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MONTHLY ECONOMIC REVIEW

October 2009

(latest data as at 6 October)

Parliamentary Library Research Paper

A Overview

Recent trend

		07/08	08/09	
↘	Economic Growth	2.5%	-1.8%	Annual average GDP Growth (June year)
↗	Unemployment	4.0%	6.0%	Unemployment Rate (June quarter)
↘	Inflation	4.0%	1.9%	Annual Inflation Rate (June year)
↘	Current Account Deficit	$14.8b	$10.6b	Current Account Deficit (June year)
↘	Interest Rates	7.95%	2.77%	90 Day Bank Bills (September month)

Latest data

In the words of Reserve Bank Governor, Alan Bollard, *"a patchy recovery is underway".* Following five consecutive quarters of contraction, the economy grew by just under 0.1 percent in the June 2009 quarter. An increase in exports, along with a drop in imports made a significant contribution to growth. This was partially offset by a huge drawdown in inventories. On an annual average basis, the economy contracted by 1.8 percent over the year ended June 2009. Fonterra has revised upward their forecast milk payout for the 2009/10 season by 55 cents per kilogram of milksolids to $5.10. It is thought that the increase in the payout will deliver an additional $750 million to $1,000 million into the rural economy over the coming season. Average prices for whole milk powder in Fonterra's October online auction were US$3,022 per tonne, up 5.7 percent from the previous month. New Zealand's current account deficit eased back to $10,614 million (equivalent to 5.9 percent of GDP) due to an improved merchandise trade balance and lower profits earned by foreign investors on their New Zealand investments. In particular, the Bank of New Zealand recorded a tax liability provision of $661 million, which reduced the net profits accrued to its Australian parent. Reserve Bank Governor, Alan Bollard, left the official cash rate steady at 2.50 percent in September, stating that *"we continue to expect to keep the OCR at or below the current level through until the latter part of 2010".*

Outlook

A fragile recovery is underway, although current consumer and business confidence levels are consistent with a robust rate of growth next year. It remains to be seen whether the reality matches current expectations, given weak demand growth for exports, rising unemployment levels, and a reduction in business investment intentions. However, positive economic growth is forecast for the September and December quarters. On an annual average basis, the NZIER Consensus Forecasts has the economy contracting by 1.3 percent over the year to March 2010, before returning to growth in the following year. Given increased unemployment and spare capacity within the economy, the inflationary environment is benign, with the annual inflation rate forecast to remain comfortably within the Reserve Bank target band for the foreseeable future.

Topic of the month: Household assets and liabilities

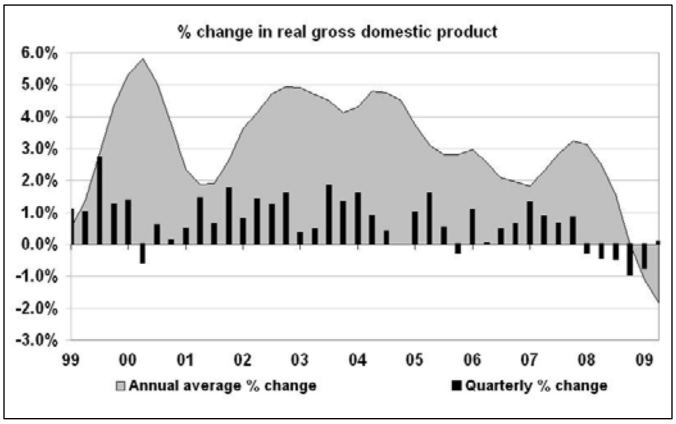
B Economic Growth

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 growth has returned to New Zealand, with the economy expanding by 0.1 percent over the June 2009 quarter. This marks a technical end to New Zealand's recession, which has lasted for five consecutive quarters. However, it must be noted that the growth rate was rounded up to 0.1 percent, and that Statistics New Zealand said in their release, *"because this movement is so close to zero, no significant conclusions can be drawn that this is a turning point".*



In annual average percentage terms, economic activity fell by 1.8 percent over the year ended June 2009. This was the largest fall in economic output recorded in annual average terms since the current GDP series began in 1987. Over the year, investment in residential buildings fell by almost a quarter, while investment in other fixed assets fell by 8.2 percent. Value-added output from the construction industry fell by 9.3 percent.

