managing risk, enabling trade

market monitor

Adapting to the challenging economic environment

December 2010

For most, insolvency figures head in the right direction

In their country reviews for this month's Market Monitor, most of our expert underwriters report a fall in the number of business insolvencies. In France, our forecast is for a 10% drop in the number of insolvencies in 2010. Norway saw a year-on-year improvement in insolvencies of 8% in the third quarter and in Australia, while still higher than pre-crisis times, the number of companies entering administration and insolvency appointments fell too. Official figures for Canada show a massive year-on-year business insolvency drop of 29.2% in September, reflecting an improvement in payment trends across most sectors.

In Spain, whose economic troubles have been well publicised, the number of business failures in the third quarter of 2010 is down 32% on the previous quarter. While Spain's recovery remains shaky, the comprehensive structural and financial reforms announced by Prime Minister Zapatero should instil some confidence in the economy, at least in the long term if not the immediate future.

Even in Italy, where business failures rose 13.8% year-on-year in the third quarter, there is cause for optimism, as we believe that the peak has now past and that insolvencies will decrease 5% next year.

In this issue…

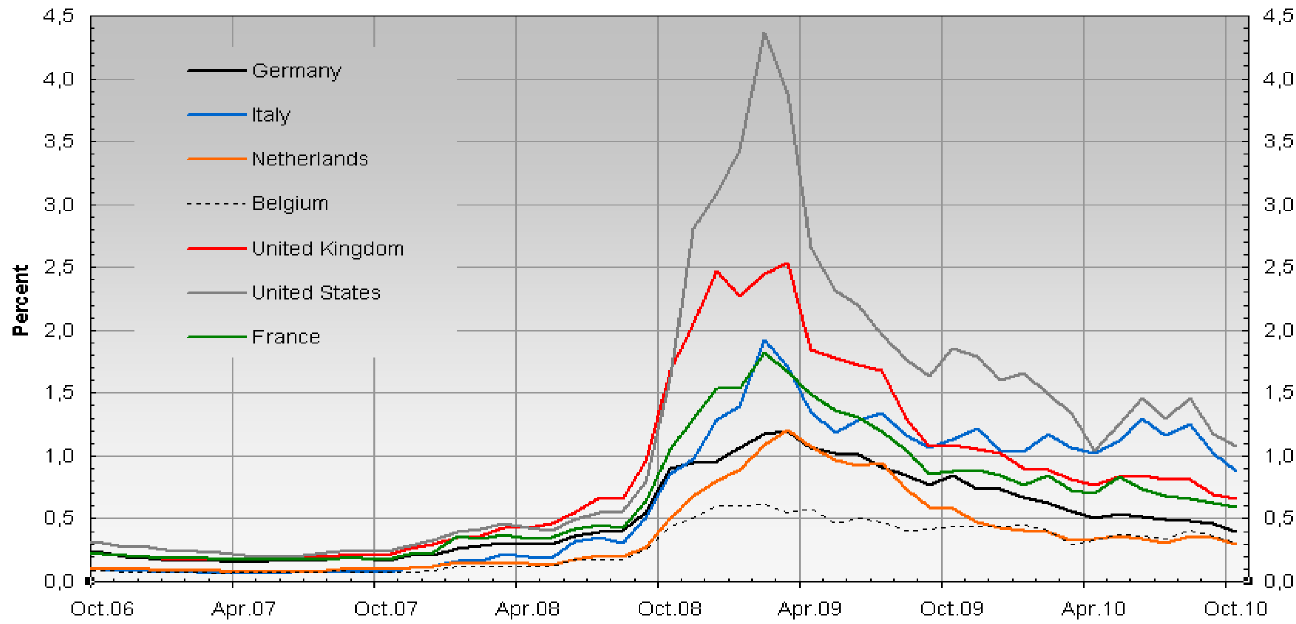
…we feature the following markets:

- France – with a spotlight on the electronic components and IT sectors
- Canada – with a spotlight on the manufacturing and forestry sectors
- Italy
- Spain
- Norway
- Australia
- India

Expected default in Western Europe and USA

One of the most important factors that any business needs to know is the trend in insolvencies in their markets. The following Expected Default Frequency (EDF) chart is based on listed companies in the markets referred to, and the likelihood of default across all sectors within the next year. In this context, default is defined as a failure to make a scheduled payment, or the initiation of bankruptcy proceedings. Probability of default is calculated from three factors: market value of a company's assets, its volatility and its current capital structure. As a guide, the probability of one firm in a hundred defaulting on payment is shown as 1%.

Median EDF evolution by country



Source: KMV Credit Monitor and Atradius Economic Research

Following the trend of last month's Market Monitor, we again see a decrease in EDF in all the economies surveyed. In addition, the median EDFs for all those countries dropped to their lowest level for more than two years. Italy recorded the largest decrease (14 basis points), followed by the US (9 basis points), Germany (6 basis points) and Belgium and the Netherlands (5 basis points).

On the following pages, we assess the impact of expected default in key markets. As well as the expert view of our underwriters, we indicate the general outlook for each market and sector featured using these 'weather' symbols:

Excellent   Good   Fair   Gloomy   Bleak

France

The recovery has stabilised

According to the Statistics Office INSEE, French GDP grew 0.4% in Q3 of 2010, confirming the country's comprehensive, if slow, economic recovery. After low growth in the second quarter, household consumption increased 1.2% in Q3. The consumer confidence indicator has improved, gaining two points in November 2010 compared to October, although it remains below the long term average. Manufacturing production increased 0.7% on the previous quarter and 7% year-on-year. Gross fixed capital formation continued to improve: by 0.5% (after 0.7% on Q2). Exports remained steady (up 3% compared to 2.7% in the second quarter) while imports slowed slightly (2.1% against 3.9% in Q2).

The business climate indicators continued to improve gradually since our last report on France in September, but levelled off in November (see chart below).

Business climate indicators

	Oct. 09	Nov. 09	Dec. 09	Jan. 10	Feb. 10	Mar. 10	Apr. 10	May 10	June 10	July 10	Sept. 2010	Oct. 2010	Nov. 2010
Business climates													
France	86	88	87	90	90	92	96	96	97	98	102	104	104
Industry	89	90	89	91	91	93	96	97	96	98	99	102	100
Wholesale trade	-	79	-	83	-	87		95		100	103		103
Building	93	93	93	93	93	91	92	93	92	94	94	95	96
Retail trade	97	104	100	103	100	98	105	103	102	100	107	109	107
Services	85	86	86	88	89	92	98	98	98	98	99	101	102

Source: INSEE, Business tendency surveys

In November 2010, production in the manufacturing industry declined slightly after a dynamic 6 months. Although the inventory level remains low, forecasts are positive, thanks to rising export orders. Activity in the electrical goods and machinery sectors fell in November and, although it remains satisfactory, forecasts are rather pessimistic. Activity in the transport and automotive industries increased, thanks to a low level of inventory. However, production will probably decline as a result of a particularly low number of orders. The performance of the pharmaceuticals, rubber and plastics sectors is very positive and, with low inventory levels and higher international demand, production will increase. Although activity in the chemicals industry declined, forecasts remain positive, again because of low inventory levels. In contrast, production in the textile sector has continued to slow down, with a scarcity of new orders signalling a problematic outlook.

