Preparing for the year ahead
As 2014 begins, we are very grateful for the support of our customers as we grow our business across Asia. We’re also very proud of the great strides and investment we’ve made to support our customers doing business in Asia. Last year we continued to build our team appointing senior regional bankers to strategic positions. In addition, we opened our first branch in Mumbai and obtained the historic AUD/CNY Market Maker licence.

We also announced the establishment of the Westpac Asia Advisory Board and appointment of our first external board member, former politician and senior businesswoman, Mrs Hwee Hua Lim. The Advisory Board will guide and contribute to Westpac’s Asia strategy and we are excited to have held our first board meeting in Hong Kong during December.

We pride ourselves on the deep insights we can offer our customers who are looking to grow in Asia and in November we had the pleasure of hosting some of our customers in Sydney to discuss the optimum modes of entry into Asia. Just last month, our Global Head of Economics and Research, Bill Evans, shared his views with our customers in Hong Kong and Singapore on the outlook for 2014, details of which can be easily accessed via WIB IQ.

We are committed to continuing to deepen our capabilities to better support our customers and we are delighted to be offering new products, such as our Structured Commodity Finance business, which is featured in this issue.

As we enter 2014, we remain confident about the opportunities in Asia and look forward to keeping you at the forefront of changing market dynamics.

We wish you all a prosperous 2014.
Gearing up for the dollar’s bumpy ride
from India continues to rise, the Korean economy is expanding and Japan is changing its resource mix while experiencing stronger growth than it has seen for some time.

“Most significantly, China, the still-emerging mega-economy, is still growing faster than the rest of the world. More importantly, as an emerging economy it maintains the global demand for raw materials well above that for finished goods,” says Smirk. “Overall, we’re still seeing demand that is more than enough to hold prices at levels well above the historical norm. Undoubtedly, Australia’s about to experience a big rundown in investment projects in the next five years, but just as investment declines, production is set to surge. As such, we are still going to experience a combination of high commodity prices and high AUD over the next five to 10 years.”

Currencies, commodities and even forecasts will be subject to volatility...

For months we’ve been experiencing a salient and enduring characteristic of this new phase: volatility. “It’s what you get when you go from rapid growth to maturity,” says Smirk. Markets like movement, and during the investment boom the trajectory was firmly upwards. “Now we’re going to be treading sideways to sideways/down, and that means the Australian dollar will be bouncing around in a quite volatile manner. Growth in developed markets is sluggish at best, while developing markets are always more prone to stops and starts. For example, China’s cycles are shorter and sharper and that makes for a bumpy ride.”

Currencies, commodities and even forecasts will be subject to volatility, and it’s vital for people to be primed for it. “There are plenty of businesses that can go untouched by volatility but if it’s a threat to your business, you need to think about how to manage it,” says Smirk. “You’ve got to look to financial products that protect your income, through hedging and risk minimisation.”

Look beyond the volatility and there are some relative certainties to be found, Smirk suggests. The Australian dollar, which for some time in late 2012 and early 2013 was overvalued thanks to vast capital inflows, has come down to the mid-range of what we might consider fair value, at around $US0.95. Barring any shocks, either internal or international, Australia should experience a period where interest rates and commodities are again the key drivers of the currency.

In the near term, Smirk sees the global growth picture remaining “reliably sluggish” this year. Westpac’s view is that China is experiencing a slowdown, while the US remains in deleveraging mode, with an increase in fiscal expenditure unthinkable for the time being. With Europe still beset by tight credit and the risk of further flare-ups, recovery is unlikely to gain traction there until at least 2015.

“In this environment, commodity prices will be falling further. While ongoing liquidity programs from the US Federal Reserve will continue to act as a brake on any appreciation of the US dollar, Australia will also be facing two more rate cuts as the economy’s going slows as the investment cycle winds down. Westpac is forecasting the Australian dollar to depreciate to around $US0.85 in late 2014.”

Westpac expects to see global growth finally bottom out in late 2014 before improving as we head into 2015. “China will be right back on track and we’ll see a moderate improvement in the US and developing nations, pushing the Australian dollar back to the high 90s and even possibly back to around parity in 2016.”
Turning risk into rewards
A plethora of opportunities exist for Australian companies to both break into Asian markets and source imports. But understanding the risks is essential. In a roundtable discussion leading Australian executives and members of Westpac Institutional Bank traded tips on making the most of trade with Asia.

**Q** How do you manage risk when dealing with new suppliers or partners?

**A Mike Kotek, Tailored Packaging:** We always visit and we meet the people. After that we start with a small order. If the business grows significantly we try to split most of our business or products to two factories to spread the risk.

