REFERRER NEWS

with Tony Alexander

A number of people remain of the view that in spite of a plethora of data showing our economy recently performing far better than expected, woe still lies ahead. They typically cite these factors.

1. Job losses once the third edition of the wage subsidy scheme ends.

2. Mortgagee sales forcing house prices lower once the extended mortgage deferral scheme ends.

3. Ending of an unsustainable post-lockdown spending binge.

4. Businesses refraining from capital spending.

5. New global GDP shrinkage in response to the second wave of infections striking Europe, the UK, and United States.

If all of these factors come into play, then the economy definitely will be weak. But how realistic is it to expect that they will be truly negative? Not all that much it seems based on a lot of the information we already have in hand.

Consider the first factor regarding job losses. There will certainly be some businesses who lay off people as a result of wage subsidies ending. But the evidence so far regarding the labour market is that shortages are appearing across a wide range of sectors and skills very quickly. Employers went into the Covid-19 shock with inability to hire, train, and retain staff being the greatest problem for many.

Now, we hear many stories in the construction sector of staff shortages – shortages which will also make it very difficult for the government to undertake the “shovel ready” infrastructure projects they touted in theory but as yet have failed to list in practice. The agricultural sector is well known as suffering labour shortages. Surprisingly, a couple of hotels have recently noted their inability to source staff to handle the surge in domestic tourism.

Businesses are responding to a better outlook and their memories of staff shortages by lifting their plans to hire people. In the recent NZIER Quarterly Survey of Business Opinion a net 16% of businesses said that they plan hiring more people in the next three months. This is a substantial turnaround from a net 28% planning layoffs in the June quarter survey, and slightly above the average level of hiring intentions for the past ten years.

The chances that consumer spending and the housing market are about to be hit by a wave of new redundancies are very small.

Second, will mortgagee sales soar come April? No. As I have been pointing out for many months now, the bulk of job losses (not all) are being experienced by young people earning below average wages in the hospitality, tourism, accommodation, entertainment, and retail sectors. Few own houses. Add in record low interest rates and now rising house prices everywhere around the country, and very few people will be forced to sell.

The housing market is strong and is likely to remain strong – though that may now become a problem for the Reserve Bank and at the latest come May 1 next year, LVR rules will be reinstated.

Third, will the post-lockdown consumer spending binge end? One day yes, and retailers of long-lasting (durable) consumer goods should take care not to extrapolate their recent exceptionally strong sales beyond perhaps the middle of 2021. But there is no evidence as yet that consumers are saying enough when it comes to buying spas and wall hangings.

In my monthly Spending Plans Survey a net 32% of over 1,300 respondents in October said that they plan raising their spending levels in the near future. This was a sharp jump from a net 13% saying they intended this in the September survey.

Fourth, will businesses refrain from undertaking the capital spending which ultimately is virtually the only way an economy can keep on growing and sustain then raise the average standard of living? They already have cut back on their investment and this can be seen in bank lending to the business sector running some $7bn lower than would otherwise have been the case without Covid-19. The question is whether businesses will step forward to re-engage with their spending plans.

This side of Christmas the answer is probably no. But during 2021 it looks reasonable to expect more business investment. Indicators for activity in sectors like manufacturing, farming, healthcare, and construction are unusually strong. And in the NZIER's survey noted above, while a net 36% of businesses said they would cut spending in the June quarter survey, this fell to only a net 2% saying so in the September quarter survey.

This is not yet a positive indicator. But the direction of movement is a good one.

Finally, could the world economy dip into a new recession? The outlook has certainly become worse again in Europe, the UK, and US where infection numbers have recently soared to new records in some instances. But a shift in some regards seems underway with acceptance of worse health outcomes in exchange for avoidance of the tight lockdowns imposed in many countries earlier this year.

But of greatest relevance to ourselves is the fact that 55% of our physical exports go to Asia including China, and growth prospects there are much brighter than in Anglo-Saxon countries. China recorded economic growth of 4.9% in the September quarter compared with a year earlier. That growth to date has come from higher infrastructure spending along with factories operating at high capacity to meet the surge in demand around the world for home furnishings.

There are signs however that consumer spending in China is finally starting to grow again. This is very positive for our exports of primary products into China and the wider Asian area and suggests prices for our exports will remain firm. In fact analysts are upgrading their predictions for dairy company payouts for this season on the back of the good demand for dairy products overseas.

We are not out of the woods yet by any means. But many things are moving in the right direction. And, as mentioned in last month's column, the next big changes for a number of things will be in the growth-promoting direction.

Specifically, the next change in bank lending policies for the business sector will be a loosening. The next change in border management will be an opening (some ways out yet). The next change in the wealth effect (from movements in asset prices) will be upward due to soaring house prices.

Also, over the coming year some $160bn worth of fixed rate mortgages will come up for renewal at rates lower than the original fixed rates. This will free up cash for household spending.

For property owners the news is good in terms of likely growth in nationwide employment, likely further very small declines in mortgage rates (not certain), and an eventual restoration of firm monthly net migration inflows when the borders once again reopen – perhaps in 2022. The thing to keep an eye on however is potential early reimposition of LVRs by the Reserve Bank.

There is evidence of a rise in bank lending to investors with less than a 30% deposit, and to first home buyers with less than a 20% deposit and debt which exceeds five times income. The LVRs are scheduled to come back on May 1, but given the housing market momentum, unless the banks rein in their new low deposit lending voluntarily, the Reserve Bank could act early. That of course just provides a further incentive for people to buy sooner rather than later and will generate even more FOMO – fear of missing out – in the housing market in the short-term.

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By Tony Alexander