BNZ Weekly Overview

5 August 2010

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.

In this week's issue….

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 email me at tony.alexander@bnz.co.nz with 'Subscribe" in the Subject line.

Monthly Survey

It's the first week of the month again so we are running our regular confidence survey. If you have not already done so in the email used for sending out the WO please cut and paste the url below into your browser, click on it and let us know whether you think the economy will get better or worse over the coming year. If time permits pen a sentence or two telling us how things are in your industry at the moment. The results will be distributed early next week.

http://survey.usuite.com/survey/7f801dd05f3742619b046cc119c15106.sur

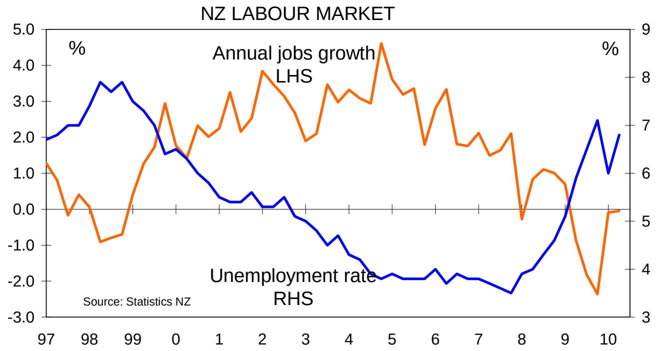
The main piece of news telling us something relevant about the state of and prospects for the NZ economy this week appeared this morning in the form of the quarterly Household Labour Force Survey. This survey has nothing to do with the number of people on the dole and instead results from a survey of about 8,000 people all over the country asking them if they have a job and what it is, and if they don't have a job why not and are they actively looking for one. In that regard it is largely directly comparable with other surveys overseas and is completely unaffected by whether people get the unemployment benefit or sickness benefit.

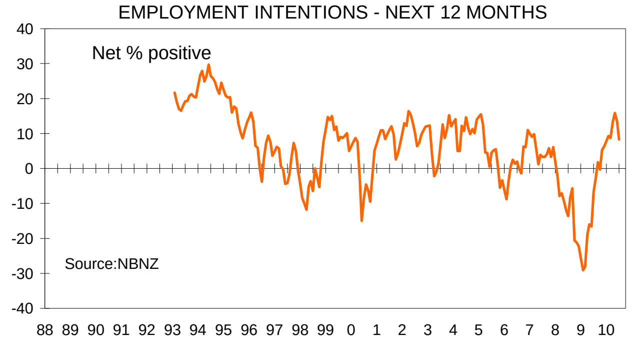
When the March quarter survey was released three months ago it showed far stronger jobs growth than expected and a fall in the unemployment rate to 6% from 7.1%, leading to some wariness about the data and an expectation that today's result would give back some of that good news as it were. And it did. During the June quarter the unemployment rate jumped back up to 6.8% courtesy of the March quarter jobs growth of 21,000 people turning into a decline of 6,000 for the June quarter.

That 0.3% fall was well away from market expectations of a 0.4% rise and the unemployment rate higher than general forecasts of a 6.4% rate and the Reserve Bank's 6% forecast. In that regard the outcome takes some of the heat off the Reserve Bank to continue hastily raising interest rates and increases the chances of a pause later this year. But given the volatility which has appeared in the Household Labour Force Survey in recent years we are not reading the June quarter results as a sign that there is a fresh deterioration underway in the labour market. In fact hours worked rose 0.6% after rising 1.3% in the March quarter so people are working longer.

The anecdotes are also quite strong regarding labour demand and other measures give more cause for hope. The NBNZ Business Outlook survey for July for instance showed that a net 8% of businesses expect boosting hiring compared with a ten year average reading of just 3%.

Also, the bulk of the June quarter surveying was done two and a half months ago and since then we think the labour market has improved.

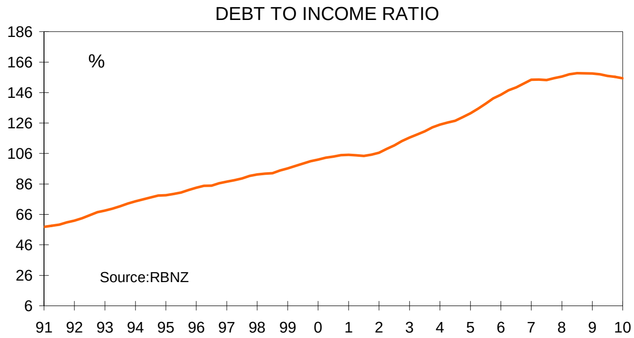


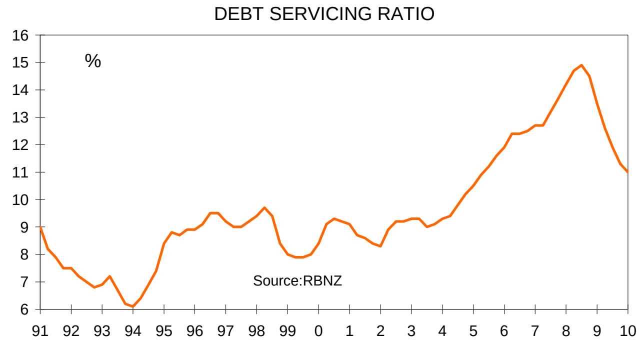


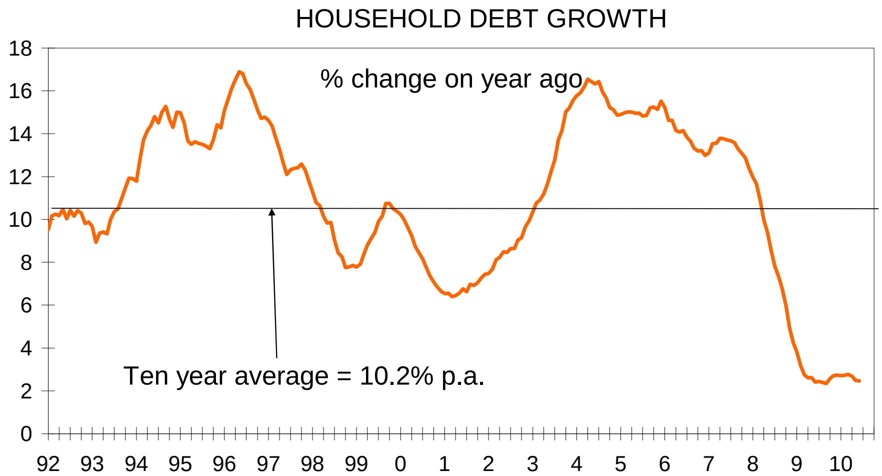
Nevertheless, today's result was worse than market expectations and has led to some pulling back in the currency and wholesale interest rates.

