BNZ Weekly Overview

15 March 2012

Mission Statement

To help Kiwi businesspeople and householders make informed financial decisions by discussing the economy and its implications in a language they can understand.

The Weekly Overview is written by Tony Alexander. The views expressed are my own and do not purport to represent the views of the BNZ. To receive the Weekly Overview each Thursday night please click here.
http://feedback.bnz.co.nz/forms/Fx-I8ploskSGWgjN_7WOAw
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On The Road

This week I have spent most of the time on the road down in Christchurch giving talks so not much time has been available to write a decent article this week. Suffice to say that just as data releases in the United States have been turning out better than expected recently and leading to the benefit of the doubt being given to improving growth, so too are we seeing a more even matching of bad with good numbers here in New Zealand. We are closer to being able to talk about reaching the At Some State lift in our economy though e are not there yet.

This was the central theme in my talks for most of last year – that at some stage we would see growth in NZ aggressively boosted by rebuilding of Christchurch houses, feed-through of higher farmer spending into the cities, and arrival of debt comfort bringing greater business and household willingness to borrow and spend. There is actually an at some stage thing happening already in the form of young people leaving home in earnest to buy their own house – now that they no longer have people putting silly ideas in their heads about house prices collapsing and banks no longer giving out mortgages. Already Christchurch house prices have risen 7% in the past year and Auckland prices over 8%.

The inevitable result of an improving growth outlook is wholesale interest rates creeping higher and this week we have seen the benchmark three year swap rate rise to its highest level since early November. Back then the three year fixed housing rate was 6.99%. Now it is 6.15%. Hence my comment four weeks ago that if I were a borrower I would fix three years. It is fairly clear that unless a new shock comes along fixed housing rates are going to be lifted very soon.

As for the currency – this week it has pulled back as investors have moved into USDs. But an improving global growth outlook tends to lift commodity prices and risk tolerance so this is likely to be one of those temporary bouts of weakness written about before which provides an opportunity for exporters to get some extra hedging on board.

Enjoy the coming week. I’ll be catching up on analysis after four weeks on the road and finishing off the March Growing With China publication which will be released to subscribers on Tuesday.

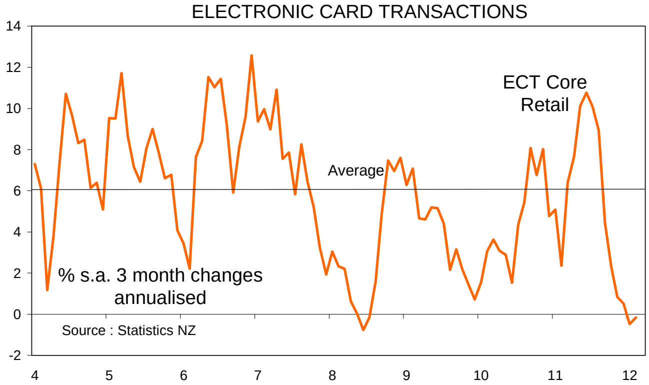
Is Our Economy Getting Better or Worse?

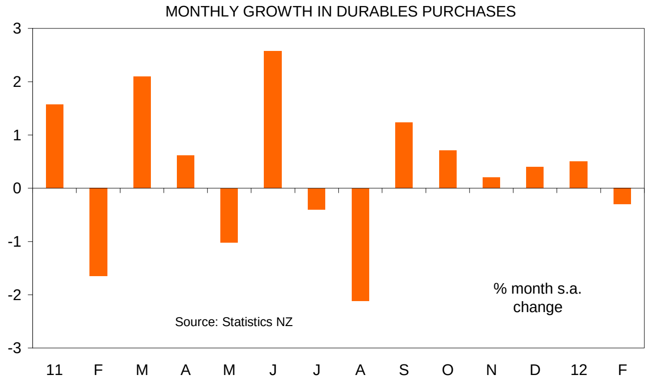
In this section we look only at what the data are actually telling us and pay no attention to forecasts or intentions measures.

The past week has produced surprisingly strong and surprisingly weak numbers which lead us to state that overall growth is occurring and maybe the positives are starting to dominate – though we have been here before and eventually the negatives came out on top.

Are householders opening their wallets more?

Our view has been that the September and December quarter unusually strong retail trade numbers have given a quite misleading view s to what is really happening with household spending and feedback from retailers suggests much of the boom was generated by hefty discounting on top of the temporary Rugby World Cup effect. This week we received further evidence of underlying weakness in consumer spending in the form of the monthly Electronic Card Transactions (ECT) release. It showed that core retail spending in seasonally adjusted terms weakened by 0.5% in February after rising 1% in January and sitting flat in December. Over the past three months spending using this measure has fallen at an annualised pace of almost 0.2% after growing 0.8% three months earlier and 8.9% six months ago (three months ending August).

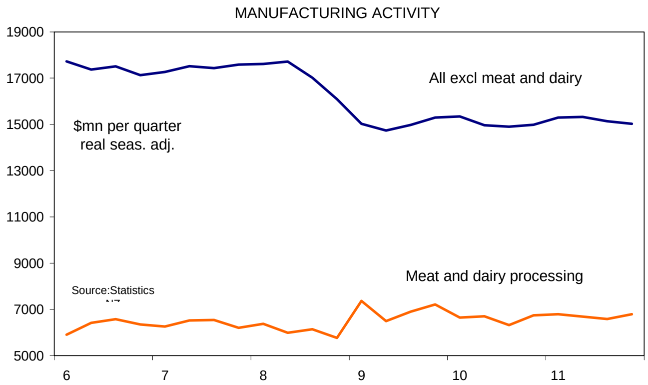




However we should not get overly pessimistic about household spending because annualised growth in durables spending was still 4% in the three months to February. Weakness occurred largely in spending on hospitality which fell 8.3%, and apparel which declined 6.6%.

