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SME PMI® Business Activity Report.

Exclusive insights into the SME economy
presented by **Judo Bank**.

Employment growth renews in August.

Key findings



Business activity softens again as new orders decline

Business activity across Australian SMEs fell midway into the third quarter, according to the latest Judo Bank SME Business Activity Report data. Reduced inflows of new work resulted in business activity lowering for a third straight month. Consequently, price pressures eased within the SME sector. That said, staffing levels climbed in August as firms increased their headcounts to cope with ongoing operations and in anticipation for future activity. Business optimism notably improved to its highest level in seven months.

The seasonally adjusted Judo Bank Australia SME Business Activity Index fell to 47.3 in August, down from 49.1 in July. Posting below the 50.0 neutral mark for the third consecutive month, the latest data signalled a sustained contraction in business activity among Australian SMEs. The rate of decline was the quickest since March, but remained modest overall.

A deepening of the contraction in new orders, underpinned by sharper reductions in both manufacturing and services new business,



Charge inflation lower alongside cost pressures

contributed to the latest decline in business activity. Anecdotal evidence from panellists indicated that higher interest rates and softening economic conditions negatively affected clients' willingness to spend in August. The fall in new business was again more pronounced among goods producers compared to service providers.

As a result of a deterioration in demand conditions, input costs climbed at a slower rate in August. Lower service sector input price inflation more than offset a quicker rise in costs among manufacturers. The rate of overall input cost inflation dipped to a two-month low, but remained elevated above the series average.

Consequently, SMEs continued to share these cost increases – stemming from higher wages, input material and transport costs – with their clients, but likewise at a slower rate. While rates of inflation for both SMEs and large enterprises remained above their respective series averages, SMEs reported a softer rise in charges compared to their larger



Business confidence highest since January

counterparts over the latest survey period.

Meanwhile renewed growth in staffing levels was recorded for the SME sector in August. Central to the expansion was rising service sector employment whereas manufacturing headcounts continued to recede. Service providers reported increasing their workforce capacity to support ongoing operations and in anticipation of rising workloads. In fact, services SMEs were the most upbeat in seven months, more than countering a deterioration in manufacturing sentiment, thereby lifting the overall Future Activity Index to the highest since January. The broadly optimistic view held by SMEs were buoyed by hopes of sales growth on the back of better economic conditions ahead.

With the support of additional staff and amid fewer new work intakes, the level of work outstanding fell in August among Australian SMEs. This extended the sequence of declines to almost a year. SMEs within the service sector cleared their backlogs at a faster rate compared to their manufacturing counterparts in August.

Judo Bank SME Business Conditions Index

sa, >50 = growth since previous month



Sources: Judo Bank, S&P Global PMI.
Data were collected 09-25 August 2023.

Comment



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Warren Hogan

Chief Economic Advisor at Judo Bank



Comment

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Warren Hogan, Chief Economic Advisor at Judo Bank said:

“Australia’s economic slowdown is starting to impact the SME sector following a strong performance earlier this year.

“The Judo Bank SME business activity report showed further easing business conditions in August. Both the activity and new business indexes fell to levels historically consistent with a soft landing for the economy.

“Manufacturing sector activity has been soft for most of 2023 and stayed soft in August. Service sector activity improved earlier this year but weakened through the winter months.

“The new business indexes for both the services and manufacturing sectors weakened significantly in August. Still, they are at levels indicative of a soft landing for the SME sector rather than a sharper downturn, which we would expect to see in an economic recession.

“SME activity levels are above those seen in 2022, when the initial wave of rate hikes disproportionately impacted SMEs compared to large businesses. The slowdown experienced through 2023 thus far has been similar between SMEs and larger firms.

“Australia’s small manufacturers will need to be watched over the months ahead. The pipeline of new work dropped off over winter against a backdrop of soft activity levels. Encouragingly, employment intentions and confidence are holding up through the current slowdown in activity.

“SMEs remain confident about the future, with an improvement in the future output index in August. This suggests that most SMEs expect the economic slowdown to be shallow and short-lived.

“This is also reflected in the employment measure, which rose in August and is in expansionary territory. Australian SMEs are planning to expand their workforce in the future, which is consistent with the expectation that the current downturn in economic activity will be temporary.

“SME cost pressures remain elevated but are well down on the historically high levels in 2021 and 2022. SME cost pressures are not dissimilar to large businesses, with August index readings higher than before the pandemic. All Australian businesses, SMEs included, are still dealing with elevated cost pressures in the middle of 2023.

