

Economic Note

Q1 Terms of Trade

1 June 2018

Favourable terms

- Q1 Terms of Trade fall, but remain near record highs.
- Indeed, the Q1 dip is likely to prove temporary.
- Meanwhile, we anticipate that the very high Terms of Trade will be one factor underpinning the NZ dollar over 2018.

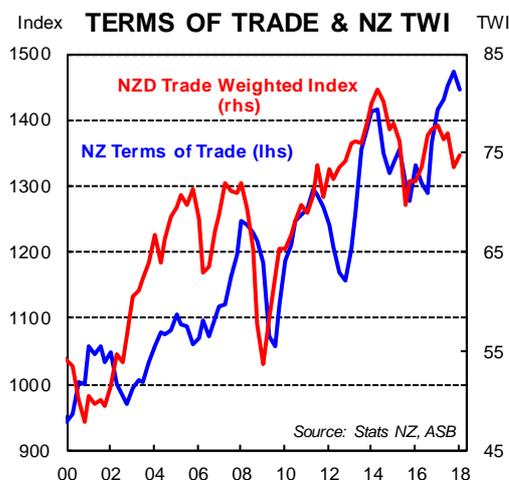
Summary

The NZ Terms of Trade remain very high. Over the March quarter, we did observe a 1.9% dip, but that was from record high levels (since the advent of quarterly data). Moreover, the quarterly dip is likely to prove temporary.

Dairy export prices have since rebounded after temporary weakness. Moreover, the suite of NZ export prices is very healthy. To name just a few kiwifruit, lamb and forestry prices are all faring well.

Meanwhile, the import side of the equation remains subdued. And outside of oil prices we see little potential for change over the remainder of the year. All up, **this points to the Terms of Trade remaining near record highs over 2018.**

Furthermore, **we anticipate that the very high Terms of Trade will be one factor underpinning the NZ dollar over 2018.** Indeed, we expect the NZD/USD to average 0.72 over the remainder of the year.



Details

Export prices dipped 2.2% over the quarter, led lower by dairy export prices as expected. That said, the 6.7% fall in dairy prices was not as large as we expected and explains most of the surprise relative to our forecast.

Meanwhile, import prices were largely flat as expected, with higher fuel import costs offset by low import prices elsewhere. Specifically, petrol and petroleum products prices lifted almost 8%, but electrical machinery and apparatus prices, for example, fell over 5%.

Looking ahead, **we expect the dip in the Terms of Trade will prove temporary.** Dairy prices have strengthened more

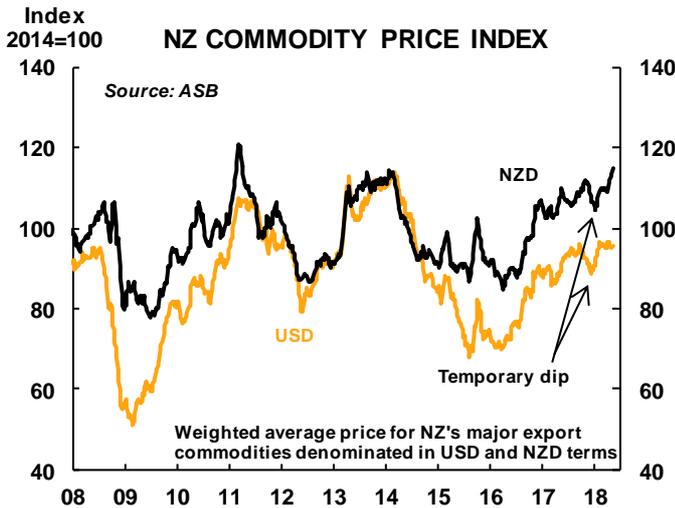
Key Results (quarterly % change)

Terms of Trade	-1.9
Export prices	-2.2
Import prices	-0.3
Export volumes (s.a.)	-2.9
Import volumes (s.a.)	0.9

recently and are thus likely to boost the Q2 Terms of Trade. Other export prices such as kiwifruit, lamb and forestry are also very strong. These gains are more than likely to offset any recent strength in oil prices.

Meanwhile, **export volumes were weak**, dipping by 2.9% on a seasonally-adjusted basis. Meat export volumes were particularly weak, slumping 10.7%. Dairy export volumes also continued their weak run, falling 0.8%, meaning volumes are now down around 5% in annual terms. Part of this weakness owes to poor growing conditions over recent quarters. We expect to therefore see export volumes lift in Q1 as weather improved through the autumn.

Import volumes remained strong, lifting 0.9% a seasonally-adjusted basis. Also this lift comes on top of the 8.5% surge last quarter. Putting lumpy transport equipment aside (i.e. Dreamliners) the import volume strength was broad-based and this strength has been sustained over the past year.



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