

Asian Economics

Australia's next growth driver

The rise of the services sectors

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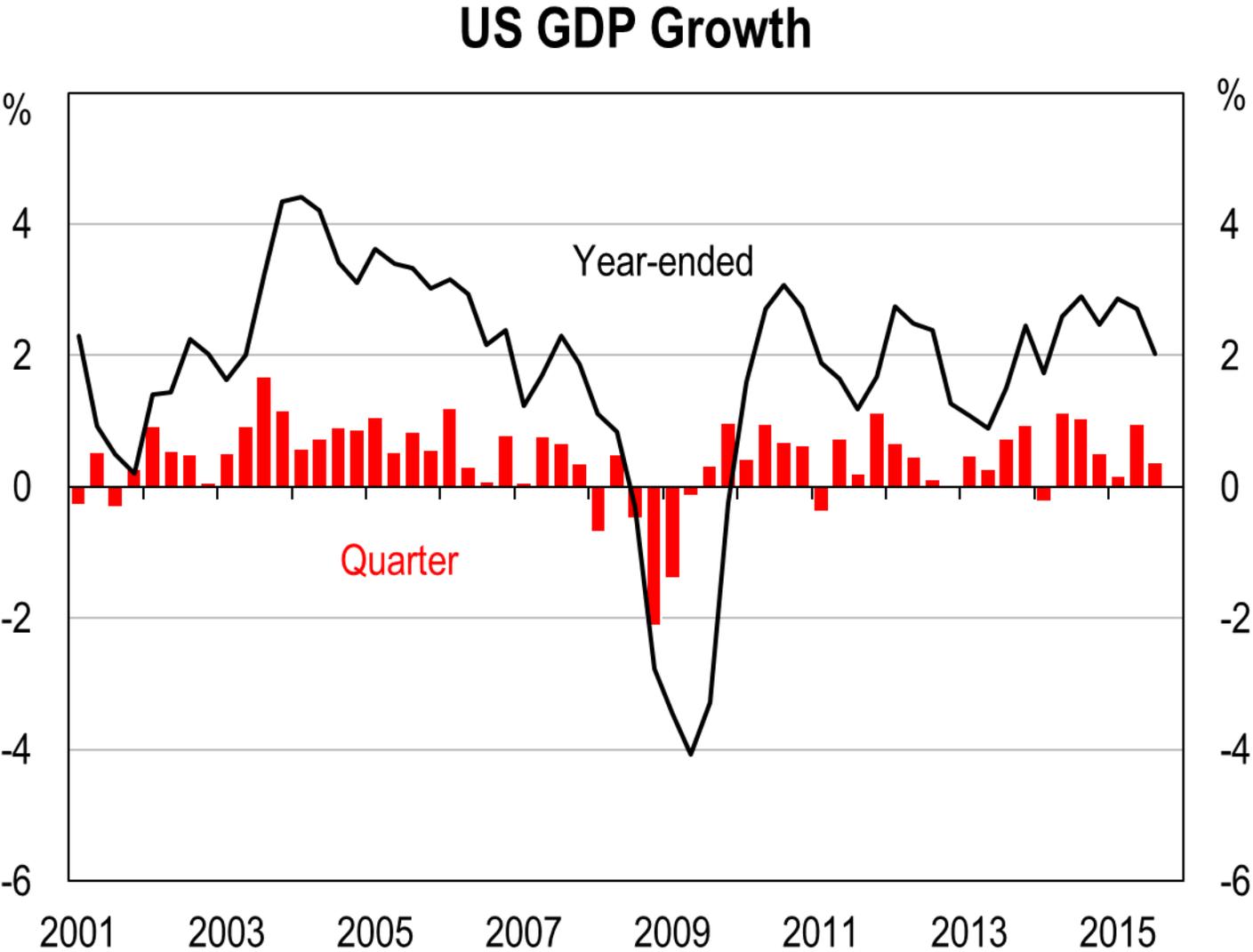
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HSBC 
Global Research

Global themes

- **US: All eyes are on the Federal Reserve and its next move**
- **Europe: Indicators have picked up, but many structural challenges remain**
- **China: Growth is slowing and shifting from investment to consumption**
- **India: Growth is lifting and is set to outpace Chinese growth this year and next**
- **Asia: Weak global trade is weighing on the smaller Asian economies**
- **Latin America and Africa: Doing poorly as the commodity crunch gets painful**
- **Global: Global trade is weak, commodity prices are down and inflation is low**

US GDP is growing at about its trend pace

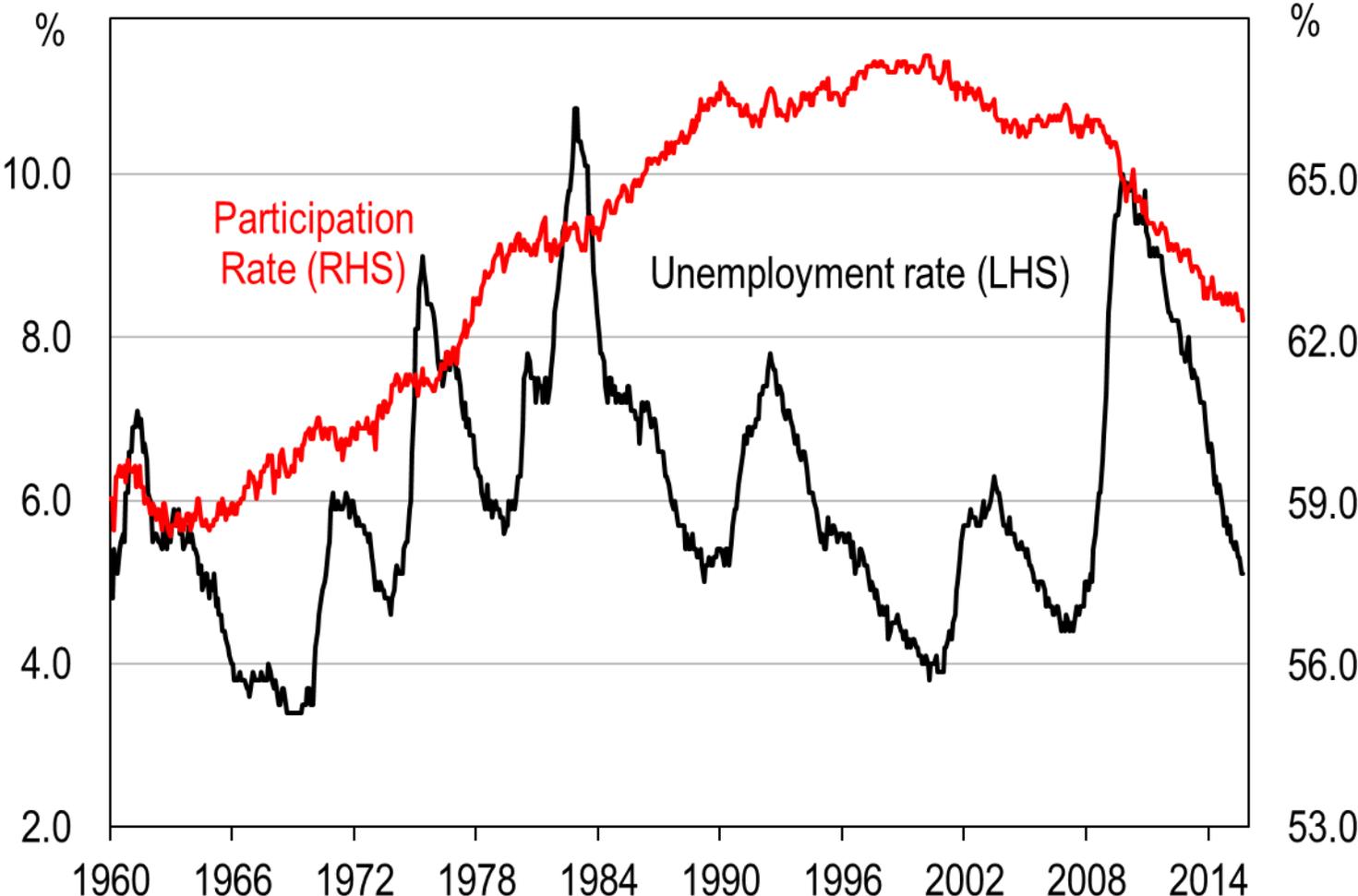


Source: BEA



The US labour market is close to full employment

US Labour market Seasonally adjusted



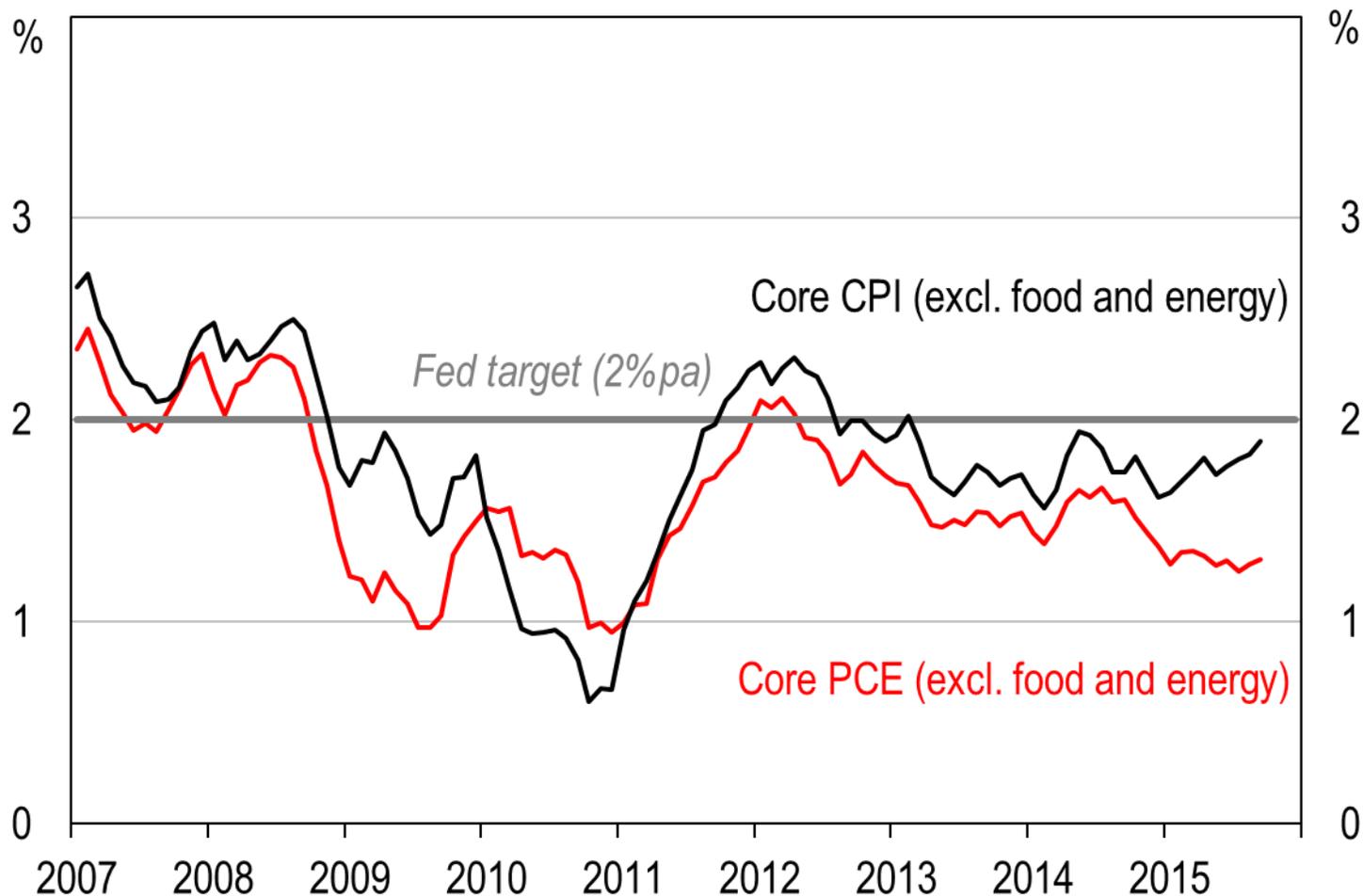
Source: Thomson Reuters Datastream



CPI inflation remains low and is below the Fed's target

US Core Inflation Measures

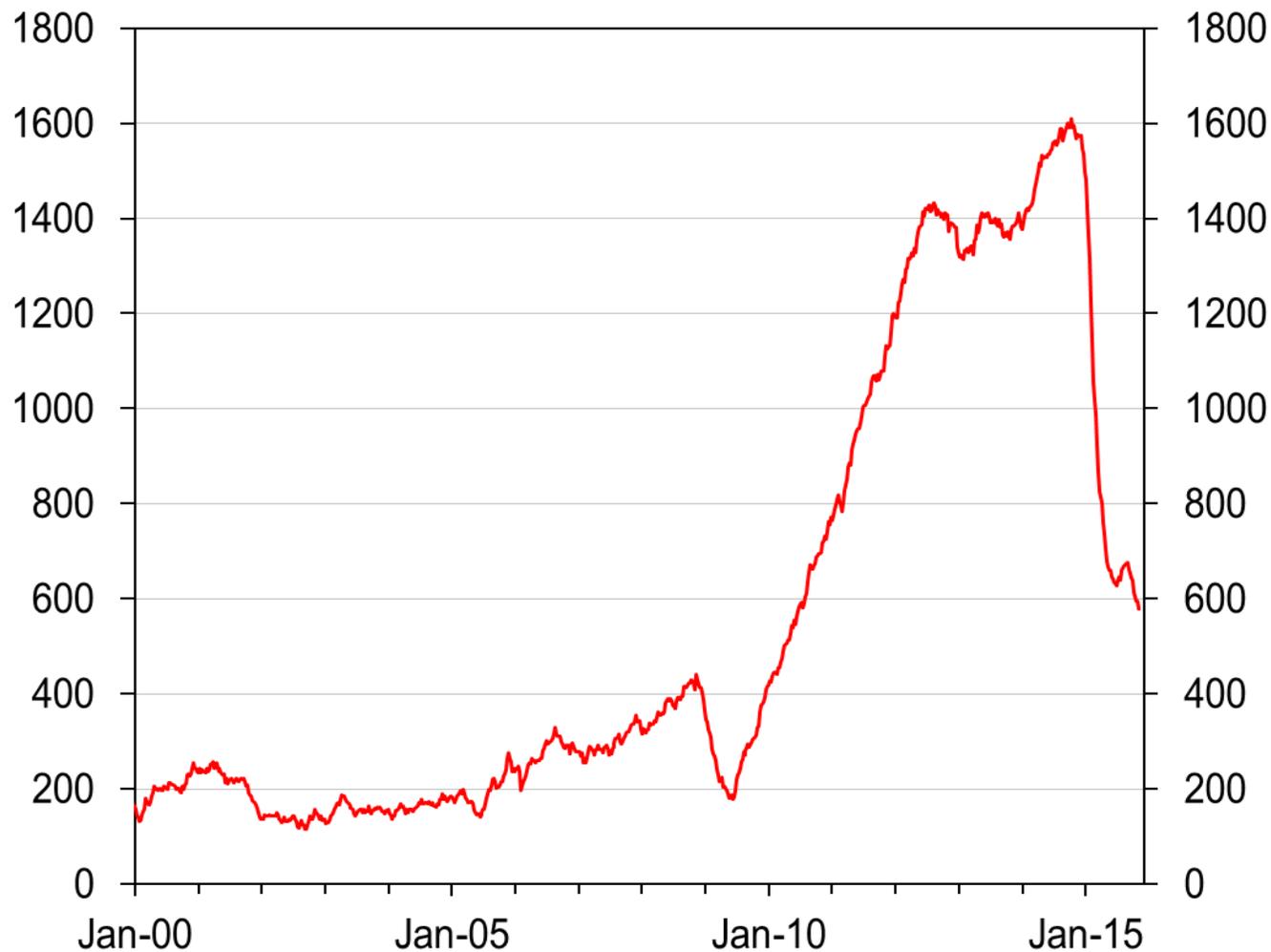
Year-ended change



Source: Thomson Reuters Datastream

A sharp fall in investment in oil production has been a headwind for the US

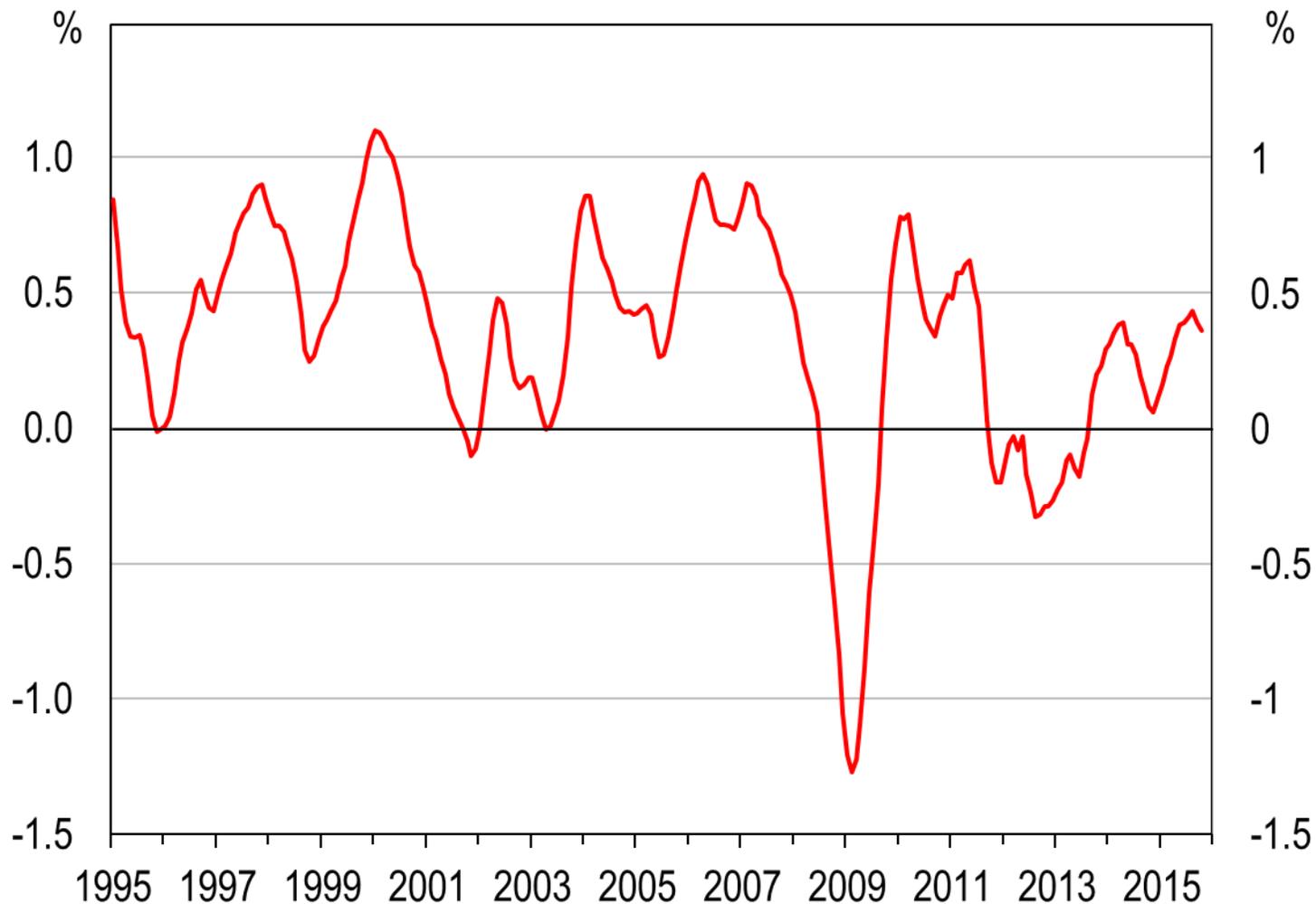
US Oil Rig Count



Source: Bloomberg

Timely indicators are lifting in Europe, supported by lower oil prices

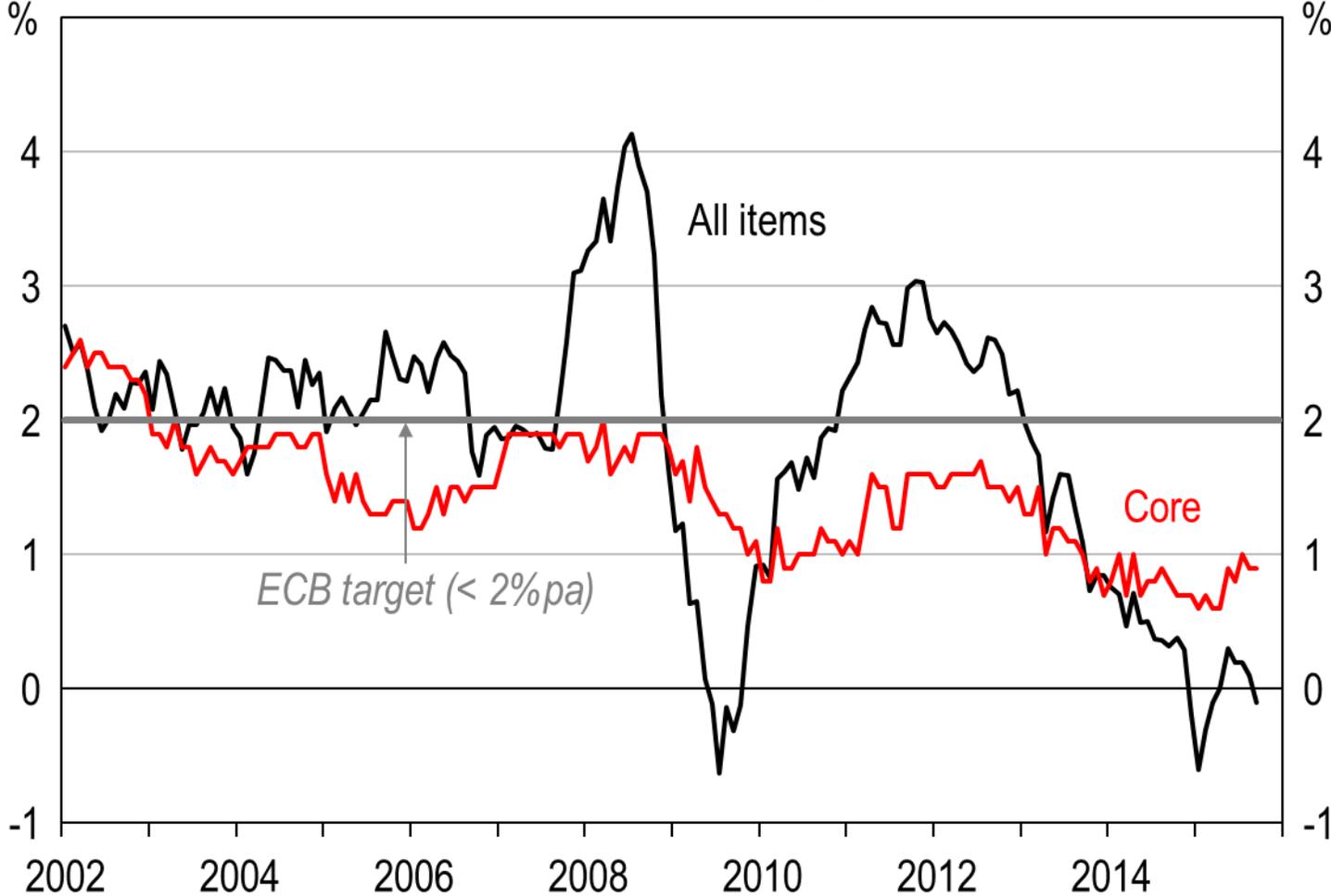
European Coincidence Indicator (EuroCOIN)



