atradius

managing risk, enabling trade

Atradius Country Report

Australia – August 2013

Overview

General information

Capital:	Canberra
Government type:	Federal parliamentary democracy
Currency:	Australian dollar (AUD)
Population:	23.1 million

Most important sectors (% of GDP, 2012)

Services:	69 %
Industry/mining:	27 %
Agriculture:	4 %

Main import sources (2012, % of total)

China:	18.2 %
USA:	11.6 %
Japan:	7.8 %
Singapore:	5.9 %
Germany:	4.6 %

Main export markets (2012, % of total)

China:	29.5 %
Japan:	19.3 %
South Korea:	8.0 %
India:	4.9 %
USA:	3.7 %

Key indicators

	2010	2011	2012	2013*	2014*
Real GDP growth (y-on-y, % change)	2.6	2.4	3.6	2.4	2.7
Consumer price inflation (y-on-y, % change)	2.9	3.3	1.8	2.2	2.7
Private consumption (y-on-y, % change)	3.0	3.3	3.2	1.9	2.7
Retail sales (y-on-y, % change)	-0.4	-0.9	1.4	0.9	3.1
Industrial production (y-on-y, % change)	4.3	-1.1	4.0	2.3	2.6
Unemployment rate (%)	5.2	5.1	5.2	5.6	5.5
Real fixed investment (y-on-y, % change)	4.4	7.2	8.4	0.9	5.7
Export of goods and non-factor services (y-on-y, % change)	5.7	-0.8	6.3	5.2	2.4
Fiscal balance (% of GDP)	-3.4	-3.2	-2.7	-1.0	-0.7

* forecast Source: IHS Global Insight

Main economic developments

Slowdown of economic growth in 2013

Australia's economic performance has been remarkably good over the last few years compared to most advanced economies and against the background of a volatile global economy. This was due mainly to the high growth rates of Australia's main trading partners in Asia - especially China, which has dominated Australian mineral exports.

However, GDP growth has begun to slow in 2013: through the combined effects of lower Chinese growth rates, decreasing commodity prices of minerals and volatility in financial markets. In addition, various domestic business surveys in June and July 2013 have indicated weaker than average trading conditions, profit expectations and business confidence. After a 3.6% increase in 2012, economic growth is expected to slow to 2.4% this year (see chart below). In early August, the central bank lowered its benchmark interest rate to 2.5% from 2.75% - a new record low - in an attempt to spur a fresh wave of economic growth, especially in the non-mining sectors. This reduction of the interest rate was the second in 2013, and extends an easing cycle that began in November 2011, when the benchmark rate was lowered from 4.75%.

*forecast

Source: IHS Global Insight

On the positive side, the volume of bulk commodity exports is expected to continue rising in 2013 and 2014. This should help to sustain the economy, as major mineral and energy projects begin to move from construction to production and export.

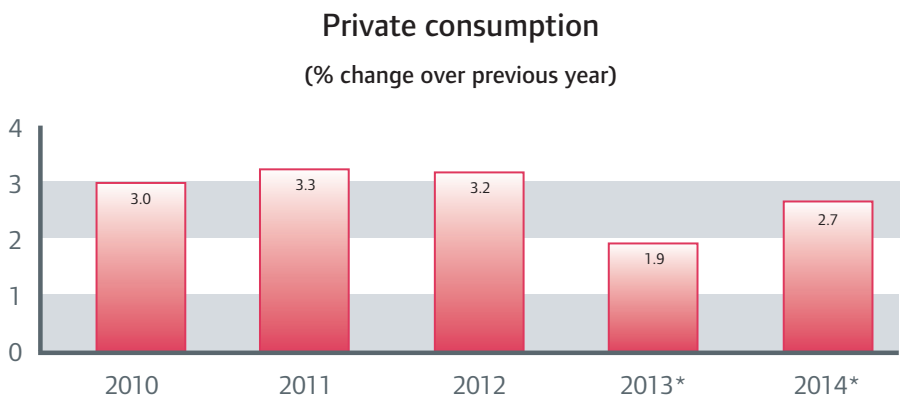
The forecast of 2.7% growth for 2014 is more uncertain as the Australian economy is in transition, with a reduction in mining investment and question marks over whether the non-mining sector can assume the role of growth engine.

