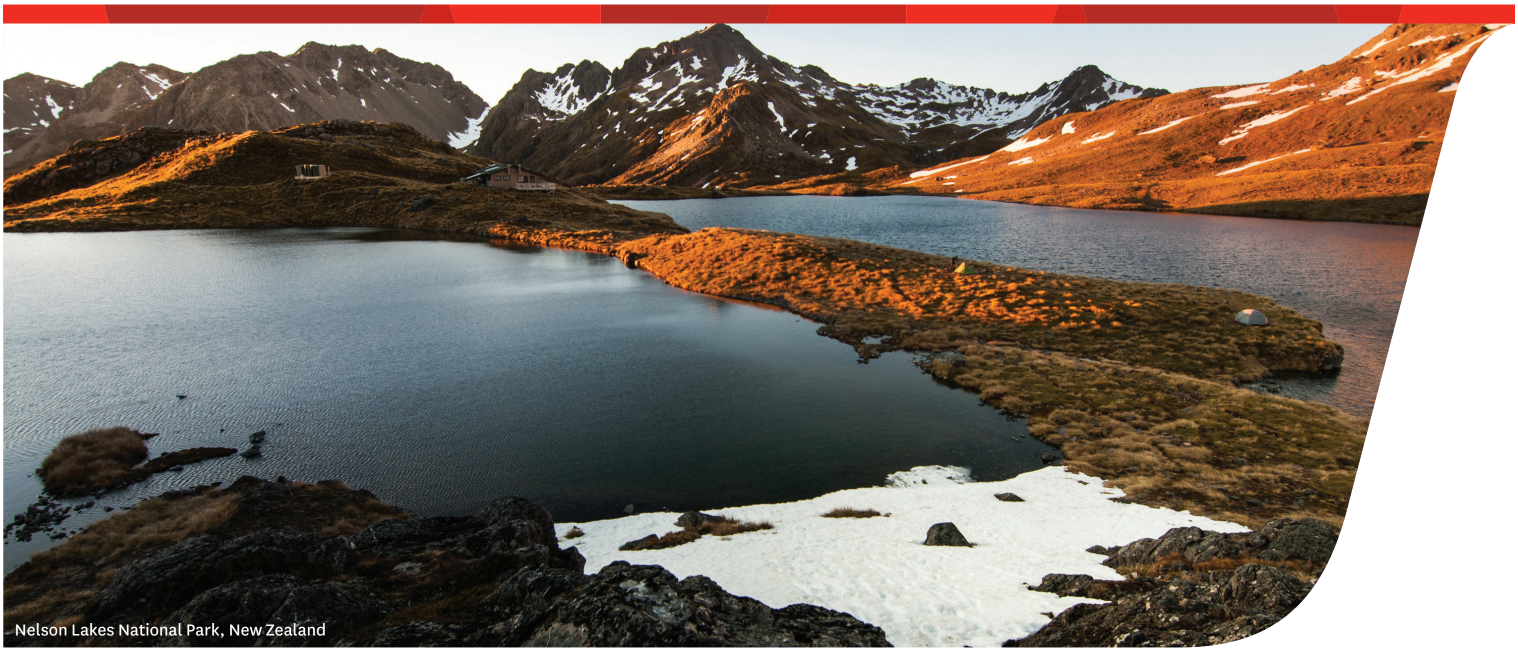


Nelson Lakes National Park, New Zealand

Weekly Economic Commentary.

The flood of returning New Zealanders has ended.

Rapid population growth on the back of high levels of net migration played a key role in shaping New Zealand's economic fortunes in recent years. However, following the outbreak of Covid-19, the inflow of people into the country has come to an abrupt halt. And with the virus continuing to spread abroad, migration and population growth are likely to remain very low for some time yet. That will severely curtail one of the major drivers of economic growth in recent years. It will also dampen demand in the housing and construction sectors, and will have important implications for the labour market.

The start of this year saw population growth surge as the Covid outbreak spread around the globe and large numbers of New Zealanders returned from abroad.

However, that surge in migration inflows has now come to a screeching halt. In fact, the number of New Zealand citizens and residents returning home each month has fallen to just one-third of normal levels. At the same time, the closure of our borders has meant that the flow of new foreign citizens arriving in the country has also dried up.

Those reduced inflows have been matched by a reduction in the number of people departing our shores. Together, these developments have seen monthly net migration slowing from an average of around 4,500 to effectively zero since April of this year.

