

NAB MONTHLY BUSINESS SURVEY

OCTOBER 2017

NEXT RELEASE:
12 DEC 2017 – NOVEMBER MONTHLY



Key points:

- **Business conditions hit an all new high in October, although leading indicators suggest the possibility of some pull-back in coming months. The business conditions index jumped by an impressive 7 points in October, to +21 index points, which is the highest level since the monthly Survey commenced in 1997 (around 4 times the long-run average).** Much of the result stems from a surprise improvement in manufacturing conditions, while conditions in personal services improved sharply as well. Meanwhile, retail remained very weak in October, but conditions were no longer negative. **By component, gains were completely driven by spikes in trading conditions (sales) and profitability, while employment conditions were unchanged.** Still, the employment index remains at levels that imply solid growth in employment, which should be sufficient to put more downward pressure on the unemployment rate. Reads on inflation from the Survey were on the softer side this month, with retail prices seeing only modest growth. Labour cost inflation dropped back sharply, while final price inflation was steady at subdued levels.
- **The business confidence index was unchanged in October at +8 index points, which is marginally above the long-run average.** The large divergence between business conditions and confidence remains a bit of a puzzle, although in our quarterly Survey (published last month), firms with worsening confidence pointed to margin pressures, an uncertain outlook and costs as the cause – the latter consistent with relatively more restrained employment conditions. Concerns about the outlook could also have negative implications for hiring and investment intentions, although reads on capex have been quite solid in the Survey. However, capacity utilisation rates eased a little in the quarter. **Forward orders, which appear to be giving a more accurate read on the strength of the non-mining economy, eased back this month** while the solid AUD still appears to be weighing on export conditions (despite the AUD depreciating a little in the month).
- Despite the very strong outcome for business conditions in October, more benign reads elsewhere in the Survey suggests a degree of caution should be exercised. The improvement in retail conditions was a welcome result, but not enough to dissuade our concerns around the household consumption outlook. Additionally, employment conditions are not at the same lofty levels as the other components of business conditions, but they have been solid and we expect to see further improvement in the labour market going into 2018. The outlook for business investment has also improved modestly, and overall we still think the RBA will be in a position to commence a shift away from emergency stimulus settings by H2 2018 (NAB expect 25bp hikes in August and November 2018). That said, potential hurdles from underemployment, an elevated AUD, household debt and peaks in LNG exports and housing construction will ensure that the RBA proceeds with caution. **More details on our economic forecasts will be released tomorrow.**

Table 1: Key monthly business statistics

	Aug 2017	Sep 2017	Oct 2017		Aug 2017	Sep 2017	Oct 2017
	<i>Net balance</i>				<i>Net balance</i>		
Business confidence	6	8	8	Employment	10	7	7
Business conditions	15	14	21	Forward orders	4	4	2
Trading	19	19	30	Stocks	0	4	2
Profitability	16	17	26	Exports	0	-1	-1
	<i>% change at quarterly rate</i>				<i>% change at quarterly rate</i>		
Labour costs	1.2	1.0	0.7	Retail prices	-0.1	0.3	0.1
Purchase costs	0.6	0.4	0.5		<i>Per cent</i>		
Final products prices	0.4	0.4	0.4	Capacity utilisation rate	81.6	81.9	81.7

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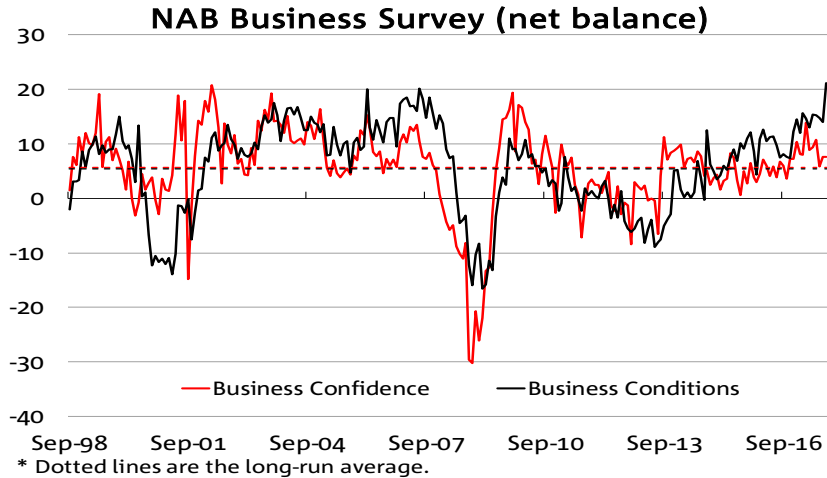
CONTENTS

Key points	1
Key charts	2
Conditions, confidence & leading indicators	3
Labour demand & costs	5
Prices & borrowing	6
More details	7
Industry results	8
State results	9

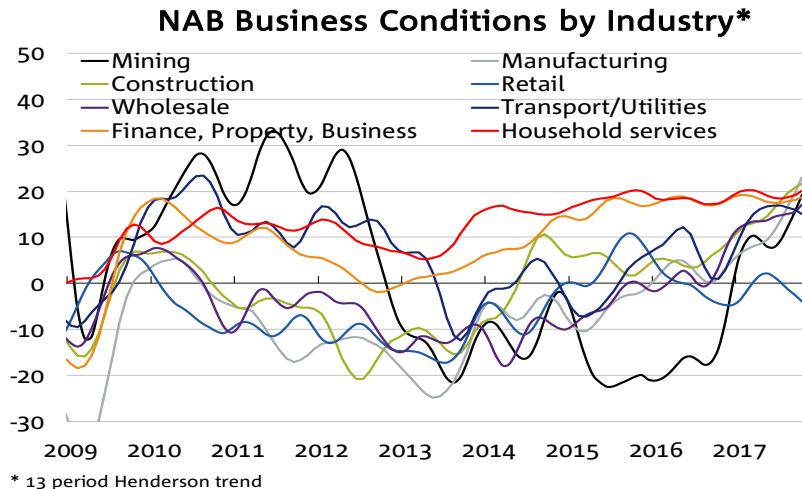
* All data seasonally adjusted and subject to revision. Cost and prices data are monthly percentage changes expressed at a quarterly rate. Fieldwork for this survey was conducted from 25 October to 31 October, covering almost 410 firms across the non-farm business sector.