Other data

Fonterra has increased their forecast payout for the 2009/10 season to $5.10 per kilogram of milksolids, an increase of 55 cents per kilogram over the previous forecast. The higher revised payout was due to a sustained increase in commodity returns, along with a more positive outlook in the international dairy markets. Both business and consumer confidence have rebounded, driven by an increase in optimism regarding future conditions, rather than being due to an improvement in current conditions. The *Westpac McDermott Miller Consumer Confidence index* has risen to a four year high, while businesses' own activity outlook in the National Bank's *Business Outlook* survey was the highest since March 2005 (on a seasonally adjusted basis). The latest NZIER *Quarterly Survey of Business Opinion* also *"surged into positive territory".*

Year ended June 2009	Nominal GDP
Expenditure GDP	$180,210 million
GDP per capita	$41,955

Source: Statistics New Zealand.

Outlook

There is a wide divergence of views regarding the track that the economic recovery will take. Job losses and limited wage growth will hamper household consumption expenditure over the near term, although economic growth is expected over the September and December quarters. The average forecast in the NZIER Consensus Forecasts is for a contraction of 1.3 percent for the March 2010 year, before growth returns in the following March year.

Net % expecting economic improvement in 12 months	Aug-09	Sep-09
NBNZ – Business Confidence	34.2	49.1
NBNZ – Own Activity	26.0	32.2

Source: National Bank.

GDP growth (%)	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09
Annual (year-on-year)	2.5	1.5	0.0	-1.1	-1.8
Quarterly (seasonally adjusted)	-0.4	-0.5	-1.0	-0.8	0.1

Source: Statistics New Zealand.

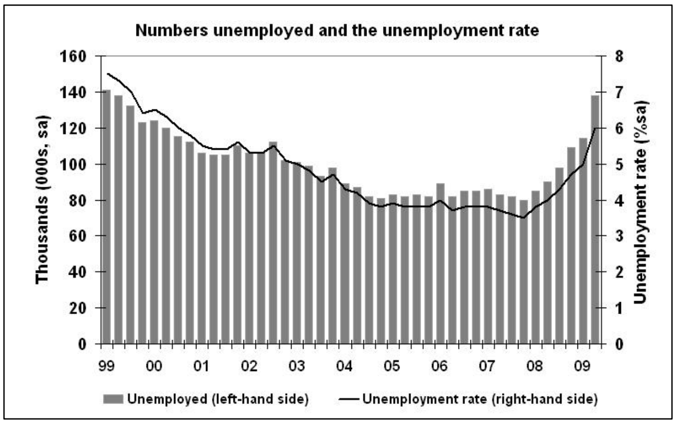
Next Release: *Gross Domestic Product: September 2009 quarter.* **Date:** *23 December 2009*

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

The labour market continues to weaken, with New Zealand's unemployment rate rising by one percentage point to six percent in the June 2009 quarter. There were 138,000 people unemployed in the quarter, up from 90,000 for the same quarter last year (in seasonally adjusted terms).



The unemployment rate for the Northland region has almost doubled over the past year, increasing from 4.2 percent in the June 2008 quarter to 8.3 percent in the June 2009 quarter (in actual terms). Nationally, in the June 2009 quarter, regional unemployment rates ranged from 3.1 percent for the Tasman, Nelson, Marlborough, West Coast regions to 8.3 percent for the Northland region.

