



Weekly Economic Commentary.

On the up and up.

The most recent batch of economic indicators have generally been on the positive side, in line with our forecasts of a steady lift in activity over the rest of this year. If that continues, government revenue is likely to significantly outstrip last month's Budget projections.

The international trade figures for the March quarter showed that New Zealand's terms of trade were broadly flat, with a modest dip in both export and import prices. In terms of volumes, exports were down for the quarter, but imports saw another strong increase, highlighting the rebound in both consumer demand and business investment. Notably, there was little evidence of rising international prices for imported goods, although shipping costs have clearly spiked.

Also for the March quarter, construction activity lifted by 3.7%. Homebuilding activity has been resilient to the Covid-related headwinds that buffeted the economy over the past year, supported by low interest rates and related strong gains in house prices. Non-residential construction also rose, although the picture here is more mixed. We've seen some softness in the retail and office segments in the wake of Covid, but demand for industrial space has been strong.

The lift in construction activity was stronger than we and the market expected. Along with the firm retail spending figures released last month, that does suggest some upside risk to our March quarter GDP forecast of a flat outturn. We'll finalise our GDP forecast later this week as the final suite of indicators is released.

The strength in homebuilding is likely to continue over the next year, given the size of the existing pipeline of work. Building consents rose another 4.8% in April, taking the total over the last year to nearly 43,000, another all-time high. Over 18,000 of those consents were in Auckland alone, reflecting the easing in building restrictions resulting from the city's Unitary Plan in 2016.

The strong pace of homebuilding, combined with the sharp drop-off in population growth as a result of the border closure, means that the country is now making significant



progress in addressing the housing shortage that had accumulated over previous years. Indeed, on current trends, we estimate that Auckland could eliminate its shortage in the next three years, with the rest of the country taking somewhat longer.

The final release of note last week was the Government's financial accounts for the 10 months to April. This was the first monthly report since the Treasury updated its projections in the May Budget, and we weren't surprised to see another strong result. After just one month, government revenue is already more than \$3bn (almost 1% of GDP) ahead of forecast.

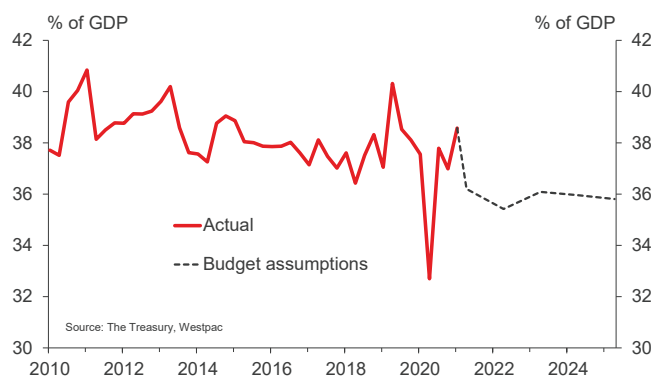
As we said in our review of the Budget, the issue is not with the Treasury's economic forecasts, which are now pretty similar to our own. After a soft patch during the summer period, GDP is expected to grow steadily over the rest of this year, with a further pickup in 2022 as international travel is gradually allowed to resume.

The issue, rather, is around how those activity forecasts translate into government revenue. The Budget projections assumed that revenue, relative to GDP, would fall below average and remain there for years to come. This assumption was little changed since the Half-Year Update last December, despite the monthly accounts repeatedly coming out stronger than forecast since then.

Our view is that, by the next fiscal update, the Government will again find itself with much more revenue than expected. That will again provide scope to both increase spending and reduce its borrowing requirement.

While we acknowledge that tax forecasting is a difficult task, we would point out that this is one area where forecast errors have real consequences. For one, it suggests that the current fiscal stance is far less stimulatory than was portrayed in the Budget: rather than a positive impulse on growth over the coming year, it's likely to provide a negative impulse, as more tax revenue is taken out of the private sector than was planned. It also suggests that social spending or economic support measures that would have been of value over the coming year may have been delayed unnecessarily.

