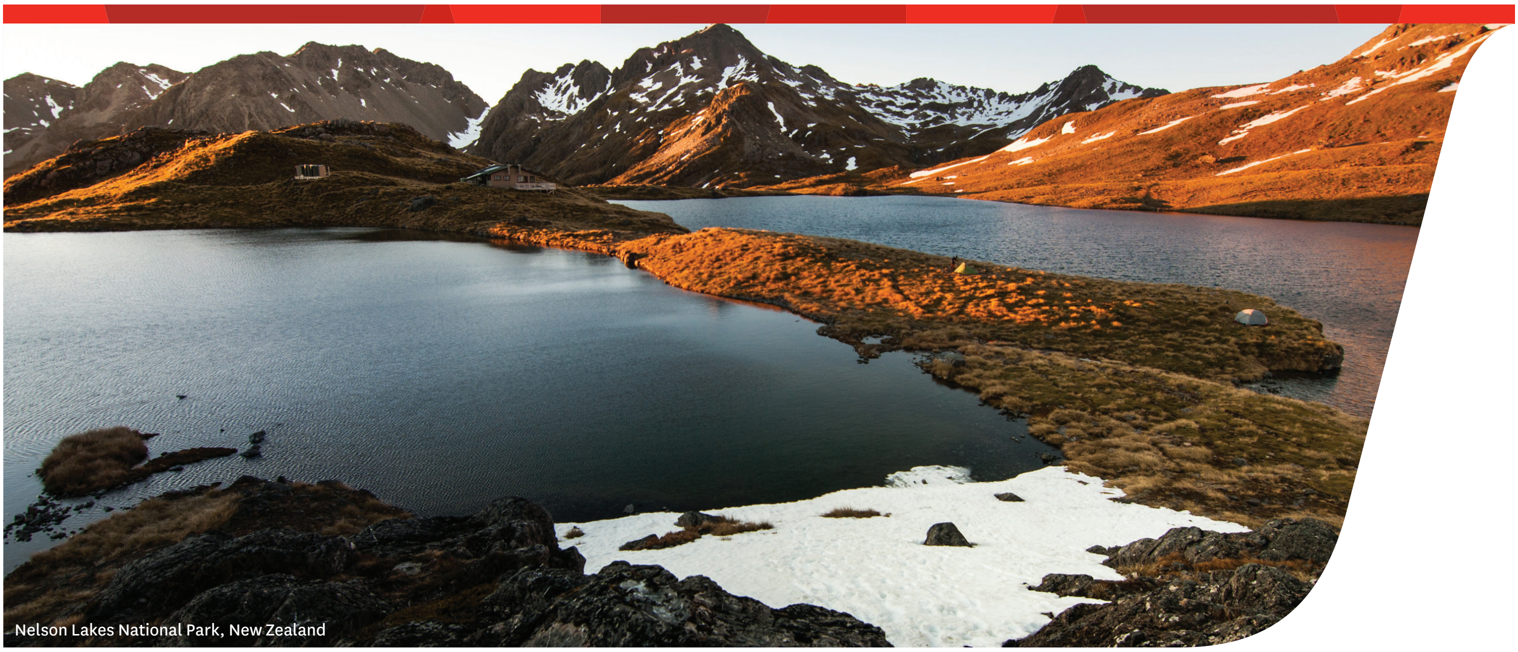

Nelson Lakes National Park, New Zealand

Weekly Economic Commentary.

Sugar rush.

The lack of international tourists has left a big hole in the economy. However, monetary and fiscal stimulus have underpinned a strong recovery in domestic demand, with signs of solid momentum as we head into the new year. Longer-term, the country will face some tough decisions, as the current 'sugar rush' from super-stimulatory policy will eventually have to be repaid.

As 2020 draws to a close, economic activity remains below the levels that prevailed prior to the outbreak of Covid-19. That's mainly due to the continued closure of our borders and the related loss of international tourist spending. However, outside of the travel and tourism sectors, much of the ground lost earlier in the year has already been recovered. As we discuss in our latest *Economic Overview*, many parts of the domestic economy have rebounded faster than expected after the lockdown. Notably, businesses linked to the building industry are reporting strong demand. We've also seen lifts in manufacturing activity (including exports) and gains in the retail sector.

