



Len Lye Centre, New Plymouth

Weekly Economic Commentary.

Not bad, considering.

The New Zealand economy has been slowing since 2016, and that came through in the September quarter labour market figures released by Stats NZ last week. However, the labour market is in better fettle than one would expect given the state of business confidence. Jobs growth has clearly slowed, but workers remain in short supply and wage inflation is gradually building. The RBNZ decision on Wednesday is a close call. We favour on hold, although the remaining uncertainty is Tuesday's inflation expectations data.

Annual employment growth according to the Household Labour Force Survey (HLFS) has slowed to 0.8%, whereas two years ago it was above 4%. Similarly, the number of hours paid according to the Quarterly Employment Survey (QES) rose just 0.4% over the quarter, consistent with a slow economy. Actually, the detail of the QES report implies a little downside risk to our Q3 GDP forecast of 0.3%.

The unemployment rate rose to 4.2%, reversing the fall to an 11-year low of 3.9% that we saw in the June quarter. That previous result came as a surprise to everyone, and we suspected that there was some survey noise involved. Last week's result supported that view. Stepping back a bit, the unemployment rate appears to have flattened off over the last

year or so, after falling steady for years before that. That's not a bad result given the slowdown in the economy. Our work suggests that the neutral, or non-inflationary, unemployment rate in New Zealand is around 4.5%, implying that we're still in 'tight' territory, but not immensely so.

Other aspects of the HLFS are also consistent with a tight labour market. The underutilisation rate (which includes underemployed workers and potential jobseekers) fell from 11.0% to 10.4% in the September quarter, its lowest level since June 2008. The decline was largely due to people shifting from part-time to full-time work. This has actually been a long-running trend, and the share of part-time workers is now at its lowest since 1990.



Squaring the circle between slow employment growth and low unemployment is slowing population growth and a declining rate of labour force participation. As a result, available workers have remained in relatively short supply. Participation is falling particularly among the 55+ age group as they choose early retirement.

Unemployment tends to lag the wider economy, so we think it's likely to worsen in the near term given the softening in GDP growth to date. However, with growth expected to strengthen again over the next couple of years, we see scope for the unemployment rate to drop below 4% again by 2021.

The built-up effect of a tight labour market in recent years appears to be translating into higher wage inflation. The Labour Cost Index rose 0.8% for the quarter, although that was boosted by recent pay agreements for teachers, nurses and police. Private sector wages rose 0.6%, lifting annual private sector wage growth rate to 2.3%. That's the highest it has been in ten years, but we do need to remember that an unusually large increase in the minimum wage played a role in that.

However, minimum wages and public sector pay agreements are not the only reasons that wage growth is accelerating. Even after adjusting for these factors, wage inflation is clearly starting to accelerate after years of being mysteriously low.

The RBNZ decision, inflation expectations, and housing data.

On October 31 we changed our call for this week's November RBNZ OCR decision to on hold, although we still expect a cut to 0.75% in February. Previously, we had expected a rash of weak data to prompt a cut by November, but that is not the

way things have turned out. GDP growth has probably been weaker than the RBNZ expected, but the housing market, inflation, and labour market have all been stronger. On top of that, the exchange rate is lower, other central banks are pausing, and global financial market sentiment has improved. In our assessment, this mix of developments is roughly neutral for monetary policy, so we think the RBNZ can hold off for now – although we acknowledge that it is a very finely balanced call.

The big remaining uncertainty is Tuesday's inflation expectations report. In the August MPS, the Reserve Bank revealed that the drop in two-year ahead inflation expectations from 2.01% to 1.86% was a big part of the decision to cut the OCR 50 basis points. The next instalment of the survey will be critical.

The RBNZ knows the result already, whereas we learn about it only the day before the MPS is released. We are expecting expectations to rebound a bit. If that is correct, then an on hold OCR decision will look more likely. If, however, expectations remain low or fall further, then we would seriously consider switching our call to a cut.

The other key piece of data this week will be the REINZ housing market report. Our long held view has been that the house prices will rise due to low interest rates, thereby boosting consumer sentiment and spending. We were completely alone when we made that call back in April, but now the idea of housing market turnaround seems to have more widespread acceptance. REINZ data has shown that house prices rose very sharply over the past two months, and preliminary data from a real estate website suggest that we are going to see a third strong month when the October data is released some time this week.