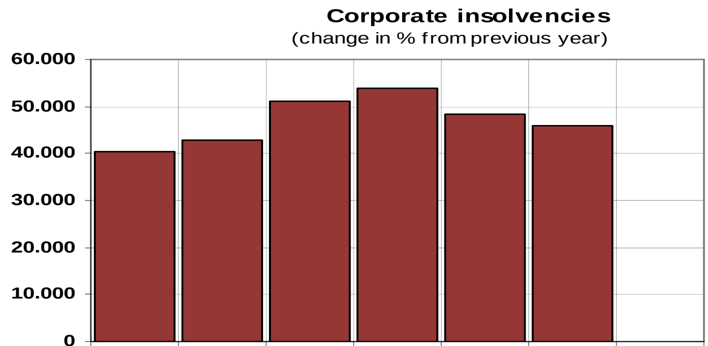
The construction sector is recovering slowly but forecasts are uncertain, as orders and backlogs are below the normal average and production capacities are not yet fully used. The retail industry recorded positive results in Q3, following a difficult second quarter. However, in November, activity slowed and forecasts are less optimistic.

France

Loans for the private sector (excluding financial institutions) continued to rise in September 2010 - up 3.6% year-on-year and 3.9% on the previous quarter - confirming the positive trend we had observed last summer. Loans for companies increased 1% year-on-year, with the contraction of short term credit issuance at last slowing (from -8.6% to -5.5%). Credit issuance for investments continued to increase: by 2.9 % year-on-year.

A 10% decrease in insolvencies seems likely for 2010

According to Altares, the number of defaulting companies decreased by 3.8% year-on-year between January and September 2010: to 44,556 cases. This trend was even more positive in Q3, with a 7.4% decrease in insolvencies. In terms of sectors, most industries showed significant signs of improvement, particularly manufacturing industries (-20%); construction (-7.8%) and retail (-8.8%). However, food suffered a 12% increase in insolvencies, mainly in the bakery subsector. Based on this overall improving trend, we still forecast a 10% decrease in business insolvencies this year, followed by a further 5% decline in 2011.



	2006	2007	2008	2009	2010*	2011*
Total	40.407	42.840	51.254	53.743	48.369	45.950
% change		6,0%	19,6%	4,9%	-10,0%	-5,0%

Source: Atradius Economic Research

In October 2010, the Expected Default Frequency (EDF) indicator for listed companies in France fell below 60 basis points for the first time this year - to 59 - reaching its lowest level since August 2008 (see chart page 2).

For the whole of 2010, the Economist Intelligence Unit and the International Monetary Fund forecast that French GDP will grow 1.6%, followed by an increase in output of between 1.4% and 1.6% next year. For manufacturing industries, the investment forecasts for 2011 are optimistic: with a 9% increase. However, private consumption is expected to stagnate.

Electronic components

How has the electronic components (manufacturing and wholesale) sector performed in the last six months?

Electronic components performed relatively well, thanks to a strong rebound in the automotive industry and dynamic activity in the aeronautics sector. Demand from the electronic equipment industries remained steady.

What is the current trend in insolvencies?

The insolvency trend in this sector has been positive. Recently, however, we have noticed a resurgence of claims received on buyers in the electronic machinery subsector, but it is too early to say if this reflects an upward trend.

What is Atradius' short term (6 month) outlook for the electronic components sector?

The short-term outlook for electronic components is still satisfactory, with stable prospects for automotive, aeronautics and electronic equipment production.

What is the Atradius underwriting approach to the sector?

The end-markets for electronic components suffered in 2008 and 2009 and the financial situation of companies in the sector has been weakened by accumulated losses and financing constraints. This is especially true in France where electronic manufacturers are mainly mid-sized companies. Our underwriting approach is prudent and depends on the subject companies having a well spread mix of product and financial flexibility to cope with investments constraints and working capital financing.

IT

How has the IT sector (software & computing services companies and IT wholesalers) sector performed in the last six months?

After 7 years of steady growth in IT purchasing, 2009 was a very disappointing year, ending with a contraction of between 2 % and 3% in the global IT trade sector. Performance in the first quarter of 2010 was still sluggish, but we have noticed significant signs of recovery since the second quarter.

What is the current trend in insolvencies?

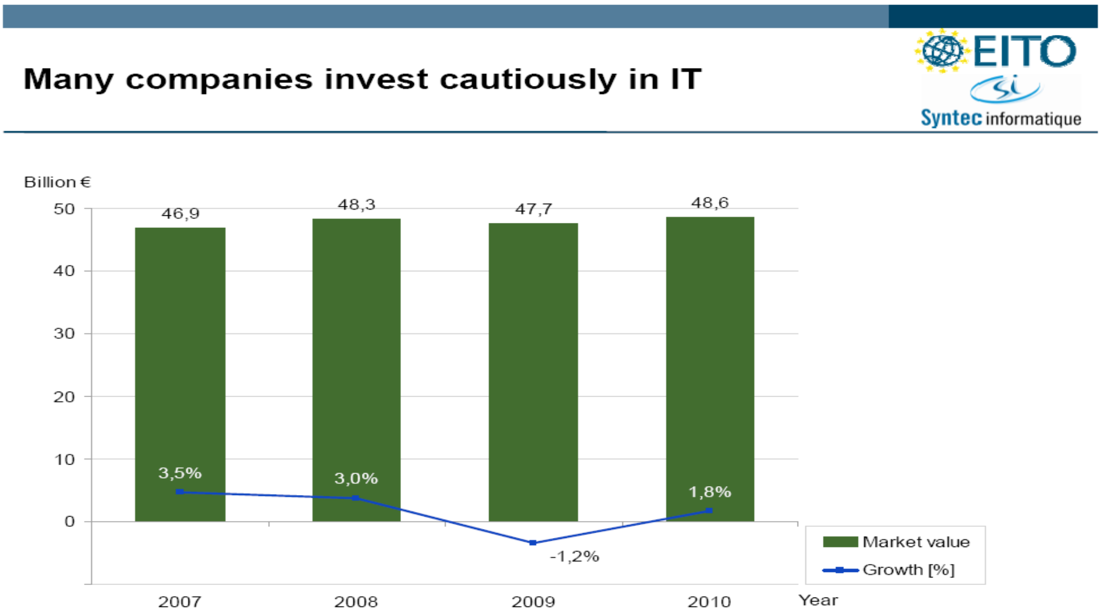
The insolvency trend has evolved favourably for software & computing services companies (SCSC), and we are seeing positive performance in both wholesale IT products and SCSC, with few credit insurance claims.

What is Atradius' short term (6 month) outlook for the IT sector?

