WESTPAC WEEKLY ECONOMIC COMMENTARY

Housing market turn up as migrant numbers surge.

18 September 2023


Southern rātā

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Last week saw the release of data casting light on various aspects of the economy. In addition, ahead of the forthcoming General Election on 14 October, the Treasury released the Pre-Election Economic and Fiscal Update (PREFU), which provided an up-to-date account of the outlook for the government's finances.

Turning first to the data, the most striking news concerned migrant arrivals and the housing market. The provisional estimate of the net inflow of migrants in July was slightly less than we had expected, However, this surprise was more than offset by an upward revision to the estimate of inflows in earlier months. Indeed, given those revisions, the inflow in the year to July now stands at over 96,000, surpassing the previous historical high seen in the lead-up to the pandemic. We expect that the annual inflow will rise further in the next few months, before likely peaking around October. If so, in percentage terms, New Zealand will achieve its strongest annual population growth since the mid-1960s (about 2.5%).

Looking ahead, it is uncertain how long inflows will remain at such high levels and how any given inflow will impact the demand and supply balance in the economy. Migrant inflows appear to be helping to alleviate previously acute skill shortages across the labour market, and so taking some pressure off wages. But the new arrivals also appear to be boosting activity in the housing market – either directly, through migrant purchases, or indirectly, by lifting the confidence of potential resident buyers. Indeed, data released this week pointed to a 5% lift in nationwide house sales in August. And while remaining at relatively low levels in historical terms, sales now stand 9% above the same time last year. Perhaps more importantly, increased activity is translating into higher sales prices. The REINZ house price index increased 0.8% in August, reducing the annual decline to 4.7%. We're forecasting that house prices will rise by close to 8% next year. Last week's figures raise our confidence in forecasting that acceleration.

The news from the retail sector was a little more upbeat in August. Based on electronic transactions data, the total value of retail spending lifted 0.7% during the month. While this in part reflected a sharp price-driven lift in spending on fuel, core retail spending increased a respectable 0.6%, marking the best outcome since April. That said, this appears to be due to activity associated with the FIFA Women's World Cup, so it remains to be seen whether any payback is seen in September. Indeed, spending on durables fell for a second consecutive month in August and spending on consumables also edged lower. While the lift in tourism inflows is assisting retailers, it is worth noting that outbound travel by New Zealanders has increased sharply. As a result, in net terms, tourist flows are probably boosting demand by less than was the case pre Covid-19.

Conditions also remain difficult in the manufacturing sector. The BNZ-Business NZ PMI declined 0.5pts to 46.1 in August. The index has now been in contractionary territory for six consecutive months with the latest reading the lowest since the GFC once the pandemic period is excluded. In the detail, the production, new orders and employment indexes all remained at contractionary levels and well below average historical levels.

Last week's pricing news concerned developments in food and rents, which collectively account for around 30% of the CPI basket. A 0.5% lift in food prices in August was in line with our expectation, allowing annual inflation to ease slightly to 8.9% from 9.6% previously. Average housing rents increased by 0.4% in August, leaving annual rental inflation steady at 4.1%. Given these developments, we continue to look for the CPI to rise by about 2.0% in the September quarter, with seasonal increases in local authority rates and sharply higher petrol prices contributing to this chunky outcome. However, at this stage our estimate remains slightly below the 2.1% increase projected by the RBNZ in the August *Monetary Policy Statement*.

Turning to the PREFU, as was widely expected, the government's fiscal position has deteriorated. The forecast cumulative operating deficit over the period to 2026/27 is now $12.7bn larger than forecast in Budget 2023. Moreover, the projected return to surplus was delayed by a further year to 2026/27. Given the weaker outlook, the Treasury announced a $9bn increase in the bond issuance programme, with a rundown in financial assets also helping to plug this year's increased shortfall.

