BNZ Weekly Overview

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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.
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If you wish to email me a comment on any matter discussed here please feel free to do so. All emails will be treated in confidence and if I reprint any insightful comment it will be without any identifying material. tony.alexander@bnz.co.nz

House Buyers

Many thanks to the near 600 real estate agents who a week and a half ago replied to our monthly BNZ-REINZ Residential Market Survey regarding conditions in the market. The results were released to this emailing list and showed a lift in most measures from where they were in early-December, A record net 35% of respondents said they are seeing more investors, and a near record net 48% said they are seeing more first home buyers.

Upon visiting Auckland this week and even before speaking with a group of Barfoot and Thompson real estate agents of an evening in Newmarket the discussions I had with many people centred around the housing market and how homes are selling at auctions for far more than they had been expecting. A few more anecdotes were thrown my way regarding the presence of Chinese buyers.

In the survey of last week I added a couple of questions quickly just before sending it out regarding whether agents were noticing more or fewer foreign buyers, and if so where they came from. The net outcome was zero and I am unsure how to interpret that so let's ignore it. But the proportions of foreign buyers by source did yield some useful information.

Nationwide if buyers come from offshore then 27% appear to come from the UK, 24% from China, 22% from Australia, then a mish mash after that. For Auckland the proportions were 45% China, 18% UK, 10% Australia.

However, had I had enough time to design the questions properly I'd have been able to get more useful information regarding specifically the proportion of total sales which appear to be going to offshore buyers, first home buyers, and investors (from wherever). That is what will be in the next survey which will go out to agents on March 11 evening. Then finally we will get a fairly good view as to the role which each of these groups is playing in housing markets nationwide and on a regional basis.

Speaking of China, on Monday I will release two papers on China. The first will be my monthly Growing With China publication. It will contain the usual examination of China's economy and trade data between NZ and China (they now take 16.8% of our goods exports by value and sent 38% extra holiday-makers our way last year). I'll also have comments from NZ Trade and Enterprise Regional Director for China Rod McKenzie.

The issue will also contain some thoughts from Richard Fyre of the NZ China Trade Association on ‘Avoiding Disputes in China”, and from Keith Marshall “The Future of NZ’s Education System Relationship With China”.

The second publication will be something I started working on back in September and took time to put the finishing pieces on while on the Gold Coast last month ‘Sources of Western Apprehension about China”. This paper contains a list of 55 reasons why people in the West feel apprehension about China.

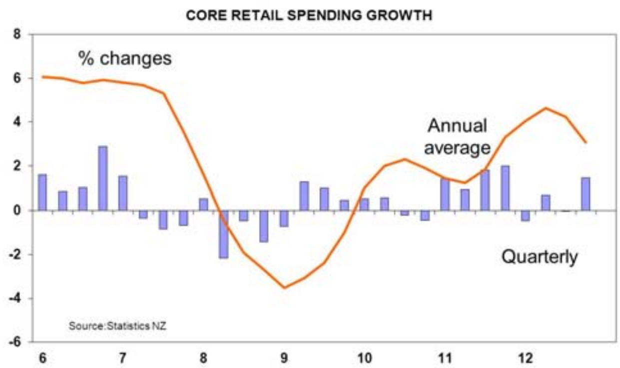
Where are foreign buyers from?

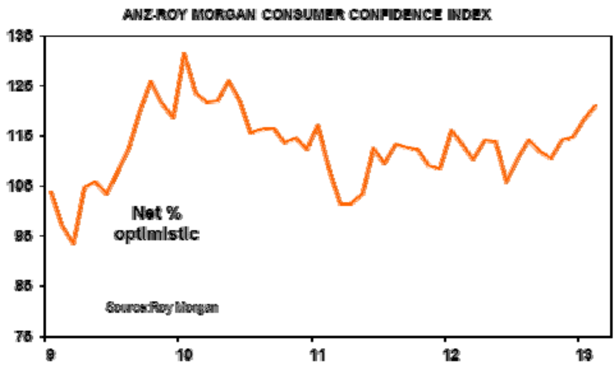
	Australia	China	Europe Excl. UK	India	Other Asia	UK	USA	Other
Northland	47.6	4.8	11.9	0.0	2.4	26.2	7.1	n/a
Auckland	9.8	44.8	5.7	9.5	9.5	18.3	2.5	n/a
Waikato	28.8	16.9	5.1	6.8	3.4	35.6	3.4	n/a
Bay of Plenty	31.8	9.1	4.5	6.8	2.3	40.9	4.5	n/a
Hawkes Bay/Gisborne	32.3	6.5	3.2	3.2	6.5	41.9	6.5	n/a
Taranaki	17.4	13.0	8.7	4.3	4.3	47.8	4.3	n/a
Manawatu/Wanganui	43.5	17.4	4.3	8.7	4.3	17.4	4.3	n/a
Wellington	26.2	9.8	8.2	1.6	3.3	44.3	6.6	n/a
Nelson/Marl. W. Coast	38.9	5.6	5.6	0.0	0.0	33.3	16.7	n/a
Canterbury	23.3	21.9	6.8	2.7	5.5	38.4	1.4	n/a
Otago	47.6	4.8	11.9	0.0	4.8	26.2	4.8	n/a
Southland	Opps. Forgot							
All	21.7	24.4	6.1	5.5	5.9	26.8	2.7	6.9

