

Key themes from the Treasury Business Liaison Programme — October 2005

Treasury officers met with over 40 companies and organisations in Sydney, Melbourne, Hobart and Launceston through the Business Liaison Programme in October 2005.¹

Retailers mostly report slower sales in the September quarter, particularly for discretionary items and especially at the lower end of the market. They suggested that this year's tax cuts have been mostly saved and attributed most of the slowdown to the recent increase in petrol prices.

Mining companies spoke of how they are expanding production and those manufacturers supplying the mining sector describe business conditions as very good.

Most businesses indicated that they plan to hire more workers. They still refer to widespread skill shortages, especially in regional and remote areas, but they say that shortages are not getting any worse. Despite the reports of skill shortages, businesses said that they are facing only a marginal acceleration in overall wages. Businesses continue to say that they have little pricing power. Wage increases are being variously met by productivity improvements, cuts in other costs, and modest reductions in profitability.

Treasury greatly appreciates the commitment of time and effort made by the Australian businesses and associations that participate in the Business Liaison Programme.²

1 A detailed explanation of the Treasury Business Liaison Programme is provided in the *Treasury Economic Roundup*, Spring 2001.

2 This summary of business conditions reported in liaison meetings reflects the views and opinions of participants. It is provided for the information of readers. While Treasury's evaluation of the economic outlook is informed by findings from business liaison, a much wider range of information and data are utilised to ensure a rigorous assessment of the Australian economy.

Retail trade

Most retailers report a slowing in sales, which became more pronounced from around mid-August. In contrast to the stimulus provided in 2004, this year's tax cuts appear to have been mostly saved. Accounts of a slowdown were not uniform. Food sales, and sales of essentials more generally, did not slow as much as more discretionary purchases. Smaller stores spoke of more difficulties than large stores.

The slowdown in retail sales is generally attributed to higher petrol prices. The volume of petrol bought has only contracted marginally, so this leaves fewer funds for other purchases. Furthermore, as petrol prices are highly visible, they were regarded as having a disproportionately large impact on consumer sentiment.

Retailers report that consumers seem to have concluded that high petrol prices were here to stay and preferences were moving towards smaller, more fuel-efficient cars. This was evident in orders for both sales and rentals of cars.

Some retailers again referred to the mild winter in much of the country, which reduced sales of some household appliances and seasonal clothing.

Production and investment

Manufacturing

Manufacturers supplying the mining industry were more confident than other manufacturers. Suppliers to the construction industry in Western Australia continue to report very strong conditions. Global demand for food is strong, leading to good conditions for Australian food manufacturers.

A number of manufacturers described their difficulty in competing with imports. A response of some companies was to move some of their own production facilities overseas. Some manufacturers related how they were increasing the proportion of components they source from overseas. Some manufacturers also told how they had successfully found niches in specialised goods where they have a technology lead.

Housing and construction

House prices are reported as having plateaued in most of the country, but to have fallen significantly in Sydney.

Housing construction has eased across the country, but the decline is only mild. Prospects are regarded as better in Melbourne than in Sydney as expansion in the

latter is hitting geographical restraints. There were reports of more homes being built at the upper end of the market.

Some contacts refer to a slowing in commercial construction. However, others cite falling office vacancy rates and changing preferences for types of offices as likely to support activity. Other building remains strong, most notably infrastructure projects such as expressways.

Mining

Mining companies continue to aspire to increase production. Accordingly, mining investment is strong. In some cases, companies regret that supply constraints are limiting their ability to expand production as much as they want. Shortages of large vehicles were mentioned, and even more commonly of the tyres required for them.

Tourism and education

Tourism operators described how cheaper airfares (and increasingly nationwide football competitions) had led to an upsurge in domestic tourism in recent years, but this effect has nearly run its course. Travel was expected to stay around the new high level (so long as petrol prices did not rise further) but not increase at previous rates. The immediate outlook for international tourism is clouded by concerns about security and health issues. In the medium term, administrative changes in China offer further scope to attract tourists from that market.

Universities report a tougher environment for attracting overseas students as Asian universities improve the quality of their faculties and facilities.

Employment

Most businesses interviewed expect at least to maintain employment around current levels. Reports continue of labour shortages for at least some categories of labour. The occupations most frequently mentioned as being in short supply include nurses, accountants, electricians, some kinds of engineers, professionals in the mining industry and truck drivers. There are also some accounts of semi-skilled or experienced unskilled labour being hard to find, particularly in more remote areas. Some businesses warn that large numbers of skilled and experienced workers were approaching retirement.

Companies, especially those with international operations, referred to bringing in workers from overseas to meet labour demands. Some large mining and construction companies are staggering projects so as to move teams from one site to another,

although as it is hard to do this smoothly, it often involves some delays to projects or temporary hoarding of labour.

Labour costs

Business contacts mentioned upward pressure on labour costs for occupations where labour is in short supply. But even in these areas, businesses were reluctant to raise wages, fearing it will just lead to matching offers by other employers. Overall, wages growth is steady with wage increases running at around 4 per cent. Many businesses reported that non-wage labour costs are rising faster than wages, especially in remote areas where better conditions are needed to attract workers.

Costs, prices and profits

Higher global oil prices have raised costs for many businesses, not just for transport but for other inputs such as packaging. Some companies have contracts allowing oil prices to be passed on, but most said they were likely to try to absorb the cost. Many retailers report much higher rents in large shopping malls. Many businesses say they had to match international product prices, regardless of domestic cost pressures.

Many contacts described how productivity increases from more efficient productive processes were sufficient to cover the increases in labour and other costs. Businesses which face volatile demand reported 'hoarding' labour during a temporary lull in sales for fear that when demand picks up they will not be able to rehire sufficient workers.

Regional economic conditions

As has been the case for some time, activity is particularly strong in south-east Queensland, driven by strong population growth. The strength of the resources sector is boosting Western Australia. New South Wales is weaker, which is generally attributed to the earlier and larger fall in house prices there, and ongoing problems with transport.

This business liaison round included meetings with Tasmanian businesses and organisations. After a period of slow growth in the 1990s, the Tasmanian economy has performed well in recent years. The boost to domestic tourism from cheaper airfares has been particularly helpful. As a result, there are a lot of investment projects aimed at expanding the capacity of the tourism industry. It has been noticed, however, that the week-long or longer tours that used to be the mainstay of Tasmanian tourism are being replaced by shorter breaks. There is some restructuring in the agricultural sector, such as away from wool and towards wine.