

NAB MONTHLY BUSINESS SURVEY

OCTOBER 2016

NEXT RELEASE:
13 DEC 2016 – NOVEMBER MONTHLY



Key points:

- The NAB Monthly Business Survey is now suggesting some moderation in the non-mining economic recovery, with the aggregate level of business conditions (a combination of trading, profitability and employment conditions) dropping in October – the trend has also steadily eased from its most recent peak in May. **Despite the subdued trend, business conditions remain at above average levels and business confidence has been tracking broadly sideways for some time** – albeit easing in the month as well. In October, **the business conditions index fell 2 points, to +6 index points, which is slightly above the long run average of +5**. There was a narrowing in business conditions across industries in the month, although this was partially the result of a deterioration in conditions for the best performing (services based) industries. However, a noticeable improvement in retail conditions was encouraging, although the trend remains quite soft. By component, both trading and employment conditions deteriorated – although the former remains elevated – while profitability was steady. Inflation measures in the Survey have been subdued and generally moderated further in the month.
- **Business confidence has proven to be relatively resilient this year, but did moderate in October – falling 2 points to +4 index points (below the long-run average of +6)**. While we would like to see confidence at higher levels as a precursor to stronger non-mining business investment, this could still be interpreted as a solid outcome, particularly given the global political uncertainty ahead of upcoming elections. However, other leading indicators were not encouraging either, with forward orders falling significantly, while capacity utilisation – of relevance to future employment and capital spending – eased further.
- The recent moderation in some NAB Business Survey indicators is a concerning trend that warrants close monitoring, but **our assessment is that the deterioration to date is not (yet) enough to warrant a significant change in the outlook**. However, if the recent trends were to continue, it would be unsettling and imply that the non-mining recovery has started to run out of steam earlier than expected. Subdued retail conditions are an additional concern. For now though, we would only be looking to slightly lower 2017 forecasts and remain reasonably comfortable with the near-term outlook - which is expected to be supported by commodity exports and the housing construction cycle. That said we are clearly more concerned than the RBA about the near term outlook. **Beyond the near-term, impetus from those growth drivers will fade which will see the economy slow into 2018. Two more 25bp rate cuts are still expected from the RBA next year in response to ongoing low inflation and a more subdued growth outlook.** NAB's latest Australian economic forecasts will be available on Thursday.

Table 1: Key monthly business statistics

	Aug 2016	Sep 2016	Oct 2016		Aug 2016	Sep 2016	Oct 2016
	<i>Net balance</i>				<i>Net balance</i>		
Business confidence	6	6	4	Employment	4	1	0
Business conditions	7	8	6	Forward orders	2	9	0
Trading	13	17	11	Stocks	1	2	1
Profitability	5	7	7	Exports	1	2	2
	<i>% change at quarterly rate</i>				<i>% change at quarterly rate</i>		
Labour costs	0.8	0.8	0.8	Retail prices	0.1	0.3	-0.3
Purchase costs	0.4	0.4	0.2		<i>Per cent</i>		
Final products prices	0.2	0.4	0.1	Capacity utilisation rate	81.0	80.6	80.5

* 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 25 Sep to 31 Oct, covering over 400 firms across the non-farm business sector.

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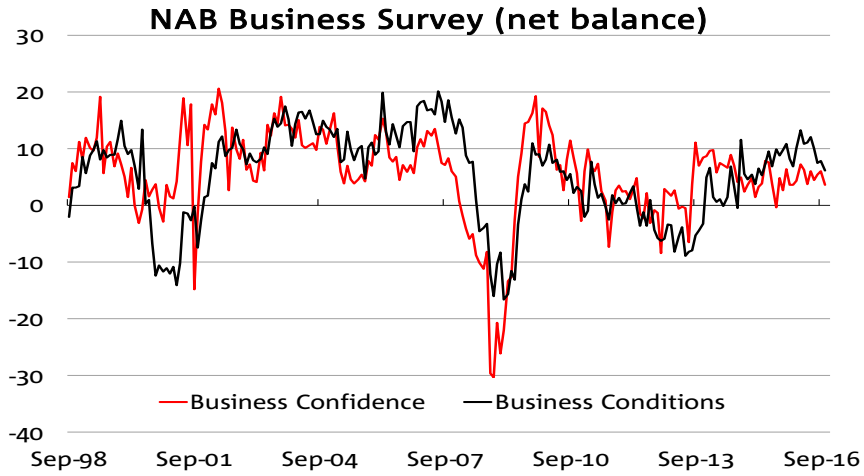
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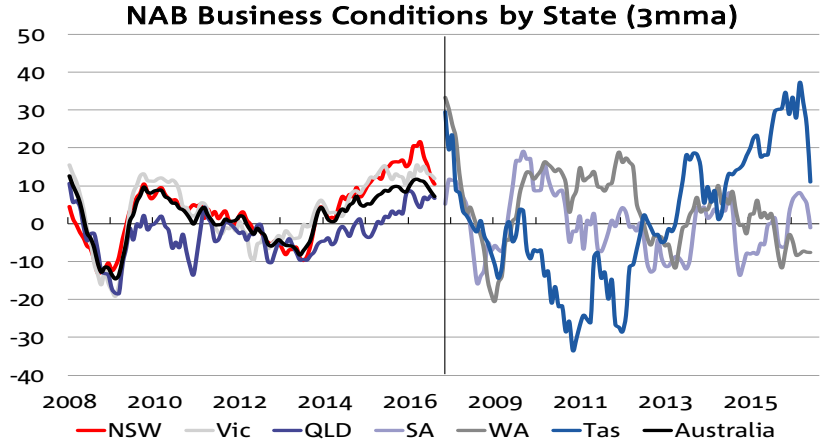
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CHARTS OF THE MONTH

