# Monthly Economic Indicators

THE TREASURY
Kaitohutohu Kaupapa Rawa

September 2016

## Executive Summary

- **Solid GDP growth in the June quarter was driven by construction, with support from the services sector**
- **The current account deficit narrowed and nominal GDP growth was strong, despite a decline in the terms of trade**
- **Although most central banks held policy rates unchanged in September, the landscape of global monetary policy has changed with lowered prospects for future easing, despite continuing economic weakness**

Key economic data releases in September point to stronger GDP growth over 2016 than expected in the *Budget Economic and Fiscal Update*. Real GDP growth for the June quarter was largely in line with market expectations but stronger than in the *Budget Update*. However, the drivers of growth were as anticipated, with construction making a particularly strong contribution, supported by services, and high population growth, chiefly from high net migration, underpinning aggregate demand more broadly. Overseas tourism was less prominent in the June quarter but remains a key driver of annual growth. Nominal GDP was also a little higher than forecast for the 2016 fiscal year, in line with the positive tax forecast variance in the 11 months to May.

Indicators for activity since June have generally been positive. Construction, both residential and non-residential, is expected to underpin growth through the remainder of 2016, although consents data indicate that the pace of growth may ease a little from recent quarters. Consumption indicators for the September quarter have been more mixed, with electronic card spending falling but consumer confidence lifting. Low interest rates, high net migration and solid labour income growth should sustain aggregate private consumption growth at a reasonable rate through the second half of 2016. House price growth remains high. This month's special topic provides a more detailed look at recent household debt developments.

The annual current account deficit narrowed in the year to June 2016. The goods deficit narrowed slightly, as a lift in net export volumes offset the fall in the terms of trade in the quarter. The primary income deficit also narrowed, chiefly on smaller investment income outflows. The services surplus remains around its long-term average, thanks to rapid growth in international tourism in previous quarters, providing a sizeable offset to the other components of the current account.

The Reserve Bank left the Official Cash Rate (OCR) unchanged at 2.0% in September and maintains an easing bias. One further cut is fully priced in for November. The NZD remains close to a 17-month high.

Although most central banks held policy rates unchanged in September, the landscape of global monetary policy has changed with slightly more flexible policy targets in Australia and Japan, and lowered prospects for future easing by the ECB, BoJ and BoE, despite continuing economic weakness. The US Federal Reserve remained on hold. Concerns about less monetary easing in the future and heightened risk aversion led global financial market volatility to rise in September.

Global data were mixed for September. US indicators of September quarter activity have been mixed, disappointing analysts, while Japan's outturns were also soft. Australia's June quarter GDP growth eased but China's growth recovered in August. There was mixed activity in the euro area, although UK growth appears unimpeded by Brexit so far.

New Zealand Government

# Analysis

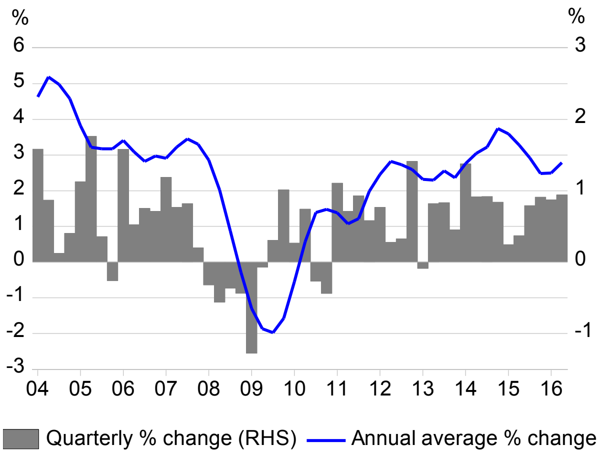
Domestic data released over September continue to show robust economic activity. GDP and Balance of Payments data for the June quarter were stronger than expected in the *Budget Economic and Fiscal Update* (BEFU), with construction and services the main drivers of growth. High population growth from record net migration has supported aggregate demand.

Indicators of more recent activity were generally positive and point to reasonable growth prospects for the remainder of 2016. Consents data suggest construction activity will continue to increase, particularly later in the year. Consumer confidence lifted, as did key export commodity prices. Interest rates remain low, with the Reserve Bank holding the Official Cash Rate (OCR) at 2.0%. However, the high New Zealand dollar may be creating some headwinds for tourism and putting downwards pressure on inflation, and house price growth remains high.

**Solid GDP growth in the June quarter…**

The major data releases in September were the June quarter GDP and Balance of Payments figures. Real production GDP rose 0.9% in the June quarter (Figure 1), largely in line with market expectations but stronger than in the BEFU (0.6%). Annual average growth lifted to 2.8% (BEFU 2.6%), partly owing to revisions to previous quarters (including the March quarter, revised from 0.7% to 0.9%). Construction and services remain key growth drivers, with overseas tourism less prominent in the June quarter.

**Figure 1: Real production GDP**



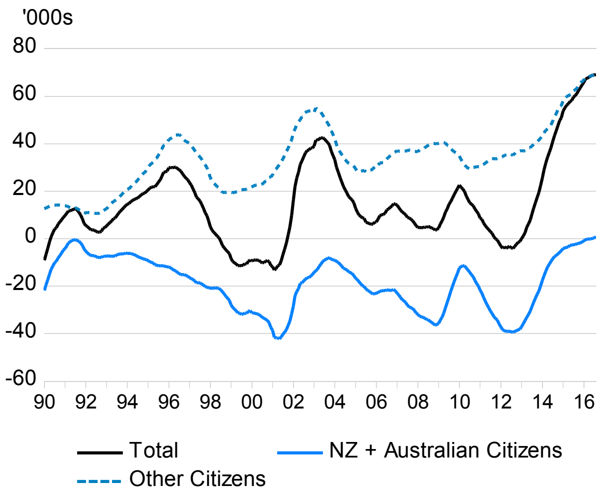

Source: Statistics NZ

Real expenditure GDP growth was stronger than production GDP growth at 1.2% in the quarter, lifting annual average growth to 3.3% (BEFU 3.5%). Nominal GDP growth was strong at 2.1% in the quarter, despite a 1.9% fall in the SNA terms of trade. Annual average growth in nominal GDP lifted to 4.2%, exceeding the $250 billion mark for the first time. Nominal GDP was around $1.7 billion higher than forecast for the year to June, in line with the $0.4 billion positive tax variance in the 11 months to May.[1]

Real gross national disposable income, which adjusts GDP for terms of trade movements (ie, a measure of the average real purchasing power of New Zealand's disposable income), increased by 2.6% in the June year. Aggregate GDP growth figures continue to be bolstered by rapid population growth (2.0% higher than a year ago), which in turn has been supported by high net migration. Real GDP per capita growth was 0.7% in the year to June.

