

**Monthly Business Survey**
**July 2013**

**Business conditions remain at 4 year lows while confidence slumps to 8 month low – despite a falling AUD and lower interest rates. Conditions very poor in manufacturing, construction, mining, retail and wholesale; WA now the weakest state. Forward orders, stocks and employment still very poor. Weaker AUD hurting wholesale and retail purchase costs but weak activity sees this reflected in lower profits not higher prices.**

- The weakness in activity that has persisted for several months continued in July, with business conditions unchanged at their lowest level since May 2009. Slightly better trading and employment conditions were offset by deteriorating profitability, with the latter index falling to a 4½ year low. Conditions were especially weak in manufacturing – despite the lower Australian dollar – construction, mining and retail (albeit the latter did see better sales in July). Forward indicators provide little hope that demand will improve in the near term, with forward orders, stocks and capacity utilisation all remaining well below long-run average levels.
- Business confidence fell to the lowest level since November 2012, with a falling dollar and the lure of lower interest rates unable to lift the mood of businesses in July. Rather, it is likely that the weakness in business activity and profitability (via the inability to pass on higher costs) is the key driver of weaker confidence. Confidence also remains extremely poor in mining – with broader flow on implications in WA. Only retail/wholesale reported better confidence levels (on the back of better retail sales). It is also possible that uncertainty over timing of the Federal election kept businesses wary during the month (the survey was completed prior the election being called).
- Overall, the survey implies underlying demand growth and GDP (6-monthly annualised) of around 2½% in the June and September quarters. Our wholesale leading indicator implies little improvement in near-term activity.
- Labour costs growth surged in July, despite still weak employment conditions; the implementation of a higher national minimum wage on 1 July is probably largely responsible for this rise. Prices fell again (retail prices rose a touch), but purchase costs rose sharply in wholesale and retail possibly reflecting higher import prices.

**Implications for NAB forecasts** (See latest [Global and Australian Forecasts](#) report also released today):

- Global forecasts remain unchanged (3% in 2013 and 3.6% in 2014). That said, business surveys and industrial data point to an upturn in growth in advanced economies, possibly heralding a shift in the drivers of growth away from emerging markets and towards advanced economies. While US growth is lower, an accelerating trend is expected to see “tapering” begin in coming months. Against that, business surveys, trade and industry data and GDP releases show a softening trend in the emerging markets – with China expected to slow further.
- Further signs Australian growth is grinding lower. We see GDP growth softening to 2.2% in 2013, before rising to 2.6% in 2014, and a significant deterioration in the labour market is expected this year (unemployment above 6%) and next. Our forecasts have been revised a touch lower – with downside risks building. When combined with still low inflation, we expect another RBA cut, probably in November, and more cuts may follow. We remain a touch more bearish than recently revised (down) forecasts from the Government and the RBA.

**Key monthly business statistics\***

	May 2013	Jun 2013	Jul 2013		May 2013	Jun 2013	Jul 2013
	<i>Net balance</i>				<i>Net balance</i>		
Business confidence	-1	0	<b>-3</b>	Employment	-6	-6	<b>-5</b>
Business conditions	-4	-7	<b>-7</b>	Forward orders	-6	-5	<b>-6</b>
Trading	-1	-7	<b>-4</b>	Stocks	-1	-5	<b>-5</b>
Profitability	-6	-9	<b>-11</b>	Exports	-3	-1	<b>-2</b>
	<i>% change at quarterly rate</i>				<i>% change at quarterly rate</i>		
Labour costs	0.8	0.7	<b>1.3</b>	Retail prices	-0.1	0.3	<b>0.2</b>
Purchase costs	0.6	0.4	<b>1.2</b>		<i>Per cent</i>		
Final products prices	-0.1	-0.2	<b>-0.1</b>	Capacity utilisation rate	79.6	79.3	<b>79.9</b>

\* All data seasonally adjusted and subject to revision. Cost and prices data are monthly percentage changes expressed at a quarterly rate. Fieldwork for this survey was conducted from 25 to 31 July, covering over 400 firms across the non-farm business sector.

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Next release:

10 September 2013 (August monthly)

## Analysis

**Business conditions** were unchanged at a subdued -7 points in July, consolidating a fairly weak set of activity readings this year (with business conditions averaging -6 points over 2013 to date). The persistent weakness in the domestic economy implied by this survey further validates the RBA's decision to lower the cash rate to 2.50% on 6 August. While solid improvements in business conditions were reported in retail, mining and recreation & personal services, these gains were largely offset by weaker conditions in finance/ business/ property, construction and transport & utilities. The still weak set of industry conditions suggests the lower Australian dollar is providing little support to activity domestically – especially in the trade dependent manufacturing industry, which experienced the weakest conditions since March. Forward looking indicators of activity suggest little near-term revival in business conditions, with forward orders, employment conditions, stocks and capacity utilisation all remaining well below long-run average levels.

