

# Economic Weekly

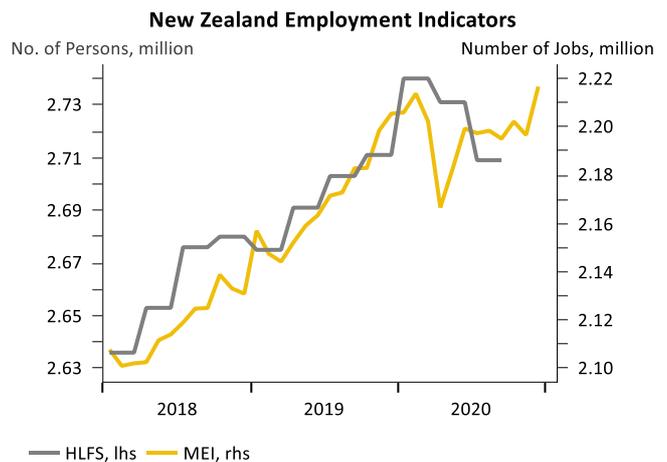
02 February 2021

## Blowing bubbles

The heady rise of the GameStop share price stole the financial market focus over the past week. This rise was reportedly driven higher by a group of sharemarket enthusiasts on a social media platform Reddit who challenged hedge funds' [short positions](#) on the stock. By driving demand higher, those short positions become increasingly expensive and risky to hold, in turn forcing the hedge fund managers to buy the stock to close out the position. Anecdotally, the trading strategy posted on Reddit started out late last year over a genuine view that GameStock was undervalued (back when it was around \$5 per share), believing the size of the short position to be unjustified relative to GameStock's financial performance (listen to NPR Planet Money podcast 'Cant Stop Game Stop' for a great summary of the GameStock share price debacle and a simple explanation of short positions and the idea behind triggering a 'short squeeze'). However, it appears the trading strategy has caught on more widely and got somewhat out of hand, driving the price to astronomical levels hand - GameStop's current share price is currently \$222, evoking comparisons to the Tulip Bubble. Reddit traders have now reportedly shifted focus to silver, driving silver prices higher over the weekend. The volatility has some financial market participants nervous about the fall-out once the bubble finally bursts.

Back in NZ, the focus is on the December quarter employment figures released on Wednesday morning. We expect the unemployment rate to lift from 5.3% to 5.6%, in line with market expectations and also the RBNZ's November forecast. See our full preview [here](#). Overall, the labour market picture is looking much better than expected and it's likely the peak in the unemployment rate is likely to be lower over 2021, compared to our forecasts from late last year. The economy has recovered faster than expected over Q3 last year, with the level of economic output (GDP) bouncing back to pre-COVID levels. The ANZ monthly business confidence survey suggests this momentum continued over Q4, with business confidence also back above pre-COVID levels by December. Furthermore, monthly job data from StatsNZ also point to improving labour demand (see chart opposite). Coupled with stronger than expected inflation data for Q4, the economy has proved itself to be on much sounder footing than ourselves and the RBNZ expected had been expecting, which reinforces our view that no further monetary stimulus is required at this point. Nonetheless, challenges to the economic outlook remain, with economic growth likely to be fairly soft this year slowed by weak exports of services and weak population growth. With borders expected to remain closed for the rest of the year and the impacts felt unevenly across the economy, there remains a case for targeted fiscal support.

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Source: Macrobond, ASB

## Foreign Exchange Market

FX Rates	Current*	Week ago	Month ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.7166	0.7191	0.7220	0.6464	FLAT	0.7100	0.7310
NZD/AUD	0.9387	0.9338	0.9377	0.9656	FLAT/DOWN	0.9320	0.9600
NZD/JPY	75.19	74.57	74.49	70.14	FLAT	72.90	75.50
NZD/EUR	0.5938	0.5923	0.5873	0.5833	FLAT/UP	0.5860	0.5950
NZD/GBP	0.5242	0.5263	0.5301	0.4912	FLAT/DOWN	0.5200	0.5400
TWI	74.8	74.5	74.8	71.66	FLAT/UP	N/A	N/A

^ Weekly support and resistance levels \* Current as at 9.30am today; week ago as at Monday 5pm

### NZD Recap and Outlook

The kiwi rode the rollercoaster of some wild moves in risk sentiment last week, but still finished the week pretty close to where it began. Stepping back, the NZD/USD has been chopping around in the 0.7100-0.7300 range for just over a month now and we think more of the same is likely for this week. We see the short-term risks as to the downside but expect support at 0.7100 to hold.

Late last week there were signs of a fraying in investors' generally buoyant risk sentiment. Equity markets were spooked by the whole 'hedge funds vs. retail investors' saga (epitomised by GameStop), boosting demand for the safe-haven USD, and weighing on NZD a little. The VIX index of risk aversion spiked briefly from 20% to 35%.

