Trends

MAY 2016

A bulletin of economic developments in South Australia

Health sector in excellent shape

Bright outlook for South Australia's largest employer

Inside this issue

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Chief Executive's Foreword

Our health success story

Welcome to the latest edition of BankSA's economic bulletin, *Trends*, compiled in conjunction with Deloitte Access Economics.

In this edition, we examine the outlook for South Australia's health sector including the opportunities that an ageing population, rising incomes and increasing life expectancies hold for the state's future prosperity.

Health is already big business in South Australia, and this latest *Trends* report shows it is primed for continued growth well into the future. The report highlights that there is no sector with more opportunity for future growth, nor is there a market less prone to volatility.

As the largest employer of South Australians, more people work within South Australia's health sector than in retail trade and manufacturing. And while employment in other industries has plateaued in recent years, the health sector has seen a rate of increase of more than double the national average in the past 15 years.

In 2014, Deloitte identified the 25 sectors that it saw as having the greatest potential for growth in the next two decades. Five of them were highly relevant to the health sector, including community and personal care, retirement living and leisure, residential aged care, preventative health and wellness, and the digital delivery of health.

While there are considerable driving forces behind this ongoing growth, none is more dominant than our ageing population – and this means there's big spending ahead.

In 2013, one in 26 Australians was aged 80 and over. By 2030, this number will rise to one in 18. This is a significant statistic.

We know that older Australians are bigger customers of the health system, and with the number of older Australians climbing rapidly, it becomes a relatively simple equation.

The Federal Government's *Intergenerational Report* explains that the impact of an ageing population will increase demand for hospital beds, and the figures in this latest *Trends* bulletin correlate with this theory.

Apart from the moderate impact of maternity services, the need for hospital stays climbs dramatically after a person enters their seventies – with the over 75 age group accumulating an average of 1.4 hospital visits per year, more than double that of the 55-64 age group.

Our ageing population won't just increase demand for health services, it will change the shape of these services as we know them.

Just as baby boomers changed the nature of Australia's schools in the 1950s and 60s, they will also change the aged care sector.

Nursing homes will undergo transformations to accommodate more people – people who have more money, and specific needs and wants. And as aged care facilities become overpopulated, private enterprise has the opportunity to meet demand by offering these same services to people within their own homes.

The needs of elderly Australians will extend well beyond the sector itself – to retail, food and home maintenance – providing further new opportunities for small business to take advantage of the burgeoning market.

Despite our ageing population though, our vitality continues to increase. Australians are living longer, resulting in a shift towards chronic conditions requiring more treatment – and a greater output from the health system.

Diabetes alone is projected to increase spending in the sector by 436% between 2003 and 2033, with dementia and Parkinson's disease following close behind. Health markets are already transitioning to cope with these projections.

As the income of our population grows, so too does our willingness to spend on our health. As such, many of the health care services and products that were once considered alternative options are now becoming mainstream.

Preventative health to combat key lifestyle factors and perceived drains to our economic prosperity will be of key consideration in the industry – leading to more opportunities for providers of alternative medicines and therapies.

In fact, no health market is likely to see as much growth in the coming decades than health and wellness. As we live longer, we want to live better, and businesses providing solutions to the factors which put our health at risk, including obesity, smoking and stress, are poised for significant growth.

While the uptake of digital services within the health sector has been relatively slow when compared to other industries, our state has the opportunity and the means for further growth in this space.

With an excellent track record in manufacturing medical devices and our willingness to try new health care delivery models, South Australia is well positioned to pioneer next generation products and solutions. Tele-consultations, such as psychiatry and other specialities, tele-radiology, imaging that is acquired locally but processed in the cities, and remote patient monitoring are all areas of health care which will become common place, supported by the further expansion of our telecommunications capacity with the NBN.

Naturally, as incomes grow and the population ages, the quality and cost of health care will continue to rise faster than costs on the average economy. The agreed National Disability Insurance Scheme (NDIS), as an example, will add 1% of national income to the wider health care sector – a boost which will become most recognisable within the next half-decade.

The cost of health for consumers is also rising faster than CPI, and while family budgets will be put under pressure, the growth in prices will make a hefty contribution to the health of the sector in the long-term.

While significant growth often brings with it volatility, this has not been the case for the state's health sector. The Australian Bureau of Statistics shows that the Health Care and Social Assistance sector had the lowest business exit rate in 2014-15 compared to any other sector. It also showed that businesses within the sector were the most likely to survive between June 2011 and June 2015.

But while future opportunities in the sector are plentiful, now is the time for businesses to act if they want to take full advantage of the growth that awaits.

Hospitals and aged care facilities should now be re-allocating their budgets and implementing staff training programs and timeframes in line with the trend towards 'at home' care.

Universities must be armed with the research budgets – and the impetus – to find new, affordable treatments to the chronic conditions which will affect not just our retired population, but our ageing workforce, and thus impact our economy.

The rising cost of health care should be addressed to ensure long-term affordability for families, at the same time as ensuring sustainability for providers who will be relied upon more heavily by the ageing population.

And while the opportunity for growth in e-health is undeniable, we must be prepared to change our traditional views on the provision of health care and the storage of health records in line with our modern approach to other forms of business, such as banking.

Ultimately though, this *Trends* report outlines a bright future for South Australia's health sector and those businesses that position themselves to capture the opportunities ahead.

N. C. Reade

Nick Reade
Chief Executive, BankSA

117,000

The number of people employed in South Australia's health sector.

1 million

The number of Australians who will be aged over 85 by 2040.

1.4

The number of hospital visits per year for people over 75, which is more than double that of the 55-64 age group.

Our ageing population won't just increase demand for health services, it will change the shape of these services as we know them.

Health sector in excellent shape

"Investing in health will produce enormous benefits"

- Gro Harlem Bruntland

"It is your health that is your real wealth, not pieces of gold and silver"- Mahatma Gandhi

"Life expectancy would grow by leaps and bounds if green vegetables smelled as good as bacon"

- Doug Larson

South Australia's economy has some well-known challenges. Previous issues of BankSA *Trends* have covered the imminent closure of car manufacturing operations in this state, as well as challenges for defence manufacturing in South Australia.

However, we shouldn't overlook one success story. The state already has one large and increasingly prospective industry - a sector which is already South Australia's largest employer – the health services industry.

Health care may already be a sectoral success story, but there's even better news for its long-term prospects. Australia's living standards are growing and our population is ageing, meaning that both the quality and the cost of health care are rising faster than costs on average in the economy. That suggests health will become an even bigger business in the future than it is today. That's even truer than most realise. For example, the nation has agreed to a National Disability Insurance Scheme (NDIS) that will add 1% of national income to the flow of funds going into the wider health care sector, and much of that boost will only become evident some five or six years from now.

Much of the health sector is largely hidden from everyday view. From personal trainers through to manufacturers of medical equipment and your local chemist, the reach and impact of the health sector travels further and faster than is widely recognised.

An ageing population also means that there's considerable potential in a number of related markets, including preventative health and wellness. Some have even gone as far as to suggest that businesses in this state will benefit from a developing 'growth cluster' of health-related businesses on the back of megatrends such as rising life expectancies, rising relative health care costs and tightening public sector health budgets.

And there's one last important point to note. In economics, rapid growth is usually accompanied by volatility, with risk rising alongside returns. Yet the health sector can claim both good growth prospects and a lack of volatility, with official business exit data indicating that businesses in the health sector have far better survival prospects than average.

Health is already big business in South Australia

While this special report focuses on the potential for growth in business opportunities in health and related sectors in South Australia in the years ahead, it is worth starting with the simple recognition that there's already a massive market at play here.

The health sector is already the largest employer in the state, shown in Chart 1.

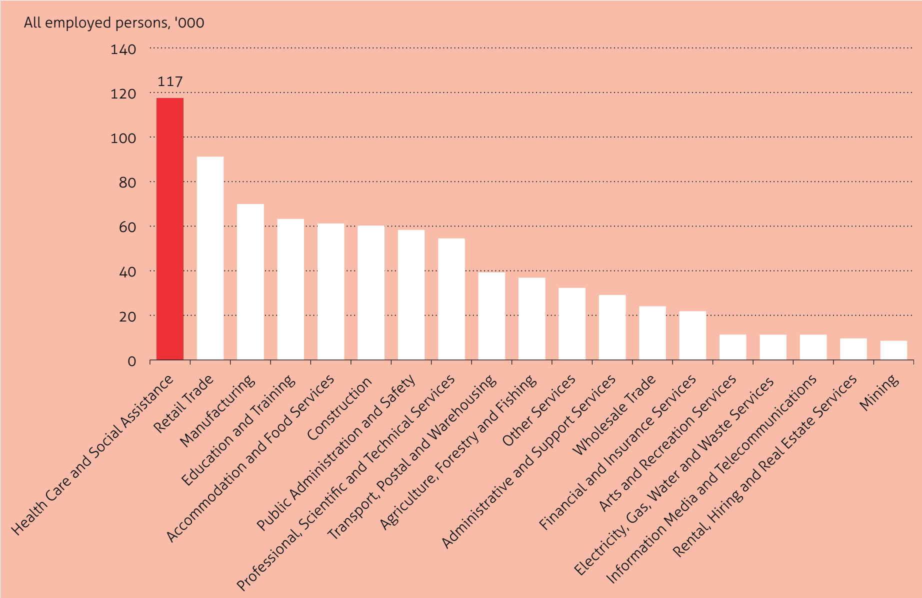
The health sector already employs more people than the retail sector, and it employs almost twice as many people as South Australia's construction sector.

That wasn't always the case. This sector took the mantle of the state's leading employer after many years of solid growth.

That can be seen in the overall employment trends in the health care and social assistance industry and in all industries, as shown in Chart 2.

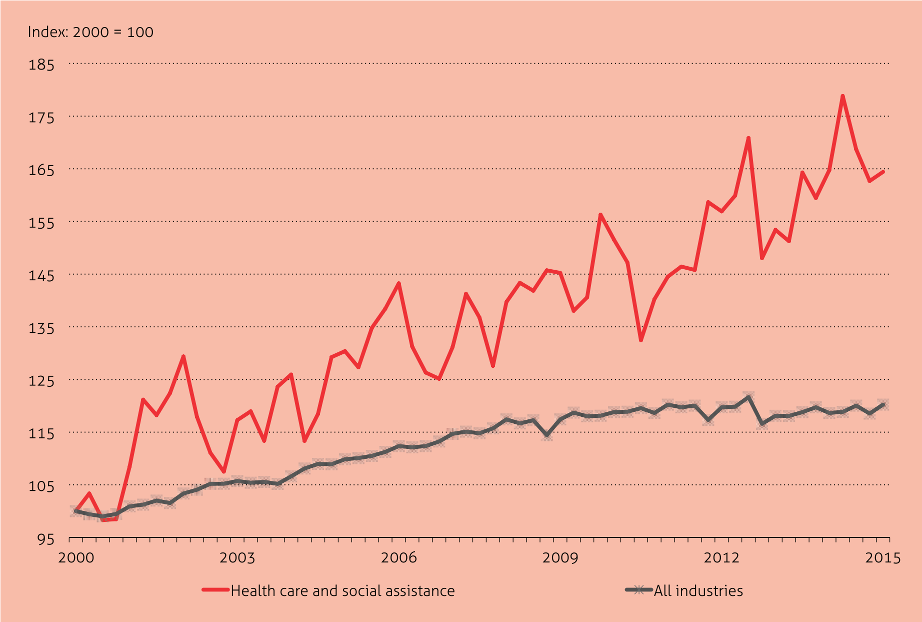
Chart 2 shows how the health sector (medical services, hospitals and aged care facilities) has been a very strong contributor to job growth in recent years. Over the past 15 years,

CHART 1
SOUTH AUSTRALIA'S EMPLOYMENT BY INDUSTRY, NOVEMBER 2015



Source: Australian Bureau of Statistics

CHART 2
SECTORAL EMPLOYMENT TRENDS IN SOUTH AUSTRALIA



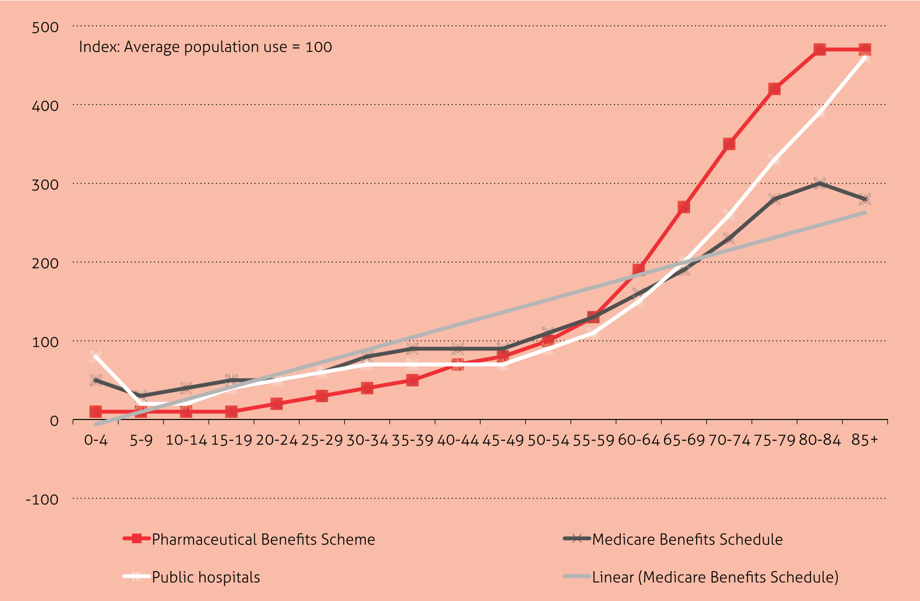
Source: Australian Bureau of Statistics

the rate of increase in employment has been double the national average. And whereas employment levels in all other industries has plateaued in South Australia in recent years, the health sector continues to grow strongly.