KEY MONTHLY CHARTS

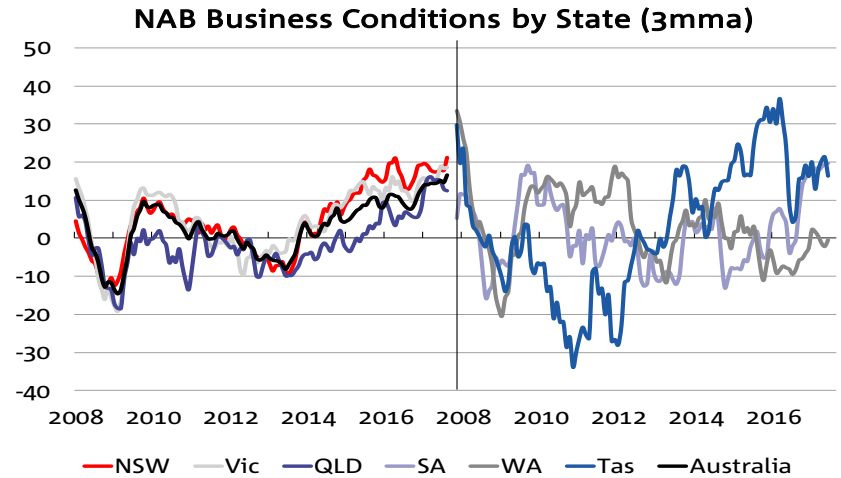
BUSINESS CONDITIONS JUMP TO A RECORD HIGH. CONFIDENCE NOT AS LOFTY, BUT HOLDING STEADY



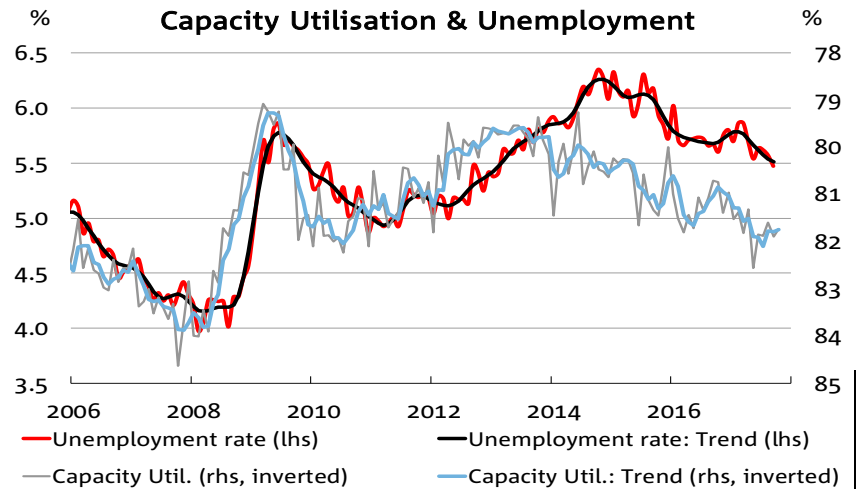
MOST INDUSTRIES LOOKING SOLID. RETAIL IMPROVED THIS MONTH, BUT THE TREND IS STILL DOWN



CONDITIONS HOLDING-UP IN MOST STATES, BUT WA STILL TRAILING BEHIND



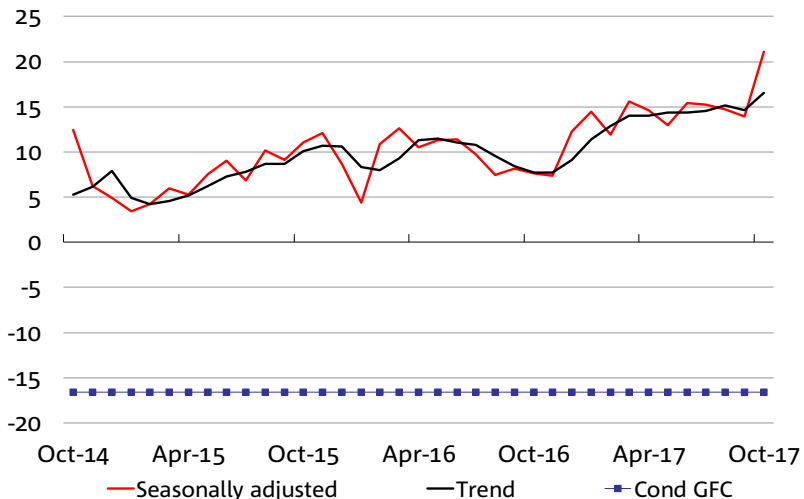
CAPACITY UTILISATION SHOWS LIMITED SLACK – CONSISTENT WITH THE DROP IN THE UNEMPLOYMENT RATE



BUSINESS CONDITIONS AND FORWARD INDICATORS

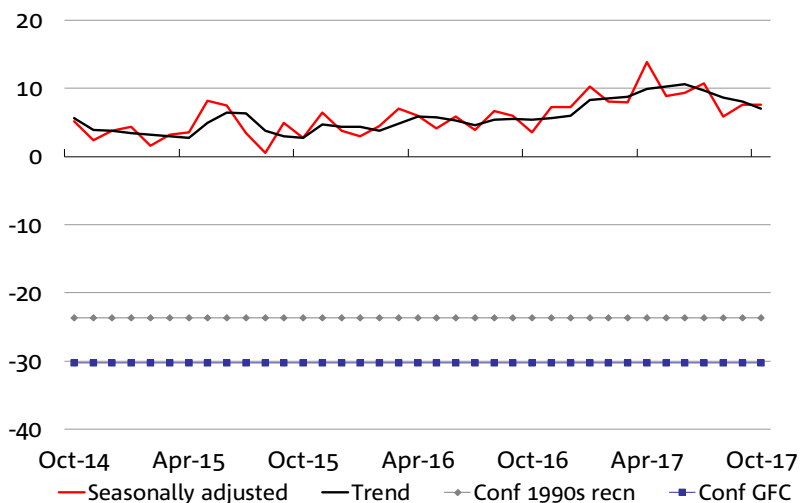
Conditions jump to a record high. Confidence is holding steady at less lofty levels.