Source: Thomson Reuters Datastream

European core inflation has started to lift

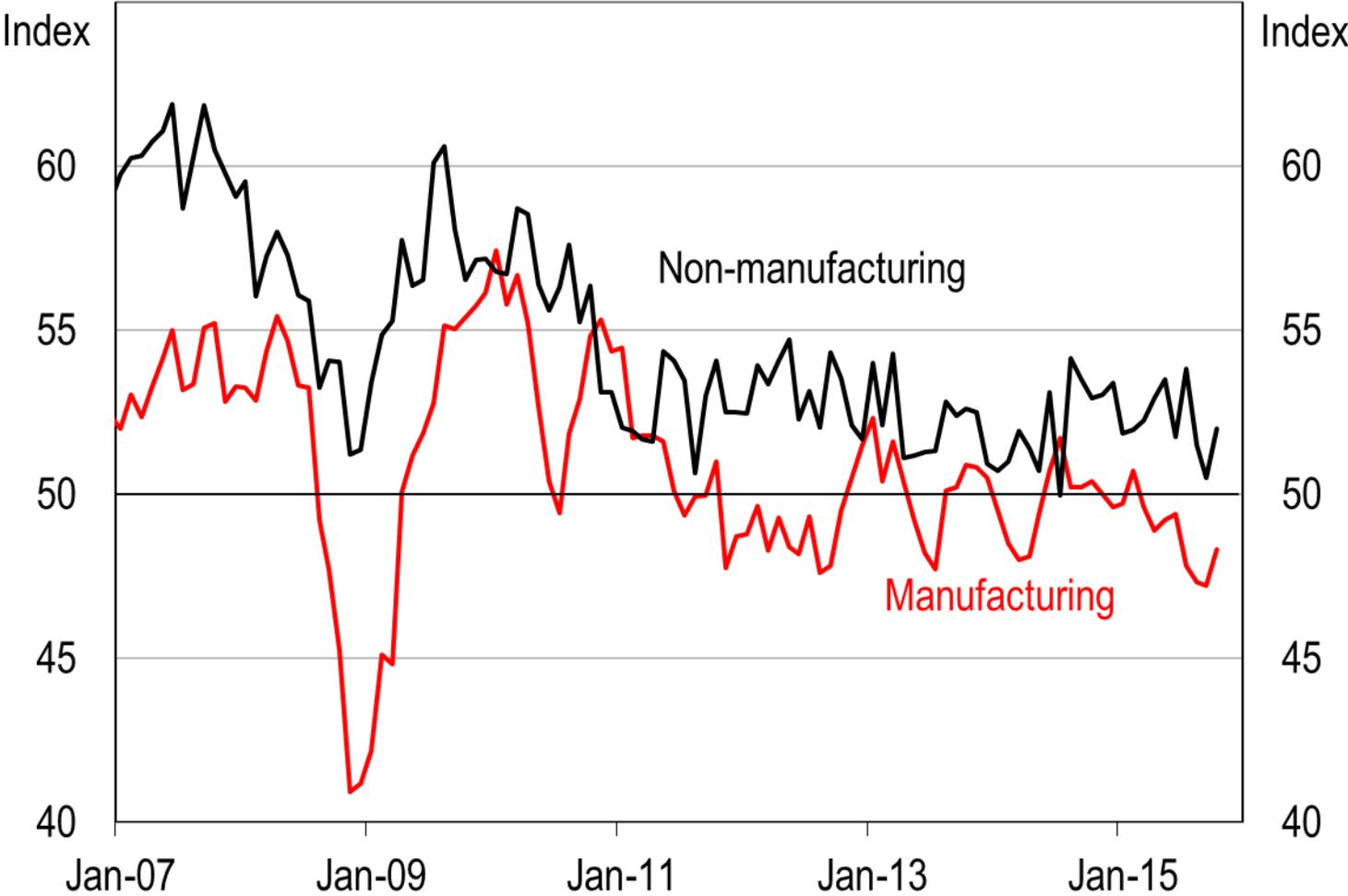
EU Inflation - HICP Year-ended change



Source: Thomson Reuters Datastream

China's economy is growing more slowly than in the past

Caixin China PMIs

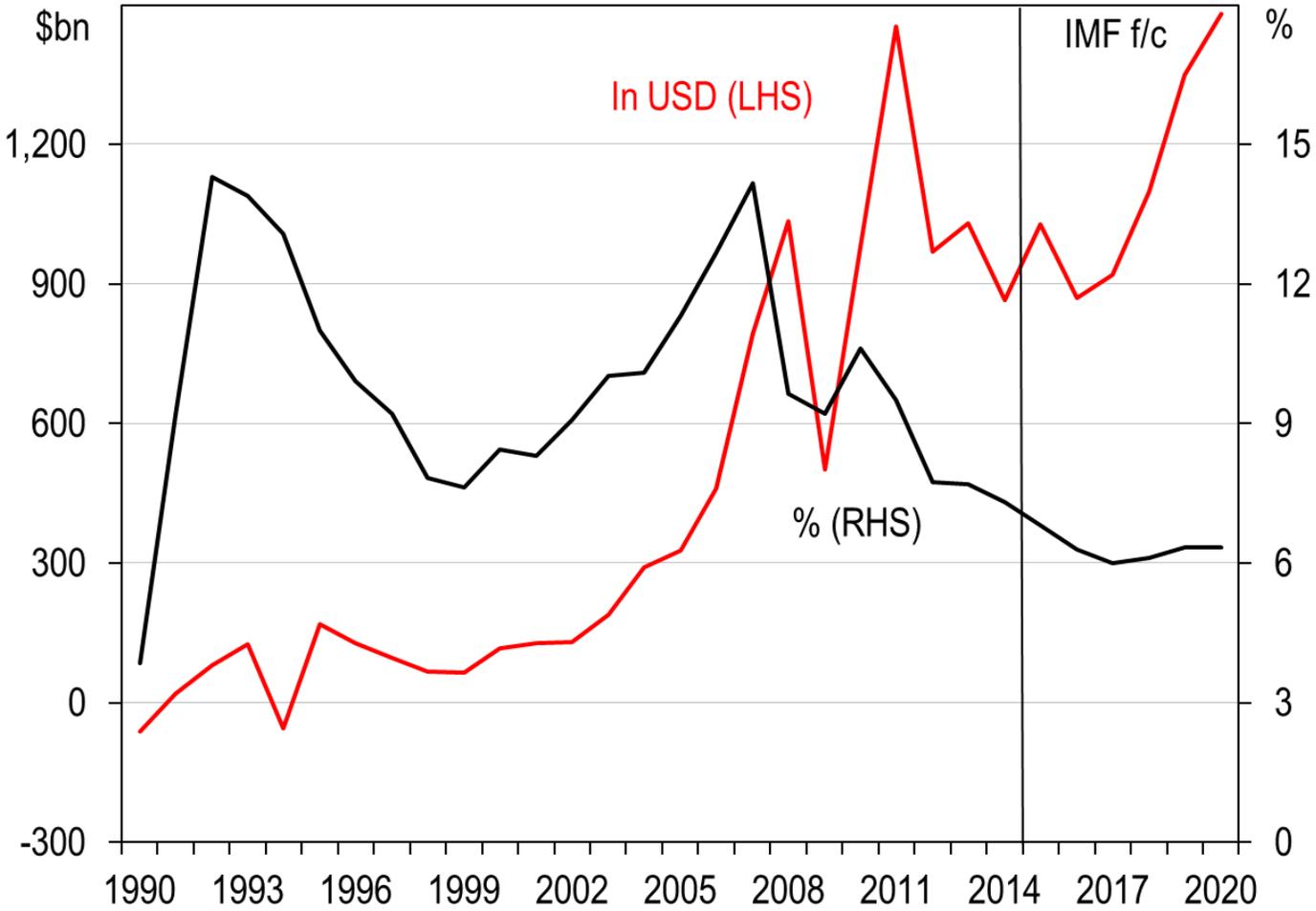


Source: Bloomberg, Markit



Despite slowing down, China is still contributing a lot to global GDP

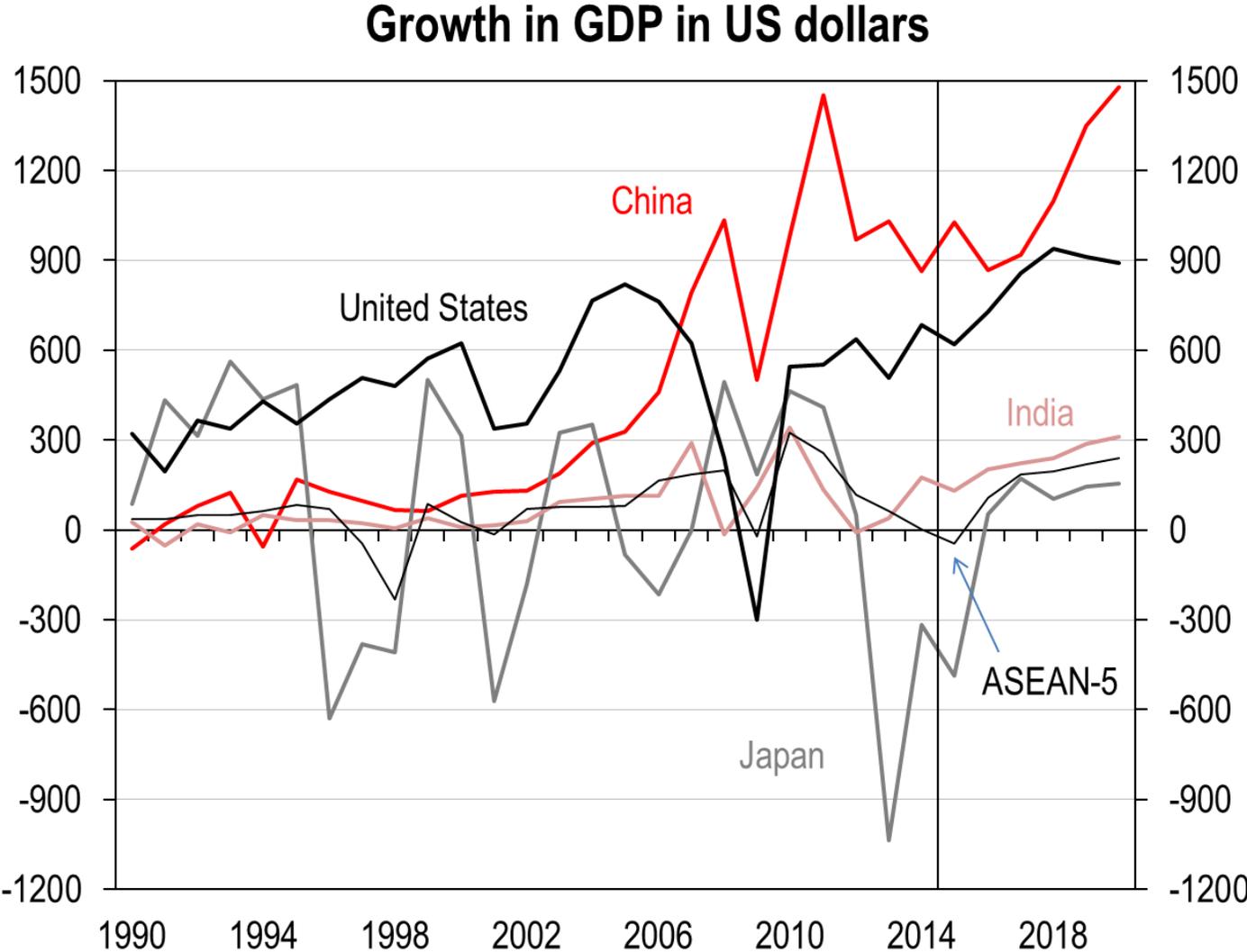
Chinese GDP growth



Source: IMF



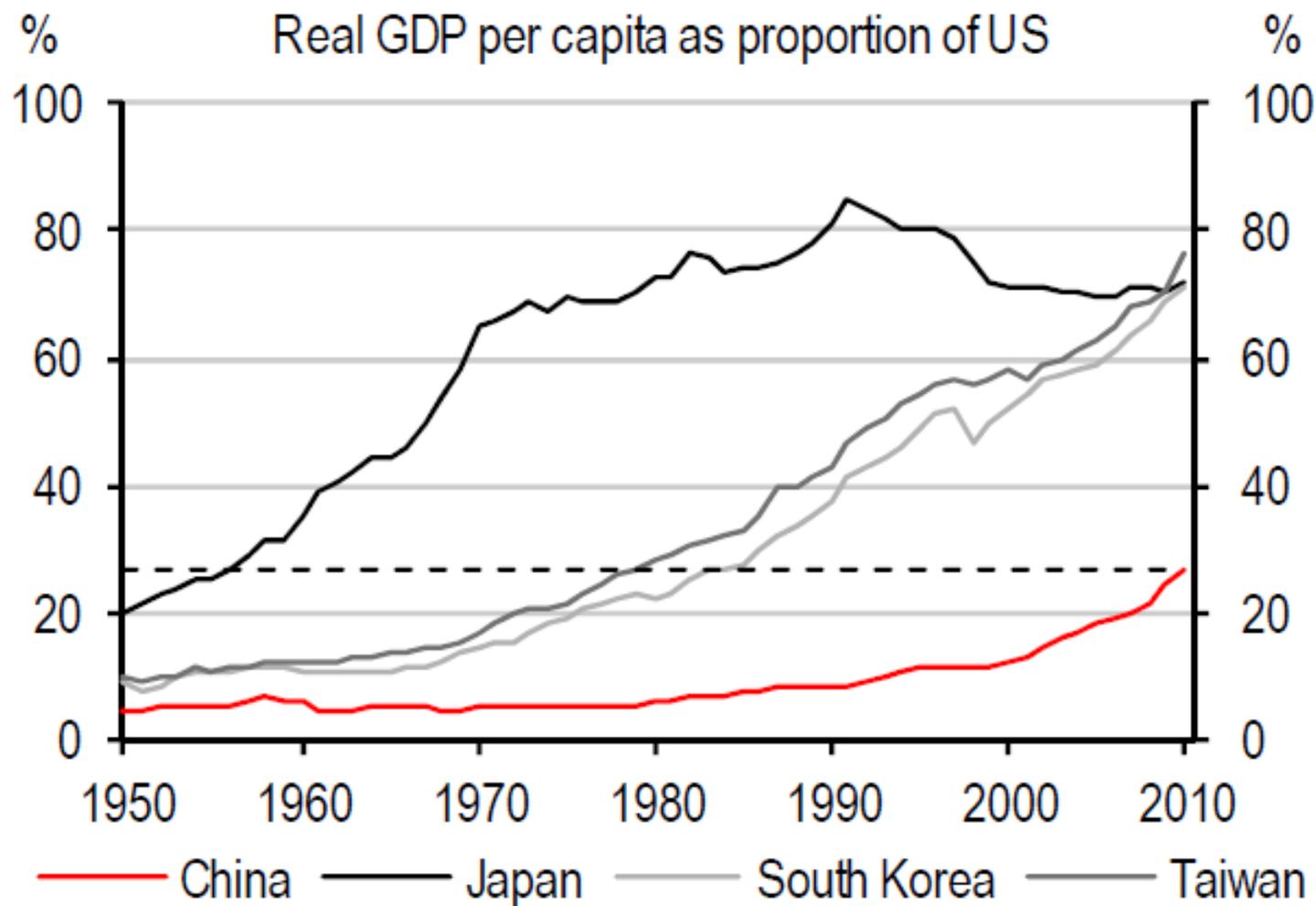
China is still contributing the most to global GDP growth



Source: IMF

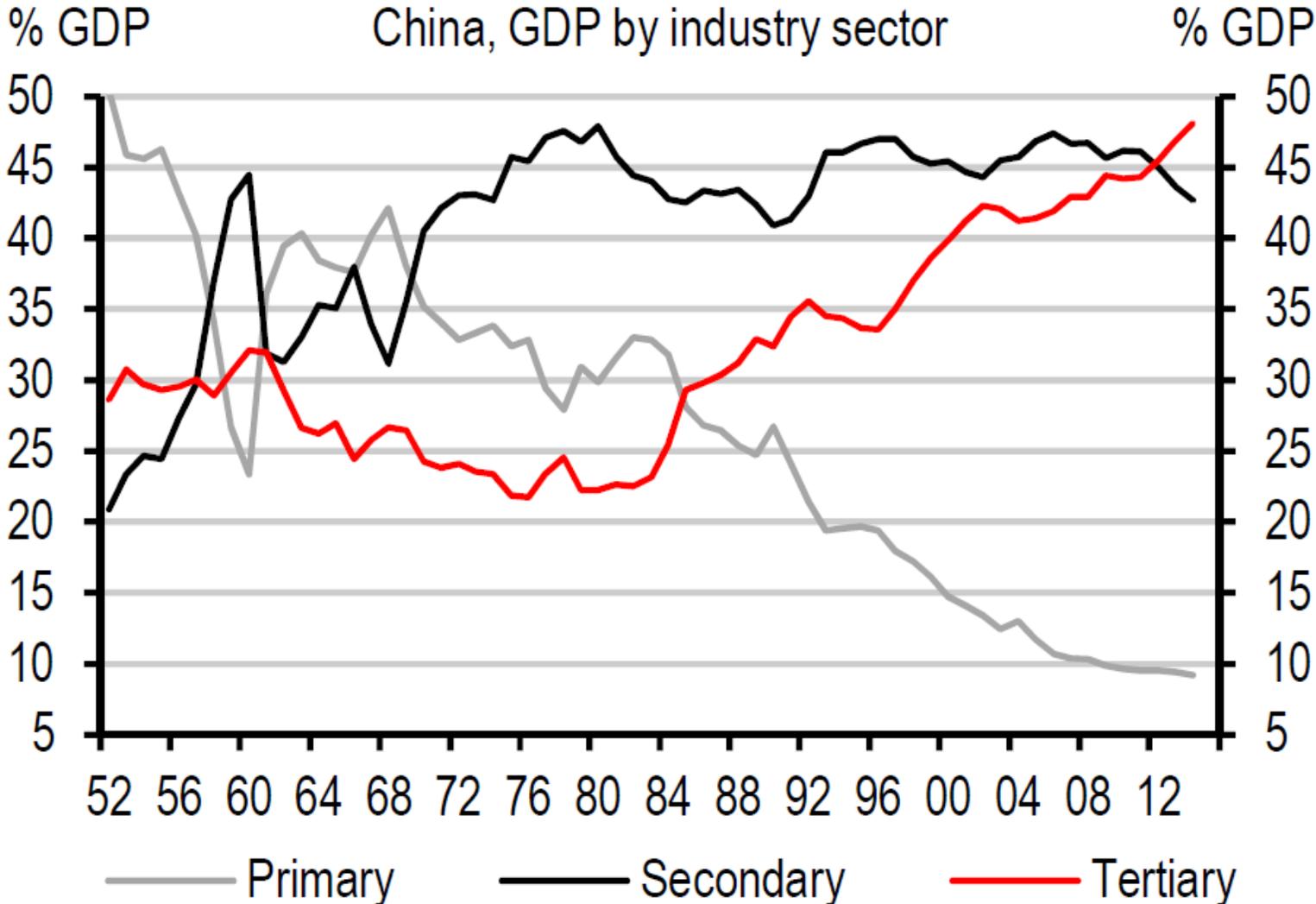


China still has a significant amount of catch up ahead of it



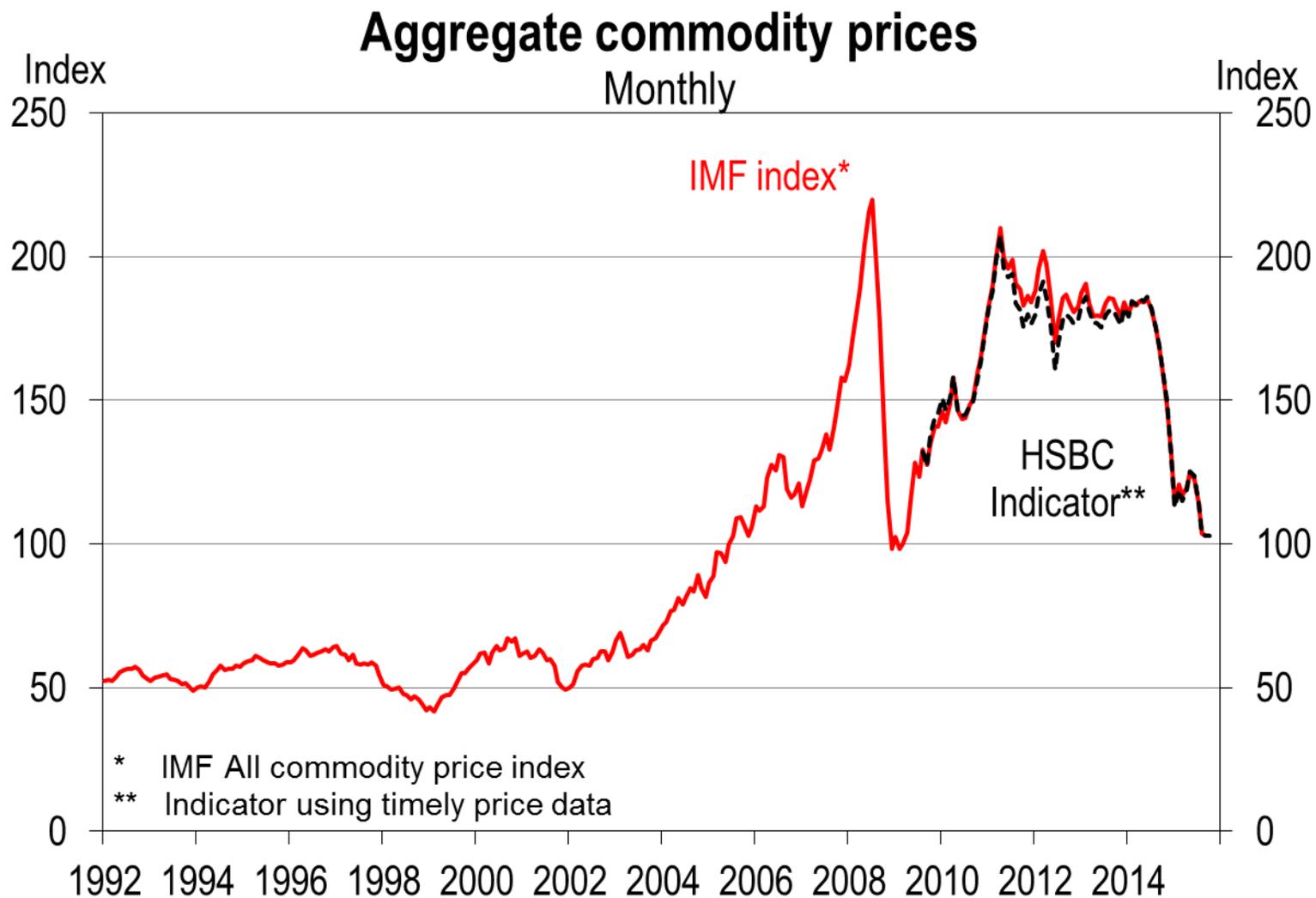
Source: Maddison Project

China's catch-up has implications for the drivers of growth



Source: Chinese National Bureau of Statistics

Commodity prices have fallen sharply, led by the sharp decline in oil prices

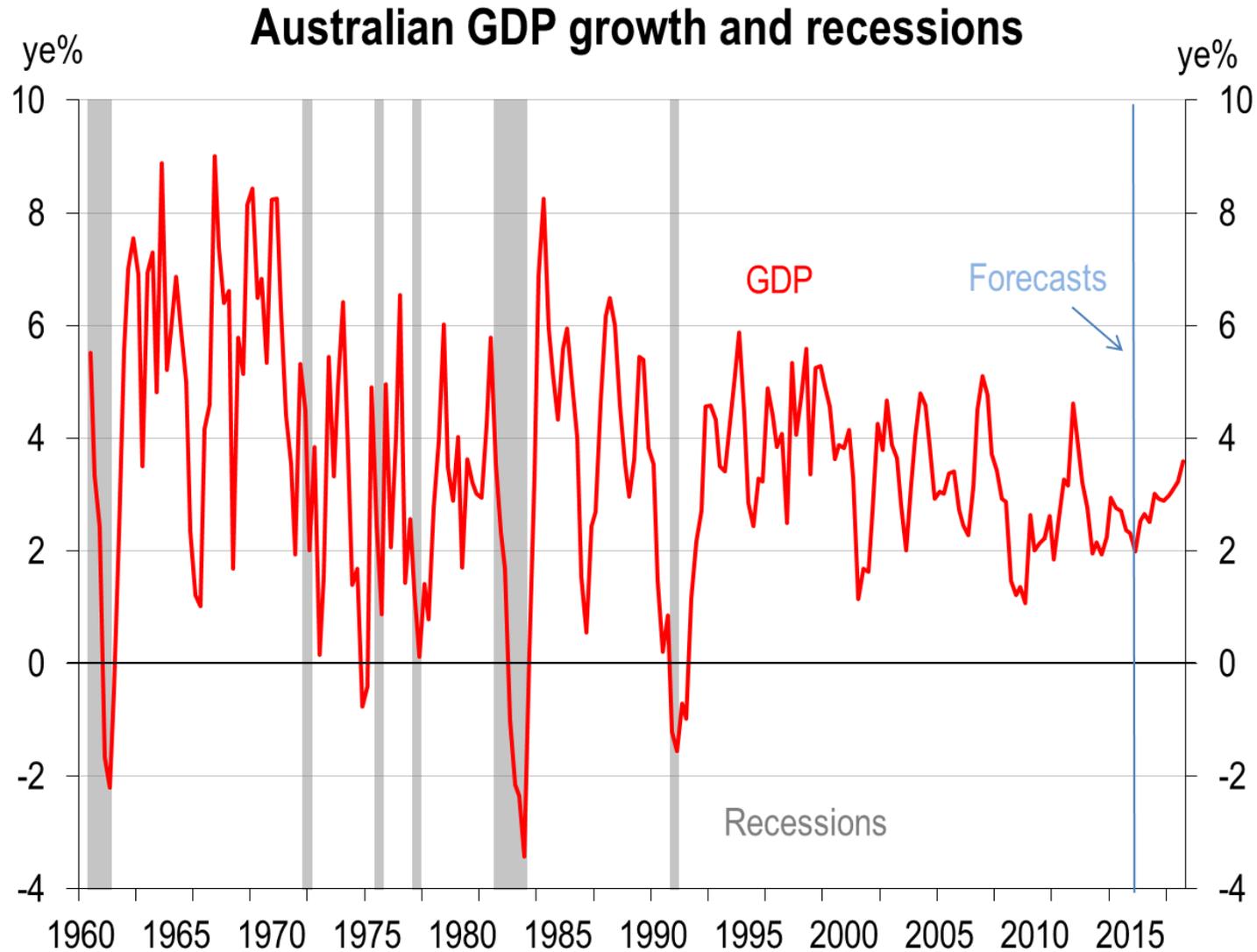


Source: Thomson Reuters Datastream, IMF, HSBC estimates

Australia's next growth driver: the services sectors

- **Mining investment and commodity prices have fallen**
- **Resource export volumes are ramping up, particularly LNG exports**
- **Low interest rates are supporting housing construction and retail sales**
- **Business conditions are improving, which could lift investment**
- **The lower AUD is supporting education and services exports**
- **Jobs growth is picking up as more people are employed in services**
- **Reform is needed to lift competitiveness and the potential growth rate**

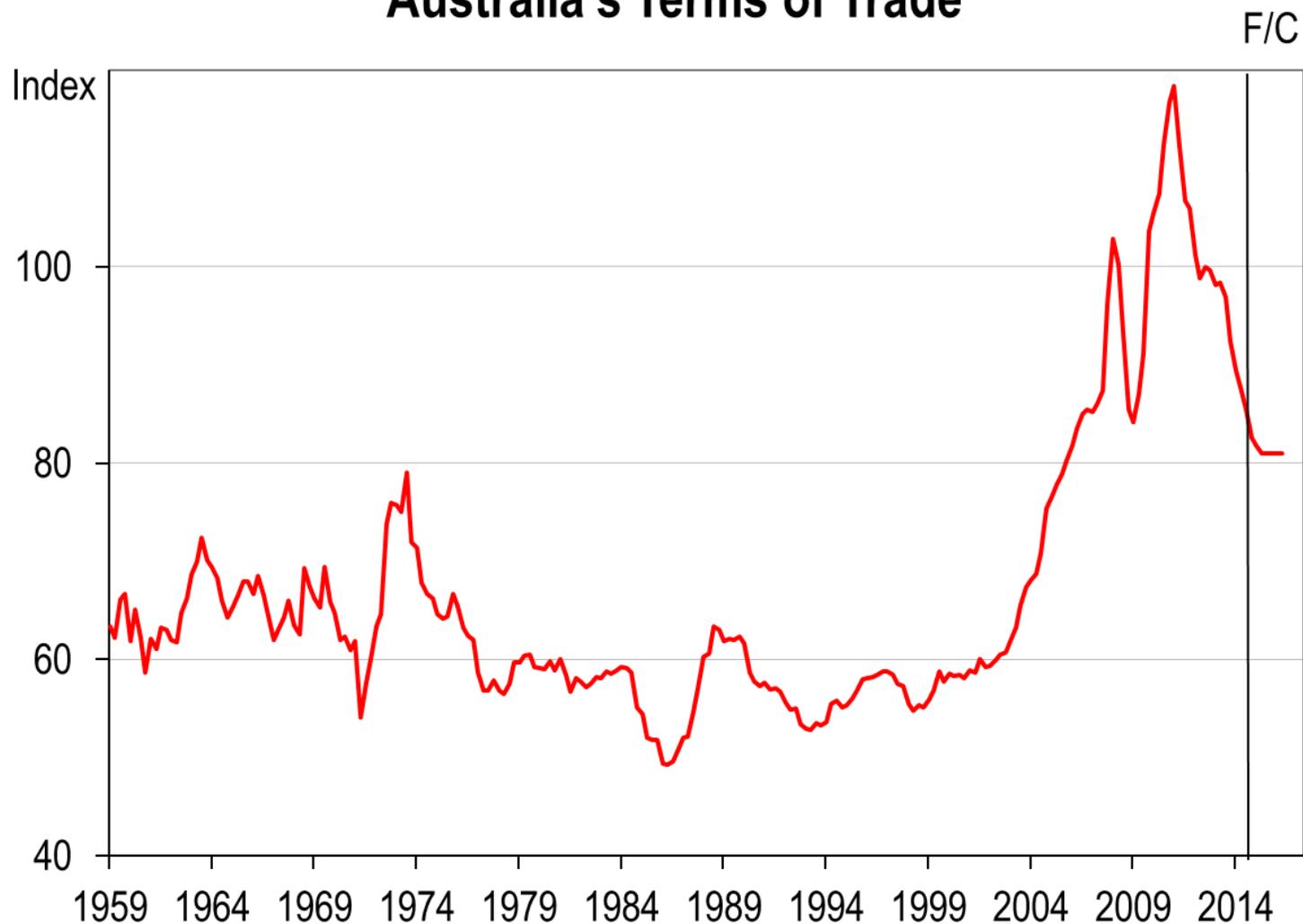
Australia is in its 25th year of continuous GDP growth



