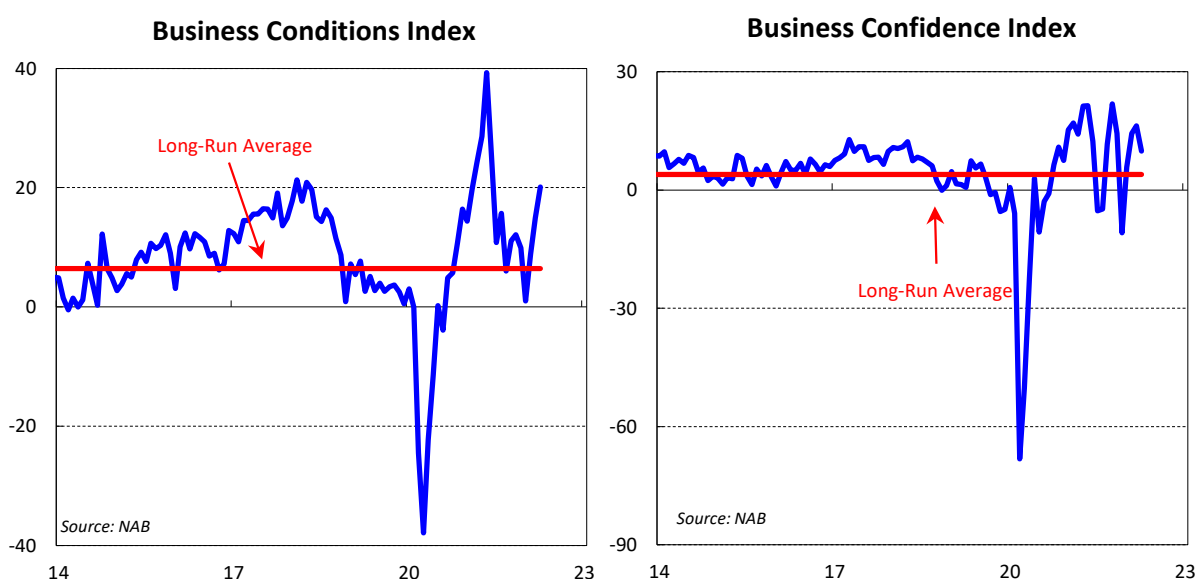


Tuesday, 10 May 2022

Business Confidence and Conditions

Costs Rise, But Conditions at 22 Mth-High

- Business conditions jumped 5 points in April to +20, the highest reading since June 2021 and more than three times the long-run average at +6. Confidence remains elevated but fell 6 points to +10 in April. It is the first fall in 4-months. Confidence is above the long-run average of +4.
- Cost pressures continued to build in April. Quarterly growth in purchase and labour costs jumped to new record highs, suggesting inflationary pressures are likely to continue to build over the coming months.
- Businesses have been incredibly resilient through the start of 2022 and confidence has remained buoyant. However, staff shortages, supply-chain disruptions and growing inflationary pressures are beginning to weigh on business optimism.
- An improvement in trading and profitability measures underpinned the rise in conditions. Each of these sub-indices jumped to a 10-month high, reflecting the strong demand in the economy. The employment measure was steady at an elevated level.
- The improvement in conditions was driven by a long-awaited recovery in the recreation & personal services sector, following a sustained period of weakness. Conditions are now strong across all industries.



Business Conditions

Business conditions rose solidly in April, marking the third consecutive monthly improvement in conditions since the Omicron outbreak over December and January. Business conditions surged 5 points in April to +20, the highest reading since June 2021 and more than three times the long-run average at +6.

An improvement in the trading and profitability measures underpinned the rise in conditions in April, while the employment measure was unchanged at an elevated level. The trading and profitability sub-indices each jumped to a 10-month high, reaching +27 and +22, respectively. This reflects the strong demand in the economy, as households continue to open their wallets despite growing cost of living pressures. Employment was steady at +10, a level more than 5 times above the long-run average.

By industry, the improvement in conditions was driven by a long-awaited recovery in the recreation & personal services sector. Alongside retail and hospitality, the recreation & personal services industry has been one of the most directly affected by COVID-19 and has relatedly undergone a sustained period of weakness.

Conditions are now generally strong across all industries. However, conditions are weakening in the construction and transport & utilities sectors, where cost pressures are most acute.

Conditions improved most in Queensland, NSW and SA in April, while conditions slipped in Victoria. In trend terms, conditions remain strong across the states.

The survey was conducted between 22 and 29 April and, therefore, does not capture business's reaction to the first interest rate rise in more than a decade, announced at the Reserve Bank's (RBA) May Board meeting.

