ANZ Research

New Zealand Weekly Data Wrap

28 January 2022

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Contact us

See page 4.

Forecast updates

Recent ANZ NZ Forecast Updates can be found here.

- NZ OCR Call Change: 3% by April 2023
- NZ Property Focus: On the house
- NZ Economic Outlook: Red light/green light
- NZ Forecast Update: Farmgate milk price forecast revised up

Our other recent publications are on page 2.

What's the view?

- GDP constrained by supply more than demand
- Labour market tighter than ever, and very inflationary
- Inflation way above target
- Further OCR hikes towards 3.0% by April 2023 needed to contain inflation

Our forecasts are on page 3.

Key risks to our view

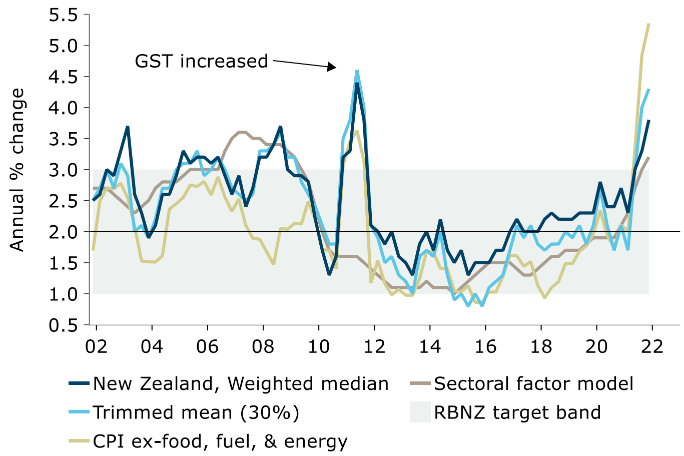
- Falling consumer and business sentiment derail momentum.
- Falling house prices could have a more significant impact on the economy than expected.
- Surging costs, inflation expectations, and highly inflationary labour market could be hard to rein in.
- Omicron outbreak causes severe disruption and shortages.

What happened this week?

At 5.9%, Q4's annual CPI inflation print came in a whisker below our forecast for a 6.0% lift in consumer prices (0.001%pts away from rounding up to 6!). But under the hood, we were surprised by the sheer strength in domestic inflation pressures, which were stronger than our already-high expectations. Non-tradables inflation surged to 5.3% y/y versus our forecast for 5.1%, while tradables prices "only" rose 6.9% y/y, versus our expectation for a 7.6% lift. The biggest drivers of inflation were construction costs (up 15.7% y/y) and petrol (up 30.5% y/y). The rise in the price of essential items is particularly hard to bear for low-income households, especially with real wages likely to keep falling for at least the next few quarters as wages play catch-up.

More alarming for the RBNZ was the lift in measures of core inflation, which aim to strip out temporary factors like one-off oil price movements. Every key measure of core inflation is now above the RBNZ's target band of 1-3%, with even the RBNZ's own sectoral factor model surging to 3.2% y/y (figure 1). Such a rapid increase in what's usually a very slow-moving series only reinforces our concerns that domestic inflation pressures are going to prove far more difficult to subdue than initially expected.

Figure 1. Core inflation measures



Source: Stats NZ, RBNZ, Macrobond, ANZ Research

All up, yesterday's data showed that while global inflation developments are still driving consumer prices higher in New Zealand, there's a very strong domestic inflation pulse moving through the economy too. With the labour market likely to keep tightening over 2022, that raises the risk of a wage-price spiral. Wage costs are surging – but productivity is still hampered by COVID, so firms have to pass these costs on to consumers or eventually go out of business. It's a nasty cycle that will gobble up any of the wage gains that workers see, and it reinforces the need for further OCR hikes by the RBNZ.

Key data summary

Performance Services Index – December. Almost broke even at 49.7. With COVID restrictions being tightened again in January, services industries may continue to struggle in coming months.

CPI – Q4. Consumer prices rose 5.9% y/y. See our Review.