Business Conditions (net balance)

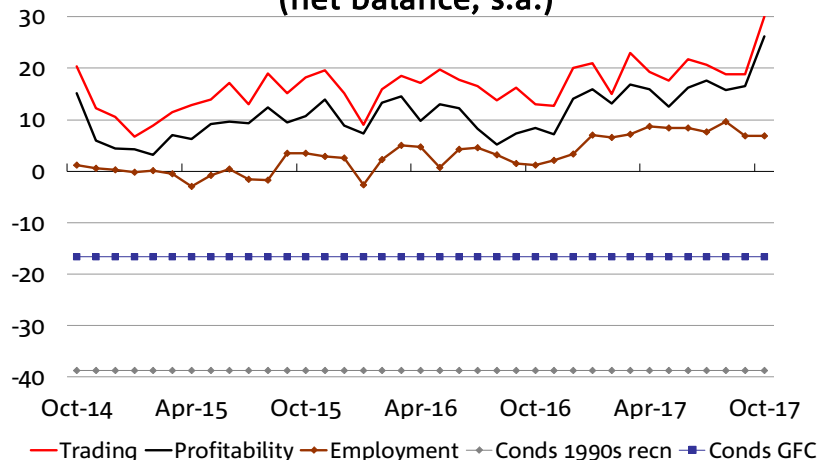


- **Business conditions** jumped sharply in October, with the business conditions index rising 7 points to +21 index points – a record high for the monthly survey, and around four times the long-run average (+5). In terms of the components, the improvement was driven by big increases in trading conditions (sales) and profitability, which actually suggests a fairly solid demand environment. Meanwhile, employment conditions were steady at less lofty (but still solid) levels. In trend terms, business conditions are well into positive territory for all industries except retail (more detail on p8).
- **Business confidence** is not as lofty as conditions, but are still holding up at reasonably solid levels. The index was unchanged at +8 index points in October, which is modestly above the long-run average for the series – although the trend has been heading down again in recent months. While it is difficult to gauge what is driving confidence, responses from firms in the recent Q3 NAB Business Survey suggest a combination of margin pressures and an uncertain outlook are holding confidence back. Confidence levels are currently positive for all industries (see p8 for industry details).
- **By state** there was an improvement in **business conditions** across all states except South Australia in October, while no states recorded a negative index – although WA remains much more subdued than other states. In trend terms, NSW regained its top position, with trend conditions at +21, although SA and Vic are close behind. **Business confidence** was positive in all states, and SA was particularly solid in October (despite being the only state to report lower business conditions). Of the mainland states, confidence is highest in trend terms for Qld (+11), but lowest in Vic at +5 index points (see p9 for state details).

Business Confidence (net balance)



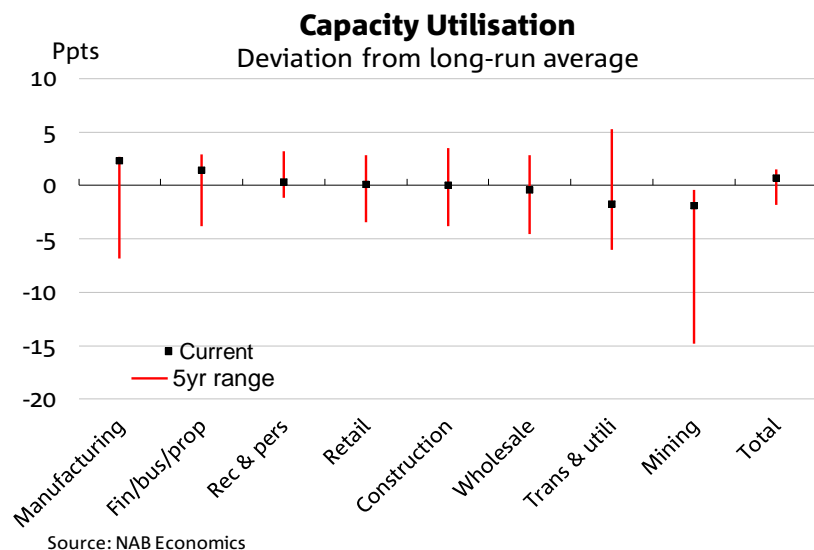
All components of business conditions (net balance, s.a.)



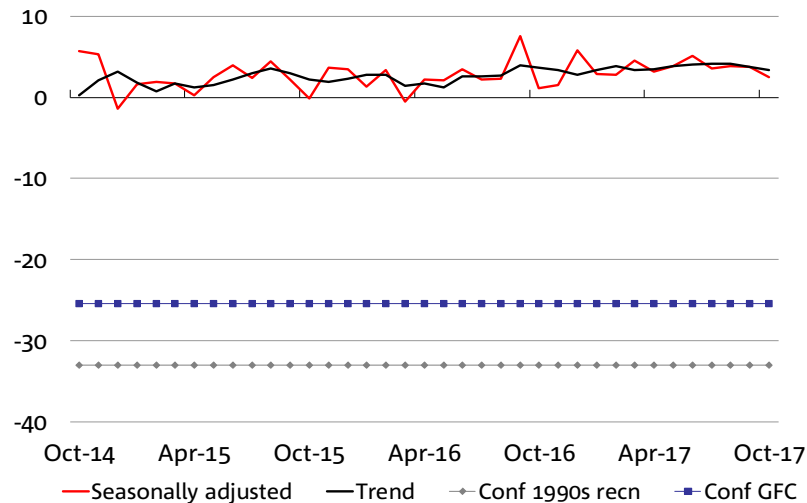
BUSINESS CONDITIONS AND FORWARD INDICATORS (CONT.)

