



The Hon Scott Morrison MP

Treasurer

Australia:

A strong and transitioning economy

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The transition of the Australian economy from the mining investment boom to a more diversified economy, with broader-based growth, is well underway.

Our economy is heading in the right direction – with improving business confidence and conditions, solid growth in consumption and dwelling construction, and strong jobs growth.

We continue to benefit from strong commodity export growth. But while the resources sector continues to play an important role in our economy, Australia's economic transition is about growth shifting to other sectors of the economy.

To date, we have seen hundreds of thousands of new jobs created in the employment-intensive service sectors of our economy. That's jobs like nurses and teachers, bricklayers, shop assistants and website designers. We're seeing new growth opportunities from a growing Asian region, such as in our booming education and tourism markets. And economic conditions are conducive for non-mining businesses to continue to grow and invest.

The Australian Government is providing economic leadership through this transition, to nurture and protect this momentum and back Australians as they continue to back themselves.

We achieve this by placing jobs and growth at the centre of our policy agenda, which in turn enables us to address our social and fiscal challenges.

The Government has a clear economic plan that is supporting this transition, to fuel economic growth and deliver our children and grandchildren the great jobs they deserve not just today, but tomorrow and for years to come.

As a government, the delicate rebalancing requires us to focus keenly on the policies that will boost investor confidence, drive productivity gains in our economy, particularly through innovation, and open up new markets through our successful and ambitious trade agenda and continue on our path of fiscal consolidation.

Our transition is underway, supporting jobs and growth

In the face of global uncertainty our economy continues to transition and grow.

Our economy grew 3.0 per cent over 2015, the strongest pace of through-the-year growth since the March quarter of 2014.

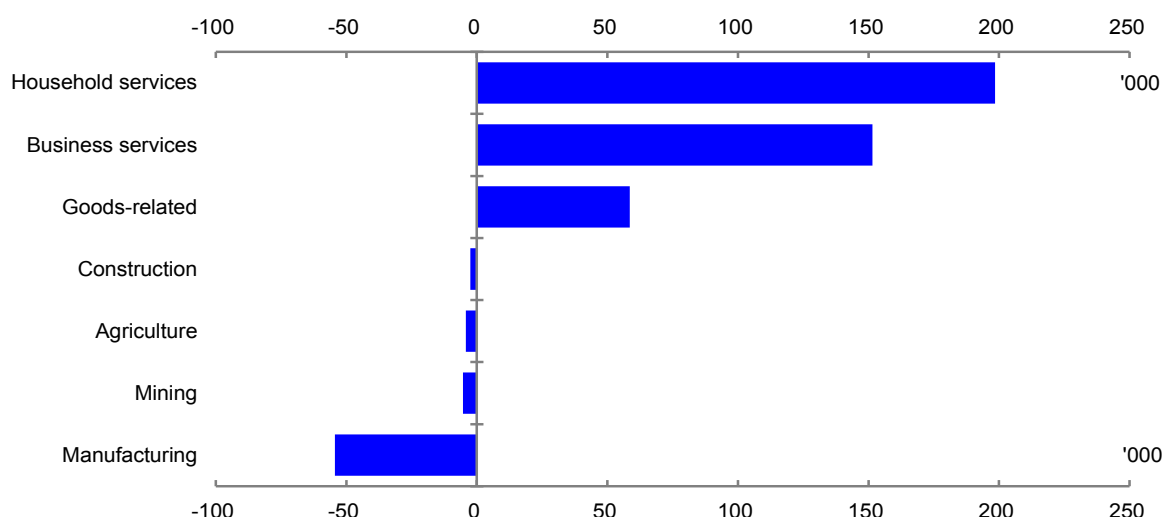
There were almost 300,000 jobs created in 2015, the highest jobs growth in a calendar year since 2007. This led the unemployment rate to fall by 0.5 percentage points to 5.8 per cent over the year to February, despite a 0.3 percentage point increase in the participation rate.

We are growing faster than every economy in the G7, and growing well above the OECD average. We are growing faster than the United States and the United Kingdom, and more than twice the pace of Canada – a comparable resource-rich advanced economy.

