GDP – 2018Q1

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COOLING GRADUALLY

BOTTOM LINE

- The economy grew 0.5% q/q in Q1, a respectable print, although the underlying details were weaker. Economic momentum continues to slow and we expect this will continue through the middle of the year. And in per capita term, the picture is weak. The economy is facing headwinds. That said, we don’t think the cycle is out in the cold just yet.
- The economy is growing a bit below trend and we expect it will struggle to achieve strong rates of growth from here. This is of relevance for the RBNZ. The outlook for core inflation is by no means assured; in the current climate interest rates will remain on hold for some time yet.

KEY POINTS

- The economy expanded by 0.5% q/q in Q1, in line with consensus expectations. This is a more modest pace of growth than the 0.6% pace recorded in Q4 and the strong rates of growth seen since 2014 (0.9% q/q on average). Annual growth moderated from 2.9% y/y to 2.7% y/y.
- Economic momentum continues to slow gradually, consistent with recent lackluster data flow. The underlying picture is weaker than the headline suggests. In per capita terms, GDP has stalled, at 0.0% q/q (0.6% y/y).
- On the production side, 13 of the 16 industries recorded stronger levels of activity. As expected, the services sector made the strongest contribution to growth, rising 0.6% with broad based gains across all 11 services industries. Primary industries partially recovered driven by increased milk production, increasing 0.6% after falling 2.6% in Q4. Goods-production was flat, with an increase in manufacturing offsetting a fall in construction activity.
- Expenditure GDP rose a more modest 0.3% q/q. As expected, net exports were a drag. Exports declined 0.1% while imports lifted 1.2%.
- Consumption was flat in the quarter (3.8% y/y), despite strong population growth. While this soft print follows strong growth (1.2%) in Q1, it is consistent with the moderation in household sentiment and spending growth in the year to date. Consumption has been growing consistently since September 2012, driven in part by strong population growth. But today we saw a fall in per capita terms. Government consumption increased 0.5% q/q.
- Gross fixed capital investment increased 0.7% q/q (3.9% y/y). Plant and machinery investment was up 2.1%, reaching annual growth of 13%. This more than offset declines in residential, non-residential and other construction. Investment can be volatile, but this is a respectable increase in the context of the challenges the economy is grappling with. It remains to be seen whether the moderation in business activity expectations and investment intentions flows through to investment in coming quarters. Inventories made a positive contribution to growth.
- Nominal GDP fell 0.4% q/q, but is running at 6.0% annually. Real gross national disposable income rose 0.1% q/q (3.4% y/y) pace.

DATA SUMMARY

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<th>Latest</th>
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<tr>
<td>Quarterly % change</td>
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<td>0.6%</td>
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<tr>
<td>Annual % change</td>
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• **Today’s outturn was a respectable print, but economic momentum continues to slow.** And in per capital terms the picture is weak. Businesses are facing credit and capacity constraints, along with policy uncertainty and margin pressure in the face of rising costs – and these headwinds are flowing through to activity. Encouragingly, businesses are investing. But consumption growth has moderated.

• **We don’t think the cycle is out in the cold just yet.** The economy is in the midst of headwinds, but it is also flexible and resilient. We are not seeing the sort of imbalances (especially external imbalances) that have often been the catalyst to tip the cycle over in the past. We expect that the economy will grow at or below trend over the next few years, supported by strong income growth (in large part a result of elevated export prices) and fiscal expansion.

• It is fair to say that downside risks to the outlook have increased a little of late. And with the economy expected to grow around trend, this is of particular relevance for the RBNZ. The outlook for core inflation is by no means assured and resource pressures look set to meander at current levels. We expect that inflation will emerge in time, but very gradually. We believe that the RBNZ will be looking to see a sustained increase in core inflation before an interest rate increase will be on the table. In the current climate, interest rates will remain on hold for some time yet.

**Figure 1. Production-based GDP**

[Graph showing production-based GDP over time, with labels for Quarterly % change and Annual % change]

**Figure 2. Production-based GDP components**

[Graph showing components of production-based GDP, with labels for Primary, Goods, and Services over time]

**Figure 3. GDP per capita**

[Graph showing GDP per capita over time, with labels for Quarterly growth in real GDP per capita, Annual growth in real GDP per capita, and Annual growth in real GDP]

**Figure 4. Contributions to quarterly growth in expenditure-based GDP**

[Bar chart showing contributions to quarterly growth in expenditure-based GDP for various components, with labels for Imports, Exports, Other investment, Residential investment, Change in inventories, Govt consumption, and Private consumption, and data for 2018Q1 and 2017Q4]
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