more give, less take

NAB Monthly Business Survey

by NAB Group Economics

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September 2014

National Australia Bank

Key Points:

- Business confidence lost ground in September –lowest level since pre election - in the face of a persistently soft operating environment for many firms. Forward orders remained soft, prompting de-stocking and competitive pricing which appears to have weighed on profitability. Confidence varies significantly across industries, with services firms the most optimistic.
- Business conditions fell again in September bringing the index back to its lowest level in 4 months and confirms our expectation that the (narrowly based) jump in July would be short lived. Most industries recorded a drop in September, although transport & utilities were surprisingly strong (falling oil prices and removal of carbon tax?). Forward orders eased again, implying Q3 domestic demand will remain soft. Capacity utilisation also fell noticeably.
- A drop in profits and employment drove conditions lower, with the latter moving significantly into negative territory – in contrast to some other labour market partials. Forward indicators are soft, but trend conditions in the 'bellwether' wholesale industry are a little less weak. Our wholesale leading indicator implies soft underlying conditions and below trend growth in Q3.
- GDP forecasts revised down modestly: 2014/15 2.8% (was 2.9%) and 2015/16 3.2% (was 3.4%). Unemployment rate still to peak at around 6½%. No change likely in cash rate until near the end of 2015.

Table 1: Key monthly business statistics*

	Jul 2014	Aug 2014	**Sep 2014**		Jul 2014	Aug 2014	**Sep 2014**
	Net balance				*Net balance*		
Business confidence	9	7	**5**	Employment	0	-1	**-4**
Business conditions	8	3	**1**	Forward orders	5	0	**-1**
Trading	12	6	**6**	Stocks	2	1	**-2**
Profitability	9	3	**0**	Exports	2	0	**1**
	% change at quarterly rate				*% change at quarterly rate*		
Labour costs	0.8	0.8	**0.8**	Retail prices	0.8	0.2	**-0.7**
Purchase costs	0.5	0.5	**0.4**		*Per cent*		
Final products prices	0.2	0.2	**0.0**	Capacity utilisation rate	81.0	80.6	**80.2**

* 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 24 Sep to 3 Oct, covering over 400 firms across the non-farm business sector.

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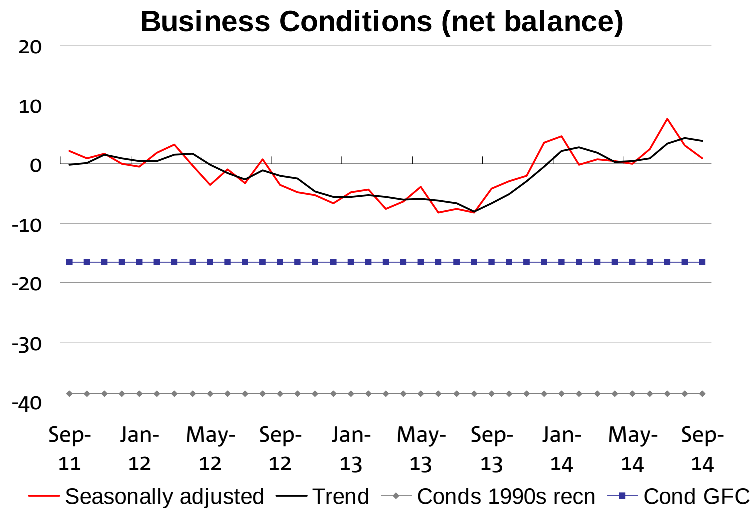
Next release: 23 October 2014 (September quarterly)
11 November 2014 (October monthly)

