Monthly Economic Indicators

THE TREASURY
Kaitohutohu Kaupapa Rawa

New Zealand Government

July 2018

Executive Summary

- **Mixed messages for growth as labour income continued to grow strongly but retail card spending weakened**
- **Risks to our growth forecasts are rising as the housing market cools, business confidence weakens, and international trade tensions rise**
- **Inflation remained subdued, but pressures appear to be gradually increasing**
- **Strong growth in the US, offset by a weaker outlook for the rest of the world**

Labour income continued to grow strongly as both wages and employment remained solid. However, retail card spending fell 0.2% in the June quarter following a 1.7% increase in the March quarter and the housing market continued to cool. On the positive side, the number of new dwelling consents rose 7.5% in the June quarter following a 6.2% increase in the previous quarter. The trade balance narrowed in the quarter driven by an increase in export values despite easing commodity prices.

NZIER's Quarterly Survey of Business Opinion (QSBO) showed headline business confidence and own-activity measures fell in the June quarter, while ANZ's monthly Business Outlook showed the deteriorating trend continued in July. Although we think growth held up in the June quarter, weaker confidence, in conjunction with other data, highlight the risk that growth over the coming fiscal year may be weaker-than-forecast in the Budget Economic and Fiscal Update 2018 (BEFU18).

Annual Consumers Price Index (CPI) inflation was 1.5% in the June year, up from 1.1% in the March year. The outturn was slightly above our BEFU18 estimate of 1.4%. The RBNZ's preferred measure of underlying inflation also ticked higher.

The international environment remains broadly stable. US growth was strong for the June quarter, however, the outlook for the rest of the world was slightly less favourable and the IMF downgraded growth projections for China, the Euro area, Japan and the UK. Trade tensions remain a key risk to the world economic outlook and have dominated headlines in July. Both China and the US have implemented tariffs on each other's imported goods. The impact on New Zealand is likely to be small at this stage.

Growth in Australia, our second largest trading partner, is also at risk from rising trade tensions. However, the impacts of trade developments to date appear to be minor. The outlook is for growth in Australia to remain around its current rate of 3% over the next 18 months or so. Our Special Topic discusses the outlook for Australia in more detail.

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Analysis

Economic data for July were mixed

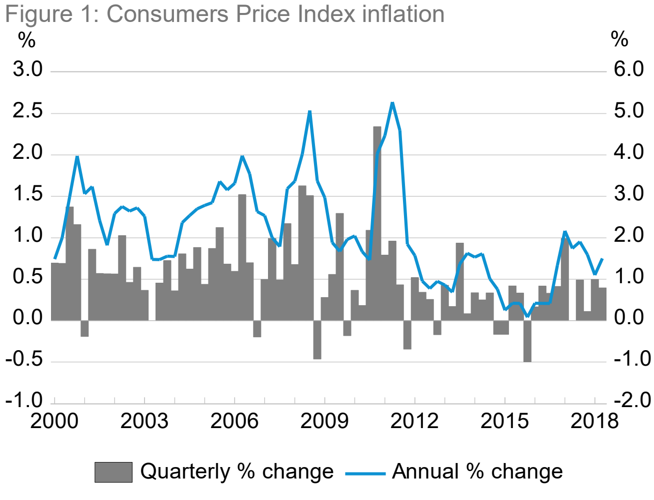
Electronic card spending suggests consumer spending was broadly steady in the June quarter. The quarterly trade deficit narrowed but business confidence measures continued to decline. The housing market continued to cool, while building consents pointed to a pick-up in residential investment for the rest of 2018. Also on the positive side, labour income continued to grow strongly as both wages and employment remained solid. Underlying inflation ticked slightly higher, but still below the mid-point of the Reserve Bank's 1%-3% target range. Financial market pricing currently implies no expectation of OCR increases for at least 12 months.

Although we think growth held up in the June quarter, weaker confidence, in conjunction with other data, highlight the risk that growth over the coming fiscal year may be weaker-than-forecast in the Budget Economic and Fiscal Update 2018 (BEFU18).

CPI inflation inching higher

Annual Consumers Price Index (CPI) inflation was 1.5% in the June year, up from 1.1% in the March year. Part of the increase was due to particularly low inflation in the June 2017 quarter dropping out of the annual calculation. Quarterly inflation fell to 0.4%, compared with 0.5% in the March quarter (Figure 1). The annual rate of headline inflation was largely in line with market expectations as well as the BEFU18 forecast of 1.4%. The outturn is within the Banks target 1%–3% range, but below the 2% mid-point.

Figure 1: Consumers Price Index inflation



Source: Stats NZ

Petrol prices, alcoholic beverages, and food led the increases in quarterly inflation, partly offset by cheaper second hand cars, audio-visual equipment, and telecommunication. On an annual basis, private transport services, cigarettes and tobacco, and rents contributed the most to headline inflation, while most of the declines came from fruit and vegetables, audio-visual equipment, and the introduction of fees-free tertiary education. Annual non-tradables inflation was 2.5%, up from 2.1% in the previous quarter. Annual tradables inflation, on the other hand, was 0.1%, increasing from -0.4%.

… petrol prices boosted inflation, but the markets expect lower prices in the upcoming five years

Petrol prices rose 3.2% in the June quarter contributing 0.2% to headline inflation, owing to higher international oil prices and a weaker New Zealand dollar. Global oil prices rose 16% between February and June 2018. However, oil prices fell 7.3% in July to US$68.8 per barrel as OPEC supply increased. In response, domestic petrol prices declined 2.2% in July relative to June, more than offsetting the national impact of the Regional Fuel Tax introduced in Auckland on July 1. Futures markets indicate global oil prices are expected to decline to around US$59 per barrel over the next 4-5 years.

Underlying inflation measures tick higher

The 10% trimmed mean measure of annual inflation rose from 1.4% to 1.8%. The proportion of items in the CPI basket increasing in price rose from 46.4% in the June quarter last year to 52.2% this quarter. The proportion of items declining in price also fell, confirming the same message of increasing inflation pressure. The Reserve Bank's preferred measure of underlying inflation, the sectoral factor model, increased from 1.6% in the March year to 1.7% in the June year.

Overall, inflation remains subdued and any monetary policy tightening remains some time away

Inflation remains subdued, and the latest outturn did not shift market expectations of monetary policy settings materially. Market pricing currently implies no OCR increases for at least 12 months. The Reserve Bank has noted that it is well-positioned to manage change in either direction. We expect the outlook for inflation to remain stable for the rest of the year as the drivers in either direction remain largely in balance.

