



Westland Tai Poutini National Park, New Zealand

# Weekly Economic Commentary.

**You ain't seen nothing yet.**

The New Zealand economy has entered a Covid-induced recession, but the official data so far captures only a fraction of the total impact. We expect more pain to come in terms of the hit to activity, employment and house prices. No part of the country will be spared from these impacts, though there are some differences across industries and regions that are worth highlighting.

New Zealand's GDP shrank by 1.6% in the March quarter, the biggest one-quarter drop in almost 30 years. The economy started the year in reasonable shape, but the Covid-19 pandemic rapidly escalated and in the last week of March the country entered a strict lockdown period. We've previously estimated that under lockdown the economy was running about a third below its potential, so even a single week of lockdown could have knocked about 2.5% off quarterly GDP.

The drop in March quarter GDP was large, but the June quarter result (due to be released on 17 September) will be off the scale. The country remained in a strict lockdown through to the end of April, with a steady easing of domestic restrictions since then. While daily and weekly data show that activity has bounced back strongly as the restrictions have been lifted, the length and severity of the lockdown make it almost inevitable that the drop in June quarter GDP will be in the double digits.

At this early stage there's a wide range of forecasts around the market. Our current forecast of a 13.5% decline is one of the milder estimates. In contrast, last month both the RBNZ and the Treasury estimated the Q2 decline at more than 20%, although stronger recent data makes it likely that those forecasts have been upgraded since then.

Looking further ahead, we expect an equally off-the-scale 14% rise in GDP for the September quarter (assuming that the country remains at Alert Level 1). But that would still leave GDP well below its pre-Covid trend. International travel will be out of action for some time, and the economic 'scarring' from the outbreak, including increases in debt, business closures and a rise in unemployment, will be an ongoing drag on activity. We expect the unemployment rate to peak at 8% this year, and a return to pre-Covid levels is likely to be many years away, even with the jobs-heavy orientation of the Government's \$62bn fiscal package.



Over the past few years there have been stark differences in the economic fortunes of New Zealand's regions. But as we highlight in our latest Regional Roundup, Covid-19 will be a great leveller. No region will be immune to the coming recession, and the economic outlook now looks more similar right across the country. We expect all regions to experience a deep recession and rising unemployment this year, followed by a recovery from late 2021 or early 2022.

The severity of the post-lockdown recession in each region, and the pace of recovery, will depend on the industry makeup of that region. Worst affected will obviously be the places that rely most heavily on overseas tourism – particularly the Queenstown-Lakes district, but the South Island in general will be hit much harder than the North.

Regions that are heavy on agriculture, forestry, and export manufacturing are also going to feel the effect of the global recession. Our expectation is that viticulture and forestry in particular will struggle. In contrast, the ongoing global demand for protein means that dairy, sheep and beef will be relatively resilient. Indeed, there has already been some uptick in world prices in recent weeks. We have upgraded our farmgate milk price forecast for this season to \$6.50/kg, slightly above the long-run average.

As we noted in a recent report, the construction industry faces another significant downturn in 2021. There is plenty of work in the pipeline right now, including projects that were halted during the lockdown period. But forward orders are drying up and some planned projects are likely to be

cancelled. Construction is a feature of all regional economies, but the upstream manufacturing, distribution and services that are associated with construction are more heavily concentrated in Auckland, Waikato and Canterbury.

Meanwhile, house prices are expected to fall in all regions. In fact this is already under way, with the REINZ house price index falling by 1.2% over April and May. The standout weak region so far is not surprisingly the Queenstown-Lakes district, where prices are already down by more than 6%. Based on past recessions, we expect nationwide house prices to fall by 7% by the end of this year.

The best prospects for recovery lie in urban industries like services, distribution, and digital technology. The most obvious way that Covid-19 will change the economy is greater digitisation. ICT, software development, and online service providers have had a real leg up, and we think that bodes relatively well for Wellington and Auckland. The other resilient industry will be government, which is a third of the economy and is stepping up to support the ailing private sector. While the Government provides services throughout the country, it is heavily represented in Wellington.

