

Economic Indicator — August 13, 2024

Small Business Optimism On the Upswing

Greater Sales Expectations Lift Outlooks in July

Summary

Outlooks Brighter, but Fed Cuts Still Incoming

The NFIB Small Business Optimism Index rose to 93.7 in July, its highest reading since February 2022. It's hard to mistake this four-month string of upticks for anything other than a trend improvement in sentiment. Although the index remains below its 50-year average of 98, the outlook for business conditions shot up 18 points in July, driven by brighter sales expectations. Yet, the underlying details continue to reveal hesitancy about the demand outlook amid a cloudy economic and political landscape. The clearest takeaways from July's survey are vital for the Fed: labor demand continues to ease and price pressures continue to fade. These soft elements of the survey measures, in concert with hard data on inflation and nonfarm payrolls, support our view that the Federal Reserve will begin cutting its policy rate next month at the September meeting.

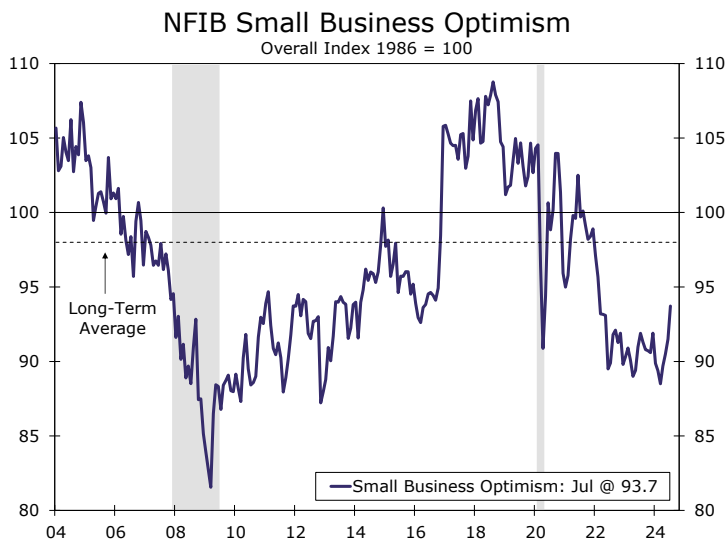
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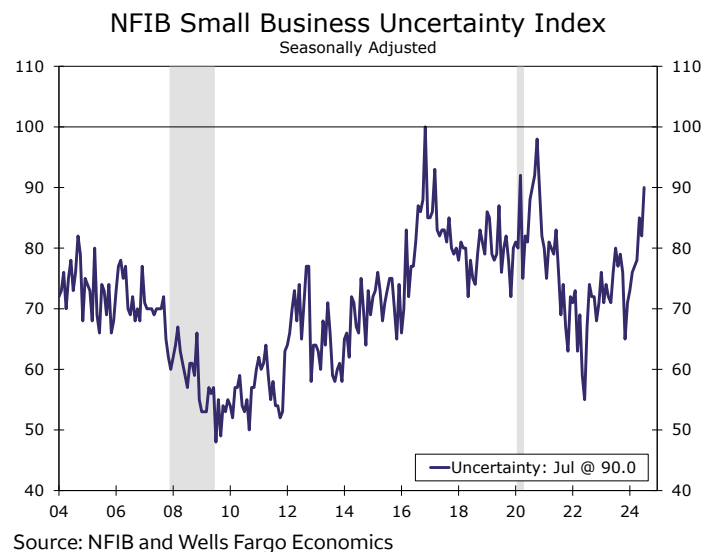
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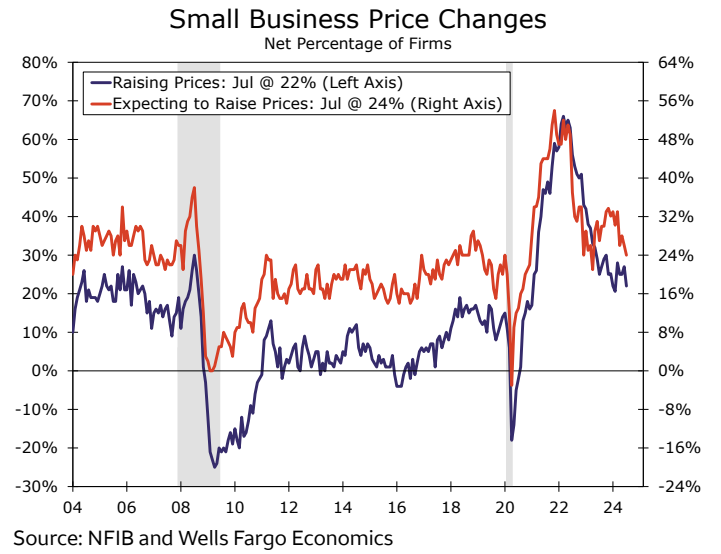
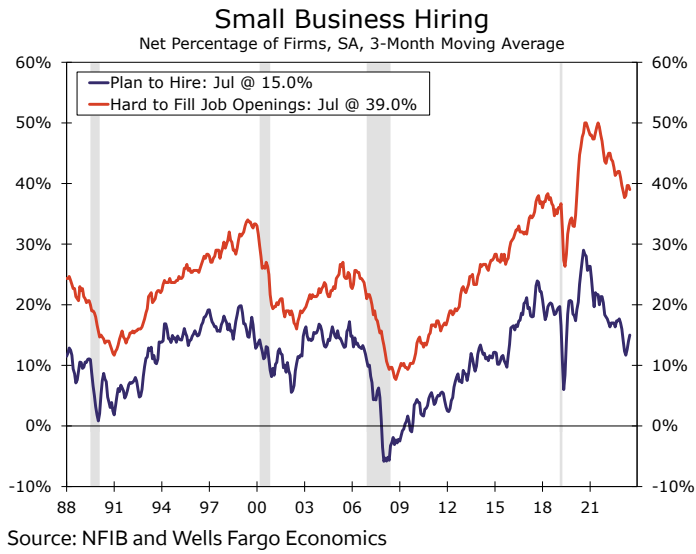