As we wrote in our review, we view the risks around the PREFU projections as skewed towards even greater deficits. On the revenue side, the Treasury's forecasts of nominal GDP – completed in early August – may be too high given the recent decline in key commodity prices. Meanwhile, the projections assume an unprecedented period of spending austerity. Indeed, the Treasury noted that while the assumed path of spending is expected to be adequate to cover critical cost pressures, it leaves reduced scope for the funding of new initiatives. So the winner of the General Election will face some challenges over the next parliamentary term. Looser policy settings might risk reaction from the ratings agencies and would certainly increase the risk of further monetary policy tightening by the RBNZ.

Over the coming week most interest will probably centre on Thursday's June quarter GDP report. We expect that this will reveal a solid rebound in activity following two quarters of contraction (at least as currently measured). Even so, annual growth is very likely to have slowed to 1.5% from the 2.2% reported in the March quarter, implying a decline in output in per capita terms. The GDP report will be preceded by an update on the current account deficit. Markets will also pay attention to Wednesday's GDT dairy auction, with futures pointing to a further recovery in prices from the steep declines seen in August. Surveys of service sector activity and consumer confidence round out the calendar.

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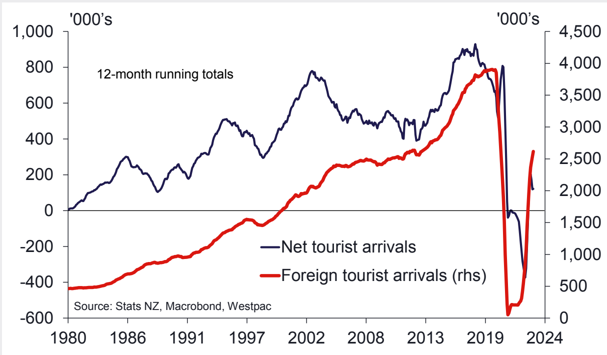
Chart of the week

Prior to the pandemic, the annual number of foreign visitor arrivals to New Zealand had grown to almost 4 million. Moreover, arrivals were as much as 900,000 greater than the number of short-term resident departures, thus providing a sizeable net boost to the local economy.

Since New Zealand reopened its international border, foreign visitor arrivals have rebounded to 2.6 million in the year to July – about two-thirds of pre-Covid levels (July month arrivals were 83% of July 2019 levels). However, in relative terms, resident departures have staged an even stronger recovery, rising to 2.5 million – almost 80% of pre-Covid levels. As a result, the *net* inflow of tourists over the past 12 months stands at just 121k – still far below pre-Covid levels, and so at this stage making only a modest contribution to the economy.

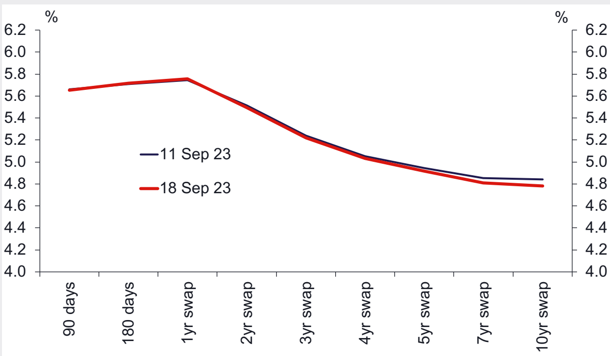
Net of resident departures, tourist arrivals remain low



Fixed vs floating for mortgages

We think the current best value for borrowers is fixing for one year and rolling for this term. That 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



The week ahead

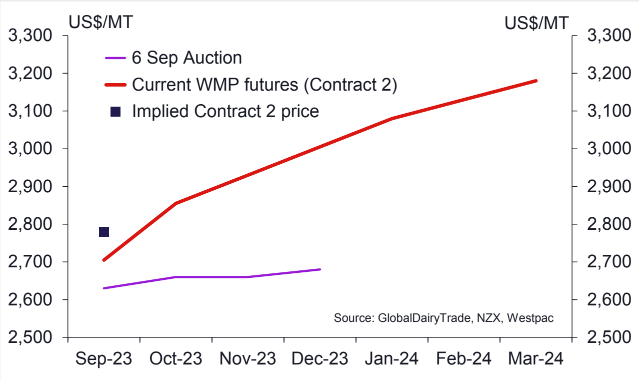
NZ GlobalDairyTrade auction, whole milk powder prices

Sep 20, Last: 5.3%, Westpac: 3.0%

We expect whole milk powder prices (WMP) to rise 3% at the upcoming auction. Note WMP prices jumped by around 5% at the previous auction. Our pick roughly splits the difference between the circa 1% rise at last week's mini (GDT pulse) auction and the circa 7% rise that the futures market is pointing to.