Health care is a labour-intensive sector, with a long track record of success in employment that is underpinned by the need for one-on-one interactions with patients and clients in many health care services.

The big picture trends underpinning the future success of the health care sector – such as an ageing population and increases in life expectancy – aren't a hypothetical. Indeed, these trends have already been shining through in the job growth evident across the

CHART 3
RELATIVE USAGE OF HEALTH SERVICES BY AGE



Source: Federal Treasury

sector and having a real impact on jobs more broadly across the state.

The next big thing

Health services are rising in importance in South Australia as businesses position themselves for the opportunities ahead.

The obvious factor in play here is that an ageing population will generate more jobs in the health sector down the track.

But there is a short term growth opportunity that hasn't yet caught the imagination of most Australians, and it is the largest short term accelerator of business opportunities in this sector.

As a nation, Australia has already agreed to the NDIS that will add 1% of national income to the flow of funds going into the wider health care sector.

Much of that boost will be evident within five or six years from now. And, as noted about the sector more generally, caring for the disabled is a very hands on business. A large portion of the $20 billion a year that state and federal governments are budgeting to spend on the NDIS will end up being spent on the wages of carers and related services for almost half a million Australians living with a disability.

At a time when the national and state economies are travelling relatively slowly, that boost from the coming ramp up in NDIS spending looks likely to be one of the few certain sectoral opportunities open to Australian businesses in the next few years.

An ageing Australia means expanding demand for health services

The largest single driver of sectoral opportunity for businesses in the health sector for many years to come is derived from two key drivers:

1. Australia is ageing; and
2. The cost of health care rises faster than costs on average in the economy.

It is therefore important to recognise that, no matter how large Australia's health markets are today, they will be considerably larger in the future.

Moreover, we already know what a lot of that increased demand will look like. In particular, the ageing of Australia's population will mean many more people over the age of 85, a relatively high proportion of whom will be suffering from a range of chronic conditions.

That points to a unique advantage for businesses selling into these markets – they know that the future looks bright.

Governments, businesses and families are becoming increasingly aware that they face twin challenges in coming decades: ageing population and health cost inflation. Both of these factors will add to the size of the health care sector in the next several decades, as well as change its composition.

The coming wave of growth in health care will see a major shift in the spending habits of Australians, presenting a range of business opportunities as it does so.

If 'demographics is destiny', then the future of health and related industries is bright. That very destiny represents a long term opportunity for Australian businesses to invest in what will clearly be a growth industry in coming decades.

Growth will come with new approaches to funding and providing care. While the health sector has a long history of not-for-profit and charitable providers, there will be new business models created as the sector sees substantial change.

Some businesses are already succeeding in doing just that, and more will undoubtedly follow.

It is not just that Australians are living longer, and that there will be a relatively older population in the future. It is also that:

- We will be wealthier;
- We will have access to more complicated (and probably more expensive) technologies; and
- We will be suffering from more chronic diseases which may be treatable without being curable.

The first challenge – Australia's ageing population – will boost the size of the health care market as, over the next quarter of a century, the number of people over the age of 85 in Australia rises from some 400,000 today to well over one million by 2040.

This change in the composition of the population will add rapidly to demands for health services, and those demands will rise even more rapidly than the base number of older Australians might suggest.

As Chart 3 makes clear, the use of health services rises rapidly as people age. The average cost of hospitalisation for people aged 65 to 74 is double that of those 55 to 64, while hospital spending per person for those aged 85 and over is almost five times that spent on those aged 55 to 65.

Chart 3 demonstrates the basic maths behind the potential growth of the core of the health sector – older Australians are bigger customers of the health care sector than are younger Australians, and the number of older

Australians is climbing fast.

Nowhere is that wave of growth more evident than in South Australia. With South Australia and Tasmania being Australia's oldest states, population ageing is driving the South Australian health sector in a way that the majority of states have yet to see – and that trend will only intensify in the future.

> **"The coming wave of growth in health care will see a major shift in the spending habits of Australians, presenting a range of business opportunities as it does so."**

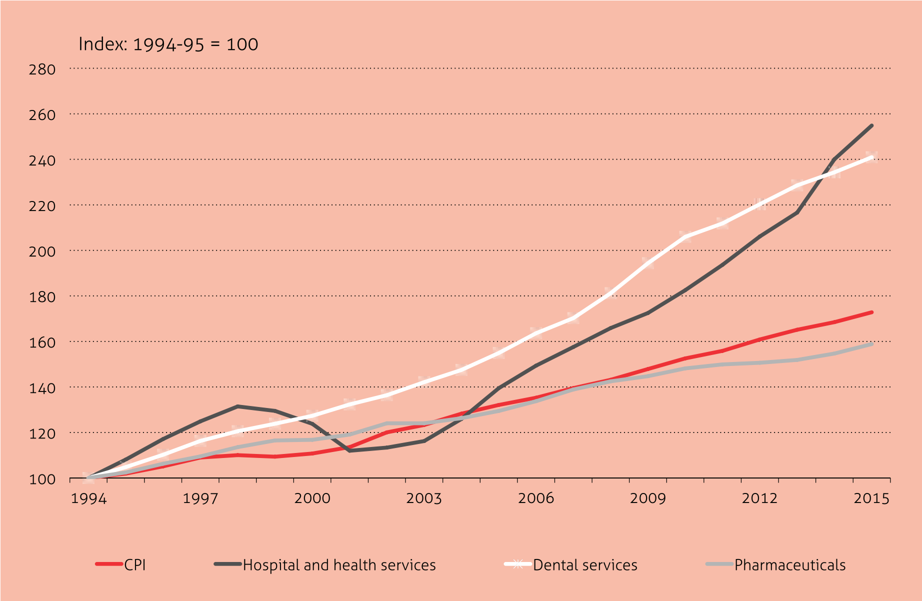
However, it's more complex than just the simple growth in the numbers. A change in the composition of health demand is also likely to be a key driver of future business opportunities. Rising life expectancies in Australia and other developed nations mean that we are seeing a shift towards chronic conditions such as diabetes, some types of cancer, dementia, Parkinson's disease, cardiovascular disorders and musculoskeletal diseases.

These chronic conditions are also likely to be future drivers of health spending. As Australians live longer, we are increasingly living with ailments that are not life threatening, but require more care than otherwise. There is therefore a transition underway within health markets towards chronic conditions.

What will that change generate? The Australian Institute of Health and Welfare has projected future disease costs as our population ages:

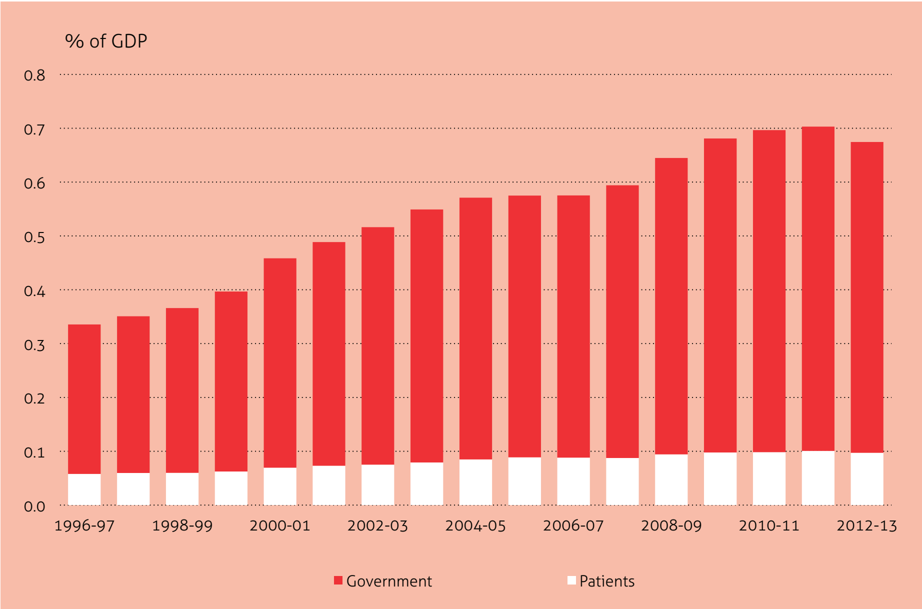
- Diabetes is projected to have the largest percentage increase in market size (with a 436% increase in spending projected between 2003 and 2033), followed by dementia (364%), Parkinson's disease (334%), digestive disorders (238%) and sense disorders (236%); and
- The projected growth in diabetes spending (436%) is due to many reasons, though the expected increase in obesity is a major factor.

CHART 4
HEALTH PRICES RELATIVE TO THE CPI



Source: Australian Bureau of Statistics

CHART 5
SPENDING ON PBS MEDICINES – SHARE OF GDP

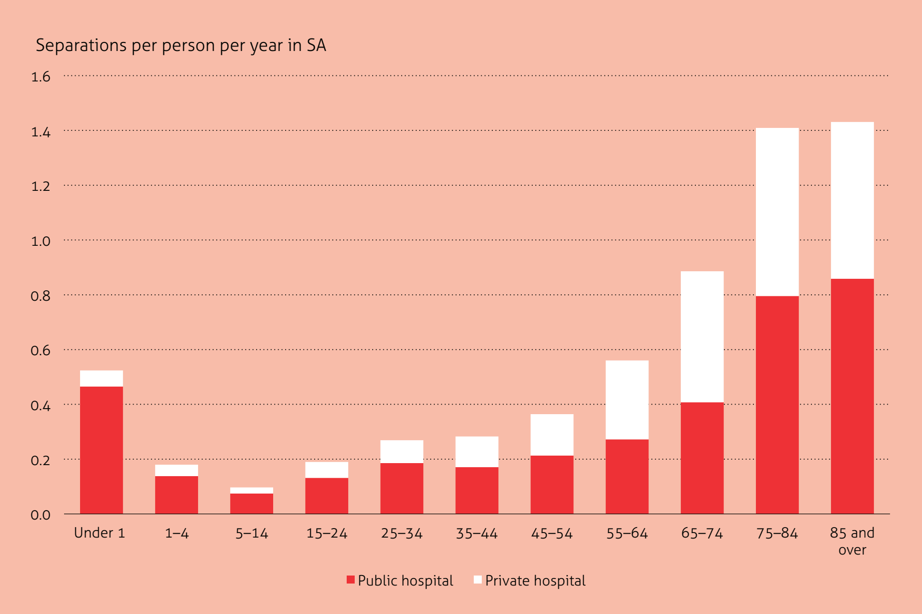


Source: Department of Health

Most businesses in Australia can look to the future with some confidence, but few can beat the confidence attached to the predicted future growth in health markets.

The second key business opportunity worth noting here comes from rapid health price inflation. As Chart 4 shows, the consumer costs of health have increased far faster than the CPI over time. And governments are not the only ones caught between rising prices and an ageing population; family budgets will also be increasingly stretched as rising health costs bite.

CHART 6
AVERAGE ANNUAL ENTRIES BY AGE



Source: Australian Institute of Health and Welfare and Australian Bureau of Statistics

For example, the price of hospital and dental services has increased ahead of prices more generally.

While the chart also suggests that the cost of pharmaceuticals to consumers has not risen particularly dramatically, the costs faced by government have not been so benign, with taxpayers picking up the tab in order to shield consumers from rising pharmaceutical costs. The same is also true for private health insurance; the fall in the cost of hospital and health services in 1999 and 2000 was due to the introduction of the 30% private health insurance rebate at that time.

Developments such as the listing of new medications on the Pharmaceutical Benefits Scheme (the spending on which is shown in Chart 5) and greater use of diagnostic procedures are likely to be an important driver of health spending pressures over the longer term. They are also an example of the way in which new technology is leading directly to new products and increased activity in the health sector.

These new medications and new medical technologies are likely to be expensive – and that means bigger dollars in the bucket that businesses in the health sector will be competing for.

Rising incomes will also be a driver of future success

Traditionally, health spending has also grown over time not merely because costs in health care rise faster than they do in other sectors, but also because health goods and services are highly income-elastic.

That is, as income grows, individuals want to spend more of their income on health care.

Indeed, health has one of the highest income-elasticities of all types of spending – unsurprisingly, humans have a voracious appetite for a healthy life and, so far at least, health technologies have delivered exactly that in enabling the supply of greater longevity and wellbeing.

Higher living standards have seen Australians demanding greater access to a wider range of health care over time. Moreover, the level of quality we demand from the health services we do receive would have been unheard of merely a decade ago.

Many of the health care services and products that were once considered a waste of money by doctors and patients are becoming more mainstream as incomes rise.

So not only are more Australians spending more money on the health services of yesterday, growth in living standards is helping to increase our appetite to spend on the health services of tomorrow.

