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.

Labour Market Fundamentally Strong

The data highlight for us economists this week was not the number ten – representing days in the job for Mr Scaramucci. Instead it was yesterday's collection of numbers showing the state of our labour market in the Household Labour Force Survey and Labour Cost Index.

Starting with the HLFS which has been running since 1986, we have learnt that during the June quarter job numbers in New Zealand fell by 0.1%. Do we panic? No. The HLFS has a long history of throwing up quarterly changes which are exceptionally big up or down and hard to explain. It is best because of this deficiency in the survey to look at the underlying trends.

Doing that we see that the 0.1% fall followed a large 1.1% rise in jobs in the March quarter, 0.7% gain in the December quarter, and 1.4% rise in the September quarter. A better number showing the state of the labour market is the 3% rise in employment from the June quarter last year. Underlying jobs growth is healthy and likely to remain so with firms reporting big difficulties finding the staff they want and well above average intentions of hiring more people. Without strong net immigration employment would be going backwards.

The unemployment rate edged down to 4.8% from 4.9% and this happened in spite of the small fall in job numbers because a number of people left the labour force so the participation rate fell to 70% from 70.6%.

There is a lot of detail in the HLFS and one thing I like to do every time we get a rouge result like the 0.1% jobs fall is try and identify where the weirdness is located. Here are a couple of places.

Employment in the Manawatu-Wanganui and Southland regions fell far more than past tendencies would suggest – by near 6,000 and 4,000 respectively. That seems not to align with what is reported on the ground. Fulltime jobs seasonally adjusted rose 0.7% in the quarter after rising 0.6% in the March quarter. But part-time work fell 1.8% after rising 3.4% and before that falling 2.4%. This seems to be the measure flip-flopping around and given that only 21.5% of people actually work part-time helps one understand how hours worked actually lifted by 1% after falling 0.6% in the March quarter.

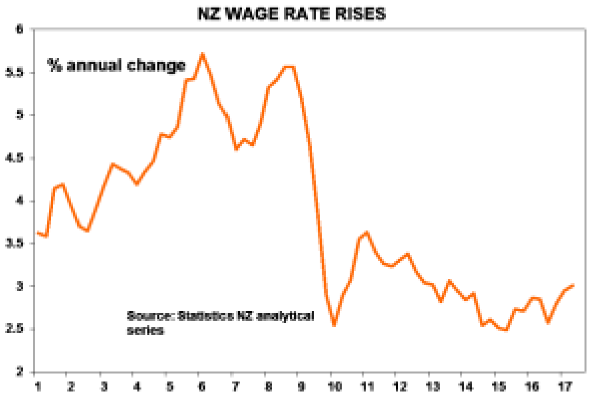
Can we look at the numbers and say anything along the lines of people being failed by the system and it is getting worse? No. Statistics NZ compute what we call the underutilisation rate. To the people officially counted as unemployed (128,000) they add part-timers who want more work (100,100), people wanting a job but not actively looking (81,000), and people actively looking but not able to start within four weeks (17,000). The resulting underutilisation rate is 11.8% which is down from 12.3% in the March quarter, 12.9% a year ago, and 13.5% two years ago.

So overall, we rate the labour market data as still strong and employers should not get excited and start thinking that loads of people will soon be banging on their doors saying gizza job, I can do that. (Boys from the Blackstuff, 1982. An absolute classic.)

And then we have wages. Around the world post-GFC, even in economies with strong jobs growth like we have, we are not seeing any decent acceleration in the pace of average wages growth.

The measure I track from Statistics NZ where best attempts are made to track the same jobs, showed an annual rise of 3% in June from 3% in the March quarter. This was up slightly from 2.8% a year ago but that is hardly awe inspiring. In fact if we look just at the private sector the annual change is 3.1% from 3.1% a year ago, 2.6% two years ago, and 3.4% three years ago.

It still seems reasonable to say that there is statistically no decent acceleration in the average pace of wages growth in New Zealand despite the reported tightness in the labour market.



As written here over 2005-07 and more recently, it would be beneficial for the economy if the pace of average wages growth were to double. It would help with home affordability, it would deliver badly needed income to parents trying to raise families, and by forcing inefficient businesses out of the market would boost productivity growth in the economy. The closures would force a reallocation of people to higher paying and higher productivity jobs they may currently be scared to take – last on first off worries.

