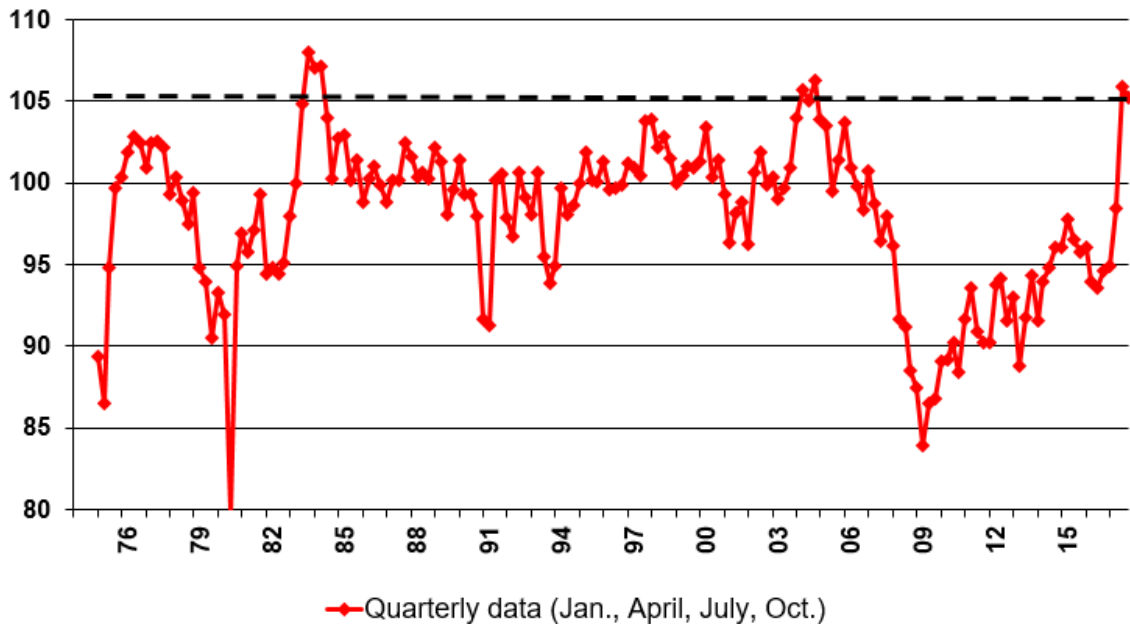


NFIB Small Business Economic Trends - July 2017

Embargoed Tuesday, August 8 at 6 a.m.

(Based on 1533 respondents to the July survey of a random sample of NFIB's member firms, surveyed through 07/31/17)

Small Business Optimism Index



Overview

The Index of Small Business Optimism rose 1.6 points to 105.2, preserving the surge in optimism that started the day after the election. Seven of the 10 Index components posted a gain, two declined, and one was unchanged. Since the recession, the Index peaked at 105.9 in January, just 0.7 points above the July reading. Main Street was buoyed by stronger customer demand despite the dysfunction in Washington, D.C. The economy (GDP) grew about 2 percent in the first half of the year, nothing special, but the second quarter was much stronger than the first, and consumer spending was a major contributor to growth. The stock market continues to post record high readings, although a bit inconsistent with moderate growth in output from the nation's business sector.

Labor market indicators surged to near-record levels and owners reported strong net hiring over the past few months. Reports of job openings hit a 16-year record high and reports of increases in compensation remained at historically high levels. The frequency of reported price increases was the highest since 2014, but

still historically low. Inventory investment plans strengthened supported by stronger consumer spending. Reports of capital outlays were unchanged and plans to spend faded a little. Capital investment is still not supportive of stronger economic growth. Expectations for improved business conditions and higher real sales posted strong gains, anticipating a stronger second half economy.

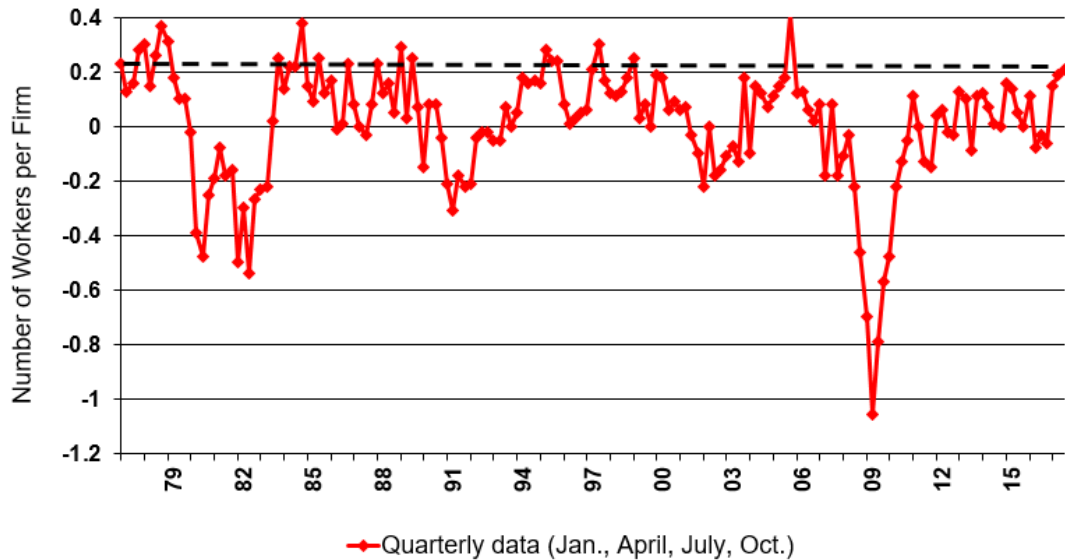
Small Business Optimism and Ten Components

