EMBARGOED UNTIL: 11:30AM AEDT, 18 OCTOBER 2018

NAB QUARTERLY BUSINESS SURVEY 2018 Q3

CONDITIONS STILL STRONG

NAB Australian Economics

Business confidence and conditions eased in Q3 – though conditions remain well above average; confidence is now below average (but improved slightly late in the quarter). Conditions eased in most industries but generally remain above average. Overall, mining continues to see the most favourable conditions while retail lags. Capacity utilisation and the difficulty in finding suitable labour remained high in the quarter, suggesting that gradually spare capacity is falling. Nonetheless, surveyed price and wage variables suggest at present inflationary pressures remain weak. This quarter we again asked about firms expectations for wage pressures over the next 6 months as well as the likely factors that will drive this wage growth (page 2).

HIGHLIGHTS

- The quarterly NAB Business Survey provides a more in-depth probe into the conditions facing Australian business than the monthly survey, and also examines additional information about how firms perceive the outlook for their industries.
- **Business conditions** (an average of trading conditions/sales, profitability and employment) decreased by 2pts to +13, pulling back further from the highs seen earlier in the year (the monthly survey suggests that conditions have stabilised at a high level late in the quarter). Falling profitability and weaker trading conditions drove the decline, offset by an increase in the employment index. The decline in conditions was broad-based across industries, with the exception of Finance, business and property services, and manufacturing. Overall, mining continues to see the most favourable conditions, while retail continues to deteriorate.
- **Business confidence** fell to +3 (from +7) and is now below average. Confidence fell in all states except South Australia, which rose (and is now highest). Western Australia is second highest and the only other state above average. New South Wales recorded the lowest confidence reading at just +1 in the Q3, and Queensland and Victoria are also below average. Confidence was weaker across most industries in the quarter, with mining declining particularly sharply – that said the mining industry continues to see the highest confidence reading of all industries. The weakest levels of confidence were recorded in wholesale, finance and property services.
- **Leading indicators** were mixed in Q3. Capacity utilisation edged higher and is well above average after trending higher over recent years. The forward orders index fell (which has been volatile on a monthly basis) fell in the quarter, and while it remains around average, the recent softening is of some concern. Somewhat in line with this, expectations for business conditions over the next 3 and 12 months declined in the quarter – though they remain at a high level. Consistent with the rise in capacity utilisation, capex and employment plans for the next 12 months remain elevated.
- **Labour indicators** suggest ongoing strength in the labour market. The employment index rose in the quarter, and while expectations for the next 3 and 12 months declined – they remained above average. Growth in labour costs (a wage bill measure) edged up, but is expected to decline slightly over the next three months. Firms reported a similar level of difficulty in finding suitable labour in the quarter (the index remains at a relatively high level) – which is consistent with further tightening in the labour market.
- Overall, survey **inflation indicators edged up slightly in the quarter** but continue to suggest weak inflationary pressures in the economy. Growth in product prices was unchanged, while retail prices growth edged up (but remains low). Wholesale price inflation was flat in the quarter, but continues to track a little higher than retail prices. Labour costs edged slightly higher but remain weak. The range of both input and final price indicators (labour costs, purchase costs and final products prices) suggest little, if any significant price pressures.
- Looking at the **construction industry** in more detail, conditions declined in the residential and engineering subsectors, while non-residential ticked up and construction services saw a return to positive territory.

TABLE 1: KEY QUARTERLY BUSINESS STATISTICS

	2018q1	2018q2	**2018q3**		2018q1	2018q2	**2018q3**
		Net balance				*Net balance*	
Business confidence	8	7	**3**	Trading	24	22	**15**
Business conditions				Profitability	18	15	**12**
Current	18	15	**13**	Employment	14	9	**11**
Next 3 months	26	24	**21**	Forward orders	9	7	**4**
Next 12 months	33	31	**27**	Stocks	6	8	**7**
Capex plans (next 12)	30	29	**28**	Exports	0	2	**0**
% change							
Labour costs	0.7	0.6	**0.7**	Retail prices (% change)	0.1	0.1	**0.2**
Purchase costs	0.5	0.4	**0.5**				
Final products prices	0.3	0.3	**0.3**	Capacity utilisation rate	82.7	82.8	**83.0**

All data seasonally adjusted, except purchase costs and exports. Fieldwork for this Survey was conducted from 24 August to 13 September 2018, covering over 850 firms across the non-farm business sector.

Next release date is 7 February 2019.

Contacts: Alan Oster – Chief Economist, Gareth Spence – Senior Economist

QUARTERLY FOCUS: WAGE PRESSURE AND ITS DRIVERS

- While the economy has recorded strong growth over the first half of 2018, inflationary pressure appears to have remained fairly meek. With global inflation having remained fairly contained, weaker growth in domestic inflation is a key factor in explaining this weakness. Weaker costs growth (as a result of slow wage growth) is a key reason why domestic inflation has been weaker, and is also important for the outlook around the consumer.
- As the growth in wages and pass through to inflation remains an important economic dynamic at present we continued to ask firms about their expectations for wage pressures over the next 6 months. In addition to asking firms for their expectations, this quarter we also asked firms about the likely drivers of these wage pressures.
- Overall it appears that the results are broadly similar to Q2 though it appears wage pressure has moved to the upside. Around 40% of firms expect current wage pressures to remain unchanged over the next 6 months (down from over 40% in June). The number of firms expecting wage pressures to increase somewhat rose from around 1 in 3 firms to closer to 40%. Around 1 in 5 firms now expect wage pressure to increase moderately. Less than 5% of firms continue to expect a significant increase in wage pressure (though this eased slightly).
- Similar to Q2, very few firms expect wage pressure to decrease over the next 6 months. This is consistent with the outlook for a tightening labour market.
- By industry, the mining sector continues to expect the largest increase wage pressures. This is consistent with other anecdotal evidence of a tightening in the sector. The expected pressures have also picked up since Q2. Firms also report a notable pickup in expected wage pressures in manufacturing, construction and transport.
- In contrast, expected wage pressures have pared back, and are lowest, in the retail sector.
- By state, expected wage pressure rose most in Victoria and New South Wales, an unsurprising result given these labour markets have tightened the most, with unemployment lowest in these eastern states.
- Overall, the bulk of firms, by and large expect wage pressures to increase rather than decrease as reflected in the distribution of responses. This is consistent with a tightening labour market and further falls in the unemployment rate.
- While wage growth has been weak, and there are so far only tentative signs of a pick-up in the wage rises, we expect that as the labour market tightens further, wage growth will eventually begin to lift from current low levels.

CHART 1: DISTRIBUTION OF EXPECTED WAGE PRESSURES (% OF FIRMS)

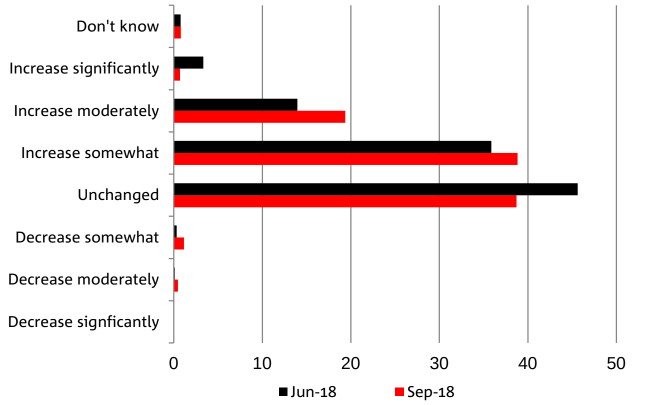


CHART 2: WAGE PRESSURES BY STATE (NET BAL)

