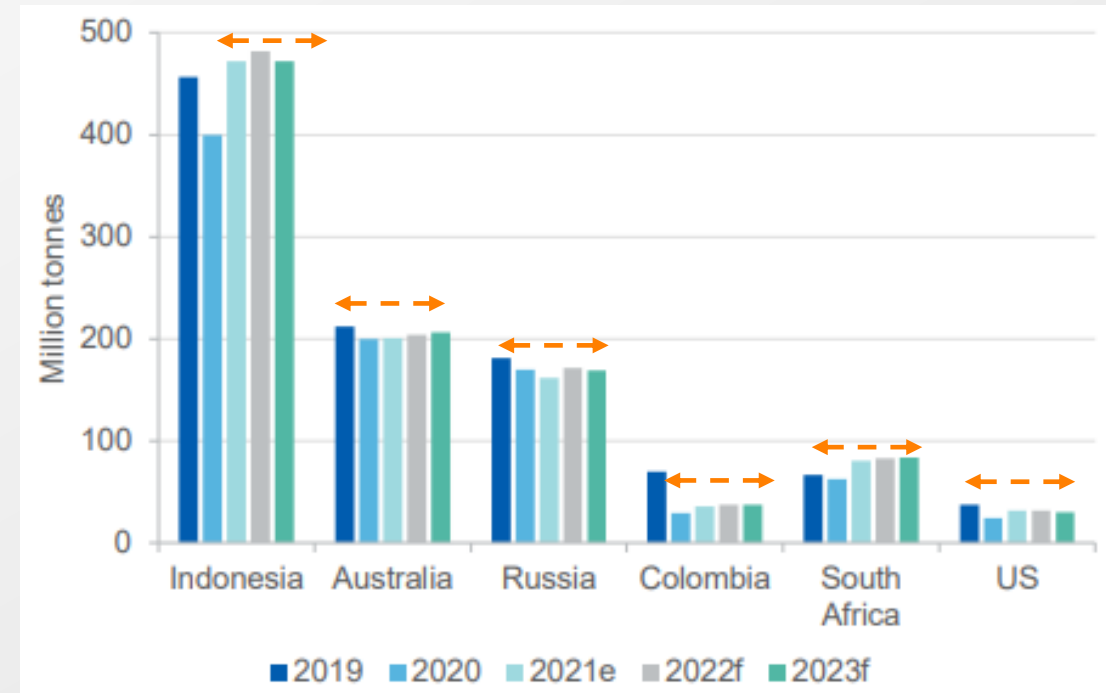
Australian thermal coal exports



Source: Department of Industry, Science, Energy & Resources' Resources & Energy Quarterly December 2021

