

NAB Monthly Business Survey

by NAB Group Economics

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Key Points:

- The NAB Business Survey suggested a slight easing in business conditions in December, but showed little signs (beyond normal monthly volatility) of a fundamental weakening in the non-mining recovery. Business conditions eased back to (still above average) +7 index points in December (from +10), as sales, profitability and employment all took a step back. Employment conditions eased back to neutral – a reading consistent with modest employment growth but counter to the (well) above trend employment growth reported in the official statistics. **Service sectors remain the best performers**, although it was disappointing to see a **sharp moderation in retail conditions**, while **very weak construction** could point beyond the mining downturn to suggest that the peak in the residential construction cycle may be fast approaching. **Capacity utilisation – a useful measure of the underlying health of the economy – eased significantly this month**, which, if maintained, could pose a hurdle for future business investment. That said the trend still remains reasonably positive. Also on the positive side, **forward orders lifted this month**, indicative of a potential pick up in activity in the near term.
- **Business confidence remains positive, despite pulling back on escalating concerns over the global economic outlook (particularly in China) and big declines in oil and equity markets since the start of the year.** While these market moves highlight potential risks, relatively positive business conditions appear to have, so far, acted to reassure business sentiment. Global equity markets were down around 10% from the time of the previous monthly survey reading. Domestic factors may also be at play, with the largest declines in confidence concentrated in the construction sector – consistent with falling mining investment and moderating housing markets.
- Recent financial market turmoil certainly highlights the risks to the outlook, but has not fundamentally changed our view of the Australian economy. Business conditions remain well above average in fundamental (trend) terms, and business confidence has been surprisingly robust in the current financial environment. Positive business conditions in most industries suggest a relatively broad based recovery in the non-mining sector is underway (services leading the way), although the deterioration in construction will be monitored closely. Given our underlying expectation for the non-mining recovery to remain on track, monetary policy is expected to remain on hold for an extended period.

Table 1: Key monthly business statistics*

	Oct 2015	Nov 2015	Dec 2015		Oct 2015	Nov 2015	Dec 2015
	<i>Net balance</i>				<i>Net balance</i>		
Business confidence	3	5	3	Employment	3	2	0
Business conditions	10	10	7	Forward orders	-2	2	4
Trading	16	16	13	Stocks	1	2	4
Profitability	9	11	8	Exports	1	1	1
	<i>% change at quarterly rate</i>				<i>% change at quarterly rate</i>		
Labour costs	0.4	0.5	0.7	Retail prices	0.6	0.6	0.5
Purchase costs	0.9	0.7	0.5		<i>Per cent</i>		
Final products prices	0.4	0.3	0.3	Capacity utilisation rate	81.2	80.8	80.0

* 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 11 Jan to 15 Jan, covering over 400 firms across the non-farm business sector.

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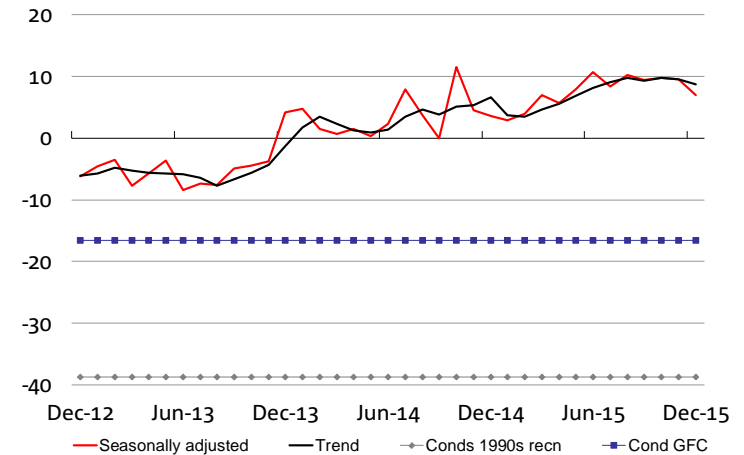
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Analysis

