Retail Health Index December 2024

KPMG Australia

Contents

Introduction

Welcome to the latest edition of KPMG Australia's Retail Health Index© (RHI). The RHI provides data-driven insights on the current and future health of Australia's retail sector from the perspective of businesses operating in the sector.

In our last edition, the KPMG RHI shows recovery stalled in the second quarter of 2024 as discretionary retail slowed amidst the cost-of-living crisis.

The latest KPMG RHI suggests that positive momentum may have returned, and a beacon of light could be on the horizon.

KPMG RHI increased by 0.72 index points, moving from -1.72 to -1.00; a step in the right direction. However, despite the improvement, the overall health of the retail sector remains in poor condition and with 'healthy' retail conditions is not likely until mid 2025, a modest acceleration from our last RHI.

Key takeaways

- *One swallow does not make a spring.*
- At best, the latest RHI suggests the *promise* of momentum to come, and as we head into the critical November–December trading period, our first RHI of 2025, is likely to confirm whether this is sustainable and better times are within reach.
- Unfortunately, the per capita retail recession has continued into the September quarter, now making nine straight quarters of falling retail sales volumes on a per person basis, representing a fall of 6.6% from the last peak in June 2022. So, while the overall direction is positive, sentiment remains in 'unfavourable' territory meaning consumers, on balance, are still relatively gloomy which translates into more cautious spending behaviour.
- Indeed, discretionary spending recorded no growth in the three months from June as households continue to spend virtually every dollar they earn, with the household savings ratio barely above zero.
- The retail sector achieved a slight improvement in overall margins during the June quarter, but profitability remains below the average achieved during the decade to the end of 2019.
- While the proportion of online sales to total retail sales fell from 11.7% to 11.3% over the September quarter, it is inherently volatile and still comfortably above the equivalent ratio of 10.3% recorded in the September quarter 2023. Non-food online retailing sits at around 13.2% of total retail sales vs online food retailing at approximately 8.5%.

Everything retail is human. Everything human is digital.

- According to KPMG's 2024 APAC *Seamless commerce* report, 42% of Australian consumers are omnichannel, but prefer online, while 38% prefer a physical store to online. We think the bottom line is that Australian shoppers are remarkably adaptable and channel agnostic. Therein lies the challenge.
- The same report also suggests most retailers are embracing (or intend to embrace) generative AI. 70% of consumer and retail leaders see AI transforming their business through customer analysis, personalisation, demand forecasting, supply chain management, and marketing content generation.
- From an Aussie consumer perspective, 44% were satisfied with generative AI driven product recommendations, albeit 36% had never tried them, with concerns about the privacy and accuracy aspects of AI remaining. This suggests an inherent desire among consumers to embrace AI technology, despite misgivings.
- When it comes to technology investment, according to our *2024 KPMG Global Tech report*, 78% of technology executives, say their organisation is struggling with the pace of change, but also say their business senior leadership is too risk averse and need to get on with it. 74% of say AI is improving the productivity of their workers and business performance, but the challenge is that AI is yet to deliver benefits at scale (only 31% is currently doing so).
- And finally, a word on sustainability with KPMG's 2024 *Global Circularity* report suggesting that there is a serious disconnect between retailers' sustainability aspirations and the steps being taken to deliver on sustainability goals. Indeed, in our *2024 CEO Outlook*, 66% of CEOs said their business was not ready to withstand shareholder scrutiny over their sustainability ambitions. With the Australian Government's new sustainability reporting obligations kicking in from 1 January 2025, this finding could send a shiver down the spine.

We hope you enjoy reading our KPMG RHI report and if you would like to know more about how KPMG can help your business, please contact us.

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Retail Health Index

KPMG's Retail Health Index© (RHI) looks to have gained some positive momentum driven by the lowest wage growth figure in a year and a small uptick in consumer sentiment, as the prospect of further rate hikes diminish in the near term.