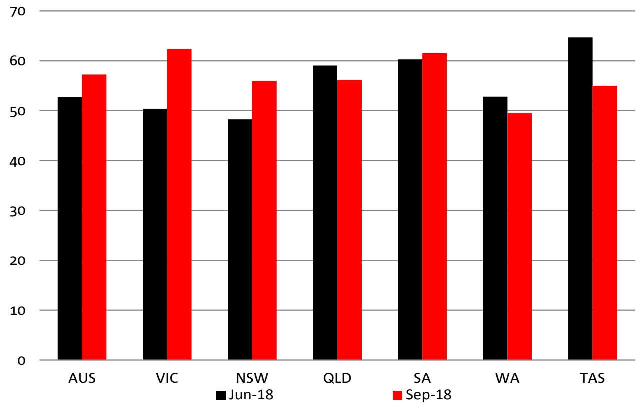
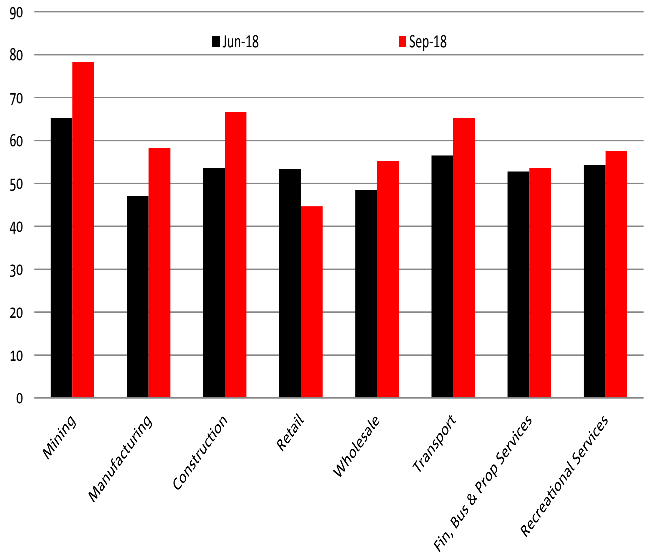


CHART 3: WAGE PRESSURES BY INDUSTRY (NET BAL)



- Firms that expected wage pressure to increase were also asked what factors were likely to drive the increase in wage pressures. Chart 4 shows the proportion of firms identifying each factor as an influence on expected wage pressure (firms may nominate more than one factor).
- In aggregate, the most significant factors that firms report that will drive wage growth revolve around competition for skilled workers and finding suitable labour. Over half of respondents see the difficulty in finding suitable labour as a factor driving increasing wage pressures. The need for more skilled staff also is reported as an important with around 40% of firms identifying this factor as driving expected wage pressure.
- The minimum wage decision and union pressures appear to be less important at present with the exception of a limited number of industries as does wage pressure around bonuses and incentives.
- Table 2 (below) shows the proportion of respondents in each industry identifying each factor as a driver of wage pressure.
- Across industries, mining and construction report the highest proportion of firms affected by skills shortages – that is wages are likely to be pushed up as firms experience a greater difficulty finding suitable labour and seek out more skilled staff.
- The impact of the recent minimum wage decision (increase of 3.5% this year) appears to be most significant in recreational & personal services and the retail sector. This likely reflects the high proportion of employees on the minimum wage in those industries.
- Union pressure appears in those industries more heavily unionised – with over 40% of construction firms and over almost 30% of firms in transport & storage reporting this as an important factor in driving wage pressures.
- Overall, these responses suggest that at present there are some signs of tightening in the labour market – that is, the forces of supply and demand are leading to increased wage pressures – though they appear contained to a small number of industries at present. As the labour market tightens further, it is likely that these factors would become more widespread, and that wage growth should begin to rise as firms compete for a more limited pool of workers.

CHART 4: FACTORS INFLUENCING WAGE PRESSURES (% OF FIRMS)

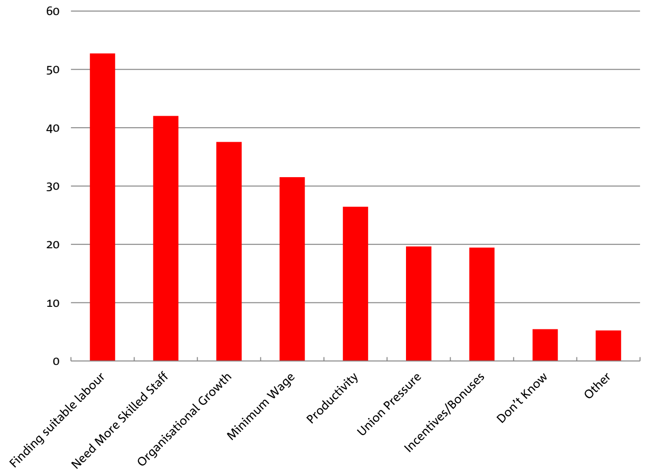


CHART 5: WAGE PRESSURE BY INDUSTRY – FACTORS (% OF FIRMS)

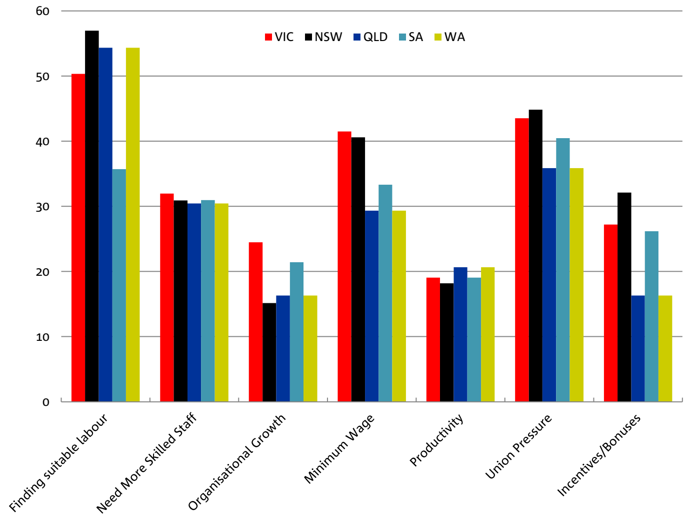


TABLE 2: FACTORS DRIVING UP WAGE PRESSURE BY INDUSTRY (% OF FIRMS)

	Finding suitable labour	Minimum Wage	Union Pressure	Organisational Growth	Incentives/Bonuses	Need More Skilled Staff	Productivity
Mining	67	17	17	39	17	56	39
Manufacturing	48	23	28	26	14	26	28
Construction	62	24	44	42	28	54	34
Retail	56	42	9	36	40	47	31
Wholesale	51	30	14	32	32	46	27
Transport/Storage	53	27	27	43	20	40	13
Finance, Business & Property	56	17	8	42	23	56	25
Recreational & Personal Services	47	50	20	39	7	33	25

NAB QUARTERLY BUSINESS SURVEY – CONDITIONS AND CONFIDENCE

CHART 6: BUSINESS CONDITIONS & CONFIDENCE (NET BALANCE S.A.)

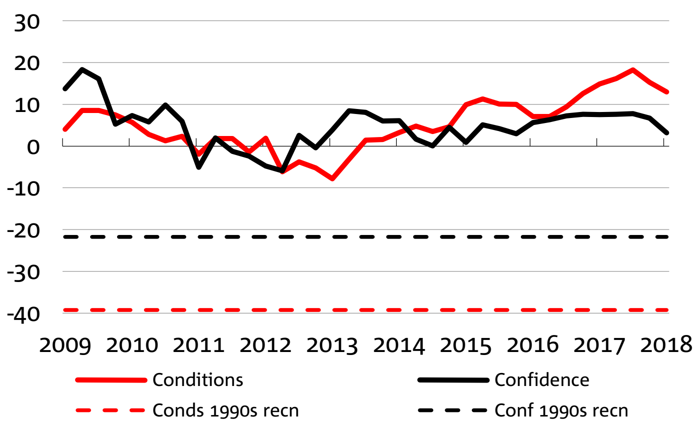
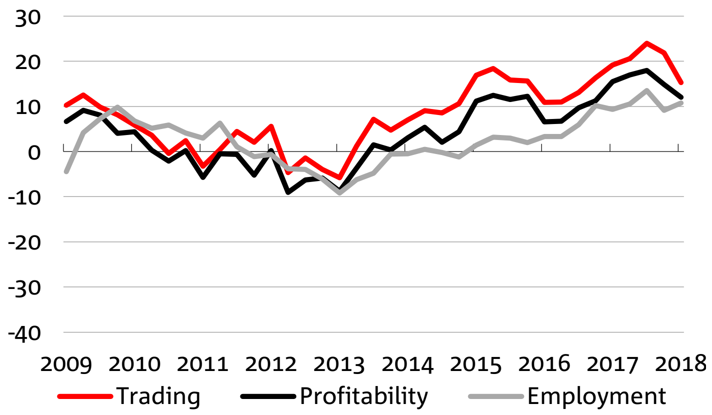


CHART 7: BUSINESS CONDITIONS COMPONENTS (NET BALANCE, S.A.)



