

NAB BUSINESS INNOVATION INDEX 2021

TOWARD A NEW PROXY OF ECONOMY WIDE INNOVATION IN AUSTRALIA



NAB Behavioural & Industry Economics

April 2021

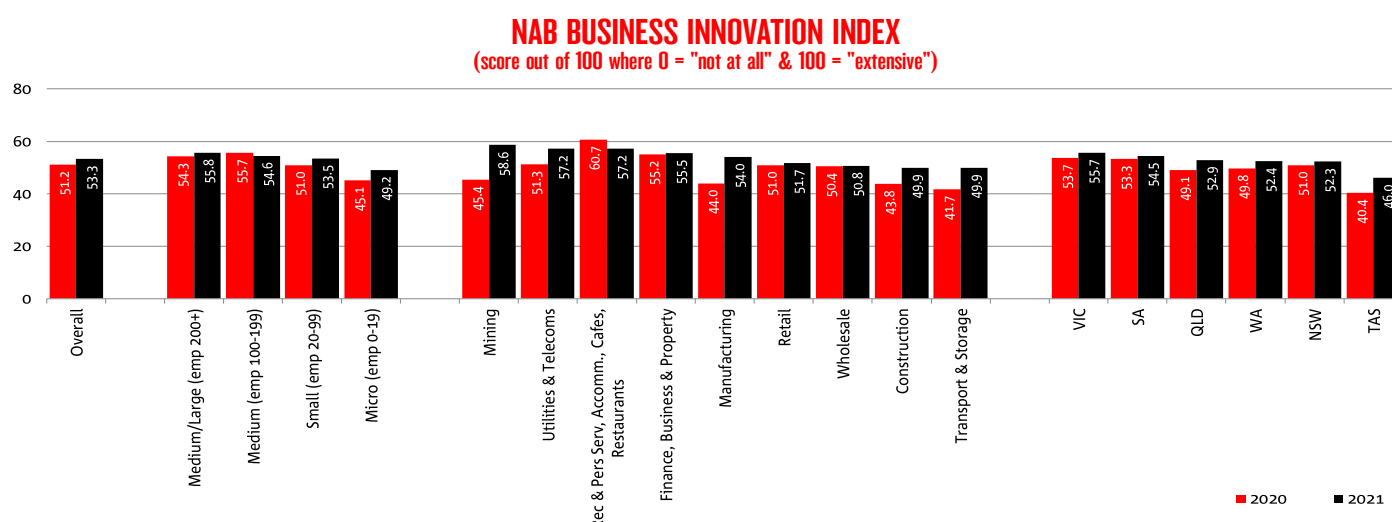
NAB's 2021 Business Innovation Index shows innovation in Australia is rising again as businesses make some difficult decisions and look to growth beyond COVID-19. 2020 was all about pivoting for survival and business continuity. 2021 has seen many businesses take a closer look at their balance sheets, inefficient processes or less profitable aspects of the business, by doubling down on the things that really make a difference to operating as quickly and efficiently as possible. Innovation needs to be back on the nation's economic agenda. Business investment in innovation has declined over the past decade as many businesses focussed on shorter-term goals. COVID-19 has created new opportunities for growth and those businesses that invest in innovation are likely to outperform post the pandemic.

After falling to a survey low 51.2 pts in 2020 at the height of the pandemic, innovation has recovered to 53.3 pts in 2021. While innovation still remains well below the levels seen during 2016-2019, there has been an important shift in the type of innovation. With business conditions returning to multi-year highs and ongoing signs of improvement in the economy, innovation is increasingly being driven by doing things more quickly (up 7.8 pts to 50.2 pts) and cost efficiently (up 5.5 pts to 53.8 pts). Innovation arising from doing things differently has fallen noticeably (down 7.0 pts to 55.9 pts), following last year's COVID-induced spike, but is still the main driver of innovation. Businesses are not usually willing or able to make drastic and rapid changes. Importantly, many businesses have taken the opportunity to build these changes made during COVID into their longer-term business models.

