

Input to your Strategy for Adapting to Challenges

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Upturn underway

My general assessment for where the NZ economy and commentary on it is headed is this. We've been through the wringer many times since the pandemic boom ended and two previous periods of expecting the following year would be okay have proved wrong. Now we are all hoping third time will be a charm, but businesses are still a tad sceptical having been burnt twice already.

This may create an interesting dynamic which was hinted at in the labour market data released a couple of weeks ago. During the September quarter there was no net growth in job numbers in the country. But the number of hours worked in total rose by 0.9%.

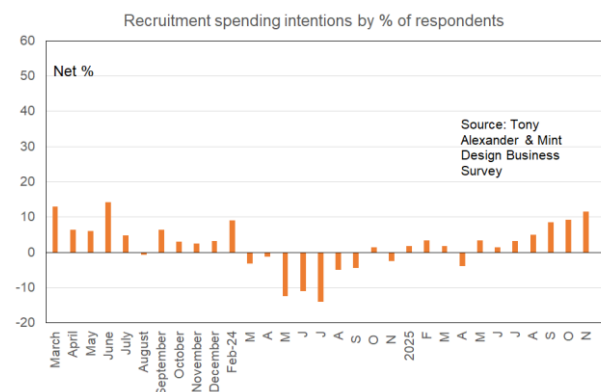
The best interpretation of this is that business activity levels picked up from the depressed June quarter when the economy shrank by 0.9%. But businesses are not yet willing to buy solidly into the upturn by hiring extra people to any great degree.

We can only make informed-sounding guesses as to when the point of hiring capitulation will be reached. That is, the point when businesses accept the upturn this time around is real and start

hiring more new people while pulling back on extra cuts in staff numbers.

I reckon it will come before the middle of next year because of my view that the signs of an acceleration in the pace of economic growth will become a lot stronger.

The latest business survey which I run with MintHC has just recorded a firm rise in business plans for spending on recruitment.



Why the confidence on my part in the economic recovery? Partly because of two strong lagged effects.

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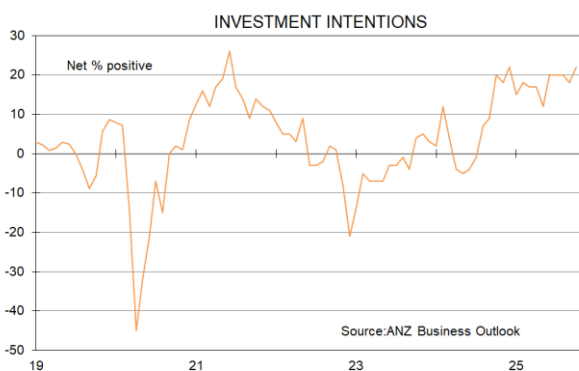
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The first is the normal 18-24 month lag between an easing of monetary policy and the true stimulatory impacts appearing. Policy started being belatedly eased by our central bank in August and that means using the rough 18-24 rule of thumb the boosting effects will really start to show through in the retail sector in particular come about February next year. After that the effects will strengthen through 2026.

The second is the lagged effect of higher incomes in the primary sector – dairying, red meat, Kiwifruit for instance. Not forestry, no idea on seafood or cropping.

Now let's chuck in some other things. The net migration flows are showing signs of turning around – as discussed below. We can also see from the ANZ's monthly Business Outlook survey that an above average net proportion of businesses (22%) are planning to boost their capital spending levels.



This is very important because if such investment were not to be undertaken the recovery would risk grinding to a halt in the face of capacity pressures quickly re-emerging and inflation jumping sharply.

We can also see strongly positive activity expectations in the construction sector and the mood of players in that widely defined industry is likely to improve as we go through summer. This will reflect the edging up of orders alongside the ending (surely) of the weeding out of over-optimistic under-capitalised operators which I started warning builders would come back in 2021. Every cycle has this phase and eventually it ends. The next phase becomes a shortage of capacity in the construction sector and that is probable over the second half of next year.

