BNZ Weekly Overview

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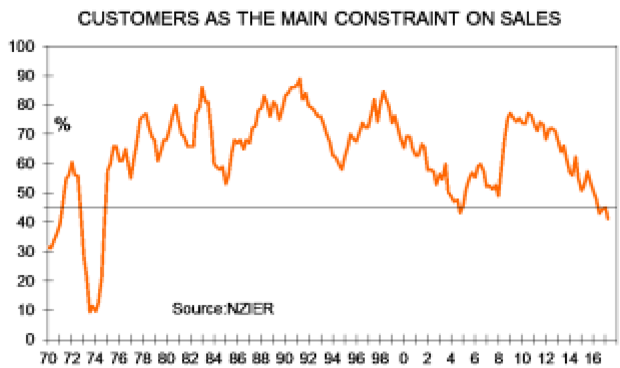
Mission Statement

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

No Shortage of Customers

The NZIER's Quarterly Survey of Business Opinion released a few weeks ago contained one number which well sums up the state of the NZ economy. 41% of businesses in the June quarter said that the main reason they cannot grow output more is a lack of customers. This number is important because it is the lowest such reading since 1974. The ten year average is 59% and in 2012 72% of businesses were saying they lacked customers.



We know that as a rule businesses like to grow and research shows that for SMEs the majority of innovation is focussed on marketing aimed at attracting more customers. But as we last pointed out during the period from 2005-07 when the customer constraint reading fell to 51%, what is the point in trying to attract more and more customers when you cannot service them?

By that we mean a gross 22% of businesses say that inability to find staff is what mainly holds them back these days (the average is 14%) – and that probably explains why the government has backtracked on its plan to make it much tougher for low skilled/low earning migrants to enter and remain in New Zealand. And that is why if NZ First find themselves in the position of again being able to determine which party forms the government, there will be backtracking away from their goal of reducing net migration inflows to 10,000 per annum. Without migrants many businesses cannot grow. Take some away and they will close.

Interestingly, only a gross 5% of businesses say that it is a lack of finance which constrains their growth. We suspect that this proportion will grow in the coming year as more and more businesses catch up with the change in credit availability in the economy. Speaking of which, the key factor causing banks to increasingly rein in their lending generosity is the need to finance lending through local borrowing, but the lack of enough growth in term deposit bases to allow this because interest rates are so low. In theory we should soon be seeing some big rises in interest rates because in theory a shortage of staff will push up the pace of wages growth and cause businesses to boost their selling prices.

But wages growth has remained low in spite of strong jobs growth in NZ and this is a common development around the world. We don't really know why yet. Still, with excess demand for their products we also in theory expect businesses to raise prices anyway as a rationing tool. But we customers react quite quickly and vocally on-line these days when prices of things go up and we cheaply search for alternatives – again online.

Businesses are uncertain just how many customers will disappear if they boost prices and uncertainty about this is one factor constraining willingness if not ability to boost selling prices. So margins are getting squeezed as businesses commit to delivering output they cannot produce. This over-trading eventually forces many out of business and this common phenomena when the economy is firm is likely to grow as businesses seeking extra overdraft financing find the bank door closed – essentially because the businesses are under-capitalised and running unprofitable margins. All businesses should think about this as they supply other businesses who then trade on your goodwill by delaying invoice settlements.

With inflation falling recently to 1.7% from 2.2% and set to decline further in response to falling oil prices and a rising currency, the chances of NZ interest rates rising much in the coming year are slim. That means deposit rates staying low and that means credit restraint from banks will worsen.

For the record, going back to the topic of immigration, this week we learnt that the annual net migration inflow rose to a record 72,300 in June. 132,000 people arrived in the country, 59,000 or so left. Five years ago these numbers respectively were 84,000 and 88,000.

In the year to June the net flow of NZ citizens was a loss of 1,284 actual Kiwis. The average annual loss since data started in 1980 has been almost 21,000 and back in 2012 the loss was 40,000. There has been no year since 1980 in which we have made a net Kiwi gain from migration flows. The closest we ever got was a net loss of 323 in the year to February 1984.

Of the gross migrant inflow in the year to June of 132,000 people, about 33,500 were Kiwis.

If I Were A Borrower What Would I Do?

Nothing much worth writing here this week given an absence of anything of any major significance regarding prospects for NZ inflation and interest rates. Chances are that borrowing costs will slowly creep higher over the remainder of this year and through 2018-19. But then again, we economists have all been painting a picture of rising interest rates since 2009 and we have had to repeatedly revise our predictions downward. It is hardly surprising then that just recently the same revisions have been made yet again.

