The beauty of hindsight
Revisions will boost the levels of NZ GDP and current account balance

- Statistics NZ has signalled a range of improvements to the measurement of GDP and the balance of payments.
- The net effect will be to portray the state of the New Zealand economy in a slightly more flattering light, with a higher level of GDP, a smaller current account deficit, and a better savings track record.
- The implications for the current economic cycle are less straightforward. While measured growth in recent years may have been stronger, the economy is probably no closer to its full capacity than we thought a week ago. Hence, the case for OCR hikes is unaffected.

Statistics NZ has recently flagged some sizeable revisions to the history of New Zealand’s national accounts, as part of its ongoing programme of quality improvements.1 While the full details won’t be published until next month, the indicative figures are significant enough to warrant bringing them to the market’s attention now.

The upshot will be a slightly more flattering picture of the state of the New Zealand economy compared to the previous record – a little wealthier, a more sustainable trade position, and a slightly better savings record. In particular, the revisions will change our understanding of how quickly the economy has powered out of recession in the last few years, with the post-earthquake rebuild a significant driver.

Although the revisions will present a stronger starting point for the economy, they shouldn’t have much bearing on forecasts of growth from here on. Nor do they present an argument for earlier OCR hikes, which is the interpretation that financial markets seem to be heading towards. While the economy may have grown faster over the last few years than previously thought, we’ve already observed how much inflation pressure was generated over that time – which is to say, not a lot. Instead, the implication seems to be that the economy’s non-inflationary potential has been similarly understated.

Details

The releases of the September quarter balance of payments (18 Dec) and GDP (19 Dec) will incorporate four major revisions to history. The first two will lead to an outright increase in the current level of GDP. The next two deal with changes in the composition of GDP, specifically the allocation between domestic and international spending. While these will have little or no impact on total GDP, they will lead to a net improvement in the balance of overseas trade.

We have to emphasise that the following figures are only indicative. Statistics NZ has given some guidance on the size of the four major revisions, but the final details will be included in the data releases next month, along with a

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1 The most recent update is available at www.stats.govt.nz/browse_for_stats/economic_indicators/NationalAccounts/improvements-gdp-dec2013.aspx
host of minor revisions and the annual updates of sectoral benchmarks for GDP (which will have an indeterminate impact on recent history).

**Construction:** The main indicator for construction GDP is a survey of building work completed, which is drawn from a sample of building consents. However, to date much of the quake-related building work in Canterbury has been repairs, which don’t require a new consent. As a result, quake-related activity appears to have been significantly undercounted.

Using industry data for the year to March 2012\(^2\) – the year following the February 2011 earthquake – Statistics NZ estimate that nationwide construction activity was 12% greater than previously reported. That equates to a 0.6 percentage point boost to total GDP growth over that period. Depending on the quarterly profile of when that boost occurred, it may end up lifting the growth rate over 2013 as well.

**Communications:** This is the most rapidly developing sector of the economy, clocking up average annual growth of almost 7% between 1991 and 2008. However, the current measurement approach has struggled to keep up with recent developments – indeed, until now the sector was reported as having been shrinking since 2010.

The new measurements take better account of the massive growth in broadband/mobile data use over the last few years, driven in part by a sharp drop in per-unit prices (which was already incorporated in the CPI). This restores the sector’s upward trend, with around 3% average annual growth since 2010, adding around 0.4ppts to annual GDP growth.

**Communications contribution to GDP**

![Communications contribution to GDP](image)

**Overseas visitor spending:** There are two measurement changes involved here. First, a new online survey of spending by overseas visitors has revealed a substantial undercount from the old survey method, which used face-to-face interviews. Second, a recent study has provided a new benchmark for international students’ living expenses.

The revisions mean that within total GDP, some spending that was attributed to New Zealanders (household consumption) will now be attributed to overseas visitors (exports of services), with no change in the total. However, the boost to services exports will narrow the current account deficit going back to 1988. We estimate that the improvement for the last year will be around $2.3bn ($1.6bn from tourists and $700m from students).

**Low-value imports:** Imports of goods valued at less than $1000, such as purchases from overseas online retailers, are a known source of under-coverage as they are not well monitored (for instance, items under $400 are not subject to GST). Statistics NZ will include an estimate of the value of these imports, dating back to 2000 (when they were seen as negligible) and reaching as high as $900m in the year to March 2013.

The net effect on GDP will be close to zero, as the increase in imports will be balanced out by an upward revision to household consumption. On its own this revision will worsen the current account balance, but as it’s smaller than the previous revision, the net change is still positive.

**Implications**

The net effect of the revisions will be to portray the state of the New Zealand economy in a slightly more flattering light. Compared to the previous record, the current level of GDP will be higher (by as much as 2%), the current account deficit will be smaller (though still large by the standards of advanced economies), and the reallocation of spending away from households and towards overseas visitors means that households’ saving record will improve.

It’s worth noting that these kinds of revisions are not out of the ordinary – Statistics NZ has made several improvements to the measurement of the national accounts over the last few years, largely in the same direction as these ones. Together, these have helped to address some of the data puzzles that we have long been highlighting, such as the implausibly low household savings rate through the 2000s (initially reported to be as low as -15%, later revised to more like -10%). However, we suspect there is still more to be done.

The implications for the current economic cycle are not so straightforward. It’s clear that the New Zealand economy has been growing faster than thought since the recession ended, and especially since the post-quake rebuild got under way. The previous figures showed that annual GDP growth had risen to a five-year high of 2.7% by June 2013; depending on how the final revisions pan out, it’s plausible that annual growth is actually running above 3% today, and that it has been for over a year.

However, from the RBNZ’s point of view, what matters is where the economy current stands relative to its non-inflationary potential, and it’s not at all obvious that these revisions change that story. We’ve already observed what inflation did in that time – falling below the 1-3% target band between mid-2012 and mid-2013, which strongly suggests

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\(^2\) This would have been incorporated next year anyway as part of the annual benchmarking process. But given its significance, Statistics NZ has included it a year earlier than usual.
that the economy was running below its potential, whatever
that may be.

The implications for financial markets are limited. We don’t
think this alters the case for OCR hikes, so there should be
no impact on swap rates. However, a smaller historic current
deficit and lower debt to GDP ratios (thanks to a larger
denominator) could warrant a small drop in government bond
yields and a slightly higher exchange rate.

Finally, we note that these revisions do not affect our
forecasts of the September quarter current account and GDP.
Our current account forecast is more or less complete – we
expect the deficit to widen by 0.3ppts, driven by a spike in
imports. Based on our estimate of the revised starting point,
this would see the deficit widen from 3.6% to 3.9% of GDP.
Last week we revised up our GDP growth forecast from 1.2%
to 1.4%, partly due to an improved estimate of the agricultural
sector’s post-drought rebound. This forecast is preliminary;
we’ll finalise it after the manufacturing and construction
surveys in early December, but we suspect the risks are more
to the upside.

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