



# Weekly Economic Commentary.

## Firing on all cylinders.

Economic data released last week continued to show strength in the economy. This trend and the expectation it will continue was one of the reasons why we recently moved our forecast of the first OCR hike from early 2024 to August 2022.

First up we had the June business confidence survey, which showed that firms are feeling more upbeat about their own prospects. The strength was broad based, which contrasts with previous months where construction was the only sector that was clearly firing on all cylinders.

Strong economic activity has contributed to inflationary pressures, although a large portion of this is likely due to a supply-side shock from the disruptive effects of Covid. This has been an ongoing trend for the last year. Rising costs are a big concern, and businesses are hoping to raise their prices in the next few months. One point of interest was the agricultural sector which showed that 100% of firms expected costs to go up in the next three months.

Inflation expectations for the year ahead from the survey reached 2.4%, the highest level since late 2014. There's good reason to expect inflation to spike higher this year. But that's not the horizon that the Reserve Bank should be focusing on.

The bigger issue for them is the extent of price pressures and capacity constraints as we head into next year and beyond.

The continued confidence about activity has helped to spur investment intentions in the last few months. The combination of the March quarter imports of capital goods and recent firm investment intentions would suggest a strong print for business investment in the June quarter.

However, investment could still be held back by a lack of skilled workers to operate and or integrate the new investment. This has been an ongoing issue since the border closed. New Zealand historically has relied heavily on migrant workers for roles requiring specialist skills. Within the survey results, it showed that finding skilled labour has become the largest problem that firms faced and the biggest hurdle for investment.

We'll get some more clarity around this when NZIER releases their Quarterly Survey of Business Opinion later this week.



The QSBO covers not just firms' expectations, but their actual experience with costs, prices, and labour turnover in recent months.

The hot demand for labour was evident in the monthly filled jobs indicator, which is based on tax data, as the number of jobs rose by 0.4% in May. This brings the number of jobs in the economy to a level that is 0.6% higher compared to pre-Covid.

Continued strength in the labour market in recent months had led us to revise down our forecast of unemployment for the June quarter to 4.5% from 4.7%. By the middle of next year, we expect it to reach about 4%, back to levels last seen in 2019. Along with strong job ads, declining Jobseeker Benefit payments suggests that positions are being filled.

Notably, our early estimate is that job ads came off their highs in June. This suggests that the rush to find workers may have passed its peak, although the level remains high.

However, the strength of the labour market continues to be uneven. Sectors that are reliant on tourism continue to be affected by the border closures. These include hospitality, transport, and recreational services. On the other hand, sectors such as construction, healthcare and IT have shown solid gains.

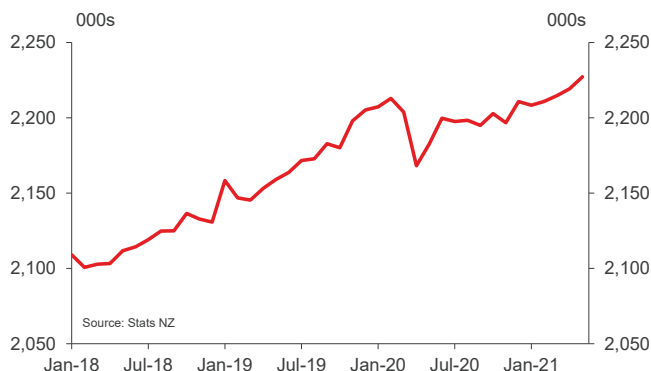
The strong demand for workers from the construction sector is not surprising as dwelling consents reached fresh record highs in May.

A large part of this work is due to construction in Auckland. This partly reflects the role of the Unitary Plan enabling more building, and more medium density building. However other regions are also joining the party, as consents in Waikato and

Canterbury have also been high. More recently, consents issued in Wellington have also picked up. The combination of closed borders and high building levels means that we're making significant progress towards addressing the housing shortage which developed over the last decade.

The strong economic conditions we've seen has been corroborated by the tax revenue within the fiscal accounts for May, which were almost \$6bn ahead of Budget forecasts. In our view, this is not because revenue has been unusually strong, but because the Budget Forecasts were unusually low.

