RESEARCH

Markets Outlook

6 September 2021

Vaccinations No Panacea

- **Full NZ vaccination will see less restriction in 2022**
- **But more COVID and more deaths**
- **This will impact confidence and spending**
- **While supply constraints remain problematic**
- **Resulting in higher inflation and interest rates**

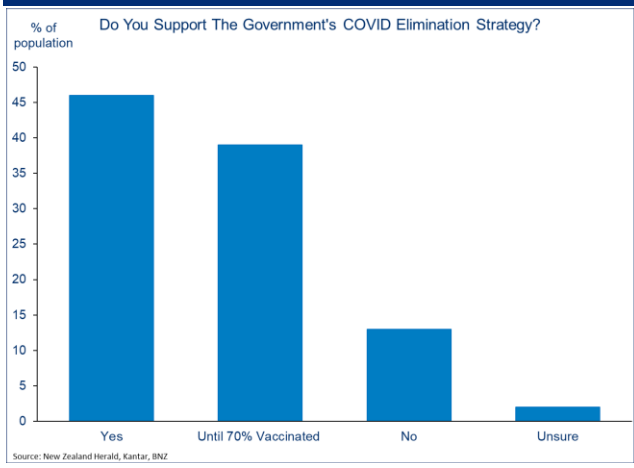
It seems highly likely that by early next year New Zealand will be progressively easing its border restrictions. Moreover, with the great majority of New Zealanders fully vaccinated by then, it will become increasingly less likely that people will again experience, or even accept, lockdowns of the current intensity. This is all great news, and is a very real cause for optimism about the future. However, we are concerned that many are starting to assume life will be a lot more rosy post vaccination than will actually be the case. A post lockdown world will come with its own set of challenges, many of which will stay with us for months/years to come. A lot of the issues that currently confront us will not magically disappear with the vaccine roll out, and there is certainly no going back to a pre-COVID world.

First the vaccines. There is a lot of political hand waving around this topic at the moment, which is tending to cloud the key matter of importance and that is, one way or t'other, it looks almost certain every New Zealander who wants to be vaccinated will have had that opportunity by the end of the year. The only real debate is how quickly can the vaccination be rolled out? As things stand, 3.684 million vaccination doses have been administered. There are 17 weeks left in 2021. The government is confident it will be able to administer at least a further 350,000 doses a week. That's another 5.95 million doses. Add the two numbers together you get 9.634 million doses, or 4.817 million people by year's end. For all intents and purposes that will be more than the number of people in New Zealand who are either old enough or desirous enough to get vaccinated. Sure, the requirement to get two doses with a six week gap between the two might mean full coverage drifts into next year but, by the end of February, there can be little doubt the population will have enough vaccine protection for the rules to change. Were we to maintain our current vaccination rate of 500,000 per week that would bring forward the end date by around four weeks.

When the majority of the population is vaccinated the politics of restrictions will change. When the country had no one vaccinated, we were COVID free and the rest of the world wasn't, the electorate overwhelmingly demanded that the disease be kept at bay at any cost. But as the pendulum swings on the vaccination dial, a greater and greater number of people will no longer accept the restrictions that we currently so willingly abide by. Therefore, change is inevitably on its way.

Supporting this view was last week's New Zealand Herald poll which showed that 85% of the population supported the current elimination strategy. However, that support drops to 46% if the country is 70% vaccinated.

New Zealanders like elimination – for now



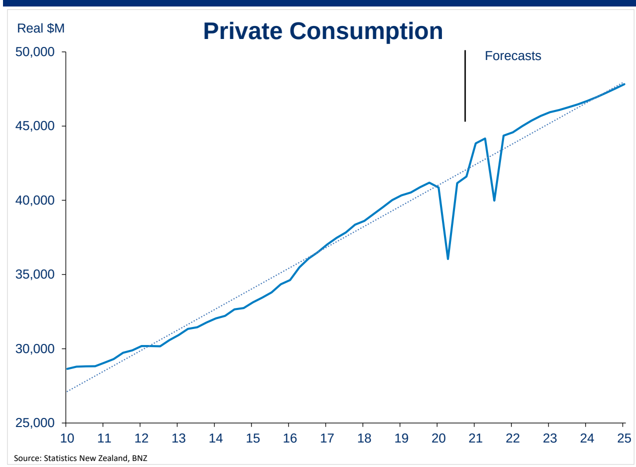
The problem is vaccination will not mean the end of COVID. Even the most heavily vaccinated countries in the world are still experiencing substantial numbers of infections, pressure on health care systems and a significant number of deaths. In England, for example, 78% of over 16s have been double-vaccinated and 88% have had at least one dose. Despite this, almost 800 people a day are still being hospitalised and roughly 70 deaths a day are being reported. The population of England is roughly 11 times that of New Zealand. Therefore, were we to follow the same path, it would imply around 70 hospitilisations a day and 6 daily deaths. To put the potential death toll in context, It's probably worth noting that last year 32,613 people died in New Zealand. That's 89 a day. A further 6 would represent a 6.7% increase.

Clearly there is a wide margin of error around likely outcomes but, whatever the case, folk need to get their heads around a very different health environment than that which we have become accustomed to. And if you don't like the comparison with England, have a look at Israel where 80% of adults are double-dosed but case numbers are now at record highs. There are 80 hospitilisations a day there and around 20 daily deaths. Israel's population is about double New Zealand's.

Over time we will, sadly, simply have to get used to the risks associated with COVID becoming endemic, not forgetting, of course, that there will be regular mutations of the virus that will create greater angst, and there will be a proportion of the population that suffers, both physically and mentally, from the longer term effects of the virus(es).

So while people will be emerging from the shelter of lockdowns, which will inevitably generate more economic momentum, that momentum may yet prove to be less than we are forecasting. International evidence shows that waves of COVID can severely dent spending, especially in hospitality, on-site retail, tourism and entertainment, as folk remain fearful of getting out and about. Accordingly, activity levels, especially in some sectors, will be adversely impacted for a substantial period of time. The new "normal" will be nothing like the old.

Too optimistic?



International tourism will be afflicted by concerns around being on a plane for extended periods. This means long-haul tourism flows are likely to be affected most. We suspect travel and health insurers will not be keen to cover COVID-related issues for some time, which will further dent the willingness of those to travel unless there are reciprocal health arrangements between countries. Conversely, this may generate more international travel between closer neighbours, which is problematic for New Zealand as we don't have many.

One factor that will need to be addressed internationally, and soon, is the COVID passport. Reports out of the UK, for example, suggest the UK authorities, and venues, are not accepting New Zealanders' proof of vaccination, and so kiwis are having to get vaccinated again in the UK.

