WEEKLY ECONOMIC COMMENTARY

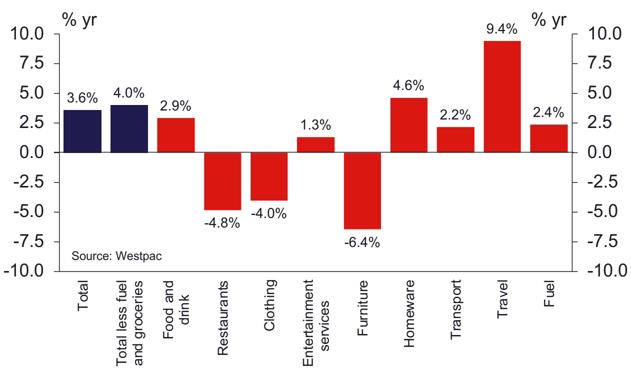
2 Apr 2024 | **Westpac Economics Team** | **westpac.co.nz/economics** | economics@westpac.co.nz

Return to fiscal surplus delayed again

Westpac New Zealand's data on spending via Westpac issued debit and credit card data for the three months ending February confirm that household spending remains weak and that it's a tough time for the retail sector.

Spending was particularly weak on discretionary items. For example, spending on furniture, clothing, and restaurants all show consumers are keeping the purse strings tight. Even in sectors like groceries, which have traditionally been more resilient to economic downturns, consumers have increasingly opted for value-for-money options over the nice-to-haves. We do see more resilience in the services sector as the past year has seen a sharp rise in spending on airfares and travel related services, reflecting a renewed appetite for travelling abroad as well as the ongoing recovery in inbound tourism.

Annual spending growth (three months to February vs same time last year)

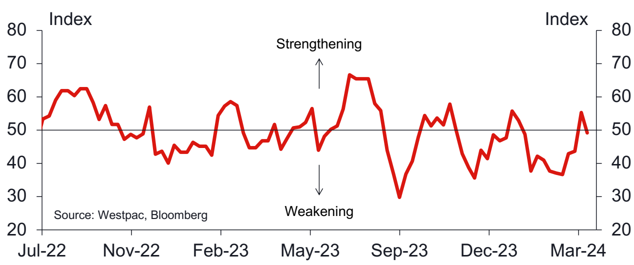


Spending seems weak across most of the country. Wellington has been particularly hard hit, with ongoing nervousness about job prospects in the region a key driver. Spending in the top of the South Island has also been weak with a softer labour market and the effects

Key views

	Last 3 months	Next 3 months	Next year
Global economy	→	→	↗
NZ economy	→	→	↗
Inflation	↘	↘	↓
2 year swap	↗	→	↘
10 year swap	→	↗	↘
NZD/USD	↘	↗	↗
NZD/AUD	↘	↗	↘

Westpac New Zealand Data Pulse Index



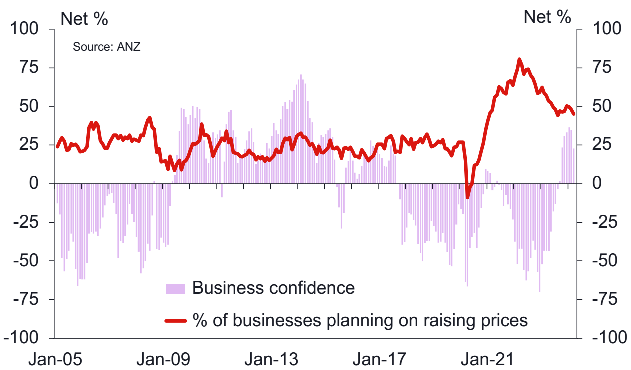
Key data and event outlook

Date	Event
4 Apr 24	Govt financial statements for 8 mths to February
9 Apr 24	QSBO business survey, March quarter
10 Apr 24	RBNZ Monetary Policy Review
12 Apr 24	NZ Selected price indexes, March
17 Apr 24	NZ CPI, March quarter
1 May 24	NZ Labour market statistics, March quarter
1 May 24	RBNZ to release Financial Stability Report
1 May 24	FOMC Meeting (Announced 2 May NZT)
7 May 24	Govt financial statements for 9 mths to March
7 May 24	RBA Monetary Policy Decision and SMP
13 May 24	NZ Selected price indexes, April
22 May 24	RBNZ Monetary Policy Statement and OCR
30 May 24	Govt to release Budget 2024
5 Jun 24	Govt financial statements for 10 mths to April

of dry weather conditions on agriculture/horticulture production likely to be key factors. By contrast, spending in the Hawke's Bay and Gisborne was strong, although most of that reflects positive base effects associated with Cyclone Gabrielle in early 2023.

