ANZ Research

New Zealand Weekly Data Wrap

23 September 2022

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Contact us

See page 5.

Forecast updates

Recent ANZ NZ Forecast Updates can be found here.

- NZ OCR Call Change: more work to do
- NZ Forecast Update: farmgate milk price forecasts revised up
- NZ Property Focus: no place for green shoots
- NZ Quarterly Economic Outlook: on the edge

Our other recent publications are on page 2.

What's the view?

- GDP currently constrained by supply more than demand
- Labour market still extremely tight, and very inflationary
- Inflation way above target, but likely peaked in Q2
- OCR hikes to 4.75% by mid-2023 needed to contain inflation

Our forecasts are on page 4.

Confused by acronyms or jargon? See a glossary here.

Key risks to our view

- Global growth risks abound, not least in China, our key trading partner.
- Falling house prices could have a more significant impact on the economy than expected.
- The neutral OCR could be increasing faster than estimated.
- Global inflation pressures may not decline as quickly or as far as anticipated.

Recalibrating what it will take

We've changed our OCR call, adding another 75 basis points to our previous expected peak, taking the OCR to 4.75% come mid-2023. That's two more 50 basis point hikes this year (as before), followed by three 25 basis point "top up" hikes in each of the first three meetings of 2023.

We've been highlighting for some time now that there's a significant risk that domestic and core inflation will prove too sticky for the RBNZ's liking. And in large part, that's owing to the fact that the current rapid pace of wage growth, courtesy of the extremely tight labour market, is taking some of the sting out of rate hikes delivered to date. In macroeconomic terms, we think the neutral OCR is under upwards pressure, and well above the 2% central estimate the RBNZ have recently clocked it at. For those unfamiliar with the concept, the neutral OCR is the OCR at which monetary conditions are neither adding to nor subtracting from inflation pressure. That is, if inflation is looking like it'll be stable at 2%, then it's time for the RBNZ guide the OCR to neutral so it doesn't end up over- or undershooting its target. Or more pertinently for today, if the neutral OCR goes up, the actual OCR needs to go up in step just for monetary conditions to maintain their previous traction.

But estimating neutral is no easy feat:

- it's unobservable;
- estimates tend to be backwards-looking (ie core inflation did X with the OCR at Y, suggesting neutral must have been around Z); and
- it's time varying, moving with both shorter-term (cyclical) shocks, such as COVID impacts on productivity, and with structural change, such as the impacts on demand for savings relative to investment as New Zealand's demographic profile changes. And with longer-run inflation expectations.

Add the ongoing and significant COVID-induced wobbles to the data and it's a tough nut to crack. But the RBNZ has to make an assumption. The RBNZ has signalled that it is reviewing its modelling of the neutral OCR, but that this is a very big piece of work that's unlikely to be completed before year-end.

From an RBNZ strategy perspective, we're not convinced this speaks to a sudden (hawkish) change. While we certainly can't rule it out, we're not expecting the RBNZ to come out at an MPS with a sharply higher neutral assumption (ie something greater than 3%) that would suggest they've suddenly decided a lot more hikes are needed to deliver the contractionary impulse required to bring inflation down.

Rather, we think it'll be more gradual than that, with indicators of inflation pressure (including labour market tightness) holding up for too long for the RBNZ to be convinced that inflation will return to target in an acceptable timeframe, and that wage-price spiral risks are appropriately mitigated. That is, a series of starting-point shocks. Persistently elevated inflation pressures could just as easily feed into a lower potential GDP estimate by the RBNZ as a higher neutral assumption. But regardless of how they square their economic outlook, we think they'll conclude (as we have) that the OCR will need to go higher than marginally north of 4% as they signalled in August.

Regarding our broad economic outlook, our call change has very few immediate implications. In the absence of a very significant supply or productivity miracle, the RBNZ needs to drive domestic demand lower in order to take the pressure off currently stretched resources and see inflation slow. As we've been saying for a while now, that will happen, it's just a question of how high the OCR will need to go to achieve it.