Source: NFIB and Wells Fargo Economics

How Do You Really Feel?

- The NFIB Small Business Optimism Index rose for the fourth consecutive month in July, indicating brightening perceptions among small business owners. At 93.7, the index is sitting at its highest reading since February 2022.
- July's improvement appears owed to a jump in sentiment surrounding the economic outlook. Although views were negative on balance (-7% on net), the portion of firms expecting business conditions to improve shot up 18 points in July to its best reading in over three and a half years.
- July's NFIB survey divulged more clues about the path of inflation, which appears firmly set on a downward trajectory. Inflation remained the top concern for small business owners. However, the share of respondents planning price hikes over the coming months fell to a net 24%, the lowest figure since April 2023. Although the percentage of firms raising prices remained elevated compared to pre-pandemic levels, it similarly dropped five points over the month to a net 22%.
- Meanwhile, labor demand remains in retreat. Despite a one-point uptick in July, the net percent of small businesses with outstanding job openings continued to decline on trend. Hiring plans have not budged for three months. Weakness in these “soft” employment measures combined with the recent softening in “hard” inflation and nonfarm payroll data support our expectation for the Federal Reserve's easing cycle to begin in September.
- Looking past the headline improvement in optimism, the details of July's survey paint a more muddled picture about economic perceptions. First, the uncertainty index jumped to its highest point since November 2020, likely driven by the upcoming presidential election.
- The sublines similarly reveal mixed messages. For example, favorable sales expectations lifted overall optimism in July. The percentage of firms expecting higher sales volumes over the next three months, although still a net negative, rose four points to its highest reading this year. Concurrently, reports of greater actual sales *fell* four points to its lowest reading this year.
- Firms' inventory management decisions also suggest a cloudy demand outlook. The portion of small businesses adding to their inventories dropped six points to a net -9%, the lowest reading since August 2020. Yet, net plans to expand inventories registered its first positive reading in nearly two years.





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