

1. The International Environment

Global economic developments continue to be influenced by the US–China trade and technology disputes. The associated increase in policy uncertainty has weighed on global trade, investment and manufacturing activity, although consumption growth has been relatively resilient (Graph 1.1). As a result, major trading partner growth has slowed a little further, and is expected to remain around its recent pace over the next two years. There are more signs that the slowing in export-oriented sectors is spilling over to the service sectors. Employment growth in the major advanced economies remains above growth in working-age population, but has eased recently; overall, labour market conditions still remain tight.

Financial market conditions remain accommodative. Several major central banks have eased monetary policy further in response to slowing growth, downside risks and subdued inflation. Yields on government and corporate bonds are around historic lows in many

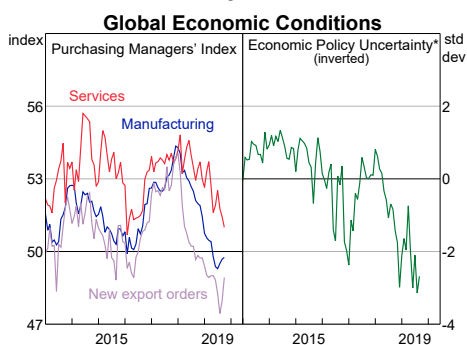
countries. Global equity prices have risen, and are near record highs in the United States. Measures of financial market volatility are generally below long-term averages. Financial conditions in emerging market economies have also eased a little. The combination of low volatility, low bond yields and buoyant prices of riskier assets suggests that market participants continue to expect that the policy stimulus that has been delivered by central banks will sustain the global economic expansion.

Trade and technology disputes have escalated ...

The US–China trade and technology disputes have escalated further since August with both countries raising tariff rates. As a result, the average tariff rates between the two countries have increased substantially to around 20 per cent, which has now fully reversed the earlier decline in tariff rates since the early 1990s (Graph 1.2).

Nevertheless, tensions have eased a little more recently: negotiations have resumed and a preliminary partial agreement was reached in October that has postponed some of the scheduled tariff increases. Even so, the prospects for a comprehensive trade agreement are uncertain and there is a risk of further escalation. The US administration is still set to impose a 15 per cent tariff on almost all remaining imports from China from mid December and China has threatened further tariff increases in response.

Graph 1.1



* Standard deviation from 2014 to 2018 average
Sources: Markit; RBA; www.policyuncertainty.com

Other trade tensions have emerged, with some countries using trade policy to address broader political disputes; this includes Japan and South Korea, which have restricted their bilateral trade in some strategic products, including certain key semiconductor materials. A decision by the United States about increasing tariffs on automotive imports from a number of countries is due in November.

... lowering the growth outlook and increasing downside risks

Major trading partner growth is expected to be around 3½ per cent in 2019 and 2020, before increasing a little in 2021 (Graph 1.3). This is a little lower than forecast in the *August Statement on Monetary Policy* because of the escalation in the US–China trade and technology disputes, a further weakening in business investment indicators and growing signs of spillovers to service sectors and labour markets. The outlook for 2019 and 2020 has been revised down successively since late last year and the cumulative downward revisions to trading partner growth have amounted to around ¼–½ percentage point. Growth appears to have slowed by more than earlier expected because the protracted nature of the US–China disputes has raised policy uncertainty and weighed on investment by more than was initially anticipated. While monetary policy has become

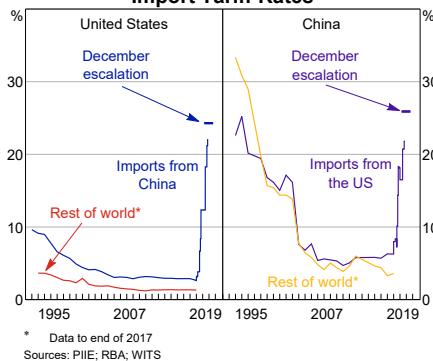
more accommodative across a range of economies, fiscal policy in the advanced economies has been broadly neutral this year and is expected to remain so next year.

While the outlook is for moderate global growth, downside risks remain. There is a high degree of uncertainty about the future evolution of the US trade disputes with China and other economies; further escalations pose significant downside risks and, conversely, resolutions of the disputes, even if partial, would support global growth. There is also a risk that the spillovers to service sectors and labour markets could be larger than expected. The form and timing of the United Kingdom's exit from the European Union (Brexit) remains a key additional source of uncertainty about the outlook for Europe.

A key question for the outlook for the Australian economy is how the global risks play out, particularly for China and how their policy response could affect China's demand for Australian exports. To date, Chinese policies to support their economy have been relatively steel intensive and have increased demand for bulk commodities from Australia. More broadly, the resolution of global risks and policy responses to their effects, including the recent decisions to ease monetary policy in a number of economies, could also affect the exchange rate and commodity prices, both of which affect domestic activity and inflation in Australia. Any indirect effects on businesses' investment intentions could also be a factor for the domestic growth forecasts.

Graph 1.2

Import Tariff Rates



In China, activity indicators continued to moderate

In China, economic conditions eased in the September quarter, driven by slower growth in domestic demand. So far, the US–China trade and technology disputes have had a limited effect on overall economic activity in China. Tariffs imposed to date have led to a material decline in exports to the United States, but

exports to other destinations have been broadly stable, and targeted monetary and fiscal easing has partly offset the effect of weaker exports by boosting domestic expenditure. Nonetheless, the associated uncertainty is likely to be affecting business decisions and thus contributing to medium-term downward pressures on growth.

In the September quarter, growth in activity indicators was mixed (Graph 1.4). Growth in retail sales declined, reflecting weakness in car sales, while growth in fixed asset investment increased a little. Infrastructure investment rebounded, reflecting measures taken by the authorities to support public spending on transportation and energy infrastructure projects, while growth in manufacturing investment eased.