SCSC will grow modestly in 2010. We expect small and medium sized players to benefit most from the recovery, thanks to their higher flexibility. Most companies are hiring new staff and 75% of the main groups should increase the number of employees before end of 2010. For the IT wholesale subsector, the coming months should also be positive, with growth of around 5%, driven mainly by demand from individual end-customers. However, IT purchases by businesses are expected to remain flat for the time being.

What is the Atradius underwriting approach to the sector?

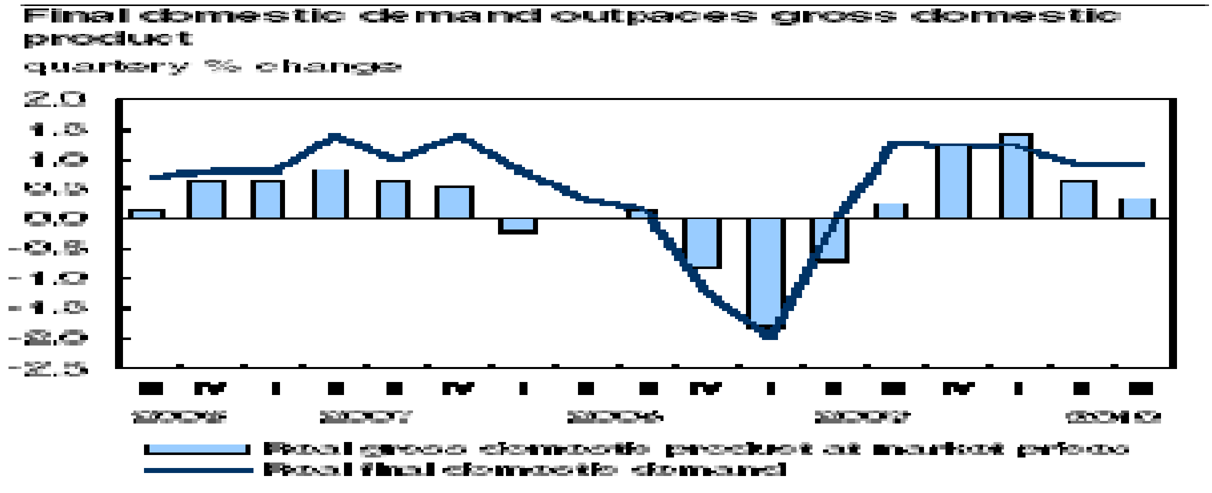
Our approach is generally positive, but we are paying close attention to the behaviour of the main IT customers, such as the public sector, banks and insurance companies, in view of budget constraints and subsequent lower IT purchases. Moreover, although the outlook for the IT market is positive, we have noticed considerable pressure on prices and margins and this could have a negative effect on suppliers in the sector.



Source: European Information Technology Observatory (EITO)

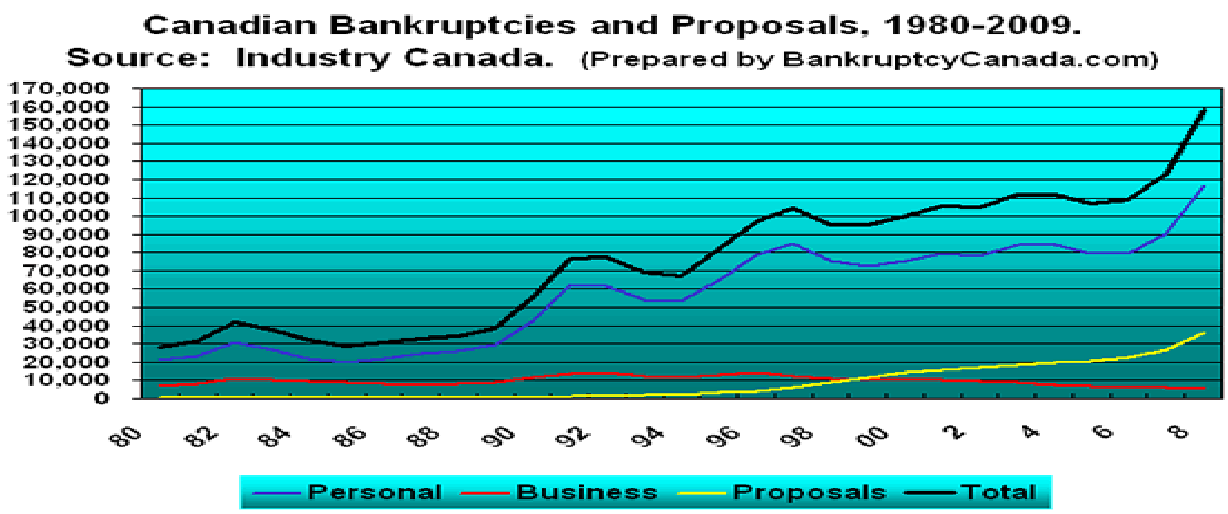
A steep drop in business insolvencies

According to Statistics Canada, the Canadian economy progressed slower than expected in Q3 of 2010, as lower exports and a weaker housing sector impeded growth. GDP grew 1% on the previous quarter, after a gain of 2.3% in Q2. On average, economists had expected a growth rate of 1.5 %, compared to the USA's 2.5% GDP growth. Domestic demand increased 0.9%, with more investment in plant and equipment: up 6.5%. Manufacturing, mining and the public sector were the main sources of growth in the third quarter, while increased consumer spending also contributed positively.



Source: Statistics Canada

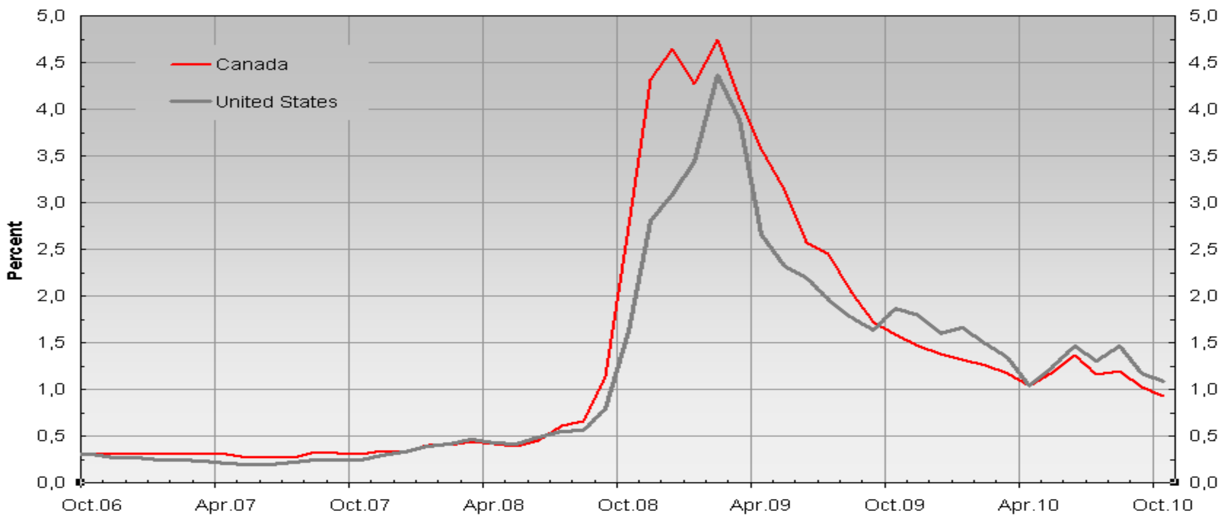
According to the Office of the Superintendent Bankruptcy Canada, the total number of business and consumer insolvencies (defined in the graph below as 'bankruptcies and proposals') decreased 26.5% year-on-year in September 2010, with consumer insolvencies dropping 26.4%, and business insolvencies 29.2%. For the year from September 2009 to September 2010, business insolvencies decreased 21%, thanks mainly to fewer business failures in the transport, warehousing, retail trade, manufacturing, construction, and agriculture sectors.