Is business output rising?

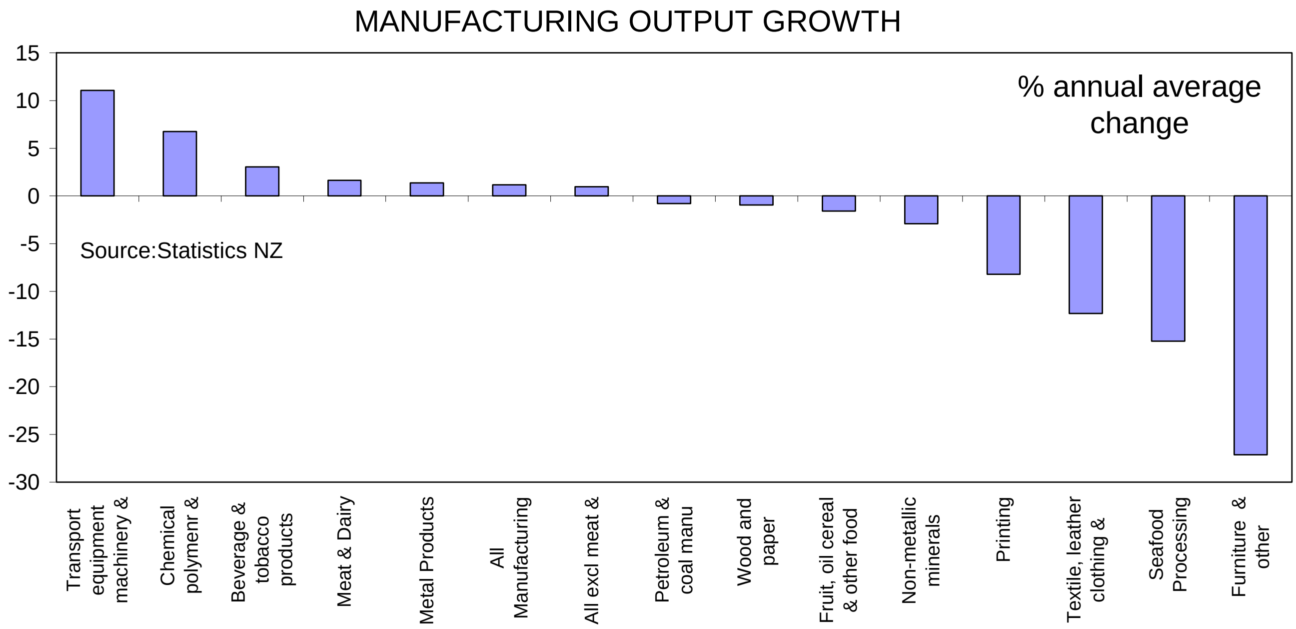
During the December quarter in real seasonally adjusted terms output of the manufacturing sector in total grew by 1.3% after falling 1.7% during the September quarter. This meant that for 2011 as a while manufacturing grew ½% after shrinking 1.6% over 2010, 5.1% over 2009, and 2.8% over 2008. the recovery is minor considering the 12.3% output fall from peak to trough.



But manufacturing data in NZ get distorted by the large milk and meat processing sectors which make up about 30% of production. Stripping them out we get a fall in output of 0.7% in the quarter following a 1.2%

fall in the September quarter. In other words, the entire 1.3% manufacturing boost plus more during the December quarter was simply due to more milk coming out of more cows, and more beasties meeting their maker.

For 2011 all up manufacturing excluding meat and dairy grew 1% after growing 0.3% over 2010, falling 12.2% over 2009, and worsening 1.9% over 2008. Output is only 0.8% off its lows and still 15.2% off levels in the first half of 2008. Not good really.



Are businesses hiring more people?

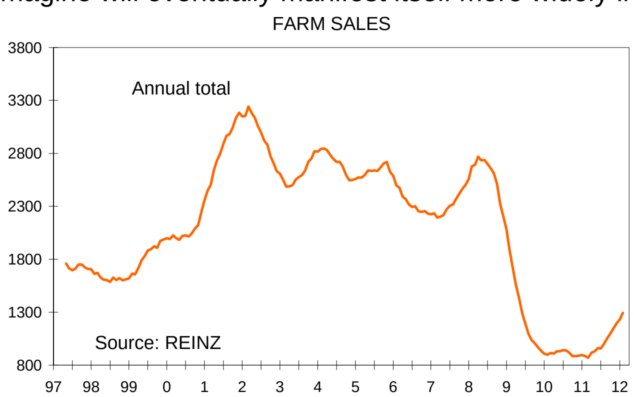
No fresh evidence.

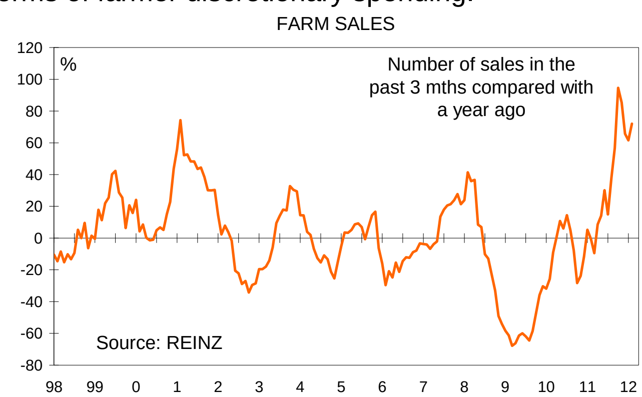
Are businesses boosting their capital spending?

For equipment yes. Buildings = mixed.