Looking ahead

Recent Publications

ANZ produces a range of in-depth insights.

- NZ Insight: The inflation outlook and the balance of risks
- NZ Insight: 2020 hindsight
- NZ Agri Insight: feeding the world sustainably
- 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 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 Insight: the RBNZ's inflation expectations headache
- NZ Insight: how is NZ's agri sector impacted by the Russian invasion
- NZ Insight: Endemic COVID-19 and labour supply

Click here for more.

ANZ Proprietary data

Check out our latest releases below.

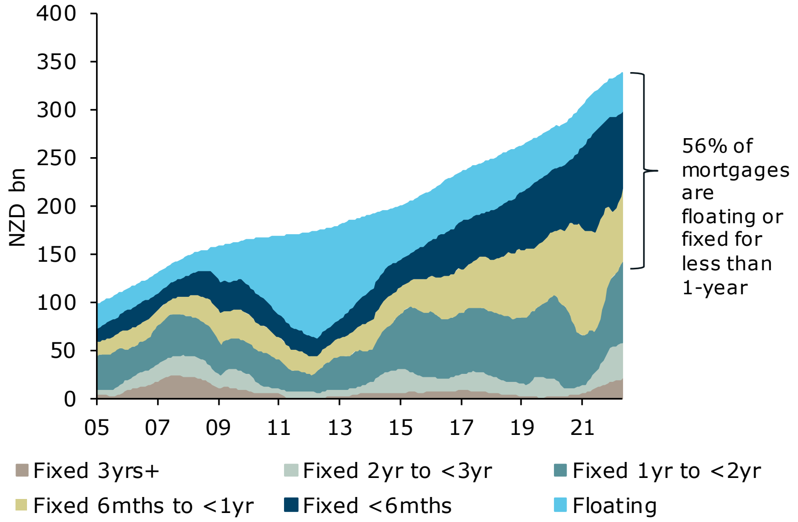
- ANZ Business Outlook
- ANZ-Roy Morgan Consumer Confidence
- ANZ Truckometer
- ANZ Commodity Price Index

Flip-flops or running shoes?

The economy is a pretty complicated and fickle beast. While we will always do our darndest, perfect economic foresight and forecast accuracy will always be unattainable. Big parts of our outlook, including our OCR call, are always going to represent what we think is most likely to happen, predicated on a suite of "most-likely" assumptions (informed by our own analysis and monitoring etc). To our minds, our updated OCR call better balances the risks around whether the OCR is likely to end up higher or lower than our forecast. But we would never claim that a 4.75% peak is a lock!

Monetary policy acts with long and variable lags, and there absolutely is a plausible scenario where a 4% OCR is all it will take to squeeze households enough to drive inflation lower. Mortgages are key. The share of loan fixes tends to vary (figure 1), meaning changes in mortgage rates will have varying lags at different times in terms of how they impact the aggregate debt-servicing burden, depending on collective behaviour.

Figure 1. Residential mortgages by fixed term



Source: RBNZ, ANZ Research

Take the one-year rate as an example. If you locked in a $500k mortgage at the low of around 2.2% in June 2021, you would have been faced with a one-year rate of around 5.1% come June 2022. Depending on how fast you were paying down principal, rolling over for one year in June 2022 would have added around $14k to your annual debt-servicing cost. Come June 2023, the one-year rate will likely be higher still.

A sizable chunk of loans is yet to fully transition to higher rates, and that could mean that we just need to be patient to see the impacts on household spending and inflation. But wages are rising strongly too, taking out some of the sting. We'll have more to say on this in our upcoming Property Focus. Suffice it to say that we think that robust household spending, strong PSI, sky-high job ads, lifting house sales, and recovering business and consumer confidence suggest that monetary tightening isn't quite getting the traction the RBNZ needs it to – more than a year since mortgage rates troughed.