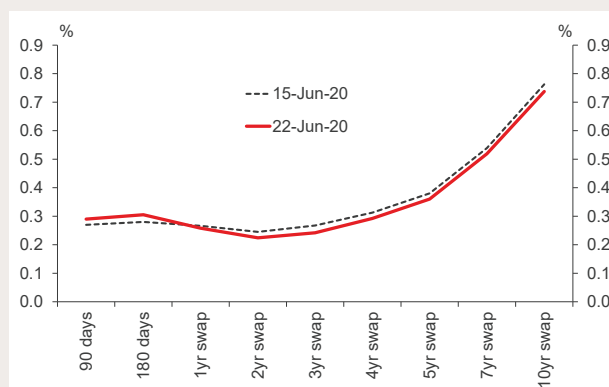
Putting all of this together suggests a weaker outlook for the south of the country and in regions with a lot of forestry, while Wellington and Auckland have the strongest prospects, followed by Bay of Plenty and Waikato. But this is only a relative picture – every part of the country is in for a rough ride this year.

## Fixed vs Floating for mortgages.

Fixed mortgage rates have fallen recently, but they may not drop much further in the near term. The drop in mortgage rates this year is now roughly commensurate with the drop in wholesale rates.

We are forecasting fairly stable interest rates this year, but early next year we expect that the RBNZ will lower the OCR to -0.5%. If that is correct, then both fixed and floating rates will fall next year.

NZ interest rates



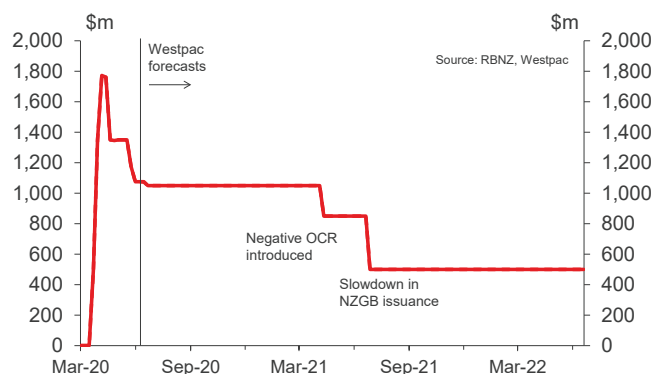
# The week ahead.

## NZ RBNZ Official Cash Rate review

**June 24, Last: 0.25%, WBC f/c: 0.25%, Mkt f/c: 0.25%**

- We expect the RBNZ to keep its monetary policy stance unchanged. The economy is proving more resilient than expected, but this is offset by a higher exchange rate.
- We expect that the weekly pace of bond buying under the LSAP will stay slightly above \$1bn for the foreseeable future.
- The RBNZ will have to lift the \$60bn cap on the LSAP at some point, just to allow headroom for that pace of bond buying to continue. There is a chance that the cap will rise to \$70bn next week. But more likely, the RBNZ will leave the cap unchanged this time, and lift it to \$80bn in Aug in a single hit.
- The RBNZ is likely to reiterate that it has other monetary tools available, but will not signal that these are necessary at this point.

## RBNZ bond purchases



## May US personal income and spending

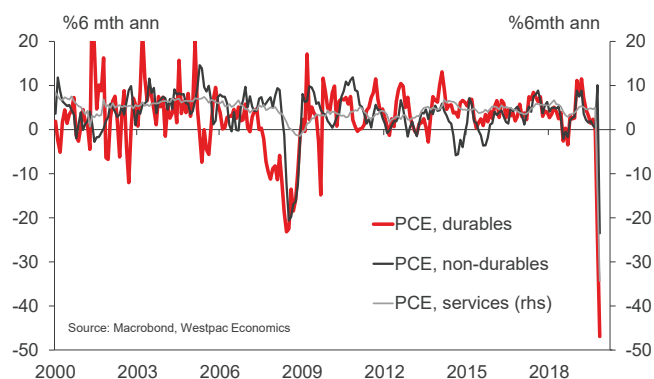
**Jun 26, personal income: last: 10.5%, WBC: -4.5%**