House Building

We learnt this week that there was a small 1% seasonally adjusted fall in the number of dwelling consents issued all around New Zealand in June. This means that in the June quarter numbers fell 0.4% after rising 4.3% in the March quarter, falling 7.4% in the December quarter, and rising 1.6% in the September quarter. The underlying pace of growth is minimal. However, this is mainly because there is a large pullback underway in Canterbury now that most of the post-quake residential construction has been done.

In the June quarter the number of consents issued in Canterbury was down by 34% from a year earlier. But Auckland was ahead 7% as was the rest of the country excluding these two large regions.

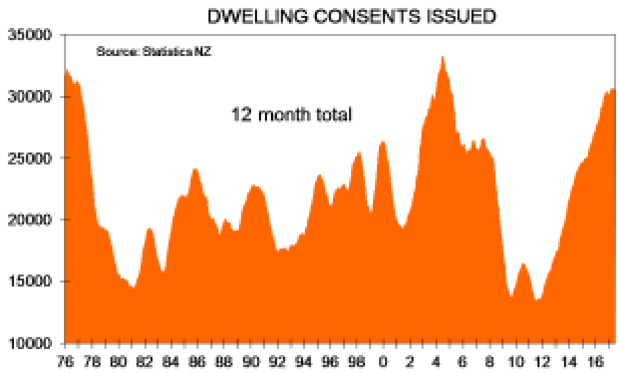
The Auckland growth is however fairly minimal and the chances of any reduction over the coming year in whatever your estimate of the shortage is are minimal. In fact we learnt on Monday that the shortage got worse by 1,000 more than we thought last year because extra digging into the data showed only 6,200 houses were actually built in Auckland – not the originally reported 7,200.

Given that Auckland's population has grown over 45,000 in that time period and housing such growth requires at least 15,000 dwellings, the shortage has worsened by 9,000 units – again, from whatever number you were using in your head a year ago as the size of the shortage. The price implications remain as obvious now as they have been since 2008, though now more in terms of supporting current prices with an upside bias further out rather than clearly boosting them.

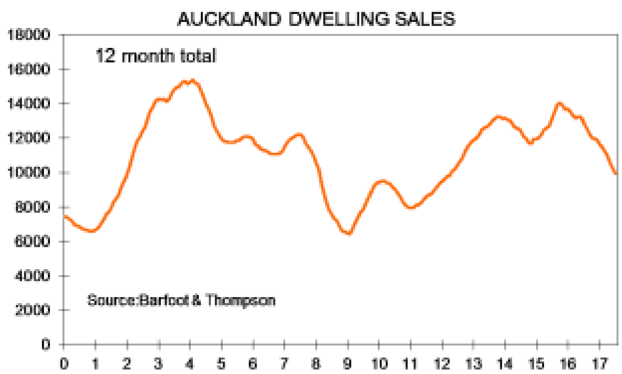
For your guide, this following table shows by how much over the year to June the number of consents issued has changed in each region.

Northland	21.0%
Auckland	6.4
Waikato	2.8
Bay of Plenty	7.1
Gisborne	-13.9
Hawke's Bay	28.0
Taranaki	23.6
Manawatu-Wanganui	38.7
Wellington	19.7
Tasman	3.3
Nelson	35.0
Marlborough	38.5
West Coast	35.3
Canterbury	-20.0
Otago	28.3
Southland	-5.5
Tasman	3.3
Nelson	35.0
Marlborough	38.5
NZ	4.7

At 30,453 the number of consents issued for the construction of all types of dwellings throughout the country is down slightly from 30,645 a month ago. The annual number has broadly gone nowhere since October as growth switches from Canterbury to the rest of the country. Hopefully this means that with more resources slowly going into the construction sector (immigrants, apprentices, people retraining or renewing qualifications) we will see some easing of the pace of growth in construction costs.

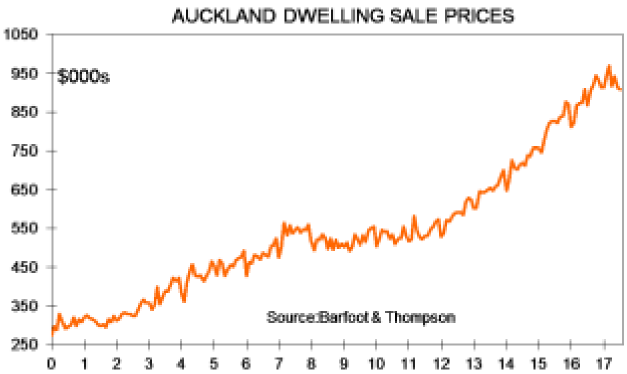


Regarding real estate turnover, Barfoot and Thompson released their monthly data yesterday. In July they sold 28% fewer dwellings than a year ago which is consistent with falls ranging from 27% to 32% for the previous three months. Sales are weak. No surprise then that the stock of listings is ahead 36% from a year back.