We are continuing to benefit from strong commodity export growth that is the result of the largest ever mining investment boom in Australia’s history.

But while the resources sector continues to play an important role in our economy, growth is shifting to more employment-intensive service sectors. The largest employment growth over the past year has come from the household and business services sectors (Chart 1), with the services sector overall accounting for 90 per cent of total jobs growth.

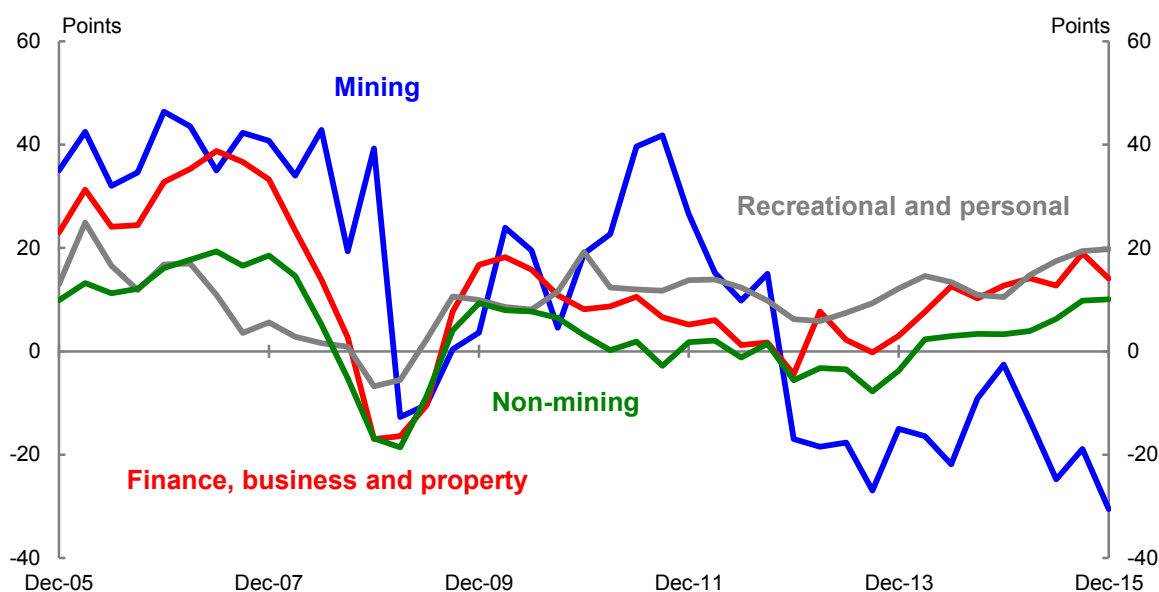
Chart 1: Growth in employment by industry, 2015



Source: ABS Cat. No. 6291.0.55.003

Improving business conditions have supported this job creation. While falling commodity prices are weighing on the mining sector, survey measures of business conditions have been rising across the non-mining economy (Chart 2).

Chart 2: Non-mining business conditions improving



Source: NAB quarterly business survey

Alongside the increase in services employment, an increase in residential construction has provided employment for some workers previously employed in mining-related construction. Residential construction activity has generated demand for a range of business services, including for some services that have experienced a decline in demand from the mining sector, such as engineering and legal services. A buoyant housing market has also supported consumption through expenditure on related items such as household furnishings.

A stronger economy provides our society with more jobs and higher incomes, as well as the opportunity for entrepreneurship and innovation (Box 1).

Box 1: Supporting jobs and growth - innovation package

The Government's \$1.1 billion National Innovation and Science Agenda (NISA) will help to create the modern, dynamic, 21st-century economy Australia needs.

To build prosperity we must encourage innovation and risk-taking, and reward effort. We are moving from the mining boom to an ideas boom.

We need to nourish the 'have a go' attitude that is critical to entrepreneurship and the continued dynamism of a modern economy by driving innovation and technological development.

We need to back the individuals, businesses and organisations generating new products and services that create value. New and improved offerings, products or technologies create new markets, improve efficiency and lead to greater prosperity.

