

Box B

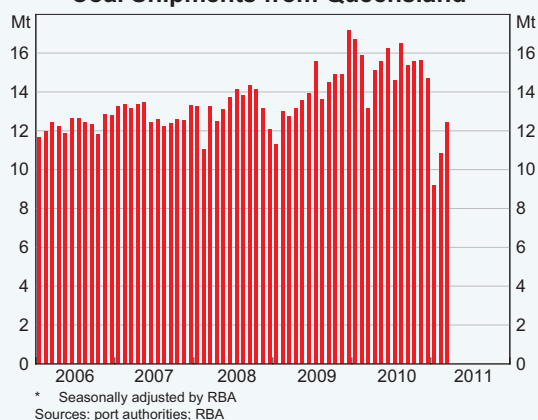
An Update on the Impact of the Natural Disasters in Queensland

Queensland is recovering from the severe rains and flooding across much of the state in late 2010/early 2011 and the damage caused by Cyclone Yasi in early February. While information is still incomplete, this box provides an update on the impact of these events on economic activity and inflation.

Impact on Economic Activity

As foreshadowed in the February *Statement*, the largest impact on activity from the rainfall has been the disruption to coal production in Queensland, which provides almost two-thirds of Australia's coal exports. It now looks likely that the loss to coal production will be somewhat larger than the 25 million tonnes estimated in February. Coal production fell sharply in the month of December and was significantly affected through the March quarter. While exports initially held up in December as inventories were run down, they fell sharply in January. The level of coal shipments recovered somewhat in February and March, although it remains well down on its pre-flood level (Graph B1).

Graph B1
Coal Shipments from Queensland*



Coal production continues to be constrained by flooded pits, with many of the state's coal mines working below full capacity and a number of miners yet to remove their declarations of *force majeure*. Coal stocks remain depleted and rail and port operators report significant spare capacity. Since December, 68 Transitional Environmental Programs have been issued in Queensland authorising the removal of flood waters from mines (a process known as 'de-watering'), subject to environmental conditions. These conditions have constrained the amount of de-watering that has occurred to date as river stream levels have fallen (high stream levels are required to prevent the build-up of pollutants in the environment). Additional rainfall across the Bowen Basin has also slowed the recovery in the level of coal production. As a result, coal production is now expected to remain below normal levels until well into the June quarter. RBA staff estimates suggest that the fall in coal production subtracted up to $\frac{1}{2}$ percentage point from GDP growth in the December quarter and will have subtracted an additional $\frac{3}{4}$ to 1 percentage point from growth in the March quarter, a larger impact than had been expected in February. Coal production is, however, expected to add significantly to GDP growth in the June and September quarters as production levels continue to recover.

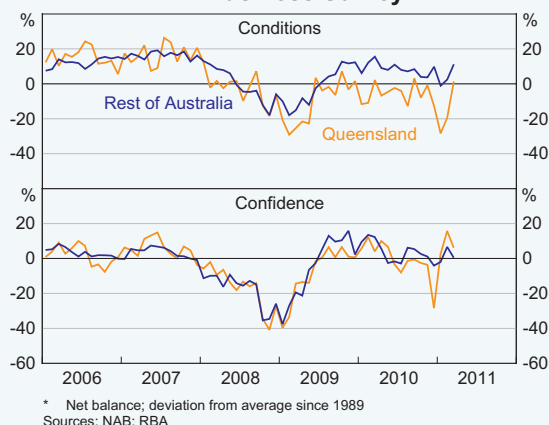
The agricultural and tourism sectors have also been significantly affected. Losses to agricultural production, as calculated by rural agencies, are in the order of \$2 billion. Losses have been particularly concentrated in the sugar cane, cotton and banana industries. In regard to the tourism sector, Australian Government estimates suggest that the recent

natural disasters will result in a loss of around \$400 million in activity.

The weather events resulted in disruptions to other economic activity as well, although much of this was temporary. Housing loans – both for new and existing dwellings – fell sharply in Queensland in January and remained low in February. There was also a sharp fall in building approvals for new houses in Queensland in the March quarter. In contrast, retail sales in Queensland rose by 0.7 per cent in the March quarter while sales in the rest of Australia were broadly flat. Queensland sales of household goods – which include furniture, floor coverings, homewares and electronic goods – rose particularly strongly in the quarter, consistent with the replacement of consumer durables damaged by flooding. Such replacement spending would have been supported by payments to households from a number of sources that have already been disbursed, including \$745 million in the 646 000 Australian Government Disaster Recovery Payments made so far, \$825 million paid on 118 000 insurance claims to date (including payments to businesses), and disbursements of \$58 million from the Premier's Disaster Relief Appeal that has raised \$252 million.

The temporary nature of much of the interruptions to business activity in Queensland is also apparent in the NAB business survey, which showed an initial sharp fall in business conditions in early January but a subsequent bounce-back in business conditions and especially in confidence (Graph B2). These results suggest that many businesses anticipate a pick-up in activity associated with repair and rebuilding. A supplementary question in the survey taken in late January indicated that business activity had returned to pre-flood levels for more than half of the affected firms, while more than three-quarters of firms expected that their activity would have fully recovered within three months of the survey's date.