Components of business conditions & leading indicators

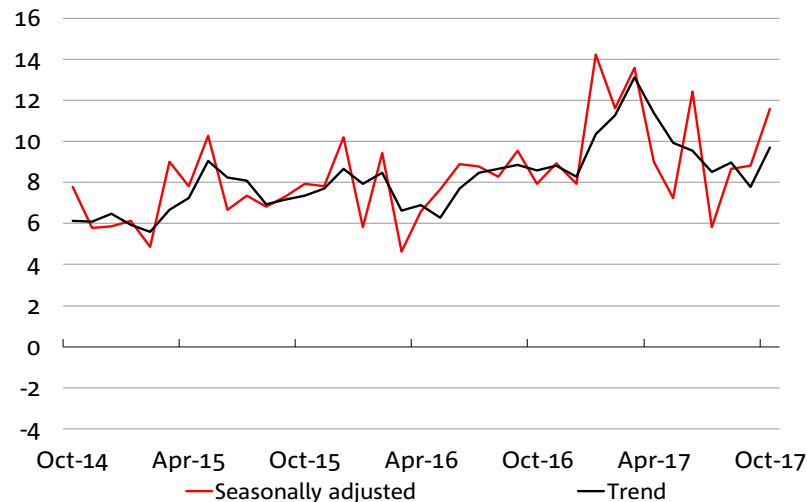
- Forward orders, eased back a little further in October, which could suggest some loss in momentum for non-mining demand – orders have had a close relationship with non-mining demand of late. The index was down 2 points, to +2 index points, although that is still a little better than the long-run average (zero). Most industries saw a decline in orders during the month, although the deterioration was particularly large in mining (down 29, following a spike in the previous month). In contrast, retail was the only industry to see an pick up in orders (up 5), which is consistent with the improvement in retail conditions and confidence, although the orders index for retail did remain in negative territory (-7 in trend terms). Orders were still highest in construction (+15, in trend terms), reflecting strong residential building activity and improvements in the non-residential sector.
- NAB's measure of **capacity utilisation** was a little lower in October (down 0.2ppts to 81.7%), although the long term trend remained solid. The transport & utilities industry and mining both reported much higher than normal levels of spare capacity (see industry detail on p8). In contrast, manufacturing and major services industries had much more limited spare capacity than normal, which may trigger addition investment or labour hiring in those industries. The Survey's **capex** measure strengthened in October, up 3 points to +12 index points, suggesting good levels of investment activity.
- Cash flow** (not seasonally adjusted) jumped sharply from already elevated levels (chart on p7). It is currently strongest in wholesale (3mma), but weakest in retail.



Forward Orders (net balance)

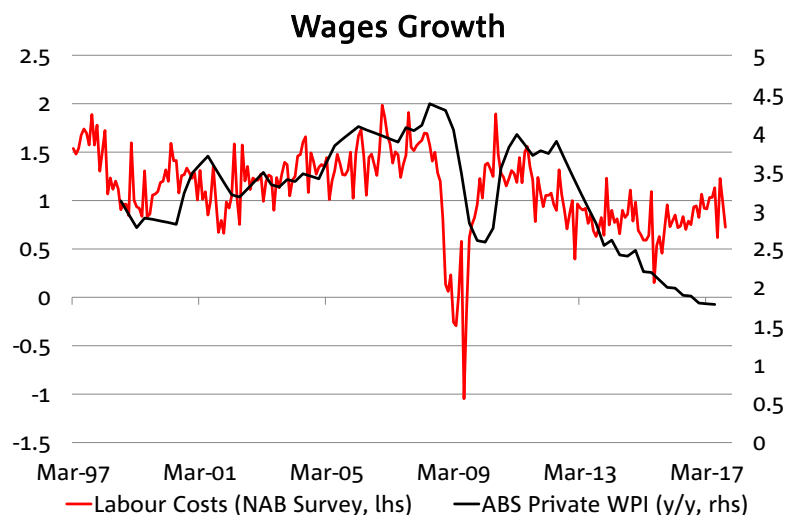
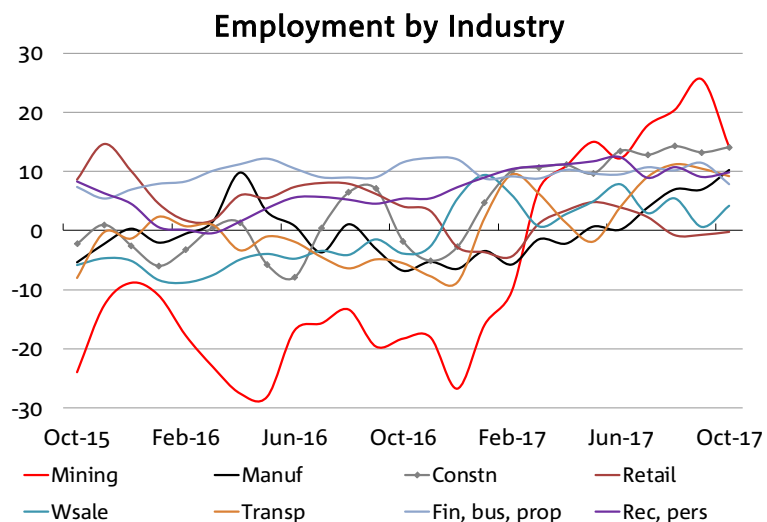
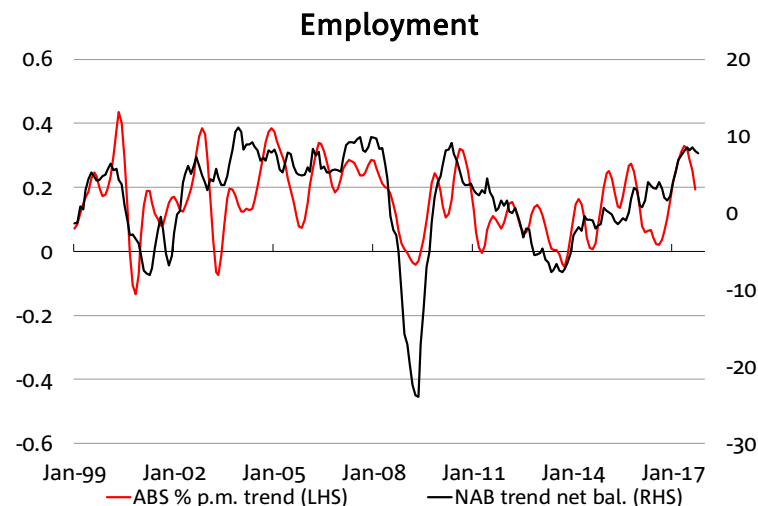