Policy settings in general and the tax system in particular need to encourage and support innovators to create new ideas and promote technological change – not hold them back.

We have to be more agile and more ready to seize the opportunities that we create by increasing innovation activity at home as well as tapping into those on our doorstep in the Asian region. This will help Australia to remain globally competitive.

There is enormous opportunity in our region for Australia’s financial services exports, including through FinTech – or financial technology. That is why the Government is backing Australia’s FinTech community in with real support, such as facilitating crowd-sourced equity funding, improving data availability, and working with regulators to create a facilitative ecosystem.

The Government is serious about taking action to support the growth of this industry. We have established a FinTech Advisory Group to advise us on the important issues facing the industry, and have also announced that we will address the ‘double taxation’ of digital currencies under the GST.

The NISA will incentivise and reward innovation, entrepreneurship and risk-taking.

We are backing Australians to be more innovative and entrepreneurial, to grow the whole ecosystem of innovation right across the economy.

We are backing a culture of embracing risk and encouraging early stage investment in startups by supporting Australians with new business ideas to find the capital they need to develop and commercialise these ideas. This includes tax concessions for early stage investors (a 20 per cent non-refundable carry forward tax offset capped at \$200,000 per investor per year; and a 10 year capital gains tax exemption for investments held for at least twelve months) and for venture capital investment (a 10 per cent non-refundable tax offset for new early stage venture capital investment).

In a vibrant ecosystem of innovation we become more experienced, more inventive, more agile, more prepared to take on risk. We must foster a culture of ideas because it is the ideas boom that will secure our prosperity in the future.

We are backing every single business, large or small to be more innovative, to be more prepared to have a go at something new because in the world of the 21st-century, in 2016, that is how you prosper.

We are seizing the opportunities on our doorstep

Australia's neighbours are growing, and Australia's flexible economy continues to adapt to benefit most from the changing opportunities presented by our region. Our flexible exchange rate is helping the economy through this transition.

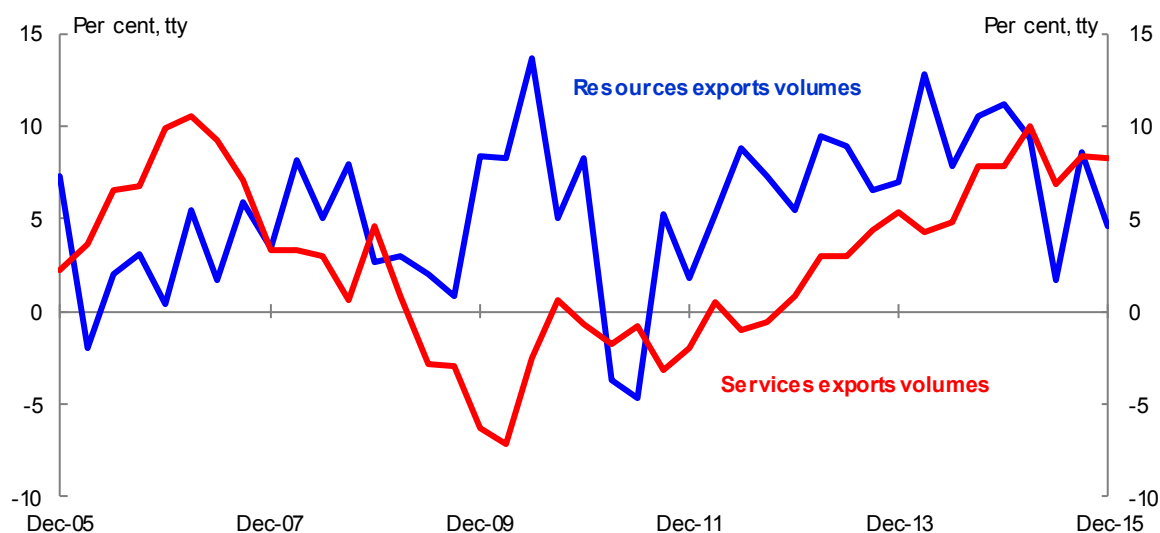
We continue to benefit from growing demand for our natural resources. Record mining investment of over \$700 billion is now translating into an increased production capacity, and the capital stock in the resources sector is now four times higher than before the boom.

