

NAB Quarterly SME Survey

by NAB Group Economics

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Sep quarter 2015



Key Points:

- **The NAB SME Survey is the leading business survey on small businesses in Australia, complementary to the comprehensive Quarterly NAB Business Survey.** It offers a rich repertoire of insights into factors affecting these firms' conditions by state, industry and size, as well as an assessment on their outlook for investment and output.
- **In the quarter, SME business conditions stayed unchanged at +4 index points.** Within the components of business conditions, trading conditions were particularly strong, which flowed into modestly better profitability conditions. However, employment conditions remained subdued.
- **Meanwhile, heightened volatility in international financial markets and renewed investor concerns about Chinese economic slowdown weighed on the confidence of SMEs.** SME business confidence sank by 5 points into negative territory to -1 index point. **Most industries recorded an improvement in conditions in the quarter, except for property, business services and wholesale firms.** Retail (see Industry Focus on page 5) recorded the first positive reading in more than 7 years at +1, while manufacturing also improved notably. Finance firms were clear outperformers in the quarter, while wholesale and construction firms (which includes residential, non-residential and mining-related construction) were the weakest.
- **Conditions across states were mixed in the quarter, with NSW and VIC continuing to claim the top two spots.** SA more than reversed its gains in the Q2 to be back in negative territory, while the mining states of QLD and WA continued to be mired in negative territory. Most states' confidence deteriorated in the quarter, except for QLD which stayed unchanged at +1.
- **Capacity utilisation reached its highest level since Q2 2011.** This, combined with a pick-up in forward orders, indicate moderate improvements in business conditions in the near future. However, capex by firms appears to have lost further momentum in the quarter.

	2014	2015	2015
	Q3	Q2	Q3
Business Conditions	5	4	4
Low-tier firms	0	-2	0
Mid-tier firms	5	2	4
High-tier firms	6	8	5
Business Confidence	5	4	-1
Low-tier firms	0	-3	-2
Mid-tier firms	8	9	1
High-tier firms	6	5	-3
Trading Conditions	13	11	14
Low-tier firms	4	6	4
Mid-tier firms	11	9	11
High-tier firms	15	15	19
Profitability	2	1	3
Low-tier firms	-3	-5	-1
Mid-tier firms	0	-2	4
High-tier firms	4	5	2
Employment	1	-1	-3
Low-tier firms	-2	-8	-2
Mid-tier firms	2	-1	-3
High-tier firms	0	5	-4

Note*: Low-tier : turnover \$2-3m p.a. Mid-tier: turnover \$3-5m p.a. High-tier: turnover \$5-10m p.a.

Table 1: Business conditions & confidence – Sep qtr

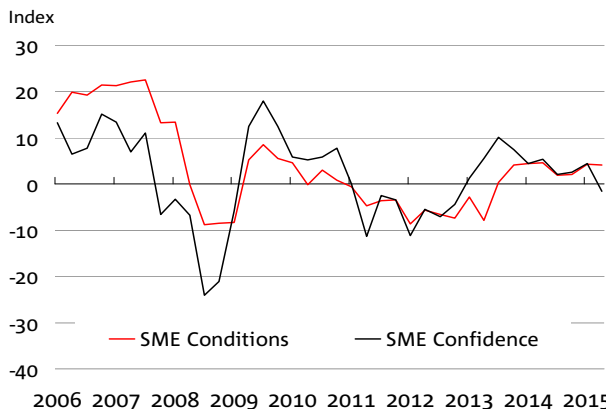


Table 2: Conditions and confidence by industry (net balance, s.a.) – Sep qtr

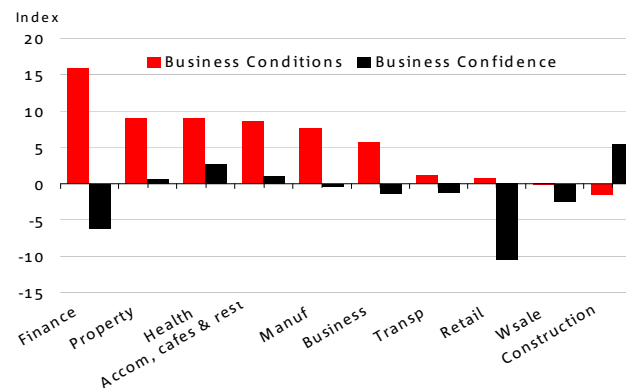
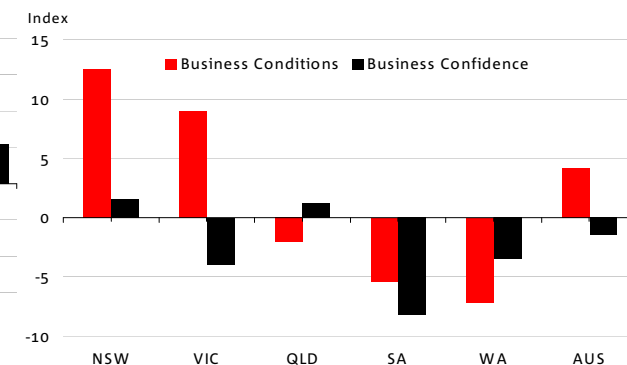


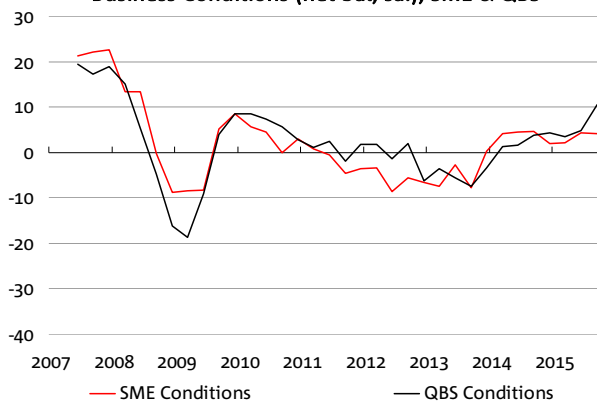
Table 3: Q3 Conditions and confidence by state (net balance, s.a.) – Sep qtr



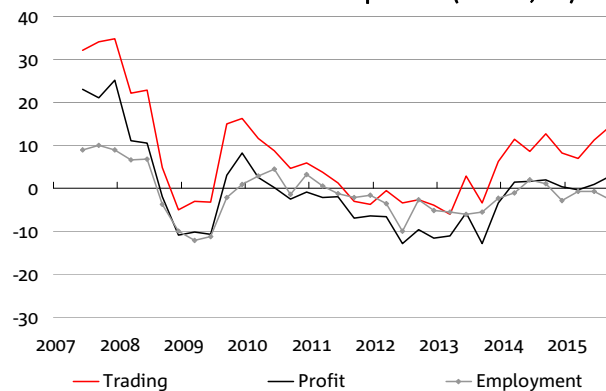
SME conditions held onto gains from the previous quarter, but confidence sagged

