National Australia Bank

Embargoed until:
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Monthly Business Survey

November 2012

The brakes have firmly tightened on activity in November; business conditions very weak in construction, retail, manufacturing and wholesale. Signs of trouble ahead with confidence slumping to lowest level since April 2009, with little hint of a pre-Christmas revival. Activity forecasts broadly unchanged following release of Q3 GDP. Weakness continues into Q4 – path for interest rates now appears even lower, with one more rate cut likely before the middle of next year.

- Business conditions were unchanged at a very poor level in November, after falling to the weakest level since May 2009 in the previous month. The subdued outcome was fairly broad-based across industries, implying recent rate reductions by the RBA have not yet materialised into stronger demand.
- This month's activity outcome reflected a deterioration in profitability, which was partly offset by a slight pick up in employment conditions – trading conditions were unchanged. Conditions rebounded in wholesale and manufacturing (but remained very subdued) and went sharply backwards in transport & utilities. Six out of eight sectors reported negative conditions.
- Pessimism is the word this month, with business confidence the weakest since April 2009. Confidence did not rise in any sector and fell especially hard in manufacturing. Firms may be concerned about a soft global economy, fiscal tightening, a soft labour market and high AUD.
- Also providing little support for a near-term rebound is the weakness in indicators of future demand. Forward orders, capacity utilisation and stocks all fell to their lowest or equal lowest levels in around 3½ years. Overall, the survey implies a significant slowing in underlying demand and GDP growth in the December quarter, both easing to around 2¼% – clearly below trend.
- Labour costs growth increased a touch in November, but remained relatively soft following three consecutive monthly declines. Purchase costs increased modestly, while product prices grew only marginally, suggesting more pressure on margins. Retail price growth was particularly weak in the month.

Implications for NAB forecasts (See latest Global & Australian forecasts report also released today):

- Although interest rates are historically low in the advanced economies and central banks have stepped up their liquidity injections, their pace of economic growth is still very weak. There is no indication the business environment is about to improve and risks in the US and Euro-zone are depressing confidence. It looks as if growth in the big emerging economies is stabilising. Global growth to remain a sub-trend 3% this year and next.
- Australian GDP growth eased further in Q3, up 0.5%. Outlook broadly unchanged this month; GDP forecasts 2.5% in 2012-13 (was 2.3%) and 2.8% in 2013-14 (was 3.0%). A still elevated AUD, fiscal tightening and very weak confidence expected to weigh on near-term activity. Frictional pressures will keep the unemployment rate elevated. Inflation unlikely to be a barrier to more monetary policy easing in the first half of 2013 (May but February possible). Core inflation (inc. carbon) 2.8% in 2012-13 and 2.9% in 2013-12.

Key monthly business statistics*

	Sep 2012	Oct 2012	**Nov 2012**		Sep 2012	Oct 2012	**Nov 2012**
	Net balance				*Net balance*		
Business confidence	0	-1	**-9**	Employment	-3	-6	**-5**
Business conditions	-3	-5	**-5**	Forward orders	-7	-6	**-11**
Trading	-2	-2	**-2**	Stocks	-1	-2	**-4**
Profitability	-6	-7	**-9**	Exports	-2	-2	**-4**
	% change at quarterly rate				*% change at quarterly rate*		
Labour costs	0.8	0.5	**0.7**	Retail prices	0.4	-0.1	**-0.2**
Purchase costs	0.5	0.6	**0.6**		*Per cent*		
Final products prices	0.1	0.2	**0.1**	Capacity utilisation rate	80.1	80.1	**79.5**

* All data seasonally adjusted and subject to revision. Cost and prices data are monthly percentage changes expressed at a quarterly rate. All other data are net balance indexes, except capacity utilisation, which is an average rate, expressed as a percentage. Fieldwork for this survey was conducted from 19 to 27 November, covering over 600 firms across the non-farm business sector.

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Next release:
29 January 2013 (December monthly)

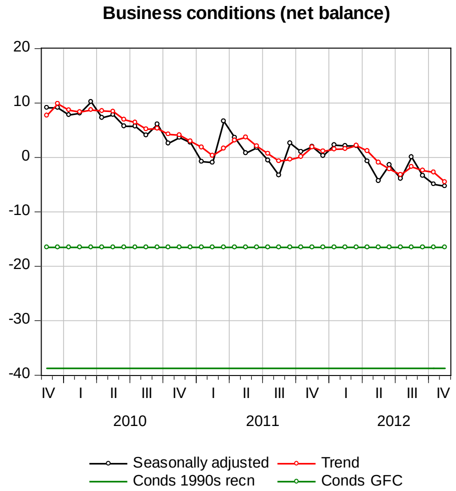
Analysis

Business conditions remained subdued in November – unchanged at -5 index points – with this outcome implying that the economy is clearly growing below trend. Business conditions were particularly challenging in construction, manufacturing and wholesale – despite improving in these industries in the month – and retail. Recreation & personal services and transport & utilities were the only industries to report positive conditions in the month, albeit only marginal. Forward looking indicators of demand signal further weakness still to come, with forward orders, capacity utilisation and stocks falling to their weakest or equal weakest levels since mid-2009.

The business conditions index is currently 10 points below its medium-term average (since 1997 for the Monthly Survey) of +5 index points. Over the time period of the full Quarterly Survey (since 1989), conditions are 6 points below the long-run average (of +1 point).

