WESTPAC ECONOMIC BULLETIN

GDP review, June quarter 2023.

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Here today, gone tomorrow?

- GDP rebounded by 0.9% in the June quarter, just 0.1ppt above our forecast but well above market and RBNZ forecasts. Growth in the prior two quarters was also revised up slightly.
- Annual growth in GDP slowed to 1.8% from 2.2% previously. We think this better reflects the underlying trend, but this slowdown is less than the RBNZ had expected.
- The level of output in the June quarter was 0.5% larger than assumed by the RBNZ in the August MPS. This suggests more pressure on resources than the RBNZ has been estimating.
- While there are several important data releases ahead, today's news supports our view that the RBNZ will most likely be compelled to tighten policy further later this year.

Key results	Jun 23	Mar 23	Westpac f/c	RBNZ f/c
GDP qtr %	**0.9**	0.0	0.8	0.5
GDP ann %	**1.8**	2.2	1.5	1.2

Key results.

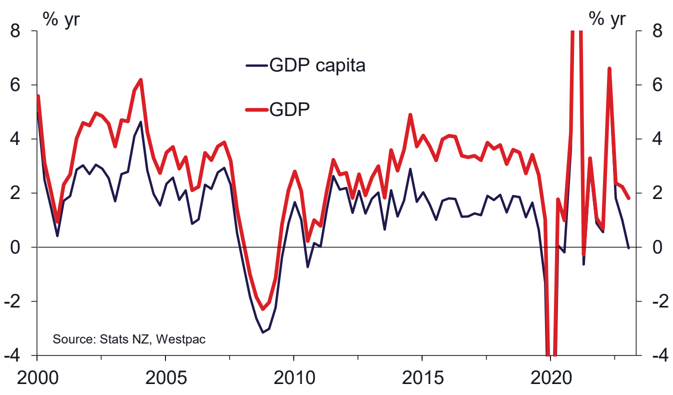
As widely anticipated, New Zealand's GDP rebounded in the June quarter. Indeed, Statistics NZ reported a sturdy 0.9% lift in production – an outcome that was well above the market forecast of 0.4% and the Reserve Bank's most recent forecast of 0.5%. However, it was just 0.1ppts firmer than Westpac's top of the market estimate of 0.8%.

Adding to today's surprise were small upward revisions to prior quarters, with the recent December and March quarters revised to -0.5% and 0.0% respectively from -0.7% and -0.1% previously. In other words, the previously reported "technical" recession has been revised away (at least at one decimal place – the economy contracted 0.01% in the March quarter). As a result, annual growth in the year through to June stands at 1.8%, which is 0.6ppts above the RBNZ's most recent forecast.

Interpretation and implications for the RBNZ.

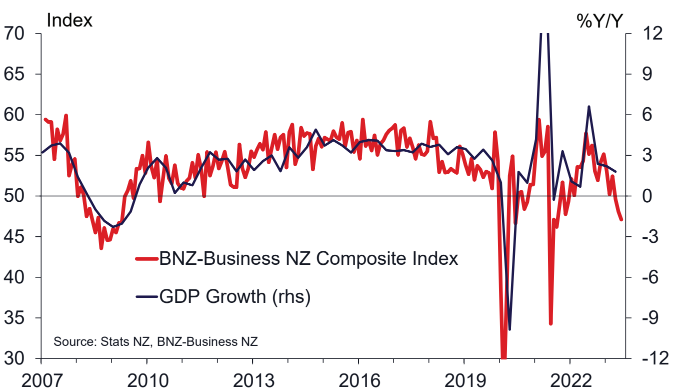
New Zealand's GDP data can be volatile at the best of times – even more so given the lingering impact of the pandemic and this year's storms – and so we would be loath to extrapolate today's outcome. As we wrote in our preview note, at present we think that the underlying trend is best represented by developments in annual growth. On that score, momentum in the economy is slowing with annual growth of 1.8% in the year to June down from the 2.2% growth recorded in the year to March. This is a below trend pace of growth, as reflected in the gradual increase in the unemployment rate over the past year. While rapid population growth is supporting demand, it is also helping to boost the economy's productive capacity. And over the past year there has been no growth in GDP in per capita terms, which helps to explain why consumer and business confidence remains in the doldrums – growth is not lifting the real incomes of New Zealand's residents. Indeed, real national disposable income per capita has declined 0.8% over the past year.