**Jun 26, personal spending: last: -13.6%, WBC: 8.0%**

**Jun 26, PCE deflator: last -0.5%, WBC: 0.0%**

- The personal income and spending data was materially affected by COVID-19 and authorities' response in Mar and Apr. Personal income initially dropped 2.2% in Mar, but then surged 10.5% in Apr as government payments more than offset the decline in income due to job loss. Spending meanwhile collapsed 13.6% in Apr, bringing the cumulative decline for the two months to over 20%.
- In May, a further decline in income seems likely given the degree of slack present in the labour market. As per the 18% rebound in retail sales already reported, spending should rally back in the month. Note though that social distancing will materially impede services, hence the gain for personal spending should be much smaller than for retail sales.

## Hit to US consumption broadbased

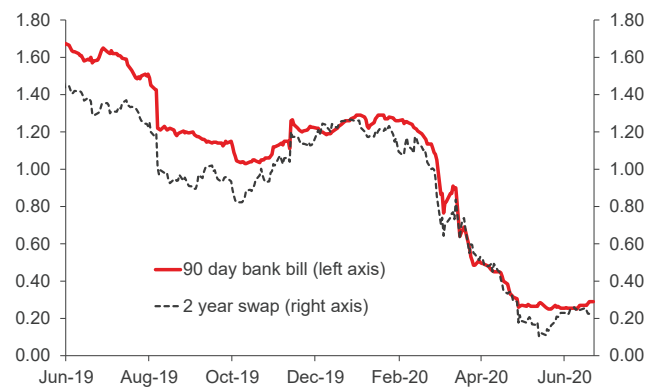


# New Zealand forecasts.

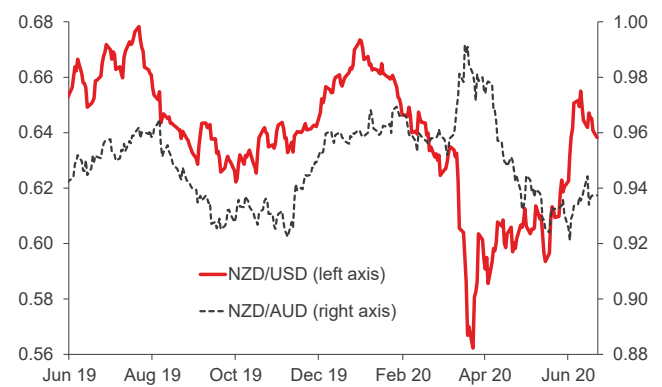
Economic forecasts	Quarterly				Annual			
	2019	2020			2018	2019	2020f	2021f
% change	Dec (a)	Mar	Jun	Sep				
GDP (Production)	0.5	-1.6	-13.5	14.0	3.2	2.3	-4.6	5.1
Employment	0.1	0.7	-7.5	0.7	1.9	0.8	-4.9	3.4
Unemployment Rate % s.a.	4.0	4.2	7.0	8.0	4.3	4.0	7.5	6.6
CPI	0.5	0.8	-0.5	0.8	1.9	1.9	0.8	0.4
Current Account Balance % of GDP	-3.0	-2.7	-2.1	-1.7	-3.8	-3.0	-1.7	-2.0

Financial forecasts	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21
Cash	0.25	0.25	0.25	-0.50	-0.50	-0.50
90 Day bill	0.25	0.20	-0.10	-0.20	-0.20	-0.20
2 Year Swap	0.10	0.00	-0.10	-0.10	-0.10	0.00
5 Year Swap	0.30	0.25	0.25	0.30	0.40	0.50
10 Year Bond	0.85	0.85	0.85	0.90	1.00	1.10
NZD/USD	0.65	0.65	0.64	0.65	0.66	0.67
NZD/AUD	0.93	0.90	0.88	0.88	0.88	0.88
NZD/JPY	68.9	68.9	68.5	69.6	71.3	72.4
NZD/EUR	0.58	0.57	0.56	0.56	0.56	0.57
NZD/GBP	0.52	0.51	0.50	0.51	0.51	0.52
TWI	71.5	70.6	69.1	69.7	70.2	70.7

