



Mt. Taranaki, Mt. Egmont National Park.

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The verdict is in

There was a notably widespread downturn across the range of activity indicators for the New Zealand economy in April, which we suggested at the time could be a temporary blip caused by the close timing of the Easter and Anzac Day holidays this year. With an extra month of data now available, the evidence for that theory is supportive, but not decisive. While there was some holiday effect in April, it also seems plausible that there's been a genuine slowing in the economy's momentum over the last few months.

In keeping with that view, last week's data was a mixed bag. On the positive side, residential building consents (excluding the volatile apartment units category, which had spiked in April), rose 4.6% in May. However, that wasn't quite enough to reverse the 5.2% drop in consents in April, and consents were surprisingly flat in the Canterbury region.

Also on the plus side, the credit aggregates showed an uptick in lending growth in May, both for business lending (which had flattened out over the previous few months) and for housing. The latter was consistent with previously published figures on high loan-to-value ratio (LVR) mortgage lending, which rose for a second time in May – though at a 5.3% share of the total, it remains well within the Reserve Bank's 'speed limit' of 10%.

But there were also some substantial negatives added to the mix last week. Firstly, business confidence fell for a fourth straight month in June, after having reached a 20-year high in February this year. While the level of confidence remains high – around where it was in September last year – it provides more evidence of a slowing in the pace of the upturn since the early part of this year.

The verdict is in continued

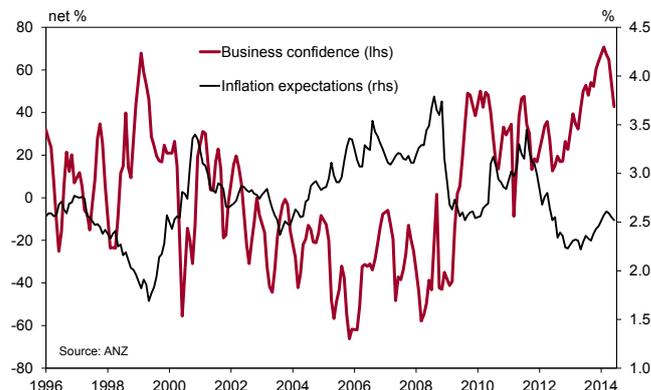
Within the survey, confidence has clearly deteriorated the most in the agricultural sector, which could reflect the substantially lower dairy payout forecast for this season compared to last season's payout of \$8.40/kg. On that note, the 4.9% fall in world dairy prices at last week's GlobalDairyTrade auction is further cause for concern. Prices are now lower than they were last February, before the supply-driven surge in prices began. We'll be reviewing our milk price forecast in coming days, but it's clearly going to be something with a 6 in front, in contrast to our initial forecast of \$7.10/kg.

The data highlight this week is likely to be the NZIER's *Quarterly Survey of Business Opinion* on Tuesday. Whereas the monthly business confidence survey is entirely forward-looking, the *QSBO* also asks about businesses' experiences over the past three months. It's the latter measure – as you might imagine from the description – that provides the single best high-level indicator of what actually happened with GDP in the latest quarter.

We suspect that it will point to something substantially slower than the 1% or so growth recorded in each of the previous three quarters. To the extent that this was a temporary Easter 'blip', the June quarter should mark the low point for GDP growth this year. But with interest rates now rising, dairying incomes dropping back, and the Christchurch rebuild now well advanced (in terms of the level of building activity), our view is that the days of 4% annualised growth have now passed.

The *QSBO* also directly addresses the extent of capacity pressures in the economy – a particularly important point for monetary policy, given the RBNZ's view that the economy is currently running about 1% ahead of its non-inflationary potential level. The March quarter *QSBO* was decidedly mixed on this matter: the number of businesses reporting capacity as their main growth constraint rose to a post-recession high, yet the direct measure of capacity utilisation actually fell below its long-run average. And while pricing intentions have risen sharply in the last few surveys, those intentions have so far been well in excess of what firms have actually been able to achieve.

