

September 2023

# No pain, no gain?

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Sharon Zollner, Chief Economist

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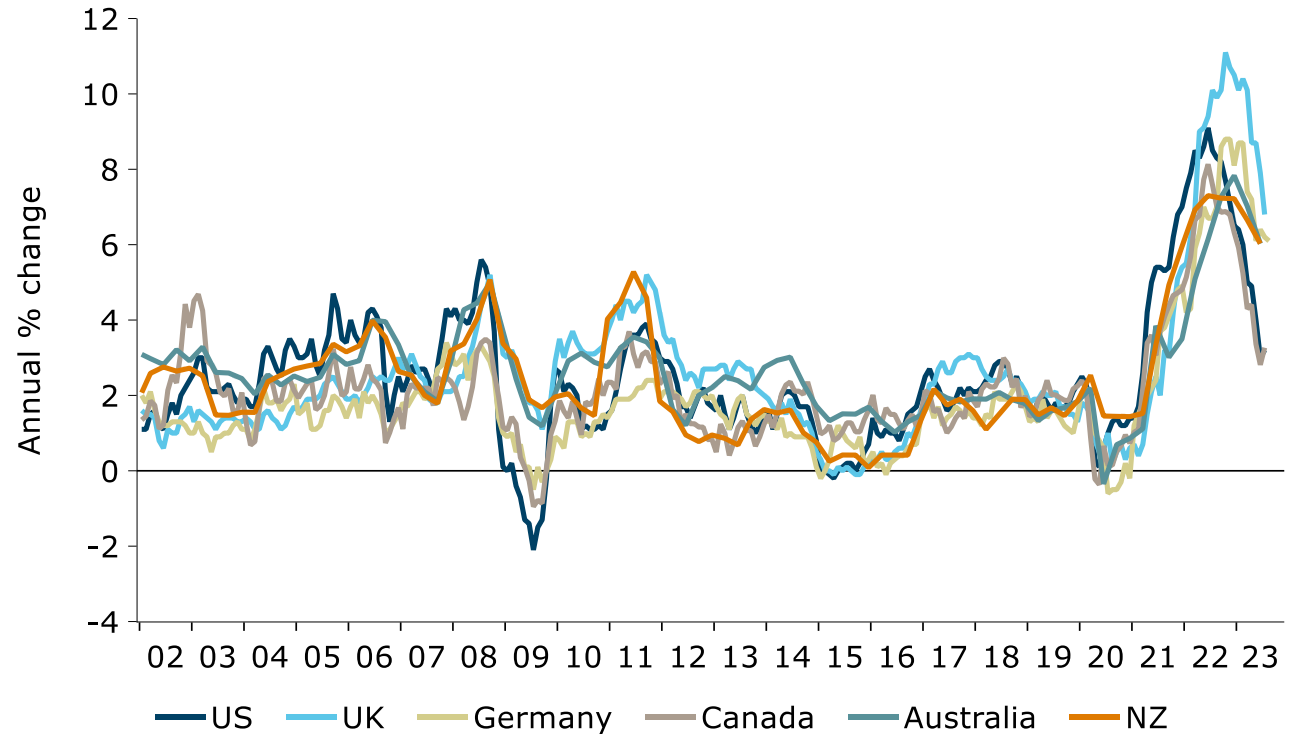
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A trouble  
shared is not  
a trouble  
halved

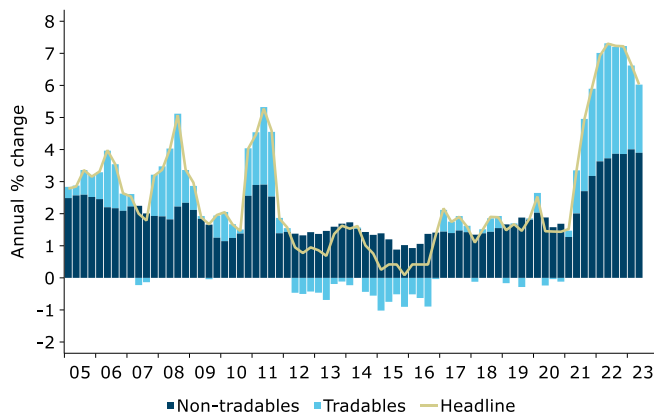
## CPI inflation



Source: BLS, ONS, DESTATIS, StatCan, ABS, Stats NZ, Macrobond, ANZ Research

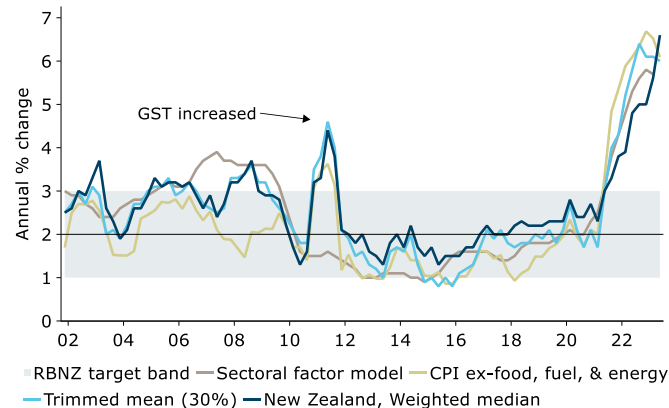
Perfect storm

## Tradable and non-tradable inflation contributions



Source: Stats NZ, Macrobond, ANZ Research

## Core inflation measures

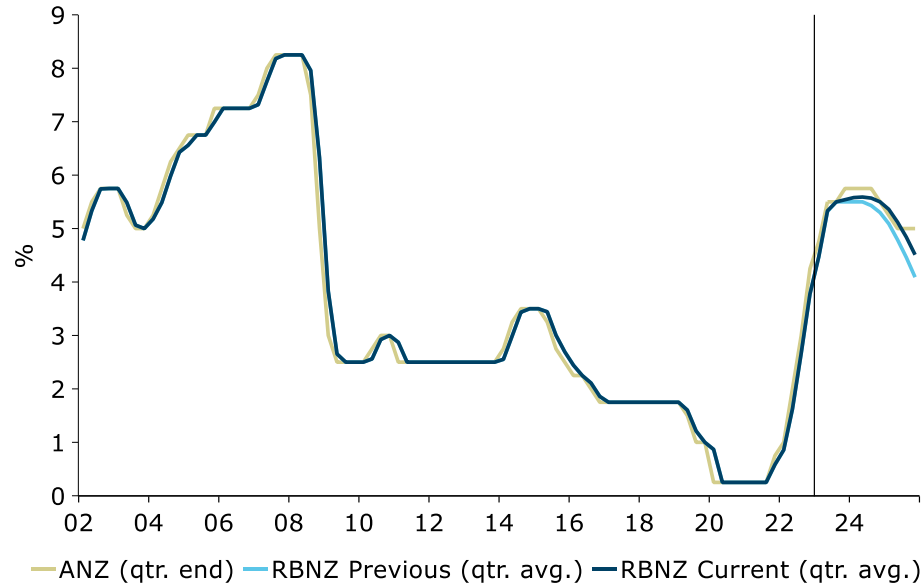


Source: Stats NZ, RBNZ, Macrobond, ANZ Research

- Goods inflation should fall quickly as large price jumps fall out of the equation.
- But core and domestic inflation is still strong.
- It's unclear how much slowing in the economy (particularly the labour market) is now baked in as the result of RBNZ tightening efforts, and it's also unclear how much it *needs* to slow to get inflation back to target.

Still  
inflationary

## Official Cash Rate forecast



Source: RBNZ, Macrobond, ANZ Research

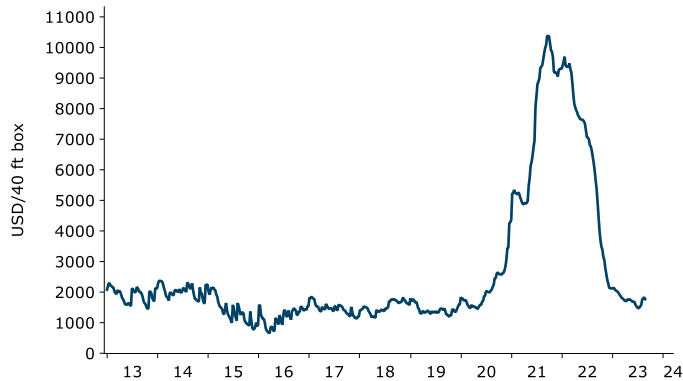
- We see OCR risks as tilted higher (while keeping a nervous eye on China risks).
- The RBNZ in August chose to raise the OCR track 9bps, a hat tip to them also seeing risks as tilted to the upside.