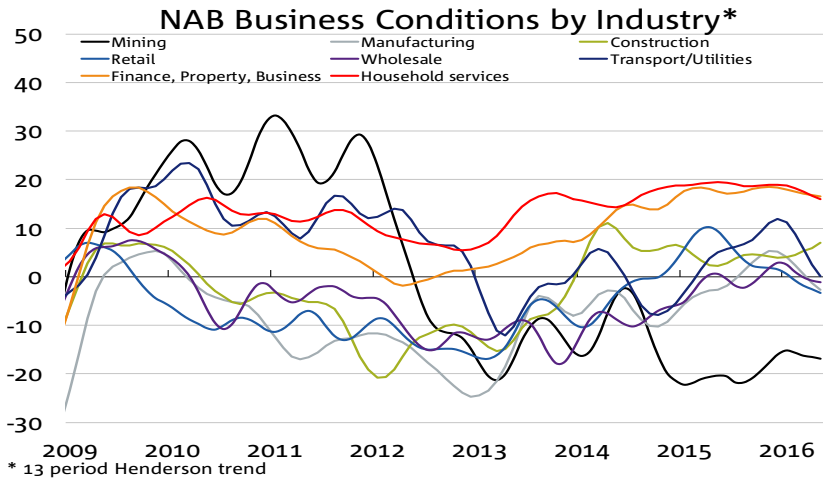
BUSINESS CONDITIONS SHOWING A DOWNWARD TREND. BUSINESS CONFIDENCE EASED, BUT IS TRACKING BROADLY SIDWAYS



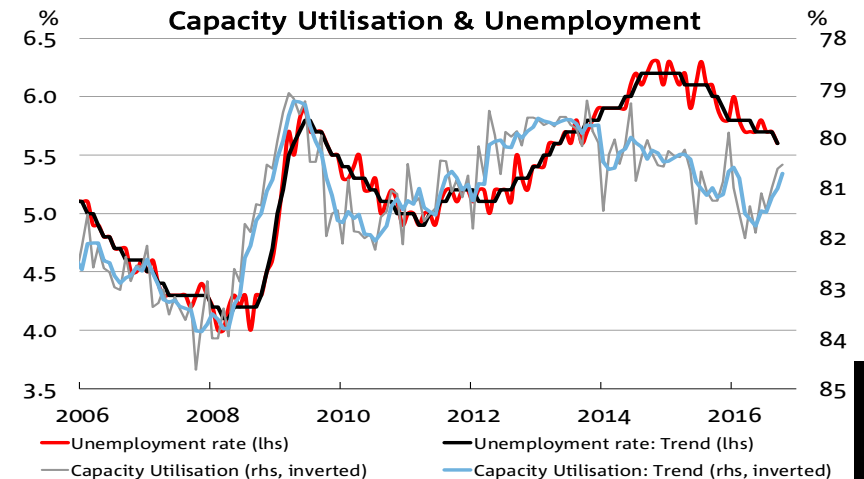
DIVIDE BETWEEN WA AND THE REST OF THE STATES REMAINS, BUT MAJOR NON-MINING STATES NOW EASING



NON-MINING ECONOMY PERFORMING WELL. SERVICES STILL THE CLEAR OUTPERFORMERS



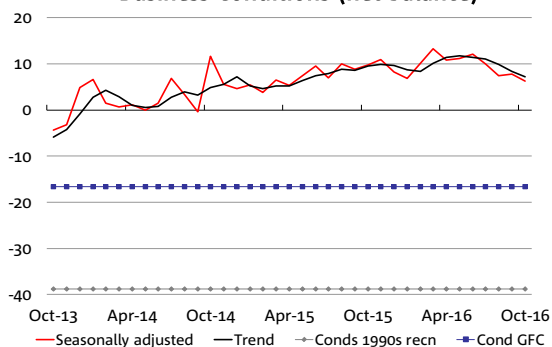
CAPACITY UTILISATION AND THE LABOUR MARKET