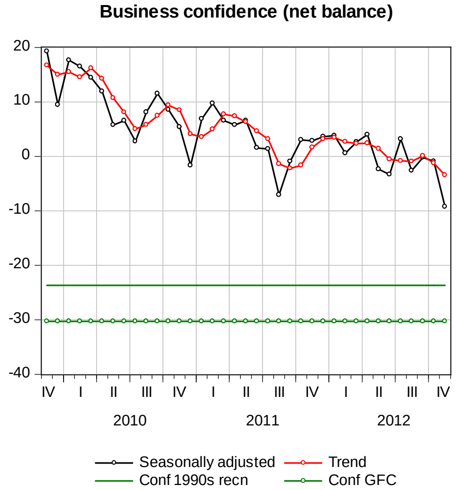
Business confidence slumped heavily in November, falling from -1 point to -9 index points, the weakest level since April 2009. The slump in confidence is likely to in part reflect businesses becoming depressed about the weak level of activity in the economy at present, while concern about the outlook for Australia's mining sector may also be playing a part. Furthermore, conditions overseas probably continue to concern business, for example, the extent of tax increases and spending cuts likely in the US next year, which are commonly referred to as the 'fiscal cliff'. Businesses still appear reluctant to borrow despite a run of rate cuts over the past year (this survey was conducted prior to the RBA's December Board meeting, when it lowered the cash rate by 25 bps to 3%). Confidence is now 15 points below the series long-run average level (of +6 points).

Conditions still subdued with no improvement in sight



Average of the indexes of trading conditions, profitability and employment.

Confidence slumped to 3½ year low



Excluding normal seasonal changes, how do you expect the business conditions facing your industry in the next month to change?

Business conditions by industry. Business conditions deteriorated heavily in transport & utilities, after being the stand out performer for the previous four months. Conditions also fell back moderately in mining, retail and recreation & personal services. In contrast, conditions improved firmly in wholesale, manufacturing and construction, though this followed even sharper declines in the previous month and the overall level of conditions in these industries remains very poor. Mining conditions have deteriorated markedly, down from an average of +26 index points over the first half of this year, to be -1 index point in November, 12 points below the medium-term average for this series (+11 points since 1997).

Business conditions by state. Conditions weakened notably in WA, SA and Queensland in November – the states more heavily exposed to mining. In contrast conditions improved a touch in NSW and Victoria. Business conditions were negative in all states in the month, with worryingly poor activity levels recorded for Queensland, which is likely to be feeling the pinch from the still high AUD, as well as the recent decline in commodity prices. Trend conditions in Tasmania improved modestly, to marginally positive territory (care should be taken when interpreting these data due to small sample size).

Analysis (cont.)

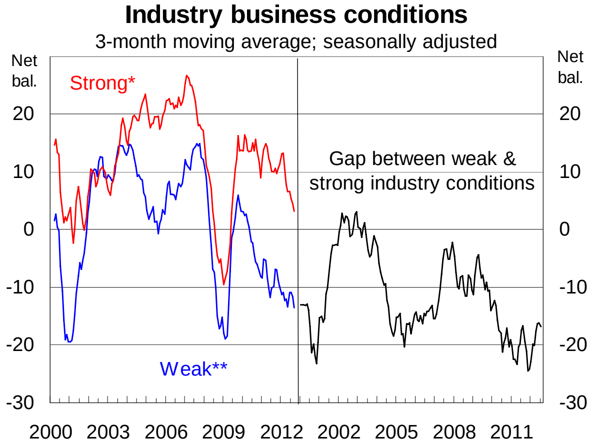
Business confidence by industry. Confidence fell across all industries the month, with the exception of construction, where it was unchanged at a subdued level. Manufacturing reported the most significant decline, while confidence was also shaken considerably in transport & utilities and recreation & personal services. There are no signs of near-term optimism, with all industries expecting activity to deteriorate further (as implied by negative confidence readings). Confidence remained weakest in mining, reflecting concerns about the outlook for the Chinese economy and therefore commodities demand. Recent RBA rate cuts appear to have done little to lift confidence.

Business confidence by state. Confidence deteriorated across all states, with particularly heavy falls reported in WA and SA. WA is now the most pessimistic state, while sentiment in SA, Victoria and NSW is not much better. All states expect activity to deteriorate in the near term. Trend confidence actually improved marginally in Tasmania (on a small sample), to a level implying a slightly better near-term outlook.

Variation in business conditions across sectors has become quite pronounced since late 2009, although the gap has narrowed over the second half of this year. This can be observed by comparing trend conditions of the recently strongest performing sectors (mining, transport & utilities, recreation & personal services and finance/ business/ property) with trend conditions of the weakest performing sectors (retail, manufacturing, construction and wholesale).

The persistent divergence in industry conditions indicates that the Australian economy is undergoing a structural transformation towards mining and service-based industries, and away from traditional manufacturing and discretionary retailing. However, the recent softening in mining conditions may restrain the pace of this restructuring.