DRIVERS OF BUSINESS CONFIDENCE

CHART 8: MOST INFLUENTIAL ISSUES AFFECTING BUSINESS CONFIDENCE

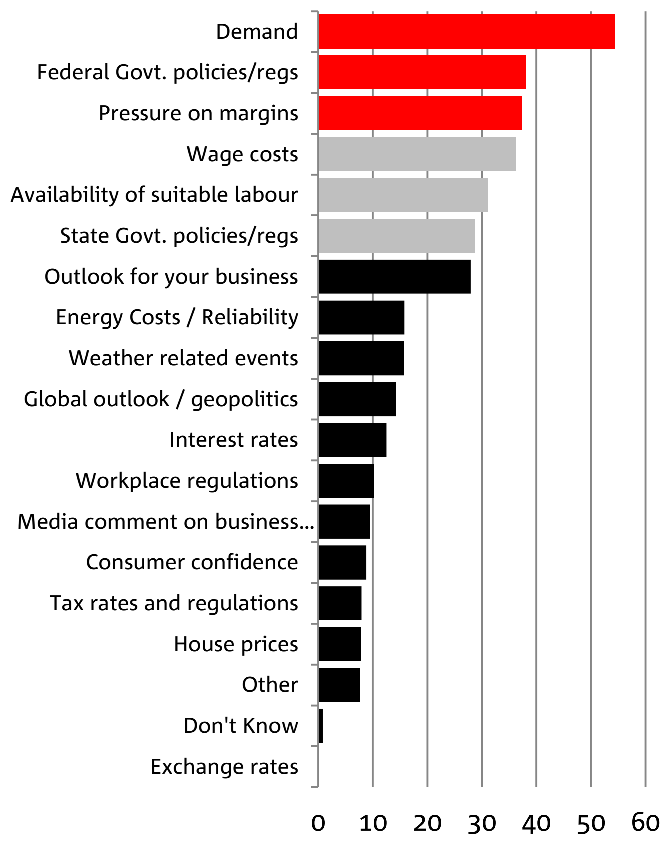


CHART 9: MOST INFLUENTIAL ISSUES AFFECTING BUSINESS CONFIDENCE – DETERIORATING CONDITIONS

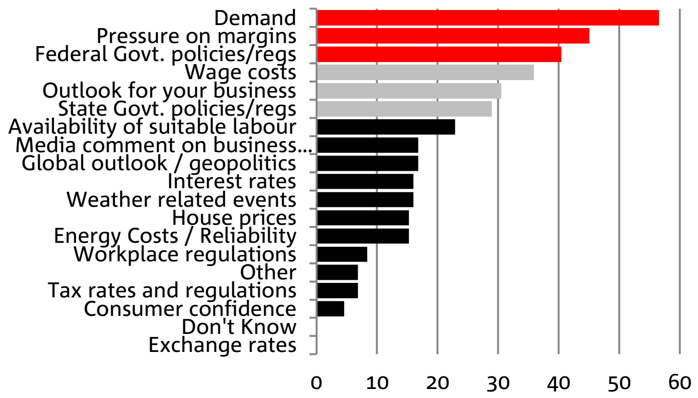
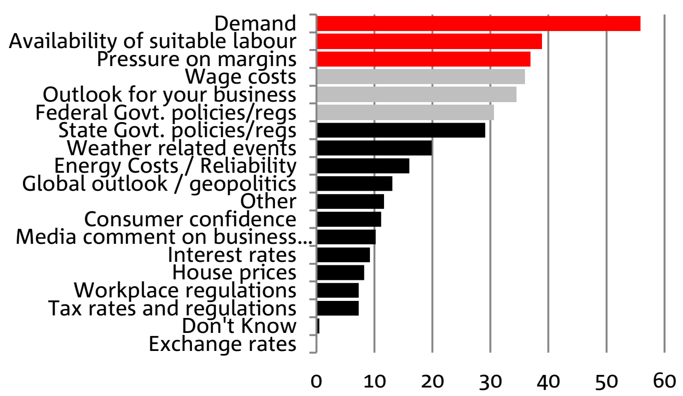


CHART 10: MOST INFLUENTIAL ISSUES AFFECTING BUSINESS CONFIDENCE – IMPROVING CONDITIONS



NAB QUARTERLY BUSINESS SURVEY – LEADING INDICATORS & INVESTMENT

CHART 11: BUSINESS CONDITIONS AND EXPECTATIONS (NET BALANCE)

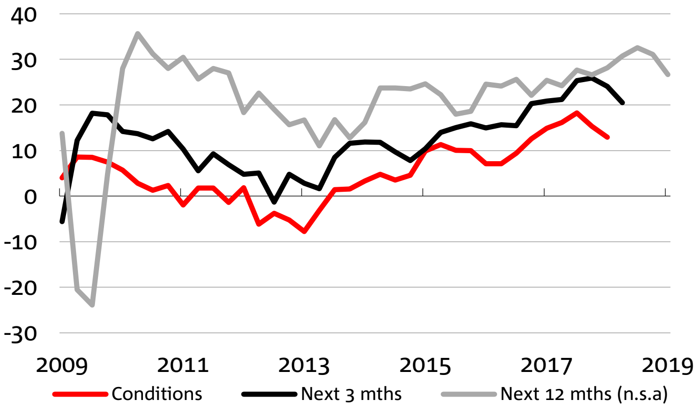


CHART 12: FORWARD ORDERS & EXPECTATIONS (NET BALANCE S.A.)

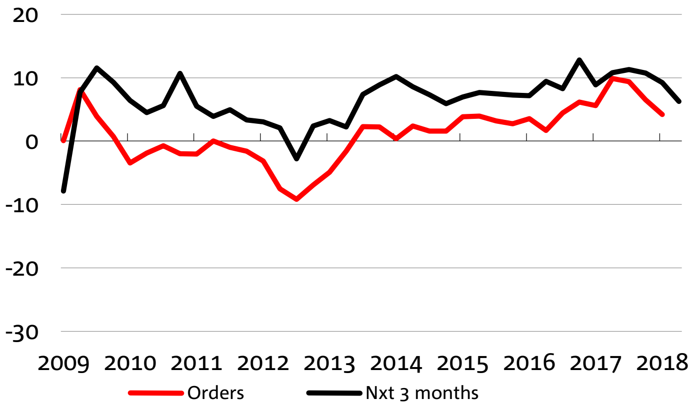


CHART 13: STOCKS (NET BALANCE S.A.)

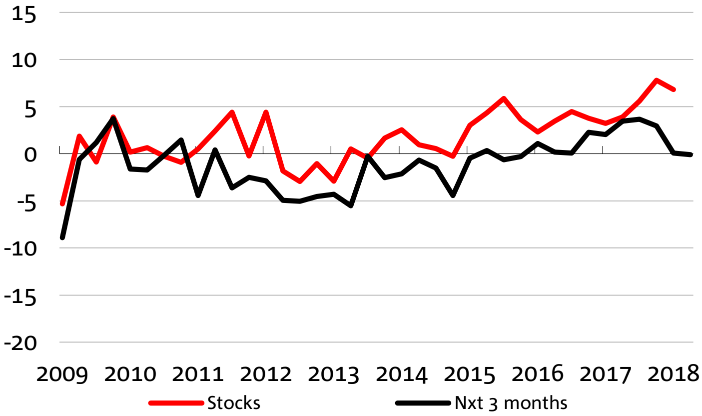


CHART 14: CAPACITY UTILISATION (PER CENT, S.A.)

