Research

Economy Watch

23 May 2025

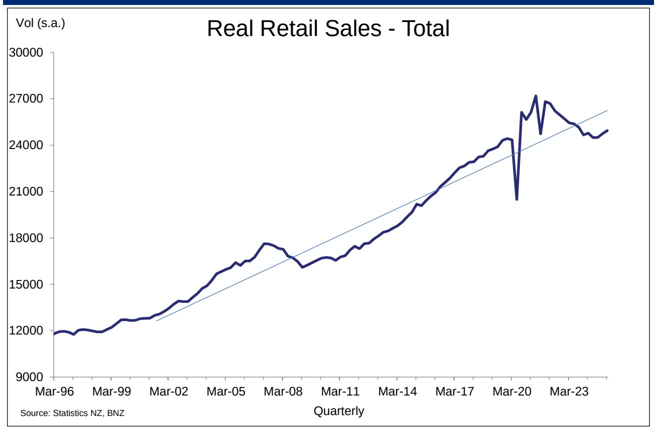
Retail Recovery From Weak Base

- **Retail sales stronger than expected**
- **South Island outperforming North Island**
- **Profitability likely to lag**
- **We nudge up our Q1 GDP forecast to +0.4%**
- **Nothing to stand in the way of the RBNZ**

Retail sales volumes increased 0.8% in the March 2025 quarter. This was well above both our forecasts and market expectations for 0.0%. Combined with +1.0% in the previous quarter, it suggests retail sales volumes are growing at an annualised pace of 3.6%.

While the latest lift in consumer spending is encouraging, it's important to remember that any recovery will be coming off a very weak base. Retail conditions have been extremely challenging in the last three years, with sales volumes still 8.3% below their peak level in mid-2021, and 11.9% below in per capita terms. These sorts of levels do not suggest that retail activity is surging away.

Lifting from a weak base

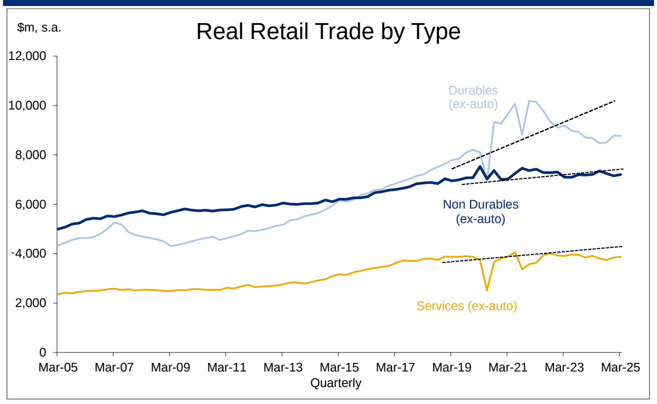


In the details, the data were not quite as firm as the +0.8% headline first appears. Core retail sales volumes (excluding autos) lifted 0.4% in the quarter. The difference between the headline and core measure was largely due to a 3.1% lift in motor vehicles and parts. We have been wary of this difference before, as the larger weight for vehicles in the retail trade survey is one of the reasons retail can diverge from private consumption in the GDP national accounts.

On our calculations, durables (ex-auto) volumes fell 0.1% in the March quarter. This is consistent with household budgets still under significant pressure. Elevated costs for essentials such as food, insurance, and rents have left households with little choice but to cut back on discretionary spending.

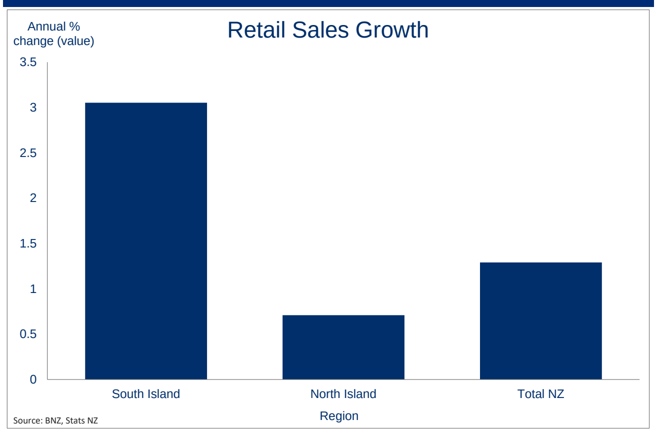
In contrast, services (ex-auto) lifted +1.0% in the quarter. This was likely supported by the ongoing (gradual) recovery of international tourism. On a seasonally adjusted basis, visitor numbers increased another 1.1% in the March 2025 quarter. The third category, non-durables (ex-auto) increased by 0.7% in the quarter.

