

August 2021

A view from the gilded cage

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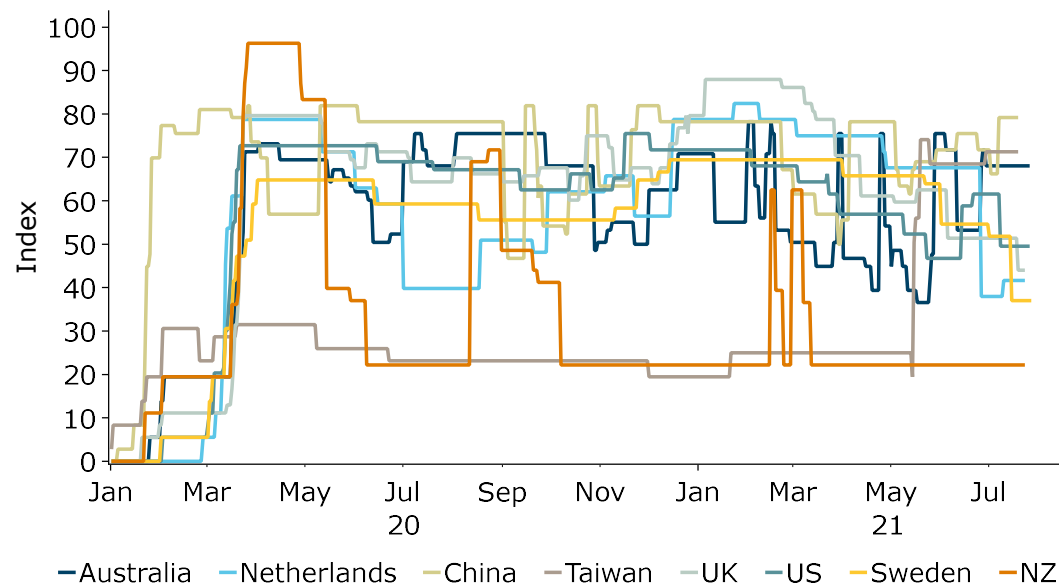
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Government Response Stringency Index



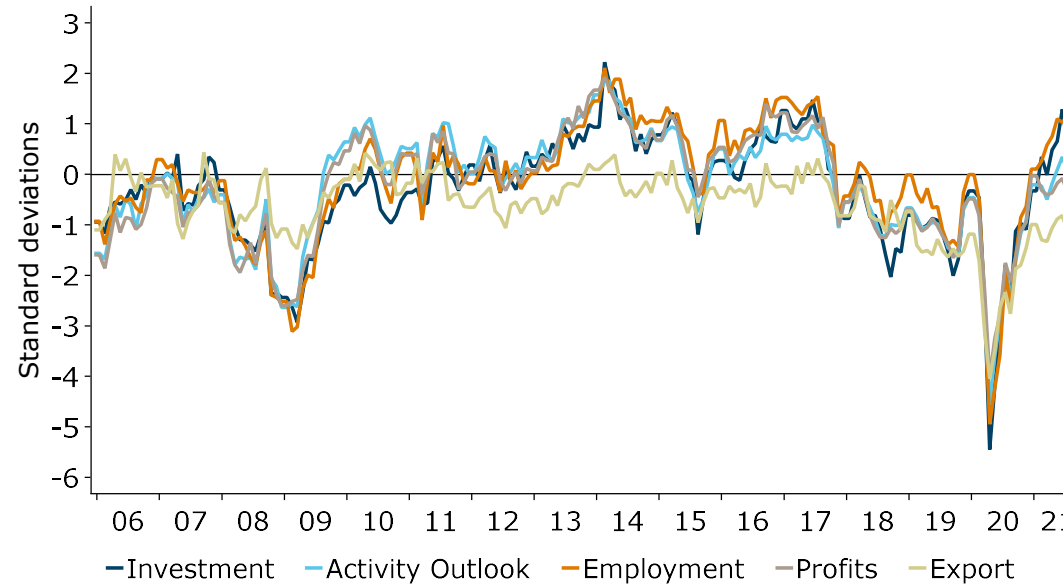
Source: University of Oxford, Bloomberg, Macrobond, ANZ Research

- NZ is facing much less economic and health scarring as a result of successfully eliminating COVID.
- Differences in quality of life will presumably narrow from here, though the Netherlands experiment didn't go well.
- NZ's exit plan is still a bit of a grey area and depends heavily on vaccination success.



Happy
days are
here again?

Business indicators higher than pre-COVID

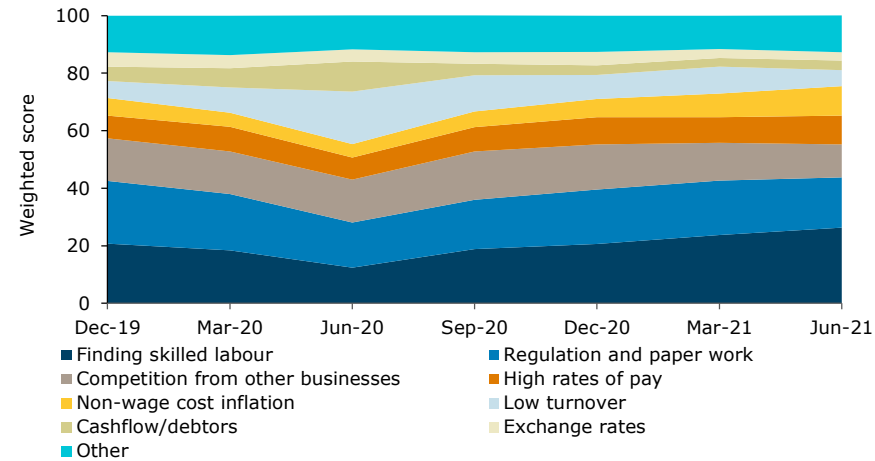


Source: ANZ, Macrobond

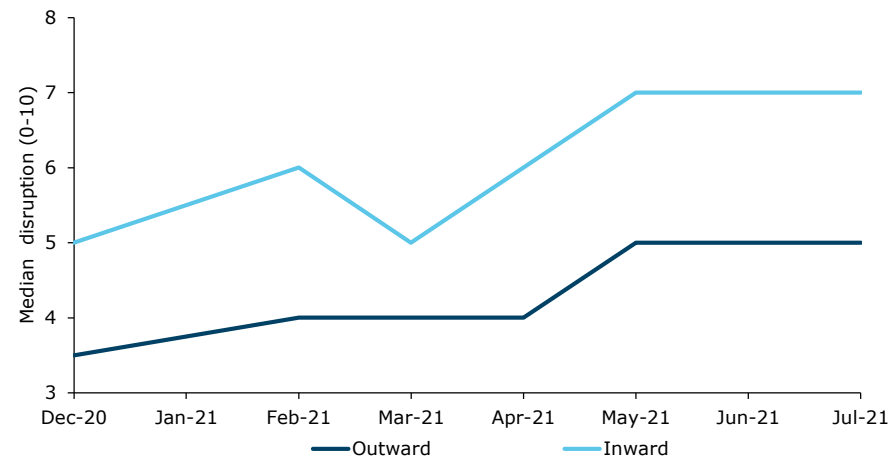
- Improvement in investment and employment intentions is particularly encouraging, though now looking a little peaky.
- Note we haven't had a "recession" in terms of a shake-out, and people reassessing their attitude towards risk.
- This is still the same business (and asset price) cycle, interrupted. That implies a shorter life-expectancy.

