Key themes from Treasury's Business Liaison Program

As part of Treasury's Business Liaison Program, staff met with over 30 organisations in Sydney, Melbourne, Brisbane and Perth during August 2009.[1] Treasury greatly appreciates the commitment of time and effort by the organisations that participate in the program.[2]

Conditions in the June quarter had surpassed expectations formed earlier in the year, although the improvement in many sectors was off a low base. Businesses remained cautious but noticeably more confident. The retail and mining sectors had experienced the strongest conditions which had in turn supported employment to a greater extent than in other sectors. Private non-residential building activity was identified as an area of continued weakness, with very little new work feeding into the pipeline.

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

2 This summary reflects the views and opinions of participants in the liaison program, which are not necessarily shared by Treasury. 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. Treasury aims to meet with a broad cross-section of the business community over time. Companies are invited to register their interest in participating.

Trading conditions

The retail sector had enjoyed a robust June quarter, benefiting from the significant monetary and fiscal stimulus. Grocery retailers, department stores and hardware stores reported sustained growth in sales, with recently reported annual results supporting the view that lower interest rates and stimulus payments had underpinned activity and confidence in the sector.

The growth in sales evident in the March and June quarters had been reversed to a small degree early in the September quarter. However, with the rebound in confidence since earlier in the year, most retailers were relatively optimistic about the second half of 2009. However, the impacts from winding back of fiscal stimulus were noted as generating some uncertainty in the near term.

Business to business suppliers reported that production activity had probably bottomed in the June quarter, with stronger sales recorded in July and August. There was also a noticeable surge in sales in the month of June relating to the temporary taxation measures encouraging investment in items of plant and equipment. Looking through the associated 'bring forward' in activity, contacts were relatively optimistic about a broadly based recovery in business demand being underway, albeit off a low base.

In aggregate, private construction activity had largely held its ground, although there were considerable sectoral and regional differences. Engineering construction and public works were the clear sources of strength with major projects, fiscal stimulus and state capital works combining to support activity. House building activity had also picked up, particularly at the lower priced end of the market, and apparently more so in Victoria than elsewhere. However, higher density dwelling construction and commercial property generally were experiencing the weakest conditions. Contacts reported expectations of continued declines in private construction work, with the mining and public sectors welcome sources of ongoing support.

The manufacturing sector was not yet exhibiting clear signs that the inventory cycle had turned, with production remaining well down from last year's levels. Contacts suggested that the retail supply chain had largely avoided significant de-stocking due to robust demand, and that weaker business spending might be responsible for the run down in inventories and weaker production and imports. Manufacturing activity levels had bottomed following steep falls, with several contacts believing that although the outlook was not particularly positive, the worst was now behind them.

Despite the fall in commodity prices, producers of Australia's key mineral and energy export commodities — coal, iron ore and LNG — reported sustained high levels of production and exports. Elsewhere in the mining sector, indications were that activity remained well below the peaks of mid 2008, though recent commodity price movements were seen as indicative that the one to two year outlook might be more positive than expected earlier in the year.

Domestic and international tourism had declined significantly, and key tourism regions such as Far North Queensland and South East Queensland were experiencing a more pronounced impact on activity and employment.

Business credit and investment

Access to finance had stabilised although tighter lending practices remain a key concern for many businesses, particularly those exposed to the commercial property and medium- to high-density residential property sectors. Contacts suggested that the major banks' property exposures may be approaching their upper limits, although there appeared to be regional variations in this theme. In contrast, mining and energy contacts generally reported a degree of comfort in terms of access to finance due to the financial strength of large foreign partners and ability to access international capital markets.

Contacts noted the cost of business credit remained high and this was supporting heightened activity in capital markets as firms pursued alternative sources of finance, together with internal capital management (e.g. delaying discretionary expenditure, lowering distributions, issuing new equity, underwriting dividend reinvestment plans).

Outside the mining sector, businesses were anticipating modest, if any, growth in capital expenditure in 2009-10, pending a clearer view of economic and financial conditions. Finance had also been a constraint in the rural sector — affecting both spending and asset values — and a return to better conditions was viewed as likely.

Capacity issues

The extent to which the Government's stimulus packages were offsetting weaker private sector demand in the building construction sector was explored in some detail during this liaison round. A number of major construction firms indicated that stimulus projects were helping to fill gaps in their planned work schedules; but activity remained down on last year's levels. Most expected further weakness in private non-residential building activity with an associated easing in input costs.

In some areas the prevailing strength in engineering construction activity and signs of large scale mining-related investment resuming were identified as potentially leading to local labour and accommodation shortages down the track. This observation particularly related to labour supply in Perth, and accommodation in mining centres.

Employment and skills

In general, labour market conditions had continued to settle with most firms indicating a degree of comfort with current staff numbers and looking for further signs of growth in demand before re-hiring.

A number of retailers reported slight increases in staff numbers. There was evidence that retail employers had pursued flexibility in work hours, meaning that the total number of workers on their payrolls had remained steady across the past year, with savings being made through reducing the number of shifts per employee.

However, the general result was that companies had reduced their workforces since 2008. Some firms have seen the slowdown as a chance to undertake restructuring and recruit talented or skilled workers that had recently become available on the labour market.

Weaker economic conditions were thought to be leading to higher training completion rates. Contacts reported that trade apprenticeship cancellations had declined during the downturn.

Prices and wages

Input price inflation and wages growth had moderated further during the June quarter.

Many contacts had instituted a freeze on executive wages, most since the beginning of 2009. Indications were that this freeze would continue until a sustained recovery in sales. Wage bill savings were also taking place through agreements with employees, for example by running down accrued leave.

At the non-executive levels, there were mixed messages, though most companies were seeing a decline in the growth of input costs, including wage costs. Some of the harder-hit companies had also frozen non-executive staff pay.