TONY'S VIEW

Input to your Strategy for Adapting to Challenges

Feel free to pass on to friends and clients wanting independent economic commentary

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To subscribe, email me…tonyalexander5@outlook.com
To enquire about having me in as a speaker, same address.

My Aim

To help Kiwis make better decisions for their businesses, investments, home purchases, and people by writing about the economy in an easy to understand manner.

One Shock Underway

New Zealand's tourism sector had a boom from 2014 to 2018 when annual visitor numbers rose by 44% from 2.7 million to 3.9 million. Now the sector is set for a recession which will come as a relief to motorists and domestic air travellers, but hit the earnings of accommodation providers including Airbnb properties, and the hospitality sector.

Many of us analysts have been expressing caution about medium and long-term prospects for the tourism sector following the boom between 2014 and 2018 which has stretched the country's resources. Airports have become crowded places sometimes unpleasant to pass through – especially Auckland. The roading network has been strained and the concept of taking a driving holiday over summer has been ditched by some Kiwis concerned about congestion and driving behaviour.

Extra pressure has been placed on the housing market with houses and apartments shifting to Airbnb use and away from long-term rental provision and owner occupancy.

But the boom in tourism has been a key source of economic and jobs growth in recent years. In fact, according to the Tourism Satellite Account, international tourism over the year to March 2019 accounted for over 20% of all our export receipts, or some $17bn. (Dairy $15.6bn, meat $7.6bn.) GST receipts from these visitors amounted to $1.8bn. The total direct and indirect contribution to our GDP from foreign tourism amounted to about 4.1% and some 165,000 jobs.

If tourism takes a hit our economy will feel it – and that is why the very first Tony's View issued this year started out by noting two big risks – Middle East war and a new SARs-like virus. The virus has spread and is now going to negatively affect our economy. The biggest effect will be on numbers of Chinese visitors, so let's start by looking at the pre-coronavirus numbers.

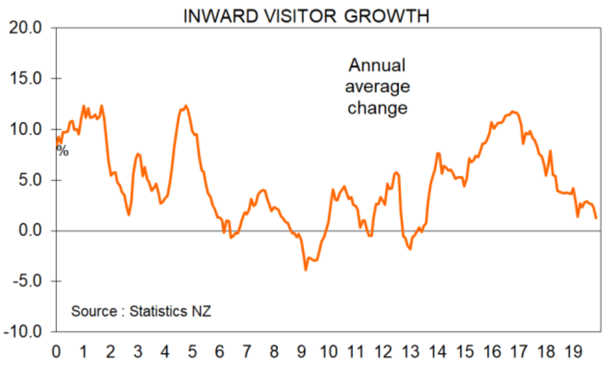
In the year to November 2019 the number of visitors from China including tourists, businesspeople etc. fell 4.7% from a year earlier to 438,489. Pre-virus New Zealand was already losing some of its allure. Now all tour group travel within and outside of China has been banned by the Chinese government. Not only that, anyone in China who has booked a package deal (not in a tour group) now won't be travelling. About 90% of the people visiting New Zealand from China are on a tour or package trip. The effects on our tourism sector and especially Queenstown, Rotorua, and their environs will be strong.

We do not know how long this will last. Even when the ban is lifted individuals are likely to be reluctant to travel for some time. Also, the depressing impact on China's pace of economic growth of the new virus will further depress willingness to travel.

But it is not just Chinese visitor numbers which are likely to decline. The virus outbreak is likely to depress the tourism industry worldwide as people choose to stay home rather than risk exposure in crowded airplanes, buses, and terminals. And it is worth adding in the slowly growing effect of the flight-shame movement coming out of Europe.

And we might also see some depressing impact on visitor numbers from the bushfires in Australia discouraging tourists from going there – thus we miss out on the side-trip many do to New Zealand.

Over the year to November total visitor numbers into New Zealand grew by only 1.3% from all source countries combined. A decline is virtually guaranteed this year and if economic history tells us one thing it is this. A slump in an industry which has just experienced an extended boom can have strong consequences for a great range of businesses, locations, and people.



