ANZ Research

GDP – 2019Q3

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Data summary

	Latest	Prev
Quarterly % change	0.7%	0.1%
Annual % change	2.3%	2.1%
Annual average % change	2.7%	2.8%

Through the worst

Bottom line

- The New Zealand economy expanded 0.7% q/q in Q3, a touch stronger than both our and market expectations of 0.5%. However, Q2 growth was revised down markedly from 0.5% q/q to just 0.1%.
- The upward surprise came from solid primary industries growth, which tends to be volatile. Services industries growth was weak, up only 0.4% q/q.
- Annual growth ticked up to 2.3% from 2.1% as expected, given downward revisions to growth in the first two quarters of 2019. Revisions saw growth hold up a bit better over 2018, but the slowdown in growth momentum in 2019 has been sharper.
- With leading indicators looking a bit brighter, we think growth will continue to bob around 2% into early 2020.

Key points

The New Zealand economy grew 0.7% q/q in the three months to September 2019, a touch stronger than the 0.5% we had pencilled in. In terms of annual growth, the small positive surprise was offset by downward revisions to Q1 (from 0.6% to 0.4%) and Q2 growth (from 0.5% to 0.1%), which together with revisions to 2018 data saw annual growth in line with our expectation at 2.3% y/y in Q3. While revisions saw growth hold up a bit better over 2018, the slowdown in growth momentum in 2019 has been sharper (figure 1).

The RBNZ took the axe to their near-term growth forecasts in the November MPS forecast, and today's print was stronger than the 0.3% q/q they had pencilled in. It was also higher in annual growth terms (they had expected 2.1% y/y). The RBNZ will also take some comfort from the recent lift in forward-looking indicators, which suggests a stabilisation in growth heading into 2020. But it's still too early to know whether growth will be lifting sharply from there, as per the RBNZ's November MPS forecasts. With headwinds weighing in the form of still subdued business confidence and credit constraints, we think a strong lift is a big ask.

In the details of today's release, weakness in services growth was more than offset by unexpected strength in primary industries. Primary industries rose 1.1% q/q, against our expectation of a 0.2% decline. Agriculture and fishing lifted in the quarter, but a 2.1% dip in forestry and a 1.1% dip in mining provided some offset. The near-term outlook for forestry and logging is capped as China continues to work through still-elevated inventories.

An increase in services industries (+0.4% q/q) was a touch weaker than the 0.6% we had expected, following Q2's 0.8% q/q lift. The easing trend in annual services growth remains firmly in place, with it slipping from over 4% in 2016 to just 2.2% in Q3. There were a few misses in terms of the underlying components, but nothing to challenge the overall narrative. Retail trade was stronger than expected, but wholesale trade was weaker.

The household sector remains robust, with a tight labour market and the recent lift in the housing market set to put a floor under the slowdown in services industries from here.

Growth across the goods-producing industries of 0.5% q/q was largely in line with our expectations. Construction was a little weaker (0.6% q/q vs 1.0% expected), while manufacturing (0.6%) was a toucher stronger and electricity production contracted by less (-0.2%). Overall, 10 of the 16 production industries recorded higher levels of activity compared to Q2.

Expenditure GDP underperformed its production-based equivalent, rising 0.6% q/q. This was a little stronger than our forecast (0.5%), but this was largely due to a build-up in inventories. In terms of the detail:

- Private consumption growth was 0.8% q/q (1.1% expected), up slightly from Q2's 0.5% print. This suggests momentum in the household sector might not be as buoyant as assumed. That said, spending on durables, up 2.6% q/q, remains healthy.
- Residential investment activity remains at a high level, but contracted 0.6% in Q3. Business investment rose 0.4%, as a decline in plant, machinery, and equipment offset growth in construction. Given the numerous headwinds we're seeing in the construction sector, we don't foresee a lot of upside from here.
- General government consumption rose 1.3% q/q, a bit stronger than our expectation for a 0.9% rise.
- Net exports were a drag on quarterly growth, as expected. Exports declined by more than expected (-2.8% q/q), while imports rose a touch more than we had anticipated (+2.3%).

The nominal economy grew a solid 1.6% q/q – faster than we had expected and well above its real counterpart. At face value, this points to higher pricing pressures across the broader economy, including the recent lift in the terms of trade. However, there isn't a strong correlation between the GDP deflator and CPI inflation.

Per capita growth bounced, up 0.4% q/q in Q3, but this followed a per capita recession in the first half of 2019, with growth of -0.1% in Q1 and -0.3% in Q2. Annual growth in this measure ticked up from just 0.4% y/y in Q2 to 0.6%. Per capita measures are being influenced by the noisy migration data, but weak per capita growth confirms that labour productivity remains soft.

