Monthly Economic Indicators

THE TREASURY
Kaitohutohu Kaupapa Rawa

July 2011

Executive Summary

- **The economy grew much more than expected in the March quarter and from a higher base owing to revisions**
- **There was little measured negative impact from the Canterbury earthquake**
- **High headline inflation, but underlying pressures more subdued for now**

Economic growth was much stronger in the March quarter 2011 than expected. A number of industries showed significant expansion in the March quarter, with the 0.8% quarterly growth rate driven by manufacturing production, as well as retail and wholesale trade. However, some the details of the release were not as strong as the headline suggested, with the majority of the growth in expenditure GDP coming from a large fall in imports and a rise in exports, accompanied by a rundown in stocks. The growth was from a higher base, with upward revisions to manufacturing and wholesale trade lifting December quarter growth to 0.5% from an initially reported 0.2%.

The expected significant drop in household spending and business output in Canterbury as a result of the 22 February earthquake did not eventuate, with the majority of large businesses able to either resume operations quickly or relocate to other premises. Households seemed to be able to switch their spending from closed outlets to those in other locations and lost spending was offset by replacement of belongings damaged in the earthquake. Positive impacts from the earthquake were picked up through increased government activity by Civil Defence and the Earthquake Commission.

Growth in the previous two quarters is expected to have continued into the June quarter and over the rest of 2011. Partial indicators of GDP in the June quarter point to growth around 0.5%. Retail sales and services indicators suggest private consumption will continue to grow at its recent 1.5% annual growth rate and merchandise trade figures point to another strong contribution from net exports. Manufacturing production also looks like adding to its recent expansion. Improving business confidence indicates that annual economic growth will continue to pick up in coming quarters, following on from the flat period in the middle of 2010.

While headline inflation is at a 21-year high of 5.3%, the majority is from increases in government-related charges and the large international commodity price increases. Removing the effects of these items gives underlying inflation of around 1.4%, below the mid-point of the Reserve Bank 1-3% target band. Although the headline rate is expected to drop back into the target band around the middle of 2012, as these temporary impacts fade, an improving economy, rising business pricing intentions and high inflation expectations should result in rising underlying inflation. There will be some offset from the recent appreciation in the New Zealand Dollar (NZD).

The strengthening recovery is balanced against a softening international outlook and uncertainty over sovereign debt problems. Growth appears to be slowing in Australia and in the US the recovery is subdued and the government's fiscal situation is causing heightened uncertainty. Counteracting these negatives are strong growth in China and positive progress in euro area sovereign debt. These developments have been positives for the NZD, reaching post-float highs on bilateral bases.

Our Special Topic this month looks at the effect of the internet on household spending.

New Zealand Government

Analysis

Economic growth picking up

The economic recovery is beginning to gain momentum, with the economy growing faster than previously thought in the December quarter 2010 and March quarter 2011. Indicators and the forthcoming Rugby World Cup and earthquake rebuild suggest that this momentum will continue over the rest of 2011 and into 2012. The rising activity comes from both a stronger underlying economy and a less-than-anticipated disruption to the economy from the 22 February 2011 Canterbury earthquake.

March quarter sets good platform for 2011…

The economy expanded 0.8% in the March quarter 2011, much more than the market had forecast (0.4%) and our own revised estimate (0.3%). Several industries showed strong expansions, indicating the domestic economy is on a better footing than was previously thought.

The 22 February earthquake did not appear to have a significant negative impact on output as measured by GDP and there were in fact some positive impacts from the earthquake. Most large businesses were either able to continue operating soon after the earthquake or relocate to alternative premises to resume production. Several industries in Canterbury, including manufacturing, electricity and construction, were negatively affected, although these did not have a noticeable impact at the aggregate level. While many retail and accommodation locations were disrupted, it appears that spending was diverted to other outlets which were still operational.

The effect of the earthquake was picked up at a regional level in other partial indicators, showing the earthquake had a sizable impact on the Canterbury economy. Accommodation guest nights in Canterbury were down 16% in May 2011 compared to a year ago, due to a 38% fall in international nights as overseas coverage of the earthquake discouraged tourists from travelling there. There was also a significant loss of accommodation capacity from the earthquake.

…driven by manufacturing and services...

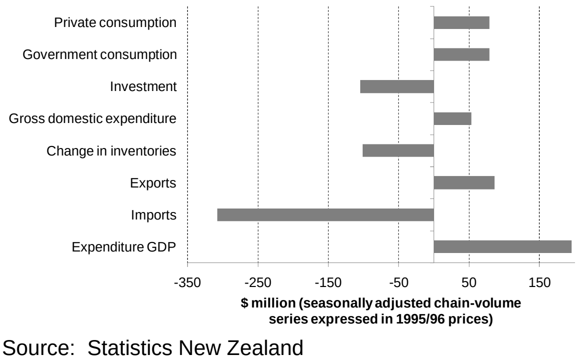
Manufacturing production grew a strong 3.6% in the March quarter, on the back of a 3.4% rise in the December quarter. This acceleration comes off a low base, with output in the sector having been in decline since 2005. The falling output was accentuated by a fall in external demand resulting from the global financial crisis in 2008.

Wholesale and retail trade rose 1.5% and 2.0% respectively in the March quarter. These are two areas we thought would have shown significant earthquake disruptions, but it appears businesses that were forced to shut down had customers go to other premises that were able to open. Government administration and defence was boosted by earthquake-related activity, including civil defence and emergency management.