If you are exposed to the foreign tourism industry, you'd best have your cash flows tightly under control already and should be reviewing them again now. If you can it may pay to delay planned capital expenditure. None of us can possibly know how long the decline in international travel – out of China in particular – will go on. Best assume the worst and slim down now before your bank does it for you.

Of course, there is the flip side people often forget about when a sector undergoes a correction. Cheapening of assets provides purchasing opportunities for those with good capital bases and access to credit. So, some consolidation of operators across accommodation, hospitality, and services is probable – but again, the timeframe here is anyone's guess. Best guess. The effects of SARs seemed to reach their worst in terms of inward visitor numbers some 3-4 months after the early-2003 outbreak. On that basis, perhaps things will be pulling back from decline by the middle of the year. But that is just pure guesswork.

But it is not just the travel industry that is going to take a hit – one reinforced by the fact the virus outbreak is happening when many people were going to travel for Chinese New Year celebrations – many of which one suspects will be cancelled not just in China but here and in other parts of the world as well – or if they go ahead will likely be poorly attended.

Our export education sector will be negatively affected. Students planning to travel here might be held at home by their two parents and four grandparents obviously concerned about the health of their single child/grandchild.

Housing Market

There were no freshly released meaningful numbers on the housing market to analyse this week. So, let's address a question. What will the impact of the coronavirus outbreak be on our housing market?

The pace of economic growth in the country will be slowed by the reduction in tourism activity and increased caution by consumers and businesses generally. This will reduce the ability of businesses to raise prices and reduce the chances of inflation moving upward. That means less chance of higher interest rates this year and the return of a possibility that rates get cut – though that would be a brave call this early in the process.

Lower interest rates will tend to boost housing activity and average prices as investors hold onto properties and perhaps seek more in the face of continued low term deposit interest rates, and increased worries about returns on equities/managed funds.

Given the biggest weakness in economic activity from the virus will occur offshore the relative attractiveness of staying in and shifting to New Zealand will grow. So, population growth from net migration flows will likely improve very marginally and that will boost housing demand. However, reduced opportunities to make money from Airbnb renting may return some properties to the rental pool – again, just at the margin.

Reduced employment in the tourism sector would depress housing demand were it not for the fact that there is a shortage of staff in New Zealand so the affected people will find plenty of other employment opportunities. However, Rotorua and its environs will likely suffer a net depressive impact and this risks stalling the rise in the Rotorua market in recent years.

All up, at the very margin, a virus outbreak looks like a net negative for housing markets in tourism-focussed locations like Rotorua and to a lesser extent Queenstown and Wanaka. But elsewhere in the country the interest rates effect and potentially tiny net migration effect could be a small net positive – UNLESS the outbreak develops into thousands of people dying offshore with no clear end in sight. In that case the interest rates effect will be swamped by the sentiment and employment effects and cause prices to decline as economies enter recession. We wait and watch though give that scenario a very low probability at this stage.

Interest Rates

The negative economic impact to come from the new virus outbreak increases the chances that there will be another easing of monetary policy this year. A cut in the cash rate at the next review on February 12 is extremely unlikely, and while the Reserve Bank will note the downside risks, they will probably be quite reluctant to signal a new bias toward lowering rates – given what is happening in the housing market.

The main impact of the virus outbreak is likely to be some declines in medium to long-term bank borrowing costs. This week such declines only amounted to around 0.05% so as yet market impact is minor. We wait and see.

CHOOSING YOUR FIXED MORTGAGE RATE TERM

There are no changes in lowest available fixed rates this week.

When fixing a mortgage rate term most people take whichever rate is the lowest. So, each week I shall calculate what rates would have to be in the future to make this option better than some alternatives. Note, there are far, far more alternatives than calculated here. And always remember, it is worth paying a premium for rate certainty over a longer period of time. It's also worth using a broker to get the best deal. Broker use is far higher in Australia than New Zealand but we will probably catch up.