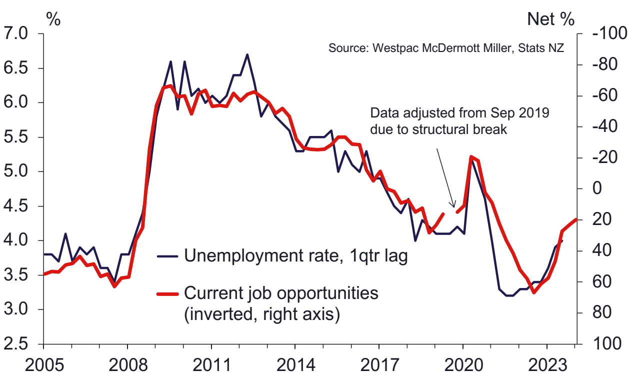
A softer tone is also evident in ANZ's business outlook survey for March. Business confidence in the economy and expectations relating to respondents' own activity fell. A lower, but significant proportion of firms still expect to be able to increase their prices over the coming three months. However, firms' expectations of year-ahead CPI inflation have moved lower and at 3.8% are now back to levels last seen in late 2021.

Business confidence



On a more positive note, the Westpac McDermott Miller employment confidence Index rose for a second consecutive quarter, with more New Zealanders feeling optimistic about the state of the labour market than those that are pessimistic. Not only are New Zealanders expecting better job prospects and improved job security, but they are also feeling more optimistic about a lift in earnings over the coming year as inflation recedes from recent highs. That said, perceptions about current job opportunities were again weaker, falling for a sixth straight quarter. This question is of particular interest to us because it tends to provide a good early read on unemployment, which in turn has implications for wage inflation and the future path of interest rates.

Current job opportunities vs unemployment rate



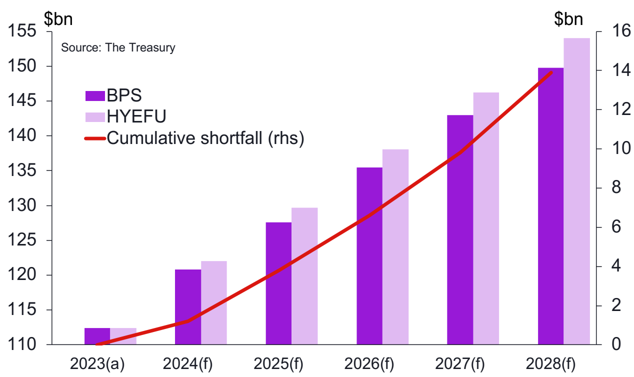
Meanwhile, the new Government's first Budget Policy Statement (BPS) has confirmed that the upcoming Budget will signal a markedly weaker fiscal outlook as well as a likely increase in the government's borrowing requirement. The BPS also reaffirmed government's commitment to delivering "meaningful" personal income tax cuts in the Budget, although no new details were provided on the magnitude or timing of that relief.

Details on operating spending allowances were similarly light. While there was confirmation that the allowance to be announced in the Budget would be less than the $3.5bn for 2024/25 originally set out in last December's Half-Year Economic and Fiscal Update (HYEFU), detail on operating spending allowances for subsequent years will only be revealed when the Budget is released at the end of May.

The Government has also committed itself to adding up to another $7bn to the Multi-Year Capital allowance, which is used to fund new capital investment over the four-year budget time horizon. This top-up alone will add to the HYEFU projections of the government borrowing requirement over this timeframe.

