

TONY'S VIEW

Input to your Strategy for Adapting to Challenges

Feel free to pass on to friends and clients wanting independent economic commentary

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My Aim

To help Kiwis make better decisions for their businesses, investments, home purchases, and people by writing about the economy in an easy to understand manner.

2021

Welcome to the first issue of Tony's View for 2021. I'm going to start the year with a simple run-through of the negative then positive factors which will affect our pace of growth this year. My view is that the positives easily outweigh the negatives, but feel free to form your own opinion.

Let's start with some of the factors which will restrain the pace of growth in our economy this year and into 2022.

Rising Kiwi dollar

The NZD has been boosted by our good Covid and economic performance over 2020, and we are riding slightly on the coattails of an Aussie dollar boosted by surging iron ore prices offsetting concerns about trade attacks from China. Further gains in the NZD look likely this year with views on interest rates likely to continue their late-2020 turning away from falling scenarios.

Switch in spending back to international travel

As the year progresses, people are likely to start setting funds aside for planned travel once the borders eventually fully reopen. It does not require actual border opening for this saving of money and diversion from other areas of spending to occur. In that regard, areas of spending cutbacks are likely to be those where things surged the most tremendously over 2020 – but picking timing of these pullbacks is impossible. Maybe late in the year?

Business closures

Some businesses in our most heavily affected sectors will have been burning through reserves to get through and not all will be able to continue to do so as we await the return of international tourists and foreign students. Some business closures still look likely. Additionally, not all businesses are nimble enough to respond to the sharp changes in what we do and how we do it which Covid-19 has accelerated. A more generalised "weeding out" of those unable to keep up is likely this year.

Labour shortages

As noted at the start of this crisis, New Zealand has a shortage of skilled, unskilled, motivated, and unmotivated staff. This shortage got hidden for a while by layoffs in the services sector caused by the effects of Covid-19. But the past three months has produced a rash of business complaints that they cannot find the staff they want. Inability to source staff will boost wages and force investment in labour-saving technologies. But it will also make business expansion more difficult and slow down the face of output growth.

39% personal income tax rate

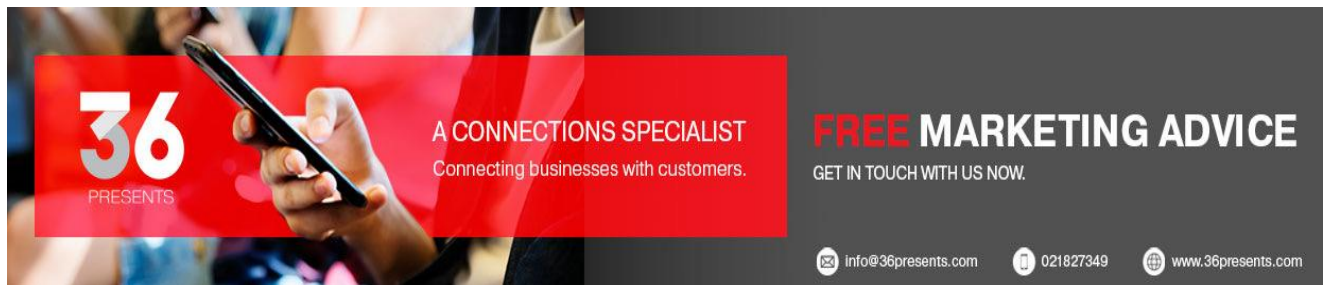
Imposition of this ideologically driven new tax bracket from \$180,000 may have some minor restraining impact on spending. But if so, the effects are likely to be impossible to find in any broad measure of the economy.



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2021 Positives

The list of factors likely to boost growth in our economy this year and next is far longer than the list of factors which will retard growth – hence my positive growth and house price outlooks, and warning about upside risks for the NZD and medium to long-term interest rates.

Low interest rates

Risks are shifting upward but actual levels will remain very low by historic standards for the next two years and this will incentivise people to spend while curtailing willingness to save. Note however, some people will save more in order to meet nominal wealth targets ahead of retirement.

Household deposits

The level of household deposits in banks at the end of November was about \$9bn more than one would have expected without Covid-19. This extra level of cash wealth will help underpin consumer spending.

Banks lending more

As bankers grow less concerned about the economic outlook, they are likely to reopen their lending books for the business sector and also increase willingness to fund home purchases for the self-employed and people working in the sectors most heavily affected by the pandemic.

Labour demand

Businesses have been quickly reminded that for many, their biggest problem heading into Covid-19 was a shortage of labour. This factor likely caused many to reverse redundancy plans from perhaps July onwards, and to more recently restart active recruitment. Good labour demand will raise job security, and while wages growth is likely to remain muted for the next couple of years, the enhanced job security will boost willingness of employed people to spend.

