

# NZ Forecast Update and Q1 GDP Preview

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## Contact

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## GDP outlook slightly better but still very bleak

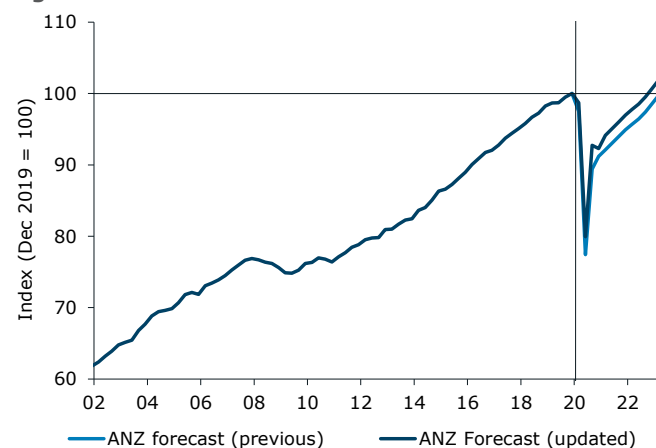
### Key points

- We have revised up our forecasts, but only slightly. Q1 GDP is expected to show a 1.3% q/q contraction but should be looked through.
- Significant economic weakness will become clear in coming quarters and it's going to be ugly, but the recovery will now occur a little faster.
- Markets might be buoyed for a while, but a reality check will come. It will be a slow recovery and the RBNZ needs to stay the course with QE.

### We have revised our forecasts up slightly

We now expect that GDP contracted 20-21% over H1 as a result of the COVID-19 pandemic and associated economic restrictions. This is less than the 22-23% fall previously estimated. The upward revision reflects that we have been able to move out of alert levels faster than previously expected.

Figure 1. ANZ GDP forecasts



Source: Statistics NZ, ANZ Research

The elimination of COVID-19 will spur a slightly stronger bounce in activity into the second half of the year, with firms and households a bit more confident than otherwise. Mass gatherings will allow some extra activity to take place, and productivity will be higher without social distancing.

But confidence and spending is still expected to be weak once the current bounce subsides, especially with some firms under pressure and unemployment rising. More economic activity will be possible, but it doesn't mean it will necessarily happen. Lost income and longer-term impacts on industries like tourism will create an economic hole that won't be easily filled. And the global outlook is bleak, making an export recovery more difficult. Our primary industries are facing headwinds via constrained production, higher borrowing costs, and lower prices. Plus the exchange rate has risen significantly, dampening net exports and GDP.

Weighing up these factors, the outlook now looks better, but only slightly. We now expect that GDP will contract 7-9% (previously 8-10%) this year. The recovery will still be slow, but it won't take quite as long for GDP to return to pre-COVID levels (end-2022 based on current forecasts, versus mid-2023 previously). We expect unemployment to peak at 10%, rather than 11%.

However, the recovery will be slow. [Labour-intensive industries](#) are under particular pressure and it will take a long time for the economy to reshape and recover to take up the slack. An updated forecast table is on [page 4](#).

We would emphasise that these forecast adjustments are not big changes relative to the size of the economic shock itself and the very wide bands of uncertainty around all forecasts at present. There are plenty of unknowns that could change the outlook. And the overall story remains the same. Eliminating COVID-19 so quickly was a best case scenario, but the best of a pretty bad bunch. New Zealand with a closed border is a smaller economy.

### Data is very noisy at present

The news flow has been more positive recently: New Zealand has eliminated COVID-19, economic activity is bouncing back, and the domestic and global economic data has been heading in the right direction. Things are looking a bit better than we had feared. But there is some noise in the data too.

As we discussed in our recent [ANZ NZ Insight: The recession is just beginning](#), there are reasons to be cautious when interpreting the recent bounce in activity. A bounce was always expected when lockdown restrictions were eased. But the buying flurry is not expected to last, with a weaker underlying economic pulse expected to be evident.

There is also a lot of other noise in the domestic and global data too. Changes in restrictions are creating volatility and will do so for a while. It is also understandably very difficult to measure what has been happening. Measurement issues may confuse the data signals meaningfully, and that uncertainty needs to be taken into consideration. It will take time for both volatility and measurement issues to abate, once more “stable” economic conditions are reached. In the meantime, separating signal from the noise will be an ongoing challenge.