Source: ABS, HSBC estimates

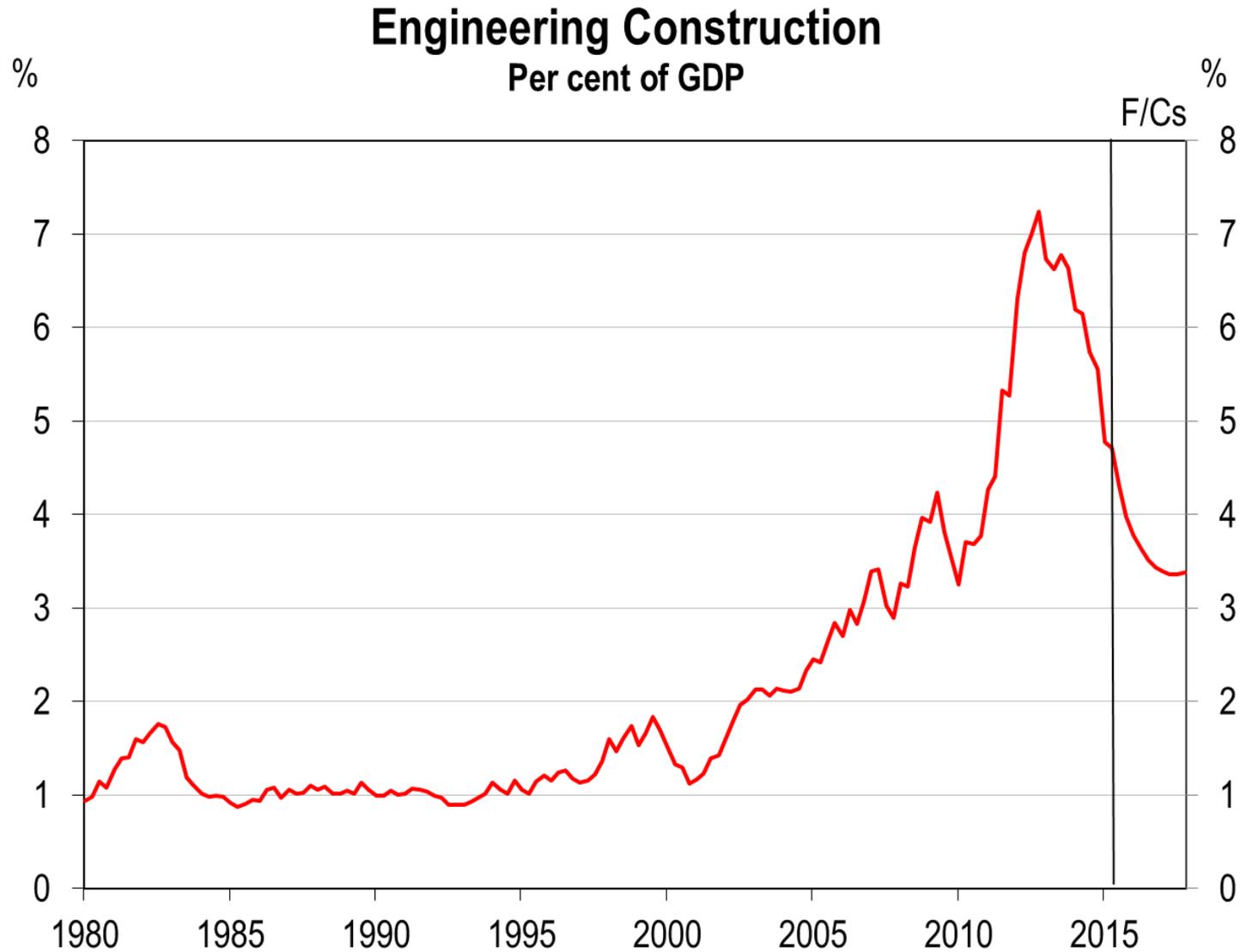
Australia saw the largest commodity price boom in its history

Australia's Terms of Trade



Source: ABS, HSBC estimates

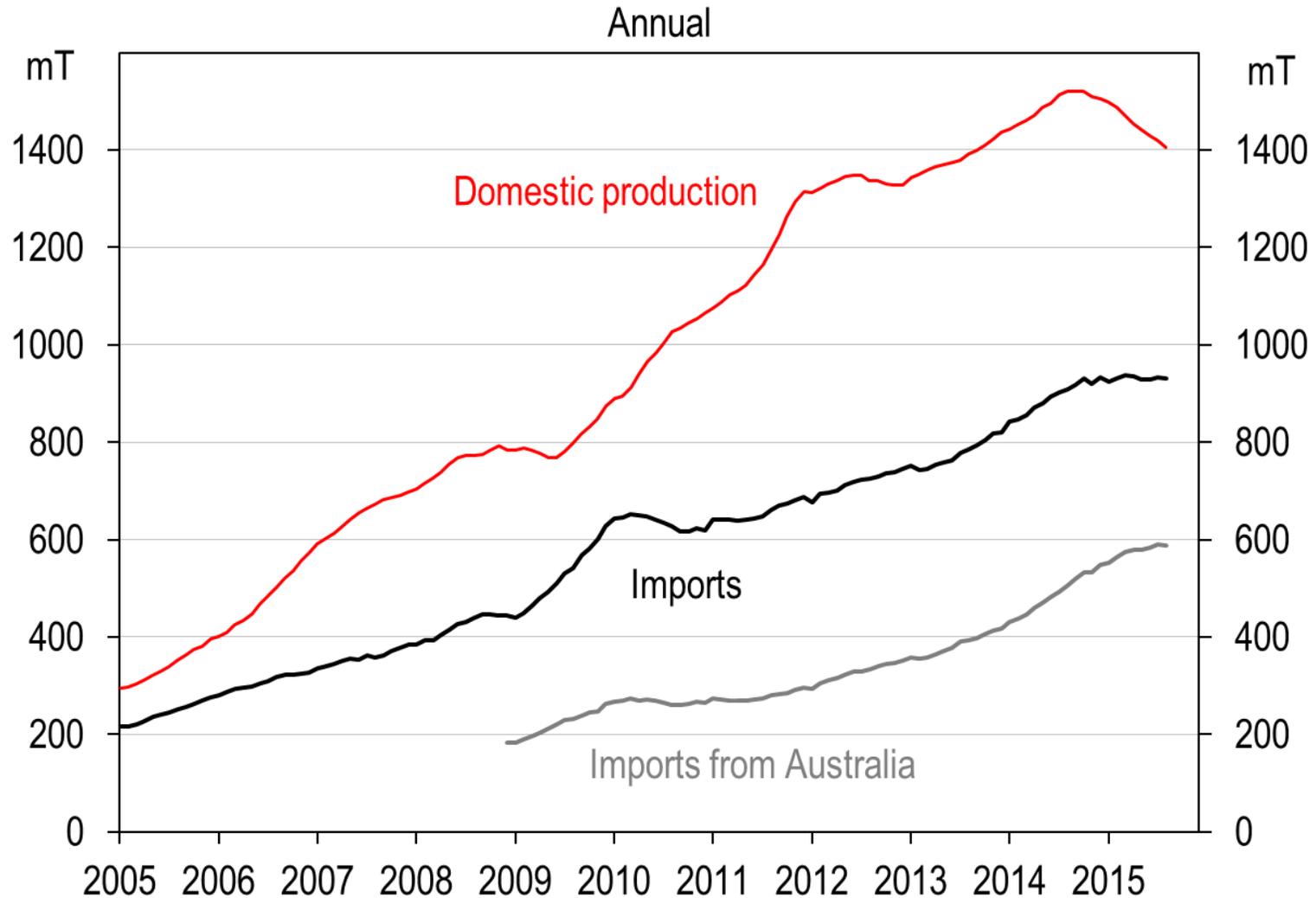
Mining investment rose to a record share of the economy



Source: ABS, HSBC estimates

Despite the weaker demand, Australia has had rising iron ore export volumes

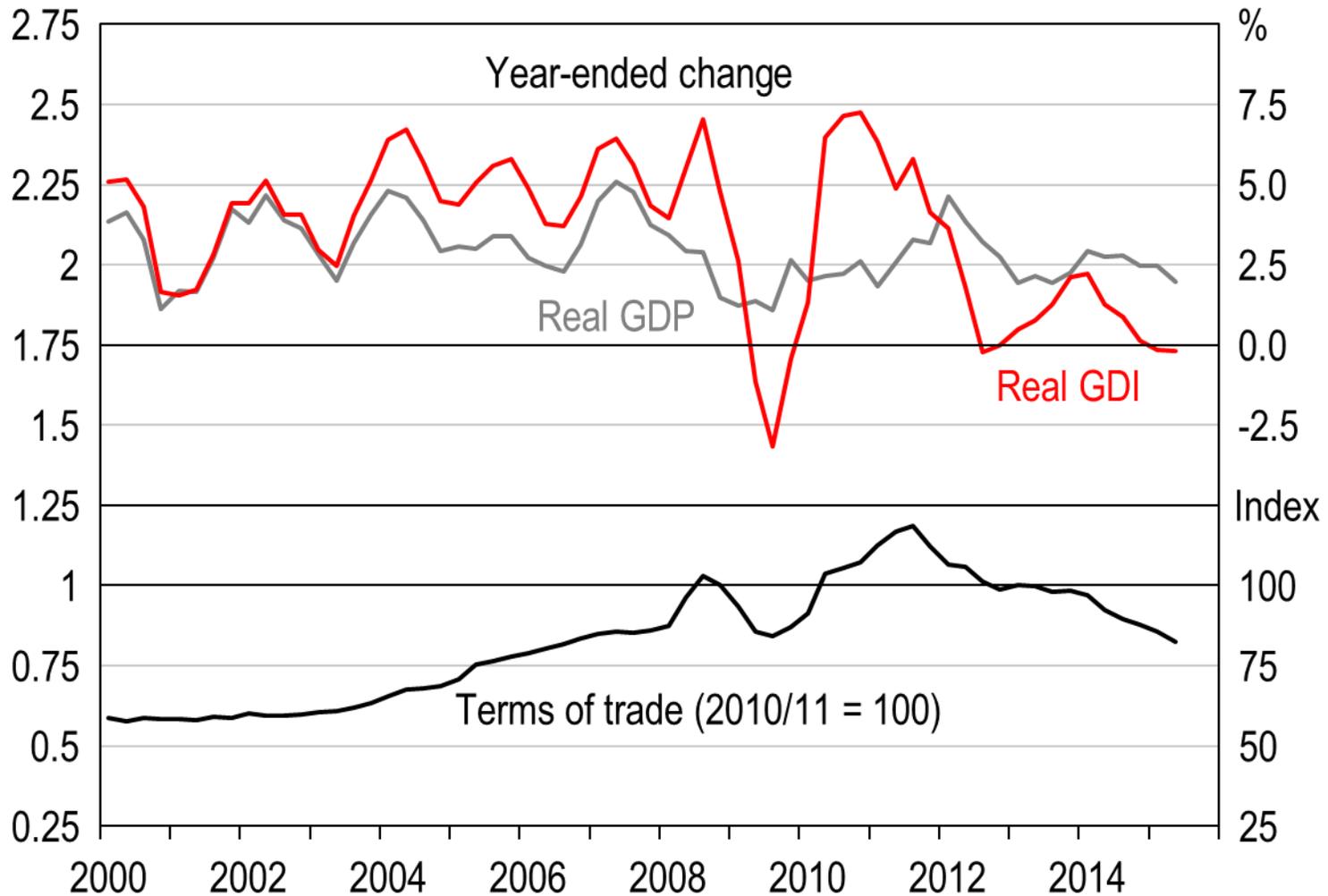
Chinese Iron Ore Production and Imports



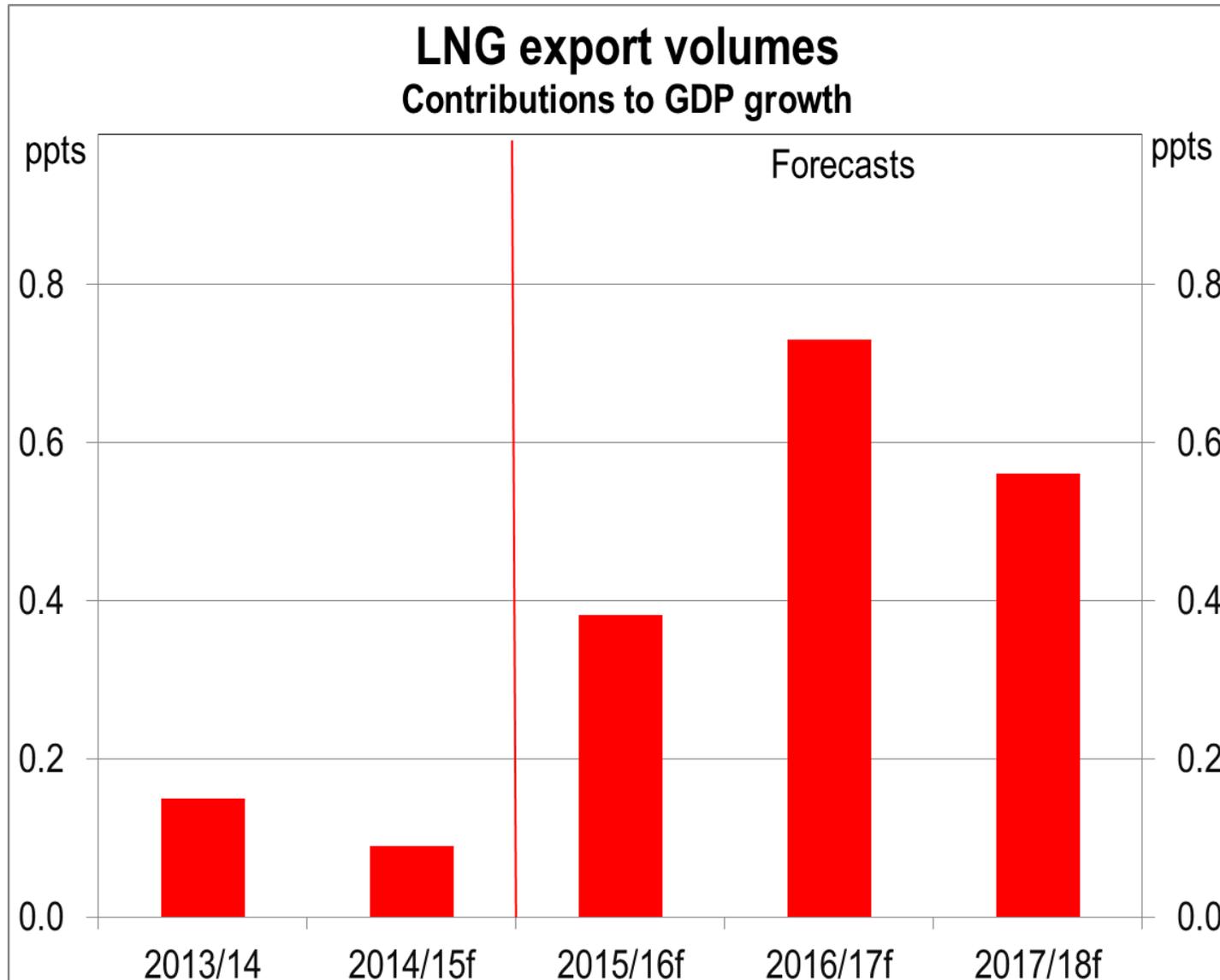
Source: CEIC

Income growth has slowed, as commodity prices have fallen

Growth in Income and Output



Resources export volumes still rising, led by a ramp-up in LNG

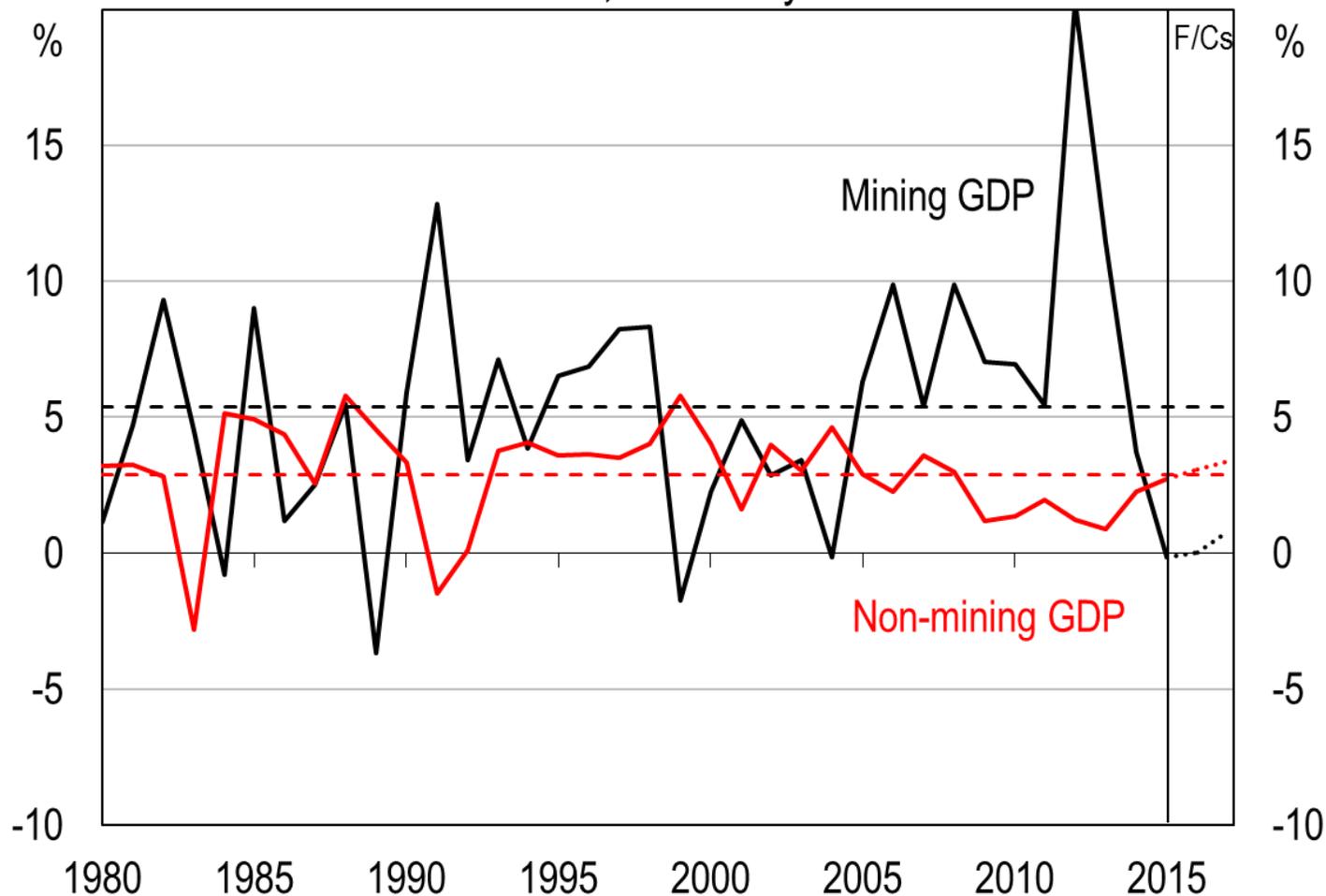


Source: BREE, HSBC forecasts

Mining GDP is leveling out and non-mining GDP is gradually rising

Mining and non-mining GDP growth*

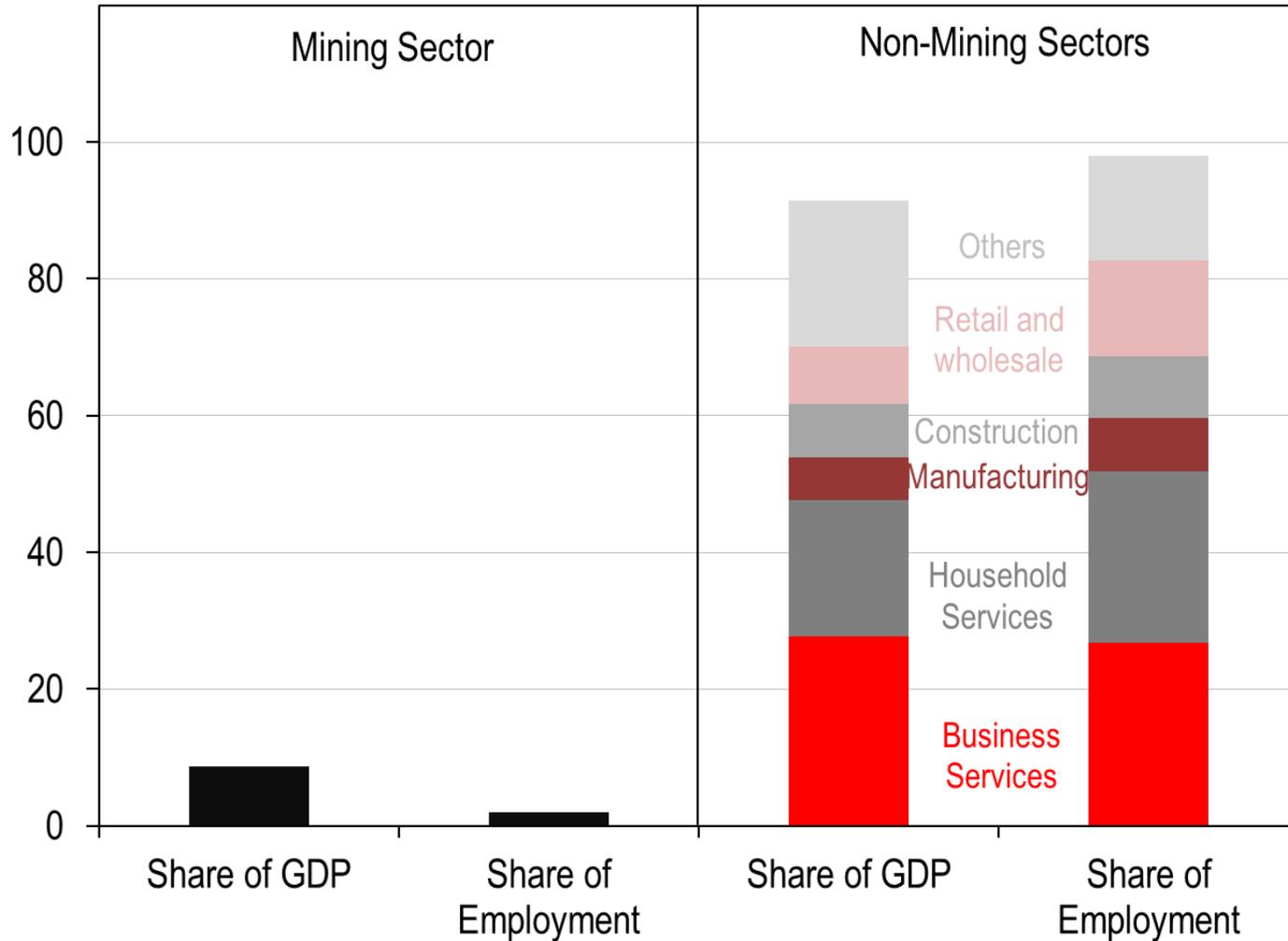
Annual, financial year



* Dashed lines represent averages for selected series

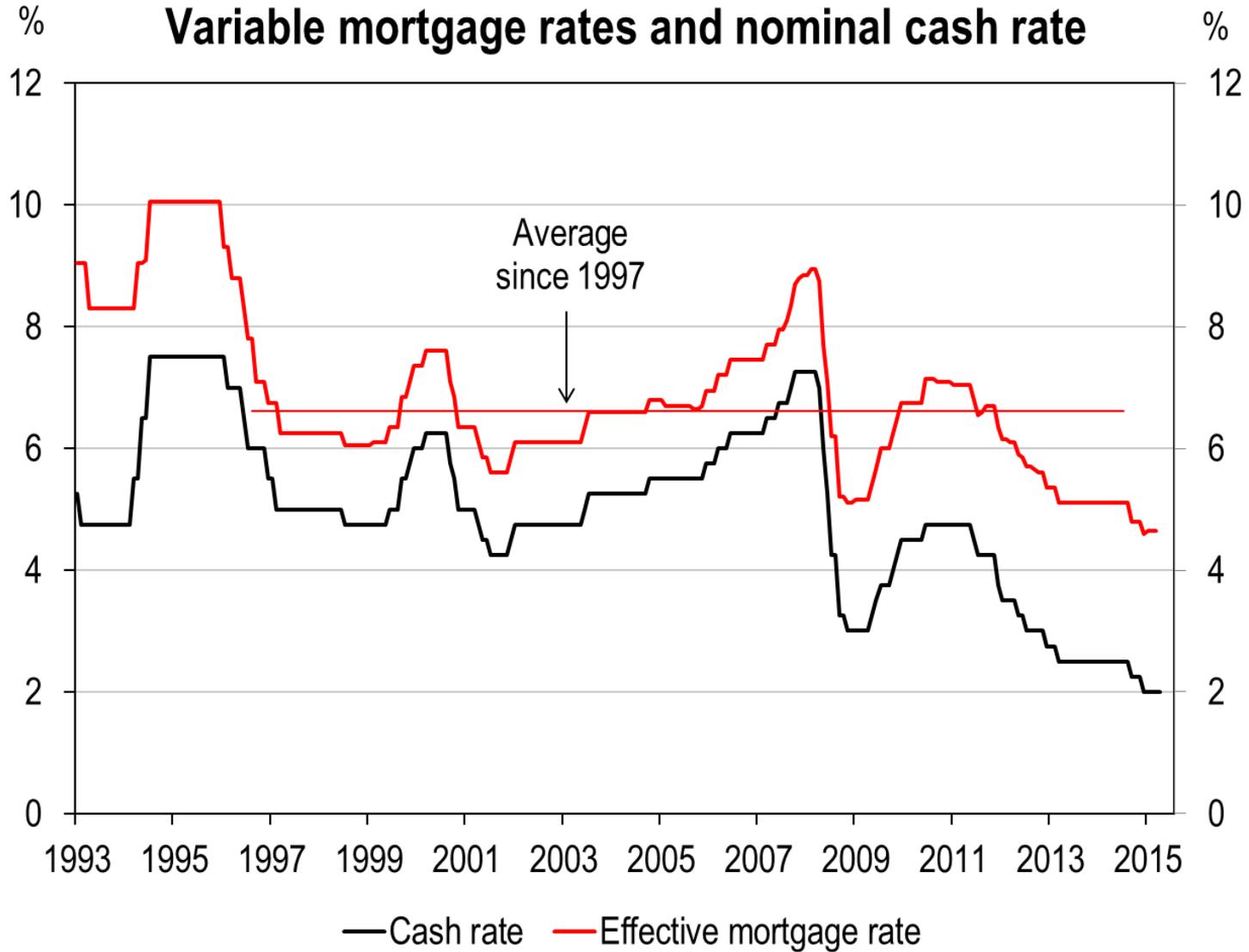
Rebalancing should be possible, as non-mining is bulk of economy

