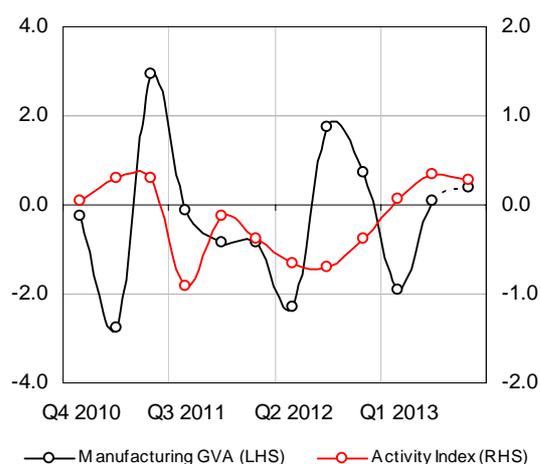


NAB Manufacturing Activity Index – Q3 2013

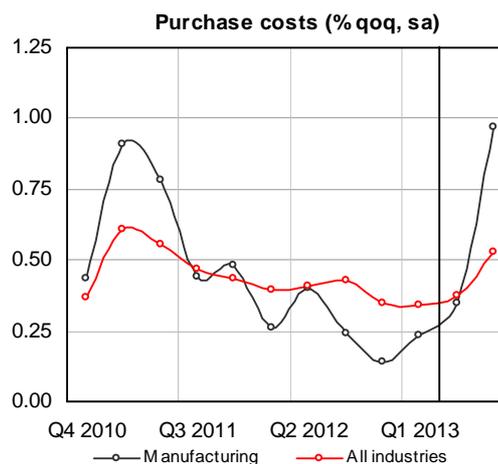
The Manufacturing Activity Index was largely unchanged in Q3 – with positive trends for business confidence offset by negative ones for labour and purchase costs and final product prices. The index implies a slight increase quarterly manufacturing activity – at around +0.4%. However purchase costs (also dollar related) are likely to push the index lower over the next six months.

- NAB's Manufacturing Activity Index remained positive in Q3 2013, at +0.3 points. This level was largely unchanged from the previous quarter, and is considerably stronger than the levels that were evident in 2012. The index implies that the manufacturing sector recorded some modest quarterly growth, increasing by around +0.4%.
- In recent times, the index has trended through a volatile growth cycle in Manufacturing Gross Value Added (GVA). The gap between our index and reported GVA in June was at its narrowest since early 2012. **The performance of the Activity Index compares favourably with other measures – particularly the Performance of Manufacturing Index – which has pointed to contractions in the sector across the past eighteen months** (see charts on page 2).
- Business confidence was the only positive influence on the Activity Index in Q3 – rising to +2 points (from -4 points in June). Confidence in the Manufacturing space may have been boosted by declines in the Australian dollar – reducing some of the competitive pressures on the industry. The largest increases in confidence were recorded in Machinery & Equipment, Food products and Printing, while there were sharp declines in Textiles, Clothing & Footwear and Non-metallic minerals.
- Final product prices was one of the key components tempering the positive influence of confidence on the Activity Index – down to -0.1% (from +0.1% previously). The negative trend was most evident in Food products, Chemicals and Machinery & Equipment, while Non-metallic minerals and Printing saw stronger trends.
- Negative trends in Purchase Costs also offset gains from Business Confidence – with Purchase Costs up to +0.2% (from +0.1% in our last report). The upturn in purchase costs was driven by stronger trends in Chemicals, Metal products and Printing, while Non-metallic minerals and TCF exhibited softer trends. Purchase costs are a lagged measure in our index, and recent data points to a sharp spike in Q3 - coinciding with the decline in the dollar, which increased the costs of imported inputs. This will likely push the Activity Index lower over the next six months.
- Labour cost trends were also negative – however this component had the smallest impact on the Manufacturing Activity Index. Costs increased sharply in Wood products and Metal products, while trends were softer in Printing, and TCF.
- While there was minimal change in the overall Manufacturing Activity Index, there were some significant changes at the subsector level. The gap between the strongest and weakest subsector Activity Indices narrowed considerably – down to its lowest level since the September quarter of 2011 – reflecting a decline in (strong performing) Chemicals and a large improvement in (weaker) Printing .

Activity Index stable in Q3 – indicates modest growth in Manufacturing



But purchase costs (AUD related) to revive headwinds in coming quarters



	Q1 2013	Q2 2013	Q3 2013		Q1 2013	Q2 2013	Q3 2013
Activity Index				Activity Index			
Manufacturing	0.1	0.3	0.3	Chemicals	1.5	1.9	1.2
Food, Beverage, Tobacco	0.1	0.6	0.8	Printing and Publishing	-1.5	-1.7	-0.5
Machinery and Equipment	0.1	-0.5	0.3	Textile, Clothing, Footwear	1.9	0.2	0.8
Metal Products	-0.5	0.1	-0.5	Wood & Paper	-0.4	0.8	0.2
Non-metallic Minerals	1.3	-0.4	0.8				

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All data is seasonally adjusted. Gross value added (GVA), Purchase costs, Labour costs and Final prices data are percentage changes expressed at a quarterly rate. Business confidence is a net balance index.

