Weekly Overview

5 September 2013

ISSN 2253-3672

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/lFdYSs5FGEq4kAjP95uzTA

Themes

There are a number of themes which we have peppering throughout the Weekly Overview and other publications over the past 2 – 4 years and here is a summary of some of them.

- There is a housing shortage concentrated in Auckland which will cause prices to rise and keep on rising with those rises slowly spreading to the rest of the country.
- There will be a shortage of builders revealed once construction picks up and this will accelerate the spread of Auckland price rises to the rest of the country while being a leading factor in pushing inflation up and eventually interest rates.
- There will be a resurgence of inner-city apartment construction in Auckland as young buyers seek more affordable homes close to where they work and they will find finance provided by the developers.
- At the start of each monetary policy tightening cycle the strong tendency is to under-estimate both the duration of the tightening period and the height to which floating interest rates must generally be pushed to contain our borrowing and spending drive.
- The Kiwi dollar rises when NZ monetary policy gets tightened and as this process has not even started yet exporters should prepare for NZD rises beyond already high levels.
- Predictability of interest rates and exchange rates is low and will remain low for many years because of massive uncertainty regarding developments overseas. These include monetary policy loosening then tightening periods in the world's biggest economies, China's transition from super-fast growth to something less stellar, Europe's grappling with issues of debt and economic rigidities.
- The migration cycle with Australia principally will turn (has turned) and while this will provide some extra employees the main effect will be to swamp any effect of measures introduced to stem housing market rises and cause extra rises in house prices.
- Employers need to (needed to, it's almost too late now) take advantage of the period of weakness in the economy and labour market to source or arrange to eventually source people from offshore through an HR company which they can work with.
- New Zealand will shift to a relationship of economic dependence upon China and managing this relationship will require a lot more knowledge about China on the part of all Kiwis.

Let's now introduce some new themes.

- Volatility in financial asset prices, fiscal constraints on the government at a time of an aging population (pension and health costs), plus house prices getting quite stretched mean the need for people to save is rising and the risks of high concentration of one's savings in one or two assets or asset classes is growing. Save more, diversify more, or at least sacrifice some yield for safer investments.
- People will put off retirement so employers will be presented with an opportunity to offset shortages of younger people by retaining and hiring older people. But to effectively utilise this resource companies will need to consider alterations to employment relationships.

- The demand for protein coming out of China and other emerging economies will spread from dairy products to meat and generate fresh investment in New Zealand's sheep, beef, and deer sectors.

One could write more but that is enough for now as the housing section below is quite long this week.

China Worries

The interesting result from our monthly BNZ Confidence Survey released on Monday was not that confidence about the economy remained at a near record high for the fourth month in a row, but that relaxed feelings about our economic relationship with China have diminished. Whereas in the previous three months a net 44% exactly each month said they feel relaxed about our economic relationship with China, this month that fell to a net 28%. That is still a strong result but the decline shows that people are aware of the importance of our dairy trade with China and its high vulnerability to the corporate practices of companies involved and food checking and reporting regimes.

BNZ-Nine Rewards Consumer Trends Survey

Tomorrow morning we shall release the results of our latest monthly survey showing how consumers feel about the economy, whether they intend spending more or less than usual, how they perceive the labour market, views on the housing market, and attitudes toward making purchases of cars, clothing, furniture etc.

IF I WERE A BORROWER WHAT WOULD I DO?

Rates are rising and we are doing our best to guess not so much when and at what level they peak but when the monetary policy tightening cycle starts (floating rates rising), and how rapidly fixed rates get driven up by developments in the United States in particular. Uncertainty is very high and borrowers should not at all base their interest rate fixing decisions on a particular set of forecasts coming true. No-one has a good record of forecasting interest rates over the past half a decade at least and nothing has magically changed so that our forecasting ability has suddenly improved.

Borrowers should recognise that rates are on an upward path of uncertain speed and shift into a risk-diversifying spread of long term fixed rates as their circumstances allow.

This week the three year swap rate has risen to 4% on the back largely or rising rates in the United States on the back of firm economic data. This is the highest rate since mid-2011. The implications for bank lending rates are fairly clear.