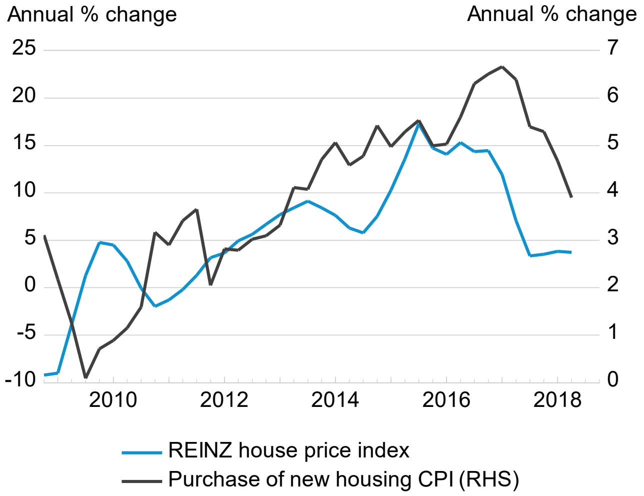
Housing market continues to cool, accompanied by slower new housing cost inflation

Monthly house price growth remained subdued in June with the REINZ House Price Index (HPI) flat following a 0.2% decline in May. Between August 2017 and March 2018, monthly house price growth picked up, but has since levelled off. The New Zealand HPI was up 3.8% from a year ago, remaining flat from the previous month. The Auckland HPI fell 0.3% to be up 0.9% from a year ago. Excluding Auckland, prices rose 0.3% in the month to be up 6.7% from a year ago. House sales also fell, again led by Auckland.

Overall, the housing market is cooling slightly faster than we had anticipated as migration continues to ease and with some forthcoming Government policies such as loss ring fencing, foreign buyer restrictions, and bright line extension, likely to reduce demand. An orderly cooling in the housing market is desirable for the soundness of the financial system. It lowers the likelihood of a sharp correction in house prices arising from a potential overvaluation and improves housing affordability. On the flip side, lower house prices are associated with lower household consumption due to the decline in homeowners' perceived wealth.[1]

The CPI class of "purchase of housing" measures the change in the price of buying a newly built house excluding land. In line with slower house price growth, new housing inflation also slowed in the June year, to 3.9% compared to 6.4% a year earlier (Figure 2). Similar regional patterns in house price growth were apparent in the CPI data with annual inflation for new housing in Auckland easing the most, to 3.4% compared with 8.1% in June 2017.

Figure 2: House price growth and inflation in the cost of purchasing a new house



Sources: REINZ, Stats NZ

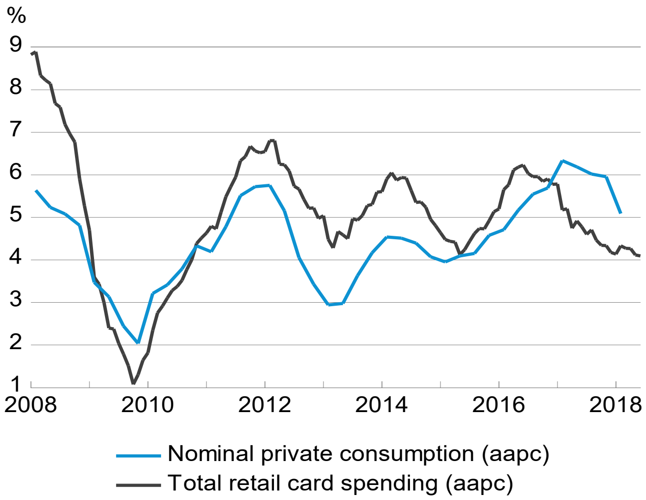
Stronger building consents point to solid residential investment for the rest of 2018

The number of new dwelling consents in June fell 7.6% following a 6.9% increase in May. The decline was expected as some of last month's strength appeared to be due to one-off developments. For the June quarter, however, consent numbers were still strong – up 7.5% compared with a 6.2% increase in the March quarter. The consents data suggest a pick-up in residential investment throughout the rest of 2018, although growth may be constrained by capacity constraints in the construction sector.

Electronic card spending points towards lower private consumption for the June quarter

Seasonally adjusted retail card spending rose 0.8% in June, following an increase of 0.6% in May. Core retail spending (excluding fuel and the purchase of vehicles) rose by 0.6% in the month, the same as in May, continuing the recovery in card spending following the large fall in April (-2.2%, sa). Overall, spending fell 0.2% in the June quarter following a 1.7% increase in the March quarter, suggesting consumer spending was broadly steady in the June quarter (Figure 3) – although electronic card spending was a poor indicator of consumption in the March quarter.

Figure 3: Consumption and electronic card spending



Source: Stats NZ

[1] Shaar, Karam, and Fang Yao. " Housing Leverage and Consumption Expenditure - Evidence from New Zealand Microdata " (2018).

Net PLT migration continued to ease

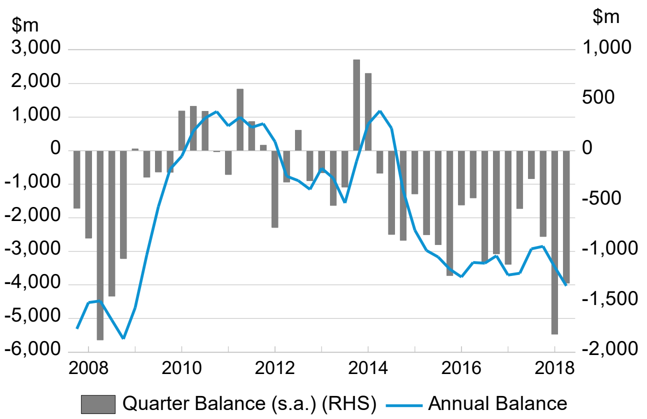
Net permanent and long-term (PLT) migration continued to decline, falling to 4,850 (sa) in the month of June from 5,090 in May. On an annual basis net migration continued to fall, down to 64,995, slightly below our BEFU18 forecast of 65,740. Arrivals continued to decline on an annual basis to 129,536, the fifth consecutive fall. Arrivals from work and student visas have been broadly flat since the beginning of 2017. We continue to expect net PLT migration to decline as departures of non-New Zealand citizens continue to pick up, and departures of New Zealand citizens remain broadly flat.