Looking ahead, if our borders remain closed, the slowdown in net migration would result in population growth falling from rates of close to 2% now to around 1% over the next few years. And with population a major driver of New Zealand's business cycle, that heralds some big changes in the economic backdrop.

The impact of lower migration and population growth will be especially evident in consumer spending. In recent years, population gains have been a significant boost to spending on items like groceries and household furnishings, as well as spending on hospitality and other services. However, looking to the next few years, many businesses in those same sectors will find that growth in their demand base is much more gradual.

The downturn in population growth will also be an important influence on the housing market and construction. In broad terms, lower migration means that we'll need fewer houses than would have otherwise been the case. There will also be less pressure on rents.

However, recent developments do need to be put into context. New Zealand is still wrestling with a significant shortage of housing. In fact, compared to the increases in our population, we estimate that New Zealand has built around 50,000 too few homes since 2013.

It's also important to remember that while slower population growth does point to less pressure on house prices, it's not the only factor that affects New Zealand's housing market. The RBNZ's easing in monetary policy settings and related falls in mortgage rates have supported a sharp rise in demand from both first home buyers and investors. That's resulted in house prices pushing higher in recent months in spite of the headwinds buffeting the economy. We expect that house prices will rise by 6.3% over calendar 2020 and have pencilled in another 8% rise over 2021.

The sharp downturn in population growth now in train, as well as the broader uncertainty around the economic outlook, will reduced the demand for new dwellings. As a result, we expect that residential construction will fall to about 10% below pre-Covid levels over the coming year. However, that's actually a more moderate decline than we initially expected when Covid-19 first arrived on our shores. In part, that's because New Zealand was able to restrict the spread of the virus faster than we dared hope. And since that time, the strengthening in the housing market is likely to have assuaged some of developers' concerns about demand, which will help to further bolster building levels. Consistent with that, we've actually seen consent issuance hold at strong levels in recent months.

Of course, migration doesn't just affect demand. It's also an important influence on our productive capacity with many businesses sourcing the skilled labour they need from overseas. The closure of our boarders has meant that businesses in a number of industries are now finding it harder to match job openings with available workers. That will be a drag on New Zealand's productivity. And for many businesses, it will also mean higher wage costs. Such pressures are more pronounced in highly specialised sectors like construction, but are also being seen in less specialised industries.

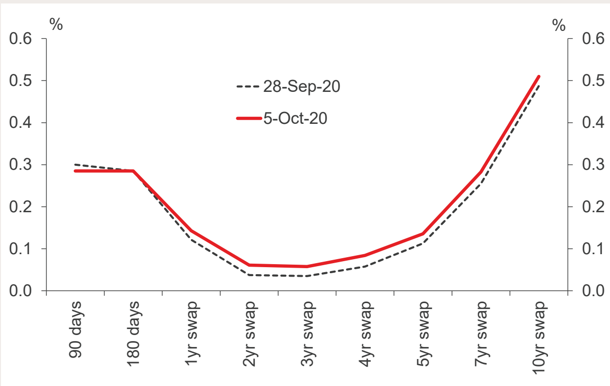
The combination of rising wage costs and lower productivity on top of the Covid related headwinds already buffeting the economy will be a drag on employment growth. But while the downturn in the economy will reduce the total number of jobs available, New Zealanders often compete for jobs with workers from abroad. Now, with those foreign workers shut out of the New Zealand market, local workers in industries like fruit picking will face less competition for the available jobs. For many lower skilled New Zealanders, that's an important development in terms of their employment prospects, incomes and potentially their overall levels of wellbeing. Longer term, this could also help with the development of skills among domestic workers.

For specialised and higher skilled workers, the implications are more mixed. These workers also compete for plumb jobs with skilled workers from abroad, and many will now find their skills are in hot demand from employers. However, such workers also often travel abroad for high paid jobs or work experience. In many cases, such job opportunities are now off the table and they're likely to remain so for some time yet.

Fixed vs Floating for mortgages.

Fixed mortgage rates fell sharply over May and June, but are stable now and don't look likely to move much in the short run. However, in November we expect the Reserve Bank will introduce a Funding for Lending Programme, the aim of which is to reduce retail interest rates. At that time, we expect that both fixed and floating mortgage rates will fall. How far they fall will depend on the details of the Reserve Banks programme, which are not known at this stage.