- **Business conditions eased back in the month, but remains above the long run average**, suggesting that despite concerns in the market, the recovery in the non-mining economy remains largely on track. Business conditions eased to +7 index points (from +10), above the long-run and post-GFC averages of +5 and +2 respectively. **The pull-back was experienced across all components** (sales, profits and employment), but outcomes across industries were quite mixed. The result for **employment conditions suggest neutral demand for labour**, somewhat at odds with the very strong results evident in the official ABS labour force survey.
- The change in business conditions **varied considerably across industries as construction and retail experienced the brunt of the decline**, with the former now posting the weakest conditions (at -8 index points). Ongoing declines in mining investment could explain construction weakness, however, a pull back in conditions for both NSW and Vic may suggest a moderation elsewhere (including the residential space). Nevertheless, **all but 2 of the 8 major industry groups (construction and mining) have reported positive business conditions**. Services sectors (outside retail) held up reasonably well during the month, remaining notable outperformers
- **Business confidence eased back a little in the month, but held up quite well in light of large declines in equity markets and oil prices** – triggered concerns over the global economic outlook. It appears as though positive business conditions are (for now) buffering sentiment from these market fluctuations. Business confidence remains positive despite falling to +3 index points, down from +5, although this is below the series average (+6). Global uncertainties appear to be the most likely factor behind the deterioration, although more concentrated declines in construction could suggest domestic factors are also at play – such as the cooling housing markets in Sydney and Melbourne.
- **The falls in confidence was relatively concentrated**, with construction seeing the largest falls (down 12), followed by manufacturing (down 8) and fin/prop/ bus services (down 6). The latter dipped into negative territory in the month, despite very strong business conditions, suggesting particularly high sensitivity to financial market turmoil. Unsurprisingly, mining confidence is lowest and is expected to remain weak. In contrast, construction confidence is the highest, despite the large deterioration in the month – a reflection of the extremely large residential construction pipeline.
- Business conditions weakened in Vic, WA and NSW during the month, but **looking through the monthly volatility shows conditions remaining very elevated in the major eastern states**. In contrast, trend conditions are negative for WA and remain relatively subdued in SA and Qld. Despite this, confidence in Qld has remained at high levels, and are positive in SA. Confidence in NSW and Vic dropped in December, but remains positive in trend terms.

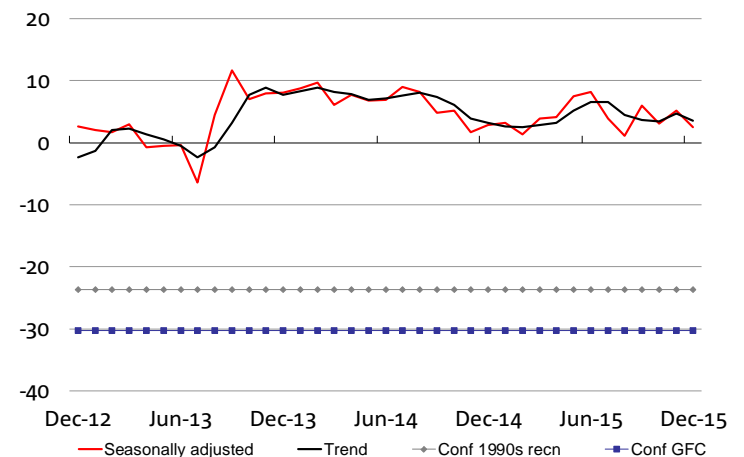
Conditions eased, but still solid

Business Conditions (net balance)



Confidence resilient despite market turmoil

Business Confidence (net balance)



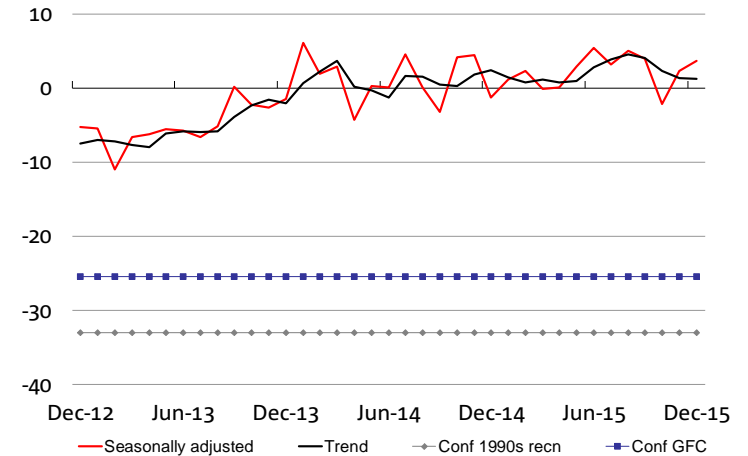
Excluding normal seasonal changes, how do you expect the business conditions facing your industry in the next month to change?

Other activity indicators

- The **forward orders** index rose further last month, increasing to +4 index points, from +2. This brings the index more into line with the most recent high of +5 (in August), but is above the long run average of the series. **Encouragingly, this suggests more of an expansion in activity in the near-term**, which should help to keep business conditions elevated in the coming month.
- The improvement in orders was not, however, experienced across all industries. Orders were surprisingly strong in mining (up 54), which does not align with an apparent softening in global commodity demand at present, and may simply represent monthly volatility. In trend terms, mining orders remain quite weak at -11 index points. Elsewhere, orders also increased in fin/ prop/ bus (up 6), recreation & personal services (up 1), construction (up 1) and manufacturing. In contrast, retail, wholesale and transport each reported notable declines (down 10, 9 and 6 points respectively). In trend terms, orders are still strongest in construction (+13), reflecting a record pipeline of residential construction projects that is helping to offset a rapidly depleting pipeline of mining projects. In contrast, outside of mining (-11), the orders index was next weakest in retail (-4), then wholesale (-3). All other industry groupings were positive.
- NAB's measure of **capacity utilisation dropped again last month** (to 80% from 80.8%), despite better trading conditions, although outcomes were quite mixed across industries; utilisation rates actually rose notably in wholesale (up 3.3 ppts) and transport (up 2 ppts). Capacity utilisation deteriorated the most in recreation & personal services (down 3.1 ppts) and retail (down 2.8 ppts). As a result of recent declines, **trend utilisation has also begun to ease, but remains reasonably positive**, which coincides with a significant improvement in the labour market. Nevertheless, utilisation rates remain well below pre-GFC levels and are only at, or below, long run averages for most industries – helping to explain persistently weak investment intentions in the official data.
- Despite the rise in spare capacity, the **capital expenditure index was slightly higher** in month at +8 index points, and while the index is down from the highs of 2015, it has sustained the prominent gains recorded over recent years – remaining above its long-run average level (+5). Above average capex **points to a stronger expansion of non-mining business investment** (which has a higher weighting in the survey). In trend terms, capex in recreation/personal services is the highest (+13 points) and transport & utilities is lowest (-4 points) – the only industry with a negative index (trend).
- Elsewhere in the survey, **cash flow** (not seasonally adjusted) was the strongest in personal & recreational services, and the weakest in mining.

