Summary:

- Queensland’s economy has been growing at a very strong pace, recovering well after the floods and cyclone in early 2012. State final demand grew by a solid 7.5% in the year to the March quarter 2012, well above its long-run average of 5.7% and domestic final demand for Australia of 5.0%.

- The outlook for Queensland’s economy is generally positive, but growth should soften from the heady pace witnessed over the past year. Although business investment will likely remain strong, we expect export growth to moderate as global growth softens. Further, the structural changes impacting on some of Queensland’s key sectors, including tourism, may lead to further labour market weakness. We continue however, to expect a solid pace of growth for 2012-13.

- Business investment has been a significant driver for growth in Queensland, and we still expect investment spending growth to remain firm. Despite a softening global backdrop and falls in commodity prices, there is likely to remain a large amount of work in the pipeline. Mineral, energy and infrastructure projects in the advanced stages of planning amount to a massive $75.3bn.

- Multispeed growth, however, is evident in Queensland, and has resulted in varied conditions across different regions in Queensland. While mining centres have prospered, there are parts of the economy that are continuing to struggle under the weight of the high Australian dollar, most notably areas dependant on Queensland’s tourism sector.

- Consumer spending has picked up in recent times, but concerns about the global outlook, slowing Chinese demand for Queensland’s commodities and a soft labour market may keep consumers sidelined, and point to a modest pace of growth.

- Queensland’s labour market was soft over 2011 and has continued to be soft so far this year. The breakdown of employment by industry reflects some of the structural changes that are underway in Queensland’s economy, including strength in the mining sector, but weakness in industries associated with housing construction and tourism. The uncertain global economic backdrop and weak business confidence indicate that firms may continue to be cautious in their hiring intentions, and that there is a risk that the unemployment rate will edge a touch higher this year.

- The housing market in Queensland has faced difficult conditions, but the outlook is more promising. Lower borrowing costs and the return of first home buyers to the market are positive signs. A recovery in population growth will also provide a boost to the housing market and Queensland’s economy. Queensland house prices should stabilise further this year, and recover towards the end of the year. Any recovery in housing in Queensland, however, is likely to be uneven across the State.

- The potential for a sharper slowdown in global growth is the key risk to Queensland’s outlook, which could lead to further slowing demand for Queensland’s commodity exports and dampen sentiment and spending.
Economic Growth

Queensland’s economy has been growing at a very strong pace, recovering well after the floods and cyclone in early 2012. State final demand grew by a solid 7.5% in the year to the March quarter 2012, well above its long-run average of 5.7% and domestic final demand for Australia of 5.0%. In comparison to other States, annual growth Queensland’s State final demand was the third fastest behind Western Australia and the Northern Territory.

Private business investment has been a strong driver of growth in Australia, and Queensland has been a large beneficiary of the mining investment boom given a large proportion of major projects is located in the State. Household consumption has also grown solidly and has provided a modest contribution to growth.

Note that ideally, gross State product, which includes inventories and net exports, is a more appropriate measure of economic growth, but this measure is published only annually on a State basis. A slump in exports, predominantly in coal, due to the floods in early 2011 detracted significantly from growth in Queensland. GSP subsequently rose by just 0.2% in 2010-11, but is set to recover strongly in 2011-12.

Net exports are also likely to detract from GSP in 2011-12, however not as much as in 2010-11. Export volumes grew at a solid annual pace of 31.1% in the year to the March quarter, but growth in imports has also been strong as the business investment upswing is demanding a large amount of imported capital. Import volumes rose by 20% in the year to March quarter 2012.
The outlook for Queensland is generally positive, but growth should soften from the heady pace witnessed over the past year. Business investment will remain a major supportive factor for growth, given there remains a large amount of business investment in the pipeline, predominantly within the mining sector. Although there are some headwinds including a clouded outlook for global growth and hurdles for coal seam gas projects, we expect that business investment will continue to be strong. Another positive for Queensland’s outlook is a pickup in population growth, which has been a recent phenomenon occurring Australia-wide. This is a welcome development for economic growth and Queensland’s housing sector which has faced a challenging environment in recent times. Ongoing reconstruction activity which has further to run after the natural disasters in 2011 will also be supportive for growth.

There are however, parts of the economy that are continuing to struggle under the weight of the high Australian dollar, most notably Queensland’s tourism sector, the State’s second largest export earner (after coal). There has been some reprieve given that the Australian dollar has fallen from above $1.08 earlier this year, but we expect the Australian to continue to stay close to parity.

