NEW ZEALAND ECONOMIC UPDATE

BRIEFING ABOUT THE RESILIENCE OF THE NZ ECONOMY DURING COVID 19

Quarter 1 2020

INTRODUCTION

This economic update has been written to provide our investors with a plain English overview of current market conditions regarding Covid-19.

GOVERNMENT'S PLANS (THEIR BIG PICTURE) & THEIR COVID 19 RESPONSE

Government is investing an additional $12 billion in new spending each year which means new Government investment will take spending in New Zealand to the highest level in over 20 years. (Figure 2).

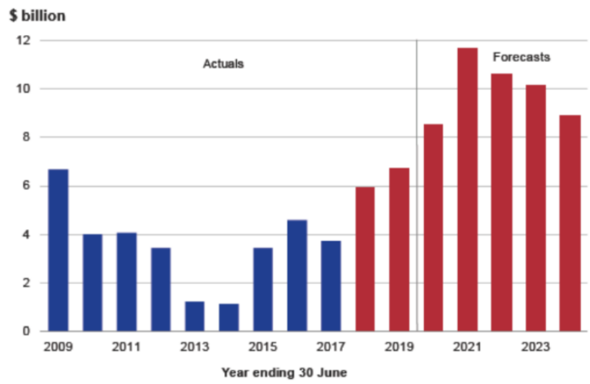
But there is also, an additional $12.1 billion package on top of the $12 billion mentioned above. This $12 billion is just to deal with Covid 19 is:

- $500 million boost for health;
- $9 billion in wage subsidies;
- $126 million in COVID-19 leave and self-isolation support;
- $2.8 billion income support & $25 per week benefit increase;
- $2.8 billion in business tax savings;
- $600 million initial aviation support package (to support Air NZ they spent an extra $900 million).

Also, there will be a new budget in May this year where they will announce more spending on top of the latest spending announcements

So, it's a new spend of $22 billion in under 10 months, (Govt budget is $100 billion). In comparison, John Key spent approx. $40 billion extra in the immediate 3 years after the GFC started.

Figure 2 - Net capital spending

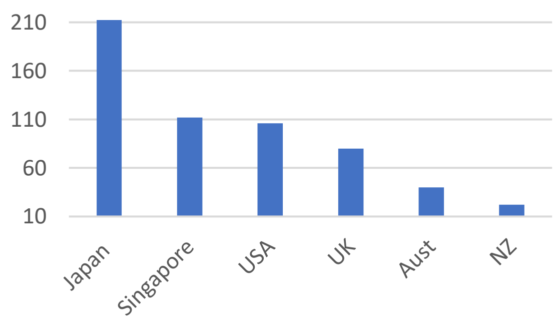


NZ GOVERNMENT DEBT IS LOW MEANING THEY CAN BORROW MORE TO HELP THE ECONOMY

It's also important to keep in mind that the Government has very low debt compared to other countries of only 19% of GDP. Singapore is 110%. (Figure 3).

This means that the NZ Government is in a very good position if the economy gets tight, as it has significant headroom to spend.

Figure 3 - Government debt as a percentage of the economy.



TEMPLETON

THREE THINGS THE RESERVE BANK OF NZ IS DOING IN RESPONSE TO COVID 19

1. EMERGENCY INTEREST RATE CUT

They have dropped interest rates by 0.75%, banks can pass on lower interest rates.

2. THE BANKS HAVE A YEAR'S GRACE OF HAVING TO KEEP BACK EXTRA CASH

The Reserve Bank requires banks to hold a certain % of its funds in a liquid form (cash for example). They were increasing that % this year, which effectively takes money out of the financial system that would otherwise have been available for lending.

They have delayed this for a year so an extra $47 billion is available to be lent to the home buyers/businesses which wasn't expected.

3. QUANTATATIVE EASING

The Reserve Bank has already implemented purchasing $30 billion of government bonds, which is a faster response than what happened in the GFC. Basically, they are putting extra money into our economy fast!

POPULATION GROWTH REMAINS STRONG

Net migration inflows are higher over the forecast period than assumed in the 2019 Budget, with 50,000 persons in 2018/19 through to 35,000 persons in the 2023/24 years.

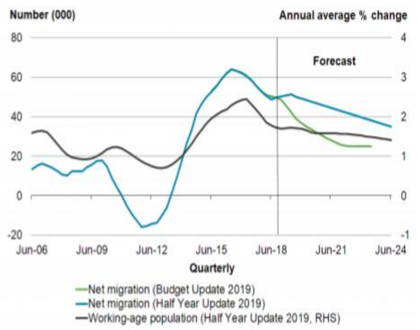
This migration growth equates to approx. 210,000 new Kiwis over the next 5 years.

Or, basically over the next 5 years there needs to be a home building programme of approx. 73,000 new homes.

NZ's net migration irrespective of what political parties say have remained consistently strong and looks to remain so.

Prior to 2010, NZ's net migration was only 15,000 people per annum.

Figure 1.2 – Population growth and changes to net migration



WHAT IS THE AVERAGE KIWI'S EXPOSURE TO THE STOCKMARKET?

A poll conducted by Colmar Brunton last year on behalf of a NZ company called Sharesies found that nearly 75% of New Zealanders have a savings account, and only 20% are investing in shares directly.

Whereas 53% of Americans are directly invested into the share market – meaning they are taking more notice of the share movements.

BUT SURELY NZ IS MASSIVELY EXPOSED THROUGH KIWISAVER TO THE WORLD STOCK MARKET?

Nope. Financial advisor Martin Hawes wrote this in February 2020 which provides some context:

"KiwiSaver now has a total of around $70 billion. Of that $70 billion, approximately 11% is invested on the New Zealand share market…and, 30% in foreign shares. The rest is in money (cash, or normal savings accounts) and bonds.

