

Navigator

Now, next and how for business

Australia report



Australia

Australia benefitting from rising incomes and links with Asia

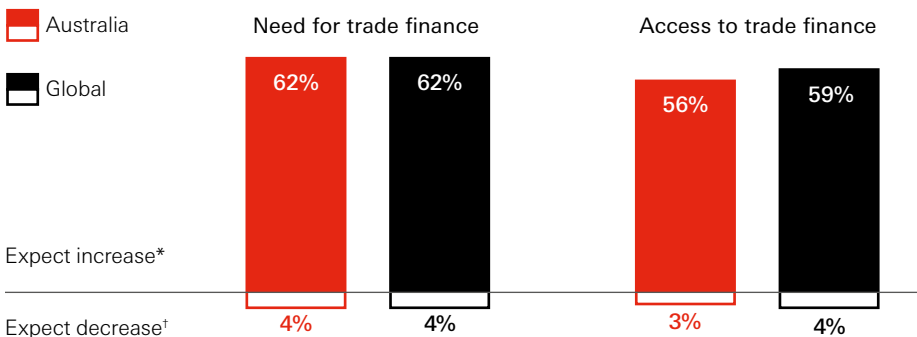
Increasing integration with Asia will continue to drive Australia’s exports. Commodity producers will continue to reap the benefit of growth in China’s economy (albeit at a slower pace) and will also see demand from other countries in the region (notably India) rise. The outlook for services and rural exports is also bright, with rising income levels in the region driving consumption. And there is upside risk to the outlook, with the recent agreement of the CPTPP and FTA negotiations with Indonesia close to being finalised.

Short-Term Snapshot

Australia’s economy is lagging behind other developed countries, with domestic demand growth still relatively subdued. But exporters are benefitting from the upturn in the global environment and a recovery in commodity prices. Although the government has been somewhat pre-occupied by political developments, they are pushing ahead with significant infrastructure investment (in transport and communications) and have recently agreed the CPTPP trade deal, which will improve trading conditions when implemented.

The outlook for Australia’s exports this year appears positive, underpinned by a further acceleration in the global economy and the coming online of LNG installations in Western Australia and the Northern Territories. Our outlook is shared by the survey respondents, with almost three quarters expecting to see growth in trade volumes this year, similar to other developed economies.

Outlook for trade finance need and access in the next 12 months



*Expect increase = Increase significantly + Increase slightly
 †Expect decrease = Decrease significantly + Decrease slightly

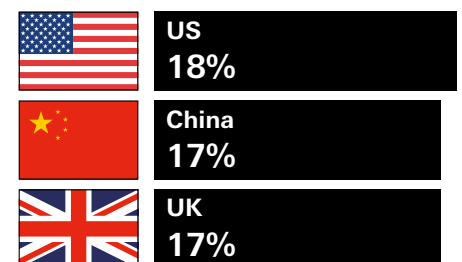
Source: TNS Kantar

Action points for business

- ◆ Look to take advantage of opportunities in the fast-growing Asia Pacific region.
- ◆ Ensure you are digital-ready for e-commerce opportunities, particularly in the service sector.

Upturn in global environment and recovery in commodity prices supported merchandise exports in 2017.

Which are the top 3 markets where your business will look to expand in the next 3-5 years?



Source: TNS Kantar

Although the economy is expected to slow, China will remain a key market in the near term, with 17% of respondents flagging it as a major source of growth. And after being a drag on exports for a number of years, developed economies will be a driver of growth in the near term, underpinned by expansionary fiscal policy in the US and accelerating domestic demand in the UK – 18% and 17% of respondents respectively are targeting these markets.

