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thebigpicture guideposts for the private investor is published by *thebigpicture* Economics (ABN 71 040 787 936). The author, John A Robertson, while working in Australia, London and New York, has over 20 years experience in international financial and commodity markets, corporate strategy, financial and business evaluation and government policy. He has been Chief Economist and a director of a leading Australian investment bank. He has been a top-rated institutional equity analyst and has marketed investment advice in all the major international financial centres.

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THE IRAQI WAR: WHEN TOO MUCH INFORMATION IS NOT ENOUGH

It is probably still too early for investors to come out of their economic bomb shelters. The implicit assumption in many financial markets that the Iraqi war would be a straightforward use of technology and military power created a danger for investors. There are also broader economic tensions surfacing.

Markets, not unusually, had been assuming the best of possible outcomes. However, as *thebigpicture* observed last week, there are a range of possible outcomes to the war which are not so attractive for the US military planners or for market conditions. And it became more evident in the past week how quickly perceptions can change and how volatile the market reaction can be in their wake.

One aspect of the war with a market impact is the abundance of information to which to react as the war goes on. Real time coverage from 'embedded' journalists is creating a television spectacle for an audience already being conditioned through by programmes like the top rating '24' to just how much can be packed into one day.

Almost in contrast, there is a sense of disappointment amongst commentators that the US military has accomplished so little in real life. If Dwight Eisenhower had been given similar scrutiny, would his command have survived the ensuing criticism of his snail-like pace following the Normandy landings?

In this war, there is an industry of former military planners and commentators second-guessing their successors. Setbacks or achievements are now evident very quickly. Making genuine investment decisions without also second-guessing them in this environment will be particularly hard.

So the biggest risk for the financial markets (and political leaders) remains that the speed and efficacy of the US military strike, no matter how exemplary by the standard of a military planner, will be too slow for the viewer at home. This overlays the already prevailing anxiety about the growth of the US and world economies.

There are some signs that the US economy as well as the European group had already seen the worst of the economic downturn. Although growth remains weak, the momentum seems to have turned. There have been some indicators which have surprised on the upside occasionally. There have been some which have disappointed but a turning point could have been forming. The level of confidence about the profit outlook, however, has not been sufficient to hold equity markets or to bolster them by enough to help them rise sustainably.

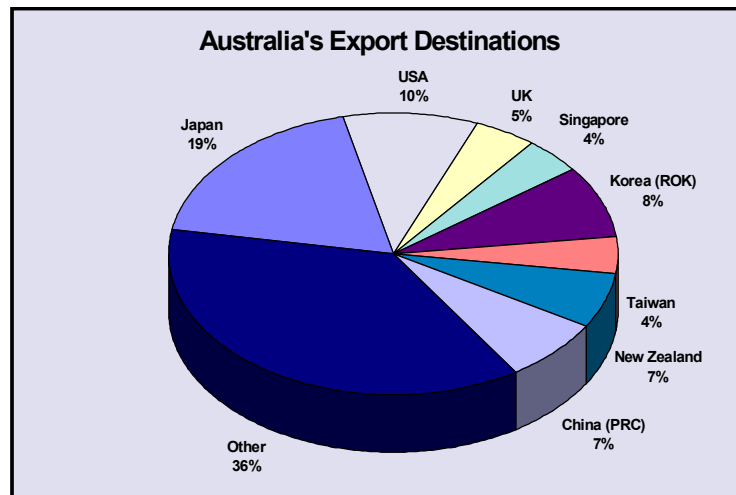
Under normal circumstances, this might still be enough to create a turning point in equity values. The war is having an additional indirect impact. Not only might it be affecting the psychology of the consumer and businessman taking spending decisions, it is also modifying the spending decisions of policy makers.

The US administration has sought an additional \$75 billion from the Congress for the

"...the biggest risk for the financial markets (and political leaders) remains that the speed and efficacy of the US military strike, no matter how exemplary by the standard of a military planner, will be too slow for the viewer at home."

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THE WEEKLY CHART SPOT



Source: Australian Bureau of Statistics

“...regional growth prospects, despite being downgraded following the late 1990s economic crisis, remain relatively attractive. Arguably, much of the growth and dynamism which had been anticipated from the region in the 1990s is still to come.”