Looking ahead, the strength of the economy will remain closely tied to the spread of the virus. Recent positive news about vaccine development has been welcome. Even so, we don't expect a widespread rollout to begin until mid-2021, and reaching effective immunity for the global population could still be several years away. As a result, we expect that New Zealand will remain cautious about reopening its borders in order to protect both public health and the economy. In fact, we've pushed out our assumptions regarding the opening of the borders and are now assuming that visitors from Australia will only be allowed entry into the country from mid-2021 onwards. Even then, the numbers arriving are likely to start off small and rise gradually over time.

Given the resilience of the domestic economy, we have revised up our forecast for GDP in the near term. However, we have moderated our longer-term forecasts due to the later opening of the border. On balance, those revisions mean that we now expect unemployment to peak at 6.2% early next year. That would be similar to the peak seen after the Global Financial Crisis and much lower than we initially feared when Covid-19 first arrived on our shores.

Helping to underpin the resilience of the domestic economy has been the huge amount of fiscal stimulus that was rolled out in recent months. And while Covid-related spending is now winding down, the coming years will see ongoing increases in general Government spending in social policy areas (like health and education), as well as huge amounts of spending on infrastructure.

As a nation, we'll be facing some tough choices about fiscal policy over the coming years. We expect that the Government will still be running large deficits mid-decade. And beyond that time, we'll be faced with increasing costs related to the ageing population, including the cost of New Zealand Superannuation and increasing spending on health care. That will leave us on an unsustainable fiscal trajectory. Future governments will therefore be forced to either reduce spending or increase taxes, or both. Given the lingering challenges stemming from the Covid outbreak and the current Government's spending priorities, we doubt that there will be significant moves on either of those fronts during the current parliamentary term. Indeed, although the Government has announced plans to lift the top income tax rate, the resulting increases in tax revenue will actually be very small.

However, the necessary adjustments to our fiscal position can't be delayed forever. Sooner or later, some form of consolidation will be necessary, though the precise form this takes will depend on which party is leading the government at the time. Our pick is that a future government will introduce some form of tax on assets, such as a land tax, capital gains tax or a wealth tax. Societal concern about increasing wealth inequality is only going to intensify, eventually creating a large constituency for such a change.

The significant increases in monetary and fiscal stimulus since the start of the year have given the domestic economy a powerful shot in the arm. In fact this week's September quarter retail spending report showed a rebound in spending to above pre-Covid levels. But while overall spending is holding up, what we're buying has changed. With many families spending more time around the house, New Zealanders have been spending up on appliances, recreational items and household renovations. That's offset reduced spending on entertainment activities and travel.

Helping to boost households' spending appetites has been the roaring strength of the housing market. When the economy first went into lockdown, we forecast that prices would initially fall by 7%, and would later shoot higher in response to low interest rates. However, what we actually got was a decline of only 2% followed by an earlier and bigger boom, with prices now up a whopping 14% over the past year.

House prices are responding squarely to the reduction in mortgage rates. Indeed, this year has clearly proven a point that we have been making for years – interest rates matter more for the housing market than physical factors like population growth or housing supply. In fact, in recent months net migration has effectively fallen to zero and booming construction activity is adding to supply. Even so, house prices have continued to charge higher.

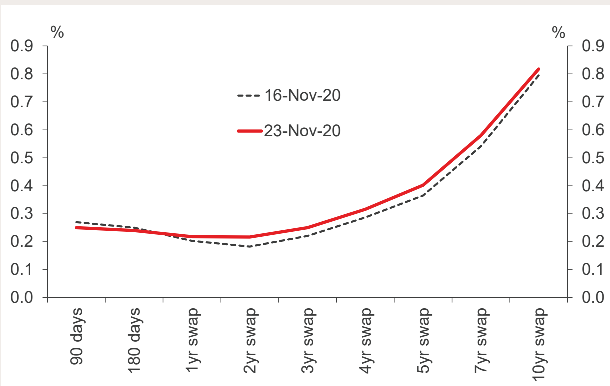
With the domestic economy continuing to firm and interest rates set to remain low for some time yet, we've again revised up our forecast for house prices. We now expect that annual house price growth will peak at 15% in mid-2021. And with strength in the housing market typically associated with firmness in households spending, that also points to firmness in demand as we head into the new year.