To see how businesses are feeling right now one can read our monthly BNZ Confidence Survey here. http://tonyalexander.co.nz/bnz-confidence-survey/

In February around New Zealand there were 120 farm sales. This makes for a gain of 72% in the three months ending February from a year earlier and clearly shows a revival in farming sentiment which we imagine will eventually manifest itself more widely in terms of farmer discretionary spending.





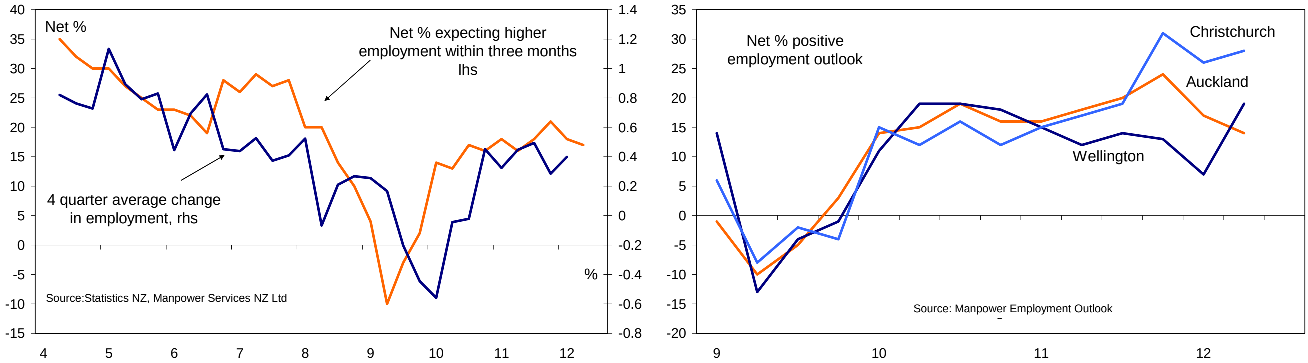
Average farm sale prices have increased 17% over the past year.

What Do The Leading Indicators Say?

In this section we look only at the factors which can at times give insight into where the economy is headed. Generally we will only cover newly released information.

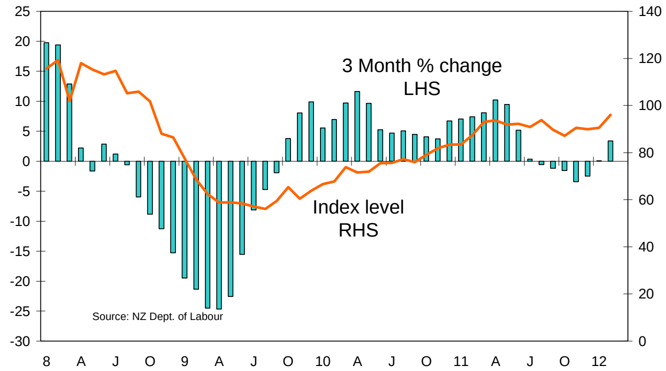
The quarterly Manpower Employment Outlook Survey found that a net 17% of employers plan boosting staff numbers. This is statistically unchanged from 18% in the March quarter and the 18% average for 2011. Therefore it is suggestive of no acceleration in jobs growth from the 0.5% over the last 3/4s of 2011.

MANPOWER SURVEY AND JOBS GROWTH



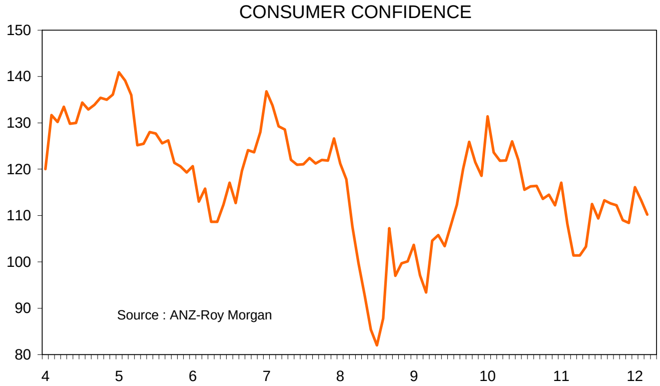
However, also this week the Department of Labour released their Jobs On-line survey of job advertisements placed on the Trademe and Seek websites. They found a strong 6.8% jump in ads which followed a 1% rise in January. The three month rolling change has now lifted to 3.2% from -2.4% three months earlier. This is a good result which for the first time since the middle of last year is suggestive of a lift in jobs growth.

ONLINE JOB ADVERTISING



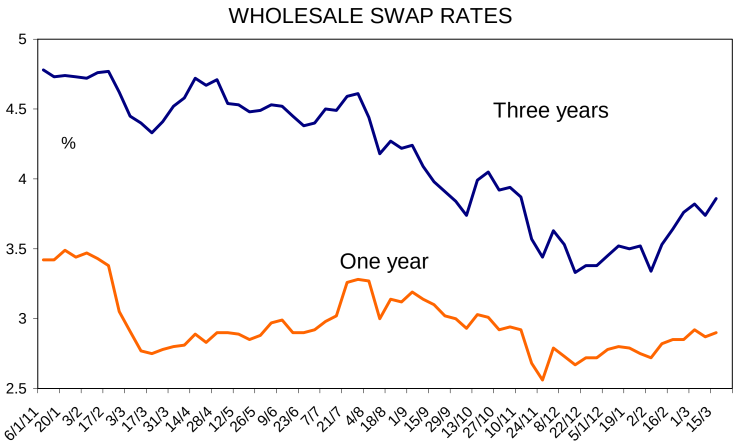
Given that both measures here are positive it is valid to expect jobs growth. But it does not yet add up to reasonably being able to anticipate accelerating jobs growth though that is our expectation for later in the year nonetheless – one hopes.