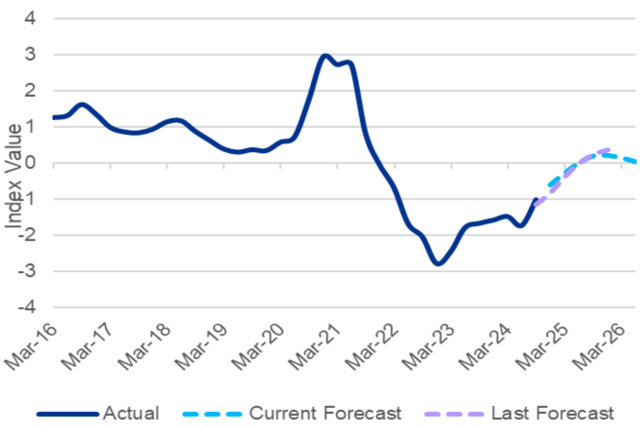
Recovery heading in the right direction

Between the June quarter 2024 and the September quarter 2024, the KPMG RHI further increased by 0.72 index points, moving from -1.72 to -1.00; a step in the right direction towards a healthy retail sector.

Our latest forecasts of the components that make up the KPMG RHI suggest the medium-term outlook for the sector remains positive, albeit relatively weak compared to either the Covid bounce or even the steadier pre-pandemic period. The short-term headwinds affecting the near-term trend are gradually diminishing.

FIGURE 1

KPMG Retail Health Index, Actual & Forecast



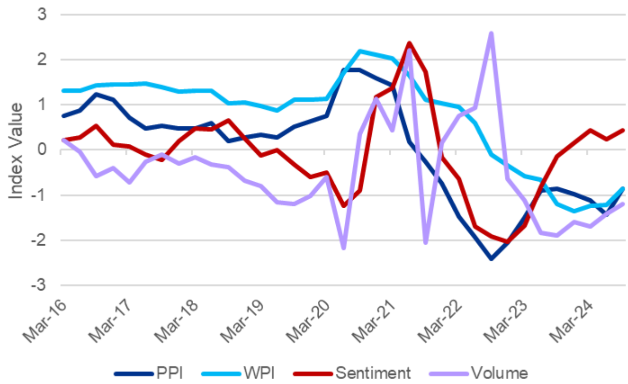
Source: KPMG's calculation, ABS, Haver

From an individual component perspective, Australian consumer confidence looks to be rising as inflation pressures ease, rate rise fears subside and disposable income ebbs higher on the back of policy decisions (including the commencement of the Stage 3 tax cuts, energy rebates and other cost-of-living relief packages).

In the September quarter 2024, wages increased by 3.5% over the year, the lowest annual rise since the December quarter 2022, following four consecutive quarters of annual wage growth equal to or above 4%.

FIGURE 2

KPMG RHI by Component Factors



Despite the near-term improvements, our 2024Q3 forecast suggests the full recovery of the retail sector is unlikely to occur before the end of CY25 as three out of four elements remain in the negative territory. It will simply take some time for these elements to return to healthier levels.

- **PPI**: from -1.44 to -0.86 (i.e. between 2024Q2 and 2024Q3 the growth rate of PPI decreased from being 144% above its historical average to just 86% above its historical average). The deceleration in PPI growth during the three months to September 2024 positively contributed 0.37 index points to the quarterly change in the RHI. That is, PPI contributed -0.55 index points to the RHI in the September quarter 2024, from -0.93 index points in the June quarter 2024.
- **WPI**: from -1.23 to 0.86. The growth rate of the WPI fell from 123% above its historical average in the June quarter 2024 to just 86% above its historical average; contributing -0.40 to the RHI in the September quarter from -0.57.
- **Sentiment**: sentiment increased to 0.44 from 0.24 and contributes 0.25 index points to the September quarter RHI (up from a 0.14-index-point contribution to the June quarter RHI).
- **Volume**: from -1.41 to -1.19 and negatively contributes 0.28 index points to the September quarter RHI (compared to a negative contribution of 0.33 index points contribution to the June quarter RHI).

Spending indicators

Consumers remain cautious, pulling back on both discretionary and non-discretionary spending, even after government policy changes to lift disposable income.

Retail sales

Retail trade stalled through the September quarter, with month-on-month sales not keeping pace with (anticipated) population growth and barely keeping up to headline inflation. Current dollar retail sales in July were flat, while August saw a little kick-up but the growth momentum did not continue into September.

The per capita retail recession has continued into the September quarter, now making nine straight quarters of falling retail sales volumes on a per person basis, representing a fall of 6.6% from the last peak in June 2022.

Retail trade volumes grew by 0.5% over the September quarter, although concerningly the volume of food sales – which represents the single largest retail category – recorded its third straight quarterly fall and is now around 1.5% lower than December quarter 2023 sales volumes. Anecdotal evidence suggests a combination of brand switching and 'belt tightening' in food budgets is driving this result, as the ongoing cost-of-living challenges continue to hurt households.