Little Borrowing Occurring

Not this week but last week the Reserve Bank released the monthly lending numbers and they show that debt repayment is the priority for most of us. In the household sector debt in seasonally adjusted terms rose by only 0.2% for the third month in a row. Compared with a year ago debt was ahead just 2.5%. Given that other data released this week showed that household incomes roughly rose 4.6% in the June quarter on a year ago for wage and salary earners one can reasonably conclude that the household debt to income ratio is continuing the downward movement which started in the December quarter of 2008.



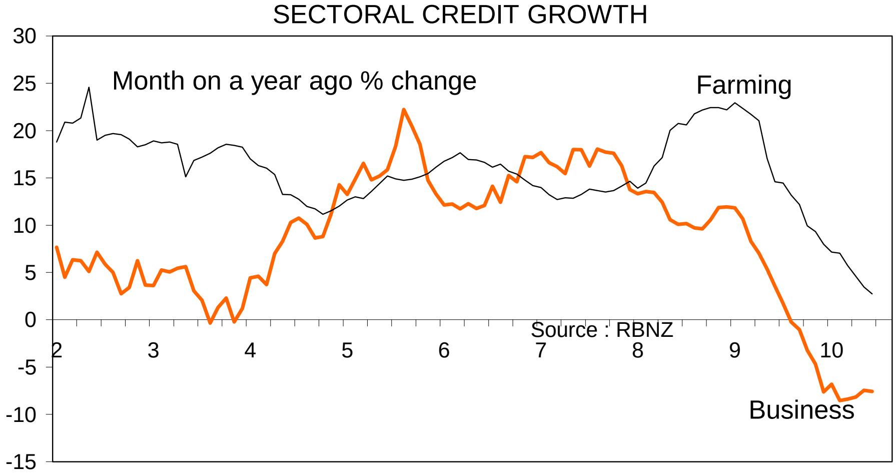




Long may this trend continue. In fact one of the best things that could happen this cycle is that as the Reserve Bank takes away below average interest rates people react quite strongly by borrowing and spending even less. This will not be good for retailing but will start to reduce New Zealand's draw upon the savings of foreigners to fund our day to day lives.

As importantly, the more reluctant we are to borrow as householders the less the Reserve Bank will need to raise interest rates and therefore the less the upward pressure on the currency on average as rates rise and the lower on average the cost of debt funding to the business sector.

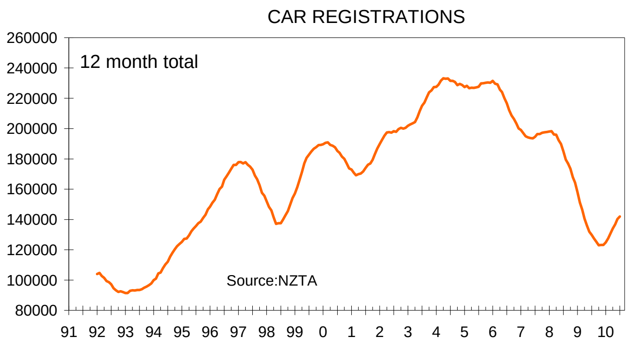
Not that businesses are taking advantage of the low interest rates around at the moment by borrowing. In June the level of business debt was down by 7.6% from a year earlier. However looking at things on a more up to date basis there is some levelling out underway. In the June quarter business debt fell $582m. But a year ago the decline was $1.3bn.

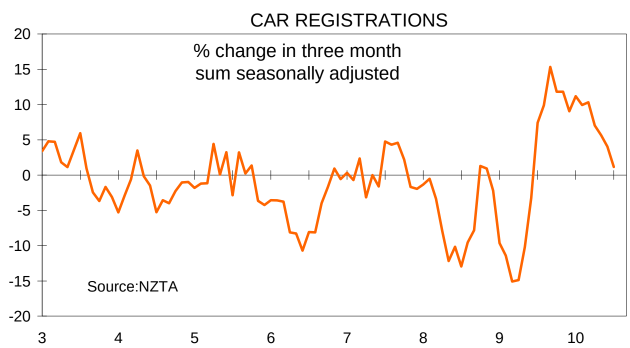


In the farming sector debt at the end of June was up just 2.7% from a year ago but looking at the monthly numbers it seems the level of debt has been essentially flat since about September last year. In the June quarter farm debt grew $47mn compared with $1.4bn in the June quarter of 2009 and $3.5bn two years ago. That is quite a massive change.

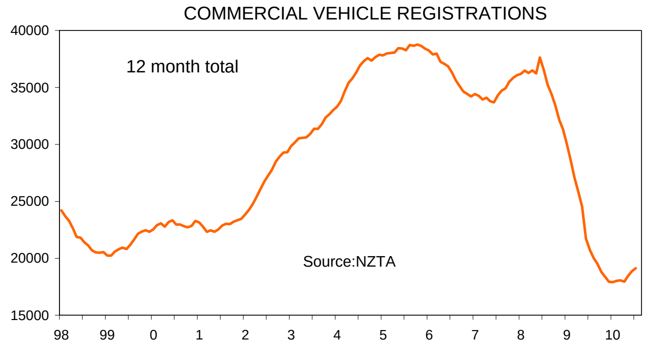
Vehicle Registrations Mixed

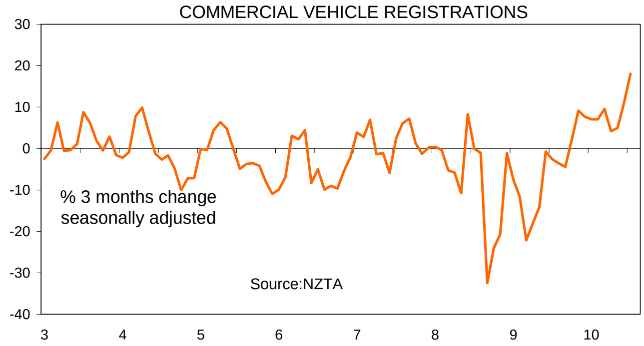
We like to report on the monthly vehicle registration numbers when they are released because they give the earliest solid insight into business and consumer spending. So here goes. In July there were 12,339 cars registered around New Zealand which was a 16% gain from a year ago. The three month change from a year ago was a 27% gain and seasonally adjusted compared with the three months to April the gain was 1.1%. There is growth but it is quite mild and becoming more in line with other weak retail spending indicators than the car rego numbers were a few months ago when they were rising quite rapidly. In other words – no early sign of a consumer spending surge.



