



WEEKLY ECONOMIC COMMENTARY



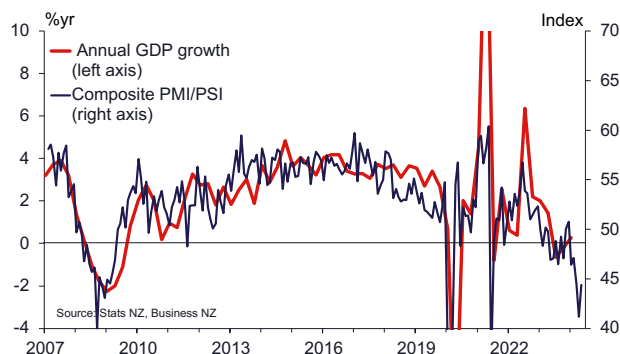
26 Aug 2024 | Westpac Economics Team | westpac.co.nz/economics | economics@westpac.co.nz

Back to data watching

Since this month's surprise RBNZ rate cut, several Monetary Policy Committee members have indicated an openness to accelerating the pace of future rate cuts if the incoming economic data flow points to downside risks to activity and inflation. However, on balance, we think that last week's data flow remained consistent with our central forecast that the Official Cash Rate will end the year at 4.75%, which is also the level signalled in the RBNZ's heavily revised August projections.

Following on from the previous week's modest bounce in its manufacturing counterpart, the BusinessNZ Performance of Services Index posted an improvement in July, rising 3.9pts to 44.6 – but still about 9pts below the historic average. The activity index rose 2.9pts to 39.1 – 15pts below the historic average and still the second worst reading ever once the Covid lockdown months are excluded. The new orders index lifted a more encouraging 6.4pts to 45.3 (almost 12pts below average) and the employment index remained in contractionary territory for an eighth consecutive month. All up, this suggests that activity probably continued to decline during July, consistent with our forecast (shared by the RBNZ) that GDP will contract slightly in the September quarter.

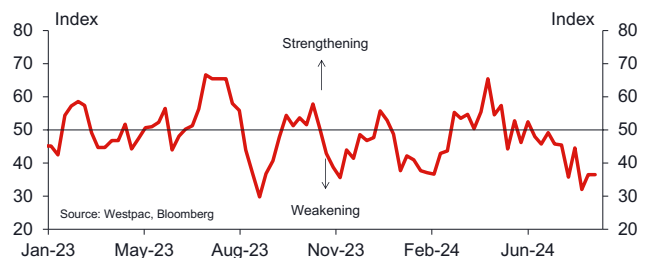
PMI indicators continue to point to mid-year weakness



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

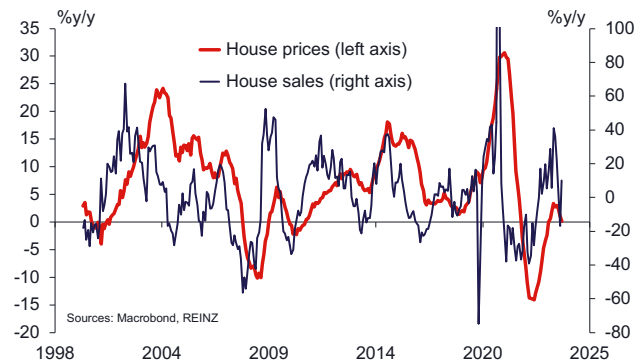


Key data and event outlook

Date	Event
12 Sep 24	NZ Selected price indexes, August
18 Sep 24	FOMC Meeting (Announced 19 Sep NZT)
19 Sep 24	NZ GDP, June quarter
24 Sep 24	RBA Monetary Policy Decision
1 Oct 24	NZIER QSBO survey, September quarter
9 Oct 24	RBNZ OCR Review
11 Oct 24	NZ Selected price indexes, September
16 Oct 24	NZ CPI, September quarter
5 Nov 24	RBA Monetary Policy Decision
27 Nov 24	RBNZ OCR Review & Monetary Policy Statement