GDP and Employment by Sector



Source: ABS

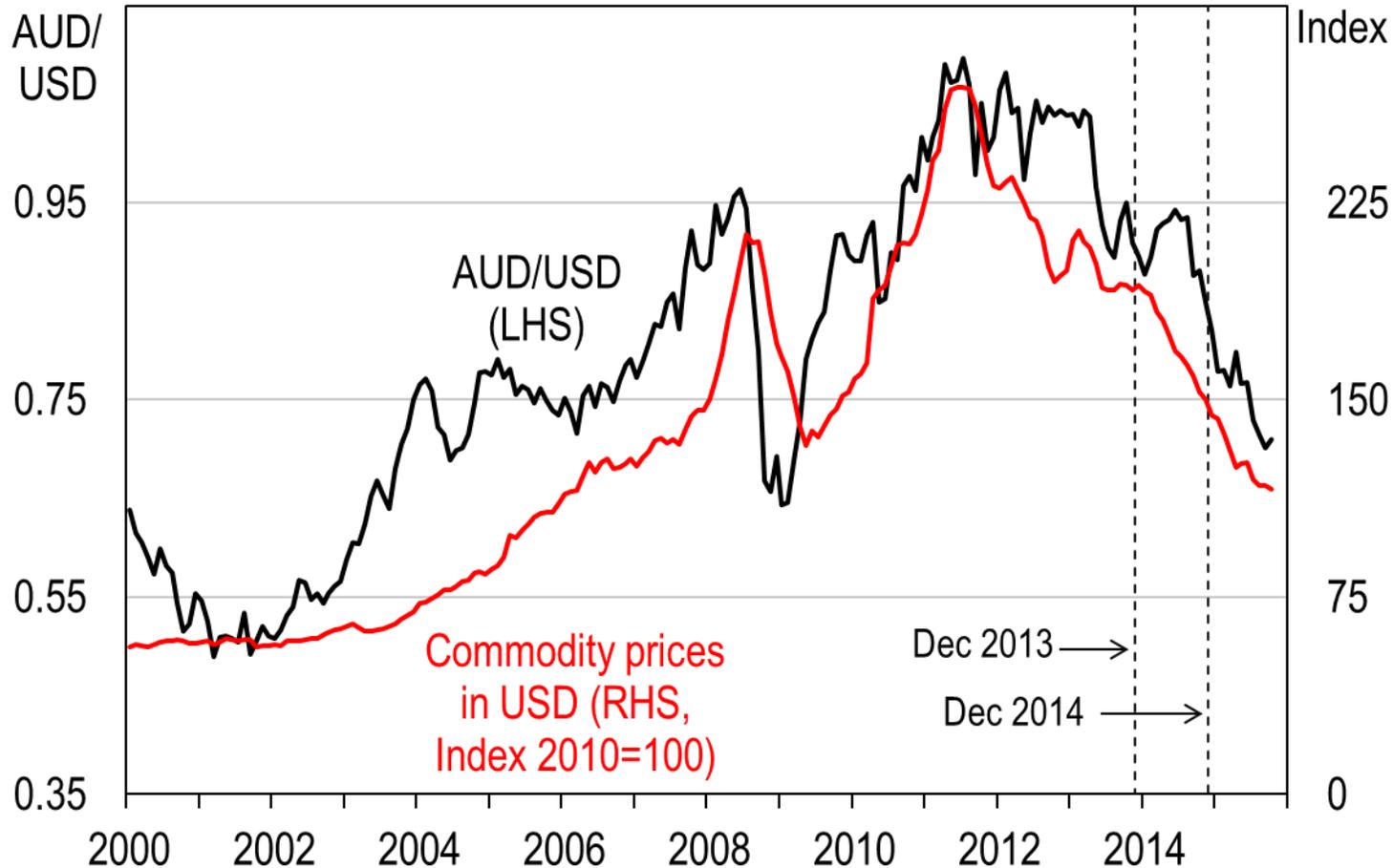
To manage rebalancing, rates have been cut to record lows



Source: RBA

AUD has fallen a long way over the past year and is now supporting growth

Australia's Commodity Prices and the AUD



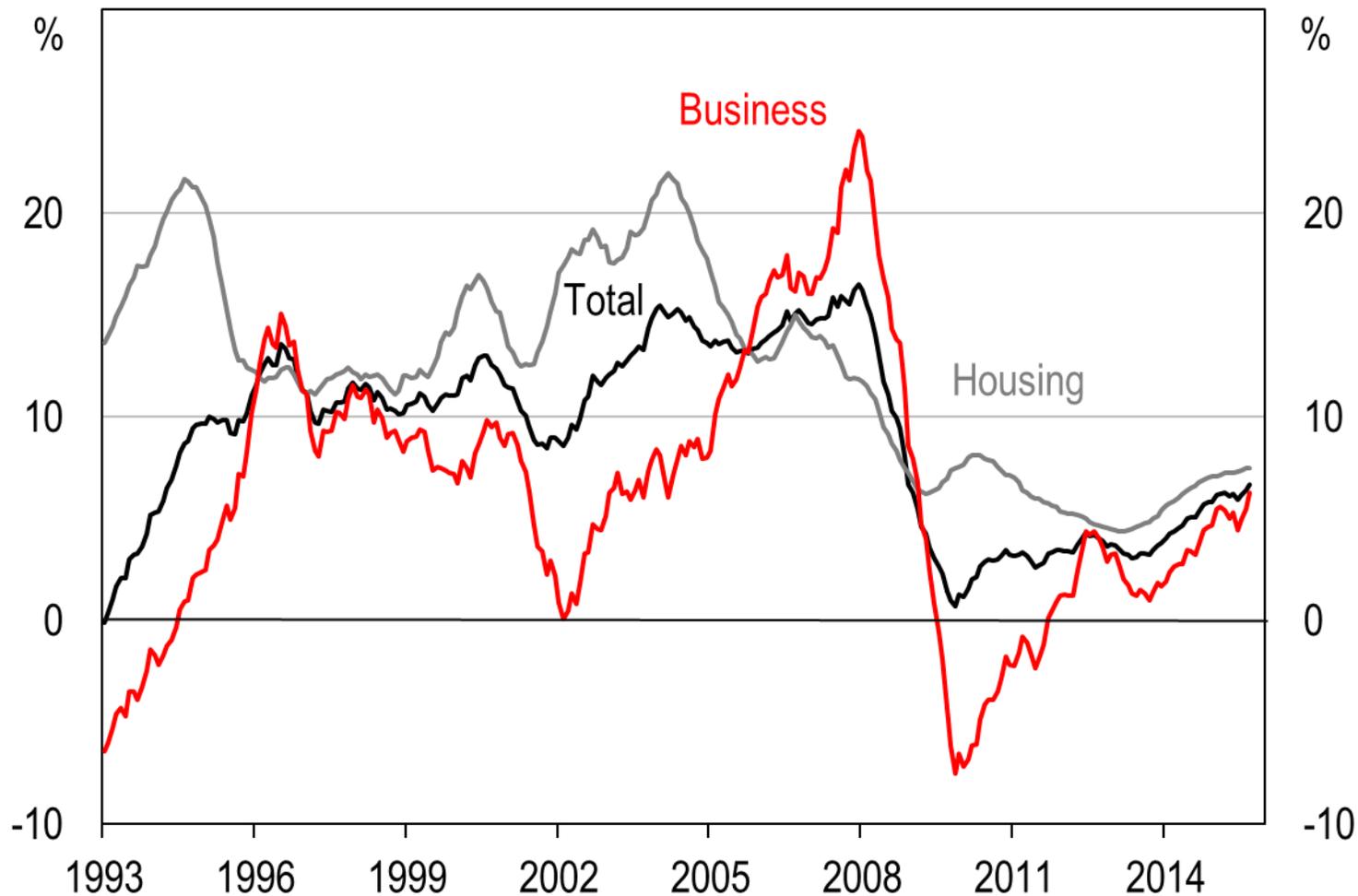
Dec 2013: RBA Governor says "85c would be closer to the mark than 95c"

Dec 2014: RBA Governor says "probably 75c is better than 85c"

Credit growth is picking up, which is a sign that monetary policy is working

Financial Aggregates - Private Credit

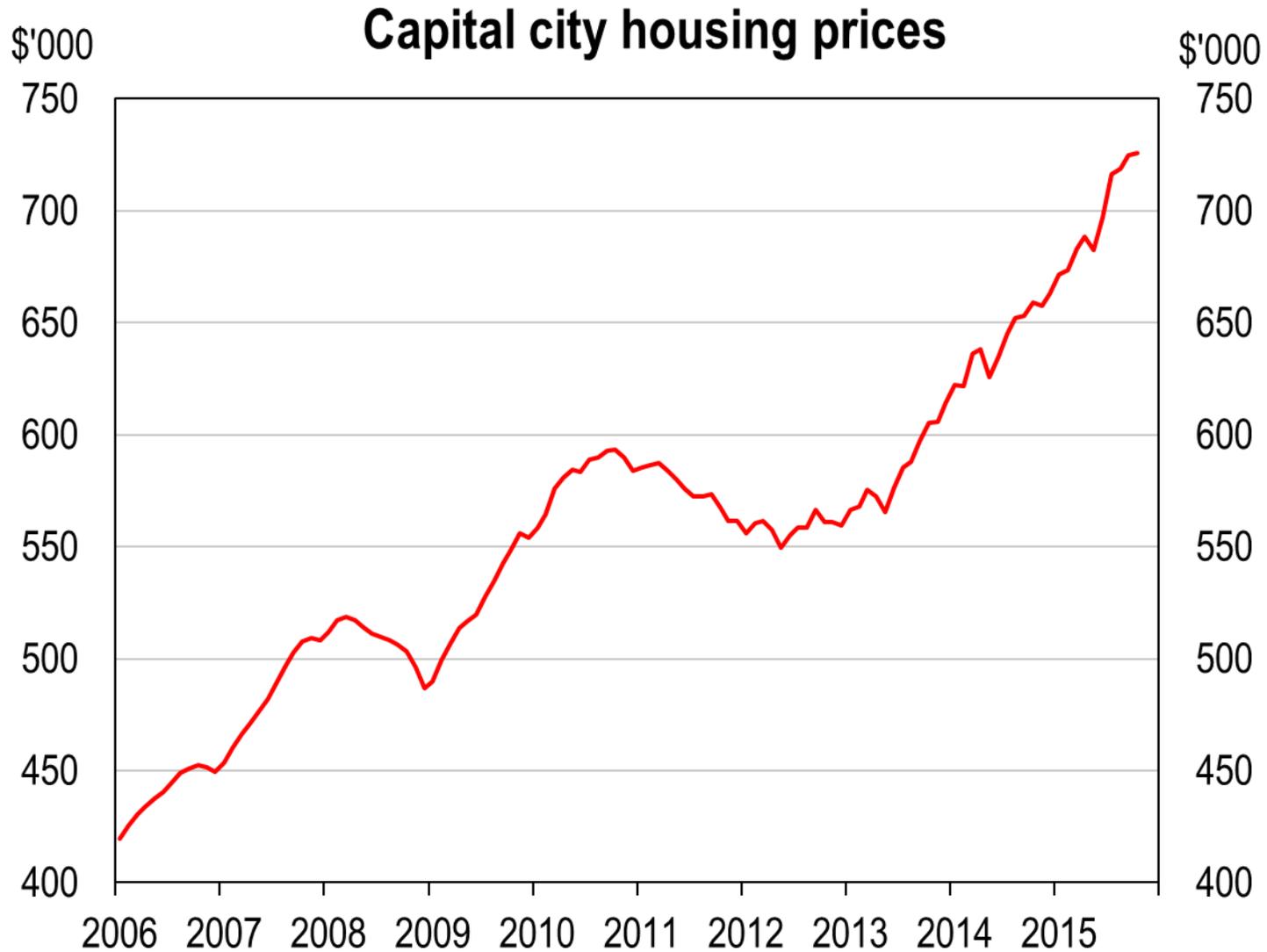
Year-ended change



Source: RBA

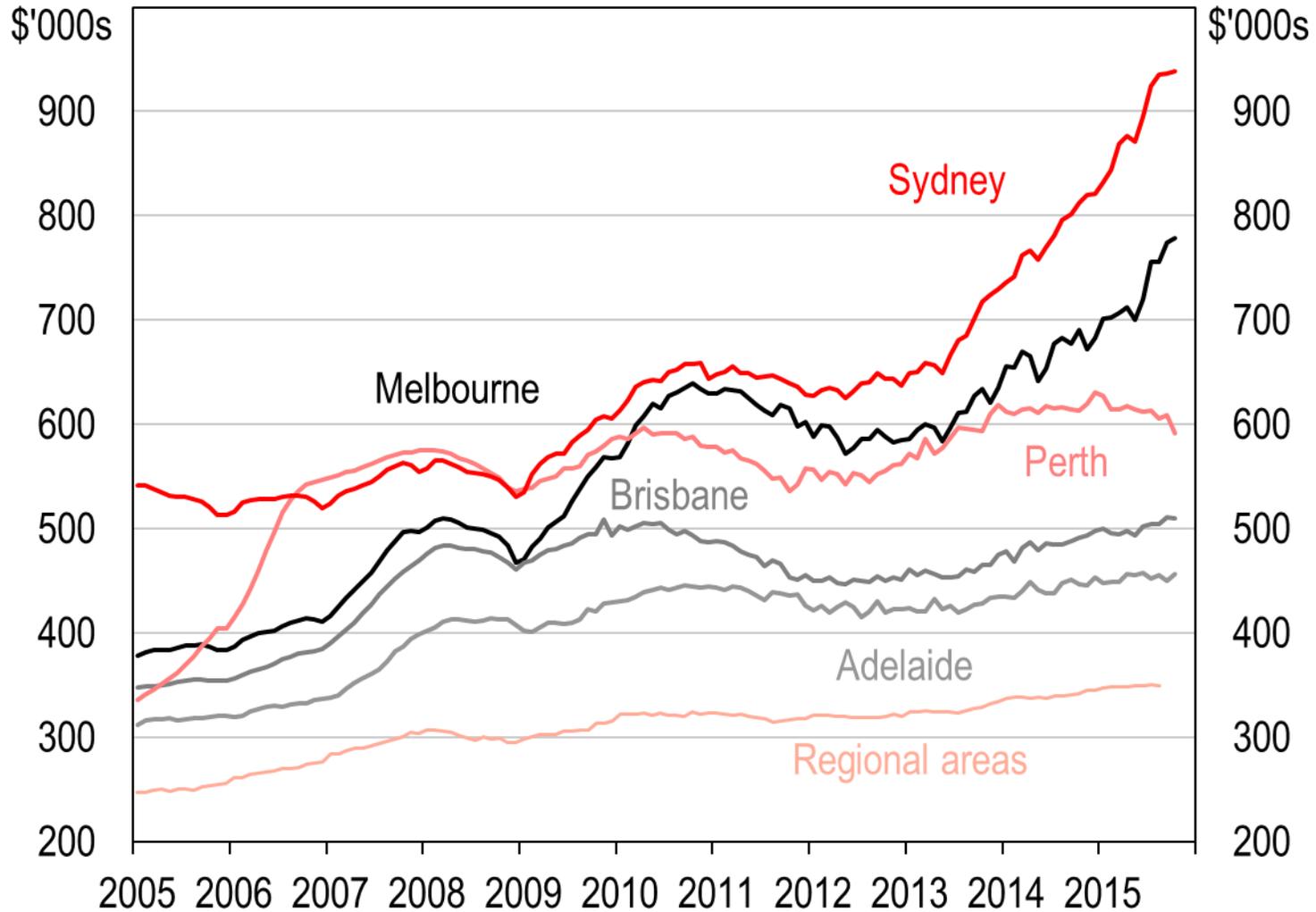


Low rates have supported a pick-up in housing prices



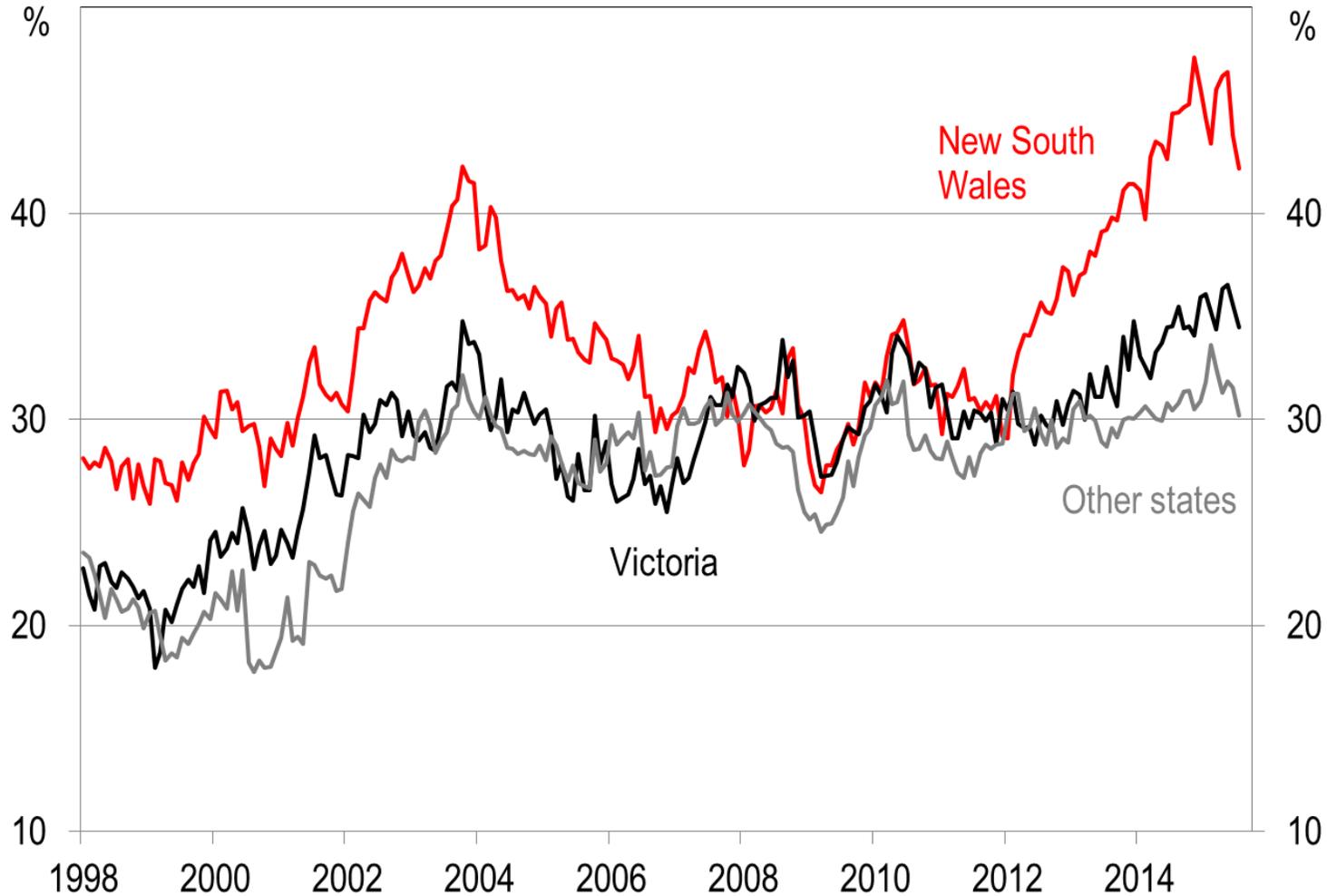
The non-mining states are seeing the strongest conditions

Housing prices by region



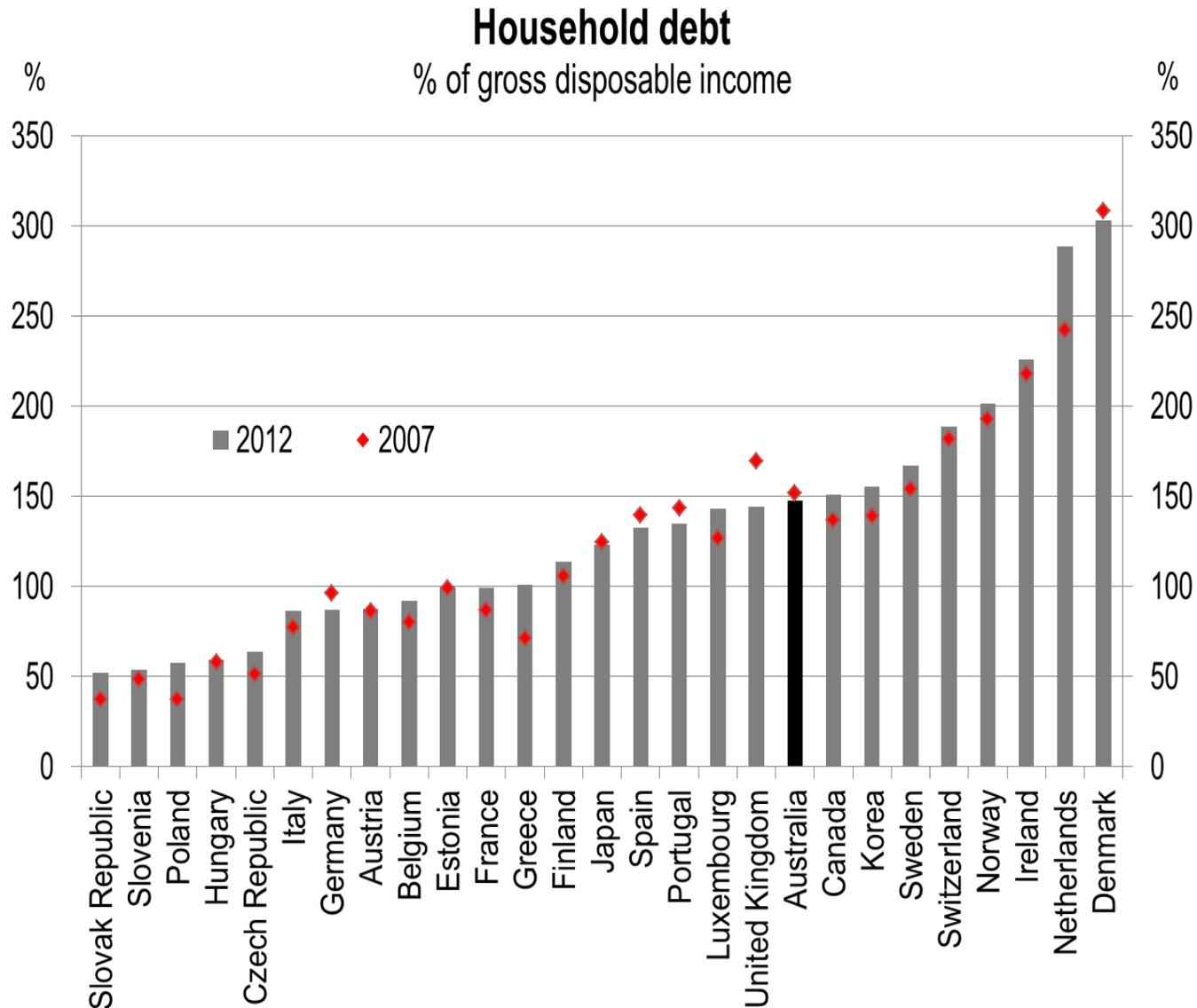
Tighter prudential settings are helping to contain the risks