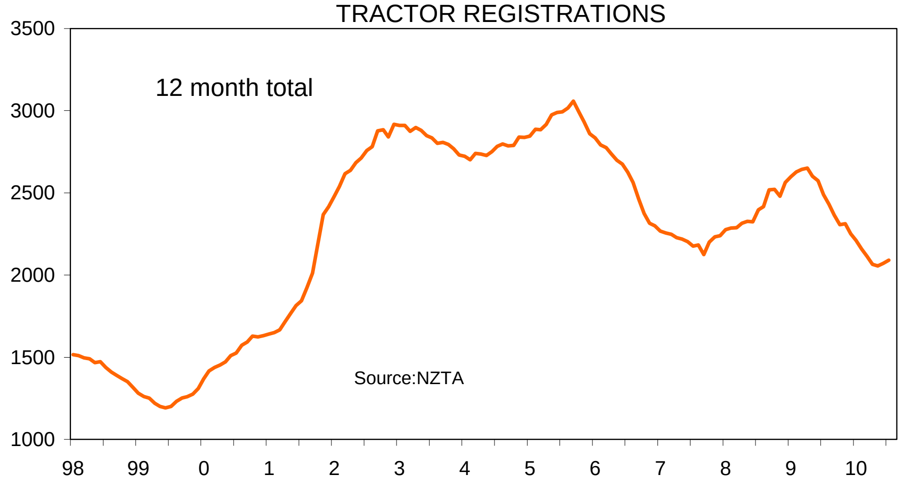


The number of commercial vehicles registered in July came in at 1,726 which was a rise of 19% from a year ago and fall for the entire year of 8%. For the three months to July seasonally adjusted growth was 18% so there is quite a strong recovery underway in this early indicator of business investment. Hopefully this will continue.





And finally in July there were 152 tractors registered around the country which was a 15% rise from a year ago and 16% fall for the entire year. In the three months to July tractor regos were up 6% from a year ago and 4% seasonally adjusted from the previous quarter. There is a growth but it is weak and from a low base. Not as low as the last recession however.



INTEREST RATES

This mornings labour market numbers came in lower than expected and taken in conjunction with an expected cut in Fonterra's forecast payout wholesale interest rates have pulled back this week. The one year swap rate has edged lower to 3.65% from 3.75% last week and the same a month ago. The three year rate has fallen to 4.25% from 4.4% last week and 4.48% a month ago. And the five year rate has eased to 4.64% from 4.76% last week and 4.9% a month ago.

The five year rate has now rallied by 1.1% from the peak back in November when there was quite high confidence in the world economy, some fairly positive indicators in the NZ economy, and few worries as yet about Europe. Since then while world growth prospects remain firm and have in fact been upgraded, investors have been scared by the Europe troubles and moved more assets into longer term debt in expectation major central banks will not be able to raise their cash rates as early as previously thought. Here in New Zealand the economic data has eased off and there is more talk of the RBNZ taking a pause in its monetary policy tightening.

But we still see the economy growing near 3.5% next year with increasing capacity issues due to low business capital spending and the labour market tightening we anticipate over the coming 18 months. That means we think the markets are underestimating future official cash rate rises and in fact the current levels of swap rates imply a peak for the cash rate under 4%. That seems quite unlikely. So borrowers may want to take advantage of the swaps rates rally to get some extra long term fixed rate hedging in place.

Key Forecasts

- Tightening through to mid-2012.

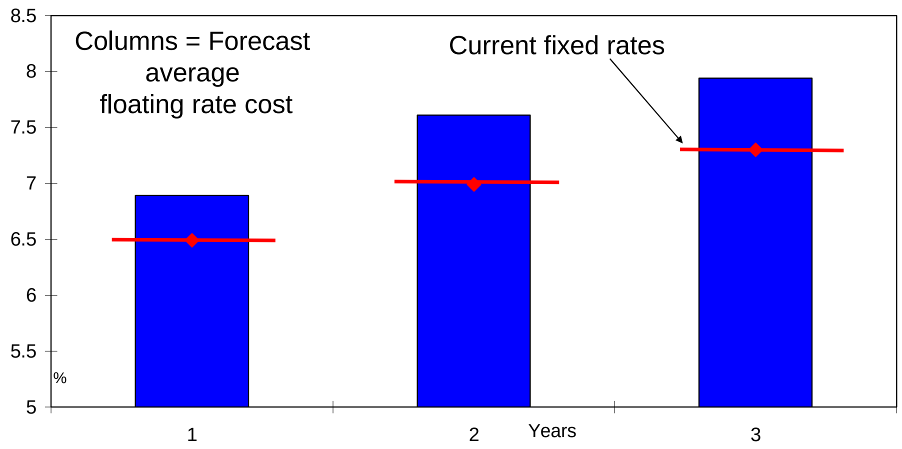
FINANCIAL MARKETS DATA	This week	Week ago	4 wks ago	3 months ago	Yr ago	10 yr average
Official Cash Rate	3.00%	2.75	2.50	2.50	2.50	5.9
90-day bank bill	3.30%	3.30	3.21	2.76	2.77	6.2
1 year swap	3.65%	3.75	3.75	3.79	3.10	6.3
5 year swap	4.64%	4.76	4.90	5.44	5.42	6.6
180-day term depo	4.10%*	4.10	4.80	4.90	3.15	6.0
Five year term depo	6.75%	6.75	6.75	6.75	6.00	6.5
* 150 days = 5%						

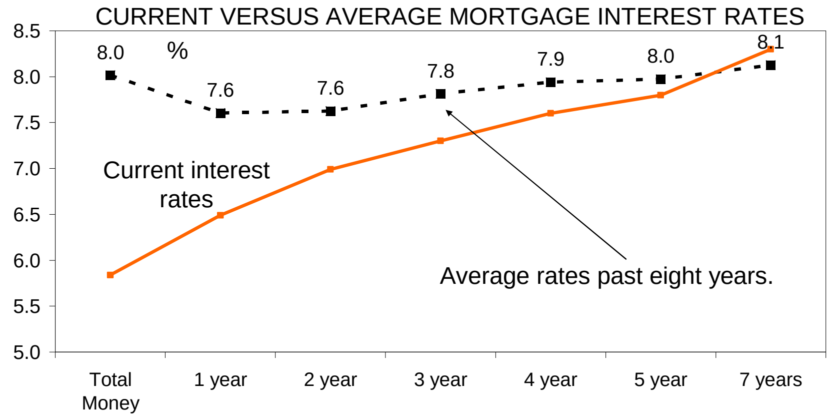
If I Were a Borrower What Would I Do?