Canada

In October 2010, the Expected Default Frequency (EDF) indicator for listed companies in Canada dropped again compared to the previous month, to 93 basis points, and ending 382 points lower than at its peak in February 2009. The Canadian EDF has reached its lowest level in more than two years (see chart below).

Median EDF evolution by country: North America



Source: KMV Credit Monitor and Atradius Economic Research

Improving payment trends

Insolvency statistics, by their nature, tend to reflect earlier cycles, and so the falling number of business insolvencies in Q2 and Q3 of 2010 indicates a continued improvement in payment trends, across most commercial sectors, from 2009. As the overall Canadian economy improves we expected that, in the near term, the trend of Canadian payment defaults will continue to improve.

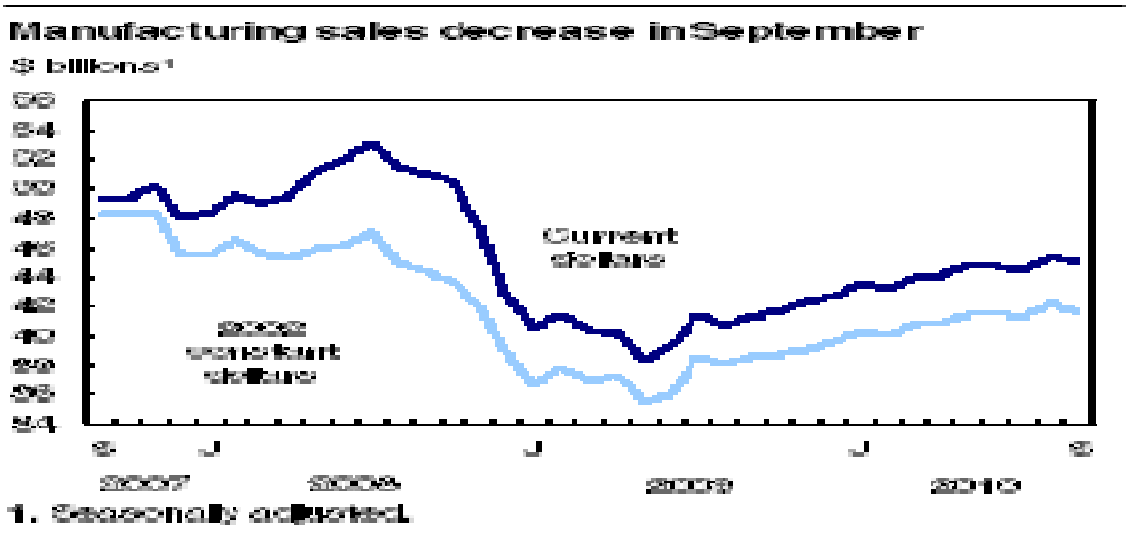
The manufacturing sector remains one of the sectors with the highest delinquency rates. Furthermore, wholesalers' position as middlemen also makes them susceptible to cash flow issues caused by late payments, and this can often lead to subsequent delays in their own outgoing payments. The natural resources and agriculture sector showed low delinquency rates, as would be expected since they are among the more stable sectors, while real estate, with its many hidden failures, tended to understate the actual extent of its delinquency rate.

The Bank of Canada currently expects the economic recovery to be more gradual than it had projected in its July Monetary Policy Report, with growth of 3.0% in 2010, 2.3 % in 2011 and 2.6% in 2012. Overall, economic growth in Canada is expected to become less reliant on household spending and government stimulus measures, while business investment and exports should pick up some of the slack. The Bank noted that output in the economy has now exceeded its pre-recession peak, and that all 400,000 jobs lost in the recession have been regained. However, unemployment remains high, at 7.9% in October 2010, reflecting a rise in the number of people looking for work. In comparison, in the United States only about one fifth of the jobs lost in the recession have been regained.

Manufacturing

How has the manufacturing sector performed in the past six months?

During the global economic downturn, demand for Canadian manufactured products, both domestically and from abroad, declined dramatically. The manufacturing sector's GDP dropped from C$ 170 billion in 2008 to C$ 151 billion in 2009. By the end of Q3 of 2010, demand had returned a little and output/production had begun to increase. The manufacturing sector's GDP at the end of September 2010 was showing a trend back to an annualized level of C$ 161 billion. However, a comprehensive rebound seems to have been constrained by a slower than expected recovery in the USA. Companies in this sector contended with a hyper-competitive marketplace and this competitive challenge was compounded by an elevated Canadian dollar. As recently as March 2009, the C$ 1.00 was equal to US$ 0.79, but it has steadily appreciated in 2009. Since January this year, has stayed above US$ 0.95.



Source: Statistics Canada

What is the current trend in payment delays and insolvencies?

Many companies in this sector are still making late payments, but nowhere near as many as in 2009, and the insolvency trend is downwards.

What should companies selling into the manufacturing sector pay particular attention to?

Companies who sell into manufacturing need to be aware of where their customers trade, i.e. what the end market is for their manufactured products. If their customers sell domestically, is their Canadian end market stable? Conversely, if they export their products, how have they managed the issues of foreign competition and exchange rate?

What is Atradius' short term (6 month) outlook for the manufacturing sector?

The short term outlook for the manufacturing sector is fair. As the global -and US- economy rebounds, the demand for Canadian manufactured products will naturally improve. However, unless companies in this sector address market issues and compete more effectively, the sector will not achieve a positive outlook in the near to medium term.

Forestry sector (wood products, pulp and paper manufacturing)

How has the forestry sector performed in the past six months?

During the global economic downturn, demand for Canadian forestry products declined, with the sector's GDP dropping from C$ 15.3 billion in 2008 to C$ 14.4 billion in 2009. By the end of Q3 of 2010, demand had returned and output/production had started to increase. The forestry sector's GDP at the end of September 2010 was showing a trend back to its pre-2009 level – at an annualized level of C$ 14.9 billion.

What is the current trend in payment delays and insolvencies?

There has been little evidence of an increase in payment defaults or insolvencies in this sector. The only meaningful data on default has been in the pulp and paper segment, as overcapacity and heavy debt loads from earlier periods of consolidation have led to reduced capacity and mill closures, and in some cases bankruptcy reorganizations: most notably Abitibi Bowater Inc.