Durables flat



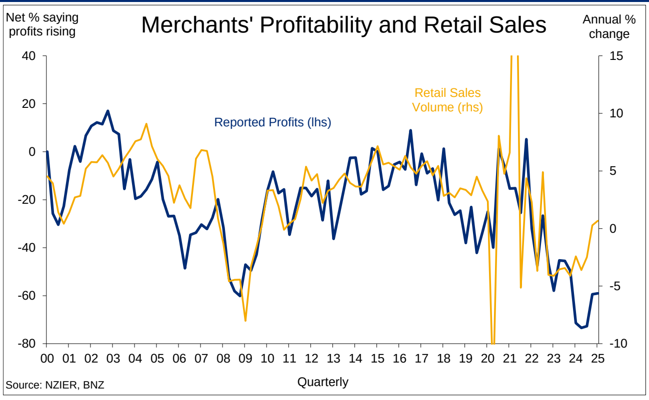
Growth in the South Island continues to outperform the North. Retail sales values in the South Island are up 3.1% on a year ago, compared to 0.7% for the North Island. This likely reflects both the recovery in tourism (with visitors to Queenstown well above pre-Covid levels) and a greater exposure to the agricultural sector which has been supported by high commodity prices.

South Island outperforming



For many retailers, it will likely take some time before it begins to feel like a recovery. According to business price data, retail input costs have increased significantly since pre-Covid, and margins appear to have been squeezed as firms have seemed unable to pass on higher costs. So, while retail sales volumes appear to have turned a corner, the same cannot said for profitability. Indicative of this in the March Quarterly Survey of Business Opinion, a net 59% of merchant respondents reported a decline profitability over the last quarter.

Profitability lagging

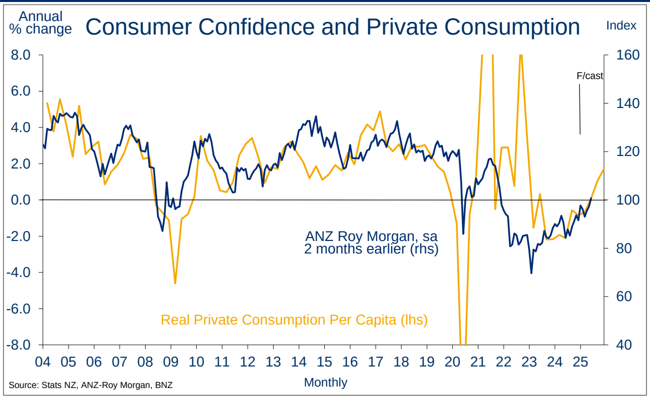


Today's data add to a growing weight of evidence that the economy is slowly turning a corner. Retail trade is the first major GDP partial for Q1 2025. Following today's release, we have nudged up our GDP forecast from 0.3% to 0.4% for the quarter. The RBNZ forecast 0.6% for Q1 GDP in its February MPS.

We don't think the 0.4% lift in core retail sales volumes for Q1 will move the dial for the RBNZ. The Bank has already pencilled in a 0.5% increase in private consumption for the quarter and will also be monitoring more timely indicators such as the PSI and electronic card transactions (which remained subdued in April) to assess the recovery in household spending.

The big question is where will spending go from here? We remain cautious about the trajectory given the multiple headwinds still faced by households. Their concerns are revealed in the weakness we continue to see in consumer confidence. Confidence is headed in the "right" direction but it will need to push much higher to be consistent with the sort of recovery most forecasters, including ourselves, are projecting.

Further improvement required



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