One area of growth will be the health system. It will need to gear up for a semi-permanent need for more hospital beds and more facilities for isolating infectious patients. In addition, staffing numbers will probably need to increase at a time when such staff are already in short supply. Moreover, it looks very much like we will be needing booster vaccines on a regular basis, and there will be an ongoing roll out of modified vaccines as the virus mutates. This will require semi-permanent infrastructure of some description and will come at significant long-term cost to government especially if it continues to provide vaccines free of charge.

Perhaps the key observation we could make is that even in a post vaccination world the landscape will have changed sufficiently to ensure potential output is lowered. Not only does this mean economic activity will be lower than previous expectations but it also means inflation will develop at lower levels of activity potentially necessitating higher interest rates than would otherwise have been the case. That said, the upside interest rate impact may be short-lived as a more permanent drop in potential output would also result in a drop in the neutral real interest rate. The extent of any interest rate response would then become a tug of war between higher inflation and lower real output.

The obvious adverse impact on potential output, that we are already experiencing, is the restriction of labour supply. The world over will be affected by higher numbers of sick days not only from the direct impact of the virus but also requirements to isolate, if infected, whether or not you feel ill. Isolation of close contacts, if this continues, will further exacerbate the problem. This is particularly problematic for smaller businesses who cannot redistribute work amongst existing staff. A classic example of this is the restaurant trade. What can you do when someone infects your whole kitchen staff? And to cap things off, we wonder how many, particularly older people, will simply to choose to exit the labour force as going to work is simply seen as being fraught with too much risk.

From a New Zealand perspective, there is hope that opening the borders will alleviate some of our physical supply shortages. We are not so sure that this will be the case. There appears to be a significant shortage in skilled professionals in numerous countries including, amongst others, USA, Canada, UK, China, Hong Kong, Singapore and Australia. Competition for these skills will be aggressive and businesses may have to pay up large not only to attract people to New Zealand but also to maintain their existing staff.

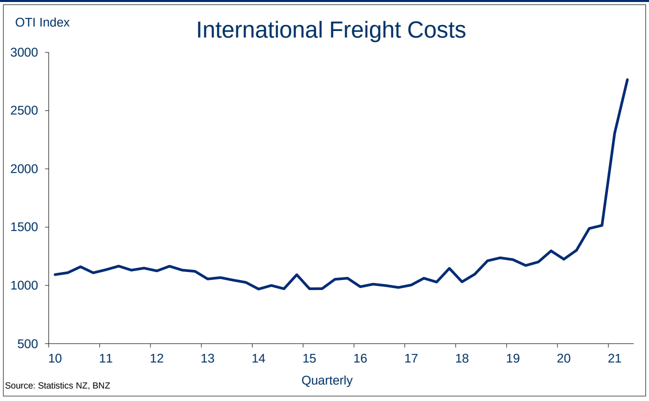
The fact that people now can work from home in many cases does provide workplaces with an element of protection from staff who are required to isolate but not all businesses can find solace in this. Clearly manufacturers, builders and those in the agriculture sector won't have many staff who can work from home. And, more generally, we believe that if too many folk stay away from the office too often it will ultimately damage collaboration, idea exchange, innovation and staff development all of which will be adverse for future productivity.

The work from home phenomenon will also adversely impact the owners of commercial and retail buildings though there may be some offset if staff require more space, businesses maintain spare capacity and office space is converted to residential.

Where opening the borders may offer immediate relief to businesses is via the supply of seasonal workers from the Pacific Islands. Clearly, however, the accessibility of these workers will be dependent on the COVID status of their home countries. Fiji, in particular, continues to have a long road ahead.

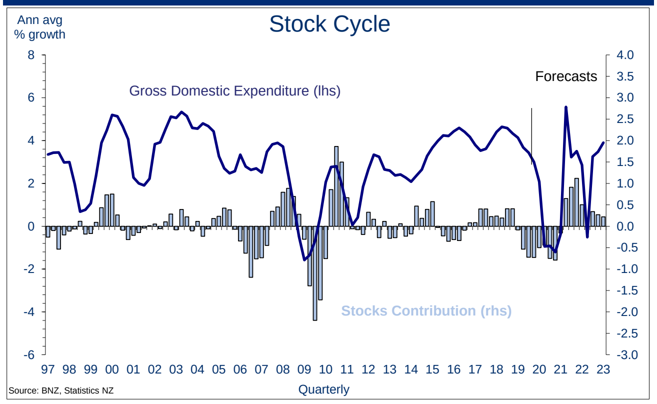
The other key problem that is likely to remain with businesses for some time is supply chain disruption. In particular, freight issues are not going away any time soon. To start with, air freight capacity is highly correlated with passenger travel. While passenger travel will improve it won't get back to pre-COVID levels for the foreseeable future. On the shipping front, New Zealand will remain oppressed by the tyranny of distance. As we are the last stop on the route any delays on the bigger circuit that ships ending up in New Zealand travel will continue to afflict us. This problem is, in the first instance, only likely to get worse as global activity continues to expand faster than the supply of ships. While freight costs may start to fall next year, they will no doubt remain elevated for an extended period of time.

A long way from normal



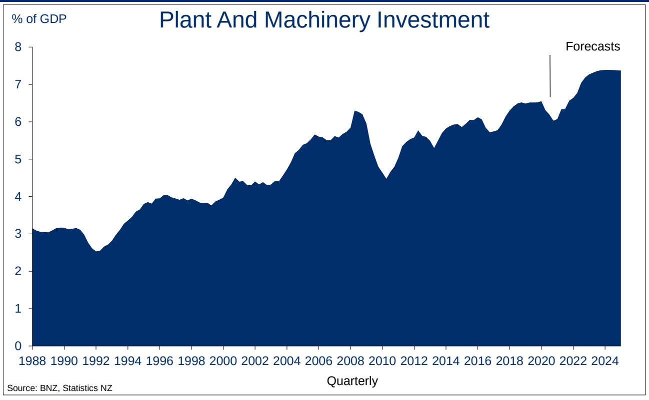
Supply chain disruptions globally are resulting in changes to business models. New Zealand will be no different in this regard. For years now businesses have been, rightfully, patting themselves on the back about their improved inventory management. Just-in-time inventory has been all the rage. However, the success of implementing such policy has now become the achilles heel of many. In response, fearing supply delays, businesses are being forced to build much higher inventory levels than had become the norm. This raises the cost of business via holding costs and wastage. Such costs will eventually find their way to the shop floor. It's good news, however, for the owners and operators of distribution centres.

Stock build likely



Of course, while there are a significant number of businesses who will face headwinds, there is one wide-ranging sector that stands to benefit from the new world – namely e-commerce. Business that doesn't depend on face to face contact and/or is heavily automated is flourishing in the current environment. It will continue to do so. Aligned with this, investment in plant, machinery and technology is set to boom. The rising cost of employing people, coupled with the risk that they won't show up to work, will strongly encourage significant fixed capital expansion. Low interest rates will also help. The only thing that will really get in the way of this will be the very things that businesses are trying to overcome, namely, supply bottlenecks and a lack of skilled labour to install the plant, equipment and technology that is so desired.