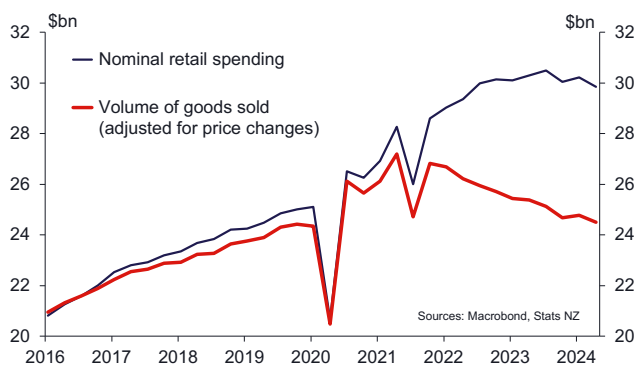
Turning to the housing market, data released by REINZ indicated that the number of home sales rebounded 7% in July after sales in the previous month were negatively impacted by the floating Matariki holiday (which was in July in 2023). The number of sales remains low and selling times remain longer than normal which was reflected in house prices falling 0.5% in July – the third consecutive decline. Especially large falls were seen Auckland (-1.3%) and Wellington (-1.8%). As a result, prices were almost unchanged from a year earlier (up 0.2%). The inventory of unsold homes rose to a fresh 9-year high in July, although the inventory to sales ratio did tick down from its very high level in June. Annual house price inflation is likely to turn negative next month but the focus is really on how quickly housing market activity responds to the marked decline in mortgage rates and the turnaround in interest rate expectations that has occurred over the past month. It's too early to tell right now.

House prices and sales volumes



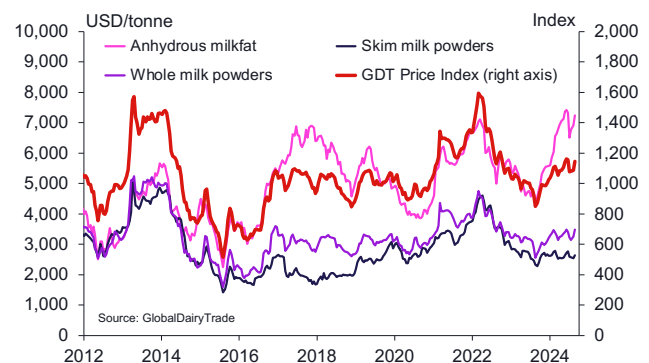
Consumer spending was downbeat but actually exceeded our expectations. Stats NZ's official retail sales report – an input into GDP calculations – showed a 1.2% decline in sales volumes in the June quarter. This result remains consistent with our view that GDP declined in the June quarter. The largest negative contributions to growth came from reduced spending on electrical and electronic goods and motor vehicles. The clampdown on discretionary spending was also highlighted by falls in spending on food and beverage services, apparel and recreational goods. By contrast, spending at supermarkets made a positive contribution to growth during the quarter.

Retail spending



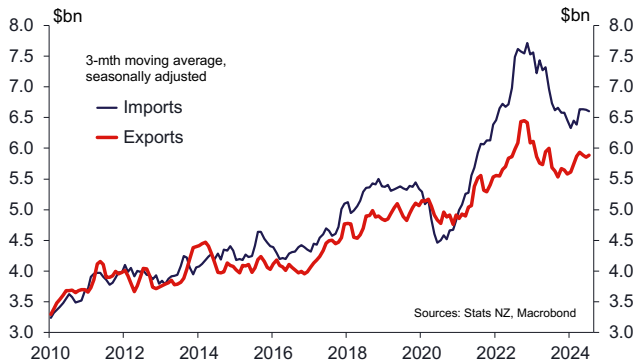
On a more positive note, last week's GDT dairy auction saw overall prices rise 5.5%, with prices for the key whole milk powder product rising 7.2%. A feature of the auction was significant participation by Chinese buyers, which doubtless played a role in driving prices higher. If prices can sustain these levels, then there are upside risks to our 2024/25 milk price forecast of \$8.40/kg. Indeed, last week Fonterra revised up its own midpoint forecast by 50c to \$8.50. That said, we need to be careful about extrapolating recent price trends. The reality is auction participation by the Chinese has been hit-and-miss this year and price volatility has been significant. Reflecting the fact that it is early in the season and most product is yet to be sold, Fonterra continues to place a wide plus-or-minus 75c range around its new midpoint forecast.

GlobalDairyTrade auction prices



In other news, a merchandise trade deficit of almost \$1.0bn in July was quite a bit wider than we had expected. Merchandise exports printed much as forecast, and over the past three months have increased 3.7% from the comparable period last year. However, imports rebounded more strongly than expected after a very weak June. While imports over the past three months are still down 1.3% on the comparable period last year, this is a much smaller decline than the 9.1% fall reported over the three months to April. Some of the rebound in July was due to a lift in petrol and intermediate imports from unusually low levels in June. However, imports of consumption goods and plant and machinery were also firmer than expected – the latter posting positive annual growth for the first time since May last year, despite firms reporting weak investment intentions. On the other hand, imports of motor vehicles remained weak, falling 26%/y/y in July.

