



# Weekly Economic Commentary.

## We have lift-off.

The Delta outbreak has disrupted economic activity and is set to remain a drag on growth for some time yet. But as we detail in our latest Economic Overview, the New Zealand economy as a whole remains in good health, and we expect a return to firm levels of activity in 2022. Behind the scenes, policy settings are shifting, notably with the OCR set for lift-off.

As 2021 draws towards a close, New Zealand is continuing to grapple with the impacts of August's outbreak of the Delta variant. We estimate that GDP fell by 6% in the September quarter. And although Alert Levels have been gradually dialled down over the past few months, health restrictions have continued to weigh on activity in some parts of the economy.

While the Delta outbreak has been a significant drag, underlying economic conditions have actually remained resilient. In fact, through the September quarter, when restrictions were at their most prohibitive, employment levels rose by 2% and the unemployment rate equalled its record low.

Looking to 2022, the economic signs remain positive. There is a large amount of construction work planned across the country with a record 47,000 new dwellings consented over the past year. Similarly, feedback from businesses in the

manufacturing sector indicates that demand has remained firm. And prices for our key agricultural exports have hit record highs.

With resilience in the underlying economy, we expect that unemployment will remain low over the coming quarters and that economic activity will rise back to firm levels as health restrictions are eased. However, it won't always be smooth sailing. With infection numbers continuing to rise, health restrictions are likely to be wound back only gradually, and there may still be periods where restrictions are tightened. Accordingly, we don't expect economic output will retrace its pre-Delta levels until mid-2022.

In addition, prior to the latest outbreak the economy was grappling with a cocktail of supply disruptions, material shortages and rising costs. Those conditions are likely to remain a feature of the economic landscape well into the new year.



While we expect a return to firm economic conditions over the coming year, behind the scenes, key policy settings are now changing.

First of these is the Government's approach to the Covid outbreak itself. The Government has signalled an end to alert levels and a move to a 'traffic light' system on 15 December. While the finer details are still to be announced, this would involve public health measures, like social distancing requirements, being dialled up or down as necessary to manage the pressure on the healthcare system, but without resorting to lockdowns in the future. A key feature of this new framework is that there will be more restrictions on the unvaccinated, while households and businesses that make use of vaccination certificates will be subject to fewer restrictions.

The shift to the traffic light system signals an important change in the economic landscape for many businesses, especially those in close-contact industries such as hospitality. As we've seen over the past year, health restrictions and social distancing requirements do dampen demand to some degree, and there's a chance that restrictions could be in place for an extended period.

However, the resulting drag on demand from such restrictions is much less severe than when the economy has been in Alert Levels 3 or 4. Furthermore, with a growing proportion of the country fully vaccinated, fewer households will be subject to strict activity restrictions if case numbers flare up again.

It was always going to be the case that once the vaccination programme was sufficiently advanced, New Zealand would need to determine how to live with Covid over the longer term. Consequently, although the current outbreak has forced the country to confront these issues sooner than otherwise, the change in approach from the Government has not meaningfully altered our outlook for the economy in 2022 and beyond.

In contrast our monetary views have changed. Interest rate reductions since the start of the pandemic have played a pivotal role in supporting New Zealand's recovery, with much of the resulting boost to demand coming through the household sector. Combined with other support measures and firmness in the labour market, those developments have super-charged household spending as well as the housing market over the past year. The record low unemployment rate and surging annual inflation (to 4.9% in the September quarter) are two clear examples of this strength.

Now clearly, the economy can stand on its own two legs, and if anything, demand needs to be cooled down. On this basis, we expect that the RBNZ will continue to raise the OCR over the coming years, reaching a cyclical peak of 3% in mid-2023.

The resulting increases in borrowing costs will reverberate through all parts of the economy, with the current strong economic conditions set to give way to a period of modest economic growth through 2023 and 2024. A cooling in the housing market and the subsequent slowing in the rapid increases in household wealth will also dampen household demand. As mortgage rates rise, we expect a substantial slowing in house price growth over the coming months, turning to modest price declines by the second half of 2022. That slowdown will likely be compounded by a tightening in lending conditions, with the RBNZ currently consulting on debt-to-income limits on mortgage lending.