Rapid increases in house prices have rekindled concerns about affordability for first home buyers and longer-term concerns about financial stability. Consequently, the RBNZ has signalled that restrictions on high loan to value lending (LVRs) are likely to be re-introduced from 1 March 2021, and we expect that they will be squarely targeted at property investors. Based on the experience with LVR since 2013, we expect that the reintroduction of lending restrictions will take a little of the steam out of the property market, but won't be a game changer. Realistically, we don't expect a material downturn in the housing market until mortgage rates push higher. However, such increases in mortgage rates are still a way off, due to continued low consumer price inflation.

Fixed vs Floating for mortgages.

Mortgage rates in the New Zealand banking system could fall in the near future. Term deposit rates have been dropping recently, and that is often a pre-cursor to fixed mortgage rate declines. The Reserve Bank has announced the introduction of a Funding for Lending Programme, effective December, which will add further downward pressure on both fixed and floating mortgage rates.

NZ interest rates



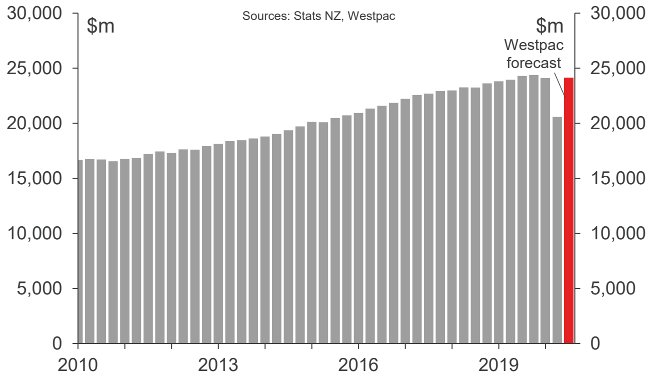
The week ahead.

NZ Q3 retail spending

Nov 23, Last: –14.6%, WBC f/c: +17%,
Mkt f/c: +20%, Range: +14% to +25%

- Retail spending fell by 14.6% in the June quarter. That result was heavily impacted by the Covid-19 lockdown of the economy in April and the related loss of international tourists.
- Spending has rebounded as the Covid Alert Level has been dialled back. And while there were some bumps through the quarter (including the temporary reintroduction of activity restrictions in August), spending levels have retraced most of the ground lost in the June quarter.
- We estimate that the volume of goods purchased rose by 17% over the quarter with a similar rise in nominal spending. That would leave spending around the levels we saw at the start of the year.

NZ quarterly real retail sales

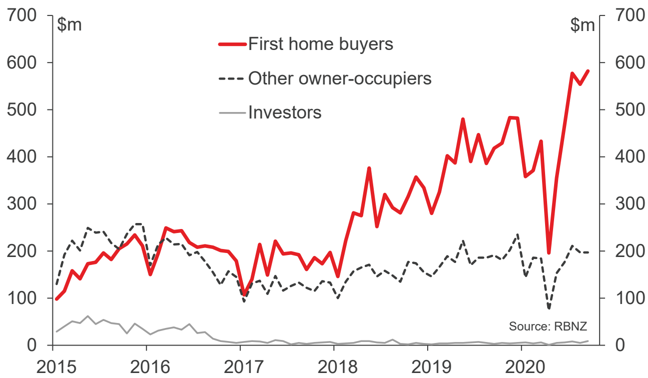


NZ RBNZ Financial Stability Report

Nov 25

- The Reserve Bank's six-monthly review of the financial system comes against a much more encouraging backdrop compared to May. Economic activity has rebounded quickly after the Covid-19 lockdown, with the exception of travel and tourism. Banks remain well capitalised and are in a position to absorb loan losses resulting from the Covid shock.
- We expect the FSR to focus on the resurgence in the housing market and the growth in mortgage lending in particular. Lending has been spurred on by the rebounding economy, record low interest rates, and the removal of limits on high loan-to-value ratio (LVR) lending in April.
- The RBNZ has said that it will consult on reinstating those limits from March next year. A consultation paper may be released along with the FSR, if not before.

