Monthly Economic Indicators

THE TREASURY
Kaitohutohu Kaupapa Rawa

June 2015

Executive Summary

- **March quarter GDP was weaker than expected and more recent indicators point to slower growth over the coming year, although underlying growth drivers remain intact**
- **The Reserve Bank reduced the Official Cash Rate to 3.25% on lower terms of trade and a weakening inflation outlook**
- **Risks associated with Greece continue to build while international developments elsewhere were generally positive**

Key economic data releases over the past month point to a slower growth path over the coming year. Real GDP growth was low in the March quarter, below Treasury and market expectations. This was partly as a result of temporary factors such as the drought which should at least partially unwind in coming quarters. However, based on more recent indicators, private consumption and residential investment may make less of a positive contribution to growth over the year ahead than expected in the Budget forecasts. That said, on an annual average basis GDP growth remains solid supported by high migration, healthy investment activity and solid labour income growth. Nominal GDP growth in the March quarter was stronger than anticipated on higher-than-expected terms of trade.

The current account deficit was smaller than expected reflecting the higher terms of trade in the March quarter. However, ongoing falls in dairy prices and higher oil prices mean the terms of trade are likely to resume their downward trend over the coming quarters. The current account deficit is expected to widen further over the coming year.

The Reserve Bank reduced the Official Cash Rate (OCR) from 3.50% to 3.25% on lower terms of trade and a weakening inflation outlook. The Reserve Bank maintains an easing bias, dependent on data developments, and market analysts expect the OCR to fall further this year.

The New Zealand dollar depreciated over the course of the month in response to the OCR reduction, weaker than expected domestic data outturns, expected US monetary policy tightening and a rise in investor risk aversion. Together with the fall in interest rates, this should act to offset some of the reduction in national income from the falling terms of trade. As a result, the Reserve Bank MPS and Treasury BEFU forecasts for real and nominal GDP growth are not significantly different (although the composition of growth differs).

Greece remains a concern, as the country failed to make its debt payment to the IMF due on 30 June, its recent bailout expired and its banks closed to limit the withdrawal of deposits. Economic developments in advanced economies generally have been more positive, contributing to an upward trend in global bond yields and inflation. Closer to home, recent Australian activity has been more upbeat. However, China eased monetary policy further on a weaker outlook.

Overall, these recent developments highlight the risks of weaker economic growth than forecast in the *Budget Economic and Fiscal Update* (BEFU) which was finalised on 10 April 2015 and released on 21 May 2015. Data releases in coming months will provide further indication of how the combination of factors affecting the economy will unfold.

This month's special topic examines recent developments in international tourism and its impact on New Zealand's travel services exports.

New Zealand Government

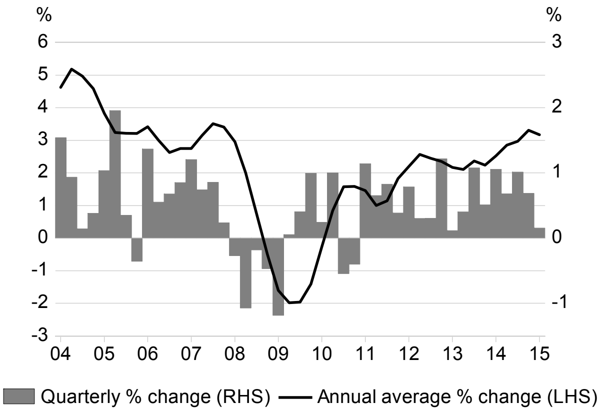
Analysis

Economic developments over the month of June point to a slightly weaker outlook than in the *Budget Economic and Fiscal Update* (BEFU). That said, the underlying drivers of growth – high migration, healthy construction activity and solid labour income growth – remain intact.

GDP growth was unexpectedly weak in the March quarter...

The main data releases in June were the March quarter GDP and Balance of Payments figures. Real production GDP rose 0.2% in the March quarter, well below market and Treasury expectations (Figure 1). Despite the weak quarter, annual average growth remained solid at 3.2%.

Figure 1: Real production GDP



Source: Statistics NZ

Real expenditure GDP growth was even weaker than production GDP at 0.1%. In contrast, nominal GDP was relatively strong at 1.0%, above BEFU (0.6%), mostly on account of the SNA terms of trade which rose 1.7%. On an annual average basis nominal GDP growth was 3.9%.

...largely owing to weak primary industries...

Drought conditions led to a decline in dairy production, while low oil prices internationally contributed to reduced oil and gas exploration and extraction. Together this saw primary industries declining 2.9% in the quarter, subtracting 0.2 percentage points from GDP growth.

Activity in goods-producing industries increased 0.6% led by construction, while the drought was a factor in lower manufacturing production. Treasury had expected a larger increase in construction activity, particularly in the residential sector. Altogether, goods-producing industries contributed 0.2 percentage points to growth.

Services industries' activity increased by 0.7%, down from 0.9% in the previous quarter, and contributed 0.5 percentage points to growth. Treasury had not expected growth in this sector would slow. Retail trade and accommodation was the largest driver of growth, owing in part to a strong quarter for tourism. Increased tourism activity was also evident in services exports, which increased 3.6% and followed a 7.7% increase in the previous quarter. (See the special topic for further analysis of travel services exports). Professional services were the other major contributor to services growth.

...and business outlook indicators suggest growth is moderating

Business confidence in the manufacturing and construction sectors was weak in the June ANZ Business Outlook (ANZBO) survey. This took the total business confidence measure into negative territory (-2.3) for the first time since the Canterbury earthquake in February 2011. That said, the more important activity outlook measure was still solid at 23.6 and most indicators were positive at the aggregate level, suggesting that growth is moderating rather that reversing. Although agricultural sector confidence was low (-28.9), pastoral conditions improved over the June quarter as drought conditions eased, and milk production recovered.

