Westpac

Institutional Bank

17 September 2015

Meek rebound

GDP rose 0.4% in Q2

- GDP rose by 0.4% in the June quarter, again falling short of market forecasts.
- As expected, agriculture, mining and electricity rebounded from their March quarter weakness.
- Nevertheless, growth remained sluggish over the first half of this year.
- Further interest rate cuts by the Reserve Bank are likely, although whether the next move comes as soon as October is uncertain.

Key results

	Actual	Previous	Q2 forecasts	
	Q2	Q1	Westpac	Market
GDP q/q	0.4	0.2	0.7	0.6
GDP ann % chg	2.4	2.6	2.6	2.5
GDP ann avg % chg	3.0	3.2	3.0	-

The New Zealand economy grew by just 0.4% in the June quarter, less than the 0.6% that was predicted by the market, the Treasury and the Reserve Bank (and even further from the 0.7% rise that we expected). The annual growth rate slowed to 2.4%, compared to a 3.5% pace at the end of last year.

It's hard to give a satisfactory answer as to why growth fell short of expectations. There was no particular sector that accounted for the miss or that seemed to be dragged down by one-off factors. In fact, in some respects this was meant to be a 'rebound' quarter, following the surprisingly weak 0.2% rise in March quarter GDP. This second soft outturn shows that the underlying trend was genuinely sluggish over the first half of this year.

Today's report leaves us confident that the Reserve Bank will need to cut the OCR further, and by more than it is currently projecting. However, the timing of the next move is still up in the air. Weak GDP growth leans in favour of an October OCR cut, but more recent activity data has been stronger and dairy export prices have bounced from their lows, which would favour a pause in October. Tomorrow's interest rate decision by the US Federal Reserve (more precisely, its impact on the New Zealand dollar) could prove to be the deciding factor.

Details

As we expected, the biggest gains in the June quarter were in those sectors that had been temporarily depressed in the March quarter. Agriculture and food manufacturing rebounded from the dry summer, led by a 10% rise in milk production in seasonally adjusted terms. Oil extraction jumped after a temporary shutdown for new drilling, although the overall rise in the mining sector was smaller than we expected due to declining coal production. And electricity generation benefited from fuller hydro lakes.

We were also pleased to see strong growth in telecommunications – perhaps belatedly reflecting the surge in the use of streaming services that was reported in the March quarter but failed to make an impact on the GDP figures.

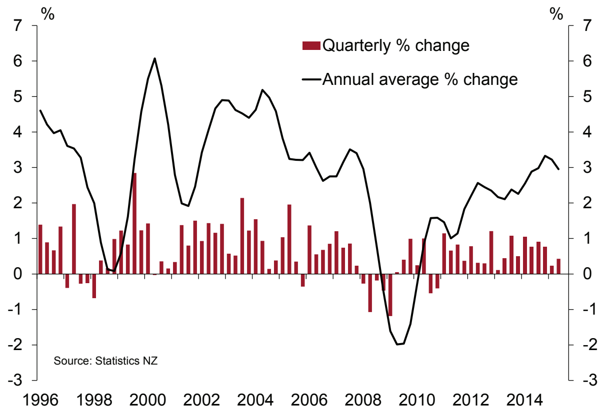
The construction sector continued to provide moderate support to growth, although the 0.8% rise was less than we expected due to a fall in infrastructure work. Professional, scientific and technical services recorded solid growth, as did finance and real estate as the housing market gathered steam.

On the negative side, there were declines in wholesale trade, most non-food manufacturing industries, and a sharp 1.8% drop in transport and warehousing (though that followed a 2.4% jump in the previous quarter). Accommodation and hospitality fell by 1.6% despite the continued strong growth in tourist spending.

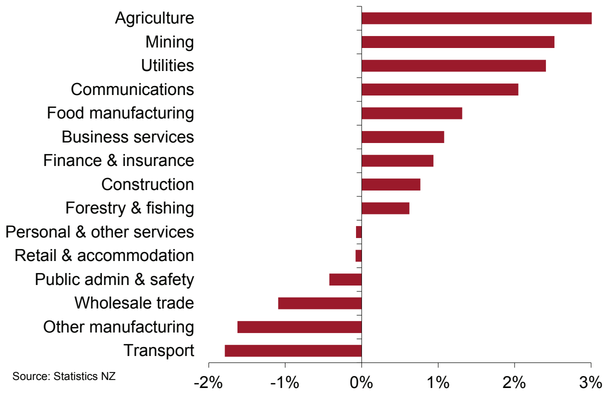
The expenditure measure of GDP was even softer than the production measure, rising just 0.2% in the June quarter on top of a 0.3% rise in March. On a positive note, investment in plant and machinery rebounded from its 10% plunge last quarter, and household consumption was stronger than we expected, led by a 0.9% lift in services. A weak international trade position (exports down 1.1%, imports up 2.3% by volume) was the main drag on this GDP measure.

Michael Gordon
Senior Economist

Production-based GDP growth



Q2 GDP growth by sector



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