

NZ GDP: Q4 2022 Review

16 March 2023



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Something for everyone

Bottom line

- Noise, pockets of softening demand, and biting capacity constraints: Q4 GDP data had something for everyone.
- The New Zealand economy contracted 0.6% q/q in Q4 on a seasonally adjusted basis, weaker than the 0.3% contraction we pencilled in, and much weaker than the RBNZ's February MPS forecast of +0.7% q/q. Q3's whopper quarterly pace was revised slightly lower from 2.0% q/q to 1.7%. That's not really surprising.
- The RBNZ know these data are not sending a clear signal regarding the degree of capacity stretch out there, because there's a mix of demand and supply effects going on. In the final three months of each year the New Zealand economy tends to expand sharply in unadjusted terms (ie before seasonal adjustment) as tourist arrivals pick up, more kiwis get out and about as the weather improves, Christmas holiday spending gives retail a bump, and longer sunshine hours make it easier to get outside work done. But in a labour market this tight, it's been hard to get the staff to meet this seasonal demand. That's dragged on growth, alongside moderating demand.
- Bottom line: the noise in these data is still deafening. We didn't take the full signal from Q3's whopper +1.7% q/q growth rate, and we're not taking the full signal from Q4's payback either. That's not to say economic momentum isn't slowing – it most certainly is – but rather, Q4 quarterly growth overstates the pace of the slowdown. Downside surprises on the activity data are unlikely to move the dial for the OCR until they are accompanied by clear evidence that the current extreme mismatch between labour supply and labour demand has turned a corner (and the noise ceases to reverberate).

Data summary

| | Latest | Prev |
|-------------------------|--------|------|
| Quarterly % change | -0.6% | 1.7% |
| Annual % change | 2.2% | 6.4% |
| Annual average % change | 2.4% | 2.7% |

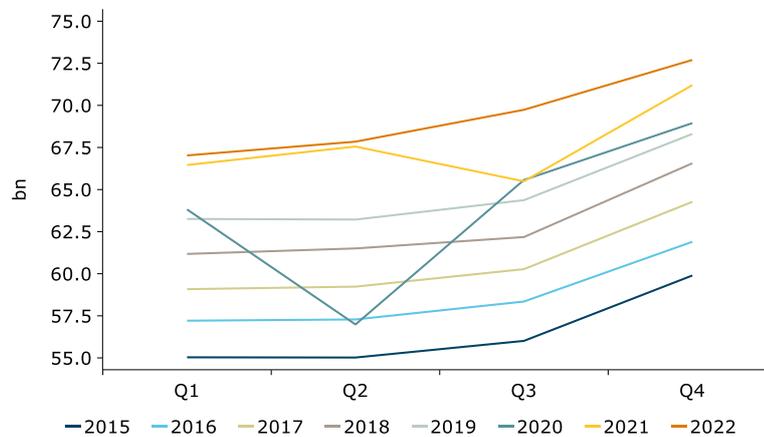
The big picture

The economy shrank 0.6% q/q on a seasonally adjusted basis in Q4. That's much weaker than consensus forecasts and the RBNZ's February MPS pick of +0.7% q/q. But those hoping this will be enough to convince the RBNZ that further OCR hikes are not required are likely to be disappointed. Even if GDP surprises on the downside again in Q1, to the point that the economy officially reaches "technical recession" status (which could happen, if flooding and cyclone disruption is large enough), that still doesn't change the fact that capacity constraints are extreme, and economic resource (particularly labour) is hard to get right now.

In fact, these very capacity constraints are partly responsible for economic activity not lifting as much as is typical for this time of year. It's easy to forget just how seasonal the New Zealand economy actually is, and that capacity constraints are always going to bite harder when economic demand typically peaks, which as figure 1 shows, tends to be in Q4. So while activity did in fact increase in Q4 in unadjusted terms, this was weak versus normal seasonal patterns. If capacity constraints are part of the reason, then that just explains why inflation has been so darn strong! It certainly doesn't give

the RBNZ a green light to go easier on the monetary tightening. That will require a clear signal that labour scarcity is no longer the biggest constraint facing firms, and wage growth and inflation expectations are convincingly on the way down.

Figure 1. Unadjusted GDP



Source: Stats NZ, Macrobond, ANZ Research

But demand is slowing (as demonstrated by weaker retail sales), and is expected to slow further as higher interest rates bite and the labour market transitions to more sustainable (less inflationary) levels. The looming economic transition won't be a happy one for many, but longer-term price and economic stability is at stake. High inflation needs to be tamed before it becomes a more permanent feature in generalised wage and price-setting behaviour. And inflation aside, yesterday's Q4 [balance of payments data](#) showed New Zealand needs to stop living so far beyond its means, or risk facing a sharp adjustment. Monetary tightening and fiscal consolidation both have roles to play.