In short, record low interest rates are now behind us, and a period of more normal rates beckons. And as the RBNZ attempts to cool the hot New Zealand economy, the challenge will be to engineer a soft landing.

**Nathan Penny**, Senior Agri Economist

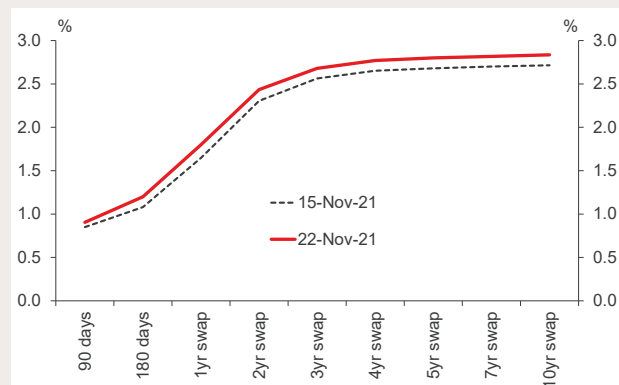
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## Fixed vs floating for mortgages.

We expect the Reserve Bank to increase the OCR further at its upcoming reviews, reaching a peak of 3% by mid-2023.

Based on these OCR forecasts, we think there is value in extending fixed-rate terms as far out as three years. Longer terms (out to five years) don't offer additional value, though they may be suitable for borrowers who value more certainty in their repayments.

**NZ interest rates**



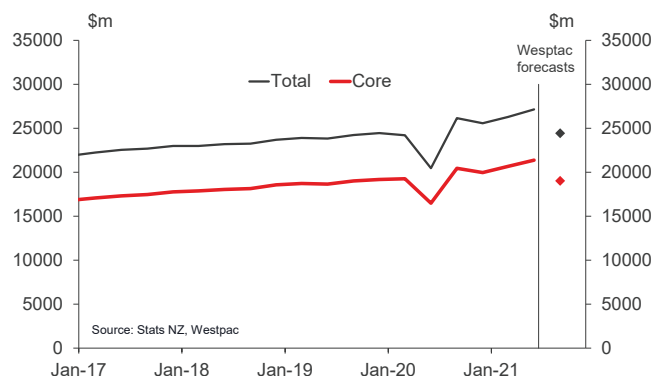
# The week ahead.

## NZ Q3 retail spending volumes

**Nov 23, Last: +3.3%, Westpac f/c: -10.0%**

- The Delta lockdown has hit retail spending hard. We expect a 10% fall in volumes over the quarter.
- Strict lockdown restrictions were imposed in mid-August, which saw spending fall sharply. Although the Alert Level was wound back over the quarter, strict restrictions remained in place in Auckland and overall spending levels remained subdued.
- While spending volumes have taken a step down in recent months, inflation pressures have remained strong, with continued increases in transport costs and ongoing disruptions to global supply chains. As a result, we expect another strong rise in retail prices, despite the fall in spending volumes.