### Monthly Employment Indicator filled jobs



**Gregorius Steven, Economist**

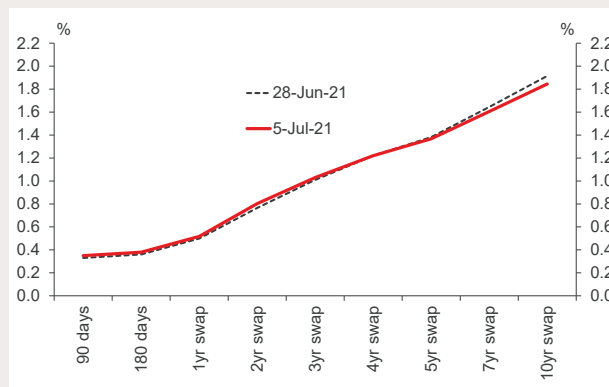
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## Fixed vs floating for mortgages.

We expect that floating rates, and shorter fixed-term rates, will be stable over the coming months. Inflation is set to spike higher this year, but the Reserve Bank will not need to respond to this.

Longer-term interest rates are now rising in response to the improved economic outlook. Given our forecasts, longer-term fixed rates (three to five years) no longer offer good value, relative to taking a short-term rate now and refixing later (albeit at a higher rate).

### NZ interest rates



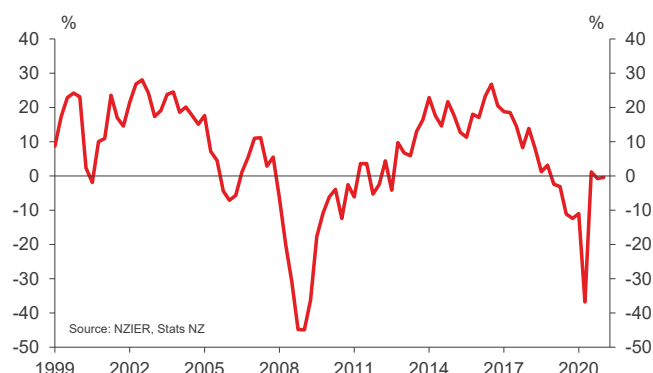
# The week ahead.

## Q2 NZIER Quarterly Survey of Business Opinion

### Jul 6, Domestic Trading Activity last: -0.4

- Business confidence improved in the March quarter, with firms feeling more upbeat about their own activity and employment. In the past this survey has been a good early indicator of quarterly GDP, but the disruptive effects of Covid-19 have weakened this link.
- We expect to see a further improvement in confidence and own-activity expectations in the June survey, reflecting recent strong data and the reopening of trans-Tasman travel.
- Measures of capacity and price pressures will be of particular interest. The March survey found that businesses had had limited success in raising their prices up to that point. Concerns about rising costs and labour shortages have escalated further in the last three months.

## QSBO domestic trading activity (past 3 mths)

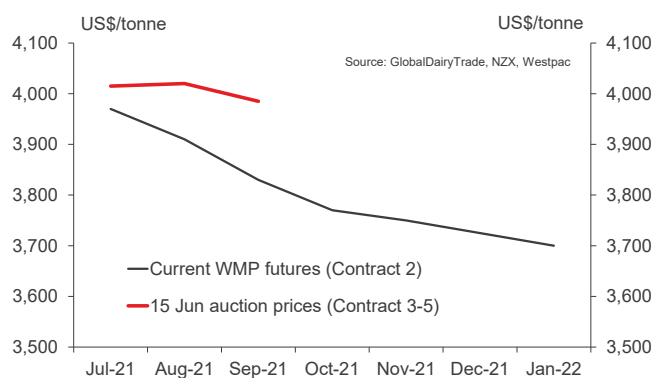


## NZ GlobalDairyTrade auction, whole milk powder prices

### Jul 7, Last: -1.8%, Westpac f/c: -1%

- Whole milk powder prices surged in the early part of 2021. While they have drifted lower in recent auctions, they remain well above their long-run average.
- We expect a small drop in prices at the early July auction, continuing the recent trend.
- Futures market pricing suggests about a 2% drop at the time of writing. However that could change by the date of the auction, as futures prices have been ticking higher in recent days.