The details

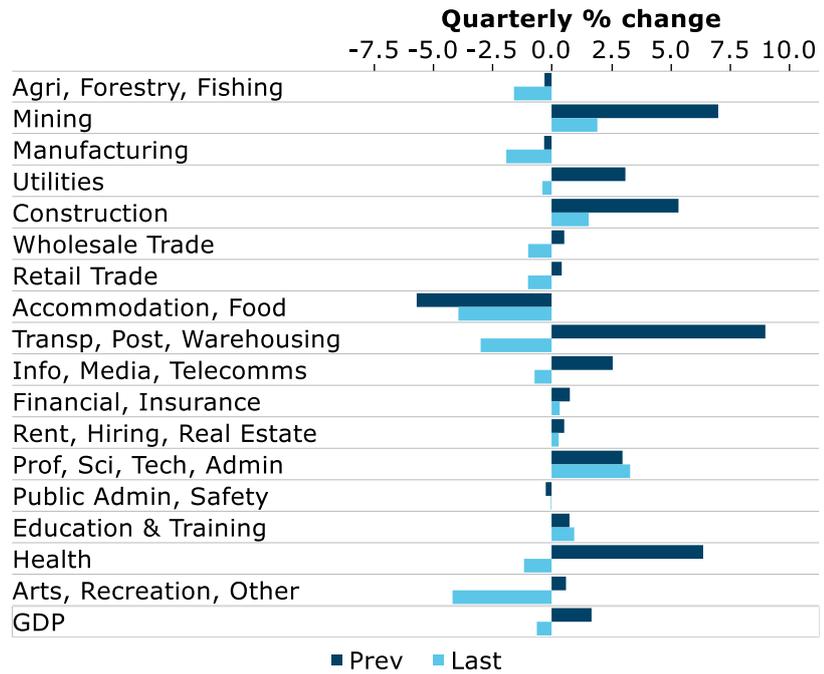
Turning to the details, there were once again some large quarterly moves in the GDP components – larger than some of our indicator models predicted.

Services industries (about two thirds of GDP) contracted 0.1% q/q, weaker than our expectation. More payback than expected in health (down 1.2% q/q following Q3's 6.4% rise) and weaker arts, recreation and other services (down 4.2% q/q) were the biggest miss vs our forecast. Retail trade and accommodation was also weaker than expected, down 1.9% q/q. Higher interest rates, falling house prices, and high inflation are clearly hurting the retail sector. Meanwhile, business services (around 10% of GDP) lifted strongly, up 3.3% q/q following Q3's 3.0% lift. That's solid.

Goods-producing industries came in stronger than expected, as building work put in place (which contracted in Q4), gave us a false steer on its GDP equivalent: construction GDP lifted 1.6% q/q in Q4. This happened a couple of quarters ago too, and we don't think it changes the story that private construction activity will soften as higher rates bite. Manufacturing fell 1.9% q/q, close to our expectation.

Growth in primary industries was weaker than expected, down 1.3% q/q, led by a 1.6% q/q drop in agricultural production. However, Q3 growth in this sector was revised higher to +0.3%, so it turns out that the string of consecutive declines across primary hasn't been as long as our prior understanding.

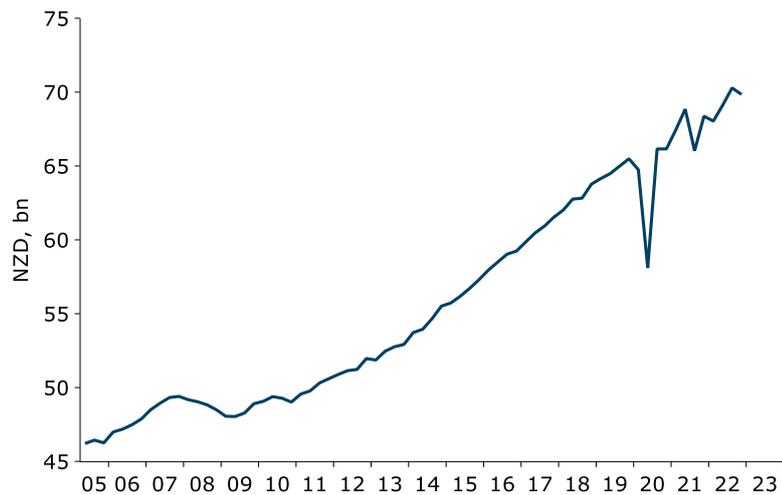
Figure 2. Quarterly change in GDP by industry



Source: Stats NZ, Macrobond, ANZ Research

In year-on-year terms, growth came in at 2.2%, with annual average growth at 2.4%. But these numbers are still being influenced either directly by lockdowns (in the case for the annual average measure), or potential pent-up demand dynamics following lockdown. In other words, annual growth measures still aren't giving us a good steer on economic momentum either. The level of GDP shows just how much volatility lockdowns have caused in the data compared to history (figure 3).