Other things equal, that is yet another reason why the health sector – and related spending – has a bright future.

The health sector is wider than you think it is

For Australians, the words 'health sector' typically conjure images of the type of health care funded by Medicare. Yet much of the health sector is hidden from everyday view, and no Medicare card is required.

Medical and health care covers a variety of services, including general practitioners, specialists, pathology, x-ray and diagnostic services, allied health professionals (dentists, optometrists, physiotherapists and chiropractors) and ambulance services.

The broader health market, employing over a million Australians, also includes the manufacturing and sale of pharmaceuticals, the health insurance industry, and the fitness sector.

> **"Aged care needs are greatest among those aged 80 and beyond. In 2013, this group accounted for one in every 26 Australians. By 2030, one in every 18 of us will be over 80."**

The middle market also includes a number of complementary health services such as acupuncture, reflexology, osteopathy and massage therapies.

And, just as the core of health markets will benefit from some of the megatrends mapped out above – including ageing and the relatively rapid pace of health care inflation – so too will a trail of related businesses and professions.

Hospitals

Let's consider a core activity of the health sector, and its future. Current expectations – including those mapped out in the Federal Government's *Intergenerational Reports* – are that the impact of an ageing population will show up dramatically in an increase in demand for hospital beds.

While other components of spending are already skewed towards older age groups, the comparative figures for hospitals are even more dramatic. Chart 6 shows the average number of separations (episodes of care) by people of different ages.

Apart from the moderate impact of maternity services (which see most children and their mothers spend some time in hospital after birth), the need for hospital stays begins to climb dramatically once a person enters their seventies.

Even in their sixties, a person experiences twice as many episodes of care in a hospital as someone in their thirties.

It is true that state and federal budgets are under a lot of pressure, and that therefore there are no guarantees that taxpayers will be willing or able to pay for the cost trends that the above implies.

Yet it is worth considering this from another perspective - that within one of the fastest growing sectors in this state, governments will be winding back their share of the pot.

Other things equal, that says the opportunities for the private sector will grow even faster than the health sector as a whole.

This result, as well as recent clinical and funding trends, points to new opportunities in the privately-funded health sector. The change in policy toward making care in the home easier for those with limited mobility also creates opportunities for privately funded home assistance services.

In particular, a shift toward more flexible day surgery facilities and elective treatments sought by private patients is proving attractive. And the combination of an ageing South Australia with rising income and wealth suggests that more of the same lies ahead.

Aged care and residential care services

The big boom in aged care over the past decade was in care delivered at home, moderating growth in nursing homes. Yet the latter will see standout growth in coming decades.

Aged care needs are more closely tied to the age of prospective residents than is true of either hospital or broader health care costs. Aged care needs are greatest among those aged 80 and beyond. In 2013, this group accounted for one in every 26 Australians. By 2030, one in every 18 of us will be over 80.

However, this will be a slow burn. The peak years for baby boomers to enter nursing homes won't start until the late 2020s, and the youngest of them will follow throughout the 2030s.

Just as the baby boomers changed the nature of Australia's schools in the 1950s and 60s, and then our workforce in the decades that followed, they will create a wave of change through the aged care sector.

Nursing homes will undergo a transformation as wealthier boomers (and their children) look to maintain the kind of lifestyle they have enjoyed in the past. This might include private room ensuite facilities, secure gardens, personally tailored services and – provided we can field the skilled professionals needed to meet the demands of these new retirees – highly competent care staff.

The ageing demographic of the Australian population will drive a steady rise in the number of 'frail aged' in nursing homes over the coming decades, suggesting that investment in sectors designed to care for the aged may generate increasing opportunities in the decades to come.

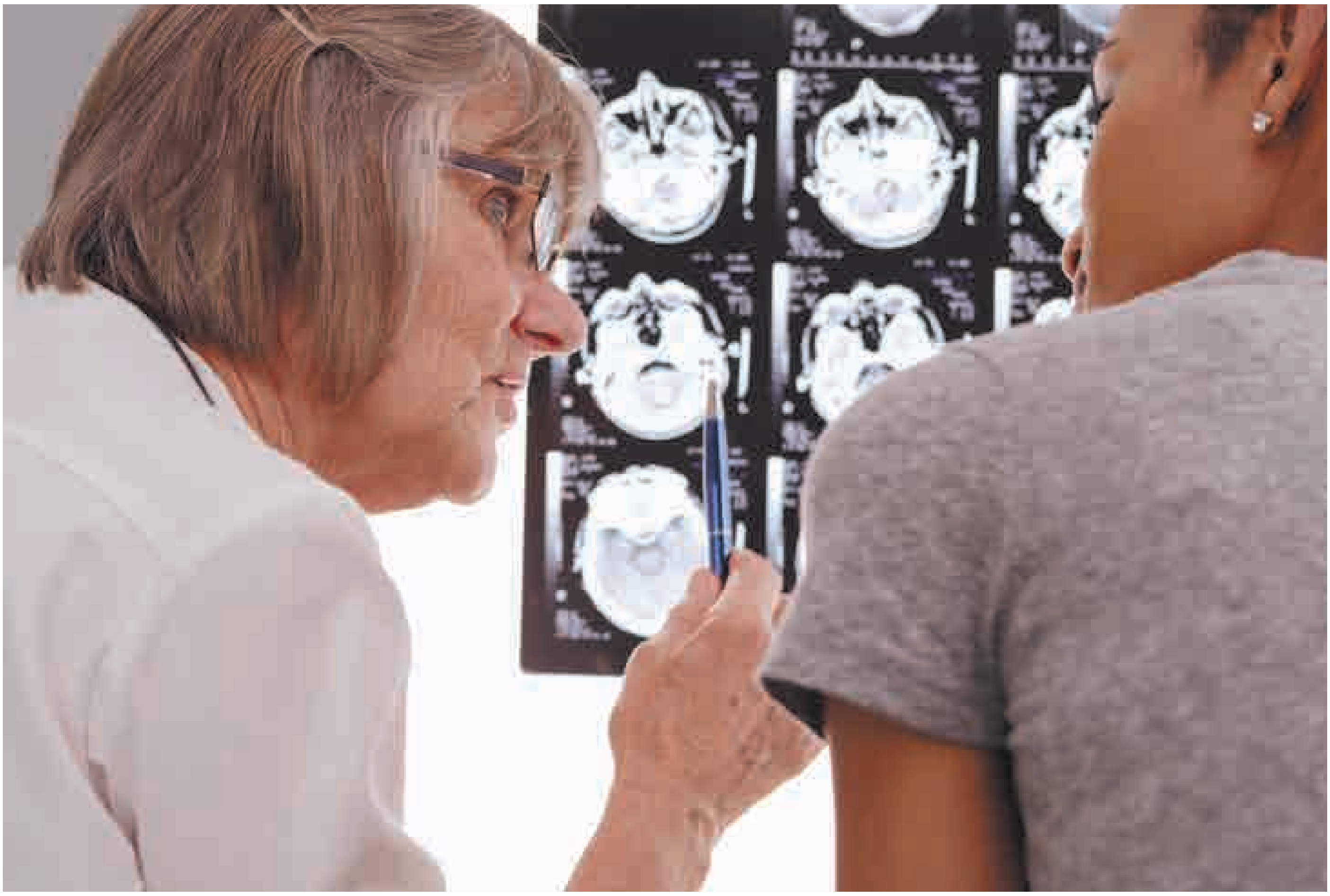
Indeed, recent moves into this sector by major investment banks hint that some sections of the market have already identified aged care as a growth industry of the future.

But there is another important trend here which is tailor-made for smaller businesses – the impact of providing more aged care services to elderly Australians in their own home.

Currently, such services are relatively rare outside government-sponsored programs, but can confidently be expected to grow, along with the pool of potential customers.

Indeed, the needs of older Australians extend well beyond the health sector itself. Older homeowners will need an array of assistance from gardening to cleaning and food preparation that will mean opportunities exist for small businesses who never thought of themselves as offering care for the elderly.

There are various intermediate choices between ageing in your own home and



moving to a retirement home as well, and these are developing rapidly. For example, more and more people will choose a 'retirement village' style residential development or an 'assisted living' community for their later years.

These trends are a reminder that the overall size of the sector is growing more rapidly than government funding – something that can be expected not only to continue but to accelerate over coming years.

These changing patterns of consumer preference over coming decades will obviously have implications beyond the health and health-related sectors of the economy.

Lifestyle choices of older Australians will drive Australian infrastructure requirements to include different types of residential construction more preferable to an older population. Similarly, there may be changes in transport requirements as a larger proportion of the population is unable to use a vehicle, or may require modifications to vehicles to assist with driving.

There's considerable potential in related markets too

Yet, there are still more areas of potential. In 2014, Deloitte identified the 25 sectors that it saw as having the greatest growth potential in Australia in the next two decades.

Five of those 25 are highly relevant here:

- Community and personal care;
- Retirement living and leisure;
- Residential aged care;
- Preventative health and wellness; and
- Digital delivery of health.

While we've covered residential aged care, these others are also worthy of a closer look.

Community and personal care

Australians are living busier lives, meaning the future for time-saving services is particularly bright. This includes a range of businesses, from those focused on helping out around the home (for example, Jim's Mowing, Dial-An-Angel, Hire A Hubby) all the way through to dog walkers and personal shoppers.

Higher living standards have seen Australians demanding greater access to a wider range of health care over time.

Adding to those opportunities will be growing demand from older Australians, who will want convenient access to a range of health and other services – both within retirement communities, and for meeting specialised needs within the broader community (such as culturally appropriate care for ethnically diverse Australians).

While public funding is increasingly moving to a consumer-led model, an increasing number of older Australians will be looking for more flexible and responsive services than fit into existing funding buckets. That will see some of the best opportunities arising for businesses who consider themselves outside the community care sector today.

The private provision of personal care in the home is an area that will therefore grow rapidly, as pressures grow on public health care and as relatively affluent retirees look to make life more comfortable by making arrangements to stay in their own homes.

Retirement living and leisure

There's big spending ahead by older Australians – and many years of that spending before that cohort will be entering aged care at home or in a residence.

But will older Australians have the funds? Compulsory superannuation is only two decades old, so the superannuation system is decades shy of maturity. Because of that we tend to assume that the retirees of the next two decades won't be particularly well-heeled.

Yet that's just plain wrong. Although the superannuation assets of retirees haven't benefitted from a lifetime of contributions, the baby boomers did own housing and shares – both of which have appreciated handsomely over the longer term. Similarly, policy changes in the past decade have consistently favoured older Australians.

The upshot is that, although there will be a wide range of experiences, those who retire in the next two decades will, on average, have funds available on a scale never seen before in Australia – or indeed elsewhere. At the same time, the coming wave of retirements among baby boomers will be large, and will come with more ambitious expectations of their retirement years than previous generations.

That will revolutionise a number of markets. One of the most obvious is retirement living, where increasing luxury will be likely compared with current operations in 'retirement living and leisure' – numbers of residents and customers will grow, but so too will the quality of the facilities and services on offer.

Health and wellness

No market is likely to see better growth in Australia over the next two decades than health and wellness services. We're living longer, but we also want to keep living better, and that combination will generate billions of dollars in opportunities.

As the saying goes, prevention is better than cure. Given what we now know about the risk factors that lead to health problems such as heart attacks and strokes, prevention is also where many of the opportunities lie. Broadly speaking, preventive health care is aimed at, on the one hand, addressing risk factors such as smoking, weight and cholesterol and, on the other hand, intervening early and effectively to help Australians with acute and chronic conditions avoid complications. For example, helping those with osteoporosis prevent fractures.

Businesses that help Australians combat the 'lifestyle factors' of obesity and inactivity are part of the answer here. And that doesn't mean just the physical activity and weight loss industries – both the time-poor and the elderly will increasingly rely on the private sector to supply nutritious meals and appropriate exercise and fitness regimes.

Businesses providing complementary medicines and treatments aimed at avoiding and relieving the symptoms of disease also fit within the sphere of preventive health and helping older people live active, healthy lives. For example, vitamins and supplements, naturopaths, acupuncturists, remedial massage, yoga, tai chi and pilates.

There are also major opportunities here for more traditional health providers. Biotechnology, pharmaceutical and medical device companies are working hard to find new and better treatments for chronic conditions such as arthritis and Alzheimer's disease. Pathology and imaging centres will continue to grow diagnostic services. Allied health professionals from a range of fields – such as nursing, optometry, dentistry, pharmacy, psychology, physiotherapy and occupational therapy – will find themselves in high demand.

The need for general practitioners, specialist medical services, hospital inpatient and outpatient treatment, day surgery, and other acute, sub-acute and primary care services will also rise fast. Medi-hotels, hospital-in-the-home services, and innovative e-health and telehealth offerings will proliferate in pursuit of more cost-effective delivery of healthy life years.

While Australia's high wages are unlikely to make us a huge magnet for medical tourism in our region, there will also be pockets of opportunities for health exports in niches such as fertility treatment, bariatric surgery, dermatology, cosmetic surgery and cardiac therapy.

Those businesses that can focus on the rapidly growing health sub-markets across the nation, and particularly among older Australians, will be well placed.