What should companies selling into the forestry sector pay particular attention to?

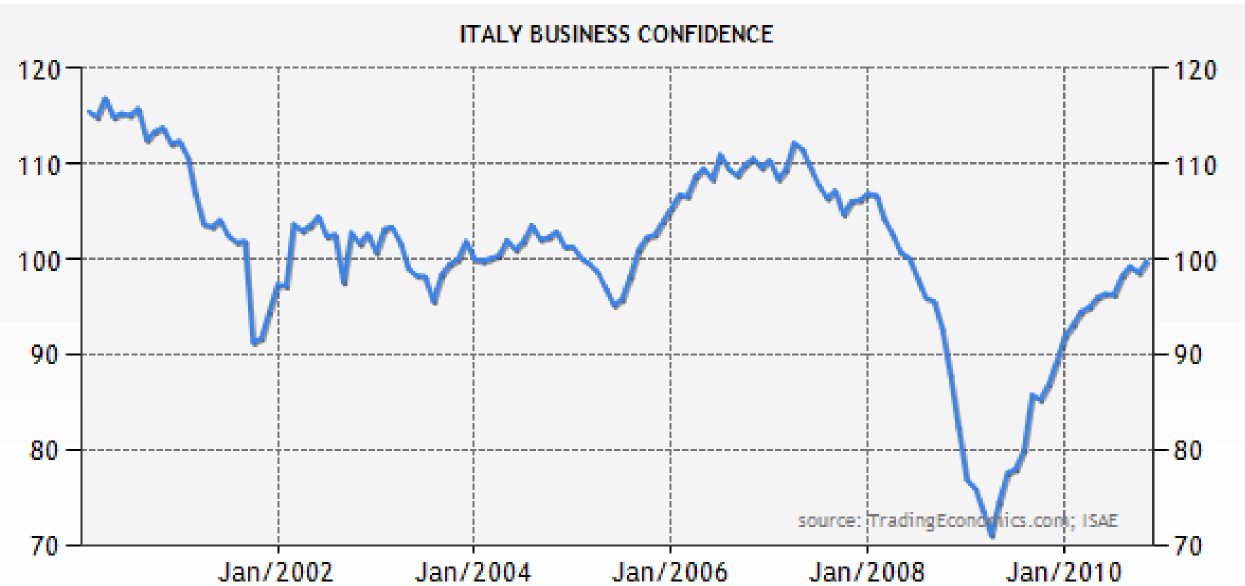
Companies selling into this sector should pay special attention to contractual terms of sale and ensure that all agreed conditions reflect industry norms. The longer the term, the more likely the chance of non-payment or the occurrence of deduction or reconciliation issues.

What is Atradius' short term (6 month) outlook for the forestry sector?

The short term outlook for the forestry sector is fair. Demand has started to return and, with overcapacity issues addressed, output should move upward. As long as the US economic recovery continues, so should the gains in Canadian forestry.

Christmas boost to electronics and IT goods

According to the Italian Statistic Office ISTAT, in the third quarter of 2010 GDP grew 0.2% on the previous quarter and 1% year-on-year, due mainly to an increase in the added value of industry and services. Several sectors have contributed to this output growth: mainly service sectors such as hotels, transport and information (+1.5%), but also manufacturing and construction (+ 0.9%), and those providing financial services (+ 0.3%) and utilities (+ 0.3%). However, added value in the agriculture sector declined (- 0.7%). In Q3, industrial turnover and new orders rose 2.0% and 2.1% respectively on the previous quarter, and business confidence increased slightly in October: to 99.8, the highest figure since June 2008 (see chart below).



Source: Tradingeconomics.com

After falling in the first eight months of 2010, consumer confidence improved again in September and October. In Q3, the ISTAT retail trade index increased 0.3% on the previous quarter and, according to Confcommercio (the association of wholesalers and retailers of goods), average family spending during this Christmas period will be quite satisfactory, although in real terms (net of inflation) its value will drop by 1.2%: from € 1,354 last year to € 1,337. In particular, Italian consumers will spend their money on food and on electronic/ICT goods such as PCs, Ipads and LCD TVs, while the purchase of traditional goods such as textiles and footwear will decrease. The electronics/ICT sector has already profited from the switch from analogue to digital TV broadcasting which has pressured consumers to either change their TVs or buy decoders.

Bank lines and overdues by sector (millions Euro)

	Bank lines 09-2010	Overdues 09-2010	Overdues/lines 2010
Agriculture	38.887	2.533	7%
Hotels and restaurants	38.490	2.270	6%
Metals	62.294	4.109	7%
Transport and logisitics	36.462	1.607	4%
Food	29.687	1.933	7%
Textile and footwear	26.015	3.619	14%
Professional and technical activities	46.638	1.139	2%
Constructions	165.812	10.166	6%
Wholesale and retail of cars and motorbikes	141.523	9.925	7%
Real estate	115.870	4.785	4%

Source: Bank of Italy

Insolvencies will decrease in 2010

According to the Italian Chamber of Commerce, corporate insolvencies increased 13.8% year-on-year in Q3 of 2010 (to 2568 cases). In terms of sectors, the insolvencies are well spread across all industries with more or less the same trend. The only peculiarity is in the wholesaler sector, in which, after a decrease in the number of insolvencies in 2009, insolvencies have risen again in 2010. From January to September there was a 23% year-on-year rise in insolvencies, indicating that the peak has now past. We estimate that insolvencies will decrease by 5% in the coming year

In October 2010, the Expected Default Frequency (EDF) indicator for listed companies in Italy dropped again compared to the previous month, to 88 basis points, and ending 110 points lower than at its peak in February 2009. The Italian EDF has reached its lowest level in more than two years (see chart page 2).

Since GDP has been growing in the last three quarters, Italy seems to be on the path of modest recovery, even though the trend has decreased in the last quarter. For 2010 the government estimates a 1% growth with an increase in consumption of 0.4% and an inflation rate of 1.6%. For 2011, both the Economist Intelligence Unit and the International Monetary Fund expect output to remain low: at 1%. Expectations are that GDP and consumption will not return the 2007 levels until the end of 2015.

