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Te Pātaka Rangahau a Te Whare Pāremata

# MONTHLY ECONOMIC REVIEW






**May 2014**

(Latest data as at 9 May)

Parliamentary Library Research Paper

## A Overview

### Recent trend

	12/13	13/14	
 Economic Growth	2.6%	2.7%	Annual average GDP Growth (December year)
 Unemployment	6.2%	6.0%	Unemployment Rate (March quarter)
 Inflation	0.9%	1.5%	Annual Inflation Rate (March year)
 Current Account Deficit	\$8.6b	\$7.5b	Current Account Deficit (December year)
 Interest Rates	2.65%	3.24%	90 Day Bank Bills (April month)

### Latest data and events

New Zealand's unemployment rate remained at six percent in the March 2014 quarter, with a 0.9 percent rise in both employment and the labour force over the quarter. The labour force participation rate, at 69.3 percent, rose to its highest level since the survey commenced in the 1980s. There was an increase in both full-time and part-time employment, with full-time employment rising by 1.1 percent over the quarter and part-time employment rising by 0.3 percent. New Zealand's unemployment rate was the 11<sup>th</sup> lowest in the OECD.

Inflation was 0.3 percent in the March 2014 quarter, resulting in an annual inflation rate of 1.5 percent in the year to the March quarter. In the March quarter, an 11.3 percent rise in the excise duty on tobacco and tobacco products from 1 January 2014 was a significant driver to higher consumer prices. Costs associated with the purchase of newly built houses rose by 1.2 percent.

Reserve Bank Governor, Graeme Wheeler, lifted the official cash rate by a further 25 basis points to three percent in April. This followed the commencement of a tightening in monetary policy in March, where the official cash rate was also lifted by 25 basis points. In the latest media release, the Governor commented that economic activity has gained considerable momentum, reducing spare capacity within the economy, and leading to inflationary pressures. This has been offset by a higher exchange rate, which has resulted in lower tradables inflation.

The exchange rate on a trade weighted basis has reached a new peak since it was floated. During the month of April, the trade weighted index (TWI) averaged 80.2 index points. The Reserve Bank considers the exchange rate to be overvalued. The Governor commented that the Bank has the policy option of intervening in the currency if it thought the exchange rate was significantly out of line with economic fundamentals.

### Outlook

Solid economic growth is expected, with respondents to the *NZIER Consensus Forecasts* survey expecting a growth rate of 0.8 percent for the March quarter, and growth of 0.9 percent in the following two quarters. Business surveys indicate that firms are planning to increase employment over the upcoming period. Bank economists are forecasting a further 25 basis point rise in the official cash rate in June, bringing the rate to 3.25 percent. Some bank economists are raising the possibility that low consumer price and wage inflation, along with the high New Zealand dollar may lead the Reserve Bank to forego an increase in the OCR in July.

**Topic of the month:** Fixed and floating mortgage lending

# 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.

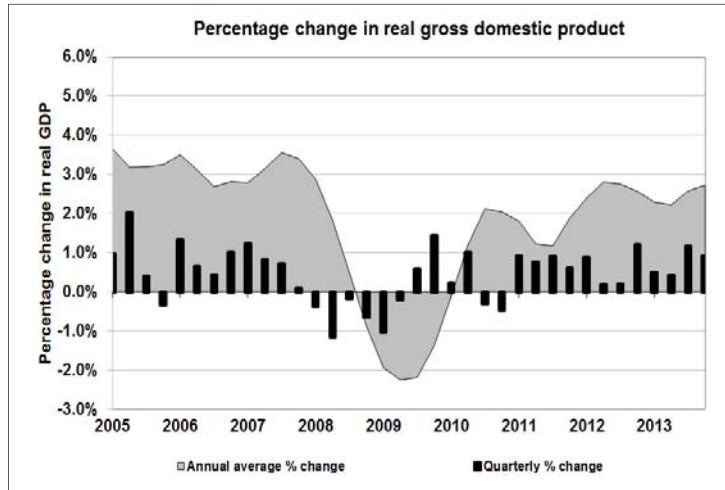
## Gross domestic product

Economic activity expanded by 0.9 percent in the December 2013 quarter, while gross domestic product rose by 2.7 percent over the 2013 calendar year.

An increase in goods and services exports, along with a rise in household spending were significant drivers of economic growth over the December quarter. Households spent more on durable goods and services, while an increase in dairy product exports were a significant factor behind the rise in exports.

Increased activity in the mining, wholesale trade, and manufacturing industries were significant drivers of the increase in production GDP over the quarter.

