

# 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.

<b>A Summary</b>	<b>1</b>	<b>Major Offshore Issues</b>	<b>5</b>
<b>Interest Rates</b>	<b>3</b>	<b>Foreign Exchange</b>	<b>7</b>
<b>Housing Market Update</b>	<b>4</b>		

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 please click here.

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## Busy. A Summary

This week I have been busy with the annual Japan New Zealand Business Council conference in Auckland plus compiling the monthly BNZ Confidence Survey and getting ready to release the results of the monthly BNZ-REINZ Residential Market Survey tomorrow. So I'll keep this week's Overview to the essentials – those being...

- Nothing has come along to change my view that the NZD will remain an elevated currency for a number of years.
- NZ growth will be very well underpinned for the next few years by a construction boom emanating from many sources and Asian growth assisting exports.
- The Reserve Bank's next monetary policy change will be a tightening in (current best guess) a year's time but before then I would keep an eye out for an attractive long term fixed rate and lock in a goodly portion of my mortgage.
- House prices will rise, especially in Auckland, because of a shortage of stock (same story there for many years).
- Farmland prices will also rise and the dairy sector continue to expand due to investors seeking exposure to the sector on the back of long term product demand out of Asia.
- The NZ labour market will tighten up rapidly from mid-2013 causing problems for firms without developed access to foreign and ex-pat people.
- The net migration flow for NZ will turn positive in a few months and settle firmly into positive territory for many years on the back of three long term trends of the cycle with Australia turning, UK and European people escaping an expected extended period of woe over there, and rising Asian middle class size boosting numbers shifting here – and on top of that there is the boost from builders coming in to rebuild Christchurch.
- New Zealand's income per capita growth is constrained not by rules and institutions but our Kiwi-centric culture and poor connectivity with foreign scientists, managers, capitalists, policy-makers, and entrepreneurs.

Just briefly on the JNZBC Conference. I gave an update on the NZ economy and a Japanese speaker gave an update on Japan's economy and as always happens there was quite a stark difference between the topics we dealt with. As with my approach here and in talks the focus was on the broad economic trends with people being invited to place their own interpretation on the relative strength of the positives and negatives. The talk from the Japan side however gave as always primary emphasis to foreign direct investment flows out of Japan and the earnings of Japanese businesses in other countries.

This focus on investment in other countries is near completely lacking in New Zealand. We still think of engagement with foreign countries as meaning we make something and ship it over to them. Our thinking about NZ business investment overseas runs along the lines of jobs being shipped out rather than opportunities and profits being created by improving the linkages between our economy and economies overseas. That is what is lacking for NZ – our linkages. We emphasise a precious stand-off relationship and have reluctance to get engaged in the messy details of foreign investment.

That myopic attitude toward international economic relations is seen also in the way we feel about foreign investment here. Rather than thinking about how we will take the capital freed up by a foreign purchase of an NZ company and invest it in overseas businesses we bemoan the selling of the Kiwi investor, envy them for the spare cash they will now have to buy better cars and more TVs, and worry about the influence which foreigners will have on our lives.

Until our attitude toward investment engagement with foreign entities and countries changes we will not overcome the key factor which prevents us rising back up the OECD income per capita ladder and offering better income earning career prospects for our young people than they can find in Australia – our poor global connectivity.

