McGrathNicol

IN RETAIL (NEW ZEALAND)
2023 EDITION

SNAPSHOT

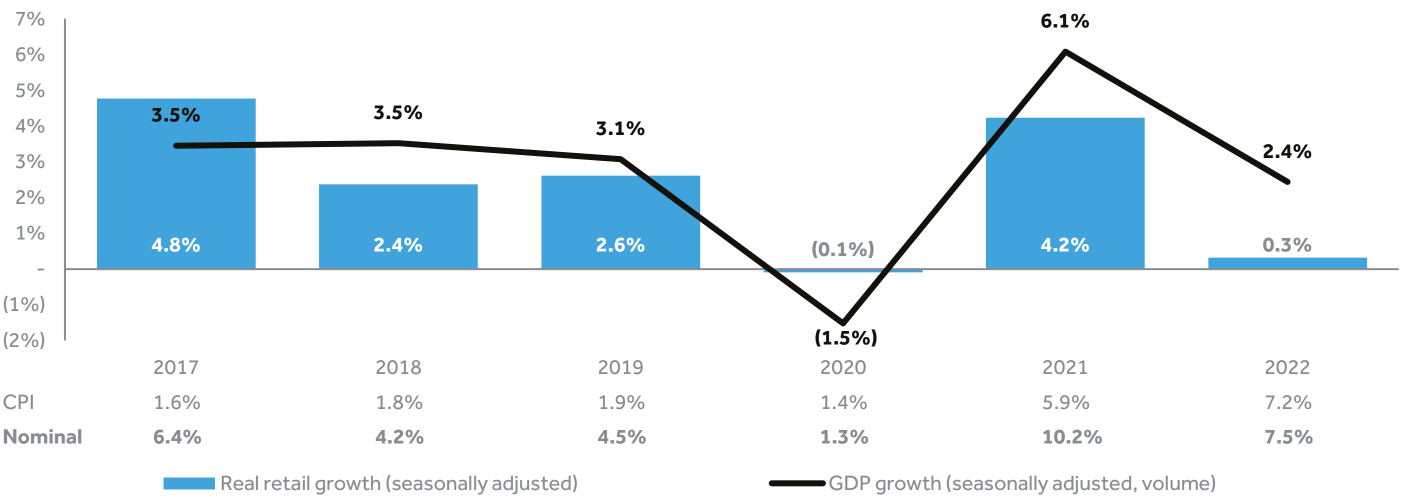
- The post-COVID spending boost ended in 2022, with core retail growth of only 0.3% (nominal 7.5%) compared with GDP growth of 2.4%. Inflation is the driver of top-line retail growth currently, with core retail spending down 0.5% in Q1 2023, despite nominal spending up 6.3%. As expected in our review last year, cost of living pressures and interest rate rises reduced discretionary budgets, compounded by consumers redirecting spending to travel and experiences.
- As domestic and international tourism returned, food and beverage services (up 7.1%) and accommodation (up 6.9%) categories recovered, with the former back in line with pre-COVID spending on a real basis, and accommodation down only 10%. However, the "home" categories that benefited so significantly post-COVID began reversing, with electrical and electronic goods down 21.6% on 2021 and losing all gains made post-COVID. Furnishings and recreational goods also fell 3.4% and 4.2% respectively after experiencing significant gains in 2021, with those trends continuing into Q1 2023. Hardware maintained some growth at 1.2%. We expect to see spending on the home continue to decline during 2023 given falling house prices and the negative residential construction outlook.
- By region, Auckland and Canterbury are driving growth, with both regions seeing real spending in 2022 c7% higher than pre-COVID, with almost all 2022 growth in Auckland (up 3.9% on 2021). Despite growth in 2021 and 2022, the Rest of South Island is still down 3.3% down on pre-COVID, as tourism and international students take longer to come back following borders reopening in Q2 2022.
- Online spending appears to have peaked as consumers move back in store, falling 5% in 2022 (and continuing to fall Q1 2023) according to NZ Post. Retail rents are still lower, and vacancies higher, than pre-COVID, although the trends are also showing signs of changing.
- Given low forecast GDP, high inflation, and mortgage rate increases continuing throughout 2023, we expect retail will struggle through this year and into 2024. This year saw the insolvencies of Bobux, EziBuy, Redcurrent, the Mulberry NZ franchise and others. The counter-points are that confidence is finally increasing from record lows, migration has bounced back strongly, and unemployment is low, although this may be tested in the next 12 to 18 months. Retailers still need to carefully manage stock, staffing, and store decisions, with scenario analysis for demand forecasting and inventory management to mitigate these risks.
- Note that we are not adjusting for COVID in this year's review, with each year compared directly with the prior year.

All quoted percentages, other than GDP, are in real terms

CORE RETAIL INDUSTRIES ("RETAIL")* GROWTH WEAK

Although core retail nominally grew by 7.5% in 2022, this falls to only 0.3% when adjusted for inflation, underperforming the wider economy with 2.4% growth in GDP. The post-COVID boost in spending is over and the years ahead look to be challenging for retailers. As detailed later in this report, there was once again significant volatility across subcategories and regions during the year.

