



Mōhua

# Weekly Economic Commentary.

## Shifting foundations.

We have updated our economic forecasts to reflect the housing policy changes announced by the Government last month. We now expect house prices to flatten off over the rest of this year, with a gradual decline in the following years as longer-term interest rates rise. This has implications for spending, activity and inflation, and will further delay the timing of OCR hikes.

The changes to the tax treatment of property investors are perhaps the most meaningful intervention into the housing market in decades. In particular, removing investors' ability to deduct mortgage interest costs from their taxable income will significantly tilt the playing field away from highly-leveraged investors and towards homebuyers and cashed-up investors. Demand from the latter two groups will now determine where house prices (and rents) settle.

At current mortgage rates, these buyers' willingness to pay is probably not too far from recent sale prices. In many cases the affordability challenge for first-home buyers hasn't been the size of the mortgage repayments, but the difficulty of saving a large enough deposit while prices continue to run away on them.

For that reason, we expect a flattening-out of house prices, rather than a substantial fall, in the near term. That is,

however, a sizeable downgrade compared to our previous forecasts, where we expected a further 20% upside for prices over the next two years. That downgrade in turn has implications for our wider economic forecasts.

We now expect that household spending (which accounts for around 60% of total economic activity) will recover more gradually than previously assumed. A weaker house price track will also have a dampening impact on residential construction, as developers may be reluctant to build into a slowing market. However, this drag is likely to be more modest, and will depend on what the Government decides about making interest costs deductible on new builds for a certain period.

The effects are not all negative for domestic demand. The housing changes are likely to reduce the demand for credit, which suggests a lower neutral interest rate (that is, the rate



that balances loan supply and demand). Lower borrowing rates would encourage some ‘crowding in’ of business investment over time.

Overall, though, the housing changes come on top of an economy that was already running below its full capacity. The shortfall is largely due to the closure of the international border and the loss of international tourism, and this has been particularly acute over the summer months.

The confirmation last week of a ‘travel bubble’ with Australia will be a welcome development for some local businesses, but the net impact on GDP is likely to be muted as we see a bounce in both inflows and outflows of tourist spending. A wider reopening of the borders, and a more complete rebound in activity, is not likely to happen until next year, once the Covid-19 vaccination programme is substantially completed.

The downgrade to our activity outlook means we expect it will take even longer for the Reserve Bank to achieve its inflation and employment goals on a sustained basis. We previously had no OCR hikes until early 2024; we have now pushed that out to early 2025. Longer-term interest rates will rise long before then, pulled higher by global forces, but holding the OCR near zero will help to stem the tide.

While the recent developments for the New Zealand economy have been on the downside, we don’t expect any significant change in the Reserve Bank’s stance at its Monetary Policy Review (MPR) on Wednesday. Softer local news has been balanced out to some degree by a rapidly improving global outlook and growing concerns about cost and price pressures.

In its February *Monetary Policy Statement*, the RBNZ concluded that “meeting [its inflation and employment] requirements will necessitate considerable time and patience”. While it didn’t publish a forward projection for the OCR (and won’t at this week’s review either), the implication was that the OCR is unlikely to rise from its current level of 0.25% for a long time. And the RBNZ emphasised that it could go lower – even below zero – if conditions warranted. We expect that message to be more or less repeated this week, which would be broadly neutral for financial markets.

The Government’s housing policy changes are probably less significant for the RBNZ’s view than for ours. The RBNZ’s forecasts in February were already on the more conservative side, with house price growth expected to cool rapidly from the second half of this year. Our updated house price forecast is only a moderate downside surprise relative to that view.

Meanwhile, inflation is becoming a hot topic again, both here and overseas. Anecdotes and business surveys reveal growing concern about rising prices, driven by factors such as disruptions to global supply chains and a jump in shipping costs. The RBNZ is already braced for a spike in inflation in the near term, with annual inflation forecast to reach 2.5% by the middle of this year, and not much has happened since February that would warrant revising that forecast even higher. However, inflation expectations are also on the rise, reflecting concerns that the recent price pressures could be longer lasting.