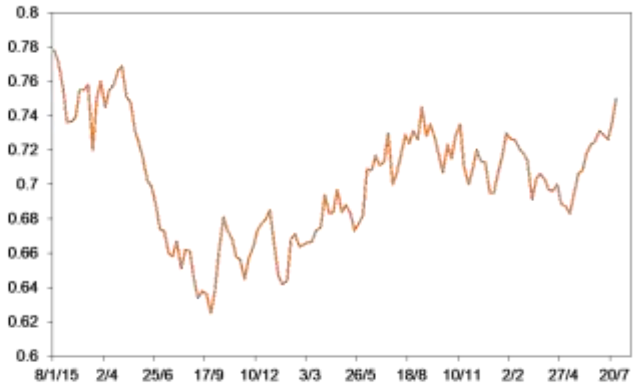
Borrowers look like continuing to face a generous environment by historical standards for a long period of time. Enjoy, but don't be averse to doing more than just fixing everything for very short time periods. There is still a small risk that inflation will surprise us on the topside one day!

NZ Dollar

The Kiwi dollar has climbed across the board this week, lifted by a variety of things. Yesterday for instance in a speech a Reserve Bank representative noted that a stronger terms of trade justifies a higher NZD. A few days ago the Finance Minister said he was not perturbed by the NZD's strength. Fonterra this morning revised up their forecast 2017/18 payout from $6.50 to $6.75 per kg of milksolids.

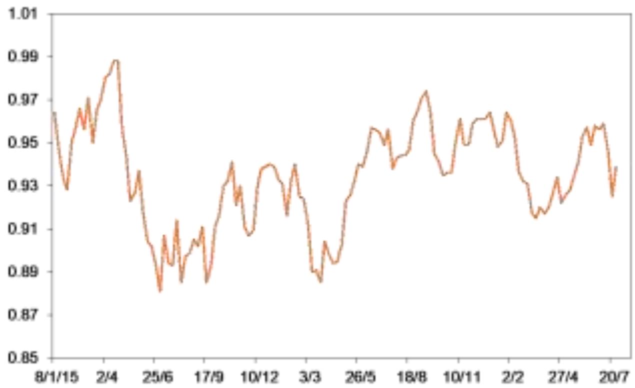
We have also seen some weakness in the USD after the Federal Reserve last night noted that inflation is tracking a tad lower than they were expecting (thus suggesting the pace of future rate rises might be less than had been factored in).

We sit now against the USD near 75.5 cents from 73.6 cents last week and 68 cents two and a half months ago.



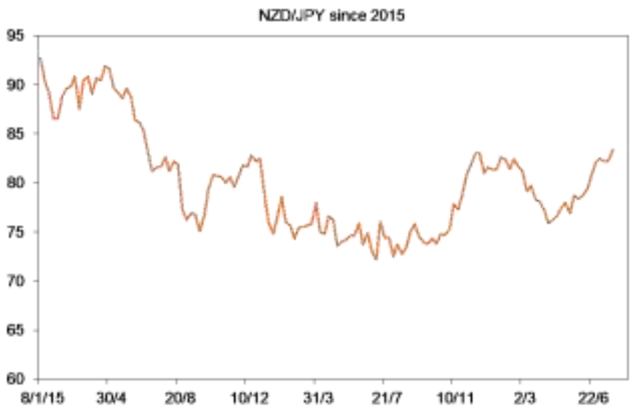
NZD/USD since 2015

Against the Australian dollar we sit near 93.6 cents from 92.5 cents last week and about the same two and a half months ago.



NZD/AUD since 2015

Against the Japanese Yen we have been on an upward trend since the second half of April while against the British Pound the NZD has settled near 57 pence after rising from 53 over May and June.



As noted here many times previously, economic fundamentals support strength in the NZD with such factors including the good pace of NZ growth, the terms of trade set to hit a record high, good government accounts, falling oil prices, and political stability at a time of huge uncertainties in all four countries just mentioned. Chances are that the NZD goes higher, but not necessarily at a rapid pace given the absence of any strong probability that NZ monetary policy will be tightened in the next few quarters. As mentioned before, exporters should keep an eye out for the inevitable periods of weakness which come along to boost hedging. A big one of these taking the NZD to 68 cents has been and gone.

If I Were An Investor ...I'd see a BNZ Private Banker

The text at this link explains why I do not include a section discussing what I would do if I were an investor.
http://tonyalexander.co.nz/regular-publications/bnz-weekly-overview/if-i-were-an-investor/

The Weekly Overview is written by Tony Alexander, Chief Economist at the Bank of New Zealand. The views expressed are my own and do not purport to represent the views of the BNZ. **This edition has been solely moderated by Tony Alexander**. To receive the Weekly Overview each Thursday night please sign up at www.tonyalexander.co.nz
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