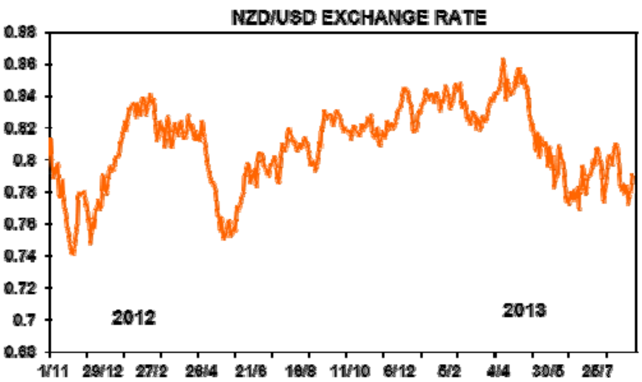
FINANCIAL MARKETS DATA

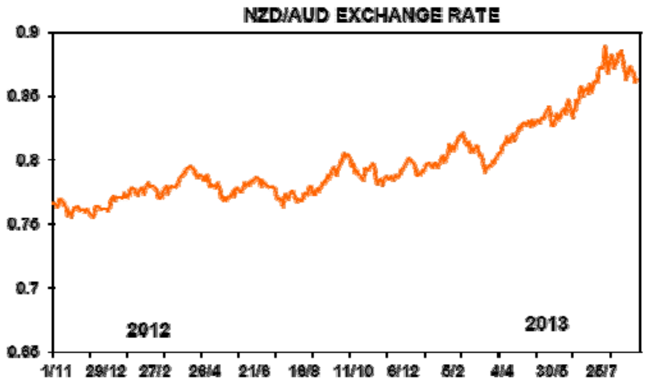
	This week	Week ago	4 wks ago	3 months ago	Yr ago	10 yr average
Official Cash Rate	2.50%	2.50	2.50	2.50	2.50	5.4
90-day bank bill	2.67%	2.67	2.66	2.67	2.76	5.7
1 year swap	3.01%	2.93	2.97	2.78	2.61	5.8
3 year swap	4.00%	3.87	3.77	3.23	2.82	6.1
5 year swap	4.58%	4.39	4.23	3.57	3.13	6.3
7 year swap	4.90%	4.71	4.50	3.85	3.44	

NZD Recovers Against Some

The NZD has risen almost one cent against the USD this past week and gained also against the Japanese Yen and Euro while shedding a cent against the Aussie dollar. The rise against the greenback mainly reflects some positive US economic data causing investors to seek out higher yielding riskier assets such as shares and peripheral currencies. The fall against the AUD mainly reflects the absence of a fresh signal from the RBA that they will cut interest rates again.

Exchange Rates	This Week	Week ago	4 wks ago	3 Mths ago	Yr ago	10 yr average
NZD/USD	0.791	0.784	0.774	0.8	0.793	0.67
NZD/AUD	0.863	0.873	0.868	0.83	0.775	0.85
NZD/JPY	78.8	76.6	76.6	80	62.2	69.6
NZD/GBP	0.506	0.505	0.506	0.523	0.5	0.388
NZD/EUR	0.599	0.589	0.583	0.611	0.631	0.52
NZDCNY	4.84	4.80	4.74	4.90	5.04	4.99
USD/JPY	99.62	97.70	98.97	100.00	78.44	105.7
GBP/USD	1.56	1.55	1.53	1.53	1.59	1.72
EUR/USD	1.32	1.33	1.33	1.31	1.26	1.28
AUD/USD	0.92	0.90	0.89	0.96	1.02	0.788
USD/RMB	6.119	6.1198	6.1298	6.1287	6.3507	7.56

