



WEEKLY ECONOMIC COMMENTARY



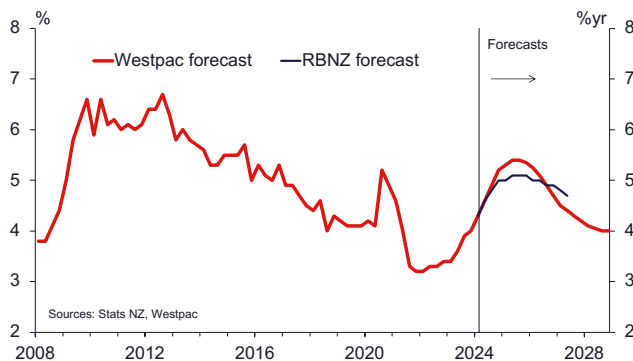
1 Jul 2024 | Westpac Economics Team | westpac.co.nz/economics | economics@westpac.co.nz

We are at full transmission!

Last week's news continued to reflect the theme of an economy that is dealing with the impact of monetary policy that is at "full transmission" from the 525 basis points of RBNZ policy tightening that occurred from October 2021 to May 2023.

The last shoe to drop in the monetary policy transmission process is traditionally the labour market. The consensus view is that the unemployment rate is set to rise relatively quickly through to the end of 2024 as past resilience in jobs growth gives way to the weakness in economic activity we have seen since late 2022. Westpac forecasts the unemployment rate to rise by 0.3% to 4.6% in the June quarter (data released August 7). The unemployment rate is set to end 2024 at 5.2%, which would be the highest unemployment rate since the Covid lockdown peak in 2020 and Q4 2016 before that.

The labour market is set to significantly ease

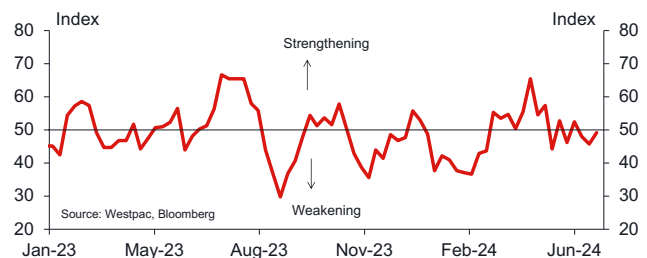


Westpac's Employment Confidence survey provided some clues on how the transition to a weaker labour market is proceeding. The survey is consistent with our forecasts that a further significant move higher in the unemployment rate is in the offing. Employment confidence fell by 13 points to 91.4 over the past quarter – the lowest level since 2020. The details indicate the public's expectations for wage growth and job security

Key views

	Last 3 months	Next 3 months	Next year
Global economy	➔	➔	↗
NZ economy	➔	➔	↗
Inflation	↘	↘	↘
2 year swap	➔	➔	↘
10 year swap	➔	➔	➔
NZD/USD	➔	➔	↗
NZD/AUD	➔	➔	↘

Westpac New Zealand Data Pulse Index

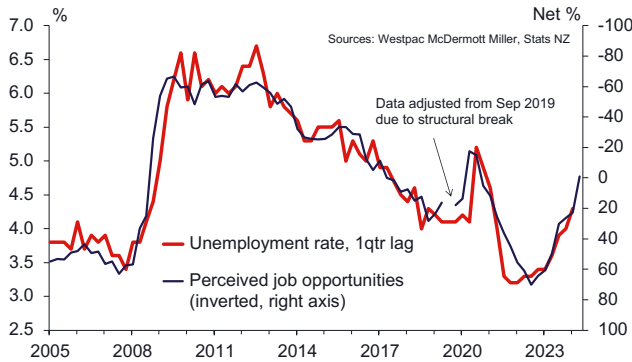


Key data and event outlook

Date	Event
2 Jul 24	NZIER QSBO survey, June quarter
4 Jul 24	Govt financial statements for 11 mths to May
10 Jul 24	RBNZ OCR Review
11 Jul 24	NZ Selected price indexes, June
17 Jul 24	NZ CPI, June quarter
31 Jul 24	FOMC Meeting (Announced 1 Aug NZT)
6 Aug 24	RBA Monetary Policy Decision & SMP
7 Aug 24	Labour market statistics, June quarter
8 Aug 24	RBNZ Survey of Expectations, June quarter
14 Aug 24	RBNZ OCR Review & Monetary Policy Statement
15 Aug 24	NZ Selected price indexes, July
12 Sep 24	NZ Selected price indexes, August
18 Sep 24	FOMC Meeting (Announced 19 Sep NZT)
19 Sep 24	NZ GDP, June quarter