Index and Components	July	Change	Share of Change
Job Creation Plans	19% (net)	4	21%
Capital Expenditure Plans	28%	-2	-10%
Inventory Plans	5% (net)	1	5%
Job Openings	35%	5	26%
Inventory Satisfaction	-2% (net)	1	5%
Good Time to Expand	23%	2	10%
Expect Better Business Conditions	37% (net)	4	21%
Sales Expectations	22% (net)	5	26%
Expect Easier Credit Conditions	-4% (net)	-1	-5%
Actual Earnings Trends	-10% (net)	0	0%
Index of Small Business Optimism	105.2	+19	100%

[Column 1 is the current reading, column 2 the change from the prior month, column 3 the percent of the total change in the Index accounted for by each component; “*” means the percent <0.5% or not a meaningful calculation. Index is based to the average value in 1986, components are not. The term “net” means that the percent of owners giving an unfavorable answer has been subtracted from the percent of owners giving a positive or favorable response. For some questions, there is no “unfavorable” response category]

LABOR MARKETS

Average Change in Employment Per Firm

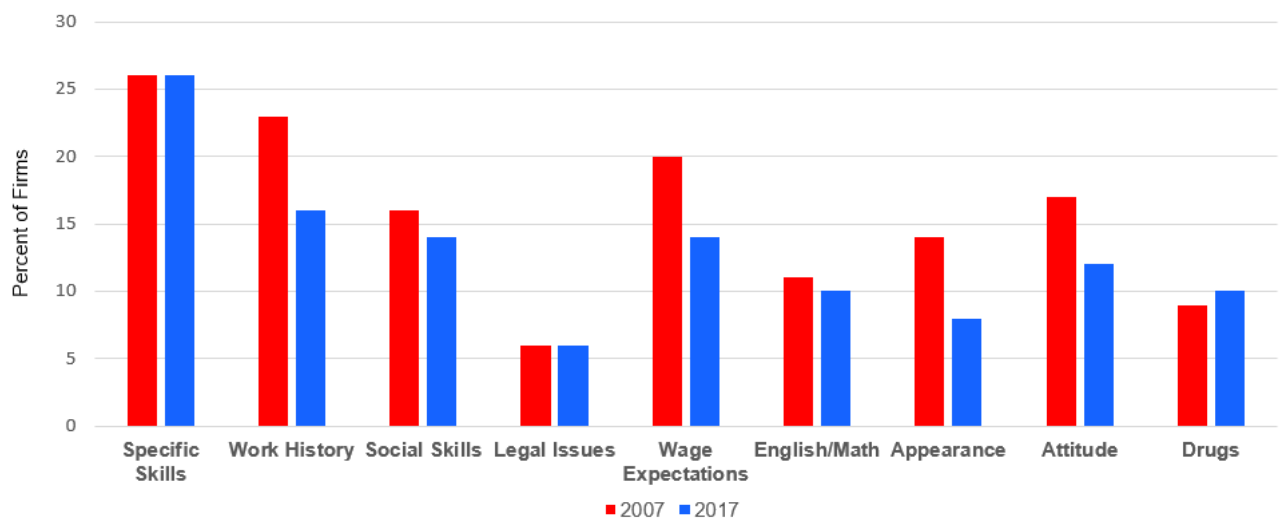


Small business owners reported an adjusted average employment change per firm of 0.21 workers per firm over the past few months, a solid performance. Thirteen percent (up 3 points) reported increasing employment an average of 4.5 workers per firm and 11 percent (unchanged) reported reducing employment an average of 1.6 workers per firm (seasonally adjusted).

Sixty percent reported hiring or trying to hire (up 6 points), but 52 percent (87 percent of those hiring or trying to hire) reported few or no qualified applicants for the positions they were trying to fill. Nineteen percent of owners cited the difficulty of finding qualified workers as their Single Most Important Business Problem (up 4 points), second only to taxes. This is a particularly severe problem in construction (28 percent) and manufacturing (21 percent) where labor shortages are the top problem, trumping taxes and regulatory costs.

According to a recent NFIB small employer survey, the most “typical” reason for “disqualification” of an applicant was a lack of specific job skills (cited by 26 percent of employers), followed by a poor work history (16 percent). Poor English and math skills typically disqualified 10 percent of the applicants. A lack of social skills disqualified 14 percent, unreasonable wage expectations 14 percent, attitude 12 percent, and appearance 8 percent, all factors that the applicant could easily improve without additional training if they really wanted a job. Drug issues were a typical reason for disqualification for 10 percent of the owners and legal status for 6 percent.

Typical Reasons Applicants “Not Qualified”