There were 114,300 people working part-time (less than 30 hours per week) in the June 2009 quarter who stated that they would have preferred to be working additional hours. They are considered to be 'underemployed', and their number has been growing steadily from 82,000 people in the September 2008 quarter. There has also been a rise in the number of people considered 'jobless'. The jobless figure includes (i) those officially unemployed, (ii) those that are available for work, but not actively seeking work, and (iii) those actively seeking work, but not available for work. In the June 2009 quarter, there were 236,100 people considered to be 'jobless' (up from 170,500 in the June 2008 quarter).

Other data

Employee optimism has returned, with the latest *Westpac McDermott Miller Employee Confidence Index* in positive territory. Key drivers behind the increase in optimism were improved perceptions of job security, and expectations of better job opportunities and earnings being available next year. In line with these results, a net two percent of respondents to the National Bank's *Business Outlook* survey expected to increase employment over the coming twelve months.

Net % expecting increase in 12 months*	Aug-09	Sep-09
Employment in their business	-2.6	1.8
Unemployment rate	63.6	50.0

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

Outlook

The unemployment rate looks set to increase further over the short-term, although forecasters have been adjusting downward the level at which they expect the unemployment rate to peak. Respondents to the NZIER Consensus Forecasts expect the unemployment rate to peak at 7.3 percent in the March 2011 quarter, with an additional 30,000 jobs to be lost.

Quarter (%)	Jun-08	Jun-09
Average ordinary time weekly earnings (pre-tax)	$886.11	$928.61
Percentage change in hourly earnings from the same period of the previous year	+4.7	+4.8

Source: Statistics New Zealand.

Household Labour Force Survey	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09
Unemployment Rate (seasonally adjusted, %)	4.0	4.3	4.7	5.0	6.0
Employment Growth (annual, %)*	0.8	1.0	1.0	0.8	-0.9

*change since the same quarter of the previous year. Source: Statistics New Zealand.

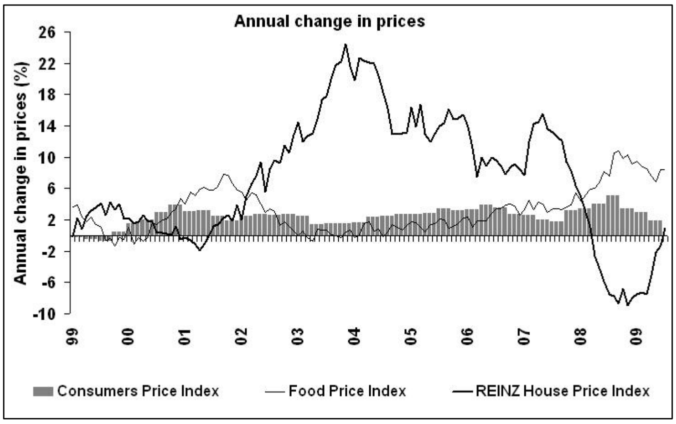
Next Release: *Household Labour Force Survey: September 2009 quarter.* **Date:** *5 November 2009*

D Inflation

Background

Inflation is the change in prices of goods and services over a certain period of time. The official rate of inflation is measured by Statistics New Zealand's Consumer 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 0.6 percent over the June 2009 quarter, resulting in an annual inflation rate of 1.9 percent for the year ended in the June 2009 quarter. The annual rate of inflation has been within the Reserve Bank's medium term target band (1 – 3 percent) since the March 2009 quarter, having previously peaked at an annual rate of 5.1 percent in the September 2008 quarter.

Tradable inflation was 0.2 percent over the year ended in the June 2009 quarter (mainly due to lower fuel prices), while non-tradable inflation was 3.3 percent. The non-tradable inflation rate is at its lowest annual rate since June 2002. It reflects an easing in wage inflation, and in inflationary pressures generally, as capacity utilisation falls.