## NZ quarterly retail spending (volumes)

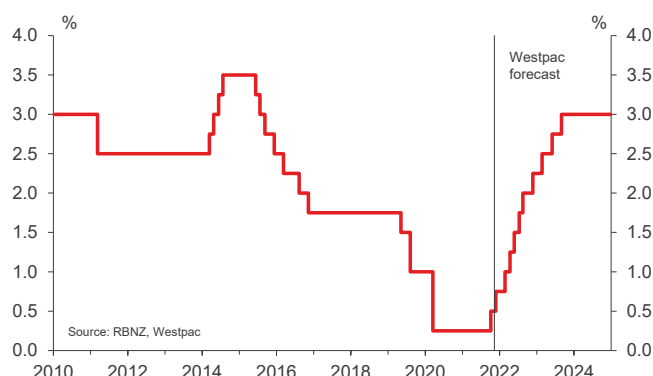


## RBNZ Monetary Policy Statement

**Nov 24, last: 0.50%, WBC f/c: 0.75%, Market f/c: 0.75%**

- We expect the Reserve Bank to lift the Official Cash Rate by 25 basis points to 0.75%. Recent data has reinforced that demand in the New Zealand economy is running hot and that inflation pressures are building.
- We expect the RBNZ's projections to show a peak cash rate of close to 3% in the coming years, similar to our own forecast. That tightening profile could be comfortably achieved in 25bp increments. But under the RBNZ's own criteria, it's possible to make the case for a 50bp move.
- Market pricing has been around 30-40% for a 50bp hike next week, so there will be some market volatility on the day regardless of which way the RBNZ goes.

## RBNZ Official Cash Rate

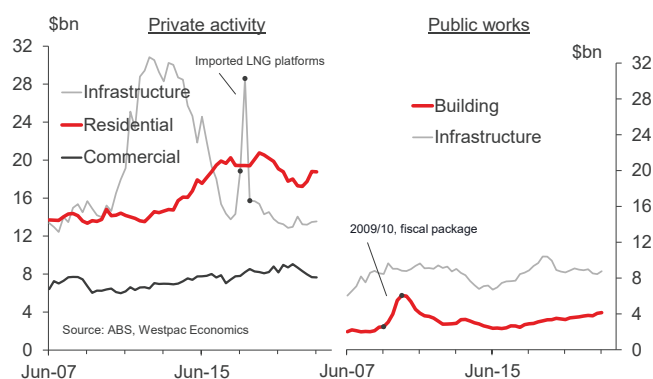


## Aus Q3 Construction work

**Nov 24, Last: 0.8%, WBC f/c: -3.2%  
Mkt f/c: -3.0%, Range: -6.0% to +0.5%**

- Construction work is coming off gains of 2.4% and 0.8% for the opening quarters of 2021, boosted by considerable policy stimulus.
- The recovery was interrupted in Q3 by the delta lockdowns. Recall that the initial lockdown in 2020 was nationwide, while the latest round was centred in NSW and Victoria, with some spill-over to other areas. Restrictions for construction were more stringent this time - with the industry shutdown for 2 weeks in NSW and workers from "areas of concern" limited in their ability to leave their local area.
- We anticipate a 3.2% drop in total construction work during the period. That is on a par with the decline in hours worked across the economy, nationwide during Q3.
- Sizeable falls in building work (residential and non-residential) are likely, potentially in the order of 6%. Private infrastructure activity and public works may be somewhat more resilient.

## Aus construction work by segment



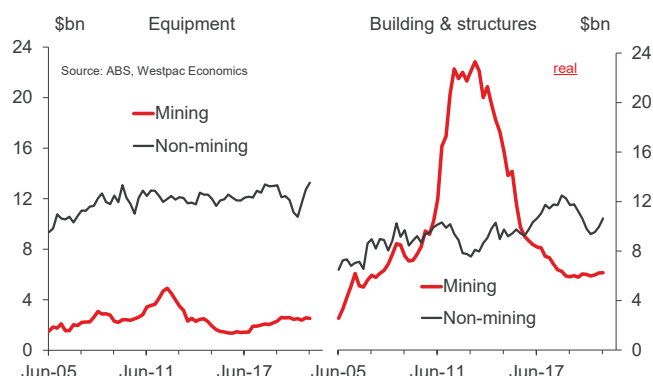
# The week ahead.

## Aus Q3 private business capex

**Nov 25, Last: 4.4%, WBC f/c: -4.8%**  
**Mkt f/c: -2.4%, Range: -5.0% to +1.5%**

- Businesses restored capex spending over the past three quarters (2020 Q4 to 2021 Q2), up by 14% (including a 4.4% rise in Q2). This strong rebound was boosted by considerable policy stimulus, including generous tax incentives.
- That was after firms cut investment expenditure during the initial lockdown, down by 9.7% over the opening three quarters of 2020.
- For Q3, we anticipate a sizeable dip in capex, in the order of 4.8%.
- This includes a 6% decline in spending on equipment, a fall that would match that in the June quarter 2020 (which followed a 2% drop in Q1 2020). The extended delta lockdowns represented a considerable disruption in NSW and Victoria. Building & structures are also likely to decline, with an anticipated fall of around 3.5%.

