

WESTPAC WEEKLY ECONOMIC COMMENTARY

Consumer confidence plummets to lowest level on record.

27 June 2022



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Consumer confidence has plummeted, as household budgets have been squeezed by higher mortgage rates and increases in living costs. That weakness in confidence is weighing on household spending appetites, reinforcing our expectations for a slowdown in economic growth. This also reinforces our expectation that the Official Cash Rate won't rise as far as market pricing implies.

There's been a palpable downturn in economic confidence. In previous weeks, we highlighted the fall in business sentiment as firms across the nation have grappled with rising cost pressures and ongoing disruptions to supply chains. That concern has now spread to the household sector. In fact, our latest Westpac McDermott Miller survey revealed that confidence among New Zealand households has plummeted, dropping to its lowest levels since we began the survey back in 1988.

Underlying this grim assessment of economic conditions, household budgets are being squeezed in a way that they haven't been for decades. Much of that is a result of the mounting pressure on living costs, with prices for all manner of consumer goods charging higher in recent months. There have been particularly large increases in the prices of household essentials, with food prices up nearly 7% over the past year and petrol prices now running at over \$3/ltr across the country.

The pressure on household budgets has been compounded by the rise in interest rates. The Reserve Bank has been hiking the Official Cash Rate at a rapid pace, and they have signalled that it is likely to rise substantially more over the coming months.

For many households, the related rise in mortgage rates has already taken a sizeable bite out of their disposable incomes. In addition, around half of mortgages will come up for repricing over the coming year, and another 20% will come due within two years. In some cases, borrowers will face re-fixing at interest rates that are 2% to 3% higher than the rates they are currently on.

Adding to the concerns about the economic landscape, many households have seen the value of their assets falling in recent months. Nationwide house prices have dropped by 6% since November. Similarly, the value of KiwiSaver balances and other financial assets have dropped sharply since the start of the year.

The pressure on household finances and sharp fall in confidence reinforces our expectations for a downturn in household spending – and economic growth more generally – over the coming months. However, there are big questions about just how stark that downturn will be.

While the economy is being buffeted by some powerful headwinds, we continue to expect that the coming months will

see a slowdown in growth, rather than a crash. A key reason for that is the strength of the labour market. Unemployment is just 3.2%, demand for workers is running hot, and wage rates are pushing higher. The related lift in labour incomes is a partial buffer from the other factors that are crimping households' discretionary spending.

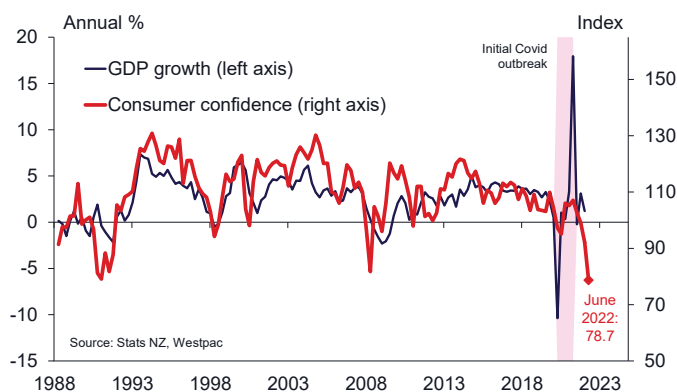
Similarly, while borrowing costs are on the rise, that is an increase from record lows back to 'average' levels. Looking at that change in a different way: for someone who took out a mortgage five years ago, the last couple of years have been a windfall as they were able to re-fix their mortgage at much lower rates. The increases in borrowing rates now in train are taking those borrowers back to where they previously were.

On balance, while the increase in financial pressures will squeeze households' disposable income and spending, overall demand in the economy is likely to remain resilient. However, that does mask some big differences among households. In particular, many families on lower incomes will be facing a significant crunch on their disposable incomes.

