20 December 2018

GDP Wellbeing Back In Focus

- **Q3 GDP disappoints with 0.3% (2.6% y/y)**
- **As manufacturing and investment fall short**
- **And services expansion gets patchy**
- **Historical revisions soften the blow**
- **And we retain our 0.8% view on Q4 GDP**
- **But RBNZ dovish itches being scratched**

Gross Domestic Product (GDP) doesn't matter…until it does. And it did today, with its September quarter growth sagging to 0.3%, compared to market expectations of 0.6%. Upward revisions to recent history helped soften the blow. And the Q3 GDP details only shored up our view that Q4 GDP will expand solidly. However, the Q3 GDP outcome, patchy as it was, adds to other factors likely to nourish the Reserve Bank's dovish leanings.

Whenever key macro-economic data deviate markedly from expectations one of the first tasks is to understand whether it was a generalised phenomenon, or more a massive curve-ball from an isolated component. From delving into the Q3 GDP detail, it looked to be something in between. A number of components fell short of (our) expectations, but others proved (surprisingly) robust.

From the production side, the obvious undershoots (from our perspective) came from;

- a moderate fall in manufacturing output, as more than just food and beverage production eased, including textiles, transport and machinery equipment, and furniture
- a dip in construction. This was sheeted to a clear fall in infrastructure activity, noted by Statistics NZ as the unwind from Kaikoura's post-quake repair. Building work, however, expanded about as much as we thought
- a slower tone in the services sector as it became very up and down in its components. Major downs were seen in Transport, ICT, Administrative and Support Services, while one of the big ups was in Arts and Recreation.

From the expenditure side, there was slippage in plant and machinery investment to note, as well as a big correction in services exports, related to international tourism (as was foreshadowed in yesterday's Balance of payments). Public investment fell 1.1%. In sharp contrast,

GDP (Production) - 2018 Q3

	Actual	Mkt Expected	Nov MPS	Previous
s.a qtr % chg	**+0.3**	+0.6	+0.7	+1.0
qtr on qtr year ago %	**+2.6**	+2.8		+3.2R
annual average % chg	**+3.0**			+3.1

R - revised

private consumption expanded a better than expected 1.0%. As for inventory, it caused no big stir either way. Overall, real expenditure GDP expanded 0.5% in Q3, for annual growth of 2.7%.

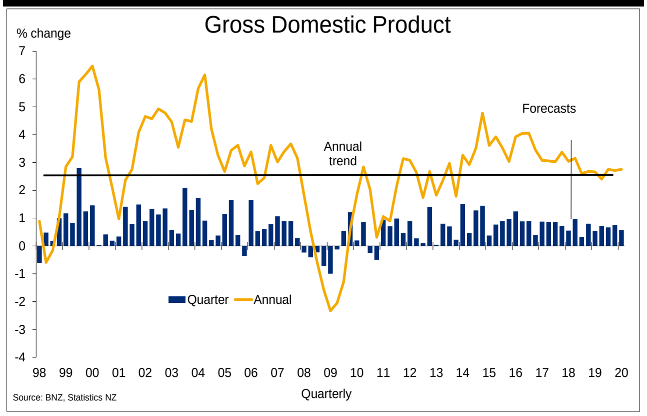
While the Q3 GDP details certainly threw us around a bit, on balance they seemed no cause to alter our view on Q4 growth. This stays at 0.8% (which would set annual growth at 2.7%).

It's also worth pointing out that the slowdown registered in Q3 GDP was coming off upgraded momentum from recent history. Not in Q2 growth, mind you. This remained at 1.0%. But the many quarters prior were each nudged up. This is why annual growth for Q2 2018 was revised up to 3.2% (from its initially reported 2.8%).

So even with the 0.3% undershoot in Q3 GDP the level came in very close to what we anticipated. With this, judgements on output gaps and the like shouldn't really change that much, if at all. For the record, ours haven't.

What about inferences about flattened per capita GDP growth? And negative productivity, recalling the big employment growth in Q3? We'd just repeat our view that these measures can be horribly volatile on a quarterly basis.

Seems Mostly A Timing Issue



Still, it does seem significant that Q3 GDP growth came in under the Reserve Bank's expectation of 0.7%. The saving grace is that the Bank didn't have such a strong benchmark for Q4 GDP, in 0.5%. However, for the meantime, today's GDP data can only nourish the Reserve Bank's reluctant tone on the OCR.

As such, it complements;

- a near-term CPI inflation story getting hammered by collapsing oil prices (potentially trimming general inflation expectations)
- global economic and financial market momentum fraying at the edges
- RBNZ proposals to increase bank capital requirements

This is not to suggest we see current monetary policy settings as entirely appropriate with the aim of sustainable economic growth and low inflation. However, we readily admit that the case for any increase in the OCR from this point will take a lot of time to get traction with the Reserve Bank, if at all.

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	qtr % chg prev qtr	% pt cont to chg (1)	ann avg % chg	ann % chg
GDP by Industry - September 2018 quarter				
Agriculture, Forestry & Fishing	0.8	0.0	1.5	2.1
Mining	12.4	0.1	0.8	-5.3
Manufacturing	-0.8	-0.1	0.5	0.3
Electricity Gas, Water & Waste Services	-2.3	-0.1	0.8	1.4
Construction	-0.8	0.0	2.4	-0.6
Wholesale Trade	1.1	0.1	5.0	5.2
Retail, Accom. & Restaurants	0.1	0.0	4.2	2.9
Transport, Postal and Warehousing	-0.1	0.0	5.3	4.1
Information Media & Telecommunications	-0.9	0.0	3.7	2.4
Financial and Insurance Services	0.7	0.0	3.7	3.1
Rental, Hiring, Real Estate Services	0.7	0.1	2.2	3.5
Prof, Scientific, Technical, Admin	0.6	0.1	4.5	3.8
Public Admin and Safety	0.6	0.0	3.8	3.8
Education & Training	0.2	0.0	1.3	0.9
Health Care and Social Assistance	0.9	0.1	3.3	2.5
Arts, Recreation and Other	0.7	0.0	1.7	3.0
Unallocated (2)	1.4	0.1	3.9	3.7
Balancing Terms (3)	..	-0.1	..	..
Gross Domestic Product	**0.3**	**0.3**	**3**	**2.6**

(1) Includes the change in inventories and the seasonal adjustment balancing item
(2) Includes unallocated taxes on production and imports, and bank service charge
(3) The seasonal adjutment balancing item

	qtr % chg prev qtr	% pt cont to chg (1)	ann avg % chg	ann % chg
Expenditure on GDP - September 2018 quarter				
Final Consumption Expenditure				
Private	1.0	0.6	3.4	3.3
General Government	-1.1	-0.2	2.2	0.5
Gross Fixed Capital Formation				
Residential Buildings	1.3	0.1	2.8	2.7
Other Fixed Assets	-2.1	-0.3	6.4	2.2
Exports of Good and Service	0.3	0.1	3.8	3.1
Imports of Goods and Services	-0.2	0.1	7.8	5.7
Change in Inv & Bal. Item (4)	..	0.2	..	..
Expenditure on GDP	**0.5**	**0.5**	**2.8**	**2.7**

(4) Includes the change in inventories and the seasonal adjustment balancing item.

Source: Statistics New Zealand

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