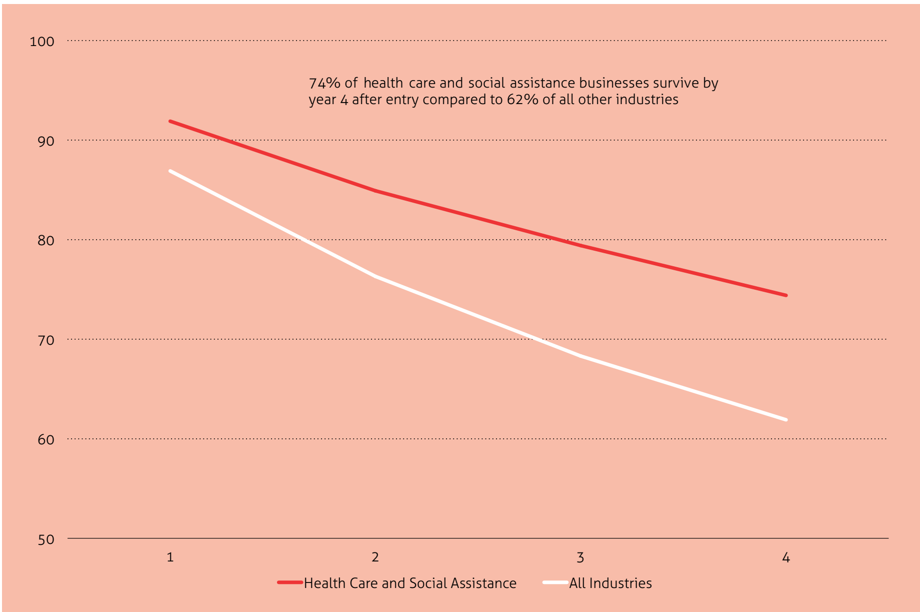
Digital delivery of health

Like many things, the delivery of health services is going digital and Australia – with our need to serve a small population over vast distances; with our excellent track record in manufacturing medical devices; and with our willingness to try new health care delivery models and sophisticated telecommunications infrastructure – is well placed to pioneer next-generation products and solutions.

And South Australia has both opportunity and motive when it comes to developing these new technologies. With relatively strong medical manufacturing and pharmaceutical businesses, and dispersed rural and regional populations, South Australia has much to gain from greater digital delivery in health.

Australia's geography has already made us something of an expert in delivering things to

CHART 7
SURVIVAL OF AUSTRALIAN HEALTH BUSINESSES COMPARED TO ALL OTHER INDUSTRIES



Source: Australian Bureau of Statistics our highly dispersed population. In particular, Australia has developed a competitive advantage in health transport services (i.e. the Royal Flying Doctor Service), tele-triaging (call centres that assess what assistance is necessary and how to access it), and a range of other telehealth services including:

- Tele-consultations – such as psychiatry and other specialities;
- Tele-radiology – imaging that is acquired locally but processed in cities; and
- Remote patient monitoring – using set-top boxes with other devices to provide biometric measurements and monitoring of conditions such as diabetes, cardiovascular disease and chronic obstructive pulmonary disease.

Australia has also developed expertise in identifying and implementing alternative models of care that reduce costs and improve quality of life for people in remote regions. A good example is providing oral (rather than intravenous) cancer therapies that allow patients to stay in their home towns or on remote properties during treatment.

In terms of devices, many have heard of the products produced by companies such as Australian bionic ear maker Cochlear and sleep device leader ResMed. But they aren't our only success stories. There is a vibrant and viable medical devices industry beyond those two well-established success stories, dominated by organisations that are still in their start-up phase and employing less than 100 people.

The drive to digitally enable medical devices, so that patient data is regularly updated in the cloud, paves the way for a massive revolution in the remote provision of health services. The growth of these new business models highlights that Australia has a great opportunity to excel in the research and development, advanced design, engineering and manufacturing of web-enabled medical devices.

These opportunities should only be enhanced by the further expansion of our telecommunications capacity with the NBN and ever-growing mobile networks.

While we still have plenty to get right at home – for instance, life expectancy in regional and remote areas of Australia is still four years lower than in metropolitan Australia, and the gap for Indigenous Australians in communities is even greater – there will also be an opportunity to export our expertise, technologies and treatment models to the island archipelagos of the South Pacific and the South East Asian region, as well as western China, south Asia and much of Africa.

Like Australia, many countries in those regions suffer from poor economies of scale, the complexities of aligning health needs with workforces that prefer to live in cities, and a broad spectrum of tropical illnesses, injuries and conditions that can be complex to manage without local or specialised facilities.

The health sector is one of the most stable in Australia

Rapid growth in business is usually accompanied by volatility, with risk rising alongside returns.

Yet the health sector can claim both good growth prospects and a lack of volatility. Official government data from the Australian Bureau of Statistics shows that the Health Care and Social Assistance sector had the lowest business exit rate in 2014-15 of all industries.

In fact, health care and social assistance businesses were the most likely to survive from June 2011 to June 2015.

The expanding health sector means there are many opportunities for businesses in the years ahead. Indeed, there are already many examples of where Australian companies have taken on the world and won.

Similarly, Chart 7 is a reminder that, not merely is this a 'steady sector' – a relative safe harbour in which to ride out the rollercoaster of the business cycle – but it is also one which has accounted for a steadily increasing share of the national economy over time.

The one downturn where health was more affected than average was seen across 2002 and 2003 when the pharmaceutical sector (whose share index dropped by nearly two-thirds) was engulfed in a global crisis of confidence as a run of solid drug development came to an end. However, despite the global falls in pharmaceutical and other health-related equities at the time, profitability in general remained solid.

The last word

The future is bright for South Australia's largest employer.

Australia is ageing, and the cost of health care rises faster than costs on average in the economy. That indicates that health will become an even bigger business in the future than it is today.

And some have even gone as far as to suggest that businesses in this state will benefit from a developing 'growth cluster' of health-related businesses on the back of megatrends such as rising life expectancies, rising relative health care costs and tightening public sector health budgets.

South Australia's energy security

In energy markets, all eyes across Australia have been on the dollars being generated by the big electricity asset sales process underway in New South Wales.

But there are some other important developments afoot, and South Australia has been central to a few of them.

Most notably, energy security is becoming a hot topic, with both South Australia and Tasmania experiencing energy reliability and security concerns over the past six to nine months.

Troubles in Tassie?

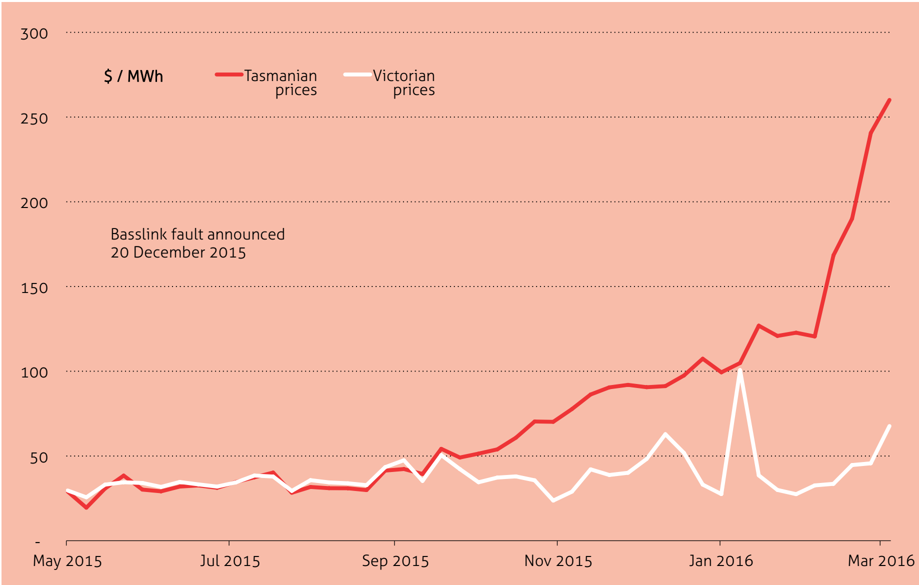
As the energy system moves towards a lower emissions fuel mix, regions within our National Electricity Market are becoming increasingly reliant on connections between one another.

Take Tasmania as an example. Gas generation was decommissioned in 2013 as the combination of hydro and imported electricity from Victoria via the Basslink cable was expected to be sufficient for that state's energy needs.

Yet a recent fault in the Basslink cable and low water reserves have highlighted the potential sensitivity of electricity prices to unexpected events.

As a result, and as Chart 1 shows, Tasmania's electricity wholesale prices have jumped and large customers have had to make sacrifices by reducing their consumption, placing even more pressure on a Tasmanian economy that is facing some pressures.

CHART 1
TASMANIAN WHOLESALE ELECTRICITY PRICES



Source: Australian Energy Market Operator, 2016

South Australia is a global leader in wind and solar renewables

South Australia is another example of the challenges arising as Australia's energy system moves to a lower carbon future.

In brief, South Australia stands out from the pack – both globally and within Australia. Yes, some countries and some states have more renewable energy than our state does – think Iceland and Tasmania. But it is worth noting that those regions have a reliance on hydropower and geothermal electricity supplies in a way that South Australia does not.

Why is that important? Because hydropower and geothermal (and nuclear) electricity supplies can be relatively readily turned on or off.

That is, admittedly, a simplification. Nuclear and coal are somewhat less flexible, while gas and hydro are more flexible. Plant of any type is subject to the occasional unexpected outage, but electricity systems are set up so that whether via price signals in a market, or simply by direction, other plants of this type can ramp up their output or switch on to fill the gap.

South Australia's renewable resources are in the form of wind and the sun. In fact, it is no exaggeration to describe our state as a global leader in wind and solar renewables.

That is to be applauded. Yet, like most things, there are both costs and benefits of any form of investment. Electricity supplies such as wind and solar are 'intermittent' – they are only available when the wind is blowing or the sun is shining. There are other regions around the world that have more intermittent renewables than our state (for example, Denmark and Iowa).

Yet most such regions with a relatively larger reliance on 'intermittent' energy sources also have stronger interconnections with neighbouring regions, which in turn makes it easier to import or export electricity at times of demand peaks and troughs.

By way of contrast, South Australia's interconnection with Victoria is equivalent to only about 23% of the state's peak demand.

Other things equal, that says South Australia runs some of the risks around electricity supplies and prices that have recently been evident in Tasmania.

In effect, the state's energy security may prove to be at risk of vulnerability as greater variable renewable energy, combined with mothballing of traditional generation capacity, place strain on the state's electricity infrastructure.

In early 2016, the Australian Energy Market Operator responsible for ensuring reliable electricity supply on Australia's east coast, found that South Australia's significant renewable electricity has increased instability in the system and would require investment in infrastructure to mitigate the risk of blackouts.

There's much to applaud

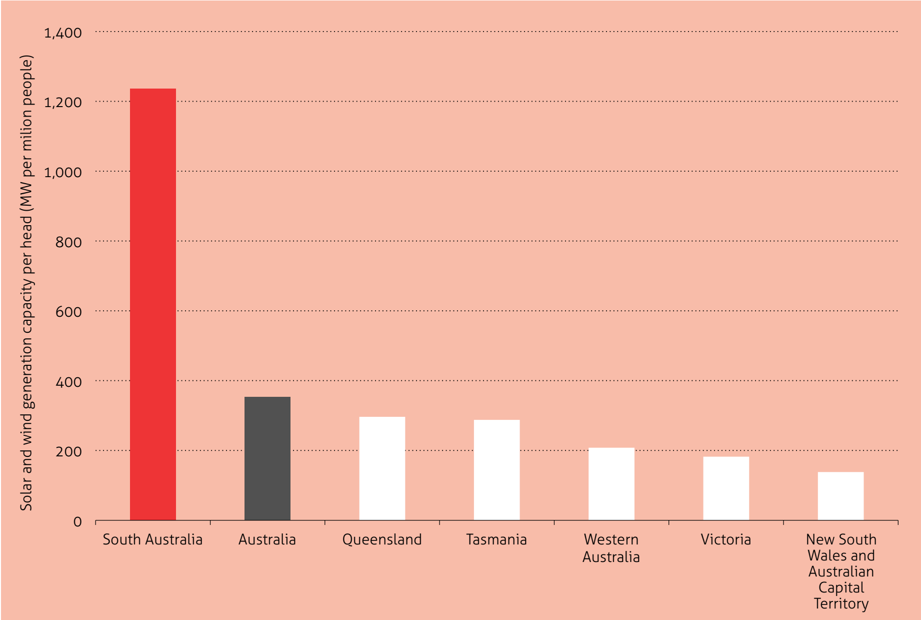
To be clear, solar and wind generation are very low marginal cost and have pushed wholesale prices down at certain times of the day – increasing competitive pressure on traditional large generators.

That is mostly to the benefit of ordinary South Australians and the prices we pay in the short term.

However, these large generators also provide the electricity system with stabilising effects which, when removed, may increase the challenge of reliability and the risk of blackouts.

That means there is a risk that electricity users in this state may face future shortages in supply at a time when the electricity network is adapting to a more variable mix of electricity generation to cater for an energy system which has a growing renewable proportion.

CHART 2
SOLAR AND WIND GENERATION CAPACITY PER HEAD (BY STATE)



Source: Energy Supply Association Of Australia

In response, we can improve our energy connections to the rest of Australia, and we have the potential to keep juggling the mix of energy supplies available within South Australia.

