ANZ Research

New Zealand Weekly Data Wrap

26 August 2022

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Contact us

See page 5.

Forecast updates

Recent ANZ NZ Forecast Updates can be found here.

- NZ Property Focus: no place for green shoots
- NZ Quarterly Economic Outlook: on the edge
- NZ Forecast Update: farmgate milk price forecasts revised down

Our other recent publications are on page 2.

What's the view?

- GDP constrained by supply more than demand
- Labour market extremely tight, and very inflationary
- Inflation way above target, but likely peaked in Q2
- Aggressive OCR hikes towards 4.0% in November 2022 needed to contain inflation

Our forecasts are on page 4.

Confused by acronyms or jargon? See a glossary here.

Key risks to our view

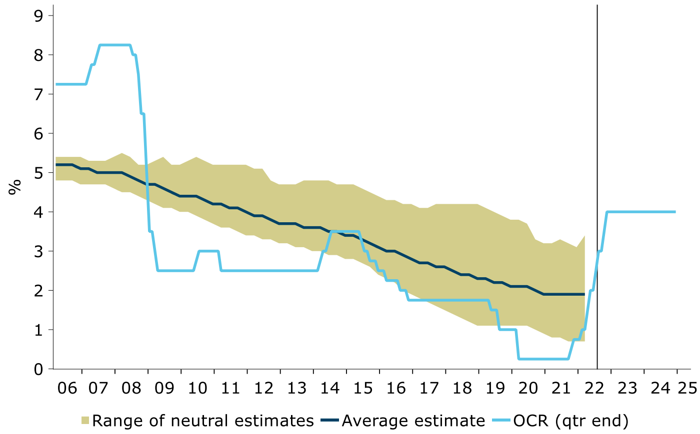
- Low consumer and business sentiment derail momentum.
- Falling house prices could have a more significant impact on the economy than expected.
- Neutral OCR is higher than the RBNZ's 2% estimate, necessitating more hikes than otherwise.
- Global inflation pressures don't decline as quickly as anticipated.

A small tweak to the end of our OCR forecast

For some time, we've had interest rate cuts pencilled into our OCR forecast for the second half of 2024, with the OCR easing from a peak of 4% down to 3.5% by the end of our current forecast horizon (Q4 2024). That's been a reflection of the fact that at some point in the next few years, the OCR hikes the RBNZ has delivered should be effective at bringing inflation back to target, allowing them to then cut interest rates back to a more neutral level (ie a level that is neither expansionary nor contractionary for the economy).

While obviously what 2024 looks like is subject to extreme uncertainty, we've now taken those cuts out of our forecast, to make it consistent with our current thinking. We continue to expect the RBNZ to lift the OCR to a peak of 4% by year-end (figure 1), though we see the risk profile tilted to more. But we no longer expect the RBNZ will be cutting the OCR over the duration of our forecast horizon (barring some miraculous recovery in the supply-side of the economy, or some unforecastable shock hitting the economy).

Figure 1. ANZ OCR forecast and RBNZ neutral OCR suite



Source: RBNZ, Macrobond, ANZ Research

The motivation behind this forecast tweak is simple – upon further reflection, we're increasingly seeing signs that high inflation is becoming embedded in wage- and price-setting behaviours in the economy. In Q2, private sector wages were up 7.0% y/y; the share of jobs receiving a larger than 5% pay rise hit its highest level since 2008; core inflation measures ranged from 4.8% to 6.1%; non-tradables inflation rose to 6.3%; and inflation expectations remained far too high. And that's not to mention the endless stream of news articles highlighting the much larger wage increases many workers are getting, the difficulty finding those workers, and employees sometimes explicitly demanding inflation compensation in their wages. In the August MPS, the RBNZ noted that in their business liaison programme some firms said wage reviews were happening more frequently as well.

Wage-setting is, in a nutshell, adjusting to a higher-inflation world. While that's undoubtedly a relief for squeezed household budgets, it's a headache for the RBNZ. If high inflation expectations are feeding higher wage-setting behaviour, that means a given interest rate is, in practice, less of a constraint on households than previously thought. In the economics jargon, it means the neutral OCR is likely creeping higher. The RBNZ's latest official estimate is that the neutral OCR is 2%, but they're currently updating their models. In post-August MPS interviews, some members of the Monetary Policy Committee have given a range of 2-3% for their estimate of where neutral is.