NZ interest rates



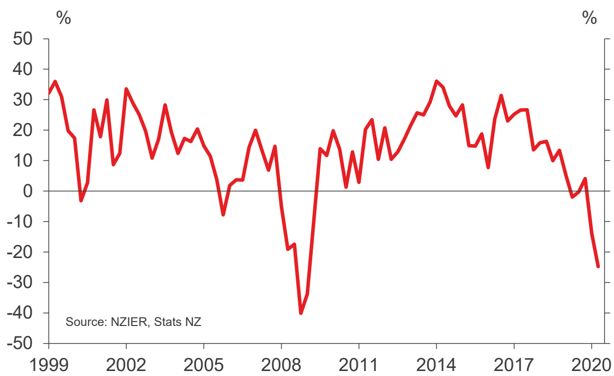
The week ahead.

NZ Q3 Survey of Business Opinion

Oct 6, General business situation, Last: -58.8
Domestic trading activity (past 3 mths), Last: -37.1

- Business confidence fell sharply in the June quarter as Covid-19 and related health restrictions dampened activity. Against that backdrop, businesses also scaled back their plans for investment and hiring
- Since the June survey, activity restrictions have been rolled back and economic activity has been bouncing back faster than expected. We expect that those developments will be reflected in a sharp rise in business conditions in the September QSBO survey. Nevertheless, activity and confidence are still expected to remain below pre-Covid levels. Hiring and investment intentions are also likely to remain subdued.

QSBO domestic trading activity (next 3 mths)

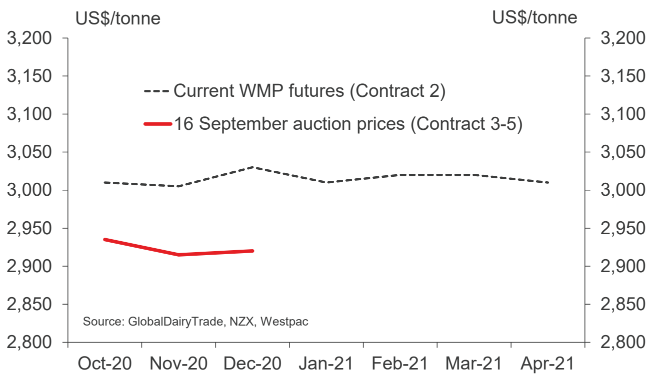


NZ GlobalDairyTrade auction, whole milk powder prices

Oct 7, Last: +3.2% chg, Westpac: +1.0%

- We expect whole milk powder prices to lift a touch at this auction and build on the previous lift. Prices also rose 3.2% at the previous auction.
- We are marginally more bearish than the dairy futures market. It is pointing to a slightly larger price lift of around 2% as at the time of writing.
- Over the coming months, New Zealand's spring weather and its impact on growing conditions will be a key factor for prices either way.

Whole milk powder prices

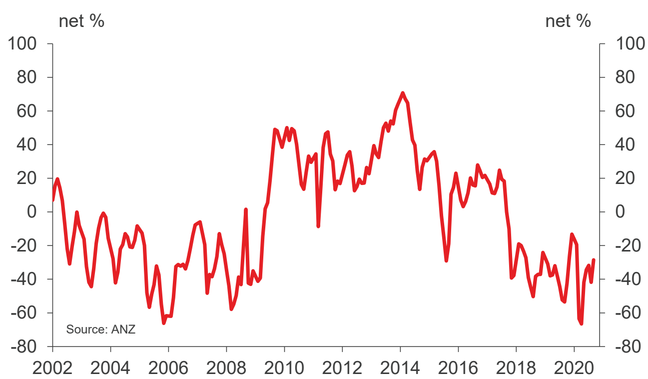


NZ Oct ANZBO business confidence (flash)

Oct 8, Last: -28.5

- Business confidence unexpectedly rose in September. That was despite the re-emergence of Covid-19 on our shores. Although business conditions remain subdued, they have not been as weak as feared. That's consistent with a range of other economic indicators which suggest that the New Zealand economy is weathering the Covid storm better than expected.
- We expect the October survey will show that business confidence remains below pre-Covid levels. However, following the recent dialling down of the Alert Level, we expect that activity gauges will continue to gradually firm.