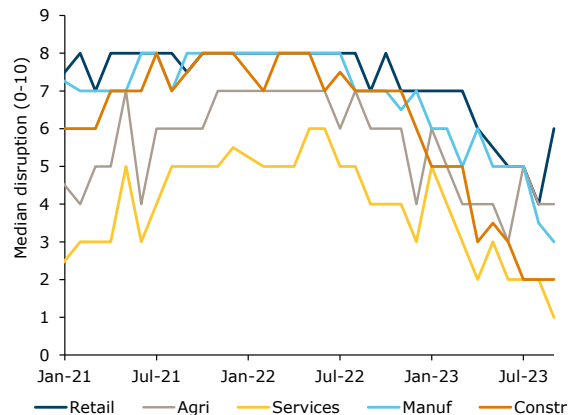


Low-  
hanging  
fruit

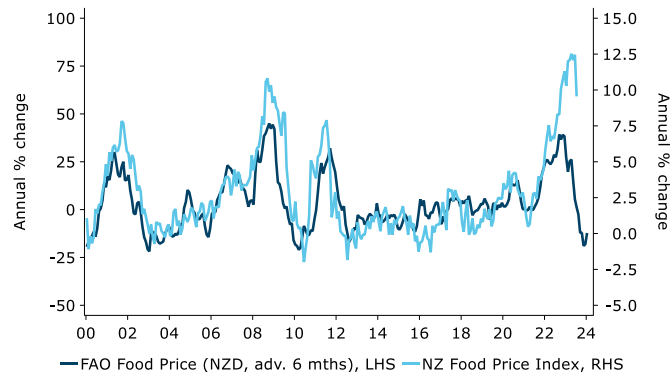
## Shipping costs



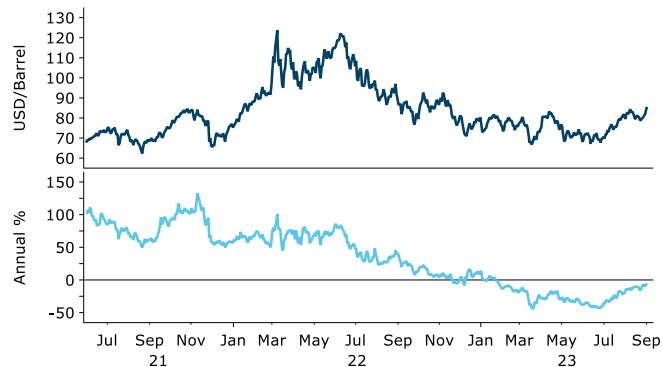
## ANZBO: inward freight disruption



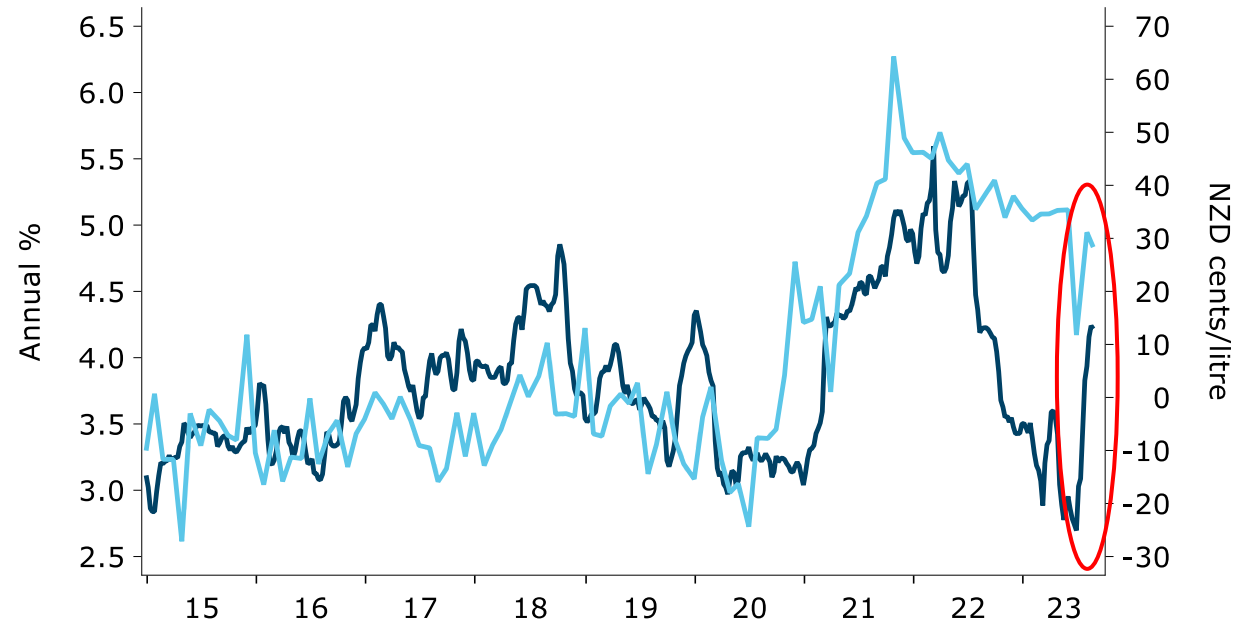
## Food prices



## WTI oil



## Petrol prices and household inflation expectations



— NZ discounted petrol price, RHS — Consumer Inflation Expectations, SA, LHS

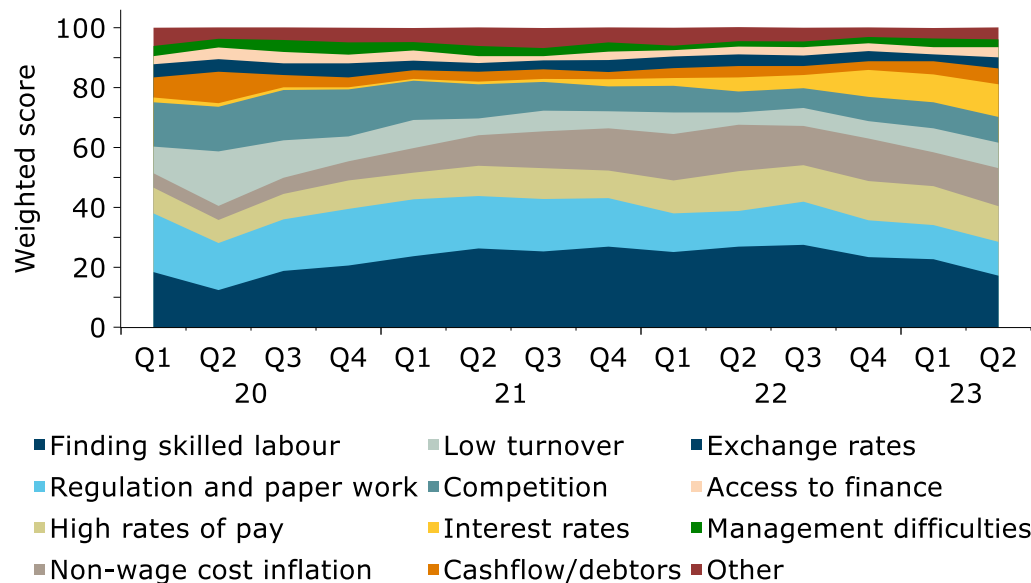
Source: MBIE, ANZ, Roy Morgan, Macrobond, ANZ Research

But...

- Weakening NZD and strengthening oil prices.

Still  
inflationary

## Firms' reported biggest problems

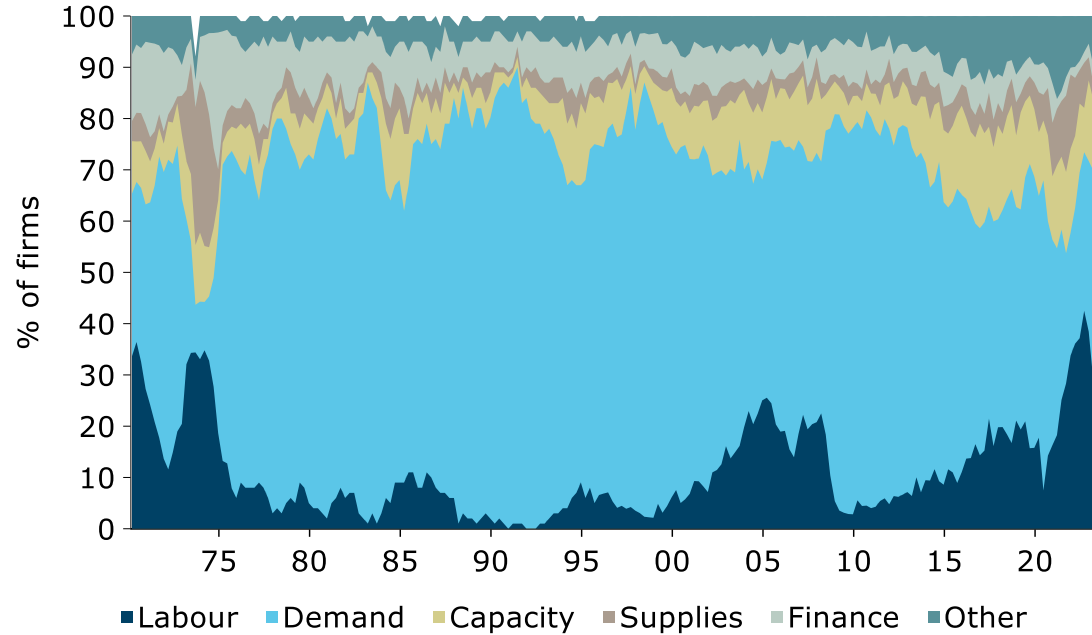


Source: Macrobond, ANZ Research

- The biggest four problems still all cause or reflect inflation: finding staff, non-wage costs, wage costs and regulation/paperwork.
- The RBNZ needs firms to have the type of problems that throw sand in the gears of inflation: low turnover, competition.

Not  
normal  
yet

## Firms' limiting factors for production



Source: NZIER, Macrobond, ANZ Research

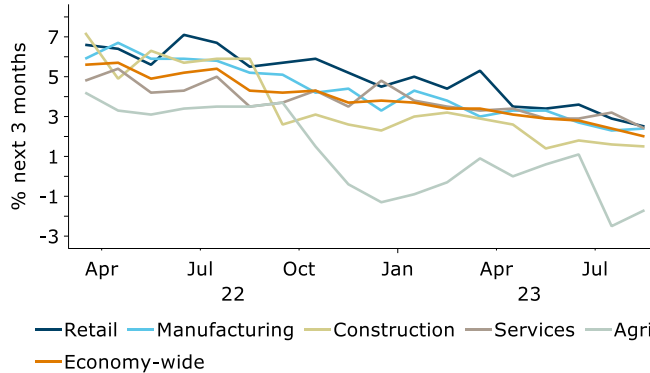
- Labour market tightness has never been such a constraint on growth as it was in the second half of last year.
- Normalising but still not 'normal'.