In fact, there's a decent risk that if wage inflation remains stronger for longer, the OCR will need to go higher than 4.75%. That's partly why we haven't added eventual OCR cuts to our forecast: it's simply not clear that 4.75% will be enough to bring inflation down fast or far enough. Cuts are expected eventually (we think neutral is below 4.75%), but possibly from a higher peak and/or outside our forecast horizon. So while our updated call means we might have to flip flop if the data surprise to the downside, there's also a decent risk the OCR will need to run higher for longer.

Financial markets update

Data calendar

What's coming up in the months ahead.

Date	Data/event
Thu 29 Sep (1:00pm)	ANZ Business Outlook – Sep
Fri 30 Sep (10:45am)	Building Permits – Aug
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**
Thu 6 Oct (1:00pm)	ANZ Commodity Price Index – Sep
Tue 11 Oct (10:00am)	ANZ Truckometer – Sep
Tue 11 Oct (10:45am)	Electronic Card Transactions – Sep
Wed 12 Oct (10:45am)	Net Migration – Aug
Thu 13 Oct (10:45am)	Food Price Index – Sep
Thu 13 Oct (10:45am)	Rental Price Index – Sep
Fri 14 Oct (10:30am)	BusinessNZ Manuf PMI – Sep
Mon 17 Oct (10:30am)	Performance Services Index – Sep
Tue 18 Oct (10:45am)	**CPI – Q3**
Wed 19 Oct (early am)	GlobalDairyTrade auction
Fri 21 Oct (10:45am)	Merchandise Trade – Sep
Wed 26 Oct (1:00pm)	ANZ Business Outlook – Oct
Fri 28 Oct (10:00am)	ANZ-RM Consumer Confidence – Oct
Tue 1 Nov (10:45am)	Building Permits – Sep
Wed 2 Nov (early am)	GlobalDairyTrade auction
Wed 2 Nov (10:45am)	**Labour Market – Q3**
Thu 3 Nov (1:00pm)	ANZ Commodity Price Index – Oct
Tue 8 Nov (10:00am)	ANZ Truckometer – Oct
Tue 8 Nov (3:00pm)	RBNZ 2Yr Inflation Expectation – Q4
Wed 9 Nov (10:45am)	Electronic Card Transactions – Oct

Interest rate markets

It has been another volatile week in global interest rate markets, with US bond yields leading the way higher into this week's Fed decision (which saw a third 75bp hike), only to correct lower in its immediate aftermath, before resuming rising again. The yield on the bellwether US 10yr Treasury is currently at a post-COVID high of 3.7%. US short-end interest rates have also surged in reaction to a trio of factors: a resolute Fed, a much higher set of "dot plot" projections for where the Fed thinks its policy rate needs to go, and more robust US economic data. None of this is directly relevant to short-end rates here, but it has increased the degree of nervousness in markets, especially with the Fed flagging a 4½% - 4¾% peak in their policy rate, which markets are reading as making it "easier" for the RBNZ to get to take the OCR to 4¾%, as we now expect. This has only been further reinforced by the much lower NZD TWI, which both adds to the cost of imports and boosts the export and tourism sectors. Without doubt, markets have had a wake-up call this week insofar as central bank resolve is concerned, and although this week's moves have been sharp, we see no scope for any meaningful correction. In line with that, we have made further upgrades to our already highest-in-market interest rate forecasts. Although it's hurting, things are panning out broadly as we expected they would, and as they need to if inflation is to be brought under control within an acceptable time frame, here and abroad.

FX markets

The USD juggernaut continues to bulldoze its way higher, taking the USD DXY index to a fresh 20yr high in the lead-up to this week's Fed meeting. While it did wobble immediately after the Fed hiked as the bulls took profit, and has been held back a touch by yen intervention overnight, the USD continues to post strong gains against most other currencies, including the NZD. This partly reflects the USD's customary appeal during periods of turbulence and slower global growth, and the fact that the US (and Canada) now sport the highest policy rates in the G10. New Zealand isn't far behind, but our new Fed and RBNZ forecasts (both published well before the Fed) now have the Fed out-hiking the RBNZ from here on in. That could be a challenge to the Kiwi, as might be the perception (vs AUD) that Australia is generally in better shape.

