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New Zealand Economics Update

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NZ Economic Update

The economy continues to perform well.

- Growth is solid, employment is buoyant and investment is strong. Migration inflows remain elevated .
- Some sectors such as tourism continue to perform well despite the restraining influence of the high NZD.
- Financial conditions, our Truckometer and Confidence Composite all point to a continuation of solid growth over the year ahead. Momentum is slower than seen in 2014, but still robust.
- The economic story is being supported by strong productivity growth and a sound microeconomic agenda. The latter adds to an economies resilience.

Some key leading indicators are starting to show signs of softening, and are receding from highs

- Part of this softening reflects normal business cycle dynamics; an economy performs stronger in the early stages of a recovery as it bounces off lows. As an economic expansion matures and the level of activity pushes up, capacity constraints start to bite and growth moderates towards trend. We can see aspects of this dynamic across New Zealand with small to medium sized businesses reporting that finding skilled staff is their biggest constraint.

The risk profile for the economy has shifted more to the downside of late

- The most obvious risk comes from a failure of dairy prices to recover. The bottom for global dairy prices does feel near. But the timing and extent of recovery remains highly uncertain.
- The incremental impetus to growth from the Christchurch rebuild is fading however there is no post rebuild hole pending. As rebuild stimulus fades, fiscal policy moves to a less restrictive stance.
- House prices in Auckland are extended relative to rents but supported by a) a supply shortage and b) major city trends. Policymakers are being more proactive trying to slow housing demand.

Inflation is low

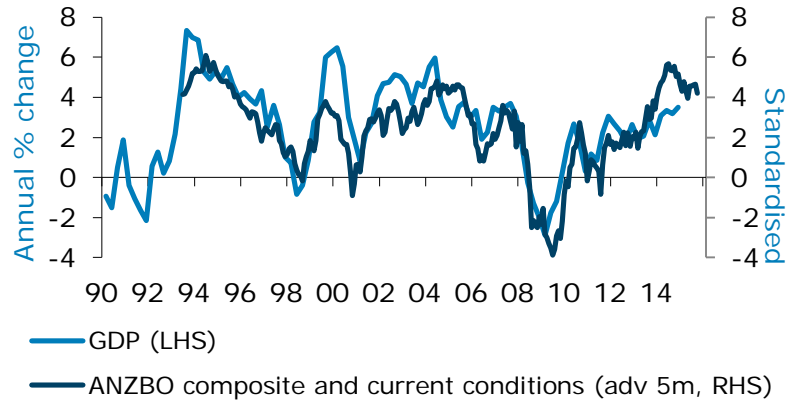
- Both headline and core inflation have been receding. Low inflation outcomes is more than petrol and NZD driven.

Scope for shock-absorbers to move

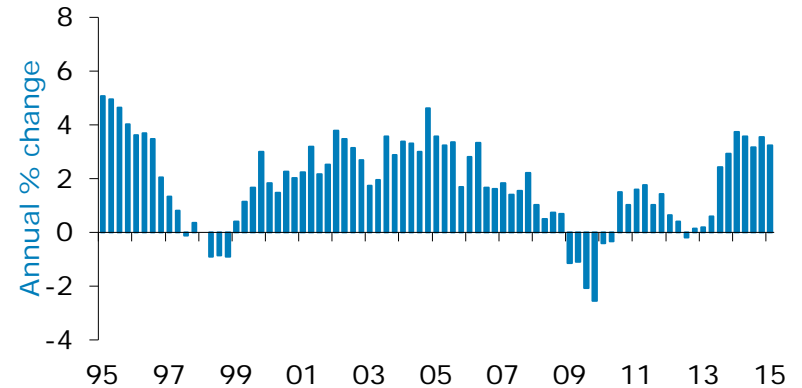
- We expect the RBNZ to cut the Official Cash Rate twice over the coming months. We still expect solid growth over the year ahead but view cutting the OCR as a low delta option to manage emerging economic risks.
- The NZD has declined of late, but remains extended relative to valuation metrics. A lower NZD remains the obvious release valve to offset the negative impact of weakening commodity price trends, with forestry, wool and lamb prices receding of late, to join dairy.
- The Government is moving from deficit to surplus and net debt is low. The Government's broad policy platform was unchanged in the Budget though we note more active initiatives in the social arena aimed at improving outcomes, and these being centred around a mixture of hand-up (more jobs), hand-outs (more \$), carrots and stick initiatives.