NZ business confidence and inflation expectations



Fixed vs Floating for mortgages

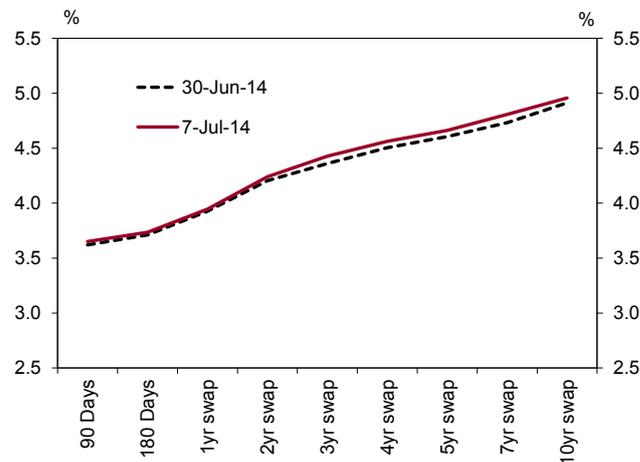
Fixing for two to three years seems likely to prove the cheapest option.

Floating mortgage rates usually work out to be more expensive for borrowers than short-term fixed rates, such as the six month rate. However, floating may still be the preferred option for those who require flexibility in their repayments.

Fixed rates are now on the rise, but in our view 2-3 year rates are still good value, given where we think shorter-term rates are likely to go over the next few years.

Fixing for four or five years may result in higher interest payments over the life of the loan than opting for shorter-term fixed rates. However, these longer-term fixed rates may still be preferred by those who are willing to pay for certainty.

NZ interest rates

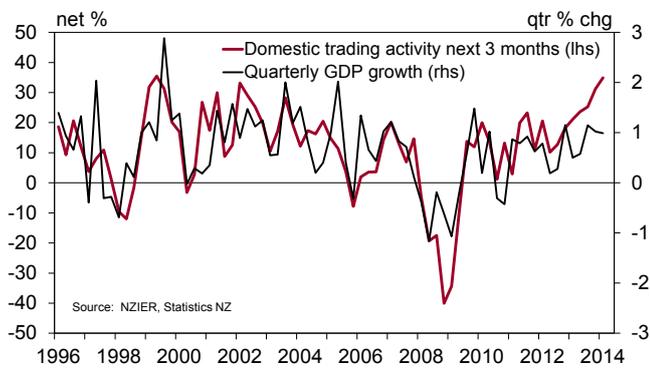


NZ Q2 NZIER business opinion

Jul 8, Last: 52

- New Zealand firms were at their most optimistic in 20 years in the March Quarterly Survey of Business Opinion, an optimism that was later borne out by a third straight quarter of 4% annualised GDP growth in the March quarter.
- Recent indicators suggest we'll see a softer tone to the June survey. In particular, firms' experiences of the last three months will provide more evidence on the extent to which activity was dented by the slowdown over the Easter holiday period.
- With the economy's upturn well established, evidence of capacity constraints is taking on more importance. The March quarter survey provided mixed messages on this front.

QSBO domestic trading activity and GDP

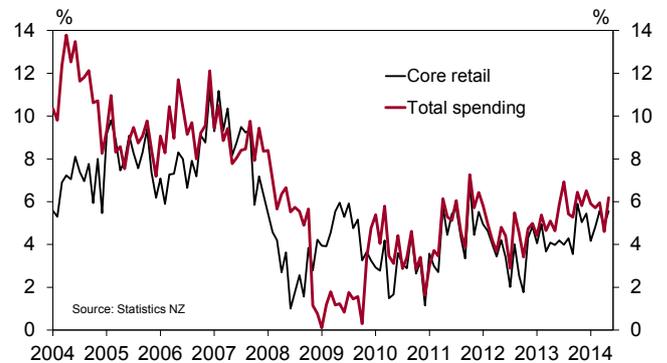


NZ June electronic card transactions

Jul 9, Last 1.7%, WBC f/c: 0.6%

- Electronic card spending rebounded very strongly in May - at least partly reflecting the unusual timing of Easter and Anzac day this year, which seems to have depressed some components of spending in April.
- However, taking April and May together raises the possibility that momentum may have picked up a little in the June quarter, albeit not to the speed seen late last year. With interest rates rising, a cooler housing market and consumer confidence slightly off its recent peak, we expect the underlying trend in spending to have slowed this year.
- Advance spending figures from Paymark (New Zealand's biggest cards processor) are likely to be published ahead of the release. These are a good, though not foolproof, guide.