...but details weaker than headline growth would suggest

Expenditure GDP rose 0.6% in the March quarter, with most of the growth coming from net exports. Gross domestic expenditure (consumption plus investment) only increased $53 million (0.1%, Figure 1). The net export contribution was mainly due to a 2.4% fall in imports, but also a 0.8% rise in exports, accompanied by a rundown in stocks. The falling imports and stock rundown suggest the domestic economy may still be some way from a strong recovery. The main contributor was passenger motor car imports down 26.0%. While the June quarter looks positive, a likely rebound in imports, along with signs of a slowing global economy (see international discussion on page 6), indicates that the net export contribution may not continue into the second half of 2011.

Figure 1 – Change in March quarter expenditure GDP



Source: Statistics New Zealand

Private consumption continues to grow at a moderate pace, rising an annual 1.5% in the March quarter. The Canterbury earthquake is likely to have dampened consumer spending in the region, although there would have been some offset from the replacement of destroyed belongings. Rising private consumption was driven by durable goods volumes which rose a strong 2.9%. This increase is at odds with recent subdued consumer confidence and housing market data, but fits as a response to recent discounting seen in the retail sector and the purchases of items to replace those damaged in the earthquakes.

Government consumption rose 1.2%, driven by increases in activity by Civil Defence, and the Earthquake Commission, as well as clean up activity related to the February earthquake. This is the main area where the earthquake had a positive impact on GDP.

More than offsetting the increases in consumption was a fall in investment and a run-down of inventories. The decrease in investment was from lower residential and non-residential building work, which partly reflect less construction in Canterbury following the two earthquakes. Inventories that were destroyed in the earthquake do not reflect economic activity so were not included in the inventory run-down.

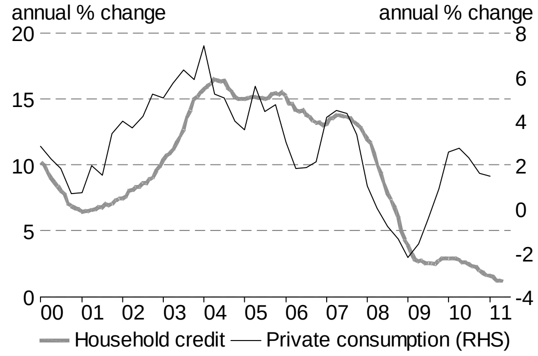
Growth starting from a higher level of activity

The strong headline March quarter result follows on from the December quarter 2010, where growth was revised up from 0.2% to 0.5%. The change was mainly due to upward revisions to wholesale trade and manufacturing; the full collection of data had been delayed due to the earthquakes. The last two quarters showed that, despite two devastating earthquakes that caused significant damage and loss of life, the economy managed steady growth that can be built on in coming quarters.

Growth expected to continue in June quarter...

Monthly activity indicators suggest that the growth seen in the previous two quarters continued through the June quarter. Private consumption appears to be growing at around a 1.5% annualised pace, similar to the previous few quarters. Electronic card transactions suggest that retail sales grew at a solid rate. The BusinessNZ BNZ Performance of Services Index, which increased further into expansionary territory in June, indicates moderate services consumption growth. Despite private consumption being more buoyant than we had expected in the *Budget Update,* households appear to still be consolidating and paying down debt rather than borrowing money to consume. While household spending is growing again, it is at a much more subdued pace than in the earlier part of the previous decade. This is supported by domestic credit growth figures, which continue to fall back from their pre-global-financial-crisis peak (Figure 2). This month's special topic discusses the changing trends in private consumption.

Figure 2 – Credit growth and private consumption



Source: Statistics New Zealand, RBNZ

Merchandise trade figures indicate that net exports will add to growth in the June quarter. Goods export values rose 4.5% and import values fell 1.0%, in the June quarter. The strong exports were led by dairy and meat, while imports were constrained by falling capital goods.

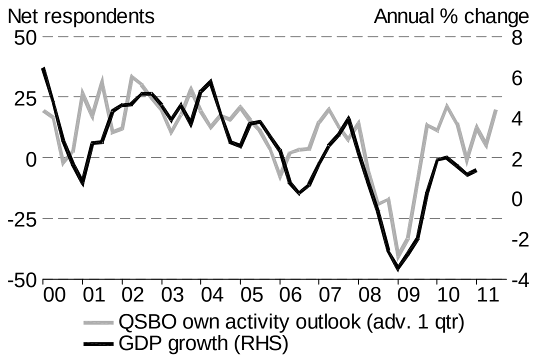
However, export prices appear to have peaked after reaching record-high levels recently. The ANZ commodity price index fell in world terms in July, following nine straight months of increases. Also, prices in the GlobalDairyTrade online auction have fallen 13.5% in the last three fortnightly auctions. High commodity prices have been one of the main factors supporting the economy; the 37-year high in the merchandise terms of trade has provided a large boost to the incomes of commodity exporters. There is usually a 2-3 quarter lag between commodity prices in spot markets and their impact on the terms of trade, indicating commodity prices will continue to support the economy in coming quarters.

We had built a rebound from the February earthquake into our June quarter GDP forecast and with little evidence of a negative impact on March quarter growth, this bounce-back is unlikely to occur. However, the underlying economy is in a stronger position, providing some offset. We are revising down our 0.8% *Budget* pick, with around 0.5% growth now expected.