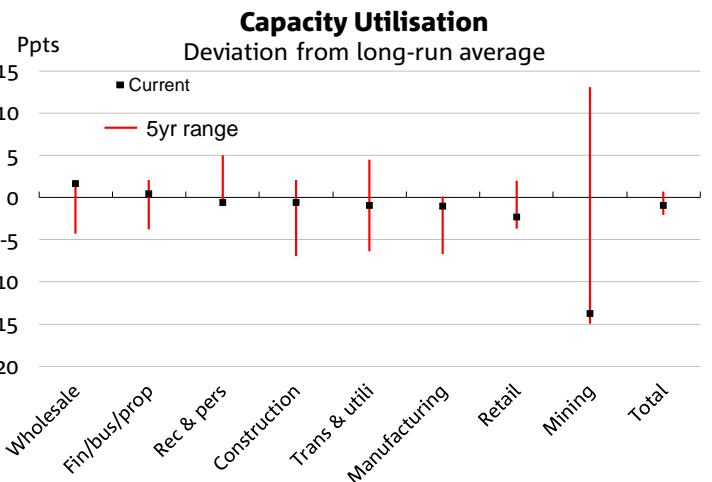
Sales orders partially recover

Forward Orders (net balance)



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

Capacity utilisation by industry



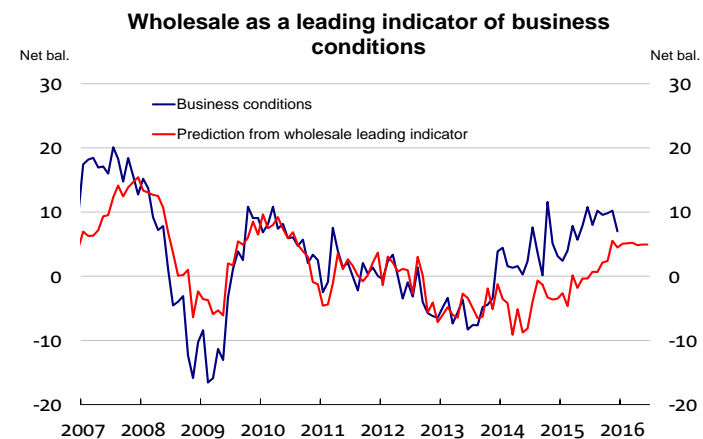
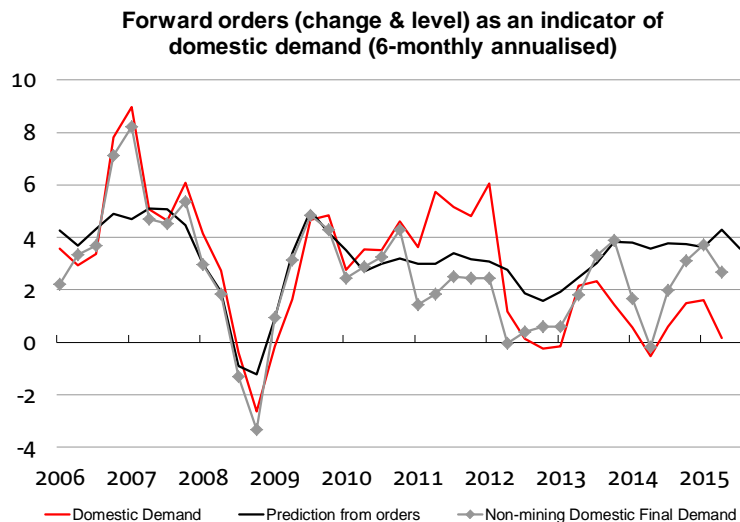
Source: NAB Economics

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

Implications for forecasts

For more information see latest [Global & Australian Forecasts](#)