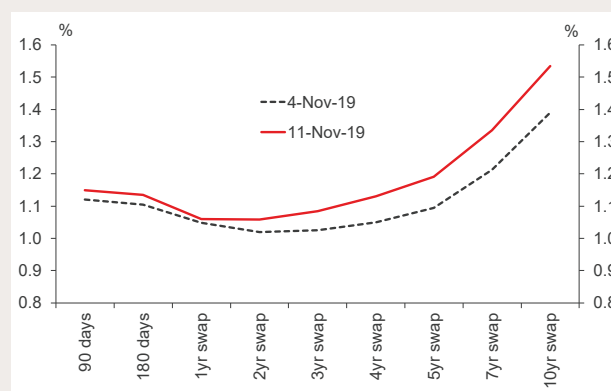
Fixed vs Floating for mortgages.

Taking a fixed mortgage is becoming more attractive. Fixed mortgage rates have tumbled over the past six months, but the period of decline may be drawing to a close. Wholesale fixed rates have risen, and the Reserve Bank does not have much further to go in the current OCR reduction cycle.

Among the fixed rates on offer, we think the best value is in the one- and two-year rates. Longer-term rates are high relative to where we think future short-term rates will go. That said, fixing for longer terms does offer security against future interest rate increases, and therefore may be preferred by those with low risk tolerance.

Floating mortgage rates are normally expensive for borrowers, but they may be the preferred option for those who require flexibility in their repayments.

NZ interest rates



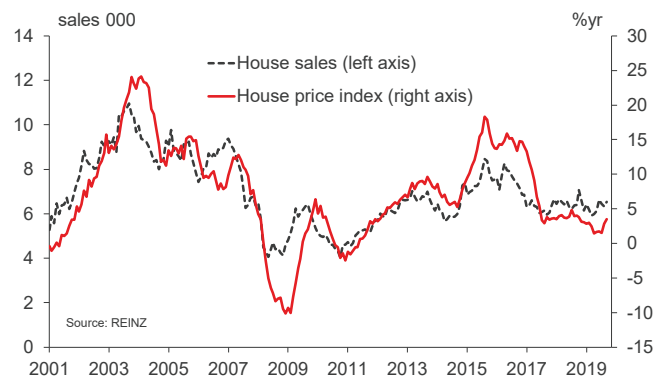
The week ahead.

NZ Oct REINZ House Price Index

Nov 11-15, last: 0.9%

- After softness through the middle part of the year, house price growth has reaccelerated in recent months. That follows the cancellation of the proposed capital gains tax and sharp falls in mortgage rates. Prices were up a total of 2.6% in August and September. The turnaround has been most notable in Auckland, where prices have quickly turned from falling to rising.
- Housing market data can be volatile. However, we've now had two months of solid gains. In addition, we've seen rising monthly sales, falling days to sell and falling inventories of unsold homes. All of this points to a continued uptrend in prices through the final months of the year.

REINZ house prices and sales

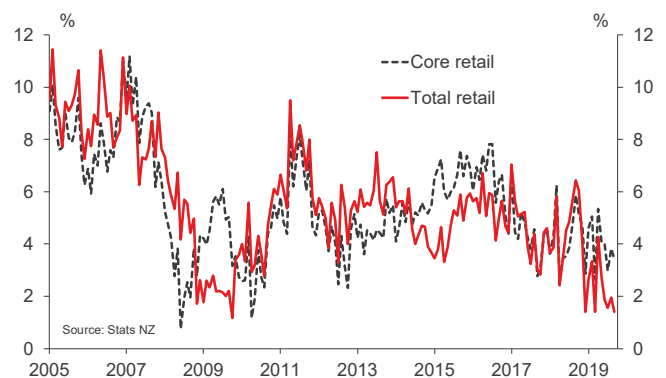


NZ Oct retail card spending

Nov 11, Last: +0.4%, WBC f/c: +0.6%

- After sluggish spending growth in the first half of the year, we may now be seeing the early signs of a resurgence in spending appetites. Retail spending has risen by more than expected over the past two months. This acceleration in spending follows reductions in mortgage rates in recent months and the related pick-up in house price growth.
- We expect that spending will remain firm in October. We're forecasting a 0.6% rise in total retail spending, underpinned by a solid 0.5% increase in core (excl. fuel and motor vehicle) categories.