- **Business conditions for SMEs remained unchanged at +4 index points in the September quarter, but business confidence eased by 5 points to -1 index point.** While still positive, SME conditions diverged notably from those of general businesses indicated by NAB Quarterly Business Survey (QBS), with the latter pushing ahead to +11 index points. Weaker momentum for SMEs may suggest they are not as well-positioned as the larger businesses to maximise the benefits/tackle the challenges arising from changes in the currency.
- **Relatively strong trading conditions are finally manifesting in an upturn in profitability.** The profitability index rose by 2 points to +3 index points, its highest level since late 2009. That said, employment conditions remained subdued and failed to mimic the pick-up evident in the QBS. The improvement in profitability in the quarter may in turn reflect better (albeit still negative) margins and therefore better cashflow.
- **Overall, the survey results pointed to a broadening non-mining sector recovery.** Business conditions remain strongest in services industries, with the finance sector (at +16 index points) overtaking property services in the quarter to be the best-performing industry. Health and accommodations/cafes/restaurants tied with property services in second spot at +9 index points. **A surprising finisher in the top five was manufacturing, which built on its recent traction to improve by 7 points in the quarter from the neutral mark. This represents its best result since mid-2010 and suggests pass-through of stimulatory effects from a low AUD.** It is also worth noting that the retail sector recorded its first positive reading in more than 7 years at +1. At -2 index points, construction was the weakest in the quarter. **By state, the two largest states of NSW and VIC continued to outperform at +13 and +9 index points respectively.** SA more than reversed its gains in the June quarter to be back in negative territory (at -8), while the mining states of QLD (-2) and WA (-7) remained in negative territory. Most states' confidence deteriorated in the quarter, except for QLD which was unchanged.
- Confidence by industry was more mixed (refer to page 10 for more details): construction was the most confident at +5 index points while retail confidence fell 16 points to be the weakest at -11 index points.
- **Compared to the larger businesses in the QBS, SME business conditions were lower in retail, finance, construction, as well as recreational and personal services.** Meanwhile, better performances were reported by SMEs in manufacturing, wholesale and business services.
- **Analysis by the size of firms shows that low-tier SME firms with \$2 to 3 million annual revenue continued to report significantly weaker conditions compared to their larger counterparts, although high-tier firms (\$5 to 10 million annual revenue) reported the worst confidence levels.**

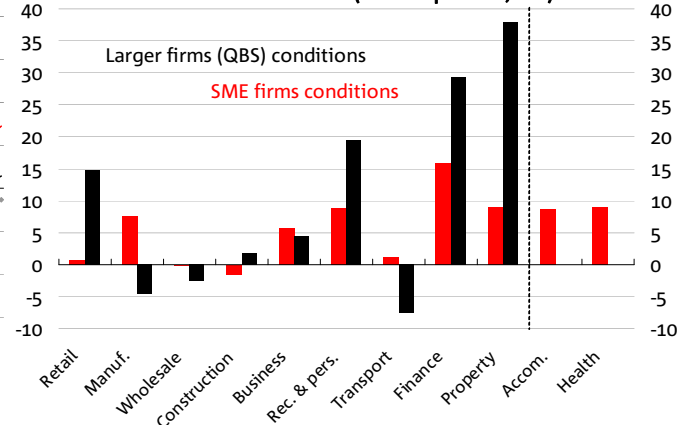
Business Conditions (net bal, sa.), SME & QBS



SME Business Conditions Components (net bal, sa.)



Business Conditions (latest quarter, sa.)

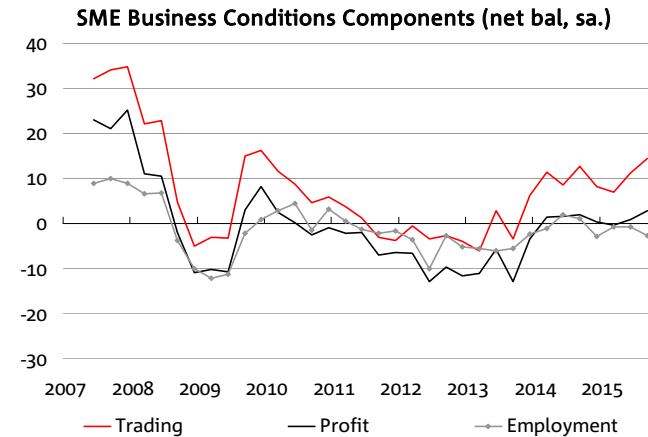


** Data are seasonally adjusted by NAB, except SME cashflow (insufficient time series available). All data are net balance indices. Fieldwork for this Survey conducted from 24 August to 9 September 2015 covering around 686 SME (non-farm) firms.

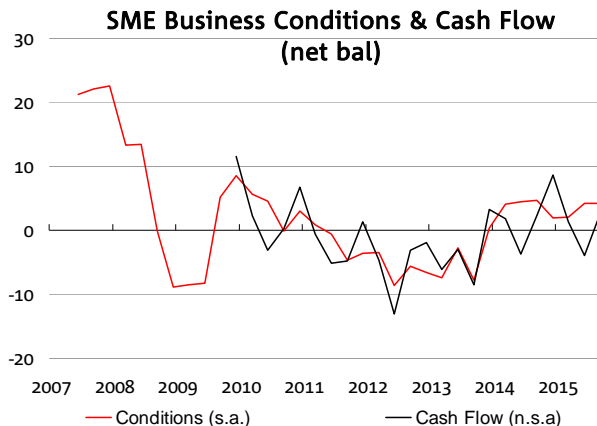
Forward and financial indicators showed promising gains

- In the September quarter, SME forward orders maintained the positive momentum witnessed in the June quarter to lift by 1 point to be at +5 index points. This is broadly consistent with the result of general businesses as reported in the QBS and represented the highest level since early March qtr 2014, although forward orders are still below pre-GFC highs.
- The generally positive readings for forward orders since early last year are consistent with a moderate recovery in real economic activity. They also appear to have been given a shot in the arm by the recently announced Budget measures targeted at micro businesses. Orders were the strongest in property services (at +13), followed by finance (at +12) and manufacturing (+10). A 9-point improvement recorded by manufacturing in the quarter was again an upside surprise. Forward orders in construction have trended significantly lower this year (currently at +2), after reaching a recent peak of +14 in Q2 2014. This possibly reflects the slowing in both engineering and dwelling construction activity. Meanwhile, health (at -1), transport (at 0) and wholesale (at +1) reported the weakest forward orders.
- The SME stock index reversed all of its gains last quarter to be at +2 index points, a level consistent with a moderate pick-up in underlying demand and aligns with that in the QBS. By industry, stocks were the highest in wholesale (+8) and manufacturing (+7), although the former recorded a sharp fall of 11 index points. Meanwhile stocks were the lowest in business services (-2) and transport (at 0), while the construction stock index managed to nudge into positive territory after a year's worth of negative readings. Overall, at their current levels, the forward and financial indicators point to a moderate but tentative recovery in coming months.