Other data

The *REINZ Housing Price Index* rose by 2.6 percent in August 2009 when compared with the same month last year. However, house prices remain 6.2 percent below their November 2007 peak (in nominal terms). A general shortage of listings is continuing to lead to competition amongst buyers for quality properties that are well priced. The average property price in New Zealand was $385,426 in August 2009, according to Quotable Value.

Annual Percentage Change (%)	Jul-09	Aug-09
Quotable Value – Residential property*	-5.0	-2.8
REINZ Housing Price Index**	0.9	2.6
Food Price Index**	8.4	4.6

*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

New Zealand's inflation outlook is benign, with the Reserve Bank projecting an annual inflation rate of 1.2 percent for the year ended in the September 2009 quarter. Furthermore, the Bank has projected that the annual rate of inflation will remain within the target band over its forecast period. A net nine percent of respondents to the latest National Bank *Business Outlook* survey are expecting to increase their prices over the coming three months. According to the National Bank, this result is consistent with an annual inflation rate of around one percent.

National Bank Business Survey	Aug-09	Sep-09
Net % of respondents expecting to increase prices in 3 months time*:	15.2	8.9
Inflation expected in 12 months time:	2.52	2.57

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

Inflation (%)	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09
Consumers Price Index - Annual	4.0	5.1	3.4	3.0	1.9
Tradables inflation	*4.8*	*6.3*	*2.3*	*1.7*	*0.2*
Non-tradables inflation	*3.4*	*4.1*	*4.3*	*3.8*	*3.3*
CPI - quarterly	1.6	1.5	-0.5	0.3	0.6

Source: Statistics New Zealand.

Next Release: *Consumers Price Index: September 2009 quarter.* **Date:** *15 October 2009*

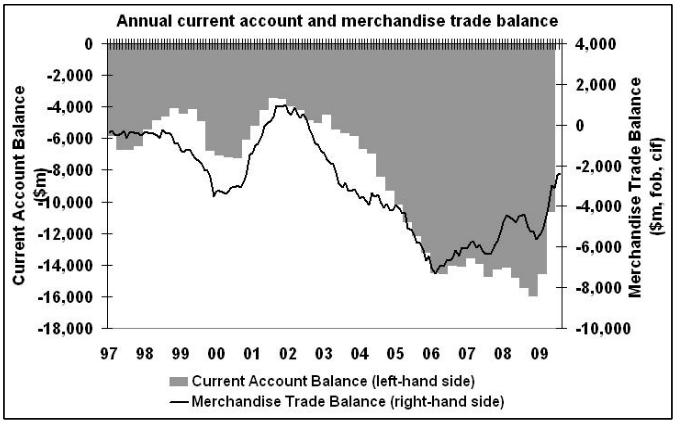
E External

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 investment income, and current transfers (e.g. foreign aid). A "balance of payments deficit" refers to a deficit of the current account.

Current account deficit

The current account deficit for the June 2009 quarter was $612 million on a seasonally adjusted basis, a decrease of $1,508 million from the previous quarter. A reduction in income earned by foreign investors on their New Zealand investments over the June quarter was a main driver behind the decrease. A factor behind the fall in foreign investors' incomes included a $661 million tax liability provision made by the Bank of New Zealand following legal action by the Inland Revenue Department (which reduces the net profit accrued to its Australian parent).



On an annual basis the actual current account deficit totalled $10,614 million, equivalent to 5.9 percent of gross domestic product. This is the smallest deficit recorded as a percentage of GDP since the year ended September 2004. It compares with an annual deficit of $14,569 million for the year ended March 2009 (which was revised down from 8.5 percent to 8.1 percent of GDP). As at 30 June 2009, New Zealand's international liabilities exceeded its international assets by $171.6 billion (equivalent to 95.2 percent of GDP).

Other data

The merchandise terms of trade (which measures the quantity of imports that can be purchased with a fixed quantity of exports) fell by nine percent in the June 2009 quarter. This follows a fall in the four previous consecutive quarters. The terms of trade index is now at its lowest level since the September 2006 quarter.

