

Fortnightly Economic Update

5 August 2022

- Labour market remains extremely tight
- Outlook for house building activity weakens
- Increasingly gloomy global outlook

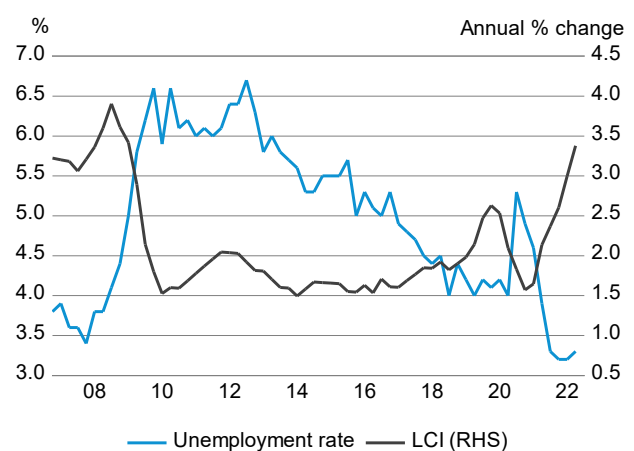
New Zealand's unemployment rate ticked up to 3.3% in the June quarter, but the labour market remains extremely tight. This tightness is being reflected in labour costs, which rose at their fastest pace since 2008. We expect the labour market to remain constrained in the near-term but to begin loosening later this year as higher immigration boosts supply and monetary tightening cools demand. Construction is one sector where demand looks to be easing rapidly, with declining new home consents and weak industry sentiment, although the pipeline of work remains large and should support sector activity for some time. Meanwhile, an "increasingly gloomy and uncertain outlook" has led the IMF to revise down its global growth forecasts, and incoming data continues to point to fading growth momentum.

While the labour market was tight over the June quarter, we expect it to ease...

The June quarter release of the labour market statistics highlights the continued resilience of the labour market to Omicron impacts. Total employment held steady, and the unemployment rate increased slightly to 3.3%, still a near record low (Figure 1). Persistently high levels of labour market tightness have seen the Labour Cost Index (LCI), a measure of pure wage inflation, recorded its fastest growth since the December 2008 quarter and record-high growth in hourly earnings.

We expect the labour market will remain tight over the next few months before the reopening of New Zealand's border leads to higher migrant inflows and enables some labour supply pressures to ease. However, there remains considerable uncertainty around the net migration outlook chiefly owing to the risk of a higher net outflow of New Zealanders exploring overseas opportunities. Demand for labour is also expected to ease as tightening monetary policy dampens economic activity.

Figure 1: Unemployment rate and wage inflation



Source: Stats NZ

... off the back of low activity and confidence...

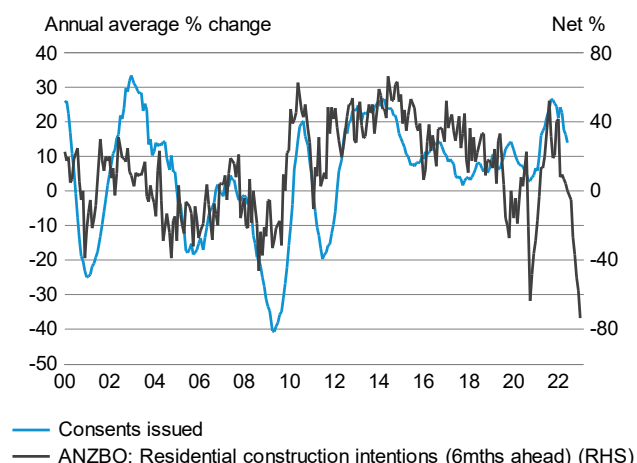
The ANZ business outlook survey for July highlights the strength of the headwinds facing the economy. Inflationary pressures are strong and business activity appears to be fading, especially in the residential sector, where consents are easing (see below) and expected activity is sharply lower. In contrast, positive employment intentions point to sustained low unemployment.

The strong demand for labour has been supporting consumer spending but with business confidence so low, demand is likely to ease. The ANZ-Roy Morgan consumer confidence survey shows confidence and planned spending remaining near all-time lows. These are both (usually) useful leading indicators of spending but have parted ways recently.