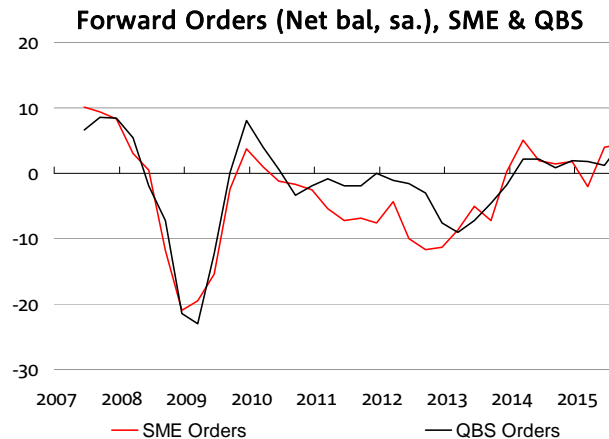
Trading conditions continued to be the key driver for overall conditions, but profitability also nudged into positive territory



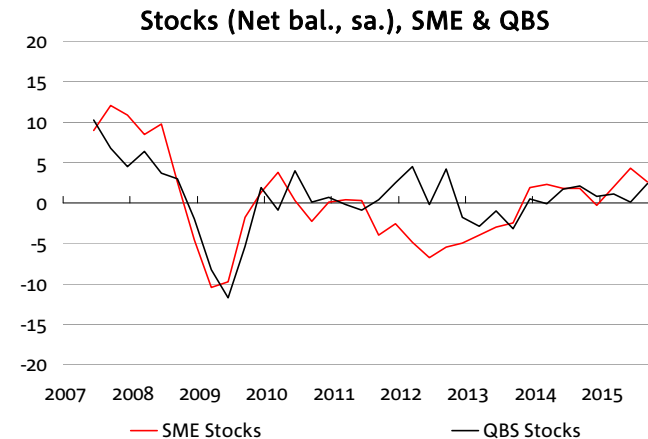
Cash flow rebounded back into positive territory



SME forward orders maintained last quarter's momentum



SME stock index largely consistent with that of QBS

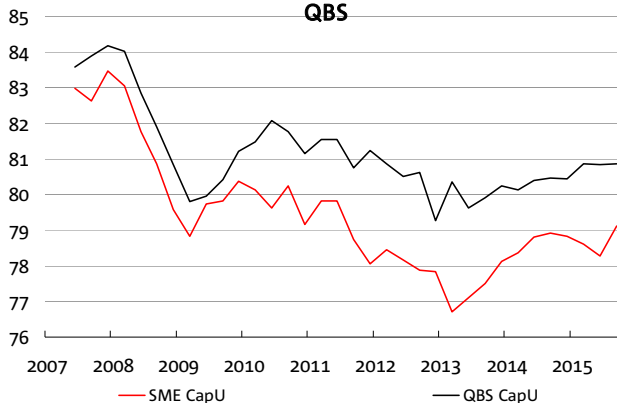


SME capacity utilisation rose to levels last seen in 2011

- **SME capacity utilisation also rebounded in the quarter by 1ppt to 79%, the highest level since 2011 (unrounded),** although it was still way below those of general businesses indicated by the QBS. Services industries continued to report higher capacity utilisation rates in general, with health at the top of the ladder at 88%, followed by business services and transport at 83%. Transport and manufacturing improved by the most in the quarter (up 4ppts), although the latter had the softest capacity utilisation reading out of all industries at 75.3%.
- The increase in capacity utilisation in the quarter was driven by low-tier and mid-tier firms, which recorded a rise of 1ppt and 2ppts respectively to 78% and 80%, while high-tier SME firms operated at a similar level of capacity in Q2 at 80%.
- **Capital expenditure (capex) by SMEs moderated further in the September quarter to stay below the capex reading for larger businesses as indicated by the QBS. This was despite a pick-up in capacity utilisation rate in the quarter.** Nevertheless, positive readings for both the SMEs and QBS capital expenditure indices indicate that firms continue to operate in an expansionary mode on balance, albeit a modest one.
- By industry, capex was the strongest in health (+25), followed by accommodation, cafes and restaurants sector (+23 points), as well as manufacturing (at +11). Meanwhile, retail (-7) and transport (-1) were the main detractors from the index. **Since Q1 2009, capex in the retail sector has recorded negative readings in 20 out of 27 quarters, a direct reflection of the poor business conditions plaguing the sector since the GFC, although there are now some green shoots emerging.** Meanwhile, all-industry longer-term capex intentions have weakened, with 12-month capex expectations retreating to +12 in the quarter from +19 the same quarter last year.

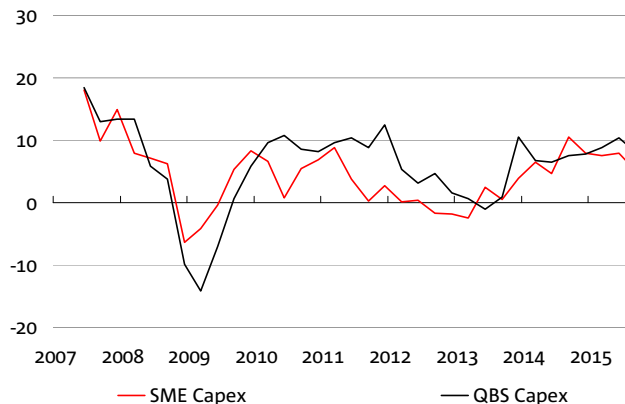
SME capacity utilisation rises to the highest level since 2011

Capacity Utilisation (per cent, s.a.) SME & QBS



Capex points to moderate expansion in near-term activity

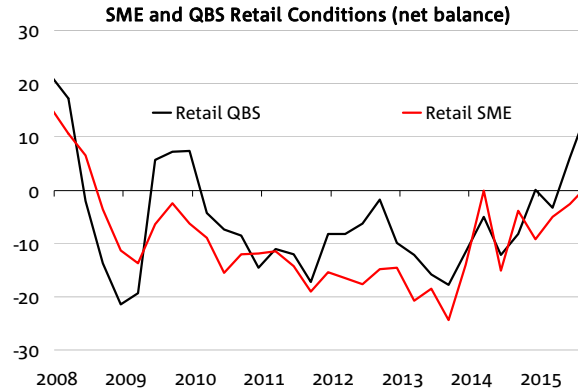
Capital Expenditure (net bal., sa.), SME & QBS



