29 June 2017

NZ Business Reality Trumps (Political) Uncertainty

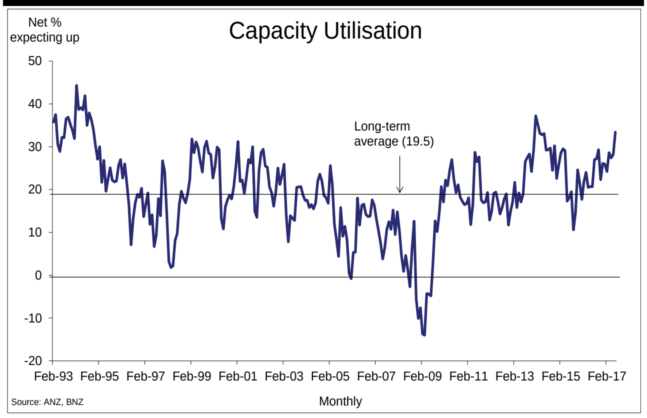
- NZ businesses beefing up their optimism
- Despite the election and other supposed uncertainties
- Agriculture very much joining the party
- Capacity constraints are clearly biting
- Pricing gauges sustain 2%-plus inflation pulse

With the word "uncertainty" being bandied around a lot lately, and a local election fast approaching, the reality is that New Zealand's business sector is full of confidence and expectation. This afternoon's ANZ business outlook survey, conducted in June, provided the latest proof. Far from doing a nervous Nelly, its net confidence index strengthened to +25, from +15. Own-activity expectations burgeoned to +43, from +38. These results were better still when we seasonally adjust them, and consistent with annual real GDP growth in the order of 4%.

Not that the NZ economy will be able to achieve such a strong degree of expansion as that. Not from the starting point we have, where capacity constraints are biting on most fronts. This is starting to seriously limit the wherewithal to grow, even though the demand side indicators are pushing hard for it. In this we continue to ask questions of those who judge that the economy is not only devoid of resource pressures but is still running some spare capacity. The Treasury took this line in the May Budget, and we strongly beg to differ.

We believe next week's NZIER Quarterly Survey of Business Survey (QSBO) will support our view; indeed will keep supporting our view, in that it has increasingly touted capacity constraint messages for a number of quarters now. More broadly, of course, the QSBO will no doubt echo the positive messages we've seen in this afternoon's monthly ANZ survey, as tends to be the case.

Stretch



ANZ Bank Business Outlook				
Net balance - next 12 months				
(All sectors)	**June**	**May**	Change	Average
General business outlook	**24.8**	**14.9**	9.9	10.9
Own business	**42.8**	**38.3**	4.5	27.4
Profits	**29.9**	**27.7**	2.2	9.8
Employment	**24.3**	**23.6**	0.7	8.2
Investment	**27.4**	**23.5**	3.9	13.9
Pricing intentions	**31.1**	**30.2**	0.9	20.9
Inflation expectations	**2.03**	**2.00**	0.03	2.64
Exports	**27.0**	**31.3**	-4.3	30.5
(Own activity outlook)				
Retail	**29.8**	**21.8**	8.0	25.3
Manufacturing	**25.5**	**37.5**	-12.0	29.4
Agriculture	**53.3**	**33.3**	20.0	22.8
Construction	**46.2**	**44.0**	2.2	18.8
Services	**46.3**	**44.3**	2.0	30.6

But this is not to overlook the capacity utilisation index in the ANZ survey. While this is supposed to be a change variable – is capacity utilisation expected to increase or decrease – it seems to have elements of a "levels" indicator as well. In the least, it suggests capacity constraints are coming into play, with little sign of spare capacity to begin with. The direction is undeniable.

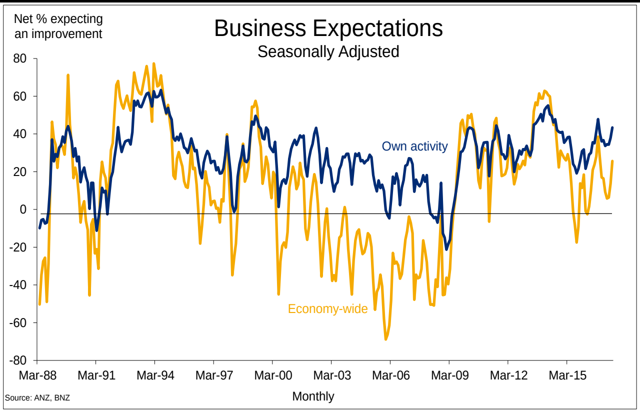
Our view on capacity pressure is integral to the inflation risks we believe the RBNZ is taking with its low-for-much-longer approach on its Official Cash Rate, which is already at a record low. Something has to give, at some stage. But the Reserve Bank does not appear to be in any mind to do so anytime soon, judging by the OCR missive it issued last week.