**Michael Gordon**, Acting Chief Economist

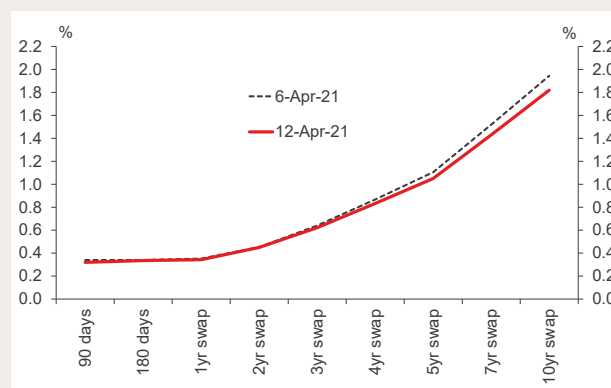
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## Fixed vs Floating for mortgages.

We expect that floating rates, and shorter fixed-term rates, will be stable over the coming months. The Reserve Bank will not respond to a temporary spike in inflation. Longer-term fixed rates may rise sooner, in response to a large increase in wholesale fixed rates over the past few months.

We expect mortgage rates to rise over the course of the coming years. Based on our forecasts, taking a longer-term fixed rate (from three years to five years) will prove less expensive for borrowers than taking a short-term rate now and refinancing later.

**NZ interest rates**



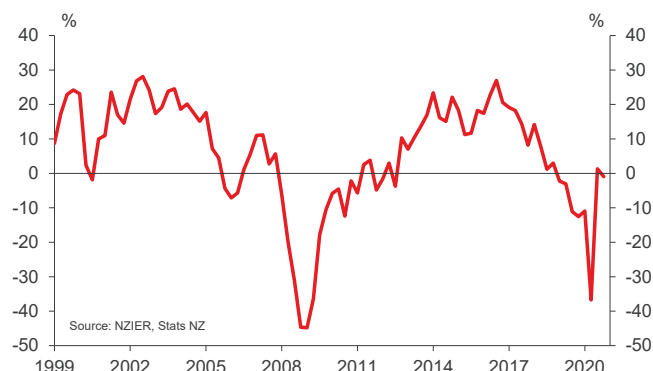
# The week ahead.

## NZ Q1 NZIER Quarterly Survey of Business Opinion

**Apr 13, Domestic Trading Activity last: -0.9**

- Business confidence rose in the December quarter with most indicators back at pre Covid levels and inflationary pressures emerging. Industries with a larger domestic focus fared better than those more exposed to international tourism.
- March is likely to have seen a dip in business confidence as New Zealand briefly returned to higher Alert Levels and the Government announced major interventions in the housing market. These changes are likely to be a drag on house prices and confidence.
- The survey's pricing gauges will be worth watching, with supply disruptions and shortages of some goods pushing costs of production and output prices higher.

## QSBO domestic trading activity (past 3 mths)

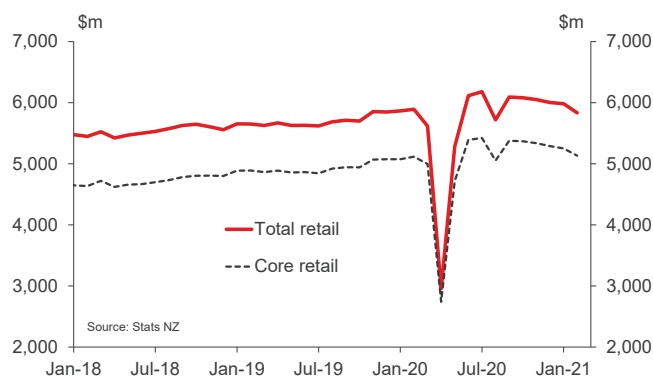


## NZ March Retail Card Spending

**Apr 13, Last: -2.5%, Westpac f/c: -0.2%**

- Retail spending fell by 2.5% in February. Spending was dampened by the dialling up of Alert Levels in the middle of the month. In addition, the absence of international tourists during the usual peak season has been a drag.
- We expect a modest -0.2% fall in spending in March. Earlier in the month, the Covid Alert level was dialled up for around 12 days. That will limit any lift in spending after February's fall.