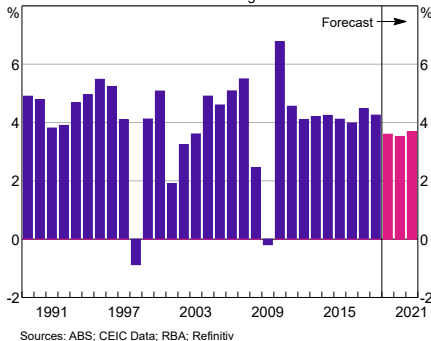
Industrial sector indicators have remained subdued in recent months: growth in the output of industrial products increased slightly, but falling producer prices have weighed on industrial profits. The output of construction materials has remained elevated, supported by growth in construction-related demand (Graph 1.5). Steel production moderated slightly in September, but remains high, reinforced by recent falls in bulk commodity prices that have supported steel producers' margins.

Conditions in Chinese property markets continued to be mixed in the September quarter (Graph 1.6). Official measures of property prices suggest that growth has moderated in recent months, while non-official measures continue to indicate notably weaker price growth. Property sales were little changed in the quarter, but spending on construction and fittings increased. The authorities increased their scrutiny of real estate financing and reaffirmed their commitment that real estate will not be used to stimulate the economy in the short term.

Producer prices declined in the quarter to be around 1 per cent lower over the past year, driven by falling prices for raw materials and

Graph 1.3

Australia's Major Trading Partner Growth
Year-average



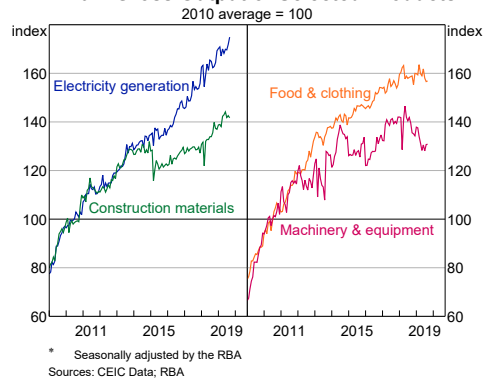
Graph 1.4

China – Activity Indicators*



Graph 1.5

China – Gross Output of Selected Products*



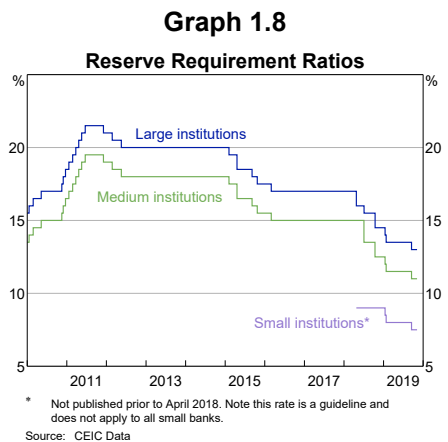
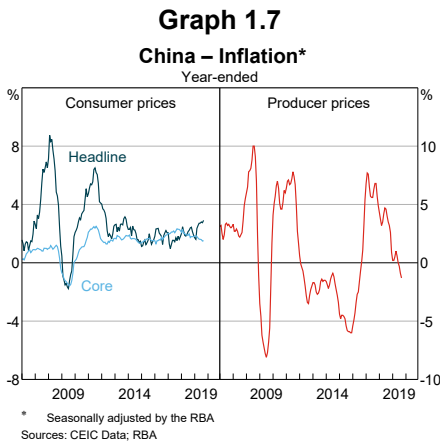
manufactured goods (Graph 1.7). Core consumer price inflation also continued to ease. Headline inflation increased slightly as a large rise in pork prices – a result of continued supply shortages caused by the African swine fever outbreak – was largely offset by lower inflation for other food and non-food items.

Chinese authorities have responded with further targeted policy easing

Chinese policymakers have announced additional targeted measures to support economic growth and the health of smaller banks, which have encountered liquidity pressures in recent months and are important

providers of financing to micro and small-sized enterprises. Since September, the People’s Bank of China (PBC) has reduced reserve requirement ratios (RRRs) by 50 basis points for all financial institutions and by an additional 100 basis points for a subset of smaller banks (Graph 1.8). The PBC estimates that the lower RRRs will inject an additional CNY900 billion of liquidity into the banking system (around 1 per cent of GDP). Also, the interest rate on the PBC’s medium term lending facility – that provides funding to banks – has declined by 5 basis points. In addition, the PBC has announced reforms to benchmark lending rates to improve the transmission of monetary policy (see Box A: Recent Reforms to Lending Rates in China). Following earlier policy easing, growth in total social financing has stabilised, reflecting steady bank credit growth, a pick-up in the growth of securities financing and a slowing in the contraction of off-balance sheet financing (Graph 1.9).

In August, the State Council announced a package of policies to boost consumption, which included measures to ease restrictions on car purchases, extend retail hours and encourage financial institutions to provide credit to consumers purchasing green energy products. Similar to last year, local governments will be allocated a portion of their 2020 special bond issuance quota before they are formally



approved by the National People’s Congress in March, which should help to support infrastructure spending. The authorities have emphasised that recent policy easing measures are not intended to stimulate the real estate sector.

Economic activity has slowed in most of the major advanced economies amid ongoing policy uncertainty

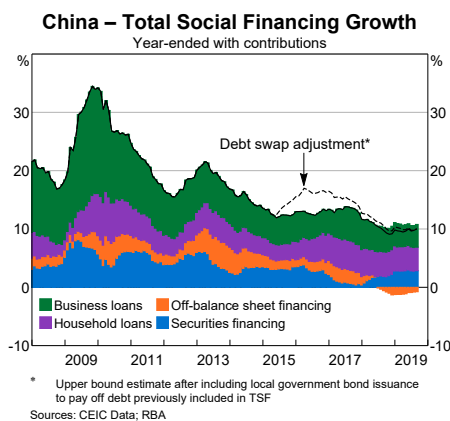
Growth in the major advanced economies was strong over 2017 and the first half of 2018, but has eased since then due to weaker investment in the United States and the euro area (Graph 1.10). Investment decisions in these economies have been affected by the increase in policy uncertainty and weaker external demand, particularly from China. Manufacturing activity in the major advanced economies has slowed sharply and the weakening in conditions appears to have been spreading to the service sectors recently. However, consumption growth has been resilient, aided by strong employment growth. Labour market conditions remain strong but there have been signs of easing recently. In particular, employment growth and forward-looking indicators of labour demand have slowed; further slowing in employment growth presents a downside risk to the growth outlook, particularly as it would suggest a lower

trajectory for both wages and incomes growth, with feedthrough into consumption growth. Monetary policy has become more accommodative, supporting growth, but fiscal policy has been largely neutral.