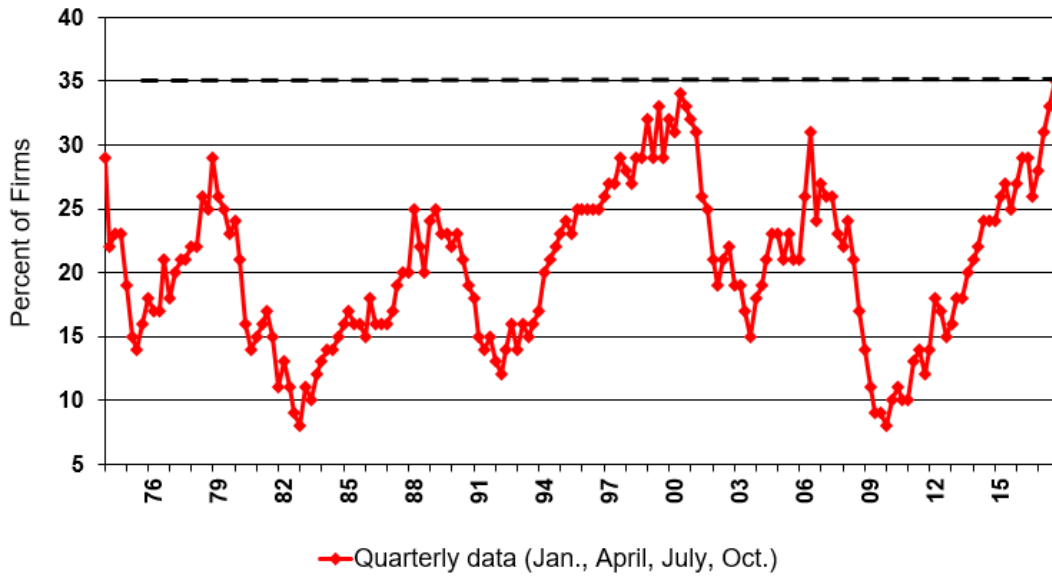


*Wade, Holly, *Job Openings*, NFIB Research Center, Vol 13, Issue 6, 2017.

Thirty-five percent of all owners reported job openings they could not fill in the current period, up 5 points, the highest reading since November 2001. Fourteen percent reported using temporary workers, up 3 points. Reports of job openings were most frequent in construction (48 percent), manufacturing (40 percent) and non-professional services (38 percent). Openings for “unskilled” workers were most frequent in manufacturing (16 percent), and the retail and wholesale trades (17 percent each).

Unfilled Job Openings

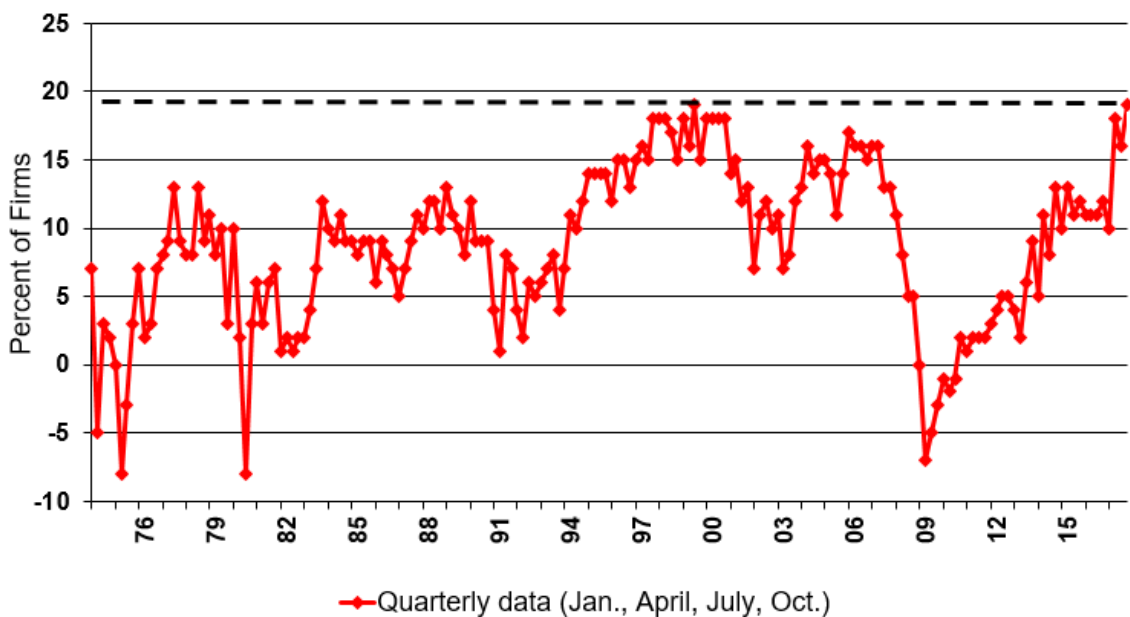
Percent with at Least One Unfilled Opening



A seasonally adjusted net 19 percent plan to create new jobs, up 4 points, with higher levels not seen since December 1999. Not seasonally adjusted, 21 percent plan to increase employment at their firm (up 1 point) and 5 percent plan reductions (up 1 point).

Job Creation Plans

Net Percent (“Increase” minus “Decrease”) in Next Three Months



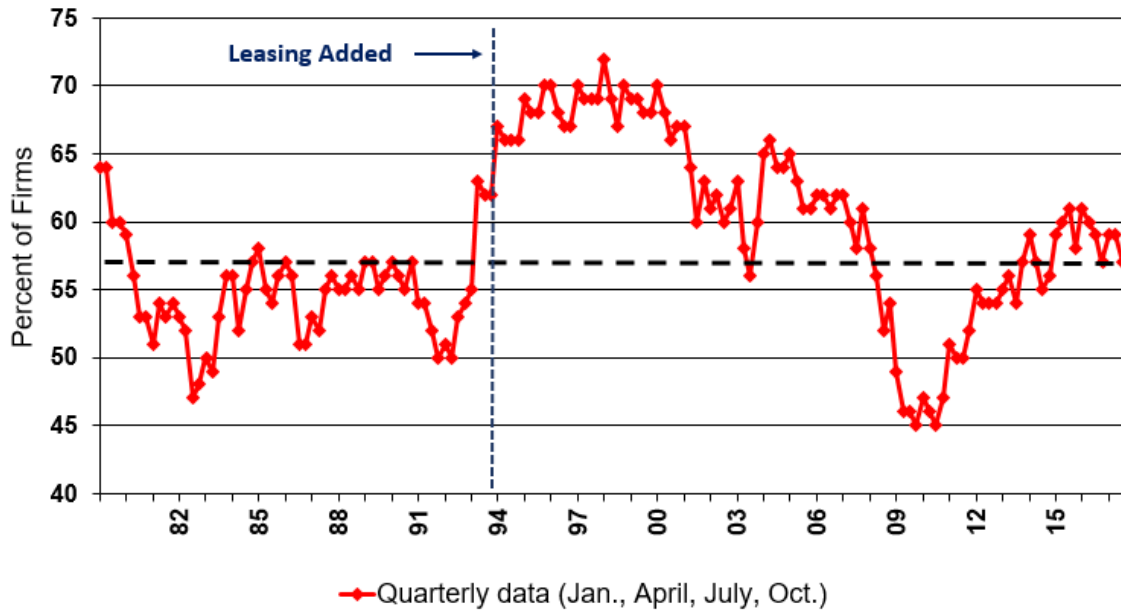
Hiring plans were strongest by far in construction and manufacturing where job openings are most frequent. Residential construction growth was not strong in the second quarter, due in part to a shortage of labor. The supply of new homes cannot keep up with demand and house prices are rising much faster than the inflation rate.