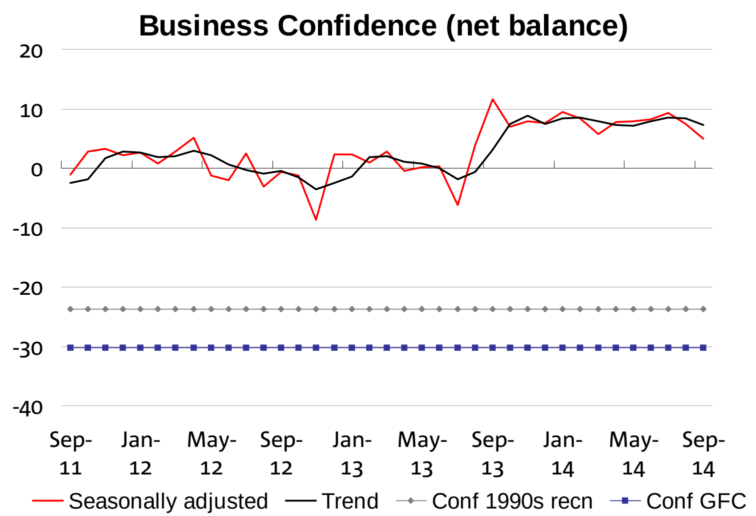
Analysis

- The multi-year high for business conditions in July appears to have been a flash in the pan, with the index falling for the second straight month. The business conditions index dropped 2 points in September (following a 5 point decline) to +1 index points. At this level, business conditions are still well up on 2013 averages, but below the long run average of the series (+5). The upward trend in the index has stalled, with very little impetus from forward indicators to suggest the trend will resume its upward trajectory in the near-term. The effects of soft national income growth – a function of lower commodity prices,, excess capacity and cautious spending behaviour – are being felt across the economy. This has been reflected in most industries, with conditions falling in the month for all but transport & utilities (up 14) and recreation & personal services (unchanged). The strength in transport & utilities is difficult to explain . But does coincide with falling oil prices (and improved profitability in the transport sector) the removal of the carbon tax. .Ex transport and utilities business conditions would have been -1 index points. Looking through the monthly volatility, the trend in business conditions still looks reasonable but unless next month improves will slow significantly. Trend conditions rose in both wholesale and transport & utilities, both up 4 points, while mining fell the most (down 4). Mining and retail are lowest (-17 and -8 points respectively), consistent with lower commodity prices and wages growth trend as well as low levels of consumer confidence. Recreation & personal services and construction are performing best in trend terms.
- Business confidence also lost ground, but remains reasonable – albeit at the lowest level since the pre election jump in mid 2013. The index dropped 2 points (to +5), with outcomes varying significantly across industries. For September, mining and wholesale were the only industries to report a negative confidence index (-22 and -3 points respectively). Despite remaining positive, confidence fell the most in construction during the month (down 20), possibly reflecting slower growth in new approvals (orders also fell) and increasing speculation that authorities may introduce measure to address speculation in residential property markets. Looking through the monthly volatility, trend confidence was down 1 point (to +7), with construction highest (+15) and mining the lowest by a large margin (-14).

Better conditions eroding away



Confidence surprisingly robust

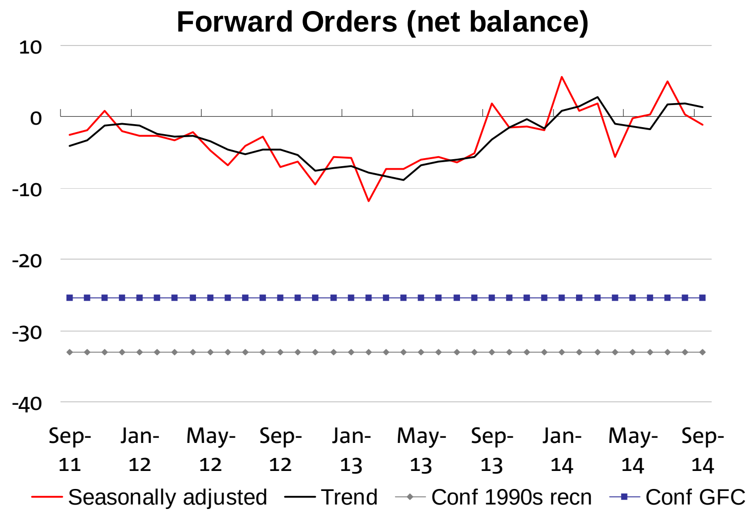


Excluding normal seasonal changes, how do you expect the business conditions facing your industry in the next month to change?

