ANZ Research

# Preview: NZ GDP and Balance of Payments – Q4 2023

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Contact

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## Services momentum key

### Bottom line

- We've pencilled in a 0.1% q/q expansion for Q4 production GDP, weaker than our previous forecast of 0.4% but a smidgen above the RBNZ's February MPS pick of 0.0%.
- For the RBNZ, the details will matter. The February MPS forecast for expenditure GDP is +0.2% q/q (ANZ: +0.3%), with private consumption expected to come in at -0.5% q/q (ANZ: -0.6%). Should headline GDP come in stronger than the RBNZ expects but it's driven, say, by weaker imports, this may not be as hawkish as the headline suggests.
- That said, disentangling the noise vs signal in the GDP data remains a harder task in the post-COVID era. Parts of the economy (particularly international tourism) are still shy of "normal" levels, and that could culminate in surprisingly weak services exports growth in seasonally adjusted terms (despite the continued recovery in unadjusted terms). Further, while quarterly growth momentum appears to be travelling somewhere between -0.2% q/q and +0.2% q/q, that doesn't mean the Q4 print won't surprise outside of this range. Determining what's signal vs noise can quickly become subjective (sometimes we won't fully appreciate what's temporary until we have more data), but the prior two Monetary Policy Statements have appeared to put a bit more weight on GDP surprises than we have.
- One of the key areas we'll be on the lookout for is a further softening in services momentum. That's where we see sticky domestic inflation risks. Services tends to lag goods, suggesting a softening is in the pipeline.
- The annual current account deficit is expected to narrow 0.5%pts to 7.1% of GDP. Some of that looks like it might come from upward revisions to services exports in Q2 and Q3. But in big-picture terms, this is still too wide to call sustainable.

### Data summary

| | Q3 2023 | ANZ Q4 2023 exp |
|---|---|---|
| **GDP** | | |
| Quarterly % change | -0.3% | 0.1% |
| Annual % change | -0.6% | 0.1% |
| Annual average % change | 1.3% | 0.7% |
| **Balance of Payments** | | |
| Current account ($m, actual) | -11,465 | -8,200 |
| Current account ($m, sa) | -7,354 | -7,230 |
| Annual CAB ($bn) | -30.6 | -29.0 |
| % of GDP | -7.6% | -7.1% |

### The big picture

New Zealand's Q4 Balance of Payments and GDP figures will be released at 10:45am next Wednesday and Thursday respectively.

The economy is slowing on the back of past monetary tightening, but there's a lot more going on out there than just the impact of tighter monetary policy, and it's not all one-way traffic:

- Fiscal settings have been stimulatory, reflecting the 1.4% of GDP increase to Government spending in Budget 2023. Focus is now turning to Budget 2024, where both we and the RBNZ are looking to weigh up the net impact of tax and spending cuts. Our current working assumption is a broadly neutral package, meaning fiscal settings are set to become less expansionary in the year to June 2025 compared to 2024.
- Surging net migration is flattering headline growth but is making for particularly grim reading in per-capita GDP terms. Population growth adds to both aggregate supply and demand, making the net impacts on inflation ambiguous. One thing's for sure, high migration is masking just how weak the economy is at the individual or household level.

- The housing market is no longer a drag, and easier LVR settings, gradually falling mortgage rates, and a loosening in housing-related Government policy will provide some support this year. But against a backdrop of a softening labour market, it's hard to see housing driving a rapid resurgence in domestic demand any time soon.

