

No alarms and no surprises

GDP rose 0.9% in Q4

- GDP rose by 0.9% in the December 2013 quarter, in line with market expectations.
- There were no dominant drivers or significant one-offs that might alter our general impression of where the economy is heading. New Zealand is in a fairly steady and broad-based growth phase at present.
- The outlook for monetary policy remains unchanged. With GDP growth consistently running above trend, higher interest rates will be needed to lean against the build-up of inflation pressures over the next couple of years.

Today's GDP report confirmed that the New Zealand economy was gathering a significant head of steam by the end of last year, with a broad range of sectors playing their part. There were no standout factors behind the 0.9% increase in the December quarter, in contrast to the agriculture-led 1.2% surge in the September quarter.

The outcome was right in line with our forecast and market expectations, and slightly ahead of the Reserve Bank's most recent published forecast. That means there's nothing in today's release to sway our expectation for another four OCR hikes this year. Moreover, there were no significant surprises or one-offs to suggest that the economy might have reached an inflection point. We expect GDP growth to maintain a similar pace over the next few quarters.

Key results

	Actual		Q4 expectations		
	Q3	Q4	Westpac	Mkt	RBNZ
GDP q/q	1.2	0.9	0.9	0.9	0.8
GDP ann % chg	3.3	3.1	3.0	3.1	3.0
GDP ann avg % chg	2.6	2.7	2.7	2.7	2.7

Details

Production GDP rose by 0.9% in the December 2013 quarter, following a 1.2% rise in the September quarter that was revised down from an initially reported 1.4%. There doesn't seem to be anything sinister in the revision – largely a softening of the scale of the massive post-drought rebound in agricultural output – and on an annual basis GDP growth was still much in line with forecasts.

As expected, the largest contributions to growth came from manufacturing and wholesale trade (though the latter should be thought of as more of a proxy for general economic activity than a driver of growth in itself). The 2.1% lift in manufacturing output included a 2.5% rise in food and beverage manufacturing and a 6.2% rise in machinery and transport equipment. Other notable contributions included a 1.3% rise in finance and insurance, a 1.1% rise in retail trade, a 1.0% rise in transport and warehousing, and a 1.3% rise in healthcare and social assistance.

There were a few small sectors with disproportionately large gains for the quarter. Mining rose by 9.5%, due to increased exploration activity (which tends to be sporadic in New Zealand). And electricity generation rose 3.8%, largely due to an increased share of higher value-added hydro generation.

The construction sector had a second slow quarter, eking out a 0.4% gain after a 1.3% drop in the September quarter. As previously reported, housing construction was flat and non-residential building fell 4.6%, but these were offset by a lift in infrastructure work. The recent softness in construction GDP seems odd given the prominence of the Christchurch rebuild, but it does come after a 29% lift in nationwide construction activity in the two years after the February 2011 earthquake. Building consents suggest that there is a significant amount of work still in the pipeline, and our view remains that this will translate into a higher level of activity over 2014.

Agricultural production was down 1.6%, following its massive post-drought rebound of 13.3% in the September quarter (revised down from 17% but still the biggest quarterly increase on record). The drought in early 2013 and the subsequent recovery have had a significant impact on the quarterly GDP figures over the last year, but with the combined impact of agricultural production and food processing close to zero for the December quarter, we think that the 0.9% rise in GDP is a fair reflection of the underlying pace of growth in the broader economy.

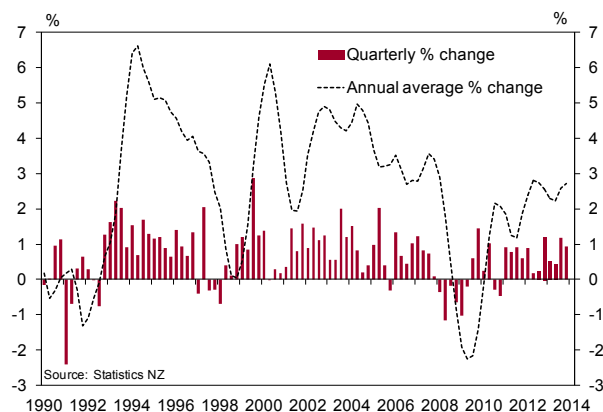
Implications

The GDP figures were bang in line with expectations, both in the headline and the detail, although financial markets appear to have caught on to the downward revision to the previous quarter. The New Zealand dollar dropped 20pts to 0.8540 and the two-year swap rate fell 3 basis points to 4.05% after the release.

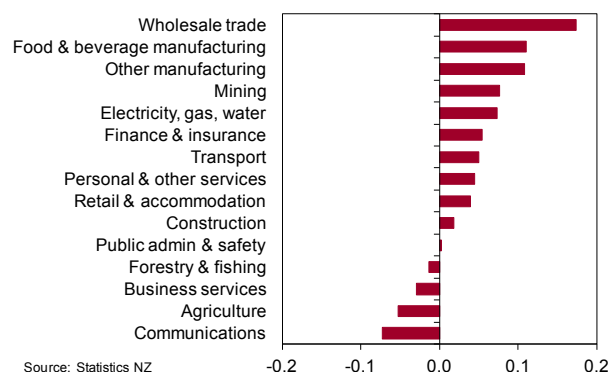
Today's figures offer no reason to alter our impression of where the New Zealand economy is heading. We are in a pervasive economic upswing owing to the Canterbury rebuild, construction activity in Auckland, consumer buoyancy following house price increases, and a four-decade high in the terms of trade. Consequently, the RBNZ will need to gradually increase interest rates over the course of the year. As interest rates rise, we suspect that the housing market will slow, consumer buoyancy will gradually diminish, and eventually, GDP growth will slow. But this is a process that could take years.

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Production-based GDP



Percentage point contribution to Q4 GDP growth



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