

NAB MONTHLY BUSINESS SURVEY

AUGUST 2017

NEXT RELEASE:
10 OCT 2017 – SEPTEMBER MONTHLY



Key points:

- Business conditions continued their solid run in August, while business confidence has taken a hit, although recent volatility suggests we should exercise caution when interpreting the result.
- Business conditions rose by 1 point in August to hit +15 index points, which is the highest level for the series since early 2008 and is significantly higher than the long run average level. Most industries appear to be performing well, but retail remains a concern with retail conditions languishing in negative territory (neutral in trend terms). We will be watching this trend closely as household consumption is a notable point of difference between our relatively subdued growth outlook and the RBA's more sanguine forecasts. **By component, there was a notable jump in employment for August (to near record highs). Trading and profitability eased back slightly, but remain at very high levels.** If employment conditions maintain these levels, that should see more than sufficient jobs creation to push the unemployment rate lower. Consistent with that, there was also a lift in a number of inflation measures from the Survey. Labour costs accelerated the most, but both final and upstream prices accelerated as well. That said, retail price inflation dipped back into negative territory in August. Meanwhile, the survey's measure of **capex improved in the month, despite a slight rise in spare capacity, while forward orders rose modestly.**
- The sharp drop in business confidence this month is somewhat concerning, although the deterioration may prove to be short lived. **The business confidence index dropped by 7 points in August, to be at +5 index points – the first time it has fallen below the long-run average since mid-2016.** While exogenous shocks such as the escalating tensions with North Korea may have contributed to the move this month, for the first time we have asked firms an additional question on what factors are having the biggest impact on their confidence. For those indicating a deterioration in confidence, demand, margins, government policy and costs (energy and wages) play a major role (detail on p5).
- The recent run of economic data has (for the most part) been relatively upbeat, consistent with the strong results evident for some time in the NAB Business Survey. Improvements in labour market indicators point to further falls in the unemployment rate, helping to mount a case for bringing forward RBA rate rises. However, there are few signs of inflation/wage pressures in the official data as yet, while relatively downbeat consumer confidence is still a point of concern in light of poor retail conditions in the NAB survey – the consumption outlook is key to the economy's sustained return to trend growth. Additionally, the previously emphasised hurdles to growth – elevated underemployment, an elevated AUD, household debt and peaks in LNG exports and housing construction – remain firmly in place. Consequently, while the recent run of better data may shift the risks towards a sooner than expected hike in the RBA's cash rate, the risks will ensure that the RBA proceed with extreme caution. **More details on our economic forecasts will be released tomorrow.**

Table 1: Key monthly business statistics

	Jun 2017	Jul 2017	Aug 2017		Jun 2017	Jul 2017	Aug 2017
	<i>Net balance</i>				<i>Net balance</i>		
Business confidence	9	12	5	Employment	8	7	11
Business conditions	14	14	15	Forward orders	5	3	4
Trading	20	19	18	Stocks	4	0	0
Profitability	15	16	15	Exports	2	-1	0
	<i>% change at quarterly rate</i>				<i>% change at quarterly rate</i>		
Labour costs	1.1	0.7	1.2	Retail prices	0.3	0.0	-0.1
Purchase costs	0.6	0.4	0.6		<i>Per cent</i>		
Final products prices	0.5	0.2	0.4	Capacity utilisation rate	81.9	81.9	81.6

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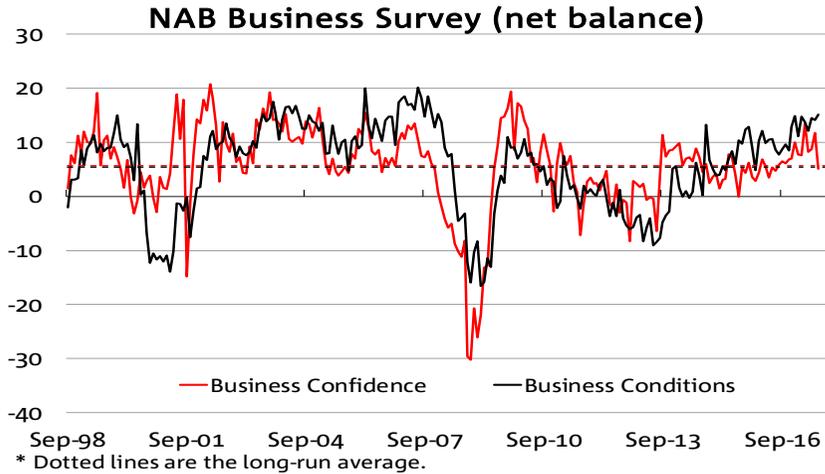
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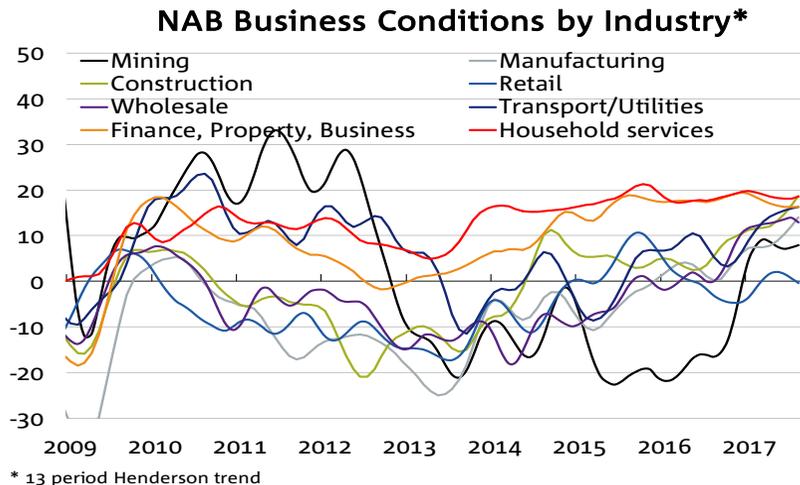
* All data seasonally adjusted and subject to revision. Cost and prices data are monthly percentage changes expressed at a quarterly rate. Fieldwork for this survey was conducted from 21 August to 25 August, covering more than 540 firms across the non-farm business sector.