# ANZBO inflation signals: getting there

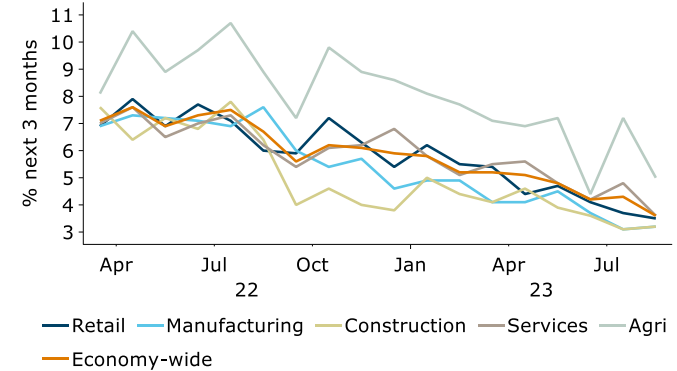
Going the  
right way

## Pricing intentions by sector



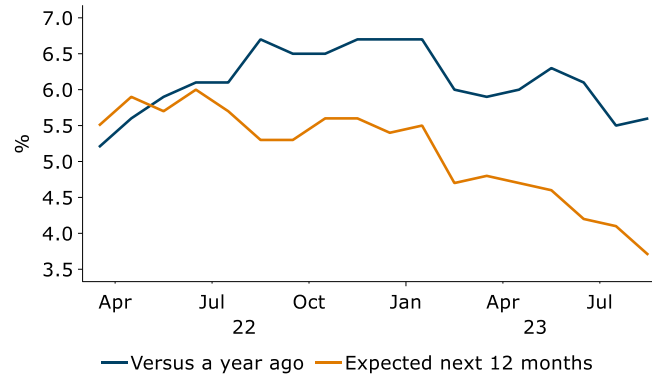
Source: Macrobond, ANZ Research

## Cost expectations by sector



Source: Macrobond, ANZ Research

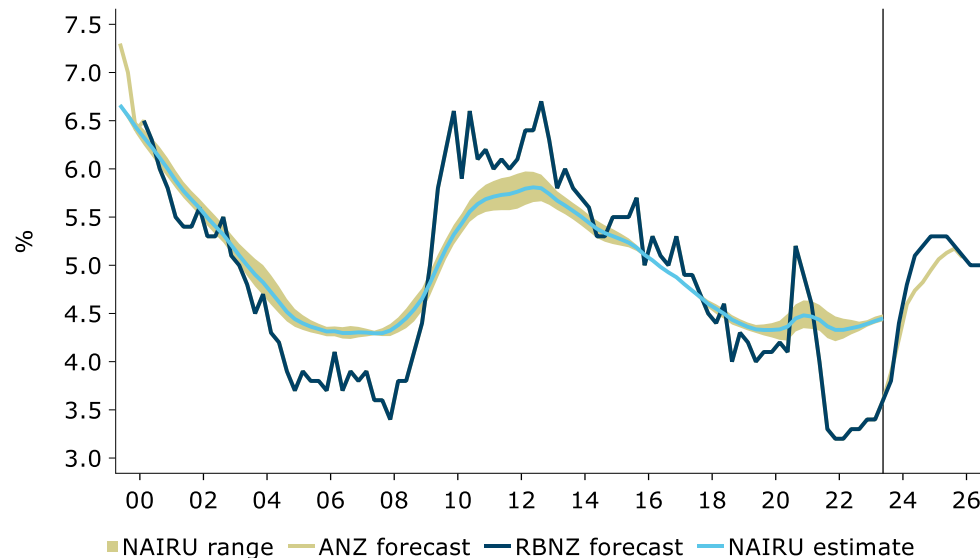
## Reported and expected wage growth



Source: Macrobond, ANZ Research

## Upside risk #1: Resilient labour market and consumer

### Unemployment vs. the NAIRU



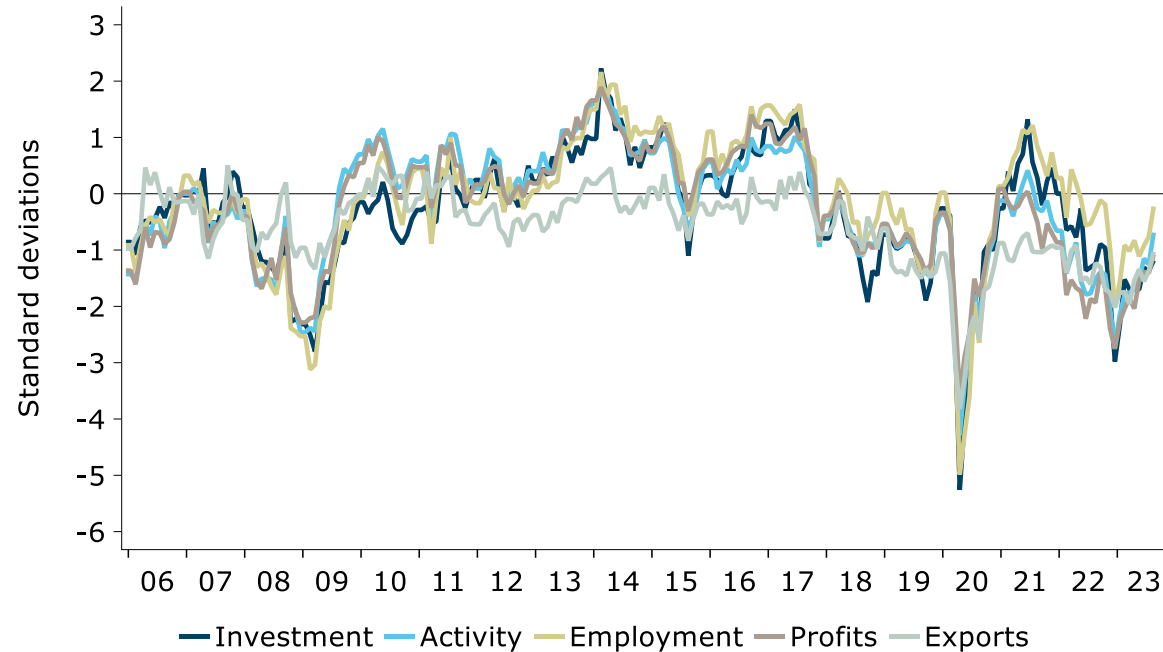
Source: Stats NZ, Macrobond, ANZ Research

How fast  
will things  
cool?

- The labour market is definitely cooling. But is the unemployment rate going to rise as quickly as when the Global Financial Crisis hit?
- Doesn't feel like that yet, but it's true that net migration is a wild card, boosting labour supply.

Relief  
rally?

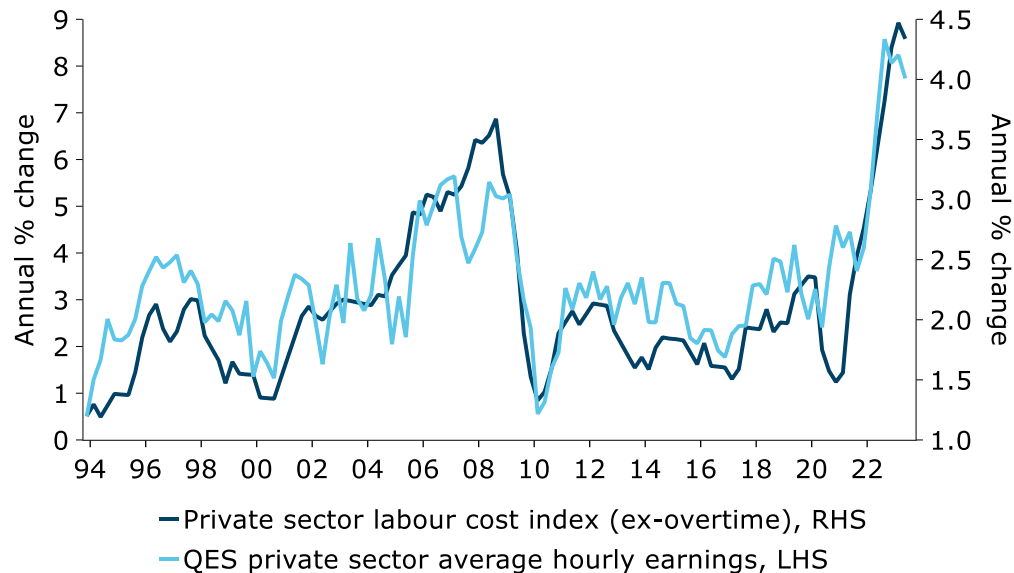
## ANZBO activity indicators



Source: Macrobond, ANZ Research

- Subdued but off their lows. Doesn't look like capitulation, but things are cooling.

## Wage growth is still very strong



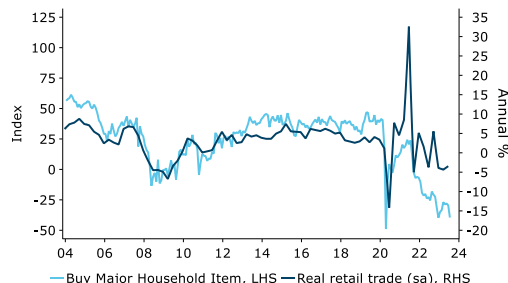
Source: Stats NZ, Macrobond, ANZ Research

Looking  
peaky

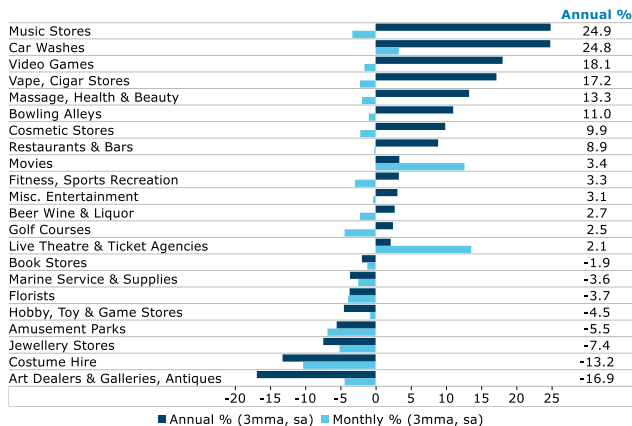
- At 3.6% unemployment is still very low despite record-high labour force participation of 72.4%.
- Strong wage growth and excellent job security goes a long way to explaining why spending, while definitely slowing, has held up so much better than consumer confidence.