## Retail card spending

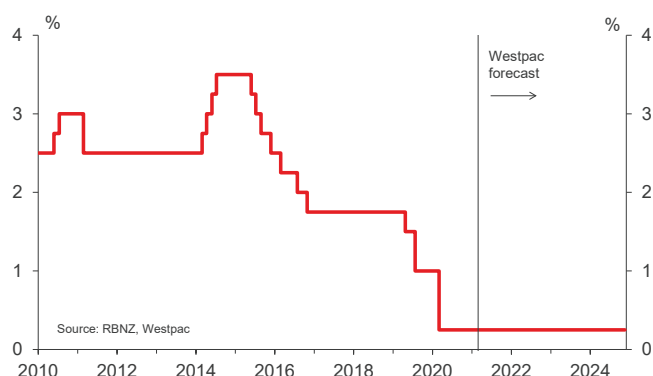


## NZ RBNZ Monetary Policy Review

**Apr 14, Official Cash Rate - last: 0.25%, Westpac f/c: 0.25%, Mkt: 0.25%**

- We expect no change in monetary policy settings at the upcoming review with the OCR to be held at 0.25% for the foreseeable future.
- A softer than expected starting point for the New Zealand economy will be balanced against a rapidly improving global outlook.
- The Government's housing policy announcement last month will only have a moderate impact on the RBNZ's house price forecasts, which were already on the conservative side.
- The RBNZ is already braced for a near-term spike in inflation. However, this is expected to be temporary, and the RBNZ will reiterate that a sustained return to its inflation and employment goals is a considerable time away.

## RBNZ Official Cash Rate



## The week ahead.

### NZ March REINZ house sales

**Apr 16 (TBC), Sales last: -3.2%, Prices last: +21.5%yr**

- March saw a watershed moment in New Zealand's housing market with the Government announcing significant changes to the tax treatment of rental properties. Over time these changes will have a significant dampening impact on house price growth.
- The Government's new housing policies were announced on 23 March. With strong demand earlier in the month, March is still likely to record another month of solid price gains. We also expect to see strength in sales.

### REINZ house prices and sales

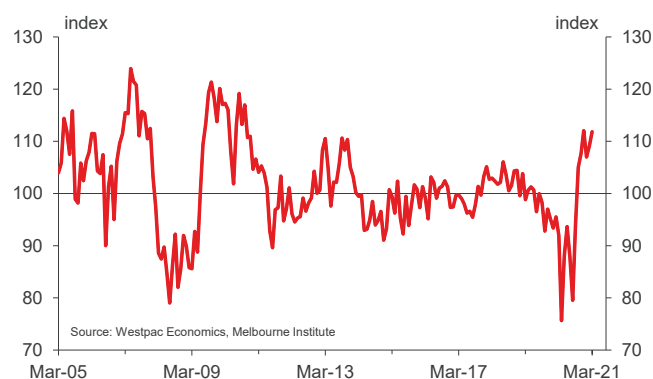


### Aus Apr Westpac-MI Consumer Sentiment

**Apr 14, Last: 111.8**

- Sentiment rose 2.6% to 111.8 in March to be just 0.2pts below the ten-year high set in Dec. Australia's continued success in containing COVID-19, the promise of vaccine rollouts bringing an end to the pandemic, and economic support from government policies have all contributed to the sustained lift.
- The Apr survey is in the field over the week to Apr 10. The last month has been less upbeat. Around COVID, yet another state 'mini-lockdown', this time in Brisbane, has highlighted that sudden virus-related disruptions are still a risk. Australia's vaccine rollout is also running well behind schedule and struck a major problem late in the week when AstraZeneca advised against vaccinating those aged under 50 due to risks of rare but serious side-effects. News around the economy has been more positive – a strong Feb labour force report in particular – but there remains unease about impacts from the expiring JobKeeper scheme. Surging house prices may also be a factor for sentiment although this is often a 'wedge' issue for consumers due to affordability and sustainability concerns.

