ANZ Research

New Zealand Weekly Data Wrap

19 August 2022

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See page 5.

Forecast updates

Recent ANZ NZ Forecast Updates can be found here.

- NZ Quarterly Economic Outlook: on the edge
- NZ Property Focus: hardening headwinds and soft landings
- NZ Forecast Update: farmgate milk price forecasts revised down

Our other recent publications are on page 2.

What's the view?

- GDP constrained by supply more than demand
- Labour market extremely tight, and very inflationary
- Inflation way above target, but likely peaked in Q2
- Aggressive OCR hikes towards 4.0% in November 2022 needed to contain inflation

Our forecasts are on page 4.

Confused by acronyms or jargon? See a glossary here.

Key risks to our view

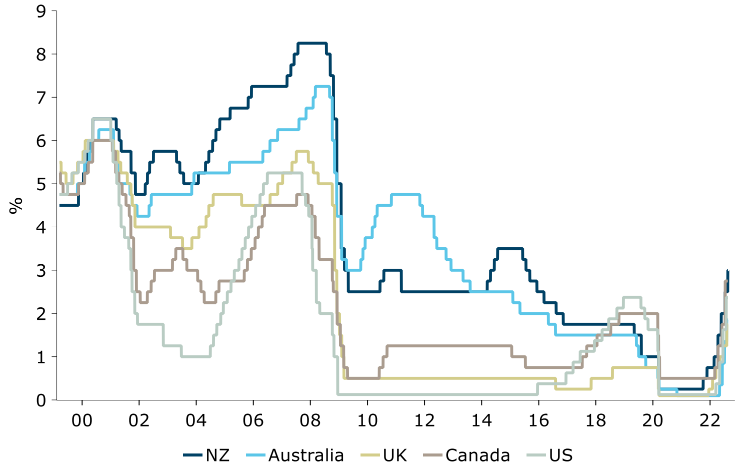
- Falling consumer and business sentiment derail momentum.
- Falling house prices could have a more significant impact on the economy than expected.
- Inflation expectations become unanchored, possibly as the labour market remains very tight.
- Global inflation pressures don't' decline as anticipated.

Inflation remains the focus for the RBNZ

This week the RBNZ released the August Monetary Policy Statement (MPS). As was pretty much universally expected, the Monetary Policy Committee (MPC) lifted the OCR 50bps to 3.0%. The overall tone of the document was hawkish, with the RBNZ raising their OCR forecast to peak at 4.1% in 2023 (versus 3.95% in the May MPS). That's broadly in line with our current forecast that the OCR will peak at 4% by year-end.

Central banks around the world continue to raise interest rates aggressively to try to catch up with surging inflation pressures (figure 1). However, markets are actually pricing policy rate cuts from the RBNZ, the US Federal Reserve, and other central banks over 2023 and beyond, reflecting market concerns about the risk of recession. In this context, it's important to remember that central banks don't target GDP growth. They're focussed on reducing inflation – since low and stable inflation is a prerequisite for sustaining economic growth and low unemployment. That's evident in the forecasts contained within the August MPS. The outlook for economic activity has received a significant downgrade, yet the RBNZ's new OCR track peaks 15bps higher than in May, at 4.10%. And the reason is simple: domestic inflation pressures are considerably stronger than the RBNZ expected back in the May MPS. So even though the domestic growth outlook is looking pretty soft over 2023, the best response for the RBNZ remains to keep rapidly lifting interest rates to try to bring inflation back down to acceptable levels (and within an acceptable timeframe). It's not going to be fun, and we're already seeing the impacts of monetary policy tightening through the housing market. But bringing inflation down is the best way to support the economy in the longer run.

Figure 1. Central bank policy rates



Source: RBNZ, RBA, BoE, BoC, Fed, Macrobond, ANZ Research

Our next update on economic activity will be Q2 retail sales – the first partial indicator for Q2 GDP. Following Q1's -0.5% Omicron-induced contraction, we expect to see a technical rebound in Q2. In fact, many of our indicator models for Q2 are strong, coming in around the 4% to 5% q/q mark. But for retail sales volumes, we need to account for strong inflation and typical volatility. After doing so, we're left with an expectation that retail sales volumes will lift 1.7% q/q. And while it'll be tempting to pin any upside or downside surprise on the day to weaker or stronger economic momentum, it's important to remember that the GDP (and related) data is still plagued with COVID-related noise, making momentum all the more difficult to gauge.