...and declining construction demand

Demand for building new homes eased further in June, down 2.3% compared with May and 14% lower than in June last year. In the 12 months ended June, consents issuance reached a new record high of 50,736, but that is likely to be the peak as monthly consents trend down. ANZ's residential construction intentions measure is a useful indicator of where things are likely to go (Figure 2). However, there remains a substantial pipeline of consents to be completed and supply chain disruptions and labour shortages remain the biggest problems for the industry.

Figure 2: Residential consents and construction intentions



Source: Stats NZ, ANZ

Meanwhile, agricultural activity increased...

Meat and dairy production rose in the June quarter, partially recovering falls in the previous quarter, which will support June quarter GDP. Meat processing was up 8.8% compared to the March quarter, as reduced worker absenteeism from COVID-19 enabled the industry to clear some of the backlog. Milk production also improved in the June quarter, up 5.5% on the previous quarter on a seasonally adjusted basis, although production was down 4.0% in the last 12 months compared to the previous year.

...but prices eased

The ANZ Commodity Price NZD Index fell 0.5% in July driven by a 2.9% fall in dairy prices, while meat prices pulled back 1.5%. A weaker NZD provided some offset to lower world prices, with the world price index declining 2.2%. Global demand has eased recently as the high prices from earlier in the year proved unsustainable in the current economic climate. Dairy prices fell a further 5% at the 2 August *GlobalDairyTrade* auction to be 27% below their March peak, which highlights the worsening price outlook. While demand has weakened, global supply remains tight, which should provide some support to prices in addition to an anticipated recovery in China as COVID-19 impacts ease.

International commodity prices also eased over the past month. Brent crude oil prices have been below US\$100 since the start of the month, mostly reflecting lower expected demand and rising inventories.

Increasing global gloom...

The IMF cut its global growth forecasts to 3.2% for 2022 and to 2.9% for 2023, broadly similar to recent World Bank and OECD forecasts (Table 1). Global inflation was revised higher and is projected to remain elevated for longer. The IMF noted an "increasingly gloomy and uncertain outlook", with stalling growth across the US, euro area and China. Risks to the outlook were "overwhelmingly" tilted to the downside and it cited a plausible scenario where further disruption to energy supplies, higher inflation expectations and tighter monetary policy would send the global economy into recession.

Table 1: IMF real GDP projections

		IMF WEO, July 2022 <i>Update</i> , years ended December, annual average %	
		2022	2023
World	new	3.2	2.9
	change*	-0.4	-0.7
Euro area	new	2.6	1.2
	change*	-0.2	-1.1
US	new	2.3	1.0
	change*	-1.4	-1.3
China	new	3.3	4.6
	change*	-1.1	-0.5

*difference from April 2022 projections

Source: IMF

Meanwhile, incoming data continue to point to weaker momentum. The combined manufacturing and services global Purchasing Managers Index (PMI) for July fell 2.7 points to a two-year low, although there were welcome signs that inflationary pressures are abating. The global manufacturing PMI fell 1.1 points, led by a sharp fall in the euro area and a reversal of China's gains in May and June. The global services PMI fell 2.8 points, led by declines in the US and euro area, and was broadly steady in China. The inflation related components of manufacturing suppliers' delivery times shortened, and input and output price measures for both manufacturing and services eased but remained high.

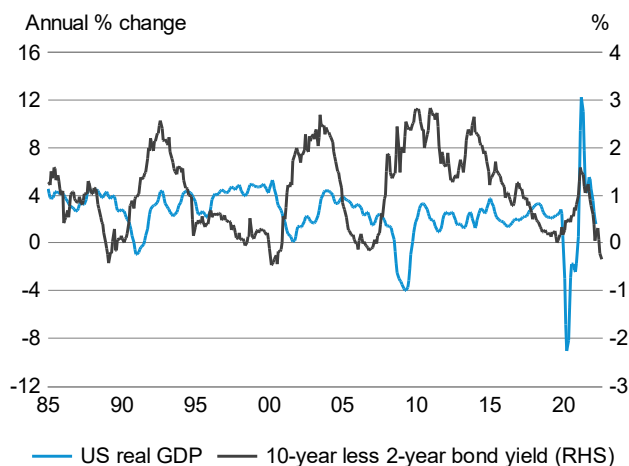
...as recession looms in the euro area and US

Euro area GDP rose 0.7% in the June quarter compared with the previous quarter, well above analyst expectations of 0.2% growth. However, growth is expected to slow sharply from here, with weak activity indicators and easing industrial activity foreshadowing a recession over the second half of the year. Real incomes remain under pressure with euro area CPI inflation rising 8.9% in July.