CAPITAL SPENDING

Fifty-seven percent reported capital outlays, unchanged. Of those making expenditures, 38 percent reported spending on new equipment (down 2 points), 24 percent acquired vehicles (up 3 points), and 17 percent improved or expanded facilities (up 4 points). Five percent acquired new buildings or land for expansion (up 1 point) and 13 percent spent money for new fixtures and furniture (up 2 points). There is still little evidence that capital spending, which raises worker productivity, is going to increase its contribution to growth anytime soon.

Actual Capital Outlays

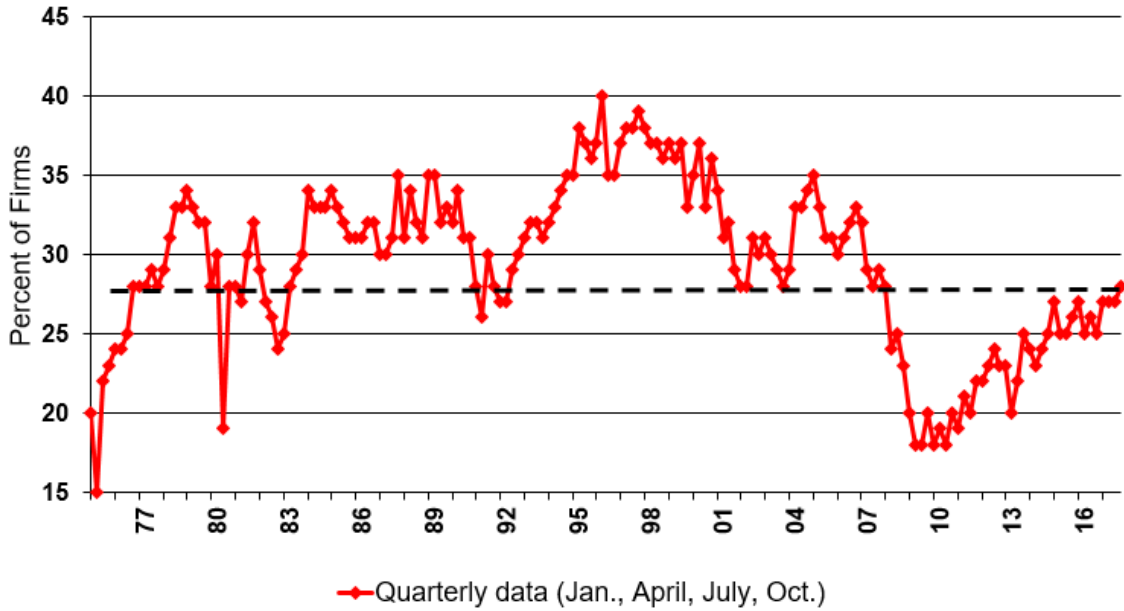
Percent Making a Capital Expenditure During the Last Six Months



Perhaps the decline in reported capital outlays will be reversed in the coming months as the percent of owners planning capital outlays in the next 3 to 6 months fell 2 points to 28 percent, still one of the strongest reading since 2007.

