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MONTHLY ECONOMIC REVIEW

July 2014

(Latest data as at 7 July)

Parliamentary Library Research Paper

A Overview

Recent trend

	2012/13	2013/14	
Economic Growth	2.3%	3.3%	Annual average GDP Growth (March year)
Unemployment	6.2%	6.0%	Unemployment Rate (March quarter)
Inflation	0.9%	1.5%	Annual Inflation Rate (March year)
Current Account Deficit	\$8.3b	\$6.3b	Current Account Deficit (March year)
Interest Rates	2.64%	3.52%	90 Day Bank Bills (June month)

Latest data and events

Gross domestic product (GDP) expanded by one percent in the March 2014 quarter, primarily driven by construction activity and mining. Construction activity levels for the March quarter were at the highest ever level. In the quarter, exports increased by 3.1 percent due primarily to an 18.6 percent rise in agriculture and fishing primary products after large falls in the two previous quarters. On an annual average basis, the economy expanded by 3.3 percent, the biggest March year increase since March 2006 with ten of the 16 industries having annual growth of at least two percent.

New Zealand's current account deficit (seasonally adjusted) for the March 2014 quarter was \$585 million, \$336 million less than the December 2013 quarter deficit due to increased exports of goods and services. For the year ended March 2014, the current account deficit was \$6.3 billion (equivalent to 2.8 percent of GDP). Our net international investment liability position (the net amount we owe to the rest of the world) was \$148 billion, equivalent to 65.3 percent of GDP.

Reserve Bank Governor, Graeme Wheeler, increased the official cash rate by a further 0.25 percent in June to 3.25 percent. The Governor noted that "*inflationary pressures are expected to increase*" while "*the speed and extent to which the OCR will need to rise will depend on future economic and financial data, and its implications for inflationary pressures*".

International commodity prices for New Zealand's main commodity exports recorded a fourth successive monthly decline in June, down 0.9 percent in the month (down 1.1 percent after currency appreciation is taken into account), according to the *ANZ Commodity Price Index*. Dairy and forestry prices have fallen in particular, while conversely meat prices are at a fourteen year high. Latest Fonterra *Global Dairy Auction* results in early July showed a fall in dairy product prices.

Outlook

Economic indicators suggest continuing economic growth for 2014 and into 2015. The Reserve Bank *Monetary Policy Statement* for June 2014 forecast a growth rate of 3.5 percent in the year to March 2015, up from 3.3 percent in the year to March 2014, increasing the likelihood of an increase in interest rates to ensure inflation remains in Reserve Bank's target band of 1 – 3 percent. NZIER's *Quarterly Predictions* forecast that while the unemployment rate should decline gradually there is unevenness across regions and sectors.

Topic of the month: Taxes and levies on petrol

B Economic Growth

Background

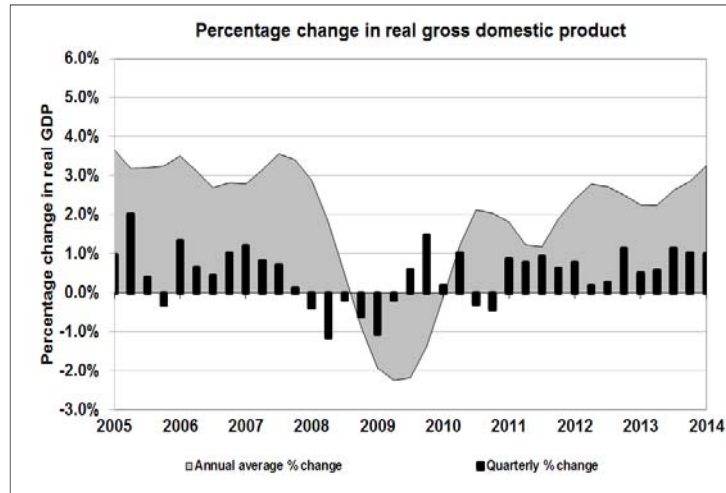
A country's gross domestic product (GDP) is a measure of economic activity during a set period of time, normally reported on a quarterly and an annual basis. It is the sum of money values of all final goods and services produced in an economy over a set period. The primary indicator used for tracking economic performance over time is known as real gross domestic product, or real GDP. Real GDP is gross domestic product adjusted for changes in prices. New Zealand's official gross domestic product figures are sourced from Statistics New Zealand.

