Box A

Insights from Liaison

This Box highlights key messages collected by teams based in Adelaide, Brisbane, Melbourne, Perth and Sydney during discussions with around 290 businesses, industry bodies, government agencies and community organisations over the period from the beginning of August to early November 2023.

Liaison information provides a timely signal that economic activity in a number of sectors has continued to moderate over recent months. While demand conditions in retail and new housing construction have slowed, generally solid levels of business activity (including in infrastructure construction) are supporting investment intentions. Employment intentions have eased over recent months and are around longer run averages. Wages growth is still tracking around 4 per cent, but forward expectations have drifted lower of late. Firms note that growth in non-labour costs has been easing since earlier in the year, though recent movements in the exchange rate and oil prices are slowing the decline in imported costs, and domestic cost pressures persist. Softer demand is weighing on firms' capacity to increase prices and maintain margins.

Consumer demand has eased and cost-of-living pressures remain acute for many households

Retail trading conditions have been broadly unchanged in recent months and remain weaker than a year ago, with sales volumes declining for most retailers since last year. Retailers continue to report that consumers – particularly those most affected by cost-of-living pressures – are more budget-conscious in their spending. Consistent with this, domestic leisure travel has declined over the past six months, though it is still at a high level.

Community organisations have flagged that cost-of-living pressures remain acute, with more people than usual seeking support, including wage earners and households with mortgages. These organisations continue to report that a lack of affordable rental accommodation is a key issue. Increasingly, demand for support is exceeding the capacity of these organisations to provide assistance.

The outlook for residential construction is subdued, but there is a large pipeline of infrastructure work that is stretching capacity in some areas

Firms working in detached residential construction report still being relatively busy as they work through the sizeable backlog of activity built up over recent years. Supply chains, upstream costs and labour availability are improving which is helping to support profitability, though there are lingering concerns around financial conditions in parts of the industry. Builders and developers generally expect slower residential construction activity in 2024 in the wake of declining home sales over the past year or so.

Sharply higher construction and financing costs over 2022 and 2023 have adversely affected feasibility for many higher density residential projects, and activity is subdued as a result. Some firms report the need to compete with infrastructure projects for materials and labour inputs. Buyer sentiment for off-the-plan purchases remains weak. Conditions are more favourable for build-to-rent and student accommodation projects, underpinned by strong population growth (including the recovery in international student numbers) and growth in housing rents.

Firms involved in infrastructure and other larger construction projects are reporting strong demand and a substantial pipeline of work. While some large road and rail projects are due to finish towards the end of 2024, there is a growing number of projects related to the renewable energy transition. Firms have noted that demand is exceeding available capacity across the non-residential construction sector; this is keeping materials and contractor costs elevated, which is flowing through to firms' pricing.

More broadly across industries, solid cashflows have been underpinning investment plans for many firms, with a continued focus on digitisation, automation and cybersecurity to improve delivery of services or increase firm productivity. This includes investment in industrial property and technology, consistent with the shift to e-commerce and the need to improve 'last mile' logistics.

Demand for labour has eased and labour availability has improved

Over recent months, firms' hiring intentions have eased back to longer run averages, led by a smaller share of firms looking to expand headcount (Graph A.1). Softer labour demand has been particularly evident for wholesale and retail firms, and remains relatively subdued for firms in manufacturing, construction and mining. Firms generally cite a mixture of rising costs – including wage costs – and weaker sales growth as reasons for moderating hiring intentions.

Firms have reported improved labour availability in recent months, though finding suitable labour generally remains more difficult than prior to the pandemic. Voluntary turnover rates have declined but are still higher than longer run averages.

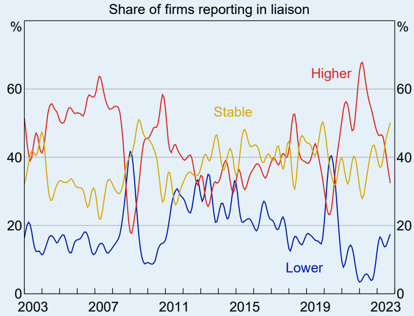
Private sector wages growth is currently around 4 per cent, while forward expectations have drifted lower

Liaison suggests that private sector wages growth is around 4 per cent in year-ended terms, as has been the case for much of the past year. The effect of higher award wages

Graph A.1

Employment Intentions*

Share of firms reporting in liaison



* Over the next 12 months; smoothed with a 13-month Henderson trend.

Source: RBA.

growth has been partly offset by moderating wages growth in certain occupations and industries, including IT, professional services and construction. In part to manage higher labour costs, firms continue to look for operational efficiencies, which is supporting investment in automation and business processes.

Expectations for wages growth over the year ahead have drifted below 4 per cent over recent months. Firms that anticipate wages growth to ease over the coming year cite expectations for lower inflation outcomes and an easing in business conditions. An improvement in labour availability, lower voluntary turnover and a continued emphasis on cost control have also been noted.

An easing in the growth of upstream costs and softer demand are filtering through to firms' pricing

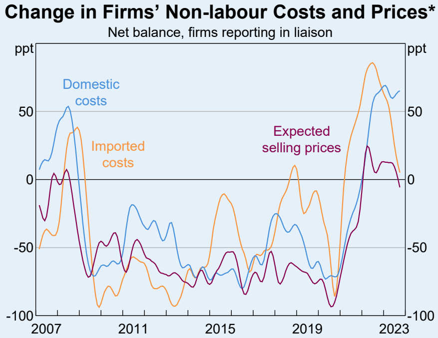
Non-labour costs are growing less rapidly than earlier in the year, driven by lower imported goods cost increases (Graph A.2). Countering this, firms have emphasised that they are facing a range of persistent upward pressures on domestic costs such as energy, logistics (including fuel) and insurance, in addition to higher labour costs over the past year. Some firms have recently flagged that a weaker exchange rate and higher fuel prices could offset some of the underlying decline in imported goods costs.

Firms across a broad range of industries have noted intensifying price competition over recent months. In the case of retailers, promotional and discounting activity has picked up and, compared with recent years, firms report that they are more constrained in the price increases that customers will accept.

Many firms expect to increase their prices by less over the next 12 months compared with the past 12 months, but the share expecting above-average increases is still much higher than prior to the pandemic. A few firms have recently indicated that their prices growth may moderate more slowly than they previously expected given persistent input cost pressures.

Graph A.2

Change in Firms' Non-labour Costs and Prices*



* Share of firms reporting above-average increases less share reporting below-average increases or decreases; average increase indexed to 0; smoothed with a 13-month Henderson trend.

Source: RBA.