## Whole milk powder prices



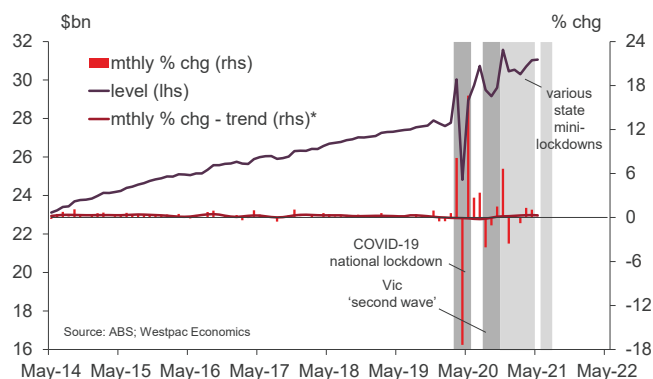
## Aus May retail trade

### Jul 5, Last: 1.1%, WBC f/c: 0.1%

### Mkt f/c: 0.1%, Range: 0.0% to 0.2%

- Preliminary estimates showed a significant slowing in retail sales in May with a 0.1% rise. Coronavirus restrictions had a more material impact than expected with Vic recording a 1.5% decline despite some lift in 'stockpiling' ahead of the 14-day lockdown in June (food retail sales up 4% in the state).
- The final release may see slight revisions and will include the full survey detail - sales by storetype, state, firm size and online vs in store.
- Looking ahead, sales are set for more weakness and volatility in the next few months. June will see the full hit from Melbourne's 14-day lockdown and subsequent reopening with some slight impacts from lockdowns across parts of Sydney late in the month. July will capture the impact of the wider Sydney lockdown - set to run for at least 14 days - and likely briefer lockdowns in Qld, WA and NT. Our Westpac Card Tracker will provide a timely gauge of these impacts.

## Aus monthly retail sales



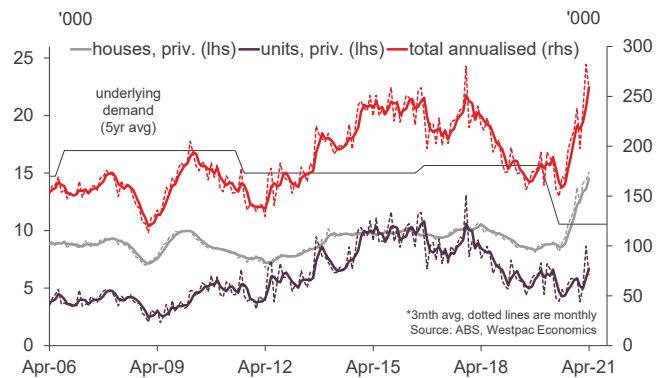
# The week ahead.

## Aus May dwelling approvals

**Jul 5, Last: -8.6%, WBC f/c: -10.0%**  
**Mkt f/c: -5%, Range: -12% to 5%**

- Dwelling approvals fell 8.6% in Apr, led by a pull back in 'high rise' but with the state detail suggesting an expected unwind of pull-forward effects from the expiring HomeBuilder scheme was starting to come through, albeit only mildly in the Apr month. Larger negatives are likely in coming months.
- Even with the Apr decline, approvals are still coming from a very high starting point up around 60% since mid-2020. Some of this is clearly related to the HomeBuilder scheme - Treasury reported just under 100k applications for new builds were received. Exactly how this plays through to indicators like dwelling approvals is uncertain - the scale of pull-forward effects, the timing of the unwind, the lags between contract signing and construction approval, and the impact of the strong upturn across the wider housing market all very difficult to gauge. On balance we expect May to show a large 10% fall concentrated in detached houses. Note that this would still leave approvals 30% above pre-COVID levels.

## Aus dwelling approvals



## Aus RBA policy decision

**Jul 6, Last: 0.1%, WBC f/c: 0.1%**  
**Mkt f/c: 0.1%, Range: 0.1% to 0.1%**

- The Reserve Bank Board meets on July 6. The Board has already informed us that decisions will be made around the Yield Curve Targeting (YCT) Program and the Bond Purchase Program (QE).
- With the economy having recovered much faster than the Bank's expectations in the November Statement on Monetary Policy, it seems reasonable that the Board will decide not to extend the 'yield target bond' to the November 2024 bond.
- We expect that the Board will decide to take a more flexible approach to its bond buying program than we have seen in the past. We think the Board will be committed to maintaining the current pace of purchases (\$5 billion per week) until late in the year (around the December Board meeting).

