Overview

Resources and Energy Quarterly September 2018

Resources and energy sector

- 9% of Australia's GDP growth in the June quarter 2018
- 8% of GDP in 2017–18
- 57% of Australia's goods and services exports in 2017–18
- 246,000 people employed (as at August 2018)

Australia’s resources and energy exports, A$ billion

- 2017–18:
  - Iron ore: $56b
  - Met Coal: $48b
  - Others: $41b
  - LNG: $31b
  - Thermal coal: $24b
  - Base metals: $20b
  - Gold: $19b

- 2018–19:
  - Iron ore: $56b
  - Met Coal: $48b
  - Others: $41b
  - LNG: $31b
  - Thermal coal: $24b
  - Base metals: $20b
  - Gold: $19b

- 2019–20:
  - Iron ore: $56b
  - Met Coal: $48b
  - Others: $41b
  - LNG: $31b
  - Thermal coal: $24b
  - Base metals: $20b
  - Gold: $19b

Major markets for Australia’s resources and energy exports, 2017–18 (A$ billion)

- EU28: 10
- India: 13
- South Korea: 18
- Japan: 41
- China: 85
1.1 Summary

- Australia’s resources and energy export volumes are expected to show firm growth over the outlook period. While the prices of Australia’s major resource commodities have generally been rising, we expect them to decline in 2019–20 because of moderating demand and rising supply.
- Helped by the decline in the Australian dollar over the past quarter, Australia’s resource and energy exports are likely to hit a new record high of $252 billion in 2018–19, but fall back to $238 billion in 2019–20.
- While global economic growth, industrial production and manufacturing output have continued to grow strongly so far in 2018, there are some concerning signs for resource and energy commodity producers, particularly with rising global trade tensions.

1.2 Export values

Australia’s export values to a quarter of a trillion dollars in 2018–19

The Office of the Chief Economist’s (OCE) Resources and Energy Export Values Index (preliminary estimate) rose by 22 per cent in the year to the September quarter 2018. This was due to a 17 per cent rise in prices and a 5 per cent rise in volumes. Figure 1.2 shows that in 2018–19, a forecast 4.4 per cent rise in prices will add to the impact of a 7.1 per cent rise in export volumes. The value of resource and energy exports is thus forecast to rise by 11.8 per cent to a record $252 billion. 2019–20 is forecast to see export values drop by 5.6 per cent to $238 billion, as a 9.2 per cent fall in prices more than offsets the impact of a 4.0 per cent rise in volumes.

The weaker AUD/USD has added significantly to commodity returns

In Australian dollar terms, the Office of the Chief Economist’s Resources and Energy Commodity Price Index grew by 4.4 per cent (preliminary estimate) in the September quarter, to be 17.0 per cent higher than a year earlier. In US dollar terms, the Index grew by 2.2 per cent in the quarter, to be 9.7 per cent higher than a year earlier. Figure 1.3 shows that prices for resources commodities rose by 2.2 per cent, while prices of energy commodities grew by 7.2 per cent in the quarter in Australian dollar terms.

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**Figure 1.1: Australia’s resource and energy export values/volumes**


**Figure 1.2: Annual growth in Australia’s resources and energy export values, contributions from prices and volumes**

Figure 1.3: Resource and energy export prices, AUD terms

Notes: The export price index is based on Australian dollar export unit values (EUVs, export values divided by volumes); the export price index is a Fisher Price Index, which weights each commodity’s EUV by its share of total export values.


1.3 Macroeconomic and trade war influences

The global macroeconomic outlook is not as benign as it has been for the past year at least, clouding the resource and energy commodity outlook slightly. Leading indicators of industrial activity, including Purchasing Managers’ Indices and base metal prices, point to slower growth ahead; US trade moves are impacting on global supply chains and have raised uncertainty, which is starting to impact on investment in some countries. US monetary conditions are set to tighten further, as US inflation rises.

US inflation is rising as the recent corporate and income tax cuts push the economy near capacity limits; increased tariffs on US imports may also raise consumer prices. Widening interest rate differentials and the US trade protection measures have helped push the US dollar higher. While the stronger US dollar lessens some US inflation pressures, it is also putting a strain on countries such as Turkey, Argentina, South Africa and Indonesia, as capital flows out of these nations to the US. South Africa, Indonesia and other emerging nations account for an inordinate amount of growth in resource commodity consumption, as they attempt to grow and develop.