Over the 2013 calendar year, investment in residential buildings rose by 17.4 percent, while investment in other fixed assets also rose, up 6.9 percent.



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## Other data

Businesses' trading activity, as measured by the NZIER's *Quarterly Survey of Business Opinion*, has risen to its highest level since 2003, indicating further GDP growth. Business confidence remains high, with confidence levels in the *ANZ Business Outlook* survey remaining at elevated levels (although down slightly from March). Indicators of both the manufacturing and service sectors are consistent with additional increases in activity. Consumer confidence also remains strong, indicating further growth is likely in household spending. However, higher mortgage rates could lead to a drop in consumer confidence over coming months.

Year ended December 2013	Nominal GDP
Expenditure GDP	\$221,417 million
GDP per capita	\$49,655

Source: Statistics New Zealand.

ANZ Business Outlook Survey	Mar-14	Apr-14
Net % expecting an improvement in business conditions in 12 months' time	67.3	64.8
Net % expecting an improvement in their own firm's activity in 12 months' time	58.2	52.5

Source: ANZ Bank, Business Outlook survey.

## Outlook

A solid economic growth rate is expected in the March quarter, with *NZIER Consensus Forecasts* expecting a growth rate of 0.8 percent for the quarter, with annual average growth of 2.9 percent for the year to March. Net migration inflows of just under 32,000 people over the last year will support household consumption expenditure growth. Construction activity and residential investment also continue to be a driver of economic growth over upcoming years.

GDP growth (%)	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13
Annual (year-on-year)	2.6	2.3	2.2	2.6	2.7
Quarterly (seasonally adjusted)	1.2	0.5	0.4	1.2	0.9

Source: Statistics New Zealand.

**Next Release:** *Gross Domestic Product: March 2014 quarter.* **Date:** 19 June 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

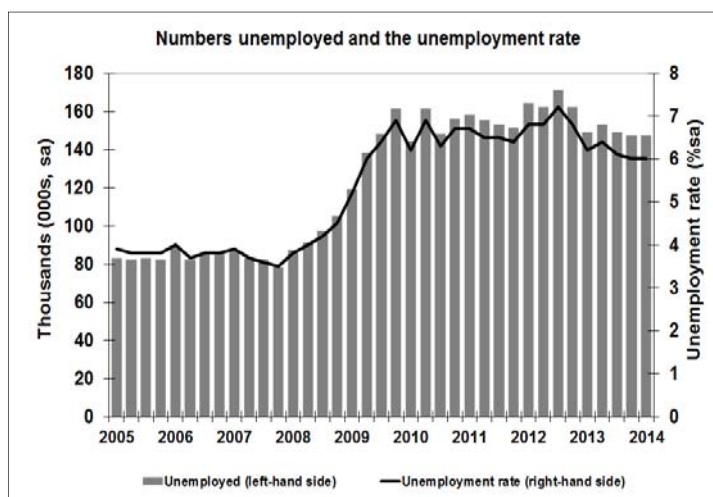
A rise in the labour force participation rate to its highest level since the current survey commenced in the 1980s meant that despite a rise in employment of 0.9 percent over the March quarter, the unemployment rate remained steady at six percent.

The labour force participation rate, which measures the proportion of those aged 15 years and over who are in work or actively seeking work, rose to 69.3 percent in the March quarter, up 0.4 percentage points from the previous quarter.

During the March quarter, full-time employment rose by 1.1 percent, while part-time employment rose by 0.3 percent. There was a 2.7 percent rise in the total number of hours worked in the quarter (when compared with the previous quarter in seasonally adjusted terms).

There were 147,000 people unemployed in seasonally adjusted terms in the March quarter, the same number as the previous quarter. Following the recession, unemployment numbers peaked at 171,000 people in the September 2012 quarter with the unemployment rate peaking at 7.2 percent in the same quarter.

Between the March 2013 and 2014 quarters employment grew by 3.7 percent, with another 84,100 people employed. There were an additional 24,400 people employed in the construction sector, while employment in the information media and telecommunications industry fell by 7,000.



## Other data

Between the March 2013 and 2014 quarters, salary and wage rates (including overtime) rose by 1.6 percent, with rates rising by 1.7 percent in the private sector and by 1.2 percent in the public sector.

Average ordinary time weekly earnings (which excludes overtime) rose by 3.2 percent between the March 2013 and 2014 quarters.

