NAB Monthly Business Survey

by NAB Group Economics

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April 2016

National Australia Bank

Key Points:

- **The NAB Business Survey continues to point to a very favourable business environment for Australian firms**, despite giving up some of the strong gains witnessed in last month's survey. Business conditions eased back to +9 points in April, but this was still an above-average result that is consistent with an ongoing recovery in the non-mining economy. **Service industries have persistently been the best performers, although other sectors including manufacturing and transport are looking relatively upbeat** – as the benefits of lower oil prices and earlier AUD depreciation continue to flow through. Retail also lifted, having disappointed in recent months. The trading (sales) and profitability components both eased in April, but remained quite positive, while **employment held on to the gains achieved last month** – suggesting ongoing resilience in the labour market.
- **Business confidence was somewhat resilient to the fall in conditions**, but ebbed lower in the month to be back to slightly below the series average. Changes in confidence varied across industries, but mining and wholesale were the only sectors showing negative confidence levels. Other forward indicators from the survey were relatively mixed. **Forward orders lifted back into positive territory**, although were still at subdued levels, while inventories and capital expenditure both rose marginally -- the improvements in these areas were primarily driven by mining and construction firms. However, capacity utilisation fell in April, with declines seen across most industries, although mining was the most notable exception, followed by retail.
- Looking through the month-to-month volatility in the Survey, **these results confirm a continuation of the favourable business environment that has helped to underpin the non-mining recovery**. We continue to look for signs that the recovery is broadening, and while evidence of that was a little less compelling this month, solid results for manufacturing and transport – as well as a bounce-back in retail – are encouraging. Low interest rates and a more competitive currency (even given its recent strength) remain key to ongoing improvement, especially in the context of global economic uncertainty. Importantly, the survey suggests that inflation pressures remain subdued, while core inflation in Q1 hit its lowest level since the RBA began inflation targeting, according to the ABS. This means that despite positive outcomes in activity data, the RBA has scope to further cement the non-mining recovery with an additional rate cut – a move that seems more likely than not at its May's policy meeting (although we see it as a close call).

Table 1: Key monthly business statistics*

	Feb 2016	Mar 2016	**Apr 2016**		Feb 2016	Mar 2016	**Apr 2016**
		Net balance				*Net balance*	
Business confidence	3	6	**5**	Employment	1	4	**4**
Business conditions	9	12	**9**	Forward orders	3	-1	**2**
Trading	13	17	**15**	Stocks	11	2	**3**
Profitability	11	15	**9**	Exports	2	0	**0**
		% change at quarterly rate				*% change at quarterly rate*	
Labour costs	0.7	0.7	**0.6**	Retail prices	0.3	0.5	**0.3**
Purchase costs	0.5	0.5	**0.2**			*Per cent*	
Final products prices	0.2	0.1	**0.1**	Capacity utilisation rate	81.5	82.1	**81.4**

* 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 15 to 21 Apr, covering over 400 firms across the non-farm business sector.

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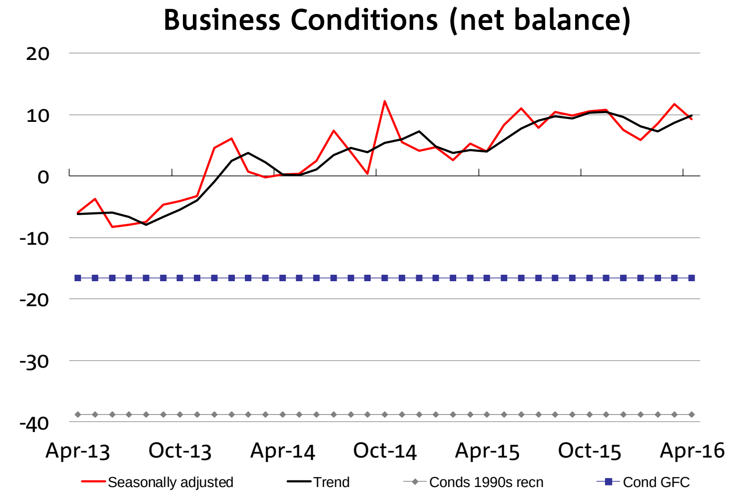
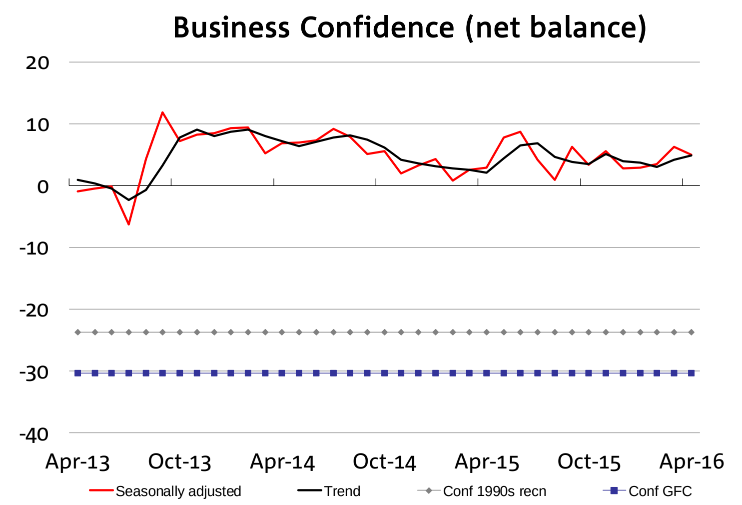
Analysis

