Economic Weekly

15 April 2024

As you were, in 140 words

Economists do have a tendency to use more words than they need to – apparently. That was the case, and also not the case, with last week's Monetary Policy Review. The policy assessment statement was the shortest it has probably ever been, at 140 words. That is brevity for summing up and outlining a policy decision. On the other hand, the RBNZ could have taken the ultimate productivity step be simply using four words: "please see February's statement".

In the RBNZ's assessment, there was very little that had changed since February. The economy was evolving "as anticipated", and the risks remained balanced. The RBNZ did change slightly its concluding policy remark. Back in February it finished up with "The OCR needs to remain "at a restrictive level for a sustained period to ensure" inflation got back into the target band. The RBNZ noted this time it was "confident that maintaining the OCR at a restrictive level for a sustained period" would have inflation back in the target band "this calendar year".

That slight change to the ending is a reaffirmation of the inflation forecast that the RBNZ published in February. It comes against the backdrop of a Q1 consumer price index inflation (CPI) outcome that is likely to be above the RBNZ's recent forecast, based on the monthly selected price series that cover 45% of the CPI. In the record of the policy decision meeting, the RBNZ noted that the risk of a higher than anticipated CPI was coming from volatile parts of the overall index (fuel, airfares, and overseas accommodation). It did not appear concerned about longer-term impacts.

In a disappointment for the doves, there wasn't anything in the statement to suggest the RBNZ had softened its stance. The RBNZ restated "there remains limited tolerance to increase the time to achieve the inflation target while inflation remains outside the target band and while inflation expectations and pricing intentions remain elevated".

We still see November as the likely timing for the RBNZ to first cut the OCR – and realistically the earliest the RBNZ would cut barring a significant change in the underlying environment. That's three CPI data releases away, and one of those reads is set to be higher than the RBNZ has factored in, even if for the time being the causes are 'one-offs'.

The story of last week's data releases was of inflation cooling only gradually while activity feels the pressure. The selected price indices from Stats NZ on Friday reinforced that the Q1 CPI increase is likely to be around 0.7% on the previous quarter as opposed to the 0.4% the RBNZ forecast back in February. The good news – particularly for those on low incomes – is that food price inflation has continued to ebb, now down to 0.7% yoy from a peak around 12%. Rental inflation continued to creep up, not unexpected given the population pressure on New Zealand's housing stock. Our full CPI preview ahead of this Wednesday's release can be read here.

The NZIER's Quarterly Survey of Business Opinion showed that price metrics are coming down very slowly and that costs remain pretty sticky. Increasingly, though, sales/demand is the biggest constraint on businesses' ability to expend, while labour as a constraint has eased sharply. The activity measures softened, essentially giving up the post-election bounce in the Q4 survey and looking more realistic relative to the subdued growth environment NZ has been experiencing than the still-lofty ANZ survey equivalent. The activity headwinds were also evident in the March electronic cards transaction data, with retail transactions down 0.7% over the month and total card transactions up only 0.1% for the month.

This week, in addition to the Q1 CPI, migration and REINZ data give us a further sense of how activity is holding up. The latest migration data released this morning come with the usual caveat: NZ migration figures are incredibly volatile. However, the strong February migration figures reveal a reality check to those thinking that net immigration flows will rapidly cool (read Mark Smith's full note here). Housing is inching higher but not with any real momentum. Wednesday's REINZ data will provide the latest steer. It remains an environment of limbo, activity pausing while inflation comes down. But with the prospect still that the RBNZ will have its job done later this year.

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Interest Rate Market

Wholesale interest rates	Current*	Week ago	Month ago	Year ago	ST Bias	MT Bias
Cash rate	5.50	5.50	5.50	5.25	UNCH	DOWN
90-day bank bill	5.65	5.63	5.65	5.54	UNCH	DOWN
2-year swap	5.08	4.95	4.97	5.03	UNCH	DOWN
5-year swap	4.63	4.48	4.42	4.31	UNCH	DOWN
10-year swap	4.66	4.54	4.47	4.21	UNCH	DOWN
10-year govt bond yield	4.80	4.74	4.69	4.10	UNCH	DOWN
Curve Slope (2s10s swaps)	-0.42	-0.40	-0.49	-0.82	UP	UP