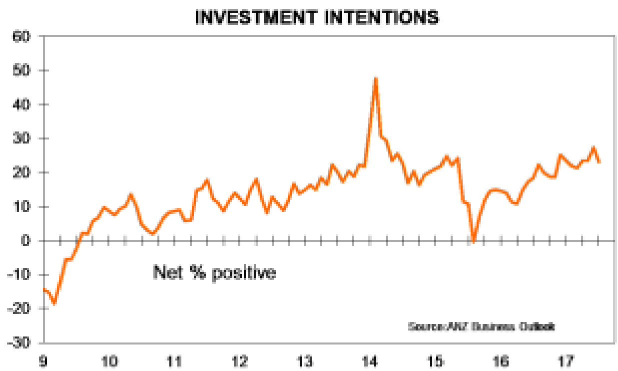


But this is where we can start to see things moving toward a new equilibrium. The number of new listings received in July was down by 18% from a year before. June was down 11% and May 9%. The July total of 1,173 new listings was the lowest for the month in six years.

Regarding prices, the average sales price in the past three months was down by 2.4% from the three months to April but still ahead 4.3% from a year ago. The 2.4% fall is less than the 3.2% fall in the three months to March 2016 so we have seen worse recently. But the flattening tendency is fairly clear and it will be interesting to see how long it takes for the adjustment of vendor price expectations to occur and for over-indebted investors to quit their assets.

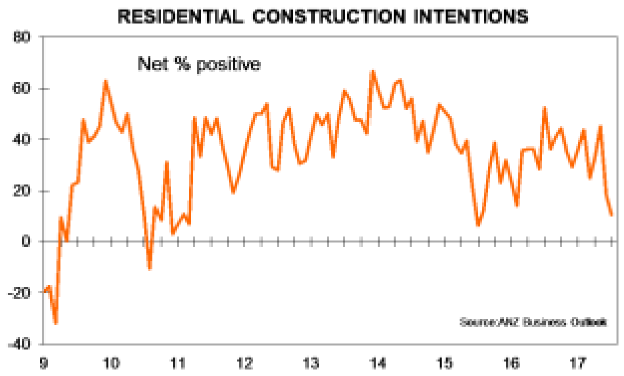


This week also saw the release of the monthly ANZ Business Outlook Survey. There was nothing startling in the survey results. Businesses continue to expect to be busy, demand for staff is strong and still rising, and businesses are planning a lot of investment.



But there has been an easing in expectations for construction sector activity.

Only a net 11% of builders expect more house building activity in the near future, down from 33% three months ago and 52% last July. Only a net 6% of commercial builders expect to get more busy, down from 35% three months back and 38% a year ago.



These two results are consistent with the consents data discussed just above and general anecdotal evidence from the construction sector of things flattening out.

The only other mildly interesting results from the ANZ survey were the two main inflation indicators. Both the net percent of respondents planning to raise their prices and the average expectation for inflation a year out eased a tad in July. Neither change is large, but the pullback helps support the view that inflation pressures remain comfortably in check and monetary policy could sit unchanged for a still very long period of time.

NZ Super

Two weeks ago Treasury released a Regulatory Impact Statement on NZ Superannuation Policy. It is a relatively easy to read piece for anyone interested in the sustainability of our current fiscal system and it focusses on the discussion about policy options.
http://www.treasury.govt.nz/publications/informationreleases/superannuation/sup-3753731.pdf

I took a look at the paper to try and gain some insight into a couple of factors relevant to the long term sustainability of the NZ super scheme. One is Treasury's assumption about net average annual migration flows. They use 12,000. That seems much too low considering that over the past ten years the flow has average almost 25,000 per annum and before that 11,000 per annum. A higher average flow will mean more employees able to make tax payments supporting NZ Superannuation flows because migrants tend to be working and tend to be young.

I also wanted to see how they factored in a rise in the proportion of people 65 years of age and over remaining in paid employment – therefore delivering more tax into government coffers. But it is not clear that this proportion is assumed to rise above the near 24% recently achieved – from less than 6% in 1998.

This means the actual rise in the after-tax cost of NZS measured as a % of GDP could be less than the projected 4+% now to just over 7% come 2060. The current OECD average is about 8%.

