



Year of the Tourist
Retail Forecasts February 2017
Public Executive Summary

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Year of the Tourist

International tourist visitation in Australia is at record highs, and spending by tourists (particularly from China) is exploding as well. This is giving Australia's retail sector a big boost. The strong growth in tourism over recent years is expected to continue during 2017, adding a key supplementary market for Australia's retailers. But tourists also exacerbate Australian retailers' vulnerability to international competition. As more tourists arrive onshore, more international retailers want to come along for the ride as well.

Still, strong growth in tourism is welcome news in an otherwise harsh landscape. Domestic retail sales demand remains sluggish, as record low wage growth, high levels of household debt, and uncertainty over interest rates and house prices are keeping overall spend growth low.

The full issue of Retail Forecasts includes a special feature article which delves into the effects of tourism on Australia's retail sector.

National Outlook

Real (inflation-adjusted) retail sales growth was 2.0% for the year to December 2016, reflecting a hard year for Australian retailers. We expect real retail sales growth will pick up a little over 2017 (2.4% growth for the year to December 2017), before recovering somewhat to 2.7% over 2018.

See Chart 1 below for our forecasts of nominal and real retail turnover.

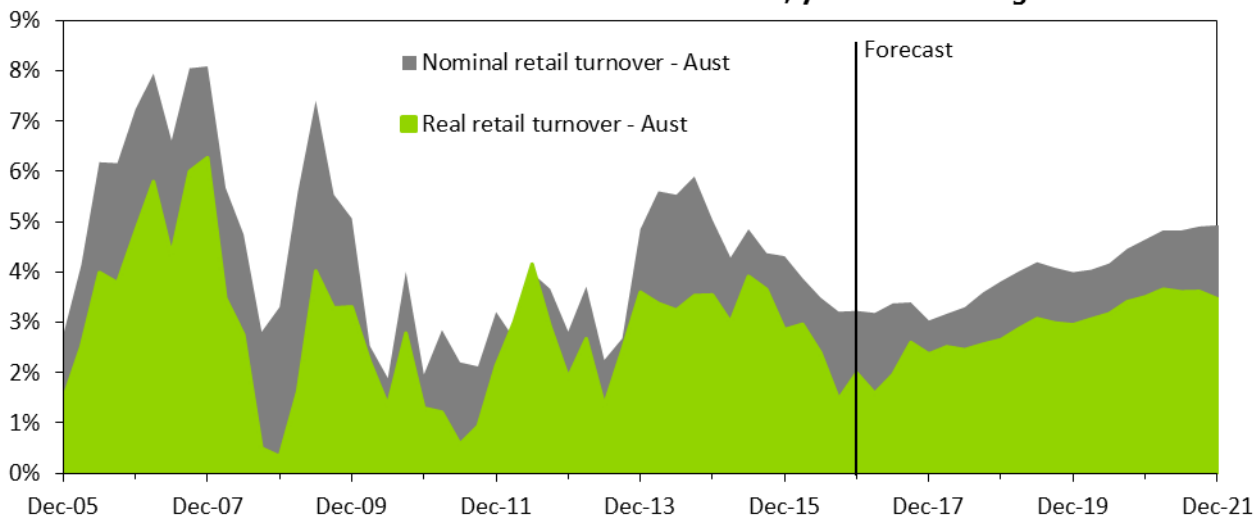
Key changes since last issue

The December quarter of 2016 showed a strong recovery in retail spending, of 0.9% during the quarter. Not to be confused with a Christmas rush (data is adjusted to exclude seasonal effects), this swing is a welcome correction for retailers, after real (inflation-adjusted) sales shrunk over the September quarter.

Employment in 2016 swung hard to part-time jobs. Over the year, the number of full time jobs in Australia shrank by 56,100, while part-time jobs rose by 159,400. Continuing underemployment in Australia is keeping wage growth at record lows (1.9% nominal growth over the year).

Retail profits are under pressure. The last six months of data for retail profits has shown the lowest results in almost five years. Intense competition mixed with slow spending growth are important contributors to this result.

Chart 1: Nominal and real retail turnover, year-to % change



Source: ABS 8501.0, Deloitte Access Economics

Economic influences

Global growth and trade is improving, despite the influences of nationalism (Trump, Brexit) and growing uncertainty. After years of disappointment, global growth is about to surprise on the upside and, despite the protectionist rhetoric emanating from the United States, it is Asia's economies that are in the box seat for the coming year. In fact leading indicators are already pointing to a lift in world trade, and if Asia outperforms, they will drag Australia along for the ride.

Jobs growth is expected to stay slow for a while longer.

Unemployment has only managed to stay steady because more workers are retiring, and because there has been a switch from full-time, high earning mining employment to part-time employment in services sectors. Population gains are also down on past peaks, meaning there aren't a lot of new workers flowing into the economy (either from coming of age or moving here from overseas). All this is contributing to the record low wage growth seen over 2016.