In the US, June quarter GDP growth came in weaker than the economist consensus, with the economy contracting 0.2% (0.9% annualised) compared to the previous quarter. Within the details, consumer spending growth slowed to 0.3% in the quarter, business investment was broadly flat but residential investment fell 3.7% as the housing market slowed. Government spending fell 0.5%, driven by non-defence spending, and net exports contributed 0.3%-points.

This was the second consecutive contraction in quarterly GDP, but observers do not consider the US to be in recession, citing the strength of the labour market as a countervailing force. The real recession risk lies ahead, as signalled by the deepening inversion of the US yield curve (Figure 3).

Figure 3: US GDP and yield curve



Source: Haver

Earlier, the US Federal Reserve (Fed) raised the federal funds target range by 75 basis points to 2.25% - 2.50%, a range it considers to be neutral for activity. Guidance remained unchanged that ongoing increases in the target range will be appropriate but having met its initial goal of raising rates to neutral, future rate decisions will be data dependent. Before the September meeting, there are another two CPI and employment prints.

The Bank of England increased its policy rate by 50 basis points to 1.75% in a widely anticipated decision. The Bank's new forecasts show inflation rising to 13% later this year and remaining above 10% percent through much of 2023, before falling back to 2% in 2024. Real GDP is forecast to contract by around 2% in 2023.

Uneven recovery in China

In China, leaders at July's Politburo meeting noted the economy is facing some prominent challenges and pledged to keep economic activity growing at a reasonable pace, although there was no explicit target to replace the previous goal of GDP growth around 5.5%. Leaders also reaffirmed commitment to the dynamic zero-COVID policy. Analysts noted there were few signals of additional policy support, despite further deterioration in housing market sentiment. Despite the fall in China's July PMIs, analysts remain confident that growth will pick up over the second half of 2022 as COVID-19 disruption eases and past policy measures are implemented.

Australian inflation rises...

Australian annual headline CPI inflation came in at 6.1%, with the key core measure based on the trimmed mean at 1.5% in the quarter and 4.9% on an annual basis.

Following this outturn, the Reserve Bank of Australia (RBA) raised its cash rate by 50 basis points to 1.85% and said it expects to take the cash rate higher in coming months, although the size and timing of future rate increases will be data dependent. The RBA Governor recently observed that the neutral policy rate was around 2.5%, suggesting rates have some distance to go before policy becomes materially contractionary.

...and growth forecasts trimmed

Earlier, Australian Treasurer Jim Chalmers gave a Ministerial Statement on the Economy in advance of a full update in the October Budget. The Treasurer's real GDP forecasts for the June years ending 2022, 2023 and 2024 were all revised down by around 0.5%-pts, with smaller downgrades in the later years (Table 2). The projected inflation peak was revised up to 7¼% in the December 2022 quarter and now remains above the RBA's 2-3% target until 2024. Those forecasts are underpinned by wage growth being at 3.8% and some easing in labour market tightness with the unemployment rate expected to rise from its current 3.5% to 3.8% by June 2023 and to 4% by June 2024.

There were few fiscal details, although Chalmers noted Government spending will be \$30 billion higher over the forward estimates than in the pre-election update. But analysts noted the 2021/22 fiscal deficit is already at least \$30 billion lower.

Table 2: Australian economic projections

	% change, year ended June				
	2022	2023	2024	2025	2026
Real GDP*	3.8	3.0	2.0	2.3	2.3
Unemployment rate**	3.8	3.8	4.0	4.3	4.3
Consumer Price Index***	6.1	5.5	2.8	2.5	2.5

