ANZ Research

Quarterly Survey of Business Opinion – 2021 Q3

5 October 2021

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Capacity constraints are biting

The bottom line

The September quarter QSBO showed that firms are continuing to grapple with increasingly intense capacity constraints. We now know that COVID restrictions are, on balance, a supply shock – ie they reduce economic activity while driving up costs and prices, and clogging up the labour market.

Reported trading activity increased in Q3, despite our expectations that GDP will contract on the back of renewed lockdowns.

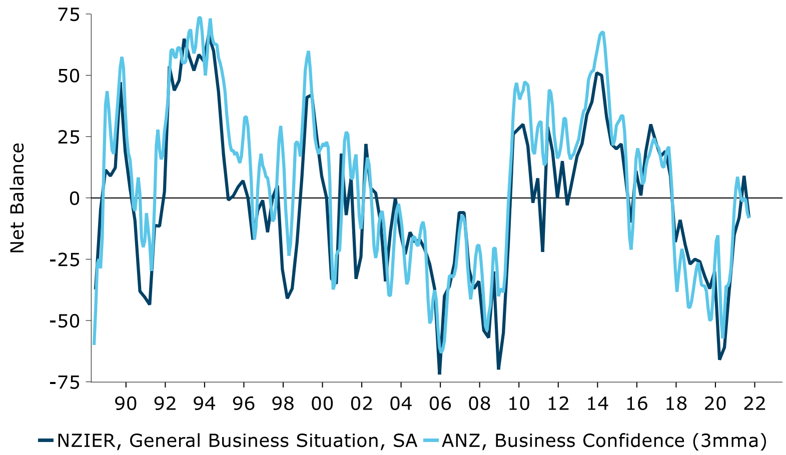
Experienced and expected costs and prices both fell sharply in the September quarter, inconsistent with the ANZ Business Outlook. But we think that's a bit of a red herring given that the CUBO measure of capacity utilisation reached a record high of 96.1%, and difficulty finding labour remained around record highs too – that's going to matter more for inflation pressure and for the RBNZ tomorrow.

Key points

The September quarter Quarterly Survey of Business Opinion (QSBO) showed that economic confidence took a hit in Q3 due to lockdown, while capacity constraints and labour shortages remain acute.

- **Businesses sentiment robust:** Business confidence ticked down to -8 in in the September quarter (+9 previous). That's still well above confidence levels immediately prior to the first lockdown in 2020, despite the country spending half of the quarter at Alert Level 2 or higher (figure 1). That's consistent with the September read of our Business Outlook. All up that probably speaks to firms' optimism that once we get past the current lockdown, the economy should rebound strongly. But the longer that takes, the higher the chance that sentiment could sour, and investment and employment plans get shelved.

Figure 1. Business confidence



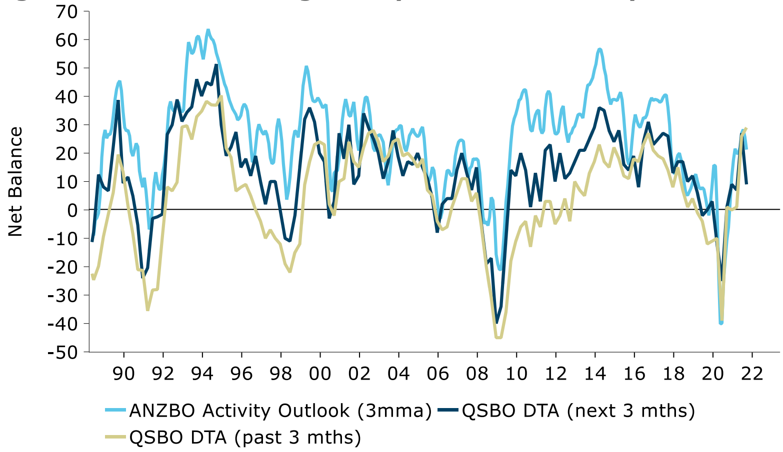
Source: NZIER, Macrobond, ANZ Research

Data summary

	Latest
Headline business confidence (actual)	-11
Headline business confidence (sa)	-8
Domestic trading activity (sa, past)	29
Domestic trading activity (sa, expected)	9
CUBO (actual)	96.1%
Avg selling price – next 3 months	4

- **Experienced domestic trading activity increased,** with a net 29% of firms reporting higher activity over the quarter, up from 26% previously (sa). That's a bit of a surprise, given that we're expecting a roughly 7% fall in GDP over Q3, and we saw actual reported activity drop sharply in the ANZBO as well. Expected economic activity ticked down sharply to 9, from 27 previously (figure 2).

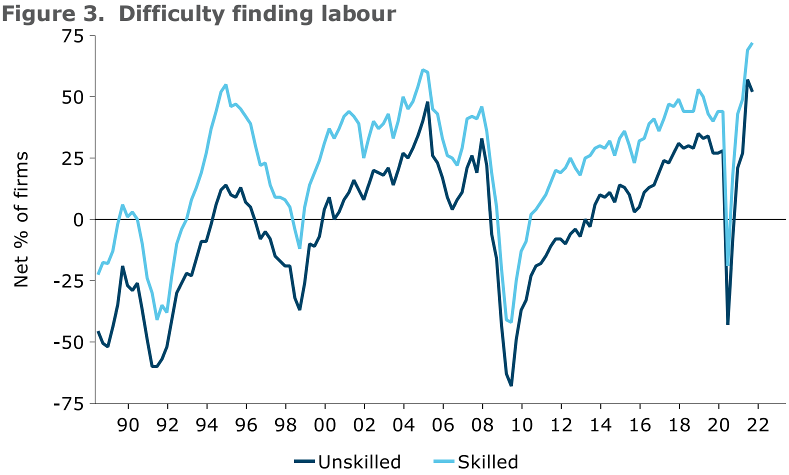
Figure 2. Domestic trading activity and ANZBO activity outlook



Source: NZIER, Macrobond, ANZ Research

- **Labour shortages are acute:** While lockdown has seen actual activity measures fall, it's done nothing to ease the extreme labour shortages firms were grappling with previously. Employment intentions remain firmly positive, with a net 42% of firms expecting to increase headcount over the next 3 months. Difficulty finding skilled and unskilled labour remains around record levels (figure 3).