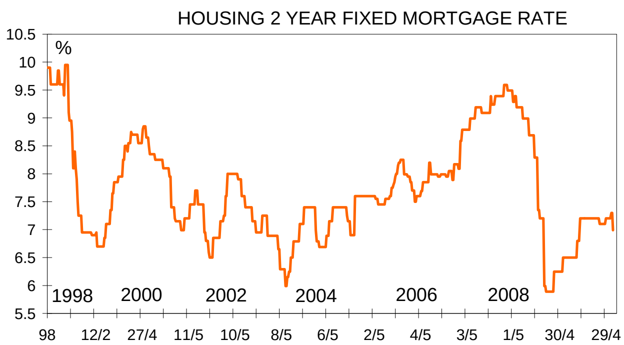
There is a new round of floating rate rises going through the market so the gap between those floating and fixed rates is falling. But the gap still exists and that means the expressed reluctance of borrowers to jump into a higher rate straight away in order to fix is likely to keep most people sitting on floating. Eventually a large number of people are likely to jump into fixed and when that happens the risk is the volume of movement causes a spike up in those fixed lending rates. That transition is not imminent but may happen early next year.

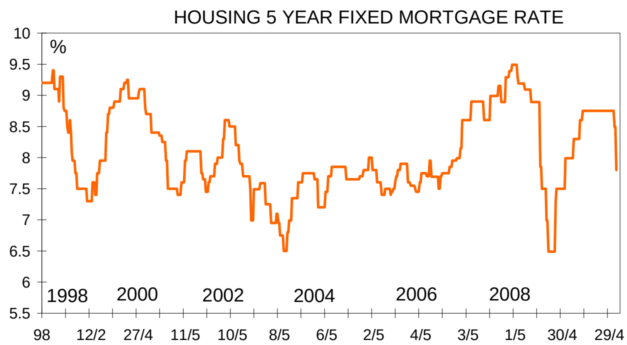
For myself I would still hop off floating into a two or three year fixed rate. Is it possible that with the labour market data this morning coming in worse than expected and wholesale rates rallying we will see another round of cuts in fixed rates which will in fact undermine the tightening the Reserve Bank is trying to achieve? The gap between those fixed housing rates and funding costs is still less than the gap just before the round of fixed rate cuts four weeks ago. So I don't think we will see reductions.

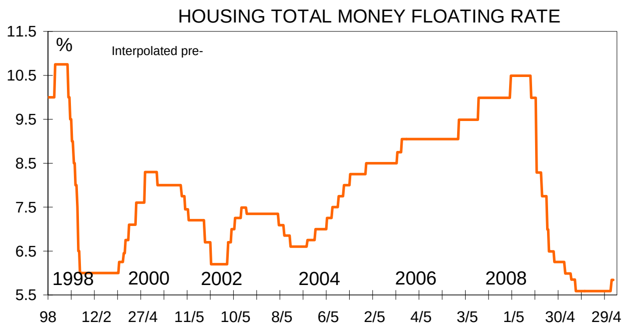
However. One cannot predict lender marketing initiatives and one could not rule out a bank deciding to offer a more competitive mid-term fixed rate to attract customers. I don't expect it but given that a rise in fixed rates again is unlikely in the very near future I would now hold off my switch into fixing for a week or two just in case someone offers me a deal.





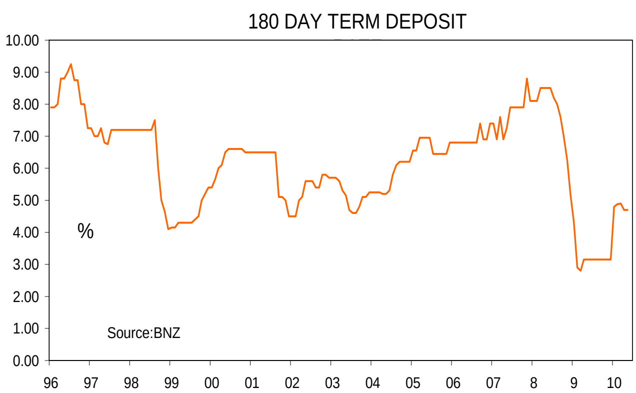


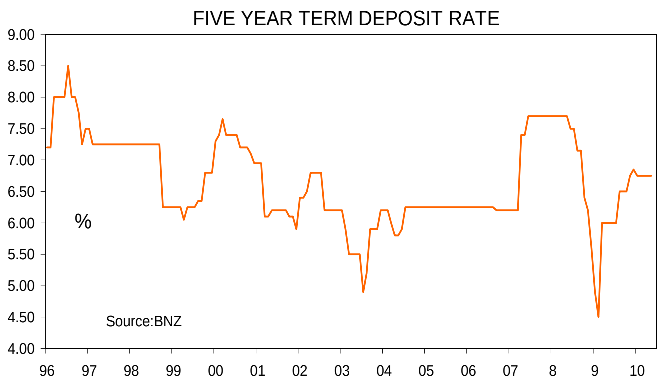




If I Were a Term Deposit Investor What Would I Do?

I would put most short term but some longer along the curve to improve the yield especially as now the pace at which the short rates will rise looks like being slower than earlier thought.



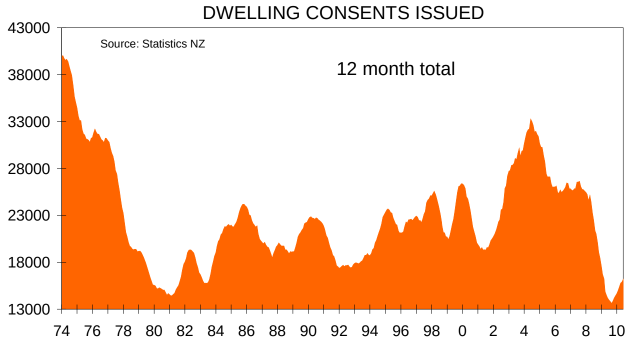


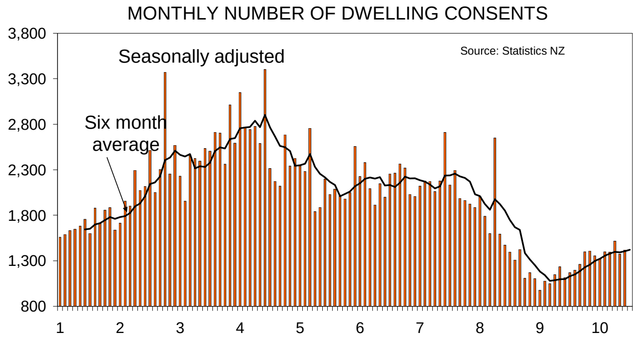
HOUSING MARKET UPDATE

Weak New Dwelling Construction

As we have been noting for some time now the level of residential construction in New Zealand is picking up. But it is starting from the lowest base in four decades and the strong view we have been running and will continue to run is that supply growth will be very constrained this cycle and because of that fundamental supply versus demand issues will both cushion prices (as has been the case for two years now) and cause them to edge back up slightly on average over 2011 with largest gains in the cities.