Business capex cycle catchup

Businesses naturally slashed their capex plans during the pandemic, and many will still be cautious. But investment intentions have moved back up to a three-year high while business confidence is back to levels last seen before Labour won the 2017 general election. A lift in the business capex cycle is likely to get underway this year, assisted by the need to boost labour-saving technology, and low borrowing costs.

Residential construction boom

If we strip out the lockdown effects, then we could not strongly say that the pandemic has led to any decline in house construction. In fact, with people focusing on their nests, redirecting money from overseas travel, responding to a structural shortage of listings, and bringing plans forward in time, the house building sector is likely to have a boom which will last for the next five years.



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Infrastructure spending

It is extremely unlikely that the government and public service will have either the expertise or the ability to source sufficient labour to make much headway on their list of supposed shovel-ready projects. Nonetheless, higher infrastructure spending is likely – though how councils will fund the long-overdue maintenance which they need to do on pipe systems is going to be a challenge. One option is the new option created by the government last year to ring-fence loan servicing costs for a project to those gaining benefits over 25-50 years.

<https://www.beehive.govt.nz/release/new-infrastructure-funding-tool-build-housing-developments-faster>

Good export prices

The country's terms of trade are sitting just below a record level, and recently prices have been improving for our biggest export sector – dairying. With world growth set to improve, prospects look good for our export prices over the coming two years.

Improving offshore growth helping exports

More generally, rising world optimism once vaccination programmes fully hit their straps over the next two months will tend to boost global growth optimism. This is traditionally positive for ourselves as primary product exporters.

Foreign tourists returning

In particular, as prospects brighten in a few months offshore, talk will naturally arise of borders reopening, and anticipation of foreign tourists returning to New Zealand over 2022 will drive investment in the sector here.

Expectations of a net immigration boom when borders reopen

There is no model which can possibly tell us what net migration flows will do once the borders reopen. The chances are that Kiwis in New Zealand are over-estimating the number of expats who will return come 2022. But we will be well into

2022 before such realisations kick in, and by then our economy will have received a boost from extra upward pressure on house prices and general optimism.

Anticipation of foreign students returning from 2022.

Perhaps late this year foreign students will be allowed to start returning in small numbers. But the big flow back is not likely to happen until 2022.

Positive house price wealth effect

More people own houses than are in the market for the first time looking to make a purchase, by a factor of perhaps up to ten times. Rising prices will make people feel wealthier and this will tend to generate some extra spending of that paper wealth.

In the absence of something new and nasty coming along, the chances seem good that our economy will record a fairly firm growth rate this year. A key factor contributing to the growth will be people's focus on the post-vaccination period and the expected return of foreign visitors and students. This will affect their behaviour now with regard to investment and hiring decisions.

Because of the uniqueness of this situation, the way I will tend to write about things this year will involve discussion of 2021 and 2022 together. Plus, over the next few months I'll be shifting my commentary away from the pandemic topic more back toward areas of focus before Covid-19 came along.

These areas include the structural shortage of labour and what businesses need to do to handle it, a shift in business price-setting ability, pressures to adopt policies addressing issues like climate change and use of plastics, the need to invest for flexibility and adaptability, plus the need to finance growth less through reliance on bank debt.

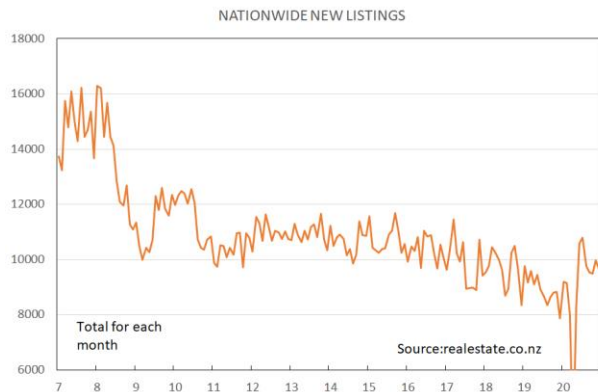
All the best to everyone for 2021-22 and don't be shy of emailing me should you have a question.