**A Andrew Eagleton, Jord International:** We do some of our design in either India or The Philippines, we have fabrication partners all over the world including China and Korea. Jord people live in these locations and work with the fabricators day in, day out performing QA, QC tasks to make sure that what we’re fabricating hits the quality and time schedules. This significantly reduces the risk of late deliveries and penalties by ensuring the product conforms to spec.

**Q** How do you deal with currency risk?

**A Mark Ryan, MD Tassal Group:** I think one thing the global financial crisis has taught everyone is to expect volatility. So, as a company faced with enough risk in agricultural risk, we try and avoid the commodity price risk and the effects of foreign exchange risk because they’re things way outside of our control in a five year cycle and three year growing cycle.... We try and deal in the Aussie dollar whenever we’re buying or selling now.

**A Bala Swaminathan, GM Asia, Westpac:** The volatility of currency is quite large and you can ill afford your margins going away on currency volatility, so clearly to be able to protect your margins and get back to your functional currency as soon as possible is important. The Aussie dollar/RMB capability was important. For Australian and Chinese companies to transact again in both their functional currencies that we have is fantastic.

**Q** What about country or counterparty risk?

**A Bala Swaminathan, GM Asia, Westpac:** We look at which countries we’d want to deal with and which countries we won’t because there are some countries which are more investment grade and some which are less investment grade and we allocate our capital risk based on that. In some of these countries when we are looking at the counterparties, we look at their business - reputation risk, in particular. Have they got sustainable practices? Do they employ child labour? Are they into things like forest destruction, if you like? And our choice of which counterparties will be good is predicated on good sustainable business practices.

*The attendees were Tony Day, MD Noble Resources Australia; Mark Ryan, MD Tassal Group, Andrew Eagleton, Financial Controller, Jord International; Shaun Egleton, Treasurer, Ricegrowers Ltd; Mike Kotek, Finance Director, Tailored Packaging; Andrew McDonald, GM Corporate Banking, Westpac Institutional Bank; Bala Swaminathan, GM Asia, Westpac; Gordon Sparrow, Head of Trade Sales, Westpac Institutional Bank.*
China

China’s economy is showing signs of a slowdown in the final months of 2013. The October and November updates on the investment cycle confirmed the infrastructure-led softening in this arena apparent in the Q3 national accounts. Railway activity is leading the slowdown with real estate investment on a modest decelerating trend. As flagged, housing controls have been re-introduced for Tier 1 cities.

In the political sphere, the Xi-Li leadership team scored high marks for their performance at the 3rd Plenum. Marketisation of the Chinese economy was front and centre of the communiqué, which was followed by an ambitious long term plan. The intent of the leadership is clear. They wish to remove the distortions that create income inequality within the system and they must convince the rank and file in the Party that they are serious in their resolve to do so. The plan is well made – it is now up to the leadership to execute their programme against the embedded interests that benefit from the status quo.

“Marketisation of the Chinese economy was front and centre of the communiqué of an ambitious long term plan.”

Japan

For the last twenty years, Japan has been fighting a losing battle against deflation. Prime Minister Abe is making some progress in curing this seemingly intractable problem but he needs help from Japan’s multi-nationals. The country needs its companies to invest and employ more at home instead of abroad and to raise wages for the local workforce. At the moment, Japanese companies have renewed international investment expansion after a temporary halt during the global financial crisis. Sales of foreign affiliates of Japanese companies outside Japan now exceed exports from Japan to the rest of the world.

Tokyo needs to offer incentives in order to lure back Japanese companies and their investments. The Japanese government could offer a ‘homeland investment’ style tax amnesty for companies that invest their foreign earnings in high-tech R&D. But Japan’s global corporates strong preference for foreign capex will be hard to shift. And in the face of an extremely stretched public debt position – gross debt is now well in excess of 200 per cent of GDP – it is hard to argue that taxes will be able to stay low forever.

We are unconvinced that the incentive matrix of Japan’s globally engaged, profit-seeking corporations will lead them home.

“In the face of an extremely stretched public debt position... it is hard to argue that taxes will be able to stay low forever.”
India

India is experiencing its worst year for economic growth since its 1991 balance of payment crisis. With a national election in early 2014, the government has not shown the political will required to enact a programme that would deliver the required boost to the country’s international competitiveness. Foreign interest in Indian assets, particularly debt, has declined rapidly, which has led to a sharp drop in domestic investment activity. With the US Fed now tapering its asset purchases in earnest, India will continue to face a considerable current account deficit funding challenge. On the plus side, changes to foreign direct investment access rules have recently attracted some big international names in the retail sector, while new RBI Governor Raghuram Rajan is universally respected and can be counted on to steer a sensible path for monetary policy.

