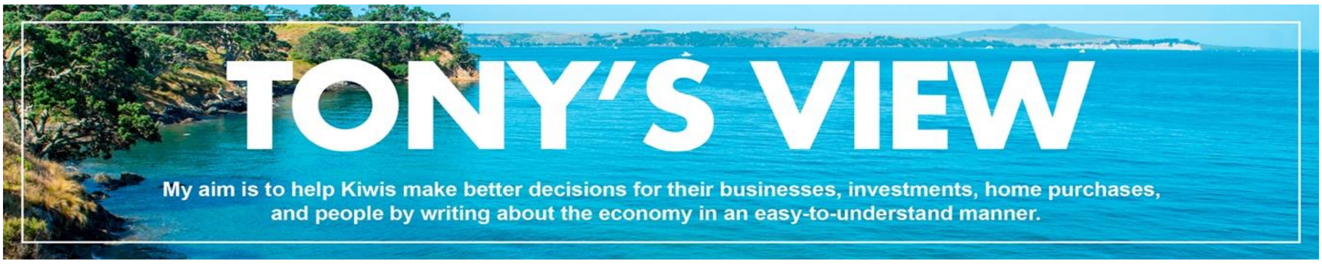

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Consumer spending shifts

Most weeks I deliver a webinar and make one or two in-person presentations around the country – when not on the Gold Coast – and speak with reporters. One question which has come up a couple of times this past week was about defensive portfolio positioning in these uncertain times.

I am not an active investor myself, have no required qualifications which would allow me to give investment advice, and don't undertake any comparative analysis of portfolio assets. That is, I don't track share prices or indices, have no database on commercial property yields, and don't peruse the lists of fixed interest securities on offer.

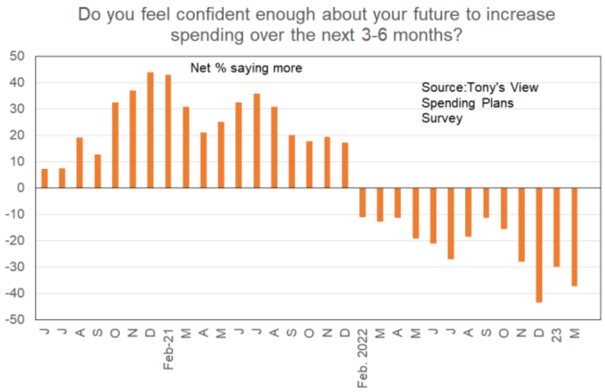
Instead I concentrate on the overall economy and the housing market in particular for which my audiences are general Kiwis, SME owners, property transactors, and house owner-occupiers generally and especially first home buyers.

But this doesn't mean the data I gather, analyse, and report on cannot yield some useful insights for investors, especially when it comes to the quarterly survey of people's portfolio intentions run with Sharesies.

This week I ran and yesterday released the results of my monthly survey of people in their capacity as consumers. The headline result was a deterioration in spending intentions to the second worst on record. There is probably a downward bias to the results brought about by the shock of the recent extreme flooding events and that means the Reserve Bank also will take the results plus other data gathered in recent weeks with a grain of salt. At face value quite a few releases in the near future might justify an ending or announced scaling back of the monetary policy tightening cycle – but the Reserve Bank will feel times are too uncertain to take that side-step at the moment.

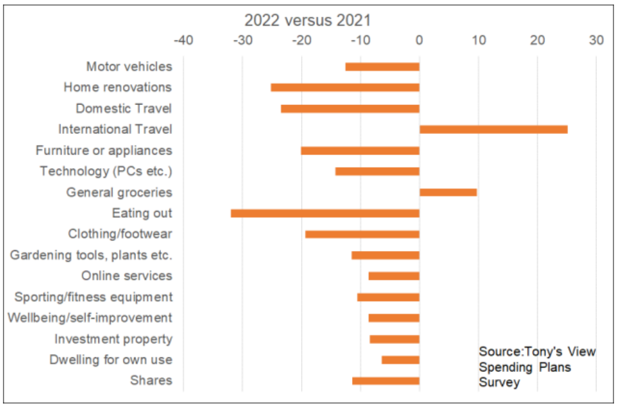
One thing I can do with my Spending Plans Survey is see which areas of spending people indicate they will cut back the most on when times get tough. Doing this can show where spending may have greatest capacity to bounce back when good times return. This exercise can also potentially give active investors some insight into portfolio positioning changes through the economic cycle.

So, what I have done is compare readings for each identified area of spending plans for 2022 versus 2021. The graph here of the overall spending intentions measure shows why I have chosen these calendar year comparisons.



Spending plans were positive through all of 2021 and negative through all of 2022.

The average 2021 reading was +27% and the 2022 reading -20%, so the change is -46%. We can calculate the shifts across all categories and graph them as done here.



International Travel shows the strongest uplift as our confidence levels have collapsed. This has nothing to do with our budgets or outlook and entirely reflects revenge travel desires after having the borders closed for over two years.

The lift in General Groceries reflects the strong price rises for things which we eat and have no choice but to keep doing so.