## Outlook

*NZIER Consensus Forecasts* has the labour market strengthening over its forecast period. An unemployment rate of 5.4 percent is forecast in 2014/15. The ASB Bank believes that the unemployment rate will not fall below five percent until 2016.

ANZ Business Outlook Survey	Mar-14	Apr-14
Net % expecting to increase employment in their business in 12 months*	26.6	29.8
Net % expecting the unemployment rate to rise in 12 months*	-49.0	-48.0

\*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

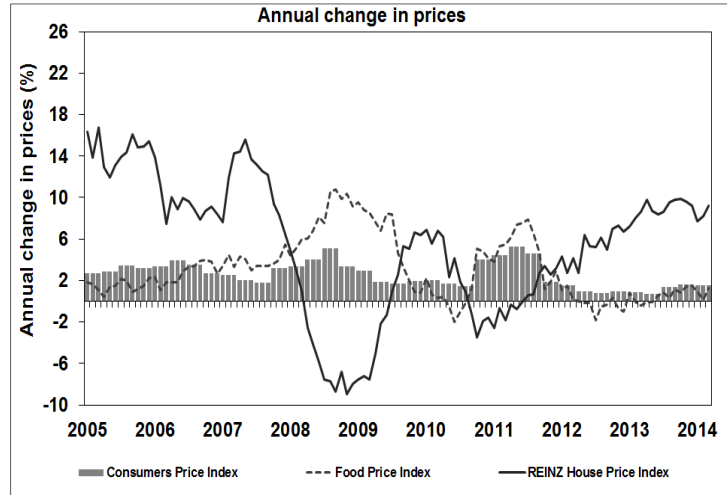
Inflation is the change in prices of goods and services over a certain period of time. The official rate of consumer inflation is measured by Statistics New Zealand's Consumers Price Index (CPI). The CPI tracks the price of a basket of household goods and services over time.

## Consumers Price Index

Consumer prices rose by 0.3 percent in the March 2014 quarter, lower than market expectations of a 0.5 percent rise in prices over the quarter.

An 11.3 percent rise in the excise duty on tobacco and tobacco products from 1 January led to an increase in the price of cigarettes and tobacco products in the March quarter.

Costs associated with newly built houses (excluding land) rose by 1.2 percent over the March quarter, with costs rising by 1.7 percent in Auckland and by 1.5 percent in Canterbury. Housing rental costs rose by 0.6 percent in the March quarter, with rental costs in the Canterbury region rising by 1.9 percent.



International airfares (which are highly seasonal) fell by 10.1 percent in the March quarter, while vegetable costs fell by 5.8 percent, and package holiday costs fell by 5.9 percent.

Annual inflation was 1.5 percent in the year ended in the March 2014 quarter, down from an annual inflation rate of 1.6 percent in the year ended in the December 2013 quarter. Half of the annual increase in consumer prices came from the housing and household utilities group, where prices rose by 3.3 percent over the year. Costs associated with newly built houses rose by 5.1 percent over the year, and housing rentals rose by two percent.

## Other data

There were 7,315 unconditional residential property sales in March, down 10 percent from a year earlier. The number of properties sold in the under \$400,000 range fell by 21.9 percent from March 2013, possibly reflecting the impact of the Reserve Bank's LVR restrictions on bank lending (and house price inflation pushing prices up into the next price bracket). The national median sale price was \$440,000 in March 2014.

Annual Percentage Change (%)	Mar-14	Apr-14
QV – Residential property values*	8.8	8.4
REINZ Median Housing Price Index**	9.2	n/a
Food Price Index**	1.2	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

## Outlook

The annual inflation rate is forecast to rise on the back of higher non-tradables inflation. *NZIER Consensus Forecasts* has the annual inflation rate rising to 2.1 percent in the year ended March 2015, and 2.4 percent in the following year.

ANZ Business Outlook Survey	Mar-14	Apr-14
Net % of respondents expecting to increase prices in 3 months' time*	30.2	30.2
Inflation expected in 12 months' time	2.61	2.59

\*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

In the 2013 calendar year, New Zealand's current account deficit totalled \$7,547 million, equivalent to 3.4 percent of GDP. Within the current account, both the goods and services balances recorded a surplus over the year, offset by deficits in the incomes and current transfers' balances.

Foreign investors earned \$15,627 million on their New Zealand debt and equity investments during 2013. Of which, \$7,401 million was in interest payments, \$4,535 million in dividends, and the remaining \$3,691 million was retained earnings.