Growing pains

Firms' reported biggest problems



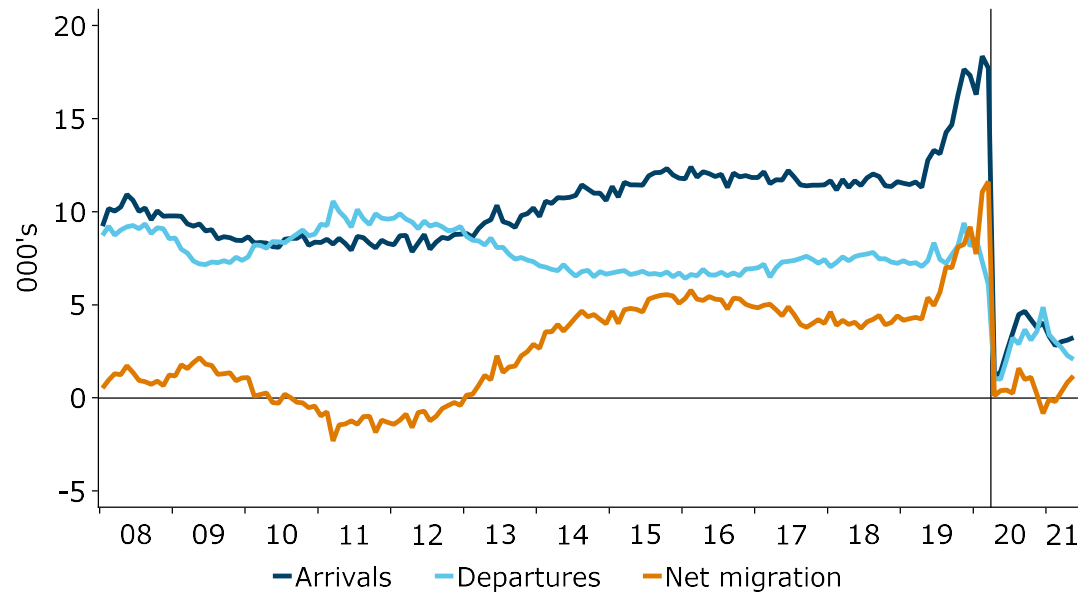
Firms' reported difficulties from freight disruptions



Source: ANZ Research

That was
that

Monthly net migration

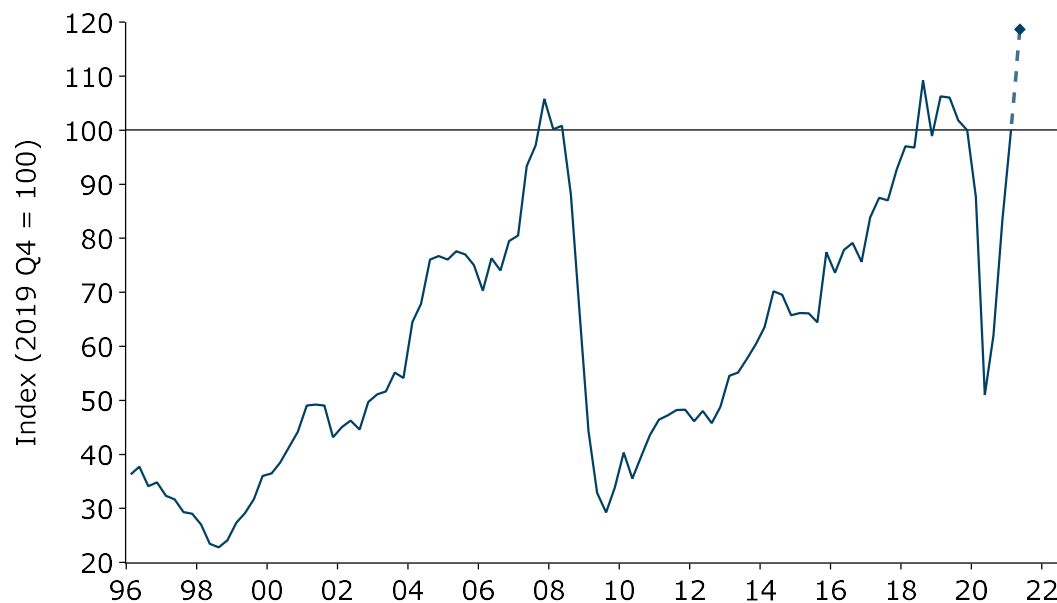


Source: Stats NZ, Macrobond, ANZ Research

- Net migration is a huge swing variable for the NZ economy.
- Population growth has provided more than half of economic growth in the past five years.
- 25% of newly returned kiwis plan to leave again.
- Australia is furiously trying to poach. Risk of recent migrants leaving again due to separated families, residency delays.

Tightest
labour
market in
decades

Job vacancy/unemployment ratio

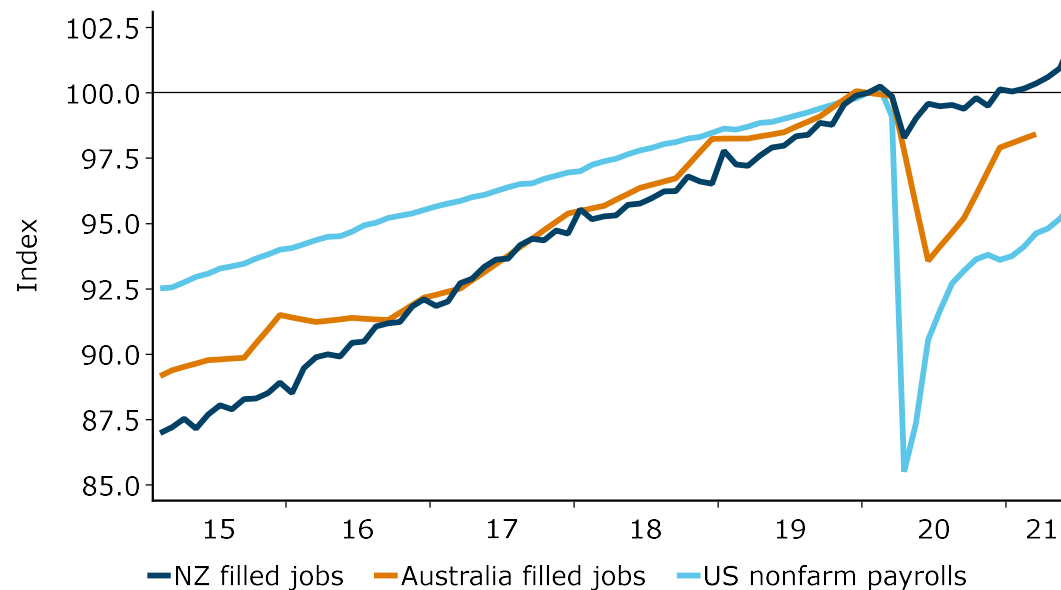


Source: Stats NZ, MBIE, Macrobond, ANZ Research

- The RBNZ believes there is still some spare capacity in the labour market. We can't see any spare capacity anywhere.
- We expect more wage inflation than the unemployment rate might ordinarily suggest. And we expect the unemployment rate to continue to fall.