While we expect economic conditions to be resilient, the sharp fall in confidence does highlight the chances of a more abrupt downturn. And that would have an important bearing on just how far the Official Cash Rate needs to rise. The RBNZ's own projections show the cash rate rising to 3.9%, while financial markets have been pricing in the chance that it could go as high as 4.5%.

We agree that there's a substantial amount of work still to be done to bring inflation pressures back into check. However, with signs that rate hikes to date are already starting to dampen demand, we expect that increases in the cash rate will be more measured. We continue to forecast a peak in the cash rate of 3.5% by the end of this year.

Consumer confidence and economic growth



Satish Ranchhod, Senior Economist

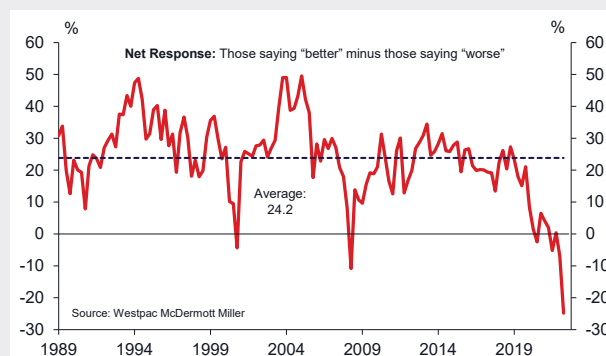
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Chart of the week

With growing pessimism about the economic landscape and mounting concerns about their personal finances, households are keeping an increasingly close eye on their purse strings. In fact, the number of households who think it's a good time to make a major purchase has collapsed, dropping to the lowest level on record. At the same time, households have reported that they have scaled back their spending on leisure activities (like dining out) even as health restrictions have been gradually wound back.

Is this a good or bad time to buy a major household item?

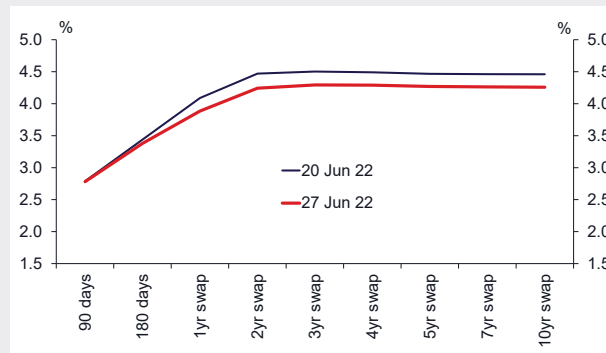


Fixed vs floating for mortgages

Wholesale interest rates remain above our forecast of a 3.5% peak in the Official Cash Rate this year. That suggests to us that there is no cost advantage to fixing for longer terms.

While a one-year mortgage rate is likely to rise further in the year ahead, fixing and rolling for this term is likely to produce a lower borrowing cost on average over the next few years. Longer fixed terms would be more suited to those who want certainty in their repayments.

NZ interest rates



The week ahead

NZ May Employment Indicator

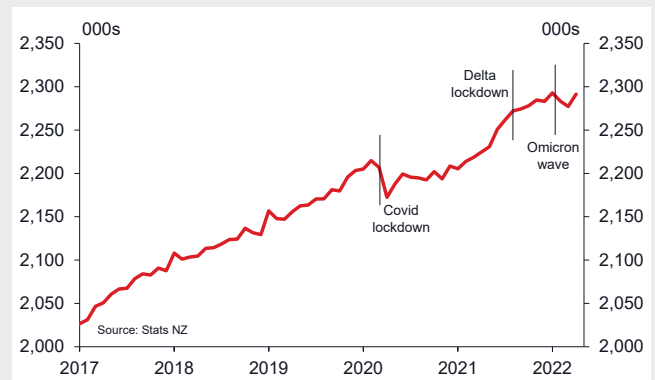
Jun 28, Last: 0.6%, Westpac f/c: 0.2%

The RBNZ has recently said that it will be keeping a close watch on high-frequency labour market data. That will likely include the Monthly Employment Indicator, a series that has received little attention from the market in the past. Being drawn from tax data, it provides quite comprehensive coverage of employment in New Zealand.

