ANZ Research

Preview: NZ GDP and Balance of Payments – Q2 2024

11 September 2024

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Contact

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Data summary

	Q1 2024	ANZ Q2 2024 exp
GDP		
Quarterly % change	0.2%	-0.1%
Annual % change	0.3%	-0.3%
Annual average % change	0.2%	-0.2%
Balance of Payments		
Current account ($m, actual)	-4359	-3857
Current account ($m, sa)	-7286	-6898
Annual CAB ($bn)	-27.6	-27.2
% of GDP	-6.8%	-6.6%

How bad was it?

Bottom line

- We expect the New Zealand economy contracted 0.1% q/q (-0.3% y/y) in Q2 (previously -0.3% q/q). While our forecast is well above the RBNZ's August MPS forecast of -0.5% q/q (-0.7% y/y), it's certainly not strong in any sense of the word.
- There's plenty of uncertainty surrounding our GDP forecast, with two-sided risks. However, overall, we don't expect the Q2 GDP data to be a game-changer for the monetary policy outlook. Even in the case of an upward surprise, economic momentum is likely to still be soft enough to be consistent with rising spare capacity and falling inflation. On the other side, a material downward surprise would need to be weighed against a rapidly shifting outlook now that interest rates are falling. And as always, substantial volatility in the GDP data warrants caution when interpreting what it all means for momentum moving forward.
- The annual current account deficit is expected to narrow 0.2%pts to 6.6% of GDP. We can't forecast revisions, but historical revisions to travel services exports could be worth around 0.3%pts off the annual current account deficit and the risks are skewed to a narrower deficit than forecast. Nonetheless, the deficit would still be a fair distance from sustainable levels.

The big picture

New Zealand's Q2 Balance of Payments and GDP figures will be released at 10:45am next Wednesday and Thursday respectively.

More than usual, these data feel like ancient history given the RBNZ has now kicked off OCR cuts, and the focus has shifted to how responsive the economy will be to lower interest rates. Nonetheless, the Q2 data will be important for gauging how much of an impact past monetary tightening has had on the real economy. After all, it was a meaningful deterioration in high-frequency activity indicators that drove the RBNZ to bring forward OCR cuts by 12 months. Now we'll get to see if the "low-frequency" data followed suit.

The broad deterioration in monthly activity indicators over Q2 suggested that traction from monetary tightening had accelerated and the economy was heading for a deeper slowdown. However, we were cautious about taking the full signal from these data at the time because of the inherent volatility and lack of a clear catalyst for such abrupt weakness. While some of these indicators suggest a much weaker Q2 GDP print than our updated forecast of -0.1% q/q, the subsequent partial industry-level data released over the past fortnight, which underpins our Q2 forecast, hasn't corroborated the extent of weakness implied by these earlier indicators.

That said, things are certainly weak, and that isn't surprising. Other drivers of economic momentum have become increasingly synchronised to the downside:

- fiscal settings are becoming less expansionary;
- population growth has slowed as the net migration cycle turns rapidly;

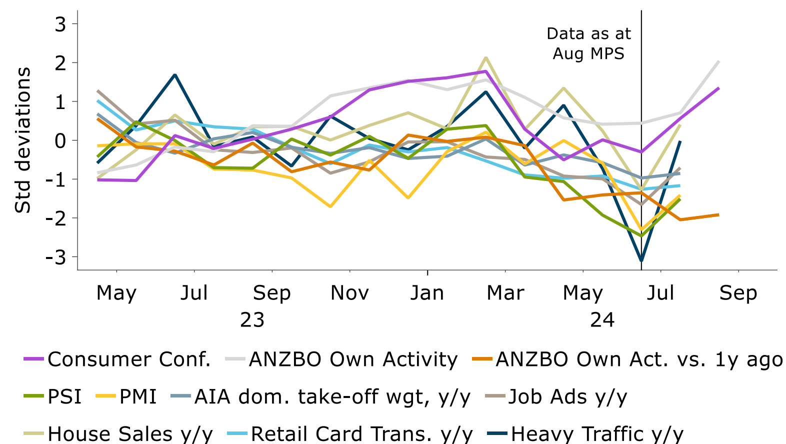
- house prices have been in decline since May; and
- business and consumer confidence has been very weak.