Still a lot of positives across the economy

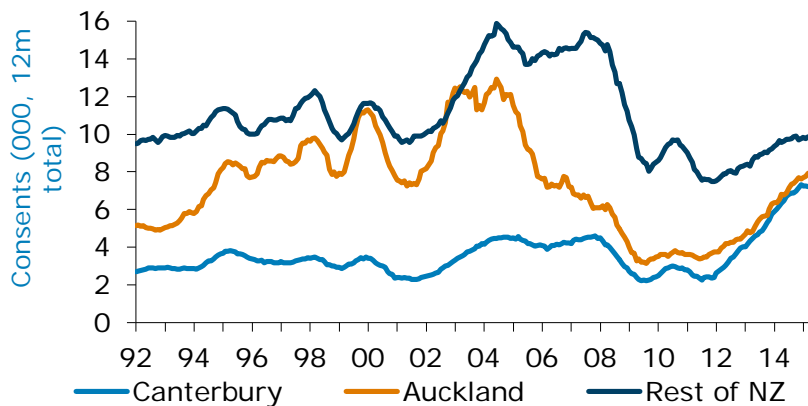
GDP vs Confidence Composite – still a strong feel-good factor



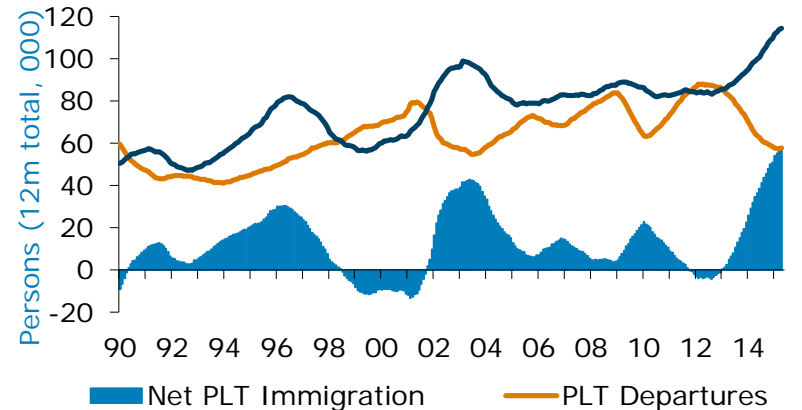
Employment growth is strong



Residential building consents up across the board – rebuild & housing shortages



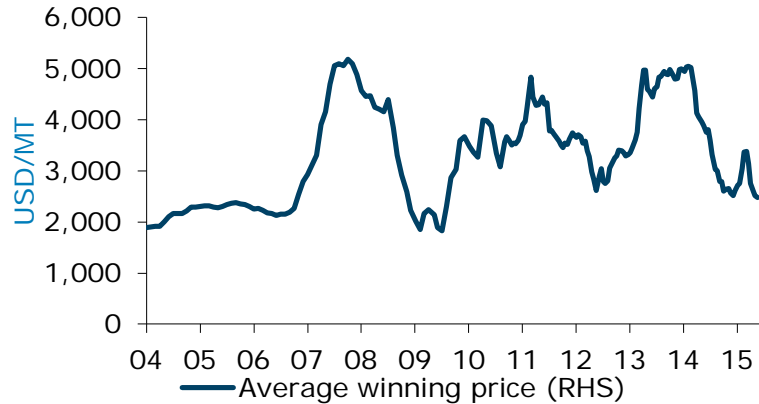
Strong net migration adding to housing demand but also the labour pool