Higher-than-anticipated trade deficit for the June quarter

For the June quarter, the seasonally adjusted goods trade deficit narrowed to $1.3 billion from $1.7 billion in the March quarter. A 4.5% increase in exports more than offset a 1.2% rise in imports. The rise in export values was broad-based with increases in dairy (up 1.1%), meat (up 4.5%), lumber (up 0.4%), and fruit (up 1.4%). On the imports side the lift was driven by a rise in passenger motor cars (up 29.2%) and transport equipment (up 32.1% not seasonally adjusted). Some of the strength in imports is temporary as the lift in passenger vehicles is related to last quarter's stink bug problems and the rise in transport equipment, which included some one-off purchases.

The export figures suggest that System of National Accounts (SNA) exports growth will be higher than forecast for the June quarter, but not sufficient to offset the decline in exports in the previous quarter. The persistent strength in imports meant that the overall merchandise trade balance in the June quarter was weaker than we had expected at BEFU18 (Figure 4). We expect the quarterly trade balance to stabilise from here as the one-off imports abate.

Figure 4: Merchandise trade balance



Sources: Stats NZ

The weaker-than-expected trade balance was partly due to less favourable commodity prices

The ANZ world commodity price index fell for the first time this year, down 1.0% for the month of June. Declines were broad-based, but led by falls in meat and dairy. Forestry prices also eased slightly – the first decline in over 18 months.

Dairy prices continued to decline in July with falls at both GDT auctions in the month. The headline GDT index fell 5.0% followed by a fall of 1.7%. Prices are now back to around the level seen at the start of the year. Milk production has been lifting which, if sustained, will add some downside risk for prices. However, the weaker New Zealand dollar provides some offset to lower prices.

Mixed signals on wage growth while unemployment ticks higher

Annual wage growth measured by the Labour Cost Index (LCI) picked up to 1.9% in the June year compared with 1.8% in the March year.

On 1 April 2018, the Government raised the minimum wage by 75 cents to $16.50 an hour. According to Stats NZ calculations, if wages affected by the minimum wage had remained constant in the June 2018 quarter, LCI salary and wage rates would have increased 1.8% for the year (compared with a 1.9% outturn). The minimum wage will continue to rise in increments, reaching $20.00 per hour by 2021.

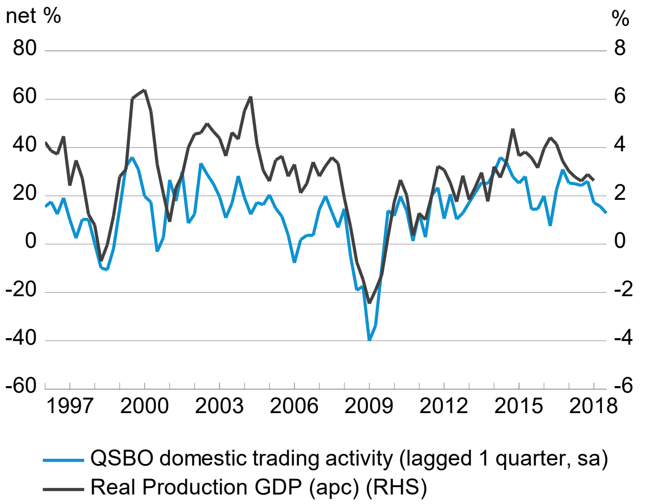
In the Quarterly Employment Survey (QES) wage growth eased to 3.1% in June from 3.6% in March but total hours paid increased 2.4% in the year to June from 2.0% in the March year. As a result, total gross earnings eased slightly to 5.5% in the year to June from 5.6% in the March year. Strong growth in total gross wages is being reflected in tax from Individuals, which is up 7.7% for the 11 months to May 2018 compared to the same period a year ago. Tax from Individuals is $371 million ahead of forecast, and the June quarter labour market outturn suggests that this variance is likely to persist, at least through to year end. Total tax revenue for the 11 months was close to forecast, as weaker corporate tax offset the stronger Individuals tax.

Unemployment rose in the June quarter from 4.4% to 4.5%. In line with the rise in unemployment, the underutilisation rate rose to 12.0%, up from 11.9% last quarter. The employment rate was 67.7%, remaining unchanged for three consecutive quarters. The latest outturn signals a broadly stable labour market as the supply and demand for labour remain broadly aligned.

Business confidence falls

NZIER's QSBO showed headline business confidence fell to a 7-year low with a net 19% of firms feeling pessimistic in the June quarter. The outlook for firms' domestic trading activity (a measure more highly correlated with GDP growth) also weakened, with a net 13% of firms expecting activity to pick up over the next 3 months, down from a net 16% in the March quarter (Figure 5).

Figure 5: Own activity, GDP



Sources: NZIER, Stats NZ

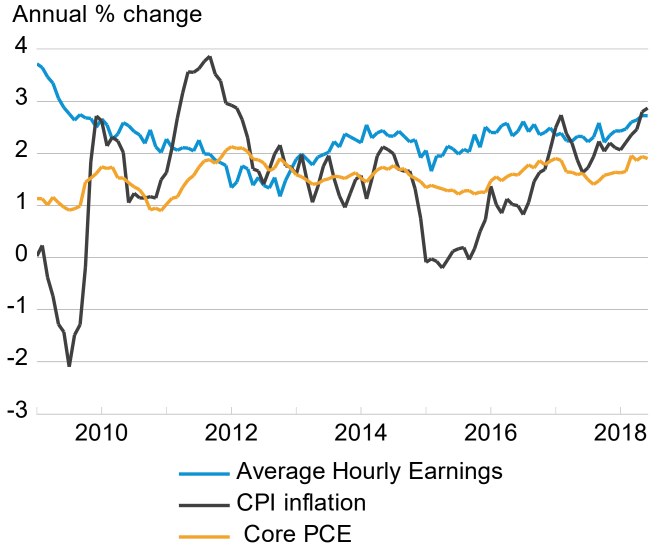
Other QSBO sentiment indicators were also weak: a net 16% of firms experienced weaker profitability in the quarter (compared to a net 7% in Q1) and investment intentions in plants and machinery were the weakest since 2012, falling from a net 16.5% in Q1 to a net 2% in Q2. ANZ's monthly Business Outlook showed the deteriorating trend continued in July.

Strong GDP growth in the US…

The preliminary US GDP release showed growth of 1.0% in the June 2018 quarter. On an annual basis, GDP increased 2.8%, following growth of 2.1% in the March quarter. This was the fastest pace in almost four years and was driven by personal consumption expenditure, exports and government spending (the US budget deficit is now approximately 7% of GDP). Some analysts attribute the strength in exports to purchases from foreigners concerned about tariff implementation, and is therefore likely to be short-lived.

