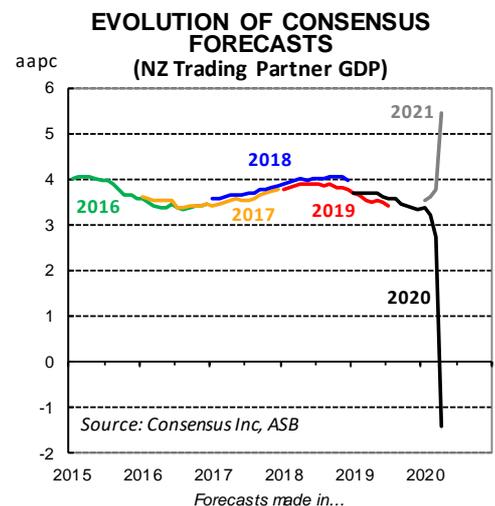


Economic Weekly

20 April 2020

Managing economic uncertainty

Economic forecasting is challenging in the best of times – often described as more of an art than a science. In these uncertain and unprecedented times, forecasting becomes a stab in the dark. Given these limitations, **users of economic forecasts have two options to manage uncertainty - alternative scenarios and forecast averaging.** Running multiple scenarios can help users of forecasts to visualise and quantify the relative impacts if events turn out different than we assume – because if there is one thing we can be certain of, it is our forecasts are unlikely to pan out as we expect. **We describe two alternative scenarios to our central economic forecasts on Page two,** with the link to our full report below. **The second option is to average a range of forecasts (ideally from different forecasters).** At times like these when economic forecasts are likely to diverge significantly due to small differences in assumptions, an average of forecasts – or the consensus forecast – is another way to account for a wide range of views. We use the Consensus Economics survey to guide our forecasts for trading partner economic growth – and while we may not know the exact size of the coming global recession, the direction for the global economy is fairly clear. Take care all. jane.turner@asb.co.nz



Recent COVID-19 publications

ASB Economic forecasts and monitoring:

- [ASB COVID-19 Chart pack](#)
- [COVID-19 and the economic path ahead \(central forecasts\)](#)
- [COVID-19 possible paths in an uncertain future \(alternative scenarios\)](#)

Financial market trends:

- [COVID-19: Market stocktake and what we are watching](#)
- [COVID-19: Market impacts, responses, and ideas](#)
- [ASB Podcast for investors](#)

Policy response:

- [RBNZ QE upside likely in May](#)
- [RBNZ policy actions](#)
- [RBNZ OCR cut March 16](#)
- [Fiscal fights back](#)

Industry specific analysis and other:

- [Farmshed Economics: COVID-19 what we know and what we don't](#)
- [Housing immunity about to be tested](#)
- [Thinking about coronavirus impacts on business: Be prepared – it doesn't hurt](#)
- [Government support – quick guide to accessing it](#)

Where to find support

- [ASB financial support package](#)
- [Government support package](#)
- [COVID-19 alert system explainer](#)

Some of the future economic paths

- There are a number of possible paths for the NZ economy. The range of outcomes is wide.
- We summarise three scenarios that capture our central view, flanked by upside and downside scenarios.
- Where the economy actual heads up is still highly uncertain. Having a degree of flexibility in your plans is paramount if you want to take advantage of the opportunities that arise. It is also vital to be informed.

Last week the team published 3 economic scenarios, all laying out possible paths for the economy (the full details, including figures, are [here](#)). They range from a fairly sharp ‘V’ rebound with little lasting economic damage, through our central ‘U’ view, to a fairly downbeat ‘L’ in which the current dip is large and recovery is drawn out.

As you can see, the outlook is a murky alphabet soup – some people have thrown a ‘W’ into the pot as well. Relying on a single point forecast of a particular outcome is not as useful as considering a range of readily plausible outcomes. So, as we come out of lockdown (shortly, hopefully), it will be a good idea to consider a range of different paths for any business you are involved in and a set of well thought out actions you would take in each one. **We hope our scenarios will give you some food for thought. Use your imagination also as to how the operating environment could now be different for your business. As they say, plan for the worst but hope for the best – and keep up with all the latest developments to help you gauge which broad direction you are heading in.**

Without further ado, here are three different paths the economy could take. We have linked them to the path the virus takes as its ease of containment or incidence of flare-ups is what will ultimately dictate people’s behaviours and government responses. How we adapt as people will also have an influence over the longer term, and we’ve put some parting thoughts after the scenario descriptions.