Australia is the world's largest exporter of both iron ore and coal. By the end of this decade we expect to overtake Qatar to be the largest exporter of Liquefied Natural Gas. Australia is also one of the world's largest exporters of gold, zinc, nickel and copper.

The resources sector today accounts for around a tenth of our economy, brings in around \$170 billion annually in export earnings, and directly employs more than 226,000 Australians, plus many more in related industries.

But services exports are now also growing strongly, supported by the depreciation in the Australian dollar (Chart 3).

Chart 3: Changing composition of Australian export volumes

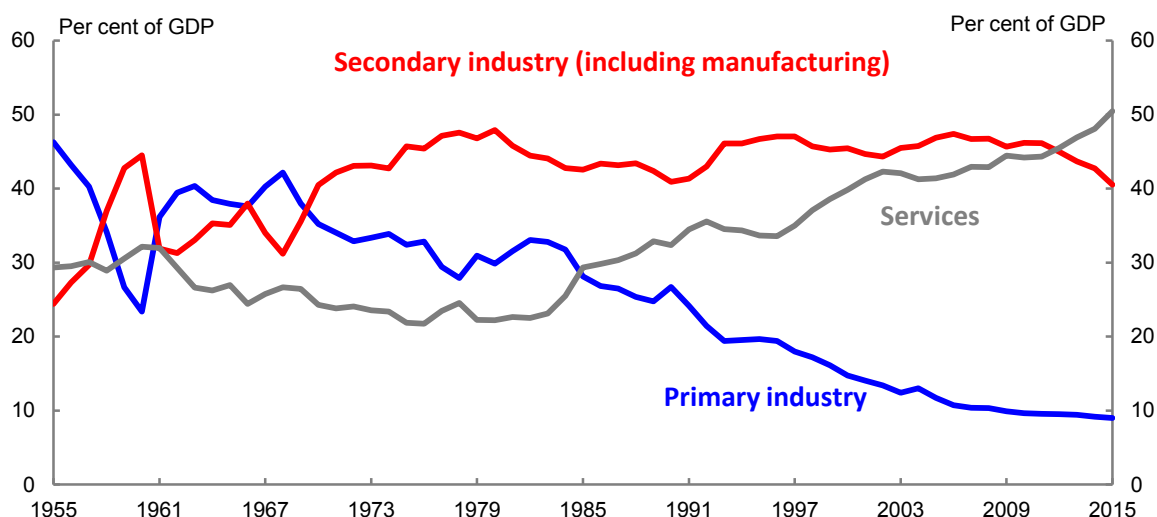


Source: ABS Cat. No. 5302.0.

Net services exports added around 0.5 percentage points to GDP growth in 2015, contributing almost as much as resources exports over the same period.

Just as we are transitioning, many of the economies of our region are experiencing transitions of their own. Rising Asian middle class incomes and shifting preferences are leading to a structural increase in demand for our services (Chart 4).