US non-farm payrolls for June showed employment growth of 1.6%. The unemployment rate rose from 3.8% to 4.0%, driven by a pick-up in the participation rate. Wage growth remained broadly unchanged at 2.7%. CPI inflation is currently at 2.9%. Core Personal Consumption Expenditure (PCE) inflation (the Fed's preferred measure of inflation) was 1.9% in the June quarter (Figure 6). The Fed has continued to signal more hikes this year.

Figure 6: US wages and inflation on the rise



Source: Haver Analytics

…but growth outlook is weaker for rest of world…

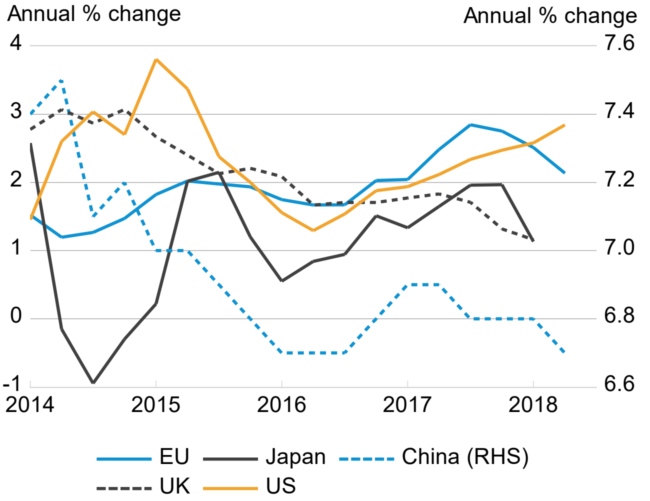
In contrast with the strength in the US, the outlook for the rest of the world is looking weaker. The IMF's World Economic Outlook (WEO) for July stated that global growth in 2018 and 2019 will be 3.9% – unchanged from their view last April. The update downgraded the growth projections for China, the Euro area, Japan, and the United Kingdom, reflecting negative surprises to activity in early 2018. The decline in growth in those countries is forecast to be offset by strengthening momentum in the United States.

Real GDP in China grew by 6.7% in the June 2018 year (Figure 7), inching lower from 6.8% in the March year, confirming the recent slowing momentum in the economy. The IMF downgraded growth in China from 6.5% to 6.4% for 2019 as regulatory tightening of the financial sector takes hold and external demand softens.

Preliminary June quarter GDP rose by 0.3% (2.1% y/y) in the European Union (EU), following a soft 0.4% rise in the March quarter (2.5% y/y). This was below market expectations of 0.4%. Growth has slowed in the EU since the start of the year - the average quarterly growth rate for 2017 was 0.7%. In contrast, preliminary CPI inflation figures for the EU were above market expectations. Headline inflation rose 0.1% to 2.1% (y/y) (previously 2.0%).

UK growth picked up to 0.3% in the month of May (from 0.2% in April). Overall this leaves the UK on track to achieve growth of 0.4% in the June quarter, up from 0.2% in the March quarter.

Figure 7: Global growth



Source: Haver Analytics

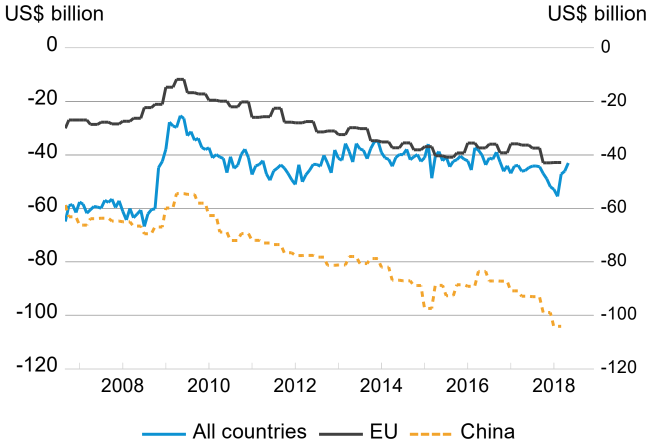
…and further trade tensions

Possibly the most significant risk to the world growth outlook is escalating trade protectionism, which has been dominating headlines in July. The US kicked off the tit-for-tat tariff measures by implementing tariffs (of 25%) on $34bn of US imports from China at the start of the month. China retaliated with its own tariffs on US imports and indicated that it will counter any further tariffs. The US also announced that it is currently preparing an additional 10% tariffs for an additional $200 billion worth of Chinese goods. These would come into effect on the 30th of August although much of the details surrounding the tariff implementation are still subject to considerable uncertainty. At the time of writing, it is being reported that both the US and China are trying to restart talks to ‘avoid a full-blown trade-war’.

Both the US and Chinese economies are beginning to feel the effects of trade protectionism. The US Government has promised US$12 billion in aid for farmers, including dairy farmers, who have been hit by Chinese tariffs. In China, the two major stock exchanges (Shanghai and Hong Kong) have seen large losses over the past 3 months and the PBoC (The People’s Bank of China) reportedly eased banks’ capital requirements in an effort to stimulate lending. The Chinese State Council decided to make fiscal policy more “proactive” and keep liquidity conditions “reasonably adequate.” The Council has indicated that both monetary and fiscal policy is expected to ease later in the year.

The US has also been involved in a series of trade discussions with the EU. As it stands, both presidents have agreed to hold off on any new tariffs while the two sides negotiate a trade deal. Both parties issued a joint statement "to work toward zero tariffs, zero non-tariff barriers, and zero subsidies on non-auto industrial goods". European equities were generally positive as a result. The US trade deficit with the EU is significantly smaller than that with China (Figure 8).

Figure 8: Monthly US trade deficit by country



Source: Haver Analytics

Brexit uncertainties continue…

The EU was also dealing with another risk mentioned in the World Economic Outlook this month: political uncertainty. The UK Government has announced its intention to pursue a ‘soft Brexit’, which signals a closer relationship with the EU than might otherwise be the case. As part of this move, the Government released a paper showing plans for free trade in goods, while services would likely face some restrictions. The shift to a softer Brexit caused some internal disruption in the governing Conservative party with a number of ‘pro Brexit’ MP’s resigning. The shift was also not taken well by the EU, with the European Commission reportedly calling on member states to step up preparations for a ‘no deal Brexit’ (where the UK would leave the EU with no trade deal signed in place).

