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.

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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/IFdYSs5FGEq4kAjP95uzTA

Some Observations from London

At the moment I am in London spending my time meeting quite a number of Kiwis over here, giving the occasional presentation, and discussing Europe and the UK with some folk from the Bank of England. In no particular order of importance here are a few observations you might find of interest. I shall write more next week after spending some time in Cyprus.

- Congruent with one of my main themes which is that NZ looks like a shining light to much of the rest of the world, there is increasing interest in investing in New Zealand from Germans with $10 mn lumps. This I learnt from people at the NZ High Commission.
- The high NZD is crimping the profits of food and wine exporters to the UK who cannot raise prices to compensate, especially with much economic weakness and rising unemployment over here.
- Problems in Europe will be around for a long time and there is little expectation that strong economic reforms will be undertaken except in response to crises. Given that drastic reforms are needed the expectation is that these crises will come in a repeating cycle. This will generate volatility in our currency, help keep NZ interest rates low, and make NZ look more and more attractive to an increasing number of people.
- Although some large lumpy redundancies are still occurring in Canary Wharf there is a shortage of good people in the financial sector. Construction in the area is happening so it is certainly not true that the financial sector in London is on its knees. In fact activity is being increasingly underpinned by investors moving their money away from Europe, money coming out of China, and financial services providers themselves shifting out of the likes of Italy. To some extent the UK financial sector is benefitting from the increasing constraints being placed on the sector across the English Channel with expectations that if a financial transactions tax is imposed in Europe there will be a massive shifting of resources to the UK.
- The London property market is strong with many nice areas such as Wimbledon rising firmly (where upon each visit I am treated to a lovely dinner at the Crooked Billet. Thanks again Patrick, Andrew and Peter).
- There is a negative fiscal impulse running through the UK economy of about 1.5% of GDP and this is one factor keeping the economy basically flat. GDP grew 0.3% during the March quarter after falling the same amount in the December quarter.
- The economic outlook for the UK along with that for Europe generally is deteriorating and the data are getting worse. There are expectations that the European Central bank will cut its 0.75% interest rate Thursday night but no-one expects this will make much difference. The barrel is all but scraped clean as far as feasible economic policy stimuli go.

This morning my time I attended a conference put on by Oxford Economics entitled "World & UK Macro, Industry and Regional Outlook Conference". I shall write about it next week.

From the many meetings I have had with expats over there some common questions have been the following.

- Did I think the NZ government would look at restricting foreign investment in New Zealand? No.
- Are commercial property yields in Auckland rising or falling, above or below average? Not my area of speciality, but there was no pre-GFC construction boom so yield pressure is upward and construction will eventually follow. Many investors are interested in commercial property.
- Are residential property yields likely to rise or fall? Fall because prices will rise far more than rents.
- How much of the money to fund the reconstruction of Christchurch is already in the country? Unsure, but whether in the country or not it has already been a factor helping raise the NZD.
- Will a capital gains tax be imposed on residential property and if so what will be its impact? Unlikely unless Labour win an election and the impact would be minimal given existing shortages, low attractiveness of many alternatives in the minds of Kiwis burnt on other assets, and absence of any discernible impact from removal of the ability to claim building depreciation and us of LAQCs.
- Is Wellington still losing public servants and head office people and getting lost in the wash in a general focus on Auckland and Christchurch? Yes, but the design, screen, fashion, etc. sectors are growing strongly and Wellington offers the best inner city living and character of any city in NZ still. Christchurch might challenge that in ten years as long as the inner city does not end up too sterile.
- Will incentives be introduced to attract Kiwis back to NZ? Zero chance. Those in NZ would never support it or see merit in it and the issue is really one of poor business utilisation of expats already returning rather than absence of returnees. Besides, the net average migration inflow for NZ averages over 10,000 per annum anyway so there is no brain drain as such, just a brain swap.
- How should an expat best prepare for their return to NZ? Maintain and build up contacts back in NZ, work that network aiming to get a job organised before returning. The best jobs usually are not advertised. Don't show up in the country one day expecting jobs to be thrown at you.

Of course most of the expats I meet ask about the exchange rate and house prices – at which point I do what I do whenever I speak about housing back in New Zealand, especially in Auckland – I say I told you so. The NZD/GBP exchange rate has now moved into a range (almost today) of 55 – 60 pence and will slowly oscillate from the 55 end toward the 60 end. Plus house prices have risen strongly because of a shortage – though I do not claim at all to have picked the extent of house price rises or the timing, only the fundamental of a shortage and how that would massively limit price declines back in 2008 – 09.

You should see their poor little faces.

