BNZ Weekly Overview

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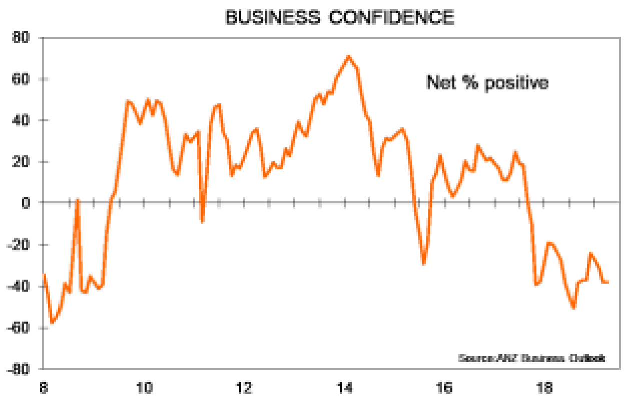
Mission Statement

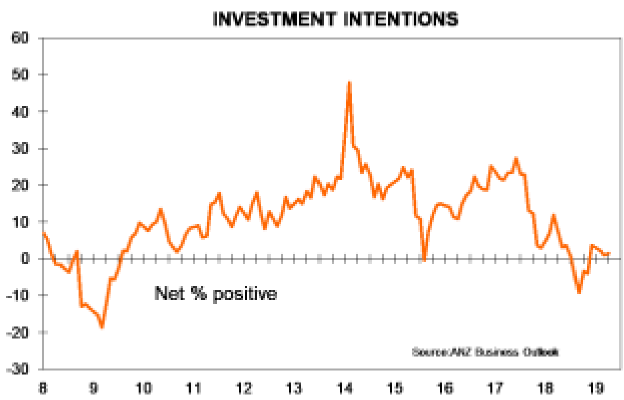
To help Kiwi businesspeople and householders make informed financial decisions by discussing the economy and its implications in a language they can understand.

Our Economy

The ANZ Business Outlook Survey was released this Tuesday and it shows that sentiment in the NZ business sector remains in the doldrums. A net 40% of businesses expect the economy to get worse. This is unchanged from the March result, down from a net 18% positive just before the late-2017 general election, and well below the long-term average reading which also is a net 18% positive.



Unsurprisingly, with their feelings so negative businesses are not overly inclined to spend money on new machinery. Only a net 2% plan boosting their capital expenditure versus a ten year average reading of 15%.

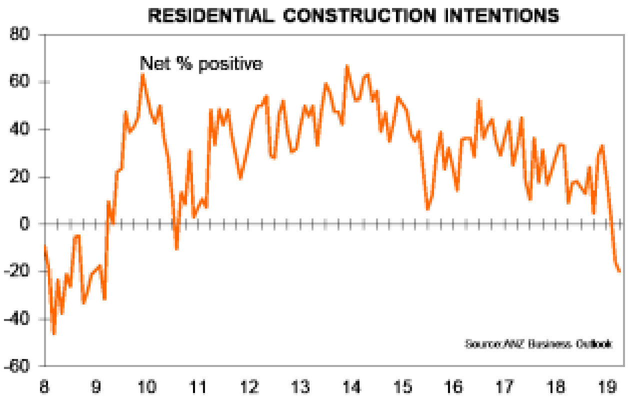


This measure is up from a low of -9% in the middle of last year which is good. But it was 23% pre-election. Its continuing weakness is bad news because it means not only are firms probably insufficiently boosting capital spending to supplant labour which they cannot find, but they are undoubtedly not maximising efforts to be able to handle the accelerating speed of change we see in most sectors.

With regard to employment, only a net 4% plan raising staff numbers. This is up from a -6% low mid-2018 but below the average of 14% and the pre-election reading of 17%.

A couple of interesting results from the survey are these. First, a net 30% of businesses in April expected interest rates to fall. The March result was a net 12% expecting rises. This massive change is consistent with the global trend over our summer away from expecting tightening monetary policies as both economic and especially inflation data came in weaker than expected.

Second, a net 20% of builders expect lower levels of house building compared with 16% negative in March and +4% in February. The ten year average for this measure is +35% and it was +36% pre-election.



