

Retail Outlook

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A quarterly analysis of the Retail Sector
prepared for the New Zealand Retailers Association

April 2009

Winning the ugly contest

- NZ better placed than most to weather the current downturn (*front page*).
- Top 10 tips to manage your business (*inside*).
- Consumer confidence down but not out (*back page*).

So far this year, the indicators for the New Zealand economy have yielded few surprises: consumer spending remains soft (particularly durable items), business confidence is subdued, unemployment is creeping higher, and house sales appear to have stabilised at a slower pace. Our latest GDP figures showed that the economy shrank by 0.9% in the December 2008 quarter, rounding off a full year of contraction, and we estimate that there was a similar decline in the March 2009 quarter. The local business environment is undeniably tough at the moment, but it is playing out much as expected.

Unfortunately, the same can't be said for the rest of the world. New Zealand's major trading partners are expected to contract by 2.2% this year, which would mark the worst slowdown since at least the 1930s. The pace of the downward revisions to world growth forecasts has been breathtaking: just six months ago, these same countries were expected to grow by 2.5% this year. Policymakers are taking drastic steps to try to revitalise their economies, but the drop in global production and trade now has some real momentum and New Zealand will not be immune.

Indeed, it would be foolish to be complacent about the impact the global downturn will eventually have on the NZ economy. Hence, our most recent forecasts see the economy continuing to contract through most of 2009. But there are some factors working in our favour, which so far

have helped NZ avoid the extremes we've seen overseas. These include:

- **The NZD:** the exchange rate is acting as a significant buffer for the NZ economy by improving export returns at the farm gate;
- **A robust banking system:** there are less than 20 AA rated banks in the world, 4 of which are in NZ;
- **The credit channel here is not broken:** credit growth in the year to February 2009 was 3% for households, 22% for agriculture, and 11% for other businesses;
- **Monetary policy traction:** the US, UK, Australia and NZ have all cut their official cash rates by close to 5%. However, while the pass-through in NZ and Australia was immediate, in the US and the UK it took over a year before the central banks got traction through lower mortgage rates;
- **Fiscal stimulus:** estimates put NZ's fiscal stimulus at around 5% of GDP over the period 2009-2010. That compares with packages worth around 4% of GDP in the US, 4% in Australia, and between 1%-2% in Japan and the UK. Moreover, we think there will be "more bang for the buck" in NZ and Australia, because the money does not have to be used for bank bailouts;
- **Labour market:** NZ has an extremely flexible labour market;
- **Migration:** net flows are turning around rapidly which should help support demand and the housing market; and
- **NZ exports basic stuff:** our product base is predominantly in food-related goods. While durable and luxury goods get hit hard in tough times, people still have to eat, meaning our exports should hold up better than most.

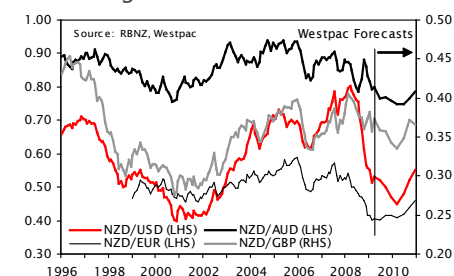
For businesses that are up against the wall, these factors will be cold comfort. But, for those that are managing to keep their heads above water or better (!), it is a case

of being thankful for small mercies. We like to think of NZ as winning the ugly contest: it may be ugly here, but rest assured it is far worse elsewhere.

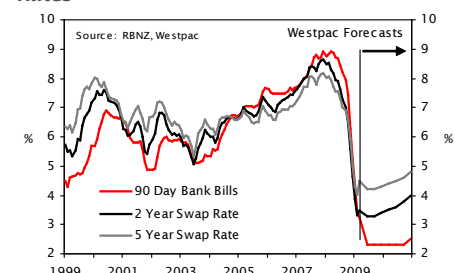
Despite these insulating factors, 2009 will still weigh up as a difficult year for many NZ businesses. We expect calendar GDP to contract by close to 3%, before picking up to around 2% in calendar 2010. Weak consumer spending will be a key feature through 2009 as rising unemployment ensures that the recent save-rather-than spend mentality dominates.

Interest rates and the exchange rate still have more work to do. We see the OCR hitting a low of 2% in July and remaining low for an extended period (i.e. through 2010). We continue to anticipate the NZD falling into the high-USD0.40's in the second half of the year.