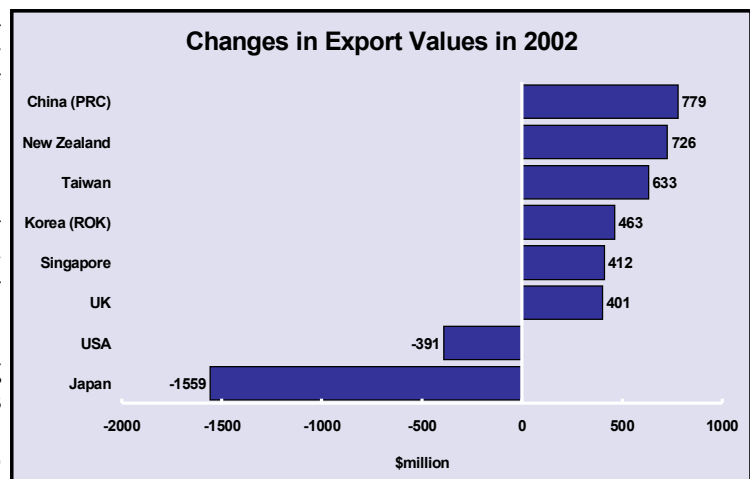
Five of Australia's largest eight export destinations were within Asia and accounted for 42% of Australia's \$119.5 billion export revenues in 2002 according to recently released foreign trade statistics from the Australian Bureau of Statistics. The statistics also show that the economic slowdowns in Japan and the USA have had an adverse effect on Australia's export performance.

While Japan takes almost twice the level of Australian exports as the next largest destination country, its growth outlook and likely change to the structure of its economy will probably constrain its ability to expand its imports of Australian products significantly. It is likely to diminish in importance over time. Nonetheless, it is starting from a sufficiently high base that, no matter what its medium term prognosis, it will remain a highly important trading partner.

On the other hand, the USA, which is the next largest importer of Australian goods, has better longer term growth prospects. The outlook for the USA as well as the size of its market are the reasons for the enthusiasm of the Australian government for a free trade agreement with the USA.

Even so, regional growth prospects, despite being downgraded following the late 1990s economic crisis, remain relatively attractive. Arguably, much of the growth and dynamism which had been anticipated from the region in the 1990s is still to come. Its population growth is expected to average 1% a year over the next 25 years and the UN has estimated that 60% of the world's population increase over the first quarter of this century will be in the Asian region.

It is hard from the statistics to be emphatic that the USA will be more important for Australia than (non-Japan) Asia over coming years. The statistics imply that Australia should be careful to avoid hitching itself



to one group or the other. Its best interests seem to lie in ensuring that it is maximizing its opportunities in both regions and that it should avoid doing anything which might jeopardize its position in one for the sake of achieving a short term advantage with the other.

THE IRAQI WAR CONT'D

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conduct of the war. This request has come sufficiently late in the piece that some have suggested duplicity on the part of the administration: perhaps it had been seeking to lock in the tax cuts which were being sought before bringing forward approval of the military expenditure.

In any event, the ploy, if that is what it was, did not work. The US Senate voted to effectively halve the \$726 billion tax cut request to curtail an estimated deficit of \$482 billion for fiscal 2004 compared to a surplus of \$87 billion as recently as fiscal 2000.

There had also been some conjecture amongst US legislators about whether the tax cuts were needed or whether they were being directed most effectively and, for some, the war provided a welcome excuse to scupper their implementation. The complication of wartime funding is already starting to have an influence on domestic economic policy choices.

Australia's budget for 2003/04 which is now being prepared will show similar tensions. Concessions on superannuation taxation, equalization of marginal personal and corporate tax rates and elimination of some temporary levies will be just some of the matters removed from the agenda by the wartime commitment as will a wide range of expenditures. Even then, most likely, the ability to retain a budget surplus will have been lost.

There could also be a longer term effect on investment flows. Those countries participating in the military coalition risk longer-term ostracism where there are choices to be made about which compa-

nies can gain access to markets. This is more likely to affect businesses operating from the USA and Britain but Australian companies, which had once been able to gain some advantage by not being associated overtly with big power politics, will no longer be able to count on that advantage, at the margin. Its small country status will have been lost.

As a small trading nation, Australia's well-being depends on its ability to export and invest. Through the Iraqi adventure it has rebalanced its relationships away from Asia, the Middle East and Europe toward the USA. While one can argue that international politics and business should not mix, they do.