Annual permanent and long-term (PLT) net migration lifted marginally from its previous peak in June to 69,100 in August (Figure 2). Seasonally adjusted monthly net inflows have been stable at around 5,600 in recent months. There are some signs that net migration is peaking. After rapid growth, annual net inflows of non-New Zealand and non-Australian citizens have started to flatten off. This has largely been driven by slowing growth in student visas, which fell in the year to August, the first annual decline since overseas student work rights were relaxed in 2013. Similarly, the decline in net New Zealand and Australian citizen outflows has tapered off in recent months.

**Figure 2: Annual PLT net migration by citizenship**



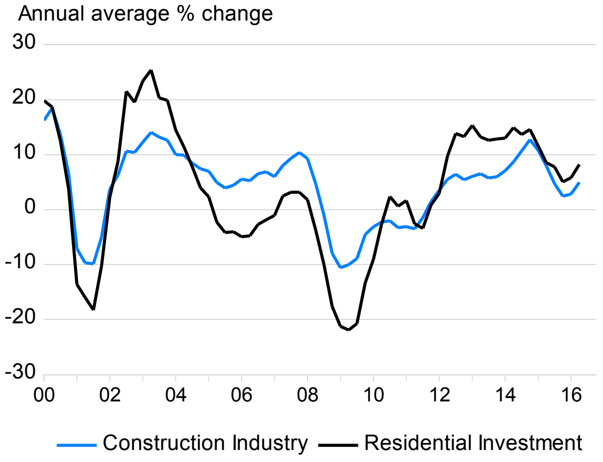

Source: Statistics NZ

[1] Financial Statements of the Government of New Zealand for the Year Ended 30 June 2016 will be published on 13 October.

**…driven by construction…**

Construction was a major driver of growth in the quarter, underpinning both measures of GDP growth. The construction industry accounted for one third of the increase in the production measure of GDP, growing 5.0% in the quarter to be up 6.3% in the year to June (Figure 3). Industries related to construction and the housing market more broadly also made significant contributions. Rental, hiring and real estate services contributed 0.2 percentage points to growth, while manufacturing (including the manufacture of glass, cement and concrete) and retail trade (where growth was driven by non-durable goods such as hardware and furnishings) contributed 0.1 percentage point each.

**Figure 3: Construction and residential investment**




Source: Statistics NZ

Much of the investment growth in the expenditure measure of GDP was construction-related. Residential building investment lifted by 6.0% in the quarter, non-residential building investment by 4.5% and other construction, which includes infrastructure investment, by 4.9%. Overall investment growth accounted for a little over half of the growth in expenditure GDP for the quarter.

Construction is expected to underpin growth through the remainder of 2016. A slight slowdown in the volume of consents issued earlier in the year, together with the greater share of apartments (which typically take longer than houses to move from consent to construction), suggests that the pace of growth may ease a little from recent quarters. Nonetheless, construction is expected to remain solid through the second half of 2016 and into 2017.

**…and supported by services**

Services industries expanded by 0.7% in the quarter, to be 2.8% higher in the year to June. Much of the growth in the quarter was driven by industries supporting the construction sector. Non-residents' expenditure in New Zealand (chiefly tourism-related activity) fell 1.7% in the quarter but together with population growth remains the main driver of annual growth in services. Slowing growth in international tourism (partly due to the headwinds of a high NZD) suggest that services sector growth in coming quarters may be driven more by domestic factors.

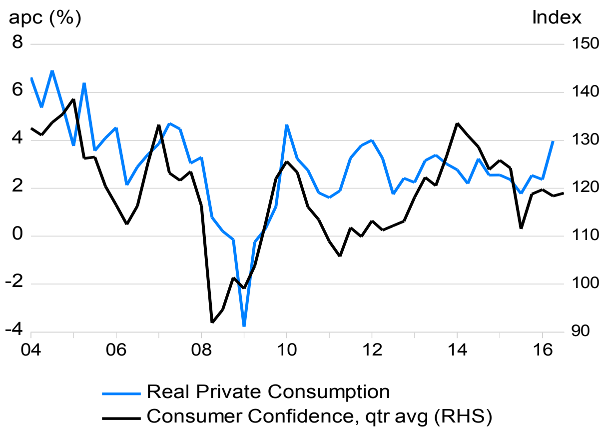
Growth in the primary sector was positive for the first time since June 2015, as increased dairy production more than offset a reduction in mining activity. The rise in primary production also benefitted food processing industries.

**Private consumption growth lifts…**

Household consumption expenditure spiked 1.9% in the June quarter, following relatively subdued growth of 0.4% in the March quarter. Consumption of services and durable goods both rose strongly in the quarter, with the latter reflecting housing activity as well as improved purchasing power from the higher NZD. Real household consumption increased by 2.6% in the year to June, underpinned by population growth, with per capita consumption growth remaining fairly weak. Nominal household consumption increased by 2.3% in the quarter, stronger than our expectations and contributing much of the positive variance from our GST forecasts.

Consumption indicators for the September quarter have been more mixed. Seasonally adjusted total electronic card spending fell 0.8% in August, with retail spending down 0.4%, following gains of just 0.3% and 0.2% respectively in July. However, consumer confidence has improved more recently, with the ANZ-Roy Morgan survey lifting in September after falling in July and August (Figure 4) and the Westpac McDermott Miller consumer confidence index increasing slightly for the September quarter.

**Figure 4: Consumption and consumer confidence**




Source: ANZ-Roy Morgan, Statistics NZ

Overall, we expect consumption growth to slow in the September quarter, partly reflecting a pull back from high growth in the June quarter, before picking up again in the December quarter. Low interest rates, high net migration and solid labour income growth should sustain aggregate private consumption growth at a reasonable rate. This month's special topic provides a more detailed look at recent household debt developments.

**…while net exports continue to drag on growth**

Exports of goods increased by 7.6% in the quarter, with large increases in both dairy and meat exports. However much of this growth, particularly of dairy exports, was met from a reduction in inventories, suggesting the pace of exports is unlikely to be sustained into the September quarter. This has been borne out so far in the overseas merchandise trade data, with seasonally adjusted dairy export volumes falling 12.9% in August, after increasing just 0.6% in July. Exports of services fell 1.6% in the quarter, mostly due to the fall in tourism-related activity. Overall, exports contributed 1.1 percentage points to growth but this was offset by the fall in inventories (also 1.1 percentage points).

Imports also rose strongly in the quarter, up 2.6%, largely reflecting strong domestic demand. Growth was driven by consumption goods (up 4.3%) and capital goods (up 6.1%), in line with the broader drivers of economic growth in the quarter. Services imports were also strong, with many New Zealanders making the most of the high NZD to increase their household expenditure overseas. All told, imports detracted 0.7 percentage points from GDP growth.