Prices appear to be finding a bottom after a sustained run of price falls. However, the spring peak in local production is around the corner and its strength or otherwise will provide fresh direction to prices. Heading into 2024, we anticipate that rebounding Chinese demand will lift prices, although there are downside risks as to the timing and magnitude of any price recovery.

Whole milk powder prices



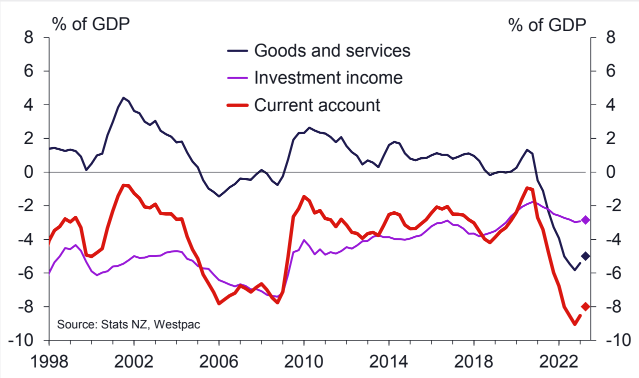
NZ Q2 current account balance, % of GDP

Sep 20, Last: –8.5%, Westpac f/c: –8.0%

The blow out in New Zealand's current account deficit over recent years has been a symptom of an overheated economy. In other words, we have been spending beyond our current means. Compounding the issue have been the loss of income from tourists (due to earlier border closure) and the sharp rise in import prices, including very high shipping costs.

That said, the current account deficit has turned the corner this year and is starting to narrow. Over the June quarter, we expect a deficit of 8.0% of GDP from 8.5% in the previous quarter. The services balance is improving as overseas tourists continue to return. Meanwhile, a bumper quarter for export volumes will also boost the annual goods balance.

Annual current account balance



NZ Q2 GDP

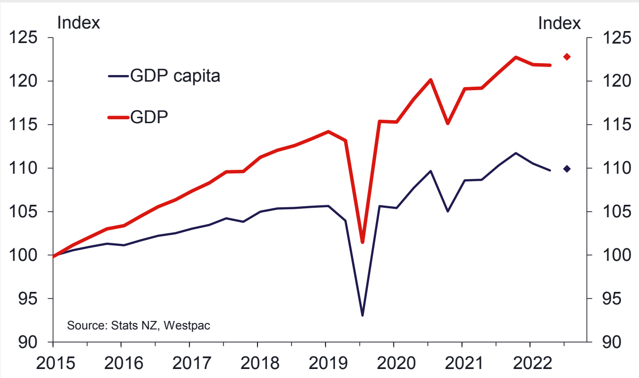
Sep 21, Last: –0.1%, Westpac f/c: 0.8%, Mkt f/c: 0.4%

We estimate that GDP rebounded 0.8% in the June quarter. This follows two quarters of decline, at least as presently estimated.

There continues to be a high degree of uncertainty around the quarterly result. Covid-19 has significantly disrupted the usual seasonal patterns and Statistics NZ will be reviewing its previous estimates this quarter. However, the underlying picture is that the economy is losing momentum, with annual growth expected to slow to 1.5% from 2.2% previously.

Our forecast is above that of both the market and the RBNZ. But given the uncertainties surrounding this data, we think that the RBNZ will be insensitive to small deviations from its forecast.