But will a more overt association with the USA compensate? One can be sceptical about what advantage Australia might glean from its newfound camaraderie with the USA. One of the lessons the USA might draw from its Iraq experience is that it is not appreciated on the world stage. A widely hostile reaction to its endeavours might go further to convincing US policymakers that its long evident isolationist tendencies are well based. In due course, this will leave Australia at the mercy of domestic US politics when it comes to having any special access to the US market.

Under these circumstances, any special relationship between John Howard and George W Bush will have value only as long as they are in office. Can the same closeness be assumed between Peter Costello and Hilary Clinton, for example? If not, then Australia's economic positioning has been disadvantaged and is based on such flimsy connections as to be of little value.

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E-COMMERCE: DOMINATED BY B-2-B CONT'D

(Continued from page 4)

e-sales through EDI networks. In 2001, EDI sales for merchant wholesalers accounted for 86 percent of their e-commerce sales.

Within retailing, over 90 percent of e-sales are accounted for by nonstore retailers (75%), and motor vehicle and parts dealers (16%). Merchandise categories with the highest percent of online sales include books and magazines with 45% of total sales online and electronics and appliances with 39% of sales online.

The statistics also show how the growth in

retail usage of e-commerce is coming from non-store retailers. This is perhaps not surprising since it means that, having already achieved acceptance amongst their customers for remote ordering, transferring customers to an electronic ordering system was relatively easy.

The Electronic Shopping and Mail-Order Houses industry association has reported that e-sales accounted for 24 percent of all sales in 2001 compared to 19 percent in 2000.

E-COMMERCE: DOMINATED BY B-2-B

e-commerce has been adopted far more widely for transactions between businesses than by consumers seeking to purchase goods or services. The extent of the difference has again been highlighted by some recent statistics from the US Census Bureau.

thebigpicture for the week commencing 3 March 2003 reported US statistics which showed that only 1.3% of retail transactions undertaken in the USA in the past year used electronic ordering systems and could be classified as e-commerce. Consumers, it appeared, were yet to be persuaded that the medium provided a sufficiently higher level of convenience for them that they should change their historical purchase patterns.

The US government has now released data for 2001 based on a wider coverage of the US economy which shows that adoption of electronic ordering technology has become widespread but was more likely to be used in certain sectors of the US economy. In particular, over 93% of e-commerce transactions were between businesses.

Sixty eight percent of e-commerce transactions were in the manufacturing sector where e-shipments accounted for 18.3 percent of the value of all shipments from US manufacturing plants. This was not significantly different to the proportion in 2000.

Manufacturing sector e-shipments are pervasive, accounting for at least 10 percent of shipments in 15 of 21 industry groups. The share of total shipments is largest in transportation equipment (44%), followed by beverage and tobacco (38%) and electrical equipment, appliances, and components (25%), according to the US Census Bureau.

E-sales represented 10.0% of total merchant wholesale sales in 2001, up from 8.8% in 2000. This is the next most significant group after manufacturing to adopt e-commerce as a means of doing business. Merchant wholesalers are characterized by taking title to the goods they sell.

Sixty four percent of total e-sales by merchant wholesalers occurred in three industry groups: drugs (36%), motor vehicles, parts and supplies (16%) and professional and commercial equipment and supplies (11%). These same industry groups accounted for about 62% of e-sales by merchant wholesalers in 2000.

Among merchant wholesalers, only six out of 18 industry segments sold 10% or more of their merchandise over online networks. Drugs and drug supply e-sales are 48% of the total sales within the segment, motor vehicles, parts and supplies represent 22% of their total sales, apparel piece goods e-sales are 14% of total sales, computer equipment and supplies account for 13% of total sales, and hardware, plumbing and heating equipment e-sales are 10% of their total sales.

Wholesalers achieve e-sales primarily through Electronic Data Interchange networks. All merchant wholesale industry segments use EDI networks and almost all generate more than two-thirds of their

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Manufacturing e-sales	
Sector	% of sector sales
Food products	11.9
Beverage and tobacco	38.4
Textile mills	9.7
Textile product mills	23.2
Apparel	19.5
Leather and allied products	16.3
Wood products	5.6
Paper	13.0
Printing and related support activities	5.8
Petroleum and coal products	7.4
Chemicals	12.4
Plastics and rubber products	16.1
Nonmetallic mineral products	8.3
Primary metals	10.3
Fabricated metal products	9.5
Machinery	13.4
Computer and electronic products	17.1
Electrical equipment, appliances, and components	24.6
Transportation equipment	43.9
Furniture and related products	13.0
Miscellaneous	13.5

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