Government revenue as a % of nominal GDP



Michael Gordon, Acting Chief Economist

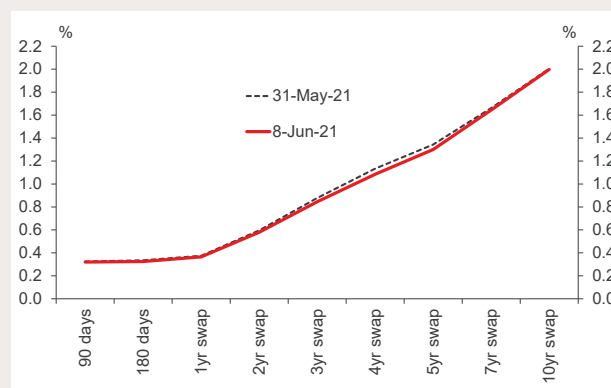
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Fixed vs floating for mortgages.

We expect that floating rates, and shorter fixed-term rates, will be stable over the coming months. Inflation is set to spike higher this year, but the Reserve Bank will not need to respond to this.

Longer-term interest rates are now rising in response to the improved economic outlook. Based on our forecasts, taking a longer-term fixed rate (three to five years) will still be less expensive for borrowers than taking a short-term rate now and refixing later. However, the advantage is narrowing.

NZ interest rates



The week ahead.

NZ June ANZBO business confidence (Preliminary)

June 9, Last (Final May): 1.8

- Business confidence and expectations of own activity continued to hold firm and trend higher in May.
- The initial release of the June business survey will let us see if the strong trend in economic data has continued. Despite the Budget not containing much additional support directly for businesses, this is the first chance we'll get to see how businesses think they will be impacted changes in government policy.
- Underlying inflation gauges will again continue to be an area worth watching. In particular, we'll be keeping a close eye on inflation expectations which have been increasing for 10 consecutive months and now sit at 2.22%.

NZ business confidence

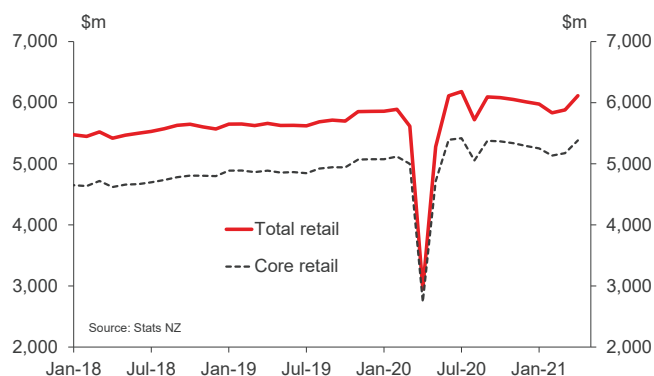


NZ May Retail Card Spending

June 10, Last: +4.0%, Westpac f/c: +0.1%

- Retail spending rose by 4% in April. That rise was boosted by the easing in Covid restrictions that had dampened spending in both February and March.
- We're forecasting a 0.1% rise in spending in May. Looking through the swings in spending associated with changes in the Alert Level, the trend in spending has been flattening off. A key reason for this is the slowdown in population growth since the borders were closed.
- There has also been a change in the composition of spending. Since the outbreak of Covid, spending on durable items like household furnishings has been strong. That's helped to offset the drag from reduced spending in the hospitality sector.

Retail card spending

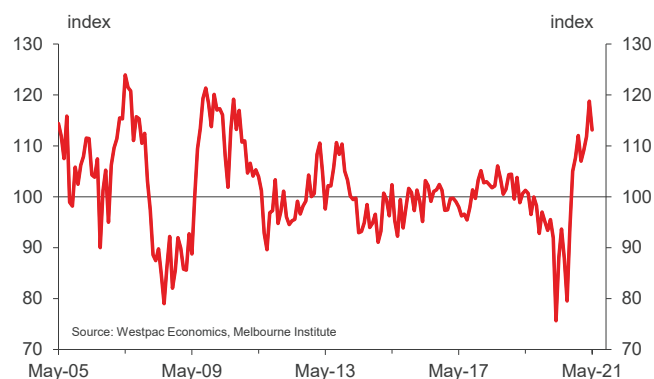


Aus Jun Westpac-MI Consumer Sentiment

Jun 9, Last: 113.1

- Sentiment fell 4.8% to 113.1 in May from 118.8 in April. The decline was a little surprising given what looked to be a relatively well-received Federal Budget although it should be noted that sentiment was coming of an 11yr high with May still the second highest print since April 2010.
- The latest survey is in the field over the week to June 8. The major development this month is Vic's move into a 14-day lockdown following a spate of COVID cases. The scale of the hit to Vic consumers and the degree of spill-over to sentiment inter-state will be of key interest. Other factors are likely to remain strongly supportive with housing markets booming and the ASX posting a strong rally, although labour market indicators have been a little more mixed in recent weeks, suggesting some fallout from the end of JobKeeper.