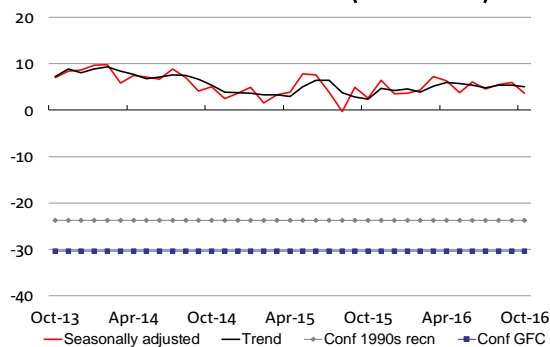
BUSINESS CONDITIONS AND FORWARD INDICATORS

Conditions above average, but trending lower. Near-term outlook weakened

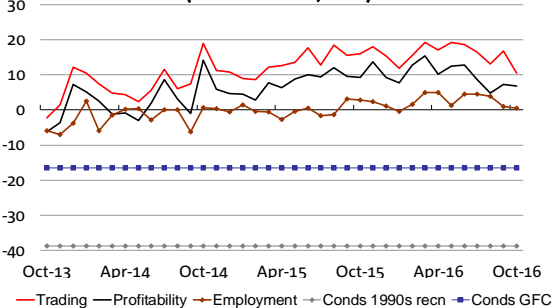
Business Conditions (net balance)



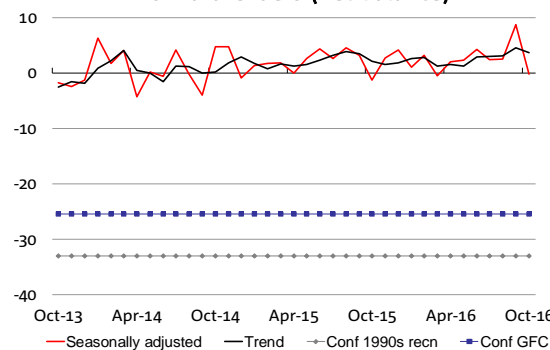
Business Confidence (net balance)



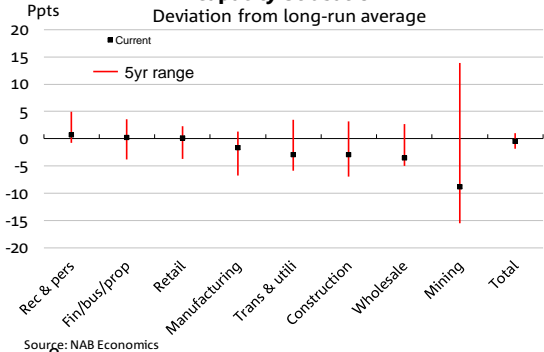
All components of business conditions (net balance, s.a.)



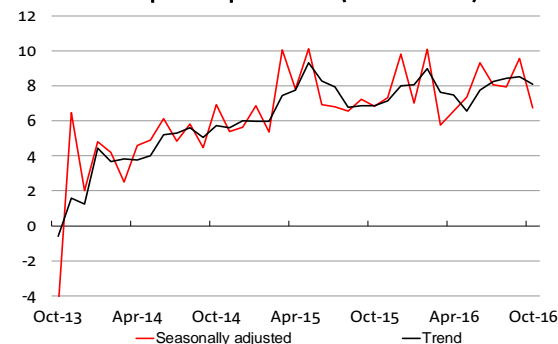
Forward Orders (net balance)



Capacity Utilisation



Capital Expenditure (net balance)

