

# WESTPAC WEEKLY ECONOMIC COMMENTARY

## Throwing the doors open.

16 May 2022



Mount Cook buttercup

### Westpac Economics Team

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For the past two years, the closure of the borders has been a significant drag on economic activity in New Zealand. That's been felt in terms of a loss of international tourist dollars. It's also resulted in a sharp downturn in population growth, which has affected the labour market and demand growth. Following the easing in border restrictions over the past month, we are now seeing those drags starting to reverse. However, there is still a long way to go.

In terms of visitor arrivals, April saw 28,000 people landing on our shores for short-stay trips. That's up sharply from rates of around 5,000 per month earlier in the year. The bulk of that rise was related to New Zealand citizens who now reside abroad, many of whom delayed coming home for holidays in recent years due to the previous isolation requirements.

More notably, we are also seeing the early signs of a recovery in international tourist arrivals. The borders opened for visitors from Australia mid-way through April. And while the absolute number of visitors from across the ditch are still low, numbers have been climbing quickly, rising from effectively zero to close to 3,000.

We expect international tourist numbers will continue to rise quickly over the coming months. Australian households are starting to travel again, and the borders with other markets will reopen over the coming months. It will still take some time for tourist numbers to retrace the levels we saw prior to the pandemic, especially as visitors from the high spending Chinese

market are unlikely to return until 2023. Even so, this change in direction will be a big boost for spending and confidence in our hospitality and accommodation sectors.

The recovery in international tourism will be an important buffer for the economy. The closure of our borders and related net loss of international tourist dollars has resulted in a drag equivalent to around 2% of annual nominal GDP for the past couple of years. As that spending starts to come back, it will limit the downside for growth as domestic demand cools in the face of rising interest rates.

In addition to a rise in short-term arrivals, the number of people moving to New Zealand on a longer-term basis has also started to turn around. Again, the net number of new migrants is still low with 1,200 people arriving in April (compared to rates of around 4,000 prior to the pandemic). Nevertheless, the outflow of people seen over the past year looks like it has stabilised. It's also notable that we have yet to see a pick-up in departures of New Zealanders.

We do expect the coming year will see longer-term departures rise as many younger New Zealanders who delayed OEs during the pandemic start to travel again. As a result, net migration is set to remain low for some time.

Longer term, net migration will turn positive again as the number of departing New Zealanders returns to more normal levels. Even so, we don't expect that net migration will rise back to the sort of levels that we saw over the past decade, with the Government now rolling out a reset of migration policy. While still trying to address current shortages of labour, those policy changes are focused on supporting job opportunities and skills development among existing New Zealand residents. To achieve that aim, the Government is tightening entry requirements for new arrivals based around skill levels.

Given that policy change, we expect that net migration will settle at around 30,000 people per annum. That's a big step down from the annual inflows of 50,000 to 60,000 people per annum that we saw in the years leading up to the pandemic. And the impacts will be felt through the labour market and economy more widely.

## Inflation, the RBNZ and the housing market.

Last week saw the release of the RBNZ's latest survey of inflation expectations. The closely watched 2-year ahead inflation measure remained at 3.3%. At the same time, expectations for inflation in five years' time have risen for a third successive quarter, climbing to 2.4% (up from 2.3%).

The elevated level of inflation expectations has raised red flags at the RBNZ, and was a key influence on April's 50bp OCR hike. We're forecasting another 50bp rise at the upcoming May policy meeting and a series of rapid OCR increases in the following months.

While interest rates are set to push into tight territory over the coming year, there are big questions about how much tightening will be required. The RBNZ will be watching for signs that OCR hikes are gaining traction in terms of slowing domestic demand. And on this front, the key area to watch is the housing market.

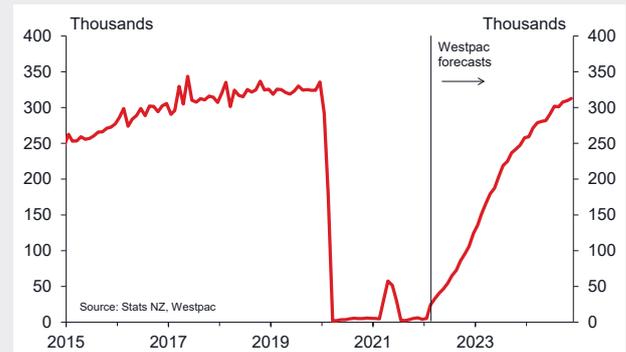
After a period of strong house price gains over the past couple of years, the market is now undergoing a rapid correction. Prices fell by 1.1% in April, and are now down 5% from their peaks in November. With interest rates continuing to rise, we expect that house prices will fall by 10% over calendar 2022, with a further 5% drop expected over 2023.