FIGURE 3

Change in Retail Turnover, Australia, Current and Inflation Adjusted, Quarterly

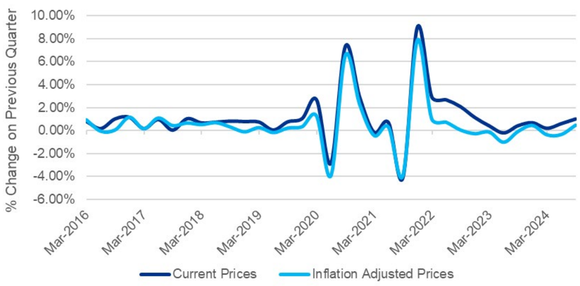
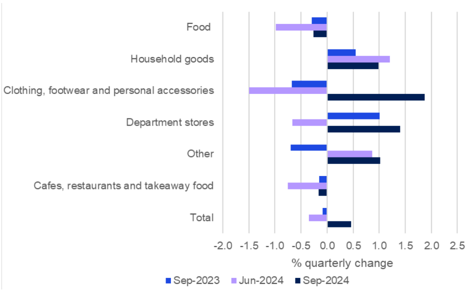


FIGURE 4

Change in Quarterly Inflation Adjusted Sales by Category, Australia



Cafes, restaurants and takeaway food services also recorded its second quarter of declining sales volumes, with turnover now more than half a billion lower in the September quarter 2024 compared to the March quarter 2023.

Consumer sentiment

The Westpac–Melbourne Institute Consumer Sentiment Index averaged 84.1 during the September quarter, up from 82.8 for the previous June quarter. There has been, however, a noticeable jump in sentiment recorded in the month of October, up to 89.8 – a level not seen since early 2022.

While the overall direction is positive, sentiment remains in 'unfavourable' territory meaning consumers, on balance, are still relatively gloomy which translates into more cautious spending behaviour. This run of sub-neutral levels in the Westpac–Melbourne Consumer Sentiment Index for Current Conditions is now tallying for *32 consecutive months.* The protracted sentiment slump is the second only to the early 1990s in terms of the duration and weakness of reads.

FIGURE 5

Westpac–Melbourne Institute Consumer Sentiment

Survey respondents clearly showed a jump in positive expectations towards the year ahead, with *Family Finances now compared to the last 12 months* jumping 7.8 points. Sentiment towards *Family Finances in the next 12 months* also jumped by 7.2 points and is sitting just below a balanced reading (99.7). Expectations surrounding economic conditions, both in the near term and over the next five years, are also improving, albeit both are still are unfavourable overall.

FIGURE 6

Westpac–Melbourne Institute Consumer Sentiment by Component, quarterly change

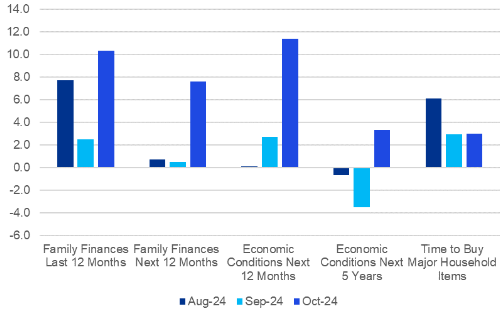
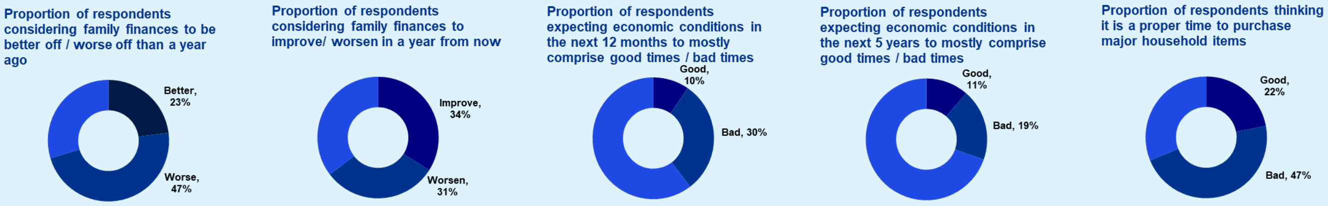


FIGURE 7

ANZ–Roy Morgan Survey of Consumer Confidence



Household spending

Household spending grew by 0.2% in seasonally adjusted current dollar terms over the September quarter, **with discretionary spending recording no growth in the three months from June**, while non-discretionary spending grew slightly above headline inflation.

