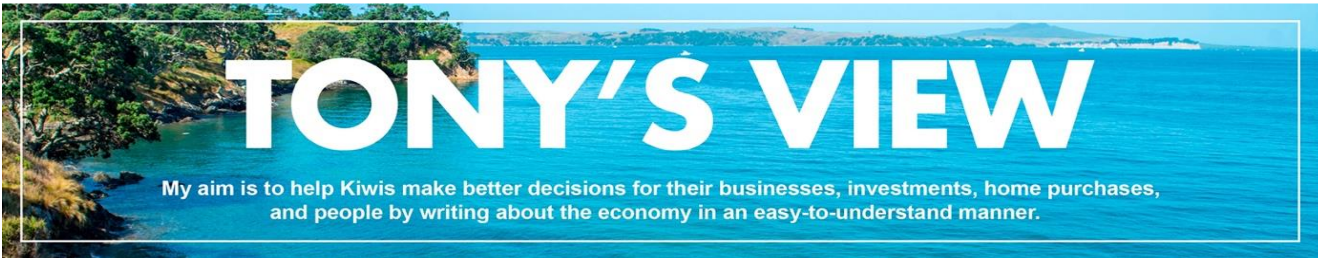

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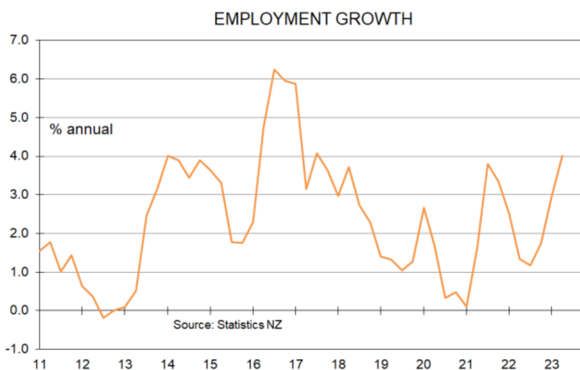
A general economic commentary

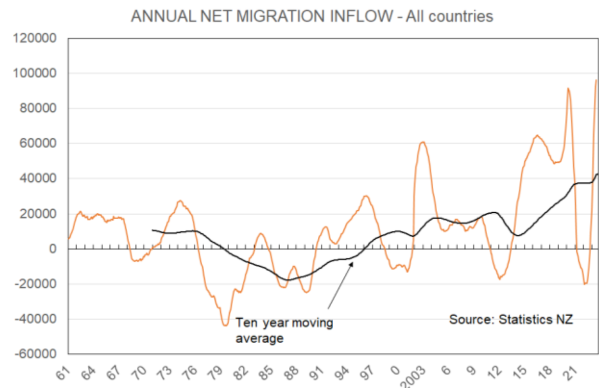
This week I'm going to run through some of the pieces of data released in New Zealand over the past few weeks to see what the numbers may be telling us about the current period of economic challenge we are living through.

I have been using the term economic challenge rather than recession because much as the media tell us everything is bad in New Zealand, it is hard to talk in terms of a recession when job numbers have risen by 4% over the past year. Employment grew 1% in the June quarter after rising 1.1% in the March quarter and 0.7% at the end of last year as the economy shrank 0.5%.

That is what the Household Labour Force Survey told us early in August. The unemployment rate has risen from a low of 3.2% last year to now sit at 3.6%.

The recovery in foreign visitor numbers and re-engagement of people with the hospitality sector has occurred in an environment of structural shortages of labour throughout the country. Businesses have taken advantage of the change in work visa rules to bring in as many people as they can resulting in a record net migration gain in the year to July of 96,000 people. The total looks set to easily exceed 100,000 fairly soon.