...and over the rest of 2011 and 2012

Business confidence and own trading activity showed a steady increase in the June quarter, reflecting both a bounce-back following March's earthquake affected Quarterly Survey of Business Opinion (QSBO) and a general pick-up in business conditions. Indicators in Canterbury rose back towards national averages, after weakening in the March quarter. The QSBO showed the earthquake contraction and bounce-back we had expected in GDP. A lift in the domestic trading activity outlook suggests that annual growth will continue to pick up in coming quarters (Figure 3). The positive outlook was supported by the July National Bank Business Outlook, with rises in business sentiment and own activity outlook.

Figure 3 – Business confidence and growth



Source: Statistics New Zealand, NZIER

Within the details of the QSBO, employment and investment intentions both picked up and profitability expectations rose. The Quarterly Employment Survey and the Household Labour Force Survey to be released on 2 and 4 August respectively will give an indication of the state of the labour market in the June quarter. The releases should shed light on whether rising employment intentions are realised following on from stronger-than-anticipated economic growth.

The industries that drove the strength in the March quarter GDP, services and manufacturing, both showed improvement in output in the June quarter QSBO, suggesting that they will continue to drive growth in future GDP. The results for these two industries are supported by the BusinessNZ BNZ PSI and Performance of Manufacturing Index, which were both in expansionary territory over the June quarter. The new orders components of both suggest continuing growth.

One-off events will boost growth in the second half of 2011 and into 2012. The Rugby World Cup, which will span the September and December quarters of 2011 is expected to increase growth by around 0.3% points, mainly through a boost in services exports as 85,000 overseas tourists are anticipated to arrive for the event.

Rebuilding from the Canterbury earthquakes is assumed to step up in 2012. The Treasury estimated that the earthquakes caused a combined $15 billion worth of damage. Rebuilding of these damaged items will provide a significant boost to the economy, especially the construction industry. Outside of earthquake rebuilding the construction industry is struggling, with output falling 6.2% in the last three quarters. An increase in investment intentions in the QSBO was driven by expectations of rebuilding in Canterbury, with the rest of the country downbeat.

Inflationary pressures relatively subdued...

Economy-wide price increases were more muted than anticipated in the March quarter, mainly due to impacts from the external sector. A 4.6% rise in import prices more than offset a 3.9% rise in export prices. The surging import prices were driven by mineral fuel price rises, due to higher global oil prices. This meant that the overall GDP price deflator only rose 0.1% in the quarter. Domestic inflation was slightly stronger with the private consumption deflator rising 0.9%. The surprisingly contained GDP deflator took annual nominal GDP growth to 5.4% (boosted by the October 2010 GST rate rise), which was very close to our *Budget* forecast of 5.3%, as stronger output was offset by weaker prices. Core crown tax revenue is also close to our *Budget* forecast and a positive variance of 0.5% in the 11 months to May indicates nominal GDP is likely to remain close to forecast in the June quarter.

... despite high headline CPI inflation

The consumers price index (CPI) rose 1.0% in the June quarter, taking annual inflation to 5.3%. The outturn was above the market pick (0.8% qpc) but the same as our *Budget* forecast. An estimated 2.0% point contribution from the GST rate rise meant that annual inflation was the highest in 21 years (when there was also a GST rate rise).

The majority of the high inflation rate is the result of internationally-generated price increases and government-related charges. The main impact of rising commodity prices has been on petrol and food prices, rising 18.1% and 7.0% respectively in the year to June. Rising commodity prices have resulted from strong emerging market demand and weather-related supply disruptions. High fuel prices have begun to flow through to other prices in the economy, demonstrated by international and domestic air transport prices rising more than 6% in the June quarter.

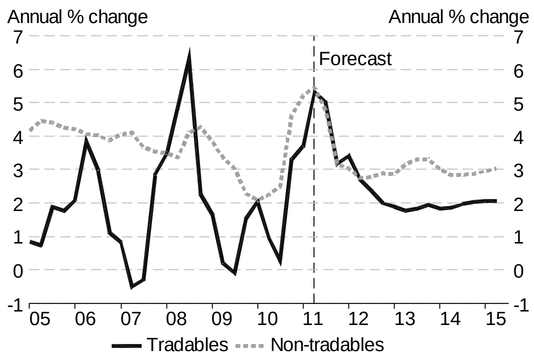
In addition to the GST rate rise, ACC levy increases, tobacco excise rate hikes and the implementation of the emissions trading scheme have all boosted the annual inflation rate. The CPI less the food group, household energy subgroup and vehicle fuels (CPI ex food and energy) is a measure of core inflation that removes most of the impact of internationally generated commodity price rises. The CPI ex food and energy rose 3.6% in the year to June. Removing the impact of the government-related charges gives a measure of underlying annual inflation of 1.4%, below the mid-point of the Reserve Bank's 1-3% target.

Underlying inflation beginning to pick up...

CPI inflation ex food and energy has picked up in recent quarters, rising from 3.1% in December to 3.6% in June. Other measures of core inflation, including weighted median and trimmed means (which strip out items with large increases and decreases) are also starting to rise.

The stronger-than-expected economic recovery will result in less spare capacity and put pressure on non-tradables inflation (items not exposed to international competition, Figure 4). The June quarter QSBO showed rising business pricing intentions as firms try to recover recently falling profit margins, which resulted from rising input costs and a subdued domestic trading environment not allowing firms to pass on these cost rises. Inflation expectations are currently high, in part due to the high headline rate of inflation (people use current inflation as a base for inflation expectations). These factors are expected to result in underlying domestically-produced inflation picking up.