Gross domestic product

Economic activity increased by one percent in the March 2014 quarter, and by 3.3 percent in the year to March 2014.

In the March quarter, the most significant contribution to growth came from the the construction industry (up 12.5 percent) and the mining industry (up 6.3 percent). The increase in the construction activity was the second highest quarterly increase ever. Mining activity was primarily oil and gas extraction.

There was a 3.1 percent rise in the volume of exports over the quarter, driven by an increase in agriculture and fishing primary products. Dairy exports fell by 3.3 percent. Household consumption was flat in the quarter, although spending on durable goods (such as clothing and audio-visual equipment) and services increased by 1.8 percent.



Other data

The *Retail Trade Survey* for the first quarter of 2014 showed strong sales across many categories although supermarket sales were weak.

Business confidence fell in June, as surveyed by the *ANZ Business Outlook Survey*. A net 43 percent of firms expect an improvement in trading conditions in 12 months' time, down from a net 54 percent in May's survey. Consumer sentiment remains high according to the June *ANZ-Roy Morgan* survey.

The seasonally adjusted *BNZ-BusinessNZ Performance of Services Index* for May was down from April at 54.2 points, averaging 56.4 so far in 2014.

Year ended March 2014	Nominal GDP
Expenditure GDP	\$226,551 million
GDP per capita	\$50,457

Source: Statistics New Zealand.

ANZ Business Outlook Survey	May-14	Jun-14
Net % expecting an improvement in business conditions in 12 months' time	53.5	42.8
Net % expecting an improvement in their own firm's activity in 12 months' time	51.0	45.8

Source: ANZ Bank, Business Outlook survey.

Outlook

The NZIER has forecast that the economic recovery will continue to strengthen. Its *Quarterly Predictions* has the economy expanding by 2.9 percent in year to March 2015. The NZIER *Consensus Forecasts* predict growth of 3.8 percent in the year to March 2015 while Westpac Bank expects the economy to expand by 3.6 percent in the year ended June 2014, rising to 3.8 percent for the 2014 calendar year.

GDP growth (%)	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Annual (year-on-year)	2.3	2.2	2.6	2.7	3.3
Quarterly (seasonally adjusted)	0.5	0.6	1.1	1.0	1.0

Source: Statistics New Zealand.

Next Release: *Gross Domestic Product: June 2014 quarter.*

Date: 18 September 2014

C Employment and Unemployment

Background

The unemployment rate measures the number of people unemployed as a proportion of those in the labour force. The labour force is the number of people of working age (15 years and over) who are working for wages or a salary, working for a family business, or who are unemployed and seeking work. In New Zealand, the official unemployment rate is sourced from Statistics New Zealand's quarterly Household Labour Force Survey.

Employment and unemployment

New Zealand's unemployment rate was six percent in the March 2014 quarter, with 147,000 people unemployed in seasonally adjusted terms.

During the March quarter, both the number of those employed and the labour force (which also includes those unemployed) rose by 0.9 percent. As a result, despite a rise in employment over the quarter, the unemployment rate remained steady.

The labour force participation rate (which measures the proportion of those aged 15 years and over who are in the labour force), at 69.3 percent in the March quarter, is at its highest level since the current survey commenced in the 1980s.

In the March 2014 quarter, regional unemployment rates ranged from 3.3 percent in the Canterbury region to 8.4 percent in the Gisborne/Hawkes Bay region. When compared with the same quarter in 2013, the Waikato, Taranaki and Southland regions all had higher unemployment rates in the March 2014 quarter.