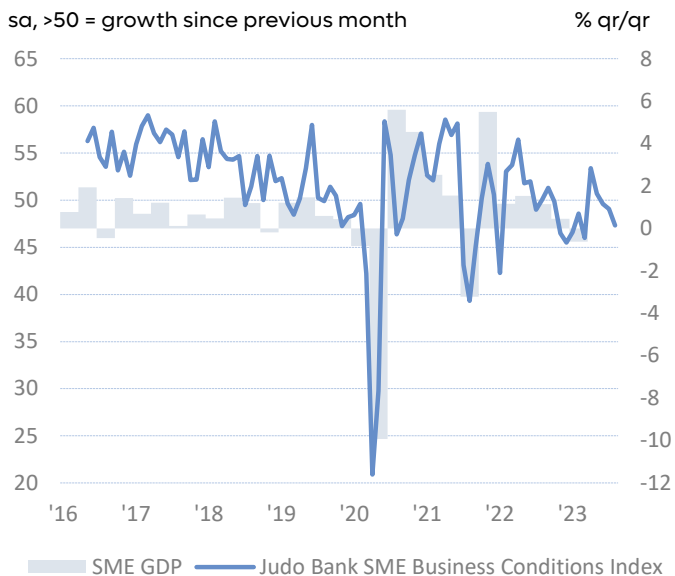
“Of some concern for SMEs is what appears to be a reduced capacity to pass cost pressures onto customers through increases in their final prices. This contrasts with larger businesses where the final price index has increased in recent months to a greater extent than for SMEs.

“This suggests that SMEs are finding it comparatively harder to protect margins through this downturn in economic activity. We will be watching the price indexes closely over the months ahead to gauge the extent to which elevated cost pressures will impact profitability and investment plans in the SME sector.

“At this stage, the continued demand for staff and confidence in future activity suggests this is not having a significant negative effect.”



Judo Bank SME Business Conditions Index



Sources: Judo Bank, S&P Global PMI, Australian Bureau of Statistics via S&P Global Market Intelligence.

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Business confidence among Australian SMEs showed further improvements in August.

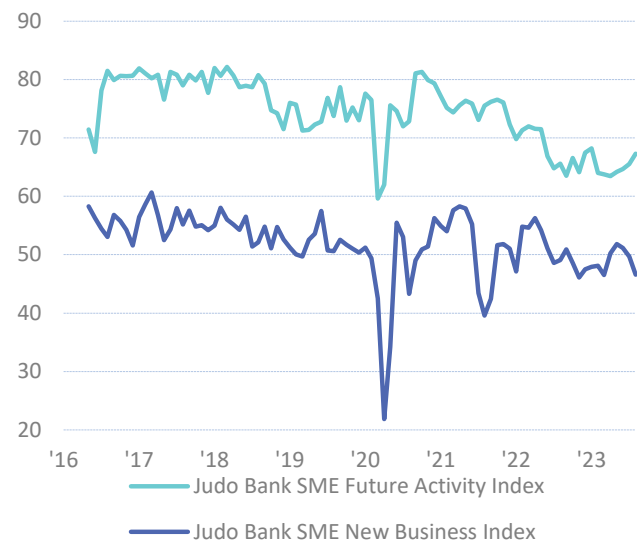


Demand and outlook

New orders for goods and services from Australian SMEs fell for a second consecutive month in August. The rate of decline was solid and the fastest since March. Shaper declines across both services new business and manufacturing new orders contributed to the latest downturn. According to panellists, higher interest rates and softening economic conditions negatively affected demand over the latest survey period.

Despite lower new orders and output in August, sentiment among Australian SMEs improved for the fourth month in a row. Moreover, the level of business confidence rose to the highest since January, driven by heightened optimism among service providers. In contrast, manufacturers were less upbeat compared to July. Overall, SMEs were generally hopeful that sales can improve in the 12-months ahead as economic conditions improve and with greater capacity to take on more work.

sa, >50 = growth since previous month



Sources: Judo Bank, S&P Global PMI.

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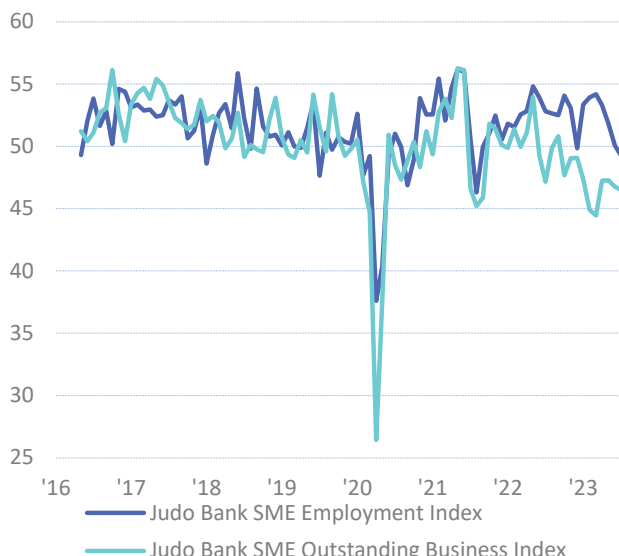


Employment and capacity

Staffing levels among SMEs in Australia rose in August after declining marginally over July. This was underpinned by a renewed increase in service sector headcounts, while manufacturers saw a modest decline in average workforce capacity. The seasonally adjusted Employment Index for the SME sector notably saw the biggest increase in seven months, outperforming the change for large enterprises even though the latter recorded a higher rate of employment growth.