## Aus capex: by industry by asset

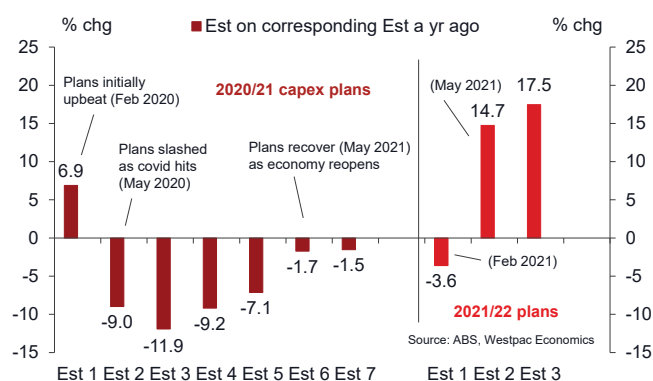


## Aus 2021/22 capex plans

**Nov 25, Last: Est 3 \$127.7bn**

- Business capex plans have been revised significantly since the initial onset of Covid - first down and then up. Initial estimates of capex plans for 2021/22 are positive. The rebound in activity (pre delta) and tax incentives are the key drivers. Est 3 for 2021/22 is \$127.7bn, up 17.5% on Est 3 a year ago - flattered by weak base effects.
- This update, surveyed in October and November, will include Est 4. Anecdotes are that firms have generally not scaled back their capital expenditure plans during the delta lockdowns. However, the interruptions do mean that there have been delays - which will impact growth for 2021/22.
- With this in mind, we speculate that Est 4 may print at around \$131bn, representing a 2.5% upgrade on Est 3. This is a below par upgrade between Est 3 and Est 4, which on average is around 5%. An Est 4 of \$131bn is 13% above Est 4 of a year ago (a comparison still flattered by weak base effects).

## Aus capex plans: positive for 2021/22

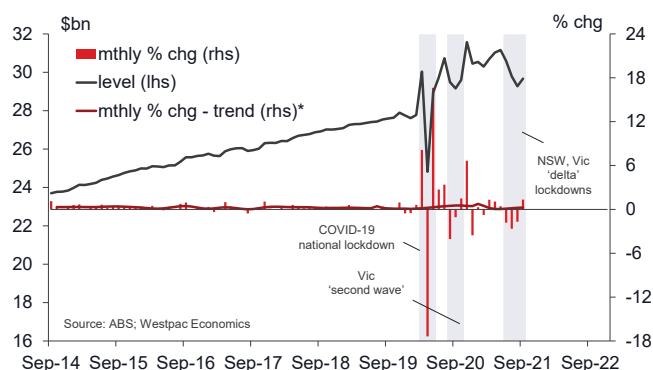


## Aus Oct retail trade

**Nov 26, Last: 1.3%, WBC f/c: 1.0%**  
**Mkt f/c: 2.5%, Range: 0.3% to 4.0% retail trade**

- Retail sales posted a 1.3% gain in Sep to be up 1.3%yr, albeit with annual growth flattered by base effects. The state breakdown showed a better than expected lift in NSW and strong gains in 'non lockdown' states that more than offset a sizeable decline in Vic.
- Our Westpac Card Tracker shows suggests retail activity continued to improve through Oct, albeit fairly gradually. However, the data understated the Sep retail gain, most likely due in part to a lift in cash spending in states that saw restrictions ease. The detail suggests there was another solid gain in NSW but more mixed conditions elsewhere - expenditure switching between retail and non retail a possible factor.
- On balance we expect Oct to show another solid 1% gain. Nov is shaping as a much bigger gain, possibly in the order of +3-4%mt.