NZ Exchange Rate



Short and Long Term Wholesale Interest Rates



Westpac

Managing your business through the downturn

Through these challenging economic times, it is more important than ever to get on top of all aspects of your business. In the following section, we provide 10 key tips to help guide you through the tough times and ensure that you are well positioned to benefit from the recovery when it eventually comes.*

1. Think cash flow, cash flow, cash flow

If one piece of advice stands above all others to position your business strongly to weather the current economic climate, it's this: be cash flow obsessed. Cash flow is the very life-blood of any business, and as soon as grim economic forecasts begin to hit the radar of industry, it can be the first thing to come to a screeching halt. We suggest developing a cash flow budget that records the amount of money that flows in and out of your business, so you can forecast the availability of cash for given time frames.

2. Revamp your receivables strategy

When areas of industry collapse or falter, a horrible but real possibility looms – that sales in your ledger may not turn into cash as soon as you'd hoped, or if you're unlucky, at all. People you do business with may fall on hard times – or some may go out of business altogether, taking the cash you're owed with them. Here are a few tips for getting paid quicker:

- Ensure that customers understand your payment terms.
- Offer incentives for early or cash payment and clearly communicate these to your customers – and where possible, seek payment up front.
- Offer a variety of payment options to increase the speed with which funds reach your account.
- For international customers, account for differences in the business culture that could lead to longer payment terms than those commonly adopted in NZ.

3. Understand your costs and control them

Before cutting costs, first and foremost, it's important to understand them. In times of economic crisis, businesses need to be highly strategic. Having your facts straight on costs is the ammunition you need in order to develop a smart attack on the challenges of the time. You should be asking yourself questions like:

- Do I know the true cost and profitability of everything we do? Our services? Our products? Our customers?
- What are our margins – do we have

room to cut costs and still remain profitable?

- Can we afford to add extra services, or will this compromise our ability to provide others?

4. Consider banking in one place

How many financial institutions does your business have accounts with now? If it's more than one, you could be missing out on getting a better deal for your business banking – by underestimating what a full financial relationship is worth to your bank and what they can offer you in return for it. On a practical level, it also means that your business banker can get a clearer picture of your business, engage with you more proactively and offer more valuable support.

5. Get the right loan type for the right purpose

It's important to remember to get the right loan for the right borrowing purpose. By doing this you can ensure your interest costs don't blow out unnecessarily, and that each of your lending facilities functions best for the need – for example a credit card for paying for taxis, a revolving overdraft facility to cushion cash flow, and an equipment finance loan for purchasing a capital asset.

6. Keep communicating your business point of difference

It's a time when survival is ever more dependent on your ability to have a point of difference – either something you do best, or something you offer that others can't – and to communicate it. Now may well be the time to allocate more resources to your marketing efforts, to fortify against losing business to hungry competitors.

7. Delight all your profitable customers

If there's a group of people with more power than anyone to help your business weather the current climate, it's your customers. They're the ones who choose when to buy from you, when to pay the bills, what to say about your business to

others – they're holding some powerful cards.

In economies where consumer confidence is low, customers also find themselves suddenly in demand and may be approached by competitors scrambling to attract their business. The message is simple: If you want to hold your best customers in times of gloom, you'd better treat them to exceptional customer service.

8. Get as much advice from experts as you can

While the current economic environment is full of challenges, there is one thing that's on your side: everyone is mobilised to the cause. Be as proactive and energetic as you can in seeking advice from experts who can keep you in touch with the latest economic indicators and thinking, so that your business stays on the pulse through these times and beyond.

9. Work smarter, not harder

A golden rule in working through trying economic circumstances is "Work Smarter Not Harder." There are so many time-saving technologies and products available to businesses now, and it's a great time to take stock of your business software, systems and processes to ensure you're making the most of them.

10. Review your business insurance

Unexpected events, fires, floods, robberies – they're the last thing a business needs at any juncture, let alone during periods of economic turmoil. In a second they can undo even the most diligent and thorough cash flow planning and financial management. There are more risks to your business than you may have first considered. The loss of key people or a major shareholder through death or disability could impact your ability to function.

* This is an excerpt from Westpac's brochure "10 Smart Money Tips for Business". For more detail, advice or to receive a copy of our brochure, please contact your Westpac Business Manager, go to our website www.westpac.co.nz, or phone 0800 888 066.

Data roundup

The official retail sales data for the last quarter of 2008 confirmed that consumers put away their purses and wallets at the end of last year. The value of sales fell 1.1% in the quarter when adjusting for seasonal patterns – the biggest quarterly decline since March 1997. That put the total value of sales 1.5% lower than the same period a year earlier. Excluding the effects of inflation, the picture is just as ugly – sales volumes fell 0.6% in the quarter to be down 3.7% on a year ago.