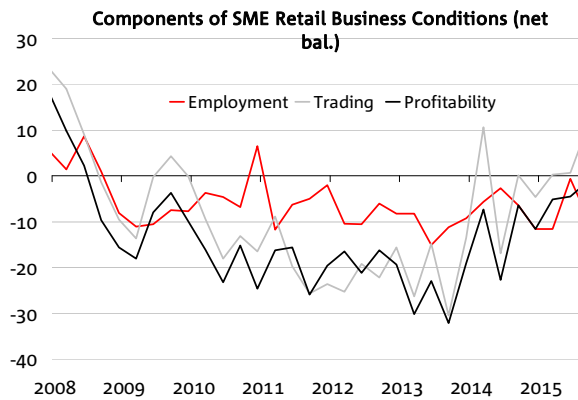
Industry Focus : Retail

- Since the GFC, SMEs in the retail sector have been confronted with challenging business conditions. **In the September quarter, the SME retail conditions index nudged into positive territory for the first time in 7 years to +1, having shown a steady improvement since the end of 2014.**
- However, business conditions experienced by the smaller retailers covered in this survey are still lagging behind those faced by their larger industry counterparts in the QBS, which suggest size-specific challenges. Despite some long-term headwinds, trends in retail businesses within the SME space have been positive across revenue brackets. **Strong residential markets in NSW and Victoria have led to a pick-up in expenditure on household durables and furnishings.**
- A lower AUD has also spurred tourism-related spending, but it also drove purchase costs higher (see chart at top right hand corner), with cost pressure accelerating over the last 2 years. That said, purchase costs growth slowed in the September quarter to 1% from 1.4% in the June quarter, possibly reflecting the disproportionate weakening of the currencies of our major trading partners, such as China, New Zealand and a number of Southeast Asian nations. **The pace of growth in retail product prices has been much more moderate than purchase prices, indicating the difficulty in retailers fully passing on costs to consumers.**
- Forward-looking indicators for retail SMEs such as capacity utilisation and stocks have also been more encouraging of late, with the former rising to levels not seen since late 2009.** While the forward orders index continued to remain in negative territory, its trends have clearly improved and stabilised over the last 2 years.

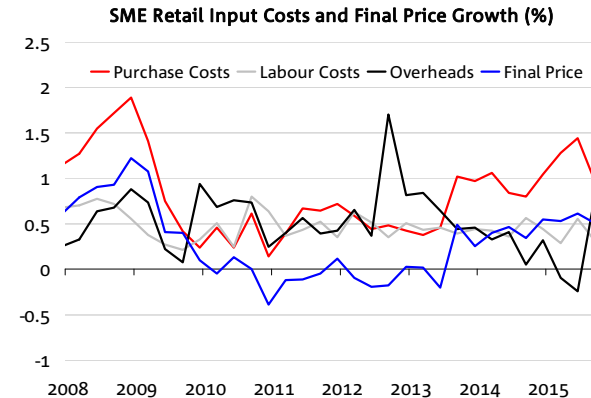
Retail SMEs are lagging behind their larger industry counterparts



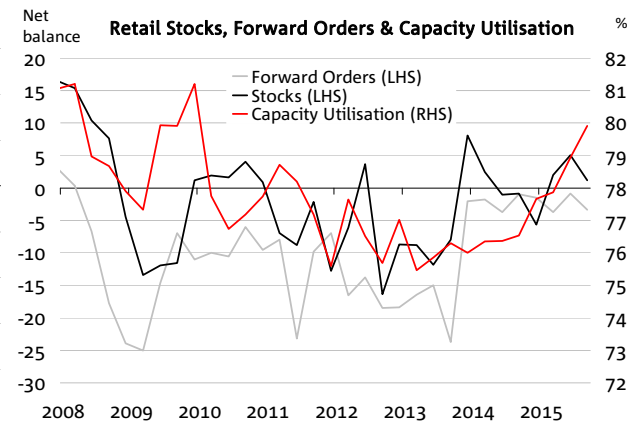
Trading conditions have improved markedly, but employment and profitability remain subdued



Retail SMEs are facing strong purchase cost growth



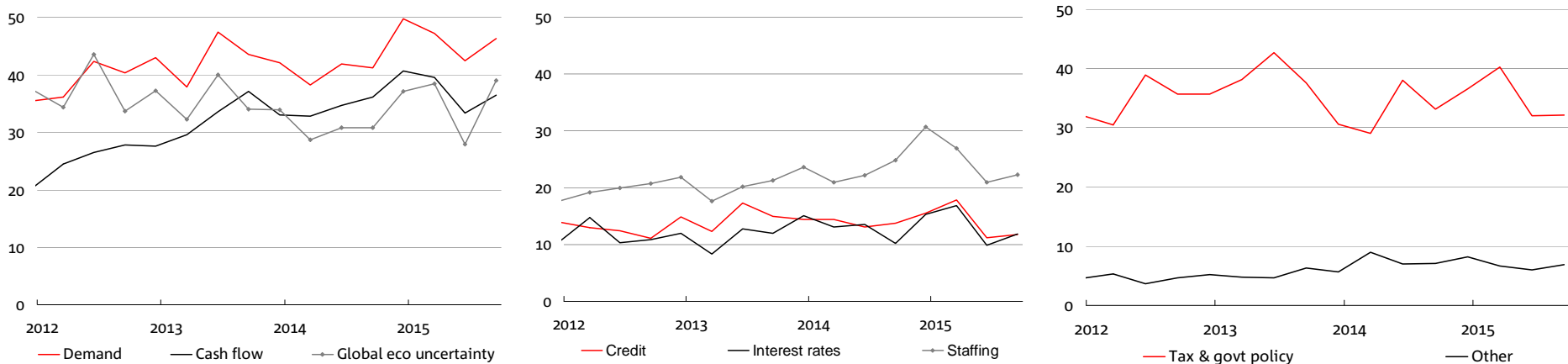
A recovery in capacity utilisation and positive forward orders conditions signal a pick-up in demand



Significant constraints affecting SMEs' long-term decisions lifted in the quarter

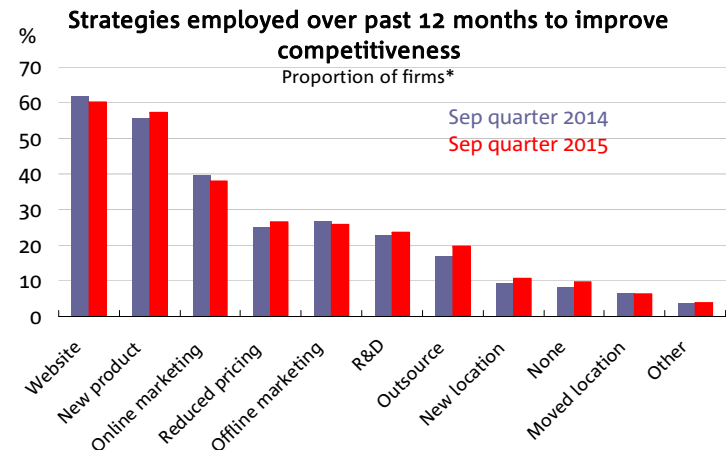
- Volatility and risk aversion increased sharply in global financial markets in the September quarter as market attention shifted towards falling commodity prices, the prospect of higher US interest rates, a build-up in debt and uncertainty over the pace of Chinese growth. **These events appeared to have taken a toll on our survey results, with SMEs reporting a worsening in every significant constraint affecting their long-term decisions on balance, except for tax and governmental policy which remained unchanged.** Perhaps unsurprisingly, global economic uncertainty showed the biggest jump of 11 points to +40, although demand conditions were still regarded as the most constraining at +46. Supply-side factors continued to be relatively benign, with credit, staffing and interest rates only showing a minor up-tick in the quarter.