Meanwhile, the Treasury has revised its own economic growth forecasts. It now expects real GDP growth of 0.1% for the 2023/24 fiscal year, which is significantly down on the 1.5% growth that was forecast in the HYEFU. Real growth is forecast to rise by 2.1% in 2024/25 and 3.1% in 2025/26 which although firmer than shown in the HYEFU, is still not enough to offset the sharply lower growth forecast for 2023/24. That together with Treasury's lower forecast trajectory for inflation, suggests that nominal GDP will come in significantly lower across the forecast horizon, reducing cumulative Crown tax revenue by $13.9bn. Treasury forecasts that Crown tax revenue will be reduced by about $1.2bn in 2023/24 and that will ratchet up to $4.2bn by 2027/28.

Forecast for core Crown tax revenue



At first blush, these updated tax revenue forecasts suggests that the Government will not achieve an operating surplus in 2026/27 or 2027/28. It is important to note, however, that these updates do not include Government's proposed personal income tax cuts or other possible sources of tax revenue. It also doesn't include spending cuts and any reprioritisation of expenditures to be announced in the upcoming Budget, as well as any further changes to Treasury's economic forecasts. All told, we expect Government will seek to forecast a small surplus in 2027/28, but it remains to be seen whether that will be achievable in Budget 2024.

The Government has also announced that it will adopt a narrower measure of net core Crown debt that excludes among other things investment assets held by the New Zealand Super Fund. It has also set itself the long-term goal of reducing this debt measure from around 44% of GDP forecast for 2023/24 – a level already relatively low compared to many advanced countries – to below 40%. Once there, the Government intends to maintain core net Crown debt in a range of 20-40% of GDP. The Government has set itself a long-term goal of achieving an operating (OBEGAL) surplus that is consistent with these net core Crown debt targets. In part it will do that by managing core Crown expenses down towards 30% of GDP from 33% at present.

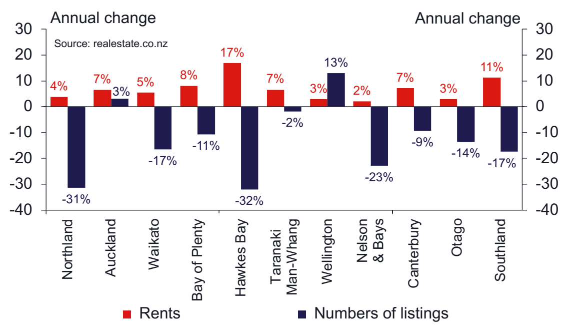
In summary, the BPS confirms that the government borrowing programme is likely to be significantly increased when the Budget is released at the end of May. Given the extent of the downgrade to the tax revenue forecast, this could be as much as $15bn over the four-year budget time horizon. Much though will depend on decisions taken between now and the Budget in May, especially with regards to the magnitude and timing of tax cuts.

Paul Clark, Industry Economist

Chart of the week.

Annual population growth has surged to 2.8% – the highest it's been in decades – and that has seen growing demand for rental housing. But at the same time as the demand for rentals has increased, the number of properties being advertised has fallen in most parts of the country. That's resulted in growing pressure on rents, with many parts of the country recording sizeable increases. There are some exceptions. Auckland has seen an increase in the number of homes available for rent. However, with most new migrants settling in Auckland, there's still strong demand for rentals and rents in the region are climbing at a rapid pace. In contrast, Wellington has recorded a more modest increase in rents than most parts of the country. The Capital has seen more modest growth in its population and an increase in the number of homes available. Reductions in public sector spending could also be playing a role. (Note: We omitted parts of the central North Island that were affected by last year's storms which has caused significant disruptions to the number of available properties.)

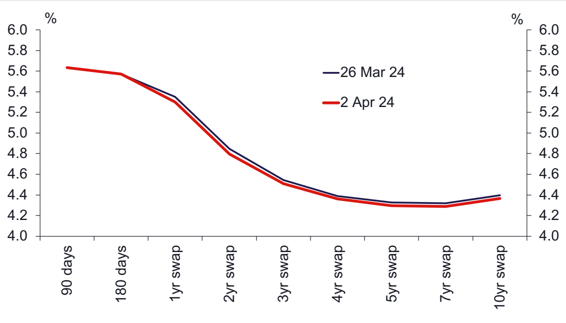
Rents and number of properties advertised for renting



Fixed versus floating for mortgages.

The RBNZ left the OCR on hold in February. While further OCR hikes don't look likely, easings are still some way off. Borrowers favouring certainty, at current fixed rates we see value in fixing for as long as two years.