Capital Expenditure (net balance)



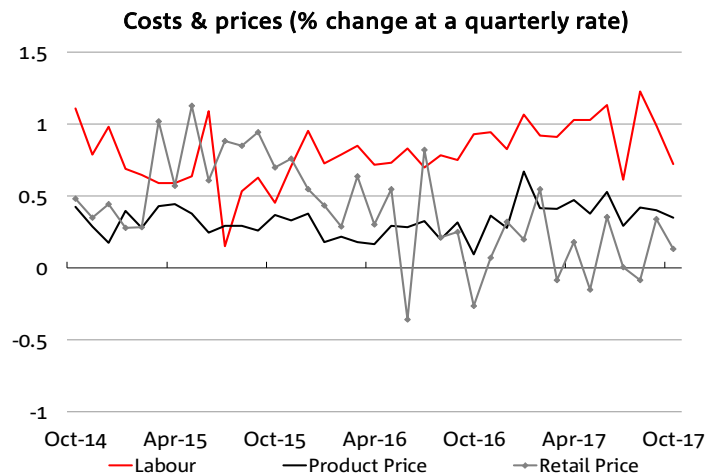
LABOUR DEMAND AND COSTS

- **Employment conditions** were steady in October, staying at reasonably solid levels and keeping in line with indications from other data sources, which show that the labour market has continued to tighten. Monthly employment growth slowed down in September according to the ABS labour force survey, but the pace of job creation has remained more than sufficient to put downward pressure on the unemployment rate. Job vacancies have also been rising steadily, which along with solid employment conditions in the NAB Survey, suggest the labour market should continue to strengthen in the near-term. The employment index remained at +7 index points, which is well above the long-run average for the series. This outcome points to an annual job creation rate of around 240k (around 20k per month) in coming months, which is sufficient to see the unemployment rate push lower (all else unchanged) – trend ABS employment growth was 23.8k in September.
- By industry, there was a particularly large deterioration in employment conditions for mining, falling 29 index points. Finance/ property/ business services, personal services and construction had more moderate falls (down 8, 3 and 1 point respectively). The largest improvement was in manufacturing (up 13) and transport (up 10). Looking through the monthly volatility, mining still has the best employment conditions, along with construction (at +14 index points for both) – labour demand from mining has improved considerably in the survey since the start of this year, but recent falls could suggest it is a temporary boost as major mining investments (namely in LNG) are completed. Retail still has very soft employment conditions, but the trend is no longer negative.
- **Labour costs** growth (a wage bill measure) pulled-back further in October, to 0.7% (a quarterly rate, previously 1%). Labour cost inflation has been relatively subdued, but trending higher, and suggests higher wage inflation than the ABS WPI (although that could partly reflect strong employment growth). Wage pressures are strongest in wholesale (at 1.3%), but softest in retail (0.3%).



OTHER COSTS, PRICES & BORROWING CONDITIONS

- In contrast, growth in **purchase costs** rose modestly in the month, to 0.5% (a quarterly rate, previously 0.4%), although this still suggests relatively subdued upstream cost pressures. Growth in purchase costs accelerated the most in transport (up 0.6 ppts), while retail decelerated the most (down 0.3 ppts). Overall, purchase cost pressures were strongest in transport & utilities (at 0.8%, quarterly rate), and weakest in retail (0.1%).
- Final product prices** growth has consistently failed to keep up with input costs, and October was no different. Final price inflation was steady at 0.4% (a quarterly rate) this month, which is modestly below purchase cost inflation and still well below labour cost inflation (despite it easing during the month). Retail price inflation remains especially subdued, although it managed to remain in slightly positive territory at 0.1% (down from 0.3%), which might indicate another soft CPI for Q4 to date. Prices are rising the most in mining, while construction prices recorded the only decline.
- Borrowing conditions** remained negative in October, although the index has improved considerably of late. Despite that, the demand for credit appears to have softened from 3 months ago. The borrowing index has been negative since early 2016, meaning that on balance, more firms found it more difficult to borrow than easier.

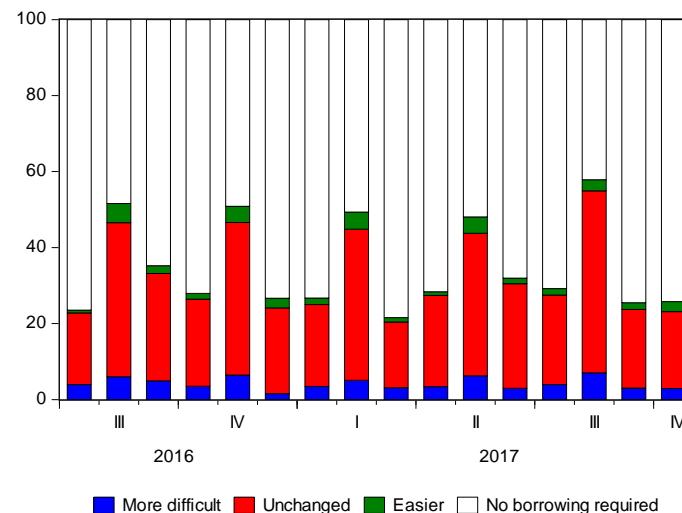


Based on respondent estimates of changes in labour costs and product prices. Retail prices are based on retail sector product price estimates.