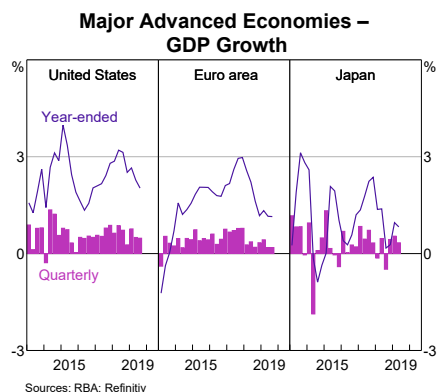
In the United States, GDP growth has slowed to around trend this year. This is largely because business investment growth has eased, due to the trade dispute and the waning effects of the 2018 tax cuts. Investment intentions declined further in the September quarter (Graph 1.11). Manufacturing activity has declined since mid 2018, while conditions in service sectors have eased more recently, to around average. Meanwhile, consumption growth has remained resilient and dwelling investment contributed to growth in the September quarter (Graph 1.12). The growth outlook for the United States for 2019 and 2020 has been lowered slightly reflecting a somewhat weaker business investment outlook, the further escalation in the US–China disputes over recent months and some expected moderation in consumption growth.

Growth has slowed significantly in the euro area since early 2018 to a little below trend pace. Growth remained subdued in the September quarter, driven by further weakness in exports and investment. Weak external demand has weighed on production in the manufacturing

Graph 1.9



Graph 1.10



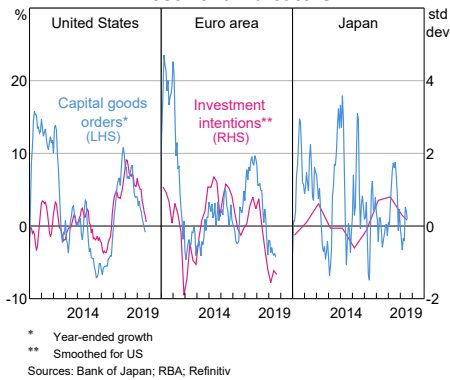
sector. Production in the German automotive industry has been particularly weak; it stalled after new emission testing standards were introduced last year and has not recovered since. Weak export growth to the United Kingdom has added to the subdued conditions given that the United Kingdom is the second largest destination for euro area exports. Investment growth has slowed and measures of investment intentions point to investment growth remaining subdued. There are signs that the weakness is spreading to the service sectors. In the United Kingdom, economic activity, particularly investment, has slowed since

2016 and survey measures of business activity and investment intentions are around their lowest in a decade (Graph 1.13). Private consumption in the euro area and the United Kingdom has remained resilient, consistent with the still tight labour markets. Euro area growth is expected to remain below trend next year due to subdued external demand and a modest easing in consumption growth, while the outlook for the United Kingdom remains dependent on the resolution of the Brexit uncertainty.

In Japan, growth in the middle of this year was supported by a frontloading of consumption ahead of the consumption tax increase in October. However, external demand, particularly from Asia, has been weak, which has been reflected in a substantial easing in conditions in the manufacturing sector. Aggregate investment and investment intentions remain relatively strong, partly because labour shortages are prompting investment in labour-saving equipment. Growth is expected to slow in late 2019 and early 2020 to be below trend because of persistent weakness in external demand, tighter fiscal policy following the consumption tax increase, and the resulting slower consumption growth.

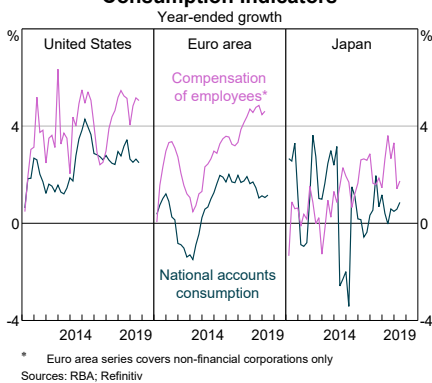
Graph 1.11

Major Advanced Economies – Investment Indicators



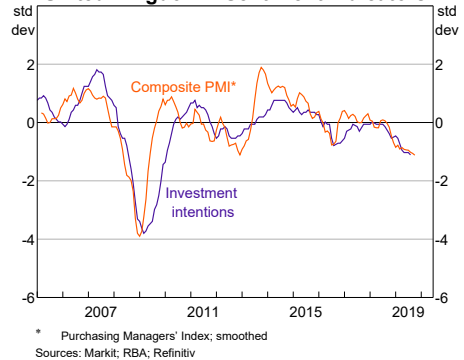
Graph 1.12

Major Advanced Economies – Consumption Indicators



Graph 1.13

United Kingdom – Sentiment Indicators



Labour market conditions are still tight although they have eased a little

Employment growth has remained above working-age population growth, unemployment rates have declined further and wages growth has remained around its recent high pace. However, there are signs that labour market conditions have started to ease in major advanced economies following the slowing in GDP growth. The slowing in employment has been particularly evident in the manufacturing sector (Graph 1.14). More recently, employment growth in the service sectors has also softened in some economies. Vacancy rates and survey-based measures of firms' employment intentions have plateaued, consistent with labour market conditions not tightening further (Graph 1.15). In the United Kingdom, employment growth had been relatively resilient but it has eased recently.

Inflation remains low in the major advanced economies

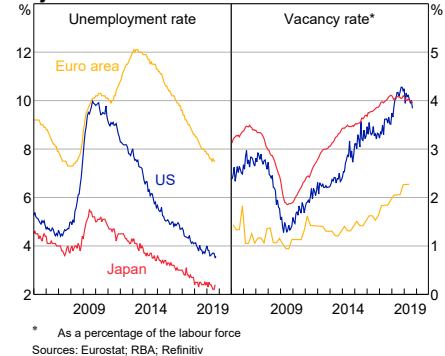
Inflation is below target in the major advanced economies, albeit to varying degrees (Graph 1.16). Core inflation in the euro area and Japan has been little changed in recent months and remains low; inflation in Japan is expected to increase temporarily by up to 0.5 percentage points in year-ended terms following the

consumption tax increase. Over the past six months, the US Federal Reserve's (Fed's) preferred measure of core inflation, in annualised terms, has been around the target of 2 per cent for headline inflation; the increase in US core goods inflation this year is likely to have reflected, in part, the effect of the higher tariffs on imports from China.