Q1 fall  
looks  
cyclone-  
related

## Good time to buy major household item vs. retail sales

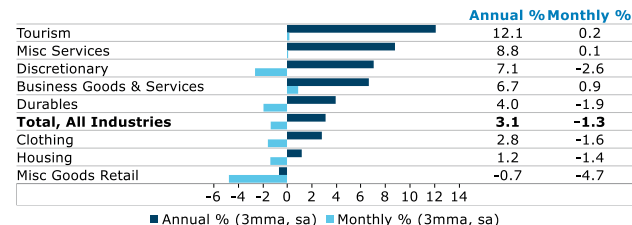


Source: Stats NZ, Macrobond, ANZ Research

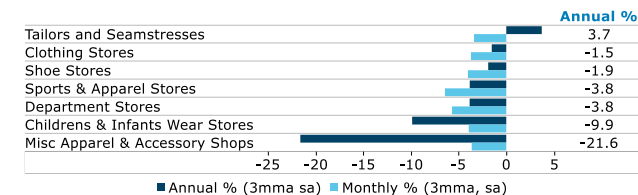


Source: Macrobond, ANZ Research

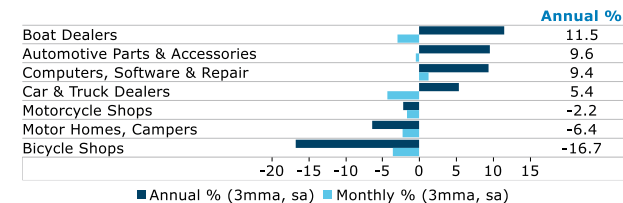
## But spending is weakening



Macrobond, ANZ Research



Source: Macrobond, ANZ Research



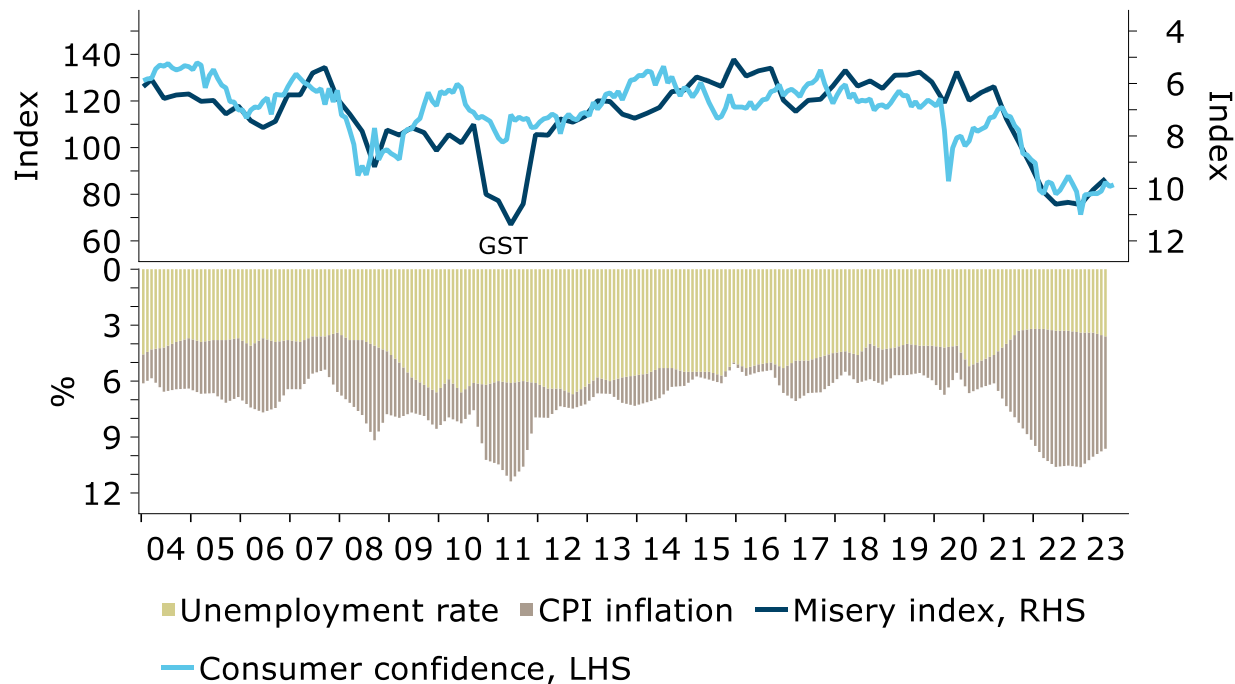
Source: Macrobond, ANZ Research

- Headwinds : higher mortgage rates, cost of living, lower house prices, loosening labour market.
- Tailwinds: very low unemployment, high wage growth, fiscal support, population growth, housing turnaround.





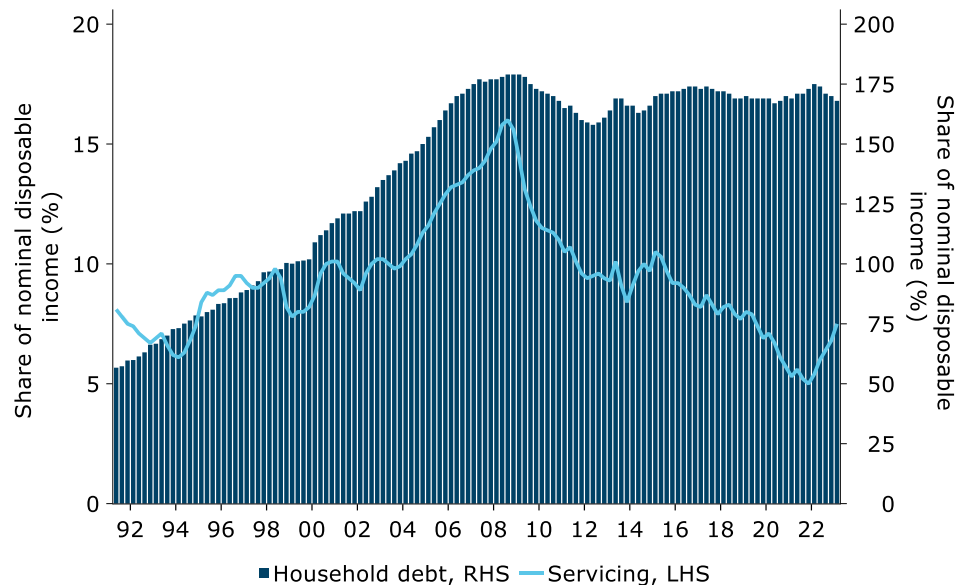
## People hate both inflation and unemployment, but the consequences for spending are very different



Source: Stats NZ, Roy Morgan, Macrobond, ANZ Research



## Household debt servicing

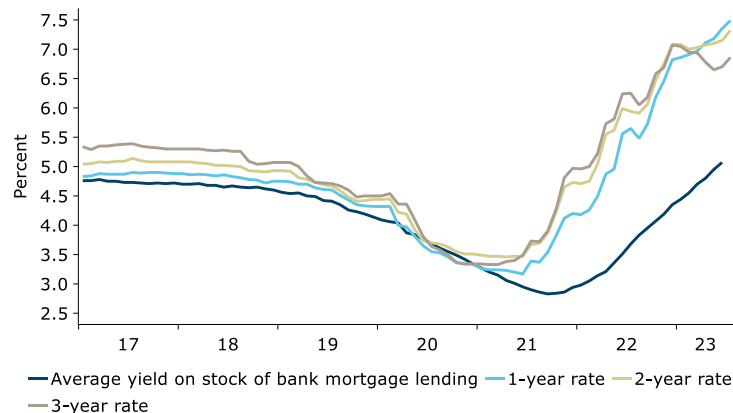


Source: Stats NZ, RBNZ, Macrobond, ANZ Research

- Household debt is (too) high, but not as high vs. incomes as you might think given such a crazy housing boom. And only 38% of households have a mortgage.
- Debt-servicing ratios are forecast to peak well below 2008. Our forecasts imply it rising to about 11% vs. 16% pre-GFC.

Pipeline  
pain

## Mortgage rates



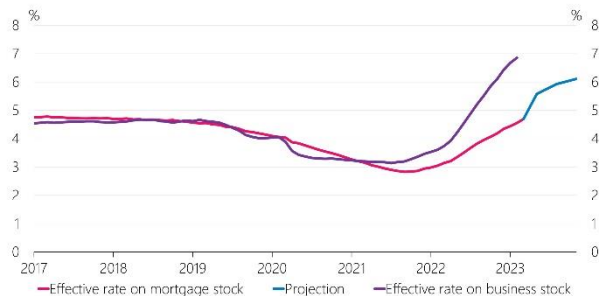
Source: RBNZ, Macrobond, ANZ Research

Latest data point: effective mortgage rate is 4.8%.

## Time to repricing

Figure 2.1

Effective lending rates



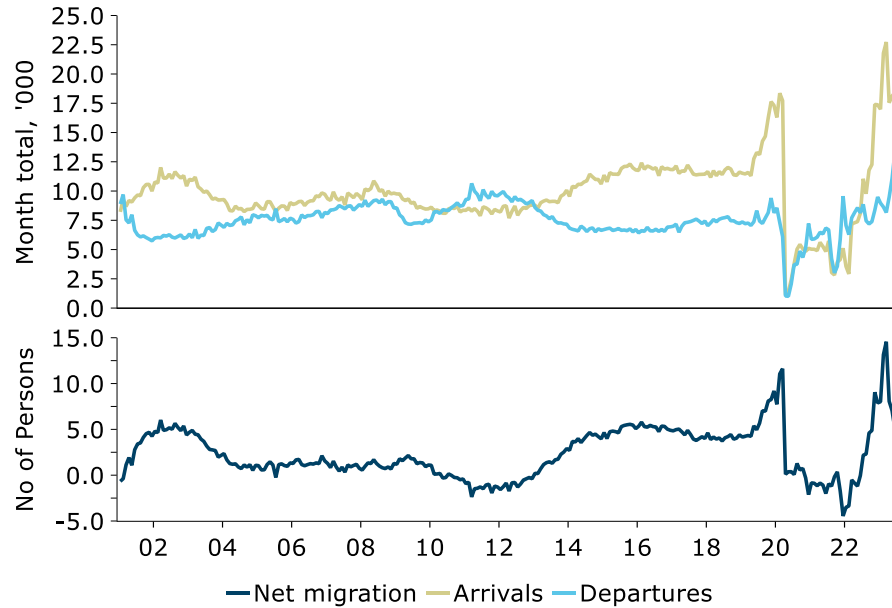
Source: RBNZ Bank Balance Sheet survey, Income Statement survey, RBNZ estimates.

Note: The effective interest rate is the average interest rate paid across the stock of all mortgage lending and all business lending. This projection is based on current mortgage and swap rates as at the 27th of April.

Only 10.5% of NZ mortgage debt is floating. Contrast with Australia (around 65%) and with business lending, where around 80% is either floating or repricing within 3 months.