The proportion of NZ's population projected to be 65 and over come 2060 is 27 from 15% currently. For your guide here are the current ratios in some other countries.

	%
Australia	15
Denmark	21
Finland	21
Germany	21
Greece	22
Italy	23
Japan	27
New Zealand	15
Portugal	21
Spain	19
United Kingdom	18
USA	15

http://data.worldbank.org/indicator/SP.POP.65UP.TO.ZS

If I Were A Borrower What Would I Do?

Economies no longer function the way they did before the GFC, and that means it is not appropriate to develop interest rate forecasts and expectations using old style thinking. Such thinking has seen us economists repeatedly and near consistently over-forecast inflation and over-predict interest rate levels since 2009. This has happened both here and overseas.

The key change of relevance is that firm economic growth which drives firm jobs growth and an apparent tightening up of the labour market is not leading to accelerating growth in the average pace of wage rises. We struggle to explain why. Maybe the internationalisation of the labour market spreading from manufacturing to services. Maybe greater pushback from employers struggling to boost selling prices now that consumers can easily go online to find an alternative supplier. Maybe the gig economy and young workers seeking to gain higher earnings through building connections at multiple firms and roles rather than securing a job and trying to boost wages as much as possible for that role. Maybe reduced union membership.

Whatever, the upshot is that we are all fairly flummoxed by the consistent downside surprises on inflation and that means we have to be cautious with regard to thinking that surely from now the old ways will return, wages growth and business pricing will jump up, and interest rates will need to rise a lot.

But there is more in the mix suggesting it is reasonable not to be too fearful of big rate hikes than just the lessons of the past eight years. There is also the de facto tightening of monetary policy already underway in New Zealand through the Reserve Bank's introduction of LVRs in October 2013 and their strengthening since then in October 2015 and July last year. By restraining credit supply (not demand) they have restrained property price growth in Auckland and the rest of the country will eventually be affected in the same manner.

Then on top of that restraint on growth we have the tightening up on lending rules being introduced unilaterally bit by bit by banks adjusting to an environment where funding for lending is more costly and less available than before. This is because lending now needs to be funded by domestic borrowing as best as possible, but raising term deposits in NZ is hard given the low level of interest rates and the tendency of Kiwis not to save.

Then on top of that we have, from a borrower's point of view a good/bad factor. The ratio of household debt to income is now higher than it was before and borrowers have become used to a lower average level of interest rates. Interest rate sensitivity has increased. That means that when the Reserve Bank some year does raise interest rates, they won't need to go up that much in order to get whatever degree of restraint they are seeking on the pace of economic growth and eventually inflation.

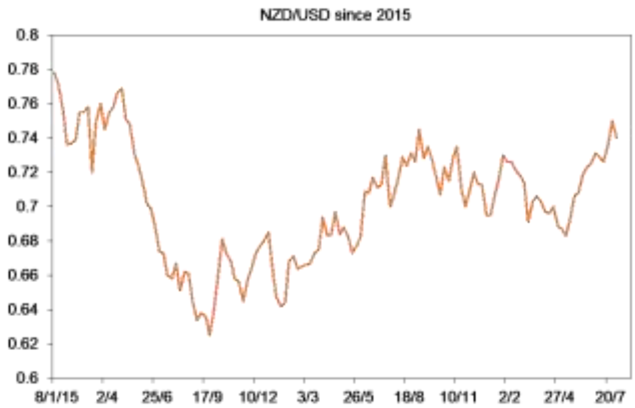
With so much uncertainty regarding the influence of all these developments on the pace of growth and inflation, and the experience of two bouts of raising the OCR since 2010 only to cut it again, the Reserve Bank can be forgiven for projecting that they will be sitting on their OCR hands until the end of 2019.

We will get an update on the RB's thinking regarding these various developments, the outlook for growth and inflation, the influence of offshore developments, and therefore the possible path for cash rates when the next Monetary Policy Statement appears in a week's time.

If I were borrowing at the moment I would have a small proportion of my loan locked in for three years, a small bit floating for the flexibility in making early repayments, and the rest divided between one and two year terms.

NZ Dollar

The Kiwi dollar this afternoon was sitting near one cent lower than a week ago at US 74 cents. The decline largely was driven by yesterday's reported fall in employment of 0.1% during the June quarter rather than the expected rise of 0.7%. The result reduces even further the chances that the Reserve Bank will be forced to raise the official cash rate earlier than their current prediction of the end of 2019.



Personally I still favour the kiwi dollar generally rising rather than falling.

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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