* *Current as at 11:00am today; week ago as at Monday 5.00 pm. Key UNCH = Broadly unchanged*

Recap

NZ yields continued to move higher last week, with swap yields about 10-25bp higher since our last update, and with NZ government bond yields about 20-25bps higher last week. There was little market reaction after the RBNZ held the OCR at 5.5% and provided a neutral bias and relatively balanced risk assessment, with the RBNZ looking through near-term upward pressures and expecting sub 3% CPI inflation to be reached by year end (see our take). The fall was despite another weak month for card spending in March (see Nat's take here). Monthly pricing data strongly suggests that Q1 NZ CPI will come in above the RBNZ's 0.4% qoq (3.8% yoy) pick. Q1 QSBO data showed a reversal of the earlier post-election bounce, with the activity struggling and hiring down, but with pricing and cost metrics barely budging. NZ yields have dropped this morning on increased risk aversion after Iran launced missile/drone strikes in Israel in the weekend in retaliation to an airstrike on an Iraniam embassy compound in Syria (captured in the table above).

Rises in NZ yields have outpaced global counterparts, but global yields will likely open lower in global markets today after the Iran attacks. Last week saw the resilient run of US data continue, with US yields up after the stronger than expected US CPI print. Central bank rate cut pricing in the US elsewhere has generally been pared back after FOMC members emphasised the resilience of the US economy and talked down the possibility of imminent Fed rate cuts. The major exception has been the Euerozone, after the ECB held rates but signalled cuts were likely from from June.

Short-term interest rate outlook

Market pricing has ticked up since our last update, with OCR cut odds pared back for 2024. There are now about 50% odds of a cut by August, with about 85% odds of a cut by October and with a total of just under 40bps of cuts for 2024. **This is more in line with our core view, with the RBNZ needing to be confident that inflation will settle below 3% before cutting.** Wednesday's NZ Q1 CPI data is expected to comfortably outstrip RBNZ expectations, but our focus will be what the core measures reveal, with further decleration expected for the RBNZ sectoral model of inflation (4.5% in Q4). We will be checking on whether the run of upward historical revisions on the RBNZ measures starts to show signs of a turn. If so, this would likely bolster the case for rates cuts towards the end of the year. If not, the RBNZ will likely wait for longer and this could see markets continue to price out the possibility of RBNZ cuts.

Global yields will remain senstive to risk aversion and are expected to start this week lower on Middle East tensions. How the conflict plays out will impact yield direction. We are hoping that tensions will subside, but if not, near-term upward pressures are expected for the NZ CPI outlook (via a weaker NZD and higher oil prices). **Increased risk aversion could dampen longer-term yields and see safe havens outperform, with spreads between NZ and US longer-term yields biased to widen**. Data is unlikely to be as big a driver for global yields in this situation.

However, on the data front, after a large 116.5k lift in Aussie employment last month, our CBA colleagues expect a flat result in March, although the degree of uncertainty is higher than normal. Canadian CPI data is expected to show inflation close to the midpoint of the Bank of Canada's 1%-3% target, with the first cut by the Bank of Canada as soon as June. We also expect inflation to ease in the UK and in Japan. Improving signs are expected to emerge from the monthly Chinese data with a solid 5.0% annual expansion in Q1 GDP.

Medium-term outlook

NZ yields are expected to remain volatile until a clearer picture on when central banks will cut rates emerges. This could be some way off. We still expect the NZ yield curve to steepen, with the yield curve to normalise as shorter-term yields drift lower relative to longer-term yields. Our expectation is that the first OCR cut occurs in November, with the OCR gradually trimmed to 3% by mid-2026**.** Our CBA colleagues expect the RBA to cut the 4.25% cash rate in small steps from Q3 2024 (2.85% by mid-2025). The FOMC is expected to cut the 5.25%-5.5% Federal Funds Rate from July 2024, with 75bps of cuts by the end of 2024, and an extended rate cut cycle taking the policy rate to 3% by the end of 2025. As the RBNZ is likely to be towards the end of the central bank rate cut queue, we expect NZ yields to remain above, and then move closer to global peers as OCR cuts are delivered. mark.smith4@asb.co.nz