Figure 4 – Tradables and non-tradables inflation



Source: Statistics New Zealand, Treasury

There will likely be some offset from lower tradables inflation (internationally influenced). The NZD has recently risen to a three-year high on a trade-weighted basis. This rising NZD will result in cheaper imported products which will be passed onto consumers. The result is that the overall inflation picture is similar to what we forecast in the *Budget,* despite a stronger economy and expected change in the composition of inflation.

...but headline inflation will likely fall back...

The impact of one-off increases in government charges will begin to fade in the September quarter, culminating in the main impact of the GST rate rise coming out of the calculation in the December quarter, meaning that inflation is expected to have peaked in the June quarter. Food prices appear to have peaked and oil prices have come back from recent highs. The result will be the effects of food and petrol price increases will begin to drop out of the inflation calculation and it will likely drop back into the Reserve Bank target band around the middle of 2012.

...with risks to inflation remaining further out

Rebuilding in Canterbury as a result of the earthquakes will put pressure on inflation, especially in the construction industry. In order to get the building done in a timely manner, higher wages and material prices may need to be paid. Also, inflation expectations have increased steadily over the past year, with surveys showing expectations around 3%, which could prove problematic if these expectations remain elevated. The Reserve Bank has assumed that high inflation expectations are temporary and this could eventuate as inflation expectations quite often follow petrol prices and headline inflation; petrol prices have fallen recently and headline inflation is expected to begin falling. The Bank signalled in its 28 July OCR review that the economy's stronger recovery will result in the need to remove the 50bps insurance cut that followed the February earthquake, in the near future. Further increases will be subject to the strength in the NZD.

Increasing GDP growth also suggests that spare capacity is starting to fade, shown by a rise in capacity utilisation in the July NBBO. These factors pose upside risks to inflation and could see it settle near the top of the Reserve Bank's target in the medium term.

Sovereign debt a focus for markets...

Sovereign debt was a major theme in July, with a new package agreed to address the sovereign debt issues in the euro area and ongoing negotiations on raising the US debt ceiling.

... with positive developments for Greece ...

The new package included a further €109 billion bailout package for Greece, as well as private sector involvement of an estimated €37 billion. The "voluntary private sector involvement" will likely cause ratings agencies to move Greece to a selective default, but not trigger insurance contracts on Greek debt. The package also included further funding and power for the European Financial Stability Fund (EFSF). The purpose of this was to add a precautionary function; the bailout fund can intervene by buying government debt, recapitalising banks and can purchase bonds on secondary markets. The markets have seen the package as a positive development; yields on Greek debt have fallen, despite the implications of a selective default.

... but lack of progress in the US situation

The US debt ceiling negotiations have since taken the focus of markets. Both Standard & Poor's and Moody's have expressed their concerns, putting the US on review for a possible credit downgrade. Even if a deal to raise the debt ceiling is reached, a downgrade is still possible if a credible longer-term deficit reduction plan is not agreed upon. We expect a last-minute deal to raise the debt ceiling will be reached, but are less certain on the outlook for reducing the deficit in future. If the debt ceiling is not raised, the US government will be not be able to issue new debt and may default on existing obligations as they fall due. A US default would have widespread consequences, not only for the US, but for the global economy. No agreement had been reached when we finalised.

Recovery sluggish in the US...

The situation is compounded by weaker economic outturns in July. The US recovery continues to be sluggish, albeit with the outlook on production slightly more positive. In contrast to falling PMIs around the world, the US equivalent unexpectedly rose in June. Motor vehicle production has been disrupted since the Japanese disasters in March due to supply-chain disruptions; these factors are unwinding and could provide a boost to September quarter growth.

The labour market remains especially weak, with June non-farm employment increasing only 18,000; the unemployment rate has risen from 8.8% in March to 9.2% in June. The housing market remains lacklustre with distressed sales keeping prices down. June quarter growth is expected to remain subdued, at around 0.5%.

... and a softer outlook for Australia...

Australia's growth outlook for 2011 was recently downgraded by several forecasters. After a weather-induced contraction in the March quarter, indicators have failed to show a strong bounce-back so far. Further difficulties have limited coal exports during the June quarter and the recovery may be pushed back into the September quarter.

Australia's growth is seen as "two-speed": the mining sector is growing strongly but the household sector continues to consolidate. This consolidation has been evident since the global financial crisis through a higher saving rate as households bolster their financial position and rein in spending relative to income growth.

Other factors which may have had an influence are the negative confidence effects of the natural disasters earlier in the year, mortgage interest rate increases and a weakening global outlook. The high value of the Australian dollar is acting as a brake on manufacturing and services exports, but the medium-term outlook remains positive with high commodity prices, increasing investment and a strong labour market.

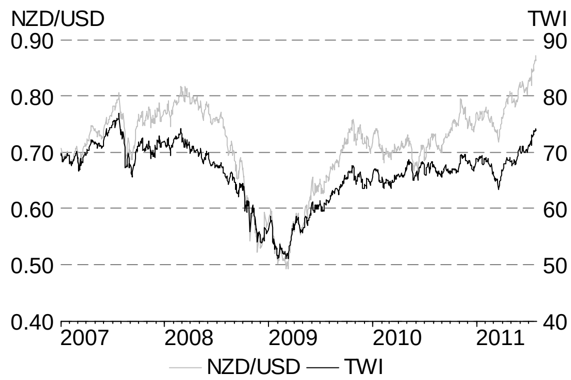
... but China still growing strongly

The outlook for Australia is closely linked to China. June quarter growth was slightly above market expectation at 9.5% but in line with our expectation of moderating growth. While some details within the headline figure show a positive picture, more recent indicators show growth may be slowing. Inflation is still a concern as consumer prices were up 6.4% in the year to June. We expect the authorities to continue to tighten monetary conditions, allowing for a soft landing.

