ANZ Research

Quarterly Survey of Business Opinion – Q2 2022

5 July 2022

Contact

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Data summary

	Latest
Headline business confidence (actual)	-65
Headline business confidence (sa)	-62
Domestic trading activity (sa, past)	-1
Domestic trading activity (sa, expected)	-11
CUBO (actual)	93.4%
Avg selling price – next 3 months	76

Inflation blues

The bottom line

The Q2 Quarterly Survey of Business Opinion (QSBO) displayed similar themes to our ANZ Business Outlook: businesses are very downbeat; activity indicators are weak; cost and pricing intentions are far too high, with capacity constraints acute (an inflation intensification story); employment intentions are faring a little better than most indicators.

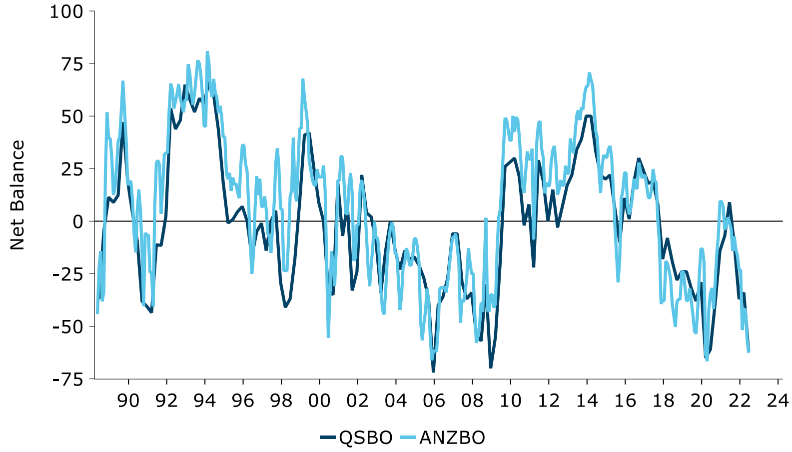
For broader economic momentum, it seems the only way from here is down. That's not to say the economic fundamentals have suddenly broken; rather, the economy is running out of resource to grow (labour in particular). And while there's bound to be an element of worry about the demand outlook too (given interest rates are on the rise and the housing market is in retreat), demand driven by a rapid increase in debt (both Government and household) was never going to be sustainable.

In this environment, the only thing left for policy makers to do is focus on withdrawing demand and boosting supply. Trying to boost growth by adding to demand will only exacerbate the inflation problem. For the RBNZ, we see nothing in these data to stand in the way of 50bp hikes in both July and August. The RBNZ needs to be convinced that inflation pressures are softening, and that's not what these data are saying (yet).

Key points

- **Businesses sentiment deteriorated** in Q2, to levels typically associated with economic contraction. A net 62% of respondents expect conditions to deteriorate, versus 34% in Q1 (seasonally adjusted, figure 1). Looking through the noise, it's very similar to our Business Outlook in Q2. Surging costs, acute capacity constraints, rising interest rates, falling house and asset prices, and ongoing COVID and economic uncertainty are a toxic mix. But that won't stop the RBNZ from hiking – it needs to get inflation down before it becomes embedded, causing long-lasting economic damage.