...and focus remains on central banks

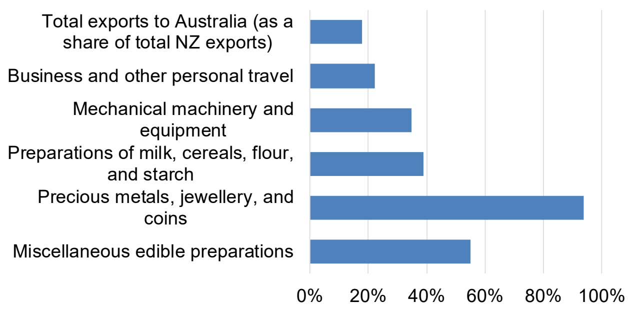
The Bank of Japan (BoJ) held interest rates steady at its July meeting but moved to add more flexibility to the policy framework, including the introduction of forward guidance. In its most recent meeting, the ECB made no changes to its forward guidance or inflation outlook. The ECB expects to end QE purchases by the end of the year and keep rates on hold into 2019. The Bank of England is expected to raise interest rates 25bpts to 0.75% overnight on Thursday (2 August) and the Federal Reserve held the target range at 1.75-2.0 at their July meeting.

Australia: Solid economic outlook but trade and household consumption pose risks

Members of the Treasury's forecasting team visited Australia and met with public and private sector economists to discuss the outlook for Australia.

Australia is New Zealand's second largest trading partner, accounting for 18% of all goods and services exports and 16% of imports. Developments in Australia are particularly important for some export industries, including tourism, manufacturing and processed food (Figure 9).

Figure 9: Major exports to Australia by industry as share of total exports by industry (year ending March 2018)



Source: StatsNZ

Summary: growth has strengthened and is expected to remain solid…

Growth in Australia has strengthened over the past year and employment has grown strongly. Inflation has remained subdued and wage growth has been weak. The unemployment rate has gradually declined but remains some way above estimates of full employment.

The outlook is for Australia to continue to grow at around its current pace, or a little below, which is slightly above the economy's medium-term potential. Inflation and wages are expected to increase gradually.

Household debt is high but the pace of increase has slowed. Macro-prudential measures and tighter financial standards, combined with a cooling housing market, are contributing to an easing in credit growth. Although cooling, housing demand is underpinned by solid migration-led population growth and residential construction activity is expected to remain at a high level.

…but trade disputes and sluggish wage growth present risks…

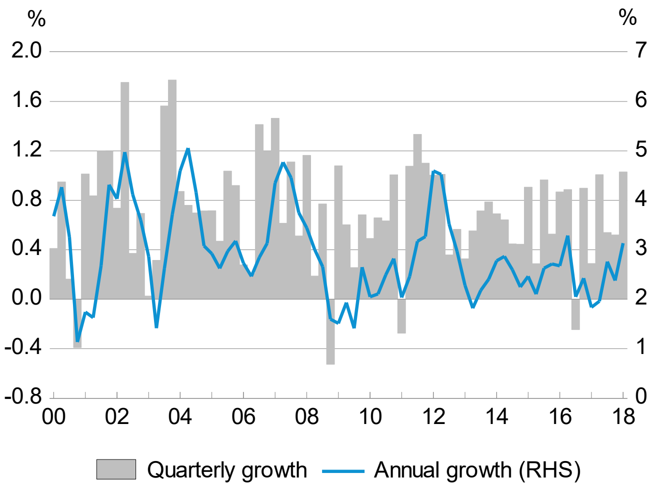
Key risks to the economy appear to be primarily external. A slowdown in global trade, which could result from an intensification and broadening of the trade dispute between the US and China, would likely lead to slower growth in Australia. However, measures announced to date are not expected to have a significant impact. Domestically, the rate at which wage growth picks up is a key area of uncertainty. Continued weak wage growth could be reflected in weaker consumer demand and overall GDP growth.

New Zealand is equally exposed to the threat of a slowdown in global trade, but with the added complication of the indirect effects via the Australian economy. A domestically driven slowdown in the Australian economy would likely lead to slower growth in export demand, but provide support for trans-Tasman net migration flows to remain around current levels.

Broad-based GDP growth…

The Australian economy expanded 3.1% over the year to the March 2018 quarter, which is slightly faster than estimates of the medium term trend growth rate (Figure 10). March quarter growth of 1.0% reflected positive contributions across all the major expenditure components.

Figure 10: Real GDP growth has strengthened



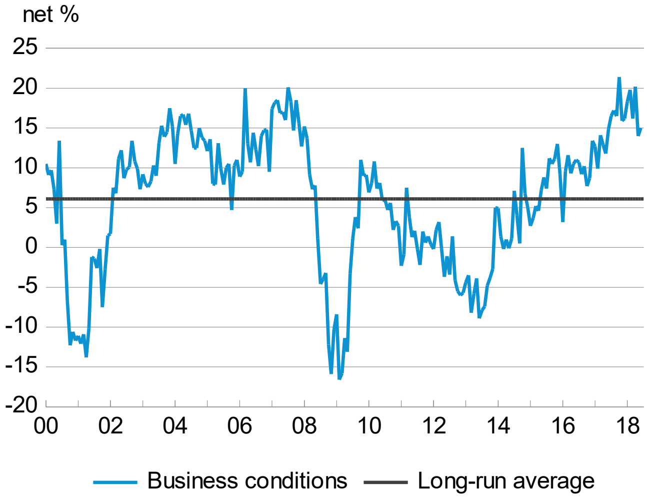
Source: ABS/Haver Analytics

Household consumption growth was modest in the quarter, but held up at 2.9% for the year to March, which is towards the top of the range experienced over the past 5 years or so. However, growth in household spending exceeded household income growth and household saving declined to its lowest rate in over a decade.

…led by the business sector…

Business confidence is high and business investment is growing strongly following a long period of decline from the peaks of the mining investment boom (Figure 11).

Figure 11: Business confidence is high



Source: NAB/Haver Analytics

Mining investment is continuing to fall, but non-mining investment is rising strongly, supported by higher business profits, high levels of business confidence and public sector infrastructure spending.

Public sector spending has picked up at both the federal and state level, particularly in NSW and Victoria where a number of large transport infrastructure projects are underway. In the private sector, tourism related infrastructure is a source of support, while plant and machinery spending has also increased, which is likely, in part, to be a spill over from higher public sector spending.