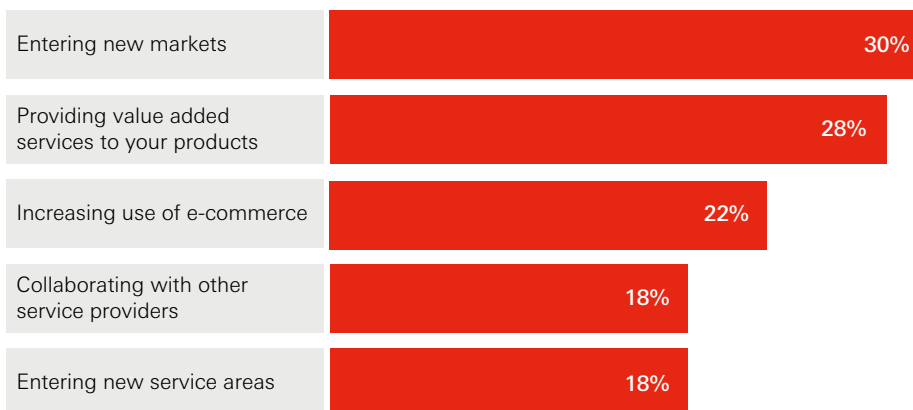
Businesses are generally well-placed to take advantage of external opportunities. Almost two thirds of respondents flagged the need to access trade finance and 56% expect their access to credit will improve. This will help facilitate export growth in the coming months, but more needs to be done to enable small businesses to use these facilities, with respondents flagging the size of their business as a key limiting factor on access.

Services are becoming an increasingly important component of trade, accounting for just over a fifth of exports in 2017. Within services, tourism and education are the largest components. Australia's natural beauty and vibrant culture makes it a popular tourist destination, and its world class universities have attracted over 500,000 students from abroad.

Respondents are positive about near-term prospects for expanding services trade, with 59% expecting volumes to increase in the next 12 months. Entering new markets and providing value-added services to existing products were the most common strategies identified by respondents for expanding their services business.

Services are Australia's second biggest export category, accounting for 22% of total export sales in 2017.

How do you plan to grow your services business?



Source: TNS Kantar



Trade Policy Developments

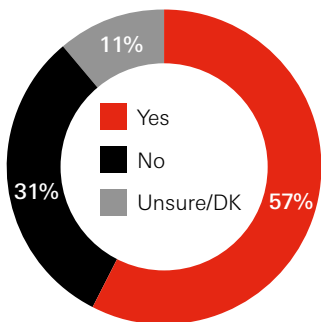
After seemingly being dead in the water following the US' withdrawal, the CPTPP agreement has been resurrected. The agreement covers 11 countries in the Asia-Pacific region, and was signed in March 2018. Australian farmers are set to benefit, with the agreement opening up the lucrative Japanese market to wheat and dairy imports, in particular. Service producers will also benefit from a reduction in non-tariff barriers to trade.

As a small open economy that is reliant on demand from abroad, Australian businesses are acutely aware of the benefits of reducing protectionism and barriers to trade. The economy is reliant on net inward migration to meet demand for key workers, with 34% of survey respondents flagging skills shortage as an unwelcome side-effect of protectionist policies, comfortably above the global average of 28%.

Action points for business

- ◆ Ensure you understand how the forthcoming CPTPP agreement will change the rules governing trade with member countries – and how your firm can capitalise on the opportunities.
- ◆ Keep abreast of Australia's ongoing trade negotiations and how they may affect your optimal business strategies.

Are governments becoming more protective of their domestic business?



