ANZ Research

NZ GDP and Balance of Payments: Q3 2022 Preview

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Economic expansion; record-breaking deficit

Bottom line

- We've pencilled in a 1.1% q/q expansion for Q3 GDP due next Thursday, but we're braced for plenty of noise and data revisions.
- The bar is extremely high (stratospheric) for these data to have material implications for monetary policy. The data are noisy, ancient history, and won't provide much forward signal, given the RBNZ's recent hawkishness.
- The annual current account deficit is expected to widen to 8.0% of GDP – the widest deficit since these data began in the late 1980s.

The view

New Zealand's Q3 Balance of Payments and GDP figures will be released at 10:45am next Wednesday and Thursday respectively.

Hold on to your hats; the GDP data could get pretty wild:

- First, there's the noise related to economic normalisation, with industries such as accommodation and food services (up 30% q/q in Q2), transport (up 19.7% q/q in Q2), and arts and recreation (up 9% q/q in Q2) all surprising our indicator models recently. While a lot of the strength in Q2 appears genuine, the seasonal adjustment seems to have added to the noise, given transport and accommodation tend to be seasonally weaker in Q2. We could see the opposite occur in Q4/Q1, when these industries typically peak. Until these industries are consistently operating closer to typical levels and seasonal patterns, seasonal adjustment may add volatility (even though in normal times it does the opposite).
- Speaking of 'typical levels', manufacturing excluding food contracted 11.1% in Q2, as the end of petroleum refining pulled manufacturing lower. Industry reclassifications from manufacturing to wholesale will have permanent implications for the levels, meaning, once again, the seasonally adjusted data for the impacted industries are very likely to be subject to greater revisions and heightened volatility for a time.
- Then there's the annual benchmarking and updated weightings that will enter the Q3 data. This has the potential to drive significant historical revisions too.

Clearly, forecasting GDP remains a tricky business. But insofar as monetary policy is concerned, the GDP data is hardly front and centre right now. That's partly owing to the fact that Q3 is both noisy and ancient history, and partly owing to the fact that inflation and indicators of capacity stretch (particularly in the labour market) are the dominant drivers of policy decisions currently. And with the RBNZ forecasting a recession from the second half of 2023, it's not as if a softening in economic momentum over coming quarters is going to suggest it's time to change tack. Conversely, stronger-than-expected growth wouldn't necessarily suggest they need to hike by more either, if it's driven by supply-side factors. It's all about estimates of capacity stretch at the moment, and GDP currently just isn't a good indicator of that.

Data summary

	Q2 2022	ANZ Q3 2022 exp
GDP		
Quarterly % change	1.7%	1.1%
Annual % change	0.4%	5.7%
Annual average % change	1.0%	2.5%
Balance of Payments		
Current account ($m, actual)	-5,224	-10,200
Current account ($m, sa)	-7,127	-6,200
Annual CAB ($bn)	-27.8	-29.6
% of GDP	-7.7%	-8.0%

Turning to the details, the key partial GDP indicators have been a little mixed of late:

- The retail trade survey showed trade volumes excluding accommodation and food services were pretty stagnant in Q3. Meanwhile, the accommodation and food services component posted respectable growth, but we're wary: these data were way off the mark in Q2 (up 4.2% q/q vs the 30% q/q lift in the GDP component).
- The volume of building work put in place lifted a solid 3.8% q/q in Q3, but in Q2 construction GDP (down 2.4% in Q2) went in the opposite direction to this indicator. Wary.
- The quarterly manufacturing survey showed volumes up 3.1% q/q following a 4.8% decline in Q2.
- After adjusting for price changes, wholesale trade rose around 1.5% q/q.

Table 1 shows our industry-level forecasts. Overall, our expectation that the economy expanded 1.1% in Q3 is driven by:

- **services industries** lifting 0.8% q/q (making a 0.6ppt contribution to headline growth), bolstered by continued recovery in transport services.
- **goods-producing industries** are expected to rebound 2.5% q/q from Q2's 3.8% decline (a 0.4ppt contribution), with both manufacturing and construction bouncing back in Q3.
- **primary industries** are expected to grow 0.8% q/q (0.1ppt contribution).

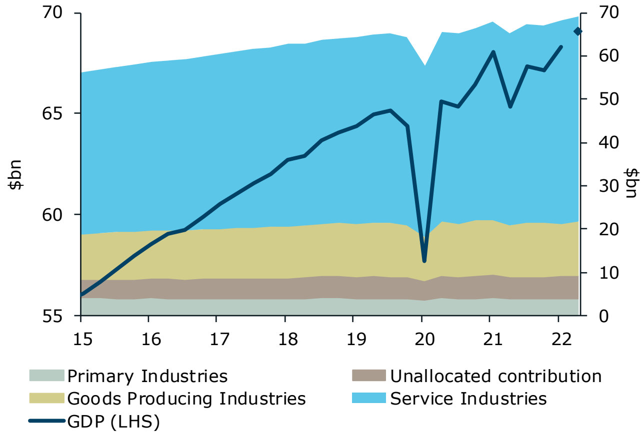
In Q3 last year, lockdown impacts saw the economy contract 3.9% q/q. That means annual growth figures are going to be bolstered by some sizeable base effects. Therefore, solid annual growth should not be interpreted as strong economic momentum.