### Aus Consumer Sentiment Index

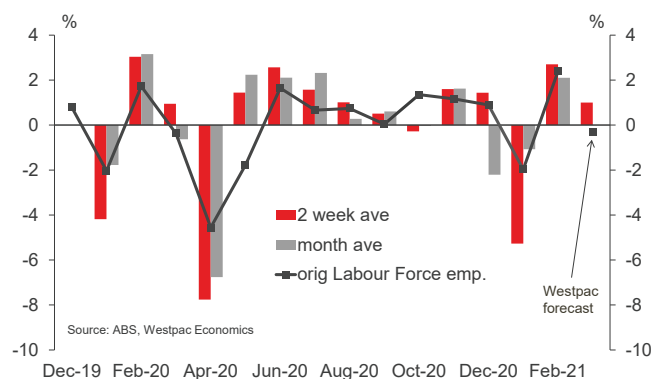


### Aus Mar labour force survey, employment change

**Apr 15, Last 88.7k; WBC f/c: 32k, Mkt f/c 35.ok, range: 10.ok to 65.ok.**

- February was cracking result with total employment rising 88.7k which were all full-time. Part-time employment was as good as flat (-0.5k).
- There was the strong recovery in hours worked, +6.1%mt, from the -4.9% collapse in January, for hours worked to now be up 0.2% in the year. Total employment is up 0.1%yr to February. As expected, NSW had a recovery from the January closures (+42.0k) with Victoria continuing the robust momentum from the reopening of its economy in late 2020 (+26.6k.)
- Leading indicators of employment, such as weekly payrolls, job vacancies and the various business surveys all suggest labour demand continued to strengthen through March and into April. As such we see upside risks to our +32k forecast.

### Aus Payrolls vs Labour Force Employment



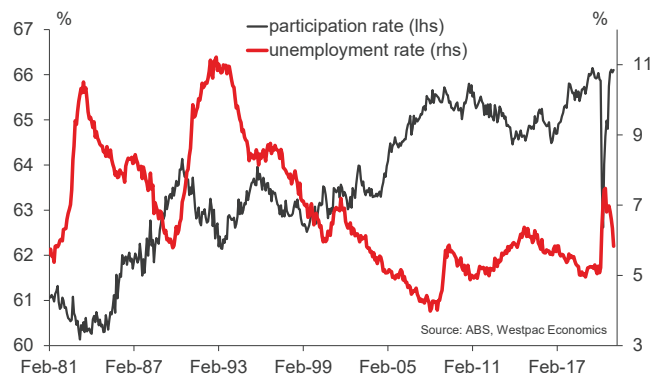
## The week ahead.

### Aus Mar labour force survey, unemployment %

**Apr 15, Last 5.8%; WBC f/c: 5.8%,  
Mkt f/c 5.7%, range: 5.6% to 5.9%.**

- With a flat participation rate of 66.1% and a robust 88.7k gain in employment unemployment fell to 5.8% from 6.3%.
- Unemployment is 0.6ppt higher than it was in March (pre COVID) and with employment now on par with March, higher unemployment is explained by the 0.2ppt increase in participation. For the same level of employment there are more people looking for work in Feb 2021 than Mar 2020.
- In Feb male participation lifted 0.2ppt while female participation gained 0.3ppt. Female unemployment fell 0.7ppt in Feb to 5.5% while male unemployment fell 0.4ppt to 6.1%.
- Rising participation is muting the improvement in unemployment. A 0.1ppt increase in participation to 66.2% will hold the unemployment rate at 5.8% with a 32k gain in employment.