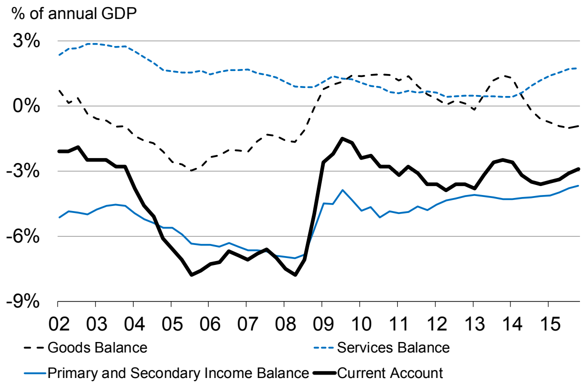
Net exports are expected to remain a drag on growth in coming quarters. Import growth is likely to remain solid in light of strong domestic demand and the Air New Zealand fleet upgrade. Meanwhile, export volumes are likely to pull back a little. Dairy, beef and sheep meat production are all expected to ease in the coming agricultural season and the high NZD may present headwinds for exporters of manufactured products and services (including tourism). A good season for horticulture and wine may provide some offset.

**The current account deficit narrowed in June…**

Despite the terms of trade falling, the annual current account deficit narrowed to 2.9% of GDP in June from 3.1% in March (Figure 5). The deficit was at the high end of market expectations (median 2.7%) but significantly lower than expected in BEFU (3.5%). Last month's special topic provides some insight into why the current account deficit has been relatively low in recent years.[2]

The annual goods deficit narrowed slightly to 0.9% of GDP (from 1.0% in March). Thanks to the inventory-related surge in export volumes, nominal goods exports rose 4.4% in the quarter, while nominal goods imports rose 3.7%, also on higher volumes.

**Figure 5: Annual current account deficit**




Source: Statistics NZ

The annual services surplus remained stable at 1.7% of GDP. Nominal services exports fell 1.8% in the quarter but remain at a high level thanks to strong growth in preceding quarters. Nominal services imports increased 1.0% in the quarter, with a 1.9% increase in travel services imports reflecting an increase in spending by New Zealanders on holidays overseas.

The annual primary income deficit (investment income flows) narrowed from an upwardly revised 3.6% of GDP in March to 3.4% of GDP in June. The smaller annual deficit is chiefly the result of a reduction in investment income from foreign investment in New Zealand (smaller investment income outflows).

New Zealand's net international liability position increased from 63.9% in the March quarter to 64.9% in June. New Zealand's liabilities increased in the quarter more than its assets held offshore, as the NZX performed relatively well compared to overseas indices (increasing New Zealand's external liabilities via market price changes) and global market volatility stemming from the Brexit vote led to a devaluation of New Zealand-held assets overseas. That said, market price changes are calculated on a quarter-end basis which, in June, closely followed the Brexit vote.

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2 http://www.treasury.govt.nz/economy/mei/aug16/03.htm

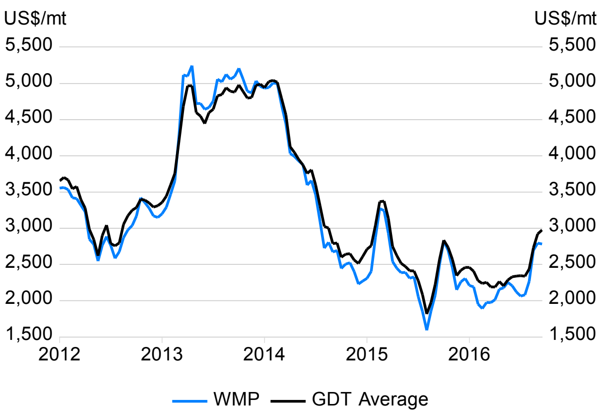
### …and commodity export prices continue to pick up

The annual overseas merchandise trade deficit widened slightly in August to $3.1 billion, although it remains slightly lower than the $3.3 billion deficit recorded in the year to June. On a seasonally adjusted basis exports fell 8.6% from July, with a particularly large fall in dairy values (-11.7%) due to lower volumes (-12.9%). Seasonally adjusted imports fell 3.0% (-2.3% excluding petrol).

Prices for New Zealand's key commodity exports continue to pick up. The ANZ world commodity price index increased 3.2% in August, its fourth consecutive monthly gain, with the index 10.2% higher than its April low. Increases have been fairly broad-based, with all the commodities measured lifting since April. Gains have been less pronounced in the New Zealand dollar index, which increased 1.9% in August and 4.3% since April, because of the 6% appreciation in the NZD TWI since April.

Dairy prices continued to gain ground on the GDT auction platform. The GDT index increased 10% in September, following a 20% increase in August (Figure 6). Increases in September have been mostly concentrated in the fat-based products, with key product whole milk powder (WMP) lifting only 3.2% to around US$2,780/mt. The lift in prices to date has been a little faster than our expectations in BEFU. There may be a small retracement in one or two upcoming auctions, following the large gains recently, but the broad direction of prices is expected to remain upwards as global supply continues to adjust.

**Figure 6: Dairy prices**




Source: Global Dairy Trade

In response to improving prices and the ongoing global milk supply adjustment, Fonterra lifted its forecast farmgate milk price from $4.75/kg milk solid (MS) to $5.25/kg MS. The new milk price forecast is above the average breakeven of around $5.00/kg MS; however, most farmers will still face negative cash flows during the current season given the low retrospective payment from the 2015/16 season.

Seasonally adjusted short term overseas visitor arrivals in August fell compared to a month ago (-1.9%) but remain close to their recent high levels. Growth in annual arrivals remains strong at 11.3%, with annual arrivals of 3.36 million. New Zealand resident departures rose compared to a month ago (1.6%), with growth in annual departures of 6.1%.

The current account deficit is expected to widen in the September quarter, due to an increase in the goods deficit as dairy volumes moderate further (before higher prices begin to show up in the December quarter). The services balance is expected to hold up around current levels, with travel services exports supported by a sustained high number of Chinese visitors as well as high levels of education exports. That said, the current account deficit is not expected to widen over the remainder of 2016 to the extent forecast in BEFU.

### House price growth remains elevated

House prices eased slightly in August but annual price growth remains high. The REINZ stratified median house price index fell 2.2% in August, with falls in Auckland, Christchurch and Wellington as well as the rest of the North Island. The monthly decline may have reflected the response by retail banks to upcoming tightening of LVR restrictions in October, although LVR data for August suggest the retail banks in aggregate are well below the "speed limits". On an annual basis, the index was 11.7% higher than a year ago. Price pressures continue to spill over from Auckland, where annual growth eased to 8.2%.