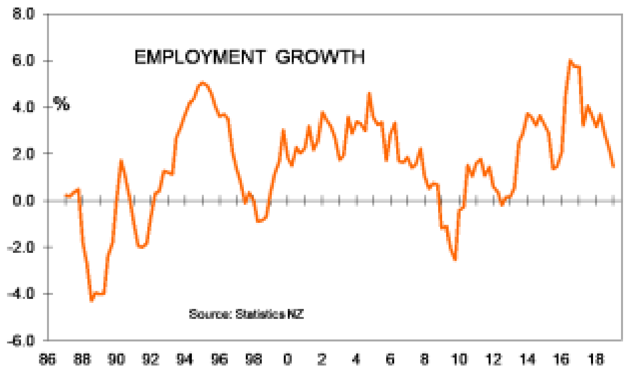
This low result, the worst since the GFC, shows why we have been so strongly warning that hopes of surging house construction causing lower prices would be misplaced. Construction cannot boom in New Zealand. We do not have either the labour resources to do it or the required level of competence in even the largest of our construction companies.

Deficiency of house construction in our major cities set alongside above average population growth will set the scene for the next period of strong cyclical rises in house prices perhaps 2 – 4 years from now in Auckland with the regions going along for the ride. Before then however the regions will go through a flat patch which will likely be locked in for most locations by early next year at current best guess. For insight into house purchasing in the regions go to this week's Housing section where we show there has not been the rush of first home buyers people keep talking about.

Based on the ANZ survey results it would be unwise for anyone to think that our GDP growth rate will surge above 3% in the near future. In the context of average world growth being likely in coming years, good population growth, firm construction and tourism, underlying growth in sectors like health, aged care, and the digital economy, easing fiscal policy pre-election, and good conditions in most primary sectors, annual growth near 2% - 2.5% seems a reasonable assumption for our economy these next few years.

Such growth will underpin jobs demand, especially as insufficient investment by businesses will mean they will need even more staff in the future to meet output goals. There is no basis however for believing that the factors constraining wages growth in a low unemployment environment of recent years will suddenly change and that wages growth will surge. It probably won't therefore inflation will remain low and interest rates also will continue at these low levels for many, many years. That will be good for borrowers – sort of – but not so good for investors. And it is that interest rate/investor link which so many people have failed to take into account whilst since 2009 incorrectly predicting falling house prices. Low term deposit returns have driven older people preparing for or in retirement into other assets like shares and houses. Continuing low interest rates will keep them there.

Speaking of jobs growth, yesterday the Household Labour Force Survey and wage measures were released for the March quarter. Seasonally adjusted job numbers fell 0.2% after sitting flat in the December quarter. Annual jobs growth has slipped to 1.5% from 3.1% a year ago. This is the weakest result since 2015. However there are a few things to remember.



First, these numbers can be quite volatile and in 2015 after employment was unchanged in the June quarter and fell 0.3% in the September quarter it then rose by over 1% in each of the following six quarters. Back then only a net 23% of businesses reported difficulties finding skilled labour and 3% unskilled versus 50% and 33% respectively now. So the labour market is tighter now than back then, as seen in the unemployment rate then being 5.6% versus 4.2% now – a small decline from 4.3% in the December quarter of 2018.

Second, you can't hire what you can't find. It was always unreasonable to think that jobs growth could continue at the 3.5% average annual pace recorded from 2014 to 2018. Businesses have reported major problems sourcing and keeping staff and one of the widely identified problems globally during this technological revolution we are living through is a growing mismatch between skills offered and those demanded.

So the interpretation I choose to take of these volatile employment numbers is that growth has slowed from unsustainable rates and the data have captured and perhaps consolidated that slowdown in the period from mid-2018 to now. From here on growth is likely to improve on a quarterly basis but remain low on an annual basis – which is what you get when you hit full employment.

On an industry basis we can work out the main contributors to the slowdown in growth over the past year. Over the year to March 2018 job numbers rose 79,000 then they rose 38,000 in the year to March 2019. The biggest percentage contributions to the 41,000 growth slowdown were

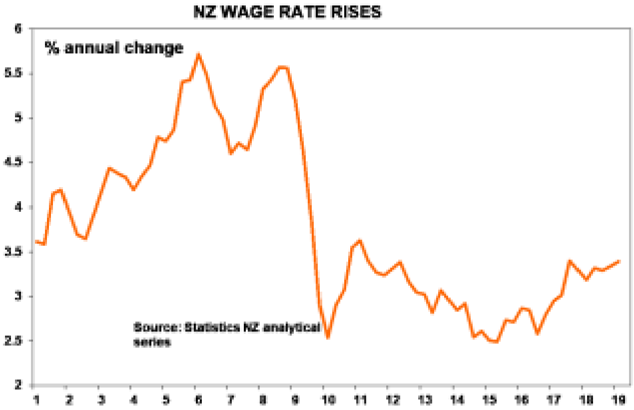
-retail trade and accommodation	54%
-public administration	26%
-education and training	67%
-manufacturing	23%

There were offsets from agriculture (less shrinkage, not growth!), IT and media, and "Not Specified" at -69%. That latter number is one of the reasons we treat the HLFS data with caution.