Aus Consumer Sentiment Index

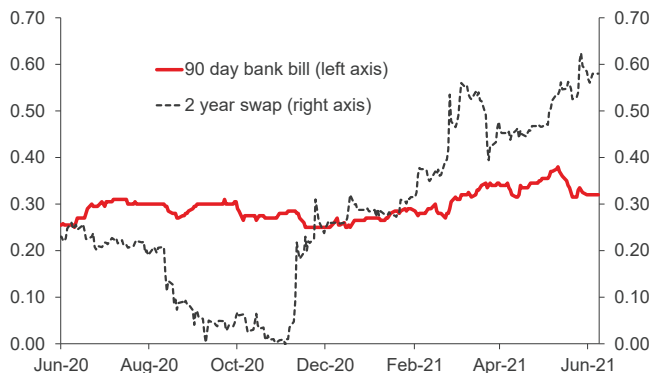


New Zealand forecasts.

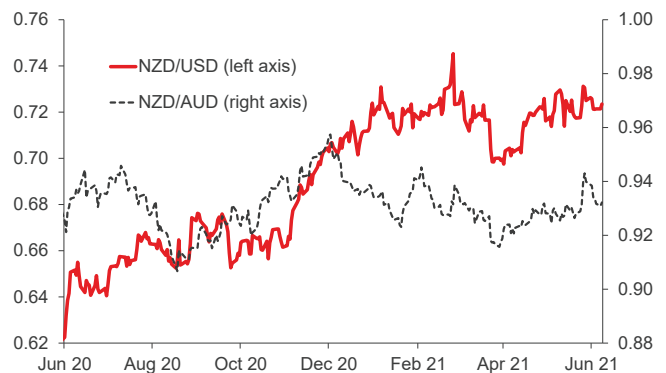
| Economic forecasts | Quarterly | | | | Annual | | | |
|----------------------------------|-----------|------|------|------|--------|------|-------|-------|
| | 2020 | 2021 | | | 2019 | 2020 | 2021f | 2022f |
| % change | Dec (a) | Mar | Jun | Sep | | | | |
| GDP (Production) | -1.0 | 0.0 | 1.2 | 0.5 | 2.4 | -2.9 | 4.2 | 4.4 |
| Employment | 0.6 | 0.5 | 0.1 | 0.4 | 1.2 | 0.8 | 1.4 | 2.1 |
| Unemployment Rate % s.a. | 4.9 | 4.7 | 4.7 | 4.6 | 4.1 | 4.9 | 4.5 | 4.1 |
| CPI | 0.5 | 0.8 | 0.5 | 0.8 | 1.9 | 1.4 | 2.4 | 1.4 |
| Current Account Balance % of GDP | -0.8 | -1.9 | -2.9 | -3.6 | -3.3 | -0.8 | -3.7 | -2.7 |

| Financial forecasts | Jun-21 | Sep-21 | Dec-21 | Mar-22 | Jun-22 | Sep-22 |
|---------------------|--------|--------|--------|--------|--------|--------|
| Cash | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 |
| 90 Day bill | 0.35 | 0.35 | 0.35 | 0.35 | 0.35 | 0.35 |
| 2 Year Swap | 0.45 | 0.45 | 0.45 | 0.50 | 0.55 | 0.60 |
| 5 Year Swap | 1.10 | 1.15 | 1.20 | 1.25 | 1.30 | 1.35 |
| 10 Year Bond | 1.75 | 1.80 | 1.90 | 2.00 | 2.10 | 2.20 |
| NZD/USD | 0.73 | 0.73 | 0.74 | 0.76 | 0.76 | 0.76 |
| NZD/AUD | 0.92 | 0.91 | 0.90 | 0.89 | 0.89 | 0.89 |
| NZD/JPY | 79.6 | 80.3 | 82.1 | 85.1 | 84.4 | 84.4 |
| NZD/EUR | 0.61 | 0.60 | 0.60 | 0.61 | 0.60 | 0.60 |
| NZD/GBP | 0.52 | 0.52 | 0.52 | 0.54 | 0.54 | 0.54 |
| TWI | 75.6 | 74.9 | 75.0 | 76.1 | 75.7 | 75.5 |