In June the seasonally adjusted number of consents issued for the construction of new dwellings increased by 3.5%. This rise followed a fall of 9.5% in May and means that over the June quarter consents were up just 4.7% from the March quarter. In unadjusted terms consent numbers for the quarter were ahead a good 24% from a year ago, but at 16,167 the annual number of consents was 33% below the ten year average and well below the 23,000 level calculated as necessary to meet population changes.

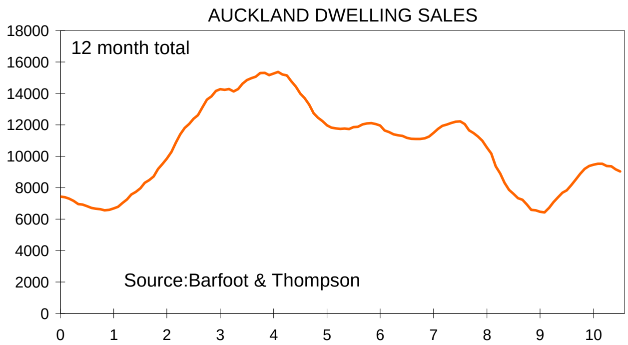


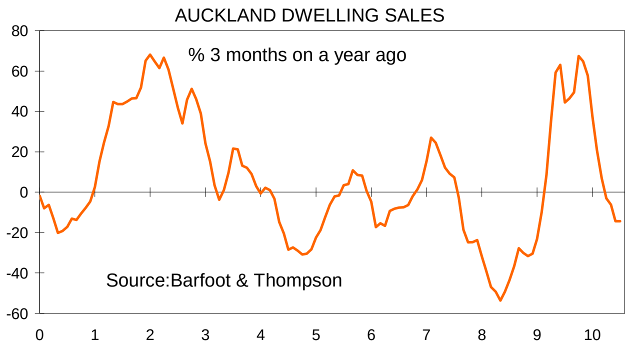


For the moment when there are a good number of sellers and weary buyers in the predominantly second hand dominated real estate market this situation of a growing housing shortage is not apparent. But come next year we expect more attention to go on this issue with some resulting pressure on councils and central government for public housing, and of course increased awareness from investors bringing greater rent gains across the price spectrum – probably more so at the lower end.

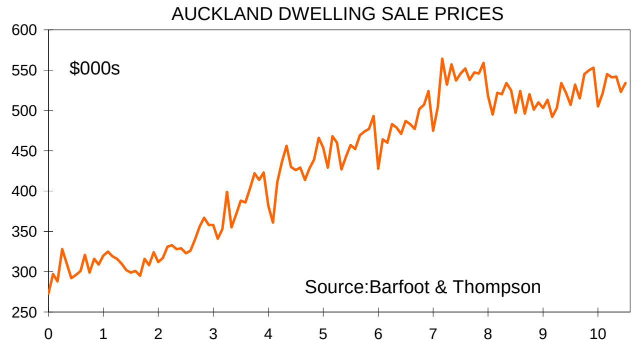
Monthly Auckland Data Flat

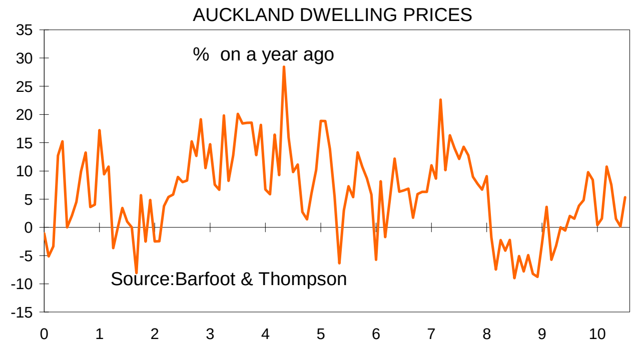
Barfoot and Thompson released the first truly decent measure of what residential real estate activity was like in July and the results are in a word uninteresting. In July they sold 644 dwellings. That was a 17% fall from a year ago and about a 1% fall seasonally adjusted from June. The three month seasonally adjusted change is a fall near 3% so activity is down slightly but not by much. Boring.



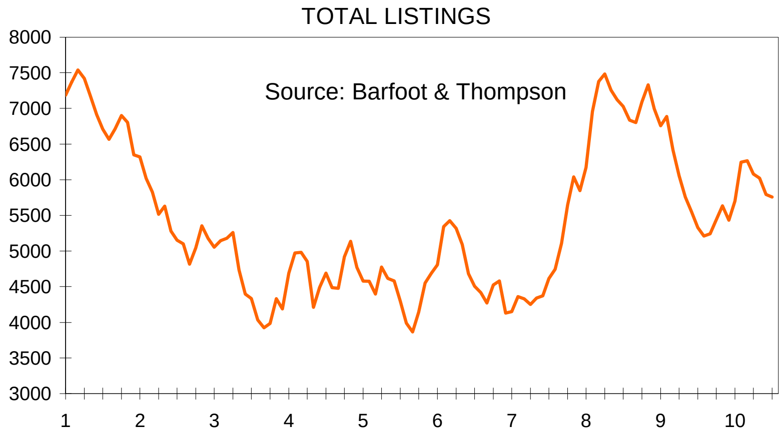


The average dwelling sale price rose to $534,000 from $523,000 but that month to month change is meaningless. Over the three months to July the average sales price was 2.3% ahead of a year ago and down just 0.5% from the three months to April. Boring.

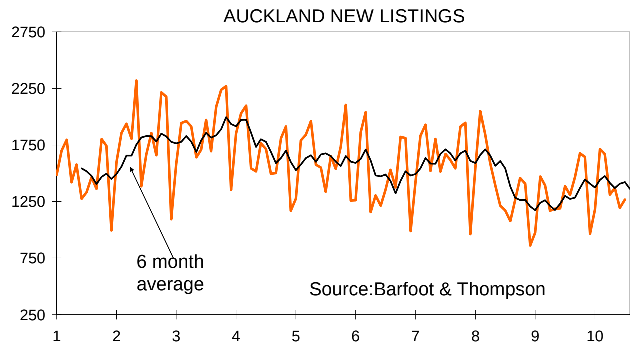


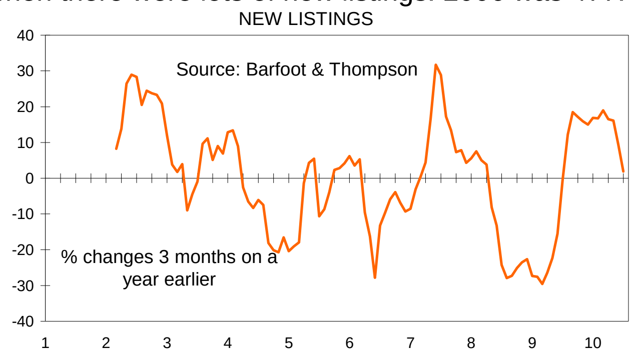


The number of properties on their books at the end of July stood at 5,759. This was an 8% rise from a year ago following 4% rises the previous two months. Compared with the end of June total listings were down 0.6% whereas in 2009 this month to month change was -4%, 2008 -1.3%, and 20075.5%. Nothing major there either. Boring.