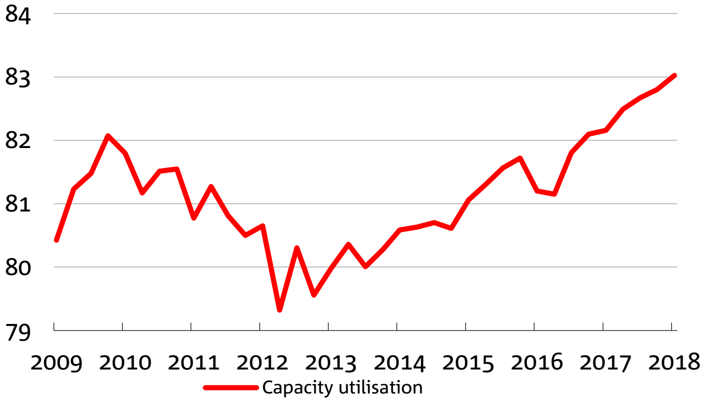


CHART 15: CAPACITY UTILISATION (PPT DEVIATION FROM LONG-RUN AVERAGE, 3 QTR MA)

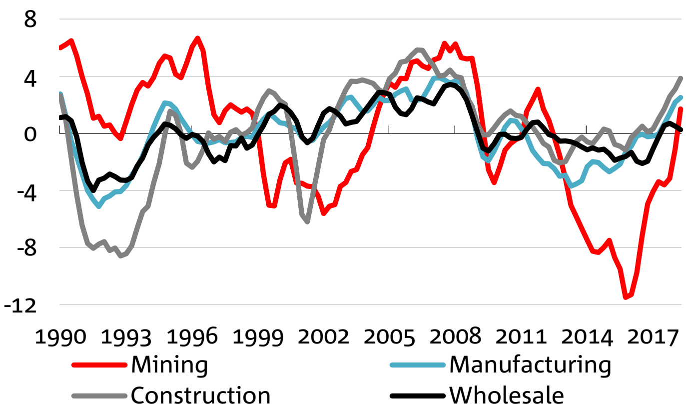
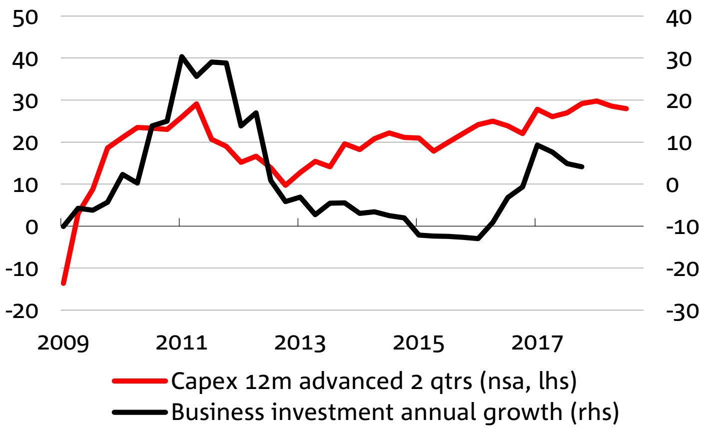


CHART 16: BUSINESS INVESTMENT & CAPEX PLANS



NAB QUARTERLY BUSINESS SURVEY – LABOUR MARKET

CHART 17: EMPLOYMENT & EXPECTATIONS (NET BALANCE)

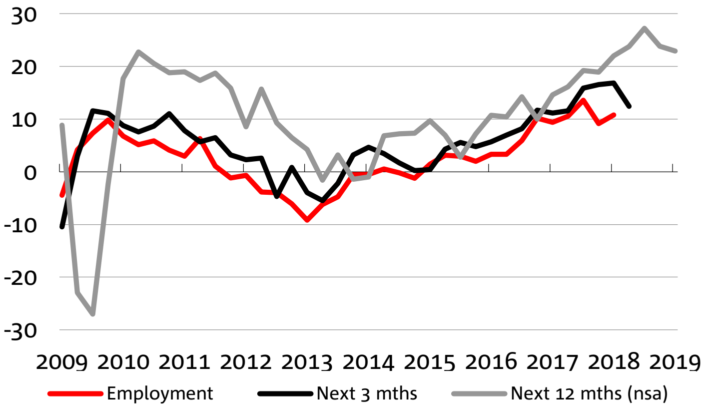


CHART 18: UNEMPLOYMENT RATE & LABOUR CONSTRAINTS

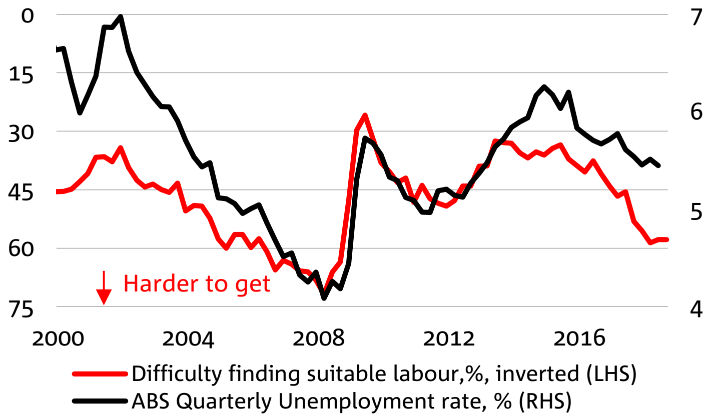


CHART 19: CHANGE IN AVERAGE HOURS WORKED (NSA)

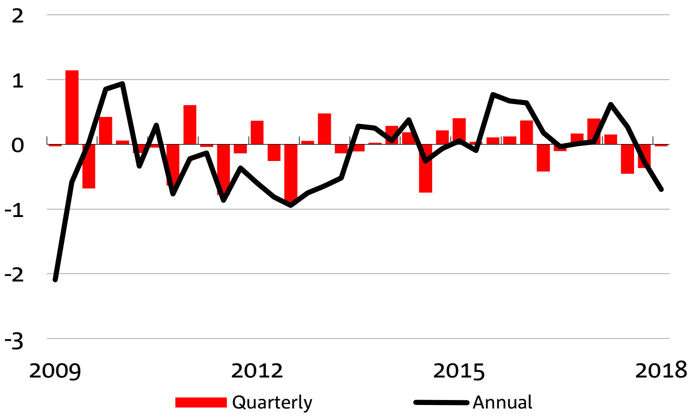


CHART 20: UNDERUTILISATION RATE & LABOUR CONSTRAINTS

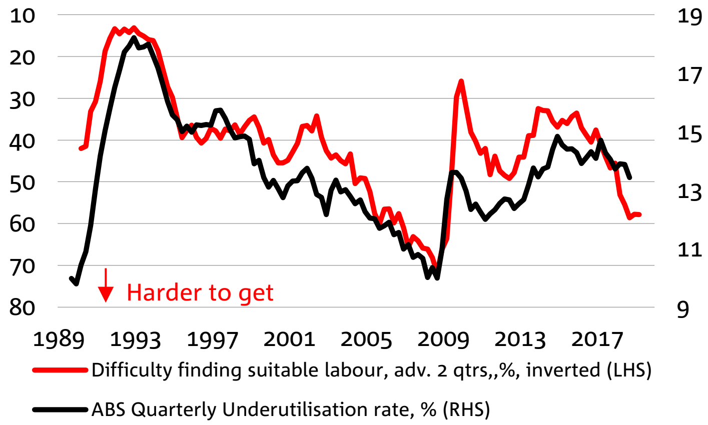


CHART 21: AVERAGE WEEKLY HOURS WORKED BY INDUSTRY (NSA)

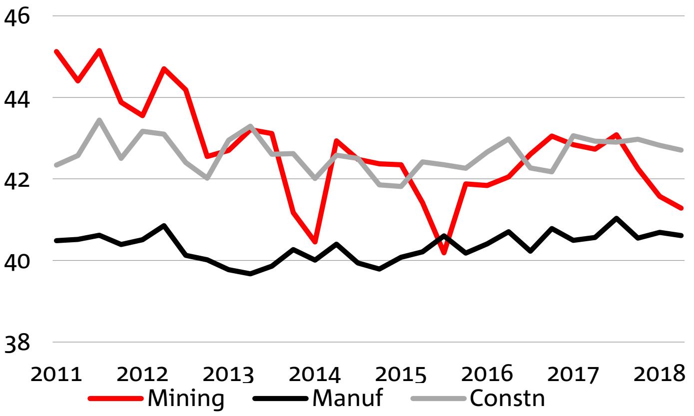


CHART 22: AVERAGE WEEKLY HOURS WORKED BY INDUSTRY (NSA)