Spain

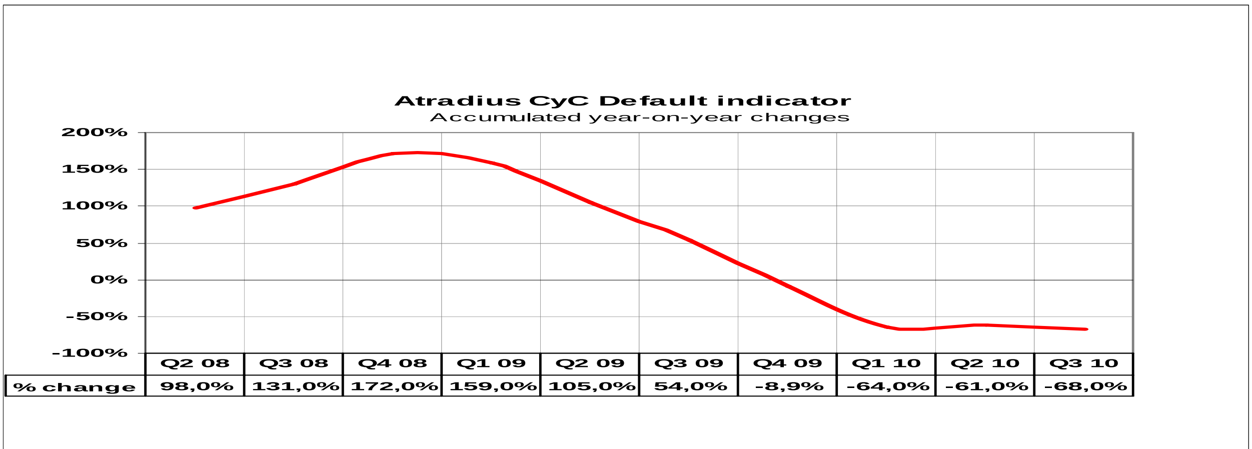
An uncertain recovery

According to the National Statistics Institute, GDP grew 0.2% year-on-year in Q3 of 2010, but not at all on the previous quarter (after a 0.3% increase in Q2). This stagnation comes as no surprise, since the Spanish government, under pressure from adverse financial market sentiment, has introduced austerity measures to reduce public debt. Curbs on public investments and on subsidies for car purchases, and the increase in the rate of VAT, from 16% to 18%, introduced in July 2010, have negatively affected both private consumption and industrial activity. After the boost to spending in Q2, with consumers rushing to beat the forthcoming VAT increase, household consumption slowed in Q3, with vehicle registration decreasing 25% after three quarters of robust growth. The industrial production index remains negative and fell 0.8% year-on-year in September, due mainly to declines in the investment intensive capital goods and durable consumer goods sectors. Export growth slowed in the third quarter: to 8.7% (after 11.6% in Q2). However, as imports fell even more, net foreign demand has again positively contributed to economic growth: increasing to 1.0 point. Future Spanish export performance depends largely on energy prices and the Euro-US$ exchange rate.

The labour market remains the Achilles´ heel of the Spanish economy, with an unemployment rate of 19.79% in October, leaving 4.5 million people jobless. Redundancies continue in the construction and manufacturing sectors and, in Q3, new jobs were created only in the service industry. Despite the passing of a labour reform bill early this year, a comprehensive improvement in the jobless situation cannot be expected in the short term, and this remains one of the biggest obstacles to a return to robust growth.

Comprehensive reforms will boost confidence in the long term

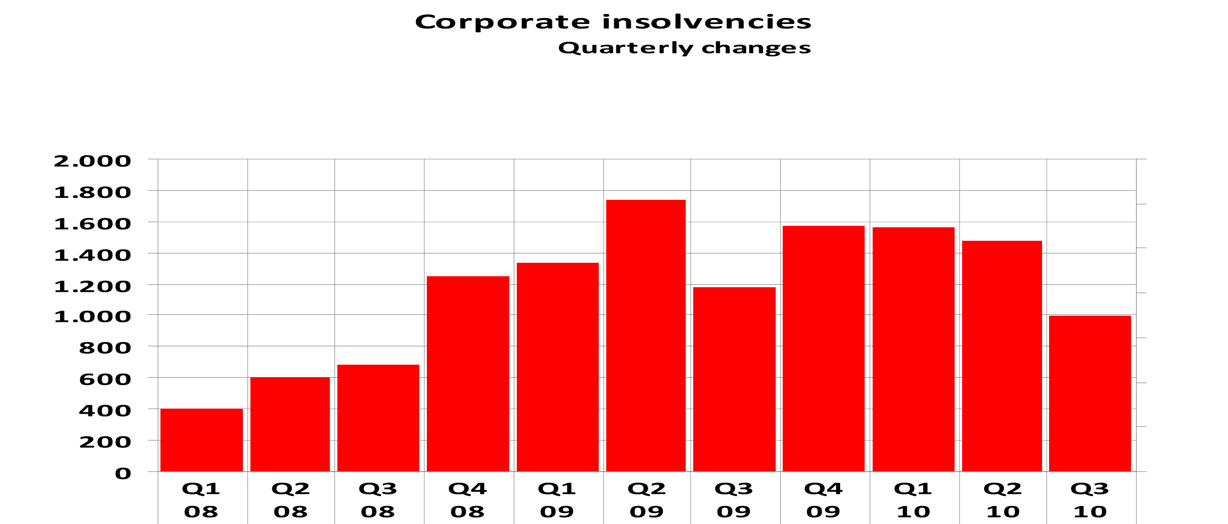
Since our last Market Monitor analysis in August, the positive change in the pattern of payment delays by Spanish companies has gained further momentum. In Q3, the median payment default decreased 68% year-on-year, after 64% and 61% decreases in the two previous quarters, according to the Atradius Crédito y Caución Default Indicator. This is the fourth consecutive quarter of improvement, although, in context, the sharp year-on-year decrease in payment delays began from a very high level (see chart below).



Source: Atradius

Spain

Spanish companies still tread a perilous path through the minefield of insolvencies. However, our data, based on figures published by the Official State Gazette (Boletīn Official del Estado), show 997 business failures in Q3: 32% less than the previous quarter and the first time since Q3 of 2008 that the quarterly number of insolvencies has been below 1,000 cases (see chart below).



	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	Q4 09	Q1 10	Q2 10	Q3 10
Total	406	604	678	1.249	1.335	1.741	1.180	1.576	1.560	1.477	997
% change	22%	49%	12%	84%	6,9%	30%	-32%	34%	-1%	-5%	-32%

Source: Atradius

In the wake of the Irish debt crisis, Spain has come under pressure from adverse financial market sentiment, with speculation of the danger of contagion from the crisis in Greece and Ireland increasing. Yields on Spanish bonds hit all-time highs in November, as a result of which Prime Minister José Luis Zapatero has announced a broadening in scope and speeding up of reforms to the labour market and pensions and the restructuring of the banking system. He has also reiterated the government's determination to reduce the budget deficit according to EU demands.

We think that, in view of these comprehensive reform measures, confidence in the Spanish economy will return in the long term. However, in the short term Spain will be characterized by low GDP growth rates due to weak domestic demand, austerity measures, structurally high unemployment and by exposure to adverse financial market sentiment. After a 0.3% contraction this year, output growth is forecast by the Economist Intelligence Unit to rebound only 0.4% in 2011.