Annual Change (%)	Aug-09	Sep-09
World Commodities Prices*	-22.7	-13.0
NZ$ Commodities Prices*	-21.4	-18.6
Overseas Visitors**	-2.8	*n/a*

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

Outlook

Economic commentators are questioning the sustainability of the improvement in the current account deficit, given that its recent improvement has been due to lower earnings from foreign investors (due to lower profits levels and interest rates), along with a reduction in imports. While further improvement is expected in the short-term, the deficit has been forecast to start rising as a percentage of GDP later next year.

Annual Balances ($m)	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Aug-09
Current Account	-14,795	-15,437	-15,969	-14,569	-10,614	*n/a*
Merchandise trade	*-1,904*	*-2,326*	*-2,382*	*-1,336*	528	*n/a*
Services	*-118*	*-425*	*-908*	*-1,118*	-977	*n/a*
Investment income	*-13,732*	*-13,728*	*-13,721*	*-13,035*	-11,027	*n/a*
Current transfers	*958*	*1,042*	*1,041*	*920*	861	*n/a*
Current Account (quarter*)	-4,622	-4,053	-3,608	-2,102	-612	*n/a*
Merchandise Trade (fob-vfd)	-1,897	-2,327	-2,729	-1,824	-410	195
Merchandise Trade (fob-cif)	-4,478	-5,048	-5,614	-4,684	-3,111	-2,365

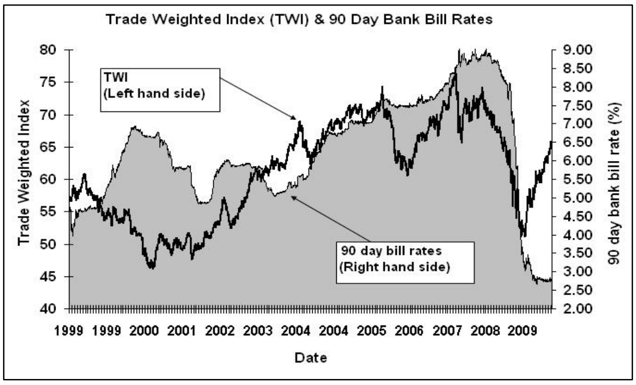
* Seasonally adjusted. VFD – The value of imports before insurance and freight costs. CIF – Cost of goods imported, including insurance and freight to New Zealand. FOB – Free on board, the value of goods at New Zealand ports before export. Source: Statistics New Zealand.

Next Release: *Balance of Payments: September 2009* **Date:** *22 December 2009*

Background

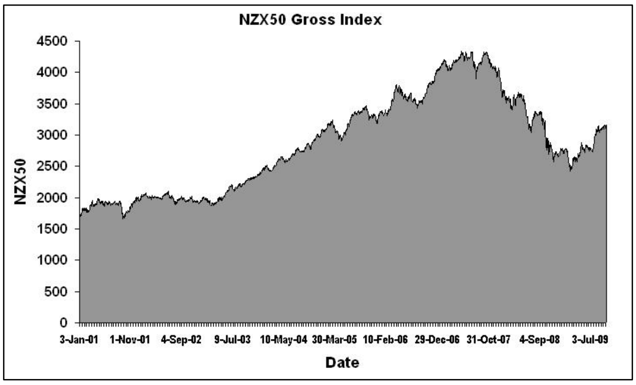
The trade weighted index (TWI) is an index of the New Zealand dollar's value against a basket of five overseas currencies, where each currency is weighted by a combination of the size of the associated country's trade with New Zealand (including the Euro group of countries) and their gross domestic product. 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 trend & latest monthly data



The exchange rate appreciated further during September 2009, averaging 64.32 index points on a trade weighted index (TWI) basis during the month. This represented an increase of 2.3 percent over the previous month's average. As the graph on the right shows, the exchange rate has been appreciating steadily since March 2009.