Merchandise exports and imports



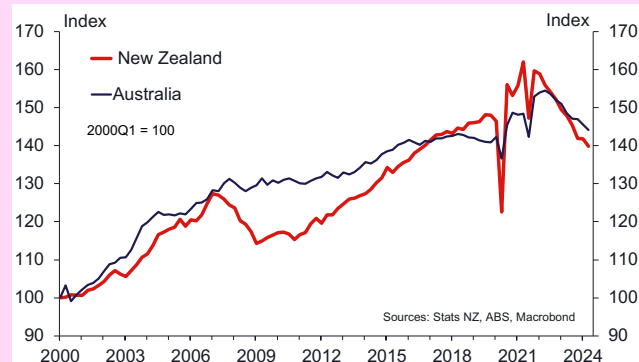
This week most interest will centre on the Monthly Employment Indicator for July and the ANZ Business Outlook survey for August. Whilst stabilising in the second half of July, weekly tax data suggests that the former will report a further decline in the number of filled jobs, with the reading for June likely to be revised lower as well. The ANZ survey will almost certainly report a lift in headline sentiment and forward-looking activity indicators (although some responses will likely have been received ahead of the RBNZ's rate cut). Of more interest will be what the survey has to say about recent levels of business activity and any developments in measures of firms' pricing intentions and inflation expectations.

Darren Gibbs, Senior Economist

Chart of the week.

Last week's retail sales report predictably revealed a further decline in real per capita spending – the tenth consecutive quarter of decline. In part that reflects the especially strong lift in spending on goods during the pandemic, when spending on services was necessarily curtailed. The experience in New Zealand is not unique - per capita spending in Australia has also declined in recent years -although per capita spending in New Zealand has tended to be much more cyclical/variable. The chart below shows that since the beginning of the millennium, growth in spending in aggregate has been quite similar in New Zealand and Australia, but New Zealand spending dropped more deeply following the Global Financial Crisis. This week we will publish a brief report highlighting some of the differences and similarities between the New Zealand and Australian experience across a range of key macroeconomic indicators.

Retail sales volume per capita

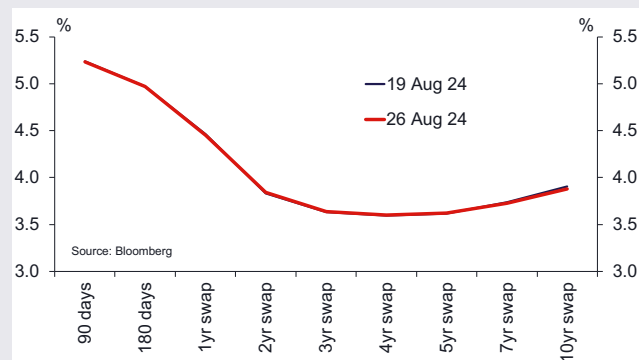


Fixed versus floating for mortgages.

Softer economic conditions have prompted the RBNZ to begin reducing the OCR. We expect further 25bp cuts at the October and November reviews, with easing continuing at a more gradual pace through 2025. However, market interest rates have factored in a much faster and deeper easing cycle than we are expecting.

With a significant amount of OCR easing already factored into longer-term mortgage rates, this suggests that it's now more attractive to fix for longer periods than it has been for a while – perhaps even for terms as long as two to three years. Mortgage rates for shorter terms of up to a year are substantially higher now but are likely to fall in the coming months towards current longer term fixed rates and might allow participation in a deeper easing cycle than markets expect.

NZ interest rates



Global wrap

North America.

Fed Chair Powell's prepared remarks at the Jackson Hole Symposium gave markets the signal for a September rate cut that they were looking for. Powell expressed more confidence that inflation is on a sustainable path back to 2% and noted that labour market conditions had cooled considerably and that "we do not seek or welcome further cooling". He concluded that "the time has come for policy to adjust... the timing and pace of rate cuts will depend on incoming data, the evolving outlook, and the balance of risks." Other Fed speakers throughout the last week referred to easing in a "methodical" fashion, suggesting that they favour 25bp moves rather than something larger. The most notable data in the week ahead is likely to be the PCE deflator, the Fed's preferred measure of inflation. We expect a 0.1% rise for July, holding the annual rate at 2.5%.

Asia-Pacific.