More or less
fully healed

The labour market has recovered remarkably quickly

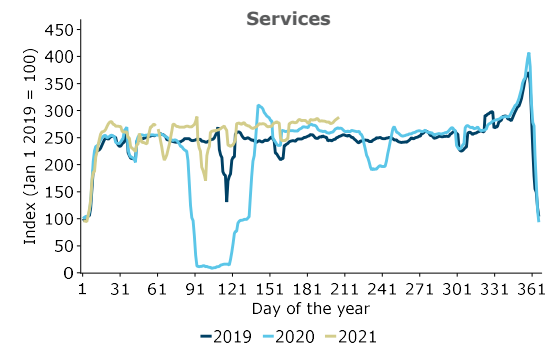
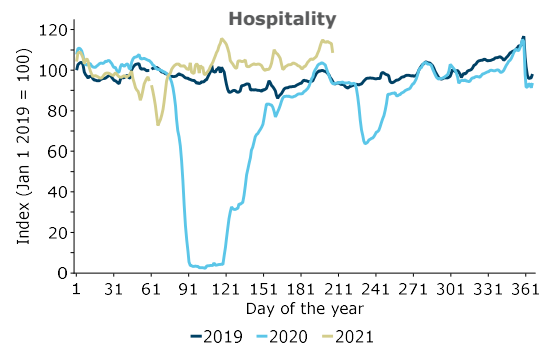
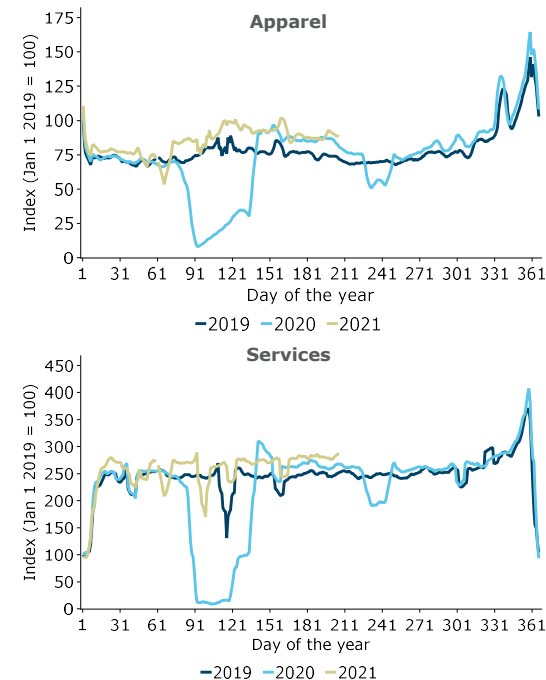
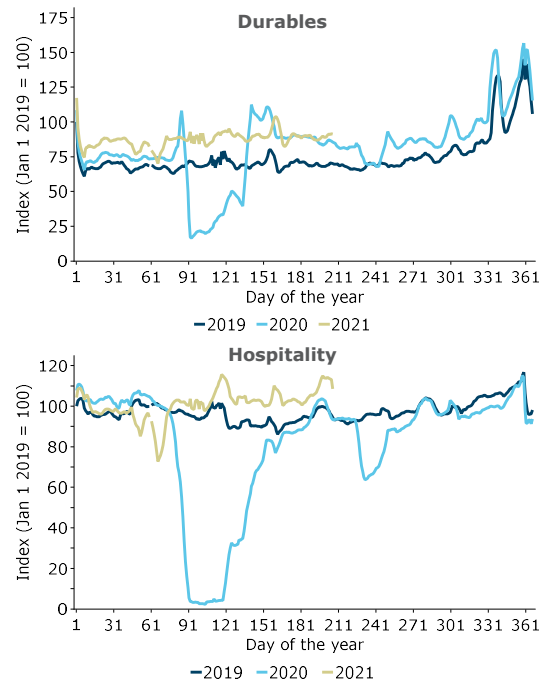


Source: BLS, Stats NZ, ABS, Bloomberg, Macrobond, ANZ Research

- A genuine good news story – have avoided long-run unemployment.
- But it was an expensive rescue!
- The RBNZ can tick the labour market box, unlike peers abroad.

What
income
shock?

Households are spending up a storm

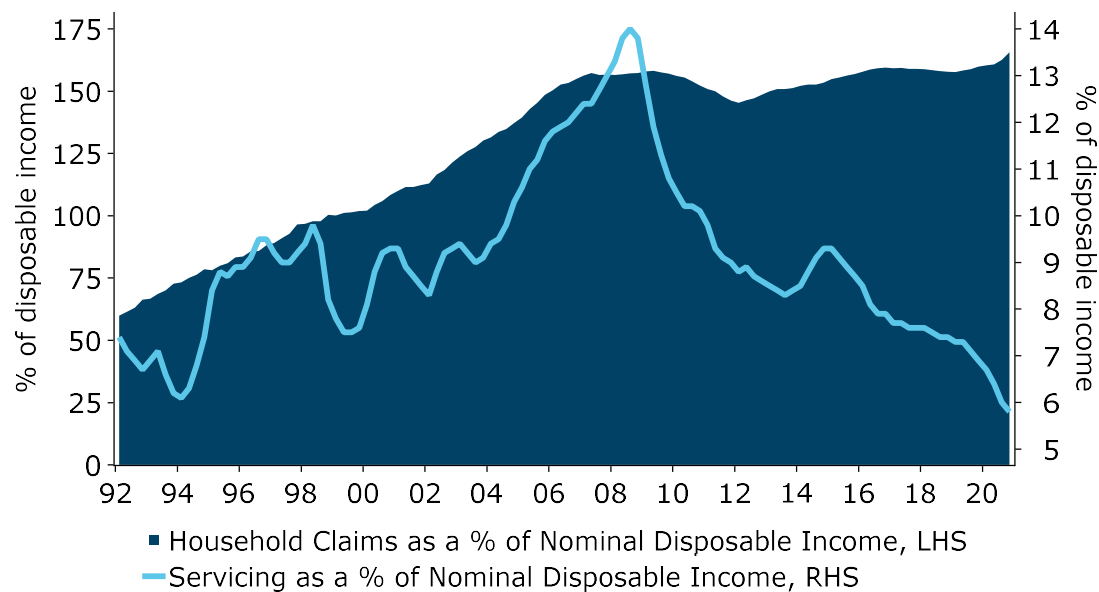


Source: Macrobond, ANZ Research

- Job security
- The housing boom
- Low interest rates, interest-free deals, BNPL
- Substitution from international holidays to stuff

Plenty of
cash to
spend –
for now

Household debt servicing ratios to income



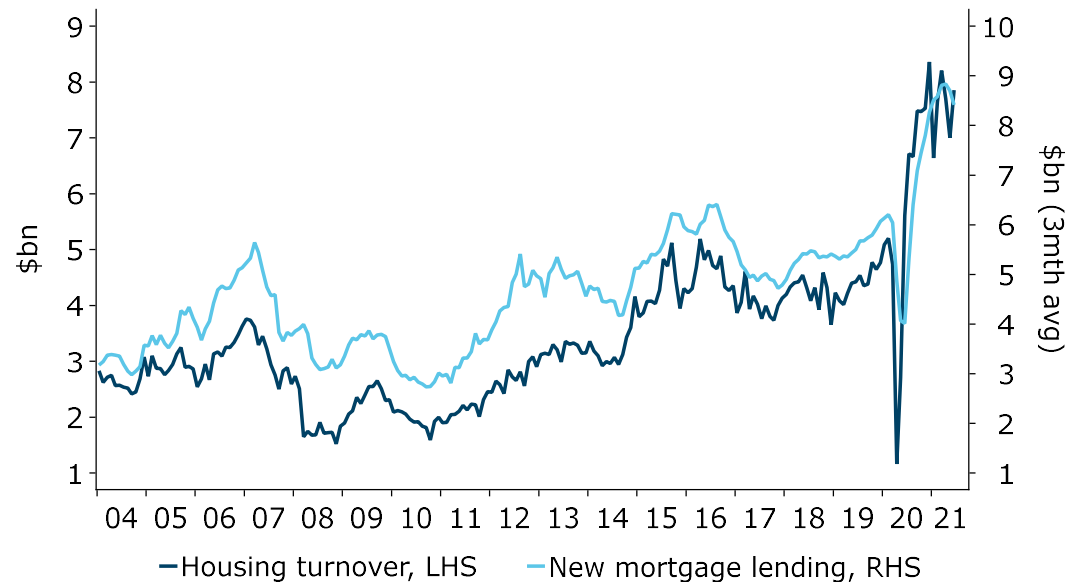
Source: RBNZ, Macrobond, ANZ Research

- Debt levels are still rising.
- Higher interest rates will hurt.
- But for now households in aggregate are feeling good.