NZ new mortgage lending above 80% LVR

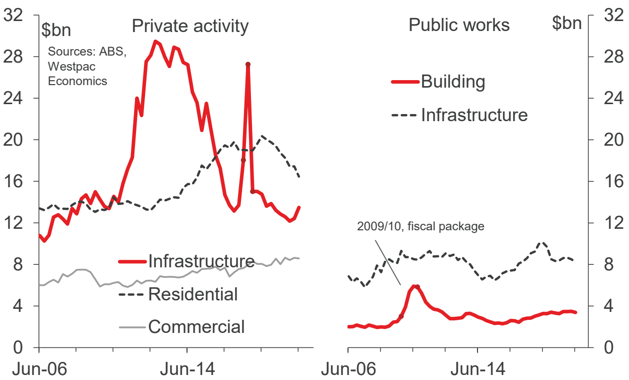


Aus Q3 construction work

Nov 25, Last: –0.7%, WBC f/c: –3.8%
Mkt f/c: –1.9%, Range: –4.0% to 0.6%

- The construction sector was in a downturn ahead of covid, with weakness led but not confined to the downturn in home building. Disruptions associated with the pandemic added another challenge in 2020.
- In Q2, work edged 0.7% lower to be down 2.2% over the year and some 11.4% below the mid-2018 peak. The Q2 print was flattered by a reported 8.6% spike in private engineering – a jump that may be due to the importation of a large structure.
- For Q3, we anticipate a 3.8% decline in total work. This allows for some reversal in private engineering, down almost 5%.
- Private building work was likely down sharply (residential and non-residential) on lower approvals and disruptions (with Victoria's 2nd lock-down). Public works are expected to bounce, +1.5%, partially reversing Q2's 3% drop.

Construction work: by segment



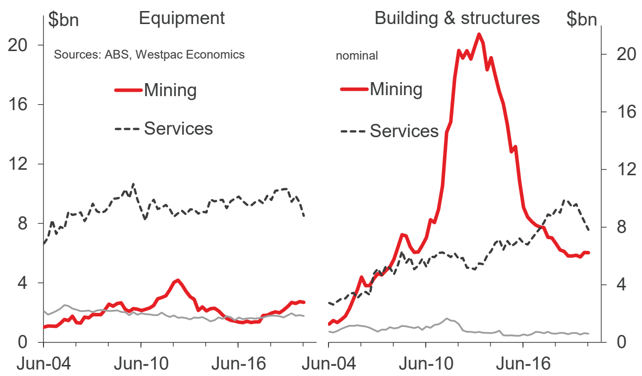
The week ahead.

Aus Q3 private business capex

Nov 26, Last: –5.9%, WBC f/c: –6.0%
Mkt f/c: –1.5%, Range: –6.0% to 1.7%

- Private business capex will contract sharply as a result of the covid recession.
- Capex slumped in Q2, falling by 5.9%, including a –4.4% for building & structures (B&S) and a -7.6% in equipment
- More of the same is likely in Q3, with capex a forecast -6%.
- Equipment spending may fall by as much as 10% in Q3. The economy is awash with excess capacity and firms have been in survival mode in these highly uncertain times. In addition, spending was brought forward from Q3 to Q2 (ahead of June 30) in response to temporary tax incentives.
- B&S is forecast to fall by almost 3%, with declines likely across both building work and for structures.