Most significant constraining factors for SMEs (per cent, multiple responses)



Pattern in SMEs' business strategies is largely stable

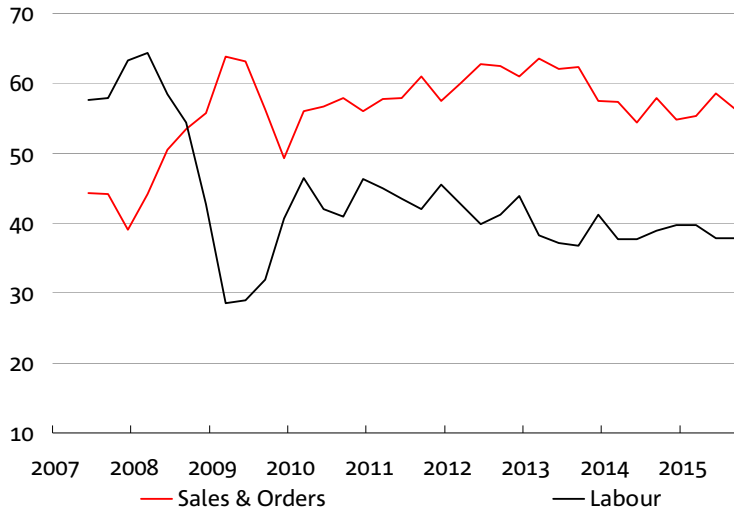
- In the September quarter, we again asked firms whether they had employed any new strategies over the past 12 months to improve their competitiveness in the market.
- There were no significant changes in their strategies in the quarter compared to the same quarter last year. This may reflect continuous improvements in underlying demand conditions over the previous twelve months which required a lesser need for firms to significantly change their competitiveness strategies.



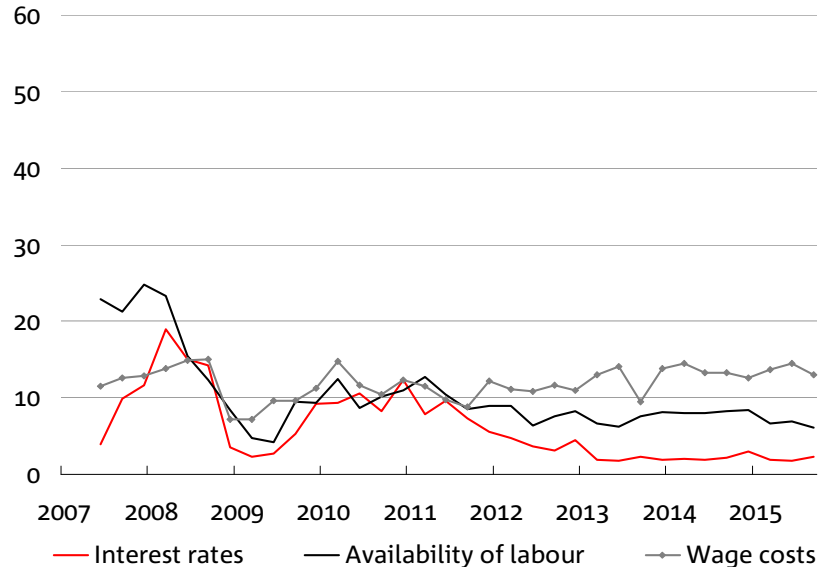
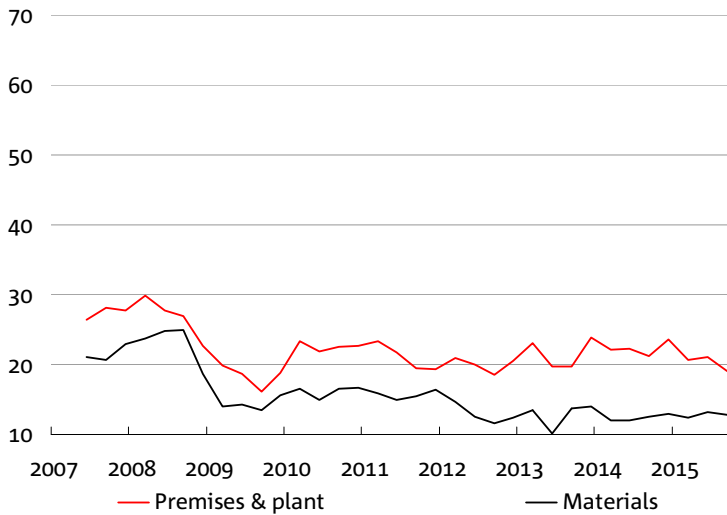
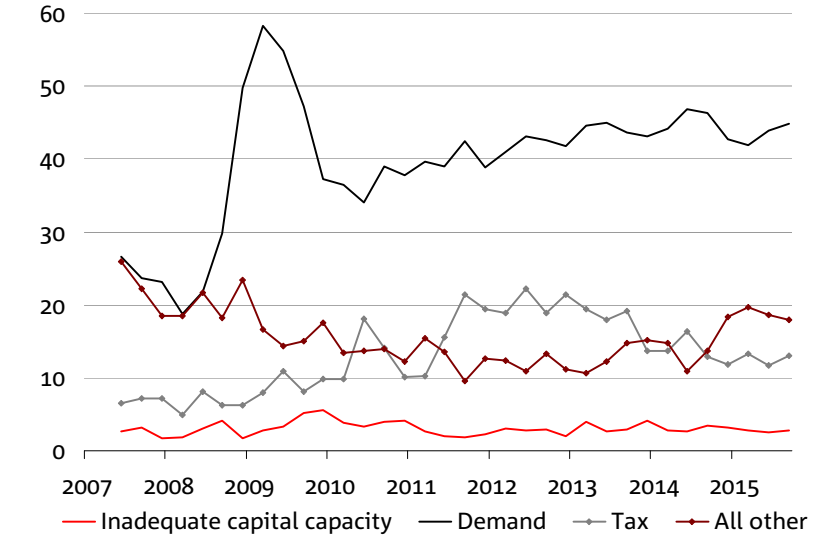
* Multiple responses allowed; will not sum to 100%
Source: NAB Quarterly SMB Survey

Constraints facing SMEs' output and profitability

Constraint on output (% of firms)