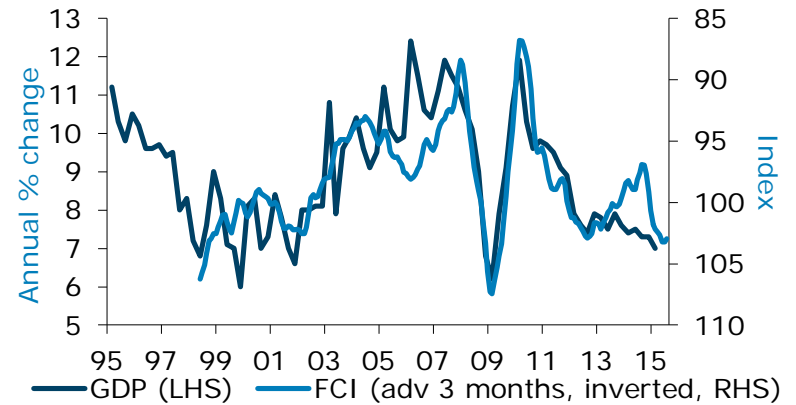
Sources: ANZ, Statistics NZ, Westpac McDermott Miller

Risks to manage and be mindful of

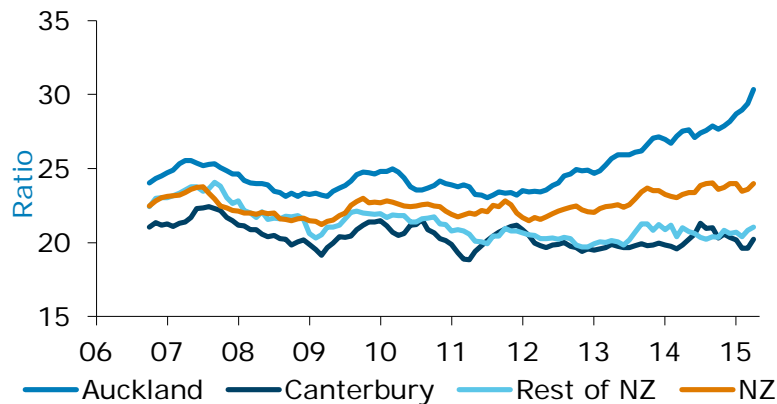
Dairy prices have tumbled



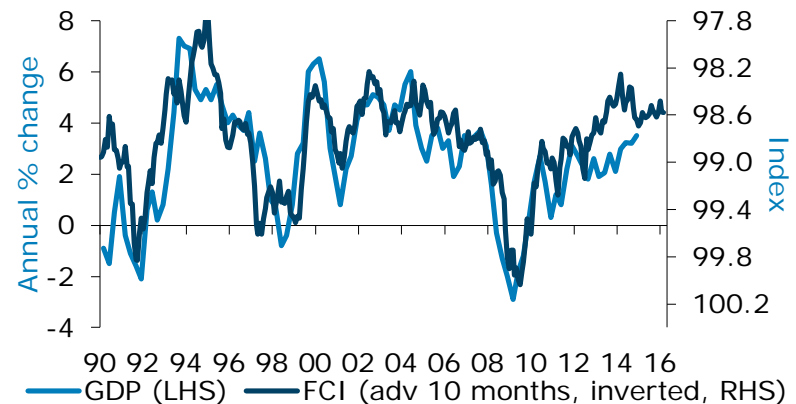
Financial conditions in China have tightened of late driven by falling property prices



Median sales price to median annual rental payments



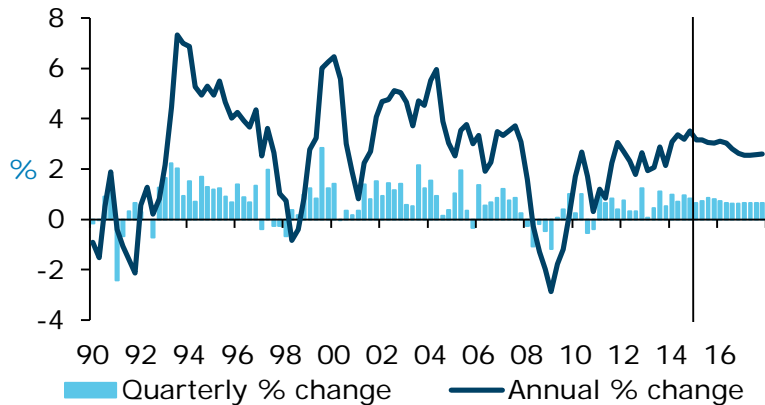
Financial conditions remain supportive despite the NZD being high