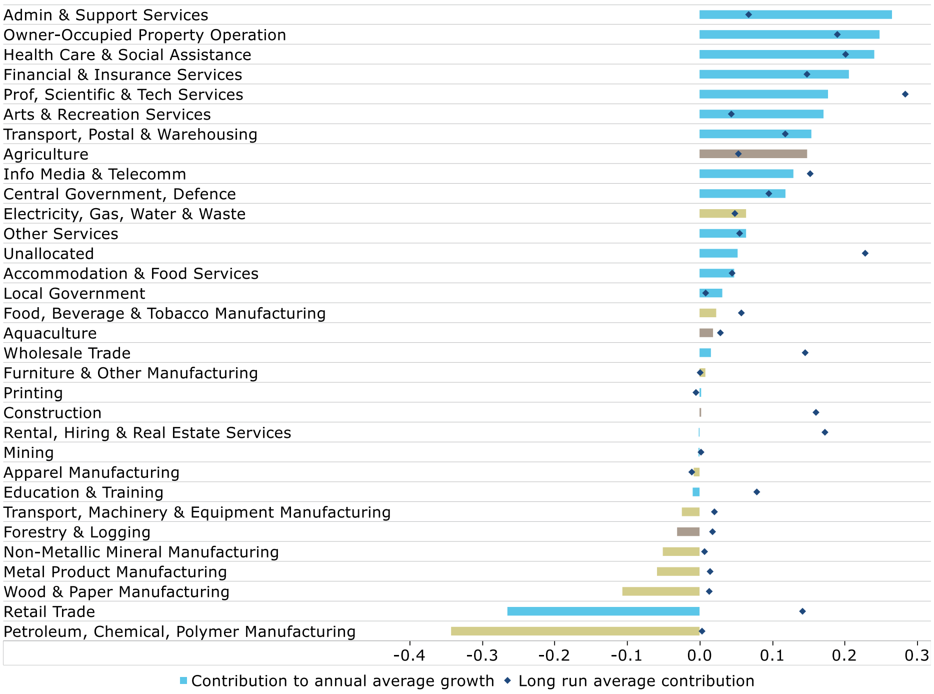
While there are lots of moving parts to consider, monetary conditions are expected to keep the pressure on demand until the RBNZ is confident it has done enough to tame inflation. But it's worth highlighting that taming inflation isn't just about restraining demand. A stronger supply recovery, such as a larger lift in labour productivity, could mean measured activity lands on the more robust side of expectations while inflation nonetheless continues to slow. Measured activity (GDP) tells only part of the story.

When it comes to the implications for monetary policy, our observation is that the RBNZ has put more weight on recent GDP outturns than we thought warranted at the time. Q2's 0.9% q/q economic expansion (which was later revised to +0.5%) was a big upside surprise to both our and the RBNZ's forecast, but we had strong suspicions there was just as much noise as signal in this release, particularly given it included temporary impacts following cyclone Gabrielle. However, the following MPS (November) had quite a hawkish tone. Fast forward to Q3's weaker-than-expected GDP read of -0.3% q/q (which included downward revisions to history), and that appeared to contribute to the relatively dovish tone of the February MPS. We're certainly not saying the RBNZ should completely discount the GDP data, but the past two quarters show just how difficult it currently is to get the balance right. The good news is that monetary policy is a repeat game.

In theory, the post-COVID "noise" in the GDP data is subsiding with each release, but it wouldn't be accurate to say the economy is currently operating "normally". International visitors, for example, are still running at around 80% of their pre-pandemic level, and that could show up in weaker seasonally adjusted services exports than expected (despite unadjusted tourist numbers lifting strongly over the summer).

We prefer the production cut of GDP to get a feel for the underlying picture of economic momentum, as it's less susceptible to quirky seasonality. We'll be paying particularly close attention to the services industries (which are expected to slow further in Q4), as these are a key source of sticky inflation risk. Figure 1 (over page) shows the contributions to annual average growth by industry to Q3 2023. It demonstrates that the residual robust momentum in the economy is being driven by services industries (retail being an outlier), and that goods industries (particularly manufacturing) is where weakness is particularly concentrated. Of note, the top seven contributions to annual growth in Q3 came from services industries, and the top four industries were all running hotter than their historical average pace. At the other end of the spectrum, the closure of Marsden point has been a significant drag on GDP growth, but one that doesn't reflect the stance of monetary policy. Retail trade on the other hand sure does! We'll update this chart in our Review of the Q4 release.