Real GDP level



The week ahead

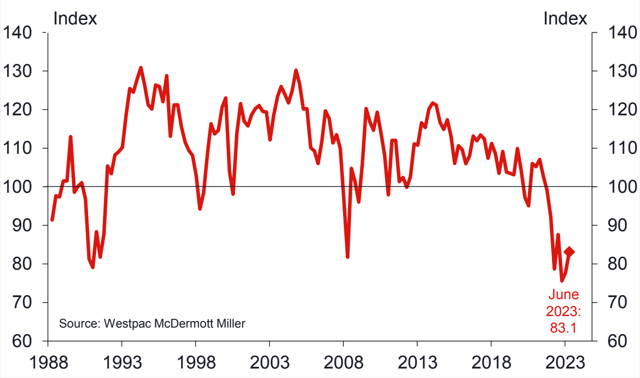
NZ Q3 Westpac McDermott Miller Consumer Confidence

Sep 23, Last: 83.1

Despite rising at the time of our June survey, consumer sentiment remained in the doldrums through the middle part of the year. The major contributor to that downbeat mood was the continued pressure on household finances, with large increases in living costs and mortgage rates.

Our upcoming survey was in the field during the early part of September. Recent months have seen continued rises in living costs and interest rates. However, we have also seen the housing market finding a base. The upcoming election will also be front of mind for many households.

Consumer Confidence



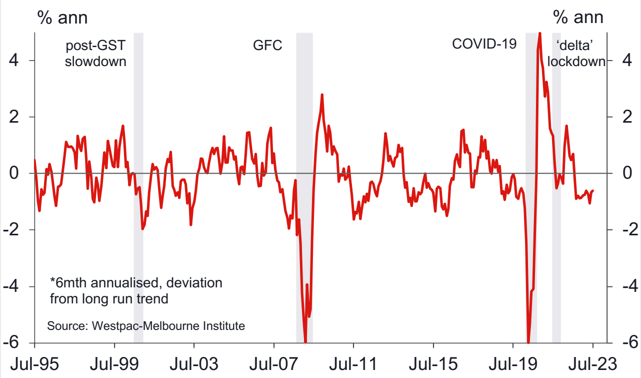
Aus Q3 ACCI-Westpac business survey

Sep 19, Last: 50.7

Conditions within Australia's manufacturing sector have been approaching a stalling speed over the last three quarters, notwithstanding a short-lived bounce at the beginning of 2023. The previous survey reported broadly flat new orders and employment, a decline in overtime and a slowing in output growth, consistent with slowing in the broader economy.

The June survey reported that manufacturers continued to face a broad set of challenges. Labour and material shortages, in particular, acting as a major drag on business activity. Additionally, input cost pressures remain intense and are flowing through (in part) to higher prices and squeezing margins. How long these pressures last, in the context of a trend downturn, remains a key question.

Aus Westpac – ACCI Composite indexes



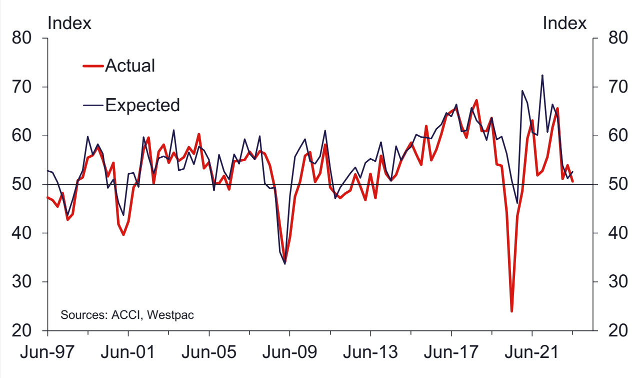
Aus Aug Westpac–MI Leading Index

Sep 20, Last: –0.60%

The Leading Index lifted slightly to lifted to –0.60% in July but remained firmly in negative territory, consistent with below-trend growth continuing through the second half of 2023 and into early 2024.

The August update looks likely to be another soft one with some notable declines in several components, including: a 14.6% drop in commodity prices (measured in AUD terms); dwelling approvals, down a further 8.1%; total hours worked down 0.5%mth; and a minor sell-off in the ASX (down 1.4%). Other components look to be largely unchanged although a stabilising yield spread – now that official interest rates are on hold – should provide some offsetting support.

