

Economic Weekly

07 September 2020

NZ's remarkable resilience

We released our latest [Quarterly Economic Forecasts](#) today, and taking a look back and comparing our current forecasts against our previous set of Quarterly Forecasts finalised in May we have been surprised by the remarkable resilience of the NZ economy. Back in May, we were bracing ourselves for a recession double the size of that seen in the 2008/09 Global Financial Crisis (and still found ourselves at the more optimistic range of economic forecasters). Subsequently, we have found ourselves nudging our GDP forecasts higher – we now expect the economy to shrink around 5% when comparing the end of 2020 with the end of 2019, vs a 6% decline we had previously forecast. Furthermore, we see some risk of further upward revisions over coming weeks. Ahead of the upcoming Q2 GDP release (September 17th), StatsNZ releases key detailed economic surveys including last week's Building Work Put in Place survey - which showed that construction activity held up better than expected, particularly construction of residential dwellings. This survey, along with other recent data, suggest that some types of activity recovered more quickly than we expected through Alert Levels 3 and Alert Levels 2 – and that production output was not as constrained by social distancing requirements as we had expected. If this finding is corroborated by additional surveys (such as the Economic Survey of Manufacturing, out on Wednesday) and ultimately Q2 GDP – we will also need to fine tune our estimates of how much economic activity takes place under Alert Level 3 and Alert Level 2. The upshot is that the economic cost of the current lockdown, for example, isn't likely to be as high as we previously estimated. The ANZ August business confidence figures released last week showed little reaction in business confidence from the news of a second lockdown – the lack of pessimism may reflect that NZ pulled through the first lockdown much better than expected. We will be watching the September preliminary results closely to see if business confidence remains steady in light of the August resurgence. jane.turner@asb.co.nz

Recent key economics

ASB Economic forecasts and monitoring:

[Quarterly Economic Projections](#)

[ASB COVID-19 Chart pack](#)

[Home Economics](#)

Financial market trends:

[Corporate Hedging Toolbox](#)

Policy response:

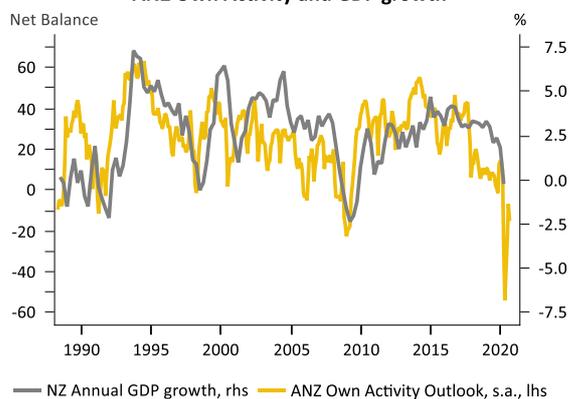
[RBNZ August MPS Review](#)

[Assessing the RBNZ's bag 'o' tricks](#)

For COVID-19 research, see [here](#)

Chart of the week

ANZ Own Activity and GDP growth



Source: Macrobond, ASB

Foreign Exchange Market

FX Rates	Current*	Week ago	Month ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.6711	0.6722	0.6662	0.6382	DOWN	0.6530	0.6790
NZD/AUD	0.9219	0.9147	0.9255	0.9361	FLAT	0.9070	0.9250
NZD/JPY	71.30	71.02	70.34	68.25	DOWN	68.80	72.00
NZD/EUR	0.5668	0.5647	0.5630	0.5781	FLAT	0.5500	0.5720
NZD/GBP	0.5065	0.5040	0.5080	0.5176	FLAT	0.4970	0.5150
TWI	72.4	72.1	72.2	71.10	FLAT/DOWN	N/A	N/A

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

NZD Recap

The NZD/USD rose to fresh 14-month high around 0.6780 last week, feeding off the combined impetus of a weaker USD and upbeat global risk sentiment. Gains on a trade-weighted basis were much less marked, revealing the extent to which the weaker USD is the driving force in currency markets at present.

The NZD has also drawn support from the halting of the NZD/AUD downtrend. This is something we warned of a fortnight or so ago given how skewed positioning had become in the cross. From a low of 0.9050 in mid-August, the NZD/AUD has slowly ground back above 0.9200 as speculative investors have reduced short positions. The weekend's news that Melbourne's lockdown has been extended for two weeks will likely solidify short-term support. Further ahead, we expect the downtrend to resume (see forecasts below).

The mini-meltdown in stock markets towards the end of last week barely ruffled the NZD. The NZD/USD eased only a little off its highs to open the week around 0.6720.