*annual average % change, **June quarter, ***annual % change

Source: Australian Treasury

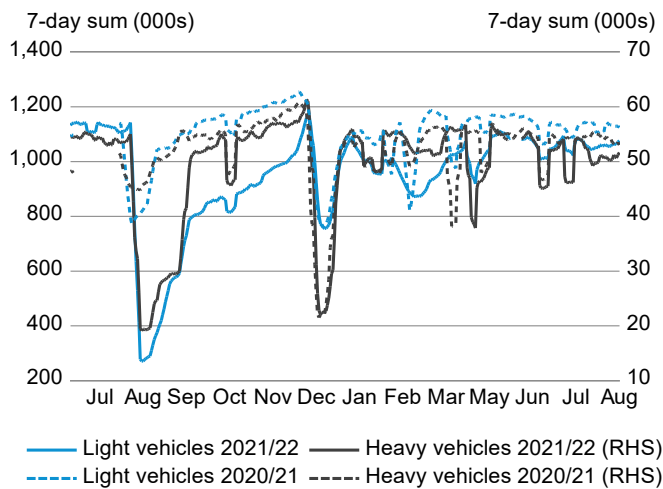
In other data, Australian dwelling prices fell 1.3% in July according to CoreLogic data as the pace of declines quickened in the largest cities. Sydney dwelling prices have now fallen 5.2% since peaking in January 2022 and Melbourne prices are down 3.4% since peaking in February 2022. Analysts expect prices to fall further, with a peak to trough fall in capital city dwelling prices of around 15% by the end of 2023. New residential building approvals also continued to fall, down 0.7% in June and 17% lower compared to June last year.

Coming Up:

Date	Release
9 Aug	Electronic Card Transaction (Jul)
11 Aug	International travel and migration (Jun)
12 Aug	Food and rental price indexes (Jul)
15 Aug	REINZ house price index (Jul)
17 Aug	RBNZ Monetary Policy Statement