The minutes of the RBA's August meeting reinforced the Board's view that there is "less spare capacity than previously assumed", given stronger momentum in demand and a weaker assessment of the economy's capacity. Members noted that "the risk of inflation not returning to target within a reasonable timeframe had increased", and while the Board decided again to leave the cash rate unchanged, it warned that market pricing for rate cuts in the near future was likely to be disappointed. Our view remains that the first cut will be delayed until February next year.

Data was light in the region last week but picks up this week with Australia's monthly CPI indicator for July (from next month this will be temporarily dragged down by electricity rebates), retail spending (the first reading since tax cuts came into effect), and the last flurry of inputs to next week's June quarter GDP figures.

Europe.

Euro area inflation for July was unchanged in the final release, with prices flat for the month and up 2.6%yr. Constructive for the inflation outlook, the ECB's wage measure also moderated to 3.6%yr from 4.7%yr three months earlier. The data flow and commentary from officials continues to point to rate cuts in the euro area and the UK in the coming months.

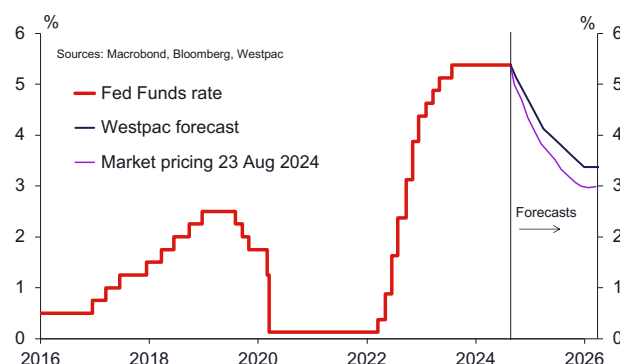
Trading partner real GDP (calendar years)

	Annual average % change			
	2023	2024	2025	2026
Australia	2.0	1.3	2.2	3.1
China	5.2	5.0	4.9	4.7
United States	2.5	2.5	1.7	1.7
Japan	1.9	0.3	1.1	0.9
East Asia ex China	3.3	4.2	4.2	4.1
India	7.8	7.0	6.8	6.5
Euro Zone	0.4	0.6	1.5	1.3
United Kingdom	0.1	0.6	1.3	1.4
NZ trading partners	3.4	3.3	3.4	3.4
World	3.2	3.3	3.3	3.2

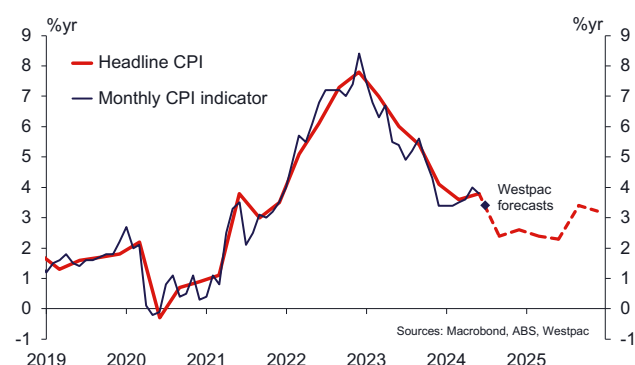
Australian & US interest rate outlook

	16-Aug-24	Sep-24	Dec-24	Dec-25
Australia				
Cash	4.35	4.35	4.35	3.35
90 Day BBSW	4.37	4.42	4.42	3.50
3 Year Swap	3.59	3.75	3.70	3.50
3 Year Bond	3.55	3.70	3.65	3.35
10 Year Bond	3.92	4.00	3.90	4.05
10 Year Spread to US (bps)	8	15	15	5
US				
Fed Funds	5.375	5.125	4.625	3.375
US 10 Year Bond	3.84	3.85	3.75	4.00

US Fed Funds rate



Australian CPI inflation



Financial markets wrap

Interest rates.

NZ swap rates consolidated last week, following the decline post-RBNZ MPS which started the easing cycle with a 25bp cut. This week we see potential for a resumption of the decline, following Fed Chair Powell's Jackson Hole speech which signalled that easing in the US would start at the next meeting on 18 September, and left its options open regarding the pace.

The event calendar this week is second-tier for NZ, although monthly filled jobs and the ANZ business confidence survey will be watched by the market, while in the US there is core PCE inflation data (the Fed's preferred inflation measure).

The 2yr swap rate, currently at 3.87%, could test the cycle low at 3.75% during the week ahead. Further declines below that during the next few weeks could be hard to come by, though, since much is already priced in. The next three meetings each have 100% chance of a 25bp cut and a 40% chance of a larger 50bp cut priced in. There is 200bp of cuts priced in for the year ahead, and a terminal rate of 2.75% (vs Westpac's forecast of 3.75%).