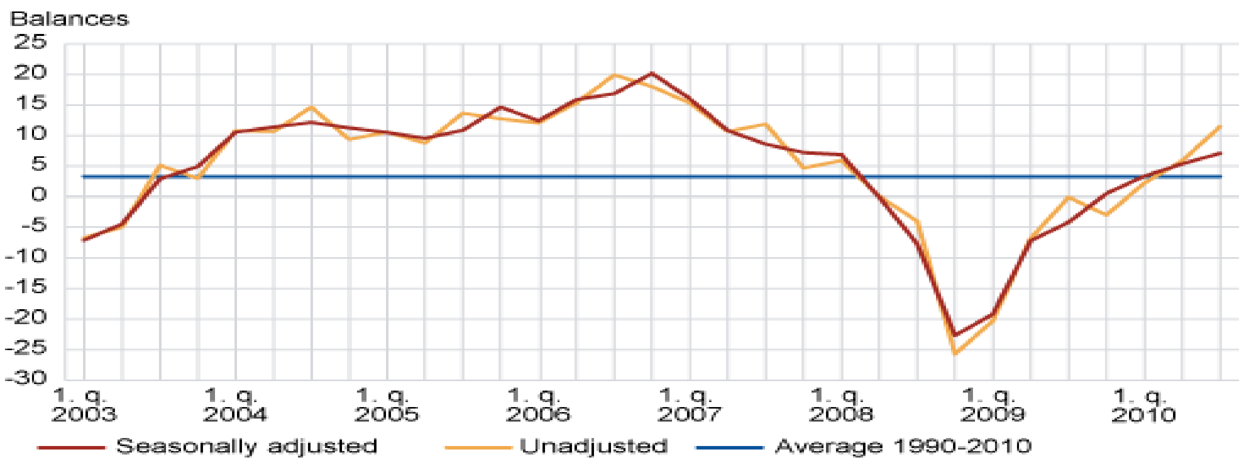
Norway

Industrial confidence increases

The Norwegian economy has livened up considerably since the summer, due mainly to stronger domestic demand. According to Statistics Norway, GDP for mainland Norway increased 0.9% year-on-year in Q3 of 2010 after 0.5% growth rates in the two previous quarters. Production increased moderately in manufacturing (1.9%) and construction (1.7%), while household consumption rose 1.3% after a slight decrease in Q2. Exports of traditional goods rose 2.2%, with fish/fish products and chemicals the major contributors. Unemployment remained unchanged at 3.5%, but this is still low compared to other countries.

With moderate growth in the third quarter, Norwegian industrial managers assess the short term outlook to be positive (see chart below).

Industrial confidence indicator. 1. quarter 2003-3. quarter 2010



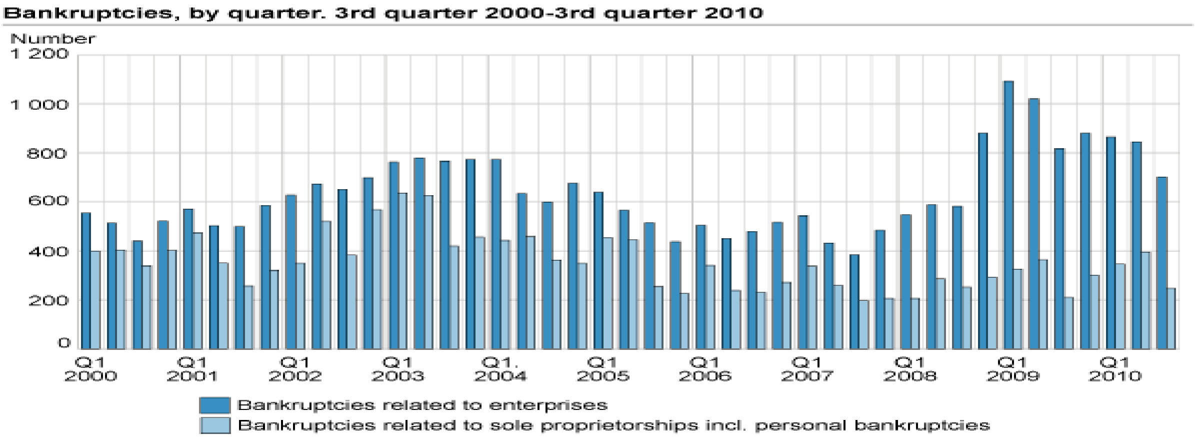
[1] Industrial confidence indicator is the arithmetic average of the answers (balances) to the questions on production expectations, total stock of orders and inventories of own products (the latter with inverted sign).

Source: Statistics Norway

The shipbuilding sector has improved markedly since the beginning of the year, thanks largely to a governmental support package launched in April, which included increased guarantee capacity, extended loan facilities, new public orders and other subsidies. Having seen severe price reductions and a record number of bankruptcies in 2009, the metal sector has recovered appreciably, with an increase in orders and in the price of metal products. However, the paper sector is still struggling as a result of worldwide overcapacity and price pressures. The important salmon sector continues to profit from the salmon virus epidemic in Chile.

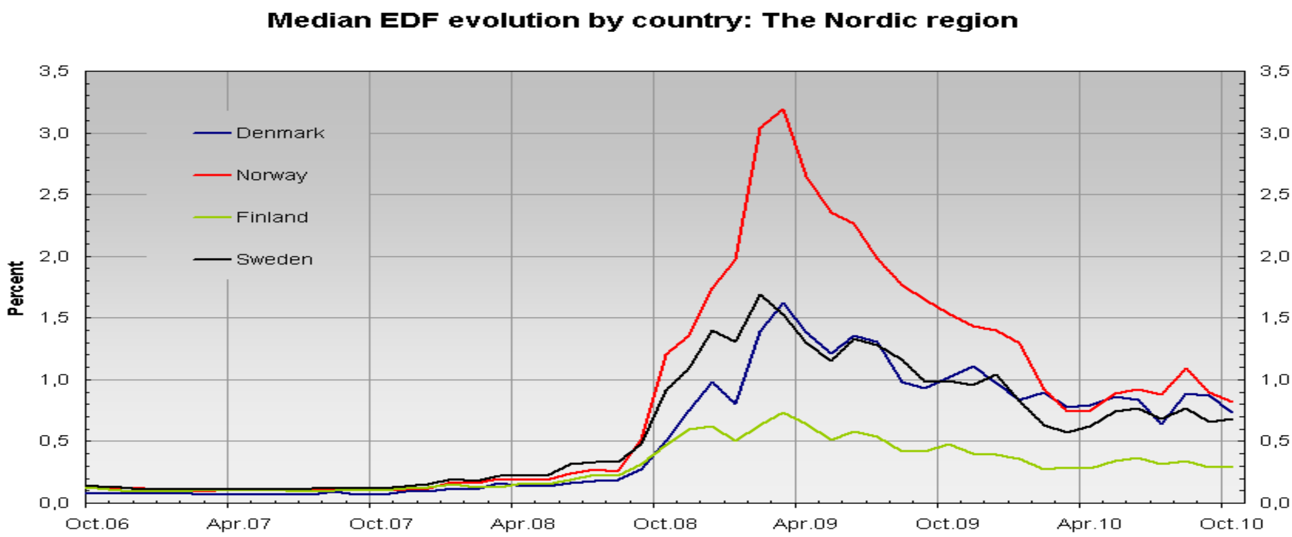
An 8% decrease in bankruptcies in Q3 of 2010

After the record number of bankruptcies in 2009, the trend has reversed this year. According to Statistics Norway, there were 949 bankruptcies in Q3: an 8% year-on-year decrease (see chart overleaf). Of these, 702 related to business failures (excluding sole proprietorships), with one in three of these in the wholesale and retail trade sectors. A third of the sole proprietorship and personal bankruptcies related to the construction sector.