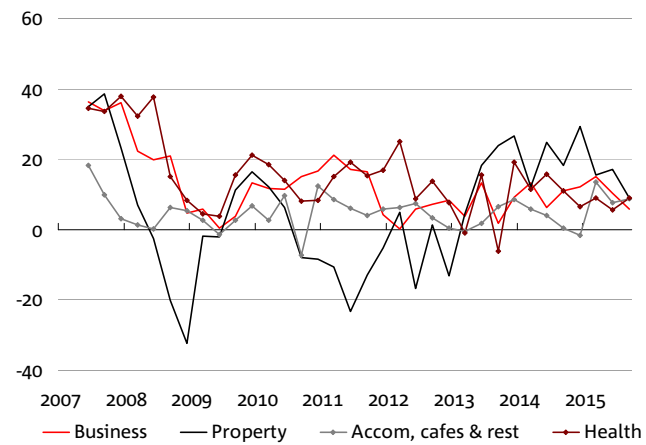
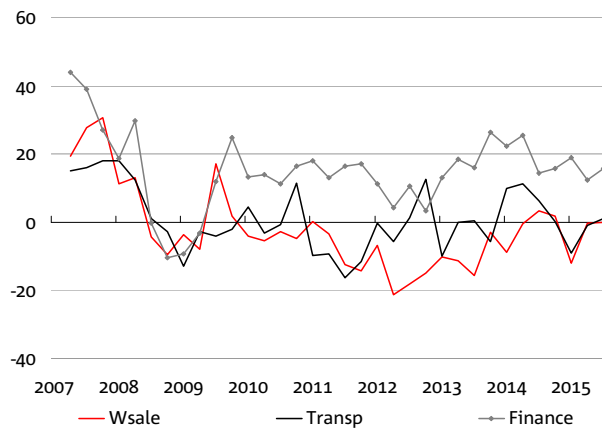
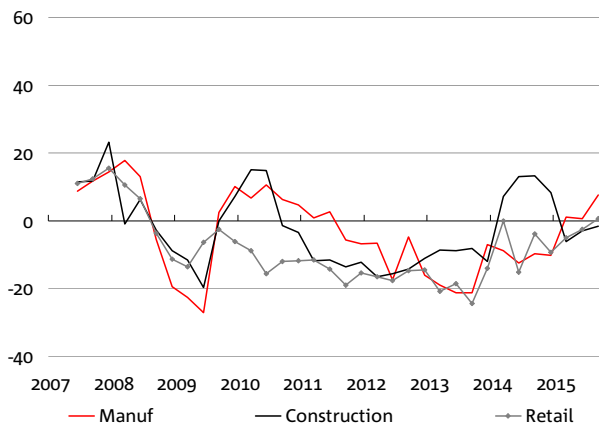


Constraint on profitability (% of firms)

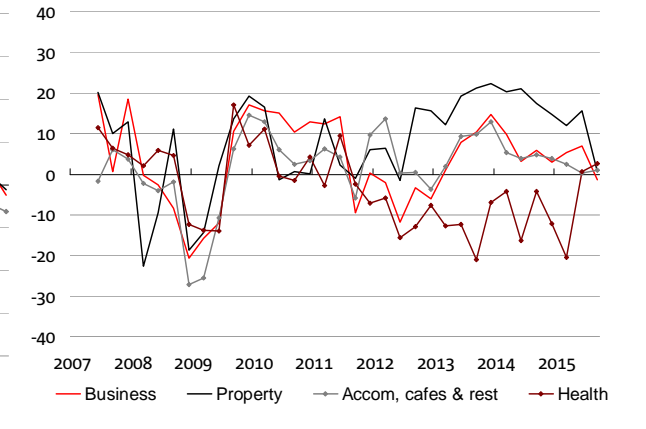
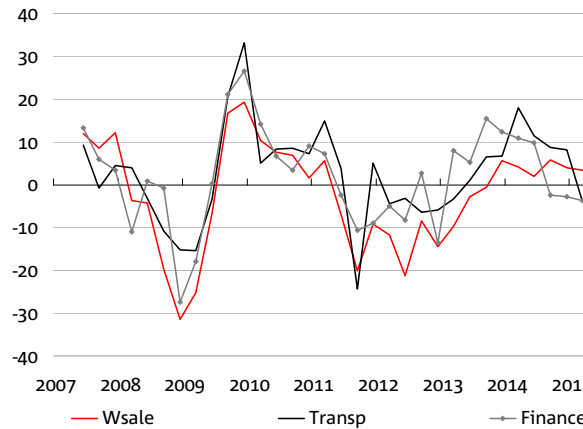
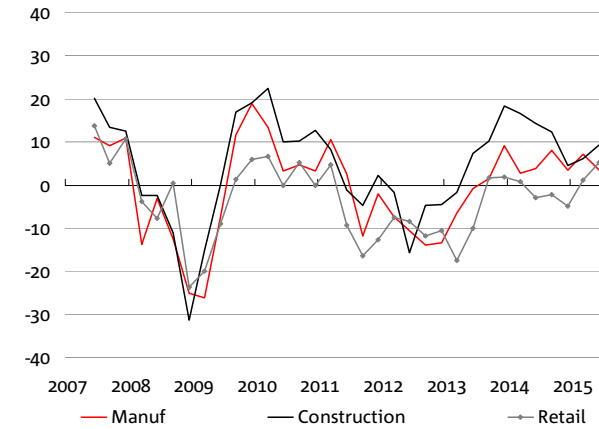


Detail by industry

Business conditions by industry (net balance)

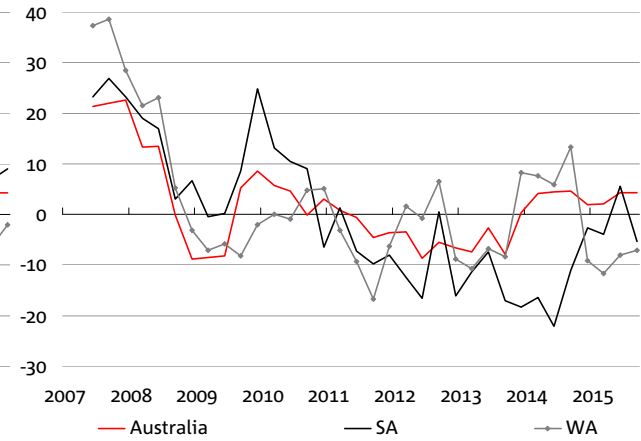
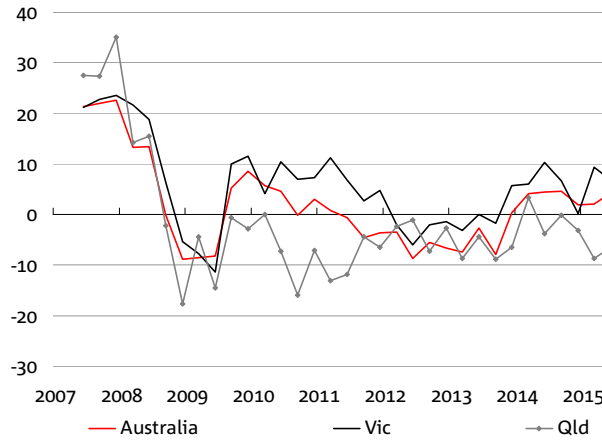
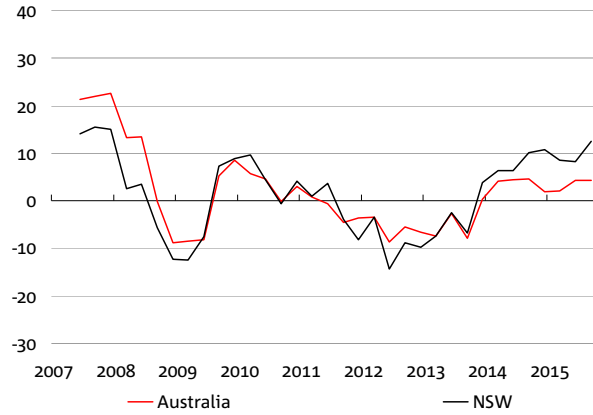