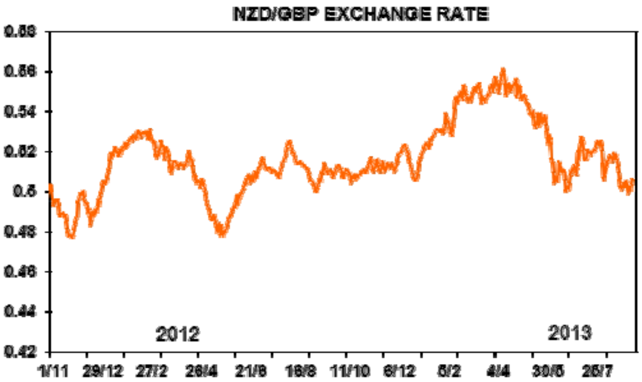


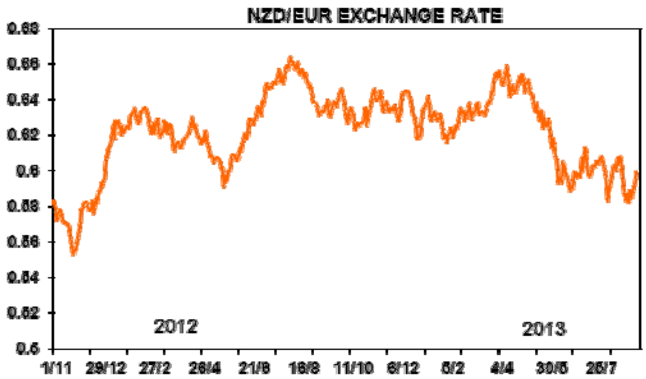


In the US data have been generally good. There was a strong upward revision to growth in GDP during the June quarter from 1.7% to 2.5%.

This Friday night the monthly employment report in the United States will be released and it always has capacity to surprise. If it comes in with jobs growth stronger than forecasts then expectations will rise of Fed. tapering starting this month and proceeding rapidly. This will place upward pressure on interest rates in the United States and in New Zealand while pushing the USD up and the NZD/USD exchange rate lower. But if the report is weak the opposite will happen.

In the United Kingdom the current economic story is one of data turning out to be better than expected with strength in housing and retailing revealed recently plus some good manufacturing data. These developments are giving the Pound some support.



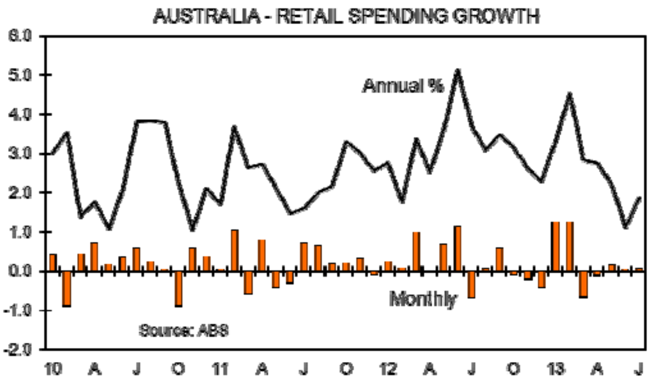


In Australia people go to the polls this week in a Federal general election with the outcome near certain to be wholesale dumping of the Kevin Rudd-led Labour government and voting in of a Liberal-National coalition led by Tony Abbott. The potentially large swing away from Labour will be due to weakness in the economy with rising unemployment following the ending of the resources boom, failure of the government to control its spending growth during the boom leaving a gaping fiscal hole which may stretch for the next decade, widespread failures of some key large spending programmes such as home insulation and the national broadband rollout, failure to stem the flood of boat-people and in fact changing policies so that numbers rose, and massive fractures within the Australian Labour Party involving respective dumpings of Kevin Rudd then Julia Gillard by each other in the past three years.

There are few expectations that the incoming government will radically alter the economy and there is literally nothing they can do to reverse the decline in resource sector investment as a proportion of GDP from 8% back to the more normal 2%. Confirmation of a new government could lift the AUD but the worsened fiscal track expected to result from a lavish spending promise on paid maternity leave will tend to cap any gain.

The AUD actually climbed against the USD (two cents) and NZD (one cent) this week assisted by some better than expected data on house construction. Dwelling approvals jumped 11.3% in July wiping out declines recorded in the previous two months. Consents issued for the three months to July were up only 1.2% from a year ago but at 157,653 annual consent numbers were up 8.4% from a year earlier. So house construction is rising in Australia though not at an accelerating pace. That may change however with interest rates at newly multi-decade lows. Speaking of which, on Tuesday the RBA reviewed their cash rate and left it unchanged at the record low of 2.5%. Their failure to meet market expectations of a hint that more easing might occur was another factor delivering some strength in the AUD this week and the weakness in the NZD against the Aussie dollar compared with a week ago.