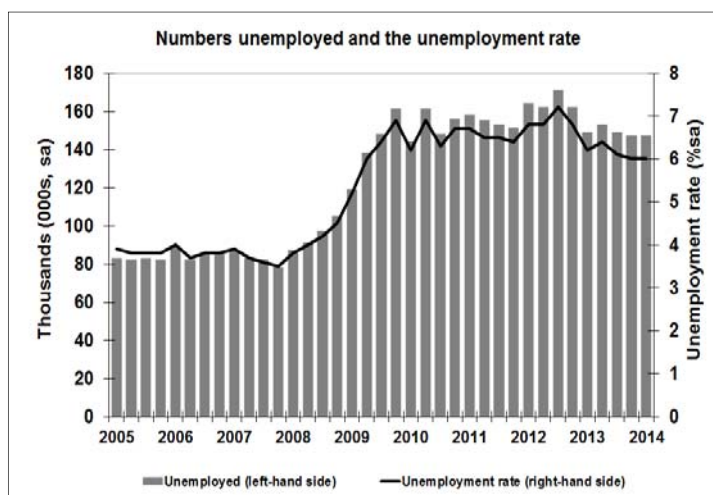
Other data

Following four consecutive months in which the number of job advertisements rose, they fell 5.2 percent in May according to the *ANZ New Zealand Job Ads* survey. The ANZ Bank speculated that the fall in advertisements may be due to recent interest rate rises, and firms taking a wait-and-see approach in regards to expanding employment within their business.

The Ministry of Business, Innovation & Employment's *Jobs Online* reported a 2.9 percent fall in online vacancies in May in seasonally adjusted terms, with a 3.9 percent fall in skilled job vacancies. However, the number of vacancies remain 7.6 percent higher than at the same time last year.

Outlook

Continuing employment growth has been forecast. As a result, the ANZ Bank has forecast an unemployment rate of 5.5 percent by the end of the year. *NZIER Consensus Forecasts* has employment expanding by 2.3 percent over the year to March 2015, falling to 1.6 percent growth in the following year. An unemployment rate of 5.3 percent has been forecast in March 2015, falling to 5.1 percent in the following year.



ANZ Business Outlook Survey	May-14	Jun-14
Net % expecting to increase employment in their business in 12 months*	29.8	23.6
Net % expecting the unemployment rate to rise in 12 months*	-40.6	-36.2

*equal to the % of respondents expecting an increase minus the % expecting a decrease. Source: ANZ Bank.

Quarter	Mar-13	Mar-14
Average ordinary time weekly earnings for FTEs (pre-tax) (\$)	\$1,031.39	\$1,064.55
Labour Cost Index - % change in salary and wage rates (including overtime) from the same quarter of the previous year	+1.7	+1.6

Source: Statistics New Zealand.

Household Labour Force Survey	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Unemployment Rate (seasonally adjusted, %)	6.2	6.4	6.1	6.0	6.0
Employment Growth (annual, %)*	0.4	0.7	2.4	3.0	3.7

*change since the same quarter of the previous year based on seasonally adjusted data. Source: Statistics New Zealand.

Next Release: *Household Labour Force Survey: June 2014 quarter. Date: 6 August 2014*

D Inflation

Background

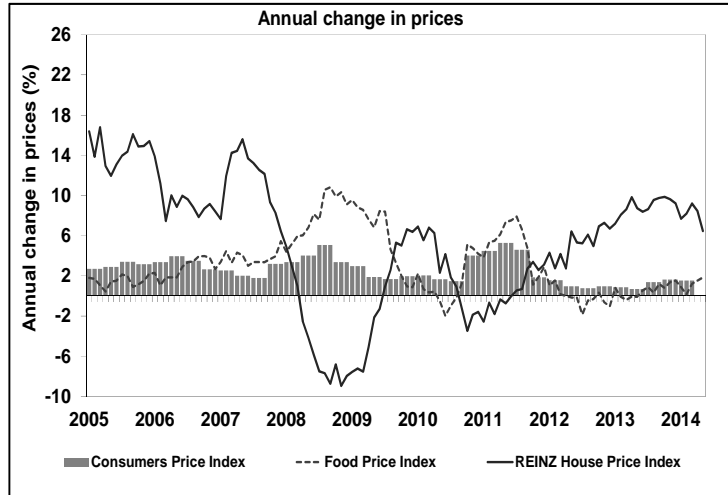
Inflation is the change in prices of goods and services over a certain period of time. The official rate of consumer inflation is measured by Statistics New Zealand's Consumers Price Index (CPI). The CPI tracks the price of a basket of household goods and services over time.