## Aus monthly retail sales

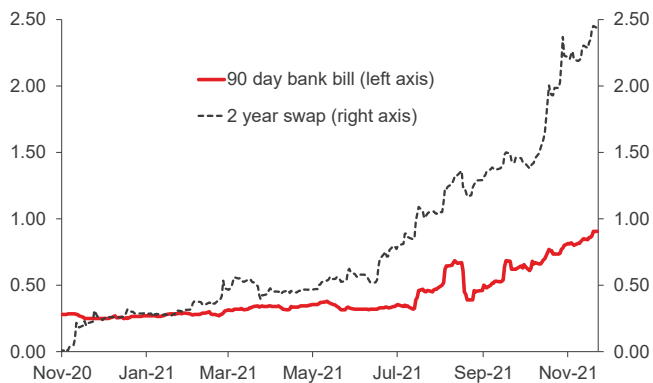


# New Zealand forecasts.

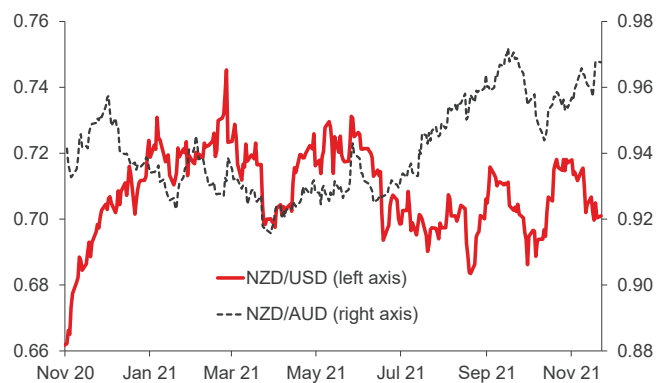
Economic forecasts	Quarterly				Annual			
	2021			2022				
% change	Jun (a)	Sep	Dec	Mar	2019	2020	2021f	2022f
GDP (Production)	2.8	-6.0	2.1	2.9	2.4	-2.1	3.8	4.6
Employment	1.0	2.0	0.0	0.2	1.2	0.6	3.5	0.5
Unemployment Rate % s.a.	4.0	3.4	3.8	3.7	4.0	4.8	3.8	3.5
CPI	1.3	2.2	0.6	0.8	1.9	1.4	5.1	2.7
Current Account Balance % of GDP	-3.3	-4.5	-5.5	-5.7	-2.9	-0.8	-5.5	-6.3

Financial forecasts	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Dec-23
Cash	0.75	1.00	1.50	2.00	2.25	2.50	2.75	3.00
90 Day bill	0.95	1.40	1.90	2.20	2.45	2.70	2.95	3.10
2 Year Swap	2.30	2.55	2.75	2.90	2.95	3.00	3.00	2.90
5 Year Swap	2.60	2.80	2.95	3.05	3.10	3.15	3.15	3.10
10 Year Bond	2.70	2.80	2.85	2.90	3.00	3.00	3.00	2.95
NZD/USD	0.71	0.72	0.73	0.74	0.74	0.74	0.74	0.73
NZD/AUD	0.95	0.95	0.95	0.95	0.95	0.94	0.93	0.94
NZD/JPY	79.5	80.6	82.5	83.6	84.4	84.4	85.1	84.7
NZD/EUR	0.60	0.60	0.61	0.63	0.63	0.63	0.64	0.63
NZD/GBP	0.51	0.52	0.52	0.52	0.52	0.53	0.53	0.53
TWI	74.6	75.2	75.9	76.6	76.4	76.3	76.0	75.3

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 22 November 2021

Interest rates	Current	Two weeks ago	One month ago
Cash	0.50%	0.50%	0.50%
30 Days	0.83%	0.68%	0.56%
60 Days	0.87%	0.74%	0.65%
90 Days	0.91%	0.80%	0.74%
2 Year Swap	2.44%	2.20%	1.99%
5 Year Swap	2.80%	2.58%	2.38%