### Aus Participation recovered with employment

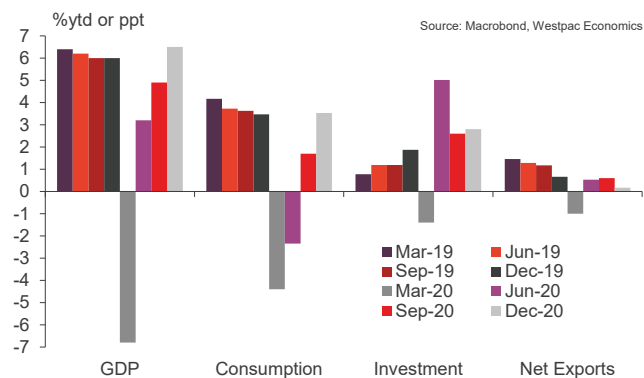


### China Q1 GDP

**Apr 16, last: 6.5%yr, WBC: 19.1%yr**

- China's economy went from strength-to-strength in 2020, registering annual growth of 6.5%yr despite the ill effects of the pandemic in Q1, when annual growth fell to -6.8%yr.
- Annual growth outcomes for the first half of 2021 will be flattered by base effects. Still, underlying a 19%yr gain at March 2021 will also be a circa 5% annualised gain quarter on quarter, fuelled by broad-based strength in investment as well as demand from the consumer.
- In the remainder of 2021, the benefit of the base effect will fade. But robust quarter-on-quarter gains are expected to continue, seeing annual growth at 5.8% come December -- a touch above our estimate of trend.
- Note though, risks to the Q1 outcome are to the downside given the sporadic incidence of the virus in Q1 that saw travel restrictions re-introduced over the LNY holidays.

### China GDP



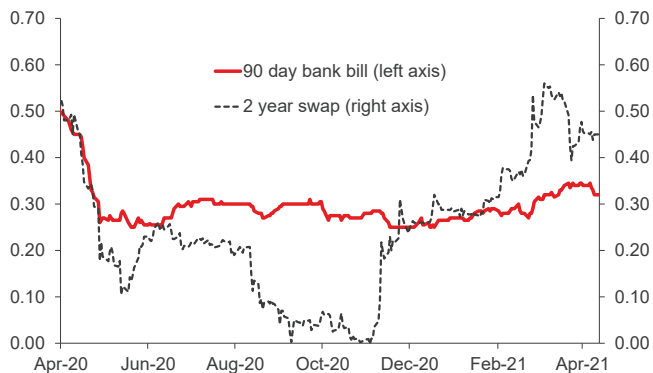


## New Zealand forecasts.

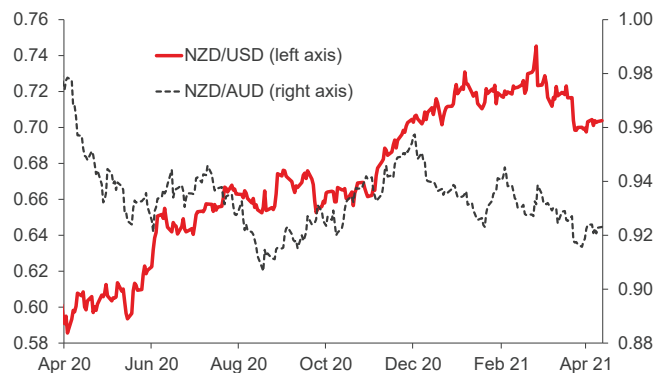
Economic forecasts	Quarterly				Annual			
	2020	2021						
% change	Dec (a)	Mar	Jun	Sep	2019	2020	2021f	2022f
GDP (Production)	-1.0	-0.4	1.8	0.4	2.4	-2.9	3.9	4.0
Employment	0.6	0.1	0.1	0.4	1.3	0.7	1.0	2.6
Unemployment Rate % s.a.	4.9	5.0	5.1	5.0	4.1	4.9	4.9	4.2
CPI	0.5	0.8	0.6	0.7	1.9	1.4	2.4	1.3
Current Account Balance % of GDP	-1.0	-1.4	-2.1	-2.5	-3.3	-1.0	-2.5	-2.2

Financial forecasts	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22
Cash	0.25	0.25	0.25	0.25	0.25	0.25
90 Day bill	0.35	0.35	0.35	0.35	0.35	0.35
2 Year Swap	0.45	0.45	0.45	0.45	0.45	0.45
5 Year Swap	1.00	1.00	1.00	1.05	1.10	1.15
10 Year Bond	1.80	1.85	1.90	1.95	2.00	2.10
NZD/USD	0.72	0.73	0.74	0.76	0.76	0.75
NZD/AUD	0.91	0.91	0.90	0.89	0.89	0.89
NZD/JPY	78.5	80.3	82.1	85.1	84.4	83.3
NZD/EUR	0.60	0.60	0.60	0.61	0.60	0.59
NZD/GBP	0.51	0.52	0.52	0.54	0.54	0.53
TWI	74.5	74.9	75.0	76.1	75.8	74.7