The MEI showed a 0.6% rise in the number of filled jobs in April, mostly reversing the decline in February and March that may have been due to Omicron disruptions. More broadly, the MEI has pointed to a slower pace of jobs growth since the Delta outbreak and the end of New Zealand's zero-Covid approach last year.

The weekly snapshots of the data, while probably too volatile to follow for monetary policy purposes, suggest another modest rise in filled jobs in May.

NZ monthly filled jobs



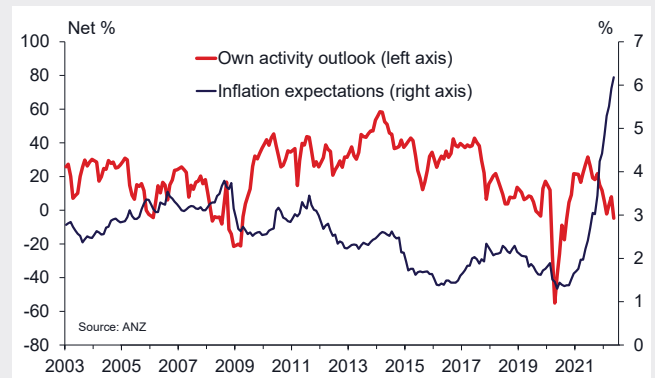
NZ Jun ANZBO business confidence

Jun 30, Last: -55.6

The May business confidence survey pointed to softening confidence as businesses grappled with the combination of staff and supply shortages, strong cost pressures and the rapid rise in interest rates. With no relief on any of those challenges, we expect that confidence will remain subdued in the June survey.

With the RBNZ acutely focused on price setting behaviour, the survey's cost and inflation gauges will be closely watched. Businesses have been highlighting significant pressure on operating costs and most expect inflation will remain elevated. However, we have seen some moderation in the number of firms who are planning on raising their prices (albeit from very high levels). That could be an early indication that businesses are finding it tougher to pass on cost increases.

NZ business confidence



NZ May residential building consents

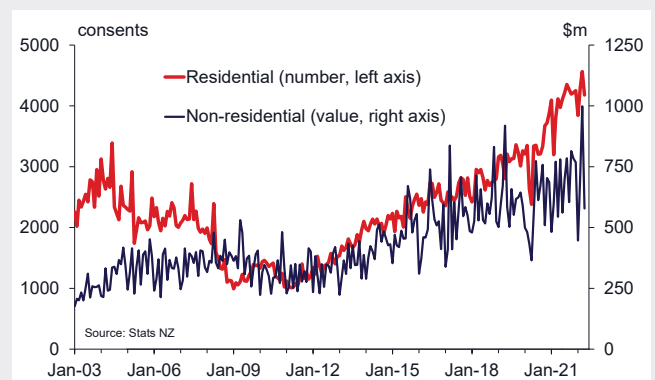
Jul 1, Last: -8.5%, Westpac f/c: Flat

The number of dwelling consents issued fell by 8.5% in April. That drop was mainly due to a pull-back in medium-density consent numbers (i.e. townhouses and apartments) after their earlier sharp rise.

Looking at the longer-term trend in consent issuance, the number of new homes being consented remains elevated, with just under 50,600 new consents issued over the past year. However, after strong increases in recent years, monthly consent issuance has flattened off.

We expect that consent issuance will remain at firm levels in May. However, the combination of rising operating costs, labour and material constraints, and increased nervousness about the economic outlook will all limit the upside for issuance. Those factors are expected to become an increasing drag on consent issuance over the coming months.