Card transactions, annual % change

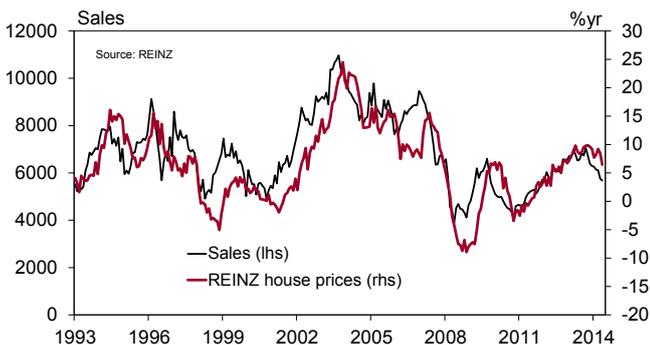


NZ Jun REINZ house prices and sales

Jul 11 (tbc), Last: Sales: -1.3%, Prices: 6.5%/yr

- House sales were surprisingly soft in May, with no sign of a post-Easter recovery. Evidence for June - mortgage approvals and reports from regional real estate agencies - suggests a modest lift in sales, but the trend clearly remains weak.
- The message on prices has been more muddled. The REINZ stratified price index fell 1.1% in May, but this followed some surprisingly strong gains in the previous three months. We regard the QV index (due Monday) as the more reliable measure of prices, but it's a little slower to pick up turning points in the cycle.
- Note that the target for the REINZ release is by the 10th working day of the month, which suggests late this week or early next week. However, actual release dates have been highly variable lately.

REINZ house prices and sales



Aus Jul Westpac-MI Consumer Sentiment

Jul 9 Last: 93.2

- At 93.2, the Westpac-Melbourne Institute Consumer Sentiment Index remained lodged in pessimistic territory in Jun, recovering only slightly (+0.2%) from the heavy post-Budget fall in May (-6.8%).
- The evidence from previous Budget-related falls shows it can often take several months for sentiment to fully recover. Accordingly the Jul, Aug and Sep reads will be key to judging the degree to which the fall may affect consumer behaviour. The Jul survey is in the field in the week to July 5. Other factors that may influence sentiment in the month include: the RBA's decision to keep rates on hold; a speech by Governor Stevens warning of potential falls in the AUD and singling out Sydney's investor housing segment as an area to 'watch'; weaker than expected May retail sales but more positive data on house prices (+1.4%/mth in Jun vs -1.9%/mth in May).

Consumer Sentiment Index

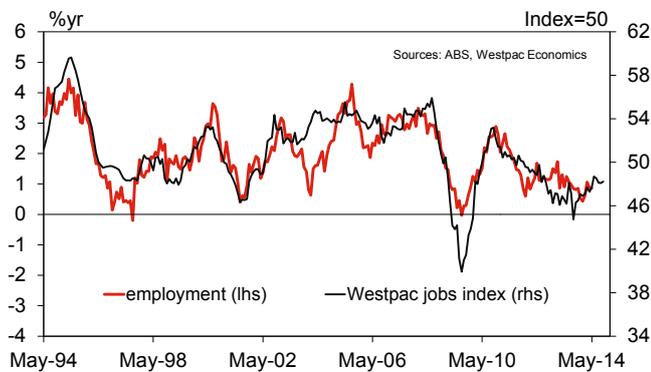


Aus June labour force, total employment

Jul 10, Last: -4.8k, WBC f/c: 25.0k
Mkt f/c: 12k, Range: -4.7k to 35k

- Total employment surprised by contracting 4.8k in May and Apr was revised to +10.3k from 14.2k. We suspect that sample volatility may have played a role in this weaker than expected print. Why? There was also a fall in the participation rate, to 64.6% from 64.7%.
- We are, however, cautious with this analysis as the gross flows data suggests hiring has eased back while separations have lifted, consistent with the softer employment outcomes.
- Total employment grew an average of just 9.4k per month in the three months to May. This is a little soft given the leading indicators hence our forecast for a +25k which marginally lifts the annual pace to 1.0%/yr from 0.9%/yr, for an average gain of 10.2k in the three months to June.