Coronation Street and Tax Rates

I felt like I was on location with Coro characters Wednesday morning when taking some time off for shopping at Europe's biggest shopping mall at Stratford. On the train going there from Canary Wharf there sat down behind me a woman who started talking loudly – really loudly – on the cell phone in a deep accent about how she was off to buy a towel. Then some of her friends got on and they started gabbing like my aunties when they get together. They moaned about the job centre calling trying to offer them jobs and how one had arthritis and the offer had been in intensive therapy for 18 months. The first one then said she was planning her annual holiday to Turkey and how she gave the job centre her mobile number but said she had no home phone so they wouldn't bother her there. Good luck with your benefit reforms Mr Osborne.

Speaking of benefits, the gains to Kiwis of going to London to work may not be as great as you have traditionally thought. First, consider the tax rates. These are the personal income tax rates.

£0 – £32k	20%
£32k -£150k	40%
£150k +	45%

Most people are eligible for the first £10,000 tax free.

But, on top of that you pay National Insurance Contributions as follows.

0 - £149 pw	0%
£149 - £797 pw	12%
£797 +	2%

These are fairly shocking rates. But it gets worse. As of a year or two ago the visa rules for Kiwis in the UK were changed. Whereas before we could hop over and work for five years now most people will only be able to work for two years under the Youth Mobility Visa for those under 31 years of age. The Highly Skilled Visa offering five years is available but you fairly much have to be a brain surgeon – that is, in a profession in which skills are high and supply is low.

You can come in being sponsored by your firm. But that is a relatively drawn out process. Apparently the visa admin fee is also close to £2,000.

What it means is that unless you have an EU passport (I could get one but can't be bothered) you need to be thinking very much in terms of just a two year OE in the UK and make a choice between having as much fun as you can in a once in a life-time opportunity – lots of travel etc. – or paying off student debt and building up a good house deposit. Personally were I to start afresh I'd probably see as much of Europe as I could, enjoy myself, then do what more and more Kiwi expats are now doing when their two years are up – move to Australia. Then maybe later I'd think about NZ.

Cheap Paris Hotels

In one's life there are many firsts – first steps, first use of the big toilet, first time out of the car seat, first kiss, first job, first marriage. In Paris I experienced a first. Having stayed in motels and hotels from London to New York, Boston, Chicago, Bruges, Dublin, Seoul, Hong Kong, Invercargill and Coober Pedy, for the first time in my life in Paris I stayed in a hotel without any ironing facilities. No board. Pas de repasseur monsieur. Mais vous pouvez en acheter un prez d'ici. (No iron sir but you can buy one nearby.)

The irony (that's ironic too – and that) is that only the day before in Bruges I'd been thinking of my earliest days on the road in the late-80s packing a travel iron.

I didn't dwell on it long however as upon walking just along the road from my hotel just north of the Madeleine I came across two things. One was a laundry offering ironing services. The other was a café which gave me the first decent coffee I have had since the one at my favourite café Groundup just north of Wellington the previous Friday morning. I think I started singing. Actually I felt like Gollum at the end of Return of the King as he danced with his precious and happily clasped it into engulfment of the lava. Best scene in all four movies.

I mention that ecstatic moment because on the two legs of the plane trip from Auckland to the Heathrow hell-hole I watched all four Lord of the Rings movies. Good – but unlike science fiction such as 2001: A Space Odyssey, or any of the Star Trek franchise episodes, no chance of ever being real therefore less awe inspiring.

You know what you don't see in Paris or any other European city one might visit as a tourist? The hopelessness of the young generation left in the gutter as the continuing effects of the global financial crisis mingle with fiscal mismanagement over an extended period of time, rigid labour markets, and something else I can't find the words for. It's something involving regulatory protection of the older generation as compensation for the horrors of WW2 extending into the generation after them, and an underlying socialist inability to recognise that success and growth (business, economic, personal) come from managing and responding to change – not resisting it.

Responsiveness to change is one of the key factors I emphasise when time permits me to deliver a talk focussed on implications of economic trends rather than lucid enunciation of the trends themselves – the bread and butter presentation. These days I try to almost reverse the order of my presentation toward emphasising seven key trends businesses need to adjust for. You'll need to attend one of my talks to find out what they are.

But back to European youth. Unemployment rates for young people (those under 25 years of age) in Europe are appalling. The Eurozone average is 24%, Greece 58%, Spain 56%, Portugal and Italy 38%, Ireland 31%, France 26%. The UK rate is 21%. The NZ rate using the same definition is 19%. Only the Netherlands at 10.4% and Germany at 7.7% are better in the Eurozone. If this is what these countries consider success to look like, and if this is what they want as an outcome from joining in a Union, and if this is what they think strong welfare states are supposed to produce – then it is guaranteed the UK will be leaving this lot as soon as they can. I would.