Food prices, which make up about one fifth of the Consumers Price Index (CPI) basket, rose 1.3% in August, following a small decline in July (-0.2%). However this increase is expected to be outweighed by the ACC levy decrease and declines in petrol prices in the September quarter. As a result, CPI inflation is likely to remain low in the quarter and possibly be negative. In the absence of further shocks, the high NZD is likely to continue exerting downward pressure on tradables inflation.

### RBNZ left the OCR unchanged at 2.0%

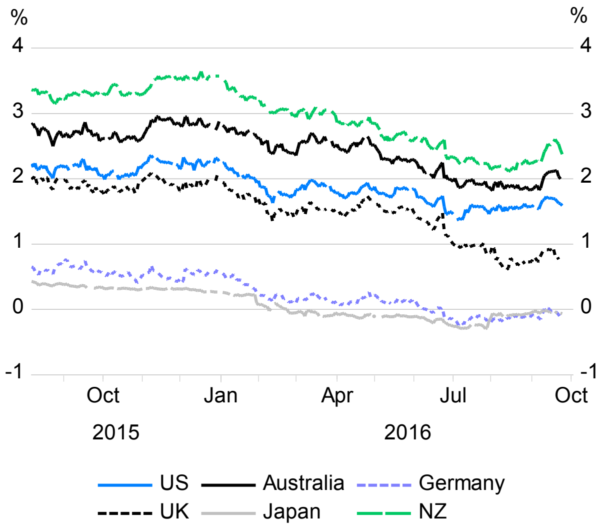
The Reserve Bank left the OCR unchanged at 2.0% in September, in line with market expectations that the next cut will be delivered in November. A further cut is around 20% priced in for February.

**Less easy global monetary policy expected**

Although most central banks held policy rates unchanged in September, the landscape of global monetary policy has changed with slightly more flexible policy targets in Australia and Japan, and lowered prospects for future easing by the ECB, BoJ and BoE, despite continuing economic weakness. Expectations of future hikes by the Fed have fallen on weaker outturns and a new Fed 'dot plot' showing a more gradual profile with two fewer 25 basis point hikes expected in 2017. With limits to monetary easing and what it can achieve, the OECD has called for increased fiscal stimulus and structural reforms to complement monetary policy, which it sees as insufficient for breaking out of the current "low-growth trap".

Concerns about less monetary easing in the future, and heightened risk aversion led global financial market volatility to rise in September, with the VIX spiking to 20.5 mid-month, and averaging around 14 compared to 12 in August. Global 10-year government bond yields rose, but most have since retraced (Figure 7).

**Figure 7: Ten-year government bond yields**




Source: Haver

**US data mixed, and Fed remains on hold…**

US indicators of September quarter activity have been mixed, disappointing analysts. Surprising declines in the August business surveys mirrored a fall in industrial production (-0.4% mpc), and a disappointing September manufacturing PMI outturn implies more of the same. Despite a surge in consumer confidence in August and September, and increased personal income and spending in July, retail sales fell in August (-0.3% mpc). Non-farm payrolls showed jobs growth of 151,000 in August, well below growth of 275,000 in July, but the unemployment rate was stable (4.9%) and earnings growth robust (2.4% apc). Housing market indicators remained mixed.

Inflation outturns diverged, as PCE inflation (the Fed's preferred measure) eased slightly to 0.8% in the year to July (core 1.6%), but annual headline CPI inflation rose to 1.1% in August (core 2.3%). At its September meeting, the Federal Reserve noted the case for a rate hike had "strengthened", but kept policy settings unchanged in order to "*wait for further evidence of continued progress towards its objectives*". The move was in line with expectations, and markets price a 44% probability of a hike in December.

**…while Japan's outturns were soft, and the BoJ changes monetary policy target**

Japan's June quarter GDP growth was revised up from 0.0% to 0.2%, with greater private capital expenditure and inventory investment. Activity deteriorated in July from a year ago, as trade declined (exports and imports fell 14% and 21% respectively), retail sales were down 0.2%, and industrial production fell 0.9%. Indicators of more recent activity appear mixed, as consumer confidence picked up in August, the manufacturing PMI expanded in September, and the unemployment rate eased slightly to 3.0%, but the August services PMI and small business confidence fell.

Japan's consumer price deflation continued for the fourth consecutive month, with headline inflation of -0.4% and core inflation (ex. fresh food) of -0.5% in the year to July. The apparent ineffectiveness of monetary policy and the perceived costs of negative interest rates prompted the BoJ to undertake a *Comprehensive Assessment* of monetary policy. The *Assessment* pointed to external factors (such as oil prices and weak global demand) and backward-looking inflation expectations to explain Japan's subdued domestic inflation. While negative interest rates had lowered borrowing costs in the economy, the associated flat yield curve was identified as having a negative effect on financial institutions' margins – detrimental for both profitability and the ability of banks to pass on further rate cuts to deposit rates.

In response, the BoJ unveiled a new monetary policy framework focusing on controlling the yield curve. In particular, a new target was introduced aimed at maintaining 10-year yields around zero percent, and the Bank committed to overshoot the price stability target in an effort to strengthen the forward-looking component of inflation expectations. Markets remain sceptical about the chances of success of these new targets. The policy rate (currently -0.1%), quantitative easing and equity fund purchases were kept unchanged.

**Australia's June quarter GDP growth eased…**

June quarter GDP growth in Australia was 0.5% (3.3% annual), down from 1.0% in March. Housing and public expenditure drove growth, both of which are expected to remain at high levels given a backlog of consents and state spending commitments. Softer consumer spending growth, weaker net exports and declining mining investment dampened growth. Subsequent data for July were mixed, with flat retail sales, a rebound in dwelling approvals (11.3% mpc), and a narrowing trade deficit as exports rose (2.8%) and imports fell (-0.4%).

The Reserve Bank of Australia held its policy rate steady at 1.5% in September, as expected, and indicated the rate would likely remain stable in the near term (market implied probability of a cut in 2016 is 28%). The RBA adopted a new Conduct of Monetary Policy, with a "flexible medium-term inflation target" for "low and stable" inflation "over time" (slightly more flexible wording than the previous target for "low" inflation "over the cycle").

**…but China's growth recovered in August**

While the official and Caixin measures of manufacturing and services PMI were mixed in August, other outturns showed decisive improvements in contrast to July's disappointing outturns across the board. Industrial production growth rose to 6.4% and real retail sales grew 10.6% (apc). Fixed asset investment growth remained at 8.1% (ytd) with higher construction investment. China's exports eased 2.9% (in USD terms), while imports growth was the highest observed in almost two years, up 1.7%, which analysts relate to increased government infrastructure investment. However, price pressures remained muted, as CPI inflation declined from 1.8% to 1.3% (apc), driven by falling growth in food prices, and producer price growth was -0.8% (apc), its highest level since 2012.