All in all, the GDP figures are still a while away from becoming settled, and a fair way from becoming a reliable momentum indicator. Looking forward, our revised OCR call and softer housing outlook is expected to drive weaker-than-otherwise activity over 2023 and 2024. We'll be revising our GDP forecast to reflect this when we incorporate the Q3 data late next week.

Table 1. ANZ Q3 GDP industry-level forecast

Industry	q/q%	%pt cont.	y/y%
Agriculture, forestry, and fishing	0.9	0.04	-1.0
Mining	0.0	0.00	-9.1
Manufacturing	2.7	0.23	1.0
Electricity, gas, water, and waste services	0.5	0.01	1.2
Construction	3.0	0.20	10.8
Wholesale trade	1.5	0.08	9.9
Retail trade and accommodation	0.9	0.07	11.6
Transport, postal, and warehousing	4.0	0.18	20.4
Information media and telecommunications	0.3	0.01	0.8
Financial and insurance services	-0.2	-0.01	-0.2
Rental, hiring, and real estate services	0.1	0.01	1.4
Prof, scientific, technical, admin, and support	0.7	0.08	9.2
Public administration and safety	1.0	0.05	1.7
Education and training	0.0	0.00	0.4
Health care and social assistance	1.0	0.07	6.6
Arts, recreation, and other services	1.0	0.03	13.7
Unallocated	1.1	0.08	7.9
Balancing item	--	--	--
Gross domestic product	**1.1**	**1.1**	**5.7**

Figure 1. GDP forecast level

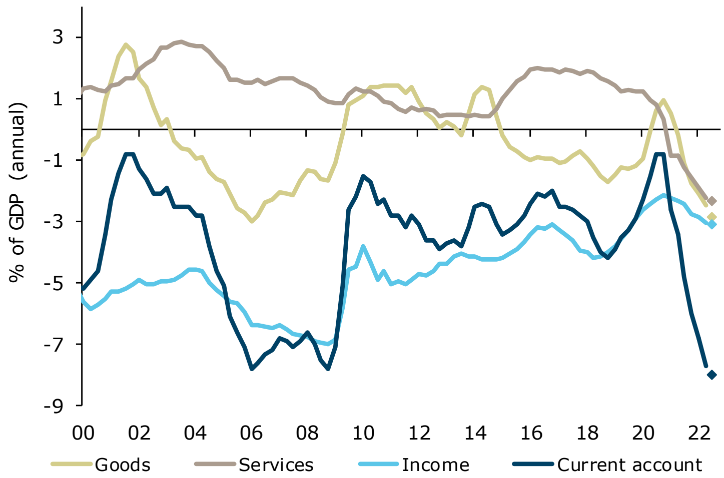


Source: Statistics NZ, ANZ Research

Turning to the balance of payments, we expect the annual current account deficit to widen 0.3ppt of GDP to 8.0% – that would mark the widest annual deficit in the history of these data (going back to the late 1980s). The big picture for the current account is little changed:

- The annual goods deficit has widened because imported goods have lifted strongly on the back of domestic demand (bolstered by fiscal and monetary stimulus). Meanwhile, exports of goods have struggled on the back of bad weather, labour shortages, and logistical challenges.
- The annual services balance (which tends to be in surplus) is in deficit thanks to closed-border impacts on tourism and education exports. The good news is that services exports are starting to recover on a quarterly basis. But there's a decent way to go before exports are outpacing imports again on an annual basis. Indeed, because services imports continue to push higher, services exports need to recover beyond their pre-pandemic level before services trade is back in the black.
- As a net borrower from the rest of the world, the rising global interest rate environment is expected to add widening pressure on the income deficit. That's a headwind that's expected to persist for a while yet.

Figure 2. Current account deficit



Source: Statistics NZ, ANZ Research

Looking forward, we see the annual current account deficit narrowing from the second half of 2023 as demand for imports softens and the recovery in travel-related exports is more advanced. But higher-for-longer global interest rates could act as a significant offset, keeping the income deficit under widening pressure.

In big-picture terms, New Zealand's external (im)balance shows that high inflation isn't the only reason to get the economy back onto a sustainable path through monetary tightening and fiscal consolidation. The current record-breaking deficit shows we've been living beyond our means, becoming more dependent on foreign capital in the process. The path to something more sustainable isn't a fun one (as it involves weaker domestic demand), but medium-term macroeconomic stability is at stake.

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