NZ foreign currency mid-rates as at 22 November 2021

Exchange rates	Current	Two weeks ago	One month ago
NZD/USD	0.7010	0.7109	0.7166
NZD/EUR	0.6211	0.6154	0.6172
NZD/GBP	0.5210	0.5276	0.5207
NZD/JPY	79.83	80.67	81.50
NZD/AUD	0.9676	0.9615	0.9565
TWI	75.11	75.71	75.91



## Data calendar.

		Last	Market median	Westpac forecast	Risk/Comment
<b>Mon 22</b>					
Eur	Nov consumer confidence	-4.8	-5.2	-	Inflation is now a clear headwind for confidence.
US	Oct Chicago Fed activity index	-0.13	-	-	To provide a timely update on activity in the region.
	Oct existing home sales	7.0%	-1.4%	-	Modest pull-back likely after sharp Sep rise.
<b>Tue 23</b>					
NZ	Q3 real retail sales	3.3%	-11.0%	-10.0%	The dialling up of Alert levels has been a drag on spending.
Aus	RBA Head Dom. Markets Kohler	-	-	-	'Securities markets through the pandemic'.
	RBA Dep. Head Dom. Markets Brischetto	-	-	-	Panel. 'Transition to risk free rates, the future of BBSW'.
Eur	Nov Markit manufacturing PMI	58.3	57.5	-	Supply shortages and delta concerns will continue...
	Nov Markit services PMI	54.6	54.1	-	... to weigh on manufacturing and services growth.
UK	Nov Markit manufacturing PMI	57.8	57.4	-	Manufacturing and services have seen continued growth...
	Nov Markit services PMI	59.1	58.2	-	... but supply, delta and Brexit loom as headwinds.
US	Nov Markit manufacturing PMI	58.4	59.0	-	Manufacturing and services remain robust...
	Nov Markt services PMI	58.7	59.0	-	... despite ongoing supply and delta concerns.
	Nov Richmond Fed index	12	-	-	Surprise lift in Oct indicates a positive outlook for the region.
<b>Wed 24</b>					
NZ	RBNZ policy decision	0.50%	0.75%	0.75%	Higher rates needed to rein in demand-driven inflation.
Aus	Q3 construction work done	0.8%	-3.0%	-3.2%	Delta lockdowns disrupted activity in NSW & Victoria.
	RBA Assist. Gov Fin. Systems Bullock	-	-	-	Panel, on 'central bank digital currencies'.
	RBA Assist. Gov Fin. Systems Bullock	-	-	-	Panel, on 'the future of payments in Australia'.
US	Initial jobless claims	268k	-	-	Downtrend remains in place.
	Oct wholesale inventories	1.4%	-	-	Stocks being replenished as supply allows.
	Q3 GDP, annualised	2.0%	2.2%	-	Only a small revision expected in second estimate for Q3.
	Oct durable goods orders	-0.3%	0.2%	-	Expected to advance, centred on ex transportation segment.
	Oct core PCE deflator	0.2%	0.4%	-	Rising prices for energy and shelter and supply disruptions...
	Oct core PCE deflator, %yr	3.6%	4.1%	-	... have lifted PCE inflation to near 30-year highs.
	Oct personal spending	0.6%	0.9%	-	Robust gains across goods and services expected.
	Oct personal income	-1.0%	0.3%	-	Set to bounce back from the conclusion of fiscal support.
	Nov Uni. of Michigan sentiment	66.8	66.8	-	Final release for Nov; weakness in sentiment jars against activity.
	Oct new home sales	800k	801k	-	Expected to hold steady as supply hinders construction.
	FOMC November meeting minutes	-	-	-	Focus on discussion of inflation and post-taper pivot to rates.
<b>Thu 25</b>					
NZ	Oct trade balance \$m	-2171	-	-1280	Seasonal increase in agricultural exports narrows deficit somewhat.
Aus	Q3 private new capital expenditure	4.4%	-2.4%	-4.8%	Delta lockdowns disrupted / delayed investment spending.
	2020/21 capex plans, AUDbn	127.7	-	-	Capex plans positive. Risk of sub-par upgrade due to delays.
	Oct 30 Weekly payrolls	-0.2%	-	-	Reopening from delta lockdowns to boost employment.
US	Thanksgiving	-	-	-	Public holiday. Markets closed.
<b>Fri 26</b>					
NZ	Nov ANZ consumer confidence	98.0	-	-	Households continue to highlight concerns about the outlook.
Aus	Oct retail sales	1.3%	2.5%	1.0%	Steady lift as 'delta' reopening gathers momentum.
Eur	Oct M3 money supply %yr	7.4%	-	-	M3 growth has slowed through 2021 but liquidity remains ample.
US	Black Friday	-	-	-	Markets early close.

