

Monthly Economic Review

For March 2015

Economic developments in the global arena were supportive of domestic economic growth and low inflation over the month of March. Unemployment rates in the U.S. and New Zealand remained constant while Australia slightly improved to 6.1%. Improvements in the New Zealand economy saw the New Zealand dollar strengthening against the Australian dollar. Global oil prices declined over the month once again, as oil producers competed for market share due to high supply levels.

Domestic economic activities were mixed during the month of March but remained broadly positive. Primary activities as indicated by banking data, generally declined over the month. Fisheries proceeds increased by 5.5%, whilst agricultural proceeds declined by \$0.2 million. Agricultural exports volume declined by 15.8% due to a decline in root crops exports. Constrastingly, imports continued to increase supporting growth in the distributive sector. Container registrations rose by 38.2% while non-oil import payments made through the banking system increased by 13.0%. The tourism sector was kept afloat by a 9.7% increase in international air arrivals despite the decline in cruiseship arrivals. Banking system data shows travel receipts increased by 7.5% over the month. The transportation sector continues to benefit from the low global oil prices with a 48.8% increase in new vehicle registrations over the month.

The falling global oil prices also contributed to the continued deflation on both monthly and annual terms. The

Consumer Price Index (CPI) fell over March by 1.8% and annual headline inflation was the lowest on record at -4.0%. Over the month, imported and domestic prices fell, particularly power and fuel consumed within the households. Food prices also declined by 2.7% over March. Although domestic food prices increased and the Tongan Pa'anga depreciated slightly against the New Zealand dollar, the falling New Zealand food prices more than offset this change. Therefore food items such as imported fish, meat, poultry and tinned foods fell by more than the rise in domestic food prices. However, in annual terms, prices for imported food rose along with imported tobacco, alcohol, clothing and footwear. The lowest annual deflation rate on record, therefore, was caused by the drop in domestic fuel, energy and transportation prices; once again, due to the falling global oil prices.

Both the Nominal Effective Exchange Rate (NEER) index, measuring of the value of the Pa'anga against the currencies of our trading partners, and the Real Effective Exchange Rate (REER) index, measuring the competitiveness of the Pa'anga against the basket of currencies of our major trading partners, fell over the month by 0.4% and 2.3% respectively. In year ended terms both the NEER and REER fell by 0.3% and 6.1% respectively.

The balance of Overseas Exchange Transactions over the month of March was a deficit of \$11.2 million, almost twice as wide as the deficit over February. The wider deficit stemmed from higher net outflows in the Current Account more than

offsetting the rise in net inflows in the Capital account. Contributing to the higher net outflows in the Current account were import payments rising by 2.6%, mainly for wholesale and retail goods. Export receipts fell by 10.1% due to a decline in agricultural exports. Travel receipts, rose over the month by 7.5% supported by a pickup in international air arrivals data. Remittances also rose, by 8.8% mainly from New Zealand and Australian sources. Foreign reserves declined to \$270.2 million at the end of March, 4.0% lower than the foreign reserves in February yet still sufficient to cover 7.9 months of imports, well above the NRBT's minimum range.

Broad Money fell slightly over March due to a decline in net foreign assets more than offsetting an increase in net domestic assets. Total domestic demand deposits and currency in circulation also fell in line with the decline in broad money. Banking system liquidity also fell by 6.4% over the month and 0.3% over the year.

Bank lending increased over March by 1.3% due mainly to a 2.1% increase in business loans. Additionally, about 20 new loans were approved from the managed funds during the month. Total lending, including loans extended by non-banks, recorded a slight growth of 0.6%. Over the year, total bank lending increased by 9.7% driven by a 10.5% and a 9.3% increase in household and business lending respectively. Including loans extended by non-banks, total lending rose by 6.5%, reflecting lower on-lent loans by the government.

Weighted average interest rate spread narrowed over the month from 6.51% to 6.33% due to a decline in weighted lending rates and a rise in the weighted deposit rates. Continued competition to retain

good customers resulted in banks offering low interest rate loans, which contributed to the lower weighted lending rates over the month whilst an increase in savings and term deposit rates drove the rise in weighted average deposit rates.

Net credit to government continued to increase by around 4% over March due to about 3% decline in government deposits.

The outlook for domestic economic activities remain broadly positive. Inflation is expected to remain low reflecting weak global commodity prices. The lower prices in turn support economic activities. Foreign reserves remain high and are anticipated to remain comfortably above the NRBT's minimum range of 3-4 months of imports. The banking system continued to remain relatively sound, with reported credit growth and strong liquidity position maintained. The existing monetary policy setting is therefore considered appropriate in the near term.

The NRBT will continue to promote prudent lending, closely monitor credit growth and be mindful of the impact of a continued deflation. The NRBT will continue to closely monitor the country's economic developments and financial conditions to maintain internal and external monetary stability, promote financial stability and a sound and efficient financial system to support macroeconomic stability and economic growth.