Looking ahead

Recent Publications

ANZ produces a range of in-depth insights.

- NZ Agri Focus: it's raining, it's pouring
- NZ Insight: the Australian labour market and the RBNZ
- NZ Property Focus: hardening headwinds and soft landings
- NZ Insight: the low consumer confidence puzzle
- NZ Property Focus: when, not if
- NZ Insight: He Waka Eke Noa recommendations
- Agri Insight: global food crisis to worsen
- NZ Property Focus: better fundamentals mean softer prices
- NZ Budget Review: Big Budget
- NZ Insight: Emissions Reduction Plan
- NZ Insight: new fiscal rules
- NZ Property Focus: regional rollercoaster
- NZ Insight: how widespread is labour market tightness?
- NZ Agri Focus: mixed blessings
- NZ Insight: the RBNZ's inflation expectations headache
- NZ Insight: how is NZ's agri sector impacted by the Russian invasion
- NZ Insight: The Reopening II – shifting economic sands
- NZ Insight: Endemic COVID-19 and labour supply
- NZ Insight: The real cost of inflation

Click here for more.

ANZ Proprietary data

Check out our latest releases below.

- ANZ Business Outlook
- ANZ-Roy Morgan Consumer Confidence
- ANZ Truckometer
- ANZ Commodity Price Index

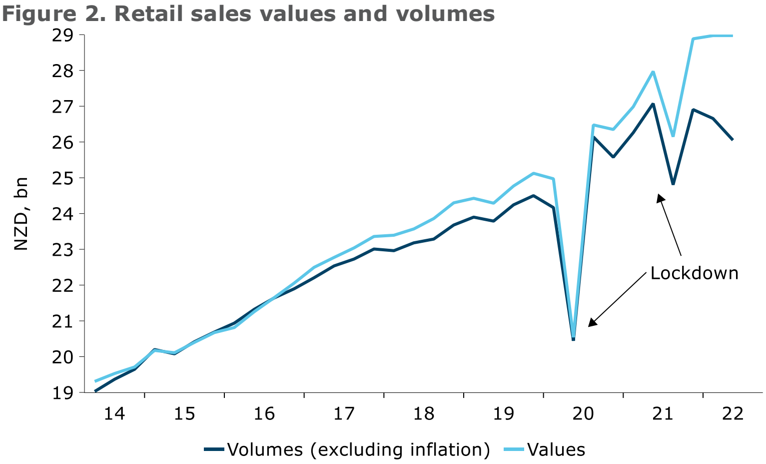
If the neutral rate has increased, it means an even higher OCR than 4% would be on the cards. For example, if the RBNZ lifted their neutral estimate from 2% to 3%, then a 5% OCR would be needed to deliver the same amount of monetary tightening. That sounds high, but remember that in the 2000s, the neutral OCR was estimated to be just over 5% (figure 1). The actual OCR got to 8.25% before the Global Financial Crisis came along.

To summarise, if neutral is slowly rising, then the OCR needed to deliver the *same* amount of monetary tightening is also increasing. At the very least, it looks like the OCR will need to be high for longer to ensure that CPI inflation returns to target within an acceptable timeframe. Hence, we've removed the 2024 OCR cuts from our forecast. Importantly, this has no implications for our other economic forecasts. Rather, we think the OCR will need to remain in contractionary territory for longer to deliver that same set of projections.

The natural question is why we haven't revised up our OCR forecast peak, given the risk that the neutral OCR has increased. We certainly see the risks tilted that way, despite slowing activity. We'll be watching wage growth closely, plus be on the lookout for any signs that the traction interest rates are getting might be slipping. But there are still other risk factors pointing in the opposite direction for interest rates. We are over a year beyond the 2021 trough in mortgage rates, which means many households will be rolling into much higher mortgage rates, both now and over the next few years (depending on how long they fixed for in 2021). That's a significant drag on discretionary spending. But the extent to which consumers will decide to reduce spending is unknown. Households have accumulated a lot of savings in the past few years, and wages are rising fast – effectively unwinding some of the increase in the debt-servicing burden. Our consumer confidence survey shows mortgage holders more circumspect on spending plans than others – but the difference is not particularly large as yet.