- Global growth continues to disappoint and remains sub-trend as the slowdown continues across many emerging market economies. The latest bout of financial market volatility and sliding commodity prices illustrate the risks hanging over even this sub-par upturn but our view is that the global economy can yet again muddle through this market instability and maintain moderate growth. The risks are, however, weighted toward worse rather than better outcomes.
- The outlook for the Australian economy is essentially unchanged despite global risks and we continue to anticipate further gradual recovery across the non-mining economy. The AUD (now expected to depreciate to USD66c by mid-2016) will continue to act as a pressure valve, the tilt towards services activity will support employment, and lower petrol prices will support the cash flow position of most households and businesses. Resource export volumes will remain strong, although the associated income and government revenue will of course be challenged by low commodity prices. Overall, real GDP is forecast to pick up gradually to 2.7% in 2016 and 3.0% in 2017. The unemployment rate track has been revised given the lower starting point, and is now expected to ease to 5.6% by end-16 and 5.5% by end-17. For the RBA, unless financial market volatility translates into substantive negative real economic outcomes offshore, the central bank is likely to remain on the sidelines and observe developments, while continuing to focus on solid momentum in non-mining economic activity.
- **Our model of 6-monthly annualised demand growth, using forward orders as a predictor, has continued to suggest stronger growth than the National Accounts.** This divergence can be partly explained by the greater representation of non-mining sectors in the business survey – headline growth in the National Accounts has masked recent improvements in non-mining domestic demand. Nevertheless, applying forward orders from December to our model suggests that predicted domestic demand growth for Q4 could be a little softer than in Q3.
- **Business conditions derived from our ‘wholesale leading indicator’ (below), which has previously had a good leading relationship with economic activity, would imply a somewhat weaker business environment than the headline index suggests** – although this could reflect margin squeeze from AUD depreciation given the difficulty passing on additional costs to retailers and final consumers. But while wholesale conditions have been soft for quite some time, cash flows apparently improved and trend conditions remained positive in the month.

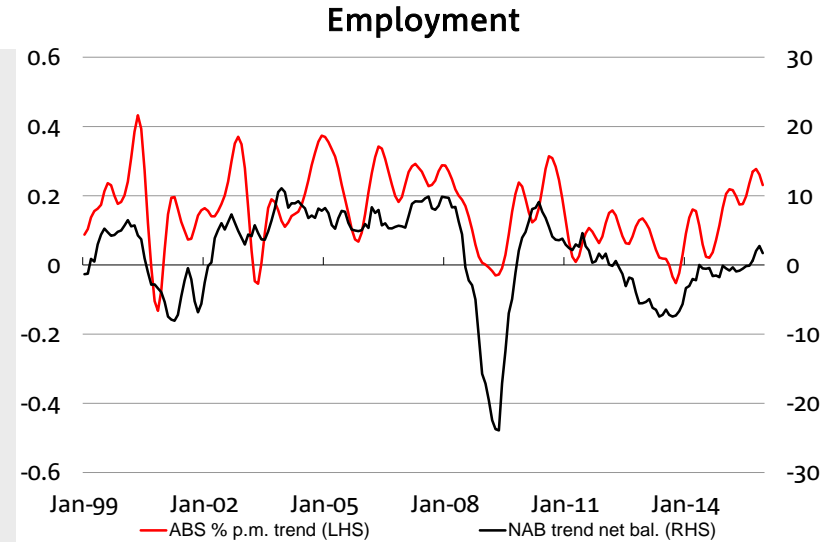


Indicator = f (business conditions wsl, business conditions wsl(-1 to -4), const.