Card transactions, annual % change

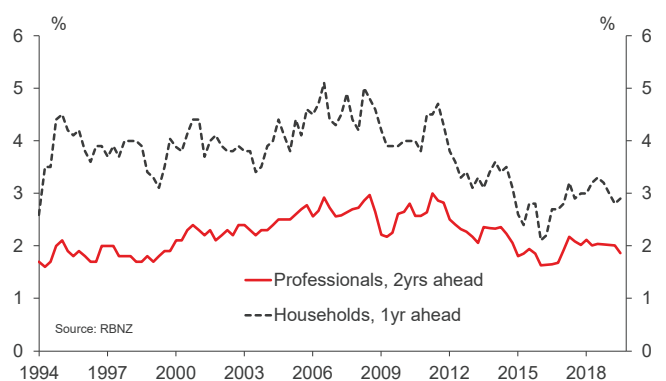


NZ RBNZ two-year ahead inflation expectations

Nov 12, last: 1.86%

- This will be critical data on the eve of the RBNZ's MPS. In August, the RBNZ's survey of two-year ahead inflation expectations fell from 2.01% to 1.86%. The RBNZ cited this as a key driver of their decision to cut the OCR by 50bp.
- The results of the November survey will be released to the market one day before the RBNZ's November policy announcement. However, the RBNZ will actually have the result about a week before the market, in time to affect its policy deliberations.
- We expect two-year ahead expectations will rebound a little. If surveyed expectations instead drop further, we would seriously consider changing our OCR call to a November cut.

RBNZ survey of inflation expectations



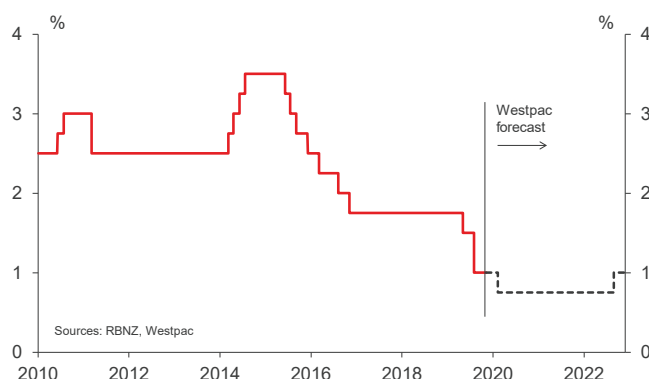
The week ahead.

NZ RBNZ Nov Monetary Policy Statement

Nov 13, last: 1.00%, WBC f/c: 1.00%, Mkt: 0.75%

- We expect the RBNZ will leave the OCR unchanged at its November meeting and deliver a statement similar to its September OCR Review. That basically said that the outlook for monetary policy has not changed significantly, risks are still to the downside, and there is scope for future easing if required.
- The November policy decision is looking like a close call. Recent developments have been mixed from an RBNZ perspective. Although activity was weak in mid-2019, recent high frequency data suggests that demand is now firming, the exchange rate has fallen, and the housing market is picking up. As noted above, inflation expectations data released on November 12 could be very influential in the RBNZ's thinking.
- We expect the RBNZ's OCR forecast to be unchanged from August, troughing at 0.9%.