Capital\labour substitution likely



With overall levels of demand expected to grow, and supply constraints becoming ever more binding, there is every likelihood that inflationary pressures will remain with us for some time. Managing these cost pressures (and you can add to these environmental and general compliance costs) will be a key to business success over the next few years.

The other cost increase that businesses will have to manage is the cost of debt as the very same inflationary pressures cause the central bank to react. There may be a large dispersion of views as to where interest rates finally settle but there is little doubt that the average cost of debt over the next few years will be higher than it was over the last twelve months.

We remain optimistic about New Zealand's prognosis for the next few years. However, we strongly caution that businesses (and households for that matter) need to start planning now for a very different world than the world we left behind in early 2020.

We are far more focused on those medium term issues than trying to read the tealeaves of the current state of affairs but current and recent past data will still provide us detail as to the state of the economy going into this shock and provide some inkling of what we might expect in the time between now and vaccination rates reaching perceived acceptable levels of protection.

Perhaps the most immediate point of interest for New Zealanders will be this afternoon's reveal from the Prime Minister of the cabinet's view on where New Zealand restriction levels should head to next. There are very good arguments for all of New Zealand, except Auckland, heading back to Level 2, which is very close to full freedom, as there have been no community cases outside of Auckland over the last week. Moreover, there have been none in the South Island for months. But New Zealand has never had a two level variation across regions before. For the government to implement it, it would have to be confident it could still keep Auckland isolated, especially given that the temptation to breach the rules would be so much greater if the guys down the road are going about their normal everyday business while you are fully locked down. An option to mitigate this concern would be to leave the North Island, ex-Auckland, at level 3 but drop the South Island to level 2. Whatever the case we will find out this afternoon.

This morning we received the latest Building Work Put in Place figures. The total increase in activity was 2.0%. Non-residential activity slipped 1.5% but this was more than offset by the 4.2% increase in residential activity. Overall activity was broadly in line with our expectations in terms of its likely impact on Q2 GDP.

On Thursday we'll get more insight into the second quarter's activity with a peak into the latest business employment and financial data. These data will include the familiar manufacturing sales and wholesale trade figures as well as selected services numbers. All these will help finalise our Q2 GDP expectation, which currently sits at 0.9%. As a point of comparison, the RBNZ was working on a 0.6% pick for the quarter. Q2 GDP could yet provide more evidence that the economy was operating further above potential than the RBNZ had realised.

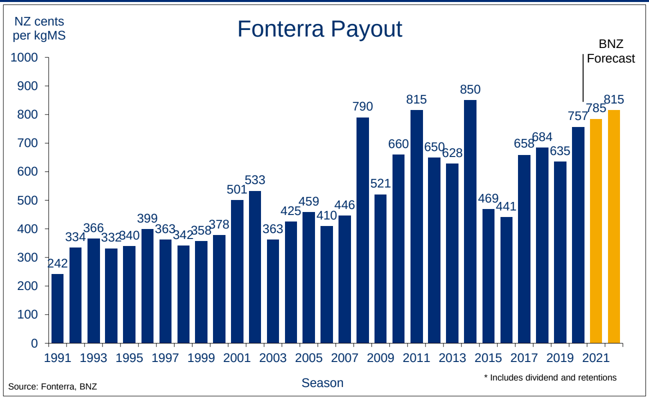
On Friday, electronic cards transactions for August and migration and travel figures for July are released.

The ECT data will be interesting as they will reflect the initial fallout from the lockdown. Our data indicate the impact on spending is not as great as was the case in 2020 but it's still significant. We believe sales across August will be around 20% down on the previous month. The good news is that sales should not fall any further in September as the country hopefully continues its move up through the alert levels. This should also mean sales should bounce meaningfully in the fourth quarter.

The migration and travel data will be of only limited interest in providing yet more confirmation that there are very few people crossing our borders, in either direction, for travel or migration purposes.

To round out the week, ANZ commodity export prices are due this afternoon and the latest GDT auction is on Wednesday morning. The ANZ series is expected to reveal a small price decline, in both world and NZD terms, led by forestry prices. In contrast, we expect to see an increase in the GDT price which, at the margin, suggests some upside risk to our forecast $7.80 milk price pick for the 2021/22 season.

Dairy revenues solid



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Global Watch

- **RBA to stick with tapering plan at Tuesday's meeting**
- **China exports/imports and CPI data for Aug. due**
- **US data quiet but Beige Book and Fed-speak to note**

Australia

The RBA on Tuesday is the main event in an otherwise quiet week in Australia. NAB expects the RBA to continue with the scheduled taper to the pace bond purchases to $4bn per week from the current pace of $5bn per week, though the optics of tapering amid protracted lockdowns, means it is likely to be a close decision.

Governor Lowe will have an opportunity to expand on the RBA's thinking the week after, Speaking at the ANIKA foundation on 14 September. Deputy Governor Debelle speaks this Wednesday and Thursday. Given the forums are FX and compliance conferences, don't expect much of interest for the Australian market.

Weekly payroll jobs for the fortnight to 14 August on Thursday are the only data after the flurry of releases from the ABS this past week. Official employment numbers the week after (16 September) will be more closely watched for lockdown impacts.

RBA September Meeting

The RBA September Meeting on Tuesday is the key focus, in a week with little in the way of new data. At its August meeting, the RBA surprised markets by sticking to its previously announced taper at the end of QE2, reasoning that the rebound alongside easing of restrictions would be sharp, and a slow pace of purchases was still adding significant support to the economy.

The current $100bn tranche of purchases is set to conclude next week, with the previously announced $4bn weekly pace of purchases to replace the current $5bn weekly pace. In announcing that the Bank would move to a $4bn weekly pace at its August meeting, the Bank also said that "*the program will continue to be reviewed in light of economic conditions and the health situation.*"

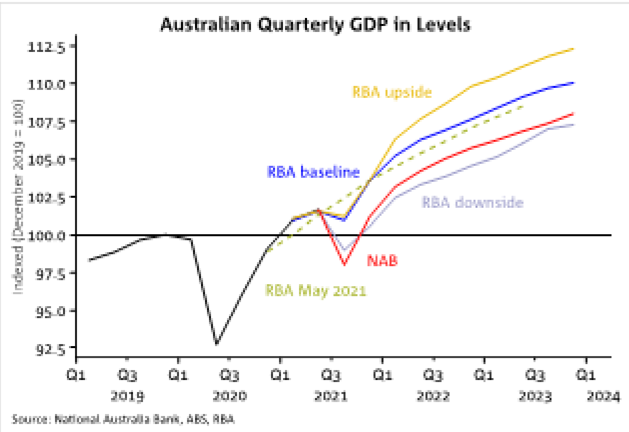
That reasoning was clarified further in the August Minutes, with the RBA noting that "*…the outlook for the economy is for a resumption of strong growth in 2022 [and] that any additional bond purchases would have their maximum effect at that time, with only a marginal effect at present, which is when the extra support might be required*"