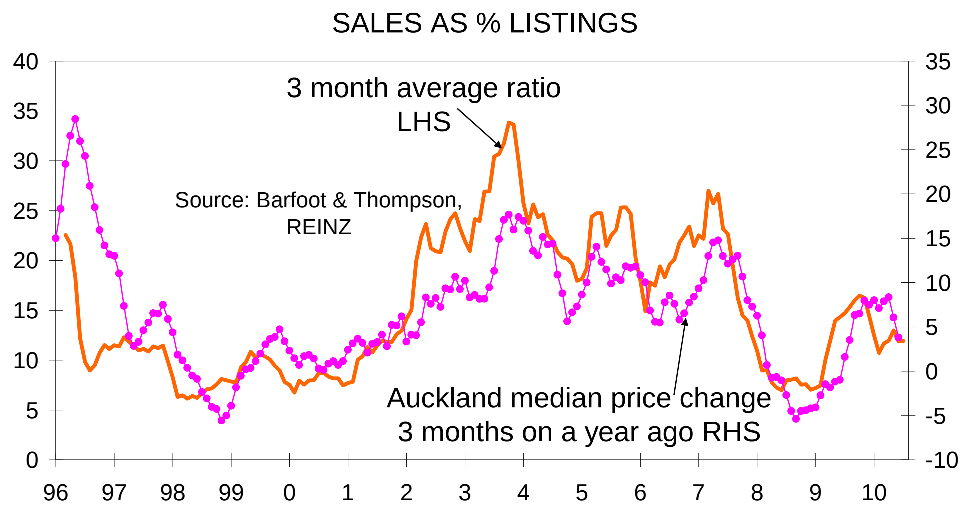


New listings received in July totalled 1,267. This was 8.6% down from new listings received in July 2009, but that month in 2009 showed a big jump over July 2008 of 18%. The number of fresh listings less actual sales in July came in at 623 (1,267 – 644) compared with a difference of 607 last year, 542 in 2008, and 772 in 2007. The only interesting year was therefore 2007 when there were lots of new listings. 2006 was 477.



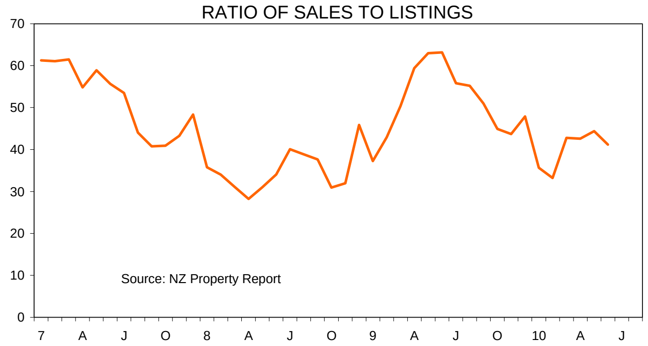


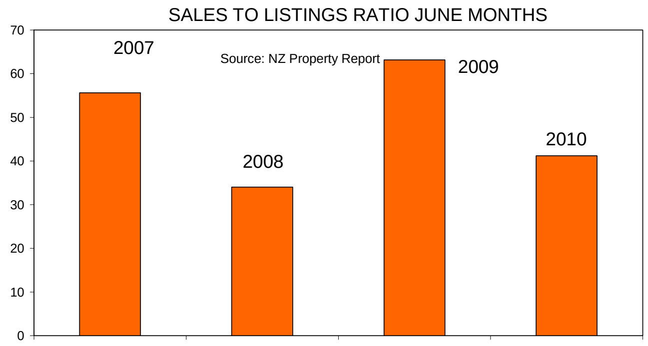
The housing market remains relatively static with slightly above average stock, flat prices, vendors only selling if they have to (just like farmers only selling if they really really need to), and buyers quite rightfully being picky. Nothing new and still no sign of investors dumping property – just an overhang we suspect which will keep the recovery in average prices next year due to supply issues relatively mild.



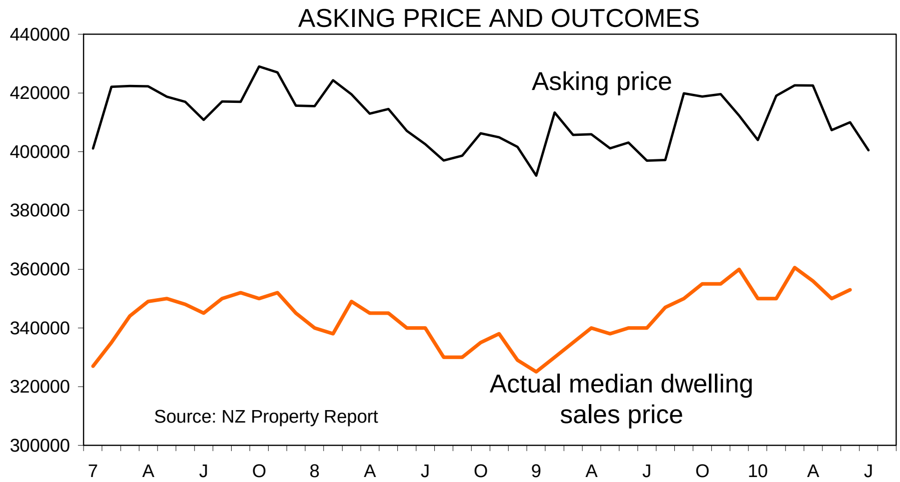
The monthly NZ property report was also released this week – compiled by the folk who run a key real estate listings website with what seems to be pretty good nationwide coverage. Their report shows that at the end of July there were 52,404 properties listed for sale and the average asking price was $400,481 which was down from $410,058 in June.