## International forecasts.


Economic Forecasts (Calendar Years)	2017	2018	2019	2020	2021f	2022f
<b>Australia</b>						
Real GDP %/yr	2.4	2.8	1.9	-2.4	3.0	5.0
CPI inflation %/yr	1.9	1.8	1.8	0.9	3.0	2.5
Unemployment rate %	5.5	5.0	5.2	6.8	4.9	3.7
Current account % of GDP	-2.6	-2.1	0.7	2.7	4.4	1.8
<b>United States</b>						
Real GDP %/yr	2.3	3.0	2.2	-3.5	5.6	4.0
CPI inflation %/yr	2.1	2.4	1.9	1.2	4.5	3.1
Unemployment rate %	4.4	3.9	3.7	8.1	5.4	4.2
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	2.3	2.7
<b>Euro zone</b>						
Real GDP %/yr	2.6	1.9	1.3	-6.6	4.9	4.4
<b>United Kingdom</b>						
Real GDP %/yr	1.7	1.3	1.4	-9.9	6.7	5.5
<b>China</b>						
Real GDP %/yr	6.9	6.7	5.8	2.3	8.5	5.7
<b>East Asia ex China</b>						
Real GDP %/yr	4.7	4.4	3.7	-2.4	3.8	4.9
<b>World</b>						
Real GDP %/yr	3.8	3.6	2.8	-3.3	5.4	4.6
Forecasts finalised 5 November 2021						

Interest rate forecasts	Latest	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Dec-23
<b>Australia</b>									
Cash	0.10	0.10	0.10	0.10	0.10	0.10	0.25	0.50	0.75
90 Day BBSW	0.04	0.07	0.10	0.15	0.20	0.40	0.65	0.70	0.95
10 Year Bond	1.83	1.95	2.05	2.15	2.25	2.30	2.30	2.30	2.30
<b>International</b>									
Fed Funds	0.125	0.125	0.125	0.125	0.125	0.375	0.625	0.875	0.875
US 10 Year Bond	1.55	1.75	1.90	2.00	2.10	2.20	2.25	2.30	2.30

Exchange rate forecasts	Latest	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Dec-23
AUD/USD	0.7280	0.75	0.76	0.77	0.78	0.78	0.79	0.80	0.78
USD/JPY	114.34	114	115	115	115	116	116	117	117
EUR/USD	1.1356	1.18	1.18	1.18	1.17	1.17	1.16	1.16	1.15
GBP/USD	1.3490	1.38	1.39	1.40	1.41	1.41	1.40	1.40	1.39
USD/CNY	6.3845	6.35	6.30	6.25	6.25	6.20	6.20	6.15	6.10
AUD/NZD	1.0338	1.06	1.06	1.05	1.05	1.05	1.07	1.08	1.07

# Contact the Westpac economics team.

**Michael Gordon, Acting Chief Economist**

 +64 9 336 5670


**Satish Ranchhod, Senior Economist**

 +64 9 336 5668

**Nathan Penny, Senior Agri Economist**

 +64 9 348 9114

**Paul Clark, Industry Economist**

 +64 9 336 5656

**Gregorius Steven, Economist**

 +64 9 367 3978

**Any questions email:**

 [economics@westpac.co.nz](mailto:economics@westpac.co.nz)

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