Economy undergoing structural transformation



* Strong industries include mining, transport & utilities, recreation & personal services and finance/business/property
** Weak industries include retail, manufacturing, construction and wholesale

The **forward orders** index fell heavily in November – down 5 to -11 points – falling to its lowest level since May 2009. The deterioration in orders was most apparent in mining – where orders were weakest – and manufacturing. In contrast, orders improved solidly in construction and they were modestly better in transport and utilities, where they were least subdued. The net balance of orders was negative in every sector in November. Consistent with weakness in orders, **capacity utilisation** also fell to 79.5%, its lowest reading since April and the equal lowest since June 2009. Even more concerning was the very low level of utilised capacity in manufacturing – at 74.3%, this month's outcome is only 2 percentage points higher than the series all time low, which was recorded in July this year. Overall, capacity utilisation was highest in transport & utilities, recreation & personal services and retail, while it was lowest in manufacturing and mining. The **stocks** index fell back in November (down 2 to -4 points), which is 9 points lower than the level just three months earlier. This outcome suggests firms may have reduced their stock accumulation in response to the poor outlook for trading conditions, as indicated by very weak forward orders. The stocks series has in the past tended to move pro-cyclically and as such, adds weight to the general weak tone of the survey.

The **capital expenditure** index rose a touch in November – up 4 to zero points – partly unwinding a modest fall in the previous month. The improvement in the month largely reflected a sharp rise in transport & utilities, as well as modest rises for finance/ business/ property and wholesale. This was partly offset by a significant fall in the capex index for construction, partly unwinding a solid rise in the previous month. In levels terms, capital expenditure was highest in recreation & personal services (+9 points) and finance/ property/ business (+7), while it was lowest in construction (-15), manufacturing (-14) and transport & utilities (-7). The capex index for mining has gradually softened from +25 points in June this year to -4 points in November; while this outcome is close to the industry average, the deterioration highlights the extent of softening taking place in the mining sector at present.

Analysis (cont.)

Assuming that average forward orders over the first two months of the December quarter continue into the month of December, the survey implies 6-monthly annualised demand growth will remain subdued, at close to 2¼% in the December quarter (down from 2¾% last month), following growth of 2.0% in the September quarter.

Similarly, if we assume that the average of business conditions over the December quarter to date persist into the month of December, the survey implies 6-monthly annualised GDP growth (ex mining) will be a subdued 2¼% (6-monthly annualised and similar to last month) in the December quarter, 2.1%.

Elsewhere in the survey, cash flow (not seasonally adjusted) was strongest in recreation & personal services and transport & utilities, and weakest in manufacturing.

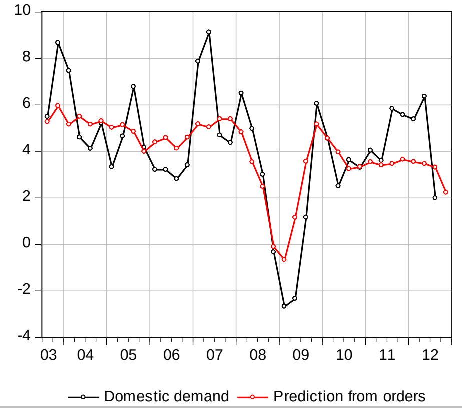
Labour costs growth (a wages bill measure) rose by 0.2 ppts to 0.7% in November (at a quarterly rate), following three consecutive months of declines. While costs pressures picked up in the month, the overall pace of labour costs growth remains low compared to recent history, and is consistent with fairly soft labour market conditions. The rise in labour costs pressures was broad based; costs pressures increased modestly in finance/ business/ property, retail, construction and manufacturing, while transport & utilities and wholesale were the only two industries to report a softening in costs growth. Overall, labour costs growth (at a quarter by rate) was strongest in recreation & personal services (1.1%) and transport & utilities (0.9%), and softest in wholesale, manufacturing and mining (all 0.3%).

Price inflation weakened a touch in November (down 0.1 ppts to 0.1%; at a quarterly rate). The rate of inflation implied by the survey remains very soft, with subdued domestic demand and a still high AUD likely to be keeping prices contained. Mining price growth fell very sharply in the month, consistent with a general softening in commodity prices. In contrast, price pressures rose slightly in construction, transport & utilities and manufacturing. Growth was least subdued in transport & utilities (+0.4%) and recreation & personal services (+0.3%), and weakest in mining (-0.6%), retail (-0.2%) and construction (-0.1%).

Purchase cost pressures were unchanged in November at 0.6% (at a quarterly rate). Across industries, purchase cost pressures eased modestly in retail, construction and transport & utilities (all 0.4 ppts softer), while they increased solidly in finance/ business/ property (up an additional 0.6 ppts). Purchase costs growth was strongest in recreation & personal services (1.0%; at a quarterly rate), while it was broadly similar across the remaining industries, ranging between 0.3% and 0.5%.

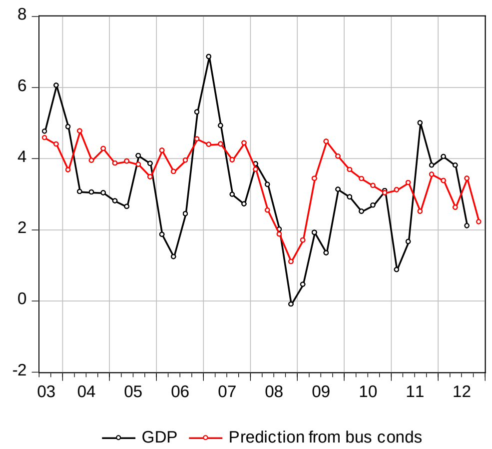
Demand growth to remain subdued

Forward orders (change & level) as an indicator of domestic demand (6-monthly annualised)