NZ interest rates



Global wrap

North America.

The US economy continued its run of solid activity indicators. December quarter GDP growth was revised up from 3.2% to 3.4% (annualised), led by an upward revision to personal consumption. The manufacturing ISM rose from 47.8 to 50.3 in March, the first reading above 50 since September 2022. However, the steady rise in the 'prices paid' measure in recent months raises another warning flag around whether inflation will continue to track down towards the Fed's 2% target as hoped. The PCE deflator for February printed at 0.3%, in line with market forecasts, lifting the annual rate slightly to 2.5%. Looking ahead, the March nonfarm payrolls report will be closely watched. In recent months we've seen some large gains on the initial release, only for them to be revised lower. The separate household employment survey has been much softer lately, and we think that the widening gap between the two surveys will eventually come home to roost. There is also a large amount of Fed-speak this week which will be closely watched for signals on the stance of policy.

Asia-Pacific.

Australian data started last week on a sour note, with a sharp fall in the Westpac-ACCI business survey from 50.1 to 43.1 in the March quarter. Manufacturers reported the lowest new orders since the GFC (excluding the Covid lockdown period), although there was a suggestion from responders that the weakness in order was overstated by a slower than usual return from the summer holidays. Consumer sentiment dipped lower in March, with 'time to buy a major household item' assessments matching the generally soft tone seen in retail spending. The RBA's more balanced commentary seems to have had a positive impact though, with responses after the policy meeting much stronger than those before. The monthly CPI indicator rose a benign 0.2% in February, leaving the annual rate at 3.4% for a third consecutive month. We continue to expect inflation to meet the top of the 2-3% target range by the end of the year. Elsewhere, China's composite PMI improved from 50.9 to 52.7 in March, with gains in both manufacturing and services.

Other regions.

UK December quarter GDP was confirmed as a 0.3% decline, putting the country into a technical recession. In the euro zone, inflation is expected to remain at 2.6% in the year to March, with sticky services inflation driving most of the increase.

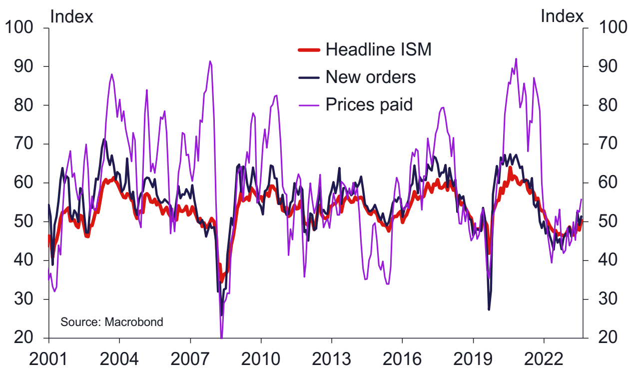
Trading partner real GDP (calendar years)

	Annual average % change			
	2022	**2023**	**2024**	**2025**
Australia	3.8	2.1	1.3	2.2
China	3.0	5.2	5.2	5.0
United States	2.1	2.5	2.6	1.4
Japan	1.0	2.0	0.7	1.0
East Asia ex China	4.5	3.4	4.1	4.2
India	7.2	7.7	6.5	6.4
Euro Zone	3.3	0.4	0.5	1.5
United Kingdom	4.1	0.4	0.5	1.3
NZ trading partners	3.3	3.4	3.4	3.4
World	3.5	3.3	3.3	3.1

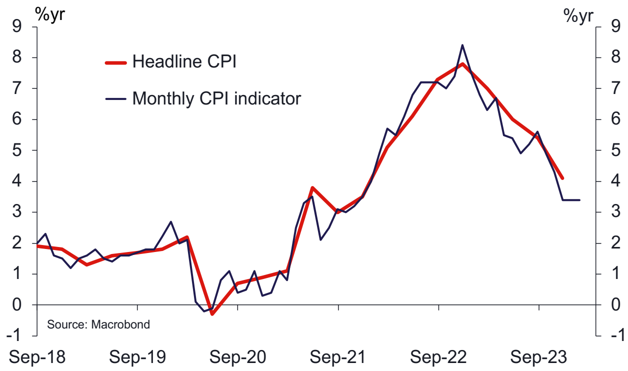
Australian & US interest rate outlook

	28-Mar	Jun-24	Dec-24	Dec-25
Australia				
Cash	4.35	4.35	3.85	3.10
90 Day BBSW	4.34	4.37	3.92	3.30
3 Year Swap	3.81	3.95	3.75	3.50
3 Year Bond	3.63	3.75	3.55	3.30
10 Year Bond	3.97	4.05	3.85	4.00
10 Year Spread to US (bps)	-24	5	5	0
US				
Fed Funds	5.375	5.125	4.375	3.375
US 10 Year Bond	4.21	4.00	3.80	4.00