**Mixed activity in the euro area…**

Euro area activity was mixed in July, as the unemployment rate remained flat (at 10.1%), but industrial production fell (-1.1%) and a range of business confidence indicators were weaker, possibly indicating some delayed Brexit impact.

The European Central Bank left its policy rates and asset purchase programmes unchanged in September, as headline and core annual CPI inflation were stable in August at 0.2% and 0.8% respectively. The second round of the ECB's TLTRO-II operation was opened this month, offering 0% interest rate loans to banks, and saw an increased uptake compared to the first round, but lower than analysts expected.

**...but UK growth appears unimpeded by Brexit**

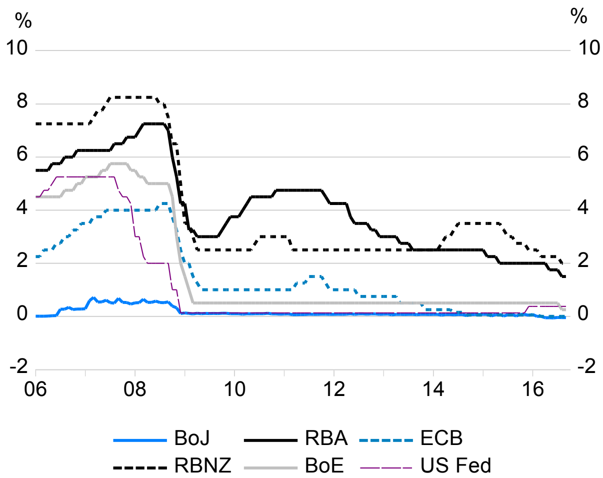
UK's GDP growth in the June quarter was confirmed at 0.6% (2.2% apc), driven by private consumption. The August manufacturing and services PMIs rose sharply, supported by BoE stimulus and greater competitiveness due to the weaker pound. Unemployment in July remained stable at 4.9%, while August retail sales growth was stable at 6.2% (apc). Industrial production rose 2.1% in the year to July, but manufacturing output growth was weaker at 0.8%. Analysts continue to anticipate growth will slow post-Brexit, but these outturns indicate the short-term impacts of Brexit may be more modest than expected.

Consumer prices rose 0.6% in the year to August (1.3% core). The Bank of England left its policy rate unchanged at 0.25% at its September meeting, in line with market pricing, and seems less likely to ease further in the near term.

**New Zealand fundamentals strong**

New Zealand's GDP growth and interest rates are amongst the highest in the advanced economies, reflected in a NZD TWI that currently sits 9% above its 10-year average. Markets expect further RBNZ easing aimed at lifting inflation, in line with other central banks around the world (Figure 8), which will strengthen New Zealand's already robust growth outlook. Continued strong growth, in turn, is expected to maintain high demand for the New Zealand dollar and equities (with the NZD TWI up 11% and the NZX 50 Index up 29% in the past year).

**Figure 8: Central bank policy rates**




Source: Haver

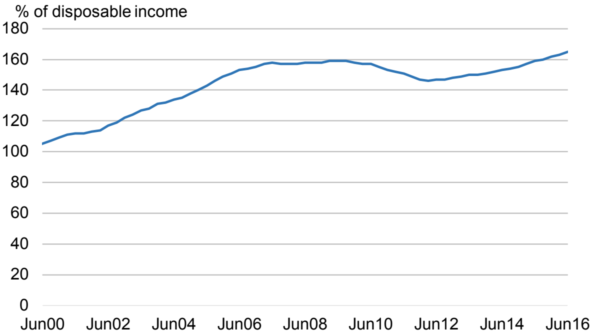
# Special Topic: New Zealand Household Debt

Debt, and household debt in particular, garnered considerable attention earlier in the year. This special topic provides an overview of household debt developments following the release by the Reserve Bank in September of its latest household balance sheet data. At an aggregate level there are reasons to believe that debt levels remain manageable, albeit with debt levels being influenced by house price developments. At an individual level there are likely to be subgroups of households that are more exposed, with high debt levels increasing households' vulnerability to shocks in income, employment and interest rates.

### Household debt continues to rise…

Household debt relative to disposable income increased to 165 percent in June (Figure 1). Debt to income has been rising since March 2012 and is currently slightly higher than the level that prevailed over 2007 to 2010.

**Figure 1: Household debt***



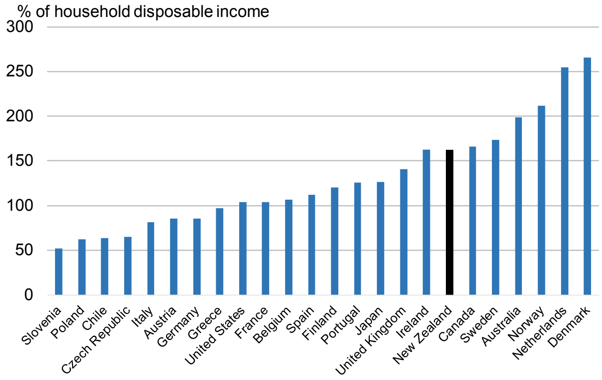

*includes rental property loans

Source: RBNZ

### … but is within OECD norms

International comparisons of household debt levels are problematic. The OECD-sourced data in Figure 2 does not include New Zealand given our lack of National Accounts balance sheet data. Comparing the RBNZ-sourced New Zealand data with those of the OECD would place New Zealand in the top of the third quartile. However, the figure for New Zealand includes rental property loans, some of which - depending on the nature of ownership - could be reclassified to other (non-household) sectors. Excluding rental property loans entirely would result in a debt to income ratio between Belgium and Spain - in the middle of the distribution.

**Figure 2: Household debt across countries**




Sources: OECD, RBNZ

### Several features limit concerns about debt levels

From a macroeconomic perspective, it is not clear what levels of debt are "too high" or problematic with the ability to take on debt playing an important role in enabling households to spread the cost of expensive assets, such as housing, across time.