New Zealand dollar continues strengthening

One of the main topics of discussion during July was the appreciating NZD. It has seen new post-float highs against the USD and GBP, and near-highs against the EUR. The TWI is still below its 2007 record highs of around 77 (Figure 5).

Figure 5 – NZD exchange rates



Source: Reserve Bank of New Zealand

Several factors have led to these recent highs. Positive risk sentiment arising from the euro area debt package has boosted the NZD, while concerns about the US debt situation have weakened the USD. Higher-than-expected GDP and CPI outturns for New Zealand have brought forward expectations of an RBNZ rate hike, putting upwards pressure on the NZD. The recent downgrade of Australia's 2011 prospects has also contributed to the NZD's stronger cross rate against the AUD. The NZD may also be supported by greater diversification in foreign governments' debt; IMF data show the share of government reserves held in "other currencies" (non-majors) has increased significantly over the last few years. The NZD has been seen as more of a "good risk" recently; the implications of this are that an increase in risk aversion no longer automatically depreciates the currency. Reinsurance inflows may also be supporting the NZD, although to what extent is difficult to evaluate.

The higher NZD means that non-commodity exporters will continue to be under pressure, although those exporting to Australia less so. There will be implications for NZ's growth outlook if the NZD remains elevated, with the ability of exports to lead the recovery under threat. Consumers, however, will benefit from cheaper imports, which could boost household spending volumes. The stronger-than-expected underlying economy, shown by the December and March quarters GDP results, should offset any negatives associated with the high NZD and ensure that annual growth continues to pick up over 2011.

Special Topic: The internet, the downturn and me: 4 reasons why households and firms can afford a smile

The internet is coming of age

The internet has been much-hyped for its potential to drive economic growth. From e-commerce to the knowledge economy, the internet has promised the world while delivering mixed results. This promise was best punctuated by the dot-com bubble of 2000. Investors ignored fundamentals like price-to-earnings ratios in the belief that technological advancements would lead to profits later. The profits, for the most part, never came.

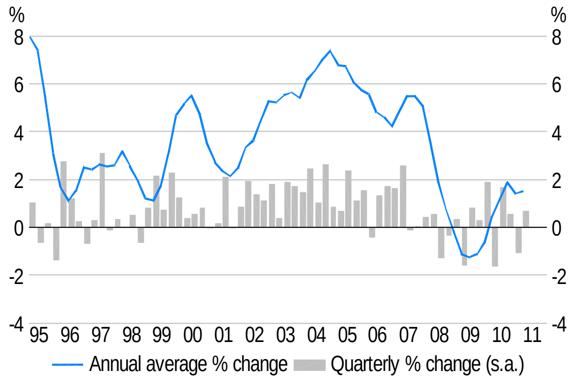
We argue that, despite the disappointments to date, the internet is coming of age economically – *well actually it may have already done so*. So what is different?

We offer *4 reasons* as why the internet over the next few years will drive productivity and economic growth, while at the same time contributing to the battle with inflation and ultimately allowing higher real consumption. We also offer *4 implications* for the wider economy.

Reason 1 – we all love a bargain

The internet is unleashing its power at just the right time – during a retail downturn. One might argue that these features may have happened anyway. Nonetheless, we all love a bargain. And when do consumers love bargains the most? Answer: during a downturn. Figure 6 below shows the recession in real core retail sales from 2007 to 2009 followed by the continued low growth up to the present.

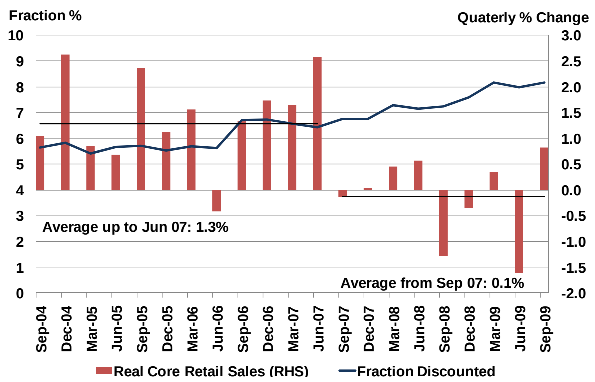
Figure 6 – Real Core Retail Sales Growth



Source: Statistics New Zealand

A recent study by economists at the Reserve Bank and Motu showed that the fraction of discounting increased during the recent (retail) downturn (Figure 7). So where are the best discounts or at least where are the discounts easiest to find? Answer: the internet.

Figure 7 – Fraction of all CPI groups discounted and Real Core Retail Sales



Source: Statistics New Zealand, Motu, RBNZ

The advent of sites like *priceme* and *price spy*, naming just a couple, gives consumers the ability to compare prices in one place easily and quickly. Consumers like this ability. A survey by Macquarie Bank showed that the number one reason for online shopping was price (55%), more than double the next reason (convenience at 25%). While this survey was conducted in Australia, one can assume that New Zealand online shoppers share similar preferences.