Consumers Price Index

Annual inflation in the year ended in the March 2014 quarter was 1.5 percent, with the price of tradable goods and services falling by 0.6 percent over the year, while non-tradable goods and services prices rose by three percent.

Higher prices within the housing and household utilities group accounted for just over half the increase in inflation over the year. Within this group, costs associated with the purchase of new housing rose by 5.1 percent over the year, while housing rental costs rose by two percent. Also during the year, cigarette and tobacco prices rose by 10.2 percent, driven by higher excise duties on tobacco and tobacco products from 1 January 2014.

This increase in cigarette and tobacco prices were the largest upward contributor to consumer prices in the March 2014 quarter. In the quarter, consumer prices rose by 0.3 percent overall. Costs associated with the purchase of new housing rose by 1.2 percent in the quarter, with costs rising by 1.7 percent in Auckland and by 1.5 percent in Canterbury. Statistics New Zealand noted that this was the second consecutive quarter in which costs associated with new housing have risen to a larger extent in Auckland than in Canterbury. Rental costs in Canterbury rose by 1.9 percent over the March quarter, and by 0.6 percent nationally.



Other data

The excise duty on petrol rose by three cents per litre from 1 July, while road user charges for diesel vehicles (which are not subject to the excise duty on the price of diesel) were also increased.

There were 6,572 dwellings sold in May according to the Real Estate Institute of New Zealand, with a national median sale price of \$430,000. The REINZ Stratified Housing Price Index for New Zealand rose by 6.5 percent over the year.

Outlook

The Reserve Bank expects the annual rate of inflation to peak at 2.1 percent over its projection period out to June 2017. Respondents to the latest *NZIER Consensus Forecasts* expect a higher rate of inflation, rising to 2.4 percent by 2016.

Annual Percentage Change (%)	May-14	Jun-14
Quotable Value – Residential property values*	8.2	8.0
REINZ Stratified Median Housing Price Index**	6.5	n/a
Food Price Index**	1.8	n/a

*change since the same three months ended in the month of the previous year
 **change since the same month of the previous year. Sources: Quotable Value; REINZ; Statistics New Zealand

ANZ Business Outlook Survey	May-14	Jun-14
Net % of respondents expecting to increase prices in 3 months' time*	27.5	24.8
Inflation expected in 12 months' time	2.55	2.52

*equal to the % of respondents expecting an increase minus the % expecting a decrease. Source: ANZ Bank.

Inflation (%)	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Consumers Price Index - Annual	0.9	0.7	1.4	1.6	1.5
Tradables inflation	-1.1	-1.6	-0.5	-0.3	-0.6
Non-tradables inflation	2.4	2.5	2.8	2.9	3.0
CPI - quarterly	0.4	0.2	0.9	0.1	0.3

Source: Statistics New Zealand.

Next Release: Consumers Price Index: June 2014 quarter.

Date: 16 July 2014

Background

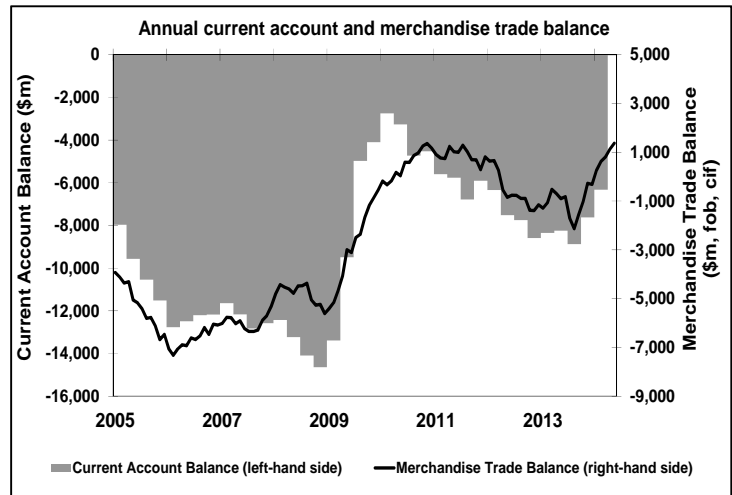
The balance of payments is the record of the receipts and payments between a country's residents and the rest of the world, over a given period. The current account is that part of a country's balance of payments which embraces its transactions of goods, services, international income, and current transfers (e.g. foreign aid). A "balance of payments deficit" refers to a deficit of the current account.