At an aggregate or macroeconomic level several features of the recent build-up of debt limit concern, namely:

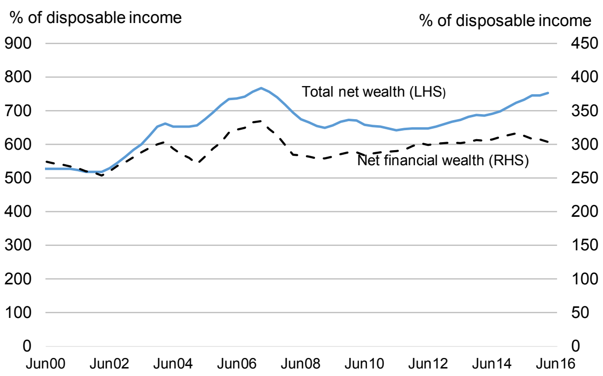
- The accumulation of debt has to date not been the result of sustained dissaving;
- Debt servicing rates are well within historical ranges and may fall further;
- Net wealth and (until recently) net financial wealth has been increasing; and
- Housing debt to asset ratios have fallen.

### Until recently growth in household financial assets had been outpacing debt…

While household debt to income has been increasing since 2010, household financial assets had been growing more rapidly and as a result net financial wealth was increasing (Figure 3). Coupled with rising house prices, overall household net wealth is returning towards pre global financial crisis (GFC) levels.

However, the latest vintage of wealth data incorporates downward revisions to the valuation of equity holdings by households and as a result net financial wealth to income has been declining over the past year, with increases in net wealth driven by house price increases.

**Figure 3: Net wealth and net financial wealth**

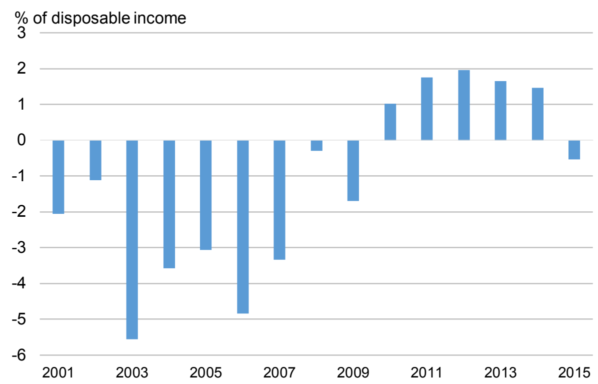



Source: RBNZ

## … reflecting a change in household behaviour post GFC…

Since the global financial crisis, there has been quite a marked change in household saving behaviour. Between 2010 and 2014 household saving was positive following negative rates over the 9 years prior (Figure 4). Saving turned slightly negative in 2015 reflecting a large fall in farm income which declined by 2.5 percentage points of disposable income. Nevertheless, the rate of dissaving (at 0.5%pts of disposable income) was modest relative to the mid-2000s.

**Figure 4: Household saving**



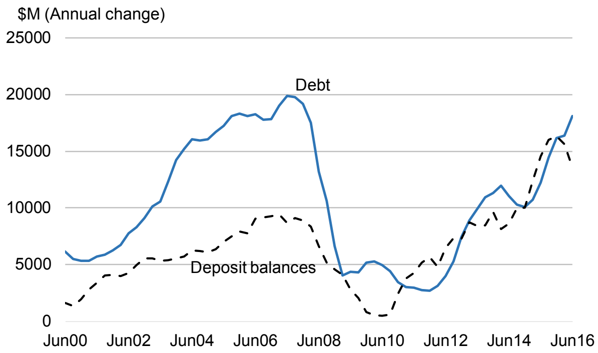

Source: Statistics NZ

One balance sheet manifestation of this change in behaviour was that household deposit holdings had been growing at around, or slightly faster than, the accumulation of debt. This contrasts to the experience of the 2000s of consistently higher debt accumulation (Figure 5).

## … although recent divergence worth monitoring

Rising net financial wealth and the pattern of an approximate matching of debt growth and deposit holdings were reasons to help balance concerns about rising indebtedness. The recent divergence shown in Figure 5 is still too short and small to call a trend, but if it were to continue may challenge a relatively sanguine view of household indebtedness.

**Figure 5: Annual change in debt and deposits**

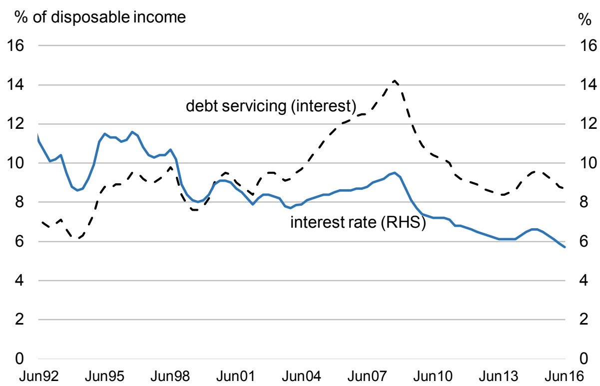



Source: RBNZ

## Debt servicing has fallen…

While debt levels have been rising, declines in interest rates have meant that debt servicing has fallen. Debt servicing (interest costs) peaked at 14% of disposable income in 2008. As interest rates have fallen debt servicing costs declined to 8.4% of disposable income in 2013 and currently sit just below 9% (Figure 6).

**Figure 6: Debt servicing**




Source: RBNZ

The future evolution of debt servicing rates will be influenced by both the accumulation of debt and interest rate developments. With current market mortgage rates below the average interest rate currently being paid, it is likely that average interest rates will continue to decline over the year ahead. Future increases in interest rates would increase debt servicing rates. Whether this results in debt servicing rates exceeding previous highs will depend on the extent and timing of interest rate increases.

## … as has the extent to which the housing stock is leveraged

Housing debt relative to the overall value of housing assets fell to a series low (dating back to 1998) of just under 24% in March 2016 after being just below 29% at the start of 2009 and in late 2001. House prices would need to fall around 17% for leverage to return to its previous peaks.

**Aggregate data may hide areas of greater pressure…**

While the focus of this special topic has been on aggregate household wealth data, it is possible that this may hide issues if debt is concentrated in particular groups of households. In particular, high Auckland house prices mean that new entrants need to take on high debt levels.

**… particularly debt servicing risks for new entrants in Auckland**

Estimates of debt servicing ratios for representative new buyers in Auckland are elevated (around 46% of income) even with current low interest rates. They would pass previous peaks if mortgage rates were to return to their 10-year average of 6.7%.[3] A representative buyer is defined as one buying an average value house, on an average income, with a 20 percent deposit.

**… although these buyers may have higher than average incomes**

Actual new buyers may face higher or lower debt servicing rates depending on their particular circumstances. Previous research covering buyers during the 2005 to 2013 period highlighted that new buyers on average had disposable incomes that were 40% higher than the overall median.[4] Nevertheless, debt servicing rates for many new buyers are likely to be relatively high at a time when interest rates are relatively low.