Reason 2 – it's as easy as 1-2-3

The internet has broadened its function from high-powered user-friendly library to include economic match-maker. Economically speaking, this addition means lower search costs for both firms and households. While in lay terms, this translates to: it's easy to find what you and I want to buy and it's easy for businesses to access the customers they are targeting.

Compare pamphlets to *grabone*. Retailers deliver pamphlets to an entire neighbourhood, regardless of interest in the product or service advertised. It's costly, requiring printing, distribution and then delivery. In summary, pamphlets are hit and miss with a majority ending up in the recycling bin. *Grabone* offers, on the other hand, are sent out via email subscription, *twitter* or *facebook*. The marginal cost is close to zero. Importantly, *grabone* can target customers. With information on your interests, preferences and recent purchases, online firms can better predict those interested in a deal and market directly to them.

Reason 3 –it's growing fast with room to grow

In the March 2011 quarter, the US Census Bureau reported that e-commerce sales grew 17.5% from March 2010, over double the 8.6% growth in total retail sales. And while e-commerce grew from 1.3% to 4.5% over the nine years to March 2011, the 4.5% share indicates that e-commerce has a lot more room to grow. While the equivalent New Zealand data are not available, a 4.5% share would represent $2.9 billion out of total retail sales of $65.5 billion.

Reason 4 – the sum of reasons 1, 2 and 3

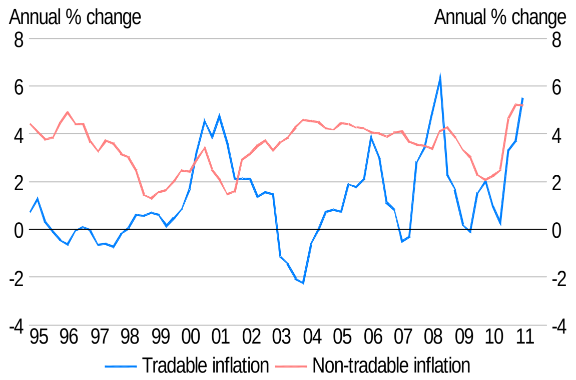
The last reason is the interaction between the first three reasons. Consumers' ability to find bargains will drive a competitive response among firms. Also, with markets for many goods and services borderless, many firms will compete globally and on an increasingly large scale. With more competitors, firms will need to innovate to increase their productivity so they can lower their costs and remain competitive.

As a result, someone, somewhere on the internet is bound to be having a sale. And with consumers' ability to find bargains, we argue that the preference for bargain hunting will persist as the economy improves. In other words, Briscoes will not be the only place running regular sales.

Implication 1 – cheaper for longer

Following on from reason 4, online-induced competition is likely to lead to lower inflation over time. The gap between tradable and non-tradable inflation demonstrates where competition has contributed to lower inflation. Tradable inflation has averaged 1.3% since 1995 and non-tradable inflation 3.4% (Figure 8), while total inflation has averaged 2.3%.

Figure 8 – Tradable and non-tradables inflation



Source: Statistics New Zealand

Tradable inflation covers goods and services where domestic firms compete globally, eg. clothing and apparel, while non-tradable inflation covers firms only competing domestically, eg. hair cuts and electricity supply. Roughly half of the CPI basket of goods and services are tradable and half non-tradable.

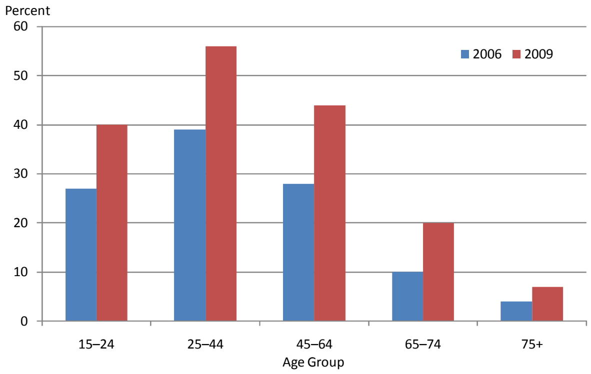
We argue that more of the CPI basket will become tradable or at least more competitive. Take the household energy subgroup of CPI with a weighting of around 4%. The study by Reserve Bank and Motu economists found that the average discount for this group was zero, indicating a less competitive sector. However, this study covered the period up to 2009, before the advent of *Powershop* and *WhatsMyNumber*. These sites allow households to compare power prices, switch suppliers and or use multiple suppliers. In turn, this ability should spur more competition between power companies.

If, for example, these and other internet developments increased competition so that the tradable non-tradable split increased to 60-40, then the long run inflation rate could potentially fall by up to 0.3 percentage points to 2.1%. Ultimately, lower inflation will allow households to buy more and thus be better off or, economically speaking, allow higher real consumption.

Implication 2 – more bargains for some, less for others

Like many areas of growth, some groups will benefit more than others. In this case, the internet-savvy will grab more of the benefits. While data on internet literacy is hard to come by, we do have data on online purchases by age.

Figure 9 – Individuals Who Made Online Purchases Over Last 12 Months



Source: Statistics New Zealand

Figure 9 shows that the highest percentage of online purchases were made by the 25-44 age group, followed by the 45-64 group, the 15-24 group and then the two groups over 65. If you equate the number of online purchases to internet-savviness, then the groups making more online purchases stand to gain more.