Peaked

Housing turnover and new mortgage lending

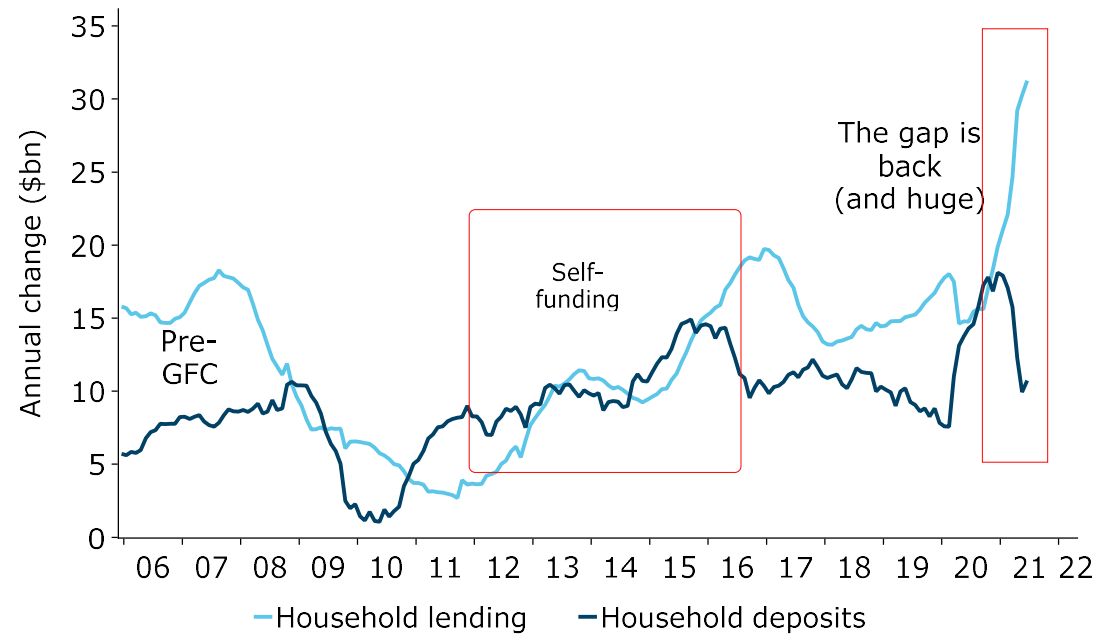


Source: RBNZ, REINZ, Macrobond, ANZ Research

- Housing turnover has peaked, but is certainly not crashing. Low stock is keeping the market tight.
- Investors are warier, but first home buyers are still experiencing fear of missing out. House price expectations are rising again.
- That'll change eventually but for now, prices keep surprising on the upside.

Financial
conditions
tightening

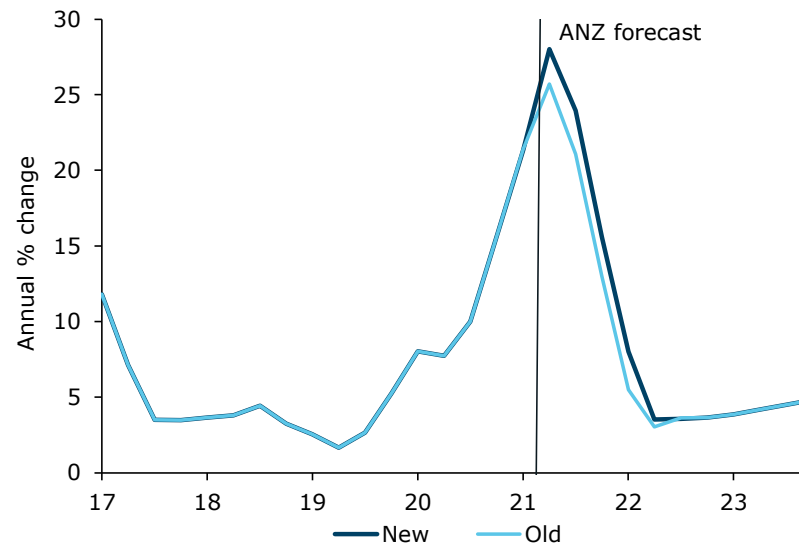
Bank funding gap



- The spike in deposit growth was QE/wage subsidy.
- But now mortgage lending growth is again putting pressure on funding positions. Term deposit rate are rising independent of RBNZ.
- A wave of fixing could now also pressure swap rates.

Tax policy
change a new
downside risk

House price inflation forecast



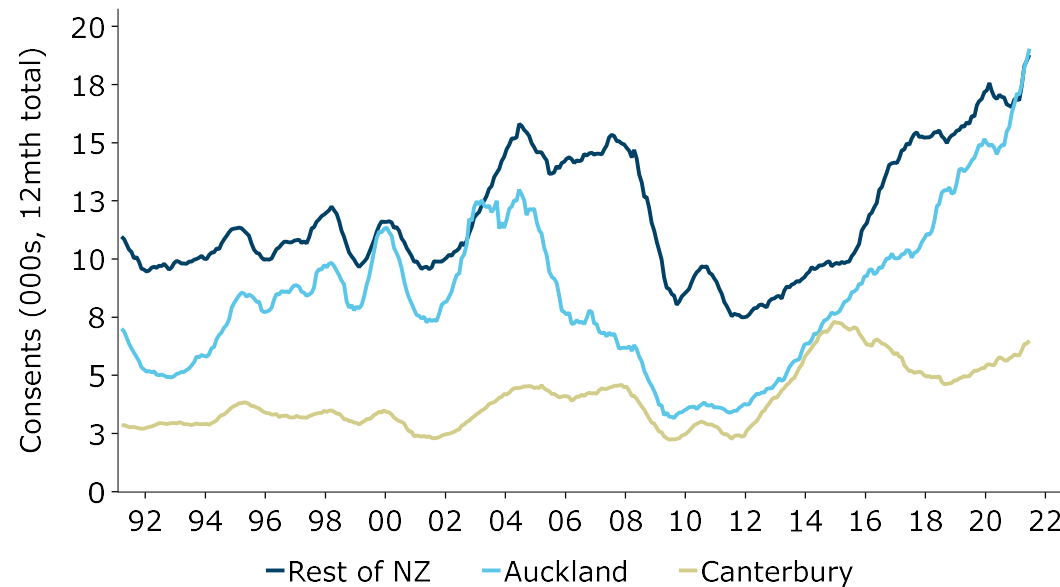
Source: REINZ, ANZ Research

- Much of the decline in annual house price inflation is baked in as previous surges drop out. But also stretched affordability, rising rates, LVRs, tax changes, boosted supply...
- Expecting a decent dent in house sales, but no fire-sale of investor properties (rates are low and there's a 4-year phase in for the tax change).
- The new tax policy will really bite when rates increase – it does increase the chance of house price falls.



Plenty of
building
planned

Dwelling consents

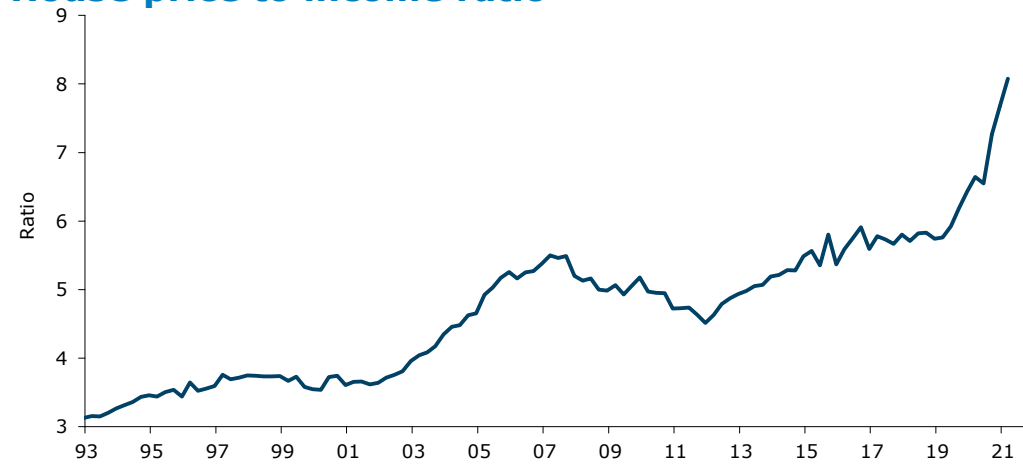


Source: Stats NZ, Macrobond, ANZ Research

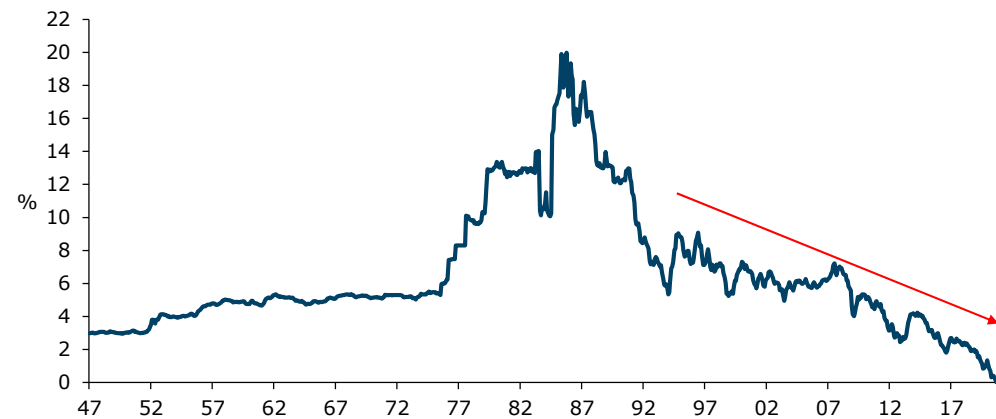
- Highest since 1974, driven by Auckland.
- Construction provides almost 10% of employment (vs 5% in the 1990s and 7.5% in 2007)
- Planning isn't doing: cost increases are extreme
- We're concerned about the impact of labour and materials shortages.