RBNZ Official Cash Rate

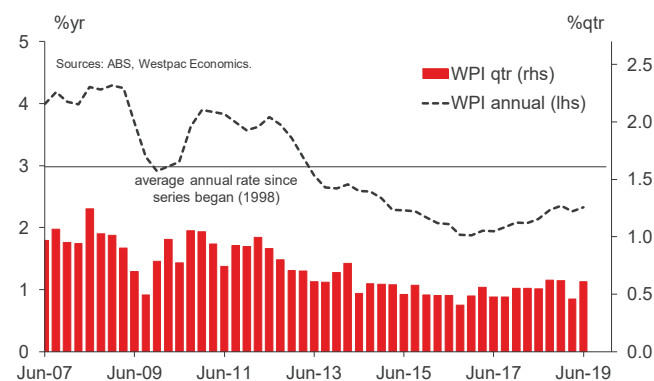


Aus Q3 Wage Price Index

**Nov 13, Last: 0.5%, WBC f/c: 0.7%
Mkt f/c: 0.5%, Range: 0.4% to 0.7%**

- The June quarter saw a slight lift in wage inflation, the Wage Price Index (WPI) rising 0.6% vs 0.5% in the March quarter, holding the annual rate flat at 2.3%/yr. The annual pace is up from the low of 1.9% in 2017 but still well below the long run average of 3%/yr.
- We expect wage inflation to drift a little higher from here but to remain below its long run average. Newly-signed EBAs have shown slightly firmer wage growth since 2017 and minimum wages saw a 3.3% increase last year. The marginal tightening in labour markets over 2017-18 may also be providing some residual support (wages tend to be slow to respond to shifts). However this lift may fade heading into 2020 as a softer labour market and a smaller 3% rise in the minimum wage rolls through. For the September quarter, we expect the WPI to show a 0.7% rise, nudging the annual rate up to 2.4%/yr.

Wages remain subdued

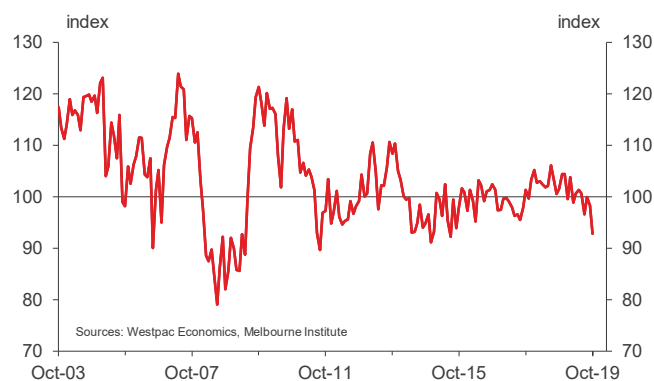


Aus Nov Westpac-MI Consumer Sentiment

Nov 13 Last: 92.8

- Consumer confidence has wilted in recent months despite targeted tax relief measures and interest rate cuts - the latter instead seemingly adding to the weakening in sentiment. The Westpac Melbourne Institute Consumer Sentiment Index fell 5.5% in October to 92.8, a four year low and is down 8.4% since the RBA started cutting rates in June. Consumers are looking behind the reason for the cuts and, arguably, the absolute level of rates and getting nervous.
- The latest survey is in the field over the week to Nov 9. To the extent that the Oct sentiment fall was an initial reaction to the RBA rate cut, this effect may diminish in Nov. Other developments also look slightly more positive with reports suggesting the US and China may be close to a trade deal, the ASX up 3.2% and more solid gains for house prices. That said, news on the wider economy has been less positive with the weak September quarter retail results released in the survey week a particular concern.

Consumer Sentiment Index



The week ahead.

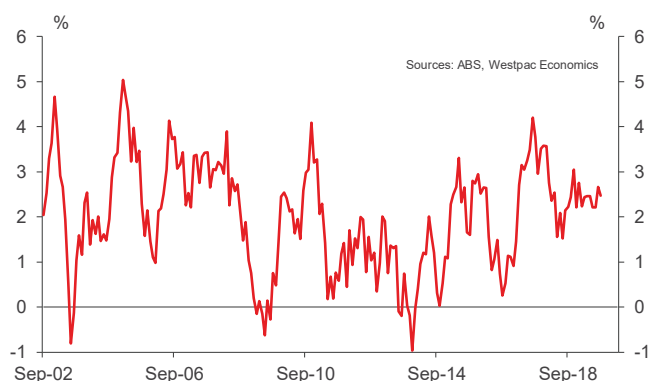
Aus October Labour Force – employment '000

Nov 14, Last: 14.7k, WBC f/c: 17k

Mkt f/c: 16k Range: 7k to 30k

- Employment rose a modest 14.7k in September.
- September's dynamic goes against the trend we have seen in 2019. Employment growth has averaged 25k per month in the year, but stronger growth in labour supply has seen the unemployment rate move up.
- In our view, while rate cuts along with the Government's tax offset payments should help to support demand, we think it will be insufficient to get economic growth moving back to trend or above in 2020. As such, we see employment growth moderating and are forecasting a 17k increase in October - another read below the recent average.