US dollar gains have contributed to weakness in resource commodity prices, especially base and precious metals. While the overwhelming majority of Chinese steel output is consumed domestically, base metal and gold demand are much more susceptible to the impacts of trade wars impacting on Asia. Gold would normally benefit from safe-haven flows induced by heightened economic/financial market uncertainty, however investors in emerging markets may be liquidating gold to shore up losses elsewhere. Investors have sold gold as the US dollar has risen and as real US bond yields held their March quarter 2018 gains.

The impact of US Administration trade moves — to protect some domestic industries from imports and try to force its trading partners to lower barriers to US exports — and growing retaliatory moves by affected nations, has yet to show up meaningfully in trade and economic activity statistics. Making interpretation even more difficult, detailed Chinese trade data post March 2018 has not been released by China’s official statisticians. The main US trade moves have been against China, but Mexico, the EU, Canada and Turkey have also been hit by significant protective measures. It could be expected that unless the new US trade barriers are reduced or abolished, there will be a significant impact on world economic growth — and hence commodity usage — over the forecast period. If recent US trade measures do succeed in trading partners such as China lowering/removing trade and investment barriers, the main benefits will be in non-commodity sectors.

The impact of winter production cuts in China continues to change the pattern of consumption of inputs to ferrous and non-ferrous metal production, making interpretation of the underlying conditions in resource and energy markets much more difficult. Strong summer Chinese steel production drew in high imports of iron ore and metallurgical coal; steel inventories will build eventually — causing steel prices to fall and harm the demand for imported iron ore and metallurgical coal — but extremely strong inventory gains are not expected in the forecast period.
Chinese economic growth appears likely to show only minor change from its current pace, as trade war impacts are offset by a recent sharp fall in the Chinese currency, cuts to bank reserve requirements and a government-supported infrastructure push.

The rest of the world is still growing slightly above trend, and low inflation in all major economies except the US continues to provide scope for easy monetary conditions to continue.

1.4 Prices

The iron ore price has been supported by the ongoing strength in China’s steel market. The iron ore price is forecast to decline modestly over the next two years, as Chinese steel output eases and world supply grows.

Metallurgical coal spot prices stabilised in the September quarter, after sharp falls in the June quarter. Some ongoing near-term price support is expected: China’s imports of metallurgical coal are expected to remain elevated over the next couple of months, as steel margins remain high.

Australian thermal coal prices have been unexpectedly strong. Their strength is partly related to strong Chinese imports — as a hot summer raised Chinese power demand — and partly related to an ongoing air-quality push for high quality coal in Asia. Prices are expected to ease through the December quarter 2018 and through 2019, as supply rebounds and demand moderates.

Oil prices have held much of the gains of the June quarter, which are set to flow through to LNG revenues over the December quarter. With oil prices expected to hold near current levels over the outlook period, Australia’s growing oil, condensate and LNG volumes should result in petroleum and LNG revenues holding at relatively high levels.

The gold price recently drifted below the US$1,200 an ounce mark for the first time since January 2017 — when US dollar strength associated with the beginning of the Trump Administration weakened the yellow metal. A rebound is expected when the US dollar finishes its rise some time in 2019.
1.5 Export volumes

Export volumes to grow, driven by growing energy exports

The 4.7 per cent year-on-year gain in the Office of the Chief Economist’s Resources and Energy Export Volumes Index (preliminary estimate) in the September quarter 2018 took the index to a new record high. Resource commodity volumes rose by 5.5 percent, and energy commodity volumes rose by 3.5 per cent.

Iron ore, zinc and copper supported annual growth in overall resources and energy export volumes in the September quarter. Growth in iron ore exports is forecast to be 1.4 per cent in 2018–19, before moderating to 0.9 per cent in 2019–20. Rio Tinto and BHP continue to ramp up towards record output levels. BHP is expected to lift capacity at its Port Hedland operations, with output forecast to reach 290 million tonnes by mid-2019.

1.6 Contribution and investment

Mining industry continues to support overall economic growth

Australia’s real Gross Domestic Product (GDP) grew by 0.9 per cent in the June quarter 2018. The mining industry directly accounted for 9.0 per cent of the growth in Australia’s GDP in the year to the June quarter. Since the start of the commodity boom, swings in resource and energy export earnings have correlated closely with swings in nominal GDP. Figure 1.6 suggests that with growth in resource and energy exports likely having peaked in late 2018, nominal GDP growth may have done the same.

Oil and gas extraction and iron ore mining have been the largest contributors to mining industry value-added growth in the last few years, propelled by growing export volumes. In the coming few years, it is likely that slowing export growth and relatively low investment will see a smaller contribution to Australia’s GDP growth from the oil and gas sector.