The Quarterly Survey of Business Opinion released in early July will provide a further steer on the business outlook.

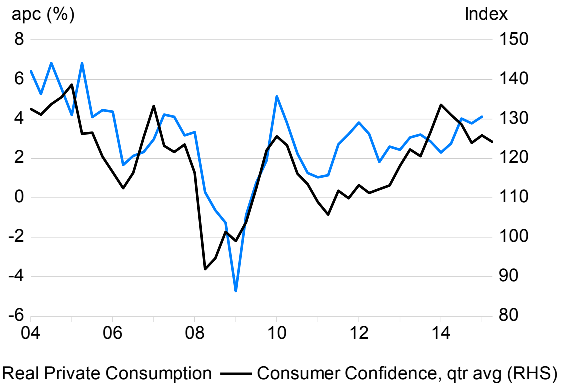
Private consumption growth has softened...

Turning to the expenditure GDP breakdown, private consumption grew 0.7% in the quarter, slightly below our expectations in BEFU (0.9%). Growth mostly came from increased expenditure on durable goods, consistent with increased imports of consumption goods and passenger cars. Services expenditure was surprisingly subdued given large increases in hospitality, cultural and recreational spending, which likely reflects a greater share of expenditure being attributed to travel services exports (chiefly international tourism).

Indicators since March have also softened. Seasonally adjusted electronic card transaction values fell 1.2% in April, with falls in both core retail and services expenditure, and the 1.4% gain in May only just offset this. Car registrations also declined in April and May.

Consumer confidence has also eased since March (Figure 2). The June ANZ-Roy Morgan Consumer Confidence survey showed declining confidence in both the current and future conditions indicators. The overall index slipped 4 points in June to 119.9, its lowest level in nearly two years, although it remains above its long-term average. The June Westpac McDermott Miller Consumer Confidence and Employment Confidence surveys also declined.

Figure 2: Consumption indicators



Sources: Statistics NZ, ANZ-Roy Morgan

Together, the March quarter GDP outturn and subsequent indicators suggest private consumption may be easing from its strong growth in 2014. That said, lower interest rates and increased household credit growth (which expanded 5.5% versus a year ago in May), continuing strong migration and solid labour income growth should sustain private consumption growth, albeit at a slower pace.

...as has residential investment

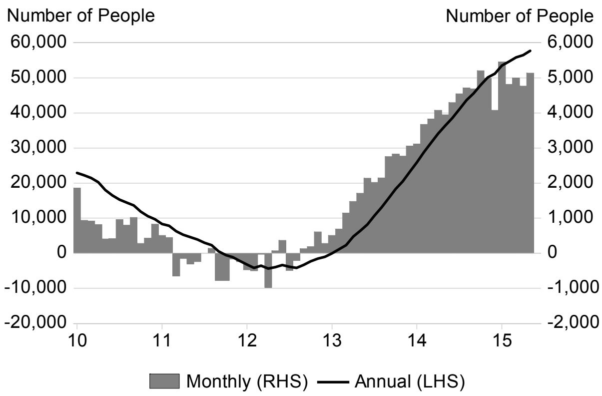
Growth in residential investment also eased in the March quarter, slowing from 4.9% growth in the December quarter to 0.6% in March. The seasonally adjusted number of housing consents issued fell in the March quarter and the 2.4% increase in May consents only just offset the 1.8% decline in April. Taken together this suggests the pipeline of residential work for the next few months may have eased. While weaker than BEFU, residential investment developments may reflect more of a change in the phasing of growth, with moderate growth for longer rather than the early peak and tail-off previously anticipated.

While residential investment growth has slowed, house price growth has not. REINZ data for May showed the seasonally adjusted national median house price increased 1.1% from April, to be 7.0% higher than a year ago. However, the housing market continues to reflect divergent trends. Auckland median house prices increased 2.2% in the month and 19.9% on a year ago. In contrast, the New Zealand median price excluding Auckland fell in the month (-1.1%) and was only modestly higher than a year ago (+2.6%). The QV house price index showed similar trends. The recent changes to LVR restrictions and government policy are unlikely to have had a material impact on (Auckland) house price growth to date.

Migration remains strong

International migration data showed that the seasonally adjusted net inflow was 5,140 in May and reached 57,730 on an annual basis (Figure 3). Net migration continues to be driven by a combination of more arrivals and fewer departures. The student inflows that had been the largest source of growth in arrivals appear to be slowing and possibly peaking. However, growth in migrants with work visas remains strong. For the second month in a row (and otherwise the first time since 1991) there was a net positive inflow from Australia in seasonally adjusted terms.

Figure 3: Net migration



Source: Statistics NZ

The outturn is slightly above the peak Treasury assumed in the BEFU and continued monthly net inflows at these levels could see annual migration reach 60,000 by September. If this were to materialise, it would pose some upside risk to the BEFU forecasts of private consumption and house price growth.

Business investment was weaker than anticipated

Business investment fell sharply in the March quarter, dropping 2.8% in the quarter, weaker than anticipated. The fall was driven by an 11.9% fall in intangible investment (partly related to the pull-back in oil exploration noted earlier) and 10.6% declines in each of plant, machinery and equipment, and transport equipment investment. The latter two results are somewhat at odds with the high level of capital goods imports in the quarter, although transport equipment investment had been running at elevated levels in the second half of 2014 due to several large aircraft arrivals (part of Air New Zealand's fleet upgrade).