NZ business confidence



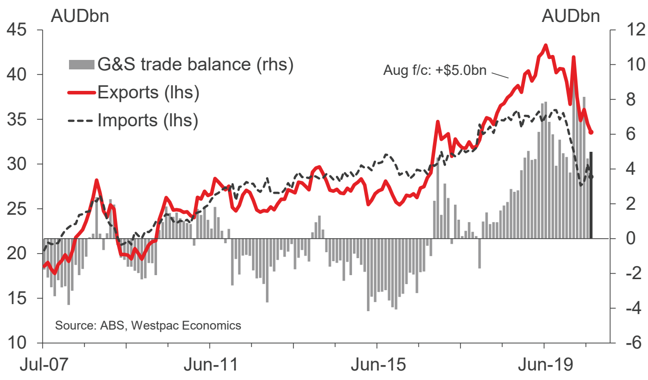
The week ahead.

Aus Aug trade balance, AUD

Oct 6, Last: 4.6, WBC f/c: 5.0
Mkt f/c: 5.0, Range: 3.0 to 5.8

- Australia is still running sizeable trade surpluses, albeit down from the highs earlier in the year.
- For August, the surplus is expected to widen a little, to a forecast $5.0bn, up from $4.6bn in July. That compares with an $8.5bn average for the four months March to June.
- Imports spiked in July, +6.8%, representing a catch-up after supply disruptions earlier in the year. A reversal is evident in August, customs data suggests. We anticipate a fall of -4.4%.
- Exports have not been immune from the global recession, with weaker demand hitting shipments and prices for LNG and coal. Over July and August, gold volatility was a factor - a spike, then a reversal. On the services side, closure of the international border is impacting the education sector. All up, export earnings are forecast to moderate, down by -2.7%.

Australia's trade balance

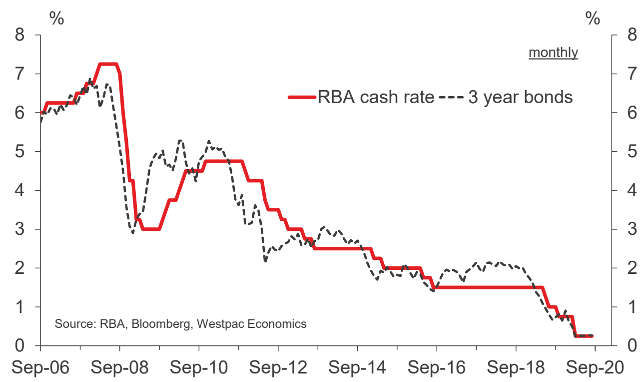


Aus RBA policy decision

Oct 6, Last: 0.25%, WBC f/c: 0.25%
Mkt f/c: 0.25%, Range: 0.10% to 0.25%

- The RBA eased policy in March, introducing a package of measures, including lowering the cash rate to 0.25% and introducing a target for the 3 yr government bond, at 0.25%.
- The Bank then eased policy further in September and is poised to make yet another move - but we assess that the timing of that is likely to be after the Federal Budget. That said, a few commentators are calling an October cut.
- In September, the Term Funding Facility was boosted - both expanding and extending the fund.
- Westpac expects the RBA to announce another round of policy easing - likely in November - lowering interest rates (including trimming the cash rate and the 3 year bond target to 0.10%) and expanding the bond buying program. For further detail on the expected package, see our update from September 23.

RBA cash rate and 3 year bonds

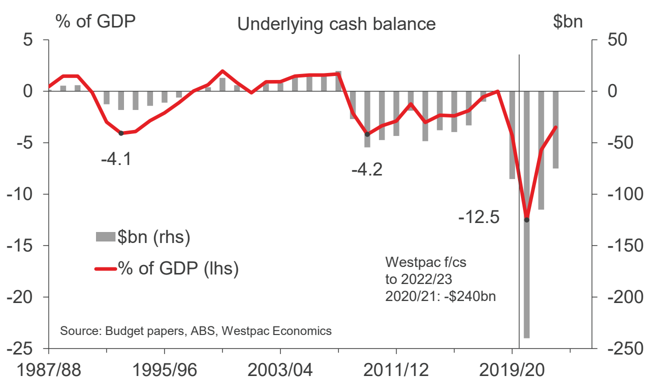


Aus Federal Budget, 2020, $bn

Oct 6, Last: -85.3, WBC f/c: -240

- The 2020 Federal Budget is a budget like no other.
- The deficit has ballooned to a forecast $240bn (12.5% of GDP) for 2020/21, from $85.3bn for 2019/20 and a balance budget in 2018/19.
- The reason of course is the Covid pandemic, the ensuing severe recession and the necessary policy response.
- The deficit is then expected to narrow to $115bn in 2021/22 as the economy reopens and activity rebounds.
- Policy measures add an expected $179bn to the budget in 2020/21 and $73bn in 2021/22. This includes an expected October Budget package of $45bn for this year and $66bn for 2021/22.
- The key budget strategy is to lift the economy to a higher growth path, enabling progress to be made in reducing the unemployment rate.