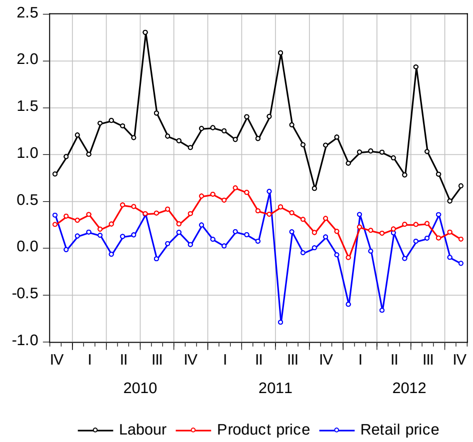
GDP (ex coal) growth to weaken in Q3, partly unwinding H1 strength

Business conditions (change & level) as an indicator of GDP (6-monthly annualised)



Labour cost pressures tick up but still soft

Costs & prices (% change at a quarterly rate)



Based on respondent estimates of changes in labour costs and product. Retail prices are based on retail sector product price estimates.

Current business conditions

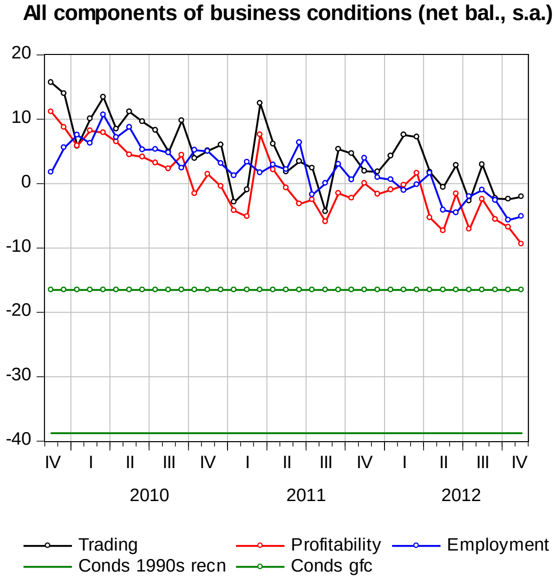
The business conditions index was unchanged at -5 index points in November, following a modest fall in the previous month. In trend terms, business conditions deteriorated a little – down 2 points to -5 index points, which is clearly below the series long-run average (of +1 point).

Trading, profitability and employment

This month's outcome reflected a slight deterioration in profitability, which was entirely offset by a marginal rise in employment conditions; trading conditions were unchanged.

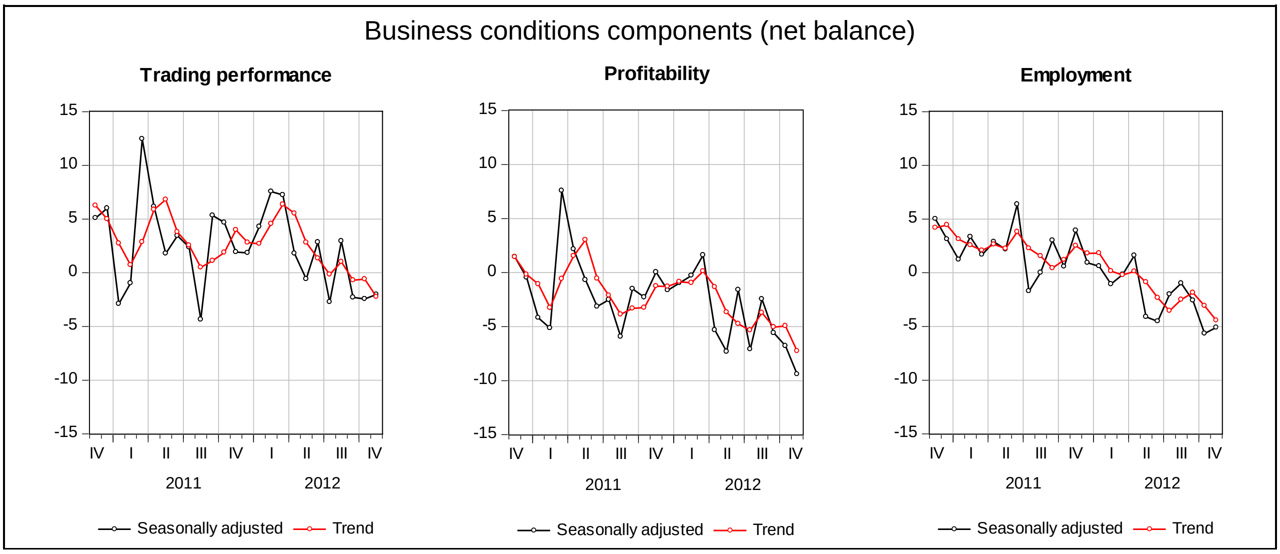
Employment conditions improved across all industries in November, with the exception of transport & utilities, where they deteriorated heavily (down 22 to -3 points), and retail, where they were a touch softer. The most notable improvements in employment conditions were reported in manufacturing (up 9 to -10 points) and recreation and personal services (up 6). In levels terms, employment conditions were weakest in wholesale (-12), manufacturing (-10) – despite a solid improvement – and construction (-9), while they were least subdued in recreation & personal services (+2) and finance/ business/ property (+1).