- **Business conditions remain at very good levels, despite giving back the gains obtained last month.** The index eased to +9 index points in April (previously +12), which was still well above the series long-run average of +5. Looking through the usual volatility, business conditions have maintained levels that give no sign of the non-mining recovery burning out – trend conditions have remained above average levels for the past 12 months. The fall in conditions was primarily driven by a drop in profitability, although trading conditions also eased. However, employment conditions held on to the gains seen last month, consistent with recent improvements in the unemployment rate.
- Industry outcomes for business conditions provided less evidence of a broadening non-mining recovery (beyond the services sector) compared to last month, but a number of additional industries looked more upbeat. Retail conditions (up 7) more than bounced back from last months decline, but finance/ property/business (FPB) services were the only other industry to improve in April. In contrast, there was a surprisingly large decline in construction (given the elevated levels of residential construction activity), although this may reflect weakness in non-residential segments. In level terms, conditions in the services sector (FPB and personal services) were still the clear outperformers, although a majority of industries have conditions above long-run average levels.
- **Business confidence eased as well in the month, but maintained most of the previous months gains.** The confidence index eased 1 point to +5 index points in April, but this was marginally below the long-run average for the series. Confidence remains crucial to the outlook, but this was still a reasonable outcome given the added uncertainties around the global economy and the upcoming Federal Budget and election. Confidence has not dipped below zero since mid-2013, suggesting firms have remained firmly focussed on the improving conditions within their own business.
- **Confidence was positive for most industries outside of mining and wholesale,** although changes in confidence over April varied notably. The largest gains occurred in construction (up 6), followed by retail (up 5). In contrast, wholesale (down 11) and mining (down 4) posted notable declines – mining fell despite surprising strength in some commodity prices of late. In trend terms, however, transport/utility and construction firms were the most confident. In contrast, mining confidence was lowest and is expected to remain weak.
- Business conditions fell notably in WA (down 14) and Victoria (down 13). This was only partially offset by a big gain in NSW (up 11) and a moderate lift in SA (up 3). In trend terms, conditions are positive in all states other than WA, with the major eastern states still the best performing of the mainland states. In terms of confidence, Qld and SA both fell 7 points in April, while confidence in WA (up 6) turned positive. In trend terms, NSW and Vic were solid, but Qld had the most confident firms on the mainland, while WA remains negative.

Conditions eases, but still solid



Confidence dips moderately below average

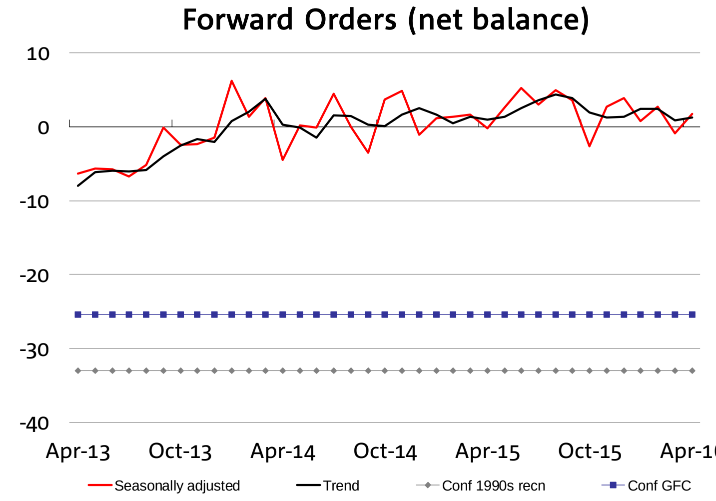


Excluding normal seasonal changes, how do you expect the business conditions facing your industry in the next month to change?

Other activity indicators

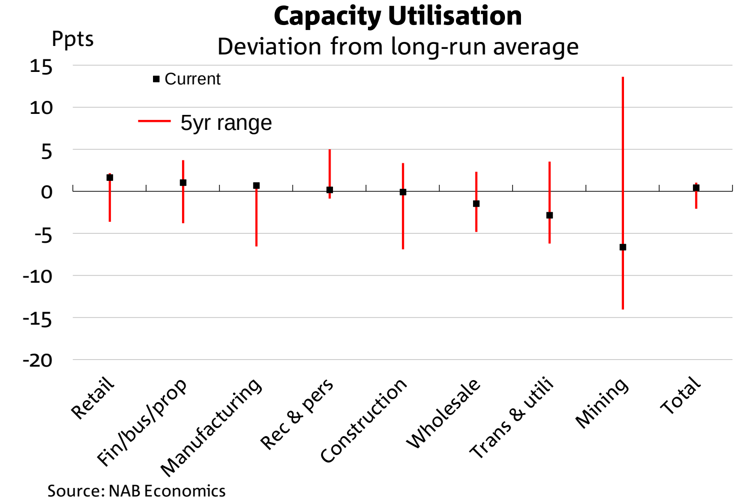
- Indicators of the near-term outlook were varied in April. The **forward orders** index regained some lost ground, lifting back into positive territory. At +2 index points (up from -1), the index was above the long-run average, which was more consistent with business conditions and **suggests good near-term prospects for activity.** However, only a small subset of industries have notably positive orders at present, while most remain negative – despite many of these improving in the month.
- **The rise in orders was most pronounced in mining (up 29)**, followed by a more moderate increase in construction orders (up 11). This reflected only a partial recovery of the large decline in construction orders last month, which may be attributed to the recent pullback in residential building approvals (although they are still elevated) and a continuation of muted growth in non-residential approvals. Orders also rose a lot in wholesale (up 9), followed by retail (up 7). In contrast, only two industries recorded a deterioration in the orders index with manufacturing (down 7) falling the most, followed by finance/ property/ business services (down 4). In trend terms, orders were still weakest in mining at -17 index points, followed by wholesale (-10). Elsewhere, trend orders are now strongest in manufacturing (+13), which could suggest that a more competitive AUD was having a positive impact on the industry, while construction was the next highest.
- NAB's measure of **capacity utilisation eased back in the month, but the trend remains very much a positive one.** Utilisation rates fell to 81.4% (from 82.1%), but remains above the long-run average of 81%, supported by the strength in trading activity (and an apparent lack of new investment). Outcomes were worse for most industries, with only mining (up 2.4 ppts) and retail (up 0.8 ppts) seeing an increase, while utilisation rates in around half of the industries were below average (chart) – especially in mining and transport. The deterioration was largest in transport (down 3.2 ppts), followed by finance/ property/ business services (down 2.7 ppts).
- Despite an easing in trading conditions and capacity utilisation, the capital expenditure index improved marginally in the month, up 1 point, to be consistent with the series long-run average of +5. This suggests average rates of growth in non-mining investment (as non-mining sectors have a larger weighting in the survey), which was a better result than ABS data would suggest (including negative Capex Survey expectations). In trend terms, capex in transport/utilities was the highest (+14 points) and mining was unsurprisingly the lowest (-29 points) – the only industry with a negative index (trend).
- Elsewhere in the survey, **cash flow** (not seasonally adjusted) was the strongest in finance/ property/ business services, and the weakest in mining – suggesting better than expected commodity prices of late have yet to help cash flows.