The housing market is a key influence on households' wealth and confidence. And just as the earlier period of rapid house price gains boosted spending appetites through the pandemic, the slowdown now in train signals a period of softer spending growth over the next few years. That will have an important impact on the strength of domestic inflation pressures.

## Chart of the week

Prior to the pandemic, international tourists spent around \$12bn per annum in New Zealand, nearly twice the amount that New Zealanders spent on overseas holidays. While still low, international visitor numbers have started to rise following the reopening of the borders. And although it will take some time for visitor arrivals to retrace their pre-pandemic highs, this signals big changes ahead for our hospitality and tourism sectors.

Monthly international visitor arrivals, s.a.

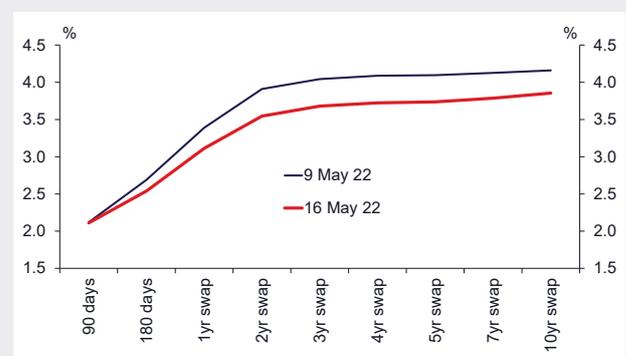


## Fixed vs floating for mortgages

Wholesale interest rates have moved above where we expect the Official Cash Rate to peak this year. That suggests to us that there is no cost advantage to fixing for longer terms.

While the one-year mortgage rate is likely to rise further in the year ahead, fixing and rolling for this term is likely to produce a lower borrowing cost on average over the next few years. Longer fixed terms would be more suited to those who want certainty in their repayments.

NZ interest rates



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# The week ahead

## NZ GlobalDairyTrade auction, whole milk powder prices

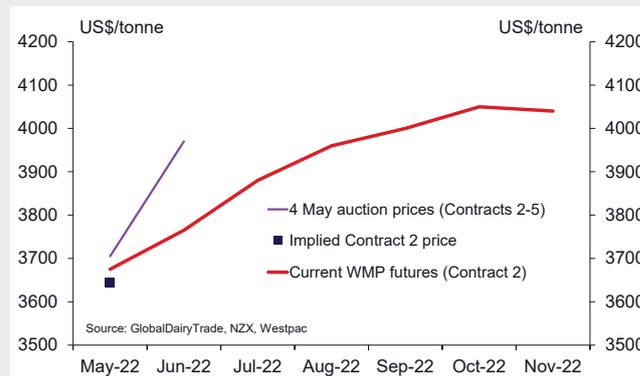
May 18, Last: -6.5%, Westpac: -2.0%

We expect whole milk powder prices (WMP) to fall 2% at the upcoming dairy auction. Prices have plunged over the last four auctions by a combined 14% as the Covid outbreak in China and a temporary surge in auction volumes have weighed on global dairy prices.

Our pick is roughly similar to futures market pricing.

Looking to the second half of 2022, we expect prices to regain some lost ground as market fundamentals remain strong. We also expect a boost to prices when China's Omicron wave eventually passes and the related Covid restrictions are relaxed.

## Whole milk powder prices



## NZ Government Budget 2022

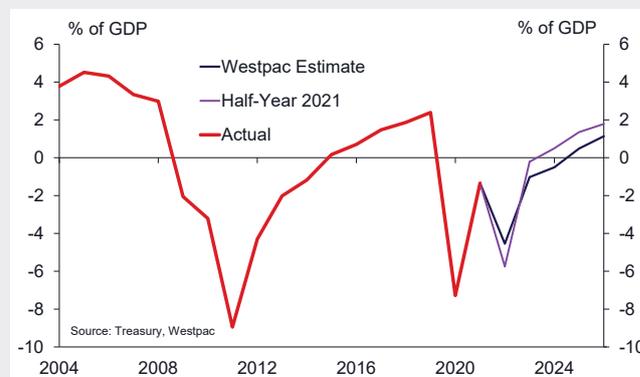
May 19

We expect Budget 2022 to show that, all things Covid considered, the Government's books continue to be in good shape.