### Q1 GDP data will have little signal

Next week’s GDP data will be affected by such measurement issues. They are also very ancient history when we consider how much has changed since the start of the year. For the record, we think that GDP actually contracted 2.2% q/q during the quarter (previous forecast: -2.5%, RBNZ: -2.4% q/q), but partial data so far suggests that only half of that may show up in official statistics.

We have pencilled in a pick of -1.3% q/q and 0.0% y/y (table 1) for reported GDP, but the uncertainty band around this is very wide. At face value, a print in line with our expectations might suggest conditions in Q1 weren’t as bad as we (or the RBNZ) feared. But we don’t think that is the case; some of this may reflect good news, but a significant portion likely comes down to measurement issues. Any weakness that has not been captured in the Q1 data won’t disappear from the record either; it is likely to be reflected in Q2 GDP instead. We estimate that GDP contracted 20-21% over H1, but how this will be spread across Q1 and Q2 is uncertain and may be impacted by the Q1 outturn next week. And of course, Q2 data is likely to be subject to measurement error too.

See [page 3](#) for more on our GDP and Balance of Payments forecasts.

**Table 1. GDP data summary**

	ANZ forecast	Prev
Quarterly % change	-1.3%	0.5%
Annual % change	0.0%	1.8%
Annual average % change	1.5%	2.3%

Source: Statistics NZ, ANZ Research

The full extent of the economic bounce will be in the Q3 GDP data, meaning that will be difficult to interpret too. But over Q3, high-frequency indicators will start to reflect the underlying data pulse. We will be watching business surveys, labour market data, the housing market, and spending in particular.

## Markets may continue to be buoyed

Markets (domestically and globally) have taken signals from recent positive news, spurred by abundant global liquidity. That has supported NZD and pushed bond yields higher.

It is reasonable to expect that low interest rates and risk premia will support asset prices, but the recent risk rally appears to be overdone. The recession is just getting started and there is a long recovery ahead. This will weigh on earnings, and is very likely to lead to a rise in defaults.

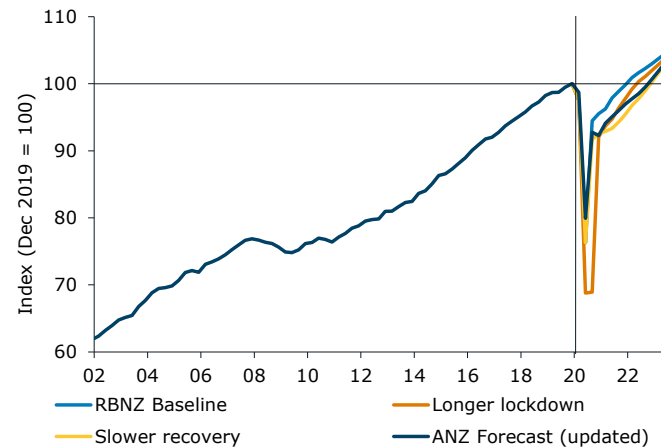
Markets are discounting these concerns and are pricing in a rapid recovery on the back of enormous stimulus. This theme may continue for a while yet. But in our view an eventual deterioration in the data and/or a reminder from RBNZ that it is a long road ahead will provide a reality check for domestic markets. That may not see yields go a lot lower, but will stem further increases. We expect to see flatter bond curves eventually, reflecting the slow recovery.

## Policy needs to stay the course

Relative to the RBNZ's forecasts, our progress eliminating COVID-19 has been faster than expected. The RBNZ assumed that we would be in Alert Level 2 for ten months in their May MPS baseline scenario. At face value, that means that recent developments present upside risk to the RBNZ's central forecast.

However, we think the RBNZ's baseline was too optimistic because it did not take into account the degree of weakness in demand we expect to become evident. In our view, the RBNZ's slow recovery scenario is the more relevant benchmark. A slightly better outlook than that (in line with our forecasts) is encouraging, but no reason for complacency.

**Figure 2. ANZ and RBNZ scenarios**



Source: Statistics NZ, RBNZ, ANZ Research

Inflation and unemployment are set to move dramatically away from target for a long time, and the RBNZ needs to keep its foot firmly on the accelerator as we enter the recovery period ahead. An acknowledgement of more positive news is expected at the OCR review, along with a dose of caution about the outlook. Then by August we think the weak outlook will become clear, with an expansion of QE to \$90bn expected.