Current account deficit

New Zealand's current account deficit totalled \$6,323 million in the year ended March 2014, equivalent to 2.8 percent of GDP. This compares with a deficit equivalent to 3.9 percent of GDP a year earlier.

In the March 2014 quarter, the current account deficit totalled \$585 million in seasonally adjusted terms (compared with a deficit of \$921 million in the December quarter). The smaller deficit was driven by an increase in merchandise exports, along with an increase in spending by overseas visitors to New Zealand.

New Zealand's net international investment position, the net amount we owe the rest of the world, totalled \$147,964 million as at 31 March 2014, equivalent to 65.3 percent of GDP.



Other data

International commodity prices fell by 0.9 percent in June according to the latest *ANZ Commodity Price Index*, with international prices 0.3 percent lower than a year ago. Once changes in the New Zealand dollar have been taken into account, international commodity prices are 7.8 percent lower than a year earlier.

Annual Change (%)	May-14	Jun-14
World Commodities Prices*	-3.1	-0.3
NZ\$ Commodities Prices*	-6.0	-7.8
Overseas Visitors**	5.9	n/a

*change since the same month of the previous year. **change since the previous year-end. Sources: Statistics New Zealand; ANZ.

International dairy product prices fell 4.9 percent according to the latest Fonterra *Global Dairy Trade* auction results. Prices have fallen in nine of the last ten auctions. As a result, international dairy prices are at their lowest price since January 2013.

Outlook

The *NZIER Consensus Forecasts* has forecast a current account deficit of \$10,100 million for the year ended March 2015. The Reserve Bank in its June *Monetary Policy Statement* has forecast a deficit equivalent to 4.3 percent of GDP in the year ended March 2015, rising to 5.9 percent of GDP in the following year.

Balances (\$m)	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	May-14
Quarterly Current Account (seasonally adjusted)	-1,784	-2,220	-2,564	-921	-585	n/a
Annual Current Account	-8,349	-8,244	-8,868	-7,623	-6,323	n/a
Goods	567	267	-294	1,306	2,893	n/a
Services	1,060	1,101	1,099	1,114	1,233	n/a
Income	-9,484	-9,026	-9,084	-9,522	-9,932	n/a
Current transfers	-492	-586	-589	-521	-517	n/a
Net international investment position (as at date)	-151,197	-151,279	-149,434	-146,908	-147,964	n/a
Annual Merchandise Trade Balance (fob-cif)*	-521	-819	-1,559	-317	801	1,373

* CIF – Cost of goods imported, including insurance and freight to New Zealand. FOB – Free on board, the value of goods at New Zealand ports before export. Source: Statistics New Zealand.

Next Release: *Balance of Payments: June 2014 quarter.* **Date:** 17 September 2014

Background

The trade weighted index (TWI) is an index of the New Zealand dollar's value against a basket of five overseas currencies, where each currency is weighted by a combination of the size of the associated country's trade with New Zealand (including the Euro group of countries) and their gross domestic product. The official cash rate (OCR) is the interest rate that applies to overnight borrowing and lending between banks and the Reserve Bank. It is currently a key operational feature of monetary policy in New Zealand. The NZX 50 is the main share index of the New Zealand Exchange. It tracks changes in the share prices of the top 50 publicly listed companies by free float market capitalisation on the NZX market. It is a gross index, so it includes the payout of dividends in its calculation.

Recent trends & data

Reserve Bank Governor, Graeme Wheeler, lifted the official cash rate by a further 25 basis points in June, the third increase this year. The official cash rate is now 3.25 percent, having previously remained at 2.5 percent from March 2011 through to March 2014.

In raising the official cash rate, the Governor said that "inflationary pressures are expected to increase", and that the Bank expects to further tighten monetary policy, depending on "...future economic and financial data, and its implications for inflationary pressures".