The latest data shows households continue to creep up their spending on Services relative to Goods, with $0.77 spent on Services for every $1.00 spent on Goods – an uplift of $0.01 during the September quarter.

Households are continuing to spend virtually every dollar they earn, with the household savings ratio barely above zero. The last prolonged period of a very low, and even negative, household savings ratio was during the early to mid 2000s – a period more so marked by stronger consumption activity than the current mismatch between household income and household spending.

FIGURE 8

Household savings ratio, Australia

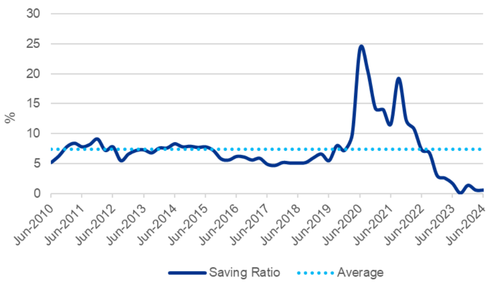
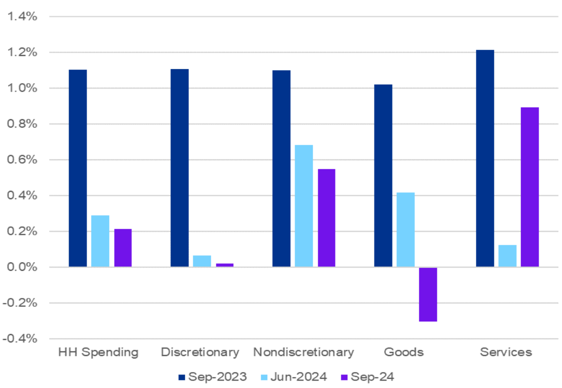


FIGURE 9

Monthly Household Spending by Type, Australia



Household spending, from a volume perspective, fell the most over the quarter in the Clothing & Footwear category (-3.5% q/q) and Alcoholic Beverages & Tobacco (-0.7% q/q).

Population

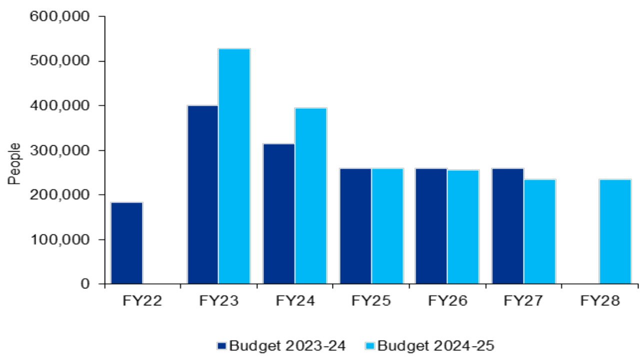
Australia's population grew by 2.3% to 27.11 million people in March 2024, according to the latest figures released by the ABS. Net Overseas Migration (NOM) drove 83% of the 615,300 annual population growth, while natural increase accounted for the remaining 17%.

A derived average population for Australia based on the June quarter national accounts suggests further population growth during the three months from the end of March of nearly 180,000 people – the second highest quarterly average population growth since 1973.

While not exactly comparable to NOM, net long-term overseas visitor arrival and departure data shows a slight slowing over the 12 months to September 2024 (656,000 people) compared to the 12 months to March 2024 (677,000). One factor influencing this outcome is lower foreign student arrivals, with 350,000 arrivals in the six months to September 2024 compared to just under 420,000 in the six months to March 2024.