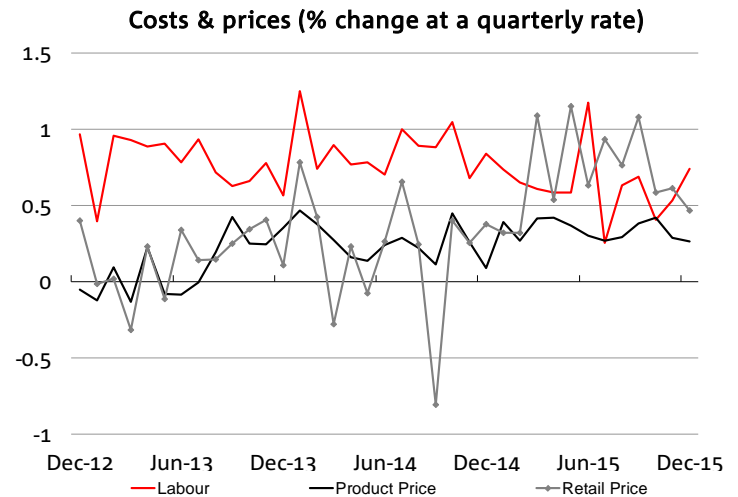
Costs, prices & labour

- The **NAB Survey's employment index eased back again in December** (to 0, from +2), pointing to less momentum in employment growth in the coming 6 months – suggesting annual job creation of around 180k (15k per month). This compares to a trend increase of 27.4k in December according to the ABS. The fall in employment conditions was particularly pronounced in a handful of industries, namely retail (down 20) and construction (down 17), consistent with a deterioration in business conditions for these industries. In contrast, manufacturing recorded a reasonable gain (up 9), as did recreation & personal services (up 5). In trend terms, the employment index is still very negative for mining (-11 points), despite a modest improvement in the month, while service industries (including retail) are reporting the strongest employment demand. The retail employment trend remained highest despite the big deterioration in the month.
- Labour costs growth (a wages bill measure) accelerated slightly in the month (up 0.2 pts), but remains well contained – at 0.7% (a quarterly rate). Moderate labour cost growth is consistent with the currently elevated – albeit improving – rate of unemployment, subdued inflation expectations, and an apparent shift in labour toward lower average income sectors (relative to high income industries such as mining). Labour cost inflation accelerated the most in construction (up 1.1 pts), with this industry now showing the highest rates of quarterly labour cost growth (1.3%). In contrast, labour costs in mining have continued to decline (-1.9%).
- Growth in purchase costs eased to 0.5% in December (at a quarterly rate), falling 0.2 pts in the month. This is below the long-run average and towards the lower end of rates seen since the GFC. More subdued growth in purchase costs is a little surprising given pressures on the currency, including renewed declines in the AUD TWI since the start of the year – although subdued inflation pressures have been a common theme globally. Growth in purchase costs decelerated the most in wholesale (down 0.8 pts), but picked up notably in construction (up 0.6 pts). Despite easing, purchase cost pressures remain highest in wholesale (1.1%, quarterly rate) and retail (0.9%), while purchase costs have continued to fall in mining.
- Final product prices growth was unchanged in December at a quarterly rate of 0.3%. Despite only modest hikes in product prices, firms have managed to maintain reasonable profitability as a result of subdued global inflation pressures and labour cost. Final prices growth was, however, mixed across industries, with the greatest slow-down occurring in wholesale (down 0.5 pts), while mining experienced a surprising pick up (up 1.4 pts). Nevertheless, final prices continue to fall in mining (-0.2%, quarterly rate), as well as construction (-0.1%), while price growth was highest in manufacturing (0.7%). Retail prices were consistent with the lower bound of the RBA CPI inflation band (0.5%, quarterly rate).

Employment subdued, but trending up



Price pressures generally subdued

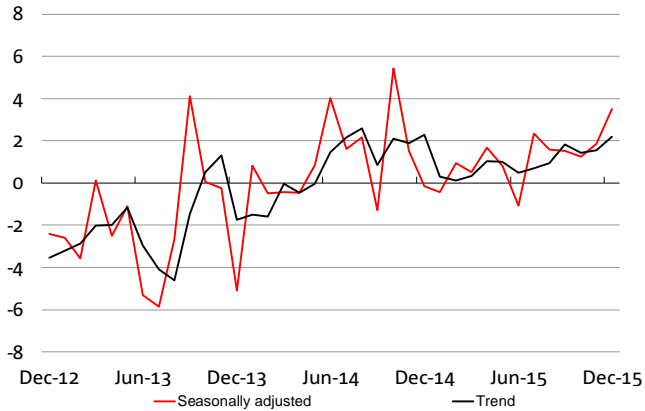


Based on respondent estimates of changes in labour costs and product prices. Retail prices are based on retail sector product price estimates.

More details on business activity

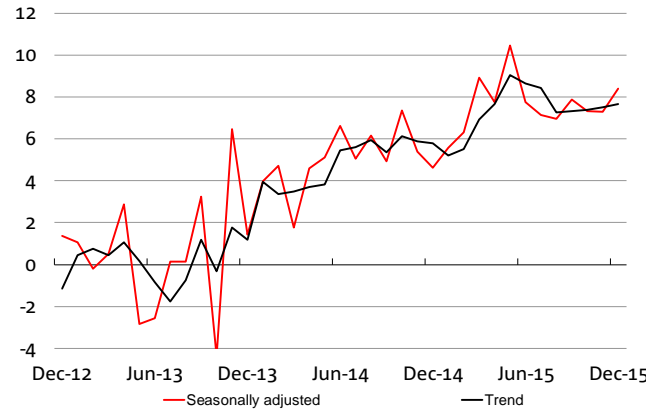
Firms ramping up re-stocking

Stocks (net balance)



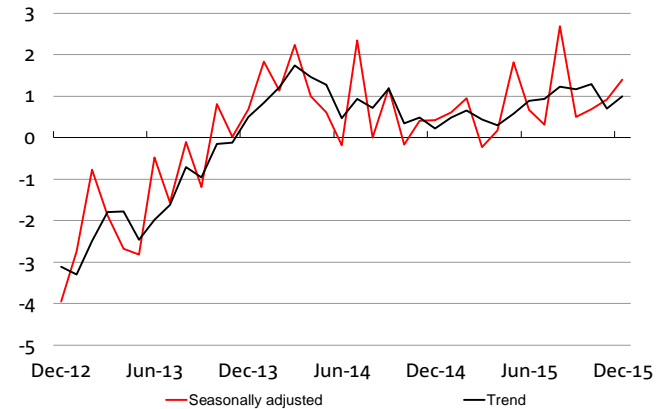
Capex momentum holding steady at solid levels

Capital Expenditure (net balance)