Current minimum fixed rates across the main banks. *

1 year	3.39%
2 years	3.55%
3 years	3.89%
4 years	3.99%
5 years	4.09%

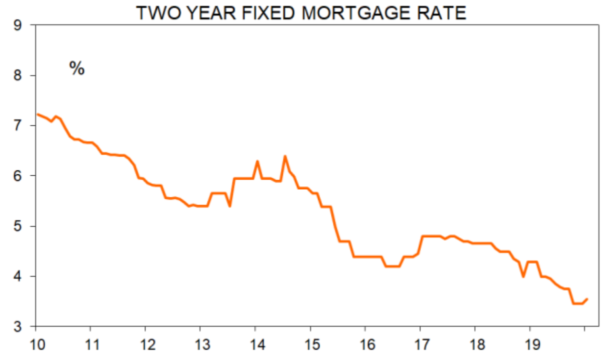
I can fix 1 year at 3.39%.

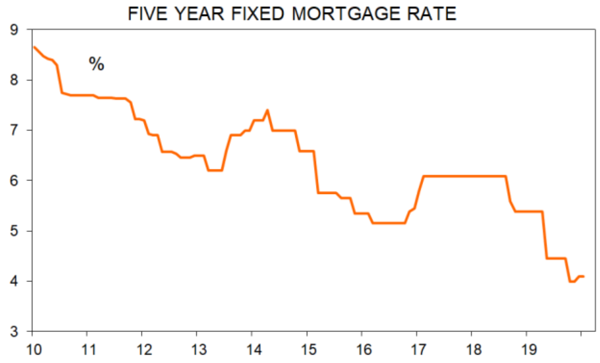
Is this better than fixing 2 years?	Yes, if in 1 year the 1-year rate is below 3.71%.
Is this better than fixing 3 years?	Yes, if in 1 year the 2-year rate is below 4.14%.
Is this better than fixing 4 years?	Yes, if in 1 year the 3-year rate is below 4.19%
Is this better than fixing 5 years?	Yes, if in 1 year the 4-year rate is below 4.14%.

If you fix one-year then you get a nice low rate. But the odds are now against further monetary policy easing, and tightening will eventually become more likely than any easing and interest rates will reflect this. Chances are in one year the one-year rate will be close to 3.51%, so if fixing two years was my preference, I'd be inclined toward that term instead of 3.39% as the cost of rate certainty looks quite cheap.

The odds that the two-year rate in one year will be below 4.14% look fairly good, so if three years was my preferred term, then taking the low one-year rate might be okay. But it is very easy to imagine that one year from now the three- and four-year rates will be higher than 4.19% and 4.14% respectively. So, if fixing for beyond three years was my goal, I'd be taking a gamble by fixing just one year now and personally would be inclined to take the current longer-term rate. Maybe this is as low as rates get outside of a recession situation. One might think about locking in for as long as possible.

*Minimum 20% deposit, owner occupiers.
Compounding is minor so is ignored.