Retail spending in Australia rose only 0.1% seasonally adjusted in July and has fallen 0.1% over the past three months. So consumers are not exactly opening their wallets and this will reflect the depressing effect on spending willingness of rising unemployment as the resource boom ends and jitters about China grow while other sectors have yet to take up the growth strain.



Speaking of China, during the weekend data were released showing the official manufacturing sector Purchasing Managers Index rising to a better than expected reading in August of 50.1 from a recessionary 47.7 in July. This jump aided the Aussie dollar's rise during the week as investing in the AUD is seen internationally as a proxy for taking a view on China given that some 35% of Australia's exports go to China.

In Japan there are increasing signs of stirrings in the economy with the annual level of housing starts this year heading to its highest level in five years, apartment prices creeping up, and more and more people locking in the likes of ten year fixed mortgage rates at 1.7%. People have been holding off buying for many years because of expectations that apartment prices would either stay flat or decline further. Main city land prices have fallen 80% since 1990.

Now those expectations are changing and that is one of the main aims of the strong monetary policy loosening being overseen by the Bank of Japan – to raise people's inflation expectations and therefore spending willingness. Here's hoping the policy works because if it doesn't and the Japanese economy remains weak the government will not be able to raise the consumption tax in two steps from 5% to 10% starting next year and the already yawning deficit and ballooning public debt will simply get worse.

In Europe there was some happiness this week following news that the number of unemployed people in the Eurozone fell by 15,000 in July. But the unemployment rate remains at 12.1% (5.3% in Germany, 27.6% in Greece) and most analysts still talk in terms of economic shrinkage ending rather than good growth appearing. Inflation has declined to 1.3% in August from 1.6% in July so little stands in the way of the ECB keeping its cash rate unchanged at 0.5% for a long period of time.

In fact the general expectation is that interest rates in the UK, Eurozone and US will not be raised until 2015 – 16. But before then rates will be increased here in New Zealand as our growth rate lifts toward and maybe above 4%. Hence our expectation of renewed NZD appreciation against the Pound, Euro and USD in the coming year.

Housing Market Update

Builder Shortage

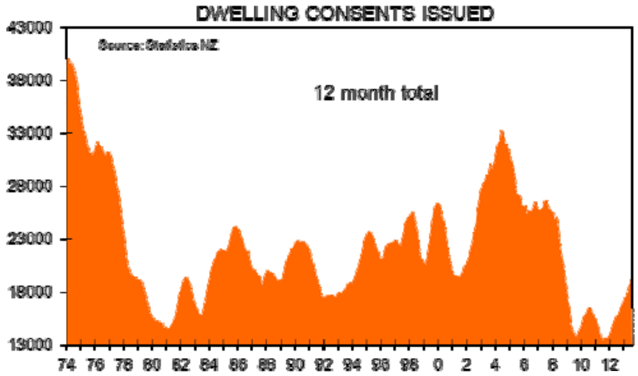
Here is growing evidence of a key factor which we have warned for the past 3 – 4 years will extent the period during which there is a housing shortage in Auckland. A shortage of builders.
http://www.stuff.co.nz/dominion-post/news/9104579/Rebuild-strips-Wellington-of-tradesmen

One factor behind the shortage of builders is the requirement for registration which came in from the start of last year. Another issue is the increasing complexity of certification. But the biggest problem may be the after-effects of the water-tightness problems last decade which have caused a change in legislation such that builders remain personally liable for any problems for a period of ten years I understand.

Add in the loss of tradespeople across the ditch plus the low levels of training during the past few years when building activity has been at low levels and you get a situation where it does not matter how much land the councils free up – the pace of house construction is not going to be greatly lifted unless we open the floodgates to builders from offshore. That is not something Kiwis are generally in favour of.

The shortage of houses therefore continues and will spread from Auckland and Christchurch slowly to other parts of the country as normal construction is retarded by the loss of builders to our two biggest cities.

