Economic Review

New Zealand

11 June 2008

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Overseas Trade Indexes – March 2008 quarter

Key points

> The terms of trade continued its impressive rise over the March quarter.

> However, volume data confirms net exports will be a drag on Q1 GDP growth.

> We remain comfortable with our -0.3 percent forecast for Q1 GDP, though see downside risks to this.

Assessment

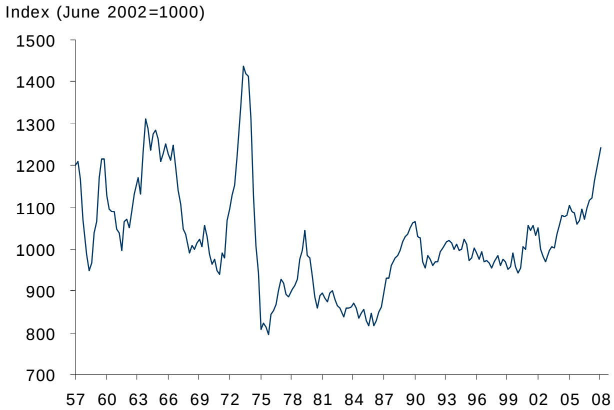
The merchandise terms of trade rose by 4.1 percent in Q1, stronger than market expectations. The level of the terms of trade is the highest since the March 1974 quarter and is 11.3 percent above its March 2007 level. This is, of course, a very good medium-term story for the economy. Dairy prices were once again the major contributor to the 4.5 percent rise in export prices, although non-food manufacturing prices also rose. Import prices only rose by 0.3 percent over the quarter, with lower mechanical machinery import prices (down 4.7 percent), which includes PCs and some electronic goods, the main offset to higher petroleum and petroleum product import prices (up 8.3 percent).

Looking forward though, it is likely that the terms of trade index is close to peaking, albeit still remaining high by historical standards. Although export commodity price strength looks to be broadening beyond dairy, dairy prices have fallen around 11 percent since their November 2007 high in world price terms. We are also mindful about the meteoric rise in oil prices – which NZ is still a net importer of. Based on the relationship between the ANZ Commodity Price Index and NZ's export price index (in world price terms), there are likely to be further increases in export prices over coming quarters. However, when looking at the economic impact of commodity price strength we must always take into account both sides of the equation, and the recent rise in oil prices (as well as other hard commodities that NZ imports) is likely to far outweigh the small increases we have seen in export commodity prices over the past few months.

In terms of the volume data, net exports look set to be a drag on Q1 GDP growth. Goods export volumes fell 3.5 percent – led by falls in dairy exports and petroleum and product exports, after both recorded record highs last quarter. The fall in the former is also likely to be a consequence of the drought-like conditions over much of the country this summer. It is reasonably pleasing, though, to see that non-food manufacturing exports maintained the growth recorded from last quarter, rising 0.2 percent. Import volumes fell 0.9 percent over the quarter, with capital good import volumes particularly weak (led by a 37 percent fall in transport imports). Although consumption good imports fell 1.6 percent in the quarter, the level is still the second highest on record. Given the slowdown seen in the retail sector over recent months, we expect further falls in consumption good imports going forward.

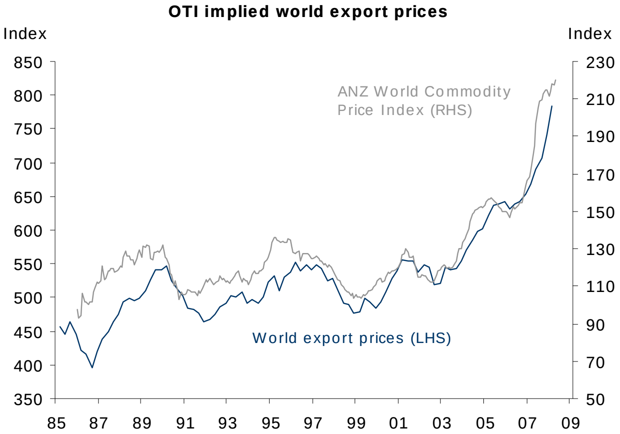
	Terms of Trade		Export Volumes		Import Volumes	
	QoQ	YoY	QoQ	YoY	QoQ	YoY
Mar 06	0.8	-3.3	-1.2	-0.4	0.3	3.8
Jun 06	2.6	0.5	0.1	0.4	-2.5	-2.2
Sep 06	-2.2	-1.3	6.4	8.1	2.2	-0.7
Dec 06	2.5	3.8	-5.1	-0.2	2.0	1.9
Mar 07	1.5	4.5	4.4	5.5	2.6	4.2
Jun 07	0.4	2.3	-0.4	5.0	2.9	10.0
Sep 07	3.7	8.4	0.5	-0.9	0.3	7.8
Dec 07	2.7	8.5	10.2	15.2	4.9	11.0
Mar-08	**4.1**	**11.3**	**-3.5**	**6.4**	**-0.9**	**7.2**
ANZ	***1.5***	***8.8***	-	-	-	-
Market	***0.9***	***8.1***	-	-	-	-

Terms of trade

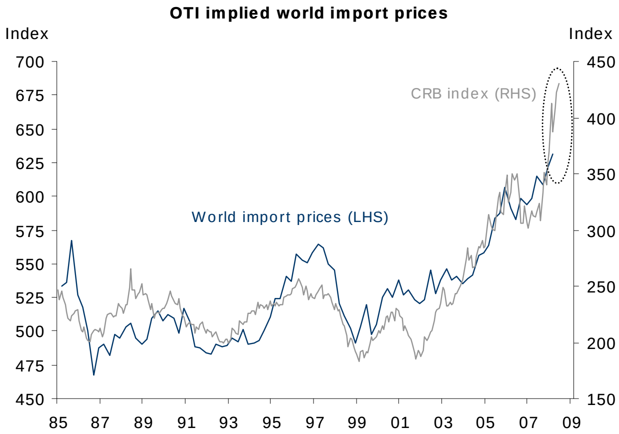


Sources: ANZ National, Statistics NZ

There are limited monetary policy implications from today's data. Although the terms of trade rose by stronger than the 2.2 percent increase the RBNZ was expecting in their June *MPS*, the Bank are likely to look through this increase, particularly given that oil prices are also currently above their projections. Following today's data, we continue to have a 0.3 percent fall pencilled in for Q1 GDP (released at the end of this month), but do see downside risk to this estimate. Manufacturing data released next Monday will enable us to firm up our expectation.



Sources: ANZ National, Statistics NZ



Sources: ANZ National, Statistics NZ

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