Private consumption losing steam

Growth in private consumption was reasonably good in 2012, at 3.2%. This picked up in early 2013, as falling retail prices led to increased sales. However, retail spending has waned since then, and is expected to grow by only 0.9% this year.

Unemployment was relatively low, at 5.2%, in 2012 but the trend has been upward since the beginning of 2013, with fewer jobs in the mining sector. Unemployment increased to 5.7% in June and July and is forecast to be around 5.6% for the year.

Overall, with continuing poor labour market conditions and only modest growth in household wealth, it seems likely that growth in private consumption will remain below trend, at 1.9% this year, with the possibility of improving to 2.7% in 2014 (see chart below). Last year, Inflation in Australia was relatively low, at 1.8%. Moderate increases are however forecast for 2013 (2.2%) and 2014 (2.7%).



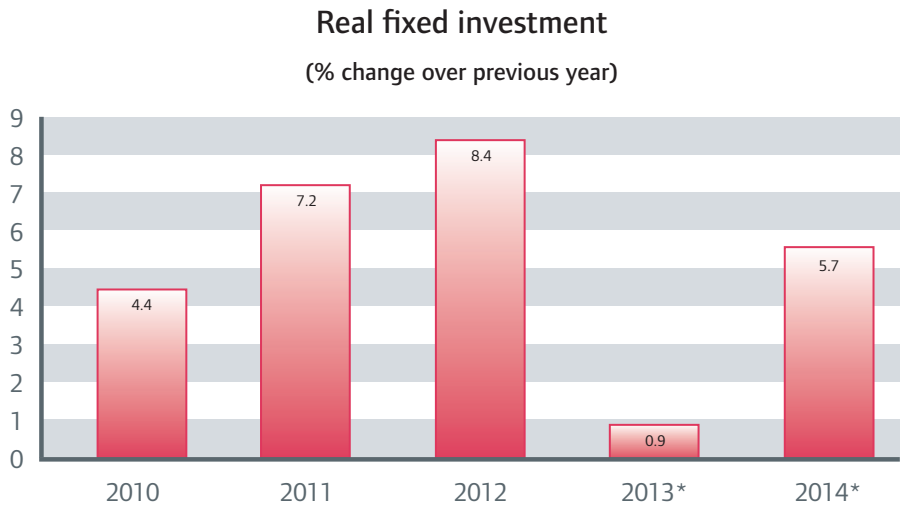
*forecast

Source: IHS Global Insight

Mining investment has reached its peak

The mining sector has been the driver of high growth in real fixed investment - 7.2% in 2011 and 8.4% in 2012 - but there are clear signs that it is no longer contributing to growth, as mining investment has reached its peak. There are still several major liquefied natural gas (LNG) projects underway to keep mining construction elevated until their completion in early 2017. However, the pipeline of incomplete work continues to decline in an environment of weak and volatile commodity prices.

In addition, interim economic data for Q1 of 2013 indicated weak non-mining sector investment, although business surveys suggest a possible modest increase over the next 12 months. Under these conditions, real fixed investment growth is forecast to be only 0.9% in 2013. A rise in the investment growth rate - to 5.7% - is expected in 2014 (see chart below) but there are risks to this forecast, especially as there are no new mega-projects on the horizon.



*forecast

Source: IHS Global Insight

Depreciation of the Australian dollar should help rebalance the economy

The Australian dollar (A$) rose against the US$, as Australian mineral export prices for iron ore and coal increased between 2009 and Q3 of 2011. However, through Q1 2013, despite the fall in mineral prices from the end of 2011, the A$ remained stubbornly - and historically - high for various reasons including increased portfolio investment (as Australia is considered a safe haven), the relative strength of the Australian economy and the gap between domestic and foreign interest rates.