Sales orders surprisingly soft



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

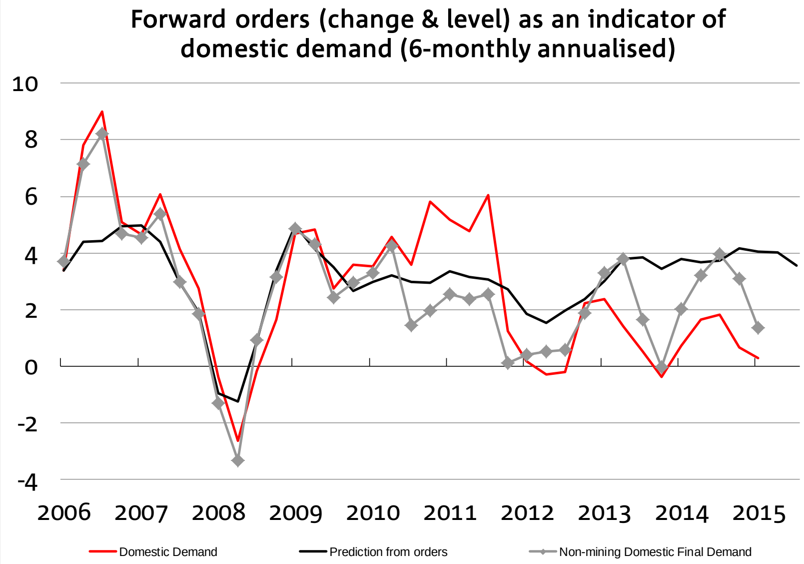
Capacity utilisation by industry

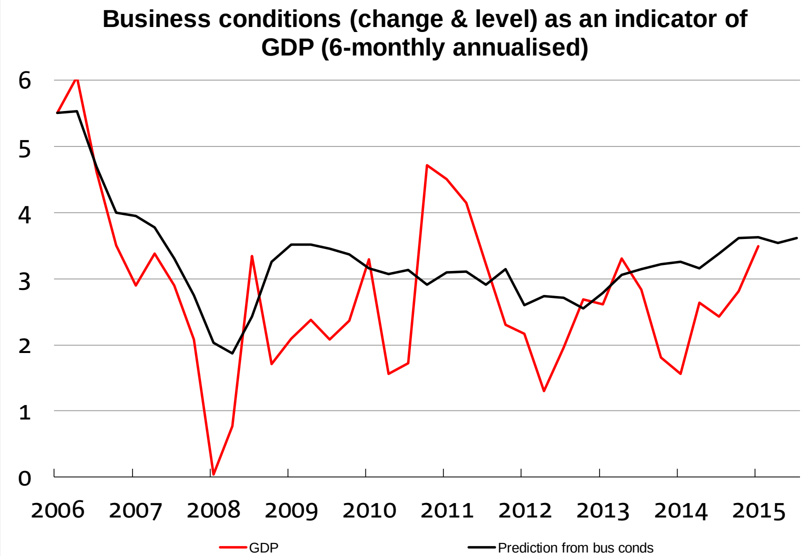


Full capacity is the maximum desirable level of output using existing capital equipment.