**Business confidence** fell to -3 points in July – the lowest level since November 2012 – down from zero points in June. Confidence remained especially lacklustre in mining, where businesses seem pessimistic about the outlook for investment in the face of slowing global demand and softening commodity prices, despite a lower Australian dollar. After showing signs of improvement at the beginning of this year, construction firms again seem worried about the poor outlook for investment. Not even a falling dollar has been able to revive hopes for manufacturers. The only sectors to report better confidence were in retail and wholesale, where conditions improved in July and the prospect of lower rates may be helping.

It is also possible that uncertainty around the timing of the Federal election may have weighed on confidence at the time the survey was conducted. The survey was conducted prior to the Federal Government's announcement that the election will be held on 7 September so provides no evidence about the business reaction.

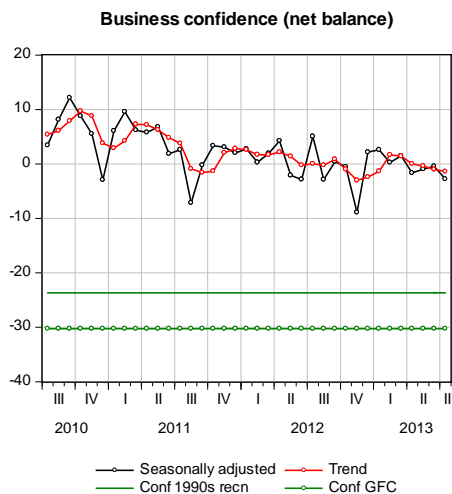
**Business conditions by industry.** Business conditions weakened considerably in finance/ business/ property (down 15 to -3 points) and construction (down 11 to -18 points), reversing promising upward trends. While only a touch softer, manufacturing conditions were especially weak in July, even in the face of a much lower Australian dollar, which should eventually help this sector become more competitive globally. Retail conditions strengthened but remained poor (up 14 to -12 points), with the weakness in this industry consistent with the soft official retail trade data. Conditions were also poor in construction and mining, where weak investment activity and intentions appear to hindering activity. The one shining light in July was the relative strength in recreation & personal services, with conditions in this industry rising solidly (up 10 to +11 points); it is possible that consumers are limiting travel abroad in response to the weaker Australian dollar and instead spending on recreational services domestically. Overall, conditions were weakest in manufacturing (-26), construction (-18), mining (-15) and retail (-12), while they were strongest (and positive) in recreation & personal services (+11), followed by transport & utilities and finance/ business/ property (both -3). The general weakness in activity across industries suggests that growth in the domestic economy has stalled.

### Conditions remain lacklustre



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

### Confidence: the lowest its been all year



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

## Analysis (cont.)

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**Business conditions by state.** There has been a clear downturn in WA business conditions, which have gradually deteriorated from -4 points in April to -13 points in July, to be 42 points lower than the most recent peak in June last year. Clearly, the mining investment slowdown is having a wider impact on the economic performance of WA. In trend terms, conditions also softened in Queensland, while conditions improved in SA, NSW and Victoria. Trend conditions were most subdued in WA (-10), SA (-9) and Queensland (-8), and least subdued (albeit still very poor) in Victoria (-3) and NSW (-5).

**Business confidence by industry.** Consistent with a deterioration in conditions, construction and manufacturing lost confidence in July. While a lower Australian dollar may be expected to improve sentiment in the manufacturing sector, it may be the case that manufacturers remain nervous about whether the dollar will remain low. For construction, it is possible that the weakness in the non-mining economy and perhaps some hesitation in the lead up to the Federal election are weighing on confidence in this industry. Retail and wholesale firms actually became more confident in July, which is consistent with rises in sales and capacity utilisation. Confidence in mining was the weakest of all industries (-23), with this industry clearly very concerned about the outlook for mining activity. Elsewhere, confidence was also poor in construction (-7), manufacturing and wholesale (both -6), while it was least subdued in retail (zero), finance/ business/ property (-1) and recreation & personal services (-2).

**Business confidence by state.** Trend business confidence weakened marginally in Queensland, NSW and WA – the three largest mining states – while it was unchanged in Victoria and SA. The overall level of trend confidence was broadly similar across the states, ranging from -5 in Victoria to zero in Queensland.

The **forward orders** index eased slightly in July, to -6 points, to be 6 points below the series long-run average since 1989. In levels terms, orders were particularly weak in mining (-18) – despite a solid improvement in the month – wholesale (-18) and manufacturing (-10). Orders were least subdued in construction (-1), retail and recreation & personal services (both -3). **Capacity utilisation** rose moderately in July, up 0.6 ppts to 79.9%, after falling to the lowest outcome in four years in the previous month. The pick up in utilised capacity was largely driven by wholesale and retail firms, while partly offsetting declines were reported in mining and manufacturing, where capacity utilisation was very low at 73.2% and 71.4% respectively. Capacity utilisation also fell in construction but remains above average at 80.5%. The **stocks** index – also a good indicator of current demand – was unchanged at a low -5 points in July. When combined with weakness in trading activity in the month, the negative stocks index implies a degree of voluntary de-stocking in the face of a soft outlook for demand.

