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.

Our Economy

Migration Boost Up Since Mid-2018?

Guess what? Statistics NZ released their monthly migration data last Friday and they were exactly as we expected – hugely different from last month. Seriously – if you are interested in getting a feel for how net migration flows are trending in New Zealand you cannot any longer place any reliance upon SNZ data for the most recent months.

Two months ago SNZ estimated that the net migration flow in the year to November was a gain of 43,400. Last month they revised that up to 48,000. Now they estimate the flow was actually 53,800. And it is not just the end of year numbers which have changed. Two months ago they showed the net annual gain steadily falling away. One month ago they showed the flow flattening. Now they show the net gain rising from a low of 50,000 in the year to June to 58,400 in the year to January.

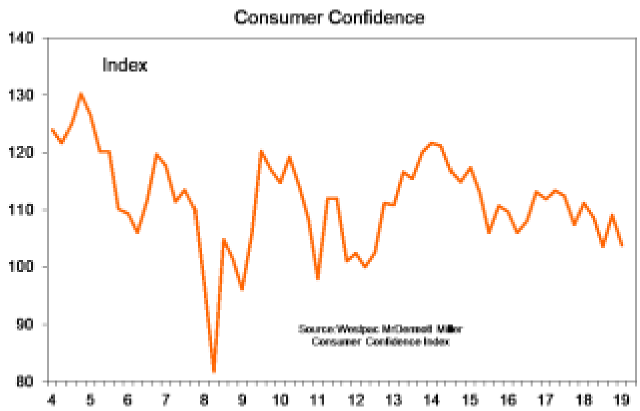
So in the space of two months we have gone from net migration flows slowly falling off to now trending up at an annual pace of about 15,000 per annum!

What are we to assume in our discussions about pressures on housing markets, transport systems, immigration policies etc? I'm going to simply say that net migration flows seem to be holding up a tad below the peak level of mid-2016 with upside risk as slowing economies elsewhere - Australia in particular - encourage Kiwis to stay home, come back home, and encourage foreigners to keep trying to get in here.

That means continuing good support for Auckland's housing market in particular, helping to offset whatever your personal guess is regarding how many people choose to sell because of ring fencing etc. The signal to such people from the migration numbers is don't be in a rush to sell. We won't see a repeat of the 95% surge in prices over 2012-16 when the next upturn one day appears, but the trend in prices is still likely to be upward and an assumption of price gains averaging 3% per annum seems acceptable to me.

Oh, and want a laugh? If you do the exercise we have done for years of annualising the latest three month seasonally adjusted net flow numbers to get a feel for where the actual annual total is heading, you get the underlying flow now sitting near a historical high of 74,000. What will next month bring us? Probably some downward revisions as the latest two months' inflow data look weirdly strong.

We also learnt this week that consumer confidence as measured every three month by McDermott Miller and Westpac decreased to a still above neutral reading of 103.8 from 109.1 in the December quarter. Is this important? Not really. It just takes the measure back to where it was in the September quarter and following that we still saw good consumer spending growth in retail stores during the December quarter. For retailers the issue is still going to be more one of competition than total spending by householders.



Landed Peasants

New Zealand's income per capita fell below the OECD average in the 1970s and 1980s when governments of the day placed hefty restrictions on economic activity and initiated a number of wasteful large-scale industrial investments. Since then things have stabilised but not improved.

Research by Treasury suggests we can lay a lot of the blame for our continued under-performance on our distance from markets and small population size. A few years ago I also discussed the role potentially played by our business culture.

Beyond our culture one problem we have is companies being developed and initially growing in New Zealand, but then shifting offshore once a certain size is reached and sufficient foreign money is offered to generate a sale. This tendency is only likely to intensify as global companies specifically search out businesses outside their home bases which have things they can incorporate in the next iteration of their products for which the need for change seems to accelerate all the time. The chances that NZ will ever have a clutch of new large companies based, listed, and producing here are negligible.