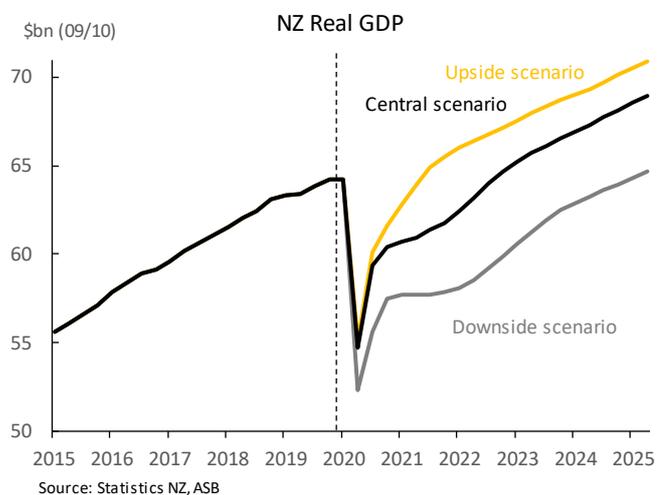
The Central ‘U’

This is our view of the most likely path for the NZ economy. It assumes that the impacts of COVID-19 on the NZ and global economies are significant but will hopefully prove to be short-lived. Recent signs indicate that efforts to flatten the curve (slow the advance of the outbreak) look to be bearing fruit, both globally and in NZ. Nevertheless, COVID-19 is expected to deliver a significant global hit. Widespread economic lockdown measures put in place look set to see the global economy shrink. We expect the global economy to contract by close to 2 ½% over 2020 before a modest 3% rebound for 2021.

The Level 4 lockdown will be gradually relaxed a week or so after April 23, with a gradual relaxation in Alert levels over the next few months. The NZ economy is expected to experience a sizeable economic contraction in Q2 but pent-up demand and the restarting of activity will trigger a rebound in 2020H2. Falls in business investment will be more sizeable given the hit to demand and subsequent recovery more gradual as capacity pressures recede. We envisage that the NZ economy will contract by roughly 6% over 2020, before pent-up demand, policy stimulus triggers a moderate recovery. The level of real GDP moves above pre-crisis levels in late 2022. The unemployment rate approaches 9% in 2020, easing towards 6% by the end of 2023.

Upside scenario

Here we put on our rose-tinted glasses and assume that just about everything goes right. The COVID-19 outbreak, while nasty, is not as virulent as initially feared. Global cases of the outbreak stabilise and then ease as containment measures prove effective. There are only occasional mild flare-ups, which impose only modest economic disruption. The Chinese economy quickly restarts from its early 2020 slump, with wider trading partner activity well onto the road to recovery in the second half of 2020. NZ’s goods exports are in strong demand. International visitor arrivals are



expected to progressively recover from later this year as different overseas markets get on top of the outbreak.

In NZ, the Level 4 lockdown contains the spread of the outbreak, with Alert levels progressively scaled down from April 23 throughout the country. The disruption to economic activity is not as large as previously feared. Demand for essential goods and services is strong. Moreover, firms and workers in non-essential activities quickly adapt to new ways of working, with less severe impacts on activity. The economy will emerge from the lock-down with more impetus, with pent-up demand triggering a rebound in demand after the lock-down ends. Actions by the RBNZ and Government prove effective in cushioning the economy and minimising job losses and boosting subsequent economic activity. NZ GDP moves above pre-crisis levels by the second half of 2021. The unemployment rate is expected to peak at just under 7% this year and steadily decline thereafter.

Downside scenario

Just about everything that can go wrong, does in this scenario. COVID-19 proves to be very difficult to contain, with regular flare-ups across the globe causing widespread, longer-lasting and sizeable economic disruption and economic dislocation. The rebound in Chinese economic activity is short-lived, with a deep global recession over 2020 and into 2021. The NZ Terms of Trade fall, with global consumers reallocating expenditures to cheaper alternatives and reducing demand for non-essential items.