US ISM manufacturing



Australian CPI inflation



Financial markets wrap

Interest rates.

NZ swap rates consolidated last week following a month-long decline. The 2yr traded between 4.80% and 4.90% and looks set to open higher today following the overnight rise in US bond yields, which responded to strong US manufacturing data. We target 5.00% this week. Major event risk comes from the plethora of Fed speakers, plus US payrolls data on Friday. The next major NZ events will be the RBNZ OCR review on 10 April and Q1 CPI data on 17 April.

Any rise in swap rates this week will be helped by paring of RBNZ OCR pricing, arguably too aggressive at a 50% chance of a cut in July, and 100% chance of cuts at the following meetings (our economists forecast the first cut in February 2025).

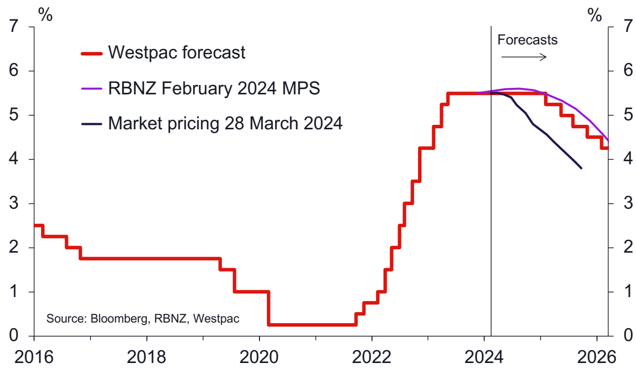
Foreign exchange.

NZD/USD has fallen 3c to 0.5940 over the past month and could extend to 0.5900 this week. The main driver has been a month-old rise in the broad US dollar, together with disappointing NZ GDP data. This week's US payrolls data and Fedspeak will be important for the US dollar's near-term prospects. We would expect to see exporters taking advantage of any decline in NZD/USD to 0.5900.

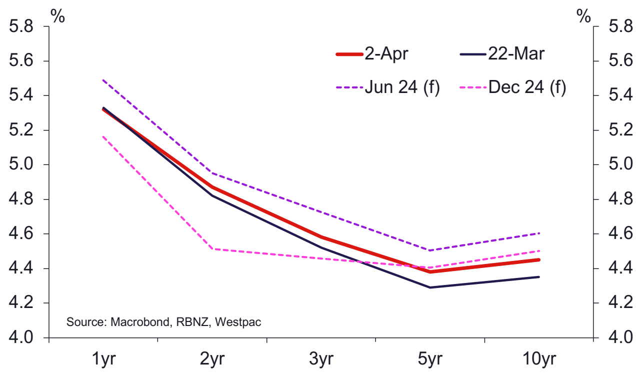
Multi-month, there is potential for a rebound to 0.6300, if our forecasts for the Fed and RBNZ prove correct (easing to start in June 2024 and February 2025, respectively).

NZD/AUD is showing tentative signs of forming a base in the high 0.91s. The main driver has been NZ-AU yields spreads, which have narrowed significantly over the past year but have limited downside from here.