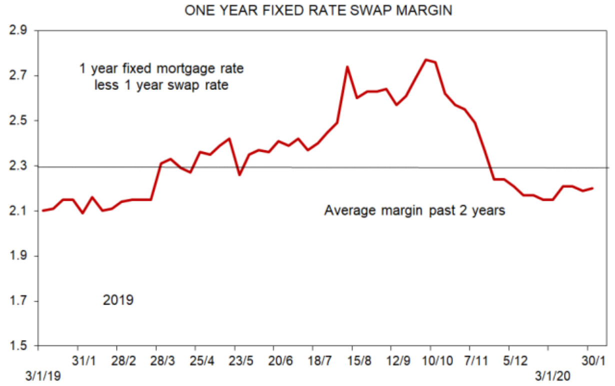


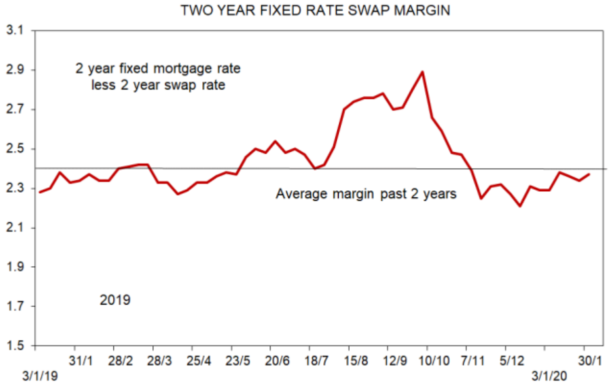


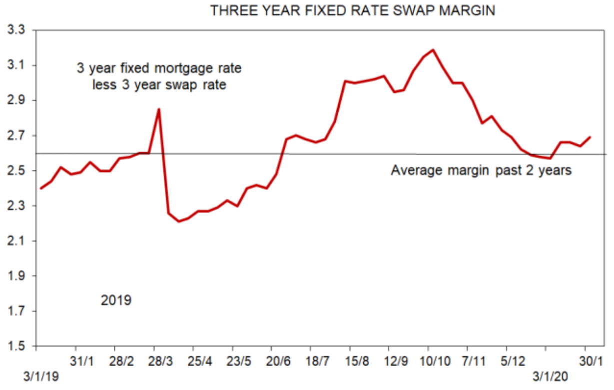
IS A FIXED RATE CHANGE IMMINENT?

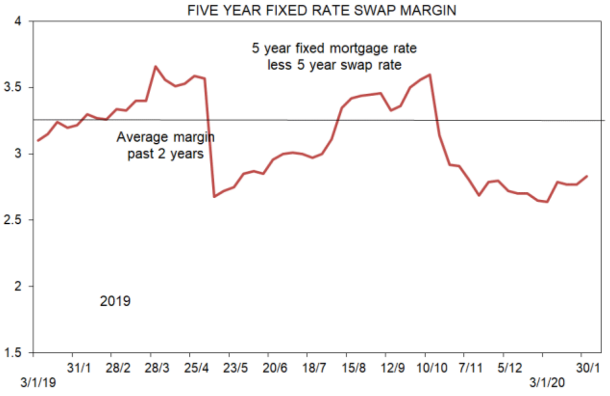
Amidst virus worries, swap rates have fallen back to early-December levels. But the small rate declines along the lines of 0.05% for three-year money are not big enough to suggest any obvious pressure on banks to alter fixed mortgage rates.

You can form your own opinion as to whether banks might be about to raise or lower their fixed rates by looking at the following graphs. They compare published fixed rates with the most frequently changing component of the total cost of funds – the swap rate. Note that there are other funding costs which will not be captured here, but they change infrequently. But be warned. There is no real forecasting insight delivered by a thing (equity, exchange rate etc.) moving further from some concept of fair value or average. If a thing is 10% above trend, it might simply be on its way to being 40% above trend. For good bank rate comparisons access www.interest.co.nz









Are You Seeing Something I'm Not?

Don't be afraid to flick me an email at tonyalexander5@outlook.com if you reckon I'm missing something happening in the economy, or you've got experience or insight into some of the developments underway which you'd like to share.

Online - It's A Family Thing

For your guide, in my family it is not just myself communicating and informing people principally online and working from home.

My wife Dr Sarah Alexander manages the network of early education and care services around the country (www.ChildForum.com) and the website for parent ratings and reviews of children's services (www.myece.org.nz).

My daughter Lilia Alexander (finalist in the Youth category for Wellingtonian of the Year 2019) owns and runs Social Media based Wellington – LIVE (160,000 followers)
https://www.facebook.com/WellingtonLIVENZ/
"…the largest go-to social media-based updates and news platform for the Wellington region…" Wellington – LIVE offers advertising options for local events and businesses.
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This publication is written by Tony Alexander, independent economist. You can contact me via LinkedIn or email tonyalexander5@outlook.com

DETAILED GRAPHS ENLARGED

None this week.