The ANZ-Roy Morgan Consumer Confidence Index weakened for the second month in a row in March to sit at 110 from 113 in February and 116 in January. Consumer sentiment regarding the coming year has deteriorated slightly and that suggests it is too early to expect sustained retail spending growth.



INTEREST RATES

With some positive data appearing in the United States wholesale interest rates there have risen and this has fed into higher rates also in NZ. The three year swap rate has climbed to 3.39% from 3.31% last year with some upward pressure also coming from an increase in fixed rate borrowing by the business sector. In particular more and more businesses are locking in fixed rates which will commence near the end of the year.

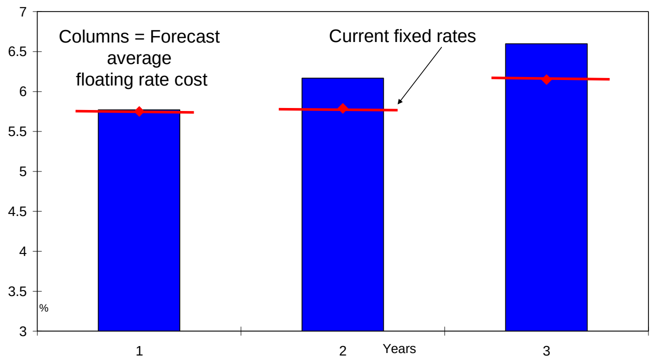


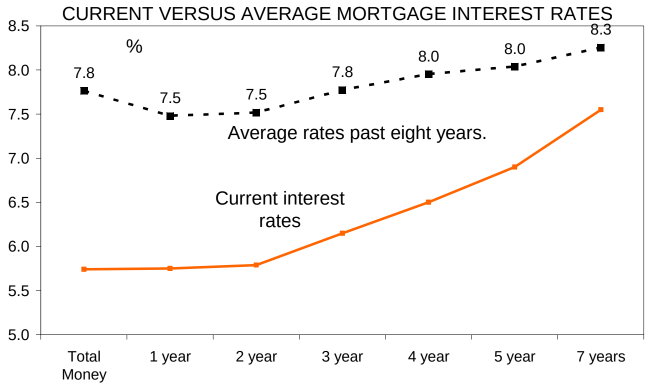
Our expectation remains for monetary policy tightening to commence late this year or more probably early in 2013, with the risk being that rates rise faster than the tiny tightening pencilled in by the Reserve Bank and the markets by the end of 2013.

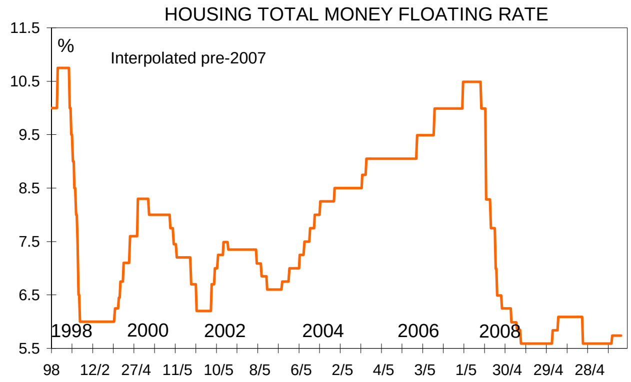
FINANCIAL MARKETS DATA	This week	Week ago	4 wks ago	3 months ago	Yr ago	10 yr average
Official Cash Rate	2.50%	2.50	2.50	2.50	2.50	5.4
90-day bank bill	2.77%	2.77	2.76	2.74	2.68	5.7
1 year swap	2.90%	2.87	2.85	2.67	2.75	5.8
3 year swap	3.39%	3.31	3.17	2.93	3.71	6.1
5 year swap	3.86%	3.74	3.64	3.33	4.33	6.3
180-day term depo	4.50%	4.50	4.50	3.60	4.90	5.7
Five year term depo	5.85%	5.85	6.00	6.00	6.75	6.4

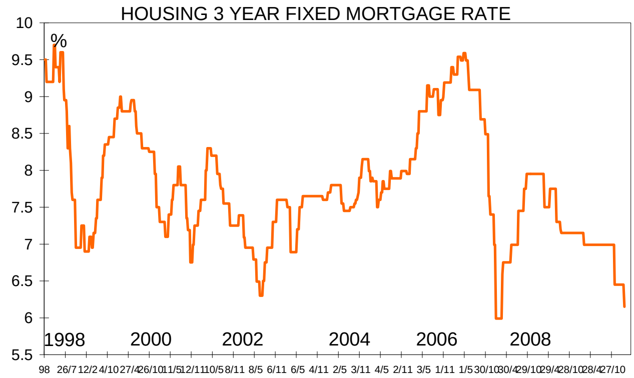
If I Were a Borrower What Would I Do?

Given that the extra I must pay to fix is the lowest I feel it will reach this cycle I would be inclined to fix three years.