Source: Statistics Norway

However, in September the number of bankruptcies was slightly above that of September 2009, suggesting that the decreasing trend may be levelling off. Winter started early this year and that isn't good news for the construction industry, already hit by last year's adverse weather conditions. In October 2010, the Expected Default Frequency (EDF) indicator for listed companies in Norway stood at 82 basis points: 237 points lower than at its peak in March 2009, but still more than 50 basis points higher than in summer 2008, i.e. before the credit crisis took hold (see chart below).



Source: KMV Credit Monitor and Atradius Economic Research

Short term forecasts for the Norwegian economy are positive, as increasing business investments and higher private consumption are expected, thanks to Christmas activity, lower interest rates and real income growth. Exports will also pick up, but the strength of the Norwegian crown may have a subduing effect on the competitiveness of Norwegian businesses. The Economist Intelligence Unit forecasts GDP growth of 1.1% in 2010 and 1.5% in 2011.

Australia

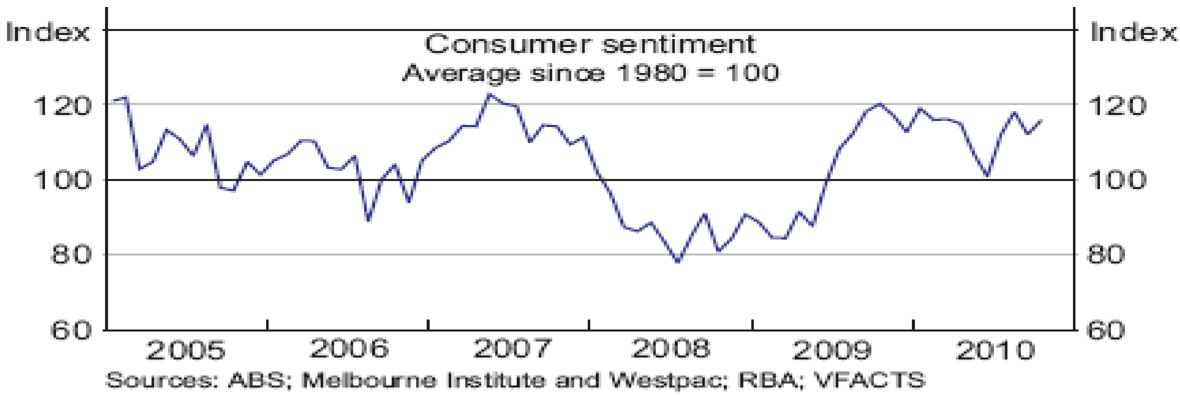
Slower growth in the third quarter

The Australian economy escaped the worst of the global credit crisis, and recovered relatively quickly from a shallow downturn thanks mainly to comprehensive fiscal stimuli and strong demand for commodities from Asia. Prime Minister Julia Gillard has promised to get the fiscal accounts back into a small surplus from 2012-13 and the chances of success are good, with the economy projected to grow strongly (3.4% this year and in 2011) keeping tax revenues buoyant.

According to the Australian Bureau of Statistics, GDP growth in Q3 of 2010 slowed to 0.2% on the previous quarter (but still 2.7% year-on-year), as a stronger currency has hurt exports, while higher interest rates and reduced government stimuli have dampened private consumption and the housing market.

However, employment continues to improve and the unemployment rate is holding steady at around 5.1%. Employment has increased in the professional, scientific and technical services as well as in the mining sector, but in the manufacturing, recreation and arts sectors it remains weak.

Consumer spending has grown a little below trend over the past year. Although surveys report that consumer confidence has been generally high over the last 18 months, consumers are still cautious in their spending. After the big rise in household sector debt over the last 10-15 years, households are now cutting back on debt and spending. This is partly because they realise, after the experience of the credit crisis, that further big increases in debt could leave them vulnerable if their incomes were to fall, and partly because lenders have become more cautious in offering credit.



Business conditions are broadly favourable, although there are considerable variations across industries. While conditions in the mining industry are at their highest since late 2007, those in the construction industry have worsened as the benefits of stimulus-related public building activity fade. Conditions in the tourism industry too have weakened, in part reflecting the appreciation of the AU$.

Business investment is supported by solid internal funding for capital expenditure. However, growth of business loans remains weak, with firms continuing to repay loans while there is little growth in new commercial loan approvals. Conditions are toughest for small businesses, as they are less likely than larger businesses to invest and are also encountering difficulties in accessing finance.

Insolvency level still higher than pre-crisis

According to the Australian Securities and Investment Commission, both the numbers of companies entering external administration and insolvency appointments decreased year-on-year in between January and October 2010: to 6732 and 10810 cases respectively (compared to 7182 and 11121 cases from January to October 2009). However, despite positive macroeconomic conditions in Australia, the number of insolvencies is still higher than pre-crisis times. Australian companies continue to suffer from negative cash flow: the result of the cost of meeting new orders on the one hand and delayed customer payments on the other.

India

The economy continues to grow strongly

India's economy continues to grow strongly (8.9% year-on-year in Q3 of 2010), with domestic demand rising and recovery evident even in those sectors that were most adversely affected by the downturn: notably real estate and textiles.

Infrastructure is attracting considerable levels of investment, with both public and private investors developing India's road network. Improvements to the quantity and quality of India's highways are vital, as freight and passenger traffic on India's roads is expected to increase extensively over the next few years: the latter boosted by higher levels of car ownership by India's burgeoning middle class and the willingness of banks to finance car purchases. The deregulation of petrol prices earlier this year does not appear to have had a major impact on car sales so far.

The telecom sector is also a success story in India, with the total number of mobile phone subscribers now believed to exceed 480 million, and penetration of 60%. However, the sector has recently been beset by allegations of corruption following the award of 2G licences. Moreover, the sector is now crowded with 15 operators vying for business. This has led to a price war and some of the lowest call rates in the world, resulting in poor financial results for many operators. As a consequence, we expect to see some consolidation in this sector in the near future.

The food sector is also expanding rapidly, with many multinational and local companies seeing opportunities for growth. The mass grocery retail sector can expect phenomenal growth provided that distribution infrastructure issues can be resolved and average incomes continue to rise. The downside risks include food price inflation, but these inflationary pressures are expected to ease following a better than expected monsoon in 2010.

Payment experience in India

We received fewer notifications of slow payment in the first half of 2010, and in general our experience of Indian payment performance and commercial morality remains good, with many companies reporting improved results in the year to March 2010. Nevertheless, it remains imperative for suppliers to get up-to-date information on their buyers to satisfy themselves of their buyers' ability to meet trade-related obligations.

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