*Aussie thermal coal export volumes to remain steady...*

Thermal coal exports

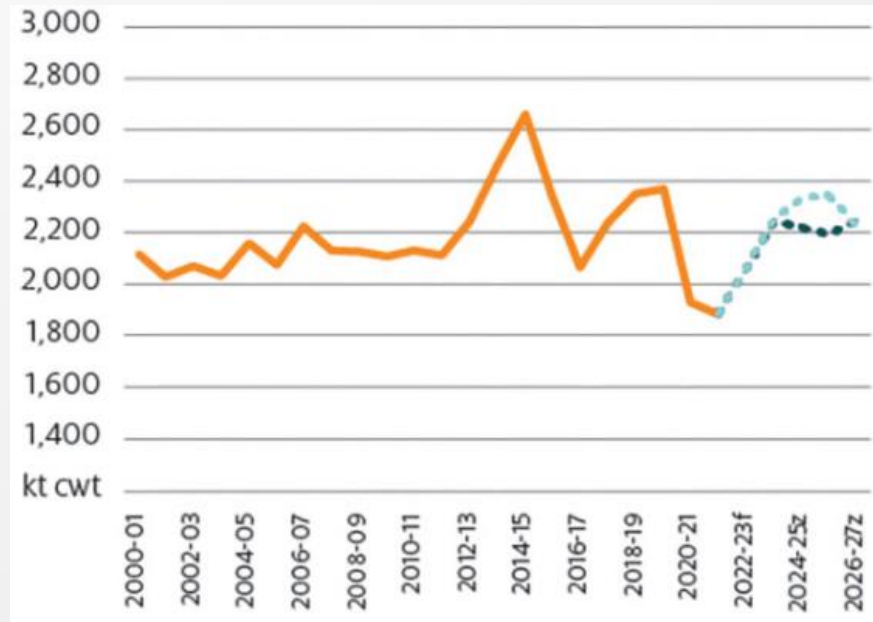
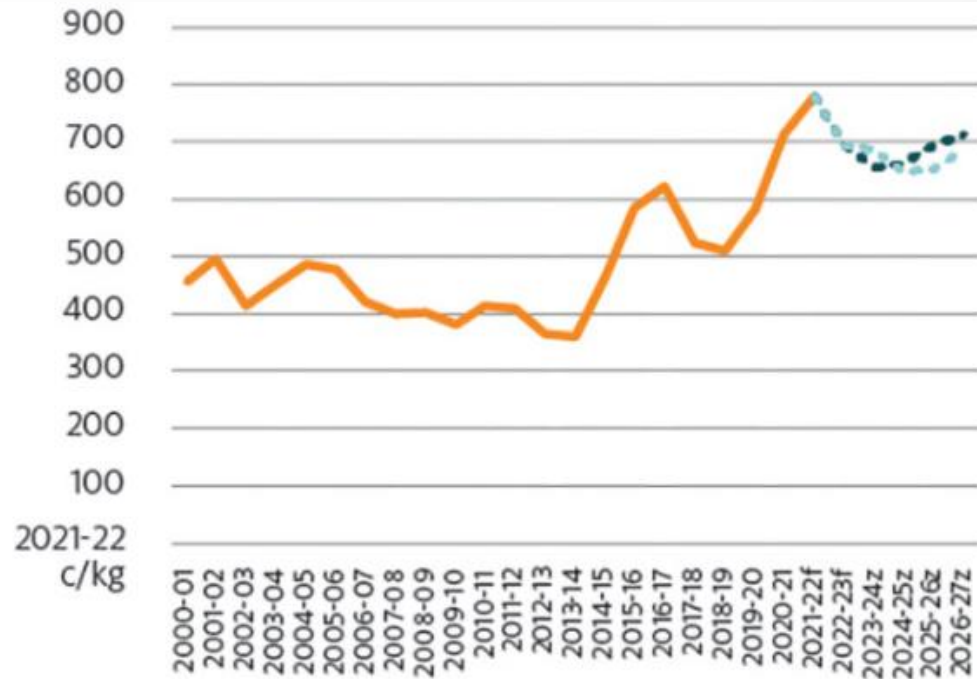


Source: Department of Industry, Science, Energy & Resources' Resources & Energy Quarterly December 2021

*...but we are by no means alone on this*

# Beef

Beef prices



Beef & Veal production

|         | FY22 | FY23 | Record? |
|---------|------|------|---------|
| Prices  | +14% | -9%  | Yes     |
| Volumes | -3%  | +11% | No      |
| Values  | +8%  | +4%  | Yes     |
| Exports | +11% | +0%  | Yes     |



Beef cattle herd size

# Crops

- For Central Queensland:
  - Rainfall:
    - “Above average rainfall is expected across summer cropping regions over the coming months, which will support continued crop development and yield potentials in central Queensland.”
  - Sorghum:
    - “...planting of the sorghum crop mostly started in late December but a particularly dry January has resulted in average to below average soil moisture levels.”
    - “The challenge ahead will be exporting the large sorghum crop, given the current disruptions to supply chains.”
  - Cotton:
    - “...above average rainfall over the past 18 months has replenished on- and off-farm water storage levels. Along with strong international prices and good soil moisture availability, cotton planted area is expected to have increased significantly.”