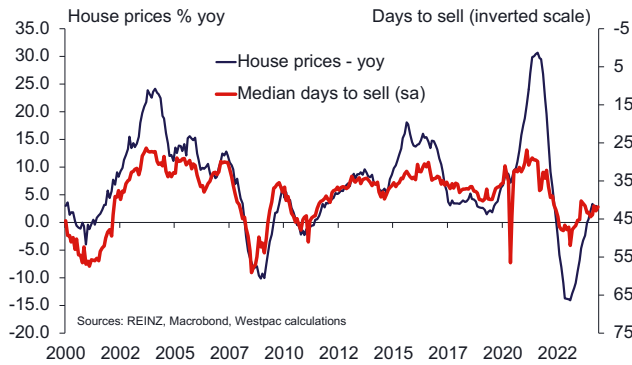
have deteriorated. Importantly, New Zealand workers are also telling us that they're seeing fewer job opportunities, with the measure of current job openings falling to its lowest level since 2020 (and 2016 before that – although changes in the survey process make comparisons to pre-2019 data more tenuous).

Current job opportunities vs unemployment rate



The message of an economy dealing with “peak interest rate transmission” was also reflected in some changes in **our view on house prices** for the rest of 2024. Momentum in the housing market has decidedly slowed since around the time of the General Election in October 2023. Growth in house sales has been flagging in recent months, just as we would have expected some resilience in market activity based on our previous house price forecast of around 6% growth for 2024.

House prices vs median days to sell



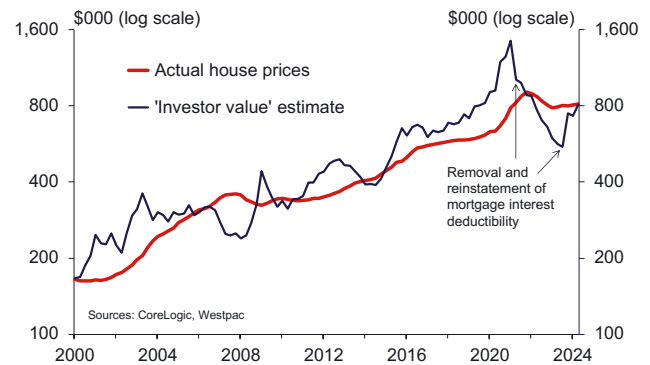
Other indicators such as median days to sell have stabilised at modest levels at around 42 days (seasonally adjusted) and look more consistent with house prices growing close to the rate of inflation and somewhat lower than the average rate of house price growth seen post-GFC and pre-Covid (6.5% per annum from 2010-2020). Similarly, the ratio of sales to listings peaked in mid-2023 and has not been recovering in recent months. As sales volumes have remained modest, listings have tended to increase – consistent with the market turning into a “buyers’ market” in recent months.

One key factor that has been leaning against house price growth and activity has been the RBNZ’s policy stance.

The RBNZ’s stance has hardened in recent months reflecting the still uncomfortably high inflation outlook. In contrast to our own expectation of a lower OCR from February 2025, the RBNZ has indicated a longer period before lower interest rates become a realistic prospect. We think this more pessimistic view has been reflected in the downturn of many economic growth and confidence indicators in recent months – the housing market included. While this pessimism persists, it seems hard to see a significant pick-up in house prices in 2024.

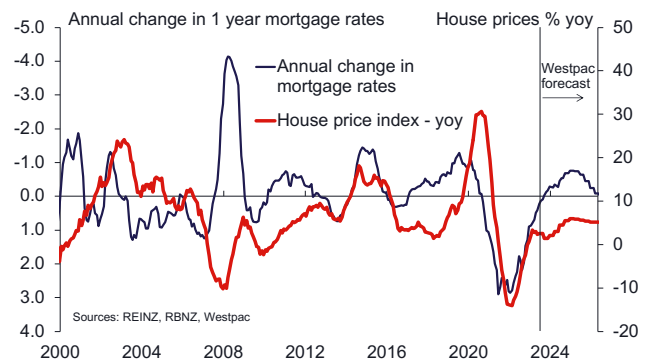
Our long-running ‘investor value’ model suggests that the housing market is roughly fairly valued now. While the ‘investor value’ is not a forecast, we find that house prices tend to gravitate towards it over time. Rising mortgage rates and the removal of interest deductibility for investors in 2021 meant that the housing market had turned overvalued since early 2022; the new Government’s commitment to restore interest deductibility has removed this downward pressure on prices, rather than providing a substantive boost.