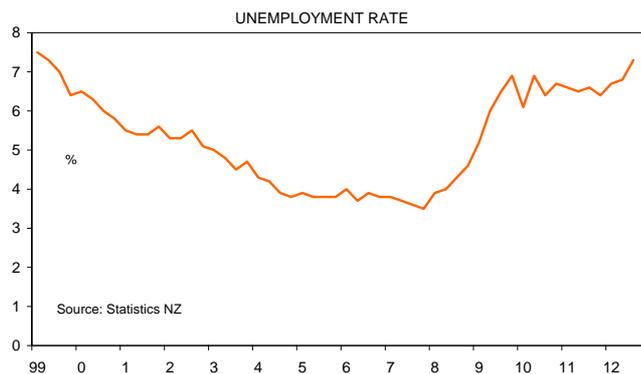
That connectivity is something pursued every year and in an ongoing basis at the company level by members of the JNZBC, and it was interesting to note that this year there was a slightly different tone to proceedings. More comments were dropped into speeches regarding taking NZ innovation overseas with Japanese companies with connectivity providing pathways for our developments to do more than just make us feel happy about our inventiveness and maybe make us a few million dollars before we sell the entire company to a US buyer who ships it out.

### **US Presidential Election**

There is zero chance that I can write anything here insightful about the US election which you will not have already seen and heard elsewhere. But for the record lets just note that Mr Obama's victory was bigger than expected but the challenge still remains of how to work with Republican-dominated House of Representatives which vehemently rejects what they perceive as the creeping socialism of Mr Obama. There is a risk that movement toward a deficit-solving fiscal package will be very bumpy and credit rating agency Fitch have already warned that they may downgrade their rating of US government debt if progress to reduce the huge US deficit over \$1.1tn is not quickly made. We should expect bumps in the financial markets over the next few weeks and months.

### **Weak NZ Labour Market**

NZ job numbers fell 8,000 or by 0.5% during the September quarter and the unemployment rate jumped from 6.8% to 7.3%. This is the highest unemployment rate since 1999 and the result shows yet again that good business employment intentions are not feeding through into actual hiring though this will come in the context of the coming construction boom which will highlight some glaring skills shortages – eventually, not yet.



## INTEREST RATES

The drift in wholesale interest rates for the moment is mildly upward with better data coming out of the United States and China, the mild tightening bias shown by the new RBNZ Governor compared with the previous one who oversaw inflation at an average of 2.7%, and this week’s decision by the RBA to leave the Australian cash rate unchanged at 3.5% rather than cutting it as the markets had expected.

Australia is interesting in that the RBA quite frequently does not undertake actions factored into market prices so people are kept on their toes. In contrast here in New Zealand it is very rare for the RBNZ to act out of expected character. Given that the element of surprise is a small tool available to central bankers maybe the new Governor wants to think about the predictability of his organisation a tad and how it weakens policy effectiveness – at the margin.

Rates rose this week as shown below and one might start to wonder if this is a structural lift in wholesale borrowing costs rather than just a fluctuation within recent ranges given the drift of sentiment toward the positive in the US and China. However this morning’s far worse than expected job numbers show that our domestic economy is weak and one cannot reasonably yet expect much strength in retail spending though this will eventually come in the context of the construction boom. So rates rallied to end largely where they were a week ago.

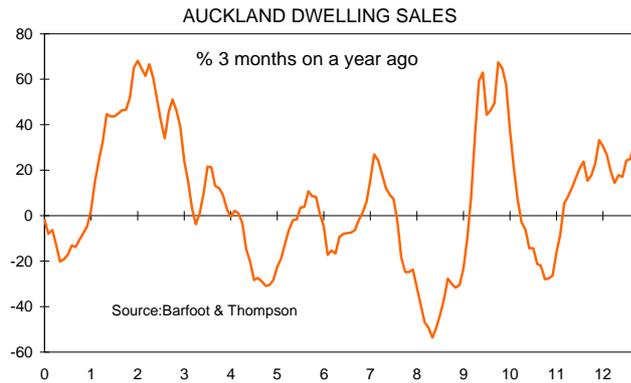
FINANCIAL MARKETS DATA						
	<b>This week</b>	<b>Week ago</b>	<b>4 wks ago</b>	<b>3 months ago</b>	<b>Yr ago</b>	<b>10 yr average</b>
Official Cash Rate	2.50%	2.50	2.50	2.50	2.50	5.4
90-day bank bill	2.67%	2.67	2.66	2.67	2.76	5.7
1 year swap	2.62%	2.63	2.60	2.66	2.92	5.8
3 year swap	2.84%	2.82	2.82	2.85	3.36	6.1
5 year swap	3.14%	3.11	3.11	3.27	3.97	6.3