Chart 4: China's services sector is now the largest sector of its economy



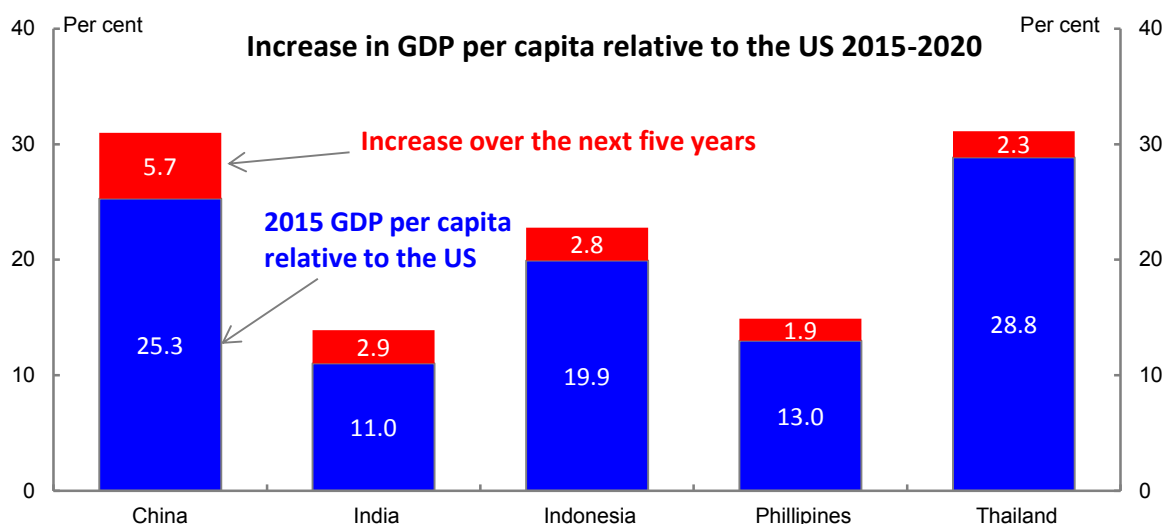
Source: CEIC China database

China is already Australia's largest services market, with services exports valued at \$8.8 billion in 2014–15.

China's economy continues to grow, and growth of just below 7 per cent in China in 2015 was worth well over 14 per cent around seven years ago.

In the next 15 years, China and India will be home to potentially hundreds of millions of new middle class consumers. Some estimates have the Chinese middle class alone growing to over 1 billion people by 2030.

Chart 5: China is growing wealthier

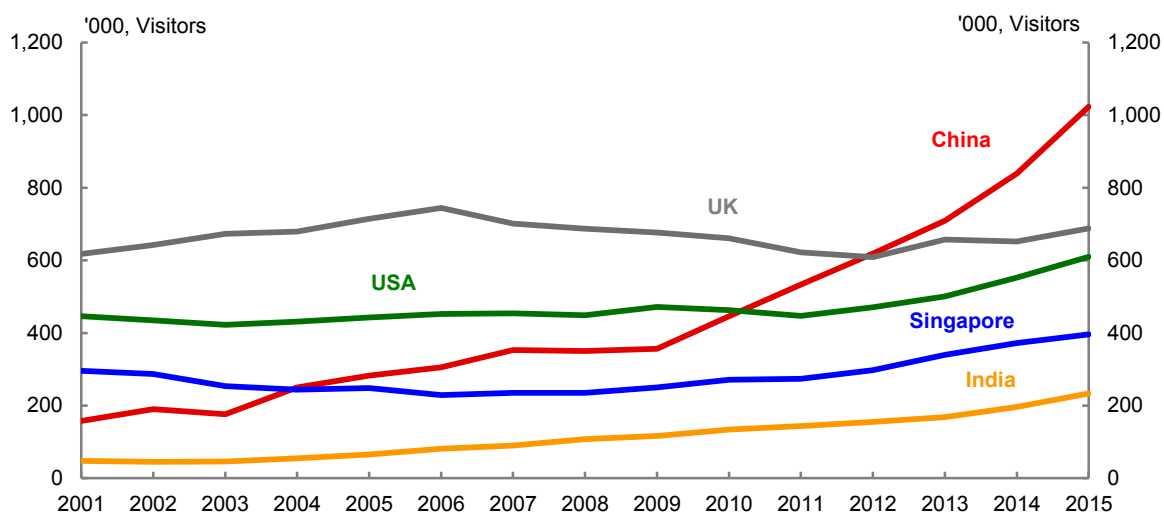


Note: GDP per capita is based on purchasing-power-parity

Source: IMF World Economic Outlook April, 2016.

The number of tourists visiting Australia from China has increased strongly, with the number of tourists exceeding one million for the first time in 2015 (Chart 6), contributing over \$7.7 billion to travel services exports in 2014-15. Future tourism growth is also likely to come from India, as well as other emerging countries in Asia.