The **capital expenditure** index lifted from -3 points in June, to -1 point in July. The still negative reading implies that investment activity remains subdued. The trend in mining capex remained poor, despite posting a significant improvement in the previous month. Elsewhere, investment was also subdued in manufacturing, with weakness in this industry likely to be limiting new capital spending. In contrast, capex was relatively strong in recreation & personal services (+7) and transport & utilities (+6) – consistent with relatively stronger conditions in these industries. At the time this survey was conducted, a Federal election date was yet to be determined, which may have been negative for capex plans.

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## Analysis (cont.)

Based on forward orders, the survey implies 6-monthly annualised demand growth was around 2¼% in Q1 2013, much higher than the actual rate of -0.2%. Based on forward orders from the Quarterly Business Survey, 6-monthly annualised demand growth is predicted to be around 2¼-2½% in Q2 2013. If we assume July forward orders from the Monthly Survey are continued into the September quarter, the implied growth rate would be around 2½%. That is, a little stronger than Q1 growth but still below trend.

Similarly, based on average business conditions for Q1 2013, the survey implies 6-month annualised GDP growth (excluding mining) of around 3-3¼% in Q1 2013, somewhat higher than actual growth of 2¼%. Based on Q2 business conditions from the Quarterly Survey, the survey implies GDP growth of around 2¾% in Q2. Assuming July business conditions are continued into the September quarter, implied growth would slow to around 2½%.

Elsewhere in the survey, cash flow (not seasonally adjusted) was strongest in recreation & personal services and finance/ business/ property, and weakest in manufacturing, mining and construction.

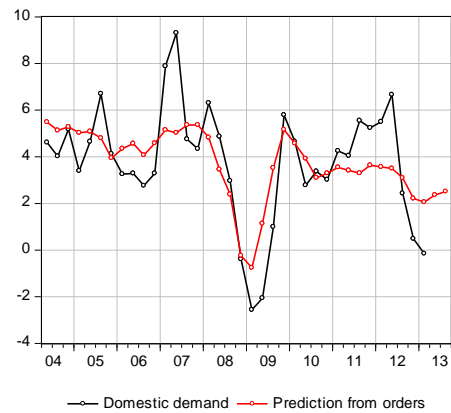
**Labour costs** growth (a wages bill measure) strengthened considerably to 1.3% in July, from 0.7% in June (at a quarterly rate). With employment conditions still negative, the sharp up-tick in costs growth appears to reflect the 2.6% increase in the national minimum wage, which came into effect on 1 July 2013. The increase was particularly apparent in retail – an industry where employee pay is more likely to be set by (or linked to) minimum wage decisions. Labour costs growth was strongest in retail (2.5%, quarterly) and recreation & personal services (1.2%), while costs fell by 0.2% in mining.

**Purchase cost** growth increased significantly to 1.2% in July (at a quarterly rate). There is emerging evidence that the lower AUD has boosted import prices, highlighted by a sharp rise in wholesale purchase costs (up 3.7%, quarterly) – the strongest pace of growth of any industry. Elsewhere, purchase costs growth was relatively high in retail (1.9%) and manufacturing (1.2%), but softest in mining and recreation & personal services (both 0.4%).

**Final product prices** fell by 0.1% in July (at a quarterly rate), the third consecutive monthly decline. While the currency depreciation will take time to flow through to higher prices, there is little sign that businesses have passed on costs associated with the lower dollar at this stage. While price growth lifted modestly in wholesale, it remained well below the rate of purchase costs growth, implying margins are being squeezed. Inflation was highest in wholesale (1.0%, quarterly) and recreation & personal services (0.9%), while price deflation was most apparent in mining (-1.0%), and finance/ business/ property (-0.5%). Retail prices increased modestly (0.2% quarterly rate).

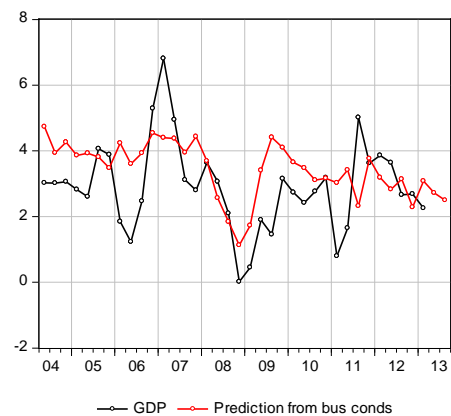
### Demand growth to stay below trend

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



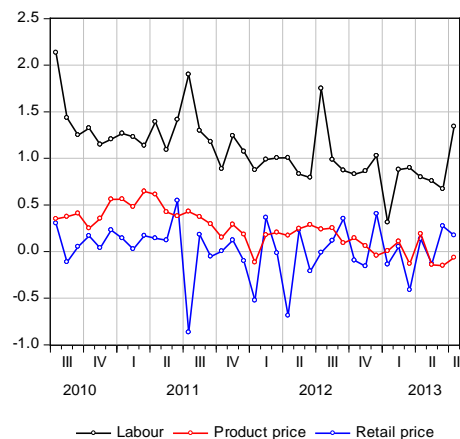
### Little sign of a near-term recovery in GDP growth

