

The RBA's Business Liaison Program*

The Reserve Bank meets regularly with businesses and associations in every state and across industries of the Australian economy. The information collected under the liaison program complements that available from official sources and helps the Bank to monitor cyclical and structural developments, as well as the effect of unusual events on the Australian economy. The broad messages gathered through liaison are incorporated into the Bank's policy discussions and public communications.

Introduction

Information provided by businesses can assist in understanding current and future trends in the domestic economy. In recognition of this, a formal program of business liaison was established by the Reserve Bank in 2001, though the Bank has had informal contacts with businesses dating back to the 1960s. This article describes how the Bank's liaison program is structured, how the information gathered is used to complement that from other sources such as the Australian Bureau of Statistics (ABS) and business surveys, and how the broad messages from liaison are incorporated into the Bank's communications.

The Business Liaison Program

While the Bank's headquarters is in Sydney, historically the Bank had branches in each of the state and territory capitals. As its banking business with state governments declined over time, these functions were progressively closed. In their place, State Offices were established in the capital cities of Queensland, Victoria (which also covers Tasmania), South Australia (which covers the Northern Territory) and Western Australia. Along with a unit in Sydney, the Bank's business liaison program is conducted through these offices. The program has around 20 staff, three-quarters of whom are economists.

The main focus of the business liaison program is to hold regular discussions with external contacts. Over time, Bank staff have established relationships across a broad cross-section of the business community, and there are currently around 1 000 active contacts across the country. This contact list is regularly refreshed to reflect structural changes in industries over time as well as emerging economic developments; for instance, the number of contacts in information technology and online retailing has increased in recent years. The Bank also has contacts with industry associations in each state. Participation by contacts in the Bank's liaison program is voluntary and company-specific information and perspectives are treated with strict confidence, though summary messages from liaison are incorporated into the Bank's publications.

How the information is gathered

Liaison meetings are undertaken continually rather than during a specific reference period, with around 70–80 discussions occurring monthly. Discussions with individual firms occur around every 6 to 12 months, with Bank staff usually meeting the chief executive officer, chief financial officer and/or operations manager. The staff speak with some business contacts on a more frequent basis, typically with firms in industries that are bellwether indicators of economic activity and consumer price pressures. Where practical, interviewees and interviewers are paired through time to support a consistent interpretation of the information discussed.

* The liaison program is managed by the Regional and Industry Analysis Section of the Economic Analysis Department.

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While the Bank's contact list is broadly representative of the industry structure of the Australian economy, the concentration of the meetings tends to be on the more cyclically sensitive industries. The relative weight of different industries in the sample of meetings also tends to change month by month as economic issues emerge and recede. As a consequence, the Bank's liaison in a particular month or quarter will generally differ from that of a standard business survey, where representativeness of the sample in line with actual industry shares in the overall economy would be an important part of survey design.

Liaison meetings are held with firms of all sizes, although most discussions are with mid-sized and large firms where conditions are most likely to reflect economy-wide trends rather than firm-specific factors. Information on general conditions facing small businesses is often gathered through contacts with industry associations and at round table meetings of small businesses organised by local Chambers of Commerce.¹ The Bank also conducts liaison in regional areas in order to assess more fully the variability of conditions across each state.

The overriding motivation of the program is to build a better understanding about how each industry is structured, the current stage of its business cycle, the challenges and opportunities faced over the medium to longer term, and how companies are responding to the domestic and international circumstances they face. To this aim, the Bank has discussions with firms in the retail, wholesale, transport, manufacturing, utilities, mining, housing, construction, business services, agriculture, tourism and education export industries. The Bank also meets with firms in the household services sector, such as in the child care, domestic education, health and aged care industries. This sector has been a major driver of employment in the economy for an extended period. Nonetheless, the household services sector

is usually underrepresented in the Bank's monthly sample since its activity is not very cyclically sensitive and there are a large number of small firms in the sector. While liaison is conducted in every state and industry, the share of the contacts in each industry varies between each state office depending on where industries tend to be concentrated geographically. For instance, liaison with firms in the mining industry is primarily undertaken by the Western Australia and Queensland State Offices, while liaison with manufacturers is most concentrated in the South Australia and Victoria State Offices.

The discussions are typically based around a set of common topics to ensure an economic picture is built up in a systematic and consistent way, both across businesses and over time. The range and depth of the topics covered are, however, quite flexible in order to cover in most detail the key economic issues affecting a particular industry at that time. The discussions are focused around recent developments in demand, investment, employment, wages, prices and margins, the main factors driving developments in these areas, and expected changes over the year ahead. While most of the discussion with contacts is qualitative in nature, some quantitative information is gathered during the discussion that can be used to help validate the strength of the signal from the official ABS data and other published surveys.