Exports picking up only gradually

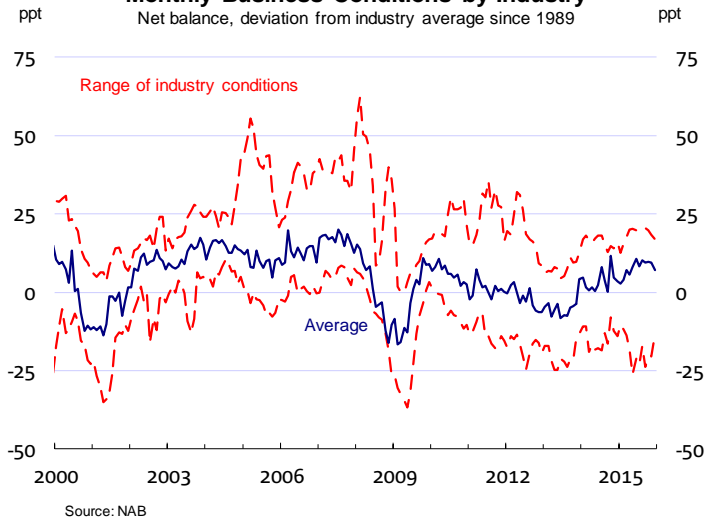
Exports (net balance)



Range of conditions narrowing as the top eases, but underperformers improve

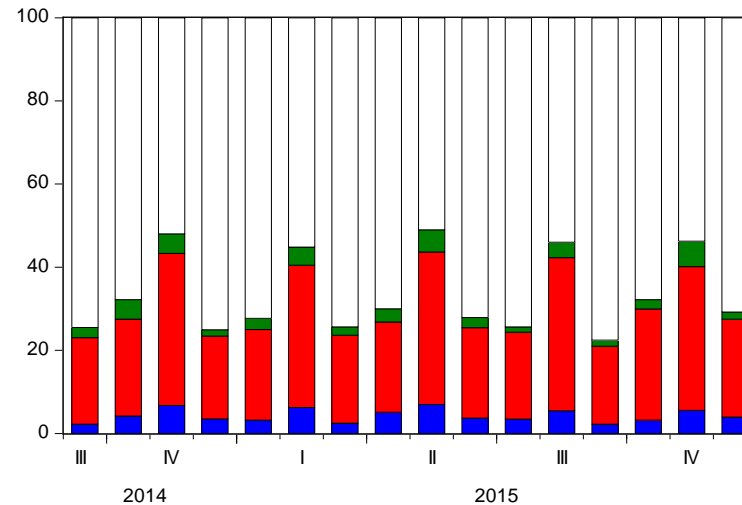
Monthly Business Conditions by Industry

Net balance, deviation from industry average since 1989



Borrowing conditions deteriorate in past 3 months, but demand for credit rose

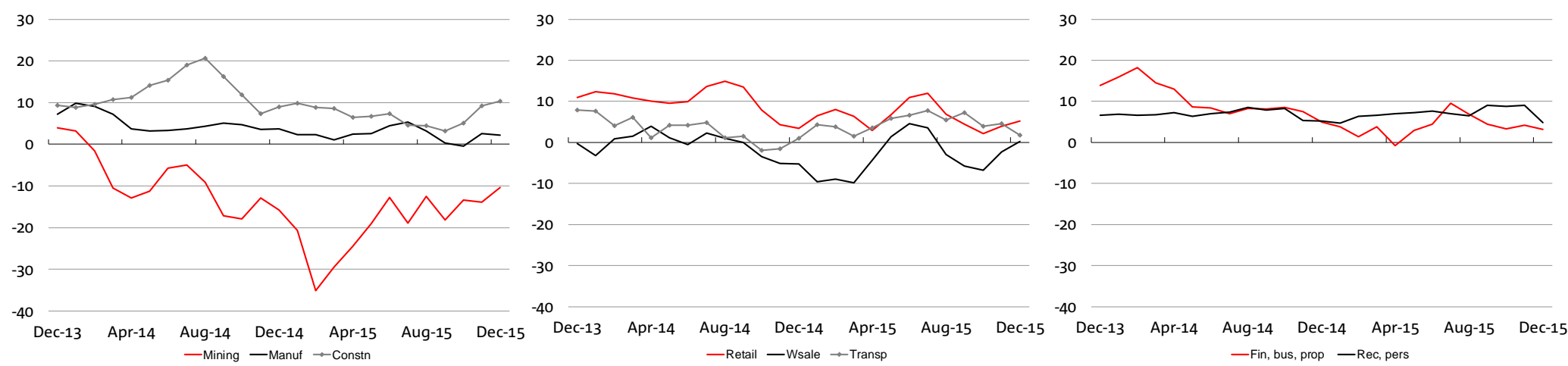
Borrowing conditions (% of firms)