# HOUSING MARKET UPDATE

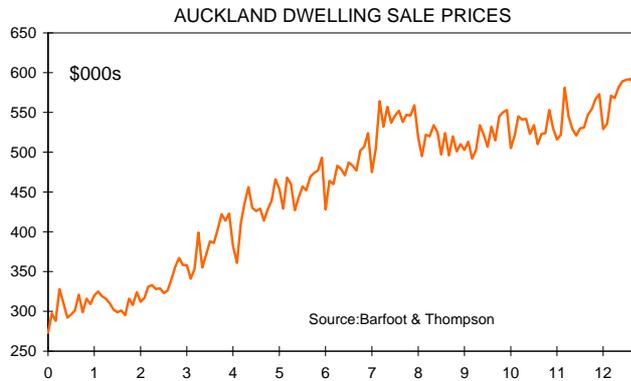
- To view the most recent results of our monthly BNZ-REINZ Residential Market Survey click here. <http://tonyalexander.co.nz/bnz-reinz-survey/>
- I also write a monthly column on the residential property market in NZ Property Investor magazine available at your bookshop or newsagent.

## Auckland Strong

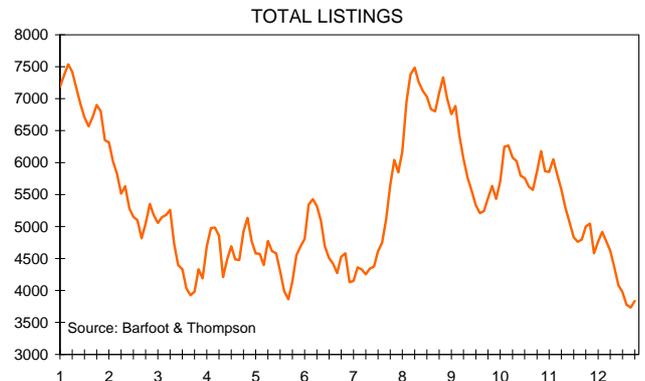
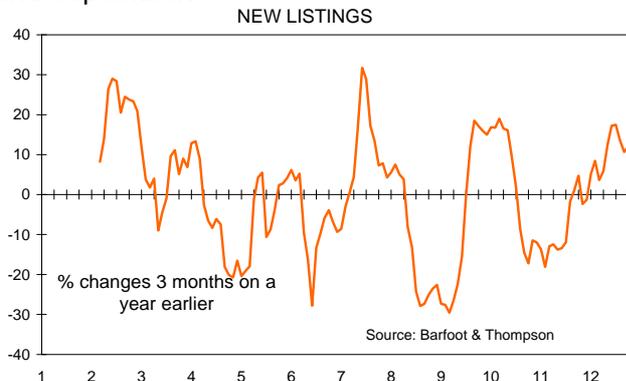
Barfoot and Thompson released their monthly numbers for Auckland residential real estate activity this week and there is nothing in the release to challenge my long term view that Auckland has a listings shortage with prices going up. The number of sales in October was ahead almost 50% from a year ago and up over 10% in seasonally adjusted terms from September. Sales have risen by 26% over the entire 12 month period.