I spent just three days in Paris this visit including a visit to MFAT and NZTE personnel at the NZ Embassy and a first-time visit to the OECD. The latter had just received a delegation from NZ Treasury to discuss the OECD's two yearly review of the NZ economy.

With regard to more general observations – I like visiting the shopping mall Quartre Temps in La Defense area. But it is somewhat disconcerting to see groups of three camouflage-wearing soldiers patrolling with their automatic weapons. One normally doesn't see that in NZ. In fact I am looking forward to getting back to NZ and undertaking shopping without having everyone in the store look at me as though I might be going to steal something – especially the almost always dark coloured men guarding the doors. I have had my bag searched on exiting stores, and upon going in as well which I found strange.

In addition, I have yet to have any shopkeeper in New Zealand undertake a variety of tests to see if the note I just passed them is real or fake. It is easy to see the attraction to people of getting their kids out of the UK or Europe to raise them in a higher trust society. Spending time here you realise that New Zealand really is Godzone.

Vodafone Data Roaming – It Doesn't Always Work

This is a system made available by Vodafone so when you go overseas they send you a text with bundle options and you do a simple text back to avoid paying $10 per megabyte and instead pay something like $1, 50 cents or less depending on the country. It sounds good but the system sometimes does not work. In Australia it went fine. It worked also earlier this year in Hong Kong. But in Singapore no text came through, I called up and they fixed it. In London however it has not worked at all. Not only have no texts come through, the call centre people at Vodafone can't figure out how to activate the system and don't know who to contact to fix it which is bad service. I anticipate no joy in Cyprus either later this week.

So if you are travelling and want to avoid paying high roaming charges, have a look around for other options as back-up.

The Week's Economic Data

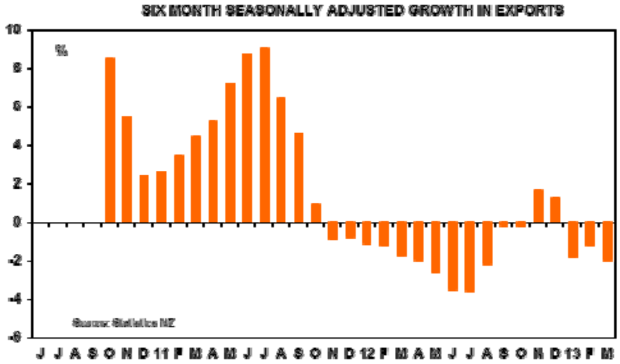
Export Trend Is Downward – Not too surprising considering the high NZD. It will go higher.

During the month of March NZ ran a trade surplus of $718mn which is very good considering last year the balance was $186mn and two years ago $582mn. In fact for the quarter exports were ahead 1% from a year ago while imports were down 4.5%.

We might normally look at that and say that the weak imports result means weakness in the domestic economy – spending by you and I plus business investment basically. And when we look at the value of machinery imports we see growth of only a lowly 1% from a year ago with consumption goods imports also ahead just 1%. Half of the imports decline from last year is actually petroleum and the other half aircraft.

But we discount such a result and do not make such a conclusion because the higher NZD naturally mutes import costs and we know an import surge is coming on the back of the construction upturn and rises in retail spending we can already see underway. So let's look instead at exports and see what the data there are telling us.

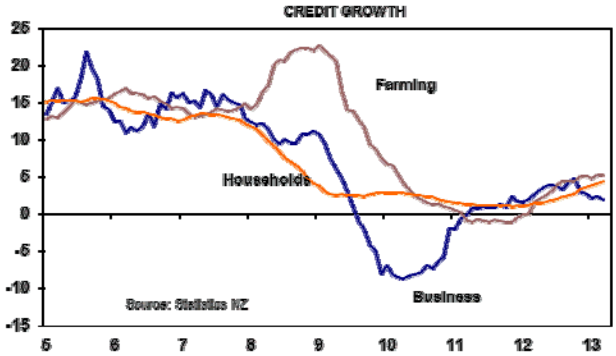
In seasonally adjusted terms exports in the March quarter were ahead 2.3% from the December quarter – but then they fell 4.4% that quarter. So for the past six months seasonally adjusted exports have actually fallen 2% after falling 0.2% in the six months before that and 1.7% in the same six months a year ago. Our underlying export receipts are falling. Import growth lies ahead. The effects of a higher NZD have not been completely felt in terms of higher import substitution and some exporters closing up shop. Plus there is higher NZD to come.



The upshot is a current account deficit headed above the current 5% of GDP toward probably 8% at which point a credit rating cut is likely.