This will be driven by the general scramble for staff as businesses catch up on delayed hiring, plus the underlying ongoing loss of skilled people to Australia where activity is strong and set to strengthen.

The Australian Federal government has an ambitious target for house construction and demand for such is being actively boosted by their introduction of a scheme to allow first home purchases with just a 5% deposit.

Across the Tasman while the underlying trend in the unemployment rate could conceivably still be upward, it has just fallen from 4.5% to 4.3%, driven by 42,000 extra jobs in October. This has led to a slashing of remaining expectations that the Reserve Bank there will cut their official cash rate from 3.6%.

As the RBA has quite publicly noted recently, they are concerned that an anticipated acceleration in their pace of economic growth through 2026 is starting with the least quantity of spare resources to handle it for a great number of decades. This is why the NZ dollar is so low against the Aussie currency. We are still easing monetary policy

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(over-easing now) while they may not ease any further.

Want to know how useless Google's AI still is? Up until yesterday morning when I'd Google "Australian official cash rate" their AI would say that the rate is " ... 4.35%, following a 0.25% increase at the most recent Reserve Bank of Australia (RBA) decision." Totally wrong.

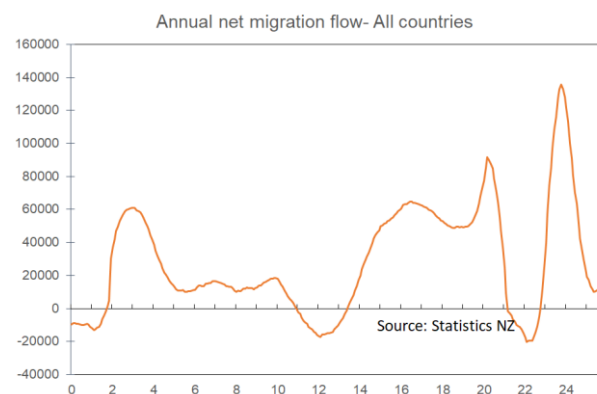
Speaking of AI and just in case you are not aware of one of the latest phenomena in your world. People are recording the entirety of meetings they have with people online or in person, along with presentations they sit in on such as mine, and then getting an app to summarise what was said for them. I don't know if the AI-generated summaries are accurate or not. In the NZ public service awareness of this practice by some people in online meetings is growing and participants are being told such recording is not permitted. So watch out for this spreading breach of etiquette.

Net migration flows turning?

This week Statistics NZ released their monthly data on migration flows in and out of the country. In recent months we analysts have been indicating that we might be seeing signs of the decline in annual flows from the 135,000 peak in October 2023 coming to an end. The latest data support this view.

In the year to September the net flow amounted to a gain of 12,400 compared with 11,100 in August and a low of 10,300 reached in May. These numbers can be volatile and subject to hefty revisions at times. But the drift in them does appear to be towards the better now and so the

guessing game begins on how quickly they will now rise.



I know from experience that it is impossible to accurately forecast New Zealand's net migration flows. Substantially this is because we have one of the most churning populations on the planet.

On average each year roughly 2% of our population emigrates and we receive a 2.7% boost from immigrants. It does not take much of a change in the numbers going out at the same time as a change in the opposite direction for the numbers coming in to produce a large nominal change in the net flow.



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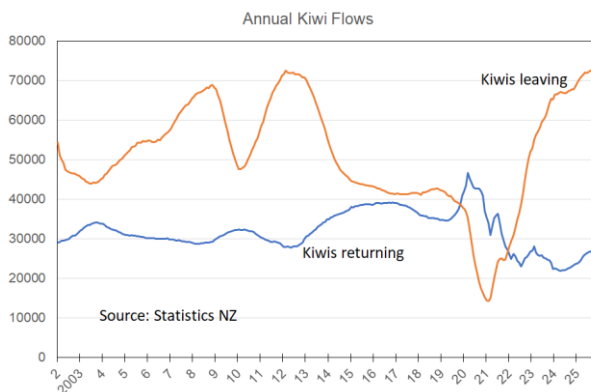
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But everyone likes a view so let's run with this one. The average net gain over the past ten years has been 50,000 a year. So, let's assume that is what we get back to by the end of 2027. In other words, there will be some mild assistance to the

recovery in the economy and a few more tenants to soak up the excess stock of rental accommodation which is causing many rents to decline.