But it may be one area that is worth watching closely. Our success in solar and wind power is world class – and something for this state to be proud of. Yet it may also have come at the risk of increased pressure on the state's energy security.

Australia's economy: proud performance amid continuing challenges

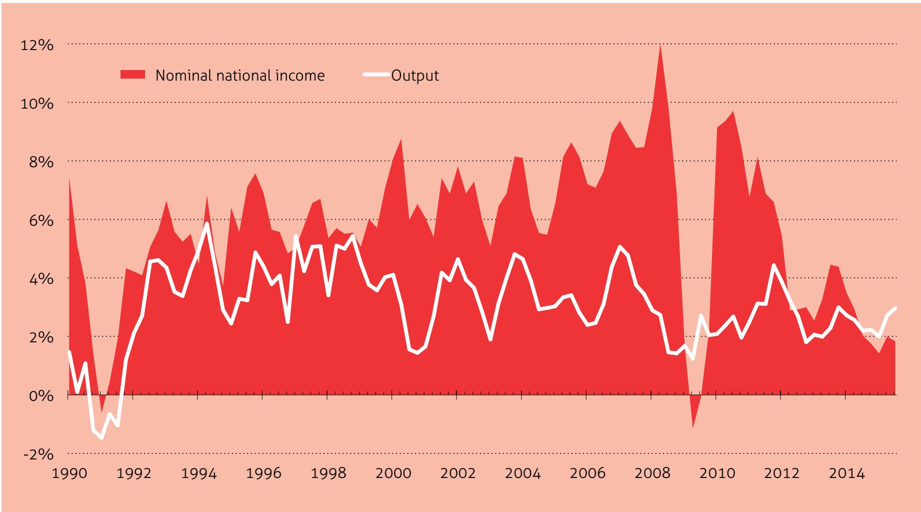
There's plenty to like about a number of recent trends in Australia's economy. In particular, output growth has lifted (as seen in Chart 1) and employment gains are solid, while commodity prices have started drifting up again and China is still growing at a decent rate. In fact, China's growth has been good enough to generate a big increase in tourist flows into Australia.

All in all, that's a pretty good outcome given the sheer size of the resources boom over the past decade – booms usually end more dismally than this.

Yet the challenges haven't gone away:

- Global growth remains under pressure, and China's construction cycle is still likely to get worse before it gets better.
- Although there's been a recent recovery in commodity markets, it is hard to see excess capacity in those markets being soaked up in the next two years – meaning that some of the pressure on Australia's national income growth (also seen in Chart 1) isn't going to disappear any time soon.
- Even if commodity prices do continue to improve, chances are that they will still be sufficiently low to render investing in new minerals and energy capacity uneconomic. Indeed, the capital expenditure intentions in the latest survey by the Australian Bureau of Statistics remain weak for 2016-17. If that turns out to be the case, it would intensify the short term pressures on the Australian economy.
- Moreover, the Australian dollar has risen alongside commodity prices (aided by a move to negative interest rates by the Bank of Japan and other central banks). That doesn't help the Australian business outlook at a time when a weaker currency would have been helpful.
- Finally, neither housing prices nor the pace of housing construction may be quite as positive for the Australian economy over the next few years as they were over the last few years.

CHART 1
NATIONAL OUTPUT AND INCOME GROWTH



Source: Australian Bureau of Statistics

In other words, the outlook is evenly poised as the balance between positives and negatives remains intact. And because both the negatives and the positives for Australia involve some pretty substantial economic forces, it's no surprise that the outlook is uncertain and that current economic indicators reveal divergent trends.

Consider, for example, the apparent contradiction between excellent employment growth and a Federal Budget that remains under considerable pressure. Yet this isn't as unusual as we might otherwise think – Chart 1 shows solid output growth, which is driving recent employment gains. But it also shows sluggish national income growth, and it is our incomes that are the key driver of the Federal Budget's tax take.

One very important trend within the Australian economy is the size of the continuing fall in business investment spending. Although this is happening in many nations around the world at present (with most of the globe looking to consumption rather than investment as the driver of growth), Australia is experiencing this to a much greater degree than elsewhere.

Businesses operating in Australia invested heavily in new capacity over the past decade – not only the mining sector on account of higher commodity prices, but most other sectors too – as incomes improved more broadly.

But that cycle has turned and China's subsequent slowdown has hit Australia hard, because construction in China has slowed more than its other sectors. It was the Chinese construction sector which was demanding vast quantities of steel and hence Australia's coal and iron ore.

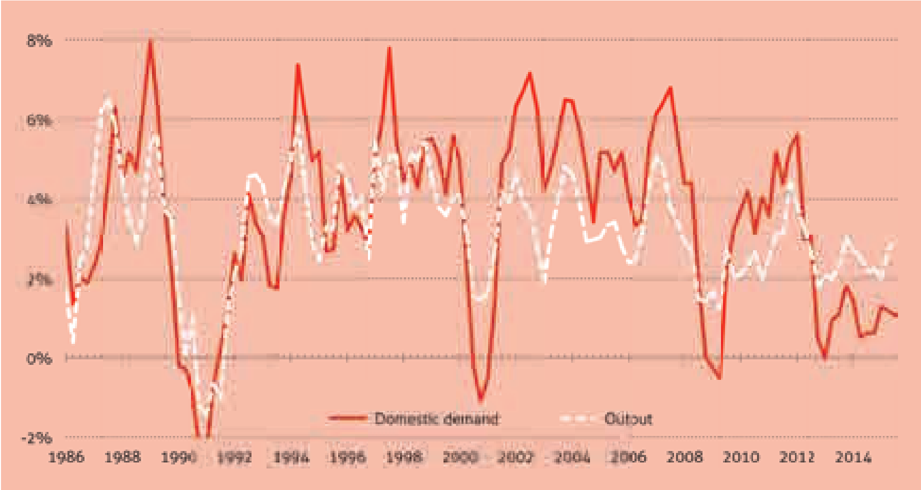
The slowdown in China has coincided with a large increase in the supply of industrial commodities in much of the world. Miners aren't merely digging deeper here in Australia, but also in the rest of the world's major minerals provinces. That suggests that not even the recent modest recovery in commodity prices is going to tempt much extra business investment in the near term.

"China's subsequent slowdown has hit Australia hard, because construction in China has slowed more than its other sectors. It was the Chinese construction sector which was demanding vast quantities of steel and hence Australia's coal and iron ore."

That's why Chart 2 shows a continuing and wide divergence between the pace of growth in Australian output versus the pace of growth in Australian spending. The slowdown in investment – in particular, continuing large falls in spending on huge resource-related construction projects – means that the growth in domestic demand is likely to remain subdued for some time.

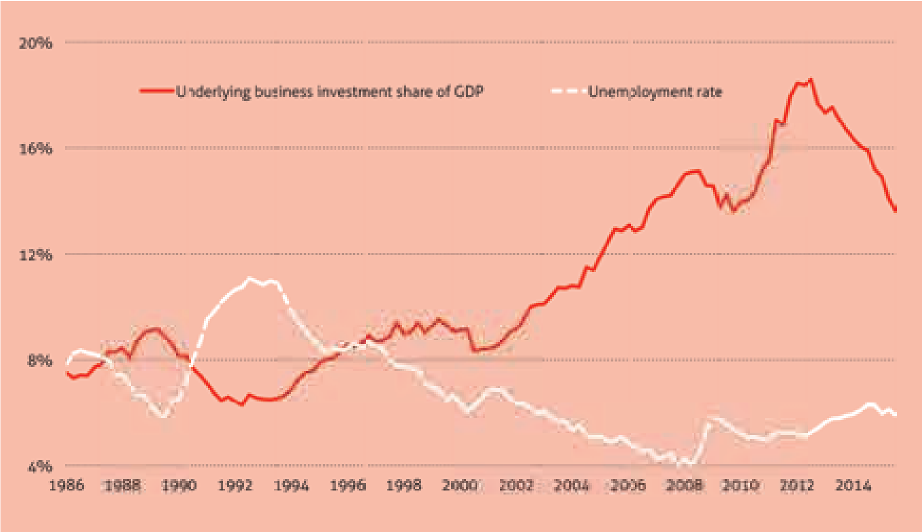
More specifically, Chart 3 shows the sheer scale

CHART 2
NATIONAL OUTPUT AND DOMESTIC SPENDING GROWTH



Source: Australian Bureau of Statistics

CHART 3
BUSINESS INVESTMENT AND UNEMPLOYMENT



Source: Australian Bureau of Statistics

of the mining-led investment boom, and the subsequent slowdown as businesses operating in Australia return towards longer term trends in their capex.

It's hard to take a hit of this size without the wider economy feeling some of the pain. Indeed, that is exactly what has been happening. Although the Australian economy has continued to show an enviable record of growth and achievement – even as we enter the fifth year of one of the greatest commodity price downswings the world has ever seen – there's known pain ahead on the business investment front.

All things considered, that isn't such a bad business backdrop. In fact, it is a pretty good outcome at the tail end of a massive resources boom. And it is a performance that, quite rightly, should make Australians proud: our growth has been solid and unemployment remains pretty low at the tail end of a big boom. That isn't what either history or economics might have predicted.

Equally, however, it isn't a set of circumstances that's pointing to a return to strong growth – Australia's economy isn't out of the woods yet, and we won't be until China's economy reaches firmer footing and commodity prices do the same.

$6 billion

THE ANNUAL VALUE OF RURAL OUTPUT IN SOUTH AUSTRALIA

25%

THE GROWTH OF TOMATO PRICES IN SOUTH AUSTRALIA OVER THE PAST YEAR

BankSA Rural Price Index

Dollar bounce bad news for SA farmers

The BankSA *Rural Price Index* informs the state's farmers and farm industries how prices are faring for South Australia's farm products, rather than merely how prices are faring across Australia as a whole. The index aggregates price movements across 17 products which make up more than 80% of South Australia's farm output.

There are three groups of products – grains (such as wheat and barley), livestock and related products (dominated by wool, milk and beef), and horticulture (dominated by grapes).

The index shows prices in Australian dollars (thereby reflecting the prices received by South Australian farmers), as well as in terms of the prices paid by foreign buyers (that is, prices in foreign currency).

Australian dollar pain returns

After a period of reprieve, the recent bounce in the Australian dollar is once again turning the macroeconomic levers against South Australian farmers. All else equal, a lower Australian dollar makes South Australian farm products more competitive in global export markets, but the recent appreciation in the nation's currency has clawed back some competitiveness from South Australia's rural producers.

Looking back for a moment, the first decade of this century was a tough time for farmers who found themselves caught up in the backwash of the global industrial commodity boom. While this period pushed up world commodity prices of all stripes – including agricultural commodities – the big price benefits were for the likes of coal and iron ore rather than wheat, beef and grapes. And that same boom also saw the value of the Australian dollar soar. As demonstrated in Chart R1, that combination drove a large wedge between the prices received by local farmers (the line in Australian dollar terms) and those paid by foreign buyers (the two other lines), a gap which peaked in around 2011.

However, the profits that could be made in the likes of the coal and iron ore markets inevitably led to large increases in capacity. And with the added help of a slowing Chinese economy, the investment boom of a lifetime came to an abrupt end, and with it brought prices back to earth. While prices on world markets fell, the fall in the Australian dollar was actually larger. That not only meant local competitiveness increased, but the prices received locally actually rose even as world prices fell.

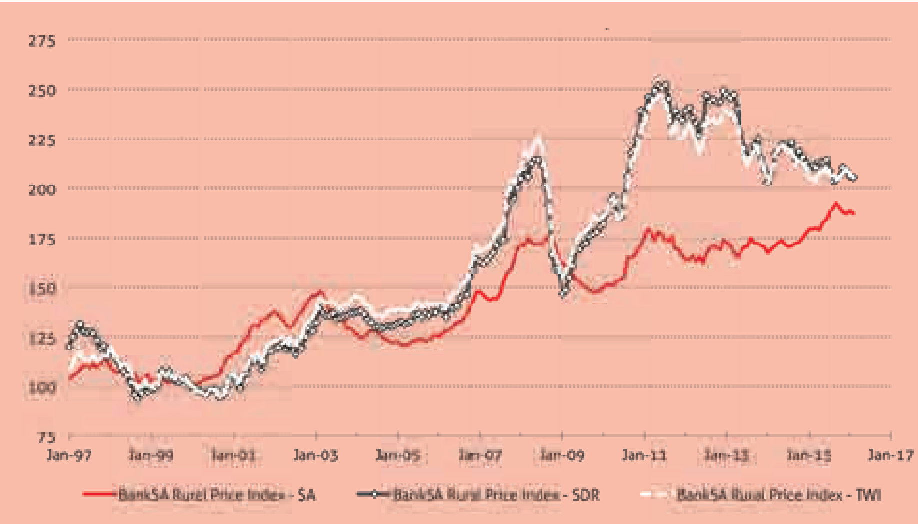
Chart R1 shows that these developments have meant a slow downturn in world prices for farm products. However, they also meant a large fall in the Australian dollar, so South Australian farmers have actually been better off even though world prices have been falling.