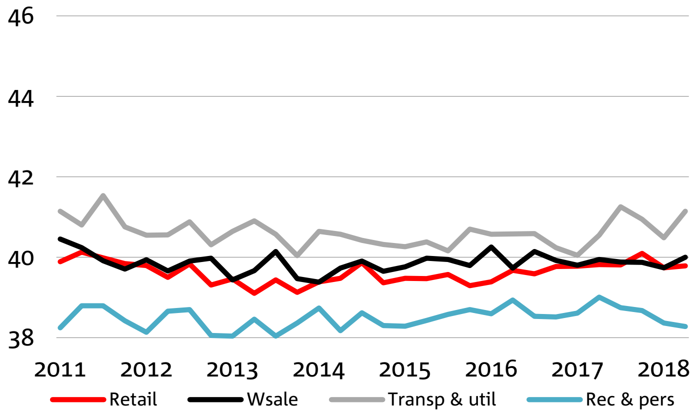
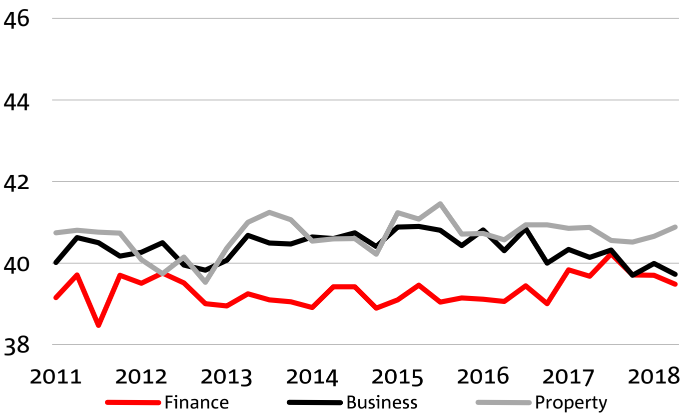


CHART 23: AVERAGE WEEKLY HOURS WORKED BY INDUSTRY (NSA)



NAB QUARTERLY BUSINESS SURVEY - MAJOR CONSTRAINTS ON FIRM OUTPUT

CHART 24: MAIN CONSTRAINTS ON FIRM OUTPUT

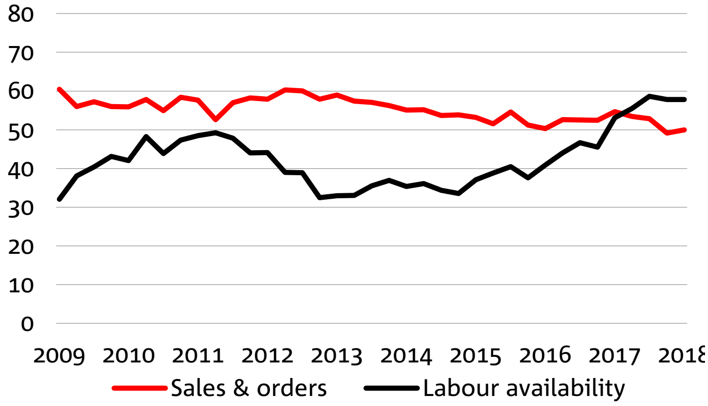
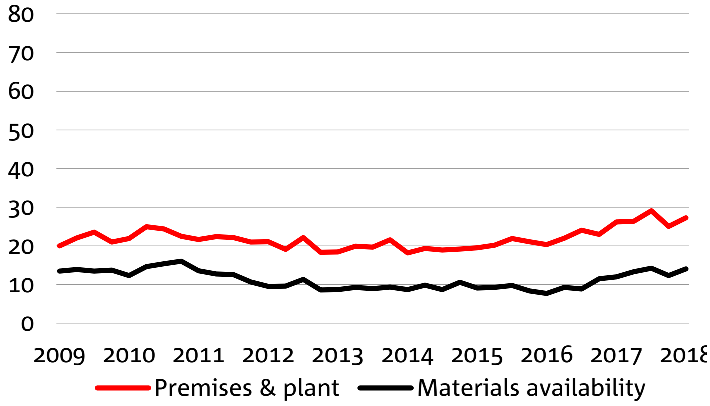


CHART 25: MAIN CONSTRAINTS ON FIRM OUTPUT



INFLATION PRESSURES

CHART 26: PRICES (% ANN, SA)

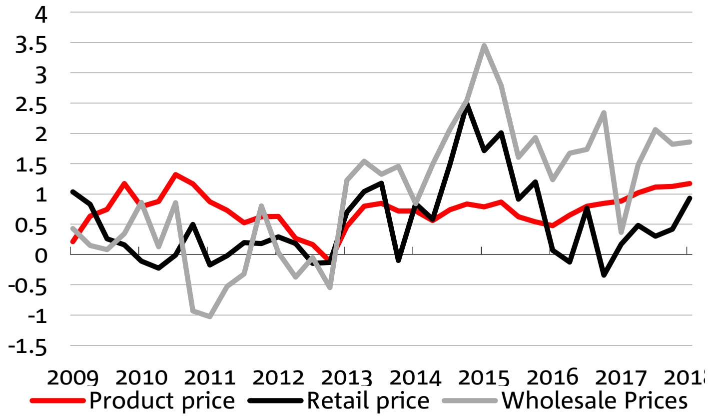
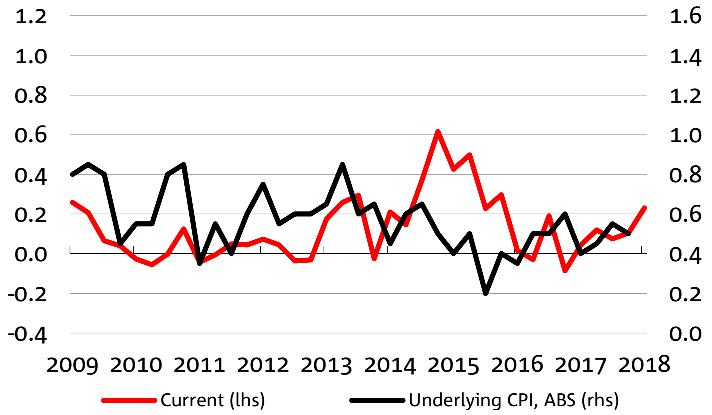


CHART 27: RETAIL PRICES (% P.Q.)



LABOUR COSTS (DETAILS)

CHART 28: LABOUR COSTS & COMPENSATION OF EMPLOYEES

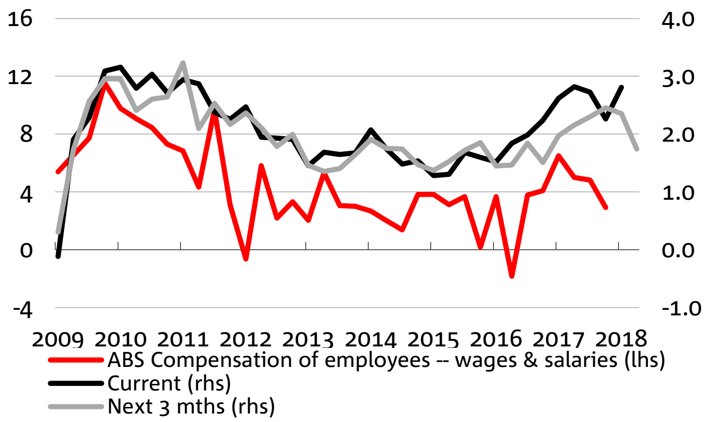
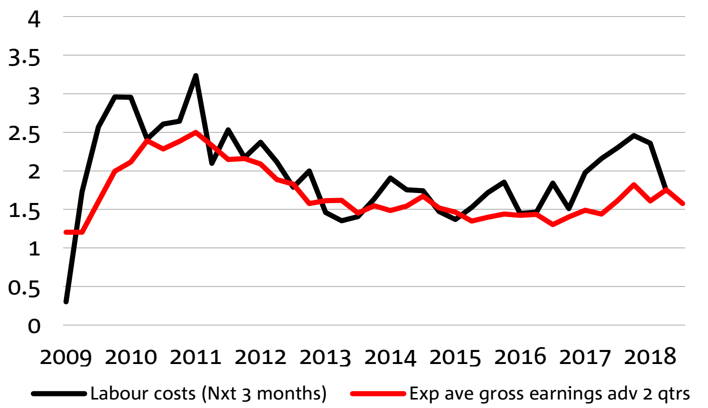


CHART 29: EXPECTED LABOUR COSTS (% ANN)