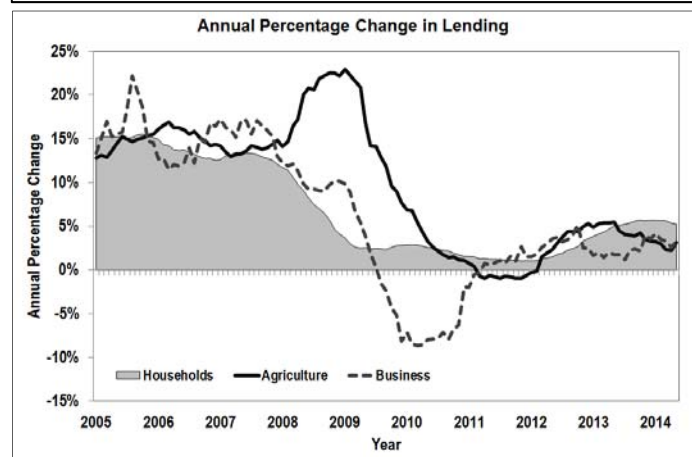
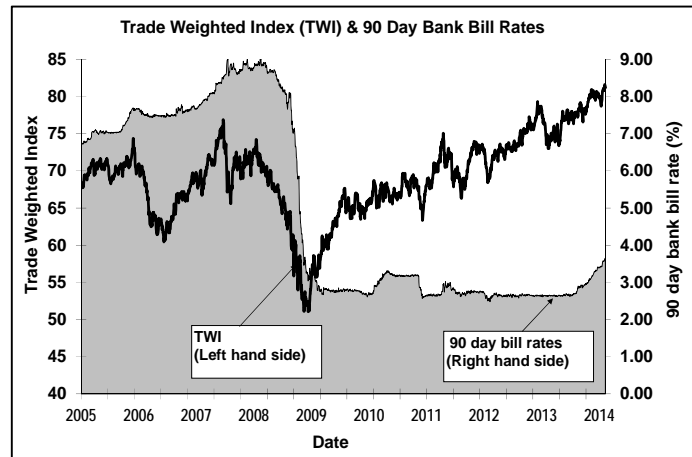
A couple of retail companies listed on the NZX have issued a downgrade of their profit forecasts for their current financial year, due to the impact of warmer winter conditions on sales revenue (particularly on their winter stock).

The exchange rate, on a trade weighted index (TWI) basis, reached a new high since it was floated on a monthly average basis in June. The TWI averaged 80.31 index points.

Household lending rose by 0.4 percent in May on a seasonally adjusted basis, with high loan-to-value (LVR) lending accounting for 5.3 percent of new mortgage lending undertaken during the month (well within the target of ten percent set by the Reserve Bank).

Outlook

The Reserve Bank announces its next official cash rate decision on 24 July. The market is still pricing in a further 25 basis point increase, followed by a pause in monetary policy tightening in September. The Reserve Bank has forecast a 90-day bank bill rate of 3.6 percent in the September 2014 quarter, rising to four percent in the December quarter.



Core Crown borrowing as at	30-Apr-14 (\$m)	30-Apr-14 (%GDP)
Gross sovereign-issued debt *	83,039	37.5
Net core Crown debt **	62,252	28.1

*Excluding Reserve Bank settlement cash and Reserve Bank bills.

** Excluding NZ Super Fund and other advances. Source: The Treasury.

Monthly averages	Feb-14	Mar-14	Apr-14	May-14	Jun-14
90 Day Bank Bill rate	2.93	3.05	3.24	3.38	3.52
10 Year Government Bond yields (secondary market)	4.57	4.58	4.55	4.29	4.42
Effective mortgage rate	5.52	5.55	5.64	5.73	n/a
Business lending rate	5.43	5.53	5.58	5.67	n/a
Trade Weighted Index (TWI) exchange rate	77.96	79.68	80.20	80.09	80.31
NZX 50 index	4896	5110	5110	5173	5162

Sources: Reserve Bank; NZX.

Next Official Cash Rate (OCR) decision: 24 July 2014

Background

New Zealand's economic growth rate, unemployment rate and central bank interest rates are compared with our main OECD trading partners. The first table below illustrates the seasonally adjusted quarterly growth rates in economic activity. The second table below shows the harmonised unemployment rate in each OECD country/area, while the third shows the main central bank interest rates for various countries (and currency group in the case of the Euro), along with the date and direction of the latest movement for each.