Foreign Exchange Market

FX Rates	Current*	Week ago	Month ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.5943	0.6012	0.6100	0.6307	FLAT/DOWN	0.5820	0.6080
NZD/AUD	0.9182	0.9135	0.9292	0.9298	FLAT	0.9040	0.9250
NZD/JPY	91.11	91.26	90.50	83.56	FLAT/UP	88.50	92.50
NZD/EUR	0.5582	0.5549	0.5607	0.5697	FLAT/DOWN	0.5550	0.5650
NZD/GBP	0.4771	0.4759	0.4788	0.5030	FLAT	0.4720	0.4900
TWI	70.39	70.7	71.3	70.6	FLAT/DOWN	N/A	N/A

*^ Weekly support and resistance levels * Current as at 11:00 am today; week ago as at Monday 5.00 pm*

As we warned in our last edition, NZD fell sharply last week and is currently trading at 2024 lows. The Kiwi climbed to a high of circa 0.6080 in the first part of the week but fell by more than a cent in the small hours of Wednesday amid the much-stronger-than-anticipated US CPI data. There was a bit more softening over the weekend amid a plethora of hawkish comments from Fed speakers. The escalation in tensions in the Middle East are another NZD negative (and USD positive) as markets resume trading today.

Offshore drivers remain very much the catalyst for NZD moves, with currency movement generally limited in the aftermath of Wednesday's snoozefest of an RBNZ meeting, though NZD/AUD managed a half-a-cent bounce.

Post-CPI USD strength was a broader theme for the currency market as a whole, with all other G10 crosses down 1-3% against the greenback last week. The traditional safe havens JPY and CHF were the next best performers, which might imply at least some of that USD strength has come from heightened risk aversion in markets and not solely the underlying moves in relative interest rates.

Near-term outlook

Ongoing geopolitical tensions and the likelihood that US interest rates will stay higher for longer are considerable USD supports for the time being. Accordingly, we see USD mostly consolidating its position this week, particularly in the event of any further escalation in tensions between Iran and Israel.

NZD could be the exception to that trend, recovering some of last week's losses if local CPI data on Wednesday prints on the strong side of expectations. **That said, a lower ceiling means that any bounce in NZD/USD should run into resistance around 0.6080.**

Among other crosses, a strong CPI print would also support gains for the always rates-sensitive NZD/AUD, with resistance eyed around the 0.9250 mark. NZD/JPY remains vulnerable to any intervention by BoJ, in the event JPY comes under further pressure versus the USD.

Medium-term outlook

Despite the present patch of softness, we expect NZD to resume its move cyclically higher as 2024 wears on, global growth recovers and commodity prices improve further. The most bearish expectations around the global and Chinese economies have passed despite some lingering weakness, and pro-cyclical or China-exposed currencies are likely to be the beneficiaries.

Our base case sees NZD/USD trending higher over H2 2024, reaching 0.6600 by year-end. That said, given the recent strength in US inflation data, the risks to that forecast are tilted to the downside. Higher-for-longer US interest rates could imply NZD/USD appreciates more slowly and to a lower endpoint this year than previously anticipated.

NZD can trend higher against JPY, EUR, and GBP from H2 2024 for the same cyclical reasons. JPY's recent weakness means our NZD/JPY have been nudged up (despite the risk of BoJ intervention), with the cross projected to reach circa 93.7 by year-end and 95.8 by the end of 2025.

We expect NZD/AUD to drift lower over the next couple of quarters in line with the present underperformance of the NZ economy, before rising thereafter.

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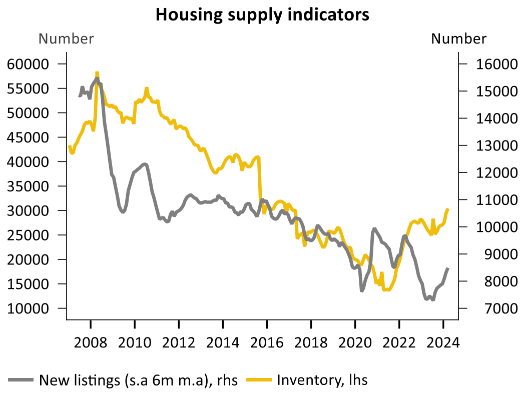
Domestic events for this week

