

Economic Indicator — September 14, 2021

Small Business Optimism Edges Higher in August

Summary

Small business confidence rose 0.4 points to 100.1 in August, as five of the ten components of the NFIB Optimism Index improved during the month. The proportion of business owners planning to increase employment and inventories both rose by five points, while the proportion of small firms planning to boost capital spending rose four points to a net 30%. At first glance, the rise in small business confidence seems at odds with other data reported for August, which noted economic conditions were weakening. Small business owners see this trend as well, with the proportion of firms expecting the economy to improve during the next six months falling eight points to a net -28%.

This past month's rise in small business confidence has more to do with the certainty owners now see in taking defensive measures. Labor shortages, supply chains bottlenecks and higher prices are expected to be at least a semipermanent part of the economic landscape, hence the rising share of firms boosting inventories at a time when a majority of business owners feel economic growth will slow. Business owners are also hoarding labor whenever possible, as 50% of owners report they have job openings that could not be filled, an increase of one percentage point from July and a 48-year record high for the second month in a row.

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NFIB Optimism Index Improves in August

Small business confidence edged 0.4 points higher to a historically healthy 100.1 in August. Business owners still see a very challenging road ahead, however, with the proportion of firms expecting economic conditions to improve over the next six months tumbling eight points this past month to a net -28%. Business owners remain frustrated by the inability to hire the workers they need. Supply chain constraints are another major source of frustration, with 37% of firms reporting that supply chain disruptions had a significant impact on their businesses. Another 29% reported that disruptions have had a moderate impact. Rising material prices are an often-cited issue as well, but so far businesses have been able to pass their higher costs onto their customers. Once consumers become more price sensitive, however, earnings will get squeezed, which is one reason firms are stocking up ahead of future price increases while also investing more in equipment so that they can automate tasks and reduce the need for labor over the long term.

The latest read on small business optimism suggests a large proportion of business owners feel that supply chain shortages, hiring difficulty and rising prices are likely to persist for quite some time. Plans to increase inventories, staffing and capital outlays when a majority of business owners expect growth to slow suggest these moves are defensive in nature, designed to protect market share and profit margins. Owners are also striving to keep a step ahead of rising raw material prices and shortages.

Small businesses are still struggling to find workers. The share of owners who reported having a job opening that they could not fill rose to 50% in August, another record high. Pandemic-related constraints, such as childcare, COVID concerns, enhanced unemployment benefits and early retirements, have pressured labor availability for months. Some business owners may see some relief now that expanded unemployment benefits have ended. That said, other constraints on labor show little signs of easing and are likely to persist. Nationally, the labor force participation rate has not materially improved for much of this year, suggesting that employers are having a difficult time pulling workers off the sidelines.

Finding qualified applicants remains a problem as well. Ninety-one percent of small employers who were trying to hire in August reported having few or no "qualified" applicants. In addition, 28% of owners cited labor quality as their top business problem, up two points from July. Compensation plans have ramped up as a result, as owners are raising wages in an attempt to attract workers. The share of owners actually raising compensation rose to 41% in August, another NFIB record high, creating inflationary pressures. Hiring challenges are likely to persist over the next few months. The Delta wave has reignited worker health concerns, pushed the return to office out further and raised uncertainty around in-person schooling.

NFIB Small Business Optimism

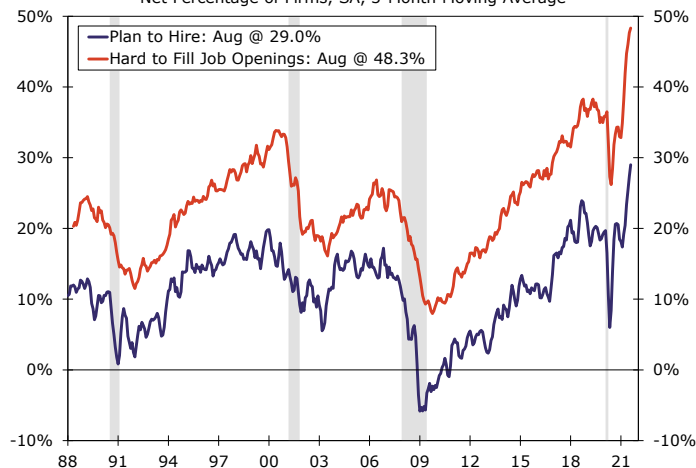
Overall Index 1986 = 100



Source: NFIB and Wells Fargo Securities

Small Business Hiring

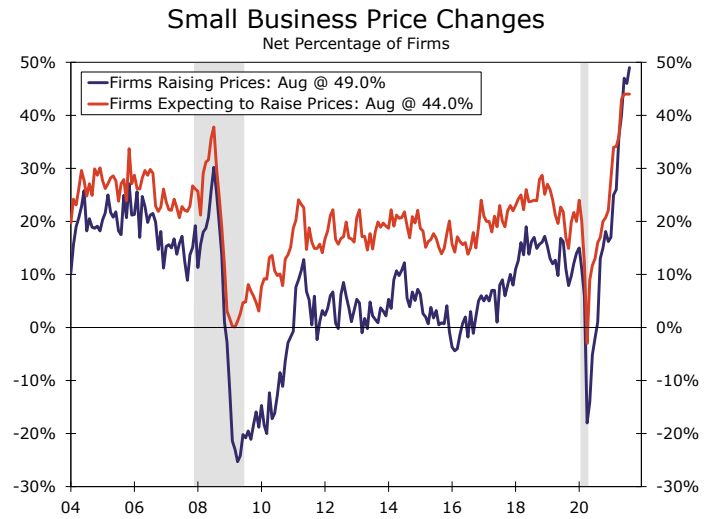
Net Percentage of Firms, SA, 3-Month Moving Average



Source: NFIB and Wells Fargo Securities

A rising share of small business owners see inflationary pressures as widespread and more likely to persist. The net share of business owners raising their average selling prices rose three points in August to 49%. Price hikes were most prevalent at the wholesale level, where 68% reported raising prices and 0% reported lowering them. Among manufacturers, 60% reported raising prices, while 2% reported lowering them. And at the retail level, 52% reported raising prices, while just 4% lowered them. The prevalence of price increases contrasts with reports that prices increases have been limited to only a few items. Typically, when prices gains are more widespread, they tend to also be more persistent.

Inflationary pressures are likely to remain. The net share of small business owners expecting to raise prices in the next three months remained unchanged at 44% in August and has maintained that high level for the past three months. This series has provided a reliable prediction of future inflationary trends and suggests inflation is likely to remain near its current pace for at least the next few months.



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