NZ building consents



The week ahead

Aus May retail sales

May 29, Last: 0.9%, WBC f/c: 0.3%
Mkt f/c: 0.3%, Range: -1.0% to 0.7%

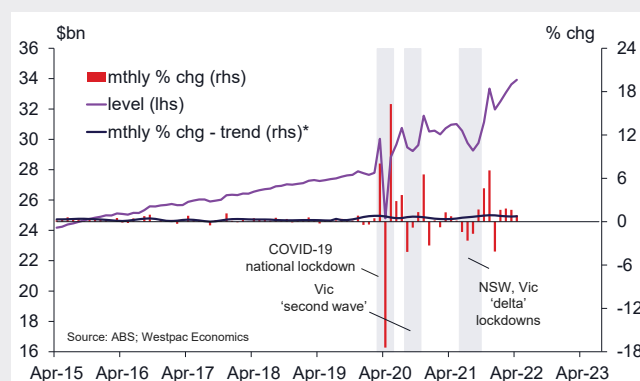
Retail sales increased 0.9% in April following strong gains in averaging 1.7% over the previous three months, annual growth hitting 9.6%/yr. Momentum was relatively well sustained despite various headwinds from the omicron outbreak; weather events and a surge in fuel prices.

May is likely to be a softer result as spending rotates towards non-retail items and given additional headwinds around rising fuel prices and interest rates, and a sharp fall in consumer sentiment.

While reopening dynamics were still very positive for wider consumer spending during the June and September quarters, much of this will bypass retail.

On balance we expect a softer result with a 0.3% gain and some risks to the downside.

Aus monthly retail sales



Aus May private sector credit

Jun 30, Last: 0.8%, WBC f/c: 0.5%
Mkt f/c: 0.6%, Range: 0.5% to 0.7%

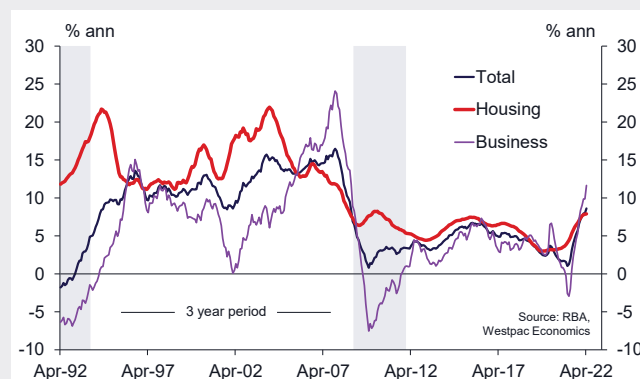
Credit to the private sector expanded by 8.6% over the past year, the fastest annual pace since October 2008, but still well below the December 2007 peak of 16.5%, pre-GFC.

Households and businesses alike have borrowed more, responding to considerable policy stimulus. Record low interest rates fired up the housing market, firms accessed lines of credit to improve cash flows to navigate lockdowns and firms also borrowed to invest.

Currently, credit momentum may be cooling. The RBA began tightening rates in May and the May Federal election was a source of uncertainty, potentially leading to a soft spot in business lending.

Credit grew by 0.6% in each of January, February and March, then lifted to a 0.8% rise in April on an oversized 1.4% increase in business lending. We anticipate a 0.5% gain for May, factoring in a smaller rise for business and with housing growth likely to tick lower after new lending slumped by 6.4% in April.

Aus credit growth



Aus Jun CoreLogic home value index

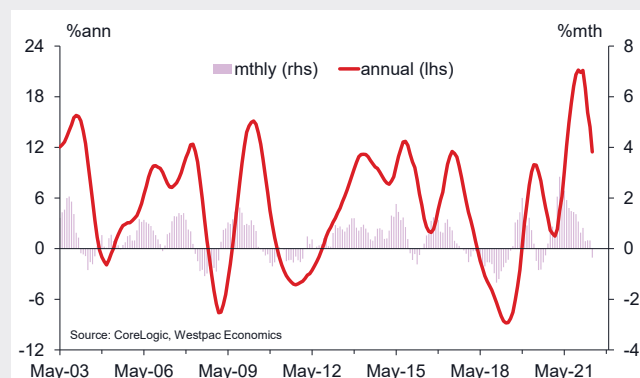
Jul 1, Last: -0.3%, WBC f/c: -0.7%

The wider housing market tipped over into correction in May, the CoreLogic home value index falling 0.3%, tipping into negative for the first time since the first wave of the COVID pandemic. The RBA's 25bp rate hike in May looks to have been a significant catalyst.