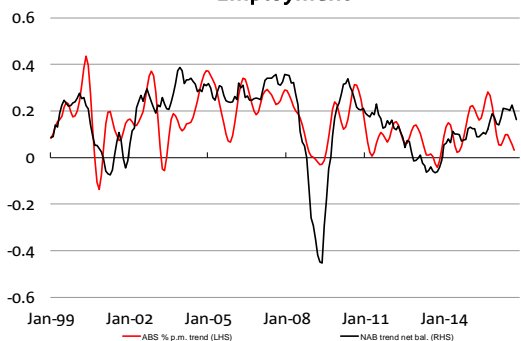


- Business conditions remain above long-run average levels, and have been for 20 straight months, but are now exhibiting a clear downward trend. The index fell by 2 points in October, to +6, which is modestly above the long-run average of +5. By component, both trading conditions and employment conditions declined in September, although the former remains elevated, while profitability was unchanged. Most industries saw a decline in conditions this month, although retail and transport were exceptions. Despite seeing declines this month, service industries remain the outperformers in trend terms, while mining and retail are trailing – industry details on p6.
- Business confidence also eased, but the trend has remained fairly steady for quite some time. This suggests firms have remained relatively unfazed by uncertainties stemming from events including Brexit and the upcoming US elections. The confidence index fell 2 points to +4 index points in September – a little below the long-run average (+6). Business confidence did not see any meaningful lift following the RBA’s interest rate cut back in August.
- By state, business conditions eased across most states in October, with Qld being the only exception. However, conditions continue to look solid in all three of the major eastern states – although NSW is now showing a clear downward trend and Victoria is starting to follow its lead. In trend terms, Victoria again had the strongest conditions, while WA remains the weakest. In terms of confidence, SA is currently best, although all states are positive (in trend terms).
- The near-term outlook appears less encouraging, according to some of the Survey’s leading indicators. The forward orders index more than gave back last month’s gains, dropping 9 points to 0 index points (consistent with the long-run average) – suggests moderate near-term prospects for activity. However, orders had been in positive territory for most of the past year and the trend has held up (industry details on p6).
- NAB’s measure of capacity utilisation also eased a little further this month, continuing the recent downward trend. Utilisation rates fell to 80.5% (from 80.6%), which is below the long-run average of 81%. The fall is consistent with softer trading conditions, and can help to explain the partial pull-back in the Survey’s capex measure (suggesting additions to capacity are less necessary). Utilisation rates are below long-term averages for most industries (see Chart) – industry detail on p6. But despite easing, at +7 index points, the capex indicator is more upbeat than other investment indicators.
- Cash flow (not seasonally adjusted) is looking solid, and was the strongest in recreational services, but weakest in mining.

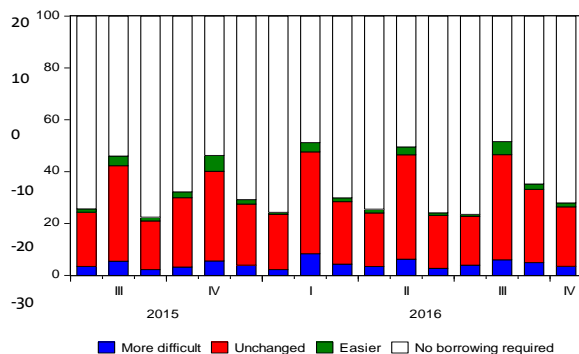


LABOUR, COSTS, PRICES & BORROWING CONDITIONS

Employment



Borrowing conditions (% of firms)



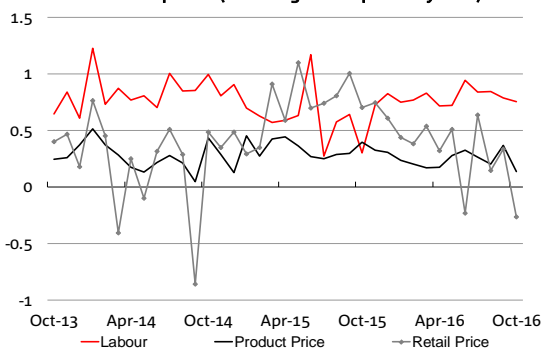
- There was another deterioration in employment conditions this month, unwinding the improvements seen since May and suggesting more subdued employment growth in the near-term. The employment index dropped to 0 index point (from +1), which is slightly below the long-run average for the series (+1). This outcome points to an annual job creation rate of around 180k (around 15k per month) in coming months, which is only sufficient to steady the unemployment rate, with all else unchanged – trend employment growth was just 3.8k in September according to the ABS.
- A majority of the major industry groupings in the Survey saw a deterioration in employment conditions, with the worst occurring in mining (down 33), followed by transport (-14). A couple of industries did improve, however, with finance/property/business services (up 4) rising the most. In trend terms, the employment index is still most negative for mining (-17 points), although manufacturing (-5), transport & utilities (-4) and wholesale (-4 points) are also negative. The strongest employment demand (trend) was in FPB services (+11).

PRICES & COSTS BY INDUSTRY (% CHANGE AT A QUARTERLY RATE)

Oct-2016	Mining	Manuf	Constn	Retail	Wsale	Tran. & utils	Rec. & pers.	Fin. prop. & bus.	Australia
Labour costs: current	1.1	0.7	1.6	0.2	0.4	1.2	1.0	0.8	0.8
Labour costs: previous	0.5	0.8	0.7	1.0	0.5	1.1	0.4	0.8	0.8
Labour costs: change	0.6	-0.1	0.9	-0.8	-0.1	0.1	0.6	0.0	0.0
Prices (final): current	-0.6	0.5	0.5	-0.3	1.1	0.3	0.2	-0.4	0.1
Prices (final): previous	-0.6	0.8	0.3	0.3	0.2	-0.2	0.9	-0.1	0.4
Prices (final): change	0.0	-0.3	0.2	-0.6	0.9	0.5	-0.7	-0.3	-0.3
Purchase costs: current	-1.3	0.7	0.2	-0.2	0.3	0.3	0.4	0.2	0.2
Purchase costs: previous	-0.5	0.6	1.0	1.0	-0.6	0.5	0.3	0.2	0.4
Purchase costs: change	-0.8	0.1	-0.8	-1.2	0.9	-0.2	0.1	0.0	-0.2