Note: may not total 100% due to rounding

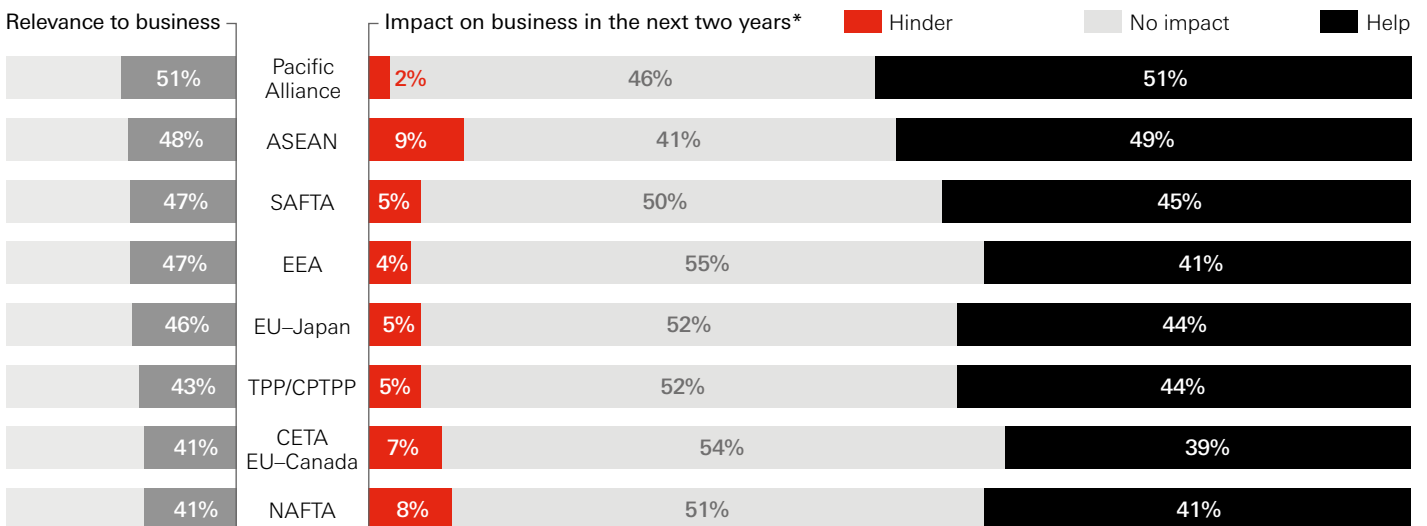
Source: TNS Kantar

Top 3 impacts of protective policies on my business



Source: TNS Kantar

Relevance and impact of trade agreements



Source: TNS Kantar

*May not total 100% due to rounding

Focussing on trade agreements, over half (51%) of respondents viewed the Pacific Alliance as being likely to have a positive impact on their business over the next two years. A similar proportion (49%) were also optimistic about the potential impact of ASEAN on business prospects.

Long-Term Outlook for Trade

Australia's natural resource endowment has inevitably resulted in commodities dominating goods exports. Coal and iron ore are the largest individual products, but the recent development of a number of LNG installations in Queensland, Western Australia and Perth has also driven up natural gas production and exports exponentially. Looking ahead, the sector will continue to dominate exports, with the composition of commodities set to evolve over time as technology and the pattern of economic development in Asia shift demand.

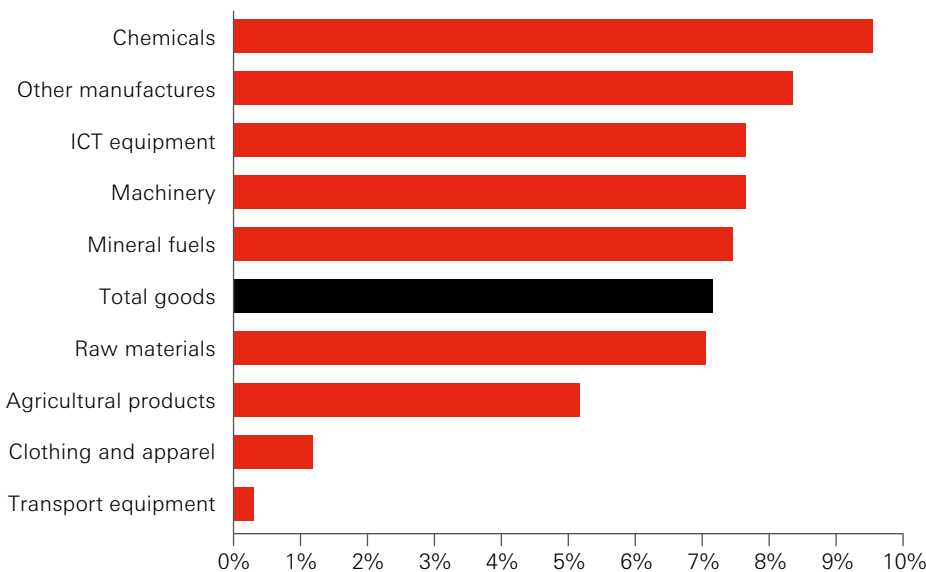
The success of the commodities sector has come at the expense of manufacturing. The appreciation of the AUD at the height of the commodities boom, when it broke through parity with the USD, and the relatively high level of labour costs (when compared to competitors in less developed economies) have eroded the competitive base of producers. As a result, manufactured goods account for only just over 10% of total exports and Australia is likely to continue sourcing many manufactured products from abroad.