While the less-internet-savvy will gain less, they will benefit as traditional retailers strive to remain competitive. Interestingly, the 15-24 group's 3rd ranking is unlikely to be due to low internet skills, but rather their lower purchasing power and also because many may not possess a credit card for online purchases. Visa debit cards may mean this last factor is less of a constraint in future surveys.

Implication 3 – hello 3D glasses, good-bye video rentals

The face of store retail is changing. Trends already evident in shopping malls indicate that growth sectors will focus on experiences and be social and or service-based, eg. 3D movie theatres, cafes and spas. On the flip side, sunset sectors will include products with low-differentiation, be transportable and/or have obsolete technology eg. book and music stores, video and DVD hire, and clothing. In general, stores selling goods and services with a difference that is not easily replicated and or transported via the internet will remain competitive.

Accordingly, many traditional retail firms will have to adapt; many will struggle and some will go out of business. This will also lead to some structural unemployment in this segment of retail and workers will need to retrain in many cases.

Implication 4 – can we measure and tax it?

The benefits of the internet are difficult to measure and current statistical measures may not fully capture the gains discussed above. Statistics NZ measures online prices for such things as domestic airfares and digital download, uses a mix of online and store prices for other things such as contact lenses and mobile phones, leaving other online prices largely unmeasured. While Statistics NZ updates methodologies from time to time, the growth and development of online retail is likely to outpace these updates, meaning that the measured benefits are likely to lag the actual benefits to households.

International online purchases are exempt from GST and duty (depending on the item) up to $400, providing an additional incentive to purchase online. As a result, domestic firms – both online and store-based – are at some disadvantage. Moreover, as international online purchases grow the government will increasingly forgo revenue.

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New Zealand Key Economic Data

29 July 2011

Quarterly Indicators

		2009Q4	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2
Gross Domestic Product (GDP)								
Real production GDP	qtr % chg[1]	0.9	0.6	0.2	-0.1	0.5	0.8	...
	ann ave % chg	-2.0	-0.7	0.5	1.4	1.7	1.5	...
Real private consumption	qtr % chg[1]	1.0	0.5	0.4	0.4	0.3	0.4	...
	ann ave % chg	-0.7	0.4	1.4	2.0	2.2	1.9	...
Real public consumption	qtr % chg[1]	0.7	1.5	0.6	0.0	1.4	1.2	...
	ann ave % chg	0.6	0.2	1.1	1.7	2.7	3.1	...
Real residential investment	qtr % chg[1]	6.2	-1.6	11.0	-6.9	-7.0	-2.1	...
	ann ave % chg	-18.1	-13.0	-4.3	3.5	2.8	2.3	...
Real non-residential investment	qtr % chg[1]	-1.1	0.3	4.2	0.1	8.2	-1.0	...
	ann ave % chg	-8.1	-8.3	-7.1	-3.8	2.1	7.0	...
Export volumes	qtr % chg[1]	-0.6	1.4	0.3	-0.9	2.0	0.8	...
	ann ave % chg	1.7	4.6	4.7	3.7	3.0	2.0	...
Import volumes	qtr % chg[1]	4.5	2.8	-0.2	3.9	6.4	-2.4	...
	ann ave % chg	-14.6	-9.4	-1.8	5.6	10.1	10.4	...
Nominal GDP - expenditure basis	ann ave % chg	0.6	1.1	2.0	3.0	4.8	5.4	...
Real GDP per capita	ann ave % chg	-3.1	-1.8	-0.7	0.2	0.4	0.4	...
Real Gross National Disposable Income	ann ave % chg	-1.5	0.5	0.9	0.4	2.2	1.9	...
External Trade								
Current account balance (annual)	NZ$ millions	-5204	-4458	-5707	-7749	-8044	-8300	...
	% of GDP	-2.8	-2.4	-3.0	-4.1	-4.1	-4.2	...
Investment income balance (annual)	NZ$ millions	-7930	-7627	-9026	-10692	-10683	-10666	...
Merchandise terms of trade	qtr % chg	5.8	6.1	2.0	3.0	0.8	0.9	...
	ann % chg	-8.2	0.1	12.7	17.9	12.3	6.8	...
Prices								
CPI inflation	qtr % chg	-0.2	0.4	0.2	1.1	2.3	0.8	1.0
	ann % chg	2.0	2.0	1.7	1.5	4.0	4.5	5.3
Tradable inflation	ann % chg	1.5	2.0	1.0	0.3	3.3	3.7	5.5
Non-tradable inflation	ann % chg	2.3	2.1	2.2	2.5	4.6	5.2	5.2
GDP deflator	ann % chg	-1.5	-0.1	1.8	2.8	5.7	4.3	...
Consumption deflator	ann % chg	1.2	0.8	0.5	0.8	2.7	3.1	...
Labour Market								
Employment (HLFS)	qtr % chg[1]	0.1	0.8	-0.2	1.1	-0.4	1.4	...
	ann % chg[1]	-2.4	-0.1	0.0	1.9	1.3	1.8	...
Unemployment rate	%[1]	7.0	6.1	6.9	6.4	6.7	6.6	...
Participation rate	%[1]	68.1	68.0	68.1	68.2	67.9	68.7	...
LCI salary & wage rates - total (adjusted)[5]	qtr % chg	0.4	0.3	0.4	0.5	0.5	0.4	...
	ann % chg	1.8	1.5	1.6	1.6	1.7	1.8	...
QES average hourly earnings - total[5]	qtr % chg	-0.2	-0.4	0.7	1.0	0.5	0.4	...
	ann % chg	2.8	1.0	1.0	1.1	1.8	2.6	...
Labour productivity[6]	ann ave % chg	0.1	2.1	2.0	1.3	0.2	-0.3	...
Retail Sales								
Core retail sales volume	qtr % chg[1]	0.6	0.1	0.6	-0.1	0.0	0.7	...
	ann % chg	2.2	3.0	2.6	1.5	0.3	1.4	...
Total retail sales volume	qtr % chg[1]	1.2	0.4	0.5	-0.4	-0.4	0.9	...
	ann % chg	0.4	3.2	3.4	1.9	-0.1	0.8	...
Confidence Indicators/Surveys								
WMM - consumer confidence[3]	Index	117	115	119	114	108	98	112
QSBO - general business situation[4]	net %	30.7	21.9	17.5	6.4	8.1	-26.8	26.6
QSBO - own activity outlook[4]	net %	10.8	14.5	11.3	9.5	11.4	-1.6	18.5

