

26 January 2016

The PSI

December's Performance of Services Index (PSI), at 58.9, wasn't far off the 8-year high it posted in November (59.8). And, like we saw in the latest PMI, it was being led by new orders, with the PSI index on this heaving away at 64.3. This suggests the currently strong pace of production in the PSI (62.1) can be sustained into the early part of 2016. The jobs expansion denoted in the PSI remained solid rather than spectacular, with an index reading of 53.6. However, it's a further sign that the decline we saw in the Q3 HLFS employment measure was a statistical anomaly. When we look at the overall PSI, over long stretch, it becomes clear that it's been picking up the pace for a good number of years now.

QSBO Services

As we've done with the PMI, we've also referred to the PSI to support a relatively positive view on the economy. This, of course, was tested with the slow GDP outcomes over the first half of 2015, as well as the big swoon in business confidence we saw last winter. But through all of this the PSI and PMI held their poise. And over recent months they have each become more assured in their expansion. This was echoed in last week's Quarterly Survey of Business Opinion. Service sector respondents to this NZIER survey lifted their reports around recent output, while maintaining a relatively strong outlook for the coming three months. This was backed up in their reports and expectations around hiring.

GDP Services

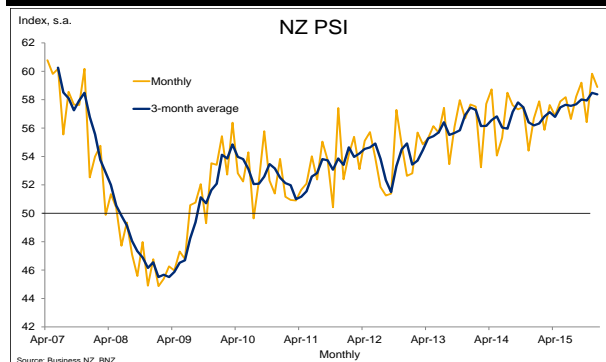
The importance of the service sector in maintaining economic growth was highlighted in the 2015 Q3 national accounts. Published 17 December (so after the previous PSI report, for November), these showed a 2.9% annual increase in real services output. This compared to overall production-GDP growth of 2.3%, y/y. This GDP definition of the services sector comprises two-thirds of total GDP, in volume terms. So if two-thirds of the economy can keep expanding at a solid clip – probably faster than average now, if one looks at the recent PSI performance – then there's a good chance overall GDP growth can post solid rates of growth without too much trouble.

Composite Strength

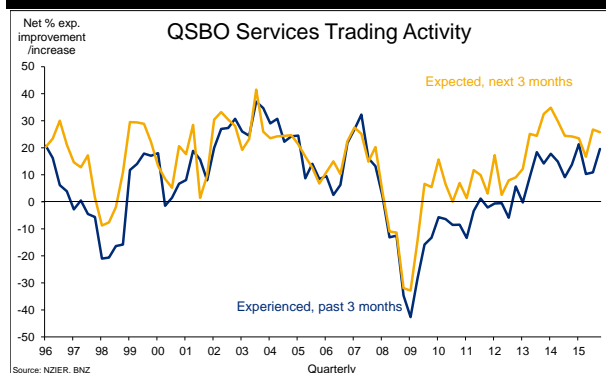
Today's PSI, combined with the 14-month high we saw in last week's PMI, is suggestive of GDP growth in the range of 3-4% on an annual basis. This is clearly faster than the rates of GDP growth we are projecting, even with the recent upgrades we've made. We now forecast real GDP growth of 2.4% for calendar 2016 (previously 1.9%) and 2.5% for 2017 (previously 2.0%). This mainly revolves around a bigger cycle in net immigration. However, we've also taken on board the sharp rebound in the domestic growth indicators over recent months. The latest PSI and PMI outcomes are very good examples.

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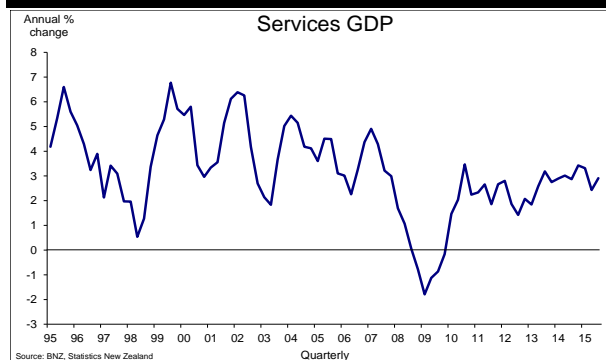
Services Still Going For It



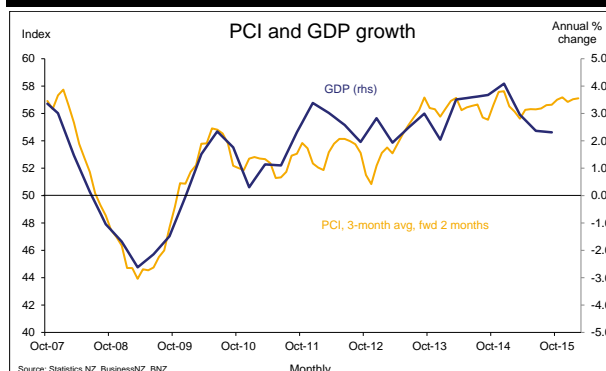
QSBO Service Firms Also Upbeat



Services A Backbone To GDP Growth



PSI/PMI Signal Upside To GDP Growth



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