Business confidence by industry (net balance)

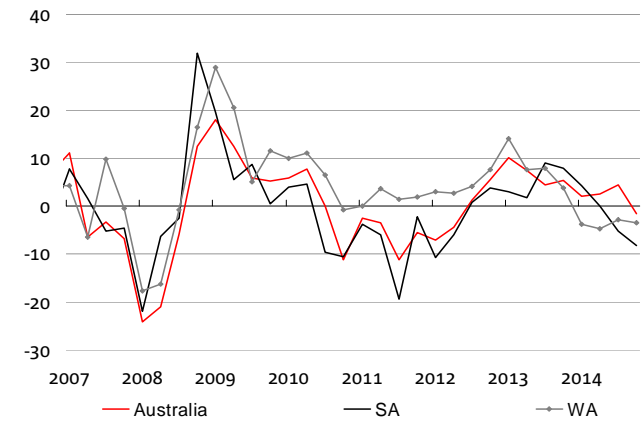
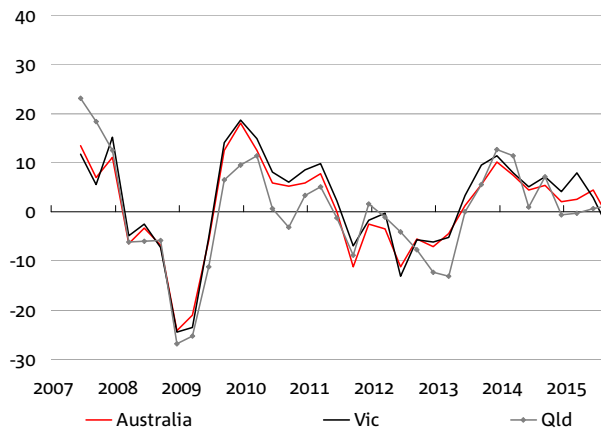
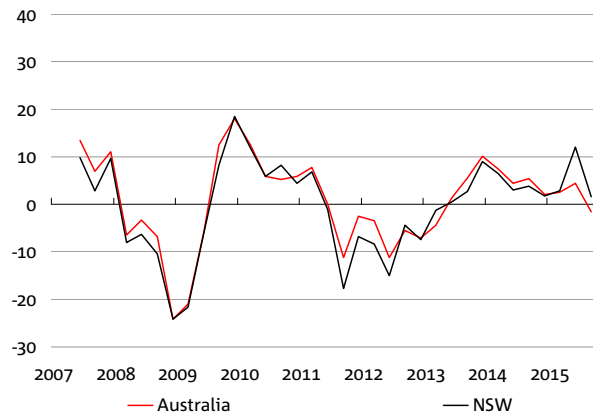


Detail by state

Business conditions by state (net balance)

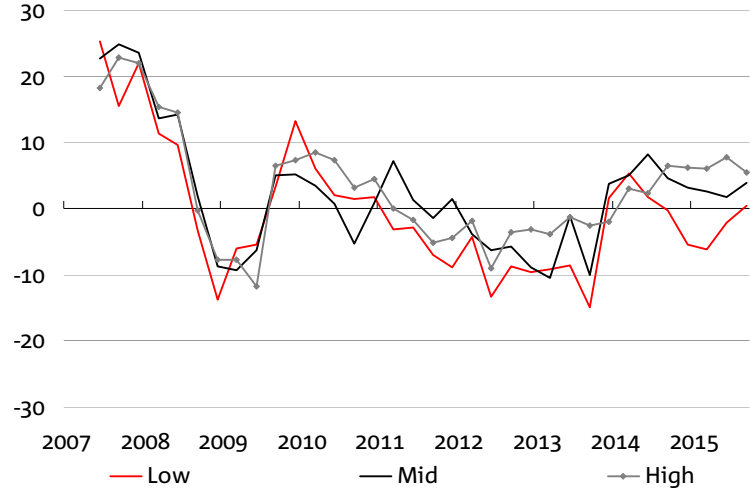


Business confidence by state (net balance)

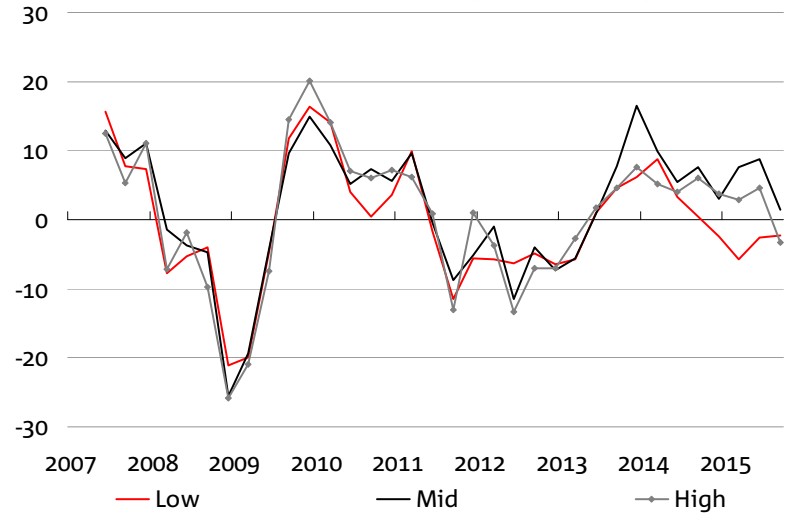


Detail by SME firm size

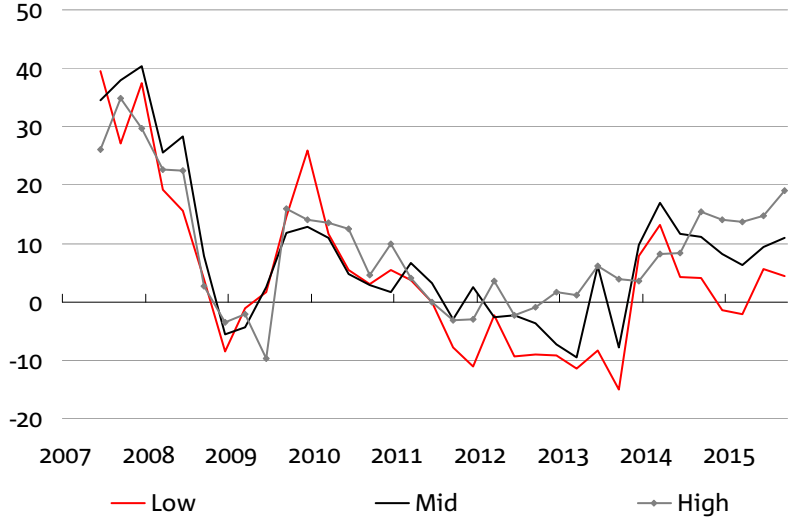
Business Conditions (net bal., sa.)