Forward indicators

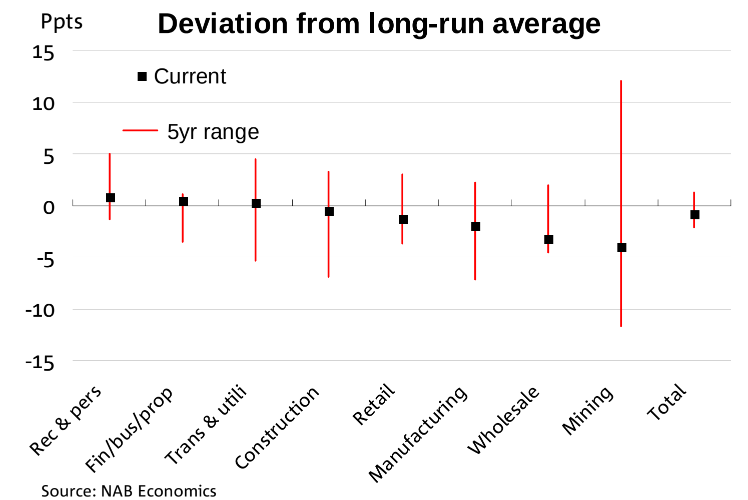
- The forward orders index dropped by 1 to -1 index points, its lowest level since April. This is below the long run average for the monthly series, suggesting soft near term demand and justifying an apparent de-stocking by firms during the month. The outcome reflected a particularly large fall in construction (down 30), suggesting the boom in new residential building approvals is losing momentum. Retail, mining, manufacturing and transport & utilities all recorded weaker forward orders as well (down 7, 5, 4 & 3 respectively). In trend terms, orders were down 1, to +1 point. Orders are now weakest in trend terms for mining and retail (both -5), but remain strongest for construction (+6) despite the significant decline in September. Growth in residential building approvals has moderated, but remains at elevated levels – as is the pipeline of work to be done.
- Capacity utilisation eased a little in September to 80.2%, although trend utilisation rates have improved steadily since early 2013. This level is below the monthly survey average of 81.1% (from 1997), as well as the long-run average of 80.4% (from 1989). The wholesale industry recorded the largest falls (down 3.1 ppts), but it is manufacturing that is reporting the lowest utilisation rates (75.9%). Utilisation rates also fell for recreation & personal services (down 1.0 ppts) and retail (down 0.1 ppts). The large pipeline of residential building construction is keeping construction utilisation rates elevated (81.6%), while utilisation in transport and professional services is generally a little higher. Utilisation in a majority of industries is below long run averages.
- The capital expenditure index fell modestly in September, down 1 point to +4 index points – close to long-run average levels. The trend index was also down 1, to +4 index points, which suggests a moderate expansion of non-mining business investment (which has a larger weighting in the survey). This trend is consistent with improving investment intentions outside of mining in the Q2 ABS Capex Survey. Trend mining and rec & pers services capex are highest (+13 and +9 points respectively).
- Elsewhere in the survey, cash flow (not seasonally adjusted) was strongest in fin/prop/bus services, and weakest in retail.

Sales orders drop - marginally



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

Capacity utilisation still mixed across industry

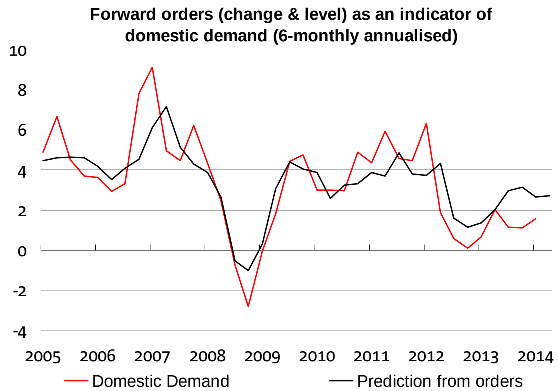


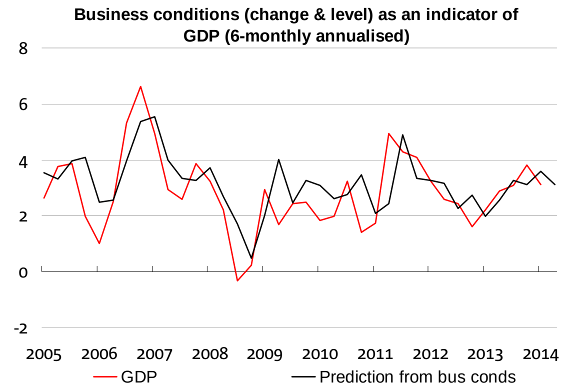
Source: NAB Economics

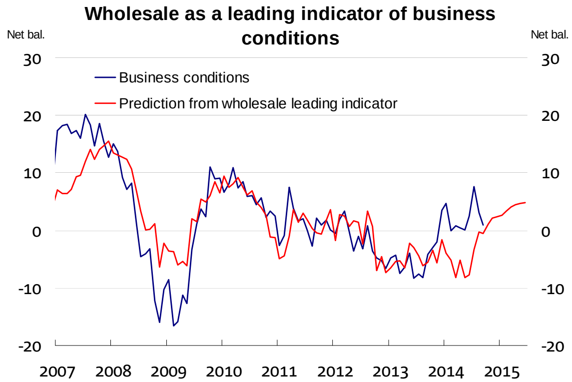
Full capacity is the maximum desirable level of output using existing capital equipment.