We struggle to glean anything truly significant from the report especially as for best insight one wants to be able to calculate a sales to listings ratio to get a feel for how firm the market may be, but we won't get July nationwide sales data for a couple of weeks. There are however hints that inventory remains high with the inventory measured in weeks using sales for the three months to June sitting at 46.8 weeks from 32.9 a year ago. But this number was down from 52 weeks two years ago, and up from 22.8 weeks three years ago. In other words there is a lot of volatility in there.





With regard to the monthly price measure one definitely wants to smooth things over a number of months and perhaps the best picture is gained by the graph below showing the level of the average asking price on a monthly basis. There is no clear trend in the measure and we see nothing strong enough to alter our view that average house prices are essentially flat at the moment. There remains however a risk of some temporary downward movement if we see investors chuck the properties they no longer want into a market where buyers know the power is in their hands. However there is as yet no indication that such a flood of property is coming.



Are You Seeing Something We Are Not?

If so, email us at tony.alexander@bnz.co.nz with Housing Comment in the Subject line and let us know.

Key Forecasts

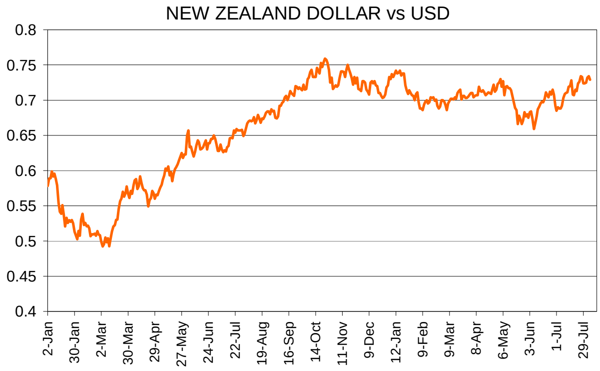
- Dwelling consent numbers to recover now with potentially good activity from late-2010.
- House prices edging higher after tax change effects wend their way through.

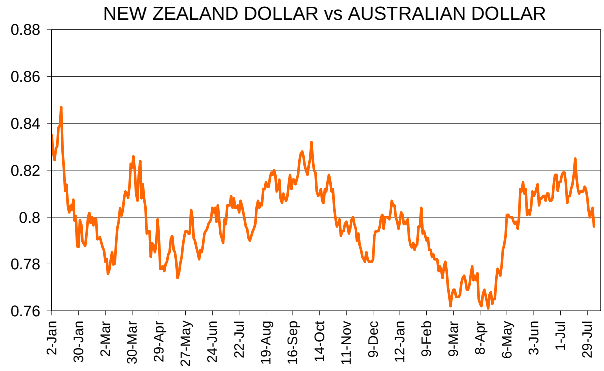
Exchange Rates & Foreign Economies

Exchange Rates	This Week	Week Ago	4 wks ago	3 mths ago	Yr ago	Consensus Frcsts yr ago*	10 yr average
NZD/USD	0.729	0.724	0.688	0.719	0.67	0.610	0.592
NZD/AUD	0.796	0.808	0.819	0.792	0.794	0.770	0.856
NZD/JPY	63.00	63.10	60.40	68.00	63.8	61.366	66.8
NZD/GBP	0.458	0.463	0.453	0.475	0.396	0.380	0.345
NZD/EUR	0.554	0.556	0.548	0.554	0.465	0.445	0.51
USD/JPY	86.42	87.15	87.79	94.56	95.24	100.600	113.9
USD/GBP	1.592	1.564	1.519	1.514	1.692	1.607	1.709
USD/EUR	1.316	1.302	1.255	1.298	1.441	1.372	1.156
AUD/USD	0.916	0.896	0.840	0.908	0.844	0.792	0.69

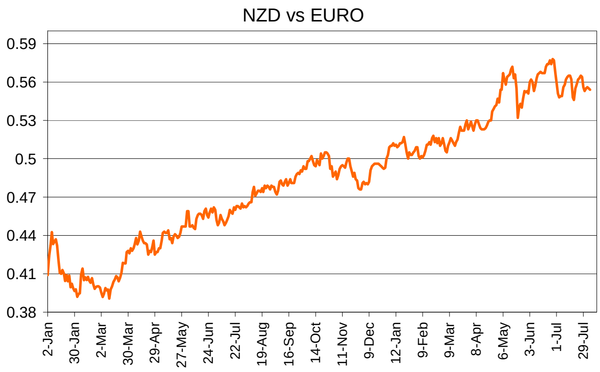
NZD Up – But Only Against The USD

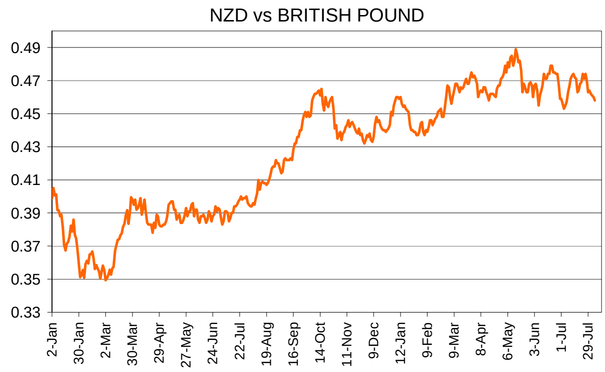
The Kiwi dollar has climbed against a weaker greenback this week to end today near 72.9 cents from 72.4 cents last Thursday. The currency has held up in spite of a call last week by the RB Governor for it to go down, a comment from the Finance Minister yesterday that the currency's level was unhelpful, the fall in dairy prices at Fonterra's monthly auction and announcement of a revision to come for this year's payout forecast, plus a creditwatch placed on Telecom's rating by Standard and Poors. And then there was this morning's weaker than expected employment data.



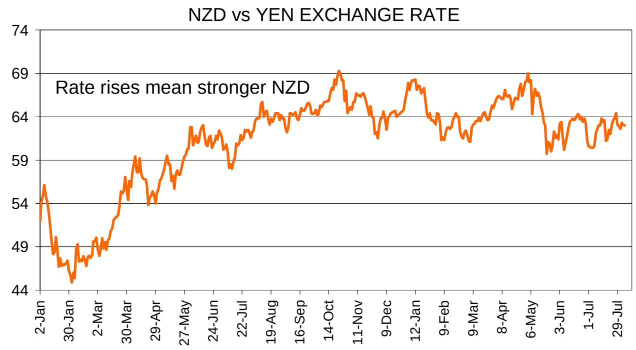


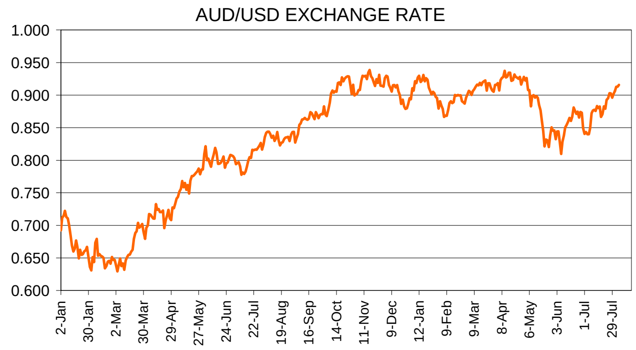
So why did the Kiwi dollar go up? As noted above one reason is that the greenback weakened slightly as investors too heart from some recent acceptable data around the planet to move investments back toward growth assets like shares, and risky assets like the far flung Kiwi dollar. In the process they sell greenbacks.





