

# New Zealand Fixed Income Monthly July 2023

Low demand becoming key challenge as inflation remains elevated

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15 August 2023

## Companies feeling squeeze with demand now seen as main concern

Weaker demand is putting New Zealand's companies under increasing pressure. The New Zealand Institute of Economic Research's latest Quarterly Survey of Business Opinion<sup>1</sup> showed a continued increase in the proportion of companies citing sales as the main limiting factor on their business in the June 2023 quarter. In contrast, the proportion reporting labour as the primary constraint on their business continued to decline, although the figure remained high. The data demonstrate that declining demand is now a major concern for companies as recent rate hikes by the Reserve Bank of New Zealand (RBNZ) increasingly constrain economic activity.

## Pressure on households shown by growing mood of restraint

Signs of an increasing mood of restraint among households are seen contributing to declining demand. The latest NZ Merchant and Card Spending Chartpack by ANZ Bank New Zealand<sup>2</sup>, which shows nominal spending for various categories in June compared to the same month in the prior year based on the bank's transaction data, depicts a clear shift in household spending away from big-ticket, discretionary items. For example, spending on items such as swimming pools, building materials and appliances all showed declines. We view this as evidence of an increasingly conservative mentality among households. We also expect the significant level of mortgage rate refixing that is set to occur in the coming months to exacerbate the trend. Given that New Zealand's Official Cash Rate currently stands at 5.5%, many households will see large increases in minimum mortgage repayments when they refix their mortgages. One sign of this is that one- to two-year mortgage special rates, which banks offer to borrowers who meet certain conditions, have held up at around the 6.5% level despite the RBNZ having paused its hiking cycle.

## Labour market factors complicating inflation picture

According to the latest data from Stats NZ, New Zealand's official data agency, inflation for the June 2023 quarter came in slightly above market expectations at 1.1% compared to the previous quarter and 6% on an annual basis<sup>3</sup>. In our view, having a larger supply of appropriately skilled labour and an associated rise in unemployment would help to ease inflation. Although the issues with demand mentioned above would usually reduce demand for labour and push up unemployment, capacity in the labour market is limited given that New Zealand has near-record low unemployment levels as well as an elevated participation rate. We feel that wage relativity is increasingly exacerbating this challenge given that minimum wage growth is currently outpacing average wage growth. Companies need to offer an appropriate premium over the minimum wage to attract and retain skilled labour. Although migration is often seen as a panacea to these kinds of problems, it only provides a solution if the labour market has acceptable wage relativity domestically and, to a lesser extent, internationally.

<sup>1</sup> <https://www.nzier.org.nz/publications/qsbo-shows-a-modest-increase-in-business-confidence-and-continued-easing-in-capacity-pressures>

<sup>2</sup> <https://www.anz.co.nz/about-us/economic-markets-research/merchant-card-spending/>

<sup>3</sup> <https://www.stats.govt.nz/information-releases/consumers-price-index-june-2023-quarter/>

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