NAB QUARTERLY BUSINESS SURVEY – CONSTRUCTION INDUSTRY DETAILS

CHART 30: BUSINESS CONDITIONS BY INDUSTRY

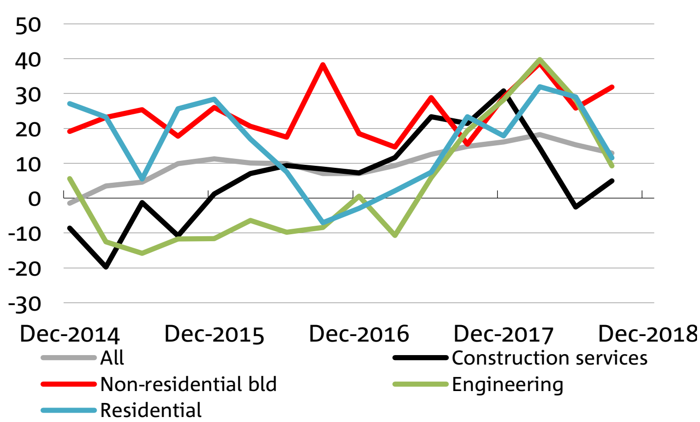


CHART 31: BUSINESS CONFIDENCE BY INDUSTRY

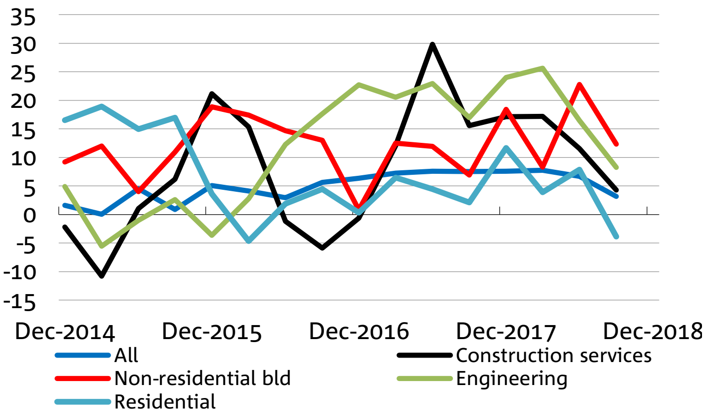


CHART 32: EMPLOYMENT CONDITIONS BY INDUSTRY

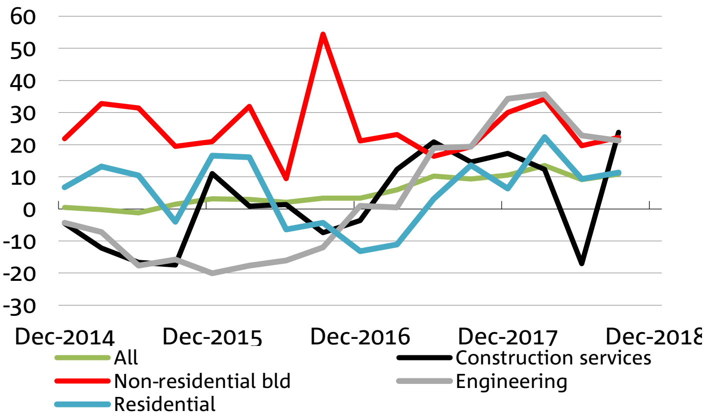
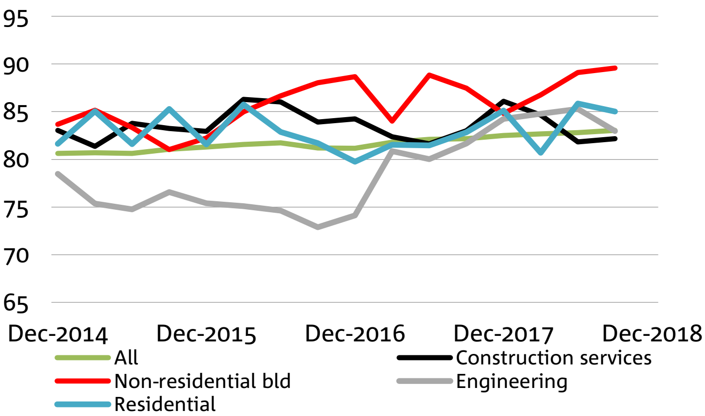


CHART 33: CAPACITY UTILISATION BY INDUSTRY



FINANCIAL MARKET EXPECTATIONS

- On average, businesses are pricing in around a 90% probability of a 25bp rate hike in the next 12-months (up from around 70% in Q2). NAB Economics' view is that the RBA will likely begin a gradual series of rate rises in mid-to-late 2019 but that this is highly data dependent. The RBA will want clear evidence that wages growth has lifted from current low rates and that this is feeding through to domestic inflation pressures before beginning the rates normalisation process. However, both their and our view is that the pick-up in wages growth will only be gradual with inflationary pressures best described as meek at present.
- Exchange rate expectations in the Survey (6-months-ahead) fell to around US72.5c from closer to US75c in Q2. This is consistent with the fall in the exchange rate over the quarter. We have also revised down our forecasts for the AUD/USD to closer to US$0.70 as global trade ructions continue to weigh, though our fair value model of the Australian dollar puts the exchange rate at closer to US75c based on current interest rate differentials and commodity prices.