While many world prices for farm products are still on the back foot, recent months saw the Australian dollar regain some altitude – since mid-2015 local prices have begun to

BankSA Rural Price Index

Index base : January 2000 = 100	Level	February 2016 % change since Aug 2015	Feb 2015	Feb 2014
AUSTRALIAN DOLLAR INDEX				
Grains	191.0	-3.5%	-3.3%	-0.9%
Livestock and Livestock Product	215.3	-1.1%	+11.3%	+24.3%
Livestock Only	219.7	-1.9%	+10.5%	+26.2%
Horticulture	115.4	+5.4%	+2.2%	+1.3%
TOTAL ($A Based)	**187.5**	**-1.3%**	**+4.5%**	**+10.6%**
SDR INDEX				
Grains	209.4	-1.5%	-9.9%	-11.1%
Livestock and Livestock Product	236.1	+0.9%	+3.6%	+11.5%
Horticulture	126.6	+7.6%	-4.8%	-9.1%
TOTAL (SDR Based)	**205.5**	**+0.8%**	**-2.7%**	**-0.9%**
TOTAL (TWI Based)	**205.6**	**-0.4%**	**+0.1%**	**-1.5%**

CHART R1
BANKSA RURAL PRICE INDEX – JANUARY 2000 = 100



ease for the first time since around 2012.

Other things equal, that bounce in the Australian dollar means pain for this state's farmers, who'll need to keep a close eye on currency trends.

Differing performances across categories

The performance across rural commodities is not consistent (see Chart R2). While crops and grains prices have plateaued since around 2013, livestock and livestock product producers have been paid a premium, and horticultural product prices have declined.

Farm commodities, particularly crops and grains, are sensitive to weather conditions with drought periods often causing prices to spike. These markets are also truly global – thanks to the relative ease of transporting these goods between markets – with developments in locations as varied as Canada, Ukraine and Australia all capable of moving world prices. It's no surprise then that crops and grains prices can be most volatile.

The recent fall in crops and grains prices has been helped along by a bumper couple of years for wheat production, with international production up and domestic production being pulled along by a number of good years for Western Australian and New South Wales wheat producers. The latter has also contributed to growing global stockpiles that are projected to exceed 600 million tonnes this year.

Early official forecasts are for stocks to remain high despite a decline in wheat production from a record 733 million tonnes in 2015 to 723 million over the course of 2016. According to the Australian Government's official farm forecaster, ABARES, average farm cash income for grain industry farms fell slightly in 2014-15, although they remain solid by recent standards.

The steam has also been taken out of livestock prices after an extended period of solid price growth that began in early 2013.

While that upswing was the result of a number of factors, a key trend has been Australia's stellar job of promoting domestic livestock products to the growing international food industry. Award winning restaurants across the world are now offering Australian beef and lamb as high-end luxury products and, as a result, Australian producers have been able to charge top dollar.

Growing demand has also helped as global livestock and livestock product producers struggle to keep pace with a fast growing appetite for high quality meat products across Asia and the Middle East.

Average prices received by South Australian livestock farmers are up by more than a quarter over the past two years. Yet prices are actually down since mid-2015. Beef prices, which were the largest longer term beneficiary of the growing global market, have been a victim of the Australian dollar bounce. Lamb and pork prices tell a similar story, with the particularly strong growth seen last year stymied in recent months.

"The steam has also been taken out of livestock prices after an extended period of solid price growth that began in early 2013."

Livestock products have fared slightly better so far in 2016, with wool prices adding to strong gains over the course of 2015.

CHART R2
COMPONENTS OF THE BANKSA RURAL PRICE INDEX

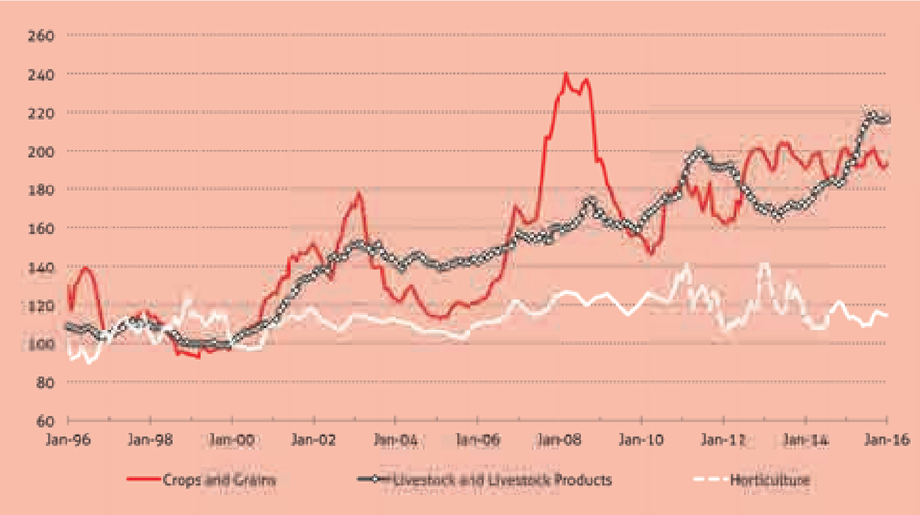
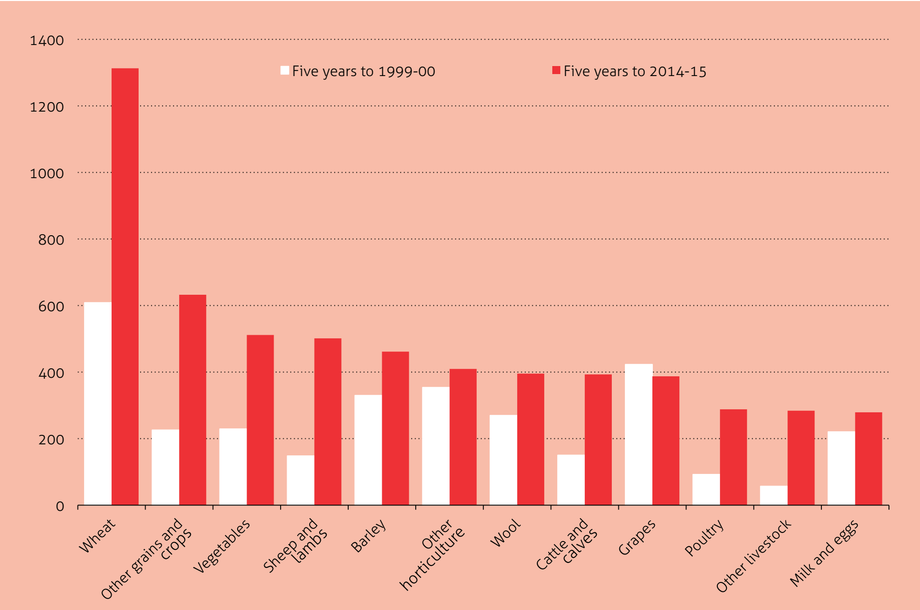


CHART R3
VALUE OF RURAL PRODUCTION BY COMMODITY



However, lower milk prices and higher fodder costs are beginning to eat into dairy farmers' profits.

Finally, horticulture products – the smallest component of the index that includes grapes (for wine) as well as the usual array of fruits and vegetables found on your local supermarket shelves – has remained steady (given South Australia is not subject to the always extremely volatile price of bananas). Prices for South Australian horticulture products have remained relatively unchanged; potato prices have been very stable of late with similar trends evident for carrots, onions, strawberries, apples and oranges. Tomato prices are an outlier, with prices up by around 25% over the last year.

Wine grape prices – the largest horticultural crop in South Australia – have also been stable in recent years. However, a global wine glut and several years of above average production from South Australia's growing number of wineries is sobering news for future prospects.

Longer term changes and regional trends

Chart R3 shows the value of rural output in South Australia across the past 15 years – a period across which production has doubled to over $6 billion per year. High production values for lamb, pork, beef and veal are driving an increase in the value of livestock, while higher wool prices are pushing up the value of livestock products, despite lower milk prices at the farm gate.

The 2015-16 winter cropping season was a good one, although better for New South Wales and Western Australia than for South Australia. While recent rainfall in South Australia has been above average, particularly in the Yorke and Lower Eyre Peninsulas, this is a small reprieve from an extended period of rainfall deficiencies in large parts of the state, and future rainfall remains a key risk to the outlook. Chart R3 shows how much is at stake, with around a quarter of the state's rural revenues coming from a single crop – wheat – and the broader grains industry worth close to $2.5 billion per year.

This will impact certain areas of the state more than others. South Australia's rural production (shown in Chart R4) is varied in its composition across the state's regions.

> **"Crops and grains tell a very different story, with prices flat but growing volumes pushing up the value of South Australian crop receipts."**

The most famous part of the state's agricultural base – the Murray Darling Basin region – is also the most diverse and the most productive. It accounted for just under a third of the state's farm output in 2014-15. This rich region produces over two-thirds of South Australia's wine grape crop, over half of all horticulture crops, and it is home to around a quarter of the state's livestock.

The adjacent South East region is relatively more focused on livestock products – notably wool and milk – which alone account for over 75% of its rural production. The region is also important for its onion and potato production and the state's main source of citrus and stone fruit. The South East also provides all

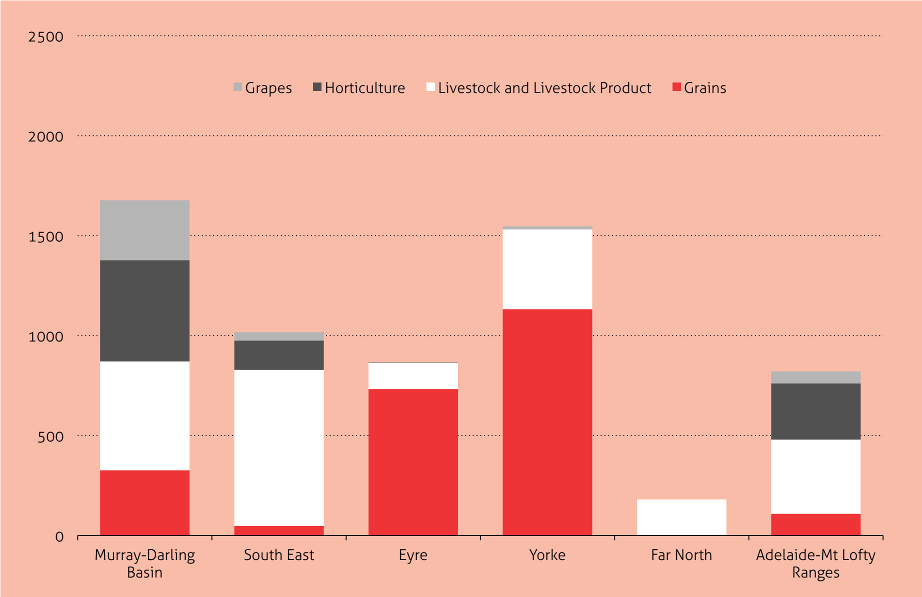
of South Australia's almond production, an industry that has grown by a factor of eight across the past two decades.

The drier weather conditions to be found in the mid-north of the state – the Yorke and Eyre Peninsula regions – favour wheat and grain crops over thirstier horticulture crops. The remaining source of farm income tends to be sheep – both for meat and wool – although the Yorke Peninsula region is also the state's key source of poultry meat. Rural activity in the massive Far North region (covering over 80% of the state) is even less diverse – characterised by some of the world's largest cattle stations, as the arid conditions limit production of other rural commodities.

"Finally, while it might not spring directly to mind, the region around Adelaide is still a key contributor to South Australia's rural production."

Finally, while it might not spring directly to mind, the region around Adelaide is still a key contributor to South Australia's rural production. Indeed, more than one in every $10 of rural output is generated in this area.

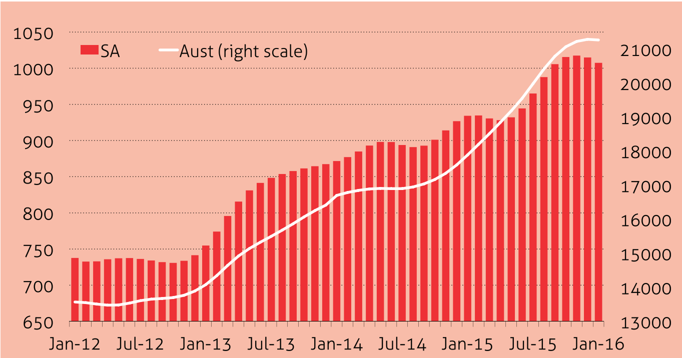
CHART R3
VALUE OF RURAL PRODUCTION BY COMMODITY



The region is the main producer of egg and apple output (each worth over $50 million a year), as well as almost all of the production in a number of fruit and vegetable crops, as well as flower production. While less of an issue at present in South Australia, the long term expansion of major capital cities (such as Sydney and Melbourne) is beginning to impinge on these types of producers, leading to conflicts between competing land use priorities.