Westpac jobs index suggests momentum continues

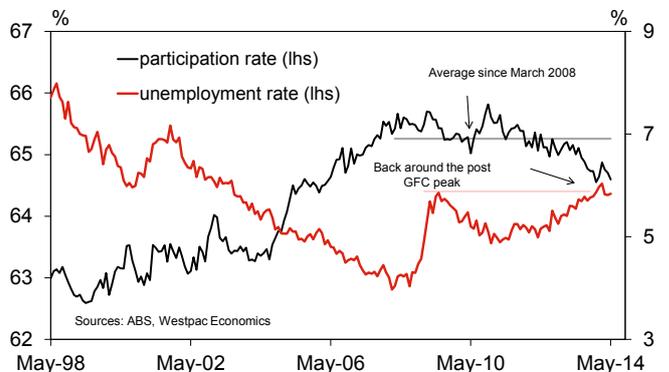


Aus June labour force, unemployment

Jul 10, Last: 5.8%, WBC f/c: 5.9%
Mkt f/c: 5.9%, Range: 5.8% to 6.0%

- Normally, you would expect that even a small fall in employment would lead to a rise in unemployment as this is much less than the around 30k per month growth in the working age population. However, the fall in the participation rate was enough to see the labour force fall 1.7k thus resulting in a flat unemployment rate of 5.8%.
- An ageing population has been driving down the participation rate. In fact, the flow of workers aged 55 to 65 out of the workforce may explain up to a 0.1ppt fall in participation per month over the last three months.
- We are therefore forecasting only a small rise in participation in June, from 64.6% to 64.7%, which will be enough to result in a rise in the unemployment rate to 5.9%.

Unemployment and participation rates

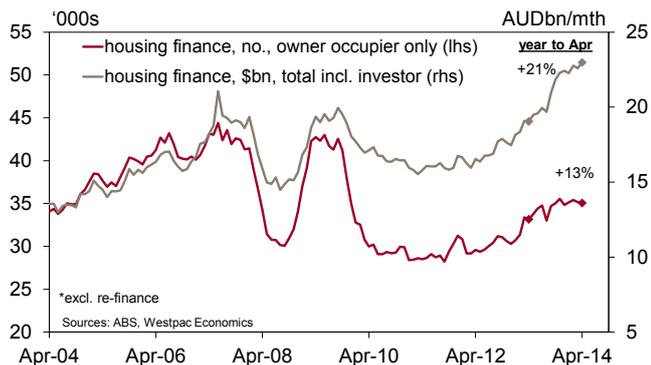


Aus May housing finance (no.)

Jul 11, Last: flat, WBC f/c: -0.5%
Mkt f/c: -0.5%, Range: -2.0% to 2.4%

- Housing finance has shown clear signs of cooling off in 2014. The number of owner-occupier approvals was unchanged in Apr after a 0.8% decline in Mar and a flat 3mths prior to that. Approvals had surged 15% in the 12mths before this period. Note that this excludes investor approvals which are only captured in the totals for the value of approvals.
- Industry figures suggest approvals continued to slow in May. We expect owner-occupier finance approvals to be down 0.5% in the month. The later timing of Easter this year did not appear to have much impact on approvals in Apr. Housing finance approvals are likely to show a more pronounced weakening in coming months as sharp declines in consumer assessments of 'time to buy a dwelling' feed through.

