

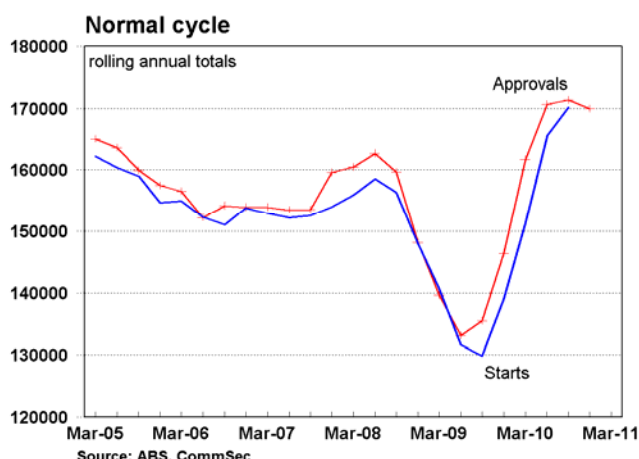
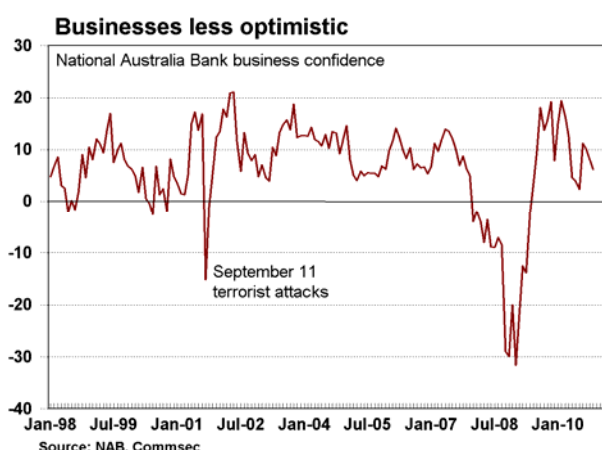
Tougher times for business; Dwellings slump

NAB business survey; Dwelling starts

- The NAB business confidence index eased from +8.1 to +6.2 in November. The business conditions index rose from +1.6 in October to +3.7 in November.
- Forward looking sub-indices remained decidedly weak despite modest improvements. Profits ticked higher from 17-month lows, trading conditions remained near nine-month lows and new orders are still contracting.
- Australian dwelling starts slumped by 13.2 per cent in the September quarter, after lifting for the previous four quarters. In the September quarter, starts rose in only three of the eight states and territories.
- In seasonally adjusted terms work started on 170,153 dwellings over the past year – the biggest annual result in almost six years.

What does it all mean?

- Corporate Australia is at present going nowhere. The rate hike in November has robbed businesses of much needed optimism. In fact business confidence has now fallen for eight out of the past nine months. Business conditions are far from rosy and sluggish retail activity and the impact of the stronger Australian dollar has added to the weaker trading environment.
- Looking forward, confidence and conditions are unlikely to improve to any great degree in the near term. The November rate hike will have a more lasting impact in coming months given the additional increase in borrowing costs, and slowdown in activity that will take place in the near term.
- More concerning is the added weakness in forward looking indicators. Business owners continue to trim future orders, while profitability is weak, bouncing of a 17-month low. Given that retailers are aggressively discounting, borrowing costs are rising, and the higher Aussie dollar is curbing manufacturing exports, it is likely that activity will remain subdued in the near term. The negative momentum is clearly worrying, meaning that the Reserve Bank could face an extended stay on the interest rate sidelines. CommSec expects the next rate hike to take place in April.
- There is no doubt that the activity in the housing sector is slowing down. Housing starts have slumped by over 13



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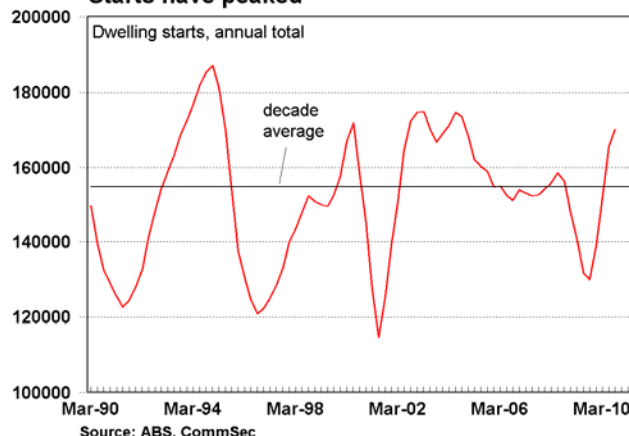
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per cent in the September quarter – marking the biggest quarterly slide in a decade. However the weakness in starts follows what has been a very strong period of dwelling commencements. In fact in the year to September over a 170,000 dwellings were started across Australia – the best annual result in almost six years.

