

The economic outlook from your consultants

What we have said

In September 2007 we asserted that the country was going into a consumer recession. However, we pointed out that consumer spending is one of at least six distinct causes of demand and that others such as government, infrastructure construction and primary production would continue to enjoy strong demand although tourism and other construction would begin to wane.

In February 2008 we warned that rising commodity prices – not just oil but costs as diverse as shipping (the BDI) and cabling – would savage growth in the English-speaking world as budget over-runs finally caught up with sources of demand (and it became significantly more expensive to build a house than buy one)

In April 2008 we warned of an inability to secure funding by financial institutions, four months before the 'credit crunch' was a concept widely understood. In May 2008 we began undertaking recessionary planning with clients.

In July 2008 we said we were about to enter the worst period. Across the board, August was the worst month by far for the majority of our clients. We also began taking bets (for a case of wine) on a 'double-dip' recession on the basis that the underlying problems had yet to emerge and be resolved.

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Why do we get it right more than most other people you hear?

1. We understand economic theory
2. We draw deeply from a wide pool of external information such as The Economist and The Harvard Business Review
3. We are in touch with economic reality
4. We pull in the objective information from our clients, pool our observations and make our predictions collectively
5. We don't have to grab headlines or sell newspapers – so we don't have to be alarmist, one way or the other – we just have to **get it right**.

See the back page for a more detailed explanation of who to listen to – and why.

What are we saying now?

Until 14 Feb 09 (Short-term)

1. Discretionary spend will be at an all time low for businesses and consumers except those unaffected by the recession (and we estimate 15-20% of all businesses are counter-cyclical).
2. Uncertainty will prevail over both finance and demand and FX rates will frequently over-react in response to the slightest political expression globally.
3. Central bank rates will continue to be cut aggressively but little of that will be enjoyed by the NZ end borrower who will not see better than 7-7.5% on home loans.
4. Trust between countries importing and exporting will be eroded in many instances as developing world businesses default on their orders.
5. Bankruptcies will peak in the first quarter but this will be masked by a greater number of businesses being absorbed by others.

From Feb to October 09 (Medium-term)

1. Stagflation will hamper some countries as governments with floor-level interest rates can only create economic stimuli through government spending and printing money. NZ interest rates have greater room to be reduced but will not enjoy as drastic a cut due to the inflationary pressures of a low exchange rate – we will continue to have the highest base rates in the OECD.
2. Global commodity prices will stabilise and then begin a slow upward trend.
3. Businesses will invest in sales initiatives (with little liability) but capital investment will remain low, hampered by the FX rate.
4. Tourism will prove surprisingly resilient and primary producers will continue to enjoy a favourable exchange rate and labour conditions.
5. The balance of power will lie firmly with employers during the medium-term, especially if the 90-day probation period is passed quickly in Parliament.
6. Wise manufacturers/distributors will look to more established, local, trustworthy suppliers (as cheap suppliers in some parts of the world become increasingly unreliable).
7. There will be considerable consolidation in industries with large proportions of owner-operators (from plumbing to trucking to IT). Larger suppliers to these industries will benefit but many smaller services firms will struggle throughout the year.
8. Capital investment will remain low creating substantial opportunities for outsource service provision.
9. NZ daughter companies of multi-nationals will remain constrained by headcount freezes as their parent companies claw back cash, happy to lose market share.
10. Retail spending will settle at levels slightly lower than those enjoyed since 2005 but luxury or bigger-ticket items (anything you could get finance on from TVs upwards) will remain stagnant. The larger high-street players will be reluctant to sacrifice market share and unwilling to acknowledge a structural reduction in spend by consumers who will find the price of petrol and food slowly returning to 2008 levels by the second half of 2009

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After October 09 (Long-term)

1. Capital investment will not return to levels needed to increase productivity until mid 2010 although productivity will make some gains as employees comply with their employers needs more enthusiastically.
2. A significant proportion of multinationals will remain hampered by a lack of funding centrally and will run a tight ship centrally and for their daughter operations, both to impress investors/rating agencies and because of a lack of clear direction – leaving them weak and slow to respond to local markets.
3. The ability of the new NZ govt to affect productivity and emigration – or the constraints placed upon it by its partners and its inheritance - will become clear in the second half of 2009.