- Labour cost growth (a wage bill measure) was unchanged in the month and shows that wage pressures remain relatively steady at 0.8% (a quarterly rate). Labour cost pressures were highest in construction (at 1.6%), but were weakest in retail (0.2%) – which had previously been seeing some of the strongest wages growth, despite margin pressures.
- Growth in purchase costs were down slightly in the month, to 0.2% (at a quarterly rate, from 0.4%). This outcome was well below the long-run average, suggesting recent commodity price rises are not yet having an effect. Subdued inflation pressures have been a common theme globally and the magnitude of currency effects on prices has been much more muted than expected in Australia. Growth in purchase costs decelerated the most in retail (down 1.2 pts), while wholesale saw the largest increase, up 0.9 pts. Overall, purchase cost pressures were highest in manufacturing (0.7%, quarterly rate), but softest in mining (-1.3%).
- Final product prices growth in September eased to just 0.1% (a quarterly rate, from 0.4%). Retail price growth was especially weak (-0.3%), which is well below the lower bound of the RBA's inflation target. Personal services (down 0.7 pts) and retail (down 0.6 pts) saw the largest deceleration in final prices growth. In contrast, wholesale (up 0.9 pts) had the biggest acceleration. Mining prices fell 0.6%, while price growth was highest in wholesale (0.9%). Final prices inflation has generally not kept pace with the rise in input costs, which is likely restricting the profitability index – although it was more resilient than trading conditions this month.
- Borrowing conditions appear to have improved from 3 months prior, while the demand for credit has increased as well.

Costs & prices (% change at a quarterly rate)

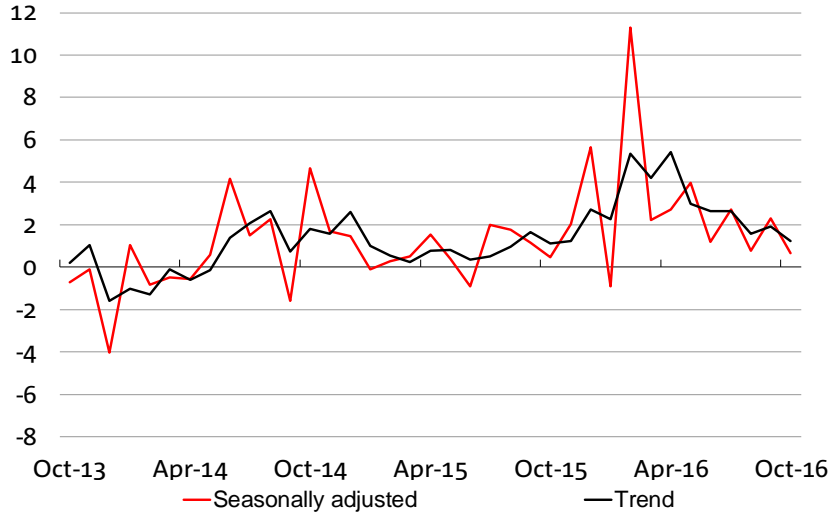


Based on respondent estimates of changes in labour costs and product prices. Retail prices are based on retail sector product price estimates.

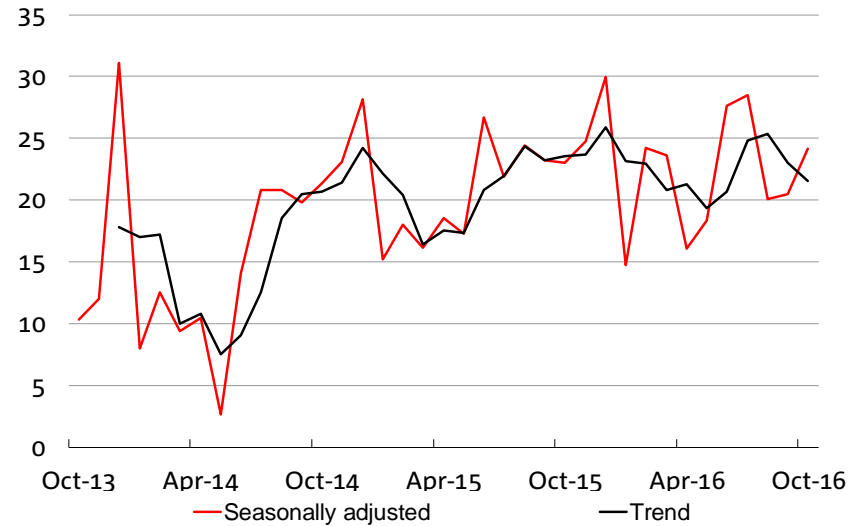
MORE DETAILS ON BUSINESS ACTIVITY

Re-stocking slowed further. Exports modest. Cash flows holding up.