Credit is likely to remain super cheap for some time. Interest rates will keep rising in the US, and other nations will eventually follow suit. But the new RBA Governor is a little more relaxed about low inflation, and a little less relaxed about crazy housing prices. That mix should keep the RBA on the sidelines, but not forever. By late 2018 rates are expected to be rising in Australia, and through 2019 much of the world will be seeing the same. Chances are the \$US will continue to rise versus other currencies, including the \$A. We see smaller \$US gains than some do, but those gains – and the threat of possible tariffs – could see the fall in China's yuan accelerate through 2017.

International tourist visitation in Australia is at record highs, and spending by tourists is exploding as well. The strong growth in tourism over recent years is expected to continue during 2017, adding a key supplementary market for Australian retailers. Tourist shopping expenditure from China alone is already around \$1.4 billion per year, and is set to almost quadruple over the next decade. Strong growth is also expected from India and the Middle East. International tourism is also adding competition to the Australian retail market, as tourists demand more international brands during their stays.

Retail is a major part of the tourism market. During the 2015-16 financial year, tourist expenditure (including domestic and international tourists) totalled around \$130 billion. Retail spending accounted for around 39.7% of this expenditure, including \$36.1 billion (27.7%) on food retailing and \$15.6 billion (12.0%) on non-food retailing.

China may be firing once more, but that isn't true of the 'sunbelt' States – Western Australia, Queensland and the Northern Territory have been hit hard by the mining-related construction slowdown, and their rising exports haven't filled that gap. With interest and exchange rates lower, it's been time for the south and east of the nation to shine, including in retail spending. Yet, having experienced a big housing boom, NSW and Victoria are now faced with inflated housing values and a risk of apartment oversupply. There may be a narrowing of State outcomes from 2018 onwards as sunbelt States emerge from their downturn.

Retail spend trends

We expect a steady improvement in retail sales through 2017 (Chart 3), which is likely to coincide with a modest improvement in jobs growth over time.

Non-food sales growth is slowing, while food starts its recovery.

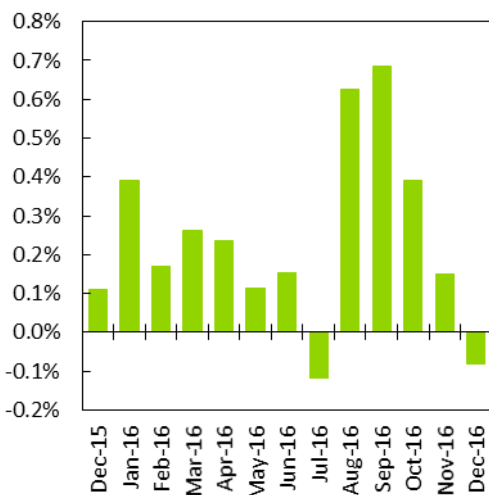
Non-food turnover growth is still outpacing food, but 2017 could see turnover growth converge. At least, temporarily. Sluggish wage growth and a cooling housing cycle means consumers are tightening their purse strings on more discretionary spending. Steady population growth and rising jobs growth should provide some support to the rate of growth in food sales. Department store turnover shrinkage is dragging down the total non-food result, while apparel continues to be the standout category.

Apparel's strong spend growth isn't enough for some retailers.

Apparel turnover is growing more rapidly than any other retail category, but many of the factors that assist apparel expenditure also create risks for retailers. The importance of online retailing in the apparel market is giving rise to an influx of international competitors, as has the rapidly growing tourism market. And a number of Australian apparel retailers couldn't handle the heat. Voluntary administration of retailers including Marcs, David Lawrence, Herringbone, Rhodes and Beckett and Payless Shoes indicate that category growth is not the only precursor to retailer success.

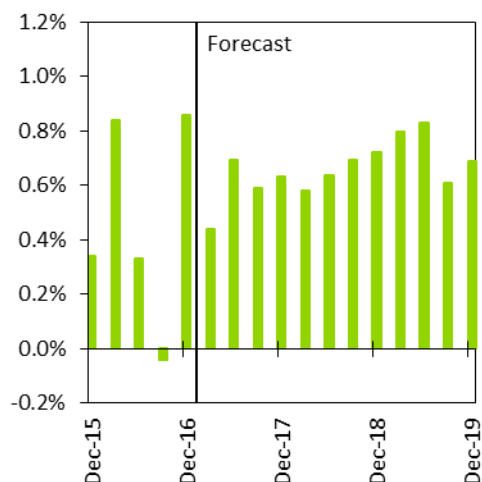
Demand for prime CBD assets is driving retail investment. The value of retail building approvals has been rising steadily over the past couple of years, at an annual rate of 11% over 2015 and 2016. Investor demand for retail assets has risen as low interest rates reduce the cost of funding. Prime retail assets are in high demand, as international retailers flock to Australia. Indeed, Sydney's Pitt Street Mall is now the 7th most expensive retail zone worldwide, with average rents exceeding \$13,000 per sq.m. Major fashion houses from overseas have shown their willingness to pay more for prominent, attractive flagship store leases.