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

Oct-2017	Mining	Manuf	Constn	Retail	Wsale	Trans&utils	Rec.&pers.	Fin,prop.&b us.	Australia
Labour costs: current	1.0	1.1	0.6	0.3	1.3	0.8	0.6	0.6	0.7
Labour costs: previous	2.8	1.3	1.4	0.0	1.1	0.4	0.9	1.1	1.0
Labour costs: change	-1.8	-0.2	-0.8	0.3	0.2	0.4	-0.3	-0.5	-0.3
Prices (final): current	2.1	0.9	-0.6	0.1	0.9	0.3	0.2	0.3	0.4
Prices (final): previous	-0.1	0.4	0.8	0.3	1.1	0.4	0.5	0.2	0.4
Prices (final): change	2.2	0.5	-1.4	-0.2	-0.2	-0.1	-0.3	0.1	0.0
Purchase costs: current	0.3	0.5	0.4	0.1	0.6	0.8	0.5	0.6	0.5
Purchase costs: previous	0.3	0.2	0.5	0.4	0.7	0.2	0.6	0.3	0.4
Purchase costs: change	0.0	0.3	-0.1	-0.3	-0.1	0.6	-0.1	0.3	0.1

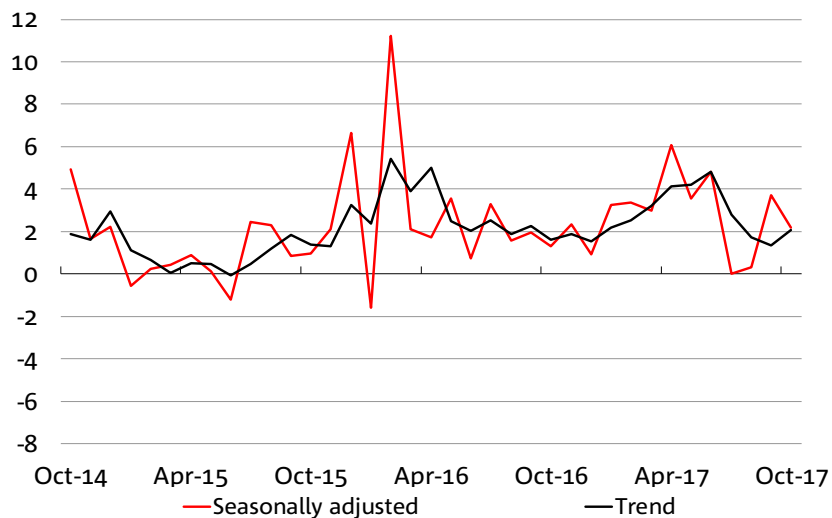
Borrowing conditions (% of firms)



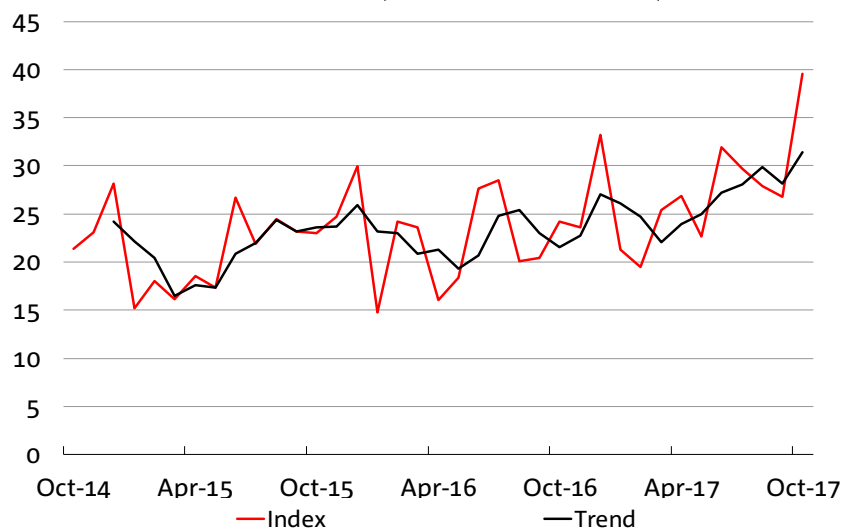
MORE DETAILS ON BUSINESS ACTIVITY

Export conditions deteriorating. Cash flows rebounded.

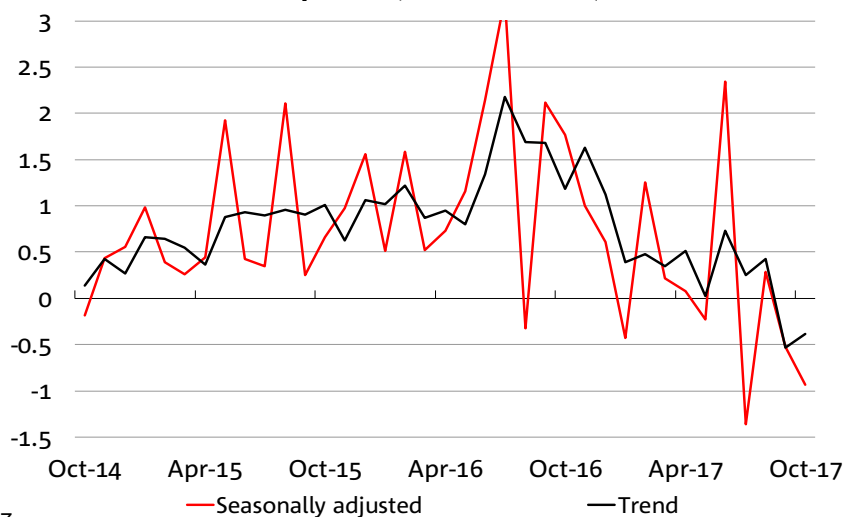
Stocks (net balance)



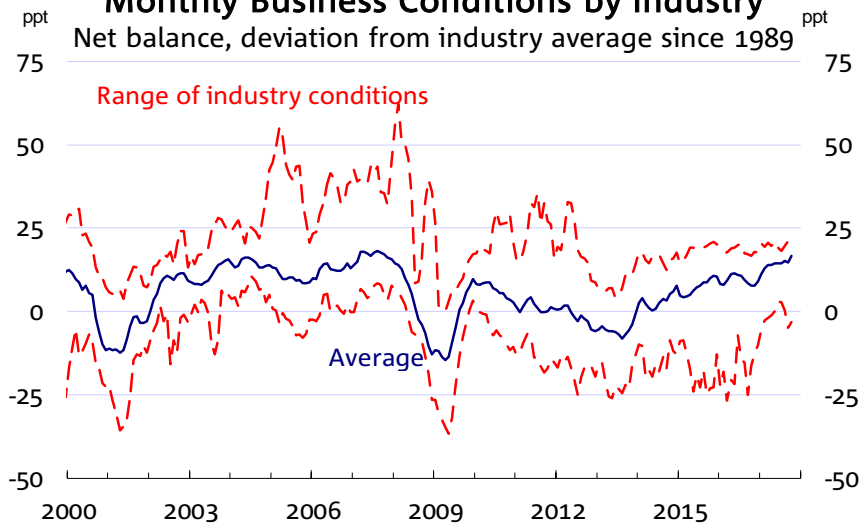
Cash Flows (net balance, nsa)