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



### Prices fall again – a sharp rise in cost growth implies even tighter margins

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 a very subdued -7 points in July. This outcome is marginally weaker than the series average of -6 points over 2013 to date, and but significantly weaker (-7 points) than the long run average business conditions of 0 points (since 1989) and the monthly survey average of +5 points (from 1996). The overall weakness in business conditions implies that the domestic economic environment remains very challenging.

### Trading, profitability and employment

This month's outcome of still weak business conditions reflected a slight up-tick in employment and trading conditions, which were fully offset by a deterioration in profitability, which fell to its lowest level in 4½ years.

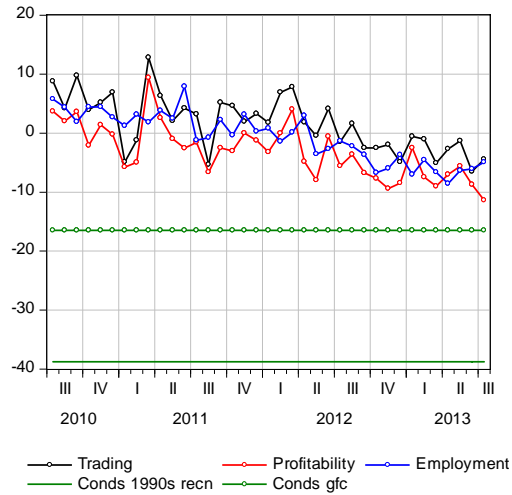
The improvement in **trading conditions** in July was driven by better conditions in mining (up 19), recreation & personal services (up 9) and retail (up 7), which were partly offset by weaker trading in finance/ business/ property (down 9) and wholesale (down 8). In levels terms, trading conditions were extremely weak in manufacturing (-24) and retail (-16), while they were strongest in recreation & personal services (+12), mining (+3) and finance/ business/ property (+2).

While **employment conditions** remained weak in July, they were a touch better reflecting improvements in mining (up 26), retail (up 15) and manufacturing (up 11), which were partly offset by weaker conditions in construction (down 11), transport & utilities and finance/ business/ property (both down 9). Overall employment conditions were weakest in construction (-15), manufacturing (-13) and wholesale (-10), while recreation & personal services was the only industry to report positive conditions (+6). Still weak employment conditions are broadly consistent with other indicators of labour market activity.

The weakening in **profitability** in July largely reflected heavy declines in finance/ business/ property (down 18), manufacturing and construction (both down 16). These were partly offset by improvements in recreation & personal services (up 11), wholesale (up 6) and retail (up 4). Profitability was very weak across a number of industries, including mining (-44), manufacturing (-41), construction (-24), retail (-19) and wholesale (-10), while recreation & personal services was the only industry to report a positive reading for profitability (+12).

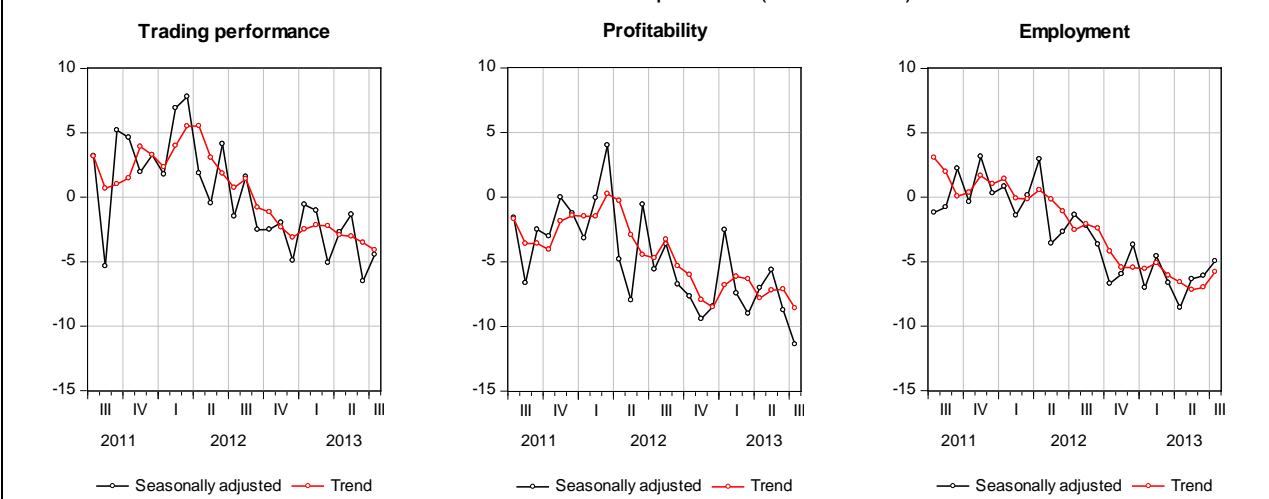
### Trading & employment improve, profits slump to 4½ year low

All components of business conditions (net bal., s.a.)