Outlook

The NZD/USD has so far proven resistant to the recent sapping in global risk appetite, but we think it may succumb this week. Notably, weaker risk appetite has shaved over a cent off our short-term valuation model's 'fair-value' range, which now sits at 0.6200-0.6600. As a result, the NZD/USD is mildly overvalued on this basis for the first time since February 2019.

Supporting this view, we think the USD is overdue a short-term bounce. Not only is safe-haven demand on the increase again but some countries are starting to push back against currency strength driven by USD weakness. The most notable of such is Europe, and any reiteration of concerns about EUR/USD strength at this week's ECB meeting would add to the pressure on the EUR to fall and USD to rise.

Outside of the ECB meeting, it's a fairly quiet week for news/events. The Federal Reserve meeting next week looms large as the next major piece of event risk. This week's key events include the prelim ANZ business confidence index and a few more Q2 indicators in NZ. Offshore, markets will be most interested in the Bank of Canada meeting and US jobless claims and inflation data.

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ASB foreign exchange forecasts

(end of quarter)

	Jun-20 << actual	Sep-20 forecast >>	Dec-20	Mar-21	Jun-21	Mar-22	Mar-23
NZD/USD	0.64	0.66	0.67	0.67	0.66	0.66	0.66
NZD/AUD	0.93	0.90	0.89	0.88	0.86	0.85	0.86
NZD/JPY	69	70	71	70	69	69	69
NZD/EUR	0.57	0.54	0.54	0.54	0.53	0.52	0.53
NZD/GBP	0.52	0.50	0.50	0.49	0.49	0.49	0.49
NZD/CNY	4.5	4.6	4.6	4.6	4.5	4.4	4.4
NZD TWI	71.4	69.6	70.0	69.5	68.0	67.5	67.7

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/DOWN	UP
90-day bank bill	0.31	0.29	0.30	1.17	UNCH/DOWN	UP
2-year swap	0.06	0.08	0.20	0.96	UNCH/DOWN	UP
5-year swap	0.17	0.19	0.29	1.02	UNCH/DOWN	UP
10-year swap	0.60	0.61	0.64	1.31	UNCH/DOWN	UP
10-year govt bond yield	0.65	0.63	0.77	1.15	UNCH/DOWN	UP
Curve Slope (2s10s swaps)	0.54	0.53	0.44	0.35	UNCH	DOWN

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

Market Recap

At the end of last week NZ swap yields touched record lows for most tenors, with more sizeable falls in longer-term yields. There were some ups and downs along the way with NZ yields rising after the speech by Governor Orr was not as explicit as the market was hoping for in signalling pending OCR cuts. There was little market reaction to local data. Global longer-term yields followed equities downward towards the end of last week, pushing NZ 10-year government bond yields (0.59%) towards their late August record low, with more sizeable falls for Australian counterparts (0.88%). This week's NZ Government bond tender was mixed, with softer demand for the 2033 maturity and with longer-term swap yields continuing to undershoot corresponding bond yields, notwithstanding the \$1,350m in RBNZ asset purchases last week. US Treasury yields snapped higher over the weekend (10Y 0.72%) following the release of a strong set of data from the US household survey data, including the sharp fall in the US unemployment to 8.4% (mkt: 9.8%), its lowest since March.

Near-term interest rate outlook

Our view remains that the prospect of a negative OCR should maintain downward pressure on short-term NZ yields. This week's local data – including further partial inputs for NZ Q2 GDP, card spending and even business confidence – are biased to surprise to the upside if COVID-19 impacts prove more modest than originally feared. We expect that the RBNZ will not be bothered in the slightest and will continue to want lower NZ yields and over time will do what they can to achieve this. We also expect minimal market reaction from overseas data, with the Australian NAB survey, and US and Chinese CPI data the major releases.

NZ longer-term yields will take their cues from global catalysts and while the lift in Treasury yields will likely lift NZ yields in the very near term, the direction of global equities should prove an important barometer for subsequent yield direction. The RBNZ has signalled a sizeable \$1.35bn weekly pace of NZ government bond purchases that will outpace the \$1,000m in weekly tenders. Cumulative RBNZ purchases (\$28.6bn to date) are well under the \$100bn LSAP cap and comfortably below Crown indemnity thresholds, providing plenty of scope for the RBNZ to front-load asset purchases over the next few months, helping to flatten the NZ yield curve and depress NZ yield.