Profitability weakens but offset by a slight rise in employment



Net balance of respondents who regard last month's trading / profitability / employment performance as good.

Profitability rebounded solidly in wholesale (up 22 points) and manufacturing (up 14), while it weakened considerably in transport & utilities (down 13) and recreation & personal services (down 10). In levels terms, profitability was weakest in construction (-19), manufacturing (-16) and retail (-15), while it was least subdued (and positive) in transport & utilities (+3) and recreation & personal services (+2).



Net balance of respondents reporting trading performance / profitability / employment as good or very good (rather than poor or very poor).

Current business conditions (cont.)

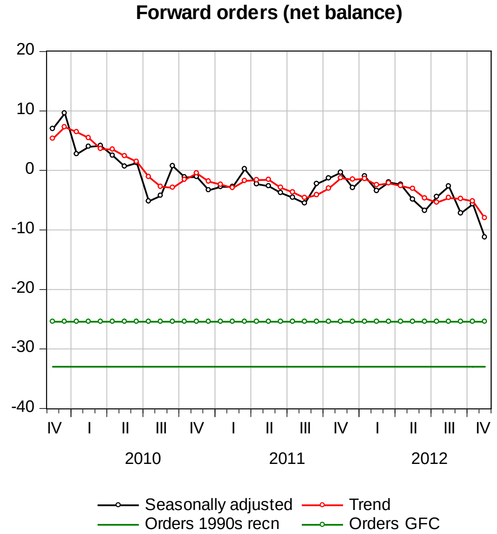
Forward orders

In October, the forward orders index – an indicator of domestic demand – moderated sharply in November – down 6 to -11 points, the weakest outcome since May 2009. This outcome is consistent with the general weakness in trading conditions over the past three years.

The weakness in orders in November reflected heavy declines in mining and manufacturing orders. In levels terms, negative orders were recorded across all industries, with the weakest outcomes in mining (-15), wholesale (-14), manufacturing (-13) and retail (-12).

Net balance of respondents with more orders from customers last month.

New demand wilts under weak trading conditions

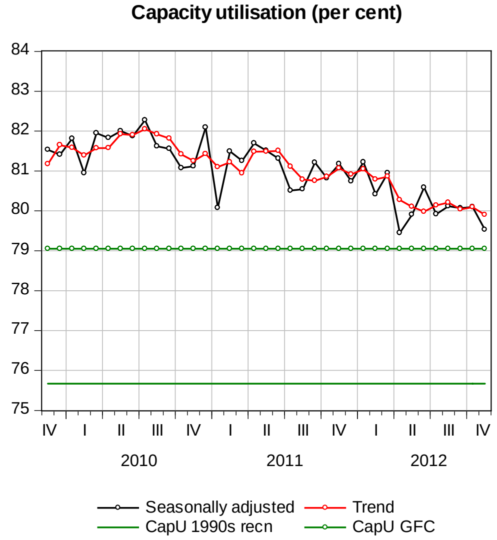


Capacity utilisation

Capacity utilisation eased to 79.5% in November, down from 80.1% in the previous month, a relatively low outcome compared to recent history. In the month, utilised capacity fell noticeably in transport & utilities (down 2.2 ppts), finance/ business/ property (down 1.5 ppts) and manufacturing (down 2 ppts), while it rose solidly in recreation & personal services (up 1). In levels terms, capacity utilisation was highest in transport & utilities (83.4%) and recreation & personal services (80.9%) – the two best performing industries according to activity levels – followed by retail (80.6%) and wholesale (80.3%). Manufacturing was at the other end of the spectrum, with capacity utilisation of just 74.3%.

Full capacity is the maximum desirable level of output using existing capital equipment.

Capacity utilisation falls sharply



Current business conditions (cont.)

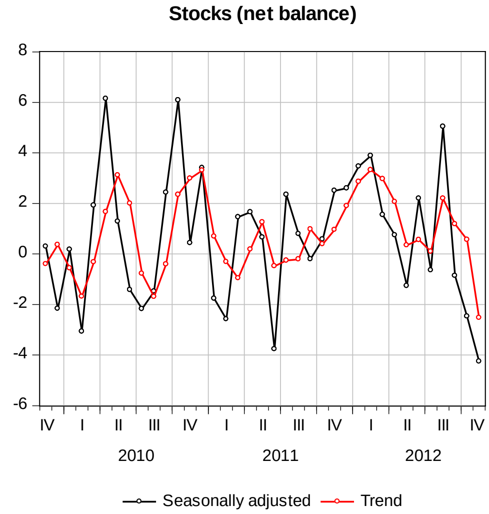
Stocks

The stocks index fell further in November, consolidating two consecutive months of declines: the index fell from -2 points to -4 index points. Stocks remained below the series long-run average (of +1 point since 1989). It appears that the weakness in near-term indicators of domestic demand has led firms to begin de-stocking.

The deterioration in stocks largely reflected falls in construction (down 8), finance/ business/ property (down 7) and transport & utilities (down 3), which was partly offset by a solid rise in manufacturing stocks (up 12). In levels terms, the stocks index was lowest in construction and transport & utilities (both -12) and finance/ business/ property (-8), and was highest in retail (+4) and mining (+1).

