ANZ Research

NZ GDP: Q2 2023 Review

21 September 2023

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Contact

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Data summary

	Latest	Prev
Quarterly % change	0.9%	0.0%
Annual % change	1.8%	2.2%
Annual average % change	3.2%	2.9%

What recession … but one looming?

Bottom line

- The New Zealand economy bounced 0.9% q/q in Q2 on a seasonally adjusted basis. That follows an upwardly revised 0.0% read in Q1 (previously -0.1%). Technical recession revised away!
- We had pencilled in a 0.4% expansion, and while some of the surprise looks like genuine strength, there's still cyclone-induced volatility to consider.
- Looking through the noise, despite the positive surprise underlying economic momentum still appears soft, just not as soft as we previously thought. And questions remain around whether the economy is soft enough to see CPI inflation sustainably back to target in an acceptable timeframe. Particularly given housing appears to be gathering steam.
- We don't think today's data are a game changer for the October Monetary Policy Review (we expect a hold), but it certainly increases the likelihood that the discussion takes a hawkish tilt. Come the November MPS, the Q3 CPI inflation and labour market data will matter a great deal more than Q2 GDP (we are pencilling in a 25bp hike in November).

The big picture

The economy expanded 0.9% q/q on a seasonally adjusted basis in Q2, much stronger than our expectation of +0.4% q/q and the RBNZ's August MPS forecast of 0.5% q/q.

Of note, Q1's -0.1% q/q has been revised to 0.0% in today's release. While it could be revised the other way in time, and it's just a technicality, this suggests New Zealand wasn't technically in recession in the first quarter of 2023. That said, growth in per capita terms remains very soggy at 0.2% q/q showing economic conditions are still very weak for people on the street. On that front, high inflation and higher interest rates are certainly taking their toll on households and businesses, and that pressure is not expected to change until the RBNZ can confidently say it's got inflation back in the bag.

As we noted in our Preview, we'd caution against reading too much into a stronger than expected Q2 GDP release, as it's difficult to diagnose how much of that is noise (eg rebound from cyclone disruption) and how much is signal. Looking through the noise, quarterly growth has averaged 0.4% to 0.5% over the past couple of quarters, which is certainly below par. That said, the RBNZ's latest forecast assumes potential GDP grew by 0.8% q/q in Q2, suggesting the Monetary Policy Committee may feel a little uneasy that Q2 activity wasn't consistent with dissipating inflation pressures. While that may add to the risk that the tone around the Committee table in October takes on a hawkish tilt, we still don't think today's data meet the threshold for a hike in October. At the end of the day, we think the RBNZ will still want to see how capacity indicators and core inflation are evolving before taking any further action. So all up, we don't think the Q2 GDP data will be a game changer for OCR settings come October's Monetary Policy Review, but by the time the November Monetary Policy Statement rolls around we think there will be sufficient evidence to suggest the RBNZ has more work to do. We continue to expect no change to the OCR in the October Review and a 25bp hike at the November MPS. Next stop Q3 CPI (out 17 October).

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.