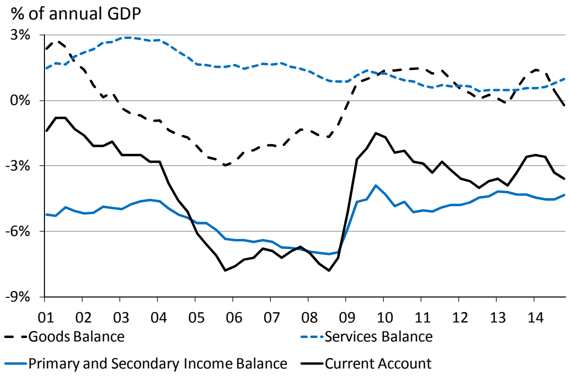
Non-residential building and other construction investment held up better in the March quarter, with 2.2% and 7.2% increases respectively. Increasing values of non-residential building consents point to growth continuing this year. The quarter-to-date average value of non-residential building and non-building construction permits is 8.5% higher than the March quarter average and 17.0% higher than the June 2014 quarter average.

The ANZBO investment intentions measure eased to 11.7 (from 17.9) in June but was positive for all industry groups except agriculture. Together with the consents data and steady capital goods imports in April and May, this points to business investment recovering somewhat in the June quarter.

The widening of the current account deficit was at the low end of expectations...

The annual current account deficit widened from 3.3% of nominal GDP in December to 3.6% in March (Figure 4). This was at the low end of market expectations. The main surprise was a narrowing of the primary income (investment income) deficit from 4.3% to 4.1% of GDP.

Figure 4: Current account



Source: Statistics NZ

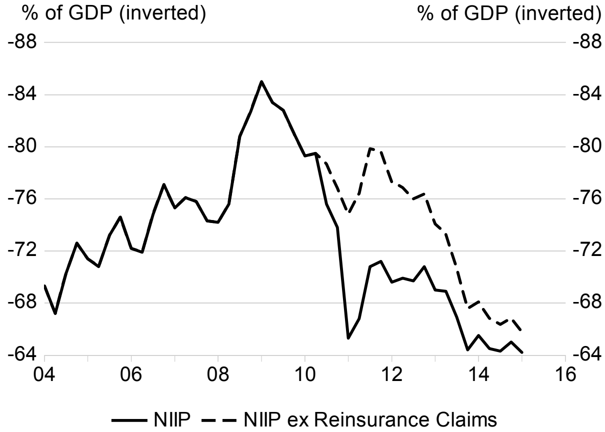
As alluded to earlier in the consumption section, travel services export values were strong in the March quarter, growing by 3.8% from an already high level in the December quarter. This was the main driver of the widening of the annual services surplus to 1.0% of GDP (from 0.8% in December).

Some of the strength in services exports was expected to be temporary, reflecting factors such as the Cricket World Cup and the longer than usual Chinese New Year holiday in February. However, visitor arrivals have remained solid in April and May (allowing for the usual seasonal downturn). A positive surprise here may help to offset some of the widening in the goods deficit (see below) and slower consumption growth.

The annual goods balance moved from a surplus of $1.1 billion (0.4% of GDP) in December to a deficit of $0.5 billion (0.2%) in March. Weaker prices drove the 1.2% fall in nominal goods exports, with real goods exports increasing by 1.0% in the quarter. However, import prices were even weaker (partly reflecting the sharp decline in oil prices), leading to nominal goods imports falling 3.6% while real goods imports increased by 0.9%. Together this saw the SNA goods terms of trade unexpectedly increase by 2.4% in the quarter. The increase is likely to be temporary and the terms of trade are expected to return to a downward path as low dairy and forestry prices continue to flow through to exports and the offset from lower oil prices fades.

New Zealand's net international investment position (NIIP) also improved, from -65.0% of GDP in the year to December to -64.2% of GDP in March, its lowest level since 2001. While some of the improvement since 2011 reflects reinsurance claims relating to the Canterbury earthquakes, this effect is receding as outstanding claims dwindle and the lower NIIP looks to be a permanent improvement (Figure 5).

Figure 5: Net international investment position



Source: Statistics NZ

...but the annual goods deficit continues to widen...

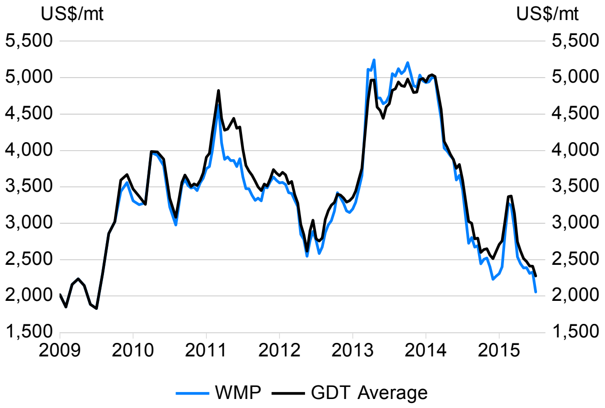
Overseas merchandise trade data showed a monthly $350 million trade surplus in May. Weak exports were evident with dairy exports 27.6% lower than a year ago and total merchandise exports 4.7% lower as a result. However, imports were lower than expected, down 7.0% on a year ago. The fall in imports was chiefly due to lower crude oil and capital goods imports than a year ago.

In annual terms the trade deficit at the end of May was $2,570 million, larger than at the end of March. If the terms of trade deteriorate as expected, the goods deficit will widen further over the course of this year.

...and commodity prices remain low

Dairy prices continued on their downward trend in June and into July, with prices weak across all products (Figure 6). The average GDT dairy price has fallen for eight auctions in a row now and is 32.5% lower than its recent peak in early March and 54.9% lower than the February 2014 high. The outlook for dairy prices remains weak as milk production remains high and demand subdued.

Figure 6: Dairy prices



Source: GlobalDairyTrade

The weakness in dairy prices was reflected in the ANZ Commodity World Price Index which fell 4.7% in May. While dairy was the main driver, lower meat and forestry prices also contributed. Thanks to a weaker NZD, the decline in the NZD Price Index was a more modest 2.7%.