Looking ahead

Recent Publications

ANZ produces a range of in-depth insights.

- NZ Agri Focus: it's raining, it's pouring
- NZ Insight: the Australian labour market and the RBNZ
- NZ Property Focus: hardening headwinds and soft landings
- NZ Insight: the low consumer confidence puzzle
- NZ Property Focus: when, not if
- NZ Insight: He Waka Eke Noa recommendations
- Agri Insight: global food crisis to worsen
- NZ Property Focus: better fundamentals mean softer prices
- NZ Budget Review: Big Budget
- NZ Insight: Emissions Reduction Plan
- NZ Insight: new fiscal rules
- NZ Property Focus: regional rollercoaster
- NZ Insight: how widespread is labour market tightness?
- NZ Agri Focus: mixed blessings
- NZ Insight: the RBNZ's inflation expectations headache
- NZ Insight: how is NZ's agri sector impacted by the Russian invasion
- NZ Insight: The Reopening II – shifting economic sands
- NZ Insight: Endemic COVID-19 and labour supply
- NZ Insight: The real cost of inflation

Click here for more.

ANZ Proprietary data

Check out our latest releases below.

- ANZ Business Outlook
- ANZ-Roy Morgan Consumer Confidence
- ANZ Truckometer
- ANZ Commodity Price Index

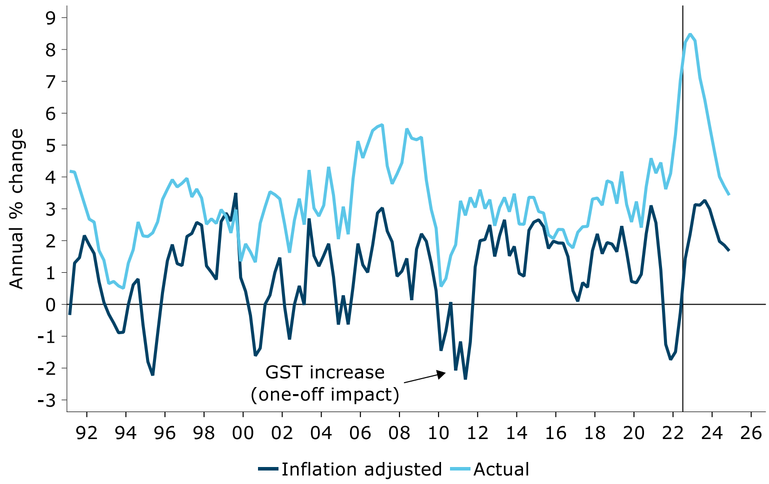
How high will the OCR go? It depends on neutral.

With the RBNZ now well into their hiking cycle, the question of exactly how high the OCR will need to go becomes ever more pertinent. As we mentioned in our Review of the August MPS, a key consideration is the level of the neutral OCR (that is, the level of the OCR which is neither stimulatory nor contractionary for the economy).

The RBNZ currently estimates that the neutral OCR is around 2%. If that is indeed the case, it means monetary policy is now solidly contractionary, with the OCR at 3% (ie it's at a level that should be reducing inflation over the medium term). But it's worth noting that in the Summary Record of Meeting the Monetary Policy Committee "discussed the possibility that neutral interest rates may be higher" and said that "staff will be undertaking further work to review their estimates". This is important, since any upward (or downward) adjustment in the RBNZ's view of the neutral interest rate needs to be reflected 1:1 in the actual OCR. Otherwise, monetary policy will not be as contractionary (or stimulatory) as previously thought or intended.

There are good reasons to think that the neutral interest rate has increased. In particular, inflation expectations have risen steeply over the past year, and that's now being reflected in wage- and price-setting behaviour. Private sector average hourly earnings rose 7.0% in the year to June 2022 – almost catching up to inflation (7.3%). We expect that wage growth will hit 8.5% over the next few quarters – surging well ahead of the cost of living (figure 2). The challenge for the RBNZ is that this strong wage growth makes households more resilient to the monetary policy tightening they've delivered. And that means with higher inflation now becoming embedded in wages, there's a risk of a higher-than-otherwise OCR being required to deliver the monetary tightening needed to return inflation to target.