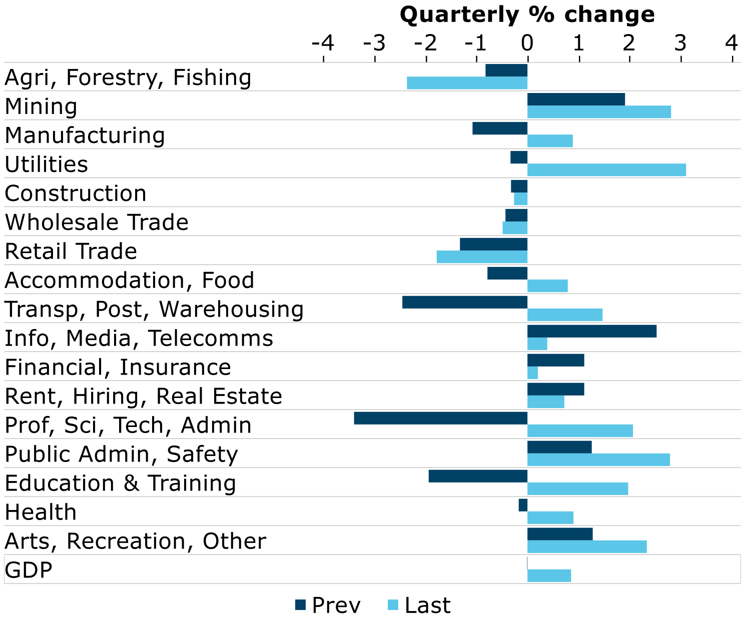
Services industries (about two thirds of GDP) expanded 1.0% q/q, stronger than our expectation of 0.4%. The miss was largely driven by transport, business services, public administration and safety, education, and health all coming in on the stronger side of our expectation. Stepping back, should growth across services industries remain elevated, sticky services inflation risks are more likely to materialise. A key worry for the RBNZ.

Goods-producing industries came in close to forecast at 0.7% q/q (ANZ: +0.6%), but with stronger electricity (+3.1% q/q) offset by weaker construction (-0.2% q/q). Manufacturing was as expected at 0.9% q/q.

Growth in primary industries surprised to the downside at -1.9% q/q vs +0.9% expected. It's tough going out there for many primary producers.

The unallocated tax component contracted 2.0% q/q, weaker than the flat read we had pencilled in. That follows growth in Q1 of 3.7% q/q. Noisy stuff.

Figure 1. Quarterly change in GDP by industry

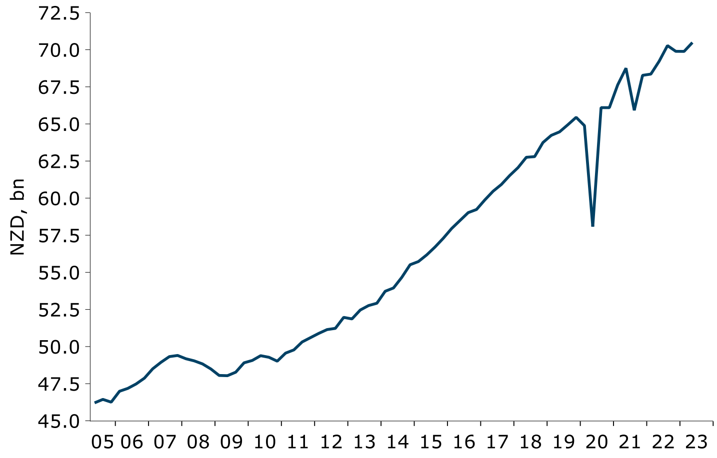


Source: Stats NZ, Macrobond, ANZ Research

In year-on-year terms, growth came in at 1.8%, with annual average growth coming in at 3.2%. That's certainly not what we'd call 'weak', but there's still plenty of quirky seasonality and COVID-related volatility making the signal from annual growth less reliable than otherwise.

The level of GDP shows just how much volatility lockdowns have caused in the data compared to history (figure 2).