With so much of the easing cycle already priced in, it will require fresh news surprises for forward starting swap rates to fall much further. The cheapest of these is currently the 2yr swap starting in one year, at 3.25%. Forward starting swaps are currently at attractive levels.

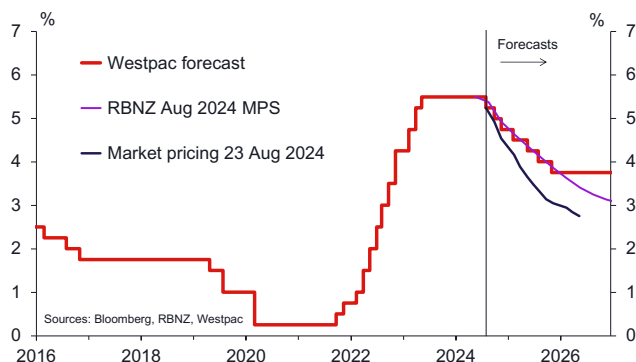
Foreign exchange.

NZD/USD has recovered strongly from the RBNZ's OCR cut two weeks ago, the main factor being the weakening US dollar. The latter fell further on Friday after Fed Chair Powell signalled easing would start at the September FOMC meeting. NZD/USD broke above 0.6220 – an important technical level, and if it sustains the move today, we'd be targeting 0.6350 during the weeks ahead.

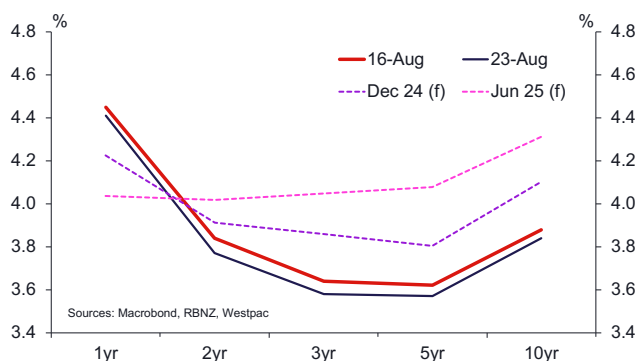
Global risk sentiment has improved, which also weighs on the USD. And NZ-US yield spreads, which fell to multi-year lows, have formed a tentative base.

Yield spreads have also formed a tentative base to support NZD/AUD during the week ahead. AU monthly CPI this week could help yield spreads recover further, and in turn, help the cross to rise to 0.9200. Multi-month, though, we remain bearish, targeting 0.8900, given the contrasting stances of the RBA and RBNZ, and contrasting fiscal and current accounts.

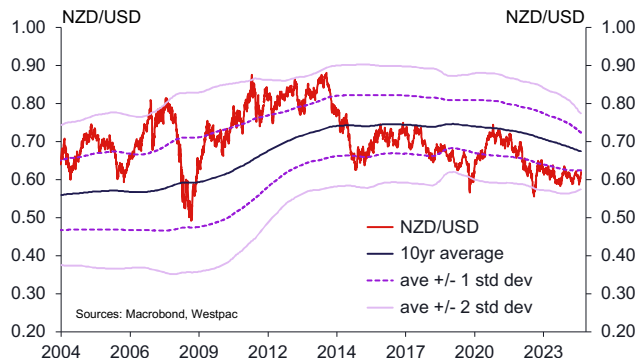
Official Cash Rate forecasts



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	0.623	0.586-0.620	0.555-0.743	0.645	0.61
AUD	0.917	0.897-0.929	0.873-0.992	0.930	0.91
EUR	0.557	0.542-0.573	0.517-0.637	0.581	0.55
GBP	0.472	0.456-0.484	0.456-0.535	0.503	0.47
JPY	89.8	86.1-98.6	61.3-98.6	80.2	91.5

The week ahead

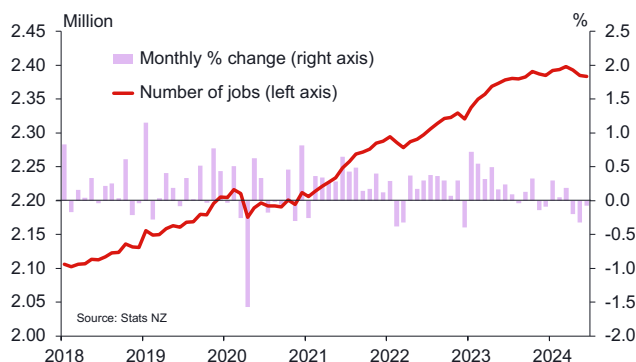
Jul employment indicator

Aug 28, Last: -0.1%, Westpac f/c: -0.3%

The monthly employment indicator is a comprehensive measure of the number of jobs, based on income tax records. Weekly snapshots provided by Stats NZ have shown a marked downturn over the last couple of months.