ANZ Roy Morgan Consumer Confidence – January. Unchanged at 98 – under its long-term average of just shy of 120.

Looking ahead

Recent Publications

ANZ produces a range of in-depth insights.

- NZ Insight: Endemic COVID-19 and labour supply
- NZ Property Focus: Coming back to earth
- NZ Agri Focus: Higher prices for Christmas
- NZ Insight: The real cost of inflation
- NZ Insight: The Reopening
- NZ Property Focus: Risks building
- NZ Insight: NZ-UK Free Trade Agreement
- NZ Insight: The 'great resignation' in New Zealand
- NZ Insight: States of the world
- NZ Property Focus: The tide is turning
- NZ Insight: RBNZ Speech Review
- Not just rugby: NZ beating Australia on wage growth
- NZ Insight: Increasing the contingency fund
- NZ Insight: What would it take to derail OCR hikes?

Click here for more.

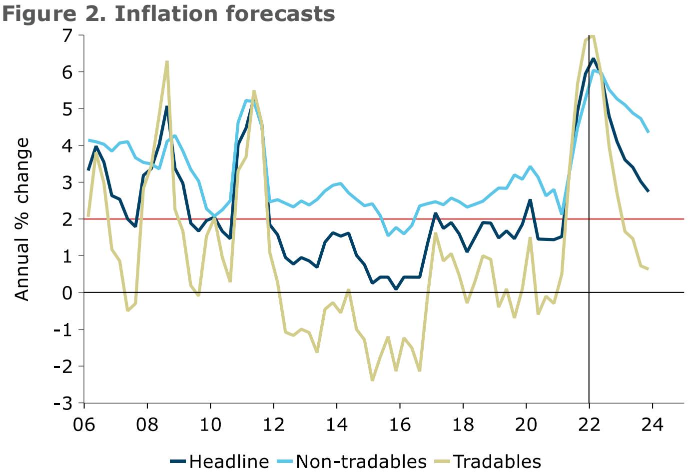
Data calendar

Date	Data/event
Mon 31 Jan (3:00pm)	RBNZ Sectoral Lending – Dec
Tue 1 Feb (10:45am)	Merchandise Trade – Dec
Wed 2 Feb (early am)	GlobalDairyTrade auction
Wed 2 Feb (10:45am)	**Labour Market – Q4**
Thu 3 Feb (1:00pm)	ANZ Commodity Price Index – Jan
Fri 4 Feb (10:45am)	Building Permits – Dec
Wed 9 Feb (10:00am)	ANZ Truckometer – Jan
Wed 9 Feb (3:00pm)	RBNZ 2Yr Inflation Expectations – Q1
Fri 11 Feb (10:30am)	BusinessNZ Manuf PMI – Jan
Fri 11 Feb (10:45am)	Electronic Card Transactions – Jan
Mon 14 Feb (10:30am)	Performance Services Index Jan

Inflation will be above target for a long time

As we noted last week, the underlying inflation pulse looks like it will be considerably more difficult for the RBNZ to rein in – and yesterday's data reinforced our fears. We've subsequently revised up our outlook for inflation over the next two years (figure 2). We expect inflation will peak at 6.4% y/y in Q1 this year, and will take a long time to get back inside the RBNZ's target band. We're forecasting inflation will only get back to 3% in the second half of 2023 – and unless something like a recession comes along, it will likely be well into 2024 before inflation is back at the target midpoint of 2%.

Figure 2. Inflation forecasts



Source: Stats NZ, Macrobond, ANZ Research

There are two key factors underlying this change of view. First, global inflation is proving more persistent. Supply disruptions are worsening, and wage pressures are rising in many countries. Central banks including the US Fed are now signalling imminent reduction of stimulus.

Second, and more importantly, the domestic inflation impulse is clearly far stronger than predicted, even at the time of the November MPS. And with the labour market likely to have drifted even further beyond maximum sustainable employment in Q4 (see our Preview), there's a self-reinforcing mechanism now in place that could drive domestic inflation higher and higher without ongoing interest rate hikes from the RBNZ.

