# WESTPAC ECONOMIC BULLETIN

## GDP review, September quarter 2022.

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# Travel broadens the mind... and the economy.

- GDP rose by 2% in the September quarter, well ahead of what the market and the Reserve Bank expected.
- The reopening of the border and the return of overseas tourists has provided a fresh boost to demand, even more so than we had factored in.
- Indeed, the strength of activity in travel-related sectors is difficult to interpret, given that visitor numbers are only halfway back to pre-Covid levels.
- But at face value, today's results will further stoke the Reserve Bank's concerns about an overheating economy, supporting the case for further interest rate hikes.

| Key results | Sep 22 | Jun 22 | Westpac f/c | RBNZ f/c |
|---|---|---|---|---|
| GDP qtr % | **2.0** | 1.9 | 0.9 | 0.8 |
| GDP ann % | **6.4** | 0.3 | 5.5 | 5.4 |
| GDP ann avg % | **2.7** | 1.1 | 2.5 | 2.5 |

The New Zealand economy surged forward again with a 2% lift in GDP in the September quarter. That was well ahead of the respectable 0.9% rise that we and the market were expecting, and the 0.8% increase that the Reserve Bank had forecast in its November *Monetary Policy Statement*.

GDP is now around 8% above where it was at the end of 2019, before the shock of Covid. Half of this has come in the last two quarters alone, as the return of international tourists has boosted activity to a surprising degree – even more than the already-strong allowance that we'd made in our forecasts.

To be clear, the strength in the September quarter wasn't entirely about tourism. There were solid gains across a range of personal and business services, including professional services (up 2.1%), information and communications (up 2.6%) and wholesale trade (up 0.9%). The electricity sector saw a 2.9% lift, as full hydro lakes boosted higher-value renewables generation.

There was also a strong 5.1% lift in construction activity, with gains across homebuilding, commercial construction and infrastructure work. The rising costs of labour, materials and finance are undoubtedly putting pressure on this sector, but the pipeline of consented work remains very strong for now.

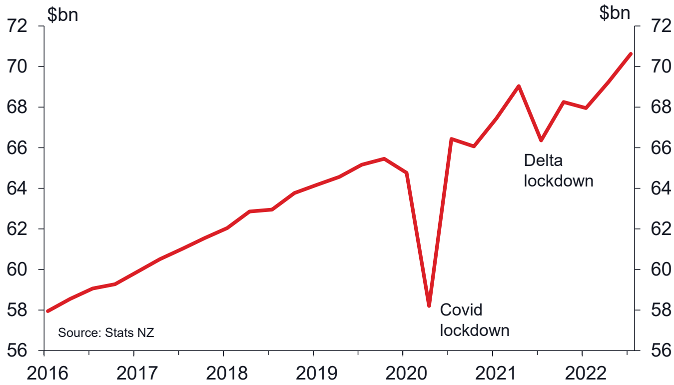
The stars of the quarter, though, were the travel-related sectors. Transport was up by a whopping 9.7%, providing both the single biggest contribution to GDP growth and the biggest miss on our forecast. Administrative services, a group that includes travel agencies, was up 7%, and arts and recreational services were up 2.8%. Accommodation recorded a small decline, but that followed a 30% jump last quarter – and the usual seasonal patterns in this sector may have been disrupted.

Indeed, the strength in these sectors is providing a real challenge in terms of how to read the state of the economy. In GDP terms, all of them are now running above their pre-Covid highs – at a time when overseas visitors were still only half of what they used to be. This raises a number of possible answers:

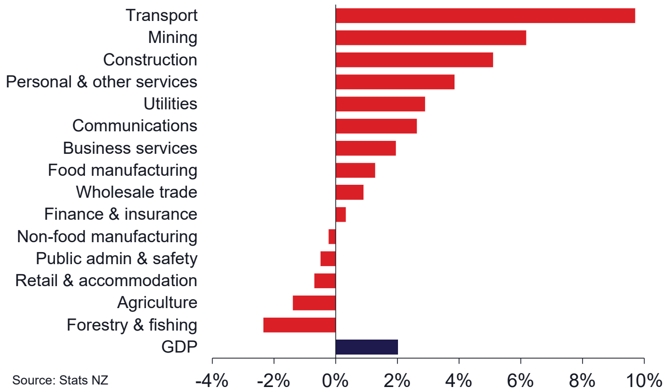
- Perhaps domestic tourism is running so hot that it is more than outweighing the shortfall in overseas visitors. If so, we wouldn't expect it to endure for much longer, as households with mortgages increasingly feel the pinch of higher interest rates in the coming months. This story seems unlikely though – for instance we know that the number of domestic flights is still running below pre-Covid levels as well. The capacity just isn't there yet.
- So perhaps it's due to mismeasurement – maybe Stats NZ has failed to appreciate the extent of the rise in prices, and is capturing it as growth in volumes instead. If so, will today's figures survive future data revisions? And what would happen if the Reserve Bank ratcheted up interest rates, only to find out later that the economy hadn't been running as hot as thought?
- Or perhaps overseas tourists have genuinely boosted the economy in this way, in which case we can expect more strong gains in GDP to come. That would complicate the Reserve Bank's efforts to engineer a slowdown in order to bring inflation under control. To be fair, the RBNZ has anticipated this to a degree – its predictions of an engineered recession don't kick in until the middle part of next year, with some solid growth in GDP expected until then.

Either way, there will be much for the market and the RBNZ to ponder over the Christmas break. Our forecast is for another 75 basis point rise in the Official Cash Rate at the next review in February, and the RBNZ's projections suggest that it has the same idea in mind. Today's result certainly won't make them inclined towards slowing down the pace of rate hikes, in the way that some of their overseas peers are now looking at.

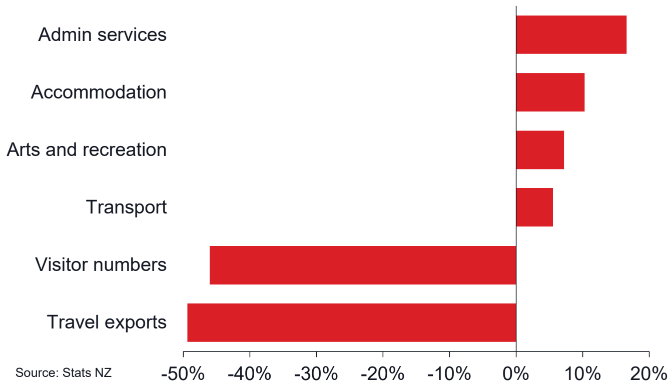
**Level of quarterly GDP**




**Q3 GDP growth by production**




**Travel-related activity vs pre-Covid levels**



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