On Monday I sent a copy of my new monthly publication ‘Brain Gain NZ” out to my emailing list plus a few outside agencies. If you received it please feel free to send to anyone you know offshore who may be interested. Feedback on the first issue has been tremendous, but the challenge I face is actually getting it in front of the expat community. Going through Kea is unfortunately not an option as they now take sponsorship from another bank. So if you feel you can help in getting it out there please email me. Tony.alexander@bnz.co.nz

Recent Economic Data

The main collection of economic data worth mentioning here and released in the past week was last Friday’s Retail Trade Survey. During the December quarter Core retail spending in real seasonally adjusted terms rose by 1.5% after being flat in the December quarter and rising 0.7% in the June quarter. The result was stronger than market expectations and included a 3.7% rise in spending on furniture and floor coverings, 4.2% rise in spending on hardware and building materials, and 2.9% gain in spending on electrical goods.





The result does not mean that the retail sector is somehow booming given that for the year as a whole the volume gain across all categories including motor vehicles was 3.7% or 3.1% core. And the past two quarters annualise to a core growth rate of 3%.

Nevertheless, we have the January debit and credit card data in hand showing 0.4% seasonally adjusted nominal growth, plus rising consents for residential and non-residential buildings, rising house prices making people feel wealthier, and consumer confidence strengthening as measured in the Roy Morgan Survey.

INTEREST RATES

There is increasing upward pressure appearing on wholesale interest rates in New Zealand and that is going to be the story we think for all of this year – though in a stop-start fashion. One has learnt to hedge one's bets regarding the speed of interest rate rises given the appalling rate forecasting record we all have from the past four years.

Pressure for first fixed rates then much, potentially much, later floating rates to go up is coming from the global switch from fixed interest securities to assets like property and equity, plus growing signs of strength in New Zealand's economy – though only the domestic bit. Yes folks we have been here before. This is one of those unbalanced upturns in our economy where domestic activity including house building and prices rises firmly, but the export sector gets munted by a high exchange rate which is going to get pushed even higher once the monetary policy tightening cycle kicks off.

But it is even worse than that. Much of the domestic upturn we are experiencing and will experience is built upon replacing buildings which have fallen or been torn down, and upgrading the existing stock to meet water-tightness and earthquake requirements. This is not activity which boosts a country's productivity or lessens external imbalances.

In fact our external imbalances will get worse whether measured in terms of the current account deficit or net international liabilities. Theory tells us that one day these developments will cause a substantial downward currency correction. But anyone forecasting the NZD's movements on this basis has been sitting waiting 28 years so far for this adjustment to occur and may still be waiting for another 28 years. Or the adjustment could happen next month. There is simply no way of knowing when the international financial community will decide that credit-worthiness of New Zealand is bad. Frankly for now they look at New Zealand and see a place which looks a lot better than many other locations in the Western world.

What this means is that the NZ dollar is highly likely to not just remain strong but go higher. That means it will help suppress the inflationary pressures we expect to come from the booming construction sector. That means the RB will be reluctant to raise the cash rate for some time – especially as their moves will just drive the NZD higher and generate even more export sector pain and outright shrinkage.