While services exports have also been hampered by the overvalued AUD in the recent past, Australia's natural advantages (particularly in travel and tourism) and rising income levels in Asia have allowed exporting firms to overcome this. These strong fundamentals should continue to drive growth in the future, with services set to increase their share of total exports.

Commodities will continue to dominate goods exports

Although commodities will remain the largest component of Australia's goods exports, technological improvements, changing growth patterns and a drive to reduce emissions will alter the composition over time. Coal is set to grow slowly, as countries move to alternative, greener fuel sources; iron ore will also see comparatively slow growth, with China's economy shifting its focus away from heavy industry and construction activity. But other commodities are set to flourish. As the cleanest fossil fuel, natural gas will fill the gap left by coal, and the development of battery technology will increase demand for lithium. Economic development and the rise in incomes in Asia will also feed demand for copper, which is a key input into consumer goods such as fridges and washing machines.

Exports of goods by sector, 2017-30 (average annual growth)



Source: Oxford Economics

Action points for business

- ◆ Commodity producers will need to look for new markets as growth in demand from China moderates over the long run.
- ◆ Asia will remain the key market for services. Rising household income will drive demand, with new markets such as India, Vietnam and Bangladesh becoming increasingly important over time.
- ◆ Rural exports will also benefit from economic development in Asia, as households choose to switch their food consumption towards beef and other higher value agricultural products.

Asia will remain the key export destination, with new markets such as India and Vietnam increasing in importance.

Top 5 Hotlist destinations of goods exports

Rank	2016	2030
1	China	China
2	Japan	Japan
3	USA	India
4	Korea	Hong Kong
5	India	Korea

Note: Ranking among the 24 trade partners covered in the forecast

Source: Oxford Economics

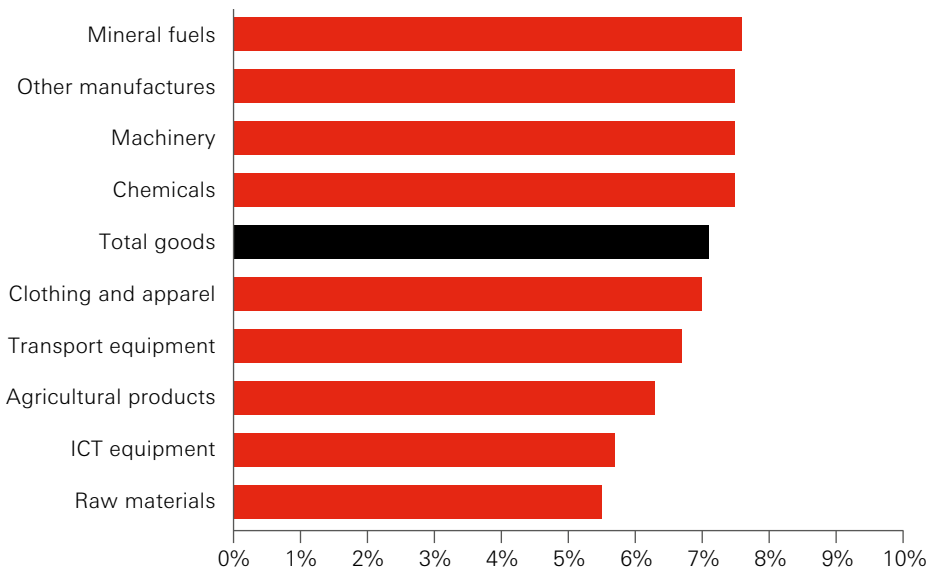
Beyond minerals and fuels, manufactured goods are likely to remain a small part of total exports. Comparatively high labour costs have hampered many sectors (particularly transport and clothing), but higher value-added sectors such as chemicals can still compete, and producers in sectors relating to agriculture (such as food processing) are also well-placed to take advantage of continued global growth. The signing of the CPTPP agreement would provide an additional boost to these sectors.

