

Key themes from the Treasury Business Liaison Programme — December 2005 to March 2006

Treasury officers met with around 50 companies and organisations in Sydney, Melbourne, Canberra and Geelong through the Business Liaison Programme between December 2005 and March 2006.¹ The companies interviewed employ over 200,000 Australian residents and represent a broad cross section of Australian industry.

Sales are continuing at the more moderate pace established since late 2005, and appear quite sensitive to petrol price fluctuations, according to retailers. Most businesses report high levels of capacity utilisation, and some note that shortages of capital equipment are limiting their investment. Farmers have welcomed the recent rains.

Real estate agents report stable house prices, and this is improving affordability and the outlook for house builders. Other builders report that infrastructure projects are supporting activity.

While businesses continue to report skill shortages, they remain optimistic this will not lead to an acceleration in wages. A number of businesses are reporting significant cost increases but most are experiencing very competitive markets in which they can not raise prices.

Treasury remains greatly appreciative of the commitment of time and effort made by the Australian businesses, industry associations and government agencies 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 that sales have continued at the slower pace evident since the latter part of 2005. This slower pace is expected to continue, with retailers suggesting this is a return to normal conditions after some years when rising house prices led to unsustainable increases in household spending. In support of this argument, a number of retailers note that demand for luxury items has weakened noticeably, and strategies to address slower sales, including an increase in advertising, are being employed.

Retailers report that higher petrol prices are affecting consumers in a number of ways. Apart from greater expenditure on petrol crowding out spending on other goods and services, contacts suggest that the high visibility of petrol prices affects consumer sentiment and influences their purchasing decisions. Petrol price rises are also affecting shopping patterns with, for example, people making fewer trips to shopping malls, which in turn means they are making fewer impulse buys and eating fewer meals at malls.

Retailers comment that a warmer summer helped sales of some household appliances and seasonal clothing. Furthermore, a spate of major televised sporting events in 2006, such as the Winter Olympics, Commonwealth Games and the soccer World Cup, are regarded as improving sales of televisions and recorders, along with the ongoing price declines and improved features on much of this equipment.

Production and investment

Few businesses report substantial excess capacity. A key theme to emerge from discussions is how investment is currently directed to boosting productivity rather than increasing production. Some companies report that shortages of equipment are hampering their investment plans.

Manufacturing

Manufacturers supplying the mining industry continue to be more confident than other manufacturers. A number of manufacturers complain that the Australian dollar is excessively strong and hampering their international competitiveness.

Housing

Real estate agents report that house prices have plateaued in most of the country. There is optimism in Sydney that the period of falling house prices has ended, while there is a solid consensus that prices are still rising in Perth. In regional areas, house prices are unsurprisingly strongest in areas where population is growing rapidly.

There is also a belief that rising incomes and steady interest rates will translate into improved housing affordability.

Construction

Businesses noted that construction activity is strong. Furthermore, builders comment that infrastructure spending by state governments is particularly robust.

Mining

Australian mining companies report large expenditures to boost production. However, many miners regret that both internal and public infrastructure capacity and supply constraints are limiting their ability to expand production. In particular, world-wide shortages of large vehicles and other capital equipment are often mentioned. Firms are responding to the constraints by placing more emphasis on maintenance and methods of reducing wear on vehicles and other equipment.

Rural sector

Rural contacts, especially crop growers in the eastern states, are pleased with recent rains. A bumper wheat harvest is predicted for 2005-06 and beef producers are rebuilding herds.

Tourism

Tourism industry contacts described concerns about competitors in Asian markets who are benefiting from cheaper airfares in the region. This, they argue, is making trips to neighbouring countries more attractive than holidays in Australia. The Commonwealth Games are giving some boost to tourism.

High petrol prices are a concern to the domestic tourism industry although, as with retailing, good weather enjoyed over the summer contributed to sales.

Employment

Current employment levels are viewed as satisfactory by most businesses. Some report a continuing move to outsource non-core activities. Shortages remain for some categories of skilled labour, with the occupations most frequently mentioned including nurses and tradespeople in the mining and related industries. Reflecting the current strength in mining, there are also some reports of competition from the mining sector making it harder for businesses in other sectors to retain good semi-skilled or experienced unskilled labour. Some companies say that experienced managers are in

short supply and ageing, while fewer businesses report shortages of IT professionals than had been the case a year ago.

Increasingly, businesses, especially those with international operations, speak of bringing in workers from overseas (especially from related companies) to meet labour demands. Another response, described by some large mining and construction companies, is staggering projects as a way of overcoming skill shortages.

Labour costs

For those occupations where skills are in excess demand, businesses mention upward pressure on labour costs. But even in these areas, contacts say they are reluctant to offer higher wages to bid away workers, as this may just be matched by higher wage offers by their current employers. Overall wages growth is steady. Most non-wage labour costs are growing at similar rates to wages.

Costs, prices and profits

Businesses report that the rise in global oil prices has flowed through to freight charges and the prices of other materials such as plastics and polyesters. There have been steep rises in prices of some other raw materials such as cement and aluminium, but steel and timber prices have stabilised. Most contracts have not allowed these cost increases to be passed on, which is squeezing margins. Farmers report that they are facing increased costs for fertilisers and chemicals.

Regional economic conditions

As has been the case for some time, activity is particularly strong in Western Australia and Queensland, and weak in New South Wales.

This business liaison round included meetings in Geelong. Businesses in Geelong report generally strong conditions, with strong population growth supporting investment in the region.