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

- Global share markets have regained much of their early 2016 losses, financial market volatility has subsided and both commodity prices and the Chinese currency have stabilised – helping to reduce the risk of a renewed downturn in global economic activity. However the backdrop to these market movements remains one of very sluggish sub-trend growth, inflation that is below target in major economies, difficulty in increasing revenue as margins are sacrificed to win modest volume gains, slow wage growth cramping spending increases, high levels of debt and central banks that have used up much of their policy ammunition. Despite the many risks, we still think global growth will muddle through 2016 at around the 3% rate seen last year but it could be a bumpy ride with plenty of further scope for volatility, reflecting the numerous triggers for further bouts of market jitters.
- On Australia, our real GDP forecasts currently anticipate 2.7% growth in 2016 and 3.0% in 2017, before easing to 2.5% in 2018 as the large contribution from net exports dissipates. The unemployment rate is also expected to continue improving in the near-term before stabilising – although our economic forecasts will be revised following this weeks Federal Budget. While recent AUD appreciation presents a downside risk to economic activity, we doubt that this move higher will be sustained and expect the downward trend to resume as the year progresses. Despite this, core inflation in Q1 hit its lowest level since the RBA began inflation targeting and is likely to undershoot their inflation target band in the near-term. This suggests there are very few downside risks (although there are some) to the RBA doing a little more to reduce Australia's unemployment rate faster. Consequently, it seems more likely than not that the RBA will cut the cash rate by a further 25bp at the May policy meeting, although it is likely to be a close call. This does not change the fact that we remain optimistic about the near-term performance of the Australian economy and labour market, especially on the east coast of Australia. However, growing headwinds expected from 2018 mean we are reviewing our rate hikes previously anticipated for 2017.
- **Our model of 6-monthly annualised demand growth, using forward orders as a predictor, has been suggesting 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 had masked recent improvements in non-mining domestic demand, although some of the momentum has begun to wane. Applying Q1 and April trend conditions to our model suggests solid (but moderating) domestic demand growth for H1 2016.
- Similarly, business conditions have over-predicted GDP growth, although the gap has begun to close more recently. **Based on strong business conditions of late, our model implies steady (solid) GDP growth for Q1 2016.**