Key data summary

Performance of Services Index - August. After lifting a whopping 4.2 points to 58.6, this indicator suggests services industries are gaining momentum.

GlobalDairyTrade auction. Dairy prices lifted 2.0%, with the price index for whole milk powder up 3.7%.

Overseas Merchandise Trade – August. The annual deficit continued to widen as imports continue to outpace exports. Consumption goods imports do appear to be plateauing, but certainly not rolling over. In other words, domestic demand still looks robust in these data.

The week ahead

ANZ Business Outlook – September (Thursday 29 September, 1:00pm).

Building Permits – August (Friday 30 September, 10:45am). After lifting 5% m/m in July, further strength in August would indicate this "interest rate sensitive" part of the economy is going against the grain. We expect residential investment to contract over 2023 (from very elevated levels).

ANZ Roy Morgan Consumer Confidence – September (Friday 30 September, 10:00am).

Key forecasts and rates

	Actual			Forecast (end month)					
FX rates	Jul-22	Aug-22	Today	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23
NZD/USD	0.628	0.612	0.585	0.620	0.620	0.630	0.630	0.630	0.630
NZD/AUD	0.900	0.893	0.880	0.886	0.886	0.875	0.863	0.863	0.863
NZD/EUR	0.614	0.613	0.594	0.626	0.633	0.649	0.630	0.618	0.600
NZD/JPY	83.7	84.9	83.2	86.8	88.0	89.5	88.2	85.1	81.9
NZD/GBP	0.516	0.527	0.519	0.534	0.539	0.553	0.548	0.538	0.534
NZ$ TWI	71.1	70.7	69.0	71.5	71.9	72.6	71.9	71.4	70.8
Interest rates	Jul-22	Aug-22	Today	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23
NZ OCR	2.50	3.00	3.00	3.00	4.00	4.25	4.75	4.75	4.75
NZ 90 day bill	3.14	3.47	3.74	3.93	4.27	4.77	4.85	4.85	4.85
NZ 2-yr swap	3.74	4.32	4.60	4.55	4.80	4.95	4.95	4.95	4.95
NZ 10-yr bond	3.42	3.98	4.11	4.25	4.50	4.75	4.75	4.75	4.75

Economic forecasts

	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24
GDP (% qoq)	1.7	**0.4**	**0.2**	**0.3**	**0.7**	**0.2**	**0.2**	**0.3**	**0.4**
GDP (% yoy)	0.4	**5.0**	**2.1**	**2.6**	**1.6**	**1.4**	**1.4**	**1.4**	**1.1**
CPI (% qoq)	1.7	**1.6**	**0.9**	**0.7**	**0.6**	**0.8**	**0.4**	**0.4**	**0.3**
CPI (% yoy	7.3	**6.7**	**6.1**	**5.0**	**3.9**	**3.1**	**2.5**	**2.3**	**2.0**
Employment (% qoq)	0.0	**0.1**	**0.1**	**0.1**	**0.1**	**-0.3**	**-0.4**	**-0.4**	**0.1**
Employment (% yoy)	1.6	**-0.1**	**0.1**	**0.3**	**0.3**	**0.0**	**-0.5**	**-1.0**	**-1.0**
Unemployment Rate (% sa)	3.3	**3.3**	**3.4**	**3.4**	**3.6**	**4.0**	**4.5**	**4.8**	**4.9**

Figures in bold are forecasts. mom: Month-on-Month; qoq: Quarter-on-Quarter; yoy: Year-on-Year. Click here for full ANZ forecasts