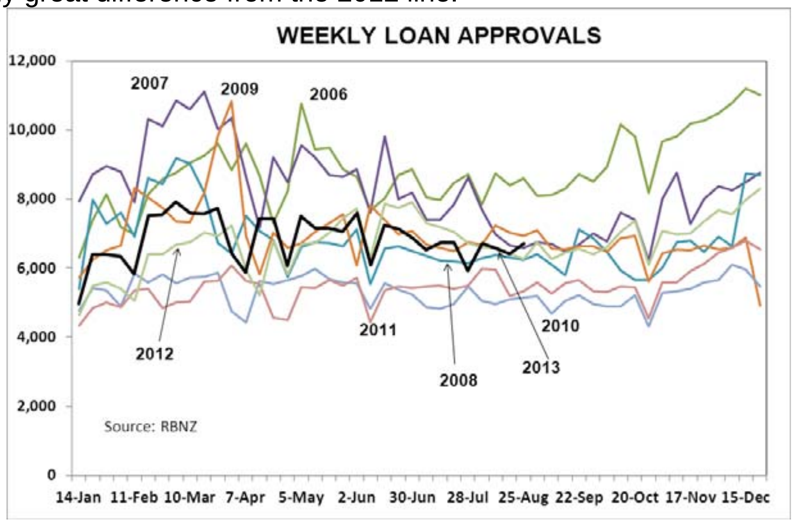
Speaking of slow construction growth, in July the seasonally adjusted number of dwelling consents issued fell by 0.8% after declining 4.3% in June. But these numbers can be quite volatile and it is best to smooth them. Doing this we see that in the past year consent numbers have risen to 19,146 from 15,722 a year earlier, and that in the three months to July consents were ahead 6.5% from the three months to April. The trend is upward but it is not stellar. At this rate the average number of consents issued each year for the past decade of 21,737 will be reached early next year.



Lending to the household sector is not soaring.

In July household debt was just 5.2% ahead of a year earlier and on a monthly basis growth has been 0.4% seasonally adjusted in June and July and on average for the past 12 months. So growth is not accelerating. House prices have been driven upward not by a lending splurge but by simple market repricing of a thing in short supply.

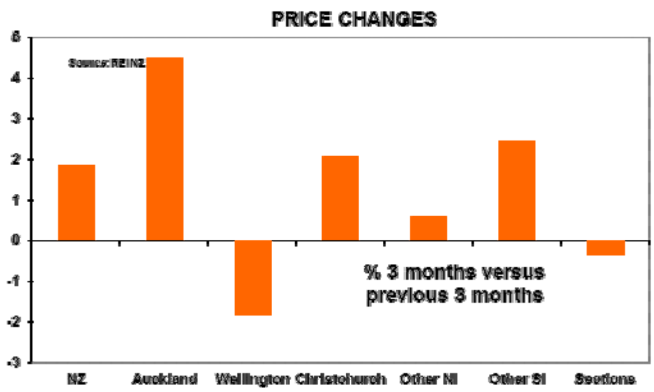
There is also no lending surge or splurge indicated in the weekly home loan approvals series. The black line in the graph here shows weekly loans during 2013 and the point to note is the absence of an upward trend and the absence of any great difference from the 2012 line.

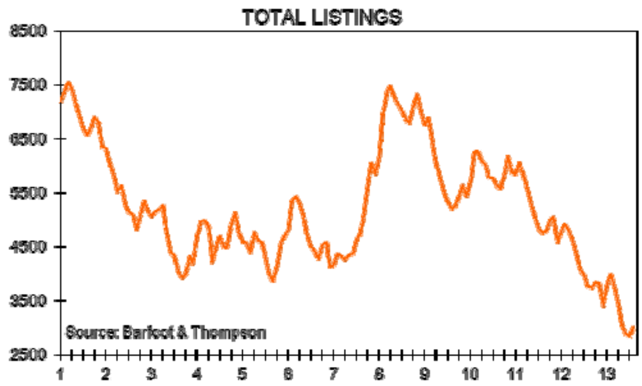


Auckland Plateauing?