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 12 April 2021

Interest rates	Current	Two weeks ago	One month ago
Cash	0.25%	0.25%	0.25%
30 Days	0.26%	0.26%	0.26%
60 Days	0.29%	0.30%	0.29%
90 Days	0.32%	0.34%	0.32%
2 Year Swap	0.45%	0.43%	0.53%
5 Year Swap	1.05%	1.02%	1.18%

NZ foreign currency mid-rates as at 12 April 2021

Exchange rates	Current	Two weeks ago	One month ago
NZD/USD	0.7038	0.6992	0.7177
NZD/EUR	0.5917	0.5927	0.6008
NZD/GBP	0.5130	0.5068	0.5156
NZD/JPY	77.20	76.69	78.23
NZD/AUD	0.9231	0.9156	0.9252
TWI	74.28	73.71	75.16

## Data calendar.

		Last	Market median	Westpac forecast	Risk/Comment
<b>Mon 12</b>					
Eur	Feb retail sales	-5.9%	1.3%	-	Extension of lockdowns into April will constrain spending.
UK	Feb trade balance £bn	-1630	-	-	Falling imports saw trade deficit narrow in Jan.
US	Mar monthly budget statement	-310.9	-	-	To widen considerably as new waves of stimulus come online.
	Fedspeak	-	-	-	FOMC's Harker; Daly; and Mester, Bostic & Rosengren.
<b>Tue 13</b>					
NZ	Q1 Quarterly Survey of Bus Opinion	-0.9	-	-	Policy changes and lockdowns may weigh on confidence.
	Mar card spending	-2.5%	-	-0.2%	Lockdowns and a lack of tourists weighing on spending.
Aus	Mar NAB business survey	15	-	-	Business conditions lifted to be at highest level since mid-2018.
	27 Mar ABS Weekly Payrolls	-	-	-	A gauge of the labour force before the end of JobKeeper.
Chn	Mar trade balance USDbn	78.17	52.00	-	Surging exports have supported the surplus.
Eur	Apr ZEW survey of expectations	74	-	-	Expectations have recovered to pre-Covid levels.
US	Mar NFIB small business optimism	95.8	98.0	-	Will be buoyed by stimulus and the pace of vaccinations.
	Mar CPI	0.4%	0.5%	-	Looking for a temporary lift over coming months.
<b>Wed 14</b>					
NZ	Feb net migration	631	-	-	Net inflows remain very low due to border closures.
	RBNZ monetary policy review	0.25%	0.25%	0.25%	RBNZ to highlight that ongoing stimulus is needed.
Aus	Apr Westpac-MI Consumer Sentiment	111.8	-	-	Near 10yr high in Mar. Brisbane lockdown, JKP end to impact.
Eur	Feb industrial production	0.8%	-	-	Output has responded to strong external demand.
US	Mar import price index	1.3%	0.3%	-	Fuel import prices have risen significantly in recent months.
	Federal Reserve's Beige book	-	-	-	An update on conditions across the Fed districts.
	Fed Chair Powell	-	-	-	Will speak to the Economic Club of Washington.
	Fedspeak	-	-	-	Vice Chair Clarida; Williams; and Bostic to speak.
<b>Thu 15</b>					
NZ	Mar food price index	-0.9%	-	0.8%	Prices have eased since Covid disruptions in mid-2020.
Aus	Mar employment	88.7k	35k	32k	Vacancies, weekly payrolls & business surveys all point to...
	Mar unemployment rate	5.8%	5.7%	5.8%	...robust labour demand, employment risks are to the upside.
	Apr MI inflation expectations	4.1%	-	-	Rising petrol prices are a risk here but what of housing costs?
US	Initial jobless claims	-	-	-	Have been choppy of late, but downtrend still in place.
	Mar retail sales	-3.0%	5.2%	6.5%	Retail sales and industrial production are set to rebound...
	Mar industrial production	-2.2%	3.0%	-	... after softer prints in Feb due to weather disruptions.
	Apr Fed Empire state index	17.4	16.3	-	Pricing power, input costs and new orders...
	Apr Philly Fed index	51.8	40.0	-	... have been a major driver of regional mfg surveys.
	Feb business inventories	0.3%	0.5%	-	Should continue to accumulate as economy reopens.
	Apr NAHB housing market index	82	84	-	Has eased off Nov record high, but still historically elevated.
	Feb total net TIC flows	106.3	-	-	Jan rise driven by increases in net holdings in Chn and Jpn.
	Fedspeak	-	-	-	Vice Chair Clarida; Bostic; Daly; and Mester to speak.
<b>Fri 16</b>					
NZ	Mar REINZ house prices %yr	21.5%	-	-	Due this week. Firm conditions early in the month...
	Mar REINZ house sales	7.6%	-	-	...but policy changes in late March will be a drag.
	Mar manufacturing PMI	53.4	-	-	Has been firming, but supply disruptions may be a drag.
Chn	Q1 GDP %yr	6.5%	18.2%	19.1%	A year on from the pandemic's nadir...
	Mar industrial production ytd %yr	35.1%	28.1%	-	... China's economy has not only re-couped its losses...
	Mar fixed asset investment ytd %yr	35.0%	27.0%	-	... but built a strong foundation for a long and robust...
	Mar retail sales YTD %yr	33.8%	32.5%	-	... new growth cycle.
Eur	Feb trade balance £bn	24.2	-	-	Europe's exporters responding to strong demand from Asia.
US	Mar housing starts	-10.3%	13.7%	-	Housing starts disrupted by weather in Feb...
	Mar building permits	-10.8%	1.5%	-	... but permits are sitting around a 15-year high.
	Apr Uni. of Michigan sentiment	84.9	88.8	-	Relaxation of restrictions; stimulus; and vaccines supportive.