Durable items – especially cars – continue to be most affected by the consumer retrenchment. Car sale volumes

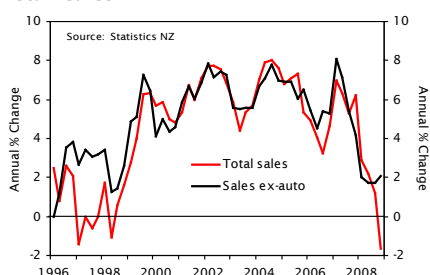
declined 4.9% in the December quarter (seasonally adjusted) to be down 17.4% on a year ago. Furniture and floorcoverings and hardware sales were also down. Appliances volumes bucked the trend of falling durable sales, rising 4.6% in the quarter to be up 13.5% on a year ago, thanks to aggressive discounting. Appliance prices fell 1.9% in the quarter to be 6.7% lower than a year ago.

More recent monthly data suggest the hit to durable spend continues. Car sales (in value terms) are the best indication of that, having fallen 15% in the first two months of this year. Meanwhile, by region the sale

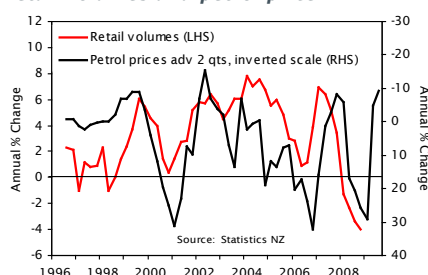
weakness is widespread, the biggest falls in February occurring in Wellington, and most parts of the South Island.

Against a backdrop of declining job security and reduced earnings expectations, consumers are being prudent in their spending decisions. How long the save-rather-than-spend mentality will dominate remains to be seen, but our recent consumer and employment confidence surveys suggest it will be a while yet. We expect real consumer spending to remain weak throughout 2009, with any sustained pick-up unlikely before the end of the year.

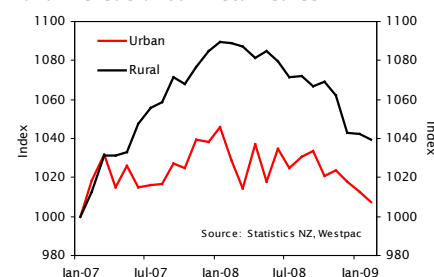
Retail sales



Retail volumes and petrol price



Rural versus urban retail sales



Retail Sales actual (\$ millions)

Storetypes	Months			Quarters		
	Feb-08	Feb-09	Annual % change	Dec-07	Dec-08	Annual % change
Supermarkets and Grocery	1,190	1,245	0.9	2,757	2,682	-2.7
Fresh Produce	73	78	3.7	170	171	0.4
Liquor	103	104	-3.2	282	275	-2.4
Other Food	61	62	-5.1	143	132	-7.2
Takeaway Food	99	101	-0.3	219	210	-4.0
Department Stores	317	311	-5.1	1,213	1,226	1.0
Furniture and Floor Coverings	127	111	-15.1	384	325	-15.3
Hardware	127	119	-13.9	399	361	-9.5
Appliance	199	204	-1.3	1,366	1,548	13.4
Recreational goods	195	194	-3.8	613	584	-4.6
Clothing and Softgoods	216	209	-9.8	677	661	-2.4
Footwear	37	39	-1.3	132	138	4.5
Chemist	149	156	-0.1	506	535	5.8
Household Equipment Repair	29	29	-2.9	62	59	-4.3
Other Retailing	232	257	10.8	731	745	1.9
Accommodation	216	212	-6.9	489	478	-2.3
Bars and Clubs	100	98	-6.2	210	215	2.5
Cafes and Restaurants	325	316	-6.2	749	702	-6.3
Personal and Household Goods Hiring	20	21	8.8	62	61	-0.8
Other Personal Services	147	147	-6.7	330	322	-2.4
Subtotal	3,961	4,016	-2.6	11,493	11,432	-0.5
Motor Vehicles	666	520	-27.4	2,518	2,079	-17.4
Automotive Fuel	607	516	-11.4	943	924	-2.0
Auto Electrical, Smash Repair, Tyres	122	121	-6.1	325	290	-11.0
Automotive Repair and Services	170	160	-8.6	343	318	-7.5
Total	5,525	5,342	-6.9	15,623	15,043	-3.7

It's bad, but not that bad

Consumer confidence slipped back below the 100 level in the March 2009 quarter, as consumers took on board the weight of recent negative economic news. The Westpac McDermott Miller Consumer Confidence Index fell to 96.0 in March, from 101.3 in December. At current levels, confidence is still above the low reached in June last year (when the Index fell to 81.7), when high interest rates, petrol and other cost pressures were putting the squeeze on consumers. An index number over 100 indicates there are more optimists than pessimists, while a number under 100 indicates that pessimists outnumber optimists. The margin of error in the survey is 2.5% at a 95% confidence interval. The survey was conducted from 1-16 March.