**Domestic factors are unlikely to lead to aggregate distress**

Almost by definition, higher debt levels mean that households are more exposed to increases in interest rates. However, in the absence of positive demand shocks, it is unlikely that interest rates will rise over the next few years. Domestically driven increases in interest rates via increases to the official cash rate will be dependent on inflationary pressures increasing as domestic activity grows. This is likely to be associated with stronger nominal income growth and an improving labour market. Higher rates of debt mean that monetary policy may be more effective in influencing demand with interest rates not needing to rise as much as in the past.

Overall, at the macroeconomic level there are reasons to limit concern about household debt developments, while being cognisant of the risks. These risks may increase if the most recent developments of declining net financial wealth were to continue or accelerate.

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



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3 See *RBNZ Financial Stability Report – May 2016*

4 *Vulnerability of new mortgage borrowers to the introduction of the LVR speed limit: Insights from the Household Economic Survey* by Ashley Dunstan and Hayden Skilling (RBNZ analytical note 2015/02)

# New Zealand Key Economic Data

## Quarterly Indicators

| | | 2015Q1 | 2015Q2 | 2015Q3 | 2015Q4 | 2016Q1 | 2016Q2 | 2016Q3 |
|---|---|---|---|---|---|---|---|---|
| **Gross Domestic Product (GDP)** | | | | | | | | |
| Real production GDP | qtr % chg[1] | 0.2 | 0.4 | 0.8 | 0.9 | 0.9 | 0.9 | ... |
| | ann ave % chg | 3.6 | 3.3 | 2.9 | 2.5 | 2.5 | 2.8 | ... |
| Real private consumption | qtr % chg[1] | 0.6 | 0.3 | 0.7 | 0.9 | 0.5 | 1.9 | ... |
| | ann ave % chg | 2.6 | 2.7 | 2.3 | 2.3 | 2.3 | 2.7 | ... |
| Real public consumption | qtr % chg[1] | 0.8 | 0.7 | 0.3 | -0.2 | 0.6 | 1.0 | ... |
| | ann ave % chg | 2.3 | 2.1 | 2.0 | 2.0 | 1.8 | 1.7 | ... |
| Real residential investment | qtr % chg[1] | 0.3 | 0.4 | 1.5 | 1.5 | 4.9 | 6.0 | ... |
| | ann ave % chg | 11.5 | 8.6 | 7.8 | 5.9 | 7.2 | 10.3 | ... |
| Real non-residential investment | qtr % chg[1] | -2.5 | 1.3 | 2.6 | -2.8 | 1.8 | 1.7 | ... |
| | ann ave % chg | 9.0 | 7.5 | 4.9 | 1.9 | 1.4 | 1.3 | ... |
| Export volumes | qtr % chg[1] | 1.8 | 0.1 | 2.0 | -0.1 | -0.4 | 4.0 | ... |
| | ann ave % chg | 4.3 | 5.9 | 7.6 | 6.8 | 5.5 | 4.9 | ... |
| Import volumes | qtr % chg[1] | 0.8 | 1.1 | -2.3 | 0.8 | 0.7 | 2.6 | ... |
| | ann ave % chg | 7.4 | 6.6 | 5.6 | 3.6 | 2.1 | 1.2 | ... |
| Nominal GDP - expenditure basis | ann ave % chg | 3.6 | 2.8 | 2.8 | 3.2 | 3.8 | 4.2 | ... |
| Real GDP per capita | ann ave % chg | 1.9 | 1.5 | 1.1 | 0.6 | 0.5 | 0.7 | ... |
| Real Gross National Disposable Income | ann ave % chg | 3.3 | 2.1 | 1.3 | 1.4 | 2.0 | 2.6 | ... |
| **External Trade** | | | | | | | | |
| Current account balance (annual) | NZ$ millions | -8,469 | -8,752 | -8,529 | -8,321 | -7,821 | -7,384 | ... |
| | % of GDP | -3.5 | -3.6 | -3.5 | -3.4 | -3.1 | -2.9 | ... |
| Investment income balance (annual) | NZ$ millions | -9,566 | -9,499 | -9,581 | -9,207 | -8,752 | -8,374 | ... |
| Merchandise terms of trade | qtr % chg | 1.2 | 1.5 | -3.8 | -2.0 | 4.2 | -2.1 | ... |
| | ann % chg | -5.6 | -4.2 | -3.6 | -3.2 | -0.4 | -3.9 | ... |
| **Prices** | | | | | | | | |
| CPI inflation | qtr % chg | -0.2 | 0.4 | 0.3 | -0.5 | 0.2 | 0.4 | ... |
| | ann % chg | 0.3 | 0.4 | 0.4 | 0.1 | 0.4 | 0.4 | ... |
| Tradable inflation | ann % chg | -2.4 | -1.8 | -1.2 | -2.1 | -1.2 | -1.5 | ... |
| Non-tradable inflation | ann % chg | 2.4 | 2.1 | 1.5 | 1.8 | 1.6 | 1.8 | ... |
| GDP deflator | ann % chg | -0.8 | 0.5 | 0.8 | 0.4 | 1.3 | 1.3 | ... |
| Consumption deflator | ann % chg | 0.5 | 0.6 | 1.1 | 0.7 | 0.8 | 0.7 | ... |
| **Labour Market** | | | | | | | | |
| Employment (HLFS) | qtr % chg[1] | 0.6 | 0.0 | -0.3 | 0.9 | 1.4 | 2.4 | ... |
| | ann % chg[1] | 3.2 | 2.9 | 1.5 | 1.3 | 2.0 | 4.5 | ... |
| Unemployment rate | %[1] | 5.4 | 5.5 | 5.5 | 5.0 | 5.2 | 5.1 | ... |
| Participation rate | %[1] | 69.3 | 68.9 | 68.3 | 68.2 | 68.8 | 69.7 | ... |
| LCI salary & wage rates - total (adjusted)[5] | qtr % chg | 0.3 | 0.5 | 0.4 | 0.4 | 0.4 | 0.4 | ... |
| | ann % chg | 1.7 | 1.6 | 1.6 | 1.5 | 1.6 | 1.5 | ... |
| QES average hourly earnings - total[5] | qtr % chg | 0.0 | 0.8 | 1.0 | 0.3 | 0.3 | 0.5 | ... |
| | ann % chg | 2.1 | 2.8 | 2.3 | 2.1 | 2.4 | 2.1 | ... |
| Labour productivity[6] | ann ave % chg | 0.5 | 0.6 | 0.7 | 0.5 | 0.9 | -0.1 | ... |
| **Retail Sales** | | | | | | | | |
| Core retail sales volume | qtr % chg[1] | 2.2 | 0.0 | 1.2 | 1.4 | 1.1 | 2.6 | ... |
| | ann % chg | 7.2 | 5.8 | 5.2 | 5.2 | 4.8 | 6.4 | ... |
| Total retail sales volume | qtr % chg[1] | 2.1 | 0.1 | 1.5 | 1.1 | 1.0 | 2.3 | ... |
| | ann % chg | 7.1 | 5.5 | 5.7 | 5.3 | 4.9 | 6.0 | ... |
| **Confidence Indicators/Surveys** | | | | | | | | |
| WMM - consumer confidence[3] | Index | 117 | 113 | 106 | 111 | 110 | 106 | 108 |
| QSBO - general business situation[4] | net % | 23.3 | 5.1 | -14.5 | 14.7 | 1.7 | 18.6 | ... |
| QSBO - own activity outlook[4] | net % | 25.0 | 9.3 | 21.7 | 21.6 | 3.8 | 16.8 | ... |