But the suddenness of the deterioration was a little more unexpected. The August MPS Summary Record of Meeting stated that Monetary Policy Committee members "were also concerned about avoiding unnecessary near-term instability in output and employment given the evolution of recent indicators." With greater confidence in the inflation outlook, the Committee appears to have become more sensitive to downside growth risks.

Financial markets are focused on these risks, pricing in a much faster pace of easing than we are forecasting in the near term, with a probability of around 40% attributed to a 50bp cut in October. In our view the chance of a 50bp cut as soon as October is low. It seems likely that such a shift in the RBNZ's view would require a materially weaker Q2 GDP print than was expected in August, but our updated GDP forecast implies the opposite. That said, given the volatility in the GDP data currently, a much weaker outturn certainly can't be ruled out.

While these data reveal the starting point for the economy, the economic landscape has changed since then. With the RBNZ kicking off OCR cuts, the impacts of the significant easing in monetary conditions are already emerging in high-frequency data. The same high-frequency indicators that drove the significant downgrade in the RBNZ's growth outlook have generally bounced from the depths they reached in June. Our own consumer and business confidence surveys have bounced sharply. The RBNZ will need to weigh the historical weakness revealed in the Q2 data against a different outlook moving forward. Data over coming months will make the picture much clearer and will ultimately determine the pace and extent of easing.

Figure 1. Selected high-frequency activity indicators



Source: Stats NZ, BusinessNZ, AIA, REINZ, Seek NZ, Macrobond, ANZ Research

The details

Turning to the details of the GDP release, key partial indicators have been mixed:

- **Retail trade** contracted 1.2% q/q, continuing its downward slide. Looking ahead, the prospects look brighter, with interest rates falling and tax cuts likely to provide a boost from Q3.
- The volume of building work put in place fell 0.2% q/q, with small declines in both residential and non-residential activity.

- The quarterly **manufacturing** survey showed volumes lifted 0.6% q/q.
- After adjusting for price changes, **wholesale trade** appears to have contracted around 2% q/q.

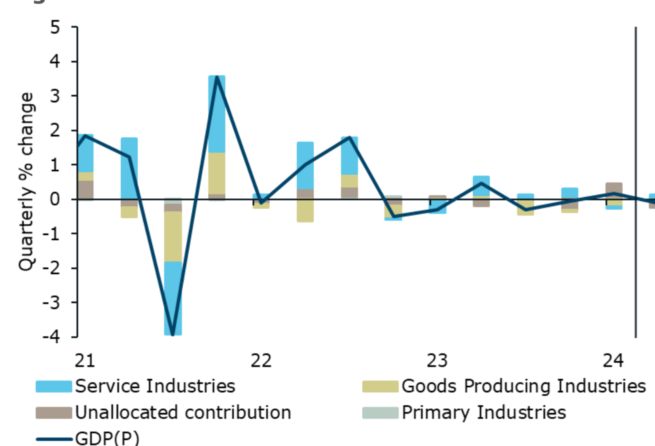
Table 1 shows our industry-level forecasts. Overall, our expectation that the economy contracted 0.1% in Q2 is driven by:

- **Services industries** (around two thirds of GDP) expanding 0.1% q/q (making a 0.1%pt contribution to headline growth).
- **Goods-producing industries** expanding 0.2% q/q (making a 0.0% contribution to headline growth).
- **Primary industries** contracting 0.8% q/q (making a 0.0%pt contribution to headline growth).
- The **unallocated tax component** and **balancing item** contribute the remaining roughly -0.2%pts to headline growth.