Note that the monthly indicator has tended to be overstated by around 0.3ppts on the first release. We expect that the 0.1% fall in June will be revised to a larger decline, and our pick of an initial print of -0.3% for July assumes future downward revisions too.

Monthly Employment Indicator filled jobs



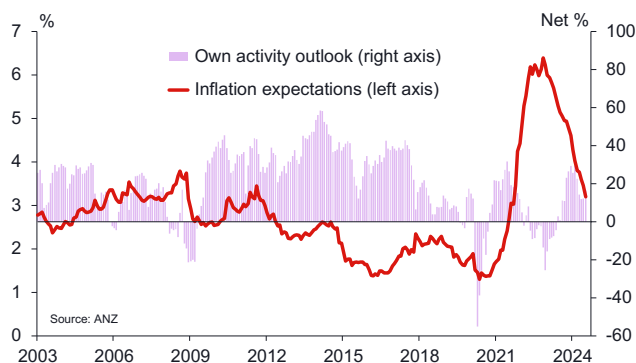
Aug ANZ business confidence

Aug 29, Last: 27.1

Business confidence lifted in July, though it remained at a relatively low level. Inflation indicators were mixed, with year-ahead inflation expectations falling to a three-year low, but firms' own price and wage expectations were little changed.

The RBNZ's dovish shift and the lower-than-expected CPI both occurred within the survey period, so we have yet to see their full impact on sentiment. Similarly, the RBNZ's surprise 25bp rate cut occurred mid-survey in August.

Business confidence



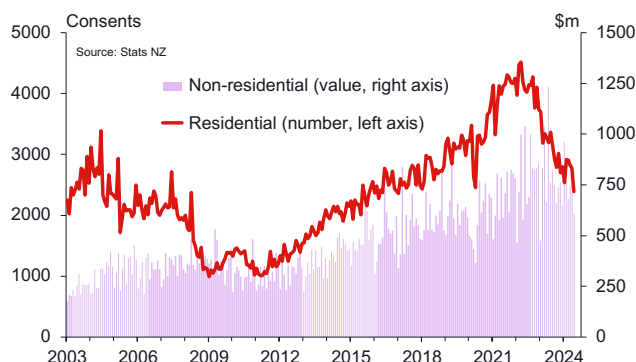
Jul building consents

Aug 30, Last: -13.8%, Westpac f/c: +10%

June saw a sharp fall in consent issuance. While that drop was likely overstated by the Matariki holiday, the broader trend in consent issuance is down. Consent numbers have fallen 25% over the past year with tight financial conditions and a soft housing market discouraging new work. We're expecting a 10% bounce in July, within a longer-term trend that remains soft.

Non-residential consent issuance has also been dropping back (though trends are mixed across segments). We expect that softness to continue for some time yet.