While not strictly news, Budget 2022 will highlight the Government's newly minted fiscal rules and the realisation that the Government is not as debt constrained as previously thought.

Market interest will be on the expansion in the bond programme to facilitate buying back of the Reserve Bank's Government bond holdings. To this end, we anticipate a circa \$28 billion increase in bond issuance spread over the 2023 through 2026 fiscal years.

## Operating balance (OBEGAL) as a % of GDP



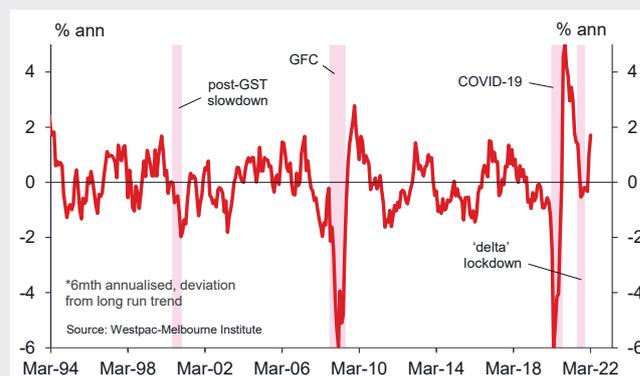
## Aus Mar Westpac-MI Leading Index

May 18, Last: 1.71%

The six-month annualised growth rate rose to 1.71% in March from 1.02% in February – posting the fastest growth rate since May 2021. This largely reflects the rebound from last year's 'delta' lockdowns with Q3 disruptions falling into the base of six-month growth rate calculations.

The Apr update is likely to show a similar pace of expansion. While monthly updates to several components will be soft (dwelling approvals down sharply, off a choppy few months, the ASX200 down -0.9% in April, consumer sentiment based measures deteriorating sharply in May) other components have been more stable and supportive in the case of commodity prices (up another 1.7% mth in AUD terms). The base effects from last year's 'delta' disruptions will also continue to hold up 6mth growth rates.

## Aus Westpac-MI Leading Index



# The week ahead

## Aus Q1 Wage Price Index %qtr

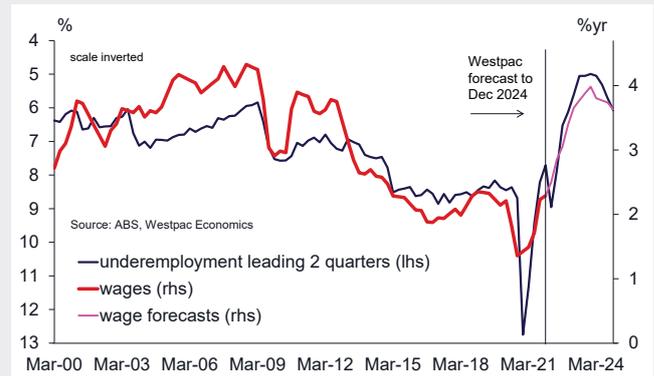
May 18, Last: 0.7%, WBC f/c: 0.8%  
Mkt f/c: 0.8%, Range: 0.7% to 0.8%

The Wage Price Index (WPI) lifted 0.7% in the Dec quarter, spot on Westpac's and the market forecast. This followed on from a 0.6% gain in Q3 which was a lift from the 0.4% print in Q2.

The annual pace lifted to 2.3% from 2.2% and is well up on the low of 1.4% in the later half of 2020. Wages are now back to a pre-Covid pace where wages were underperforming economic activity. If there was ever a time for wages to regain some of relationship with broader labour market indicators, 2022 must be the year.

Even more important than the fall in unemployment to 4% has been the more than halving of underemployment, from a peak of 13.6% in Apr 2020 to 6.3% in Mar 2022. Along with business and consumer surveys reporting meaningful rises in wages, we are looking for the Wage Price Index quarterly pace to lift to 0.8% from 0.7%. A rise closer to, or above 1.0% would be a surprise given the lags between labour market conditions and wages plus the structure of the WPI.