Aus Westpac – MI Leading Index



The week ahead

US Sep FOMC meeting

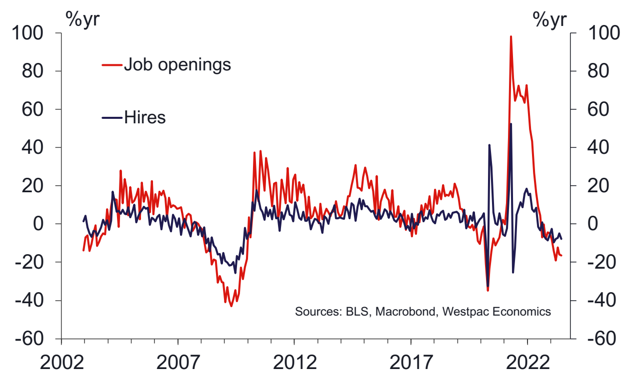
Sep 19-20: Last: 5.375%, Mkt f/c: 5.375%, WBC f/c: 5.375%

The US economy remains in very healthy condition. But labour market demand is coming into balance with supply, while inflation pressures and risks recede.

There is therefore little reason for the FOMC to tighten policy further at their September meeting. That said, they are unlikely to definitively signal an end to the tightening cycle or how far away rate cuts are likely to be. Key will be the revised forecasts, giving not only a view on the immediate future but also medium-term prospects and longer-run neutral.

We continue to expect the first 25bp rate cut in March 2024, to be followed by 25bps per quarter to the end of 2025. At that point, the fed funds rate will be 3.375%, still around 90bps above neutral as inflation holds modestly above target.

US job openings

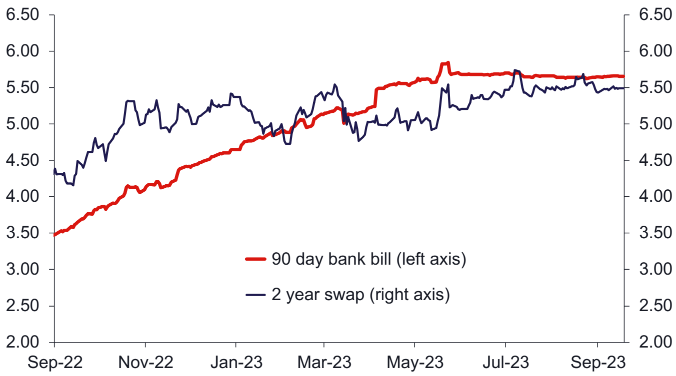


New Zealand forecasts

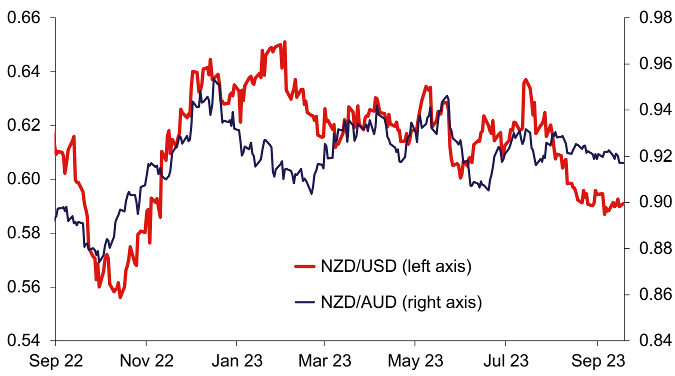
Economic forecasts	Quarterly				Annual			
	2022	2023						
% change	Dec	Mar	Jun	Sep	2021	2022	2023f	2024f
GDP (Production)	-0.7	-0.1	0.8	0.1	6.0	2.7	1.1	0.3
Employment	0.7	1.1	1.0	0.3	3.3	1.7	2.4	0.1
Unemployment Rate % s.a.	3.4	3.4	3.6	3.8	3.2	3.4	4.3	5.2
CPI	1.4	1.2	1.1	2.0	5.9	7.2	4.9	2.9
Current Account Balance % of GDP	-8.7	-8.2	-8.0	-8.2	-5.7	-8.7	-7.8	-6.0