Price declines look to have accelerated in June, with the RBA's 50bp rate hike and more hawkish stance clearly impacting auction market activity and prices in Sydney and Melbourne in particular.

For June, the daily measure is pointing to a 0.7% decline across the major capital cities, with considerably larger falls in Sydney (-1.5%/mth) and Melbourne (-1%/mth).

Aus dwelling prices

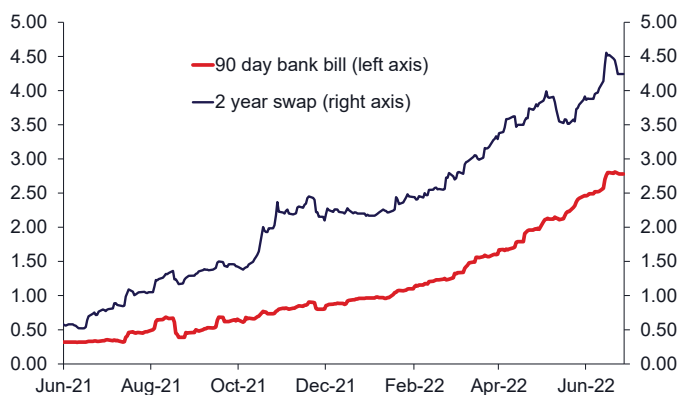


New Zealand forecasts

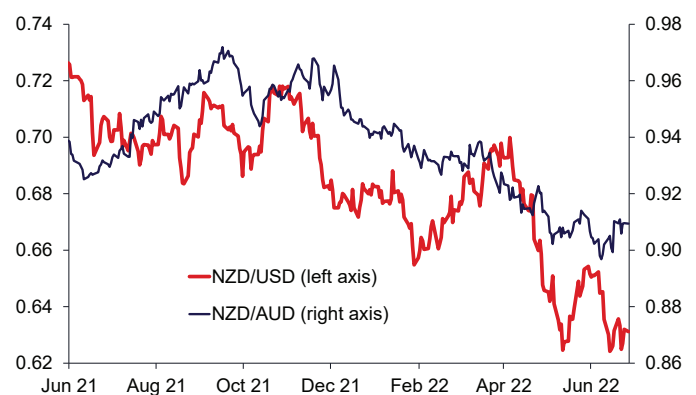
Economic forecasts	Quarterly				Annual			
	2021	2022						
% change	Mar (a)	Jun	Sep	Dec	2020	2021	2022f	2023f
GDP (Production)	-0.2	1.0	0.7	1.2	-2.1	5.6	2.1	3.3
Employment	0.1	0.2	0.2	0.2	0.6	3.5	0.8	0.9
Unemployment Rate % s.a.	3.2	3.1	3.0	3.0	4.9	3.2	3.0	3.3
CPI	1.8	1.1	1.2	0.4	1.4	5.9	4.5	2.7
Current Account Balance % of GDP	-6.5	-7.5	-7.8	-7.5	-0.8	-5.8	-7.5	-6.1

Financial forecasts	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Cash	3.00	3.50	3.50	3.50	3.50	3.50	3.50
90 Day bill	3.40	3.60	3.60	3.60	3.60	3.60	3.60
2 Year Swap	4.50	4.30	4.10	3.80	3.50	3.20	2.90
5 Year Swap	4.60	4.40	4.10	3.80	3.55	3.30	3.05
10 Year Bond	4.30	4.10	3.70	3.40	3.20	3.00	2.90
NZD/USD	0.65	0.68	0.70	0.71	0.72	0.72	0.72
NZD/AUD	0.90	0.91	0.91	0.91	0.91	0.90	0.90
NZD/JPY	85.8	87.7	88.9	88.0	87.2	87.1	86.4
NZD/EUR	0.61	0.62	0.63	0.63	0.63	0.63	0.62
NZD/GBP	0.52	0.54	0.55	0.55	0.54	0.54	0.53
TWI	71.6	73.3	74.4	74.7	74.5	74.7	74.5

