

The Bank of New Zealand - Business NZ Performance of Services Index is a monthly survey of the services sector providing an early indicator of activity levels. A PSI reading above 50 points indicates services activity is expanding; below 50 indicates it is contracting.

psi

Service sector expansion picks up in February

Bank of New Zealand - Business NZ PSI for February 2008

- The February Bank of New Zealand - Business NZ Performance of Service Index (PSI) picked up from its lowest result in January to sit at 55.6, up 3.7 points from the previous month. While this was the highest value since November, it was still below the average score of 57.3.
- All five diffusion indices that make up the PSI exhibited expansion and improved on the January results. *New orders/business* (61.4) leapt back over the 60-mark, while *stocks/inventories* (51.3) returned to show positive activity after the Christmas/holiday sales period. *Activity/sales* (56.2) also improved from its stationary position at the start of 2008 although, like the overall PSI result, still below its average figure of 59.0.
- Activity by region was up for all, with the *Otago/Southland* region (61.1) recovering strongly from two consecutive months of decline to lead the February results. This was closely followed by the *Canterbury/Westland* region (60.2). The *Northern* region (52.8) result for February was almost identical to January, while the *Central* region (55.6) showed moderate growth.
- Most service sub sectors showed consistent expansion for the second month of 2008, with seven falling within a fairly narrow band of activity. *Retail trade* (56.6) took the top spot for activity, followed by *health & community services* (55.7). The lowest result was for *accommodation, cafes & restaurants* (53.4), after leading the sectors in January.
- The improvement in activity for the sector led to a recovery in the proportion of positive comments received, rising from 43.5% in January to 52.8% in February. Compared with the same time last year, activity for those with positive (2.4*) and negative (3.3) comments for February remained the same as January. Therefore, the national result for activity compared with 2007 also remained at 2.8.

HIGHLIGHTS

- Activity level for the service sector stood at 55.6 in February, up 3.7 points from the January result.**
- New orders/business (61.4) was again the leading index, returning to a post-60 result.**
- All regions showed an increase in activity, with Otago/Southland rebounding from the low result in January.**
- The proportion of positive comments improved to 52.8%.**
- Next Bank of New Zealand - Business NZ PSI: April 14 2008**

SPONSOR STATEMENT

The Bank of New Zealand is delighted to be associated with the Performance of Services Index (PSI) and Business NZ. This association brings together the significant experience of leading business advocacy body Business NZ, and business finance specialist BNZ. We look forward to continuing our association with Business NZ and its associated regional organisations and to playing our part in the ongoing development of New Zealand's services sector.

Bank of New Zealand (www.bnz.co.nz)

PARTICIPANTS

Business NZ gratefully acknowledges the participation of the following associations in the PSI:

- Employers & Manufacturers Association (Northern)
- Employers & Manufacturers Association (Central)
- Canterbury Employers' Chamber of Commerce
- Otago Southland Employers Association
- Hospitality Association of New Zealand
- New Zealand Retailers Association
- Tourism Industry Association New Zealand

| National Indexes | Nov 2007 | Dec 2007 | Jan 2008 | Feb 2008 |
|------------------------|-------------|-------------|-------------|-------------|
| Business NZ PSI | 62.6 | 53.9 | 51.9 | 55.6 |
| Activity/Sales | 65.9 | 53.7 | 50.2 | 56.2 |
| Employment | 57.6 | 51.1 | 51.8 | 52.1 |
| New Orders/Business | 67.2 | 59.2 | 55.6 | 61.4 |
| Stocks/Inventories | 63.6 | 53.4 | 48.5 | 51.3 |
| Supplier Deliveries | 57.3 | 50.3 | 51.1 | 53.5 |

| Regional Indexes | Nov 2007 | Dec 2007 | Jan 2008 | Feb 2008 |
|------------------------|-------------|-------------|-------------|-------------|
| Business NZ PSI | 62.6 | 53.9 | 51.9 | 55.6 |
| Northern | 64.1 | 55.2 | 52.7 | 52.8 |
| Central | 61.9 | 52.4 | 51.8 | 55.6 |
| Cant/Westland | 59.6 | 56.3 | 55.6 | 60.2 |
| Otago/Southland | 62.0 | 44.7 | 40.9 | 61.1 |

* Respondents are asked for a score from 1-5, where 1= large rise and 5= large fall.