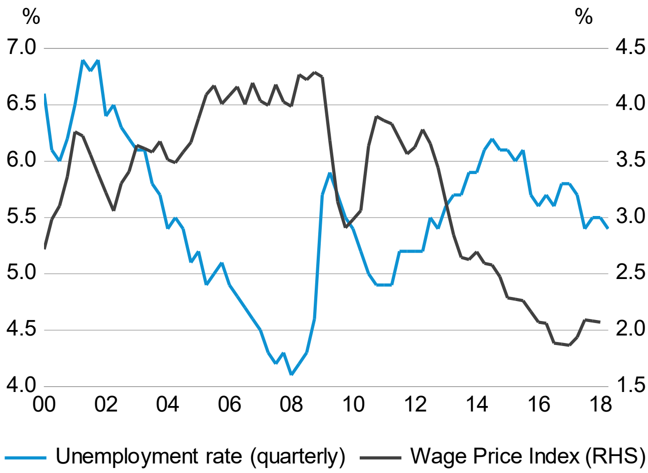
Resource export volumes strengthened in recent quarters as earlier coal supply issues were resolved and more LNG production came on stream. LNG exports are expected to increase further this year, but their contribution to growth is expected to wane over 2019. Exports of tourism and education services have levelled off after several years of strong growth.

Conditions in the labour market are gradually improving…

The unemployment rate has declined gradually over the past two years or so and is expected to continue declining gradually to a rate consistent with full employment, which is generally considered to be around 5% (Figure 12). However, in light of persistent weakness in wage growth, even as the unemployment rate has fallen, the possibility that the full employment rate of unemployment is lower is acknowledged.

Most measures of wage growth have increased, with the closely watched Labour Cost Index (excluding bonuses) rising 2.1% in the year to March 2018 from a low of 1.9% in June 2017 year (Figure 12). Minimum wages are increasing 3% this year and new Enterprise Bargaining Agreements (EBAs) are generally stronger, although many EBAs are on a three-year cycle. More generally, there is some evidence that fewer firms are keeping wages flat and in some industries there are reports of capacity constraints driving wages up.

Figure 12: The unemployment rate has declined and wages growth has picked up

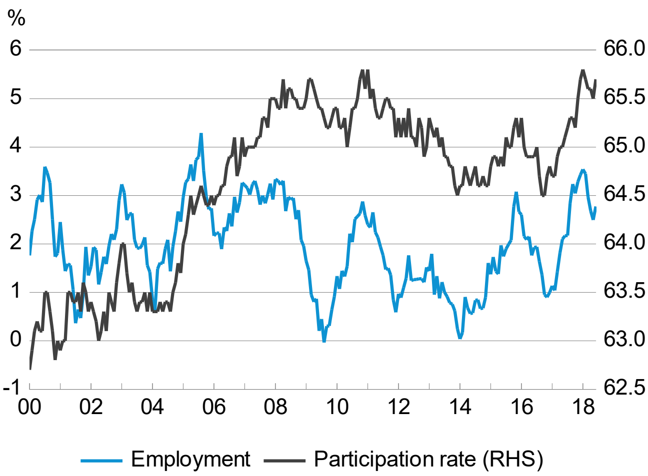


Source: ABS/ Haver Analytics

Employment growth has been strong, rising 2.7% over the past year, driven by increases in health and construction (Figure 13). The former reflects, in part, the expansion of the National Disability Insurance Scheme, (NDIS), which provides support to individuals with significant and permanent disabilities. Further expansion of the NDIS scheme over coming years will continue to support demand for health-related jobs.

In the construction industry, demand for labour is being supported by high levels of residential and infrastructure related construction.

Figure 13: Employment and participation are increasing



Source: Haver Analytics

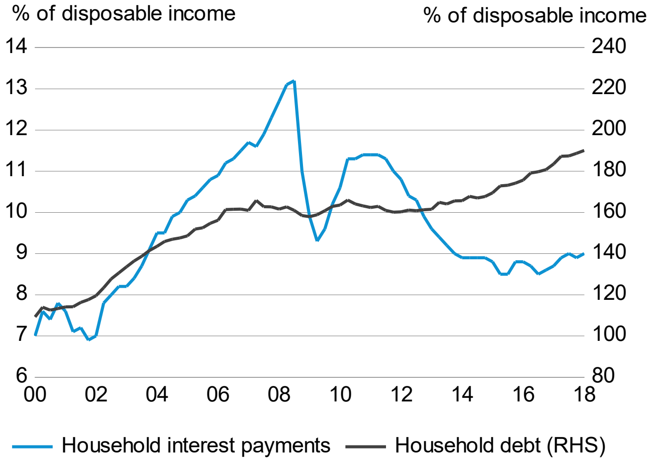
Growth in labour supply has also been strong, with the participation rate rising to near record highs, driven by female labour force participation (Figure 13). To some extent the rise in female participation may reflect increased employment in the health care and social assistance industry, with new employees in this industry, compared with other industries, more likely to be drawn from outside the labour market. An increase in the age that people are eligible to access the age pension, from 65 to 65½ years, in July 2017 may be a factor encouraging people to remain in the labour market.

The Federal Government's May Budget presented a seven year plan for lower and simpler personal income tax structures skewed initially to low and middle income earners. A key feature of the package is a tax rebate at the end of the tax year. At a macro level the Budget shows an expected return to surplus in 2019/20. However, with significant progress having been made in recent years, the overall contractionary effect of further fiscal consolidation is likely to be modest.

…but the housing market is cooling…

The housing market is cooling, with falling prices in Sydney driving a nationwide decline in house prices. Credit growth has slowed in response to tighter lending standards over the past few years. Investor lending had been most affected by the tighter standards. Owner-occupier lending has picked up over the past year, led by an increase in lending to first-home buyers.

Figure 14: Household debt-to income has increased



Source: Haver Analytics

With household debt rising strongly in recent years the slowdown in the housing market is generally perceived as a welcome development, in so far as it indicates that debt to income metrics may stabilise.

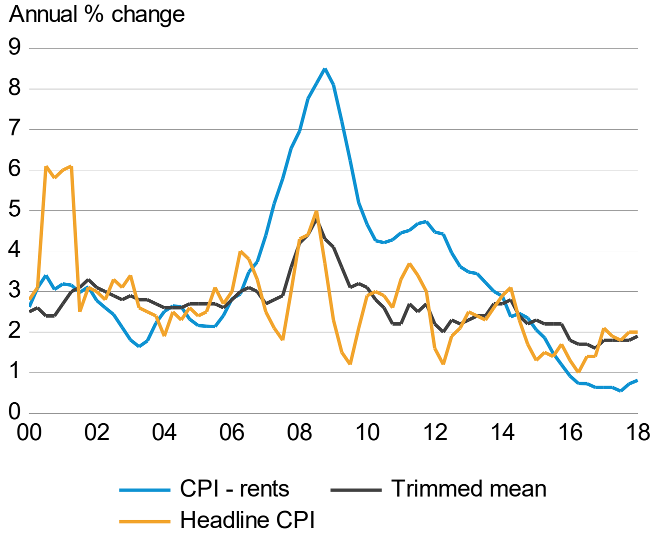
That said, there were few signs of stress in meeting current mortgage debt obligations (Figure 14).