KEY MONTHLY CHARTS

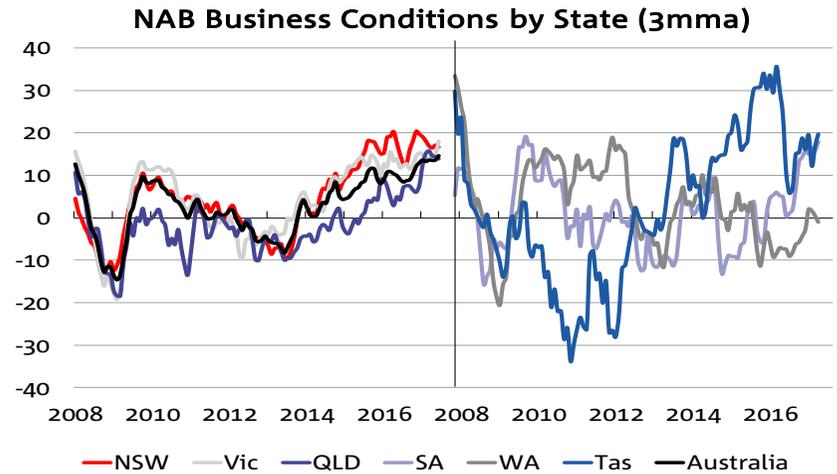
BUSINESS CONDITIONS DRIFTING TOWARD RECORD HIGHS. CONFIDENCE HITS A ROADBLOCK



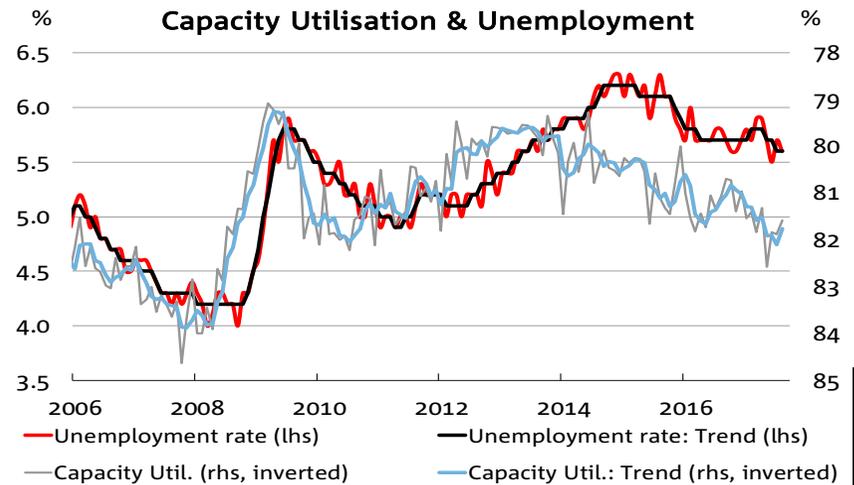
ALL INDUSTRIES ARE POSITIVE, BUT RETAIL APPEARS TO BE DETERIORATING AGAIN



CONDITIONS HOLDING-UP IN MOST STATES. WA IS STILL SUBDUED BUT IS UP FROM PREVIOUS LOWS



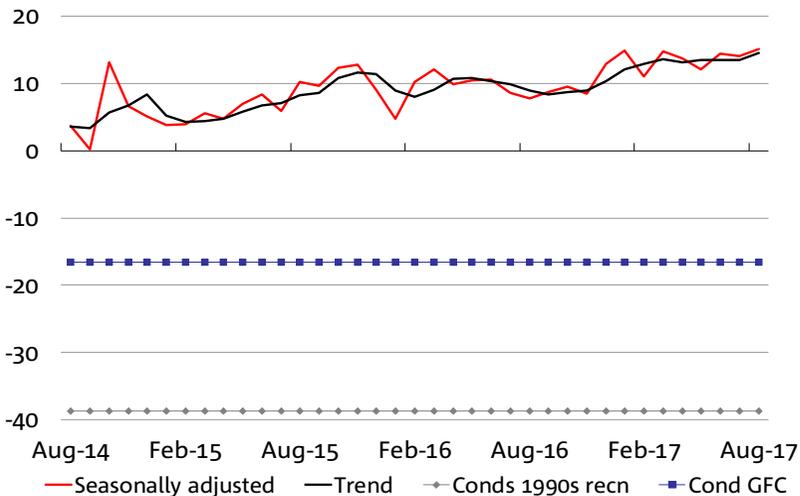
CAPACITY UTILISATION SHOWS LIMITED SLACK – CONSISTENT WITH DROP IN THE UNEMPLOYMENT RATE



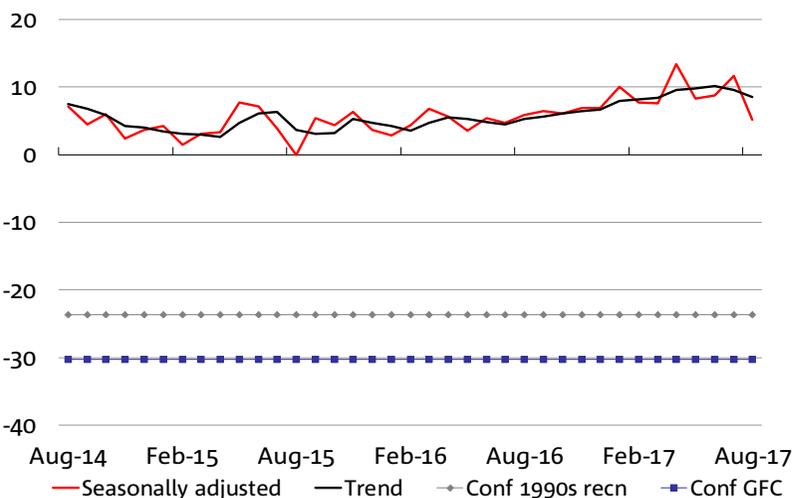
BUSINESS CONDITIONS AND FORWARD INDICATORS

Conditions continue their strong run, but confidence takes a dive.

