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Notes from the Economics Desk

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Small Business Animal Spirits

The business sector has generally interpreted the November election results as a positive for the economic outlook. Small businesses seem particularly excited, as the NFIB monthly survey of small business economic trends recorded a sharp uptick in optimism in November. Though executives may take some time to actually ramp up their operations as they await the details of forthcoming tax and regulatory changes, the details of the November NFIB survey results bode well for capital investment over the medium term.

NFIB Survey

Since the 1970s, the National Federation of Independent Business, a trade group representing small and independent firms, has conducted a monthly survey of its members to gauge general attitudes as well as plans for their own operations. The poll typically receives around 500 to 600 responses most months, and larger surveys, conducted once a quarter, can return 1,200 to 1,500 responses. This exercise has proven to be a valuable source of intelligence regarding the attitudes of business.

General Economic Outlook

In November, small business optimism surged. The headline NFIB index jumped by 8 points to 101.7, the best reading by far since 2021 (see Chart 1). This reaction to the election of Donald Trump as President was remarkably similar to the response in 2016, when the gauge jumped by almost 11 points combined in November and December. The text of the November 2024 report cited a “major shift in economic policy, particularly for tax and regulation policies, that favor economic growth.”

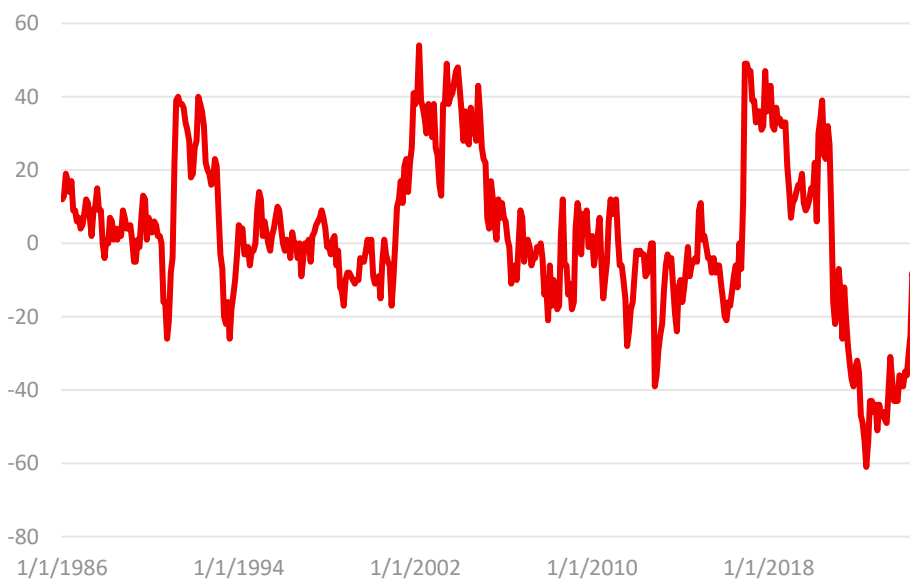
Chart 1: NFIB Optimism Index



Source: NFIB.

Respondents' outlook for general business conditions swung positively in a particularly violent manner last month. As Chart 2 shows, this gauge was easily at its historical lows for most of the post-pandemic period but began to move higher this summer and surged by 41 points in November to +36, one of the higher readings in the history of the series. Similarly, in the wake of the 2016 election, this gauge jumped by 56 points over two months, nearly ascending to an all-time record high.

Chart 2: Outlook for General Business Conditions



Source: NFIB.

Business Plans

A jump in optimism is nice, but it is more important to know what respondents are planning for their own firms. Across all of the key parameters, small business owners indicated in November that they intend to be more aggressive over the next six months.

Hiring plans inched up modestly in November, rising by 3 points to +18, reversing, at least for now, the steady moderating trend that had been in place since the height of the post-pandemic labor shortage in 2021-2022 (see Chart 3).

Chart 3: Hiring Plans



Source: *NFIB*.

Moreover, respondents intend to sweeten their wage offers to increase their headcount. The compensation plans measure rose by five points in November to +27, the highest reading in nearly a year (see Chart 4). In fact, while the November reading was well below the peak levels post-pandemic, it was higher than at any time in the history of the series (going back to 1986) through mid-2021.

Chart 4: Compensation Plans



Source: NFIB.

Fed officials have discussed extensively in recent months that their business contacts have been telling them that consumers are becoming more price-sensitive, eroding firms' pricing power. However, the NFIB gauge of price plans for the next six months arrested the moderating trend that had been in place and ticked up in November by two points to +28 (see Chart 5). That level is far below the post-pandemic peak but is still well above the prevailing level for much of the past 40 years.

Chart 5: Price Plans



Source: NFIB.

Finally, and perhaps most importantly for assessing economic prospects, small businesses are ramping up their capital spending plans over the next three to six months. This measure jumped by six points in November to the highest level since early 2022, when the economy was still normalizing after the COVID lockdowns (see Chart 6).

Chart 6: Capital Expenditure Plans



Source: NFIB.

Conclusion

The NFIB small business survey results for November suggest that small businesses are poised to ramp up activity in the months ahead. The heightened optimism may or may not translate into a sizable jump in economic activity, but I believe that more widespread intentions to invest, in particular, bode well for the economic outlook. As the text of the report indicates, a key factor in the response by small business executives to the election is an aspect of government policy that tends to often be overlooked because it is difficult to quantify. The tone of the regulatory landscape is absolutely critical in establishing a favorable environment for firms to invest. When executives have confidence that their businesses will be treated well, they are more likely to undertake large projects. In contrast, when there is uncertainty regarding the prospects for the future (for example, if there is concern that an unexpected regulatory decision could render a capital spending initiative unprofitable), decisionmakers tend to take a more cautious approach.

This dynamic, however, can work in both directions as it relates to the policies of the incoming Trump Administration. While, as the NFIB report indicates, expectations regarding tax and regulatory policy have buoyed attitudes, upcoming tariff hikes could work to dampen moods. In fact, in President Trump's previous term, once the Administration began imposing tariffs in 2018, the NFIB small business optimism index started to slip, and the resulting uncertainty led to a cooling in business investment gains. In my view, it was not so much the tariffs themselves that had a negative impact on the economy in 2018 and 2019. Instead, the widespread uncertainty about what industries might be next for tariff hikes or might get caught up in a retaliatory tit-for-tat move by one of the U.S.'s trading partners was the main impetus that led to a deterioration in the business investment environment.

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