NAB QUARTERLY BUSINESS SURVEY – MORE DETAILS ON INDUSTRY

CHART 34: BUSINESS CONDITIONS BY INDUSTRY

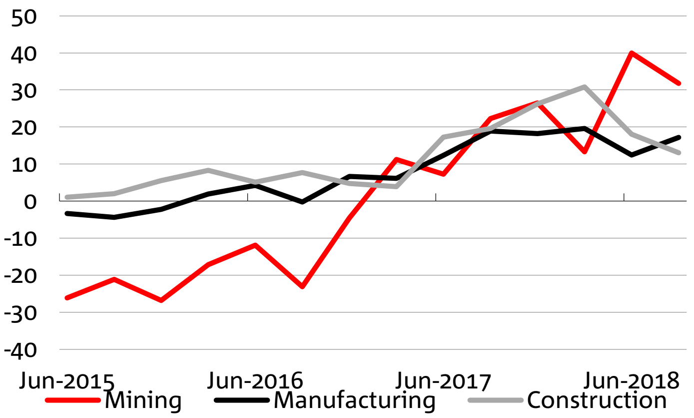


CHART 37: BUSINESS CONFIDENCE BY INDUSTRY

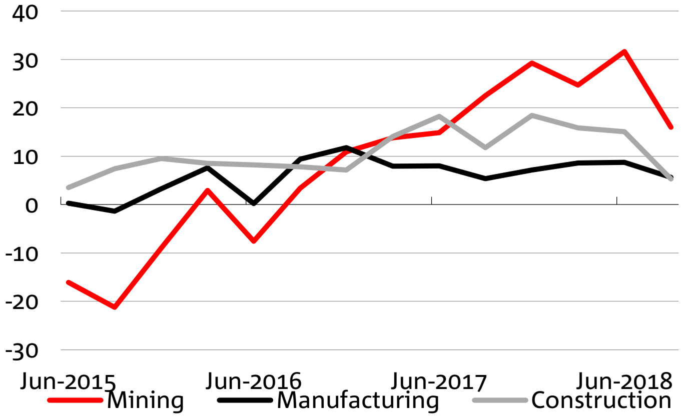


CHART 35: BUSINESS CONDITIONS BY INDUSTRY

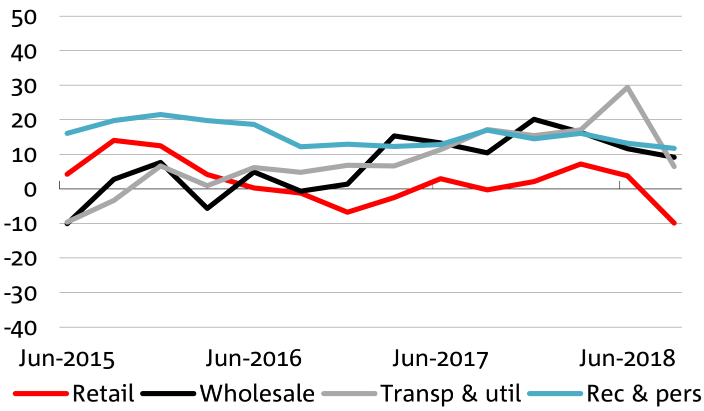


CHART 38: BUSINESS CONFIDENCE BY INDUSTRY

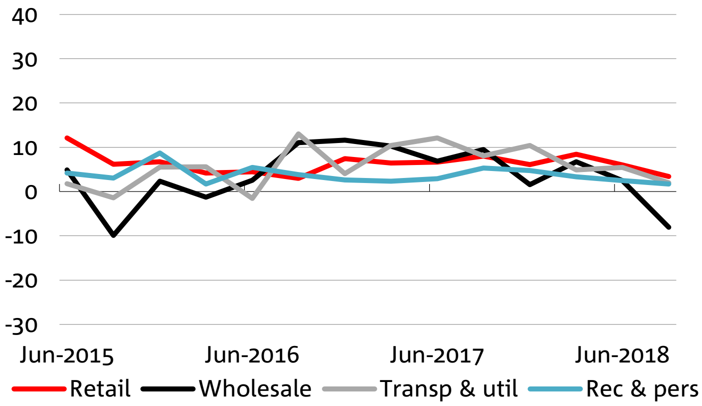


CHART 36: BUSINESS CONDITIONS BY INDUSTRY

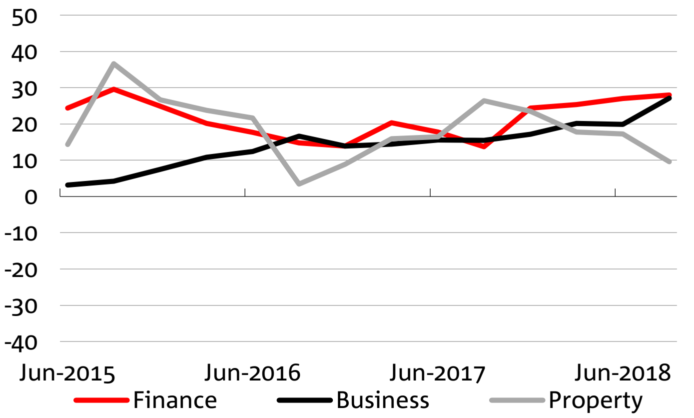
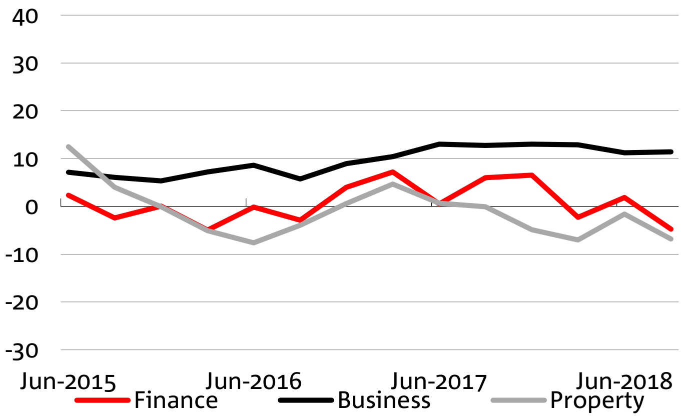


CHART 39: BUSINESS CONFIDENCE BY INDUSTRY



NAB QUARTERLY BUSINESS SURVEY – FURTHER DETAILS BY STATE

CHART 40: BUSINESS CONDITIONS BY STATE (NET BALANCE, S.A.)

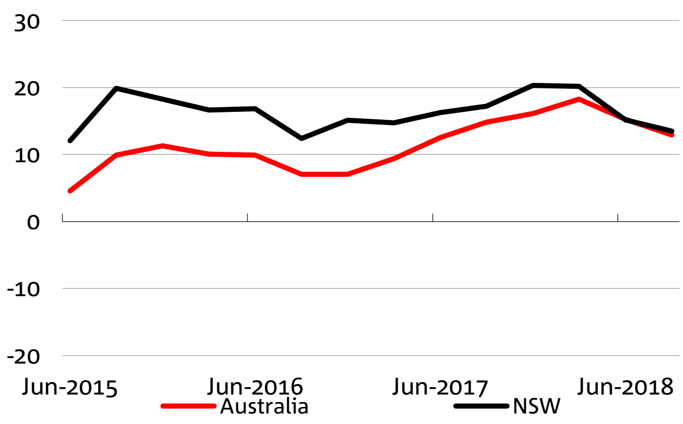


CHART 43: BUSINESS CONFIDENCE BY STATE (NET BALANCE, S.A..)

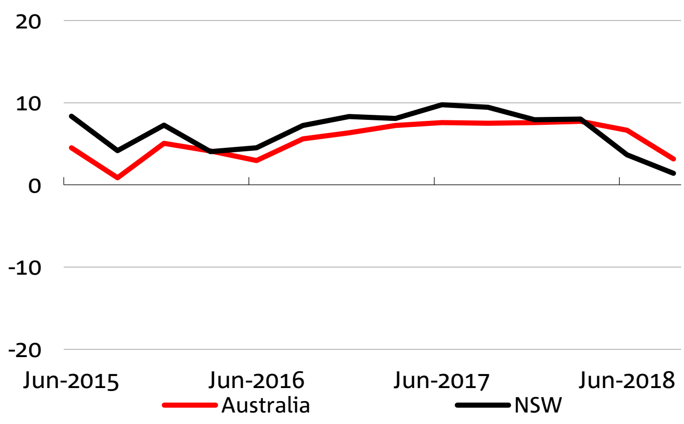


CHART 41: BUSINESS CONDITIONS BY STATE (NET BALANCE, S.A.)

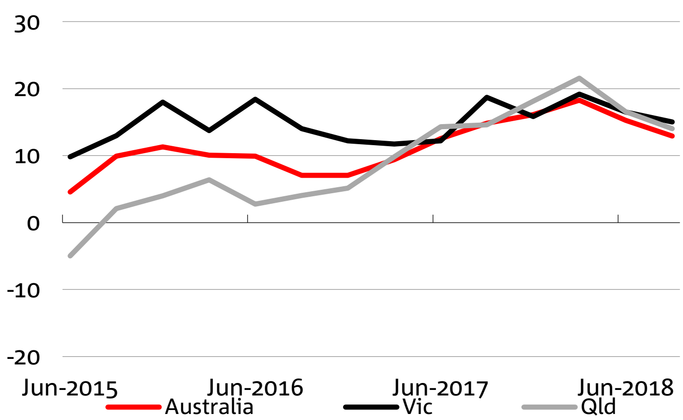


CHART 44: BUSINESS CONFIDENCE BY STATE (NET BALANCE, S.A..)

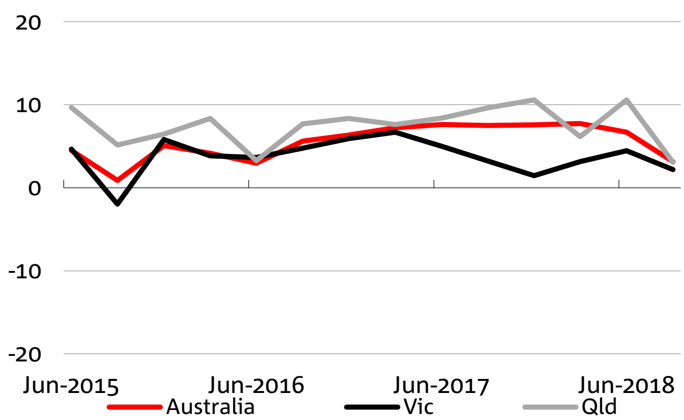


CHART 42: BUSINESS CONDITIONS BY STATE (NET BALANCE, S.A.)

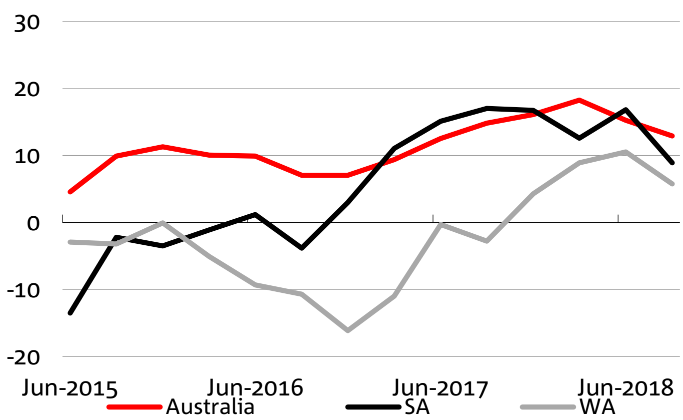
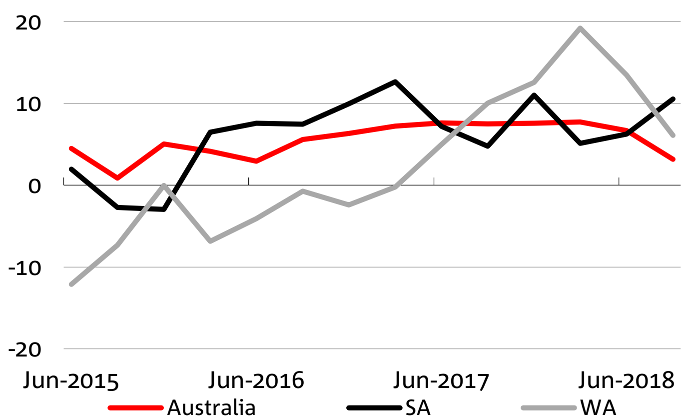


CHART 45: BUSINESS CONFIDENCE BY STATE (NET BALANCE, S.A..)