In NZ, a resurgence of new cases sees the Level 4 lockdown extended to the end of May, with some regions exiting later. The impacts of the lockdown persist for longer, with firms and households remaining in hibernation. GDP declines by around 10% over 2020. Job losses and firm closures are large and will temper the rebound from pent-up demand. A more sizeable contraction is expected for domestic demand, with consumption spending sharply lower and business investment down by one-fifth over 2020. The recovery will be sluggish over 2021 and beyond given hits to economy-wide balance sheets, and the impact of continued disruptions from the outbreak on lowering productivity growth. It will not be until early 2025 that the level of real GDP is back above pre-crisis levels.

Furthermore, policy actions prove to have less of a supportive impact than envisaged. The unemployment rate moves into double-digits in late 2020 and only gradually declines thereafter, ending 2022 at around 9% and only gradually drifting lower thereafter.

Parting thoughts...

There are many paths forward, with all sorts of permutations based off whether the virus truly gets eliminated in NZ or merely contained, how quickly NZ eases back through its COVID Levels, how resilient businesses are to the disruption of lockdown, the extent of the hit the global economy takes. Over the longer term, factors such as whether there is any lasting immunity against COVID-19 and any future mutations will matter – will it actually be safe to interact once more or will distancing become a long-term fact of life? We will gradually find answers to which path of the permutation tree we are heading down: some answers could surface within weeks while others take years.

The cliché is that the future is always uncertain – and for the timing being there will be so many questions none of us have good answers for. We are all going to need to become adept at making the decisions we need to make in an environment of high uncertainty, be conscious of minimising the consequences of getting it wrong and improve our resilience. The encouraging thing to bear in mind is the adaptability of humankind and the sheer amount of global intellectual power that will be focused on overcoming the challenges that COVID-19 has thrown up.

nick.tuffley@asb.co.nz

Foreign Exchange Market

FX Rates	Current*	Week ago	Month ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.6037	0.6015	0.5752	0.6716	FLAT/DOWN	0.5860	0.6130
NZD/AUD	0.9486	0.9655	0.9804	0.9355	FLAT/DOWN	0.9410	0.9530
NZD/JPY	64.90	65.55	63.39	75.13	FLAT/DOWN	62.00	66.00
NZD/EUR	0.5553	0.5536	0.5357	0.5945	FLAT	0.5400	0.5600
NZD/GBP	0.4829	0.4856	0.4948	0.5147	FLAT	0.4760	0.4900
TWI	68.8	68.7	67.0	72.68	FLAT	N/A	N/A

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

NZD Recap

Currency markets continued to stabilise last week, as investors slowly price out the extreme negativity of March. The NZD/USD has spent most of April to date chopping around inside a relatively narrow 0.5850-0.6100 range. Compare this to the wild, almost 10 cent wide, range of March (0.5500-0.6450).

The VIX index (a proxy for global risk aversion) has eased from above 80% in March to around 38%, and the MSCI World Equity Index is up around 40% from its recent lows. Contributing factors to the sentiment improvement have been COVID-19 data showing a clear slowing in the spread of the virus, an end in sight for the lockdowns in place across many parts of the world (heralding the start of economic recovery), and aggressive action from policy makers to combat the virus. On the latter, there was more optimism for markets on Friday following the release of the White House's plan to reopen the US economy and the Fed's tapering of daily bond purchases to US\$15b, from \$30b the week before.

In currency markets, the Fed's actions to improve USD liquidity and backstop lending to US corporates have been particularly effective at quelling the USD shortage and bringing to a halt the squeeze higher in the greenback. This was a key factor driving the NZD/USD's recovery to almost 0.6100 last week.

Short-term outlook

We're wary that markets' recent optimism is going to be tested, as economic data for April begin to reveal just how much damage COVID-19 disruptions has done to the global economy. US economic data in particular have been coming in weaker than expected, and this may continue this week. We also expect US corporate earnings reports will reinforce the bleak economic outlook. Global April PMIs will be particularly important to watch this week (Thursday). Further flare ups in global risk aversion would support the USD and see NZD/USD squeezed back below 0.6000.