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 27 June 2022

Interest rates	Current	Two weeks ago	One month ago
Cash	2.00%	2.00%	2.00%
30 Days	2.28%	2.11%	2.03%
60 Days	2.53%	2.34%	2.24%
90 Days	2.78%	2.57%	2.46%
2 Year Swap	4.24%	4.14%	3.87%
5 Year Swap	4.27%	4.25%	3.81%

NZ foreign currency mid-rates as at 27 June 2022

Exchange rates	Current	Two weeks ago	One month ago
NZD/USD	0.6312	0.6301	0.6543
NZD/EUR	0.5991	0.6019	0.6073
NZD/GBP	0.5138	0.5164	0.5176
NZD/JPY	85.31	84.72	83.35
NZD/AUD	0.9094	0.9042	0.9111
TWI	71.20	70.93	72.56

Data calendar

		Last	Market median	Westpac forecast	Risk/Comment
Mon 27					
Eur	ECB annual forum on Central Banking	–	–	–	Challenges for monetary policy, Sintra, June 27 to 29.
US	May durable goods orders	0.5%	0.1%	–	Supply issues an ongoing headwind.
	May pending home sales	–3.9%	–3.5%	–	Demand is cooling amid higher rates.
	Jun Dallas Fed index	–7.3	–	–	Manufacturers concerned with elevated cost pressures.
Tue 28					
NZ	May monthly employment indicator	0.6%	–	0.2%	RBNZ is taking a close interest in labour market indicators.
US	May wholesale inventories	2.2%	–	–	Inventory levels vary considerably across the economy.
	Apr FHFA house prices	1.5%	–	–	Price momentum expected to show some slowing...
	Apr S&P/CS home price index	2.42%	1.80%	–	... as rate hikes begin to take effect.
	Jun consumer confidence index	106.4	100.0	–	Inflation worries offsetting labour market strength.
	Jun Richmond Fed index	–9	–	–	Labour and material shortages are a key concern.
	Fedspeak	–	–	–	Daly.
Wed 29					
Aus	May retail sales	0.9%	0.3%	0.3%	Loss of momentum, in part a rotation away from retail.
Eur	Jun economic confidence	105.0	–	–	Russia-Ukraine still clouding the outlook...
	Jun consumer confidence	–23.6	–	–	... elevated prices are the chief concern of households.
US	Q1 GDP, final	–1.5%	–1.4%	–	A small upward revision expected in final Q1 estimate.
	Fedspeak	–	–	–	Chair Powell at ECB Forum. Mester and Bullard too.
Thu 30					
NZ	Jun ANZ business confidence	–55.6	–	–	Confidence has waned while cost pressures remain acute.
Aus	May private sector credit	0.8%	0.6%	0.5%	Set to slow, as rates rise & following an oversized rise in April.
	Q2 Job vacancies (ABS series)	6.9%	–	–	Job vacancies a plenty - limited labour supply.
Chn	Jun manufacturing PMI	49.6	–	–	Easing of virus disruptions should see further progress...
	Jun non-manufacturing PMI	47.8	–	–	... in the manufacturing and services rebound.
Eur	May unemployment rate	6.8%	6.7%	–	Tight labour market laying foundation for wages growth.
UK	Q1 GDP, final	0.8%	0.8%	–	Q1's gain to be followed by an abrupt slowing.
	Jun Nationwide house prices	0.9%	–	–	Demand to soften as rate hikes take effect.
US	May personal income	0.4%	0.5%	–	Purchasing power is an ongoing concern...
	May personal spending	0.9%	0.4%	–	... as households run down savings.
	May PCE deflator	0.2%	0.7%	–	PCE inflation looks to have crested...
	May core PCE deflator	0.3%	0.5%	–	... price pressures to slowly abate through 2022.
	Initial jobless claims	229k	–	–	To remain at a low level.
	Jun Chicago PMI	60.3	58.8	–	Concerns around supply issues remain.
Fri 01					
NZ	Jun ANZ consumer confidence	82.3	–	–	Confidence low, dampened by rises in living costs.
	May building permits	–8.5%	–	0.0%	Set to remain at firm levels.
Aus	Jun CoreLogic home value index	–0.3%	–	–0.7%	Downturn is underway as RBA begins tightening cycle in May.
Chn	Jun Caixin China PMI	48.1	–	–	Easing of restrictions and policy support to aid mfg.
Eur	Jun S&P Global manufacturing PMI	52.0	–	–	Final estimate for the month.
	Jun CPI %yr	8.1%	8.3%	–	Price pressures are intensifying and broadening.
UK	Jun S&P Global manufacturing PMI	53.4	–	–	Final estimate for the month.
	May net mortgage lending £bn	4.1	–	–	Rising rates and slowing economy to weigh on lending.
US	Jun S&P Global manufacturing PMI	52.4	–	–	Final estimate for the month.
	May construction spending	0.2%	0.5%	–	Activity supported by home building strength.
	Jun ISM manufacturing	56.1	55.4	–	Robust momentum still evident in manufacturing.