Investor share of housing loan approvals



Source: ABS

Household debt is high, but not exceptionally high



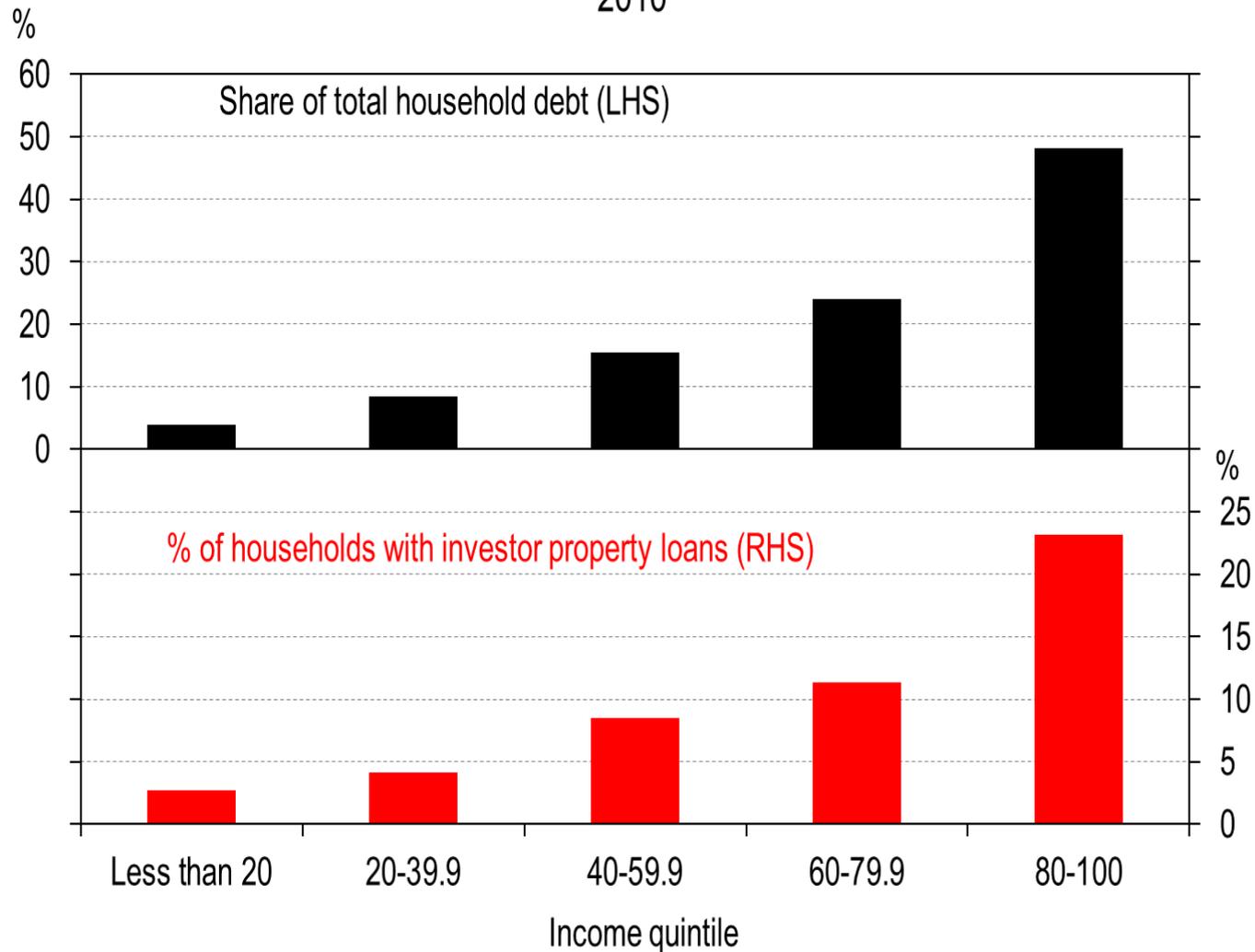
Source: OECD, RBA



Household debt is mostly held by higher income earners

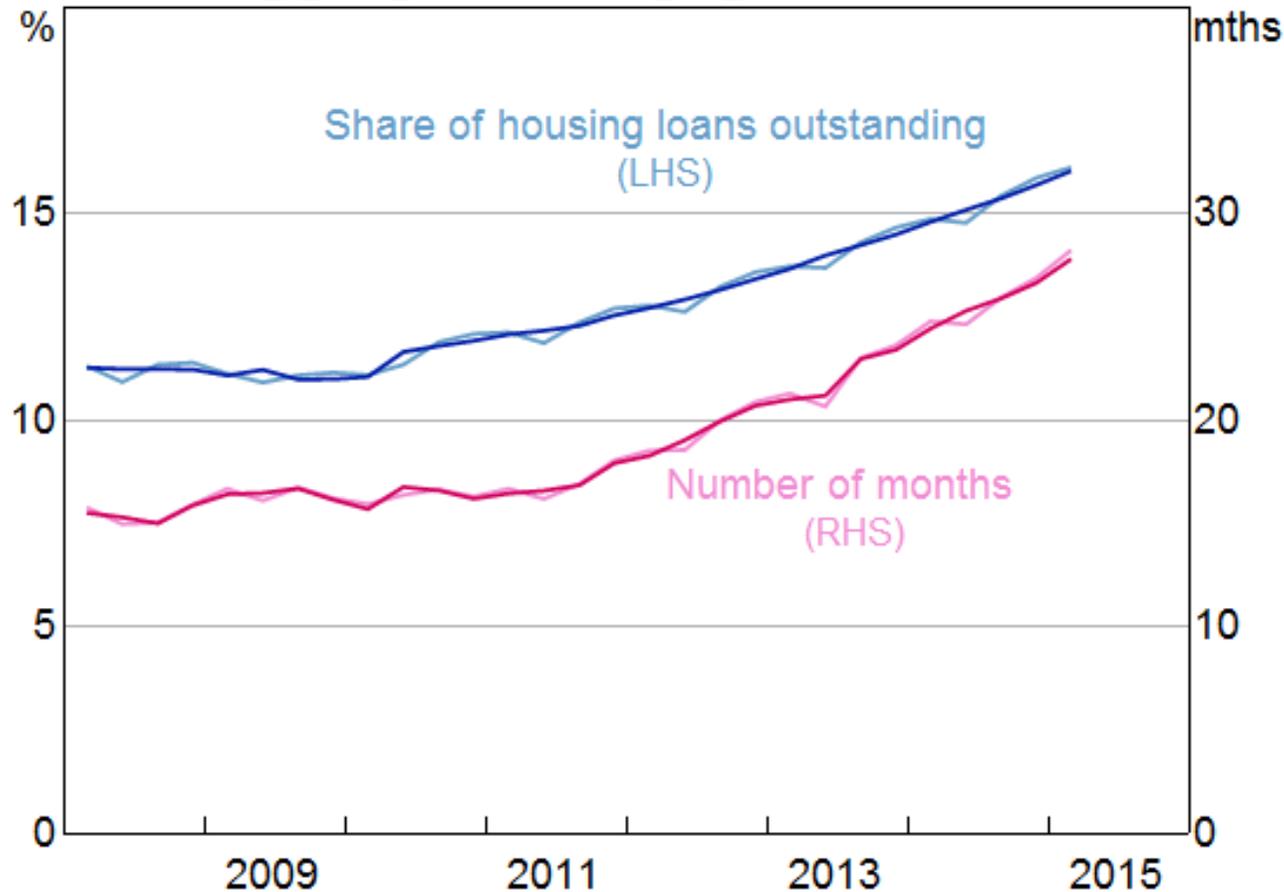
Distribution of debt and property loans by income

2010



Households are well ahead on their mortgage repayments

Aggregate Mortgage Buffers*



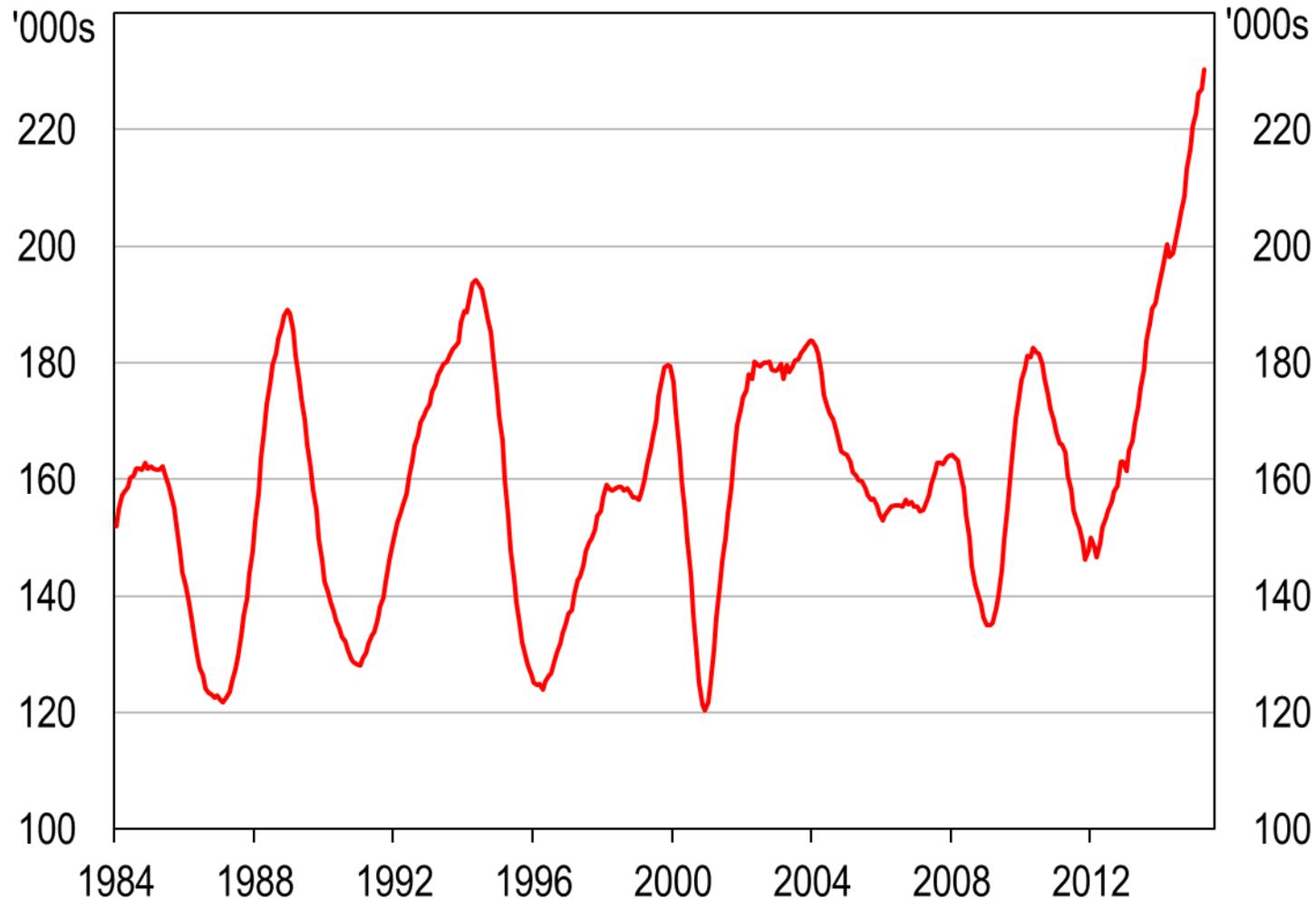
* Data are backcast before December 2010 to adjust for a reporting change by one bank; darker lines are seasonally adjusted

Sources: APRA; RBA

A strong housing construction upswing is under way

Residential Building Approvals

Number of buildings, rolling 12 month sum

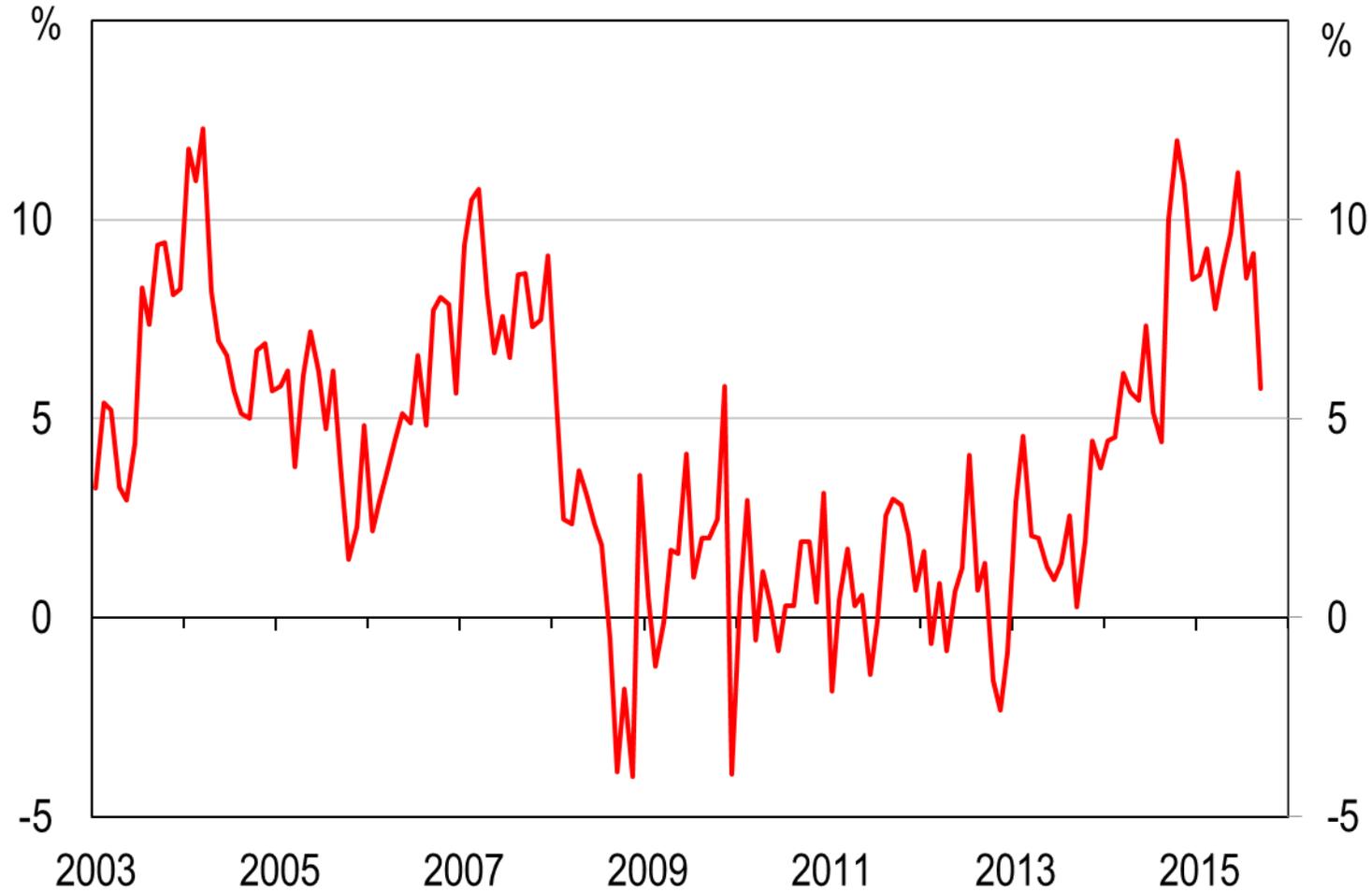


Source: ABS



Sales of household goods have been growing as new houses are filled

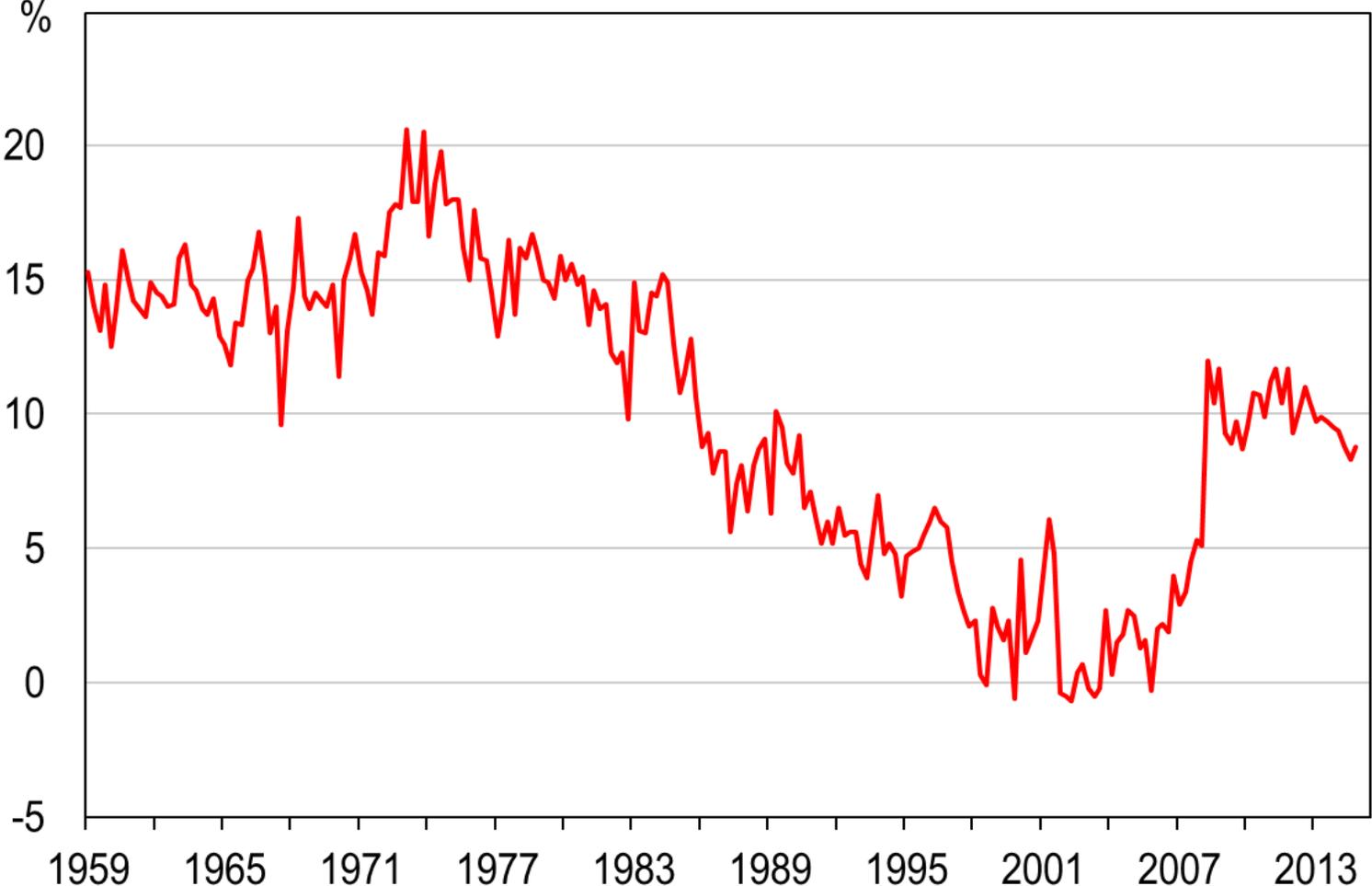
Sales of household goods Year-ended change