2 year swap and 90 day bank bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on 22 June 2020

Interest rates	Current	Two weeks ago	One month ago
Cash	0.25%	0.25%	0.25%
30 Days	0.27%	0.27%	0.26%
60 Days	0.28%	0.26%	0.26%
90 Days	0.29%	0.26%	0.25%
2 Year Swap	0.22%	0.25%	0.16%
5 Year Swap	0.36%	0.42%	0.23%

NZ foreign currency mid-rates as at 22 June 2020

Exchange rates	Current	Two weeks ago	One month ago
NZD/USD	0.6383	0.6500	0.6093
NZD/EUR	0.5705	0.5756	0.5592
NZD/GBP	0.5170	0.5123	0.5001
NZD/JPY	68.16	71.24	65.56
NZD/AUD	0.9374	0.9330	0.9329
TWI	71.33	72.13	69.16

## Data calendar.

		Last	Market median	Westpac forecast	Risk/Comment
<b>Mon 22</b>					
Aus	RBA Governor Lowe	-	-	-	Panel, Leadership Forum, "Global Economy & COVID".
Eur	Jun consumer confidence	-18.8	-14.5	-	A modest improvement on easing restrictions expected.
US	May Chicago Fed activity index	-16.7	-	-	Regional surveys point to strong confidence over outlook.
	May existing home sales	-17.8%	-4.2%	-	Turnover to remain low for a lengthy period.
<b>Tue 23</b>					
Aus	May merchandise trade, prelim	-	-	-	Data in "unfriendly format": customs basis, not seasonally adj.
Eur	Jun Markit manufacturing PMI	39.4	43.0	-	Euro zone as a whole is also experiencing the...
	Jun Markit services PMI	30.5	40.0	-	... beginning of a broad-based recovery.
US	Jun Markit manufacturing PMI	39.8	47.8	-	Regional surveys have surprised materially to the upside...
	Jun Markt service PMI	37.5	44.8	-	... but much of this strength has been due to expectations.
	May new home sales	0.6%	1.1%	-	Home sales unlikely to see strong rebound in near term.
	Jun Richmond Fed index	-27	-11	-	Regional surveys have been very positive this month.
<b>Wed 24</b>					
NZ	RBNZ policy decision	0.25%	0.25%	0.25%	RBNZ to maintain weekly pace of bond purchases.
Chn	Q1 current account balance, \$bn	-29.7	-	-	Services balance to be very supportive of g'th in 2020.
US	Apr FHFA house prices	0.10%	-	-	The index has recorded slight gains throughout COVID-19.
	Fedspeak	-	-	-	FOMC Evans and Bullard.
<b>Thu 25</b>					
NZ	May trade balance \$m	1,267	1,290	1,250	Imports remain subdued under COVID-19 conditions.
US	May wholesale inventories	0.30%	-	-	Likely to detract from growth through mid-20.
	Q1 GDP	-5.0%	-5.0%	-	Final estimate for the quarter. No revision expected.
	May durable goods orders	-17.7%	12.0%	-	A robust rebound anticipated as business re-opens.
	Initial jobless claims, '000	1,508	-	-	Downtrend seems to be losing momentum.
	Jun Kansas City Fed index	-19	-10	-	Regional surveys have been very positive this month.
	Fedspeak	-	-	-	FOMC Bostic.
<b>Fri 26</b>					
NZ	Jun ANZ consumer confidence	97.3	-	-	Has picked up as lockdown has eased, still very low.
Chn	Industrial Profits %yr	-4.3%	-	-	Stimulus necessary to support SOE and private business.
Eur	May M3 money supply %yr	8.3%	-	-	ECB actions have put money supply on strong uptrend.
US	May personal income	10.5%	-5.8%	-4.5%	Income was boosted by federal payments under CAREs Act.
	May personal spending	-13.6%	8.7%	8.0%	Savings rate at record 33% in Apr. Spending to rebound.
	May PCE deflator	-0.5%	0.0%	0.0%	Inflation to remain weak in coming months on oil...
	May core PCE deflator	-0.4%	0.0%	0.0%	... and given sharp increase in economic slack.
	Jun Uni. of Michigan sentiment, final	78.9	78.9	-	Sentiment climbed in June as employers restored jobs.