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

Business conditions components (net balance)



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

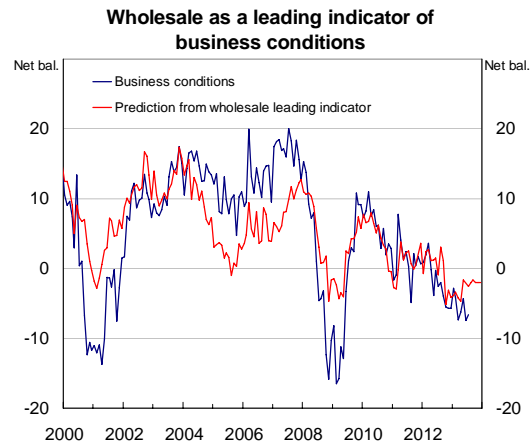
## Current business conditions (cont.)

### Wholesale: Signalling continued softness in the domestic economy?

The weakness in wholesaling that has persisted for the best part of 3½ years has continued into 2013. While conditions have been volatile in recent months, wholesale conditions remained poor, at -10 points in July.

Based on historical relationships, wholesale conditions appear to be a reasonably good predictor of overall business conditions – certainly there is strong statistical evidence of a leading relationship (Granger causality). Our analysis suggests that if seasonally adjusted wholesale conditions in July (-10) were to continue over the remainder of this year, overall business conditions could be expected to remain poor, averaging just -2 index points. That, in turn, is suggestive of an economy still running below trend and with little upward momentum in the growth rate.

### Wholesale activity points to modestly better overall conditions



Indicator =  $f(\text{business conditions}_{wsl}, \text{business conditions}_{wsl}(-1 \text{ to } -4), \text{ar}(1), \text{ar}(3))$

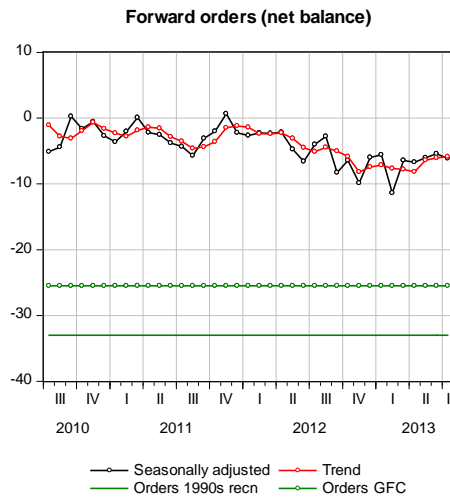
### Forward orders

The forward orders index ticked down to -6 index points in July, and remained well below the series long-run average of zero points since 1989. This measure of future demand implies that activity is likely to remain poor in the near term.

Forward orders deteriorated notably in construction (down 11) and wholesale (down 6). These falls were largely offset by improvements in mining and manufacturing (both up 10), but orders in these sectors remained poor overall. In levels terms, orders were most subdued in mining, wholesale (both -18) and manufacturing (-10), while they were least subdued in construction (-1), retail and recreation & personal services (both -3).

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

### New orders still weak, but stabilising

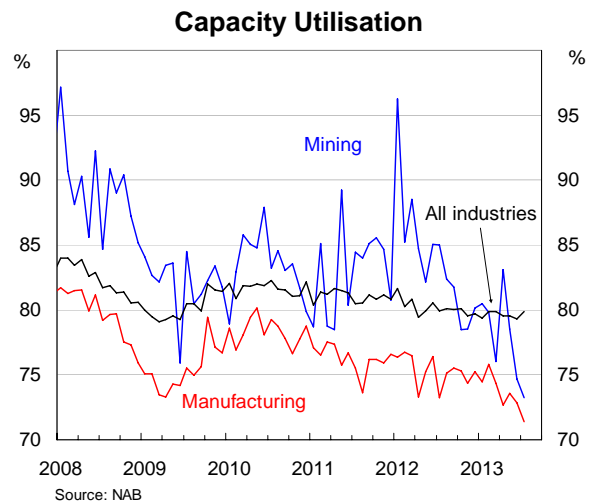


### Capacity utilisation

In July, capacity utilisation lifted modestly to 79.9%, from 79.3% in June. While the higher level of utilised capacity suggests weak activity could be abating, the level remains low relative to the series average (of 80.4% since 1989) suggesting any improvement may be limited. The rise in capacity utilisation was largely driven by wholesale (up 2.8 ppts) and retail (up 1.2 ppts). However, utilised capacity continued to tumble in mining (down 1.5 ppts), while it also fell in manufacturing (down 1.4 ppts to 71.4%; the lowest level in the history of the survey) and construction (down 0.9 ppts). Capacity utilisation was lowest in manufacturing (71.4%) and mining (73.2%), but highest in finance/business/property (82.8%), wholesale (82.3%) and recreation & personal services (82.2%).