Innovation was higher in all states in 2021 with Victoria once again crowned Australia's most innovative state (up 2.0 pts to 55.7 pts, ahead of SA at 54.5 pts). Mining has emerged as the most innovative sector (up 13.2 pts to 58.6 pts), with notable improvements also in Manufacturing, Transport, Storage and Construction. In 2020 innovation tumbled to survey lows in the wake of COVID-19. Amid widespread supply-chain and cashflow disruptions, forced business closures and labour shedding, innovation arising from businesses doing things more quickly and cost efficiently sank. But the pandemic also brought considerable change and adaptation. Innovation from businesses doing things differently rose sharply as many were forced to pivot due to COVID. Necessity was the mother of invention, with some of the sectors hit hardest by the pandemic such as Recreational & Personal Services, Accommodation and Cafes & Restaurants, among the most innovative in 2020.

In marked contrast, in 2021 innovation has lifted in all industries except Personal, Recreational Services & Hospitality sector (down 3.5 pts to 57.2 pts). Innovation also increased across all sizes of business, with the exception of medium-sized firms. Innovation was highest in medium/large firms (up 1.4 pts to 55.8 pts), but improved most in micro firms (up 4.1 pts to 49.2 pts).

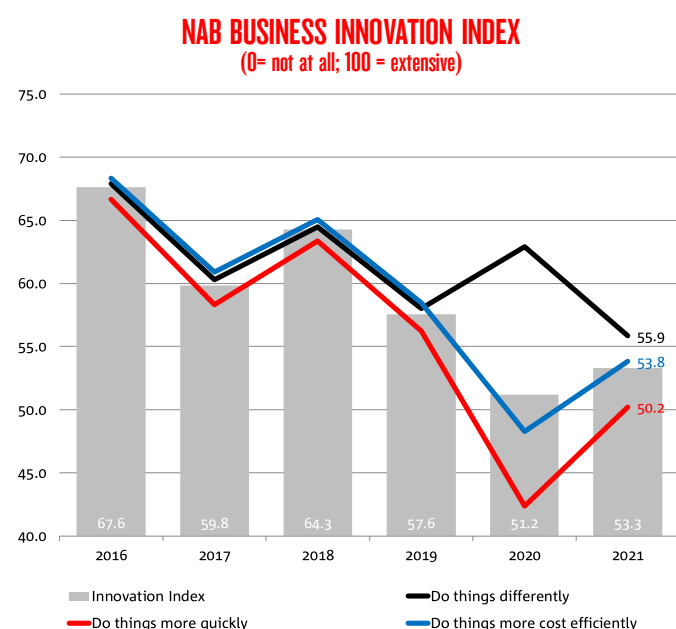
The NAB Business Innovation Index has been running annually since 2016, and is derived from a survey of around 1,700 Australian businesses from small to very large. The latest survey was taken during the period 18 Feb- 13 Mar.



NAB BUSINESS INNOVATION INDEX

For many businesses, innovation can seem like an abstract concept. But we know that innovation is common across the entire business sector. Driven by their passion for customers and competitive pressures, many business owners innovate continuously, irrespective of the size of the business. Many businesses don't perceive themselves as innovators and often do not even call what they are doing "innovation". Rather they are more likely to speak of improvements or simple changes they have made to their everyday processes or incremental enhancements to their products or services.