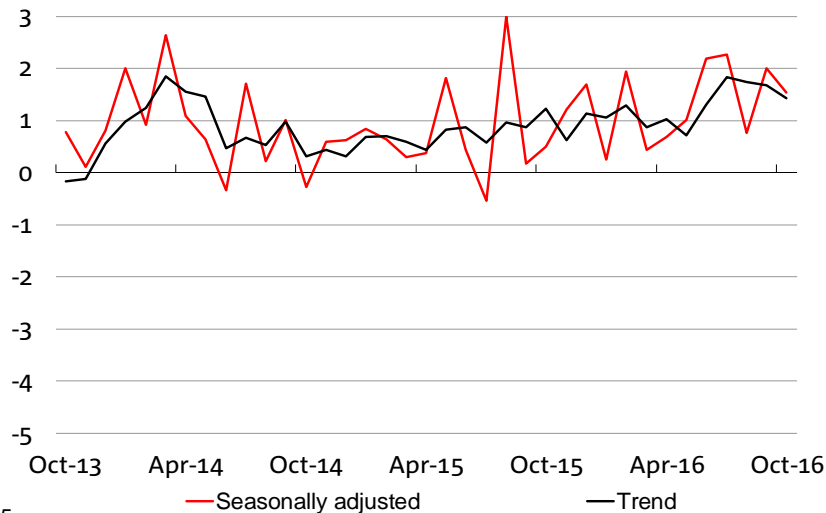
Stocks (net balance)



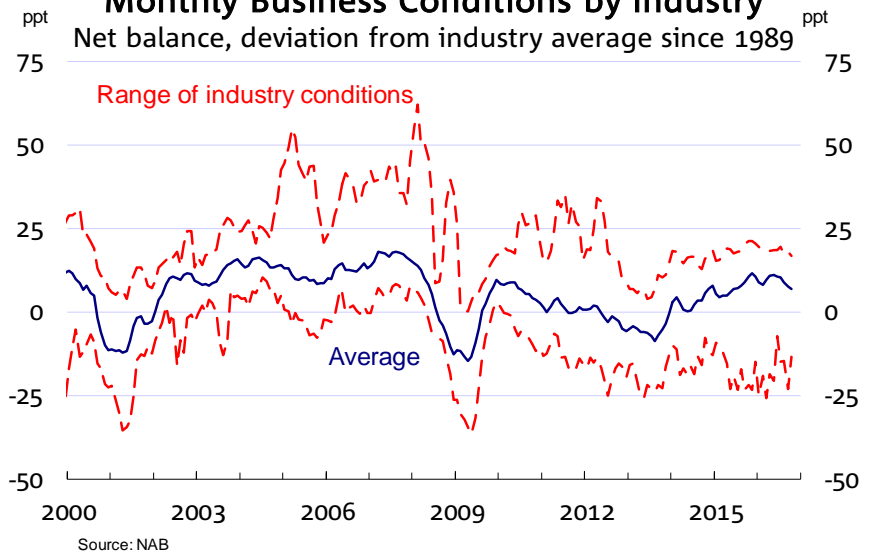
Cash Flows (net balance, nsa)



Exports (net balance)



Monthly Business Conditions by Industry

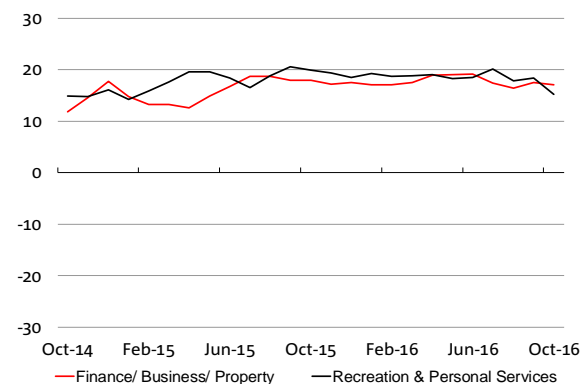
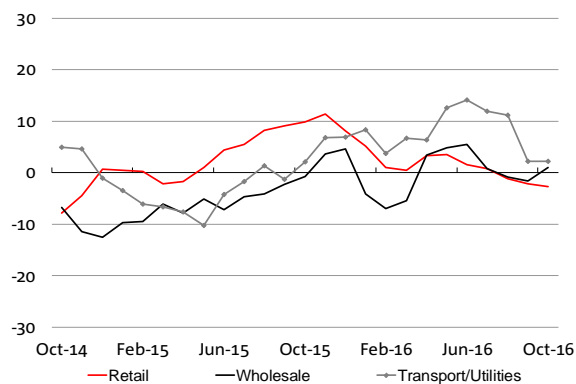
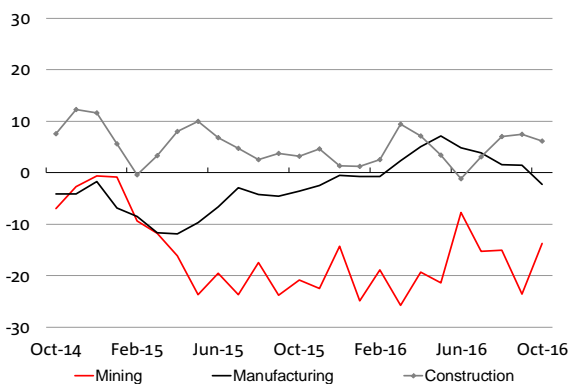


