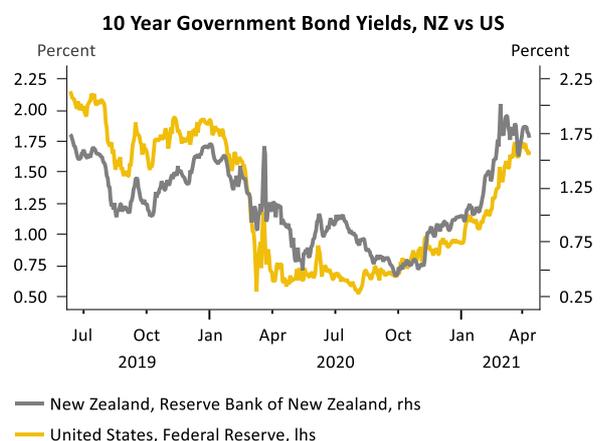


Economic Weekly

12 April 2021

Travel bubble boost and RBNZ interest rate angst

The Reserve Bank of New Zealand's (RBNZ) April Official Cash Rate (OCR) review on Wednesday is likely to be the key focus of domestic markets this week. The April OCR review is typically a one-page statement plus a summary of the Monetary Policy Committee's meeting, and does not publish updated forecasts. The key focus of the RBNZ communication will be keeping a lid on longer-term interest rate expectations - 10-year interest rates have jumped sharply in NZ and abroad over 2021. This lift has been supported by improved global financial market sentiment as the end of the COVID-19 pandemic seems in sight. And while that may be the case for the US, which could reach herd immunity within the next three months, there is still a long way to go in NZ before we can open the borders and return to normal. The RBNZ will be wanting to avoid a premature tightening in monetary conditions in NZ. The unexpected fall in December quarter GDP highlights the fragility of the NZ economic recovery over the year ahead. Read our full RBNZ preview [here](#).



Source: Macrobond, ASB

Last week, NZ has finally confirmed a reciprocal travel bubble with Australia. The announcement is likely to be some relief to those with friends and family across the ditch. It also opens the possibility for more New Zealanders to relocate back home from Australia. However, the hopes that it would also boost the numbers relocating from further abroad were dashed somewhat, as it was revealed that some of the MIQ facilities that have been used for 'low-risk' Australian arrivals are not appropriate to safely manage arrivals from higher-risk countries.

For the economy, our view is that the Trans-Tasman travel bubble will have limited net impact on the economy, with the possibility of a small positive. However, the bubble may only have limited benefits to the tourism industry. The bubble is more appropriate for those visiting friends and family, rather than holiday makers given there is the ongoing possibility of being stranded if there was a community outbreak. Given the relative frequency of outbreaks due to MIQ breaches in both in NZ and Australia over recent months, a short-term pause or suspension of quarantine-exempt flights is likely at some point. The Prime Minister has made it very clear that travellers need to be prepared for such a scenario. Nonetheless, to the extent that Australian visitors here to see family may also take the opportunity to visit some of NZ's tourism highlights, the travel bubble may help shift some of the spending towards some of the regions which have been struggling due to closed borders. Over summer anecdotes suggest NZers preferred to holiday at the beach rather than Queenstown and the southern regions have been struggling. However, with winter approaching, Queenstown could be set for a solid ski season with the possibility of both NZers and Australians keen to hit the slopes given the lack of other winter holiday alternatives. jane.turner@asb.co.nz

Foreign Exchange Market

FX Rates	Current*	Week ago	Month ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.7033	0.6966	0.7217	0.6015	FLAT	0.6950	0.7175
NZD/AUD	0.9233	0.9200	0.9269	0.9655	FLAT	0.9160	0.9460
NZD/JPY	77.17	77.06	78.43	65.55	FLAT/UP	75.60	79.20
NZD/EUR	0.5912	0.5941	0.6030	0.5536	FLAT	0.5880	0.6130
NZD/GBP	0.5132	0.5054	0.5161	0.4856	FLAT	0.5050	0.5380
TWI	74.2	73.5	75.1	68.71	FLAT	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

Last week was a bit of a nothing week as far as financial markets were concerned. A dearth of market-moving news/events kept most asset markets quiet, and this extended to currencies where the NZD/USD was confined to a sideways 0.7000-0.7070 range.