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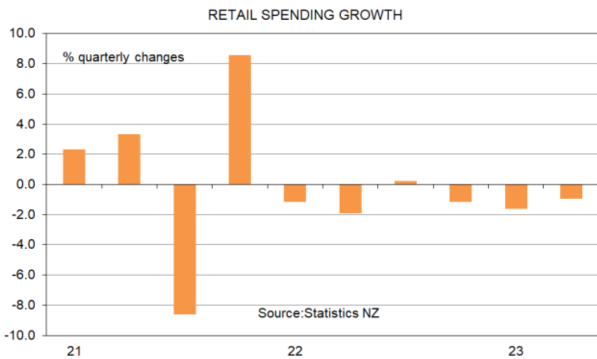
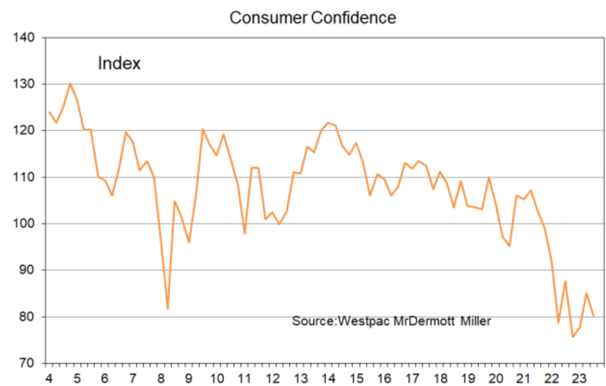
In Australia the anticipated gain of 400,000 this year is already at 450,000 and set to exceed 500,000 so we are not unique in experiencing a post-pandemic population boom.

But despite this boom in our population as people from China, India, and the Philippines in particular shift here, consumer spending is falling.

Retail spending volumes fell 1% in the June quarter after falling 1.6% in the March quarter, and 1.1% in the December quarter last year.



Household spending has fallen as consumer confidence has plumbed deep depths. Last week we learnt that the Westpac McDermott Miller consumer sentiment index had weakened to a reading of 80.9 where 100 is neutral. Households are being hit by above average debt servicing costs, an 18%+ jump in the cost of living over the past three years, alongside a long list of ongoing reasons for feeling bad about the world – Russia's invasion of Ukraine, climate change and extreme weather events, increasing industrial action, the general election, potholes, infrastructure cost blowouts, and so on.



Low consumer sentiment alongside high interest rates in particular suggests bad times continuing for retailers through to late next year.

The high cost of living increase is broadly represented by the inflation rate which currently sits at three times the average for the three decades after 1991 at 6% from a peak of 7.3% last year.

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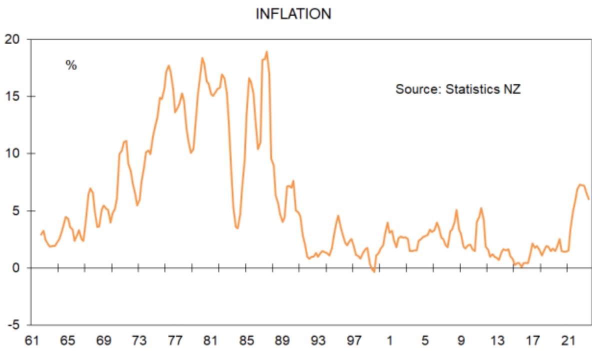
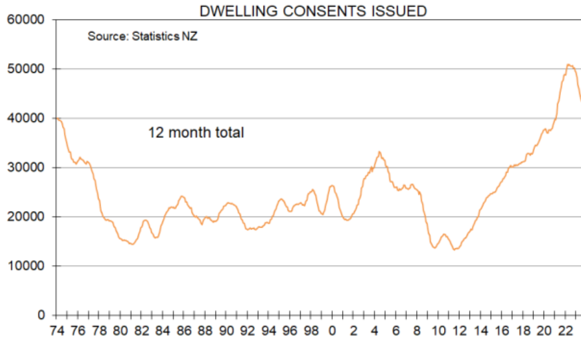


Because there remains extreme uncertainty regarding the speed with which inflation declines in a post-pandemic environment with structural labour shortages and the effects of excessively stimulatory fiscal and monetary policies during the pandemic, relief for borrowers from high interest rates may take a long time coming. Interest rates will remain a drag on the economy over the coming year but won't stop the housing market registering further gains to follow the 2.1% nationwide rise in average prices over the past three months.

The government's accounts are not in good order and whichever party wins the October 14 general election there will be a tightening of fiscal policy. This will act as an additional drag on the economy's rate of growth and reduce willingness of the government to tighten migration settings because of the deleterious impact that would have on the pace of growth. Worries about the impact of the population surge on the housing market probably won't receive much official attention until 2025.

Regarding the upturn in the housing cycle, it will be some time before gains in turnover and prices produce a rise in construction. That is likely a story for 2025. Until then the wariness many people have of new-builds and see consent numbers and construction levels fall away.