More generally, while the NZ economy may well emerge from the COVID-19 crisis in better shape than some, this doesn't not necessarily mean NZ dollar outperformance will follow. NZ's commodity export prices remain the NZD's most important driver. And it's hard to see commodity prices racing away in an environment of recessionary global growth and oil prices hitting 18-year lows on a near daily basis. At the same time, we argued in a [recent note](#) that further material declines in the NZD look unlikely, and this remains our view. For this week, we favour the downside for choice, but expect any NZD/USD selloffs to be limited to initial support around 0.5860. mike.jones@asb.co.nz

ASB foreign exchange forecasts

(end of quarter)

	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Mar-22	Mar-23
		<< actual	forecast >>					
NZD/USD	0.67	0.60	0.55	0.58	0.60	0.61	0.64	0.65
NZD/AUD	0.96	0.97	0.96	0.97	0.95	0.94	0.94	0.94
NZD/JPY	73	65	54	58	61	63	67	69
NZD/EUR	0.60	0.54	0.47	0.51	0.53	0.54	0.57	0.58
NZD/GBP	0.51	0.49	0.46	0.47	0.48	0.48	0.49	0.50
NZD/CNY	4.7	4.3	3.9	4.1	4.2	4.3	4.5	4.6
NZD TWI	73.8	68.8	63.7	66.6	68.1	68.8	71.5	72.4

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	1.75	UNCH	UP
90-day bank bill	0.39	0.45	0.69	1.77	UNCH	UP
2-year swap	0.34	0.45	0.68	1.65	UNCH	UP
5-year swap	0.49	0.61	0.92	1.81	UNCH	UP
10-year swap	0.89	1.00	1.37	2.26	UNCH	UP
10-year govt bond yield	1.12	0.98	1.47	1.97	UNCH/UP	UP
Curve Slope (2s10s swaps)	0.55	0.55	0.69	0.61	UNCH	DOWN

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

Market Recap

As we highlighted last week, the tick-up in yields proved to be short lived. COVID-19 is casting a shadow over the global economy, with the string of poor global data triggering a renewed bout of risk aversion. Chinese GDP contracted by a record 6.8% yoy in Q1. The IMF Global Outlook highlighted a sizeable and geographically broad-based slump in global economic activity for 2020. US Treasury yields rose overnight, buoyed by the lift by global equities, the reduced Federal Reserve bond purchases and hopes the US economy will soon be restarted. Bills-OIS spreads have narrowed to around 20bps - about half of that at the peak of the crisis, with credit spreads also narrower. NZ yields eased after RBNZ Governor Orr reiterated that a negative OCR is possible beyond early 2021 and that the RBNZ could increase quantitative easing (QE) as NZ Government borrowing rises. Courtesy of RBNZ QE the effective (or shadow) OCR is already 'deeply negative' with the RBNZ's \$30bn of QE equivalent to 150bps of easing. The market largely ignored today's much stronger than expected Q1 NZ CPI data (+0.8% qoq, 2.5% yoy). We expect CPI inflation to eventually move towards the lower bound of the 1-3% CPI inflation target, keeping NZ yields low.

Near-term NZD interest rate outlook

Monday's 4pm announcement on when NZ's Level 4 lockdown will be lifted will have a crucial bearing on the NZ economic and interest rate outlook, as will be decisions on easing restrictions globally. The US Government has issued guidelines towards starting the US economy (positive for global yields), but we are wary this might be too premature given a number of countries in Europe extending lockdowns through to mid-May. Picking the direction of yields is a lottery and data will take a back seat, with upward surprises largely discounted given the changed economic landscape. On Tuesday, Reserve Bank of Australia (RBA) Governor Lowe will deliver an economic and financial update speech, with the RBA meeting Minutes also due. Any comment by the RBA on the economic impact of COVID-19 on Australia and the RBA's continued asset-purchasing program will be closely watched. NZ QE is set to continue, albeit at a slightly less frenetic pace, the RBNZ has signalled a scaled down \$1.35bn of Government bond purchases and \$130m of LGFA paper this week, below last week's \$1.8bn of NZ Government bonds and \$140m of LGFA purchases. We expect the RBNZ will increase its QE programme to \$40-50bn in May, with more QE beyond that highly likely given the weak fiscal outlook.