Chart 6: Visitor arrivals



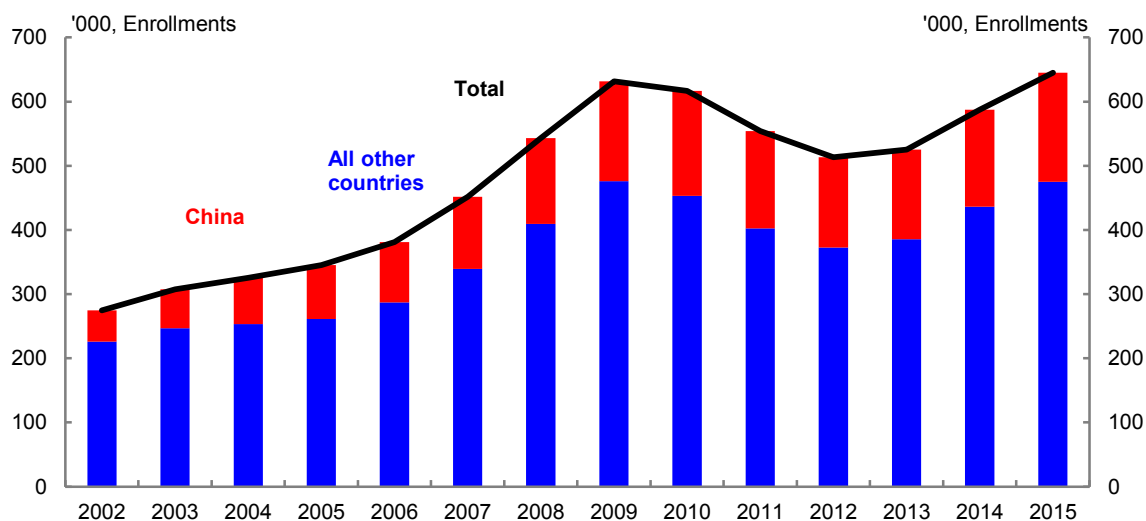
Source: ABS Cat. No. 3401.0.

Note: Original data, annualised.

India was the fastest growing major economy in 2015 and is expected to remain so in 2016. During this century, India will benefit from the largest and youngest workforce in history, with a working age population projected to reach 1 billion by 2030. This demographic dividend will drive growth and expand India's demand for imports, including from Australia.

Australia has experienced strong growth in international student enrolments (Chart 7), with education exports reaching \$17.7 billion in 2014-15.

Chart 7: Foreign student enrolments

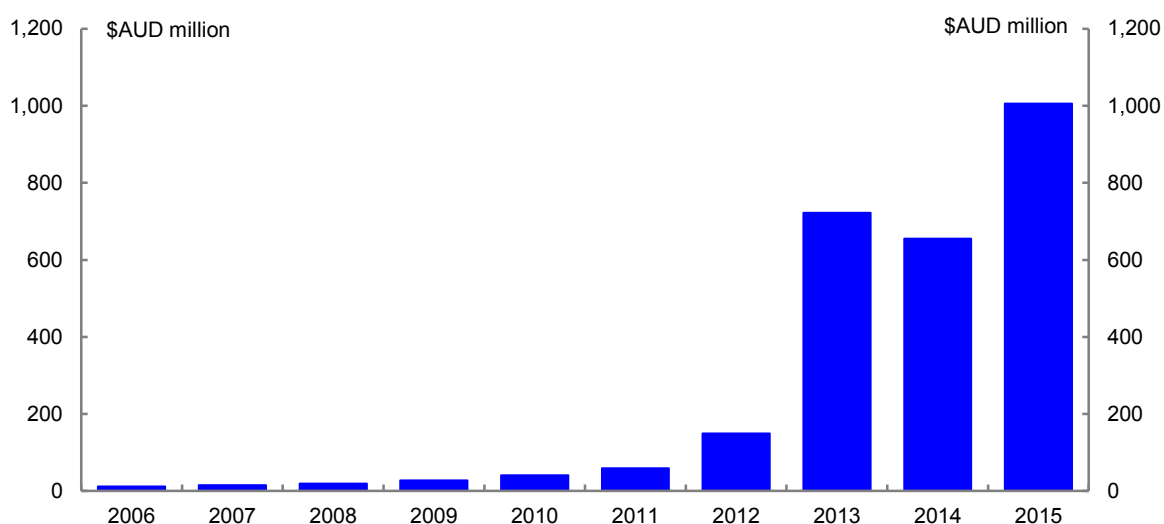


Source: Department of Education.