Figure 2. ANZ forecast: Private sector average hourly earnings (ordinary time)



Source: Stats NZ, Macrobond, ANZ Research

We're forecasting the OCR to lift to 4% by year-end, very similar to the RBNZ's track. But that's conditional on a neutral OCR of about 2%. Signs that neutral might be higher would be indications that monetary policy isn't getting the traction expected, eg housing market green shoots or household spending refusing to roll over. That's not to say that interest rate risks are all to the upside. Recent data out of China highlights growth risks in our largest trading partner. Youth unemployment reached 19.9% in July, and the PBOC cut their policy rate by 10bps to 2% earlier this week as a softening property sector and the ongoing zero-COVID approach continue to weigh on the economy. But for now, the RBNZ's focus is firmly on medium-term inflation pressures.

Financial markets update

Data calendar

What's coming up in the months ahead.

Date	Data/event
Thu 25 Aug (10:45am)	Retail Sales – Q2
Fri 26 Aug (10:00am)	ANZ-RM Consumer Confidence – Aug
Wed 31 Aug (10:45am)	Building Permits – Jul
Wed 31 Aug (1:00pm)	ANZ Business Outlook – Aug
Wed 31 Aug (3:00pm)	RBNZ Sectoral Lending – Jul
Fri 2 Sep (10:45am)	Terms of Trade – Q2
Mon 5 Sep (10:45am)	Building Work Put in Place – Q2
Mon 5 Sep (1:00pm)	ANZ Commodity Price Index – Aug
Wed 7 Sep (early am)	GlobalDairyTrade auction
Thu 8 Sep (10:45am)	Economic Survey of Manufacturing – Q2
Fri 9 Sep (10:00am)	ANZ Truckometer – Aug
Fri 9 Sep (10:45am)	Electronic Card Transactions – Aug
Mon 12 Sep (10:45am)	Net Migration – Jul
Tue 13 Sep (10:45am)	Food Price Index – Aug
Tue 13 Sep (10:45am)	Rental Price Index – Aug
Wed 14 Sep (10:45am)	Balance of Payments – Q2
Thu 15 Sep (10:45am)	**GDP – Q2**
Fri 16 Sep (10:30am)	BusinessNZ Manuf PMI – Aug
Mon 19 Sep (10:30am)	Performance Services Index – Aug
Wed 21 Sep (early am)	GlobalDairyTrade auction
Thu 22 Sep (10:45am)	Merchandise Trade – Aug
Thu 29 Sep (1:00pm)	ANZ Business Outlook – Sep
Fri 30 Sep (10:00am)	ANZ-RM Consumer Confidence – Sep
Fri 30 Sep (3:00pm)	RBNZ Sectoral Lending – Aug
Tue 4 Oct (10:00am)	NZIER QSBO – Q3
Wed 5 Oct (early am)	GlobalDairyTrade auction
Wed 5 Oct (2:00pm)	**RBNZ Monetary Policy Review**

Interest rate markets

The MPS was the main focus for interest rate markets this week, and while the reaction on the day was fairly muted, key short-end rates like the 2yr swap had risen by around 20bps over the past fortnight. We regarded the MPS as hawkish – not only did the RBNZ see it fit to deliver another 50bp hike, but the new, higher track is consistent with two more 50bp hikes (in October and November), and the chance of another lesser hike in February. Markets have yet to close the gap, and may not for some time given global (and domestic) recession fears, but we still think it is too soon to say that short-end rates have peaked. An op-ed by Bank of Canada Governor Tiff Macklem caught our eye this week; he said that "the best way to protect people from high inflation is to eliminate it". He went on to say "that's our job, and we are determined to do it", and that "we know our job is not done yet — it won't be done until inflation gets back to the two per cent target". Everything he said is relevant to New Zealand, and while the RBNZ did get underway sooner than the Bank of Canada, they are seeing the same issues we are here, and his comments are a shot across the bow to markets that think we might see easing in 2023. Global rates have range-traded, and that has helped keep local long-end rates fairly steady. However, the tone we got from most US Federal Reserve speakers this week was hawkish (again), and that could set the scene for another blip higher in US bond yields in the lead-up to the 22 September FOMC meeting. The Kansas City Fed holds its annual symposium at Jackson Hole next week. In past years, this event has been a bit of a scene setter for how global central banks are thinking about the challenges they face, so expect to see plenty of headlines coming out.