Employment growth 6m annualised



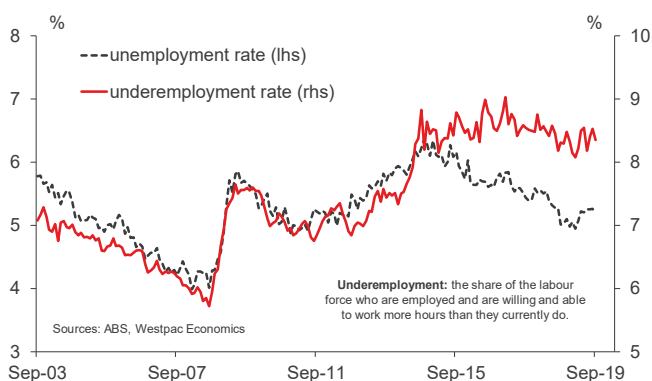
Aus October Labour Force – unemployment %

Nov 14, Last: 5.2%, WBC f/c: 5.3%

Mkt f/c: 5.2% Range: 5.2% to 5.3%

- The most notable update in the September Labour Force survey was that the unemployment rate declined from 5.3% to 5.2%, against consensus expectations for a steady read. That comes from a moderate 14.7k rise in employment but a retracement in the participation rate from 66.2% to 66.1%.
- Note that in August, the unemployment rate was 5.25% at two decimal places and is 5.20% in September. The modest 0.05ppt movement is not uncommon given the volatility in the Labour Force survey.
- We think September's modest decline in the unemployment rate will be temporary and the unemployment rate will edge back up to 5.3%.

Unemployment & underemployment

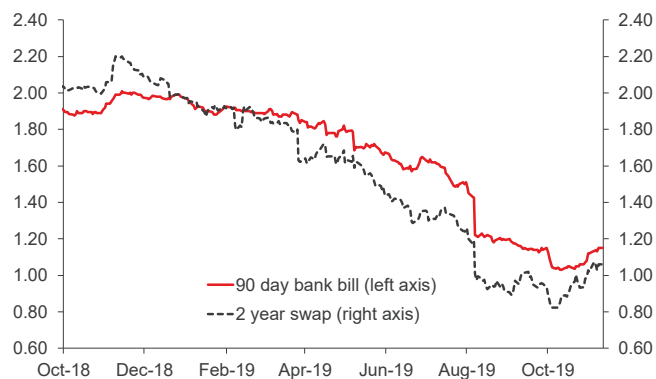


New Zealand forecasts.

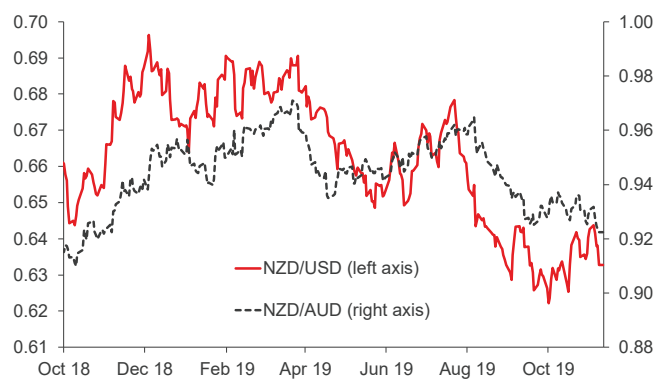
Economic forecasts	Quarterly				Annual			
	2019	2020			2018	2019f	2020f	2021f
% change	Jun (a)	Sep	Dec	Mar				
GDP (Production)	0.5	0.3	0.5	0.6	2.8	2.2	2.3	2.8
Employment	0.6	0.2	0.4	0.3	1.9	1.2	1.8	2.0
Unemployment Rate % s.a.	3.9	4.2	4.3	4.4	4.3	4.3	4.2	3.9
CPI	0.6	0.7	0.3	0.5	1.9	1.7	1.7	1.8
Current Account Balance % of GDP	-3.4	-3.4	-3.2	-3.2	-3.9	-3.2	-3.0	-2.8

Financial forecasts	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21
Cash	1.00	0.75	0.75	0.75	0.75	0.75
90 Day bill	1.00	0.90	0.90	0.90	0.90	0.90
2 Year Swap	1.10	1.00	1.00	1.00	1.00	1.00
5 Year Swap	1.20	1.15	1.15	1.20	1.25	1.30
10 Year Bond	1.35	1.20	1.20	1.20	1.25	1.35
NZD/USD	0.63	0.62	0.62	0.63	0.63	0.64
NZD/AUD	0.94	0.94	0.94	0.94	0.94	0.94
NZD/JPY	68.0	66.3	65.7	66.2	66.2	67.8
NZD/EUR	0.58	0.57	0.56	0.57	0.56	0.57
NZD/GBP	0.49	0.47	0.47	0.48	0.48	0.49
TWI	70.5	69.5	69.2	69.6	69.3	69.9