Westpac ‘investor value’ model of house prices



This all has led us to scale back our expectations for house price growth to reflect close to 2% growth in 2024, and 6% growth in 2025 (where we remain optimistic that house prices will be stronger as the OCR will fall – likely a bit earlier than the RBNZ currently indicates). The ongoing mismatch between housing demand and supply remains (reflected in ongoing above general inflation rent increases) plus improvements in investor tax treatment points to higher house price inflation in 2025.

Annual change in house prices vs change in mortgage rates



Other survey data released this week also look consistent with a flat economy with some mixed news on inflation. Consumer confidence fell slightly, although interestingly the survey's measure of inflation expectations rose from 3.8% to 4.2%. Similarly, in the business sector the latest ANZ survey pointed to activity that is continuing to bounce along the bottom, with the gauge of trading activity over the past year languishing at low levels. Growth looks like it was weaker in Q2 compared to Q1's +0.2% but doesn't look to have started a step lower still based on the June survey. We will learn more from the NZIER Quarterly Survey of Business Opinion on Tuesday.

On the inflation front, the number of businesses planning on increasing their prices dropped to a net 35% – the second month in a row that we've seen a meaningful downward move. A net 69% of firms are expecting cost increases, which is still a relatively high proportion, but the average size of wage and other cost increases is tracking lower.

Kelly Eckhold, Chief Economist

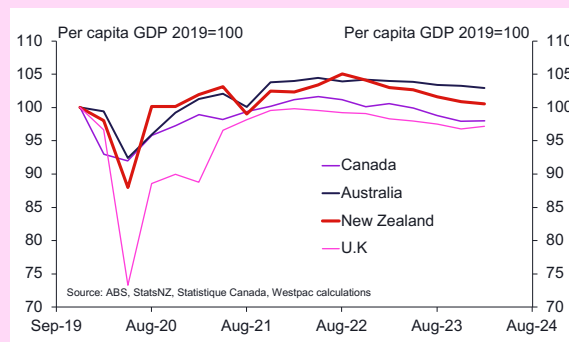
Chart of the week.

Much has been made of New Zealand's weak trend in per capita GDP since 2022 as output has stagnated and population has continued to grow strongly. Since Q3 2022 per real capita GDP has fallen by almost 5 percent which represents a significant decline in the living standards of New Zealanders. Some commentators have attributed this weak performance on factors specific to New Zealand – for example the stance of monetary/fiscal policy, structural and regulatory settings etc.

What's less recognised is that many of our peer economies have been experiencing similar trends. Our chart of the week looks at the experience of Australia, Canada and the UK. What we can see is that all these peer economies have had a disappointingly weak trend in real per capita GDP since Covid. New Zealand does not look special in this regard.

New Zealand does look special with respect to the volatility of per capita GDP since Covid-19. New Zealand per capita GDP rose by more than most until September 2022, reflecting the extent to which the New Zealand economy was overheated by expansive fiscal and monetary policy and closed borders. Much of the fall in per capita GDP since then reflects a natural retracement of that earlier overheating.

Developments in real GDP per capita – peer countries

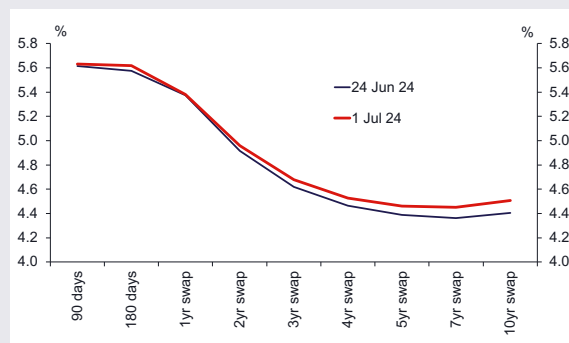


Fixed versus floating for mortgages.

The RBNZ left the OCR on hold in May and signalled that rate cuts are still some way off. Westpac is not forecasting OCR reductions until early 2025.

For borrowers favouring certainty, at current fixed rates we see value in fixing for as long as two years.

NZ interest rates



Global wrap

North America.