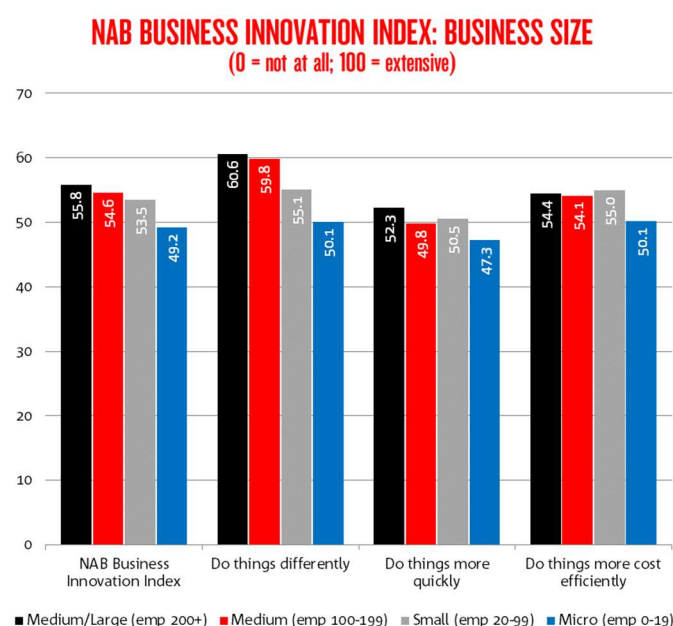
Many businesses have an immature approach to innovation measurement. While individual innovation projects can be accomplished without organisational measures of innovation, to sustain high levels of systematic innovation capability, businesses typically need to set up measures and business outcomes. But, there is no simple diagnostic for capturing innovation. The NAB Innovation Index provides an intuitive and simple metric for all sizes of businesses to track their innovation performance and drivers through time. The Index provides a measure applicable to all business, regardless of size, type, industry or location. It has been running annually since 2016, and is derived from a survey of around 1,700 Australian businesses from small to very large. The Index is based on the extent to which firms have "tweaked", "adjusted", "improved" or "changed" anything in their business that allowed them in the past year to do things differently; more quickly; and more cost efficiently.



After falling to a low of 51.2 pts at the height of the COVID pandemic (mid-2020), the NAB Business Innovation Index recovered to 53.3 points in 2021 (March) but is still below levels seen from 2016-2019.

In 2020, widespread supply-chain and cashflow disruptions, forced business closures and labour shedding. This saw innovation from doing things more quickly and cost efficiently sink. But the crisis also brought change and adaptation with innovation coming doing things differently up sharply.

But with business conditions since returning to multi-year highs and ongoing signs of improvement in the economy, higher innovation in 2021 is being driven by doing things more quickly (up 7.8 pts to 50.2 pts) and cost efficiently (up 5.5 pts to 53.8 pts). Innovation stemming from doing things differently has fallen noticeably (down 7.0 pts to 55.9 pts), but it is still the biggest contributor to overall innovation.



In 2021, innovation increased across all sizes of business - except medium-sized firms (down 1.1 pts to 54.6 pts).

Innovation was highest in medium/large firms (up 1.4 pts to 55.8 pts). It improved most in micro firms (up 4.1 pts to 49.2 pts), but overall innovation in this group continues to be somewhat lower than for all other sizes of business.

Innovation from doing things differently was lower in all sizes of businesses relative to 2020, particularly mid-sized firms (down 9.7 pts to 59.8 pts), after having out-performed on this measure in 2020.

All firms reported a sharp increase in innovation arising from doing things more quickly, particularly micro firms (up 10.0 pts to 47.3 pts). Innovation from cost efficiencies also increased across the board, led by small firms (up 7.6 pts to 55.0 pts). Medium/large firms again scored highest for doing things differently (60.6 pts) and more quickly (52.3 pts), but small firms led the way for cost efficiency innovations (55.0 pts). Micro firms continued to rate their innovation lowest across all components of the NAB Business Innovation Index - see table below for 2021 versus 2020 comparison.

Some of NAB's more interesting findings over the past few years have centred around innovation behaviours among smaller enterprises. Importantly, the research suggests small businesses innovate more than they realise and particularly shows the energy and dynamism among younger businesses, with a break point being at around 10 years of operation.

Importantly, being highly innovative has a strong positive impact on the business performance of highly innovative firms. The most innovative firms tend to be at both ends of the spectrum - very high performing businesses (with strong business conditions and capital to match) as well as and very low performing (weak conditions with little capital and desperate for survival). Innovation among high performing firms is often accompanied by capital investment. Once an innovation occurs, this investment can spread the innovation throughout a business to help diffuse innovation throughout the organisation and further drive growth.

The key motivation of businesses is to innovate to drive growth and revenues. However, this is typically a much bigger driver of innovation for large businesses, while SMEs are more likely to be motivated by factors such as differentiating their business, widening their customer base and enabling them to manage change and respond to key trends.

