ANZ Research

NZ GDP: Q3 2023 Review

14 December 2023

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Contact

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Weaker across the board

Bottom line

- The New Zealand economy contracted 0.3% q/q in Q3 on a seasonally adjusted basis, weaker than our (and the RBNZ's) forecast of +0.3% and the market consensus expectation.
- In addition, data revisions suggest economic momentum in recent quarters has been softer than previously thought. Q2 was revised to +0.5% q/q (from +0.9%), and the Q4 2022 to Q1 2023 technical recession is back (after it was revised away).
- Compared to the RBNZ's November MPS forecast there appears to be a bit less momentum out there, and all else equal that raises the bar considerably for a hike. However, the evolution of capacity indicators between now and the February MPS will be key. Importantly, today's data is not an obvious catalyst for a cut any time soon. Sticky inflation remains the big concern.

Gauging momentum in supply and demand

The economy contracted 0.3% q/q on a seasonally adjusted basis in Q3, much weaker than our expectation (and the RBNZ's November MPS forecast) of +0.3% q/q, as well as the market consensus expectation (+0.2%).

Data revisions (reflecting improvements made by Stats NZ and the annual benchmarking process) imply the economy has been running a little cooler in recent quarters than previously thought, suggesting monetary tightening has been getting a little more traction.

Under the hood, the details are also soft:

- In the production cut, momentum across goods-producing industries remains very weak as higher interest rates continue to bite. But more importantly, our understanding of momentum across services industries is softer, suggesting sticky services inflation risks are more contained than previously.
- In the expenditure cut, the economy overall was softer than we expected, with domestic demand particularly weak and net exports struggling despite recovering services exports (chiefly international tourism).

All up, we'd say the combination of the headline read, the underlying details and the data revisions suggests economic momentum in Q3 was travelling at a slower pace than we and the RBNZ expected. Accordingly, all else equal today's data will likely see the RBNZ revise down their estimate of how inflationary economic conditions are, and could see them revise their output gap assumption into negative territory by year end (was 0.0% as at Q4 in the November MPS).

Our assessment is that the supply side of the economy is recovering relatively quickly, and that today's softer data are thus more reflective of waning demand and inflation pressures. However, subsequent data on the CPI, labour market, and capacity indicators will all colour the RBNZ's ultimate interpretation of today's data when it comes to updating forecasts in February.

Data summary

	Latest	Prev
Quarterly % change	-0.3%	0.5%
Annual % change	-0.6%	1.5%
Annual average % change	1.3%	3.0%

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.

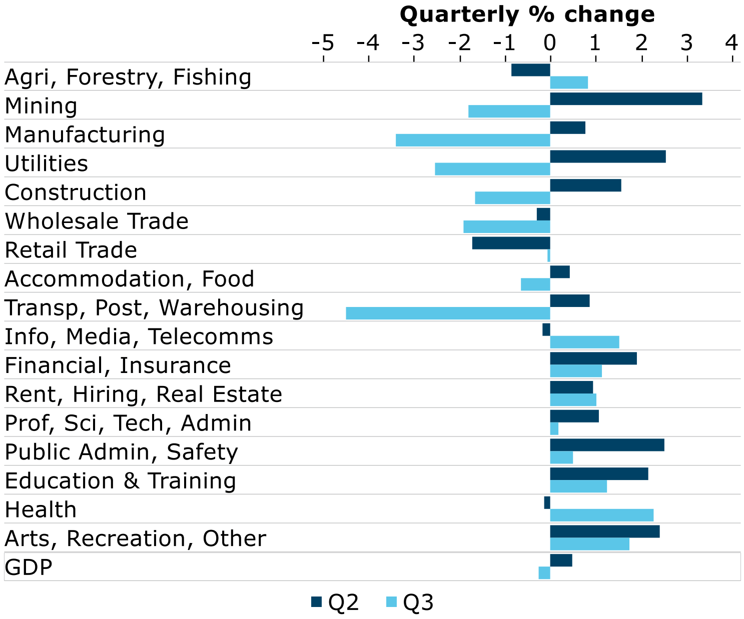
Services industries (about two thirds of GDP) expanded 0.4% q/q, weaker than our expectation of 0.6%. The miss was largely driven by weaker wholesale trade (-1.9% q/q), retail (-0.2% q/q), transport (-4.5% q/q), and business services (+0.2% q/q). Stepping back, today's data suggest momentum across services industries is slower than previously thought, mitigating sticky CPI inflation risks somewhat.

Goods-producing industries came in a lot weaker than forecast at -2.6% q/q (ANZ: -1.1%). Electricity (-2.5% q/q), construction (-1.7% q/q), and manufacturing (-1.4% q/q) were all weaker than expected.

Growth in primary industries was close to our expectation at +0.6% q/q (ANZ: 0.7%).

The unallocated tax component contracted 4.9% q/q, much weaker than the 1% lift we had pencilled in.