## International forecasts.

Economic forecasts (Calendar years)	2016	2017	2018	2019	2020f	2021f
<b>Australia</b>						
Real GDP % yr	2.8	2.5	2.8	1.8	-3.6	2.5
CPI inflation % annual	1.5	1.9	1.8	1.8	0.2	2.3
Unemployment %	5.7	5.5	5.0	5.2	8.3	7.1
Current Account % GDP	-3.1	-2.6	-2.0	0.6	2.5	1.0
<b>United States</b>						
Real GDP %yr	1.6	2.4	2.9	2.3	-5.5	2.1
Consumer Prices %yr	1.4	2.1	2.4	1.9	0.7	1.4
Unemployment Rate %	4.9	4.4	3.8	3.7	12.7	9.8
Current Account %GDP	-2.3	-2.3	-2.3	-2.6	-2.5	-2.4
<b>Japan</b>						
Real GDP %yr	0.5	2.2	0.3	0.7	-5.0	1.0
<b>Euro zone</b>						
Real GDP %yr	1.9	2.5	1.9	1.2	-8.5	1.7
<b>United Kingdom</b>						
Real GDP %yr	1.9	1.9	1.3	1.4	-7.0	2.5
<b>China</b>						
Real GDP %yr	6.8	6.9	6.8	6.1	0.1	10.0
<b>East Asia ex China</b>						
Real GDP %yr	4.1	4.6	4.4	3.7	-2.6	5.5
<b>World</b>						
Real GDP %yr	3.4	3.9	3.6	2.8	-3.0	4.9

Forecasts finalised 12 June 2020

Interest rate forecasts	Latest	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21
<b>Australia</b>							
Cash	0.25	0.25	0.25	0.25	0.25	0.25	0.25
90 Day BBSW	0.10	0.10	0.15	0.20	0.25	0.30	0.35
10 Year Bond	0.92	1.00	1.00	1.05	1.15	1.25	1.35
<b>International</b>							
Fed Funds	0.125	0.125	0.125	0.125	0.125	0.125	0.125
US 10 Year Bond	0.75	0.75	0.75	0.80	0.85	0.90	0.95

Exchange rate forecasts	Latest	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21
AUD/USD	0.6888	0.70	0.72	0.73	0.74	0.75	0.76
USD/JPY	107.39	106	106	107	107	108	108
EUR/USD	1.1262	1.13	1.14	1.15	1.16	1.17	1.18
GBP/USD	1.2572	1.26	1.27	1.27	1.28	1.29	1.30
USD/CNY	7.0862	7.00	6.90	6.85	6.80	6.70	6.60
AUD/NZD	1.0678	1.08	1.11	1.14	1.14	1.14	1.13

# Contact the Westpac economics team.

**Dominick Stephens, Chief Economist**

+64 9 336 5671

**Michael Gordon, Senior Economist**

+64 9 336 5670

**Satish Ranchhod, Senior Economist**

+64 9 336 5668

**Nathan Penny, Senior Agri Economist**

+64 9 348 9114

**Paul Clark, Industry Economist**

+64 9 336 5656

**Any questions email:**

economics@westpac.co.nz

Past performance is not a reliable indicator of future performance. The forecasts given in this document are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

## Disclaimer.

### Things you should know

Westpac Institutional Bank is a division of Westpac Banking Corporation ABN 33 007 457 141 ("Westpac").