Business Conditions (net balance)



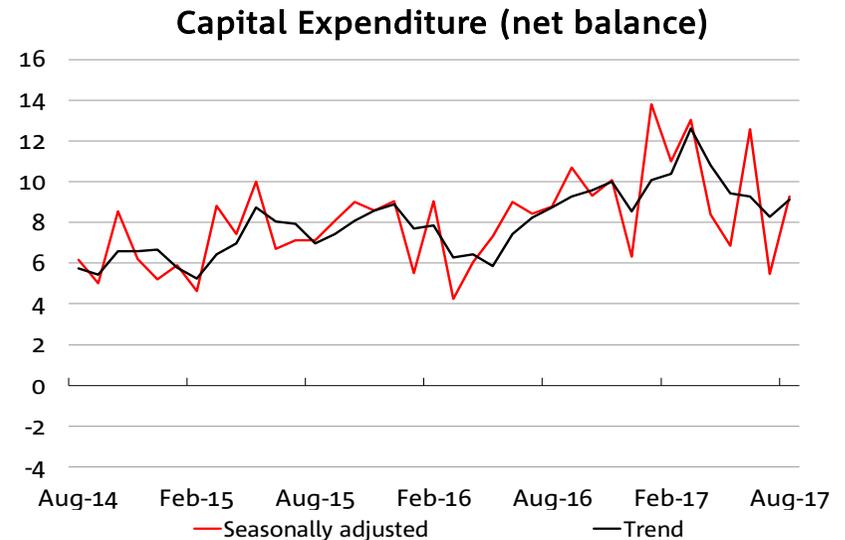
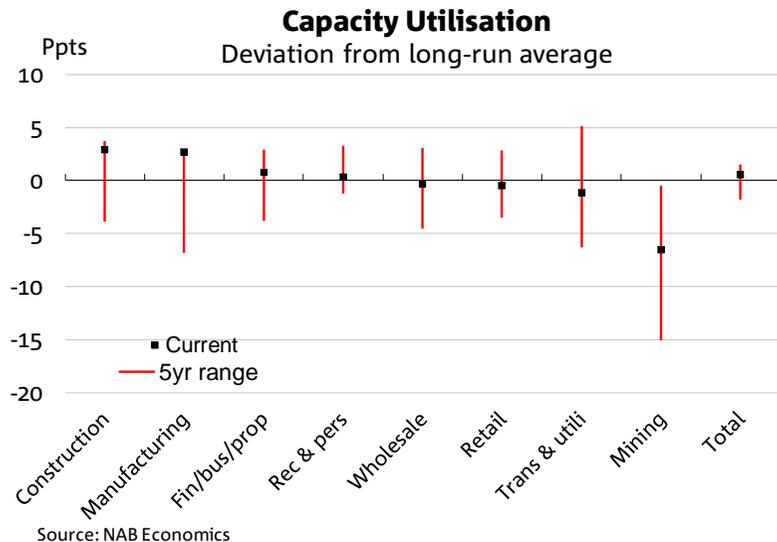
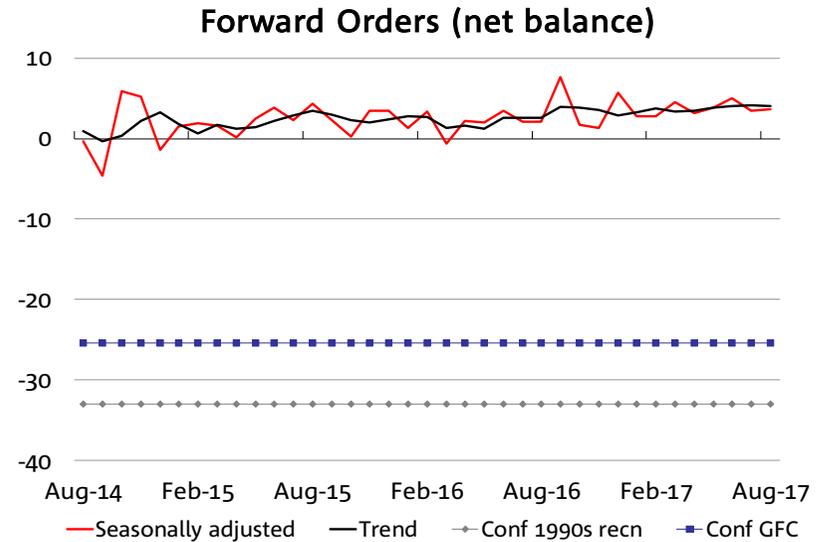
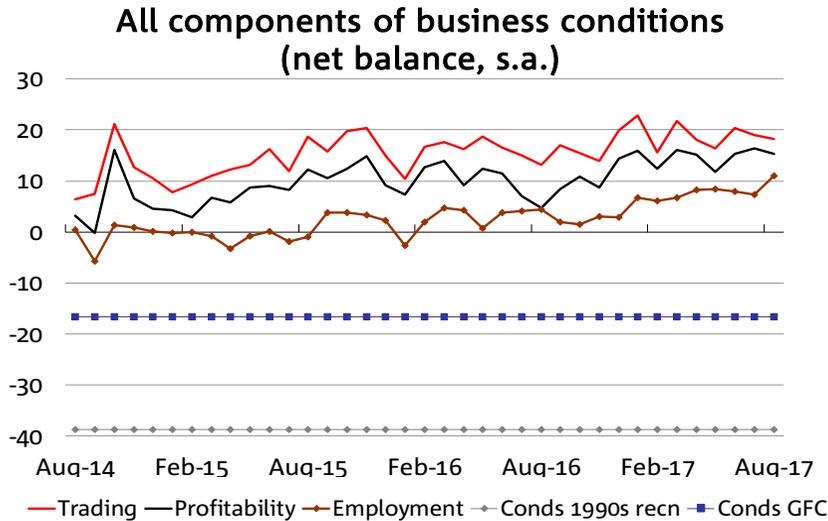
Business Confidence (net balance)