Building consents

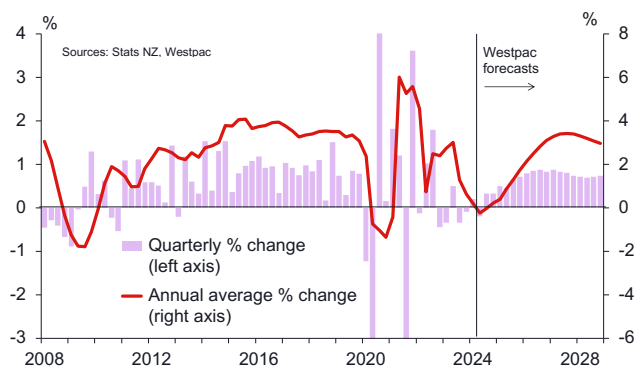


Economic and financial forecasts

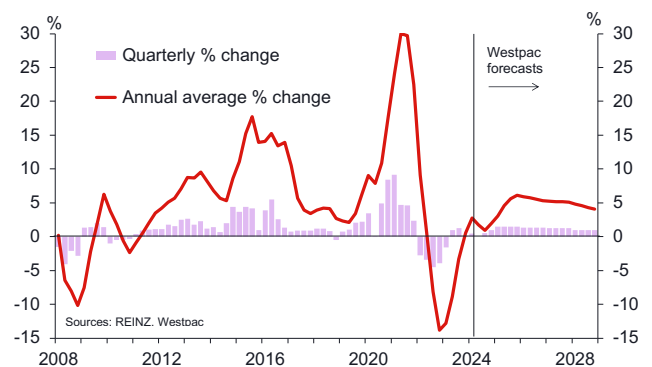
Economic indicators	Quarterly % change				Annual % change			
	Mar-24	Jun-24	Sep-24	Dec-24	2023	2024	2025	2026
GDP (production)	0.2	-0.6	-0.2	0.4	0.6	-0.3	1.3	2.3
Consumer price index	0.6	0.4	1.1	0.3	4.7	2.5	2.2	2.1
Employment change	-0.3	0.4	-0.4	-0.2	2.9	-0.4	-0.1	1.5
Unemployment rate	4.4	4.6	5.0	5.3	4.0	5.3	5.6	4.9
Labour cost index (all sectors)	0.9	1.2	0.7	0.7	4.3	3.5	2.3	1.9
Current account balance (% of GDP)	-6.8	-6.5	-6.0	-5.3	-6.9	-5.3	-4.0	-4.2
Terms of trade	5.1	3.2	1.7	-0.5	-10.7	9.8	2.4	1.8
House price index	0.4	-0.4	0.0	0.5	0.6	0.5	6.4	4.1

Financial forecasts	End of quarter				End of year			
	Mar-24	Jun-24	Sep-24	Dec-24	2023	2024	2025	2026
OCR	5.50	5.50	5.25	4.75	5.50	4.75	3.75	3.75
90 day bank bill	5.66	5.63	5.05	4.75	5.65	4.75	3.85	3.85
2 year swap	4.91	5.01	3.80	3.90	5.28	3.90	4.00	4.00
5 year swap	4.40	4.53	3.65	3.80	4.85	3.80	4.25	4.25
10 year bond	4.69	4.74	4.20	4.20	5.09	4.20	4.40	4.35
TWI	71.6	71.4	70.4	70.8	70.8	70.8	70.6	69.9
NZD/USD	0.61	0.61	0.60	0.61	0.60	0.61	0.63	0.64
NZD/AUD	0.93	0.92	0.91	0.91	0.93	0.91	0.89	0.88
NZD/EUR	0.56	0.56	0.55	0.55	0.56	0.55	0.56	0.56
NZD/GBP	0.48	0.48	0.47	0.47	0.49	0.47	0.48	0.48