FX markets

The Kiwi took well to the MPS initially, but as with past data releases and central bank decisions elsewhere, enthusiasm waned later as FX markets transitioned back to trading global themes. The USD continues to be well supported despite market participants' hankering for the global recession narrative. In the context of a safe-haven or "risk-off" vibe, further USD strength can't be ruled out, despite higher rates here and the RBNZ being well positioned to tackle inflation. Against that backdrop, it's hard to take a high-conviction view on NZD direction; instead we think it makes sense to expect more range-trading and the potential for a flare-up in volatility.

Key data summary

Performance of Services Index - July. Slowed to 51.2 (from 54.7), easing to below-average levels after a solid second quarter.

GlobalDairyTrade auction. The GDT Price Index dropped a further 2.9% this week, to an average price of USD3,768/t.

RBNZ Monetary Policy Statement – August. The Official Cash Rate (OCR) was lifted 50bp to 3%, as was universally expected. See our Review.

Overseas Merchandise Trade – July. The annual deficit grew to NZD11.6bn (NZD10.5bn previously), with imports (up 26% y/y) outpacing exports (up 16% y/y) by a significant margin.

The week ahead

Retail Trade Survey – Q2 (Tuesday 25 August, 10:45am). We've pencilled in a 1.7% rebound, and see risks on both sides.

ANZ Roy Morgan Consumer Confidence – August (Friday 26 August, 10:00am).

Key forecasts and rates

FX rates	Actual Jun-22	Jul-22	Today	Forecast (end month) Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23
NZD/USD	0.621	0.628	0.626	0.630	0.630	0.640	0.650	0.650	0.650
NZD/AUD	0.904	0.900	0.905	0.887	0.875	0.865	0.867	0.867	0.867
NZD/EUR	0.597	0.614	0.620	0.618	0.600	0.598	0.591	0.580	0.575
NZD/JPY	84.7	83.7	85.0	84.4	83.2	83.2	83.2	82.6	81.9
NZD/GBP	0.513	0.516	0.524	0.521	0.512	0.516	0.516	0.512	0.508
NZ$ TWI	70.5	71.1	71.4	71.0	70.2	70.4	70.7	70.3	69.9
Interest rates	**Jun-22**	**Jul-22**	**Today**	**Sep-22**	**Dec-22**	**Mar-23**	**Jun-23**	**Sep-23**	**Dec-23**
NZ OCR	2.00	2.50	3.00	3.00	4.00	4.00	4.00	4.00	4.00
NZ 90 day bill	2.86	3.14	3.35	3.93	4.10	4.10	4.10	4.10	4.10
NZ 2-yr swap	4.06	3.74	3.96	4.37	4.21	3.99	3.93	3.82	3.76
NZ 10-yr bond	3.86	3.42	3.52	4.25	4.00	4.00	4.00	3.75	3.75

Economic forecasts

	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
GDP (% qoq)	-0.2	**1.0**	**0.5**	**0.8**	**0.5**	**0.1**	**0.2**	**0.2**	**0.5**
GDP (% yoy)	1.2	**-0.1**	**4.4**	**2.2**	**2.8**	**1.9**	**1.6**	**1.0**	**1.0**
CPI (% qoq)	1.8	1.7	**1.6**	**0.9**	**0.7**	**0.6**	**0.8**	**0.4**	**0.4**
CPI (% yoy	6.9	7.3	**6.7**	**6.1**	**5.0**	**3.9**	**3.1**	**2.5**	**2.3**
Employment (% qoq)	0.0	0.0	**0.1**	**0.1**	**0.1**	**0.1**	**-0.3**	**-0.4**	**-0.4**
Employment (% yoy)	2.7	1.6	**-0.1**	**0.1**	**0.3**	**0.3**	**0.0**	**-0.5**	**-1.0**
Unemployment Rate (% sa)	3.2	3.3	**3.3**	**3.4**	**3.4**	**3.6**	**4.0**	**4.5**	**4.8**