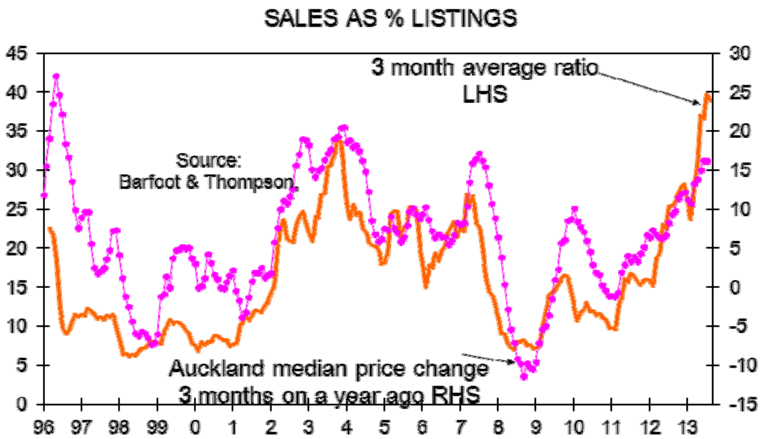
Barfoot and Thompson real estate agency account for about one-third of the Auckland residential real estate market and their data released this week for August show sales in the month ahead 18% from a year earlier. Their average selling price was $648,000 which was 9.5% ahead of a year earlier but almost the same as five months earlier in March. Have prices plateaued?

A better measure is contained in the REINZ's stratified house price index which at the moment runs just to July. August data will appear shortly. It shows a median price in July of $606,000 compared with $600,000 in March and ahead 13.9% from a year earlier. The following graph shows price changes in the three months to July compared with the three months to April. In Auckland prices rose 4.5% and while this pace probably won't be sustained it is likely to be closer to the speed for the rest of the year than zero implied by the Barfoot and Thompson data.





What about listings supply? The B&T data show that while the number of new listings received in August was ahead 20.7% from a year ago at 1,710, the stock of listings at 2,999 was down 20.6% from a year earlier. But given that the stock usually (not always) declines between July and August and this year rose by 162 units one can run the case that there has been some very mild alleviation of the shortage. The second graph above shows that this change does not really count for much however and the third graph shows why we believe prices will continue to rise.



BNZ Confidence Survey

For those who may have missed them, here are the comments in our BNZ Confidence Survey released Monday morning showing conditions in the residential real estate sector.

- Real Estate----Bright
- Real Estate: its busy, winter has been mild and people have continued to be active in the market. We are starting to see the beginnings of our usual spring listings uplift so there will soon be more options for buyers. Perhaps fear, lack of understand, a little bit of panic about the upcoming changes to LVR is filling open homes. There seems to be quite a lot of misunderstanding about what these changes mean.
- Property Valuation in Auckland is busy, no one should accept their insurance companies idea of replacement value and should get professional advice. The online calculators do not provide an accurate basis of assessment if there is a total loss situation .
- Residential real estate - Hawkes Bay. Steady
- Property industry. Industry is positive at present.
- Real Estate - low stock levels but doing well
- Real Estate - Has been a shortage of listings
- Residential Real Estate Hamilton. we still have only 50% of the stock on the market we need to. Big competition for well-presented houses in good areas. A lot of First homebuyers need to relook at their expectations on a limited budget and get back to looking for properties that they can "Add Value" to, rather than fully done up. Excellent investor interest also & more coming down from

Auckland making it even harder for first buyers to compete. The majority of property coming to the market using an auction strategy as buyers are happy to accept market value in such a transparent forum. Appraisals are increasing as sellers start thinking about the "Spring" market, but doubt we will see anywhere enough stock come on the market prior to xmas to quell the rising interest and demand.