- It is important to highlight that the weakness in dwelling starts is not uniform across the nation. Rather it seems that it is only a couple of states that could be classified as under building when compared with decade averages. Building in NSW and Queensland is 11 per cent below long term averages. Weaker population growth in Queensland would have played a part and the super low vacancy rates across NSW attests to the lack of building that is taking place.
- The increased supply of homes coming onto the market, together with the softening of demand in response to higher interest rates should lead to more balanced conditions and more sustainable growth of home prices. CommSec expects Australian home prices to grow by 5-8 per cent over 2011.

Starts have peaked



What do the figures show?

National Australia Bank Business Survey:

- The **National Australia Bank business confidence index** fell for the eighth time in nine months, easing from +8.1 to +6.2 in November.
- The **business conditions index** rose from +1.6 to +3.7 in November.
- The index of trading conditions recorded a marginal improvement, up from +4.0 to +4.1 – still holding near nine-month lows; profitability improved from 17 month lows of -4.0 to +1.6; employment eased from +6.0 to +4.1; and forward orders remained weak despite a modest improvement from -3.0 to -2.0.
- The monthly reading of labour costs fell modestly from 1.2 per cent to 1.1 per cent in November. NAB noted that annual growth of labour costs stands at 4.4 per cent.
- Inflationary pressures are well contained. Retail prices rose at a 0.3 per cent annual rate in November. Purchase costs jumped by a 0.6 per cent quarterly rate, and final product prices rose by a 0.4 per cent quarterly rate.
- Capacity utilisation** fell slightly from 81.1 per cent to 80.9 per cent in November - below the decade average of 81.6 per cent.

Dwelling commencements

- The number of **dwelling commencements** fell by 13.2 per cent in the September quarter after rising by an upwardly revised 2.1 per cent in the June quarter. Public sector activity slumped by 57.7 per cent – however it only makes up just 6 per cent of total activity. Private sector commencements fell by 7.1 per cent in the quarter with house starts down 4.3 per cent and apartment starts down 13.5 per cent.
- In the September quarter, starts rose in only three of the eight states and territories. Leading the gains was the Northern Territory (up 27.6 per cent), followed by Tasmania (up 22 per cent) and Victoria (1.5 per cent). Starts fell most in the ACT (down 30.5 per cent), followed by Queensland (down 25.2 per cent), Western Australia (down

Outlook uncertain



Over or under-supply?

Annual dwelling starts

% change on decade average

ACT	73.3
Victoria	35.7
Tasmania	27.9
South Australia	17.5
Northern Territory	16.7
Western Australia	16.2
AUSTRALIA	9.9
NSW	-11.0
Queensland	-11.3

Source: ABS, CommSec

19.9 per cent), NSW (down 14.5 per cent) and South Australia (down 5.7 per cent).

- Compared to decade averages only two states could be classified as under building (see attached table).
- In the year to September 2010, 170,153 dwellings were started across Australia – the best annual result in almost six years. Annual starts hit an 8-year low of 129,868 in the year to September last year.

What is the importance of the economic data?

- The monthly **National Australia Bank business survey** is valuable in providing a timely reading on the health of Corporate Australia. Key indicators of business conditions such as orders, employment, profitability and capacity use are covered together with a gauge on confidence levels.
- The ABS figures on **dwelling commencements** are compiled on the basis of returns collected from builders and other individuals and organisations engaged in building activity. The data is useful in highlighting activity levels in residential construction

What are the implications for interest rates and investors?

- The frequency of rate hikes has taken its toll on the household budget. Consumers aren't keen to spend, putting margins under pressure and causing retail prices to fall. While the environment is great news for conservative consumers, it represents more challenging times for Corporate Australia.

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