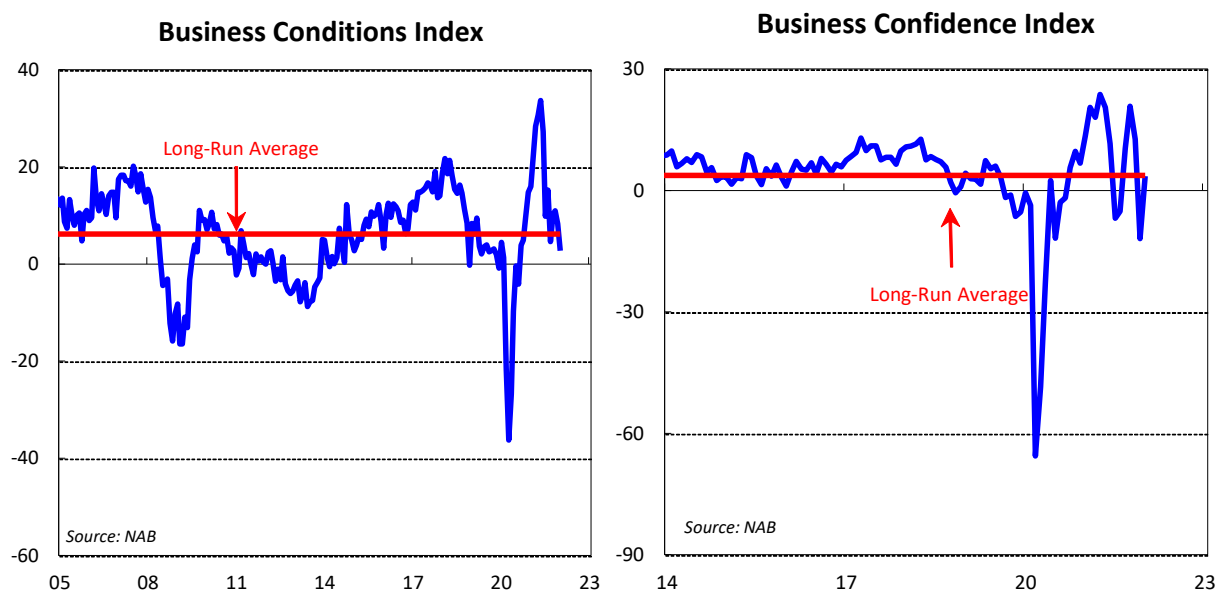


Tuesday, 8 February 2022

# Business Confidence and Conditions

## Mood Lifts as Disruptions Set to Ease

- Business confidence rebounded in January to around average levels, signalling optimism that Omicron will not derail the recovery. The confidence index rose 15 points to +3, after plunging 25 points in December alongside surging case numbers.
- Meanwhile, business conditions declined 5 points to +3 in January, as businesses grappled with staff shortages, supply disruptions and a drop in foot traffic. There were declines across all three subcomponents of the conditions index.
- The increase in business confidence and the deterioration in conditions was broad-based across states in January. Conditions weakened across most industries, with those which are sensitive to rising case numbers being the most affected – notably retail, transport and construction.
- Cost pressures remain elevated alongside rising inflation. Notably, purchase cost growth rose to a record high of 3.4% in quarterly terms.
- Forward looking indicators have generally held above their long-run averages, pointing to a solid pipeline of work, but are below the peaks they reached last year.
- As case numbers decline, we expect the upswing in economic activity to resume, which will support business conditions and investment. Generous tax incentives also continue to encourage investment. However, price pressures and the prospect of rate hikes later this year may weigh on some businesses. Regardless, we expect strong growth in investment in 2022.



Business confidence rebounded in January to around average levels, signalling optimism that Omicron will not derail the recovery. The survey was taken in the second half of the month, which captured the period when case numbers began declining.

The confidence index rose 15 points to +3, after plunging 25 points in December alongside surging case numbers. Confidence remained below its level from prior to the Omicron outbreak, but well above the lows reached during the lockdowns in 2020 and 2021.

This is consistent with what we are hearing directly from our business customers, who appear to be mildly optimistic about the outlook. Labour shortages and supply bottlenecks remain an issue. But many businesses are still cashed up, and some are also beginning to make working-capital drawdowns. Rising inflationary pressures and the prospect of higher interest rates are also in focus.

Meanwhile, business conditions declined 5 basis points to +3 in January, as businesses grappled with staff shortages, supply disruptions and a drop in foot traffic as consumers were more cautious about leaving the house.