Looking at the industry breakdowns, does it make sense when core retail spending volumes have risen by 4.5% this past year and visitor numbers have risen 3% in the one year and 35% over four years that employment in these sectors would fall? And who is laying off the teachers? Perhaps the 7% fall in education numbers this past year reflects reduced foreign student numbers? It seems a bit excessive. Regarding a centre-left government producing a slowdown in public servant numbers growth to 1.2% this past year from 9.1% the year before – maybe they've simply run out of desk space?

Much as we would like to write stories and produce interesting graphs regarding industry employment growth rates, frankly they go all over the place. So it's best to stick with the total numbers showing simply that jobs growth has slowed down.

What about wages growth? Is it accelerating yet? Only marginally. The measure which I follow contained in the Labour Cost Index calculations recorded a rise in the year to March 2019 of 3.4% from 3.3% in calendar 2018 and 3.2% a year ago.



Housing

Young Home Buyers Are Not Flocking To The Regions

One of my key themes in recent years has been that every house price cycle people over-estimate how many young people will shift to the regions. This happens because popular discussion gives the impression that the most important thing for young people is buying a house and locking themselves into a location and mortgage as soon as humanely possible – so they can then start breeding and become responsible citizens. People in the regions wax lyrical about ready access to the outdoors. But they also lobby hard for big city amenities like community swimming pools, perhaps because the rivers are unswimmable, and forget that NZ cities are so small by world standards everyone has ready outdoor enjoyment access already.

The belief in regional surges is especially strong this cycle because Auckland house prices started rising firmly about three years before the regions. Now, with Auckland stalled since late-2016, the regions are completing their catch-ups. The more usual cycle is prices generally moving together.

So, do we as a rule see few young buyers in the cities perhaps because houses are so terribly expensive, and a dominance of such buyers in the regions? No.

Using CoreLogic data, drawn from their analysis of property title transfers, we can see for each of 72 locations around New Zealand which places have high sales to first home buyers and which have low. Over the year to March 37% of sales in

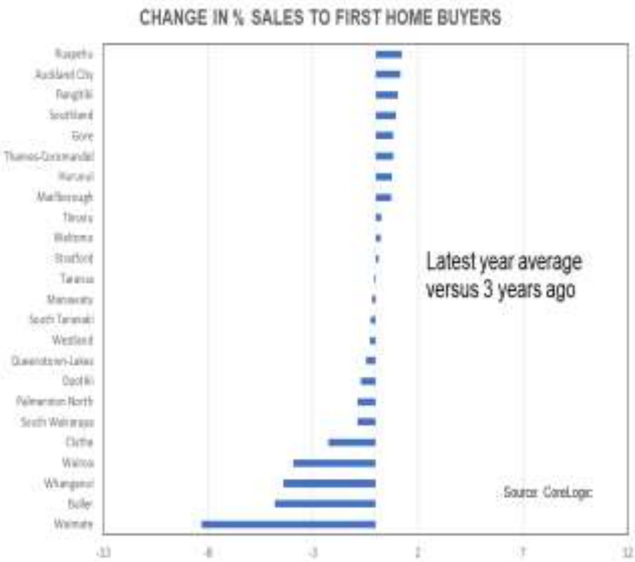
Auckland's Papakura City were to first home buyers. In Waitakere it was 35%. Dunedin is on a par with Auckland's North Shore. South Wairarapa, just over the Rimutaka Hill from Wellington sits at only 13%.

I have split the graph showing the proportion of sales (title transfers but we will for simplicity call them sales) into three sections. If you still can't read the location names – enlarge the image. For anyone old and decrepit reading this still wondering how to do that – imagine two pennies on the screen and pushing them apart with two fingers on the same hand.

Owning a house may well be important for many young people and it is politically incorrect to challenge this view. But employment and income advancement is the unspoken nasty secret, and it is in the cities that the widest range of opportunities exist – again, it being politically incorrect to make such a capitalistic claim.

Nonetheless, could it be that we have seen a surge in first home buying in the regions? We can gauge this by comparing the past year's average proportion of sales to FHBs in a location with three years ago. Why three years back? Because from July 2016 banks began to enforce the 40% investor deposit requirement required officially by the Reserve Bank from October that year, and because this was when Auckland was approaching its peak and the regions not cranking yet.