Financial forecasts	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
Cash	5.50	5.75	5.75	5.75	5.50	5.25	5.00
90 Day bill	5.65	5.85	5.85	5.85	5.60	5.35	5.10
2 Year Swap	5.64	5.49	5.29	5.06	4.80	4.55	4.33
5 Year Swap	4.84	4.74	4.62	4.51	4.38	4.26	4.15
10 Year Bond	4.95	4.85	4.65	4.45	4.25	4.10	3.95
NZD/USD	0.59	0.61	0.61	0.62	0.62	0.62	0.63
NZD/AUD	0.92	0.92	0.92	0.91	0.90	0.89	0.88
NZD/JPY	85.6	87.8	87.2	86.4	85.6	84.9	83.4
NZD/EUR	0.55	0.55	0.55	0.55	0.55	0.55	0.55
NZD/GBP	0.46	0.48	0.48	0.48	0.48	0.48	0.48
TWI	69.1	70.3	69.9	69.4	68.9	68.6	68.2

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 18 September 2023

Interest rates	Current	Two weeks ago	One month ago
Cash	5.50%	5.50%	5.50%
30 Days	5.60%	5.60%	5.61%
60 Days	5.63%	5.62%	5.63%
90 Days	5.66%	5.64%	5.64%
2 Year Swap	5.50%	5.58%	5.52%
5 Year Swap	4.92%	4.99%	4.91%

NZ foreign currency mid-rates as at 18 September 2023

Exchange rates	Current	Two weeks ago	One month ago
NZD/USD	0.5910	0.5902	0.5986
NZD/EUR	0.5539	0.5459	0.5469
NZD/GBP	0.4770	0.4690	0.4713
NZD/JPY	87.34	86.49	86.80
NZD/AUD	0.9171	0.9209	0.9211
TWI	69.64	69.56	70.04

Data calendar

		Last	Market median	Westpac forecast	Risk/Comment
Mon 18					
NZ	Aug BusinessNZ PSI	47.8	–	–	Possible bounce from July's poor reading.
UK	Sep Rightmove house prices	–1.9%	–	–	Modest declines to persist as rates rise.
US	Sep NAHB housing market index	50	50	–	Floor emerging as supply dwindles
Tue 19					
Aus	RBA Minutes	–	–	–	Decision less “finely balanced” as case for pause strengthens.
	Q3 ACCI–Westpac business survey	50.7	–	–	Conditions in manufacturing are approaching a stalling speed.
Eur	Aug CPI %yr	5.3%	5.3%	–	Final estimate; detail on drivers of core inflation of note.
US	Aug housing starts	3.9%	–0.8%	–	Rising borrowing costs and insurance premiums are...
	Aug building permits	0.1%	0.3%	–	... disincentivising new projects but backlog persists.
Wed 20					
Aust	Aug Westpac–MI Leading Index	–0.60%	–	–	Pointing to below–trend growth carrying into 2024.
NZ	GlobalDairyTrade auction (WMP)	5.3%	–	3.0%	Global dairy prices finding a bottom after sustained weak run.
	Q2 current account % of GDP	–8.5%	–	–8.0%	Turning the corner after earlier blow-out.
UK	Aug CPI %yr	6.8%	–	–	Services keep pressure on, but goods pricing starting to ease.
US	FOMC policy decision, midpoint	5.375%	5.375%	5.375%	To remain on hold as inflation ticks lower.
Thu 21					
Aus	RBA September Bulletin	–	–	–	Quarterly publication including RBA research articles.
NZ	Q2 GDP	–0.1%	0.4%	0.8%	GDP is likely to have broken a two quarter losing streak.
Eur	Sep consumer confidence	–16	–15	–	Consumers remain downbeat as cost of living remains high.
UK	BoE policy decision	5.25%	5.50%	5.50%	Strong wages print to prompt further action.
US	Initial jobless claims	220k	–	–	Will remain at low levels, for now.
	Sep Phily Fed index	12.0	–0.4	–	Manufacturing to gradually find its legs.
	Aug existing home sales	–2.2%	0.7%	–	Low inventory weighing on sales.
	Aug leading index	–0.4%	–0.4%	–	Activity to slow ahead but not halt.
Fri 22					
NZ	Aug trade balance $mn	–1107	–	–2300	Improving on an underlying basis as import demand cools.
	Q3 WBC–MM Consumer Confidence	83.1	–	–	Has lingered at low levels for the past year.
Jpn	Aug CPI %yr	3.3%	3.0%	–	Down-tick led by ongoing fall in energy prices.
	BoJ policy decision	–0.10%	–	–	Little to change in the absence of demand-driven inflation.
	Sep Nikkei manufacturing PMI	49.6	–	–	Japanese manufacturers to benefit from Asian demand.
	Sep Nikkei services PMI	54.3	–	–	Tourism driving much of services optimism.
Eur	Sep HCOB manufacturing PMI	43.5	43.7	–	Manufacturing sentiment flailing...
	Sep HCOB services PMI	47.9	47.5	–	... consumer demand also under pressure.
UK	Sep S&P Global manufacturing PMI	43.0	–	–	Muted demand will drag on manufacturing outlook...
	Sep S&P Global services PMI	49.5	–	–	... services faces a similar fate, given the emerging fragility...
	Sep GfK consumer sentiment	–25	–	–	... in consumer sentiment as a consequence of higher costs.
	Aug retail sales	–1.2%	–	–	Weaker sales to persist as consumer cut back on treats.
US	Sep S&P Global manufacturing PMI	47.9	–	–	Outlook remains cloudy for manufacturers.
	Sep S&P Global services PMI	50.5	–	–	Flow through of rates will see services demand dampen.