The health situation has indeed deteriorated since their meeting on 3 August. Victoria re-joined NSW in lockdown from 5 August, and the two largest states, together representing over half of the national economy, are now in protracted lockdowns. That points to the risk that the RBA could reverse its announced taper on Tuesday. But the vaccine rollout is continuing and phased reopening alongside increased vaccination coverage is set to support the recovery. Nationally, vaccine targets of 70% and 80% are achievable by mid-November, with NSW outpacing the national rollout (for more detail, see our latest [vaccine weekly]). Prime Minister Morrison last Friday announced a vaccine swap agreement with the UK for 4m Pfizer doses that has the potential to significantly ease supply constraints on the rollout in the near term. Accordingly NAB still expects a strong rebound in activity in 2022, with the RBA, looking beyond the near-term impact from lock-downs, still likely able to forecast progress towards its goals of full employment and inflation sustainably within the band, to be consistent with its central scenario of hikes in 2024.

Consequently, NAB expects that the RBA will continue as scheduled with its scheduled taper to $4bn per week in early September from its current pace of $5bn per week. We pencil in the next QE taper in February 2022, by which time the strong rebound in the economy will be evident. We expect the total QE program from September to total around $130bn with tapering to occur progressively before ending in mid to late 2022. The optics of tapering amid protracted lockdowns, though, means it is likely to be a close decision.

On the outlook for rate hikes, NAB continues to expect the first rate hike to occur in early 2024. We see the first move as lifting the cash rate target by 40bps to 0.5%; this is to allow normalisation of the ES rate corridor and would see the actual cash rate trade closer to 25bps (i.e. it would effectively be a 35bp rate hike). Following this, we see increases of around 25bps per quarter – a fairly rapid normalisation as the RBA becomes forward looking. By mid-to-late 2025, we expect the cash rate to trade around 1.75-2.00% depending on the degree of spare capacity in the labour market.

Downside risk to RBA's August SoMP forecast



The deterioration in the health situation since the RBA's August SoMP forecasts were finalised, and the consequent more widespread and protracted lockdowns, suggests downside risks to their outlook in the near term. Hints as to the RBA's assessment of whether the outlook for a rapid recovery alongside easing of restrictions remains intact will be closely watched. There is unlikely to be expansive discussion in the post meeting statement, but Governor Lowe will have an opportunity to expand on these issues on 14 September, when he speaks at the ANIKA Foundation.

Weekly Payroll Jobs

Following a big week for domestic data releases last week, it is very quiet from the ABS in the week ahead. The only data release of note is the Weekly Payroll Jobs for the fortnight to 14 August on Thursday, which will continue to be buffeted by lockdowns. The previous release to 31 July showed NSW payroll jobs 7.1% below pre-lockdown levels, and weakness is likely in Victoria with the state re-joining NSW in lockdown from 5 August.

More closely watched for lockdown impacts in the labour market, though, will be the August employment release the following week on Thursday 16 September.

China

The trade balance for August kicks of the week data-wise on Tuesday, with expectations for a small decline in the trade surplus from US$56.6bn to US$51.0bn. Inflation prints are on Thursday with the annual rate for CPI expected stable at 1.0% and for PPI still at 9.0%. Money supply and aggregate financing numbers are due anytime in the week from Thursday.

US

A quieter week ahead in the US, after last Friday's mixed labour market reports for August. Producer prices on Thursday are expected to show still strong growth in input prices, even as the monthly rate is expected to slow to 0.6% from 1.0% in June. The Fed's Beige Book is out Wednesday, with a cast of Fed speakers due from Wednesday kicking off with NY Fed President Williams on the economic outlook. Other notable speakers are Kaplan, Daly and Mester. Ongoing reaction to last Friday's payroll print, in the context of tapering implications, will continue to be watched.

Eurozone

The ECB meets on Wednesday, with expectations tilted towards a cut to the pace of purchases in its emergency purchase program from the current €80bn monthly pace to €70bn per month next quarter. Maintaining the current pace remains a distinct possibility. On the data side, the final estimate for EZ Q2 GDP is seen in line with the upside surprise of 2.0%q/q from the first estimate. German industrial production and trade numbers for July, as well the ZEW survey are also out during the week.

UK

A quiet week with nothing from the BoE. Monthly GDP numbers for July, alongside other monthly indicators including industrial production and trade balance data are all out on Friday

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Fixed Interest Market

Reuters: BNZL, BNZM Bloomberg:BNZ

NZ rates continue to rebound, with falling NZ Covid-19 case numbers giving the market confidence the RBNZ will start its rate hike cycle next month. The 5-year swap rate has reached its highest level since mid-2019, at 1.78%, while the 10-year rate is up to its highest level since February, above 2%.

Market pricing for the October continues to edge up, to be around 0.49% now, implying an almost certain chance of a 25bp OCR hike at the RBNZ's meeting next month. There are 70bps of OCR hikes priced for the next three meetings. Market pricing reflects the strong starting point for the economy (both core inflation and employment were above the RBNZ's mandated targets before the latest lockdown), recent hawkish messages from senior RBNZ officials, and the drift lower in Covid-19 case numbers, giving the market greater confidence that New Zealand will have moved down the alert levels by the time of the meeting. Ongoing hedging of fixed rate mortgages in the swap market is also adding consistent upward pressure to short-end rates.

Assuming Covid case numbers continue to trend down, the market will likely price a chance of a 50bps OCR rate increase to start the tightening cycle next month, as it did before the August meeting (a ~20% chance of a 50bp move was priced-in right on the day before lockdown). The logic for a 50bps move would be, firstly, that the RBNZ judges the OCR to be a long way below 'neutral', seen as around 2%, and, secondly, a 50bps hike would allow it to 'catch up' for the fact that it left the OCR on hold in August, in what was a finely balanced call. In this scribe's view, a 50bps OCR hike is both unnecessary and unlikely. There is significant uncertainty around exactly where the 'neutral' rate lies, there would be unpredictable impacts on confidence (including on the housing market), and the RBNZ can achieve significant tightening by communicating a hawkish message and moving in 25bp increments. Simply tightening 25bps at every meeting to the end of next year would take the OCR to 2.5%, well above what is priced for any other developed market central bank over the next 10 years.