Manufacturing Activity Index: Index stable in Q3 – remaining positive, which indicates modest quarterly growth in the Manufacturing sector

NAB's Manufacturing Activity Index remained positive in Q3 2013, at +0.3 points. This level was largely unchanged from the previous quarter, and is considerably stronger than the levels that were evident in 2012.

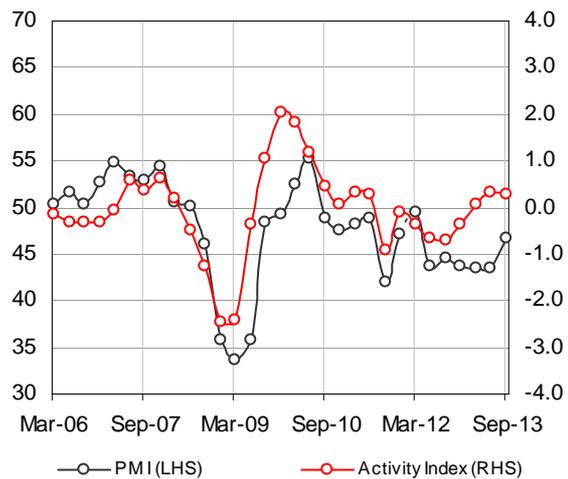
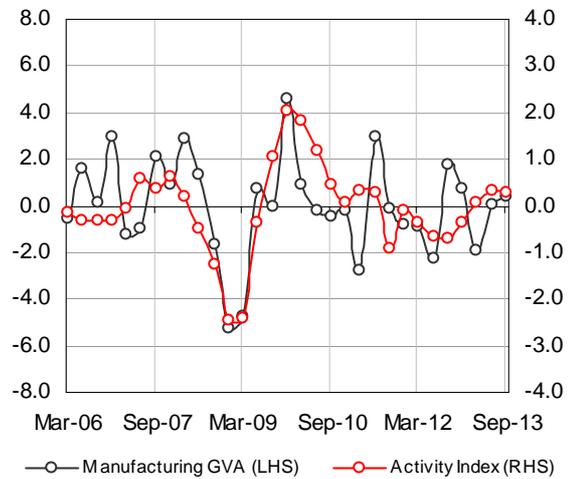
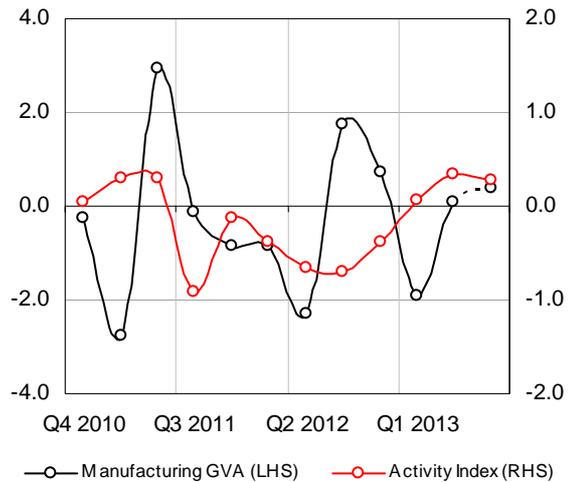
The Manufacturing Activity Index implies that the manufacturing sector recorded some modest quarterly growth, increasing by around +0.4%.

The Manufacturing Activity Index has been constructed to replicate quarterly movements in the manufacturing sector. It comprises weighted components of business confidence and profits from NAB's Quarterly Business Survey (with the latter based on weighted movements in output and input prices, which are lagged by two quarters).

In recent times, the Manufacturing Activity Index has trended through a volatile growth cycle in Manufacturing Gross Value Added (GVA) (which is produced by the ABS). The gap between our index and reported GVA in June was at its narrowest since early 2012.

One of the key challenges in attempting to replicate quarterly movements in manufacturing activity is that these estimates are subject to significant revision over time. In the most recent National Accounts data, there was a substantial downward revision to Manufacturing GVA for the March quarter of 2013 – down to -1.9% (from the initial estimate of -0.8%).

The performance of the Manufacturing Activity Index compares favourably with other measures of manufacturing performance. In particular, the Activity Index has recorded a closer relationship to GVA than the Performance of Manufacturing Index – which has pointed to contractions in the sector across the past eighteen months.



