OPENING STATEMENT- ECONOMIC DEVELOPMENTS

Since I last appeared before the Committee forecasts for the Australian economy have been updated in the Budget. They point to the significant headwinds that the economy is facing in the transition from the mining investment boom and the unevenness of the global recovery.

The US economy is back to near full employment providing impetus to global growth. The US Federal Reserve has signalled that it expects to start raising interest rates later this year.

In China, growth has eased leading authorities to provide additional policy stimulus with lending and deposit rates cut further early this month. Signs suggest that the cuts are having a more significant impact than earlier moves. Given its size, growth in the Chinese economy will continue to make a significant contribution to global growth and have a significant impact on Australia's medium term prospects.

Activity in the euro area has improved recently with signs that consumer spending is being bolstered by lower oil prices, a weaker euro and stabilising labour markets. But mounting risks of Greece defaulting on its debt obligations highlights the inherent fragility and structural challenges facing the euro area. The latest data from Japan also suggest that activity continues to recover.

Closer to home, the Australian economy is facing the challenge of rebalancing from mining investment led growth at the same time as the terms of trade are falling. Mining investment is expected to fall by around 25 per cent in 2015-16 and 30 per cent in 2016-17 and the iron ore price has nearly halved over the past year.

On the other hand supportive fundamentals including the lower exchange rate, lower oil prices and low interest rates are expected to underpin the transition to broader-based growth. The Budget forecasts the economy to grow at 2¾ per cent in 2015-16 before rising to around its trend rate of 3¼ per cent in 2016-17.

There is evidence of these fundamentals at work in household consumption which grew at three year highs in the December quarter of last year. Indicators since Budget such as retail trade, automotive sales and consumer sentiment are consistent with a further improvement in the outlook for consumption.

Dwelling investment is responding to low interest rates as well as strong house prices and solid population growth. The significant pipeline of approvals suggests that the upswing still has some way to run.

The depreciation of the Australian dollar over the past year will play an important role in the transition to broader-based growth by making businesses in export-orientated and import-competing sectors more competitive. Exports are expected to continue to make a significant contribution to GDP growth with resource and services export volumes growing particularly strongly.

Although investment by the services sector has grown strongly over the past year, the latest CAPEX survey, which was conducted in advance of the Budget ,continues to suggest that businesses in the non-mining economy overall remain reluctant to commit to significant investment plans in 2015-16.

. Liaison conducted by Treasury staff since the Budget suggests that the Jobs and Small Business package has been well received across a range of businesses especially those operating in parts of the retail sector. This is consistent with a notable lift in consumer confidence following the release of the Budget.

It remains our view that the supportive conditions I have highlighted earlier and healthy corporate balance sheets should encourage increased investment going forward. Nonetheless, the pace and timing of a recovery in non-mining business investment remains a significant source of uncertainty.

In the midst of this transition the labour market has been resilient. In recent months, employment growth has picked up, labour force participation has risen and the unemployment rate has remained steady. That said, with GDP forecast to grow below trend, the unemployment rate is still expected to edge a little higher to 6½ per cent in 2015-16 before falling to 6¼ per cent in 2016-17.

Wage growth continues to be constrained by spare capacity in the labour market. Although modest growth in wages is weighing on household income growth, it has been crucial to supporting employment during a period where the economy has been growing a little below trend.

Incomes are being affected by weaker commodity prices. Although they have recovered a little recently, further growth in low cost supply is expected to continue to weigh on prices for many of our key non-rural commodity exports.

As a result, nominal GDP growth is forecast to grow by 3¼ per cent in 2015-16 before picking-up to 5½ per cent in 2016-17. This has driven a substantial downgrade to tax receipts of $52 billion since the 2014-15 Budget, $20 billion of this due to iron ore prices alone. I note that these forecasts are sensitive to assumptions about the future path of key commodity prices. In the Budget we have assumed an iron ore price of US$48/tonne FOB, which was the four week average of the iron ore price on the day the assumptions were finalised. The iron ore price has been somewhat higher since which, if sustained, provides upside risks for nominal income growth.