Planned Capital Outlays

Percent Planning to Make a Capital Expenditure in the Last Six Months

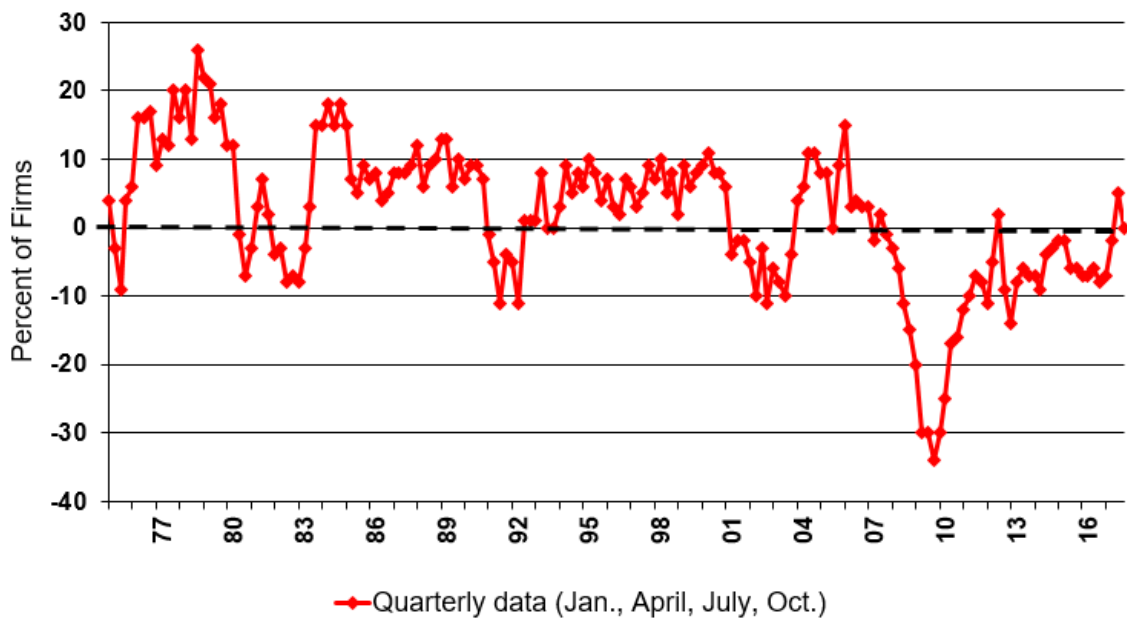


SALES

The net percent of all owners (seasonally adjusted) reporting higher nominal sales in the past three months compared to the prior three months was a net 0 percent, a 4-point improvement over June.

Actual Sales Changes

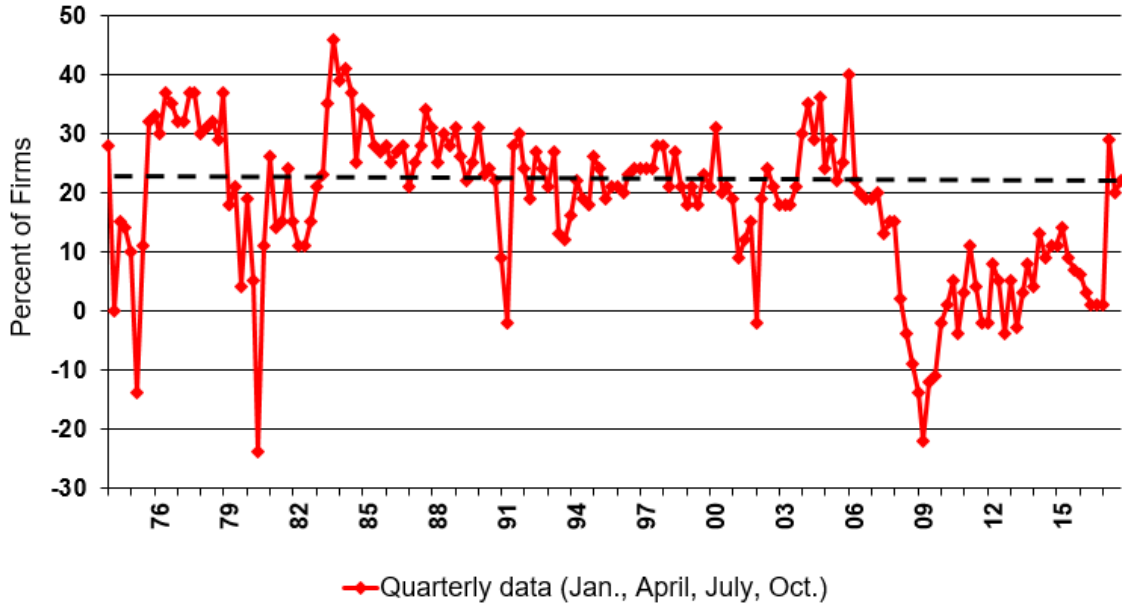
Net Percent ("Higher" minus "Lower") the Last Three Months Compared to the Prior Three Months



Seasonally adjusted, the net percent of owners expecting higher real sales volumes gained 5 points, increasing to a net 22 percent of owners. Stronger sales expectations are very supportive of the record hiring plans and strong inventory investment plans recorded in July.

Sales Expectations

Net Percent (“Higher” minus “Lower”) in the Next Three Months



INVENTORIES:

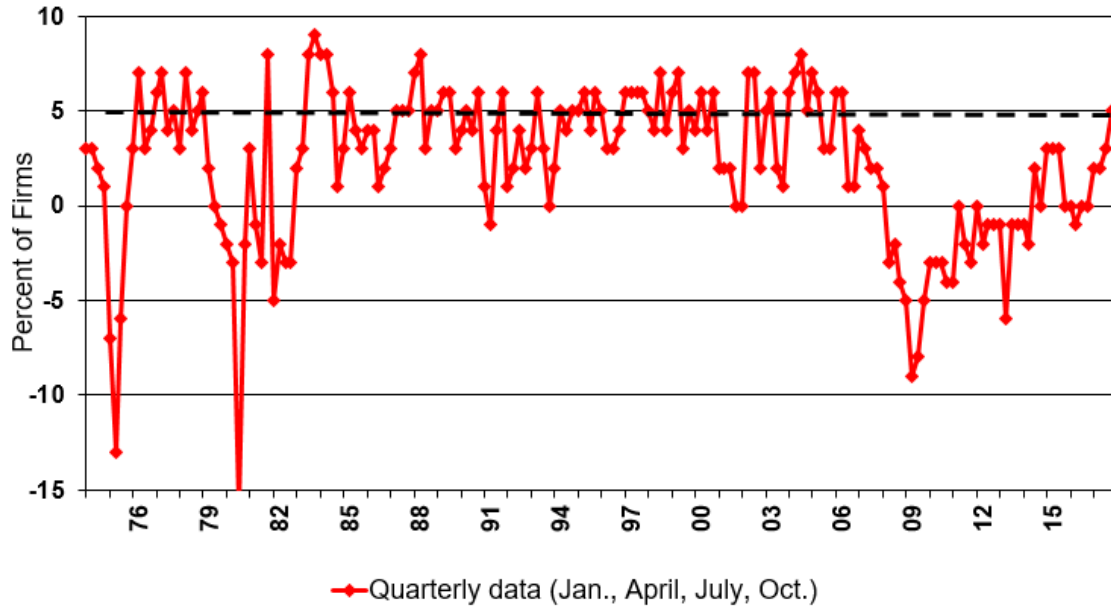
The net percent of owners reporting net inventory increases gained 4 points to a net 1 percent (seasonally adjusted), reversing months of inventory stock reductions that were generated by solid consumer spending in the second quarter.