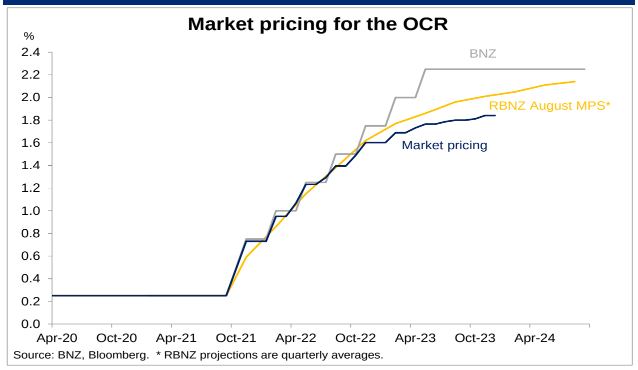
Medium-term OCR expectations also continue to push higher. Market pricing for end-2022 and end-2023 are around 1.60% and 1.80% respectively, with the gap to the RBNZ's MPS projections having materially shrunk over the past fortnight. We now think the risks at the short end of the curve, relative to what is priced into forward swaps, are now more balanced.

The US 10-year rate is trading towards the upper-end of its broad 1.15% to 1.35% range that has prevailed over the past two months. Friday's lower-than-expected jobs number in the nonfarm payrolls release means the Fed is highly unlikely to announce at tapering of its bond buying at its meeting this month, with a November, or even December, announcement more likely. The Fed's emphasis on restoring the shortfall of people employed back to pre-Covid levels would seem to be creating greater medium-term inflation risks, but for now the market seems sanguine. We think the US 10-year rate is likely to track higher over the coming year, dragging up the long-end of the NZ curve as well.

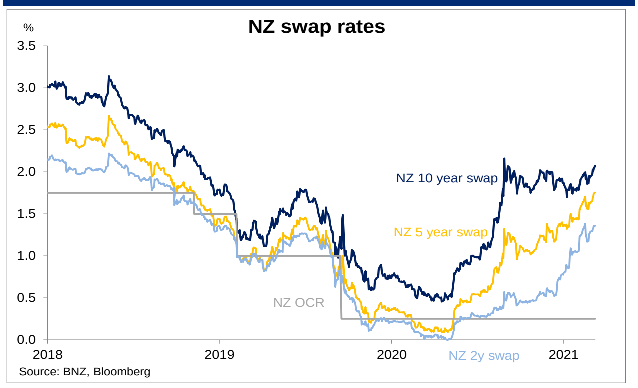
The German 10-year rate has been edging higher over the past month, albeit to a still ultra-low -0.36%, as market expectations build that the ECB will announce a reduction to its pace of bond purchases at this week's meeting. The consensus is that the ECB will slightly reduce its monthly QE purchase pace next quarter, from €80b per month to a still hefty €60-70b pace. Unlike in the US, where the Fed is expected to taper all the way to zero once it gets going, the ECB 'tapering' is more a recalibration after it temporarily boosted purchases in Q2 in response to a rise in bond yields at the time. Its pandemic bond buying programme is due to end in March, but the ECB will still be buying bonds under its Asset Purchase Programme.

In Australia, our NAB colleagues expect the RBA to stick to its tapering plan, reducing purchases from $5b per week to $4b, although they acknowledge the optics for the RBA are challenging amidst the lockdowns in Victoria and NSW, so it's a close call. The RBA's ongoing bond buying and the expected divergence in the RBNZ and RBA cash rates has seen the 10-year NZ-AU bond spread hit a 5½ year high of 70bps. This spread has historically reached as high as 100bps, suggesting it might be able to widen a bit further, but at these levels we see greater scope for positive surprise on the Australian side, including for the RBA.

Market pricing converging on the RBNZ's projections



10-year rates remain rangebound



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Foreign Exchange Market

Reuters pg BNZWFWDS Bloomberg pg BNZ9

For the second week in a row, both the NZD and AUD strongly outperformed, recovering from cheap levels against the backdrop of higher risk appetite. Both were up around 2% to 0.7150 and 0.7460 respectively. After touching a 19-month high around 0.9660 earlier in the week, NZD/AUD hovered flat around the 0.96 mark. The NZD was up 1.3-1.9% against the other key crosses, with NZD/EUR reclaiming the 0.60 handle. NZD/JPY has strengthened over 5% through the past fortnight to reach 78.5.

What a difference a fortnight makes. It was only a couple of weeks ago that NZD was plumbing a year-to-date low of just over 0.68 and since then it has been one-way traffic, breaking up through resistance of 0.71, putting the previous resistance level of 0.7315 back into the frame. A couple of weeks ago we noted how cheap the NZD had become, relative to our short-term fair value model, suggesting some overshooting to the downside. At last week's close our fair value estimate was 0.7260, taking the value gap to within a statistically insignificant 1½%.

We'd point to two key factors driving the positive turnaround in sentiment. Firstly, there is less concern about the global spread of the delta variant of COVID19. Investors have become more willing to accept that it will cause a hiccup in the global economic recovery, without throwing it completely off course. China's success in containing the virus, less growth in the spread of the virus across the US, and easier than otherwise policy settings going forward by both the PBoC and US Fed have supported improved sentiment. Our risk appetite index is back up to the 70% mark, recovering losses over the past couple of months.

Fed Chair Powell's Jackson Hole speech just over a week ago and much softer than expected US payrolls data last week support the view that US rate hikes remain a distant prospect. Furthermore, there is no longer much chance of the Fed announcing a tapering of its asset purchases this month, and there is a growing chance that tapering might be pushed out into early next year. The pushing out of expectations of when the Fed might start to reduce policy stimulus has been supportive of higher risk appetite and detrimental to the USD.

The Fed's mid-June meeting, which was more hawkish than expected with committee members bringing forward their rate hike expectations into 2023, was a key trigger for the NZD's demise from that date. It was trading around 0.7150 at that time and has made a round trip back up to that mark, via 0.68.

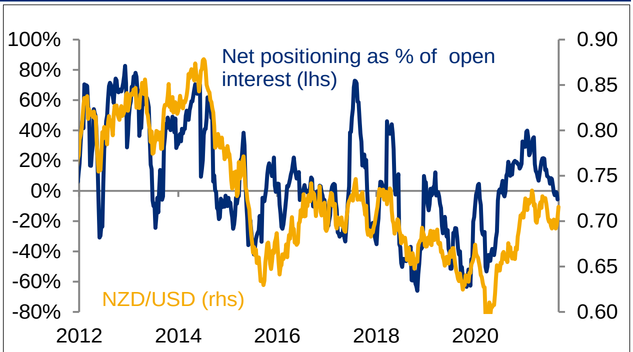
Prior to that June meeting, the 0.71 mark was the level of technical support and looking ahead that might well prove to be the case again. We therefore suggest that a new higher trading range of 0.71-0.7315 could come into play over the short term.