Medium-term outlook

Central bank policy rates are expected to maintain highly accommodative settings. Given the risks to the outlook we don't expect the OCR to move above its 0.25% operational lower bound until 2024 at the earliest. The OCR could move lower if the RBNZ deemed this to be operationally feasible. Weak global growth, negative risks and the prospect of central bank asset purchases should cap long-term NZ interest rates, although we are wary over the impacts of sizeable global and NZ public debt issuance on government bond yields. mark.smith4@asb.co.nz

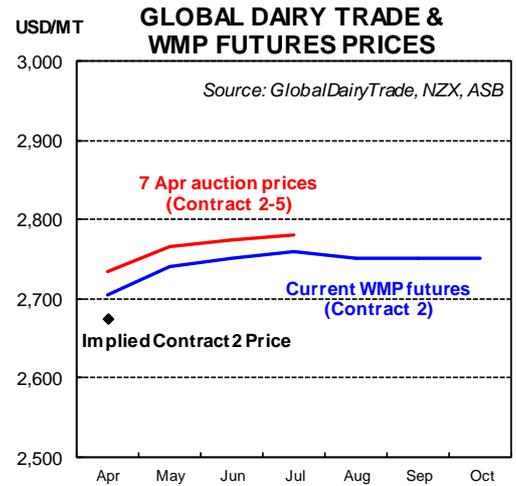
ASB interest rate forecasts

	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Mar-22	Mar-23
(end of quarter)		<< actual	forecast >>					
NZ OCR	1.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25
NZ 90-day bank bill	1.29	0.51	0.50	0.50	0.50	0.50	0.50	0.50
NZ 2-year swap rate	1.26	0.53	0.50	0.50	0.50	0.50	0.50	0.60
NZ 5-year swap rate	1.45	0.63	0.65	0.65	0.65	0.65	0.65	1.05
NZ 10-year swap rate	1.78	0.93	1.00	1.00	1.50	1.50	1.10	1.50
NZ 10-year Bond	1.65	1.03	1.40	1.40	1.40	1.40	1.40	1.45

Domestic events

Data	Date	Time (NZT)	Market	ASB
GlobalDairyTrade auction, whole milk powder, % change	21/04	overnight	-	0.0

We expect whole milk powder (WMP) prices to stabilise further and to come in largely unchanged at the GlobalDairyTrade auction overnight Tuesday. A fortnight ago, WMP prices rose 2.1%, breaking a run of four consecutive COVID-19-generated price falls. At this juncture, futures pricing points to a circa 1% WMP fall. However, futures have been overshooting actual auction price falls over recent auctions.



Major International Events for the week ahead*

Data	Date	Time (NZT)	ASB
RBA Economic And Financial Update, Gov. Lowe	21/04	5:00 pm	-
RBA Board Meeting Minutes, April	21/04	1:30 pm	-
UK ILO Unemployment Rate, February, %	21/04	6:00 pm	3.9
UK CPI, March, %yoy	22/04	6:00 pm	1.7
UK Retail Sales, March, %yoy	22/04	6:00 pm	2.5
Australia CBA PMI, April	23/04	-	-

Originally published by CBA Global Markets Research on Thursday 17th April at 14:07 pm

The **Reserve Bank of Australia's Governor Philip Lowe will deliver an economic and financial update**. Any comment on the impact to Australia's economy from COVID-19 will be eagerly awaited by the market, particularly given the forecasts by Treasury and the IMF for Australia's labour market.

In the **RBA's** April meeting, both the cash rate and the target for the yield on 3-year ACGBs were retained at 0.25%. The RBA stated that they expect a "very large" economic contraction in Q2 20. Of interest will be further comment on the hit to GDP and the labour market. The market will also note any further **comment** on the rate of the RBA's asset purchases.

In **Australia**, the **CBA Composite PMI** plunged in March to 39.4, its weakest reading in the survey's relatively short history. The services sector drove the weakness, with the index diving to 38.5. The manufacturing PMI has slipped into contractionary territory, printing at 49.7 which is marginally below the critical 50 level that separates expansion from contraction.