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 8 June 2021

| Interest rates | Current | Two weeks ago | One month ago |
|----------------|---------|---------------|---------------|
| Cash | 0.25% | 0.25% | 0.25% |
| 30 Days | 0.27% | 0.28% | 0.27% |
| 60 Days | 0.30% | 0.30% | 0.32% |
| 90 Days | 0.32% | 0.32% | 0.37% |
| 2 Year Swap | 0.58% | 0.53% | 0.52% |
| 5 Year Swap | 1.30% | 1.19% | 1.16% |

NZ foreign currency mid-rates as at 8 June 2021

| Exchange rates | Current | Two weeks ago | One month ago |
|----------------|---------|---------------|---------------|
| NZD/USD | 0.7235 | 0.7175 | 0.7283 |
| NZD/EUR | 0.5932 | 0.5892 | 0.5987 |
| NZD/GBP | 0.5101 | 0.5068 | 0.5206 |
| NZD/JPY | 79.03 | 78.16 | 79.13 |
| NZD/AUD | 0.9322 | 0.9282 | 0.9280 |
| TWI | 75.04 | 74.67 | 75.54 |

Data calendar.

| | | Last | Market median | Westpac forecast | Risk/Comment |
|---------------|-----------------------------------|---------|---------------|------------------|---|
| Mon 07 | | | | | |
| NZ | Queen's Birthday | - | - | - | Public holiday. |
| Aus | May ANZ job ads | 4.7% | - | - | Vacancies forging ahead, but employment has lagged. |
| Chn | May trade balance US\$bn | 42.85 | 50.50 | - | Export growth to remain robust through 2021. |
| | May foreign reserves \$bn | 3198.18 | 3214.5 | - | Authorities do not seem overly concerned re currency. |
| Eur | Jun Sentix investor confidence | 21 | 23.8 | - | Confidence will continue to build as recovery gathers pace. |
| US | Apr consumer credit | 25.841 | 22.500 | - | Auto loans providing strong support. |
| Tue 08 | | | | | |
| Aus | May NAB business survey | 32 | - | - | Conditions jumped 14pts to 32 past 2 mths. Potential pull-back? |
| Eur | Q1 GDP | -0.6% | -0.6% | - | Final estimate; no change expected. |
| | Jun ZEW survey of expectations | 84 | - | - | Will be looking through to the rebound phase in H2. |
| US | May NFIB small business optimism | 99.8 | 100.8 | - | Confidence running high across economy. |
| | Apr trade balance US\$bn | -74.4 | -68.5 | - | Strong consumer demand begets import strength. |
| | Apr JOLTS job openings | 8123k | - | - | Hiring rates and job openings the focus currently. |
| Wed 09 | | | | | |
| NZ | Jun ANZ business confidence | 1.8 | - | - | Confidence is likely to follow the trend of strong data. |
| Aus | Jun Westpac-MI Consumer Sentiment | 113.1 | - | - | Vic's 14-day snap lockdown to impact. |
| | RBA speak | - | - | - | RBA's Kent Gives Speech at Online Webinar. |
| | May 22 ABS Weekly Payrolls | - | - | - | Will provide important insights for May labour force survey. |
| Chn | May CPI %yr | 0.9% | 1.6% | - | Consumer price growth will remain benign in 21/22... |
| | May PPI %yr | 6.8% | 8.4% | - | ... despite upstream pressures. |
| | May M2 money supply %yr | 8.1% | 8.1% | - | Credit growth is weaker than 2020, but well up on 2019... |
| | May new loans, CNYbn | 1470.0 | 1400.0 | - | ... new loans are quality minded and targeting capacity. |
| Thu 10 | | | | | |
| NZ | May card spending | 4.0% | - | 0.1% | Spending continuing to firm, low population growth a drag. |
| Aus | Jun MI inflation expectations | 3.5% | - | - | Edged up in May, but still remain below pre-covid levels. |
| Eur | ECB policy decision | 0.0% | 0.0% | - | Looking for guidance on pace of purchases in Q3. |
| US | May CPI | 0.8% | 0.3% | 0.4% | Price pressures are expected to dissipate in coming months. |
| | Initial jobless claims | 385k | - | - | Continue to trend down. |
| | May monthly budget statement | -225.6 | - | - | Deficits to continue. |
| Fri 11 | | | | | |
| NZ | May manufacturing PMI | 58.4 | - | - | Strong trend to continue, mirroring global trend. |
| UK | Apr trade balance £bn | -1966 | - | - | Has fluctuated considerably over the Brexit/pandemic period. |
| US | Jun Uni. of Michigan sentiment | 82.9 | 83.8 | - | Sentiment measures have provided mixed signals of late. |