The one exception was GBP, where concerns about the efficacy of the Astra-Zeneca vaccine, which the UK has relied heavily upon for its rollout, saw GBP/USD shed about 2 cents over the week. NZD/GBP was swept back up to almost 0.5140 as a result. We don't expect the NZD/GBP rally to extend. Our friends at CBA believe that the GBP is a little oversold given the strong UK economic recovery. We suspect further gains in NZD/GBP will run out of steam around resistance at 0.5180-0.5200.

Beneath the quiet trading of last week, the steady improvement in market sentiment continued. US and European equity markets rose to fresh record highs, and the VIX index (a proxy for risk aversion) fell to pre-COVID lows. A slowing in the bond market sell-off, the impressive UK/US vaccine rollout, and the ongoing promise of more fiscal stimulus are all important drivers of such.

These factors are all NZD positives, both directly via bolstering investors' risk appetite, and indirectly via support for commodity prices. We continue to highlight the fact that fundamentals are supportive of a higher NZD/USD in time, and our estimated fundamental 'fair-value' range for the NZD/USD remains at 0.7100-0.7500.

However, for this week we suspect rallies in NZD/USD will continue to be capped around 0.7100. US data out this week should confirm the US recovery is gathering pace and this may proffer additional support for the USD. We also have the RBNZ meeting on Wednesday although, unlike the February meeting, this one should be fairly straight-forward and hence not confronting for markets. For NZD/AUD, Thursday's Aussie employment figures will be key. Another month of surprising gains would again throw the spotlight on whether the RBA can really hold down rates until 2024, posing additional headwinds for the cross. mike.jones@asb.co.nz

ASB foreign exchange forecasts

(end of quarter)

	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Mar-23
		<<actual	forecast>>				
NZD/USD	0.72	0.70	0.73	0.74	0.74	0.74	0.73
NZD/AUD	0.94	0.92	0.91	0.89	0.91	0.94	0.95
NZD/JPY	75	77	80	83	84	85	88
NZD/EUR	0.59	0.60	0.59	0.59	0.58	0.57	0.54
NZD/GBP	0.53	0.51	0.51	0.51	0.51	0.50	0.48
NZD/CNY	4.7	4.6	4.7	4.7	4.7	4.7	4.5
NZD TWI	75.1	73.9	75.2	75.4	75.5	75.5	74.6

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	0.25	UNCH	UP
90-day bank bill	0.33	0.34	0.32	0.45	UNCH	UP
2-year swap	0.46	0.45	0.52	0.45	UNCH	UP
5-year swap	1.09	1.11	1.18	0.61	UNCH	UP
10-year swap	0.00	1.95	1.90	1.00	UNCH	UP
10-year govt bond yield	1.75	1.82	1.73	0.98	UNCH	UP
Curve Slope (2s10s swaps)	-0.46	1.49	1.37	0.55	UNCH	DOWN

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

Market Recap

Local and global yields start the week lower, with a curve flattening bias. Last week's announcement by PM Ardern on the start of the trans-Tasman bubble on April 19 had little impact on local yields. Messaging by global central banks has reiterated the need for very low interest rates and downplayed the risks of the economy overheating. The RBA signalled it would not hike rates until 2024 at the earliest. Fed chair Powell and the flurry of Fed members cited that while the speedy vaccine rollout and policy stimulus had the US and global economy primed for stronger growth, COVID-19 remained a key risk and now was not the time to consider monetary policy tightening. The prospect of economic overheating was also downplayed by central banker's, with the uptick in inflation likely to prove brief. Higher than expected inflation data (Chinese CPI and PPI and US PPI) had a modest impact on yields.

Near-term interest rate outlook

Market pricing has a full 25bp OCR hike priced in by late 2022, which is a shade later than our OCR view (August 2022), but consistent with our view of the risk profile. Local data this week (March ECT spending) should highlight the potential for the NZ economy to be in recession, dampening yields. At Wednesday's Monetary Policy Review (see our preview [here](#)), the RBNZ will likely stick to the script, deliver a dovish policy assessment and reiterate there was no hurry to unwind current monetary stimulus. On the LSAP programme, we expect the Bank to maintain the \$100bn mid-2022 ceiling and keep flexibility to alter the pace of asset purchases so as to provide liquidity for markets and dampen yields. Weekly RBNZ asset purchases have been scaled back of late (\$420m in NZ government bond purchases this week), in line with the lower NZ bond issuance profile by NZDM (\$300m this week) and should weigh on bond yields at the margin. We also expect the tone from other central banks – including speeches by FOMC Chair Powell and other Fed members – to downplay the risks of economic overheating and a pronounced lift in inflation. For now, at least, the rise we expect in forthcoming inflation prints (including March US CPI (Tue), Eurozone CPI (Fri) and NZ Q1 CPI on 21st April), should have a modest impact on yields. This may be harder to brush off if activity and employment data - including March US retail sales, Q1 Chinese GDP and the March monthly Chinese retail sales, industrial production, Australian labour market data – should continue to show the global recovery heating up more quickly than earlier thought.