Coal mining made its strongest contribution to growth in more than three years in the June quarter 2018. The Australian coal industry is reacting to high prices, and has had fewer weather, transport and industrial disruptions than in 2016–17.
Coal mining investment has been largely stable in recent times, easing by 2 per cent in the June quarter, to be 3 per cent higher through the year. Growth in investment remains largely confined to the metal ore sector, where investment rose by a strong 19 per cent in the quarter and 14 per cent through the year. This follows a recent surge in prices for copper, nickel, zinc, and lithium.

1.7 Revisions to the outlook

The outlook for Australia’s resources and energy export earnings in 2018–19 has been revised up by around $13.7 billion from the June 2018 Resources and Energy Quarterly. The weaker AUD/USD factored into our forecasts is estimated to add $10.6 billion to export values, while higher-than-expected thermal coal and LNG prices account for the rest of the forecast gain. The forecast for Australia’s resources and energy export earnings in 2019–20 has been revised up by $5.9 billion, reflecting both a larger than previously forecast rise in energy prices and a slightly weaker outlook for the AUD-USD exchange rate in the latter half of 2019.
Figure 1.10: Australia’s major resource & energy commodity exports

Notes: per cent change is compound annual growth (CAGR) from 2017–18 to the specified year; f forecast.

Table 1.1: Outlook for Australia’s resources and energy exports

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<tr>
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<th></th>
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</thead>
<tbody>
<tr>
<td><strong>Resources and energy</strong></td>
<td>A$m</td>
<td>204,130</td>
<td>226,737</td>
<td>251,893</td>
<td>238,369</td>
<td>11.1</td>
</tr>
<tr>
<td>– realb</td>
<td>A$m</td>
<td>212,854</td>
<td>231,952</td>
<td>251,893</td>
<td>232,724</td>
<td>9.0</td>
</tr>
<tr>
<td><strong>Energy</strong></td>
<td>A$m</td>
<td>85,328</td>
<td>101,846</td>
<td>124,896</td>
<td>114,553</td>
<td>19.4</td>
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<tr>
<td>– realb</td>
<td>A$m</td>
<td>88,974</td>
<td>104,188</td>
<td>124,896</td>
<td>111,841</td>
<td>17.1</td>
</tr>
<tr>
<td><strong>Resources</strong></td>
<td>A$m</td>
<td>118,802</td>
<td>124,891</td>
<td>126,998</td>
<td>123,815</td>
<td>5.1</td>
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<tr>
<td>– realb</td>
<td>A$m</td>
<td>123,879</td>
<td>127,764</td>
<td>126,998</td>
<td>120,884</td>
<td>3.1</td>
</tr>
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</table>

Notes: b In 2018–19 Australian dollars. f forecast.

Table 1.2: Australia’s resources and energy commodity exports, selected commodities

<table>
<thead>
<tr>
<th></th>
<th>Volume</th>
<th>Value</th>
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<tbody>
<tr>
<td><strong>Alumina</strong></td>
<td>kt</td>
<td>17,746</td>
</tr>
<tr>
<td><strong>Aluminium</strong></td>
<td>kt</td>
<td>1,431</td>
</tr>
<tr>
<td><strong>Copper</strong></td>
<td>kt</td>
<td>892</td>
</tr>
<tr>
<td><strong>Gold</strong></td>
<td>t</td>
<td>348</td>
</tr>
<tr>
<td><strong>Iron ore</strong></td>
<td>Mt</td>
<td>849</td>
</tr>
<tr>
<td><strong>Nickel</strong></td>
<td>kt</td>
<td>191</td>
</tr>
<tr>
<td><strong>Zinc</strong></td>
<td>kt</td>
<td>1,165</td>
</tr>
<tr>
<td><strong>LNG</strong></td>
<td>Mt</td>
<td>62</td>
</tr>
<tr>
<td><strong>Metallurgical coal</strong></td>
<td>Mt</td>
<td>179</td>
</tr>
<tr>
<td><strong>Thermal coal</strong></td>
<td>Mt</td>
<td>203</td>
</tr>
<tr>
<td><strong>Oil</strong></td>
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</tr>
<tr>
<td><strong>Uranium</strong></td>
<td>t</td>
<td>7,684</td>
</tr>
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</table>

Notes: f forecast. CAGR is compound annual growth rate in percentage terms from 2017–18 to 2019–20