Activity Index Components: Stable Activity Index reflects that gains in Business Confidence were offset by weaker trends in Purchase Costs and Product Prices

Business Confidence in the Manufacturing sector was considerably stronger in Q3 2013 – rising to +2 points, from -4 points in the June quarter. This was the strongest level of confidence recorded since the March quarter of 2011. Confidence was the only positive influence on the index this quarter.

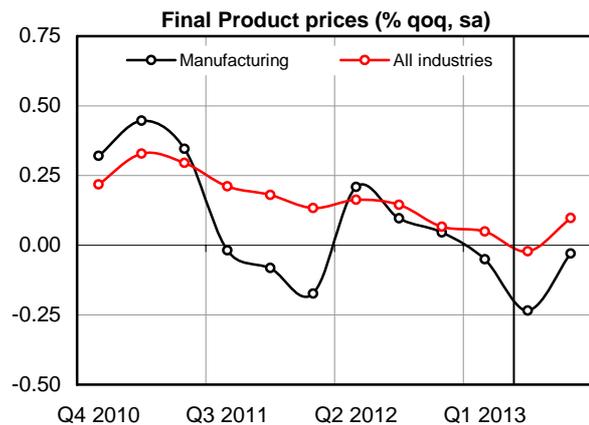
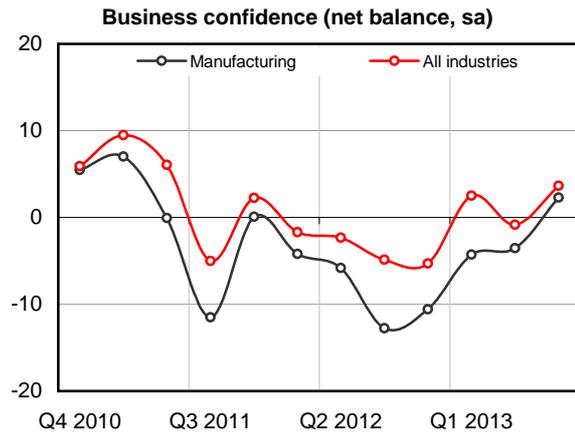
Confidence in the Manufacturing space may have been boosted by positive trends for the Australian dollar, which averaged US 92 cents (from US 98 cents in Q2) – reducing some of the competitive pressures on the industry.

At the subsector level, the largest increases in confidence were recorded in Machinery & Equipment, Food products and Printing, while there were sharp declines in Textiles, Clothing & Footwear and Non-metallic minerals.

Final product prices (a lagged measure in our index) declined in the March quarter, down to -0.1% (from +0.1% in Q4 2012). This trend was weaker than the broader economy, and was one of the key components tempering the positive influence of confidence on the Activity Index.

By subsector, the negative trend was most evident in Food products, Chemicals and Machinery & Equipment, while both Non-metallic minerals and Printing saw stronger trends.

Manufacturing product prices continued to decline in the June quarter – down to -0.2% - which will have a negative influence on the Activity Index next quarter.



Purchase costs (also a lagged measure) trended slightly higher in the March quarter – moving up to +0.2% (from +0.1% in Q4 2012). Combined with the decline in Final Product Prices, these measures offset the gains from improved Business Confidence.

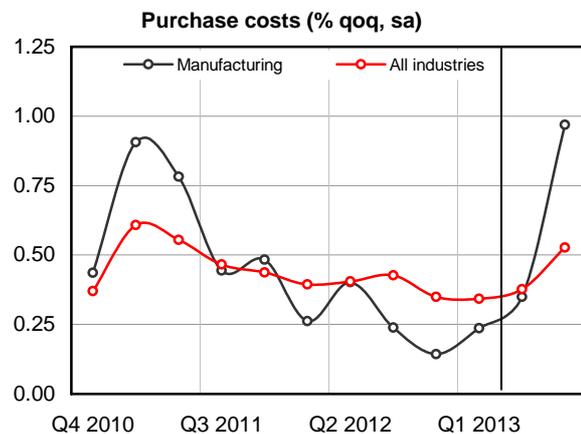
The upturn in purchase costs was driven by stronger trends in Chemicals, Metal products and Printing, while Non-metallic minerals and Textiles, Clothing & Footwear exhibited softer trends.

Purchase cost trends will continue to have a negative influence on the Activity Index, with a modest rise next quarter, followed by a sharp spike which will impact Q1 2014. This spike coincided with the decline in the dollar – which increased the costs of imported inputs.