While many small businesses view innovation as a core tenant of their broader business strategy, it is much more embedded in the overall business plan of a younger business. Strategy, both overall and specifically for innovation, is known to be a core driver of innovation activities and of success. That said, relatively few businesses, regardless of age, have well developed processes or structures in place to select and prioritise which innovation projects get approved and/or funded. Relative to strategic focus, innovation processes and structures are weak, and without these implementation mechanisms effectively in place, innovation strategy will be limited in their impact. The differences between low and high innovation cultures on these factors are large.

Knowing their markets and customers, constant process reviews, learning from failures and passion and drive are the most common aspects of culture of innovation that have allowed firms to be innovative. Highly innovative SMEs also identified their ability to generate and implement new ideas as key aspects of their culture. Significantly, small businesses report having the most intimate knowledge of their customers.

NAB BUSINESS INNOVATION INDEX: BUSINESS SIZE

	NAB Business Innovation Index		Doing things differently		Doing things more quickly		Doing things more cost efficiently	
	2021	2020	2021	2020	2021	2020	2021	2020
Micro	49.2	45.1	50.1	53.4	47.3	37.3	50.1	44.6
Small	53.5	51.0	55.1	63.0	50.5	42.6	55.0	47.4
Medium	54.6	55.7	59.8	69.5	49.8	45.0	54.1	52.6
Medium/Large	55.8	54.3	60.6	68.4	52.3	45.0	54.4	49.6

NAB's Business Innovation Index lifted in all industries in 2021 except Personal, Recreational Services & Hospitality sector (down 3.5 pts to 57.2 pts). This sector - one of the hardest hit by the pandemic - was previously the most innovative in 2020. Instead, Mining emerged as the most innovative sector in 2021 (up 13.2 pts to 58.6 pts). There was also a significant uplift in innovation activities recorded in the Manufacturing (up 10.0 pts to 54.0 pts), Transport & Storage (up 8.2 pts to 49.9 pts) and Construction (up 6.2 pts to 49.9 pts) industries - although Transport & Storage and Construction were the least innovative sectors in the 2021 survey.

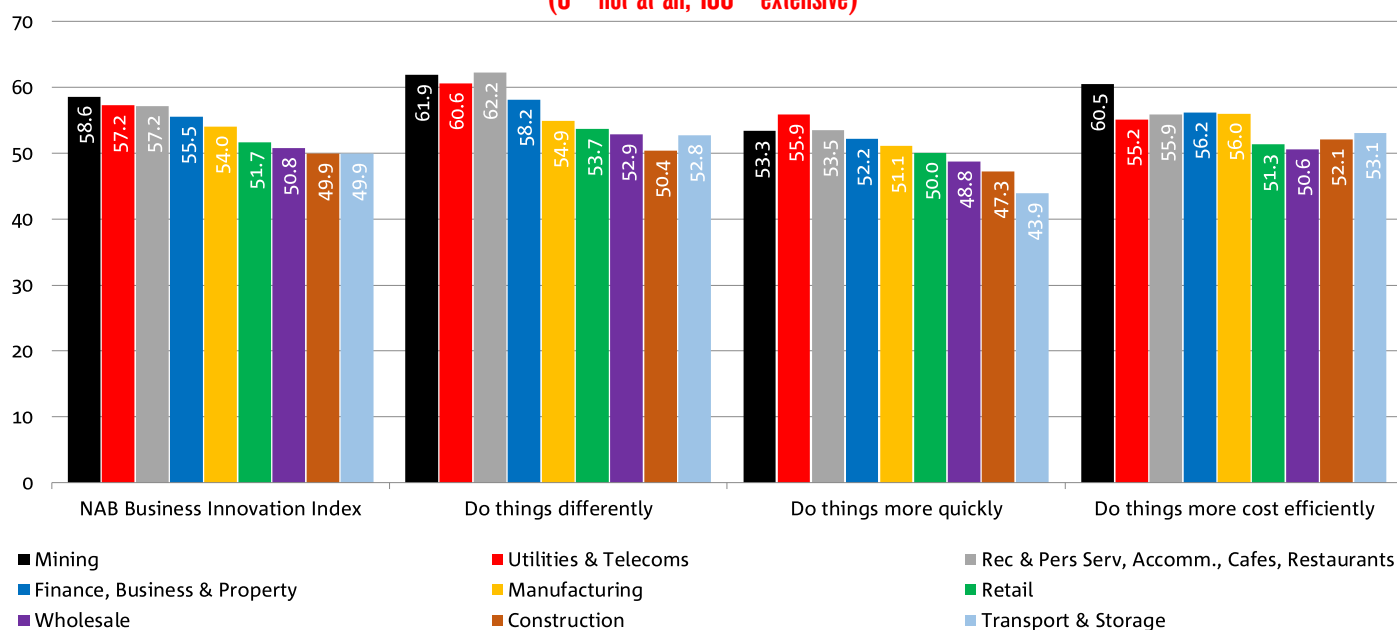
All industries reported lower innovation from doing things differently, except Mining (up 2.9 pts to 61.9 pts) which also rated this innovation highest. Innovation from doing things differently fell most in the Personal, Recreational Services & Hospitality (down 9.9 pts to 62.8 pts), Finance, Business & Property Services (down 8.7 pts to 58.2 pts) and Retail (down 7.1 pts to 53.7 pts) industries, but was lowest overall in Construction (down 3.7 pts to 50.4 pts). Doing things differently was however the biggest contributor to overall innovation in most industries except Manufacturing and Construction, where cost efficiency contributed most.