## FINANCIAL MARKETS

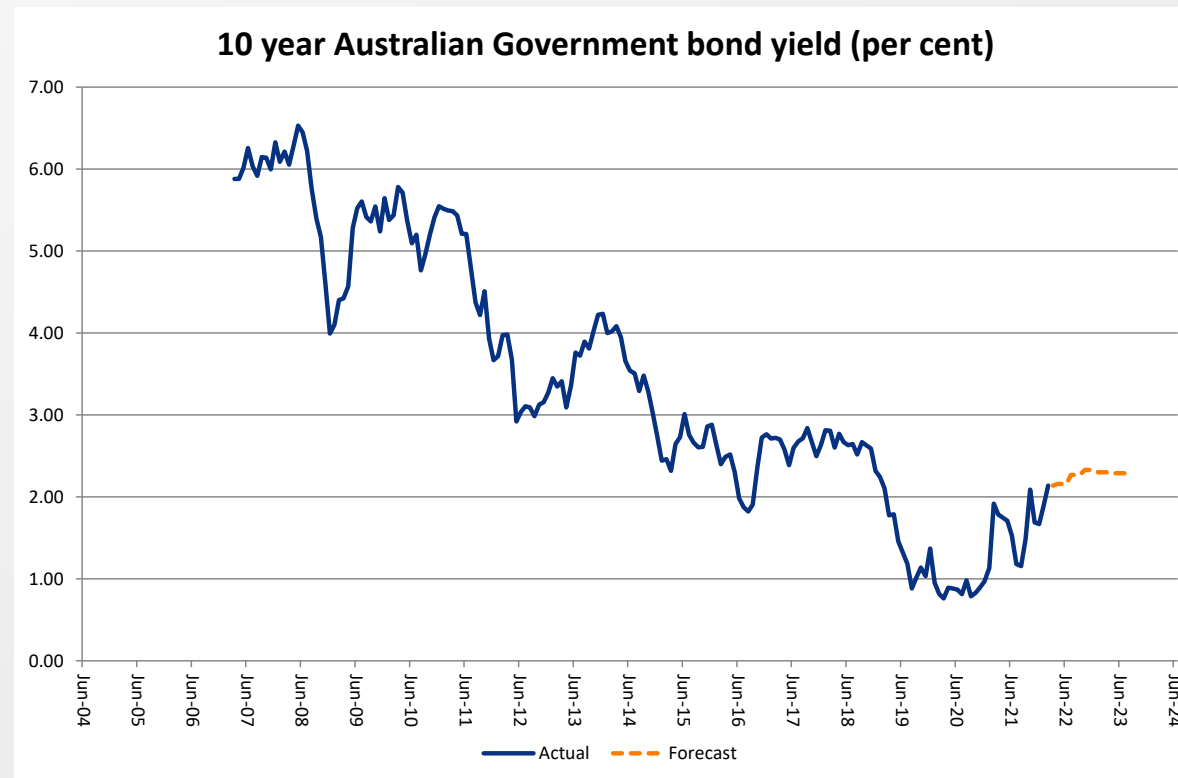
# Bond yield outlook

## Outlook for long-term interest rates<sup>2</sup>

| TIME HORIZON | DIRECTION | COMMENTS                                                                                                                                                                                                                                               |
|--------------|-----------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 – 3 months | ↗         | Strong momentum in global inflation and central banks looking to combat this by tightening policy should see yields continue to rise in the near-term.                                                                                                 |
| 12 months+   | ↗         | There is scope for yields to move higher but by how much is hard to tell given the prospect that inflationary pressures will ease at some point and that investors may start to price weaker future economic conditions after central bank rate hikes. |