### Disclaimer

This material contains general commentary, and market colour. The material does not constitute investment advice. Certain types of transactions, including those involving futures, options and high yield securities give rise to substantial risk and are not suitable for all investors. We recommend that you seek your own independent legal or financial advice before proceeding with any investment decision. This information has been prepared without taking account of your objectives, financial situation or needs. This material may contain material provided by third parties. While such material is published with the necessary permission none of Westpac or its related entities accepts any responsibility for the accuracy or completeness of any such material. Although we have made every effort to ensure the information is free from error, none of Westpac or its related entities warrants the accuracy, adequacy or completeness of the information, or otherwise endorses it in any way. Except where contrary to law, Westpac and its related entities intend by this notice to exclude liability for the information. The information is subject to change without notice and none of Westpac or its related entities is under any obligation to update the information or correct any inaccuracy which may become apparent at a later date. The information contained in this material does not constitute an offer, a solicitation of an offer, or an inducement to subscribe for, purchase or sell any financial instrument or to enter a legally binding contract. Past performance is not a reliable indicator of future performance. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

### Country disclosures

**Australia:** Westpac holds an Australian Financial Services Licence (No. 233714). This material is provided to you solely for your own use and in your capacity as a wholesale client of Westpac.

**New Zealand:** In New Zealand, Westpac Institutional Bank refers to the brand under which products and services are provided by either Westpac or Westpac New Zealand Limited ("WNZL"). Any product or service made available by WNZL does not represent an offer from Westpac or any of its subsidiaries (other than WNZL). Neither Westpac nor its other subsidiaries guarantee or otherwise support the performance of WNZL in respect of any such product. The current disclosure statements for the New Zealand branch of Westpac and WNZL can be obtained at the internet address [www.westpac.co.nz](http://www.westpac.co.nz). For further information please refer to the Product Disclosure Statement (available from your Relationship Manager) for any product for which a Product Disclosure Statement is required, or applicable customer agreement. Download the Westpac NZ QF Group Financial Advisers Act 2008 Disclosure Statement at [www.westpac.co.nz](http://www.westpac.co.nz).

**China, Hong Kong, Singapore and India:** This material has been prepared and issued for distribution in Singapore to institutional investors, accredited investors and expert investors (as defined in the applicable Singapore laws and regulations) only. Recipients in Singapore of this material should contact Westpac Singapore Branch in respect of any matters arising from, or in connection with, this material. Westpac Singapore Branch holds a wholesale banking licence and is subject to supervision by the Monetary Authority of Singapore. Westpac Hong Kong Branch holds a banking licence and is subject to supervision by the Hong Kong Monetary Authority. Westpac Hong Kong branch also holds a license issued by the Hong Kong Securities and Futures Commission (SFC) for Type 1 and Type 4 regulated activities. This material is intended only to "professional investors" as defined in the Securities and Futures Ordinance and any rules made under that Ordinance. Westpac Shanghai and Beijing Branches hold banking licenses and are subject to supervision by the China Banking and Insurance Regulatory Commission (CBIRC). Westpac Mumbai Branch holds a banking license from Reserve Bank of India (RBI) and subject to regulation and supervision by the RBI.

**UK:** The contents of this communication, which have been prepared by and are the sole responsibility of Westpac Banking Corporation London and Westpac Europe Limited. Westpac (a) has its principal place of business in the United Kingdom at Camomile Court, 23 Camomile Street, London EC3A 7LL, and is registered at Cardiff in the UK (as Branch No. BR00106), and (b) authorised and regulated by the Australian Prudential Regulation Authority in Australia. Westpac is authorised in the United Kingdom by the Prudential Regulation Authority. Westpac is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request. Westpac Europe Limited is a company registered in England (number 05660023) and is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

This communication is being made only to and is directed at (a) persons who have professional experience in matters relating to investments who fall within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the "Order") or (b) high net worth entities, and other persons to whom it may otherwise lawfully be communicated, falling within Article 49(2)(a) to (d) of the Order (all such persons together being referred to as "relevant persons"). Any person who is not a relevant person should not act or rely on this communication or any of its contents. The investments to which this communication relates are only available to and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such investments will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely upon this communication or any of its contents. In the same way, the information contained in this communication is intended for "eligible counterparties" and "professional clients" as defined by the rules of the Financial Conduct Authority and is not intended for "retail clients". With this in mind, Westpac expressly prohibits you from passing on the information in this communication to any third party. In particular this communication and, in each case, any copies thereof may not be taken, transmitted or distributed,

directly or indirectly into any restricted jurisdiction. This communication is made in compliance with the Market Abuse Regulation (Regulation(EU) 596/2014).