## RBA cash rate and 3 year bonds

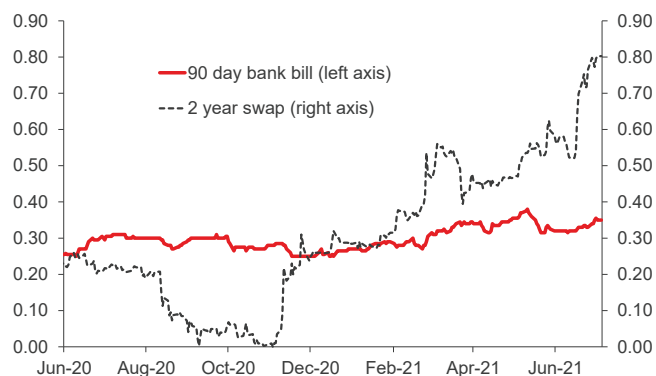


# New Zealand forecasts.

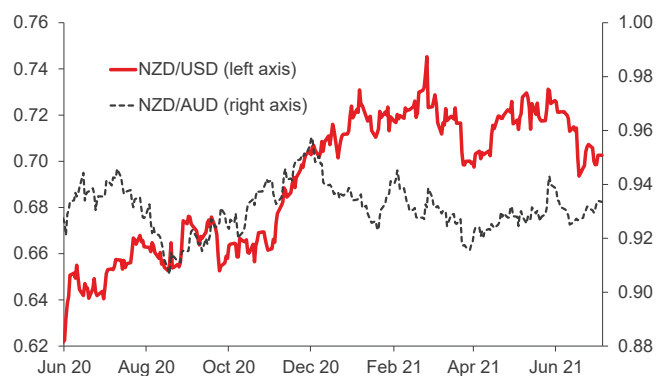
Economic forecasts	Quarterly				Annual			
	2021				2019	2020	2021f	2022f
% change	Mar (a)	Jun	Sep	Dec				
GDP (Production)	1.6	0.6	0.9	1.3	2.4	-2.9	5.8	4.5
Employment	0.5	0.3	0.4	0.4	1.2	0.8	1.7	2.1
Unemployment Rate % s.a.	4.7	4.5	4.4	4.2	4.1	4.9	4.2	3.9
CPI	0.8	0.4	0.7	0.2	1.9	1.4	2.2	1.7
Current Account Balance % of GDP	-2.2	-3.3	-4.1	-4.4	-3.3	-0.8	-4.4	-3.4

Financial forecasts	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Jun-23	Dec-23
Cash	0.25	0.25	0.25	0.25	0.50	0.75	1.00	1.50
90 Day bill	0.35	0.35	0.35	0.45	0.70	0.85	1.20	1.60
2 Year Swap	0.60	0.70	0.80	0.90	1.05	1.20	1.50	1.70
5 Year Swap	1.30	1.45	1.60	1.75	1.90	2.00	2.20	2.40
10 Year Bond	1.90	2.05	2.20	2.35	2.50	2.60	2.80	2.90
NZD/USD	0.72	0.74	0.76	0.78	0.78	0.77	0.75	0.72
NZD/AUD	0.92	0.93	0.93	0.92	0.92	0.92	0.91	0.92
NZD/JPY	78.5	80.7	83.6	85.8	86.6	85.5	81.8	77.8
NZD/EUR	0.59	0.60	0.61	0.62	0.61	0.61	0.59	0.57
NZD/GBP	0.51	0.52	0.53	0.54	0.54	0.53	0.52	0.50
TWI	74.0	75.2	76.6	77.7	77.5	76.4	74.7	72.2

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 5 July 2021

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	0.31%	0.30%	0.30%
90 Days	0.35%	0.33%	0.32%
2 Year Swap	0.80%	0.68%	0.58%
5 Year Swap	1.37%	1.34%	1.30%

NZ foreign currency mid-rates as at 5 July 2021

Exchange rates	Current	Two weeks ago	One month ago
NZD/USD	0.7026	0.6942	0.7235
NZD/EUR	0.5921	0.5856	0.5932
NZD/GBP	0.5081	0.5027	0.5101
NZD/JPY	77.99	76.54	79.03
NZD/AUD	0.9335	0.9275	0.9322
TWI	74.09	73.23	75.04