- **Business conditions** managed to ebb higher from their already elevated level in August, providing more encouraging signs on the health of the economy. The business conditions index rose 1 point, to +15 index points, which is well above the long-run average (+5). Employment conditions saw the biggest gains of the three components, while both profitability and trading conditions deteriorated. In trend terms, business conditions are positive for most industries, although retail is a notable exception and appears to be deteriorating once again (more detail on p8).
- Despite impressive levels of business conditions, **business confidence** took a dive this month, with the index dropping 7 points to just +5 index points (below the long-run average, +6). It is possible that external shocks, such as escalating tensions with North Korea, contributed to the decline, although new information from the survey indicates that customer demand, margin squeeze, government policy are having the greatest influence on confidence at present (see p5). Despite the drop, confidence levels are currently positive for all industries (see p7 for industry details).
- Of the mainland states, the rise in **business conditions** was driven by Victoria (up 10) and South Australia (up 14), but were largely offset by falls in NSW (down 10), Queensland (down 4) and WA (down 1). WA remains the only state in negative territory, while all other states remain quite solid. Abstracting from the usual monthly volatility, Victoria and SA have moved into the top spot for the mainland states, with trend conditions sitting at +18 index points. The other states are following close behind however, with NSW at +17 and Qld on +14 index points. While being well up from its previous trough, WA is underperforming (at -1) and appears to be trending lower again. Meanwhile, **business confidence** is positive in all states, even though most saw a marked deterioration in August. Of the mainland states, confidence is highest in trend terms for NSW and Qld (+11), but lowest in WA at +6 index points (trend).
- The more forward looking indicators from the Survey have remained relatively upbeat. The **forward orders** index was up slightly to +4 index points (above the long-run average of zero, see chart on p4), driven by an especially large increase in manufacturing orders (up 16). In contrast, retail orders fell sharply (down 21), which is consistent with the concerning trend seen in retail conditions. Despite easing somewhat, orders are still highest in construction (+17, in trend terms), in line with the surprising resilience in residential building approvals lately. Trend orders are only negative for retail (-3).
- NAB's measure of **capacity utilisation** was lower in August (down 0.3ppts to 81.6%). Despite the rise in spare capacity, the Survey's **capex** measure jumped 4 points to +9 index points (see chart on p4). Capacity utilisation rates are currently above long-run averages for around half the major industry groups in the Survey (see chart on p4 and industry detail on p7). Mining is sitting furthest below its long-run average despite the recent ramping-up of LNG exports.
- **Cash flow** (not seasonally adjusted) eased back slightly, but is still elevated (chart on p7). It is currently strongest in wholesale, but weakest in retail.

BUSINESS CONDITIONS AND FORWARD INDICATORS (CONT.)

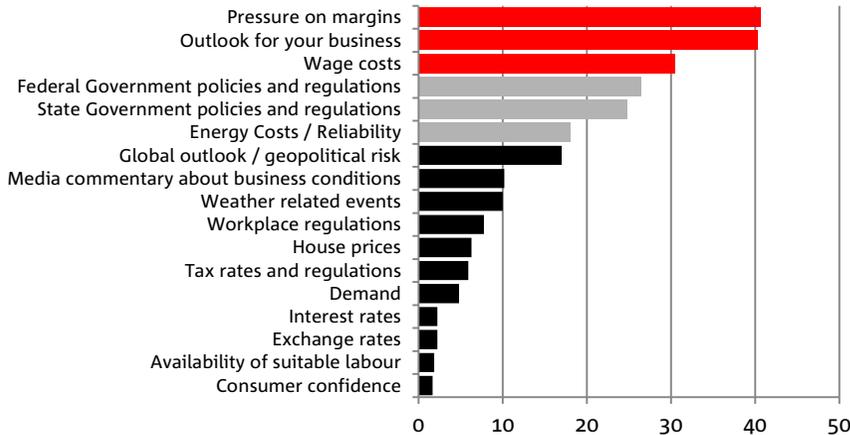
Components of business conditions & leading indicators



DRIVERS OF BUSINESS CONFIDENCE

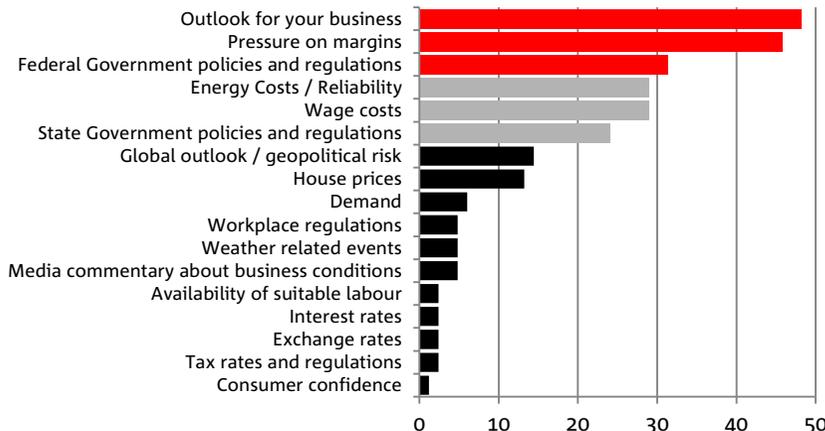
Demand, margins and policy are most significant for firms with weaker confidence.

