CRUISE CONTROL

BOTTOM LINE

- Economic growth was steady in Q4, with the economy expanding at a slightly slower-than-expected pace. Modest downward revisions also gave the figures a softer feel, although the details are perhaps not as disappointing as the headline figures suggest.

- Ultimately though, the figures paint a picture of an economy growing close to trend, and it is a pace we more-or-less see continuing over the coming year or so. The economy is not firing on all cylinders, but neither is it rolling over to any worrying degree. At this point in the cycle, that is nothing to be scoffed at.

- Overall, we see few implications for monetary policy. The OCR is on hold for some time yet.

KEY POINTS

- The economy expanded by 0.6% q/q in Q4, which was below consensus expectations (0.8%). It is a similar pace of growth to that recorded in Q3. But on the back of some modest downward revisions, annual growth was broadly steady at 2.9% y/y (where it has effectively held for the past 12 months).

- Despite the softer-than-expected result, growth was actually reasonably broad-based in the quarter. In fact, 13 of the 16 production-based industries recorded stronger levels of activity, with agriculture, forestry and fishing (-3.2% q/q) proving to be the biggest drag, most likely on account of unseasonably dry and hot weather. Relative to our own expectations, this was the main source of surprise. Goods-producing industries eked out 0.4% q/q growth, led by a modest lift in construction activity and stronger value-added production from the utilities sector. Services sector activity, as expected, posted the strongest growth, rising 1.1% q/q, led by solid growth in retail and accommodation, professional and administrative services and transport.

- Expenditure GDP rose a more modest 0.4% q/q. While that does sound weak, again the composition was arguably a little firmer. On the back of a solid lift in household consumption (1.2% q/q) and other fixed asset investment (3.7% q/q), final domestic demand posted a decent 1.2% lift. Courtesy of some large capital imports, net exports dragged on growth to the tune of 1.3%pts, while inventories made a large 1.3%pt contribution.

- Across other elements of the figures, it was a mixed bag. Nominal growth was solid, at 1.4% q/q (6.1% y/y), and goes a long way to explain the recent strong run in monthly tax revenue outcomes. Real gross national disposable income also rose at a decent 1.4% q/q (3.0% y/y) pace. However, per capita growth has remained mediocre, at just 0.1% q/q (0.8% y/y).

- Stepping back, while today’s figures are perhaps a touch disappointing, they still paint a picture of an economy recording a respectable pace of growth. Yes, the economy has cooled from the strong, above-trend rates experienced over 2016 (this is most noticeable in per capita terms). However, growth around trend (~3%) is certainly
nothing to be scoffed at, especially at a time when the economy has been grappling with a softer housing market, credit headwinds, late-cycle capacity pressures and increased political uncertainty. It speaks to the economy’s flexibility and resilience.

- **And looking forward, it is a pace of growth we more-or-less expect to continue.** Yes, there are headwinds. Firms are facing greater margin pressure, the low-hanging fruit growth wise have already been picked. We need solid rates of productivity growth to be maintained, given that recent strength in population and labour utilisation growth is unlikely to be maintained. There remain risks from the global backdrop, especially, most recently, on the trade front. And we expect household consumption growth to slow (even with still decent household income growth) as precautionary saving is rebuilt. But with fiscal stimulus around the corner, the terms of trade at historic highs and internal and external imbalances far less pronounced than they’d typically be at this point cycle, we don’t see the cycle tipping over in any meaningful way just yet.
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