Medium-term outlook

We expect the RBNZ to continue to trim LSAP programme and to halt purchases altogether from 2022, prior to raising the OCR from August 2022 - with risks of a slightly later start to RBNZ tightening. The OCR is expected to reach 1.25% in March 2024, slightly below neutral levels. Our bias is for shorter-term yields to edge up over the next few years and for the yield curve to flatten, with longer-term NZ yields to peak at historically-low levels. mark.smith4@asb.co.nz

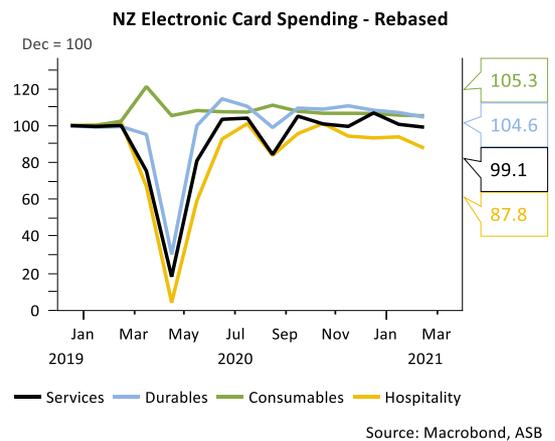
ASB interest rate forecasts

(end of quarter)	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Mar-23
		<<actual	forecast>>				
NZ OCR	0.25	0.25	0.25	0.25	0.25	0.25	0.75
NZ 90-day bank bill	0.27	0.35	0.30	0.30	0.30	0.35	0.90
NZ 2-year swap rate	0.28	0.47	0.57	0.67	0.77	0.87	1.27
NZ 5-year swap rate	0.54	1.12	1.22	1.32	1.42	1.52	1.92
NZ 10-year swap rate	0.98	1.96	2.01	2.06	2.11	2.16	2.36
NZ 10-year Bond	0.99	1.78	1.86	1.91	1.96	2.01	2.21

Domestic events

Data	Date	Time (NZT)	Market	ASB
Electronic Card Transactions, Retail, Mar, % mom	13/04	10:45 am	-	-1.5
RBNZ Monetary Policy Review (OCR)	14/04	2:00 pm	-	0.25%
Food Price Index, Jan, % mom	15/04	10:45 am	-	1.0

We expect a second consecutive monthly fall in card spending in March. **February/March are the peak months for overseas tourism to NZ and headwinds from the border restrictions are expected to be the most acute at this time of year.** The shifting of Alert Level restrictions has likely disrupted spending, with NZ starting March at Alert Level 2, while moving to Alert Level 1 on March 7. Auckland started March at Alert Level 3, dropping to Level 2 (March 7) and Level 1 (March 12). Our internal card spending data showed a dip in weekly spending at the start of the month and a subsequent recovery. Hospitality and accommodation spending are expected to be weak, and consumers are likely to already have their fill of durable goods. Consumer spending is likely to remain lukewarm over 2021 as slowing population growth hits home.



We expect the RBNZ to strike a similar tone on Wednesday's Review to February's Monetary Policy Statement, namely that the RBNZ needs to "maintain the current stimulatory level of monetary settings in order" to meet its objectives, and that "considerable time and patience" will be needed. Events since February have been mixed. The global outlook is improving, and some key NZ export prices are firm. Domestically, since the Government's recent housing announcements that target property investors there is more uncertainty around the housing market's outlook and any flow-on impacts to the economy. Although we don't see the real economic impacts as being material, the policy changes are yet another reason for the RBNZ to remain cautious. Meanwhile, cost-push inflation pressures from supply chain disruption are likely to be looked through for the time being.