Market-implied measures of long-term inflation expectations have declined this year, particularly in the euro area, where they are the lowest in a decade. In contrast, economists' long-term inflation expectations (as reflected in survey data) have been stable around 2 per cent in the United States and euro area, and short-term

Graph 1.15

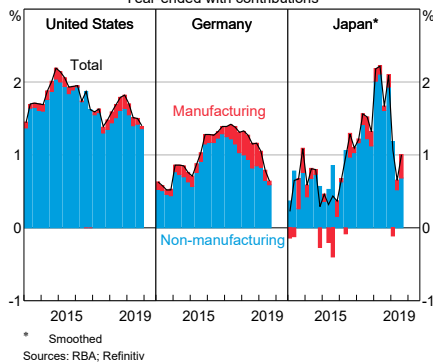
Major Advanced Economies – Labour Market



Graph 1.14

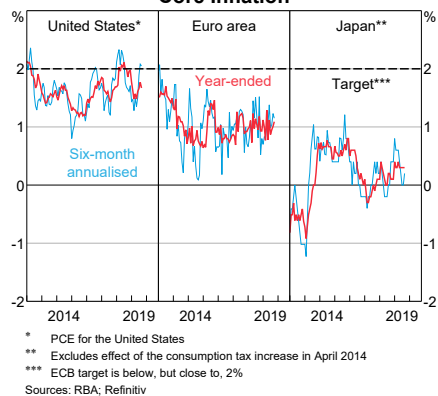
Advanced Economies – Employment Growth

Year-ended with contributions



Graph 1.16

Major Advanced Economies – Core Inflation



consumer inflation expectations have increased in the United States and Japan in recent months.

Central banks have eased policy in recent months, although expectations for further easing have been scaled back

Several central banks have eased policy further recently in response to a deteriorating outlook for economic growth in an environment of subdued inflation. Market expectations for additional easing have been scaled back in recent weeks as concerns about some key downside risks have abated somewhat. Current market pricing suggests that the Fed is expected to lower its policy rate further in the first half of 2020, while most other central banks are expected to leave rates around current low levels for some time (Graph 1.17).

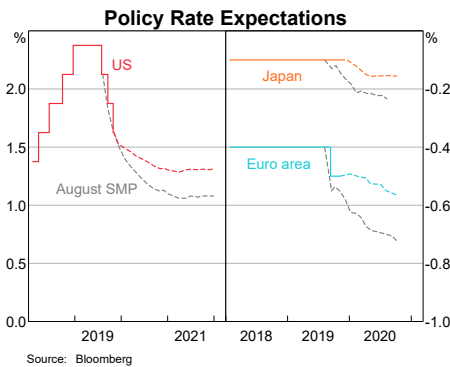
The Fed has lowered its policy rate by a cumulative 75 basis points (to 1.5–1.75 per cent) since it began easing policy in July. Fed Chair Powell has reiterated that the US economy continues to perform well, and that these reductions in policy rates have been a response to subdued inflation and downside risk to the global growth outlook. Powell described current policy settings as appropriate and noted that it would take a material change in the outlook to adjust policy settings further.

The European Central Bank (ECB) left policy settings unchanged in October, having

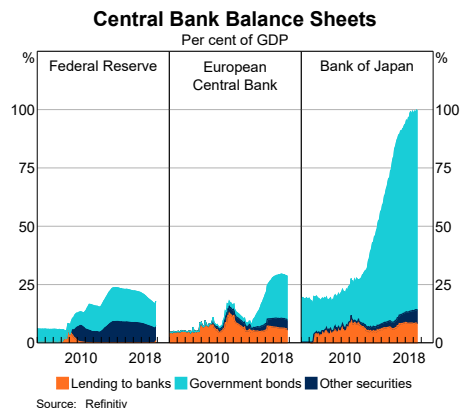
announced a package of stimulus measures at its September meeting. This package included: lowering the deposit rate by 10 basis points to –0.5 per cent; introducing a tiered system of reserve remuneration to lower the portion of banks’ excess reserve holdings that are subject to the negative deposit rate; renewing asset purchases; and easing the conditions of its targeted long-term refinancing operations. ECB officials stated that these measures were introduced in response to inflation running persistently below the ECB’s target (of close to, but below, 2 per cent), protracted weakness in euro area growth and downside risks to the outlook. The Governing Council committed to purchase government and private sector securities until shortly before it increases its policy rate and not to lift rates until there is a sustained increase in inflation (Graph 1.18).

The BoJ left its policy settings unchanged in October but signalled that it may provide further policy stimulus if there is evidence of a loss of momentum in inflation towards the 2 per cent target. In late September, the BoJ announced that it plans to increase purchases of short-term bonds and reduce purchases of long-term bonds in an effort to steepen the yield curve. The BoJ noted that a steeper yield curve could mitigate the effects of negative yields on long-term institutional investors, such as pension

Graph 1.17



Graph 1.18



funds and life insurance companies, and improve the transmission of monetary policy to the real economy.

The Reserve Bank of New Zealand (RBNZ) left its policy rate unchanged at 1.00 per cent at its September meeting, while noting that the 50 basis point rate cut in August was having the desired effect on retail lending rates and the exchange rate. Market participants expect the RBNZ to lower the policy rate by a further 25 basis points by early next year.

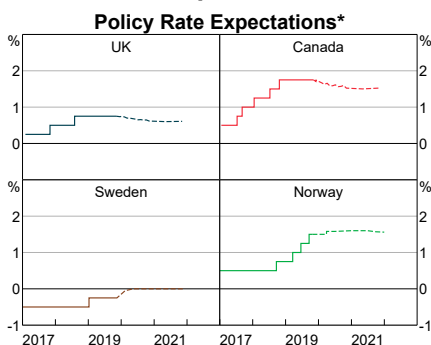
A number of other central banks in advanced economies have left policy rates unchanged in recent months, including the Bank of Canada, Bank of England (BoE) and Swedish Riksbank, while Norges Bank increased rates in September (Graph 1.19). All have noted that inflation is close to target and their economies are judged to be operating close to potential. However, they have also emphasised that the future path of policy remains uncertain, reflecting risks to the global economic outlook and uncertainty as to how these might transmit domestically. The BoE has also noted that future policy remains dependent on the nature of the United Kingdom's exit from the European Union.