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

### Spare capacity still relatively low



Source: NAB

## Current business conditions (cont.)

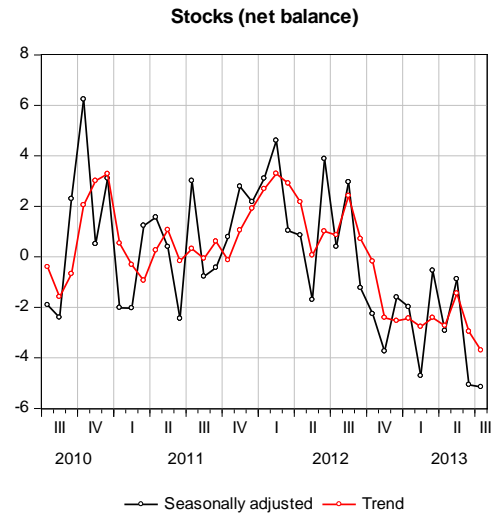
### Stocks

The stocks index remained at a low -5 points in July. When combined with still poor trading activity, the negative reading implies firms are voluntarily de-stocking in the soft demand environment. In trend terms, the stocks index edged 1 point lower to -4 points, to remain below the series average of +1 point since 1989.

The stocks index fell in construction (down 10), manufacturing and retail (both down 6), while it lifted considerably in mining (up 13) and wholesale (up 10). All industries reported negative stock indices in July, with particularly low readings reported in mining (-14), manufacturing (-10), retail (-9) and construction (-8).

*Net balance of respondents with a rise in stocks last month*

### Voluntary de-stocking continues

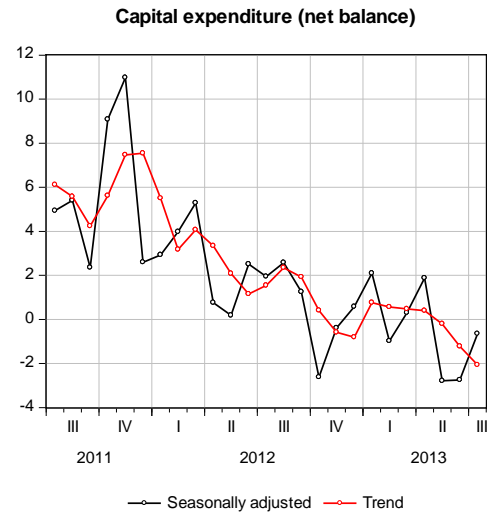


### Capital expenditure

The capex index picked up from a four year low in the month – up 2 to -1 index point. The outcome was driven by improvements in recreation & personal services (up 4) and transport & utilities (up 2), partly offset by falls in mining (down 5, partly unwinding a sharp rise in June) and retail (down 2). In levels terms, capex was lowest in manufacturing (-9); firms in this sector are probably scaling back investment in response to very poor activity and low levels of capacity utilisation. Capex was also low in mining (-6) and wholesale (-5), while it was highest in recreation & personal services (+7) and transport & utilities (+6).

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

### Capex improves but still relatively low



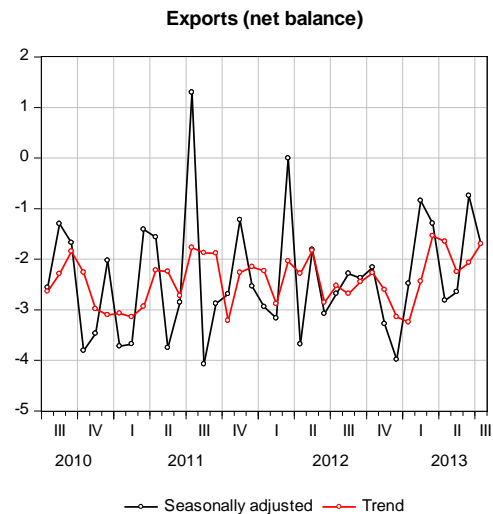
### Exports

The exports index, which represents export conditions for the economy as a whole, edged 1 point lower to -2 points in July, partly unwinding a modest rise in June. In manufacturing, the index rose by 6 points, perhaps reflecting the lower dollar, but remained negative. Elsewhere, the index fell heavily in mining (down 14) - probably a consequence of soft commodities demand - and transport & utilities (down 6). The exports index was highest in construction (+7) and lowest in mining (-16), manufacturing and transport & utilities (both -6).