**Figure 1. Industry contributions to growth (Q3 2023)**




Bars are coloured according to industry group: Services (light blue), Goods (lemongrass), Primary (brown)
Source: Stats NZ, Macrobond, ANZ Research

## The details

Turning to the details of the GDP release, key partial indicators have landed on the softer side:

- The **retail trade** survey was as soft as a kitten, with trade volumes down 1.9% q/q and broad-based weakness across most categories. Recent changes to the seasonal adjustment methodology in the retail survey may improve the correlation with the GDP component, but we'll have to wait and see.
- The **volume of building work put in place** fell 0.1% q/q in Q4, with a 2.4% q/q fall in residential work broadly offset by a 4.6% rise in non-residential work put in place.
- The quarterly **manufacturing** survey showed volumes fell 0.6% q/q in Q4, with both food, and ex food and petrol manufacturing down in the quarter.
- After adjusting for price changes, **wholesale trade** appears to have contracted in the quarter.

Table 1 (over) shows our industry-level forecasts. Overall, our expectation that the economy expanded 0.1% in Q4 is driven by:

- **Services industries** (around two thirds of GDP) lifting 0.1% q/q (making a 0.1ppt contribution to headline growth).
- **Goods-producing industries** expected to contract 0.2% q/q (making a flat (0.0%pt) contribution to headline growth at one decimal place).
- **Primary industries** expected to contract 0.3% q/q (with its contribution to headline GDP also coming in flat).

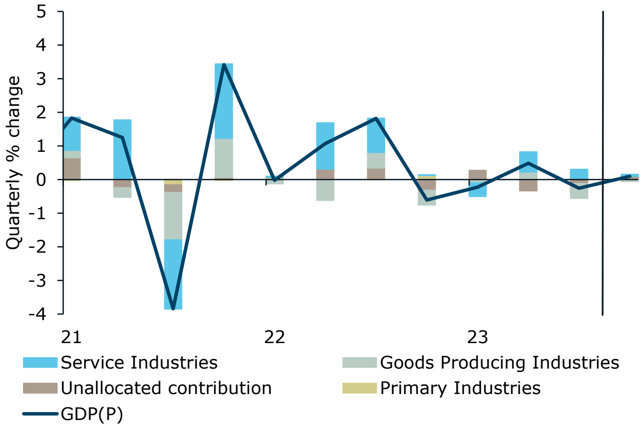
Regarding the expenditure cut, we've pencilled in a 0.3% q/q expansion for GDP. Net exports, particularly of goods, look set to make a strong contribution to quarterly growth as imports fall due to slowing domestic demand. On that front: private consumption is expected to contract 0.6% q/q, residential investment is expected to contract around 3%, other investment is expected to be little changed, and government consumption is expected to lift 0.7% q/q. Meanwhile, changes in inventories are expected to weigh on quarterly growth, broadly offsetting the strong net exports contribution.

Turning to the per capita story, population growth of 0.6% q/q in Q4 sets the bar pretty high for avoiding yet another per capita GDP contraction. On our forecast, Q4 will mark five consecutive quarters of negative per capita GDP growth, down 3.7% from Q3 2022. And with net migration still very elevated, we think this measure has further to fall over coming quarters. For context, per capita GDP contracted for seven consecutive quarters (4.2% peak to trough) following the Global Financial Crisis.