The difficulties facing tourism combined with the ongoing strength of the mining sector highlights the multispeed nature of the economy, which is evident across different regions in Queensland.

Ongoing worries from abroad continue to pose downside risks to economic activity for Queensland and Australia, and point to some downside risk for Queensland’s exports. Indeed, softening global demand suggests that export growth will continue to soften this year. However, recent rate cuts from the Reserve Bank (RBA) should provide support to Queensland’s economy, particularly for consumption and Queensland’s struggling property sector.

Queensland Treasury expect gross State product to expand by 4.25% in 2011-12 and 5% in 2012-13. Our forecast is for growth of 6.9% 2011-12, driven by a rebound in exports, and very strong growth in business investment. It also reflects a much stronger than expected growth outcome in Q1, which has been published since Queensland’s Treasury released its forecast in its Mid-Year Fiscal and Economic Review in January. Our forecast for 2012-13 is for growth to soften to 4.6%. Although business investment will likely remain strong, we expect export growth to moderate as global growth softens. Further, the structural changes impacting on some of Queensland’s key sectors may lead to further labour market weakness. We, however, continue to expect a solid pace of growth, which is above the 10-year average growth rate of 4.2% for Queensland’s economy (For more detailed forecasts, see page 8).
Business Investment

Private business investment has accelerated in Australia, thanks to the high terms of trade and a mining boom. A large proportion of recent growth in national business investment has been in Queensland due to its growing mining industry. In the year to the March quarter, business investment in Queensland grew at a solid pace of 29.0%.

Prospects for business investment are also very positive. Nationally, based on ABS data, we estimate that firms raised capital expenditure by 30.6% in 2011-12 and this will rise to 33.7% in 2012-13, of this, a large proportion will be spent in Queensland.

A softening global backdrop and recent falls in commodity prices have prompted major miners to defer some projects, and there is a heightened possibility that spending outcomes will be lower than estimated. However, we still expect investment spending growth to remain strong, given the large amount of projects that are in the later stages of planning and very unlikely to be pulled back.

The Bureau of Resources and Energy Economics (BREE) has noted the large pipeline of projects in Queensland that are in the advanced stages of planning, worth an estimated value of $75.3bn. These projects are classified as those that are either “committed” or “under construction”. Leading the projects underway are some large LNG projects including BG Group’s Curtis Island LNG facility worth US$20bn and the Gladstone LNG project with an estimated cost of US$16bn. There are also a number of coal mine projects in the pipeline.
In addition to capital expenditure, engineering construction has been the other major driver of business investment in Queensland and Australia. Engineering construction in Queensland grew by a remarkable pace of 59.5%, in the year to the March quarter, and is set to remain very strong. According to the ABS, work yet to be done [the value of work on outstanding projects] in engineering construction stood at $56.9bn in the March quarter.

Outside of the mining sector, non-residential building has picked up to an annual rate of growth of 23.3%, the strongest annual pace in almost six years. There remain a number of projects in the pipeline and this should support non-residential building activity next year, with commercial and industrial building commencements expected to post modest growth.

### Consumer Spending

Consumer spending has picked up in recent times, rising 4.7% in the year to the March quarter, the fastest pace in nearly four years. Annual growth is just above long-run average growth of 4.6% for household consumption in Queensland, and above growth in Australia of 4.2% for the year to the March quarter. Firm wage growth over the past few years and rate cuts from the RBA late last year may have helped buoy consumer spending.

Similarly, retail spending has also recovered in recent months. Retail spending grew by 4.3% in the year to May, accelerating from 2.0% annual growth in the year to February, likely supported by falls in petrol prices and a further cut to the cash rate in May.

Consumers are spending a greater proportion of income on services, a phenomenon not only occurring in Queensland, but nationwide. In the year to March, growth in spending on transport, recreation and health were among the strongest, although spending on food and alcoholic beverages also grew strongly.