Source: ABS

Households have been reducing their saving, as asset prices rise

Household Saving Ratio



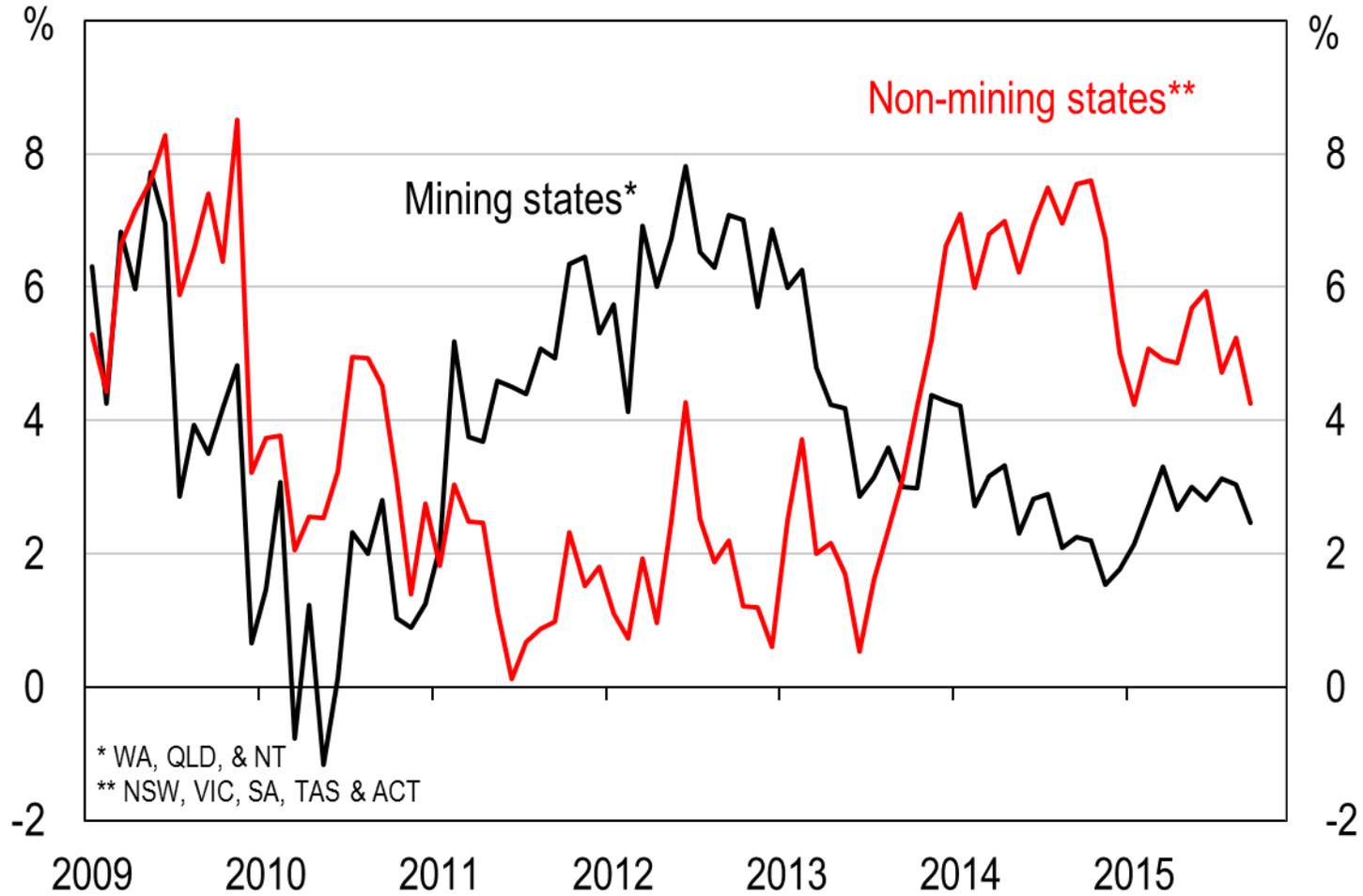
Source: ABS



Rebalancing is happening across the states

Retail sales by region

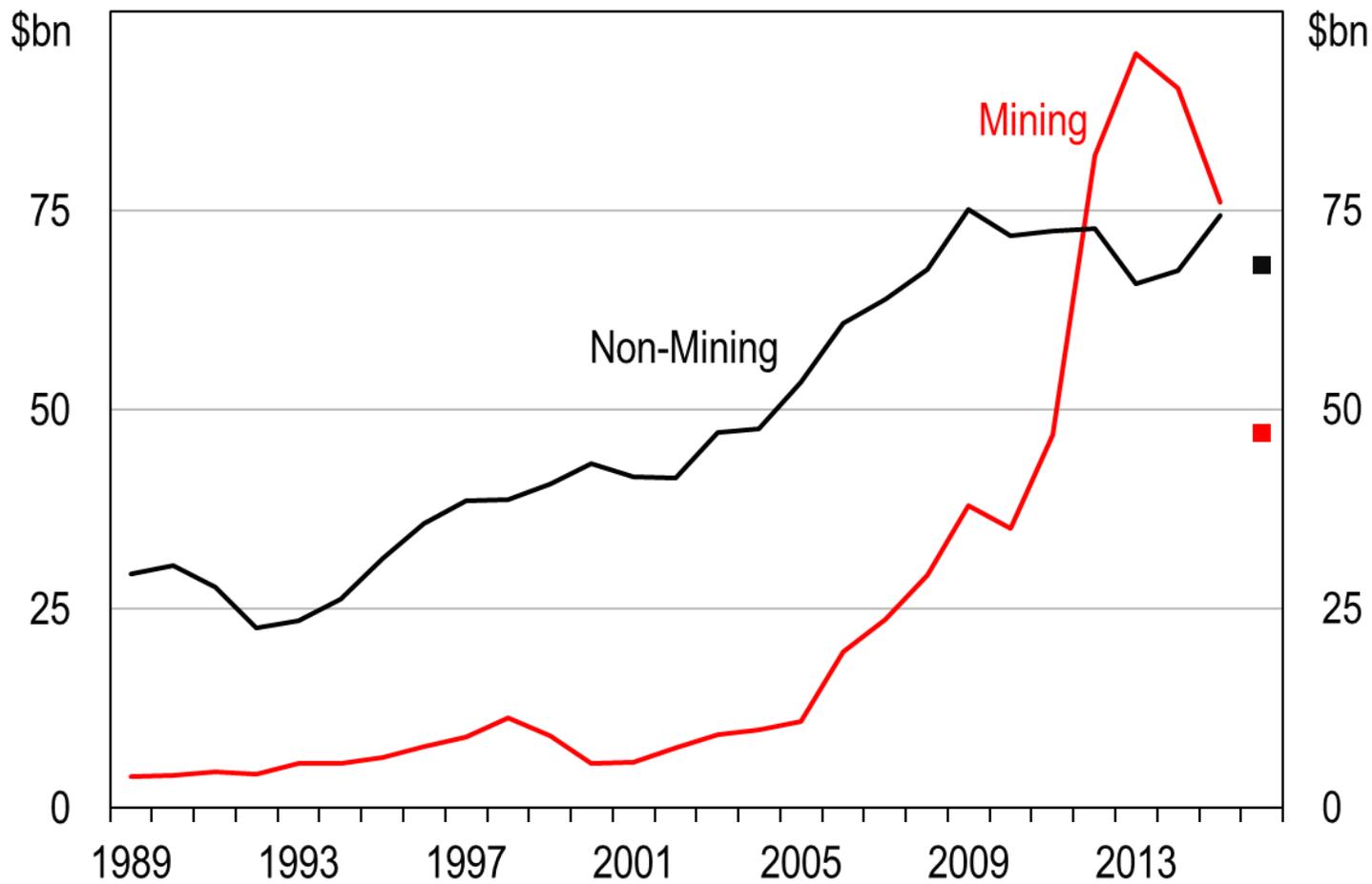
Year-ended change



Mining investment is falling and non-mining is not lifting enough

Capital Expenditure Survey

Current prices

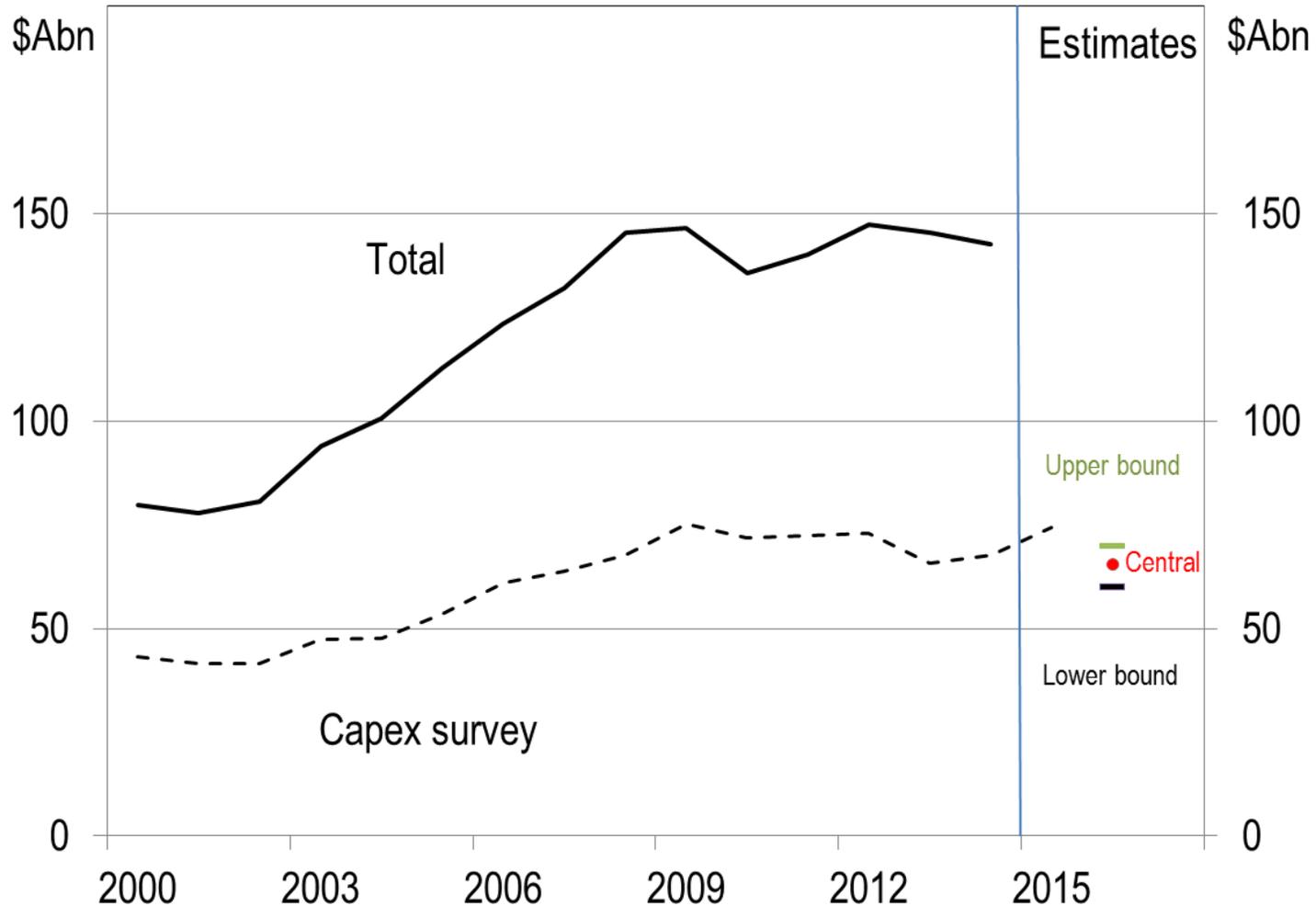


*Five-year realisation ratio applied

Non-mining investment outlook is highly uncertain

Non-mining business investment

Current prices



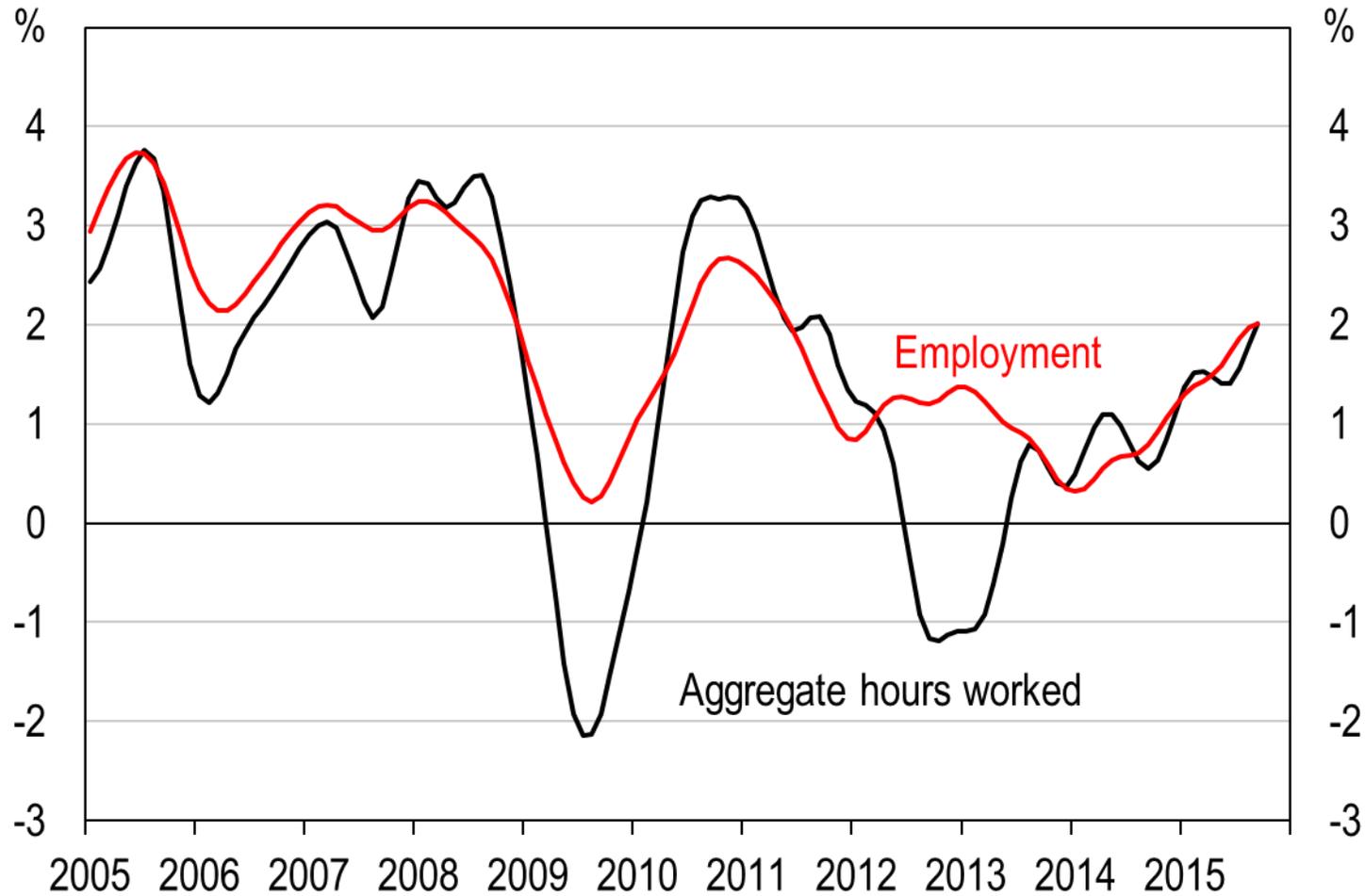
Source: ABS, RBA, HSBC estimates



Employment growth and hours worked appear to be lifting

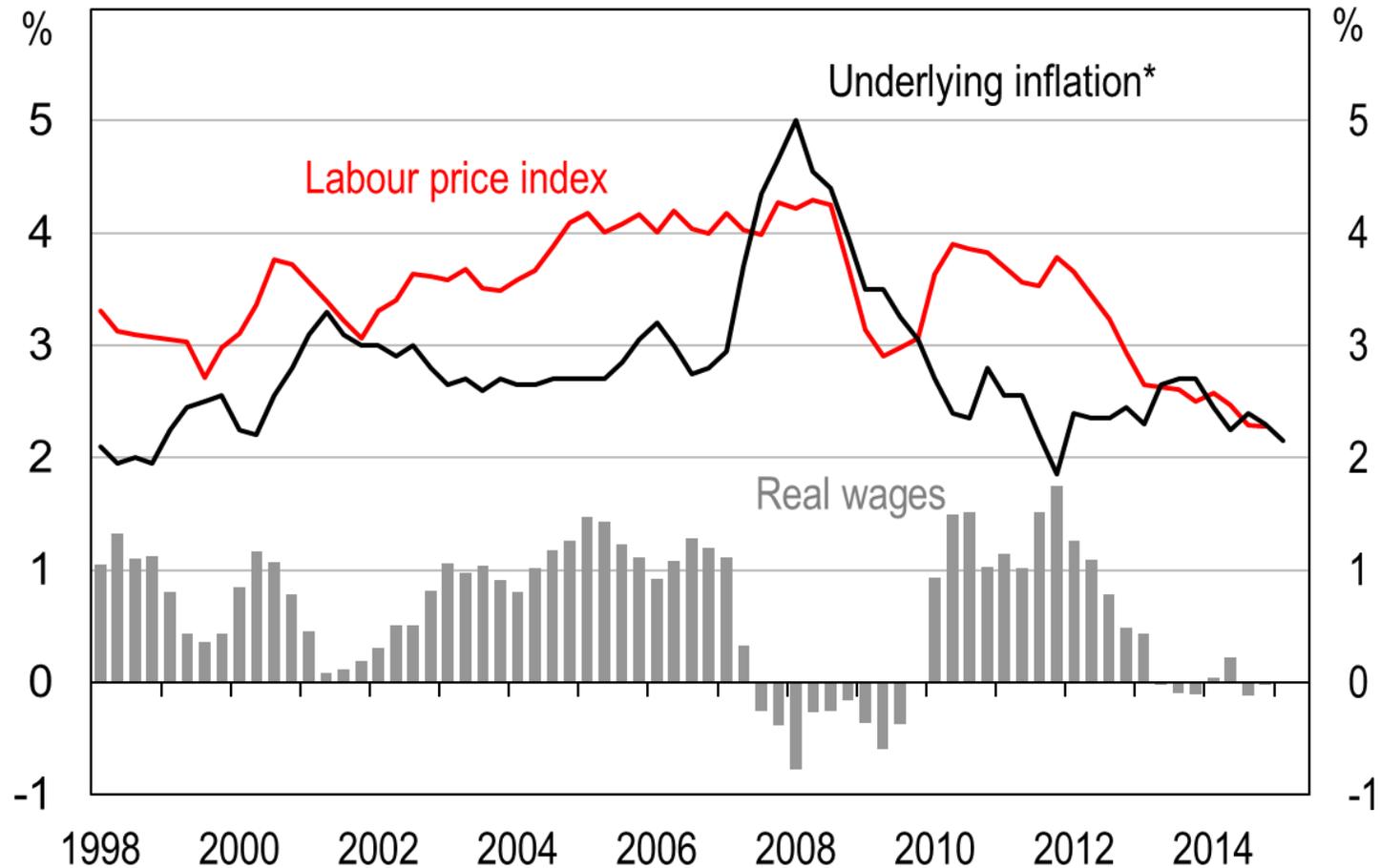
Hours Worked and Employment

Year-ended change, trend



Real wages are flat, holding back incomes but also reducing costs

Labour Price Index and Underlying inflation Year-ended percentage change

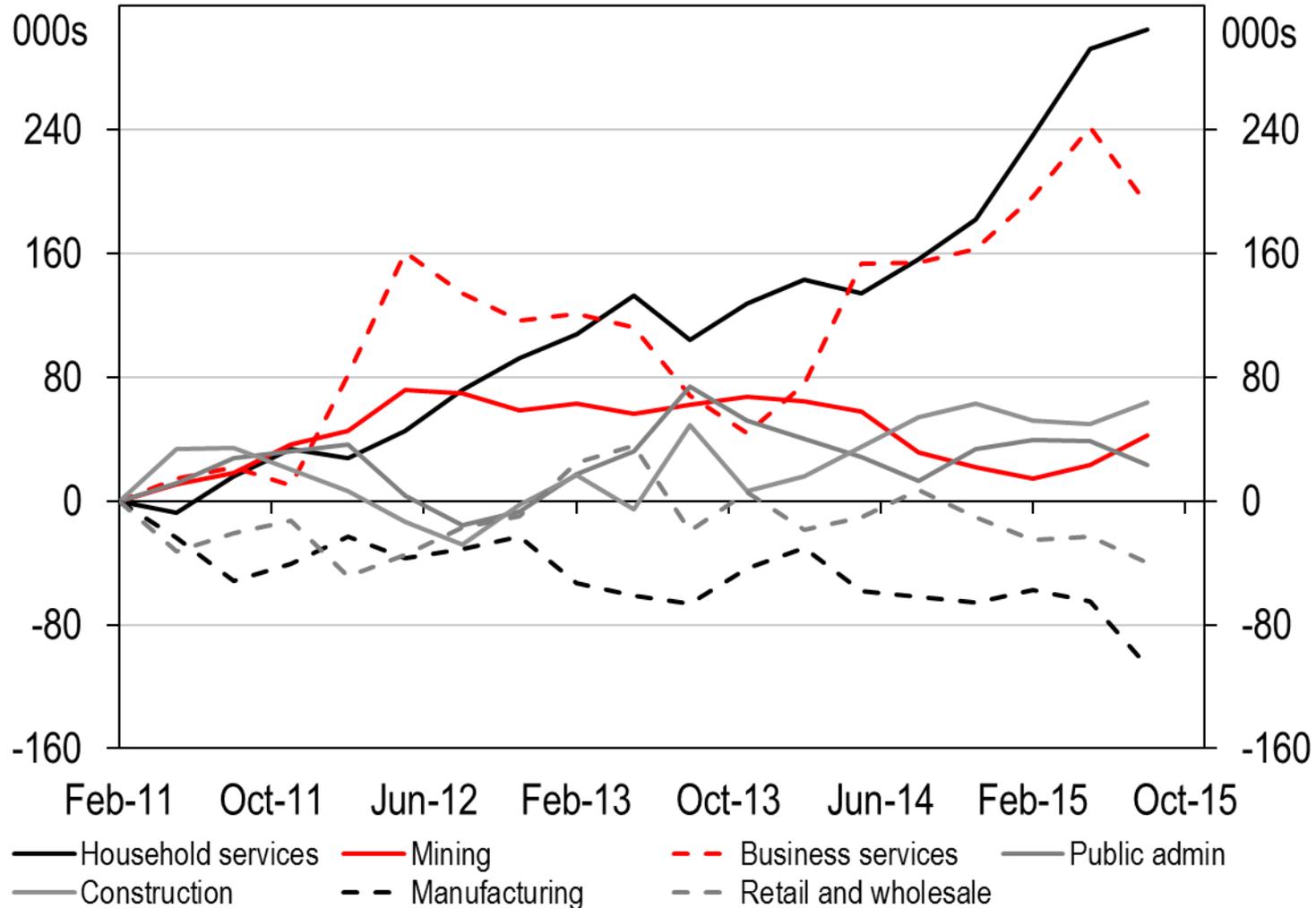


*Average of trimmed mean and weighted median

There are signs that growth is rebalancing towards services

Employment by sector

Cumulative change since February 2011

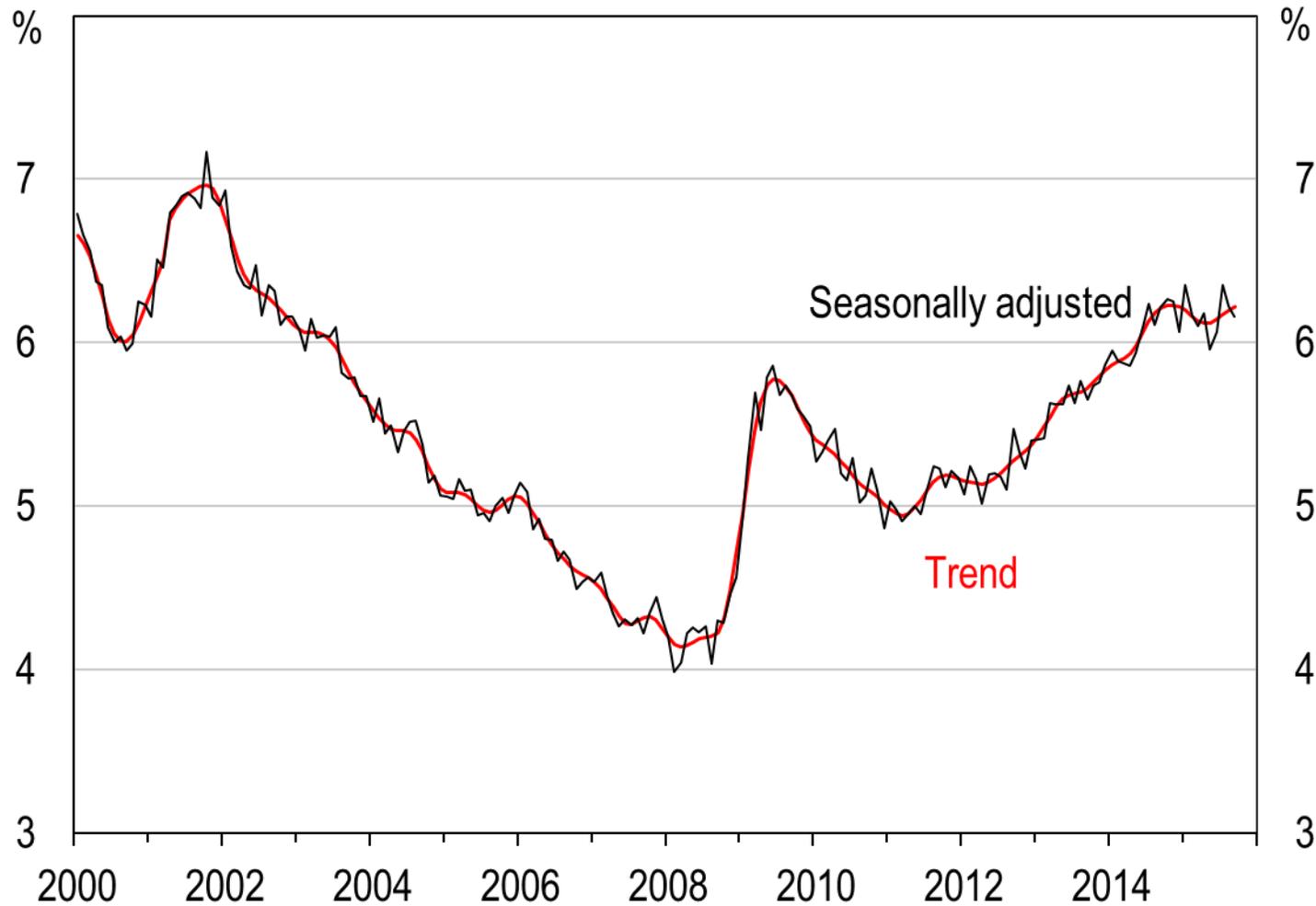


Source: ABS



The unemployment rate may be stabilising

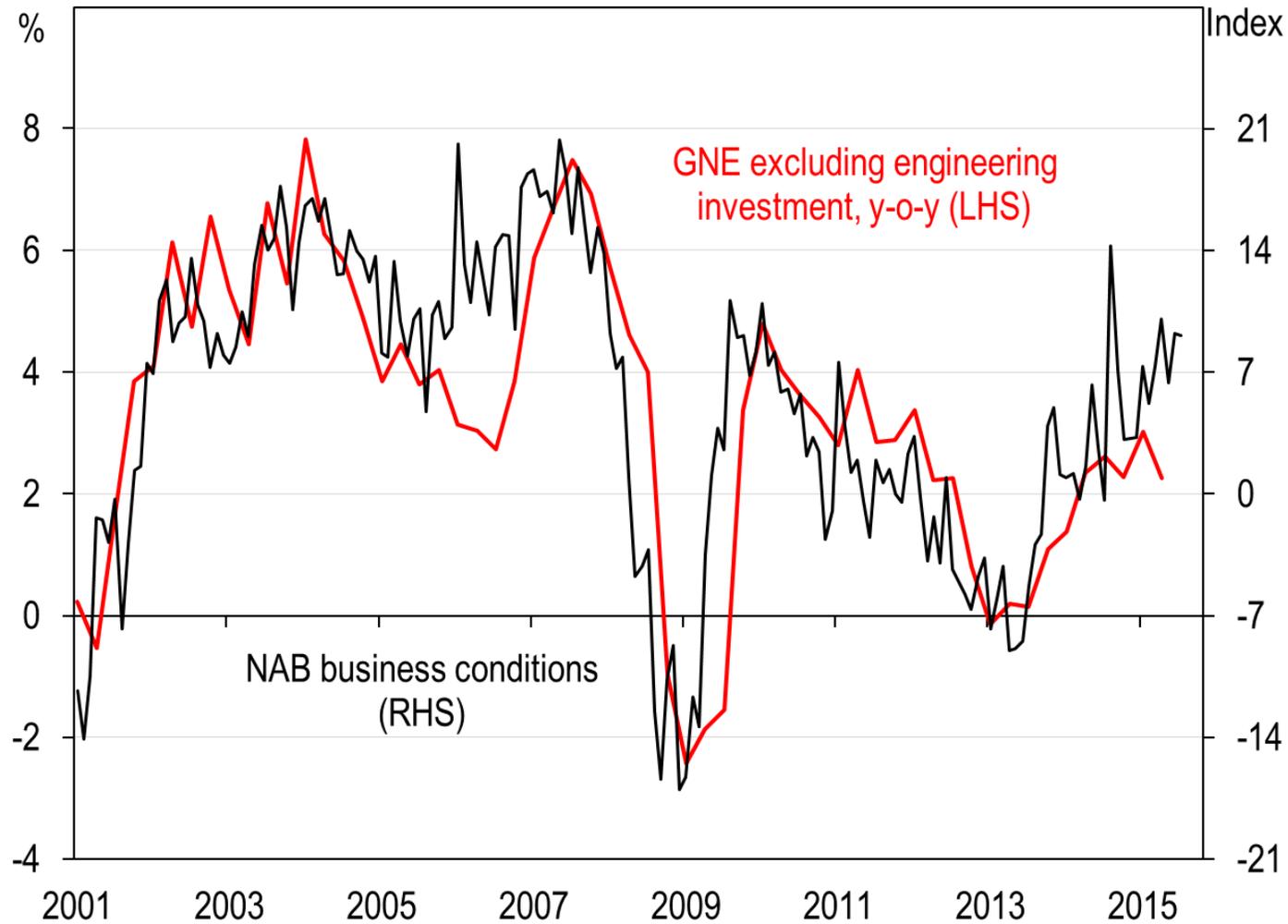