## Aus underemployment and wages



## Aus April Labour Force Survey, employment '000

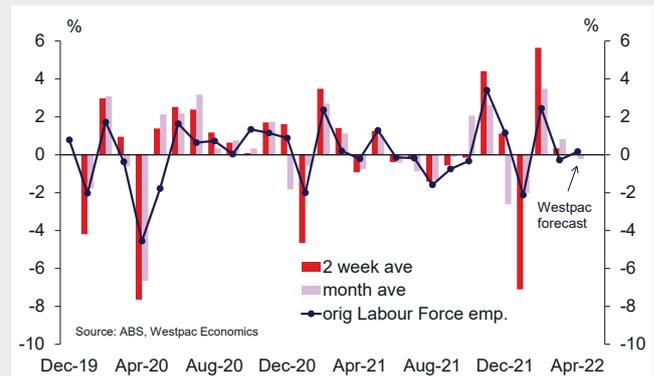
May 19, Last: 17.9k, WBC f/c: 20k  
Mkt f/c: 30k Range: 20k to 60k

March saw the 5th consecutive gain in employment with a 17.9k gain, a bit softer than Westpac's 25k estimate and below the market estimate of 30k. Given flooding and wide spread heavy rain on the east coast, it is not surprising that hours worked contracted 0.6%.

Given the flooding and wet conditions in Mar there was expected weakness in NSW (-0.3k) but we were surprised by the greater weakness in Victoria (-2.8k) contrasted by robust Queensland employment (+8.0k).

Based on a two-week average to Mar 12 compared to a two-week average to Apr 16, payrolls were flat through that five-week period. Our current forecast for employment in the April Labour Force Survey is +32k which we estimate to be a 0.3% rise in original (not seasonally adjusted) terms. We have revised our forecast from +32k to +20k to acknowledge a softer momentum in employment while still allowing for a softer than expected recovery in hours worked.

## Aus employment and labour force participation



## Aus April Labour Force Survey, unemployment %

May 19, Last: 4.0%, WBC f/c: 3.9%  
Mkt f/c: 3.9% Range: 3.7% to 4.0% tr

With a fifth consecutive monthly gain in employment there was a small dip in the participation rate to 66.42% from 66.45% (66.4% from 66.5% rounded). This is not surprising as the wet conditions and flooding in some regions would have discouraged workers from looking, restricting the rise in the labour force to just 8.5k and thus holding the unemployment rate flat at 4.0% (now 3.95% from 4.04%).

As noted by the ABS, 4.0% is the lowest the unemployment rate has been in the monthly survey. Lower rates were seen in the series before November 1974, when the survey was quarterly.

With our forecast for +20k on employment holding the participation rate flat at 66.42% will see a 13k rise in employment with the unemployment rate rounding down to 3.9%.

## Aus unemployment

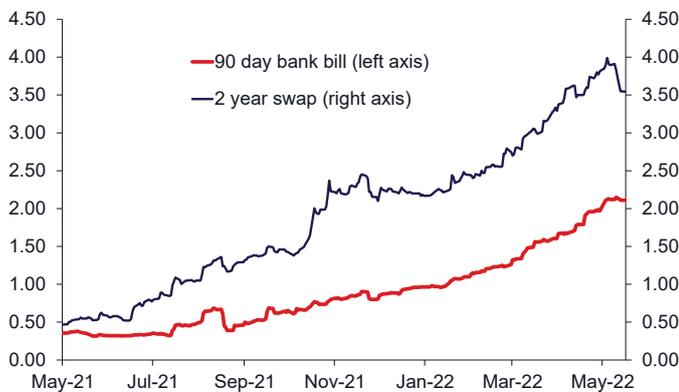


# New Zealand forecasts

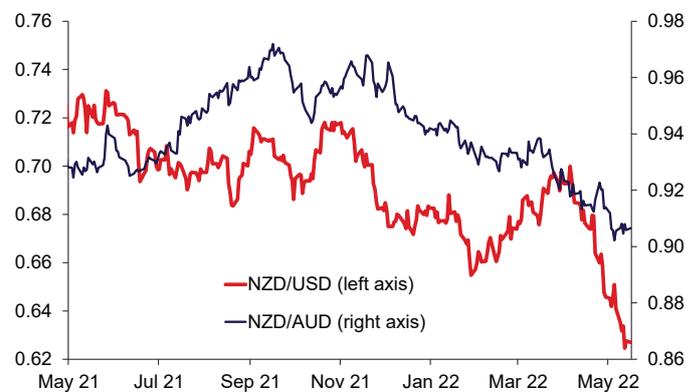
Economic forecasts	Quarterly				Annual			
	2021	2022						
% change	Dec (a)	Mar	Jun	Sep	2020	2021	2022f	2023f
GDP (Production)	3.0	0.3	0.7	2.3	-2.1	5.6	3.4	4.8
Employment	0.0	0.1	0.3	0.3	0.6	3.5	0.8	0.9
Unemployment Rate % s.a.	3.2	3.2	3.1	3.0	4.9	3.2	3.0	3.3
CPI	1.4	1.8	0.8	1.1	1.4	5.9	4.3	2.7
Current Account Balance % of GDP	-5.6	-5.8	-6.5	-6.5	-0.8	-5.6	-6.1	-5.5

