Manufacturers Business Planning Forecasts

20 February 2001

FORECASTS: MARCH QUARTER 2001

Introduction

This bulletin is designed to help plan your business. It brings together forecasts of important indicators to help you prepare budgets and business plans.

The forecasts are drawn from two main sources. The New Zealand information is based on a survey of the five main trading banks (ANZ, ASB, BNZ, NBNZ and WPT). The Australian information is based on consensus forecasts put together by the UK based magazine “The Economist”. Sources of other information are as shown.

We stress that the information in this publication is by its nature uncertain. Your firm is unique, and you will need to make your own decisions. However, we believe the better informed you are about the way various business people see the future, the better decisions you can make.

Where appropriate we have not only included the average value across all forecasters, but also the highest and the lowest forecast. This gives some idea of the spread of forecasts, and therefore an idea of the uncertainty involved.

The New Zealand Economy

Growth in real GDP, the measure of how much New Zealand’s production is likely to increase or decrease, illustrates how demand, in terms of volume, might change in the New Zealand market.

The forecasts for the economy over the next 18 months show a fairly stable level of growth over the next six months (2.5%) but there is an increasing divergence of views about growth in 2002. Forecasts for GDP growth in the year to September 2002 range from 3.9% to only 2.6%.

The average GDP growth forecast of 2.5% for the March and September quarters in 2001 is well below the latest GDP growth level of 4.5% to the year end September 2000. The result for last year, however, was influenced by very strong growth at the beginning of 2000. Growth in the September 2000 quarter was 2.4% up on September 1999. Forecasters are therefore expecting growth to remain at that level.

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There is still considerable uncertainty about the level of growth to be expected this year. This is because no one is certain about the extent of the downturn in the United States. New Zealand's economic growth will also depend on what impact the US downturn has on our main trading partners. The evidence to date suggests that the downturn in Australia is having a more immediate impact on New Zealand manufacturers than that in the United States, particularly those selling into the Australian construction sector.

It is difficult to gauge whether the low value of the New Zealand dollar (despite its recent appreciation) will allow New Zealand manufacturers to continue to grow export markets, particularly as demand in some of these markets may be slowing. The low dollar over the previous 12 months will continue to boost domestic demand, particularly through increased prices for the primary sector. The dairy sector alone is talking of a $1 billion boost to farmers' earnings.

The latest WestpacTrust Manufacturers Business Opinion survey taken in December suggests domestic demand in the quarter was stronger than expected. Moreover, manufacturers expected domestic demand to increase further in the March quarter but exports were still expected to be the main driver of growth.

It is still not clear what direction the Reserve Bank will take on interest rates, but strengthening domestic demand is likely to result in the Official Cash Rate (OCR) being held at the present level for a while. A fall in longer term interest rates, however, is bringing down rates for longer term fixed mortgages.

At this stage it appears the Bank is waiting to see the extent to which wage setting follows the rise in the CPI, or whether there will be a longer period of time where wages continue to fall in real terms.

Real GDP % Growth

	Years Ending		
	Mar 01	*Sept 01*	*Sept 02*
Highest	2.6	2.7	3.9
Average	2.5	2.5	3.2
Lowest	2.2	2.4	2.6

Source: ANZ, ASB, BNZ, National and WestpacTrust

The second key indicator is the rate of inflation, which gives an idea of the extent to which prices have increased, as well as wage increase demands. There have been in the past two measures: headline inflation that includes all price movements faced by households including interest rate movements; and underlying inflation that excludes interest rate movements.

The new CPI released in October 1999 excluded interest rates, bringing it in line with the underlying inflation rate measure used by the Reserve Bank. There is now, therefore, no distinction between headline and underlying inflation.

Inflation reached 4.0% in the December quarter, but is expected to fall quickly this year. The impact of petrol price increases and the increase in tobacco tax will come out of the figures over the next nine months. In addition, the 1 December reduction in State housing rentals will offset some of the price rises in other sectors.

What is not clear is the extent to which stronger domestic demand will allow businesses to continue to pass on the impact of the sharp fall in the currency over the past year. The CPI data for the December quarter showed that price increases had become more wide spread. Further price rises across most sectors are expected in the March quarter, but will be partly offset by the rental reductions.

% Change in Inflation (CPI)

	Years Ending		
	Mar 01	*Sept 01*	*Sept 02*
Highest	3.6	3.1	2.3
Average	3.2	2.1	1.7
Lowest	2.8	1.6	1.3

Source: ANZ, ASB, BNZ, National and WestpacTrust

Statistics NZ produces an index that measures movements in the total cost of employing labour. Short-term forecasts for growth in labour costs have increased due to the higher CPI and stronger growth in the labour market. While real wages have fallen, a recovery in real wages is expected from September 2000 as the rate of increase in the CPI slows. A tighter labour market and further cost increases will mean an ongoing business focus on productivity improvement.

Labour Cost Index % Change

	Years Ending		
	Mar 01	*Sept 01*	*Sept 02*
Highest	2.3	2.6	2.7
Average	2.0	2.3	2.3
Lowest	1.8	2.0	2.0

Source: ANZ, ASB, BNZ, National and WestpacTrust

The level of unemployment is expected to fall steadily over the next two years. High productivity growth and increased labour force participation by workers aged 60 years and over will be two factors impacting on the level of employment growth and composition of the labour force. The survey data is volatile due to the impact of high sample errors so the numbers for each quarter are hard to pick.