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

Figure 3. Production GDP

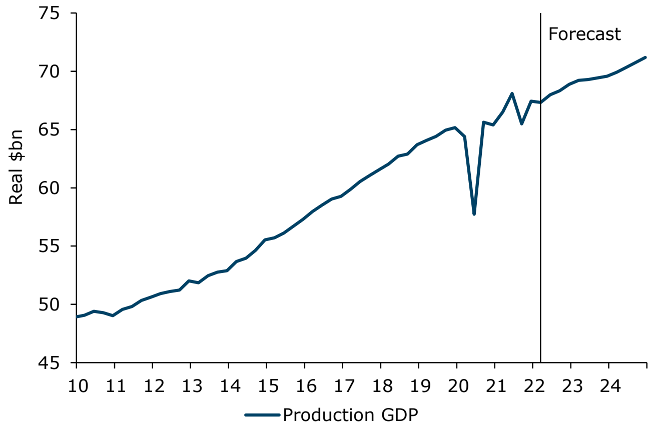


Figure 4. CPI inflation components

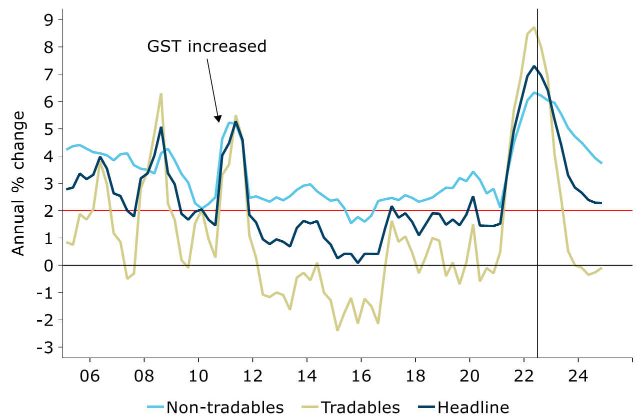


Figure 5. ANZ OCR forecast

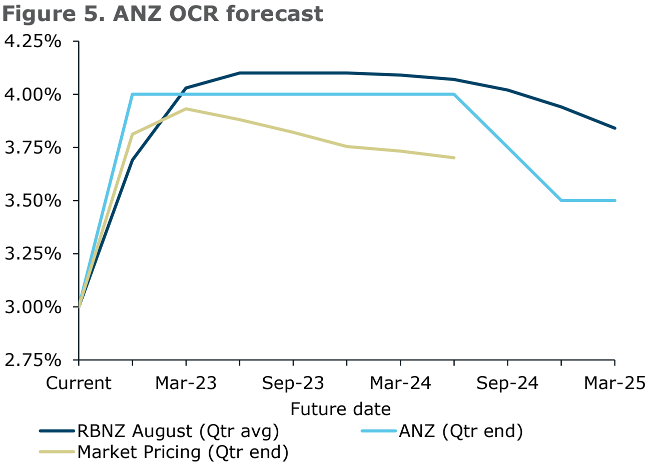
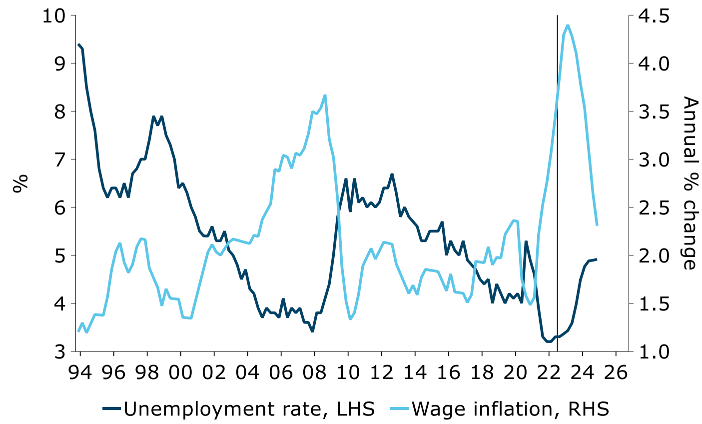


Figure 6. Unemployment and wage inflation



Source: Stats NZ, Bloomberg, RBNZ, Macrobond, ANZ Research

Contact us

Meet the team

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 9 357 4094
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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Ph 64-9-357 4094, e-mail nzeconomics@anz.com, http://www.anz.co.nz