Aus Federal budget



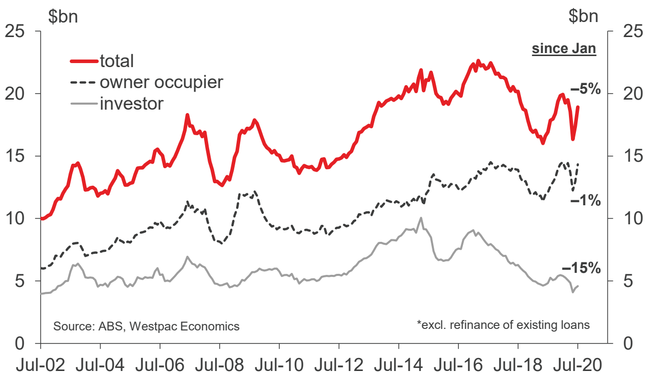
The week ahead.

Aus Aug housing finance approvals

Oct 9, Last: 8.9%, WBC f/c: –1.5%
Mkt f/c: 1.0%, Range: -2.0% to 8.1%

- Housing finance approvals posted a strong rebound through June-July, the total value of approvals rising 15.8% to be just 3% below pre-COVID levels. Remarkably, the value of total approvals ex refi is up 11.8%yr.
- Overall, the shock to finance activity from COVID-19 disruptions has been relatively mild and short-lived, particularly compared to the likes of turnover.
- This broad theme is expected to carry into August, albeit with some renewed weakness associated with Victoria's second lock-down.
- That said, there is some uncertainty around the monthly move with reopening continuing in other states, some boost likely from the HomeBuilder scheme and potential lags in the way all of these factors play through to financing activity (e.g. the bulk of the impact from the wider lockdown back in April came through in May). On balance, we expect the total value of approvals to decline by 1.5%.

Aus new finance approvals*

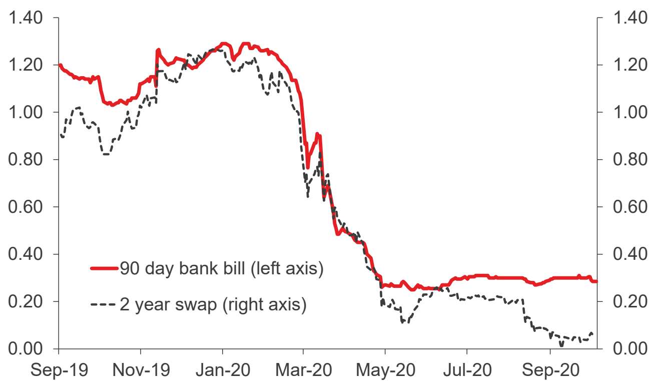


New Zealand forecasts.

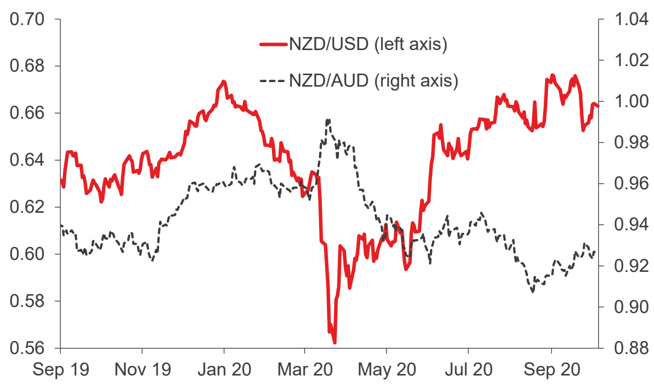
Economic forecasts	Quarterly				Annual			
	2020			2021				
% change	Jun (a)	Sep	Dec	Mar	2018	2019	2020f	2021f
GDP (Production)	-12.2	8.5	3.7	0.5	3.2	2.3	-5.1	6.0
Employment	-0.4	-2.8	-1.0	0.2	1.9	1.0	-3.2	1.8
Unemployment Rate % s.a.	4.0	5.5	6.2	6.6	4.3	4.1	6.2	6.5
CPI	-0.5	0.6	-0.1	0.1	1.9	1.9	0.8	0.5
Current Account Balance % of GDP	-1.9	-1.2	-1.2	-1.6	-4.3	-3.4	-1.2	-3.6