CAPEX: by industry by asset

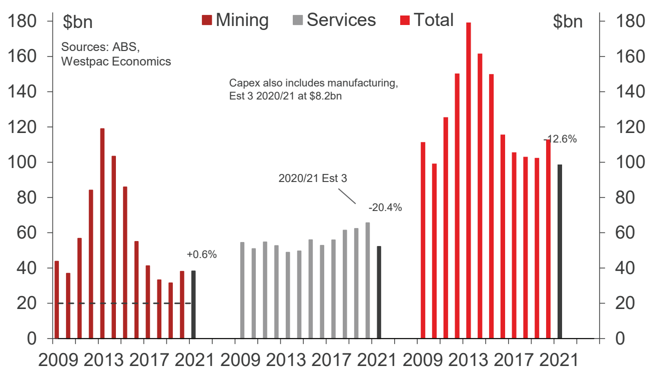


Aus 2020/21 capex plans

Nov 26, Last: Est 3 2020/21: $98.6bn,
–12.6% vs Est 3 a yr ago

- The covid recession will see businesses cut non-essential capex – particularly equipment in the non-mining sectors. The focus is survival and firms are looking to preserve cash flows.
- Est 3 for 2020/21 was $98.6bn, -12.6% below Est 3 a year ago.
- Est 4 for 2020/21 may potentially print around $107bn, -9% below Est 4 a year ago.
- A $107bn print would represent an 8% upgrade on Est 3, which is in excess of the historical average of around 4%.
- The above par upgrade reflects a relief bounce – locally the pandemic, including Victoria's 2nd lock-down, has not been as dire as feared.
- The outlook would still be for a decline in business investment – potentially a near double digit fall for non-mining, with only a partial offset from a modest lift in mining. The mining sector has not been immune, with some projects shelved or delayed as energy prices tumbled on weaker demand.

Capex plans, by industry: Estimate 3

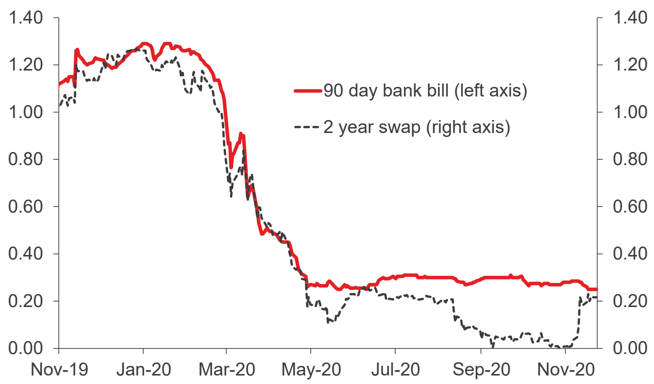


New Zealand forecasts.

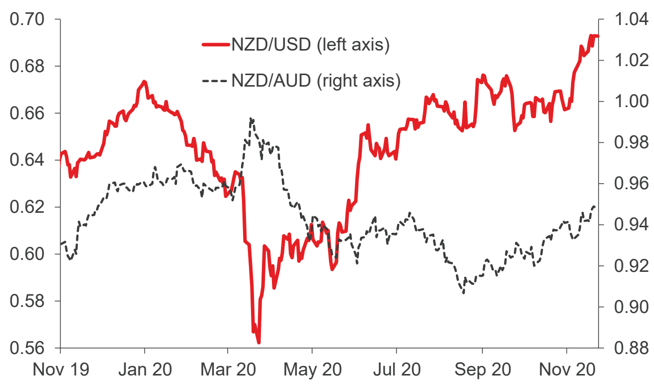
Economic forecasts	Quarterly				Annual			
	2020			2021				
% change	Jun (a)	Sep	Dec	Mar	2019	2020f	2021f	2022f
GDP (Production)	-12.2	12.0	1.0	1.3	2.3	-4.2	6.1	3.0
Employment	-0.3	-0.8	-0.6	0.1	1.2	-0.7	1.7	3.4
Unemployment Rate % s.a.	4.0	5.3	6.0	6.2	4.1	6.0	6.0	5.2
CPI	-0.5	0.7	0.0	0.1	1.9	1.0	0.6	1.6
Current Account Balance % of GDP	-1.9	-1.4	-1.7	-2.4	-3.4	-1.7	-4.1	-4.0