## Upside risk #2: net migration and housing

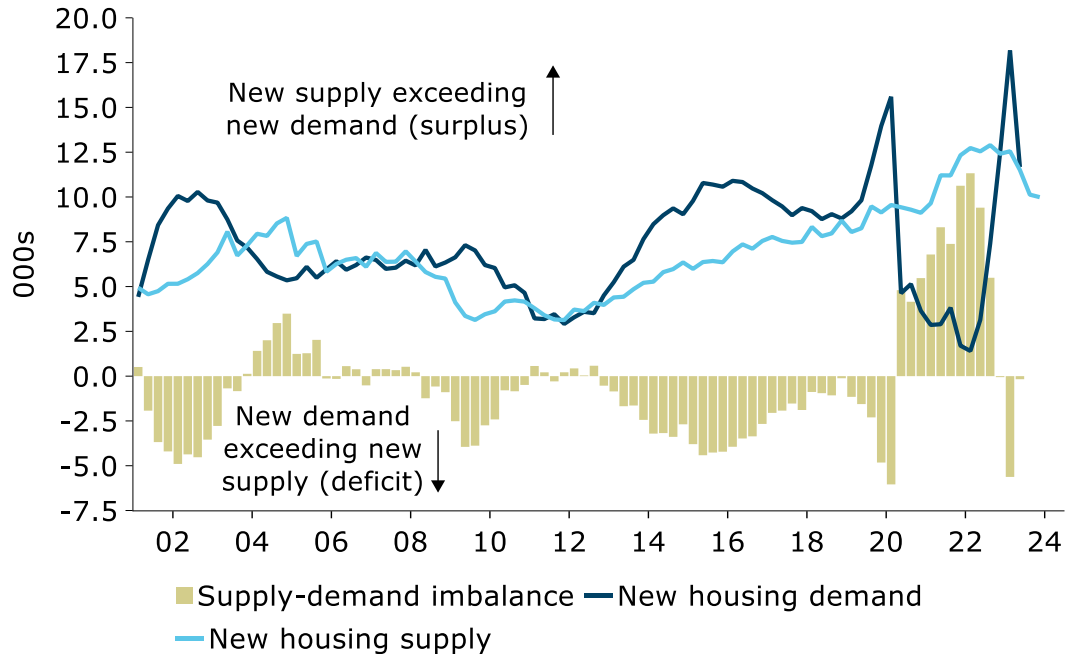


- Immigration policy has been significantly loosened. That plus pent-up demand means net migration is likely to be around 80k this year.
- Net migration boosts labour supply but also demand (incl. housing). The RBNZ is assuming a low but positive impact on inflation.





## New housing demand vs supply growth



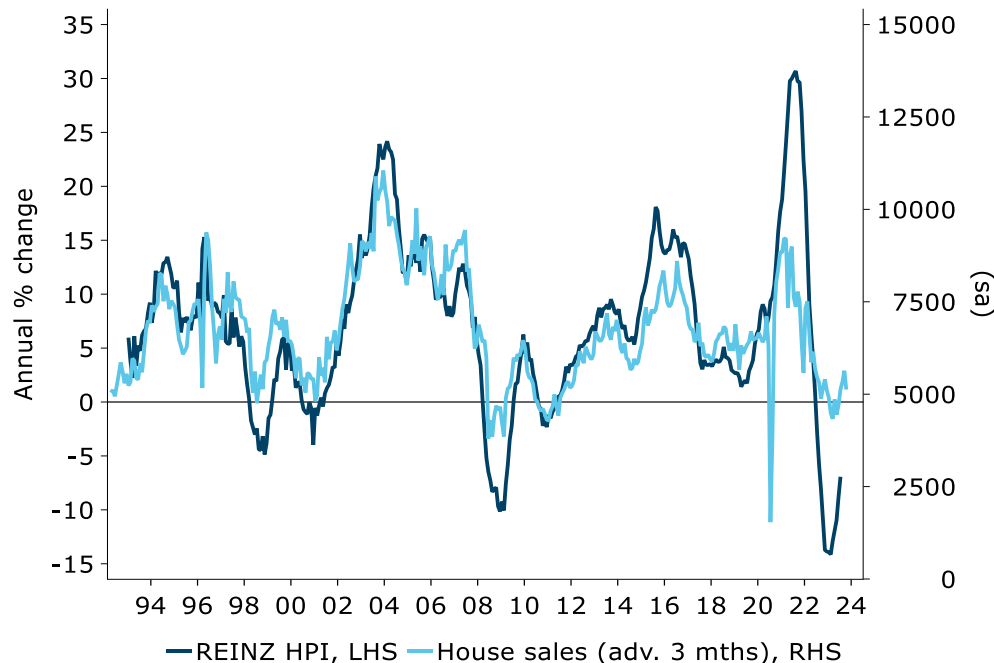
- House building is slowing just as population growth takes off.
- Progress in reducing housing shortages could be undone quickly.





Bottoming  
out

## Housing turnover and house price inflation

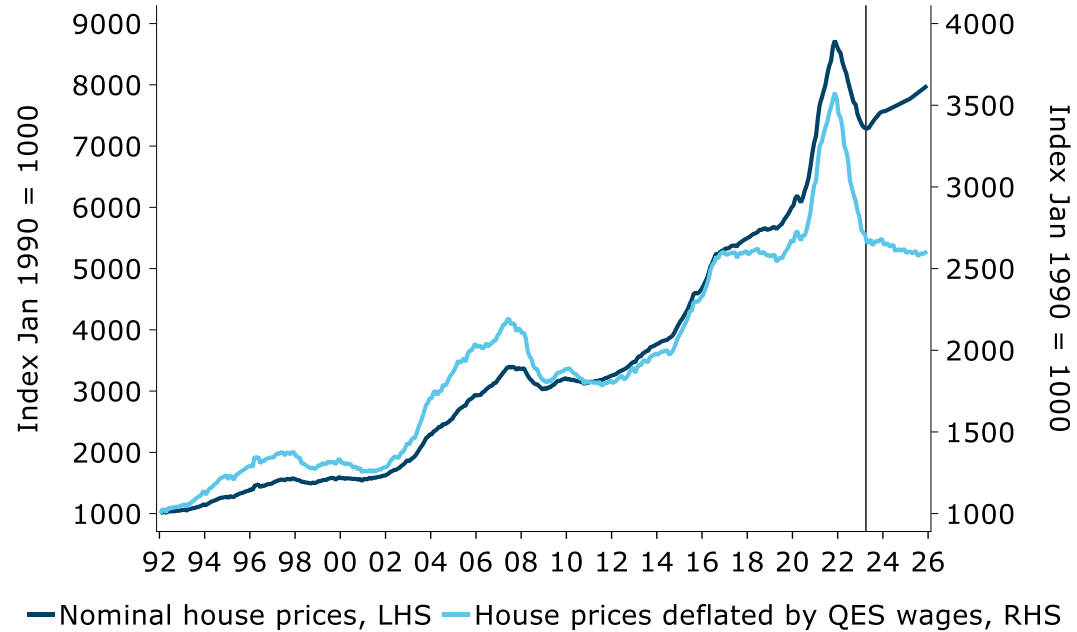


Source: REINZ, Macrobond, ANZ Research

- House prices fell more than 16% from their November 2021 peak.
- We are forecasting that to be the bottom. That's a soft landing.

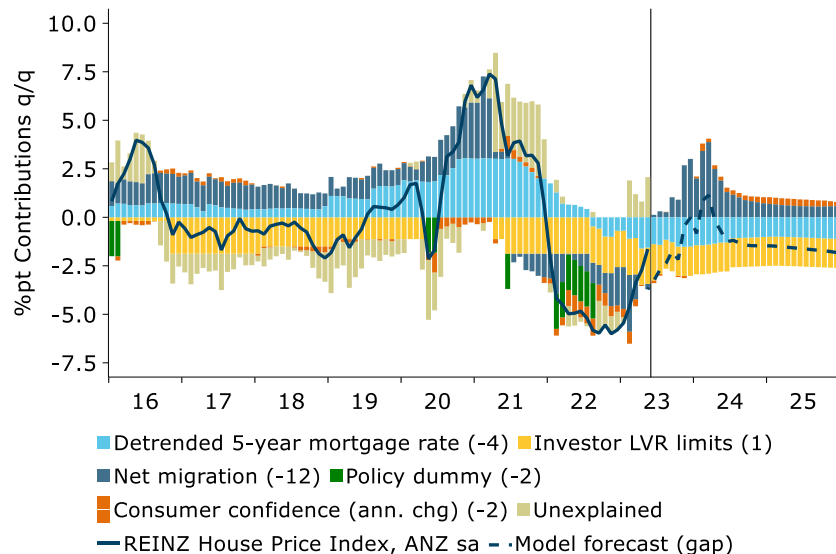


## Still too high



- Due partly to strong wage growth, *real* house prices are now around a quarter lower than they were at their peak.
- Getting back to 2010 levels of affordability would imply a near-halving in real house prices. Getting back to 1992 levels would take a near-70% fall from their peak.

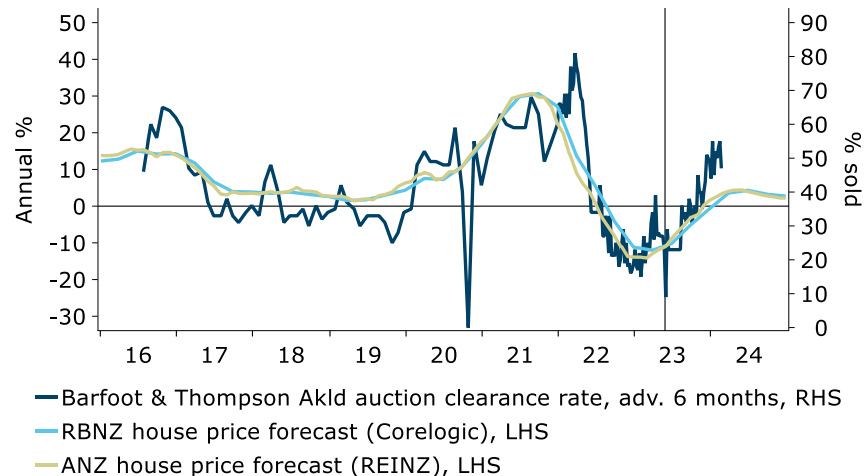
## What's driving it?



Source: REINZ, ANZ Research

- Modeled using our forecasts for mortgage rates and migration and assuming policy is unchanged (CCCFA, investor property tax rules).