Implications for forecasts For more information see latest Global & Australian Forecasts

- Disappointing global growth continued into mid-2014 with GDP expanding by a sub-trend 3% yoy and concern over weakness in Japan and the Euro-zone offsetting solid growth in the US and UK. Chinese forecasts unchanged. We expect global growth to improve to around 3½% yoy through 2015 and 2016, mainly reflecting faster growth in the US and India as well as a return to more normal growth in Latin America. Inflationary pressures should remain subdued, allowing central banks in the US and UK to lift rates very gradually through the next few years while rates should stay low in Japan and the Euro-zone.
- Weaker Q3 and terms of trade means GDP forecasts revised down modestly: 2014/15 2.8% (was 2.9%) and 2015/16 3.2% (was 3.4%). Unemployment rate still to peak at around 6½%. We continue to expect no change in cash rate until a tightening cycle begins near the end of 2015.
- Our model of 6-monthly annualised demand growth, using forward orders as a predictor, has been suggesting stronger growth than the national accounts in recent quarters. Nevertheless, applying trend forward orders for September to our model for Q3 (+1) suggests that predicted demand growth will be similar to Q2. Similarly, business conditions over predicted GDP growth in Q2. Based on trend business conditions from the August monthly survey, our model implies slightly softer predicted GDP growth in Q3. Applying business conditions derived from our 'wholesale leading indicator' implies even softer GDP growth in Q3.
- Wholesalers gave back some of the gains of recent months, suggesting the industry continues to face significant challenges – AUD depreciation would exacerbate challenges facing wholesale importers. Wholesale conditions eased back into negative territory (-4), which makes 24 out of 25 months where wholesale conditions have been negative. Based on past relationships, wholesale conditions have been a reasonably good predictor of overall business conditions – exhibiting strong statistical evidence of a leading relationship (Granger causality). The measures have diverged since late last year as broader conditions improved, but the gap has since narrowed. This indicator predicts slightly softer business conditions in Q3 than the regular conditions index, but comes more into line in late 2014.







Indicator = f(business conditions wsl, business conditions wsl(-1 to -4), const.

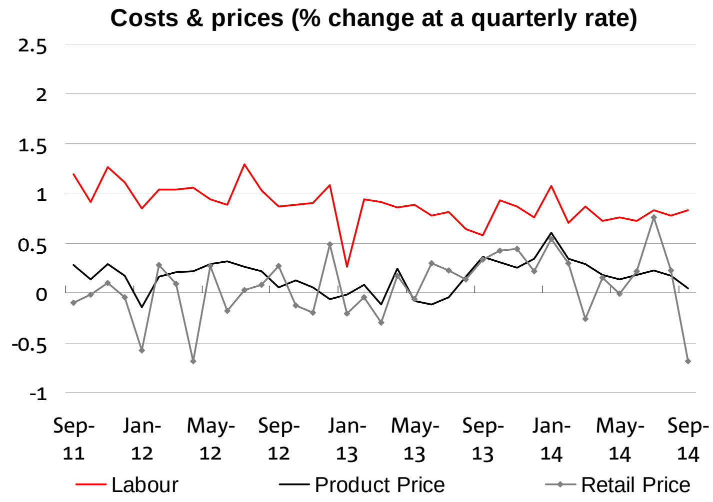
Costs and prices

- Labour costs growth (a wages bill measure) was unchanged at 0.8% in September, consistent with the slack labour market and modest wage growth.. Labour cost changes varied across industries. The downturn in mining investment and efforts of mining firms to control costs appear to be having an impact on the sectors wages. Mining labour cost deflation ramped-up 0.9 ppts in September to -1.2% -- the largest decline of any industry by a noticeable margin. The only other industry to record falling labour costs was wholesale (-0.1%, down 0.2 ppts). In contrast, labour cost growth was strongest in transport & utilities (1.4%), fin/ prop/ bus services (1.4%) and recreation & personal services (1.3%). Transport & utilities and recreation & personal services also reported the strongest employment conditions in the month. Labour market conditions are softest in mining and wholesale, consistent with labour cost deflation. Labour market indicators in Australia have become difficult to read (largely due to statistical issues with the official ABS labour market survey), but generally remain soft. Based on the weakening employment outcomes in the Survey (and official estimates) the prospects are for further limited wage pressures ahead.