Net balance of respondents with a rise in stocks last month

De-stoking accelerates



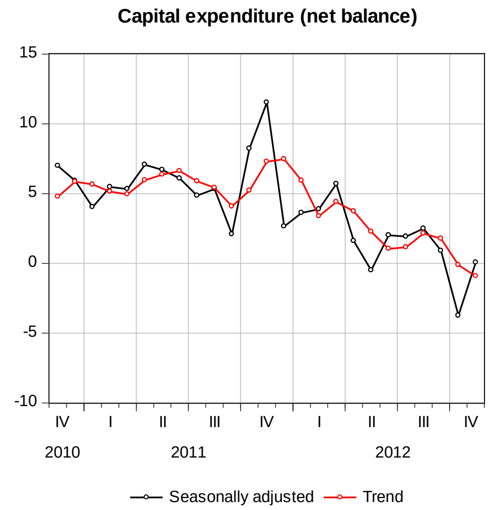
Capital expenditure

Capex bounced back in November – up 4 to zero – after recording its lowest level in October since August 2009. The softening in mining activity appears largely responsible for the general softening in capital expenditure, led by a generally softer outlook for global commodities demand. Mining capex has eased from a recent peak of +36 points in March 2012 to -4 points.

The capex index deteriorated heavily in construction (down 13), followed by mining (down 6), while it improved solidly in transport & utilities – after deteriorating very sharply in the previous month. In levels terms, capex was highest in recreation & personal services (+9) and lowest in construction (-15) and manufacturing (-14).

Net balance of respondents with an increase in capital expenditure last month.

Capex up but still low relative to history



Exports

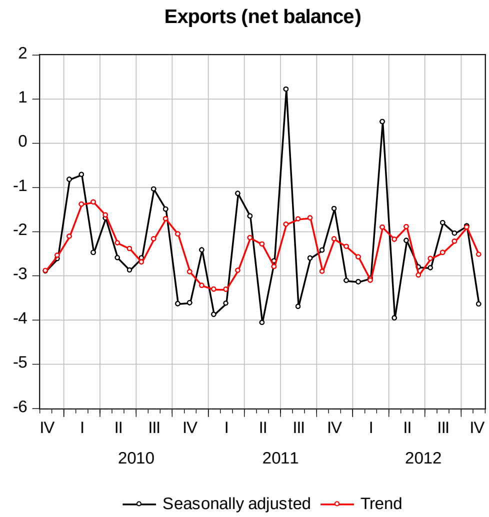
The exports index, which represents export conditions for the economy as a whole, fell back in November – down 2 to -4 index points.

By industry, the exports index fell heavily in wholesale (down 6), followed by construction (down 5). Exports improved modestly in mining, partly unwinding a significant decline in the previous month – this outcome is consistent with a partial recovery in demand for commodities. In level terms, the exports index was lowest in manufacturing (-8), while it was highest in mining and transport & utilities (both zero).

The exporters' sales index, which represents export conditions for exporting industries, also fell in the month – down 6 to -15 points.

Net balance of respondents with an increase in export sales last month.

Exports falter – perhaps due to high A$



Current business conditions (cont.)

Credit availability

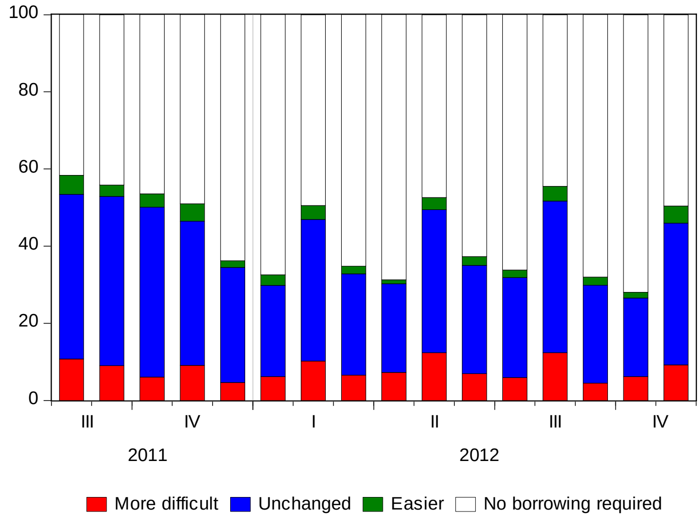
Firms reported that borrowing conditions remained difficult in November. However, demand for credit strengthened, possibly in response to lower borrowing costs.

The net borrowing index (easier minus harder) was unchanged at a relatively low -5 index points in November. This month's outcome reflected a rise in the proportion of firms finding borrowing more difficult to obtain, which was entirely offset by an increase in firms reporting that finance was easier to obtain. The proportion of businesses requiring finance rose significantly from 28% to 50%; while it appears that businesses have little desire to undertake investment at present (as highlighted by a low capex index), it is possible that businesses may need to borrow funding simply for general upkeep of existing capital, which may explain part of the increase in demand for credit in November.