Real retail and GDP growth



Source: Statistics NZ

**Retail industries reported by Statistics NZ, excluding fuel, motor vehicles and parts.*

CATEGORY WINNERS AND LOSERS REVERSE FROM THE LAST TWO YEARS

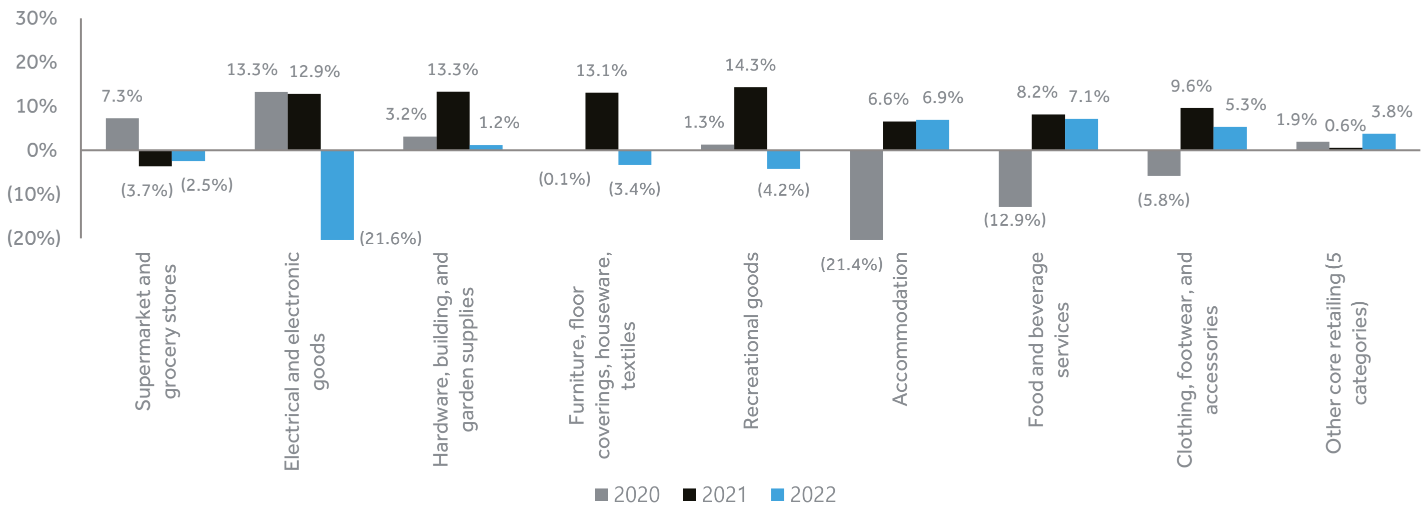
In a year of weak retail growth, the trends we saw over 2020 and 2021 reversed in 2022. Accommodation and food and beverage services started to recover, with the latter now back to 2019 levels. Despite c7% growth in each of 2021 and 2022, accommodation is still 10% below pre-COVID levels following the 21% fall in 2020. Apparel also performed better than average this year, growing 5.3%, with real spending 9% higher in 2022 than pre-COVID.

What was particularly interesting was the reversal in trends within the "home" categories that we saw post-COVID. Electrical and electronic goods saw the largest drop, down 21.6% on 2021 and losing all gains made post-COVID. Furnishings and recreational goods also lost their luster, falling 3.4% and 4.2% respectively after experiencing significant boosts in 2021. Hardware maintained some growth at 1.2%, but we expect to see this continue to decline during 2023 given falling house prices and building consent applications.

As we noted last year, these categories benefited from the post-COVID lockdown, work-from-home trends and from retail customers reallocating international travel budgets to big ticket discretionary items. We noted in prior reports that this spend may not be sustainable when travel and "normal" life resumed, with consumers gradually reverting to pre-pandemic spending habits.