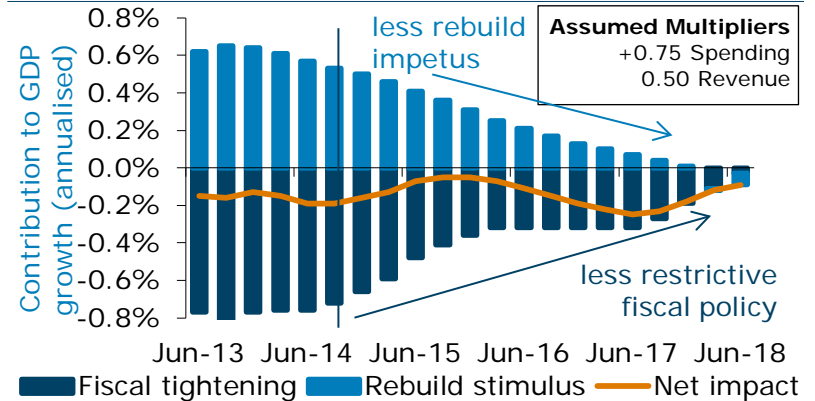
Sources: ANZ, Statistics NZ, GlobalDairyTrade, REINZ, Bloomberg

Key thematics: solid growth, building boom but restrained consumer & inflation to rise gradually

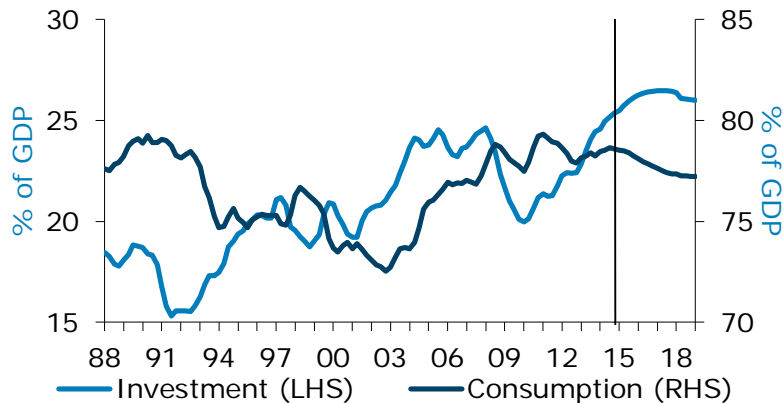
Still solid growth for New Zealand



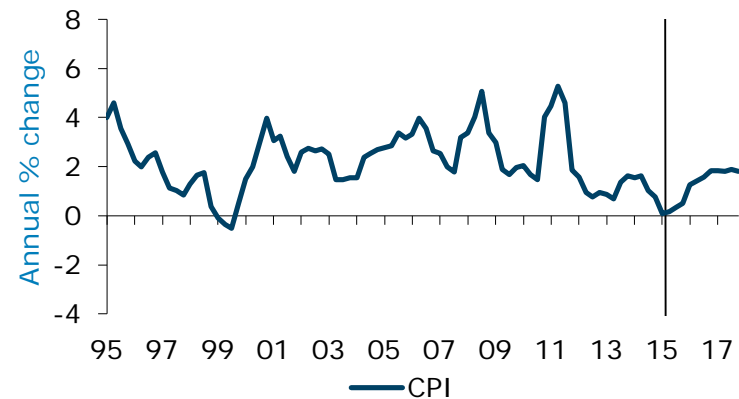
Canterbury vs Fiscal Stance: No "hole" looming



Consumption needs to give way for a construction boom



Inflation to rise gradually



Sources: ANZ, Bloomberg, Statistics NZ, RBNZ

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