Table 1. ANZ Q1 GDP industry-level forecast

Industry	q/q%	%pt cont.	y/y%
Agriculture, forestry, and fishing	-0.7	-0.04	1.2
Mining	-1.5	-0.01	-8.4
Manufacturing	0.5	0.04	-4.6
Electricity, gas, water, and waste services	-1.2	-0.03	-0.5
Construction	0.3	0.02	-3.6
Wholesale trade	-2.1	-0.11	-6.4
Retail trade and accommodation	-0.9	-0.06	-1.9
Transport, postal, and warehousing	-0.2	-0.01	-3.5
Information media and telecommunications	0.5	0.02	1.6
Financial and insurance services	0.3	0.02	-0.1
Rental, hiring, and real estate services	0.4	0.06	3.8
Prof, scientific, technical, admin, and support	0.6	0.07	-0.7
Public administration and safety	0.5	0.02	2.6
Education and training	0.1	0.00	2.0
Health care and social assistance	0.8	0.05	3.6
Arts, recreation, and other services	0.8	0.03	1.1
Unallocated	-0.6	-0.05	-0.6
Balancing item	N/A	-0.14	N/A
Gross domestic product	**-0.1**	**-0.1**	**-0.3**

Figure 2. Production GDP forecast



Source: Statistics NZ, ANZ Research

Regarding the expenditure cut of GDP, we've pencilled in a -0.3% q/q contraction. Broadly we expect a contraction in domestic demand to be partially offset by positive contributions from net exports and change in inventories. That said, COVID-related disruption and subsequent changes in seasonal patterns have generated significant volatility in the measure of travel services exports, which has impacted private consumption. We would advise caution when interpreting the quarterly movements in these components, given this volatility. Stats NZ have advised that these components will be revised in the Q2 release. We'll assess these changes following the release next week.

Turning to the Balance of Payments, we expect the annual current account deficit narrowed from 6.8% of GDP in Q1 to 6.6%. Trade data released for Q2 suggest both the annual goods and services deficits will narrow a touch. Meanwhile, the income deficit, which is always the harder part to forecast given limited indicators, is expected to remain broadly unchanged. Stats NZ has advised that changes to the measurement of travel services exports over history will result in a narrower-than-otherwise current account deficit in Q2. Revisions to services exports across the past three quarters could be worth around 0.3%pts off the annual current account deficit. We can't forecast revisions, but the risks are skewed to a narrower current account deficit on the day.

Monetary policy implications

All up, we're not expecting the Q2 GDP data to be a game-changer for the monetary policy outlook. There is plenty of scope for a surprise on the day, in either direction, but there are many reasons to be cautious about overinterpreting a forecast miss:

- In the case of an upward surprise, it's important to remember that the RBNZ's potential output assumption (the economy's growth speed limit before generating inflation) is 0.6% q/q. That means growth anywhere below this threshold is likely to be interpreted as consistent with rising spare capacity across the economy and ongoing disinflation.
- In the case of a downward surprise, it will need to pass the volatility sniff test and be weighed against emerging signs that some parts of the economy are already responding to lower interest rates. Broad-based weakness across services industries would be an important signal in this context; it would be more meaningful than an undershoot driven by the more volatile goods components, for example. We view the risk that a downward surprise crosses the materiality threshold as low.

Volatility in the activity data is unlikely to go away any time soon. Just as the deterioration in high-frequency indicators in Q2 looks to have overstated the extent of weakness in the economy, the subsequent rebound following the easing in monetary conditions may also overstate the extent of the economic recovery. We expect the RBNZ will stick to the current course of action for the time being, delivering a steady stream of 25bp cuts at each meeting, allowing time to assess the economy's response. Risks to the pace of the easing cycle certainly remain two-sided. The broad evolution of data over the coming months will be key for assessing the skew of those risks, rather than one print alone.

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