The relatively high A$ hit Australia's tourism industry and export demand for its manufactured goods and educational services. Moreover, domestic manufacturing found it difficult to compete against imports: with domestic steel and car manufacturing in particular suffering.

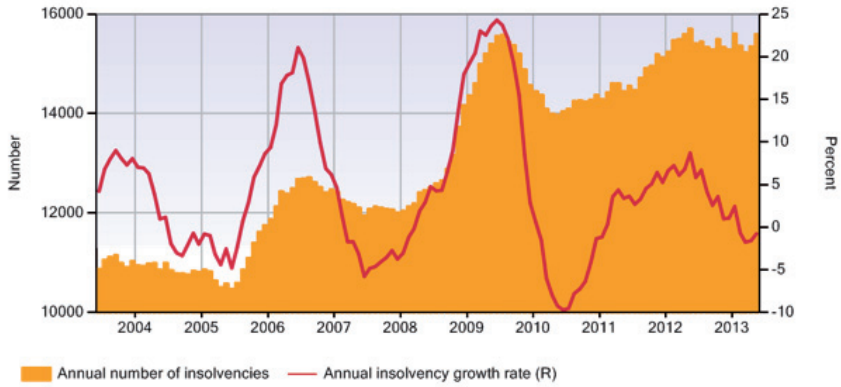
Finally, the A$ started to depreciate against the US$ in May this year, falling by about 10% since then, for several reasons: general upward pressure on the US$; lower expectations for China's growth; falling mineral prices; and a drop in confidence in the outlook for the Australian economy. The decline in the A$ is generally seen as a good thing as it should provide some relief for trade-exposed sectors and would help to foster a rebalancing of growth in the economy.

A moderate depreciation of the A$/US$ exchange rate is expected to continue for the rest of 2013 and into 2014, with a further 10% devaluation by the end of 2014: to around US$ 0.83 to the A$. The forecast depreciation partly reflects the expected strength in the US$ as the US economy continues to recover. Adding to this is the A$-specific effect of the slowing of the Chinese economy and lower mineral export prices.

The insolvency environment

Insolvency trends: Australia

(1-year trailing sum of insolvency counts based on monthly data)

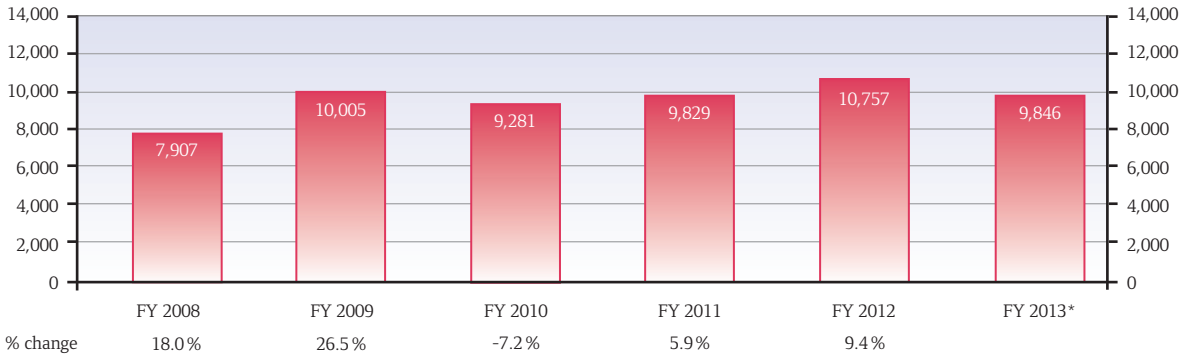


Source: IHS Global Insight, Australian Securities and Investments Commission

Business insolvencies increased sharply in 2008 and 2009, due to the global financial crisis, and have remained at a historically high level since. Insolvencies for the 11 months to May 2013 are at around the same rate as in the fiscal year (FY) 2012 (in Australia the fiscal year start on 1 July and ends on 30 June).