The Bank's approach to conducting business liaison is similar to that undertaken at other central banks. The most established liaison program, which has been in operation since the 1930s, is run by the Bank of England. In the United States, the regional Federal Reserve Banks conduct liaison. The Bank of Canada has been conducting business liaison since the mid 1990s. In contrast to the practices in many other countries, the Reserve Bank of Australia incorporates summaries of liaison information directly into its regular assessments of economic conditions and policy advice, rather than collating it into a separate product such as the Federal Reserve's 'Beige Book'. The Bank has assisted several central banks within the Asia region to establish their own business liaison programs.

¹ The Bank also discusses the financial and economic developments facing these firms through its Small Business Finance Advisory Panel, which meets on an annual basis.

The State Offices play a key role in the Bank's communication with members of the public. Staff interact with a broad cross-section of the community, giving presentations on economic developments to businesses and community organisations, industry association meetings, teacher conferences, and university and school students in their respective states. Along with the liaison meetings themselves, this provides an opportunity for the public to highlight certain issues and discuss the key messages contained in the Bank's various communications.

How the information is used

The Bank uses liaison information in a variety of ways to complement the picture of economic developments obtained from official data sources and published business surveys. In essence, liaison is used to help fill information gaps to strengthen the Bank's capacity to assess current cyclical and structural trends in the Australian economy. This information provides an important input to understanding emerging developments in the main industries of the economy, which helps build a 'bottom-up' approach to the Bank's forecasts.

In particular, the Bank uses the timely information from liaison to keep staff and the Reserve Bank Board abreast of the latest developments. Businesses are able to describe the 'here and now', while information from official data sources such as the ABS is subject to a publication lag. The timeliness of the liaison information is especially useful when the Bank needs to make an assessment of the effect that natural disasters and other unexpected events will have on economic activity and prices.

Liaison information is also used to help understand the economic trends reported in official data, including for inflation. Business liaison provides an independent source of information that can be compared with official releases to assist the Bank in distinguishing signal from noise in economy-wide data, though the signals from the comparatively small sample underpinning the monthly liaison information are often quite noisy as well. In addition, liaison information can help resolve data puzzles,

such as inconsistencies in recent trends between different economic variables as reported in the official data. Most importantly, the liaison discussions provide an opportunity to understand the factors that lie behind the latest trends as reported by the ABS in economic variables such as employment, activity and inflation and to assist the Bank in assessing whether these trends are likely to persist.

In addition, liaison provides insights about economic variables that are not directly observable or reported. For instance, liaison enables a closer focus on activities that are not reported separately in the national accounts, such as the tourism sector. The discussions with firms about their expectations over coming years are also useful in preparing the Bank's forecasts.

The information collected helps Bank staff understand how each industry is structured, the current challenges and opportunities faced by the industry, and how firms are responding to the circumstances they face. This can provide the Bank with a sense of, for instance, the degree of structural change that is occurring within each industry and hence in the national economy overall. Liaison discussions might cover firms' views on the availability of particular labour skills, specific strategies to deal with the high level of the exchange rate, and the regulatory framework. Much of the information gathered is qualitative, and there is clearly variability in firms' responses to the various issues discussed. Nonetheless, the Bank aims to discern overarching signals from the firm-specific messages, both in regard to the issues most commonly raised and the degree to which these issues appear to be important drivers of overall activity and pricing behaviour.

The summary messages derived from the Bank's liaison process are integrated with the advice provided to the Board and are communicated to the public through the Bank's regular statements and reports as well as speeches by senior staff. The Bank includes articles drawing on liaison in its *Bulletin*, covering developments across states and analysis of current developments and challenges in specific industries.

Some Examples from Recent Years

Through the contacts the Bank has built in all states and industries, the liaison program has been used to gather information when the economic momentum changes rapidly. For instance, the Bank was able to collect and assess information on the magnitude of the decline in consumption and the impact of tighter credit conditions during the onset of the global financial crisis in 2007–08, well before the economic slowdown was apparent in the official data.

Liaison was helpful following the widespread flooding in Queensland in 2010–11, which enabled the Bank to assess quickly the impact of the floods on coal production and exports from Queensland, the reduction in activity from the forced closure of businesses in Brisbane and elsewhere, and the magnitude of the damage to homes and state infrastructure that would need to be rebuilt. These estimates were included in the Bank's *Statement on Monetary Policy* published in early February 2011 (see RBA (2011a)).² The liaison program also helped the Bank to assess the effects on agricultural output and prices of the severe drought during the 2000s, as well as the effects of Cyclones Larry and Yasi in 2006 and 2011. The cyclones had important effects on economic activity, including the output and prices of bananas, which as it turned out had a very significant effect on overall CPI inflation.