Crude oil prices have remained fairly stable over the past two months, with WTI and Brent trading in fairly tight ranges around the US$60/barrel and US$64/barrel marks respectively.

The Reserve Bank reduced the OCR to 3.25% on a weaker inflation outlook...

Earlier in June the Reserve Bank surprised markets by reducing the OCR 25 basis points (bps) to 3.25% in its Monetary Policy Statement (MPS) released on 11 June. While most analysts were expecting reductions at some point, and this was priced into the market, the timing of the reduction was earlier than most had anticipated.

The main factors behind the Reserve Bank's decision were the continuing decline in the terms of trade (thanks to weaker commodity prices) and lower domestic inflation increasing the risk of inflation returning to the mid-point later than expected. The impact of low dairy prices on farm expenditure and rural spending was flagged as a significant risk. Annual non-tradables inflation was noted as being relatively weak despite above-trend growth over the past three years, with strong growth in labour supply helping to offset capacity constraints elsewhere.

...with further monetary easing expected

The Reserve Bank noted that further easing may be appropriate, although conditional on emerging data. Most analysts have a further 25 bps reduction pencilled in for July and some are forecasting a third reduction by the end of the year. Monetary policy is expected to remain accommodative throughout 2016 and into 2017.

Interest rates are now expected to remain below those forecast in the BEFU for some time, and the depreciation in the exchange rate is expected to offset some of the income effects of the lower terms of trade. As a result, the Reserve Bank MPS and Treasury BEFU forecasts for real and nominal GDP growth are not significantly different (although the composition of growth differs).

The exchange rate has depreciated in part due to domestic factors...

The reduction in the OCR, coupled with weaker than expected domestic data, contributed to exchange rate depreciation over the month. At the start of June, the NZD was trading at 0.76 and 0.96 versus the USD and AUD respectively; by the end of June it had fallen to 0.68 and 0.88 respectively. This depreciation will help boost export receipts and will also put upwards pressure on tradables inflation by making imported goods more expensive in domestic terms.

...although more upbeat global activity has also contributed

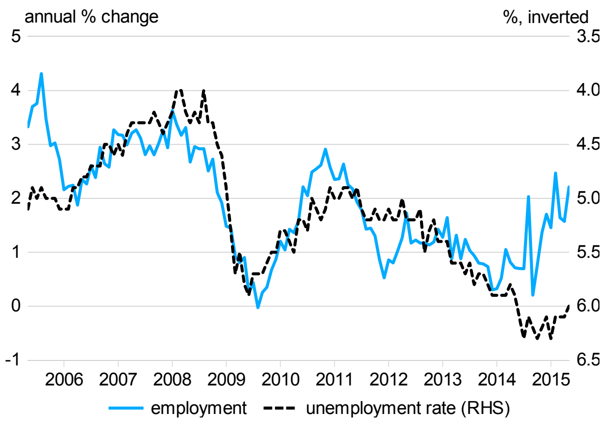
International developments were mostly positive, with improvements in the Australian labour market and continued recovery in the US economy, although Greece failed to make its payment to the IMF due at the end of June. Global bond yields rose on the back of positive data and Greek risks. US monetary policy is on track to tighten in late 2015, and expectations of extended stimulus have fallen in the euro area. The mostly positive international news also contributed to the NZD depreciating.

Australian GDP shows weak domestic demand but labour market strengthens...

Australian March quarter (Q1) GDP growth was strong at 0.9%, driven by residential investment and net exports, but household consumption growth was soft and business investment contracted heavily, leaving total domestic demand flat in the quarter. Nominal GDP growth was lower than real growth at 0.4% in Q1, owing to falling terms of trade and low inflation.

However, the labour market has picked up. Employment rose 2.2% from a year ago in May, and the unemployment rate fell 0.1% point to 6.0%, its lowest since May 2014 (Figure 7); meanwhile, the participation rate (64.7% in May) has risen since 2014. Annual house price growth stabilised at 7.5% in Q1, down from 11% growth a year ago. Retail spending was flat in April, but this may have reflected poor weather. Low interest rates, an improving labour market and house price growth should support spending in coming quarters.

Figure 7: Australian labour market



Source: Haver

...and Chinese house prices may have bottomed out

China's house prices ticked up 0.2% in May (but remained 5.7% lower annually), showing a tentative stabilisation. Stronger housing market activity reflects the sizable monetary and regulatory easing by the government since mid 2014. However, growth in broader economic activity was subdued in the June quarter (Q2), particularly for manufacturing. Reflecting soft domestic demand and lower import prices, annual inflation fell from 1.5% in April to 1.2% in May.

US recovery resumes in Q2 while inflation was higher in the euro area...

US Q1 GDP growth was revised up 0.2% points to slightly negative (rounded to 0.0%), still showing the impact of the harsh winter and dock strike. However, activity rebounded in Q2. Non-farm payrolls grew 280,000 in May, and annual growth in weekly earnings lifted to 2.3%. Solid growth in personal income in May (0.5%) helped boost personal spending (0.9%). Consumer confidence surged in June, suggesting solid spending.

Activity and inflation rose in the euro area. Euro area PMIs show faster growth in activity in June, supported by low interest rates and the earlier euro depreciation. Employment expanded 0.8% from a year ago in Q1 and the unemployment rate has fallen to 11.1% in May from 11.6% in May 2014. Annual inflation was 0.3% in May and 0.2% in June, up from early 2015, attributed to higher oil prices and labour costs.

In Japan, Q1 GDP growth was revised up to 1.0%, driven by business investment. Recent data suggest a moderate pace of growth in Q2. Annual inflation fell from 2.3% to 0.6% in April and 0.5% in May as the effect of the tax rise last year dropped out.