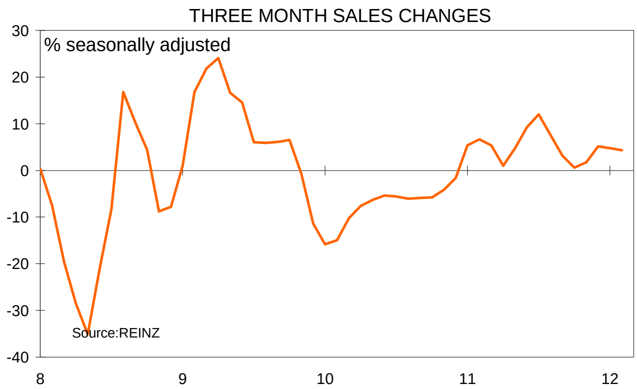


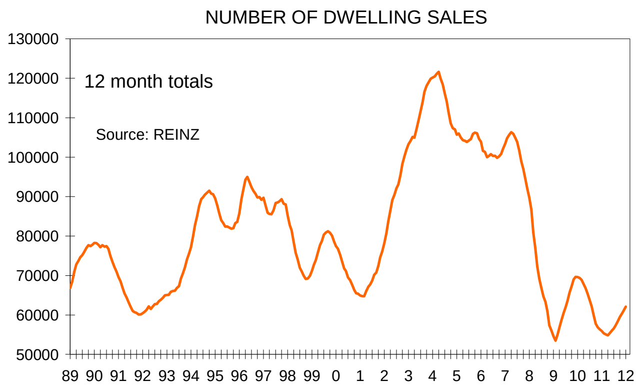
HOUSING MARKET UPDATE

To view the most recent results of our monthly BNZ-REINZ Residential Market Survey click here.
http://tonyalexander.co.nz/bnz-reinz-survey/

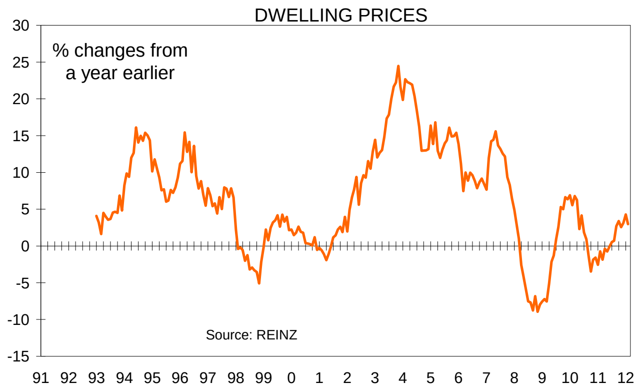
Sales Rise Strongly

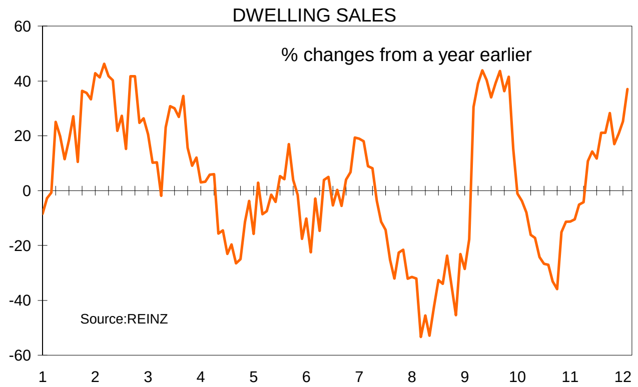
The REINZ reported this week that in February real estate agents around New Zealand sold 6,168 dwellings. This was a very strong 37% rise from a year earlier and 3% gain in seasonally adjusted terms from January. Over the past three months sales have risen 4.3% seasonally adjusted after rising 1.8% in the three months to November. There is therefore some evidence of an acceleration in the pace of growth of dwelling sales.



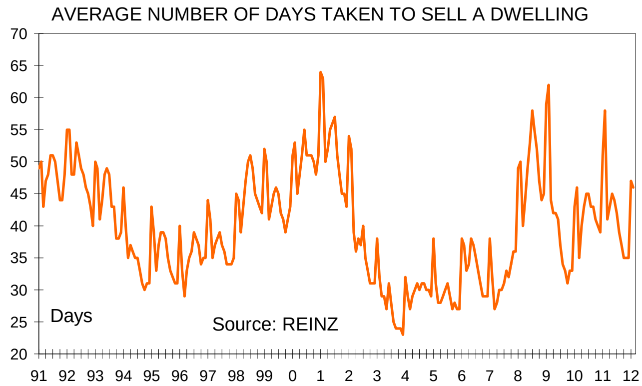


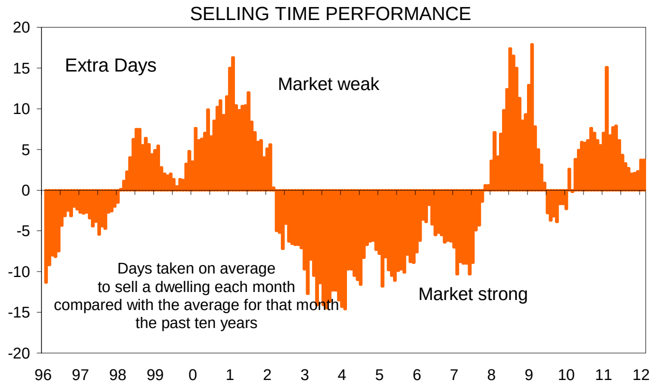
The stratified median sales price improved another 0.8% in the month to lie 3% ahead of a year ago but down 0.2% in the past three months compared with up 2% in the three months to November. We read these numbers as telling us that prices are rising but at a slow pace.



