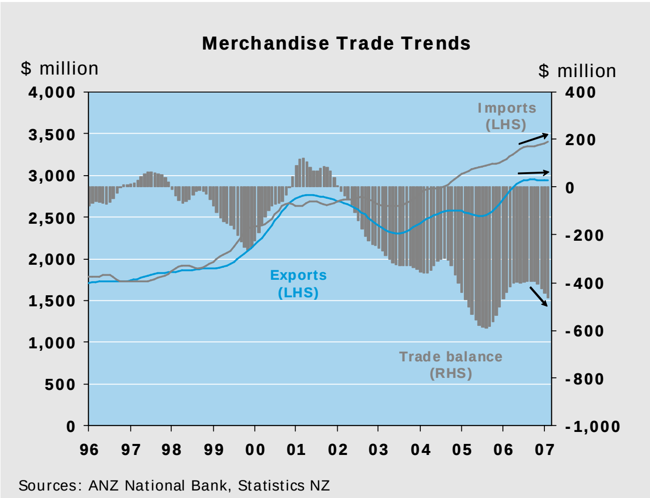
ANZ
Economic Review
NEW ZEALAND
DATE 26 March 2007

OVERSEAS MERCHANDISE TRADE – FEBRUARY 2007

Key points

- **New Zealand's February trade balance came in better than expected at -$127 million.**
- **The weakness in imports driven by volatile components, which will reverse. Imports of consumption goods and cars remain elevated – an indication that domestic demand is yet to show signs of moderation.**
- **Exports came in line with expectations – driven higher by rising commodity prices but dampened somewhat by the level of the NZD.**
- **While high commodity prices are providing an offset to the high NZD for New Zealand's primary exports, ultimately a material improvement in the trade balance rests on a much lower NZD.**
- **There are limited monetary policy implications from today's data. The Reserve Bank will take some comfort from the fact that consumption imports are not accelerating away. But at current levels, it continues to point to ongoing demand from consumers.**

	Actual	ANZ-National	Market
Merchandise trade balance	**-$127m**	-$200m	-$297m
Imports	$2,973m	$3,100m	$3,210m
Exports	$2,846m	$2,900m	$2,900m



Assessment and implications

- **The headline trade balance came in at a better than expected deficit of $127 million (ANZ $200 million deficit, market $297 million deficit).** Exports, at $2,846 million, were in line with both our and the market's expectations, while imports were weaker than expected at $2,973 million.

- **Higher commodity prices, particularly for dairy, resulted in the largest rise in exports for a February month since 2001.** The high world prices for New Zealand's main export commodities have played an import role in offsetting the high currency, managing to record higher export receipts. But high commodity prices give manufacturing exporters no such relief, as they continue to struggle under the high NZD. Total manufacturing exports are down 3.5 percent compared to a year ago. On a trend basis, exports have been virtually flat since September 2006, with any benefit from high commodity prices completely offset by the impact of the NZD.

- **Imports were weaker than expected, driven by the volatile transport equipment and oil import components.** The timing of when oil shipments arrive into the country can throw the import numbers (and hence trade balance) around. We note that crude oil imports in February, at $125 million, is less than half of the average monthly import value over the past year ($267 million). Given the rise in world oil prices over recent weeks, a rebound in crude oil imports in March can be expected. On a trend basis, the monthly total value of imports has risen for the fourth consecutive month, resulting in a widening trend trade deficit.

- **Consumer related imports remain elevated.** Though well below the $1 billion mark achieved over October and November last year, consumption goods imports at $790 million is still 13.6 percent higher compared to a year ago, and remains at elevated levels. Car imports are similarly up 7.7 percent from a year ago. Given where the currency is and the generally downward movement in prices for consumer goods, this implies reasonably strong consumer import volumes.

- **The Reserve Bank will read the consumption imports as a sign that domestic demand remains resilient.** We doubt the consumer import numbers are a sign of further inventory rebuilding following a Q3 rundown. Most of the rebuild would have occurred in Q4 (we will get confirmation of this in the Q4 GDP numbers this Friday). Further confirmation of the extent of consumer demand will come with the release of the Westpac McDermott Miller consumer confidence survey this Wednesday. A rise in confidence will signal that consumer demand is unlikely to moderate in the near-term – and will likely lead to further consumption related imports over the coming months.

- **Improvement in trade deficit to be a slow grind.** While we note that the annual trade deficit at $5,779 million is the lowest since September 2005 and an improvement from the peak of $7,321 million in February 2006, further improvement will be slow and gradual. The trend trade balance is widening and the higher NZD will continue to weigh on export returns. Any substantial improvement in the trade deficit will need to come from either further gains in commodity prices (without any accompanying appreciation in the NZD), or the currency moving and staying lower for a period of time. With the market attuned to prospects of further interest rate hikes from the Reserve Bank, the latter look unlikely at this stage.

- **There are limited monetary policy implications in today's release.** The import components point to continued resilience in domestic demand, while the export components show that a rebalancing in growth towards the external sector is some way off. The upcoming dataflow culminating in Q4 GDP and the March National Bank *Business Outlook* this Friday will set the tone for the rates market and the currency in the lead-up to the April OCR *Review*.

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