The net percent of owners viewing current inventory stocks as “too low” improved 1 point to a net negative 2 percent, as sales expectations changed for the better, requiring higher inventory stocks.

The net percent of owners planning to add to inventory rose 1 point to a net 5 percent, the highest reading this year to date and historically normal for a growing economy. This is a positive indicator for second half growth, consistent with the improvement in real sales expectations and future business conditions.

Inventory Investment Plans

Net Percent (“Increase” minus “Decrease”) in the Next Three to Six Months

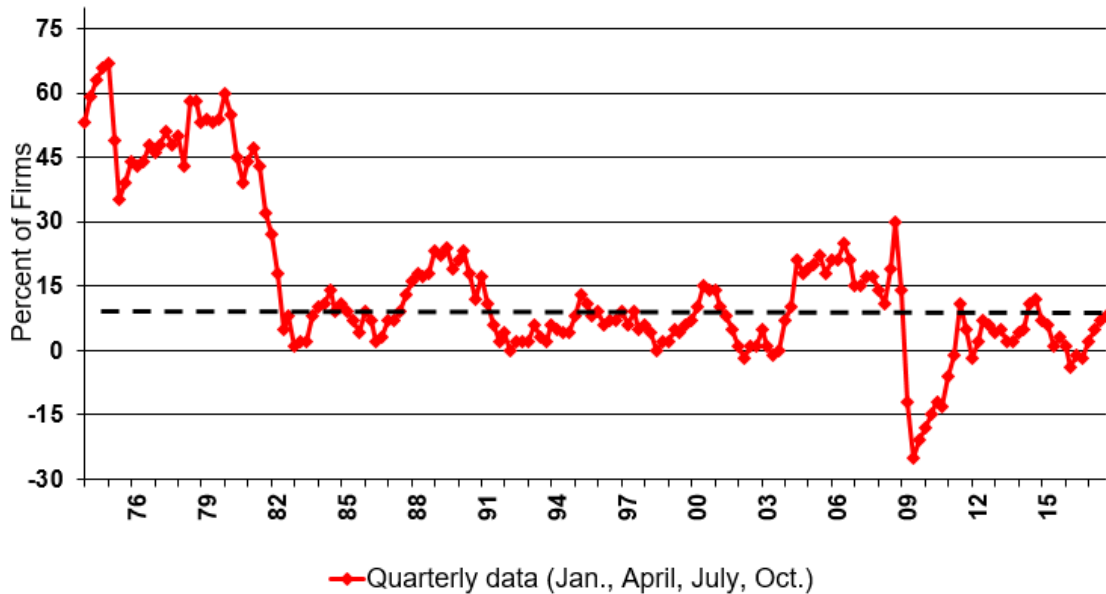


INFLATION:

The net percent of owners raising average selling prices posted a 7-point increase, rising to a net 8 percent of all firms, and erasing the dramatic decline posted in June. This is the highest reading since 2014, good news for the Federal Reserve which is trying to generate more inflation. Nine percent of owners reported reducing their average selling prices in the past three months (down 2 points) and 18 percent reported price increases (up 4 points).

Actual Price Increases

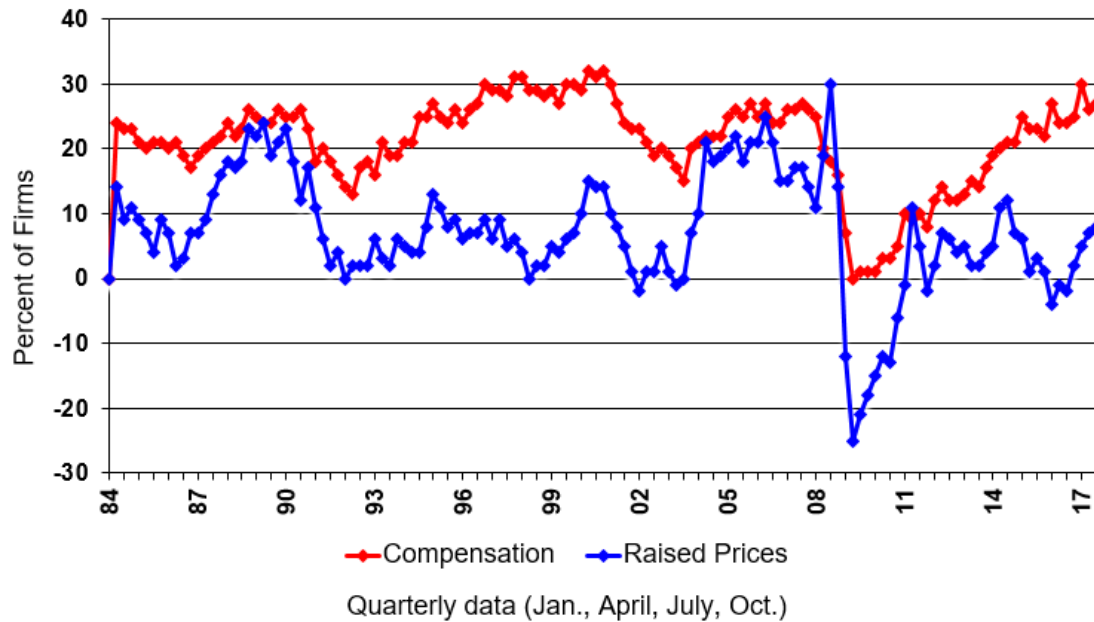
Net Percent (“Higher” Minus “Lower”)
Compared to Three Months Ago
(Seasonally Adjusted)



Seasonally adjusted, a net 23 percent plan price hikes (up 4 points). If expectations for sales volumes are realized, some of the price hikes may stick. That said, the Federal Reserve should be delighted that inflation remains well below 2 percent as the economy continues to grow. There is nothing “magic” about a 2 percent inflation target and efforts to create more inflation as a matter of policy invites real danger to economic stability.