Asia is Australia's key export market, and with the region set to drive the global economy over the next decade it will absorb an increasing amount of Australia's goods. China will remain the single most important destination, but economic development (and the need for raw materials for construction and industry) will see growth in exports to Vietnam and India outpace China. Rising income levels in the region are also driving demand. As households in the region grow richer their consumption patterns are evolving, with a transition to higher quality food products and an increase in spending on consumer products. Australia's farmers (and food processing firms) are very well-placed to take advantage of these trends, with a reputation for high-quality produce.

Investment driving goods imports

The capital-intensive nature of resource extraction has resulted in construction materials, machinery, vehicles and other equipment dominating Australia's imports. Looking ahead, although we do not expect to see a repeat of the recent mining investment boom, the need to replace worn out equipment and expand productive capacity as demand rises is projected to drive imports over the next decade or so. As a result, other manufacturing (which includes iron and steel and non-ferrous metals), transport equipment, and machinery are projected to account for around 60% of the increase in imports from now to 2030. Oil will also remain significant, and is expected to account for 10% of the rise in imports in the long run.

Imports of goods by sector, 2017-30 (average annual growth)



Source: Oxford Economics

Consumers will also be an important source of demand. The end of domestic car production in October 2017 is likely to drive up vehicle imports (part of transport equipment), and the relatively high cost of domestically producing clothing and other consumer goods should drive imports of these products over the next decade or so.

Commodity firms' requirement for machinery, vehicles and other equipment is forecast to drive growth in imports

Top 5 Hotlist origins of goods imports

Rank	2016	2030
1	China	China
2	USA	USA
3	Japan	Korea
4	Germany	Japan
5	Singapore	Germany

Note: Ranking among the 24 trade partners covered in the forecast

Source: Oxford Economics

Developing Asia and North America are the largest suppliers of goods imports to Australia’s economy, accounting for over 75% of total inflows. We expect these relationships to be maintained and reinforced over the long run. The signing of the CPTPP agreement will further open up Australia’s economy to imports from the broader Asia-Pacific region (the agreement includes Canada, Mexico and Chile as well as key Asian economies). And the development and increasing dominance of Asian supply chains in manufacturing production coupled with the ability of new low-cost producers such as Bangladesh and Vietnam to supply consumer goods will cement the region’s position as a supplier to Australia.

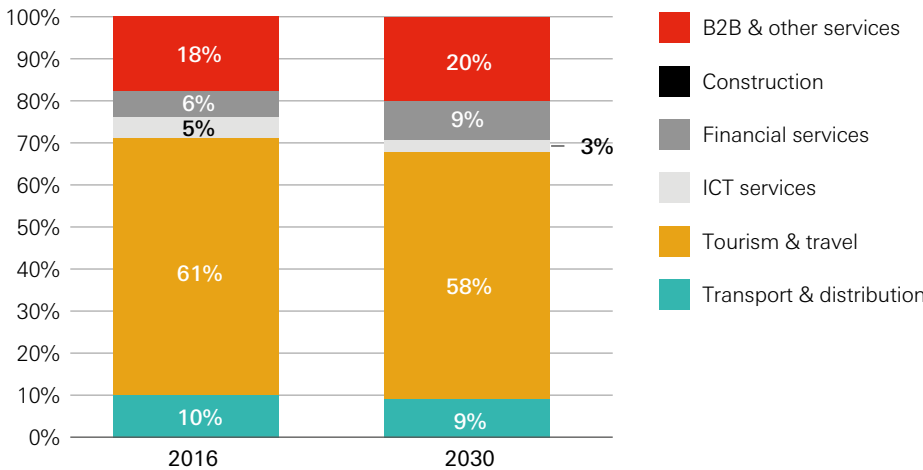
Business services are a small but rapidly-growing component of services exports

Tourism and travel will maintain competitive advantage

The combination of an attractive local environment and relatively good demand prospects will underpin rapid growth in services exports in the long run. Australia’s natural beauty and culture will remain attractive to tourists, and the high quality of the country’s universities will draw international students. Investment in transport and communications infrastructure will also help, by improving the economic environment and experience of visitors. Coupled with this the external environment is becoming more favourable over time – these services see their demand increase as household incomes rise, so the development of Asia over the long run will provide an additional boost.