A seasonal increase in March food prices is expected followed by sizeable February declines. We expect food prices to increase by approximately 0.8% over Q1, contributing roughly 0.15 percentage points to the Q1 CPI. **Rising prices for dairy and some other global food commodity prices point to a firming outlook for retail food prices over 2021.**

Major International Events for the week ahead

Data	Date	Time (NZT)	ASB
China Trade Balance, March, US\$bn	13/04	-	50
UK GDP, Feb, %mom	13/04	6:00 pm	-
US CPI, March, %yoy	13/04	12:30 am	2.5
Australia Unemployment, March, %	15/04	1:30 pm	5.6
US Retail Sales, March, %mom	15/04	1:15 am	6.0
US Industrial Production, March, %mom	15/04	1:15 am	3.5
China GDP, Q1, %yoy	16/04	2:00 pm	19.6

* Forecasts and commentary originally published by CBA Global Markets Research Friday 9 April at 1:41 pm

We estimate **China's trade surplus** expanded in March. China is benefiting from the recovery in the world economy, particularly the US. Still, the momentum in Chinese domestic demand supports imports, particularly of commodities.

We are expecting another strong **employment result for Australia** over March after a very strong February survey. We see employment growth of 45k and an unchanged participation rate which would drive the unemployment down to 5.6%.

The extreme weakness in early 2020 will flatter all economic data presented in year-to terms. Still, we expect **Chinese economic growth** to be solid albeit growth momentum will ease as policy-makers become less supportive now that the crisis is largely over.

The composite PMI suggests the contraction in **UK GDP** will ease further over February. But leading indicators point to a sharp recovery in economic activity in the next few months.

We expect headline **US CPI** jumped to 2.5%yoy in March, reflecting a combination of base effects and a further increase in gasoline prices. The US Federal Reserve has said it will look through any near-term surges in inflation caused by base effects. We expect core CPI ticked higher towards 1.5%. Nevertheless, ongoing economic slack in the US economy will remain a drag on core inflation for some time.

We expect another surge in **US retail sales** took place over March because the latest round of stimulus cheques (\$US1,400) started to be distributed. We expect high gasoline prices will have further boosted headline retail sales in March.

We expect **US industrial production** rebounded in March after poor weather in February hampered activity. At the same time, the economic recovery is underpinning demand and should continue to support industrial production in coming months. For example, the sharp rise in capex plans bodes well for continued growth in industrial production.

Key Forecasts

ASB NZ economic forecasts

	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Mar-23
	<< actual	forecast >>					
GDP real - Q%	-1.0	-0.2	1.1	1.0	-0.8	-0.6	0.5
GDP real - A%	-0.9	0.2	13.8	0.9	1.2	0.7	4.5
GDP real - AA%	-3.0	-3.0	3.0	3.2	3.7	3.9	2.7
NZ House Prices (QV Index) - A%	15.1	19.7	20.0	15.4	9.1	2.8	5.1
CPI - Q%	0.5	0.9	0.6	0.5	0.4	0.5	0.7
CPI - A%	1.4	1.6	2.6	2.5	2.4	2.0	2.5
HLFS employment growth - Q%	0.6	0.0	0.1	0.3	0.3	0.4	0.5
HLFS employment growth - A%	0.7	-0.3	0.0	1.1	0.7	1.1	2.0
Unemployment rate - %sa	4.9	5.0	5.2	5.4	5.4	5.3	4.6

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

	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Mar-23
(end of quarter)		<< actual	forecast >>				
NZ OCR	0.25	0.25	0.25	0.25	0.25	0.25	0.75
NZ 90-day bank bill	0.27	0.35	0.30	0.30	0.30	0.35	0.90
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NZ 10-year swap rate	0.98	1.96	2.01	2.06	2.11	2.16	2.36
NZ 10-year Bond	0.99	1.78	1.86	1.91	1.96	2.01	2.21

ASB foreign exchange forecasts

	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Mar-23
(end of quarter)		<< actual	forecast >>				
NZD/USD	0.72	0.70	0.73	0.74	0.74	0.74	0.73
NZD/AUD	0.94	0.92	0.91	0.89	0.91	0.94	0.95
NZD/JPY	75	77	80	83	84	85	88
NZD/EUR	0.59	0.60	0.59	0.59	0.58	0.57	0.54
NZD/GBP	0.53	0.51	0.51	0.51	0.51	0.50	0.48
NZD/CNY	4.7	4.6	4.7	4.7	4.7	4.7	4.5
NZD TWI	75.1	73.9	75.2	75.4	75.5	75.5	74.6

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