Recent RBA rate cuts should help support further spending, however subdued consumer confidence in Queensland suggests that the outlook for consumer spending is for a more modest pace of growth. The Westpac-Melbourne Institute survey of consumer sentiment in Queensland is suggesting that consumers have become more pessimistic about the outlook. In July, the consumer sentiment index for Queensland stood at 91.7, indicating that pessimists outweigh optimists, and is well down from a peak of 104.3 in November 2011. Consumer sentiment in Queensland is also below the index for Australia which stood at 99.1 in July, indicating that Queenslanders are more pessimistic than Australia-wide. Concerns about the global outlook, slowing Chinese demand for Queensland’s commodities and a soft labour market may keep consumers sidelined.
Housing

The housing market in Australia and Queensland faced difficult conditions over 2011, and has remained soft over much of 2012. According to the Australian Bureau of Statistics (ABS) house prices in Brisbane rose 0.4% in the March quarter, but are still down 3.7% in the year to March. An alternative measure of house prices published by RP Data-Rismark reveals a similar story. Brisbane dwelling prices rose 1.0% in June, but are still down 4.7% in the year to June.

- Outlook

The outlook for Queensland’s housing market, however, is improving, and it appears that house prices in Queensland may be close to stabilising. Rate cuts from the RBA since November will be supportive for housing.

An encouraging sign is a return of first home buyers to the market, which as a percentage of new dwellings financed has increased. First home buyers comprised 19.8% of new home loans to owner occupiers in Queensland in May, much higher than a year ago when the proportion of new loans to first home buyers stood at 15.6%. A pick up in first home buyer activity provides support to house prices as it adds to overall housing demand.

Another positive for the housing market is a recovery in population growth after slowing throughout 2010 to 2011. The annual population growth rate picked up from 1.1% in June 2011 to 1.5% in December 2011. This improvement in population growth combined with very lacklustre residential building activity in recent years is expected to contribute to a growing housing shortage in coming years according to BIS Shrapnel, although to a lesser extent than in NSW or WA.

The emerging housing shortage should provide a floor for house prices, although growing concern about the global economic backdrop and a soft labour market may keep potential home buyers sidelined. However, lower borrowing costs and the boost in population growth should lead to further stabilisation in Queensland house prices and recovery towards the end of the year.

As the housing market tightens and as the outlook for house prices improves, a recovery in residential building should eventuate. Dwelling investment in Queensland has been very weak since 2010. Although dwelling investment rose 5.0% in the March quarter and 5.4% in the year to March, it came from a low base and activity is still much lower than average. There may be some crowding out effect as residential construction competes for resources with engineering construction. Leading indicators point to a continued softer trend in residential building activity over the short-term. Building approvals in Queensland are down 9.1% in the year to May.
Any recovery in housing in Queensland however is likely to be uneven across the State. Some parts of the Queensland housing market will take longer to recover, notably those also suffering from lower tourism activity such as the Sunshine Coast. Meanwhile, other parts are likely to see strong growth, particularly the regional centres with an overwhelming concentration of mining investment.

**- Rental Markets**

Brisbane has witnessed modest growth in rents over the past year. Rents for a 3-bedroom house in Brisbane rose 2.9% in the year to March, while rents for a 2-bedroom other dwelling rose by 4.3% in the year to March. Low vacancy rates also provide an indication of tight rental markets. The vacancy rate in Brisbane stood at 1.7%, in the March quarter 2012. Vacancy rates below 2% are indicative of very strong demand for rental accommodation, and point to further upward pressure on rents.

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**Labour Market**

Queensland’s labour market was soft over 2011 and has continued to be soft so far this year. The State’s labour market has been weaker than the labour market Australia-wide. In the six months to June 2012, Queensland has lost a net 10.4k jobs. Meanwhile a net 86.3k jobs have been added across Australia. Despite soft job growth, the unemployment rate in Queensland remains low at 5.3%, and just a touch higher than Australia’s unemployment rate of 5.2%.

The breakdown of employment by industry reflects some of the structural changes that are underway in Queensland’s economy, including strength in the mining sector, but weakness in industries associated with housing construction and tourism. In the year to May, the industry that added the most jobs was in finance & insurance services (+23.8k) followed by mining (+13.6k), then healthcare & social assistance (+11.3k). Meanwhile, jobs were lost in construction (-15.8k) and accommodation & food services (-15.7k).

The uncertain global economic backdrop and weak business confidence indicate that firms may continue to be cautious in their hiring intentions. Further, a range of leading indicators of employment are suggesting that labour market conditions will remain subdued in coming months with a risk that the unemployment rate will edge a touch higher this year.
Key Forecasts:

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<th>Economic Indicators, % Change</th>
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<th>2012–13 (f)</th>
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* Actual data

Source: St.George Banking Group
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