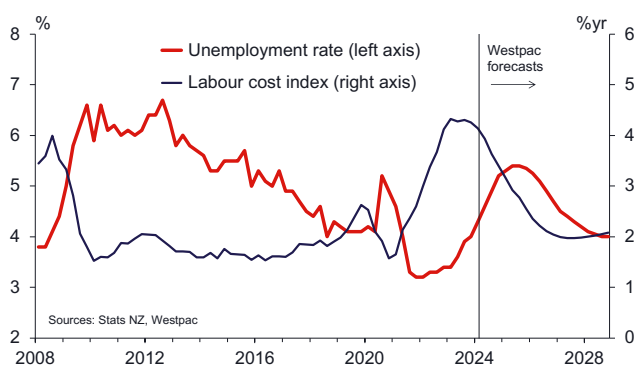
GDP growth



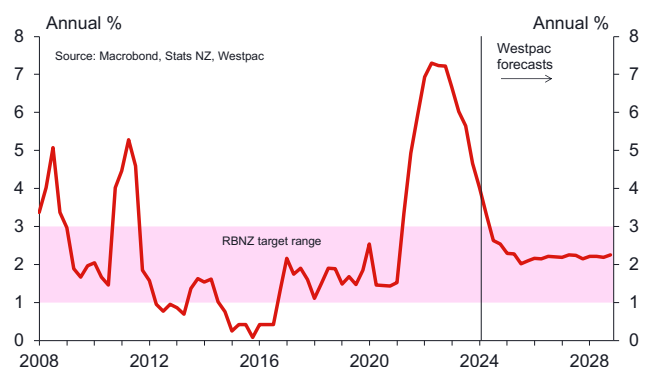
House prices



Unemployment and wage growth



Consumer price inflation



Data calendar

		Last	Market median	Westpac forecast	Risk/Comment
Mon 26					
Ger	Jul BusinessNZ PSI	87.0	-	-	Suggests headwinds to only slowly abate.
US	Jun Machinery Orders, %mth	-6.7%	3.9%	-	Investment outlook challenged by politics and cycle.
	Jul Leading Index, %mth	-17.5	-	-	Manufacturing is weak across the regions.
Tue 27					
Chn	Jul Industrial Profits, %yr	3.6%	-	-	Soft demand outlook remains a headwind to profitability.
US	Jun S&P/CS Home Price Index, %mth	0.34%	-	-	Robust price growth a reflection of limited inventory.
	Aug CB Consumer Confidence	100.3	100.0	-	Labour market softening, delaying sentiment recovery.
	Aug Richmond Fed Index	-17	-	-	Manufacturing is weak across the regions.
Wed 28					
NZ	GlobalDairyTrade Auction	0.5	-	-	Milk powder futures prices higher since last auction.
Aus	Jul Westpac-MI Leading Index, %yr	-0.13	-	-	Consistent with lacklustre growth momentum.
US	Jul FOMC Minutes	-	-	-	Participants will closely assess views on risks.
Thu 29					
NZ	Aug ANZ Business Confidence	27.1	-	-	Prospect & delivery of OCR cut may lift confidence further.
Aus	Q2 Private Business CAPEX, %qtr	1.0%	1.0%	-	Signs of firming.
Eur	Aug Economic Confidence	95.8	-	-	Significant uncertainty remains over outlook.
US	Q2 GDP, %ann	2.8%	2.8%	2.8%	Second estimate; no change expected.
	Jul Pending Home Sales, %mth	4.8%	-	-	Has been declining year-on-year for nearly three years.
	Jul Wholesale Inventories, %mth	0.2%	-	-	Steady inv-to-sales points to sound order management.
	Aug 24 Initial Jobless Claims, 000s	-	-	-	To remain low, for now.
	Jul Trade Balance, \$bn	96.6	97.5	-	Should narrow on softer consumer into year end.
Fri 30					
NZ	Aug ANZ Consumer Confidence	87.9	-	-	As with business confidence, may be boosted by OCR cut.
	Jul Building Consents, %mth	-13.8%	-	10.0%	Bounce after last month's fall, longer term trend weak.
Aus	Jul Retail Sales, %mth	0.5%	0.3%	0.8%	First official post-tax-cut read on consumer spending.
	Jul Private Sector Credit, %mth	0.6%	0.5%	0.4%	Tracking a modest 5.2% annual pace.
Jpn	Aug Tokyo CPI, %yr	2.2%	-	-	Path to sustainable at-target inflation is in sight.
	Jul Jobless Rate	2.5%	-	-	Labour market tight, and likely to remain so.
	Jul Industrial Production, %mth	-4.2%	-	-	Contraction from auto halts will prove temporary.
Eur	Aug CPI, %yr	2.6%	-	-	Services inflation sticky at twice the ECB's 2% target.
	Jul Unemployment Rate	6.5%	-	-	Holding firm at a historically low level.
US	Jul Personal Income, %mth	0.2%	0.2%	0.2%	Softening labour market to slow income growth...
	Jul Personal Spending, %mth	0.3%	0.5%	0.4%	... and eventually household spending.
	Jul PCE Deflator, %mth	0.1%	0.2%	0.1%	Inflation is at target on an ex-shelter basis.
	Aug Chicago PMI	45.3	-	-	Volatile around a very weak trend.
	Aug Uni. of Michigan Sentiment	67.8	67.8	-	Final estimate.
Sat 31					
Chn	Aug NBS Manufacturing PMI	49.4	-	-	Policy support will take time to filter its way through...
	Aug NBS Non-Manufacturing PMI	50.2	-	-	... the economy; downside risks to linger in the interim.

CONTACT

Westpac Economics Team | westpac.co.nz/economics | economics@westpac.co.nz

Kelly Eckhold, Chief Economist | +64 9 348 9382 | +64 21 786 758 | kelly.eckhold@westpac.co.nz

Satish Ranchhod, Senior Economist | +64 9 336 5668 | +64 21 710 852 | satish.ranchhod@westpac.co.nz

Darren Gibbs, Senior Economist | +64 9 367 3368 | +64 21 794 292 | darren.gibbs@westpac.co.nz

Michael Gordon, Senior Economist | +64 9 336 5670 | +64 21 749 506 | michael.gordon@westpac.co.nz

Paul Clark, Industry Economist | +64 9 336 5656 | +64 21 713 704 | paul.clark@westpac.co.nz

Imre Speizer, Market Strategist | +64 9 336 9929 | +64 21 769 968 | imre.speizer@westpac.co.nz

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