It remains uncertain how the economy will ultimately respond to this rapid tightening cycle from the RBNZ once the shock value wears off. Unfortunately, the activity data are still highly volatile. Yesterday's Q2 retail sales data showed volumes were down 2.3%, after a 0.9% fall in Q1. That raises the risk of a technical recession in New Zealand. If the fall was demand-driven, then all else equal it's a deflationary force. But with sales values still holding up (figure 2), it could simply reflect that inflation is eroding real purchasing power – which just points to the need for rate hikes. Inflation won't solve inflation! The picture is muddled, and the challenge for the RBNZ is to work out when they've done enough to bring inflation down. That threshold is a moving target, and the noisy data are obscuring the RBNZ's vision.

Figure 2. Retail sales values and volumes



Source: Stats NZ, Macrobond, ANZ Research

Financial markets update

Data calendar

What's coming up in the months ahead.

Date	Data/event
Wed 31 Aug (10:45am)	Building Permits – Jul
Wed 31 Aug (1:00pm)	ANZ Business Outlook – Aug
Wed 31 Aug (3:00pm)	RBNZ Sectoral Lending – Jul
Fri 2 Sep (10:45am)	Terms of Trade – Q2
Mon 5 Sep (10:45am)	Building Work Put in Place – Q2
Mon 5 Sep (1:00pm)	ANZ Commodity Price Index – Aug
Wed 7 Sep (early am)	GlobalDairyTrade auction
Thu 8 Sep (10:45am)	Economic Survey of Manufacturing – Q2
Fri 9 Sep (10:00am)	ANZ Truckometer – Aug
Fri 9 Sep (10:45am)	Electronic Card Transactions – Aug
Mon 12 Sep (10:45am)	Net Migration – Jul
Tue 13 Sep (10:45am)	Food Price Index – Aug
Tue 13 Sep (10:45am)	Rental Price Index – Aug
Wed 14 Sep (10:45am)	Balance of Payments – Q2
Thu 15 Sep (10:45am)	**GDP – Q2**
Fri 16 Sep (10:30am)	BusinessNZ Manuf PMI – Aug
Mon 19 Sep (10:30am)	Performance Services Index – Aug
Wed 21 Sep (early am)	GlobalDairyTrade auction
Thu 22 Sep (10:45am)	Merchandise Trade – Aug
Thu 29 Sep (1:00pm)	ANZ Business Outlook – Sep
Fri 30 Sep (10:00am)	ANZ-RM Consumer Confidence – Sep
Fri 30 Sep (3:00pm)	RBNZ Sectoral Lending – Aug
Tue 4 Oct (10:00am)	NZIER QSBO – Q3
Wed 5 Oct (early am)	GlobalDairyTrade auction
Wed 5 Oct (2:00pm)	**RBNZ Monetary Policy Review**
Thu 6 Oct (1:00pm)	ANZ Commodity Price Index – Sep
Tue 11 Oct (10:00am)	ANZ Truckometer – Sep

Interest rate markets

Local interest rates have risen sharply this week, with the short end under pressure as markets reassess the outlook for inflation and the OCR, and the long end under pressure as US bond yields reposition higher ahead of Fed chair Powell's keynote speech at the Kansas City Fed's symposium at Jackson Hole, Wyoming. For the short end, it all boils down to what the neutral rate is, and how sticky inflation proves to be, which we've discussed in detail on pages 1 and 2. In that regard, we have come around to the view that the question markets should be asking is; "Why doesn't the OCR need to go back to 8.25%?" rather than "Why does it need to go beyond 4%?" Okay, the 2007 high of 8.25% is clearly a stretch given house price levels and dynamics and how late we are in the cycle, but we think the onus is on the data to disprove the case for ongoing hikes, given real rates are still negative. Market pricing is at least now more aligned to what the RBNZ is signalling, and that's a plus. But it is still pricing in cuts beyond May next year, and that seems premature. Markets are always eager to jump on turns, so that expectation isn't likely to change any time soon, but historic experience suggests that markets will be disappointed as projections for the peak policy rate get revised up. US long-end rates are off earlier highs (the US 10yr Treasury bond yield got to 3.12% overnight), but the US market is now also reacting to the possibility policy rates there may remain higher for longer, likely peaking at 4% or thereabouts. That's not a great backdrop for US long bonds unless a recession is imminent, and the jury is still out on that, with consumers thus far fairly resilient thanks to tight labour markets.