Exports (net balance)



Monthly Business Conditions by Industry



Source: NAB

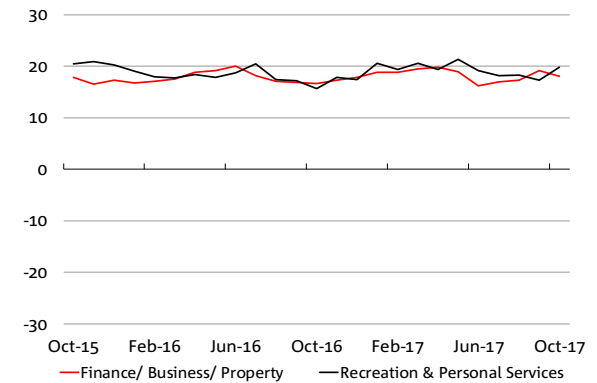
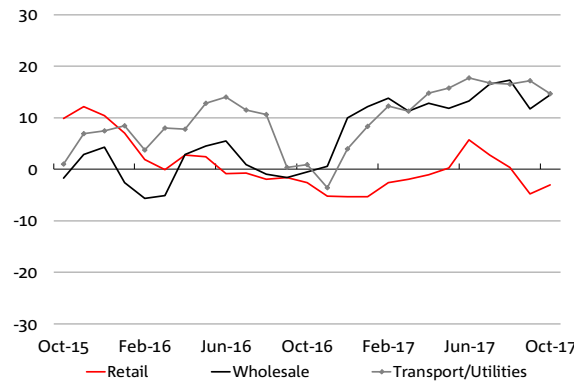
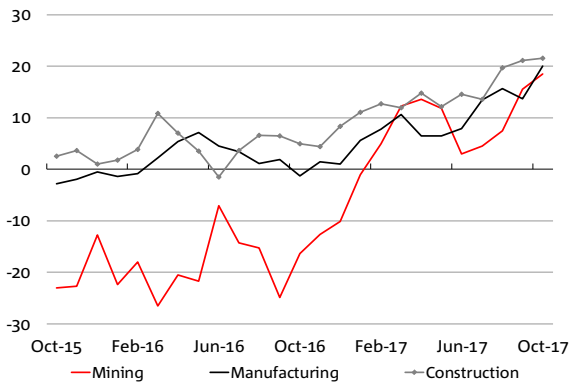


INDUSTRY BUSINESS CONDITIONS & CONFIDENCE

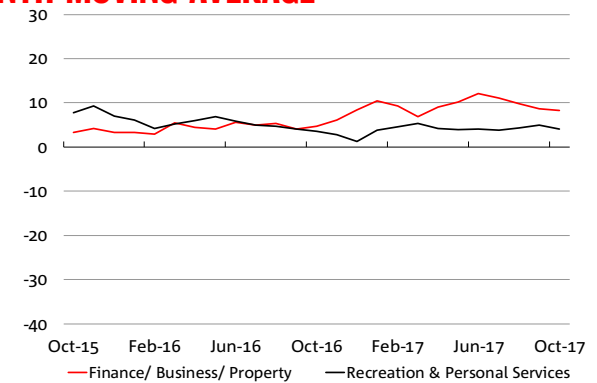
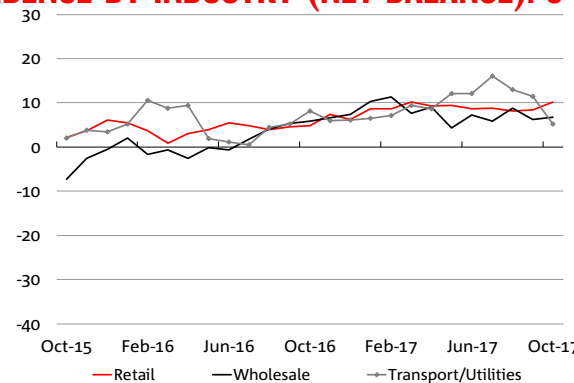
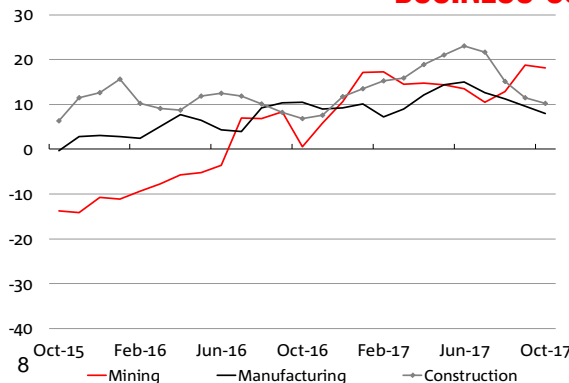
Retail still weak, but showing a slight improvement

- The strength in **business conditions** was relatively broad-based across industries. Retail has been the main exception, establishing a clear downward trend in previous months and moving back into negative territory. However, the retail index did improve in the month of October, with the index rising modestly in trend terms as well (lifting to -3, from -5 index points). At the other end of the scale, the construction industry is performing incredibly well (+21 index point, in trend terms), thanks to support from both a large pipeline of residential construction and a likely improvement in non-residential construction activity. Mining has also gone from being a major drag on the index, to one of the best performing industries this year.
- **Business confidence** was fairly solid across all industries in October, although there has been a noticeable downturn in the trend for both construction and transports/utilities – potentially reflecting prospects for higher oil prices and concerns around apartment oversupply and a slowdown in the Sydney housing market. In contrast, retail confidence was surprisingly strong in October, while mining confidence has rebounded this year in trend terms and is now sitting well above the other industries (+18, in trend terms).
- The deterioration in **forward orders** in October was most evident in mining (down 29), followed by transport (down 8). Only retail saw an improvement, but was still negative (-7, in trend terms). Orders are highest in construction (+15, in trend terms). Wholesale **capital expenditure** is highest in trend terms, although all are positive.