...amid heightened risks around Greece

Risks increased as Greece failed to make its payment to the IMF on 30 June (€1.5bn) and its current bailout expired. Negotiations between Greece, the EU and the IMF broke down without extended funding being agreed. While the Greek government had shown some willingness to compromise on key issues, its creditors viewed further public spending cuts as necessary. The Greek government will take the EU's latest proposal to a national referendum scheduled for 5 July. The ECB has capped its emergency liquidity assistance to Greek banks, which are shut with limits on the withdrawal of deposits.

Global bond yields continue to rise...

Long-term bond yields increased across the major economies over June, reflecting stronger activity, slightly higher inflation and Greek risks. The US 10-year Treasury yield rose 21 basis points (bps) to 2.35%, while the 10-year German bund yield lifted 28 bps to 0.77%. Euro area peripheral bond yields increased by around 50 bps on average as a result of heightened Greek risks. The 5-year Greek bond yields surged from 15.5% to 24%. Greek risks initially led to some volatility in the NZX50 and the NZD, but markets have settled.

Despite higher global yields, the NZ 10-year bond yield fell 8 bps over June to 3.64%, reflecting lower OCR expectations. The NZD TWI fell 3.4 points to 71.3 over the month, owing primarily to low Q1 GDP growth, an OCR reduction by the RBNZ (see domestic section) and some safe-haven demand for the USD.

...as US monetary tightening is expected...

Federal Reserve (Fed) Chair Yellen indicated that US monetary tightening in late 2015 is appropriate given recent data outturns. However, the Fed's latest forecasts showed that policy tightening over the next couple of years is expected to be slower than previously anticipated, with the Fed Funds rate 25 bps lower at the end of 2016 and 2017, at 1.6% and 2.9% respectively.

...and further easing elsewhere is uncertain

The improvement in euro area economic conditions points to a lower likelihood of expanded stimulus by the European Central Bank, which did not view higher bond yields as a concern. The Bank of Japan remains upbeat on the outlook for activity and inflation, although analysts view further easing as necessary to achieve its 2% inflation target. The Reserve Bank of Australia left its cash rate at 2.0% in June, with the policy outlook heavily dependent on data. Meanwhile, the People's Bank of China cut its lending rates by 25 bps each (with the 1-year rate down to 4.85%) in response to the growth slowdown and a large fall in Chinese equity prices

.

Special Topic: International Tourism Developments and Travel Services Exports

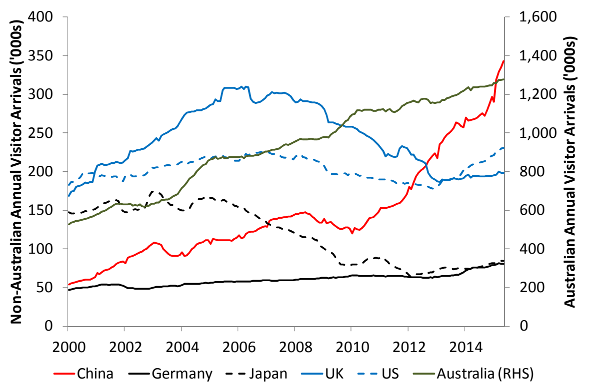
Tourism, comprising both domestic and international elements, is an important industry in the New Zealand economy. Travel services exports, of which international tourism is the main contributor, accounted for 16% of New Zealand's total exports in the March 2015 year. This special topic concludes that recent rapid growth in travel services exports has come from a combination of increased visitor arrivals, an increase in the average length of stay, and an increase in the average spend per visit. The outlook for travel services exports is positive and could help offset some of the slowing momentum elsewhere in the economy.

Visitor numbers rise rapidly…

After remaining steady around the 2.4-2.5 million mark between 2005 and 2011, the number of short term visitor arrivals to New Zealand has trended steadily upwards. The latest data puts visitor arrivals in the year to May 2015 at 2.98 million, a 6.9% increase on the previous year and a new record level.

China (including Hong Kong) is New Zealand's largest source of visitor arrivals growth, accounting for more than 40% of the increase in visitor arrivals since 2011 (Figure 1.1). Since 2012 China has been the second largest source of visitor arrivals. While Australia is by far the largest source of visitor arrivals, it accounted for only a third of the increase, much less than its market share of 43-45%. The next four largest sources, the US, UK, Japan and Germany, contributed a further 8% to the increase, with the US contributing the lion's share of this and visitor numbers from the UK actually declining over the five year period.

Figure 1.1: Annual visitor arrivals



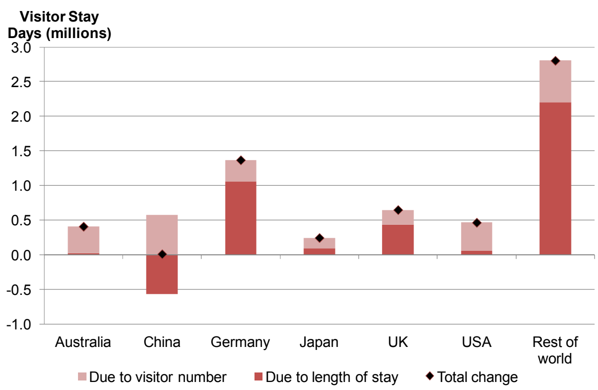
Source: Statistics NZ

As a result, the recent upward trend in total visitor arrivals reflects steady growth in some of New Zealand's traditional sources of visitors such as Australia, Germany and the US, and the rapid expansion of visitor arrivals from China. The changing composition of New Zealand's visitor arrivals, with proportionally more visitors from China, the US and Germany, has positive implications for the average length of stay.

…contributing to a surge in visitor expenditure…

International visitor expenditure has grown rapidly in the last year with around a third of that growth due to the solid growth in international visitor arrivals. Expenditure growth has also been supported by a longer average length of stay and increased average daily spend which have both also accounted for around a third of the increase each. International travel services exports rose $1.3 billion (13.7%) to $10.7 billion in the year ended March 2015. This is the fastest pace of growth since 2003 and consistent with the high levels of activity being reported by the hospitality sector in Treasury's business talks,[1] and is reflected in solid growth in other indicators such as hospitality spending in the Electronic Card Transactions data and accommodation and food and beverage sales in the Retail Trade Survey.