Related to that, this week has brought another example of why we will never go strongly back up the income per capita ladder. Westland Milk is poised to sell itself, subject to shareholder votes and official approval, to Chinese company Yili Industrial Group for $588mn. This will give Westland Milk a different structure to Fonterra for which any benefits of going up the value added and marketing chain can accrue to Fonterra shareholders. Suppliers to Westland will lose that.

Any profit gains from new products etc. will go solely to the owners. Capital supplied by Yili after the initial purchase will not go into basic milk processing (drying) equipment to handle the extra volumes farmers seem always to want to produce and be paid for. Instead the capital can be devoted solely to boosting returns from their finished product range.

Suppliers will not be shareholders (capitalists) so they will receive no return above payment for their milk. It may sound attractive to some that the annual payment for the next ten years will not be below whatever Fonterra pays and they can get their high levels of borrowing from banks down with an average payment for their shares near $0.5mn. What are the chances that the annual payout to Yili suppliers will voluntarily be above Fonterra's payment? Maybe that depends upon the ability of current Westland suppliers to sell their milk elsewhere – and given the transport logistics involved that ability looks to be low. So…..

The term "peasants in our own land" has been used over a long period in New Zealand, usually in the context of selling land to foreigners. Retaining ownership of land is good. But relinquishing ownership of assets into which contributing capital will likely yield a far, far greater return than investing the same capital on the land is near effectively the same thing – landed peasants receiving cash for their raw material production. Like a forestry company selling logs. Or a mining company selling coal.

And apparently in the North Island some Fonterra suppliers are selling their shares and choosing to supply a foreign-owned company. They get a lump sum in the hand but by becoming simple croppers will receive no benefit from branding and product development of the buying Chinese company.

Does this mean that when the Reserve Bank raises NZ bank capital requirements and lending to higher risk activities like dairy farming and commercial property development gets priced higher and cut back, that more Fonterra suppliers will seek to sell out for the lump sum and debt reduction? In 50 years' time will activists in China initiate a Fair Trade campaign to see NZ milk growers receive a fair payment for their product – as we in the West now do for coffee bean growers? You don't need to sell your land to lose control of your future. Just take on too much debt and become a desperate seller.

Housing

CoreLogic produced some interesting work this week looking at how long different types of property owners hold onto their properties. On average all owners who sold last year had held their property for 7.4 years before selling, well up from 3.8 years in 2007. There is no justification for a view that people are buying and flicking off quickly. First home buyers tend to hold for about one year less on average than investors.

Your Strategy

-Things to consider in your next annual strategy session.

The terrible events of last Friday, the Christchurch earthquake of 2011 and earthquakes after then, relatively frequent flood events, and even industrial actions remind us that we can never assume smooth continuity of operations in our business plans. Beyond necessary preparations such as fire drills and in schools lockdown procedures, businesses need to draw up ahead of time "plans" for how to handle or more accurately mitigate the effects of unexpected events of unknowable intensity, spread, and duration.

Insurance is one obvious route for certain events – and in that regard, following the IAG announcement that they will not write new policies in Wellington, what could be one's response to actual withdrawal of insurance cover? Eventually insurance is likely to be removed or priced very expensively for properties not just at high risk of seismic damage but flood inundation as well.

Half a day spent discussing potential sources of disruption and initial thoughts on how to prepare and respond could be a very useful input into developing written contingency plans.

If I Were A Borrower What Would I Do?

There is no hint offshore that the risks facing world growth, world inflation, and interest rates are starting to shift. The risks are still mainly downward and that means the incentive for a borrower to fix long-term are low unless someone is offering an extremely low rate – perhaps to buy market share.

It is not likely that the potential decline in sentiment and perhaps willingness of some foreign visitors to travel to NZ or Christchurch following last Friday's atrocity will feature large in the 2019-20 macroeconomic outlook. But nonetheless, on top of this week's decline in consumer sentiment recorded earlier in this quarter and still weak levels of business confidence, an outlook for sustained low interest rates remains valid.

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 here. http://feedback.bnz.co.nz/forms/lFdYSs5FGEq4kAjP95uzTA
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