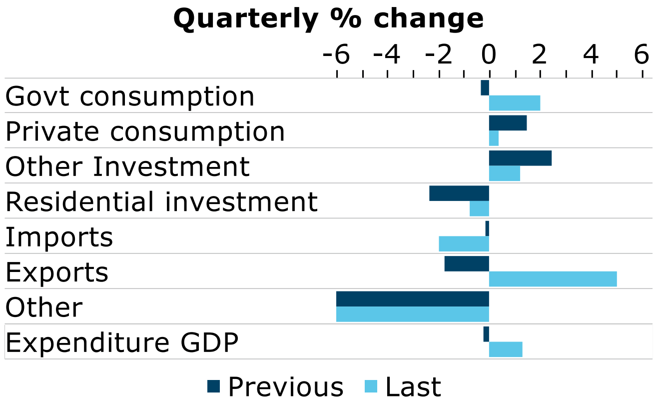
Figure 2. Production GDP



Source: Stats NZ, Macrobond, ANZ Research

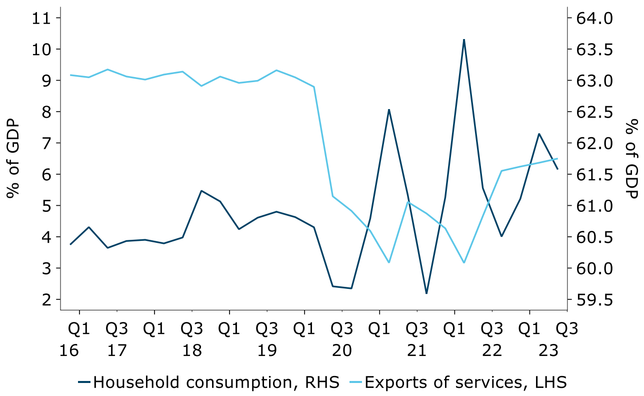
In real (price-adjusted) expenditure terms, GDP expanded 1.3% q/q, with private consumption lifting 0.4% q/q (after lifting 1.5% in Q1), well above the RBNZ's -1.8% pick. General government expenditure came in strong at 2.0% q/q as investment remained weak (-4.3% q/q). Net exports made a solid contribution to quarterly growth with total exports up 5.0% q/q and imports down 2.0%. Inventories were sharply lower for a second consecutive quarter dragging on headline growth. It's all a bit of a mixed bag.

Figure 3. Expenditure GDP growth



Source: Stats NZ, Macrobond, ANZ Research

Figure 4. Selected components share of GDP



Source: Stats NZ, Macrobond, ANZ Research

All in all, lockdown-level volatility may now be a thing of the past, but it would still be a stretch to call these data 'stable'. It's still a little early to say the private consumption and services exports as a share of GDP have stabilised, but volatility does appear to be reducing. Users of these data (including the RBNZ) will need to take into account just how much noise continues to reverberate long after lockdowns and closed borders, and more recently, weather disruptions.

Looking forward, New Zealand looks to have a touch more momentum than previously thought, but there is still plenty of noise look through. That said, momentum is softening, and is likely to remain subpar until the RBNZ has sufficiently tamed inflation. A loosening in fiscal settings on the other side of the election, a stubbornly tight (and inflationary) labour market, or a stronger housing-induced bump to domestic demand than expected may need to be met with a higher OCR than otherwise. In other words, provided CPI inflation pressures are too strong, monetary policy settings will need to remain a key constraint on economic activity. Conversely, the next big global shock could be just around the corner, which could end up doing a lot of the RBNZ's work for them. Our take is that risks are skewed towards domestic momentum not rolling over quite fast enough to prevent too-high domestic inflation from sticking around for too long, and that the RBNZ will need to come back to the hiking table. Today's data are unlikely to move the dial for the RBNZ at the October Monetary Policy Review (but they will likely impact the tone). Come the November MPS (when we'll have the Q3 reads on both CPI inflation and the labour market) we continue to pencil in a 25bp hike.

In terms of market reaction, interest rates spiked higher immediately after the data, with the 2yr swap up around 9 basis points, and the yield on the 10-year government bond (the April 2033) up around 4 basis points. Both had risen following this morning's US Federal Reserve meeting, which drove US bond yields higher, but today's GDP data just underscores our view that the risks remain heavily skewed towards the RBNZ hiking again in November. The Kiwi didn't really react to the data, and it's still struggling in the face of USD exceptionalism, but this data comes hot on the heels of a string of better than expected data prints, including yesterday's bump in milk prices, and that is likely to reassure FX markets and limit downside, even if it doesn't propel the Kiwi higher.

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