Q4 GDP AND BALANCE OF PAYMENTS PREVIEW

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CONTRIBUTORS

Phil Borkin
Senior Economist
Telephone: +64 9 357 4065
E-mail: philip.borkin@anz.com

DATA SUMMARY

<table>
<thead>
<tr>
<th>GDP</th>
<th>Last</th>
<th>ANZ exp</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quarterly % change</td>
<td>0.6%</td>
<td>0.7%</td>
</tr>
<tr>
<td>Annual % change</td>
<td>2.7%</td>
<td>3.1%</td>
</tr>
<tr>
<td>Annual average % change</td>
<td>3.0%</td>
<td>2.9%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Balance of Payments</th>
<th>Last</th>
<th>ANZ exp</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current account ($m, actual)</td>
<td>-4,679</td>
<td>-2,240</td>
</tr>
<tr>
<td>Current account ($m, sa)</td>
<td>-1,309</td>
<td>-1,670</td>
</tr>
<tr>
<td>Annual CAB ($bn)</td>
<td>-7.10</td>
<td>-7.40</td>
</tr>
<tr>
<td>% of GDP</td>
<td>-2.6%</td>
<td>-2.6%</td>
</tr>
</tbody>
</table>

AROUND TREND

- We expect respectable GDP growth of 0.7% q/q in Q4, which would see annual growth tick up to 3.1% (i.e. around trend). If anything, we see some modest upside risk to our expectation.
- Primary, goods-producing and services sector activity should all contribute positively to overall growth. Net exports look set to drag on expenditure-based growth, but final domestic demand growth should be strong.
- We expect balance of payments figures to show a modest widening in the seasonally adjusted current account deficit, but the annual deficit stable at 2.6% of GDP.

KEY POINTS

- December quarter Balance of Payments and GDP figures are released at 10:45am next Wednesday and Thursday respectively.
- We see GDP expanding by a respectable 0.7% q/q, on par with the pace of growth recorded in Q3. If anything, we see risks skewed modestly to the upside. A result in line with our expectation would see annual growth tick up to 3.1% y/y, which is pretty much where we see trend at present. It would see per capita growth remain at a modest 0.2% q/q (1.0% y/y).
- We expect primary industries to recover from Q3’s weakness. Milk production over the quarter was weather impacted, but thanks to another strong quarter for the forestry sector (with sawn timber and log exports up 11% q/q), and what appears to have been a decent performance from horticultural sectors, we see overall primary-sector activity lifting by 0.4% q/q.
- We expect goods-producing sectors to rise 0.8% q/q (0.2%pt contribution) due to a combination of modest growth in construction activity and a further small lift in manufacturing production. Partial data for the latter suggests a lift in both food manufacturing (largely due to a jump in livestock slaughtering) and underlying ‘core’ manufacturing volumes.
- Services sector activity (exp. +0.9% q/q) is expected to record reasonably broad-based growth at the industry level. Retail spending certainly ended the year on a stronger footing, in part due to a rebound in accommodation and food services, and wholesale trade also looks set to post decent growth. With housing market activity rebounding, the financial services, and rental, hiring and real estate services sectors should also post a lift in activity, while professional and administrative services should continue to record a solid run of growth. The one soft spot looks likely to be arts and recreational services activity, where activity is expected to ease in the quarter.
- Net exports (-1.0%pts) look set to be the major drag on the equivalent expenditure-based measure of GDP. However, that should be offset by respectable growth in private consumption, modest growth in residential investment, and a solid lift in other fixed asset investment. And after dragging on growth for the past three quarters (and in fact five of the past six quarters), inventories are also expected to make a positive contribution.
• **We turned a little more circumspect on the near-term growth picture last year.** This was on an expectation that a softer housing market, capacity pressures, credit headwinds and political uncertainty would act as modest headwinds. However, the recent flow of data has suggested that if there is to be a growth wobble, it is unlikely to be a large one – that’s encouraging in terms of what it suggests about the economy’s flexibility and resilience. The Q4 GDP figures are consistent with that reasonable picture.

• **In saying that, our longer-term views on the outlook have not changed.** The economy is late in the cycle and growth is off its 2015/16 highs. Firms are facing greater margin pressure. The low-hanging fruit growth-wise has already been picked and we need productivity growth to lift to maintain decent rates of activity growth from here, given that recent population and labour utilisation growth is unlikely to be maintained. At a time when house price growth is unlikely to race away again (or fall sharply, for that matter) we see households rebuilding precautionary saving, which will weigh on spending growth, all else equal. That message shouldn’t be confused with us being negative on the outlook from here. It’s just that we only see growth around trend for the next year or so, which is of course nothing to be scoffed at.

• **With regards to the Balance of Payments, we expect the seasonally adjusted current account deficit to widen modestly.** We have pencilled in a $1.7bn seasonally adjusted deficit, which is around $0.4bn larger than in Q3. While in absolute terms that should see the annual deficit grow a touch, it is not expected to be enough to see the deficit widen as a share of GDP, which we see holding steady at 2.6%.

• **The widening in the current account deficit in the quarter is largely on an expectation of the goods balance falling back into deficit in the quarter.** That is after it showed a positive a surplus (albeit small) in Q3 for the first time since Q2 2014. Despite the terms of trade reaching a new all-time high in Q4, strong import volume growth should weigh on the goods balance (notwithstanding that some of the strength in the partial import data will reflect the leasing of planes by Air NZ and is unlikely to be included in the GDP figures). Elsewhere, we are expecting both the services balance (at a surplus of $1.2bn) and the income deficit (at $2.4bn) to be broadly steady in the quarter.
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