Service Sector Confidence Surprises

- Service sector relatively upbeat
- But activity indicators look sick
- Housing, construction, retail, hospitality and tourism sectors all vulnerable
- Advisers, Kiwi saver providers and those exposed to Government better placed
- Financing costs an issue

We are rather intrigued by this month's Performance of Services Index. We are increasingly of the view that the New Zealand economy is headed for a mild recession and that folk in the services sector will bear the brunt of such. Yet today's PSI would tend to suggest that either (a) we are wrong; (b) that the softening we are anticipating hasn't really hit home yet; or (c) businesses are in denial. No doubt there is probably a combination of these factors at work.

Nonetheless, we still contend that the services sector is in for a difficult 2008 and that while levels of activity may be sustained on average across the economy, bits of this sector will come under substantial duress.

Heading the list of the disgruntled is likely to be anyone involved either directly, or indirectly, with the residential property sector. House prices are now definitively in decline but, more importantly for sector participants, turnover is plummeting. In February house sales were down 35% on year earlier levels, on a seasonally adjusted basis, and that's despite this February having an extra day. The total fall from the peak in 2003 is 46%. That's a lot of real estate agents, mortgage writers and conveyancers who have a lot less work to do. And there

is no sign of an imminent change for the better. This is feeding through into residential construction which is also in retreat.

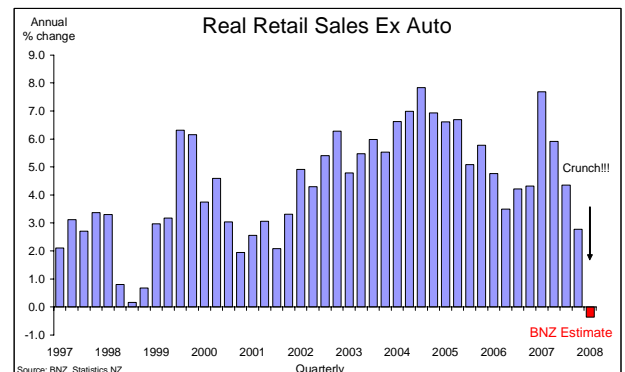
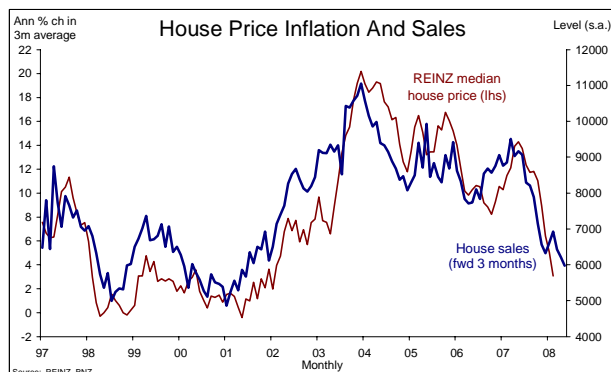
Softening in the housing market, generally, is already adversely impacting retail sales. By the end of the March quarter it is likely that ex-auto sales volumes will be below year earlier levels. This will be the first annual decline since the 1991 recession. With mortgage rates rising and heightened inflation in staple goods continuing, effective disposable incomes will stay under pressure keeping retail spending constrained.

For the hospitality industry this is also problematic and will be exacerbated by relatively weak tourism inflows as the combination of declining global growth and the ongoing strength in the NZD makes its impact.

During these difficult times all businesses will be either directly, or indirectly, impacted by the global credit crunch. For further detail on this we refer you to the note we published alongside last week's Performance of Manufacturing Index release.

For some, however, the economic downturn will bring opportunities and parts of the service sector will be insulated by ongoing growth in the civil service, the election campaign, the need for heightened advice in difficult times and the industry proliferation around KiwiSaver.

All in all, nonetheless, we reiterate that we are at the start of a bumpy ride and it's a ride that the service sector will not escape.



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