But looking at the cross rates one can see that the NZD has not received the normal level of support one would expect from a lift in investor risk tolerance. We have fallen to a near three month low against the Australian dollar near 79.6 cents while shedding small amounts on the other crosses. The Aussie dollar has risen two cents against the USD over the week buoyed by rising oil prices leading to purchases of other assets exposed to mineral price gains.





With monetary policy expectations in NZ likely to pull back a bit more following the employment data the risk for the NZD in the short term is some further downside movement. But with changes in investor risk tolerance impossible to forecast and that factor being a strong NZD influencer currently the coming week, month, quarter and year will bring whatever they bring. Volatility with upside risk as long as the world continues to look an acceptable place.

For more detailed commentaries from BNZ and the NAB group on foreign currencies, commodities, etc click on the following link.
https://research.bnz.co.nz/Research/Pages/default.aspx

*Sourced from Consensus Economics. http://www.consensuseconomics.com/

ECONOMIC DATA

All %		Latest qtr only	Previous qtr only	Latest year	Year ago	2 Yrs ago
Inflation	RBNZ target is 1% - 3% on average	0.3%	0.4	1.8	1.9	4.0
GDP growth	Average past 10 years = 2.6%	+0.6	0.9	-0.4	-1.4	2.8
Unemployment rate	Average past 10 years = 4.7%	6.8	6.0	......	5.9	4.0
Jobs growth	Average past 10 years = 2.0%	-0.3	1.0	0.0	-0.9	0.8
Current a/c deficit	Average past 10 years = 5.9% of GDP	2.4	2.9	......	7.9	7.8
Terms of Trade		5.8	-1.6	-8.2	1.8	8.8
Wages Growth	Stats NZ analytical series	0.4	0.8	2.7	5.4	5.0
Retail Sales ex-auto	Average past 9 years = 3.9%.	1.3	0.7	1.3	-0.6	2.8
House Prices	REINZ Stratified Index	0.7	-1.2	5.1	-5.0	-1.9
Net migration gain	Av. gain past 10 years = 13,900	+16,504	20,973yr	......	12,515	4,735
Tourism – an. av grth	10 year average growth = 3.2%. Stats NZ	3.8	4.2	3.8	-2.8	0.9
		Latest year rate	Prev mth year rate	6 mths ago	Year ago	2 yrs ago
Consumer conf.	10 year average = 3%. Colmar survey	46	36	57	3	-34
Business activity exps	10 year average = 19%. NBNZ	32	39	39	13	-8
Household debt	10 year average growth = 10.3%. RBNZ	2.5	2.7	2.7	2.6	9.4
Dwelling sales	10 year average growth = 2.5%. REINZ	-24.2	-17.2	15.2	40.3	-42.4
Floating Mort. Rate	(TotalMoney) 10 year average = 7.9%*	5.84	5.59	5.99	5.99	10.49
3 yr fixed hsg rate	10 year average = 7.8%	7.30	7.75	7.95	6.99	9.09

ECONOMIC FORECASTS

Forecasts at July 29 2010	March Years					December Years				
	2009	2010	2011	2012	2013	2008	2009	2010	2011	2012
GDP - annual average % change										
Private Consumption	-1.1	0.6	2.7	2	1.4	-0.3	-0.5	2.7	2.1	1.6
Government Consumption	4.2	1.4	2.7	1.4	0.9	4.8	1.6	3	1.4	1
Investment	-7.2	-9.5	4.5	5	3.3	-3.6	-12	2.2	5.9	2.9
GNE	-1.5	-3.2	5.2	2.3	1.7	0.4	-5	4.9	2.7	1.7
Exports	-3.4	2.9	2.4	6.4	2.4	-1.4	0	2.8	5.8	3.2
Imports	-4.7	-9.6	9.1	3.3	2.6	1.9	-14.9	9.5	3.6	2.9
GDP	-1.5	-0.4	3.2	3.2	1.6	-0.2	-1.6	2.8	3.4	1.7
Inflation – Consumers Price Index	3	2	4.5	2.8	2.6	3.4	2	4.3	2.7	2.6
Employment	0.7	-0.1	2.4	2.3	0.9	1	-2.4	2.6	2.9	0.8
Unemployment Rate %	5.1	6	5.7	4.9	5	4.6	7.1	6	4.9	5
Wages	5.1	1.6	2	3.6	3.4	5	3.1	1	3.2	3.5
EXCHANGE RATE ASSUMPTIONS										
NZD/USD	0.53	0.7	0.72	0.66	0.61	0.56	0.72	0.73	0.68	0.62
USD/JPY	98	91	99	105	105	91	90	97	103	105
EUR/USD	1.31	1.36	1.21	1.25	1.24	1.34	1.46	1.2	1.24	1.28
NZD/AUD	0.8	0.77	0.83	0.84	0.84	0.83	0.79	0.82	0.83	0.83
NZD/GBP	0.37	0.47	0.47	0.4	0.38	0.37	0.44	0.49	0.42	0.38
NZD/EUR	0.41	0.52	0.6	0.53	0.49	0.41	0.49	0.61	0.54	0.48
NZD/YEN	51.8	63.7	71.3	69.3	64.1	50.9	64.2	70.8	69.5	65.1
TWI	53.8	65.1	69.9	65.3	61.6	55.1	64.7	70.5	66.3	61.6
Official Cash Rate	3	2.5	4	5.5	5.25	5	2.5	3.75	5.25	5.5
90 Day Bank Bill Rate	3.24	2.67	4.15	5.65	5.4	5.23	2.78	3.95	5.57	5.65
10 year Govt. Bond	4.77	5.86	6.3	7	7.5	4.88	6.02	5.9	6.8	7.5

All actual data excluding interest & exchange rates sourced from Statistics NZ.

The BNZ Weekly Overview is prepared by Tony Alexander, Chief Economist at the Bank of New Zealand. Ph 04 474-6744.

*extrapolated back in time as TotalMoney started in 2007