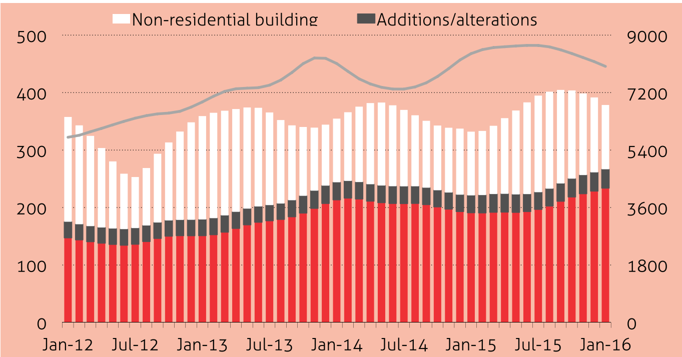
Statistics

CHART 1
SECURED HOUSING FINANCE COMMITMENTS - TREND ($M)



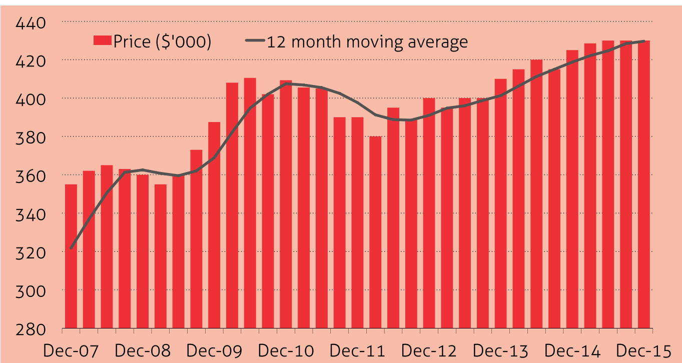
South Australia had been failing to keep pace with the national recovery in housing construction, but a spurt in late 2015 helped to restore relativities with national performance. That said, and at both the national and state levels, the recent leap in secured housing finance commitments appears to be finally losing steam.

CHART 2
BUILDING APPROVALS - TREND ($M)



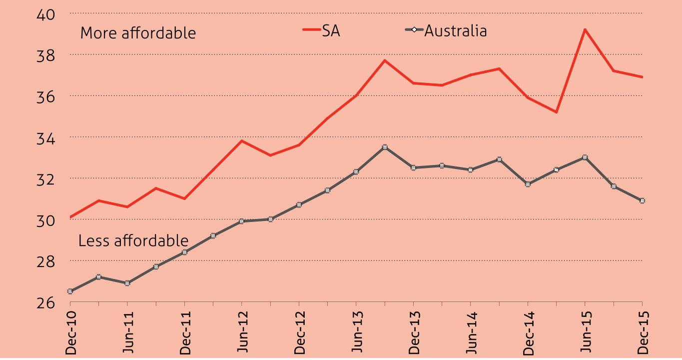
A similar picture is evident in building approvals, where South Australia achieved a second wind in recent times, with a rising trend in residential building approvals offsetting something of a softening in commercial construction approvals in the state. That variation in activity across different elements of the construction sector has the potential to work in the state's favour, though the recent net downtrend across the combined total bears monitoring.

CHART 3
MEDIAN PRICE OF HOUSES SOLD ($'000)



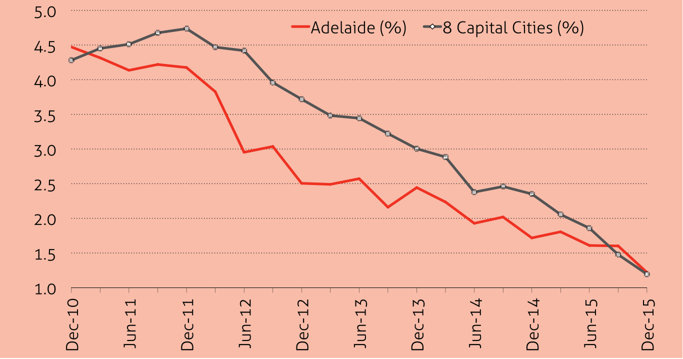
Australia has seen a rapid increase in median housing prices in recent times, and trend values in Adelaide have certainly risen substantially since mid-2012. However, two things stand out. First, although housing prices in Adelaide have moved up, the extent of those gains pale alongside the matching increases in Sydney in particular. That observation holds true in percentage terms and even truer in absolute dollar terms. Second, and as is increasingly evident across a range of capital city markets, there is some indication that Adelaide housing prices have recently levelled off following four years of solid gains.

CHART 4
HOME LOAN AFFORDABILITY - INDICATOR STATISTIC



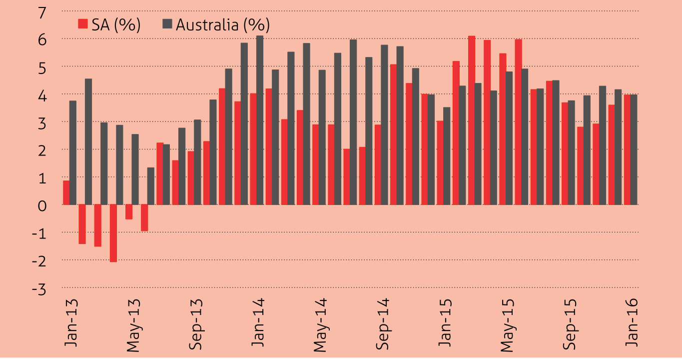
Home loan affordability in South Australia has been notably better than that in the nation as a whole for many years. But whereas home loan affordability in this state is holding relatively steady at high levels, the fastest price increases evident in some other states have seen national affordability drop back to levels last seen in early 2013.

CHART 5
INDEX OF DWELLING RENTS - % CHANGE ON PREVIOUS YEAR



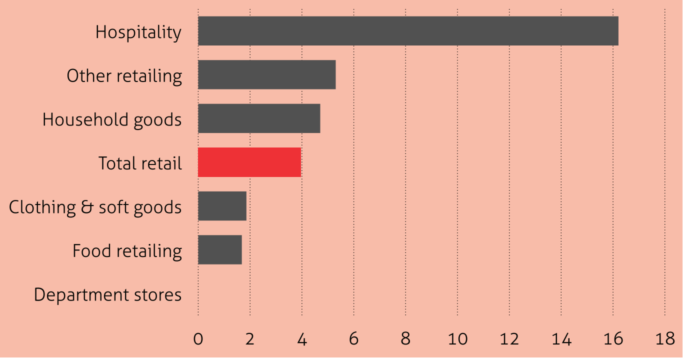
With investors having been enthusiastic participants in the purchasing of homes and apartments in recent years, the supply of available rental homes has increased. Add in moderating overall inflation trends, and it's no surprise that – in both Adelaide and in Australia as a whole – the overall pace of increase in housing rents has been moderating for a number of years now.

CHART 6
RETAIL TRADE - % CHANGE OVER PREVIOUS YEAR - SEASONALLY ADJUSTED SERIES



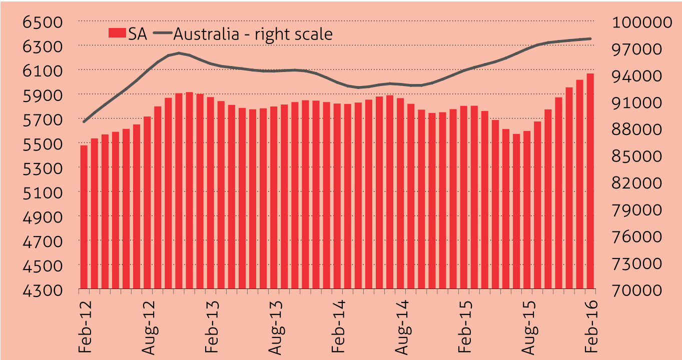
Retail sales in South Australia saw growth that lagged behind the national level through much of the decade through to late 2014. However, South Australia has shrugged off the effects of the more modest rates of population growth in this state to generate growth in retail turnover at, or close to, the Australian average for a couple of years now.

CHART 7
RETAIL TRADE BY SECTOR - % CHANGE JAN 2015 TO JAN 2016 - SEASONALLY ADJUSTED



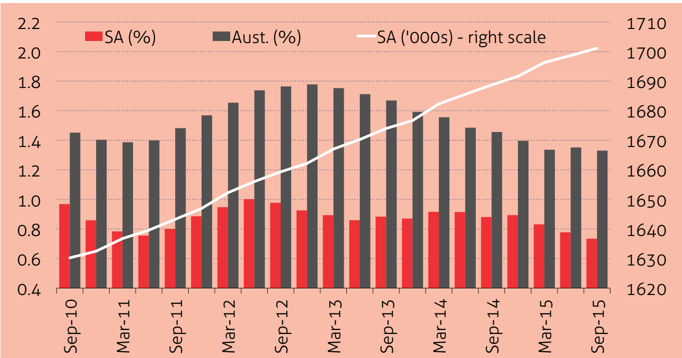
The solid local outcomes in retail trade cover a relatively wide divergence of experiences across different retail categories. Over the past year, the strongest growth in sales has been in hospitality, with rising housing prices also encouraging families to spend more on household goods. At the other end of the scale, there's been no growth in sales at department stores over the past year and only relatively modest growth in the food and clothing categories.

CHART 8
NEW MOTOR VEHICLE REGISTRATIONS - SEASONALLY ADJUSTED



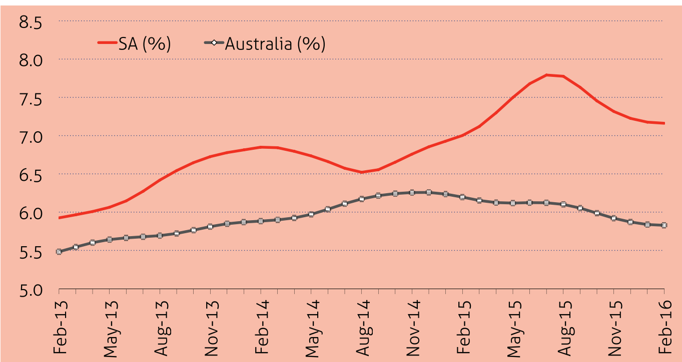
Motor vehicle sales in South Australia have surged relatively sharply over the past half year. That's also consistent with the greater confidence seen in some housing investment decisions, with families in this state showing a degree of willingness to lay out money on big dollar decisions. The surge in sales of motor vehicles in South Australia over the past six or so months makes this state a relative standout on the national stage, characterised by more modest gains in new motor vehicle registrations.

CHART 9
POPULATION TRENDS - % CHANGE ON PREVIOUS YEAR AND LOCAL LEVEL ('000S)



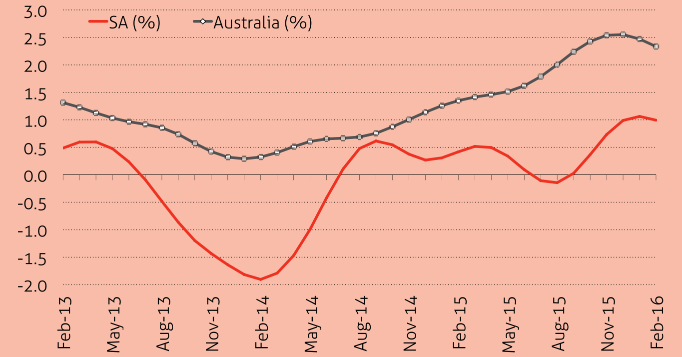
Latest population data shows that continuing moderation in the growth of 'people power' in the state has seen population gains drop below the trend averaged since the turn of the current decade. However, although South Australian population growth has been slowing, it has been relatively small against a sharper national population slowdown.

CHART 10
TREND UNEMPLOYMENT RATE (%)



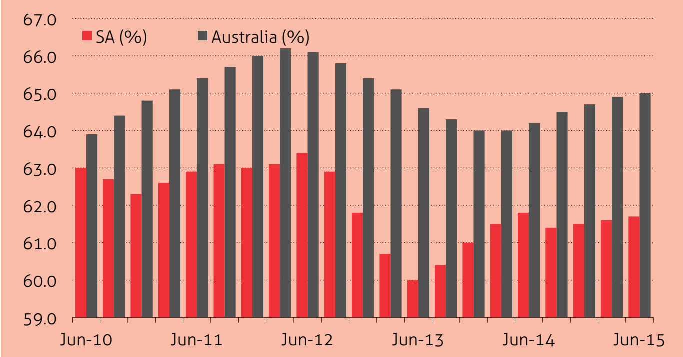
The South Australian economy continues to suffer from the earlier strength in Australian interest rates and exchange rates. It has therefore benefitted less than state economies with a similar sectoral make up – such as Victoria – from recent trends in financial markets. That said, the big phase of weakness in the local economy was probably in the first half of 2015, with the state's unemployment rate picking up at around that time, but subsequently easing. However, it remains well ahead of the national unemployment rate, and that gap shows no sign of narrowing in the near term.

CHART 11
EMPLOYMENT - % CHANGE ON PREVIOUS YEAR - TREND SERIES



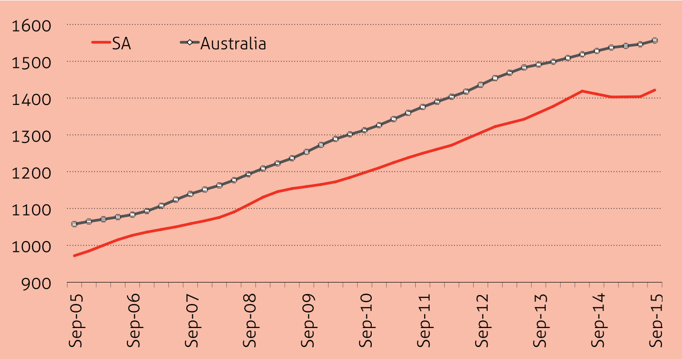
Alongside a range of other indicators, employment outcomes in South Australia made good gains in the second half of 2015. However, that doesn't change the fact that this state has been a relative underperformer in employment growth for some years now, with current trend gains in job numbers running at only half the matching rate evident nationally. Equally, there are some cause and effect factors in play. Adjusting for this state's weaker population growth and older population structure, South Australia's employment outcomes have been solid.

