Euler Hermes Economic Research

Country Report

Australia

Enough tools to cope with the current challenges

General Information

GDP	USD1453bn (World ranking 12, World Bank 2014)
Population	23.5mn (World ranking 52, World Bank 2014)
Form of state	Federal Parliamentary Democracy (Commonwealth)
Head of government	Malcolm Turnbull (PM-elect after the ousting of Tony ABBOTT)
Next elections	2016, Senate and House of Representatives

Strengths

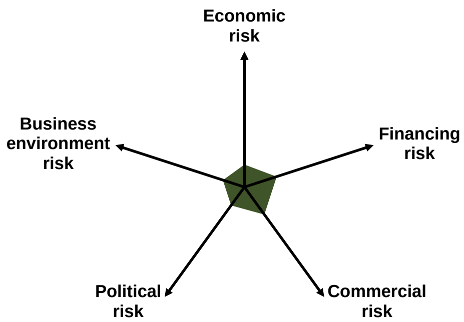
- Large natural resource endowments
- Strong infrastructure and business environment
- Proximity with Emerging Asia
- Strong economic performance

Weaknesses

- Dependent on Chinese demand and commodity prices
- Highly vulnerable to change in climate
- External vulnerabilities stem from chronic current account deficit and high external debt
- High household's debt

Country Rating

AA1



Source: Euler Hermes

Trade Structure

By destination/origin (% of total)

Exports		Rank		Imports
China	30%	1	18%	China
Japan	19%	2	12%	United States
Korea, Republic of	8%	3	8%	Japan
India	5%	4	6%	Singapore
United States	4%	5	5%	Germany

By product (% of total)

Exports		Rank		Imports
Metalliferous ores	30%	1	16%	Petroleum products
Coal, coke and briquettes	17%	2	13%	Road vehicles
Gold	6%	3	5%	Industrial machinery
Gas	6%	4	5%	Specialised machinery
Petroleum products	6%	5	5%	Electrical machinery

Source: ITC, Chelem

Economic Overview

Structural change in growth pattern

GDP growth is set to remain solid but below trend. After growing by +2.7% in 2014, Australia is set to slow to +2.0% in 2015. Q2 2015 was marked by a significant slowdown in GDP growth from +0.9% in Q1 to +0.2%. Falls in commodity prices and the deceleration of Chinese demand continue to weigh on exports. Investment is still adjusting as the economy is going through a structural adjustment following the end of the mining boom. Private consumption is holding strong supported by improving employment and lower saving rates.

Going forward, the pace of growth is set to remain fragile. The economy is adapting to lower global demand from its main partners (China), and has to find new growth drivers outside the mining sectors. Net exports is set to remain a key growth driver in the short run benefiting from lower imports of capital goods and progressive pick up in exports (volume of mining and services exports) as a lower AUD/USD improves price competitiveness. Furthermore, the accommodative monetary policy stance should allow for a gradual rebalancing in investment with a steady expansion in non-mining investment (construction and services). Private consumption is set to grow at a solid pace but below trend, limited by high household debt: debt to income ratio is 156% in Q1 2015.

Stimulating monetary policy and lowering the rate of fiscal consolidation

In a context of globally low inflation and commodity prices, the Reserve Bank of Australia kept its key interest rate relatively low (2% in Q2 2015) to stimulate the economy and to keep inflation in the target range of 2% to 3%. This accommodation is likely to be maintained until growth stabilizes at a robust level (around +2%). Inflation is expected to ease to 1.5% in 2015. On the currency side, The AUD is set to remain at a low level reflecting diverging trends in monetary policy between the FED and the RBA, and Australian authorities' intention to foster export growth.

On the fiscal front, the rate of consolidation is likely to be lowered. Australia's relatively low public debt exceeded 30% of GDP in 2014 but is still low compared with other advanced economies. The public deficit has increased since 2009 reflecting government action to keep growth in a decent range. While the current stance is to consolidate public finances (medium term target is to reach a fiscal surplus by 2020), the government is likely to adopt a flexible stance, allowing deviation around the current target (-2.1% of GDP is the target for FY2015-2016).

Current account deficit will remain large in 2015

The current account deficit is expected to increase to -4.0% of GDP in 2015 from -3.0% in 2014 reflecting lower external demand and negative price shocks from commodities. Export diversification, firmer external demand and progressive commodity price normalization should allow a gradual reduction in the deficit from 2016 onwards. Australia's external debt is still elevated (above 100% of GDP). Sustainability risk should be contained in the short run due to strong governance and the sound economic outlook.

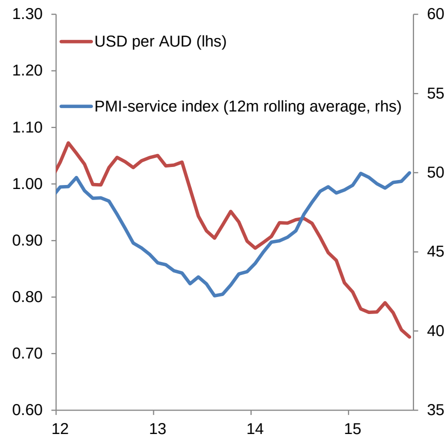
Key economic forecasts

	2013	2014	2015	2016
GDP growth (% change)	2.1	2.7	2.0	2.2
Inflation (%, yearly average)	2.4	2.5	1.5	2.2
Fiscal balance (% of GDP)*	-2.8	-2.5	-2.4	-2.0
Public debt (% of GDP)*	30.7	34.3	39.0	40.5
Current account (% of GDP)	-3.4	-3.0	-4.0	-3.2
External debt (% of GDP)	91.8	95.7	100	102

* 2013 refers to FY2013-14
** Public debt refers to General government debt, IMF

Sources: National sources, IMF, IHS, Euler Hermes

Currency and confidence in services



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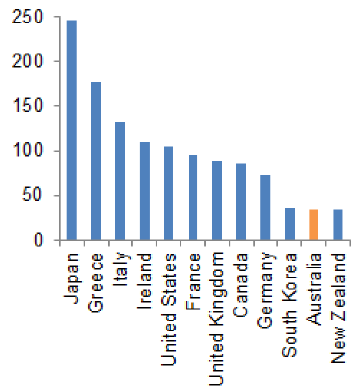
Public Debt (% GDP)



Sources: IMF, IHS, Euler Hermes

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