Changes in Prices and Labor Compensation

Net Percent (“Higher” minus “Lower”) Compared to Three Months Ago



COMPENSATION AND EARNINGS:

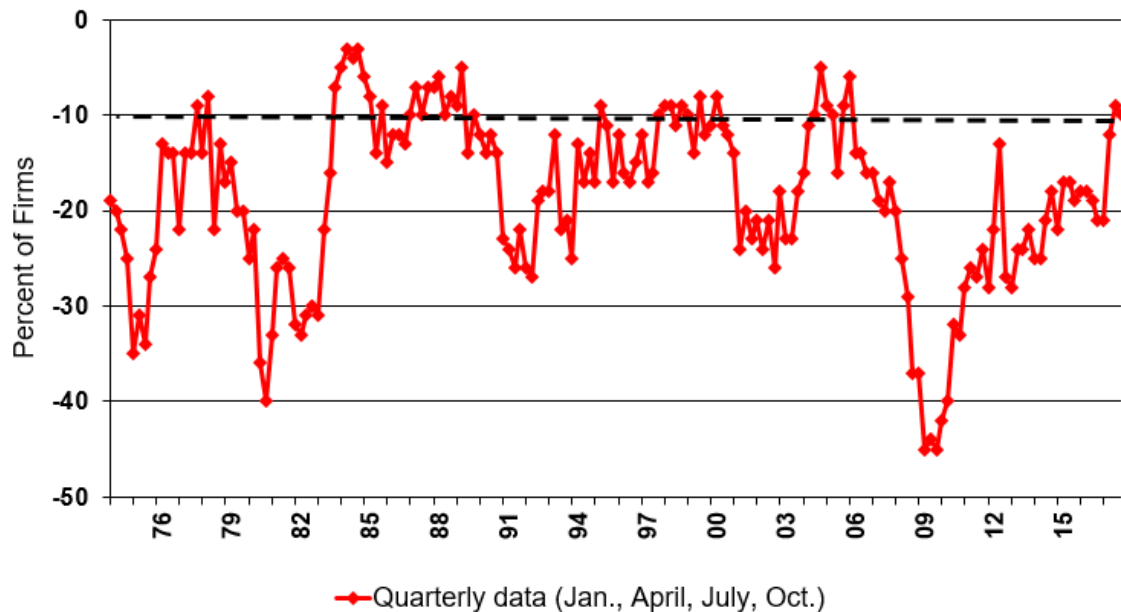
While inflation remains low, reports of higher worker compensation continue to be strong, consistent with historically tight labor markets. Reports of increased compensation rose 3 points to a net 27 percent. The Federal Reserve is hoping this will result in inflation as owners pass these costs on in the form of higher selling prices.

Owners complain at record rates of labor quality issues, with 87 percent of those hiring or trying to hire reporting few or no qualified applicants for their open positions. A record 19 percent selected “finding qualified labor” as their single most important business problem, far more than cite weak sales. Levels this high were last seen at the end of the last expansion in 2000. There is little that government policy can do to deal with this problem short of freeing up the educational system to innovate and respond to market needs. Rising compensation will attract workers back into the labor force, but it is a slow process.

The frequency of reports of improved profit trends was unchanged at a net negative 10 percent reporting quarter on quarter profit improvements, historically an excellent reading and one of the best readings in this expansion. In spite of rising labor costs, owners are seeing decent bottom line performance.

Actual Earnings Changes

Net Percent (“Higher” minus “Lower”) the Last Three Months Compared to the Prior Three Months



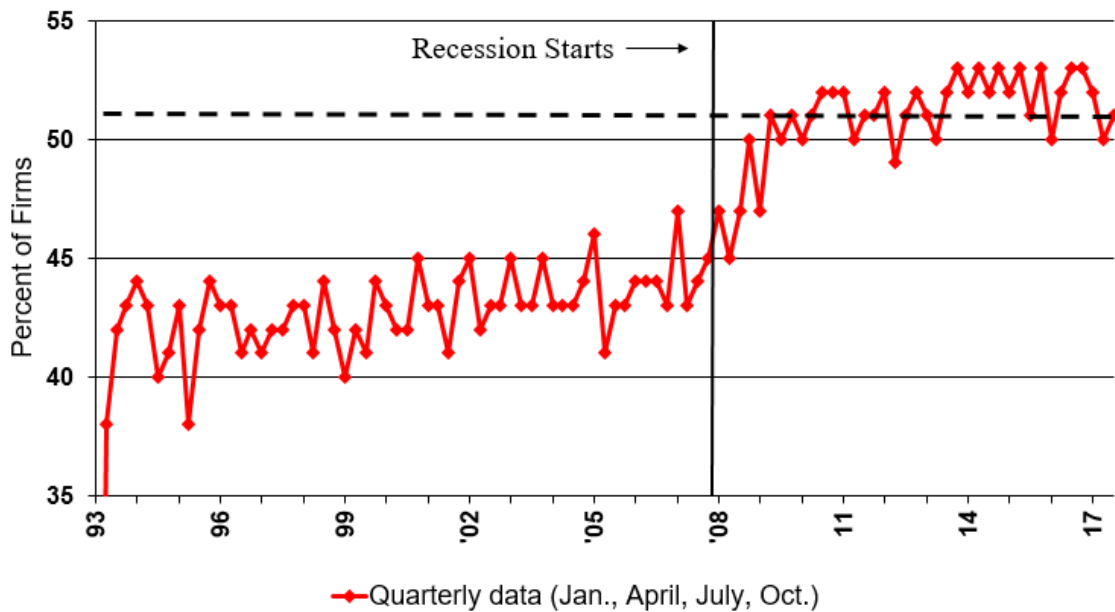
CREDIT MARKETS:

Three percent of owners reported that all their borrowing needs were not satisfied, down 1 point and historically very low. Thirty-one percent reported all credit needs met (up 4 points) and 51 percent explicitly said they were not interested in a loan, down 3 points. Including those who did not answer the question, 66 percent of owners have no interest in borrowing, down 3 points. Only 2 percent reported that financing was their top business problem compared to 21 percent citing taxes. Sixteen percent citing regulations and red tape, and 19 percent the availability of qualified labor. Weak sales garnered 8 percent of the vote.

Thirty percent of all owners reported borrowing on a regular basis (up 3 points). The average rate paid on short maturity loans was up 30 basis points at 5.9 percent. Overall, loan demand remains historically weak, even with cheap money. Small businesses have been restructuring over the past ten years and

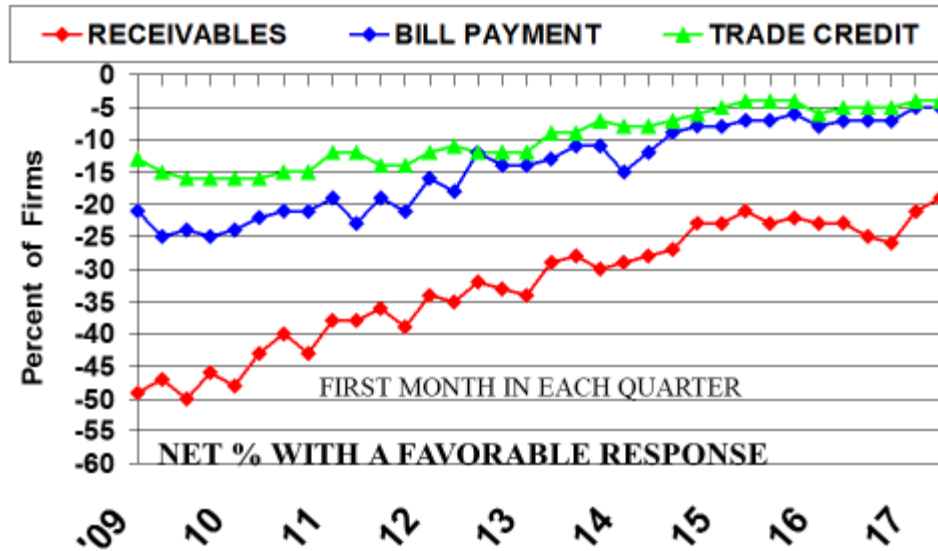
profit trends are now at historically good levels. Owners are in a good position to borrow again once they have a good reason to do so.

Percent of All Firms Not Wanting a Loan



General indicators of credit market conditions show continued gradual improvement. Owners report improving success in collecting receivables. They also report paying their own bills at a faster pace and trade credit is increasingly available.

BILL PAYMENT, RECEIVABLES COLLECTION AND TRADE CREDIT



The net percent of owners expecting credit conditions to ease in the coming months deteriorated 1 point to a net negative 4 percent, not much change in recent months. Lenders will appreciate higher yields on loans, but loan rates will have little impact on the decisions of owners to “take the plunge” once economic conditions and policies change convincingly. Hopefully the Federal Reserve will surrender control of interest rates to markets and not the whims of social policy engineers.

THE LARGER PERSPECTIVE:

It appears that the Federal Reserve will stay on course, with a likely announcement about shrinking their portfolio in September and another 25 basis point increase in rates in December. Neither of these moves will have a major impact on owners, interest rates are still low, and lenders are more comfortable making loans now that we have left the “0 floor” behind.

Second quarter GDP growth came in at 2.6 percent. However, this is the first estimate from the Bureau of Economic Analysis, two revisions are yet to come. First quarter GDP was revised down to 1.2 percent. Consumers spent more, but residential investment weakened, and capital spending did not add to the growth. Inflation measures were lower in Q2, not good news for the Federal Reserve but they should be pleased that inflation has remained so low.

Although no progress has been made on health care or tax reform, many important changes have occurred to the regulatory structure with few if any new rules showing up in the Congressional Register. These changes will seep into the regulatory structure with little fanfare, but will have significant impacts on regulation costs paid by small businesses going forward.

Apparently economic activity in the second quarter was good enough to divert owner attention from the impotence of Washington lawmakers. There's nothing like more customers to make owners happy, and optimism held up as did important measures of spending and hiring plans. Congress still holds the key to faster growth, so let's hope they open the door.

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NFIB began surveys of its membership in October 1973. Surveys were conducted in the first month of each quarter through 1985 when monthly surveys were instituted. The first month in each quarter is based on between 1,200 and 2,000 respondents, while the following two monthly surveys contain between 400 and 900 respondents. The term "net percent" means that the percent of owners giving an unfavorable response has been subtracted from the percent giving a favorable response. If, for example, 20 percent reported that they were going to increase the number of workers at the firm and 5 percent reported an intention to reduce the number of workers, the "net percent" would be 20 percent – 5 percent or a net 15 percent planning to expand employment. These figures are seasonally adjusted unless noted. The graphs show quarterly data (first survey month in each quarter), updated when available by subsequent monthly surveys.