But in our view, global growth fundamentals actually continued to strengthen last week, and this is part of the reason we expect the NZD to remain well supported. European and Canadian GDP growth came in above expectations, US economic data mostly surprised on the upside (notwithstanding last night's small fall, to still-high levels, in the US ISM manufacturing index), and the vaccine news continues to be encouraging. Johnson & Johnson and Novavax reported strong efficacy results, and Pfizer said it is ramping up production of its vaccine.

There's a bit more on the slate this week that could see the NZD potentially test the range noted above. Local flavour will come from today's RBA meeting, tonight's GDT auction, ANZ business confidence on Thursday and likely the most market-moving event – tomorrow's Q3 labour market figures. We think the risk to markets from the labour market figures is mainly to the upside. An unemployment rate printing below the RBNZ's expectation (5.6%, same as ASB) would add to other indicators suggesting the economy is travelling well and likely see the yield curve continuing to lift and steepen.

For the RBA, we and the market expect no change in monetary policy. Market participants are alert to any hints about what the RBA will do after its current \$A100b bond buying program ends in April. We expect an \$A100b extension will be announced in March or April, but some analysts expect an announcement this week. As such, we could see some support for the AUD, and falls in NZD/AUD, if the RBA doesn't outline its intentions this week. We expect any knee-jerk NZD/AUD selling to run into support around 0.9300.

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### ASB foreign exchange forecasts

(end of quarter)	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Mar-22	Mar-23
	<<actual		forecast>>				
NZD/USD	0.66	0.72	0.70	0.70	0.71	0.71	0.71
NZD/AUD	0.93	0.94	0.93	0.92	0.92	0.91	0.92
NZD/JPY	70	75	74	74	76	77	80
NZD/EUR	0.56	0.59	0.57	0.56	0.56	0.55	0.53
NZD/GBP	0.51	0.53	0.52	0.51	0.52	0.52	0.52
NZD/CNY	4.5	4.7	4.6	4.6	4.6	4.5	4.5
NZD TWI	71.6	75.1	73.4	73.0	73.7	73.0	72.9

## Interest Rate Market

Wholesale interest rates	Current	Week ago	Month ago	Year ago	ST Bias	MT Bias
Cash rate	0.25	0.25	0.25	1.00	UNCH	UP
90-day bank bill	0.29	0.29	0.27	1.27	UNCH	UP
2-year swap	0.33	0.30	0.29	1.07	UNCH	UP
5-year swap	0.68	0.61	0.54	1.11	UNCH	UP
10-year swap	1.23	1.11	0.99	1.38	UNCH	UP
10-year govt bond yield	1.19	1.04	0.99	1.24	UNCH	UP
Curve Slope (2s10s swaps)	0.90	0.81	0.70	0.31	UNCH	DOWN

\* Current as at 9.30am today; week ago as at Monday 5pm. Key UNCH = Broadly unchanged

### Market Recap

NZ and global yields have continued to grind higher with a curve steepening bias. The NZ 2-year swap rate and 10-year NZ Government bond yield are at their highest level since April 2020, with the NZ yield curve (2s10s on interest rate swaps), its steepest since late 2018. This was particularly notable given the detection of some community cases of COVID-19 in NZ (which looks to have been contained for now), data pointing to a stronger fiscal starting point (implying less future issuance) and last week's \$650m in RBNZ bond purchases (outpacing the \$450m weekly tender).

Global yields have also nudged higher, albeit to a lesser extent, with the move higher despite recent wobbles in global equity markets and concerns over the timetable for COVID-19 vaccinations. Messages from global central banks have remained dovish. The US Federal Reserve left policy interest rates on hold, maintained its monthly USD120bn rate of asset purchases and signalled policy tightening (rate hikes or asset purchase tapering) were a long way off. There was little market reaction to the stronger than expected 0.9% qoq, 0.9% yoy) Australian CPI print, with annual core inflation measures (1 to 1.2% yoy) still very, very low. US inflation readings also modestly surprised to the upside, with forward-looking gauges continuing to point to strengthening momentum.

### Near-term interest rate outlook

In view of the recent run-up in NZ yields we have dropped our earlier upward bias. There are still risks of pronounced volatility over the coming months. Short-term NZ yields are expected to cluster at (or slightly above) 0.25% given our on-hold OCR view for 2021 and 2022. This week's NZ labour market data could surprise to the upside and pressure yields higher given the improving tone of domestic demand. News on COVID-19 in NZ and forward-looking gauges, including the ANZ business outlook (Thursday), could modestly impact yields. There are no NZ Government bonds to be tendered this week, with the syndication of the 2026 bond by NZ Debt Management expected to come into the region of \$NZ3-4bn. This should be easily absorbed by the market, and in conjunction with the (tapered down) \$570m in RBNZ NZ Government bond purchases should help dampen NZ medium to longer-term yields.

