15 January 2019

QSBO Highlights Cyclical Stretch

- **Improved QSBO consistent with trend growth**
- **Albeit as capacity constraints still biting hard**
- **Pricing intentions middling rather than soft**
- **Employment gauges positive re Q4 HLFS**
- **QSBO solidity should hold the RBNZ's attention**

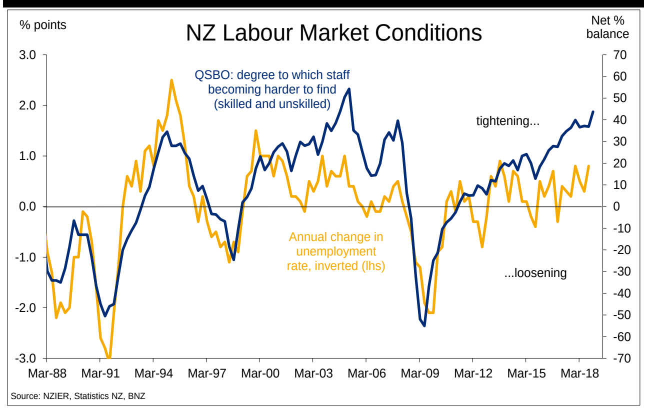
Just how hot is the NZ economy? Judging by pricing intentions in this morning's Quarterly Survey of Business Opinion (QSBO), not very. But look at the survey's capacity constraint variables and it's clear the economy is relatively heated. And that this is likely to remain the case for a while yet, with the QSBO's improved growth measures more consistent with annual GDP running around trend (2.5-3.0%).

This backs up the view on the NZ economy we've largely stuck with, throughout the recent slump in business confidence. Or less of a slump, as today's NZIER survey showed, with net confidence at -17%, from -30% in the previous quarter. Sure, it's still negative, but less so.

In any case, the real news (as usual) lay in the QSBO's own-activity expectations, cost and pricing variables and, especially this time around, its supply-constraint metrics.

What jumped out at us in today's business survey was the degree to which staffing constraints amped up anew. Just when there were signs that the worst might be over (in a relative sense), a net +53% of respondents said that sourcing skilled staff was becoming more difficult, from +44% in Q3. For unskilled staff the number jumped to +35%, from +29%. Each is the highest this cycle.

Even Tighter



QSBO - Summary of key results

Net % of respondents	Sep-18	**Dec-18**	Expected 3m ahead
General Business Situation (next 6m)	-30	-17	
- s/adj	-28	-18	
Trading Conditions (s.a.)	flat	+4	+17
Capacity Utilisation	93.2%	92.8%	
Plant & Mach invest (next 12m)	-5	-4	
Building investment (next 12m)	+4	+7	
Employment	-3	+5	+13
Profitability	-23	-22	-15
Selling Prices	+23	+20	+21
Costs	+44	+47	+36

And each is comparable to the extremes experienced over the previous economic cycle (2003-2007).

Over the previous cycle, of course, the unemployment rate ultimately raked down to 3.3%. New Zealand is most of the way back down there now, with 3.9%. There might be technical/timing issues that bump the jobless rate up bit in the Q4 Household Labour Force Survey (HLFS), due 7 February. However, today's QSBO indicates the labour market retains a fundamental momentum, and stretch.

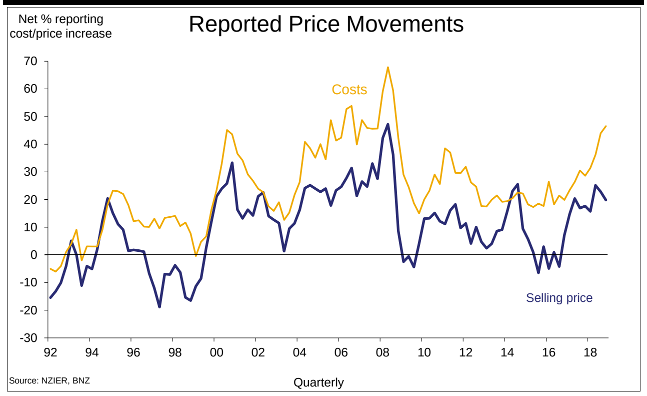
Like most of the activity indicators in today's QSBO, employment reports regarding the last 3 months firmed up – to +5, from -3 in Q3. Employment expectations simply stayed robust, at +13. Both variables are now comfortably above their respective long-term averages (going back to 1970).

To be sure, the QSBO's capacity utilization variable, CUBO, was off a bit. But at 92.8% in Q4 it was still way above trend, and from a Q3 reading (93.2%) that was very close to the all-time high.