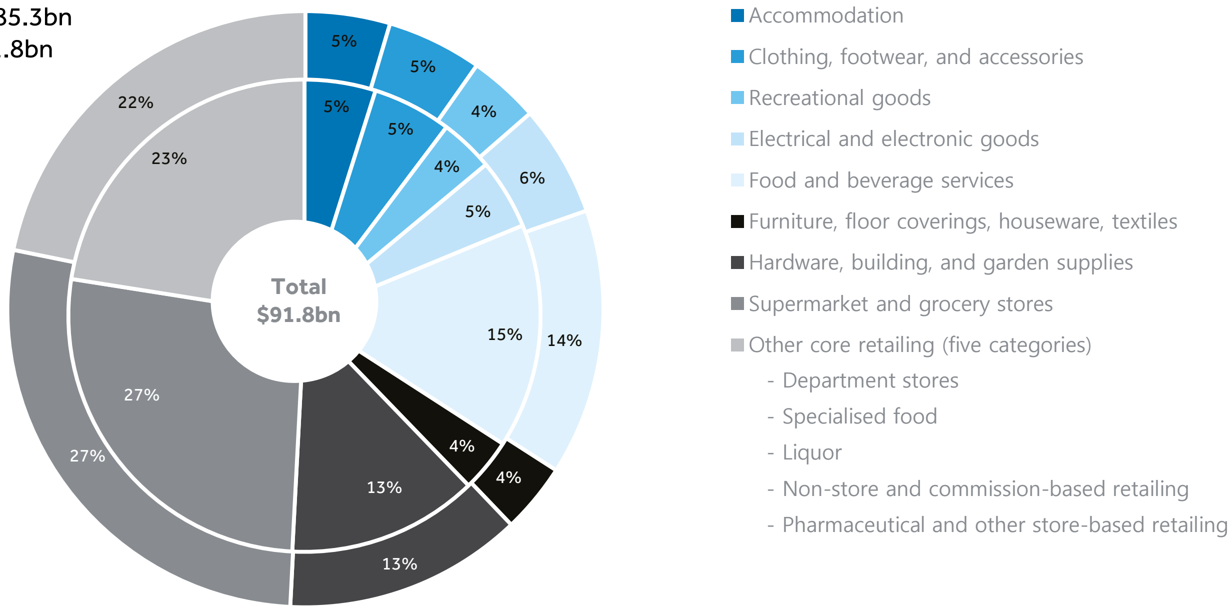
We expect 2023 and possibly 2024 to be worse still, as the cost-of-living crisis and potential increase in unemployment further erodes consumers' discretionary budgets.

Real retail growth by category versus prior year (includes non-core retail, seasonally adjusted)



Source: Statistics NZ

Core retail categories
2021 (outside) $85.3bn
2022 (inside) $91.8bn



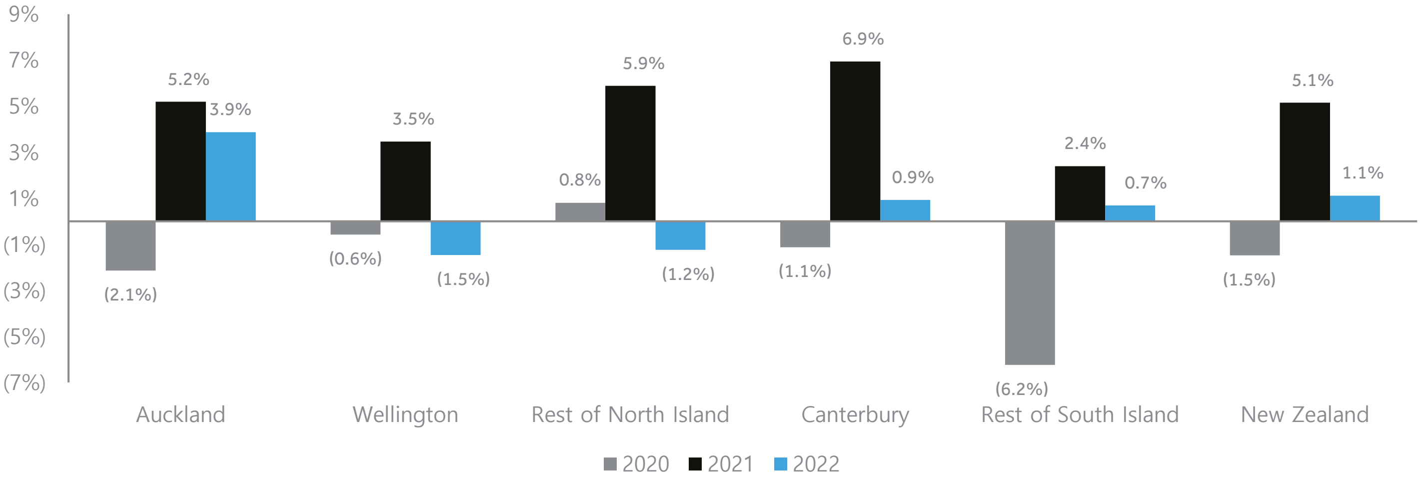
Source: Statistics NZ

RETAIL SPENDING AUCKLAND FOCUSED, WITH REGIONAL SOUTH ISLAND SLOWLY RECOVERING

Almost all 2022 growth occurred in Auckland, which was up 3.9% on 2021 and which has maintained retail spending above pre-COVID levels on a real basis throughout the period (6.9% up in 2022). Canterbury managed 0.9% growth in 2022, but on the back of strong 2021 growth; like Auckland, Canterbury's real retail spending is 6.7% higher than pre-COVID.

Wellington and the Rest of North Island declined in 2022 after growing in 2021, but are still just ahead of pre-COVID levels on a real basis. The Rest of South Island is still playing catch up. Despite some growth in 2021 (2.4%) and 2022 (0.7%), this region is still 3.3% down on pre-COVID retail spending levels on a real basis, as tourism and international students take longer to come back following borders reopening in Q2 2022.