- Purchase cost growth was down modestly to 0.4% in September (at a quarterly rate), which is well down on growth rates seen over 2013. Purchase costs decelerated in most industries – rec & pers services eased the most (down 0.4 ppts). Wholesale and transport & utilities were the exceptions (up 0.9 and 0.2 ppts respectively). As the AUD depreciates, import cost pressures facing wholesalers could lift further – purchase cost pressures are strongest in this industry (1.2%, quarterly rate). Purchase costs growth was weakest in mining (-0.1%).

- Final product prices were flat in September (at a quarterly rate) suggesting only little relief for firm's margins despite subdued input cost growth. This means the RBA can maintain their loose stance on monetary policy to allow greater traction for domestic demand. Retail prices dropped considerably in September (-0.7%), which could be an indication of fiercely competitive discounting in the subdued demand environment – although this bodes well for the CPI outlook. Upstream price pressures (e.g. manufacturing) are also reasonably subdued (down 0.5 ppts). The mining sector recorded the most price deflation (-3.1%), while prices growth is highest in transp & util (0.4%).

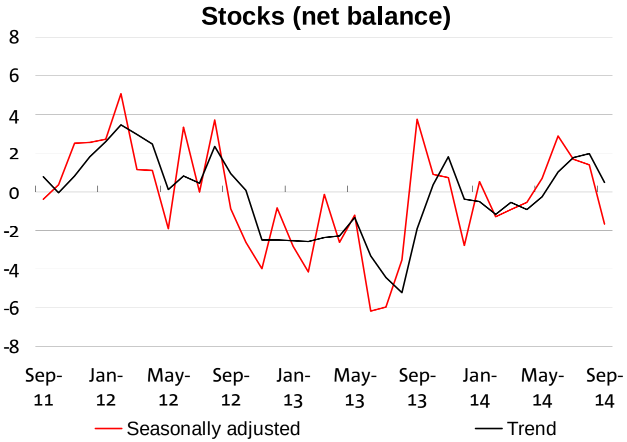
Price pressures ease back after temporary spike



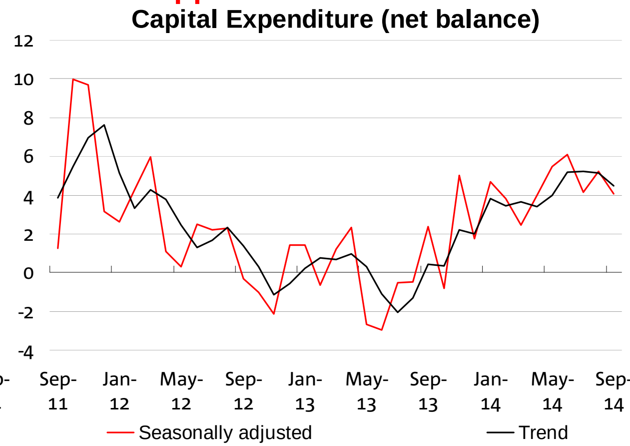
Based on respondent estimates of changes in labour costs and product prices. Retail prices are based on retail sector product price estimates.