Financial forecasts	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23
Cash	2.00	2.50	3.00	3.00	3.00	3.00	3.00
90 Day bill	2.40	2.90	3.10	3.10	3.10	3.10	3.10
2 Year Swap	4.00	4.00	3.90	3.70	3.50	3.30	3.10
5 Year Swap	4.10	4.00	3.90	3.70	3.50	3.35	3.20
10 Year Bond	3.80	3.70	3.50	3.30	3.20	3.10	3.00
NZD/USD	0.65	0.67	0.69	0.70	0.71	0.72	0.72
NZD/AUD	0.90	0.91	0.91	0.91	0.91	0.91	0.90
NZD/JPY	83.9	85.8	86.9	87.5	88.0	87.2	87.1
NZD/EUR	0.61	0.62	0.63	0.63	0.63	0.63	0.63
NZD/GBP	0.52	0.53	0.54	0.55	0.55	0.54	0.54
TWI	71.3	72.6	73.8	74.0	74.4	74.4	74.6

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 16 May 2022

Interest rates	Current	Two weeks ago	One month ago
Cash	1.50%	1.50%	1.50%
30 Days	1.83%	1.75%	1.57%
60 Days	1.97%	1.92%	1.68%
90 Days	2.11%	2.08%	1.79%
2 Year Swap	3.55%	3.85%	3.50%
5 Year Swap	3.74%	3.98%	3.64%

NZ foreign currency mid-rates as at 16 May 2022

Exchange rates	Current	Two weeks ago	One month ago
NZD/USD	0.6270	0.6452	0.6741
NZD/EUR	0.6030	0.6129	0.6241
NZD/GBP	0.5121	0.5133	0.5174
NZD/JPY	81.03	83.79	85.35
NZD/AUD	0.9065	0.9119	0.9148
TWI	70.83	71.78	73.05

# Data calendar

		Last	Market median	Westpac forecast	Risk/Comment
<b>Mon 16</b>					
NZ	Apr BusinessNZ PSI	51.6	-	-	Returned to growth in March as Omicron peak passed.
Chn	Apr retail sales ytd %yr	3.3%	1.2%	-	Near-term weakness in consumption due to lockdowns...
	Apr fixed asset investment ytd %yr	9.3%	7.0%	-	... but building momentum for investment...
	Apr industrial production ytd %yr	6.5%	5.0%	-	... and lingering strength in trade providing resilience.
Eur	Mar trade balance €bn	-9.4	-	-	Deficit to remain wide on elevated energy prices.
UK	May Rightmove house prices	1.6%	-	-	Demand to soften as rate hikes take full effect.
US	May Fed Empire state index	24.6	15.0	-	NY mfg sector well supported by firm order pipeline.
	Fedspeak	-	-	-	Williams.
<b>Tue 17</b>					
Aus	RBA minutes	-	-	-	More colour to the RBA Boards views.
Eur	Q1 GDP	0.2%	0.2%	-	Second estimate to confirm rapid slowing of economy.
UK	Mar ILO unemployment rate	3.8%	3.8%	-	Unemployment now at pre-Covid level.
US	Apr retail sales	0.5%	1.0%	-	Inflation pressuring discretionary incomes and spending.
	Apr industrial production	0.9%	0.4%	-	Volatility to linger as firms navigate supply issues.
	Mar business inventories	1.5%	1.9%	-	Businesses rebuilding inventory at a strong pace.
	May NAHB housing market index	77	75	-	Affordability concerns; rising input costs and interest rates.
	Fedspeak	-	-	-	Chair Powell interview. Bullard, Harker and Mester too.
<b>Wed 18</b>					
NZ	GlobalDairyTrade auction price (WMP)	-6.5%	-	-2.0%	China's Omicron outbreak still weighing on prices.
Aus	Apr Westpac-MI Leading Index	1.71%	-	-	Post-delta rebound still driving strong above-trend reads.
	Q1 wage price index	0.7%	0.8%	0.8%	A tighter labour market will be pushing on wages in 2022.
Eur	Apr CPI	0.6%	0.6%	-	Elevated energy prices remains the key driver...
UK	Apr CPI	1.1%	-	-	... behind European and UK headline inflation.
US	Apr housing starts	0.3%	-1.3%	-	Strength of labour market and limited supply...
	Apr building permits	0.4%	-2.4%	-	... to support residential construction into the medium term.
	Fedspeak	-	-	-	Evans and Harker.
<b>Thu 19</b>					
NZ	Q1 PPI	1.4%	-	-	Higher oil and dairy prices over the quarter.
	Budget 2022	-	-	-	Budget will show Govt's books in relatively good shape.
Aus	Apr employment, '000 chg	17.9	30.0	20.0	Payrolls suggest weather & holiday dampened employment...
	Apr unemployment rate	4.0%	3.9%	3.9%	... and also dampened participation so falling unemployment.
US	Initial jobless claims	203k	-	-	To remain at a very low level.
	May Philly Fed index	17.6	16.1	-	Business conditions still healthy.
	Apr existing home sales	-2.7%	-1.8%	-	Limited supply and cooling demand headwinds to sales.
	Apr leading index	0.3%	0.0%	-	Pointing to a slowing of economic momentum.
<b>Fri 20</b>					
NZ	Apr trade balance \$mn	-392	-	-200	Dairy price strength running up against the oil price surge.
Eur	May consumer confidence	-22	-22	-	Inflation pressuring real spending capacity and sentiment.
UK	May GfK consumer sentiment	-38	-	-	At lowest level in series history back to 1980.
	Apr retail sales	-1.4%	-	-	Cost-of-living pressures to weigh on spending.