Figure 1.2: Change in visitor stay days (March 2015 year)



Sources: Statistics NZ, MBIE

Travel services exports are the second largest export category by value after dairy exports and rising tourism expenditure has offset some of the lower national disposable income from depressed dairy prices. On current trends, travel services

[1] See March 2015 MEI special topic http://www.treasury.govt.nz/economy/mei/mar15

export values may temporarily become the largest export category later this year.

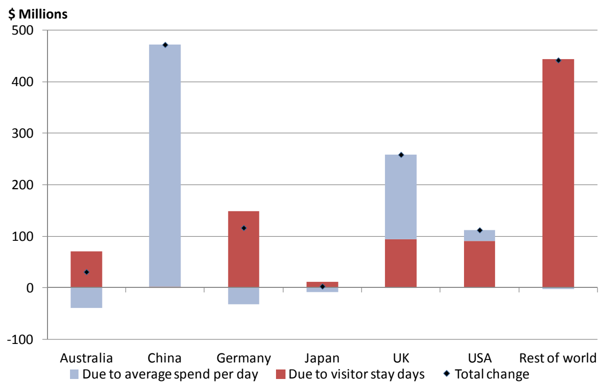
The Ministry of Business, Innovation and Employment's (MBIE) International Visitor Survey (IVS) - which excludes education travel expenditure - shows that visitor spending rose $1.4 billion in the year ended March 2015.[2] This has been driven by an increase in both the number of visitor stay days (visitor arrivals multiplied by length of stay) and average spending per day. Around half of the increase in visitor stay days is attributable to an increased length of stay, reflecting a general lift across most countries (excluding China) and the changing mix of visitor arrivals (Figure 1.2).

These positive impacts have been marginally offset by lower average spending per day from Europe, Japan and Australia, likely as a consequence of the fall in the euro and yen as a result of quantitative easing and a slowdown in economic growth in Australia.

…led by Chinese visitor expenditure…

The largest positive contribution in the March 2015 year came from a $470 million rise in Chinese visitor expenditure – with annual expenditure rising 61.2% to exceed $1.2 billion. This rise has been driven almost exclusively by increased average spending per day (Figure 1.3). A shorter length of stay completely offset the increased number of Chinese visitor arrivals in the last year.

Figure 1.3: Change in visitor expenditure (March 2015 year)



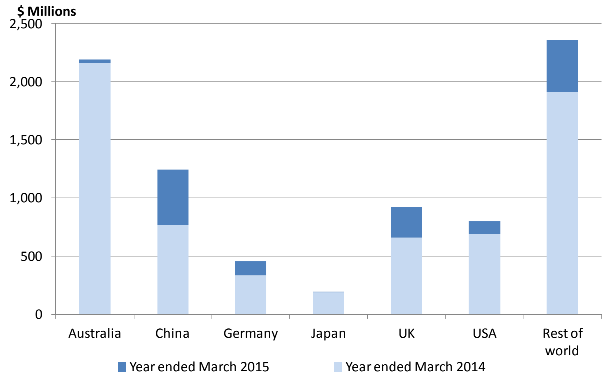
Sources: Statistics New Zealand, MBIE

Rising average spends could in part reflect a change to Chinese travel laws which took effect in October 2013 and restricted low-cost tour providers. Consequently, Chinese visitors are now spending more on average for package holidays and to travel in tour groups. Average daily spend has also increased for independent travellers.

…and a recovery in traditional markets…

Total expenditure has also been supported by rising visitor stay days by traditional markets and, in the case of the UK, a higher average daily spend. Expenditure from the UK rose $258 million to $919 million (Figure 1.4) in the year ended March 2015, while expenditure by visitors from the US, Germany and the rest of the world (mainly the rest of Asia and Europe) rose $112 million, $116 million and $440 million respectively.

Figure 1.4: Total visitor expenditure



Sources: Statistics New Zealand, MBIE

…but Australian visitor spending flat

The main drag on growth came from the Australian market (up just $30 million to $2.2 billion), with an increase in visitor numbers partially offset by a lower average daily spend. This likely reflects the slowdown in the Australian economy and consequent rise in unemployment in recent years, coupled with the effects of a stronger New Zealand dollar which reached post-float highs against the AUD in early 2015. Despite these headwinds, New Zealand's proximity relative to other destinations means that it is seen as a relatively low-cost destination buffering the impacts on visitor numbers. Personal ties also play an important role in sustaining visitor numbers, with around 40% of Australian visitors coming to visit friends and relatives (compared to 12% of Chinese and 20% of Americans).

[2] IVS and Balance of Payments measures differ slightly given MBIE international visitor expenditure data incorporates updated outlier methodology which Statistics New Zealand will incorporate in the June quarter GDP and Balance of Payments releases.

Outlook for international travel services exports growth supported by China…

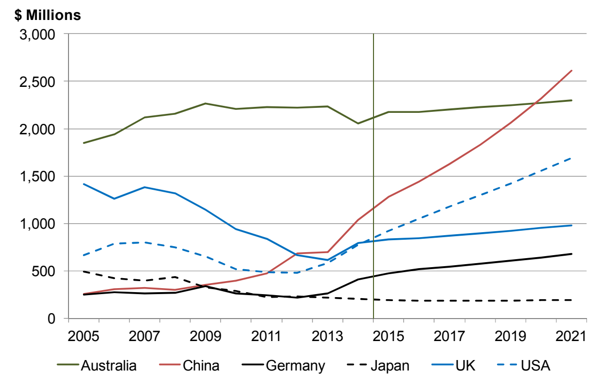
Treasury does not forecast travel services exports separately, instead producing a forecast of total services exports. That said, MBIE tourism forecasts released in September 2014 for the 2015-2021 period are similar to those implied by assuming the historical ratio of travel services exports to total services exports and the ratio of IVS expenditure to total travel services exports.