US Treasury yields are expected to remain sensitive to US fiscal news and should push higher if President Biden manages to overcome some Senate opposition and secure a package close to the USD1.9 trillion. There is also the risk that yields could edge up if governments and corporates take advantage of extremely low interest rates and increase debt issuance. Central banks will do their best to keep yields low. The RBA is widely expected to maintain its record low 0.1% cash rate and our CBA colleagues believe the RBA will maintain a dovish tone with the likelihood it will commit to buying a further AUD100bn of government bonds when the current AUD100bn programme expires in March/April. No policy changes are expected from this week's Bank of England meeting.

### Medium-term outlook

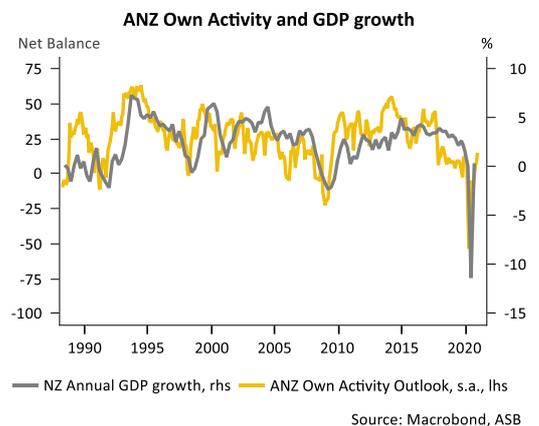
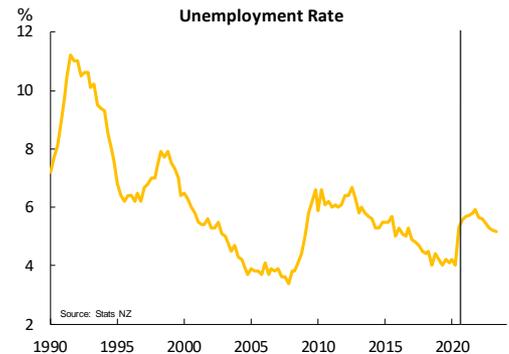
We have pencilled in a 0.25% OCR until mid-2023, given the resilience being displayed by the NZ economy and the expectation that the RBNZ's Funding for Lending Programme will pressure interest rates for borrowers lower. Our medium-term bias is for yields across the NZ yield curve to edge up. We expect local and global longer-term yields to subsequently grind higher over the next few years. [mark.smith4@asb.co.nz](mailto:mark.smith4@asb.co.nz)

## Domestic events

Data	Date	Time (NZT)	Market	ASB
Unemployment rate, Q4, %	03/02	10:45am	-	5.6%
ANZ business outlook survey, Feb, own activity	04/02	1:00 pm	-	-

We expect to see unemployment lift to 5.6%, from Q3's 5.3%. This is predicated on a small (0.1% qq) rise in employment and a tick up in the labour force participation rate to 70.2% (from 70.1%). The Government's wage subsidy was wound up in September/October, thus predictions initially abounded of a big increase in Q4 unemployment. But partial labour market data like Statistics NZ's Monthly Employment Indicator have tended to confirm the picture of steady employment through the quarter, rather than any material declines. Indeed, the overall outlook for NZ's labour market has brightened considerably.

ANZ monthly business confidence surged in December, with indicators of economic activity comfortably back at pre-COVID levels. We hope to see this confidence sustained in early 2021. Over the coming year the focus will shift away from growth, to the impact of growing cost pressures and the ability of businesses to pass these on



## Major International Events for the week ahead

Data	Date	Time (NZT)	ASB
Australia CoreLogic House Prices, Jan 2021, %mom	01/02	-	0.5
RBA Interest Rate Announcement, %	02/02	4:30 pm	0.1
Eurozone GDP, Q4, %qoq	02/02	11:00 pm	-
RBA Governor Lowe speech	03/02	2:30 pm	-
Australia Building Approvals, Dec 2020, %yoy	03/02	1:30 pm	2.5
Eurozone CPI, January, %mom	03/02	11:00 pm	-
Bank of England Interest Rate Announcement, %	05/02	1:00 am	-
RBA Governor Lowe testimony to Parliament	05/02	-	-
RBA Statement of Monetary Policy	05/02	4:30 pm	-
Australia Retail Trade, December, Q4, %qoq	05/02	1:30 pm	2.0
US Non-farm Payrolls, January, Unemployment rate, %	07/02	2:30 am	6.7

\* Forecasts and commentary originally published by CBA Global Markets Research Friday 29 January at 12:03 pm

Data are suggesting a moderate 0.5% lift in **Australia's dwelling prices** in January. Sydney and Melbourne look to have posted small gains in the month, while price gains have been stronger in Brisbane, Adelaide and Perth.