## The details: Q1 GDP and BOP

New Zealand Balance of Payments and GDP figures are released at 10:45am next Wednesday and Thursday respectively. We think the economy contracted 2.2% q/q in Q1, based on our understanding of the various COVID-19 Alert Levels. But measurement issues could mute this by up to half. We expect to see a print closer to -1.3% q/q, with industry impacts as in table A1. There is much more uncertainty around these forecasts than usual.

**Table A1: ANZ Q1 industry-level forecast**

Industry	q/q%	%pt cont.
Agriculture, forestry, and fishing	-0.5	-0.03
Mining	-1.8	-0.02
Manufacturing	-1.0	-0.10
Electricity, gas, water, and waste services	0.0	0.00
Construction	-5.7	-0.36
Wholesale trade	-1.0	-0.05
Retail trade and accommodation	-0.6	-0.05
Transport, postal, and warehousing	-1.0	-0.04
Information media and telecommunications	-0.8	-0.03
Financial and insurance services	1.2	0.07
Rental, hiring, and real estate services	-1.2	-0.16
Prof, scientific, technical, admin, and support	-1.7	-0.17
Public administration and safety	0.3	0.01
Education and training	-4.8	-0.18
Health care and social assistance	1.2	0.07
Arts, recreation, and other services	-2.0	-0.06
Unallocated	-2.2	-0.17
Balancing item	--	0.00
<b>Gross domestic product</b>	<b>-1.3</b>	<b>-1.3</b>

Source: Statistics NZ, ANZ Research

Annual growth is expected to soften from 1.8% to 0.0% y/y. A print of -1.3% q/q for GDP is weaker than our previous forecast (-2.5% q/q) and the RBNZ's expectations at the time of the February MPS (-2.4%).

The annual current account deficit is expected to narrow by 0.4% pts of GDP to 2.6%. Significant improvement in the goods balance will be a key driver here, with seasonally adjusted goods exports lifting around 2.5% q/q and imports falling almost 3%. Services exports and imports are both expected to decline around 6%, reflecting the beginning of the zero-tourism dynamic that will be an even bigger feature of the Q2 data. The income deficit is expected to narrow in the quarter, but the magnitude is more uncertain than usual. Low global interest rates will keep the primary deficit under pressure, while reduced dividend payments to offshore investors could see outflows shrink considerably. However, that too could be more of a story for Q2.

**Table A2: Balance of payments data summary**

	ANZ forecast	Prev
Current account (\$m, actual)	1,874	-2,657
Current account (\$m, sa)	-950	-1,877
Annual CAB (\$bn)	-8.1	-9.2
% of GDP	-2.6%	-3.0%

Source: Statistics NZ, ANZ Research

## The details: ANZ economic forecasts

	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21
GDP (% qoq)	0.5	<b>-1.3</b>	<b>-19.0</b>	<b>16.0</b>	<b>-0.5</b>	<b>2.0</b>	<b>1.0</b>	<b>1.0</b>	<b>1.0</b>
GDP (% yoy)	1.8	<b>0.0</b>	<b>-19.0</b>	<b>-6.8</b>	<b>-7.7</b>	<b>-4.6</b>	<b>18.9</b>	<b>3.5</b>	<b>5.1</b>
CPI (% qoq)	0.5	0.8	<b>-0.4</b>	<b>0.1</b>	<b>-0.1</b>	<b>0.5</b>	<b>0.2</b>	<b>0.3</b>	<b>-0.2</b>
CPI (% yoy)	1.9	2.5	<b>1.6</b>	<b>1.0</b>	<b>0.4</b>	<b>0.1</b>	<b>0.7</b>	<b>0.9</b>	<b>0.8</b>
Employment (% qoq)	0.0	0.7	<b>-6.0</b>	<b>-1.9</b>	<b>1.5</b>	<b>1.0</b>	<b>0.7</b>	<b>0.9</b>	<b>0.9</b>
Employment (% yoy)	1.0	1.6	<b>-5.1</b>	<b>-7.1</b>	<b>-5.8</b>	<b>-5.5</b>	<b>1.3</b>	<b>4.2</b>	<b>3.5</b>
Unemployment Rate (% sa)	4.0	4.2	<b>7.6</b>	<b>10.0</b>	<b>9.7</b>	<b>9.3</b>	<b>9.2</b>	<b>8.9</b>	<b>8.4</b>

Figures in bold are forecasts. mom: Month-on-Month; qoq: Quarter-on-Quarter; yoy: Year-on-Year



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