The exporters' sales index, which represents export conditions for exporting industries, also pared back earlier gains, down 5 to -8 points.

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

### Exports fall back a touch



## Current business conditions (cont.)

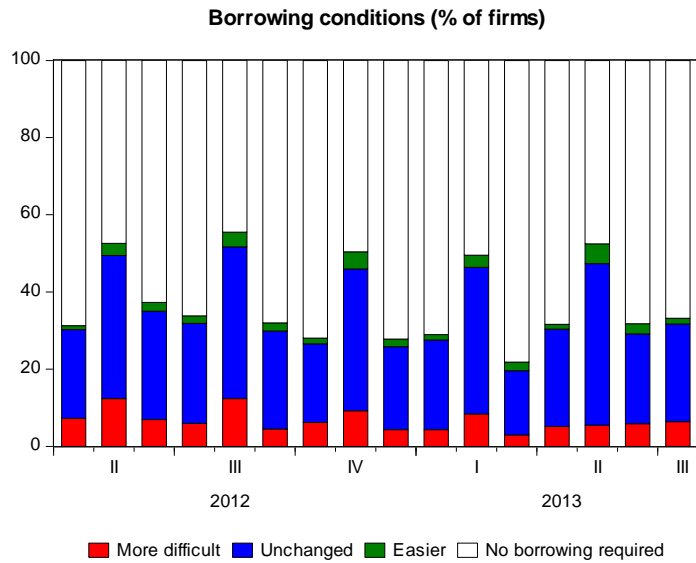
### Credit availability

Borrowing conditions tightened moderately in July, suggesting that finance became more difficult for businesses to access in the month.

The net borrowing index (easier minus harder) fell from -3 to -5 points in July. This outcome reflected a slight increase in the proportion of firms finding borrowing more difficult, which was compounded by a fall in the proportion of firms finding borrowing easier. Overall, around one third of firms required borrowing in the month.

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

### Borrowing conditions tighten

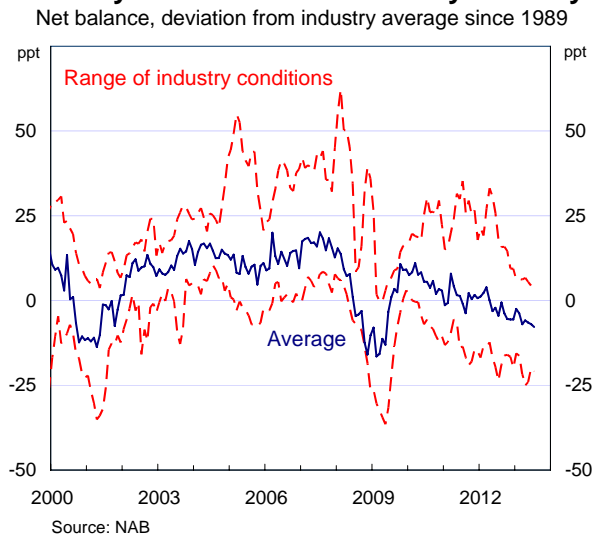


### Range of industry conditions continues to narrow

The variation in business conditions across industry has been quite pronounced since late 2009, largely reflecting the relative strength of mining and service related industries compared to the weaker consumer dependent and trade based industries following the GFC. However, the range of industry conditions has narrowed notably over the past year or so. This can be observed by comparing the difference between the best performing and worst performing industries each month.

While the variation in conditions across industries has narrowed more recently, it largely reflects a weakening in conditions of the previously stronger performing industries – including mining, services and transport firms – suggesting weakness elsewhere may be spreading.

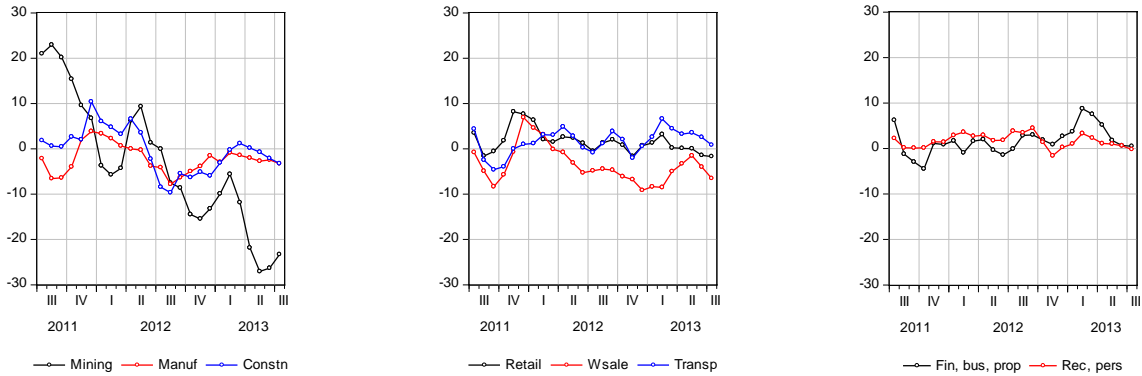
### Monthly Business Conditions by Industry