**The Reserve Bank of Australia's (RBA) Board are set to meet today** after a two-month break over Christmas. Since the last meeting in December we have seen economic data come in on the stronger side. But we have also had new lockdowns imposed (and lifted again) on the back of coronavirus outbreaks. We don't expect any changes to the stance of monetary policy at this meeting.

On Wednesday, **RBA Governor Lowe is slated to speak** on "The Year Ahead". The speech is a chance to outline the RBA's latest thinking on how the economy is tracking and outline their forecasts for 2021.

We expect another small lift in **Australian building approvals** in December. Approvals for detached houses have lifted sharply thanks to the Government's HomeBuilder scheme, which will be in place until end March 2021.

**In Governor Lowe's semi-annual testament to parliament**, a prepared speech will be followed by a long Q&A session. The housing market is likely to be a topic of interest given very strong growth in lending over H2 2020.

**At Friday's Statement of Monetary Policy (SMP)**, we expect the RBA to upgrade its forecast profile for GDP and lower its profile for the unemployment rate. Modest upward revisions are also expected to its inflation forecasts.

Preliminary data showed a 4.2% fall in **Australian retail trade** over December after a 7.0% surge in November. Retail trade is up by 2.4% in Q4 in nominal terms. This release also includes retail volumes for Q4 2020. We are forecasting a 2.0% lift in retail trade volumes in the quarter, which would see the annual rate of growth lift to a very strong 6.0%.

**The European Central Bank (ECB)** projects real GDP to have declined by 2.2% in Q4 2020 after rising by 12.5% the previous quarter because of tighter containment measures.

Headline annual **CPI inflation in the Eurozone** printed below 0% for a fifth consecutive month in December 2020. Ample spare capacity suggests inflation will remain negative until early 2021.

**We expect the Bank of England (BoE) to make no policy changes** at its February meeting. The Bank policy rate and the total stock of asset purchases will remain at 0.10% and £895bn, respectively.

The recovery in the **US labour market** moderated at the start of 2021. We estimate no new jobs were added to the labour market in January because economic activity was constrained to control the virus. We expect the unemployment rate to print at 6.7% for the third consecutive month.

## Key Forecasts

### ASB NZ economic forecasts

	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Mar-22	Mar-23
	<< actual	forecast >>					
GDP real - Q%	14.0	0.6	0.2	0.2	0.2	0.3	0.8
GDP real - A%	0.4	0.8	2.2	15.1	1.2	1.0	3.4
GDP real - AA%	-2.3	-2.5	-2.0	4.3	4.5	4.2	2.4
NZ House Prices (QV Index) - A%	9.5	11.7	12.8	15.2	12.7	7.1	4.9
CPI - Q%	0.7	0.5	0.6	0.4	0.7	0.3	0.4
CPI - A%	1.4	1.4	1.2	2.1	2.1	1.6	1.9
HLFS employment growth - Q%	-0.8	0.1	0.6	0.7	0.4	0.5	0.5
HLFS employment growth - A%	0.2	0.1	-0.4	0.7	1.9	1.8	1.8
Unemployment rate - %sa	5.3	5.6	5.7	5.7	5.8	5.6	5.0

Q% = percentage change on previous quarter

A% = percentage change since same quarter the previous year

AA% = percentage change for year ending quarter since the previous year

### ASB interest rate forecasts

	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Mar-22	Mar-23
	<< actual	forecast >>					
(end of quarter)							
NZ OCR	0.25	0.25	0.25	0.25	0.25	0.25	0.25
NZ 90-day bank bill	0.31	0.27	0.30	0.30	0.30	0.30	0.30
NZ 2-year swap rate	0.05	0.28	0.25	0.25	0.25	0.25	0.45
NZ 5-year swap rate	0.13	0.54	0.50	0.50	0.50	0.50	0.65
NZ 10-year swap rate	0.50	0.98	1.00	1.00	1.00	1.00	1.15
NZ 10-year Bond	0.46	0.99	1.00	1.00	1.00	1.05	1.20

### ASB foreign exchange forecasts

	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Mar-22	Mar-23
	<< actual	forecast >>					
(end of quarter)							
NZD/USD	0.66	0.72	0.70	0.70	0.71	0.71	0.71
NZD/AUD	0.93	0.94	0.93	0.92	0.92	0.91	0.92
NZD/JPY	70	75	74	74	76	77	80
NZD/EUR	0.56	0.59	0.57	0.56	0.56	0.55	0.53
NZD/GBP	0.51	0.53	0.52	0.51	0.52	0.52	0.52
NZD/CNY	4.5	4.7	4.6	4.6	4.6	4.5	4.5
NZD TWI	71.6	75.1	73.4	73.0	73.7	73.0	72.9

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