Most influential issues affecting business confidence

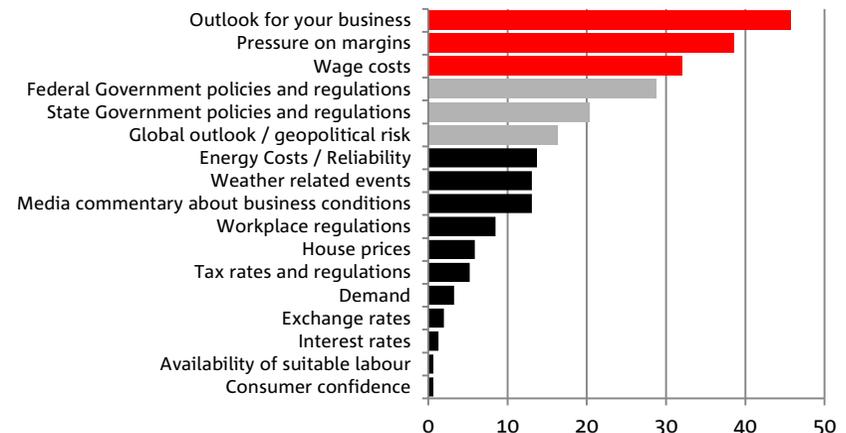


- This month we have included a new question in the NAB Business Survey which asks firms about what are the most influential factors impacting their confidence. This question will remain in the Survey going forward, but will only be asked on a quarterly basis.
- While we do not know how the significance of each factor has evolved at this juncture, the results provide an interesting insight into what is at the forefront of business concerns in Australia. Despite whether firms have indicated an improvement or a deterioration in confidence recently, there appears to be some common themes. In particular, firms are mostly concerned with the outlook for customer demand, pressure on margins, and government policy
- Costs also tend to feature prominently (both wages and energy costs), although firms indicating a deterioration in confidence place more concern on energy costs over wage costs at present.
- Interestingly, geopolitical risks did not feature in the top 5 concerns for firms, despite escalating tensions with North Korea – although the missile launch over Japan did not take place until quite late in the month. However, as mentioned above, we do not know how the significance of this issue has evolved over time (it is still possible that it has become more significant than previously).

Most influential issues affecting business confidence - Deteriorating Confidence

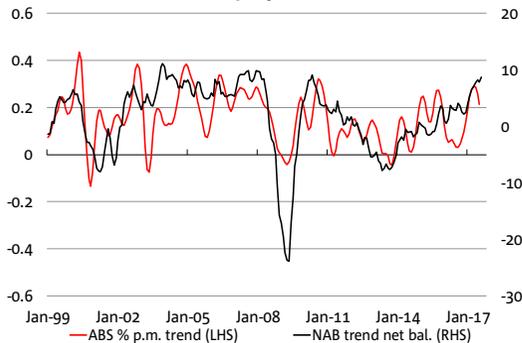


Most influential issues affecting business confidence - Improving Confidence

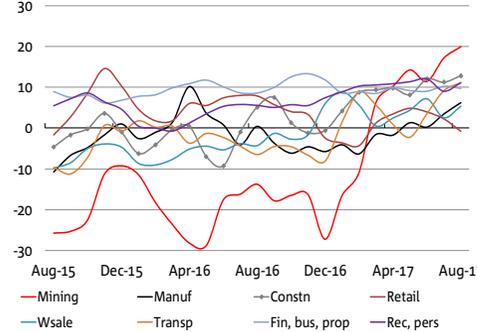


LABOUR DEMAND, COSTS, PRICES & BORROWING CONDITIONS

Employment



Employment by Industry



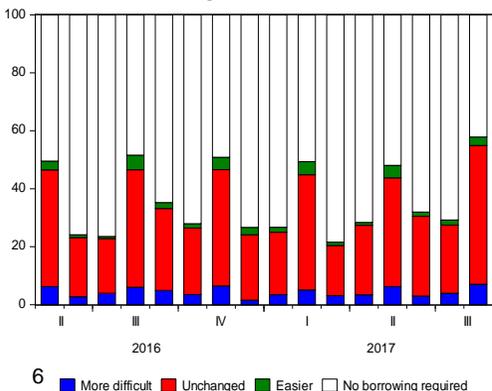
- There was an impressive jump in **employment conditions** during August, continuing the recent run of stronger labour market indicators. The ABS labour force survey has been showing strong job gains of late, and solid employment conditions in the NAB Survey suggest that is likely to continue over coming months. The employment index jumped 4 points, to +11 index points, which is well above the long-run average for the series and not far from record highs. This outcome points to an annual job creation rate of around 270k (around 22k per month) in coming months, which is sufficient to see the unemployment rate push lower (all else unchanged) – trend ABS employment growth was 26.2k in July.
- By industry, employment conditions picked-up the most in recreation & personal services (up 12), followed by manufacturing (up 6). Meanwhile, the largest decline was in transport (down 10). In trend terms, mining and construction have the best employment conditions (at +20 and +13 index points respectively) – labour demand from mining has improved considerably in the survey over the past 6-months or more (see chart). Retail is the only industry showing negative employment conditions (trend).

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

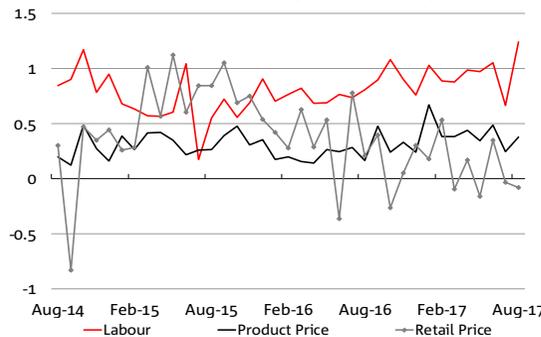
Aug-2017	Mining	Manuf	Constn	Retail	Wsale	Trans&utils	Rec.&pers.	Fin,prop.&b us.	Australia
Labour costs: current	1.1	1.5	1.2	0.9	1.0	1.4	1.5	0.9	1.2
Labour costs: previous	-0.7	0.7	0.8	0.8	0.4	0.7	0.6	0.9	0.7
Labour costs: change	1.8	0.8	0.4	0.1	0.6	0.7	0.9	0.0	0.5
Prices (final): current	0.5	0.5	0.0	-0.1	0.6	0.2	0.7	0.4	0.4
Prices (final): previous	0.3	0.7	0.2	0.0	0.1	0.0	0.4	0.4	0.2
Prices (final): change	0.2	-0.2	-0.2	-0.1	0.5	0.2	0.3	0.0	0.2
Purchase costs: current	-0.2	0.4	1.2	0.5	0.7	0.3	0.6	0.4	0.6
Purchase costs: previous	0.4	0.3	0.4	0.0	0.6	0.1	0.7	0.3	0.4
Purchase costs: change	-0.6	0.1	0.8	0.5	0.1	0.2	-0.1	0.1	0.2