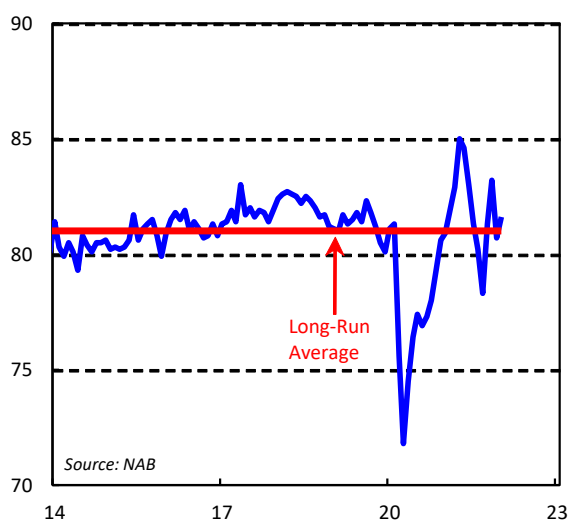
There were declines across all three subcomponents of the conditions index. There were significant falls in trading, down 7 points to +7, and profitability, down 8 points to +2. The employment subindex also declined 3 points to -1. This reflects the complexity of labour market dynamics, as businesses battled a drastic increase in absenteeism alongside surging infections.

Encouragingly, customer liaison suggests that staffing challenges caused by the Omicron outbreak have eased as case numbers have declined. However, staffing remains an ongoing issue beyond the immediate impact of Omicron. Finding and holding onto the right staff remains challenging. Some businesses have reported a rise in turnover as people take the opportunity to move to higher paid roles.

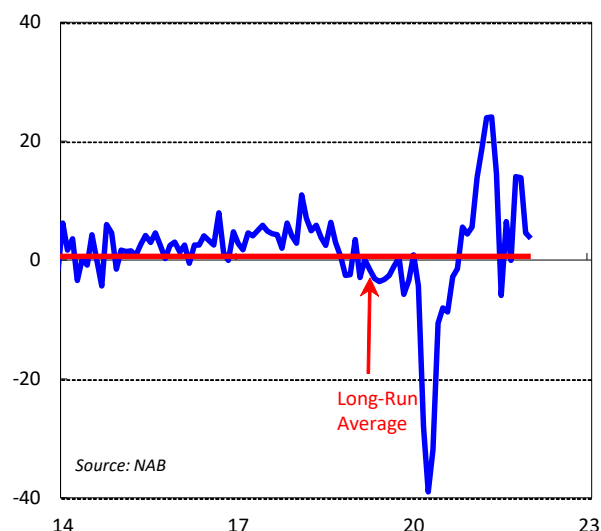
Business confidence rebounded strongly across all states in January. Queensland and Tasmania led the way, followed by SA. While NSW and Victoria also experienced solid upticks in confidence, followed by WA.

The fall in business conditions over January was generally broad-based across the states. Conditions dropped sharply in Victoria and WA, compared with more modest falls in SA, NSW and Tasmania. Queensland bucked the trend, reporting a solid improvement in conditions. In trend terms, conditions are strongest in WA and Tasmania, despite monthly falls.

**Business Capacity Utilisation Rate**



**Forward Orders Index**



Conditions weakened the most in industries which are sensitive to rising case numbers – notably retail, transport and construction. Regardless, conditions deteriorated in most industries.

Encouragingly, business confidence picked up in all industries in January, except for mining. The largest increases in confidence were reported in the wholesale, transport & utilities and recreation & personal services sectors.

Cost pressures remain elevated alongside rising inflation. Notably, purchase cost growth rose to a record high of 3.4% in quarterly terms. Labour costs grew at 1.9% in quarterly terms in January, as they did in December. Labour cost pressures have been building over recent months and will be a key measure to watch as the Reserve Bank closely monitors wage developments in the economy.

Forward looking indicators have generally held above their long-run averages but are below the peaks they reached last year. Capacity utilisation increased to 81.6%, while forward orders pulled back a little but continue to point to a solid pipeline of work.

### **Outlook**

Omicron has posed another hurdle for businesses but the stabilisation in confidence suggests businesses expect challenges associated with Omicron will be short-lived. As case numbers decline, we expect the upswing in economic activity to resume, which will support business conditions and investment. Plus, generous tax incentives continue to encourage businesses to invest. However, price pressures and the prospect of rate hikes later this year may weigh on some businesses. Regardless, despite the ongoing challenges, we expect strong growth in business investment in 2022.

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