## Monthly Indicators

| | | 2016M03 | 2016M04 | 2016M05 | 2016M06 | 2016M07 | 2016M08 | 2016M09 |
|---|---|---|---|---|---|---|---|---|
| **External Sector** | | | | | | | | |
| Merchandise trade - exports | mth % chg[1] | -7.5 | 11.6 | -1.4 | -1.0 | 4.1 | -3.0 | ... |
| | ann % chg[1] | -14.4 | 4.7 | 4.7 | 2.3 | -4.9 | -8.7 | ... |
| Merchandise trade - imports | mth % chg[1] | -17.3 | 24.2 | -1.4 | -1.1 | 1.8 | -8.6 | ... |
| | ann % chg[1] | -5.5 | 0.7 | 5.7 | -4.5 | -11.9 | -3.1 | ... |
| Merchandise trade balance (12 month total) | NZ$ million | -3765 | -3600 | -3624 | -3335 | -2956 | -3131 | ... |
| Visitor arrivals | number[1] | 288,210 | 284,680 | 285,230 | 282,990 | 290,980 | 285,340 | ... |
| Visitor departures | number[1] | 284,010 | 294,450 | 295,070 | 286,630 | 297,950 | 284,450 | ... |
| **Housing** | | | | | | | | |
| Dwelling consents - residential | mth % chg[1] | -9.4 | 6.9 | -0.2 | 21.9 | -10.5 | ... | ... |
| | ann % chg[1] | 1.9 | 11.8 | 16.1 | 34.8 | -0.5 | ... | ... |
| House sales - dwellings | mth % chg[1] | 5.2 | 8.2 | -3.4 | -2.1 | -10.5 | 9.5 | ... |
| | ann % chg[1] | 8.2 | 18.4 | 13.6 | 5.9 | -10.1 | -3.1 | ... |
| REINZ - house price index | mth % chg | 2.2 | 2.2 | 2.0 | 1.7 | 2.6 | -2.2 | ... |
| | ann % chg | 13.3 | 14.5 | 14.7 | 14.2 | 16.3 | 11.7 | ... |
| **Private Consumption** | | | | | | | | |
| Electronic card transactions - total retail | mth % chg[1] | 0.1 | 0.8 | -0.2 | 1.1 | 0.2 | -0.4 | ... |
| | ann % chg | 6.2 | 7.8 | 3.3 | 6.8 | 5.8 | 3.7 | ... |
| New car registrations | mth % chg[1] | -3.8 | 6.2 | -3.5 | -0.9 | -0.3 | 10.1 | ... |
| | ann % chg | -0.2 | 8.7 | 4.2 | -1.2 | -1.9 | 10.5 | ... |
| **Migration** | | | | | | | | |
| Permanent & long-term arrivals | number[1] | 9,900 | 10,430 | 10,220 | 10,240 | 10,430 | 10,300 | ... |
| Permanent & long-term departures | number[1] | 4,560 | 4,940 | 4,670 | 4,540 | 4,810 | 4,700 | ... |
| Net PLT migration (12 month total) | number | 67,619 | 68,110 | 68,432 | 69,090 | 69,015 | 69,119 | ... |
| **Commodity Prices** | | | | | | | | |
| Brent oil price | US$/Barrel | 38.20 | 41.58 | 46.74 | 48.25 | 44.95 | 45.84 | ... |
| WTI oil price | US$/Barrel | 37.80 | 40.76 | 46.76 | 48.80 | 44.69 | 44.76 | ... |
| ANZ NZ commodity price index | mth % chg | -3.0 | -2.8 | 2.5 | 0.1 | -0.3 | 1.9 | ... |
| | ann % chg | -14.3 | -8.5 | -3.5 | -6.1 | -5.8 | -0.5 | ... |
| ANZ world commodity price index | mth % chg | -1.3 | -0.8 | 1.0 | 3.5 | 2.1 | 3.2 | ... |
| | ann % chg | -22.4 | -16.8 | -11.7 | -5.6 | 1.9 | 11.1 | ... |
| **Financial Markets** | | | | | | | | |
| NZD/USD | $[2] | 0.6733 | 0.6892 | 0.6804 | 0.7034 | 0.7123 | 0.7229 | *0.7315* |
| NZD/AUD | $[2] | 0.9001 | 0.8998 | 0.9290 | 0.9502 | 0.9472 | 0.9481 | *0.9658* |
| Trade weighted index (TWI) | June 1979 = 100[2] | 72.19 | 72.80 | 72.86 | 75.23 | 76.30 | 76.77 | *77.94* |
| Official cash rate (OCR) | % | 2.25 | 2.25 | 2.25 | 2.25 | 2.25 | 2.00 | 2.00 |
| 90 day bank bill rate | %[2] | 2.43 | 2.34 | 2.38 | 2.37 | 2.37 | 2.24 | *2.23* |
| 10 year govt bond rate | %[2] | 3.02 | 2.86 | 2.68 | 2.51 | 2.27 | 2.20 | *2.41* |
| **Confidence Indicators/Surveys** | | | | | | | | |
| ANZ - business confidence | net % | 3.2 | 6.2 | 11.3 | 20.2 | 16.0 | 15.5 | ... |
| ANZ - activity outlook | net % | 29.4 | 32.1 | 30.4 | 35.1 | 31.4 | 33.7 | ... |
| ANZ-Roy Morgan - consumer confidence | net % | 118.0 | 120.0 | 116.2 | 118.9 | 118.2 | 117.7 | 121.0 |
| Performance of Manufacturing Index | Index | 54.8 | 56.6 | 57.0 | 57.5 | 55.5 | 55.1 | ... |
| Performance of Services Index | Index | 55.2 | 57.8 | 56.9 | 56.6 | 54.5 | 57.9 | ... |

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

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

Sources: Statistics New Zealand, Reserve Bank of New Zealand, NZIER, ANZ, Haver Analytics, Thompson Reuters, Westpac McDermott Miller, ANZ-Roy Morgan, REINZ, BNZ-Business NZ