All sectors reported higher innovation gains from doing things more quickly - particularly Mining (up 17.6 pts to 53.3 pts), Manufacturing (up 16.1 pts to 50.0 pts), Transport & Storage (up 13.1 pts to 43.9 pts) and Construction (up 13.0 pts to 47.3 pts). Innovation driven by doing things more quickly was highest in Utilities & Telecoms (55.9 pts) and lowest in Transport & Storage (43.9 pts). Doing things more quickly contributed least to overall innovation in all industries, except Utilities & Telecoms, where cost efficiency contributed the least.

Innovation from doing things more cost efficiently also increased in all sectors except Personal, Recreational Services & Hospitality (down 3.1 pts to 55.9 pts). Mining (up 19.0 pts to 60.5 pts), Manufacturing (up 15.9 pts to 56.0 pts) and Transport & Storage (up 12.7 pts to 53.1 pts) reported the biggest innovation gains from cost efficiency in 2021, with overall cost efficiency innovation highest in Mining (60.5 pts) and lowest in Wholesale Trade (50.6 pts) - see table for more detail.

NAB BUSINESS INNOVATION INDEX: INDUSTRY

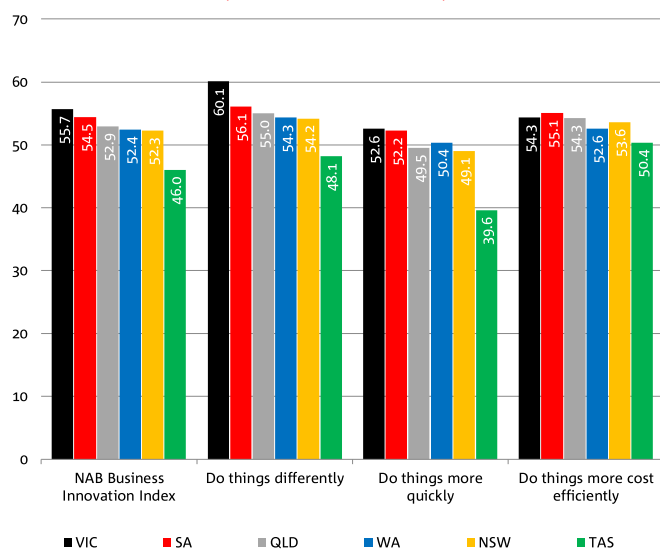
(0 = not at all; 100 = extensive)