FIGURE 10

Net Overseas Migration Targets by Year, Commonwealth May 2024 Budget



Cost indicators

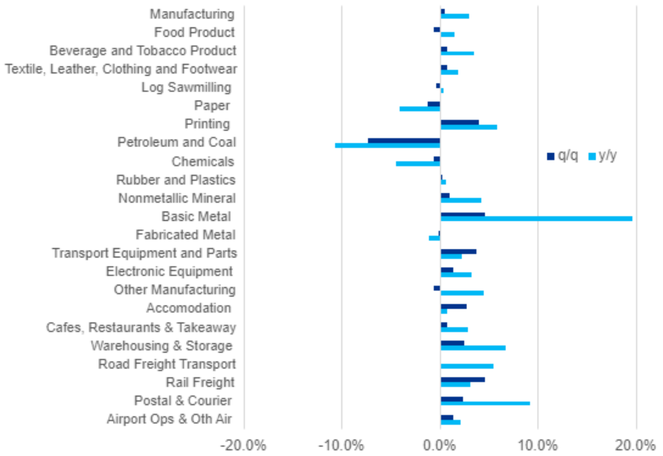
Producer Price Index

The producer price index (PPI) increased by 1% q/q in the September quarter of 2024; the same as the rate of growth experienced in the June quarter 2024. Annual PPI growth dropped from 4.8% y/y to 3.9% y/y as the previously strong June quarter 2023 data (1.8% q/q) fell out of the annual calculation.

Prices for manufacturing output continue to moderate further, increasing by only 0.5% q/q and 3.1% y/y. This growth, albeit weaker, was still mostly driven by the increase in metal input costs, up 4.6% q/q and nearly 20% y/y. In the transport, postal, and warehousing services sector, prices were influenced by a combination of factors. Postal and courier pick-up and delivery services recorded price increases of 2.4% q/q, while road freight saw no movement in prices over the quarter.

FIGURE 11

Producer Price Index, Output Price Growth by Selected Industry Sectors, June Quarter 2024



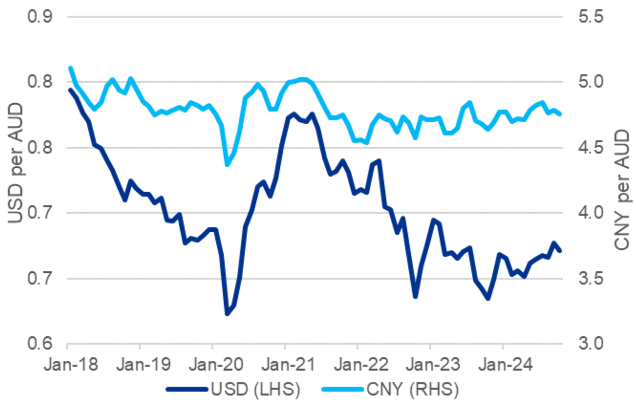
Foreign exchange

The Australian Dollar continued to trade in a narrow band for most of the year, with monthly average exchange rates staying between USD 0.653 and USD 0.677. At the time of writing the report (late November) the AUD/USD exchange rate had depreciated slightly to be slightly lower than USD 0.65, largely reflecting an appreciation of the USD following the recent US election which saw former President Trump re-elected.

While this largely reflects a flight to reserve currency due to uncertainty surrounding what trade and fiscal policies the new Trump Administration will enact, some of this strengthening in the USD is also in response to recent comments by US Fed Chairman Powell who suggested further cuts to the Federal Funds Rate did not need to be rushed.

FIGURE 12

Exchange Rate, AUD vs USD vs CNY



Wages

The national Wage Price Index (WPI) rose 0.8% in the September quarter 2024, and 3.5% for the year.

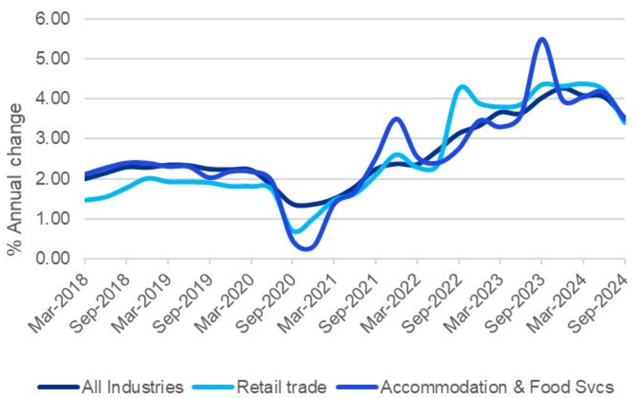
Consistent with the step down in the annual rate of growth in the national WPI, the Retail sector saw a *pullback in annual increases* in total hourly rates of pay excluding bonuses, down from 4.2% in the June quarter to 3.4% in the September quarter.

The Accommodation and Food Services sector also experienced a similar drop in annual wages growth, falling from 4.2% in the June quarter compared to 3.5% in the September quarter.

These drops in wage growth are also reflective of a lower increase in the national minimum wage and modern award wages as set by the Fair Work Commission, down from 5.75% for the 2023/24 year to 3.75% for the 2024/25 year.