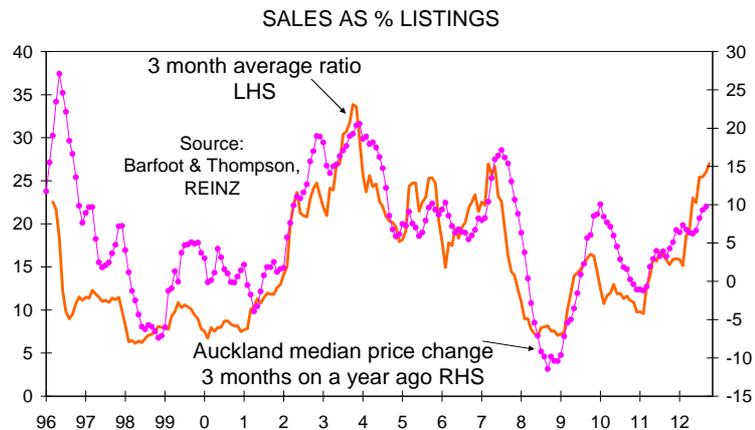
The average sale price climbed above \$600,000 for the first time due partly to high sales of houses over \$1m. The average price was \$619,000 compared with \$585,000 in September.



The number of new listings received during the month was ahead a good 25% from a year ago, but the stock of listings at 3,835 was down 23% from a year ago and the third lowest total in the past decade after August and September.



As a result, the ratio of sales to listings over the past three months has risen to the highest level since a brief spike in March 2005 and before that late-2003. A rise in this ratio is associated with accelerating house price inflation.



Read the Housing Section in the November 1 Weekly Overview for a list of 19 reasons why Auckland house prices will keep rising.

<http://tonyalexander.co.nz/wp-content/uploads/2012/11/WONovember-1.pdf>

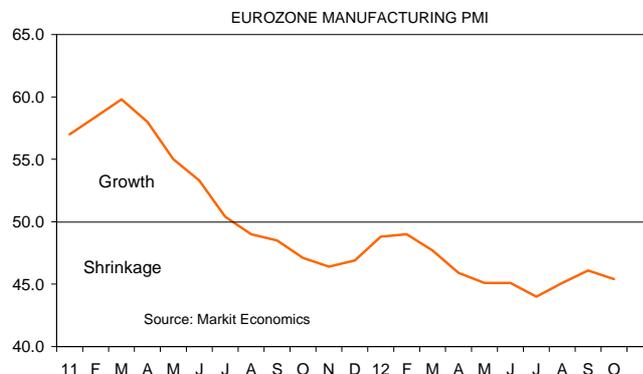
## If I Were A Borrower What Would I Do?

Stay floating for now but keep an eye out for any discounted long term fixed rates. At some stage the United States outlook will look good enough that the markets will start talking about the Federal Reserve raising the funds rate ahead of the mid-2015 timing the Chairman has indicated. Triggers will be getting a plan in place to smoothly reduce the US fiscal deficit, plus better growth in China and backing away from the European collapse scenario. We are not there yet.

## MAJOR OFFSHORE ISSUES

### Europe

Whereas during the week we learnt that manufacturing measures improved in the United States and China, in Europe the PMI got worse. It fell in October to a reading of 45.4 from 46.1 in September. In fact not only did the index fall it sits at a very low level signaling a fair degree of contraction in EU manufacturing output.

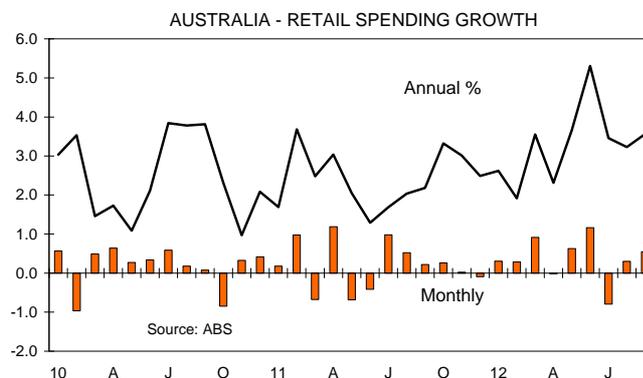


The European Commission this week cut its forecasts for Euro-zone growth in 2013 to just 0.1% from a 1% prediction back in May with Germany's growth forecast cut to 0.8% from 1.7% and only 0.4% growth forecast for France. Spain is forecast to shrink 1.4% and the budget deficit to blow out to 6% in 2013 then