INDUSTRY BUSINESS CONDITIONS & CONFIDENCE

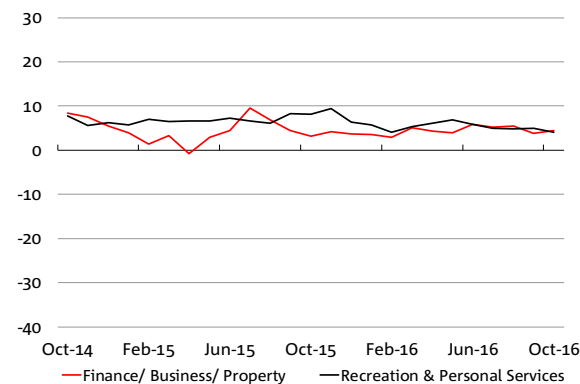
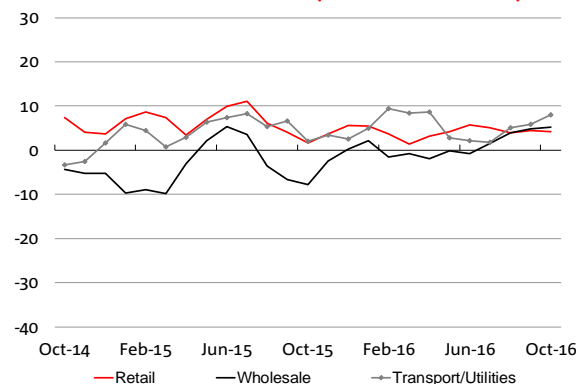
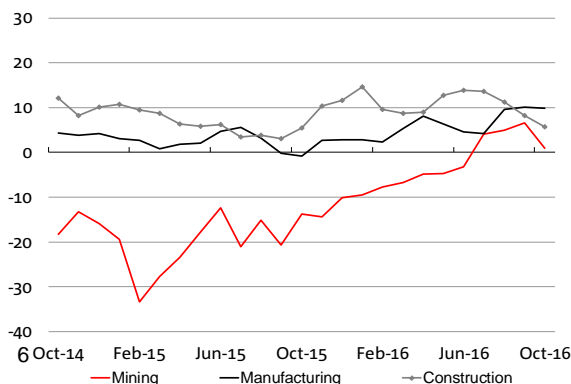
Less divergence in business conditions, but mostly due to a fall in best performers

- The deterioration in **business conditions** this month was seen across most industries, with mining (down 12), wholesale (down 10) and recreation & personal services (down 10) falling the most. In contrast, retail (up 12) and transport (up 9) were the only industries to improve – although conditions in both remain quite subdued overall. In trend terms (3mma), conditions are now highest in finance/ property/ business (FPB) (+17) and recreation & personal services (+15), but lowest in mining (-14) and retail (-3). The largest fall in **business confidence** came from mining (down 9), while transport (up 6) saw the biggest improvement. In trend terms, all industries are reporting positive confidence levels, but manufacturing (+10) was the most confident, while mining is now weakest (at +1).
- Most industries reported weaker **forward orders** in the month, but the deterioration was particularly large for mining (down 49) and transport (down 28). In contrast, construction was the only industry to see an improvement (up 8). In trend terms, orders are positive for most industries excluding wholesale (-4) and retail (0). Manufacturing orders (trend) were highest at +7. Changes in **capacity utilisation** varied across industries, but wholesale (down 6.1 pts) and construction (down 1.8 pts) saw the worst of the falls. Capacity utilisation in personal services is currently highest above 5-year average levels (slide 3), which is consistent with relatively elevated business conditions. Consequently, personal services also had the highest **capex** index (+16) in trend terms. Construction is lowest (-2), which might reflect mining investment headwinds.