FIGURE 13

Annual Growth in Wage Price Index by Selected Industry



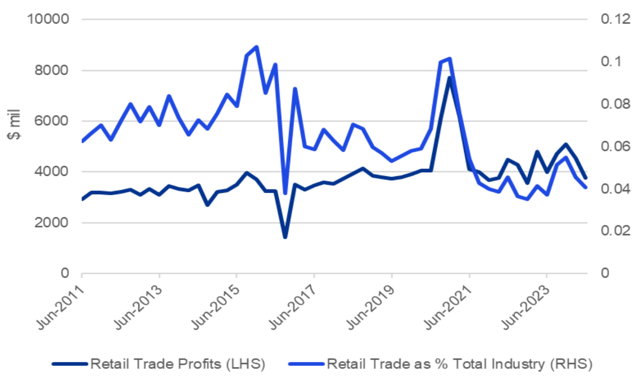
Performance indicators

Profitability

The retail sector achieved a slight improvement in overall margins during the June quarter, but **profitability remains below the average achieved during the decade to the end of 2019.** While the chart below suggests the retail sector has seen a solid uptick in its relative importance in generating profits compared to other industries, the (unfortunate) reality is that aggregate profitability across Australian companies went backwards in the June quarter 2024, thereby overinflating the significance in the slight improvement of the sector's recent profitability.

FIGURE 14

Retail Sector Profit Before Income Tax

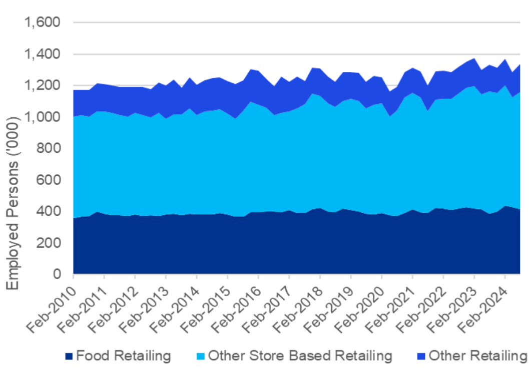


Employment

Total employment in the retail sector increased by slightly more than 50,000 people during the three months to August 2024, with around 1.34 million people now employed in the sector. The mix of employment continues to fluctuate on a subsector basis. Food retailing recorded a contraction in employment of around 14,300 workers between May and August, while Other store-based retailing and Other retailing experienced employment growth of just over 45,000 and 18,000 respectively during the same time.

FIGURE 15

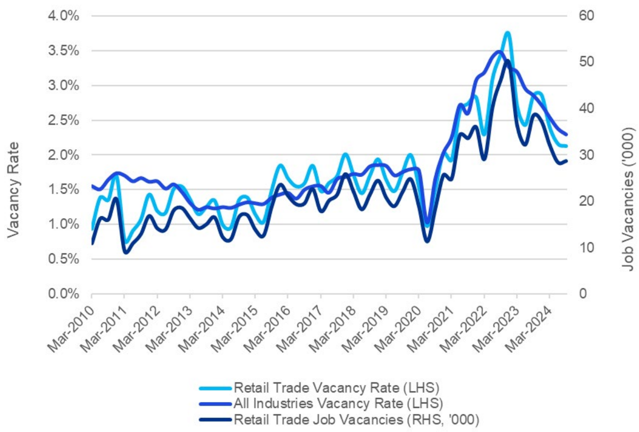
Retail Sector Employment, Australia ('000)



While the number of job vacancies in the retail sector lifted slightly during the September quarter 2024, the job vacancy rate fell slightly given the proportionally higher growth in employment within the sector. Further, the retail sector has continued with a relatively tighter job market than the economy, with the retail sector job vacancy rate running below the All-industry level now for three continuous quarters.