The Fed's preferred inflation metric – the core PCE deflator – increased just 0.1% in May, lowering annual inflation to 2.6%. However, Fed speakers continued to note that a run of such outcomes will be required to establish that inflation is back on a clear downward path. In other news, Q1 GDP growth was revised up 0.1ppt to 1.4% annualised. After slumping in April, pending home sales fell a further 2.1% in May and were down 6.8%/y/y, while durable goods orders rose 0.1% in May but were down 1.2%/y/y. In Canada, a higher-than-expected May inflation reading reduced the prospect of a follow-up rate cut at this month's BoC policy meeting. The coming holiday-shortened week will see attention turn back to the labour market. We expect Friday's employment report to point to a 165k lift in non-farm payrolls in June, leaving the unemployment rate steady at 4.0%. Tuesday's JOLTS survey will also be of interest after reporting a fall in job openings in April, while the latest ISM readings (manufacturing today and services Wednesday) are also of note.

Europe.

Following on from last week's softer-than-expected PMI reports, Germany's Ifo survey and the European Commission's economic sentiment index also pointed to a slight pullback in confidence over the past month, notwithstanding the ECB's recent rate cut. Exit polls from the weekend's first round of the French parliamentary elections point to an outcome broadly in line with prior surveys, so attention will now turn to the second-round election on Sunday. On the data front, the focus in the euro area this week will be on inflation, with Germany's preliminary report released today and the area-wide report released on Tuesday. Final manufacturing and services PMI readings for June will also be of interest this week. In the UK, the key diary entry is Thursday's General Election, with polls pointing to a change in government.

Asia-Pacific.

China's official PMI reports were somewhat disappointing in June, with the manufacturing index steady at a soft 49.5 and the non-manufacturing index declining to 50.5. This week the BoJ will release its closely watched Tankan business survey, which will feed into the BoJ's assessment when it contemplates further policy tightening next month. Closer to home, last week's Australian monthly CPI report was in line with our expectations. However, it was firmer than had been expected by the market, which is now pricing a better-than-even chance of a rate hike this year. This week's key diary entries are retail and building reports on Wednesday and trade data on Thursday.

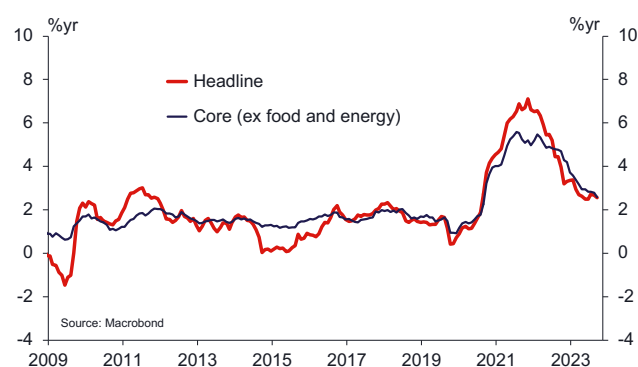
Trading partner real GDP (calendar years)

	Annual average % change			
	2022	2023	2024	2025
Australia	3.8	2.1	1.6	2.3
China	3.0	5.2	5.2	5.0
United States	1.9	2.5	2.5	1.5
Japan	1.0	1.9	0.5	1.0
East Asia ex China	4.5	3.3	4.2	4.2
India	7.0	7.8	6.9	6.7
Euro Zone	3.4	0.4	0.6	1.5
United Kingdom	4.3	0.1	0.5	1.3
NZ trading partners	3.2	3.4	3.4	3.4
World	3.5	3.2	3.2	3.0

Australian & US interest rate outlook

	28 Jun	Sep-24	Dec-24	Dec-25
Australia				
Cash	4.35	4.35	4.10	3.10
90 Day BBSW	4.45	4.37	4.17	3.30
3 Year Swap	4.24	4.10	4.00	3.50
3 Year Bond	4.10	3.90	3.80	3.30
10 Year Bond	4.34	4.30	4.25	4.00
10 Year Spread to US (bps)	3	-10	-5	0
US				
Fed Funds	5.375	5.125	4.875	3.875
US 10 Year Bond	4.31	4.40	4.30	4.00

US PCE deflator



Chinese PMIs



Financial markets wrap

Interest rates.

NZ swap rates rose last week, led by AU yields which rose after stronger than expected Australian CPI inflation data. The 2yr rose from 4.90% to 5.00%, with speculative receivers capping the rise.

The 4.90% support area continues to hold and will require fresh news for the market to price in further OCR cuts and, in turn, push swap rates lower. Currently, markets price a 50% chance of a cut in October, and over 100% for November. We continue to expect the first cut to be in February 2025.

Intending fixed-rate payers could consider forward starting swaps, rather than spot starts, since the former are at lower rates, having effectively priced in a good part of the looming easing cycle. For example, a 2yr swap starting in 2 years' time is at around 4.00%, compared to a spot starting 2yr swap at around 4.96%.