CHART 12
ROOM OCCUPANCY RATE - TREND SERIES



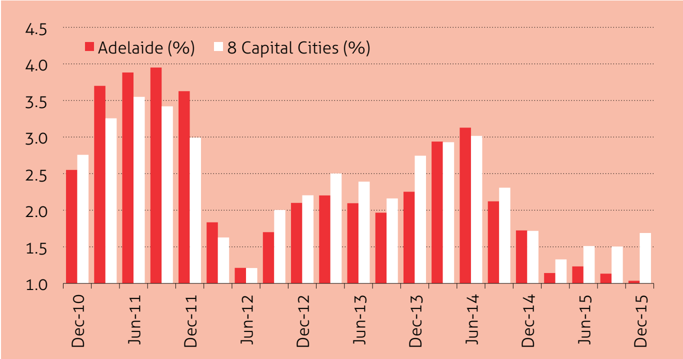
The downswing in the Australian dollar in recent years has seen: first, a trend away from Australians holidaying overseas; and second, towards the world increasingly visiting Australian shores. The first of these two factors is consistent with increased domestic tourism. A swing towards holidays within Australia by Australians usually works to the advantage of room occupancy rates in South Australia. On the other hand, however, increased flows of international visitors to our shores tend to be more important for other states than it is for South Australia. On balance, recent years have indeed seen some modest gains in average room occupancy rates in this state, but they are still tracking below the equivalent indicator nationally.

CHART 13
TOTAL AVERAGE WEEKLY EARNINGS ($) - PERSONS IN FULL-TIME EMPLOYMENT



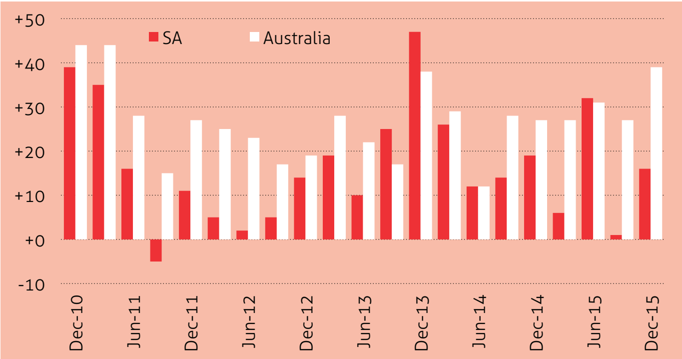
There's long been a gap between average wages available in South Australia and those evident elsewhere. For a long time that reflected the wage premiums for working in Australia's biggest states – New South Wales and Victoria – and acted as an offset for the higher living costs evident in cities such as Sydney and Melbourne. More recently, wage gains have been faster in the sunbelt states selling into China's resources boom. Either way, wages in this state have been relatively stagnant for a couple of years now, leaving a gap versus the national average wage rate which has been increasing in size.

CHART 14
CONSUMER PRICE INDEX, ALL GROUPS - % CHANGE ON PREVIOUS YEAR



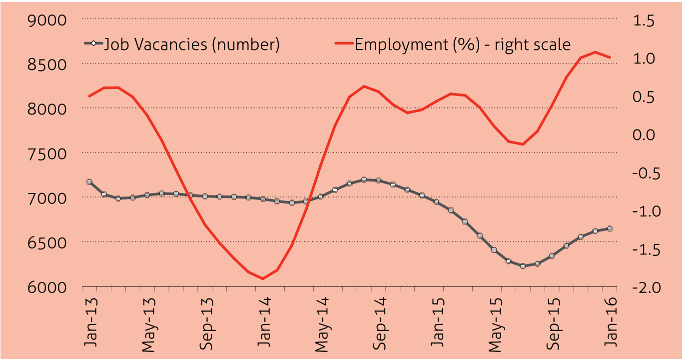
State and national trends in the growth in consumer prices typically run fairly closely together. But the Australia-wide slowdown in inflation since the middle of 2014 has been even more evident at the local level. In part that owes itself to the modest pace of economic growth in this state. As a result, South Australian businesses have less pricing power than their national counterparts, and the overall growth in consumer prices has been very little for more than a year now.

CHART 15
SMALL BUSINESS CONFIDENCE - NET BALANCE



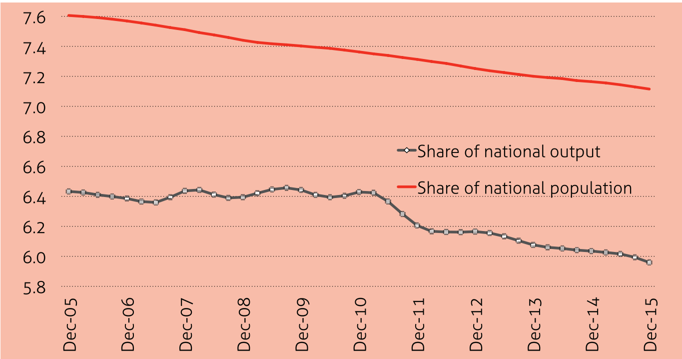
Small business confidence in South Australia tends to go through relatively big cycles compared to the equivalent levels on the national stage. Latest data saw a pickup in business confidence both nationally and in this state, but local small business confidence has lagged the national figure since mid-2015.

CHART 16
EMPLOYMENT GROWTH & JOB VACANCIES



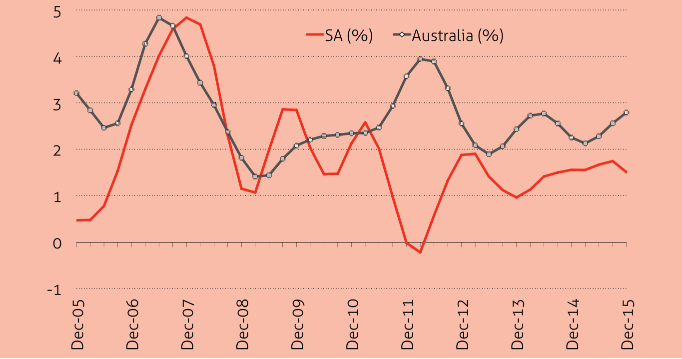
Employment growth in South Australia lifted over the past six months, broadly mirroring a matching increase in job vacancies in the state. However, the pickup in vacancies has been pretty modest, and current levels of vacancies are actually below those of a year ago and even further below those of two years ago. That suggests it may be hard for the recent pickup in employment growth to maintain its pace.

CHART 17
SHARE OF NATIONAL OUTPUT AND POPULATION (%)



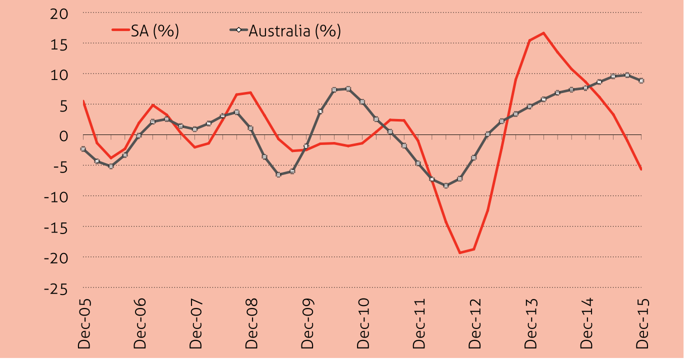
South Australia broadly maintained its share of the Australian economy in the half a decade prior to 2011. Given that the state's population growth lagged the national number across this period, and also that the resources boom did bigger things in other states than it did in South Australia, that's a pretty good outcome. Since then, however, the state has lost market share within Australia on both the economy and population.

CHART 18
OUTPUT - % CHANGE ON PREVIOUS YEAR



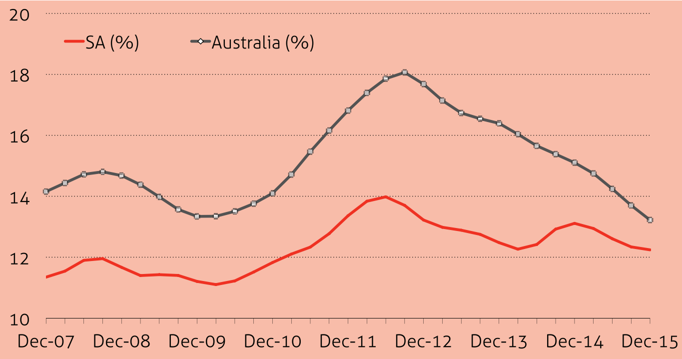
Overall economic growth in South Australia is estimated to have been close to 2% through the course of 2015. Although that lagged the national growth across the matching period, it does suggest that South Australia's growth has held up relatively well since 2011.

CHART 19
DWELLING INVESTMENT - % CHANGE ON PREVIOUS YEAR



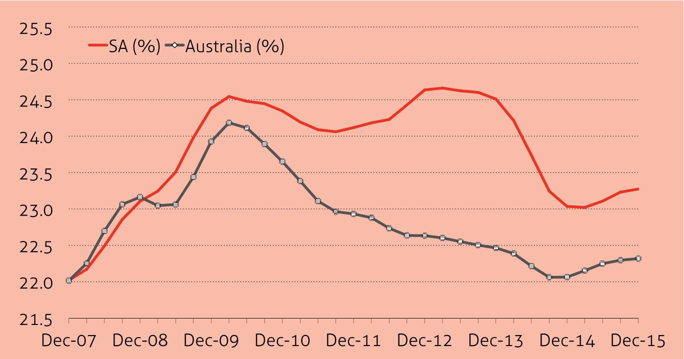
The recent uptick in a number of forward indicators for housing construction activity point to the potential for some better news ahead for the local homebuilding sector. That said, to do so would require swimming against the current tide, given that the pace of building new homes and renovating old ones in this state recently dropped into negative territory.

CHART 20
BUSINESS INVESTMENT - % OF OUTPUT



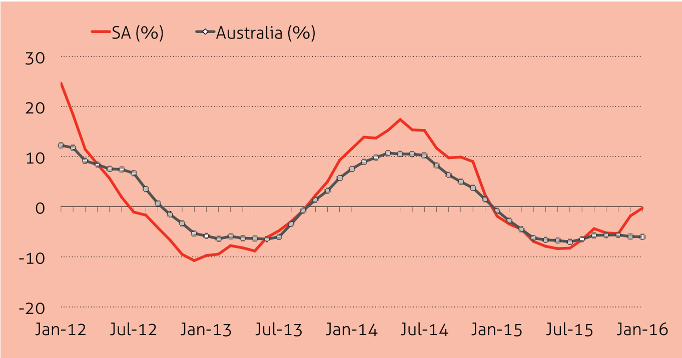
A surge in business investment spending through to early 2012 has been a remarkable feature of Australia's economic landscape over the past decade and more. However, the so-called 'construction cliff' continues to weigh on the national numbers, whereas the matching downturn in South Australia has been small, moving the state and national measures closer together.

CHART 21
PUBLIC SECTOR OUTPUT - % OF TOTAL CONSUMPTION AND INVESTMENT



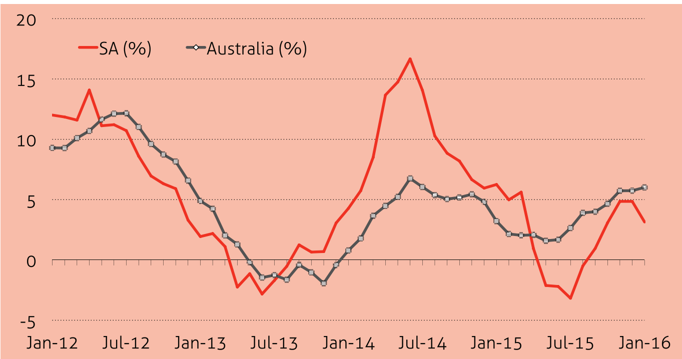
Public sector spending in this state got a considerable boost during the global financial crisis, but public sector output has been easing as a share of the national economy as the big stimulus programs increasingly wrapped up through the course of 2010. South Australia's own public sector cutbacks came rather later, with a rush of writedowns through the course of 2013 and well into 2014. However, public sector spending has regained its momentum as share of the economy as a whole over the course of 2015.

CHART 22
MERCHANDISE EXPORTS - % CHANGE LAST TWELVE MONTHS TO PREVIOUS



Although South Australia's merchandise exports earnings have been flat over the past year, that is still a strikingly successful performance when compared to its national counterpart. Nationally, the increase in the volume of mineral and energy exports has been more than offset by the big falls in commodity prices (such as coal and iron ore).

CHART 23
MERCHANDISE IMPORTS - % CHANGE LAST TWELVE MONTHS TO PREVIOUS



With export earnings under pressure, it is no surprise that import growth has moderated since 2014 – especially for South Australia. However, the impact of the lower Australian dollar has pushed up a range of import prices, with a consequent flow on effect to a lift in the value of merchandise imports over the year.

Trends May 2016

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