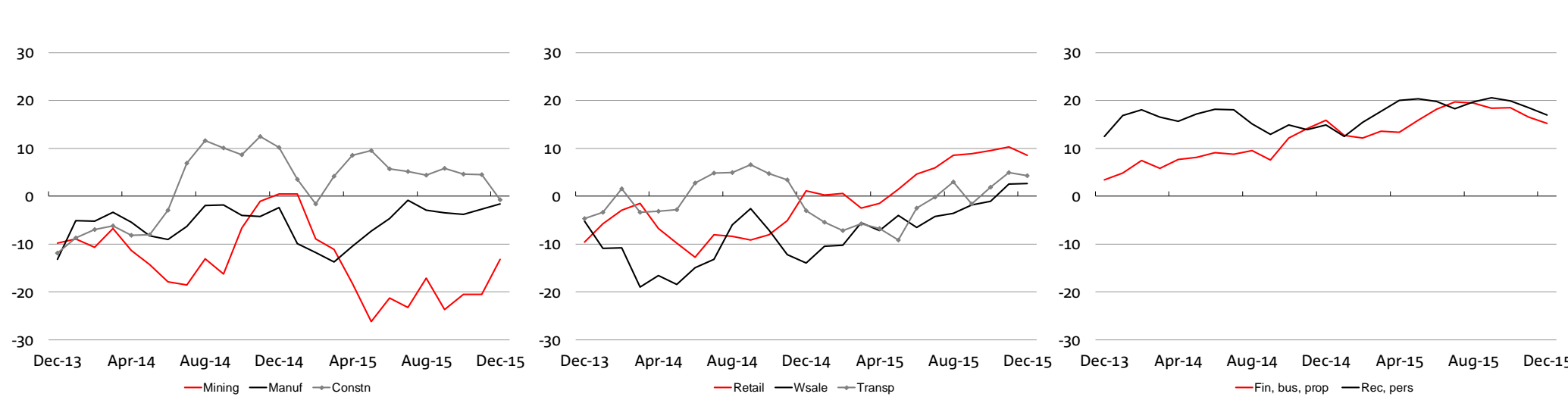
More difficult Unchanged Easier No borrowing required

More details on industries

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

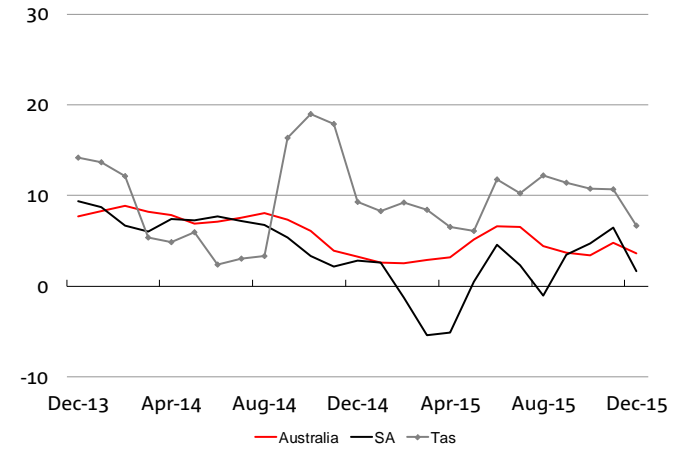
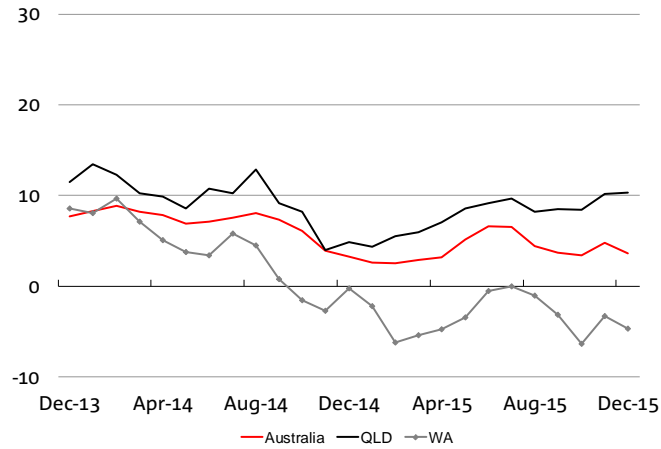
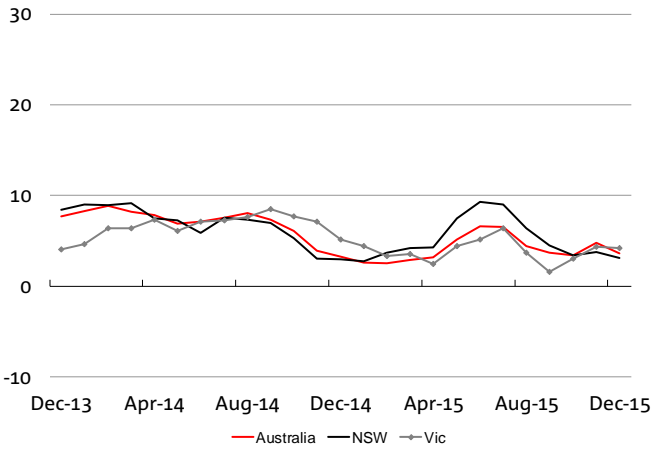