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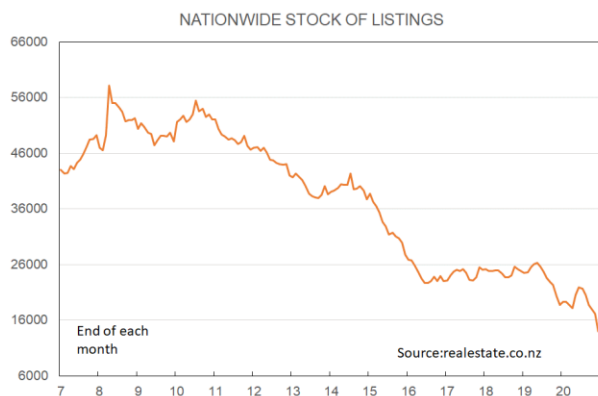
New Zealand's Housing Markets

Listings Shortage

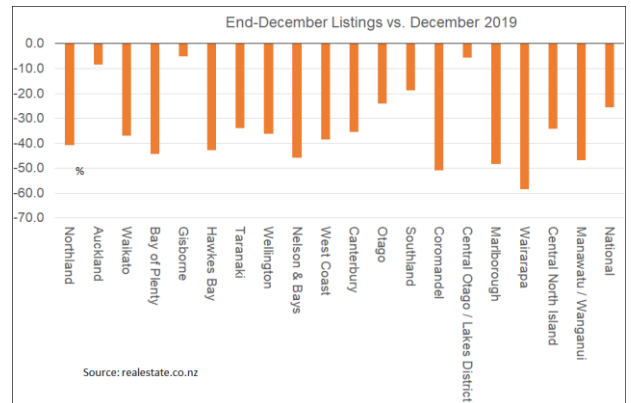
Last week realestate.co.nz released their monthly Property Report and it showed us that while there is a strong flow of new property listings coming forward, sales levels are so high that the stock shortage continues to worsen.



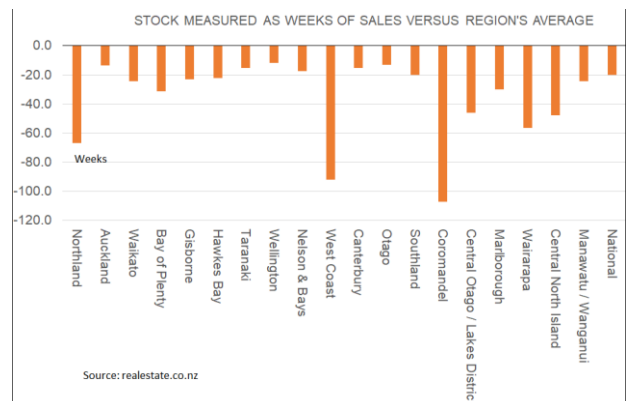
At the end of December, all around New Zealand on their website realestate.co.nz had 13,948 properties listed for sale. This was a 26% fall from a year ago and the lowest stock of listings on record.



If we look at things on a regional basis, we see listings as in short supply everywhere when compared with a year earlier.



But what if a year ago things were already tight? We can get a better feel for how tight things are from a long-term perspective by focussing in on the number of weeks' worth of sales represented by end-month stocks. Then we can compare that calculation with the average for the past 14 years. The result is shown for each region below.



We see that stocks are extremely below average on the West Coast, in Coromandel, and in Northland. But stocks are below average everywhere – which is not what prospective property buyers will want to hear, though those already owning properties will be happy because of the price implications.

For your guide, this next graph shows for each region just how many weeks' worth of sales end-December stocks add up to.

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Property Investment

Retirement Planning

Wealth Creation



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"We take the time to look at who is behind the numbers because in the end, that's what it's all about"



