When we first came into office just over a year ago, the global economic outlook was improving. That changed over the course of the year and by late 2011/early 2012, there were grave concerns about another global banking crisis emanating from Europe.

Thankfully, those concerns appear to have eased, but as US Treasury Secretary Tim Geithner said recently, Europe is “only at the beginning of a very tough, very long, hard road”.

An emerging concern of financial markets and policy makers is that growth in China will slow sharply and that global commodity prices and the Australian economy will suffer. Already that possibility has been reflected in a slightly lower Australian dollar in recent weeks, and since early 2011 we have seen Newcastle coal prices fall from $US140 tonne to around US$105 currently.

China is very important for the global outlook. It overtook Japan as the world’s second largest economy in 2010. China is also NSW’s largest trading partner. NSW goods exports to China now tally over $5 billion a year, and have more than doubled over the last three years.

So if a major slowdown did occur in China, the world economy would be affected, and Australia and NSW would not be immune.

While a major global downturn is not what I expect, it remains a possibility that cannot be ignored. If it were to happen it is likely the Reserve Bank would respond by cutting interest rates, and prudent fiscal stimulus in Australia may also be appropriate. That stimulus should be temporary, targeted and timely. Spending on infrastructure fits all those requirements and has the highest multiplier, in terms of jobs added to the economy. The Federal government has the capacity to fund such infrastructure stimulus, and the states have the ability to implement it most effectively.

That is why our Government is preparing a list of shovel-ready state infrastructure projects as a contingency plan. We are doing this for two reasons. Firstly, so that stimulus money will not be wasted and secondly, so that funds will be directed to high- priority state projects.

The financial fallout from the GFC and sovereign debt crisis has implications-- not just for the economy-- but also for asset prices. These should not be ignored. The OECD’s Pension Markets in Focus study found that Australian super funds have one of the highest exposures to share markets among all OECD countries, and they have a relatively low exposure to fixed income products. Accordingly, there is a strong case for people to reassess their super portfolios, especially as they approach retirement, when lower risk and stable income streams become more important.

Recognising this issue we have recently added an annuity-style bond to the NSW Waratah Bond program. For the first time in Australia a product is available for retiree investors that offers a NSW government guaranteed, stable income stream which will protect against inflation. The product enables the government to diversify its funding base by tapping into the growing Self-Managed Super Fund market, while at the same time providing retirees with greater confidence in spending power, income and peace of mind.

A key policy challenge for NSW is housing supply. The preconditions for a pickup in housing investment seem to be there – significant pent up demand after years of under-building, low vacancy rates and rents rising well above CPI inflation, while housing finance is up strongly over the past year. However, these positive signs have yet to be translated into home building. Building approvals and housing starts are near multi-decade lows -- a situation that we will focus on in coming months.

As I enter my second year as Treasurer there are some genuine positive signs for NSW. In particular, the steady unemployment rate of 5.2 per cent and the increase in the number of jobs are good news for NSW. Job vacancies data is also encouraging and business confidence is holding up.

After decades of underperformance, the NSW economy is moving, but there are many challenges that lie ahead. We will be working to address some of these issues in the Budget on 12 June. Fiscal discipline remains the key foundation for achieving long-term sustainable economic growth in NSW.

Mike Baird
NSW Treasurer
The numbers behind the numbers

China is NSW’ major trading partner. Almost one quarter of goods imports to NSW were sourced from China over the last twelve months while over 13 per cent of NSW goods exports go to China.

- The value of NSW goods exports to China has more than doubled over the last three years, from around $2 billion to over $5 billion currently.

Residential building approvals are volatile on a month to month basis, especially for detached housing such as high rise apartments, flats, etc, where large projects can swing around the figures. Total building approvals are trending down as at February 2012.

- Detached house approvals are showing a modest downward trend.
- High rise apartment, flat, etc approvals are showing a larger downward trend.

Employment by industry shows that different parts of the NSW economy are being affected differently by the mining boom, high exchange rate and less consumer spending on retail items.

- Construction and mining employment have lifted over the last 12 months, while employment in manufacturing, accommodation and food, and wholesale and retail trade has declined.
- Business services continue to be the key driver of employment in the state, with the strongest increases in the admin and IT sectors.