**Table 1. ANZ Q4 GDP industry-level forecast**

| Industry | q/q% | %pt cont. | y/y% |
|---|---|---|---|
| Agriculture, forestry, and fishing | -0.4 | -0.02 | -0.9 |
| Mining | 0.4 | 0.00 | 5.6 |
| Manufacturing | -0.5 | -0.04 | -3.1 |
| Electricity, gas, water, and waste services | 0.4 | 0.01 | 0.1 |
| Construction | -0.2 | -0.01 | -1.6 |
| Wholesale trade | -1.0 | -0.05 | -3.9 |
| Retail trade and accommodation | -1.4 | -0.09 | -3.7 |
| Transport, postal, and warehousing | -1.3 | -0.05 | -6.6 |
| Information media and telecommunications | 0.6 | 0.03 | 4.1 |
| Financial and insurance services | 0.5 | 0.03 | 5.6 |
| Rental, hiring, and real estate services | 0.8 | 0.11 | 3.8 |
| Prof, scientific, technical, admin, and support | -0.2 | -0.02 | -2.6 |
| Public administration and safety | 0.7 | 0.03 | 5.0 |
| Education and training | 0.4 | 0.01 | 2.0 |
| Health care and social assistance | 0.5 | 0.03 | 1.1 |
| Arts, recreation, and other services | 0.7 | 0.02 | 5.7 |
| Unallocated | 1.4 | 0.10 | -3.2 |
| Balancing item | N/A | 0.00 | N/A |
| **Gross domestic product** | **0.1** | **0.1** | **0.1** |

**Figure 2. Production GDP forecast**




Source: Statistics NZ, ANZ Research

Turning to the Balance of Payments, we expect the annual current account deficit to narrow from 7.6% of GDP in Q3 to 7.1% (a touch narrower than our previous published forecast of 7.3%). Trade data released for Q4 suggest both the annual goods and services deficits will narrow in Q4. Meanwhile, the income deficit, which is always the harder part to forecast given limited indicators, is expected to widen 0.1%pts to 3.1% of GDP as foreign-held NZ investments outperform NZ-held foreign investments.

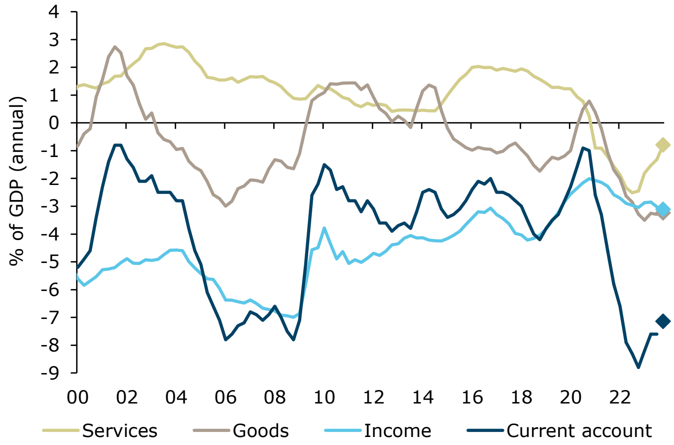
We also wouldn't be surprised if the annual deficit is revised a little narrower. Services exports look like they are in for positive revision in Q2 and Q3, and all else equal that could shave as much as 0.2%pts off Q3's annual deficit of 7.6% of GDP. We're not in the habit of forecasting revisions, but that's the way the risks appear skewed this quarter.

On a quarterly seasonally adjusted basis:

- We expect the goods deficit to narrow, with exports down around 1% q/q and imports declining 2.5%. Under the hood, weak import volumes and solid quarterly growth in export volumes is expected to more than offset the weaker terms of trade, which fell 7.8% q/q on an OTI basis. Importantly, we won't know the volumes/price split until Q4 GDP data are released.

- The services deficit is expected to narrow in the quarter as exports recover 10% q/q or so and imports dip slightly. However, it's important to note that the seasonal adjustment of these data (particularly exports) is highly uncertain given Stats NZ are still working through the fact that the international tourism recovery from closed borders is not complete, and that makes disentangling the “seasonal component” from the “trend” and the “irregular component” all the more difficult. But one observation we’ve made looking at the pre-BoP trade data is that unadjusted services exports look like they’ll be revised slightly higher in Q2 and Q3. It’s just not clear how that will impact the seasonally adjusted series.
- The income deficit (which isn’t seasonally adjusted) is expected to remain broadly stable, with high global interest rates continuing to weigh on the primary deficit.

**Figure 3. Current account deficit**




Source: Statistics NZ, ANZ Research

Looking forward, we see the annual current account deficit narrowing from here as demand for imports softens and the recovery in travel-related exports continues. But higher global interest rates are expected to partially offset a narrowing in the goods and services deficits.

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