## International forecasts.

Economic Forecasts (Calendar Years)	2017	2018	2019	2020f	2021f	2022f
<b>Australia</b>						
Real GDP %/yr	2.4	2.8	1.9	-2.4	5.2	3.6
CPI inflation %/yr	1.9	1.8	1.8	0.9	2.6	2.1
Unemployment rate %	5.5	5.0	5.2	6.8	5.7	5.2
Current account % of GDP	-2.6	-2.1	0.7	2.5	3.7	1.8
<b>United States</b>						
Real GDP %/yr	2.3	3.0	2.2	-3.5	6.0	4.1
CPI inflation %/yr	2.1	2.4	1.9	1.2	2.2	2.1
Unemployment rate %	4.4	3.9	3.7	8.1	5.3	4.3
Current account % of GDP	-2.3	-2.3	-2.6	-2.5	-2.4	-2.4
<b>Japan</b>						
Real GDP %/yr	1.7	0.6	0.3	-4.8	2.7	2.2
<b>Euro zone</b>						
Real GDP %/yr	2.6	1.9	1.3	-6.6	4.2	3.9
<b>United Kingdom</b>						
Real GDP %/yr	1.7	1.3	1.4	-9.9	5.5	5.5
<b>China</b>						
Real GDP %/yr	6.9	6.7	5.8	2.3	10.0	5.7
<b>East Asia ex China</b>						
Real GDP %/yr	4.7	4.4	3.7	-2.4	5.0	4.9
<b>World</b>						
Real GDP %/yr	3.8	3.6	2.8	-3.3	5.9	4.5
Forecasts finalised 9 April 2021						

Interest rate forecasts	Latest	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
<b>Australia</b>								
Cash	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
90 Day BBSW	0.04	0.02	0.02	0.02	0.04	0.06	0.08	0.10
10 Year Bond	1.71	1.85	1.95	2.10	2.20	2.30	2.40	2.50
<b>International</b>								
Fed Funds	0.125	0.125	0.125	0.125	0.125	0.125	0.125	0.125
US 10 Year Bond	1.63	1.75	1.85	2.00	2.10	2.20	2.30	2.40

Exchange rate forecasts	Latest	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
AUD/USD	0.7660	0.79	0.80	0.82	0.85	0.85	0.84	0.82
USD/JPY	109.27	109	110	111	112	111	111	110
EUR/USD	1.1920	1.20	1.21	1.23	1.25	1.26	1.27	1.27
GBP/USD	1.3749	1.40	1.40	1.41	1.41	1.41	1.42	1.42
USD/CNY	6.5509	6.40	6.30	6.20	6.15	6.10	6.05	6.00
AUD/NZD	1.0842	1.10	1.10	1.11	1.12	1.12	1.12	1.11



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