Graph B2
NAB Business Survey*



The extent of the damage to the stock of private dwellings and public infrastructure from the natural disasters has become clearer over time. According to the Queensland Reconstruction Authority report released in late April, around 7 600 residential properties were severely affected, with at least 3 300 homes needing to be completely rebuilt and an additional 1 700 needing to be vacated in order to be repaired. Much public infrastructure in Queensland was also damaged and rebuilding and repair spending is under way. The restoration of essential services has largely been completed: virtually all affected homes and businesses have had power restored, and the affected water supply schemes and sewerage treatment plants have now mostly returned to operation. Of the 411 schools affected across Queensland, only one continues to operate from a temporary location. The state's main rail systems have reopened following the restoration of the Western Rail Line (three months earlier than scheduled), and all the state's ports are operating following the resumption of shipping in March at the Port of Bundaberg. Much of the total public repair spending is expected to be on the road network.

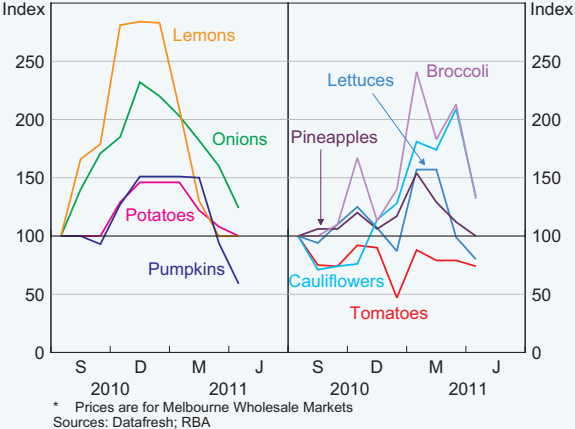
According to the Reconstruction Authority, around one-quarter of the state road network was damaged and, while work in this area is also underway, around one-third of the affected roads are yet to be restored to former speeds and legal load limits.

Looking ahead, the remaining rebuilding of damaged private and public assets is expected to provide a modest boost to activity. The Queensland Government expects the overall public reconstruction effort associated with the floods will eventually reach \$5 billion, with damage to public infrastructure associated with Cyclone Yasi estimated at an additional \$0.8 billion. Under the Natural Disaster Relief and Recovery Arrangements, the Federal Government will fund around \$4.4 billion of this total damage cost. Both the Federal and State Governments have indicated that they will review spending priorities and reduce other planned infrastructure spending to fund part of this work. Taking all these factors into account, net additional private and public spending – with quite a high share of the latter likely to be offset by delays to other planned spending – will provide a mild boost to overall activity in the next couple of years. Liaison suggests much of the housing reconstruction task can be accommodated by the Queensland construction industry, given existing spare capacity.

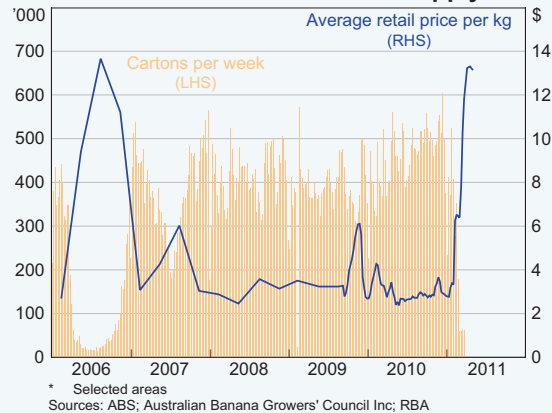
Impact on the Consumer Price Index

As had been expected, the Queensland floods and Cyclone Yasi have led to a temporary increase in food prices, primarily due to their effect on some fruit and vegetable crops. Prior to these events, wet weather had put upward pressure on fruit and vegetable prices in the December quarter. The floods had an additional effect on the prices of a range of vegetables in the March quarter, with Cyclone Yasi also raising the price of bananas in the quarter.

Graph B3
Wholesale Fruit and Vegetable Prices*
July 2010 = 100



Graph B4
North Queensland Banana Supply*



More timely wholesale fruit and vegetable price data indicate that supply pressures for many fruit and vegetables affected by the poor weather conditions have since eased, with the notable exception of bananas (Graphs B3 and B4). Wholesale prices for a range of fruit and vegetables (including potatoes, pumpkins, lettuce and pineapples), which spiked during the December and March quarters,

had returned by April to around or below pre-flood levels. For many of these crops, the ready availability of alternative sources or short production cycles has meant that the price impact of the adverse weather events has been relatively short.

In contrast, since bananas have a comparatively long production cycle and cannot be imported, the supply impact will be more prolonged. The supply of bananas from areas in North Queensland has fallen sharply as a result of Cyclone Yasi, to around 15 per cent of normal levels; the fall is, however, expected to be slightly smaller than that following Cyclone Larry in 2006. Supply is not expected to start to recover until the second half of this year, and prices have risen sharply from February. While banana prices appear to have stabilised in recent weeks, in quarterly average terms they are likely to add further to food price inflation in the June quarter, before returning to their pre-cyclone level by around the end of this year. ❖