More details on business activity

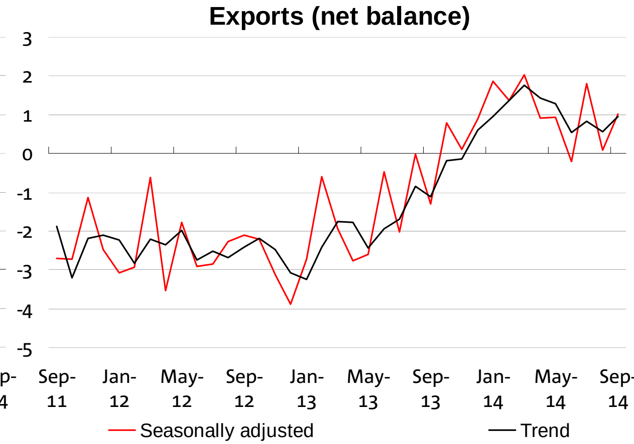
Re-stocking seemingly short lived



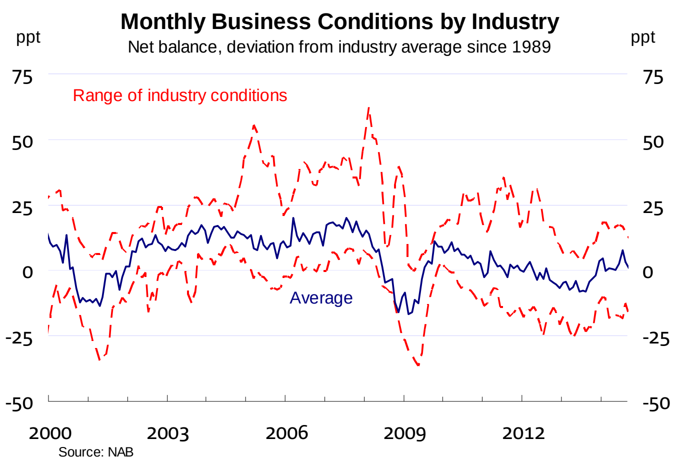
Capex still positive, but momentum appears to have stalled