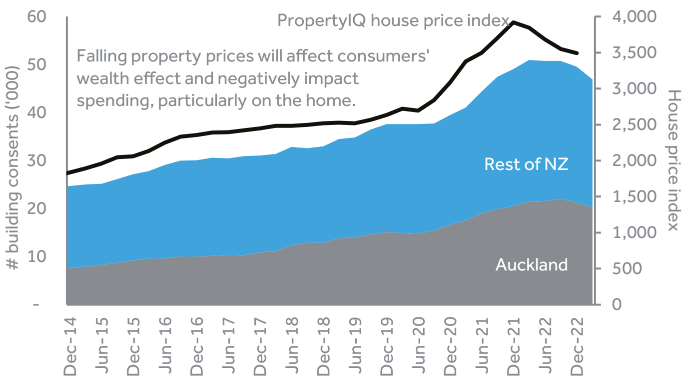
Real retail growth by region versus prior year (includes non-core retail, seasonally adjusted)



Source: Statistics NZ

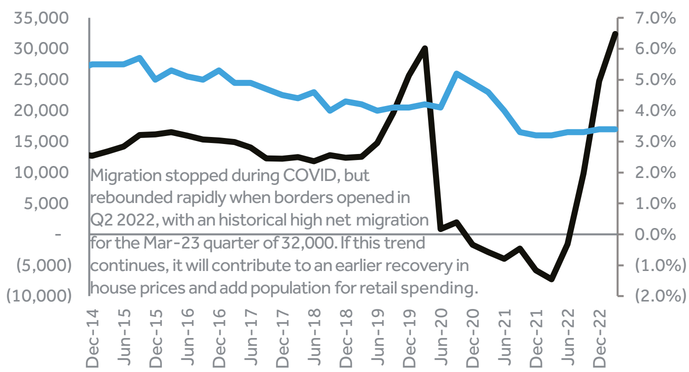
OTHER ECONOMIC INDICATORS

Residential building consents and PropertyIQ house price index



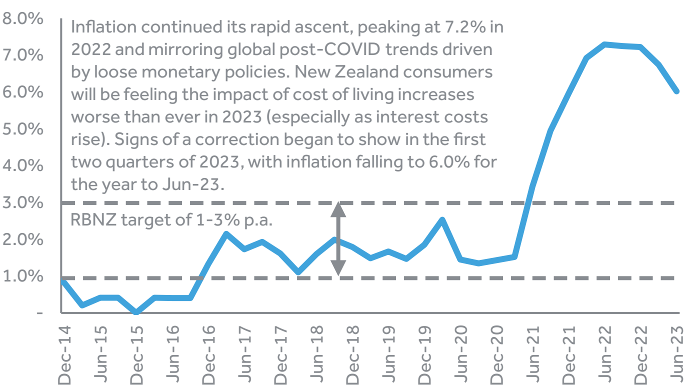
Source: Statistics NZ; Reserve Bank New Zealand

Net migration (# black) and unemployment rate (% blue)



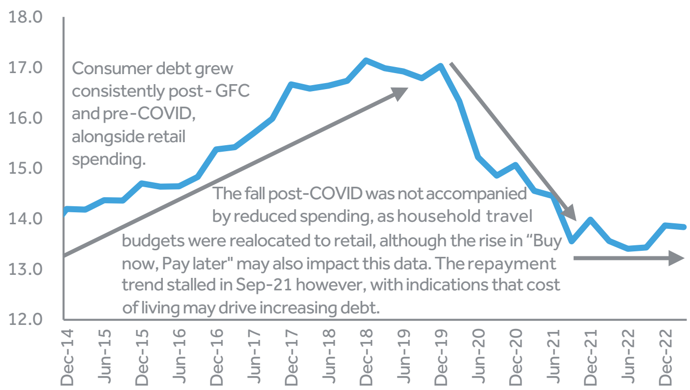
Source: Reserve Bank New Zealand

Consumer price index (LTM)



Source: Statistics NZ

Household consumer credit (non-property debt)



Source: Reserve Bank New Zealand

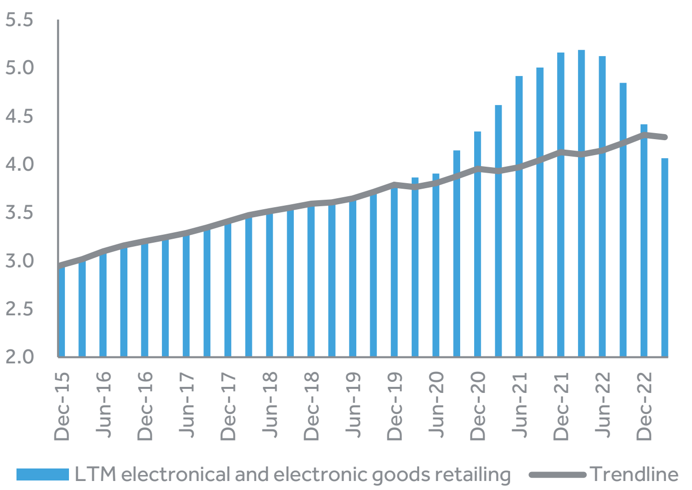
DISCRETIONARY SPENDING GAINS REVERSE

Retail categories linked to the home (below) saw significant growth in 2020 and 2021, up 13% to 30% on pre-COVID levels. However, in our review last year, we noted that *"there is a risk that spending in these categories falls back to long term trend lines, or even below, as consumers revert to pre-pandemic spending habits with international travel resuming in 2022 and given consumers have largely purchased their big-ticket items over the last two years. These categories also face risks to spending from stagnating house prices, inflation, and rising interest rates reducing discretionary spending."*