Credit growth isn't accelerating – no debt fuelled bubbles out there

Some people claim that the sharp rises in house prices in Auckland and Christchurch mean those markets are in bubbles. They aren't. All that is happening is that prices are moving to new equilibriums to reflect existing shortages and expectations that the shortages will get worse. Were bubbles underway we would expect to see high debt growth. That is not happening.



In seasonally adjusted terms household debt grew only 0.4% in March and that has been the rate of growth for almost all of the months since July last year. Annual growth is just 4.3% compared with average growth of over 14% per annum between 2003 and 2007.

But it is not just in the household sector that debt growth is low. In the farming sector debt is ahead just 5.2% from a year ago with no apparent acceleration. Business debt is ahead just 1.9% from last year.

House Supply Rising – But not as fast as many would like

Seasonally adjusted dwelling consent numbers fell by 9.1% in March after rising 4.4% in February showing that the upward trend in house building is a quite erratic affair month to month. But the trend nonetheless is upward with consents in the March quarter ahead 3.5% from the December quarter and 12.1% on a year ago. Growth for the full year has been 18.9% but at 17,397 the annual number of consents is still well below the average of 22,000 for the past ten years. Thus the housing shortage worsens still as each month goes by.

In Auckland the popular estimate is that there is a shortage of 20,000 to 30,000 and that consent numbers need to rise to 13,000 per annum for a number of years to solve the problem. I pointed out at a housing affordability seminar in Auckland a month ago that this is highly unlikely to happen as I can find no data showing that Auckland ever had 13,000 consents in a 12 month period. Plus consent issuance has been below the ten year average near 7,500 since the start of 2007. Plus the number in the past year was only 4,764 – which was actually a decrease from the year to February's 4,882.

The upshot? Higher prices which already have risen 38% from late-2008 levels. Plus a deepening housing crisis which people have not focussed on for five years because of their earlier very misplaced belief that house prices in NZ were about to crash from 2008 simply because they "should".

Interest Rates

Nothing suggesting inflation going up soon

Although our monthly business confidence survey has risen quite firmly with not a single mention of the drought (in stark contrast to a month ago) we don't think the Reserve Bank will look at the results and develop greater concern about inflation. New Zealand's inflation rate has been below 1% for a year now and there is no sign in the various vague readings we peruse to suggest that inflationary pressures are picking up.

The NZIER's Quarterly Survey of Business Opinion released a few weeks ago showed that during the March quarter only a net 16% of non-farm businesses expected their costs to go up. This was less than half the net 36% average and the equal lowest result since late-2003. In addition only a net 13% said they expect to put their prices up compared with an average of 24%. This is the second equal lowest reading since early-2009.

The survey results mean we read little into the capacity utilisation rate rising to slightly above average levels at 91.5 in the quarter (average = 90.7%), or difficulties in finding skilled and unskilled employment both moving to about average tightness. In fact we have no evidence at all that wages growth is increasing in the economy though admittedly this is hard to gauge given the paucity of data in New Zealand.

Of relevance also to the inflation outlook is what is happening with the currency and in that regard the pressure remains disinflationary. The NZD continues to creep higher, most notably recently against the Japanese yen and Australian dollar. Note however that the rise against the Yen is unlikely to produce substantially falls in prices for Japanese goods such as cars in New Zealand given that offshore manufacturers of hard to arbitrage items (like cars, not iPads) will tend to price to whatever each market will bear. As the NZD rises against the Yen the manufacturers will pocket the Yen gain, just as when the NZD falls they soak up the Yen loss.

Additionally there is new downward pressure appearing on fuel prices courtesy partly of the higher NZD but partly also the combination of a new slight weakening in global growth prospects and slow factoring in of the multi-generational change in global energy dynamics. One hardly at all these days hears the term OPEC – especially in the context of them exercising market power. They are certainly still hugely relevant, but their power is waning as new drilling techniques and imaging systems open up new vast areas of gas and oil production in other countries.

These developments are set to make the United States the world's biggest oil producer by 2017 and to become energy independent by 2030. Who'd have thunk it?

Now let's allow for rises in building costs as the now newly bigger Christchurch rebuild gets cracking, developers get active in the Auckland commercial and residential market, at the same time as rural construction rises (buildings, milk factories, irrigation schemes). We get a still benign inflation outlook which suggests no change upward in the official cash rate until well into next year – or 2015 given the way European growth prospects are dimming anew at the same time as the United States is again having an early-summer pause with falling business profits questioning the sustainability of higher equity prices. If you are chasing share prices upward then good luck. Global money printing will probably keep asset prices rising for two or three years. But once that printing stops the house of cards could easily fall down again.