This week's key event will be the US payrolls data on Friday, with some interest also in Tuesday's local NZIER business confidence survey.

Foreign exchange.

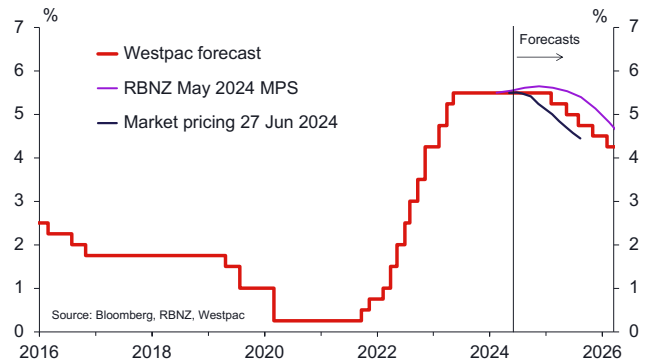
NZD/USD finally broke below its two-month old range last week, and could extend the move slightly to the 0.6000 area during the week ahead. Further ahead, though, we remain bullish, targeting 0.6200 by August.

The US dollar strengthened in June, partly due to mixed US economic data and partly due to safe-haven flows. That positive USD momentum could spill over into this week, although the most recent data suggests US inflation is gradually moderating, and any USD gains could be modest. Much further ahead, we expect the Fed to start cutting its policy rate in September 2024, well before the RBNZ in February 2025, which, via yield spreads, would be NZD/USD supportive.

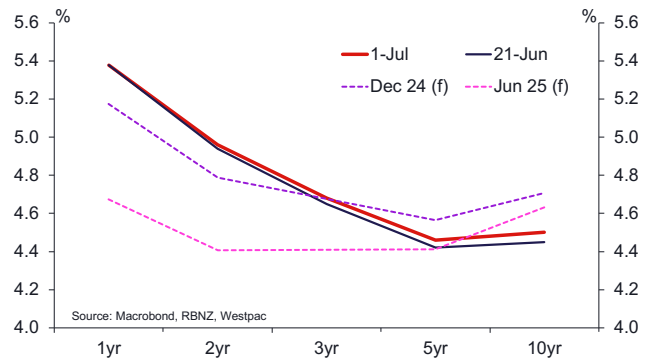
NZD/AUD's sharp reversal lower in June was mainly due to the RBA's hawkish hold and stronger CPI data. These surprises should resonate for some time via NZ-AU yield spreads and the cross, such that the one-year low of 0.9065 could be tested during the next week or two.

NZD/JPY made a fresh post-float high of 98.25 on Friday, which should be attractive to NZ importers. The yen remains weak amid tepid intervention so far from the MoF and BoJ, although the July meeting could signal a change.

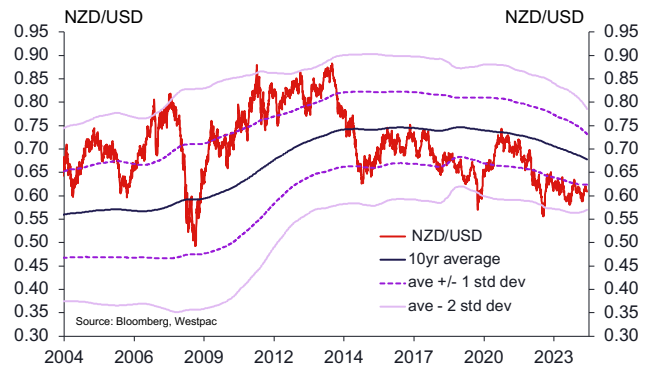
Official Cash Rate forecasts



Swap rates



NZD/USD vs rolling 10yr average



FX recent developments

	Historical data				F'cast
	Spot	3mth range	5yr range	5yr avg	Dec-24
USD	0.610	0.586-0.620	0.555-0.743	0.647	0.61
AUD	0.914	0.907-0.929	0.873-0.992	0.931	0.91
EUR	0.568	0.552-0.573	0.517-0.637	0.582	0.55
GBP	0.483	0.471-0.484	0.464-0.544	0.505	0.48
JPY	98.0	90.2-98.0	61.3-98.0	79.5	93.9