FX markets

NZD weakness gave way to volatility this week as markets repositioned for Fed chair Powell's speech (2am Saturday NZT). The current narrative in FX markets seems to be that the USD will be the best of a bad bunch if global growth does slow, and additionally, that if the RBNZ was an early started with rate hikes, NZ could be at risk of entering a recession sooner. That logic is hard to refute, and we remain pretty neutral on the Kiwi here now that it's close to our 2yr-ahead estimate of fair value. NZD/AUD has broken lower. That not only fits with where we see macro relativities, but technical charts now look bleak, with "clear air" down to around 0.8750.

Key data summary

Retail Trade Survey – Q2. Sales volumes fell 2.3% q/q, after a downwardly revised 0.9% fall in Q1.

ANZ Roy Morgan Consumer Confidence – August. Confidence lifted a little in August, but remains at very subdued levels.

The week ahead

Building Permits – July (Wednesday 31 August, 10:45am). Consent issuance appears to have peaked – and our Business Outlook suggests sizeable declines are on the cards in coming months.

ANZ Business Outlook – August (Wednesday 31 August, 1:00pm).

RBNZ sectoral lending data – July (Wednesday 31 August, 3:00pm). Housing lending growth is slowing as the housing market cools, while consumer lending continues to fall well below pre-pandemic levels.

Overseas Trade Indices – Q2 (Friday 2 September, 10:45am). Import price increases are expected to outpace higher export prices due to the sharp rise in the price of energy related imports such as oil and fertiliser.

Key forecasts and rates

		Actual				Forecast (end month)			
FX rates	Jun-22	Jul-22	Today	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23
NZD/USD	0.621	0.628	0.622	0.630	0.630	0.640	0.650	0.650	0.650
NZD/AUD	0.904	0.900	0.892	0.887	0.875	0.865	0.867	0.867	0.867
NZD/EUR	0.597	0.614	0.624	0.618	0.600	0.598	0.591	0.580	0.575
NZD/JPY	84.7	83.7	84.9	84.4	83.2	83.2	83.2	82.6	81.9
NZD/GBP	0.513	0.516	0.526	0.521	0.512	0.516	0.516	0.512	0.508
NZ$ TWI	70.5	71.1	71.2	71.0	70.2	70.4	70.7	70.3	69.9
Interest rates	Jun-22	Jul-22	Today	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23
NZ OCR	2.00	2.50	3.00	3.00	4.00	4.00	4.00	4.00	4.00
NZ 90 day bill	2.86	3.14	3.44	3.93	4.10	4.10	4.10	4.10	4.10
NZ 2-yr swap	4.06	3.74	4.17	4.20	4.20	4.25	4.25	4.20	4.10
NZ 10-yr bond	3.86	3.42	3.86	4.10	4.10	4.00	4.00	3.75	3.75

Economic forecasts

	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
GDP (% qoq)	-0.2	**1.0**	**0.5**	**0.8**	**0.5**	**0.1**	**0.2**	**0.2**	**0.5**
GDP (% yoy)	1.2	**-0.1**	**4.4**	**2.2**	**2.8**	**1.9**	**1.6**	**1.0**	**1.0**
CPI (% qoq)	1.8	1.7	**1.6**	**0.9**	**0.7**	**0.6**	**0.8**	**0.4**	**0.4**
CPI (% yoy	6.9	7.3	**6.7**	**6.1**	**5.0**	**3.9**	**3.1**	**2.5**	**2.3**
Employment (% qoq)	0.0	0.0	**0.1**	**0.1**	**0.1**	**0.1**	**-0.3**	**-0.4**	**-0.4**
Employment (% yoy)	2.7	1.6	**-0.1**	**0.1**	**0.3**	**0.3**	**0.0**	**-0.5**	**-1.0**
Unemployment Rate (% sa)	3.2	3.3	**3.3**	**3.4**	**3.4**	**3.6**	**4.0**	**4.5**	**4.8**