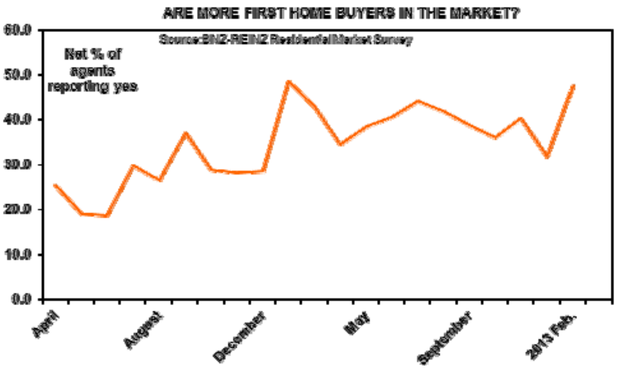
FINANCIAL MARKETS DATA

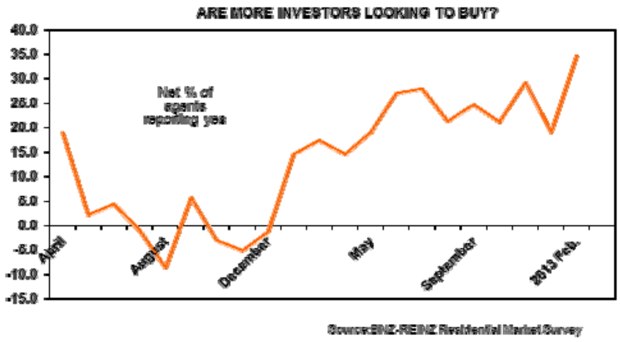
	This week	Week ago	4 wks ago	3 months ago	Yr ago	10 yr average
Official Cash Rate	2.50%	2.50	2.50	2.50	2.50	5.4
90-day bank bill	2.70%	2.70	2.66	2.67	2.76	5.7
1 year swap	2.84%	2.86	2.77	2.60	2.85	5.8
3 year swap	3.27%	3.20	3.03	2.83	3.29	6.1
5 year swap	3.64%	3.52	3.33	3.12	3.76	6.3
7 year swap	3.93%	3.83	3.63	3.44	4.15	

HOUSING MARKET UPDATE

Nothing

This week we have not received any fresh news on the state of the housing market. But I've put together my next article for the NZ Property Investor magazine and sent it through so keep an eye out for that in the shops. For your guide, here is the link to my November 1 2012 weekly Overview in which on page 5 you will find a list of 19 reasons why Auckland house prices will keep rising. http://tonyalexander.co.nz/wp-content/uploads/2013/02/WONovember-1.pdf





Minimum LVRs?

Will the Reserve Bank try to stem the rise in the housing market by forcing banks to impose maximum loan to value ratios (LVRs) = minimum % deposits? No.

- Housing conditions including affordability and availability vary across the country and measures put in place to combat Auckland's price squeeze would be quite wrong for a lot of the rest of New Zealand.
- Young buyers would be near completely shut out of the market as few have a deposit of, say, 30%.
- Investors would down-shift to buying lower priced properties in order to meet a lower LVR, thus increasing competition in the price range first home buyers are looking.
- Many offshore buyers (detail coming in next month's BNZ-REINZ Residential Market Survey) tend to buy with cash. They would not be affected.

Thus the impact of maximum LVRs would basically be to prevent young NZ-domiciled Kiwis from buying property and opening up greater opportunities for offshore cashed up buyers. Now who on earth is going to vote for that?

If I Were A Borrower What Would I Do?

I'd look at managing my interest rate risk with a mix of half my debt floating or at short term fixed rates out to two years, and the other half locked in for 3-5 years taking advantage of any discounted rate a lender might be offering as part of a market positioning campaign. You see with the housing market picking up lenders are presented with the opportunity to gain some good sales growth and that means a mixture of rate discounting, advertising, and encouragement of borrowers to take interest rate only deals etc.

OFFSHORE

In Europe the week started quite badly with news that European GDP shrank 0.6% during the December quarter whereas a fall of "only" 0.4% had been expected. Germany shrank 0.6% and France 0.4%. However sentiment improved, sharemarkets rose and the Euro firmed after the monthly ZEW business sentiment gauge in Germany came in at a much better than expected level.

In the United States consumers are increasingly in good heart. The monthly University of Michigan consumer sentiment index rose to a higher than expected 76.3 this month from 73.8 in January. But this is not really any different from the 75.3 level of exactly a year ago and it is still below the 100 neutral reading. Therefore it would seem wrong to conclude that things are into safe territory in the United States. In fact at the Group of 20 meeting over the weekend the Federal Reserve board Governor ben Bernanke made it clear that he intends keeping US monetary policy very loose.

Exchange Rates

Exchange Rates	This Week	Week ago	4 wks ago	3 Mths ago	Yr ago	10 yr average
NZD/USD	0.836	0.847	0.84	0.815	0.839	0.67
NZD/AUD	0.814	0.818	0.795	0.786	0.78	0.85
NZD/JPY	78.3	79.3	75	66.6	66.7	69.6
NZD/GBP	0.548	0.546	0.527	0.512	0.529	0.388
NZD/EUR	0.628	0.63	0.629	0.637	0.633	0.52
NZDCNY	5.21	5.28	5.22	5.08	5.28	4.99
USD/JPY	93.66	93.62	89.29	81.72	79.50	105.7
GBP/USD	1.53	1.55	1.59	1.59	1.59	1.72
EUR/USD	1.33	1.34	1.34	1.28	1.33	1.28
AUD/USD	1.03	1.04	1.06	1.04	1.08	0.788
USD/RMB	6.2379	6.2325	6.2181	6.2326	6.2954	7.56

Kiwi Up and Down

The Kiwi dollar shot upward earlier this week to reach near US 85 cents, 55 pence and 82 Aussie cents on the back of a couple of things. One was the much stronger than expected data on retailing spending during the December quarter released last Friday. The 2.1% rise in spending implies a greater chance of monetary policy being tightened late this year rather than early next year and certainly increases the chances of a move before the March 2014 timing pencilled in by the Reserve Bank.