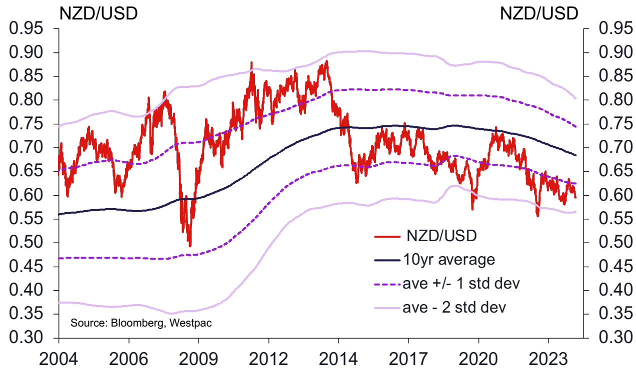
Official Cash Rate forecasts



Swap rates



NZD/USD vs rolling 10yr average



FX recent developments

	Historical data				F'cast
	Spot	**3mth range**	**5yr range**	**5yr avg**	**Dec-24**
USD	0.595	0.595-0.635	0.555-0.743	0.650	0.64
AUD	0.917	0.917-0.944	0.873-0.992	0.933	0.91
EUR	0.554	0.553-0.572	0.517-0.637	0.584	0.56
GBP	0.474	0.474-0.497	0.464-0.544	0.507	0.50
JPY	90.2	88.7-93.1	61.3-93.1	78.4	88.3

The week ahead

NZ Feb monthly employment indicator

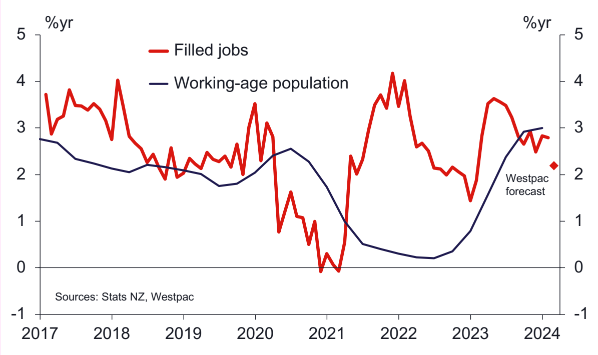
Apr 3, Last: +0.6%. Westpac f/c: 0.0%

The monthly employment indicator is drawn from income tax data, making it a comprehensive record of the number of people in work. While there are conceptual differences, it generally does a good job of predicting the more widely followed quarterly household survey measure of employment.

The 0.6% rise in jobs in January was stronger than expected. However, it may have been a product of shifting seasonal patterns in hiring, resulting in weaker Decembers and stronger Januarys. The broader picture is that jobs growth remains positive but has now fallen behind the pace of population growth, which continues to be boosted by record net inward migration.

We expect a flat result for February. The weekly data snapshots have been soft so far, but these have tended to understate the monthly result. (Note that this release was delayed by a week, after Stats NZ identified some issues with the supply of data.)

Monthly filled jobs growth



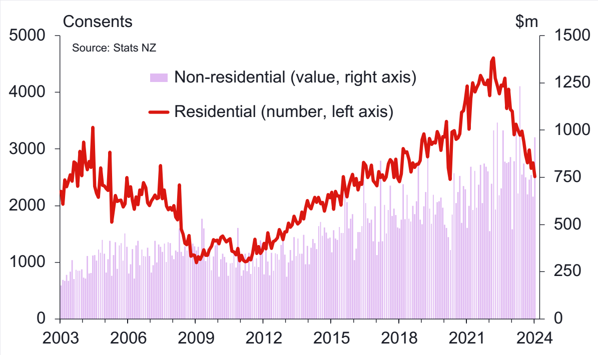
NZ Feb building consents

4 Apr, Last: -8.8 %. Westpac f/c: +5%

The number of new dwelling consents fell nearly 9% in January. Under the surface, the number of standalone homes being consented remains low. In addition, the number of townhouses and other medium-density developments being consented has fallen sharply, with developers reluctant to bring new projects to market given high financing costs and a slow market for sales.

We're forecasting a modest 5% bounce in consent numbers in February, with some of January's sharp drop in the more volatile consent categories likely to be reversed. However, that won't dislodge the longer-term downtrend in consent issuance. In annual terms, we expect consent numbers to slip below 36,000 for the first time since 2019.