The changes are shown in the following three graphs. In 28 of our 72 locations the proportion of sales going to first home buyers either fell or rose less than a fairly insignificant 2%. Note the small decreases for Palmerston North and Wanganui, miniscule rises for the likes of Gisborne, Nelson, and Invercargill, and even Wellington where it had seemed reasonable to run a theory of young people shifting there from Auckland. The biggest shifts toward first home buyers gaining ownership were the tiny locations of Mackenzie and Kawerau, plus Papakura and Waitakere in Auckland. Note the 7% increase for Waikato, 7% for Otorohanga, 6% for Hamilton, but also 5% for Manukau in Auckland. The 5% gain for Auckland's Franklin and 4% for Rodney exceed the gains for Hastings, Napier and Whangarei which equalled Auckland's North Shore.



One cannot run a generalised argument that young people are flocking to the regions. Apart from the employment and income growth reasons there is another. By making it harder for investors to enter the market from the second half of 2016 through the 40% nationwide minimum deposit requirement, a key reason for young people to go to the regions – strong competition from investors at auctions in the cities – was reduced. And another reason to go regional was removed last October when the ban on foreign buyers came into force.

There are some in government who are trying to craft policies which will boost the flow of new blood into the regions. But every move which reduces big city competition for first home buyers provides them with an incentive to stay focussed on our big centres. In fact the placing of high minimum deposit requirements on investors from 2016 has pushed them out to the regions from the main centres and made it more difficult for young people to get on the housing ladder in the regions.

And what will ring fencing of tax losses from wage and salary income do? Greater than desired annual cash losses will lead some investors to try and make those losses more manageable by investing in lower-priced properties in the regions. The effect will be a mini version of LVRs on investors.

In a few weeks we will do the above graphical analysis for investors rather than first home buyers.

Pointless Price Gauges

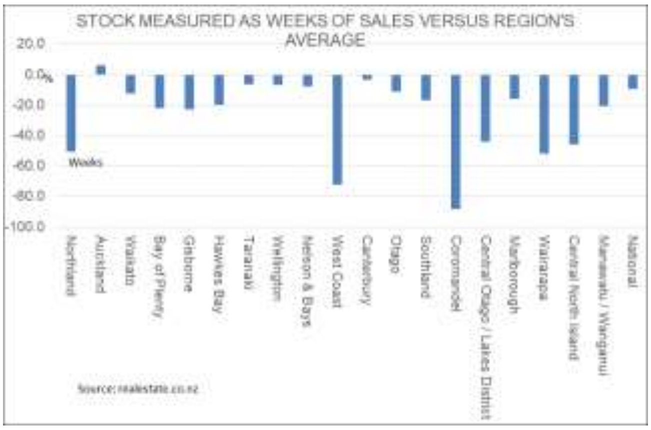
Just for your guide, this week data were released showing some big changes in median price measures, not any individual house prices, over the past year for some suburbs in Auckland. One headline read "Central Auckland House Prices Plummet", another read "Housing Prices Fall By Up To 30%." Ignore the "information for two reasons.

First, at the suburb level prices can go all over the place even comparing six months with a year earlier. Second, the median price measure does not adjust for shifts in the composition of dwellings sold.

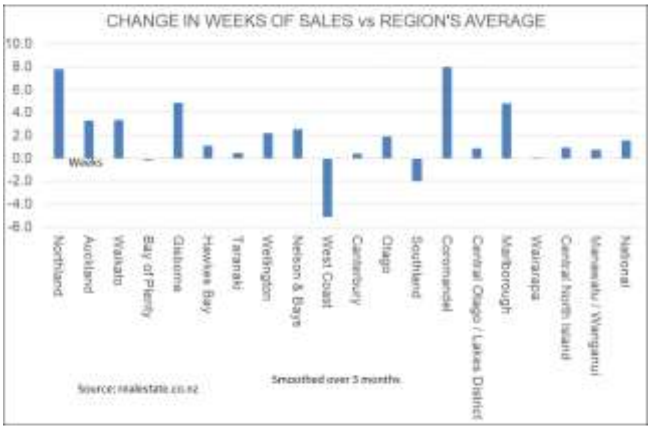
The only price measures worth looking at and the only ones I analyse here are the House Price Indexes compiled by REINZ and released in their normal mid-month reporting of what happened the previous month. The HPIs adjust for composition changes by comparing differences in the price of whatever sold with its rateable value.