Chart 2: Nominal retail turnover, monthly % change



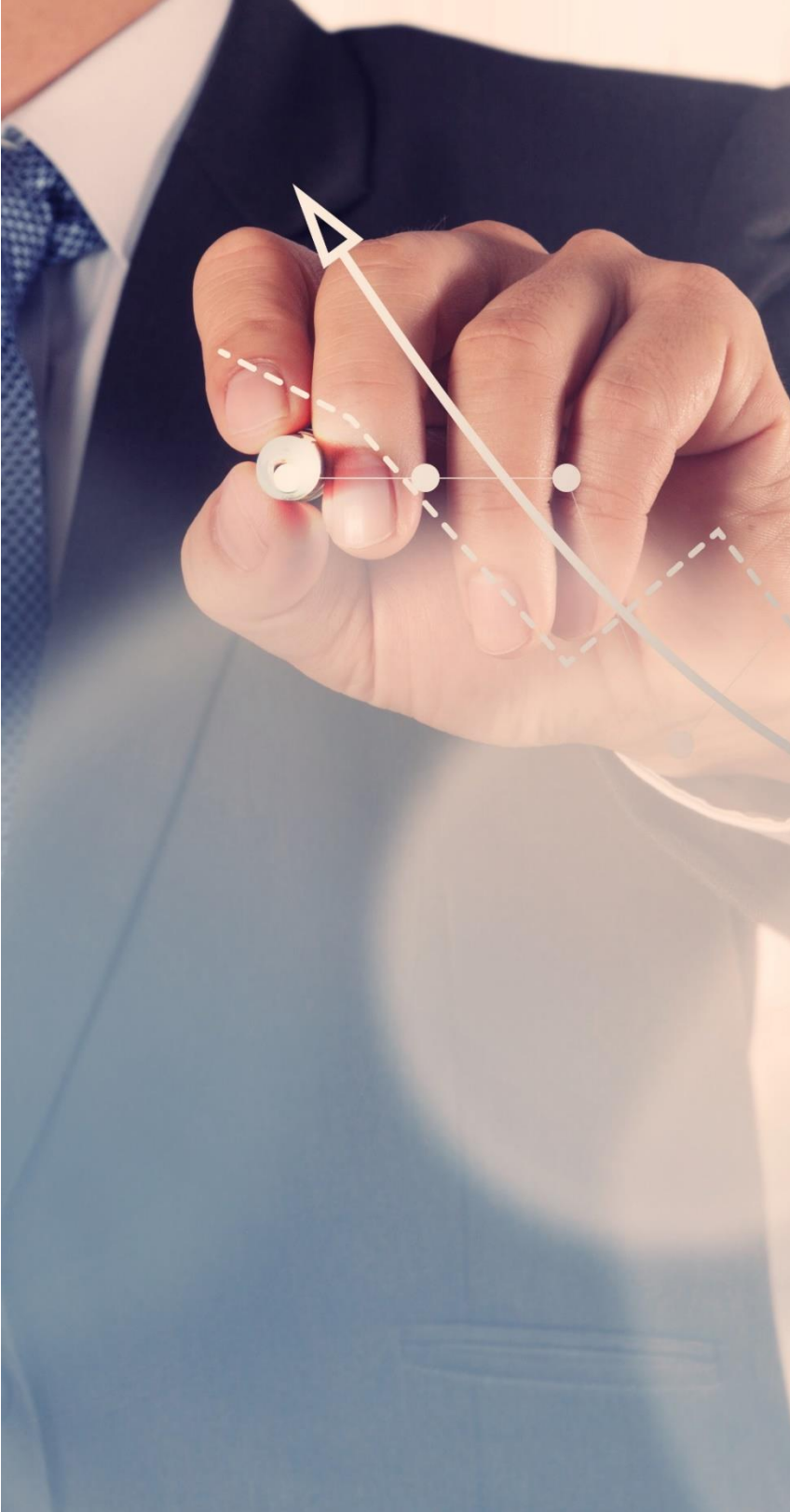
Source: ABS 8501.0

Chart 3: Real retail turnover, quarterly % change



Source: ABS 8501.0, Deloitte Access Economics

What is Retail Forecasts?



Retail Forecasts, produced quarterly, provides detailed analysis of current retail sales and consumer spending, and the important economic drivers which influence them.

Included are National retail forecasts, retail category forecasts and State retail forecasts, as well as the broader income and non-income influences of retail spending.

An annual subscription includes four quarterly reports plus Excel spreadsheets including 10 year forecasts and charts.

The accompanying Detailed Consumer Spending provides ten year forecasts of detailed Household Final Consumption Expenditure categories and detailed Retail Sales categories.

Contact us

We are happy to respond to any inquiries in relation to the publication or our forecasts.



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