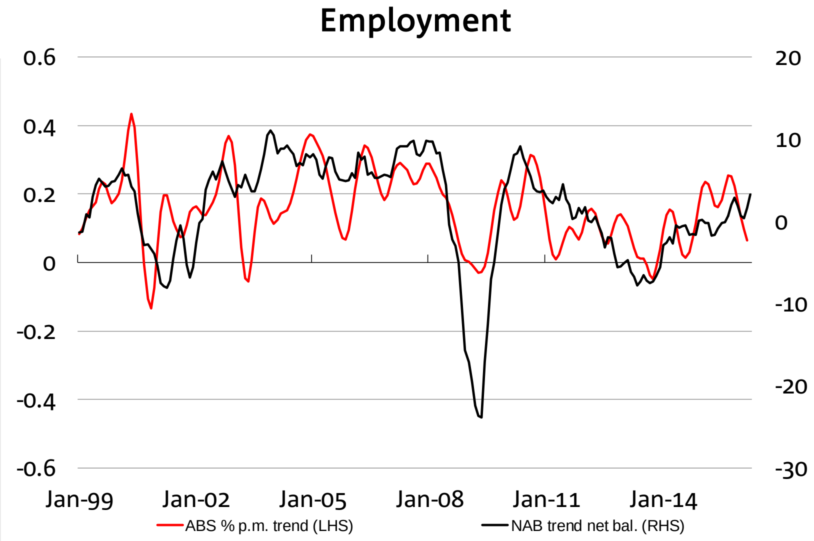




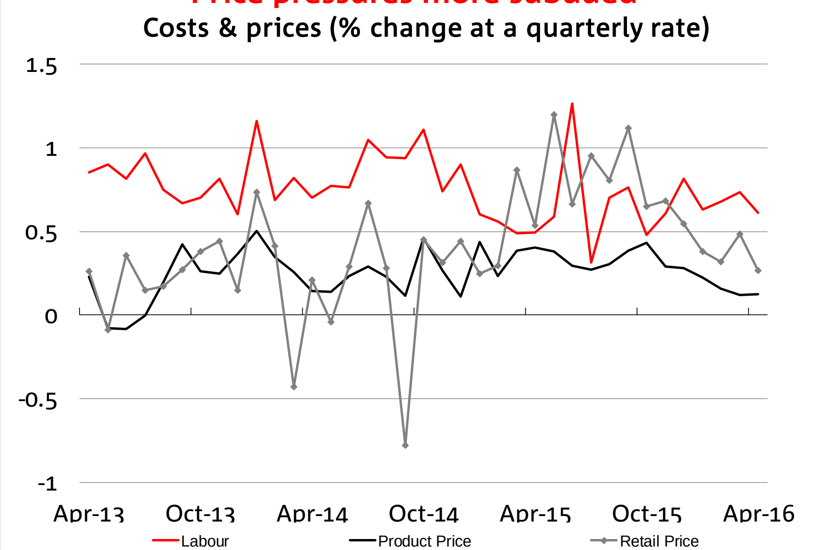
Costs, prices & labour

- The **NAB Survey's employment index held on to last month's gain, despite a dip in overall conditions.** The employment index remained at +4 index points in April, maintaining a level that points to a clear long-running positive trend. Recent solid outcomes for the index are somewhat in contrast to official labour market statistics, which suggest that employment growth has lost momentum of late – although this follows a period of much stronger growth in employment. This outcome hints at an annual job creation rate of around 220k (close to 18k per month) in coming months, which compares to a trend increase of just 7.7k in March according to the ABS.
- Although total employment conditions were unchanged, this masks **varied outcomes across industries**. Retail (up 6), recreation & personal services (up 5) and wholesale (up 3) all posted improvements, but this was **offset by sharp falls in mining (down 24) and construction (down 11), with all remaining industries also down**. In trend terms, the employment index was still very negative for mining (-23 points), followed by transport (-3 points) and wholesale (-2). The strongest employment demand (trend) was in finance/ property/ business services (+10) and (surprisingly) manufacturing (+10).
- **Labour cost growth (a wage bill measure) eased a little in the month**, suggesting wage pressures remain relatively contained – at 0.6% (a quarterly rate). Restrained labour cost growth is consistent with the currently elevated – albeit improving – rate of unemployment, subdued inflation expectations, and other shifts in the composition of employment. Labour cost pressures were highest in wholesale (1.3%), but still falling in mining (-2%).
- **Growth in purchase costs were also down to 0.2% in April (at a quarterly rate, from 0.5%).** This was below the long-run average and is very weak relative to the history of the series. More subdued growth in purchase costs is a little surprising given the pressure from currency depreciation – although subdued inflation pressures have been a common theme globally. Growth in purchase costs decelerated the most in wholesale and construction (both down 0.8 ppts), but rose the most in transport (up 0.1 ppts). Purchase cost pressures were softest in mining (-0.2%), but highest in manufacturing, recreation & personal services and transport (all 0.3%).
- Final product prices growth in April remained at just 0.1% (a quarterly rate). Final prices growth was, however, mixed across industries, with the greatest slowdown occurring in finance/ property/ business (down 0.7 ppts), while mining experienced the largest pick-up (1.4 ppts higher). Construction prices are falling (-0.6%) despite strong residential building activity, while Fin/ Prop/ Bus (-0.4%) and transport prices (-0.1%) are also lower. Prices are flat to rising elsewhere, with price growth highest in mining and recreation & personal services (both 0.5%). **Growth in retail prices (0.3%, quarterly rate) was consistent with a CPI below the RBA's target inflation band.**

Employment maintained recent gains



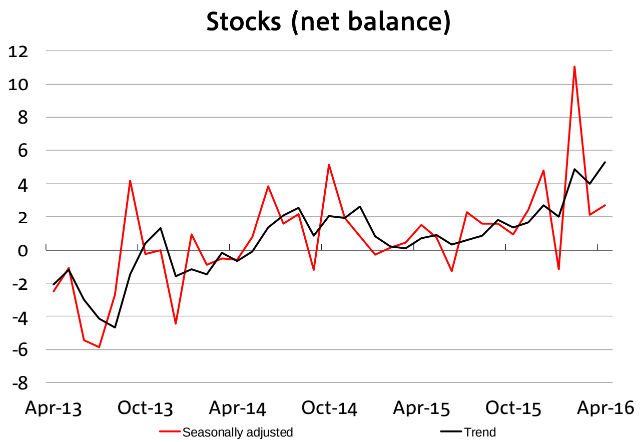
Price pressures more subdued



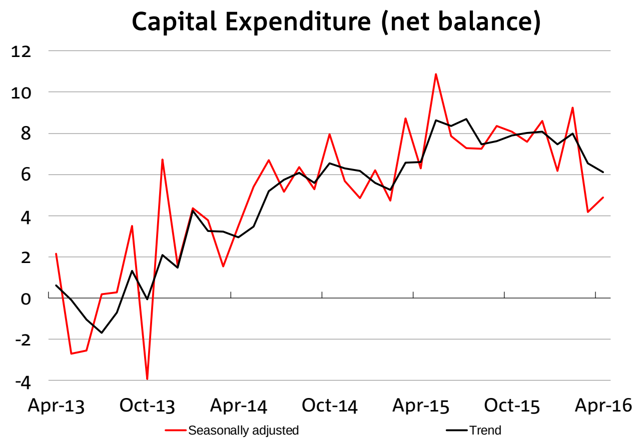
Based on respondent estimates of changes in labour costs and product prices. Retail prices are based on retail sector product price estimates.