Government bond yields remain low; a large share are trading with negative yields

Government bond yields in advanced economies have increased slightly since the August *Statement* but remain near historic lows in a number of countries (Graph 1.20). Since late 2018, bonds yields have declined substantially, and a large share of bonds issued in advanced economies are now trading with a yield below zero (Graph 1.21). The governments of some European countries have been issuing short-term government bills with negative yields since 2011, as has the Japanese government since 2014, when policy rates in these countries first fell close to zero. More recently, governments have been issuing debt at negative yields for longer maturities, and some governments have been able to borrow at negative interest rates for 30 years or more. A few highly rated corporations have also issued bonds with yields below zero.

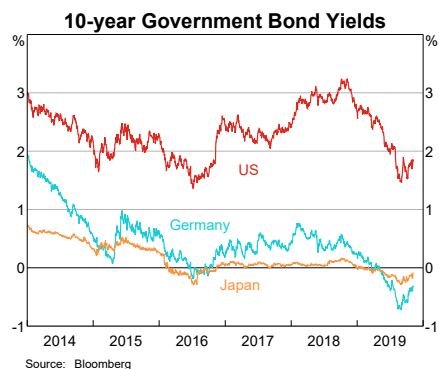
There are a number of reasons for investors to hold negative-yielding securities. Many institutional investors, such as life insurance companies and defined benefit pension funds, operate under mandates or are required by regulation to hold highly rated, long-duration assets, even at negative yields. Some are prepared to hold negative-yielding securities where they are considered to have superior

Graph 1.19



* Expectations for the UK and Canada are derived from OIS curves, expectations for Sweden and Norway are central bank forecasts
Sources: Bloomberg; Norges Bank; Sveriges Riksbank

Graph 1.20



Source: Bloomberg

liquidity characteristics (including during periods of heightened risk aversion). Other investors may expect rates to fall even further below zero, or may opt to invest in fixed income securities (even with low or slightly negative interest rates) to hedge against the risk of prolonged deflation. Some foreign buyers may also be able to earn positive returns on negative-yielding bonds due to the currency basis; this is the extra compensation received for lending currencies that are in high demand (such as the US dollar) in exchange for other currencies (such as the Japanese yen).

The cost of funding for corporations remains low

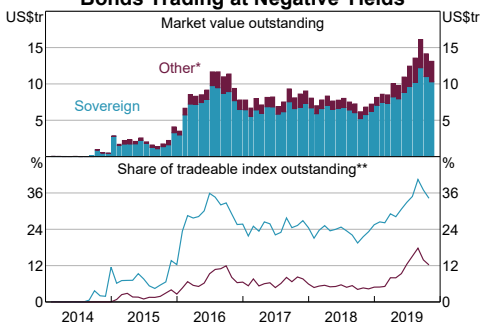
Yields on corporate bonds remain low, reflecting both low government bond yields and narrow credit spreads (Graph 1.22). Demand for corporate bonds has remained robust, driven by strong appetite for higher yields compared with government securities and expectations that corporate default rates will remain low. In China, the improvement in financial conditions for corporations in part reflects the targeted policy easing directed to smaller banks, which in turn direct relatively more of their lending to private enterprises than larger banks. This policy easing has reduced banks' funding costs, which can be

passed on to corporations in the form of lower lending rates.

Global equity indices have traded mainly within a 5–10 per cent range for the past six months after increasing strongly in the early part of the year, and are now at record highs in the United States (Graph 1.23). Valuation metrics that compare prices to earnings or book value are around historical averages, though equity risk premiums (the excess inflation-adjusted yield on equities compared to bonds) appear somewhat higher than longer-term averages, in part reflecting the unusually low levels of real sovereign bond yields. Market analysts expect profitability of corporations to remain sound, despite some recent slowing in earnings growth.

Graph 1.21

Bonds Trading at Negative Yields

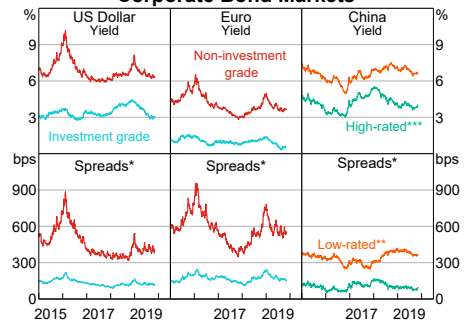


* Includes corporate, quasi/foreign government, and securitised
 ** Share of outstanding securities in ICE Data's Global Fixed Income Index as at October 2019

Source: ICE Data is used with permission

Graph 1.22

Corporate Bond Markets



* Spread to equivalent maturity government bond yield

** Based on five year AA- domestically rated bond

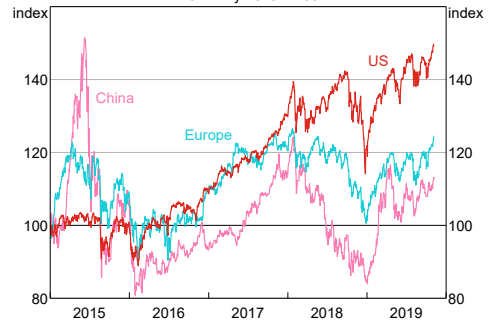
*** Based on five year AAA domestically rated bond

Sources: Bloomberg; CEIC Data; ICE Data is used with permission

Graph 1.23

Equity Prices

1 January 2015 = 100



Source: Bloomberg

The cost of borrowing in short-term US dollar money markets (over and above expected policy rates) has risen in recent months, partly reflecting an increase in Treasury bill issuance after the debt ceiling was suspended in the United States (Graph 1.24). In mid September, US dollar repo rates increased sharply, which spilled over to some other short-term rates and resulted in the effective fed funds rate briefly exceeding the top of the Fed’s target range. The sharp rise in repo rates appears to have been largely driven by a rise in the net demand for US dollars in money markets, due to high corporate tax payments as well as the increased issuance of debt by the US Treasury, in an environment of declining bank reserves. The Fed responded to these pressures by injecting additional short-term liquidity into the repo market and increasing the stock of bank reserves via purchases of Treasury bills. It expects these measures to remain in place through the new year, in order to facilitate the fed funds rate remaining within the target range set by the Federal Open Market Committee.