Multi-decade
tailwind has
run its
course

House price to income ratio



NZ 5-year bond yield



Source: REINZ, RBNZ, Statistics NZ, ANZ Research, Macrobond

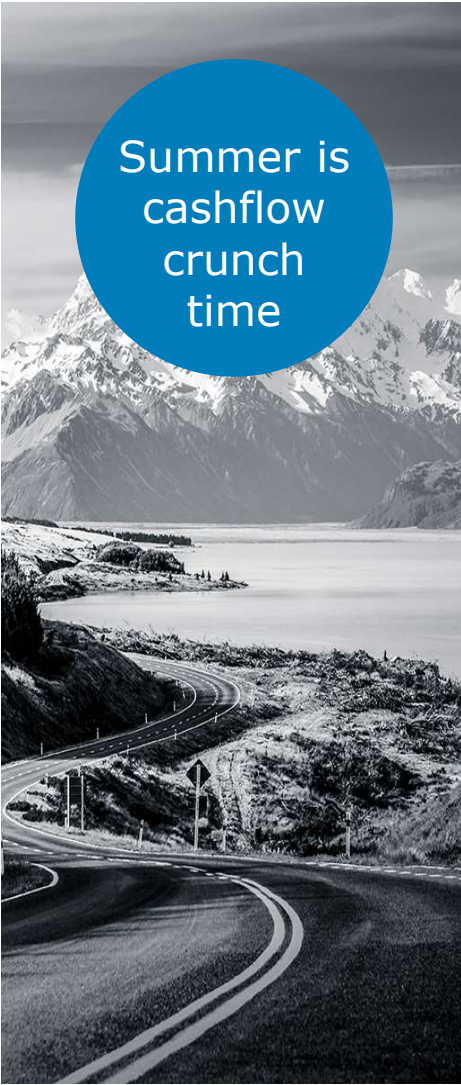
Mortgage
rates have
changed
direction

Swap rates



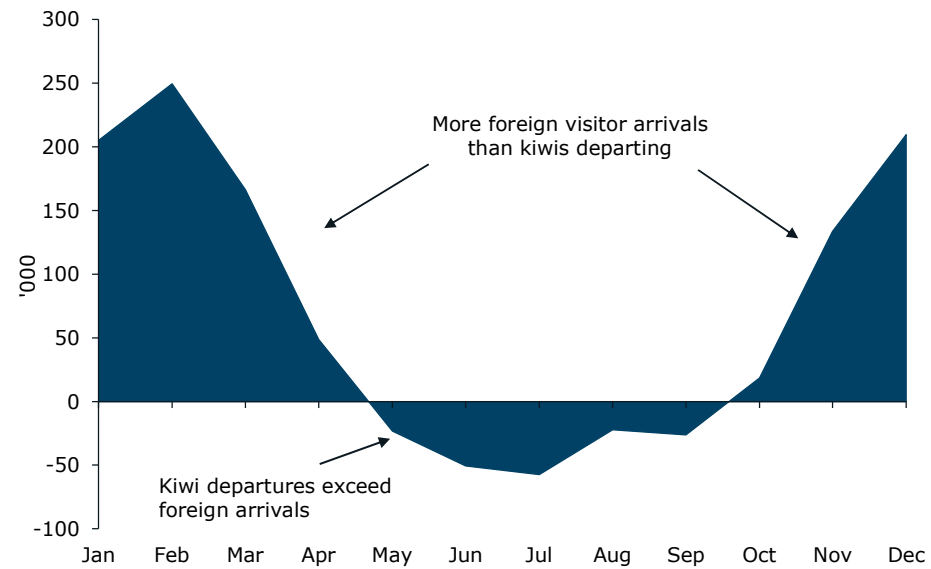
Source: Bloomberg, Macrobond, ANZ Research

- There's no longer room to hide at the short end.
- Mortgage rates are rising, with the RBNZ expected to hike at least twice this year.
- 80% of mortgage debt is either floating or has less than 12 months left on its fixed term.



Summer is
cashflow
crunch
time

Seasonality of tourism (average 2016-19)

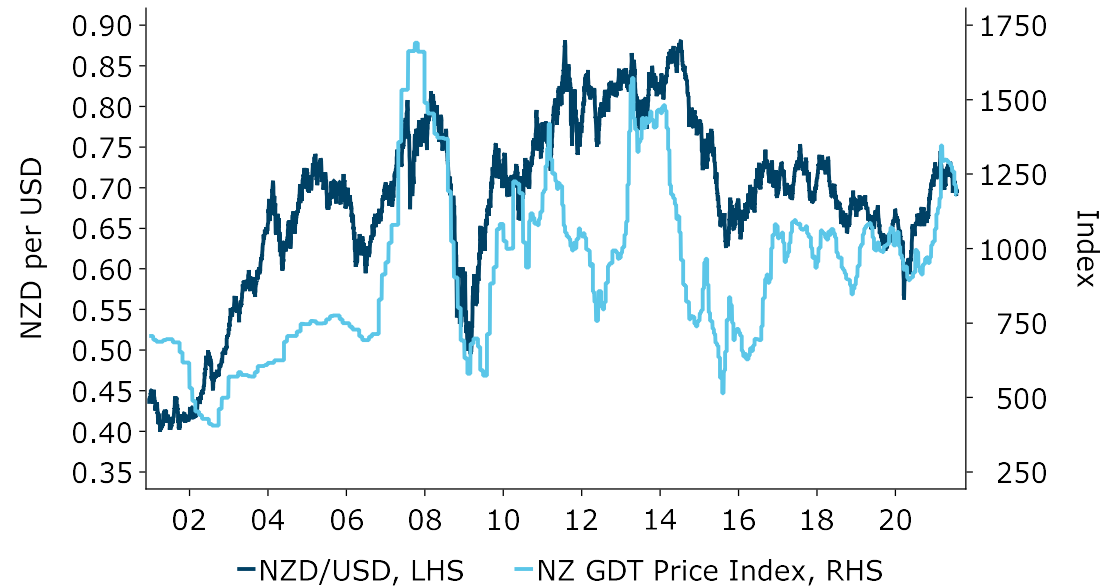


Source: Statistics NZ, ANZ Research

- The travel bubble seems unlikely to return. Limited economic upside, vast potential downside.
- Turns out the tourism industry was to a reasonable extent self-staffing.
- Really unclear what the long game is for the sector.