Could the net flow come late-2027 actually be zero? Yes, but unlikely. Could it be 100,000? Yes, but also unlikely. Good luck if your activities are heavily influenced by the size of the net migration gain.

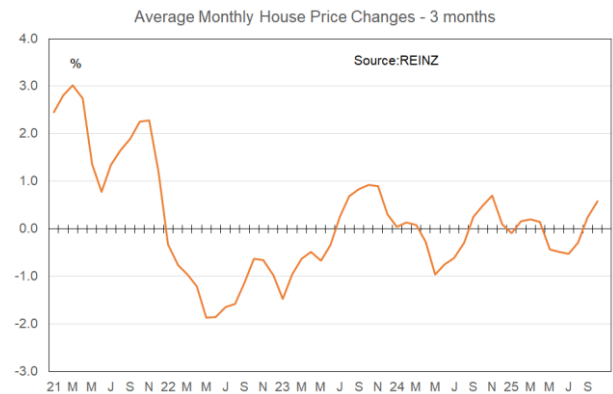
Finally, just for your guide, the net flow of Kiwis has been a loss of 46,000 over the past year. The total has been stuck very close to this since the start of this year and no trend change is yet obvious.



House prices creeping higher

REINZ this week released their monthly data on residential real estate activity around the country in October and these are the main things we learnt.

On average house prices rose 0.6% in the month after gaining 0.8% in September and 0.4% in August. That averages out at 0.6% a month or an annualised gain of 7% over the past three months. That is a turnaround from near exactly the opposite 7% annualised pace of decline over the three months to July.

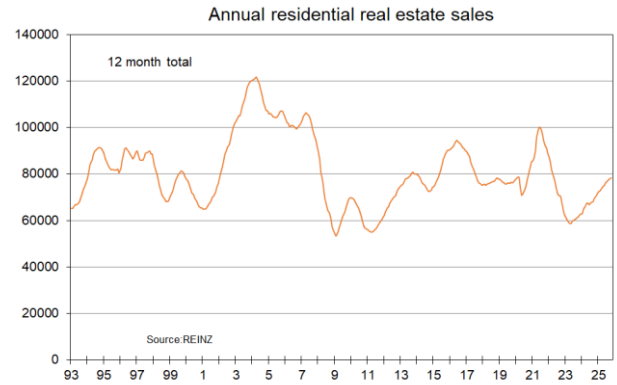
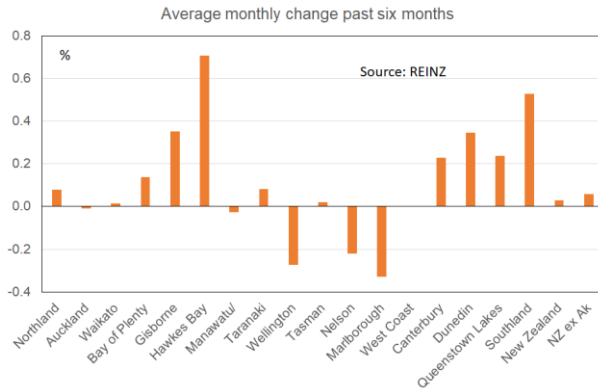


What does this tell us? Mainly that prices have bounced off the bottom. But it would seem a bit too bold to say that the underlying pace of price increase is now running along at 7% per annum. A lot of the recent strength could simply represent a pullback from the depths of the winter months and the period over the June quarter when our economy shrank by 0.9%.

The advertisement for 'Christmas Hampers The Zealand' features a festive design with a red ribbon, a white Christmas ball, and a gift box. The text includes 'GIFT BOXES - GIFT BASKETS - GIFT HAMPERS' and a large 'REWARD' section with three bullet points: '★ YOUR STAFF', '★ YOUR CUSTOMERS', and '★ YOURSELF'. The website 'www.christmashampers.co.nz' is listed at the bottom.