Monthly Indicators

		2011M 1	2011M 2	2011M 3	2011M 4	2011M 5	2011M 6	2011M 7
External Sector								
Merchandise trade - exports	mth % chg[1]	2.9	4.3	0.5	6.1	-6.0	-0.1	...
	ann % chg[1]	4.7	16.3	13.2	18.0	10.2	4.3	...
Merchandise trade - imports	mth % chg[1]	-1.4	6.5	-1.2	-6.7	11.4	-6.5	...
	ann % chg[1]	15.3	22.5	15.7	7.7	18.7	4.5	...
Merchandise trade balance (12 month total)	NZ$ million	909	765	741	1230	1012	1021	...
Visitor arrivals	number[1]	218220	208610	191960	206780	205670	195100	...
Visitor departures	number[1]	220700	212200	200990	201100	215390	198550	...
Housing								
Dwelling consents - residential	mth % chg[1]	9.2	-9.7	2.5	-1.2	2.3	-1.4	...
	ann % chg[1]	-14.9	-28.8	-26.1	-32.1	-21.9	-25.7	...
House sales - dwellings	mth % chg[1]	-6.8	2.8	5.1	1.0	10.3	-0.6	...
	ann % chg[1]	-9.9	-10.0	-5.0	-5.2	10.8	14.0	...
REINZ - house price index	mth % chg	-2.6	2.3	0.5	1.1	-1.8	1.3	...
	ann % chg	-2.6	-0.7	-1.8	-0.4	-0.7	0.0	...
Private Consumption								
Electronic card transactions - total retail	mth % chg[1]	2.4	-0.2	1.4	1.4	-0.7	1.2	...
	ann % chg	5.7	6.2	6.6	10.0	6.8	9.0	...
New car registrations	mth % chg[1]	0.9	-1.4	-0.5	-5.6	3.2	-2.2	...
	ann % chg	6.8	2.8	-1.0	-10.5	-3.7	-9.5	...
Migration								
Permanent & long-term arrivals	number[1]	7000	6920	7060	7090	6900	6840	...
Permanent & long-term departures	number[1]	6590	6490	7600	7230	7240	7180	...
Net PLT migration (12 month total)	number	8689	8249	6554	5508	4625	3867	...
Commodity Prices								
Brent oil price	US$/Barrel	96.95	104.24	114.92	123.33	114.93	114.37	...
WTI oil price	US$/Barrel	89.52	89.41	102.94	110.15	101.30	96.29	...
ANZ NZ commodity price index	mth % chg	2.8	2.9	8.1	-3.9	-0.7	-3.3	...
	ann % chg	9.9	10.1	18.4	9.8	7.6	4.9	...
ANZ world commodity price index	mth % chg	4.3	2.7	4.7	1.6	0.4	-1.2	...
	ann % chg	16.3	20.3	23.5	19.8	19.6	20.6	...
Financial Markets								
NZD/USD	$[2]	0.7653	0.7623	0.7408	0.7859	0.7959	0.8150	...
NZD/AUD	$[2]	0.7692	0.7565	0.7333	0.7450	0.7447	0.7686	...
Trade weighted index (TWI)	June 1979 = 100[2]	68.70	67.80	65.20	68.20	68.70	70.30	...
Official cash rate (OCR)	%	3.00	3.00	2.50	2.50	2.50	2.50	...
90 day bank bill rate	%[2]	3.19	3.13	2.69	2.65	2.66	2.65	...
10 year govt bond rate	%[2]	5.61	5.56	5.58	5.70	5.23	5.04	...
Confidence Indicators/Surveys								
National Bank - business confidence	net %	42.4	34.5	-8.7	14.2	38.3	46.5	47.6
National Bank - activity outlook	net %	41.3	36.6	14.7	29.5	39.7	38.7	43.7
ANZ-Roy Morgan - consumer confidence	net %	117.1	108.1	101.4	101.4	103.3	112.5	109.4

qtr % chg — quarterly percent change
mth % chg — monthly percent change
ann % chg — annual percent change
ann ave % chg — annual average percent change

1 Seasonally adjusted
2 Average (11am)
3 Westpac McDermott Miller
4 Quarterly Survey of Business Opinion
5 Ordinary time
6 Production GDP divided by HLFS hours worked

Sources: Statistics New Zealand, Reserve Bank of New Zealand, ANZ National Bank of New Zealand, NZIER, Datastream, Westpac McDermott Miller