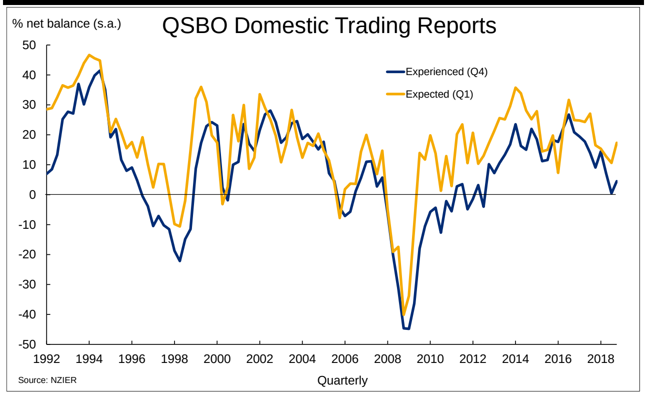
So it remains a bit perplexing that pricing signals are not stronger than they are. Indeed, pricing reports eased a bit to a net +20%, from +23%, and pricing expectations moderated to +21%, from +28%.

Even so, they are simply more middling now, than anything weak. As such, they still suggest that CPI inflation is trending close to 2% per annum. This is even though headline CPI inflation itself might struggle to reach this magical mark over the nearer term. Speaking of which, we still expect the Q4 CPI to come in flat, which would trim its annual rate of inflation to 1.8%, from 1.9%. That report is due Wednesday next week (23 January).

Squeezed



Trend-Like

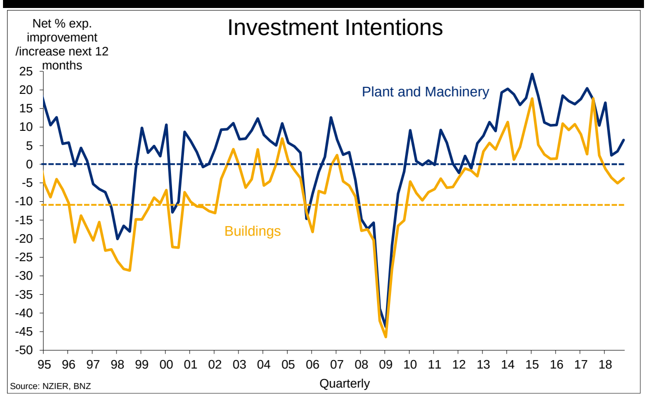


The lack of force in the QSBO's selling price series is not for any lack of cost pressure. In fact, messages regarding the latter became stronger in this morning's QSBO. A net +47% of firms reported increased costs over the trailing three months. But there remains a sense that firms can't pass this on, which is reflected in profitability still being nibbled back (albeit not to especially weak levels per se).

By and large, however, the local business sector appears to be trundling along not too badly. Sure, the way ahead might get choppier, if only for the slowdown in the international economy presently playing out. However, for the meantime, there is little sign that this is affecting, or spooking, NZ firms.

The QSBO fix on GDP growth was certainly a shade more encouraging. Domestic trading conditions improved from the previous survey. The view on the last 3 months (call it Q4) lifted to 4%, from flat. Trading expectations for the coming 3 months strengthened to +17% from +11%. This is broadly consistent with GDP running around trend.

OK, Actually



This, in turn, leaves us comfortable in forecasting a 0.8% expansion in Q4 2018 GDP, and annual growth of 2.6% for calendar 2019. The risk was that today's QSBO growth indicators sagged further, questioning our view in this respect.

What of those who say the NZ economy can't possibly be overheating, because CPI inflation is still under control? We'd suggest a broader look around. And a chat with the NZ business sector, whose resources are demonstrably stretched. If that's not a tried and true indicator of the economic cycle, we don't know what is.

In this sense, today's QSBO should be plenty enough to hold the RBNZ's attention.

But as for what the Bank is actually thinking on the economy, it looks like we'll have to wait for its next meeting/MPS. This isn't until 13 February. We are not aware of any speeches by Reserve Bank officials beforehand. And the customary New Year address by the RBNZ Governor to the Canterbury Employers' Chamber of Commerce looks to have been consigned to history, as a scene-setting event for the markets.

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 Markets Strategist
+64 4 924 7652

Nick Smyth
Interest Rates Strategist
+64 4 924 7653

Main Offices

Wellington
Level 4, Spark Central
42-52 Willis Street
Private Bag 39806
Wellington Mail Centre
Lower Hutt 5045
New Zealand
Toll Free: 0800 283 269

Auckland
80 Queen Street
Private Bag 92208
Auckland 1142
New Zealand
Toll Free: 0800 283 269

Christchurch
111 Cashel Street
Christchurch 8011
New Zealand
Toll Free: 0800 854 854

National Australia Bank

Ivan Colhoun
Global Head of Research
+61 2 9237 1836

Alan Oster
Group Chief Economist
+61 3 8634 2927

Ray Attrill
Head of FX Strategy
+61 2 9237 1848

Skye Masters
Head of Fixed Income Research
+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