1 September 2017

Good-Looking Goods Trade

- **Q2 merchandise terms of trade lift 1.5% (10% y/y)**
- **Likely fattening nominal GDP growth to 8% y/y**
- **Export and import volumes strongly expansive**
- **Putting upside pressure on our +0.9% pick for Q2 GDP**

This morning's overseas trade indexes (OTI) added to the many signs of a solidly growing NZ economy. The merchandise terms of trade itself rose 1.5% in Q2. While this was a little under market expectations (+3.0%) it was not materially different to them, in broad perspective. The rise of 1.5% would have secured an all-time high, was it not for a downward revision to Q1. This was principally via a lesser gain reported in (forestry) export prices, such that they now show a lift of 6.9% in Q1 rather than 8.0% as first published.

Still, this is to split hairs. The terms of trade need only go up a sliver from Q2's level to surpass the absolute high-water mark achieved back in 1973. And we expect more than a sliver of increase is in store for Q3.

Even as they are, compared to a year ago New Zealand's merchandise terms of trade have lifted 10%. This is fundamental to the 8% annual growth we expect for nominal expenditure GDP growth in Q2, compared to "just" 2.6% on real (production-based) GDP. Imagine if the central bank had a, talked-about, nominal GDP target (rather than one centred on just the CPI)?

Consideration of TOT-fuelled nominal GDP growth is also important for thinking, more generally, about (per capita) income, the ability to save (and strengthen balance sheets), equity valuations and tax revenue to boot.

Merch. Overseas Trade Indexes - Q2

Q/Q % change	**Actual**	Mkt Pick	Previous
Terms of trade	**+1.5**	+3.0*	**+3.9R**
- annual % change	***+10.2***		***+6.4R***
Export prices	**+2.4**		**+6.9R**
Import prices	**+0.9**		**+2.9R**
Export volume - s.adj	**+6.8**		**-2.3**
Import volume - s.adj	**+2.3**		**+1.2**

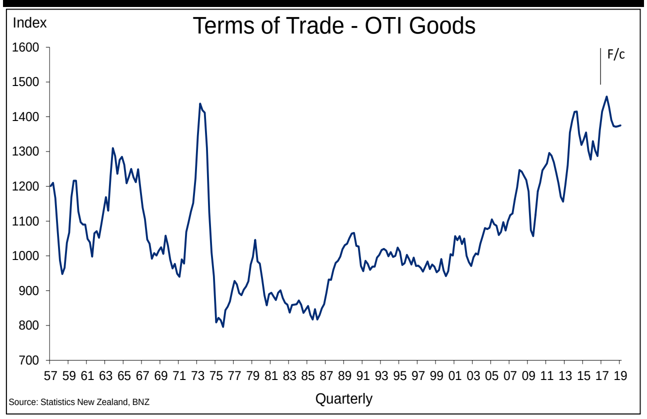
* Bloomberg

But even confining attention to last quarter's real GDP performance, this morning's OTI data also said good things. Trade volume growth was very strong in the June quarter. Real merchandise exports, in particular, rebounded a whopping 6.8%, seasonally adjusted. Just bear in mind this followed contractions over previous quarters, so was mostly a righting in nature. And that the pickup is being driven by primary goods, whereas non-food manufacturing export volumes were still struggling in Q2.

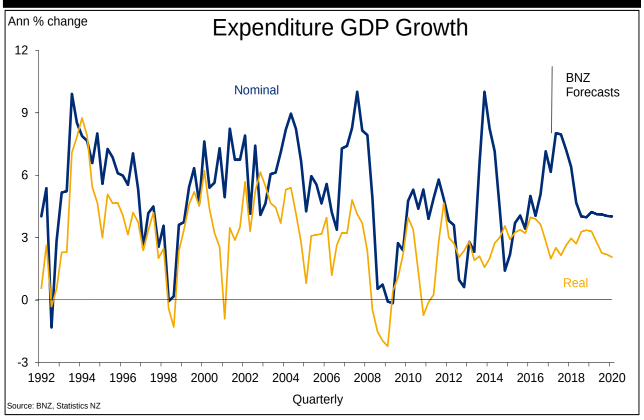
Merchandise import volumes expanded a seasonally adjusted 2.3% in the June quarter, which, at face value, suggests decent expansion in domestic demand too. The detail was also encouraging, in that capital goods import volumes (excluding transport items) increased a further 3.5% in Q2 to be 14% higher than they were a year ago.

These latest merchandise trade data thus support our view that Q2 GDP growth will be hefty in real terms. We currently expect +0.9%, but with upside risks starting to circle. But before formally lifting our estimate we need to see next week's trio of GDP partials.

Massive



Mind the Gap



These begin with Tuesday's Building Work Put in Place report for the June quarter. We expect a decent bounce-back in real terms, after a 3.5% fall in the March quarter that we judged as mainly technical/timing rather than the start of any rot. For next Thursday's June quarter Wholesale Trade we are looking for its nominal sales to increase in the region of 2% (seasonally adjusted). This would infer a 1.0% expansion in volume, which is what we are working with for the wholesale component of GDP. And we anticipate Friday's manufacturing sales and inventory data to infer a 1.5% expansion in the industry's production for Q2. Food processing should support this.

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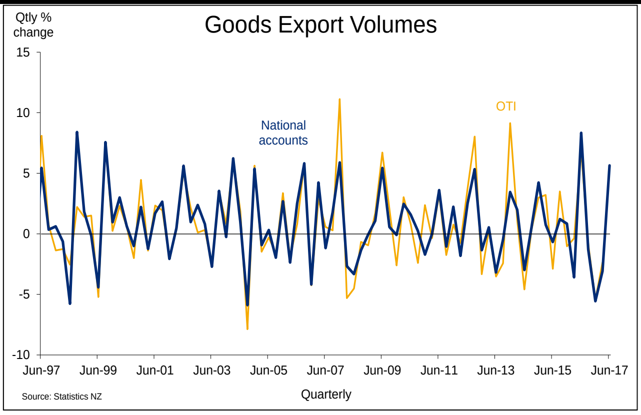
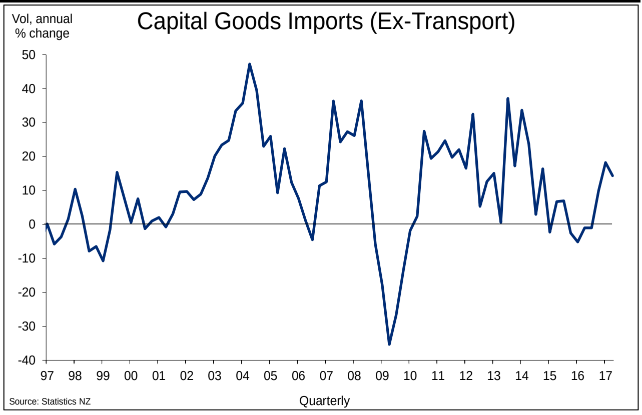
Ups-a-daisy



Encouraging



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