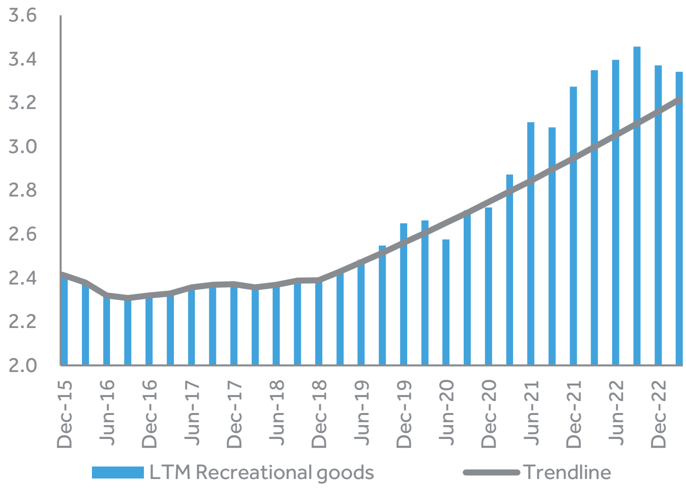
This proved to be prescient, with electrical and electronic goods experiencing the largest decline, down 21.7% ($1.1bn) from $5.2bn for the year to March 2022 to $4.1bn for the year to March 2023, with total spending now below the pre-COVID trendline. Recreational goods, hardware, building and garden supplies, and furnishings all experienced declines in the two quarters to March 2023 from the peak year to September 2022, but are still above their pre-COVID trendlines, and so should still be performing well. The risk is that these trends continue, as the issues highlighted last year have persisted throughout the 2023 year to date, depressing these categories further. Residential construction in particular appears likely to reduce significantly in the coming year, given trends in building consents and availability of capital for development. As we noted previously, retailers in these categories should consider that the abnormal levels of sales may have been temporary when considering stock levels and store/staff investments.

Although the Auckland floods and cyclone Gabriel may provide some additional revenue, total claims across residential and businesses, including motor vehicles, are $2.5 billion, with $0.4 billion paid out per ICNZ's 4 April 2023 media release. About half the cyclone Gabriel claims related to home and contents, so assuming the same ratio across both disasters, this could add up to 5% of additional spending in the categories below, which totaled $23.1 billion in 2022; not enough to offset the declines.

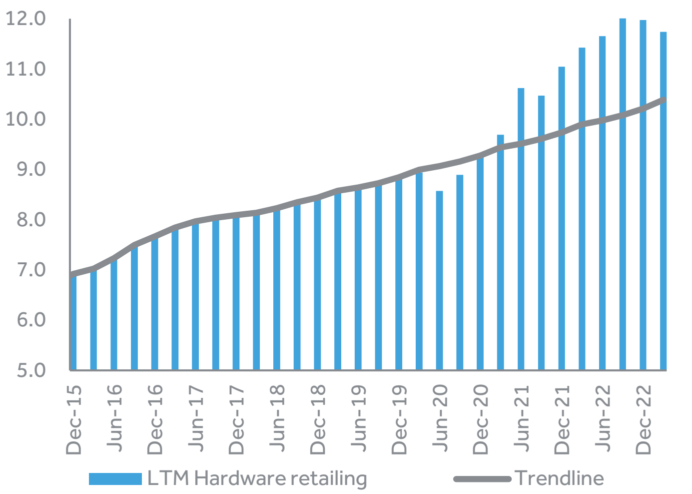
Electrical and electronic goods retailing ($'bn)



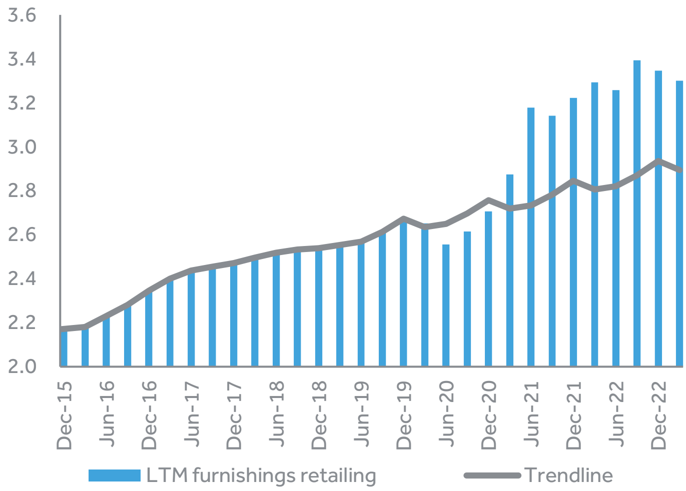
Recreational goods retailing ($'bn)