We expect the RBNZ will need to lift the OCR in 25bp increments to 3% by April 2023 in order to put a stop to surging inflation. And even when they do that, monetary policy typically influences the economy with long lags – so we expect underlying inflation will be uncomfortably high for some time before higher interest rates start to gain traction.

The week ahead

RBNZ sectoral lending data – December (Monday 31 January, 3:00pm). May give insight into the impact of the CCCFA on overall lending.

Overseas Merchandise Trade – December (Tuesday 1 February, 10:45am). Exports and imports are both expected to ease, resulting in a $400m trade deficit for December.

GlobalDairyTrade auction (Wednesday 2 February, early am). Dairy markets have lifted sharply, indicating GDT prices will lift at least 5%.

Labour Market Statistics – Q4 (Wednesday 2 February, 10:45am). We expect the unemployment rate fell to 3.0%. See our Preview.

ANZ Commodity Price Index – January (Thursday 3 February, 1:00pm).

Building Permits – December (Friday 4 February, 10:45am). Holding up.

Markets and forecasts

What's happening in financial markets

The Q4 NZ CPI release added conviction to our call for an OCR at 3% by April 2023 (assuming the hiking cycle isn't interrupted by one or more of the many downside risks out there). Very strong core and domestic inflation measures mean the RBNZ has its work cut out. Rates markets took a little more conviction from the data too, and if next week's Q4 labour market data print as we expect, there could be more to come. We don't think the RBNZ will hike 50bps in February, but market pricing may well move a little further in that direction. As interesting as the domestic situation is, it hasn't really been in the driver's seat in FX markets this week. On that front, the Fed took centre stage, signalling lift off for the fed funds rate and an end to QE in March. This drove broad-based strength in USD and sent commodity currencies lower. The Fed doesn't seem to have caught too many analysts by surprise, but this is just the first leg of the tightening journey. In this environment, the risk-off implications could easily become the dominant driver for FX markets. So far, risk appetite appears to have handled the transition to hawkishness with some support from dip buying and robust US economic data. However, it's a long road ahead. And with inflation gaining momentum, it would likely take a much larger correction in asset prices and corresponding dent to economic activity than it may have in the past to deflect the Fed from its course. Indeed, central banks the world over may well find themselves in a situation where the least-worst choice is to inflict pain on risk markets and the broader economy in order to rein in the inflation beast. In that world, perhaps the current 65 handle on NZD/USD won't seem all that low.

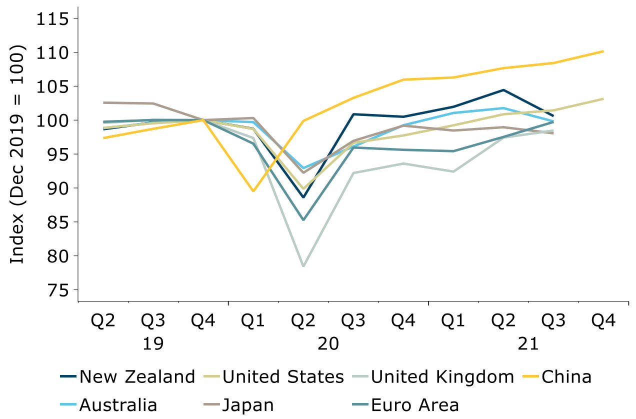
	Actual			Forecast (end month)					
FX rates	Nov-21	Dec-21	Today	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23
NZD/USD	0.682	0.683	0.659	0.720	0.720	0.720	0.720	0.720	0.720
NZD/AUD	0.956	0.942	0.936	0.960	0.960	0.960	0.960	0.960	0.960
NZD/EUR	0.600	0.600	0.591	0.637	0.637	0.632	0.626	0.626	0.621
NZD/JPY	76.9	78.6	75.9	83.5	83.5	83.5	83.5	83.5	83.5
NZD/GBP	0.510	0.506	0.492	0.533	0.533	0.529	0.526	0.526	0.522
NZ$ TWI	73.2	73.2	71.2	76.5	76.4	76.1	75.9	75.8	75.5
Interest rates	Nov-21	Dec-21	Today	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23
NZ OCR	0.75	0.75	0.75	1.00	1.50	2.00	2.50	2.75	3.00
NZ 90 day bill	0.81	0.97	1.10	1.52	2.02	2.52	2.77	3.10	3.10
NZ 10-yr bond	2.49	2.39	2.67	2.70	2.90	3.10	3.40	3.50	3.50