Medium-term outlook

Providing operational hurdles are cleared and the RBNZ sticks to its forward guidance, we expect to see the RBNZ cut the OCR to -0.50% by early 2021 (most likely April) and for a Funding for Lending Programme to be introduced at this time. Prior to then we expect the RBNZ to front-load asset purchases and employ forward guidance to dampen yields. Low global inflation and subdued global growth prospects should keep NZ yields low and the curve reasonably flat despite high public debt issuance. mark.smith4@asb.co.nz

ASB interest rate forecasts

	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Mar-22	Mar-23
(end of quarter)	<< actual	forecast >>					
NZ OCR	0.25	0.25	0.25	0.25	-0.50	-0.50	-0.25
NZ 90-day bank bill	0.30	0.25	0.15	0.00	-0.50	-0.50	-0.20
NZ 2-year swap rate	0.21	0.10	0.00	-0.15	-0.30	-0.30	0.00
NZ 5-year swap rate	0.35	0.15	0.10	0.00	-0.15	-0.15	0.15
NZ 10-year swap rate	0.74	0.50	0.30	0.10	-0.10	0.10	0.50
NZ 10-year Bond	0.91	0.55	0.45	0.25	0.00	0.20	0.55

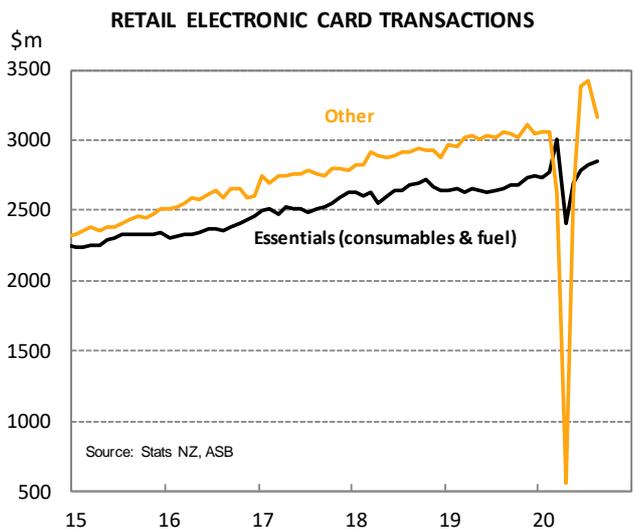
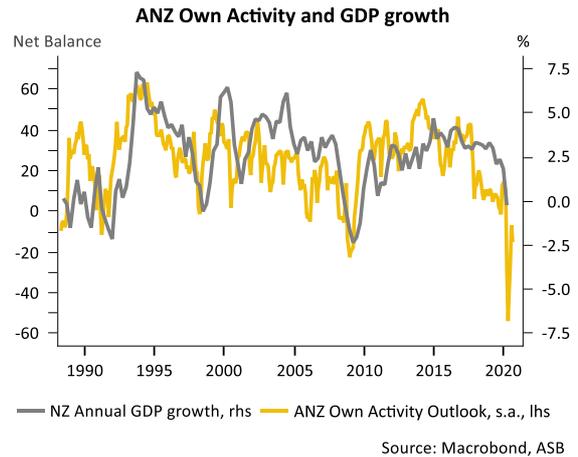
Domestic events

Data	Date	Time (NZT)	Market	ASB
NZ Economic Survey of Manufacturing, %qoq, Q2	09/09	10:45am	-	-
ANZ Business Outlook, Own activity, Sep, Preliminary	09/09	1:00pm	-	-
Retail Electronic Card Transactions, August, % mom	10/09	10:45am	-	-3.5

We use sales and inventory from the Economic Survey of Manufacturing as an indicator for Q2 GDP ex-meat and dairy manufacturing production. **We have pencilled in a 25% contraction in Q2 GDP ex-meat and dairy manufacturing production.** We expect manufacturing activity was disrupted by shutdowns for non-essential production under the Alert Level 4 restrictions, and under Alert Level 3 and 2 production was impacted by social distancing requirements. There is an extremely high degree of uncertainty around our Q2 estimates, particularly the impact of the lockdown and other measures put in place to contain the COVID-19 outbreak.

Business confidence declined in early August – but surprisingly the discovery of COVID-19 in the community did not result in a further fall in confidence over the second half of the month when the full results were released. **We will be watching the early September results with great interest.** We could see an improvement in confidence coinciding with the move of Auckland from Alert Level 3 to Alert Level 2.5 on September 4th. Alternatively, a delayed reaction to the re-emergence of COVID-19 in the community could weigh on sentiment.

We expect a pullback in August **card spending** as the stepping up in Alert Level restrictions from 12 August (Auckland to level 3, rest of NZ to level 2) likely restricted non-essential retail sales. Our internal card spending data showed a tailing off in overall spending over the second half of the month. Anecdotes suggests there has not been as much panic buying and stocking up by NZ consumers, with retailers likely better prepared to operate under the stricter criteria. **Nevertheless, we expect falls in non-essential retail, with hospitality particularly impacted.** Rising unemployment, few overseas visitors and weak household income growth point to a soft trajectory for card spending over the next few months.