Hardware, building and garden supplies ($'bn)



Furnishings retailing ($'bn)



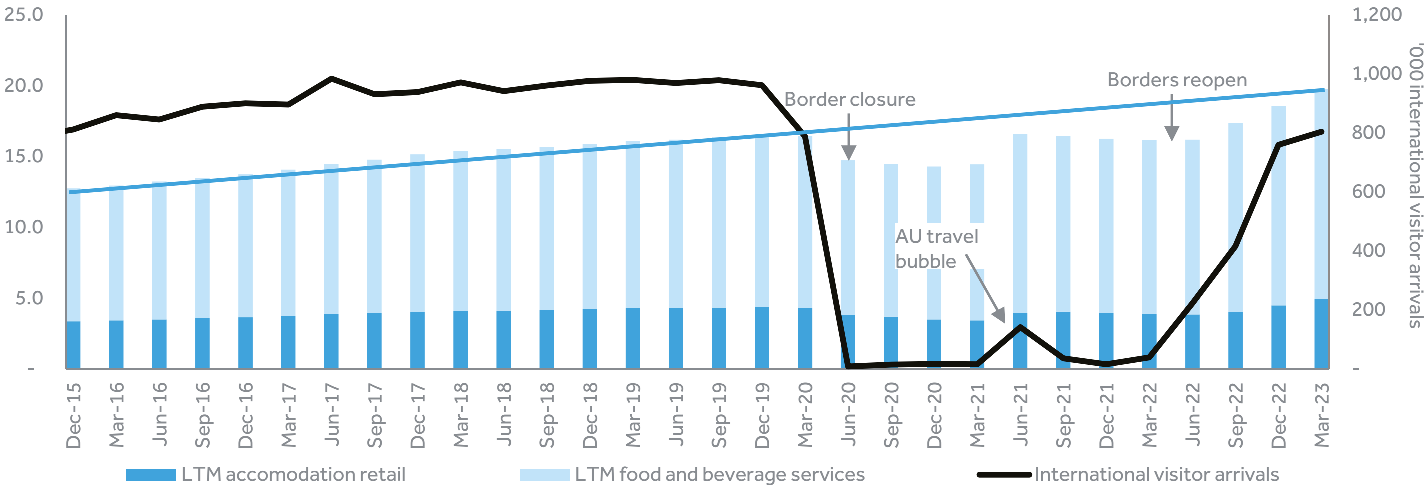
Source: Statistics NZ; all figures are LTM quarterly and seasonally adjusted but not inflation adjusted

TOURISM RELATED SECTORS RECOVERING

New Zealand's borders finally reopened in Q2 2022 with tourists returning over the next 12 months. International visitor arrivals exceeded 0.8 million in Q1 2023, only 18.0% down on Q1 2019. Coupled with the domestic return to experiential spending and removal of the traffic lights, food and beverage services spending grew 20.9% for the year to March 2023 compared with the same period last year, with 2022 spending in line with pre-COVID levels on an inflation adjusted basis.

Accommodation spending grew 27.0% over the year to March 2023, but was still 10% below pre-COVID levels in 2022 on an inflation adjusted basis. However, there are clear signs that, despite global concerns around cost of living, international tourists are still willing to travel and spend on experiences. Accommodation would also have performed worse during 2020 and 2021 were it not for the effective subsidy of MIQ and motels being used to house the homeless. Barring any new external crisis, we expect accommodation and food and beverage services to continue to see increasing spend.

Food and beverage services + accommodation retail ($'bn) and international visitor arrivals



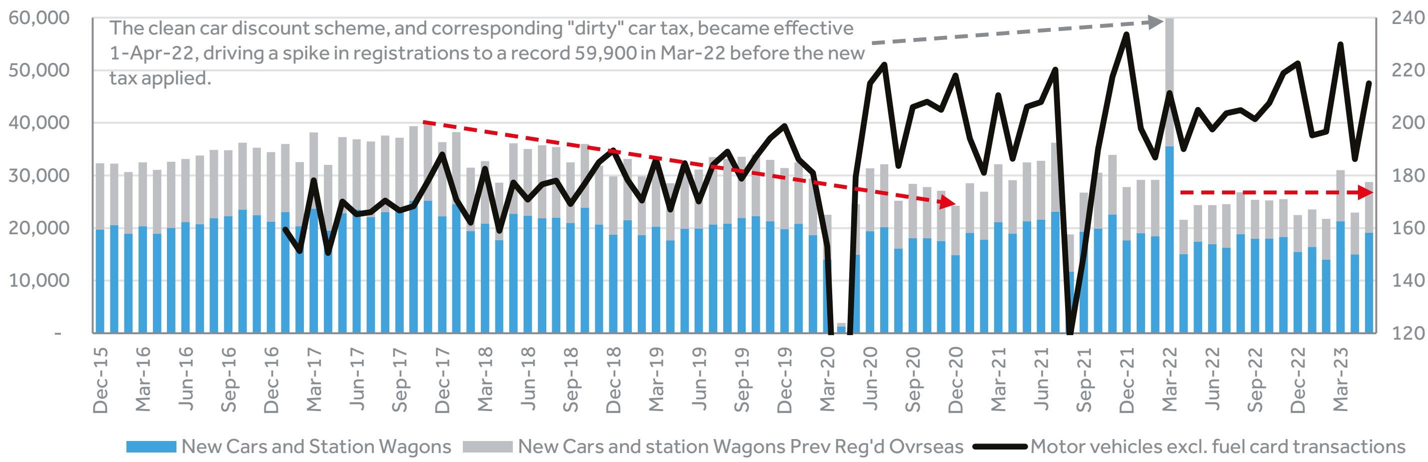
Source: Statistics NZ; all figures are LTM quarterly and seasonally adjusted but not inflation adjusted