In terms of the borrowings required for your business in the last month, has it been …

Demand for credit strengthens but borrowing conditions still difficult

Borrowing conditions (% of firms)



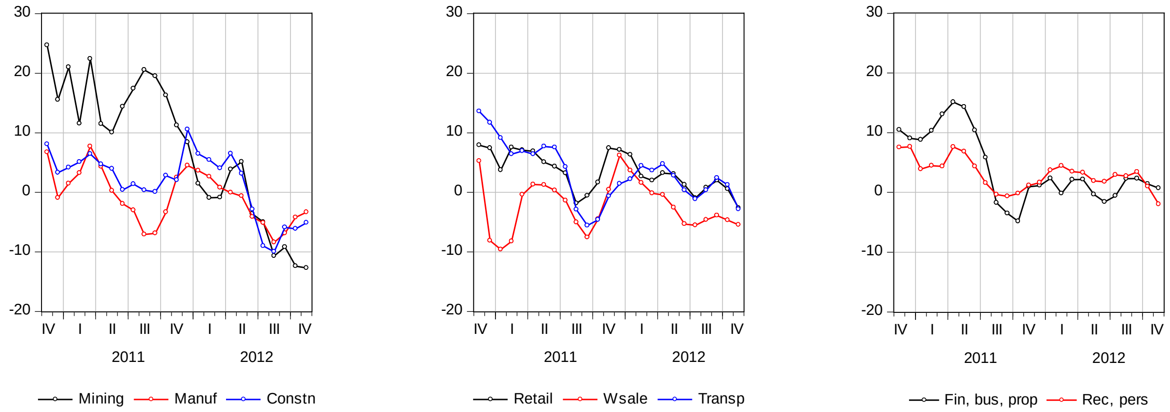
Industry sectors

Business confidence *Pessimism's the word: Miners particularly concerned*

Business confidence deteriorated across all industries in November, with the exception of construction, where it was unchanged. The most notable deterioration in confidence was in manufacturing (down 13 to -9 points), followed by transport & utilities and recreation & personal services (both down 9). Confidence was subdued in all industries, with no industry expecting an improvement in activity in the month ahead (eg. no industry reported a positive net balance). Mining was the least confident in the month (-16) – consistent with the general softening in commodity prices and weaker outlook for global demand – followed by manufacturing, construction, transport & utilities (all -9), wholesale and recreation & personal services (both -8). Confidence was least subdued, albeit still very poor, in finance/ business/ property (-3) and retail (-7). In aggregate, these outcomes imply businesses are feeling quite uneasy about the outlook for activity in the lead up to the Christmas holiday season.

Business confidence by industry (net balance)

3-month moving average

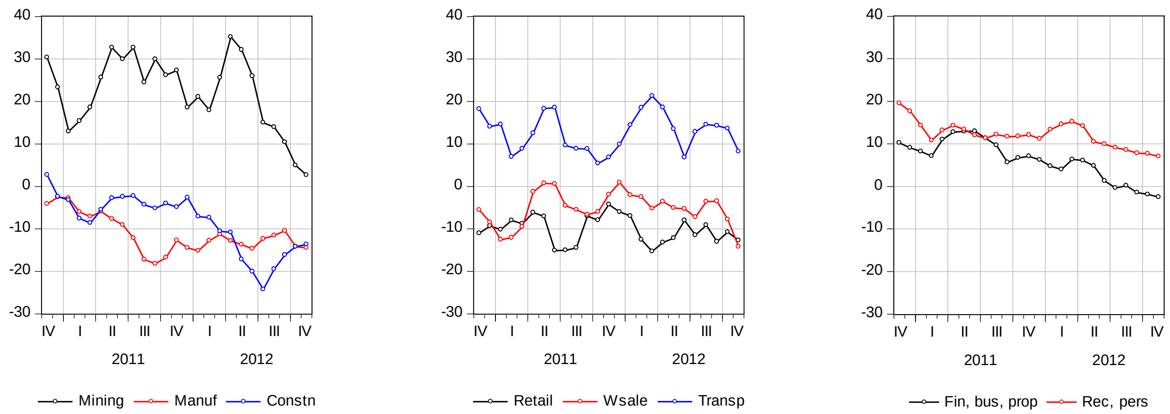


Business conditions *Conditions very bad in construction, retail, manufacturing & construction. Recreation & transport least subdued*

Movements in industry conditions were fairly mixed over the month. Conditions strengthened significantly in wholesale (up 17), manufacturing (up 11), and to a lesser extent, construction (up 4), though these improvements merely reflected a rebound from particularly weak outcomes in the previous month. Industry conditions deteriorated heavily in transport & utilities (down 13) – with activity appearing much weaker this month compared to the relative strength this industry has enjoyed most of this year. Conditions also deteriorated modestly in mining, retail and recreation & personal services (all down 4). Overall, conditions were weakest in construction (-14), retail (-13), manufacturing (-11) and wholesale (-10), and were least subdued in recreation & personal services (+4) and transport & utilities (+1).

Business conditions by industry (net balance)