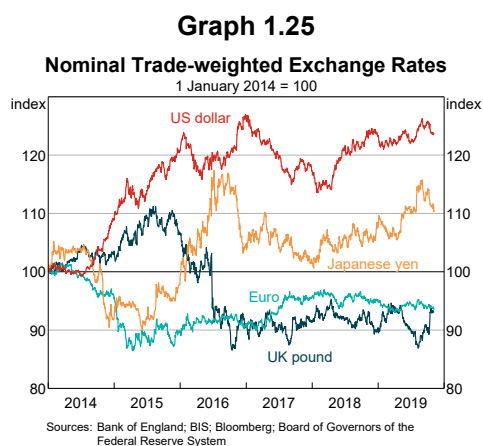
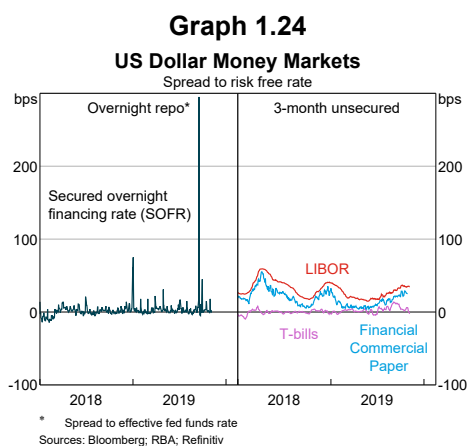
Movements in the exchange rates of the major currencies are mixed

The US dollar has been little changed in recent months, having appreciated over the past two years on a trade-weighted (TWI) basis

(Graph 1.25). The euro is also little changed on a TWI basis; there has been little reaction since the announcement of additional stimulus measures by the ECB in September. In contrast, the Japanese yen has depreciated since the previous *Statement*, largely reversing the sharp appreciation that occurred in August alongside an increase in financial market uncertainty. The UK pound has appreciated sharply from earlier in the year, as the likelihood of a ‘no-deal’ Brexit declined. The UK Parliament has agreed in principle to a withdrawal agreement bill and the exit deadline has been extended to 31 January 2020.

The Chinese renminbi has been relatively stable in recent months following depreciation earlier in the year

Movements in the Chinese renminbi remain responsive to developments in the US–China trade and technology disputes. After depreciating through 7 yuan per US dollar in August, the renminbi has appreciated somewhat in recent weeks against the US dollar and on a TWI basis (Graph 1.26). While China’s foreign currency reserves have been stable at around US\$3 trillion, in recent months, the authorities have generally set the daily fixing rate at a level that signals support for the



renminbi. The PBC has also reduced liquidity in the offshore renminbi money market, which makes it more expensive to sell renminbi in the forward market. Over the past year or so, and in contrast to early 2016, the currency has also been supported by an increase in China's net portfolio inflows alongside the inclusion of Chinese bonds and equities in benchmark indices that are widely tracked by global portfolio managers (Graph 1.27).

In east Asia, the decline in global trade continues to weigh on growth

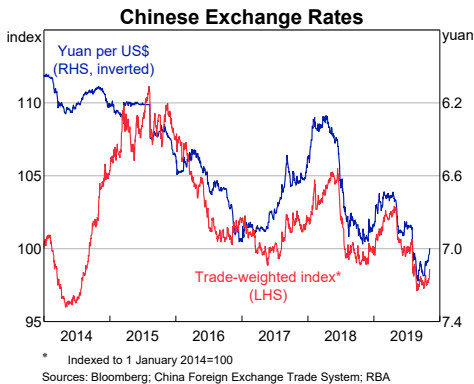
Weak external demand has continued to weigh on growth in east Asia. The outlook for the region remains subdued, particularly for the high-income economies, despite support from

monetary and fiscal policies. The escalation in the US–China trade dispute is likely to have a material impact on the region given its integration in global supply chains, especially, those involved in Chinese export production.

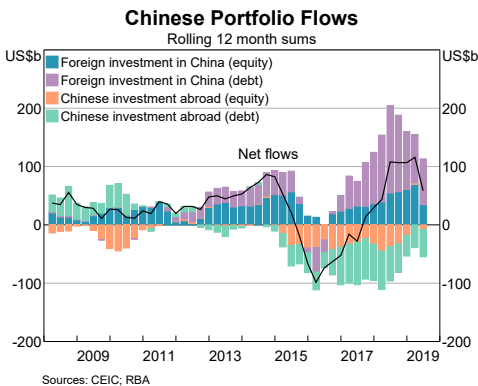
Merchandise export values have continued to decline (Graph 1.28). The export weakness has been mainly concentrated in South Korea and Singapore; these two economies are key exporters of memory integrated circuits, which have experienced large price declines due to oversupply and weak global demand. Exports to the United States have been boosted in some economies as trade has been diverted from China as a result of the higher tariffs. Export volumes and industrial production have tentatively stabilised since May at around year-ago levels (Graph 1.29). Surveyed business conditions and new export orders have picked up in some economies in recent months, but remain below average levels.

GDP growth in east Asia continued at a subdued rate in the September quarter, particularly in the more export-oriented economies in the region (Graph 1.30). Investment has declined and consumption growth has slowed over the past year in the more export-oriented economies (Graph 1.31). Political unrest has weighed additionally on activity in Hong Kong. Governments in the region have taken steps to support

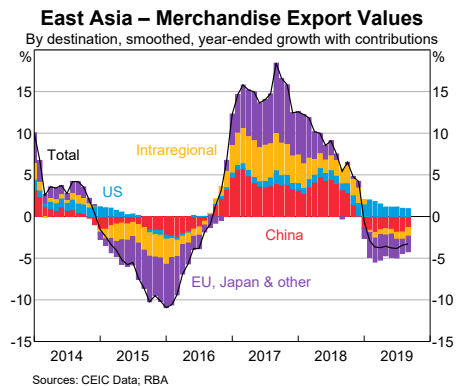
Graph 1.26



Graph 1.27



Graph 1.28



growth. The South Korean government has increased spending this year and a further large increase is proposed for next year. Growth has been more resilient in the less export-oriented economies, especially Indonesia, supported by steady consumption growth. Activity has picked up in some economies, such as Vietnam, because production of some exports to the United States has relocated from China.