# International forecasts

Economic Forecasts (Calendar Years)	2018	2019	2020	2021f	2022f	2023f
<b>Australia</b>						
Real GDP %yr	2.8	2.0	-2.2	4.7	4.5	3.5
CPI inflation %yr	1.8	1.8	0.9	3.5	5.6	2.6
Unemployment rate %	5.0	5.2	6.8	4.7	3.2	3.4
Current account % of GDP	-2.1	0.7	2.6	3.5	1.9	-1.8
<b>United States</b>						
Real GDP %yr	3.0	2.2	-3.5	5.7	2.6	1.8
CPI inflation %yr	2.4	1.9	1.3	7.1	3.7	2.3
Unemployment rate %	3.9	3.7	8.1	5.4	3.7	4.1
Current account % of GDP	-2.3	-2.6	-2.5	-2.4	-2.4	-2.4
<b>Japan</b>						
Real GDP %yr	0.6	0.3	-4.8	1.8	2.2	1.4
<b>Euro zone</b>						
Real GDP %yr	1.9	1.3	-6.6	4.9	2.2	1.5
<b>United Kingdom</b>						
Real GDP %yr	1.3	1.4	-9.9	7.2	3.7	0.0
<b>China</b>						
Real GDP %yr	6.7	5.8	2.3	8.1	5.3	5.5
<b>East Asia ex China</b>						
Real GDP %yr	4.4	3.7	-2.4	4.2	4.5	4.7
<b>World</b>						
Real GDP %yr	3.6	2.8	-3.3	5.5	3.4	3.3

Forecasts finalised 6 May 2022

Interest rate forecasts	Latest	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23
<b>Australia</b>								
Cash	0.35	0.75	1.25	1.75	2.00	2.25	2.25	2.25
90 Day BBSW	0.98	0.95	1.45	1.95	2.20	2.45	2.45	2.45
10 Year Bond	3.36	3.30	3.15	2.90	2.65	2.50	2.40	2.30
<b>International</b>								
Fed Funds	0.875	1.375	2.125	2.625	2.625	2.625	2.625	2.625
US 10 Year Bond	2.85	2.90	2.80	2.60	2.40	2.30	2.20	2.10

Exchange rate forecasts	Latest	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23
AUD/USD	0.6873	0.72	0.74	0.76	0.77	0.78	0.79	0.80
USD/JPY	128.52	129	128	126	125	124	122	121
EUR/USD	1.0384	1.05	1.07	1.09	1.11	1.13	1.14	1.15
GBP/USD	1.2207	1.23	1.24	1.26	1.28	1.30	1.32	1.34
USD/CNY	6.7861	6.65	6.50	6.35	6.25	6.20	6.15	6.15
AUD/NZD	1.1001	1.11	1.10	1.10	1.10	1.10	1.10	1.11

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