MBIE forecasts show visitor arrivals growing around 4% a year, rising by 900,000 to reach 3.8 million by 2021. Total IVS visitor expenditure is projected to rise 48% to $11.1 billion in 2021 driven by rising disposable incomes and airline route availability and capacity.

Around a third of the increase in visitor arrivals is driven by China. Arrivals are forecast to rise 11.6% per year and reach over 500,000 by 2021. Chinese visitor expenditure is expected to rise at a faster pace of around 14% per year as the market matures with a move towards longer stays. Consequently total Chinese visitor spend is projected to surpass Australia's in 2020, and rise to $2.7 billion in 2021 (Figure 1.5).

Solid growth in visitor arrivals is also expected from Germany (6.0%), the United States (4.9%) and other developing markets such as India (11.8%) and Indonesia (12.4%) – although the latter two are from a much lower base. Australian visitor arrivals are expected to continue to expand at a 3.0% pace, contributing around a third to the increased arrivals across the projection period, although a lower average daily spend is expected to temper the impact on total Australian visitor expenditure.

Figure 1.5: Projected annual expenditure



Sources: MBIE, NZIER

Conclusion

With the rapid growth in Chinese arrivals expected to continue and Australia and other traditional markets providing a solid foundation, the trend in visitor arrivals is likely to remain positive for some time to come. When the upward trends in visitor expenditure are added in, travel services exports growth is expected to remain strong in the medium term.

This is reflected in the *Budget Update* forecasts, where the services balance is expected to remain in surplus throughout the forecast period despite solid growth in services imports. Furthermore, if the exchange rate continues to remain weaker than previously forecast, or oil prices remain lower for longer (impacting on airfare costs), New Zealand's attractiveness as a destination could increase further. Positive surprises to travel services exports could help mitigate some of the downside risks seen elsewhere in the current account.

Monthly Economic Indicators is a regular report prepared by the Forecasting team of the Treasury.

Contact for enquiries:
The Treasury
PO Box 3724, Wellington
NEW ZEALAND

information@treasury.govt.nz
Tel: +64 4 472 2733
Fax: +64 4 473 0982

New Zealand Key Economic Data

Quarterly Indicators

		2013Q4	2014Q1	2014Q2	2014Q3	2014Q4	2015Q1	2015Q2
Gross Domestic Product (GDP)								
Real production GDP	qtr % chg[1]	0.5	1.1	0.7	1.0	0.7	0.2	...
	ann ave % chg	2.2	2.5	2.8	3.0	3.3	3.2	...
Real private consumption	qtr % chg[1]	0.9	0.4	1.2	1.4	0.7	0.7	...
	ann ave % chg	2.9	2.9	2.8	3.0	3.2	3.7	...
Real public consumption	qtr % chg[1]	0.5	1.2	0.5	0.8	0.6	0.2	...
	ann ave % chg	1.9	2.7	3.3	3.3	3.4	3.0	...
Real residential investment	qtr % chg[1]	0.2	10.3	0.0	-0.2	4.9	0.6	...
	ann ave % chg	16.6	16.6	18.0	16.0	16.2	12.3	...
Real non-residential investment	qtr % chg[1]	-0.3	0.4	1.9	3.8	-1.3	-2.8	...
	ann ave % chg	6.2	8.4	8.7	7.4	6.2	4.6	...
Export volumes	qtr % chg[1]	2.5	2.6	-2.8	0.4	5.9	1.5	...
	ann ave % chg	1.0	0.3	0.6	2.0	3.3	3.9	...
Import volumes	qtr % chg[1]	0.2	2.0	2.9	0.3	2.8	1.0	...
	ann ave % chg	6.3	8.0	8.9	7.9	7.8	7.5	...
Nominal GDP - expenditure basis	ann ave % chg	5.4	6.8	8.1	7.6	5.5	3.9	...
Real GDP per capita	ann ave % chg	1.4	1.5	1.7	1.6	1.8	1.5	...
Real Gross National Disposable Income	ann ave % chg	4.4	5.8	6.3	5.9	4.5	2.9	...
External Trade								
Current account balance (annual)	NZ$ millions	-7,350	-6,005	-5,814	-6,093	-7,798	-8,604	...
	% of GDP	-3.3	-2.6	-2.5	-2.6	-3.3	-3.6	...
Investment income balance (annual)	NZ$ millions	-9,027	-9,338	-9,770	-9,956	-9,996	-9,706	...
Merchandise terms of trade	qtr % chg	2.5	1.8	0.1	-4.5	-2.4	1.4	...
	ann % chg	20.2	17.3	12.2	-0.3	-5.0	-5.4	...
Prices								
CPI inflation	qtr % chg	0.1	0.3	0.3	0.3	-0.2	-0.3	...
	ann % chg	1.6	1.5	1.6	1.0	0.8	0.1	...
Tradable inflation	ann % chg	-0.3	-0.6	0.1	-1.0	-1.3	-2.8	...
Non-tradable inflation	ann % chg	2.9	3.0	2.7	2.5	2.4	2.3	...
GDP deflator	ann % chg	7.7	5.6	4.5	1.2	-2.1	-0.8	...
Consumption deflator	ann % chg	0.9	0.9	1.0	0.6	0.7	0.7	...
Labour Market								
Employment (HLFS)	qtr % chg[1]	0.8	1.0	0.4	1.0	1.2	0.7	...
	ann % chg[1]	2.9	3.7	3.6	3.2	3.5	3.2	...
Unemployment rate	%[1]	6.1	6.0	5.7	5.5	5.8	5.8	...
Participation rate	%[1]	68.7	69.0	68.6	68.8	69.4	69.6	...
LCI salary & wage rates - total (adjusted)[5]	qtr % chg	0.5	0.3	0.5	0.5	0.5	0.3	...
	ann % chg	1.6	1.5	1.6	1.7	1.7	1.7	...
QES average hourly earnings - total[5]	qtr % chg	0.2	0.5	0.2	1.4	0.5	0.0	...
	ann % chg	2.9	2.5	2.5	2.3	2.6	2.1	...
Labour productivity[6]	ann ave % chg	-0.7	-0.9	-0.9	-0.7	-0.3	0.0	...
Retail Sales								
Core retail sales volume	qtr % chg[1]	1.0	0.9	1.3	1.5	1.9	2.9	...
	ann % chg	3.7	3.5	3.0	4.5	6.0	7.5	...
Total retail sales volume	qtr % chg[1]	1.1	0.9	1.3	1.6	1.9	2.7	...
	ann % chg	3.9	3.6	3.6	4.7	5.9	7.4	...
Confidence Indicators/Surveys								
WMM - consumer confidence[3]	Index	120	122	121	117	115	117	113
QSBO - general business situation[4]	net %	52.8	51.7	31.7	19.0	23.6	23.0	...
QSBO - own activity outlook[4]	net %	18.5	34.8	20.4	12.1	33.1	19.0	...