The week ahead

NZ May monthly employment indicator

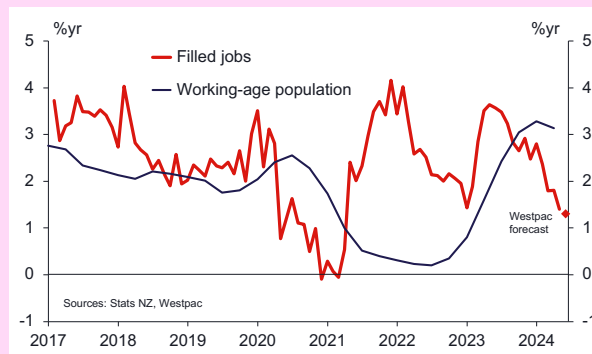
Jul 1, Last: +0.1%, Westpac f/c: -0.1%

The monthly employment indicator is drawn from income tax data, making it a comprehensive record of the number of people in work. While there are conceptual differences, it generally does a good job of predicting the more widely followed quarterly household survey measure of employment.

Job growth has been slowing since mid-2023, and has now fallen behind the pace of population growth, which continues to be boosted by strong net inward migration. Surveys show that businesses are no longer struggling to find workers, and job advertisements have fallen substantially below pre-Covid levels.

We've pencilled in a small decline in June, though it's not a confident view that figures have turned negative yet, and the usual weekly data snapshots have been late to arrive.

Monthly filled jobs growth



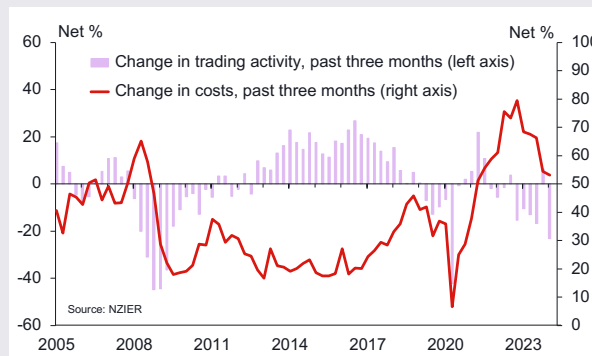
NZ Q2 NZIER Survey of Business Opinion

Jul 2, General business confidence Last: -23.7

The NZIER's March quarter update showed a sharp fall in business sentiment, as the initial post-election optimism gave way again to the reality of a slowing economy. That was consistent with our forecast of weak to negative economic growth through the early part of this year, although the survey's correspondence with GDP from quarter to quarter has broken down somewhat in recent years.

The March quarter survey was also less encouraging in terms of the gauges of inflation pressures. While cost pressures and pricing intentions have been tracking down from their highs, the process has been gradual so far, and in many cases they remain above what would be consistent with the RBNZ's inflation target. With the RBNZ's current focus on sticky non-tradables inflation, there will be particular interest in what the June survey says about the extent of domestically-driven inflation pressures.

NZIER Quarterly Survey of Business Opinion



NZ May building consents

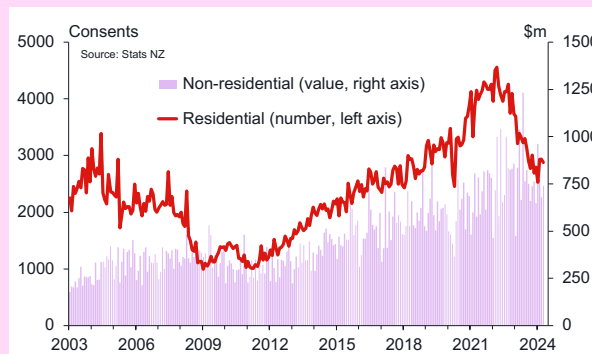
2 July, Last: -1.9%. Westpac f/c: -5%

Over the past year, consent issuance has fallen 23% in response to tougher financial conditions in the building sector. However, the downturn looks like it is finding a base. For the past few months, consent issuance has been bobbing around 2,900 per month.

We expect to see a modest drop in May, but for the flattening trend to continue.

But although consent issuance may be finding a floor, a material pickup is still a long way off. Developers are likely to remain cautious about bringing projects to market until interest rates fall and the housing market begins to recover.