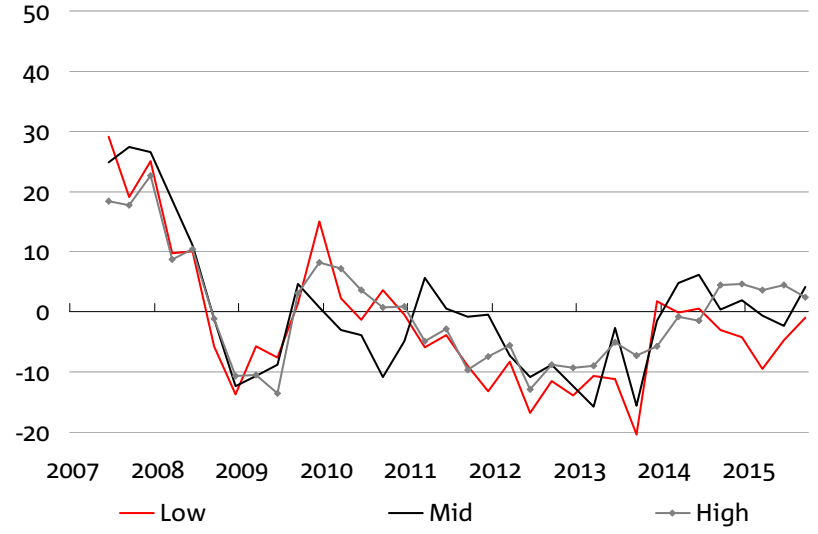
Business Confidence (net bal., sa.)



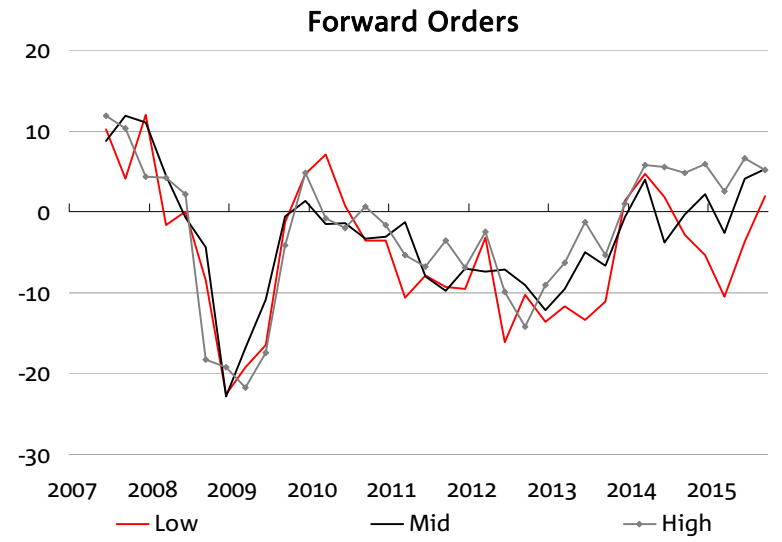
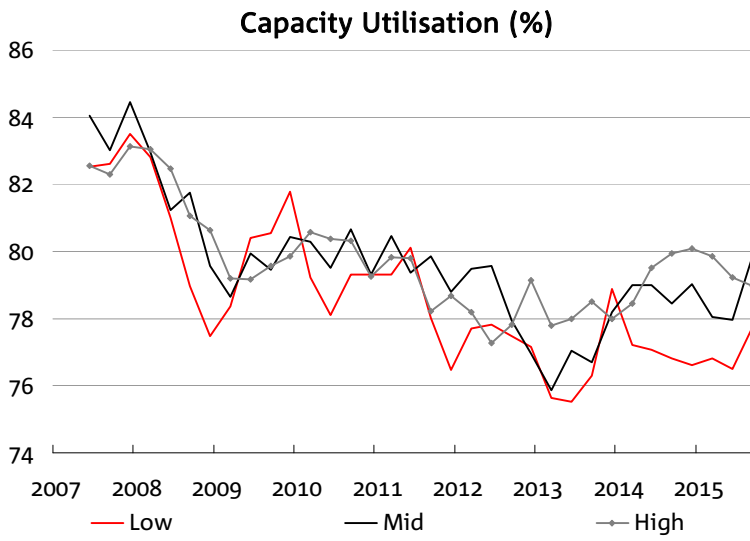
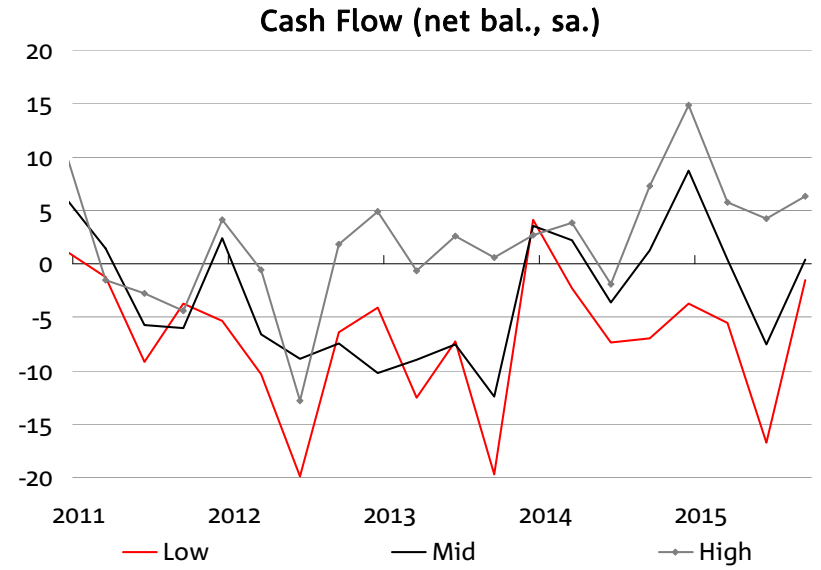
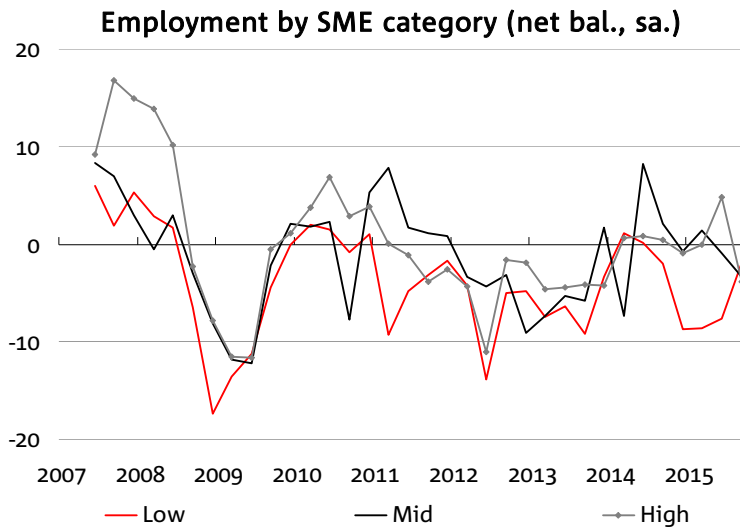
Trading Conditions (net bal., sa.)



Profitability (net bal., sa.)



Detail by firm size (cont.)



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