Senate Economics Legislation Committee

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Supplementary Budget Estimates 1 - 2 November 2006

Question:	**sbt 29**
Topic:	**Commodity Price Outlook**
Hansard Page:	**Written**

Senator EVANS asked:

The Reserve Bank's indexes of commodity prices in USD, AUD and SDR terms all rose to record highs in October. The largest contributors to the rise in commodity prices in October were increases in the prices of nickel, aluminium, zinc and wheat.

(1) What is Treasury's view of where commodity prices are heading?

(2) What would be the consequences for company tax receipts of a downturn in commodity prices?

(3) What has been the contribution of the boom in commodity prices to revenue over the last 5 budgets?

(4) Revenue forecasts in the Budget were formulated on the assumption that commodity prices would return to long run trends in a two steps over the 2-3 year period — is this correct?

(5) Does Treasury believe there will be any adjustments to this timeframe (either forward or backward)? What is the quantum of each step down?

(6) What does Treasury expect to happen to mining volumes?

(7) Is mining sector profitability expected to be maintained as a consequence of increased volumes?

Answer:

(1) As stated in the 2006-07 Budget, commodity prices are expected to moderate as global supply expands. The timing and extent of any fall in commodity prices is uncertain and will depend, in part, upon the speed with which additional supply becomes available.

(2) The 2006-07 Budget's company tax estimates and projections incorporate a forecast of commodity prices for 2006-07 and then a technical assumption of prices of key commodities returning to a longer run level over the first two years of the projection period, 2007-08 and 2008-09 (see 2006-07 Budget Paper No. 1, page 3-31).

Should commodity prices be lower than forecast in 2006-07 then, other thing being equal, company tax would be lower.

In the Budget, 2007-08 to 2009-10 are projection years and, as outlined above, the technical assumption for commodity prices relates to the first two years of the projection period. There are considerable risks associated with the technical assumption, particularly given the uncertainty around the future demand for resources and the associated supply response.

(3) See Treasurer's press release number 81 of 1 June 2006.

(4) The 2006-07 Budget makes the technical assumption that the prices of key commodities will return to a longer run level over the first two years of the projection period, 2007-08 and 2008-09.

The technical assumption is explained in Box 6 on page 3-31 of Budget Statement 3, Budget Paper No. 1 2006-07.

(5) The technical assumption that the prices of key commodities will return to a longer run level over the first two years of the projection period was used in the 2005-06 Budget and MYEFO and the 2006-07 Budget. Any change to this assumption is a matter for the Government.

The technical assumption results in a 12½ per cent fall in aggregate non-rural commodity export prices in 2007-08 and an 11¾ per cent fall in 2008-09.

(6) Mining production and exports are expected to increase as additional production capacity comes on stream.

(7) Future mining sector profitability will depend, in part, on the extent to which volumes increase and commodity prices fall.