Figure 3. GDP forecast level

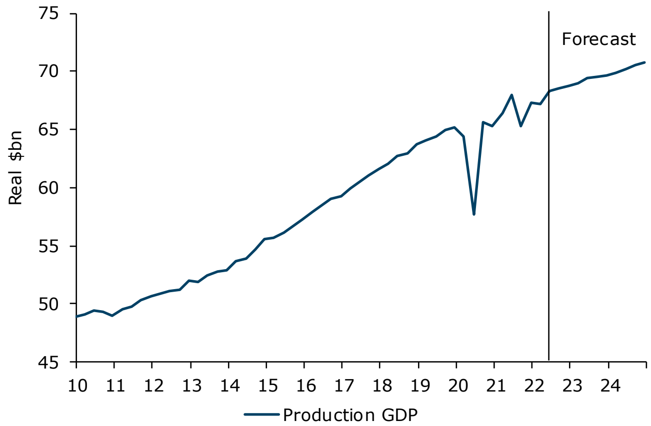


Figure 4. CPI inflation components

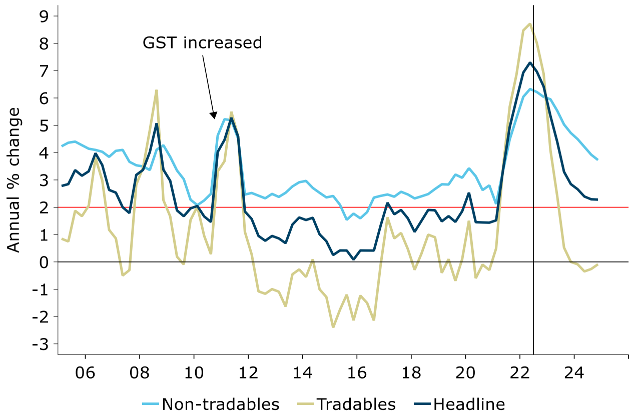


Figure 5. ANZ OCR forecast

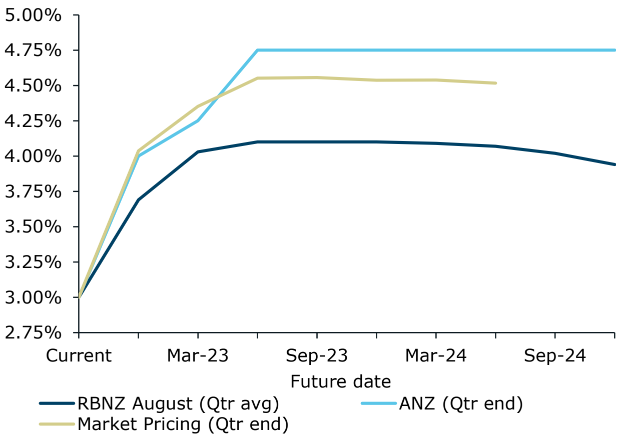
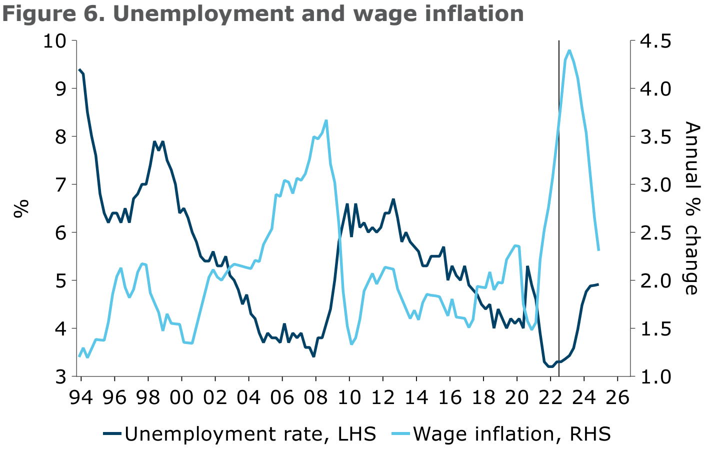


Figure 6. Unemployment and wage inflation



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

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