Listing Stocks Creeping Higher

Each month I look at the data released by realestate.co.nz to see how listings are going. What I concentrate on is their weeks' worth of stock on hand measure to see if it is falling – market strong – or rising – market easing off. The first graph shows by how much the most recent weeks' worth of stock measure for each region compares with the regional average.



Stock levels are below average everywhere except in Auckland. Markets are strong. In the next graph I look at whether stock levels are rising or falling. They are becoming less below average in all regions bar Bay of Plenty and the tiny West Coast, and more above average in Auckland.

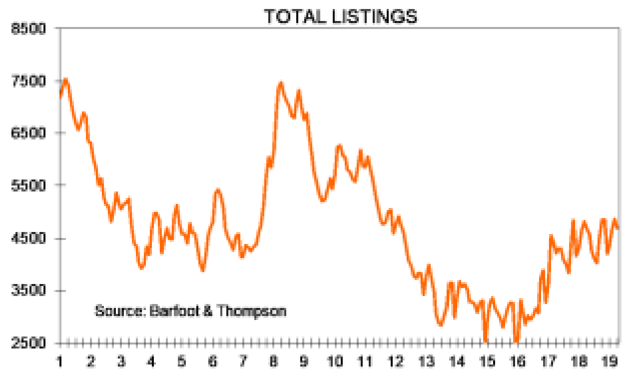


These numbers tell me that in the regions the high strength in conditions is starting to ease but sellers' markets remain.

Barfoots Data For Auckland in April

In Auckland in April Barfoots, which has over 40% of the residential real estate market, report that the number of new listings they received was down by 12% from a year earlier. In the three months to April new listings received were down 10% from the same period in 2018 and the end of month stock of listings was unchanged from the end of April 2018.

The data tell us that there is no rush of people looking to list their properties. Without such a rush one would severely struggle to run a story that earlier concerns about a CGT, foreign buyer ban, and worries about ring fencing are encouraging people to quit their property holdings.



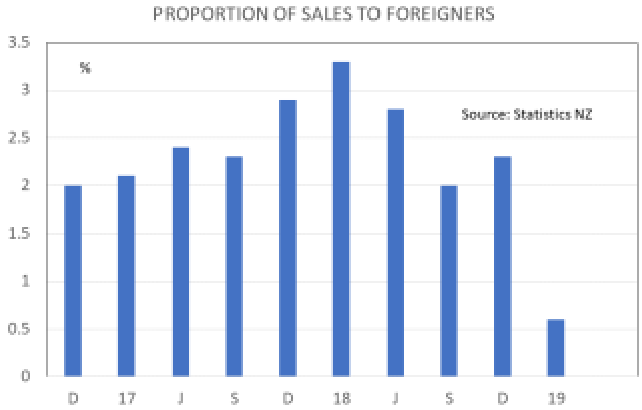
Few Offshore Sales

Data released this morning by Statistics NZ show that during the March quarter 0.6% of title transfers for residential property in New Zealand involved purchase by a foreigner – someone without citizenship or a residents visa. This is the lowest proportion since data started in the December quarter of 2016 and was down from 2.3% in the December quarter of 2018 and 3.3% a year ago.

The proportion of sellers who are foreigners declined from 1.5% a year ago to 1.0% now. What do these numbers tell us?

First, the ban on foreign buying from October last year has been effective in lowering sales offshore.

Second, that very few properties have in fact been sold to foreigners over the past two and a half years – just 2.3%.



Third, absence of foreign buyers has not had a noticeably negative impact on the NZ housing market. Sales have remained strong outside Auckland with rising prices. In Auckland during the March quarter average house prices fell 1.1% after falling by 0.9% during the December quarter. One could run an argument of some impact there but if so then the depressing impact on prices of foreign buyers being largely absent has been a fairly minor one and the impact may now have ended.

If I Were A Borrower What Would I Do?

I'd still be very happy to take my time before fixing for either a two or three year period. Following lower than expected inflation in New Zealand, surprise surprise there were lower than expected inflation numbers released in Australia last week. Their inflation rate now sits at a record low and the shock result of 1.4% has caused markets there to firm up pricing for rate cuts soon by the RBA. The same has happened in New Zealand with financial pricing suggesting over a 50% expectation that come the next RBNZ cash rate review on May 8 a cut will be made.

However, it seems a bit bold to strongly expect an NZ rate cut next week in light of recent economic data for the US, China, and European Union coming in better than expected.

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/IFdYSs5FGEq4kAjP95uzTA
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