BUSINESS CONDITIONS BY INDUSTRY (NET BALANCE): 3-MONTH MOVING AVERAGE



BUSINESS CONFIDENCE BY INDUSTRY (NET BALANCE): 3-MONTH MOVING AVERAGE

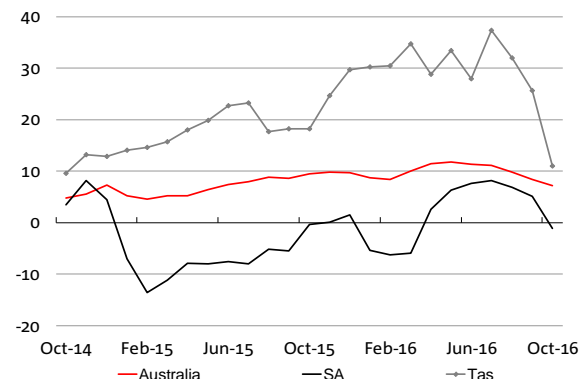
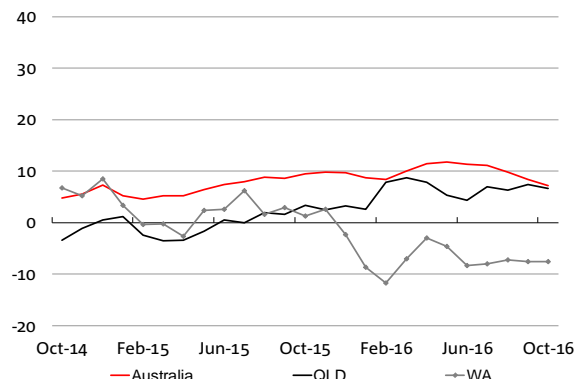
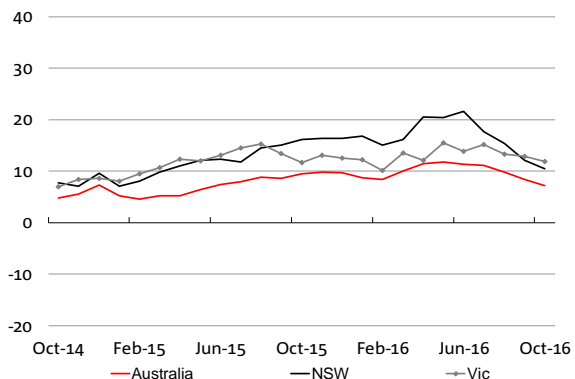


STATE BUSINESS CONDITIONS & CONFIDENCE

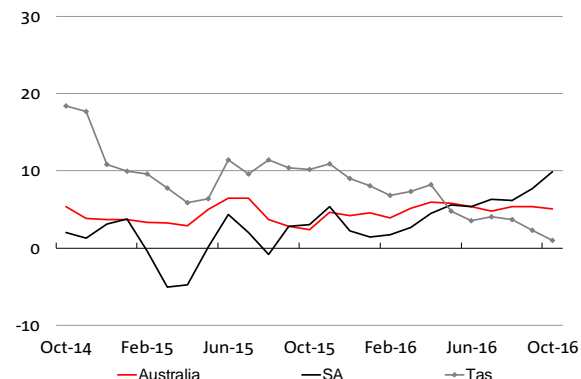
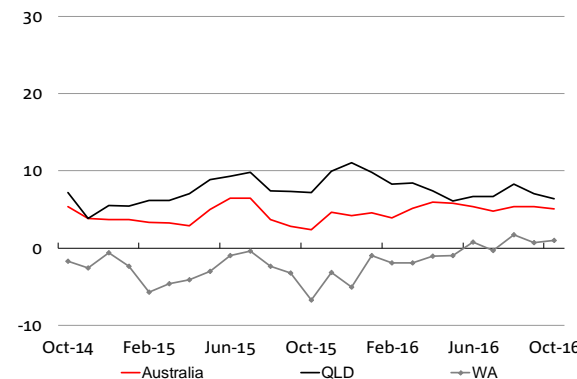
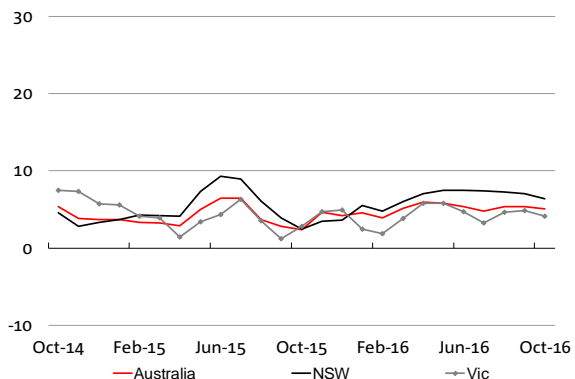
Softer trends in NSW and Vic raise some concerns about the non-mining recovery

- In trend terms, **business conditions** have continued to softened in NSW (down 2 to +10), and while Victoria is now ranked the highest mainland state, business conditions there has also drifted lower – the trend index in Victoria fell 1 to +12. Last months jump in WA business conditions was partially unwound, falling 5 points to -9 (but unchanged in trend terms), while SA conditions fell noticeably (down 6 to -1 index points in trend terms). Qld was the only state to see a modest improvement.
- On **business confidence**, all states other than SA were flat-to-lower in trend terms. NSW, Vic & Qld all eased by 1 point, while WA was flat and SA was up 2 points. SA is now most confident (+10 in trend terms), followed by NSW and QLD (both +6), while WA is still least confident (+1 index points).
- **Employment conditions** (trend) are positive in most states, with WA and SA (both -6) the exception. Qld was the only state to see an improvement in the trend employment index this month (up 3), while the worst deterioration was in SA (down 11) – unwinding much of the positive progress made recently. NSW has steadily eased from its recent peak of +11 (to +3), while Victoria has improved modestly over that period despite easing back this month (down 1 to +5).

BUSINESS CONDITIONS BY STATE (NET BALANCE): 3-MONTH MOVING AVERAGE



BUSINESS CONFIDENCE BY STATE (NET BALANCE): 3-MONTH MOVING AVERAGE



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