GDP growth



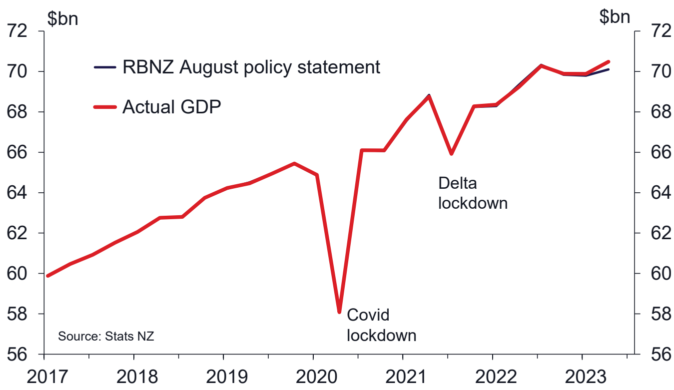
Looking ahead, with past monetary policy tightening steadily gaining traction as mortgages are refinanced, and low commodity prices now weighing on rural incomes, we expect the economy will continue to flirt with recession. Indeed, the BNZ-Business NZ PMIs suggest that the economy may already be contracting in the September quarter, and annual growth in the year to September is likely to be close to nil. As a result, we expect that the unemployment rate will remain on an upward trajectory, contributing to a gradual easing of inflation pressures.

Real GDP and Composite Index



However, especially after today's release, it remains to be seen whether inflation pressures will dissipate quickly enough to satisfy the RBNZ. After allowing for cumulative revisions, the overall size of the economy in the June quarter is 0.5% larger than the RBNZ had estimated in the August MPS. A portion of that forecast error will likely feed into the RBNZ's estimate of the output gap, at the margin lifting the Bank's estimate of the degree of inflation pressure sitting in the economy during that quarter. All else equal, this will place upward pressure on the RBNZ's inflation forecasts.

Level of quarterly GDP



Given the ongoing uncertainty surrounding these figures – including the likelihood of future revisions – we think that the RBNZ will also choose to draw inference from a wider array of economic indicators in assessing how excess demand and inflation pressures are evolving, including developments in the labour market. **Even so, today's data clearly supports our view that the RBNZ will be compelled to tighten further later this year.** That said, there are a number of important indicators ahead that will have at least as great a say on whether further policy tightening is judged to be necessary. In the near-term, attention will now turn to the various cost and pricing indicators in next month's QSBO business survey and in the September quarter CPI report. The September quarter labour market report – released in early November – will also be important in determining whether the RBNZ lifts the OCR at the November MPS meeting. And the fiscal strategy of the incoming government following the 14 October General Election will also factor into the RBNZ's deliberations, together with developments in the international economy.

For the record, we don't view today's news as likely to be sufficient to bring about a tightening at the RBNZ's next meeting on 4 October. However, it could be enough to cause the RBNZ to put the market on clear notice that the November meeting is very much "live" with the outcome to depend on whether upcoming data provides the Bank with any further unpleasant surprises.

Details.

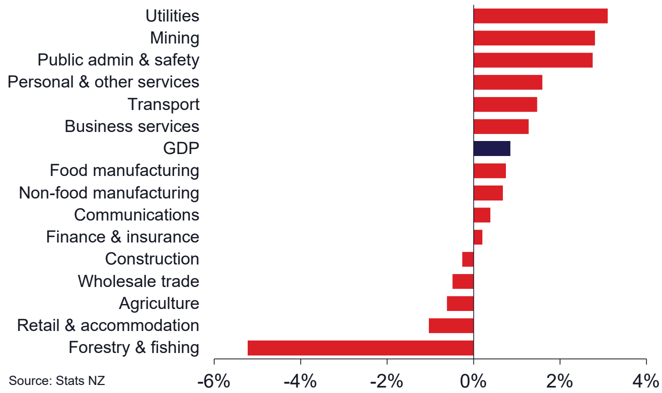
The industry detail of today's GDP report was broadly in line with what had been signalled by the various partial indicators released in recent weeks.

As we had expected growth was driven by the services industry, with activity rising 1% during the quarter. Especially strong growth was recorded in the utility sector (3.0%), public administration and safety sector (+2.8%) and business services sector (+2.1%). The transport and storage sector also reported strong growth this quarter. The education and training sector rebounded a little more than we had expected considering ongoing strike action during the quarter, pointing to solid underlying growth (education services clearly benefitting from strong migrant inflows).

On the negative side, as expected growth was weighed down by lower activity in the retail trade and accommodation (-1.0%) and wholesale trade (-0.5%) and sectors. With the impact of earlier storms leading to a further near 8% decline in output in the horticulture industry, output fell 0.6% in the agriculture sector despite a sharp lift in output in the dairy sector. This quarter there were also declines in output in the forestry and fishing sector and construction sector.

The expenditure-based measure of GDP, which is a slightly more volatile measure of activity, increased 1.3% in the June quarter and 1.9% in the year to June. This measure indicated a strong rebound in exports and strong growth in business investment and government consumption spending.

Q2 GDP quarterly change by industry



Source: Stats NZ

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