Riding the
global
commodity
wave

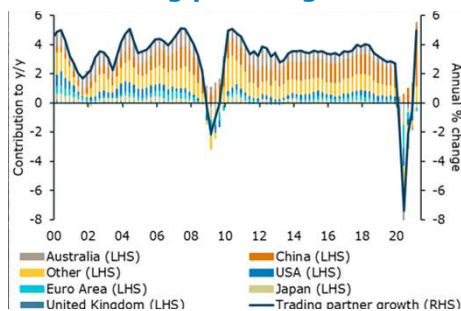
NZD/USD vs GlobalDairyTrade



Source: GlobalDairyTrade, Bloomberg, Macrobond, ANZ Research

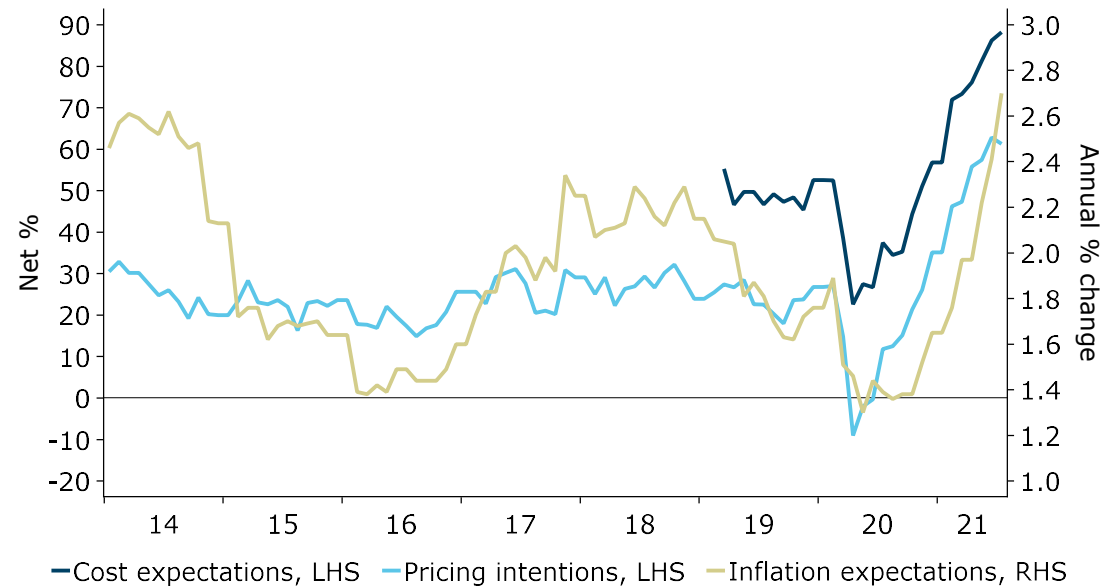
- Dairy prices are at a very profitable level (for most) but are off highs.
- NZD certainly not overvalued, but it might become so: RBNZ doesn't appear scared to be early out of the gate with hikes.

Trading partner growth





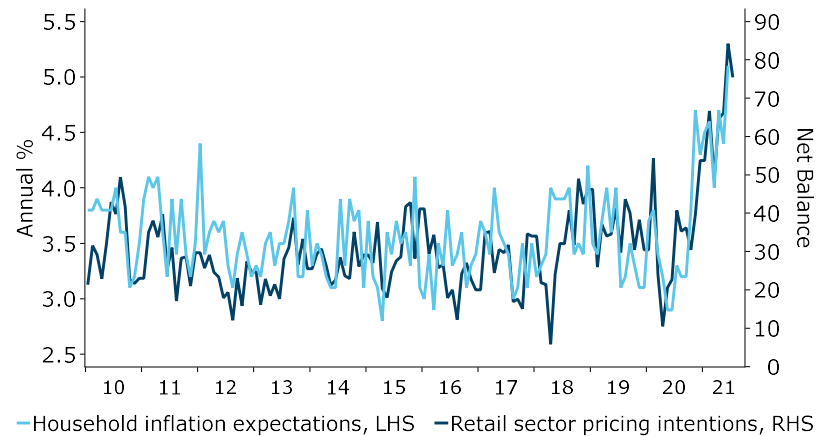
Inflation pressures are rising dramatically



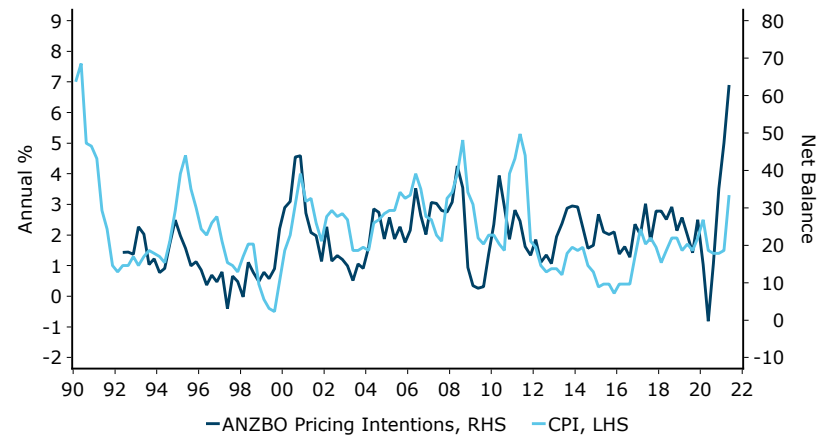
Source: ANZ Research, Macrobond

- Highest pricing intentions since the data began in 1992!
- Transitory? Looking more persistent by the day. Demand is strong; supply is hampered.
- Wages and inflation expectations are rising – much harder to look through than supply-side cost increases.
- Inflation expectations look set to go above 3%.

Pricing intentions vs pricing reality



Source: ANZ, Macrobond, ANZ Research

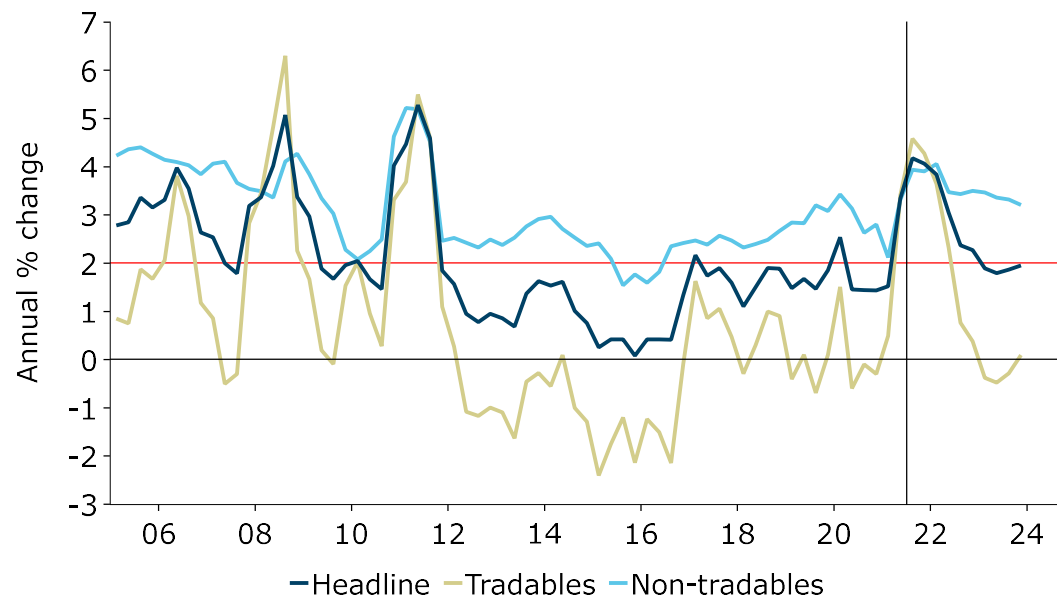


Source: ANZ, Stats NZ, RBNZ, Macrobond, ANZ Research

- Retailers and households agree that higher inflation is coming.
- You can argue that households are uninformed (they get the level wrong). But businesses should know what they're going to do with their prices.

OCR hikes
will work

Inflation forecasts

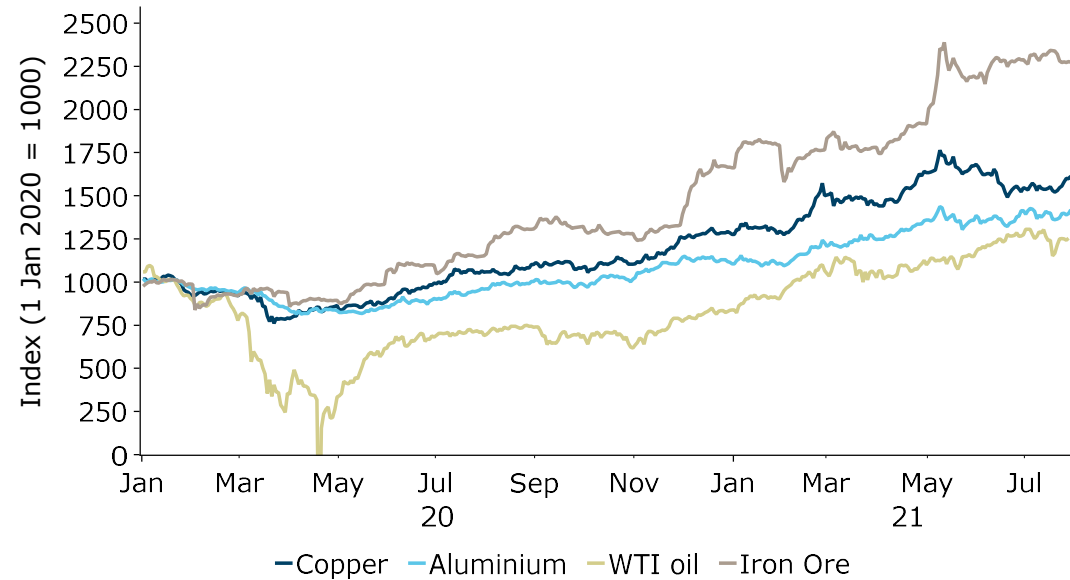


Source: Stats NZ, Macrobond, ANZ Research

- Inflation is transitory in our forecasts because we assume the RBNZ will ensure that it is by hiking the OCR.