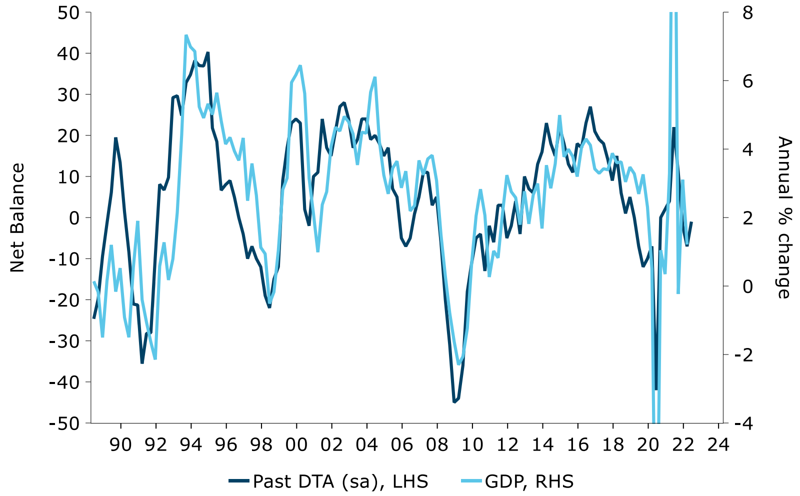
Figure 1. Business confidence



Source: NZIER, Macrobond, ANZ Research

- **Experienced domestic trading activity (DTA) lifted 6 points** on a seasonally adjusted basis, but at -1% this measure suggest economic activity is struggling (figure 2). COVID-related volatility in the GDP data has seen the relationship between experienced activity and GDP break outside historical ranges in recent quarters, but given the noise in annual GDP growth (eg base effects from lockdowns), we'd actually put more weight on DTA (and our Business Outlook) than on GDP for a steer on underlying economic momentum right now. Indeed, our forecast for 4.8% y/y growth in Q3 2022 is not nearly as impressive as it sounds when you consider the fact that the economy contracted 3.8% q/q in Q3 2021! Meanwhile, expected trading activity for the next three months (Q3) fell, with a net 11% of firms expecting activity will decrease. All up, these data suggest downside risk to our expectation for broader economic momentum over 2022. Recession risks are building.

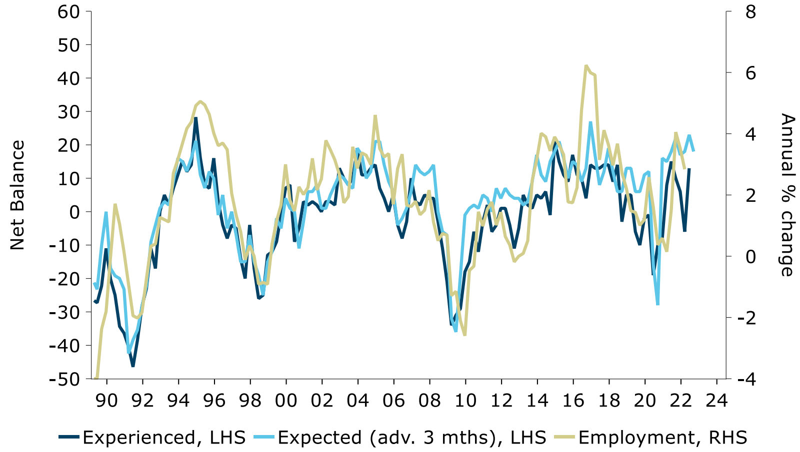
Figure 2. Domestic trading activity and ANZBO activity outlook



Source: NZIER, Stats NZ, Macrobond, ANZ Research

- **Employment is bouncing back from Omicron.** A net 13% of firms reported increasing headcount in Q2, versus 6% of firms reporting lower headcount in Q1. Given that we saw more Omicron disruption over Q1, that's not a surprise. It's a similar pattern to what we've seen in the monthly filled jobs data, with job numbers bouncing back solidly over April and May. The forward-looking measure of employment remains robust, with a net 18% of firms in Q2 expecting to increase headcount, versus 23% in Q1. The persistent gap between actual and expected employment in the QSBO likely reflects the sheer difficulty in finding workers. Firms need to increase headcount to meet demand – but with the domestic labour supply pretty much tapped out, hiring remains slow.