Unemployment % (HLFS)

	Years Ending		
	Mar 01	*Sept 01*	*Sept 02*
Highest	6.0	6.0	6.2
Average	6.0	5.9	5.6
Lowest	5.9	5.6	5.2

Source: ANZ, ASB, BNZ, National and WestpacTrust

The other major cost driver is interest rates. In general overdraft rates and mortgage rates will move in line with the 90 day bill rate. Interest rate forecasts have changed significantly over the last quarter. Most forecasters now expect interest rates to be cut by the Reserve Bank in March or May.

Interest Rates (90 day bills)

	Years Ending		
	Mar 01	*Sept 01*	*Sept 02*
Highest	6.7	6.8	6.9
Average	6.5	6.3	6.3
Lowest	6.3	5.9	5.3

Source: ANZ, ASB, BNZ, National and WestpacTrust

Exchange Rates

A number of forecasts of exchange rates are available. Individual cross-rates (e.g. the NZ$/A$) can change quite sharply, but the trade weighted index (TWI) is more stable because of the way the Reserve Bank operates. There is considerable uncertainty over the expected movement of the NZ$ against the Australian Dollar, but a high level of agreement over the movement against the US Dollar. At the same time there is disagreement on whether the exchange rate will appreciate or depreciate against the Australian Dollar. The average, however, is now at $0.80 compared with $0.77 three months ago. The currency is expected to continue to appreciate against the US Dollar, reaching $0.52 by September 2002.

A$

	Mar 01	*Sept 01*	*Sept 02*
Highest	81.2	82.5	84.1
Average	80.3	80.1	80.2
Lowest	79.0	79.0	77.0

US$

	Mar 01	*Sept 01*	*Sept 02*
Highest	46.5	52.0	53.0
Average	46.2	49.5	51.8
Lowest	46.0	48.0	50.0

TWI

	Mar 01	*Sept 01*	*Sept 02*
Highest	53.0	57.4	57.9
Average	52.5	54.5	55.9
Lowest	52.1	53.0	54.4

Source: ANZ, ASB, BNZ, National and WestpacTrust

In practice, buying forward the A$ and US$ can reduce the risk in cross rate movements. Indicative bank buy rates quoted by the NBNZ (all other banks are the same but the rates change from day to day) on 20 February 2000 were:

A$		**US$**	
20 Aug 01	*20 Feb 02*	*20 Aug 01*	*20 Feb 02*
.8107	.8071	.4299	.4279

Source: National Bank of New Zealand

Forward cover rates are based on the exchange rate when it is bought, so it pays to watch daily movements and buy at the right time, particularly in light of recent movement in the exchange rate with Australia and the US. These rates, for instance, are now significantly higher than those quoted six months ago.

The Australian Economy

The performance of the Australian economy impacts on New Zealand in two ways. It provides a measure of how well exporting is likely to go, and it gives an idea of what kind of competition there is coming from Australian sourced products.

GDP Growth

	Calendar Years	
	2000	*2001*
Highest	4.6	4.0
Average	4.4	3.3
Lowest	4.2	2.5

Source: The Economist

Short term growth forecasts for the Australian economy have fallen, but may still be lagging behind the actual pace of slow down in that economy. Business confidence became more negative in the December quarter with a net 9% of manufacturers reporting a fall in output in the quarter. A net 3% expect sales to fall in the March quarter. Exports by New Zealand manufacturers to Australia fell in both November and December, mostly due to weaker exports of wood products.

The recent cut in interest rates by the Reserve Bank of Australia should help to boost the housing sector, but there is uncertainty over the extent to which slowing growth in the US and Japan will impact on the Australian economy.

Headline Inflation

	Calendar Years	
Quarter	*2000*	*2001*
Average	4.6	4.0

Source: The Economist

Inflation forecasts have also lagged behind the official statistics, with forecasters expecting a CPI increase of 4.6% in December and an actual outturn of 5.8%. Strong wage growth and continued weakness in the Australian dollar are expected to result in a CPI of 4.0% to December 2001, even though the 1 July 2000 GST impact will no longer show in the figures.

Interest rates (90 day bills)

	Calendar Years	
2001	*2002*	*2003*
6.5	5.4	5.3

Source: NZIER Quarterly Predictions

Short-term interest rates have fallen due to the recent cut by the Reserve Bank of Australia, and the slowing in economic growth. Further interest rate cuts are now expected in 2001, but the outlook for 2002 and 2003 is so far unchanged.

Rest of the World

Short term international growth prospects have been revised significantly over the last three months. This change in sentiment is not reflected in the NZIER forecasts which were released in December. Growth is now expected to slow rapidly in the US. The main uncertainty is now how quickly the economy will recover from recession. Forecasts for growth in Japan and Asia have also been revised downwards, but there has so far been little change to forecasts for Europe.

World GDP Growth (Trading Partners)

Calendar Years

2001	*2002*	*2003*	*2004*
3.5	3.7	3.7	3.9

Source: NZIER Quarterly Predictions