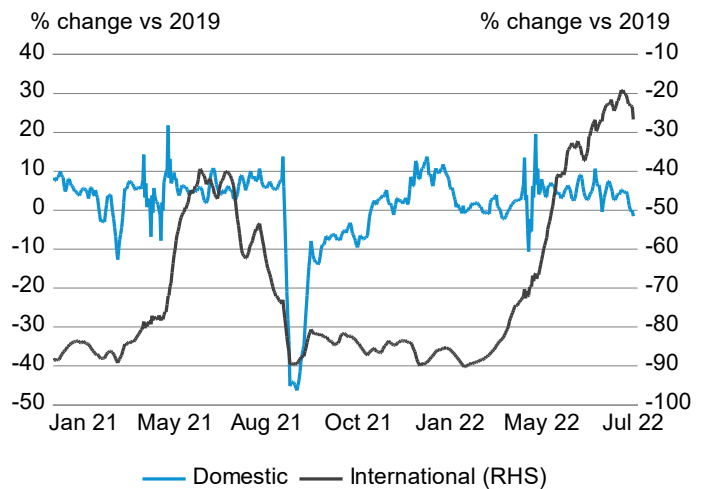
High-Frequency Indicators

Traffic and Freight Movement



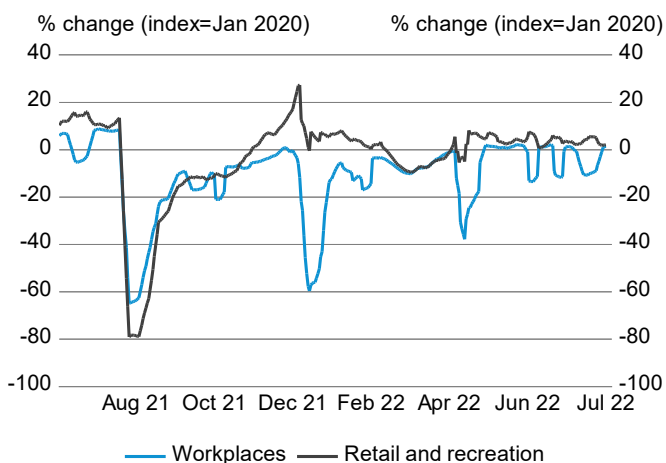
Source: Waka Kotahi NZ Transport Agency

Card Spending



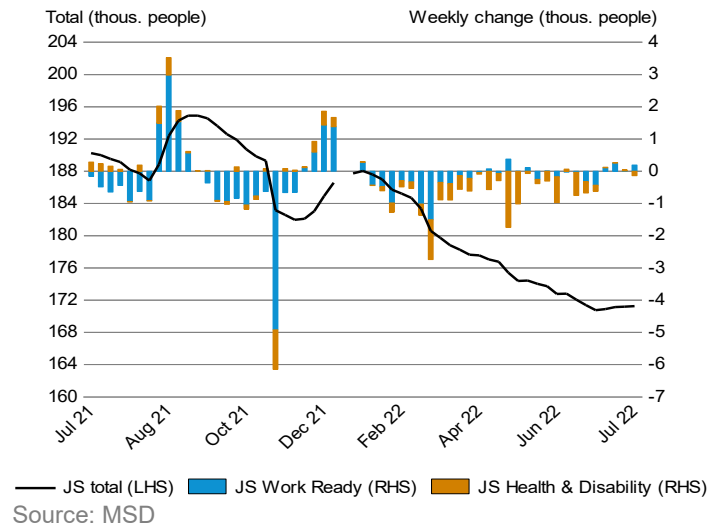
Source: Marketview data via MBIE

People Movements at Selected Locations



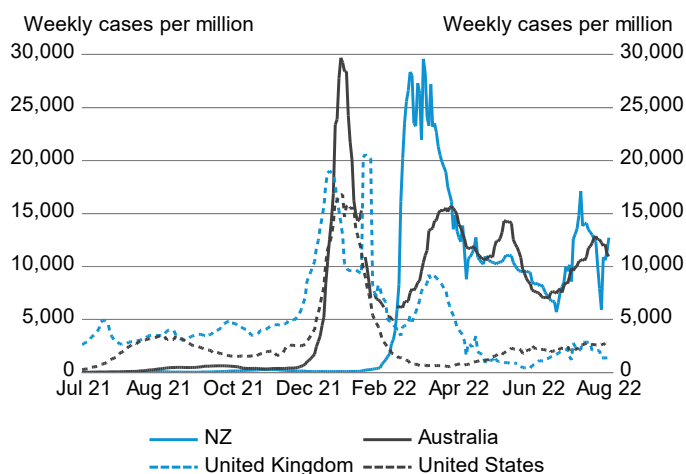
Source: Google/Haver

Jobseeker (JS) and Income Support Receipts



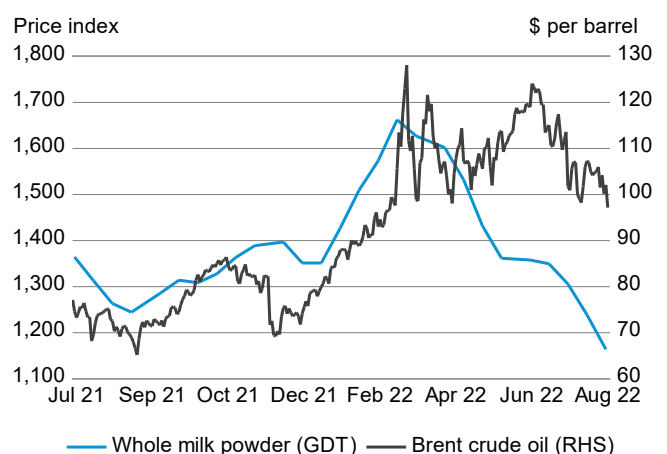
Source: MSD

COVID-19 Cases Per Million People



Source: John Hopkins University/Haver

World Commodity Prices



Source: Haver

Tables

Quarterly Indicators		2021Q1	2021Q2	2021Q3	2021Q4	2022Q1	2022Q2
Real Production GDP (1)	qpc	1.7	2.4	-3.8	3.0	-0.2	...
	aapc	-1.4	5.2	4.9	5.6	5.1	...
Current account balance (annual)	%GDP	-2.5	-3.3	-4.6	-5.8	-6.5	...
Merchandise terms of trade	apc	-0.9	-0.1	5.2	2.8	3.3	...
CPI inflation	qpc	0.8	1.3	2.2	1.4	1.8	1.7
	apc	1.5	3.3	4.9	5.9	6.9	7.3
Employment (HLFS) (1)	qpc	0.6	1.1	1.7	-0.1	-0.0	0.0
Unemployment rate (1)	%	4.6	3.9	3.3	3.2	3.2	3.3
Participation rate (1)	%	70.4	70.5	71.2	71.0	70.9	70.8
LCI salary & wage rates - total (2)	apc	1.6	2.1	2.4	2.6	3.0	3.4
QES average hourly earnings - total (2)	apc	4.0	4.0	3.5	3.8	4.8	6.4
Core retail sales volume	apc	5.3	30.0	-3.2	5.1	3.2	...
Total retail sales volume	apc	6.6	33.1	-5.1	4.4	2.3	...
WMM - consumer confidence (3)	Index	105.2	107.1	102.7	99.1	92.1	78.7
QSBO - general business situation (1,4)	net%	-7.1	9.3	-11.4	-36.6	-34.0	-61.6
QSBO - own activity outlook (1,4)	net%	4.6	30.4	8.8	6.7	5.3	-10.5