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 11 November 2019

Interest rates	Current	Two weeks ago	One month ago
Cash	1.00%	1.00%	1.00%
30 Days	1.14%	1.14%	1.17%
60 Days	1.15%	1.10%	1.10%
90 Days	1.15%	1.06%	1.03%
2 Year Swap	1.06%	0.94%	0.89%
5 Year Swap	1.19%	1.01%	0.94%

NZ foreign currency mid-rates as at 11 November 2019

Exchange rates	Current	Two weeks ago	One month ago
NZD/USD	0.6348	0.6346	0.6337
NZD/EUR	0.5747	0.5718	0.5726
NZD/GBP	0.4953	0.4934	0.5015
NZD/JPY	69.16	69.16	68.61
NZD/AUD	0.9224	0.9277	0.9334
TWI	70.05	70.37	70.56

Data calendar.

		Last	Market median	Westpac forecast	Risk/Comment
Mon 11					
NZ	Oct REINZ house sales	3.1%	-	-	Due this week. Price growth has picked up...
	Oct REINZ house prices %yr	3.5%	-	-	...and signs point to a continued acceleration.
	Oct card spending	0.4%	-	0.6%	Spending appetites have firmed in recent months.
Chn	Oct foreign direct investment %yr	3.8%	-	-	FDI key to China's continued economic development.
UK	Q3 GDP	-0.2%	0.4%	-	Stabilisation from Q2 decline post Brexit related stockpiling.
US	Veterans Day	-	-	-	Public holiday. NYSE is open.
	Fedspeak	-	-	-	Rosengren (dissenter) in Oslo.
Tue 12					
NZ	Sep net migration	3530	-	-	Annual migration down from its peak, but still elevated.
	Q4 RBNZ inflation expectations	1.86%	-	-	A key focus for the RBNZ ahead of its OCR decision.
Aus	Oct NAB business survey	2	-	-	Conditions weak. Will we start to see any stimulus boost?
Eur	Nov ZEW survey of expectations	-23.5	-	-	Sentiment is negative.
UK	Sep ILO unemployment rate	3.9%	3.9%	-	Employment is weakening, unemployment rate still low.
US	Oct NFIB small business optimism	101.8	102.0	-	Small businesses have been more optimistic than big firms.
	Fedspeak	-	-	-	Harker in New York.
Wed 13					
NZ	Oct food price index	0.0%	-	-1.2%	Seasonal decline; annual pace has picked up a little.
	RBNZ policy decision	1.00%	0.75%	1.00%	A close call; we favour no change in the OCR.
Aus	Nov WBC-MI Consumer Sentiment	92.8	-	-	In Oct, slumped 5.5% to a four year low.
	Q3 wage cost index	0.6%	0.5%	0.5%	Subdued underlying trend.
Eur	Sep industrial production	0.4%	-0.3%	-	Manufacturing is contracting.
UK	Oct core CPI %yr	1.7%	1.8%	-	Has cooled to be back below the 2% target.
US	Oct core CPI %yr	2.4%	2.4%	2.4%	Core prices up 0.2% in month; 0.3% for headline.
	Fed Chair Powell speaks	-	-	-	Addressing the congressional Joint Economic Committee.
	Fedspeak	-	-	-	Kashkari in Wisconsin (10am AEDT and overnight).
Thu 14					
Aus	RBA Assist. Gov Financial Mkts	-	-	-	Michele Bullock, panel at superannuation funds, 9:50am.
	Oct employment	14.7k	16k	17k	Jobs growth to slow from 2019 ytd avg of 25k/month.
	Oct unemployment rate	5.2%	5.2%	5.3%	Placing upward pressure on the unemployment rate.
Chn	Oct fixed asset investment ytd %yr	5.4%	-	-	Investment continues to disappoint, overall and by sector.
	Oct industrial production	5.6%	-	-	External demand and weak investment weighing.
	Oct retail sales %yr	7.8%	-	-	Consumer income gains constrained by soft growth.
Eur	Q3 GDP 2nd estimate	0.2%	0.2%	0.2%	A below trend pace on growth, held down...
	Q3 employment	0.2%	0.2%	-	Signs that slower growth may start to impact jobs growth.
UK	Oct retail sales	0.0%	0.2%	-	Consumption has held robust on solid wages growth.
US	Oct PPI	-0.3%	0.3%	-	No upstream price pressures of significance.
	Initial jobless claims	211k	-	-	Firing remains historically low.
	Fed Chair Powell speaks	-	-	-	Before the House Budget Committee.
	Fedspeak	-	-	-	Clarida, Evans, Daly, Williams, and Bullard.
Fri 15					
Aus	RBA Deputy Governor Debelle	-	-	-	Panel at FINSIA event on "Mortgage Arrears", 12:30pm.
	2018/19 Annual State Accounts	-	-	-	Output estimates for the state economies, on an annual basis.
Eur	Sep trade balance €bn	20.3	-	-	Remains in surplus even after trade slowdown.
	Oct core CPI final %yr	1.1%	1.1%	-	Stuck around 1%, below the 2% target.
US	Nov Fed Empire state index	4	6	-	Regional surveys remain volatile.
	Oct import price index	0.2%	-0.2%	-	US dollar strength continues to hold back import prices.
	Oct retail sales	-0.3%	0.2%	0.4%	September was disappointing. Growth hence to be volatile.
	Oct industrial production	-0.4%	-0.3%	-	US manufacturing likely to remain weak for some time.
	Sep business inventories	0.0%	0.1%	-	Inventories should be wound down into 2020, as GDP slows.