What should clients do?

Keep things tight and accept uncertainty until 1 Feb 09 and use this time well to [prepare](#) for a **golden period** of market share acquisition during Feb-Oct 09.

Actively consider the consequences of the economic climate on their business and [follow the BMC's 10-point Action Plan for 2009 which can be found here](#).

The critical commodity for the next 12 months will be courage (where it has been staff, certainty and cash latterly) – does your business have courage?

How will this focus on economic forecasts benefit our clients?

The BMC will release an **Economic Outlook** whenever we believe the previous one needs updating (expect Jan/Feb 09 for the next). The format will be loose but it will generally discuss forces affecting demand and the forces affecting supply and contain predictions for the short, medium and long-term.

Will this comment on foreign exchange (FX) rates? Only when there is substantial good reason to take a definite position. The structural exchange rate – driven by a country's balance of payments and productivity – is easily assessed, however a million market forces (and many political ones) cause short-term volatility and enormous fluctuation from that structural exchange rate

Will this comment on unemployment or interest rates? Yes in a broad sense it will, though it will focus more on the consequences of this to the markets, customers and needs of clients of The BMC than numerate predictions.

This forecast will normally be accompanied by a series of recommended actions – just as the recessionary advice suggested clients return purchasing authority centrally and increase QA on materials received from suppliers, so this forecast is accompanied by a [10 Point Action Plan](#) assisting clients to be best placed to succeed in 2009.

[Read a copy of The BMC's 10 Point Action Plan for the next 10 weeks](#)

So why are some information sources more likely to be wrong?

The January Shark - A lazy media swing from the complacent to the hysterical in their need to boost numbers and sell advertising – that's why there is bound to be a shark scare in the newspapers in the second week of January again this year. This is not economic journalism, just uneducated sensationalism.

Self interest - In the absence of other qualified commentators, the financial organisations in NZ play a leading role in shaping public opinion. They are the loudest voice on the effect of macro-economic conditions on business and domestic finance and they use this position to increase their profits by inflating concerns, keeping charges high and then withdrawing from lower margin activity.

Poor data – The real estate market is often headlined by the median or mean property values; this is a worthless statistic being such a gross indicator. Median value per sq m might be indicative of a trend, but median value can be skewed so easily by a small portion of transactions it is unreliable – and the use of unreliable data is in many ways worse than no data at all.

Delayed data – Xmas retail figures for instance are initially based on the GST returns received from larger retailers. Smaller outfits who return twice-monthly or six-monthly are calculated on a historic ratio of their proportion of the whole. Every time Rebel Sport displaces a local sports store or a florist sells more gifts to businesses than shoppers, the retail data will be out – and over-optimistic – for some time to come, as M Cullen had to concede earlier this year.

Crowd effects – All significant commercial organisations do not want to be the first to report losses but once the flood-gates are breached, want to release all their bad news quickly. Everyone (customers, staff, suppliers) needs to believe that the business will survive – just – but that painful measures are necessary. Figures that were once manipulated upward are just as easily manipulated downward when it suits.

Ignorance – A significant proportion of people in a position to make statements on economic issues have never experienced a major downturn and do not have the ability to identify or predict the consequences. They are only familiar with positive forces and until recently thought (like so many before over the past few hundred years) that we were in a 'new economic age – an era when the cycle of boom and bust had finally ceased'

Optimism – Optimism is a character trait which is, from an evolutionary perspective, desirable. Unfortunately it does lead people to overlook or discount risks or problems with which they are less familiar, less comfortable or less able to control. A good economic commentator should start from the facts and work back, not their feelings and work forwards. Consultants are by definition dispassionate and realistic about the economic climate and its impact on markets and businesses.