MOTOR VEHICLE RETAILING IMPACTED BY SUPPLY CHAIN ISSUES AND UNCERTAIN DEMAND

The declining trend in vehicle registrations since 2017 has still not reversed. New Zealand new and used registrations averaged 35,000 per month in the two years to December 2017, peaking at 40,000 in November 2017, but fell 20% to an average of 28,000 per month in 2020 (excluding March and April 2020). The trend appeared to be reversing in 2021 but deteriorating macro-economic conditions and supply constraints kept vehicle registrations at an average of 28,000 per month in the two years to May 2023. This includes the spike in registrations in March 2022 to 60,000 vehicles, as cars were registered before the "clean car" tax came into force on 1 April 2022. This spike suppressed new vehicle registrations for the next 12 months, with an average 25,000 for the year to May 2023, 29% lower than the average pre-2017.

The amount spent on cards however is elevated, from $180 million pre-COVID to over $205 million in the last two years, despite fewer registrations, suggesting inflation. This aligns with US research, where the average selling price for a new vehicle was 36% higher in 2022 than 2019. Demand going forward is uncertain as consumers' discretionary spending falls from rising inflation and interest rates and reallocations to travel, possibly partially offset by corporate and rental fleets being rebuilt as New Zealand tourism recovers.

New and ex-overseas motor vehicle registration (# LHS) and motor vehicle (excl fuel) card transactions ($'m RHS)



Source: Statistics NZ; 5 Ways That Buying a Car Has Drastically Changed, Wall Street Journal, 28 July 2023

CONSUMERS RETURNING TO STORES

Unfortunately, we no longer have access to the detailed footfall, in-store and online spending data to continue analysing trends in consumer habits and online spending. However, NZ Post data showed online spending down 5% in 2022, with that trend continuing in Q1 2023, as consumers moved spending back in-store. This will be driven in part by the increase in food and beverage services spending, with Westfield also reporting increasing footfall at its malls.

JLL's February 2023 retail market report showed Auckland CBD retail vacancies finally peaked at 8.6% in June 2022, up from 2% at December 2019, reducing to 8.2% at December 2022. Average rents are still flat or falling in the case of Prime CBD, down 4.2% to $2,300 per sqm at Q4 2022. Suburban retail vacancies continued to fall to 9.4% at December 2022, down from the peak of over 12% in June 2021, although still above the 6% pre-COVID. Wellington vacancies also reduced to 8.2% as rents fell c10% in 2022, with Canterbury the only reported region able to hold rents over the last two years and reduce vacancies to 4.9%.

CONSUMER CONFIDENCE AND RETAIL OUTLOOK REMAINS SUBDUED

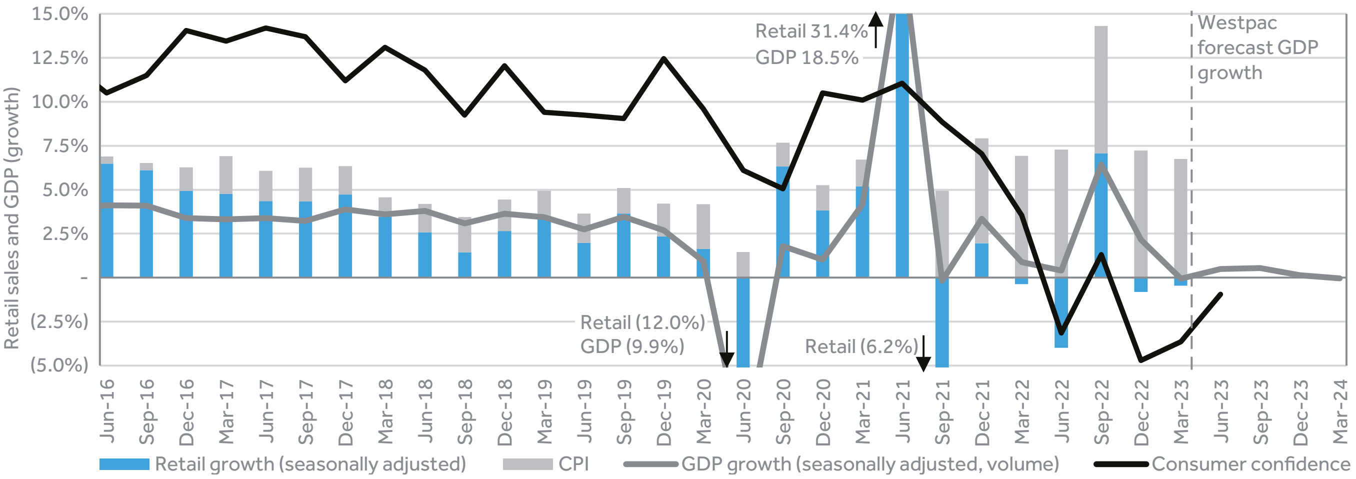
Consumer confidence continued its precipitous decline in 2022, falling to the lowest level since records began in 1988, before recovering slightly. Consumers were more pessimistic than during the GFC, or when COVID first hit. ANZ's confidence index showed the same, with Australia and the United Kingdom similarly down, but the United States showing comparative resilience. Despite all this pessimism, consumers continued spending, with nominal retail growth above 6% in five of the last six quarters; i.e., consumers were willing to pay the higher prices, rather than reduce consumption volumes.