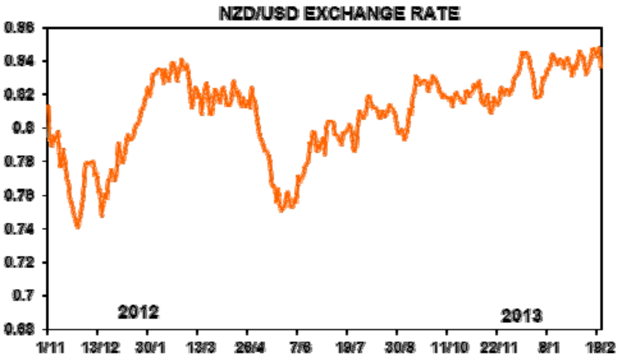
A second factor pushing the NZD up was the 3.2% rise in average prices at Fonterra's fortnightly auction. Prices are now 40% higher than their low point of last year and up 9% so far in 2013. Dairying made up about 27% of all NZ merchandise export receipts during 2012 including casein products. Therefore the markets read rising dairy prices as a good sign for export receipts overall and age-old economic theory says that this means the NZD goes up.

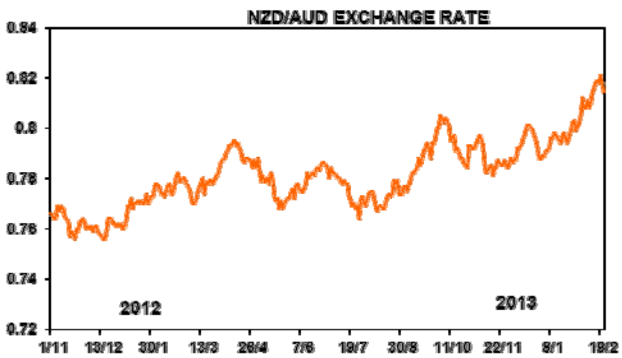
The trouble with this of course is that the same economic models say a persistently large current account deficit will cause one's currency to fall and that does not happen. Also the interest rate parity theory says that a country which averages interest rates above those offshore will see its currency depreciate. But that also does not happen. The NZD has offered a persistent excess yield to investors.

But come Wednesday and then Wednesday night the NZD got hammered down to near US 83.5 cents (still very high) on the back of comments from the Reserve bank Governor. Mr Wheeler said that the RB stands ready to act against a "significantly " overvalued NZD – though they gave direct intervention a go in 2007 at US 76 cents and it ended up at 82 cents nine months later. Intervention can only have a good chance of success if backed up with other policies such as interest rate cuts – and that will not happen given the way the domestic economy in NZ is lifting.

The NZD also got pushed lower last night when the release of minutes from the US Federal Open Market Committee meeting in January showed somewhat less enthusiasm for continuing money printing operations than previously thought.

History suggests to us that the NZD will rise when NZ monetary policy tightens and that process has not even started yet. History also suggests that the NZD will not fall until the housing market goes into reverse. We are years off that happening. Therefore exporters are going to be faced with a persistently high and one must assume rising NZD for the next perhaps three years. Or two. Or four. No-one can put a reliable time-frame around currency movements during the calmest of times let alone the backwash from the biggest global financial crisis since the 1930s.





Key Forecasts

Dec. year		2011	2012	2013	2014
GDP	annual average chg	1.5	2.0-3.0%	2.0 – 2.5	1.0 – 2.0
CPI	on year ago	1.8	0.9	1.0 - 2.0	2.0 – 2.5
Official Cash rate	end year	2.5	2.5	2.5 – 2.75	2.75 – 4.25
Employment	on year ago	1.6	-0.5 – 0.5	1.0 – 2.0	0.5 – 1.5
Unemployment Rate	end year	6.4	7.0 – 7.5	6.0 – 7.0	6.0 – 7.0

The Weekly Overview is written by Tony Alexander, Chief Economist at the Bank of New Zealand. The publication is sent to 27,500 subscribers each week and is one of a stable of regular releases which include the

- monthly Growing With China publication, http://tonyalexander.co.nz/topics/china/
- monthly BNZ Confidence Survey, http://tonyalexander.co.nz/topics/surveys/bnz-confidence-survey/
- monthly BNZ-REINZ Residential Market Survey. http://tonyalexander.co.nz/topics/surveys/bnz-reinz-survey/
- Monthly column for the NZ Property Investor magazine, http://www.propertyinvestor.co.nz/
- Monthly column for the NZ China Trade Association. http://www.nzcta.co.nz/
- Most of these publications plus research into impediments to NZ's economic growth are available on his website. www.tonyalexander.co.nz

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