In the week ahead, the RBA and ECB meetings will be in focus. We expect the RBA to continue with its scheduled tapering of bond purchases from $5b to $4b a per week, but it's hard to see this update having any sustained impact on the AUD. The RBA will note the current negative impact on the economy of the lockdown restrictions but will still likely be looking for a strong rebound as restrictions are loosened. For our views on the cross, see our NZD/AUD note published earlier today.

The ECB is expected to announce a cut to its pace of QE under the emergency pandemic programme from next quarter. Again, we wouldn't expect this to rattle the currency market. Our view on NZD/EUR remains one of further modest upside pressure this year, as the RBNZ kicks off its tightening cycle.

The US data calendar looks light, but a number of Fed speakers are scheduled to enlighten us. Domestically, only second tier data are released. We'll get an update from the government later today on restriction levels. The trend down in new case numbers looks promising, but we don't see the local lockdown as a major driver of the NZD.

Speculative positioning no barrier to further NZD upside



Source: BNZ, Bloomberg

Cross Rates and Model Estimates

	Current	Last 3-weeks range*
NZD/USD	0.7158	0.6810 - 0.7170
NZD/AUD	0.9599	0.9490 - 0.9660
NZD/GBP	0.5163	0.4980 - 0.5170
NZD/EUR	0.6025	0.5820 - 0.6030
NZD/JPY	78.56	74.60 - 78.70

*Indicative range over last 3 weeks, rounded figures

BNZ Short-term Fair Value Models

	Model Est.	Actual/FV
NZD/USD	0.7260	-1%
NZD/AUD	0.9140	5%

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Technicals

NZD/USD

Outlook: Trading range
ST Resistance: 0.7315 (ahead of 0.7460)
ST Support: 0.7100 (ahead of 0.6900)

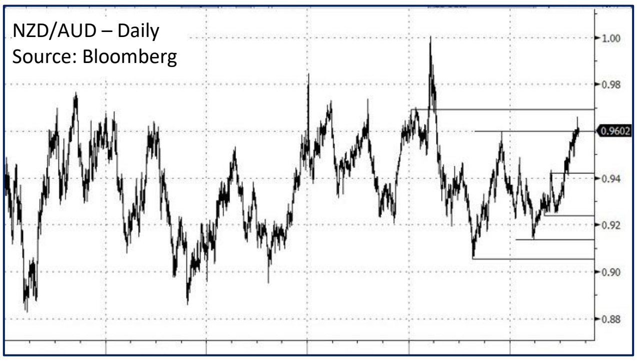
Another sharp increase last week puts the NZD back into the familiar 0.7100-0.7315 range seen earlier this year, a range which defines the new support/resistance levels.

NZD/USD – Daily
Source: Bloomberg

NZD/AUD

Outlook: Trading range
ST Resistance: 0.9600 (ahead of 0.9700)
ST Support: 0.9430 (ahead of 0.9300)

While 0.96 has been broken to the upside several times, we'll leave it as a resistance level until the break is more convincing, ahead of 0.97.



NZD/AUD – Daily
Source: Bloomberg

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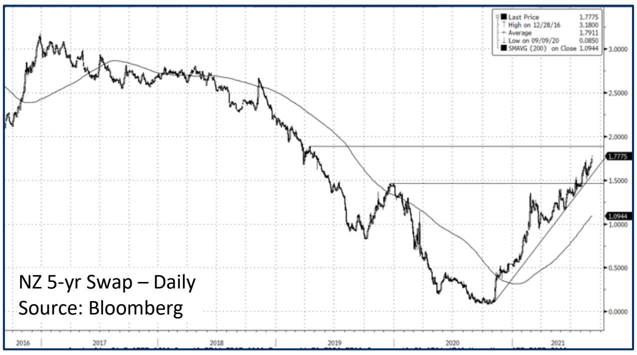
NZ 5-year Swap Rate

Outlook: Higher
MT resistance: 1.89
MT support: 1.46

No change here, if you want a tight stop trendline support comes in at 1.59 now

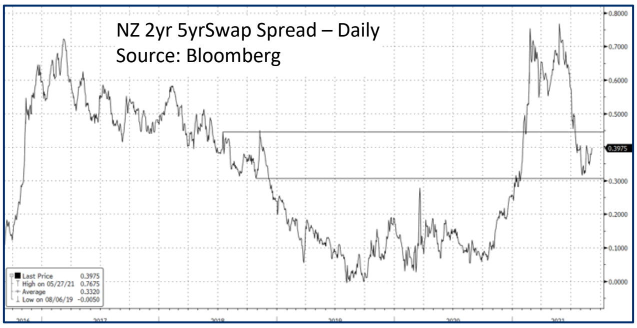


NZ 5-yr Swap – Daily
Source: Bloomberg

NZ 2-year - 5-year Swap Spread (yield curve)

Outlook: Steeper
MT resistance: 0.45
MT support: 0.31

Still looking for 0.31 to hold take profit around 0.45.



NZ 2yr 5yrSwap Spread – Daily
Source: Bloomberg

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Quarterly Forecasts

Key Economic Forecasts

Quarterly % change unless otherwise specified

Forecasts

	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22
GDP (production s.a.)	-1.5	-10.8	14.1	-1.0	1.6	0.9	-7.0	8.0	0.5	1.0
Retail trade (real s.a.)	-1.0	-15.5	27.8	-2.2	2.8	3.3	-12.0	13.0	1.5	0.8
Current account (ytd, % GDP)	-2.8	-1.8	-0.8	-0.8	-2.2	-3.3	-3.5	-4.0	-4.3	-5.0
CPI (q/q)	0.8	-0.5	0.7	0.5	0.8	1.3	1.5	0.6	0.6	0.4
Employment	1.0	-0.4	-0.6	0.7	0.6	1.1	-0.2	0.2	0.7	0.6
Unemployment rate %	4.2	4.1	5.3	4.8	4.6	4.0	4.0	4.3	3.9	3.7
Avg hourly earnings (ann %)	3.2	2.4	3.7	4.6	4.1	4.5	2.8	3.7	4.0	4.3
Trading partner GDP (ann %)	-2.4	-5.3	-0.9	0.7	6.3	9.8	4.5	4.1	4.5	4.6
CPI (y/y)	2.5	1.5	1.4	1.4	1.5	3.3	4.2	4.3	4.1	3.2
GDP (production s.a., y/y))	0.0	-11.2	0.4	-0.8	2.4	15.8	-5.6	3.0	1.9	2.0