Financial forecasts	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Jun-22
Cash	0.25	0.25	-0.25	-0.50	-0.50	-0.50
90 Day bill	0.25	0.05	-0.30	-0.40	-0.40	-0.40
2 Year Swap	0.20	0.00	-0.10	-0.20	-0.20	-0.15
5 Year Swap	0.40	0.25	0.15	0.10	0.10	0.20
10 Year Bond	0.80	0.80	0.80	0.80	0.90	1.10
NZD/USD	0.70	0.71	0.71	0.71	0.71	0.71
NZD/AUD	0.93	0.93	0.91	0.90	0.89	0.89
NZD/JPY	72.8	74.6	75.3	75.3	75.3	76.0
NZD/EUR	0.59	0.59	0.59	0.58	0.57	0.57
NZD/GBP	0.53	0.54	0.55	0.55	0.55	0.55
TWI	74.1	74.6	74.0	73.5	72.9	72.6

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 23 November 2020

Interest rates	Current	Two weeks ago	One month ago
Cash	0.25%	0.25%	0.25%
30 Days	0.27%	0.27%	0.27%
60 Days	0.26%	0.28%	0.27%
90 Days	0.25%	0.29%	0.27%
2 Year Swap	0.22%	0.04%	0.01%
5 Year Swap	0.40%	0.14%	0.13%

NZ foreign currency mid-rates as at 23 November 2020

Exchange rates	Current	Two weeks ago	One month ago
NZD/USD	0.6927	0.6782	0.6685
NZD/EUR	0.5845	0.5705	0.5658
NZD/GBP	0.5216	0.5154	0.5132
NZD/JPY	71.93	70.00	70.09
NZD/AUD	0.9474	0.9337	0.9380
TWI	73.57	72.17	71.97

Data calendar.

		Last	Market median	Westpac forecast	Risk/Comment
Mon 23					
NZ	Q3 real retail sales	–14.6%	20.0%	17.0%	Sales have rebounded after April's lockdown.
Eur	Nov Markit PMIs	–	–	–	Lockdowns over Europe & UK will stifle the recovery...
UK	Nov Markit PMIs	–	–	–	... in both the manufacturing and services sectors.
US	Oct Chicago Fed activity index	0.27	–	–	Continues to ease; positive read implies g'th above-trend.
	Nov Markit manufacturing PMI	53.4	52.5	–	Business activity growing at strongest pace since Feb '19.
	Nov Markit service PMI	56.9	55.8	–	Services have been expansionary for four straight months.
	Fedspeak	–	–	–	Daly (06:00 AEDT) and Evans (07:00 AEDT) to speak.
Tue 24					
Aus	RBA Deputy Governor Debelle	–	–	–	`Monetary Policy in 2020' Aus. Business Economists (1:30pm)
US	Sep FHFA house prices	1.5%	–	–	September set a series record for FHFA monthly growth...
	Sep S&P/CS home price index	0.47%	0.40%	–	... and the 20-city index saw growth at 5.2%yr in Aug.
	Nov consumer confidence index	100.9	98.0	–	**Weakened ahead of the election on uncertainty.**
	Nov Richmond Fed index	29	–	–	Recent increase led by strong new orders and shipments.
	Fedspeak				Bullard on monetary policy challenges (03:00 AEDT).
Wed 25					
NZ	RBNZ Financial Stability Report	–	–	–	Likely to focus on housing risks.
Aus	Q3 construction work done	–0.7%	–1.9%	–3.8%	Underlying weakness + covid disruptions (Vic 2nd lockdown).
US	Initial jobless claims	742k	–	–	Downtrend was interrupted by an uptick last week.
	Oct wholesale inventories	0.4%	–	–	To remain expansionary as firms continue to restock.
	Oct personal income	0.9%	0.1%	0.2%	Support from government now in rear-vision mirror.
	Oct personal spending	1.4%	0.5%	0.4%	Services spending restricted by COVID's spread.
	Oct PCE deflator	0.2%	0.0%	0.0%	Inflation pressures to remain absent for some time.
	Oct durable goods orders	1.9%	1.0%	1.4%	Investment to lag consumer recovery.
	Q3 GDP	33.1%	33.1%	33.1%	Third estimate, likely unrevised.
	Nov Uni. of Michigan sentiment	77.0	76.8	–	Final print; surprised to the downside on expectations.
	Oct new home sales	959k	970k	–	Remain elevated at c. 25% above pre-COVID levels.
	FOMC meeting Minutes	–	–	–	For November 5 FOMC meeting; risks the focus.
Thu 26					
NZ	Oct trade balance $m	–1017	–	–500	Export values rebounded after a soft September.
Aus	Q3 private new capital expenditure	–5.9%	–1.5%	–6.0%	Sharp falls, particularly equipment, due to COVID recession.
	2020/21 capex plans, AUDbn	98.6	–	107	Est 4 may not be as weak as Est 3, on a "relief bounce".
Eur	Oct M3 money supply %yr	10.4%	–	–	Money growth remains elevated on ECB support.
US	Thanksgiving	–	–	–	Public holiday.
Fri 27					
NZ	Nov ANZ consumer confidence	108.7	–	–	While still low, consumer confidence has been rising.
Aus	Black Friday sales	–	–	–	Retail sales / discounting - "biggest day of the year".
Chn	Oct industrial profits %yr	10.1%	–	–	Has been supported by consumption and external demand.
Eur	Nov economic confidence	90.9	86.2	–	Economic confidence recovery moderating...
	Nov consumer confidence	–15.5	–	–	... as consumer confidence begins to turn down.
UK	Nov Nationwide house prices	0.8%	–	–	Prices have been volatile. Policy and rates supportive.
US	Black Friday	–	–	–	Beginning of the Christmas shopping season.