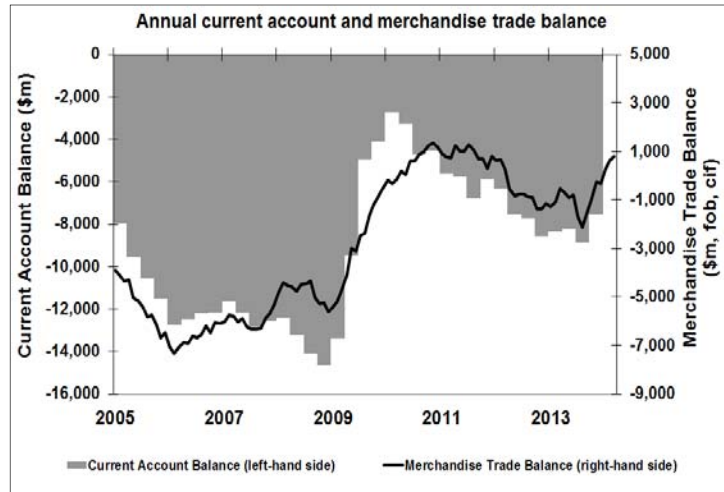
## Other data

New Zealand's terms of trade (the volume of imports that can be purchased with a fixed volume of exports) were at their highest level in 40 years in the December 2013 quarter. Import prices fell to a greater extent than export prices over the quarter, increasing the terms of trade.

While international commodity prices for New Zealand's exports remain near historically high level, prices have eased recently. The ANZ *Commodity Price Index* fell by four percent in April, with international commodity prices 2.8 percent lower than a year ago. International dairy prices have fallen in each of the last six global dairy trade auctions undertaken by Fonterra, with prices in early-May almost 22 percent lower than those recorded three months earlier in February.

## Outlook

The current account deficit as a percentage of GDP has been forecast to fall in the near term, with increased export earnings expected to be a factor following the impact of last year's drought on the deficit. The Reserve Bank has forecast the deficit to equate to 3.2 percent of GDP in the year ended March 2014, while *NZIER Consensus Forecasts* expects a current account deficit of \$7,500 million in the year ended March.



Annual Change (%)	Mar-14	Apr-14
World Commodities Prices*	14.0	-2.8
NZ\$ Commodities Prices*	11.8	-3.6
Overseas Visitors**	5.4	n/a

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

Balances (\$m)	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Quarterly Current Account (seasonally adjusted)	-2,142	-1,770	-2,212	-2,577	-837	n/a
Annual Current Account	-8,590	-8,349	-8,244	-8,871	-7,547	n/a
Goods	150	567	267	-294	1,332	n/a
Services	1,234	1,060	1,101	1,097	1,082	n/a
Income	-9,454	-9,484	-9,026	-9,084	-9,440	n/a
Current transfers	-520	-492	-586	-589	-521	n/a
Net international investment position (as at date)	-152,809	-151,284	-151,366	-149,522	-147,564	n/a
Annual Merchandise Trade Balance (fob-cif)*	-1,155	-521	-819	-1,559	-317	805

\* 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: March 2014 quarter.* **Date:** 18 June 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

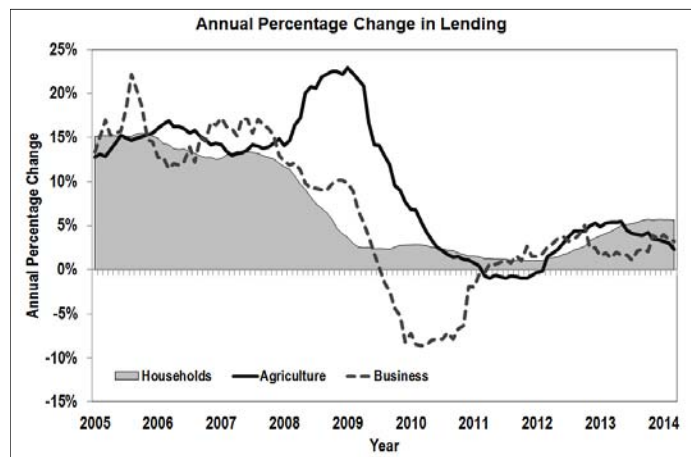
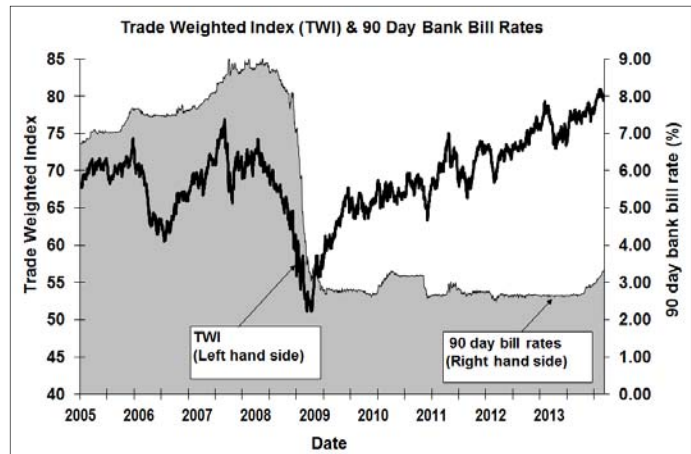
Reserve Bank Governor, Graeme Wheeler, lifted the official cash rate in April for the second time this year, increasing the OCR by a further 25 basis points to three percent. The Governor noted that spare capacity within the economy was being absorbed, adding to inflationary pressures, which are expected to rise over the next two years. He said that further increases in the OCR are dependent upon economic data and the Bank's assessment of emerging inflationary pressures.