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



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

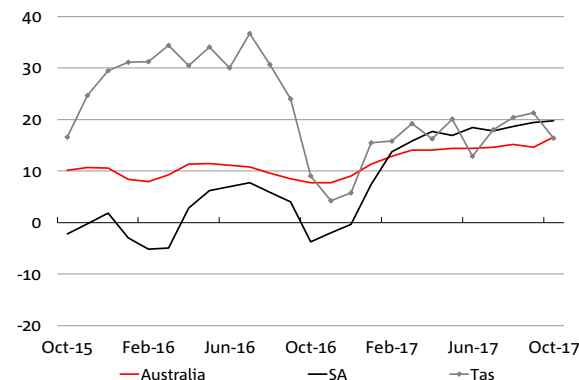
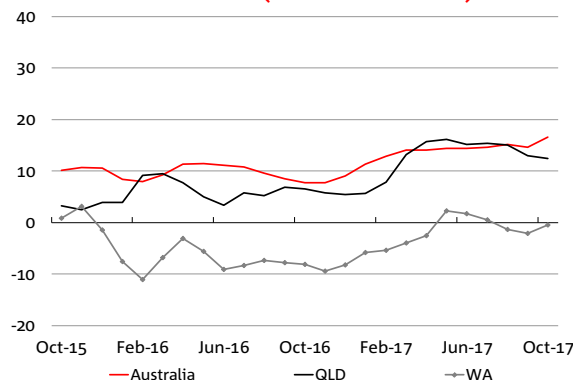
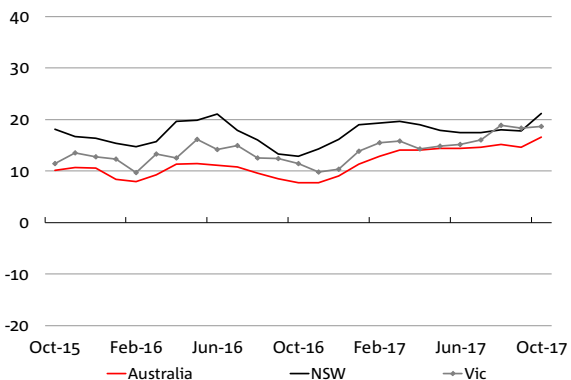


STATE BUSINESS CONDITIONS & CONFIDENCE

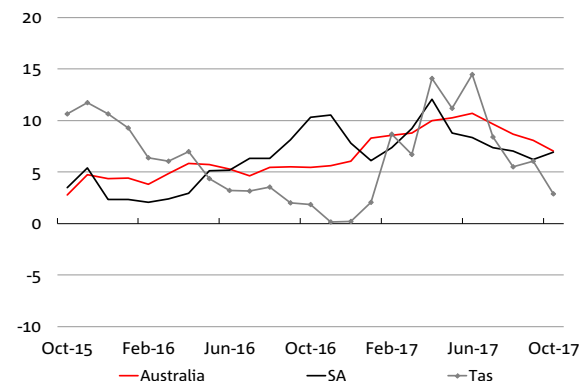
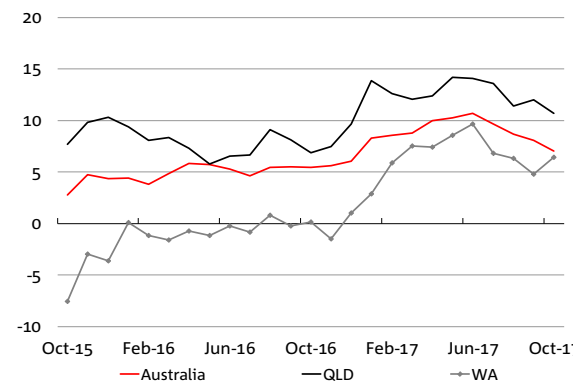
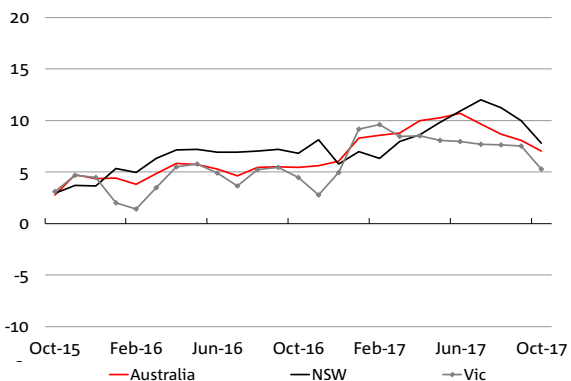
NSW strengthened in October. WA is still lagging behind

- **Business conditions** were higher in all states outside of South Australia in October (down 5). NSW saw the biggest increase (up 14), regaining its top position across the states. Abstracting from monthly volatility, NSW had the strongest mainland conditions at +21 index points (in trend terms), although the other states are following close behind, with SA at +20, Victoria at +19 and Qld on +12 index points. Conditions in WA have improved since last year, but appear to have stabilised at quite subdued levels (currently at 0 in trend terms).
- The change in **business confidence** varied across the states this month, although most are reporting quite solid levels. Only SA and NSW saw an improvement in October (up 6 and 3), while Qld saw the largest deterioration (down 6 points). Nonetheless, the level of confidence is still highest in trend terms for Qld (+11), while Victoria is actually the lowest of the mainland states at +5 index points (trend) – a surprise given some of the broader economic trends.
- **Employment conditions** (trend) are positive in all states outside of WA (currently 0 index points), which has deteriorated sharply in recent months – albeit still a notable improvement from the extremely negative levels seen in late 2016. NSW is seeing the highest level of employment conditions, remaining unchanged in the month (to +12, trend terms), while QLD, Victoria and SA are all sitting around similar levels (+6-7).

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



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



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