Financial forecasts	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Jun-22
Cash	0.25	0.25	-0.50	-0.50	-0.50	-0.50
90 Day bill	0.30	-0.10	-0.20	-0.20	-0.20	-0.10
2 Year Swap	0.05	0.00	-0.10	-0.10	-0.10	0.10
5 Year Swap	0.20	0.20	0.20	0.25	0.35	0.55
10 Year Bond	0.60	0.65	0.70	0.75	0.80	1.00
NZD/USD	0.67	0.66	0.66	0.68	0.70	0.70
NZD/AUD	0.89	0.87	0.87	0.87	0.88	0.88
NZD/JPY	70.4	69.3	70.0	72.1	74.2	74.9
NZD/EUR	0.55	0.54	0.54	0.55	0.56	0.56
NZD/GBP	0.50	0.49	0.49	0.50	0.50	0.50
TWI	71.5	69.9	69.5	70.7	72.0	71.7

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 5 October 2020

Interest rates	Current	Two weeks ago	One month ago
Cash	0.25%	0.25%	0.25%
30 Days	0.28%	0.28%	0.28%
60 Days	0.26%	0.29%	0.29%
90 Days	0.29%	0.30%	0.30%
2 Year Swap	0.06%	0.05%	0.06%
5 Year Swap	0.14%	0.13%	0.14%

NZ foreign currency mid-rates as at 5 October 2020

Exchange rates	Current	Two weeks ago	One month ago
NZD/USD	0.6630	0.6756	0.6719
NZD/EUR	0.5665	0.5703	0.5672
NZD/GBP	0.5131	0.5225	0.5074
NZD/JPY	69.83	70.60	71.41
NZD/AUD	0.9258	0.9271	0.9219
TWI	71.73	72.70	72.48

Data calendar.

		Last	Market median	Westpac forecast	Risk/Comment
Mon 05					
NZ	Sep ANZ commodity prices	–0.9%	–	–	Commodity prices a touch stronger over the month.
Aus	Public holiday in some states	–	–	–	Labour Day NSW, ACT. Queen's Birthday Qld.
	Sep MI inflation gauge	1.3%	–	–	Subdued and impacted by Covid.
Eur	Sep Markit services PMI	47.6	–	–	Reimposed restrictions a risk for activity...
	Oct Sentix investor confidence	–8	–	–	...6–month economic outlook is challenging.
	Aug retail sales	–1.3%	–	–	Signs of recovery in May–June, but weakened in July.
UK	Sep Markit services PMI	55.1	–	–	Ongoing health concerns a material risk to recovery.
US	Sep Markit services PMI	54.6	54.6	–	New business has been expanding at a robust pace...
	Sep ISM non–manufacturing	56.9	56.3	–	...as the economy continues to reopen.
	Fedspeak	–	–	–	FOMC's Evans and Bostic.
Tue 06					
NZ	Q3 QSBO survey business opinion	–58.8	–	–	Expected to rebound after last quarter's Covid–related fall.
Aus	Aug trade balance $bn	4.6	5.0	5.0	Imports down, reversing July spike.
	Sep AiG PCI	37.9	–	–	Construction –4.8pts in Aug, hit by Victorian lock–down.
	Sep ANZ job ads	1.6%	–	–	Labour market stress evident.
	RBA policy announcement	0.25%	0.25%	0.25%	Poised to ease further – November more likely timing.
	Federal Budget, 2020, $bn	–85.3	–	–240	Budget hit by recession & policy response.
US	Aug trade balance US$bn	–63.6	–66.1	–	Largest trade deficit since July 2008.
	Aug JOLTS job openings	6618	6500	–	Business recovery supporting job openings.
	FOMC Chair Powell	–	–	–	Address to NABE Conference in Chicago.
	Fedspeak	–	–	–	FOMC's Harker and Bostic.
Wed 07					
NZ	GlobalDairyTrade auction (WMP)	3.2%	–	1.0%	We expect another positive result at this dairy auction.
Aus	Sep AiG PSI	42.5	–	–	Services –1.5pts in Aug, again hit by Victorian lock–down.
Chn	Sep foreign reserves $bn	3,164	3,159	–	Hit 4 year high in Sep, supported by weakening dollar.
US	Aug consumer credit $bn	12.25	14.50	–	Rebound continuing, driven by auto sales.
	Sep FOMC Meeting Minutes	–	–	–	Focus on new policy framework and view of risks.
	Fedspeak	–	–	–	Kaplan, Rosengren, Bostic, Kashkari, Williams and Evans.
Thu 08					
NZ	Oct ANZ business confidence	–28.5	–	–	Expected to pick up, but remain below pre–Covid levels.
Chn	Sep Caixin China PMI services	54.0	54.3	–	Comfortably in expansionary territory as new orders rise.
US	Initial jobless claims	837k	–	–	Remain elevated; continuing claims show loss of access.
Fri 09					
Aus	RBA Financial Stability Review	–	–	–	Half yearly update.
	Aug housing finance	8.9%	1.0%	–1.5%	Housing finance snap back faulted in August...
	Aug owner occupier finance	10.7%	–1.5%	–1.0%	...as Victoria went into a second lock–down...
	Aug investor finance	3.5%	–	–3.0%	...weakness to be led by investor segment.
UK	Aug trade balance GBPmn	1074	–	–	Weak domestic demand restricting goods imports.
US	Aug wholesale inventories	0.5%	–	–	Inventories to be a big positive for GDP growth in Q3.