Figures in bold are forecasts. mom: Month-on-Month; qoq: Quarter-on-Quarter; yoy: Year-on-Year

Figure 3. Production GDP

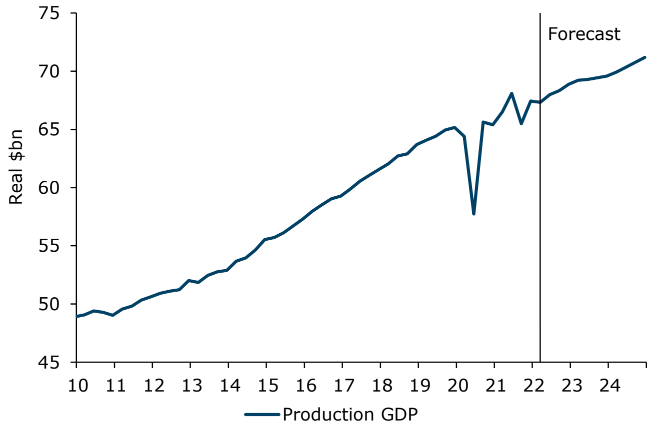


Figure 4. CPI inflation components

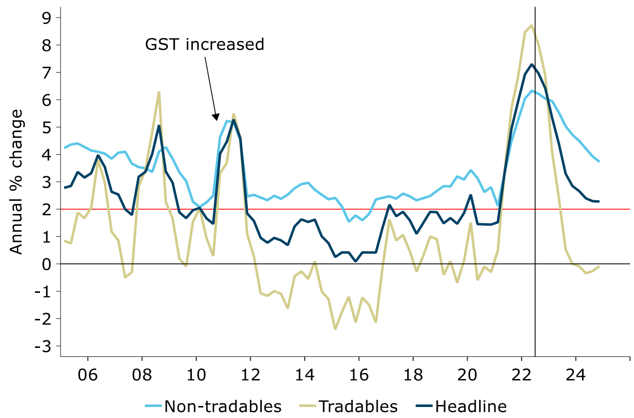


Figure 5. ANZ OCR forecast

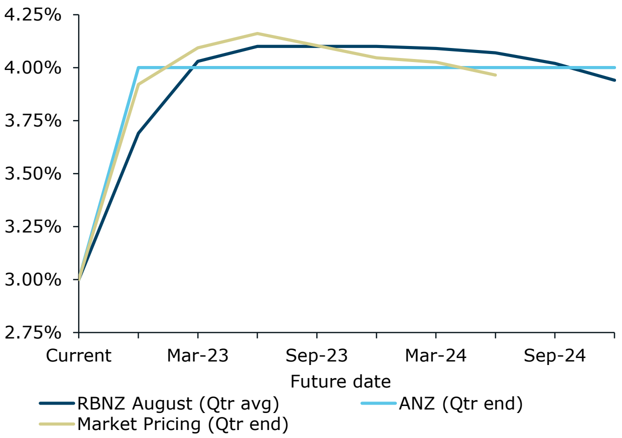
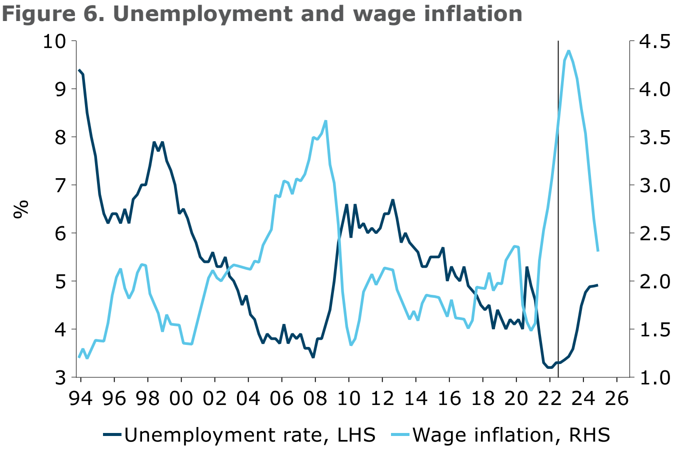


Figure 6. Unemployment and wage inflation



Source: Stats NZ, Bloomberg, RBNZ, Macrobond, ANZ Research

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