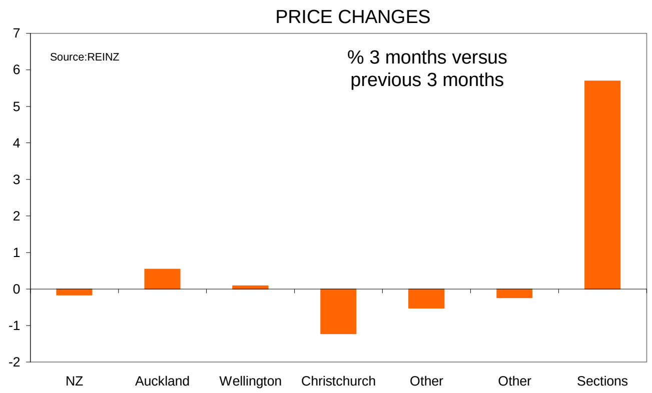


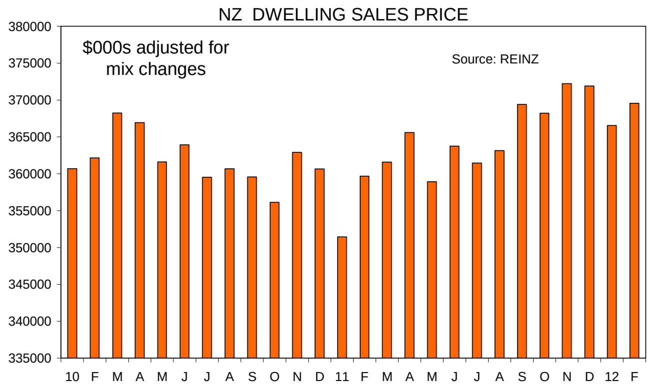
On average in February it took 46 days to sell a dwelling. This was 3.7 days longer than average which is exactly the same result for January. This suggests no acceleration yet in the pace of sales though that is likely to change as strong sales in February likely soaked up some of the longer sitting market stock and March's days to sell number is likely to be far closer to average.





All up the results tell us that the NZ housing market is improving but the pace of price gains is as yet very mild. Having said that, in Auckland where sales have improved 4% in the past three months prices have risen 0.5% and lie 8.7% up from a year ago. Wellington prices are down 2.7% from a year earlier and Christchurch ahead 7.1%.





MAJOR OFFSHORE ISSUES

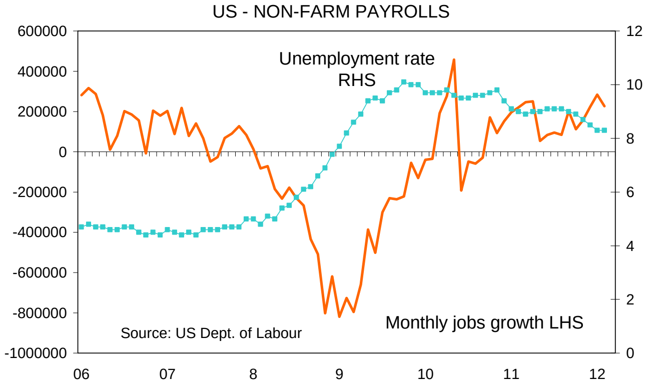
European Debt

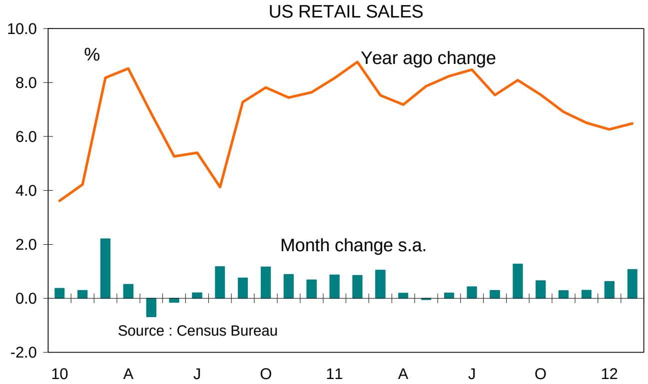
Enough holders of Greek government bonds agreed to the proposed haircut that this week Greece was able to force all private holders to loss some 75% of their investment and €105bn of Greece's €365bn debt was written off. Compared with 2008 when all of Greece's government debt was held in the private sector now only 27% is with the rest held by other EU members, the ECB, and the IMF. The private sector bond haircut means Greece's debt to GDP ratio is still expected to be the highest in the EU come the end of this year just over 150% of GDP. On that basis and with few people expecting Greece will fundamentally alter its economic structure (and tax-dodging) behavior to deliver sustained strong revenue generating growth the expectation is that yet another bailout will be required down the track. That means the debt debacle is going to remain on the European analytical radar for at least the next two years. For now though things have settled down and attention will more firmly focus on the depth of the latest recessions in a number of Euro-Zone economies.

United States Growth

Improving data, more upbeat Fed = USD, equities and US interest rates all up.

There were probably quite a few sighs of relief when the monthly non-farm payrolls report for February printed slightly better than expected on Friday night rather than delivering a weak result which would have severely dented the generalised view of improving US growth. Employment rose by 227,000 in the month which was just above expectations. But the January increase previously reported as 243,000 was revised up to 284,000. The December result was also boosted 20,000. The unemployment rate held steady at 8.3%.





Over the past two years 3.5 million net extra jobs have appeared in the US and this growth may account for a strong lift in retail spending in February which prompted a 218 point rally in the Dow Jones share index on Tuesday night. US retail sales rose by a higher than expected 0.9% excluding autos, taking sales in the past three months to 6.2% ahead of a year earlier. The bars in the second graph above hint at accelerating spending growth.

The growing view that US growth is improving was reflected in the Federal Reserve's Open Market Committee report this week in which growth forecasts were lifted and more positive commentary was employed regarding growth prospects, jobs growth etc.

The upshot is that investors have moved funds into equities in the US and other countries, US bond yields have risen, and the USD has been bought.

Australian Growth

No time this week.