This week wholesale interest rates have fallen slightly in response to falling yields offshore on the back of deteriorating economic data. The US ten year government bond yield for instance has fallen to 1.63% from 1.7% a week ago and 1.86% a month ago.

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	2.66%	2.66	2.66	2.67	2.76	5.7
1 year swap	2.75%	2.78	2.77	2.76	2.84	5.8
3 year swap	3.05%	3.09	3.14	300	3.23	6.1
5 year swap	3.33%	3.39	3.48	3.32	3.68	6.3
7 year swap	3.59%	3.67	3.77	3.64	4.06	

Housing Market Update

Nothing new – listing shortage continues, prices rise.

Results from our monthly BNZ Confidence Survey show that conditions remain the same as ever in the residential real estate market. Listings are in short supply, prices are rising, but upward pressure on rents is not that great. This latter dimension reflects the inability of landlords to raise rents in our medium income country where people can afford only so much. In addition with investors purchasing more properties largely for the capital gains they expect to accrue, rent is not the primary consideration. You can read the survey results here.
http://tonyalexander.co.nz/wp-content/uploads/2013/04/BNZ-Survey-Results-April-29-2013.pdf

In this way residential property investors are a bit like farmers. They know that they grow their wealth simply by holding onto the land for as long as humanly possible, and while you wait for yourself to get old and for the land to rise in price you place some interesting animals on the fields to generate a small yield and muck around with their genetics and the trees they might shelter under.

In addition, with regard to Auckland, we have reached the point in the cycle where people leaving Auckland are not selling their properties because they fear they will not be able to buy back in again when they return. So they are renting them out and simply hope to get someone who won't kick the walls in too much or crack too many toilet bowls.

The Hong Kong version of this has been (until recently, the rules have just massively changed) mainlanders buying Hong Kong apartments and leaving them completely empty because being a landlord is not worth the hassle with the yield only 1 – 2%. Singapore has been facing a similar situation. One wonders then if this is what we might see happening in Auckland as we see perhaps more buyers coming in from overseas.

We should all be aware that in New Zealand, much as we view the place as a Garden of Eden remote from the world's troubles, we are not isolated. There is literally trillions of dollars shifting around the planet looking for a safe home with people prepared to accept a lowish yield simply because it is better than near nothing in their home country, carries little risk of confiscation by the government, and is away from their leaders' prying eyes.

New Zealand sticks out not as a tax haven by any means, but as a nice safe place run on the basis of a strong rule of law and openness to foreign investment in all but large companies and sensitive land simply because of a lack of rules outside those particular areas. As noted elsewhere in this Weekly, interest from German investors in New Zealand is growing. And as noted here and in some of my other publications for many months, interest in New Zealand from China is rising.

In that regard increasing concerns about pollution in China will drive more families to send their child to NZ to study and many will buy a house for them to live in.

In a week's time I shall once again run my monthly survey of the country's 10,000+ licensed real estate agents and will include the questions again regarding foreign purchasing. My aim in doing so is threefold.

1. Counter the sprawling anecdotes regarding Chinese buying everything in sight. They are not representative of the true picture.
2. Warn that whatever the level of Chinese buying is now it will grow tremendously in coming years (look at the trade and tourism rates of growth).
3. Encourage debate around introducing restrictions on foreign purchases of NZ residential property in line with Australia's rules.

If I Were A Borrower What Would I Do?

Nothing new. Float, look for fix half 3 -5 years when lenders offer heavily discounted rates, and place some of the floating portion out to 18 months.

Offshore

At the end of the rope

I was there at the conference in Brussels when the European Commission President Mr Barosso essentially said the limit of fiscal austerity has been reached – though I was too busy taking notes from his comments a few minutes before then to realise the significance of his utterance.

I have been travelling to Europe these past three years partly with the aim of trying to identify at what point the Europeans will have no choice other than to sacrifice financial reputation in the interests of holding their societies together. He said
"I know that there are some technocratic advisors who tell us what the perfect model to respond to a situation is, but when we ask how we implement it, they say "That is not my business." We need to have a policy that is right. At the same time we need to have…acceptance, political and social."

That acceptance is not there in Europe any longer. This is evident not in the rioting which breaks out every now and then in the debtor countries, not in the comedian's electoral success in Italy and the comeback of the bunga bunga old guy, not in the votes for the political extremity in Greece, or even the dumping of essentially every party in power during the GFC. Instead the unwilling acceptance of fiscal austerity has been shattered by the new signs of economic weakness showing that despite pain to date no sustained upturn has yet appeared out of the private sector.

In particular there are growing concerns about
- the French economy,
- the narrative of decline which is gaining traction throughout Europe, and
- the decreasing popular support for European cohesiveness itself amongst voters in the EU member countries.