## Will the RBNZ tolerate green shoots?

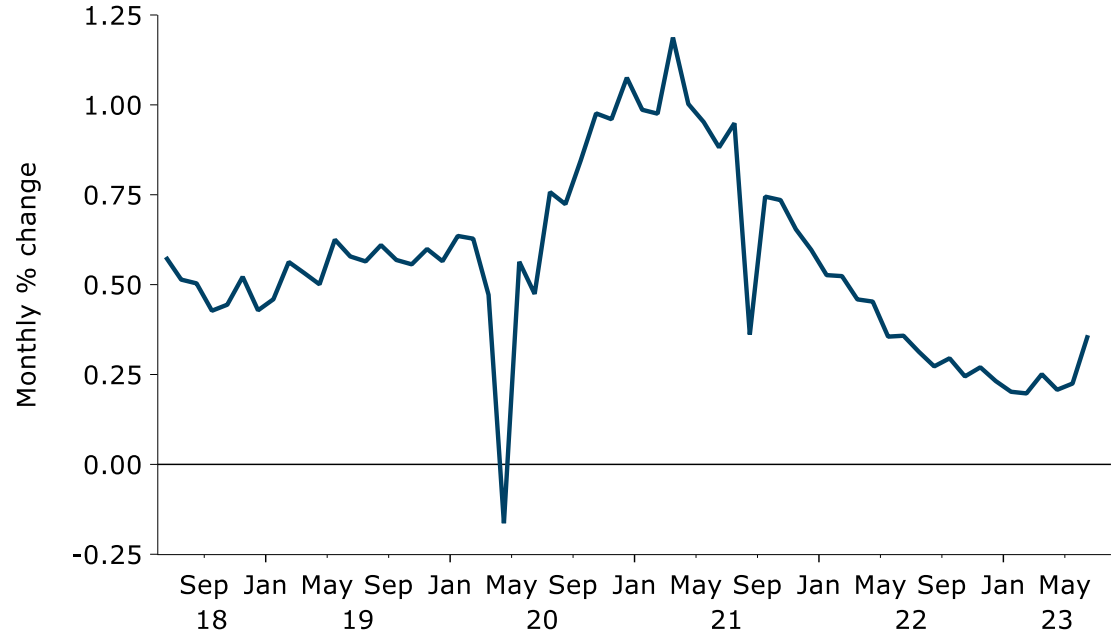


Source: Corelogic, REINZ, B&T, interest.co.nz, Macrobond, ANZ Research

- There is potentially a little upside risk to the RBNZ's and our forecast for house prices.
- Whether this is seen as problematic would depend on how the labour market is going.



## Mortgage lending rising again

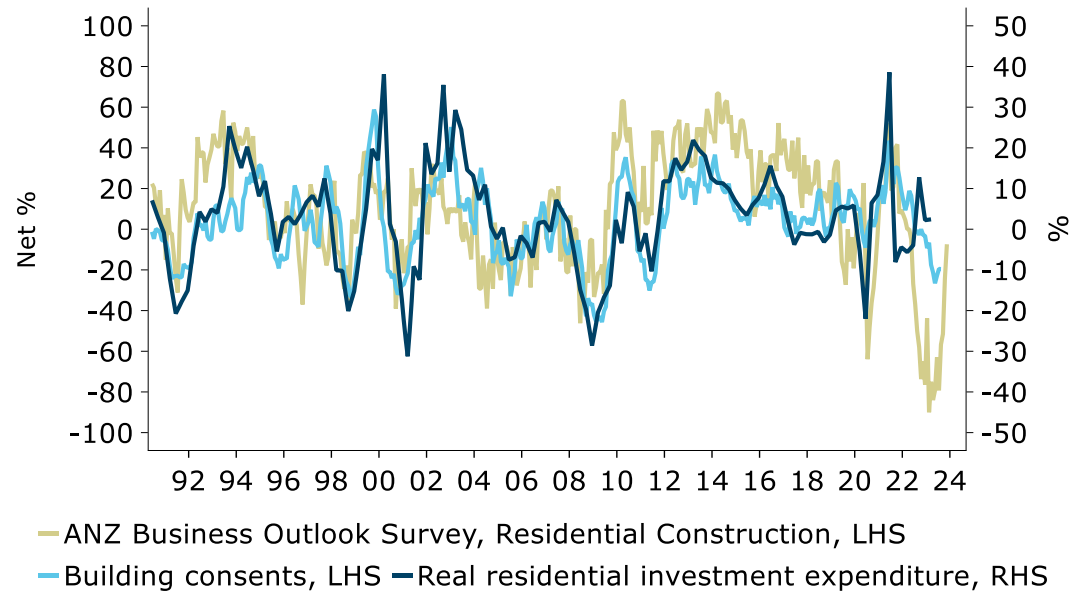


Source: RBNZ, Macrobond, ANZ Research





## Builders are very pessimistic, but less than previously



Source: Stats NZ, ANZ, Macrobond, ANZ Research

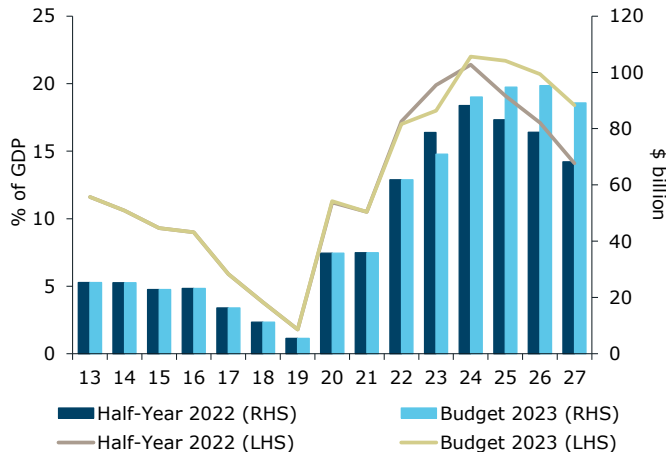
- Weak house sales, still-high construction costs, high interest rates and lower house prices make the maths very hard on new builds now.
- But with migration now soaring and construction costs easing the outlook could improve.
- It's been an emotional rollercoaster for builders.



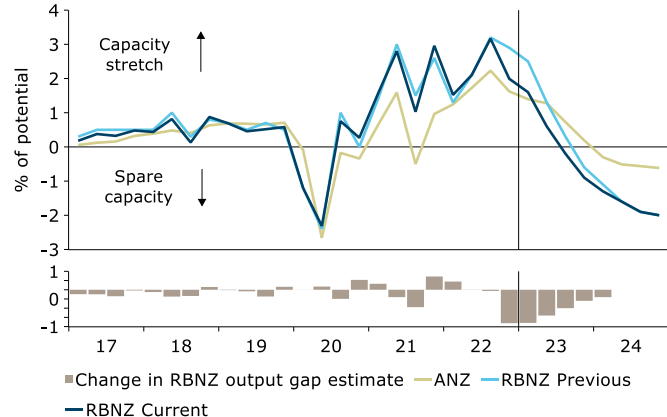


## Upside risk #3: fiscal policy

### Net debt



### Output gap estimate

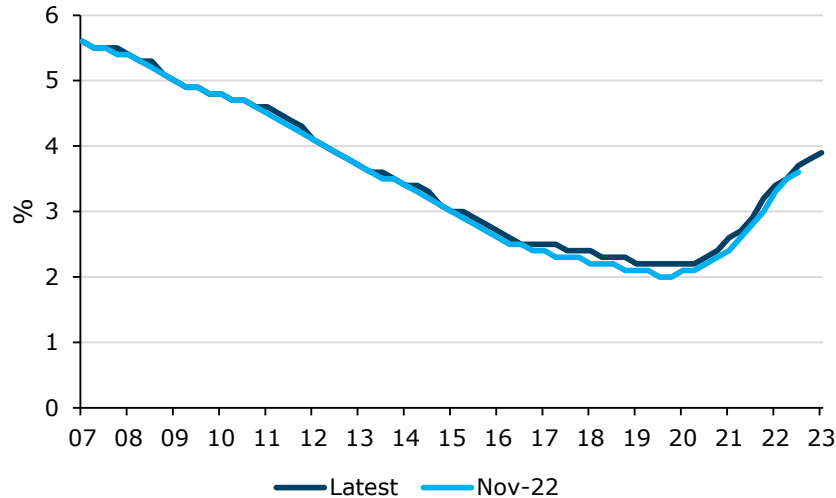


Source: RBNZ, Macrobond, ANZ Research

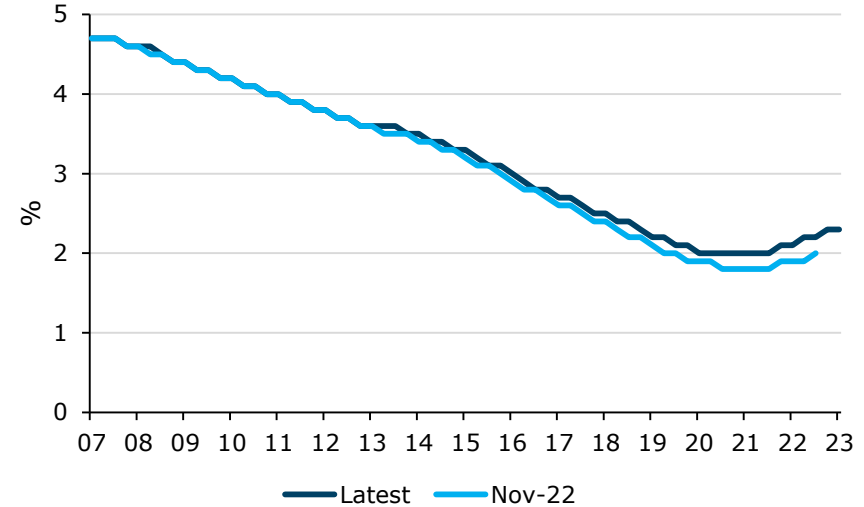
- Compared to Dec 22, the Budget implies an extra \$5bn of spend in the year to June 2024 – that's 1.4% of GDP.
- A good chunk of that is capex, but it's still a big ask.
- The Treasury's macro forecasts are due a downgrade in the PREFU.