Understanding and monitoring developments in the mining industry has been a focus in liaison over recent years. In its discussions, the Bank has sought to corroborate information from official sources such as the ABS and the Bureau of Resources and Energy Economics, including the projected magnitude and timing of the run-up and run-down in the level of mining investment, and the impact of mining and infrastructure investment projects on Australia's resource exports. Some issues raised in discussions with mining companies have been the share of investment that is imported over the life of a project, the availability of the required skilled labour, and the ability of labour to move into other industries as investment projects are completed. The Bank has

discussed with a range of business service companies the degree to which the mining sector has affected demand for their services, which has highlighted in particular the importance of developments in the mining industry for employment services, engineering services and leasing activities. This information was incorporated in a recent *Bulletin* article (see Manalo and Orsmond (2013)).

The challenges in dealing with the high value of the Australian dollar has been a prominent part of the discussions with non-mining export firms and import-competing firms for several years. Liaison suggests that company responses to changes in the level of the exchange rate have varied considerably across industries. For instance, manufacturing contacts have highlighted a range of responses, including greater use of 'offshoring', reliance on imported products, and capital deepening. Tourism contacts generally report that the exchange rate does not have a large impact on the number of arrivals, but that it affects the amount of spending by tourists that come to Australia and the number of Australians that travel abroad rather than undertake domestic holidays.³ The Bank has contacts with English-language course providers, TAFE institutions and universities, which report that trends in overseas student enrolments in recent years have been affected by policy changes more so than the varying level of the exchange rate. The Bank's discussions with companies have covered the willingness and ability of firms to pass on exchange rate changes to the intermediate and final prices of tradable goods and services. An article in the *Bulletin* estimating the degree of exchange rate pass-through drew on the insights provided by business, as well as formal econometric analyses (see Kohler, Manalo and Perera (2014)).

Given the cyclical sensitivity of housing demand to changes in interest rates, the liaison program has a range of contacts with exposure to the housing market, including builders, renovators, real estate agents, valuers and legal firms. These contacts have been helpful in understanding the extent to which housing supply can respond to upswings in

2 An update on these estimates was provided in RBA (2011b).

3 The issues facing the tourism industry were discussed in Hooper and van Zyl (2011).

housing demand in a timely manner. In this regard, contacts have highlighted the shortage of land availability, complexity of the planning system, high development fees and community resistance to new housing projects.⁴ The Bank has discussed foreign ownership of real estate, and information in this regard was used in preparing its recent submission to a parliamentary inquiry into this issue.⁵

Wages and employment trends are a common topic in the Bank's liaison discussions. During the global financial crisis, companies indicated a marked change in the flexibility of labour markets compared with previous economic downturns, and the Bank was able to detect this change in behaviour before it became apparent in the official data. In particular, there was frequent recourse made by companies to wage freezes and reductions in working hours rather than outright job losses. Bank liaison indicates that only some of this reduction in average job hours has since been retraced, partly due to ongoing softness in the labour market and in some cases employee choice.⁶

Recently, the Bank has established contacts with a range of community service organisations, which can provide information on the economic conditions faced by economically disadvantaged members of society, many of whom are only marginally attached to the workforce. The discussion with these contacts combined with research undertaken by the Bank indicates that around half of the economically disadvantaged move out of disadvantage over a five-year period, primarily by obtaining and retaining full-time work. However the other half faces a range of structural impediments to obtaining employment (see Cunningham, Orsmond and Price (2014)).

Conclusion

Business liaison provides important perspectives on developments across industries and the state of the

business cycle, and has become a valuable input into the Bank's assessment of the Australian economy. Liaison provides a timely gauge of developments that is often only provided by traditional sources of information with a delay or is not available at all from these sources. It also provides a deeper understanding of the longer-term structural changes that are occurring within industries. As the economic landscape changes, the Bank incorporates the information obtained from liaison into its regular assessments of economic conditions, forecasts and policy decisions. The broad themes derived from business liaison in this regard are incorporated in a timely fashion in the Bank's publications, such as the quarterly *Statement on Monetary Policy* and the *Bulletin*. ✎

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4 See Hsieh, Norman and Orsmond (2012) for a summary of around 50 contacts' views.

5 For a summary of the Bank's Submission to the Inquiry into Foreign Investment in Residential Real Estate, see Gauder, Houssard and Orsmond (2014).

6 For further details, see Plumb, Baker and Spence (2010).