New finance approvals



Data calendar

		Last	Market median	Westpac forecast	Risk/Comment
Mon 7					
Aus	Jun ANZ job ads	-5.6%	-	-	Job ads fell in May, -5.6%, largely reversing gains earlier in the year.
Eur	Jul Sentix investor confidence	8.5	-	5.5	Stock mkt correction, Jul ECB meeting, US payrolls data: all factors.
Ger	May industrial production	0.2%	0.2%	-0.5%	Orders down 1.2% in March-April; factory PMI at 2014 low in May.
Can	May building permits	1.1%	3.0%	-	Sharp falls in permits earlier this year only partially reversing.
	Jun Ivery PMI	48.2	-	53.0	Down March-May to close to cycle lows; bounce usually follows.
	Q2 BoC senior loan officer survey	-10.9	-	-	Credit availability relatively easy though not as loose as in 2011.
	Q2 business outlook survey	27	-	-	Future sales index.
Tue 8					
NZ	Q2 NZIER business opinion	52	-	-	Momentum appears to have peaked earlier in the year.
Aus	Jun NAB business survey	-1	-	-	In May, conditions index fell 1pt to -1, confidence steady at +7.
Ger	May exports	2.9%	-	-0.5%	If IP is down, exports are unlikely to sustain Apr bounce from Q1 fall.
UK	May industrial production	0.4%	0.2%	-0.4%	Manufacturing solid but IP constrained by utilities (weather), mining.
US	Jun NFIB small business optimism	96.6	97.0	-	ISM surveys of big business in June were broadly unchanged from May.
	May consumer credit \$bn	26.8	20.0	-	Student and auto loans now joined by renewed credit card use.
	Fedspeak	-	-	-	Lacker, Kocherlakota.
Wed 9					
NZ	June electronic card transactions	1.7%	-	0.6%	A clearer read following May's post-Easter bounce.
Aus	Jul Westpac-MI Consumer Sentiment	93.2	-	-	Has often been slow to recover from Budget-related falls in the past.
	Jul Westpac-MI unemploy. expect.	156.5	-	-	Down 1.1% in Jun & 4.8% below Mar peak, but trend 22% above 10yr avg
	Jul MI inflation expectations	4.0%	-	-	Down 0.4ppts to 4.0% in May, below LR avg of 4.5%. Trend flat @ 4.2%.
Chn	Jun PPI %yr	-1.4%	-1.0%	-	Deflationary impulse in intermediate goods has lessened of late.
	Jun CPI %yr	2.5%	2.5%	-	Food prices lifted a month ago, but shelter heading the other way.
UK	Jun BRC shop price index %yr	-1.4%	-	-	Further rise from -1.7% in Mar would signal turning point in CPI.
US	June 17-18 FOMC minutes	-	-	-	A range of views re when rates might rise since the meeting.
Can	Jun housing starts	13.8%	-4.2%	-	Single family starts up in Apr-May; multiples volatility a driver too.
Thu 10					
NZ	Jun manufacturing PMI	52.7	-	-	May was the least positive reading since 2012.
Aus	May employment, chg	-4.8k	12k	25k	The leading indicators suggests momentum should be a little stronger.
	May unemployment rate	5.8%	5.9%	5.9%	A small rise in participation is enough to lift unemployment.
Chn	Jun trade balance USDbn	35.92	36.95	-	Import weakness of May could be repeated, exports look more secure.
	Jun new bank loans RMBbn	871	955	-	Tentative date. Bank loans increasing TSF share in year to date.
	Jun total credit supply RMBbn	1400	1400	-	Tentative date. Modest improvement of late as policy stance shifts.
	Jun money supply M2 %yr	13.4%	13.5%	-	Tentative date. Capital inflows modest, nominal activity likewise.
UK	Jun house prices net balance	57%	55%	-	RICS surveyors series remains close to 58% peak in March.
	May trade balance £bn	-8.9	-9.0	-	Exports down 1.4% and imports up 0.8% saw Apr deficit widen.
	Bank of England rate decision	0.50%	0.50%	0.50%	Some members seem to be edging towards policy tightening but
	BoE asset purchase program £bn	375	375	375	still in minority; recent message from Carney somewhat unclear.
US	Initial jobless claims w/e Jul 5	315k	315k	-	Claims about to be impacted by summer auto plant shutdowns.
	May wholesale inventories	1.1%	0.6%	0.4%	Steadier gasoline prices will constrain inventories rise.
	Fedspeak	-	-	-	George.
Can	May new house prices	0.2%	-	-	Running < 2% yr annual pace since April last year; 1.6% yr in Apr 14.
Fri 11					
NZ	Jun food price index	0.6%	-	1.6%	Annual food price inflation is starting to tick higher again.
	Jun REINZ house sales	-1.3%	-	-	Release date not confirmed. Sales down 19% since Sep.
	Jun REINZ house price index %yr	6.5%	-	-	Prices have been volatile, but appear to be slowing.
Aus	May housing finance	flat	-0.5%	-0.5%	Clear signs of cooling off after strong 2013; headline excludes investors.
UK	May construction output	1.2%	-	0.3%	Data noisy month to month; construction PMI off Jan high.
US	Jun federal budget \$bn	96.0	79.0	-	Budget deficit running \$190bn lower on ytd basis in May.
	Fedspeak	-	-	-	Lockhart, Evans.
Can	Jun employment ch ¹	26k	26k	-15k	Jobs growth trend Dec-May slowed to 3k from 11k in Jun-Nov 13.