China

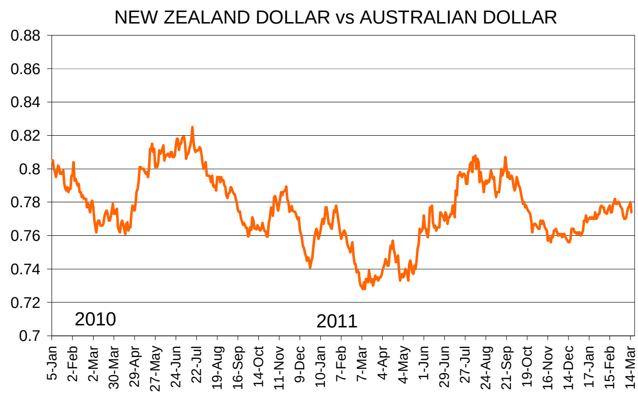
Chinese economic developments will now be covered in our new publication "Growing With China", the next issue of which will appear on March 20. If you wish to receive this monthly then please email me specifying your name, company name, and connection with China. Tony.alexander@bnz.co.nz

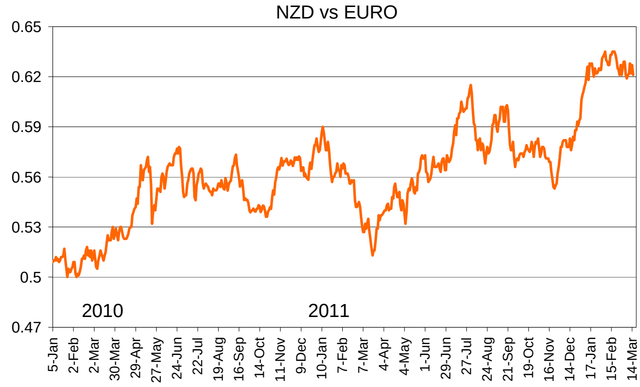
Exchange Rates

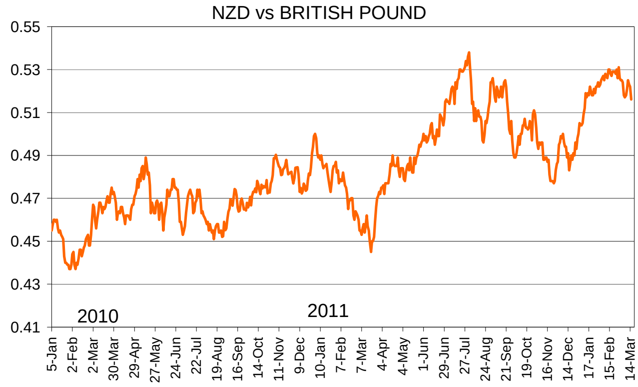
Exchange Rates	This Week	Week ago	4 wks ago	3 Mths ago	Yr ago	10 yr average
NZD/USD	0.808	0.816	0.830	0.748	0.739	0.67
NZD/AUD	0.774	0.771	0.778	0.756	0.732	0.85
NZD/JPY	67.800	66.200	65.100	58.400	60.3	69.6
NZD/GBP	0.516	0.518	0.530	0.483	0.457	0.388
NZD/EUR	0.621	0.621	0.633	0.576	0.528	0.52
NZDCNY	5.117	5.153	5.227	4.766	4.855	4.99
USD/JPY	83.911	81.127	78.434	78.075	81.597	105.7
USD/GBP	1.566	1.575	1.566	1.549	1.617	1.72
USD/EUR	1.301	1.314	1.311	1.299	1.400	1.28
AUD/USD	1.04	1.06	1.07	0.99	1.01	0.788
USD/RMB	6.3332	6.3147	6.298	6.3713	6.5701	7.56

Kiwi Weakens Again

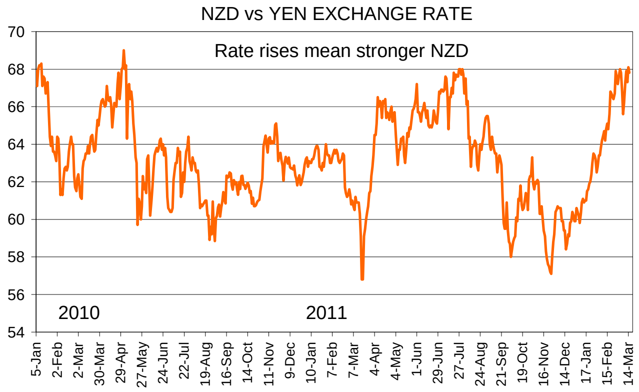
The FX market story this week has predominantly been one of the US dollar rising in response to positive economic data. Hence we have dropped almost one US cent while rising slightly against the AUD and JPY while sitting steady against the Euro and GBP.