Business conditions by industry (net balance): 3-month moving average

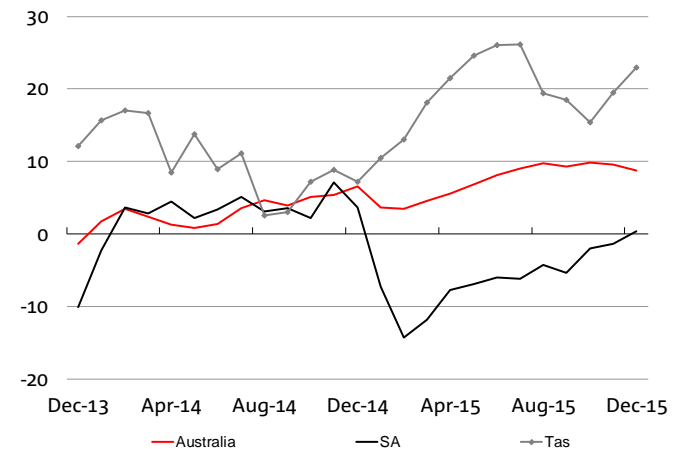
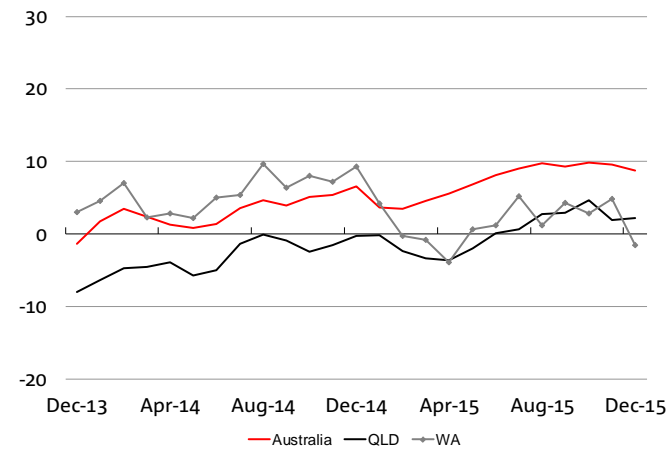
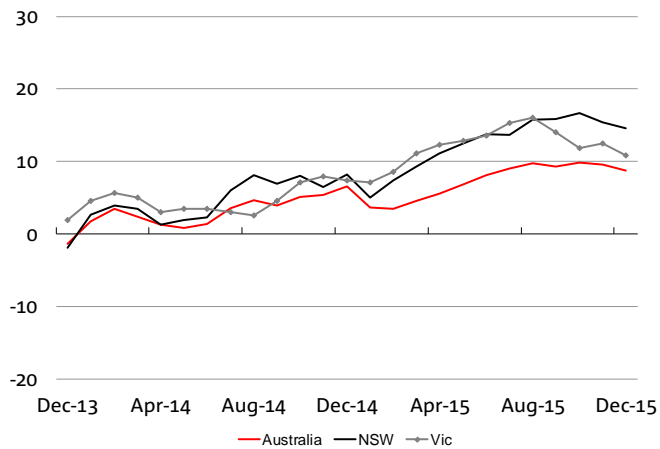


More details on states

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)

Dec-2015	Mining	Manuf	Constn	Retail	Wsale	Tran. & utils	Rec. & pers.	Fin. prop. & bus.	Australia
Labour costs: current	-1.9	0.7	1.3	0.3	0.1	1.1	1.1	1.0	0.7
Labour costs: previous	-1.1	0.4	0.2	0.5	0.5	0.4	0.8	0.6	0.5
Labour costs: change	-0.8	0.3	1.1	-0.2	-0.4	0.7	0.3	0.4	0.2
Prices (final): current	-0.2	0.7	-0.1	0.5	0.5	0.5	0.4	0.0	0.3
Prices (final): previous	-1.6	0.2	-0.2	0.6	1.0	0.1	0.5	0.1	0.3
Prices (final): change	1.4	0.5	0.1	-0.1	-0.5	0.4	-0.1	-0.1	0.0
Purchase costs: current	-0.6	0.1	0.8	0.9	1.1	0.2	0.5	0.6	0.5
Purchase costs: previous	-0.2	0.7	0.2	1.0	1.9	0.6	0.7	0.4	0.7
Purchase costs: change	-0.4	-0.6	0.6	-0.1	-0.8	-0.4	-0.2	0.2	-0.2

Key state business statistics for the month

Dec-2015	Monthly Business Survey Data: By State						
	NSW	VIC	Qld	SA	WA	Tasmania	Australia
Bus. conf.: current	3	0	9	3	-3	5	3
Bus. conf.: previous	6	4	11	2	-2	14	5
Bus. conf.: change	-3	-4	-2	1	-1	-9	-2
Bus. conf: current - Trend	3	4	10	2	-5	7	4
Bus. conf: previous Trend	4	4	10	6	-3	11	5
Bus. conf.: change -Trend	-1	0	0	-4	-2	-4	-1
Bus. conds: current	12	7	3	5	-5	24	7
Bus. conds: previous	17	15	-5	-3	3	23	10
Bus. conds: change	-5	-8	8	8	-8	1	-3
Bus. conds: current -Trend	15	11	2	0	-2	23	9
Bus. conds: previous -Trend	15	13	2	-1	5	20	10
Bus. conds: change -Trend	0	-2	0	1	-7	3	-1

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