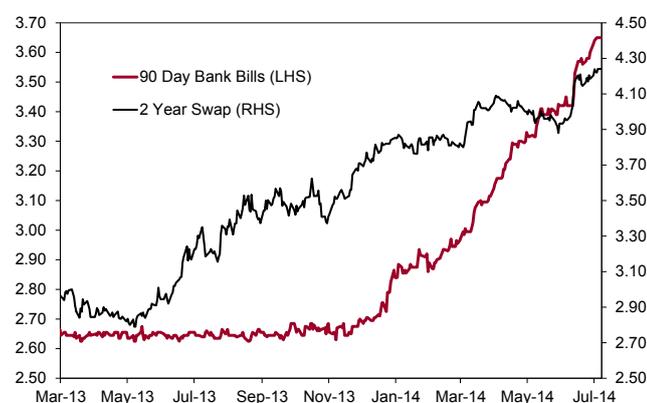


New Zealand forecasts

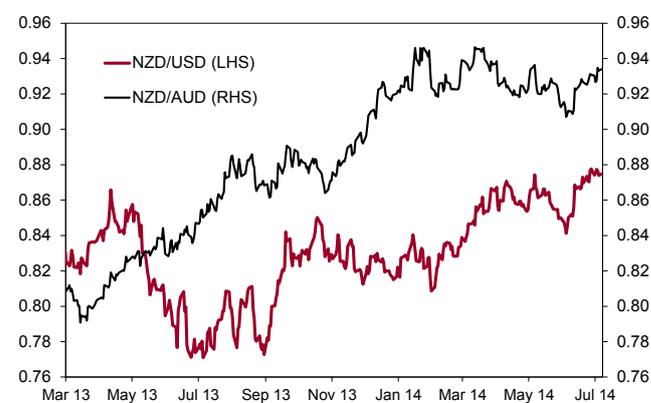
Economic Growth Forecasts	March years				Calendar years			
	2013	2014e	2015f	2016f	2012	2013	2014f	2015f
% change								
GDP (Production) ann avg	2.3	3.3	3.7	3.1	2.5	2.9	3.8	3.2
Employment	0.4	3.8	2.5	2.0	0.4	2.9	2.9	2.4
Unemployment Rate % s.a.	6.2	6.0	5.3	4.9	6.8	6.0	5.5	4.9
CPI	0.9	1.5	1.9	2.6	0.9	1.6	1.7	2.6
Current Account Balance % of GDP	-3.9	-2.8	-3.9	-4.4	-4.1	-3.4	-3.0	-4.6