6.4% in 2014. Growth this year of only 0.4% is expected but improvement to 1.4% is predicted for 2014. Essentially there is no growth in the Euro-zone expected for the coming year and risks still seem to lie on the downside with more rioting in Greece over spending cuts and removal of privilege accorded to so many people in the past decade who never deserved it on the basis of the Greek economy's performance. Greeks still don't want the party others paid for to end and as they drag their heels on matching expenditure to their inefficiently generated income social strains just get worse and worse.

## Australia

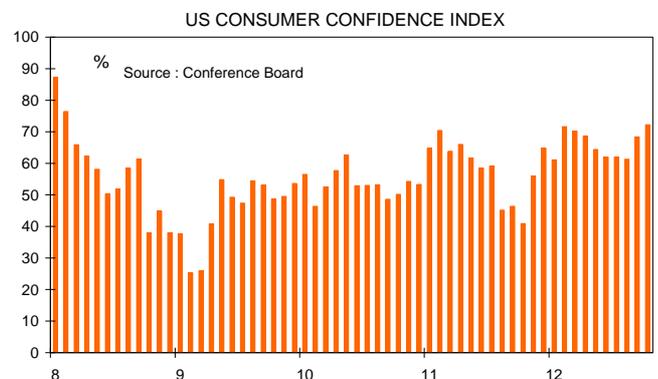
A small bit of strength returned to the retailing sector in Australia with sales rising 0.5% in September after gaining just 0.3% in August and falling 0.8% in July. Sales are running 3.6% ahead of a year ago adjusted for price and show that reasonable growth is occurring – though this is unlikely to be enough to prevent more rationalization in a sector which like so many others has some strong parts in Western Australia but gross weakness elsewhere.



Out of Australia recently we have seen some generally downbeat comments associated with weakness in prices for coal and iron ore due to the slowdown in China's rate of economic growth. However as the retail sale numbers show there is good life left in the economy, and this was revealed also in a quarterly survey by Dunn and Bradstreet. It found that one in three Australian businesses plan making long term investments soon. In fact its capital investment index sits at a reading of 20 which is well above the long term average of just 6.

## United States

This week's data news got off to a good start for the United States with news last Thursday night that the ISM index for the manufacturing sector rose to 51.7 in October from 51.5 in September. The index has now risen for three months in a row and feeds into an argument that underlying growth in the US economy is improving, though the pace is not particularly strong.



A second piece of good news was evidence that the improving labour market may be making consumers feel happier with the Conference Board monthly sentiment gauge rising to a reading in October of 72.2 from 68.4 in September. This is still well below the average level since the 1960s of 93 but is the strongest

reading since February 2008 and therefore quite interesting to ponder. Then on Friday night we learnt that job numbers in October rose by a stronger than expected 171,000 with earlier months also revised upward.



The ISM services sector reading however fell in October but remained in positive territory with a reading of 54.2 from 55.1 in September.

### China

You can find my China page on Facebook at <http://www.facebook.com/TonyAlexanderNZ> I have set up this page specifically for discussing the NZ-China relationship and as a tool for disseminating information and furthering my own still inadequate knowledge.

## Exchange Rates

Exchange Rates	This Week	Week ago	4 wks ago	3 Mths ago	Yr ago	10 yr average
NZD/USD	0.817	0.822	0.818	0.815	0.796	0.67
NZD/AUD	0.785	0.794	0.804	0.772	0.767	0.85
NZD/JPY	65.2	65.6	64.3	64.1	62.1	69.6
NZD/GBP	0.511	0.51	0.507	0.522	0.496	0.388
NZD/EUR	0.64	0.634	0.627	0.658	0.578	0.52
NZDCNY	5.13	5.13	5.18	5.19	5.06	4.99
USD/JPY	79.80	79.81	78.61	78.65	78.02	105.7
USD/GBP	1.60	1.61	1.61	1.56	1.60	1.72
USD/EUR	1.28	1.30	1.30	1.24	1.38	1.28
AUD/USD	1.04	1.04	1.02	1.06	1.04	0.788
USD/RMB	6.2755	6.2373	6.3304	6.3677	6.351	7.56

