



NEW ZEALAND ECONOMIC UPDATE

September 2005

Introduction

This New Zealand Economic Update is produced monthly and presents current information on recent national business events, along with an update of key economic indicators.

Quarterly GDP Stronger Than Expected

According to Statistics New Zealand, the June quarter Domestic Gross Product [GDP] grew by 1.1%. This result was better than the 0.7% growth expected by the market and followed increases of 0.7% and 0.2% recorded in the March 2005 and December 2004 quarters respectively. Annual GDP growth was 3.1% for the year ended June 2005 (which was lower than market expectations of 3.3%).

Eight of out 11 industries showed upward movements over the quarter, while the remaining three sectors moved downwards. Domestic focused sectors remained a driving force behind the economy. Wholesale trade activity lifted by 2.5% quarterly, which in turn, contributed 0.2 percentage points (pp) growth to the 1.1% GDP increase. Finance, insurance and business services were up 0.9% compared to three months ago. This sector added another 0.2 pp growth to the June quarter GDP movement.

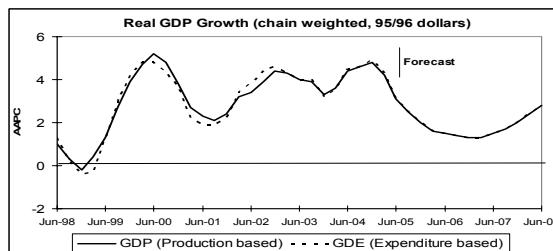
The retail, accommodation and restaurants group rose by 1.5%, while the transport and communication services increased by 0.6% over the June quarter. The service sectors made a 0.5 pp contribution to the GDP growth.

The goods-producing sectors showed a modest growth of 0.6% over the past three months. The positive movements, due to the energy group (2.2%↑) and the construction industry (2.3%↑), were partly offset by a fall in manufacturing activity (0.3%↓).

The primary industries were mainly flat (only a rise of 0.5%) over the June quarter. This was a mixed result as increased activity in agriculture (1.0%↑, largely due to the 1.7% growth of dairy production), was met by falls in forestry (3.9%↓) and fishing groups (0.6%↓).

Expenditure based GDP grew by 1.3% between the March and June quarters of 2005. However, 1.1 pp of the growth came from a build-up in stocks. While business investment in fixed assets remained robust (6.1%↑), household spending grew only 0.7% (the lowest over the past three years). In addition, the strong dollar was hostile to exporters with the volume of net exports down by 2.8%.

In summary, the June quarter GDP result confirms that the New Zealand economy remains on a positive track. However, unbalanced aggregate supply and demand will slow down the economy over the next six months.



Source: NZIER and Statistics NZ

Terms of Trade Fell Slightly

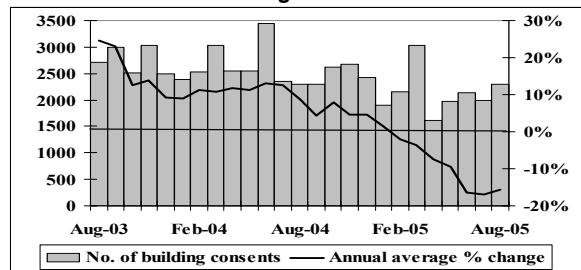
New Zealand's Terms of Trade [ToT], expressed as the ratio of export prices over import prices, fell 1.0% over the June quarter. Since the ToT measures relative price of exports compared to imports, it represents what a country gets in return for what it gives up. Therefore, an increase in the ToT suggests an improvement in the country's welfare.

The ToT deteriorated slightly over the June quarter. Export prices actually rose by 0.5% in spite of the strengthening in the TWI (1.8%↑). The price surge in petroleum products (up 24% from the March quarter) was almost totally offset by increases in export prices. If the fuel imports were excluded from the import category, the ToT would have risen.

The decline in the ToT will not shift the RBNZ's outlook on inflation in the short term, since it has considered the effects of high oil prices in its June report.

Key Indicator Trends

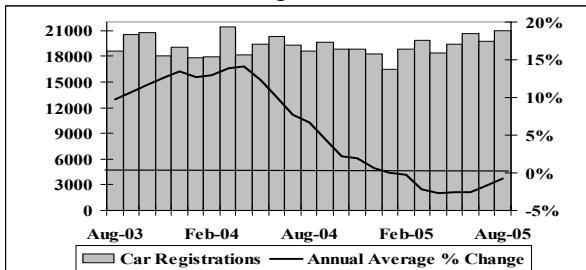
Building Consents



Source: Dept of Statistics Building Surveys and Vitals Section

A partial recovery occurred in the New Zealand dwelling construction sector in August 2005. A total of 2,301 permits were issued for new dwellings in August. This was the highest level over the last five months, and was marginally above the 2,296 issued 12 months ago. The annual average growth rate in the number of new permits issued was -15.8% for the year to August 2005.

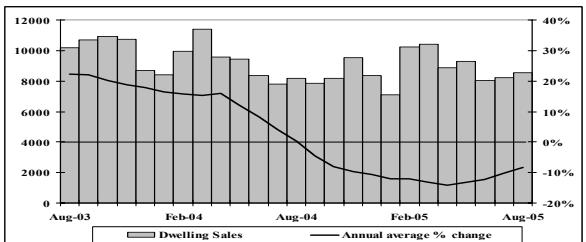
Car Registrations



Source: Land Transport Safety Authority

New car registrations maintained a high level in August 2005. A total of 20,933 cars (including both new and ex-overseas types) were registered during the month. This was the highest number recorded over the last 17 months. It was also the second time over the last three months that new car registration numbers exceeded 20,000. The annual average growth rate in the number of new car registrations improved from -1.7% for the July 2005 year to -0.7% for the year to August 2005.