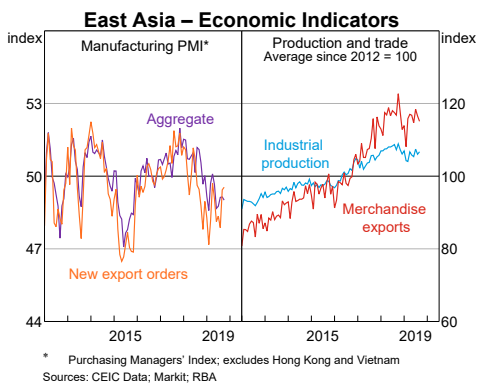
Monetary policy has become more accommodative in response to lower growth and low inflation in the region (Graph 1.32). Inflation has declined in South Korea partly due to the slowdown in growth and despite stronger wage growth since 2018 following substantial minimum wage increases. Inflation has also

declined to below the target band in the Philippines following tighter monetary policy in 2018 and more subdued food prices this year. In Indonesia, inflation is around the midpoint of the inflation target range, supported by easing policy and relatively resilient domestic demand. In Malaysia, inflation has increased this year because of base effects from changes in consumption taxes a year ago.

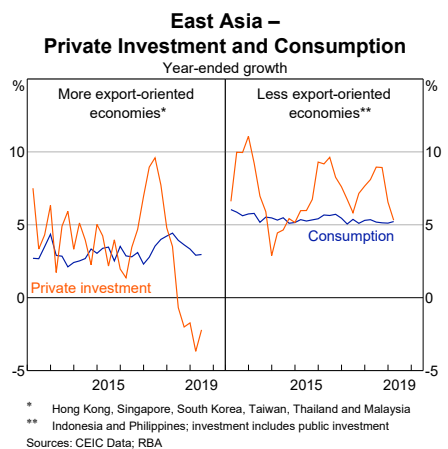
Indian authorities have eased policy further to support growth

Indian economic growth declined further in the June quarter, reflecting a broad-based slowdown in domestic demand (Graph 1.33).

Graph 1.29



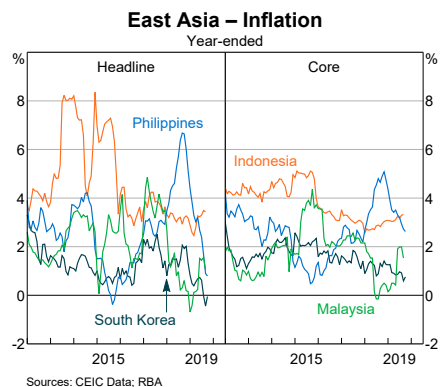
Graph 1.31



Graph 1.30



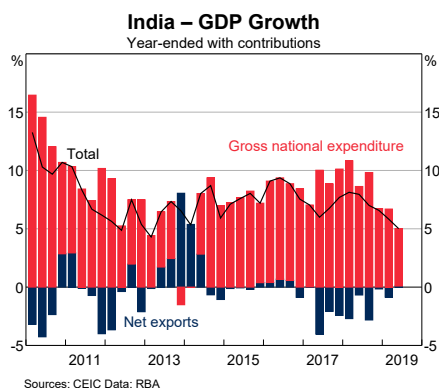
Graph 1.32



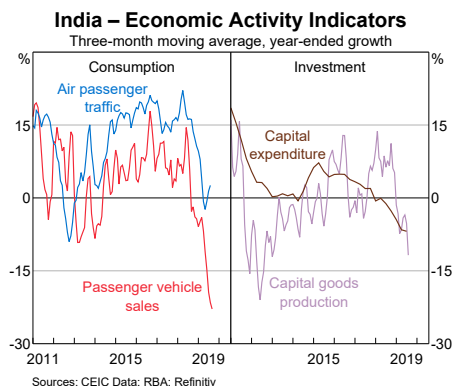
Domestic demand has softened at the same time that regulators have given more attention to bad debts on lenders' balance sheets; these institutions have therefore had to clean up their balance sheets, which has weighed on credit growth. Timely indicators suggest that consumption and investment have remained weak in recent months; car sales have continued to fall and growth in air passenger traffic remains subdued (Graph 1.34). Production and imports of capital goods have also declined markedly and capital expenditure has contracted further. In September, headline inflation increased to be in the middle of the Reserve Bank of India's (RBI's) target band, reflecting rapid inflation in food and beverage prices, while core inflation has been steady.

The Indian Government has announced a number of measures in recent months to support growth. Most significantly, the government reduced the base corporate tax rate from 30 per cent to 22 per cent, and lowered the tax rate applicable to new manufacturing companies from 25 per cent to 15 per cent. Other measures announced included lifting a ban on government purchases of new vehicles, consolidating 10 state-owned banks into four to support lending activity and cancelling a planned tax increase on foreign portfolio investors. The RBI reduced its policy rate by a further 25 basis points in October, taking the cumulative easing in the policy rate this year to 135 basis points.

Graph 1.33



Graph 1.34



Accommodative global financial market conditions have supported emerging financial markets

Like the RBI, many other emerging market central banks have lowered their policy rates this year, in response to the weaker external growth outlook, subdued domestic inflationary pressures and reduced external financing risks (Graph 1.35). Policy easing has contributed to declines in yields on government bonds denominated in local currencies and increases in equity prices (Graph 1.36). The currencies of most emerging market economies have been little changed against the US dollar in recent months. Argentina is a notable exception where financial market conditions have deteriorated further. Government bond yields have risen, the Argentine peso has depreciated and capital controls have been tightened as political developments raise concerns that the government may postpone or restructure debt repayments.