Hard commodities

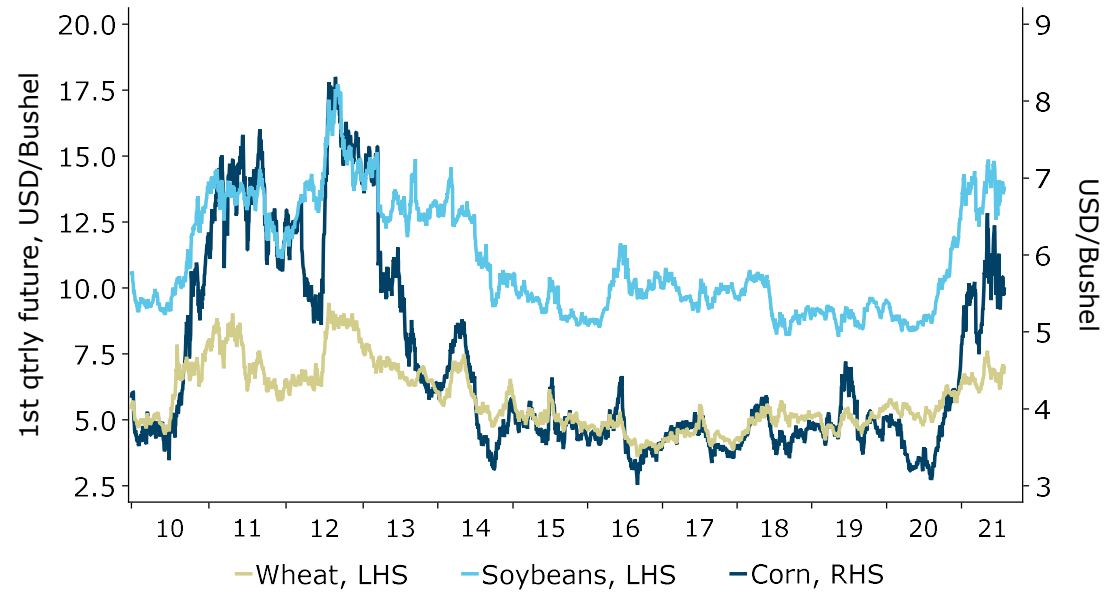


Source: LME, EIA, SGX, Bloomberg, Macrobond, ANZ Research

- Not just finished goods and shipping costs.
- The building blocks of “stuff” have gotten more expensive.
- Opinions are very divided on how persistent it will prove.



Soft commodities

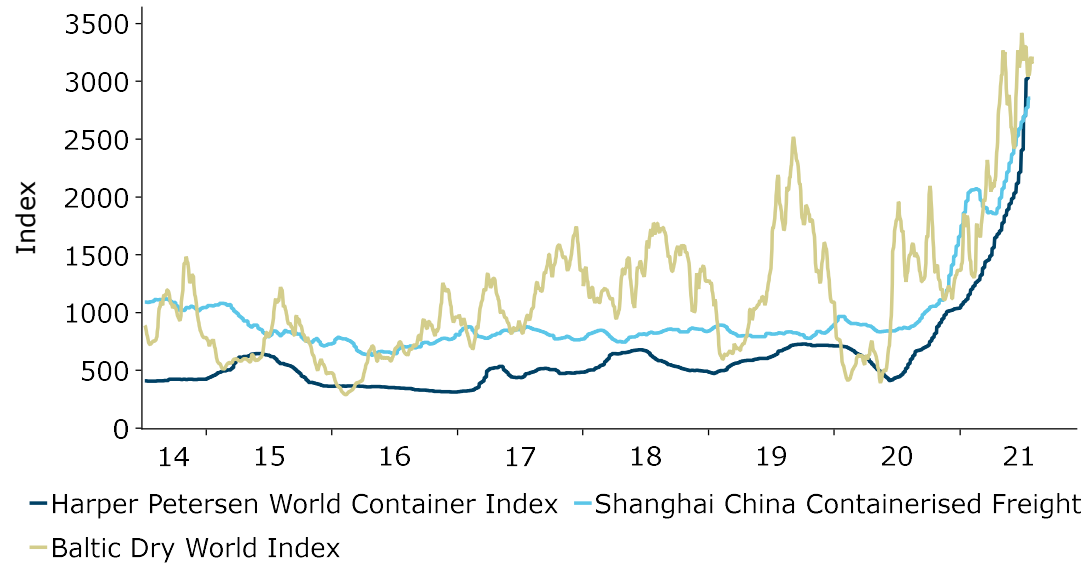


Source: Macrobond, ANZ Research

- High food prices suit NZ fine, but very challenging for poor countries
- Food security, climate change, COVID disruptions, geopolitics all suggest food prices higher



Shipping costs

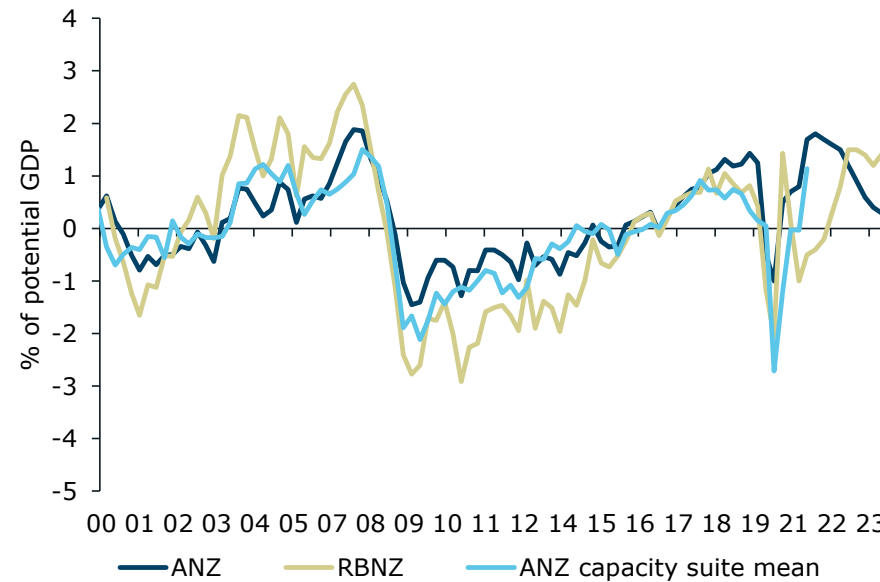


Source: Harper Petersen & Co., Shanghai Shipping Exchange, Baltic Exchange, Bloomberg, Macrobond, ANZ Research

- This is not a NZ-specific issue.
- Estimates of when it will improve keep getting pushed out.
- Problematic for retail, manufacturing, construction, agriculture.