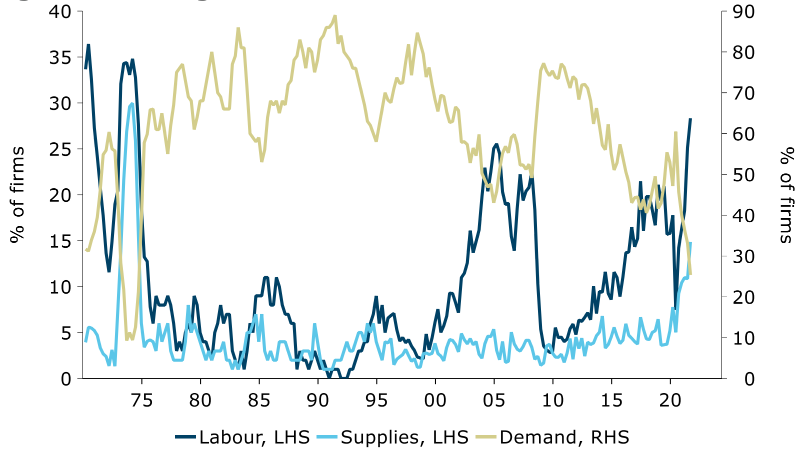
Figure 3. Difficulty finding labour



Source: NZIER, Macrobond, ANZ Research

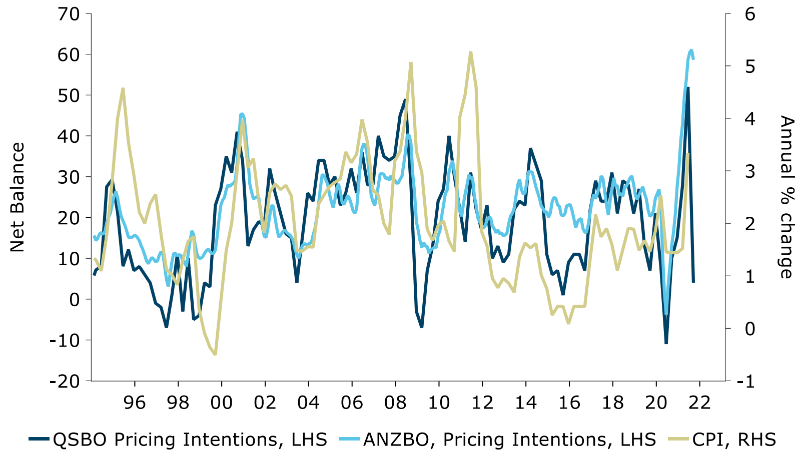
- **Capacity constraints are getting more and more extreme**, with a historically high proportion of firms pointing to labour and materials shortages as limiting turnover. By contrast, lack of demand is now less of a constraint than at any time since the oil shock of 1973 – the textbook supply shock (figure 4). These supply pressures and associated rises in costs have already shown up in consumer prices – and we think that these strong price rises have some way to go yet. We expect that CPI inflation peaked at 4.2% y/y in Q3.
- **Price and costs fall a red herring:** Strangely, the QSBO reported a very rapid reduction in the share of firms reporting higher costs and prices in the September quarter. That could reflect that the survey was conducted from 2 August to 27 September –during most of this time, all of New Zealand was in some form of increased Alert Level. But the sharp fall in prices (and costs) seems inconsistent with both the still-extreme levels of price pressure reported in the ANZBO (figure 5), as well as other measures in the survey, which show ongoing tightening in capacity constraints. The CUBO measure of capacity utilisation reached a record high of 96.1% in the September quarter – in a survey going back to the 1960s. So for now, we're not going to take much signal from the reported drop in costs and prices in this data. Capacity constraints remain intense – and that's ultimately what's going to drive inflation pressures higher.

Figure 4. Limiting factors



Source: NZIER, Macrobond, ANZ Research

Figure 5. Pricing intentions and CPI inflation



Source: Stats NZ, NZIER, Macrobond, ANZ Research

What does this data mean for the RBNZ? Looking through the considerable noise, it's another green light for beginning their long-expected OCR hikes. Monetary policy is a tool designed to stimulate/reduce demand by lowering/raising interest rates and making it cheaper/more expensive to spend today. But when you've got an economy that's recording record high levels of capacity utilisation and difficulty finding labour, adding demand via low interest rates is simply pouring fuel on an already roaring fire.

The RBNZ have emphasised that reduced monetary stimulus is needed to avoid overshooting their targets – and for us, today's data confirms that this is a real risk despite the likelihood of prolonged lockdown in Auckland – and the very real risk that the rest of the country will find itself under more onerous restrictions before long. We continue to expect the RBNZ will raise the OCR 25bps to 0.5% at tomorrow's meeting. Of course, that's not to say there aren't risks. For example, momentum and confidence could wane as lockdown drags on, hitting investment and employment. But since lockdown started, most of the data we've seen has actually been surprisingly robust. Indicators such as our ANZ card spending data show that so far, we've been able to keep operating far better than 2020. We think the least regret for the RBNZ is still to stabilise the economy by gradually lifting the OCR to a rate that is no longer stimulatory (we think that's around 1.5%), while being prepared to pause or even reverse course should downside risks eventuate.

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Last updated: 3 September 2021

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