More details on business activity

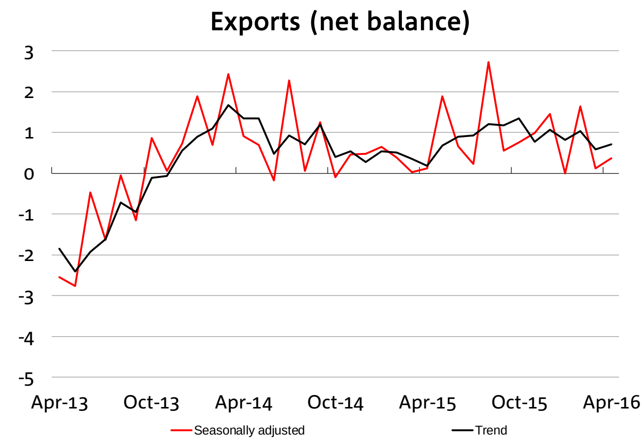
Firms re-stocking, but at a modest pace



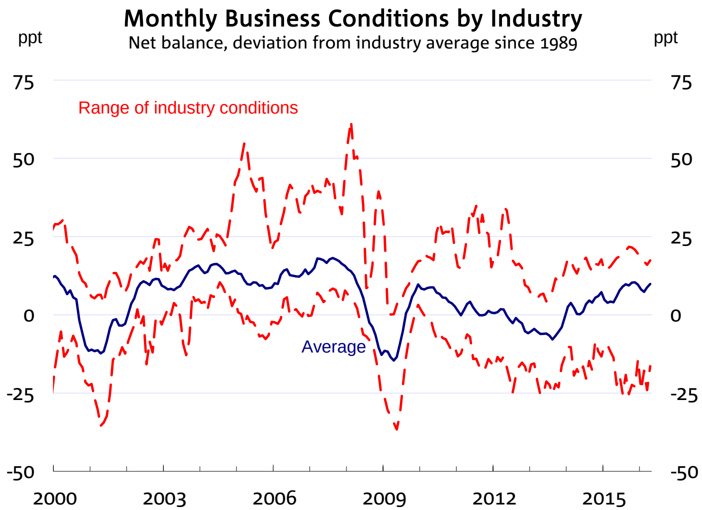
Capex positive, but has lost momentum



Exports looking subdued

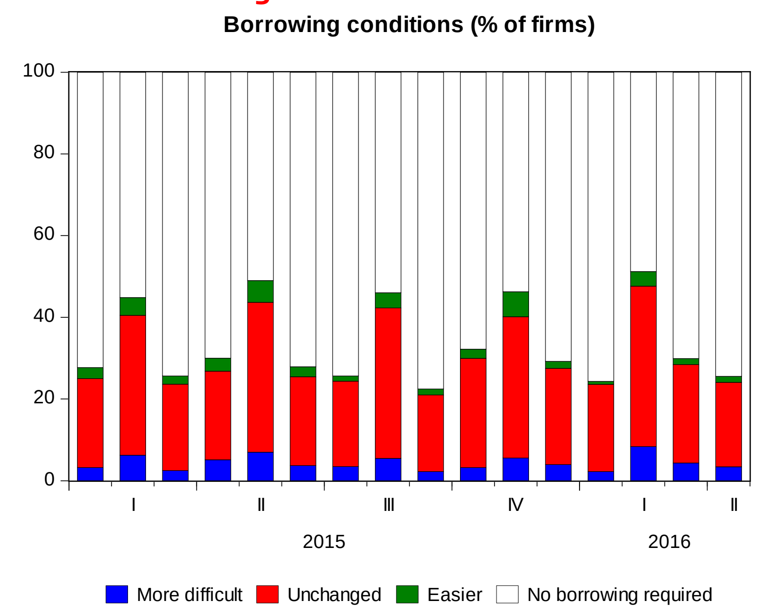


Range of conditions widen as minig falls and fin/ prop/ bus lift



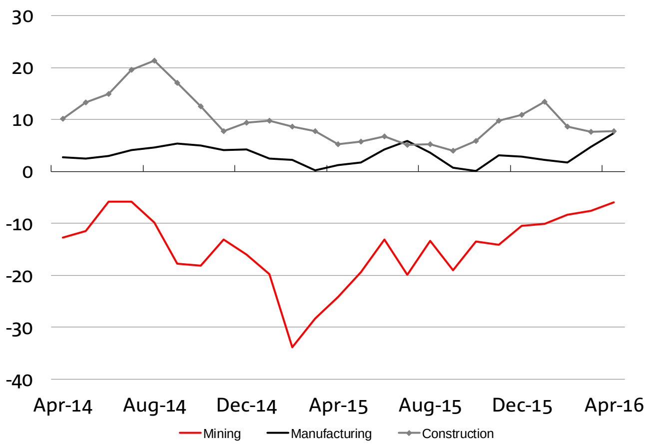
Source: NAB

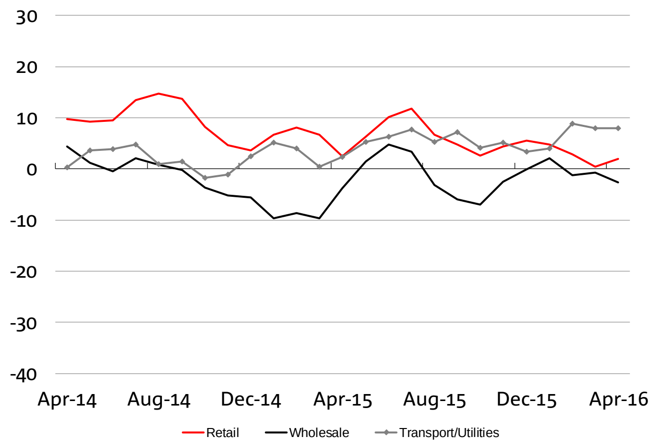
Borrowing conditions deteriorated in past 3 months, although demand for credit rose

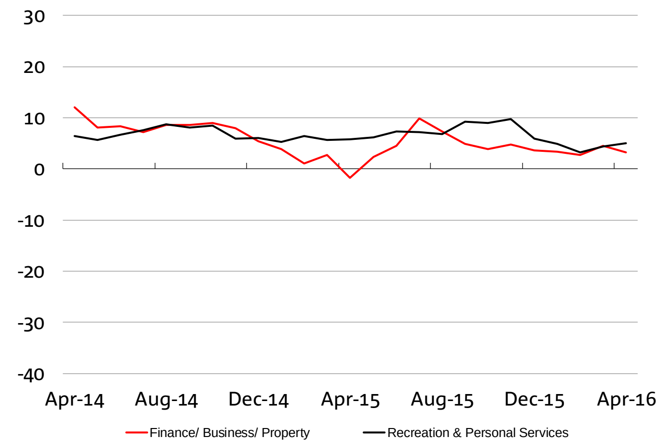


More details on industries

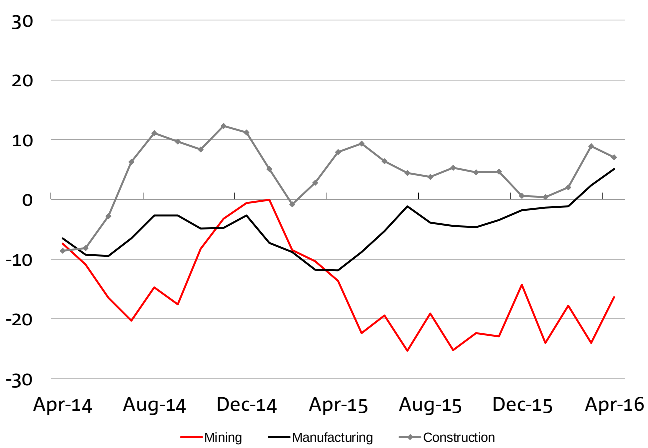
Business confidence by industry (net balance): 3-month moving average