Australian business insolvencies

(year-on-year change)



*11 months until May 31, 2013
Source: Australian Securities and Investments Commission

Despite the economy's good performance, the high number of insolvencies is the result of continued volatility in those sectors that have been adversely affected by the high A$ and tight loan conditions: including construction, manufacturing, tourism and retail. In addition, the mining services sector is coming under increasing pressure amid lower commodity prices and the fading mining boom.

Developments in some main sectors

Retail

Weak consumer sentiment continues to add pressure across all segments of retail with discretionary spending continuing to decline. Consumers are now much more focused on reducing their household debt levels, saving 'for a rainy day' and managing the impact of increasing prices paid for utilities on their overall household budget.

Atradius' recent claims experience is reflective of a number of high profile retail business failures within the last 12-18 months, mainly in the retail of electronic goods and furniture/goods subsectors. Given that those failures have reduced the number of local competitors, the market has moved away from intense price discounting and back towards preserving margins, using service as their sales tool and improving online offerings to compete against cheap imports.

Construction

Growth in the construction sector continues to be subdued on the back of tight credit conditions, a decrease in government spending on infrastructure projects, and lower mining investment. On top of this, the upcoming federal election on September 7th, 2013, has added some uncertainty to existing or planned infrastructure and community construction projects across the states. Despite the recent interest rate cut by the central bank, which will have a positive effect on home buyers and investors, the number of new buildings/developments is likely to remain low in the short-term. Looking forward to post-election, the elected federal government should provide incentives for a strong building and construction sector if it is to be the engine of economic growth and employment, as Australia transitions to a post resources economy. Business failures in the construction and construction materials sectors will be in close relation to such public incentives, while private construction investment continues to slow.

Mining

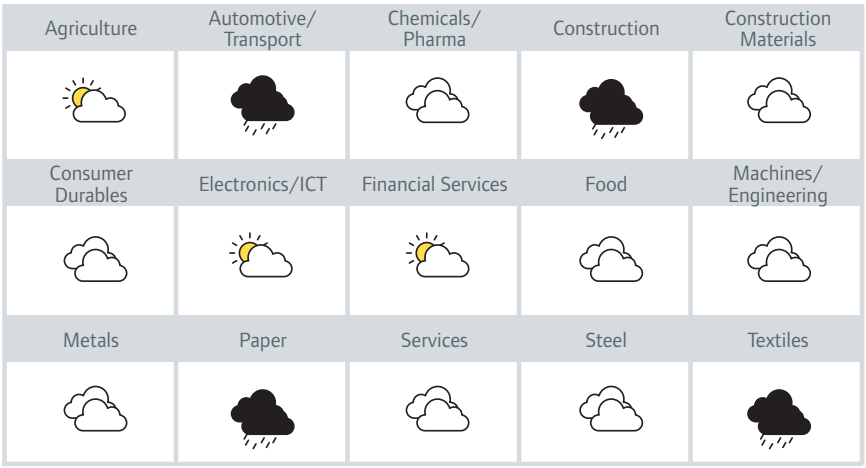
Current issues in the Australian mining sector are the end of the mining investment boom (see above) and declining commodity/ metal prices: It is obvious that the mining investment boom that Australia has experienced for at least the last five years has come to an end, an this will have a negative impact on service providers to the sector such as mining contractors. Australian miners are also in the process of adjusting their businesses to lower commodity/metal prices. In particular prices for coal and gold have sharply decreased during the last 12 months. Iron ore prices continue to be volatile with the expectation of future price decreases from the current position.

Paper

The main subsector of concern is printing, which continues to experience difficulties as the industry still adjusts to the move to digital communication. During the last six months the printing industry has recorded some large business failures including Vega Colour Group and Geon Australia.

Australian industries performance forecast

August 2013



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