That brings us to the rest. Our plans for eating out have declined more than for any other area of household spending. I do however question the extent to which we are following up on this expressed change in our spending plans. Were we really slashing eating out plans the shortages of hospitality staff would surely not be as intense as they are.

Next biggest change is for Home Renovations. There is an effect running through here which is the opposite of that for International Travel. During the pandemic we could not travel so we shouted ourselves better living conditions. Upgrades which we had been planning to do perhaps this year or through to 2025 have already been done.

For operators in the home renovations sector conditions are going to be very challenging for the next couple of years.

Our Domestic Travel spending plans have fallen sharply. But again, there will be a pandemic effect at work here. People could not go offshore so they hit the road either staying in motels or travelling with caravans on in motor homes.

That binge has ended and is unlikely to come back for a while – especially with the new disincentive to travel by road of the dysfunctional ferry service across Cook Strait. But operators in the sector can expect an offset from foreign travellers heading our way – then going home with shocking stories of our prices, roading quality, and ferry service.

Next biggest change is in the areas of spending on Furniture and Appliances plus Clothing and Footwear. Finally we are getting close to normal cyclical spending change territory – except that there is probably an element of binge spending on new furniture ending as the pandemic has ended.

Not everyone upgraded their living environment by renovating their home. Some people will have simply modernised their furniture and old appliances. But this area of spending is traditionally one which varies widely over the economic cycle and weakness here is not too surprising.

The weakness for Clothing and Footwear reflects cutting back on discretionary spending as we tighten our belts to provide money for higher debt servicing costs and groceries not to mention insurance and utilities.

The area of spending showing the smallest change is a Dwelling For Own Use. But as we know, activity in this area has fallen substantially with January's real estate sales the weakest in at least three decades for instance. The relatively small change reflects the fact that relatively few of New Zealand's 5.1 million people are in the market for a change of owned house at any time.

What do these results suggest for when the current tight conditions pass? First, when times improve be prepared for many people not buying into it. In New Zealand we often focus more on the things going wrong and points of pressure on particular groups than on the things going right which can make this a good country to live in.

But still people spend, look to buy a house, plan for their long-terms here, and thoroughly enjoy themselves in a beautiful environment. Acknowledge areas of challenge and the fact not everyone is having a good time, but learn to step aside from the sometimes dystopic views of collapse you are frequently presented with and focus on underlying positives. These can include the impact of new infrastructure developments making far flung land more valuable for living and operating from, plus trends in population growth.

One of those for the next 2-3 years will be the return of good population growth in Auckland now that net migration flows are once again positive and the pandemic-induced shift of some people to the regions earlier than they planned has ended – with some reversal likely.

From an investment portfolio point of view what does our analysis of 2022 versus 2021 Spending Plan averages tell us? For those who are active investors awareness of the recovery which will eventually come for depressed areas of consumer spending indicated above may suggest counter-cyclical purchasing opportunities currently. These might be shares, struggling businesses bereft of sufficient cash reserves or credit access, commercial premises, and well run franchises.

These opportunities come on top of those which have been presented by the pandemic temporarily depressing some parts of the country.

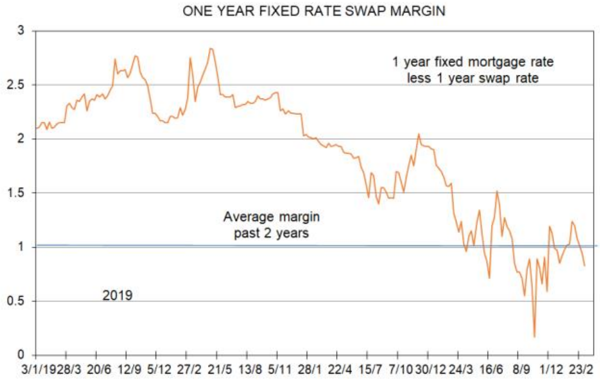
I guess the best focus might be to identify areas and assets which have been depressed by the pandemic and may remain so, and also are now depressed by the weakening of the economy and depressed consumer sentiment. Some double-barrelled counter-cyclical investment opportunities are probably sitting out there still for those with the capital and the timeframe to wait for the double whip back the other way.

If I were a borrower, what would I do?

I would fix one year but not totally discount fixing for two years. Inflation is proving harder to suppress than hoped internationally so we have to be open to the possibility that monetary policy here does not ease as soon as many of us have pencilled in for 2024.

This week bank costs of borrowing in the wholesale markets at fixed rates in order to lend fixed have risen about 0.2% and now sit 0.4% - 0.65% higher than four weeks ago. These rises almost entirely reflect a change in expectations for United States monetary policy with inflation looking likely to persist longer than thought and requiring tougher monetary policy over there.

The following graph is one which I include each week in Tview Premium and it shows the margin between a bank borrowing one year fixed and lending one year fixed. Note the fall most recently.



Will banks respond to the hikes in fixed rate borrowing costs by raising their fixed rates anew? Probably not. There is little new business being written because of weakness in the residential real estate market. But there is high vulnerability to the loss of existing customers should one not have a competitive rate when people renew the rates on their $170bn worth of debt in the next 12 months.

Nothing I write here or anywhere else in this publication is intended to be personal advice. You should discuss your financing options with a professional.