International forecasts

Economic Forecasts (Calendar Years)	2019	2020	2021	2022	2023f	2024f
Australia						
Real GDP %yr	1.9	-1.8	5.2	3.7	1.6	1.0
CPI inflation %yr	1.8	0.9	3.5	7.8	3.9	3.2
Unemployment rate %	5.2	6.8	4.7	3.5	3.8	4.7
Current account % of GDP	0.7	2.4	3.1	1.2	1.0	0.3
United States						
Real GDP %yr	2.3	-2.8	5.9	2.1	1.8	0.4
CPI inflation %yr	1.9	1.2	7.2	6.4	2.5	2.0
Unemployment rate %	3.7	8.1	5.4	3.6	3.6	4.5
Current account % of GDP	-2.6	-2.5	-2.4	-2.4	-2.4	-2.4
Japan						
Real GDP %yr	-0.4	-4.3	2.1	1.1	1.4	1.0
Euro zone						
Real GDP %yr	1.6	-6.1	5.4	3.5	0.6	1.2
United Kingdom						
Real GDP %yr	1.6	-11.0	7.6	4.0	0.3	0.5
China						
Real GDP %yr	6.0	2.2	8.4	3.0	5.2	5.5
East Asia ex China						
Real GDP %yr	3.8	-2.3	4.3	4.5	3.7	4.3
World						
Real GDP %yr	2.8	-2.8	6.3	3.4	3.0	3.0

Forecasts finalised 7 August 2023

Interest rate forecasts	Latest	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24
Australia							
Cash	4.10	4.10	4.10	4.10	3.85	3.60	3.35
90 Day BBSW	4.13	4.30	4.30	4.22	3.97	3.72	3.47
10 Year Bond	4.09	4.00	3.80	3.60	3.40	3.30	3.22
International							
Fed Funds	5.375	5.375	5.125	4.875	4.625	4.375	4.125
US 10 Year Bond	4.27	4.10	3.90	3.70	3.50	3.40	3.30

Exchange rate forecasts	Latest	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24
AUD/USD	0.6462	0.66	0.67	0.68	0.69	0.70	0.71
USD/JPY	147.41	144	142	140	138	136	133
EUR/USD	1.0645	1.10	1.11	1.12	1.13	1.14	1.15
GBP/USD	1.2421	1.27	1.28	1.29	1.30	1.30	1.30
USD/CNY	7.2565	7.15	7.00	6.90	6.80	6.70	6.60
AUD/NZD	1.0902	1.08	1.10	1.10	1.11	1.13	1.13

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