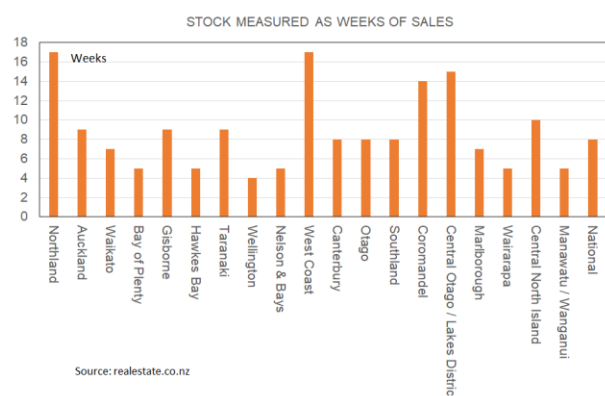
Property Investment



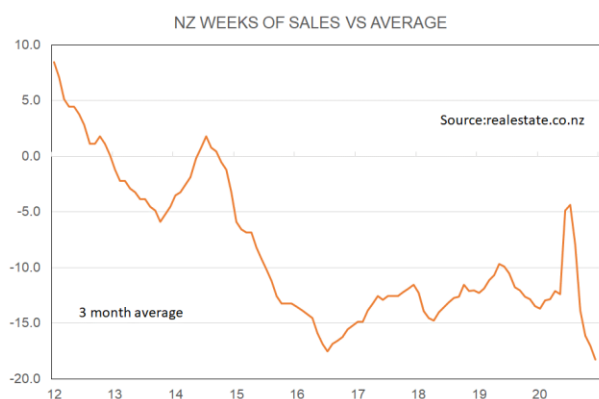
Retirement Planning



Wealth Creation



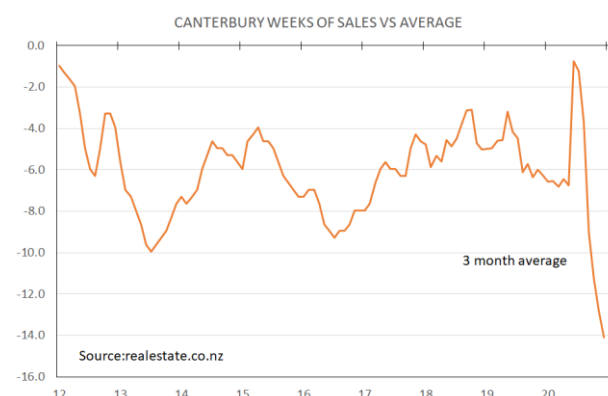
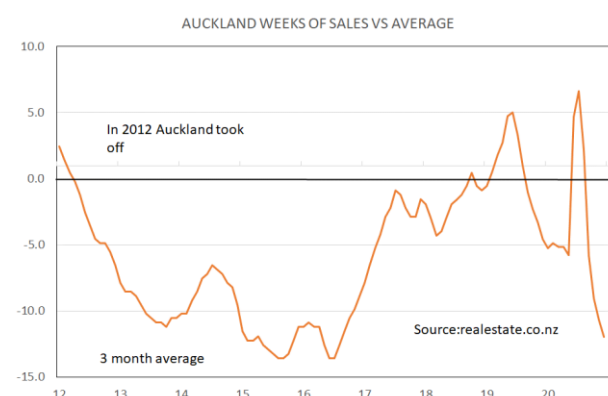
Before finishing, I'd like to focus in on the speed with which the availability of listings has changed. This following graph shows end-month listings measured as weeks' worth of sales and compared with the long-term average. We can see the structural decline in listings availability underway since 2012, plateauing of availability near 12% below average readings from 2017-mid-2020, the soaring associated with lockdown, and now the swift reversal in availability since lockdown ended.



What does the worsening of listings imply? That prices will continue to rise.

Just briefly, here is what the above graph looks like for a few regions. For truly deep regional analysis you can access the monthly Regional Property Insights report I write with sponsorship from First Mortgage Trust. Issues are here.

https://firstmortgagetrust.co.nz/first_mortgage_trust_articles



Interest Rates

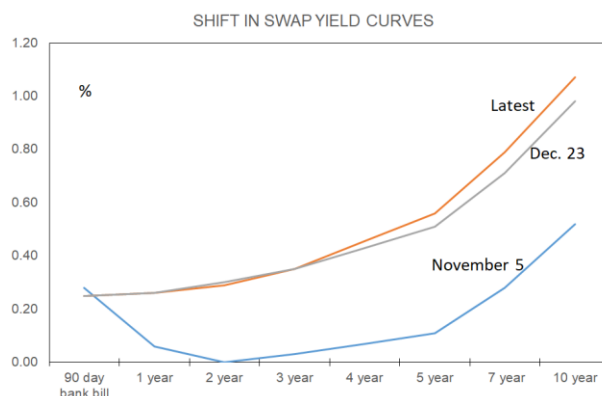
In Tview Premium this week I examine the way in which most people entering a mortgage since 1979 have ended up with an average interest rate lower than what they started with. That is extremely unlikely to be the case here on out and that has implications for the sustainability of rapid house price rises beyond this year into 2022.

But here in Tony's View I thought it would be useful simply to remain people that the winds of change are slowly shifting against interest rates falling further and moving towards medium- to long-term rates edging higher this year. I don't believe the Reserve

Tony's View

Bank will cut the official cash rate again given the pressure being placed on the government to rein in the Reserve Bank's independence which has produced these extremely low interest rates. The low rates are causing political problems for the government because of the growing disparity in wealth between those who own property and those who do not.

For the record, the yield on 90-day bank bills is where it was three weeks ago just below 0.3%. Swap rates however have edged up as shown in the following graph comparing the swaps yield curve now with December 23 and the lows of early-November.



This publication is written by Tony Alexander, independent economist. You can contact me at tony@tonyalexander.nz including for speaking enquiries. Subscribe here <https://forms.gle/qW9avCbaSiKcTnBQA>

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