- **Labour costs** growth (a wage bill measure) lifted in July, to 1.2% (a quarterly rate, previously 0.7%). Labour cost inflation has been relatively subdued, but this month's jump pushes it to its highest level since early 2014. Labour costs accelerated in most industries leaving wage pressures particularly strong in manufacturing and recreational & personal services (both at 1.5%). Labour cost inflation was softest in fin/ prop/ bus services and retail (0.9%).
- Growth in **purchase costs** also strengthened in the month, to 0.6% (a quarterly rate, previously 0.4%), although this still points to relatively subdued upstream cost pressures. Growth in purchase costs accelerated most notably in construction (up 0.8 pts), although most industries were higher. Overall, purchase cost pressures were strongest in construction (at 1.2%, quarterly rate), and weakest in mining (-0.2%). Higher construction costs may reflect elevated levels of residential building activity (tighter capacity).
- Margins may have taken a hit as **final product prices** growth failed to keep up with input costs – rising 0.4% (a quarterly rate), up from 0.2% last month. Retail price inflation returned to negative, at -0.1% (from +0%), suggesting further headwinds to CPI. Prices are flat-to-rising in all other industries.
- **Borrowing conditions** have deteriorated notably since May, with the index hitting its lowest (negative level since early 2016 – meaning that on balance, more firms found it more difficult to borrow than easier. Despite the negative index, demand for credit has improved in that time.

Borrowing conditions (% of firms)



Costs & prices (% change at a quarterly rate)



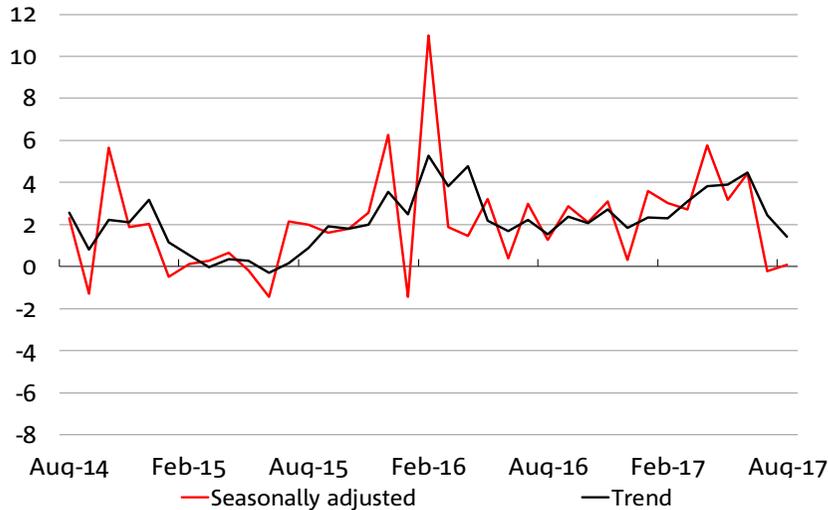
Based on respondent estimates of changes in labour costs and product prices. Retail prices are based on retail sector product price estimates.



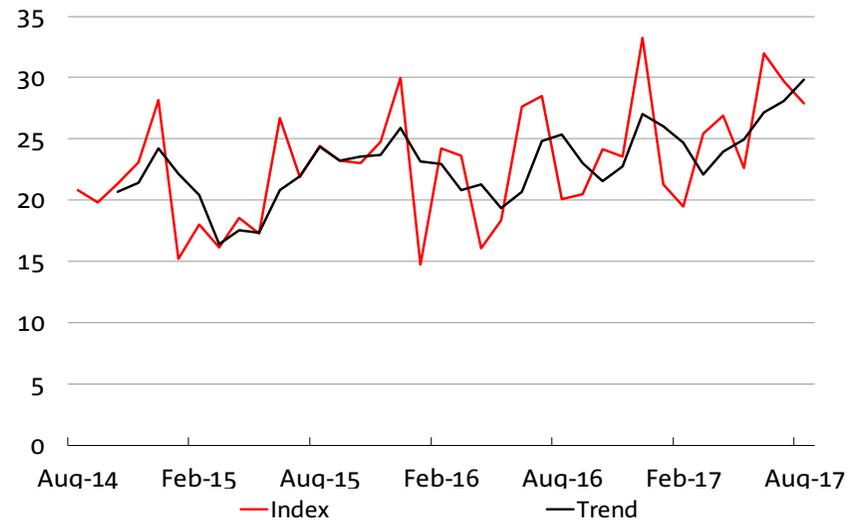
MORE DETAILS ON BUSINESS ACTIVITY

Restocking activity and exports still soft. Cash flows eased, but are elevated.

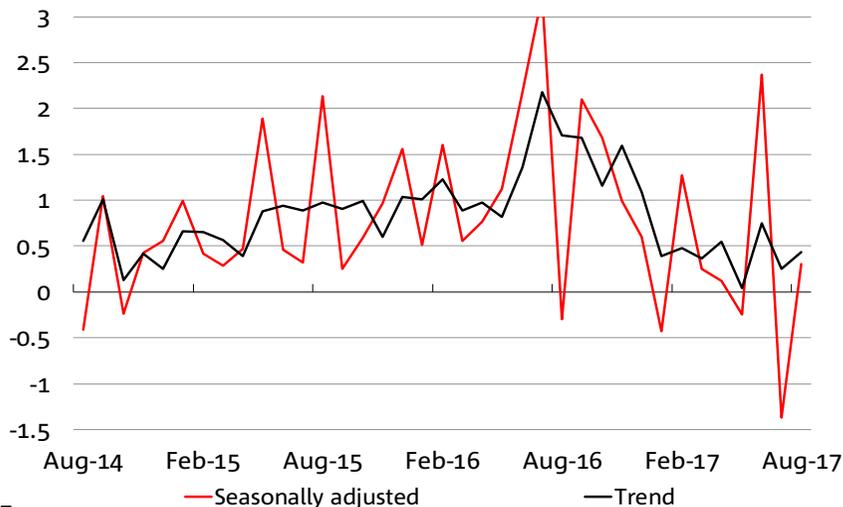
Stocks (net balance)