## Upside risk #4: Getting 'used' to higher inflation?

Short-run



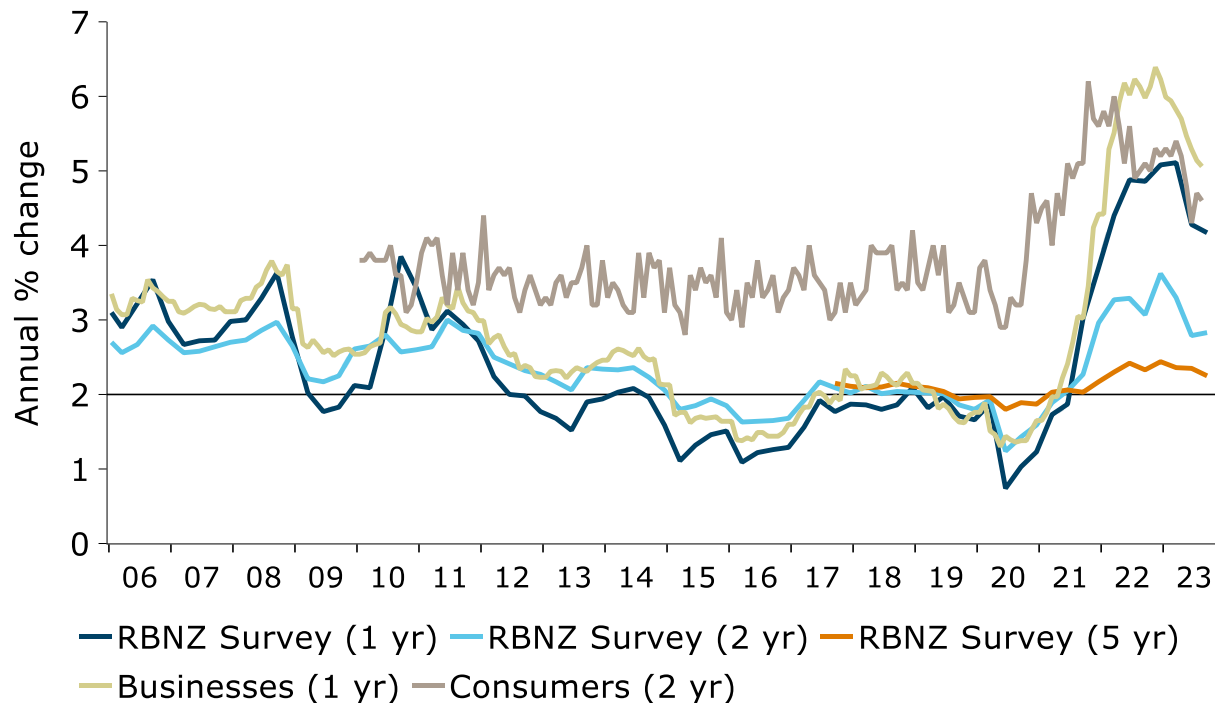
Long-run



- Is the neutral rate more than 150bps lower than 2005-7? Why?
- Can't raise estimate by 25bps too many more times without having to hike to offset it.
- With the RBNZ's range of estimates of the short-run neutral OCR 280bp wide (and the long-run range 250bp wide), the real question is whether where the OCR should be between 4% or 7%, not whether it should be 5.5% or 5.75%.

Not there  
yet

## Inflation expectations

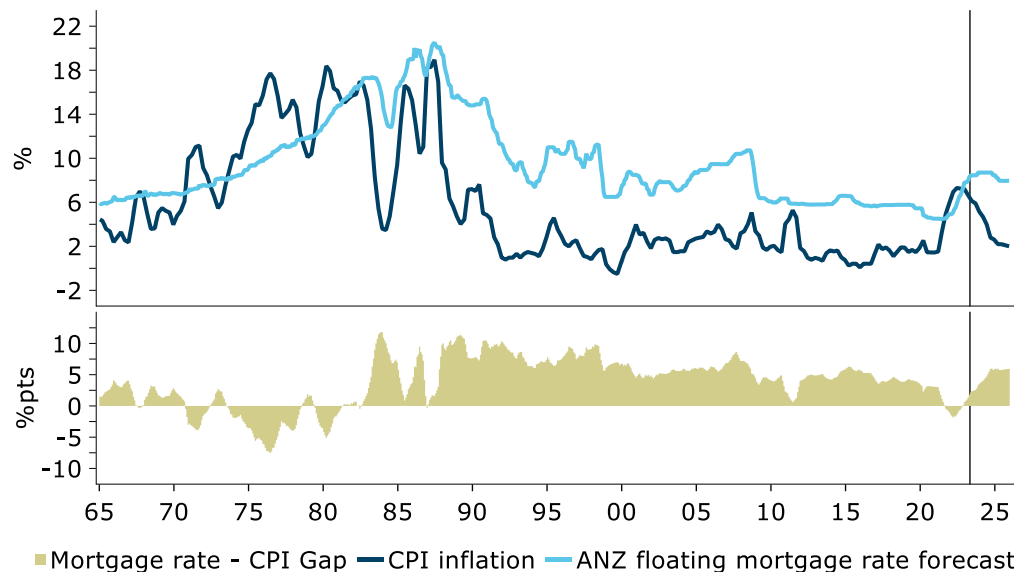


Source: RBNZ, Roy Morgan, Macrobond, ANZ Research

- Mixed bag. Getting there!

How high  
could rates  
go?

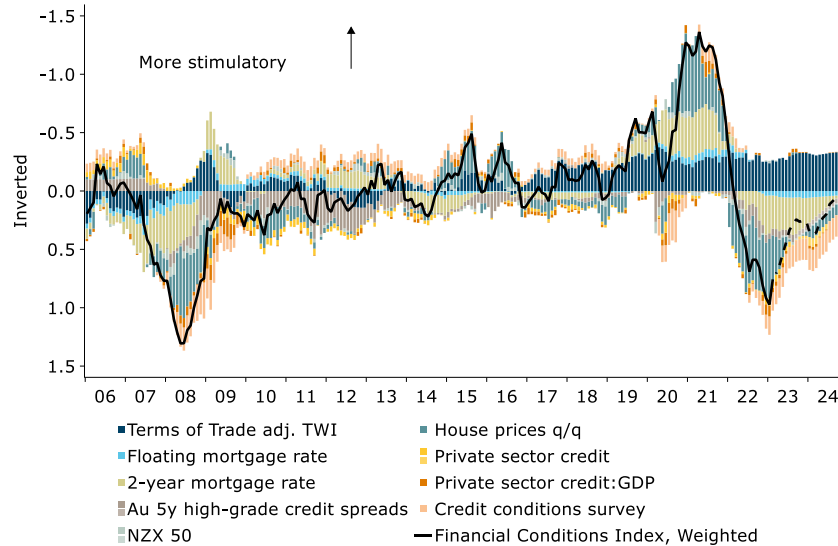
## Floating mortgage rate and CPI



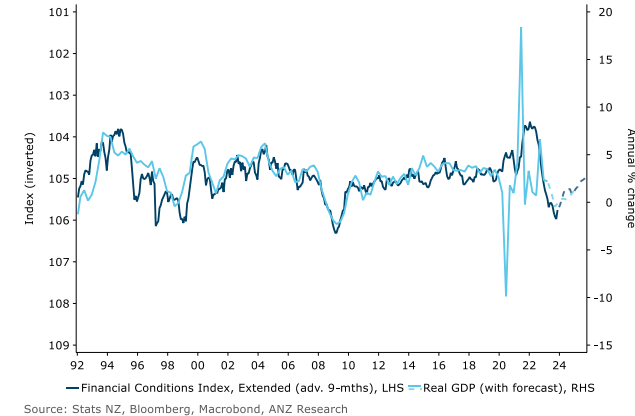
Source: Stats NZ, RBNZ, Macrobond, ANZ Research

- Positive real interest rates are a crucial nominal anchor. Most of the work getting there in our forecasts is done by inflation falling by about 5%pts from its peak.
- If inflation doesn't fall as far or fast as expected, the OCR will need to go higher.

## Putting it together: Financial conditions index



Source: Stats NZ, Bloomberg, Macrobond, ANZ Research

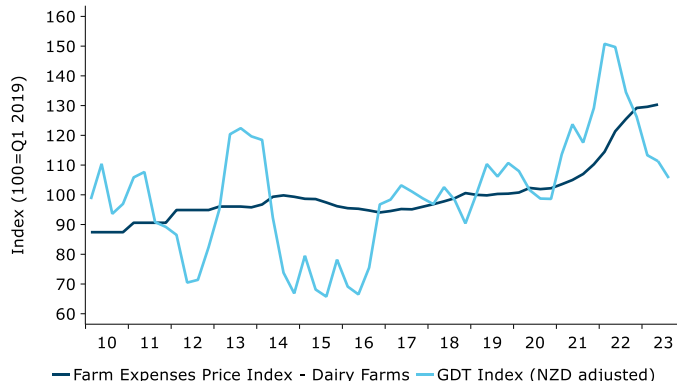


- Plugging in our forecasts for house prices, mortgage rates and the TWI shows financial conditions are currently the tightest since 2009, driven primarily by mortgage rate increases and house price falls (roughly equally). NZD providing an offset.
- But financial conditions are set to ease from here, as house price falls peter out, all else equal. Watch global risks though.



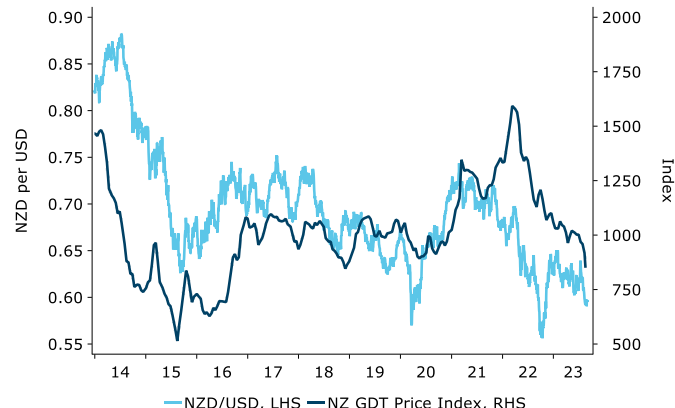
Grim  
outlook  
for  
exporters

## Dairy price below breakeven



Source: Stats NZ, RBNZ, Global Dairy Trade, Macrobond, ANZ Research

## NZD is out of favour



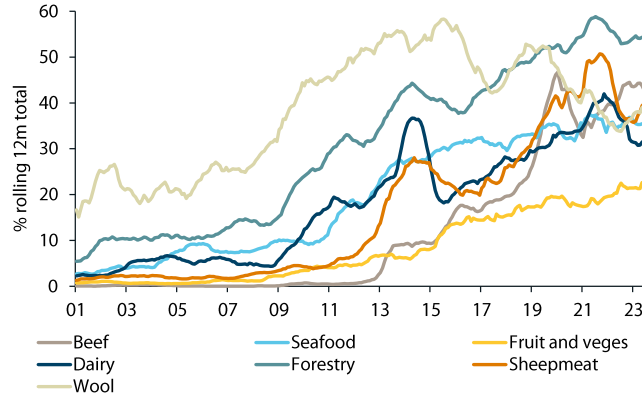
Source: Bloomberg, Global Dairy Trade, Macrobond, ANZ Research

- Weakening global demand for dairy products is outweighing weak growth in global supply. We've revised down our 2023/24 milk price estimate to \$7.15/kgMS, but there's downside risk.
- The global trade environment is really tough: toothless WTO, geopolitics, climate change driving protectionism.
- The NZD's fate has been driven by the broader USD story rather than NZ-specific factors, but the latter could start to count.