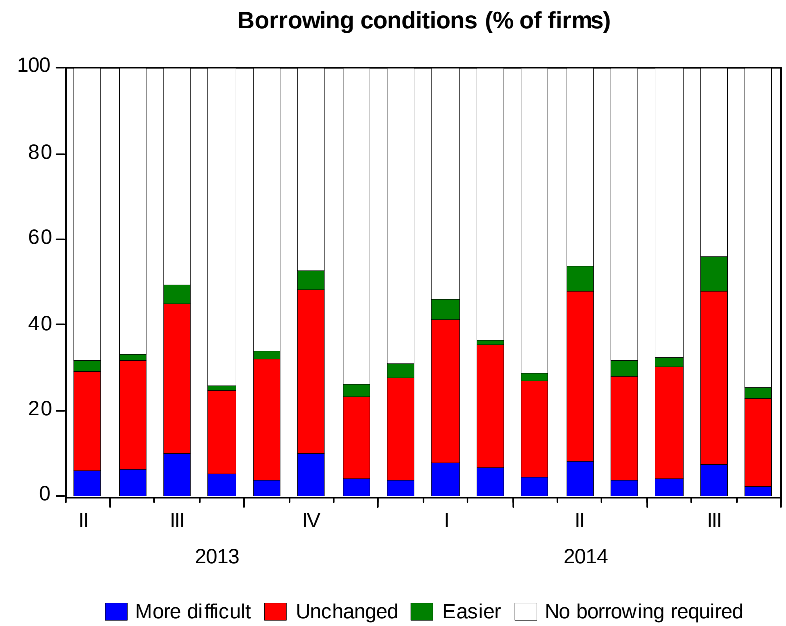
Exports increasing moderately



Range of conditions remains wide, but narrowing

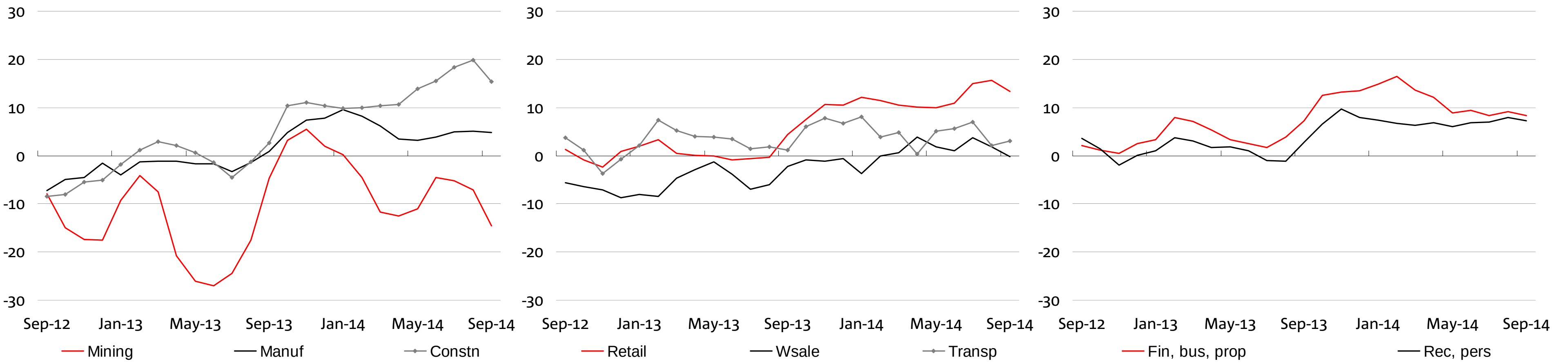


Borrowing conditions & demand for credit worsened in past 3 months

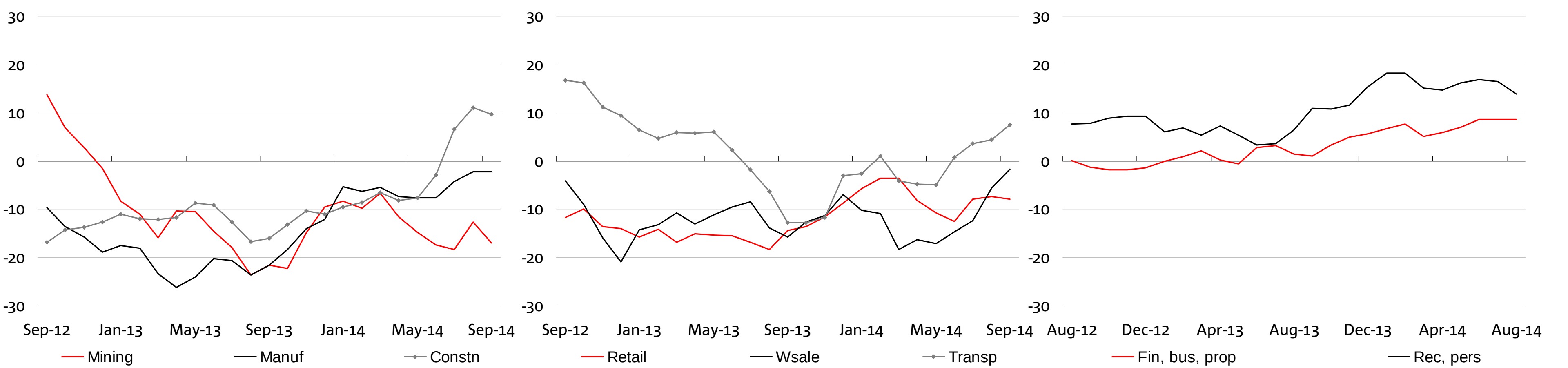


More details on industries

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

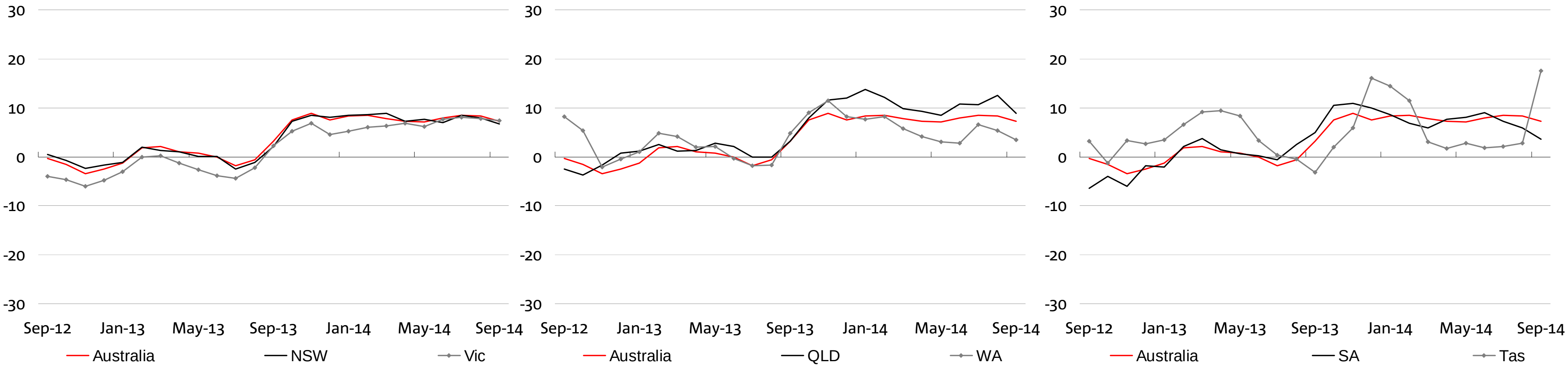


Business conditions by industry (net balance): 3-month moving average

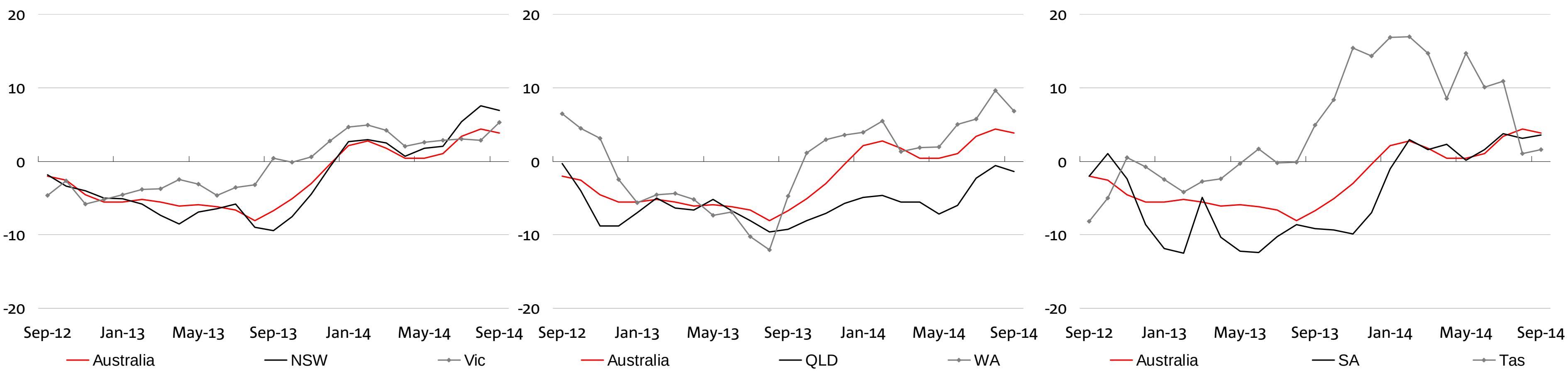


More details on states

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



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



Data appendix

Prices & costs by industry (% change at a quarterly rate)

Sep-2014	Mining	Manuf	Constn	Retail	Wsale	Tran. & utils	Rec. & pers.	Fin. prop. & bus.	Australia
Labour costs: current	-1.2	0.3	0.1	0.5	-0.1	1.4	1.3	1.4	0.8
Labour costs: previous	-0.3	0.5	0.1	0.8	0.1	0.9	1.2	1.3	0.8
Labour costs: change	-0.9	-0.2	0.0	-0.3	-0.2	0.5	0.1	0.1	0.0
Prices (final): current	-3.1	-0.2	-0.1	-0.7	0.3	0.4	0.3	0.3	0.0