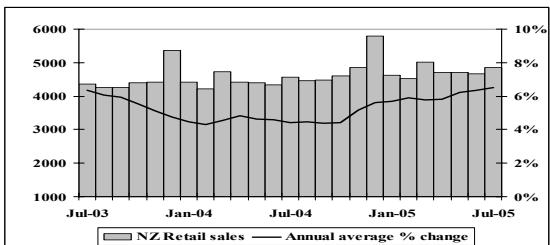
Residential Real Estate Sales



Source: Real Estate Institute of New Zealand

The national housing market has shown a steady improvement over the last few months. The monthly volume of sales totalled 8,537 during August, up from 8,213 recorded in July, 8,025 in June and 8,191 in August 2004. The median sale price also increased by \$10,000 on July's level to reach \$290,000 in August. The annual average growth rate growth in the volume of dwelling sales was -8.4% for the year to August 2005.

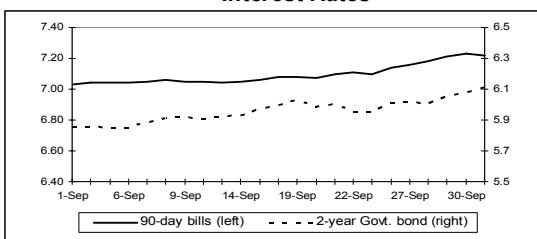
Retail Sales



Source: Business Statistics Section, Statistics New Zealand

Domestic retail demand remained buoyant in July. The value of retail sales was \$4,857.3 million. This was \$194.8 million more than the value recorded in June, and an increase of \$294.4 million (or 6.5%) compared to July 2004. The annual average growth rate in the value of retail sales was 6.5% for the year to July 2005.

Interest Rates

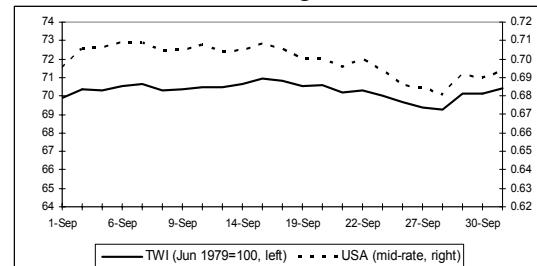


Source: Reserve Bank of New Zealand

Both the wholesale and the two year government bond yields increased in September. This result was commensurate with market expectations of high inflation as recorded in the National Bank's September Business

Confidence survey. By the end of the month, 90-day bill rates stood at 7.23%.

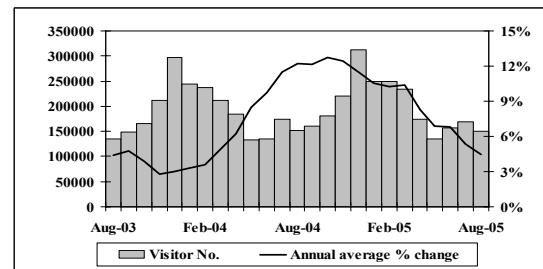
Exchange Rates



Source: Reserve Bank of New Zealand

The wider than expected August trade deficit, along with the concern about the June quarter current account deficit, dragged New Zealand's dollar down for the most of September. However, the possibility of another OCR hike pushed the Kiwi dollar back up by the end of September.

International Arrivals



Source: Statistics New Zealand

There were a total of 150,700 short-term international arrivals to New Zealand during August 2005. This figure was down from 168,422 recorded in July and from 152,104 (a drop of 0.9%) in August 2004. The annual average growth rate in the number of international arrivals to New Zealand decreased from 5.3% for the July 2005 year to 4.5% for the year to August 2005.

Summary

The June quarter GDP figure suggests that the New Zealand economy remains strong. However, the massive build-up in business stocks does raise a degree of concern.

According to the National Bank [NB], business confidence was low in September, with a net 37.5% of respondents expecting overall business conditions to deteriorate over the next 12 months. A net 32.1% of respondents took a similar negative view in the NB's August confidence survey. According to the NB's survey, firms were optimistic about their business future. A net 16% of firms expected to improve their business activity for the coming year.

The September quarter Westpac McDermott Miller 'Consumer Confidence' index stood at 120.2 (>100 means more optimists than pessimists). This result was the same as in the June quarter. The Westpac McDermott Miller 'present conditions' index decreased from the June quarter index value whereas the 'future Conditions' index increased in value. The September quarter results for these two consumer confidence indices show that consumers have become less optimistic about their current financial situations (probably due to continual surges in oil prices) but nevertheless feel optimistic about the future. These results are consistent with a buoyant labour market, the wealth effect associated with New Zealanders inclination towards the acquisition of real estate and the possibility of future tax cuts.

Overall Economic Outlook

Overall economic growth is slowing down and will continue to be cooled off by lower net migration, higher interest rates and the lagged effect of the high New Zealand exchange rate. Domestic demand is likely to be further moderated by a slowing down in the housing market and a fall in the terms of trade. Persistent and strong inflationary pressures remain buoyed by high oil prices and a tight labour market.

According to the Reserve Bank CPI, inflation is expected to peak in early 2006 at around 4.0%. The effects of intended government infrastructure investment, especially on roading and the possible implementation of

expansionary fiscal expenditure promised during the election, will put considerable pressure on the economy's productive capacity. Additionally, the government Family Support Package will be predominantly distributed to low income earners who generally possess a high propensity to consume and are therefore very stimulatory to the New Zealand economy. However, a recent period of strong investment by businesses in plant and machinery should result in an improvement in productivity. Global growth is expected to ease off over 2005 and 2006.

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