With rising incomes comes increased demand for high quality meat and produce, creating opportunities for our farmers to capitalise on a growing market. There are significant opportunities for agricultural exports, especially to China as a result of the China Australia Free Trade Agreement.

For example, Australian beef sales to China have surged six-fold in three years to a record \$1 billion (Chart 8). The volume of beef shipped to China rose more than four times over the same period.

Chart 8: Australian beef sales to China



Source: Department of Foreign Affairs and Trade.

The Government’s progress in delivering our ambitious trade agenda will continue to open new markets for Australian exporters (Box 2).

Box 2: Supporting jobs and growth: free trade agreements

Increased trade and investment creates more Australian jobs and delivers more opportunities for Australian businesses.

The Government has established an ambitious trade agenda to push for greater trade liberalisation through bilateral, regional and global trade agreements. This will open new markets for Australian exporters and reduce import costs for Australian businesses and consumers.

The Government has implemented free trade agreements with Korea, Japan and China. We have signed the Trans Pacific Partnership that will integrate twelve economies in the Asia-Pacific region and are pursuing new trade agreements, including with India and the European Union.

These agreements are an important part of the Government's strategy to support the diversification of our economy in the post mining boom phase. They will create opportunities for Australian exporters and investors to expand their business into key overseas markets, help attract much-needed investment and strengthen economic linkages with key overseas countries and regions.

Free trade agreements also increase Australia's productivity and contribute to higher growth by allowing domestic businesses access to cheaper inputs, introducing new technologies, and fostering competition and innovation.

Importantly, reductions in trade barriers also help boost the competitiveness of Australian exports in the services sector. For example, the China Australia Free Trade Agreement that came into force on 20 December 2015 makes it easier for Australian businesses to operate and expand in the growing Chinese market by securing or improving access for Australian services providers in China.

Beneficiaries include Australian banks, insurers, securities and futures companies, law firms and professional services suppliers, and education services exporters, as well as health, aged care, construction, manufacturing and telecommunications services businesses in China.

Modelling commissioned by the Department of Foreign Affairs and Trade indicates that goods and services liberalisation under the three North Asia free trade agreements is expected to raise Australia's GDP by \$24.4 billion by 2035. Real wages are also expected to increase by up to 0.5 per cent over the same period.

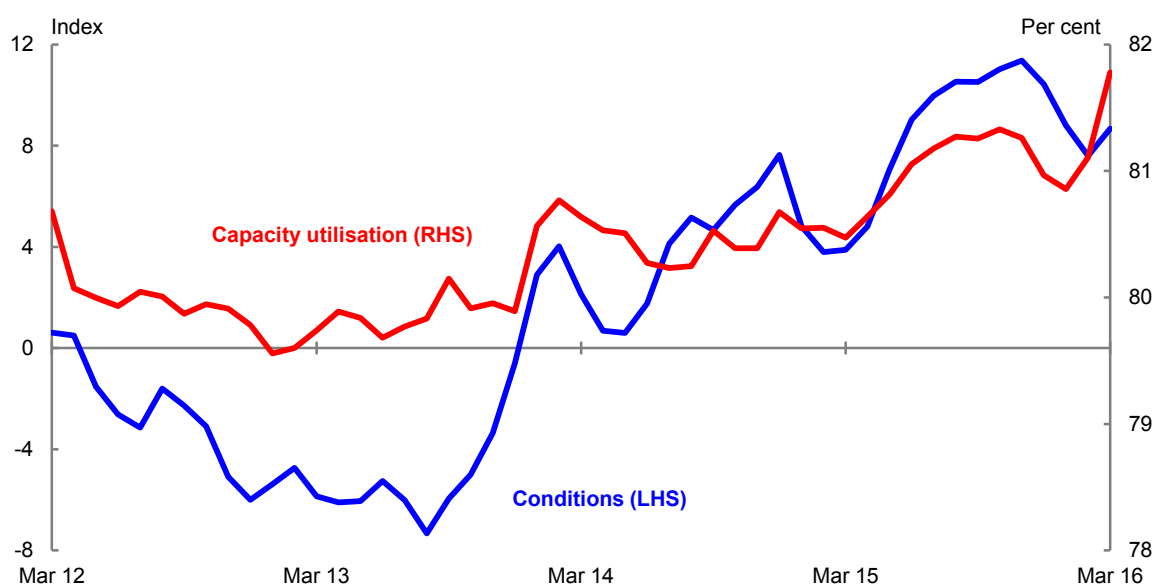
Our economy is supporting Australians to work, save and invest