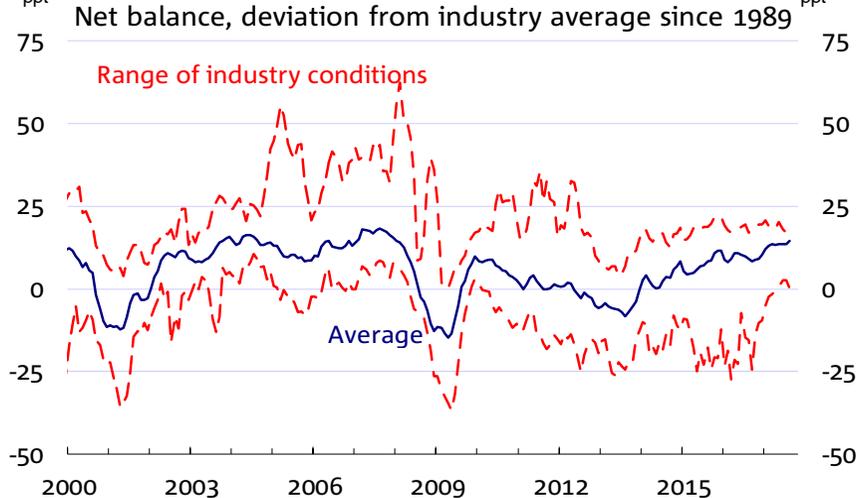
Cash Flows (net balance, nsa)



Exports (net balance)



Monthly Business Conditions by Industry



Source: NAB

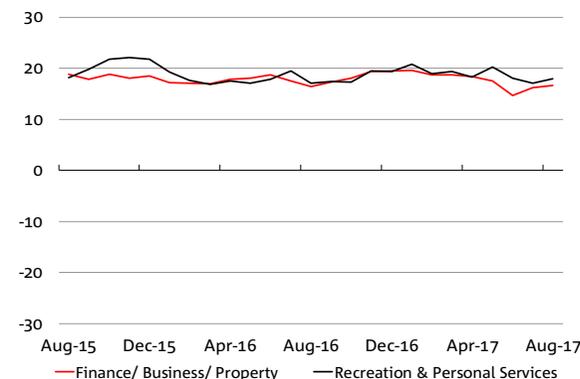
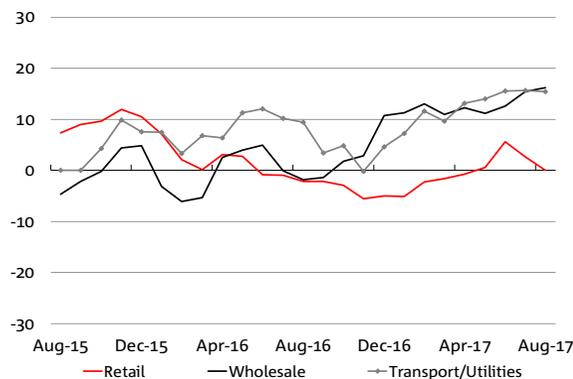
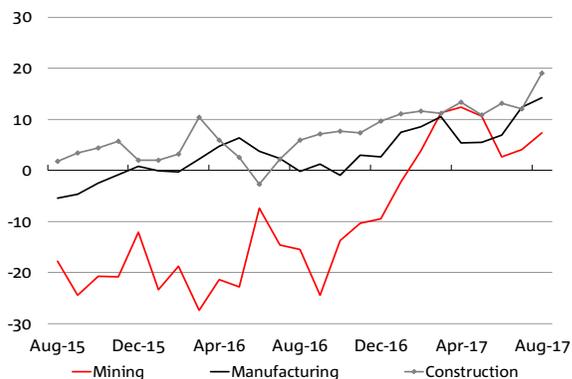


INDUSTRY BUSINESS CONDITIONS & CONFIDENCE

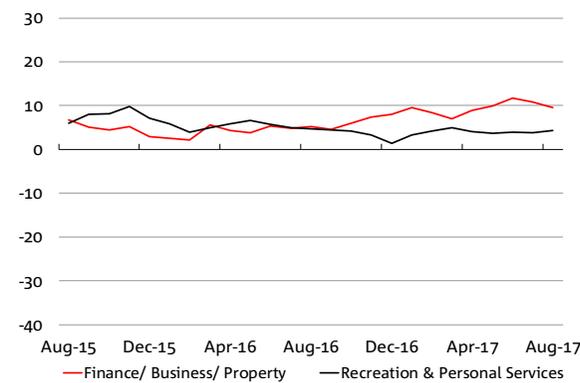
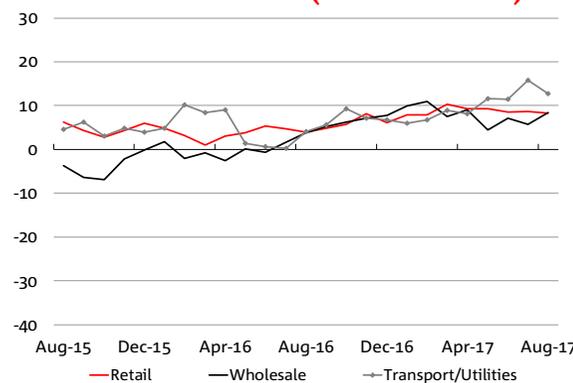
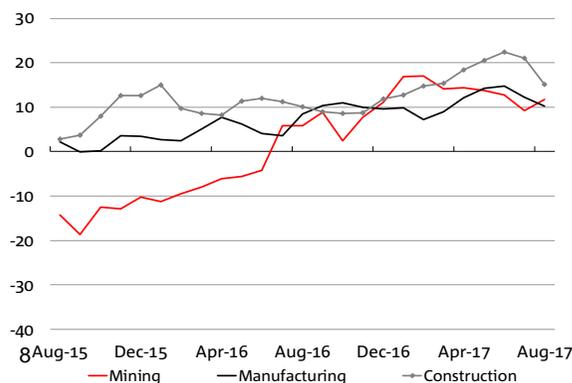
Residential and infrastructure supporting construction. Retail still disappointing