Interest Rates

Historical data - qtr average Forecast data - end quarter	Cash	Government Stock 90 Day Bank Bills	5 Year	10 Year	Swaps 2 Year	5 Year	10 Year	US Rates Libor 3 month	US 10 yr	Spread NZ-US Ten year
2019 Dec	1.00	1.15	1.05	1.40	1.10	1.20	1.50	1.95	1.80	-0.40
2020 Mar	0.75	1.05	1.00	1.35	1.00	1.10	1.40	1.55	1.40	-0.03
Jun	0.25	0.30	0.40	0.85	0.25	0.40	0.80	0.60	0.70	0.15
Sep	0.25	0.30	0.25	0.65	0.15	0.25	0.60	0.25	0.65	0.02
Dec	0.25	0.25	0.25	0.70	0.15	0.30	0.75	0.20	0.85	-0.15
2021 Mar	0.25	0.30	0.75	1.40	0.40	0.85	1.50	0.20	1.30	0.09
Jun	0.25	0.35	1.00	1.75	0.55	1.20	1.90	0.15	1.60	0.17
Forecasts										
Sep	0.25	0.60	1.60	1.90	1.45	1.80	2.10	0.15	1.50	0.40
Dec	0.75	0.95	2.05	2.35	1.80	2.15	2.45	0.15	1.80	0.55
2022 Mar	1.00	1.20	2.40	2.60	2.05	2.50	2.70	0.15	2.00	0.60
Jun	1.25	1.45	2.60	2.85	2.30	2.70	2.95	0.15	2.20	0.65
Sep	1.50	1.75	2.80	3.05	2.50	2.90	3.15	0.15	2.35	0.70
Dec	1.75	2.00	2.95	3.20	2.65	3.05	3.30	0.15	2.50	0.70
2023 Mar	2.00	2.25	3.00	3.25	2.65	3.10	3.35	0.15	2.65	0.60

Exchange Rates (End Period)

USD Forecasts

	NZD/USD	AUD/USD	EUR/USD	GBP/USD	USD/JPY
Current	0.72	0.74	1.19	1.39	110
Sep-21	0.72	0.76	1.21	1.41	109
Dec-21	0.75	0.78	1.23	1.43	109
Mar-22	0.76	0.80	1.24	1.46	109
Jun-22	0.75	0.80	1.26	1.48	109
Sep-22	0.75	0.80	1.28	1.52	109
Dec-22	0.74	0.80	1.30	1.54	109
Mar-23	0.73	0.79	1.28	1.52	108
Jun-23	0.72	0.77	1.26	1.50	108
Sep-23	0.71	0.76	1.25	1.47	107
Dec-23	0.69	0.75	1.24	1.47	107

NZD Forecasts

	NZD/USD	NZD/AUD	NZD/EUR	NZD/GBP	NZD/JPY	TWI-17
Current	0.72	0.96	0.60	0.52	78.5	75.5
Sep-21	0.72	0.96	0.60	0.51	78.8	75.2
Dec-21	0.75	0.95	0.61	0.52	81.5	76.6
Mar-22	0.76	0.95	0.61	0.52	82.8	77.3
Jun-22	0.75	0.94	0.60	0.51	82.0	76.4
Sep-22	0.75	0.94	0.59	0.50	82.0	76.3
Dec-22	0.74	0.93	0.57	0.48	80.7	75.1
Mar-23	0.73	0.92	0.57	0.48	78.8	74.5
Jun-23	0.72	0.93	0.57	0.48	77.5	74.0
Sep-23	0.71	0.93	0.57	0.48	76.0	73.6
Dec-23	0.69	0.92	0.56	0.47	73.8	71.8
TWI Weights	13.3%	19.2%	10.5%	4.1%	6.4%	

Source for all tables: Statistics NZ, Bloomberg, Reuters, RBNZ, BNZ

Annual Forecasts

Forecasts as at 6 September 2021	March Years					December Years				
	Actuals		Forecasts			Actuals		Forecasts		
	2020	2021	2022	2023	2024	2019	2020	2021	2022	2023
GDP - annual average % change										
Private Consumption	2.9	-0.7	6.4	5.2	1.9	3.6	-1.9	7.7	4.8	2.3
Government Consumption	6.1	6.3	5.1	1.8	1.3	5.4	6.4	5.8	2.3	1.2
Total Investment	1.3	-4.7	8.2	7.4	-0.7	3.2	-7.4	9.3	8.1	-0.3
Stocks - ppts cont'n to growth	-0.5	-0.2	0.5	0.2	-0.1	-0.7	-0.8	1.1	0.3	-0.2
GNE	2.5	-0.5	6.9	5.3	1.1	3.0	-2.5	8.6	5.4	1.3
Exports	-0.3	-15.9	2.0	12.5	8.9	2.3	-11.8	-5.4	9.1	12.6
Imports	1.2	-16.2	13.7	15.2	5.4	2.2	-16.4	10.7	14.7	7.3
Real Expenditure GDP	2.1	-0.4	2.9	3.9	1.6	3.0	-1.2	3.5	3.5	2.0
GDP (production)	**1.7**	**-2.3**	**3.4**	**4.5**	**1.6**	**2.4**	**-2.9**	**3.5**	**4.2**	**1.9**
GDP - annual % change (q/q)	*0.0*	*2.4*	*1.9*	*2.9*	*1.6*	*1.8*	*-0.8*	*3.0*	*3.0*	*1.4*
Output Gap (ann avg, % dev)	1.9	-1.6	-0.3	1.5	0.6	2.3	-1.7	-0.3	1.4	0.8
Nominal Expenditure GDP - $bn	322	325	347	366	380	319	322	342	363	376
Prices and Employment - annual % change										
CPI	2.5	1.5	4.1	2.3	2.7	1.9	1.4	4.3	2.2	2.6
Employment	2.5	0.3	1.8	1.8	1.1	1.2	0.7	1.6	2.2	1.0
Unemployment Rate %	4.2	4.6	3.9	3.9	4.6	4.0	4.8	4.3	3.6	4.5
Wages - ahote	3.2	4.1	4.0	4.0	2.8	3.8	2.6	4.6	3.7	4.1
Productivity (ann av %)	-0.3	-2.8	1.7	2.6	0.5	0.5	-4.1	2.3	2.3	0.6
Unit Labour Costs (ann av %)	3.4	5.5	4.7	1.6	2.8	2.5	6.6	3.6	2.2	2.9
House Prices	7.8	22.0	8.5	2.3	2.0	4.6	17.0	15.7	2.8	2.0
External Balance										
Current Account - $bn	-9.1	-7.2	-14.9	-20.1	-15.7	-10.6	-2.4	-13.8	-22.5	-16.7
Current Account - % of GDP	-2.8	-2.2	-4.3	-5.5	-4.1	-3.3	-0.8	-4.0	-6.2	-4.4
Government Accounts - June Yr, % of GDP										
OBEGAL (core operating balance)	-7.3	-2.8	-5.0	-1.5	0.0					
Net Core Crown Debt (excl NZS Fund Assets)	26.3	32.0	42.0	45.0	42.0					
Bond Programme - $bn (Treasury forecasts)	29.0	45.0	30.0	25.0	25.0					
Bond Programme - % of GDP	9.0	13.8	8.6	6.8	6.6					
Financial Variables [(1)]										
NZD/USD	0.60	0.71	0.76	0.73	0.69	0.66	0.71	0.75	0.74	0.69
USD/JPY	108	109	109	108	107	109	104	109	109	107
EUR/USD	1.11	1.19	1.24	1.28	1.24	1.11	1.22	1.23	1.30	1.24
NZD/AUD	0.97	0.93	0.95	0.92	0.92	0.96	0.94	0.95	0.93	0.92
NZD/GBP	0.49	0.51	0.52	0.48	0.47	0.50	0.53	0.52	0.48	0.47
NZD/EUR	0.55	0.60	0.61	0.57	0.56	0.59	0.58	0.61	0.57	0.56
NZD/YEN	65.1	77.5	82.8	78.8	73.8	72.0	73.6	81.5	80.7	73.8
TWI	68.9	74.8	77.3	74.5	71.8	72.8	74.3	76.6	75.1	71.8
Overnight Cash Rate (end qtr)	0.25	0.25	1.00	2.00	2.25	1.00	0.25	0.75	1.75	2.25
90-day Bank Bill Rate	0.71	0.33	1.20	2.25	2.40	1.23	0.26	0.95	2.00	2.40
5-year Govt Bond	0.80	1.00	2.40	3.00	3.00	1.25	0.40	2.05	2.95	3.00
10-year Govt Bond	1.15	1.75	2.60	3.25	3.30	1.60	0.90	2.35	3.20	3.30
2-year Swap	0.65	0.50	2.05	2.65	2.65	1.25	0.28	1.80	2.65	2.65
5-year Swap	0.80	1.15	2.50	3.05	3.10	1.40	0.49	2.15	3.05	3.10
US 10-year Bonds	0.90	1.60	2.00	2.65	3.00	1.85	0.90	1.80	2.50	3.00
NZ-US 10-year Spread	0.25	0.15	0.60	0.60	0.30	-0.25	0.00	0.55	0.70	0.30