Confidence has remained remarkably resilient given the sheer volume of negative news consumers have been bombarded with in recent months. It has been virtually impossible to escape the bad news from offshore, with nearly every day bringing another tale of woe from one of our major trading partners. The news from within NZ has been far less sensational, but it has still been disturbing. That raises the question as to whether NZ consumers are being staunch or whether they are simply in denial. Indeed, when we look at our international counterparts, New Zealand consumers appear to be less pessimistic than most – confidence amongst US consumers is at a mind-bogglingly low 56.6 on their Index, while in Australia the Index is at 85.6.

There are a number of plausible explanations as to why NZ consumers are not suffering such a bad case of depression. These include the traction policy makers are getting from monetary and fiscal stimulus, the relatively low exposure NZ households have to financial assets, and the mild correction in our housing market relative to the experience in the US, UK and much of Europe.

Regardless of how we compare with our international friends, at current levels the Index still points to continued weak consumer spending over the next few months at least.

Key components

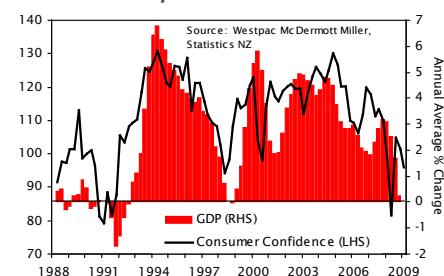
The fall in confidence was widespread, with all the components of the index lower than in December. However, apprehension around the short term economic outlook continues to drive the decline. A net 57% of respondents expect bad economic times over the next 12 months, up from 45% in December last year. This is the most negative response to this question since June 1998. Fortunately, consumers still believe that the downturn will be short lived – a net 50% expect better economic times over the next five years, down only marginally from the record high of a net 51% reached in December. The long term average for this component is a net 30%. The above average result is likely to be reflecting where we are in the current economic cycle – i.e., it seems reasonable that during a recession the majority of consumers would expect better times over the medium to long term.

Consumers' assessment of their own finances worsened over the quarter. A net 28% of respondents said they felt worse off now compared to a year ago – from a net 21% in the December quarter. Still, that is better than the 41% of respondents saying they felt worse off in June last year when cost increases were at their peak. A net 6% of respondents expect to be better off in a year's time, although that is down from a net 10% in December.

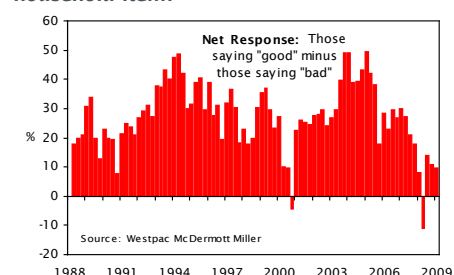
Perceived purchasing power fell further this quarter, despite the massive drop in interest rates since the last survey was taken. Only a net 10% of respondents said now is a good time to buy major household items – down 1 point from the December survey. Clearly, cheaper credit is not enough to offset the negatives of falling job security and a lower currency (making imported items more expensive).

By demographic grouping, the 50+ age group is the most pessimistic – not surprising given they arguably have the most to lose in this environment. The 18-29 age group is the only group where the index is still over 100 (i.e. the optimists outweigh the pessimists). Males are less pessimistic than females, albeit only by a very small margin.

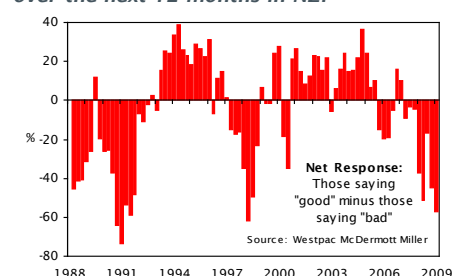
Consumer Confidence and GDP



Is now a good or bad time to buy a major household item?



Do you expect good or bad economic times over the next 12 months in NZ?



Regional Consumer Confidence

	Mar-08	Dec-08	Mar-09
Northland	87.4	98.8	91.8
Auckland	99.8	102.3	95.4
Waikato	92.1	96.0	98.2
Bay of Plenty	95.7	105.7	93.4
Gisborne/ Hawkes Bay	92.1	104.5	98.3
Taranaki/ Manawatu-Wang.	92.1	102.0	93.9
Wellington	96.3	103.2	97.8
Nelson-Marlborough West Coast	101.5	105.6	96.9
Canterbury	98.7	95.7	98.7
Otago	96.2	104.2	93.4
Southland	91.6	102.6	93.8
New Zealand	96.5	101.3	96.0