There were 321 registered mortgagee sales reported by Terralink for July 2009, with 1,583 for the year-to-date. Over recent months, around a fifth of all mortgagee sales have been for single family owned properties, as opposed to being a property development unit, or owned as an investment property.



Since its recent low point in early March 2009, the NZX 50 has risen by over 30 percent as at the end of September to 3161 index points. However, the NZX 50 still remains 27 percent below the high reached in May 2007 of 4333 index points. During September 2009, Fletcher Building overtook Telecom as having the largest market capitalisation on the New Zealand sharemarket. The current market capitalisation of Fletcher Building is $5.15 billion, while Telecom's market capitalisation is $5.03 billion. Together, they account for over 27 percent of the market capitalisation of the NZX 50.

Outlook

The Reserve Bank in their September *Monetary Policy Statement* has projected the 90-day bank bill rate to rise at a steeper rate than had been projected in their June *Statement*. In line with commentary that they tend to leave the official cash rate *"at or below the current level through until the latter part of 2010",* the Bank has projected the 90-day bank bill rate to rise in the December 2010 quarter, and to reach five percent in the March 2012 quarter. Financial markets are expecting an earlier start to official cash rate rises, with a number of banks forecasting these to commence in the first half of 2010. At its current level of 2.50 percent, the official cash rate is providing substantial monetary policy stimulus to the economy, which the Reserve Bank will want to unwind in a timely fashion to prevent inflationary pressures building within the economy. Therefore, it is possible that once they commence, the step increments in the OCR will be larger than 25 basis points.

Monthly averages	Apr-09	May-09	Jun-09	Jul-09	Aug-09	Sep-09
Trade Weighted Index (TWI) exchange rate	56.87	57.95	60.32	60.59	62.85	64.32
90 Day Bank Bill Rate	3.12	2.82	2.78	2.79	2.76	2.77
Official Cash Rate*	2.50	2.50	2.50	2.50	2.50	2.50
NZX50	2643	2787	2798	2843	3081	3126

* actual rate at end of month, the Official Cash Rate is an interest rate set by the Reserve Bank to implement monetary policy.

Sources: Reserve Bank; NZX.

Next Official Cash Rate (OCR) decision: *29 October 2009*

Background

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

Economic growth

Thirteen OECD countries recorded positive economic growth over the June 2009 quarter (including New Zealand), compared with three OECD countries over the March 2009 quarter. Overall, in the June 2009 quarter, economic output within the OECD area was flat when compared with the previous quarter.

The International Monetary Fund expects that the economic recovery will be slow, *"as financial systems remain impaired and support from public policies will gradually have to be withdrawn".* In the IMF's October 2009 *World Economic Outlook*, the Monetary Fund projects that the economies of the world's advanced economies will contract by 3.4 percent in 2009, before expanding by 1.3 percent in 2010. This is an improvement of 0.4 percentage points in 2009 and 0.7 percentage points in 2010 from the Monetary Fund's July 2009 forecasts.

Quarterly economic growth rates

Country	Dec-08	Mar-09	Jun-09
Australia	-0.7	0.4	0.6
Japan	-3.4	-3.3	0.6
NEW ZEALAND	-1.0	-0.8	0.1
United Kingdom	-1.8	-2.5	-0.6
United States	-1.4	-1.6	-0.2
OECD Total	-1.9	-2.2	0.0

Source: OECD

Unemployment

The harmonised unemployment rate within the OECD has risen by 2.4 percentage points during the year, to 8.5 percent for the month of July 2009. Within the member countries of the OECD, the unemployment rate ranges from a lowly 3.1 percent in Norway (as at May 2009) to 18.5 percent in Spain (as at July 2009).

The International Monetary Fund is expecting the unemployment level in the advanced economies to peak at over ten percent. Currently, the unemployment rate in the United States is 9.8 percent.