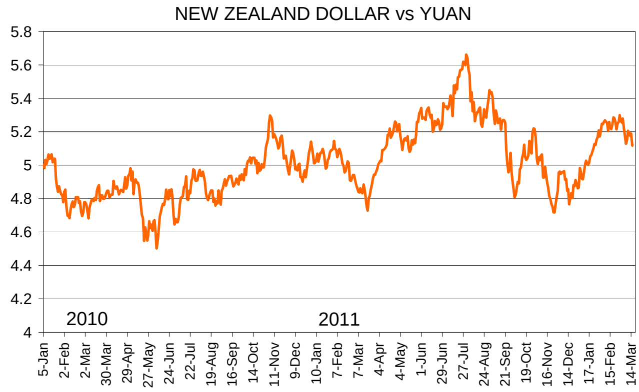




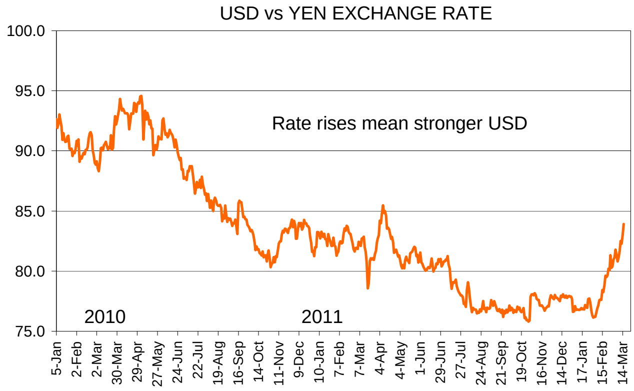


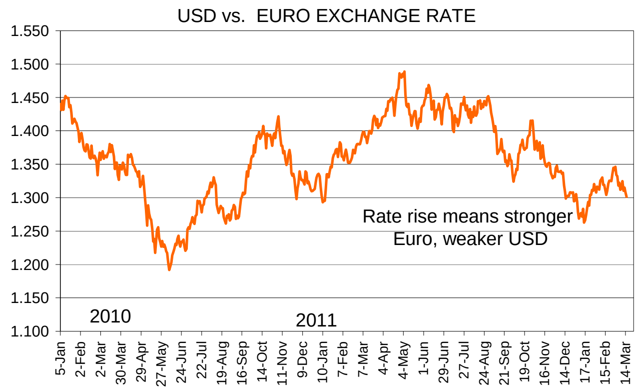
Last Friday the Dominion Post ran a headline on the Business page indicating that I am predicting the Kiwi dollar to hit US88 cents again. I am. But what might not have come across well enough in the article is that this is something I expect to happen with greatest probability only when the NZ monetary policy tightening is underway. That is because as a rule when NZ interest rates are rising the NZD goes up as well. All that will be different this cycle is that the starting point for the policy-induced rise will be much much higher than in the past. Plus it is highly unlikely that over 2013 and 2014 the Federal Reserve will be raising interest rates in the United States. Then on top of that, with wage-driven inflationary pressure likely to become worrying in Australia the RBA is likely to be tightening again come 2013-14 and as this pushes the AUD even higher we will ride its coat-tails.





Timing on all of this – as with all forecasts around the planet currently – is of course very uncertain so one should not be silly enough to ask in which part of 2013 the NZD will hit 88 cents. Note that this is not the same question as where will the peak in the NZD be. History tells us we have no hope of picking that.





Exchange Rate Assumptions

This table contains the latest NAB currency forecasts. In red I indicate where I believe the risk lies for these rates. You are welcome to toss your own coin and generate an equally valid table.

	2011	2012	Risk	2013	Risk

Year end					
NZD/USD	0.77	0.82	Higher	0.77	Higher
NZD/AUD	0.76	0.82		0.81	
NZD/YEN	60.0	66		63	Higher
NZD/GBP	0.50	0.53	Higher	0.50	Higher
NZD/EUR	0.60	0.64	Higher	0.57	Higher
USD/JPY	78	81	Lower	82	Lower
GBP/USD	1.54	1.56	Lower	1.53	Lower
EUR/USD	1.30	1.29	Lower	1.36	Lower
AUD/USD	1.01	1.00	Higher	0.95	Higher

ECONOMIC DATA

All %		Latest qtr only	Previous qtr only	Latest year	Year ago	2 Yrs ago
Inflation	RBNZ target is 1% - 3% on average	-0.3%	0.4	1.8	4.0	2.0
GDP growth	Average past 10 years = 2.6%	0.8	0.1	+1.3	1.0	-2.7
Unemployment rate	Average past 10 years = 4.8%	6.3	6.6	......	6.7	6.9
Jobs growth	Average past 10 years = 1.9%	0.2	0.2	1.6	1.3	-2.2
Current a/c deficit	Average past 10 years = 5.5% of GDP	4.3	3.7	......	3.5	3.0
Terms of Trade		-0.6	2.4	3.4	17.9	-14.1
Wages Growth	Stats NZ analytical series	1.0	0.8	3.4	3.4	3.7
Retail Sales ex-auto	Average past 9 years = 3.9%.	2.9	2.6	4.0	1.9	-1.0
House Prices	REINZ Stratified Index	-0.2	2.0	2.7	-0.6	5.5
Net migration gain	Av. gain past 10 years = 13,900	-3,134	-103yr	......	8,689	22,588
Tourism – an. av grth	10 year average growth = 3.2%. Stats NZ	2.9	1.2	2.9	2.8	-0.0
		Latest year rate	Prev mth year rate	6 mths ago	Year ago	2 yrs ago
Business confidence	BNZ survey	27	13	36	-12	35
Consumer confidence	ANZ-Roy Morgan 100=neutral	110	113	113	101	122
Household debt	10 year average growth = 10.3%. RBNZ	1.0	1.1	1.2	1.8	2.9
Dwelling sales	10 year average growth = 2.5%. REINZ	37.0	25.2	21.1	-10.5	-3.8
Floating Mort. Rate	(TotalMoney) 10 year average = 7.9%*	5.74	5.74	5.59	6.09	5.59
3 yr fixed hsg rate	10 year average = 7.8%	6.15	6.15	6.99	6.99	7.95

All actual data excluding interest & exchange rates sourced from Statistics NZ.
The BNZ Weekly Overview is prepared by Tony Alexander, Chief Economist at the Bank of New Zealand. Ph 04 474-6744 tony.alexander@bnz.co.nz www.tonyalexander.co.nz

Key Forecasts

Dec. year		2010	2011	2012	2013
GDP	annual average chg	1.4	1.5 – 2.0	1.5 – 2.2	2.5 – 3.5
CPI	on year ago	4.0	1.8	2.0 – 2.6	2.5 – 2.9
Official Cash rate	end year	3.0	2.5	2.25 – 2.75	3.25 – 4.25
Employment	on year ago	1.3	1.5 – 2.0	1.0 – 1.6	1.5 – 1.9
Unemployment Rate	end year	6.8	6.0 - 6.5	5.5 – 6.0	4.8 – 5.5

*extrapolated back in time as TotalMoney started in 2007