Data	Date	Time (NZT)	Previous	Market Expects	ASB Expects
REINZ Housing Data, March, HPI, % mom	17/4	9:00am	0.2		Small lift
CPI, Headline, Q1, % qoq	17/4	10:45am	0.5		0.7

The latest migration data released this morning come with the usual caveat: NZ migration figures are incredibly volatile, and subject to large revisions. February data represents a reality check to those thinking that net immigration flows will rapidly cool (read Mark Smith's full note here). Meanwhile, visitor numbers were up a seasonally adjusted 0.9% in February, with annual visitor numbers (3.11m) edging higher and at post-COVID highs.

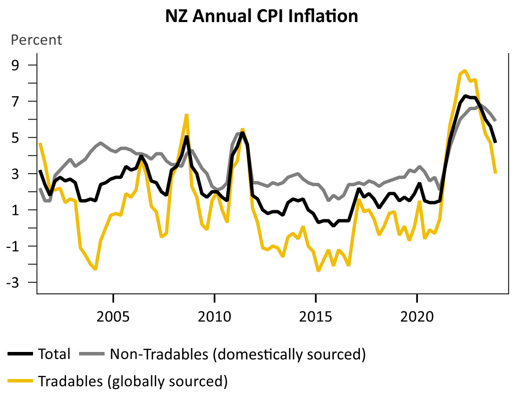
We expect the REINZ house price index will show another small lift in house prices in March. There is a bit of a tug-o-war underway between key tailwinds and headwinds in the housing market at the moment. Strong population growth, a more favourable policy mix and soft construction activity suggest that house prices can continue to lift. However, affordability constraints and relatively high inventory levels should keep a lid on the pace of any gains over the coming months. Nevertheless, with the headwinds likely to give way to tailwinds as the year progresses, we still expect to see a more pronounced upswing develop over 2024.



Source: Macrobond, ASB

Our CPI pick is for a 0.7% quarterly increase in headline CPI in Q1, above February MPS expectations. Importantly however, the general cooling in annual inflation is expected continue, with annual headline inflation down to 4.1%, its lowest in almost 3 years. Rates of annual core inflation are also expected to cool.

We expect lower tradable inflation will continue to be the key driver of cooling headline inflation. Easing global goods inflation is weighing on tradable prices, with lower fuel prices also impacting the quarterly print. On the other hand, non-tradable inflation remains sticky, with a solid 1.2% quarterly print pencilled in. Although a 6.5% lift in tobacco prices will largely be looked through. We still expect headline inflation to fall back below 3% by Q3 24. But uncertainty over the inflation outlook is still high. Lingering upside risks, including to tradable inflation, suggest the RBNZ will continue to err on the side of caution. We don't anticipate rate cuts until November 2024.



Source: Macrobond, ASB

Major International Events for the week ahead

Data		Date	Time (NZT)	ASB
US	Retail Sales, Mar	16/4	12.30am	0.4%/mth
CN	Industrial Production, Mar	16/4	2.00pm	6.0%/yr
	Retail Sales	-	-	4.5%/yr
	Fixed Assets Ex Rural YTD	-	-	4.2%/yr
	GDP, Q1 2024	-	-	1.2%/qtr
UK	Labour Market Data, Feb	16/4	6.00pm	-
CA	Headline CPI, Mar	17/4	12.30am	-
UK	Headline CPI, Mar	17/4	6.00pm	3.2%/yr
	Core CPI	-	-	4.1%/yr
AU	Labour Force, Mar	18/4	1.30pm	-
	Employment	-	-	0k
	Participation Rate	-	-	66.7%
	Unemployment Rate	-	-	3.9%
JN	CPI, Mar	19/4	11:30am	2.6%/yr
	Excluding Fresh Food & Energy	-	-	3.0%/yr

** Forecasts and commentary originally published by CBA Global Markets Research Friday 12th of April.*

Offshore there is a raft of inflation data released this week. In Canada CPI is again expected to be benign and see inflation close to the midpoint of the Bank of Canada's 1%-3% target. Our CBA colleagues expect the first rate cut from the Bank of Canada to occur in June.