[(1)] *Average for the last month in the quarter*

Source for all tables: Statistics NZ, EcoWin, Bloomberg, Reuters, RBNZ, NZ Treasury, BNZ

Key Upcoming Events

	Forecast	Median	Last
Monday 6 September			
NZ, Building Work Put In Place, Q2 vol s.a.			+3.7%
NZ, Govt Reviews COVID restriction levels			
NZ, ANZ Commodity Prices (world), August			-1.4%
Aus, ANZ Job Ads, August			-0.5%
Aus, Inflation Gauge (Melbourne Institute), Aug y/y			+2.6%
Germ, Factory Orders, July		-0.7%	+4.1%
UK, BRC Retail Sales Monitor, Aug y/y		+3.2%	+4.7%
US, Holiday, Labor Day			
Tuesday 7 September			
Aus, RBA Policy Announcement	0.10%	0.10%	0.10%
China, Trade Balance, August		+¥323b	+¥363b
Jpn, Household Spending, Jul y/y (real)		+2.7%	-5.1%
Euro, GDP, Q2 3rd est		+2.0%	+2.0%P
Germ, ZEW Sentiment, September		30.5	40.4
Germ, Industrial Production, July		+0.9%	-1.3%
Wednesday 8 September			
NZ, Dairy Auction, GDT Price Index			+0.3%
Aus, RBA's Debelle Speaks, Online			
Jpn, GDP, Q2 2nd est		+0.4%	+0.3%P
Jpn, Eco Watchers Survey, Aug (Outlook)		46.2	48.4
US, JOLTS Job Openings, July		10,000k	10,073k
US, Beige Book			
Can, BOC Policy Announcement		0.25%	0.25%

	Forecast	Median	Last
Thursday 9 September			
NZ, Filled Jobs (PAYE-based), Q2			+0.2%
NZ, ANZ Truckometer Index, August			-1.1%
NZ, Business Financial Data, Q2			
China, PPI, Aug y/y		+9.0%	+9.0%
China, CPI, Aug y/y		+1.0%	+1.0%
Euro, ECB Policy Announcement, Depo		-0.50%	-0.50%
Germ, Trade Balance, July		+€14.6b	+€16.3b
US, Jobless Claims, week ended 04/09		335k	340k
Friday 10 September			
NZ, International Travel, July			
NZ, International Migration, July s.a.			+897
NZ, Electronic Card Transactions, August			+0.9%
Germ, CPI, Aug y/y 2nd est		+3.9%	+3.9%P
UK, GDP monthly, July		+0.5%	+1.0%
UK, Trade Balance, July		-£1.6b	-£2.5b
UK, Industrial Production, July		+0.4%	-0.7%
US, PPI ex-food/energy, Aug y/y		+6.6%	+6.2%
US, Wholesale Trade Sales, July			+2.0%
Monday 13 September			
NZ, ANZ Business Survey, Sept prelim			-14.2
NZ, Food Price Index, August			+1.3%
Jpn, BSI Business Survey, Q3			-4.7
US, Budget Statement, August			-$302b

Historical Data

	Today	Week Ago	Month Ago	Year Ago
CASH AND BANK BILLS				
Call	0.25	0.25	0.25	0.25
1mth	0.32	0.28	0.48	0.28
2mth	0.40	0.37	0.57	0.29
3mth	0.48	0.46	0.65	0.30
6mth	0.68	0.64	0.82	0.29
GOVERNMENT STOCK				
04/23	0.97	0.91	0.93	0.08
04/25	1.35	1.24	1.19	0.09
04/27	1.54	1.42	1.39	0.27
04/29	1.71	1.60	1.58	0.47
05/31	1.84	1.72	1.68	0.62
04/33	2.05	1.94	1.87	0.80
04/37	2.34	2.23	2.14	1.08
05/41	2.62	2.51	2.40	1.33
GLOBAL CREDIT INDICES (ITRXX)				
Nth America 5Y	47	46	49	67
Europe 5Y	45	45	46	53

	Today	Week Ago	Month Ago	Year Ago
SWAP RATES				
2 years	1.38	1.29	1.27	0.05
3 years	1.58	1.47	1.41	0.06
4 years	1.70	1.57	1.52	0.09
5 years	1.78	1.64	1.61	0.15
10 years	2.07	1.96	1.94	0.57
FOREIGN EXCHANGE				
NZD/USD	0.7158	0.6999	0.6993	0.6692
NZD/AUD	0.9600	0.9593	0.9538	0.9196
NZD/JPY	78.54	76.94	77.12	71.11
NZD/EUR	0.6023	0.5933	0.5958	0.5663
NZD/GBP	0.5162	0.5087	0.5050	0.5083
NZD/CAD	0.8966	0.8823	0.8794	0.8765
TWI	75.6	74.5	74.7	72.3

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