The place is starting to fall apart – even as more countries want in.

Unfortunately, should targets for achieving reduced fiscal deficits be extended, it is a long shot that this will in fact allow growth to resume. This is because all that easier monetary and fiscal policies can do is buy time for the private sector to get its house in order and return to normal spending, hiring, and investment patterns with an initial cyclical catch-up period of rapidly accelerating growth.

But ECB money printing and low interest rates have not worked and easy monetary policy has a far quicker impact on economic activity than easy fiscal policy. Easing off of the pace of fiscal austerity will sell well with the European electorate. But unless the extra time bought does lead to private sector normality things will be even worse in two years' time with investors even less enamoured of holding European government debt.

In other words – if the Europeans ease off their pace of fiscal austerity we will likely see extra upward pressure on asset prices based on optimism for growth. But like the money printing of the Japanese it will be a gamble that may not pay off, and if it doesn't Europe will sink into Japan's pattern for the past two decades. This will be especially the case if the time bought is not used to deregulate and reform European labour, goods and services markets. The chances are these deregulatory moves will not happen – after all they did not in Japan and leaders in Europe are decreasingly telling a story of the need for radical change. The Irish President just this week moaned about Europe's "hegemonic" economic model and the risk of a loss of popular legitimacy amidst social upheaval.

Do I despair then for Europe? Not for the EU overall or individual countries. It is a high wealth and high income part of the world. But I do for the ever-enlarging lost generation of youth, and I despair for what that will mean in 5 – 10 years' time in terms of social and electoral outcomes.

Now place that view alongside the resurrection of the United States on the back of more successful management of the effects of the GFC, better economic structures, and newly cheap energy. Now consider the rise of Asian economies. New Zealand's interests and yours from a long term market and product development point of view need to be moving toward those two latter parts of the world – their consumers and their businesses.

But keep an eye on Japan's economy. The new Prime Minister is said to have a three arrows approach to improving things – easier monetary and fiscal policies, plus economic reform including joining the Trans-Pacific Partnership negotiations. But with an aging electorate hefty economic reform is unlikely, opening up agriculture is extremely unlikely, debt is already a massive house of (domestic) cards waiting to collapse, and monetary policy can't work if banks won't lend and people won't borrow. Therefore the Japanese PM may already be developing another policy in the interests of societal cohesiveness (something not happening in Europe) – popular resistance to Japan's ages-old enemy of China. Nationalism sells well during economically tough times.

Our back yard in other words which we feel so clever about having in the context of Europe declining, is moving toward a fragile geo-political and military condition which will place us in a difficult position with regard to balancing interests in the next few years. End of history Mr Fukiyama? – Only one chapter of it.

In Japan the core inflation rate came in lower than expected in March at -0.5% illustrating just how far the Bank of Japan has to go in order to get to 2% inflation – something they expect either late in 2015 or in 2016. Good luck.

In the United States this week things got off to a weakish start with the durable goods number for March coming in lower than expected. Total orders fell 5.7% in March after rising 4.3% in February giving growth of only 1.2% on a year ago. This becomes an even weaker annual change of only 0.2% if one focusses on the core measure which excludes the defence sector and aircraft. Following that we learnt on Friday that the US economy grew at an annualised pace of 2.5% in the March quarter. This is a gain from just 0.4% in the December quarter and a silly person might say this represents an acceleration and everything is rosy. Actually, much of the March quarter rise was a simple bounce back from the previous quarter. Also since

WW2 growth in the US GDP has averaged 3.2% per annum but since 2009 the average has been just 2.1% which is nowhere near enough to make a dent in the growing ranks of the under-employed.

On top of that for the next two quarters analysts expect annualised growth rates from 1% - 1.5% as the effects of the sequester wend their way through the economy.

The upshot then? It is way too early to be talking about the Federal Reserve ending its extraordinary stimulatory measures and that means continued low NZ interest rates as our currency rises higher against a USD being devalued through massive liquidity injections. In fact just last night the Fed. Added that there was scope for increasing their monthly $85bn asset buying programme.

In Australia, although the housing market is rising, despondency is also growing with regard to forecasts of ongoing fiscal deficits resulting from an accepted failure of both Coalition and Labour governments to effectively bank the benefits of the China-driven resources boom for the long term rather than having a short-term sugar high. A lot of worry coalesces around the likes of these numbers. On average investment in the resources sector has accounted for 2% of GDP in Australia but recently the contribution has been 8%. With the investment boom passing (though not collapsing given the pipeline), growth worries are increasing.

Now add in decreasing political support for continuing to artificially support the motor vehicle sector, expectations of commodity prices falling as China's growth becomes less driven by infrastructure development.