Business Confidence

Business confidence did not fare as well, falling from a 5-month high in March and recording the first monthly fall in confidence since December 2021. Business confidence fell 6 points to +10 in April but remains elevated at more than double its long-run average of +4.

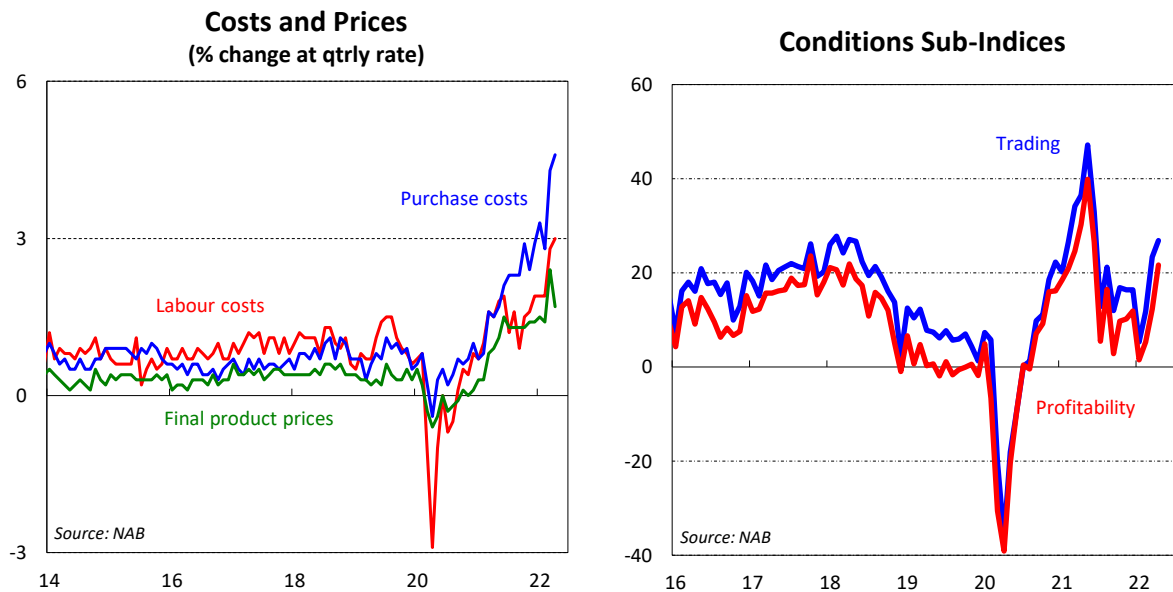
Businesses have been incredibly resilient through the start of 2022 and confidence has remained buoyant despite staff shortages, supply-chain disruptions and growing inflationary pressures. However, while business confidence is generally strong, today's result indicates that these headwinds are beginning to weigh on confidence. Meanwhile, the prolonged conflict in Ukraine and lockdowns across parts of China mean that supply bottlenecks are unlikely to ease quickly, adding to the uncertainties that businesses face.

Confidence also remained high across industries, although large monthly declines in confidence were recorded in the transport & utilities, recreation & personal services and finance, business & property sectors.

Similarly, business confidence is high across the states, despite broad-based falls in April. The exception being Tasmania, where confidence is materially softer.

Cost Pressures

The survey revealed that cost pressures continued to build in April. Quarterly growth in purchase and labour costs jumped to new record highs, at 4.6% and 3.0%, respectively. However, growth in final product prices and retail prices slowed in April, indicating that businesses absorbed some of the rising costs. Nonetheless, the result suggests inflationary pressures are likely to continue to build over the coming months. This follows the hottest inflation print in more than two decades in the March quarter, which saw annual headline inflation surge to 5.1%.



It is in this context that the RBA lifted the cash rate by 25 basis points last week and prefaced further hikes in the months ahead. The RBA expects headline inflation to reach a peak of 6% in 2022 and does not expect inflation to return to its 2-3% target band until the middle of 2024.

Leading Indicators – Capacity Utilisation and Forward Orders

The survey leading indicators were mixed in April. Capacity utilisation edged up half a percentage point to an 11-month high of 83.9%, which is considerably above the long-run average of 80.8%. In contrast, forward orders pulled back to +9, from +12 in March. However, forward orders are comfortably above the long-run average.

Outlook

Staff shortages, supply-chain disruptions and growing inflationary pressures are beginning to weigh on the optimistic mood among businesses.

The commencement of the RBA's interest rate tightening cycle last week represents another headwind for businesses.

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