To be sure, the near-term CPI outlook has been dampened by the recent drop in oil prices, and the recent wriggle higher in the New Zealand dollar.

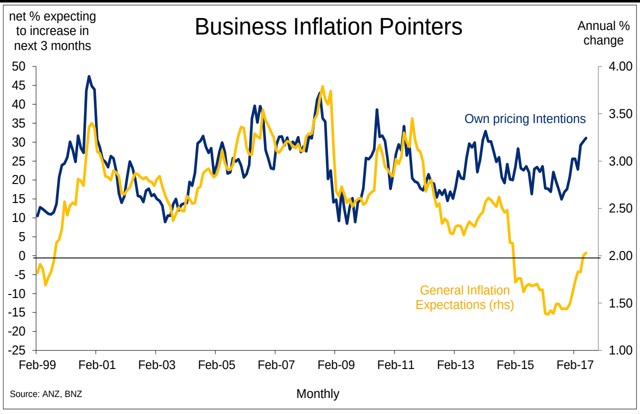
However, it would be a bold person to suggest that inflation will fade away as an underlying issue, when we have not only such a stretch of capacity, but respondents to today's business survey expressing a firm intent to raise prices. The degree of it – a net +31, from +30 in May – was consistent with annual CPI inflation running at 2% if not closer to 3%. While this might struggle to be the outcome for the headline CPI over the near horizon, it's something to bear in mind regarding the various core rates of inflation out there, many of which have lifted to around about 2% already.

Also from a general perspective, it's interesting to note that inflation expectations in today's ANZ business survey come in at 2.03% this month, from 2.00% in May. This consolidates quite some rebound, since a 1.38% low back in March 2016.

More Solid



Firm



While the generalities of today's business survey were certainly firm, there were a few details which are worth commenting on.

For instance, it's been agriculture that has boosted the ANZ survey the most over recent months. Then again, this simply reflects the strength we're seeing in commodity export prices, and for reasons far beyond the normalisation in dairy returns. And it's not as though the other sectors have fallen by the wayside. Services are still vying with agriculture for the most optimistic, and retail and manufacturing respondents have certainly improved in confidence compared to just a few months ago.

As for the construction category of the ANZ business survey, while it was still reasonably positive with regard to activity, it was less so than earlier in the year. And its confidence in the general business outlook was now lagging the pack, for the second month running. Yet its employment intentions were still leading from the front and its investment intentions series was still substantially north of its long-term average.

In the least, the mixed messages we're getting from the construction industry make it one to keep an eye on, and keep thinking about. In this vein, we can imagine that resource and costs pressures are assailing it more than most, and that, given the vulnerability inherent in high property prices, financing issues might also be coming into play for some.

craig_ebert@bnz.co.nz

Contact Details

BNZ Research

Stephen Toplis
Head of Research
+(64 4) 474 6905

Craig Ebert
Senior Economist
+(64 4) 474 6799

Doug Steel
Senior Economist
+(64 4) 474 6923

Jason Wong
Senior Market Strategist
+(64 4) 924 7652

Main Offices

Wellington
42-52 Willis Street
Private Bag 39806
Wellington Mail Centre
Lower Hutt 5045
New Zealand
Phone: +(64 4) 473 3791
FI: 0800 283 269

Auckland
80 Queen Street
Private Bag 92208
Auckland 1142
New Zealand
Phone: +(64 9) 976 5762
Toll Free: 0800 081 167

Christchurch
111 Cashel Street
Christchurch 8011
New Zealand
Phone: +(64 3) 353 2219
Toll Free: 0800 854 854

National Australia Bank

Peter Jolly
Global Head of Research
+(61 2) 9237 1406

Alan Oster
Group Chief Economist
+(61 3) 8634 2927

Ray Attrill
Global Co-Head of FX Strategy
+(61 2) 9237 1848

Skye Masters
Head of Interest Rate Strategy
+(61 2) 9295 1196

Wellington

Foreign Exchange	+800 642 222
Fixed Income/Derivatives	+800 283 269

Sydney

Foreign Exchange	+(61 2) 9295 1100
Fixed Income/Derivatives	+(61 2) 9295 1166

London

Foreign Exchange	+(44 20) 7796 3091
Fixed Income/Derivatives	+(44 20) 7796 4761

New York

Foreign Exchange	+1 212 916 9631
Fixed Income/Derivatives	+1 212 916 9677

Hong Kong

Foreign Exchange	+(85 2) 2526 5891
Fixed Income/Derivatives	+(85 2) 2526 5891