Implications? The rise in the number of people returning to New Zealand from Australia is likely to continue. The gross flow back in the year to March was 15,755 compared with 13,781 a year ago. The gross outflow to Australia has also eased to 51,273 from 53,237. That makes for a near 4,000 reduction in the net loss in the past year to 35,518. Shocking, but less shocking. Stimulatory for retailing and the housing market.

Exchange Rates

Exchange Rates	This Week	Week ago	4 wks ago	3 Mths ago	Yr ago	10 yr average
NZD/USD	0.848	0.847	0.837	0.846	0.814	0.67
NZD/AUD	0.829	0.824	0.803	0.812	0.788	0.85
NZD/JPY	82.4	84	78.2	76.9	65.3	69.6
NZD/GBP	0.546	0.554	0.55	0.539	0.502	0.388
NZD/EUR	0.644	0.65	0.652	0.621	0.615	0.52
NZDCNY	5.23	5.23	5.20	5.27	5.11	4.99
USD/JPY	97.17	99.17	93.43	90.90	80.22	105.7
GBP/USD	1.55	1.53	1.52	1.57	1.62	1.72
EUR/USD	1.32	1.30	1.28	1.36	1.32	1.28
AUD/USD	1.02	1.03	1.04	1.04	1.03	0.788
USD/RMB	6.1658	6.1781	6.2083	6.229	6.2824	7.56

NZD peak lies where? Impossible to say, but…

The Federal Reserve in the United States is determined to get growth self-sustaining with rising consumer spending and business investment. The business investment leg suffered a crick this week with weaker than expected durable goods data. That just reinforces the Fed.'s determination to keep monetary policy easing. The household spending side is mixed with housing activity improving, most notably with regard to prices, but house construction also rising. With retail spending things are not as strong as hoped. Throw in a recent small set-back in the rising asset prices which the Fed. is also targeting (share prices) and again their money printing determination will remain.

What do we take from that? Mainly that risks for the NZD/USD exchange rate continue to lie on the upside and I can see a rate of 90 cents at some stage – at which point if I were a currency trader with a view extending longer than a year I would sell NZDs. Why?

Because the world is changing and much as one's initial thought upon reading that is that this refers to Asia – that is only half the story. The other half involves the United States being projected to be the world's biggest oil producer come 2017, and gas prices falling almost three-quarters from where they were just five years ago. The world which you grew up with involving OPEC having us all by the throat is ending. This is very important.

First it means that whereas our previous running assumption was that fuel prices would keep rising, that may not necessarily be the case. Increasingly I am happy about my Mustang purchase two years ago. Should have bought the Shelby – but seriously, 500 hp!

Second, with European energy prices however rising because of decisions made to close down nuclear electricity generation, coupled with cheap US energy, the world's energy-intensive industrial sector is shifting investment into the United States. Even from China. That investment will eventually be accompanied by industries which feed off of those chemical, petro-chemical, high energy manufacturing industries etc.

Third, it means not just an extra positive for the US economy, it also changes the nature of the US currency so it is not just a safe haven but a petro-currency also.

Now let's throw in some more factors. Medium to long-term prospects for Europe do not look good and companies are already looking at locating new investment elsewhere – in the US and Asia. This will keep the Euro depressed especially as the easing off in the pace of fiscal austerity means deteriorating government financials and more credit rating cuts.

Also, while Asia is growing strongly in an economic sense, it is also becoming more militarily risky. Shocks for Asia associated with armed conflicts are rising. That will eventually start to be factored more and more into Asian currencies and emphasise the relative safety to multi-national firms of investing in the United States rather than Asia.

Also, Japan's experiment in printing money to boost growth may not work given the shrinking population, huge domestic debt, and inherent resistance to change not forced upon them by surrender or cannonballs. That means a weakening Yen beyond that which has already happened. Related to that, given the economic pressures developing in the more advanced Asian countries as a result of the Yen's fall boosting Japanese manufacturing competitiveness, efforts to depress those other Asian currencies are likely. De facto that also implies a stronger greenback.

Now let's look back at the US economy again and add in the economic boost which people are increasingly thinking may come as a result of legitimising the residency status of up to 11 million illegal immigrants. Plus let's throw in robotics increasing US manufacturing competitiveness, decreasing Chinese manufacturing competitiveness, and 3D printing.

Taken in conjunction with the creative destructionalism model which works well in the United States but is not allowed to function in Europe and you get a steadily brightening long term outlook for the USA. That will eventually manifest itself in a much stronger US dollar – though probably not just yet given the dollar printing and outlook for sustained low interest rates. It is also going to take some time for investors to wake up to the massive geo-political implications of America's change in energy status.