3-month moving average

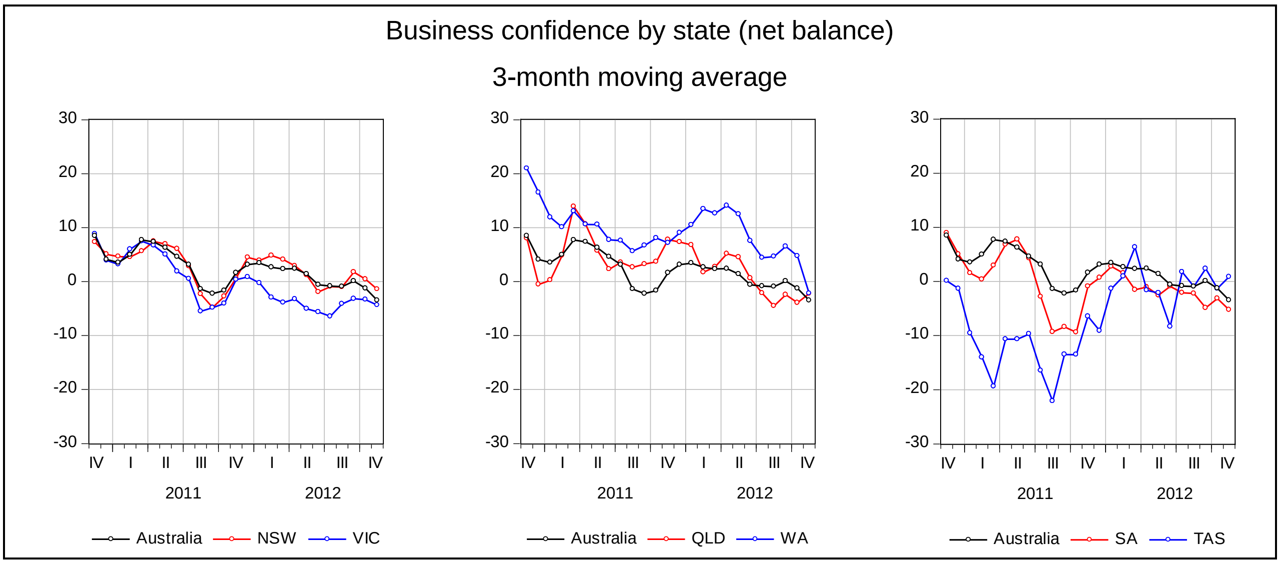


States

Business confidence

Confidence weakens across the mainland states, WA and SA particularly pessimistic.

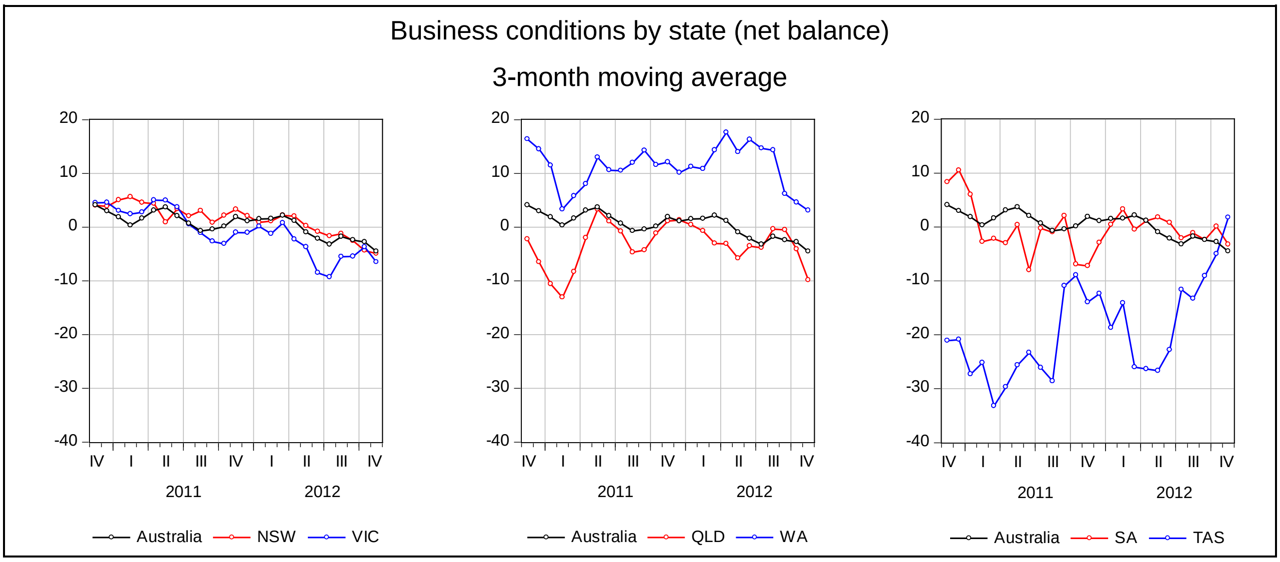
Business confidence deteriorated across all of the states in November, with particularly large falls reported in WA and SA. While the general mood by region is gloomy, the weakness in sentiment is particularly embedded in WA, where concern about the outlook for the mining sector – which contributes around one third of the state's production – is weighing heavily. Confidence in the month was weakest in WA (-12), followed by SA (-9), Victoria and NSW (both -8), while it was least subdued in Queensland (-4). Trend confidence improved a touch in Tasmania, up 2 to +1 point – while this outcome is positive, it still points to little improvement in the near term (care should be taken when interpreting data for this state given the relatively small sample of respondents included in the survey).



Business conditions

Conditions extremely poor in Queensland; WA continues to outpace all other states, but only just

Business conditions deteriorated heavily in WA (down 9) and SA (down 8) in November, and they were moderately weaker in Queensland (down 4 to -16), where they were the most subdued overall. The weakness in Queensland activity is likely to reflect lower commodity prices, weakness in the domestic tourism industry due to a still high AUD, while public sector cut backs are also likely to be playing a part in the overall weakness in this state. Conditions in SA (-6) and Victoria (-4) were also poor, while activity was least subdued in WA (-2) and NSW (-3). In Tasmania, trend conditions improved solidly (up 7 to +2 points; on a small sample).



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