Economic growth

In the March 2014 quarter, the United States economy contracted by 0.7 percent, pulling down the average economic growth rate within the OECD area to 0.2 percent for the quarter. A decline in exports and private sector investment were the major drivers of the contraction in the United States economy.

The Reserve Bank has forecast that New Zealand's trading partners economies have expanded by 3.6 percent in the year ended March 2014, with economy growth rising to 3.8 percent in the following year. Economic growth in China, while remaining high, has slowed over recent quarters from 2.3 percent in the September 2013 quarter to 1.4 percent in the March 2014 quarter.

Quarterly economic growth rates (%)			
Country*	Sep-13	Dec-13	Mar-14
Australia	0.7	0.8	1.1
Japan	0.3	0.1	1.6
NEW ZEALAND	1.1	1.0	1.0
United Kingdom	0.8	0.7	0.8
United States	1.0	0.7	-0.7
Euro area	0.1	0.3	0.2
OECD Total	0.7	0.5	0.2
China	2.3	1.7	1.4

Notes: * Seasonally adjusted growth rate from the previous quarter.
Source: OECD.

Unemployment

The harmonised unemployment rate within the OECD area fell 0.1 percentage point to 7.4 percent in April, compared with a rate of 7.5 percent in the preceding three months. The youth unemployment rate was 14.8 percent in April.

Australia's unemployment rate remained at 5.8 percent in May in seasonally adjusted terms. The unemployment rate ranged from five percent in Western Australia to 7.5 percent in Tasmania. The unemployment rate rose during 2013 and in early 2014 from 5.4 percent in January 2013 to six percent in January and February 2014.

Harmonised unemployment rates (%)			
Country	Mar-14	Apr-14	May-14
Australia	5.8	5.8	5.8
Japan	3.6	3.6	3.5
NEW ZEALAND	<i>n/a</i>	6.0 (qtr)	<i>n/a</i>
United Kingdom	6.6 (Feb)	<i>n/a</i>	<i>n/a</i>
United States	6.7	6.3	6.3
OECD Total	7.5	7.4	<i>n/a</i>

Sources: OECD; Australian Bureau of Statistics.

Central banks

The Australian Reserve Bank left its cash rate steady at 2.5 percent in early July, with Reserve Bank Governor Glenn Stevens commenting that monetary policy remained accommodative, with inflation "...expected to be consistent with the 2 – 3 per cent target over the next two years".