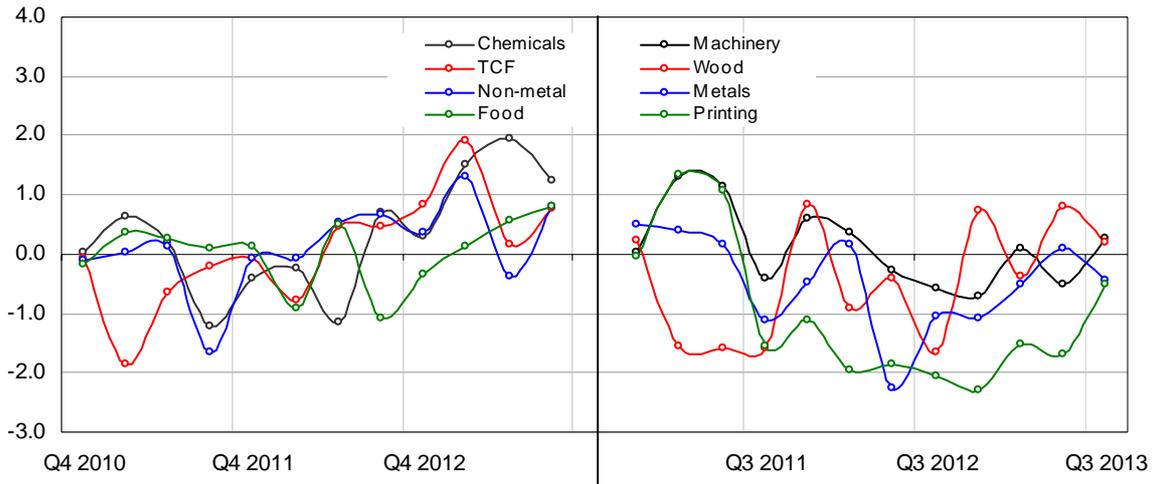
Labour costs trends were also negative in Q1 2013 – pushing up to 0.4% (from 0.3% in the December quarter) – however this component had the smallest impact on the Manufacturing Activity Index.

Labour costs increased sharply in Wood products and Metal products, while trends were softer in Printing, and Textiles, Clothing & Footwear.

Labour costs trends dipped in the June quarter, which will have a modest positive impact on the Activity Index next quarter.



Subsector Analysis: Narrower gap between the strongest and weakest sectors – as Chemicals pulls back and Printing improves



While there was minimal change in the overall Manufacturing Activity Index, there were some significant changes at the subsector level. The gap between the strongest and weakest subsector Activity Indices narrowed considerably – down to its lowest level since the September quarter of 2011 – reflecting a decline in (strong performing) Chemicals and a large improvement in (weaker) Printing.

The **Food & Beverage** activity index strengthened a little further in Q3, up to +0.8 points (from +0.6 points previously). A strong increase in Business Confidence (now in positive territory) was offset by weaker trends in Final Product Prices, while Purchase and Labour Costs were moderately positive.

The **Chemicals** activity index pulled back sharply in the September quarter, but remained the strongest overall at +1.2 points (compared with +1.9 points in Q2). A negative trend for Purchase Costs was the main contributor to the decline, along with Final Product Prices and Labour Costs. In contrast, Business Confidence improved, tempering the decline.

The **Printing and Publishing** activity index was one of the strongest improvers in Q3, although it remained the weakest sector overall at -0.5 points (compared with -1.7 points in the June quarter). There were stronger trends for Final Product Prices, Business Confidence and Labour Costs, while there was a slight downturn in Purchase Cost trends.

The **Textiles, Clothing & Footwear** activity index recorded a modest improvement in the September quarter – pushing up to +0.8 points (from +0.2 points in Q2). The gains were driven primarily by a strong improvement in Purchase Cost trends, along with an improvement in Labour Cost trends. In contrast, Business Confidence in the sector pulled back sharply, and Final Product Prices were largely unchanged.

The **Wood Product** activity index pulled back in Q3, down to +0.2 points (from +0.8 points in June), the second largest decline this quarter. This decline was driven primarily by a strongly negative trend for Labour Costs, with a modest improvement in Business Confidence offset by a negative trend in Purchase Costs, while there was minimal change in Final Product Prices.

The **Machinery & Equipment** activity index improved in the September quarter, rising to +0.3 points (from -0.5 points in Q2). Stronger trends for Business Confidence and Purchase Costs were the key drivers of the improvement, while Labour Cost trends were subdued and Final Product Prices were moderately negative.

The **Metal Product** activity index contracted moderately in Q3, down to -0.5 points (from +0.1 point in the June quarter). While there was a modest improvement in Business Confidence, all other components recorded negative trends, led by Purchase Costs and Labour Costs.

The **Non-metallic minerals** activity index recorded the largest increase this quarter – moving up to +0.8 points in September (from -0.4 points). This improvement was driven by a considerably stronger trend for Purchase Costs, while a strong gain in Final Product Prices was offset by negative trends for Business Confidence (and to a much lesser extent Labour Costs).

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