Emerging East Asia

Emerging East Asia is showing signs of life again after sluggish growth early this year on the back of an improved global trade environment. In contrast, the Indonesian economy is slowing down as the result of capital outflows, softer commodity prices and the maturation of the domestic construction upswing. The advanced exporting countries of Taiwan and Korea have seen a recovery in business conditions as Chinese demand has stabilised. The Philippines had been the outstanding performer in the region prior to the typhoon hitting.

Despite challenging economic conditions, India continues to be a country to watch closely, given the reforms underway.

Regional Profile

India continues to be a country to watch closely. With a young population of 1.25 billion and the world’s third largest national economy in PPP terms, India is ripe with potential. However, 2013 was something of an annus horribilis for India, with a number of factors conspiring to lower growth and reduce investor confidence. Even so, “With challenging economic conditions, we are seeing the new Reserve Bank Governor announcing progressive reforms to make India an attractive investment destination” says Vikram Nimkar, Westpac’s Country Head of India. The RBI recently liberalised bank licensing to allow foreign banks a larger role in India’s banking sector and this has opened up a great opportunity for foreign investors and organisations. “Reforms include opening a swap window to attract foreign currency non-resident deposits [FCNR (B)], and increasing overseas foreign currency borrowing and foreign direct investments into India. Through these reforms the RBI has raised around US$25 billion in two months”.

Focus on India

Progressive reforms underway.
Shanghai Free Trade Zone

China is making substantial efforts to reform its economy and the Shanghai Free Trade Zone (FTZ) is just one example of this. It has been largely touted as a predictor of the future direction of China’s economy. Andrew Whitford, Head of Greater China, Westpac says, “There is significant potential with the free trade zone and it is definitely an exciting prospect for many of our customers and Australian businesses”.

According to China’s Ministry of Commerce, several measures to ease legal barriers for foreign investment will be implemented in the FTZ, including cancellation of the requirement on government approval for the establishment of foreign-invested enterprises (“FIE”) and removal of the restriction on foreign-invested auction enterprises to participate in the auction of cultural relics.

Restrictions on RMB convertibility and raising funds abroad for use in the zone will be lifted but there are still RMB risks on the capital account and a lack of transparency at this stage around regulations and cross-border activities.

Andrew adds, “Westpac has a number of onshore and offshore RMB products available for customers to assist their business in the zone. It is still early days and we are seeing continuous adjustment, so we are monitoring the zone’s development closely to help our customers benefit from the zone’s enormous potential.”

“There is significant potential with the free trade zone and it is definitely an exciting prospect...”
It’s no secret that the world is hungry for Australia’s raw materials. The country chalked up $177 billion of energy and mineral exports in 2012/13, and that number is expected to touch $300 billion within five years.

It’s of urgent importance to keep these materials moving to places like Asia, where China is the biggest customer and demand is robust from the likes of India, Korea and Japan. All along the commodities value chain – from producers to refiners, traders and end users – businesses need financing to keep operating and expanding.

That’s why Westpac Institutional Bank is expanding its Structured Commodity Finance capabilities ranging from short term working capital requirements via ownership based products such as Repos through to flexible medium term financing structures such as prepayment and borrowing base structures. It’s an area that requires a deep understanding of the processes and production cycles involved in order to isolate and mitigate risks.

Westpac Institutional Bank’s Global Head of Structured Commodity Finance, Paul Gardner, has been a structured finance specialist for more than 25 years – almost 10 of those in Asia – and he’s joined by a team of SCF specialists in Hong Kong and Singapore.

“Our focus is on using our deep understanding of commodity flows and the inherent risks to provide liquidity and financing solutions to our clients in a manner which minimises their and our risk, while optimising the utilisation of our clients’ credit lines,” says Gardner. “Structured Commodity Finance is a natural fit for an Australian bank looking to follow the trade flows of its Australian and Asian clients.”

Bukhara

Number 26 in San Pellegrino’s top 50 restaurants in Asia, Delhi’s Bukhara has barely changed its menu in 32 years. That’s because the popularity of the tandoor-driven North-West Indian and Pakistani cuisine has never wavered.

Situated away from the noise and bustle of chaotic Delhi in the diplomatic enclave, this iconic restaurant in the ITC Maurya Hotel allows diners to perch on camel hair stools and eat with their hands for an authentic Indian experience.

A favourite of Delhi’s political movers and shakers – Bukhara has also hosted two US Presidents in Bill Clinton and Barack Obama.

The signature dish is a whole leg of lamb marinated in malt vinegar, cinnamon and cumin and cooked in a tandoor oven, while that classic sub-continental staple – dhal – is a highlight.

Perfect for clients looking for sublime Indian food.

Bookings essential.

ITC Maurya Hotel, Diplomatic Enclave, Sardar Patel Marg, 110 021, New Delhi +91 11 2611 2233 itchotels.in

To find out more about Westpac Institutional Bank’s focus on Asia, speak to your Relationship Manager today.
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