International forecasts.

| Economic Forecasts (Calendar Years) | 2017 | 2018 | 2019 | 2020f | 2021f | 2022f |
|-------------------------------------|------|------|------|-------|-------|-------|
| Australia | | | | | | |
| Real GDP %/yr | 2.4 | 2.8 | 1.9 | -2.4 | 5.2 | 3.6 |
| CPI inflation %/yr | 1.9 | 1.8 | 1.8 | 0.9 | 2.2 | 1.8 |
| Unemployment rate % | 5.5 | 5.0 | 5.2 | 6.8 | 5.0 | 4.7 |
| Current account % of GDP | -2.6 | -2.1 | 0.7 | 2.5 | 3.5 | 1.9 |
| United States | | | | | | |
| Real GDP %/yr | 2.3 | 3.0 | 2.2 | -3.5 | 6.5 | 4.1 |
| CPI inflation %/yr | 2.1 | 2.4 | 1.9 | 1.2 | 2.9 | 2.1 |
| Unemployment rate % | 4.4 | 3.9 | 3.7 | 8.1 | 5.3 | 4.3 |
| Current account % of GDP | -2.3 | -2.3 | -2.6 | -2.5 | -2.4 | -2.4 |
| Japan | | | | | | |
| Real GDP %/yr | 1.7 | 0.6 | 0.3 | -4.8 | 2.7 | 2.1 |
| Euro zone | | | | | | |
| Real GDP %/yr | 2.6 | 1.9 | 1.3 | -6.6 | 4.2 | 4.0 |
| United Kingdom | | | | | | |
| Real GDP %/yr | 1.7 | 1.3 | 1.4 | -9.9 | 5.5 | 5.5 |
| China | | | | | | |
| Real GDP %/yr | 6.9 | 6.7 | 5.8 | 2.3 | 10.0 | 5.7 |
| East Asia ex China | | | | | | |
| Real GDP %/yr | 4.7 | 4.4 | 3.7 | -2.4 | 4.8 | 4.9 |
| World | | | | | | |
| Real GDP %/yr | 3.8 | 3.6 | 2.8 | -3.3 | 5.9 | 4.5 |

Forecasts finalised 7 May 2021

| Interest rate forecasts | Latest | Jun-21 | Sep-21 | Dec-21 | Mar-22 | Jun-22 | Sep-22 |
|-------------------------|--------|--------|--------|--------|--------|--------|--------|
| Australia | | | | | | | |
| Cash | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 |
| 90 Day BBSW | 0.03 | 0.07 | 0.09 | 0.10 | 0.10 | 0.10 | 0.10 |
| 10 Year Bond | 1.69 | 1.95 | 2.10 | 2.20 | 2.30 | 2.40 | 2.50 |
| International | | | | | | | |
| Fed Funds | 0.125 | 0.125 | 0.125 | 0.125 | 0.125 | 0.125 | 0.125 |
| US 10 Year Bond | 1.62 | 1.85 | 2.00 | 2.10 | 2.20 | 2.30 | 2.40 |

| Exchange rate forecasts | Latest | Jun-21 | Sep-21 | Dec-21 | Mar-22 | Jun-22 | Sep-22 |
|-------------------------|--------|--------|--------|--------|--------|--------|--------|
| AUD/USD | 0.7657 | 0.80 | 0.82 | 0.85 | 0.85 | 0.85 | 0.85 |
| USD/JPY | 110.26 | 109 | 110 | 111 | 111 | 111 | 110 |
| EUR/USD | 1.2114 | 1.21 | 1.23 | 1.25 | 1.26 | 1.27 | 1.27 |
| GBP/USD | 1.4092 | 1.40 | 1.41 | 1.41 | 1.41 | 1.42 | 1.42 |
| USD/CNY | 6.4042 | 6.30 | 6.20 | 6.15 | 6.10 | 6.05 | 6.00 |
| AUD/NZD | 1.0717 | 1.10 | 1.11 | 1.12 | 1.12 | 1.12 | 1.12 |

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