BNZ Weekly Overview

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Mission Statement

To help Kiwi businesspeople and householders make informed financial decisions by discussing the economy and its implications in a language they can understand.

Business Sentiment Collapse Impact

Business sentiment in New Zealand started collapsing back in September last year when opinion polls began to show a strong probability that Labour would lead the next government. The ANZ's monthly measure went from +18% in August to zero in September, -10% in October, then -39% in November which is basically where it sits now having hit -50% in August this year.

Has this collapse in business happiness about where the economy is headed been reflected in spending indicators? Certainly not retail spending. Core retail spending volumes in seasonally adjusted terms rose by 1.7% during the December quarter, 0.7% during the March quarter, and 1.4% in the June quarter. The more up to date but not entirely accurate data from debit and credit card spending shows that in the September quarter core spending surged another 1.9% in nominal terms.

So consumers have continued to spend up large and given that consumer spending makes up about 65% of activity in the economy it would be hard for businesses to argue that their pessimism is justified because people have shut their wallets since September.

What about jobs growth? This is harder to make definite statements about for a couple of reasons. One is that employment is a lagging indicator. It takes some time before changes in the economy feed through to changes in the pace of jobs growth. The other is that there have been shortages of staff across a massive range of sectors in NZ for a few years now and trying to fill vacant positions can keep labour demand and job placements high even if employers are pulling back from creating new positions.

But it is hard to conclude that employers have in fact gone into their shells in light of the still very strong labour market measures. After soaring 2.2% in the September quarter of last year one would normally expect the following quarters to be quite weak simply reflecting the volatility in the employment measure in the Household Labour Force Survey. But jobs still grew by 0.4% in the December quarter, 0.6% in the March quarter and 0.5% in the June quarter – delivering 3.7% growth over the past year.

But the ANZ Business Outlook survey shows that whereas in August last year a net 17% of businesses said they planned hiring more people, now a net 1% say they plan laying some off. The NZIER's quarterly survey however shows the latest level of employment intentions to be a net 13% positive compared with 19% a year ago. The ten year average reading is 12% so one cannot unequivocally claim that businesses have pulled back strongly from seeking new staff.

In fact the NZIER survey tells us that a net 44% of businesses still find it hard to get skilled staff and a net 29% are struggling even to get unskilled staff.

Is it worth looking at data on exports to see if collapsed confidence has had an effect? Not at all. Primary sector volumes and values reflect growing conditions and global prices. Tourist numbers reflect decisions of travellers and movements in the exchange rate.

What about business investment? Surely if businesses are depressed they won't invest. It is unfortunately near impossible to develop an up to date view on business capital spending changes because the data are simply not available. Import value changes reflect decisions made potentially a long time in the past. Non-residential construction consent values likewise can reflect processes which started years ago. But it may be worthwhile noting that the value of such non-residential consents has risen 5% in the past year for the business sector. Growth was 9% a year earlier but the change doesn't really tell us much.

What about investment intentions? In the monthly ANZ survey they are at a bad -9% from +22% pre-election. In the NZIER survey they are at 4% from 17%. Businesses are clearly indicating less willingness to invest and that is concerning in an environment not just of low productivity growth but a growing need to invest to handle the accelerating speed of change in most sectors.

Based on the limited data in hand the case can be made that businesses are backing up their high pessimism with reduced capital spending but that they have pulled back much less when it comes to hiring people. And that pretty much takes us right to the heart of one of the key problems in our business sector – long-term underinvestment and reliance for growth upon hiring disposable people under the assumption that the country is awash with skilled, motivated people just waiting to be plucked from the dole queue and put to useful purposes.

Given that the labour market is likely to get a lot tighter, businesses are going to face some huge challenges in coming years because of the way they are stepping back from investing. This will show through on average in returns on equity, share prices, and competitiveness against offshore alternatives.

Much as we can all see some exciting businesses springing up and growing in NZ, from the macro point of view from which I see things, the fundamentals argue in no way for improving productivity and therefore national income growth rates.

But for now the majority of the big macro influences remain on the positive growth side – low interest rates, 8% fall in the NZD in the past year, stimulative fiscal policy with more loosening coming, good export commodity prices, average-like trading partner growth, and low inflation. But just to reiterate some key points we have been making here for some time, business pricing ability to recoup rising costs and maintain margins has collapsed in the face of new technologies allowing us consumers to easily find alternatives. The unsettling speed of change in operating environments facing businesses is fast and likely to get faster. Staff availability is likely to worsen further. Staff turnover is rising and that means loss of meta-knowledge plus extra recruitment, training and retention costs. And then there are whatever imposts the new government brings along.

If I Were A Borrower What Would I Do?

Although New Zealand's annual inflation rate has just lifted to 1.9% from 1.5% the underlying measure I look at which excludes volatile food and energy items only rose from 1.1% to 1.2%. There is little evidence as yet of any decent acceleration in wages growth outside the public sector. Businesses struggle to raise selling prices. And the Reserve Bank have said they will discount the effect on inflation of the shift in petrol prices.

Chances are not high that the RB will cut the official cash rate, but raising the rate from its current 1.75% still does not look imminent. If I happened to get struck once more by the property bug and purchased again I would be inclined to fix most of my mortgage interest rate for two and three year periods.

The Weekly Overview is written by Tony Alexander, Chief Economist at the Bank of New Zealand. The views expressed are my own and do not purport to represent the views of the BNZ. **This edition has been solely moderated by Tony Alexander.** To receive the Weekly Overview each Thursday night please sign up at www.tonyalexander.co.nz
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