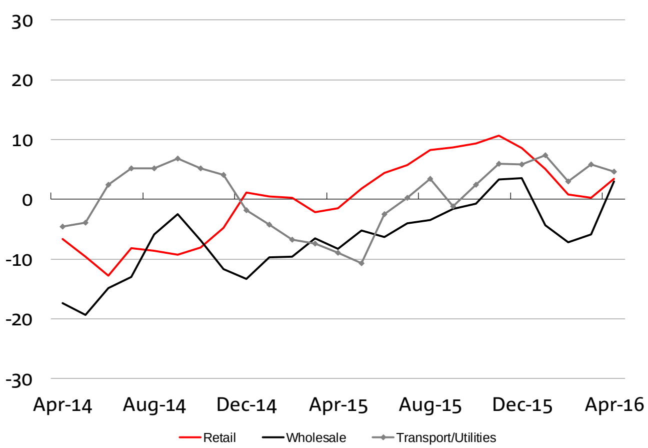


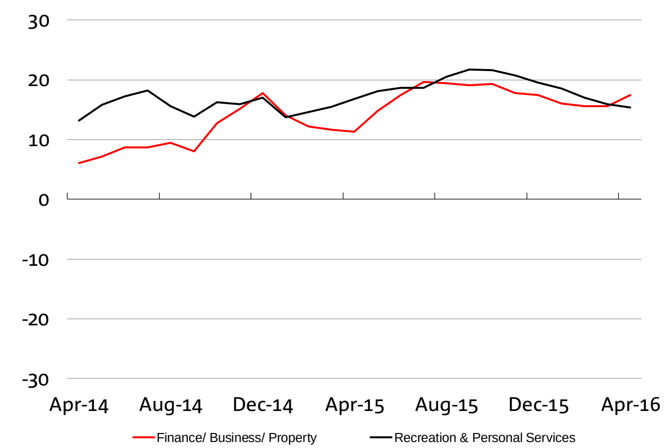




Business conditions by industry (net balance): 3-month moving average

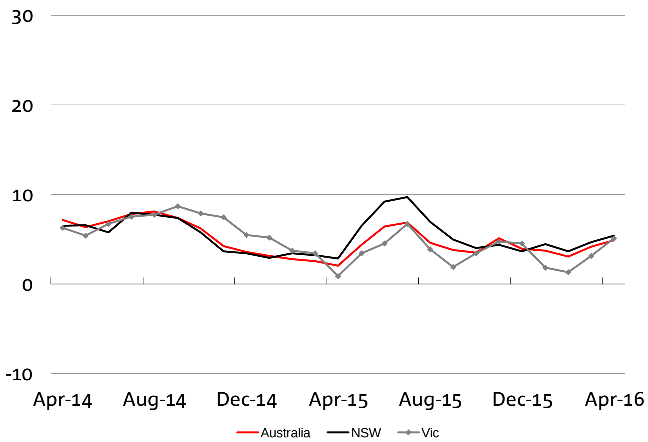


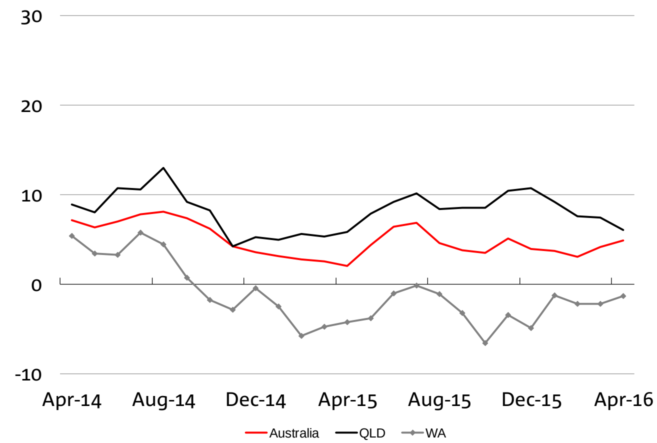


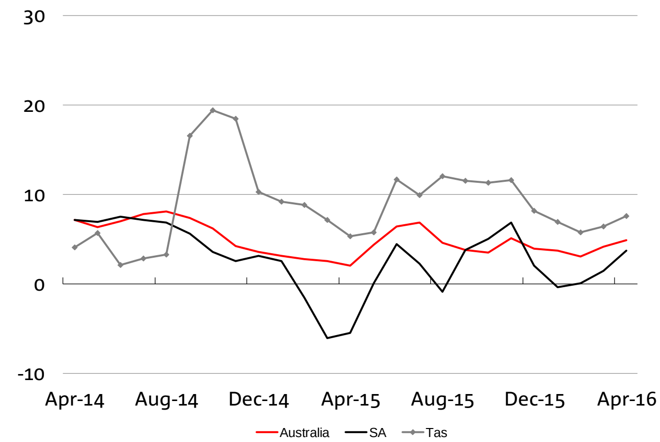


More details on states

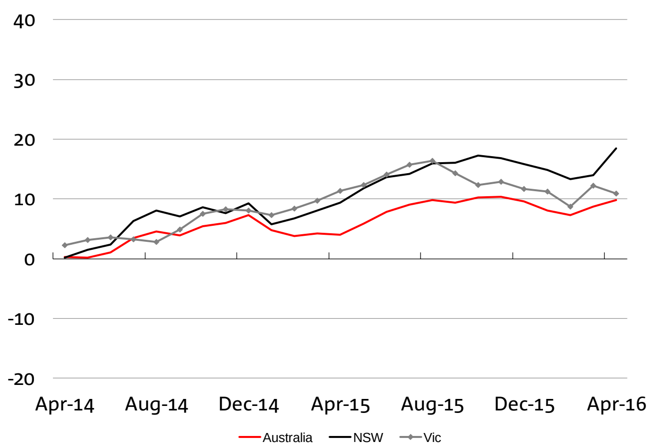
Business confidence by state (net balance): 3-month moving average

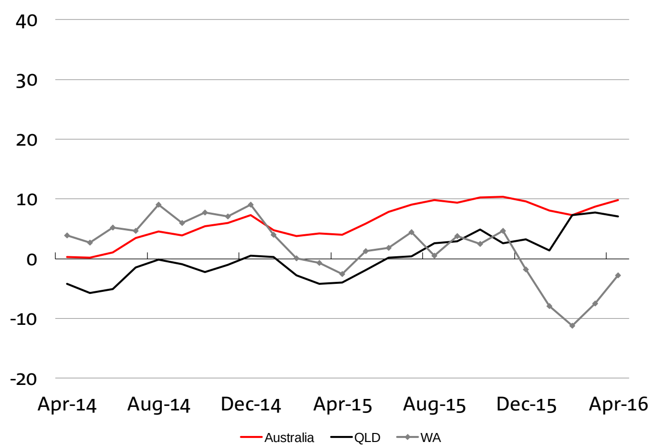


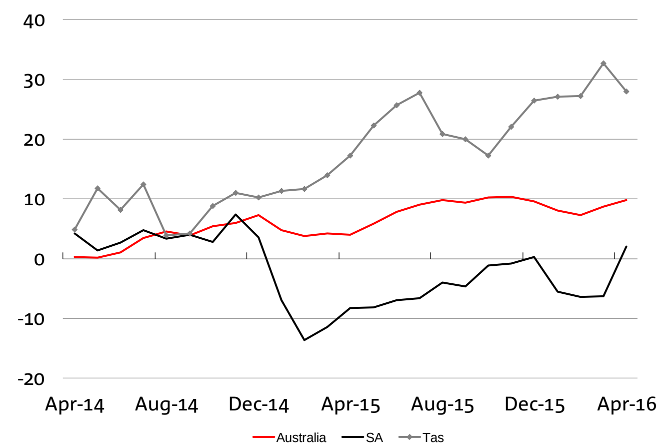




Business conditions by state (net balance): 3-month moving average







Data appendix

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

Apr-2016	Mining	Manuf	Constn	Retail	Wsale	Tran. & utils	Rec. & pers.	Fin. prop. & bus.	Australia
Labour costs: current	-2.0	0.5	0.5	0.2	1.3	1.2	0.9	0.8	0.6
Labour costs: previous	-2.0	1.5	0.5	0.5	0.8	0.4	1.0	0.8	0.7
Labour costs: change	0.0	-1.0	0.0	-0.3	0.5	0.8	-0.1	0.0	-0.1
Prices (final): current	0.5	0.2	-0.6	0.3	0.2	-0.1	0.5	-0.4	0.1