This means that at some point the USD will be a screaming buy against a clearly over-valued NZD which one day will correct downward. When will that downward correction come? There is zero way of forecasting that so don't pay any attention to anyone who gives you a time-frame for it. They're dreaming. But a trigger may be something bad involving a shock to China's economy leading to sharp falls in currencies of countries highly dependent upon the Chinese market for their primary exports – New Zealand and Australia.

The world which you grew up with is changing. China's rise, Europe's ineffectual economic model being revealed as financing chooks come home to roost, and a new rising of the US economy. To what extent have you given thought to these things in your strategic planning?

Oh – and blah blah, the Kiwi dollar went down a bit during the week for reasons you can easily find looking at one of the many daily FX commentaries available out there.

Discussion

In this section I shall include noteworthy comments made by emailers. Some weeks nothing will be here. No names will be printed.

Building Costs

A 140 m2 house with no garage can be bought for $161,768 before carpet , drapes and driveways etc.(incl gst) . Auckland Council now quotes a total of $38,000 for their fees – 24% of the actual cost to build the house! This was for a infill house with all infrastructure in place (New Lynn). The "Supercity" has now managed to move average local body fees for West and Central Auckland from around $11,500 in 2007, to $38,245 in 2013 (incl gst) Manukau city often had around an extra $20k fee to deal with lack of storm water infrastructure in certain areas. The only mitigating factor is that it also includes a previously excluded reserve contribution of around $10,000 a section. At any rate the increase in fees is still well over 50%. Unfortunately this looks set to continue as Water care has now moved connection fees from $500 to $6810 in the last 4 years and now have signed a lease on a new flash office block at one of the highest market rents (m2 rate) I have heard off. These "added" fees are not just restricted to Auckland as a building consent from a Bay of plenty council last week had a $1000 levy on the BC bill, which I was told it was a new fee for helping train staff on building consents.

EU Federalism
To understand the differences between USA and Australia vs. EU - you have to understand that both USA / AUS have had their "Federal" gov structure more or less side by side with the local development of their states e.g. they grew along with each other. Compare that with 1000 or even 3000 years of "local" identity / sovereign living in EU and last 10 years a "federal" state over the top. It would take 3-5 Generations of people (or 100-200 years) and lots of goodwill to be moderately successful at establishing a good working federal system. Then and only then will we see a powerful modern economic block from Europe.

Migration to NZ
Feedback from new clients today, a young married rather hip couple working in visual effects – just returned from UK as day rates all dropped over there because of the financial crisis, and at the same time the cost of living rose sharply. Tax rates for high earners increased in London and so the work stopped coming there. Instead of the work going to big companies in London, clients are now seeking out small flexible couples/companies to take the work directly to – no middleman and no dividends required by shareholders, just taking work directly to the creatives. And these creative are leaving London and moving to countries that are known to be developing these industries and have better lifestyle opportunities and lower taxes – Canada, they said, and New Zealand (i.e., Weta Workshops he said. Though many of these high earning visual effects people that I act for deal directly with clients in various countries, and don't work indirectly or directly through Weta at all) They said even though our high dollar means working from NZ for international clients isn't the fabulous money doubler or tripler it used to be, the rates are still very good compared to what they could earn in London….and the traffic's not nearly as bad – (though all the Aucklanders seem to complain about it no end at the moment!)

And the second new client today works in landscape design via computer – has a nearly full time job in New Zealand, and also nearly full time work from the UK – gets sent the work each day and sends it back each night – has been doing this for three or four years, with day rates gradually being increased as the dollar rises to compensate – the UK fellow likes his work and wants to keep him

Key Forecasts

Dec. year		**2011**	**2012**	**2013**	**2014**
GDP	annual average chg	1.5	2.0-3.0%	2.5 – 3.0	3.0 – 3.5
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	1.0	1.0 – 2.0	1.5 – 2.0
Unemployment Rate	end year	6.4	6.5 – 7.0	6.0 – 7.0	5.5 – 6.0

The Weekly Overview is written by Tony Alexander, Chief Economist at the Bank of New Zealand. The publication is sent to 28,000 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 Brain Gain NZ publication http://tonyalexander.co.nz/topics/brain-gain-nz/
- 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/
- Most of these publications plus research into impediments to NZ's economic growth are available on his website. www.tonyalexander.co.nz

Tony Alexander has been Chief Economist at the BNZ since 1994 and apart from publications and advising management spends considerable time on the road around New Zealand making presentations and speaking with the media. He travels to the UK and Europe twice a year to assess economic conditions and present at numerous functions, has five children, tramps, and his partner Dr Sarah Farquhar runs the early childhood education network www.childforum.com

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