To put that into money terms, assuming a total of $70 billion in KiwiSaver, $7.7 billion is in New Zealand shares with $21 billion invested offshore.

Or compared to the whole economy, the $21 billion represents only 7% of the total Kiwi economy.

DEFENSIVE STRATEGIES WHICH WILL SUPPORT THE NZ ECONOMY

OVERALL INFRASTRUCTURE SPEND

The story here is positive for NZ infrastructure investment. The Government has established the New Zealand Infrastructure Commission to identify the infrastructure New Zealand needs to keep pace with population growth, to continue to grow the national infrastructure pipeline, which is still under development by the Infrastructure Commission. It contains more than 500 projects over the short to medium-term – with an estimated value of $21.1 billion. The Commission will improve how New Zealand coordinates, plans and invests in infrastructure through the delivery of a 30-year infrastructure strategy.

HOUSEHOLD DEBT

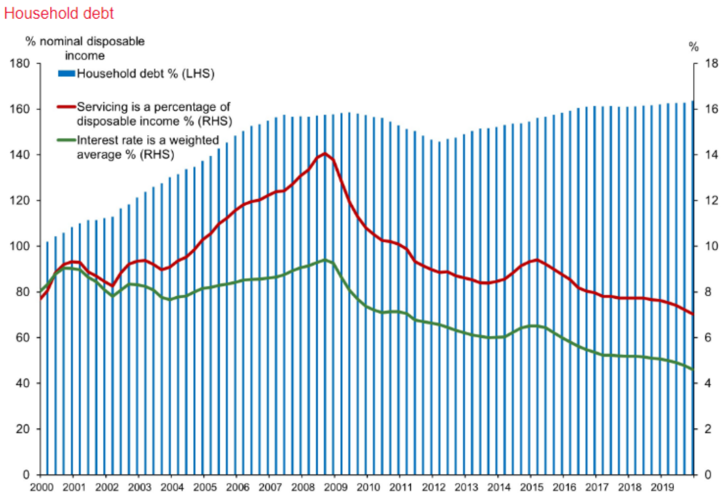
This is something not often publicised, but household debt servicing (being able to pay back your mortgage/credit card as a % your income) has decreased a lot compared to the Global Financial Crisis in 2008-2010. See the red line in the graph.

This means that households will benefit from further reduced interest rates with the latest Reserve Bank interest rates. NOTE; It takes approx. 6 months for interest rate cuts to kick in.

Household debt

Household debt comprises mortgage loans, consumer loans such as credit cards, and student loans. Data is available from 1998.

Data for the graph below is available in a spreadsheet containing all key graph data (XLSX <200KB).



Source: RBNZ and RBNZ estimates, Stats NZ.

NZ SUPERANNUATION FUND AND ITS GROWING SIZE

Again, this is a strong story and one many don't think of as a defensive strategy during a recession. Having restarted payments to the NZ Superfund (Fund), the Government is now making regular contributions. These are projected to increase the size of the Fund to $71.4 billion by 2023/24.

Currently the fund is $33.3 billion. Over the next 5 years, the Govt will contribute $11.5 billion into the Fund.

It will obviously be looking to invest into our economy which means that there is more support for investment into the economy.

CREDIT RATING AGENCIES

The international view of NZ's fiscal position is very strong.

Moody's most recent credit opinion report states:

"the stable outlook is anchored by an expectation that, even in the face of shocks, New Zealand's credible institutions with highly effective policymaking and ample policy space (read they can do quantitative easing) will maintain economic and financial stability".

HOW YOU CAN PLAN FOR ANY DISRUPTION IN ADVANCE

New Zealand Bankers' Association chief executive Roger Beaumont says customers financially affected by COVID-19, are encouraged to contact their bank.

Depending on the customers' individual circumstances potential options for support include:

1. Reducing or suspending principal payments on loans and temporarily moving to interest-only repayments
2. Helping with restructuring business loans
3. Consolidating loans to help make repayments more manageable
4. Providing access to short-term funding
5. Referring individual customers to budgeting services.

The best advice is if you are concerned then talk to your bank or financial provider sooner rather than later.

FOR MORE INFORMATION

Chris Simpson: Templeton Group
Chris.simpson@templetongroup.co.nz
Phone: 021922787
www.templetongroup.co.nz

SOURCES

- Reserve Bank
- Treasury

TEMPLETON

THANK YOU FOR READING

I've written this paper in a factual way to provide you with context in an uncertain world. I'm a former Director of Research of the Government Parliamentary Research Unit, and I've sat through several economic shocks. Including working in Parliament through the tough times of the early 90s when unemployment was 12% and the economy was minus 2% (going backwards) with Govt debt sitting at approx. 70% of GDP.

I also watched how John Key's government managed the GFC in the late 2000s, where they effectively borrowed $60 billion for new spending during their time in Govt.

Unlike previous economic shocks which weren't initially as clear regarding the cause, this economic event is created by something which is immediately known, it's a virus.

Previous economic surprises were different. They ranged from the Global Financial Crisis (GFC) which was created by the failure of financial products that bundled debt together and weren't understood by the market.

Through to the Great Depression of 1929 to 1939 where the United States' economy declined by 30% and unemployment reached more than 20%. That was a depression (not a recession) and a major reason was that it was created by people thinking that the stock market was easy money.

By comparison, during the GFC of 2007–09, the second largest economic downturn in US history, GDP declined by 4.3% and unemployment reached slightly less than 10%. Whereas in NZ during the GFC unemployment was only 6.8% compared to the 1991 recession where it was nearly 12%.

This paper isn't written for investment advice, it is to provide some key facts in an easy to access way. Feel free to contact me if you wish to discuss further.

Chris Simpson