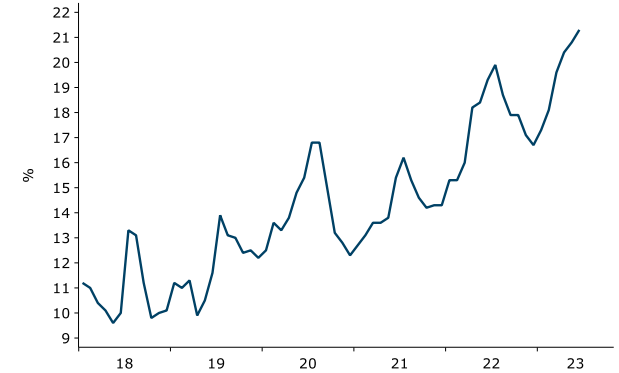


China under pressure

## % of NZ commodity exports to China

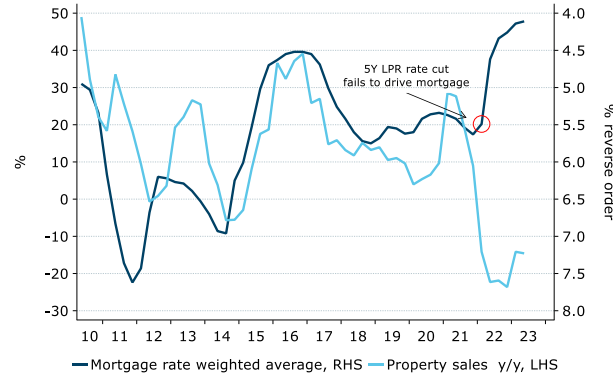


## China unemployment 16-24



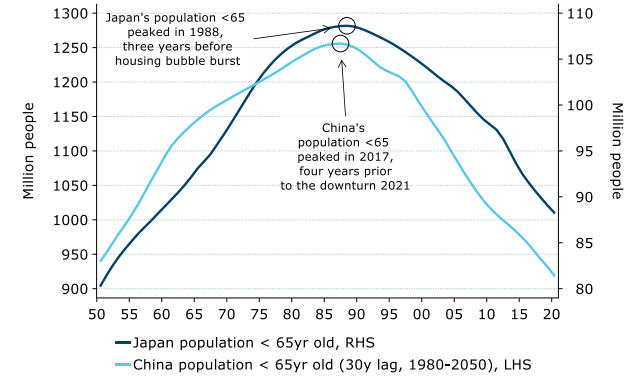
Source: China National Bureau of Statistics, Bloomberg, Macrobond, ANZ Research

## China rate cuts are failing to stimulate property sales



Source: PBoC, Bloomberg, Macrobond, ANZ Research

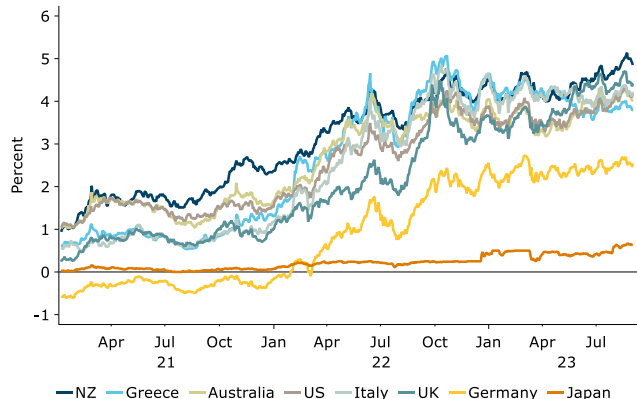
## China population is shrinking



Source: BIS, PWT, MLIT, NBS, Bloomberg, Macrobond, ANZ Research

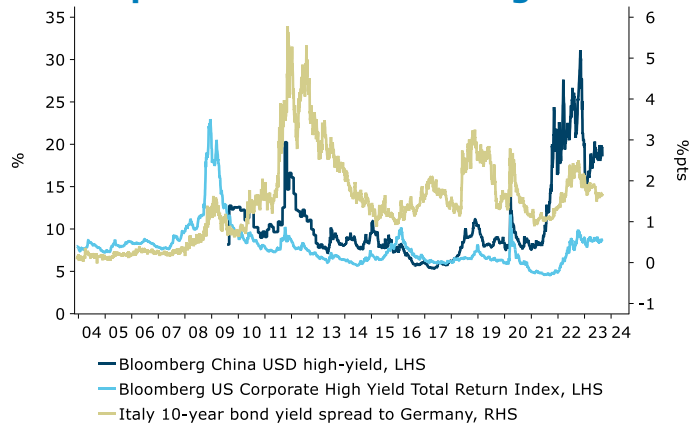
## What to watch

### 10-year bonds: under pressure



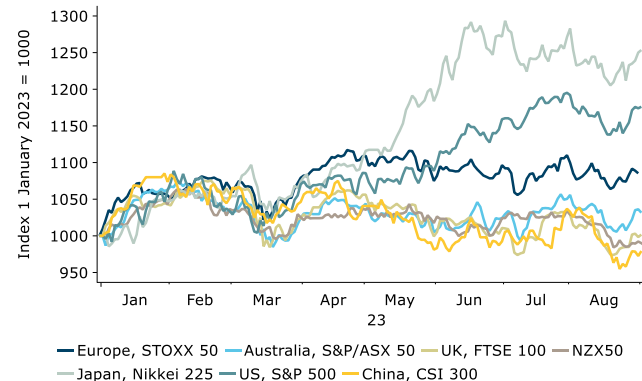
Source: RBNZ, U.S. Department of Treasury, Macrobond, ANZ Research

### Credit spreads: worth watching



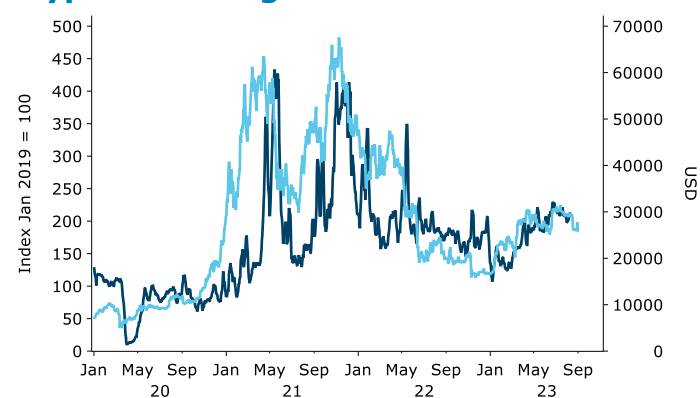
Source: U.S. Department of Treasury, Bloomberg, Macrobond, ANZ Research

### Global equities: hoping for soft landing



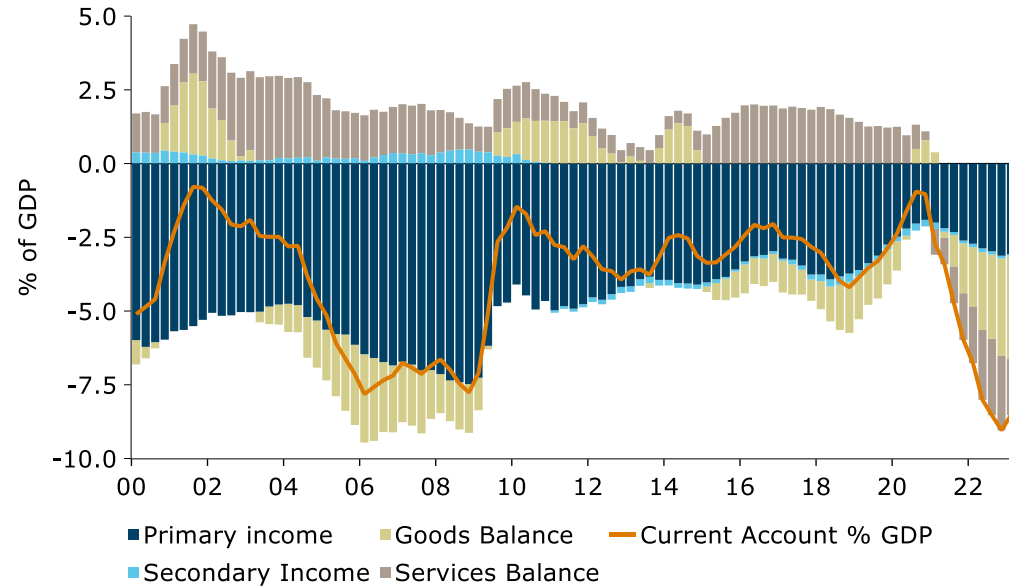
Source: STOXX, S&P Global, FTSE, Nikkei Inc., Bloomberg, Macrobond, ANZ Research

### Crypto: refusing to die



Source: Macrobond, Bloomberg, ANZ Research

## Current account deficit



Source: Stats NZ, Macrobond, ANZ Research

- The recession we need to have?
- It's not just inflation that is indicating that we need to stop living beyond our means.
- Could lead to a harsh adjustment via much weaker currency, much higher rates.

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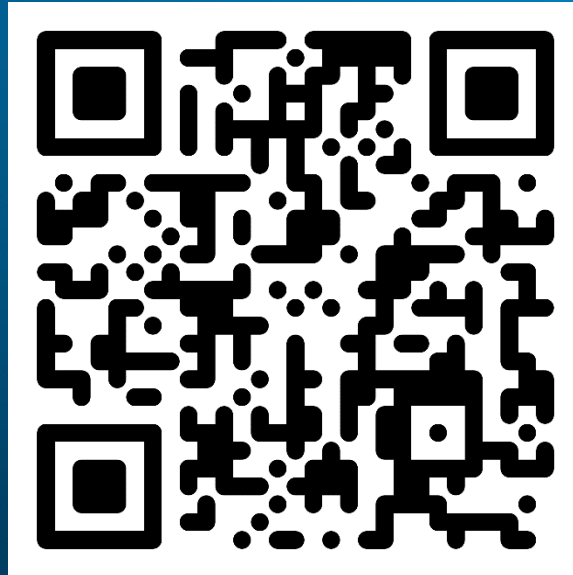
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Last updated: 18 April 2023

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