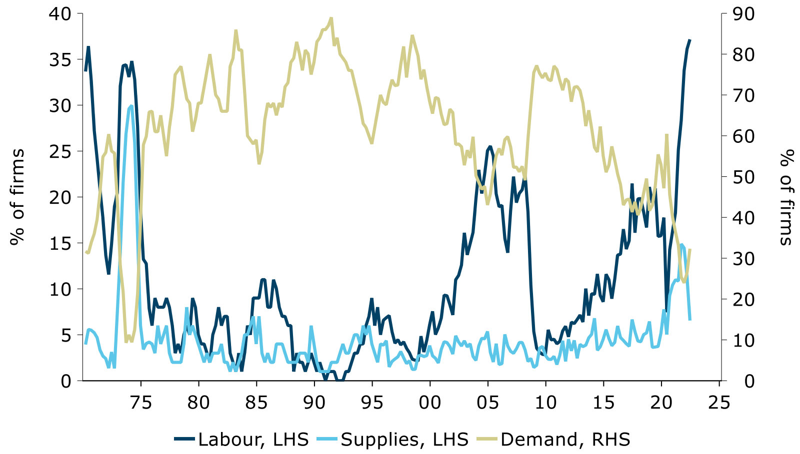
Figure 3. Employment



Source: Stats NZ, NZIER, Macrobond, ANZ Research

- **Labour still the most limiting factor**. The CUBO measure of capacity utilisation remained high at 93.4% in Q2, but the RBNZ will welcome the reduction from Q1's record high of 97.1%. That said, this measure has been very volatile in recent quarters. Broadly speaking, we remain in uncharted territory in terms of overall capacity utilisation. The biggest constraint on firms expanding their production remains labour. Demand is still a relative non-issue. Given recent volatility, any indication of capacity pressures easing in these data is not overly convincing. If anything, we expect labour shortages to get worse over 2022, with domestic labour demand remaining intense and Australian job ads at record highs.

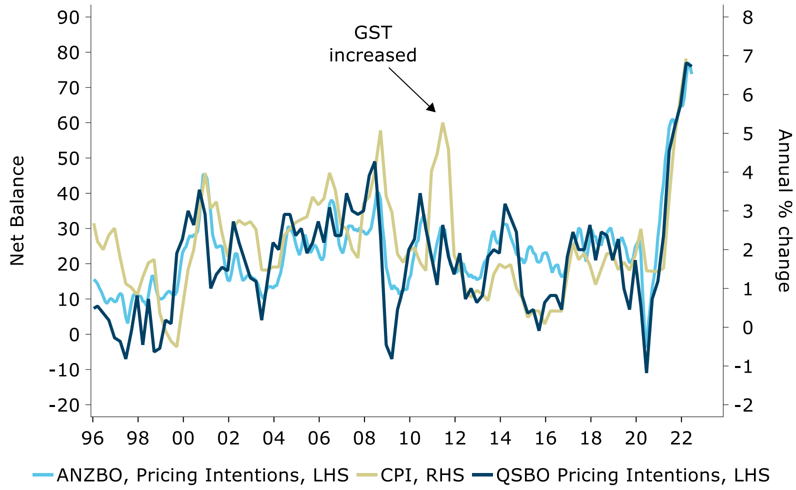
Figure 4. Limiting factors



Source: NZIER, Macrobond, ANZ Research

- **Price and costs still too high:** Cost and pricing measures for Q2 increased – that's consistent with our expectation that CPI inflation will accelerate a little further in Q2 (data out 18 July). Cost and pricing expectations for the next three months (Q3) remained at very high levels (relatively stable versus the Q1 read). To be comfortable that inflation is well and truly on the way down, the RBNZ will want to see a significant improvement in these inflation indicators. While we expect that softening demand over the second half of this year will generate the fall in inflation that the RBNZ is looking for, evidence of such a decline is yet to be seen in these data.

Figure 5. Pricing intentions and CPI inflation



Source: NZIER, Stats NZ, Macrobond, ANZ Research

Weakness in this quarter's QSBO was particularly concentrated in construction, with highly acute labour shortages and other capacity constraints clearly weighing. Consistent with our outlook for residential construction, architects are now reporting a shrinking pipeline of housing-related activity for the 12 months ahead. It's even softer 12-24 months ahead. Commercial and Government workflow are at positive levels for the next 12 months, suggesting it's not all one-way traffic.

All up, we don't see a lot of new news in the QSBO. It's the same broad story as our Business Outlook, with cost and inflation indicators still far too high for the RBNZ to pause for breath just yet. With a fresh wave of Omicron seemingly brewing, supply disruptions seem likely to remain the dominant economic force for some months yet, despite the clear housing slowdown.

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