- Real Estate Sector Hamilton: More houses are selling but as yet no appreciable rise in value. Fewer choice properties available so vendors are reluctant to accept low prices. Expect that as more homes sell there will be a demand led recovery.
- Real Estate : Johnsonville. Has been slow in new listings coming to the market but appears to be freeing up a bit more. Good numbers of buyers in the market. Tenders have been getting multiple offers.
- Residential Real Estate Tauranga continues to be very steady with lower stock numbers remaining but good number of potential sellers preparing for sale. Some concern around Reserve Bank speed bumps affecting the wrong people.
- Real Estate. Buoyant. Lack of listings.
- Real Estate is looking very positive.
- Real Estate - Tasman Region. Been a fantastic winter and spring looking even better. Plenty of buyers about.
- Real estate- buoyant, looking promising, but shortage of stock until the spring and warmer weather kicks in.
- Property Valuer Auckland - Our office is very busy with both C & I properties and residential valuations, the latter being more for insurance requirements with a slowdown in requests for finance valuations on residential properties due to changes to lending requirements.
- Real estate.. Good momentum, variety of ethnicity of clients, strong demand and remaining shortage of stock level.
- Real Estate. More buoyant than in the last 5 years with increased sales. However, after the artificial highs pre GFC, house and land prices are not increasing like they are in Auckland. We dream of this for our Vendors!!! The positive pricing in Auckland is encouraging purchasers who are doing well with their house values to invest in a Bach or a retirement plan, an hour or so to the north!! We love that!!!
- Strong interest in good quality well located properties tempered with a high degree of caution. Demand stronger than supply. Commercial real estate
- Real Estate.. Very positive in our area, Mount Maunganui and Papamoa. More buyers but not so many listings, improving though.
- Real Estate Sales, North Shore. A very good result for July and August looks great. More listings coming on and upward pressure on prices. School zones becoming important.
- Real Estate South Auckland. Very hard to get listings yet plenty of buyers wanting to buy.
- Residential Real Estate. Still very positive
- Buyers are now committing to purchasing houses and apartments off the plans which helps with bank funding of the construction
- Real estate Mt Maunganui. Things picking up and prices starting to firm short of listings.
- Wellington real estate: Slow going. Hopefully spring will un-stick the housing market here.
- Real Estate. Properties are selling very fast but mostly to Chinese buyers.
- Property. Unduly positive.
- Real Estate - Nelson. Increase in activity, multiple offers on many listings. Listings volumes slightly better than last month. Confidence high from both sellers and buyers.
- Real estate industry - still lack of listing that is driving prices up. Buyers becoming jaded from missing out at auctions.
- Real Estate, is looking good, although there is a shortage of listing.
- Real Estate - Hastings District - Hawkes Bay. Stock levels remain critically low. Buyer activity is high. Multi-offers are now common. Sales volumes are increasing. At last we are seeing the "green shoots" of recovery!
- Real Estate sales. Based in Havelock North. Market in a state of inertia due lack of listings and therefore lack of choice for buyers. No shortage of buyers and most are happy to wait for what they consider to be the right property.

- Good- real estate

Property Management/Investment

- Property Management. The rental market in the Queenstown/ Arrowtown area is currently experiencing very high occupancy and this should continue for the next period. There may be a softening as winter visitors vacate but with the projections for increased development in the Frankton area any slack will be short-lived. Prices are holding and good quality homes are receiving a premium.
- Property investor Wellington. Good properties attract good tenants and rents.
- Rental Property - things are slow in Palmerston North at the moment.
- Residential property investment in Wellington: good tenant demand. Have recently raised rents by 10%. Tenants for mid-level properties in the central city are mostly from overseas (India, China, Philippines, UK, Ireland). Many are young-ish professionals working in IT. Increases in insurance premiums are still a major concern - not as bad as previous years, but still high.
- Property (Project Management) - very busy - good although there is still pressure on fees.
- Property Investment. Flat. Tenants tight, some still struggling. Higher interest rates will keep it flat as confidence and activity increases, so too will property overheads.
- Property Management - steady and improving
- Property Manager North Shore rental listings on Trademe are now starting to fall from historic highs so the market can expect some rental pressure going into spring. This is a nice change from the last 6 months where there has been flat enquiry rents. With the sharp turn around with immigration and returning Kiwi's from Australia I can see rental shortages emerging in the next 6 months.
- Rental property and sales. Fully tenanted but sales slack.
- Property Management - Looking promising with more local investment both private and public. Will make a significant difference long term.
- Medium Size Residential Property Investment (Wellington). We are enjoying the lower interest rates locked in and potentially growth in the value of the properties on the back of Auckland and CHCH.

Key Forecasts

Dec. year		2011	2012	2013	2014	2015
GDP	annual average chg	1.4	2.7%	2.5 – 3.0	3.0 – 3.5	2.0 – 3.0
CPI	on year ago	1.8	0.9	0.5 – 1.5	1.5 – 2.0	2.5 – 3.0
Official Cash rate	end year	2.5	2.5	2.5	3.5 – 4.25	3.5 – 4.5
Employment	on year ago	1.6	-1.3	2.5 – 3.5	2.0 – 2.5	1.0 – 2.0
Unemployment Rate	end year	6.3	6.8	5.5 – 6.5	5.0 – 6.0	5.0 – 6.0

Tony.alexander@bnz.co.nz