In the **UK**, data will likely capture some of the initial negative impact on the labour market from the lockdown. The UK was put into lockdown on 23rd March. The Department for Work and Pensions reported a sizable increase in Universal Credit applications during the last two weeks of March, consistent with a surge in the **unemployment** rate.

UK core and headline CPI inflation printed at 1.7% in February. Bank of England policy maker Silvana Teneyro expects inflation to fall below 1% in coming months because of the collapse in oil prices. Still, the Office for National Statistics warned that the coronavirus will make it difficult to interpret CPI data in the next couple of months, in part, because of the technical challenges to measuring inflation during the containment period.

In the **UK**, the British Retail Consortium March **retail sales** monitor points to significant decline in non-food retail sales.

Key Forecasts

ASB NZ economic forecasts

	Dec-19 << actual	Mar-20 forecast >>	Jun-20	Sep-20	Dec-20	Mar-21	Mar-22	Mar-23
GDP real - Q%	0.5	0.0	-14.7	8.5	1.5			
GDP real - A%	1.8	1.3	-13.6	-7.0	-6.2	-6.3	2.7	4.8
GDP real - AA%	2.3	1.9	-2.1	-4.4	-6.4	-8.3	4.0	4.5
CPI - Q%	0.5	0.8	0.0	0.2	0.1			
CPI - A%	1.9	2.5	2.0	1.5	1.1	0.9	1.2	1.4
HLFS employment growth - Q%	0.0	0.0	-5.4	-1.4	0.1			
HLFS employment growth - A%	1.0	1.0	-5.2	-6.8	-6.7	-6.5	3.0	2.7
Unemployment rate - %sa	4.0	4.4	8.7	8.8	8.5	8.4	7.3	6.4
Annual current account balance as % of GDP	-3.1	-3.2	-3.6	-3.7	-4.2	-4.7	-3.3	-2.3

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

(end of quarter)	Dec-19 << actual	Mar-20 forecast >>	Jun-20	Sep-20	Dec-20	Mar-21	Mar-22	Mar-23
NZ OCR	1.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25
NZ 90-day bank bill	1.29	0.51	0.50	0.50	0.50	0.50	0.50	0.50
NZ 2-year swap rate	1.26	0.53	0.50	0.50	0.50	0.50	0.50	0.60
NZ 5-year swap rate	1.45	0.63	0.65	0.65	0.65	0.65	0.65	1.05
NZ 10-year swap rate	1.78	0.93	1.00	1.00	1.50	1.50	1.10	1.50
NZ 10-year Bond	1.65	1.03	1.40	1.40	1.40	1.40	1.40	1.45

ASB foreign exchange forecasts

(end of quarter)	Dec-19 << actual	Mar-20 forecast >>	Jun-20	Sep-20	Dec-20	Mar-21	Mar-22	Mar-23
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NZD/JPY	73	65	54	58	61	63	67	69
NZD/EUR	0.60	0.54	0.47	0.51	0.53	0.54	0.57	0.58
NZD/GBP	0.51	0.49	0.46	0.47	0.48	0.48	0.49	0.50
NZD/CNY	4.7	4.3	3.9	4.1	4.2	4.3	4.5	4.6
NZD TWI	73.8	68.8	63.7	66.6	68.1	68.8	71.5	72.4

ASB Economics & Research

Chief Economist
Senior Economist
Senior Economist
Senior Economist
Senior Rural Economist
Senior Economist, Wealth
Publication & Data Manager

Nick Tuffley
Mark Smith
Jane Turner
Mike Jones
Nathan Penny
Chris Tennent-Brown
Judith Pinto

nick.tuffley@asb.co.nz
mark.smith4@asb.co.nz
jane.turner@asb.co.nz
mike.jones@asb.co.nz
nathan.penny@asb.co.nz
chris.tennent-brown@asb.co.nz
judith.pinto@asb.co.nz

Phone

(649) 301 5659
(649) 301 5657
(649) 301 5853
(649) 301 5661
(649) 448 8778
(649) 301 5915
(649) 301 5660

www.asb.co.nz/economics

@ASBMarkets

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