Harmonsied unemployment rates

Country	Jul-09	Aug-09	Sep-09
Australia	5.8	5.8	
Japan	5.7		
NEW ZEALAND	6.0 (Mar)		
United Kingdom	7.7(May)		
United States	9.4	9.7	9.8
OECD Total	8.5		

Source: OECD

Central banks

In a widely unexpected move, the Australian Reserve Bank has increased its cash rate by 25 basis points to 3.25 percent, effective from 7 October 2009. The majority of economists had believed that the bank would deliver a hawkish statement this month, with an increase in the bank rate to have taken place later this year. In explaining its action, the Bank said that it was prudent to gradually reduce the level of monetary policy stimulus in the local economy due to improving conditions. It has forecast that the Australian economy will grow at a rate close to trend over the year ahead, with the rate of inflation expected to be close to target. The Bank is the first central bank apart from Israel's to start tightening monetary policy since the international financial crisis hit last year.

Central Bank interest rates (as at 6 October 2009)

Central Bank	Key Rate	Interest Rate (%)	Effective from	Direction (Basis points)
Australia	Cash Rate	3.25	7-Oct-09	+25
European Central Bank	Main Refinance Rate	1.00	13-May-09	-25
Japan	Uncollateralized overnight rate	0.10	19-Dec-08	-20
NEW ZEALAND	Official Cash Rate	2.50	30-Apr-09	-50
United Kingdom	Bank Rate	0.50	5-Mar-09	-50
United States	Federal Funds Rate	0.00 – 0.25	16-Dec-08	-75

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

Household assets and liabilities

Total household financial liabilities (excluding student loans) totalled $177 billion as at 31 December 2008, an increase of seven billion dollars from the year before. The vast majority of household liabilities are held by registered banks (92 percent), with the remainder held by non-bank financial institutions, and loans from life, super and managed funds. The value of student loans outstanding at the end of December 2008 was ten billion. According to the Reserve Bank, the outstanding total debt of households has increased more than six times in nominal dollar terms since 1990.

Looking at household financial assets and total assets, it becomes apparent the extent that household assets are tied up in housing. Approximately three-quarters of household asset wealth were in housing at the end of December 2008, with the value of housing assets totalling some $568 billion. This represented a reduction of $46 billion over the previous year (due to falling house prices). Since 1990, housing values have risen 347 percent from $127 billion as at 31 December 1990.

Household financial assets are mainly held in bank and non-bank financial institution deposits. Just over half ($99 billion) of household financial assets were held in deposits at the end of December 2008. A further $28 billion were held in managed funds, and another $20 billion was held in superannuation funds.

New Zealanders do not tend to hold equity investments directly. As at 31 December 2008, direct domestic and overseas equities accounted for only 8.2 percent of households' financial assets. However, the fall in equity prices during 2008 affected the proportion of financial assets held in equities directly. At the end of December 2007, directly held equities accounted for 12.6 percent of household financial assets.

As at December ($billions)	2005	2006	2007	2008
Household financial assets				
Deposits	73	82	90	99
Other fixed interest assets	14	16	19	23
Superannuation	21	23	23	20
Life insurance	9	9	9	8
Managed funds	27	33	33	28
Direct domestic equities	15	18	16	11
Direct overseas equities	6	8	9	5
Total household financial assets	165	188	199	194
Housing value	506	559	614	568
Total household assets	671	747	813	762
Household financial liabilities				
Loans from registered banks	121	136	154	163
Loans from non-bank lending institutions	12	14	15	12
Life, super and managed funds loans	1	1	1	1
Total household financial liabilities*	135	152	170	177
Student loans	8	9	10	10
Total liabilities	143	161	180	187
Household net wealth	528	586	633	575

Note: * - Excluding student loans

Source: Reserve Bank. *Household financial assets and liabilities, housing value and net wealth 1978 – 2008.*

Grant Cleland, Research Analyst - Economics
Economics and Industry Team
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