Unemployment Rate



Source: ABS

Business conditions have been lifting

Business conditions and non-mining domestic demand

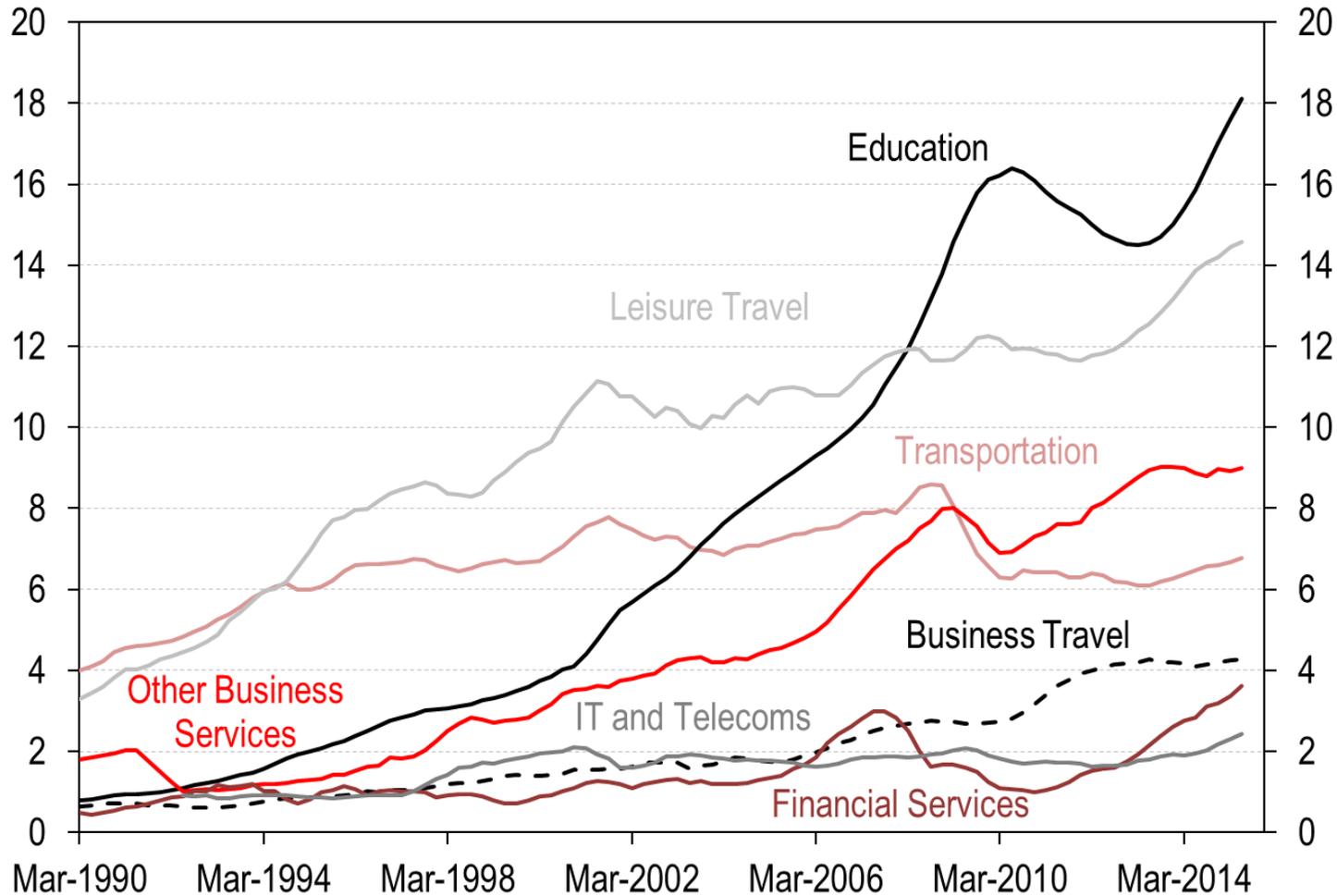


Source: Thomson Reuters Datastream, ABS

Services and agricultural exports are picking up

Australian Services Exports

Rolling annual totals, A\$bn

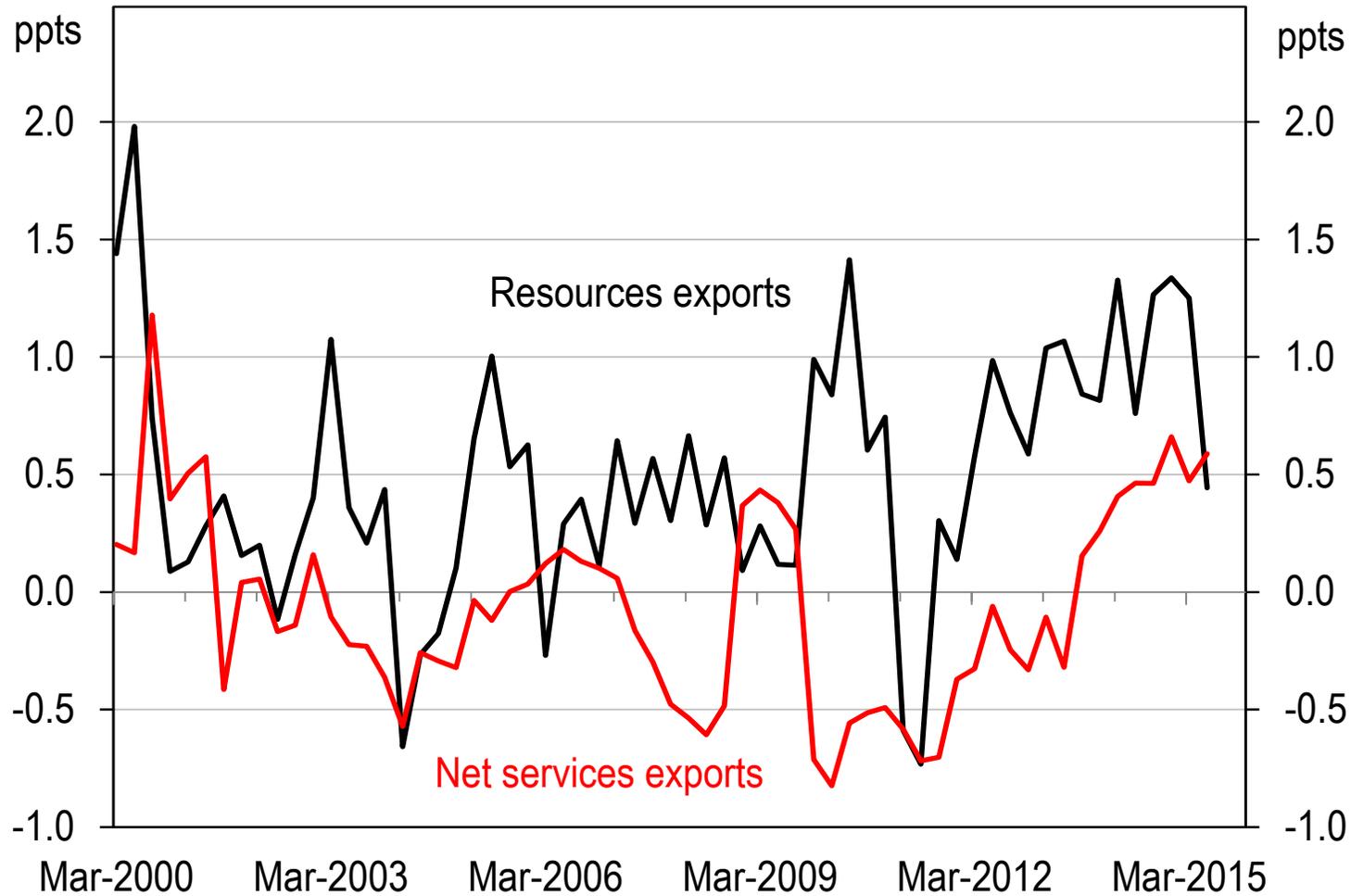


Source: ABS



Services exports are contributing more to growth than resources

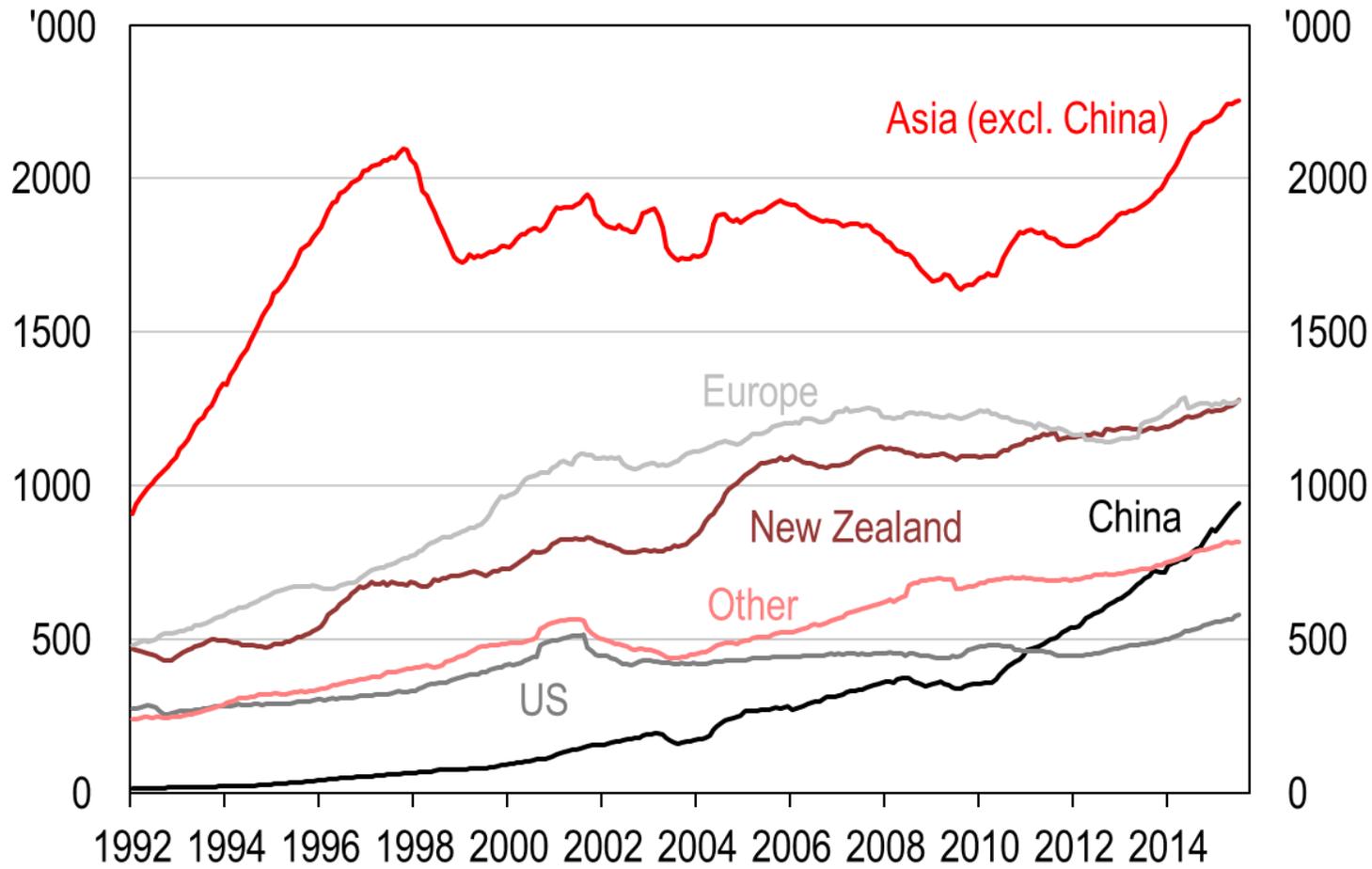
Contributions to real GDP growth (y-o-y)



Chinese tourist arrivals into Australia have risen by 150% in five years

Country of Origin for Short-term Arrivals

Annual totals

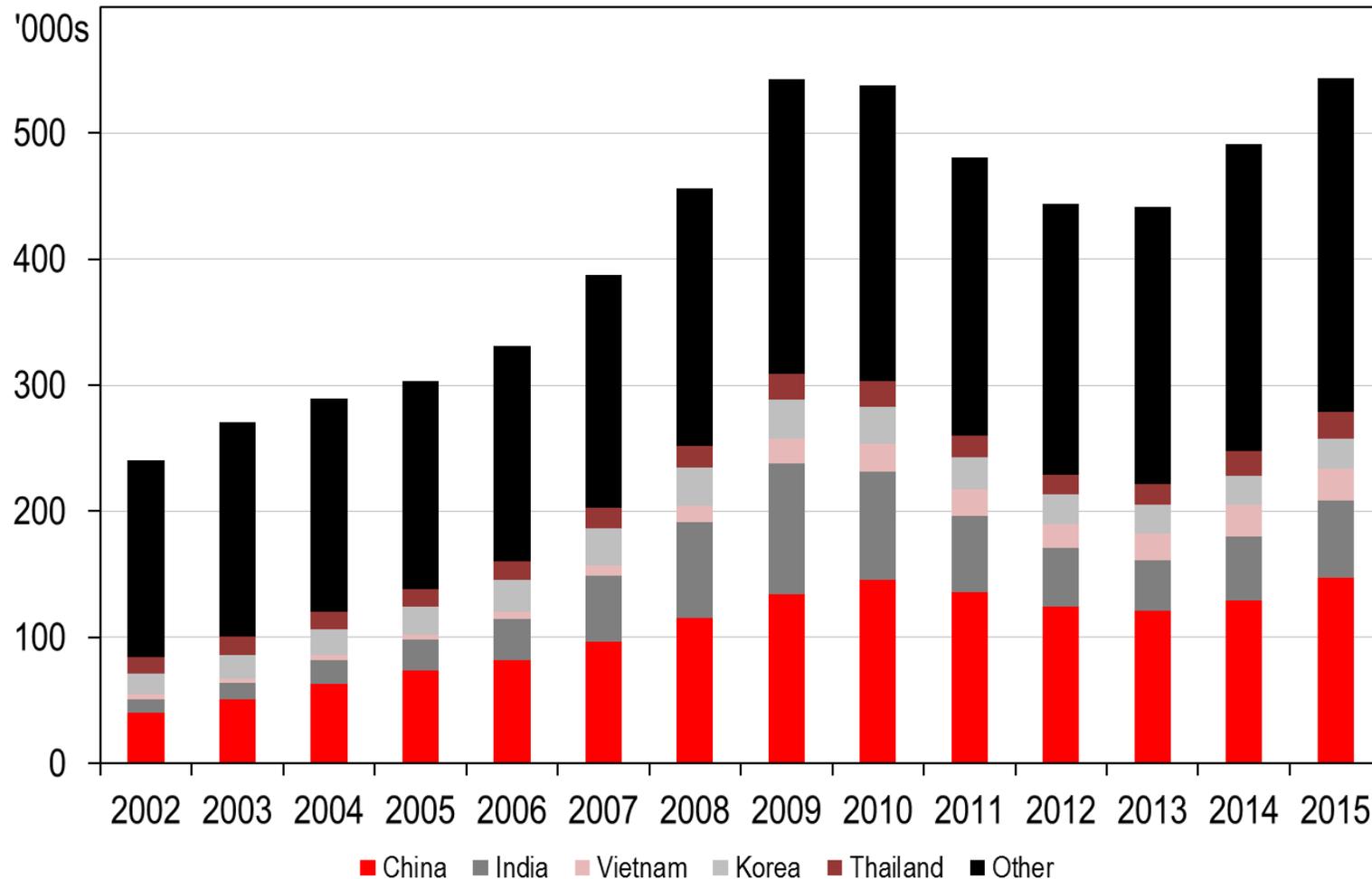


Source: ABS

Education exports are rising again

International student enrolments in Australia

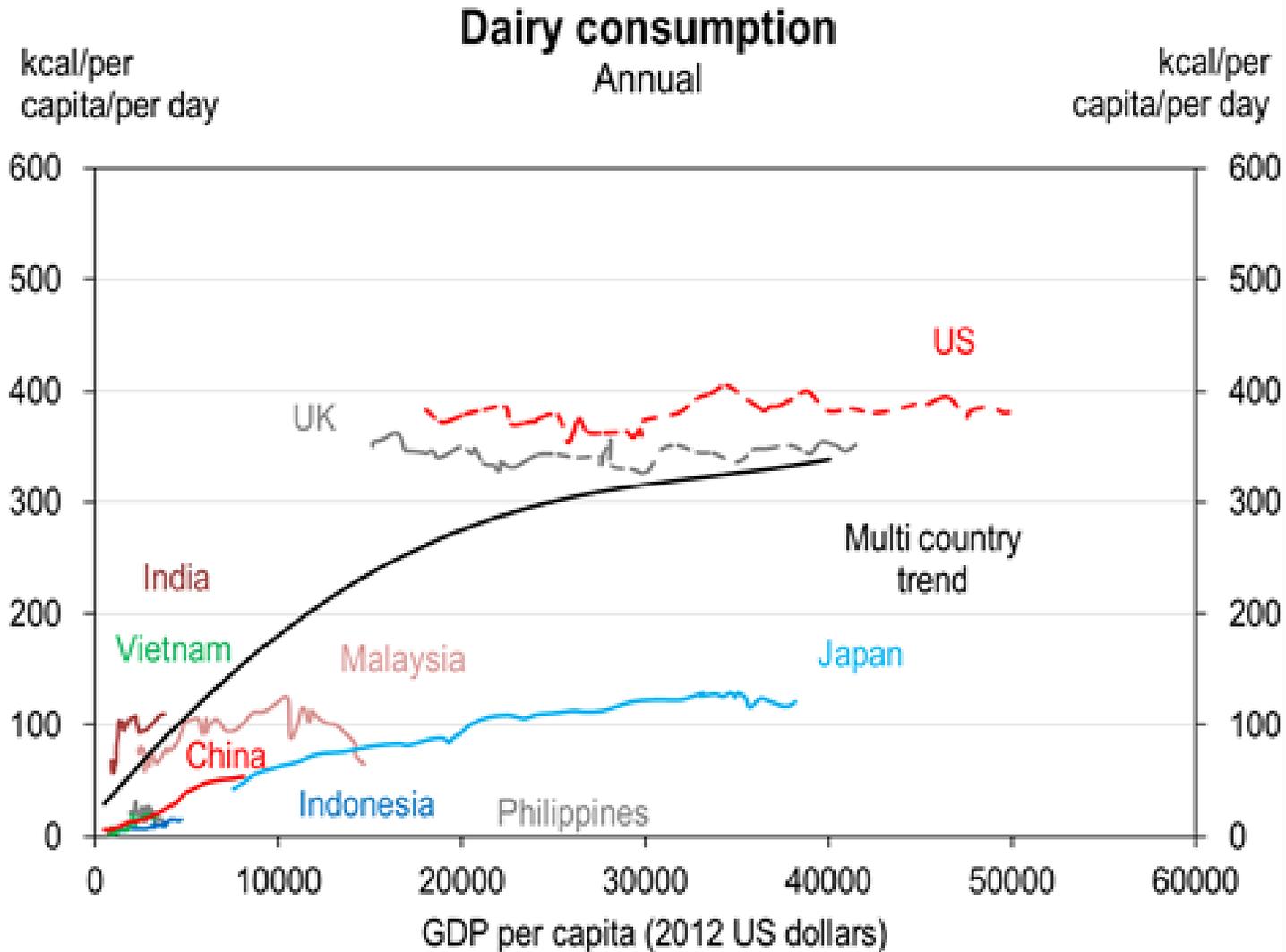
YTD as of July, by nationality



Source: Australian Education International

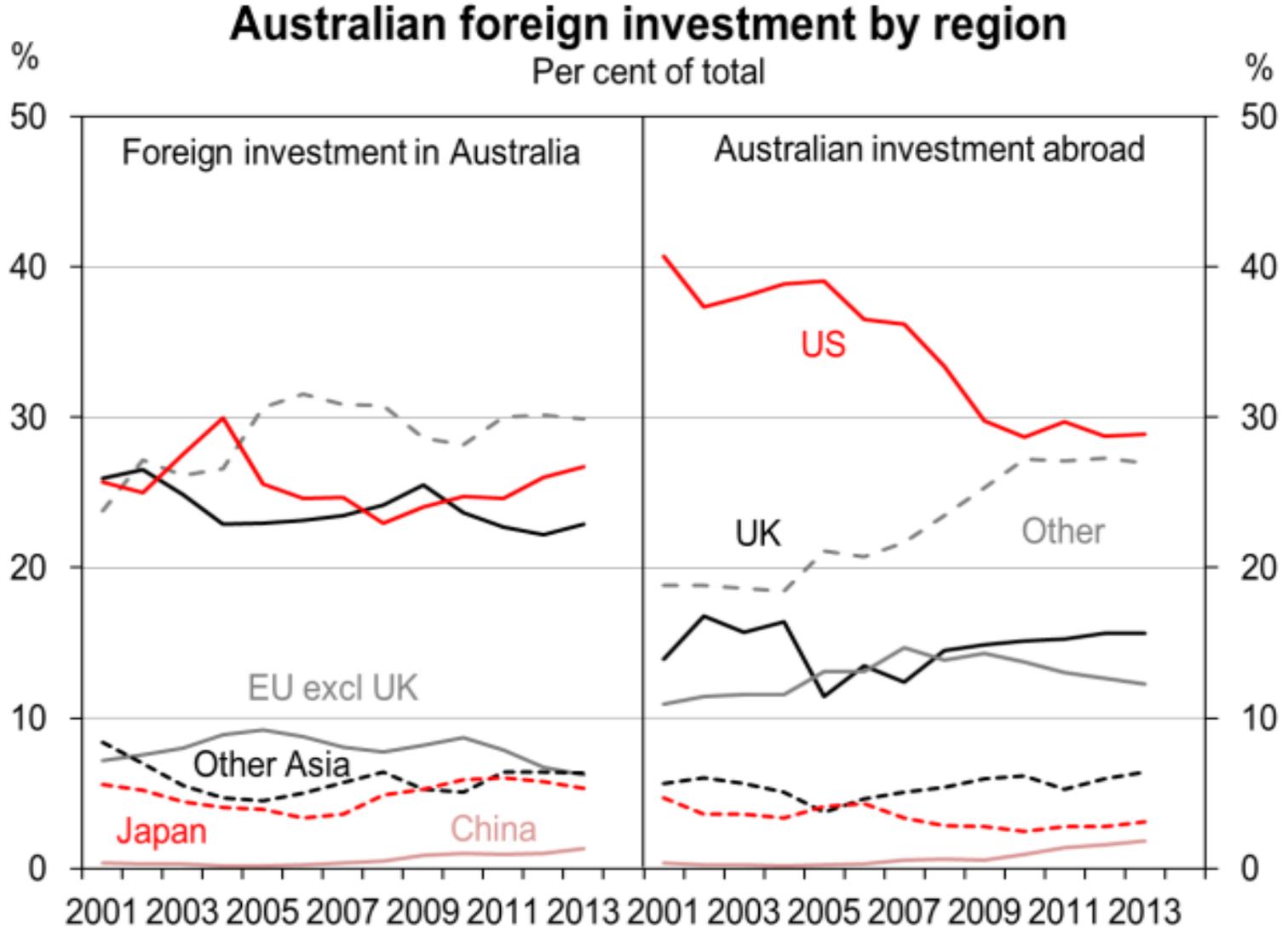


Dairy consumption rises from low levels as countries get richer



Source: FAO, Conference Board, HSBC

Financial links are still mostly to Western markets, but Asian links are growing

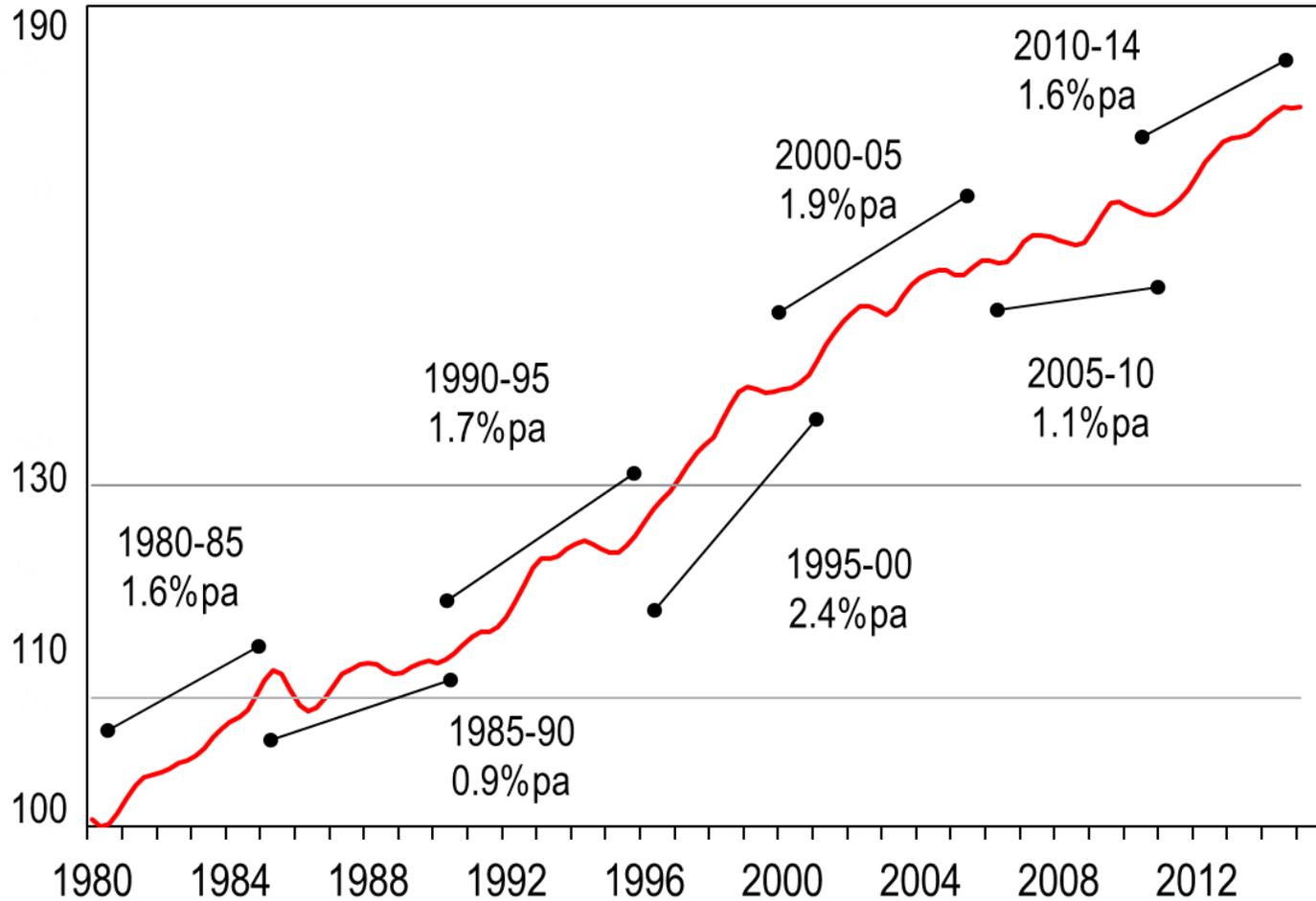


Source: ABS



Productivity growth has been weak in recent years

GDP per hour worked* Index (log scale)