Monthly Indicators		Feb 22	Mar 22	Apr 22	May 22	Jun 22	Jul 22
Merchandise trade balance (12 month)	NZ\$m	-8,685.1	-9319.7	-9260.9	-9562.8	-10509.1	...
Dwelling consents - residential	apc	34.1	25.6	-6.9	7.8	-6.5	...
House sales - dwellings	apc	-30.9	-31.9	-32.9	-26.4	-38.1	...
REINZ - house price index	apc	14.2	9.0	6.2	3.7	0.8	...
Estimated net migration (12 month total)	people	-13,616.0	-11823.0	-10890.0	-10673.0	...	...
ANZ NZ commodity price index	apc	29.2	20.9	17.5	16.5	14.5	14.2
ANZ world commodity price index	apc	20.4	18.0	13.2	6.2	4.8	4.3
ANZBO - business confidence	net%	-51.8	-41.9	-42.0	-55.6	-62.6	-56.7
ANZBO - activity outlook	net%	-2.2	3.3	8.0	-4.7	-9.1	-8.7
ANZ-Roy Morgan - consumer confidence	net%	81.7	77.9	84.4	82.3	80.5	81.9

Daily Indicators		Fri 29/7/22	Mon 1/8/22	Tue 2/8/22	Wed 3/8/22	Thu 4/8/22	Fri 5/8/22
NZ exchange and interest rates (5)							
NZD/USD	\$	0.6295	0.6293	0.6328	0.6235	0.6283	...
NZD/AUD	\$	0.8993	0.9008	0.9022	0.9016	0.9035	...
Trade weighted index (TWI)	index	71.38	71.27	71.60	70.83	71.34	...
Official cash rate (OCR)	%	2.50	2.50	2.50	2.50	2.50	...
90 day bank bill rate	%	3.14	3.17	3.19	3.19	3.21	...
10 year govt bond rate	%	3.40	3.41	3.37	3.37	3.36	...
Share markets (6)							
Dow Jones	index	32,845	32,798	32,396	32,813	32,727	...
S&P 500	index	4,130	4,119	4,091	4,155	4,152	...
VIX volatility index	index	21.3	22.8	23.9	22.0	21.4	...
AU all ords	index	7,174	7,213	7,216	7,203	7,207	...
NZX 50	index	11,493	11,526	11,532	11,705	11,735	...
US interest rates							
3 month OIS	%	2.32	2.33	2.33	2.33	...	...
3 month Libor	%	2.79	2.80	2.81	2.83	...	...
10 year govt bond rate	%	2.67	2.60	2.75	2.73	2.68	...
Commodity prices (6)							
WTI oil	US\$/barrel	101.31	96.59	97.14	90.66	88.54	...
Gold	US\$/ounce	1,753.40	1,772.40	1,779.75	1,761.25	...	...
CRB Futures	index	582.45	580.95	581.81	581.55	583.11	...

(1) Seasonally adjusted
(2) Ordinary time, all sectors
(3) Westpac McDermott Miller