Figure 1. Quarterly change in GDP by industry

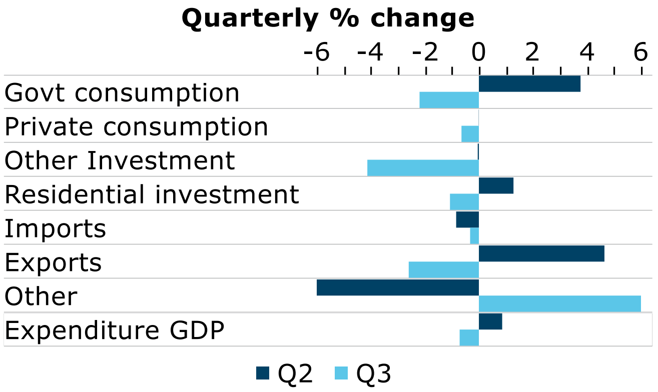


Source: Stats NZ, Macrobond, ANZ Research

In per-capita terms, quarterly growth came in at -0.9% q/q. Surging migration-led population growth means the economy at the individual household level is much weaker than headline GDP suggests. It's worth recalling that the RBNZ's working assumption is that net migration is a net positive for CPI inflation pressure, suggesting the more migration-driven growth we get, perhaps the more pain the RBNZ will need to inflict at a per-capita level, whether that's through more hikes or just holding rates high for longer. But today's data suggests plenty of per capita pain.

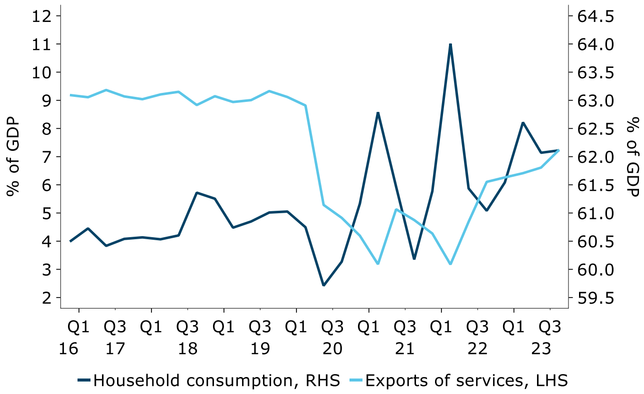
In real (price-adjusted) expenditure terms, GDP contracted 0.7% q/q, with private consumption down 0.6% q/q, a shade stronger than the RBNZ's -0.9% pick. However, durables goods consumption was particularly soft, down 3.2% q/q, suggesting strength in Q2 was likely more cyclone-related than momentum, which was our diagnosis at the time. General government expenditure came in weak at -1.8% q/q as investment remained weak (-3.4% q/q). Net exports made a negative contribution to quarterly growth, with total exports down 2.6% q/q and imports down 0.3%. Changes in inventories made a strong contribution to growth (1.5ppts) after dragging over the past two quarters. This inventory build was possibly largely unintended, reflecting demand weakening faster than the likes of retailers were expecting.

Figure 2. Expenditure GDP growth



Source: Stats NZ, Macrobond, ANZ Research

Figure 3. Selected components share of GDP



Source: Stats NZ, Macrobond, ANZ Research

Looking forward, the economic backdrop is expected to remain sub-par until CPI inflation has eased and the RBNZ can normalise monetary conditions. While today's data were on the softer side, the RBNZ will not yet be convinced that an OCR at 5.5% will be enough to get the inflation-fighting job done in an acceptable timeframe. But in all-else-equal terms, it certainly reduces the odds that the RBNZ will be hiking again.

As we note in this Insight, there is plenty of nuance in the upcoming data to keep in mind between now and the February MPS. GDP data is just the first course. Next week's Half-Year Economic and Fiscal Update will provide our first glimpse into fiscal settings under the new Government, but we're cognisant that the full details of the policy agenda may not be incorporated into the Treasury's outlook until May's Budget, and that the Half-Year Update forecasts may look more stimulatory than what ends up coming to pass.

Markets

Interest rates have fallen a long way today, having opened lower in line with moves in US interest rates, which fell sharply after this morning's dovish Fed meeting, only to go another leg lower on soft GDP data. To put the moves in perspective, the 2yr swap rate has settled at around 4.85%; that's exactly 100bp below where it peaked in early October, and 21bp below where it closed yesterday. Long-end rates are down almost as much, with the 10yr NZGB yield now around 4.66%, down 95bp from its October peak and around 12bps since yesterday.

In FX markets, the Kiwi jumped 90bps on the Fed statement, but it has come back around 40bps since the GDP data, coming to rest around half a cent higher. These market reactions are understandable – having essentially confirmed that they are done, the Fed has given the market implicit licence to ponder when and by how much rates will fall in the US, and local GDP data represents a direct challenge to the RBNZ's view of resilience on the activity front. Inflation still isn't licked in New Zealand, but if activity continues to slow in line with trends in today's GDP data, it's hard to see markets backing away from calls for cuts, especially with the Fed now signalling 75bp of cuts in 2024.

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