Over the three months to July the number of consents issued for new dwellings to be built was 1.6% down from the three months to April which was down 10.6% from the three months to January. The trend has been down since the middle of last year and annual consent numbers have declined to 43,400 from a peak of 51,000 in May last year. This is still very high by historical standards.



Falling house construction will act alongside high interest rates, depressed household sentiment, tightening fiscal policy and cost of living pressures to contain the pace of economic growth in the coming year.

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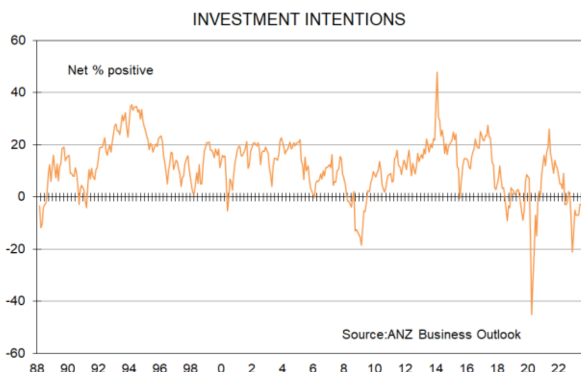
THE Windsor
2 2

Extra weakness is also likely from business capital spending. We do not have good data on capital expenditure in New Zealand but we do have investment intentions measures from business surveys. The ANZ Business Outlook Survey last month showed that a net 1% of businesses planned cutting their investment spending. This was below the ten year average of a net 5% planning more investment which is actually very low.



Weak business investment and excess reliance upon hiring people to deliver higher output explains much of the poor average level of productivity in New Zealand and the poor productivity growth.

Until the economic outlook is a lot better businesses are likely to continue to refrain from investing to boost labour productivity even though most will now accept that there has been a structural tightening up of our labour market. It has actually been this way since about 2005 with relief only temporarily coming from the GFC and pandemic periods.

But some things apart from foreigner numbers in the country are growing. Tourist numbers in July were over 80% of the July 2019 number and with China now allowing group travel off the mainland again we can expect further growth in our international tourism sector.

Student numbers are rising, and there is a lot of infrastructure spending to be done in coming years and decades – which will lead to growth-sapping increases in our council rates and taxes.

Overall, the outlook for our economy is not so good – especially when we allow for the lagged effects to come through 2024 into 2025 of reduced export commodity prices and El Nino causing farmers to slash their spending where possible.

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Maybe 2025 will be a lot better with interest rates declining, house building recovering, housing paper wealth higher, and recoveries to occur in business investment and farm spending.

In case you missed it

My monthly survey of residential property investors undertaken with Crockers Property Management showed the following main things.

- Landlords increasingly report that it is getting easier to secure good tenants.
- Fewer investors are contemplating selling because of loss of interest expense deductibility.
- For those looking to buy, preference for a new property is declining.

https://www.crockers.co.nz/investor-insight-with-tony-alexander/?page=1

If I were a borrower, what would I do?

There is not much good news for borrowers doing the rounds at the moment. Wholesale interest rates in NZ continue to creep higher in response to rises in US rates. These rises offshore are being driven by surprising strength in the US labour market curbing expectations of slowing wages growth in the near future, concerns about a Federal government shutdown, and rising petrol prices directly boosting inflation.

The inflation number released in Australia this week was also slightly higher than expected and expectations have returned for another tightening of monetary policy across the Tasman.

We remain in a unique environment none of us have seen before and that means uncertainty regarding where interest rates peak and when is going to remain high well into next year.

The chances are good that at some stage the inflation outlook will look surprisingly better and interest rates undergo a decent and quick pullback from high levels. But there is no way of knowing when this will occur.

Here in New Zealand the various developments in play have contributed to the one year wholesale interest rates banks must pay in order to lend at a fixed rate to you and I for one year rising to near 5.89% from 5.83% last week, 5.72% a month ago, and near 5.77% three months back.

For now the track for borrowing costs still looks to be slightly upward and that brings a risk of some further nudging up of bank fixed mortgage rates.

I'd fix 12-18 months.

Nothing I write here or anywhere else in this publication is intended to be personal advice. You should discuss your financing options with a professional.

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