Recoil

Bottom line

- The New Zealand economy expanded 0.3% q/q in Q3, reflecting payback from Q2’s strong 1.0% q/q print, but also a hint of deceleration in underlying momentum.
- Annual growth moderated to 2.6% in Q3 from a revised 3.2% in Q2, within recent ranges and consistent with our expectation that growth will remain range bound at 2½-3% over the next couple of years.

Key points

The economy expanded 0.3% q/q in Q3, weaker than both market (0.6%) and our own expectations (0.5%). This saw annual growth moderate to 2.6% from an upwardly revised 3.2% in Q2. This is the weakest quarterly pace of growth since Q4 2013.

Data revisions (as part of Statistics NZ’s annual benchmarking methodology) saw historical GDP growth revised a little lower in the year to March 2017 (from 3.7% to 3.6%) but higher in the year to March 2018 (from 2.7% to 3.1%). On balance, this paints a slightly stronger picture of the economy’s performance in recent years.

There was plenty in today’s release for the RBNZ to ponder:

- First, it was below the November MPS forecast for growth of 0.7% q/q, presenting downside risks to their outlook for growth to accelerate to 3.4% in 2019.
- In addition, upward revisions will likely increase the Bank’s view of potential output in history, which if carried through to the outlook, implies slightly weaker underlying inflation pressures for a given rate of growth – at least at the margin.
- And beyond this, the Bank will need to make an assessment of whether economic momentum is (and will remain) consistent with a sustained lift in core inflation to 2% over the medium term. And with growth looking like it’s decelerated a little faster over the past year, we remain sceptical.
- Combined with slowing global growth, wobbly global equity markets, and a cooling housing market, the case is mounting for a more dovish RBNZ stance. No doubt, Q4 core CPI (out 23 January) will be closely watched.

Turning to the details of today’s release, the degree of payback from Q2’s strong 1% print was slightly greater than expected, and admittedly it wasn’t quite where we had anticipated. Indeed, agriculture, forestry & fishing and mining both came in ahead of expectations, at 0.8% q/q and 12.4% q/q respectively.

Rather, it was goods production that showed the largest degree of payback, down 1.0% q/q following an upwardly revised 1.5% lift in Q2.
That said, growth in services industries (up 0.5% q/q) was also a little softer than we had pencilled in, and at the margin this suggests the economy’s momentum is slowing. However, services still put a floor under Q3’s deceleration, which we suspect is owing to still-high (but easing) migration-led population growth, with respectable household financial positions (supported by the tight labour market, the Families Package, and low interest rates), and the elevated terms of trade also playing a part.

Overall, 11 of the 16 production industries recorded higher levels of activity compared to Q2.

Expenditure GDP outperformed its production-based equivalent, rising 0.5% q/q. Private consumption rose a healthy 1.0% q/q (making a 0.6%pt contribution), while general government consumption (down 1.1%) provided a partial (0.2%pt) offset. Residential investment (up 1.3% q/q) was strong, while other investment was softer (down 2.1%). Net exports made a broadly neutral contribution. The nominal economy grew 1.0% q/q, boosted by higher consumption prices.

Per capita growth (or lack thereof, at 0.0% q/q) is certainly nothing to write home about. Annual growth in this measure, at just 1.0% y/y, remains mediocre, with implied labour productivity growth an underwhelming story and migration-led population growth the key narrative.

All up, we expect growth can continue to muddle along at an annual pace of 2½-3%, as a number of economic headwinds and tailwinds play out. This would be a touch shy of where we see trend growth, suggesting it will be a struggle for core inflation to lift sustainably to the RBNZ’s 2% target.
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