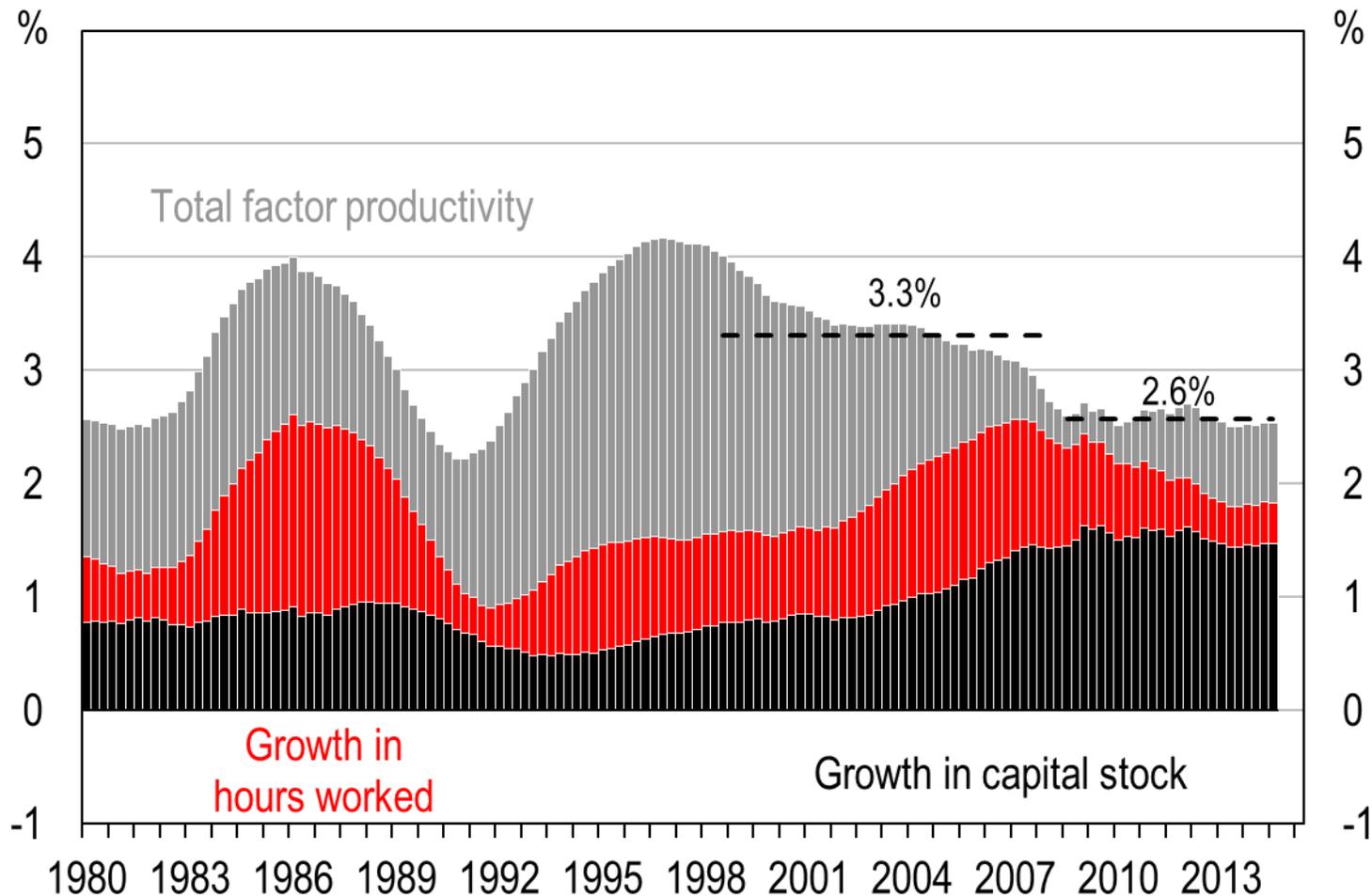


Source: ABS, HSBC estimates

Australia's potential growth rate may be lower than previously

Factor Contribution to Potential GDP Growth

Year-ended change

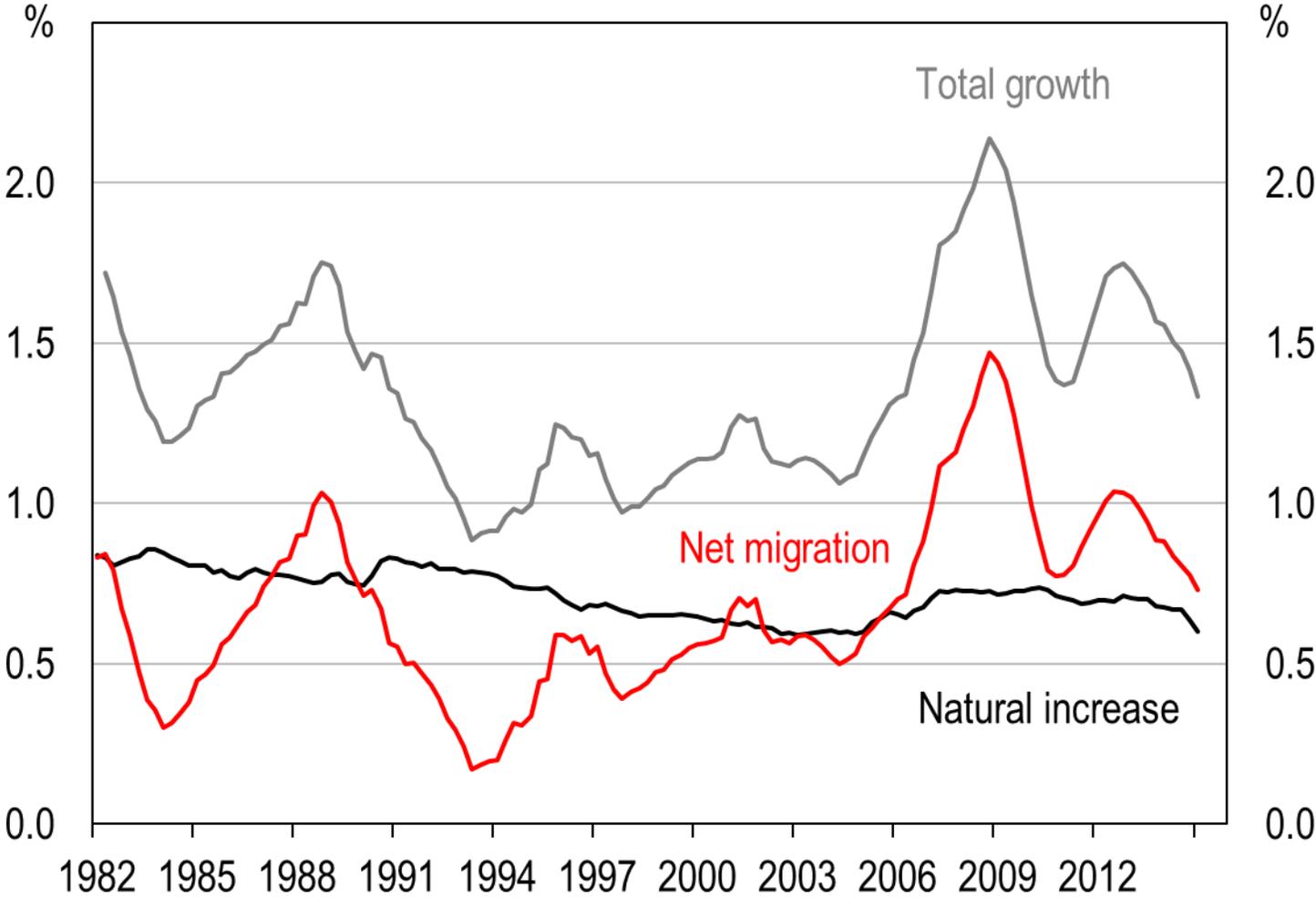


Source: ABS, HSBC estimates

Australian population growth has been slowing but is still solid

Population growth

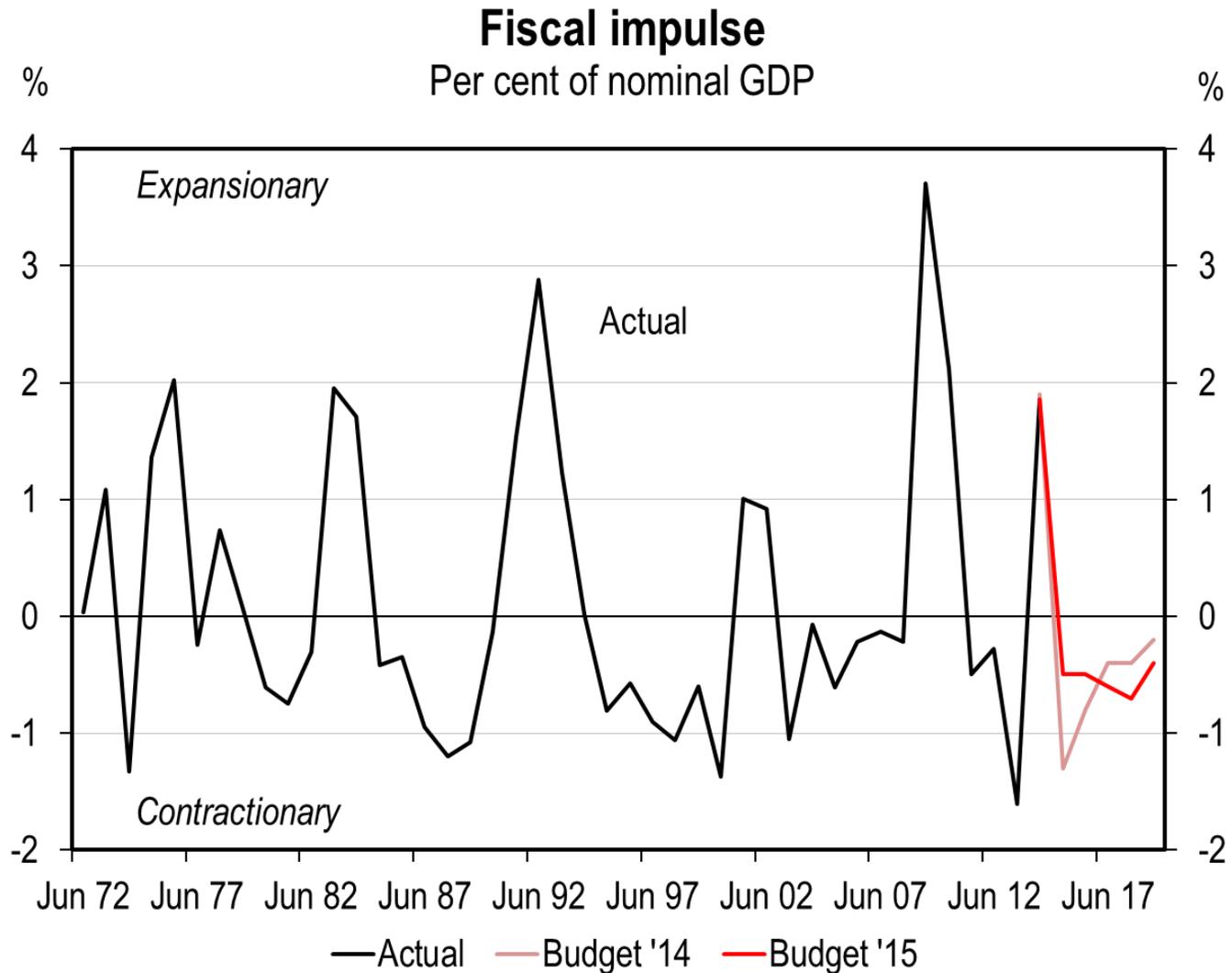
Contributions to growth in resident population



Source: ABS

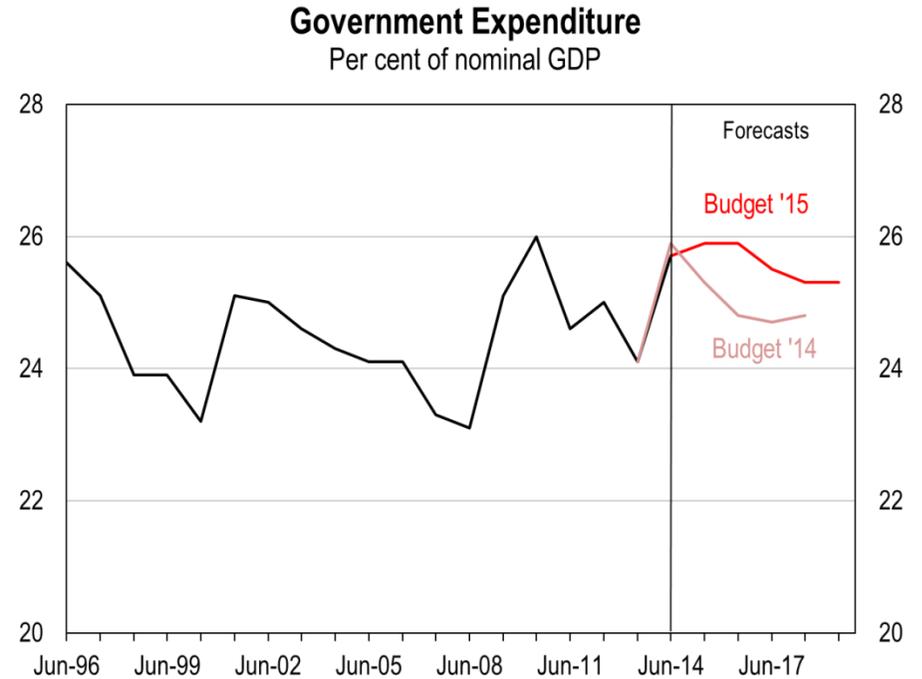
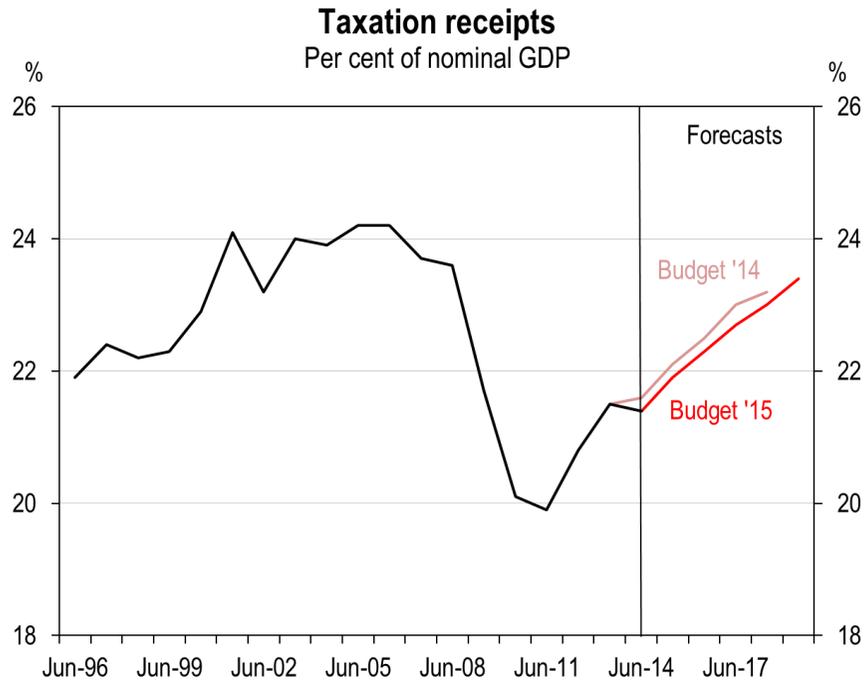


Fiscal policy has been a drag on growth



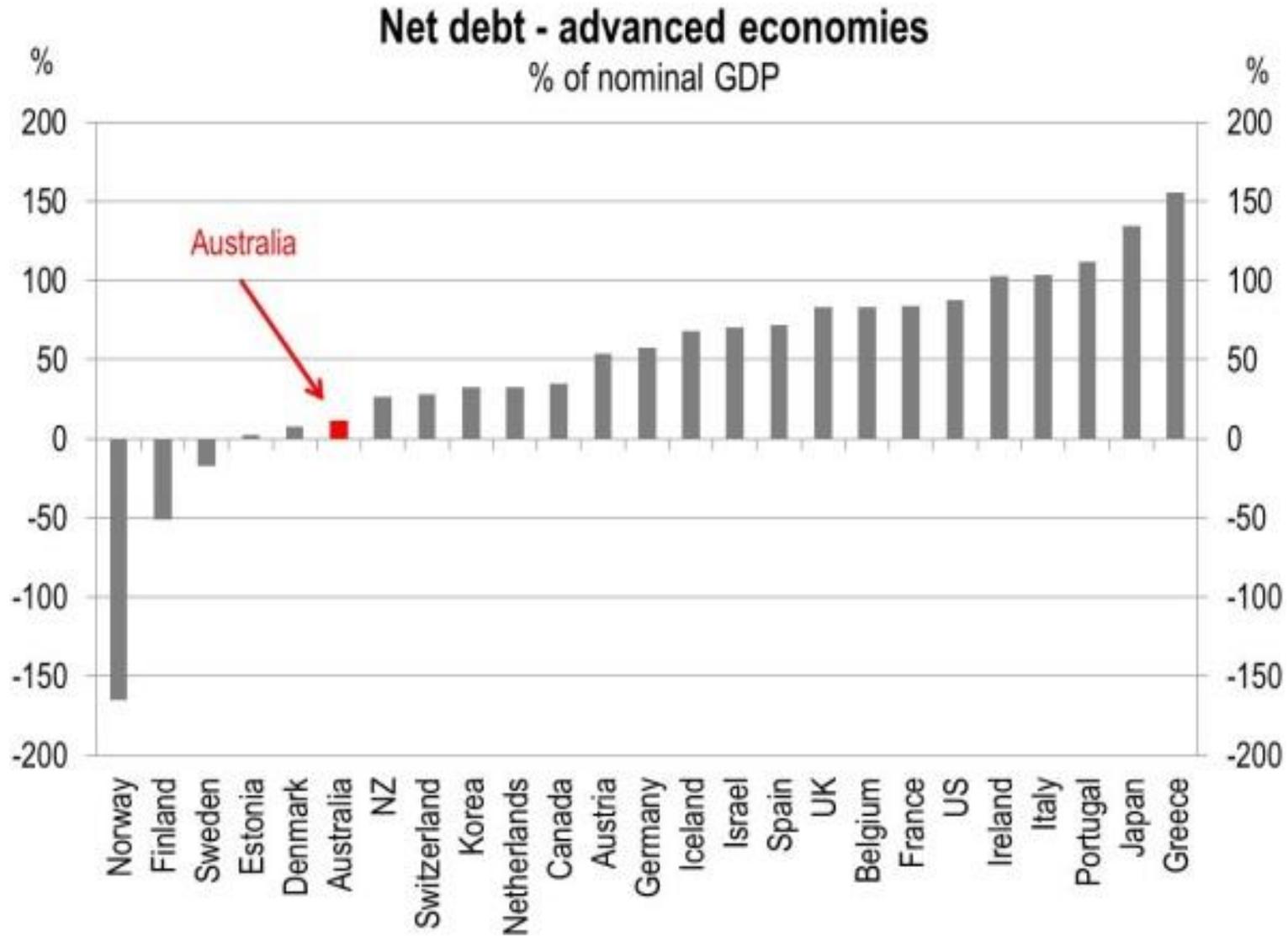
Source: Australian Treasury, HSBC estimates

Budget deficit has been mostly due to a fall in revenue, not rising spending

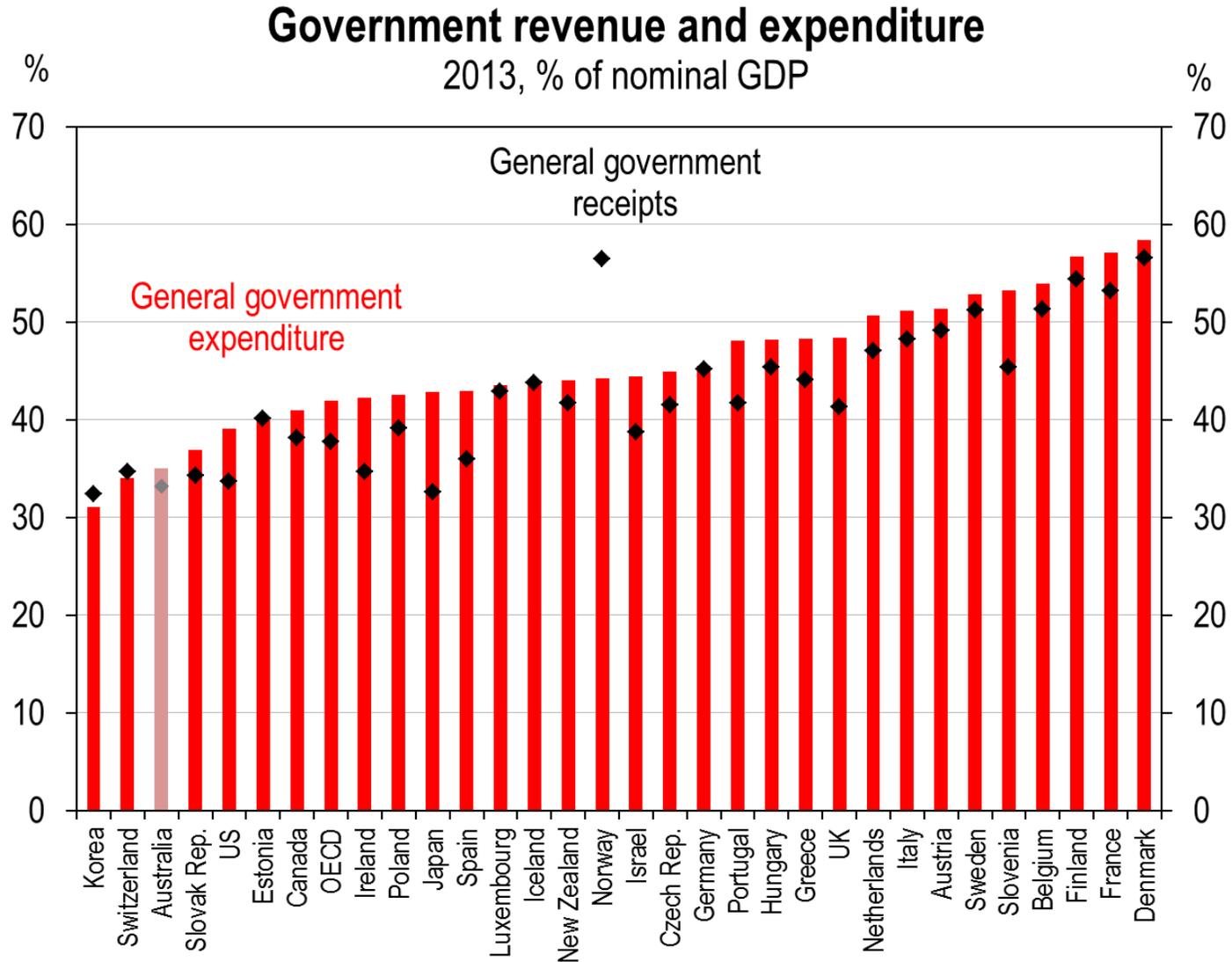


Source for both charts: Australian Treasury

Public debt could be lower, but is still low by global standards



Australian government spending and tax are not high by global standards

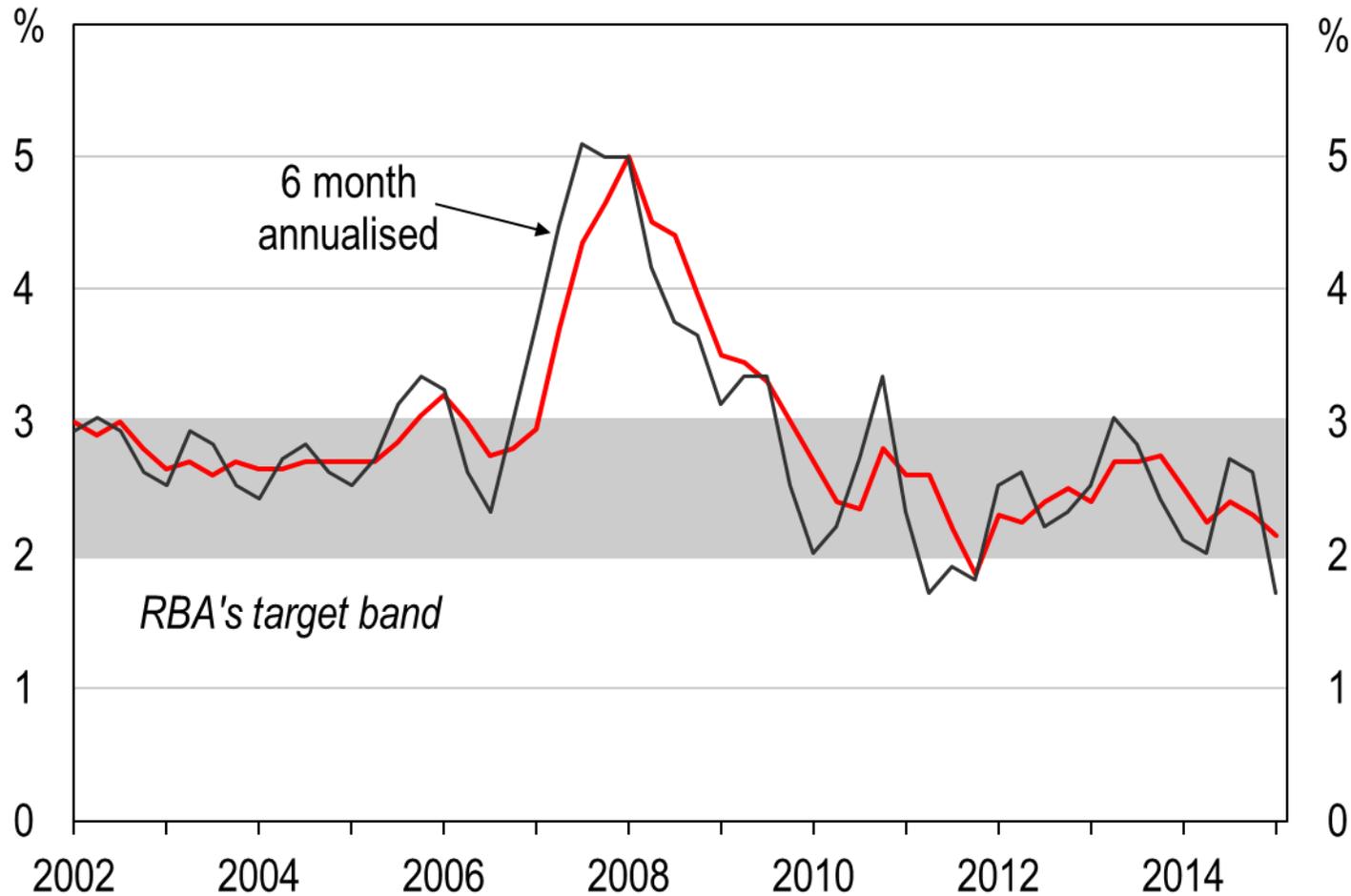


Source: OECD

Underlying inflation is low, leaving the RBA with scope to cut further

Underlying Inflation

Average of trimmed mean and weighted median (annual)



Key economic forecasts

HSBC's forecasts for Australia

	Year-average			Year-ended						
	2015e	2016e	2017e	Q215	Q315e	Q415e	Q116e	Q216e	Q316e	Q416e
%*										
AUSTRALIA										
GDP	2.4	2.8	3.2	2.0	2.5	2.5	2.4	3.0	2.9	2.9
Consumption	2.6	2.9	3.1	2.5	2.7	2.7	2.7	3.0	3.0	2.9
Public consumption	3.3	2.0	1.5	4.0	3.7	3.6	3.6	1.6	1.5	1.4
Investment	-2.6	-0.9	2.9	-3.7	-1.0	-1.8	-1.2	-1.4	-0.7	-0.1
- Dwelling	9.7	5.4	2.6	7.4	11.9	9.3	5.0	7.8	5.2	3.9
- Business	-6.6	-3.6	2.3	-6.8	-6.6	-6.8	-4.8	-4.8	-3.1	-1.6
- Public	-1.8	1.0	5.1	-4.5	5.7	3.6	4.5	-0.5	0.0	0.0
Final domestic demand	1.5	1.9	2.8	1.2	2.0	1.8	2.0	1.7	1.8	1.9
Domestic demand	1.5	1.8	2.8	0.9	1.6	2.0	1.8	1.7	1.8	1.9
Exports	5.4	7.8	7.7	4.5	4.7	4.8	3.8	9.7	8.6	9.2
Imports	1.9	3.6	6.0	-0.7	1.6	4.0	1.8	3.8	3.8	5.1
GDP (% quarter)	--	--	--	0.2	0.8	0.6	0.8	0.7	0.8	0.6
CPI	1.6	2.3	2.9	1.5	1.5	1.9	2.2	2.3	2.4	2.4
Trimmed mean	2.2	2.4	2.8	2.2	2.2	2.2	2.2	2.2	2.6	2.7
Unemployment rate	6.1	5.9	5.5	6.1	6.2	6.0	6.0	5.9	5.8	5.7
Labour price index	2.3	2.8	3.5	2.3	2.3	2.3	2.5	2.6	2.9	3.1
Current A/C (%GDP)	-4.2	-3.7	-3.8	-4.7	-4.4	-4.4	-4.0	-3.8	-3.6	-3.5
Terms of trade	-9.8	-2.1	-2.3	-10.6	-8.6	-7.8	-5.3	-2.0	-1.0	0.0
Budget balance (%GDP)	-2.5	-1.9	-1.5							
Capital city house prices	9.2	6.8	4.1	9.8	10.4	9.8	9.8	6.4	5.6	5.4
Private sector credit	6.1	7.0	5.8	5.8	6.1	6.3	6.5	7.3	7.2	6.9
USD/AUD (end period)	0.72	0.70	0.70	0.77	0.73	0.72	0.71	0.71	0.70	0.70
Cash rate (end period)	2.00	1.75	2.50	2.00	2.00	2.00	1.75	1.75	1.75	1.75

Source: ABS, RBA, HSBC forecasts

*unless otherwise specified

Disclosure appendix

Analyst Certification

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