An increasing supply of new dwellings is also likely to be weighing on house prices, with some segments of the market appearing to be oversupplied. New dwelling construction has increased to a high level, driven by growth in higher-density construction. Although dwelling construction eased over the past year, approvals rose, suggesting activity will remain at a high level. Demand continues to be underpinned by strong population growth and low interest rates.

…and inflation pressures remain subdued

The growing supply of housing is also restraining rents and contributing to subdued rates of core inflation, which remain below the Reserve Bank of Australia's (RBA) 2-3% inflation target (Figure 15). Although measures of core inflation have lifted from their lows in early 2015/16, a sustained pick up to the mid-point of the RBA's medium-term target range is expected to be some time away. A period of faster wage growth is likely to be required to achieve the target and, with some spare capacity remaining in the labour market and wage pressures still subdued, inflation is expected to rise only gradually. Consistent with the outlook for inflation, financial markets expect the RBA to keep its policy cash rate steady at 1.5% until mid-to-late 2019.

Figure 15: Inflation pressures are subdued



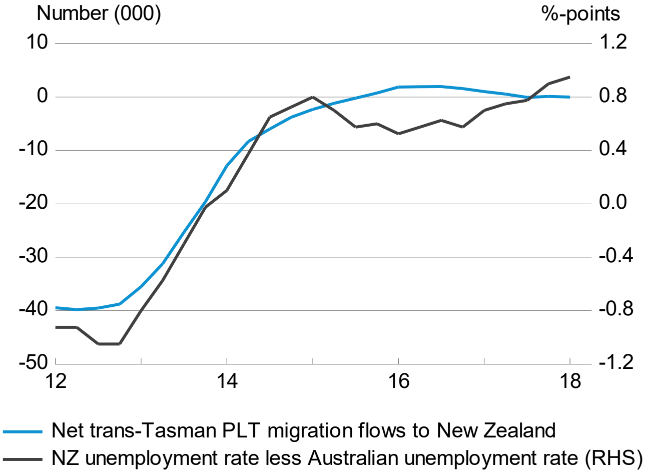
Source: Haver Analytics

Sluggish wage growth and slowing house price inflation pose risks to the outlook…

The combination of slower house price growth, high household debt and sluggish wage growth poses a risk to the outlook for household consumption growth. Wealth effects from rising house prices may have been a factor in the declining saving rate that has supported consumer spending. As support from rising wealth wanes, growth in consumption becomes more dependent on income growth, which is yet to show convincing signs of a breakout from current weakness. In addition, housing market weakness may prove to be deeper or more protracted than currently expected. In this scenario of slower consumption growth, employment growth is likely to be weaker and the unemployment rate higher.

For New Zealand, relative labour market conditions are an important driver of trans-Tasman labour market flows. A higher Australian unemployment rate may contribute to increased net migration inflows (Figure 16).

Figure 16: Relative unemployment rates and net migration



Source: Haver Analytics

… and international trade tensions are high

International trade tensions have risen as the US and China raise tariff barriers against each other. To date, announced tariff measures affect around $US106 billion of US imports, however the US has threatened to raise tariffs on a further $US700 billion of imports, including automobiles from the EU and other countries. Although measures implemented to date are not expected to have a significant impact on global trade, the risks to trade are mounting as more goods are identified as potential targets for tariffs. However, Australia is expected to be relatively well positioned given most of Australia's exports to China are not re-exported. The bigger impact is expected for those involved in global value chains with the China and the US, such as Taiwan, Malaysia and South Korea.

Although the direct effects of tariff measures announced by the US and China to date are expected to be minor, the Australian and New Zealand economies are likely to be significantly impacted should there be a more generalised downturn in commodity prices. A fall in the exchange rate would likely help to buffer the impacts of the shock, but trans-Tasman trade in goods and services would likely suffer as income growth slowed. New Zealand visitors are an important part of the Australian tourisms industry and vice versa, and it is likely these flows would ease. Australia is also a major New Zealand goods export destination accounting for 16% of total goods trade but significantly more in some industries.

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

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New Zealand Key Economic Data

Quarterly Indicators

02 August 2018

		2016Q4	2017Q1	2017Q2	2017Q3	2017Q4	2018Q1	2018Q2
Gross Domestic Product (GDP)								
Real production GDP	qtr % chg[1]	0.4	0.8	0.9	0.6	0.6	0.5	...
	ann ave % chg	4.0	3.7	3.3	3.0	2.8	2.7	...
Real private consumption	qtr % chg[1]	0.8	1.2	0.8	0.9	1.2	0.0	...
	ann ave % chg	5.1	5.5	5.2	4.6	4.4	3.8	...
Real public consumption	qtr % chg[1]	1.1	1.1	1.1	2.7	-0.1	0.5	...
	ann ave % chg	1.6	1.9	3.0	4.2	4.6	4.9	...
Real residential investment	qtr % chg[1]	0.2	-1.2	-0.8	2.9	0.5	-0.2	...
	ann ave % chg	11.8	9.5	5.0	2.5	0.7	0.6	...
Real non-residential investment	qtr % chg[1]	0.5	1.1	1.0	1.1	3.9	0.6	...
	ann ave % chg	4.1	3.9	3.9	4.3	4.8	5.5	...
Export volumes	qtr % chg[1]	-2.2	0.7	4.5	0.6	-0.3	-0.1	...
	ann ave % chg	1.6	0.7	0.0	0.5	2.3	3.9	...
Import volumes	qtr % chg[1]	1.1	1.5	0.5	2.6	3.7	1.2	...
	ann ave % chg	3.4	5.1	6.0	6.2	6.7	7.0	...
Nominal GDP - expenditure basis	ann ave % chg	6.0	6.1	6.4	6.8	6.5	6.0	...
Real GDP per capita	ann ave % chg	1.8	1.6	1.2	0.8	0.7	0.6	...
Real Gross National Disposable Income	ann ave % chg	5.3	4.8	4.5	4.4	3.5	3.4	...
External Trade								
Current account balance (annual)	NZ$ millions	-5,985	-7,156	-7,145	-7,013	-7,697	-7,910	...
	% of GDP	-2.2	-2.6	-2.6	-2.5	-2.7	-2.8	...
Investment income balance (annual)	NZ$ millions	-7,133	-7,700	-7,952	-8,471	-9,430	-9,525	...
Merchandise terms of trade	qtr % chg	5.8	3.9	1.1	1.3	1.4	-1.8	...
	ann % chg	6.7	6.5	9.7	12.6	7.9	2.0	...
Prices								
CPI inflation	qtr % chg	0.4	1.0	0.0	0.5	0.1	0.5	0.4
	ann % chg	1.3	2.2	1.7	1.9	1.6	1.1	1.5
Tradable inflation	ann % chg	-0.1	1.6	0.9	1.0	0.5	-0.4	0.1
Non-tradable inflation	ann % chg	2.4	2.5	2.4	2.6	2.5	2.3	2.5
GDP deflator	ann % chg	4.2	3.8	2.9	3.6	3.1	1.3	...
Consumption deflator	ann % chg	0.8	1.6	1.3	1.5	1.5	0.6	...
Labour Market								
Employment (HLFS)	qtr % chg[1]	0.9	1.1	-0.1	2.2	0.4	0.6	0.5
	ann % chg[1]	5.8	5.7	3.1	4.1	3.7	3.1	3.7
Unemployment rate	%[1]	5.3	4.9	4.8	4.6	4.5	4.4	4.5
Participation rate	%[1]	70.5	70.6	70.1	71.1	70.9	70.8	70.9
LCI salary & wage rates - total (adjusted)[5]	qtr % chg	0.4	0.4	0.4	0.6	0.4	0.3	0.5
	ann % chg	1.6	1.6	1.7	1.8	1.8	1.8	1.9
QES average hourly earnings - total[5]	qtr % chg	-0.1	0.5	0.6	1.2	0.8	0.9	0.1
	ann % chg	1.3	1.5	1.6	2.2	3.1	3.5	3
Labour productivity[6]	ann ave % chg	-1.3	-2.7	-1.7	-1.5	-0.7	-0.3	...
Retail Sales								
Core retail sales volume	qtr % chg[1]	1.4	1.4	1.9	0.5	1.8	0.6	...
	ann % chg	4.9	4.9	5.2	5.2	5.6	4.8	...
Total retail sales volume	qtr % chg[1]	1.4	1.5	1.8	0.3	1.4	0.1	...
	ann % chg	4.8	5.4	5.8	4.6	5.4	3.0	...
Confidence Indicators/Surveys								
WMM - consumer confidence[3]	Index	113	112	113	112	107	111	109
QSBO - general business situation[4]	net %	24.9	16.3	16.8	9.0	-14.9	-8.5	-23.4
QSBO - own activity outlook[4]	net %	25.7	25.0	25.8	23.3	17.8	16.7	14.3