Oil prices have been volatile in recent months

Oil prices increased sharply in mid September following attacks on Saudi Arabian oil assets,

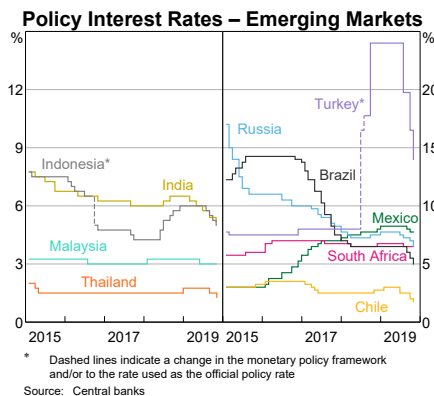
which affected around 5 per cent of global oil supply (Graph 1.37). However, oil prices subsequently retraced this fall because oil production was restored faster than initially expected, according to Saudi authorities and market reports. More broadly, increases in US oil production and concerns about the outlook for oil demand stemming from more moderate global growth have weighed on oil prices, which remain around 15 per cent below their recent peak in mid May.

Bulk commodity prices have been driven by Chinese policies and global supply developments

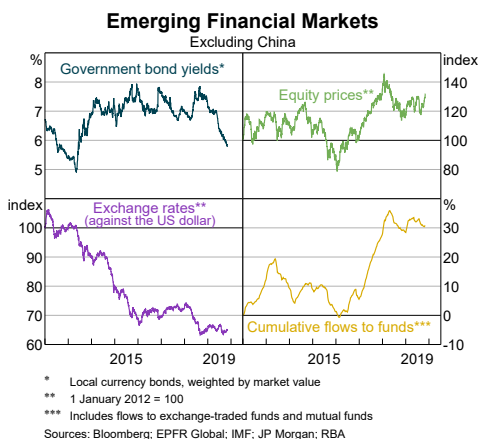
Iron ore prices are 13 per cent higher than a year ago, in part because of ongoing strength in Chinese steel production as a result of policy measures to support the Chinese economy (Graph 1.38; Table 1.1). Recently announced measures to accelerate and increase infrastructure investment by local governments over the next year suggest that the outlook for Chinese iron ore demand remains fairly positive. A portion of global supply also remains offline, following production disruptions in Brazil earlier in the year, although the restoration of some supply has weighed on prices in recent months. The ongoing US–China trade and technology disputes have also contributed to price volatility in recent months.

Australian thermal coal prices have declined over recent months because seaborne supply, including from Australia, has increased (Graph 1.39). Global demand has also been softer, in part because electricity generators have been substituting away from coal to gas in response to a decline in global spot prices for gas over the past year. Coking coal prices have also declined, partly reflecting some weakness in demand from Asian economies.

Graph 1.35



Graph 1.36



Graph 1.37

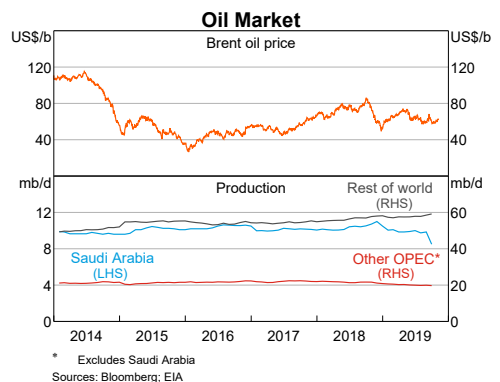


Table 1.1: Commodity Price Growth^(a)

	Since previous <i>Statement</i>	Over the past year
Bulk commodities	-12	-12
– Iron ore	-13	13
– Coking coal	-16	-39
– Thermal coal	-5	-35
Rural	2	-4
Base metals	4	-2
Gold	-1	22
Brent crude oil ^(b)	8	-13
RBA ICP	-5	-5
– Using spot prices for bulk commodities	-7	-11

(a) Prices from the RBA Index of Commodity Prices (ICP); bulk commodity prices are spot prices

(b) In US dollars

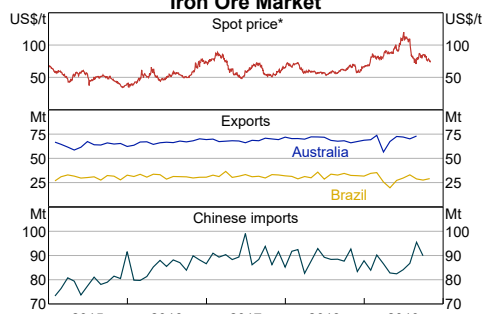
Sources: Bloomberg; IHS Markit; RBA

Base metal prices are generally higher since the previous *Statement* (Graph 1.40). Zinc, lead and nickel prices have increased following some supply disruptions. Prices for Australian rural exports have been mixed over the previous three months. Lower pork production in China and strong demand from the United States has supported beef and lamb prices, although lamb prices have declined from their peak partly because of a seasonal increase in Australian supply. Wool prices have decreased because of softer demand from China.

Based on partial data, Australian export prices (including the prices of non-commodity exports) are expected to have increased in the September quarter, which suggests Australia's terms of trade have remained at a high level. ✎

Graph 1.38

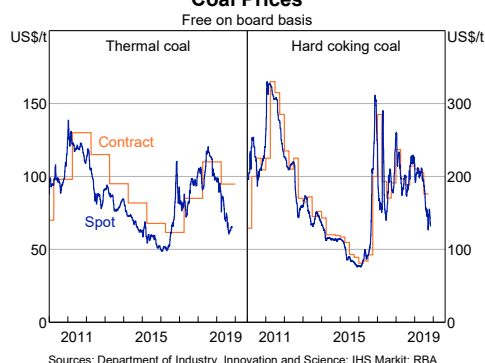
Iron Ore Market



* 62% Fe Fines index; free on board basis
Sources: ABS; Bloomberg; CEIC Data; RBA

Graph 1.39

Coal Prices

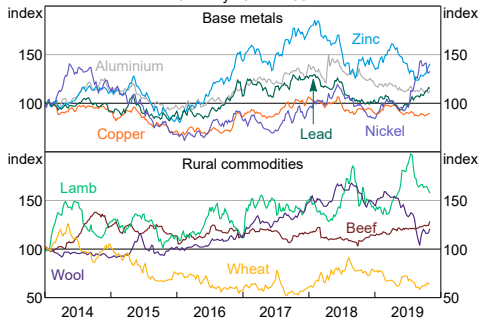


Sources: Department of Industry, Innovation and Science; IHS Markit; RBA

Graph 1.40

Base Metal and Rural Prices

January 2014 = 100



Sources: Bloomberg; Landmark; MLA; RBA