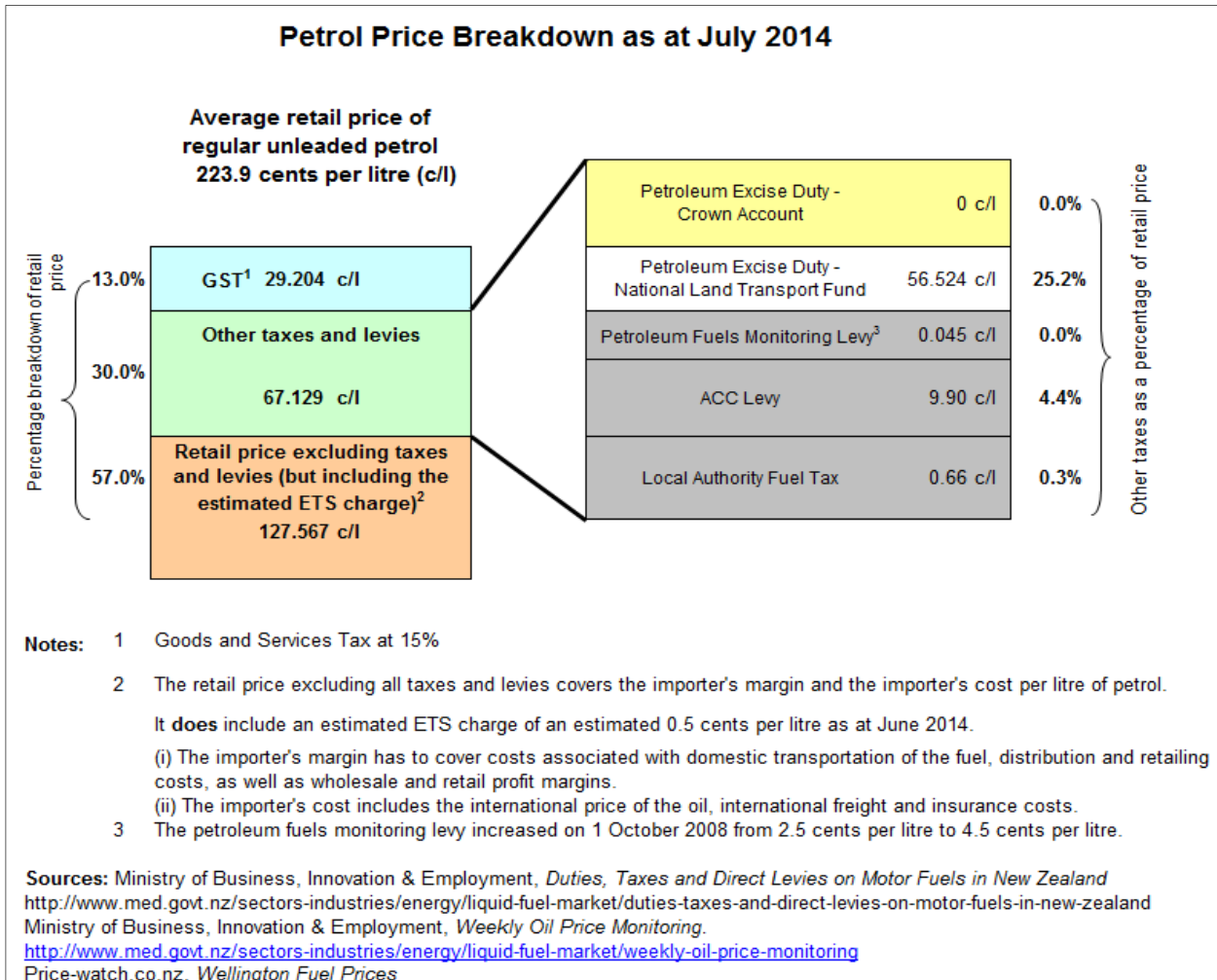
The United States Federal Reserve announced in June that it was reducing the size of its quantitative easing programme by US\$10 billion per month. It will now purchase \$35 billion per month of agency mortgage-backed securities and Treasury securities. This compares with a monthly purchase of US\$85 billion at the peak of the quantitative easing programme.

Central Bank interest rates (as at 7 July 2014)				
Central Bank	Key Rate	Interest Rate (%)	Effective from	Direction (Basis points)
Australia	Cash Rate	2.50	7-August-13	-25
China	Benchmark lending rate	6.00	6-Jul-12	-31
European Central Bank	Main Refinance Rate	0.15	11-Jun-14	-10
Japan	Uncollateralized overnight rate	0.00 - 0.10	5-Oct-10	-10
NEW ZEALAND	Official Cash Rate	3.25	12-Jun-14	+25
United Kingdom	Bank Rate	0.50	5-Mar-09	-50
United States	Federal Funds Rate	0.00 – 0.25	16-Dec-08	-75

Source: Central Bank interest rates as at the date stated.

Taxes and levies on petrol

Taxes and levies on a litre of petrol account for approximately 43 percent of the overall price. With a retail price of 223.9 cents per litre in early July, 96.3 cents per litre was in taxes and levies (including GST). From 1 July 2014, the petroleum excise duty on petrol rose by three cents a litre to 56.524 cents per litre. The entire amount raised through excise duties goes into the National Land Transport Fund. According to the *Budget Economic and Fiscal Update 2014*, a forecast \$1,702 million is expected to be raised through the excise duty on petroleum in the year ended June 2015. This includes \$936 million in petroleum excise duty on domestic production, and a further \$766 million on petroleum imports. There is a 9.9 cents per litre ACC levy on the price of petrol, a local authority fuel tax of 0.66 cents per litre, and a petroleum fuels monitoring levy of 0.045 cents per litre. The ETS charge per litre of petrol is currently estimated at 0.5 cents per litre. The following diagram shows the taxes and levies on a litre of petrol (including GST).



Grant Cleland & Emma Doherty
 Research Services Analysts – Economics
 Economics, Society and Infrastructure Team.
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