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Economic  
Research →

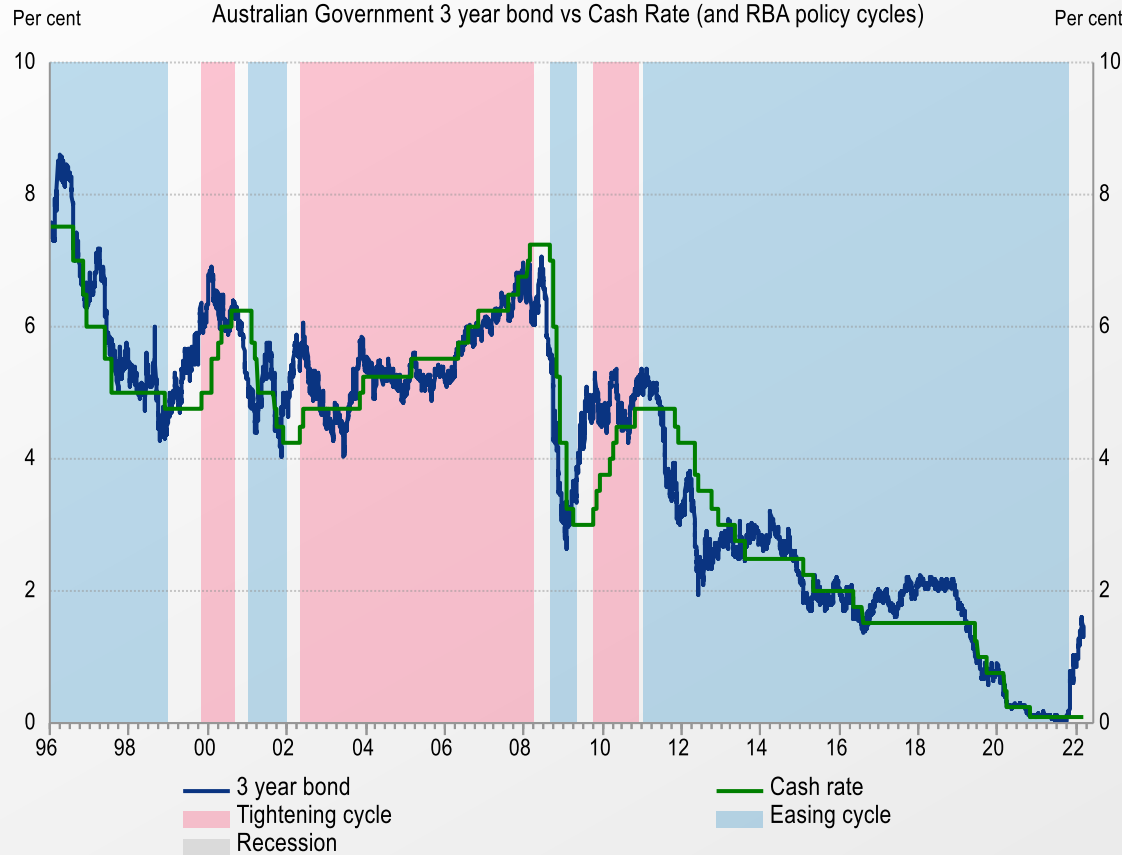
Market  
economists →



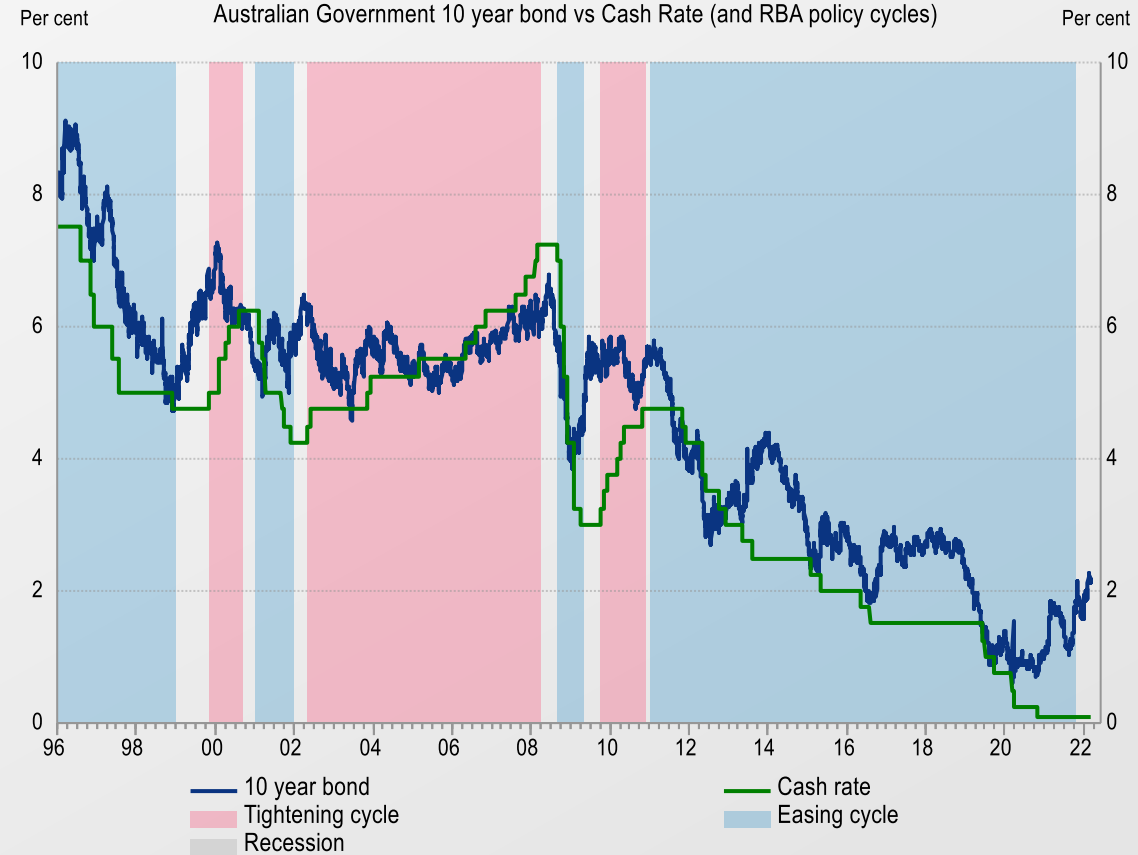
*It is also our view (in a few months time though)*

# Bond yield outlook

Australian Government 3 year bond yields and the RBA cash rate



Australian Government 10 year bond yields and the RBA cash rate



Source: Bloomberg, RBA, QTC Economic Research

Source: Refinitiv Datastream, QTC

Source: Refinitiv Datastream, QTC

*Both short and long-term yields will typically rise less than the cash rate in a tightening cycle*

# Bond yield outlook

Base case

Yields rangebound

Expected real rates  
Expected inflation exp  
Uncertainty over real rates  
Uncertainty over inflation



*Our base case is that yields will rise a little, though remain within broad ranges*

*Catalyst: Demand-supply imbalances normalise, inflation moderates (but to higher levels), central banks don't need to do more than priced*

Risk case

Yields higher than expected

Expected real rates  
Expected inflation  
Uncertainty over real rates  
Uncertainty over inflation



*The risk case (a reasonable probability) is that yields rise by more than we expect*

*Catalyst: Demand-supply imbalances remain more acute and for longer, inflation remains higher, interest rates need to rise by more than markets expect*



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## What to expect when you're expecting inflation

Trent Saunders, QTC Principal Economist

Published: 28 June 2021

6 min read

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## SUMMARY

- Global economic conditions have moderated
- An imbalance between demand and supply is constraining production and boosting inflation
- For Australia, labour markets should tighten, wages rise and inflation stay firm
- The outlook for Central Highlands key industries is reasonable over coming years

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