Financial Forecasts	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15
Cash	3.50	3.75	4.25	4.25	4.50	4.50
90 Day bill	3.70	4.00	4.30	4.45	4.60	4.75
2 Year Swap	4.40	4.60	4.80	4.90	5.00	5.10
5 Year Swap	4.80	5.00	5.10	5.20	5.30	5.40
10 Year Bond	4.60	4.80	4.90	5.00	5.05	5.10
NZD/USD	0.86	0.85	0.84	0.84	0.84	0.84
NZD/AUD	0.95	0.94	0.93	0.91	0.90	0.89
NZD/JPY	86.9	85.0	84.8	85.7	86.5	87.4
NZD/EUR	0.65	0.65	0.65	0.64	0.64	0.64
NZD/GBP	0.52	0.51	0.49	0.47	0.47	0.47
TWI	81.2	80.6	79.7	79.1	79.0	78.7

2 Year Swap and 90 Day Bank Bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on Monday 7 July 2014

Interest Rates	Current	Two weeks ago	One month ago
Cash	3.25%	3.25%	3.00%
30 Days	3.51%	3.42%	3.03%
60 Days	3.59%	3.49%	3.11%
90 Days	3.65%	3.57%	3.42%
2 Year Swap	4.24%	4.15%	3.95%
5 Year Swap	4.66%	4.53%	4.41%

NZ foreign currency mid-rates as at Monday 7 July 2014

Exchange Rates	Current	Two weeks ago	One month ago
NZD/USD	0.8749	0.8702	0.8501
NZD/EUR	0.6435	0.6403	0.6231
NZD/GBP	0.5097	0.5114	0.5058
NZD/JPY	89.30	88.85	87.13
NZD/AUD	0.9341	0.9284	0.9103
TWI	81.42	80.98	79.25



Economic and Financial Forecasts

Economic Forecasts (Calendar Years)	2010	2011	2012	2013	2014f	2015f
Australia						
Real GDP % yr	2.2	2.6	3.6	2.4	3.2	3.0
CPI inflation % annual	2.8	3.0	2.2	2.7	2.5	2.6
Unemployment %	5.2	5.2	5.3	5.8	6.2	5.9
Current Account % GDP	-3.5	-2.8	-4.1	-3.2	-3.0	-2.5
United States						
Real GDP %yr	2.5	1.8	2.8	1.9	1.3	2.5
Consumer Prices %yr	1.6	3.1	2.1	1.5	1.8	1.8
Unemployment Rate %	9.6	8.9	8.1	7.4	6.3	5.8
Current Account %GDP	-3.0	-2.9	-2.7	-2.4	-2.4	-2.4
Japan						
Real GDP %yr	4.9	-0.3	1.5	1.5	1.3	1.3
Euroland						
Real GDP %yr	2.0	1.6	-0.6	-0.4	0.8	1.0
United Kingdom						
Real GDP %yr	1.7	1.1	0.3	1.8	2.6	2.1
China						
Real GDP %yr	10.4	9.3	7.7	7.7	7.2	7.6
East Asia ex China						
Real GDP %yr	7.8	4.4	4.0	4.0	4.2	5.0
World						
Real GDP %yr	5.2	3.9	3.2	3.0	3.0	3.7
Forecasts finalised 4 July 2014						

Interest Rate Forecasts	Latest	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15
Australia						
Cash	2.50	2.50	2.50	2.50	2.50	2.75
90 Day Bill	2.67	2.55	2.55	2.55	2.65	3.00
10 Year Bond	3.59	3.60	3.70	3.80	4.20	4.50
International						
Fed Funds	0.125	0.125	0.125	0.125	0.125	0.250
US 10 Year Bond	2.64	2.70	2.70	2.70	2.80	3.20
ECB Repo Rate	0.15	0.15	0.15	0.15	0.15	0.15

Exchange Rate Forecasts	Latest	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15
AUD/USD	0.9350	0.91	0.90	0.90	0.92	0.93
USD/JPY	102.15	101	100	101	102	103
EUR/USD	1.3607	1.32	1.30	1.30	1.31	1.31
AUD/NZD	1.0690	1.06	1.06	1.07	1.10	1.11

Westpac economics team contact details

Dominick Stephens, Chief Economist
+64 9 336 5671

Michael Gordon, Senior Economist
+64 9 336 5670

Felix Delbrück, Senior Economist
+64 9 336 5668

Anne Boniface, Senior Economist
+64 9 336 5669

Any questions email:
economics@westpac.co.nz

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