Major International Events for the week ahead*

Data	Date	Time (NZT)	ASB
China Trade Balance, August, US\$bn	07/09	-	-
Australia CBA Weekly Card Spend, week ended 4 th Sep	08/09	-	-
Australia Weekly Payrolls Data, week ended 22 nd Aug	08/09	-	-
Japan Current Account Surplus, July, ¥bn	08/09	11:50 am	1,500
Australia Home Loans Value, July, %mom	09/09	1:30 pm	+2.0
China CPI Inflation, August, %yoy	09/09	1:30 pm	2.8
US CPI, August, %yoy	11/09	12:30 am	1.1

*Originally published by CBA Global Markets Research on Friday 4 September at 1:33 pm

China's import and new export order components of the PMIs lifted notably in August. We expect exports to grow by 6%yoy because of recovering foreign demand and resilient demand for COVID-19 related products. An accelerating recovery in domestic demand implies imports lifted by around 1%. We estimate a US\$46bn **trade surplus**.

Over the week ending 28 August, **Australia CBA's credit and debit card spending data** eased to sit just 1% higher than a year ago. Annual spending fell in all jurisdictions. We expect the theme of growing disparity in spending between Victoria and the other jurisdictions to remain for some time until restrictions are eased in Victoria.

The **weekly payrolls and wages data (released fortnightly) in Australia** are displaying a disparity between economic outcomes across different jurisdictions. Data to 8th August showed that jobs are falling in Victoria but are making a recovery in Western Australia, Queensland and to a lesser extent New South Wales.

We estimate **Japan's current account surplus** to lift to ¥1,500bn in July because rising exports to China and the US have narrowed the trade deficit.

We **expect Australia's value of new home loans** to rise 2.0% in July after lifting 6.2% in June. The easing in COVID-19 restrictions is enabling more real estate activity like auctions and open homes. Lower mortgage rates are also supporting new home lending.

We estimate **China's CPI inflation** lifted to 2.8%yoy in August because of rising food and pork prices. PPI deflation should have eased to 1.9%yoy because a recovery in demand lifted commodity prices.

US retail gasoline prices were flat in August. Excess capacity in labour and product markets will keep inflation low for several years in our view.

Key Forecasts

ASB NZ economic forecasts

	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Mar-22	Mar-23
	forecast >>						
GDP real - Q%	-13.1	10.6	0.9	0.3	0.1		
GDP real - A%	-13.4	-5.0	-4.6	-2.8	12.1	0.8	3.2
GDP real - AA%	-2.4	-4.2	-5.8	-6.5	-0.5	3.6	2.3
CPI - Q%	-0.5	0.9	0.0	0.1	0.2		
CPI - A%	1.5	1.7	1.2	0.6	1.2	1.3	1.3
HLFS employment growth - Q%	-0.4	-2.7	-1.1	-0.2	0.2		
HLFS employment growth - A%	1.1	-1.9	-3.2	-4.3	-3.7	1.9	1.8
Unemployment rate - %sa	4.0	6.4	7.2	7.7	7.8	7.1	7.0
Annual current account balance as % of GDP	-2.3	-2.0	-2.2	-2.7	-3.1	-3.1	-3.4

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

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(end of quarter)	<< actual	forecast >>					
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NZ 90-day bank bill	0.30	0.25	0.15	0.00	-0.50	-0.50	-0.20
NZ 2-year swap rate	0.21	0.10	0.00	-0.15	-0.30	-0.30	0.00
NZ 5-year swap rate	0.35	0.15	0.10	0.00	-0.15	-0.15	0.15
NZ 10-year swap rate	0.74	0.50	0.30	0.10	-0.10	0.10	0.50
NZ 10-year Bond	0.91	0.55	0.45	0.25	0.00	0.20	0.55

ASB foreign exchange forecasts

	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Mar-22	Mar-23
(end of quarter)	<< actual	forecast >>					
NZD/USD	0.64	0.66	0.67	0.67	0.66	0.66	0.66
NZD/AUD	0.93	0.90	0.89	0.88	0.86	0.85	0.86
NZD/JPY	69	70	71	70	69	69	69
NZD/EUR	0.57	0.54	0.54	0.54	0.53	0.52	0.53
NZD/GBP	0.52	0.50	0.50	0.49	0.49	0.49	0.49
NZD/CNY	4.5	4.6	4.6	4.6	4.5	4.4	4.4
NZD TWI	71.4	69.6	70.0	69.5	68.0	67.5	67.7

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