(4) Quarterly Survey of Business Opinion
(5) Reserve Bank (11am)
(6) Daily close

Data in italic font are provisional
... Not available

Country	Indicator		2021Q4	Jan 22	Feb 22	Mar 22	2022Q1	Apr 22	May 22	Jun 22	2022Q2	Jul 22
United States	GDP (1)	qpc	1.7				-0.4				-0.2	
	Industrial production (1)	mpc		0.4	0.8	0.7		0.8	0.0	-0.2		...
	CPI	apc		7.5	7.9	8.5		8.3	8.6	9.1		...
	Unemployment rate (1)	%		4.0	3.8	3.6		3.6	3.6	3.6		...
	Employment change (1)	000s		504.0	714.0	398.0		368.0	384.0	372.0		...
	Retail sales value	apc		13.7	17.7	7.1		7.8	8.2	8.4		...
	House prices (2)	apc		19.0	20.3	21.2		21.2	20.5	...		...
	PMI manufacturing (1)	index		57.6	58.6	57.1		55.4	56.1	53.0		52.8
	Consumer confidence (1)(3)	index		111.1	105.7	107.6		108.6	103.2	98.4		95.7
Japan	GDP (1)	qpc	1.0				-0.1				...	
	Industrial production (1)	mpc		-2.4	2.0	0.3		-1.5	-7.5	8.9		...
	CPI	apc		0.5	0.9	1.2		2.5	2.5	2.3		...
	Unemployment rate (1)	%		2.8	2.7	2.6		2.5	2.6	2.6		...
	Retail sales value	apc		1.1	-0.9	0.7		3.1	3.7	1.5		...
	PMI manufacturing (1)	index		55.4	52.7	54.1		53.5	53.3	52.7		52.1
	Consumer confidence (1)(4)	index		36.6	35.1	32.5		32.0	33.1	32.3		30.1
Euro area	GDP (1)	qpc	0.4				0.5				0.7	
	Industrial production (1)	mpc		-0.8	0.6	-1.7		0.5	0.8	...		...
	CPI	apc		5.1	5.9	7.4		7.4	8.1	8.6		...
	Unemployment rate (1)	%		6.9	6.8	6.7		6.6	6.6	6.6		...
	Retail sales volume	apc		8.5	5.1	1.9		4.2	0.4	-3.7		...
	PMI manufacturing (1)	index		58.7	58.2	56.5		55.5	54.6	52.1		49.8
	Consumer confidence (5)	index		-9.6	-9.6	-21.7		-22.1	-21.3	-23.8		-27.0
United Kingdom	GDP (1)	qpc	1.3				0.8				...	
	Industrial production (1)	mpc		0.9	-0.5	0.3		0.0	0.8	...		...
	CPI	apc		4.9	5.5	6.2		7.8	7.9	8.2		...
	Unemployment rate (1)	%		4.0	3.8	3.7		3.8	3.8	...		...
	Retail sales volume	apc		9.6	7.5	1.9		-5.8	-4.7	-5.8		...
	House prices (6)	apc		11.2	12.6	14.3		12.1	11.2	10.7		11.0
	PMI manufacturing (1)	index		57.3	58.0	55.2		55.8	54.6	52.8		52.1
	Consumer confidence (1)(5)	net %		-19.0	-26.0	-31.0		-38.0	-40.0	-41.0		-41.0
Australia	GDP (1)	qpc	3.6				0.8				...	
	CPI	apc	3.5				5.1				6.1	
	Unemployment rate (1)	%		4.2	4.0	3.9		3.9	3.9	3.5		...
	Retail sales value	apc		5.8	9.1	8.2		11.1	10.2	12.2		...
	House Prices (7)	apc	27.5				...				...
	PMI manufacturing (1)	index		48.4	53.2	55.7		58.5	52.4	54.0		52.5
	Consumer confidence (8)	index		102.2	100.8	96.6		95.8	90.4	86.4		83.8
China	GDP	apc	4.0				4.8				0.4	
	Industrial production	apc		7.5	7.5	5.0		-2.9	0.7	3.9		...
	CPI	apc		0.9	0.9	1.5		2.1	2.1	2.5		...
	PMI manufacturing (1)	index		50.1	50.2	49.5		47.4	49.6	50.2		49.0
South Korea	GDP (1)	qpc	1.3				0.6				0.7	
	Industrial production (1)	mpc		0.4	0.3	1.2		-3.2	0.2	1.9		...
	CPI	apc		3.6	3.7	4.1		4.8	5.4	6.0		6.3

(1) Seasonally adjusted

(2) Case-Shiller Home Price Index 20 city

(3) The Conference Board Consumer Confidence Index

(4) Cabinet Office Japan

(5) European Commission

(6) Nationwide House Price Index

(7) Australian Bureau of Statistics

(8) Melbourne/Westpac Consumer Sentiment Index