The trade weighted index reached a new post-float high, averaging 80.2 index points during April, up 2.8 percent from a year earlier (and by 13 percent against the Australian dollar). In his statement announcing the increase in the OCR, the Governor noted that the Bank believed that the current level of the exchange rate was not sustainable.

Latest high loan-to-value (LVR) residential mortgage lending equated to 3.6 percent of new lending in March (after exemptions), with the Reserve Bank commenting that such lending had fallen to 5.6 percent over the last six month period. This compared with approximately 25 percent of new lending undertaken in September last year.

## Outlook

A further tightening of monetary policy is expected. In its March *Monetary Policy Statement*, the Reserve Bank projected that the 90-day bank bill rate would rise by around 130 basis points during 2014, to average four percent in the December 2014 quarter. The ANZ and Westpac banks expects a further 50 basis point rise in the OCR this year (although the high exchange rate may delay one of the interest rate hikes). The next rise is expected in June.



Core Crown borrowing as at	31-Mar-14 (\$m)	31-Mar-14 (%GDP)
Gross sovereign-issued debt *	84,034	38.0
Net core Crown debt **	61,178	27.6

\* Excluding Reserve Bank settlement cash and Reserve Bank bills.  
\*\* Excluding NZ Super Fund and other advances. Source: The Treasury.

Monthly averages	Dec-13	Jan-14	Feb-14	Mar-14	Apr-14
90 Day Bank Bill rate	2.73	2.88	2.93	3.05	3.24
10 Year Government Bond yields (secondary market)	4.76	4.64	4.57	4.58	4.55
Effective mortgage rate	5.51	5.51	5.52	5.55	n/a
Business lending rate	5.37	5.37	5.41	5.50	n/a
Trade Weighted Index (TWI) exchange rate	77.50	78.40	77.96	79.68	80.20
NZX 50 index	4729	4881	4896	5110	5110

Sources: Reserve Bank; NZX.

**Next Official Cash Rate (OCR) decision: 12 June 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

Economic growth in China slowed in the March 2014 quarter, with its economy expanding by 1.4 percent (the lowest quarterly growth rate in two years). On an annual basis, the economy expanded by 7.4 percent, below the Chinese Government's targeted annual growth rate of 7.5 percent.

Economic activity in the OECD area expanded by 0.5 percent in the December 2013 quarter, with 28 countries recording an increase in gross domestic product output. Adverse winter weather conditions in the United States were a significant factor behind the nil growth rate in GDP output in the March 2014 quarter.

## Unemployment

The harmonised unemployment rate within the OECD rose slightly in February to 7.6 percent, up 0.1 percentage point from the previous month. The unemployment rate in the United States rose to 6.7 percent in February (where it remained in March). Norway and Japan have the lowest unemployment rate in the OECD, at 3.6 percent, while the unemployment rate for South Korea rose from 3.2 percent in January to 3.9 percent in February (a three year high). The highest unemployment rate was recorded in Greece at 27.5 percent (December 2013).

## Central banks

The United States Federal Reserve announced in late April that it was reducing the size of its quantitative easing programme in May by a further US\$10 billion per month to US\$45 billion. This compares with US\$85 billion per month at the height of the asset purchasing programme. The Federal Open Market Committee noted that it believed that there was "...sufficient underlying strength in the broader economy to support ongoing improvement in labor market conditions".