Monthly Indicators

		2018M01	2018M02	2018M03	2018M04	2018M05	2018M06	2018M07
External Sector								
Merchandise trade - exports	mth % chg[1]	-16.4	2.6	-3.2	6.0	-1.0	2.5	...
	ann % chg[1]	8.6	10.7	4.5	5.4	9.1	4.6	...
Merchandise trade - imports	mth % chg[1]	0.8	-5.6	6.8	0.7	-3.9	6.8	...
	ann % chg[1]	18.6	4.9	14.3	14.5	6.3	12.9	...
Merchandise trade balance (12 month total)	NZ$ million	-3286	-3056	-3468	-3820	-3675	-4031	...
Visitor arrivals	number[1]	313,810	323,970	318,740	314,820	322,460	311,280	...
Visitor departures	number[1]	314,520	319,320	327,080	321,390	316,630	318,530	...
Housing								
Dwelling consents - residential	mth % chg[1]	0.3	6.3	13.0	-3.8	6.9	-7.6	...
	ann % chg[1]	9.4	-0.2	5.3	29.6	21.9	9.1	...
House sales - dwellings	mth % chg[1]	4.8	0.4	-3.5	1.4	-0.9	-7.5	...
	ann % chg[1]	5.5	4.3	-7.6	9.7	4.9	-1.6	...
REINZ - house price index	mth % chg	0.4	0.6	0.4	-0.2	-0.3	0.0	...
	ann % chg	3.5	3.9	4.1	3.7	3.7	3.8	...
Private Consumption								
Electronic card transactions - total retail	mth % chg[1]	1.4	-0.4	1.5	-2.2	0.6	0.8	...
	ann % chg	4.1	4.0	6.7	1.4	4.2	4.9	...
New car registrations	mth % chg[1]	2.8	-8.4	-4.1	0.2	12.3	-6.8	...
	ann % chg	6.2	-4.2	-11.9	-9.0	-0.6	-4.9	...
Migration								
Permanent & long-term arrivals	number[1]	11,460	10,190	10,810	10,510	10,780	10,600	...
Permanent & long-term departures	number[1]	5,220	5,280	5,440	5,600	5,700	5,750	...
Net PLT migration (12 month total)	number	70,147	68,943	67,984	67,038	66,243	64,995	...
Commodity Prices								
Brent oil price	US$/Barrel	69.08	65.32	66.02	72.11	76.98	74.40	...
WTI oil price	US$/Barrel	63.66	62.21	62.76	66.26	69.99	67.33	...
ANZ NZ commodity price index	mth % chg	-3.0	2.4	2.1	1.2	5.0	-1.1	...
	ann % chg	4.5	6.4	5.1	5.8	6.8	7.4	...
ANZ world commodity price index	mth % chg	0.7	2.8	1.2	1.0	1.5	-1.0	...
	ann % chg	4.1	5.0	5.8	7.1	5.4	2.2	...
Financial Markets								
NZD/USD	$[2]	0.7255	0.7312	0.7257	0.7258	0.6953	0.6941	*0.6805*
NZD/AUD	$[2]	0.9123	0.9277	0.9343	0.9432	0.9239	0.9265	*0.9172*
Trade weighted index (TWI)	June 1979 = 100[2]	74.90	75.09	74.72	74.88	73.01	73.50	*73.30*
Official cash rate (OCR)	%	1.75	1.75	1.75	1.75	1.75	1.75	1.75
90 day bank bill rate	%[2]	1.88	1.91	1.93	2.01	2.02	2.01	*1.91*
10 year govt bond rate	%[2]	2.88	2.97	2.89	2.83	2.78	2.90	*2.76*
Confidence Indicators/Surveys								
ANZ - business confidence	net %	...	-19.0	-20.0	-23.4	-27.2	-39.0	-44.9
ANZ - activity outlook	net %	...	20.4	21.8	17.8	13.6	9.4	3.8
ANZ-Roy Morgan - consumer confidence	net %	126.9	127.7	128.0	120.5	121.0	120.0	118.4
Performance of Manufacturing Index	Index	55.2	53.4	53.1	59.1	54.4	52.8	...
Performance of Services Index	Index	56.0	55.2	58.7	55.7	57.1	52.8	...

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