- The strength in aggregate **business conditions** can also be seen across most industries in the NAB Survey. Conditions are currently positive in almost all industries, with retail being the only exception. Construction has seen a steady improvement in conditions over the past year or more, and stepped up sharply in August, potentially spurred on by public investment in infrastructure and high levels of residential construction activity. Meanwhile, transport recorded the largest deterioration in conditions during August, although conditions for the industry remain quite positive. In trend terms, conditions are now highest in construction (at +19), but weakest in retail (0 index points).
- Despite a sharp fall in August, **business confidence** is positive in all industries. The biggest decline in August came from transport (down 17), while mining reported the largest improvement in confidence (up 8). Construction maintains the highest level of confidence in trend terms (+15), while personal services are lowest (+4).
- **Forward orders** rose slightly in August, and were flat to higher in most industries. Retail orders fell sharply (down 21), more than unwinding a surprise jump in the previous month. Orders are highest in construction (+17, in trend terms), consistent with elevated residential building approvals, while they are negative for retail (-3). Personal services and mining **capital expenditure** are highest in trend terms, although all are positive (only modestly so in retail and fin/prop/bus services).

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



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

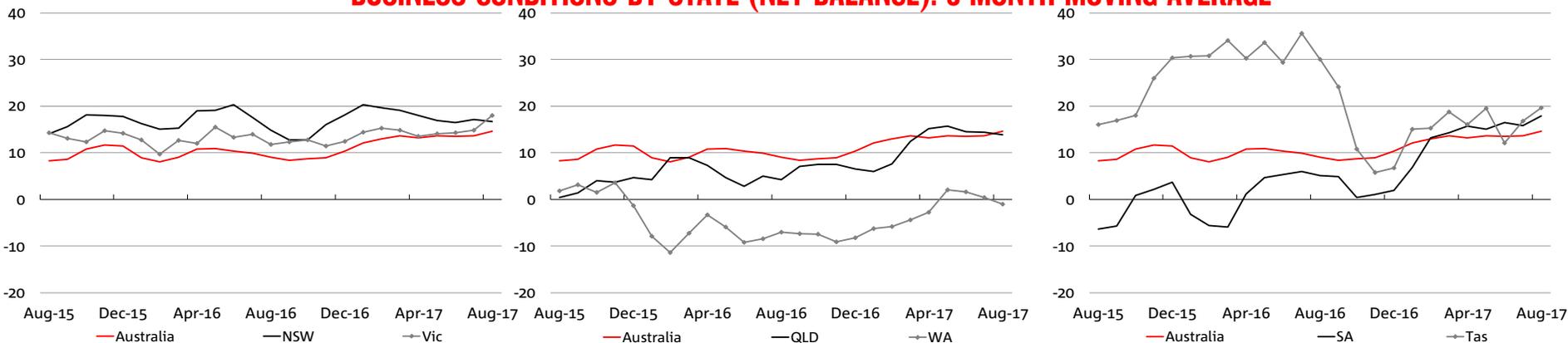


STATE BUSINESS CONDITIONS & CONFIDENCE

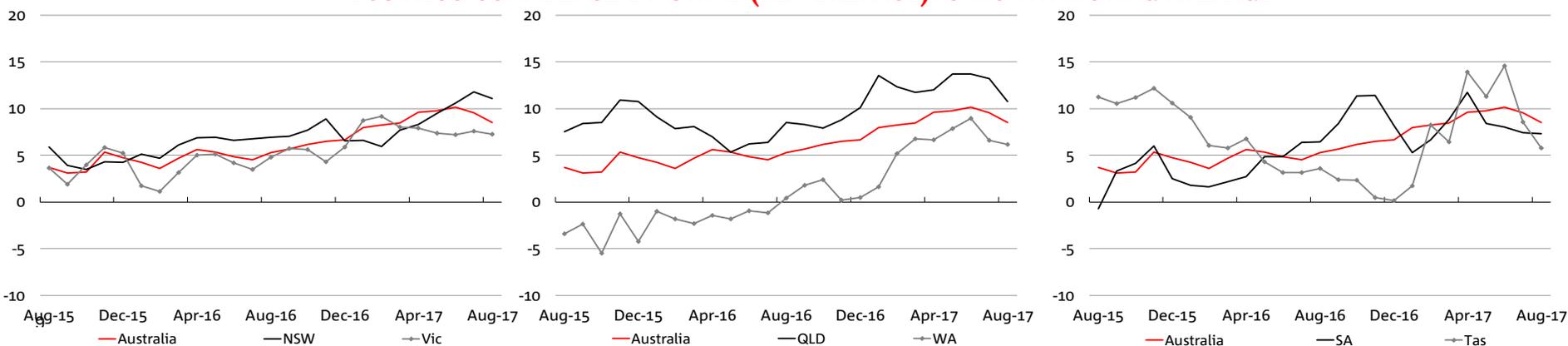
Most states are looking strong, but WA has begun to turn down again

- Of the mainland states, the rise in **business conditions** was driven by Victoria (up 10) and South Australia (up 14), but were largely offset by falls in NSW (down 10), Queensland (down 4) and WA (down 1). WA remains the only state in negative territory, while all other states remain quite solid. Abstracting from monthly volatility, Victoria and SA have moved into the top spot for the mainland states, with trend conditions sitting at +18 index points. The other states are following close behind however, with NSW at +17 and Qld on +14 index points. While being well up from its previous trough, WA is underperforming (at -1) and appears to be trending lower again. Tasmania continues to report the highest level of conditions.
- Business confidence** is positive in all states, even though most saw a marked deterioration in August. Of the mainland states, confidence is highest in trend terms for NSW and Qld (+11), but lowest in WA at +6 index points (trend).
- Employment conditions** (trend) are positive in all states. Consistent with trends in business conditions, the employment index is currently lowest in WA at just +3 index points – albeit still a notable improvement from the extremely negative levels seen in late 2016. Queensland continues to see the highest level of employment conditions, despite easing in the month (to +10), while NSW, Victoria and SA are all sitting around similar levels (+7-9).

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



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



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