International forecasts.

Economic Forecasts (Calendar Years)	2017	2018	2019	2020f	2021f	2022f
Australia						
Real GDP %yr	2.4	2.8	1.8	-3.3	2.3	3.4
CPI inflation %yr	1.9	1.8	1.8	0.6	1.6	2.1
Unemployment rate %	5.5	5.0	5.2	7.5	7.5	6.6
Current account % of GDP	-2.6	-2.1	0.6	2.0	-0.8	-3.0
United States						
Real GDP %yr	2.3	3.0	2.2	-3.6	3.1	2.2
CPI inflation %yr	2.1	2.4	1.9	1.1	1.8	1.9
Unemployment rate %	4.4	3.9	3.7	8.4	6.8	5.8
Current account % of GDP	-2.3	-2.3	-2.6	-2.5	-2.4	-2.4
Japan						
Real GDP %yr	2.2	0.3	0.7	-5.8	2.2	1.7
Euro zone						
Real GDP %yr	2.6	1.8	1.3	-8.3	3.1	3.0
United Kingdom						
Real GDP %yr	1.9	1.3	1.5	-11.3	5.7	5.0
China						
Real GDP %yr	6.9	6.8	6.1	1.7	10.0	5.6
East Asia ex China						
Real GDP %yr	4.7	4.4	3.7	-2.9	4.9	4.7
World						
Real GDP %yr	3.8	3.5	2.8	-3.8	5.3	4.0
Forecasts finalised 6 November 2020						

Interest rate forecasts	Latest	Dec–20	Mar–21	Jun–21	Sep–21	Dec–21	Jun–22	Dec–22
Australia								
Cash	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
90 Day BBSW	0.02	0.02	0.02	0.02	0.02	0.02	0.06	0.10
10 Year Bond	0.86	0.80	0.95	1.05	1.15	1.25	1.50	1.70
International								
Fed Funds	0.125	0.125	0.125	0.125	0.125	0.125	0.125	0.125
US 10 Year Bond	0.83	0.80	0.90	1.00	1.10	1.20	1.40	1.50

Exchange rate forecasts	Latest	Dec–20	Mar–21	Jun–21	Sep–21	Dec–21	Jun–22	Dec–22
AUD/USD	0.7291	0.75	0.76	0.78	0.79	0.80	0.80	0.78
USD/JPY	103.81	104	105	106	106	106	107	107
EUR/USD	1.1877	1.19	1.20	1.21	1.22	1.24	1.25	1.25
GBP/USD	1.3265	1.32	1.34	1.36	1.38	1.39	1.40	1.40
USD/CNY	6.5766	6.60	6.55	6.50	6.45	6.40	6.30	6.20
AUD/NZD	1.0535	1.07	1.07	1.10	1.11	1.13	1.13	1.11

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Past performance is not a reliable indicator of future performance. The forecasts given in this document are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

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