It's the most wonderful time of the year

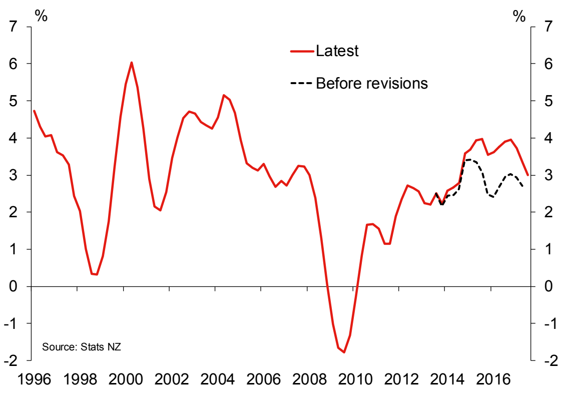
NZ GDP, September quarter 2017

21 December 2017

- Annual revisions to the GDP figures reveal that economic growth has been substantially stronger than thought in recent years.
- The revised figures help to solve some recent puzzles such as New Zealand's poor productivity performance.
- However, they shed less light on why inflation has been so subdued in the face of strong growth.

Key Results	Jun 2017	Sep 2017	Westpac f/c	Market f/c
GDP Q/Q %	1.0	**0.6**	0.4	0.6
GDP Ann %	2.8	**2.7**	2.2	2.4
GDP Ann Avg %	3.3	**3.0**	2.4	-

Annual Average GDP growth



September quarter GDP was stronger than we expected, but that was almost an incidental detail in today's release. Stats NZ's annual benchmarking of the national accounts has led to some major upward revisions to the reported rate of growth over the last few years.

The clear outcome is that the New Zealand economy is larger and more productive than the previous figures portrayed. It's less obvious, though, whether the economy is running closer to full capacity than previously thought, since we know that inflation was very subdued over the period of revisions. We'll spend some more time chewing through the implications when we return next year.

Annual revisions

For each September quarter release, Stats NZ revises the recent history of GDP to incorporate better-quality data that is available on an annual basis only, often with a substantial lag. There is no systematic pattern to the revisions; GDP is revised up in some years and down in others. This time, process improvements mean that Stats NZ has been able to include two years' worth of annual benchmarks instead of the usual one, so the size and extent of the revisions was greater than usual this time.

Stats NZ had previously indicated the scale of the revisions, at least as expressed in terms of the level of expenditure GDP, in nominal terms. What we didn't know was how this would translate into the preferred production measure of GDP, in real (inflation-adjusted) terms. The revisions proved to be even greater than we were anticipating: for instance, GDP in the June 2017 quarter is now 2.7% higher than previously reported.

The revised figures tell a substantially different tale of the New Zealand economy's recent performance. The previous figures suggested that annual GDP growth had been steady at around 2.5-3.0% over the last few years – at a time when population growth, led by net migration, had accelerated sharply. As a result, per-capita GDP growth appeared to have slowed significantly, from just under 2% in 2014 to near zero today.

The new figures show instead that GDP growth has, for the most part, accelerated along with population growth. GDP growth is now estimated to have peaked at 4% in the 2016 calendar year, when population growth was a little over 2%.

Per-capita growth is now more consistent at just under 2% over recent years.

The GDP figures still point to a slowdown in the rate of growth in 2017 – though we note that this year's figures have yet to be subjected to the annual benchmarking process. We'll continue to treat this slowdown as genuine, as it has been corroborated by other evidence.

The revised figures help to resolve some puzzles about the economy's recent performance. For instance, modest GDP growth at a time of strong employment growth left us with a dismal picture of labour productivity in recent years. The revised picture is more encouraging.

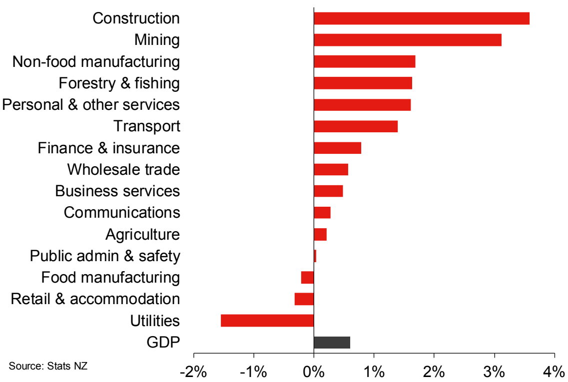
Some other puzzles remain, however. We already know that inflation was persistently below 2% between 2012 and 2016, a time when the economy now appears to have been growing at a strong clip (even after accounting for population growth). Should we then treat these GDP revisions as a sign that the economy's potential growth has been higher than thought? To a large degree yes, but we can't rule out the possibility that strong growth has brought the economy closer to full capacity than we thought. We'll be interested to see the interpretation that the Reserve Bank takes at its next Monetary Policy Statement in February.

September quarter GDP

GDP rose 0.6% in the September quarter, in line with the median market forecast but ahead of our forecast of a 0.4% rise. Growth was also revised up in each of the two previous quarters of this year.

Construction made the biggest contribution to growth in the September quarter. Output rose by 3.6%, reversing the decline seen over the first half of this year that may have been due to wet weather delaying activity. There were also surprisingly strong gains in transport (+1.4%) and mining (+3.2%). Agricultural output was about flat, as a drop in milk production was offset by gains in cattle farming. Retail spending was up, but accommodation and hospitality was down, as tourist numbers dropped back after the Lions rugby tour in June. Electricity demand was down due to a warmer than usual winter and spring.

Q3 GDP changes by sector



Our view remains that the September quarter will mark the low point for growth in 2017. Many of the factors that held back growth – in dairying, tourism and electricity generation – were temporary, and the indicators to date for the December quarter have been significantly stronger.

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