NAB BUSINESS INNOVATION INDEX: INDUSTRY

	NAB Business Innovation Index		Doing things differently		Doing things more quickly		Doing things more cost efficiently	
	2021	2020	2021	2020	2021	2020	2021	2020
Mining	58.6	45.4	61.9	59.0	53.3	35.7	60.5	41.4
Utilities & Telecoms	57.2	51.3	60.6	62.8	55.9	45.0	55.2	46.1
Rec & Pers Serv, Accom., Cafes, Restaurants	57.2	60.7	62.2	72.1	53.5	50.9	55.9	59.0
Finance, Business & Property	55.5	55.2	58.2	66.9	52.2	46.9	56.2	51.7
Manufacturing	54.0	44.0	54.9	57.0	51.1	34.9	56.0	40.1
Retail	51.7	51.0	53.7	60.7	50.0	42.2	51.3	50.0
Wholesale	50.8	50.4	52.9	58.6	48.8	44.5	50.6	48.3
Construction	49.9	43.8	50.4	54.1	47.3	34.3	52.1	42.9
Transport & Storage	49.9	41.7	52.8	53.9	43.9	30.9	53.1	40.4

NAB BUSINESS INNOVATION INDEX: STATES (0 = not at all; 100 = extensive)



Innovation was higher in all states in 2021. VIC was again the most innovative state (up 2.0 pts to 55.7 pts), ahead of SA (up 1.2 pts to 54.5 pts). Innovation improved most in TAS (up 5.6 pts to 46.0 pts) but it remained the least innovative state by some margin.

All states reported lower innovation from doing things differently, with particularly large falls in TAS (down 12.7 pts to 48.1 pts) and SA (down 10.3 pts to 56.1 pts). Doing things differently was again the key driver of innovation in all states, bar TAS (cost efficiency). It was highest in VIC (60.1 pts) and lowest in TAS (48.1 pts).

All states reported higher innovation from doing things more quickly, with the biggest gains in TAS (up 12.8 pts to 39.6 pts) and WA (up 10.2 pts to 50.4 pts). VIC however led the way for doing things more quickly (52.6 pts), just ahead of SA (52.2 pts), with TAS trailing by some margin (39.6 pts).

Innovation arising from cost efficiency was higher in all states relative to 2020. Innovation gains from this measure were highest in SA (55.1 pts), ahead of VIC (54.3 pts) and QLD (54.3), and lowest in TAS despite reporting by far the biggest gains in cost efficiency (up 16.8 pts to 50.4 pts).

NAB BUSINESS INNOVATION INDEX: STATE

	NAB Business Innovation Index		Doing things differently		Doing things more quickly		Doing things more cost efficiently	
	2021	2020	2021	2020	2021	2020	2021	2020
VIC	55.7	53.7	60.1	64.9	52.6	45.2	54.3	50.9
SA	54.5	53.3	56.1	66.4	52.2	45.0	55.1	48.5
QLD	52.9	49.1	55.0	60.3	49.5	40.5	54.3	46.6
WA	52.4	49.8	54.3	61.8	50.4	40.2	52.6	47.3
NSW	52.3	51.0	54.2	62.5	49.1	42.2	53.6	48.3
TAS	46.0	40.4	48.1	60.8	39.6	26.8	50.4	33.6

CONTACT THE AUTHORS

Dean Pearson

Head of Behavioural & Industry Economics

Dean.Pearson@nab.com.au

+613 8634 2331

Robert De lure

Senior Economist - Behavioural & Industry Economics

Robert.De.lure@nab.com.au

+613 8634 4611

Brien McDonald

Senior Economist - Behavioural & Industry Economics

Brien.McDonald@nab.com.au

+613 8634 3837

Important Notice

This document has been prepared by National Australia Bank Limited ABN 12 004 044 937 AFSL 230686 ("NAB"). Any advice contained in this document has been prepared without taking into account your objectives, financial situation or needs. Before acting on any advice in this document, NAB recommends that you consider whether the advice is appropriate for your circumstances.

NAB recommends that you obtain and consider the relevant Product Disclosure Statement or other disclosure document, before making any decision about a product including whether to acquire or to continue to hold it.

Please click [here](#) to view our disclaimer and terms of use.