### Investment Recommendations Disclosure

The material may contain investment recommendations, including information recommending an investment strategy. Reasonable steps have been taken to ensure that the material is presented in a clear, accurate and objective manner. Investment Recommendations for Financial Instruments covered by MAR are made in compliance with Article 20 MAR. Westpac does not apply MAR Investment Recommendation requirements to Spot Foreign Exchange which is out of scope for MAR.

Unless otherwise indicated, there are no planned updates to this Investment Recommendation at the time of publication. Westpac has no obligation to update, modify or amend this Investment Recommendation or to notify the recipients of this Investment Recommendation should any information, including opinion, forecast or estimate set out in this Investment Recommendation change or subsequently become inaccurate.

Westpac will from time to time dispose of and acquire financial instruments of companies covered in this Investment Recommendation as principal and act as a market maker or liquidity provider in such financial instruments.

Westpac does not have any proprietary positions in equity shares of issuers that are the subject of an investment recommendation.

Westpac may have provided investment banking services to the issuer in the course of the past 12 months.

Westpac does not permit any issuer to see or comment on any investment recommendation prior to its completion and distribution.

Individuals who produce investment recommendations are not permitted to undertake any transactions in any financial instruments or derivatives in relation to the issuers covered by the investment recommendations they produce.

Westpac has implemented policies and procedures, which are designed to ensure conflicts of interests are managed consistently and appropriately, and to treat clients fairly.

The following arrangements have been adopted for the avoidance and prevention of conflicts of interests associated with the provision of investment recommendations.

- (i) Chinese Wall/Cell arrangements;
- (ii) physical separation of various Business/Support Units;
- (iii) and well defined wall/cell crossing procedures;
- (iv) a "need to know" policy;
- (v) documented and well defined procedures for dealing with conflicts of interest;
- (vi) steps by Compliance to ensure that the Chinese Wall/Cell arrangements remain effective and that such arrangements are adequately monitored.

**U.S.:** Westpac operates in the United States of America as a federally licensed branch, regulated by the Office of the Comptroller of the Currency. Westpac is also registered with the US Commodity Futures Trading Commission ("CFTC") as a Swap Dealer, but is neither registered as, or affiliated with, a Futures Commission Merchant registered with the US CFTC. Westpac Capital Markets, LLC ("WCM"), a wholly-owned subsidiary of Westpac, is a broker-dealer registered under the U.S. Securities Exchange Act of 1934 ("the Exchange Act") and member of the Financial Industry Regulatory Authority ("FINRA"). This communication is provided for distribution to U.S. institutional investors in reliance on the exemption from registration provided by Rule 15a-6 under the Exchange Act and is not subject to all of the independence and disclosure standards applicable to debt research reports prepared for retail investors in the United States. WCM is the U.S. distributor of this communication and accepts responsibility for the contents of this communication. All disclaimers set out with respect to Westpac apply equally to WCM. If you would like to speak to someone regarding any security mentioned herein, please contact WCM on +1 212 389 1269. All disclaimers set out with respect to Westpac apply equally to WCM.

Investing in any non-U.S. securities or related financial instruments mentioned in this communication may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the SEC in the United States. Information on such non-U.S. securities or related financial instruments may be limited. Non-U.S. companies may not be subject to audit and reporting standards and regulatory requirements comparable to those in effect in the United States. The value of any investment or income from any securities or related derivative instruments denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related derivative instruments.

The author of this communication is employed by Westpac and is not registered or qualified as a research analyst, representative, or associated person under the rules of FINRA, any other U.S. self-regulatory organisation, or the laws, rules or regulations of any State. Unless otherwise specifically stated, the views expressed herein are solely those of the author and may differ from the information, views or analysis expressed by Westpac and/or its affiliates.