Although currently a relatively small share of service exports, business services (including finance, accounting, legal, marketing and other support) are set to increase their share of the total over the coming decade. Australia’s relatively well-educated workforce (almost 40% of 25-34 year-olds hold a bachelor’s degree), good institutional environment and investment in new infrastructure provide businesses in this sector with an excellent platform with which to service clients globally. Additional investment (by the government and private sector) in digital technology and knowledge will be needed to allow businesses to take advantage of these new opportunities.

Sectoral shares in total services exports



Source: Oxford Economics

Top 5 Hotlist destinations of services exports

Rank	2016	2030
1	China	China
2	USA	USA
3	Singapore	India
4	UK	Singapore
5	India	UK

Note: Ranking among the 23 trade partners covered in the forecast

Source: Oxford Economics

Emerging markets will drive the growth in service exports over the long run. But demand is set to come from a relatively broad group of countries, with Argentina, Mexico and India joining the Asian powerhouses (India, Indonesia and China) in the top six fastest-growing destinations. Although developed economies will see naturally slower growth, in line with the broader economic outlook, the US and UK will remain inside the top five destinations for service exports. This reflects cultural ties and the absence of a language barrier, with firms in Australia easily able to service both businesses and consumers in these destinations. The potential to negotiate a free trade agreement (which includes liberalisation of the service sector) with the UK following Brexit represent a potential upside to the outlook for Australia-UK bilateral services flows.

About the HSBC Navigator

The HSBC Navigator presents a blend of survey evidence, policy analysis, and economic modelling to generate unique and timely insights into the changing landscape for global trade.

The business survey is a quantitative indicator of the short-term outlook for global trade. The survey, which is the largest of its kind, is conducted on behalf of HSBC by Kantar TNS. It is compiled from responses by decision-makers at over 6,000 businesses – from small and mid-market to large corporations – across a broad range of industry sectors in 26 markets. Interviewees were polled on a range of questions including expectations around future growth in trade, trade finance needs, attitudes toward trade policy developments and strategic business plans.

The survey represents a timely source of information on the fast-evolving trade environment. And it can provide a useful contextual setting for interpreting developments in official data. In this way, economists at Oxford Economics are able to blend insights from the survey with their own analysis and modelling of developments in trade.

Oxford Economics has tailored a unique service for HSBC which forecasts bilateral trade in goods and services, in part based on HSBC's own analysis and forecasts of the world economy. A top-down approach is employed, with Oxford Economics' suite of models used to ensure consistency between HSBC's forecasts for economic growth and exchange rates in key countries and the more granular projections for bilateral trade flows presented here.

Oxford Economics employs a global modelling framework, with headline bilateral trade forecasts constructed as a function of demand in the destination market and the exporter's competitiveness (as measured by unit labour costs in nominal USD terms). Exports, imports and trade balances are identified, with both historical estimates and forecasts for the periods 2017-20 and 2021-30.

These headline bilateral trade forecasts for goods and services are also disaggregated by sector, using Oxford Economics' Industry forecasts to inform future production trends and taking into account the historic relationship between output and exports in each sector, by market:

- ◆ For trade in goods, sectors are classified according to the UN's Standard International Trade Classifications (SITC) system at the two-digit level and grouped into 30 sector headings.
- ◆ For trade in services, we identify five broad sectors: B2B and other services, tourism & travel, transport & distribution, financial services, ICT services and construction.

Drawing on the Kantar TNS survey results and Oxford Economics' long-term forecasts, Oxford Economics produces in consultation with HSBC a global report and specific reports on the following 23 markets: Argentina, Australia, Bangladesh, Canada, China, Egypt, France, Germany, Hong Kong, India, Indonesia, Ireland, Japan, Malaysia, Mexico, Poland, Saudi Arabia, Singapore, Turkey, UAE, UK, USA and Vietnam. The analysis of trade in goods also includes trade with Brazil and Korea for a total sample of 25 key trading markets; for trade in services the analysis also includes Korea for a total sample of 24 key trading markets.

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