FIGURE 16

Job Vacancies

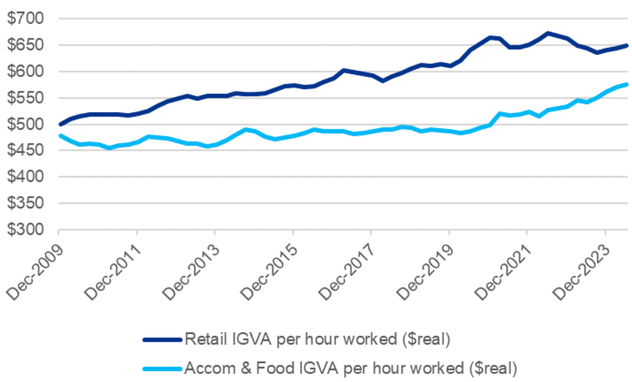


Labour productivity

KPMG has calculated a proxy labour productivity measure using real Industry Gross Value Added and hours worked. Labour productivity for the retail sector stopped declining in late 2023 and is now achieving a seemingly sustained recovery. The Accommodation and food sectors continue to see a strong kick-up in labour productivity, growing well above the rates achieved during the previous decade.

FIGURE 17

Labour Productivity Estimates



Online indicators

Online retail sales

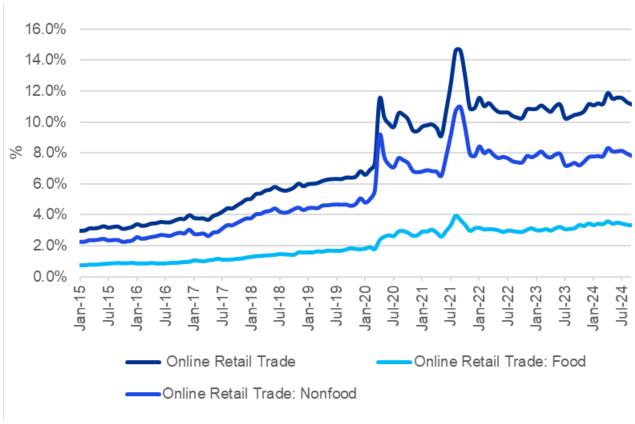
Online retail sales have experienced a contraction in activity across both food and non-food categories during the September quarter, with total online activity falling -1.4% during the three months to September compared to total retail sales growth of 1.0% for the same period.

Total online retailing sales, in seasonally adjusted terms, was $12,355.8 million in the September quarter 2024, down from $12,584.4 million recorded in the June quarter 2024. **The proportion of online sales to total retailing correspondingly fell from 11.7% to 11.3% over the September quarter, although it is still comfortably above the equivalent ratio of 10.3% recorded in the September quarter 2023**.

The proportion of online food retailing sales to total food retailing for the September quarter 2024 fell slightly from 8.8% to 8.5%, while the proportion for online non-food retailing sales to total non-food retailing fell from 13.6% to 13.2% over the same period.

FIGURE 18

Online Retail Sales by Type as a Proportion of Total Sales



Online shopping behaviour and working from home

The latest biannual University of Sydney Transport Opinion Survey (TOPS), prepared by the Institute of Transport and Logistics Studies (ITLS), also reveals online spending by households has fallen over the six months to September 2024 despite the proportion of Australians shopping online increasing over that time.

Specifically, the survey found that online shoppers in Australia spent about $388 on average in the four weeks prior to the survey period (being 2 September 2024 to 11 September 2024), which is about 6% less than the equivalent spend recorded in March 2024 ($413).

Consistent with the ABS data discussed above, the latest TOPS findings reiterated that online spending in Australia has been growing over the previous 18 months.

Survey respondents in NSW and TAS/ACT/NT spent the highest amounts online, averaging $417 and $477 respectively in four weeks.

The survey results also suggest buying behaviour can oscillate over time. For example, while the number of respondents purchasing online in TAS/ACT/NT declined in the latest survey period, the average spend by those purchasing online increased significantly such that total spending by those respondents online would have been materially greater compared to their spend 12 months previous. Conversely, participation in online shopping increased significantly in WA over the past year, but average spend fell by proportionally more such that total online spending by WA residents was lower during the current survey period compared to last year.

FIGURE 19

Proportion of TOPS Respondents by State who made an online purchase in the previous 4 weeks, Sept 2023 & Sept 2024 (%)