This graph shows average monthly price changes for each region over the past six months – but with the tiny West Coast removed because the 7.1% outcome messes the graph up.

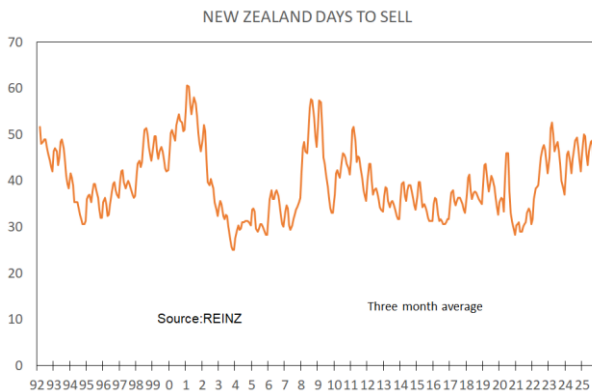
In Wellington prices are falling, Canterbury is rising, Auckland is flat. Note the strength across the middle of the North Island and mid to lower half of the South Island.



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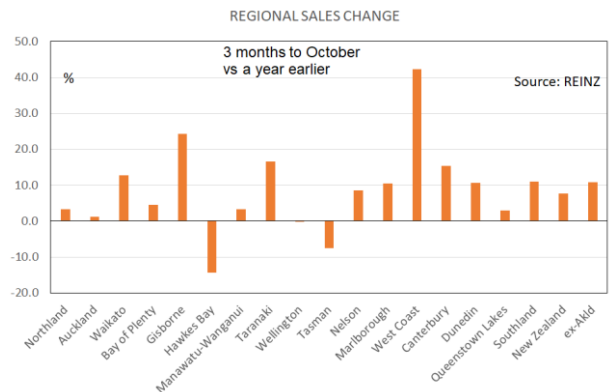
On average in October it took 41 days for a dwelling to sell. This was about the same as 42 days a year ago and tells us that buyers still feel fairly relaxed and feeling no great need to hasten their purchase.



However, when we look at sales data, we see that turnover in October was a firm 7% ahead of a year ago and in rough seasonally adjusted terms for the three months to October was ahead 4%.

There is an upward trend in dwelling sales, but the pace is moderate as yet.

This graph shows sales over the past three months compared with a year earlier. The NZ gain is 7.6%, Auckland 1.2%, Wellington -0.2%, Canterbury +15.4%. Those numbers seem to sum the situation up pretty well for our three main centres. Canterbury's prospects remain very good, Auckland will play catch-up soon with restraint from untold townhouses on the market, and Wellington (mainly Wgtn City) will lag because it's dysfunctional in so many ways.



Overall, residential real estate activity is improving at a mild pace.

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If I were a borrower, what would I do?

I've nothing much of interest to write about interest rates this week. Next week however the Reserve Bank will once again review the official cash rate and almost certainly cut it 0.25% to 2.25%. That will probably be the low-point for this cycle.

The established tendency of our central bank is to tighten too late then tighten too much, and after that ease too late then ease too much. They probably place excessive reliance on old economic models of the economy which no longer work and being public servants will psychologically oscillate around being sticks in the mud and fearful of change and then wanting to exercise "an abundance of caution."

What does that mean? The chances are good that they are again injecting extra stimulus into our economy when it does not need it given the factors already set to strengthen in impact through 2026 and 2027. That will set the scene for some eventually greater than expected tightening of monetary policy come perhaps late-2027 but more certainly 2028.

That is why if I were borrowing at the moment, I would be inclined to lock in fixed for five years

below 5% in order to get protection against upside risks to interest rates which will emerge from late-2027.

But most people don't like thinking out that far and will fix one year, justifying this by saying times are so tough they need to minimise debt servicing cash outflows. Fair enough, but it does reinforce how silly it is to moan about banks not offering 30 year fixed rate loans in New Zealand. There is extremely little demand for any fixed term longer than three years.



To see the interest rates currently charged by major lenders go to www.mortgages.co.nz

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