

Severe quake likely to have modest economic impacts

- A severe earthquake struck North Canterbury overnight and was widely felt across NZ.
- Reports of moderate damage in major urban centres and damage to transport infrastructure.
- Short-term economic disruption likely to be offset by demand for replacement and repair.
- Increased construction requirements will be inflationary - OCR on hold remains our base case.
- However, any drop in economic confidence due to disruption may increase the odds of a rate cut next year.

Earthquake details

A **7.5 magnitude earthquake struck near Hanmer Springs** in North Canterbury overnight. Since then, there have been at **least 100 aftershocks since, many above 6.0**. So far, there have been two confirmed deaths and widespread damage around Canterbury and up into Wellington.

There appears to be **moderate to large damage to buildings and infrastructure across a number of areas** including Blenheim, Kaikoura and Wellington. The Wellington CBD will remain closed while the buildings can be checked; Wakefield St appears to be quite badly damaged. There also appears to be **damage to the Wellington Port**. Roads leading into Cheviot (north of Canterbury) are damaged and a number of sections of SH1 and SH7 are closed due to slips and visible damage. The rail link from Picton (ferry terminal) to Christchurch is blocked. However, a number of uncertainties remain and we are only just starting to get an update on the impacts of the quake.

The quake also set off widespread tsunami warnings for most of the east Coast of New Zealand. **Tsunami waves of about 2m have hit the Kaikoura region, but there have been no reports of any serious damage**. The tsunami warning has been subsequently downgraded this morning.

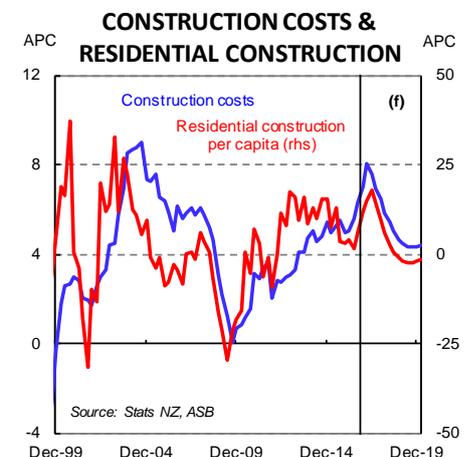
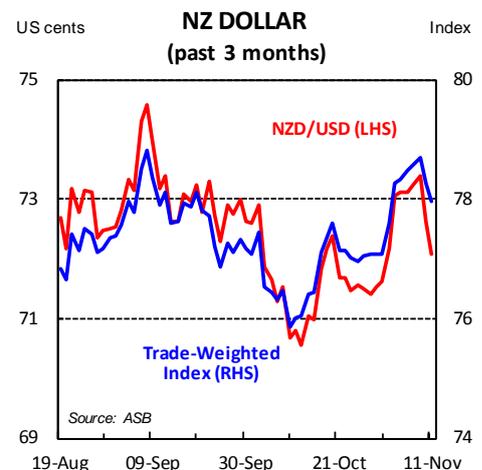
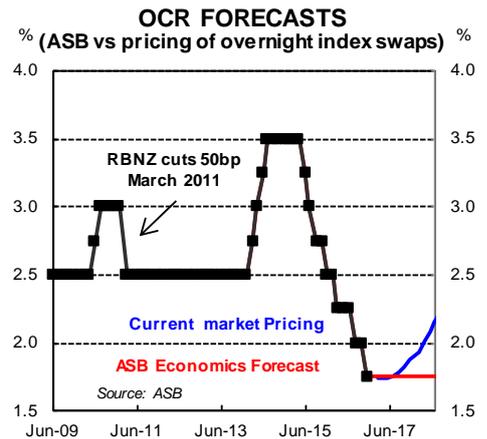
Market implications

The **NZD fell in response to the earthquakes**, but the extent of decline appears fairly limited. The timing of the earthquakes allowed for more information to be available before the markets reacted. This morning the NZD was 1.5-2% lower against most crosses and down just 0.5% against the AUD.

At the margin, this morning's earthquakes could increase the odds of another **rate cut next year** if economic disruption causes a fall in confidence. While the earthquake was severe, the location suggests a **limited economic impact**. Several provincial towns have been hit hard, but to date only moderate damage has been reported in NZ's major urban centres. However, it is too soon to say without further information on the extent of damage and disruption, particularly around infrastructure.

In comparison, **the 22nd February 2011 Canterbury earthquake caused catastrophic damage** to NZ's second biggest city and economic confidence was at risk. In response, the **RBNZ delivered a 50 basis point rate cut on 10th March 2011** (at its scheduled MPS review), returning the OCR to "emergency settings". This had followed two 25 basis point hikes in mid-2010. The OCR remained at 2.5% until March 2014.

The **RBNZ's next scheduled OCR review is now 3 months away** (February 9th 2017).



Economic impacts

Based off damaged reports, **South Island transport infrastructure and Wellington Central Business District** are the key areas that are vulnerable to short-term economic disruption.

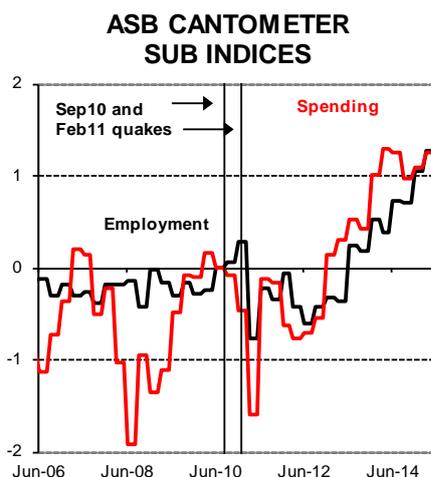
The **2013 Seddon earthquakes caused moderate damage** to a number of Wellington buildings. However, the **initial business disruption was offset by increased demand for repair and replacement of damaged goods**. With larger events, such as the 2011 Canterbury quake, the negative economic impact was a result of subsequent population outflows and the impacts on spending and broader economic demand in the region.

Construction

The resulting damage from the earthquakes will **boost construction demand over the coming year, at a time when construction capacity is already stretched**. We expect this will result in **even stronger construction inflation**. Earthquake repair demand will be broad-based across infrastructure, commercial buildings (in particular Wellington) and residential housing. As there may be limited capacity for further increase in construction activity, the **urgency of repair work may crowd out or defer activity which would have otherwise taken place**. In the short term, if there is a prolonged period of aftershocks, there may be a temporary fall in construction activity.

Tourism

There is some **risk that large earthquakes could deter or defer overseas visitor arrivals**. Tourism activity is likely to be diverted away from the mid-upper South Island as a result of the most recent quakes. Canterbury suffered a large decline in guest nights due to the destruction of accommodation capacity. Given damage appears to be more limited, any impacts on tourism should be comparatively short lived.



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