Economic forecasts

	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23
GDP (% qoq)	-3.7	**2.5**	**1.2**	**0.5**	**0.5**	**0.7**	**1.0**	**0.6**	**0.6**
GDP (% yoy)	-0.3	**2.6**	**2.3**	**0.4**	**4.8**	**2.9**	**2.7**	**2.8**	**2.9**
CPI (% qoq)	2.2	1.4	**1.3**	**0.9**	**1.2**	**0.8**	**0.8**	**0.7**	**0.8**
CPI (% yoy	4.9	5.9	**6.4**	**5.9**	**4.8**	**4.1**	**3.6**	**3.4**	**3.0**
Employment (% qoq)	2.0	**0.7**							
Employment (% yoy)	4.3	**4.3**				**Under review**			
Unemployment Rate (% sa)	3.4	**3.0**							

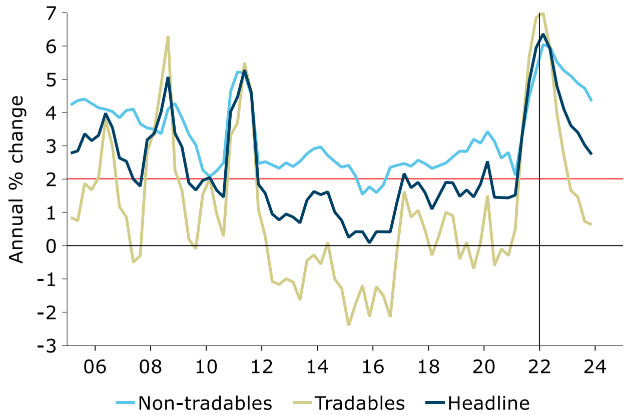
Figures in bold are forecasts. mom: Month-on-Month; qoq: Quarter-on-Quarter; yoy: Year-on-Year

Figure 3. GDP levels (Q4 2019= 100)



Source: Macrobond, ANZ Research

Figure 4. CPI inflation components



Source: Stats NZ, Macrobond, ANZ Research

Contact us

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We welcome your questions and feedback. Click here for more information about our team.

Sharon Zollner
Chief Economist

Follow Sharon on Twitter
@sharon_zollner

Telephone: +64 27 664 3554
Email: sharon.zollner@anz.com

General enquiries:
research@anz.com

Follow ANZ Research
@ANZ_Research (global)

David Croy
Senior Strategist

Market developments, interest rates, FX, unconventional monetary policy, liaison with market participants.

Telephone: +64 4 576 1022
Email: david.croy@anz.com

Susan Kilsby
Agricultural Economist

Primary industry developments and outlook, structural change and regulation, liaison with industry.

Telephone: +64 21 633 469
Email: susan.kilsby@anz.com

Miles Workman
Senior Economist

Macroeconomic forecast co-ordinator, fiscal policy, economic risk assessment and credit developments.

Telephone: +64 21 661 792
Email: miles.workman@anz.com

Finn Robinson
Economist

Macroeconomic forecasting, economic developments, labour market dynamics, inflation and monetary policy.

Telephone: +64 21 629 553
Email: **finn.robinson@anz.com**

Kyle Uerata
Economic Statistician

Economic statistics, ANZ proprietary data (including ANZ Business Outlook), data capability and infrastructure.

Telephone: +64 21 633 894
Email: kyle.uerata@anz.com

Natalie Denne
PA / Desktop Publisher

Business management, general enquiries, mailing lists, publications, chief economist's diary.

Telephone: +64 21 253 6808
Email: natalie.denne@anz.com

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