As growth in domestic demand and exports gather pace, Australian businesses will have more opportunities to invest and expand, further accelerating Australia's transition to broader-based growth.

Although growth in non-mining investment remains subdued to date, the conditions are in place for businesses in the non-resources sectors of the economy to increase their investment.

There are many factors currently supporting a recovery in non-mining investment, including record low interest rates, the depreciation of the exchange rate, a sustained lift in business conditions and rising utilisation of existing capital (Chart 9).

Chart 9: Non-mining business conditions and capacity utilisation



Source: NAB Monthly Business Survey and Treasury.

Note: Three-month moving average.

As these developments translate into increasing profits they will support increased capital spending and employment in the future.

When demand increases many businesses first look to increase employment and hours. This initial activity can be expected to be followed by investments in fixed capital. Investment plans may initially be limited to the replacement of old capital until firms in fast growing sectors such as tourism and healthcare invest to expand.

In this regard non-mining investment can be seen as a lag indicator, as businesses first adjust to stronger demand before making decisions to invest, which will be assisted by historically low interest rates to fully realise the growth opportunities.

The latest ABS investment survey showed that in the December quarter investment by services industries increased strongly by 12.4 per cent in the quarter.

That said, with more economic growth coming from the services sectors, going forward we may require less capital investment, but higher employment growth, to continue our economic expansion.

We need to do all that we can during this critical phase of rebalancing in the economy to encourage non-mining investment and to support activity in the sectors of our economy that will underpin our continued growth and prosperity.

The Government is supporting record levels of infrastructure investment through its \$50 billion infrastructure package announced in the 2014-15 Budget, increasing the economy's productive capacity, generating jobs and expanding business and labour market opportunities (Box 3).

Box 3: Supporting jobs and growth: investing in productive infrastructure

Our future prosperity depends on getting the right infrastructure in place. The Government is implementing a \$50 billion national infrastructure plan to unlock our productive capacity, generate jobs, and expand business and labour market opportunities. To support this plan, the Government has reformed Infrastructure Australia to improve decision-making on infrastructure projects and ensure taxpayers' money is spent on projects that return the greatest productivity improvement.

A key part of the infrastructure plan is the Asset Recycling Initiative.

The first agreement under the Initiative was signed with the Australian Capital Territory in February 2015 and the second with New South Wales in March 2015.

The efficiency gains through privatisation of the New South Wales electricity network will place downward pressure on electricity prices, with the proceeds from the sale to fund new productivity-enhancing infrastructure.

That is a great example of the type of innovative policies which this Government is encouraging through the Asset Recycling Initiative.

We have also established a \$5 billion Northern Australia Infrastructure Facility to provide concessional financing to catalyse the development of major projects in the North.

The Government has announced that Badgerys Creek will be the site for a Western Sydney Airport.

A new airport would be a major generator of economic activity, providing employment opportunities closer to where people in Western Sydney live.

This Government will support our economy, and the Australian people, to successfully and prosperously make this transition

As a government, we are keenly focussed on the policies that will boost investor confidence and drive productivity gains in our economy, particularly through encouraging innovation, opening up new markets through our successful and ambitious trade agenda, investing in productive infrastructure, and continuing on our path of fiscal consolidation.

There is a pragmatic realism to our optimism about our economic future in this country. We are not naïve about the uncertainty and volatility in global economic conditions, nor the need for our economy to transition and diversify, post the mining boom. We back ourselves, as a Government and the Australian people, to successfully and prosperously make this transition.