Prices (final): previous	-0.9	-0.5	-0.1	0.5	0.5	-0.3	0.3	0.3	0.1
Prices (final): change	1.4	0.7	-0.5	-0.2	-0.3	0.2	0.2	-0.7	0.0
Purchase costs: current	-0.2	0.3	0.1	0.2	0.0	0.3	0.3	0.1	0.2
Purchase costs: previous	0.1	0.3	0.9	0.5	0.8	0.2	0.5	0.1	0.5
Purchase costs: change	-0.3	0.0	-0.8	-0.3	-0.8	0.1	-0.2	0.0	-0.3

Key state business statistics for the month

Apr-2016	**Monthly Business Survey Data: By State**					
	NSW	**VIC**	**Qld**	**SA**	**WA**	**Tasmania**	**Australia**
Bus. conf.: current	6	7	2	0	3	2	5
Bus. conf.: previous	6	5	9	7	-3	9	6
Bus. conf.: change	0	2	-7	-7	6	-7	-1
Bus. conf: current - Trend	5	5	6	4	-1	8	5
Bus. conf: previous Trend	5	3	7	1	-2	6	4
Bus. conf.: change -Trend	0	2	-1	3	1	2	1
Bus. conds: current	26	6	1	7	-8	12	9
Bus. conds: previous	15	19	5	4	6	46	12
Bus. conds: change	11	-13	-4	3	-14	-34	-3
Bus. conds: current -Trend	18	11	7	2	-3	28	10
Bus. conds: previous -Trend	14	12	8	-6	-8	33	9
Bus. conds: change -Trend	4	-1	-1	8	5	-5	1

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