On the back of higher workforce capacity and reduced new order inflows, Australian SMEs worked through their backlogged orders in August, resulting in an eleventh straight monthly reduction in the level of unfinished work. The rate of decline was quicker among service providers compared to goods producers.

sa, >50 = growth since previous month



Sources: Judo Bank, S&P Global PMI.



Comment



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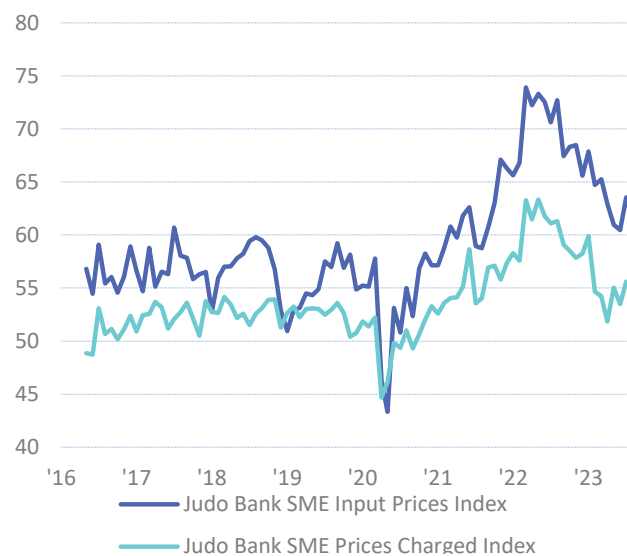
Prices



Higher wages, raw material and transport costs continued to push up overall input costs for Australian SMEs in August, according to panellists. That said, cost pressures eased as higher manufacturing sector price inflation was more than offset by lower cost inflation among service providers. The rate of input cost inflation was nevertheless still elevated above the series average in August.

As a result, SMEs continued to share their higher cost burdens with clients, leading to a further increase in output charges. Although the rate of charge inflation eased slightly from July, in line with costs, it remained historically elevated.

sa, >50 = inflation since previous month



Sources: Judo Bank, S&P Global PMI.



Contact

Warren Hogan Chief Economic Advisor

Judo Bank

T: +61 414 498 675

warren.hogan@judo.bank

Jingyi Pan Economics Associate Director

S&P Global Market Intelligence

T: +65-6439-6022

jingyi.pan@spglobal.com

SungHa Park Corporate Communications

S&P Global Market Intelligence

T: +82-2-6001-3128

sungha.park@spglobal.com

If you prefer not to receive news releases from S&P Global, please email katherine.smith@spglobal.com. To read our privacy policy, click [here](#).

Survey methodology

The Judo Bank SME Business Activity Report is compiled by S&P Global from responses to questionnaires sent to around 650 manufacturing and service sector SMEs. SMEs are defined as companies with less than 200 employees. The sectors covered include manufacturing, consumer services (excluding retail), transport, information, communication, finance, insurance, real estate and business services. The manufacturing and services panels are stratified by detailed sector and company workforce size, based on contributions to GDP. Data collection began in May 2016.

Survey responses are collected in the second half of each month and indicate the direction of change compared to the previous month. A diffusion index is calculated for each survey variable. The index is the sum of the percentage of 'higher' responses and half the percentage of 'unchanged' responses. The indices vary between 0 and 100, with a reading above 50 indicating an overall increase compared to the previous month, and below 50 an overall decrease. The indices are then seasonally adjusted.

The headline figure is the SME Business Conditions Index, a GDP-weighted average of the SME Manufacturing Business Conditions Index and the SME Services Business Conditions Index. These are diffusion indices calculated from questions that ask for changes in the volume of output (for manufacturers) or business activity (for service providers) compared with one month previously. The weights reflect the relative size of the manufacturing and service sectors according to official GDP data.

Underlying survey data are not revised after publication, but seasonal adjustment factors may be revised from time to time as appropriate which will affect the seasonally adjusted data series.

For further information on the survey methodology, please contact economics@ihsmarkit.com.

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Judo Bank is Australia's first purpose-built challenger bank for small and medium-sized businesses (SMEs) and the first fully licensed Australian bank to IPO in 25 years. Judo was founded by a small group of experienced lending professionals and its purpose is to be the most trusted SME business bank in Australia. The company's relationship-led lending model, which brings back the craft of relationship banking, is enabled by its legacy free, digital, cloud-based technology architecture. Lending products are originated and distributed through direct and third-party channels and are funded by deposits, wholesale debt and regulatory capital. www.judo.bank

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