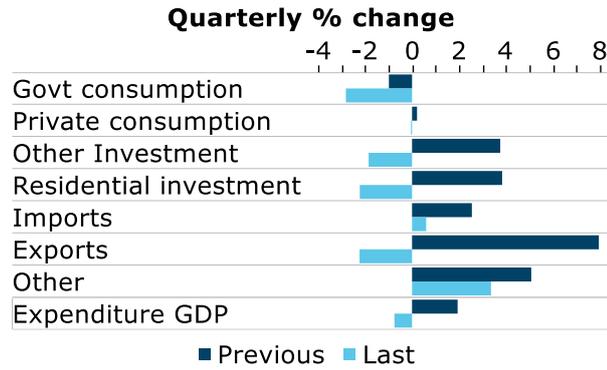
Figure 3. Production GDP



Source: Stats NZ, Macrobond, ANZ Research

In real (price-adjusted) expenditure terms, GDP contracted 0.8% q/q, with private consumption flat (0.0% q/q), government consumption down 2.4% q/q from a high level (hard to see this persisting given cyclone-related demand), residential investment down 2.2%, other investment 1.5% lower, exports down 2.2% q/q, and imports up 0.6% q/q. In other words, other than private consumption, all the expenditure components went backwards in Q4 from a 'contribution to growth' perspective.

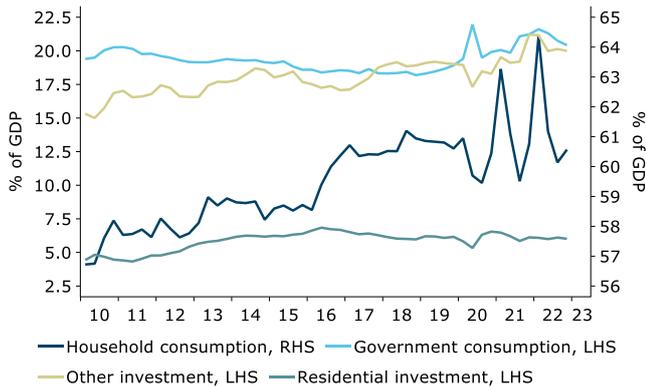
Figure 4. Expenditure GDP growth



Source: Stats NZ, Macrobond, ANZ Research

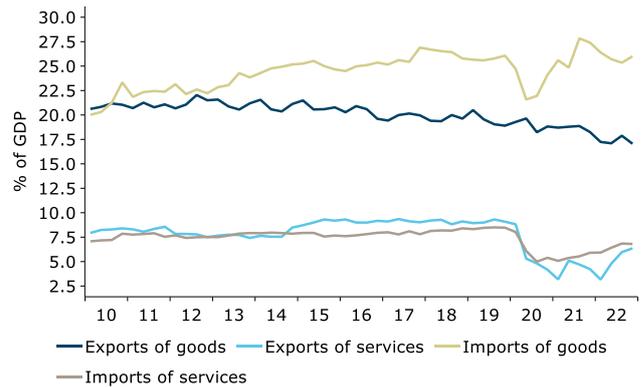
While the Q4 data did have its share of payback noise, the expenditure components as a share of GDP for both private consumption and services exports showed some tentative evidence that they are stabilising. If that persists, it means the days of wild surprises in the GDP data may be coming to an end. We'll still see surprises, just hopefully of a smaller magnitude.

Figure 5. Domestic components share of total



Source: Stats NZ, Macrobond, ANZ Research

Figure 6. External sector components share of total



Source: Stats NZ, Macrobond, ANZ Research

All in all, the data are still noisy, but looking through that, slowing demand in some sectors (particularly for those industries related to housing) is real, but capacity constraints in other industries persist and are also hampering growth (eg firms reducing opening hours because they can't get staff). Those looking for signs of capitulation and those looking for signs of resilience would all be able to find something in this data to suit their story. We'll publish our updated GDP and current account forecasts tomorrow.



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