NAB QUARTERLY BUSINESS SURVEY – DATA APPENDIX

	Quarterly					*Monthly*				
	2017q3	2017q4	2018q1	2018q2	**2018q3**	2018m5	2018m6	**2018m7**	**2018m8**	**2018m9**
Confidence	8	8	8	7	**3**	7	6	7	5	6
Conditions	15	16	18	15	**13**	15	15	13	14	15

	Quarterly					*Monthly*				
	2017q3	2017q4	2018q1	2018q2	**2018q3**	2018m5	2018m6	**2018m7**	**2018m8**	**2018m9**
Trading	19	21	24	22	**15**	22	23	18	18	17
Profitability	16	17	18	15	**12**	14	17	11	14	14
Employment	9	11	14	9	**11**	11	5	10	9	12

	Quarterly[(a)]					*Monthly*				
	2018q2	2018q3	2018q4	2019q2	2019q3	2018m5	2018m6	**2018m7**	**2018m8**	**2018m9**
Conditions	15	**13**	NA	NA	NA	15	15	13	14	15
Conds. next 3m	26	24	**21**	NA	NA					
Conds. nxt 12m	27	28	31	31	**27**					
Orders	7	**4**	NA	NA	**NA**	4	3	2	5	2
Orders next 3m	11	9	**6**	NA	NA					

(a) Quarter to which expectation applies. Business conditions next 12 months not seasonally adjusted.

	Quarterly[(a)]					*Monthly*				
	2017q4	2018q1	2018q2	2018q3	**2018q4**	2018m5	2018m6	**2018m7**	**2018m8**	**2018m9**
Capacity utils.	82.5	82.7	82.8	**83.0**	NA	82.0	82.4	82.2	82.3	82.1
Stocks current	4	6	8	**7**	NA	7	4	2	5	1
Stocks next 3m	3	4	3	0	**0**					

(a) Quarter to which expectation applies. All data are seasonally adjusted.

	2017q4	2018q2	2018q3
Constraints on output (% of firms)*			
Sales & orders	54.7	49.2	**49.9**
Labour	53.1	57.8	**57.8**
Premises & plant	26.2	25.0	**27.3**
Materials	12.0	12.3	**14.1**

** not s.a.*

	Quarterly[(a)]					*Monthly*				
	2018q2	2018q3	2018q4	2019q2	2019q3	2018m5	2018m6	**2018m7**	**2018m8**	**2018m9**
Empl current	9	**11**	NA	NA	NA	11	5	10	9	12
Empl next 3m	17	17	**12**	NA	NA					
Empl nxt 12m	19	22	24	24	**23**					

(a) Quarter to which expectation applies. Employment conditions next 12 months not seasonally adjusted.

NAB QUARTERLY BUSINESS SURVEY – DATA APPENDIX – STATE TABLES

	Quarterly					*Monthly*				
	2017q3	2017q4	2018q1	2018q2	**2018q3**	2018m5	2018m6	**2018m7**	**2018m8**	**2018m9**
Business conditions										
NSW	17	20	20	15	**13**	16	14	10	15	15
VIC	19	16	19	17	**15**	16	17	18	14	19
QLD	15	18	22	17	**14**	16	20	16	17	11
SA	17	17	13	17	**9**	14	11	6	7	9
WA	-3	4	9	11	**6**	14	7	8	14	10

	Quarterly					*Monthly*				
	2017q3	2017q4	2018q1	2018q2	**2018q3**	2018m5	2018m6	**2018m7**	**2018m8**	**2018m9**
Business confidence										
NSW	9	8	8	4	**1**	3	5	6	2	3
VIC	3	1	3	4	**2**	5	3	6	5	6
QLD	10	11	6	11	**3**	11	11	7	7	11
SA	5	11	5	6	**11**	7	11	13	11	6
WA	10	13	19	13	**6**	15	8	8	9	6

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APPENDIX: LIST OF SERIES AVAILABLE TO SUBSCRIBERS^

MONTHLY BUSINESS SURVEY*

Business Confidence	Net balance
Business Conditions	Net balance
Trading Conditions	Net balance
Profitability	Net balance
Employment	Net balance
Forward Orders	Net balance
Stocks	Net balance
Exports	Net balance
Capital Expenditure (Capex)	Net balance
Cash Flow	Net balance
Labour Costs	% change at quarterly rate
Purchase Costs	% change at quarterly rate
Final Prices	% change at quarterly rate
Capacity Utilisation	Per cent
Borrowing Demand & Conditions	%; net balance

All series available on an industry basis for:

Mining
Manufacturing
Construction
Retail trade
Wholesale trade
Transport / Utilities
Finance / Property / Business Services
Recreation / Personal Services

All available on a state basis for:

New South Wales
Victoria
Queensland
WA
SA/NT
Tasmania

*All data available in original, seasonally adjusted and trend terms.

^Subscribers also receive a copy of the Subscriber details publication which contains a variety of extra charts and tables.

QUARTERLY BUSINESS SURVEY*

Business Confidence

Business Conditions (current, next 3 mth, next 12 mth)

Trading conditions (current, next 3 mth, next 12 mth)

Profitability (current, next 3 mth, next 12 mth)

Employment (current, next 3 mth, next 12 mth)

Forward orders (current, next 3 mth)

Stocks (current, next 3 mth)

Export orders (current, next 3 mth)

Capital expenditure (current, next 3 mth, next 12 mth, fiscal year)

Required rate of return on investment

Cash flow

Labour costs (current, next 3 mth)

Purchase costs (current, next 3 mth)

Final prices (current, next 3 mth)

Capacity Utilisation

Borrowing index (current, next 3 mth)

Borrowing demand (current, next 3 mth)

Constraints on output (demand, labour, materials, premises & plant, finance/working capital)

Constraints on profit (capital, demand, high AUD, low AUD, interest rates, labour, tax, wages, energy costs, other)

Constraint on employment (demand, confidence, cashflow, suitable labour, high wages, government policy, labour not at full capacity, other, don't' know)

Margins (current, next 3 mth)

Overheads (current, next 3 mth)

Productivity growth

Number of employees

Hours worked

Gross Sales

Output/sales growth (current fiscal year)

Average earnings (current fiscal year)

Short term interest rate

Exporters hedged FX exposure (%)

Importers hedged FX exposure (%)

Months hedged (exporters)

Months hedged (importers)

Favourable hedge position (% of exporters)

Favourable hedge position (% of importers)

Affected vs not affected by AUD

Response to AUD (downsized, reduced, overheads, hedging, import substitution, focus on domestic market, other, don't' know)

Driver of trading conditions (demand, wages/jobs, house prices, rates, exchange rate, tax/govt policy, seasonal, finance/working capital, company specific, other)

What will improve confidence (lower rates, more suitable labour, easier funding, government policy, higher demand, higher AUD, lower AUD, easier compliance, other)

All series available on an industry basis for:

Mining (sub-groups: Mining Extraction, Mining Services)

Manufacturing (sub-groups: food beverage & tobacco, textile clothing footwear & leather, wood & paper product, printing publishing & recorded media, petroleum coal chemical & associated products, non-metallic mineral product, metal product, machinery & equipment, other)

Construction (sub-groups: Residential Building, Non-residential Building, Other Construction, Construction Services)

Retail trade (sub-groups: Food, Personal & Household Goods, Motor Vehicle Retailing & Services, Other Retail)

Wholesale trade

Transport / Utilities

Finance / Property / Business Services (sub-groups: Finance, Insurance, Services to Finance & Insurance, Property Services, Business Services)

Recreation / Personal Services (Sub-groups: Motion picture, Radio & Television Services, Libraries Museums & the Arts), Sports & Recreation, Personal Services, Accommodation Cafes & Restaurants, Health Services, Education, Other Services)

All series available on a state basis for:

New South Wales

Victoria

Queensland,

WA

SA/NT

Tasmania

*Data available in original, seasonally adjusted and trend terms.