International forecasts.

Economic forecasts (Calendar years)	2016	2017	2018	2019	2020f	2021f
Australia						
Real GDP % yr	2.8	2.4	2.8	1.8	-3.3	2.3
CPI inflation % annual	1.5	1.9	1.8	1.8	0.4	2.2
Unemployment %	5.7	5.5	5.0	5.2	7.7	7.6
Current Account % GDP	-3.1	-2.6	-2.1	0.6	2.6	0.1
United States						
Real GDP %yr	1.6	2.4	2.9	2.3	-4.7	3.4
Consumer Prices %yr	1.4	2.1	2.4	1.9	1.1	1.8
Unemployment Rate %	4.9	4.4	3.9	3.7	8.8	7.9
Current Account %GDP	-2.3	-2.3	-2.3	-2.6	-2.5	-2.4
Japan						
Real GDP %yr	0.5	2.2	0.3	0.7	-5.2	1.5
Euro zone						
Real GDP %yr	1.9	2.5	1.9	1.2	-7.6	5.4
United Kingdom						
Real GDP %yr	1.9	1.9	1.3	1.4	-11.0	7.0
China						
Real GDP %yr	6.8	6.9	6.8	6.1	2.5	10.5
East Asia ex China						
Real GDP %yr	4.1	4.6	4.4	3.7	-2.3	5.2
World						
Real GDP %yr	3.4	3.9	3.6	2.8	-3.8	5.8
Forecasts finalised 9 September 2020						

Interest rate forecasts	Latest	Dec–20	Mar–21	Jun–21	Sep–21	Dec–21	Jun–22
Australia							
Cash	0.25	0.10	0.10	0.10	0.10	0.10	0.10
90 Day BBSW	0.09	0.05	0.05	0.05	0.05	0.10	0.20
10 Year Bond	0.85	0.80	0.90	1.00	1.05	1.15	1.25
International							
Fed Funds	0.125	0.125	0.125	0.125	0.125	0.125	0.125
US 10 Year Bond	0.68	0.60	0.65	0.75	0.75	0.85	0.95

Exchange rate forecasts	Latest	Dec–20	Mar–21	Jun–21	Sep–21	Dec–21	Jun–22
AUD/USD	0.7173	0.75	0.76	0.76	0.78	0.80	0.80
USD/JPY	105.55	105	105	106	106	106	107
EUR/USD	1.1736	1.21	1.22	1.23	1.24	1.25	1.25
GBP/USD	1.2881	1.33	1.34	1.35	1.37	1.39	1.40
USD/CNY	6.7908	6.75	6.75	6.70	6.60	6.50	6.40
AUD/NZD	1.0795	1.12	1.15	1.15	1.15	1.14	1.14

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