International forecasts

Economic Forecasts (Calendar Years)	2018	2019	2020	2021f	2022f	2023f
Australia						
Real GDP %yr	2.8	2.0	-2.1	4.8	4.5	2.7
CPI inflation %yr	1.8	1.8	0.9	3.5	6.6	3.0
Unemployment rate %	5.0	5.2	6.8	4.7	3.2	3.5
Current account % of GDP	-2.1	0.7	2.6	3.5	1.4	-1.3
United States						
Real GDP %yr	3.0	2.2	-3.4	5.7	2.5	1.6
CPI inflation %yr	2.4	1.9	1.2	5.1	7.1	2.5
Unemployment rate %	3.9	3.7	8.1	5.4	3.6	4.0
Current account % of GDP	-2.3	-2.6	-2.5	-2.4	-2.4	-2.4
Japan						
Real GDP %yr	0.6	0.3	-4.8	1.8	1.7	1.8
Euro zone						
Real GDP %yr	1.9	1.3	-6.6	4.9	2.2	1.5
United Kingdom						
Real GDP %yr	1.3	1.4	-9.9	7.2	3.7	0.0
China						
Real GDP %yr	6.7	5.8	2.3	8.1	5.3	5.5
East Asia ex China						
Real GDP %yr	4.4	3.7	-2.4	4.2	4.5	4.6
World						
Real GDP %yr	3.6	2.8	-3.3	5.5	3.4	3.3

Forecasts finalised 10 June 2022

Interest rate forecasts	Latest	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Australia								
Cash	0.85	1.85	2.35	2.60	2.60	2.60	2.60	2.60
90 Day BBSW	1.74	2.30	2.72	2.80	2.80	2.80	2.80	2.80
10 Year Bond	3.72	4.10	3.80	3.40	3.00	2.70	2.50	2.35
International								
Fed Funds	1.625	2.875	3.375	3.375	3.375	3.375	3.125	2.875
US 10 Year Bond	3.10	3.50	3.30	3.00	2.70	2.50	2.30	2.20

Exchange rate forecasts	Latest	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
AUD/USD	0.6905	0.72	0.75	0.77	0.78	0.79	0.80	0.80
USD/JPY	134.86	133	131	129	127	125	123	121
EUR/USD	1.0529	1.08	1.10	1.12	1.13	1.14	1.15	1.16
GBP/USD	1.2272	1.25	1.27	1.28	1.30	1.32	1.34	1.35
USD/CNY	6.6961	6.50	6.35	6.25	6.20	6.15	6.15	6.10
AUD/NZD	1.0980	1.11	1.10	1.10	1.10	1.10	1.11	1.11

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