Medium term
inflation
pressures
rising too

Output gap estimates

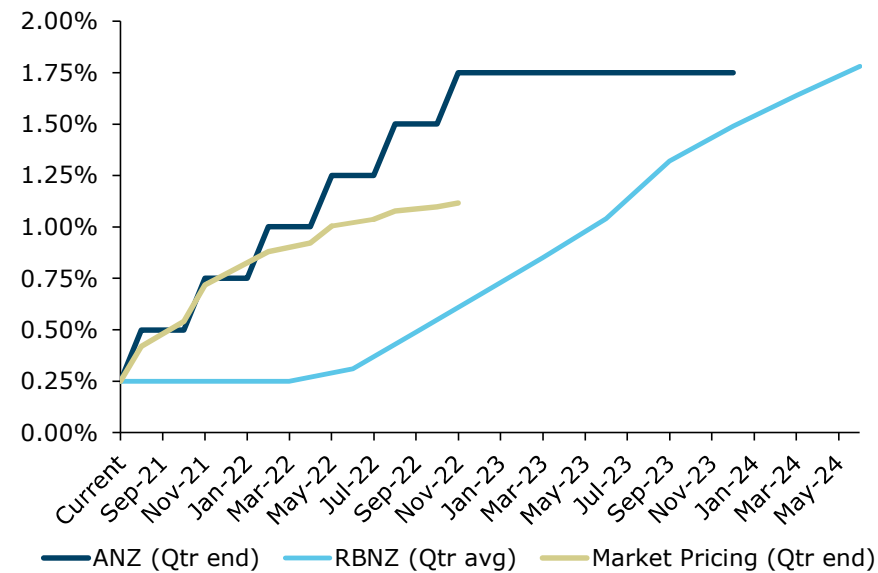


Source: RBNZ, ANZ Research, Macrobond

- When COVID hit we (and the RBNZ) thought we were looking at a temporary supply shock and a persistent demand shock.
- It turned out to be the opposite.

Can't stay
low forever

OCR forecast: ANZ and market pricing



Source: RBNZ, Bloomberg, ANZ Research

- RBNZ would probably prefer to wait for the data dust to settle, but inaction comes with its own risks. Don't want to have to scramble.
- The economists and market are united on an August kick-off.
- Labour market data on 4 August will be key.

Where's
neutral?

How will the RBNZ know where to stop?

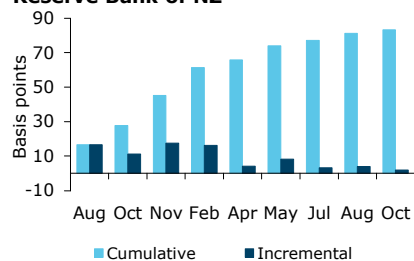


© Bill Waterson

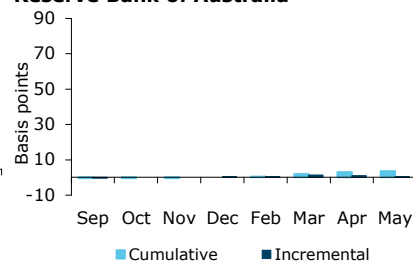
One of these kids is doing his own thing

Going their own way

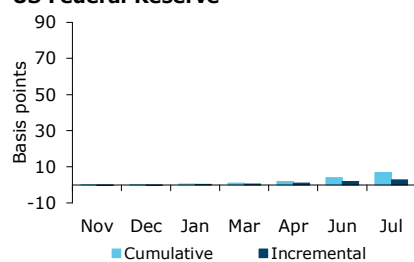
Reserve Bank of NZ



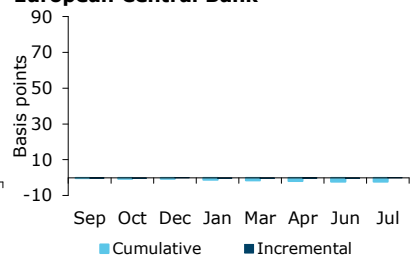
Reserve Bank of Australia



US Federal Reserve



European Central Bank



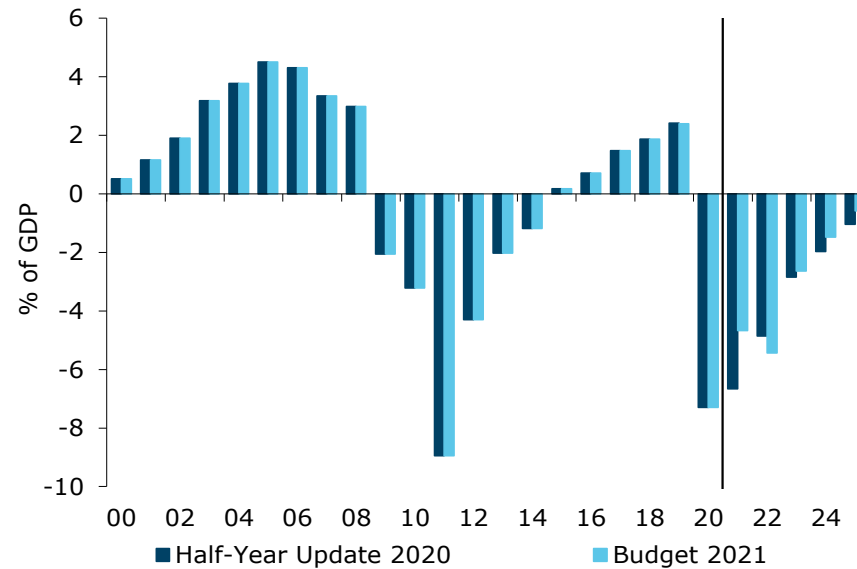
Source: Bloomberg, ANZ Research

Compared to the RBA, the RBNZ:

- Is less prescriptive about required wage growth
- Had a higher inflation starting point vs. target
- Has gotten QE out of the way
- Has a nuttier housing market (for now)

Medium-term
challenges
shouldn't be
forgotten

Total Crown OBEGAL

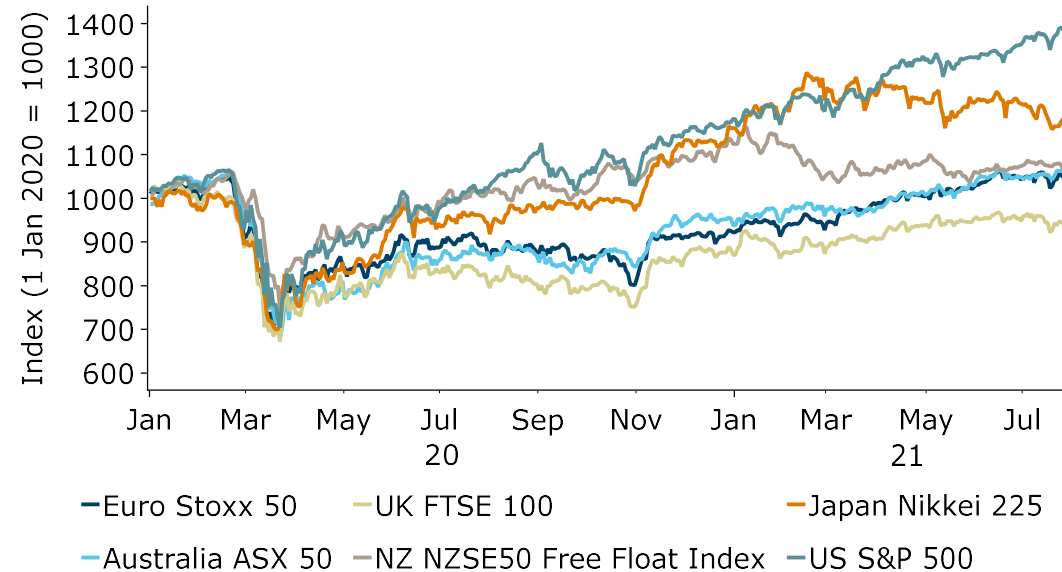


Source: Treasury, ANZ Research

- We had better hope for no recession (or earthquake or global financial crisis) any time soon.
- One day we'll have to repair the fiscal position: higher taxes, new taxes, superannuation changes?

The power
of the
printing
presses

Global equities



Source: STOXX, SPDJI, FTSE, Nikkei Inc., Bloomberg, Macrobond, ANZ Research

- Global risk appetite under threat if long-end yields rise, but for now, they are very well-behaved.
- Inflation holds the key – if long-term inflation expectations rise, the yield curve will steepen regardless of how central banks are expected to react.
- So far so good, but risk appetite is a bit wobbly.

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