NZ building consents

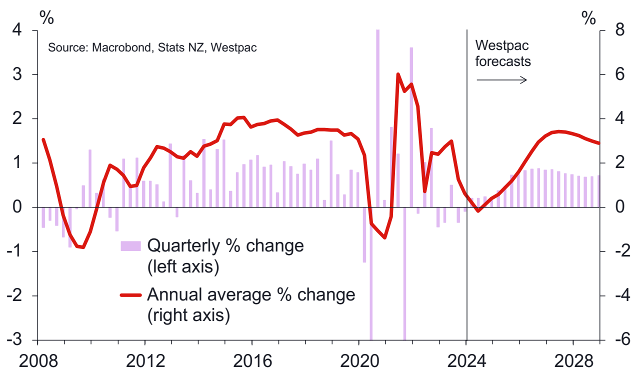


Economic and financial forecasts

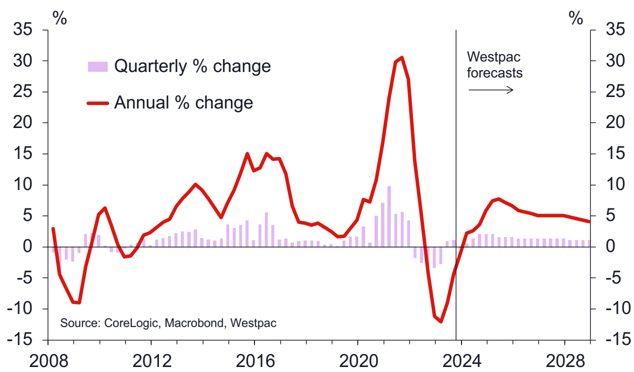
Economic indicators	Quarterly % change				Annual % change			
	Sep-23	Dec-23	Mar-24	Jun-24	2022	2023	2024	2025
GDP (production)	-0.3	-0.1	0.2	0.2	2.4	0.6	0.4	1.6
Consumer price index	1.8	0.5	0.8	0.6	7.2	4.7	2.8	2.3
Employment change	-0.1	0.4	0.0	0.2	1.7	2.4	0.3	1.0
Unemployment rate	3.9	4.0	4.3	4.6	3.4	4.0	5.1	5.2
Labour cost index (all sectors)	1.1	1.0	0.8	0.8	4.1	4.3	3.4	2.5
Current account balance (% of GDP)	-7.4	-6.9	-6.3	-6.0	-8.8	-6.9	-4.9	-3.9
Terms of trade	-0.6	-7.8	6.4	2.7	-4.1	-10.6	12.0	3.4
House price index	1.0	-0.2	0.5	1.3	-11.2	-1.1	5.9	6.7

Financial forecasts	End of quarter				End of year			
	Sep-23	Dec-23	Mar-24	Jun-24	2022	2023	2024	2025
OCR	5.50	5.50	5.50	5.50	4.25	5.50	5.50	4.50
90 day bank bill	5.66	5.65	5.60	5.60	4.26	5.65	5.50	4.50
2 year swap	5.53	5.28	5.10	4.95	5.10	5.28	4.50	4.00
5 year swap	4.90	4.84	4.60	4.50	4.67	4.84	4.40	4.10
10 year bond	4.87	5.09	4.85	4.70	4.31	5.09	4.60	4.25
TWI	70.6	70.8	72.2	72.3	70.8	70.8	71.7	70.0
NZD/USD	0.61	0.60	0.62	0.63	0.60	0.60	0.64	0.65
NZD/AUD	0.92	0.93	0.94	0.93	0.92	0.93	0.91	0.89
NZD/EUR	0.56	0.56	0.57	0.57	0.59	0.56	0.56	0.56
NZD/GBP	0.48	0.49	0.49	0.50	0.51	0.49	0.50	0.50