Building consents

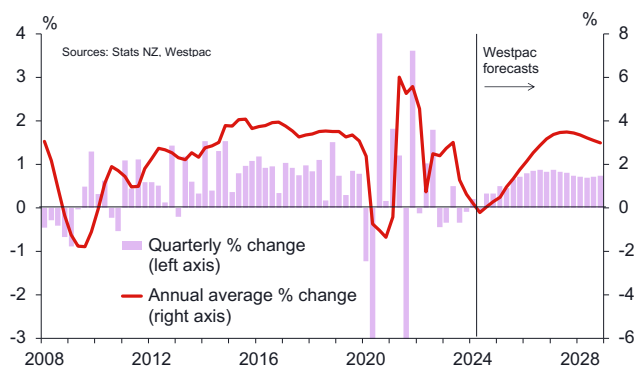


Economic and financial forecasts

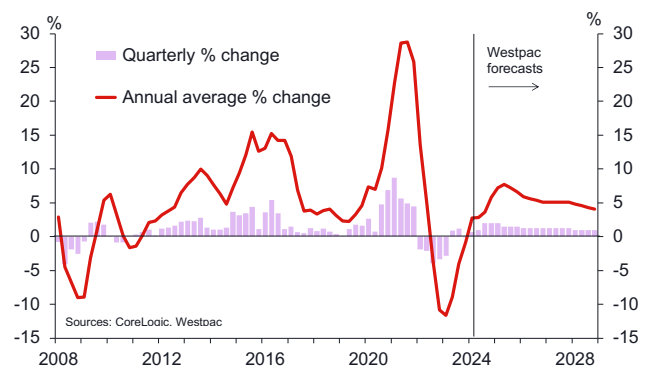
Economic indicators	Quarterly % change				Annual % change			
	Mar-24	Jun-24	Sep-24	Dec-24	2022	2023	2024	2025
GDP (production)	0.2	-0.1	0.3	0.3	2.4	0.6	0.3	1.8
Consumer price index	0.6	0.6	1.1	0.4	7.2	4.7	2.8	2.2
Employment change	-0.2	0.2	0.1	0.1	1.7	2.7	0.1	0.9
Unemployment rate	4.3	4.6	4.9	5.2	3.4	4.0	5.2	5.4
Labour cost index (all sectors)	0.9	0.9	0.8	0.8	4.1	4.3	3.4	2.5
Current account balance (% of GDP)	-6.8	-6.4	-5.9	-5.3	-8.8	-6.9	-5.3	-4.6
Terms of trade	5.1	4.0	2.2	0.6	-4.2	-10.7	12.3	0.7
House price index	0.5	0.0	0.5	1.0	-13.8	0.6	2.0	6.1

Financial forecasts	End of quarter				End of year			
	Mar-24	Jun-24	Sep-24	Dec-24	2022	2023	2024	2025
OCR	5.50	5.50	5.50	5.50	4.25	5.50	5.50	4.50
90 day bank bill	5.66	5.63	5.60	5.50	4.27	5.65	5.50	4.50
2 year swap	4.91	5.01	5.00	4.80	5.10	5.28	4.80	4.15
5 year swap	4.40	4.53	4.65	4.55	4.67	4.85	4.55	4.30
10 year bond	4.69	4.74	4.90	4.80	4.31	5.09	4.80	4.50
TWI	71.6	71.4	70.5	70.9	70.8	70.8	70.9	72.1
NZD/USD	0.61	0.61	0.60	0.61	0.60	0.60	0.61	0.65
NZD/AUD	0.93	0.92	0.91	0.91	0.92	0.93	0.91	0.91
NZD/EUR	0.56	0.56	0.55	0.55	0.59	0.56	0.55	0.57
NZD/GBP	0.48	0.48	0.47	0.48	0.51	0.49	0.48	0.49