Monthly Indicators

		2014M12	2015M01	2015M02	2015M03	2015M04	2015M05	2015M06
External Sector								
Merchandise trade - exports	mth % chg[1]	5.7	-8.9	4.8	1.3	-3.3	0.4	...
	ann % chg[1]	-7.3	-9.5	-14.2	-2.5	-6.2	-4.7	...
Merchandise trade - imports	mth % chg[1]	-5.6	2.5	-3.8	6.1	-2.3	3.9	...
	ann % chg[1]	8.1	-4.1	1.8	2.8	0.3	-7.0	...
Merchandise trade balance (12 month total)	NZ$ million	-1183	-1416	-2129	-2372	-2656	-2570	...
Visitor arrivals	number[1]	246,150	248,560	266,930	255,790	259,600	259,830	...
Visitor departures	number[1]	253,850	251,940	259,810	269,310	259,550	267,950	...
Housing								
Dwelling consents - residential	mth % chg[1]	-6.5	-2.5	-5.6	9.9	-0.9	0.0	...
	ann % chg[1]	8.1	3.6	-0.6	13.6	1.4	2.2	...
House sales - dwellings	mth % chg[1]	17.7	-15.7	4.0	4.7	0.1	-1.4	...
	ann % chg[1]	24.2	2.6	12.6	20.3	27.6	21.6	...
REINZ - house price index	mth % chg	0.6	1.8	1.2	1.0	1.2	1.9	...
	ann % chg	5.7	8.5	7.1	8.5	9.3	11.8	...
Private Consumption								
Electronic card transactions - total retail	mth % chg[1]	0.0	0.0	1.1	0.7	-0.7	1.2	...
	ann % chg	3.7	4.5	4.0	3.7	3.9	3.2	...
New car registrations	mth % chg[1]	2.1	-0.7	-0.3	2.4	-1.6	-0.4	...
	ann % chg	21.0	17.1	12.1	11.8	11.2	6.8	...
Migration								
Permanent & long-term arrivals	number[1]	8,800	10,060	9,550	9,890	9,610	9,900	...
Permanent & long-term departures	number[1]	4,710	4,600	4,740	4,880	4,840	4,760	...
Net PLT migration (12 month total)	number	50,922	53,797	55,121	56,275	56,813	57,822	...
Commodity Prices								
Brent oil price	US$/Barrel	62.34	47.76	58.10	55.89	59.52	64.08	*61.53*
WTI oil price	US$/Barrel	59.29	47.22	50.58	47.82	54.45	59.27	*59.86*
ANZ NZ commodity price index	mth % chg	-3.8	0.1	9.7	1.5	-9.0	-2.7	...
	ann % chg	-13.7	-14.1	-6.5	-2.5	-6.9	-7.9	...
ANZ world commodity price index	mth % chg	-4.4	-0.3	4.2	4.6	-7.4	-4.7	...
	ann % chg	-17.2	-18.4	-15.8	-11.9	-15.3	-17.8	...
Financial Markets								
NZD/USD	$[2]	0.7764	0.764	0.7444	0.7473	0.7583	0.7394	*0.6990*
NZD/AUD	$[2]	0.94	0.9465	0.9555	0.9658	0.9814	0.9368	*0.9055*
Trade weighted index (TWI)	June 1979 = 100[2]	78.24	78.18	77.16	78.27	79.17	76.49	*72.97*
Official cash rate (OCR)	%	3.50	3.50	3.50	3.50	3.50	3.50	3.25
90 day bank bill rate	%[2]	3.67	3.67	3.63	3.63	3.63	3.53	*3.33*
10 year govt bond rate	%[2]	3.78	3.42	3.27	3.30	3.25	3.66	*3.77*
Confidence Indicators/Surveys								
ANZ - business confidence	net %	30.4	...	34.4	35.8	30.2	15.7	-2.3
ANZ - activity outlook	net %	37.3	...	40.9	42.2	41.3	32.6	23.6
ANZ-Roy Morgan - consumer confidence	net %	126.5	128.9	124.0	124.6	128.8	123.9	119.9
Performance of Manufacturing Index	Index	57.1	51.3	56.4	54.6	51.7	51.5	...
Performance of Services Index	Index	56.8	57.9	56.0	57.6	56.5	58.0	...

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, NZIER, ANZ, Haver, Westpac McDermott Miller, ANZ-Roy Morgan, REINZ, BNZ-Business NZ