Inflation drove most (if not all) retail growth in 2022 and the first quarter of 2023, with nominal spending up 6.3%, but real spending down 0.5% for Q1 2023. Real retail spending now lags GDP growth, as the impact of cost-of-living inflation and interest rate increases impact consumers' discretionary budgets.

Last year we noted that the outlook for retailers remained mixed, with the potential return of tourists, international students and easing of lockdown restrictions providing much needed relief for hospitality and accommodation retailers, but with concerns around domestic consumers reverting to pre-pandemic spending habits, re-balancing away from tangible goods and towards experiential and service-based spending, including hospitality, leisure, and tourism. We noted that consumers' discretionary spending would also be negatively impacted by rising costs of living, inflation and interest rates increasing mortgage servicing costs. These predictions turned out to be accurate, with leisure increasing and tangible goods sales slowing to varying degrees.

Given Westpac forecasts little GDP growth over the next year, and given inflation and mortgage rate increases are continuing throughout 2023, we expect retail will similarly struggle through this year and into 2024. Retailers will need to carefully manage stock, staffing, store, and working capital decisions, with scenario analysis for demand forecasting and inventory management to mitigate these risks.

Retail and GDP growth (quarterly vs PY) and consumer confidence index



Source: Statistics NZ; Westpac McDermott Miller Consumer Confidence Index; Westpac New Zealand economic and financial forecasts

FOR MORE INFORMATION, PLEASE CONTACT OUR RETAIL SPECIALISTS

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Who do we help?

We help retailers, both listed and private, including some of Australia and New Zealand's best known organisations to perform better

Project	Engagement type	Sector	Role
Bobux	Receivership	Shoe wholesaling	Ran an accelerated, global, sale process to preserve value in the Bobux brand, achieving a sale as a going concern to Munro Footwear Group.
Gull NZ	Hold Separate Manager	Fuel retailing	Managed the day-to-day operations of the Gull fuel retail network during a divestment period on behalf of the Commerce Commission.
Liquor King	Sale advisor	Liquor retailing	Managed the successful divestment of the Liquor King retail store network for parent Lion Nathan.
Max Fashion	Creditors compromise	Fashion retailer	Developed and implemented a restructuring plan that reduced payments to suppliers, closed unprofitable stores and reduced rent on remaining stores, saving jobs and the company from insolvency.
Nido	Receivership	Furniture retailer	As receivers, we executed an efficient stock realisation strategy to maximise returns for creditors and ultimately close New Zealand's largest furniture retailer.
Project Rain	Retail advisory	Clothing retail	Assisted the Board to refresh their digital and store strategy through providing benchmarking data and analytical tools. Subsequently assisted with Covid-19 preparation and contingency planning.
Project Pew	Retail advisory	Furniture retailing	Assisted with landlord negotiations for Covid-19 relief and contingency planning.
Ziera Shoes	Voluntary administration	Shoe retailing	As administrators, we deployed technology and a trading strategy that increased turnover five-fold, whilst securing a sale of the IP, resulting in secured creditors being repaid in full and creditors receiving c90% of their claims.
Project Clip	Retail advisory	General retailing	Detailed independent business review, forecasting and ongoing monitoring to improve profitability and redirect the business's strategy.
Topshop	Receivership	Fashion retailer	As receivers we leveraged our retail expertise to maximise returns from stock through targeted marketing and merchandising.
Identity	Receivership	Fashion retailer	As receivers, we closed unprofitable stores whilst selling down stock and completed a sale of the business and assets as a going concern.
Project Black	Retail advisory	Sports hardware retailer	Detailed independent business review and on-going monitoring and advice to improve profitability, including recommending changes in product mix, supply chain and strategic direction.
Project Music	Retail advisory	Music retailer	High-level independent business review to identify key issues and provide recommendations and strategy to improve profitability, including recommending the closure of stores and advice regarding online competition.

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