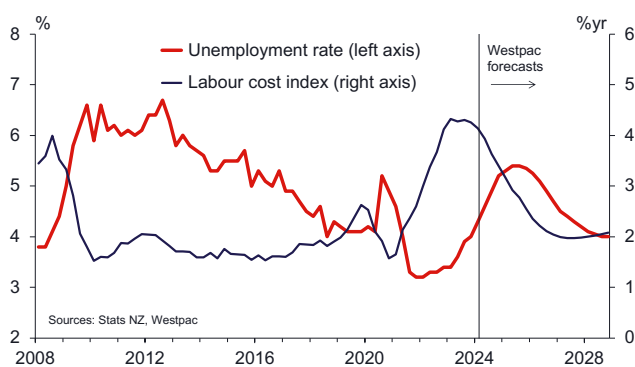
GDP growth



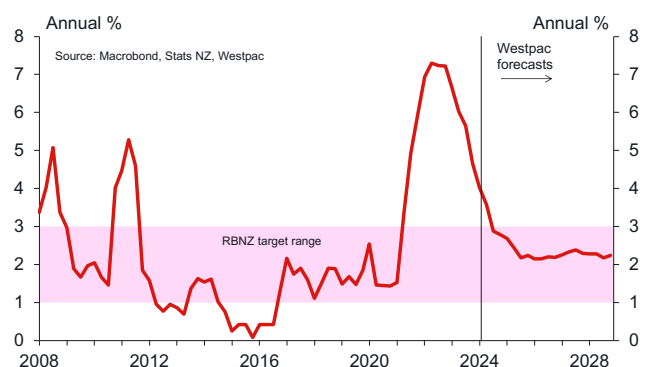
House prices



Unemployment and wage growth



Consumer price inflation



Data calendar

		Last	Market median	Westpac forecast	Risk/Comment
Mon 01					
NZ	May Employment Indicator %mth	0.1%	-	-0.1%	Hiring has slowed as the economy cools.
Aus	Jun CoreLogic Home Prices %mth	0.8%	-	0.8%	Another robust rise but varied across cities.
	Jun MI Inflation Gauge %yr	3.1%	-	-	Provides a general view on risks.
	Jun ANZ-Indeed Job Ads %mth	-2.1%	-	-	Indicative of further easing in labour demand.
Jpn	Q2 Tankan Large Manufacturers Index	11	11	-	Wage and inflation outlook is critical.
Chn	Jun Caixin Manufacturing PMI	51.7	51.5	-	Level consistent with growth above 5%.
US	Jun ISM Manufacturing	48.7	49.2	-	Drop in new orders consistent with soft domestic demand.
	May Construction Spending %mth	-0.1%	0.3%	-	Elevated costs and uncertainty hinder capacity expansion.
Global	Jun S&P Global Manufacturing PMI	-	-	-	Final estimate for Japan, Eurozone, UK, US.
Tue 02					
NZ	Q2 NZIER Survey of Business Opinion	-23.7	-	-	Important gauge of activity and cost pressures.
	May Building Permits %mth	-1.9%	-	-5.0%	The downturn is now flattening off.
Aus	RBA June Meeting Minutes	-	-	-	More colour on the Board's policy deliberations.
Eur	Jun CPI %yr	2.6%	2.5%	-	Attention on services inflation.
	May Unemployment Rate %	6.4%	6.5%	-	Holding firm at historically-low levels.
US	May JOLTS Job Openings	8059k	-	-	Labour demand and supply are moving into balance.
US/Eur	FOMC and ECB Panel	-	-	-	Panel with Chair Powell and President Lagarde.
Wed 03					
NZ	GlobalDairyTrade Auction	-0.5%	-	-	Futures and GDT Pulse point to a small fall in WMP prices.
	Jun ANZ Commodity Prices %mth	1.1%	-	1.0%	Stronger dairy prices to lift the overall index.
Aus	May Dwelling Approvals %mth	-0.3%	1.7%	1.5%	Still bumping around 12yr lows.
	May Retail Sales %mth	0.1%	0.3%	0.3%	Slightly better in May but 3mth trend still weak.
Chn	Jun Caixin Services PMI	54.0	-	-	Consumers remain very cautious on outlook.
US	May Trade Balance \$bn	-74.6	-72.2	-	Deficit should narrow as consumer demand cools further.
	Jun ISM Non-Manufacturing	53.8	-	-	Services firms still experiencing growth, but risks growing.
	May Factory Orders %mth	0.7%	-	-	Durable orders weak ex transport and defence.
	Initial Jobless Claims	233k	-	-	Remain near historic lows.
	FOMC June Meeting Minutes	-	-	-	Guidance on evolving risks key.
	Fedspeak	-	-	-	Williams.
Global	Jun S&P Global Services PMI	-	-	-	Final estimate for Japan, Eurozone, UK, US
Thu 04					
Aus	May Goods Trade Balance \$bn	6.5	6.2	7.0	Port data points to an improvement in export volumes.
UK	General Election	-	-	-	A change in government seems likely.
US	Independence Day	-	-	-	Markets closed.
Fri 05					
Jpn	May Household Spending %yr	0.5%	0.2%	-	Beginning to resurface after a challenging year.
Eur	May Retail Sales %mth	-0.5%	0.5%	-	Spending starts to lift as consumer gloom gradually fades.
US	Jun Non-Farm Payrolls	272k	188k	165k	Disconnect between payrolls and household employment...
	Jun Unemployment Rate %	4.0%	4.0%	4.0%	... unsustainable, but unlikely to disappear quickly.
	Jun Average Hourly Earnings %mth	0.4%	0.3%	0.3%	Labour market balance to see wage growth slow to trend.
	Fedspeak	-	-	-	Williams.

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