Prices (final): previous	-0.7	0.3	-0.2	0.2	0.1	0.2	0.3	0.2	0.2
Prices (final): change	-2.4	-0.5	0.1	-0.9	0.2	0.2	0.0	0.1	-0.2
Purchase costs: current	-0.1	0.7	0.3	0.3	1.2	0.6	0.3	0.1	0.4
Purchase costs: previous	0.0	0.8	0.5	0.5	0.3	0.4	0.7	0.2	0.5
Purchase costs: change	-0.1	-0.1	-0.2	-0.2	0.9	0.2	-0.4	-0.1	-0.1

Key state business statistics for the month

Sep-2014	Monthly Business Survey Data: By State						
	NSW	**VIC**	**Qld**	**SA**	**WA**	**Tasmania**	**Australia**
Bus. conf.: current	3	7	2	1	-5	39	5
Bus. conf.: previous	7	6	13	3	2	9	7
Bus. conf.: change	-4	1	-11	-2	-7	30	-2
Bus. conf: current - Trend	7	7	9	4	3	18	7
Bus. conf: previous Trend	8	8	13	6	5	3	8
Bus. conf.: change -Trend	-1	-1	-4	-2	-2	15	-1
Bus. conds: current	1	12	-6	5	1	0	1
Bus. conds: previous	8	2	-4	-5	11	6	3
Bus. conds: change	-7	10	-2	10	-10	-6	-2
Bus. conds: current -Trend	7	5	-1	4	7	2	4
Bus. conds: previous -Trend	7	3	-1	3	10	1	4
Bus. conds: change -Trend	0	2	0	1	-3	1	0

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