There were significant revisions to the growth profile in recent years, due to the national accounts annual benchmarking process, with production GDP growth revised higher over 2018 but falling more sharply to the same growth rate over 2019. The RBNZ often 'looks through' GDP revisions, as their estimate of potential growth will also be revised, limiting the impact on their inflation forecasts. The revisions help resolve some of the mystery of the tight labour market and robust inflation outturns despite slowing GDP growth. The sharper deceleration in growth momentum over 2019 may concern the RBNZ, but the recent stabilisation in leading indicators such as business sentiment, PMI surveys, and consumer confidence will provide a degree of comfort that a further deceleration is now looking less likely.

All up, despite the slightly stronger print than expected, today's data reflect an economy that slowed sharply in 2019 – indeed, more sharply than we had previously believed. But the good news is that forward-looking indicators suggest a stabilisation in growth going into 2020. In the meantime, growth continues to fall short of the roughly 2.6% y/y rate that the RBNZ needs to see exceeded for inflationary pressure to build. And looking forward, it remains a story of growth just not quite delivering what the RBNZ needs to be confident of hitting its inflation target, with inflation pressures set to wane in this environment and inflation expectations at risk of falling further. Given that, we think that a lower OCR is likely in time. We have pencilled in a 25bp cut in for May, taking the OCR to 0.75%.

Figure 1. Production-based GDP

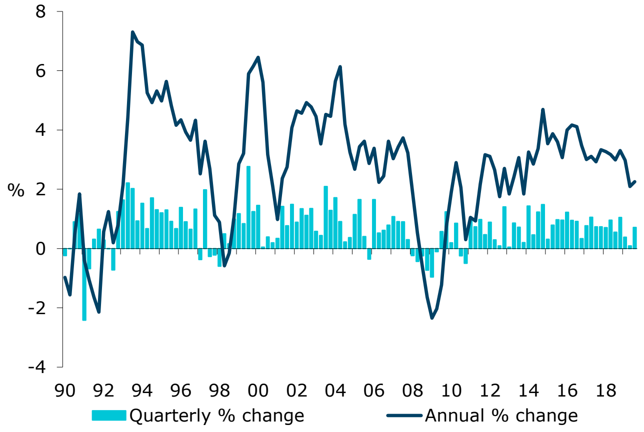
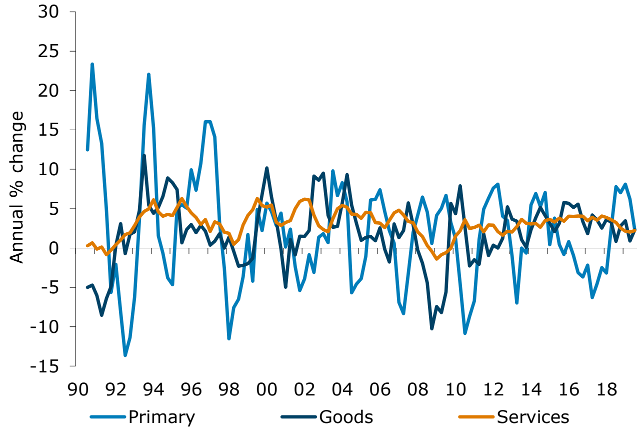


Figure 2. Production-based GDP components



Source: Statistics NZ

Figure 3. GDP per capita

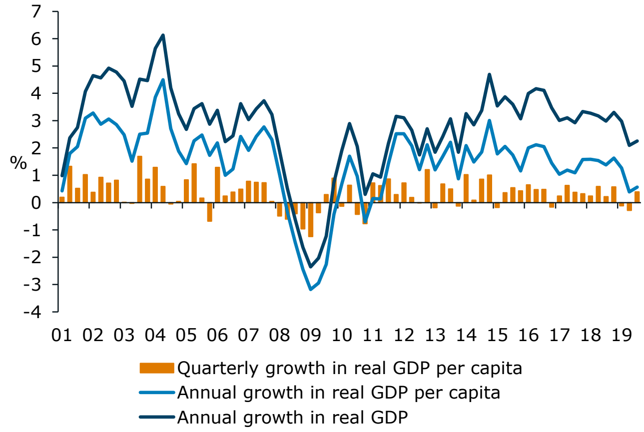
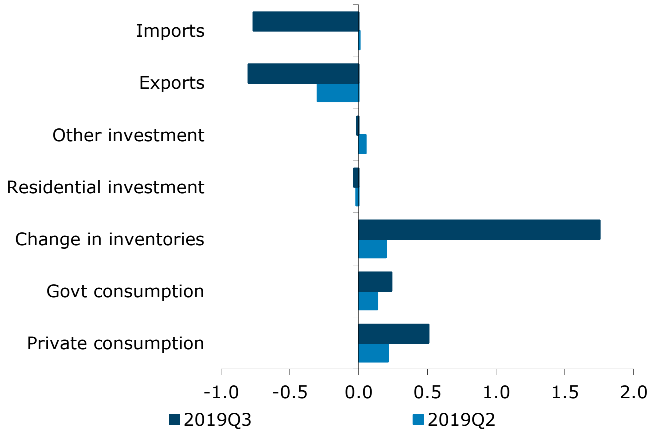


Figure 4. Contributions to quarterly growth in expenditure-based GDP



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