### NZD Well Underpinned

As long as money printing continues in Japan, the United States, Europe, the UK and Switzerland (and there is no sign of it slowing let alone ending) then the natural bias for other currencies is that they rise. Now throw in NZ export commodity prices which have risen for three months in a row, more recent upward creepage in global dairy prices, and the eventually interest rate rising inflation lift to come from the arriving construction boom in NZ and one can easily paint of picture of the NZD at US 85 cents in a few weeks time. Then higher after that but no-one really wants to start talking about the big nine figure just yet.

This week the Euro fell following weak growth projections from the European Commission and rioting in Greece. The US dollar weakened because of expectations that the Fed. will keep turning the money presses. The Yen weakened because of deepening political and economic worries with rising expectations of intervention by the Bank of Japan and more money printing to get the Yen lower and help exporters. The

## BNZ WEEKLY OVERVIEW

AUD on the other hand rose because the RBA failed to meet expectations this week when it left its cash rate unchanged at 3.5% rather than cutting it.

With these developments underway the NZD initially rose against all bar the AUD. But following this morning's weaker than expected NZ employment data the NZD has pulled back (temporarily) to finish a tad lower than last week.



### Key Forecasts

Dec. year		2011	2012	2013	2014
GDP	annual average chg	1.4	2.0-3.0%	2.0 – 2.5	1.0 – 2.0
CPI	on year ago	1.8	1.8	2.2 - 2.9	2.5 – 3.5
Official Cash rate	end year	2.5	2.5	2.5 – 2.75	2.75 – 425
Employment	on year ago	1.6	0.0 – 0.5	1.0 – 2.0	0.5 – 1.5
Unemployment Rate	end year	6.4	6.5 – 7.0	5.5 – 6.0	5.0 – 5.6

The Weekly Overview is written by Tony Alexander, Chief Economist at the Bank of New Zealand. The publication is sent to 27,000 subscribers each week and is one of a stable of regular releases which include the

- monthly Growing With China publication, <http://tonyalexander.co.nz/topics/china/>

## BNZ WEEKLY OVERVIEW

- monthly BNZ Confidence Survey, <http://tonyalexander.co.nz/topics/surveys/bnz-confidence-survey/> and the
- monthly BNZ-REINZ Residential Market Survey. <http://tonyalexander.co.nz/topics/surveys/bnz-reinz-survey/> This latter survey provides information from a survey of over 10,000 licensed real estate agents on the current state of the residential property market in New Zealand.
- He has also written a weekly newspaper column since 1998, search [www.stuff.co.nz](http://www.stuff.co.nz)
- produces a monthly column for the NZ Property Investor magazine, <http://www.propertyinvestor.co.nz/> and
- writes a monthly column for the NZ China Trade Association. <http://www.nzcta.co.nz/>
- Most of these publications plus research into impediments to NZ's economic growth are available on his website. [www.tonyalexander.co.nz](http://www.tonyalexander.co.nz)
- Discussion of New Zealand's relationship with China can be found here. [www.facebook.com/TonyAlexanderNZ](http://www.facebook.com/TonyAlexanderNZ)

Tony Alexander has been Chief Economist at the BNZ since 1994 and apart from publications and advising management spends considerable time on the road around New Zealand making presentations and speaking with the media. He travels to the UK and Europe twice a year to assess economic conditions and present at numerous functions, has five children, tramps, and his partner Dr Sarah Farquhar runs the early childhood education network [www.childforum.com](http://www.childforum.com)



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