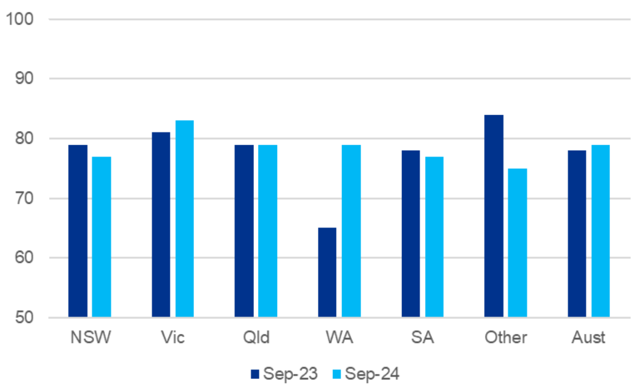
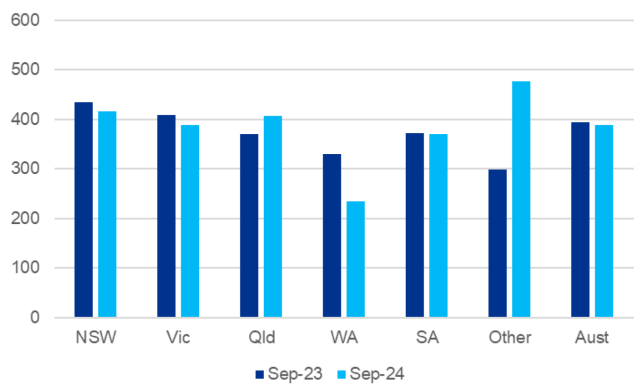


FIGURE 20

Average online spend per TOPS Respondent by State during the previous 4 weeks, Sept 2023 & Sept 2024 ($)



Technical appendix

The KPMG Retail Health Index (RHI) provides an assessment of the health of the Australian retail sector based on households' and producers' data available at a quarterly frequency. It represents the common component of series covering consumer behaviour and retailers' production.

A leading framework for the construction of an economic index from multiple time series is the so-called factor model. The factor model suggests the existence of a small number of unobserved series, called factors, which drive the co-movements of the observed economic time series. Leading applications of the framework includes the New York's FED Weekly Economic Activity Index.

In our application, we assume that there is a single factor, RHI_t, that drives co-movements of the retail variables, X_t

$$X_t = \Lambda RHI_t + \epsilon_t,$$

where Λ captures the factor loadings and ϵ_t refers to the idiosyncratic dynamics.

And the common method for estimating the unobserved factors is by principal components. In other words, principal component analysis is a dimensionality reduction method that is often used to reduce the dimensionality of large datasets, by transforming a large set of variables into a smaller one that still contains most of the information in the large set of variables. That is, principal components are constructed components from linear combinations of variables which best explain the variance in the data.

The RHI is computed as the first principal component of four quarterly variables: retail volume, the producer price index (PPI), the retail sector wage price index (WPI), and the Westpac–Melbourne Institute's consumer sentiment index. These data are then transformed to year-on-year growth terms. All transformed series are then standardised to have a mean of zero and a standard deviation of one. Furthermore, the growth rates of wages and prices are reversed for the purpose of interpretation, i.e. higher wages and costs mean the retail sector is not doing so well.

Table T.1 below shows the respective weights of each variable on the RHI, and the total variance explained by the RHI.

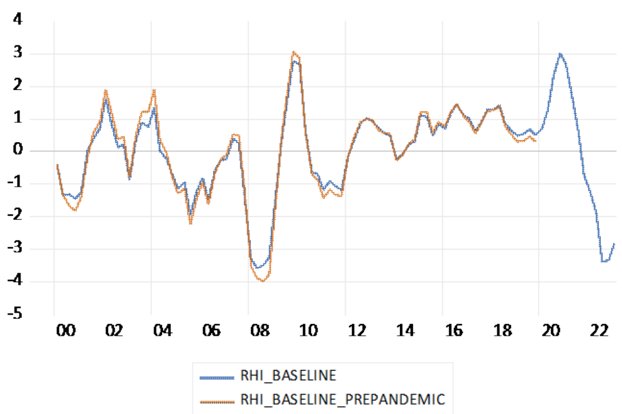
Table T.1 – RHI Weights

Variables	Weights	
	Baseline	Baseline Pre-pandemic
Producer Price Index	0.64	0.64
Wage Price Index	0.47	0.47
Consumer Sentiment	0.56	0.57
Retail Sales Volumes	0.24	0.22
Total Variance Explained	0.49	0.48

Source: KPMG

The first column provides the weights using the full sample between the March quarter 1999 to the March quarter 2023. The second column shows the weights using the pre-pandemic sample for the baseline, which are little changed from the full sample weights. The pre-pandemic RHI, as a result, remains quite similar to the full sample one (Chart T.1).

Chart T.1 – RHI Baseline & Pre-pandemic Baseline



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December 2024 | 1535655274TL