The Board of the Reserve Bank of Australia decided to leave the bank's cash rate steady at 2.5 percent in early May. In announcing the decision, Reserve Bank Governor Glenn Stevens commented that while economic growth in Australia was below trend in 2013, that recent indicators are suggesting modest growth in consumer demand. Exports are increasing, and an expansion in housing construction is also expected.

Quarterly economic growth rates (%)			
Country*	Sep-13	Dec-13	Mar-14
Australia	0.6	0.8	n/a
Japan	0.2	0.2	n/a
NEW ZEALAND	1.2	0.9	n/a
United Kingdom	0.8	0.7	0.8
United States	1.0	0.7	0.0
Euro area	0.1	0.3	n/a
OECD Total	0.7	0.5	n/a
China	2.3	1.7	1.4

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

Harmonised unemployment rates (%)			
Country	Feb-14	Mar-14	Apr-14
Australia	6.0	5.8	5.8
Japan	3.6	n/a	n/a
NEW ZEALAND	n/a	6.0 (qtr)	n/a
United Kingdom	7.1 (Dec)	n/a	n/a
United States	6.7	6.7	n/a
OECD Total	7.6	n/a	n/a

Sources: OECD; Australian Bureau of Statistics.

Central Bank interest rates (as at 9 May 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	0.25	13-Nov-13	-25
Japan	Uncollateralized overnight rate	0.00 - 0.10	5-Oct-10	-10
NEW ZEALAND	Official Cash Rate	3.00	24-Apr-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

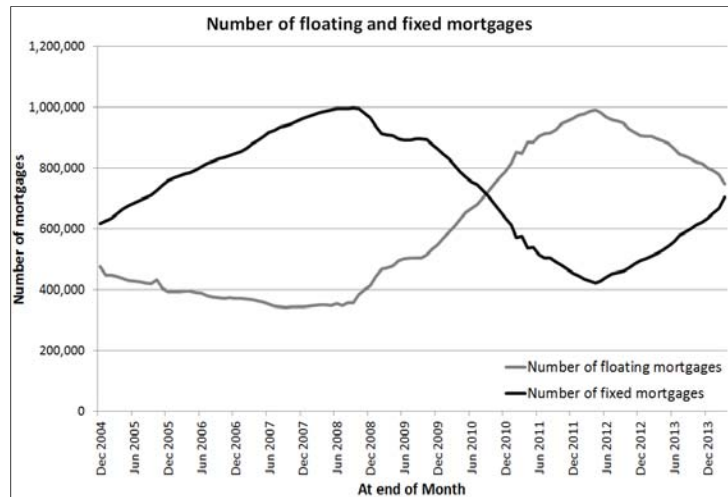
Source: Central Bank interest rates as at the date stated.

## Fixed and floating mortgage lending

With New Zealand's lenders increasing floating mortgage rates as a result of the Reserve Bank tightening monetary policy over recent months, there has been a move from floating to fixed term mortgages. It has almost reached the point where there are more fixed rate mortgage loans than floating rate mortgage loans. This hasn't been the case since August 2010, as households took advantage of lower floating mortgage rates which are more heavily influenced by the rate of the official cash rate. When looking at the value of mortgages outstanding, the value of fixed rate mortgages surpassed that of floating rate mortgages from May 2013.

In March 2014, there were 748,091 floating rate mortgages and 703,967 fixed rate mortgages. The value of floating rate mortgages was \$70 billion as at March 2014, while the value of fixed rate mortgages was \$122.2 billion. The total value of mortgages outstanding at the end of March 2014 was \$192.6 billion.

According to Statistics New Zealand's 2013 *Household Economic Survey* approximately a third of all households occupied by the usual residents made a mortgage repayment during the year to June 2013 (note that this excluded rental properties, where the landlord may have a mortgage over the property). Of these households, the average weekly mortgage repayment was \$356 per week, a slight reduction from the previous year due to lower interest rates.



As at March 2014	Number of mortgages	Value of mortgages (\$m)	Monthly weighted average mortgage rate (end of month) (%)
Floating	748,091	70,030	5.67
Fixed	703,967		
< 1 year		64,806	5.23
1 < 2 years		35,604	5.57
2 < 3 years		15,174	6.01
3 < 4 years		3,818	6.11
4 < 5 years		2,812	6.32
5+ years		39	7.11
Total fixed		122,253	5.48
Unallocated		309	6.20
<b>Total</b>	<b>1,452,058</b>	<b>192,592</b>	<b>5.55</b>

**Source:** Reserve Bank of New Zealand, *S8 Banks: mortgage lending (SSR Part E)*

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