International forecasts.

Economic forecasts (Calendar years)	2016	2017	2018	2019f	2020f	2021f
Australia						
Real GDP % yr	2.8	2.4	2.7	1.8	2.4	2.7
CPI inflation % annual	1.5	1.9	1.8	1.7	1.9	1.9
Unemployment %	5.7	5.5	5.0	5.3	5.6	5.3
Current Account % GDP	-3.1	-2.6	-2.1	0.6	-0.5	-1.8
United States						
Real GDP %yr	1.6	2.4	2.9	2.3	1.6	1.5
Consumer Prices %yr	1.4	2.1	2.4	1.8	1.9	1.9
Unemployment Rate %	4.9	4.4	3.8	3.6	3.6	3.8
Current Account %GDP	-2.3	-2.3	-2.3	-2.6	-2.5	-2.4
Japan						
Real GDP %yr	0.6	1.9	0.8	0.8	0.2	0.4
Euro zone						
Real GDP %yr	1.9	2.5	1.9	1.2	1.0	1.2
United Kingdom						
Real GDP %yr	1.8	1.8	1.4	1.3	0.8	1.1
China						
Real GDP %yr	6.7	6.8	6.6	6.1	5.8	5.8
East Asia ex China						
Real GDP %yr	4.0	4.5	4.3	3.6	3.7	3.9
World						
Real GDP %yr	3.4	3.8	3.6	3.0	3.0	3.2

Forecasts finalised 8 November 2019

Interest rate forecasts	Latest	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Jun-21	Dec-21
Australia								
Cash	0.75	0.75	0.50	0.50	0.50	0.50	0.50	0.50
90 Day BBSW	0.93	0.85	0.70	0.70	0.70	0.70	0.75	0.75
10 Year Bond	1.29	1.10	0.90	0.90	1.00	1.10	1.30	1.50
International								
Fed Funds	1.625	1.625	1.375	1.125	0.875	0.875	0.875	0.875
US 10 Year Bond	1.91	1.70	1.50	1.45	1.40	1.50	1.60	1.80
ECB Deposit Rate	-0.50	-0.50	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60

Exchange rate forecasts	Latest	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Jun-21	Dec-21
AUD/USD	0.6882	0.67	0.66	0.66	0.67	0.67	0.69	0.72
USD/JPY	109.22	108	107	106	105	105	107	109
EUR/USD	1.1052	1.09	1.09	1.10	1.11	1.12	1.14	1.15
GBP/USD	1.2815	1.30	1.33	1.32	1.32	1.31	1.31	1.32
USD/CNY	6.9780	7.10	7.10	7.05	6.95	6.90	6.75	6.60
AUD/NZD	1.0813	1.06	1.06	1.06	1.06	1.06	1.07	1.08

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