We also expect inflation to ease in the UK and in Japan. In the UK, the annual rate of both headline and core CPI inflation can ease further in March to 3.2%/yr and 4.1%/yr respectively. High interest rates are dampening economic activity and inflationary pressures in the UK. The already released Tokyo inflation suggests the headline national inflation likely eased a touch in March. The BoJ's core inflation measure also likely continued to ease, though remains well above its 2%/yr inflation target.

China's monthly data dump is scheduled for Tuesday, as well as Q1 24 GDP. China's economic activity data so far this year has shown some signs of improvement, and our colleagues at CBA expect GDP growth picked up to 1.2%/qtr.

UK labour market data has been volatile because of low survey response rates. On balance there are some tentative signs that the labour market has become a little less tight, with the latest data out on Tuesday night.

In Australia the latest monthly labour data is released on Thursday. Australia's labour force data has experienced a larger than normal degree of volatility in recent months. The seasonal adjustment of the data by the ABS, changing patterns of people starting work and changing spending patterns have all impacted on the monthly numbers. In February a large 116.5k lift in employment occurred, as more people started work than normal and as a result the unemployment rate fell from 4.1% to 3.7%. Second tier labour market data as well as broader economic conditions suggest the labour market is loosening. CBA expect flat employment growth in March and the unemployment rate to rise to 3.9% on an unchanged participation rate. But our CBA colleagues flag recent volatile numbers and seasonal adjustment challenges lead to more uncertainty than normal.

Key Forecasts

ASB NZ economic forecasts	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Mar-25	Mar-26
	<< actual	forecast >>						
GDP real - Q%	-0.1	-0.2	-0.2	-0.2	0.0	0.3	0.3	1.0
GDP real - A%	-0.3	-0.1	-0.8	-0.7	-0.6	-0.1	-0.1	3.4
GDP real - AA%	0.6	0.1	-0.5	-0.5	-0.6	-0.6	-0.6	2.1
NZ House Prices (QV Index) - A%	-1.2	1.8	2.3	3.7	7.3	11.3	11.3	13.9
CPI - Q%	0.5	0.7	1.0	0.6	0.5	0.5	0.5	0.5
CPI - A%	4.7	4.1	4.0	2.8	2.9	2.6	2.6	2.2
HLFS employment growth - Q%	0.4	0.3	0.0	0.0	0.0	0.2	0.2	0.5
HLFS employment growth - A%	2.4	1.7	0.6	0.7	0.3	0.2	0.2	1.8
Unemployment rate - %sa	4.0	4.2	4.5	4.8	5.2	5.4	5.4	5.1

Q% = percentage change on previous quarter

A% = percentage change since same quarter the previous year

AA% = percentage change for year ending quarter since the previous year

ASB interest rate forecasts	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Mar-26
(end of quarter)	<< actual	forecast >>						
NZ OCR	5.50	5.50	5.50	5.25	5.00	4.50	4.00	3.25
NZ 90-day bank bill	5.64	5.60	5.50	5.25	5.00	4.50	4.00	3.30
NZ 2-year swap rate	4.79	4.85	4.70	4.50	4.35	4.20	4.05	3.75
NZ 5-year swap rate	4.29	4.40	4.30	4.20	4.10	4.00	3.95	3.85
NZ 10-year swap rate	4.36	4.50	4.40	4.30	4.20	4.10	4.00	3.85
NZ 10-year Bond	4.59	4.70	4.58	4.45	4.33	4.20	4.08	3.88

ASB foreign exchange forecasts	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Mar-26
(end of quarter)	<< actual	forecast >>						
NZD/USD	0.60	0.61	0.64	0.66	0.68	0.70	0.71	0.72
NZD/AUD	0.92	0.92	0.93	0.93	0.93	0.93	0.93	0.92
NZD/JPY	91	90	92	94	95	96	96	96
NZD/GBP	0.47	0.48	0.50	0.51	0.52	0.52	0.53	0.53
NZD/EUR	0.55	0.56	0.57	0.57	0.58	0.57	0.57	0.58
NZD/CNY	4.3	4.4	4.5	4.7	4.8	4.8	4.8	4.8
NZD TWI	70.5	70.2	72.6	74.1	75.5	76.7	77.1	77.5

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