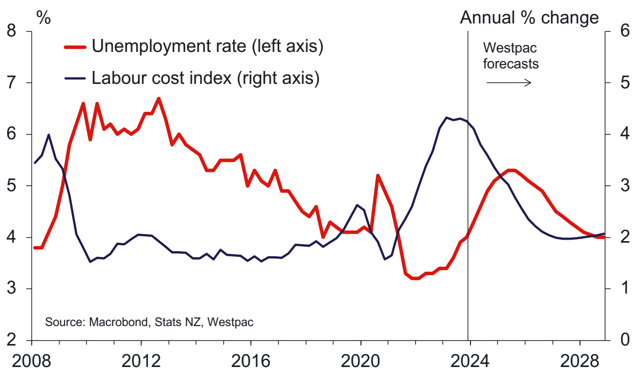
GDP growth



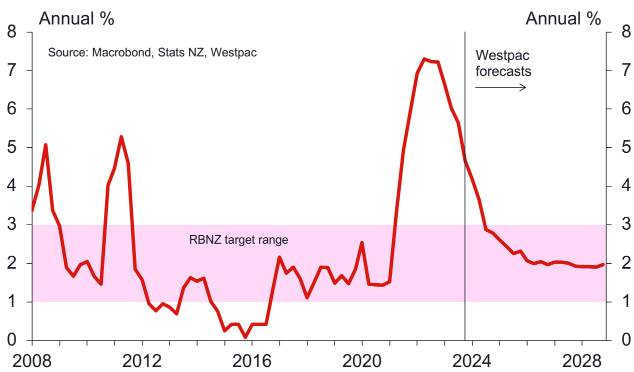
House prices



Employment and wage growth



Consumer price inflation



Data calendar

		Last	Market median	Westpac forecast	Risk/Comment
Mon 01					
NZ	Easter Monday	–	–	–	Public holiday; markets closed.
Jpn	Q1 Tankan large manufacturers index	12	10	–	Setting the tone for the year.
Chn	Mar Caixin manufacturing PMI	50.9	50.7	–	Stimulus and global structural growth to buoy in '24.
US	Mar ISM manufacturing	47.8	48.5	–	Employment indicator signalling downside for jobs.
	Feb construction spending	–0.2%	0.5%	–	A dwindling pipeline sees fewer projects in motion.
Tue 02					
Aus	RBA Minutes	–	–	–	RBA's commentary becoming more balanced.
	RBA Assist' Governor (Financial Mkts)	–	–	–	Speaking on "The Future for Monetary Policy Implementation".
	Mar CoreLogic home value index	0.6%	–	0.6%	Slightly firmer pace than Nov-Jan but still down vs. 2023.
	Mar MI inflation gauge %yr	4.0%	–	–	Provides a general view of risks.
	Mar ANZ job ads	–2.8%	–	–	Official data points to further declines ahead.
US	Feb factory orders	–3.6%	1.0%	–	Palsy durable goods to keep print near 0.
	Feb JOLTS job openings	8863k	–	–	Businesses taking down the 'help needed' sign.
	Fedspeak	–	–	–	Williams, Mester, Daly.
Wed 03					
NZ	GlobalDairyTrade auction (WMP)	–4.2%	–	–	GDT Pulse, futures prices down slightly on previous auction.
	Feb employment indicator	0.6%	–	0.0%	Surprising strength in Jan, not expected to be maintained.
Chn	Mar Caixin services PMI	52.5	–	–	Full impact of stimulus is yet to be felt.
Eur	Mar CPI %yr	2.6%	2.6%	–	Sticky services inflation drives most of inflation.
	Feb unemployment rate	6.4%	–	–	Labour market remains historically tight.
US	Mar ISM non–manufacturing	52.6	52.6	–	Employment indicator the focus.
	FOMC Chair Powell	–	–	–	Speaking at a Standford Forum.
	Fedspeak	–	–	–	Goolsbee.
Thu 04					
NZ	Feb building permits	–8.8%	–	5.0%	Bounce after recent falls, annual downtrend still in place.
	Mar ANZ commodity prices	3.5%	–	2.0%	Strong lift in beef export prices.
Aus	RBA Assist' Governor (Financial Syst)	–	–	–	Speaking at the COSBOA National Small Business Summit.
	Feb dwelling approvals	–1.0%	3.0%	3.0%	Feb to provide a clearer idea on the underlying trend.
Fri 05					
Aus	Feb goods trade balance $bn	11.0	10.8	9.7	Surplus to narrow, lower commodity prices a drag on exports.
Jpn	Feb household spending %yr	–6.3%	–3.0%	–	Wages growth to support spending, in time.
Eur	Feb retail sales	0.1%	–	–	Tight financial conditions dissuade consumers from spending.
US	Mar non–farm payrolls	275k	216k	180k	Likely to moderate and narrow gap to other indicators.
	Mar unemployment rate	3.9%	3.8%	3.9%	Unemployment rate to grind higher in 2024...
	Mar average hourly earnings %mth	0.1%	0.3%	–	... dampening wage growth.
	Feb consumer credit $bn	19.5	–	–	Some slowing occurring as financial conditions remain tight.

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