## Data calendar.

		Last	Market median	Westpac forecast	Risk/Comment
<b>Mon 05</b>					
NZ	Jun ANZ commodity prices	1.3%	-	0.7%	Dairy prices edging down, modest gains elsewhere.
Aus	Jun ANZ job ads	7.9%	-	-	Vacancies have surged ahead in official ABS measure.
	Jun MI inflation gauge	3.3%	-	-	Lifted significantly in recent months - at a 10 year high.
	May dwelling approvals	-8.6%	-5.0%	-10%	HomeBuilder unwind to show through more clearly.
	May retail sales (final)	0.1%	0.1%	0.1%	Preliminary estimate showed initial lockdown hit to Vic.
Eur	Jul Sentix investor confidence	28.1	-	-	Strength now appearing in 'current situation' component.
US	Independence Day (observed)	-	-	-	Public holiday.
<b>Tue 06</b>					
NZ	Q2 NZIER business opinion	-0.4	-	-	Results should reflect strong Q2 economic data.
Aus	Weekly Payrolls w/e Jun 19	-	-	-	Will serve as a guide to June labour force survey.
	RBA policy decision	0.10%	0.10%	0.10%	To announce a decision on both the YCT and QE programs..
	RBA Governor Lowe	-	-	-	Remarks on Today's Monetary Policy Decision.
Eur	May retail sales	-3.1%	-	-	Pent-up demand to spur sales as reopening progresses.
	Jul ZEW survey of expectations	81.3	-	-	Expectations ebullient on prospects of H2 rebound.
US	Jun ISM Services Index	64.0	63.9	-	Has surged on economic reopening and consumer spending.
<b>Wed 07</b>					
NZ	GlobalDairyTrade auction (WMP)	-1.8%	-	-1.0%	Dairy prices easing back after surge in early 2021.
Chn	Jun foreign reserves \$bn	3221.80	-	-	Strength in recent months driven by USD weakness.
US	May JOLTS job openings	9286k	9344k	-	Setting record highs on improved hiring/labour churn.
	Jun FOMC Meeting Minutes	-	-	-	Will be looking for commentary around risks to the outlook.
<b>Thu 08</b>					
Aus	RBA Governor Lowe	-	-	-	Speech at the Economic Society of Australia, online.
US	Initial jobless claims	-	-	-	Downtrend to continue, despite some choppiness of late.
	May consumer credit	18.612	-	-	Vehicle loans behind strength in non-revolving credit.
<b>Fri 09</b>					
Chn	Jun PPI %yr	9.0%	8.8%	-	Upstream prices surging on base effects and commodities...
	Jun CPI %yr	1.3%	1.3%	-	... but consumer price growth more modest.
	Jun new loans, CNYbn	1500.0	1800.0	-	Policymakers squarely focussed on quality lending.
	Jun M2 money supply %yr	8.3%	8.3%	-	Money supply growth has eased off mid-2020 peaks.

## 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	5.4	3.8
CPI inflation %/yr	1.9	1.8	1.8	0.9	2.6	1.8
Unemployment rate %	5.5	5.0	5.2	6.8	5.0	4.7
Current account % of GDP	-2.6	-2.1	0.7	2.6	4.2	2.6
<b>United States</b>						
Real GDP %/yr	2.3	3.0	2.2	-3.5	6.5	4.1
CPI inflation %/yr	2.1	2.4	1.9	1.2	2.9	2.2
Unemployment rate %	4.4	3.9	3.7	8.1	5.3	4.3
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	2.7	2.1
<b>Euro zone</b>						
Real GDP %/yr	2.6	1.9	1.3	-6.6	4.2	4.0
<b>United Kingdom</b>						
Real GDP %/yr	1.7	1.3	1.4	-9.9	5.8	5.5
<b>China</b>						
Real GDP %/yr	6.9	6.7	5.8	2.3	10.0	5.7
<b>East Asia ex China</b>						
Real GDP %/yr	4.7	4.4	3.7	-2.4	4.9	4.9
<b>World</b>						
Real GDP %/yr	3.8	3.6	2.8	-3.3	5.9	4.6

Forecasts finalised 9 June 2021

Interest rate forecasts	Latest	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Jun-23	Dec-23
<b>Australia</b>									
Cash	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.50	0.75
90 Day BBSW	0.03	0.04	0.07	0.10	0.15	0.20	0.40	0.70	0.95
10 Year Bond	1.48	1.95	2.10	2.20	2.30	2.40	2.50	2.70	2.90
<b>International</b>									
Fed Funds	0.125	0.125	0.125	0.125	0.125	0.125	0.375	0.875	0.875
US 10 Year Bond	1.47	1.85	2.00	2.10	2.20	2.30	2.40	2.60	2.80

Exchange rate forecasts	Latest	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Jun-23	Dec-23
AUD/USD	0.7463	0.78	0.80	0.82	0.85	0.85	0.84	0.82	0.78
USD/JPY	111.60	111	111	112	112	113	113	114	115
EUR/USD	1.1844	1.22	1.23	1.24	1.23	1.22	1.21	1.20	1.19
GBP/USD	1.3767	1.42	1.43	1.43	1.44	1.45	1.45	1.44	1.43
USD/CNY	6.4739	6.30	6.20	6.15	6.10	6.05	6.00	6.00	5.95
AUD/NZD	1.0718	1.08	1.08	1.08	1.09	1.09	1.09	1.10	1.08

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- (vi) steps by Compliance to ensure that the Chinese Wall/Cell arrangements remain effective and that such arrangements are adequately monitored.

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