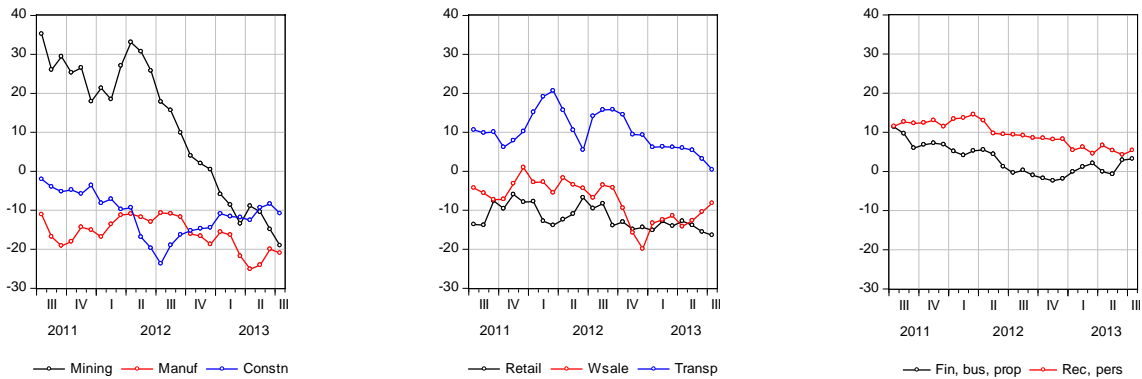


# Industry sectors and states

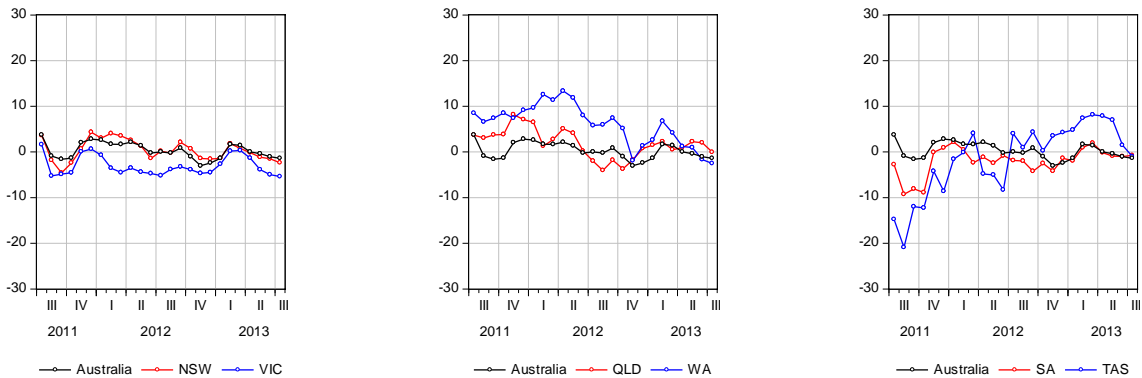
Business confidence by industry (net balance): 3-month moving average



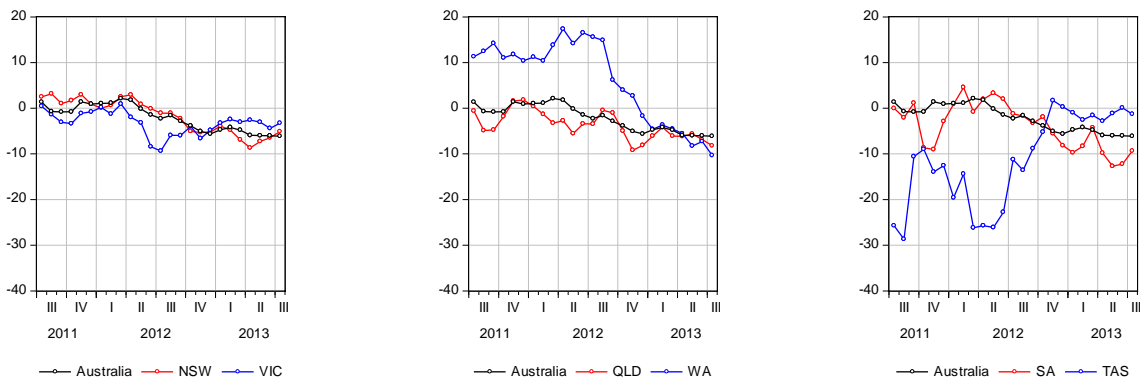
Business conditions by industry (net balance): 3-month moving average



Business confidence by state (net balance): 3-month moving average



Business conditions by state (net balance): 3-month moving average



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